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decision behavior experts

Net Revenue Management Beyond the 2020 Corona Crash

Consumer behavior implications and recommendations for pricing strategies

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Executive summary

During the 2020 Corona Crash, consumer decisions and consumer buying behavior are atypical. The situation is unique, and people react differently. The context in which people decide is unique, but this period will pass. In the post-crisis recovery phase, reality will have changed: people may have switched to online shopping and they may have been forced to use other brands. For a group of people, spending power will have been reduced and several businesses they buy from may not even exist anymore.

However, analyses of the effects of previous crises on consumer behavior (SARS, 9/11, 2008 banking crisis, etc.) show that while some trends are accelerated, after the recovery period, we see many trends reverting back to the pre-crisis times. Consequently, some buying behavior and the decisions people make will differ from before. However, the question is how and to what degree buying behavior will change. What does it mean for your business goals and in particular:

"What does it mean for Net Revenue Management (NRM)?"
We see from history that companies that maintain prices during a recession are better placed to recover to pre-recession revenues and margins afterwards. Companies that automatically slash prices, and those that stop investing in their brand, will be in a worse position post-COVID. The big challenge will be to balance out short-term revenue potential and long-term potential.

Is your company ready to reassess its strategy, so you are better positioned to thrive following the COVID-19 crisis and in the recovery phase?

This paper explores the behavioral impact of disrupted decision behavior on Net Revenue Management strategies and consequences for consumer brands. We share six proven recommendations for brands who want to emerge stronger after the Corona crash.

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Net Revenue Management (NRM) and impact of behavioral shifts

To manage revenue, companies use their product offering with four main business levers: brand, product, price and promotion. The sensitivity of consumers to these levers (and their willingness to pay) is context specific. Online consumers behave differently than those in brick and mortar stores, for example in terms of price sensitivity and pack size preferences.

When consumers experience a change in conditions, e.g. when spending power is reduced, they will behave differently. To maximize short- and/or long-term revenue, the business levers need to be fine-tuned based on the context. When done successfully, you can better influence consumer decision behavior and maximize revenue potential.

At SKIM we consider the four business levers plus four different, but intertwined dimensions of context: channel, competitors, consumers and conditions (e.g. trade terms). Our framework offers a better way to understand and address revenue management questions. The resulting insights allow companies to make more holistic and accurate pricing decisions.

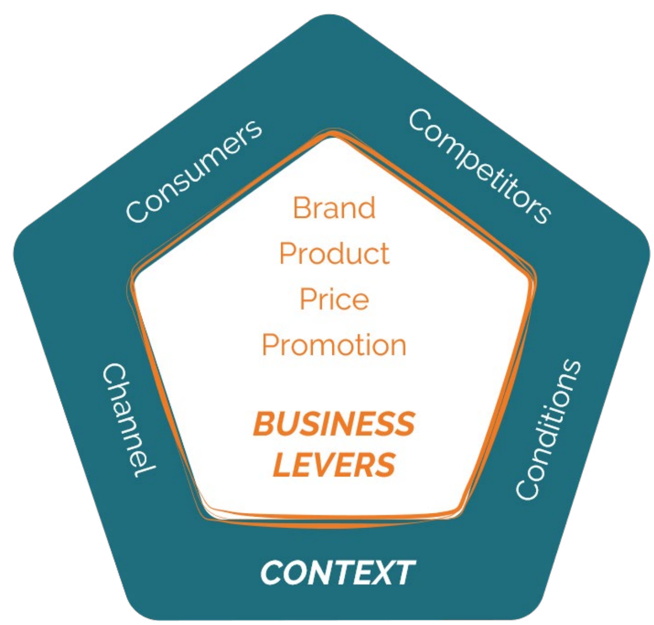
Net Revenue is defined as revenue minus all costs and rebates to realize revenue. So, rather than simply seeing the total revenue flow (which may come at a very high cost to generate), it focuses on whether the company is able to build greater value. Costs to consider can be marketing and sales-related, but also related to other business functions like production, packaging and logistics. Consequently, in NRM many different stakeholders are involved; NRM is often a multifunctional discipline in which accounting and marketing or client-facing functions such as business development and channel management dominate.

The most successful consumer goods NRM strategies are data-driven ones. To effectively manage net revenue, companies need to leverage a wider set of data sources and information: sales data, brand tracking data, marketing mix models, expert views, and primary research (such as consumer insights on price elasticity via conjoint pricing studies). Each of these information sources are good to deal with specific challenges – setting promotions, optimizing product assortment, etc. In addition, some data is at an aggregate level (macro), while other data is at a more detailed level (meso or even micro). Some data is generated by the business process (so ex-post data) and other data is experimental primary research data modeled to predict the outcomes (ex-ante data).

Bottom line: these various data sets are all relevant to managing net revenue – all should be considered and combined.

However, to ensure the most accurate predictions, it is essential that analytical rigor be applied when combining different data sources. The research techniques chosen can affect the results and impact the overall success of your NRM strategy.

SKIM Net Revenue Management (NRM) Framework



Adapting to the new situation

To answer the question "*What does the 2020 Corona Crash mean for Net Revenue Management?*", we must consider how revenue is generated. At SKIM, we see revenue as the sum of all consumers' buying decisions. So, revenue is generated by consumers, who follow various decision processes and who react differently to companies' product offerings depending on the context or situation they are in.

The Corona Crisis and the Corona Crash are shaking the context for consumer decision behavior and the context for Net Revenue Management is also disturbed. This means NRM must adapt to the new situation while consumers adapt to the new normal. Anticipating and influencing consumer decisions in a changing environment is the way for companies to be successful during and after the Corona Crash.

Although globally the pandemic is not over, based on previous crises and based on observation and information, we can already start to sketch the new situation, so the consequences for NRM can be partially mapped out.

To assess the impact of different dimensions shaping the new situation for NRM, we will first look at the impact per dimension of change:

1. **Economic change**
2. **Behavioral change**
3. **Psychological change**

Next, we will view them in conjunction and identify the consequences and opportunities for NRM strategies.

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1. Changing economics

The economic impact of the COVID-19 Crash is very serious and despite the huge amounts of money reserved by governments to manage the situation, in most countries and globally a recession is inevitable. The impact will differ by country, by industry and by consumer group. For Net Revenue Management it means that the economics behind all four dimensions defining the context are disturbed. Although these dimensions cover more than just economic change, we will limit ourselves to discussing some of the biggest disruptions in this paper.

(Internal & External) Conditions

First and foremost, the conditions internally and externally are changing dramatically – and will continue to do so.

The external conditions: macro-economics, governmental support packages, supply chain disruption etc. create a new condition to operate in. This includes the obvious examples where businesses may not be allowed to operate temporarily in certain situations. In addition, external changes (e.g. changes to raw resource production or competition for resources) can lead to limited availability or price increases for certain resources. Because of all of these changes, previously profitable products may not be profitable anymore or may not even be feasible to produce.

From an internal company point of view, the external disruption results in adjustment of goals and objectives. Therefore, the relationship between functions may change and your NRM goals and objectives will change. For instance, when your company's cash flow is seriously impacted, this would lead to very different priorities in product marketing strategies. Especially for publicly listed companies, there will be huge pressure from shareholders to show how sales and value can be maintained. Rather than focusing on high-value, high-margin business, priorities may shift to simply getting sufficient cash flow to stay afloat.

When reassessing NRM strategies, it's important to plan for these shifting priorities, without harming long-term brand positioning and pricing potential where it can be avoided.

Consumers

Consumers are expected to be impacted heavily by a recession, as unemployment goes up and spending power goes down. From an economic perspective, declining consumer spending is relevant and directly impacts revenue for companies. For NRM it is critical to realize that the decline is specific to discretionary categories, and because not all consumers are equally affected, the decline differs per consumer group. As a result, reducing price everywhere to boost revenue can be seriously counterproductive: it may not move the right people or it could reduce revenue from consumers who would have bought your product regardless of the price drop.

Perhaps even more important than economic changes, consumers have been forced to change behavior. During and after the crash, consumer psychology changes and we will explore this further in the following sections.

Channels

Channels are the third dimension of economic changes and as with consumers, not all channels are equally affected. Some channels, like online, are benefitting as consumers are massively changing their habits. In some cases, consumers are simply buying more online and in other cases, they are being forced to try eCommerce for the first time. Other channels, like on-the-go outlets, are seriously hurt and fighting to survive. These channel shifts create a different dynamic for companies, making it even more important to optimize the business levers specific to each channel. Brands, products, prices, and promotions all need to be tailored to each channel.

It's worth noting that these sales channels are themselves going through major changes, so there may be opportunities or threats that impact your revenue management strategy: what types of products will retailers push to consumers; *are they aiming to generate traffic or to increase their value and margins?* In general, after a crash, channels tend to compete on price and promotions and try to put the burden on the producers or the brands – resulting in less net revenue for the brand. Channel managers should push back and aim for solutions which are beneficial for both the channel and the brand. Having an up-to-date understanding of consumer preferences based on research insights can be hugely beneficial in these negotiations.

Competition

The rules of engagement are going to change as each competitor's priorities shift in the post COVID-19 situation. Some brands are dialing up marketing and advertising efforts during the crisis, while others are reducing spend in these areas. You may need to prepare for a price-based battle for volume with your competitors. Facing upcoming difficulties, some competitors may not survive the crisis, which could leave major opportunities. Alternatively, it may just result in different challenges as competitors merge or acquire other brands themselves. In short, you will need an agile approach to thrive in the recovery period. You need to be ready for anything when it comes to the competitive landscape and have a host of different potential competitive scenarios in mind when planning for the future.

This dimension of economic change also requires NRM to be revised. In the past, a crash for discrete categories could trigger a price war resulting in a revenue reduction and in irreversible loss of equity for the whole category. In such a scenario, everybody loses, which is why it will be crucial to think before acting.

> ***"Reducing price everywhere to boost revenue can be seriously counterproductive.***

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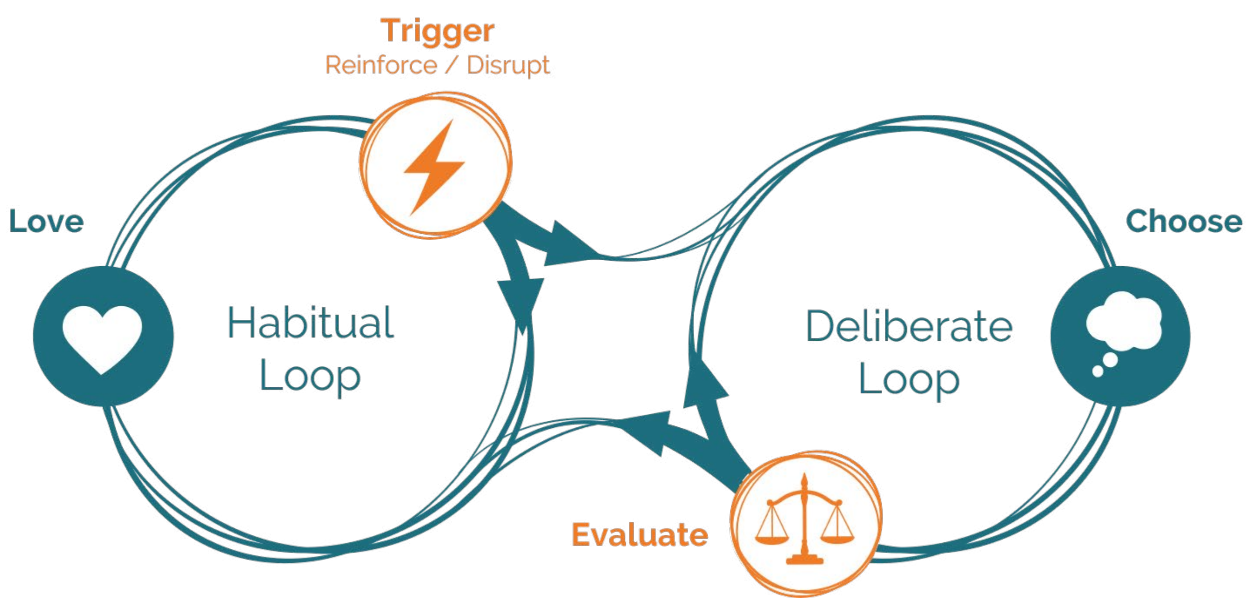
2. Changes in consumer behavior

As observed, and as published by many others, the changes in consumer behavior are unprecedented. This is resulting in new consumer behaviors, some of which are temporary and some of which will stay. Underlying these changes are changing attitudes and beliefs, changing rules and regulations, and most of all, experiences with "new" technically or digitally enabled solutions. Online meeting, online teaching, online shopping, and online medical consulting were all technically possible pre-crisis. However, the sudden and vast shift will result in a "new normal." People are making different decisions and consumers are deciding in different ways. Discrete products and services will be bought less and others more. Over time the "new normal" will settle in. The decisions may have changed, but the framework reflecting the decision-making process will not. In the "new normal" recently adopted buying decisions may become routine, hence following a habitual loop, or will be more deliberate and follow a deliberate loop. Consumer decision behavior is captured in SKIM's Habitual-Deliberate Decision Loop framework, which helps companies to understand, disrupt, and reinforce consumer decision behavior.

From a Net Revenue Management perspective, it is critical to bind the consumer to you and raise the loyalty barrier to prevent switching. This requires reinforcing the habit (encouraging him/her to stick to the habitual loop) and guiding the consumer through the deliberate loop. To do so, ensure you offer the most relevant benefits, and communicate those, so that when a consumer ends up in the deliberate loop, they will choose your brand and product again, because it best fits their needs. In addition, you must win new consumers, which requires triggering, activating, and guiding them through the deliberate loop.

SKIM Habitual-Deliberate Decision Loop



During this time of crisis specifically, we should be conscious that all consumer decision behavior will be impacted as regular habits are disrupted. This means that each brand will need to work harder to convince the consumer to (continue to) choose their product or brand. It will be key to assess how existing habits are disrupted and in what context consumers are making new conscious trade-offs.

What is most important to consumers in this new situation? How can your brand and product be leveraged to win?

Changing consumer behavior is mainly complicating Net Revenue Management, but the changes offer opportunities for brands as well. As specified before, not all consumer groups are equally affected and not all consumers adapt their buying behavior in the same way, nor to the same degree. This means the variation in consumer behavior and the number of clusters of consumer behavior increase. Old ways of segmenting the market may not be valid anymore, partly due to new behavior, partly due to new economic conditions resulting in a split of the former clusters – as some have to adapt based on their budgets and others can afford to maintain their choices. In either case, it will be more important to understand how to meaningfully segment the market in the new situation.

For NRM, this means it is more challenging to fine-tune the use of the business levers to the different groups – to prioritize and decide it is most relevant to identify which groups are dynamic or changing most, and which groups are less affected. The latter requires maintenance and monitoring, but existing insight can be used to guide NRM decisions. Where it is most dynamic, NRM should be on top of fine-tuning product offers. To capture consumers, consider launching new products to play at specific price points, or otherwise better meet consumer needs (through features that are functionally relevant and products that resonate emotionally). This approach will help you guide consumers towards better experiences, and increase willingness to pay, which will in turn maximize revenue.

In fact, this may be an ideal time to launch new products that fit better within consumers' new needs and priorities. Out of every crisis, winners are born.

Consider the household names that launched as startups after the 2008 recession. Companies like WhatsApp, Uber and Venmo disrupted many traditional categories and triggered new consumer habits. As consumers' habits have again been disrupted by the COVID-19 crisis, more will be actively evaluating alternatives and choosing the product or service that best fits their needs. Once the dust settles, and people have reestablished their routines, it will be more challenging again to disrupt their behavior with new products or services.

3. Changing consumer psychology

Each crisis is unique, but all serious crises have the following in common: people's beliefs, needs, and attitudes change during and after a crisis. Although people differ in the way they respond and progress through the crisis, the one thing they have in common is that they are all going through the same experience. Two broad reactions occur: the immediate reaction is fear, followed directly by or delayed by hope. During the crisis, basic needs are activated and people tend to fall back on traditional values. The need for security, protection, and connection, within a smaller circle though, are clearly present. In the recovering phase there is hope, a new beginning and the need to act responsibly, to care for the community, and to value and protect the environment.

What does this mean for Net Revenue Management?

During and after the crisis, people's priorities, beliefs, needs, and attitudes change, and the perceived value of products and services may change. This reaction may range from "it is valuable, but I will use smaller units" to "I do not need this brand/product now." For example, consumers may opt for conventional vs. organic products. Consumer decisions are heuristic, and over time the logic may change. NRM is rational, and as part of a company using the business levers to realize the revenue goals, you must anticipate and react to heuristic decisions, without imposing economic rationality on consumer decisions.

This does not mean that consumers do not act rationally or in economically driven ways. The changing consumer psychology impacts the perceived value by a group of consumers for discrete products. Therefore, to better manage revenue, companies must better identify which consumers to target, which products/brands to offer, which value drivers are most important, what the new heuristics are and what consumers are willing to pay.

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Consequences and tips for NRM

The consequences of the COVID-19 Crash differ per industry and per category. There is no panacea, but we can learn from the past and from monitoring the situation. Where before COVID-19 you may have had a clear idea of which data sources to use for which purposes, the questions we need to ask ourselves in this time of crisis are likely very different from the questions we were asking before. Still, we should try to use all the data sources available to us to answer our questions and inform NRM strategies. Our goal should still be an approach to pricing that is fact-based and confirms our hypotheses about how markets and situations for our customers are changing – and to adapt accordingly.

1. **Dive deeper into consumer segments to uncover changing dynamics**
   It's important to understand that NRM is often based on averages and totals, which don't reflect the significant increases in consumer diversity. Not all consumers will be affected in the same way by the crash. For example, cutting prices to reflect reduced spending power is to be avoided, if that reduces revenue from shoppers who would have bought anyway. It's crucial to recognize the changing dynamics that affect your consumer segments, so you know if your intended strategy will be effective for specific target groups.

2. **Use your portfolio to manage revenue**
   It's important to recognize that in the recession there will be a significant decrease in market demand and spending power. Rather than only changing prices, you should adapt your offer to match the needs of consumers who are spending more prudently. One option is to create affordable, alternative SKUs or brands, but this must be done with attention to NRM, value, cost, and price constraints.

   On the other hand, there are those who will be able to afford their usual brands/products. Here, your goal will be to strengthen their habits, and manage revenue by adding value to justify price or even command a higher premium based on their needs.

3. **Evolve your research approach for more agility**
   While much is changing, old standards may not apply. You need agile research methods to come up with more accurate answers. Targeted primary research will help you track changes in consumer perception about your brand, product, pricing, and promotions. It is also worth considering that the insights you gained three months ago (or more) could well be out-of-date, so there is great value in repeating your research exercises to reflect the new context. In April 2020, we conducted a pricing re-run of 8 large CPG pricing studies to determine if/how price elasticities changed pre and during COVID-19.

Download the "Impact of COVID-19 on consumer price sensitivity in the U.S and Europe"

While a data-driven approach is key to successful pricing and revenue management strategies, a wide set of data sources is essential. Sales data, brand trackers, marketing mix models, expert views, and consumer insights on price elasticity (e.g. pricing research like conjoint studies) can all give you a piece of the puzzle. However, to ensure the most accurate predictions, analytical rigor must be applied when combining different data sources.

The bottom line is that the research techniques chosen can affect the results and can impact the overall success of your NRM strategy.

4. **Accept that there are areas where you won't be able to get full visibility**
   Rather than trying to get a complete understanding of your entire category and consumer groups, focus on having enough information and evolve your plans over time. First, get enough information – new or existing – to inform your strategies, then regularly reassess the assumptions you have had to make. Work out which data sources you need to fill in gaps – again, this could become clearer over time – to help you predict coming trends.

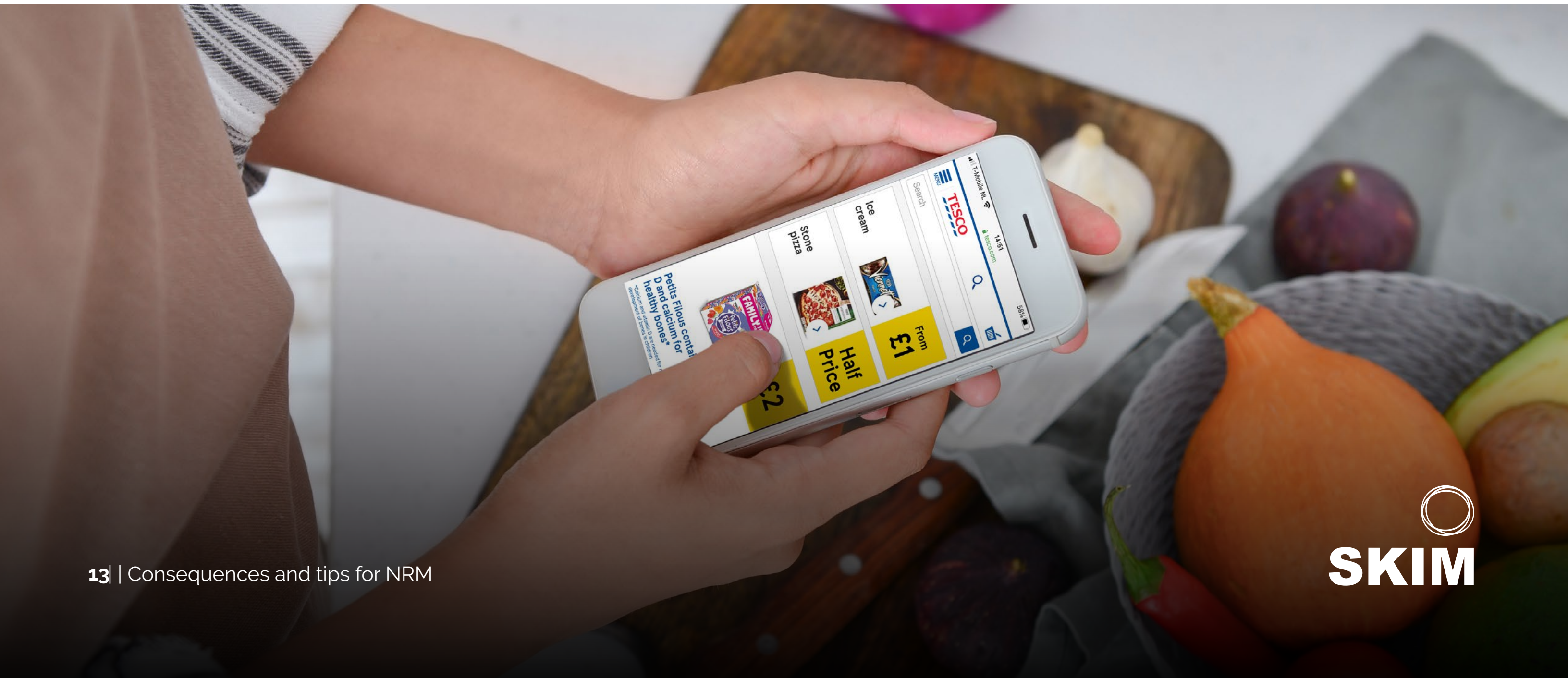
5. **Focus on the future to reinforce positive habits and disrupt unfavorable ones**
   Consumer behavior and consumer psychology is changing. It's important not to extrapolate too much from the past as this may not be reliable. Instead, carefully consider which parts of consumer behavior are changing and which ones will quickly go back to pre-COVID behavior. The focus should be on understanding what "the new normal" will look like. Use the changing dynamics to strengthen your position for the future.

   Lead in the new normal with products and services that are more relevant and that resonate differently in the new context. Your goal is to manage positive new habits (e.g. buying online), disrupt those that are not favorable (e.g. ditching private label brands) and encourage repeat buying in the new context (e.g. choosing healthier options).

6. **Don't damage long-term revenue potential with frequent price reductions**
   Net price is a key component of revenue generation. While rebates and price promotions can be used to boost sales, in an unstable market, promotions may be less effective. Use pricing strategies wisely: frequent reductions and buying market share can damage long-term value, price perception and revenue potential.

   Price is a very important influencer for consumers, so use it. But, even in a recession, it's better to compete on value or the value price ratio. Use pricing consciously to influence the decision and realize net revenue goals!

> ***The insights you gained three months ago (or more) could well be out-of-date, so there is great value in repeating your research exercises to reflect the new context.***



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Conclusion

Due to economic changes, changes in consumer buying behavior and psychological changes, people will be making different trade-offs after the 2020 Corona Crash. Companies need to be ready to play into changing consumer behavior to survive the disruption or even thrive in its wake.

Having a clear understanding of how the needs and preferences for different segments will change over time – and adapting your product offering accordingly – will be crucial. To do so, leveraging the data you have and using agile research methods to help fill knowledge gaps quickly and inform strategies for this context will be key.

For four decades we've partnered with leading brands to help answer their tactical and strategic pricing, assortment and promotions questions. Contact us to learn how applying SKIM's robust analytical approach can help improve your revenue management strategies in the post-Corona recovery phase.

About SKIM

SKIM is a global insights agency helping leading companies thrive by understanding decision-making. To stay ahead in today's environment, it's critical to know how decisions are made and how the changing environment influences decisions for consumers, healthcare and B2B professionals. To understand how decision-making has changed (and how it hasn't!), we adapt sophisticated research techniques and develop new innovations to address this new reality. *The result?*

Practical brand communications, revenue management, product innovation, e-Commerce, and advanced analytics recommendations you can use to propel your business forward, both online and offline. What sets SKIM apart is our decision behavior expertise + deep analytical and choice-modeling roots + a thorough understanding of the marketing challenges brands face. This unique combination, along with our creative thinking, is the reason why strategy consultants and leading companies, from Fortune 500 to digital disruptors, have continued to partner with us for decades.

With 9 offices around the world and 170+ enthusiastic SKIMmers ready to help crack your business case, how can we team up with you today?

skimgroup.com/covid

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