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by acoustic

Aligning *Pricing & Promotion* Optimization Ambition to Operational Reality

2024 FMCG Retail Readiness Report

IN PARTNERSHIP WITH RSR Retail Systems Research

Executive Summary: Perfect FMCG Pricing

In hyper-competitive times, shoppers are proving even more difficult to please than ever. They've prioritized price like never before and use mobile search and apps to find the price they are willing to pay for any item – large or small – regardless of which retailer has that price.

How a Fast Moving Consumer Good (FMCG) retailer prices and promotes its goods has always been an invaluable component of its overall go-to-market strategy. It has historically been - and can still be - a foundational block to customer loyalty.

Yet, shoppers have become so inundated with offers from retailers trying to compete for this loyalty that they've turned a deaf ear to the ceaseless promotional chatter directed at them. RSR conducted multiple surveys of consumers in 2023, and discovered that shoppers, as a whole: value price above all else, and are rapidly growing frustrated with how little retailers seem to be learning about how they like to shop. They've been providing retailers with enormous amounts of personal and shopping information for years - only to have seen little relevance in return. Seemingly arbitrary prices, decidedly bland promotions are the norm.

As a result, we partnered with RSR to take the industry's temperature.

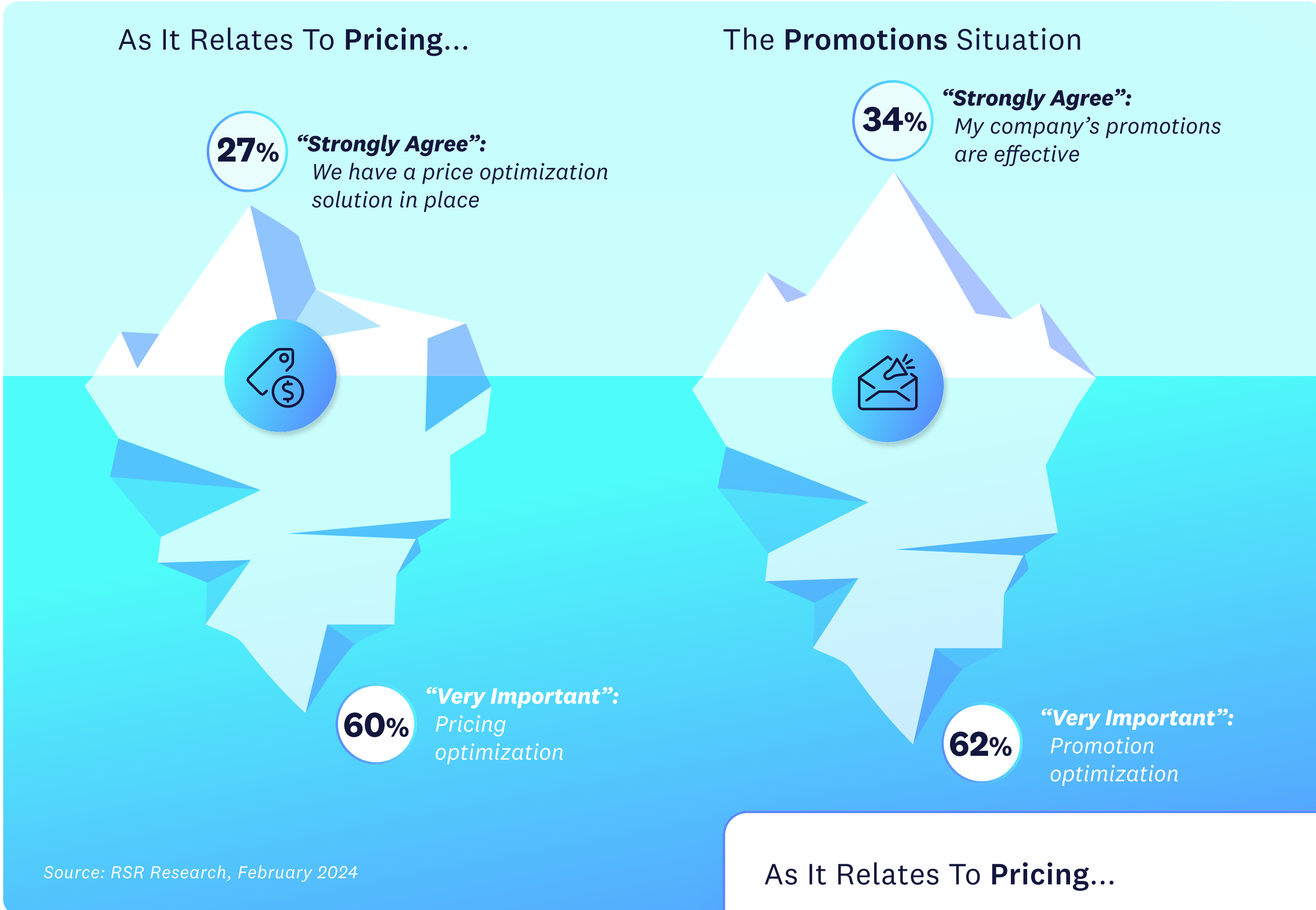
Our Hypothesis
Organizations have made significant progress in identifying the relevant price optimization levers and scale of change but have not sufficiently invested in the enablers that will unlock transformation at the necessary speed and scale.

Validating Our Hypothesis
We surveyed 100+ retail leaders across FMCG and general merchandise (GM), representing more than $1 billion (USD) in revenue. Our research highlights a stark contrast. While companies know the rising need to evolve in line with a new reality, the operational fundamentals necessary to enable a digital transformation are not yet in place.

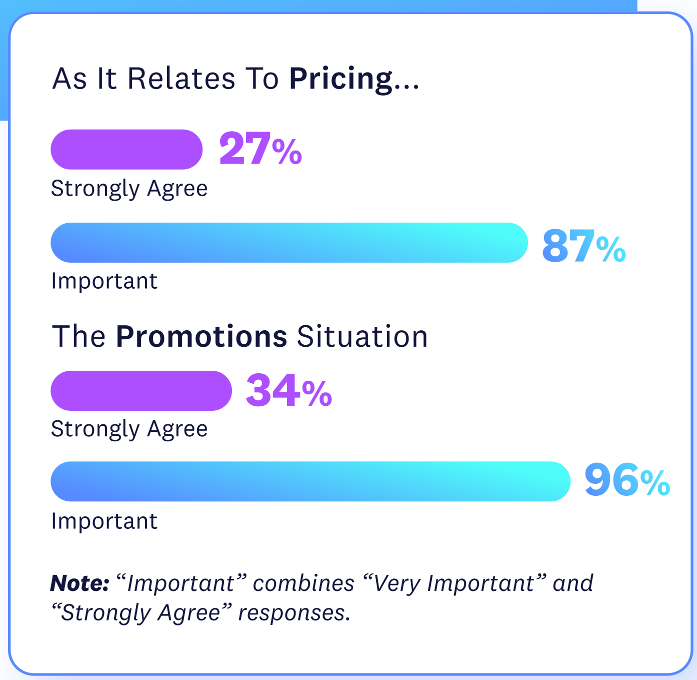
The first thing we wanted to know: what kind of importance do retailers ascribe to the capabilities required to offer more relevant pricing and promotional offers to their shoppers? And just as importantly, where are they currently in their maturity to realize these capabilities?

The very first thing we uncovered: **a wide chasm between what retailers say is important - and what they have the capability to execute upon** (Figure 1).

Figure 1: The Pricing State of Affairs



Source: RSR Research, February 2024



When given the choice, 98% of retailers say pricing optimization is an important component to achieving their pricing and promotion initiatives (60% of them, pictured above, cite this as "very important.") Yet only 27% of our grocery respondents strongly agree that they have a price optimization solution in place that can help them meet these demands. Put simply, this doesn't work. Most retailers are just touching the tip of the iceberg.

To further compound issues, this same trend of high value/low ability extends to their ability to offer effective promotions to increasingly demanding shoppers (Figure 1).

The Largest Grocers ($5B+) Have Differences

Place a much higher value on Dynamic Pricing than any other revenue band (67% to small retailers' 32%)

Clearly view Dynamic Pricing as a way to manage/move product more intelligently, helping to avoid/reduce waste.

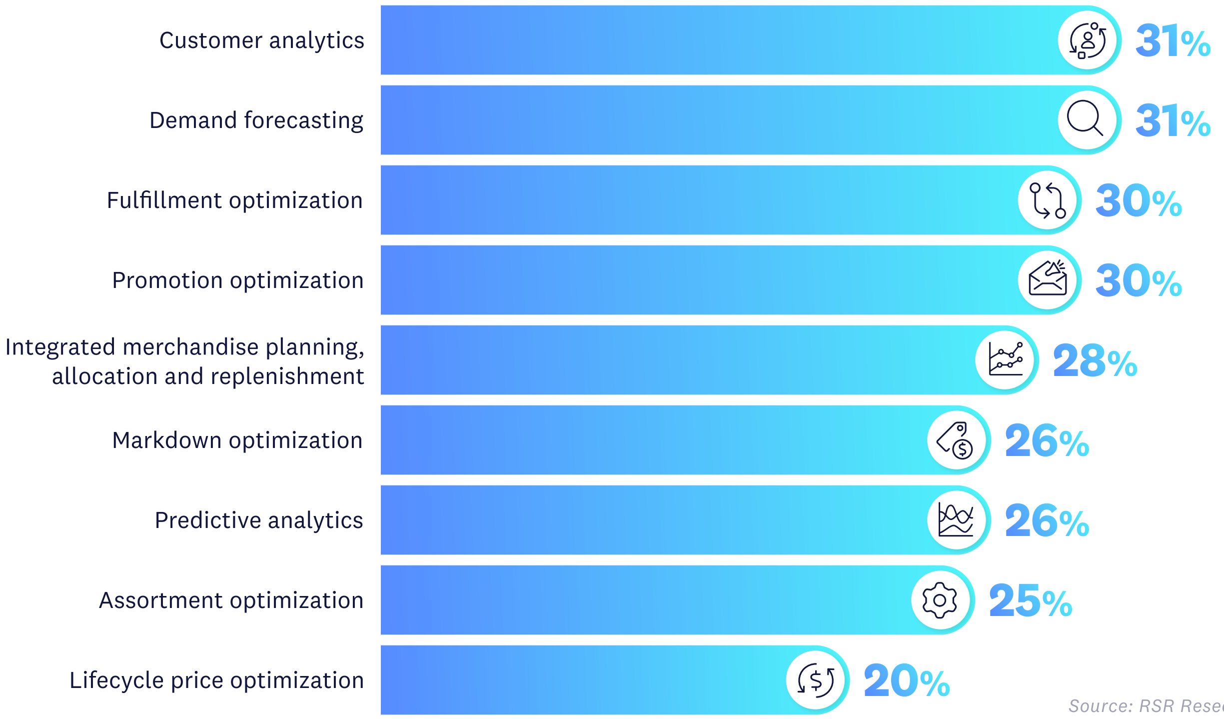
Much more challenged by dirty data issues than their smaller competitors. 69% report top inhibitor to better pricing is lack of clean price, competitor, and purchase data.

The most likely revenue band to have a price optimization solution in place – but still only 42%. Even the biggest retailers have work to do.

Once we probe further and ask our grocery respondents to self-assess their current ability to meet customer demand, however, we uncover a more systemic root to such problems: retailers lack the prerequisite expertise necessary for success in virtually every corresponding field (Figure 2).

Figure 2: Houston, we Have a Problem

How would you rate your organization's maturity when it comes to the following merchandising tools and techniques?



Source: RSR Research, February 2024

Bridging The Gap Between Ambition & Expectations

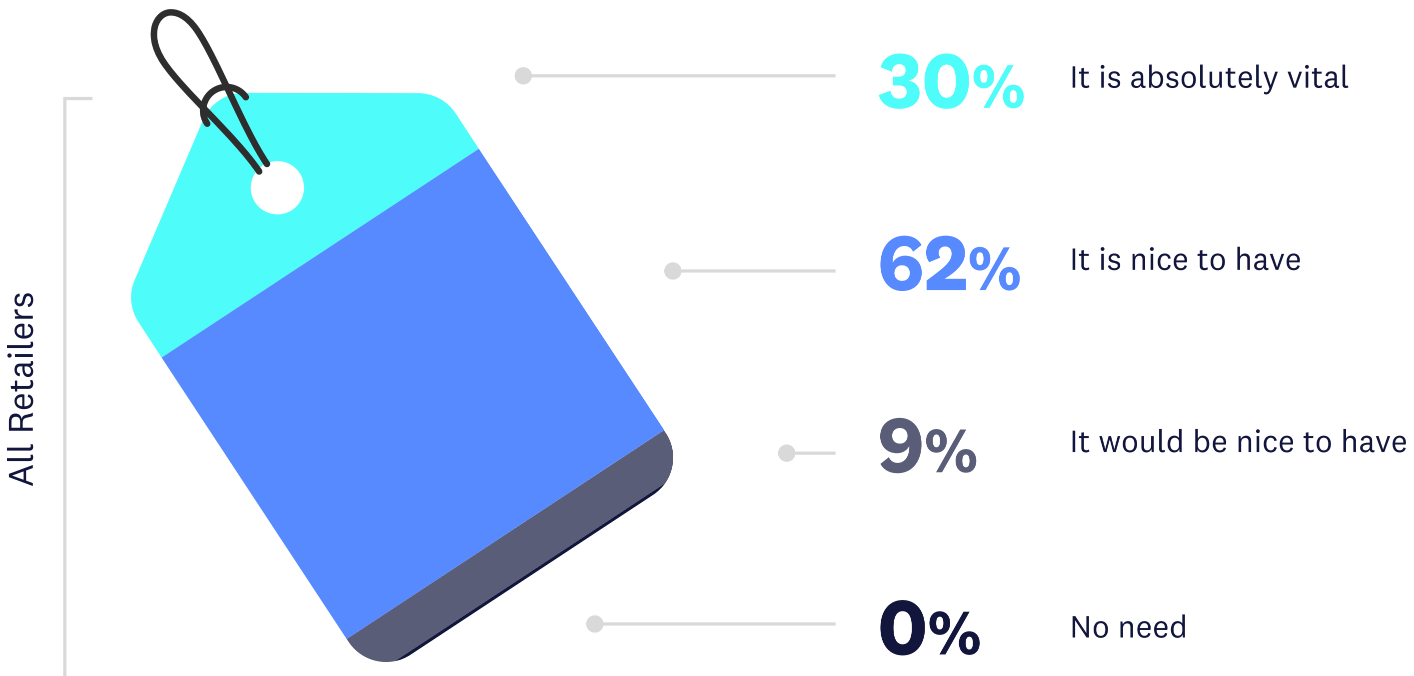
The ability to glean insight from customer analytics, the ability to confidently forecast demand – *even the ability to optimize product fulfillment* – all are required to confidently set an effective price. Without the ability to deliver on these bread-and-butter issues, retailers are losing customers to retailers who can. **Yet less than a third of our grocery respondents report full confidence in these areas.**

FMCG retailers are in a pickle. Perhaps most shockingly, only **1 in 5 say they can currently optimize price across an item's lifecycle.** How can this be?

As it turns out, our retailers' views on what it takes behind the scenes to effectively set prices is out of date (Figure 3).

Figure 3: Still More Revealed

Which of the following best describes your opinion of pricing optimization?



Source: RSR Research, February 2024

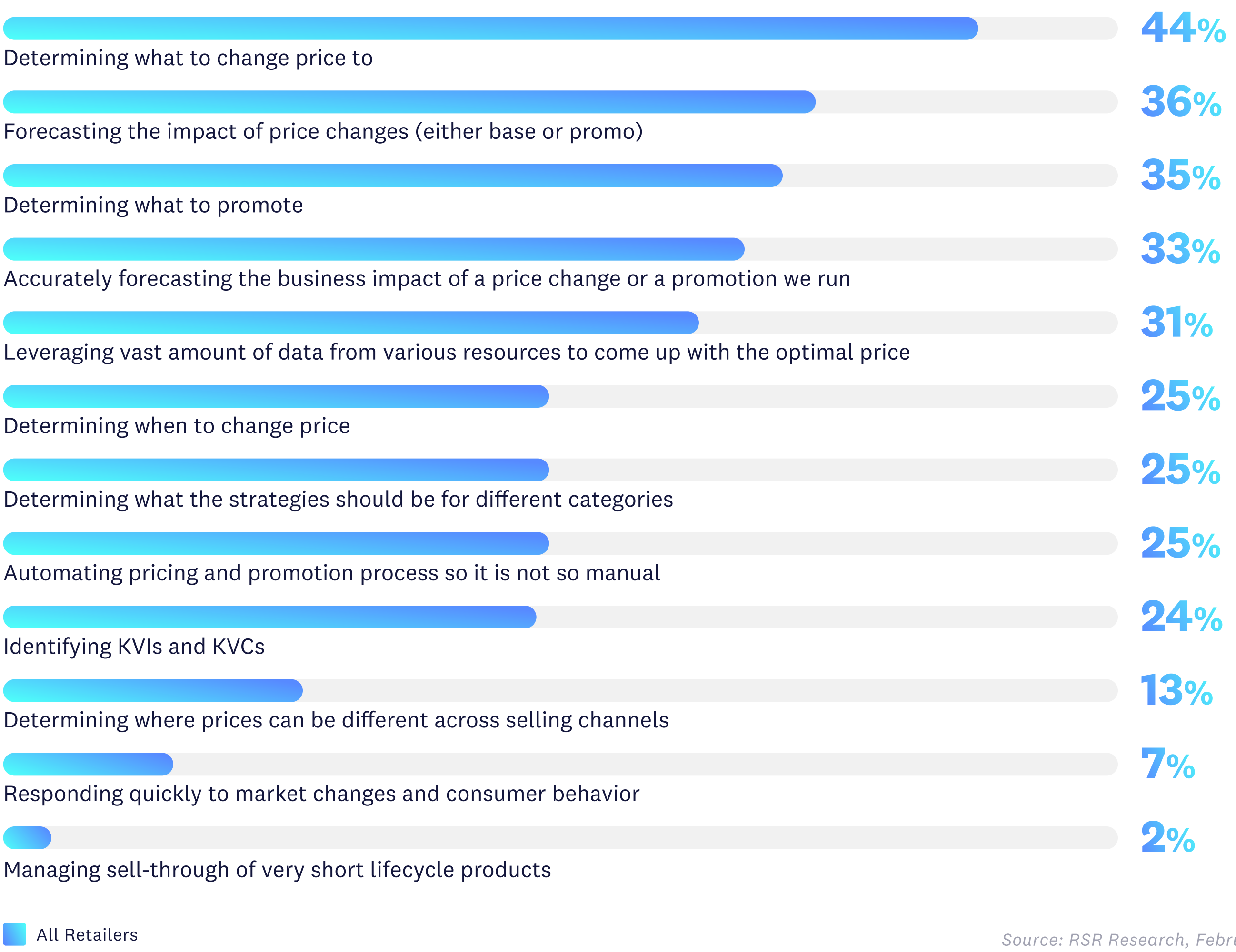
Most FMCG retail respondents view price optimization technologies as a “nice to have” feature. Less than a third see it as **absolutely vital.**

Thinking of price optimization as a nice-to-have feature in 2024 seems woefully outdated. It will be virtually impossible to meet customer demand if a retailer still has interpretive error gaps in its pricing policies. In short, those days are behind us.

With this in mind, it only makes sense to find where retailers perceive the biggest challenges to better pricing and promotion practices. As we see in Figure 4, it all starts at the top.

Figure 4: Honesty 101

Which are the TOP THREE most challenging aspects of pricing and promotion for your organization?



Source: RSR Research, February 2024

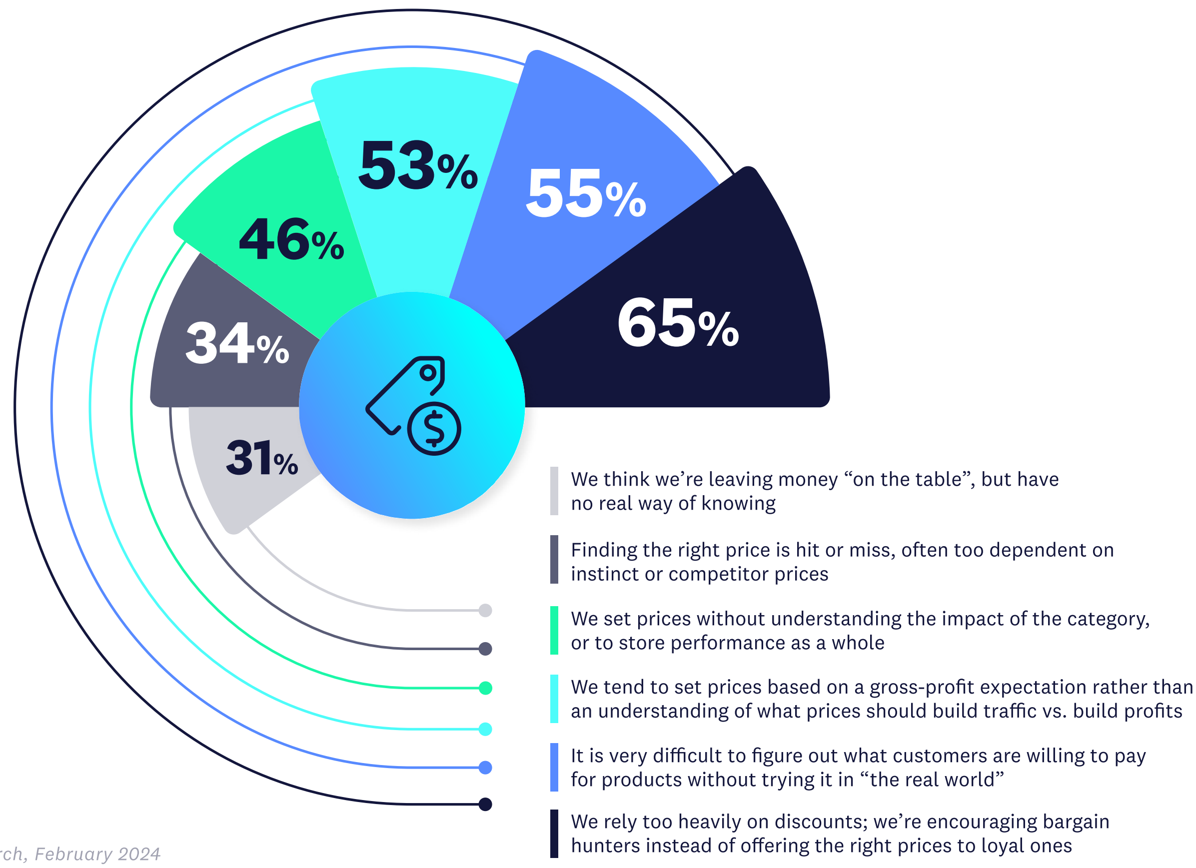
Our grocery respondents are candid. When given a list of a dozen options and asked to pick only three, nearly half go right to the heart of the matter. 44% of retailers say they are challenged to know what a price change should even look like. If they decide to make such a change? Their second most popular selection is the ability to forecast the impact that change will have.

These are problems fully based in reality. Grocers may yearn for the days of relative tranquility they enjoyed from post WWII era until the last decade, when supply chains became more stable with the passage of time and customers didn't have price checking and promo-hunting technology. Instead, recent years have brought increasingly unpredictable supply chains shocks, coupled with a well-documented increase in consumer adoption of digital technology.

Add in what our research shows is a steady decline in any patience shoppers might have for retailers' challenges and the result is cacophony. Retailer shave trouble knowing what to promote, what to change prices on, what to change prices to, and how to make sense of the vast amounts of data they are collecting to make sense of it all. Figure 5 only further codifies their current predicament.

Figure 5: Bargaining Based on Bargains

What are the TOP THREE business challenges that would cause you to consider adopting pricing optimization?



Source: RSR Research, February 2024

It's hard to get ahead when data like that evidenced in the above chart is status quo. Retailers cannot thrive – or survive – by simply offering discounts blindly, in grocery or otherwise. The recent demise of several major chains should serve as proof to this. Nor can they set prices based purely on a gross-profit expectation instead of a true understanding of which prices should be building traffic and which should be building profits. These are just not acceptable practices any longer. Retailers need help. The good news is that they know it. Let's now examine some of the best ways they can move forward.

Why 'Optimization' Matters to FMCG Now More Than Ever

Many of the largest Fast Moving Consumer Goods and General Merchandise retailers have been using *price optimization* technologies for decades to determine which products are **traffic-builders** and which are **profit-builders**. Retailers tried to achieve a balance between the two which is both good for consumers and the business. To a lesser extent, those same retailers implemented promotion optimization solutions with the same objectives in mind, with the added complexities associated with time-constrained and partner-funded campaigns.

But in today's hyper-competitive environment, *optimization* faces new requirements. Retailer **decision cycles** have sped up remarkably. It's not enough to review product categories every few quarters – consumer demands change too quickly for that, and e-commerce giants like Amazon are relentless as they attempt to disintermediate traditional retailers with speed and agility (and, consumers have shown a great willingness to view Amazon as the *default*).

Consumers are demanding that store assortments, pricing, and promotions are much more focused now.

As a result of dynamic consumer demand and the speed and agility of competitors, retailers know that they need to move more quickly than ever before and can't wait "until the next cycle" to update assortments, pricing, and promotions.

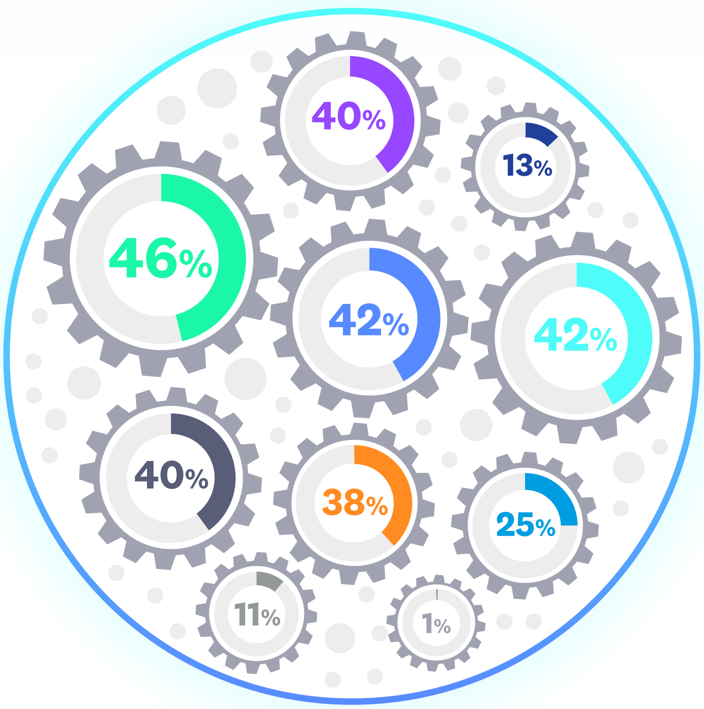
Optimization has moved from being a specific analytical step to maximize sales and profits to being intrinsic to every phase of merchandise assortment, allocation and replenishment, pricing, and promotions planning.

The best way for retailers to address challenges to adopting *optimization* as a concept is to encourage better communication between merchandising, marketing, and the sales channels about the benefits to be derived and how to achieve them (Figure 6). One retailer noted that an immediate benefit from implementing price optimization in several fast-moving product categories was that the category managers and pricing analysts began working more closely with each other. That's a win, and the more the retailer uses the tools, the more collaboration will be possible.

The reason that improved collaboration is so important is because *optimization is a reiterative process*. Retailers see phased rollouts as a way to develop more sophisticated capabilities over time – and of course, to make course corrections when results "on the ground" demand. When people are working together using the same insights as a guide, corrective iterations are faster and more impactful to the business.

Figure 6: Making Optimization Work for the Business

Please select the TOP THREE (3) ways you believe your company can overcome barriers to 'Optimization'



46% Better communication and education of merchandising, marketing, and channels

42% Phased roll out with milestones

42% Vendor-sponsored trial by category and/or location prior to commitment

40% Tailor a technology solution to our business process and needs

40% Build up progressively more sophisticated pricing capabilities over time

38% Improved integration technology tools

25% Better proof of concept from the technology community

13% Executive buy-in

11% Better training to improve pricing skill sets

1% Re-engineered business processes

Source: RSR Research, February 2024

But many retailers are still unsure about how to take the first step so they seek vendor support for proof-of-concept projects before making any big commitments. While this is hardly surprising given consumer packaged goods (CPG) vendors' hands-on involvement in general category management processes, retailers can't wait for their trading partners. RSR believes that retailers need to push the vendors to collaborate – not the other way around.

Finally, retailers want better integration tools between price and promotion optimization solutions and legacy systems. Today's price optimization solutions are no longer an invisible external process that determines recommended prices based on sales lift or drag factors. In the past, implementing recommendations from optimization analyses involved manual handling. But with faster analysis and decision cycles, automated feeds to merchandise and price management systems are vitally important.

Unlocking Pricing Potential

With pricing being such a fundamental component of every retailer's merchandise management portfolio, it would be fair to expect that retailers would be confident in their tools and abilities. But that is clearly not the case. As we saw earlier, retailers' top challenge to pricing and promotions in the current state is in "*determining what to change price to*".

An almost identical number of over-performing Retail Winners and their lesser-performing competitors give this issue the same weight (Winners 44%, Others 43%).

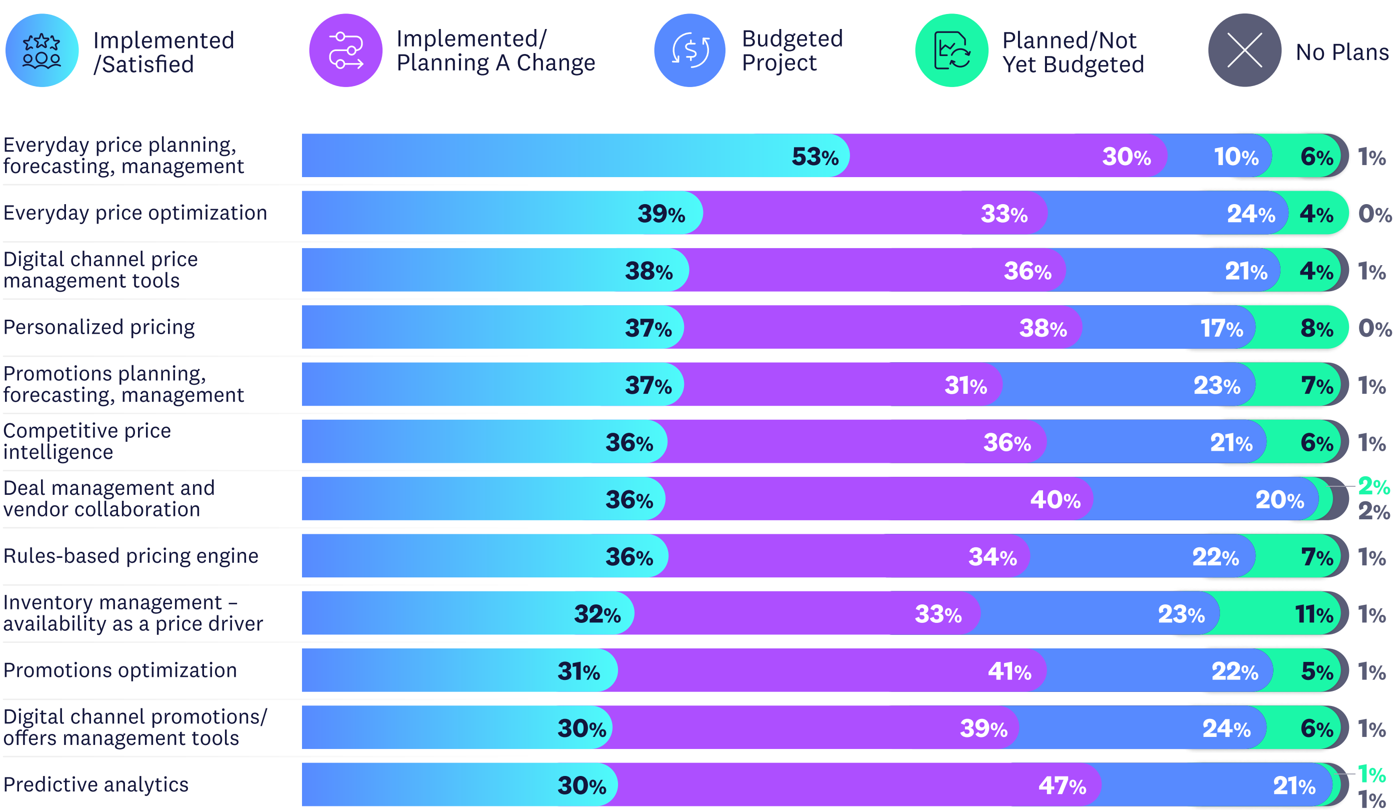
A similar number of retailers express a concern that "*increased pricing and promotional aggressiveness from competitors*" is putting them ata disadvantage (Winners 49%, Others, 51%).

These concerns help explain why retailers are dissatisfied with the technologies in place (Figure 7).

With the exception of "*Everyday price planning, forecasting, management*", no technology that we asked retailers to rate received an "implemented & satisfied" vote by 50% of those we surveyed.

Figure 7: Very Little of the Current State is Satisfactory

Please rate your adoption/plans for the following technologies:



Source: RSR Research, February 2024

A Word About FMCG Retail Winners

So far, this report has looked at FMCG retailers' insight in aggregate. However, in their work, RSR frequently cites differences between retailer over-performers in year-over-year comparable sales and their competitors. We call sales over-performers: "Retail Winners."

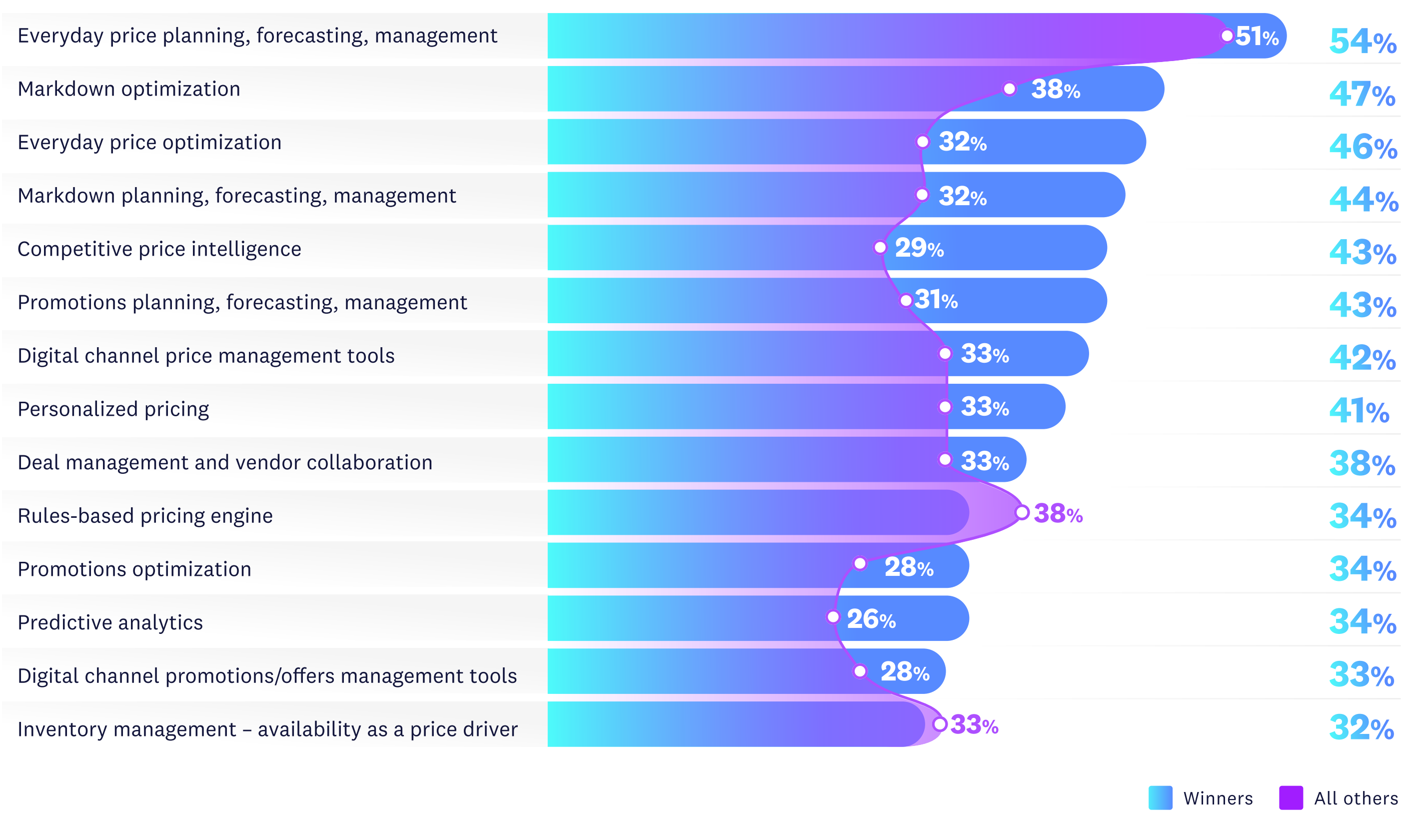
> RSR's definition of these Winners is straightforward. Assuming industry average comparable store/channel sales growth of 5%, we define those with sales above this hurdle as Winners, while those at or below this sales growth rate are referred to as "all others."

In this project, as in nearly every study RSR has ever conducted, Winners show us that they don't win by accident: their above-average sales performance results from a differentiating set of thought processes, strategies, and tactics. As this report proves, they also approach pricing differently (Figure 8).

Beyond one point of concurrence, more retail Winners than other retailers are satisfied with their current solutions – but that is faint praise. In no case are Winners happy with what they've got, and for non-Winners it's even worse. So, it can hardly be said that Winners have a strategic advantage. Clearly, retailers know they need to re-invent their pricing and promotional capabilities.

Figure 8: Barely Satisfied

'Implemented & Satisfied'



Source: RSR Research, February 2024

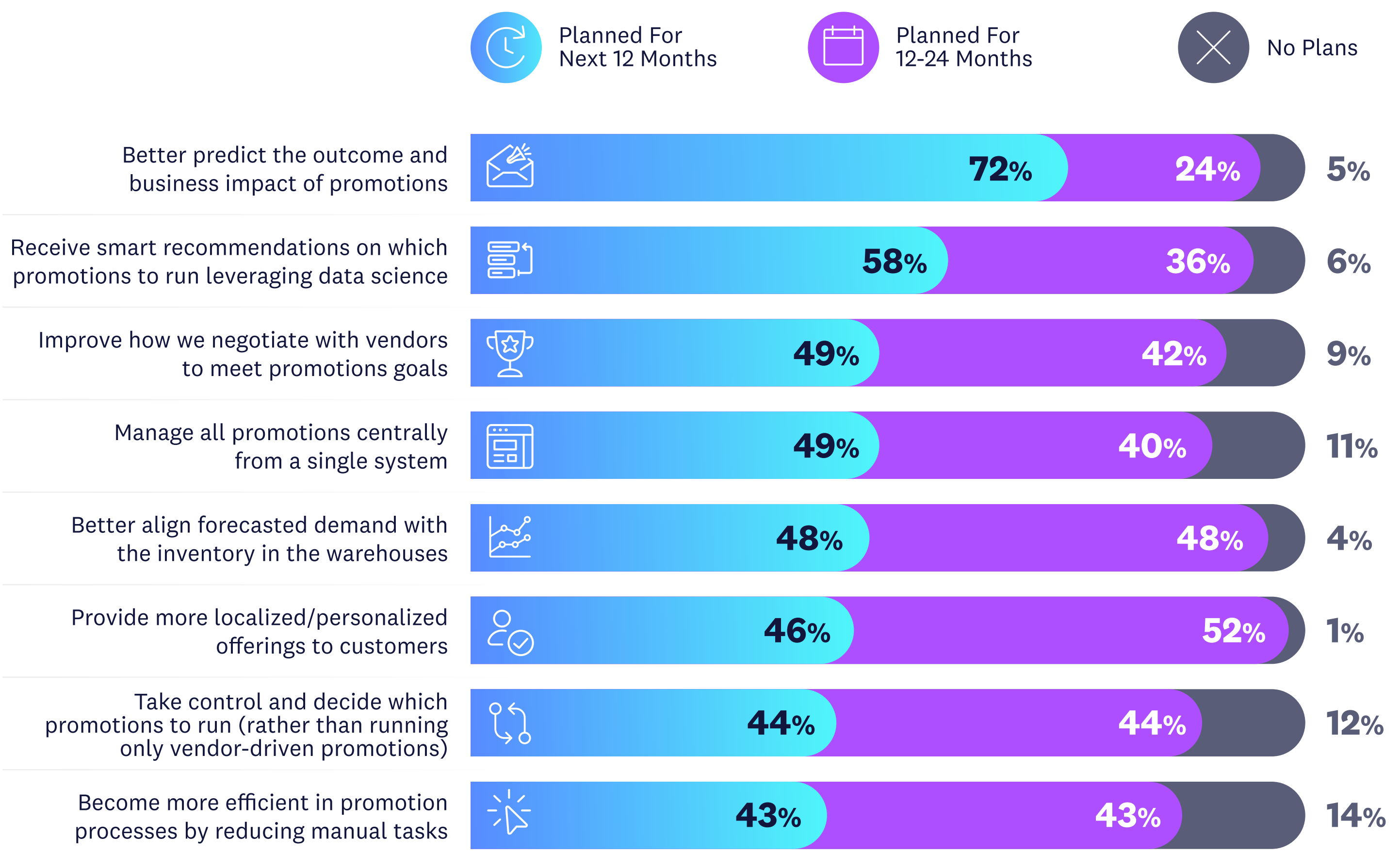
Promotion Evaluation to Maximize Results

Earlier in this report, we noted that FMCG retailers complain that "*we rely too heavily on discounts; we're encouraging bargain hunters instead of offering the right prices to loyal ones*" (Figure 5). Given the hyper-competitive nature of the retail environment today, it's not surprising that retailers are looking to invest in tools to improve planning and effective execution of promotions.

What is surprising is the pressure that retailers are putting on themselves to deploy predictive analytics to help them improve promotions' effectiveness. In fact, the top two investments retailers plan to make relate directly to new analytical capabilities (Figure 9).

Figure 9: Predictive Analyses = More Effective Promotions

To what extent are you planning major investment in the following promotions tools?



Source: RSR Research, February 2024

But averages can be deceiving. Although a similar number of Winners and others indicate that they plan to implement capabilities to enable them to better predict the outcome of promotions, the similarities end there (Figure 10). Winners are far more likely to take those capabilities one big step further, to "*receive smart recommendations on which promotions to run leveraging data science*."

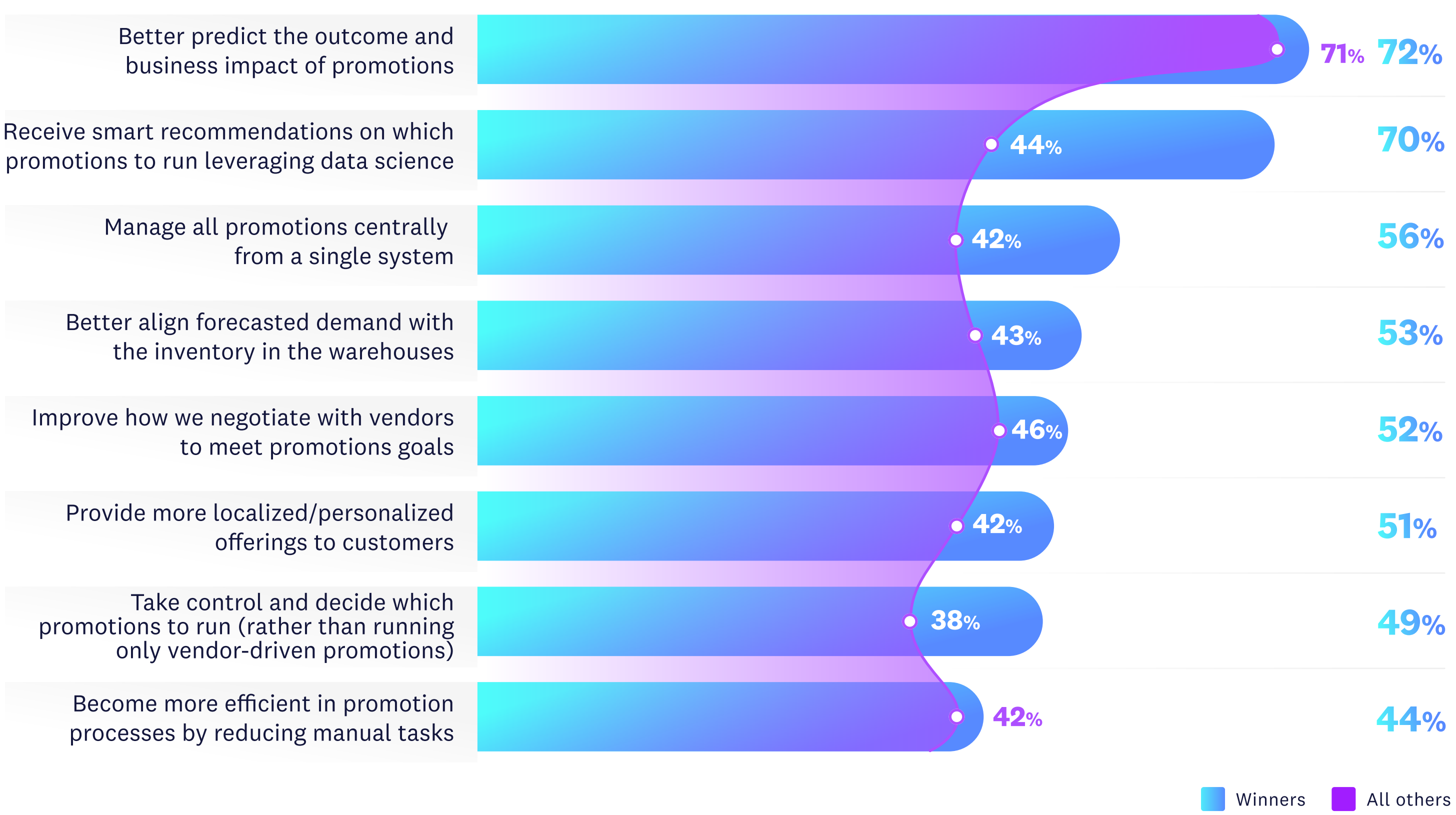
The difference is discordant with a data point in Figure 5, where retailers told us that "*it is very difficult to figure out what customers are willing to pay for products without trying it in 'the real world*'".

Both Winners and others agreed (Winners 54%, Others 56%). But only 44% of non-Winners seek to use data science to make smart recommendations about what to promote compared to 70% of Winners.

That's a big miss on the part of non-Winners, and demonstrates why Winners tend to keep winning. Throughout the research, RSR consistently found that over-performers understand the strategic value of data and analytics, where non-Winners tend to think more tactically. This is clearly one of the cases.

Figure 10: Why Winners Keep Winning

Investments For Promotion Planning Techs – Next 12 Months



Source: RSR Research, February 2024

Weaponize your Pricing. The Optimization Advantage

Failing to take advantage of the science behind price optimization technologies is a true inhibitor to retailers' success. Over-performing retail "Winners" – particularly those who operate in the FMCG and GM verticals – have been taking advantage of it since the late 1990s.

The solutions have advanced by leaps and bounds in the last 10 years because of the recent improvements made to *data science*. The business processes enabled by those solutions must be much more responsive to rapid changes in both supply and demand. Full product category reviews need to occur much more frequently than in the past, as business needs dictate, and promotions planning should be much more targeted to those locations – and customers - that are most likely to take advantage of the offers presented.

The good news is that the solutions available today are accessible to more retailers-price optimization is no longer a tool only for the largest businesses. What was once perceived as something reserved for companies like Walmart and Kroger is now available to mid-sized retailers, too.

Based on what we've seen in this research, we offer the following recommendations:

There is No Time Like Now to Get Started
The greatest impediment to adopting the science of price optimization is *organizational inertia*. Too often, retailers find themselves in a holding pattern or have excuses not to act. **Inertia is the enemy.**

Leadership Matters
Retail Winners take strong line-of-business leadership for granted. But an executive-level champion goes a long way towards overcoming the inertia standing in the way of adoption. Whether it's the VP of Merchandising who wants to promote a more agile response to the hyper-competitive conditions in the market, the CFO who wants to maximize revenue and profitability, or the CEO who believes in the strategic competitive advantages that data science creates in general, price and promotion optimization needs a champion. However, developing a step-wise approach towards more sophisticated capabilities is also important to get to"good pricing."

The Science is Proven
Price and promotions optimization solutions have improved remarkably in the past several years as a result of data science tools like artificial intelligence (AI)/ machine learning (ML) and because of the availability of external data like competitive intelligence, market, weather, and customer data to better model the impact of price and promotion strategies. Retail Winners and their trading partners are already taking full advantage of these capabilities, and there are testimonials and case studies available that can help the company understand the potential benefits.

Be Wary of "Shiny Objects"
The data science behind price and promotion optimization can hardly be called a "shiny object" – but today's modern solutions use advanced capabilities made possible by AI/ML – which is certainly new and exciting. But it's important to keep in mind that the most successful price and promotion optimization solutions have also codified a tremendous amount of human domain expertise in merchandising practices. Although newcomers to the price and promotion optimization space may be able to make new technologies perform amazing analyses, they often lack that all-important domain expertise.

Fast-track to Success with Outside Expertise
The data analyses required to establish rollout priorities are complex – most retailers have to contend with potentially millions of store/SKU combinations, new market dynamics, and competitive intelligence. The learning curve can be steep, but outside expertise is available to help retailers get up to speed more quickly – and train in-house staff to be self-sustaining in the long run.

Collaboration is Key
One of the most desirable outcomes from the implementation of price and promotions optimization is *improved collaboration* inside of the company, and between retailers and their trading partners. Within the enterprise, adoption of new analyses and supporting technologies fosters greater collaboration between category managers, price analysts, financial analysts, and sales channel operations. Promotion optimization fosters greater collaboration between merchants, marketing, and sponsoring vendor partners. Breaking down the silos between those entities has proven to be a positive by-product of solution adoption for retail Winners.

Seek Out a Strategic Business Partner
Price and promotion optimization is a highly specialized endeavor that has equal parts data science and business expertise. Retailers should look for a partner that will be there for the long haul – a company that will keep up with changes in both the business practices and the underlying technologies. Successful solution providers add to their expertise with every implementation – and each succeeding retail client should benefit from that accumulation of knowledge.

Discover value in our report? Interested in more research or benchmarking your organization?

Connect with us to schedule a tailored meeting and elevate your strategic initiatives.

A pioneering leader for decades, DemandTec continues to usher in the new era of retail pricing technology. With its ML-powered pricing, promotions, markdowns, and collaboration solutions, CPG and retail partners can balance real-time shopper demand with business objectives to drive sustainable, profitable revenue growth. www.demandtec.com.

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