ATKEARNEY

“No Insult” Pricing and Promotions

A smarter approach to winning back value-conscious retail customers

Savvy shoppers know how to get the best deals and savvy retailers know how to create these deals while still turning a healthy profit. But the relentless push by value retailers such as Wal-Mart and Costco means the days of straightforward pricing and promotions tactics are gone. Instead, retailers must begin crafting strategies that build on existing pricing techniques and focus more on meeting customers' needs and desires. The potential reward—regaining lost customers and attracting new ones—is well worth the effort.

Much has been written about today's value-conscious shoppers and how they are flocking to value retailers such as Wal-Mart and Costco. Penetration and market share of superstores and club stores have increased significantly across most segments—electronics, toys and especially grocery. Over the past several years, superstores saw their annual sales rise by more than 20 percent in the grocery, consumables and pharmacy categories; over the same period, traditional supermarkets saw only a minimal annual increase.[1] Supermarkets are rapidly losing customers, especially for stock-up items and products generally located in middle aisles. More than 95 percent of consumers shop four or more store formats annually, and for some categories, more than 70 percent say they regularly shop two or more formats.[2]

While these numbers clearly denote discount-seeking behavior, are they a symptom of a fundamental shift in shopping needs? We don't think so. Consumers have always been value conscious; shoppers crave the excitement of bargains and periodic promotions. From department stores to supermarkets, the entire retail industry thrives on "sale" events, especially during the holidays. Supermarkets have long used weekly ads to lure customers into stores, enticing them with promotions on select brands and counting on them to fill their baskets with non-promotional items as well. Sale prices were, in fact, a key driver of a supermarket's favorable price image, making the weekly circular the cornerstone of a competitive strategy.

However, faced with price competition from Wal-Mart and other value retailers, traditional mass marketing and "high-low" promotions strategies have not been successful—even with a more aggressive focus on price. In fact, retailers' aggressive price responses turned into a vicious cycle

[1] *A.T. Kearney research*

[2] *Information Resources, Inc. and A.T. Kearney analysis*

in which ever-lower promotional prices fail to improve market share, with base prices rising to allow for the promotional losses.

Some retailers abandoned their high-low strategies and instead embraced an everyday low-price strategy, only to realize that lowering base prices didn't lead to a large enough increase in volume, at least not enough to offset the lost margin.

Having little success with these traditional strategies, retailers are struggling to understand how, if at all, they can use everyday pricing and promotions to improve their price image and competitive position in each product category.

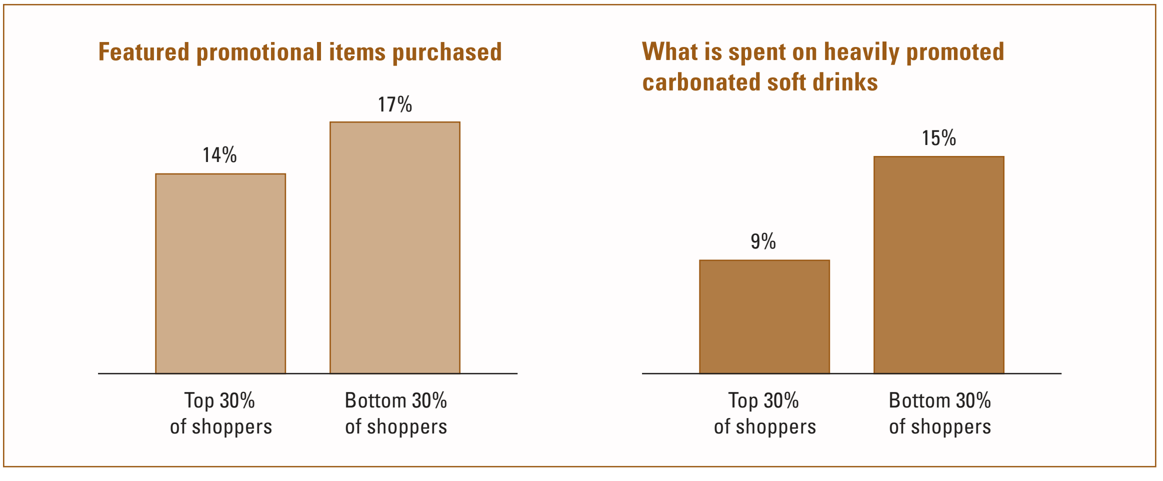
This paper discusses A.T. Kearney's approach to pricing and promotion. We offer a customer-focused approach in which retailers identify and exploit the items most important to customers—items that will help build and sustain a positive price image. It is a rigorous strategy that builds on retailers' experience and historic perspective on pricing and offers help in making better, fact-based and timely pricing decisions. It also acknowledges that shoppers know how get to the best deal; shying from slick promotional activities, this is the "no-insult" approach to pricing.

Weekly Promotions. There Must Be a Better Way

If consumers have always been value conscious, and retailers have responded to growing price competition by offering aggressive discounts, why are supermarkets losing market share so rapidly? Why are retailers that offer weekly promotions—for example, office products and electronics superstores—also being pressured by value retailers with different pricing and promotion strategies?

The answer to both questions is that consumers have changed how they shop for value *(see side-*

Figure 1
Promotional shopping behavior by customer segment*



** Segments divided into top-three and bottom-three deciles based on purchases, frequency and profitability*

Source: A.T. Kearney

bar: What's It Worth?). With easy and widespread access to alternate channels offering the same brands at cheaper prices, consumers are cleverly splitting their purchases. For each type of shopping trip, shoppers look for, and can now find, the channel that provides most value. For example, people go to superstores or club stores such as Sam's Club or Costco to stock up on staple items rather than wait for their favorite brands to go on sale at the neighborhood supermarket. For convenience shopping, more people go to the nearby drugstore chain rather than the more expensive gas-station marts.

As a result, many retailers are stuck in the middle, attracting more consumers who are on fill-in or bargain-hunting shopping trips. These consumers, having already loaded their cupboards and filled their closets with items from a superstore, will then take advantage of an attractive promotion if it happens to coincide with their weekly shopping trip. This "cherry-picking" behavior is becoming increasingly prevalent, with a growing number of sales coming from promotional items. Indeed, traditional grocers admit that they sell 50 percent or more of their top nonperishable categories via discounts or coupons.

But what about retailers' most loyal shoppers? These are the ones who, after selecting several front-page sale items, fill a greater portion of their shopping carts with the more profitable, regular-priced items *(see figure 1)*. Unhappily, this primary segment of shoppers is also shrinking the fastest due to competition from discounters. Simultaneously, retailers are seeing their "occasional" customers grow at 5 percent or more. Figure 2 illustrates the behavioral changes of grocery shoppers following the opening of a new Wal-Mart. As a result, many grocery stores are

Figure 2

Changes in weekly averages after a nearby Wal-Mart opening*

	Number of transactions	Number of customers per segment	Average value of market basket	Number of units per market basket	Number of transactions per week
Primary shoppers	**–16%**	**–22%**	**–5%**	**–15%**	**7%**
Secondary shoppers	–5%	–10%	8%	-5%	6%
Occasional shoppers	**8%**	**5%**	**4%**	**8%**	**2%**
Non-loyalty card holders	–2%	n/a	n/a	–4%	n/a
Total	–2%	–3%	–1%	–3%	2%

** Data samples taken three months prior to and three months after a Wal-Mart opening in the market for 15 stores across the United States*

Source: A.T. Kearney

becoming little more than 50,000-square-foot convenience stores for occasional customers.

Clearly, weekly discounts alone, no matter how attractive, are not the way to create a positive price image. In conducting a shopper survey, one regional retailer found that despite receiving consistently high ratings on its promotional prices, its ratings on "overall price and value" declined substantially. Failure to recognize the importance of everyday prices to their price image has sent many retailers into a vicious cycle of declining share and margins: raising prices to offset the profit pressure from aggressive promotions and, ultimately, further damaging their price image.

Switching to an everyday low pricing strategy without combining it with an aggressive communications plan to attract new shoppers **will result in little more than giving away margin to existing customers.**

Smarter Is Better

It's no secret that value retailers use variations of an everyday low-price strategy to create a positive price image with shoppers. But is this image also the result of having the lowest prices across the board? Do people shop at Wal-Mart to get lower-priced products on everything they buy? Not necessarily.

Our analysis shows that value retailers do more than offer low prices—they follow a smarter and more targeted pricing strategy. They identify and aggressively price the brands and items that the largest segment of shoppers care about and are likely to remember. For example, Wal-Mart may be the price leader on diapers—the jumbo pack of the leading Pampers brand goes for just US$9.49—but isn't on Enfamil baby formula. Yet people who arrive for the great deal on Pampers also buy the Enfamil formula.

To improve their price image among shoppers, most value retailers follow a five-pronged pricing strategy:

- Offer attractive prices on image-enhancing brands and items
- Create opening price points in each category, sometimes through private-label brands
- Appeal to shoppers' "treasure hunting" mindset by establishing a highly visible discount price on a unique or limited item
- Offer large sizes and value packs
- Communicate an everyday low price to establish price credibility

If we follow this line of thinking, it would seem that everyday low price (EDLP) is the right strategy for repairing some retailers' damaged price reputations. However, an EDLP strategy is both expensive and risky, and not necessarily the fastest remedy. Even Wal-Mart cannot fully deny the importance of "high-low" pricing. When Wal-Mart recently backed away from its traditionally steep discounts the day after U.S. Thanksgiving, it felt a quick backlash from frugal consumers and reversed course.[3]

Indeed, while price image can be damaged in just one shopping trip, regaining traffic, trust and loyalty takes far longer. Switching to an EDLP strategy without combining it with an aggressive communications plan to attract new shoppers will result in little more than giving away margin to existing customers. Several years ago, both Kmart and Sears learned firsthand that a quick switch from a high-low promotion strategy to EDLP could be costly. Neither retailer developed the right communication program or differentiation to drive incremental volume once promotions lapsed; nor did they have the cost structure to support their reduced margins.

Additionally, pricing is just one component of a retailer's value proposition. To compete effectively, traditional retailers must combine pricing with other factors—location, service and assortment, for instance—appealing to targeted customer segments and differentiating their stores from the value retailers *(see figure 3 on page 6).*

For now at least, rather than adopting an EDLP strategy, traditional high-low retailers should realign their pricing and promotions strategy to focus on the customer.

A.T. Kearney's Approach to Pricing And Promotion

The ideal pricing and promotion strategy offers "fair and honest" everyday pricing on the products

What's It Worth?

On the surface, value is a subjective concept at best and impossibly vague at worst. The process of determining and articulating it is the largest hurdle in creating a pricing strategy. Consider the predicament: If the seller cannot fully identify the value that its product or service brings to its customers, the set price will inevitably be off mark. If the customer is not familiar with the offering or its value, and is not given a clear and compelling case for its return on investment, a sale is unlikely.

There is a way to overcome these pricing obstacles. It requires an unwavering focus on three key principles, which together form the basis for an effective value-based pricing strategy.

Value must be defined from the buyer's point of view, not the seller's. Rather than overemphasizing the features of a product, focus instead on the hard and soft benefits that the customer perceives. A vacuum cleaner's extended hose feature is not the selling point, it is what the customer can do with the feature—in this case, reach into the corners of a ceiling to clear out cobwebs.

The value of the offering must be clearly superior to that of alternatives. If not, the price will end up being set either by your least sophisticated or your most aggressive competitor. The implication is that if a company cannot meaningfully differentiate its products and services, it is unlikely to be able to put a price on their value.

All sources of value must be uncovered and communicated to customers. Only then can you effectively estimate, quantify and communicate how a product or service is going to benefit a specific customer.

When combined, these three principles are the foundation for A.T. Kearney's value-based pricing strategy. The entire strategy is outlined in "Finding New Answers to the Pricing Question," a business issue paper available at www.atkearney.com.

[3] The Wall Street Journal, *13 December 2004.*

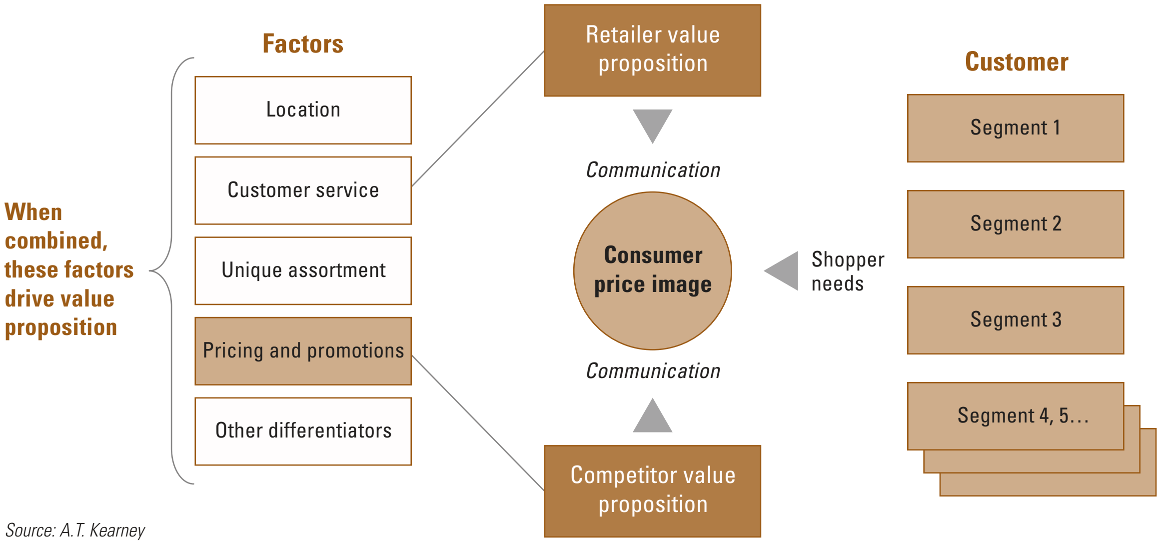
that matter most to consumers, while maintaining the use of promotions to drive traffic and expand categories. In other words, focus first on consumers and then on competitor activity. In our work with several high-low retailers we developed a customer-focused approach: All pricing and promotions decisions are initiated by identifying price-image drivers and then implemented with a coordinated pricing and promotions plan *(see figure 4)*. The approach includes robust analysis and modeling, and is supported by an integrated organization, effective execution and continuous measurement.

Initial results have been positive. Real sales growth at one retailer ranged between 3 and 4 percent with a 5 to 6 percent increase in profits—this translated to a 200 basis point improvement in margins across 30 categories.

The following offers a brief overview of our pricing and promotions approach. It blends strategic pricing elements favored by value retailers with strategies that promotional retailers use to communicate their unique value:

1. Determine what drives price image. Knowing what drives price image begins with gaining a better understanding of shoppers' behavior: analyzing the frequency of consumer purchases, household penetration, responsiveness to price changes and promotions (elasticity) and the propensity for brand switching. This quantitative analysis becomes the basis for classifying categories, brands and SKUs according to shopping patterns. Kleenex facial tissue, for example, ranks among the top 50 items for household penetration and the top 100 for purchase frequency. It also has a high promotion response and return on investment (US$0.99 for US$0.89), and low cross-category elasticity in the premium segment.

Figure 3
What drives consumer price perception?



Source: A.T. Kearney

Research suggests that laundry products, paper goods, carbonated soft drinks, cereal and several other items attract shoppers to a store. This helps explain the market share erosion of supermarkets by superstores and club stores, which use aggressive pricing strategies and prominent in-store displays to sell these products.

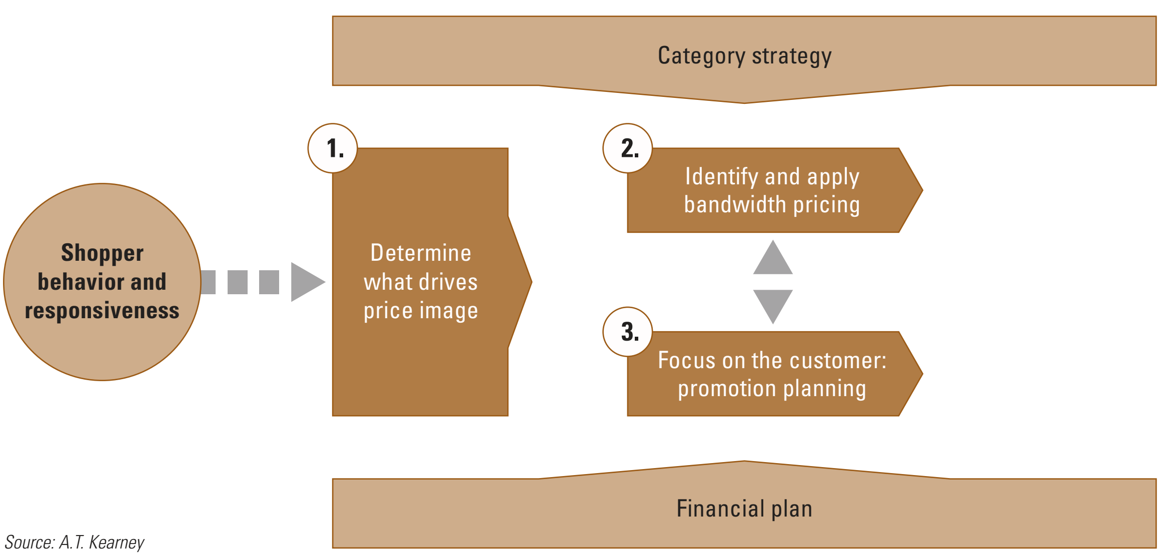
Because consumers comparison shop, they do not perceive all brands and items the same way within a category. Therefore, retailers must identify "known-value" items—those that are purchased frequently across outlets and are recognizably higher or lower in price relative to a consumer's previous shopping experiences. Consumer demand for these items can be highly elastic, while demand for items that consumers do not compare across outlets—impulse purchases, incomparable goods or harder-to-find items—is relatively inelastic.

To identify known-value items, retailers perform an in-depth evaluation of consumers' shopping behavior, both in their own stores and when they go to other stores and channels. This is where the quantitative techniques mentioned earlier come in.

Consider Best Buy, which targets high-opportunity shoppers at home and at the point of sale. Desirable shoppers are classified into five distinct groups: upper-income men, suburban mothers, small-business owners, young family men and technology enthusiasts. Based on demographic analysis, stores are clustered to target a few segments through tailored merchandising, promotions and services.

Retailers must also measure qualitative factors such as health and wellness trends and the popularity of new items. Armed with solid data and insights, they can identify and reward their best

Figure 4
A.T. Kearney pricing and promotions plan



Source: A.T. Kearney

Building Loyalty at the Store Level

Despite the many discussions about identifying individual shoppers or micro-segments of customers and then devising targeting strategies to meet their needs, very few success stories exist in retail. The retailers that have succeeded in generating sales have not always driven bottom-line results or sustained loyalty. Up to 70 percent of chains offer loyalty cards and collect valuable information, but most of it isn't used—cards have simply become discount vehicles, with an average consumer owning two or more competitors' cards.

Fortunately, things are changing. A recent analysis of shoppers at a large U.S.-based retailer found that of the top 30 percent of shoppers (those who spend up to US$5,000 per year and visit at least once a week), 15 percent did not buy anything in the paper aisle (bath tissue, paper towels), and more than 50 percent spent less than the average in this category *(see figure)*. Through this analysis, the retailer obtained a quick, yet powerful, opportunity to target these shoppers with special promotions. In doing so, it increased share in the category, improved store loyalty and discouraged the purchase of at least one item from a competitor club store.

The following are four ways to increase loyalty at the store level:

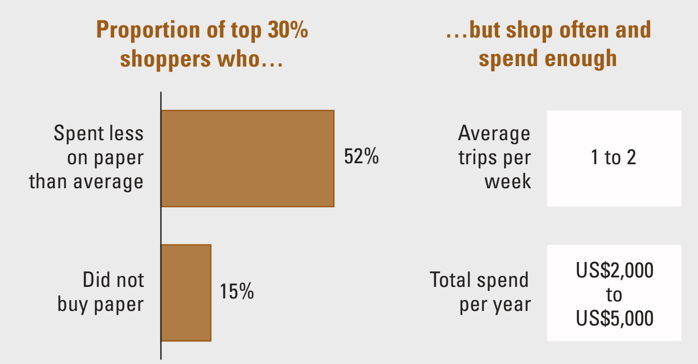
Identify and target loyal consumers. Evaluate shopper baskets for gaps and affinities that can be quickly filled. Find the 20 to 30 percent of unprofitable shoppers who typically fill 80 percent or more of their basket with price deals.

Take a cross-category, total-store view. Most of the so-called targeted promotions focus on a brand manufacturer's coupon. While this benefits a brand in the short term, loyalty to a retailer is solidified through category or store-level promotions.

Incorporate all aspects of merchandising and marketing, not just discounts. Make targeted promotions and pricing a part of an overall loyalty marketing program that includes tailored assortments, services and other rewards. Identifying shoppers by spend level can be effective in building loyalty, but only when rewards are significant and tailored to meet their needs.

Empower managers and associates at the store level. The store is where it all comes together. Associates should be trained to serve the desirable shoppers and build trust and loyalty. For example, Best Buy trains its associates to identify desirable customers through observation and a quick interview. The target customers then receive shopping assistance and services that are not available to everyone.

Identifying and targeting consumers who "skip the aisle"



Benefit potential from targeting these shoppers: 3% sales increase, 0.4% profit increase

Source: A.T. Kearney

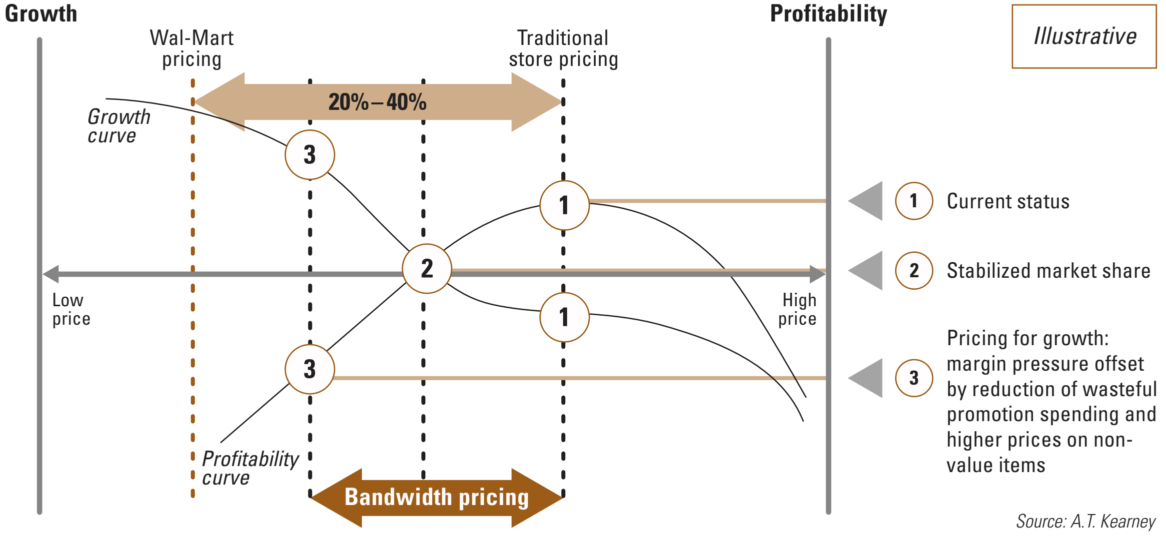
shoppers, and cultivate those who spend more *(see sidebar: Building Loyalty at the Store Level).* For example, Best Buy invests in promotions targeted at its most loyal and profitable customers. Similarly, British grocer Tesco offers US$0.50 off certain products to specific loyal shoppers, estimating the value of motivating its regular shoppers to try new departments at almost US$3.7 billion.

Also, these same insights can help discourage unprofitable shoppers. Best Buy, for example, charges a restocking fee for returned merchandise to those customers who buy on rebates or distressed prices and then return the merchandise or sell it on eBay. The retailer is also experimenting with selling its "open-box" items online.

2. Identify and Apply Bandwidth Pricing. The normal shelf price of "known value items" plays an important role in driving price image. As discussed earlier, this does not necessarily mean dropping prices on known value items to match cross-channel competitors. Rather, it means the price must be within an acceptable price "bandwidth" *(see figure 5)*. Prices within this bandwidth help support an image of fair-and-honest pricing and encourages consumers to buy at your store rather than make a trip to a discounter. Retailers can reinforce this image of fair value through promotions that also generate excitement and support the impression that their stores offer good value every day and a great value on special occasions.

Items that are unique or generate excitement but do not drive consumers' price perceptions can be profitably priced according to affordability and demand elasticity. Raising the price on such items, if they are currently priced lower than necessary, can generate enough margin gains to help offset margin losses on known-value items. This was the

Figure 5
Bandwidth pricing methodology (profitability and growth curves)



Source: A.T. Kearney

lesson learned by a regional retailer that applied a bandwidth pricing methodology. The retailer optimized its typical pricing on four key categories by reducing prices on almost 80 image-driving items and increasing prices, within acceptable bands, on about 560 other items. The result was a 1 percent increase in profits, a break-even on sales and a marginal reduction in volume. In the long term, the retailer increased its market share by reversing its negative price image.

A proven strategy is to offer an attractive opening price point in each category, which is often accomplished by aggressively pricing a quality private-label product. For example, Wal-Mart's advertising of a DVD player at less than US$40 and a 23" LCD TV at US$898 creates a good price image for the retailer in consumer electronics. In both cases, the products were not national brands, but relatively unknown Asian brands, which behaved as private labels in the category.

Private-label pricing is a critical component of an overall pricing strategy. Traditional pricing on private-label items has followed a simple 10 to 15 percent average differential against targeted national brands. A complication here, faced by many retailers, is the deep and frequent promotions on certain national brands. For example, when a department store puts its name-brand hats on promotion, the competing private-label hats suddenly look expensive, although they're technically priced at a discount. An ongoing debate among pricing experts is whether "price shielding" is required in such cases—whether the private label should be priced lower than the discounted national brand for the duration of the promotion.

> The ideal pricing and promotion strategy offers **"fair and honest" everyday pricing on the products that matter most to consumers,** while maintaining the use of promotions to drive traffic and expand categories.

In our experience, answering the price-shielding questions requires establishing pricing rules for three distinct situations. The first is categories in which a targeted national brand is on promotion as frequently as the consumer purchase cycle. A shopper who knows 3M's Scotch Tape goes on sale once a month at Staples waits for the sale price. The rule for this situation is to price the private-label item relative to the promotional price of the national brand. The second situation applies to national-brand promotions that appear less frequently than the purchase cycle: Price shielding is appropriate, but only for promotions that last longer than one week. Finally, price shielding is unnecessary when brand promotions are less frequent than the purchase cycle and the private-label brand enjoys high penetration and consumer loyalty.

To fine-tune these rules, we recommend applying a penetration strategy to all target items. The retailer adjusts the acceptable price band relative to the national brand based on these targets—the band is wider for items with a more aggressive penetration goal and smaller for those with a more conservative goal.

Finally, communication is key. To reverse a negative image or regain lost customers, retailers must effectively communicate any broad price restructuring. Examples of good communication strategies include some rather creative methods, such as sending a personal video message from a company president to shoppers, and more mainstream options, such as weekly circulars, in-store signs, and targeted emails and mailings. The financial impact of a good communications strategy far outweighs its costs.

Best Practices in Pricing and Promotion

A large retailer, burdened by a negative price perception and declining market share, tended to apply a similar pricing and promotion strategy to not-so-similar products. For example, a traffic-building brand received the same treatment as popular brands. The retailer averaged between 98 and 102 percent on a weighted index compared to target-competitor prices. On popular brands, the retailer was typically overpriced by 10 percent or more, and underpriced on less-popular brands (those that did not drive price image). And more than 50 percent of the retailer's target competitors in each price zone were unconnected to where the chain consumers cross-shopped the most.

The retailer spent 5 to 10 percent of its gross sales on weekly promotions—partially funded by manufacturers—but many of these discounts were ineffective. Consumers were either uninterested in the product or the discounts were cannibalized by other brands. For example, over a 52-week period, the retailer offered five promotions on a premium product. When measured, two of the five promotions showed a negative ROI (return on investment) on the category and there was minimal impact on consumer traffic or basket size.

While this presents a classic example of what not to do in retailing, top retailers stay focused on consumers and exhibit four best practices:

Consumer-focused strategy. Pricing and promotions are determined by category roles and strategies and driven by consumer behavior. High-low retailers understand which brands and items drive price image.

Planning and measurement. Consumer impact and ROI of promotions are consistently measured and incorporated into the planning process. Promotions aren't driven by past experience and manufacturer recommendations, nor are they always motivated by meeting quarterly target numbers. Retailers that use appropriate incentives are able to drive customer-focused and profitable promotions.

Integrate organization and decisions. The best pricing and promotion strategies combine the talents of both pricing and category managers. The pricing department shares information on market baskets compared to competitors; category managers plan promotions by engaging the pricing group. And advertising zones and pricing zones are fully aligned.

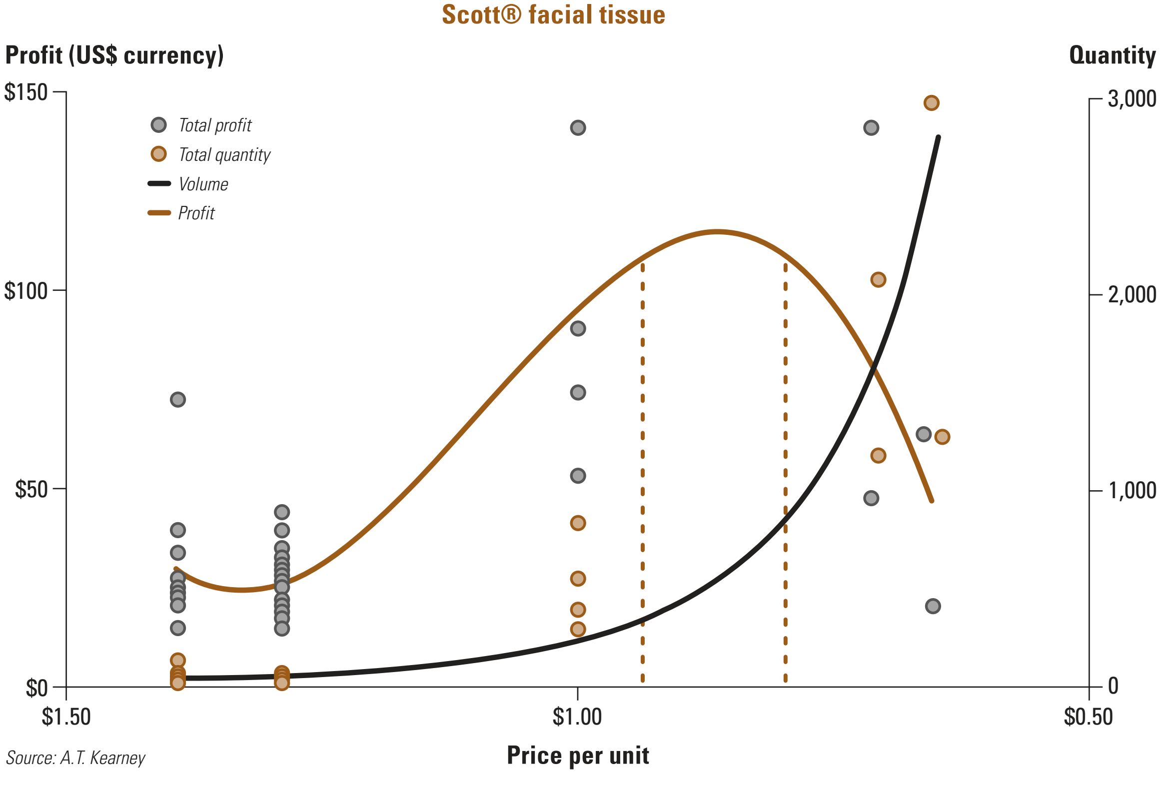
Execute at the store level. Price changes and promotion plans are well communicated and compliance is consistent across all stores.

3. Focus on the customer: The art of promotions management. After all these years, promotions are still a viable competitive tool. Many shoppers still use their weekly circulars to plan their shopping lists and trips. Retailers that get their promotions right will benefit from higher traffic, sales and profitability—and a better overall image. But getting it right is more difficult than it sounds *(see sidebar: Best Practices in Pricing and Promotion)*.

Consider the challenge: Promotions management requires numerous decisions to promote thousands of items across the store. No matter what sellers of modeling software may promise, the many variables and thousands of items in a typical store result in millions of combinations and possible outcomes. It is a complex undertaking that becomes even more complex when retailers do not have data on variables such as displays, store-compliance statistics and competitive promotions.

Success in promotion planning depends on developing a practical understanding of consumer behavior and responsiveness, and then using this understanding to identify systemic and manageable patterns. For example, matches from a drug-

Figure 6
Price point elasticity



Source: A.T. Kearney

store will light the candles on your birthday cake and cost nothing; a US$1.49 plastic BIC lighter will do the same; so will a sleek US$70 Colibri piezoelectric lighter. Each offers a similar degree of practical utility, but each also has a very different value to the consumer.

Based on our work with several retailers, we've developed a five-dimensional framework to improve promotions management at the category level:

What to promote? Knowing what your target shoppers care about must be incorporated into promotion planning. Once you know how specific items rank in terms of consumer preference and their ability to drive price image, the information should be used in determining category-, brand- and item-level roles, which drive pricing and promotion strategies. Generally, brands that drive price image and encourage higher store traffic should feature prominently in promotions.

Why do they buy? Understanding how consumers shop the categories, the successive choices they make and their switching behavior among brands is critical to determining the sequence and depth of brand promotions. For example, an analysis of loyalty-card data at a major retailer revealed that 63 percent of consumers who buy Scott facial tissues also buy Kleenex tissues. Not only should the two brands not be promoted in the same week, they should not be promoted in successive weeks given the stock-up effect.

How deep to promote? Consumers' reactions to previous promotions can predict how they will behave in the future, assuming enough history exists and a reasonable pattern can be established. The goal is to establish consumer responsiveness and elasticity. This is where statistical analysis can help. Figure 6 shows the elasticity analysis of promotions and the corresponding volume and profit of different price points. Combined with the role of a brand or item, retailers can make an informed decision for the desired volume-to-profit tradeoff on each item. In figure 6, for example, the retailer has to determine if Scott facial tissues drive enough traffic or consumer interest to warrant promotions that fall outside the maximum-profit zone.

Success in promotions planning depends on **developing a practical understanding of consumer behavior and responsiveness,** and then using this understanding to identify systemic and manageable patterns.

How often to promote? The timing of previous promotions in a category can result in consumers being taken "out of the market" for a product. Purchase cycles can also help define the duration of the promotional event. For example, an analysis of one retailer's extended promotional program showed that a 13-week promotion was too long for many categories. There was high impact early, and again toward the end of the 13 weeks. In between, there was a trough of demand as shoppers consumed the items they purchased at the beginning of the event. A more effective strategy would be to hold two shorter promotions separated by the average consumption cycle.

When to promote? Some categories have significant seasonal patterns, but even when the patterns are less dramatic they should still be exploited. For instance, the price of airline tickets changes as the scheduled take-off time approaches and gasoline prices along highways vary over the course of a week. In retail, many consumers time their stock-up purchases at the beginning of each month to coincide with the arrival of their paychecks. Understanding this window, and timing the promotions of key image brands or those with positive promotion ROIs to coincide with it, can lead to significant benefits.

When applying the five dimensions, companies should also keep in mind additional insights on promotion strategies. For example, promotions that last longer than a week have, on average, a greater ROI for the entire period, while promotions that last longer than four weeks show a sharp drop in sales and ROI, especially in categories that have a six-week or longer purchase cycle.

Features in the weekly circular and in-store displays significantly improve the effectiveness of promotions. Key items and brands that rank high in consumer importance and are priced competitively every day should be featured frequently, without necessarily dropping the price each time. Other image, excitement or unique brands should be promoted less frequently. In this way, you generate excitement and preserve margins while still offering an occasional deal to your loyal customers.

Better pricing and promotions strategies can result in stronger competitiveness, sales and profitability, with profit improvements ranging from 20 to almost 40 percent.

Private-label promotions are most effective in the weeks prior to the promotion of a targeted national brand. For example, when one retailer put a national-brand mouthwash on promotion, the unit volume of the private-label brand dropped 40 percent. When the private-label promotion preceded the national-brand promotion, sales of both rose 20 percent. At other times, private-label promotions generate lower comparable ROI, especially if priced attractively on an everyday basis or when competing with a national brand with strong, frequent promotions.

Finally, continuously tracking promotion strategies to measure consumer behavior patterns will help identify the successful and unsuccessful promotions. There is certainly no lack of information available to measure the impact of promotions—with data from point-of-sale, loyalty cards and markets all providing indicators of what is going on. Sifting through this data to identify metrics that the retailer should focus on is perhaps the most critical aspect of measurement. A comprehensive promotional scorecard will highlight five key measures:

- Item lift, including cannibalization in weeks following the promotion
- ROI for each event and brand
- Category sales and profit
- Category penetration
- Average basket size
- Store traffic count

Improved pricing and promotion strategies can result in stronger competitiveness, sales and profitability. Results from such initiatives have been powerful, with profit improvement ranging from 20 to almost 40 percent.

Building a Better Price Image

In the end, pricing and promotion strategies will only be successful if they are designed in a consistent way with all other merchandising and operational elements that provide value to the consumer. Top retailers establish a relevant point of differentiation to provide distinct value to their target audience. Base prices, promotions, assortment, service, private labels and visual merchandising all combine to create a value-to-price relationship.

In a recent customer survey of a traditional retailer, customers rated the retailer as higher priced than its EDLP competitors, but gave the retailer a higher overall value rating. The retailer scored well in differentiated product assortment, exceptional service, product freshness, store cleanliness and a good overall shopping experience. These are all part of the value equation along with price. Today, this retailer is successfully growing market share while many of its EDLP competitors are languishing.

Firms must focus on retaining and growing a loyal customer base. Fair pricing for the items consumers "know" the value of and targeted promotions on particular high-visibility items are good strategies. However, in an effort to bring more people through their doors, retailers should avoid dangling too large a carrot; some people might come just for the free lunch.

Armed with all the information available, retailers can gain better insight into the increasingly sophisticated buying habits and tastes of both their best and worst customers. They can use this data to create strategies that either reward and attract the profitable shoppers or change or dissuade the habits of the unprofitable.

A.T. Kearney is a global strategic management consulting firm known for helping clients gain lasting results through a unique combination of strategic insight and collaborative working style. The firm was established in 1926 to provide management advice concerning issues on the CEO's agenda. Today, we serve the largest global clients in all major industries. A.T. Kearney's offices are located in major business centers in 35 countries.

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