Switch Marketing and the Retail Pricing of Brands and Private Label Products

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Introduction

The Private Label Phenomenon…

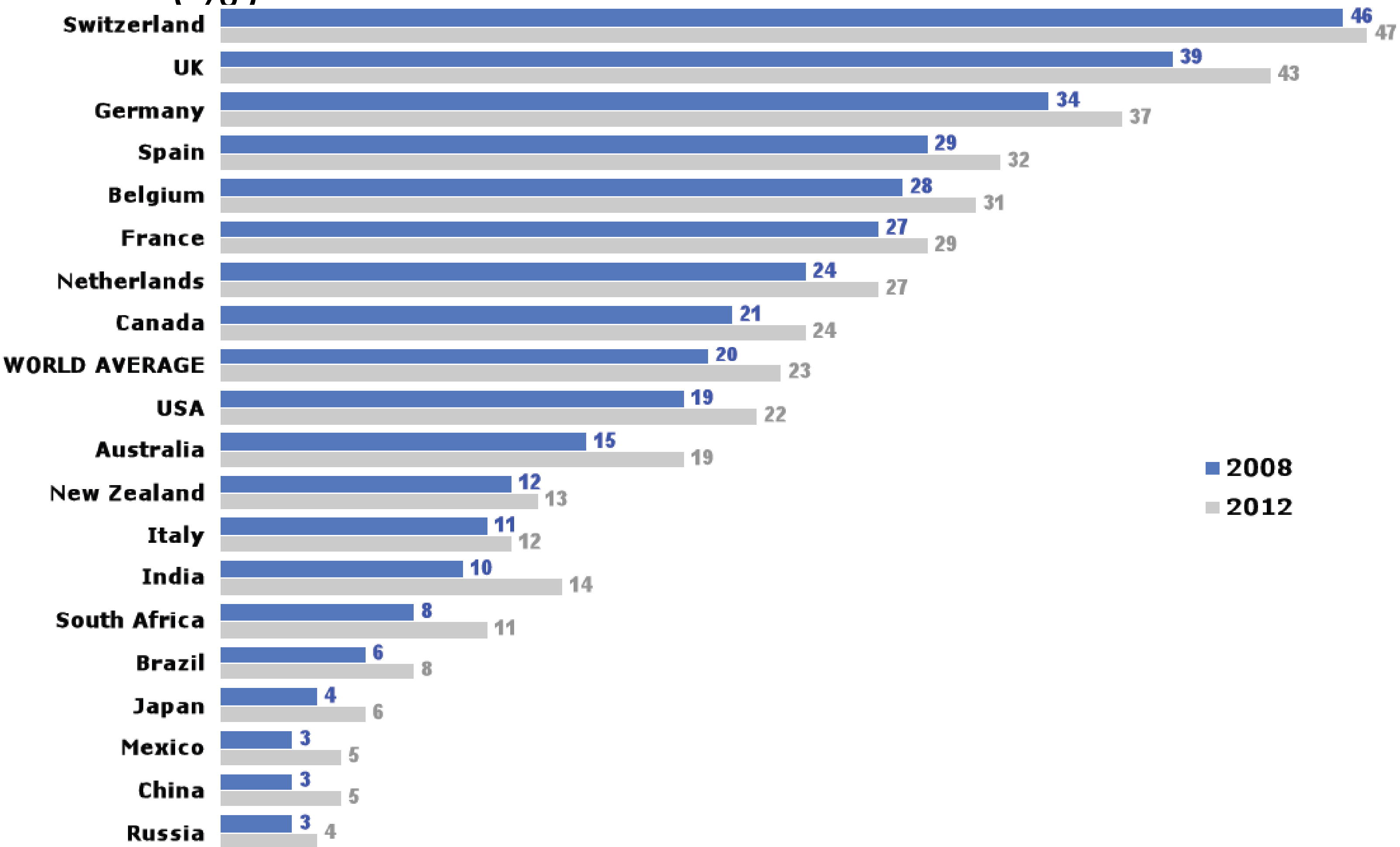
- Private label ("PL") market share has grown as grocery markets have become more concentrated
- Private label has come to rival and even dominate brands in many categories

But….

- Is this growth in private label necessarily benign?
- How has this growth in private label affected retail and producer competition?
- Do retailers favour private label at the expense of brands and distort consumers' choices and the prices they face?

Private Label Share Forecast to Keep Growing

Private Label Share of Market by Value, 2008-20012 (%)



Note: Based on selected mature and emerging markets; e – estimate; f - forecast.
Source: Planet Retail Ltd - www.planetretail.net; partly based on AC Nielsen

Steering Consumers to Buy Private Label

Concerns about retailers' use of "switch marketing":

- *The Practice:*
  - Using marketing to encourage consumers to switch from buying one product to a different one
- *The Context:*
  - Retailers encouraging consumers to switch from brands to private labels
  - Retailers exploiting "double agent" role as brand producers' *customer* and *competitor*
- *The Implications:*
  - Distorted competition?
  - Consumer detriment?

Why Favour Private Label?

Possible business advantages for the retailer:

- *Generate higher margins*
  - saving on brand marketing costs; free-riding on brand investments
- *Facilitate consumer segmentation*
  - multiple price-quality tiers in category price architectures
- *Promote own name & build consumer loyalty*
  - label bearing retailer's name; draw quality inferences from the leading brands; consumers' champion image
- *Enhance retailer differentiation & reduce price comparability*
  - differentiation as own brands are unique to the retailer
- *Weaken brand producer's bargaining position*
  - extract more favourable terms through increased discounts and incentive payments from brand producers

PL Favouritism and the Marketing Mix

- **Product** – *influencing consumers' product choices*
  - controlling range; advanced brand design knowledge; PL copycat formulation/packaging; PL multiple quality tiers; brand delisting
- **Price** – *influencing consumers' value perceptions*
  - label bearing retailer's name; draw quality inferences from the leading brands; framing effects
- **Place** – *influencing consumers' accessibility*
  - gatekeeper power controlling distribution; in-store product placement; shelf allocation; shelf positioning; stock replenishment
- **Promotion** – *influencing consumers' knowledge*
  - controlling in-store advertising; media advertising campaigns ("switch and save"); targeted advertising ("cheaper alternatives!"); personalised marketing (loyalty card data)

Examples of Blatant PL Favouritism #1

- ***Brand Lookalikes***

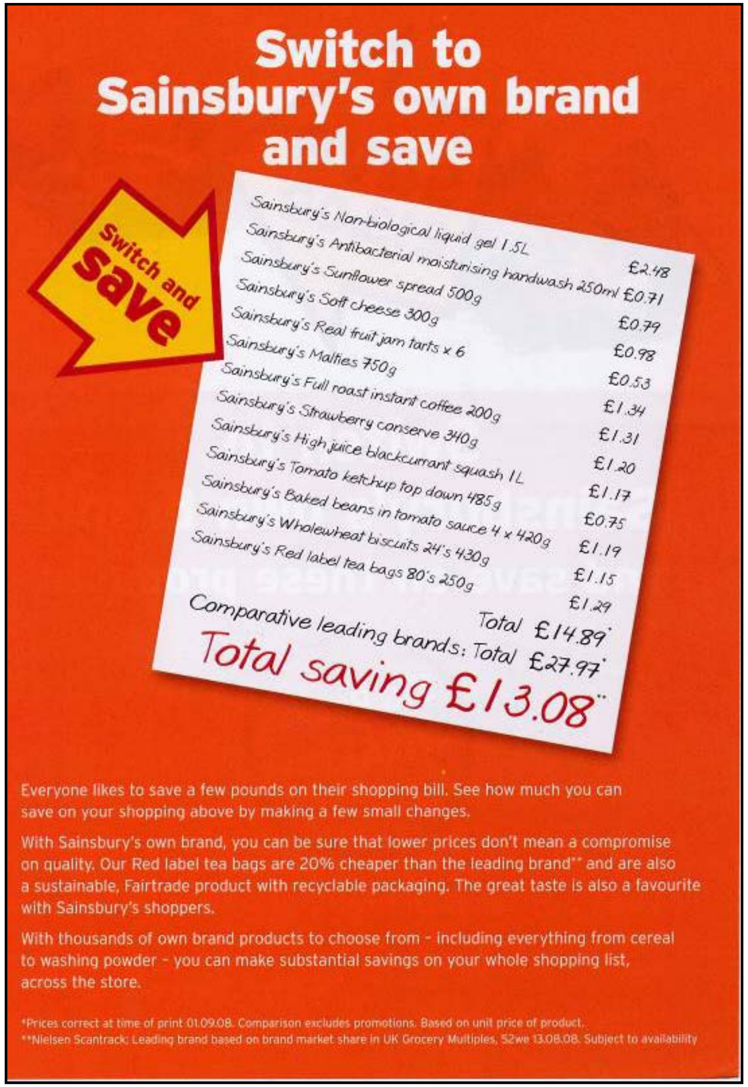
Examples of Blatant PL Favouritism #2

- ***Tactics focused on consumer trial***
  - Blind taste tests – Wegmans in US ("Great Taste Wins" campaign), Sainsbury's in UK ("Taste Test Challenge")
  - Coupons – Buying a brand triggers coupon for PL – Spartan in US
  - Giveaways – "Buy the brand, get the PL equivalent free" – Publix in US ("Brands Challenge" BOGO campaign)
  - Brand delisting trials – temporarily delist brand and see if consumers complain or shop elsewhere – Asda in UK
- ***Shelf-space allocation and shelf positioning***
  - Giving PL a greater number of facings and mid-shelf, eye-level placement as well as special product displays – see Fernandez Nogales and Gomez Suarez (2005) for a Spanish case study

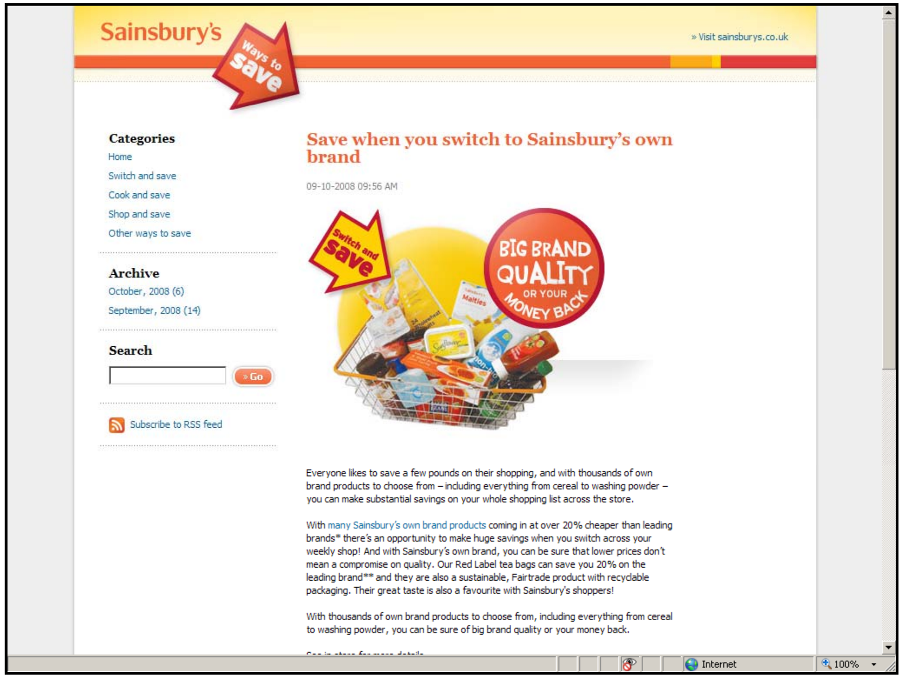
Examples of Blatant PL Favouritism #3

- ***"Compare and Save" Promotions***
  - Established in-store signage tactic used by grocery, general merchandising, drug store and stationery retailers in the US (e.g. Wal-Mart, CVS, and Staples)
  - Similar tactic seen in other countries including Australia (Woolworths) and through advertising leaflets in Germany (Rewe and Müller)
  - Large-scale "switch marketing" campaigns in the UK:
    - Sainsbury's "Switch and Save" promoting "Switch to Sainsbury's own brand and save at least 20%"
    - Tesco "See Cheaper Alternatives!" web tool on tesco.com and backed up by TV advertising campaign

Sainsbury's "Switch and Save" #1



Sainsbury's "Switch and Save" #2


Sainsbury's
Ways to save
» Visit sainsburys.co.uk

Categories
Home
Switch and save
Cook and save
Shop and save
Other ways to save

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October, 2008 (6)
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Save when you switch to Sainsbury's own brand

09-10-2008 09:56 AM

Switch and save
BIG BRAND QUALITY OR YOUR MONEY BACK

Everyone likes to save a few pounds on their shopping, and with thousands of own brand products to choose from – including everything from cereal to washing powder – you can make substantial savings on your whole shopping list across the store.

With many Sainsbury's own brand products coming in at over 20% cheaper than leading brands* there's an opportunity to make huge savings when you switch across your weekly shop! And with Sainsbury's own brand, you can be sure that lower prices don't mean a compromise on quality. Our Red Label tea bags can save you 20% on the leading brand** and they are also a sustainable, Fairtrade product with recyclable packaging. Their great taste is also a favourite with Sainsbury's shoppers!

With thousands of own brand products to choose from, including everything from cereal to washing powder, you can be sure of big brand quality or your money back.

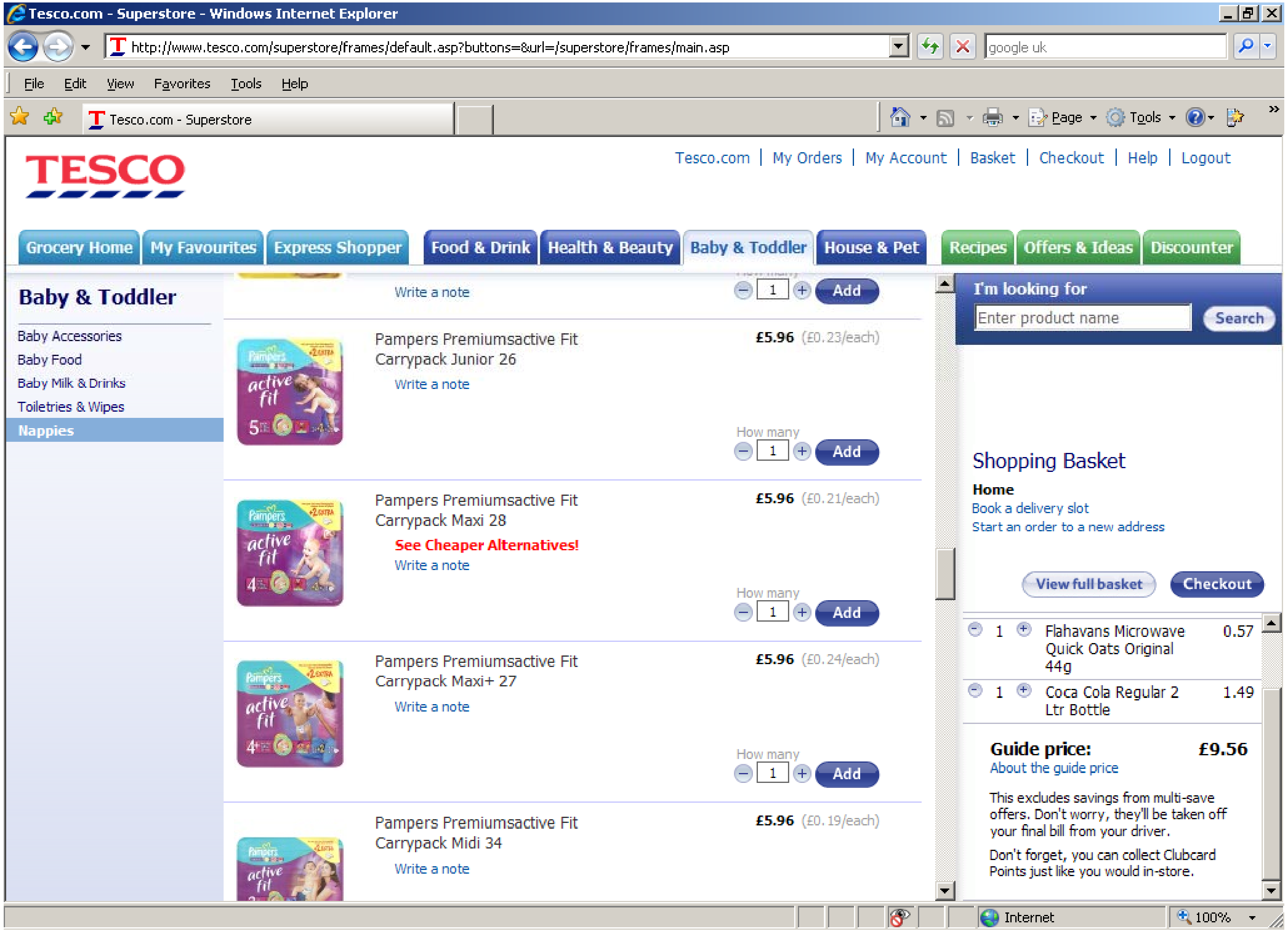
Internet
100%

Tesco "See Cheaper Alternatives!" #1

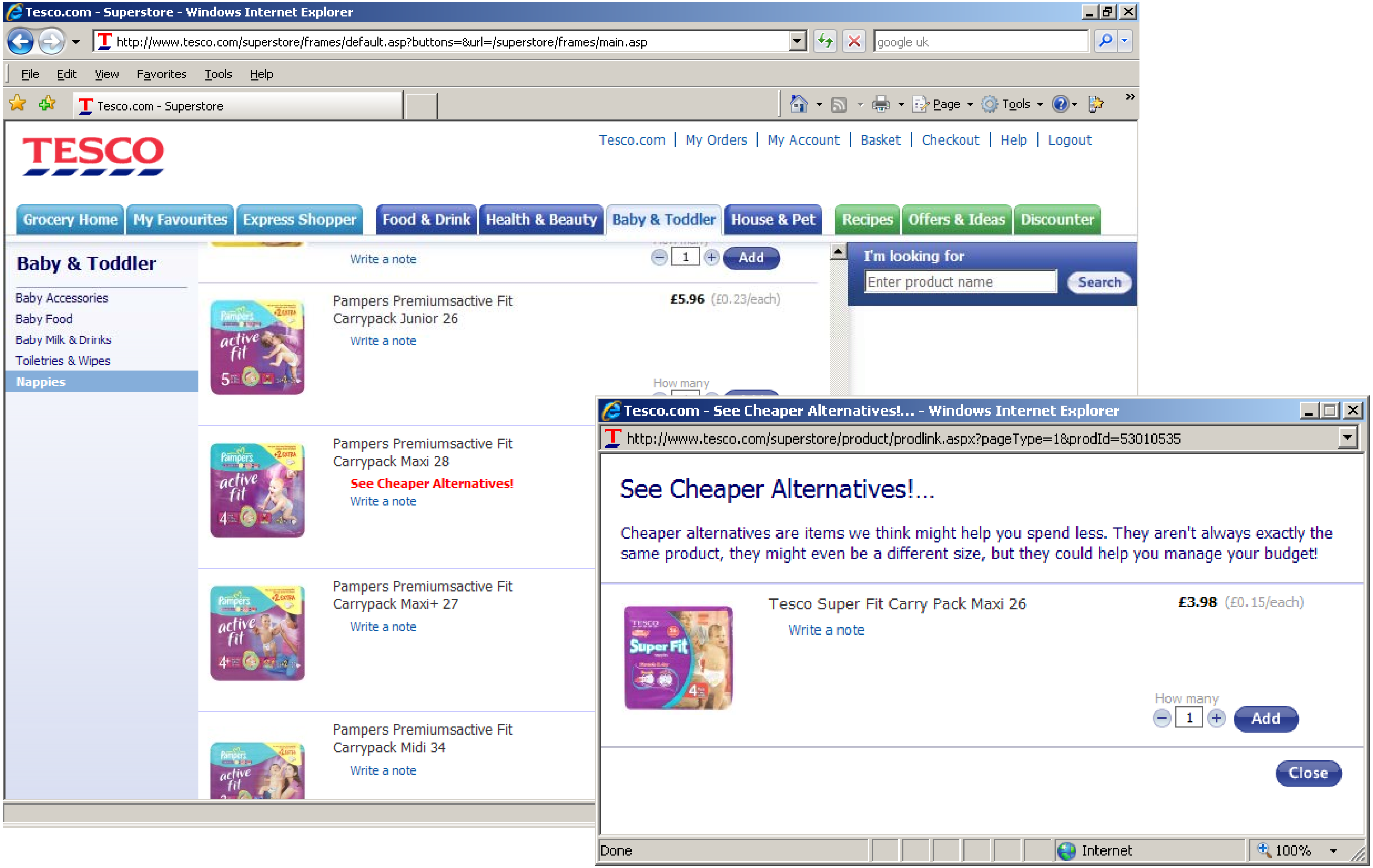
TESCO

Every little helps

Tesco “See Cheaper Alternatives!” #2



Tesco “See Cheaper Alternatives!” #2



More Subtle PL Favouritism

Strategic pricing for driving PL growth or extracting more category revenue:

- Do retailers using pricing either to steer consumers towards PL or to better price target them through their different price sensitivity on brands and PL?
- What pricing tactics might be used to favour PL and/or better segment consumers and how common are these?
- To what extent do pricing tactics favouring PL depend on the retailer's identity, producer's identity, brand status, private-label status, and/or product category?

Pricing Tactics to Favour Private Label

- *"Rip-off Brand" Tactic*
  - Brand price raised to choke demand in favour of switch to PL
- *"Value Champion PL" Tactic*
  - Private label price reduced to enhance perceived value for money and make brands look poor value by comparison
- *"Equal-Quality-But-Better Value PL" Tactic*
  - Private label price tracks brand price closely but at a slight discount (e.g. umbrella pricing)
- *"Dubious Brand Value" Tactic*
  - Brand prices raised and lowered in yo-yo fashion or in Edgeworth Cycles (small steps down then big jump up) to confuse consumers on real value and encourage trial of more consistently priced PL

…but are these tactics used in practice?

Empirical study of brand and equivalent PL prices in UK grocery retailing:

- Matched pairs of branded goods and private label equivalents across different grocery product categories
- Weekly updated prices from top 4 UK grocery retailers over a five-year period on these matched pairs
- Study provides insights on retail price competition, whether different retailers apply the same or different pricing tactics, as well as the treatment of brand and private label prices

Background on UK Grocery Market

- UK grocery sector worth £140bn in 2008 (IGD)
- The "Big 4" (Tesco, Asda, Sainsbury, and Morrison) dominate the national market (with 75% of supermarket sales and 65% of all grocery sales)
- Sector subject to several investigations over the past decade (e.g. Competition Commission 2000, 2003, 2005, 2008)
- Continued concerns about the power of the major chains as both sellers and buyers and the impact on consumers
- Concern that with continuing consolidation retailers will increasingly be able to dictate product choices and prices to consumers

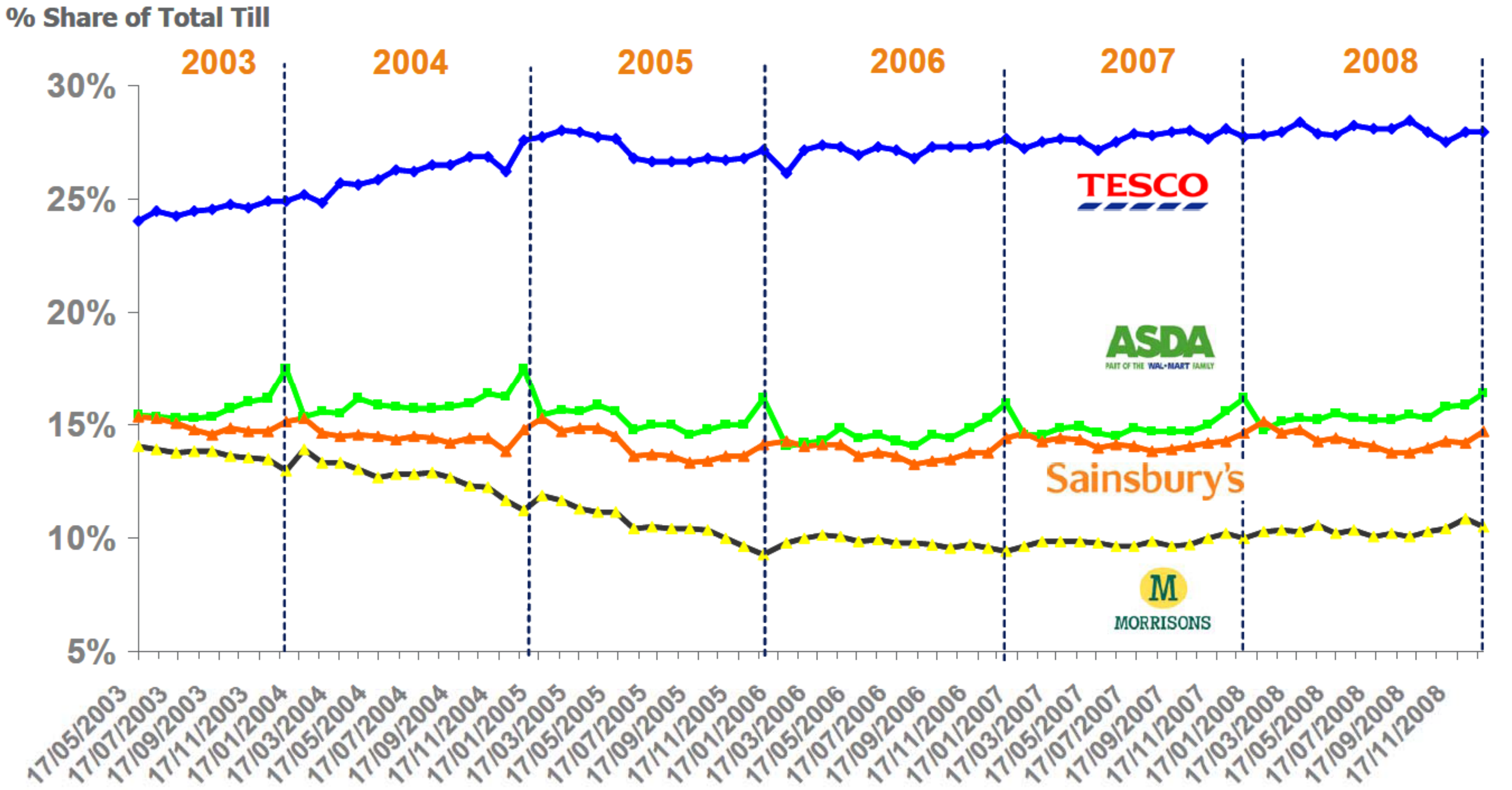
Comparison of the "Big 4" UK Retailers

Table 1: Sales Performance of Top 4 UK Grocery Retailers, 2008

Measure	Tesco	Asda	Sainsbury's	Morrisons
Share of trade (%)	28.1	15.5	14.3	10.4
Penetration – all shoppers (%)	84.9	67.9	63.7	60.2
Average visits per shopper p.a.	39.9	25.7	27.5	24.6
Average spend per shopper (£)	1265.74	871.83	862.18	606.05
Average spend per visit (£m)	31.75	33.95	31.34	26.85
Penetration – main shoppers (%)	34	18	16	13
Retailer loyalty – main shoppers (%)	65	64	66	60
% Spend on promotional offer	28	28	30	30
Own label share (%)	47	47	48	47

Source: Adapted from Nielsen (2009)

Market Share Trends of the Big 4



Total Till Spend = All General Merchandising, New Non Food and Total Traditional Grocery.

Source: Nielsen Homescan Total Till:
4 week ending periods to 27th December 2008

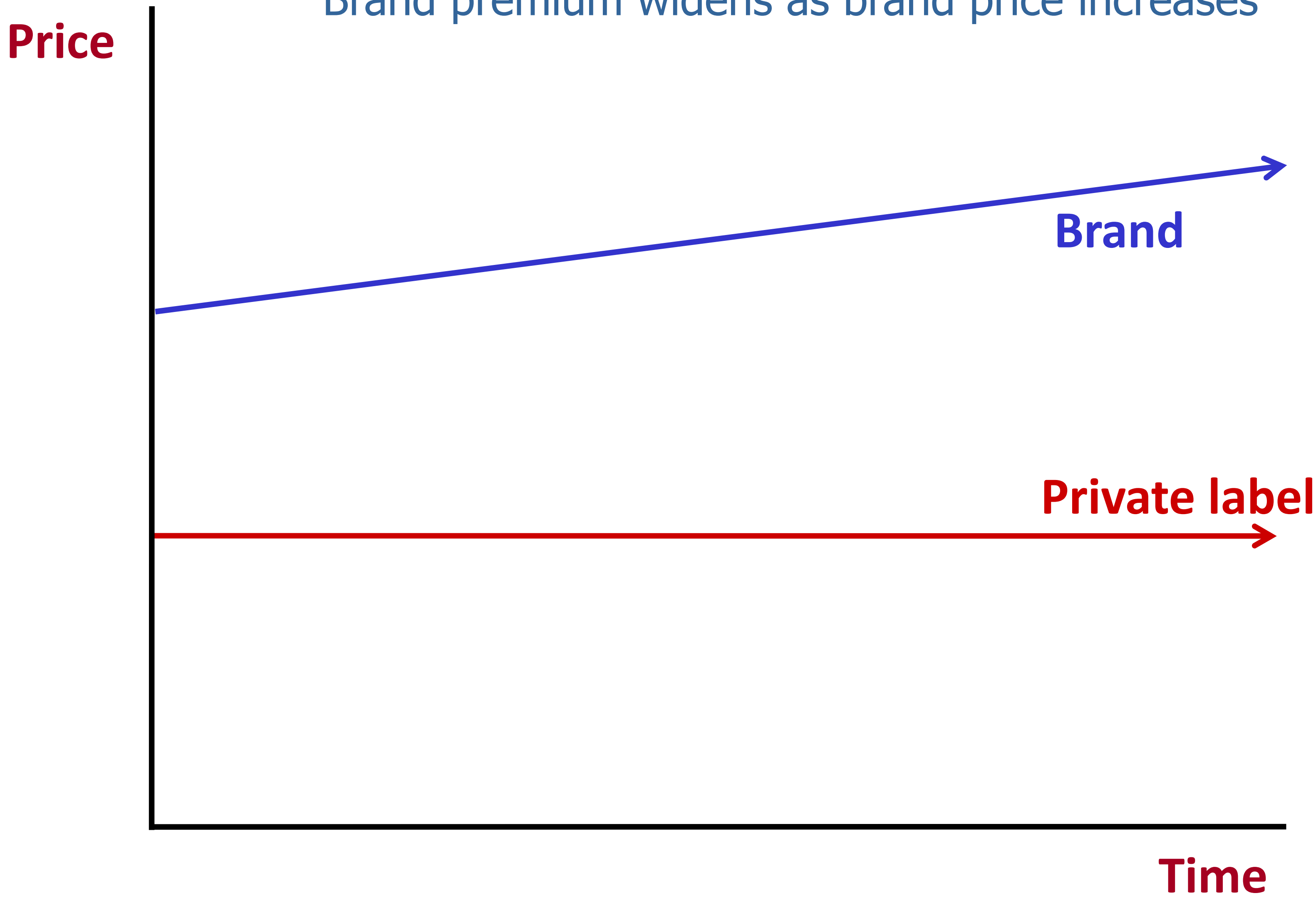
Matched-Pairs Analysis – Preliminary Results

Analysis of pricing patterns across matched pairs of branded goods and private label equivalents

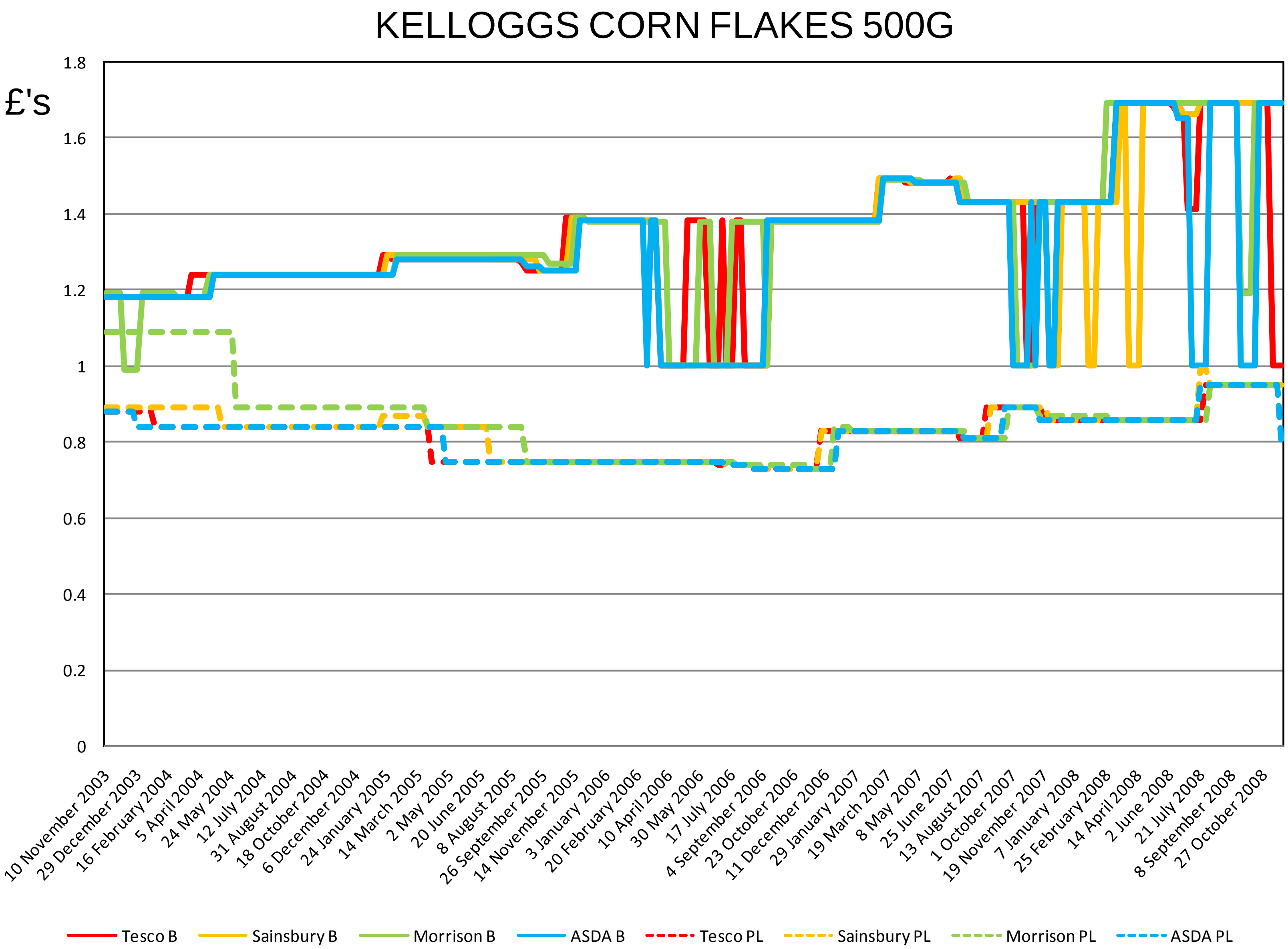
- *Time Period* – 5 years (10/11/03 to 24/11/08)
- *Data* – Weekly prices on single items
- *Sample* – 60 matched pairs in Big 4 retailers (127K obs)
- *Products* – packaged goods for range of categories
- *Price range* – min £0.12, max £7.69, mean £1.12

"Rip-off Brand" Tactic

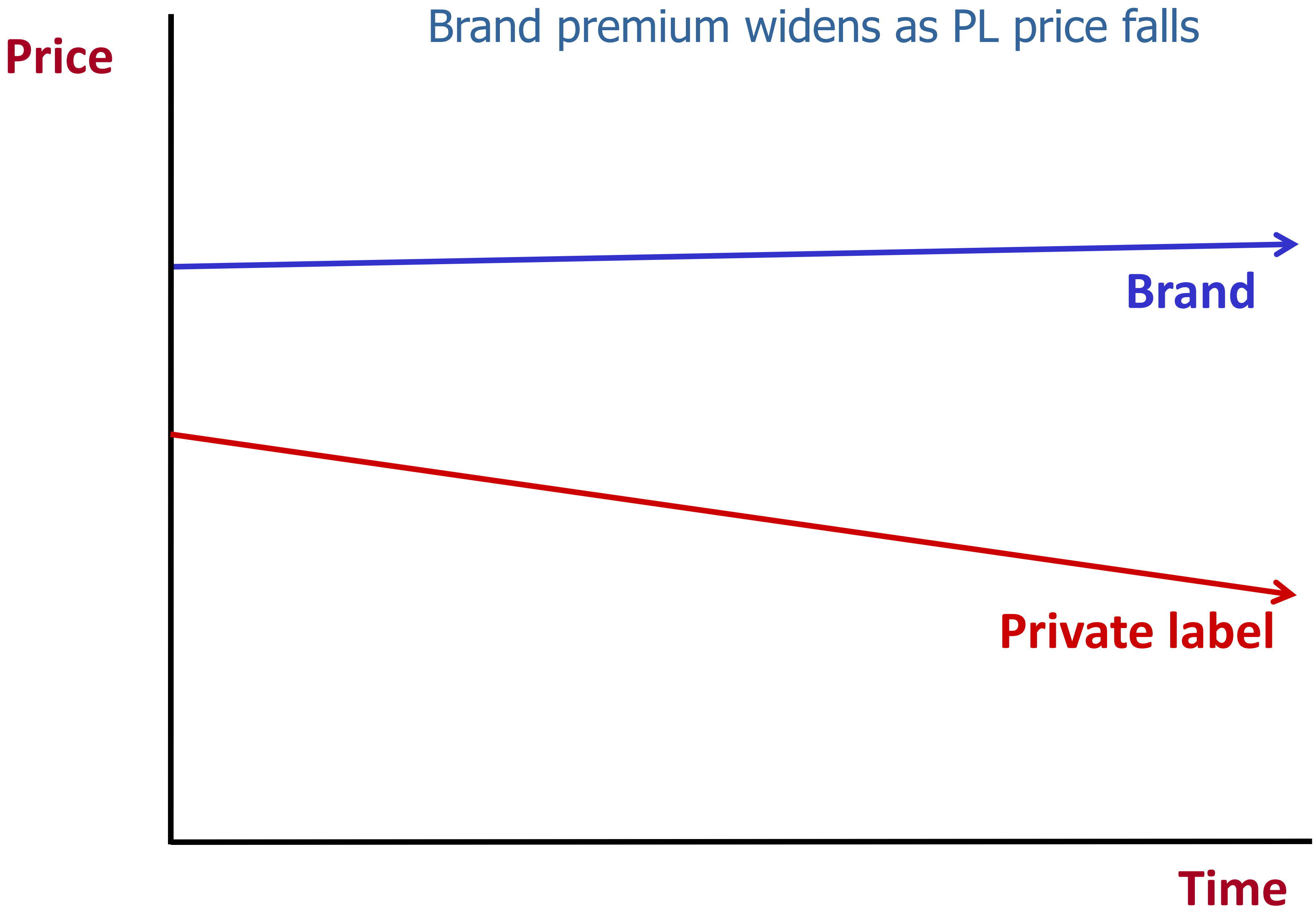
Brand premium widens as brand price increases



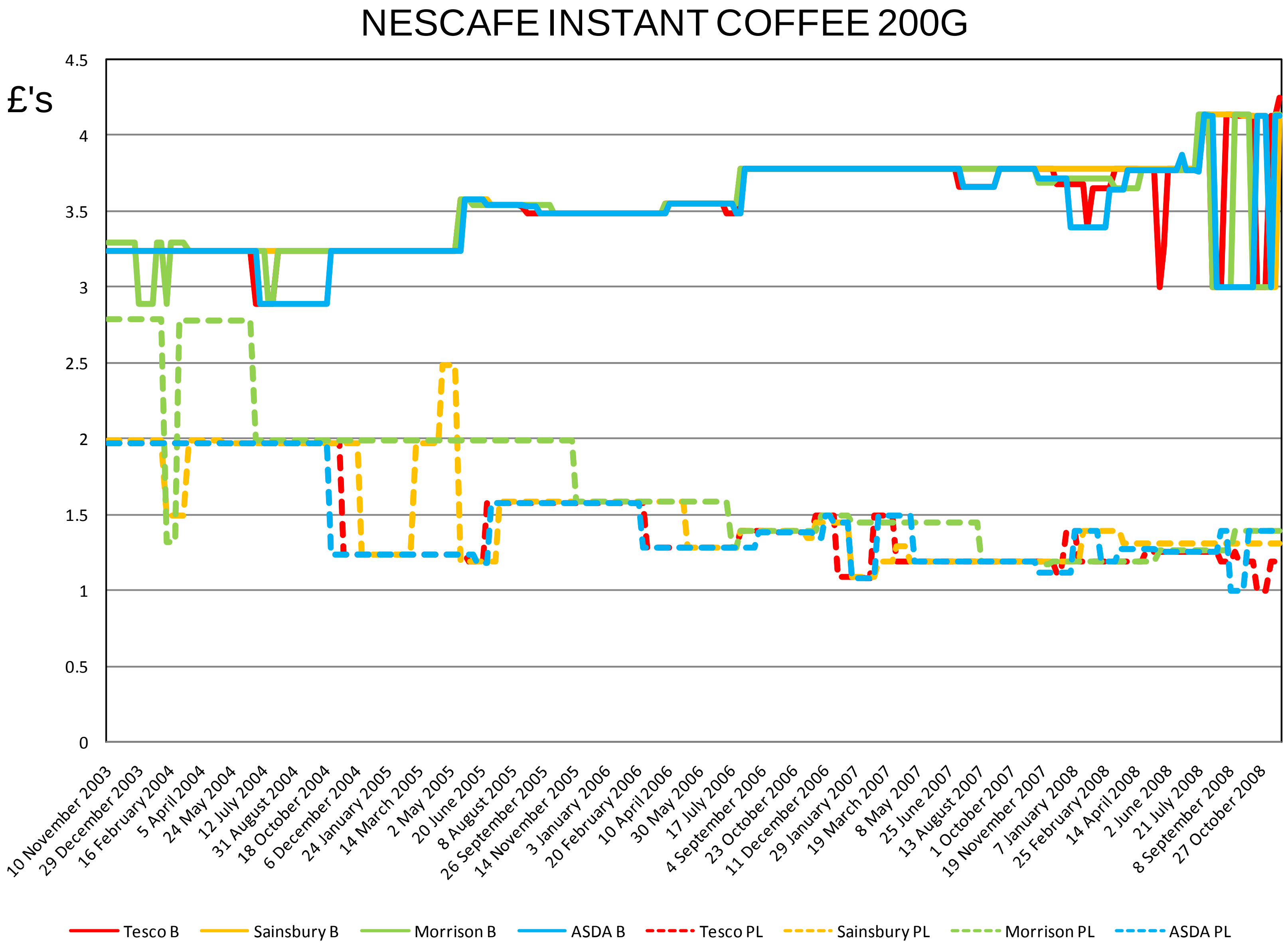
"Rip-off Brand" Tactic?



"Value Champion PL" Tactic

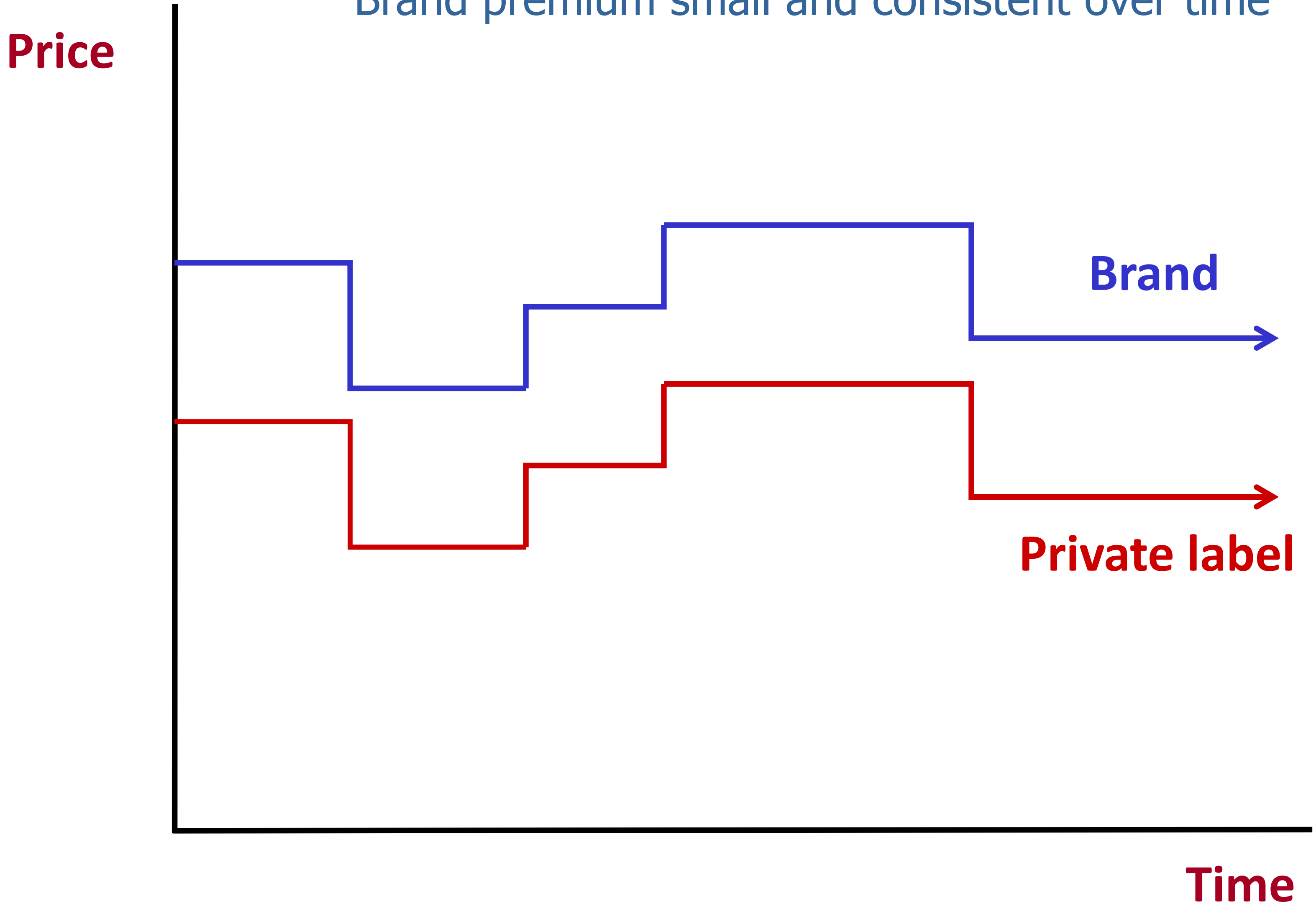


"Value Champion PL" Tactic?

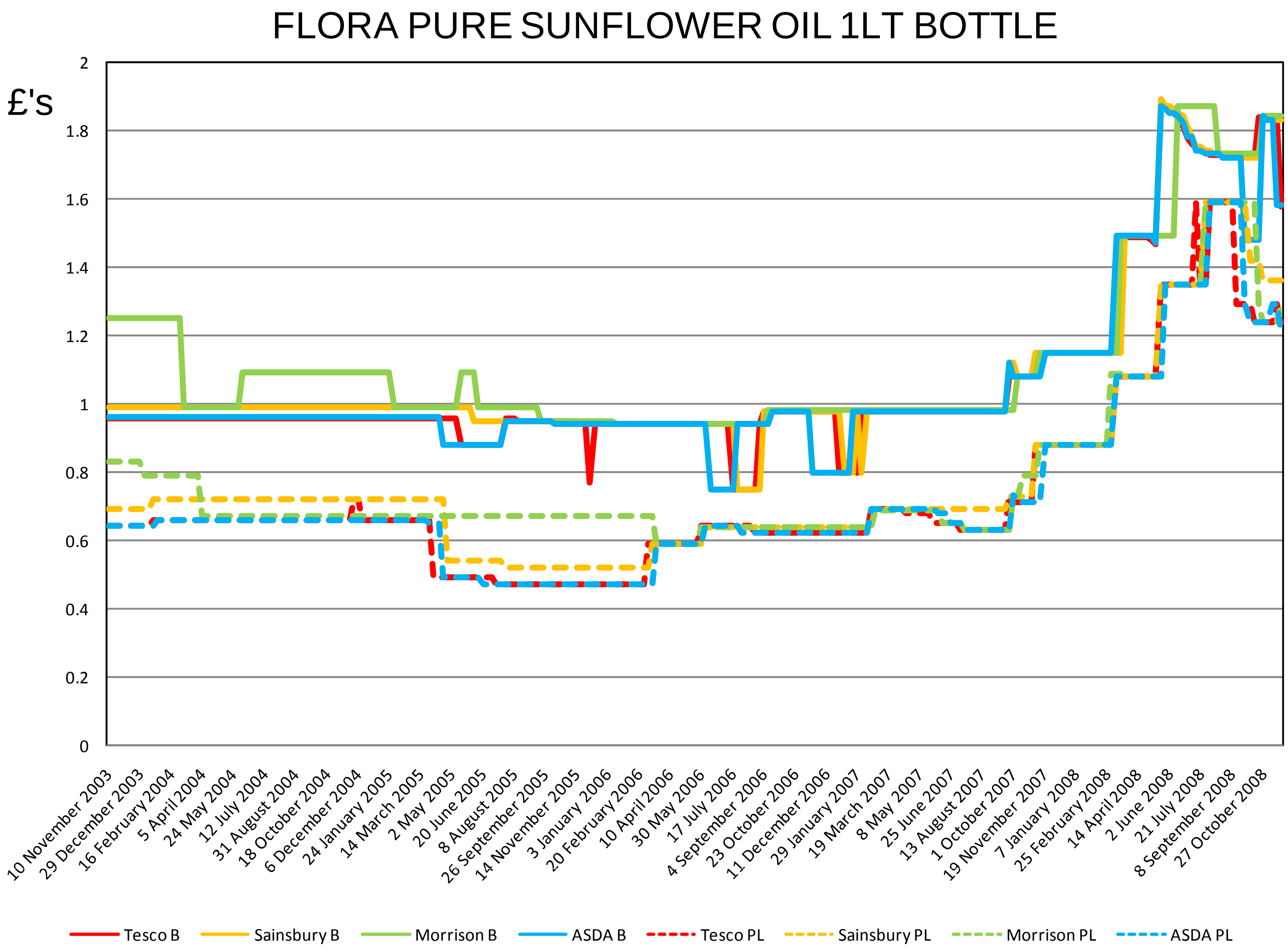


"Same-Quality-Better-Value PL" Tactic

Brand premium small and consistent over time

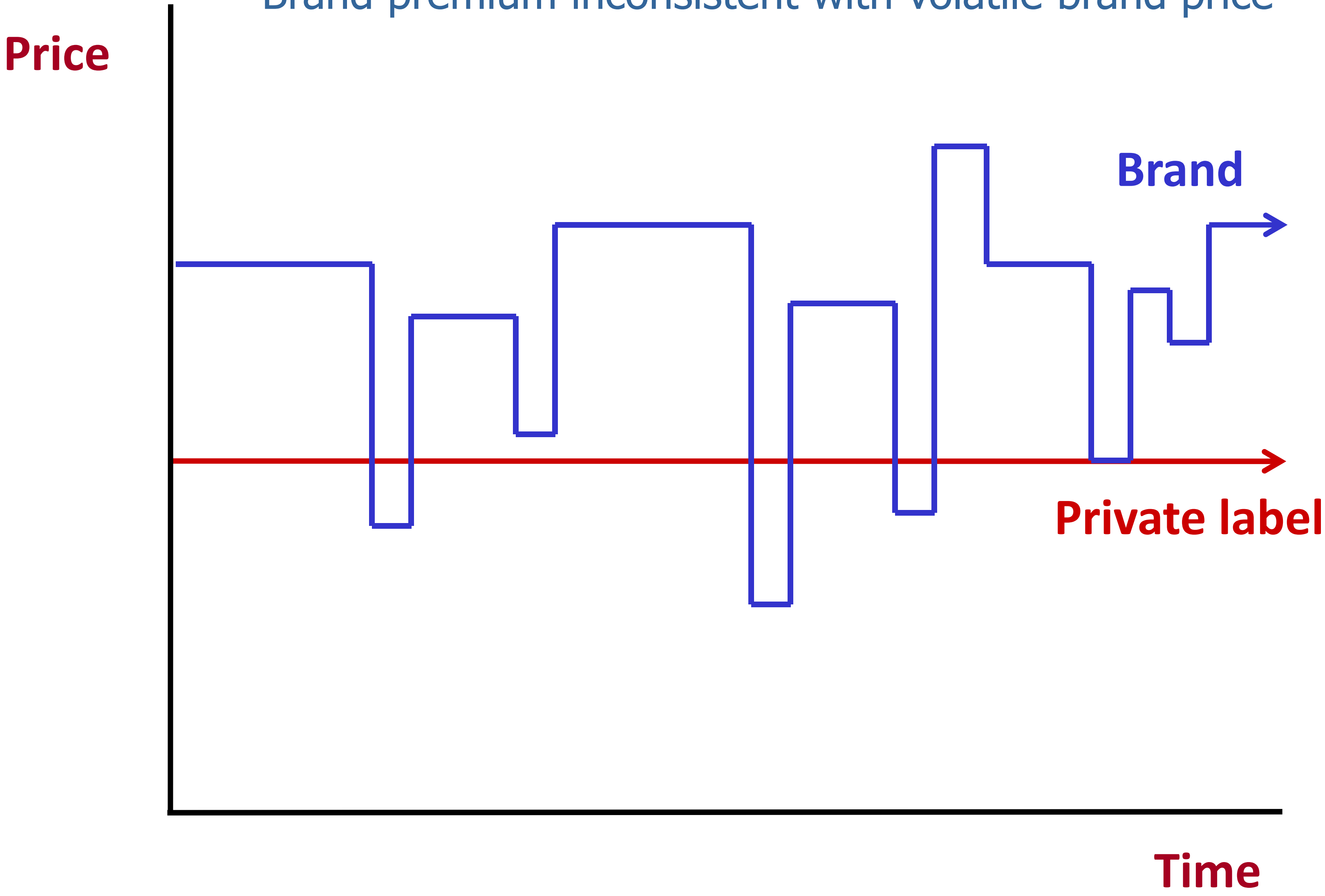


"Same-Quality-Better-Value PL" Tactic?

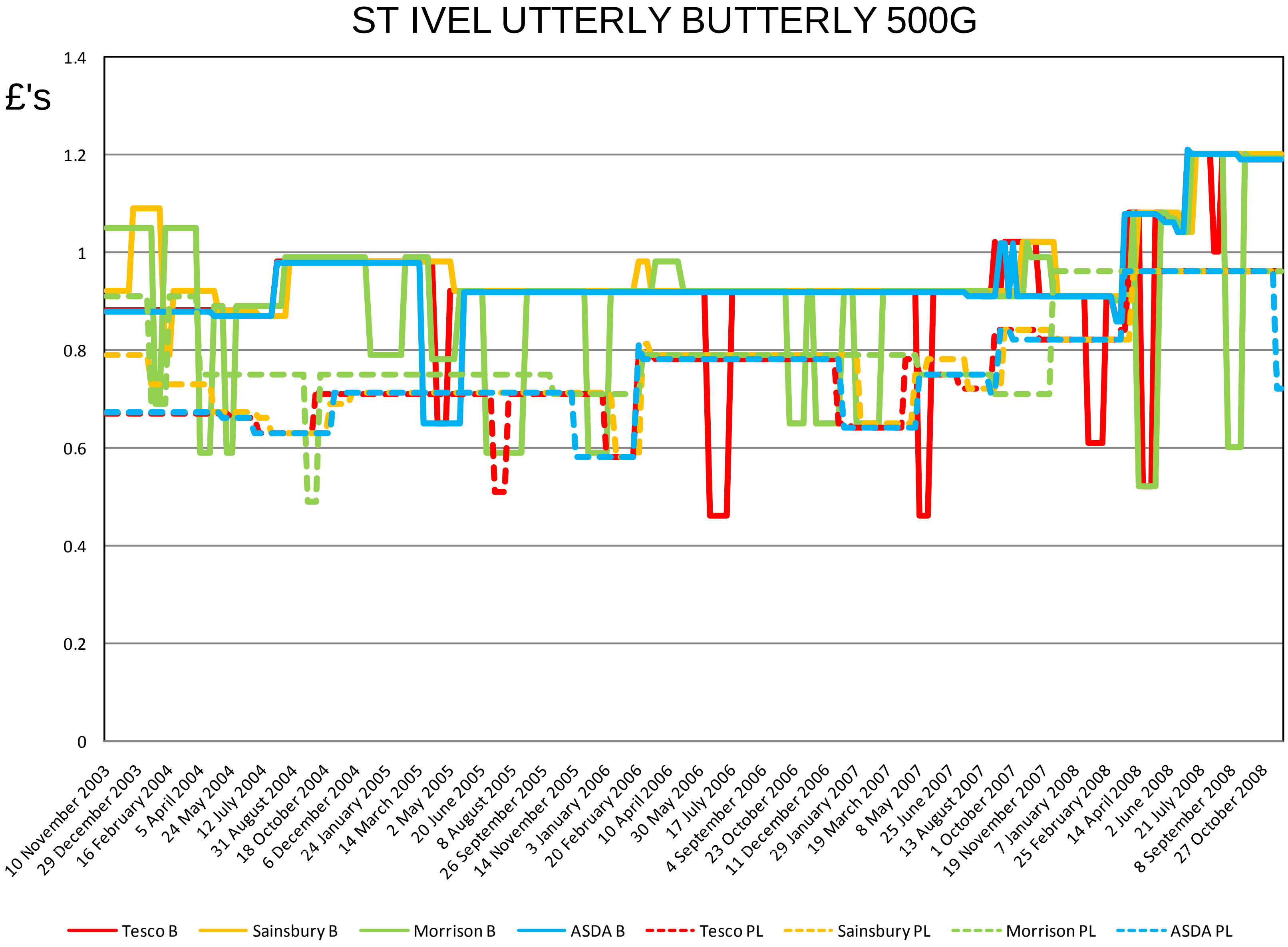


"Dubious Brand Value" Tactic

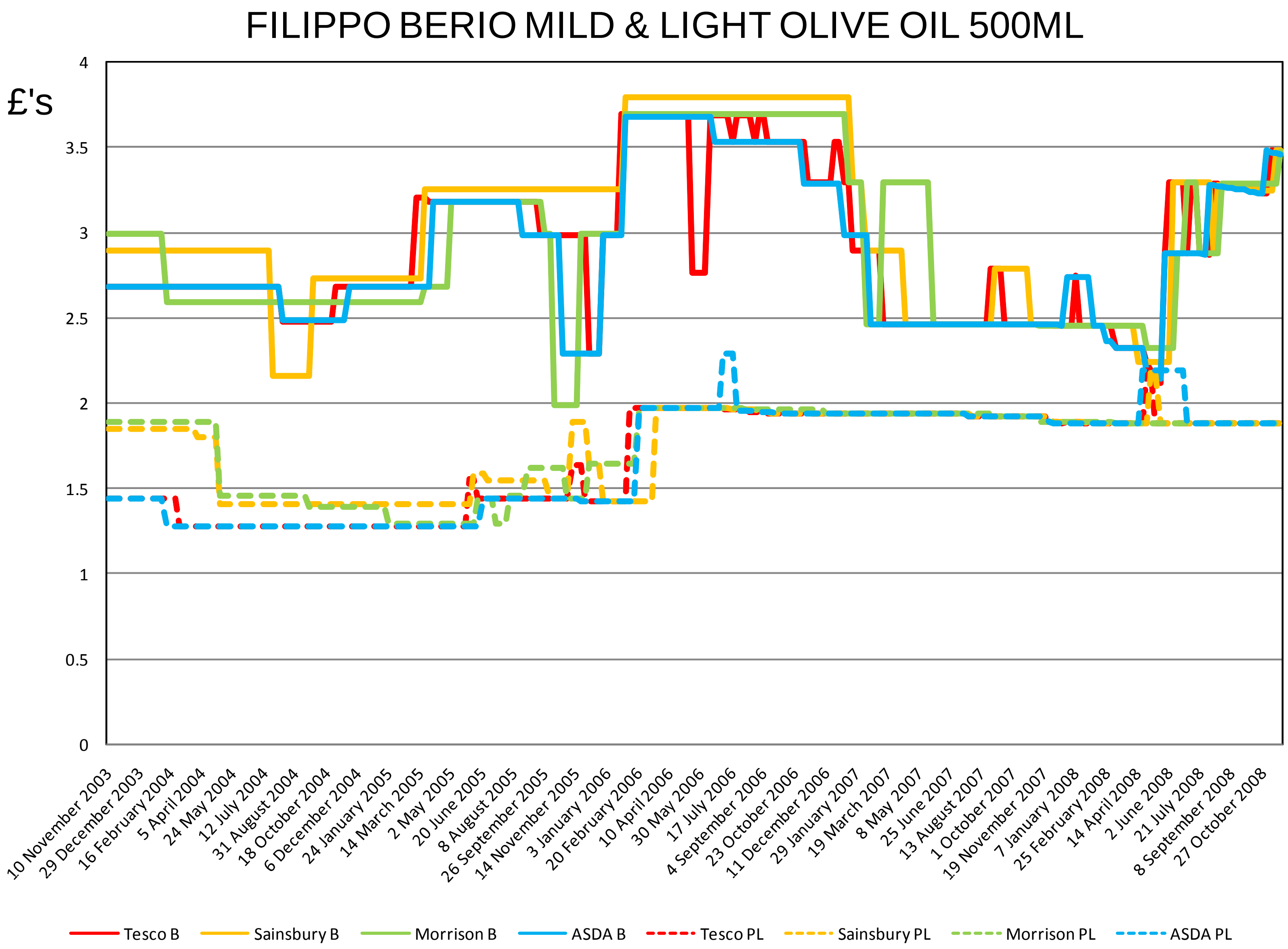
Brand premium inconsistent with volatile brand price



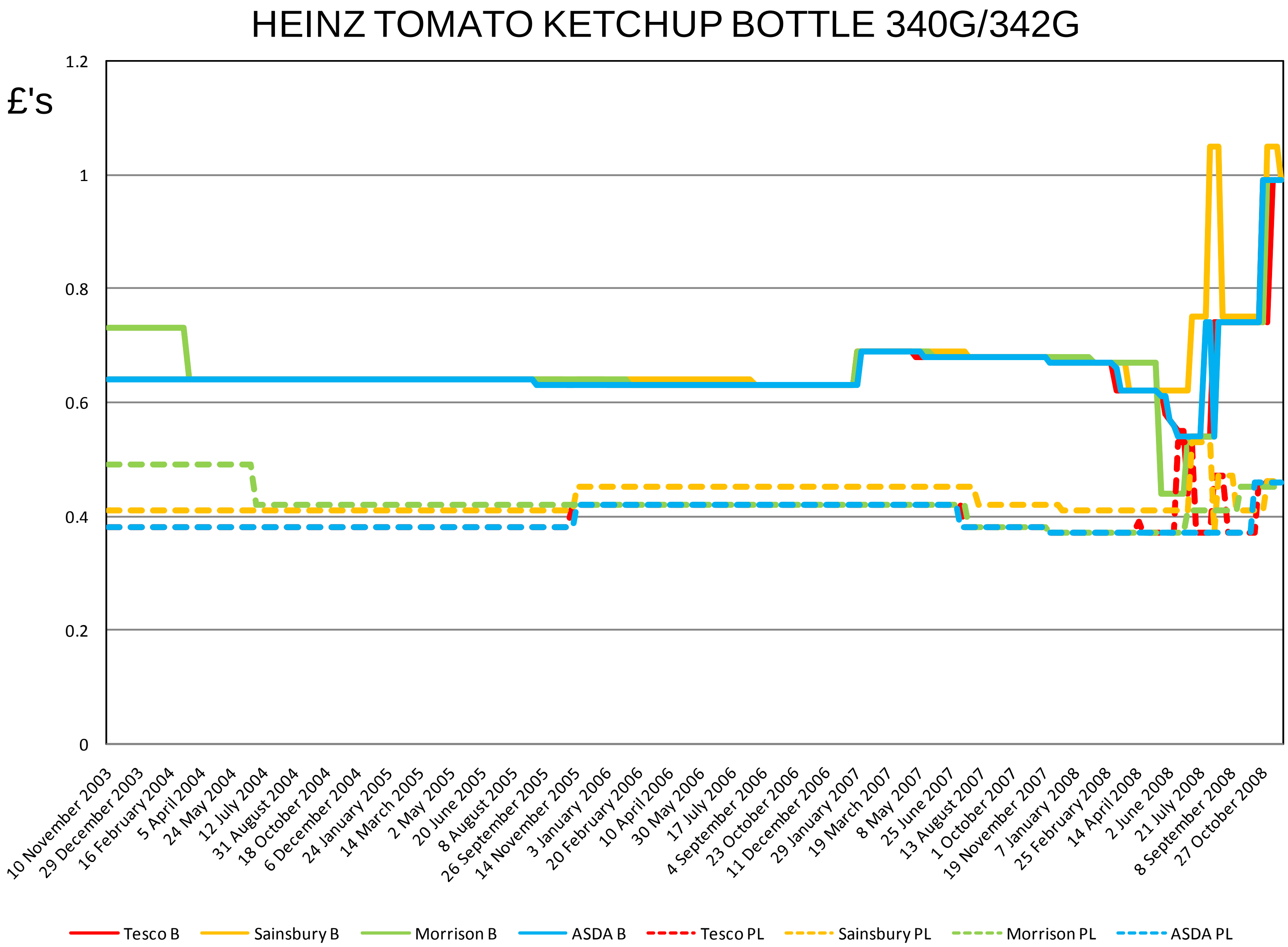
"Dubious Brand Value" Tactic?



Example of Unstable Price Relationship



Example of Suddenly Changing Price Relationship

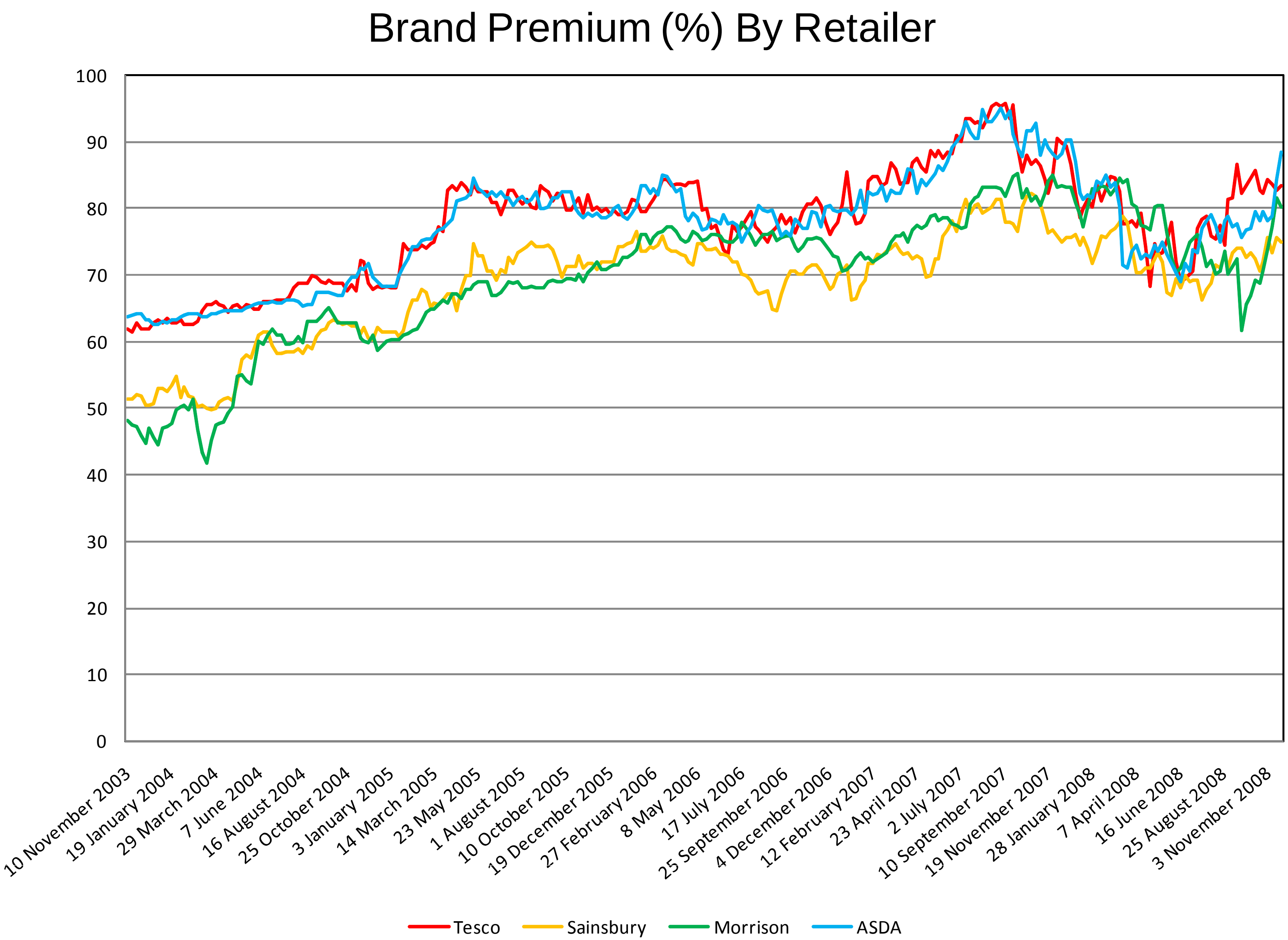


General Empirical Findings

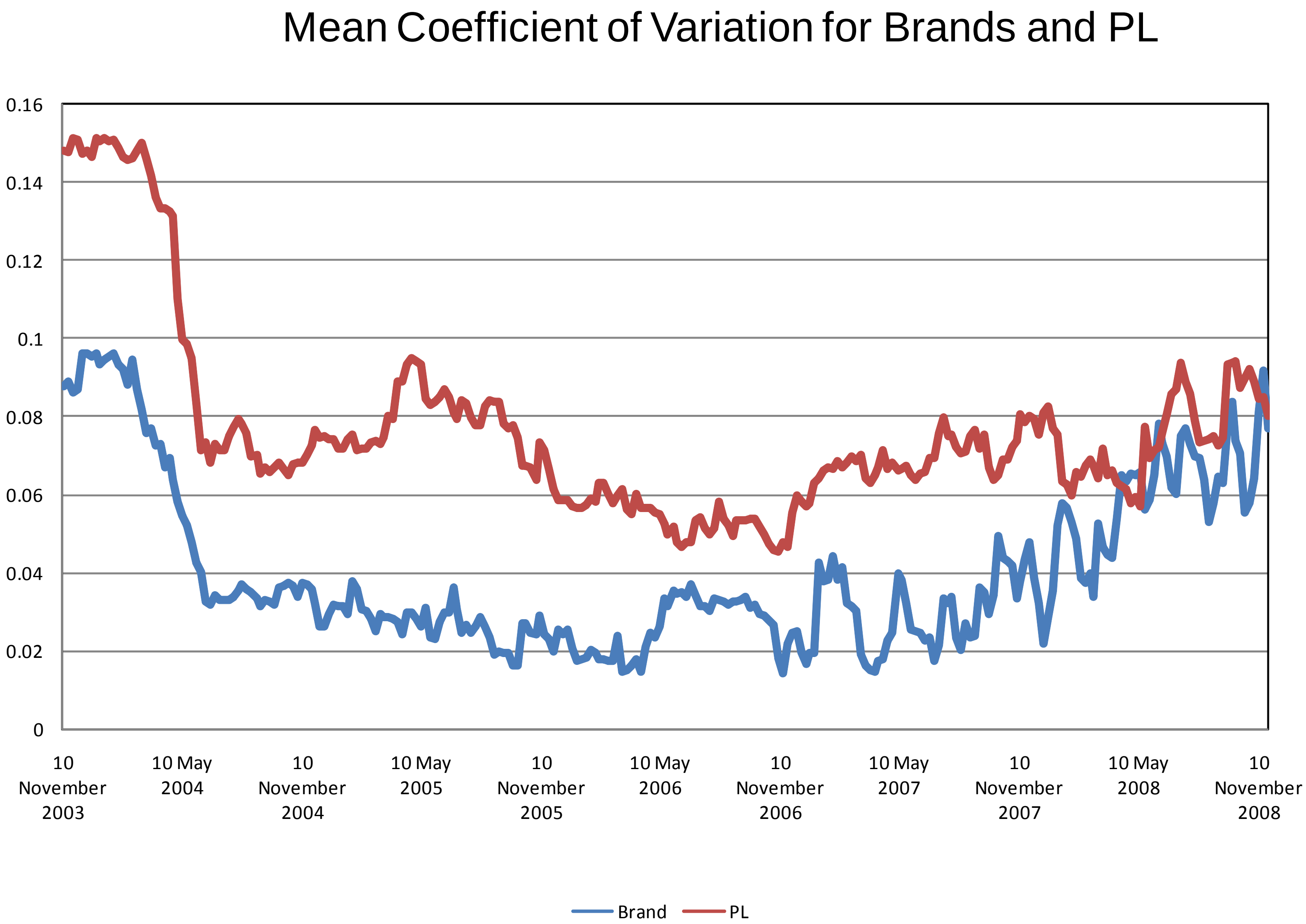
Matched pairs analysis suggests the following:

- *Brand premium* – Increased over 5 yrs by 45% on average
- *Price dispersion across retailers* – greater on PL, until 2008
- *Price matching across retailers* – greater on brands, until 2008
- *Price volatility* – price churn much greater for brands and much greater for Tesco and Asda than Sainsbury and Morrisons
- *Price changes*
  - almost twice as many price cuts as price rises over 5 yrs
  - six times more price changes ≥ 50p on brands than PL
  - 33% of brand price cuts by 1p; 18% of PL price cuts by 1p
  - 32% of Tesco price cuts by 1p; 29% of Asda price cuts by 1p

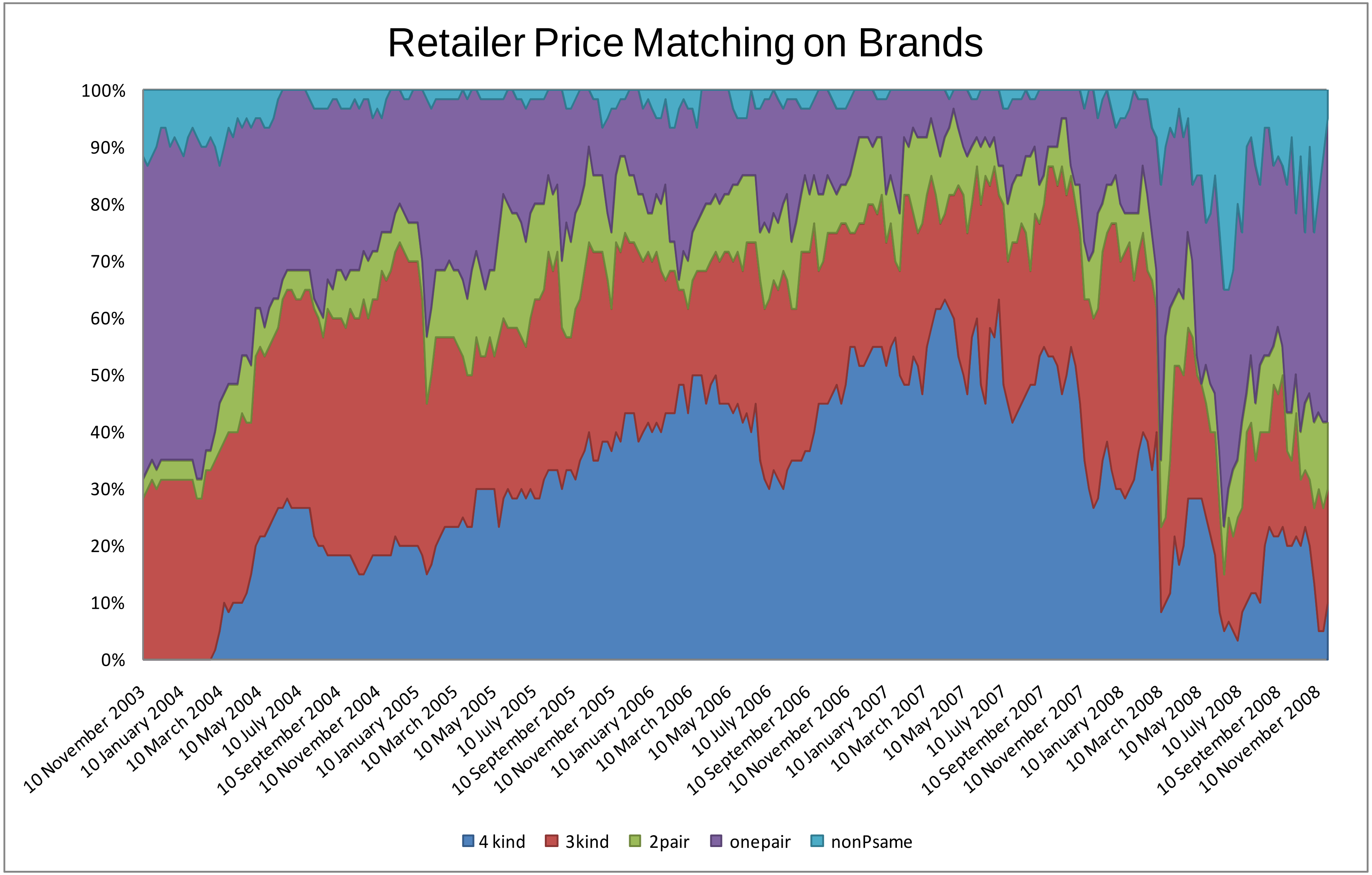
Rising Brand-PL Price Gap



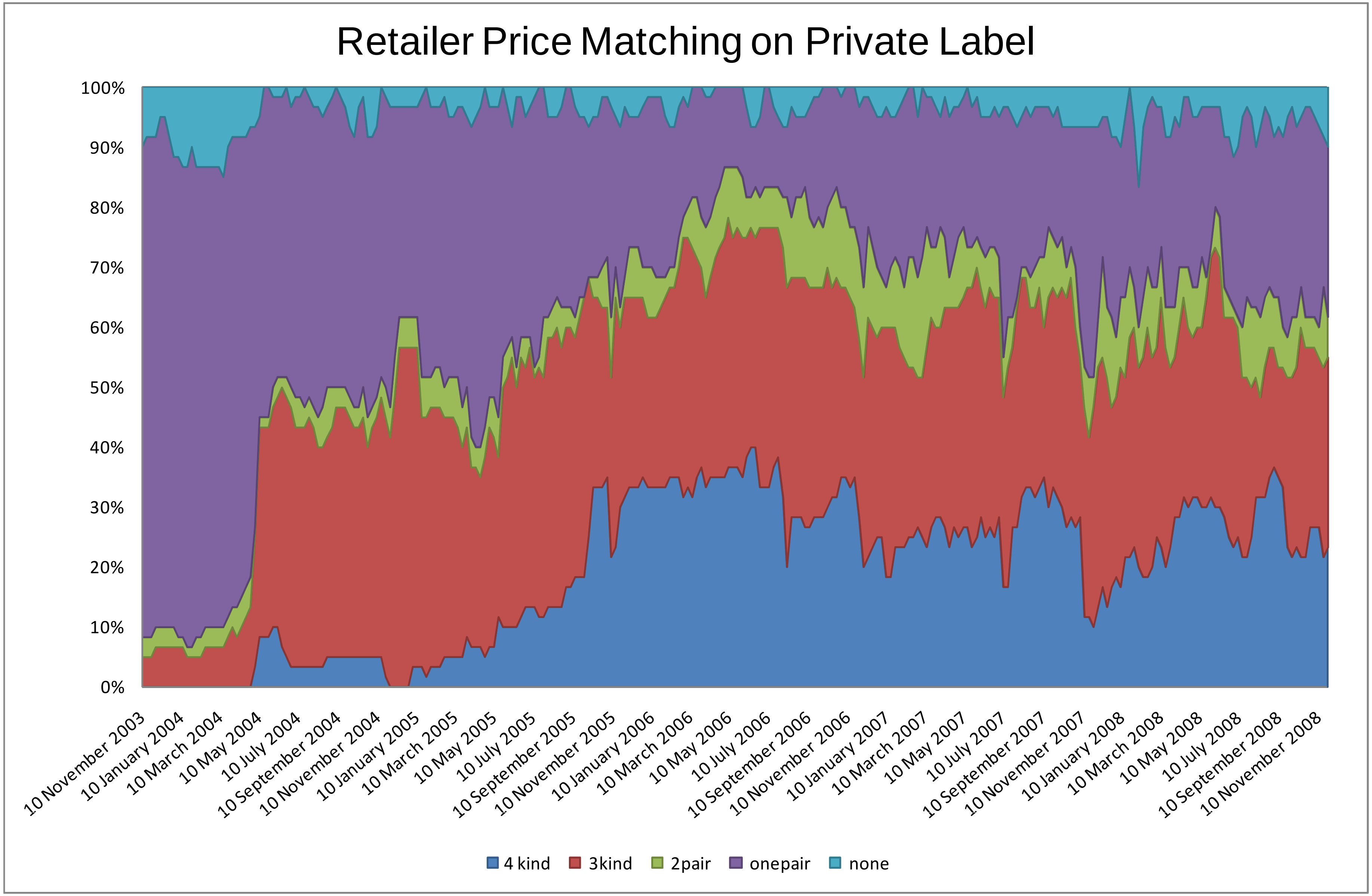
Price dispersion greater on PL, until recently



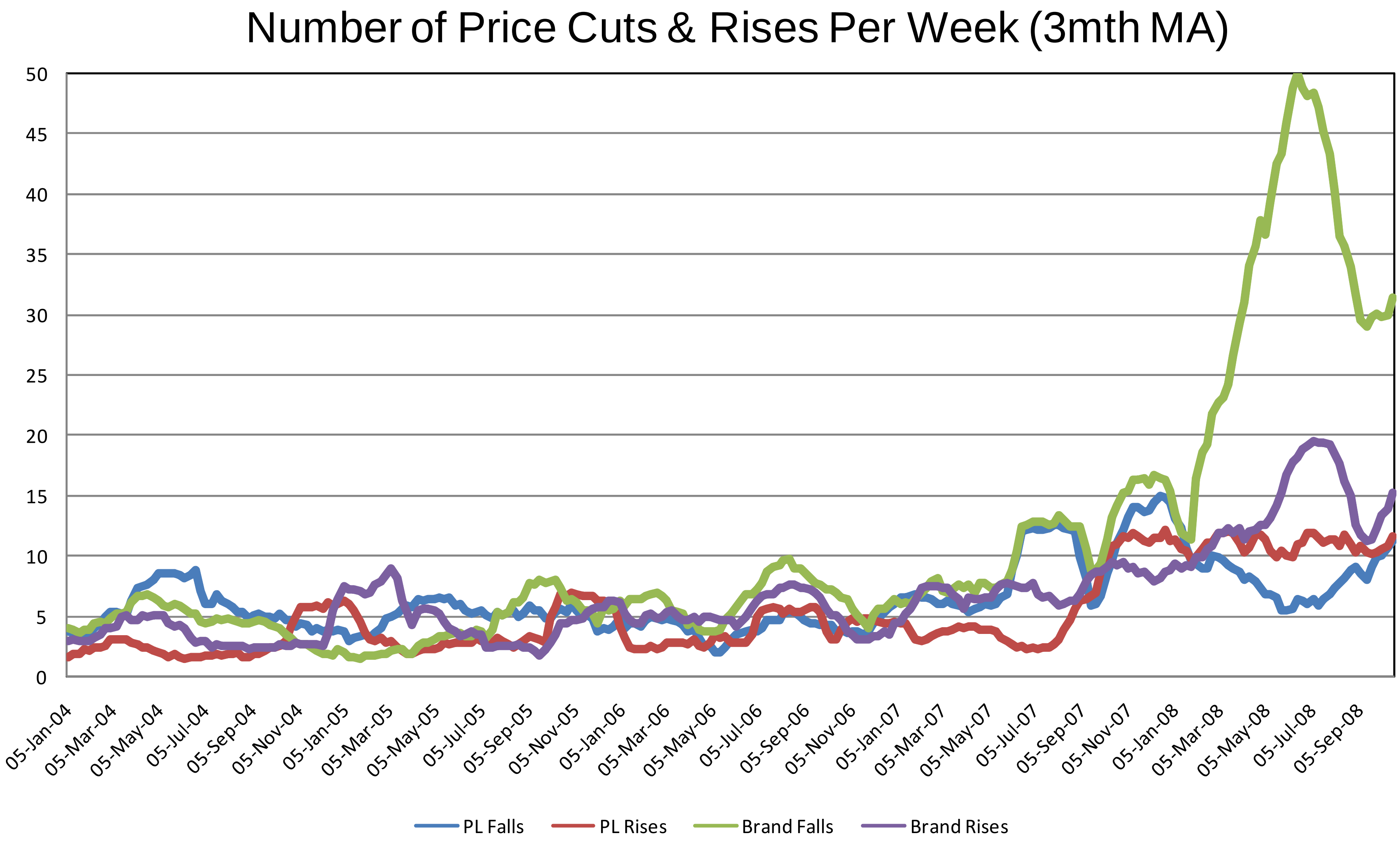
Retailer price matching – rises then falls on brands



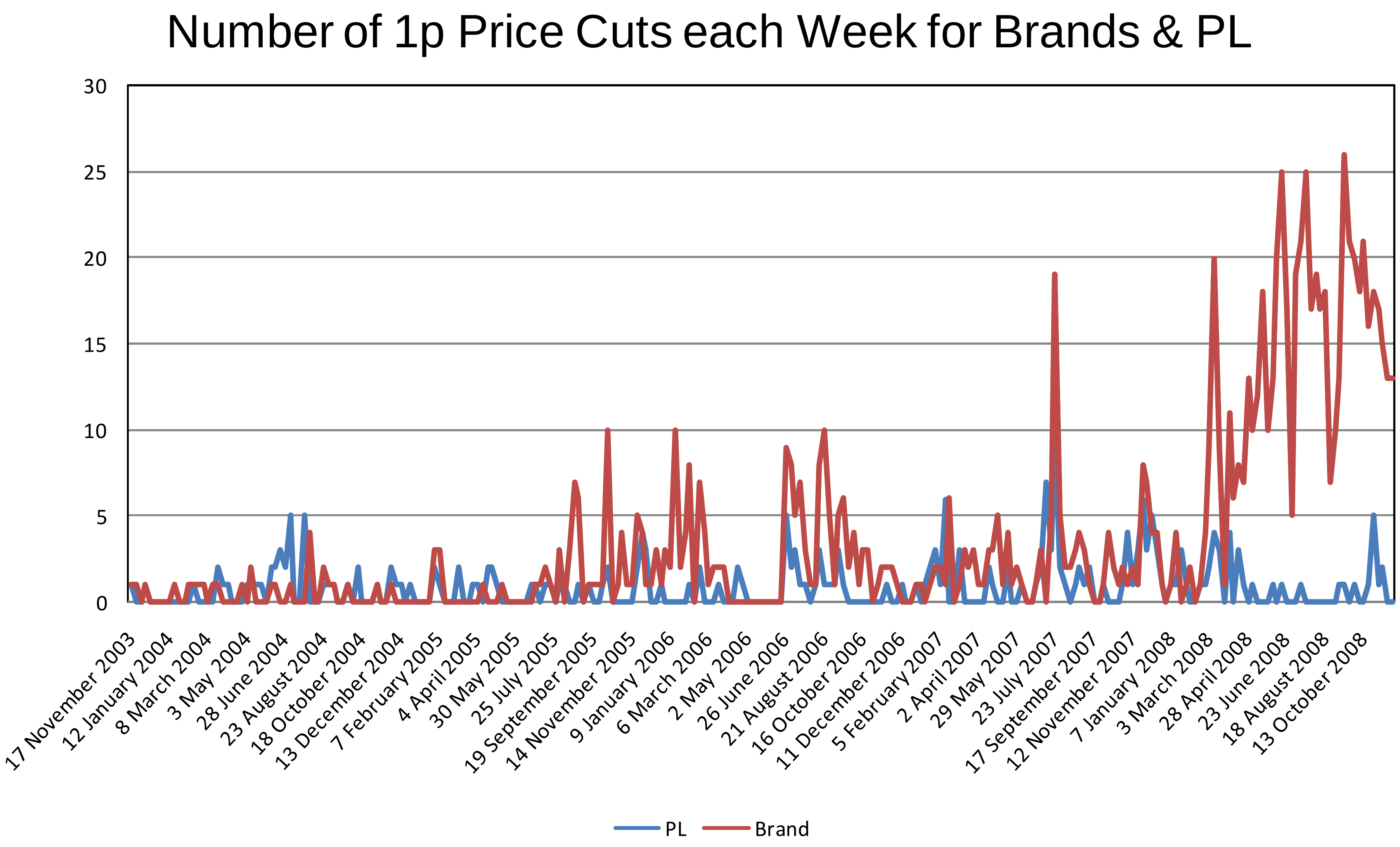
Retailer price matching – rises and falls less on OL



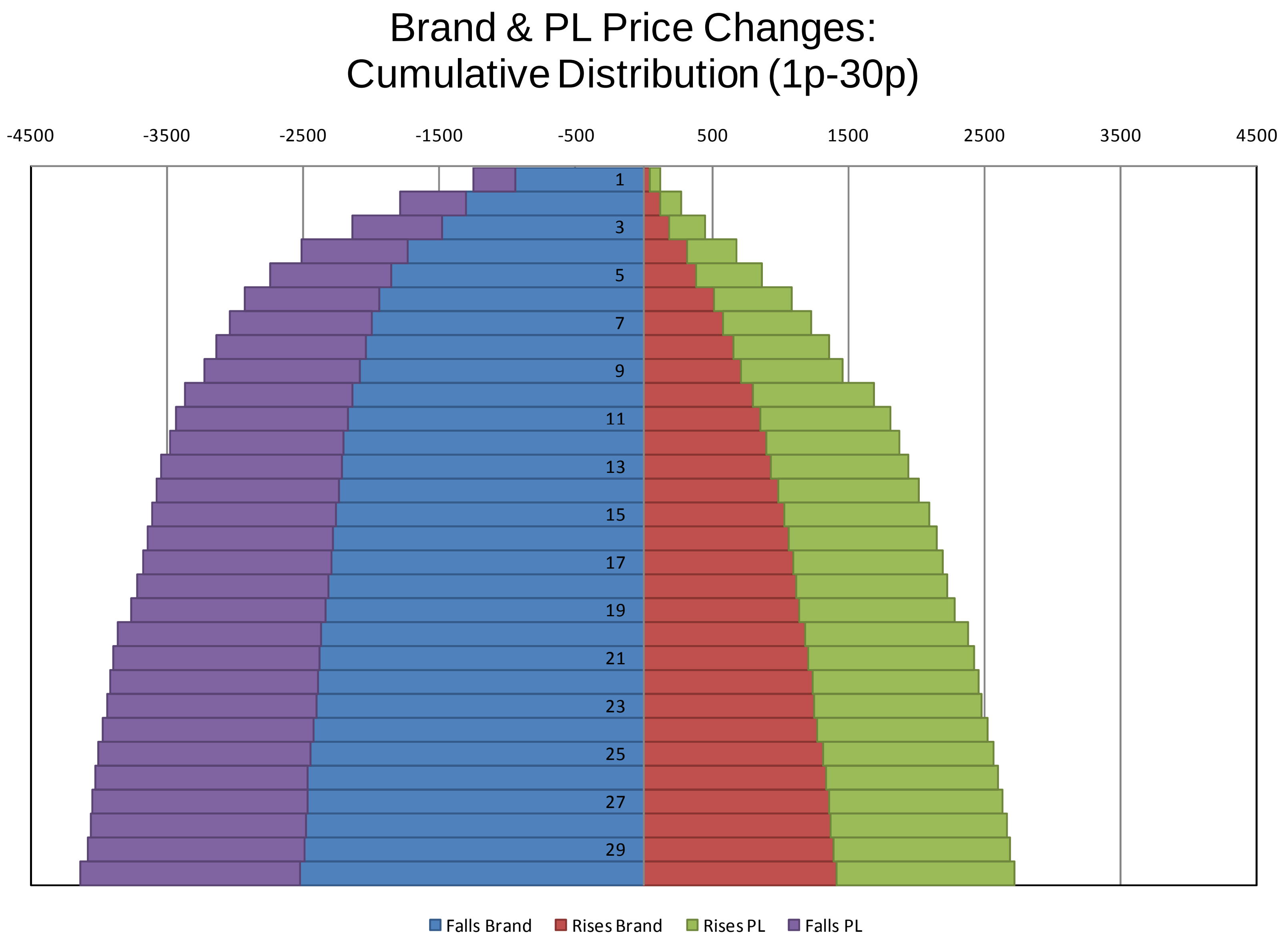
Increasing Price Volatility



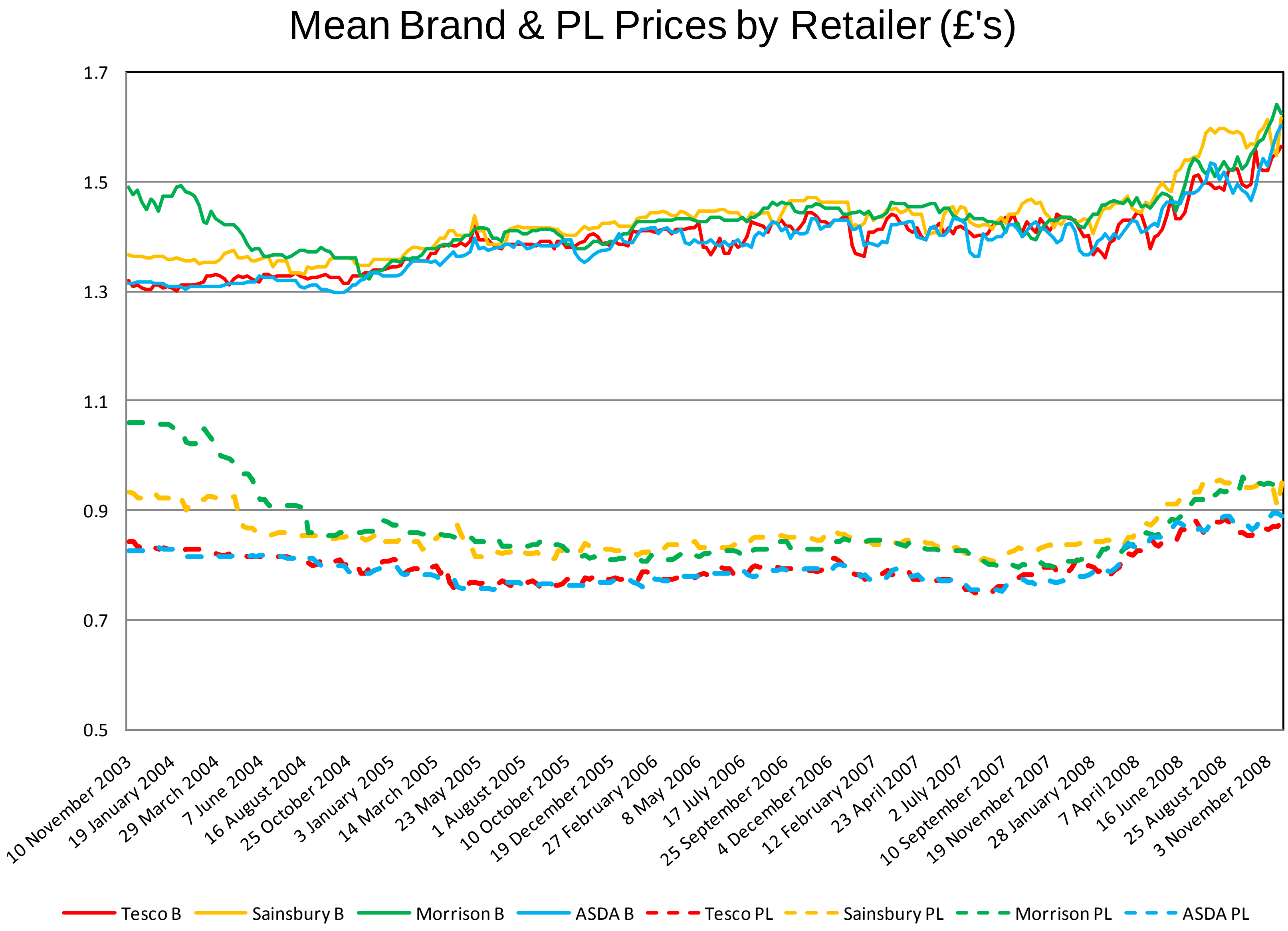
....but many price cuts are just one penny



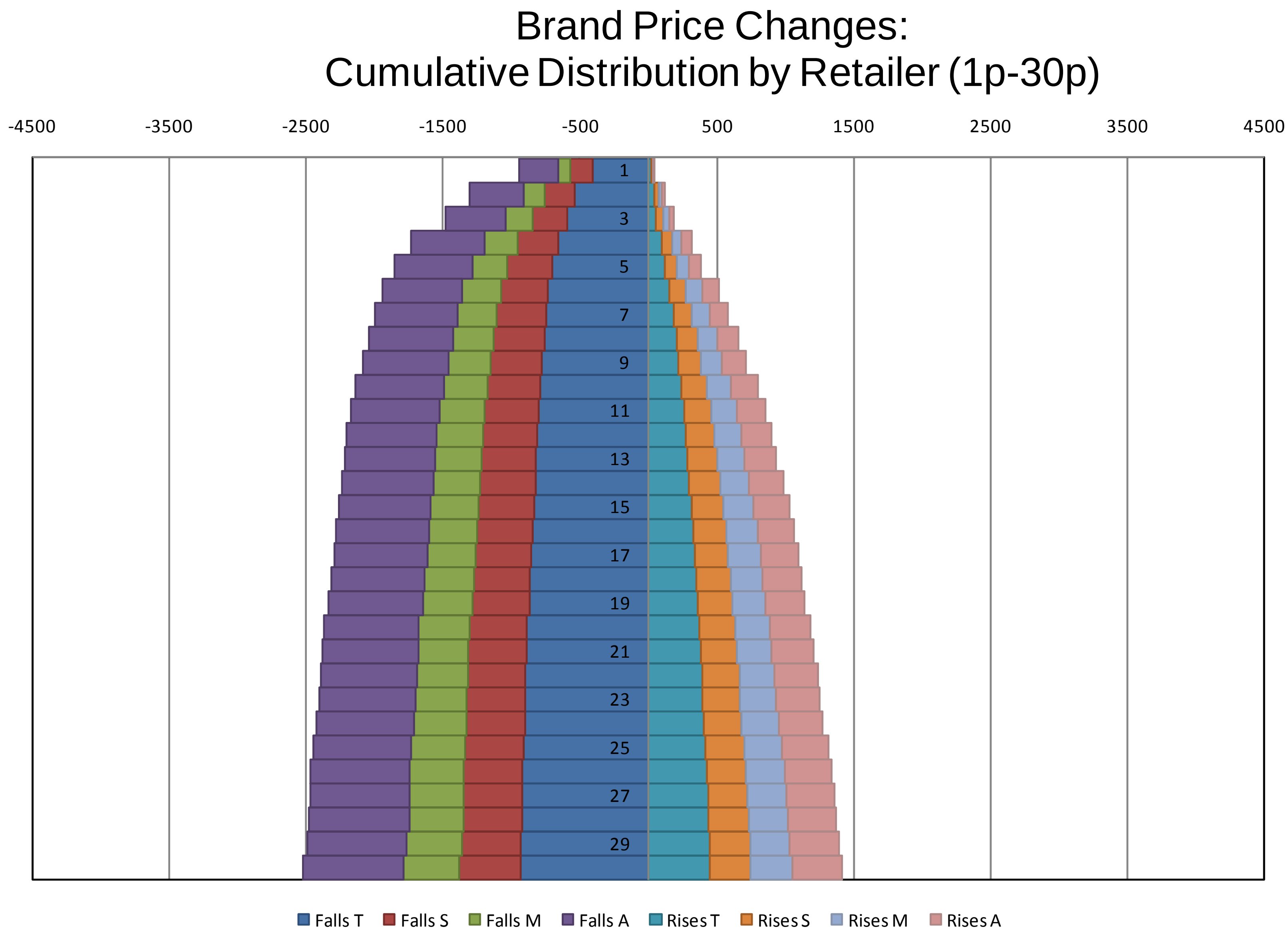
Price cuts more frequent than price rises



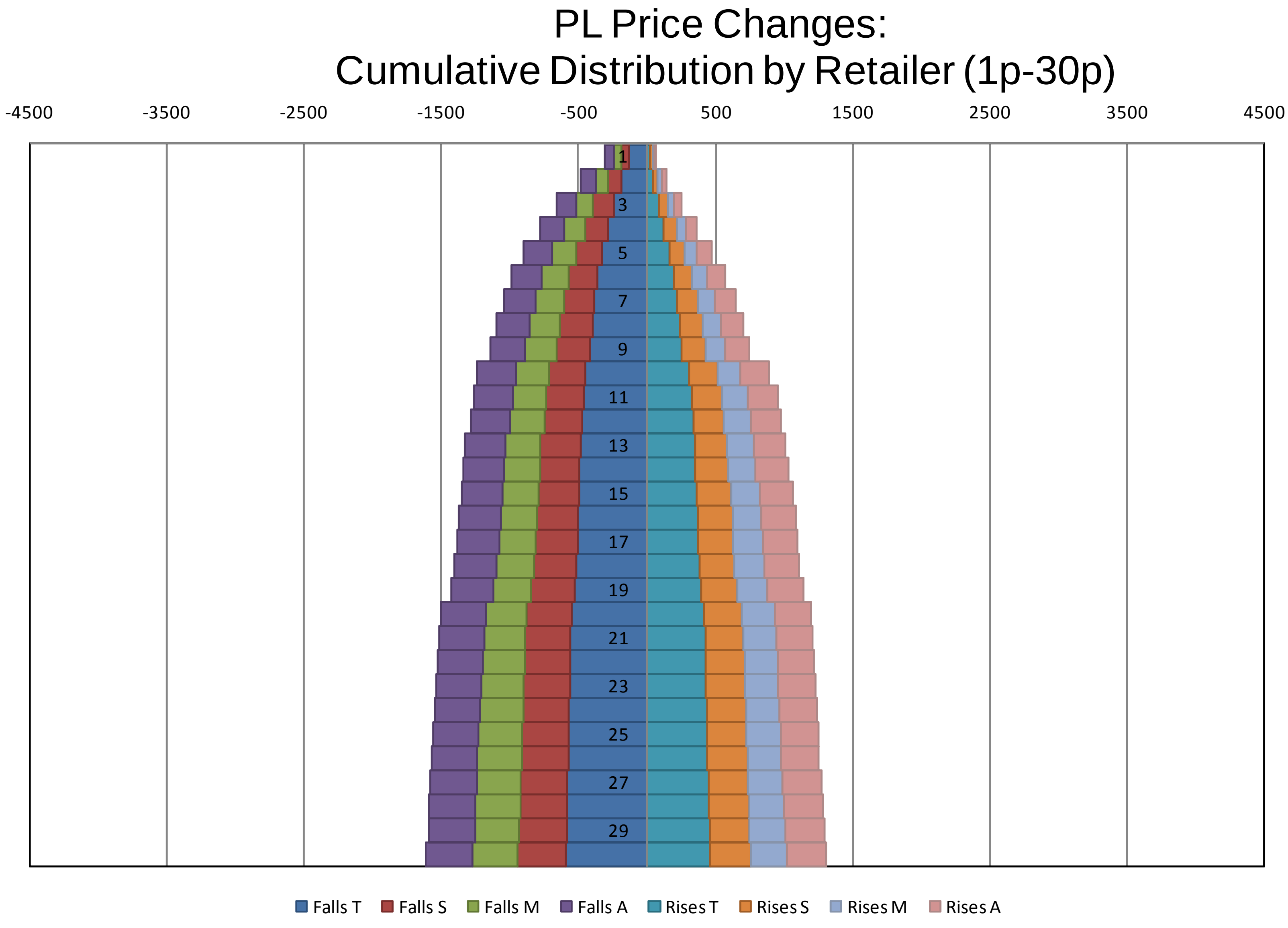
....but average prices rising over time



Brand price churn greater at Tesco & Asda



….less OL price churn and more symmetric

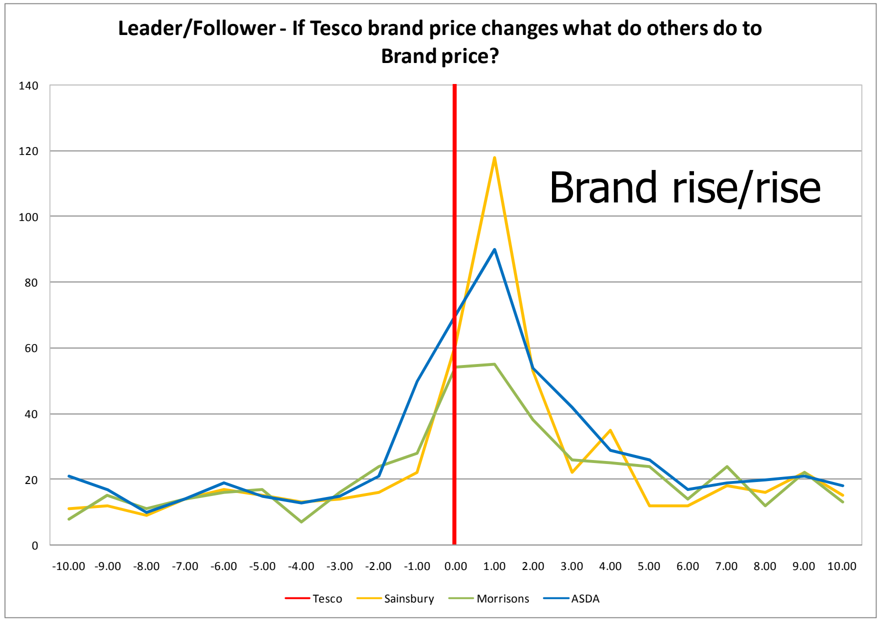


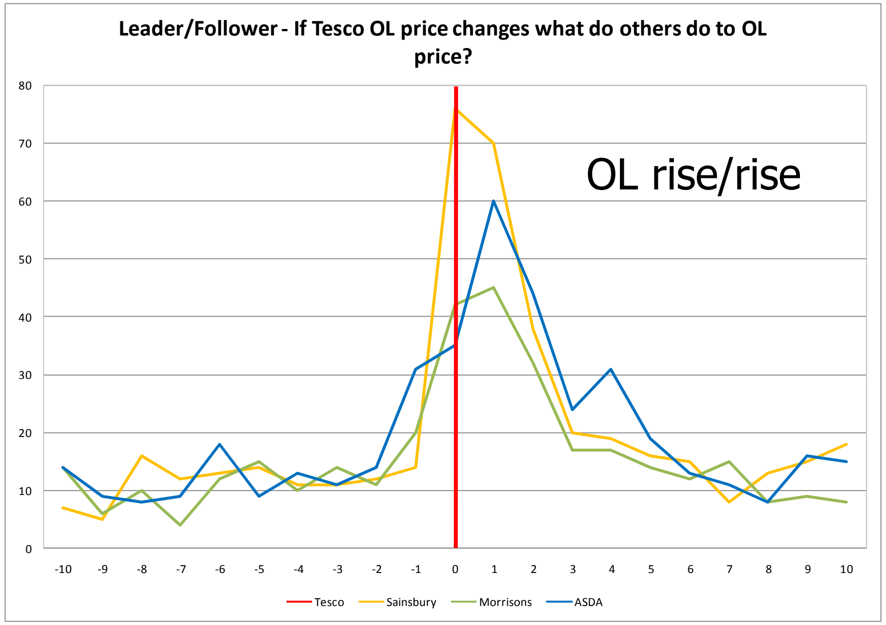
Alternative Explanations

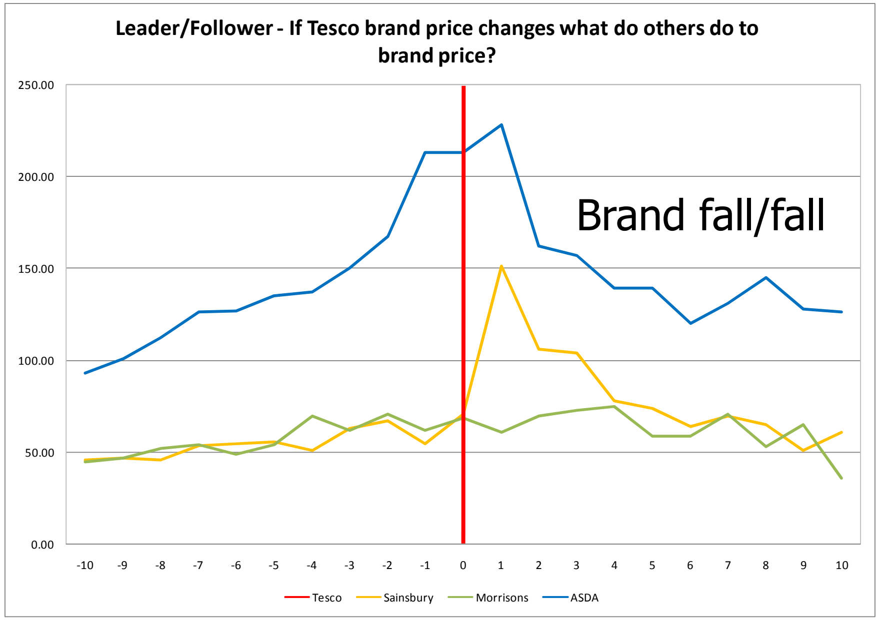
- *Outcomes down to manufacturers?*
  - Manufacturers cannot fix retail prices (as RPM is banned)
  - Temporary price reductions co-funded but does not explain small price changes on brands
  - Little indication of fixed or regular interval (e.g. annual) brand price rises

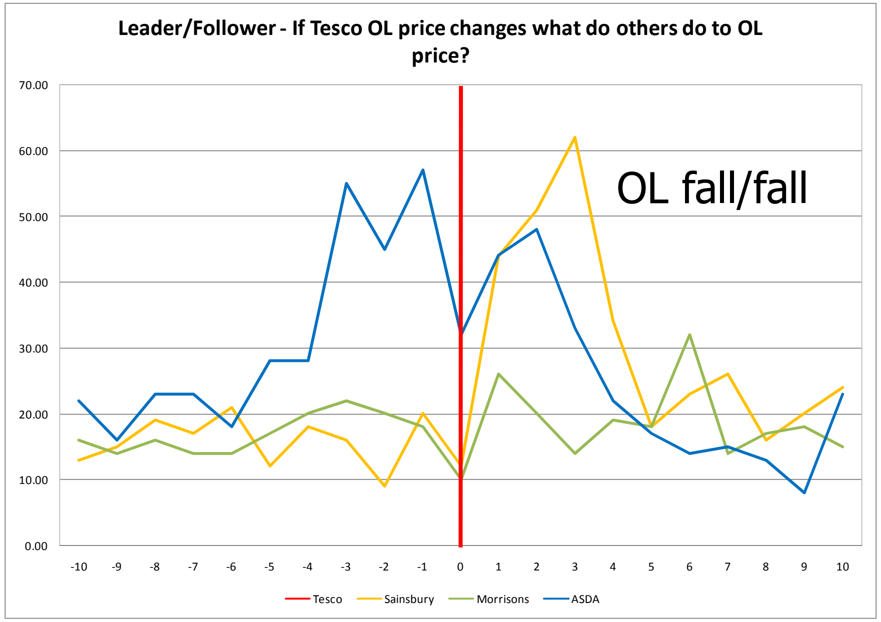
- *Innocent retail behaviour as an outcome of effective competition preventing price manipulation?*
  - But is retail price competition effective?
    1. Indication that price leadership behaviour exists
    2. Indication that brand/OL price movements very weakly aligned – suggesting consumer segmentation strategy

Leads/Lags to Tesco Price Changes

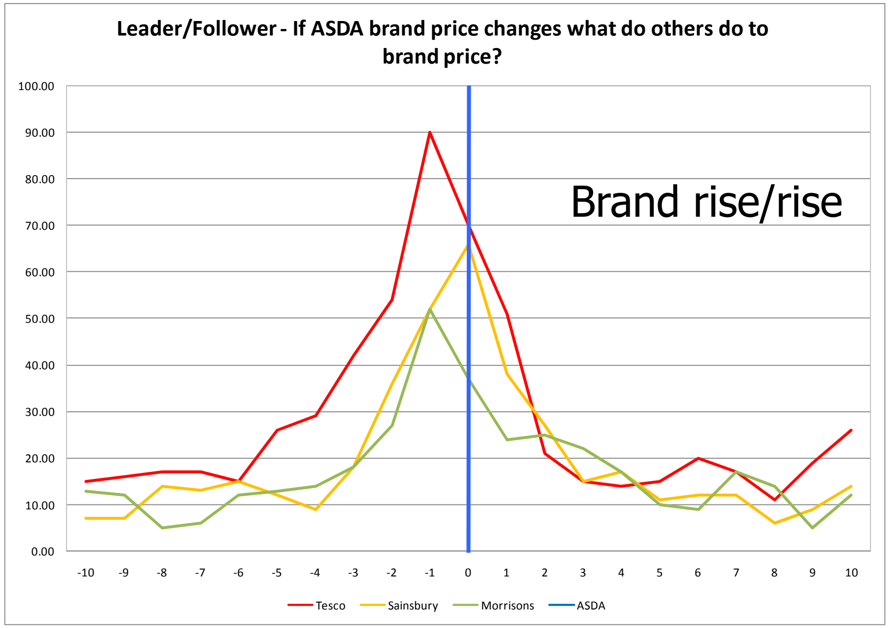


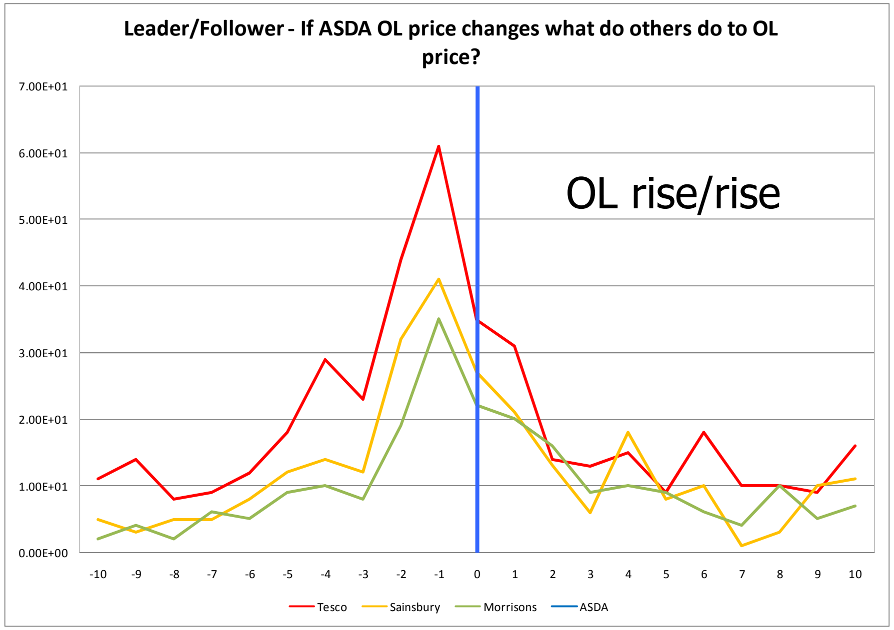


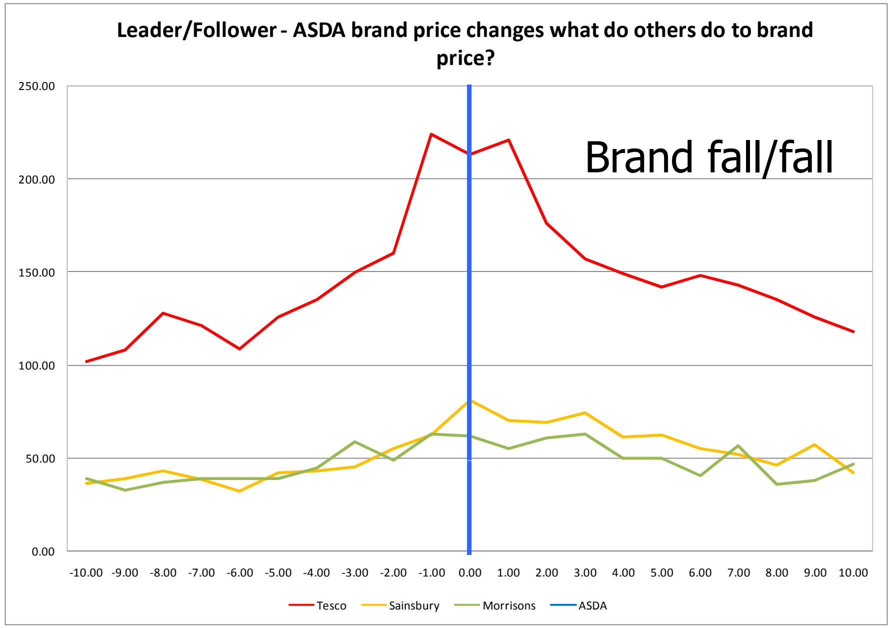


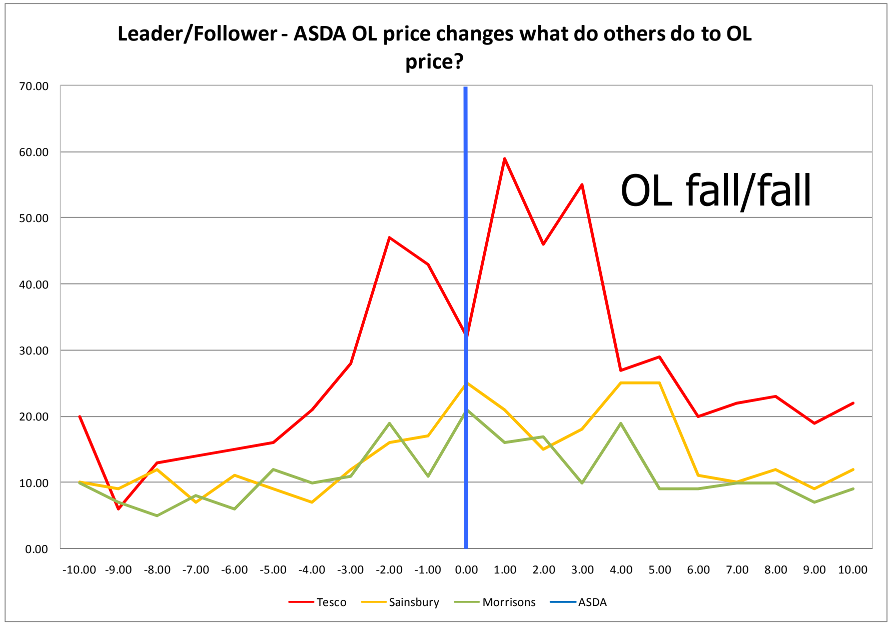


Leads/Lags to Asda Price Changes









Price Correlation Analysis

- Average correlation coefficients across the sample:

	Tesco B	Sains B	Morr B	ASDA B	Tesco OL	Sains OL	Morr OL	ASDA OL
Tesco B	1.000	0.628	0.503	0.682	0.180	0.132	0.075	0.192
Sains B	0.628	1.000	0.523	0.620	0.227	0.217	0.129	0.250
Morr B	0.503	0.523	1.000	0.503	0.220	0.235	0.232	0.239
ASDA B	0.682	0.620	0.503	1.000	0.183	0.154	0.083	0.212
Tesco OL	0.180	0.227	0.220	0.183	1.000	0.652	0.505	0.830
Sains OL	0.132	0.217	0.235	0.154	0.652	1.000	0.583	0.622
Morr OL	0.075	0.129	0.232	0.083	0.505	0.583	1.000	0.493
ASDA OL	0.192	0.250	0.239	0.212	0.830	0.622	0.493	1.000

- Warning: interpret with caution given non-stationarity/cointegration issues, oddly behaved residuals, and very little change in the data

Implications: Effects on Competition

Private label favouritism could distort competition:

- *Restricted access for brand producers*
  - secondary brands replaced by PL and store "discounter" brands
  - difficulty for new brands to gain entry
- *Undermining brand investments*
  - "me-too" PL free riding on marketing, formulation and packaging
  - "copycat" PL free riding on brand image and goodwill
- *Raising rivals' costs*
  - increased brand advertising, R&D effort, funded price promotions, shelf-space fees and other payments/obligations to retailers

Implications: Effects on Consumers

Private label favouritism could harm consumers:

- *Poor value*
  - E.g. "umbrella pricing" – PL tracks brand prices rather than costs
- *Misleading value*
  - E.g. "goldilocks pricing" – distorted pricing architectures
- *Undermined value*
  - E.g. "yo-yo pricing" – damage brand image and worth
- *Restricted value*
  - E.g. restricted choice with brand foreclosure
- *Declining value*
  - E.g. moral hazard problem deters future brand investment

Conclusion

- Retailers in "double agent" position as *customer* and *competitor* for branded goods producers
- Scope for favouring private label over brands through switch marketing and strategic retail pricing
- Concerns about distorted competition leading to consumer harm
- Empirical work required to determine the extent of the problem and its effects on the market
- Consideration of policy measures to protect competition?