**Market Segmentation Analysis**

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**Steps**

* Step 1: Deciding (not) to Segment
* Step 2: Specifying the Ideal Target Segment
* Step 3: Collecting Data

**Step 1 - Deciding Whether to Segment the Market**

**1.1 Implications of Choosing Market Segmentation**

Market segmentation can be a powerful strategy, but it's not always the right choice. Before you start, consider these points:

* **Long-Term Commitment**: Market segmentation isn't a quick fix; it's a long-term strategy requiring ongoing effort and resources.
* **Cost**: Segmenting the market involves costs for research, surveys, designing various packages, and different advertisements. Ensure the potential sales increase justifies these expenses.
* **Organizational Changes**: You might need to develop new products, modify existing ones, adjust prices and distribution channels, and change how you communicate with the market. This could also mean restructuring your organization to focus on market segments rather than products.
* **Executive Decision**: The decision to segment should come from the highest level of management and be clearly communicated throughout the organization.

**1.2 Barriers to Implementation**

Successfully implementing market segmentation can be challenging due to several barriers:

1. **Senior Management Issues**:
   * Lack of leadership and commitment from top management can hinder success.
   * Not providing enough resources for both the initial analysis and long-term implementation can be problematic.
2. **Organizational Culture**:
   * Resistance to change, lack of creativity, poor communication, short-term thinking, and office politics can obstruct implementation.
   * Insufficient training and understanding of market segmentation can lead to failure.
3. **Resource and Process Issues**:
   * Limited financial resources and the inability to make necessary structural changes can be obstacles.
   * Poor planning, unclear objectives, and inadequate processes can impede progress.
   * Management's reluctance to use unfamiliar techniques can be mitigated by presenting analysis results clearly and understandably.

Most barriers can be identified early and addressed proactively. If they cannot be resolved, reconsidering the segmentation strategy might be necessary.

**1.3 Step 1 Checklist**

Use this checklist to decide if market segmentation is viable. If you answer "no" to any of these questions, reconsider proceeding.

1. **Cultural Readiness**:
   * Is the organization market-oriented?
   * Is the organization willing to change?
   * Does the organization take a long-term view?
   * Is the organization open to new ideas?
   * Is communication across units good?
2. **Structural and Financial Readiness**:
   * Can the organization make significant structural changes?
   * Are there enough financial resources to support segmentation?
3. **Senior Management Commitment**:
   * Secure visible commitment from senior management.
   * Ensure active involvement of senior management in the analysis.
   * Obtain necessary financial support from senior management.
4. **Team and Training**:
   * Make sure the segmentation concept and implications are understood; conduct training if needed.
   * Form a team of 2-3 people, including marketing and data experts.
   * Set up an advisory committee from all affected units.
5. **Process and Planning**:
   * Ensure clear objectives for the analysis.
   * Develop a structured process for the analysis.
   * Assign responsibilities to team members and ensure enough time for the analysis.

**Step 2: Identifying the Optimal Target Segment**

**2.1 Criteria for Segment Evaluation**

For effective market segmentation analysis, continuous user input is essential. It’s crucial that user involvement occurs throughout the process, not just at the beginning or end, to ensure the analysis is beneficial to the company.

Once a company opts for segmentation (Step 1), substantial contribution from the company in Step 2 is necessary. This involvement influences subsequent steps, particularly Step 3 (data collection) and Step 8 (segment selection). In Step 2, the company needs to establish two sets of criteria for segment evaluation. The first set, known as knock-out criteria, includes essential features a segment must have to be considered. The second set, attractiveness criteria, assesses how appealing the remaining segments are based on the knock-out criteria. Research provides numerous options for these criteria, often presented in various ways without clear separation.

The distinction between these two sets of criteria is important. Knock-out criteria are crucial and non-negotiable, while attractiveness criteria offer a broader range of considerations. The segmentation team uses the attractiveness criteria to evaluate potential segments and prioritize them based on importance. Knock-out criteria automatically eliminate certain segments, whereas attractiveness criteria, selected by the team, help in assessing segment desirability in Step 8.

**2.2 Knock-Out Criteria**

Knock-out criteria serve as an initial filter to determine if market segments can be further evaluated using attractiveness criteria. Kotler (1994) suggested the initial criteria, including substantiality, measurability, and accessibility. Later additions to these criteria include:

* Homogeneity within the segment.
* Distinctiveness from other segments.
* Adequate size.
* Compatibility with the company's strengths.
* Identifiability and reachability of individuals within the segment.

It's crucial for senior managers, the team, and advisors to comprehend these knock-out criteria. Most criteria are straightforward, though some, like segment size, may require detailed specifications.

**2.3 Attractiveness Criteria**

Beyond knock-out criteria, there are numerous segment attractiveness criteria that the segmentation team can select based on their specific needs. Unlike binary knock-out criteria, attractiveness criteria allow segments to be rated on a scale, indicating varying levels of attractiveness. These ratings collectively determine a segment’s suitability as a target in Step 8 of the analysis.

**2.4 Implementing a Structured Evaluation Process**

A structured approach to market segmentation is widely recommended (Lilien and Rangaswamy 2003; McDonald and Dunbar 2012). One effective method is the "segment evaluation plot" (Lilien and Rangaswamy 2003; McDonald and Dunbar 2012), which visualizes segment attractiveness and the company’s competitive position. The team selects relevant factors for attractiveness and competitiveness from numerous options, typically focusing on around six key factors as suggested by McDonald and Dunbar (2012).

A diverse team representing various company divisions should manage the process (McDonald and Dunbar 1995; Karlsson 2015). If a smaller team leads the effort, they should consult with an advisory committee that represents the entire company. This inclusive approach ensures that different perspectives are considered and the strategy impacts all units appropriately. Although the segment plot is not created in Step 2, identifying attractiveness criteria early ensures that crucial information is gathered in Step 3, facilitating segment selection in Step 8.

By the end of this step, the team should finalize approximately six attractiveness criteria, each assigned a weight reflecting its importance. A common practice (Lilien and Rangaswamy 2003; McDonald and Dunbar 2012) is to allocate 100 points across the criteria, which is then discussed and agreed upon. It’s advisable to get approval from the advisory committee, which includes representatives from various company segments to incorporate diverse viewpoints.

**2.5 Step 2 Checklist**

* Convene a meeting with the segmentation team.
* Discuss and finalize knock-out criteria such as homogeneity, distinctness, size, compatibility, identifiability, and reachability. These criteria will lead to the automatic elimination of non-compliant segments (by Step 8 at the latest).
* Present the knock-out criteria to the advisory committee for review and potential adjustments.
* Individually review available criteria for assessing market segment attractiveness.
* Collaborate with the segmentation team to agree on a subset of no more than six attractiveness criteria.
* Individually distribute 100 points among the agreed-upon attractiveness criteria, reflecting their relative importance.
* Discuss and agree on the weightings with the segmentation team.
* Present the selected attractiveness criteria and their proposed weights to the advisory committee for review and potential adjustments.

**Step 3: Collecting Data**

**3.1 Segmentation Variables**

Data is crucial for both commonsense and data-driven market segmentation. The term **segmentation variable** refers to the data characteristic used to divide a market into segments. In commonsense segmentation, a single characteristic, such as gender, is used to split the sample. For example, in Table 5.1, gender is used as the segmentation variable to create separate segments for men and women.

**Descriptor Variables** are additional characteristics used to detail each segment, such as age or vacation preferences. These variables help to describe the segments comprehensively and are essential for tailoring marketing strategies.

In **data-driven market segmentation**, multiple segmentation variables are used. These variables help identify or create market segments based on various attributes. For example, in Table 5.2, benefits sought from vacations are used as segmentation variables, creating segments based on shared preferences rather than demographic characteristics alone.

**Empirical Data** quality is vital for both commonsense and data-driven segmentation. High-quality data ensures accurate segment identification and detailed descriptions, enabling effective marketing mix development.

**Data Sources** can include:

* **Surveys:** Directly collect consumer opinions and behaviors.
* **Observations:** Use scanner data or loyalty programs to track purchase history.
* **Experimental Studies:** Test different scenarios to gather behavioral data.

It is crucial to choose data sources that reflect actual consumer behavior, avoiding reliance on potentially unreliable survey data.

**3.2 Segmentation Criteria**

Before collecting data, organizations must decide on the **segmentation criteria**. These criteria guide the selection of segmentation variables and can include geographic, socio-demographic, psychographic, and behavioral aspects. The choice of criteria affects the segmentation outcome and should be based on relevance and simplicity.

**Geographic Segmentation** uses location-based criteria to form market segments. For example, a national tourism organization might segment tourists by language or region. Geographic segmentation is straightforward and practical but may not always capture relevant product preferences.

**Socio-Demographic Segmentation** uses characteristics such as age, gender, income, and education. This approach is useful in industries like luxury goods or tourism, where socio-demographic factors often correlate with preferences. However, socio-demographic criteria alone may not fully explain consumer behavior, as they often account for only a small portion of behavior variance.

**3.3 Data from Survey Studies**

Surveys are a common method for collecting data. Key considerations include:

* **Choice of Variables**: Select relevant variables that align with your segmentation goals (e.g., demographic, psychographic, behavioral).
* **Response Options**: Design response options carefully to capture accurate and useful data.
* **Response Styles**: Be aware of potential biases in how respondents answer questions and account for them in your analysis.
* **Sample Size**: Ensure the sample size is large and representative enough to provide reliable results.

**3.4 Data from Internal Sources**

Leverage internal data such as customer databases, sales records, and transaction histories. This data reflects real customer interactions and behaviors, offering valuable insights for segmentation.

**3.5 Data from Experimental Studies**

Conduct experiments to observe how changes in variables affect consumer behavior. This approach helps in understanding cause-and-effect relationships and refining segmentation strategies.

**3.6 Step 3 Checklist**

* Convene a market segmentation team meeting.
* Identify potential segmentation variables and descriptor variables.
* Determine data collection methods to capture both segmentation and descriptor variables effectively.
* Design data collection processes to minimize biases and systematic errors.
* Collect and analyze data.