The Wall Street Journal has reported that Proctor & Gamble Co.'s new CEO, Robert McDonald, is “slashing prices” and warns of an impending price war in the branded consumer packaged good (CPG) industry. Yet, in this article, the author argues in favor of P&G’s tactics and explains how this strategy is both applicable and effective in the new, recovering economy. Tim Smith, PhD is the Managing Principal of Wiglaf Pricing, Adjunct Professor of Marketing at DePaul University, Academic Advisor and Facilitator for the Certified Pricing Professional (CPP) designation, and author of Pricing Strategy: Setting Price Levels, Managing Price Discounts, & Establishing Price Structures to Win the Market. He can be reached at tsmith@wiglafjournal.com.

In this article, I argue in favor of Mr. McDonald and moreover why he might be prescient in taking a sensible pricing strategy shift to meet the post-recession market demands.

Up the Price-to-Benefits Trajectory

For decades following the 1940’s, the US economy was growing and much of the middle class was enjoying greater wealth and spending power. With their increased spending power, these middle class consumers sought not only more products, but also better products.

To meet the demand for more and bet-
In the 1990’s two forces however put a halt to the value of this strategic trajectory. First, the introduction of low cost store brands that Sanford Bernstein research reports as being perceived as “good or better than those they replaced” in the consumer’s basket of goods. Second, incomes stopped growing.

**Entry at the Bottom**
The lower priced discount and store brands began eating away at branded consumer packaged goods’ pricing power early in the 1990’s. Evidence of their growing strength can be seen through the increased market share of store brands and the growth of store-brand only retailers such as Aldi. (See 1990-2009 P&G Competitive Landscape for a conceptual representation.)

To combat this growing threat, branded consumer packaged goods firms relied on couponing, trial offers, and promotional bundles in order to induce customers back into the brand fold. This approach may have stemmed some market share erosion, yet discount promotions are a blunt instrument at best.

As customers tried store brands, they began to determine that the difference in benefits between branded goods and store goods didn’t outweigh the difference in price. As such, the ability of discounts to attract customers that would convert to becoming a profitable and loyal following waned.

While the threat of lower priced store brands was at best contained through targeted discounting strategies, a second shift to the marketing environment was underway.

**Income Growth Arrested**
Since 1999, the middle class has seen flat to falling incomes in inflation adjusted dollars. Their newly found poverty, or at best limited income growth, has driven a purchase behavior towards a more discriminating position. (See US Median Income Stopped Growing in 1999.)

Without a growing income within the core consumer market segment, the strategy of constantly improving and up-selling customers to higher price and benefit points becomes an economic anathema.

To be clear, some customers will continue to be willing to pay more for some items. Splurging does continue, but it is proving to be more selective. For instance, a middle class business man may be willing to accept store brand bathroom paper towel but eschew anything less than an Allen Edmonds’ shoe. Or, skimping on the dentist may imply a higher willingness to pay for Crest premium dental products. Yet does the difference in benefits between P&G’s Charmin and Albertson’s Homelife Soft Choice outweigh the differences in price? They both end up down the toilet.

The flip side of an increased selectivity in customer’s willingness to pay for higher benefits is that that the mass market has moved to lower price / lower benefit demands. That is, consumers are increas-
Anecdotal evidence appears to point to a price reduction that has been targeted appropriately to meet the needs of the increased demand for “good enough” products.

P&G’s US market share in 8 out of the 13 largest product categories increased in recent months according to Consumer Edge Research, LLC.

Moreover, P&G increased or maintained market share in all regions of the world for the quarter ending June 30. Yet the evidence is mixed. P&G also reported profits falling by 12% for the quarter ending June 30, 2010 due to increased advertising expenditures and lower prices.

Communicate

The likelihood of an all out price war can be contained. To do so, Mr. McDonald has to improve his messaging to investors and consumers (as well as competitors) regarding the focus of the pricing policy shift.

By focusing his price decreases on the lowest value products within the category, P&G can meet two challenges with
one instrument: the increase in store brands and the lost buying power of their customer base.

**Up, Up and Away into Till the Field**
The past progression of improving the benefits and raising the prices matched middle-class income growth of US. The current and foreseeable future stagnation to decline in middle class incomes implies that the past strategy will fail.

A shift in pricing policy that focuses on the needs of the growing price sensitive market segment should prove profitable in the US, Europe, Japan, and rest of the developed world. (P&G’s Brazilian and Emerging Market strategy requires a separate missive.)

Mr. McDonald, I suspect you have been prescient in taking a wise strategic shift in pricing policy to meet the post-recession market demands. But suspicion isn’t proof and I hold insufficient data to confirm my suggestion. Until either of the gaps are closed, good luck McDonald.

**References**


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