

CHAPTER 2

IDENTIFYING MARKET SEGMENTS AND SELECTING TARGETS

ALICE M. TYBOUT and KENT GRAYSON

INTRODUCTION

The Hyatt hotel chain offers a variety of brands in order to serve different types of travelers and use occasions. Park Hyatt properties are designed for affluent, individual business travelers who desire elegant, contemporary luxury and attentive, personalized service. These properties, which are found in major cities around the world, feature high-end art collections in the public spaces and award-winning chefs in the kitchens of the restaurants. Hyatt Regency properties cater to a somewhat less elite traveler and, accordingly, offer more modest furnishings and food. A subset of Park Hyatt and Hyatt Regency properties are sub-branded as “resorts,” conveying that these properties are tailored to travelers who seek a full-fledged vacation rather than a short-term stay for business or leisure. Hyatt Summerfield Suites were developed to address the needs of business travelers on extended assignments. These suites resemble furnished condominiums, providing everything the traveler might need to prepare meals, relax, and socialize.

Hyatt recently launched yet another brand, Hyatt Place. These properties were developed in response to market research that identified an emerging segment of travelers who live a 24/7 technology-enhanced lifestyle that blurs the distinction between work and leisure. They work at home while listening to music or keeping one eye on the television, and they view their time on the road as an opportunity for both work and personal growth and relaxation.

Hyatt Place addresses the needs of these travelers by offering a casual hospitality similar to what travelers might experience at home. Rooms include a living area with a sofa-sleeper, a 42-inch flat panel, high-definition television with access to a wide range of channels, a plug panel that enables guests to connect their own entertainment media to the high-definition TV, and free Wi-Fi access. Common areas, such as the wine café, bakery, and TV den, allow guests to socialize, while the StayFit@Hyatt gym enables guests to maintain their fitness regimen.

However, despite its many brands, Hyatt does not attempt to address the needs of all travelers and use occasions. There are no Hyatt properties for the traveler who merely wants a basic room at a bargain-basement price.

Hyatt's strategy illustrates two key elements of marketing planning: *Segmentation* and *targeting*. Segmentation involves dividing the market of potential customers into homogeneous subgroups. These subgroups may be distinguished in terms of behavior patterns, attitudes, demographic characteristics, psychographic profile, and the like. Targeting then involves selecting those subgroups whose needs the firm has the capability of addressing and designing offerings in accord with those needs. Although it is relatively easy to identify examples of successful segmentation and targeting, such as that done by Hyatt, many managers find undertaking these tasks for their own products and services daunting. One reason is that the list of potential ways to segment a market is seemingly endless, making it difficult to decide where to begin. Further, once the segmentation analysis is complete, many or even all of the subgroups may appear to be attractive targets, making it difficult to set priorities for allocating resources.

The goal of this chapter is to address the challenges of segmentation and targeting by offering a *strategic* approach that begins with a focus on patterns of usage. This approach may be particularly valuable to companies that are just beginning to embrace segmentation and targeting. It also may be helpful to companies that are experienced at these tasks and are seeking a fresh approach. Customers are grouped according to category use, brand use, and perhaps also the frequency, occasion, and purpose of use of either the category or brand. The resulting subgroups are then characterized in terms of other factors, such as demographics, geographic location, attitudes, and lifestyle—factors that both distinguish between the groups and that are relevant to marketing decisions. Once segmentation is complete, targets are selected by prioritizing the subgroup(s) whose needs can be better served by the company versus its competitors. Before turning to the details of how to segment and target, we briefly consider the question of whether segmentation is necessary at all.

WHY SEGMENT?

For marketers, segmentation is usually considered to be the strategy of last resort. Managers would rather attract a single, large universe of potential buyers than partition the market into subgroups and target one or several of these subgroups. Occasionally, if consumer preferences are sufficiently homogeneous, it is possible to appeal to nearly everyone in a particular market (see later discussion of “mass marketing”). For example, Arm & Hammer has been able to pursue all potential baking soda users due to a lack of competition as well as a lack of variation in customer preferences.

When a new product or service category is created, customers may have little choice but to accept a “one-size-fits-all” offering from the category pioneer. However, if the market offers attractive margins as well as low barriers to entry, competitors are likely to enter and differentiate from the pioneer by providing offerings that are more closely aligned with the preferences of some subgroup of customers. For example, Apple’s entry into the personal computer market with an operating system that was more user-friendly and intuitive than IBM’s effectively segmented a universal market into two types of customers: those who preferred Macs that were easy to use versus those who preferred PCs that were “safe” because they were the industry standard. Likewise, the introduction of personal digital assistants (PDAs) based on Microsoft’s operating system segmented the market previously dominated by Palm’s PalmPilot. The market segmented to include customers who wanted a PDA that integrated seamlessly with enterprise PC software and those who were drawn to the elegant simplicity and ease of use of the PalmPilot.

Although it may seem counterintuitive, segmenting the market and tailoring the marketing strategy to a subgroup of potential customers may prove to be more profitable than attracting a broader customer base. The experience of Yorkie candy bar in the United Kingdom is a case in point. The Yorkie bar is a calorie-heavy “meal replacement” that features blue-collar men in its advertising. Nevertheless, historically 40 percent of Yorkie’s sales were to women who were also interested in meal replacement. When research revealed that women were becoming more concerned about calories, and Yorkie’s main competitor showed signs of targeting women, Yorkie chose to sharpen its focus on men, positioning the product in its advertising as “not for girls.” Although the campaign may have alienated some female customers, it energized the targeted male customers and resulted in a net sales increase.

As implied by the Yorkie example, segmentation and targeting go hand-in-hand with positioning, the topic of Chapter 4, “Developing a Compelling Brand Positioning.” A successful segmentation strategy is one that yields a

target(s) for which the firm can develop a compelling positioning and meet its growth goals. If the strategy for a product involves trying to attract two distinct customer segments with two different needs, efforts to appeal to both segments with a single positioning are likely to fail because they will not be optimal for either segment. Sometimes this problem can be solved by adopting different positioning strategies to different segments. However, when the positioning is conveyed by using media seen by both segments, this may create confusion or alienate core customers.

Consider Eastern Mountain Sports (EMS), an outdoor apparel and equipment retailer in the northeastern United States. EMS discovered that its products appealed not only to its intended target—people who are passionate about the outdoors and who purchase clothing and gear to help them live their passion—but also to people who simply liked outdoorsy clothing. However, when the company adjusted its product line and advertising in an effort to embrace both segments, it ran into trouble. The outdoor enthusiasts interpreted the move as a reduced commitment to serving their needs. Rather than risk alienating its profitable core customer base, EMS quickly reverted to focusing on serving the needs of the outdoor enthusiast.

Because customer preferences for products and services in most categories are heterogeneous, firms often find it difficult to attract everyone with a single marketing program. This is where segmenting becomes important, allowing a company to tailor marketing efforts toward subgroups of consumers who are likely to be most responsive to their offerings, resulting in maximized profits.

THE EVOLUTION OF APPROACHES TO SEGMENTATION

Firms have not always focused on market segmentation and targeting. In the United States immediately following World War II, conditions enabled companies to adopt what is sometimes called a “mass marketing” approach, emphasizing what people had in common rather than how they differed. Men returned from war, married, and began families, creating the Baby Boom. Many took advantage of the GI Bill to attend college, which they combined with new skills learned during the war to fuel upward mobility and create a large middle class. The U.S. government’s investment in infrastructure projects such as highways enabled these middle-class households to live in suburban communities, where they shared experiences not only in their personal lives but also in the lives they experienced vicariously through the newly affordable radios and televisions (which offered a limited range of programming). These

factors resulted in a large market of customers whose needs and preferences were relatively homogeneous and who could be efficiently reached through network programming. In the 1960s an advertiser could reach 80 percent of U.S. women with a spot aired simultaneously on CBS, NBC, and ABC.

At that time, companies' capabilities were well-matched to serving the needs of such a market. Recent innovations in manufacturing enabled firms to produce large quantities of the same product cost-effectively; commercials inserted in radio and network television programming provided an efficient way to reach consumers and tout the benefits of these products. New, large-scale retailers emerged to serve the needs of suburban communities and provided an efficient means for producers to distribute their goods. Thus, U.S. companies enjoyed the luxury of appealing to most consumers by focusing on what they had in common rather than how they differed.

Since that time, many developed markets have become more differentiated and fragmented. Some marketing managers still focus on important similarities among these fragments in an effort to identify a target segment that is large and inclusive. Walmart focuses on low prices and good value—a benefit that is attractive to downscale and upscale consumers alike, and one that encourages more than a third of U.S. consumers to shop at the store each week. The 100 million weekly Walmart shoppers are often further segmented on dimensions such as life stage and attitudes. However, by defining its target segment primarily in terms of need for value, Walmart is able to focus on a large cross-section of consumers because, despite their differences, these consumers share an important need.

In practice, few companies are able to segment the market in a way that defines such a large set of target consumers. Managers in recent decades have therefore placed a greater emphasis on market niches that reflect different preferences attributable to differences in demographics, lifestyle, life stage, or values and attitudes. The 32-year-old woman with a young child may or may not be married, may or may not be in the workforce, and may or may not think that shopping “green” is important. All of these factors are likely to color her view of alternative brands of detergent and the type of car she buys. Furthermore, although a broad cross section of consumers shop at Walmart, the company's customer base has an income that is lower than average, political beliefs that are more conservative than average, and a lower-than-average likelihood of holding a bank account when compared to customers of Costco. Thus, even Walmart's broad appeal resonates more with some and less with others.

The insight that consumers differ in their preferences and will be more responsive to marketing efforts tailored to their needs is not new. However,

advances in technology enable marketers to address the needs of ever-narrower targets more profitably than they could in the past. The Internet and smart phone technology, as well as a proliferation of vehicles in traditional media (cable channels, specialized magazines, etc.), make it possible to reach smaller segments of consumers in a cost-effective manner. Further, mass customization techniques allow producers to quickly and efficiently tailor their offerings to customers' tastes. Want M&Ms to match your office decor and sport the company logo? No problem, just order online. Are you a chocolate lover seeking a Caribbean escape vacation? A quick search online will turn up several options, including a stay at the Cotton Tree Lodge in Belize, where guests harvest cacao pods, make their own chocolate, and learn about fair-trade issues from members of the Toledo Cacao Grower's Association.

In his book *The Long Tail*, Chris Anderson argues that innovations in technology make marketing narrowly targeted goods and services as economically attractive as marketing more mainstream fare.¹ Consider products such as movies, games, books, or software. Historically, the high production, distribution, and promotion costs meant that only a few well-funded players could afford to compete, and they required a focus on blockbusters. However, advances in technology such as digital video cameras, desktop music and editing software, or desktop publishing enable any creatively minded individual to record a song or movie, publish a book, or design a new game. Further, digital versions of products can be stored digitally and distributed online for almost no cost, in contrast to the high inventory carrying costs a manufacturer or retailer incurs when these products are distributed in hard copy format. Finally, instead of the producer investing in an extensive mass-media advertising campaign in hopes of reaching prospective customers, search engines, blogs, and other filtering devices allow customers to efficiently search a near-infinite array of offerings to find the ones that suit their idiosyncratic tastes. Although Anderson's view has generated some debate, there can be no doubt that technology has made it economically viable to reach smaller segments with more targeted offerings.² As a result, new ventures such as TCHO, an artisanal chocolate company offering "fair trade" chocolate, are able to reach the niche of customers who care about the origins of their chocolate bar. Similarly, established players such as Amazon are able to strengthen their hold on the book market by serving customers in search of the latest blockbuster and customers looking for one-of-a-kind books.

How segments are defined has also evolved over time. In the early days of market segmentation, focus centered on identifying subgroups based on descriptive characteristics such as demographics and geography. The logic was that men and women, young and old, rich and poor, northerners and

southerners would differ in their preferences and, therefore, require different marketing programs. Although this holds true in some situations, often there is significant variation among individuals who share the same demographic profile. Accordingly, segmentation schemes based on attitudes, values, opinions, and lifestyle were developed. This so-called “psychographic” approach identifies subgroups of “Thinkers,” “Experiencers,” and the like, each of whom shares a set of psychological and attitudinal characteristics. Segments defined by psychographics have proven to be especially helpful when designing marketing communications. However, psychographics are often poor predictors of specific behaviors related to a category and brand. As a result, in an effort to segment in ways that help managers set strategic priorities, there has been a recent emphasis on partitioning the market based on usage patterns and related behaviors.³ Brand users may be distinguished from competitors’ users and nonusers of the category. Further segmentation may identify subgroups based on when and how often usage occurs and whether the user is actively loyal to the brand, endorsing it to others.

Our view is that an insightful and actionable approach to segmentation requires not choosing among the different approaches to segmentation but rather combining them. It is important to understand who (demographics and geography) is engaging in what behavior (usage) and why (psychographics and specific motivations). At the same time, the insight provided by different bases for segmentation will vary as a function of the decision being made.

Consider Vosges, a company that makes exotic “East meets West” chocolates, such as the Black Pearl Bar, which combines ginger, wasabi, black sesame seeds, and dark chocolate. If Vosges were to segment the market based on *who* is most likely to purchase its products, it might divide the market based on gender (women versus men), age (25 to 35 versus 35 to 45), or geography (urban versus rural). Or if the company segmented the market based on *what* behaviors customers exhibit in relation to the product category, it might divide the market based on those who do or don’t purchase high-end chocolate, those who buy frequently versus infrequently, or those who buy from a particular competitor. Another alternative is focusing on *why* consumers buy the product, in which case Vosges might divide the market based on people who are buying for a gift versus themselves, or people who buy because they love chocolate in particular versus those who like all kinds of artisan food products.

As the Vosges example illustrates, all of the dimensions (who, what, and why) contribute to a rich understanding of segments in the marketplace and the attractiveness of targeting these segments. Nevertheless, different dimensions of a targeted segment will be more or less relevant depending on the decision at hand. For example, if Vosges were making decisions related to selecting

new retail outlets, information about where targeted customers live and shop would be critical; whereas if the company were designing communications, information about the motives for purchase as well as general values, aspirations, and attitudes would be more informative.

USAGE-BASED SEGMENTATION

We recommend that companies begin the segment definition process by creating subgroups based on *patterns of usage*. In general, current usage is most likely to predict (albeit imperfectly) future usage. Therefore, understanding current usage patterns helps marketers prioritize targets and design marketing strategies to achieve the firm's goals by altering current usage patterns.

The usage-based segmentation approach begins by dividing the market into subgroups on the basis of current behavior patterns. Nonusers of the category are separated from users, and users are grouped according to the brand that they use. Users of a brand may be further segmented based on their frequency, occasion, and motivation for use.

Next, the usage segments are analyzed and understood in terms of the demographic, geographic, psychographic, and motivational characteristics that distinguish them from each other. These characteristics help the marketer estimate the current size and growth potential of a segment from population data, select media that reaches a particular segment in a cost-effective manner, and tailor communications to the general lifestyle, values, and attitudes of the segment.

Finally, the current and potential profit associated with a segment is estimated. Some segments may be well-defined in terms of their usage and descriptive characteristics, but they may be unattractive targets because their long-term value is low and/or there are too few members in the segment to justify a unique marketing effort.

Segmenting Steps

The first step in usage-based segmentation is to divide the market into users and nonusers of the product category. This categorization is valuable because users and nonusers pose different challenges for the marketer. Nonusers may be unaware of the category and its benefits or believe that the category does not fit their needs. They also may be ineligible to use the product (i.e., 16-year-olds are not legally permitted to consume beer). Marketers must overcome these barriers when targeting nonusers. For example, to attract nonusers, a vacation cruise company will need to spend resources describing the experience of

taking a cruise, dispelling potential misconceptions about cruises, and explaining how a cruise is different from (and better than) other categories of vacation experiences, such as visiting a resort.

Category users are familiar with and (presumably) find some value in consuming within the category. Thus, the task is to sustain and perhaps expand their usage. Usually marketers further segment users on the basis of brand—do they use your brand or a competitor's brand? Consumers generally choose a particular brand because they believe that it provides a benefit that is different from (and presumably better than) other brands. Thus, current customers are likely to be more receptive to the firm's marketing efforts. Further, a firm typically can obtain more detailed data on its customers versus competitors' customers. This data may allow more efficient, customized marketing activities directed at current customers. These advantages become challenges when a firm attempts to attract the customers of a competing brand.

Marketplaces often include consumers who are not loyal to any single brand. For example, some consumers are variety seekers who habitually consume a handful of brands, rather than just one. Others are price-conscious consumers who gravitate to whatever brand offers the lowest price or the best perceived value. These additional usage segments (and the associated challenges) are important to consider when developing a usage-based segmentation plan.

The basic segmentation of customers into nonusers, brand users, and competitor-brand users is often further refined by considering the level and occasion of use. These variables help identify customers who differ in their value to the firm. Frequently, a small number of customers or use occasions account for a disproportionate amount of brand usage. Indeed, brand usage is often said to follow the "80/20 rule," where 80 percent of consumption is done by 20 percent of the users. This statistic holds true for most major beer brands, as well as fast-food franchises such as McDonald's. Further, use occasion and brand loyalty may be associated with the level of use; heavy users may use the brand across multiple occasions and may be highly loyal. For example, a heavy drinker of Bud Light may drink the brand nightly at home as well as in a bar on the weekend, and he may endorse the brand to friends. By contrast, a light drinker might drink the brand only occasionally in a bar and also drink other brands of beer. Similarly, frequent customers of Hyatt hotels are business travelers who stay on weeknights and are vested in the company's frequent stay program, whereas light users are leisure travelers who stay on weekends.

The purchase motivation or purpose of a product or service should also be considered. Purchasing may be motivated by features of the product, such as its price, performance, or convenience, or by how the product makes the purchaser feel or appear to others when using it. Knowledge of the primary

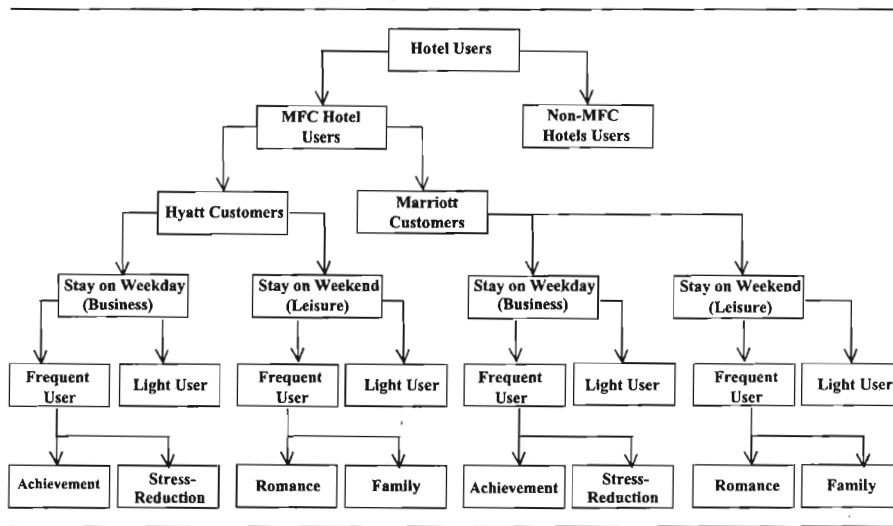
motivation for purchasing is useful when deciding how to position a product. For example, a \$1,299 ecologically friendly washing machine might be presented as “saving the consumer \$90 per year on water bills” or as being “good for the environment,” depending on whether the target is more likely to be motivated by functional versus emotional considerations (see Chapter 4, “Developing a Compelling Brand Positioning,” and Chapter 6, “Creating and Managing Brands”).

One factor that influences the motivation for purchase is the role that the targeted individual plays in the purchase process, which is sometimes called the “buying center.” Buying center roles include the influencer, decider, purchaser, and user. In categories such as toys or presweetened cereals, parents typically play the roles of deciders and purchasing agents while children are influencers and users. Parents are likely to weigh heavily functional considerations such as the nutritional value and safety of products. In contrast, children are more likely to focus on the experience of using the product (i.e., taste, fun).

In business-to-business settings, buying center roles might be filled by engineers (influencer), VPs of marketing or finance (decider), purchasing agents (purchaser), and operatives (user). These individuals are often rewarded differently, leading to different motivations. For example, the compensation of a CFO might be tied to the overall profitability of the firm, the compensation of a purchasing agent might be based on extracting price concessions from suppliers, and the compensation of a plant foreman (who actually uses the products) might be tied to measures of production efficiency.

The astute marketer understands that the motivations of those playing different roles in the decision process vary and thus focuses the marketing effort on the person in a household or company whose motives are best served by the firm’s brand. Such was the case when Philips sought to make inroads into General Electric’s (GE) dominant position in the lighting industry. GE focused on corporate purchasers, who seek lower purchase prices and longer bulb life. GE’s strong share position gave the company economies of scale that allowed them to market traditional fluorescent bulbs for as little as 80 cents, a price that competitors could not match. However, such bulbs have a hidden cost due to their high content of toxic mercury. Replacing a traditional fluorescent bulb can cost \$1 due to restrictions in collection and disposal and due to the need for legal protections against damage in dumping sites. Although purchasing agents are not sensitive to these replacement costs, corporate financial officers are. Philips developed Alto, a low-mercury bulb that can be disposed in the regular trash, and they marketed it to corporate financial officers. The bulb gained favorable press coverage and political support due to its environment-friendly status. More importantly, thanks to Philips’s decision to target a different role

Figure 2.1
Usage-Based Segmentation Tree for Hotels



in the buying center, the company was able to win some new customers and deliver high margins, despite GE's historical stronghold on the lighting business.

An example of a usage-based segmentation tree for customers in the “mass first class (MFC)” hotel industry appears in Figure 2.1. For simplicity, only two hotel chains that compete in this category, Hyatt and Marriott, are shown. Although the tree could be expanded to include additional players such as Westin, Sheraton, and Renaissance, often a company focuses on its most direct competitors when segmenting a market based on usage.

Profile Characteristics

Having initially defined segments based on behaviors and motivations for behaviors, the firm can turn to questions about who exhibits these behaviors. Such information is critical to assessing the attractiveness of targeting different usage segments and to designing and implementing marketing programs aimed at changing their behavior. Variables that are commonly employed at this stage in the segmentation process are discussed next.

Demographics In consumer markets, usage segments are typically described in terms of demographics such as gender, age, marital status, life stage,

education, occupation, and income. Accordingly, those who frequently purchase Corona beer might be described as unmarried, college-educated men ages 20 to 25 who work in white-collar professions and have a household income between \$30,000 and \$40,000.

Identifying customers in terms of demographics serves several purposes. First, the profile can be applied to census data to arrive at a rough estimate of how many people share the demographic profile of the current customers. This enables the company to assess its success in penetrating the segment and the potential for further growth by attracting customers similar to current ones. Second, demographic characteristics may be helpful in making product design and pricing decisions, because market research reports often include data on the behaviors and consumption patterns of people with certain demographic characteristics. For example, if people who share the demographic profile of Hyatt Place customers have been found to be more concerned about fitness than the population at large, adding a state-of-the-art gym to each of these properties might strengthen customer loyalty. However, if people who share the demographic profile of Hyatt Place customers are typically “couch potatoes,” the same dollars might be better spent on larger flat-screen televisions for the guest rooms.

Demographic characteristics also have implications for the placement and content of marketing communications. Demographics are correlated with media habits, and market research companies such as Nielsen frequently use demographic characteristics to categorize those who use different kinds of media. Young children watch different television programs than teens, teens visit different web sites and read different magazines than their parents, men attend more sporting events than women (and thus have greater exposure to venue-based advertising). If a company has a clear demographic profile for a targeted segment, it can then select media that cost-effectively reaches targeted individuals while avoiding nontargeted people.

Further, knowledge of the demographic characteristics of a target is helpful when designing communication content. If the message includes visual elements, such as a product user or spokesperson, that person can be chosen to be similar to the target customer in age, gender, and social class, reinforcing the perception that the product is for people like them. However, caution should be used here, as evidence suggests that customers' self-perceptions and aspirations may be different from reality. For example, older adults often perceive themselves as looking 10 to 15 years younger than their chronological age, so an advertisement targeted to 65-year-olds would do better featuring adults closer to age 50. Conversely, teens often aspire to appear older than their years and are likely to respond more favorably to images of people in

their twenties rather than teens. Further, consumption in categories such as beauty and fashion is motivated more by aspirations than by the target's current self-perception.

In addition, demographics inform message presentation because certain demographic characteristics have been linked to differences in processing information. For example, adults 45 and older are somewhat slower than younger adults to master tasks that require skills that they did not learn earlier in life. As a result, self-paced media (such as print) are likely to be more effective than externally paced media (such as television or radio) when targeting older adults and conveying new, complex information.

Gender is also associated with different processing styles. Women tend to be communal, considering both themselves and others in decision making. In the context of marketing communications, this orientation leads women to consider disparate bits of information, such as multiple product benefits, when forming judgments. By contrast, men are more agentic, focusing more narrowly on self-expression, goal-directedness, and critical decision-making information. Accordingly, in forming their judgments, men are likely to focus on a single product benefit as well as exhibit greater reliance on prior knowledge and other cognitive shortcuts.

Finally, individuals' cultural backgrounds affect their general orientation and judgments. For example, evidence shows that people from Asian cultures tend to be more interdependent, whereas people from western cultures tend to be more independent. Like gender, this difference in orientation may influence the willingness to consider multiple benefits and perspectives when processing marketing communications and forming judgments. It suggests that Asians may be more likely to consider multiple benefits and perspectives than Westerners.

This approach is equally applicable to business-to-business markets. In these situations, potential customers can be initially divided into groups based on the usage characteristics we outlined previously (e.g., user/nonuser, user of Brand X versus Brand Y). As with consumer usage segments, business-to-business usage segments may then be further characterized in terms of distinctive descriptive characteristics, which are sometimes termed "firmographics." The most commonly used descriptive characteristics are industry/SIC code and firm size because information on the number of companies in these categories is publicly available, allowing a firm to estimate how effectively it has penetrated a segment, as well as the growth potential associated with targeting a particular segment. These characteristics are useful not only because they are easily available, but also because product and service needs often vary by industry and firm size. The electronic test equipment needs of a large telecommunications company are likely to be quite different from the needs of a small general

industrial company. Industry and firm size also may be helpful in designing marketing communications. Most industries have their own publications and conferences, enabling firms in particular industries to reach these communities efficiently. Finally, the buying process may vary as a function of industry and firm size. For example, the decision process is likely to be more complex and formal when selling to the government versus private industry and when selling to a large versus a small firm.

Geography It can be useful to describe both consumer and business segments in terms of their locations, because where customers live and work may influence their preferences and behaviors. For example, geography is often correlated with economic status. In developing countries, consumers may aspire to purchase global brands offered by companies such as Cadbury, Procter & Gamble, and Unilever, but they lack the purchasing power to afford such products in the large package sizes used in more developed countries. In response, companies introduce smaller package sizes (i.e., a single razor blade) at lower prices in these areas of the world.

Further, consumers in a particular geographic area may share a cultural orientation. For instance, individuals raised in the Japanese culture prefer different compartments for different things. This insight led Panasonic to introduce refrigerators with four to six doors in Japan, a feature unlikely to appeal to the U.S. consumer, who does not have this preference. Different geographic areas are also governed by different laws and regulations. In the alcoholic beverage market, some European countries have relatively few regulations about where liquor can be distributed and to whom it can be sold. At the other extreme, some Middle Eastern countries have tight restrictions—or even outright prohibitions—regarding the sale of alcohol. Accordingly, Diageo focuses more on marketing nonalcoholic beer in some countries than in others.

The geographic location of a segment is also important because it has implications for a variety of marketing decisions beyond product design. For example, in regions where customers are widely dispersed (rather than heavily concentrated), the sales territories are likely to be larger. Therefore, media such as outdoor advertising may not be effective, because billboards are not seen by enough customers to justify the expense.

Geographic information about customers can also provide insight about demographic characteristics. Additech, a company that markets and distributes fuel additives at the gas pumps of retailers such as Murphy U.S.A., has detailed usage data for each customer transaction (i.e., time of day, method of payment, amount and type of gas pumped, pump location), but it does not have a demographic profile of its customers. It uses transaction data to

identify geographic areas with a high concentration of Additech customers and then profiles these areas demographically and psychographically using services such as Nielsen's PRIZM, which defines household types of geographic areas on 66 demographic and behavioral dimensions (http://en-us.nielsen.com/tab/product_families/nielsen_claritas/prizm).

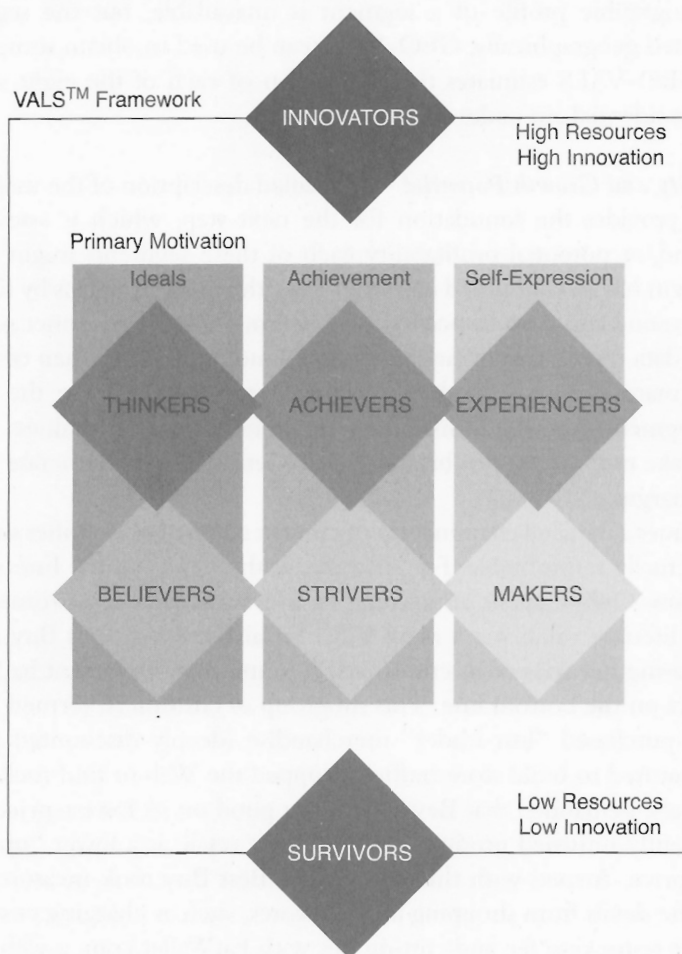
At the same time, it is important to recognize that, just as is the case for demographic characteristics, preference will not always vary with geography. Procter & Gamble has found that teenage girls around the world have similar concerns regarding puberty. In response, the company created a global web site for products and information related to this life stage. The Phonak group, which sells hearing aids, has found that both European and American baby boomers have similar needs for enhanced hearing, as well as similar qualms about using hearing aids. These observations reinforce the importance of defining segments based on characteristics that are not merely differences, but rather differences that impact how, why, and whether the product or service is used. In the preceding P&G and Phonak examples, age segmentation is meaningful, but geographic segmentation fails to capture important differences in consumption.

Psychographics It is also useful to characterize segments in terms of general psychological or personality traits and lifestyle. SRI Consulting Business Intelligence offers a tool for psychographic classification known as VALS. This framework classifies consumers into one of eight groups (see Figure 2.2) that vary along two dimensions—motivation and resources—on the basis of their responses to a survey. The survey asks respondents to indicate their levels of agreement/disagreement with 35 attitudinal statements such as, “I like to try new things,” “I consider myself an intellectual,” “I like to make things with my hands,” and “The federal government should encourage prayer in public schools.” The respondents also report their gender, age, education, and income.

Each of the groups is profiled in terms general motivation and decision making. For example, *thinkers* are described as:

mature, satisfied, comfortable, and reflective people who value order, knowledge, and responsibility. They tend to be well-educated and actively seek out information in the decision-making process. They are well-informed about the world and national events and are alert to opportunities to broaden their knowledge. Thinkers have moderate respect for the status quo institutions of authority and social decorum, but are open to consider new ideas. Although their incomes allow them

Figure 2.2
VALS™ Framework



many choices, Thinkers are conservative, practical consumers; they look for durability, functionality, and value in the products they buy. (www.sric-bi.com/VALS/thinkers.shtml)

A psychographic profile of a targeted segment may be particularly helpful in designing marketing communications that resonate with those customers' general values and orientations. For example, logical arguments and data,

as well as endorsements by well-regarded authorities, are likely to enhance the persuasiveness of a message with thinkers. If direct information regarding the psychographic profile of a segment is unavailable, but the segment is concentrated geographically, GEO-VALS can be used to obtain some general insight. GEO-VALS estimates the proportion of each of the eight segments across all residential zip codes and block groups.

Profitability and Growth Potential A detailed description of the usage-based segments provides the foundation for the next step, which is assessing the current and/or potential profitability each of these segments might provide. When a firm has an established customer base, this analysis begins by scrutinizing the revenue and costs associated with serving current customer segments. Typically, data reveals that some segments are more profitable than others. For example, many airlines find that it is more profitable to serve the business traveler segment than the leisure traveler segment because business travelers typically take more trips, exhibit lower price sensitivity, and generate a higher per-trip margin.

Sometimes a detailed examination of current customers identifies subgroups that are actually unprofitable. For example, at the height of the Internet bubble, CDnow Online spent an average of \$40 to acquire a customer whose estimated lifetime value was a mere \$25.⁴ Similarly, when Best Buy analyzed the purchasing histories of its customers, it found that 20 percent had a negative impact on the bottom line. This subgroup of customers, termed “devils,” primarily purchased “loss leader” merchandise (deeply discounted products that are featured to build store traffic), shopped the Web to find rock-bottom price quotes, demanded that Best Buy make good on its lowest-price pledge, and frequently returned products, forcing their resale at a lower “open-box” discount price. Armed with this knowledge, Best Buy took measures to discourage the devils from shopping at their stores, such as charging customers a 15 percent restocking fee and cutting ties with FatWallet.com, a web site that had collected referral fees for delivering bargain-hunting consumers to Best Buy’s web site.

However, in many instances, customers who might seem unprofitable in the short term become more attractive if the value of a relationship over time is considered. Gillette may lose money when it sends free razors to young men who are just beginning to shave, but the firm ultimately makes a tidy profit because a subset of these men become customers and purchase high-margin replacement blades year after year. Similarly, car dealers may make a modest profit from the sale of a car, but this is supplemented by profits from maintenance and repairs and future sales to the customers that they acquire.

Therefore, when examining the profitability of a segment, it is important to begin by calculating Customer Lifetime Value (CLV), as shown below.⁵

$$CLV = \sum_{a=1}^N (M_a - c_a)r^{(a-1)} / (1+i)^a - AC$$

where:

N = the number of years over which the relationship is calculated

M_a = the margin (i.e., the revenue-cost) the customer generates in year a

c_a = the cost of marketing communications or promotions targeted to the customer in year a

r = the retention rate ($r^{(n-1)}$ is the survival rate for year a)

i = the interest rate (also called discount rate, which represents the time value of money; a dollar today is worth less than a dollar next year)

AC = the initial cost to acquire a customer

An estimate of the potential profits associated with the segment can be made by multiplying the CLV by the number of customers thought to belong to the segment. In addition, the CLV formula can serve as a framework for assessing growth strategies targeted at a particular segment. For example, a manager might calculate the increase or decrease in CLV that would result if a 10 percent increase in spending on marketing communications (c_a) resulted in an increase in retention rate (r) of 2 percent.

In sum, usage patterns serve as a useful starting point for segmentation because they identify groups that pose different demand stimulation tasks for the marketing manager: Nonusers must be persuaded to use the category, users of competing brands must be persuaded to switch, and users of the firm's brand must be persuaded to remain loyal and expand their usage. Profiling usage segments in terms of their distinguishing demographic and psychographic characteristics, as well as estimating their profitability and growth potential, lays the foundation for the next step: setting targeting priorities.

SETTING TARGETING PRIORITIES

The selection of target segments should be based on the firm's current position in the market as well as its goals and resources. We begin by discussing targeting priorities for established brands and then consider how to modify this approach when the launch of a new product requires that the firm identify a target for the first time.

Established Brands in Existing Categories

When a brand is established in a product category, there are three options for growth. Growth may be achieved by (1) targeting current customers and convincing them to increase their spending on the brand, (2) targeting competitors' customers and persuading them to switch their purchasing to the firm's brand, and (3) convincing noncategory users both to consume in the category and to choose the firm's brand when so doing. We consider each of these strategies in turn.

Targeting Current Customers Established brands, by definition, have an existing base of customers. Accordingly, a natural first step in targeting is to consider the growth potential afforded by investing resources in this segment. There are several reasons to make current customers the first priority. Current customers are aware of the brand and presumably have a more favorable disposition toward it than those who have chosen other brands or are nonusers of the category. Further, a firm is likely to have data about past purchases as well as contact information for current customers. This information allows it to deliver customized products and services, as well as messages, to current customers in a cost-effective manner. Finally, the high cost of acquiring customers means that return on investment is often greater for customer retention than customer acquisition. Specifically, one study reports that a 10 percent improvement in customer retention increases overall value of the customer base by 30 percent, whereas a 10 percent reduction in acquisition costs improves the overall value of the customer base by only 1 percent.⁶ Another study reveals that increasing customer retention by as little as 5 percent can result in a corresponding 100 percent increase in profits. For example, in the case of regional banks, a 20-year customer is worth 85 percent more in profit than a 10-year customer. As the years pass, older loyal customers take out loans for cars, homes, and so on, without incurring the costs that are attendant to acquiring new clients.

The process of focusing on existing customers begins by assessing customer loyalty. Two related questions are useful in this regard. First, what percentage of customers are retained from one year (or buying period) to the next? The more customers that are retained, the more loyal the customer base is. The average customer retention in the United States is estimated to be around 80 percent, suggesting that there is room for improvement at many firms. Second, what proportion of customers' category spending does the firm capture? If the firm captures only a small percentage of a customer's category spending, this suggests opportunities for growth.

If retention is low or customers spread their category spending across multiple brands, the firm should implement strategies designed to increase loyalty. The company might implement loyalty programs, such as the frequent stay or frequent flyer rewards programs used by hotels and airlines. Or, for suppliers of frequently used products such as toiletries or pet food, customers might be encouraged to sign up for an automatic replenishment program. If the reason for defection is that customers are facing tough economic times and are trading down to store brands to save money, increasing retention may require introducing a more affordable version of the brand. Accordingly, during the 2008–09 recession, Procter & Gamble introduced Tide Basic, a product that lacks the full cleaning power of the base brand but offers good performance at a price that is competitive with store brands.

If retention is high and the firm captures the majority of a customer's current category spending, then growth might be achieved by identifying new use occasions for the product or by persuading loyal consumers that their needs would be better served by a more expensive, higher-margin version of the product. A classic example of this approach to growth has been Arm & Hammer's identification of new uses for its basic baking soda product. Building from baking soda's original cooking uses, Arm & Hammer has encouraged consumers to use the product for everything from deodorizing drains, refrigerators and carpets to whitening teeth. In a similar vein, Starbucks coffee has expanded its product line in an effort to increase the amount consumers spend each time they visit a store. Sandwiches, newspapers, coffee-making equipment, and even music on DVDs are available for sale in addition to the firm's trademark coffee. Brands such as Gillette regularly introduce improved versions of their shavers to encourage consumers to trade up to better-performing and higher-margin products.

Targeting Competitors' Customers Although it is critical to target current customers for retention and growth, the long-term success of a firm requires that it also acquire new users of the brand. One approach is to target customers of competitors' brands who are similar to the firm's current customers or who have aspirations to be like the firm's customers. These people are already users of the category, and their similarity to current customers increases the likelihood that they might be persuaded to switch to the firm's brand. Thus, Apple, whose users are considered to be young and hip, targets PC users who are (or aspire to be) seen as young and hip. Similarly, the Dove brand, which has aligned itself with women who accept the body changes that come with aging, targets users of competing brands, such as Olay, who may be attracted to this attitude.

However, a word of caution is in order. Efforts to steal competitors' customers sometimes provoke a counterattack, especially if the competitors' core business is threatened. For example, Burger King spent \$100 million to promote the superiority of its new fries over those offered by McDonald's. This campaign involved advertising that reported more favorable consumer reactions to Burger King's fries than McDonald's fries, as well as offering free samples to customers at Burger King. McDonald's responded by increasing advertising spending on its fries and by conducting its own taste test, which not surprisingly favored its fries. The result was that while Burger King experienced an increase in the sales of its fries, its share of the fast-food business dropped in relation to McDonald's. By contrast, efforts to steal noncore customers from competitors may be more successful. ThoughtWorks, a medium-sized IT consultancy known for highly sophisticated, custom applications, has been able to attract some specialized projects from competitors without attracting a strong response. Because these specialized projects are not central or critical to ThoughtWorks's competitors, these competitors do not spend resources trying to win such business back and sometimes even recommend ThoughtWorks as an option.

Targeting Noncategory Users When opportunities are limited to increase category consumption through an existing customer base, firms should turn attention to attracting nonusers of the category. Two strategies are point-of-entry (targeting first-time users) and building out the category.

Point of Entry (Attracting First-Time Users) In many product categories there are nonusers who are likely to enter the category coincident with some life stage or life event. The goal of a point-of-entry strategy is: (1) to identify who will enter the category; (2) to determine when entry is likely; and (3) to direct their consumption to the firm's brand. A point-of-entry strategy is analogous to a first-mover strategy, because both strategies involve a focus on being the first product in the category that the consumer buys. However, with a point-of-entry strategy, the user is new to the category rather than the product being new to the market.

Targeting customers at the "point-of-entry" to the category is appealing because these individuals have reached a point in their lives when they are particularly receptive to the category. Also, because these consumers do not yet purchase in the category, companies can avoid the switching costs normally associated with targeting users of a competitive brand. In addition, acquiring a customer at the moment they are ready to start using a product category maximizes the time period over which the product will be used, increasing the CLV.

As an example, PNC Financial Services focuses on attracting members of Generation Y with its online product "Virtual Wallet." Virtual Wallet is three linked accounts called "Spend," "Reserve," and "Growth." Customers can drag money from account to account on one screen, get bank balances via text message, and view balances on a calendar that displays estimated future cash flow based on when they are paid, when they pay bills, and when they tend to spend. These point-of-entry customers are attractive because they hold higher-than-average balances and are inexpensive to serve because they rarely call customer service or visit branches. And, they also accept an interest rate that is lower than the national average in exchange for the convenience of the online product. PNC knows that these customers will be at the point-of-entry for other services, such as home loans and brokerage accounts, in the not-so-distant future.

Similarly, Procter & Gamble and Kimberly Clark aggressively compete to win the disposable diaper business from couples expecting their first child. AARP markets long-term care insurance to individuals who have recently passed an age milestone such as 65. And Budweiser pursues young men who are coming of legal age to drink alcoholic beverages.

Building the Category An alternative approach to attracting nonusers involves building the category. Category-build strategies are appropriate when managers believe that demand for the category is unsaturated and might be stimulated through marketing. Unlike point-of-entry strategies, where entry into the category is a matter of timing, category-build strategies focus on individuals who have no intention of using products from a category. They might also target customers who do use such products but not for the purpose the firm has in mind.

There are a number of reasons why a category might be unsaturated. When a category is relatively new, as was the case with digital video recorders (DVRs) in the early 2000s, prospective customers may be unaware of the category and its benefits. In such instances, diffusion of information about the category may increase consumption. Alternatively, the lack of saturation may be attributable to consumers' failure to recognize the problem for which the category is a remedy. This situation arises frequently in the pharmaceutical arena, where consumers are often unaware of their depression, low thyroid condition, or high blood pressure and thus do not prompt their physicians to prescribe the products available to treat these conditions. At other times, consumers may desire to consume products from the category but perceive barriers to their consumption. For example, low-income households may not purchase a computer because they believe they lack the means to do so.

Sales for seasonal categories may also be viewed as being unsaturated during seasons when sales are traditionally low. For example, a significant proportion of sales for Bailey's Irish Cream occur during the winter holiday months of October, November, and December. Over the years, the brand's managers have committed resources toward encouraging consumers to use Bailey's during other times of the year, such as by advertising consuming the beverage over ice as a summer drink.

It is often difficult to know whether a category is unsaturated in the absence of data regarding the reasons for nonuse. Electric razors are purchased by about 30 percent of the U.S. population. Is this category saturated or not? Most shavers are aware of the option of using an electric razor and have chosen to use a wet shaving system, presumably because they perceive it is a superior shaving solution. If this choice is based on accurate information, such as personal experience with an electric shaver, demand may be saturated. However, if the choice of a wet shaving system was based on incomplete or out-of-date information about electric shavers or if shaving needs change over time (which they do, as skin gets drier with age), then demand may be unsaturated. Thus, market research to gather insight into the reasons for category nonuse may be required to assess whether a category-build strategy is appropriate.

In general, a category-build strategy is more likely to be effective when nonuse is attributable to lack of awareness, rather than to a negative disposition toward the category. Thus, the observation that 13 million Americans are unaware of (and undiagnosed for) thyroid conditions, suggests a substantial opportunity to grow demand for thyroid medications.

Before investing in category-build strategies, the firm should assess the likelihood that it will be the primary beneficiary of any category expansion. A useful starting assumption is that firms will capture new category sales in proportion to their current market share. Thus, only firms holding a strong share position may find it worthwhile to undertake category-build efforts on their own. When no single firm dominates in a market but category-build activities are needed, companies might band together through a trade association and contribute funds that are used to build the category. A familiar example is the "Got Milk?" campaign, which was funded by dairy farmers' contributions to the Milk Processor Education Program. In addition, there are a variety of devices that can be used to ensure that a firm's brand benefits from any efforts it makes to build the category. Firms with strong sales forces may use advertising to build the category and then employ their sales force to direct the increased demand to the firm's brand.

On occasion, it is possible to succeed in pursuing both point-of-entry and category build targeting. Consider the category of small, lightweight, inexpensive (\$200 to \$500), network-enabled laptop computers known as “netbooks.” When netbooks were introduced in 2007, the vision was to target first-time buyers in emerging and developing markets who were unable to afford computers with greater functionality and computing power. However, netbooks have also appealed to owners of one or even two PCs, who view them as secondary machines or as durable options for younger children.

In summary, we recommend that companies with current customers follow what we term is the “path of least resistance” in targeting. They should begin by exploring the opportunity to grow by increasing the revenue from current customers through increased loyalty or expanded purchasing. The next step is to attract new customers who are similar to current customers, perhaps by stealing them from competitors. If these approaches prove to be inadequate to meet growth goals, then targeting nonusers either at the point of entry or by attracting new users to the category should be considered.

Targeting When Launching a New Product

Achieving growth over the long term often leads a firm to introduce a new product. When the firm has a current customer base in one category, research that uncovers unmet needs of existing customers in other, related categories may prompt entry into the new category. In such situations, targeting proceeds in much the same manner as when the firm has an existing customer base in a category. Focus centers on current customers, but the emphasis is on persuading them to consume the firm’s brand in a new category. For example, research on Mr. Clean customers revealed that some customers were unable to protect their hands while doing heavy cleaning because they were allergic to latex, which is used to make most household gloves. Thus, Procter & Gamble developed a nonlatex glove, Mr. Clean Nyplex Reusable Gloves, to serve the needs of these customers.

In other instances, entry into a new category is motivated more by the opportunity to leverage the firm’s competencies and resources to attract new customers than by a desire to serve existing customers. For example, BIC grew by launching pens, then lighters, and then razors. All of these products leveraged the company’s expertise in manufacturing inexpensive, molded plastic products and distributing these products through mass-merchandising outlets. However, the targeted customers were not necessarily the same; smokers were targeted for lighter sales, but pens and razors appealed to smokers and

nonsmokers. What unifies customers across the product categories is the type of value they seek: all three products appeal to consumers who want basic, functional products, conveniently available at a low price.

In the case of “really new” or “new to the world” products, the firm not only launches a new product, but it also pioneers a new category. TiVo created a new category of digital video recorders (DVRs), Swiffer Sweeper created a new category of sweeper mops, and the launch of Kindle created a new category of wireless electronic reading devices. In such situations, all prospective customers are nonusers, and the firm must build the brand and category simultaneously. Addressing this targeting challenge requires insight into both the goals that the new product helps the customer achieve and how those goals are being served currently.

For example, TiVo empowers TV watchers by enabling them to easily control what they watch and when they watch. Prior to the introduction of TiVo, VCRs were used to achieve this goal in a more limited fashion. Accordingly, the DVR category and the TiVo brand were built by targeting VCR users who sought greater control over their viewing experience and who had the means and willingness to embrace new technology. The Swiffer Sweeper provides a simple, efficient way to clean floors. Before Swiffer, floor cleaning typically was a two-step process that involved first sweeping the floor with a broom to remove particles and then mopping to shine the surface. Procter & Gamble built the sweeper mop category and the Swiffer brand by targeting homemakers who sought a more convenient way to clean floors. Kindle gives avid readers easy, digital access to a vast library of books and other printed material wherever they happen to be. Before Kindle, books could only be obtained by visiting a bookstore or ordering them online for later delivery. Thus, when launching a new product in a new category, a firm must target nonusers who are achieving the goal served by the new product with products from a different category that serves the same goal.

When entering a new category, the firm should begin by reflecting on its distinctive competencies and the way it creates value. Such an approach may seem counter to the common marketing advice that companies should focus less on what they make and more on the customer’s needs. However, when identifying new market opportunities, a firm that begins with consumers’ needs may identify opportunities that it is ill-suited to serve. By understanding what it does well, the firm can then examine the market to determine the likelihood that there are segments of customers whose needs it can meet better than existing competitors.

In their book, *The Discipline of Market Leaders*, Michael Treacy and Fred Wiersema describe three broad approaches or disciplines that a firm may

adopt to create value: operational excellence, product leadership, or customer intimacy.⁷

Operational Excellence Walmart and McDonald's are prime examples of firms that have risen to the top in their categories via operational excellence. Operationally excellent firms create value by providing middle-of-the-market products at great prices and with minimal inconvenience. In order to create such offerings, these firms have core business processes that sharpen distribution systems and provide no-hassle service; a management structure with a strong, central authority and a finite level of empowerment; management systems that maintain standard operating procedures; and a culture that acts predictably and believes one size fits all.

The offerings of an operationally excellent firm are likely to appeal to customers who prefer habitual consumption experiences and don't like surprises or significant variation from one purchase to the next. They seek functional products and base their choice of brands on logic rather than emotion. When entering a new category, the operationally excellent firm typically seeks a large target segment in order to leverage its ability to produce large quantities at a low cost and distribute broadly. This may lead it to target customers of the existing market share leader with the promise of a low price or greater convenience.

Product Leadership Intel, Apple, and Nike employ a product leadership approach to creating value. Firms that pursue this approach focus on developing new and better products. In so doing, they often make prior generations of their own products obsolete. Firms embracing the product leadership discipline have core business processes that nurture ideas, translate them into products, and market them skillfully. They have a structure that acts in an organic way, management systems that reward individuals' innovative capacity, and new product success and a culture that rewards experimentation and "out-of-the-box" thinking.

The offerings of firms practicing product leadership appeal to consumers who become easily bored with product or service experiences and who therefore are instinctively attracted to new ways of consuming. However, mere newness is often not enough to satisfy these consumers—they are often highly knowledgeable about the products and services they purchase and need to be convinced that a new offering will provide better and/or different value relative to the old one. Thus, these consumers tend to be existing category users who seek the very best and are willing to pay for it. Such users are likely to be customers of the competitor that currently offers the most advanced

technology or best product. These consumers are likely to view themselves as capable and sophisticated buyers of products in the category and will be skeptical of empty claims of superiority.

Customer Intimacy Ritz-Carlton, Nordstrom's, and Intuit are companies that create value through customer intimacy. Firms that select customer intimacy as the primary means of delivering value to customers focus on building strong customer relationships through solutions that are tailored to their unique needs. Such firms have organizations that are relatively flat and management structures that empower front-line employees. The culture is flexible and customer-driven, with employees' rewards being tied to customer satisfaction and loyalty measures. The offerings of customer-intimate firms appeal to customers who are emotionally involved with and seek self-expression through their purchases in the category. They desire an approach tailored to their needs and lots of personal attention. When surprises occur and when their needs change, these customers expect companies to be both responsive and adaptive. Firms that are customer intimate may be best able to attract a subset of the market leader's customers who are dissatisfied and open to switching to an option that is more tailored to their needs.

It is difficult for a firm to excel at more than one value discipline because the different disciplines are served by distinct processes, management systems and structure, and culture. However, successful firms must perform in accordance with the industry standard on the remaining two disciplines at which they do not excel. Thus, Apple, which has adopted a product leadership approach with its computers, must not only offer new, cutting-edge computers that replace the company's older models, it must also have operations that enable it to produce and distribute computers with reasonable efficiency and a product line that accommodates variation in customer needs for attributes like memory capacity.

TARGETING DYNAMICS

Our analysis of segmentation and targeting suggests that there are a variety of approaches to growing and sustaining a firm's position in the market. In this section, we examine issues that arise over time.

For established firms in a product category, targeting begins by focusing on current customers and then moves to targeting competitors' customers and nonusers who are similar to current customers. However, if current customers and others like them represent a shrinking or stagnant segment, this approach may limit growth.

Consider the case of Old Spice, a line of men's toiletries. The brand was purchased by Procter & Gamble in 1990 so that the company could build sales in the high-margin men's deodorant business. Aside from its high margins, the deodorant business was attractive to P&G because consumers tend to be relatively loyal to their deodorant brand, which increases the average CLV in this category. However, at the time Old Spice was purchased, the average user was in his early- to mid-fifties. Since men of that age already had loyalty to a particular deodorant brand, stealing share was difficult, and Old Spice sales were stagnant. What is an appropriate strategy when faced with a loyal but stagnant or shrinking customer base? Should the firm focus on current customers or shift its attention to high-growth segments? The answer depends both on the reason for the stagnant or declining growth and on the relationship between current customers and higher-growth segments of the population.

Several years ago Entenmann's baked goods observed that its current customer base liked its product but was consuming less due to concerns about middle-aged "spread." The company considered expanding its customer base to include younger, less weight-conscious customers for its existing products. It also considered developing new, lower-calorie products for its aging current customers. Entenmann's chose to serve the needs of its current customer base with a low-fat line extension. In the process, they found that the low-fat products attracted younger customers who were concerned with health and fitness. Apparently, the new line of products served an unmet goal and thus stimulated category build while also sustaining current user consumption.

Old Spice, on the other hand, found success by shifting its focus from existing consumers to young consumers—new category users whose loyalty to a deodorant brand has not yet been established. The danger in shifting focus from one segment to another is that the new target consumers may be unconvinced by the product's new positioning, and they may continue to believe that the product is better suited for a different consumer. Although the Old Spice brand did face challenges overcoming its image as the product used by grandfathers, it was able to avoid many of these problems by "skipping a generation"—focusing on consumers who were less aware of who the brand's core customer had been. By 2004, Old Spice had become the top-selling deodorant for teen males.

As the Old Spice example suggests, distinct segments often do not wish to be affiliated with the same brand, so success with one segment undermines the appeal to another segment. Such was the case when Porsche introduced the Cayenne SUV. Prior to the introduction of Cayenne, 85 percent of Porsche cars were bought by men. Although Cayenne expanded Porsche's customer base by attracting female drivers, it also created backlash with male customers

who felt the Cayenne and the drivers it attracted diluted the sports-car purity and “chick-magnet” status of the Porsche brand. Such problems can be avoided if, as in the Old Spice example, consumers in one segment are unaware of how the product is marketed to the other segment. For example, clinical-strength deodorants, such as Secret Clinical Strength, are designed for consumers with above-average perspiration problems. As a treatment for problem perspiration, these products are often recommended by doctors and other health professionals. However, these products are also advertised to consumers without such problems but who are about to face “cannot fail” situations where sweating must be avoided at all costs (i.e., outdoor summer weddings, job interviews). These consumers might be hesitant to purchase a clinical deodorant if they associated it with having “problem perspiration.” However, because the problem perspiration use is primarily marketed to physicians, most consumers are unaware of this use.

SUMMARY

This chapter presents a usage-based approach to segmentation and targeting. We prefer this approach to alternative approaches for two reasons. First, the segments that are identified using this approach require distinct marketing *strategies*, not simply different marketing tactics. When current customers are targeted, the goal is to retain these customers and, if possible, expand their usage. When competitors’ customers are targeted, the goal is to offer a proposition that is sufficiently attractive to overcome switching costs. And, when nonusers are targeted, the reasons for abstaining from category consumption must be addressed. Second, the usage-based approach focuses on the costs and potential return associated with pursuing alternative targets. Current customers are easiest to reach and are most profitable to focus on in the short run. Attracting nonusers can be costly, but they may be important to sustaining the brand over the long run.

Alice M. Tybout is the Harold T. Martin Professor of Marketing and a former chairperson of the Marketing Department at the Kellogg School of Management. She is also co-director of the Kellogg on Branding Program and director of the Kellogg on Consumer Marketing Strategy Program at the James L. Allen Center. She is co-editor of Kellogg on Branding (John Wiley & Sons, 2005). She received her BS and MA from Ohio State University and her PhD from Northwestern University.

Kent Grayson is the Bernice and Leonard Lavin Professor of Marketing at the Kellogg School of Management. Before joining Kellogg in 2002, he served on the

faculty at London Business School for eight years, where he also directed the LBS Centre for Marketing for two years. He has written several published cases on segmentation and has worked on segmentation issues with a number of Fortune 500 companies. He received his BA and MA from the University of Michigan and his PhD from Northwestern University.

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