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Price competition in FCMG in South Africa: Know the facts before you begin.

Competition for market share growth and market share retention is very high in the South African fast moving consumer goods (FMCG) markets. Small enterprises and big business alike devote much time, human, material and financial resources in attempting to develop sustainable advertising and sales promotion strategies. In several instances, FCMGs often compete on the basis of price, in what is known as price competition.

Basically businesses attempt to price their selected products, product ranges or at the extremes whole range of products with the expectation that the law of supply and demand i.e. low prices equals high demand and vice versa, will apply. A slight extension is that high demand would be a result of clients moving from rival businesses and possibly a small percentage of new consumers taking an interest in the product or product range, or whole outlet because of the newly begotten low pricing.

For FMCGs in metropolitan South Africa the issue of price competitiveness based on the premises of increasing sales volumes makes both economic and marketing sense. However, it must be emphasized that for the price competitiveness pragmatics highlighted above to appear certain company-specific as well as market dynamics must hold. The rest of the article will now focus on these dynamics with specific reference to the South African metropolitan FMCGs enterprises.

Competitor retaliatory strike-backs

Price competitiveness works where the reduction of prices to outcompete rivals is less likely to attract retaliatory action from competitors. If an outlet can sustain consequent strike-backs like rival outlets pricing even further below the set competitive price, it is okay. However, if a main rival's counter lower offer is set below the production or procurement cost then there is problem.

Theoretically, in an market awash with information, the effects of such a move will definitely dislodge the initial attempt of increasing sales volumes through lower pricing as customers will resort to the next lowest price shop for the same product. The good news is customer do not behave like this. Issues like customer convenience, loyalty, information asymmetries, service quality may offset a rivals counter-strike, but only if the price change is considered (from the perspective of the majority of customers with an interest in the product) significant.

Price elasticity of demand

FMCG outlets must consider the price elasticity of demand of a product or product range prior to embarking on a price competitiveness campaign. Price elasticity of demand measures the degree to which the demand of a product goes up as a result of a given unit change in prices. Products with a high price elasticity of demand will see a bigger increase in sales as a result of a smaller downward change in prices. These products are most likely to benefit the company through sales volume increases under price competitive efforts.

In South Africa, market research shows such products to be more on the basic side- the basic commodities if you will. Some products on the other hand will not result in any significant sales volume growth under price competition. Basically all FMCG will bring in higher sales if the price reduction is considered significant by the customers.

Substitution and cannibalistic effects

Due to the wide manufacturing sector endeavouring to meet the wants and needs of divergent customer groups, South African FMCG products are on the high side as far as substitute products are concerned. Simply explained, for every FMCG product in a South African shop, you are sure to find at least 6 other products that can satisfy the same need-not 6 other brands, but 6 other different products that the consumer can consider for the same use and benefit.

Under such a scenario, it is possible that price reduction in one product or a set of products may result in increase in sales volumes in the particular product or product range but a decrease in the sales volumes of the products close substitutes. This is because regular buyers of substitute products may simply shift their focus to the newly price-lowered product and temporarily abandoning their customary products. Thus price competition can result in an internal competition between products in the same store and overall this is creates offsetting relationships by which the sales volumes of one product may increase without causing much positive change to the total outlet sales volumes. Marketers use the word, cannibalism to describe this situation.

Revenue growth

Sales revenue resulting from increased sales volumes as a result of a more competitive price are a standard expectation in most price competition strategies. However, related to the issue of product cannibalisation and price elasticity issues discussed earlier, revenue growth may not always be the result of a price competitive strategy. A successful strategy ensures that total revenue streaming in as a result of the strategy is not below the general current revenue trends.

Total revenue is being used to refer to total outlet revenue and not only product revenue. Because a price- lowered, popular product may attract customer traffic into the outlet and customers may end up buying other products, it can have an indirect revenue increase effect. The direct effect is what the article has been discussing from the start. If the indirect effect of a price competition promotion is high to such an extent that it can offset the revenue decrease caused by the new low price (the direct effect), then the strategy might as well be viewed as a success.

Businesses therefore must look at the profit and revenue effects of price competition from a holistic view. In this view a good strategy is one that has a positive revenue output.

Avoid the misconception of price decreases as a measure of low quality

The South African consumers are comparatively cognisant of price-quality relationships. The average consumer expect low price for low quality products and vice versa but still also expects occasional price quality bargains where high quality products are disposed at below average price ranges. Within the FMCG sector , it is important to effectively communicate that respective price decrease are as a result of sales promotional efforts lest the market takes them as an indication of low quality. This is particularly important with new as well as less known brands. The risk is that the promotional lower prices might create a negative price-quality perception that might take much effort to change. Also the whole price reduction effort may not be very effective under these circumstances.

Expectation of lower prices going ahead

Consumers can expect lower prices to prevail. Under this scenario, there is no much urgency to benefit from an outlet's publicised low price promotion. The effect of low uptake with the expectation of buying the product in the distant future-while it is still cheaper, will flatten the revenue per unit time output and not result in much meaningful sales volume change despite the market being impressed by the low prices. This is probably the reason why most business present low promotional price deals for very short periods usually coinciding with periods when the targeted market is expected to be liquid.

FMCGs therefore need to understand the market buying characteristics in order to benefit more meaningfully from these promotions. Obvious information like payment dates, general customer buying preferences and targeted customer groups is important in tis regard.

Lowered prices and supply conditions

Low prices, as per the law of demand increases sales volumes. This is good for business unless business cannot sustain product supply to support the new demand levels. Inability to meet customer demand after having publicly promoted a product can create a harmful reputation as an unreliable supplier. Furthermore, current and regular customer groups can be crowded-out by temporary low-price seeking customer groups to the detriment of the more beneficial regular customer relations.

Price competition sales promotion must therefore be conducted under supportive supply conditions. Massive oversubscriptions might as well mean that the product prices were lowered below a necessary price range required to support a given volume of sales.

Legality

Finally, any price competition effort in South Africa must not be part of a collusive effort with other businesses as this might attract legal attention. Collusive industrial behaviour is illegal under South African law and businesses, particularly small enterprises in the FMCG need to acquaint themselves with the provisions of the laws of competition.

In conclusion, various factors affect the success of price competition efforts. The degree of the various effects depends on individual FMCG outlets financial, marketing and operational circumstances. Other factors however are external to the FMCG industry at large. There are a lot of success factors to the discussed matter. However, research efforts have indicated the above as the most operational in the South African metropolitan fast moving consumer goods sub-sector. This is why it is imperative for outlets to ensure adequate business, financial and market research prior to embarking on a massive price promotion.