PROFESSIONAL PPS PRICING SOCIETY™

PRICING ADVISOR

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The 5 Pitfalls of Conjoint Analysis in Pricing Research

by: Dr. Felix Friederich

Conjoint analysis is one of the most popular methods used in measuring the preferences of individuals or groups. It determines, for instance, the degree to which consumers value specific products, which then helps in developing sound pricing strategies. However, this method has some pitfalls that can hinder its effectiveness and application in pricing research, which the author addresses in this article. Dr. Felix Friederich is a Business Development Consultant at Horváth Germany. He can be reached at FFriederich@horvath-partners.com.

Introduction

In the realm of pricing strategies, the application of robust research methodologies stands as a cornerstone for informed decision-making. Discrete choice experiments, also called conjoint analysis, have been widely applied in various industries to understand consumer preferences and inform strategic decision-making, particularly in pricing. Whether it's Toyota and Ford in the automotive sector, Apple and Samsung in the technology industry, or Procter & Gambler and Unilever in retail and consumer goods, they all use this method to make better pricing decisions.

However, while the allure of conjoint analysis in pricing remains undeniable, a critical caveat demands attention. The effectiveness of the method depends on careful adherence to certain criteria and stringent standards that many practitioners still stumble over. In fact, failing to fulfill these requisites not only undermines the effectiveness of the method but also risks distorting the insights derived, potentially leading to flawed pricing decisions that fail to resonate with the targeted consumer base. This article identifies **five pitfalls** of conjoint analysis to help practitioners successfully and effectively use this method to optimize their pricing strategies.

> THE EFFECTIVENESS OF THE METHOD DEPENDS ON CAREFUL ADHERENCE TO CERTAIN CRITERIA AND STRINGENT STANDARDS THAT MANY PRACTITIONERS STILL STUMBLE OVER.

Conjoint Analysis in Pricing Research

Conjoint analysis is a quantitative research method used to measure how consumers value different product attributes or features.[1] It estimates the utility or value that consumers associate with each attribute. Specifically, conjoint analysis is highly effective in pricing research due to its ability to reveal consumer preferences and willingness to pay for specific product attributes. By assessing how consumers prioritize and trade off different attributes against price, the method helps in understanding the price sensitivity of consumers and in determining the optimal pricing strategy that maximizes perceived value and market competitiveness. The major advantage of the method lies in the simulation of a real purchase scenario, as participants have to choose between different options instead of ranking them. This makes the method a valuable tool for developing pricing strategies and optimizing product offerings to meet consumer demand. However, reaping the benefits of this method depends on several pitfalls that practitioners often stumble upon. The following section therefore outlines the five most common pitfalls of conjoint analysis.

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8 Is There a PERFECT Pricing Model?

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The Five Pitfalls of Conjoint Analysis

1. Research scope definition

The first pitfall relates to the scope, or the objectives, the analysis is used for. Conjoint analysis is particularly useful in determining the optimal combination of product features, functionalities, and consumer price sensitivity. Yet, for certain research objectives, other traditional methods might be more applicable due to lower complexity and scope focus. For instance, for pricing research aiming to solely identify willingness to pay or price elasticities, the Price Sensitivity Meter (PSM) or Gabor Granger are useful. Specifically, both methods are more suitable for **quick market assessments** as they are more practical and less complex in the study design. Second, both methods are specifically useful when the primary focus lies in assessing consumer price sensitivity as a **single attribute**, without evaluating trade-offs or preferences for multiple attributes simultaneously. Moreover, in **resource-constrained situations** (e.g., data availability) these methods are more likely to yield effective results without the need for extensive data collection and analysis. On the other hand, neuroscience tools like EEG, fMRI, and eye-tracking provide a deeper understanding of consumer preferences. Specifically, neural responses shared across individuals represent a universal index of preference and can be used to **improve forecasts** of market behaviour, particularly in terms of price perceptions.

Therefore: *Pricing researchers should not lose focus of the research scope. Conjoint analysis is helpful in exploring consumer utility perceptions, but it is not an "all-purpose" research method!*

2. Capabilities and resources

The second pitfall relates to the research capabilities. Projects can fail based on unfavorable decisions of executing in-house research or engaging external vendors. When considering in-house pricing research, the resources in terms of **expertise and specialized skills** to effectively conduct such projects have to be carefully considered. For instance, you should evaluate if **access to necessary tools and technologies** is available. That is, pricing researchers need to ensure the availability of typical purpose or statistical programming languages (e.g., Python, R or SPSS) as well as the handling of multinomial logistic or simple logistic regressions. Furthermore, practitioners need access to survey or feedback management tools (e.g., Qualtrics or Open Lab) for data collection. Conversely, when hiring external vendors, evaluating the vendor's **track record** and past performance in conducting pricing research projects is critical. Furthermore, assessing the **efficiency and speed** of execution that vendors can offer, taking into account their expertise, established methodologies, and dedicated resources for conducting pricing research is essential. Finally, the provision of in-depth industry knowledge and market experience from external vendors is crucial. This applies in particular to understanding specific industry-relevant product features and pricing schemes.

Therefore: *Research projects should not fail due to a lack of internal capabilities or collaboration with vendors who lack industry expertise - rigorous evaluation is key!*

3. Attribute and level selection

The third pitfall relates to the attribute and level selection. An unfavorable choice of attributes and corresponding levels leads to mediocre study insight. Therefore, well-chosen attributes and levels help in capturing the most relevant information from respondents, accurately

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reflecting consumer preferences. First, the selected attributes and levels should be **realistic and practical**, aligning with the actual product characteristics that consumers encounter in the market. Unrealistic or overly complex attributes may lead to respondent confusion and compromise the validity of the study. Second, achieving **balance and orthogonality** in the design of attributes and levels is essential. That is, to minimize potential bias and ensure that each attribute contributes independently to the overall utility function. And third, conducting pilot tests to **validate the relevance** of the selected attributes and levels is critical before proceeding with conjoint analysis. With this, the overall suitability of the attribute set among the target respondent group can be assessed. For instance, an efficient and straightforward validation approach is using pre-tests with small sample sizes and ranking the attributes and corresponding levels of importance.

Therefore: *The importance of an appropriate set of attributes and corresponding levels is often neglected but is key for insightful results. Resources must be devoted to this topic!*

4. Design generation

Once the proper attributes and levels have been selected, the fourth pitfall lies in the optimal design of the conjoint analysis to produce reliable and valid results. The design of such analysis will determine to a large extent the accuracy with which the preference parameters can be estimated. First, the design should carefully **distribute attribute levels** to ensure that each attribute contributes independently to the overall consumer preference estimate. This helps in preventing bias and confounding effects that may arise from uneven distributions or interactions among the attribute levels. Second, pricing researchers want to avoid **respondent fatigue**. That is, a well-structured design with a balanced number of choice sets and a manageable number of attributes helps in sustaining respondent interest and minimizing the likelihood of dropouts or incomplete responses. Third, a robust design ensures **efficient estimation of preference utilities** and partworths. This leads to more accurate and reliable results. By optimizing the design structure and maximizing the information content of the choice sets, researchers can enhance the statistical efficiency of the analysis and improve the precision of the preference estimates. When engaging with external vendors, the design creation and certain threshold applied for optimal design set-up should be evaluated.

Therefore: *An inefficient design leads to unreliable results. This pitfall should be avoided by carefully generating optimal study designs!*

5. Sample selection

The final pitfall relates to the sample size. Sampling plays an essential role in producing insightful and useful results, but it is often a victim of cost-cutting in studies. To avoid obtaining mediocre results, several aspects have to be considered. First, a well-defined and **representative sample** ensures that the results accurately reflect the preferences and behaviours of the target population. It helps in generalizing the research results to the broader market, enabling more reliable and applicable insights for decision-making. For this, the sample should not be restricted (ex-ante) to certain demographics or psychographics (rather using sample diversity ex-post). Second, the size and composition of the sample directly impact the **statistical power** of the study, and thus, the results. A sufficient sample size (~300 to 400 participants) enhances the statistical power of the analysis, allowing the detection of relevant differences in preferences and accurate estimates of preference parameters. This, in turn, ensures the robustness and reliability of the research findings.[2] Finally, a robust sample size allows for **segmentation analysis** (also in interplay with sample diversity) which allows identifying distinct consumer segments based on their preferences for specific product attributes and prices.

Therefore: *The sample size should not fall victim to the "reduction of study costs," as this directly leads to poor results. To avoid this pitfall, a robust sample size is required!*

Conclusion

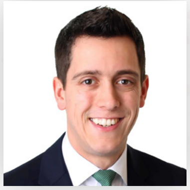
Conjoint analysis is a powerful and insightful tool for conducting pricing research. By assessing consumer preferences and trade-offs across various product attributes, it offers valuable insights into willingness to pay and price sensitivity. However, in order to fully exploit the potential of the method and derive meaningful pricing decisions, the pitfalls outlined in this article must be taken into account. In this way, the method's potential can be fully leveraged to help practitioners make informed pricing decisions and ultimately increase revenues.

1. The difference between conjoint analysis and discrete choice experiment is not considered. Traditional conjoint analysis is based on conjoint measurement, while discrete choice experiments are based on random utility theory.
2. Sample size depends to a large extend on number of included attributes and levels.

Mastering the Price Wars: Thriving in Competitive Markets

by: Ed Heskins

Successfully navigating pricing challenges in a competitive environment requires a comprehensive understanding of your value proposition, segmented by customer type, and supported by price data and pre-approved responses. With these in place, your business will be in a strong position to rise above the competition, as the author explains. Ed Heskins is Head of Pricing, Europe, at Iris Pricing Solutions. He can be reached at eheskins@pricingsolutions.com.



To be in business is to be in competition. Few, if any, businesses operate in a vacuum, and even if your products and services are highly differentiated, customers will often seek alternatives to compare you with. In this way, pricing against your competition is as challenging as it ever was.

In other respects, however, the challenge today is far greater. With the rise of eCommerce and, alongside it, dynamic pricing, consumers have never been better informed, nor better able to take advantage of differences in pricing. And price wars have never been easier to start. So how should the savvy pricer look to stay on top of pricing in a competitive environment?

Document Your Value

The first step is to document precisely how and where your business offers differentiated value. Define who your competitors are, how these differ between different customer segments, and the extent to which different aspects of your offer meet customers' needs.

We use Price Value Mapping, which allows businesses to visualize their market and develop hypotheses for pricing responses in different scenarios. Begin by building up a picture of your competitive environment based on the knowledge across your business, including input from sales, marketing, finance, and product or service delivery teams.

Once you have documented value drivers and performance scores across your various customer segments and product areas, validate these insights through direct research with your customers. Be prepared to challenge assumptions within the business on what factors customers consider important, and how your solution is perceived to perform.

WITH THE RISE OF ECOMMERCE AND, ALONGSIDE IT, DYNAMIC PRICING, CONSUMERS HAVE NEVER BEEN BETTER INFORMED, NOR BETTER ABLE TO TAKE ADVANTAGE OF DIFFERENCES IN PRICING.

Segment Your Offer

For different customers, your offer will provide different levels of value. For this reason, price segmentation is the backbone of any good pricing strategy, and it is especially important when customers have a range of options from which to choose. Using your value maps as a guide, identify those customer groups where you offer the greatest incremental value relative to the competition.

Now identify how you can segment your offer to ensure your value proposition is targeted for each group. This may be by offering low-cost, low-value products to cater to your most price-conscious customers, or bundling together features in a way that maximizes the value offered to attract those with a higher willingness to pay. An affordable core proposition combined with value-add opportunities can help you navigate a fast-moving customer base.

Gather Intelligence

"The most meaningful way to differentiate your company from your competitors... is to do an outstanding job with information. How you gather, manage, and use information will determine whether you win or lose."

Bill Gates (2009). "Business @ the Speed of Thought: Succeeding in the Digital Economy", p.12, Hachette UK

If you are in a consumer-facing or eCommerce business, then there has never been greater access to pricing data than there is today. Pricing data can be bought or built through the use of

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web-scraping solutions capable of tracking price changes on a weekly, daily, or intra-day basis. These can alert you to price adjustments requiring action before you see any shift in sales volumes.

For businesses whose competitors do not publish pricing online, gathering pricing data is complicated but just as important. Insights on competitor pricing and tactics, gleaned from conversations with clients, are often held within sales teams, but frequently remain undocumented. Capturing this in a central hub will allow for a joined-up response to changes in tactics. Customer research can also be used to build a picture of competitor pricing by proxy.

Plan Ahead

Armed with this information, it's time to build out our playbook. In the modern pricing environment, reacting swiftly to changing price conditions is crucial to maintaining an advantage, and defining our responses in advance will save you from wasting valuable time securing stakeholder buy-in when quick decision-making is required.

Define your pricing floors and ceilings; identify which competitors to track, which to monitor, and which to ignore; and agree on your authorization processes in advance. Build out your anticipated response to different price moves, including time to respond. Agree on the KPIs performance will be measured against and where this will be captured.

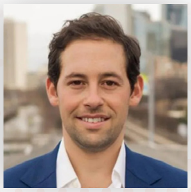
Track Results, Document Lessons Learned, Iterate, and Improve

Pricing challenges in a competitive market are not fixed. What works today may not work tomorrow. It's important to capture data on pricing performance, monitor your pricing strategy's effectiveness, and adapt as needed. Look out for changes to market trends, customer feedback, and competitor pricing strategies, which can all be indicators that you need to consider a change to your pricing strategy.

Ultimately, successfully navigating pricing challenges in a competitive environment requires a comprehensive understanding of your value proposition, segmented by customer type, and supported by price data and pre-approved responses. With these in place, your business will be in a strong position to rise above the competition.

Restaurant Cost and Price Increases: The Value of Digital and Loyalty Initiatives

by: Philip W. Daus and Dave Clement

Most restaurants anticipate being affected by recession and cost increases over the next year. How can brands continue to drive growth with price differentiation and digital & loyalty initiatives? Although specific to the restaurant industry, this article offers insights for pricing in the currently challenging global economy that can be applied across numerous industries. Philip W. Daus (philip.daus@simon-kucher.com) is a Partner in the Houston office and Dave Clement (dave.clement@simon-kucher.com) is a Partner in the New York and Toronto offices of Simon-Kucher & Partners. Erin Kilbride, Senior Consultant at Simon-Kucher & Partners, also contributed to this article.

Our recent study with more than 50 leading US restaurant brands revealed that 97% of brands expect a recession within the next year, the majority of whom believe it will affect the restaurant industry. Combined with an expected average cost increase of 9%, restaurants need to take action to protect margins, traffic, and guests. To do this, it is important for restaurant brands to implement strategic price increases as well as optimize digital initiatives throughout 2023 and into next year.

Restaurant brands should implement *next level price differentiation* to combat an expected 9% cost increase this year

Restaurant brands face several challenges this year with a looming recession and significant cost increases. While cost increases will not be as severe as 2022 for most restaurant types, the brands we surveyed expect an overall average 9% cost increase throughout this year, with fast food restaurants expecting a 15% cost increase.

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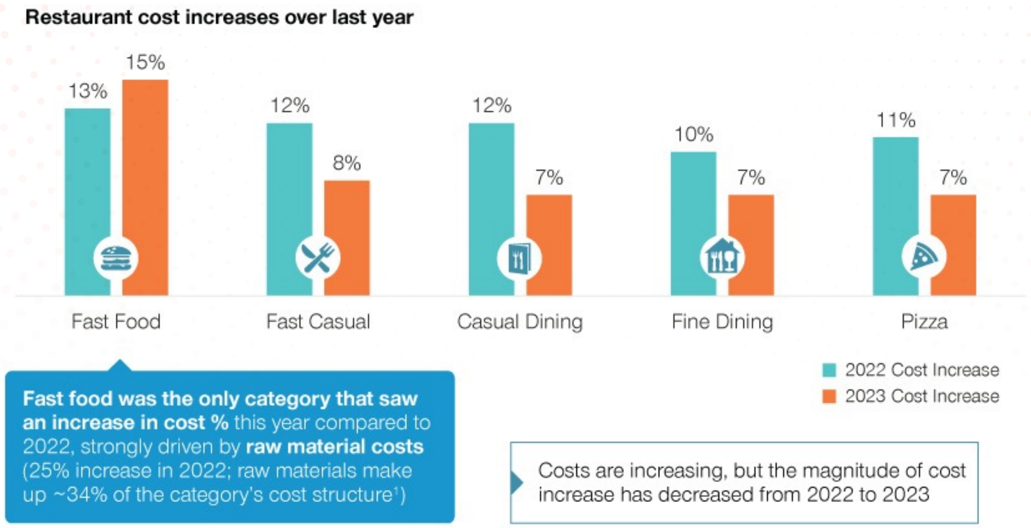
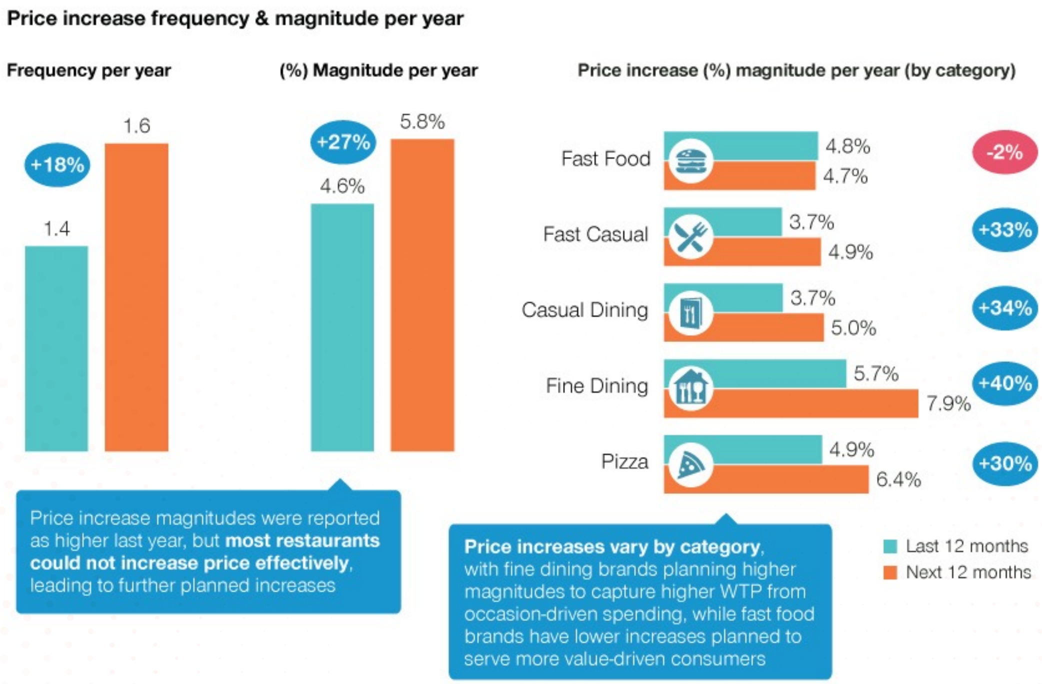


With strong expectations of a recession and as inflation continues to hit consumers' pockets, it is imperative that restaurants conduct precise price increases to cover costs and protect margin. Restaurants are planning for larger and more frequent price increases in 2023 compared to 2022, with the average total price increase in 2023 expected to be 5.8% (up 27% from 4.6% in 2022). The average planned price increase is even higher in fine dining restaurants (7.9%), likely driven by consumers' higher willingness-to-pay.



Although the average restaurant price increase this year is expected to be 5.8%, brands should not implement a blanket price increase as they see costs rise. Instead, it is becoming increasingly important to differentiate price increases, including next level price differentiation, as brands have exhausted standard differentiation strategies.

In the past, restaurants have primarily focused on differentiating price increases based on products, day/time, and store type. In 2022, we saw most brands implementing these methods to avoid blanket price increases. While these have helped in the past to implement precise price increases on products, times, and store types with higher consumer willingness-to-pay, there is an opportunity in 2023 to optimize next level factors like channel and store location. Differentiating price increases based on channel and location will allow brands to target their price increases toward areas with higher consumer willingness-to-pay to decrease the loss of volume and traffic.

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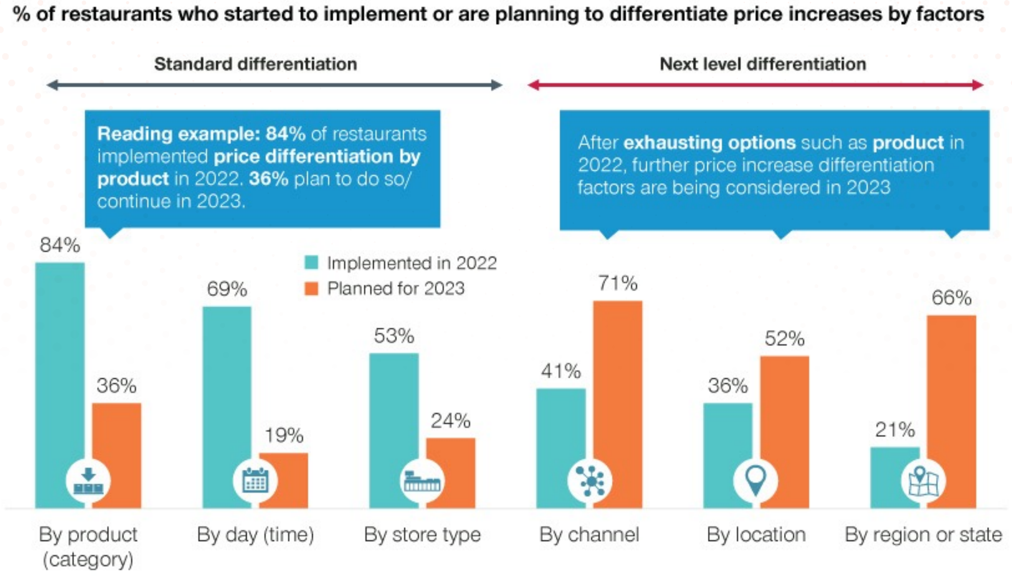
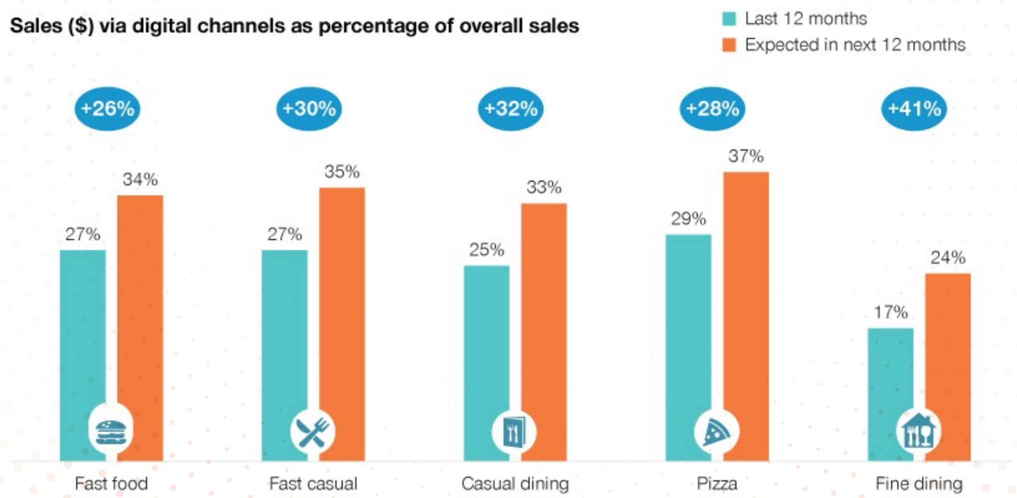


With rising costs and recessionary expectations, digital and loyalty initiatives are increasingly important to develop

Most restaurant brands surveyed expect a recession in 2023, and the greatest changes in consumer behavior are expected to be 1. consumers looking for more promotions, 2. a decrease in the number of unique guests, and 3. consumers shifting to better value items/brands. So, what can address all three of these changes that consumers are likely to make? The answer is restaurants' digital capabilities and their loyalty programs.

1. **Promotions:** 55% of brands stated that their loyalty programs are used to offer members more attractive promotions compared to the promotions offered elsewhere, and 49% stated they offer more attractive promotions in their digital app compared to other channels. Use your digital channel and loyalty program to provide exclusive promotions to guests who engage with your brand.
2. **Guest churn:** Utilize your digital and loyalty initiatives to create additional touchpoints with guests and provide rewards that reduce churn and increase frequency of purchase.
3. **Trading down to better value items:** Advertise value products in your digital channel or loyalty program to prevent consumers from trading down to lower-priced competitors.

An increased focus on digital initiatives is not only important for combatting expected behavior changes caused by low economic confidence, but digital is also expected to be the largest growing channel throughout 2023 in terms of revenue mix.



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Brands expect a higher increase in sales from delivery, curbside, and pick-up compared to in-store purchases, which enforces the need to optimize digital initiatives. COVID accelerated the trend of consumers ordering delivery or placing mobile orders, but the convenience of digital ordering is here to stay.

Overall, restaurants face several challenges with increasing costs and an overall muted economic outlook. However, there are numerous ways to combat this, including next level differentiation for price increases, enhancing digital and loyalty initiatives as these channels increase in revenue mix, and utilizing digital and loyalty to offer promotions and rewards to reduce churn.

Is There a PERFECT Pricing Model?

by: Manuel Wätjen

The question of the right pricing model is a topic of heated and controversial debate in the pricing community. There is no simple answer to this question - but here is what you can look out for. Manuel Wätjen is a member of the executive board at Vocatus with a focus on applying behavioral economics to pricing strategy and sales optimization in B2B and B2C. He studied social sciences at the Ludwig Maximilian University in Munich and the University of Queensland in Brisbane, and worked as a brand strategy consultant before joining Vocatus in 2010. He can be reached at Manuel.Waetjen@vocatus.de.

A few years ago, **the subscription model was considered the best pricing model**. Compared to the classic purchase, where the customer acquires all the rights and obligations associated with the offer in a one-time transaction, the customer subscribes to pay a **regular fee to use the offer**.

The business models of the **world's largest companies by market capitalization (e.g., Apple, Microsoft, Amazon)** are partly based on subscription models, and for a good reason.

This **ensures recurring revenues** for companies and **flexible access to services** for customers without large one-time investments or expenses. **Startups also tend to be more interesting for investors** if their business model is based on subscriptions. Yet, alternative models can be effective as well.

Performance-based pricing models have been **increasingly discussed** recently. This is where the customer does not pay for the opportunity (subscription) or the activity (pay per use) but for the **result of the use**. For example, worth mentioning in the B2B area is Google Advertising (price per lead). The **advantage** for the customer is that the **goals of the provider and those of the customer coincide** (namely, to provide a high benefit), which is therefore perceived as particularly fair. The **advantage** for the provider is that **customer-specific price acceptance can be better exploited** because the **pricing model can scale better**.

THE BUSINESS MODELS OF THE WORLD'S LARGEST COMPANIES BY MARKET CAPITALIZATION (E.G., APPLE, MICROSOFT, AMAZON) ARE PARTLY BASED ON SUBSCRIPTION MODELS, AND FOR A GOOD REASON.

From the perspective of classic value-based pricing, a pricing model is superior for the customer if it costs the customer as little as possible for as much benefit as possible. In this sense, performance-based pricing would be the "best" pricing model for the customer. But is this actually true?

What is the "right" pricing model?

The answer to this depends on the respective decision-making situation and the **(price) motivation** of the customer.

#1 The Classic Purchase

This pricing model applies to products that have a symbolic value that goes beyond their practical use and is linked to the possession of the product. The value of prestigious products such as cars, jewelry, and clothes, for example, results from the possession or the possibility expressed by the possession to afford the product. Other pricing models are possible but only allow the practical use, i.e., a small part of the total value, to be monetized.

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#2 The Subscription

This pricing model applies to products where customers do not know their exact needs in advance and at the same time have a high level of confidence that the provider will meet their needs. Subscriptions relieve customers because they do not have to weigh whether it is worth spending money on each use. Once the decision has been made, e.g., for a newspaper subscription or a streaming subscription, the provider is continuously obliged to establish usage routines so that the subscription is worthwhile from the user's point of view.

#3 Pay Per Use

This pricing model applies to products where ownership has no symbolic value or would require high investment. They are used on such an irregular basis that customers with a subscription would feel that they are paying for something they do not need. For example, if someone only plays squash once in a while, they would rather rent a court for a certain time. This feels fairer than opting for a membership, although the latter could save money in the long run.

#4 Pay Per Performance

This pricing model applies to the same products that fall under the pay per use category. It even seems a bit fairer because it aligns the interests of the customer and the provider. However, the benefit must be clearly identifiable. Otherwise, there will be conflicts of interest in the billing process. Instead of charging by the minute (pay per use), a car-sharing provider can also charge by kilometer (pay per performance). From the customer's point of view, this is even fairer because the customer does not have to pay for further use without the benefit (e.g., when stuck in a traffic jam).

THIS PRICING MODEL APPLIES TO THE SAME PRODUCTS THAT FALL UNDER THE PAY PER USE CATEGORY. IT EVEN SEEMS A BIT FAIRER BECAUSE IT ALIGNS THE INTERESTS OF THE CUSTOMER AND THE PROVIDER.

The (Price) Motivation is Decisive

As you can see, there is **no one best pricing model**. Which pricing model is suitable depends on:

- the type of benefit the product provides for your customers (e.g., practical, symbolic),
- the degree to which customers are willing to be involved in the purchase decision,
- the question of whether customers know and can articulate their needs,
- the (price) motivations of customers (e.g. predictability, fairness),
- and the question of which price elements the customers pay attention to in their usage decision.

This can often also result in a **hybrid pricing model**.

According to the **GRIPS typology**, the decision strategy of customer types condenses some of these aspects. It thus gives indications of the adequate price model. Price accepters are typically more susceptible to symbolic value propositions, so the purchase model is more suitable. Risk avoiders want to be treated fairly and not pay for services they do not use, so they tend to feel more comfortable with pay per performance. Routine buyers have a lot of trust in the provider and little desire to make decisions, so a subscription model is an obvious choice.

We observe time and again that **young companies** (understandably) focus intensively on their product and **do not consider the issue of the pricing model until very late in the process**. However, since the pricing model is decisive for the business model's success, we recommend **addressing the decision** for the appropriate pricing model **very early and intensively**.

What is Price Sensitivity and Why Should EVERY E-Commerce Business Measure it?

by: Krzysztof (Kris) Szyszkiewicz

Every e-commerce manager strives (or rather should strive) to boost conversion rates while still keeping margins intact. But let's face it, it's a tricky one. More often than not, you gain one while losing the other. But it doesn't have to be this way. With the awareness of your products' price sensitivity, you can increase conversions without sacrificing your margins, as the author explains. Krzysztof (Kris) Szyszkiewicz is Partner and Head of Delivery at Valueships. He is a certified expert in price, revenue, and margin management in B2B companies and e-commerce. He can be reached at contact@valueships.com.

I had this burning desire to upgrade my entertainment game some time ago and decided to buy a new TV. So, with my detective skills, I Googled a dozen stores in my city that had my dream TV in stock. After a 30-minute price comparison, I picked the one with the cheapest tag and hit the road.

On my way there, I realized I also needed an HDMI cable, an extension cord, and some batteries for my alarm clock, which had been showing 9:30 for two weeks straight.

Shopping summary? I bought the TV below the market price, about 3 to 5% cheaper than the average. And the cable, extension cord, and batteries. How much did I actually pay for them? How much do they even cost? I probably spent twice as much as their average price.

Moral of the story? Price sensitivity is lowkey king in e-commerce and retail. Let's explore it.

What is price sensitivity?

Price sensitivity is like a mood ring for the wallet – it tells you how much you care about the price of a product. Think of it this way: if the price of your favorite soy milk went up by 10%, would you still buy it? Or would you start hunting for cheaper options, like it's a treasure hunt, and switch to a more affordable alternative or buy it somewhere else?

Now, the price sensitivity level depends on many factors, like how often you buy the product, how many alternatives are available, or how easy they are to find and compare. Interestingly, depending on the **purchasing context**, the same product can have high or low price sensitivity.

Take my TV shopping spree for instance. I was super sensitive to the price of the TV itself and spent some time searching for the best deal. But when it came to buying the cable and battery, I was like, "Just give me what you have."

However, if the HDMI cable had been my primary purchase, I would have spent some time looking for a decent deal. The same product would become more price sensitive for me in a different context.

On a side note: **price sensitivity is a metric used in retail and B2C e-commerce** because you need a big pool of data on similar or identical products to make accurate comparisons. The equivalent of price sensitivity in B2B is WTP (Willingness to Pay).

Why should EVERY e-commerce business measure price sensitivity?

Every e-commerce manager strives (or rather should strive) to boost conversion rates while

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still keeping margins intact. But let's face it, it's a tricky one. More often than not, you gain one while losing the other.

For instance, if you want to boost your conversion rates, you might spend big bucks on UX optimization or paid ads. As a result, you do get more conversions, but because all that spending increased your customer acquisition costs (CAC), you ended up torpedoing your margins.

But it doesn't have to be this way. With the awareness of your products' price sensitivity, **you can increase conversions without sacrificing your margins**. That's right, you can have your cake and eat it too!

Competitively priced products will make fewer people rebound from your store because of the price (just like the price of the TV has attracted me to this particular store). **At the same time, your overall revenue will increase because you will earn extra on low-sensitivity products, like the HDMI cable, extension cord, and batteries**.

What if e-commerce doesn't measure price sensitivity?

Now picture this: a laptop supplier decides to jack up the price of a specific model. The e-commerce manager, trying to maintain profitability, increases the selling price. But then, the marketer slashes the price to maintain conversion rates of the promo campaign.

It's a never-ending game of peek-a-boo that kills margins and results in unprofitable (or barely profitable) promotions and wasted business potential.

The solution? Understanding the price sensitivity of your key products. Without it, you're left with:

- lower margin on low price-sensitive products,
- wasted marketing costs on high-price-sensitive products, and
- missed opportunities for cross-selling.

Plus, you won't be able to **keep up with the competition's price movements**. Ultimately, you want to be the cheapest for high-price-sensitive products, cost-optimal for medium sensitivity, and expensive for low-sensitivity items (I'm looking at you, soy sauce).

3 types of price sensitivity

Now let's look at the 3 price sensitivity groups that products fall into. Remember, however, that as in the example from the beginning, the same product can be high, medium, or low price sensitive. It all depends on the purchasing context.

Here's another real-life example: **OTC drugs, like vitamin C or dietary supplements, are usually price-sensitive. But when you have a toothache, your price sensitivity for painkillers drops faster than a hot potato – you'll grab whatever gets the job done, no matter the cost.**

But let's focus on some classic examples to grasp the principle of price sensitivity.

High-price-sensitive products

This group includes items with **highly transparent and easily comparable prices**. Groceries, clothing, and household goods are great examples.

These are typically items that must be purchased regularly, so shoppers tend to be more aware of price changes in these categories. **They may opt for generic or store-brand versions of these items if they feel they can get the same benefits at a lower cost.**

Despite their relatively high price, travel services are good examples

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too because, again, they're easily comparable. Shoppers often compare flights, hotels, rental cars, and other travel services to find the best deals.

Selling high-price-sensitive items usually makes up around 15% of a store's revenue. If the store keeps the prices low, customers will think they're getting a sweet deal, making them more likely to return for more and spend more.

(This mechanism is so simple that it's beautiful).

Mid-level sensitivity products

These are items that shoppers occasionally compare prices for, but **the price point is typically not the primary consideration** when buying them.

Examples of mid-level sensitivity products would be furniture and appliances, as they are usually large enough purchases that customers may take their time when comparing prices, but they may also be willing to pay a slightly higher price if certain features or quality requirements are met.

Mid-level price sensitivity can also apply to everyday items like bio food. Many shoppers may be willing to pay extra for organic products even though cheaper alternatives are available. Still, if the price of bio tomatoes doubles, many will go for the more affordable, regular stuff.

Low-price sensitivity products

We tend to be less or not concerned about those items' prices. Typical examples are luxury goods, collectibles, and art. These kinds of products have high markups due to their perceived value and the simple fact that they're not to be found in the same abundance as everyday items (making them harder to compare prices on or find discounts for).

3 examples of low-price sensitivity products:

- luxury goods
- collectibles
- art

Valueships

On the flip side, these products allow e-commerce stores to recoup the margins they cut (but not too much!) on highly price-sensitive products. Think again how simple and beautiful this mechanism is: you attract customers and visitors with one product on which you earn a little less. **Then, you reflect the profit on other complementary (or independent) products.**

Two birds with one stone!

How to analyze price sensitivity in an e-commerce business that is not large international player?

Big e-commerce players, whose traffic is counted in hundreds of thousands of customers, have it easier. They can crunch numbers with high-tech tools to understand supply and demand and monitor their competitors' moves.

But for the smaller guys, analyzing external and internal data is the secret sauce to determine their price sensitivity and keep their customers clicking and buying.

Example questions:

- What gets people to your website?
- How do people see your store on Google?
- What items have the best and the worst reviews, and why?
- What do shoppers usually put in their shopping carts?
- How much does it cost to lure them to your store?
- Which of your competitors' products overlap with yours or have fluctuating prices?

The answers to these and other questions (depending on the type and scale of the store) will show the trends in the price sensitivity of products. You will arrange your assortment linearly, from the least to the most price-sensitive.

With that knowledge, you'll **profitably** attract people to your store who come for the best deal on one product but leave with a basket full of other things that will earn you the most percentage.