

# Summary

## Step 1

### Implications and Barriers of Market Segmentation

#### 1.1 Implications of Committing to Market Segmentation

Market segmentation is a critical marketing strategy that requires a long-term commitment from an organization. Unlike a temporary tactic, it necessitates substantial changes and investments in areas like product development, pricing, distribution, and communication. These changes may also lead to structural adjustments within the organization, particularly if different market segments are targeted. The decision to implement market segmentation must be made at the highest executive level and should be communicated consistently across all organizational levels.

#### 1.2 Implementation Barriers

Several barriers can impede the successful implementation of a market segmentation strategy:

**Senior Management Issues:** Lack of leadership, commitment, and involvement from senior management can undermine the process. Without their support, allocating resources and implementing the strategy becomes challenging.

**Organizational Culture:** Resistance to change, lack of market orientation, poor communication, and short-term thinking within the organization can hinder the implementation. Training is crucial to ensure that all stakeholders understand the foundations and implications of market segmentation.

**Operational Challenges:** A lack of a formal marketing function, qualified marketing experts, or data analysts can be major obstacles. Additionally, financial constraints and the inability to make necessary structural changes can prevent successful implementation.

**Process-Related Barriers:** Issues such as unclear objectives, lack of planning, inadequate process structuring, and time pressure can negatively affect the segmentation outcome. Ensuring that management understands and accepts the techniques used is essential for success.

These barriers should be identified early in the market segmentation study and addressed proactively. If they cannot be removed, it may be wise to reconsider pursuing the strategy.

### 1.3 Step 1 Checklist

Before proceeding with market segmentation, organizations should ensure they are market-oriented, open to change and new ideas, capable of making structural changes, and have sufficient financial resources. Senior management's visible commitment and involvement are crucial, along with clear objectives and a structured process for the segmentation analysis. Proper training and the inclusion of marketing and data experts in the team are also essential.

## STEP 2

### 2.1 Segment Evaluation Criteria

**User Involvement:** Continuous involvement of the user throughout the segmentation process is necessary for producing meaningful results.

**Evaluation Criteria:** The organization must determine two sets of evaluation criteria:

**Knock-out Criteria:** Non-negotiable, essential features that a segment must have to be considered.

**Attractiveness Criteria:** Used to evaluate the relative attractiveness of segments that meet the knock-out criteria.

### 2.2 Knock-Out Criteria

**Purpose:** To filter out segments that do not meet essential requirements.

**Common Criteria:** Homogeneity, distinctness, size, match with organizational strengths, identifiability, and reachability.

**Role of Management:** Senior management, the segmentation team, and the advisory committee must understand and agree on these criteria.

### 2.3 Attractiveness Criteria

**Purpose:** To assess the relative attractiveness of each qualifying segment.

**Assessment:** Segments are rated on a spectrum of attractiveness rather than as simply meeting or not meeting criteria.

## 2.4 Implementing a Structured Process

**Importance:** Following a structured process, such as a segment evaluation plot, is beneficial.

**Segment Evaluation Plot:** A tool used to visually assess segment attractiveness and organizational competitiveness.

**Team Involvement:** Representatives from various organizational units should be involved to provide diverse perspectives.

## 2.5 Step 2 Checklist

**Tasks:** A series of tasks are outlined, including convening a segmentation team meeting, agreeing on knock-out and attractiveness criteria, and presenting these criteria to an advisory committee for approval.

### Summary

In Step 2, the organization establishes critical criteria for evaluating market segments. Knock-out criteria ensure that only viable segments proceed, while attractiveness criteria help in selecting the most promising target segments. A structured approach involving various stakeholders is recommended to ensure that all relevant factors are considered.

## 3.1 Segmentation Variables

### Empirical Data in Segmentation:

**Segmentation Variable:** A characteristic used to split data into market segments.

**Commonsense Segmentation:** Uses a single characteristic (e.g., gender) to create segments. Other characteristics serve as descriptor variables (e.g., age, vacation habits).

**Data-Driven Segmentation:** Uses multiple characteristics (segmentation variables) to identify or create segments. Descriptor variables provide additional detail about the segments.

Examples:

**Commonsense Segmentation:** Splitting data by gender (male/female) and using age, number of vacations, and benefits sought as descriptors.

**Data-Driven Segmentation:** Using benefits sought (relaxation, culture, etc.) as segmentation variables, with socio-demographics and travel behavior as descriptors

### **Importance of Data Quality:**

**Commonsense Segmentation:** Accurate data ensures correct segment assignment and description.

**Data-Driven Segmentation:** Good data quality is crucial for valid segment creation and detailed descriptions.

### **Sources of Empirical Data:**

**Survey Studies:** Common but can be unreliable, especially for socially desirable behaviors.

**Observations:** Includes scanner data and loyalty programs.

**Experimental Studies:** Provide additional data reflecting consumer behavior.

**Best Practice:** Use data sources that most accurately reflect actual consumer behavior for reliable segmentation analysis.

## **3.2 Segmentation Criteria**

Long before segments are extracted, and long before data for segment extraction is collected, the organisation must make an important decision: it must choose which segmentation criterion to use (Tynan and Drayton 1987). The term segmentation criterion is used here in a broader sense than the term segmentation variable. The term segmentation variable refers to one measured value, for example, one item in a survey, or one observed expenditure category. The term segmentation criterion relates to the nature of the information used for market segmentation. It can also relate to one specific construct, such as benefits sought.

The decision which segmentation criterion to use cannot easily be outsourced to either a consultant or a data analyst because it requires prior knowledge about the market. The most common segmentation criteria are geographic, socio-demographic, psychographic and behavioural.

Bock and Uncles (2002) argue that the following differences between consumers are the most relevant in terms of market segmentation: profitability, bargaining power, preferences for benefits or products, barriers to choice and consumer interaction effects. With so many different segmentation criteria available, which

is the best to use? As Hoek et al. (1996) note, few guidelines as to the most appropriate base to use in a given marketing context exist (p. 26). Generally, the recommendation is to use the simplest possible approach. Cahill (2006) states this very clearly in his book on lifestyle segmentation (p. 159): Do the least you can. If demographic segmentation will work for your product or service, then use demographic segmentation. If geographic segmentation will work because your product will only appeal to people in a certain region, then use it. Just because psychographic segmentation is sexier and more sophisticated than demographic or geographic segmentation does not make it better. Better is what works for your product or service at the least possible cost.

### **3.2.1 Geographic Segmentation**

Geographic information is seen as the original segmentation criterion used for the purpose of market segmentation (Lewis et al. 1995; Tynan and Drayton 1987). Typically – when geographic segmentation is used – the consumer's location of residence serves as the only criterion to form market segments. While simple, the geographic segmentation approach is often the most appropriate. For example: if the national tourism organisation of Austria wants to attract tourists from neighbouring countries, it needs to use a number of different languages: Italian, German, Slovenian, Hungarian, Czech. Language differences across countries represent a very pragmatic reason for treating tourists from different neighbouring countries as different segments. Interesting examples are also provided by global companies such as Amazon selling its Kindle online: one common web page is used for the description of the base product, then customers are asked to indicate their country of residence and country specific additional information is provided. IKEA offers a similar product range worldwide, yet slight differences in offers, pricing as well as the option to purchase online exist in dependence of the customer's geographic location.

The key advantage of geographic segmentation is that each consumer can easily be assigned to a geographic unit. As a consequence, it is easy to target communication messages, and select communication channels (such as local newspapers, local radio and TV stations) to reach the selected geographic segments.

The key disadvantage is that living in the same country or area does not necessarily mean that people share other characteristics relevant to marketers, such

### **3.2 Segmentation Criteria :**

as benefits they seek when purchasing a product. While, for example, people residing in luxury suburbs may all be a good target market for luxury cars, location is rarely the reason for differences in product preference. Even in the case of luxury suburbs, it is more likely that socio-demographic criteria are the reason for both similar choice of suburb to live in and similar car preferences. The typical case is best illustrated using tourism: people from the same country of origin are likely to have a wide range of different ideal holidays, depending on whether they are single or travel as a family, whether they are into sports or culture.

Despite the potential shortcomings of using geographic information as the segmentation variable, the location aspect has experienced a revival in international market segmentation studies aiming to extract market segments across geographic boundaries. Such an approach is challenging because the segmentation variable(s) must be meaningful across all the included geographic regions, and because of the known biases that can occur if surveys are completed by respondents from different cultural backgrounds (Steenkamp and Ter Hofstede 2002). An example of such an international market segmentation study is provided by Haverila (2013) who extracted market segments of mobile phone users among young customers across national borders.

### **3.2.2 Socio-Demographic Segmentation**

Typical socio-demographic segmentation criteria include age, gender, income and education. Socio-demographic segments can be very useful in some industries. For example: luxury goods (associated with high income), cosmetics (associated with gender; even in times where men are targeted, the female and male segments are treated distinctly differently), baby products (associated with gender), retirement villages (associated with age), tourism resort products (associated with having small children or not).

As is the case with geographic segmentation, socio-demographic segmentation criteria have the advantage that segment membership can easily be determined for every consumer. In some instances, the socio-demographic criterion may also offer an explanation for specific product preferences (having children, for example, is the actual reason that families choose a family vacation village where previously, as a couple, their vacation choice may have been entirely different). But in many instances, the socio-demographic criterion is not the cause for product preferences, thus not providing sufficient market insight for optimal segmentation decisions.

Haley (1985) estimates that demographics explain about 5% of the variance in consumer behaviour. Yankelovich and Meer (2006) argue that socio-demographics do not represent a strong basis for market segmentation, suggesting that values, tastes and preferences are more useful because they are more influential in terms of consumers' buying decisions.

### **5.2.3 Psychographic Segmentation**

When people are grouped according to psychological criteria, such as their beliefs, interests, preferences, aspirations, or benefits sought when purchasing a product, the term psychographic segmentation is used. Haley (1985) explains that the word psychographics was intended as an umbrella term to cover all measures of the mind (p. 7). Benefit segmentation, which Haley (1968) is credited for, is arguably the most popular kind of psychographic segmentation. Lifestyle segmentation is another

popular psychographic segmentation approach (Cahill 2006); it is based on people's activities, opinions and interests.

Psychographic criteria are, by nature, more complex than geographic or socio-demographic criteria because it is difficult to find a single characteristic of a

person that will provide insight into the psychographic dimension of interest.

As a consequence, most psychographic segmentation studies use a number of segmentation variables, for example: a number of different travel motives, a number of perceived risks when going on vacation.

The psychographic approach has the advantage that it is generally more reflective of the underlying reasons for differences in consumer behaviour. For example, tourists whose primary motivation to go on vacation is to learn about other cultures, have a high likelihood of undertaking a cultural holiday at a destination that has ample cultural treasures for them to explore. Not surprisingly, therefore, travel motives have been frequently used as the basis for data-driven market segmentation in tourism (Bieger and Laesser 2002; Laesser et al. 2006; Boksberger and Laesser 2009). The disadvantage of the psychographic approach is the increased complexity of determining segment memberships for consumers. Also, the power of the psychographic approach depends heavily on the reliability and validity of the empirical measures used to capture the psychographic dimensions of interest.

### **3.2.4 Behavioural Segmentation**

Another approach to segment extraction is to search directly for similarities in behaviour or reported behaviour. A wide range of possible behaviours can be used for this purpose, including prior experience with the product, frequency of purchase, amount spent on purchasing the product on each occasion (or across multiple purchase occasions), and information search behaviour. In a comparison of different segmentation criteria used as segmentation variables, behaviours reported



by tourists emerged as superior to geographic variables (Moscardo et al. 2001).

The key advantage of behavioural approaches is that – if based on actual behaviour rather than stated behaviour or stated intended behaviour – the very behaviour of interest is used as the basis of segment extraction. As such, behavioural segmentation groups people by the similarity which matters most. Examples of such segmentation analyses are provided by Tsai and Chiu (2004) who use actual

### **3.3 Data from Survey Studies**

expenses of consumers as segmentation variables, and Heilman and Bowman (2002) who use actual purchase data across product categories. Brand choice behaviour over time has also been used as segmentation variable by several authors (Poulsen 1990; Bockenholt and Langeheine 1996; Ramaswamy 1997, see also Section 7.3.3). Using behavioural data also avoids the need for the development of valid measures for psychological constructs.

But behavioural data is not always readily available, especially if the aim is to include in the segmentation analysis potential customers who have not previously purchased the product, rather than limiting oneself to the study of existing customers of the organisation.