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**Market Segmentation**

Marketing is about matching what people want with what companies offer. This helps both customers and companies. Planning for marketing is like making a plan for a trip. It has two parts: ***a big plan and a detailed plan.***

***The big plan says*** where the company wants to go. The detailed plan says how to get there. It's like deciding which mountain to climb and what to bring for the hike. The big plan is more important, and the detailed plan depends on it.

To make a good big plan, companies think about what they're good at, what could stop them, and what people want. They also use research to learn about what people want. After that, they decide who to sell to and how to make their brand look good. Only then do they work on the detailed plan. This plan covers things like making products, deciding the price, where to sell, and how to talk about the product.

The big plan is like picking the right mountain, and the detailed plan is like getting the right gear for the hike. Both are important, but the big plan is more important. If the big plan is bad, the detailed plan can't save it. If both plans are good, the company does well. If the big plan is good and the detailed plan is bad, things might be okay.

But if the big plan is bad and the detailed plan is good, it's like running up the wrong mountain. The best is to have a good big plan and a good detailed plan.

# **What is Market Segmentation**

Market segmentation is a way for companies to decide who they want to sell their products to. They divide the big group of customers into smaller groups that are similar to each other. This helps the company create products and marketing that these groups will like. It's like cutting a cake into slices, where each slice represents a different group of customers. This is important because if a company tries to sell the same thing to everyone, they might not make customers happy. Instead, they can focus on one group and make something that group really wants.

For example, imagine a company that sells mobile phones. They can't make just one type of phone for everyone because people have different preferences. Some want a phone with lots of features and are willing to pay a high price, while others want a simple and cheap phone. By dividing customers into groups like this, the company can make phones that match each group's desires. This is called market segmentation.

There are different strategies a company can use. One is to focus on just one group, which can work well if the company doesn't have a lot of resources. Another is to make different products for different groups, which is good when customers can tell the difference between products. And there's also the option to not focus on any specific group and sell the same thing to everyone. This is often done with products like basic food items. The choice depends on the company's resources and the customers they want to reach.

**Here 10 Steps of Market Segmentation Analysis**

## **Step 1: Deciding (not) to Segment**

### **Implications of Committing to Market Segmentation**

Even though market segmentation is an important strategy used by many companies, it's not always the best choice for every situation. Before a company decides to use market segmentation, they need to understand what it means for their business.

The most important thing to know is that once a company starts using market segmentation, they should stick with it for a long time. It's not a short-term thing. They have to be ready to make big changes and investments.

Doing market research, creating different products, changing prices, and finding new ways to communicate with customers all take time and money.

So, it's important to think about whether the expected increase in sales will be worth the effort and cost of using segmentation.

Using market segmentation might require the company to change their products, prices, and how they sell things. This can even affect how the company is structured inside.

For example, if they want to focus on different groups of customers, they might need to create teams that look after each group's needs.

Because deciding to use market segmentation has such big effects, the decision should be made by top executives in the company. And once the decision is made, it should be communicated clearly to everyone in the company, so everyone knows what's happening and why.

This way, the whole company can work together towards the same goal.

### **Implementation Barriers**

Several books on market segmentation focus on how to successfully use this strategy in businesses. These books mention challenges that can make implementing a market segmentation strategy difficult.

One group of challenges involves senior management. If top leaders don't actively support and get involved in the market segmentation process, it's hard for the strategy to work well.

They need to understand and care about it. Lack of resources, both for starting the analysis and for carrying out the strategy long-term, can also be a problem.

Another group of challenges relates to the company's culture. If the company doesn't prioritize understanding customers, is resistant to change, lacks creativity, doesn't communicate well, and only thinks short-term, it can hinder market segmentation.

Having a formal marketing function and knowledgeable experts is crucial. Without them, it's tough to succeed.

Sometimes, there might be practical limitations like not having enough money or not being able to make the necessary structural changes. Problems with the process itself, like not setting clear goals, poor planning, or lacking a structured approach, can also get in the way.

It's important to overcome these challenges or seriously consider whether to continue with market segmentation. If a company decides to move forward, it needs determination, patience, and a willingness to deal with problems that might come up.

**Step 2: Specifying the Ideal Target Segment**

## **Segment Evaluation Criteria**

The third layer of market segmentation analysis depends mostly on input from users, which means the people who will use the results of the analysis. This step is crucial for the analysis to be helpful to a company.

User input should not only happen at the beginning when the analysis starts or at the end when planning marketing, but throughout most of the process.

Once a company decides to look into market segmentation (Step 1), they need to contribute a lot in Step 2. This contribution helps shape the analysis and influences many other steps, especially Step 3 (data collection) and Step 8 (choosing target segments).

In Step 2, the company has to decide on two sets of criteria. The first set is called "knock-out criteria." These are the most important features that a segment must have for the company to consider targeting it.

The second set is called "attractiveness criteria." These are used to compare and decide which remaining segments are the most appealing.

Different sources offer various segment evaluation criteria, but they don't always clearly distinguish between knock-out and attractiveness criteria. The literature suggests a wide range of possible criteria at different levels of detail.

## **Knock-Out Criteria**

Knock-out criteria help decide if the market segments found in the segmentation analysis are suitable to be considered further. They are like filters to narrow down the options.

There are several important knock-out criteria that were first suggested by Kotler and later expanded upon by other authors:

***1. Homogeneity:*** The people in the segment should be similar to each other.

***2. Distinctiveness:*** The segment should be noticeably different from other segments.

***3. Size:*** The segment should have enough people to make it worth customizing marketing efforts.

***4. Fit with Company Strengths:***The company should have the ability to meet the needs of the segment.

***5. Identifiability:***The segment's members should be recognizable or identifiable in the market.

***6. Reachability:*** The company should be able to connect with and communicate to the members of the segment.

These criteria help ensure that the segments are feasible and valuable for the company. It's important that senior management, the segmentation team, and advisors understand these criteria. While some criteria are clear, like size, others might need specific details, like setting a minimum number of people for a viable segment.

## **Attractiveness Criteria**

Unlike knock-out criteria, attractiveness criteria aren't a simple yes-or-no question. Each market segment gets a rating for each criterion. This rating indicates how attractive the segment is based on that criterion. When you look at the attractiveness ratings across all the criteria, you can then decide if a market segment should be chosen as a target segment in Step 8 of the market segmentation analysis. This means that you're evaluating how well a segment fits not just one criterion, but multiple factors to make the best decision.

## **Implementing a Structured Process**

In the field of market segmentation, there's a consensus that using a structured process to assess market segments is helpful. The structured approach is recommended by experts such as Lilien and Rangaswamy (2003) and McDonald and Dunbar (2012).

A widely used structured method for evaluating market segments involves creating a segment evaluation plot. Both attractiveness and competitiveness values are determined by the segmentation team. However, since there isn't a universal set of criteria suitable for all organizations, the specific factors that make up these values need to be discussed and agreed upon.

To achieve this, it's common to involve representatives from various organizational units. These representatives bring different perspectives and will be affected by the segmentation strategy if it's implemented. Their input is valuable during the discussion and modification of the proposed criteria.

Although the segment evaluation plot can't be fully completed in Step 2 because there are no segments to assess yet, selecting attractiveness criteria at this early stage is important. It ensures that data collected in Step 3 captures the necessary information and simplifies the task of selecting a target segment in Step 8.

By the end of this step, the segmentation team should have about six attractiveness criteria, each with a weight indicating its importance compared to the others.

The usual method for assigning weights involves team members distributing 100 points among the criteria and then negotiating until agreement is reached. Involving the advisory committee, which includes representatives from different organizational units, can provide a well-rounded perspective during this process.

**Step 3: Collecting Data**

Segmentation Variables

In market segmentation, empirical data is the foundation for both commonsense and data-driven approaches. This data is used to define or form market segments and, later in the process, to provide detailed descriptions of these segments.

In this context, the term "segmentation variable" refers to the specific characteristic from the empirical data used in commonsense segmentation to divide the sample into market segments. In commonsense segmentation, this variable is typically a single trait of the consumers being studied. In this example, gender is the segmentation variable. The market segments are simply created by splitting the sample into male and female segments based on this variable.

The other personal characteristics available in the data – such as age, number of vacations taken, and preferences for vacation benefits – are referred to as "descriptor variables." These variables help provide a detailed description of the segments. This description is crucial for developing an effective marketing strategy tailored to the segment. Descriptor variables commonly include socio-demographic data and information about media behavior, which assists marketers in reaching their target segment with appropriate communication.

The distinction between commonsense and data-driven market segmentation lies in the number of segmentation variables used. In data-driven segmentation, multiple variables are employed as the starting point to identify or create market segments that are useful for the organization.

Segmentation Criteria

Before even extracting segments or collecting data for segment extraction, an organization faces a crucial decision: picking the segmentation criterion (Tynan and Drayton 1987). In this context, "segmentation criterion" refers to the nature of the information used for segmenting, and it can relate to various aspects like geographic, demographic, psychographic, or behavioral characteristics.

This decision can't be easily handed off to a consultant or data analyst because it requires a deep understanding of the market. There are several common segmentation criteria, including geographic (location-based), socio-demographic (characteristics like age, gender, income), psychographic (lifestyle, values), and behavioral (how consumers act and interact).

Different experts suggest various important distinctions among consumers for segmentation, such as their profitability, bargaining power, preferences, barriers to choice, and how they interact with each other. Given the variety of criteria available, determining the best one to use can be challenging. As Hoek et al. (1996) mention, there aren't strict rules for choosing the most suitable approach for a particular marketing context.

In general, it's recommended to opt for the simplest approach that works. If demographic segmentation fits your product or service, use it. If geographic segmentation makes sense due to product regional appeal, then use that. The choice isn't about what's trendier or more sophisticated, but what suits your product or service effectively and efficiently.

## **Geographic Segmentation**

Geographic information, such as a consumer's location of residence, is often considered the original segmentation criterion for market segmentation (Lewis et al. 1995; Tynan and Drayton 1987). In geographic segmentation, consumers are grouped based on where they live.

This approach is simple but can be quite effective. For instance, if a tourism organization in Austria wants to attract tourists from neighboring countries, language differences play a practical role in treating tourists from different countries as distinct segments.

Geographic segmentation offers the advantage of easy assignment of consumers to specific geographic units. This makes it convenient to target communication messages and select communication channels like local newspapers and radio stations to reach specific geographic segments.

However, a major drawback is that living in the same area doesn't necessarily mean people share other characteristics relevant to marketing, such as their preferences when buying products. For instance, people living in luxury suburbs might have similar income levels, but their product preferences might differ significantly. Thus, using location alone might not provide accurate insights into consumer preferences.

Despite these limitations, the use of geographic information has gained renewed interest in international market segmentation studies, where researchers aim to identify market segments across different countries.

However, this approach is challenging as the segmentation variables must hold meaning across various cultural backgrounds and regions.

Biases can arise if surveys are conducted with respondents from different cultures. International studies like the one conducted by Haverila (2013), which identified market segments of young mobile phone users across national borders, demonstrate the complexity and potential of such approaches.

## **Socio-Demographic Segmentation**

Socio-demographic segmentation criteria, like age, gender, income, and education, are commonly used to group consumers with similar characteristics. These criteria work well in certain industries like luxury goods, cosmetics, and retirement villages, where these factors strongly influence consumer choices. However, they might not fully explain preferences in many cases, and their usefulness can be limited. Scholars suggest that values, tastes, and preferences are often more influential and valuable for creating effective market segments.

## **Psychographic Segmentation**

Psychographic segmentation involves grouping individuals based on their psychological characteristics such as beliefs, interests, preferences, aspirations, and benefits sought when making purchases.

Benefit segmentation, introduced by Haley, is a popular form of psychographic segmentation. Another approach is lifestyle segmentation, which considers people's activities, opinions, and interests.

Psychographic criteria are more intricate than geographic or socio-demographic ones because a single characteristic might not fully capture the psychological dimension. Thus, psychographic segmentation typically involves using multiple variables, such as different travel motives or perceived risks.

While psychographic segmentation provides deeper insights into consumer behavior, it also poses challenges in determining segment memberships and relies on accurate measurement of psychological dimensions.

## **Behavioral Segmentation**

Behavioral segmentation involves categorizing individuals based on their observable behaviors or reported behaviors, such as prior experience with a product, purchase frequency, amount spent on purchases, or information search behavior. This approach seeks to group individuals who exhibit similar patterns of behavior.

The advantage of behavioral segmentation lies in its direct alignment with the behavior of interest. For instance, using actual purchase data or observed expenses as segmentation variables can lead to more accurate and meaningful segmentations.

This approach also eliminates the need for developing complex psychological constructs and measuring them accurately.

However, one challenge with behavioral segmentation is that obtaining behavioral data can be challenging, especially when trying to include potential customers who have not yet made a purchase. This can limit the scope of the segmentation analysis to existing customers rather than capturing a broader market perspective.

**Data from Survey Studies**

**Choice of Variables:** Selecting the right attributes to measure in the survey is essential for effective market segmentation. These attributes could be demographic, psychographic, or behavioral in nature.

**Response Options:** The choices provided to respondents while answering survey questions can be open-ended or closed-ended. Careful selection of response options ensures relevant and accurate data collection.

**Response Styles:** Researchers need to be aware of biases like acquiescence or extreme response tendencies, which can affect how respondents answer survey questions.

**Sample Size:** Having an appropriate sample size is crucial for reliable survey results. It balances representation and accuracy in data collection.

Data from Internal Sources

Organizations increasingly utilize their internal data for market segmentation analysis. Examples include scanner data from grocery stores, booking data from airline loyalty programs, and online purchase data. The advantage of such data lies in its representation of actual consumer behavior rather than self-reported behavior or intentions. Internal data is automatically generated and easily accessible, but a potential drawback is that it might be biased towards existing customers and may lack insights into potential future customers' consumption patterns.

**Data from Experimental Studies**

Experimental data, generated from field or laboratory experiments, can be another valuable source for market segmentation analysis. These experiments could involve testing responses to advertisements or conducting choice experiments to understand consumer preferences based on various product attributes and levels. The resulting data from such experiments can serve as potential segmentation criteria.