Attracting and retaining customers with insights-driven dynamic pricing

Strategic scenarios for reacting to competitor and market activity

Contents

A world of constant change

Dynamic—adjective. (of a process or system) characterized by constant change, activity or progress.

The story is all too familiar. Empowered by advanced mobile technologies and multiple digital channels, socially-connected, savvy consumers now shop on their terms. Retailers are being forced to evolve if they are to retain the custom of loyal shoppers and entice those that currently purchase elsewhere. They need to protect their share of wallet against an increasing landscape of nimble competitors.

With so much choice, in both products and service, consumers are now self-trained to not pay full price. Why should they when it's so easy to shop around for the best deal?

In response, and to remain competitive, retailers are adjusting prices more frequently than ever before. According to a 2015 benchmark report "Learning to Live in a Dynamic Promotional World" from leading retail analyst firm RSR Research, 75 percent of retailers increased the number of price changes sent to stores and other channels over the last three years.[1]

Sense and respond

This growth is driven primarily by online price changes where retailers are reacting to competitor and market activity. More sophisticated retailers are not just reacting but instead proactively testing various pricing strategies to see what effect they have on their customers; they are sensing and responding. This is dynamic pricing, and the same RSR report indicates that retailers are increasingly viewing dynamic pricing as a major opportunity to contribute to business strategy.

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There are many descriptions for dynamic pricing, but when simplified it is the ability to optimally adjust prices based on internal and external factors. Market demand, social sentiment, competitor prices, inventory availability, time of day, conversion rates, financial goals, and even the weather, are just some of the elements that retailers may incorporate into their pricing algorithms.

The “dynamic” adjective also relates to the increased frequency and automated nature with which retailers, primarily online, are able to update prices. For some this means multiple times a day (intra-day), even approaching real time for some products. But the key to successful dynamic pricing is knowing which prices to change, when, and by how much in order to win the customers’ business. Lest we forget in all this talk about being dynamic, a retailer’s ultimate goal is to increase sales and profit.

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The omni-channel impact

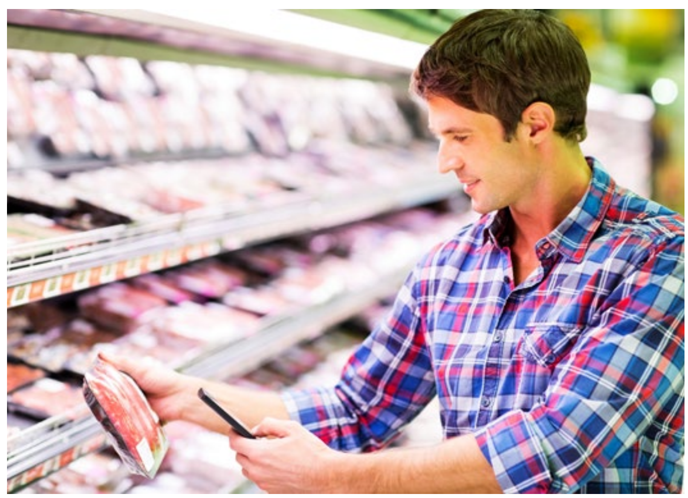
According to market research firm eMarketer, e-commerce sales will surpass the USD3.5 trillion mark within the next five years. The digital world is the principal venue for dynamic pricing, and yet physical stores are still predicted to account for 80–90 percent of total retail sales.

With recent advancements in electronic shelf edge label (ESL) technology, dynamic pricing may not be confined to an omni-channel retailer’s digital store in the near future. However, the mere thought of dynamic pricing in physical stores causes consternation among many retailers as they visualize prices changing before a consumer’s eyes at the shelf, or having the items they have in their shopping basket suddenly cost more than expected when they reach the checkout.

In reality, this is an unlikely scenario for in-store dynamic pricing. Retailers know adopting such an approach could turn loyal shoppers away in droves. In addition, legislation in some countries would prevent prices being increased while the store is open for trading.

It is also well documented and understood that changing prices in the brick and mortar world has historically been a manual, time consuming and costly chore. But with ESLs and a dynamic pricing system, there are situations where more frequent updates may make sound business sense and benefit customers.

For example, perishable produce that is nearing its "sell by" or "best before" date could be more easily repriced (marked down) throughout the week/day. Not only would this be financially beneficial to both retailer and consumers but would also help to reduce waste.



Online there are also many strategic scenarios for dynamic pricing beyond just staying competitive on key items — for example, inventory control. Products with high demand but limited availability could have their prices marginally increased and vice versa. And while we’re not talking about 50 percent price hikes but rather a few cents on the dollar, systematically and continually identifying these opportunities adds up.

Channel price coordination

A major strategy decision for omni-channel retailers is how or whether to coordinate prices across channels. Having the ability to dynamically adjust prices in store does not mean prices have to be matched across physical and digital channels, accelerating the proverbial race to the bottom. “Omni-channel is about delivering a personalized and consistent shopper experience including pricing. This means delivering the same price-value proposition online as in-store to the same shopper and vice versa (this does not mean delivering the same price to all shoppers across all channels),” says Jenn Markey, VP Marketing & Product Management at leading price intelligence vendor 360pi.

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Price coordination refers to a holistic set of capabilities that enable the design of pricing architectures within and across channels — this encompasses pricing relationships between products, pricing relationships for the same product across channels, and pricing relationships with respect to competitors. There are categories and products where a change in pricing (either in the store or online) has no impact on sales in the other channel, and other categories where a price change in one channel has a significant impact on another.

The similar is true of competitor price changes across categories and channels. As channels blur and retailers have multiple touch points with consumers, price coordination becomes essential — without a holistic omni-channel approach to dynamic pricing, the opportunity to create confusion (and discontent) in the marketplace with consumers is high.

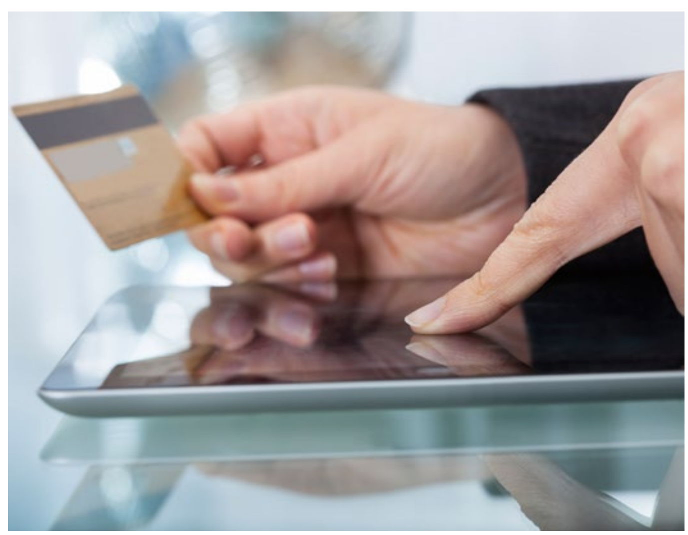
The dynamic pricing journey

Before diving headlong into dynamic pricing, it is important for retailers to have a clear pricing strategy, especially those with physical and digital channels. Without this foundation there can be unintended consequences, such as the aforementioned “race to the bottom” through naïve competitor matching, which can quickly and unnecessarily erode margins.

Retailers need ongoing access to a vast and growing ocean of data, the ability to quickly uncover insights and intelligence to inform pricing decisions, and the ability to execute changes on a "right time" basis.

Phase I – Timely, automated response

The first phase of implementing a dynamic pricing system should focus on enabling the organization for quick reaction to changes in market conditions, such as fluctuations in competitor prices or product demand.



By applying rules to competitive price information and other external data gathered in real-time, retailers can make price updates in line with their strategy whilst maintaining various brand, product line and other price relationships.

Once new prices are determined, these should be executed in real-time. While this sounds obvious, many retailers currently rely on legacy systems or manually publish prices. They need to focus on improving their price execution capabilities to effectively support dynamic pricing.

Unleash the power of data to intelligently inform decisions

This is where automation can help tremendously, especially with pricing analysts generally overwhelmed managing prices for thousands of products. However, any system should allow the pricing analyst to retain control, providing the ability to manually review prices of key products that are critical to the business while applying automation to intelligently price all other products.

Phase II – Data-driven, cross channel

Once an organization is enabled for timely, potentially intra-day, pricing, the next phase is to unleash the power of data to intelligently inform decisions. The first and most obvious data point is the price sensitivity of products. In addition to the impact on sales volume resulting from a price change, it is important to consider the price sensitivity with respect to major competitors (competitor elasticity). In other words, when various competitors adjust their prices how does it affect a retailer's own sales, and how does this vary by competitor and product?

As previously mentioned, for an omni-channel retailer cross-channel elasticities also play an important role. Products with high cross-channel elasticities could cannibalize sales in stores due to a price reduction in the online channel, and vice versa.

Pricing strategies should be designed to be competitive on key value items that are price sensitive while being aggressive with niche items that are less sensitive to price movements.

The inclusion of online behavioral metrics are also critical factors to include in any dynamic pricing solution.

The inclusion of online behavioral metrics such as page views, cart abandonment and conversion rates are also critical factors to include in any dynamic pricing solution. Automatic tracking of these metrics can signal changes in demand and provide retailers with key indicators that their pricing may be wrong; ideally, product groups are dynamically created to identify and address opportunities.

And these are not the only relevant metrics — other data including inventory levels (both a retailer's own and their competitors) can play a key role in the pricing process.

A retailer may decide not to follow a competitor and reduce the price on items that have limited stock available, for example.

With this plethora of data, retailers can leverage sophisticated science and optimization capabilities to help them dynamically determine optimal prices based on their business goals, which can vary for a category or a set of products.

Phase III – Cognitive pricing and promotions

The holy grail of dynamic pricing is achieved through the application of cognitive computing, a self-learning environment that "Understands, Reasons, and Learns" from inputs to intuitively determine the best prices and promotions for customers in context. This brings a unique advantage to even the most advanced retailers whose merchandising and marketing departments closely collaborate.

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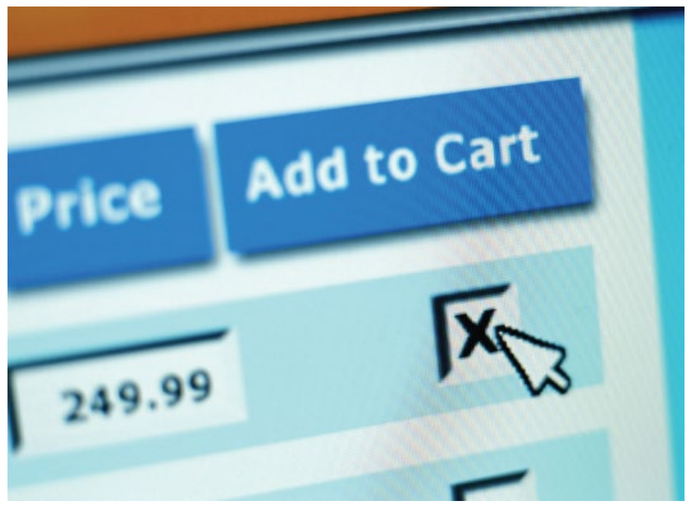
In addition to dynamically adjusting prices, retailers can optimize promotions for their customers. For example, when a customer is on the retailer's website various types of information including their past purchases, loyalty status, navigation sequence and other factors can be used to assess their propensity to buy. With this information a cognitive system can determine the most appropriate promotion for that unique customer at that point in time, in essence engineering a moment of serendipity.

How dynamic is your pricing?

As retail continues to reinvent itself so too do pricing strategies, processes and tools. From cost-plus pricing with infrequent updates using spreadsheets, and more automated management of pricing based on business rules, to the appliance of science and predictive analytics that identify optimal prices at scale.



Omni-channel and real-time, insight-driven dynamic pricing approaches build on this, as we move rapidly towards cognitive pricing methods.

But one thing remains constant—the importance of pricing. In a world of cool mobile technologies and digital stores, getting prices right is critical and still one of the biggest levers retailers can use to drive profit.

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Not all retailers will be at the same phase of the dynamic pricing journey, but those who move up the curve quickly will have a significant competitive advantage over their peers. These will be the retailers that leverage science and analytics to inform their pricing decisions with insights gleaned from a multitude of data sources.

They will do this in an automated, dynamic and timely manner, coordinated effectively across channels. They will attract and retain the loyalty of their customers, and be the financial and market share winners in the hyper-competitive retail environment.

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IBM Corporation
IBM Commerce
Route 100
Somers, NY 10589

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