

## “One-deal-fits-all?” On Category Sales Promotion Effectiveness in Smaller versus Larger Supermarkets

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### Abstract

Even within a store chain and format, supermarket outlets often exhibit substantial differences in selling surface. For chain managers, this raises the issue of correctly anticipating the promotion lift, and of profitably managing promotion activities, across these outlets. In this paper, we conceptualize why and how store size influences the category sales effectiveness of four promotional indicators (depth of the promotional discount, display support, feature support, and whether the promotion is quantity-based). We then estimate the net moderating effect on four product categories for 103 store outlets belonging to four chains. For each of the promotion instruments, we find the *percentage* sales increases to be lower in large stores. For instance, whereas a 10% point increase in feature activity enhances category sales by about 1.64% in a 700 m<sup>2</sup> store, this figure drops to only 1.03% in a 1300 m<sup>2</sup> store – a 59% reduction. This moderating effect is especially pronounced for discount depth, the relative sales lift from a typical price cut being about 78% lower in the larger-sized outlet. However, since large outlets also have larger base sales, the picture changes when we consider *absolute* sales effects. The net outcome is that deeper discounts or quantity-based promotions do not systematically generate larger or smaller absolute sales bumps in large stores, whereas for in-store displays and features, we obtain a clear positive (be it less than proportional) link between store size and absolute category sales lift. When it comes to margin implications, we show that large stores gain higher profit from price cuts than small outlets only as long as the retailer *keeps* part of the manufacturer discount to himself. Managers can use these insights to improve their promotional forecasts across outlets, as well as to tailor their mix of instruments to store selling surface.

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Recent changes in the retail food business have led to intensified retail competition (Morganosky and Cude 2000), and have motivated grocery retailers to continuously increase the number of store outlets within their (umbrella) chain (see e.g. Dawson 2006). Even within a given store format, these outlets often exhibit substantial differences in selling surface. For instance, within the Albert Heijn supermarket format, store sizes easily range from a low 200 to a high 2800 square meters – comparable within-format size differences being observed for other chains. Effectively managing these differently sized-outlets, and specifically, the pricing and promotional program for these outlets, has become a paramount concern for retail format managers (Bolton, Shankar, and Montoya, 2009). Given the vast budgets spent on sales promotion activities, the cost of maintaining these

activities, and the lack of profitability of prevailing sales promotion efforts for retailers (Ailawadi et al. 2009; Kim, Srinivasan, and Wilcox, 1999; Srinivasan et al. 2004), effective promotion management continues to be a key point of attention among academics and practitioners. Managing promotions *across stores that widely differ in size* adds to the complexity of this task, and raises several additional issues.

First, headquarters need to accurately *forecast the sales lift* from promotional activities in the different stores, in order to anticipate the product quantities that need to be shipped to these different outlets. It is well-known that logistical efficiencies associated with trade dealing are crucial for retailer profitability (Hoch, Drèze, and Purk, 1994). Overestimating promotional demand in a store will lead to high storage costs or to perished items, whereas promotional stock-outs may be costly in terms of lost sales (Mantrala et al. 2009) or decreased customer goodwill (Fitzsimons 2000; Olsen and Parker 2008). In a recent interview, the chief promotion manager of a major Dutch retail chain estimated the margin losses from inaccurate store-level predictions at three million Euros annually – a sizable amount. Yet,

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while common sense seems to dictate that the *sales lift* from a promotion *increases with store size*, little is known about the magnitude of the store size effect. For instance: will the relative sales increase due to the promotion, be the same in an outlet that is twice as large? Moreover, based on the scarce available evidence, even the *direction* of the effect remains equivocal (Ailawadi et al. 2006; Boatwright, Dhar, and Rossi, 2004; Montgomery 1997), leaving retailers with little guidance on what to expect.

Second, if promotion effectiveness varies with store size, retailers may need to *adjust their promotional programs* accordingly. Following Bolton et al. (2009), successful retailers are developing customized pricing practices, that are neither chain- nor store-wide, and in which promotion intensity depends on store size and clientele. There is evidence that some retail chains, indeed, tailor their dealing activities to outlet selling surface. In an empirical analysis of retailer pricing decisions, Shankar and Bolton (2004) observe that retailers price promote more intensively in their larger stores. Ellickson and Misra (2008), in contrast, report that large stores within a chain more strongly engage in EDLP (rather than Hi-Lo) pricing. This begs the question: which of these approaches is more advisable, and why is that so? To further complicate matters, the impact of store size on promotion effectiveness may well vary with the type of promotion. For instance, even if the percentage sales lift from a display would be the same in a 1000 m<sup>2</sup> as in a 500 m<sup>2</sup> store, this might not hold for a price cut. Unfortunately, the literature to date offers little insight into such instrument differences or their underlying drivers (Ailawadi et al. 2006) – thereby hampering proper adjustment of promotion programs to the stores' selling surface.

In this paper, we shed more light on the relationship between promotion effectiveness and store size, and – hence – on the potential payoffs from tailoring promotional programs to store size. Given the extensive accumulated knowledge on the drivers of promotion response, what could we gain from such an analysis? We see four reasons why analyzing the impact of store size on promotion effectiveness is fruitful. First, as we argue below, the sheer selling surface of the store, through its effect on fixed in-store shopping costs and search costs, exerts an impact on the promotion's category sales lift not captured by other drivers. Second, apart from its effect on promotional sales lift, store size shapes the profitability of alternative promotion instruments. As we will empirically document below, large stores – because of their larger (base) sales – are less suited for promotion activities with a large per-unit cost component. Third, store size may serve as a valuable proxy for (a multitude of) other factors that are difficult or costly to measure and integrate. Even after local *inhabitant* characteristics are controlled for, differently sized stores will attract different types of *customers*, for different types of shopping *trips* (Fox and Sethuraman 2006). While trip-specific shopping goals and customer profiles (including their distance to the store) have been documented to influence promotion response (Gauri, Sudhir, and Talukdar, 2008; Lee and Ariely 2006; Seetharaman, Ainslie, and Chintagunta, 1999), such data may be unavailable to retailers (for instance shoppers' time constraints or shopping goal abstractness, Lee and Ariely,

2006) or difficult to integrate with their promotion databases.<sup>2</sup> Store size, in contrast, is immediately accessible, and may then proxy for these trip- or customer-related drivers. Finally, tailoring the promotional program to store size is appealing from an implementation viewpoint. Recognizing the vast size discrepancies, retailers have often adjusted their logistic operations to accommodate supermarket outlets of different selling surface. An example is Albert Heijn's store replenishment system called Cels, which distinguishes five different logistical procedures tailored to different supermarket size classes (Beerens 2002; Verhoef et al. 2009). Promotion programs that exploit differences in promotion response among these size classes would, then, be easily integrated into the logistical systems already in place.

In sum, while reflecting on the 'unique' store size effects (first and second point above) may add to our academic knowledge on promotion effectiveness and shopper response, we believe that an important contribution of our study lies in its managerial usefulness. By documenting the role of store size (either in itself or as a proxy for other drivers), we also hope to offer a practical perspective on how retailers can better anticipate the promotional sales lift across differently sized outlets, or differentiate their promotion programs across these outlets. Hence, our research fruitfully combines a shopper marketing perspective, with the need for improved resource allocation tools – two points on the Marketing Science Institute's 2010–2012 research priority list.

Our analysis proceeds as follows. First, we aim to uncover why the sales lift from promotions may vary with store size, and how this effect differs across promotional instruments. To this end, we develop a conceptual framework that clarifies the store size effect on four promotion variables: discount depth, display, feature, and promotion format (i.e. whether the promotion involves a quantity discount or a straight price cut). From the retailer's perspective, especially the promotion impact on category sales is important (Ailawadi et al. 2009; Nijs et al. 2001; Raju 1992). Hence, we will use the category as our focal level of analysis. Second, we set out to empirically quantify the promotion effect across supermarket stores of 'umbrella branded' grocery retail chains. These outlets share the same 'retail chain image' and format positioning, but widely differ in selling surface – thereby offering the opportunity to separate store size effects from chain or other format characteristics. To further enhance the validity of our findings, we conduct the analysis in four different product categories and four chains, and control for a broad set of store trading area characteristics. Moreover, as recently advocated by Grewal, Levy, and Kumar (2009), we explore the store size implications for complementary promotional store metrics: immediate and net incremental

<sup>2</sup> Contacts with several major retailers reveal that, even though they collect background data from their loyalty card holders, these data are often not integrated with their 'transactional' databases (containing information by receipt), nor with their product-based sales and promotion databases (containing information by SKU). Also, receipt data alone do not provide a good indication of consumers' shopping goals (Bell, Corsten and Knox, 2010) and hence their implied promotion response.

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