The Next Generation of Pricing

Benchmark Study: January 2008

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Executive Summary

The transformation of retail from product-centric to customer-centric has come right as price optimization has "crossed the chasm" of technology adoption and found its way into the mainstream. What future lays in store for one of the most successful retail technology innovations of this decade? This study benchmarks how far the retail industry has come in adopting advanced pricing techniques, and examines where retailers plan to take pricing capabilities as they move forward with their customer-centric strategies.

The Business Challenge

Whatever the price strategies a retailer follows, they face the same business challenges regardless of segment or size: maintaining or increasing gross margin, beating the competition, and driving sales. But the biggest challenge is a fundamental retail paradox: while there is certainly pressure to become more customer-centric, retailers can give no quarter on price – gains in customer service cannot come at the cost of price competitiveness. A clear difference emerges among retail winners: Whether it is the primary differentiator or not, winners keep price central to their retail strategy and laggards don't.

Opportunities

As a way to drive the business, retailers are stuck on price as a lever for margin, and so are missing other opportunities to maximize the value of pricing capabilities. Few survey respondents currently use sophisticated techniques to set or change prices, relying mostly on staying on top of the competition and average markup based on cost. Respondents are also focused mainly on base price setting, leaving lots of room to expand across the entire price lifecycle. Using data in price optimization decisions also presents an important opportunity for making more strategic use of pricing capabilities.

Organizational Barriers and How Winners Overcome Them

Concerns over skill sets and concerns over technology constraints vie with "other priorities" as retailers' biggest challenges when it comes to maximizing the value of pricing capabilities internally. There is no longer a lot of distrust in the science behind the solutions – what was once a major barrier earlier in the adoption of price optimization. However, laggards still struggle with cultural resistance, and are the least prepared to take on advanced pricing capabilities. Pilots are what pave the way to overcoming organizational inhibitors – with pilots by category or product line taking the lead over regional pilots.

Technology Enablers

Atypical for our surveys, laggards either are at parity with winners in technology adoption, or lead the pack in adoption of pricing solutions. While there are a few instances where winners are more likely to have solutions in place, it is unusual for laggards to track so closely with winners in terms of adoption. However, for all that laggards have more solutions in place, it is winners that do more – making greater use of optimization capabilities across the product lifecycle. But no matter the differences, respondents have their sights locked on evolving towards end-to-end price lifecycle management.

Bootstrap Recommendations

The end-game for pricing solutions will be an end-to-end pricing capability embedded in the front lines of merchandising decision-making, and it will encompass both consumer-facing objectives, like promotion optimization, and supply chain objectives, like optimizing inventory across or within channels. Getting there is the hard part, but winners, as usual, are leading the way, by focusing on category- (rather than individual item-) objectives, avoiding isolated groups, paying attention to inventory, and planning ahead for end-to-end lifecycle capabilities.

SECTION I: OVERVIEW

WHY THE STUDY WAS CONDUCTED

Five years ago, price optimization and advanced pricing technologies seemed like the answer to the increasingly desperate question of how to compete with Wal-Mart: by running point of sale data through mysterious black box algorithms, the computer systems that merchants have historically disdained would magically spit out the right price to recapture both the consumer's loyalty and the retailer's margins – whether through a better match of prices to demand, or a better management of end-of-season inventory.

However, even for as desperate as many retailers were for that magic price, price optimization solutions still had to run through conservative retail IT buying practices and it took several years before the solutions evolved from new technologies that only leading-edge retailers were willing to adopt to now a nearly expected part of the merchandising systems portfolio.

That evolution has come in the midst of a rapidly changing retail environment – consumers realized that new channels like eCommerce gave them a lot more power in the consumer-retailer relationship just as retailers realized that price alone is not enough of a differentiator to win at retail. Retailers' response to consumers, in the form of customer centricity, has become a lasting strategy that will continue to shape the development of the industry for years to come.

For pricing, this transformation of retail from product-centric to customer-centric has come right as price optimization has "crossed the chasm" of technology adoption and found its way into the mainstream. So what future lies in store for what is arguably one of the most successful retail technology innovations of this decade? This study benchmarks how far the retail industry has come in adopting advanced pricing techniques, and examines where retailers plan to take pricing capabilities as they move forward with their customer-centric strategies. We'll take a close look at the business challenges, opportunities, and technology enablers that are most important to retail winners, identifying the pricing practices and solutions that winners use to maintain and grow their competitive advantage.

METHODOLOGY

RSR uses its own model, called the "BOOT," to analyze Retail industry issues. We examine the approaches retail winners take to solving specific business challenges and how technology supports those winning ways. The model is built from retailer answers to our surveys. An explanation of the methodology can be found in Appendix A.

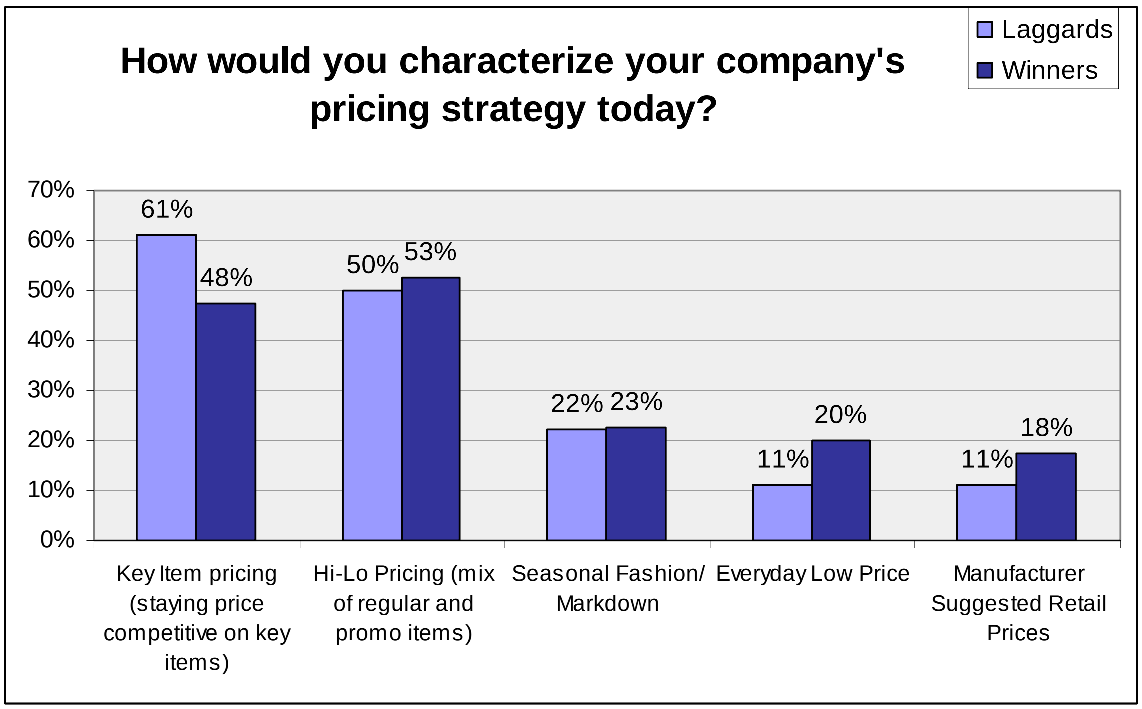
Winning is not an accident in the world of Retail. Customers vote with their wallets. Sustainable sales improvement and successful execution of brand vision are direct results of an enterprise's recognition of external and internal business issues, its ability to take advantage of opportunities for improvement, and its use of technology enablers to simplify and rationalize business processes. Data that emerges from the BOOT model helps us understand the behavioral and technological differences between winners and their peers.

DEFINING RETAIL WINNERS AND WHY THEY WIN

Our definition of retail winners is straightforward. We choose to follow Wall Street. Wall Street judges retailers by year-over-year comparable store sales improvements, and we do the same. Assuming industry average comparable store sales growth of three percent, we define retailers with sales above this hurdle as "winners," those at this sales growth rate as "average," and those below this sales growth rate as "laggards" or "also-rans." In addition, depending on the subject matter, we also consider a consistent or declining payroll to sales ratio as a hallmark of retail winners, or improved gross margin results. Interestingly, we find that most other KPI's fall into line behind the leading indicator of comparable sales.

Among respondents to this survey, we found that the choice of price strategy does not dictate retail success – there are no pricing strategies that are clearly and overwhelming employed by retail winners over their peers (Figure 1). However, too much focus on certain price strategies can lead to a losing path: laggards tend to focus more heavily on key item pricing compared to peers.

Figure 1: Choice of price strategy does not differentiate winners



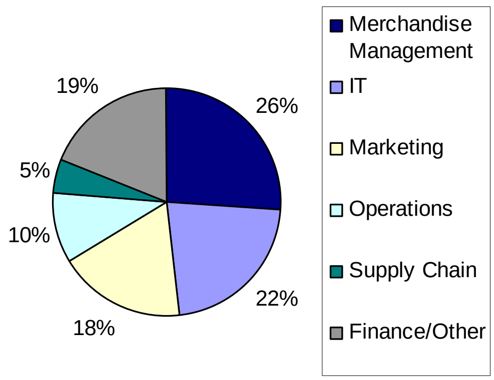
Source: RSR Research

This only underscores the importance of tools in defining, applying, and enforcing a price strategy to the business: pricing capabilities are not enough to make a retail winner. It's how you use those capabilities as part of the overall strategy that separates the best from the also-rans.

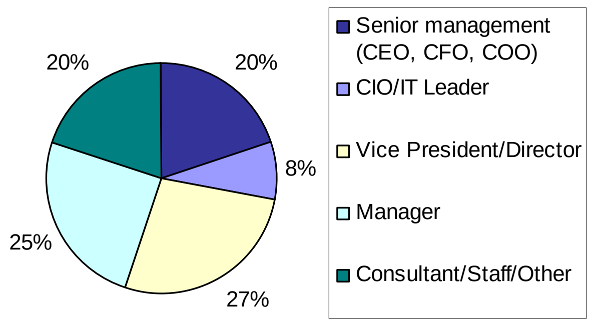
SURVEY RESPONDENT CHARACTERISTICS

RSR conducted an online survey between November and December 2007 and received responses from 106 retail respondents. Respondent demographics are as follows:

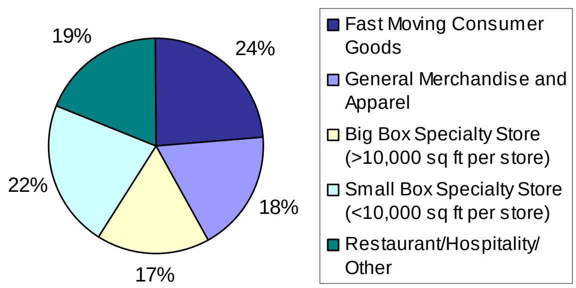
Respondents by Functional Area



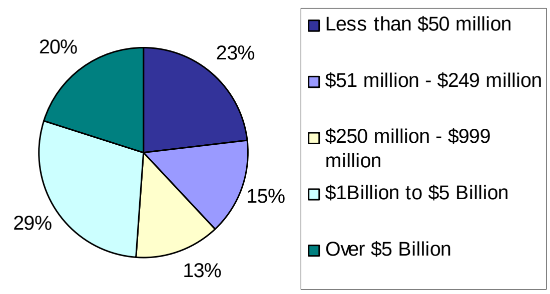
Respondents by Job Title



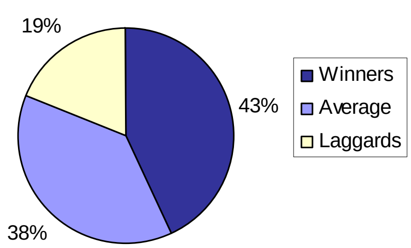
Respondents by Segment



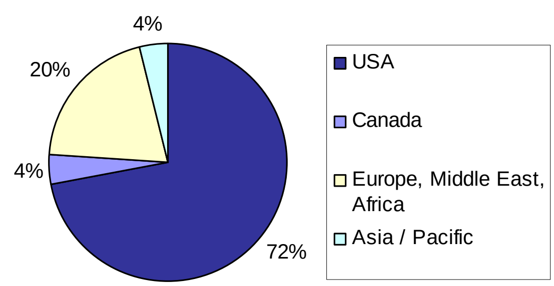
Respondents by Revenue



Respondents by Performance



Respondents by Headquarters Location



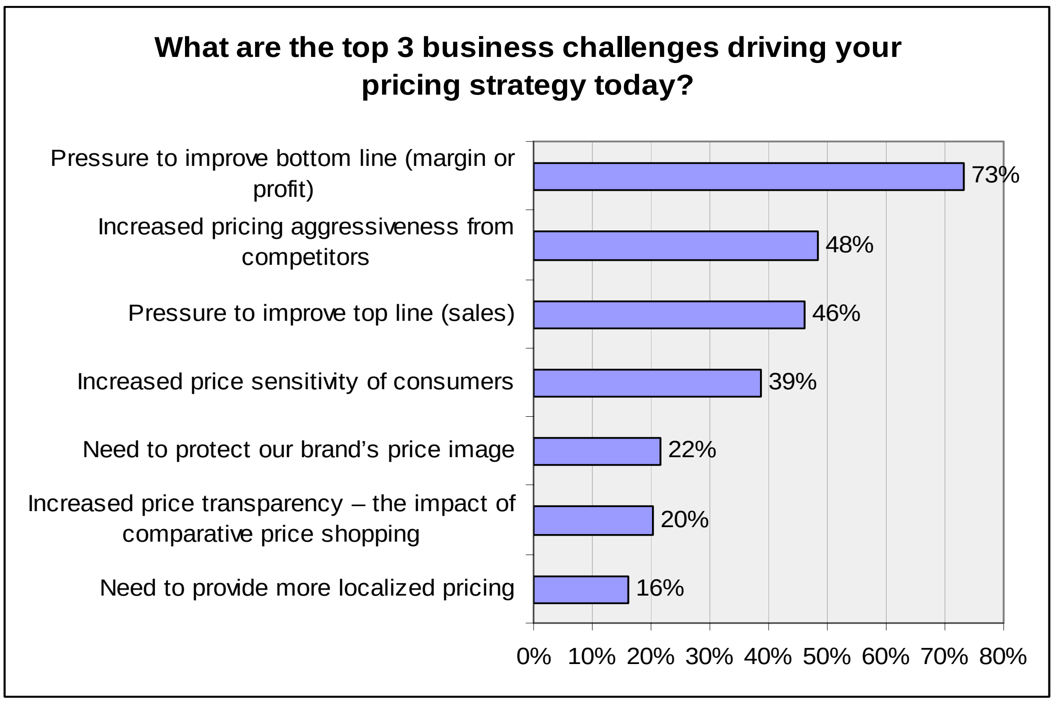
SECTION II: BUSINESS CHALLENGES

PRICE: THE MOST SENSITIVE LEVER

Retailers have a lot of different levers to pull in order to drive business success, but price is one of the most sensitive. Pulling a little on the price lever can have a big impact and as a result a retailer's pricing strategy is also extremely sensitive: often, one of the most heavily guarded secrets within the enterprise, perhaps even more jealously guarded than customer insights.

But whatever the price strategies a retailer follows, when it comes to the business challenges that shape retailers' price strategies they face the same challenges regardless of segment or size: maintaining or increasing gross margin, beating the competition, and driving sales (Figure 2).

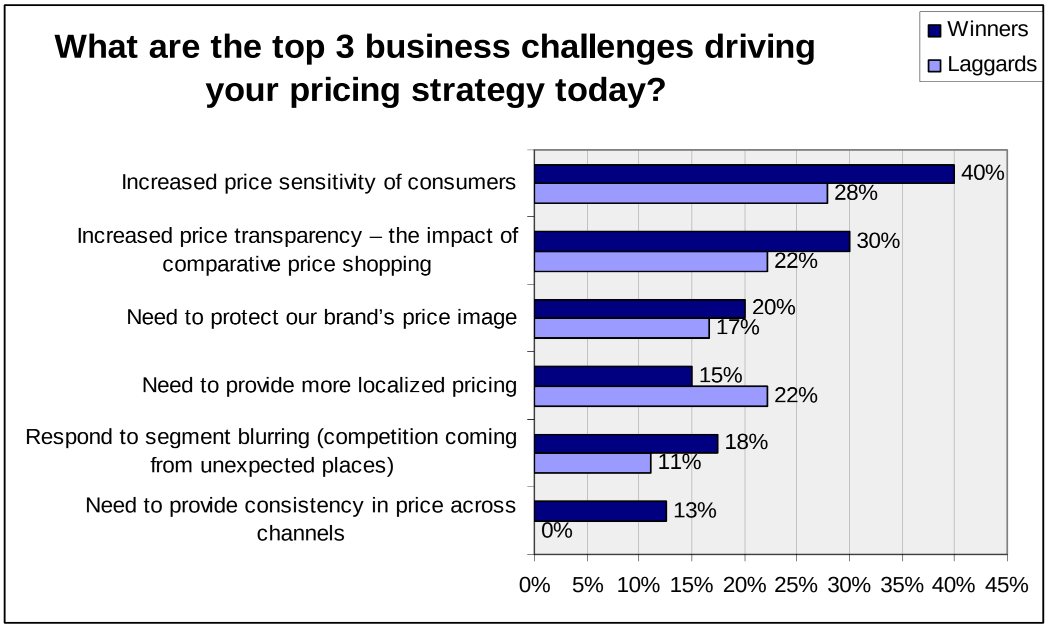
Figure 2: Business challenges are the same no matter the price strategy



Source: RSR Research

Outside of the top 3 challenges, winners are more likely to also keep an eye on consumer perception and reaction to prices, with more emphasis on segment blurring (competition from unexpected places), cross-channel price consistency, and price transparency (Figure 3). In contrast, laggards are more unfocused - spreading their concerns across a variety of challenges, and not keeping their eye on the customer.

Figure 3: Winners are more focused on consumer reaction to prices



Source: RSR Research

There are also different priorities by retail segment, but the differences are not surprising. Retailers of fast-moving consumer goods (FMCG) and general merchandise and apparel (GMA) are more concerned about price sensitivity of consumers than their peers (57% FMCG and 47% GMA vs. 39% overall) – not surprising, given the fiercely competitive nature of those industries. Specialty retailers large and small are more concerned about maintaining their margins than peers (87% big box specialty and 80% small specialty vs. 73% overall), again not surprising given their need to preserve higher margins to support their business model.

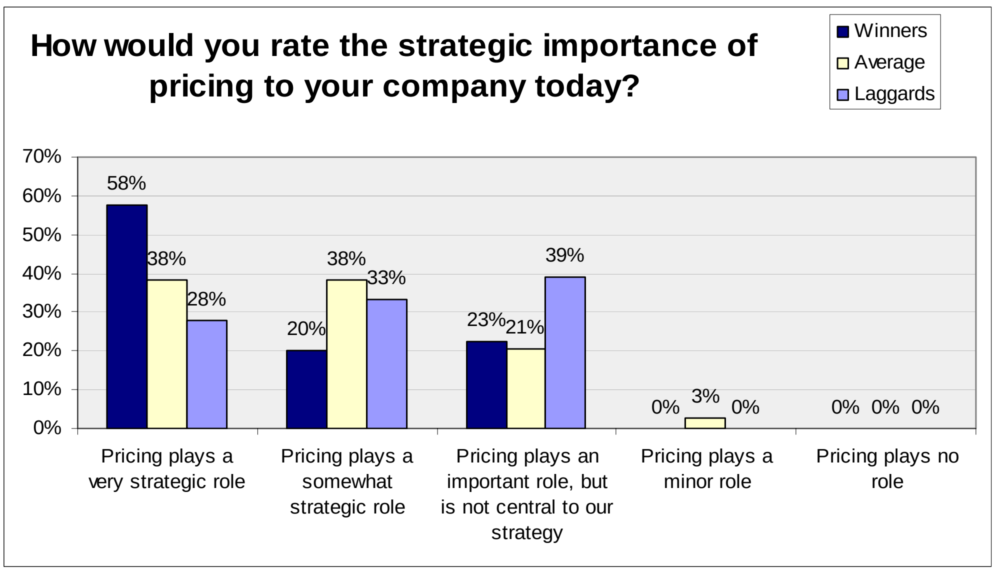
The amount of private label merchandise that a retailer carries also has little impact on the priority of business challenges that drive retailers' pricing strategies, according to survey respondents. Private brand retailers face the same challenges as national brand merchants when it comes to pricing, though they are more likely to be concerned about increased price competition (60% of respondents with more than 75% private label merchandise vs. 48% overall) and the need to protect their brand's price image (60% of respondents with more than 75% private label merchandise vs. 21% overall).

Price and the Retail Paradox

At RSR, we constantly argue that price alone is no longer a competitive differentiator, for many of the reasons that respondents cited as major business challenges today – like price transparency and increased price sensitivity of consumers. When a customer can find out about your sales before your employees do, thanks to the likes of BlackFriday.net, the retailer is clearly at a disadvantage. But we also argue that retailers cannot completely abandon price in pursuit of customer service differentiators. Wall Street would hardly stand for a major hit to the bottom line simply to increase the number of employees on the floor or add free new services.

This fundamental challenge is the foundation of RSR's concept of the "Retail Paradox." Gains in customer service cannot come at the cost of price competitiveness, and this research bears us out: Whether it is the primary differentiator or not, **winners keep price central to their retail strategy and laggards don't** (Figure 4).

Figure 4: Winners keep price central to their retail strategy

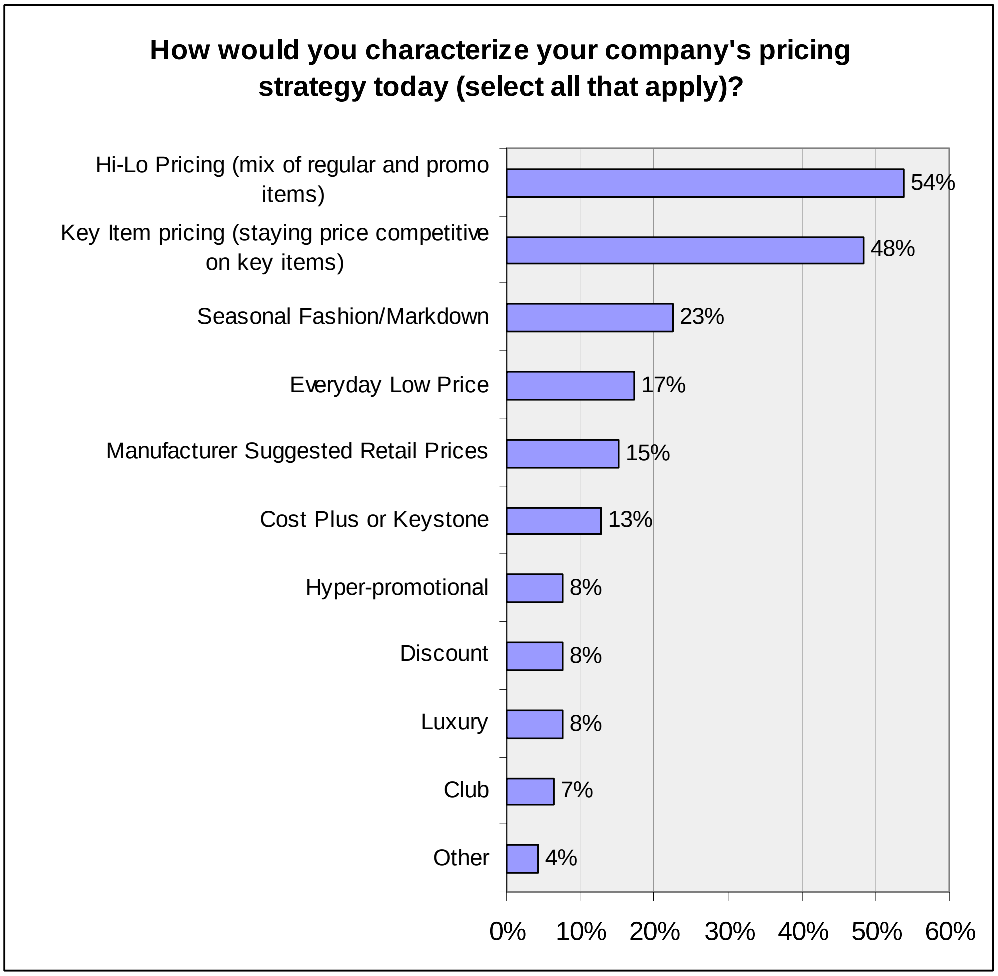


Source: RSR Research

Pricing as a strategy is naturally more important to some segments over others: FMCG and Big Box specialty retailers indicate it as generally more strategic (61% and 53% respectively, vs. 45% overall indicating "pricing plays a very strategic role"). GMA retailers are more likely to see price playing a "somewhat strategic role" (41% GMA vs. 29% overall), and small specialty and restaurant & hospitality segments tend to see pricing as less strategic (45% and 35% respectively, vs. 25% overall indicating "pricing plays an important role, but is not central to our strategy"). But even in segments where pricing is less strategic overall, winners held it as more important than their peers.

Overall, respondents tend toward a blend of price strategies, averaging nearly two strategies each (1.9 on average) across the range of pricing strategies. The two most common price strategies among respondents are high/low pricing and key item pricing (Figure 5).

Figure 5: Retailers employ a range of price strategies



Source: RSR Research

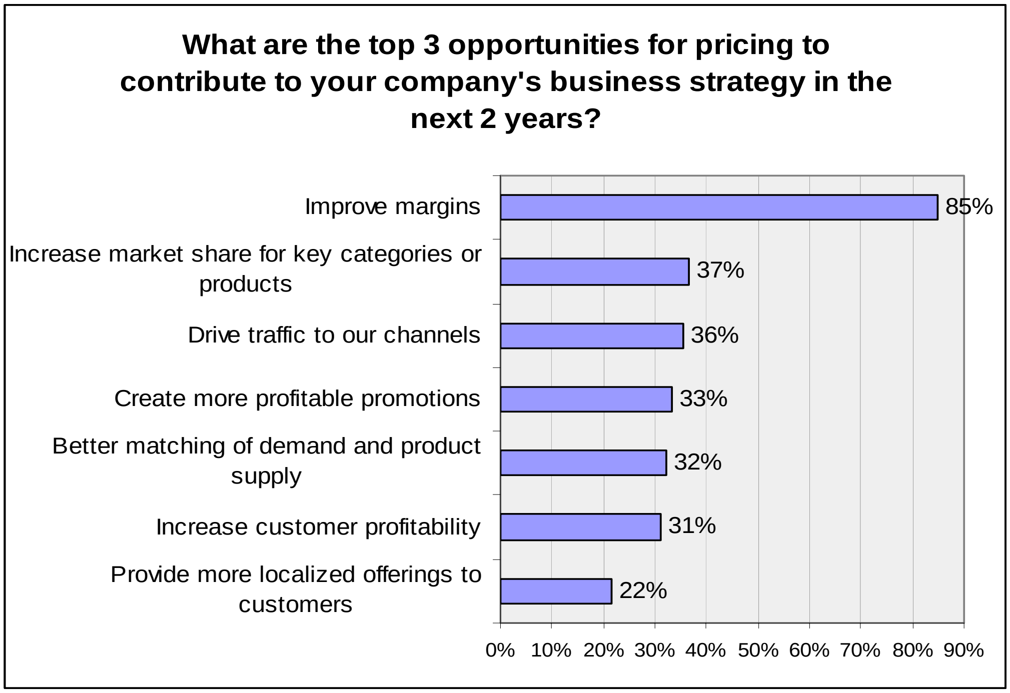
Respondents are likely to stick with the strategies they've adopted – indicating either no change in strategy over the last three years, or intensifying their focus on existing strategies (i.e., those focused on key item pricing as a strategy have become even more focused on it over the last three years). Laggards are more likely to have changed their price strategy in the last three years – of the 29 respondents who have changed their strategy, 28% are laggards, compared to 19% of laggards in the general population of respondents. But even though winners are slightly less likely to have changed their pricing strategy in the last three years, they do tend to be slightly more flexible in the strategies they employ, averaging 2.1 pricing strategies, compared to 1.9 overall.

SECTION III: OPPORTUNITIES

PRICE IMPACTS MARGIN

Respondents name margin improvements as the biggest opportunity by far for pricing capabilities, with other opportunities for pricing to contribute to the business lagging far behind (Figure 6).

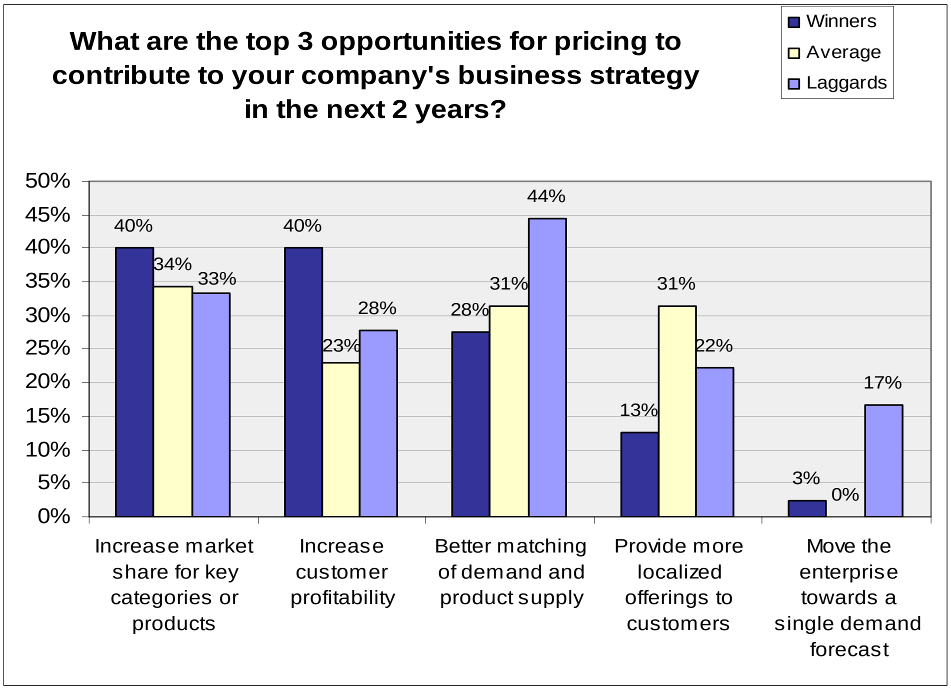
Figure 6: Respondents see price as a single lever tied to margin



Source: RSR Research

There are some differences in perspective by performance. Typical for our surveys, winners are more likely to also look for opportunities to differentiate from the competition, in this case by focusing more on price to drive market share in key categories (Figure 7). This is in contrast to laggards, who as we pointed out earlier, are more focused on key items – missing the bigger picture of overall category success in an effort to cherry pick prices – and customers – based on individual items. Laggards are also more worried about the supply chain impacts of pricing, giving higher priority to opportunities to use price to match demand to supply and to move the enterprise to a single demand forecast.

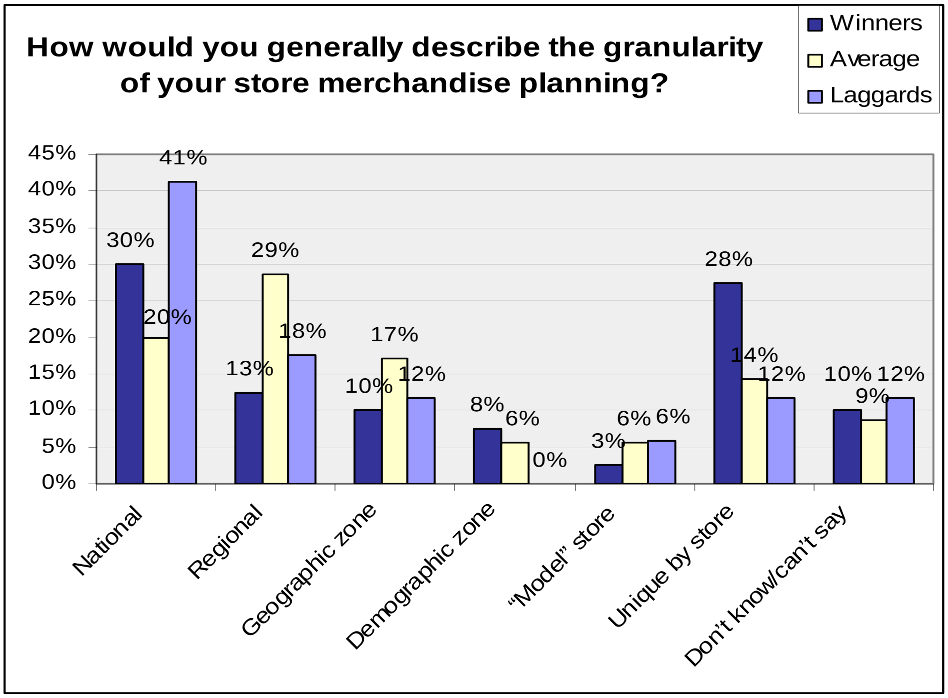
Figure 7: Winners are more likely to seek competitive differentiation through price



Source: RSR Research

Winners are less focused on using price to drive localized offerings than their peers, but this is not surprising given that winners also tend to be more granular in their merchandise planning (Figure 8) – they don't need price for localization when they already have the capability available through assortment planning and allocation.

Figure 8: Winners tend to plan merchandise at a more granular level

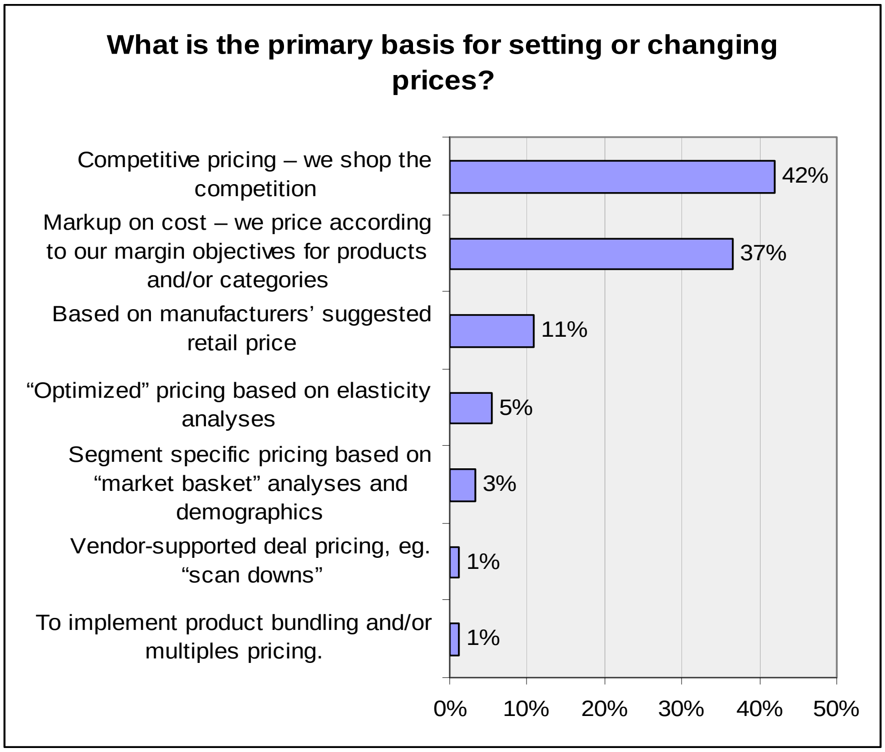


Source: RSR Research

Pricing Opportunities Abound

Retailers' singular focus on margin as the opportunity for price management is disappointing. In fact, there are multiple areas where the opportunity to be more strategic about pricing is underutilized. For example, few respondents currently use sophisticated techniques to set or change prices, relying mostly on staying on top of the competition and average markup based on cost (Figure 9). Only 5% of respondents use elasticity analysis – and half of those respondents come exclusively from the grocery segment.

Figure 9: Few respondents use sophisticated techniques to set or change prices

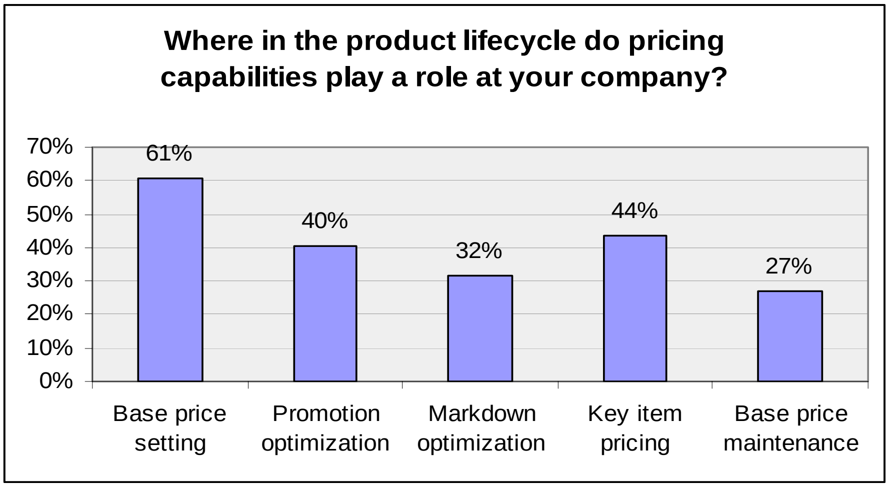


Source: RSR Research

Winners are not any more likely than their peers to use sophisticated pricing techniques. In fact, the only clear difference by retail performance comes from laggards, who are the only performance segment to report using vendor-supported deal pricing.

When looking at the overall price lifecycle, pricing capabilities are focused mainly on base price setting, leaving lots of room to expand across the entire price lifecycle (Figure 10). Interestingly, base price maintenance currently has little uptake among respondents, suggesting that they don't revisit their prices very often – another missed opportunity for being more strategic about price.

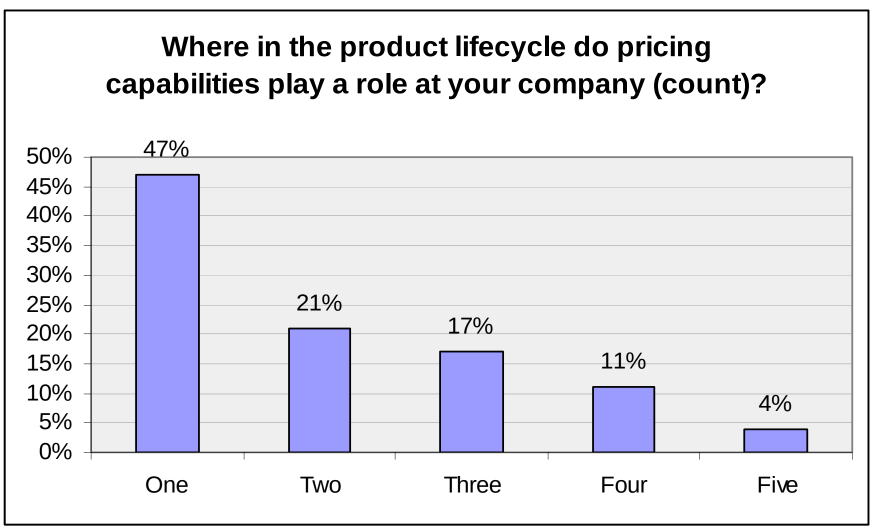
Figure 10: Opportunities cross the entire pricing lifecycle



Source: RSR Research

However, even these adoption numbers can be misleading, as very few retailers have implemented price optimization across the entire product lifecycle (Figure 11). Also, winners aren't any more likely to cover the entire product lifecycle than their peers.

Figure 11: Most retailers only cover one or two aspects of the price lifecycle



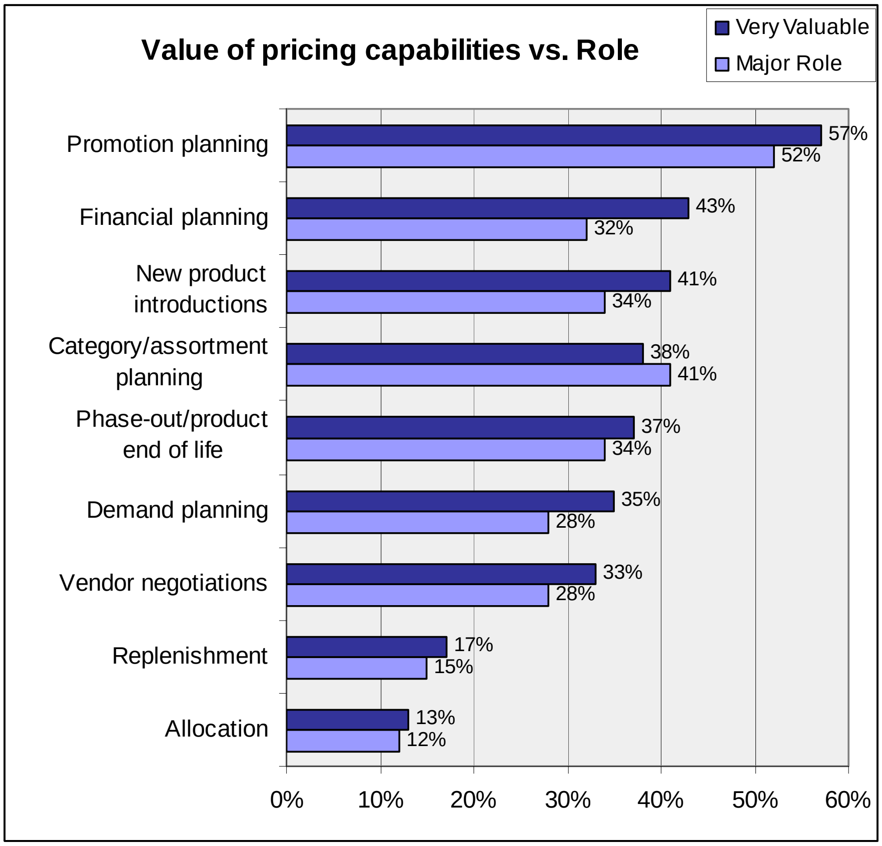
The X Axis in Figure 11 refers to the number of pricing capabilities that a respondent indicated in Figure 10. Read this chart as "Of the five pricing capabilities identified in Figure 10, 11% use four."

Source: RSR Research

When looking across all the areas of the business where price optimization can play a role, the gaps between where pricing is seen as very valuable and where it actually plays a major role are smaller than we typically see in our surveys. Respondents see the most value in using price capabilities in promotions, but don't generally see the value in using price to help drive allocation or replenishment decisions (Figure

12). The biggest gap between value and use is in financial planning, followed by demand planning and new product introductions.

Figure 12: Respondents show few gaps between pricing's value and its use across functions

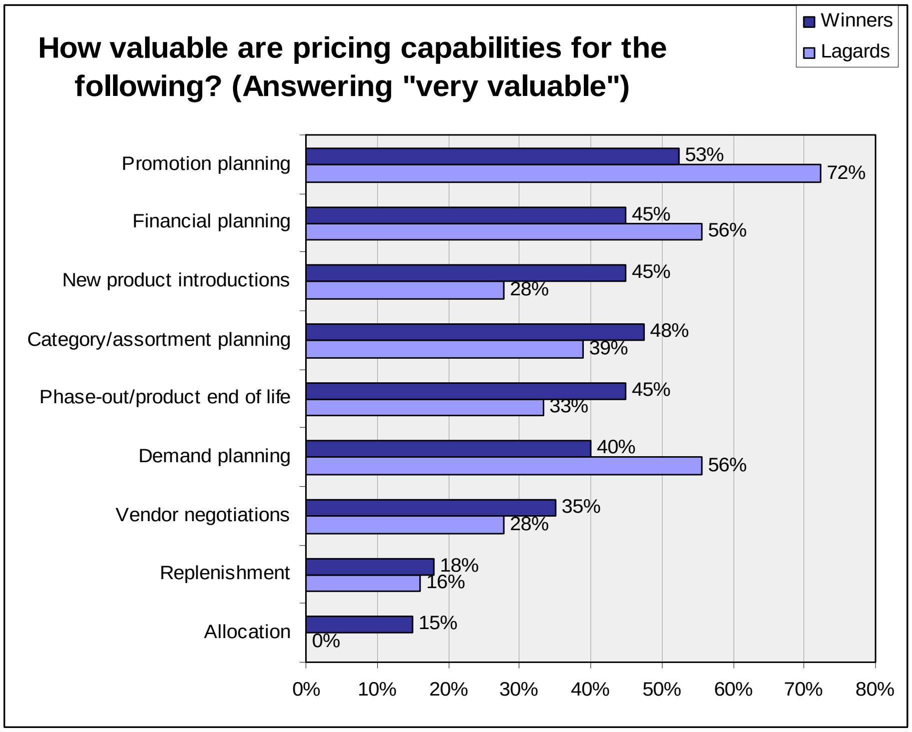


Source: RSR Research

Winners are generally more even in their consideration of the value of pricing – they see the value across the entire product lifecycle, rather than focus on one or two opportunities. Compared to laggards, winners are more likely than their peers to the see the value of pricing capabilities at the two ends of the product lifecycle: during new product introductions and at products' end-of-life (Figure 12). They are also more likely to see the value in using price to inform category or assortment planning.

Laggards are less balanced than their peers in their consideration of the value of pricing. They appear to be more taken with the supply-side and financial planning value of pricing capabilities, but focus more on higher-complexity opportunities, with more emphasis on promotion planning and demand planning, but little emphasis on replenishment or allocation.

Figure 12: Winners are more likely to value pricing for its impact across the product lifecycle

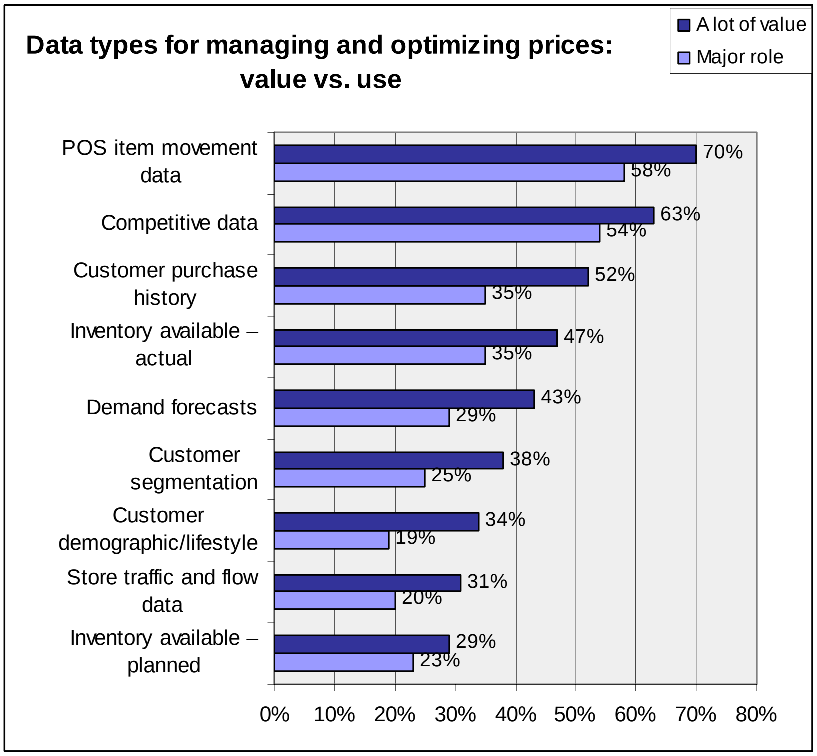


Source: RSR Research

Deciding In The Dark

Using data in price optimization decisions also presents an important opportunity for making more strategic use of pricing capabilities. Overall, respondents report a bigger gap between the data elements they feel are valuable and the data elements that they actually use in practice, and they don't tend to see a lot of value in using supply chain data like inventory availability in making pricing decisions (Figure 13).

Figure 13: Respondents don't make as much use of different data elements as they would like



Source: RSR Research

It was surprising at first to see that respondents were just as likely to use customer purchase history in pricing decisions as on-hand inventory available – neither of which is used by a majority of respondents. It seems a big risk to make pricing decisions in an inventory vacuum. What good is it to have an optimized price when there is no inventory on hand to sell? However, there are a few trends at play that explain the parity. First, as we'll see in the Technology Enablers section, and as we've seen in past research,[1] promotion optimization is a high priority for retailers, and customer data is a key component needed to make optimized promotional offers, which explains why customer-oriented data types rate fairly high in value.

Second, there are certain sets of respondents that do rely heavily on inventory. Respondents that use pricing capabilities for markdowns are much more likely to value – and use - inventory availability (actual) than their peers. Only 10% of these respondents report little to no role for on-hand inventory data (compared to 25% of their peers), and less than 3% feel that current inventory data has little to no value (compared to 22% of their peers). The value and use of inventory data also follows industry lines – FMCG retailers are less likely to rely on inventory data, given their high-replenishment environments, while specialty and apparel retailers of all stripes both value it more and make more use of it.

[1] *"Getting Loyalty Programs Back to Loyalty,"* by Nikki Baird. July 2007. Nearly 50% of survey respondents are planning or budgeting a promotions optimization implementation in the next year.

The issue around inventory seems to be more a matter of trust than a matter of value – POS movement data is heavily used no matter the segment, retail performance, or level of adoption of price optimization. In-store inventory is notoriously inaccurate and expensive to maintain, so many retailers rely on item movement at POS as a proxy for store inventory levels. Winners do see more value in using inventory data, though they aren't any more likely to use it than their peers (34% of winners see "inventory data – actual" as very valuable vs. 17% of laggards). This suggests that while winners would *like* to trust – and use – their inventory data, they still haven't established enough trust in that data to use it to make pricing decisions.

Price is Much More Than a Lever for Margin

As a way to drive the business, retailers are stuck on price as a lever for margin, and so are missing other opportunities to maximize the value of pricing capabilities. Thinking about price as a lever primarily for margin is thinking small: price is a lever for *demand*, which influences much more than margin: it impacts supply, and most especially can impact customer perception of the retailer, both directly and indirectly through levels of supply. Price also influences how fast product moves through channels, and if you don't have a good handle on the inventory levels (both actual AND planned) that support a current price or price strategy, you're risking a lot more than just margin: you risk stockouts or overstocks, and a major amount of customer dissatisfaction.

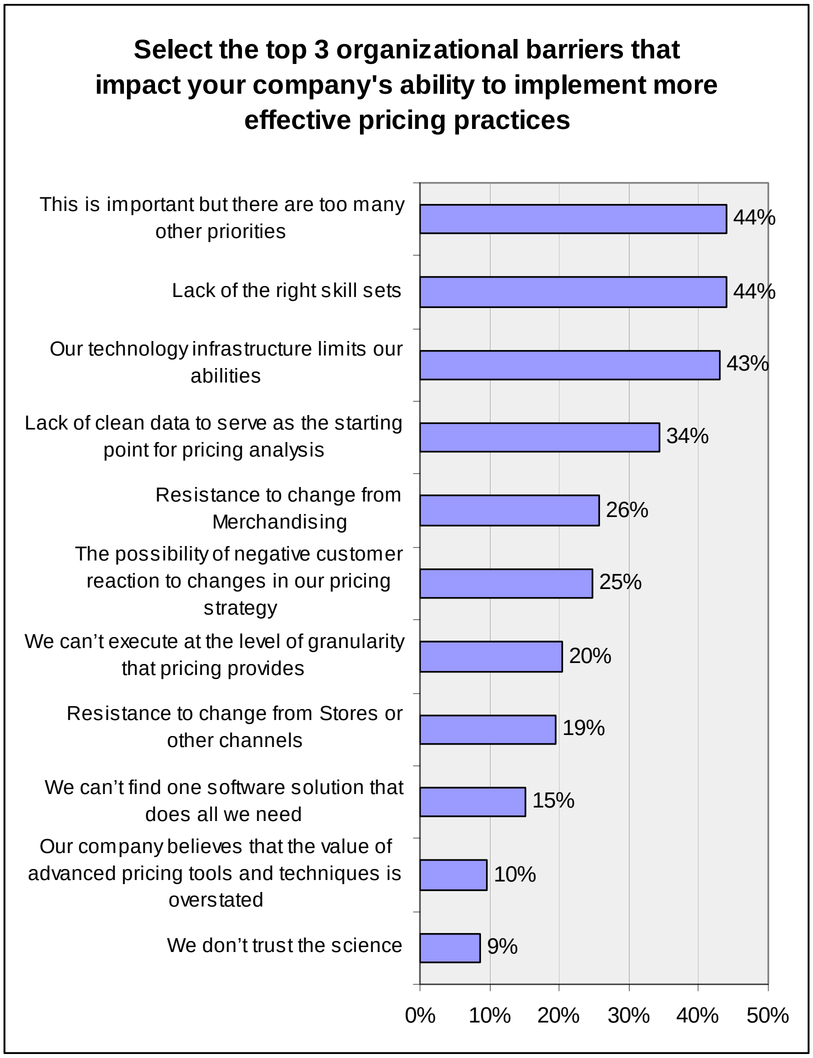
Even if circumstances (like extreme competition) dictate that you must focus on margin alone, there are still lots of opportunities for driving value to the business through price – by expanding across the product lifecycle and by taking a more holistic view of the role that price plays in customer satisfaction. Without this holistic view – encompassing demand, supply, and customer perception – price optimization is like a symphony being played in an empty room. It might be perfect in every way, but it's meaningless if there is no one there to hear it.

SECTION IV: ORGANIZATIONAL BARRIERS

SKILL SETS AND INFRASTRUCTURE DOMINATE INTERNAL CHALLENGES

While “other priorities” nearly always make the top of the list in our surveys, usually either technology constraints or people constraints weigh heavily on survey respondents’ minds, but rarely both at the same time. For pricing, they compete head to head for the top challenge – concerns over skill sets and concerns over technology constraints vie with other priorities as retailers’ biggest challenges when it comes to maximizing the value of pricing capabilities internally (Figure 14).

Figure 14: Respondents are challenged by both people and infrastructure constraints

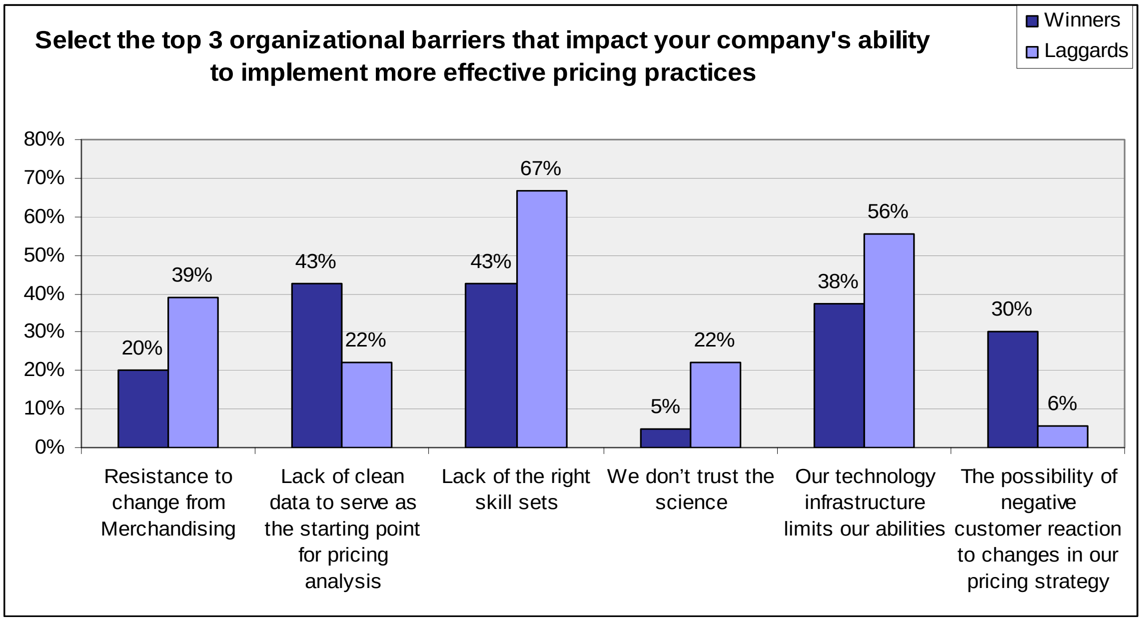


Source: RSR Research

There is no longer a lot of distrust in the science behind the solutions – what was once a major barrier earlier in the adoption of price optimization. Today, only 10% cited beliefs that the value of the technology is overstated, and 9% said they don't trust the science, the bottom two organizational inhibitors on our list.

Laggards are the least prepared to take on advanced pricing capabilities. In addition to greater challenges around technology infrastructure and skill sets, laggards are much more likely to battle cultural resistance from merchandising groups and an internal lack of belief in the science (Figure 15).

Figure 15: Laggards are more likely to still battle cultural resistance



Source: RSR Research

Winners, for the most part, are over the need to prove that the science works, and also pretty much have the Merchandising team bought into the concept. But winners are also more cognizant of the data requirements needed to get a pricing capability off the ground – this awareness is reflected in their higher rating of data challenges as an internal barrier to adoption.

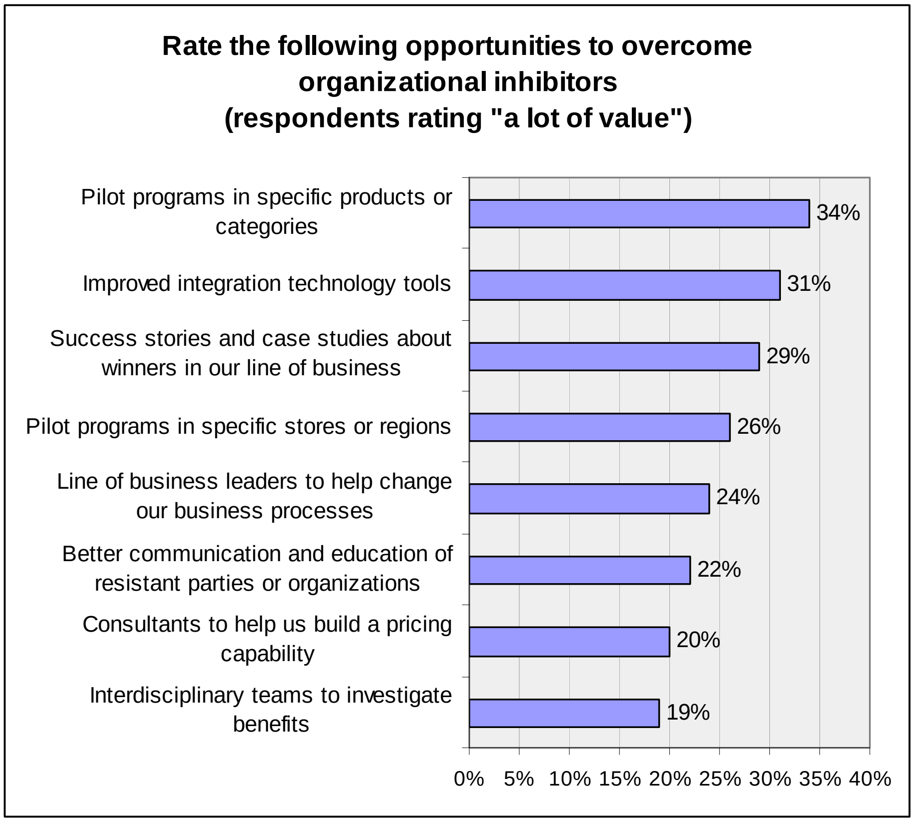
Winners are also more worried about their face to the customer, with more emphasis on cross-channel implications and negative customer reaction to changes in pricing strategy. However, the cross-channel concern isn't necessarily a differentiator between how winners approach pricing vs. laggards. We have found in other surveys that winners tend to operate more channels than their peers,[2] and so it is natural for them to give cross-channel concerns a higher priority.

Overcoming the Barriers

According to respondents, pilots are what pave the way to overcoming organizational inhibitors – with pilots by category or product line taking the lead over regional pilots (Figure 16).

[2] *"Searching for the True Multi-Channel Retailer,"* by Paula Rosenblum. 2006. Nearly 70% of retail winners operate more than one channel, vs. less than 50% of laggards.

Figure 16: Category pilots lead the way past organizational inhibitors



Source: RSR Research

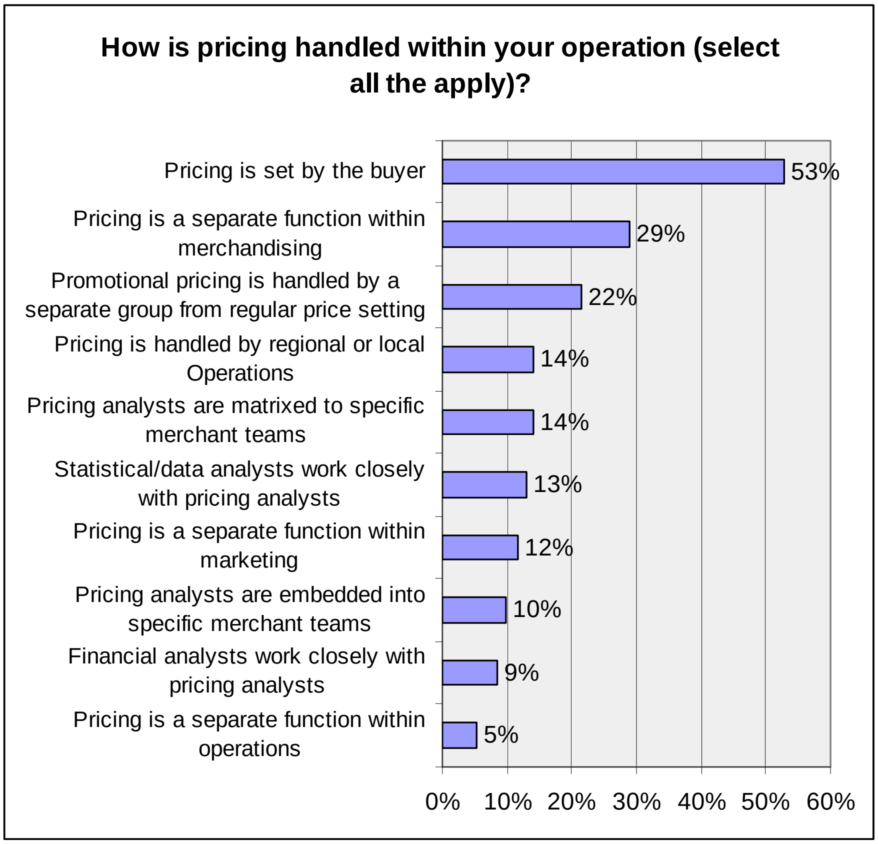
Close behind category pilots are improved integration tools, reflecting the need to address technology infrastructure issues, and case studies about specific retail segments. Larger retailers in particular see value in category pilots (36% of retailers with greater than $1B in revenue vs. 26% overall). Winners are much more wary of inter-disciplinary teams when it comes to defining the value of pricing solutions (53% of winners saw little to no value in such teams vs. 11% of laggards).

Tackling the Skill Set Challenge

For all respondents, skill sets is the bigger concern. Only the largest retailers (over $5 billion in revenue) indicated any confidence in making sure that they have the right skill sets in place to make the most of pricing capabilities. But **despite the concern over skill sets, respondents are unwilling to give up control over the issue in order to overcome it** – opportunities to overcome the barrier that focused on outsourcing or offloading the problem, like consultants, systems integrators, or vendor quick-start capabilities, ranked among the lowest.

For a majority of respondents, price is set by the buyer (Figure 17). The next most popular organizational structure places pricing into a separate group within the merchandising function, followed by nearly a quarter or respondents who have separate promotional pricing groups from those that set regular prices.

Figure 17: Respondents are still working out the right pricing organization



Source: RSR Research

Laggards tend to favor more complex organizational structures than their peers – 44% keep pricing separate within merchandising compared to 29% overall, and 22% operate a matrixed pricing function compared to 14% overall. Winners keep pricing decisions as close to the front line as possible – 58% favor the buyer as price-setter – and 18% of winners pair statisticians with pricing analysts compared to 0% of laggards.

Headway in the Cultural Battle

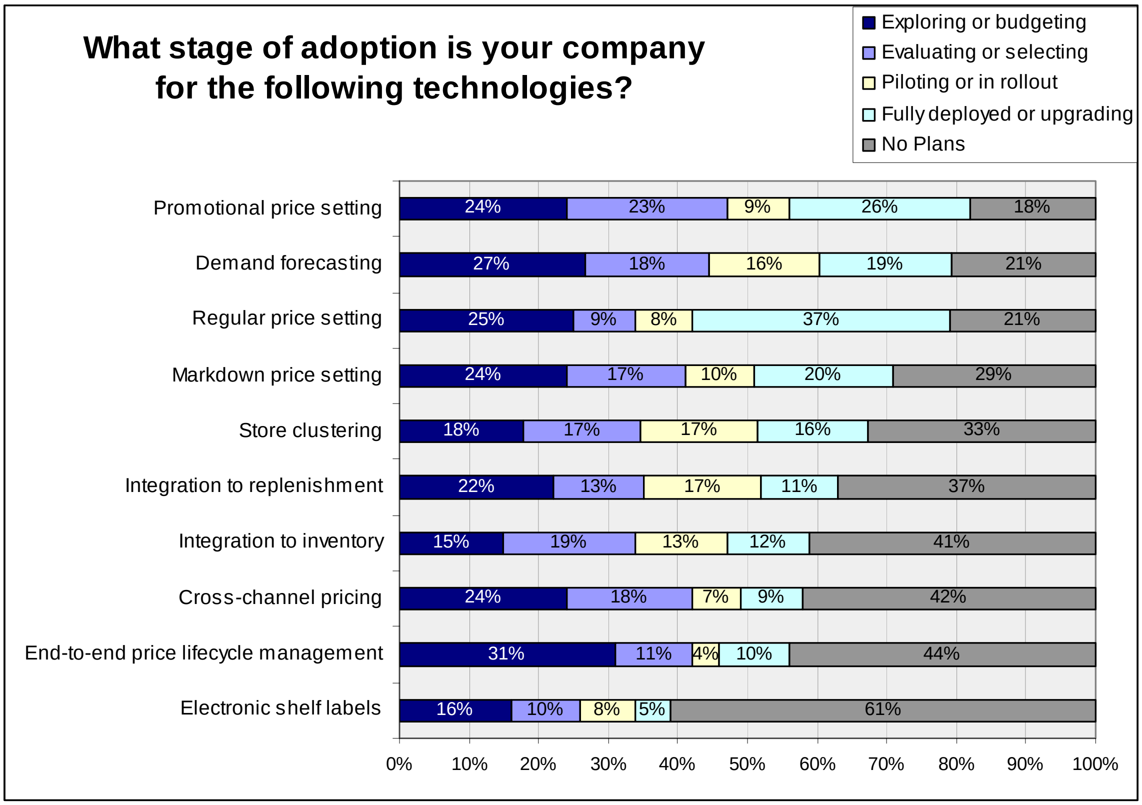
Winners' trust in the science of pricing is heartening. It shows that progress has been made in educating retailers about the opportunities that pricing and price optimization present, though this continues to be challenge for laggards. The battle needs to move from struggling to understand the science behind the technology, to struggling to find the right alignment between the technology and people. Whether the people who use the technology to make pricing decisions sit right at the front line or not, the closer the decision is made to the front line of merchandising, the better. Laggards hamstring themselves by creating overly complex organizations. While those organizations can work, they only work if you focus specific attention on communication processes that address the shortcomings of the org structure – for example, co-locating statisticians and pricing analysts.

SECTION VI: TECHNOLOGY ENABLERS

END-TO-END PRICE LIFECYCLE MANAGEMENT IS COMING

Respondents are looking ahead to pulling together all of the pieces needed to span the entire price lifecycle – if they aren't exploring or planning on promotion or markdown optimization, they are looking at end-to-end lifecycle management, cross-channel price management, or demand forecasting (Figure 18).

Figure 18: Plans focus on building out the end-to-end price lifecycle



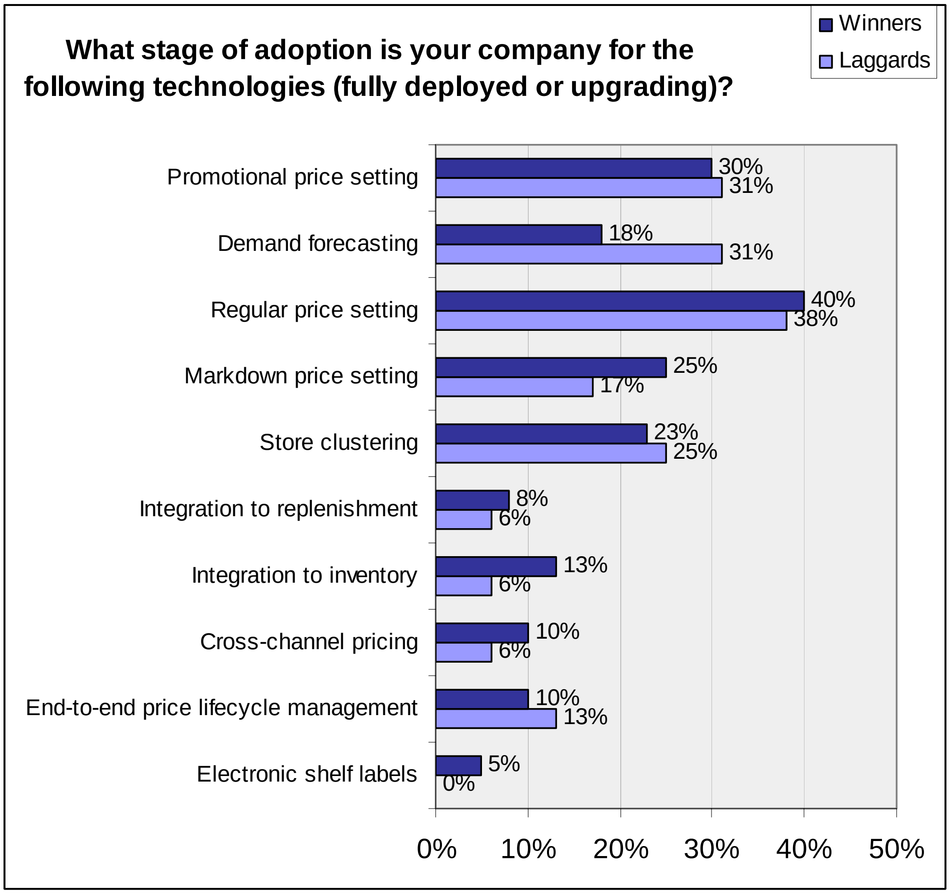
Source: RSR Research

With so much emphasis on building out an end-to-end capability, solutions that focus on building out the "last mile" of execution – like electronic shelf labels and integration to other systems have a lower priority.

LAGGARDS HAVE MORE TECHNOLOGY BUT DO LESS WITH IT

Atypical for our surveys, laggards either are at parity with winners in technology adoption, or lead the pack in adoption of pricing solutions (Figure 19). While there are instances where winners are more likely to have solutions in place, the gap in adoption between winners and laggards is usually much larger, and rarely do laggards already have more technology than their peers.

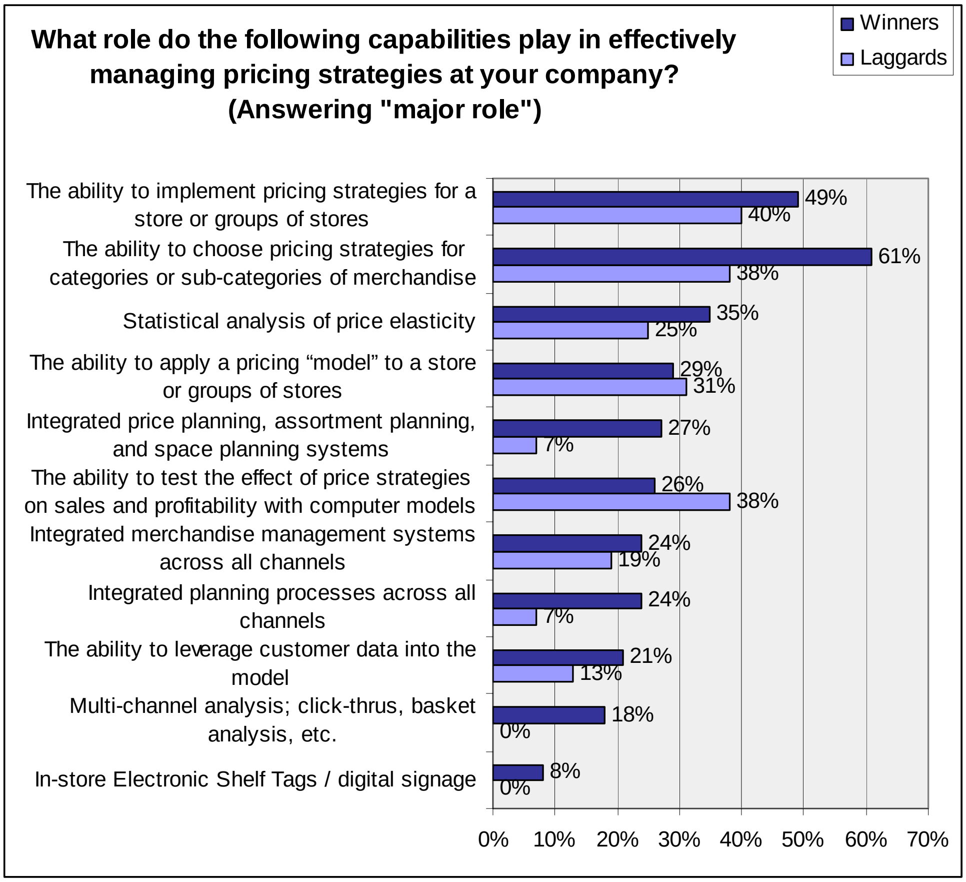
Figure 19: Laggards have already invested in pricing tools



Source: RSR Research

But for all that laggards have as much as, if not more, technology fully deployed, in most cases winners indicate they actually do more than laggards do – from implementing pricing strategies at a more granular level both by store or region and by category or sub-category, to the use of customer data, winners do more with the capabilities they have (Figure 20). The only places where laggards actually do more are purely technology-related: the ability to model potential pricing strategies and then test their effects are the only two areas where laggards indicate that capabilities play a greater role than winners.

Figure 20: Winners Do More With Less



Source: RSR Research

DON'T BELIEVE THE BACKLASH

Just because you have a fast car and a helmet, does not mean that you are a race car driver. Laggards have run out and purchased a lot of pricing tools in the hopes of gaining the quick and impressive margin improvements that such tools have been proven to bring. But just because they have them, doesn't mean they are positioned to use them successfully.

To date, pricing tools have not suffered the "backlash" that most technology solutions encounter when adoption picks up and people learn all over again that technology is not a silver bullet. But with this many laggards out there with the tools, and challenged by cultural barriers, misaligned processes, and burdensome infrastructure, the environment is ripe for a backlash against price optimization from retailers who implemented the solutions badly in an unprepared environment.

Such a backlash is not justified, but with the environment ripe for it, retailers embarking on a pricing solution path will need to tread carefully when gathering information. The tools are just as promising as they were five years ago – if you implement them well and use them right.

SECTION VI: BOOTSTRAP RECOMMENDATIONS

WINNERS LEAD THE WAY

The end-game for pricing solutions will be an end-to-end pricing capability embedded in the front lines of merchandising decision-making, and it will encompass both consumer-facing objectives, like promotion optimization, and supply chain objectives, like optimizing inventory across or within channels. Getting there is the hard part, but winners, as usual, are leading the way:

- **Focus on category objectives.** One clear difference in pricing strategies between winners and laggards is that winners focus on the bigger picture within a category, while laggards cherry-pick, trying to identify the key items within a category that magically unlock margin and customer loyalty success.

- **Avoid isolated groups.** It can be hard to avoid creating an isolated pricing function when you're focusing on starting up a pricing capability – a dedicated group creates focus and makes it easier to make sure that you have the right skill sets in place. But if the group stays isolated, then pricing capabilities don't make it to the front lines of merchandising – where it can have the most impact – and those cultural barriers that you worked through to get price optimization implemented can easily creep back into an isolated environment. Even if you choose to implement a distinct pricing organization, you will need to provide explicit mechanisms for embedding pricing decisions within the merchandising process.

- **Don't ignore inventory.** With all of the focus on customer-centricity and emphasis on promotion optimization right now, it's easy for inventory concerns to get lost in the shuffle, but pricing is part of a 3-sided triangle, along with supply and demand. No one has perfect control over all three, and you ignore any one of them to your cost. The most perfectly designed promotional offer is meaningless if you sell out on the first day. The margin returns from the early days of a pricing implementation can be heady, but don't forget: price influences demand, but it also influences the speed of movement of supply.

- **Plan for end-to-end capabilities now.** It's easy to invest in just markdown optimization, or just promotion optimization. But the next level of business benefits from pricing will come through a holistic view of each product's lifecycle, and the prices needed to support each phase of that lifecycle. Don't lock yourself out of those benefits by taking a piece-meal approach to pricing, because in 3-5 years time, you'll regret that decision – and have to shell out a lot of money to integrate what should have been holistic solution to begin with.

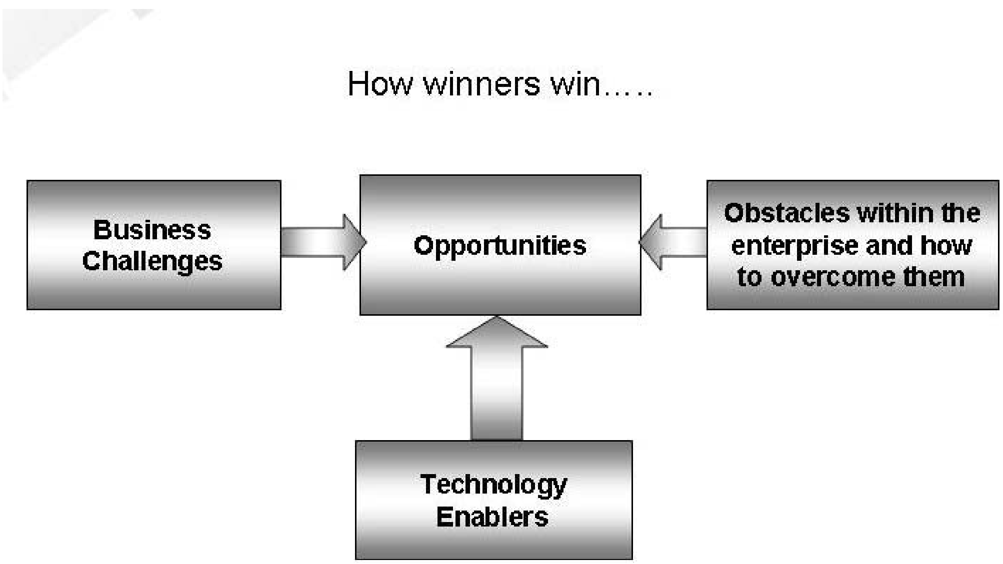
If nothing else, this research has proven that technology is not a silver bullet – for all that laggards have invested in technologies to improve their pricing capabilities, it is winners, with their focus on process and organization, that have reaped the rewards. However, as pricing processes and organizations mature, winners are beginning to turn to a broader role for technology solutions – which means we have yet to see what the next generation of pricing is truly capable of accomplishing.

APPENDIX A: THE BOOT METHODOLOGY

The "BOOT" methodology is designed to reveal and prioritize the following:

- **Business Challenges** – Retailers of all shapes and sizes face significant **external** challenges. These issues provide a business context for the subject being discussed and drive decision-making across the enterprise.
- **Opportunities** – Every challenge brings with it a set of opportunities, or ways to change and overcome that challenge. **The ways retailers turn business challenges into opportunities often define the difference between winners and "also-rans"**. Within the BOOT, we can also identify opportunities missed – and describe leading edge models we believe drive success.
- **Organizational Inhibitors** – Even as enterprises find opportunities to overcome their external challenges, they may find **internal** organizational inhibitors that keep them from executing on their vision. Opportunities can be found to overcome these inhibitors as well. Winning retailers understand their organizational inhibitors and find creative, effective ways to overcome them.
- **Technology Enablers** – If a company can overcome its organizational inhibitors it can use technology as an enabler to take advantage of the opportunities it identifies. Retail winners are most adept at judiciously and effectively using these enablers, often far earlier than their peers.

A graphical depiction of the BOOT follows:



APPENDIX B: ABOUT OUR SPONSORS

DemandTec's suite of on-demand applications empowers retailers and consumer products companies to optimize strategic decisions and collaborate in order to achieve their revenue, profitability and sales volume objectives. DemandTec (NASDAQ: DMAN) customers include leading retailers such as Advance Auto Parts, Best Buy, Circle K Stores, Delhaize America, Giant-Carlisle, H-E-B Grocery Co., Monoprix and Safeway, as well as more than 100 consumer products companies. DemandTec has managed more than one million trade promotion deals between retailers and their manufacturer partners. For more information, please visit www.demandtec.com.

KSS Retail is a leading supplier of predictive pricing intelligence, optimization and modeling solutions to the grocery, convenience retail, chain drug, mass and general retail industries. Merchants using KSS Retail software are able to take an integrated view to model and optimize both regular and promotional pricing, understanding the impact that promotions have on regular prices, and vice versa. KSS Retail provides an intuitive, fast solution that allows optimization to be used on the front-lines of merchandising, thus empowering a merchant with predictive insight as part of their daily workflow. For more information, visit www.KSSRetail.com, or contact us at Info@kssretail.com.

Revionics is a leading provider of price, promotion and category optimization technology for Fast Moving Consumer Goods Retailers. The Revionics Advanced Pricing System (RAPS) generates increased sales and profits through sophisticated consumer demand intelligence and proprietary retail pricing science. The Revionics offering is available to retailers as a Software-as-a-Service (SaaS) subscription offering over the Internet. For more information please visit www.revionics.com.

APPENDIX C: ABOUT RSR

Retail Systems Research ("RSR") is the only research company run by retailers for the retail industry. RSR provides insight into business and technology challenges facing the extended retail industry, and thought leadership and advice on navigating these challenges for specific companies and the industry at large. RSR's services include benchmark reports covering the state of retailer technology adoption for topics ranging from merchandising and supply chain, store operations and workforce management, to customer-facing and multi-channel technologies. Custom research reports provide more in-depth views into topics of industry interest, and advisory services help retailers and technology vendors make the most of the insights RSR provides. To learn more about RSR, visit www.rsrresearch.com.