

Broad Grocery Price Cuts May Not Pay

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What works for Wal-Mart may not be good for the nation's grocers.

That's the bottom line of an extensive study of whether supermarkets should adopt the "everyday low prices" strategy that helped propel Wal-Mart Stores Inc. to become America's largest retailer. The grocery industry is hotly debating the approach, and some big consumer-product manufacturers are backing it.

But University of Chicago researchers next week will tell supermarket executives that everyday low pricing probably can't match the profits generated from most grocers' traditional traffic builder—weekly specials on a few products and higher prices on everything else.

In the experiment, a marketing research team from the university's Graduate School of Business manipulated prices in 19 product categories in a Chicago-area supermarket chain. Some stores used the standard pricing approach, called "high-low" in the industry. Others were converted to everyday low pricing, in which prices were reduced and kept low.

Higher Margins

The result: Stores featuring everyday low pricing rang up slightly more sales but a lot less profit than the high-low stores. Overall, profits in the categories that used everyday low pricing were about 17% below what grocers would have made with the traditional high-low approach, the researchers calculate. They attribute the difference to the higher profit margins on items that aren't on sale.

"Everyday low pricing may not be the marketing panacea believed," says project manager Mary E. Purk. "In fact, so striking are the findings that they raise questions as to whether stores that say they are offering everyday low pricing really are. If they are, in many cases it is probably working to their detriment."

The study's conclusions may stiffen the resolve of grocers who oppose efforts by Procter & Gamble Co. and a few other big manufacturers to bring everyday low pricing to the typical supermarket. Advocates argue that lowering prices on major items every day will help build brand loyalty, fend off private-label inroads and reduce manufacturing and inventory costs.

'EVERYDAY LOW PRICING may not be the marketing panacea believed,' says Mary E. Purk, project manager for a University of Chicago supermarket pricing experiment. 'In fact, so striking are the findings that they raise questions as to whether stores that say they are offering everyday low pricing really are.'

In exchange, the companies want grocers to give up much of the promotion money they now get to put certain products on sale — a tradeoff that leaves many supermarket operators skeptical. Some doubt they will end up with as much profit in the till.

Many consumers also seem to favor high-low pricing. The researchers found that specials add excitement to what can be a dreary chore. "Everyday low pricing goes against what shopping's all about," says Stephen J. Hoch, a marketing professor overseeing the multiyear study.

Other findings about pricing in the research study show that:

- Income alone doesn't determine the price sensitivity of consumers. The proximity of the nearest supermarket competitor is also a big factor. Stores with many elderly, minority and working women customers are under more pressure to keep prices down.

- Customers buy more of a product when it's featured in multipacks, even though the per-unit price isn't a bargain. For instance, when paper towels were marked "2/\$1.49," sales far surpassed those of single rolls marked "75 cents."

- Requiring shoppers to use in-store coupons to get a discount is much more profitable for grocers than reducing the product's shelf price. The researchers found that only 58% of shoppers buying a product used a coupon, even though they merely had to take it from the shelf to the cashier. The other 42% paid full price.

- Some items are more conducive to discounting. Frozen entrees and soft drinks moved more quickly when put on sale than did dish detergents. People aren't going to wash dishes more often if soap is cheaper, whereas they probably will drink more soda pop if it's sold at a discount, the researchers say.

Even Spread

The researchers analyzed eight months of scanner data to reach their conclusions, which will be reported next week at the Food Marketing Institute's show in Chicago, the supermarket industry's biggest.

The researchers are also likely to deliver a message about pricing that may make some in their audience squirm: Many grocers are mispending their marketing dollars by spreading them equally across an entire chain. Instead, the team will contend, supermarket operators should be allocating different amounts according to consumer needs and characteristics of a store's "micro-market."

In some of those markets, the emphasis should be on price promotions, the researchers say. But in others, customers may be more interested in the quality of produce and meats, the variety of goods and other shopping amenities.

Too often, the main reason retailers adopt certain prices is to match their competition. "They ought to pay more attention to the people coming into their stores," says Mr. Hoch.

In their analysis of everyday low pricing, the researchers moved prices up and down 10% in the key categories — which included beer, cereals, cigarettes, detergents, frozen entrees and juices and soft drinks — and accounted for about 30% of an average store's sales. In stores with everyday low pricing in those categories, prices were dropped an additional 10%. In stores with a high-low strategy, prices were raised 10% to test consumer response.

No Evidence

Some results were surprising. For example, when prices of Budget Gourmet

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frozen entrees were dropped further in everyday low pricing stores, unit sales rose 10% but overall category profits fell 11%. Conversely, when prices were marked up in high-low stores, unit volume declined 8% but the category's profits rose 1%.

"We thought consumers would be more likely to notice a price increase than a decrease, but there was absolutely no evidence of that," Mr. Hoch says.

While everyday low pricing may make sense as a market-entry strategy, Mr. Hoch questioned its value as a defensive one. "Where you have customers already coming to your store, why would you go to everyday low pricing to increase your market share? You're spending all your effort on your opposition and ignoring a fairly content installed base."

Moreover, he says, grocers who convert to an everyday low pricing strategy are likely to have to cut back on other services to cut costs and maintain profit margins.

The study is being conducted in 88 stores of Dominick's Finer Foods Inc., patronized by an estimated one million people each week. Eighteen companies are sponsoring the project, including Campbell Soup Co., Colgate-Palmolive Co., General Mills Inc., Gillette Co., H.J. Heinz Co.'s Starkist unit, PepsiCo Inc., Philip Morris Cos., Procter & Gamble, Quaker Oats Co. and Scott Paper Co.

As for the potential impact of the pricing research on consumer grocery bills, Mr. Hoch says, "The idea is to be more efficient in spending dollars, which should bring the cost of business down. . . . If executed appropriately, the long-term benefit should be lower food bills."

That's the theory, anyway.