



Customer Segmentation: Is It Improving Your Bottom Line?

Customer segmentation, an often misused buzz word in the business vocabulary, is the process of dividing customers with similar attributes into homogeneous groups and targeting those homogeneous groups differently. This process has the potential to affect various choices from what products to sell to whom, where and when and how to market and sell the products. The first question you may ask is: Should a business segment its market into homogeneous groups of customers to better serve their customers and improve profitability?

The answer is simply yes, but the complexity and its success is in how the segmentation is conducted. Segmentation is necessary to effectively target customers. I will assume as a starting point that we all agree that focus is very important for businesses given the need to utilize limited resources in a world of resource constraints. Therefore by defining which customers to target and how to effectively do this by targeting their common attributes, we are leveraging and focusing resources in an optimal way. Others have argued that advances in technology have made segmentation less important, as businesses can market to segments of one i.e. personalize their message and in some cases even the product to meet each individual customer's needs. An example of this is Nike and the option for consumers to customize their athletic shoes on their web site prior to purchase. One (the business) to one (an individual customer) marketing, a service that can be offered through the Internet, has to be carefully analyzed for cost considerations since it is not a volume driven business model and the merit of each case needs to be analyzed relative to the individual customer segment desires.

Our experience in the consumer and business customer markets has proven that customer segmentation can be extremely powerful if done correctly. The effect on profitability is significant as a result of the "double whammy" effect – firstly the increase in revenue from a more targeted marketing approach and secondly from the saving in costs as a result of the more focused and efficient use of human and other marketing assets within the business.

If the benefits are so significant, why are companies not taking advantage of this through a more effective segmentation approach and process?

Although many companies have bought into the concept of customer segmentation their analysis of those markets and their implementation is not clear and effective – their delivery is poor. Traditional segmentation schemes are not very useful for a number of reasons:

1. The groups that are created are too broad to be truly distinct. For example, in **business customer** markets companies often **segment their customers based on size**, for example small, medium and large segmentation schemes with minor variations on the theme e.g. by specialty etc. In **consumer markets a significant focus is placed on**

demographics such as age, income, geography with little emphasis on other factors.

2. These segmentation schemes, although actionable, often **do not effectively cater for the psychological and behavioral attributes** that drive customers to act the way they do and therefore cannot cater to the customers' motivations. Where pseudo-psychographic variables are used (e.g. lifestyle), they are often too superficial and lack insight to deliver real results.
3. The segmentation is **not properly integrated into the sales and marketing** function to create differentiated messages and campaigns that effectively target the customer segments differently and effectively.

The key areas and questions are:

On which customer segments should the company focus?

- What are the truly distinct customer groups and segments? What are the demographic, psychographic and behavioral segmentation variables?
- Which of these truly distinct segments are most attractive? Attractiveness comprises various dimensions such as:
 - The size and profitability of the customer segment?
 - The strategic importance of that segment to the company's business currently and in the future
 - The competitive dynamics in that customer segment – who is serving them and how are they being served (current and future)
 - The potential for the company's products / services to meet the needs of that customer segment relative to current and potential competitor products and services - can the company create a sustainable competitive advantage?

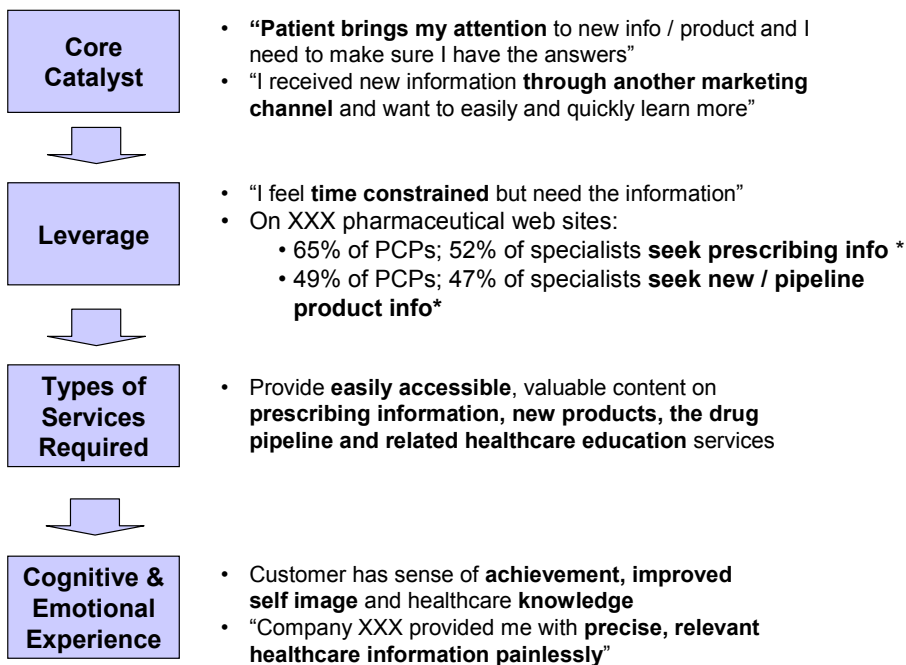
How will the company succeed in serving these customer segments?

- Understand the target customer segments and what influences their actions?
 - What are the core catalysts that drive the segment to buy a service or product – these can be practical (e.g. "My old pair of shoes have worn out and I need a new pair") and/or emotional (e.g. "Buying a new pair of shoes fulfills an emotional need of") and they need to be clearly understood and defined in detail in each of the target customer segments
 - What is the leverage that the company can use to meet the core catalyst and serve the customers' needs. The leverage is defined as the target customer's actions, views and behavioral responses that the customer exhibits when purchasing and using the product or service and that the company can leverage in order to appeal to that customer segment.
 - Define the service and value provided to the customer group to address the areas of leverage and what effect it has on the customer groups' emotional and cognitive experience? This experience can then be translated into a value proposition for the company.

- Create marketing messages and tactics to deliver on the strategy. What are the visual and psychological profiles of the target customer segments that would be used to tailor messages to address the customer group’s core catalysts and leverage points?
- How do you translate this visual and psychological profile into tangible, clear actions for the sales force that they could use to activate the customer?

Summary Outline of the Link between the Core Catalyst, Leverage, Service / Value Provided to the Customer and the Customer’s Experience

Example: A physician that uses the Internet to find specific pharmaceutical information



Source: Overview example from pharmaceutical client – sanitized to protect confidentiality, * Research data

What type of process should be used to achieve this?

We believe that the best approach **combines organizational psychology and competitive business strategy techniques** to segment the market based on demographic, psychological and behavioral attributes of the customer in order to create distinct and useful groups.

This would include a review and analysis of existing segmentation schemes and data to create hypotheses of segmentation variables to test. Through one on one interviews and/or focus groups test the segmentation variables and gain a detailed insight into customers’ motivations by analyzing their buying and selling (where appropriate) processes. Statistically analyze (where appropriate) relationships to assess the correlation and the most effective segmentation variables. Create a segmentation scheme that is useful and creates homogeneous groups of customers that can be effectively and efficiently targeted.

Once this is completed the company needs to select the target customer segments based on attractiveness criteria and identify the core catalysts and leverage points that can be used to

influence the customer segment to purchase the company's products and services and define specific value added services, messaging and tactics to address their needs.

Customer segmentation can be a powerful tool, if used correctly, to improve the bottom line but companies do need to be fully committed to the process and approach it in a systematic, integrated and practical manner, selecting the most attractive target segments, catering for and providing marketing messages that address their real needs and behaviors.