Tesco has announced the biggest shake-up of its pricing strategy in nearly 20 years. Why is this? Well, despite Tesco’s monumental rise to be Britain’s biggest supermarket, competition in the market has seen Tesco experience a fall in its like for like sales in the last 3 months. Its market share has fallen from 30.8% to 30.4% over the same period. It is hoped the change in strategy will reverse this.

A strategy is a plan by which a business intends to achieve its objectives. There are many strategies that businesses can pursue. Ansoff’s matrix classifies four key marketing strategies that businesses can choose from as a way of achieving corporate objectives.

As can be seen from the diagram, the key strategies range from relatively low risk plans, e.g. existing market and existing product (market penetration) to the riskiest strategy of new markets, new products (diversification). Tesco has decided through its “Big Price Drop" to pursue the strategy of market penetration. This means increasing the sales of its current products to existing customers and attracting new customers from its competitors in the market.

As a result, over the last weekend in September 2011, 14,000 Tesco staff across the UK had to change nearly three million price labels on such things as milk, bread and fruit and vegetables.

So, what actually is the “Big Price Drop" and why does Tesco think it will work? Tesco’s previous marketing strategy has relied on promotions (multibuys) and its Clubcard loyalty scheme as a way to lure shoppers. Tesco surveyed 200,000 customers who said they were weary of having to shop around for the best deals, complained that prices changed too often and that “buy one get one/two free” offers, especially on fresh food, just resulted in wastage. The UK Chief Executive of Tesco, Richard Brasher, said the market had become cluttered, shopping trips complicated as cash-strapped consumers shop around for the best deals and that shoppers wanted to see value for money when they paid at the checkout rather than the delayed gratification of extra Clubcard points. As a result he said, “We're giving customers a more straightforward shop – reducing the number of promotions and putting the emphasis on clear and reliable savings that everyone can benefit from.”

The change in Tesco’s strategy is in response to aggressive price competition and soaring living costs. Households are struggling with the biggest squeeze on their incomes since the 1920s with rising petrol prices, energy prices, food prices and muted wage growth. In this climate, all supermarkets have been fighting to
take customers off one another with price matches, price cuts and promotions. Asda, the second biggest UK supermarket, upped the stakes this year by introducing a price guarantee scheme, i.e. that they guarantee to be 10% cheaper than their rivals. With a falling market share, it is no surprise that Tesco has responded and changed its marketing strategy. So, what does the “Big Price drop” actually cover? It involves cutting the prices of 3,000 everyday foodstuffs by up to 30%. For example, carrots will fall by 14p per kilo, a medium sliced loaf will fall from 69p to 55p, Braeburn apples will fall from £1.75 per bag to £1.40, maris piper potatoes will fall from £1.74 a bag to £1.39 and an Italian peperoni pizza will fall from £3.59 to £2.85. It is estimated it will cost Tesco £500 million a year to do this, however, it is thought the scrapping of its double Clubcard points reward offer and reverting to one point for every pound spent will save Tesco £350 million.

The pricing strategy that Tesco is now pursuing will have implications for its rivals. Asda’s promise to guarantee to be 10% cheaper than its competitors and Waitrose, who matches Tesco’s prices on 8,000 of its products, will see their profits squeezed. It will be interesting to see how the other supermarkets respond to the biggest player in the market radically changing its pricing strategy. Watch this space!