

Chapter 4

Step 2: Specifying the Ideal Target Segment



4.1 Segment Evaluation Criteria

The third layer of market segmentation analysis (illustrated in Fig. 2.1) depends primarily on user input. It is important to understand that – for a market segmentation analysis to produce results that are useful to an organisation – user input cannot be limited to either a briefing at the start of the process, or the development of a marketing mix at the end. Rather, the user needs to be involved in most stages, literally wrapping around the technical aspects of market segmentation analysis.

After having committed to investigating the value of a segmentation strategy in Step 1, the organisation has to make a major contribution to market segmentation analysis in Step 2. While this contribution is conceptual in nature, it guides many of the following steps, most critically Step 3 (data collection) and Step 8 (selecting one or more target segments). In Step 2 the organisation must determine two sets of segment evaluation criteria. One set of evaluation criteria can be referred to as *knock-out criteria*. These criteria are the essential, non-negotiable features of segments that the organisation would consider targeting. The second set of evaluation criteria can be referred to as *attractiveness criteria*. These criteria are used to evaluate the relative attractiveness of the remaining market segments – those in compliance with the knock-out criteria.

The literature does not generally distinguish between these two kinds of criteria. Instead, the literature proposes a wide array of possible segment evaluation criteria and describes them at different levels of detail. Table 4.1 contains a selection of proposed criteria.

Table 4.1 Criteria proposed in the literature for the evaluation of market segments in chronological order. (Modified from Karlsson 2015)

Source	Evaluation criteria
Day (1984)	Measurable, Substantial, Accessible, Sufficiently different, At suitable life-cycle stage
Croft (1994)	Large enough, Growing, Competitively advantageous, Profitable, Likely technological changes, Sensitivity to price, Barriers to entry, Buyer or supplier bargaining power, Socio-political considerations, Cyclicalities and seasonality, Life-cycle position
Myers (1996)	Large enough, Distinguishable, Accessible, Compatible with company
Wedel and Kamakura (2000)	Identifiable, Substantial, Accessible, Responsive, Stable, Actionable
Perreault Jr and McCarthy (2002)	Substantial, Operational, Heterogeneous between, Homogeneous within
Lilien and Rangaswamy (2003)	Large enough (market potential, current market penetration), Growing (past growth forecasts of technology change), Competitively advantageous (barriers to entry, barriers to exit, position of competitors), Segment saturation (gaps in marketing), Protectable (patentable products, barriers to entry), Environmentally risky (economic, political, and technological change), Fit (coherence with company's strengths and image), Relationships with other segments (synergy, cost interactions, image transfers, cannibalisation), Profitable (entry costs, margin levels, return on investment)
McDonald and Dunbar (2004)	Segment factors (size, growth rate per year, sensitivity to price, service features and external factors, cyclicalities, seasonality, bargaining power of upstream suppliers), Competition (types of competition, degree of concentration, changes in type and mix, entries and exits, changes in share, substitution by new technology, degrees and type of integration), Financial and economic factors (contribution margins, capacity utilisation, leveraging factors, such as experience and economies of scale, barriers to entry, or exit), Technological factors (maturity and volatility, complexity, differentiation, patents and copyrights, manufacturing processes), Socio-political factors (social attitudes and trends, laws and government agency regulations, influence with pressure groups and government representatives, human factors, such as unionisation and community acceptance)
Dibb and Simkin (2008)	Homogeneous, Large enough, Profitable, Stable, Accessible, Compatible, Actionable
Sternthal and Tybout (2001)	Influence of company's current position in the market on growth opportunities, Competitor's ability and motivation to retaliate, Competence and resources, Segments that will prefer the value that can be created by the firm over current market offerings, Consumer motivation and goals indicating gaps in marketplace offerings when launching a new company
West et al. (2010)	Large enough, Sufficient purchasing power, Characteristics of the segment, Reachable, Able to serve segment effectively, Distinct, Targetable with marketing programs
Solomon et al. (2011)	Differentiable, Measurable, Substantial, Accessible, Actionable

(continued)

Table 4.1 (continued)

Winer and Dhar (2011)	Parsimonious, Large enough, Growing, Competitively advantageous
Jain (2012)	Measurable, Accessible, Substantial, Develops maximum differential in competitive strategy, Preserves competitive advantage, Valid even though imitated
Kotler and Keller (2012)	Measurable, Substantial, Accessible, Differentiable, Actionable, Segment rivalry (competition), Potential entrants, Substitutes, Power of buyers, Power of suppliers, Compatible with company
Pride et al. (2012)	Sales estimates (potential sales for product item, product line, geographical area in the short, medium or long term), Competitive assessment, Cost estimates, Long-term profit opportunities, Financial resources, Managerial skills, Employee expertise, Facilities to compete effectively, Fit with corporate objectives, Legal issues, Conflicts with stakeholders, Technological advances
Sharp (2013)	Measurable, Targetable, Large enough, Profitable

In Sects. 4.2 and 4.3, these criteria are discussed under two separate headings to reflect the difference in nature. The shorter set of knock-out criteria is *essential*. It is not up to the segmentation team to negotiate the extent to which they matter in target segment selection. The second, much longer and much more diverse set of attractiveness criteria represents a shopping list for the segmentation team. Members of the segmentation team need to select which of these criteria they want to use to determine how attractive potential target segments are. The segmentation team also needs to assess the relative importance of each attractiveness criterion to the organisation. Where knock-out criteria automatically eliminate some of the available market segments, attractiveness criteria are first negotiated by the team, and then applied to determine the overall relative attractiveness of each market segment in Step 8.

4.2 Knock-Out Criteria

Knock-out criteria are used to determine if market segments resulting from the market segmentation analysis qualify to be assessed using segment attractiveness criteria. The first set of such criteria was suggested by Kotler (1994) and includes substantiality, measurability and accessibility (Tynan and Drayton 1987). Kotler himself and a number of other authors have since recommended additional criteria that fall into the knock-out criterion category (Wedel and Kamakura 2000; Lilien and Rangaswamy 2003; McDonald and Dunbar 2012):

- The segment must be **homogeneous**; members of the segment must be similar to one another.
- The segment must be **distinct**; members of the segment must be distinctly different from members of other segments.

- The segment must be **large enough**; the segment must contain enough consumers to make it worthwhile to spend extra money on customising the marketing mix for them.
- The segment must be **matching** the strengths of the organisation; the organisation must have the capability to satisfy segment members' needs.
- Members of the segment must be **identifiable**; it must be possible to spot them in the marketplace.
- The segment must be **reachable**; there has to be a way to get in touch with members of the segment in order to make the customised marketing mix accessible to them.

Knock-out criteria must be understood by senior management, the segmentation team, and the advisory committee. Most of them do not require further specification, but some do. For example, while size is non-negotiable, the exact minimum viable target segment size needs to be specified.

4.3 Attractiveness Criteria

In addition to the knock-out criteria, Table 4.1 also lists a wide range of segment attractiveness criteria available to the segmentation team to consider when deciding which attractiveness criteria are most useful to their specific situation.

Attractiveness criteria are not binary in nature. Segments are not assessed as either complying or not complying with attractiveness criteria. Rather, each market segment is rated; it can be more or less attractive with respect to a specific criterion. The attractiveness across all criteria determines whether a market segment is selected as a target segment in Step 8 of market segmentation analysis.

4.4 Implementing a Structured Process

There is general agreement in the segmentation literature, that following a structured process when assessing market segments is beneficial (Lilien and Rangaswamy 2003; McDonald and Dunbar 2012).

The most popular structured approach for evaluating market segments in view of selecting them as target markets is the use of a segment evaluation plot (Lilien and Rangaswamy 2003; McDonald and Dunbar 2012) showing segment attractiveness along one axis, and organisational competitiveness on the other axis (for an example

see Fig. 10.1). The segment attractiveness and organisational competitiveness values are determined by the segmentation team. This is necessary because there is no standard set of criteria that could be used by all organisations.

Factors which constitute both segment attractiveness and organisational competitiveness need to be negotiated and agreed upon. To achieve this, a large number of possible criteria has to be investigated before agreement is reached on which criteria are most important for the organisation. McDonald and Dunbar (2012) recommend to use no more than six factors as the basis for calculating these criteria.

Optimally, this task should be completed by a team of people (McDonald and Dunbar 1995; Karlsson 2015). If a core team of two to three people is primarily in charge of market segmentation analysis, this team could propose an initial solution and report their choices to the advisory committee – which consists of representatives of all organisational units – for discussion and possible modification. There are at least two good reasons to include in this process representatives from a wide range of organisational units. First, each organisational unit has a different perspective on the business of the organisation. As a consequence, members of these units bring different positions to the deliberations. Secondly, if the segmentation strategy is implemented, it will affect every single unit of the organisation. Consequently, all units are key stakeholders of market segmentation analysis.

Back to the segment evaluation plot. Obviously the segment evaluation plot cannot be completed in Step 2 of the market segmentation analysis because – at this point – no segments are available to assess yet. But there is a huge benefit in selecting the attractiveness criteria for market segments at this early stage in the process: knowing precisely what it is about market segments that matters to the organisation ensures that all of this information is captured when collecting data (Step 3). It also makes the task of selecting a target segment in Step 8 much easier because the groundwork is laid before the actual segments are on the table.

At the end of this step, the market segmentation team should have a list of approximately six segment attractiveness criteria. Each of these criteria should have a weight attached to it to indicate how important it is to the organisation compared to the other criteria. The typical approach to weighting (Lilien and Rangaswamy 2003; McDonald and Dunbar 2012) is to ask all team members to distribute 100 points across the segmentation criteria. These allocations then have to be negotiated until agreement is reached. Optimally, approval by the advisory committee should be sought because the advisory committee contains representatives from multiple organisational units bringing a range of different perspectives to the challenge of specifying segment attractiveness criteria.

4.5 Step 2 Checklist

Task	Who is responsible?	Completed?
Convene a segmentation team meeting.		<input type="checkbox"/>
Discuss and agree on the knock-out criteria of homogeneity, distinctness, size, match, identifiability and reachability. These knock-out criteria will lead to the automatic elimination of market segments which do not comply (in Step 8 at the latest).		<input type="checkbox"/>
Present the knock-out criteria to the advisory committee for discussion and (if required) adjustment.		<input type="checkbox"/>
Individually study available criteria for the assessment of market segment attractiveness.		<input type="checkbox"/>
Discuss the criteria with the other segmentation team members and agree on a subset of no more than six criteria.		<input type="checkbox"/>
Individually distribute 100 points across the segment attractiveness criteria you have agreed upon with the segmentation team. Distribute them in a way that reflects the relative importance of each attractiveness criterion.		<input type="checkbox"/>
Discuss weightings with other segmentation team members and agree on a weighting.		<input type="checkbox"/>
Present the selected segment attractiveness criteria and the proposed weights assigned to each of them to the advisory committee for discussion and (if required) adjustment.		<input type="checkbox"/>

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