



Segmentation in B2B Markets

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WHAT IS MARKETING IF IT IS NOT ABOUT SEGMENTATION?

Satisfying people's needs and making a profit along the way is the purpose of marketing. However, people's needs differ and therefore satisfying them may require different approaches. Identifying needs and recognising differences between groups of customers is at the heart of marketing. We cannot do everything, we cannot satisfy everybody; resources do not stretch that far. This means we have to be clever in targeting our offers at people who really do want and need them, and we have to be strong in setting aside those who do not. We have to choose our target audience on the basis of our capabilities or just our strengths. In other words we have to choose our own battlefield where we are confident that we are more attractive than our competitors. This early observation is fundamental, as it requires us to think as hard about where we don't want to sell our product as where we do.

This brings us to the consideration of the difference between marketing and selling. Selling focuses on the product in hand and our pressure to get rid of it, almost regardless of the needs of the customer. It is clear that brutal selling may leave a customer with a product they wish they had never bought and therefore, they may never return as a customer again. Marketing takes a longer-term view. The matching of customers' needs and suppliers resources may take more time and effort but the customer is more likely to be comfortable with their decision and be loyal.

The fundamentals of marketing are the same fundamentals of segmentation. **Know your customers, know how they differ, and have a clear proposition that lights their fire.** We will return to these issues but first we will examine the differences between consumer and business-to-business markets, as our challenge is to arrive at a business-to-business segmentation.

THE DIFFERENCE BETWEEN CONSUMER & BUSINESS-TO-BUSINESS MARKETS

Business-to-business markets are characterised in a number of ways that makes them very different to their consumer cousins. The number of customers supplied by a chemical company is likely to number in the hundreds or small number of thousands in contrast to consumer companies that ultimately address markets of many thousands or millions.

Business-to-business customers range wide in their consumption of products. A few customers dominate followed by a long tail of customers with a comparative miniscule consumption. Private individuals have physical limitations in the amount of product a single person can consume. Companies, by comparison, do not.

The selection of a supplier in business-to-business markets is more complicated. Since people are buying on behalf of their organisation rather than themselves, there is (at face value) a greater pressure to be objective and rational about their decision. In business-to-business markets the buyers and specifiers may well know as much about the products purchased as the companies that supply them. Also, it is unlikely in a business-to-business situation that just one person will make the buying decision. A specifier may test and approve the product; a production manager may run it through trials; a board of directors



may impose an overriding structure on the source of supply; a buyer will almost certainly negotiate the price. Compare this with an item of clothing or personal care or food where an individual will have most sway, occasionally influenced by another member of the family.

The aim of segmentation in consumer markets is to bring the focus on to manageable groups of like-minded individuals who have a high disposition for a product. Coca-Cola has customers who want low cost drinks for consumption at home. It has customers who want a mixer or a non-alcoholic drink in a bar. It has customers who are hot and thirsty and want a cool refresher outside the Duomo in Florence. The same consumers may at various times join one of the segments and when they do, they will see the product in a different light and value it in a different way.

In business-to-business markets the aim of segmentation is similarly to arrive at clusters of like-minded companies. There is a very strong pressure to use segmentation in business-to-business markets to win a competitive advantage as there is often little to differentiate one product from another. Segmentation therefore links strongly with a strategy to achieve a sustainable differentiated position.

HOW TO SEGMENT

The benefits of segmentation are not hard to grasp. The challenge is arriving at the most effective groupings. In consumer markets, segmentation is almost always according to need i.e. the cola customers who need a drink at home or a mixer in the pub or a cool drink on holiday. However business-to-business customers have more complicated needs, which can make a needs-based segmentation both difficult and even dangerous. There is a saving grace in business-to-business markets – people who buy steel lintels in Japan use them in very similar ways to buyers of steel lintels in Germany. These similarities in the use of products have led many business-to-business marketers down the road of convenience segmentation i.e. a group of customers in France would be treated the same as a group of customers in Spain, except that the first group is spoken to in French and the second in Spanish. In other words, language is the criteria for segmentation and not needs. There are numerous examples of business-to-business companies segmenting their customers merely on the basis of their location in the north, midlands or south of England – a convenience for their sales force.

A variation to the segmentation philosophy in business-to-business markets is to apply a segmentation based on company size. We have seen that the consumption levels of business-to-business customers are so widely different that this often makes sense due to large companies usually thinking and acting differently to small ones. A further sophistication may be to classify customers into those who are identified as *strategic* to the future of the business, those who are important and therefore *key* and those who are smaller and can be considered more of a *transactional* typology.

These 'demographic' segmentations, sometimes referred to as 'firmographics' in business-to-business markets, are perfectly reasonable and may suffice. However, they do not offer that sustainable competitive advantage that competitors cannot copy. A more challenging segmentation is one based on behaviour or needs. Certainly large companies may be of key or strategic value to a business but some want a low cost offer stripped bare of all services while others are demanding in every way. If both are treated the same, one or both will feel unfulfilled in some way and be vulnerable to the charms of the competition.

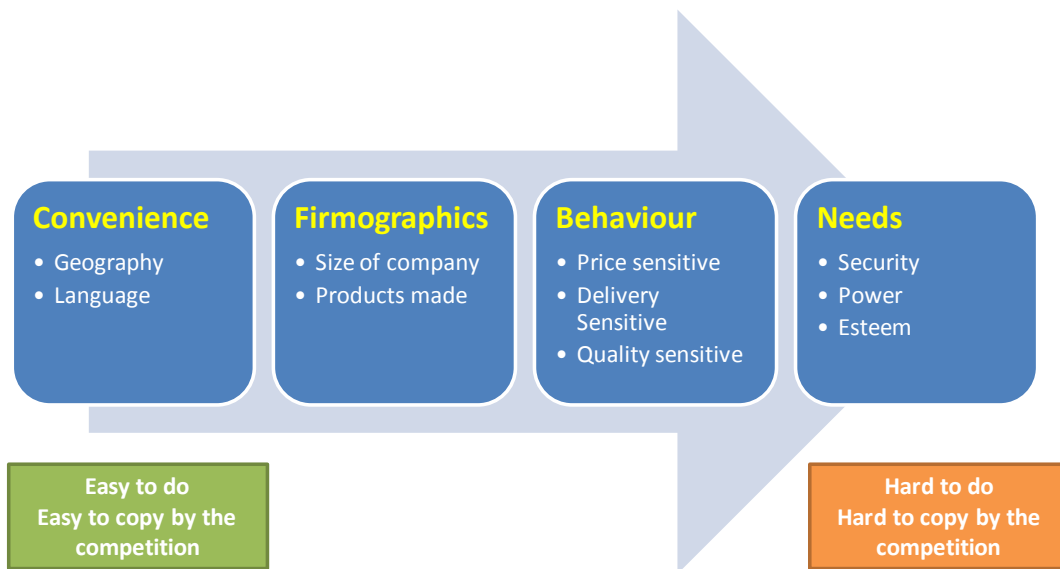
Needs are, of course, one of the most difficult things to assess. There are many questions that must be answered:

- Whose needs? Those of the production team or the customers? Those of the purchasing team? Those of the health and safety executive?
- And how consistent are those needs? Will they change from being price driven to technical driven as the buying negotiations proceed or if the customer develops a new product or hits production problems?

Treating a company as a price buyer when it needs technical service could frustrate both the customer and supplier. Recognising a switch from one classification to another may be easier said than done. The sales force may not be the best arbiters on this decision as there just may be a bias in favour of believing price to have a higher influence than is the case. The marketing team may not have their fingers on a sensitive enough pulse.

It is not easy to jump straight into a fully-fledged needs-based segmentation. Most companies are starting with some history of involvement in segmentation, even if it is only a north/south split of its sales force. Companies move down the road of segmentation learning all the way.

The Road To A Needs-based Segmentation



There may be problems in developing a needs-based segmentation but this is at least an aspiration to drive towards. The question is 'how?'

The starting point of any business-to-business segmentation is a good database. A well-maintained database is high on the list in any audit of marketing excellence in a business-to-business company. The database should, as a minimum, contain the obvious details of correct address and telephone number together with a purchase history. Ideally it should



also contain contact names of people involved in the decision-making unit, though this does present problems of keeping it up to date.

Management is frequently blissfully unaware of the parlous state of their databases as they are never involved in inputting and maintaining data. Sometimes the best database in the company is the Christmas card list held close to the chest of every sales person.

A comprehensive and up-to-date database is only the start of the segmentation process. A mechanism is now needed for determining every need of every company on the database. The commonsense approach may appear to be to ask them. However, what questions would you ask and could you be sure of the answers? It is not that people lie but they may not be able to acknowledge the truth;

- Do people really buy a Porsche for engineering excellence?
- Do people really choose an Armani suit because it lasts so well?
- Do people, who say they buy their chemicals purely on price, never require any technical support or urgent deliveries from time to time?

Sometimes the simple question and the straightforward answer is enough. At other times a more sophisticated approach is required. Statistical techniques (specifically factor analysis) can be used to show the association between the overall satisfaction with a supplier and satisfaction of that supplier on a whole range of attributes that measure the customers' needs. It can be determined that any individual attributes receiving high satisfaction scores must drive the overall satisfaction score and therefore be an important reason for choosing that supplier. In other words, instead of asking what factors are important, we can derive them. Buyers of Armani suits may show a strong link between overall satisfaction with the suit and attributes related to the brand and so point to the importance of the brand in the buying decision.

USING STATISTICS TO ARRIVE AT A SEGMENTATION

The classification data on questionnaires provides demographics data while questions in the body of the interview determine aspects of behaviour. Cross tabulations of data on these criteria allow us to see the different responses amongst groups of respondents. This is segmentation at its simplest level and every researcher uses the computer tabulations of findings to establish groups of respondents with marked differences.

However, we can use statistical techniques, in particular multivariate analysis, to allow more sophisticated segments to emerge. In a segmentation study (or even in a customer satisfaction study), respondents are asked to say to what extent they agree with a number of statements. These statements are designed to determine the needs and interests of the respondents. Typically there are a couple of dozen such statements, sometimes more. The possible combinations of groupings from 200 interviews is literally millions and we need some means of creating combinations that have a natural fit.

Using a technique known as factor analysis, statisticians can work out which groups of attributes best fit together. Looking through the different statements or attributes that make up these groupings it is usually possible to see common themes such as people who want low prices with few extras, people who want lots of services or add-ons and are prepared to pay for them, people who are concerned about environmental issues and so on.



Factor analysis reduces the large number of attributes to a smaller but representative sub-set. These sub-sets are then given labels such as “price fighters”, “service seekers” and any other such terms that help the marketing team know exactly who they are addressing.

The groupings of needs that have been worked out by factor analysis are now run through further computations using a technique known as cluster analysis. These factors are presented to the cluster analysis whose algorithms rearrange the data into the partitions that have been specified and so determine how neatly the population fits into the different groupings.

The statistical approach to a needs-based segmentation has become extremely popular and it is certainly an important objective means of finding more interesting and possibly more relevant ways of addressing the customer base. However, the tastes and needs of populations are constantly changing and we should always be mindful of new segments that may not show up as more than a dot on the current radar screen. For example, if Guinness had carried out a needs-based segmentation amongst its customers in the 1960s, it may not have recognized the opportunity to re-position the drink as young and trendy. This segment was developed by a series of astute marketing campaigns.

WILL THE SEGMENTATION WORK?

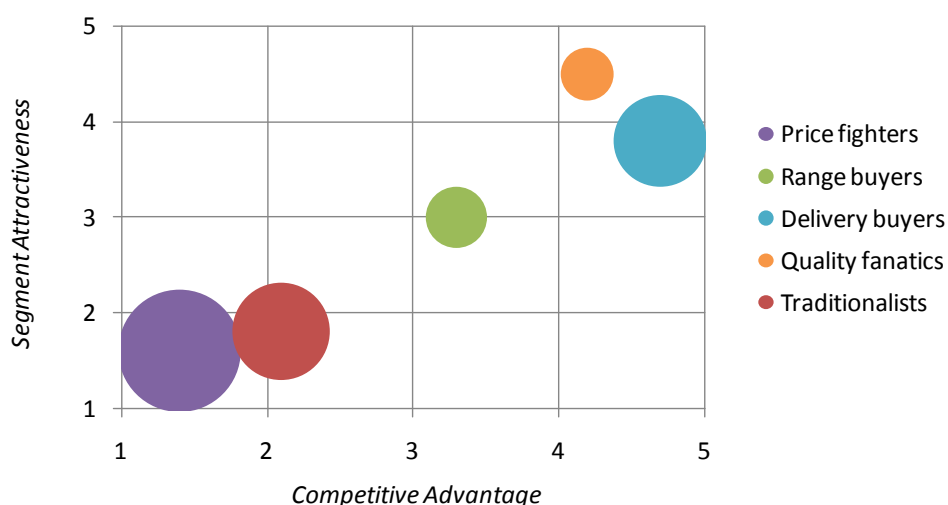
By whatever means the segmentation is arrived at, be it by judgement, by classifying the database or by statistical techniques, the segments must pass a three-question test:

- Are they truly different in a meaningful way? If not then they are not a segment and should be collapsed into one of the others. In determining, if and how segments differ from one another, it is helpful to give each a characterising nickname i.e. price fighters, range buyers, delivery buyers and whatever else suits. The name will ultimately become the shorthand description used in the company that immediately identifies the customer typology.
- Are the segments big enough? If they are not, they will require too much resource and energy.
- Can companies be easily positioned in one or other of the segments; especially new and potential customers, for otherwise the segments cannot grow? A company cannot be in more than one segment. This is unlike consumer segments where one week I may fit into an airlines business class segment and another week fit into low cost.

CHOOSING SEGMENTS TO WORK WITH

By plotting the different segments on an X Y grid¹ it is possible to determine which are worth targeting and, equally important, which are not. The two factors that influence this decision are the attractiveness of the segment against the supplier's competitive position within that segment. In this way it is possible to identify targets that justify resources in targeting and development. In the example below it may be thought that the price fighters offer no margin and are not worth targeting, even though they form a large segment. However, the traditionalists may be worth working on to see if they can be moved north and east to join a more attractive segment such as the range buyers, quality fanatics or delivery buyers.

The Directional Policy Matrix Used To Select (and De-Select) Segments



¹ The recommended tool to use here is The Directional Policy Matrix based on the methodology of Professor Malcolm H B McDonald of the Cranfield University School of Management



Segmentation is the first crucial step in marketing. It is often the mix of where-what-who and why (the benefit or need) which is driving the segmentation. The grouping together of customers with common needs now makes it possible to set marketing objectives for each of those segments. Once the objectives have been set, strategies can be developed to meet the objectives using the tactical weapons of product, price, promotion and place (route to market).



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