9 Ways Market Segmentation Improves Business Success

Research Rockstar

What is Market Segmentation?

Market segmentation divides a target market into logical subgroups based on some combination of demographic, psychographic, attitudinal or behavioral variables. The resulting model allows an organization to fine-tune its activities and strategies to address specific market opportunities.

The premise of market segmentation is that to maximize sales to a large population of customers, it is best to divide it into logical subgroups. The assumption is that by dividing one large, amorphous mass into subgroups, you can fine-tune your product, messaging, promotional, support, and/or distribution strategies to meet the specific needs of unique customer groups. Thus, the goal is to use market segmentation to optimize marketing ROI.

Segmentation models vary from basic to complex, and the approaches to developing and applying them is a topic for an entire book itself. But here are some examples:

Example 1: A telecommunications company selling mobile phone services might segment its market based on need complexity.
One customer group might only need voice service, and very little volume at that. Another group might primarily use mobile texting services. Yet another might be a heavy user of mobile phones for voice, text, email and web browsing. By identifying distinct patterns in customer needs, the company can optimize product bundles and target them at the correct audiences.

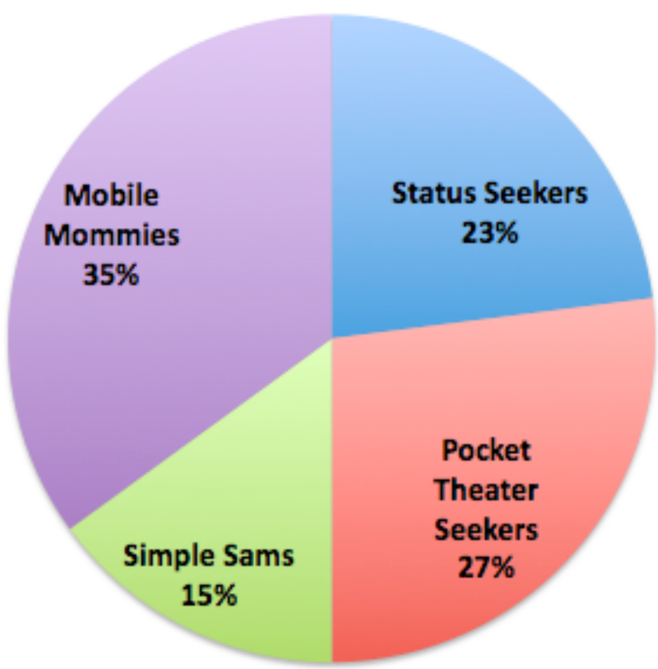
Example 2: A hotel chain that caters to families might segment its market based on continuums of income level and travel frequency. The chain might find that a group of moderate income-frequent travelers exists that is swayed by certain loyalty program rewards. It might find another important group exists that is more swayed by on-site amenities. With this information, the hotel can optimize its offerings and loyalty programs to each group's unique interests.

Example 3: A software company that sells to large enterprises might segment its market by vertical industry. It may find that in its product category, needs and price-sensitivity vary by industry, making it a practical approach.

In reality, segmentation studies are designed to meet different goals. Some of the most common goals are as follows:

- To identify attractive customer groups
- To select sales channels that best reach desirable customer groups
- To custom-tailor marketing messages that will resonate with specific customer groups
- To inform product roadmaps based on customer needs and behaviors
- To assign customers to groups for tactical campaigns

If we then fast-forward to the end of a segmentation project, the result is a segmentation model. The model usually consists of 3 to 7 segments, sometimes more, that can be profiled and sized (see example, below). In some cases, the segments have strong correlations to demographic variables. In others, the segments are distinguished by unique patterns related to purchase behavior, product needs, or brand preferences. In any case, there is usually some basis by which the organization using the model can assess each segment for attractiveness.



A simple example of a model consisting of 4 segments

Are segments the same as "personas"?

A persona is a rich, detailed profile of a person (usually hypothetical) that represents a customer group or market segment. The profile is intended to create insight and empathy towards a specified customer group. Personas help product developers and marketers by having a clear, "human" image of a target customer group's needs and behaviors.

Personas are drawn from ethnographic and qualitative research methods, or from more comprehensive quantitative studies (in some cases, a mix of quantitative and qualitative methods are used). However, the term is sometimes used loosely; some "personas" are not based on research, and in reality may be very anecdotal.

In an ideal world, a market segmentation model is created first, segments are profiled, and *then* representative personas developed. In fact, market researchers have been creating personas for years, though not under that name. Specifically, market researchers presenting a new market segmentation model often "personify" a segment by creating a construct of a person who represents that segment. Usually a name is associated with the segment and the representative persona, such as "Status Seekers," "Mobile Mommies", or "Digital Devotees."

What types of organizations use Market Segmentation?

Short answer? All types.

Consumer marketing companies often use market segmentation models. These models typically use some combination of price sensitivity, brand preferences, behaviors, values and psychographic attributes.

Business-to-business companies increasingly use segmentation. Further, they are becoming more sophisticated in how they do it. Up until about 5 years ago, many B2B segmentation models relied heavily on vertical industry and company size; increasingly, B2B companies are creating needs-based models.

The 9 Benefits

How can market segmentation help my organization be more successful?

Market segmentation models can be designed to meet a wide variety of goals. If executed properly by an organization seeking to pursue customer-centric strategies, market segmentation can lead directly to important money saving and revenue generating opportunities. Following are the nine most common market segmentation benefits.

1. **Achieve differentiation**. How can you make your brand or product stand out in an increasingly noisy marketplace? By identifying, with more originality than your competitors' do, positioning opportunities with specific, attractive customer groups. Resist the temptation to be all-things-to-all-people. Use a segmentation model to identify attractive customer groups, and boldly focus on them. By doing so, you will differentiate your brand from the crowd.

2. **Inform messaging decisions**. Why use generic messages that mimic, or react to, competitors' messages? Informed by a strong segmentation model, organizations can create messages that will truly resonate with specific, selected, customer groups.

   Better still? A segmentation model helps you create new messages on an ongoing basis, sometimes even in response to a changing macro-level environment. If you have selected carefully profiled segments, you can better predict the impact of macro trends—such as a recession—on purchase behavior. You may know that some customer groups react more to a recession than others. Now you can talk to them effectively with current, timely context.

3. **Plan product roadmaps.** It's a lot easier to craft a roadmap when you have internal agreement about the profiles—including needs and behaviors—of the most attractive customer segments. If decision makers share a common view of what the most attractive segments are, and their emerging needs, planning new products and product improvements becomes a far more efficient and cooperative process. And wouldn't that be nice!

4. **Embrace niche marketing**. Few companies can afford to compete with the big fish in the big pond. Instead, a segmentation model shows you how to be a big fish in a little pond—or several little ponds. A segmentation project can be designed to identify, profile and select niches.

5. **Select sales channels.** It's not as easy as it used to be! In many markets, the ratio of direct versus indirect sales is changing. In some categories, intermediaries are losing out to direct, online sales. In other consumer categories, customers are more loyal to the store than the product brand. Optimization of a sales channel strategy amidst all of this upheaval is hard. But an organization that has identified and selected priority customer groups, and examined their purchase behaviors, can make these decisions firmly.
6. **Inform media mix**. One of the biggest marketing expenses for any organization is media. Yet optimizing the mix of advertising on tv, radio, billboards, print, online, via direct mail, and so on often requires a very expensive trial-and-error process. Optimizing the mix of media investments is difficult, and often fraught with painful second-guessing. But with a segmentation model, an organization can optimize for the media behaviors and influence factors of specific customer groups. Perhaps one segment tends to surf the web while watching television. Perhaps another is very coupon-centric. Perhaps in a B2B case, a segment exists that is highly influenced by third party thought leaders. All of these examples give concrete pointers to effective media strategies.
7. **Optimize your marketing budget**. Hey, if you can afford to advertise like Proctor & Gamble, great! But for the rest of us, a more selective approach is necessary. As already described, segmentation optimizes marketing spend by A) allowing you to focus on the most attractive segments (so you aren't wasting money on "bad" segments), and B) informing what marketing investments to make that will be most effective for the attractive groups. But the model can also help you to set the budget itself and optimize it on an ongoing basis:
    a. **Setting your budget**. Instead of letting a marketing budget be set by something arbitrary—such as percent of sales—a segmentation model can provide an objective guide. Given the size of attractive segments, and objectives for each segment (awareness/preference/market share, etc.), a *strategic* budget aligned with actual goals can be built.
    b. **Optimizing the budget**. With a segmentation model, new, precise metrics are possible. Now you can analyze effectiveness of marketing investments *by customer segment*. The marketing budget can be evaluated and fine-tuned based on actual results by groups *precise enough to effectively measured*.
8. **Improve brand management**. With known, profiled customer segments, brand awareness and perceptions can be measured in total, and by those groups of greatest interest. Tactics for improving brand awareness and perceptions are far easier to identify and test for efficacy when done by more narrow customer groups.

9. **Deploy customer retention strategies**. When it comes to customer retention, some strategies are obviously universal. All customer-centric companies seek to keep customer satisfied, be responsive to support requests, honor promises and warrantees. But what else is there? A segmentation study that includes analysis of *current* customers can identify options for satisfiers. Is it possible that some groups are more likely to remain loyal based on different experiences with your brand? Maybe one group exists that is more likely to repurchase if they have a loyalty program. Perhaps another group is more swayed if they feel listened to or otherwise valued.

Practically speaking, a single market segmentation study cannot deliver all nine of these benefits. But a single study can be designed to accomplish 2 or 3 of these items; then, subsequent studies can build on the selected model, adding new dimensions and details.

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