

[pricing study]

A CONSUMER PERSPECTIVE:
**DYNAMIC
PRICING**



[whitepaper of results and implications, 2021]

Introduction to Dynamic Pricing

Not only since the COVID-19 pandemic, where prices for hygiene masks and sanitizers increased significantly, dynamic pricing is a hot topic. A recent study by the German Federal Cartel Office shows that gas stations adjust prices several times a day during the course of the day, seeking to maximize profits in line with high levels of traffic.



Figure 1: Price differences during the day on the example of E5 fuel

Source: Bundeskartellamt, Markttransparenzstelle für Kraftstoffe, 2020

Also, the airline or hotel industry uses Yield Management – a special form of dynamic pricing – to market their capacities in advance with dynamically changing prices.

Dynamic pricing is omnipresent in everyday life. No wonder, if dynamic pricing is used intelligently, it can have major benefits for companies such as maximization of company revenues, exploitation of customer willingness to pay (even varying with time) and higher competitiveness in dynamic markets. Consumers may benefit as well, for example by making a favorable deal.

In addition to those benefits, with the rise of e-commerce and new technologies like artificial intelligence and advanced pricing software, prices can be changed easier and more effectively than ever. This development makes dynamic pricing attractive for a variety of industries.

With this article, EbelHofer Consultants helps to address and reflect on the following questions:

- Is dynamic pricing attractive for my company?
- How well is dynamic pricing accepted by consumers?
- Are there price drivers that are particularly well accepted by consumers?
- Which distribution channel is attractive for dynamic pricing?
- What prerequisites do I need to consider for dynamic pricing?

Study Design

In our recent study on the drivers of dynamic pricing and their acceptance from a consumer perspective, the fashion industry served as a focus sector. A mixed methods approach was applied, consisting of:

- a) Expert interviews with informants from backgrounds in consultancy, software, research, seeking to gain in-depth insights into business practices and success factors.
- b) Online survey on the consumer perspective with a total of ≈340 participants.

Study Results

While dynamic pricing may be omnipresent in everyday life, the study reveals that not even half of the study respondents accept dynamic pricing approaches. It is thus necessary to better understand consumer sensitivity and acceptance towards specific drivers of dynamic pricing.

A consumer perspective:

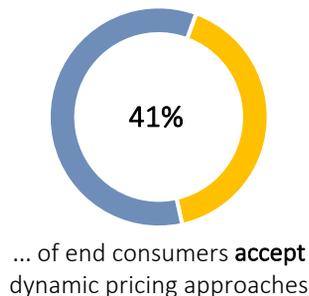


Figure 2: Acceptance of dynamic pricing

» Accepted drivers: Time and demand

Time is the most important driver in dynamic pricing according to expert interviews and the online survey. Particularly seasonal price changes are well accepted by consumers who have learnt over years that prices change each season. Thereby, a low frequency of price changes is perceived as fair.

Also, price adjustments due to low and high demand are accepted. During periods of low demand when prices decrease, consumers are under the impression of making favorable deals. In case of demand peaks, the logic doesn't necessary apply in a reversed manner with a higher price leading to a negative buying decision. The price is just one parameter among other emotional aspects such as brand image or reputation.

» Not accepted drivers: Individualization, high frequency & weather

Expert interviews reveal that especially price differences on an individual customer level are perceived as unfair and tend to be not accepted. Also, the acceptance of dynamic pricing decreases with an increasing frequency of price changes.

Price adjustments due to weather conditions are not accepted, as the evaluations of quality and financial value behind most products, e.g. for clothes, remain equal. The consumer receives no additional value from dynamic price adjustments. Furthermore, price adjustments due to weather conditions could even lead to the feeling of being exploited.

Drivers are accepted differently

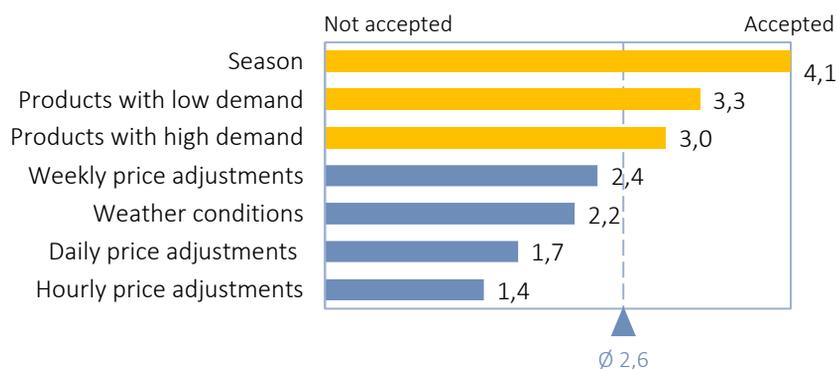


Figure 3: Acceptance of selected drivers

» Online retail is the channel with the highest acceptance

Dynamic pricing is more likely to be accepted in online retail whereas in stationary retail consumers expect a certain price stability. Online retail benefits from the fact that dynamic pricing is easier to implement and more cost-effective compared to stationary retail where, for example, electronic shelf labels must be installed.

Online retail is the most accepted distribution channel

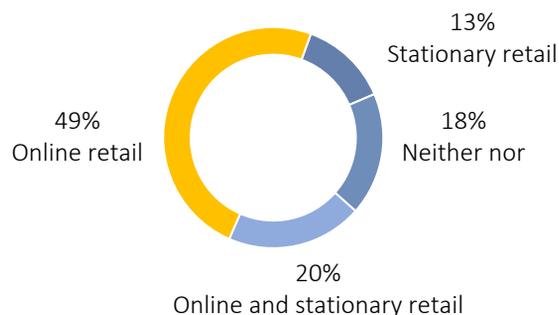


Figure 4: Acceptance of dynamic pricing by distribution channel

Transparent price adjustments are essential for the acceptance

Through access to apps and price comparison sites, consumers gain more insight into prices. Consumers thus appreciate transparency for reasons behind price fluctuations and general notice of the application of dynamic pricing by retailers. For example, when an item is added to the personal wish list on amazon, price changes of these items are indicated. Consumers see that they can benefit from dynamic prices when prices fall. With increased transparency and notice, it is not only possible for consumers to better understand fluctuations. Also, they may build a stronger trust in the company once arbitrariness and financial exploitation can be excluded as drivers of dynamic pricing. Therefore, transparent price adjustments increase the acceptance of dynamic pricing.

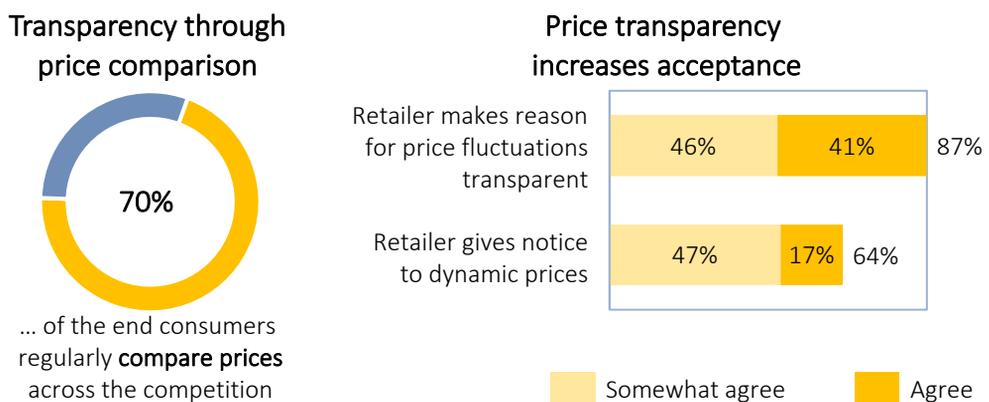


Figure 5: Transparency through price comparison and companies

Prerequisites for applying dynamic pricing

To apply dynamic pricing successfully, a strategic fit between the pricing strategy and the overall corporate strategy and goals should be given. On a more operative note, a successful implementation requires sufficient company resources in IT-know-how, data management and pricing managers to implement and operate the pricing process. While IT-infrastructure and algorithms can assist companies to implement dynamic pricing, the human element of pricing managers should not be disregarded, as illustrated by the following example: on the online platform amazon, a book was offered for a price of \$23 million. The reason: the pricing software tools of two retailers tracked each other and pushed up each others' prices without anyone monitoring.

Furthermore, a valid database must be provided including, for example, digitalized transactional information, consumer purchasing behavior or KPI's. Besides, the company needs the possibility to adjust prices without major investment in time and financial resources as in online retail.

Pricing software should only be used as a support and not as a substitute for the functions of pricing managers. Otherwise, the intuition for consumers gets lost.

In addition to strategic and operational considerations, it is important to understand that dynamic pricing is not suitable for every product. Especially seasonal products or products with a short product life-cycle, e.g. swimsuits, qualify for dynamic pricing. Luxury goods, which are part of a standard or rather traditional portfolio, typically have rather constant prices (except for annual price increases). Dynamic pricing may not be suitable for these goods.

Recommendations for successfully implementing dynamic pricing

The following Do's and Dont's should be kept in mind to make your dynamic pricing implementation a success story:

»» Do's

- Select a suitable distribution channel, for example online retail, and align your multichannel pricing strategy.
- Use dynamic pricing especially for seasonal products or products with a short product-life-cycle.
- Choose the right price segment: Dynamic Pricing is best suitable for the medium price segment (comparatively large price range and high willingness to pay by consumers).
- Include unique company-specific drivers in the pricing process to optimally respond to price adjustments to your consumers (e.g. consumers' purchasing history).
- Use value pricing to make sure not to leave money on the table. Ensure competitive price levels in order to not price yourself out of the market.
- Create the impression of transparency to the consumer.
- Communicate the benefits of dynamic pricing to the consumer.
- Involve experienced experts in the implementation process.

»» Dont's

- Price adjustments should not be exaggerated with respect to frequency and magnitude of price changes.
- Weather-driven price adjustments should be avoided.
- Use pricing software as a support and not as a substitute for the functions of pricing managers. Otherwise, the intuition for consumers gets lost.

In a nutshell

The application of dynamic pricing helps your company to maximize profits and to stay competitive in a constantly changing market environment. To implement the pricing strategy successfully, it is recommended to clarify your objectives first, ensure to meet the prerequisites and finally select the right drivers and support to implement the change in your company. Professional value pricing approaches ensure a good balance between profitability and competitiveness.

EbelHofer Consultants helps you on your way to more market and consumer orientation in sales and pricing. We are happy to assist you along the entire implementation process of dynamic pricing from rethinking your pricing, over selecting the right resources and solution to managing the change.



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