Fundamentals of Market Segmentation

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Part I Introduction

1. Market Segmentation

Market segmentation is the process of dividing a broad market into smaller groups of consumers with similar needs, wants, and behaviours. This allows businesses to target their marketing efforts more effectively and efficiently. Once a business has identified its target market, it can develop marketing strategies that are tailored to the specific needs of that group. For example, a business that sells clothing might target young adults with a hip and trendy marketing campaign, while a business that sells retirement homes might target older adults with a more sedate and dignified marketing campaign.

Part II Steps of Market Segmentation Analysis

2. Step 1: Deciding (not) to Segment

The first step in market segmentation is to decide whether or not to segment the market. There are a number of factors to consider when making this decision, including the size of the market, the diversity of the customer base, the company's resources, and the company's goals.

Deciding not to segment can be a viable option for some companies. If the market is small, the customer base is not very diverse, or the company does not have the resources to invest in segmentation, it may be better to focus on marketing to the entire market. However, for most companies, segmentation is a valuable tool that can help them to reach their marketing goals.

2.1 Implications of committing to market segmentation

First, it requires the organization to invest time and resources in market research. Second, market segmentation requires the organization to be flexible and adaptable.

2.2 Implementation barriers

The first group of barriers relates to senior management. Lack of leadership, pro-active championing, commitment and involvement in the market segmentation process by senior leadership undermines the success of market segmentation.

A second group of barriers relates to organisational culture. Lack of market or consumer orientation, resistance to change and new ideas, lack of creative thinking, bad communication and lack of sharing of information and insights across organisational units, short-term thinking,

unwillingness to make changes and office politics have been identified as preventing the successful implementation of market segmentation.

3. Step 2: Specifying the Ideal Target Segment

This step of market segmentation analysis is to specify the ideal target segment. This involves identifying the criteria that are most important to the organization when selecting a target market. The criteria may include factors such as the size and growth potential of the segment, the profitability of the segment, the organization's ability to reach and serve the segment, and the fit between the segment's needs and the organization's capabilities.

Once the criteria have been identified, the organization can evaluate each segment to determine which segments meet the criteria. The organization may then select one or more segments to target.

By specifying the ideal target segment, the organization can increase its chances of success in the marketplace.

3.1 Segment evaluation criteria

The criteria used to evaluate market segments. Segment evaluation criteria can be divided into two main categories:

Knock-out criteria: These are criteria that must be met for a segment to be considered for targeting. If a segment does not meet any of the knock-out criteria, it will not be considered for targeting.

Attractiveness criteria: These are criteria that are used to assess the relative attractiveness of segments that meet the knock-out criteria. The organization will select the segments that have the highest scores on the attractiveness criteria.

3.2 Knock-out criteria

The following are some examples of knock-out criteria:

The segment must be homogeneous
The segment must be large enough to be profitable.
The organization must be able to reach and serve the segment.
The segment's needs must be compatible with the organization's capabilities.

3.3 Attractiveness criteria

Attractiveness criteria are not binary in nature. Segments are not assessed as either complying or not complying with attractiveness criteria. The following are some examples of attractiveness criteria:

Customer loyalty: The segment's customer loyalty.
Purchase frequency: The segment's purchase frequency.
Purchase size: The segment's purchase size.

4. Step 3: Collecting Data

This step of market segmentation analysis is to collect data. This involves gathering information about the target market, such as their demographics, psychographics, and behaviour. The data can be collected through a variety of methods, such as surveys, interviews, focus groups, and observation.

The data collected in this step will be used to create a profile of the target market. This profile will help the organization to understand the needs and wants of the target market, as well as their buying behaviour. The profile will also help the organization to identify the best way to reach and communicate with the target market.

By collecting data about the target market, the organization can gain a better understanding of the market and develop a more effective marketing strategy.

4.1 Segmentation Variables and Criteria

Geographical Variables: It is the original segmentation criterion of market segmentation. The consumer's location of residence serves as the criterion to form market segments.

Socio-Demographic variables: These variables include age, gender, income, education, and location.

Psychographic variables: These variables include personality, lifestyle, values, and interests.

Behavioural variables: These variables include purchase behaviour, usage rate, and loyalty.

The choice of segmentation variables depends on the specific market and the objectives of the segmentation analysis. For example, a company that is targeting a new product at young professionals might use age, income, and education as segmentation variables

Segmentation criteria are the rules that are used to select the most appropriate segmentation variables.

4.2 Data from Survey Studies, Internal Sources and Experimental Studies

There are a variety of sources that can be used to collect data for market segmentation analysis. Some of the most common sources include:

Survey studies: Survey studies are a great way to collect data about a target market. Surveys can be conducted online, by phone, or in person.

Internal sources: Internal sources of data include sales data, customer feedback, and website traffic data. This data can be used to identify trends and patterns in the target market.

Experimental studies: Experimental studies are a more controlled way to collect data about a target market. Experimental studies involve exposing different groups of people to different marketing messages and then measuring their response.

The data collected from these sources can be used to create a profile of the target market. This profile can then be used to develop marketing strategies that are tailored to the specific needs of the target market.

5. Step 4: Exploring Data

Data exploration is done to gain a better understanding of the data and to identify any potential problems with the data. The following are some of the methods followed during data exploration:

A First Glimpse at the Data: This step is to get a general overview of what it looks like. This can be done by looking at the data's structure, such as the number of variables and observations, and the types of variables. It is also helpful to look at the distribution of the data, such as the mean, standard deviation, and range.

Data Cleaning: This involves removing any errors or inconsistencies in the data. Data cleaning is important because it ensures that the data is accurate and reliable.

Descriptive Analysis: This involves describing the data in detail. This can be done by using statistical techniques such as means, standard deviations, and ranges. Descriptive analysis can help you to understand the data and identify any patterns or trends.

Pre-Processing: This can involve transforming the data or removing outliers. Pre-processing is important because it can help to improve the accuracy and effectiveness of the segmentation process.

Principal Components Analysis: Principal components analysis (PCA) is a statistical technique that can be used to reduce the dimensionality of the data. This can be helpful when you have a large number of variables, as it can make the data easier to interpret. PCA can also be used to identify clusters in the data, which can be helpful for market segmentation.

6. Step 5: Extracting Segments

Extracting segments is done by grouping consumers together based on their similarities. There are a number of different methods that can be used to extract segments, including:

Grouping consumers: This involves identifying common characteristics among consumers and then grouping them together based on those characteristics. For example, consumers could be grouped together by age, gender, income, or location.

Distance-based methods: These methods use the distance between consumers to identify clusters of similar consumers. The most common distance-based method is k-means clustering, which groups consumers into k clusters such that the distance between any two consumers in the same cluster is minimized.

Model-based methods: These methods use statistical models to identify segments. The most common model-based method is latent class analysis, which identifies segments by estimating the probability that a consumer belongs to each segment.

Algorithms with integrated variable selection: These methods use algorithms that select variables that are most important for segmenting consumers. The most common algorithm with integrated variable selection is recursive partitioning, which recursively splits the data into smaller and smaller groups based on the values of the variables.

Data structure analysis: This involves identifying patterns in the data that can be used to identify segments. For example, cluster analysis can be used to identify clusters of consumers who have similar purchasing patterns.

The method that is used to extract segments will depend on the specific data that is available and the goals of the market segmentation analysis. For example, if the goal is to identify segments that are most likely to respond to a marketing campaign, then a model-based method such as latent class analysis may be the best option. However, if the goal is to identify segments that have similar needs and wants, then a distance-based method such as k-means clustering may be a better option.

7. Step 6: Profiling Segments

Profiling Segments is done by describing the characteristics of each segment in detail. The following are some of the things that can be done to profile a segment:

Describe the demographic characteristics of the segment: This includes the age, gender, income, and education level of the segment.

Describe the psychographic characteristics of the segment: This includes the values, attitudes, and interests of the segment.

Describe the behavioural characteristics of the segment: This includes the buying habits, media habits, and product usage of the segment.

Describe the needs and wants of the segment: This includes what the segment is looking for in a product or service.

Describe the potential of the segment: This includes the size of the segment, the growth rate of the segment, and the profitability of the segment.

Overall, Profiling Segments is an important step that can help to ensure that the segments are understood and that they can be used to develop successful marketing strategies.

8. Step 7: Describing Segments

This step is to describe the segments that have been identified. This involves providing a detailed profile of each segment, including information on its size, demographics, psychographics, and buying behaviour. The goal of this step is to gain a deep understanding of each segment so that the company can develop a marketing strategy that is tailored to its specific needs.

Once the segments have been described, the company can then select the ones that it wants to target. The criteria for selecting target segments will vary depending on the company's goals and resources. However, some common factors that companies consider include the size of the segment, its growth potential, its profitability, and it fit with the company's overall strategy.

9. Step 8: Selecting the target segment(s):

The selection of the target segment(s) is the final step in the segmentation process, and it is where the company decides which segments it will focus its marketing efforts on.

9.1 Targeting Decision

There are three main methods for selecting target segments:

Undifferentiated targeting is when a company ignores segment differences and markets its products or services to the entire market. This is a risky strategy, as it can be difficult to appeal to everyone.

Differentiated targeting is when a company markets its products or services to multiple segments, but with different marketing strategies for each segment. This is a more complex strategy, but it can be more effective in reaching a wider audience.

Concentrated targeting is when a company focuses its marketing efforts on a single segment. This is the most risky strategy, but it can be the most rewarding if the company is able to successfully target the segment.

The company's targeting decision will depend on a number of factors, including the company's resources, the nature of the market, and the company's goals.

9.2 Market Segment Evaluation

Once the company has decided on its targeting strategy, it needs to evaluate the attractiveness of the target segments. This involves assessing the size and growth potential of the segments, the competitive landscape, and the company's ability to meet the needs of the segments.

After evaluating the target segments, the company can select the segments that it will focus its marketing efforts on. The company should select segments that are large and growing, have a low level of competition, and that the company is able to meet the needs of.

10. Step 9: Customising the Marketing Mix

The next step of market segmentation analysis is the customization of the marketing mix. This is where the company tailors its marketing strategies to the needs of the target segments.

The marketing mix is a set of four elements that a company can use to influence its customers: product, price, place, and promotion.

Product: The product is the good or service that the company offers to its customers. The company can customize the product by changing its features, benefits, or design to meet the needs of the target segments.

Price: The price is the amount of money that customers pay for the product. The company can customize the price by offering discounts, coupons, or free trials to attract customers.

Place: The place is where the product is sold. The company can customize the place by selling the product online, in stores, or through a combination of channels.

Promotion: Promotion is the way that the company communicates the value of its product to customers. The company can customize the promotion by using advertising, public relations, or social media to reach the target segments.

By customizing the marketing mix, the company can increase its chances of success in the marketplace.

11. Step 10: Evaluation and Monitoring

The last step of market segmentation analysis is the evaluation and monitoring of the segmentation process. This is where the company assesses the effectiveness of its segmentation strategy and makes adjustments as needed.

The company should evaluate its segmentation strategy on a regular basis, If the company finds that its segmentation strategy is no longer effective, it should make adjustments. The company may need to change the segmentation criteria, the target segments, or the marketing mix.

By continuously evaluating and monitoring its segmentation strategy, the company can ensure that it is targeting the right customers with the right marketing message. This will help the company achieve its marketing goals.