IBM Commerce
Thought Leadership White Paper

Best practices in implementing omni-channel pricing solutions

Overview

Many retailers that have deployed IBM®'s omni-channel pricing solutions and followed our best practices approach to implementation have achieved better price image, clearer insight into impact of pricing changes, alignment between strategy and action and time saving automation.

Best practice #1: cleansing your data

Part of the process of implementing a pricing solution involves cleansing data so that you get better results. While laborious, this process offers many benefits. Most retailers feel that they have some minor data issues, but feel good overall about the state of their data. However, price optimization implementations almost always highlight previously hidden data issues such as missing size information, the wrong product families, and incorrect cost information. Each data issue can cost a retailer money. For example, when one retailer first loaded its data, IBM's solutions helped uncover a Known Value Item (KVI) with the wrong competitive data. The company the retailer used to check its competition had recorded a promotional price instead of a base price. With the retailer's legacy system, the retailer would have matched that low price and lost a lot of money. IBM reports showed competitive outliers to make sure that did not happen anymore. The retailer also used IBM's solutions to set up pricing rules so that if any bad competitive data were to slip through, no price would fall below cost. Many retailers consider data cleansing part of the price you have to pay to deploy price optimization. This is true, but when evaluating this cost, you want to make sure you take into account the extended benefits of running your business on accurate data.
(Hidden benefit: running your business on accurate data.)

Best practice #2: align strategy and execution

A key process in implementing pricing solutions is mapping category roles with the intent and goals for the category. Many retailers have formal category role names, such as "traffic builder," "profit generator" and "convenience." These goals usually map neatly into the optimization goals built into IBM's solutions, such as "maximize profit," "maximize revenue" or "maximize volume." However, for some retailers, how each category is aligned with a category role is sometimes an open question. Often, much of this information is stored only in managers' heads, stashed away in research studies, or hidden in presentation slides. The implementation process can act as a catalyst to align category managers and pricing managers with the role of each category to help ensure that each merchant is "singing from the same songbook."
(Hidden benefit: increase business alignment by providing an opportunity to articulate strategic objectives.)

Best practice #3: give merchants more freedom

The IBM omni-channel pricing solutions are designed to help retailers achieve goals such as dramatically increasing profit while constraining prices by a series of prioritized rules, including competitive rules, omni-channel rules, allowable last digit rules, line price rules and price zone rules. Often, retailers can translate the pricing rules from their legacy systems into rules in the IBM solution because these rules are written in plain, everyday English with a fill-in-the-blanks structure. The sheer number of rules in the rules library also provides retailers with greater flexibility and more granularity in pricing scenarios than was previously possible. For pricing teams, this new power and flexibility also provides them with the

opportunity to step back and think more strategically about their approach to pricing across both physical and digital channels. Many pricing analysts find that they no longer need to make compromises in their pricing strategies, and are now free to investigate new pricing tactics.
(Hidden benefit: a more flexible pricing tool empowers retailers to use pricing more strategically to achieve goals.)

Best practice #4: use a single system for managing prices across channels

Today the majority of leading retailers are multichannel, selling merchandise through both physical and digital stores, but most are using different pricing processes, systems and teams. Historically retailers created a separate online channel so as not to disrupt their existing brick and mortar business. However, in the current omni-channel world of retailing, where price transparency is the norm, and shoppers can start their path to purchase in one channel and complete in another, having a disconnected and uncoordinated approach to omni-channel pricing raises a number of questions and challenges for retailers including:

1. How to deliver coordinated and/or consistent pricing across all channels
2. How to understand if price changes in one channel will negatively affect (cannibalize) sales in another
3. How to identify the relative importance of competitors, by category and channel
4. Knowing whether to take action in any of their channels when a competitor changes prices online. As not all price changes by all competitors in all categories and channels will have the same impact, which ones should be ignored?

With IBM retailers can adopt a true omni-channel pricing approach and system, one which allows them to use data and insights from one channel to intelligently inform decisions in another. Using a single solution retailers can maximize sales, profit and shopper loyalty by coordinating pricing across channels, dynamically and intelligently reacting to competitor and market changes.
(Hidden benefit: delivering coordinated and synchronized pricing across all channels drives customer loyalty, in addition to sales and margin improvements.)

Best practice #5: take on the competition without going head-to-head on price

Some retailers follow fairly simple, rigid, competitive pricing strategies. For example, they would match the price of image items with their strongest competitors in each zone or channel, and price other items within 20 percent of the competition. While this type of approach can be easier to implement, it often limits flexibility and essentially allows competitors to dictate prices. IBM's solutions allow retailers to take a more sophisticated approach to help them to achieve margin goals and simultaneously become more competitive on price.
For example, a retailer could use volume-weighted CPI (Competitive Price Index) rules to stay within 10 percent of its competition at the category level. The flexibility of volume-weighting allows the optimization engine to bring individual item prices above or below this 10 percent collar to improve margin, and at the same time, maintain greater competitiveness for the category as a whole. In many cases, retailers that originally planned to retain their existing CPI strategy prior to using the IBM solution, later realized the power of IBM's volume-weighted CPI rules and made them a core part of their competitive pricing strategy. And now IBM's solution includes awareness of omni-channel competitive pricing, including online.
(Hidden benefit: increased competitiveness without sacrificing margin.)

Best practice #6: understand price elasticities

Before choosing IBM, retailers' pricing teams may have had some understanding of the price elasticities of their categories through third party research, but most had little understanding of the elasticities of each item. Merchants usually were aware of common cross-elasticity effects with some of their items, such as the sale of hotdogs driving the sale of buns, but this kind of knowledge often did not factor into their decisions. A better understanding of cross-elasticity effects can help improve pricing strategies. Today, with a single click, IBM customers can graphically view how a change in the price of each item could affect unit volume, revenue and profit for the item and the line. This capability not only allows merchants to quickly understand how elastic an item is in order to make better pricing decisions, merchants can also incorporate this capability in making other decisions, such as which items in a line should be slated to appear in a flyer or on an endcap. With IBM, virtually all of a merchant's different pricing scenarios can incorporate cross-elasticity effects. The solutions offer retailers a more granular and precise understanding of shopper behavior that can give them a competitive edge.
(Hidden benefit: gaining a clear understanding of price elasticities provides insight into consumer behavior that allows retailers to make better decisions and more accurate forecasts across the board.)

Best practice #7: make pricing analysts a strategic resource to merchants

At the beginning of a pricing project, buyers and category managers sometimes have concerns that their experience will somehow become less valued, and that they might lose power or control to the newly empowered pricing team with its new solution. In general what we have seen is that category managers retain overall authority for the strategy and prices in a category, and are now able to rely on pricing managers to develop alternative scenarios for them to consider and review.

Within the pricing team, there is often a shift in the required skill set. Before implementing IBM pricing analysts have typically spent a large portion of their time performing administrative and clerical tasks. With the implementation of an omni-channel pricing or price optimization solution, many of these traditional tasks are eliminated, freeing up pricing analysts to focus on conducting and interpreting analyses. Time and again, we have seen that pricing team members may also feel that their role is more satisfying and rewarding post-deployment.
(Hidden benefit: because pricing is a more strategic function within an organization, members of the pricing team typically have higher job satisfaction, and can do more in less time.)

Best practice #8: tame the "domino effect" in price changes

Price maintenance is a challenge at most retailers, even when prices are relatively stable. A manufacturer's price advance is like a snowball touching off an avalanche. A cost increase on one item could affect the price of the entire line. This could then misalign size relationships since a retailer could now be charging more per ounce for larger sizes than smaller ones. Then, the carefully structured price gaps of a retailer's good-better-best price tiers could be altered. It often does not take much to set off a chain reaction. Add in the effects of ecommerce and the connected shopper and things can become even more complex. IBM consultants work closely with merchants to configure their solutions' price maintenance capabilities. Rather than bluntly setting the maximum number of price changes that could occur in a given week, the combined team works together to set individual and cumulative thresholds to dictate what criteria will trigger price changes in store or online.

IBM's solutions also provide merchants with advanced capabilities to selectively override price recommendations and help them understand the impact of choosing not to approve a suggested price change. Some members of a pricing team may initially be skeptical about some of the early price change recommendations the system suggests, but they quickly come to trust and rely on these recommendations once they see what sparked a recommendation and what the impact could be on the overall category.
(Hidden benefit: better ability to evaluate the impact of pricing changes and when and how often to make them.)

Best practice #9: measuring success

"How do we know that the system is working?" As retailers evaluate pricing solutions, this question comes up repeatedly. Some retailers consider taking a test and control approach for pricing in their stores, but many ultimately decide that this is a time consuming, expensive and flawed approach. They often decide that they do not have the resources, and sometimes believe that they would have trouble creating a credible control group given the nature of their competition. Instead of test and control methodologies many retailers depend on IBM's pricing solutions, which provide a comperehensive, statistical decomposition of historical volume by isolating base volume, seasonality and incremental lift from pricing and merchandising tactics.
Not only does this approach help document success, but routinely tracking success can also help identify when you have gone off course and need to re-optimize a category. The results provided by this capability allow you to improve your performance, and are key in maintaining executive support and building confidence in a project.
(Hidden benefit: improved results by routinely tracking and course-correcting.)

Summary

The improvements most retailers see in revenue, volume, margin and price image have been well documented, but the value retailers see in improving their processes and improving efficiency are equally valuable to many retailers. This whitepaper highlights many of the common benefits associated with an implementation, but each retailer also sees its own unique sources of value.

About IBM Commerce

IBM Commerce enables clients to uncover and realize new, sometimes hidden, growth and efficiency opportunities by infusing intelligence and context into key processes across the commerce cycle. Our market leading products and services help organizations orient their entire business around the customer from procurement to supply management, to marketing, merchandising, eCommerce, payments and customer analytics. Differentiated by deep industry expertise and service capabilities, we help our clients create value as they engage with their customers, partners and suppliers. This is the power of IBM Commerce.

For more information

To learn more about IBM's Omni-Channel Merchandising solutions, please contact your IBM representative or IBM Business Partner, or visit the following website: **ibm.com**/merchandising.

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