RETAIL IQ

ANALYTICS-POWERED PRICING IN THE OMNICHANNEL AGE

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Maturity Ladder:

Analytics Powered Pricing

The *RIS News* Retail IQ Report Maturity Ladder is a diagnostic measurement tool for a retailer's state of technology advancement in a specific category. There are four key phases: **1. Basic** – minimal capabilities, **2. Intermediate** – mostly basic with some advanced capabilities, **3. Advanced** – mostly advanced capabilities with some limitations, and **4. State-of-the-Art** – comprehensive capabilities are fully integrated and up to date. Note that it is possible to be on more than one step of the ladder simultaneously as specific technology components and processes are upgraded in phases.

04

4. STATE-OF-THE-ART

- Using predictive analytics, retailers adopt price optimization solutions to delve into inventory levels, their brand's unique product and sales dynamics, and then apply these insights to determine different shoppers' levels of price sensitivity and elasticity.
- Retailers account for customer value propositions, channel activity, competitor prices and assortments, category trends, private brands, and other factors. Armed with this data, retailers base pricing decisions with full visibility of the omnichannel marketplace.
- New players still continue to up the ante, including those that take on a "club" retailing model that is supported by a collaborative pricing strategy.

03

3. ADVANCED

- Retailers automate manual processes so they can transition to more sophisticated pricing strategies.
- Retailers adopt more advanced analytics tools so they can make more informed, competitive pricing decisions.
- Pricing optimization tools make their way into the hands of pricing managers, and retailers begin to make pricing decisions from a customer-centric point-of-view versus a product-centric perspective.

02

2. INTERMEDIATE

- As retailers begin to expand omnichannel operations with store-level digital touch points, retailers are inundated with customer-specific, informational nuggets that can improve pricing strategies.
- Retailers try to compete with agile pure-play competitors that have homegrown, sophisticated analytics tools that allow them to do customer-specific pricing. However, a lack of automated tools makes it impossible for omnipresent retailers to harness and analyze their increasing volumes of data.
- Slowly retailers begin centralizing data, making it easier to harness information.

01

1. BASIC

- Omnichannel retailing platforms enable consumers to search for merchandise and compare prices between competing retailers in real-time.
- Consumers begin to do "homework" before entering a store — or while inside of a store — to ensure they are getting the best price.
- Managers still create pricing strategies based on gut instincts, with little insight or factual recorded data to back up their decisions.
- Prices are recorded and — maintained on paper-based spreadsheets, a practice that leads to duplicated, erroneous and stale information.

Anytime, anywhere shopping has catapulted price transparency into a critical shopping tool for consumers, a move that is changing the game for omnichannel retailers. No longer able to compete on price alone, all-channel brands need to redefine their overall businesses strategies as a means of differentiating themselves in a competitive marketplace, as well as attracting shoppers and driving long-term loyalty.

As a result, retailers are investing in forward-thinking analytics tools that drive visibility into consumer behavior. The solutions are the foundation needed to help brands design symbiotic pricing and merchandising strategies, an effort that can improve localized pricing efforts designed to drive customer loyalty.

The digitally-influenced omnichannel retail model has changed the shopping experience exponentially. In a traditional retailing landscape, consumers choose where to shop based on the brand that routinely offered the "lowest price" or best deal. However, omnichannel models have completely changed the game.

Shoppers now connect with their favorite brands via desktop, laptop or mobile devices. Shoppers are leveraging powerful web-based search engines and 24/7 access to retail websites to gain product-level pricing visibility. And oftentimes, this price transparency is the deciding factor that drives purchase decisions. In fact, 47% of companies reported that price transparency is one of their top pricing business challenges, compared with 24% of retailers in 2014, according to "Pricing 2015: Learning to Live in a Dynamic, Promotional World," a report from Retail Systems Research.

Add in the pressure from pure-play competitors, such as Amazon and Google, that continue to up the ante on service, and it is no wonder why all-channel companies are growing increasingly confused about how to fight back. Besides offering same-day fulfillment strategies that are often hard to duplicate, Amazon is rewriting the rules when it comes to pricing.

The pure-play has built its reputation on mining customer data, and changing thousands of prices across innumerable categories and products on a daily (sometimes hourly) basis. Using a home-grown, distributed, decentralized service oriented architecture, Amazon catalogs all product data, and collects information among a variety of sources, including cus-

47%

Retailers reported that price transparency is one of their top pricing business challenges, compared with 24% of retailers in 2014.

Source: Retail Systems Research, "Pricing 2015: Learning to Live in a Dynamic, Promotional World" tomer databases, web affiliates, third-party sellers, retailers, fulfillment partners, public data sources and credit card companies, among other entities. Meanwhile, self-developed algorithms track business performance against approximately 500 measurable goals, as summarized in "State of the Industry Research Series 2014: 3rd Annual Analytics in Retail Study," an EKN Research report.

The pricing strategy of Amazon and others has armed consumers with unprecedented price transparency. This real-time access to the pricing landscape set the groundwork for showrooming, using personal mobile devices to compare prices during in-store shopping trips, as well as the new trend of webrooming, where consumers check online prices, only to buy merchandise cheaper in-store. With 80% of consumers checking prices online, according to "Beyond the Checkout Cart," a report from MIT, it is no wonder that consumers keep jumping from brand-to-brand in hopes of finding desired merchandise at the lowest price possible.

500

Measurable goals Amazon's self-developed algorithms track against business performance.

Source: EKN Research, "State of the Industry Research Series 2014: 3rd Annual Analytics in Retail Study"

Keeping Pace With the Pricing Leaders

The new digitally-influenced shopping era has clearly changed the retail landscape. This fast-moving environment requires an overhaul of retailers' pricing strategies and capabilities if omnichannel retailers want to remain relevant.

It has also created an intensely competitive playing field — one that welcomes new players across the physical and digital landscapes, each presenting complex pricing strategies and expanding assortments. It is becoming evident that retailers that maintain traditional pricing strategies, especially those based purely on gut feelings as opposed to harnessing cold, hard data, often do not know what information is most important when making pricing decisions.

While some retailers are taking a stab at analyzing data, they are getting sidetracked with one-sided efforts. For example, too many companies are approaching pricing as a singular strategy, one that works independently of its assortment and promotional efforts. Others don't even bother to take into account competitor assortments and related prices — a factor that is taking a very real toll on 48% of companies, according to RSR Research's "2015 Pricing Report."

Pricing Structure for Retail Strategies

DARIUS JAKUBIK
VP of Sales & Marketing,
Advanced Pricing Logic, Inc.

> "Strategic price planning starts with a clear vision of desired goals. Once those goals are established, then the logical step is to reverse engineer how to attain those goals."

Q: How has the Omnichannel experience changed customer expectations — and access — to competitive pricing?

DARIUS JAKUBIK: The advent of the omnichannel experience has given consumers the power to choose how, when and where they shop for anything and everything within the marketplace. Consumers understand that price matching and competitive data are readily available and that switching loyalties from one seller to another due to their recent "price-education" is just par for the shopping-course these days. Whether it's a trip to the mall, surfing the web, or scrolling through smartphone apps, today's savvy retailers have all bases covered. Competitive pricing, product availability, vendor ratings, shipping options, you name it, they've got it and it will be factored into every purchasing decisions. This expanded competitive price availability has opened the door to global catalogues forcing retailers to prepare intelligent strategies to do battle against competitors both large and small.

Q: Why should retailers still analyze pricing among channels independent of each other, as well as combined?

JAKUBIK: When analyzing the channel as a whole, it's best to set prices within an acceptable market range. But once you narrow the focus, the game gets much trickier. A strong pricing analyst needs the power to consider internal metrics when pricing, as well as the ability to look at individual competitors and across the market as a whole. Today's hyper-competitive retail world demands that companies have the ability to read and react to changing market conditions in real time. By taking advantage of strong analytic software, companies will have the luxury of making fact-based decisions, instilling the confidence to compete in each individual matchup, as well as maintaining internal profitability metrics across the board.

Q: The key to a successful dynamic pricing strategy requires companies to understand their strengths or weaknesses so they can optimize pricing. Once they are aware of these variables, what is the next step in creating a successful pricing strategy?

JAKUBIK: Pricing strategists must first begin the process by taking into consideration what effect SKU prices will have on operations. This cannot be overstated. By always considering business metrics first, you begin with a tremendous advantage no matter what the strategy is. This methodical approach of initially looking into one's own strengths and weaknesses is absolutely necessary to get a clear picture of which strategies are to be executed. It initiates the wisdom and clarity of how past and future pricing have and will affect all aspects of operations, which is a direct correlation to profits and revenues. This holistic and logical approach is highly sophisticated and is yet to be in widespread use in today's retail environment. Retailers are either uninformed, or simply don't have the time or wherewithal to develop such intense routines. As more companies are discovering, price optimization solves the problem. Those that continue to operate without will lag behind. A good pricing system is worth its weight in gold.

Q: What are the ideal analytical tools that retailers should be using to best optimize pricing in an omnichannel landscape?

JAKUBIK: The exponential growth of data is driving the need for scalable solutions. Primitive pricing tools can't keep up with the explosion of information being gathered by companies aimed at achieving a big advantage over their competition.

Discovering a comprehensive, intuitive, end-to-end automated pricing solution is imperative if you want to compete in today's hyper-competitive omnichannel marketplace. Implementing such a solution allows you to dive deep into back end analytics as well as glimpse the competitive landscape that will provide a structure by which to implement the corporate strategies that define your company.

It has never been more important for retailers to be responsive to customers' buying patterns. This requires retailers to consider the relationship of price in regard to other product prices across their assortment, as well as competitors' assortments, and the impact of supplier promotions on price. At the heart of how all of this product moves however, is based on the consumers' perception of price. It is no longer a matter of delivering the lowest available price on an item that will drive a purchase. Instead, it is about delivering the "fairest" price on merchandise their shoppers demand most often.

80%

Consumers that check prices online before making a purchase.

Source: MIT, "Beyond the Checkout Cart"

An Analytical Approach to Setting Price

When determining how to deliver the fairest price, and thus, drive a valuable price perception, retailers need to turn their attention to a key factor: customer demand. "The pricing strategy needs to be driven by a view of the customer, including various inputs that are used to make a final decision to purchase," as summarized in "Prioritize 10 Best Practices for Successful Price Optimization Implementations," a report from Gartner. "Once you develop a view-of-the-customer perspective, this will inform the business objectives and requirements to ensure that customer needs are fulfilled within a profitable framework."

As a result, retailers need to up the ante on analytics efforts. While some companies will undoubtedly argue that they are adopting analytics to better understand how to manage their pricing strategies, the truth is efforts remain rudimentary. Still stuck in a product-first pricing model, too many companies focus on specific lines or categories to determine a price or sales value. While this works in a mass pricing and promotions model, this process only shows a portion of demand, and is not effective in a competitive, always-evolving omnichannel world.

Instead, today's strategic pricing models must be consumer-driven. By understanding what pricing across specific consumer market baskets look like, especially those of a brand's most loyal shoppers, retailers can compete not by absently playing "catch-up" with hard-hitting competitors, but by pricing merchandise to meet the demand of its most profitable shoppers. This approach becomes even more appealing when you consider that companies that fully engaged shoppers represent an average

HOWARD LANGER
Managing Director of Price and Promotion, dunnhumby

“Retailers need pricing strategies for each customer group to free themselves from the downward spiral of competitor matching.”

Analytics and Customer-First Pricing

Q: How can analytics assist retailers in creating a pricing strategy that will help them avoid the “race to bottom,” yet still be profitable? Why is a one-price-fits-all strategy no longer optimal?

HOWARD LANGER: Instead of focusing on moving products, retailers need to focus on people. Analytics will show which shoppers are more important to your business than others. dunnhumby research shows that one loyal customer is worth 12 uncommitted customers — and knowing which prices are important to them is crucial. It is no longer enough to simply understand the impact of price changes at a “product” level and be blind to the quality of customers that responded, and what else they purchased — or didn’t. Understanding your most important groups of customers (segmented pricing) and the ability to target individuals (personalized pricing) is the future of pricing. That makes data and analytics mission critical.

Q: Why is it important to understand your data, especially related to customer-centric information, and price strategy before implementing a pricing analytics tool?

LANGER: Put simply, when retailers understand which customers are shopping and how their behaviors are impacting each category and each product’s sales, they can understand where to invest more — and where to invest less — to move the needle on loyalty and price perception. If they cannot successfully mine that data, then they will continue to repeat last year’s mistakes and risk losing their most valuable shoppers. Knowing which customers are price sensitive helps you determine which lines to price match on, and how much it will cost you. Knowing which customers are most valuable helps you focus price and promotions and loyalty-driving activity. Retailers need pricing strategies for each customer group to free themselves from the downward spiral of competitor matching.

Q: Why do retailers still struggle with how to create the optimal pricing strategy? What continues to trip them up?

LANGER: A 2014 study shows that firms with superior pricing capability have margin rates 33% higher than those that don’t. Meanwhile eight in 10 companies have a pricing strategy that can be summarized as “follow suppliers” or “follow competitors.” Both are weak positions. Retailers struggle because they’re chasing margin rates instead of long-term brand value. They struggle because tools like spreadsheets can’t show them the ROI available from better pricing. Only recently have retailers begun to invest seriously in pricing teams to support merchants. We are close to a turning point as marketers continue to strive to attract shoppers with more personal communications. Meanwhile marketers can’t understand why prices and promotions aren’t more relevant. This is encouraging as pressure grows on the merchant teams to construct prices that are good for customer segments and individual customers.

Q: Can you share any tips for retailers that want to get started down the path to expertly using pricing analytics?

LANGER: A robust optimization tool that combines every day and promotional pricing into a single forecast is essential. This enables retailers to see category cross-effects and other unintended consequences of their decisions. If your current tool cannot show you impacts by customer segments, you are operating to pre-digital principles. Change it. At the same time, software tools won’t solve everything: you need a solid pricing strategy to support them. By analyzing shoppers, financial goals and competitive position, retailers can get a clear view of the big picture and develop a customer-first strategy that ensures future success. Analyze your data to find your most profitable customers and invest in them. Defend your most price-sensitive customers but don’t overspend. Target promotions to your valuable customers and personalize promotions in-store and online. Those steps will lead to *lasting* pricing power.

23% premium return in terms of share of wallet, profitability, revenue, and relationship growth compared with the average customer, according to the "Gallup Customer Engagement Score (Gallup CES)," report from Gallup.

These points reflect that forward-looking success is all about seeing value from the perspective of the shopper, and aligning price as a piece of that overall value proposition. "Fundamentally, it is all about approaching pricing from the eyes of customer," Greg Girard, program director, merchandise strategies, International Data Corp. (IDC) said. "Make sure that your data is about your customer base and their shopping behavior. By blending this with current, accurate data about the competitive environment, retailers are ready to respond to consumer demand."

48%

Retailers that don't take into account competitor assortments and related prices.

Source: Retail Systems Research, "Pricing 2015: Learning to Live in a Dynamic, Promotional World"

Analyzing the Opportunities

As retailers prepare to use customer relationships to create more relevant, valuable pricing strategies, they need to set the right foundation. Their first step is to get their data in order — something that tends to be an overwhelming task, especially for 9 out of 10 companies that still fail to make customer profiles available to merchandising and marketing teams in real-time, according to "State of the Industry Research Series 2014: The 3rd Annual Analytics in Retail Study," EKN Research.

However, these retailers know how important it is to get this customer data into the hands of key decisions makers, especially those involved in creating pricing strategies. At the heart of their efforts is getting a robust cross-section of information about each shopper and customer segments. This requires companies to leverage customer data from loyalty programs, point-of-sale, online transactions, mobile apps, social media, in-store videos, public sources, and more.

The next step is to understand what is happening on a channel-by-channel basis. While retailers are eager to connect with consumers seamlessly through the omnichannel retailing experience, they need to be able to understand the activity happening individually in each channel to get a clear understanding of customer demand, price elasticity and the perception of value. Once retailers can understand what is happening individually, it is easier for the brand to get a holistic view of a customer, and whether the company is hitting the mark, channelwide. Belk is one leader in this area.

KEVIN STERNECKERT
Executive Vice President – Marketing, Predictix

Changing the Game in Omnichannel Pricing

Q: How have online-only retailers changed the game when it comes to pricing strategies, and how have they impacted all-channel retailers?

KEVIN STERNECKERT: The nimble and aggressive pricing practices of online-only retailers have wreaked havoc on omnichannel retailers. As an example, Amazon averages three million price changes per day. If an omnichannel retailer tries to compete on price in this environment, the result will be numerous price changes throughout the day that must be reconciled (both online and in physical stores). Even with electronic shelf labels, it's unlikely that retailers would elect to change prices in stores that often. Consider the customer experience of prices changing multiple times while the shopper is standing in front of the item.

The impact of such competitive activities results in cross-channel conflicts, where the price in the store will likely be different from the online price and also higher than prices from online-only retailers.

Q: Making pricing decisions based on merchandising, inventory and assortment is a challenge for retailers. Why does this continue to trip them up and how can they change this?

STERNECKERT: Retailers typically make pricing decisions independent of assortment and inventory decisions. However, retailers do understand that pricing, assortment and inventory are all part of the same equation. Change a price, and it affects inventory; change the assortment, and the prior inventory demand and pricing will not agree with the new assortment. Unfortunately, most retailers' systems cannot handle these simultaneous decisions, and over time these became siloed. Now retailers are faced not only with a technology obstacle, but an organizational one, as retailers would need to unlearn treating these decisions separately.

Ultimately, retailers must invest in adapting their organizations, processes, and ultimately systems so they can address these decisions simultaneously.

Q: What impact is analytics playing in this new retail model, and what do retailers need in their tool kit to keep them competitive?

STERNECKERT: If a retailer understands consumer demand from the data both within their organization and from external sources, they can make profitable demand-driven decisions. Yet the tools that are generally used today are outdated and cannot understand and recommend appropriate merchandising decisions based on the true demand drivers. A new breed of tools has emerged that leverages machine learning, unlimited data and advanced prescriptive analytics in the cloud. Omnichannel retailers must secure tools that offer these capabilities in order to compete — and win — against online-only retailers.

Q: Can you give any advice to retailers trying to master pricing in an increasingly customer-driven marketplace?

STERNECKERT: First, focus on acquiring tools that can analyze all data across the entire retail and external footprint; these tools should be able to proactively recommend actions based on demand analytics. Next, develop policies that address the challenges of brick and mortar as well as the other channels of retail. Finally, live up to your brand promise; if your policy is to have the same price in every channel, then take special care to ensure you deliver on that promise.

> "If a retailer understands consumer demand from the data both within their organization and from external sources, they can make profitable demand-driven decisions."

Supporting dedicated data warehouse appliances and a retail logical data model, the department store chain is also supporting an end-to-end business service that integrates all channels across the chain. Enabled by timely data, analytic insights are used to revamp traditional approaches to pricing, as well as marketing, promotions, assortment and fulfillment.

The final piece of the puzzle is to incorporate a foundation of information from competitors. It is imperative to have an understanding of what competitors are doing in near-real-time, and you need it in an easy-to-consume data feed. If you don't possess competitive pricing data you are operating in a vacuum, which is never a good thing for a healthy business.

Retailers are ready to dust off these data sources, and delve into how their shoppers are approaching price in relation to making a purchase decision — and those who get it right are on their way to growing sales. These leaders are the ones that are applying these data sources to robust analytics tools and strategic pricing applications.

"Advanced tools enable retailers to understand the propensity for consumers to react a specific way to different pricing models," IDC's Girard explained. "Advanced analytics uncover the interplay of attributes beyond processes, and getting into the correlation of customers and transactions."

23%

Premium return of wallet share, profitability, revenue and relationship growth among companies that fully engaged shoppers.

Source: Gallup, "Gallup Customer Engagement Score"

Turning Insight into Action

While 80% of retailers report they tend to lag behind Amazon in terms of the strategic use of analytics, they do consider the tools extremely strategic, EKN's "The 3rd Annual Analytics in Retail Study," revealed. One of the top tools of choice: price optimization.

An analytics tool that uses artificial intelligence to determine how customers will respond to different product prices throughout different channels, price optimization provides the "so what" factor, and considers elasticity, lifecycle, profitability, and popularity of the product.

Slowly but surely, more companies are learning the value of price optimization, including the promise of greater sales, margin and price perception lift. While 21.1% of retailers said they currently use digital commerce pricing optimization software, in the coming year, another 18.4% plan to deploy it as well, all with hopes of increasing sales by 6.7% and profits by 4.6%, according to *RIS News*' "New World of Pricing Optimization" report.

Discount merchandiser fred's can attest to these significant results. It's overall pricing strategy and key market differentiator comes from its ability to create real-time pricing scenarios, define rules and constraints, simulate revisions, and understand the impact to the category. Using the analytics technology, fred's is able to validate the company's key value items (KVIs) and key competitor items (KCIs) within each category to enhance competitive positioning, according to a company statement.

The solution enabled fred's to compete more effectively on price by monitoring and modeling the competitive price index (CPI) by category. Focusing on its top-tier KVIs and KCIs, fred's leverages competitive pricing data and rules when formulating pricing decisions. In addition, fred's can now explore additional margin lift for private-label items compared to their national brand equivalents. By modeling promotions, fred's is able to forecast anticipated lift and determine whether a promotion will achieve the desired objective, often identifying better targets for investing promotional funds.

Overall, fred's has been able to achieve dramatic lift across categories, while maintaining gross profit dollars while continuing to deliver on its commitment to being the "low price leader" in its markets.

9 out of 10

Retailers don't make customer profiles available to merchandising and marketing teams in real-time.

Source: EKN Research "State of the Industry Research Series 2014: The 3rd Annual Analytics in Retail Study"

The Next-Generation Pricing Strategy

The omnichannel world — and other digital influences — continues to change the retail landscape, as well as how consumers research and buy products. As more companies embrace tools like price optimization, they are opening the door to more advanced pricing techniques. One of the evolving trends is the concept of clubs. One of the most popular examples is jet.com.

The newcomer, which launched in July to compete with the likes of discounters and category killers, is a new online discount marketplace that hopes to lure shoppers away from behemoths like Amazon and Walmart. Focused on a "club" business model, shoppers pay an annual $50 membership fee, and can shop products across 16 major categories, including health and personal care, beauty, home goods, furniture, electronics, toys, video games and office supplies.

What makes the business model different is the more a customer purchases, the slower the delivery option they choose, and if they waive return fees, customers are poised to save even more. Using a proprietary pricing algorithm, jet.com can analyze shoppers' baskets and match real-time dynamic prices based on retail partners in their network that are closest to the proximity of the shopper, creating a more efficient, cost-effective fulfillment strategy. The same algorithm then determines other prices for less loyal shoppers.

"It is a collaborative shopping model that opens the door for more interesting pricing techniques," Girard explained. "In the past, price is how retailers differentiated themselves in the marketplace. Based on dynamic pricing, jet.com is proving that the notion of convenience, and a 'have it your way' pricing model is what allows it to stand out from the crowd."

21%

Retailers that currently use digital commerce pricing optimization software.

Source: *RIS News*,"New World of Pricing Optimization"

Conclusion

Price transparency may now be a critical shopping tool for consumers, but it is teaching omnichannel companies they can no longer simply compete on price alone. To differentiate themselves in a competitive marketplace, as well as attract shoppers and drive long-term loyalty, retailers are investing in forward-thinking analytics tools that drive visibility into consumer behavior. The next-gen solutions enable retailers to deliver more localized pricing to customer segments through the right channels when shoppers are ready to make a purchase decision.

80%

Consumers that check prices online before making a purchase.

Source: MIT, "Beyond the Checkout Cart"

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