grasp

… a tasty segmentation

For many products and services, mass marketing is becoming a contradiction in terms. Segmentation is an opportunity for every business to focus on what they do best: what strategically delivers the most cash profit. So how should we be thinking of and talking to our customers and end-users?

What is it?

> *"Market segmentation is among the most powerful weapons in the marketing arsenal. Competitors leave themselves open to crippling attack when their products or services lump together groups of customers with different needs that are better met by different value propositions. Identifying segments where others see an undifferentiated mass market creates opportunities for innovations based on meeting specific customers' needs more precisely."* (Raynor & Weinberg, 2004).

It is a measure of how far we have come that the statement "different customers have different needs" now sounds facile! When Henry Ford said his customers could **have a Model T in any colour as long as it was black**, it was a means to an end: to reduce prices to a point where his products were available to new markets. **The Ford Focus is now available in nearly 5,000 "standard" combinations** of body shape, engine, gearbox, colour and options (including a £15 "smokers pack").

Tesco have been arguably the most successful segmenter in UK business history. Their rapid tiering of product ranges into "good, better and best" (Value, core – including "healthy living"/Cherokee etc – and *Finest**) has allowed them to be all things to all people. The actual complexity of how people relate to these products is characterised by the upmarket Tesco shoppers who buy Value tissues but wouldn't use them for anything other than wiping the windscreen of their 4x4s!

The principle of segmentation is to usefully identify groups of customers based upon their needs, and then strategically decide which segments you are going to serve and which you are not. To do this usefully the **segmentation must offer benefits (profits!) to the organisation undertaking it**, the resulting segments should:

1. **Present a big enough opportunity to be communicated with profitably**

2. **Be accessible via cost-effective communication.**

Segmentation has to be based upon the data that can be made available. The breadth of data used can cause issues where the ideal range of data is not available, or where valuable criteria are overlooked at the data gathering stage. "Artificial" (inaccurate) segments can result in these instances but can – on a judgement call – still be valuable as a first stage segmentation, subject to future refinement when better data is available.

Making segmentation dynamic is key to its long-term success. The accuracy and desirability of your segmentation will change over time, as your business and your marketplace changes. Even more important, a steady approach to segmentation enables individual segments to be approached and the Return on Investment measured. In this way the whole process can be evaluated:

- The effectiveness of indirect costs (eg management time),
- The accuracy of the segmentation,
- The effectiveness of the direct costs (eg communication) and
- The ultimate desirability of new customers.

Why invest in it?

How valuable each customer is to you is a vital part of segmentation (and is inextricably linked to how valuable you are to them)! The point of segmentation is to drive profitability. Research clearly shows that **just because some customers are cheap to find doesn't mean that they are profitable** (Thomas et al, 2004). Correlating acquisition cost against retention cost, low maintenance customers can be some of the most expensive to acquire but typically make up 15% of the customer base yielding 40% of an organisations profits!

The *lifetime value* of a retained low maintenance customer far outstrips that of others. **Finding and keeping the right customers by investing in segmentation can be very rewarding**.

It is important for any organisation to consider the segmentation of the broader market (rather than just current customers). Segmentation of current customers is likely to reveal less profitable segments – such as customers with unprofitably high maintenance costs – that the business wishes to trade up or trade out of. These customers need to be replaced by prospects that are likely to be more profitable.

Even if you are happy with the performance of your current business, you may wish to undertake segmentation to inform launches into new markets.

How should we go about it?

Segmentation can be undertaken using internal data (existing customer records) and external data (prospects). Internal data is generally easier to secure but can still be surprisingly time-consuming to collate, clean and enhance. An objective outside agency (like grasp) can help collate and assess this information. The more that is known, the better:

- **Who are your customers, where are they** … if they are **businesses** – how big are they (employees/turnover/brand), which "industrial" sector do they operate in? … If they are **shoppers/consumers** – what are their demographics, how do they behave, what benefits are they looking for, what attitudes do they hold?

- **Purchasing history**: How often do your customers purchase, when did they last buy, how long have they been a customer? What products/services does each customer buy, what level of spend do they display across these products?

- **What is the profitability of each customer account** (what are the drivers of profit within each one) what is the trend for each customer?

Two further lines of enquiry that are likely to be much less readily available (but can be extremely useful) are:

- **What do you know about your customers' interaction with your competitors**?

- **What specific criteria are important to your customer in doing their job / living their lives**? (eg Are they predominantly price-driven, are there specific criteria where they want to see the game raised?)

These last two strands of information and insight can be gleaned through bespoke research and can be done confidentially by grasp.

If you ask the right questions, some answers can be surprising: how many of your customers would like regular face-to-face interaction, how many would much rather only deal with you over the internet? Some high street banks were surprised by their customers' answers:

- First Direct has arguably been even more successful on the web than it has been on the phone

- The fall of bricks-and-mortar banking in the UK has been abated by the value of local branches to key customer segments (large numbers of small businesses and heavy users of cash).

Summary

With many businesses facing consolidation in their sectors, and those of their customers / suppliers, segmentation is a solid response to these trends.

Rather than trying to match the economies of scale of market leaders, smaller businesses are better off being different: serving different customers, and understanding the value their businesses can uniquely add to their best customers (and their hottest prospects).

References

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