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—A tune-up from experts in market-focused strategy



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## Segmentation: Matching Resources to Opportunities

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### Key Points:

- Segmentation is the process of organizing a market into distinct groups of customers with similar wants and similar value systems.
- There are at least 3 bases of segmentation: outward or identifying characteristics, wants (or benefits sought), and behavior and attitudes toward suppliers.
- Segmentation can: help you leverage your strengths; promote customer loyalty; prevent you from trying to be “all things to all people.”
- To segment markets begin with the question: *What do customers want?* Then ask: *Are there differences among customers in terms of what they want?*
- Segmentation is always relevant when customers respond differently to various mixes of product, price, promotion, distribution, or service.
- Needs-based segmentation schemes, although more difficult to develop than schemes based on such outward, identifying characteristics as location or demographics, will provide you with greater insight into how you might appeal to your customers.

Peter Drucker suggests that every organization has two basic functions: marketing and innovation. At the heart of marketing is segmentation, a critical element in matching resources to opportunities.

Customers have distinct and differing needs, wants, preferences, and buying patterns. Segmentation provides a means of revealing and capitalizing on the opportunities represented by these differences.

### What Is Segmentation?

The process of organizing a market into distinct groups of customers where there are similarities within each group but clear differences among groups.

There are many ways you might organize your customers. For example, you could segment markets based on:

- customers’ outward characteristics: size, geographic location, type of organization
- your product’s characteristics: distribution, price or image
- the differences among your customers in terms of needs, wants and preferences such as their preferred relationship with suppliers, their service requirements, or the specific benefits they derive from the use of your product or service.

### Why Segment?

Segmentation is challenging. Effective ways to segment markets are rarely obvious. Research alone won’t do the trick. You need an in-depth understanding of markets and customers’ needs, wants and preferences.

Still, the task is well worth the effort, offering you at least three important advantages.

1. Helps you focus finite resources on opportunities that best match your capabilities.
2. Encourages customer loyalty, since your offering can be geared closely to customers’ preferences.
3. Finally, since few organizations are capable of delivering all benefits sought by customers, segmentation can let you concentrate your strengths, preventing you from trying to be “all things to all people.”

### How to Segment

Start by asking yourself this question: Do all of our customers want the same thing in terms of product, price, distribution, or service? Probably not! Okay, then what *do* customers want? Answers to this second question will get you started on preparing a list of wants that you can use to differentiate customers.

Once you have hypotheses about what customers seek, use market research to corroborate and amplify your intuitions. Although the more quantitative aspects of research are best left to professionals, it can be of great value to do some research yourself. For example, direct observation of how and why your customers use your products.

## Perfection Is Your Enemy

The process is never perfect. Differences in needs or wants are subjective and not easy to discern. Segment boundaries are often fuzzy. However, don't let this stop you from striving to understand your customers and to segment your markets.

Segmentation is always relevant when customers respond differently to various mixes of product, price, promotion, distribution, or service. Whether the scheme you come up with is perfect or not isn't the issue. "Close enough" is good enough! Segmentation, when based on solid information about what customers seek, is a "fault-tolerant" and relatively low-risk proposition.

## The Power of Multiple Dimensions

Segmentation schemes built on a single criterion or dimension are good first starts at dividing up markets. On the other hand, such "linear" schemes often fail to capture important behavioral and attitudinal differences among customers.

For example, in business-to-business markets, within the extensive range of customers' wants that you might consider, you may find differences in the kinds of relationships customers seek with suppliers. Differences may also be found in their attitudes toward the application or use of the product that they purchase from you and others. If there is little correlation between such preferences and attitudes, a segmentation scheme based on these variables can differentiate among customers as illustrated in the following example:

Customer's preferred relationship with suppliers	Collegial	<i>(Customers in this segment seek a closer relationship with their suppliers but tend to view the product supplied as a "last resort" addition to their offering, used only when necessary.)</i>	<i>(Customers in this segment seek a closer relationship with their suppliers and view the type of product offered as strategically important to the success of their business.)</i>
	Adversarial	<i>(Customers in this segment choose to deal at arm's length with their suppliers and use the product category only when absolutely required, if and when "forced" by their customers.)</i>	<i>(Customers in this segment tend to view their suppliers as "interchangeable" but view the product category offered by suppliers as of great importance to their business.)</i>
		Necessary evil	Strategically important
Customer's attitude toward supplier's product category			

Generally, segmenting on the basis of attitude and behavior will be more difficult for you to do, but will be of potentially greater value by providing you with insight into how you might appeal to your customers.

### Doing a Better Job of Segmenting

What can you do to improve how you segment your markets? Some suggestions:

1. Keep in mind that promising ways to segment markets are rarely obvious.
2. Also keep in mind that segmentation is a creative as well as analytical process. There are literally hundreds of ways to segment a market.
3. Use intuition as a starting point, then corroborate and improve your initial hypotheses with qualitative and quantitative research.
4. Knowledge of customers is critical. Creativity along with solid information about customer wants is also necessary.
5. To capture important attitudinal and behavioral differences among customers, use two-dimensional rather than linear models. This can help you develop more precise segment boundaries.
6. Focus on the benefits sought by customers, a highly useful segmentation variable, since this in turn can help you develop your value propositions.



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