

The 1% Principle

Is 1% a little or a lot? One of the smartest and most successful food retailers I've ever known once asked me this question ... and then taught me how to find, and use, the answer.

by Brian Woolf (August 4, 2014)

1% Price Change

“Consider,” he asked, “if we lowered our prices by 1% across-the-board. Would it affect our sales? Unlikely. A 1% price change doesn't get noticed.” I agreed.

“If instead we took items that comprise 5% of our total sales and dropped their prices by 20%, would that affect our sales? Of course. They'd be noticed and sales would rise.

“Are you aware of what I just did?” he prodded me. “The two options cost us the same, 1% of sales. (Calc: $100\% \text{ sales} \times 1\% \text{ price reduction} = 1\% \text{ sales}$; $5\% \text{ sales} \times 20\% \text{ price reduction} = 1\% \text{ sales}$.) Yet the first option has little impact; the second a lot more. Same cost. Different effect.”

The lesson? It's not so much the size of a price decrease or increase but how it is spread across your item offering. It's how it is spread that determines whether its impact will be a little or a lot. Spreading it equally over all sales (as in option 1) is a lot less attention-getting than taking the same amount of money and concentrating it on a group of selected items (as in option 2).

You have probably thought of other price change options that also cost 1% sales, notably a 10%-price reduction on items comprising 10% sales ($10\% \times 10\% = 1\%$); and a 5%-price reduction on items comprising 20% sales ($5\% \times 20\% = 1\%$).

Does The Principle Apply If There's No Overall Price Change?

Consider your current prices. Can the 1% Principle be applied without lowering or raising your average price? Yes. In option 2 above, for example, items comprising 5% sales were reduced by 20%, costing an overall 1% margin reduction. So what do you do if you want the effect of those 20% price reductions yet still be cost-neutral? Simple: raise the prices on the items comprising the other 95% sales by 1.05% ($95\% \text{ sales} \times 1.05\% = 1.0\% \text{ sales}$). Obviously, you would probably choose not to do this overnight but over time as price changes are

received. As noted at the outset, this off-setting price increase of a hair over 1% will trigger little customer reaction.

This is an important point. Applying the 1% Principle, you can improve your price perception while keeping your average prices the same. In other words, you can improve your price perception while maintaining the same price gap with the low-price leader in your marketplace. And it's easy to do.

The 1% Principle in Practice

The *Customer 5% Reward Program* ([read about it here](#)), that offers a group of 12-15 Loss Leaders to Regular Customers, has some of its markdowns offset by a small across-the-board price increase. The price reductions are dramatic; the wide price increase is insignificant. Result: no increase in the average selling price or the size of the competitive Price Gap.

The idea behind the 1% Principle is also used when Price Optimization companies are hired to help retailers regularly reset their shelf prices with the objective of increasing overall margins. This outcome is achieved by adjusting selected individual prices (by more than 1%) on items that are somewhat price insensitive or unlikely to be noticed rather than a widespread 1% increase. The objective is a little different but the focus is the same.

The Loss Leader approach to price adjustments could be described as “Sensible Approximation” and Price Optimization as the “Gnat’s Eyebrow” approach. Each company must choose what it’s primary objective is.

The Bottom Line

How would you describe your company’s price perception in customers’ eyes? Using the 1% Principle as a guide, do you see an opportunity to strengthen your price appeal without increasing your average price or the competitive price gap? Remember: 1% can mean a little ... or a lot!

Copyright © Brian Woolf

About the author...

Brian Woolf is a global leader in loyalty marketing and has written three definitive works on the subject, *Measured Marketing: A Tool to Shape Food Store Strategy*, *Customer Specific Marketing*, and *Loyalty Marketing: The Second Act*. He devotes his time to helping retailers develop, critique and strengthen their loyalty programs.

And there's more where this came from...

Visit us on the web for our complete collection of loyalty marketing articles, insights and practical advice, at

www.brianwoolf.com

E: brian@brianwoolf.com

T: +1 864 458-8277

*Retail Strategy Center Inc.
6 Parkins Lake Court,
Greenville, SC,
29607-3628
USA*

For more customer loyalty articles and research, we also recommend:

The Wise Marketer - free loyalty marketing news & research - TheWiseMarketer.com

The Loyalty Guide - the complete guide to loyalty marketing - TheLoyaltyGuide.com

Colloquy - customer loyalty news and webinars - Colloquy.com

Loyalty 360 - customer loyalty news and webinars - Loyalty360.org