

# Market Segmentation Process Steps and Checklists

## Step 1: Deciding (not) to Segment

### Implications of Committing to Market Segmentation (Step 1):

- Market segmentation is a significant, long-term marketing strategy that provides numerous benefits to organizations, it requires good amount of investments and organizational changes. It requires a long-term commitment, this commitment is linked to an organization's willingness and capability to undergo changes and investments. Segmentation doesn't come for free; it involves costs such as research, surveys, product adaptations, and the development of multiple communication strategies. To justify these expenses, it's important that the expected increase in sales outweigh the costs. Furthermore, implementing market segmentation often includes modifications in product development, pricing strategies, distribution channels, and communication methods. These changes can also extend to the internal structure of the organization, which may need realignment to effectively target different market segments. It is important that the organization thoroughly consider these implications before deciding on a market segmentation strategy.

### Implementation Barriers (Step 2):

While market segmentation promises great rewards, its successful implementation is not without its challenges. These barriers can hinder the smooth rollout of a market segmentation strategy. First and foremost, senior management plays a crucial role. Lack of leadership, proactivity, commitment and active involvement in the segmentation process by senior leaders can severely weaken its success. Without the executive's support and understanding, it becomes almost impossible for senior marketing executives to implement the segmentation conclusions effectively. Additionally inadequate

resource allocation from senior management both for initial analysis and long-term is important. Short-term thinking, hesitation in making necessary changes and internal office politics can complicate the matter even more. Another challenge is lack of training. If senior management and segmentation team do not fully understand the fundamentals of market segmentation or potential risks of pursuing this strategy, their efforts may falter. The absence of a qualified data manager and analyst can also become significant blocks in the implementation.

### **Checklist:**

- **Culture:** Is the organization's culture market-oriented? (Yes/No)
- **Willingness to Change:** Is the organization genuinely willing to embrace change? (Yes/No)
- **Long-term Perspective:** Does the organization take a long-term perspective? (Yes/No)
- **Openness to New Ideas:** Is the organization open to innovative ideas and approaches? (Yes/No)
- **Communication:** Is communication across organizational units effective? (Yes/No)
- **Capability for Structural Changes:** Is the organization capable of making substantial structural changes if required? (Yes/No)
- **Financial Resources:** Does the organization have sufficient financial resources to support segmentation? (Yes/No)
- **Management Commitment:** Is there visible commitment from senior management to segmentation? (Yes/No)
- **Management Involvement:** Is senior management actively involved in the analysis? (Yes/No)
- **Financial Commitment:** Has the necessary financial commitment been secured? (Yes/No)

- **Understanding of Segmentation:** Is the concept of market segmentation fully understood across the organization? (Yes/No)
- **Understanding of Implications:** Are the implications of pursuing segmentation well-understood? (Yes/No)
- **Responsibility Assignment:** Have responsibilities been assigned to the segmentation team? (Yes/No)
- **Time Allocation:** Is there enough time for segmentation analysis without time pressure? (Yes/No)

## Step 2: Specifying the Ideal Target Segment

In this phase of market segmentation analysis the focus shifts to determine the ideal target segment. User input plays a important role throughout this stage, focusing the need for continuous involvement and collaboration. Two sets of criteria are developed: Knock-out criteria and attractiveness criteria both serving a different purpose.

### Segment Evaluation Criteria:

**Knock-Out Criteria:** These are non-negotiable criteria that a segment must meet to be considered for targeting. Some of those are -

- 1) Homogeneity: Segment members must be similar to each other.
- 2) Distinctness: Segment members must be distinctly different from members of other segments.
- 3) Size: The segment must be large enough to justify customization.
- 4) Match: The segment should align with the organization's strengths.
- 5) Identifiability: Members of the segment must be identifiable.

6) Reachability: There must be a way to access segment members.

**Attractiveness Criteria:** These criteria evaluate the relative attractiveness of potential target segments. The segmentation team selects from a diverse range of criteria, such as market potential, competitiveness, profitability, and more.

### **Implementing a Structured Process:**

- A structured approach involving a team is recommended for evaluating segments.
- The segment evaluation plot a popular tool helps visualize segment attractiveness and organizational competitiveness.
- The team selects approximately six attractiveness criteria and assigns weights to each criteria hence reflecting their importance.

### **Step 2 Checklist:**

- Schedule a segmentation team meeting.
- Define and agree upon knock-out criteria : similarity, distinctness, size, match, identifiability and reachability.
- Present knock out criteria to the advisory committee for discussion and potential agreement.
- Study and discuss potential segment attractiveness criteria with the segmentation team.
- Present the selected attractiveness criteria and their weights to the advisory committee for discussion and potential adjustment.

In Step 2, the groundwork is laid for assessing and selecting the ideal target segment in later stages of the market segmentation analysis. It involves careful

consideration of criteria, collaboration among team members, and alignment with organizational objectives.

## **Market Segmentation: Step 3 - Collecting Data and Choosing Segmentation Criteria:**

In step 3 of the market segmentation process collecting data is crucial for both common-sense and data-driven segmentation. Empirical data helps identify and describe market segments. The key term here is “segmentation variable” which is a characteristic used to split a sample into market segments. For commonsense segmentation a single characteristic is used while data-driven segmentation involves multiple variables.

Descriptor variables like age and travel behaviour are used to provide detailed descriptions of the segments. Good quality data is essential for accurate segmentation and effective marketing strategies.

Data can come from surveys, observations or experiments. However the data should reflect actual consumer behaviour and surveys may not always be the best source.

Choosing a segmentation criteria is a critical decision and should align with market knowledge. Common criteria include geographic and socio-demographic and behavioural factors. The recommendation is to use the simplest approach that works for the product or service as complexity does not necessarily equate to effectiveness.

Collecting high quality empirical data is essential for successful market segmentation. The choice of segmentation criteria should be based on what

aligns best with the specific market and product/service, focusing on simplicity when possible

## **Segmentation Criteria -**

### **a) Geographic Segmentation**

- 1) Geographic information is an essential segmentation criterion.
- 2) Consumer location often forms the basis for market segments.
- 3) It's practical, especially when language or location-specific factors matter.
- 4) Advantages include easy targeting of communication channels.
- 5) Disadvantages include overlooking other relevant consumer characteristics.

### **b) Psychographic Segmentation**

- 1) Psychological criteria like beliefs, interests, and benefits sought are used.
- 2) Often involves multiple segmentation variables to capture complexity.
- 3) Provides insights into the underlying reasons for consumer behavior.
- 4) Complexity arises in determining segment memberships and relies on reliable measures.

### **c) Socio-Demographic Segmentation:**

- 1) Criteria like age, gender, income, and education are common.
- 2) Useful in industries like luxury goods, cosmetics, and retirement villages.
- 3) Offers straightforward segment determination but may not explain product preferences.
- 4) Socio-demographics explain a small part of consumer behaviour.

### **Behavioural Segmentation:**

- 1) Focuses on similarities in consumer behavior or reported behavior.
- 2) Behaviours like prior experience, purchase frequency, and spending are considered.
- 3) Advantages include using the most relevant behavior as the basis for segmentation.
- 4) Challenges include obtaining behavioural data, especially for potential new customers.

## **Data from Survey Studies**

### **Choice of Variables:**

- 1) Selecting the right variables for segmentation is crucial.
- 2) In data-driven segmentation, all relevant variables for the segmentation criterion must be included.
- 3) Avoid including unnecessary variables that can lead to respondent fatigue and complicate analysis.
- 4) Noisy or masking variables should be avoided, as they hinder correct segmentation.

### **Response Options:**

- 1) Survey response options impact subsequent analysis.
- 2) Binary and metric data are ideal for segmentation.
- 3) Nominal data can be transformed into binary data.
- 4) Ordinal data, though common, pose challenges due to undefined distances.
- 5) Binary or metric options should be used when meaningful.

### **Response Styles:**

- 1) Survey data can capture biases and response styles.
- 2) Response styles are systematic tendencies to respond differently.
- 3) Response styles can affect segmentation results.
- 4) Minimizing the risk of capturing response styles is crucial for accurate segmentation.
- 5) Additional analyses or removal of affected respondents may be necessary.

### **Sample Size for Market Segmentation Analysis:**

- 1) The sample size is a critical factor in market segmentation analysis.
- 2) Small sample sizes can lead to unreliable segmentation results.
- 3) Increasing sample size improves the accuracy of segmentation results, but the effect varies depending on market and data characteristics.
- 4) Recommendations for sample size depend on factors like the number of segmentation variables, market characteristics (e.g., segment size, overlap), and data quality.

### **Sample Size Recommendations:**

- 1) Viennese psychologist Formann recommends a sample size of at least  $2p$  (better five times  $2p$ ), where  $p$  is the number of segmentation variables.
- 2) Qiu and Joe recommend a sample size of at least ten times the number of segmentation variables times the number of segments in the data.
- 3) Dolnicar et al. suggest a sample size of at least  $60 \cdot p$  or  $70 \cdot p$  for more challenging scenarios.

### **Data Quality Recommendations:**

- 1) To ensure reliable segmentation, data should contain all necessary items, exclude unnecessary items, and avoid correlated items.



2)High-quality responses, binary or metric measurement, and the absence of response styles are essential.

3)A suitable sample size, typically 100 times the number of segmentation variables, should be ensured.

### **Data from Internal Sources:**

1)Organizations often have access to substantial internal data that can be used for market segmentation.

2)Examples include scanner data in grocery stores, booking data from airline loyalty programs, and online purchase data.

3)Advantages of internal data include representing actual consumer behavior and not relying on self-reported data, which can be subject to memory and response biases.

4)Internal data may be biased towards existing customers, potentially missing information about potential future customers with different consumption patterns.

### **Data from Experimental Studies:**

1)Experimental data can be collected through field or laboratory experiments.

2)Experiments can involve testing consumer responses to advertisements, conducting choice experiments, or conjoint analyses.

3)Experimental data can provide insights into consumer preferences and the impact of specific product attributes on choice, which can be used as segmentation criteria.

### **Step 3 Checklist for Data Collection:**

1)Schedule a market segmentation team meeting.

2)Select segmentation and descriptor variables.

3)Plan data collection to minimize biases and errors.

4)Collect the necessary data.

In summary, the market segmentation process involves a series of strategic steps aimed at identifying and targeting specific customer segments for more effective marketing efforts. This process begins with the decision to segment or not, considering the organizational commitment and potential barriers. It then progresses to specifying the ideal target segment, defining criteria, and evaluating segment attractiveness. Data collection and the choice of segmentation criteria are pivotal in this phase. Different data sources, including surveys, internal data, and experimental studies, can provide valuable insights.

This summary report provides comprehensive checklists for each step, addressing critical considerations such as organizational culture, leadership commitment, resource allocation, and data quality. It emphasizes the importance of a structured approach, teamwork, and careful selection of segmentation variables. Moreover, it highlights the significance of high-quality data, sample size, and the alignment of segmentation criteria with market and product specifics.