REVIONICS®
an aptos company

Price Perception:

How To Win Customers and Influence Perception

Defining your current price perception and developing a strategy for improvement

REVIONICS®
an aptōs company

Price Perception:

How To Win Customers and Influence Perception

In retail, perception is reality. This is particularly true with pricing, where consumers are well-informed and have developed strong perceptions of pricing over time.

Creating a winning market price perception is an essential strategy in an increasingly competitive and dynamic retail landscape. However, too often retailers let consumers determine the pricing perception, instead of influencing the market with an effective, organization-driven strategy.

It starts with gaining a better understanding of how to look at price perception and preparing the right battle plan to drive your strategy. Then, retailers can build upon that foundation to create a pricing strategy that will successfully influence consumer perception for a stronger pricing performance.

Finding Your Price Perception Arena

Retailers commonly mistake price perception as a "race to the bottom." That is to say, having a good price perception is all about having the lowest price on the market, or at least a lower price than your competition. While this is a fundamental aspect for two virtually indistinguishable retailers, it ignores the quintessential relationship between quality and price.

The correlation between price and quality allows various retailers to compete in different 'price perception arenas.' In this case, quality relates to the broader shopper experience, and not just the physical attributes of the product. Two retailers may sell similar products, but a vastly different shopping experience at one can dramatically increase how the consumer perceives quality. Understanding your quality proposition in relation to your price is key to establishing where you compete and is a great starting point for building a holistic price perception strategy.

Price Perception (LOVE) Matrix

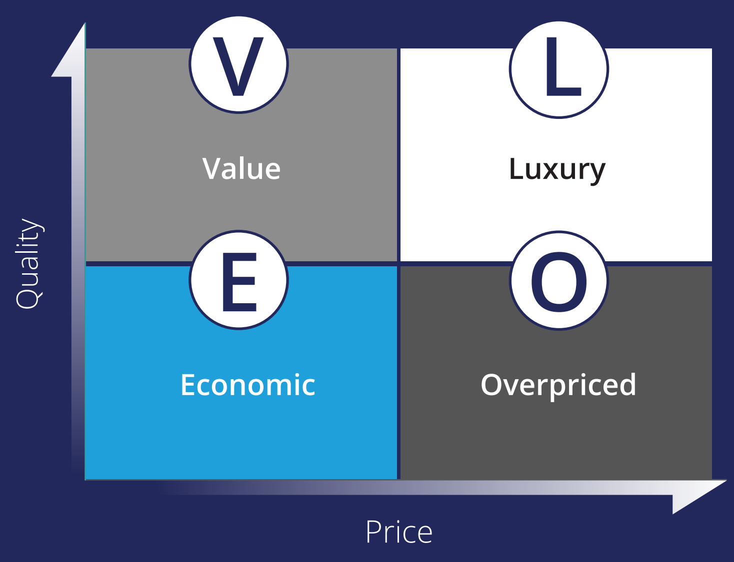
To illustrate price perception arenas, one can use the simple LOVE matrix below which outlines the four possible arenas that exist for brands and retailers: Luxury, Overpriced, Value and Economic.

Now perform this quick experiment:

1. Select a product, service or retailer that you shop (this could be clothing brands, cars, restaurants, wine, airlines - anything that you spend money on).

2. Without doing any research, select ten brands within the chosen category and place them in the above LOVE matrix in one of the four arenas.

3. Ask others to classify the same brands within the same matrix; don't allow them to see how you classified those brands until after they've completed the exercise.



Price Perception (LOVE) Matrix

The purpose of this is to demonstrate several key elements of price perception while also defining the concept of price perception arenas. Here are a few observations you could make from the matrix:

- Consumers inherently know which arena brands live in without doing any research. This is fundamentally the essence of price perception.
- Different consumers will place the same brands in different arenas.
- Brands consistently placed in the same arena have done a better job defining their price perception than others.
- Even though Value is the one arena that a lot of brands and retailers claim to play in, it's not the arena that they are ultimately placed in by consumers.
- Overpriced is the only arena where consumers probably won't spend their money, and where brands are most likely to fail unless they improve their price or quality perception.

Key Items: Choosing Your Battleground Within the Arena

Once you know the arena you are competing in and who your top competitors are in that arena, it is essential to identify the right items to focus on. These are most commonly referred to as key items and need to become the battleground for your competitive pricing.

Most retailers have a list of key items (often called KVIs or Key Value Items) they focus on. However, retailers do not always use analytical methods when compiling these lists. Often retailers allow merchants to dictate the KVIs or simply chose items based on sales volume. While this can be a good place to start, it is not necessarily best practice.

Retailers need to have the right balance of KVIs for the right regions, seasons and channels. Successful retailers evaluate their KVIs regularly in order to stay competitive in an ever-changing market. Your best guarantee is to rely on analytics for an unbiased, customer-driven approach to identifying key items with enterprise objectives in mind.

Looking in The Mirror: What Is Our Current State?

Having defined your price perception arena, your key competitors, and the key items to focus on, it is now time to see where your price perception currently stands. Knowing your baseline helps properly model out and forecast the true value and expense of moving to a desired price perception.

Answering the following three questions can help you to develop an understanding of what your current price perception is in relation to your top competitors.

Question 1:
What is your Competitive Price Index?

One influence of your price perception is your competitive intelligence capabilities. A Competitive Price Index (CPI) is a metric that quantifies how your products, categories or brands are positioned in the market. To build a comprehensive overview of your current Competitive Price Index, you need to track competitors' prices on a daily basis and see how your KVIs compare.

Of course, collecting and analyzing pricing data across dozens of competitors and millions of products is no small task. That's where an advanced analytics platform can streamline processes and provide more accurate, up-to-date data.

Once you have the data, it is equally important to have the ability to analyze and filter that data to understand some of the nuances of your current CPI. Are you 5% above the lowest market competitor in Category A but 3% below in Category B? Are your key items not priced competitively? Are you drastically over or underpriced in one region or market? These insights are key to adapting your price perception.

Question 2:
What do third party price perception reports say?

While the CPI is useful for an unbiased comparison to your competition, it does not discern between the 'actual' price against the competition and the 'perceived' price against the competition. And of course, we are talking about influencing perception here. Thus, third party reports, like rankings, studies and surveys from industry analysts, are very valuable tools to understanding what consumers actually think about your current price.

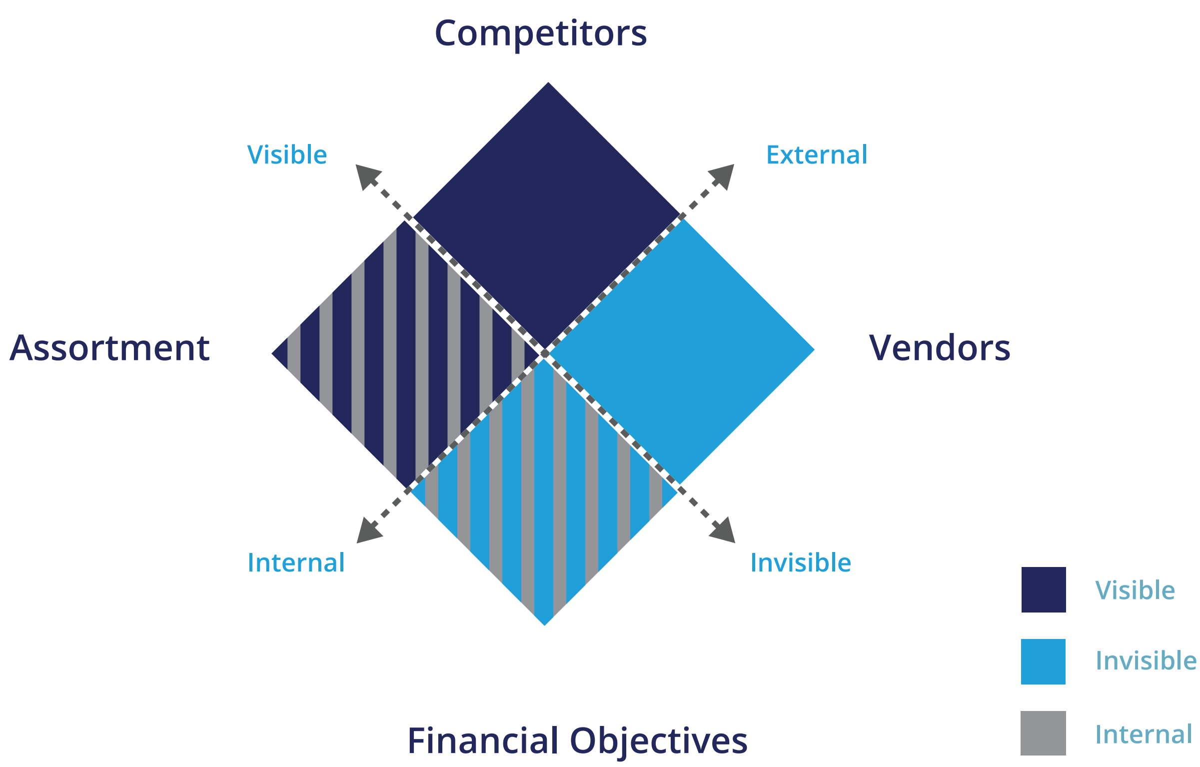
Very frequently retailers may have a better actual price than their competitors but are not getting credit for it when consumers provide their feedback. Various reasons can account for this disparity:

- It takes time to establish price perception in the market.
- The competition may be winning in specific categories, regions or channels most important to survey respondents.
- They might have better analytics or more relevant key items lists than you.
- They might have more sophisticated AI pricing platforms.
- Marketing matters – having low prices is not enough; it needs to be communicated.

Question 3:
What is actually influencing pricing in your organization?

Moving away from analytics and consumer surveys, it is important to take a candid look at what is driving pricing decisions within your organization. One tool that can help you accomplish this is the Price Influence Diagram (PID) shown below.

Price Influence Diagram



The PID assesses the primary influences on merchant pricing decisions and evaluates them along two key criteria - whether they are visible to consumers, and whether they are internal or external. Using the diagram is simple; just ask several merchants where they would place their business on the diagram based on how influential the following four things are to their pricing decisions:

- Competitors
- Assortment (including brand gaps, private label vs. national, volume discounts, G-B-B, etc.)
- Vendors (this includes all aspects ranging from MAP to vendor funding, etc.)
- Financial Objectives (includes global plans and self-imposed ones like item level margin targets)

Why is this exercise meaningful? If most of your merchants are placing their businesses in the blue (invisible) diamonds, they are making pricing decisions based on things that the customer does not see or care about. While all four of these pricing influences are important to running a successful retail business, the ones that are visible, particularly competitors, are the only ones that drive price perception. It does not matter to consumers if merchants hit a margin target of 24%, but it will matter if your price is 20 cents higher than your top competitor.

Knowing what is internal versus external is also important because it denotes what the retailer can control. Retailers cannot govern the competition and have limited sway over vendors. However, retailers do have complete authority over their financial objectives and assortment decisions. Retailers need to focus on adjusting the things they can control to support the creation and adoption of a world-class price perception strategy.

One simple example of this is re-adjusting margin targets in categories with a high mix of key items to focus on volume objectives. An assortment-based example would be expanding a brand or eliminating brands that do not support the pricing perception objectives you wish to achieve.

Regardless of how you evaluate current pricing influences, it is important to understand which obstacles and existing practices might conflict with the price perception-focused strategy you are planning to build. This basic discovery of why merchants are pricing the way they are will also help when trying to drive adoption and change management once the correct price perception strategy is in place.

Building a Winning Price Perception Strategy

At this point, you should now have conducted an honest assessment of your current price perception, as well as identified where you wish to be strategically and which KVIs are most influential. Once you know the arena you compete in, which competitors you compete against, where your gaps are compared to those competitors, and what internal obstacles may exist, you can begin to build your future.

To influence and strengthen price perception in the market, retailers need to align their competitive, promotional, and messaging and marketing strategies with their price perception goals. All three of these strategies require best practices, data and analytics to properly design and execute. However, for our purposes we will take a look at several important considerations when developing these strategies and how they relate to your price perception.

Promo mix matters

A lot of retailers falsely identify as an EDLP or Hi/Lo retailer. In reality, most retailers offer a mix of both. Competitive strategy and promotional strategy collectively drive price perception, so there isn't just one lever a retailer can pull to fix their pricing image. Thus, retailers can adjust their regular and promotional mixes to find the sweet spot and drive perception for shoppers while hitting key business objectives.

The best retailers will leverage analytics to identify important key items and successful promotions. By identifying what works and what doesn't, retailers can achieve more effective promotions for driving business performance and price perception.

Competitive strategies need to be effective – not complex

What's your competitive strategy elevator pitch? Compare the difference between these two options:

> **Option #1:** We match the lowest market price on our most important items in all stores and channels

> **Option #2:** For key items we look at the median price of six different regional competitors. We also look at the lowest two prices within a mile of each store. We then take the lowest of the two values and aim to be priced between 100% and 103% of that number on those items. For non-KVIs, we apply a regional matrix where we price at different indexes vs. the average of the four most important regional competitors. In metro areas, we...

You get the idea. If you can't explain your competitive strategy in a few sentences, then good luck with your messaging and marketing. Yes, your strategy can be layered or hyper-locally focused. It should absolutely treat key items differently than non-key items and rigorously apply the right indexes and matching strategies appropriately. It should not, however, be an inefficient, tangled web of logic.

Progress vs. perfection

Improvement takes time. It is not advisable to make drastic shifts, like changing all your prices by 10% in one massive pricing action, or dramatically altering your promotional mix. Instead, your strategy should focus on making minimal adjustments and monitoring the impact on value and price perception. The risk is simply too high and there are often trade-offs between volume and margin when decisions are made. This does not mean that bad practices, like ineffective promotions or matching on inelastic background items, should continue. It simply means you should plan on measured and data-driven strategy adjustments for gradual progression, not immediate perfection.

The need for speed

While you shouldn't make huge shifts, you should be able to make small changes quickly. Improving your price perception is highly dependent on your capability to price more frequently than your competition. Even the best strategies will make little difference if your competition has the speed and technology advantage.

Say you only take pricing changes on Tuesday, but your competitor can change prices every day of the week. If they drop to a lower price in Wednesday, you will lose an entire week of price perception before you can react. And once you do match or beat their price, they can simply adjust as well and continue the pattern of winning 6 out of 7 days every week.

This is critical in a rapidly evolving retail environment that is becoming more dynamic every year. Quarterly competitive shops are simply not good enough for most retail verticals anymore, and the trend toward daily and intra-day competitive pricing is accelerating.

Adopt, Measure and Improve – A Virtuous Cycle

Developing world class competitive and promotional strategies is one thing – getting an entire organization's worth of merchants to adopt it is a completely different challenge. However, a top-down, centralized approach is critical to price perception success. Consumers base their price perception on the entirety of their interaction with your products, and it only takes a few merchants deviating from the plan to sink a pricing strategy.

If Merchant A and Merchant B are both matching competitors on KVIs and Merchant C is 20% above, all three stores are negatively impacted by the inconsistent pricing. An effective approach needs to be aggregated to a greater objective, not a collection of separate tactics.

The Value of Adoption

One way to think of the value of adoption is by using the simple formula below.

$$V = Q \times A$$

Q is the quality of the strategy being put in place. For price perception, it is all of the competitive, promotional and marketing elements.

A is the adoption of that strategy across the organization. It is both the percentage of merchants and percentage of their businesses.

V is the value generated as a result. In our case, value is driving a world class pricing perception that beats your top competitors in your arena.

Even the best strategy using the best analytics and advanced pricing capabilities will fail to drive value with zero adoption. Similarly, a poor strategy adopted by many will have little effect on price perception. However, a great strategy coupled with strong organizational adoption and governance can easily generate tremendous value.

Challenges to Adoption

Of course, experience teaches us that driving adoption in retail can often be a challenge. These are the 5 most common reasons why individual merchants may avoid adoption of a new pricing or promotional initiative.

Risk averse

People tend to be risk averse and err on the side of caution. This is one of the main reasons why retailers run the same ineffective promotions year after year. It is also a reason why it is hard to convince a merchant whose business is healthy to change course on their pricing and promotional strategies.

Loss of control

Pricing remains the quickest lever that a merchant can pull to improve their volume or profitability. It can take months to make assortment changes, and category innovations do not occur every day. Because of this, merchants cling to the power they hold over pricing as a tool for achieving the financial goals to which they are held accountable. While it is hard enough to take a risk, it is even harder to feel like you are losing control to an algorithm. However, the reality is that even the best merchants cannot beat the top analytical platforms for effective and accurate pricing recommendations and forecasts.

Vendor influence

Vendors drive much of the pricing in retail, from setting the initial price on the product, to determining promotional activities and funding. Yet, price perception is determined by the consumer, not the vendor. As such, it is mutually beneficial for merchants and vendors to leverage as much consumer demand-based analytics as possible when determining pricing and promotions. Simply shifting vendor funds and promotional activities from one product to another can drive enormous value for all parties while keeping the focus on the consumer.

Incented to not adopt

This is perhaps the largest barrier to adoption. Merchants are given a financial plan and personal incentives, like bonuses, to hit or exceed that plan. It is very challenging to convince a merchant to support a larger pricing initiative that on the surface contradicts his business goals. A misalignment between financial objectives and pricing strategies can lead to serious adoption challenges and should strongly be considered when building pricing and adoption strategies.

Partial Adoption

Another complication is that all merchants benefit from a better price perception – including those who do not adopt the strategy. Say 9 out of 10 merchants implement a great competitive strategy and increase traffic. This ultimately helps the 10th merchant who did not adopt, and with their store performing better than ever, they might be even less likely to change.

Essential Foundations for Driving Adoption

With all of these possible roadblocks to adoption, it can be difficult for even the best designed strategies to see implementation organization-wide. That is why it is key to prepare accordingly. When it comes to driving change in an organization, governance and measurement are the two most essential pieces.

Governance

New strategies need strong executive support and a well-thought-out governance model. Retailers need to incentivize the correct behaviors and ensure compliance to key top-down initiatives. Although this might seem basic, it is surprising how often this can be overlooked or mishandled.

The best way to drive adoption is to prevent it from being a choice. Your brand and price perception are too important to allow a few moldy blueberries to spoil the batch. However, governance goes beyond just adoption. To support all of the complexities of a world-class price perception strategy, governance is necessary to guarantee that all of the right processes, decisions and actions occur according to plan.

Measurement

CPIs, third-party surveys, and other various measurements for price perception are critical to understanding if the new strategies are effective. The best retailers use sophisticated value measurement capabilities to scientifically discern how much value has been derived from pricing and promotional activities, while cancelling out other influences. These retailers can see exactly how they are affecting price perception and if they are driving the intended results.

On top of this, the best pricing platforms can even segment out value measurement reports to clearly demonstrate that the merchants who have adopted the best practices are outperforming those who did not. Concrete, measurable proof is a highly effective tool to encouraging full adoption.

Improving Your Price Perception

Creating the right pricing and promotional strategies can lead to enormous value generation and a much stronger price perception in the market. Becoming a price perception leader is not easy and requires work, data analytics and consumer-focused best practices. If you follow these tips, trust the data and listen to the customer, you will be able to craft a winning price perception strategy that will benefit business objectives and build customer loyalty.

Your
Data + Our
AI + Our
People = An
Optimized Strategy
for You

About Revionics

Revionics guides retailers on the lifecycle pricing journey with leading AI solutions for pricing, promotions, markdowns and competitive insights. As a trusted partner, we provide our customers with clarity and confidence to make optimal pricing decisions for powerful results.

Revionics is an Aptos company and plays a key role in their suite of unified retail solutions.