

Customer Segments Matter

Define and manage them in the organization so that their value is specifically differentiated.

Many companies articulate detailed segment plans, but few define and manage their segments in ways that allow the organization to easily differentiate the value it offers specific groups of customers. As market polarization widens the gap in the lifetime value of various segments and fragmenting customer needs create opportunities for specialist competitors to go after niche segments, companies need to get better at identifying and delivering distinctive value to their most attractive customer segments.

One implication of failing to define and manage segments is, it's extremely difficult to understand how much customer migration (defined as satisfied customers spending more, or dissatisfied ones spending less) occurs, much less measure its financial impact or actively manage it through differentiated customer propositions and experiences.

Consider a typical, large retail bank that plans and tracks performance by product group, such as checking, credit cards, and mortgages, and by channel, such as branches, phone, and mail. The bank compares sales, costs, profits, attrition rates, cross-sell penetration, and customer satisfaction across products and channels. But it doesn't link performance in individual customer segments like investors, retirees, homeowners, renters, and students with aggregate financial objectives and results. The bank also lacks a process to modify its tactics as customers move within and across segments. Last, for historic reasons the bank organizes and manages accountability along product, channel, and geographic lines.

As the bank's customer segments become increasingly fragmented, operating without an understanding of segment dynamics becomes extremely costly. For example, in an environment of rising interest rates, the bank does not understand that a substantial portion of its investor segment is shifting large portions of short-term liquidity balances to competitors. Even though these customers report no changes in satisfaction levels and have no intention of closing their accounts, their annual contribution to the bank's profits has been reduced by 60--70 percent. Unfortunately, without a plan or the ability to measure results along segment lines, the bank won't redesign products and restructure pricing.

The bank, as part of its planning and performance management process, needs a blueprint for what changes must be made in customer acquisition, product or service usage, and attrition rates within and across customer segments. The plan would yield a set of customer proposition and experience initiatives aimed at goals like growing usage in the renter segment. Additionally, this would have organizational implications, since individuals and groups would be accountable for specific segment sales, profit, retention, and experience targets.

The imperative for the bank, and many other companies, is to measure, understand, and focus management attention on what is happening within and across segments, on how that relates to aggregate business or marketing plans, on implications for performance management, and on the organizational changes needed to effect segment-level change. In practice this means:

- Choosing a useful segmentation approach and creating explicit linkages between segment objectives and overall business goals.
- Building formal mechanisms within the planning, measurement, and performance management processes to effectively manage customer segments.
- Creating organizational accountability for segment results. Segment owners should augment rather than replace the product, service, and functional aspects of the organization, and be held accountable for segment-level results.

Executing segment-based strategies requires organizational change and a significant reorientation of planning and performance management processes. Taking the plunge is worthwhile, not just because of the financial rewards it can yield, but also because doing so will catalyze a closer relationship between the company and its customers.

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