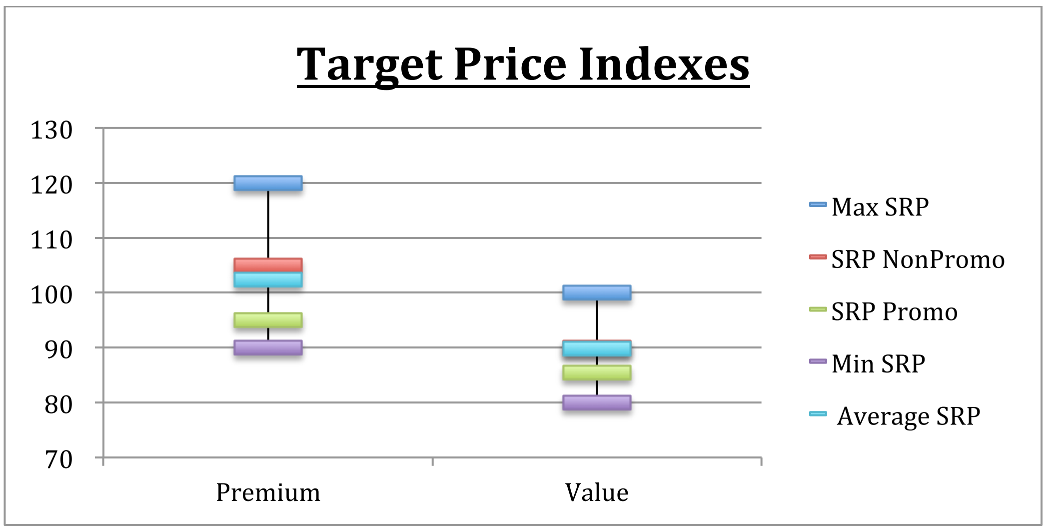
Pricing Tool Guides

Setting Strategic Target Price Indexes

It is easy to fall into the trap of viewing prices as points in the market place, when in fact they are ranges. It is also easy to set indexes versus internal or external benchmarks without clarifying how the index is defined and how it will be monitored. This Tool Guide illustrates how to clarify the assumptions behind price index guidelines. Another Tool Guide explains how price ladders for actual and suggested retail pricing can help monitor how execution is conforming to price strategy.

The result of the Price Index Tool could look like the following:



How to Use:

Step 1: The first step in setting an index is to select the SKUs or the product lines that one wants to compare. If the goal is create guidelines for how internal SKUs are priced versus one another, then putting those SKUs side-by-side is the starting point. If the purpose is to create external indexes, then pairing one's own SKUs versus a competitor is the starting point.

Step 2: The next step is to identify the benchmark's in-market prices over a recent time period or in snapshot across customers. If there is information as to whether a price is promoted or non-promoted, that is also important to record.

Step 3: The third step is, preferably informed by pricing research, what the target retailer prices should be going forward. The price index tool identifies 5 kinds of prices.

1. **Maximum Price:** The absolute maximum that one wants to see in the market place for one's own SKUs. This might be particularly important for SKUs that have a value proposition that could be undermined if priced too high.

2. **Non-Promo Price:** The targeted non-promoted price. This is the price for products when not sold on promotion. This is meant to be more of an average for this type of sale, with the maximum in step 1 providing a ceiling.
3. **Promoted Price:** The targeted promoted price should be an average for the promoted prices that one expects to see in the market.
4. **Minimum Price:** This is the floor prices below which one would walk away from a sale. It is important for many reasons: avoiding provoking unintended competitor responses, avoiding cross-customer conflicts or dissatisfaction, establishing boundaries for the sales force.
5. **Average Retail Price:** The average SRP will require an estimate of the percent of promoted and non-promoted sales. In the simple version in the tool, this is not necessary, but there is a weighted average version that allows this input as well.

One should consider how enforceable these targets are, especially with an intermediary is setting the prices to the end customer. In the US, for instance, pricing to the end customer is at the sole discretion of the customer and so these targets can, in most cases, only be suggested in some situations. Another consideration when setting these targets is how they targets relate to current market realities. If they vary from current pricing in the market, one must ask what one will do/ can do to move prices closer to the targets. A final consideration is to clarify how one will monitor these prices in the market place. If the prices are not visible, then how can they be monitored? And if they are visible, what would one do to remedy divergences vs. target?

The fourth step is to review how the different SRP price points overlap with the benchmark. In the tool example, there is an overlap between the minimum and promoted prices for the premium product with the non-promoted pricing for the value product. This might be acceptable if the purpose is to entice the value product consumers to trade-up during promotions on the premium product. If that is not the strategy, however, then it might be worth reexamining the target prices for the two SKUs to better match one's promotional objectives. The tool has a visualization of the price points that makes this comparison easy.

A fifth step is to look at the calculated price indexes that are created by the targets. This helps clarify which type of price one is indexing against – non-promoted, promoted, average? It is important to realize as well that it is possible for one's benchmarks to be equivalent on a non-promoted and promoted price basis, but for the average to be different because of the percent promoted mix. This percent promoted mix is a function of frequency of promotion and relative lifts while on promotion. Understanding this and thinking through what this means for monitoring and enforcement is an important task when setting the targets.

The sixth step is to translate these indexes into guidelines for execution and to set up systems to monitor them. With the above information, one can create ideal price architectures across internal and external benchmarks for monitor actual prices for deviation vs. the targets via price ladders.