SUMMARY OF FUNDAMENTALS OF MARKET SEGMENTATION ANALYSIS

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**DATE: 23/03/2023**

# Step 1: Deciding (not) to Segment

Implications of Committing to Market Segmentation

**The key implication is that the organization needs to commit to the segmentation strategy on the long term. Market segmentation is a marriage, not a date. The commitment to market segmentation goes hand in hand with the willingness and ability of the organization to make substantial changes and investments. Segmenting a market is not free. There are costs of performing the research, fielding surveys, and focus groups, designing multiple packages, and designing multiple advertisements and communication messages.**

**Potentially required changes include the development of new products, the modification of existing products, changes in pricing and distribution channels used to sell the product, as well as all communications with the market. These changes, in turn, are likely to influence the internal structure of the organisation, which may need to be adjusted in view of, for example, targeting a handful of different market segments.**

**Because of the major implications of such a long-term organisational commitment, the decision to investigate the potential of a market segmentation strategy must be made at the highest executive level, and must be systematically and continuously communicated and reinforced at all organisational levels and across all organisational units.**

*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.** **Senior management can also prevent market segmentation to be successfully implemented by not making enough resources available, either for the initial market segmentation analysis itself, or for the long-term implementation of a market segmentation strategy.**

**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.** **Another potential problem is lack of training.** **The lack of a qualified data manager and analyst in the organisation can also represent major stumbling blocks. Another obstacle may be objective restrictions faced by the organisation, including lack of financial resources, or the inability to make the structural changes required.**

**Most of these barriers can be identified from the outset of a market segmentation study, and then proactively removed. If barriers cannot be removed, the option of abandoning the attempt of exploring market segmentation as a potential future strategy should be seriously considered.**

# Step 2: Specifying the Ideal Target Segment

Segment Evaluation Criteria

**It is important to understand that – for a market segmentation analysis to produce results that are useful to an organization – user input cannot be limited to either a briefing at the start of the process, or the development of a marketing mix at the end.** **It is not up to the segmentation team to negotiate the extent to which they matter in target segment selection. The second, much longer and much more diverse set of attractiveness criteria represents a shopping list for the segmentation team. Members of the segmentation team need to select which of these criteria they want to use to determine how attractive potential target segments are. The segmentation team also needs to assess the relative importance of each attractiveness criterion to the organization.**

Knock-Out Criteria

**Knock-out criteria are used to determine if market segments resulting from the market segmentation analysis qualify to be assessed using segment attractiveness criteria.** **Knock-out criteria automatically eliminate some of the available market segments, attractiveness criteria are first negotiated by the team, and then applied to determine the overall relative attractiveness of each market segment.**

* **The segment must be homogeneous; members of the segment must be similar to one another.**
* **The segment must be distinct; members of the segment must be distinctly different from members of other segments.**
* **The segment must be large enough; the segment must contain enough consumers to make it worthwhile to spend extra money on customising the marketing mix for them.**
* **The segment must be matching the strengths of the organization; the organization must have the capability to satisfy segment members’ needs.**
* **Members of the segment must be identifiable; it must be possible to spot them in the marketplace.**
* **The segment must be reachable; there has to be a way to get in touch with members of the segment in order to make the customized marketing mix accessible to them.**

**Knock-out criteria must be understood by senior management, the segmentation team, and the advisory committee. Most of them do not require further specification, but some do.**

**Attractiveness criteria are not binary in nature. Segments are not assessed as either complying or not complying with attractiveness criteria. Rather, each market segment is rated; it can be more or less attractive with respect to a specific criterion.**

**At the end of this step, the market segmentation team should have a list of approximately six segment attractiveness criteria. Each of these criteria should have a weight attached to it to indicate how important it is to the organization compared to the other criteria.**

# Step 3: Collecting Data

**Segmentation Variables**

**The term *segmentation variable* refers to the variable in the empirical data used in commonsense segmentation to split the sample into market segments. In commonsense segmentation, the segmentation variable is typically one single characteristic of the consumers in the sample.**

**Segmentation Criteria**

**The term *segmentation criterion* is used here in a broader sense than the term segmentation variable. Theterm segmentation variable refers to one measured value, for example, one item ina survey, or one observed expenditure category. The term segmentation criterionrelates to the nature of the information used for market segmentation. It can alsorelate to one specific construct, such as benefits sought.**

**To collect data, businesses should first identify the information they need to make informed decisions about market segmentation. This may include**

* **Demographic data**
* **Psychographic data**
* **Geographic data**
* **Behavioural data*.***

**Data from Survey Studies**

**Most market segmentation analyses are based on survey data. Survey data is cheap and easy to collect, making it a feasible approach for any organisation. But survey data – as opposed to data obtained from observing actual behaviour – can be contaminated by a wide range of biases. Such biases can, in turn, negatively affect the quality of solutions derived from market segmentation analysis. A few key aspects that need to be considered when using survey data are discussed below.**

* ***Choice of Variables***
* ***Response Options***
* ***Response Styles***
* ***Sample Size***

**Data from Internal Sources**

**Increasingly organisations have access to substantial amounts of internal data that can be harvested for the purpose of market segmentation analysis. Typical examples are scanner data available to grocery stores, booking data available through airline loyalty programs, and online purchase data. The**

**Data from Experimental Studies**

**Experimental data can result from field or laboratory experiments. For example, they can be the result of tests how people respond to certain advertisements.** **The aim of such studies is to present consumers with carefully developed stimuli consisting of specific levels of specific product attributes.**

# Step 6: Profiling Segments

Identifying Key Characteristics of Market Segments

**The aim of the profiling step is to get to know the market segments resulting from the extraction step. Profiling is only required when data-driven market segmentation is used. For commonsense segmentation, the profiles of the segments are predefined. The situation is quite different in the case of data-driven segmentation: users of the segmentation solution may have decided to extract segments on the basis of benefits sought by consumers.** **Profiling consists of characterising the market segments individually, but also in comparison to the other market segments.**

**At the profiling stage, we inspect a number of alternative market segmentation solutions. This is particularly important if no natural segments exist in the data, and either a reproducible or a constructive market segmentation approach has to be taken. In the following sections we discuss traditional and graphical statistics approaches to segment profiling. Graphical statistics approaches make profiling less tedious, and thus less prone to misinterpretation.**

Traditional Approaches to Profiling Market Segments

**Data-driven segmentation solutions are usually presented to users (clients, managers) in one of two ways: (1) as high level summaries simplifying segment characteristics to a point where they are misleadingly trivial, or (2) as large tables that provide, for each segment, exact percentages for each segmentation variable.**

**To identify the defining characteristics of the market segments, the percentage value of each segment for each segmentation variable needs to be compared with the values of other segments or the total value provided in the far right column.**

**Sometimes – to deal with the size of this task – information is provided about the statistical significance of the difference between segments for each of the segmentation variables. This approach, however, is not statistically correct. Segment membership is directly derived from the segmentation variables, and segments are created in a way that makes them maximally different, thus not allowing to use standard statistical tests to assess the significance of differences.**

**Segment Profiling Visualization**

**Graphics are particularly important in exploratory statistical analysis (like cluster analysis) because they provide insights into the complex relationships between variables. In addition, in times of big and increasingly bigger data, visualisation offers a simple way of monitoring developments over time. So, recommend the use of visualisation techniques to make the results of a market segmentation analysis easier to interpret.**

## Identifying Defining Characteristics of Market Segments

**A good way to understand the defining characteristics of each segment is to produce a segment profile plot. The segment profile plot shows – for all segmentation variables – how each market segment differs from the overall sample. The segment profile plot is the direct visual translation of tablesoption is to order segmentation variables by similarity of answer patterns.**

**Assessing Segment Separation**

**Segment separation can be visualised in a segment separation plot. The segment separation plot depicts – for all relevant dimensions of the data space – the overlap of segments. Segment separation plots are very simple if the number of segmentation variables is low, but become complex as the number of segmentation variables increases. But even in such complex situations, segment separation plots offer data analysts and users a quick overview of the data situation, and the segmentation solution.**

**The two dimensions representing the segmentation variables can be directly plotted. This is not possible if 20-dimensional travel motives data serve as segmentation variables. In such a situation, the 20- dimensional space needs to be projected onto a small number of dimensions to create a segment separation plot**