UNIT-3 Markets and Market Segmentation

Learning Outcomes

By the end of this unit the learner will be able to:

- ✓ Explain the meaning of a market.
- ✓ Identify different types of markets and explain their characteristics
- ✓ Describe the meaning and significance of market segmentation.

Unit 3

Markets and Market Segmentation

In the previous two units you have gone through the meaning, nature and scope of marketing and the marketing environment. In order to succeed in your marketing efforts, it is important to understand the characteristics of the market for your product and focus your efforts on the segment where there is likely to meet the most success. This is essential, as it is nearly impossible to sell one product to every single consumer, as not all consumers will have the same taste or buying capacity. In this unit you will study what marketing means, how markets are classified and the characteristics they possess. You will also be studying the meaning and importance of market segmentation, why segmentation is required and the basis on which segmentation is carried out.

What is a Market?

The term "market" has a number of meanings. It may refer to the place where a group of buyers and sellers are located. In Economics it refers to a collection of buyers and sellers who buy or sell a particular product or product range (electronics, fashion goods etc.). However there is a disagreement between marketers and economists, because in their opinion all the sellers constitute a market and all the buyers constitute the market for marketers. A market consists of all potential buyers who share a need or want that has to be fulfilled and who are able to exchange something in return for that need being fulfilled. Therefore for a marketer, a market is the group of all actual and potential buyers of a product. In this unit when we refer to the term market we will use the definition of a marketer, as opposed to that of an Economist. According to this definition, if there are 100 variants of a product are produced in a country, and then there exist 100 distinct markets, Therefore the market may be spread throughout the country.

Market Types and Characteristics

As you are already aware, individuals purchase numerous goods for their own consumption, business organisations procure goods for reselling, and manufacturing organisations procure goods for further production and so on. Therefore, there are several kinds of buyers who purchase goods and services, each having a different set of practises and procedures for securing their purchase. In order to understand a market, it is therefore essential to classify the markets on the basis of the kind of buyer. A market may fall into one of the following two, broadly defined, groups,

a) Consumer markets and
b) Organisational markets. Let us study these two types of markets in detail.

Consumer Markets

When we talk about consumers we mean all individuals and households who purchase goods and services for their own personal consumption. Therefore, the consumer market consists of buyers who buy goods for their own household use. The purchasing done in such a market is strictly to satisfy personal, non-business wants. For example, an individual buys goods such as toiletries, biscuits, meals etc for his/her personal consumption or family consumption. On the other hand, when an individual purchases goods to resell or for further production, such an individual does not belong to the consumer market. A characteristic of the consumer market is that, these final consumers are spread throughout the country and are numerous in number. Such consumers also vary by age, income, level of educational achievement, taste, preference etc. Consumer purchases are influenced by a number of factors such as; cultural, social, personal, economic and psychological characteristics of the buyer. The consumer buying process consists of five stages:

1) Recognition of a Problem
2) Searching for Information
3) Evaluating Alternatives
4) The Decision to Purchase and,
5) Post-purchase behaviour.

Organisational Markets

There are three types of organisational markets:

a) **Industrial Market:** Industrial markets consist of all individuals and organisations which purchase or acquire goods and services that are used, either directly or indirectly, for the production of other goods and services which are then either sold, rented or supplied to others. For example, sofa manufacturing factory purchases raw materials such as cloth, wood, cushions etc, this factory then produces the sofas and sells them. In this example the firm purchased the raw material to use for further manufacturing of sofas which are meant for sale. Major types of industrial markets include: I) agriculture, forestry, and fisheries, 2) mining. 3) Manufacturing, 4) construction, 5) transportation, 6) communication, 7) public utilities, 8) banking, finance and insurance, and 9) services.

b) **Reseller Market:** The Reseller Market consists of individuals and business organisations which procure goods that are resold to either industrial buyers or the final consumer of the product. If the reseller is a small wholesaler or a retail outlet, the purchasing process is carried out be a few individuals. However, if the reseller is a large scale reselling organisation, the purchasing is carried out by an especially dedicated purchasing department and if the product being bought is a new product item, the buying process is similar to that of an industrial organisation, discussed later. Likewise, in the case of standard items which have already been bought before, the purchasing process consists of standard operating procedures for reordering and renegotiating contracts.

c) **Government Market:** The Government Market is made up of government agencies (central, state and local bodies) which procure goods for the government. Government agencies procure a wide range of goods and services. Every product bought by the government has to fulfil specific criteria regarding the quantity, quality, price and source of the purchase. Generally government purchases are carried out through a tendering process and the tender is awarded to the supplier offering the lowest price. A unique characteristic to government buying is that government purchases are overseen by auditors and other interested parties. Auditors and Controller General ensure that the proper procedure is followed. The media is also interested and investigates to see how the public wealth is being spent. Because government organisations are accountable to the public, they have to follow a strict procedure which generally includes a lot of paper work. A number of forms must be completed and the approval of a number of authorities must be sought before a purchase can be made. Marketers must find a way to get through this red tape.

When dealing with the organisational market there are a number of things we must consider that we do not have to consider with the consumer markets.

1) Industrial organisations make their purchase decisions on the basis of reducing costs and increasing profits. These organisations set certain criteria that the products must match and then go out in the market and purchase the products.

2) More people are involved in the organisational buying process than the personal buying process. Each individual involved in the organisational buying process has a different responsibility and a different criterion for their purchase decision.

3) The organisational buyers have to follow formal policies, procedures and standard operating procedures established by their organisations.

4) The buying process involves paper work and formalities such as request for quotations, proposals, purchase & tracts, etc., which add another stage in the buying process not found in consumer buying.

Main Features of Organisational Markets

There are certain aspects of the industrial market that differentiate it from the consumer market. These aspects are described below:

1) **Fewer Buyers:** Generally speaking there are fewer organisational buyers as compared to household buyers. Therefore, an industrial marketer normally deals with a smaller market than a consumer marketer. For example, if a tyre manufacturing company wants to sell its tyres in the industrial market, it may focus its attention on one of the large car manufacturing concerns.

When the same company wishes to sell tyres to the end consumers (vehicle owners) it may have to contact thousands of car owners.

2) **Larger Buyers:** Organisational buyers usually demand a larger quantity of product than household buyers. Therefore, industrial buyers are large scale buyers. Even in the industrial buyer market, some larger companies will account for a greater proportion of the purchases. In such industries as automobile, electronics, toiletries, tobacco, synthetic yarn etc. a handful of the larger manufacturers account for a majority of the output. These industries account for a major share of raw material brought in the market.

3) **Geographical Concentration:** As opposed to consumer markets, industrial markets are not geographically spread out. The consumers in this market will be centred on a few geographical locations such as major cities. As a result, the marketing network for Industrial Markets does not need to be spread throughout the country.

4) **Derived Demand:** The demand for industrial goods is derived from the demand for consumer goods. For example, in the fashion goods industry, the demand for cotton will depend on the demand for clothes, as the demand for clothes rises and falls, the demand for cotton will rise and fall as well. Therefore the demand for industrial goods is derived demand

5) **Inelastic Demand:** The price elasticity of demand for industrial goods is lower than it is for consumer goods. This means that the quantity demanded is not affected, as much, by the price of the good. For example in the fashion industry a lower price of cotton will not necessarily cause an increase in the purchase of cotton from a clothes manufacturer. However, if the demand for clothes from the end consumer increases, there will be a higher demand for the cotton for manufacturing those clothes. Similarly, an increase in the price of cotton will not necessarily decrease the demand for cotton, unless a cheaper substitute is available or there is a way to use less cotton for the same amount of output of clothes. Demand is especially inelastic in the short run as it is nearly impossible to change output in the short run. Similarly demand is also inelastic for industrial goods that make up a small portion of the total production cost of the product. The price will have an impact in terms of which producer to buy from, although the buying quantity will not be impacted.

6) **Fluctuating Demand:** The demand for industrial goods is more volatile than the demand for consumer goods. This phenomenon is especially pronounced in the demand for industrial equipment such as plant and machinery. This is because as the demand for consumer products increases the demand for industrial equipment will increase by even more and when the demand for consumer goods decreases the demand for industrial equipment will decrease by even more. This phenomenon is known as the acceleration principle in economics.

7) **Professional Purchasing:** Most organisations have professional buyers staffed in their purchasing departments. Additionally there are professional trade journals that can guide the purchasing decision of these professional buyers. Consumers however do not have this level of support and therefore do not buy as carefully. Furthermore, in industrial purchasing there may be specialists involved in the purchasing department for the purchase of complex goods. Purchase committees may involve several people from a number of different departments which may include experts and people from the senior management.

8) **Miscellaneous Characteristics:** Some additional characteristics must also be taken into account.

   a. **Direct purchasing:** Industrial buyers will more likely buy directly from the producer of goods/services instead of buying through a middle man; this is especially true for goods/services which are complex or technical.

   b. **Reciprocity:** Industrial buyers will usually buy from suppliers who will in turn buy from them. For example a truck manufacturer will most likely buy steel from a company which buys its transport vehicles. Even in this reciprocal buying, the buyer will make sure to get the supplies at a competitive price, of proper quality and service.

   c. **Leasing:** Organisational buyers are most likely to lease their equipment instead of paying the full amount up front. This happens with computers, machinery, packaging equipment, heavy construction equipment, delivery trucks, machine tools and automobiles. Leasing equipment has a number of advantages which include; reduced upfront investment, ability to purchase the most up to date products, tax advantages etc. The advantage for the leaser is that it gets more income by being able to sell to more consumers, who may not otherwise have been able to afford the products.

Major Type of Buying Situations: An organisation buyer will usually face three major types of buying situations:

- **Re buy:** Re buying the product from the same supplier, this is a routine re purchase decision
- **Modified re buy:** This is when the same type of product is bought from the same supplier but the product specs i.e. quality, is different. New terms have to be agreed and some research may need to be carried out.
- **New Purchase:** A new purchase where the products and suppliers need to be researched and new contracts need to be drawn up.

What is market Segmentation?

In the real world both suppliers and buyers will exhibit a lack of homogeneity. For suppliers this lack of homogeneity may be the result of factors such as, difference in production equipment, processing or production technology, level of skilled workforce and varying availability of raw material, all these factors may cause heterogeneity. As a result of these imperfect markets- markets in which firms lack uniformity of size and product- are common. Segmenting the market may help reduce this problem to some extent.
Now let's discuss market segmentation. As I have already discussed above, a market is defined as the set of all actual and potential buyers. This means that the buyers in a given market will be seeking products for the same function. However, these said buyers will have different criteria to evaluate how a product will fulfil the function for which it is meant for. This means that within one overall market there will be submarket which differs from one another. This lack of homogeneity within the overall market may be due to differing buying habits, purchasing power or the difference in the motive for buying a product. It is due to this reason that it is necessary to divide the overall market into submarkets which help ensure successfully marketing the product. This process of dividing the overall market into sub categories based on differing buying criteria is known as market segmentation, with each market segment being homogenous in all significant aspects, unlike the overall market.

Following from the above discussion, we can now say that a market segment refers to a submarket of the overall market which is homogenous in all significant aspects. Market segmentation allows the marketer to have multiple marketing strategies, one for each segment of the market.
A market segmentation strategy would begin by the marketer to first divide the overall market into sub segments which depend on the buying behaviour or other key aspects of the intended customer; this would obviously involve identifying these customer groups. Market segmentation would also allow focusing the marketing strategy towards the segment which yields the highest return on effort and investment.

There are three other strategies in marketing which may be pursued these are: 1) undifferentiated marketing 2) differentiated marketing and 3) concentrated marketing. In undifferentiated marketing, no segmentation is carried out; only one marketing programme is followed. Differentiated marketing involves designing separate marketing programmes for each segment. Differentiated marketing is usually an expensive alternative to follow as it requires customisation of the product and promotion material for each segment of the market; this will also increase the administrative cost of the business. Unless the segment is big enough to justify the cost, these customisation costs may be a burden on the marketer. Finally, in concentrated marketing the producer concentrates its efforts on a few lucrative segments and ignores the rest.

Of the above mentioned strategies, homogenous marketing is best used for a market which is homogenous whereas for a heterogeneous market it is best to use either a differentiated or a concentrated market approach. The marketing strategy deployed will also depend on the stage of the product life cycle that the product is in. In the initial stages of the product life cycle an undifferentiated marketing strategy is suitable to help build demand. In the later stages, especially when the market is concentrated with many product offerings, either an undifferentiated or a concentrated approach is best.

Market segmentation and product differentiation are two separate concepts and should not be mixed up. Product differentiation is usually carried out in homogenous markets where the product offering is quite standard. Product differentiation is carried out to set one's product apart from the other products in the market in order to eliminate product competition. However to reduce competition, in addition to product differentiation, a strategy of market segmentation may also be carried out. Market segmentation may be carried out to increase a share of the market. It may be said that the product differentiation seeks to secure a layer of the market cake, whereas market segmentation strategy strives to secure one or more wedge-shaped pieces. Unlike product differentiation, market segmentation is only a short term strategy to help capture more market share.

Importance of Market Segmentation.

When a product is marketed, it is nearly impossible to market to all buyers in a given market. There are many buyers, widely scattered, and with varying requirements and buying habits. Some producers may be able to serve one segment better than the others. Every competitor in the market has to identify the market segment which it can most effectively serve. Market segmentation has the following advantages:

a. Instead of wasting your resources on marketing to the entire market, you can concentrate your marketing efforts on one given segment.

b. Because a single segment is being served, the product offering can be customised to the particular requirements of that segment of the market.

c. It helps to pay proper attention to particular areas.

d. By segmenting the market you can adopt different policies that are suited to each segment of the market.

e. Advertising and promotion can be customised towards each segment, thus enabling the efficient use of advertising channels.

f. Overall there is a more efficient use of the marketing resources

g. Every one of the 4Ps of the marketing mix (product, price, promotion and physical distribution) can be customised to suit the target market in mind.

Requirements for Segmenting a Market

If a market segment is to be useful it must exhibit the following qualities:

Measurability: Measurability is the degree to which the market segment can be ascertained. Certain segment characteristics are difficult to measure. For example, it is difficult to measure the number of teenagers who smoke as an act of rebellion against their parents.

Accessibility: Accessibility refers to how easily a market segment can be reached and served. For example, a perfume manufacturing company may discover that the heaviest user segment for its products is single men who are out late at night. Unless all such men live in a single geographical location, it will be very difficult for this company to identify them. Therefore when segmenting a market, the marketer must ensure that each segment is accessible and approachable.

Substantiality: Each segment should be sizeable enough to ensure a return. The segments should be sizeable enough to ensure the largest possible homogenous group worth going after with a single definite marketing programme. For instance, for a car manufacturer it may not be possible to manufacture vehicles for consumers who are over 7 feet tall, as the size of such a specific market is quite small.

Actionability: This refers to the ease with which marketing programmes can be formulated for serving a given segment of the market. For example a tourism company may identify seven segments of the market; however their staff may not be large enough to serve all seven

Bases for Segmentation

As already discussed, market segmentation involves dividing a single heterogeneous market into sub parts which are homogenous in all major respects. However, there must be a basis on which the market is segmented. In order to segment the market various variables may be used. As discussed above, markets may be classified as either consumer or organisational markets. Some of the widely used characteristics for segmenting these two markets are discussed below.

Bases for Segmenting Consumer Markets
Broadly, there are four bases for segmenting the consumer market. They are:

1) Geographic
2) demographic
3) psychographic and
4) behaviouristic factors.

Geographic Segmentation:

Segmentation on the basis of geography calls for dividing the market into unique geographic units such as countries, states, regions, cities, neighbourhoods etc. The company will decide to focus on a few geographical locations when the market is segmented in this manner and customise its offerings for the customers of each location; the customisation will take into account preferences and needs of the customers.

Demographic Segmentation

Demographic segmentation is when the market is divided into sub groups based on demographic characteristics such as age, gender, family size, income level, occupation, level of education attainment, religious beliefs, race, nationality etc. Demographic characteristics are the most commonly used basis for segmenting a market. This is because consumer preferences are usually associated with demographic characteristics. Even when the target market is described in non-demographic terms (say, a personality type), it should be linked back to demographic characteristics in order to know the size of the target market and to reach it effectively. Another reason for using demographic characteristics is that these variables are easy to measure. Some commonly used demographic basis are discussed below

- **Age and life cycle stage:** The needs of the consumer vary with age. For example, new born infants differ from toddlers in terms of food consumption and what they eat. A toy manufacturer may capitalize on this and decide to segment the market into, let's say, 12 segments based on the age of the consumer. Such a strategy of segmentation will allow the customer to identify the toy that most suits their requirement simply by considering their age.

- **Sex:** Market segmentation based on gender is especially prominent in products such as clothes, cosmetics, magazines etc. You may occasionally see gender based segmentation in other products as well for example garments, soaps and toiletries. Finally another example of a product which has just recently started to segment the market is the two wheel automobile industry, which has in the past only been targeting the male segment of the population. However, with the increase in the number of females who are now working, some manufacturers have started to design scooters for women.

- **Income:** Income based market segmentation is common in industries like automobiles, clothing, cosmetics and travel. Other industries use income as a basis to segment the market as well. The market may be segmented in terms of low, middle and high income groups. Price differentiation may be used to target each group. Generally speaking, towards the lower income groups, as the price goes up other non-economic considerations or basis become more important. As the income goes up other non-economic considerations or bases have a greater influence.

Psychographic Segmentation

Psychographic segmentation is when a market is segmented on the basis of social class, life style, personality characteristics etc. Individuals within the same demographic group may exhibit very different psychographic profiles. Some of the more commonly used psychographic characteristics are used below.

- **Social class:** Social class may influence an individual's buying habits for products such as cars, clothing, leisure activities, reading habits etc. There are many companies which produce and market their products based on social class. Marketing strategies then appeal to consumers belonging to one of those social classes.
- **Life style:** Lifestyle influences people's interest in various goods and services. In fact, consumption of certain goods and services itself portrays lifestyle. Lifestyle is increasingly becoming an important psychographic basis of market segmentation. For example, a manufacturer of blue jeans may design jeans styled for a specific male group. Each group may have its own requirements in terms of the design of the product, price, advertising appeal, availability and distribution etc. Unless the producers can adopt a unique marketing strategy for each group, the product may not appeal to anyone.

- **Personality:** Marketers also use personality variables to segment markets. They design their products with appropriate brand images that correspond to consumer personalities.

Behaviouristic Segmentation

When considering behaviour segmentation, the market is divided into segments on the basis of their knowledge, attitude, use, or response to a product. Many marketing professionals are of the opinion that behaviour based characteristics are the best starting point for identifying market segments. Some of the most commonly used behaviour based characteristics are discussed below.

- **Occasions:** The first such characteristic is the occasion or event when a consumer purchases a product. An example of this is when tourism services are sold depending on festivals and occasions- honeymoons, summer vacations etc. Similarly a tourist bus operator can uses occasions to segment the market and serve one such market segment. . Occasion segmentation can help firms build up product usage. For example, lemonade may be commonly consumed during a tour. A lemonade producing company may want to promote its product in tourist areas.

- **User status:** Many markets can be segmented into non-users, ex-users, potential users, first-time users and regular users of a product. Companies with the largest market share will be most interested in potential users. Potential users and regular users require unique marketing strategies and promotion strategies.

- **Usage rate:** Markets may also be segmented on the basis of usage so for example you may segment the market in terms of light, medium and heavy user groups. Another name for this is Volume Segmentation. An interesting feature of such a segmentation strategy is that heavy users, while accounting for a small proportion of the market, account for a large proportion of consumption of the product.

- **Loyalty status:** As you may be aware, consumer loyalty- towards brands, products, retailer's etc- is a commonly found trait in most markets. A market, therefore, may also be segmented in terms of consumer loyalty. lets consider brand loyalty. Suppose there are five brands A,B,C,D and E. Buyers can be divided into four groups according to how loyal they are towards a brand.

i. **Hardcore loyalists** these are consumers who only buy one brand, all the time. Thus, a buying pattern of A, A, A, A, A, A, represents a consumer who is a hardcore loyalist to brand A.

ii. **Soft-core loyalist** these are consumers who will purchase two, maybe three, brands all the time. Thus, a buying pattern of A, A, B, B, A, B, represents a consumer with a divided loyalty between A and B.

iii. These are consumers who shift their loyalty from one brand to another. The buying pattern A, A, A, B, B, B, would suggest a consumer who is shifting brand loyalty from A to B.

iv. **Switchers** these are consumers who have no loyalty towards any given brand. The buying pattern A, C, E, B, D, B would suggests a non-loyal consumer. Every market consists of the above mentioned four types of buyers and a customised marketing and promotional strategy is required to reach each of these market segments.. A brand-loyal market is one with a high proportion of buyers who exhibit hard core brand loyalty. A good example of this is the market for toothpastes which exhibits a high degree of brand loyal consumers. Competitors operating in a brand loyal market face a difficult challenge in gaining market share, likewise companies trying to gain a foothold in such markets also face a difficult time entering such markets.

v. **Attitude:** Consumers of a product can also be segmented by the degree of their enthusiasm for the product. On the basis of attitude five types of consumers can be identified: enthusiastic, positive, indifferent, negative, and hostile. A door-to-door campaign can assess the general consumer attitude towards your product; sales personnel who are involved in the campaign can assess the attitude of the households and decide about the time to be spent with them. Accordingly more time may be spent with enthusiastic prospects reminding them to buy. Likewise spending excess time with negative or hostile prospects may be a waste of time. To the extent that attitudes are correlated with demographic descriptions, the organisation can increase its efficiency in reaching the best prospects.

Bases of Segmenting Organisational Markets

Many of the grounds for segmenting consumer markets discussed above can also be used for segmenting organisational markets. Organisational markets can be segmented geographically and by several behaviouristic variables, benefits sought user status, usage rate, loyalty status, and attitudes. The following three grounds for segmentation are the most commonly used:

a) Type of customer
b) Size of customer, and
c) Type of buying situations.

Type of Customer

A common way to segment industrial markets is by identifying the end users i.e. the consumer. Different end user/consumers seek different benefits from the product and may in turn be approached using a different marketing mix. Different end users often seek different benefits and can be approached with different marketing mixes. As already discussed some of the major industrial markets include:

1. Agriculture, Forestry and fisheries,
2. Mining,
3. Manufacturing.
4. Construction.
5. Transportation.
6. Communication,
7. Public utilities.
8. Banking, finance and insurance.
9. Services.

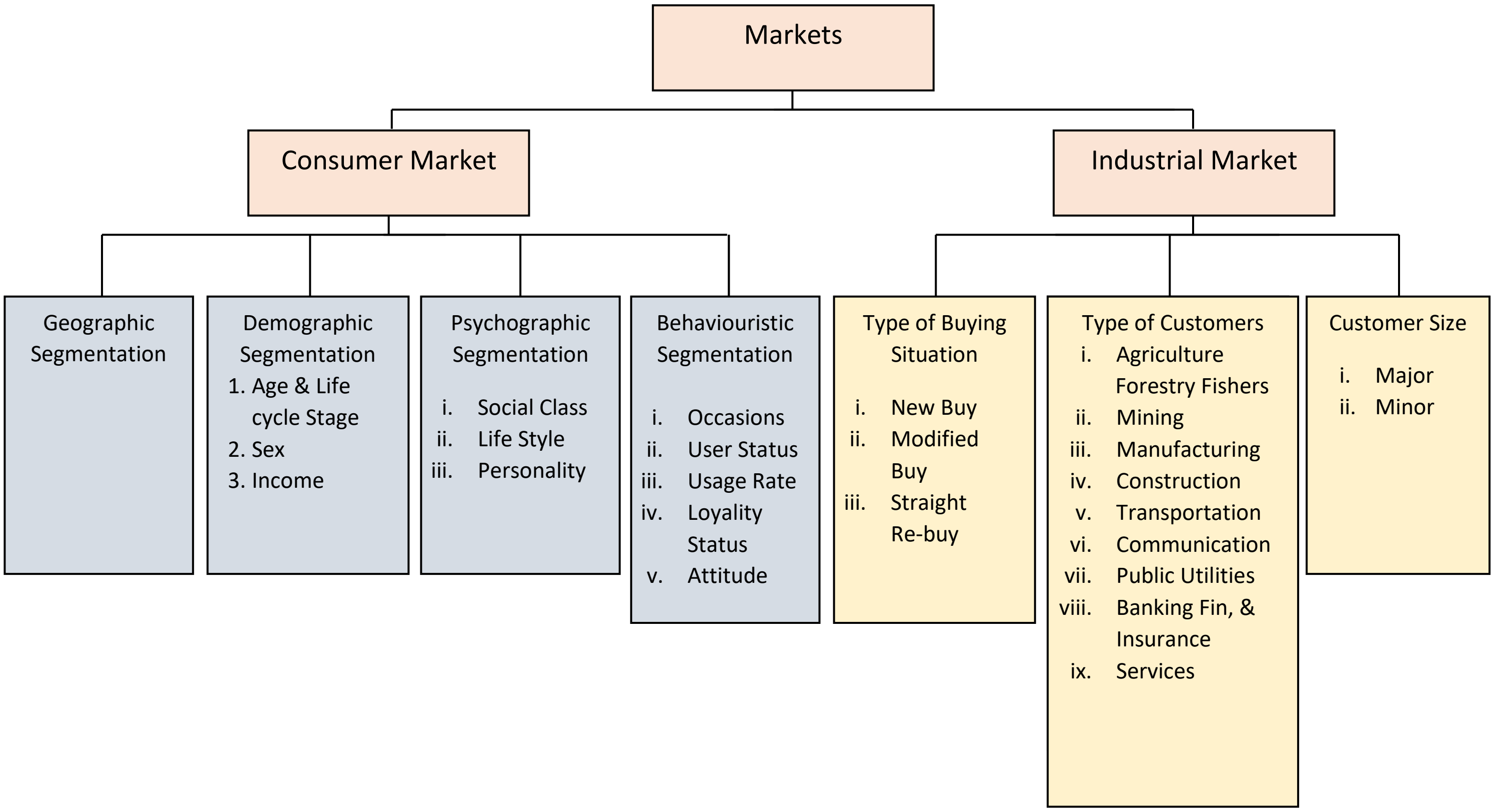
This, above mentioned classification, is an accepted classification known as Standard Industrial Classification (SIC) Code. Each of these markets can be further divided up to very minute levels and, accordingly, directories of industries are published.

Customer Size

Another variable that may be used for segmenting organisational markets is the size of the customer. A commonly seen practise in many companies is separating the customer facing departments in terms of those dealing with small customers and those dealing with larger customers. For example Steelcase; a large office furniture manufacturer, divides its customers into two groups; Major Accounts and Dealer Accounts. Accounts of large and reputed companies are dealt with by Major Accounts. These accounts are looked after by National Account Managers who work with District Field Managers. Smaller accounts are categorised as dealer accounts. These accounts are looked after by the Field Personnel who work with franchised dealers who sell Steelcase products.

Type of Buying Situations

We have already gone over the three types of buying situations: 1) new buy. 2) Modified buy. and 3) straight re-buy. These buying situations, as you know, are different from one another in a significant way. An industrial seller can segment his market on this basis of buying situations and adopt marketing strategies accordingly. Look at Figure 3.1 carefully. It summarises the discussion on bases of segmenting the market.



Further Reading:

- ✓ ***Market Segmentation,(2012), By Malcolm McDonald***
- ✓ ***Market Segmentation in Markets,(2009), By Natalie Zonis***