decode Science Update 2_2012

Customer segmentation –
New approaches from Behavioural Economics

November 2012

Welcome to the decode Science Update

Customer segmentation is key for effective Marketing. We segment on the basis of demography, attitudes, life-stage/style, values, motivations or functional needs in order to derive ideas for innovation, assess commercial potential and manage the marketing mix. There's a major challenge here: the traditional ways of segmenting have no direct reference to buying patterns and/or customers' decisions, and they often only give a rough idea for implementation at Touchpoints rather than concrete guidelines.

Research from the field of behavioural economics introduces another approach to customer segmentation that applies directly to the crux of marketing: (buying) decisions. This new technique is based on the idea of **segmenting customers according to how they decide**.

Science has revealed the most important decision-making strategies of consumers and these yield **fascinating possibilities for marketing**. Using examples, this Science Update shows how this type of segmentation generates better understanding of (buying) decisions and how it helps to accurately target offers.

We hope that you enjoy reading it.

Your decode Team

Dr. Christian Scheier   Dirk Held   PD Dr. Martin Scarabis   Johannes Schneider   Dr. Dirk Bayas-Linke   Dr. Björn Held   Tobias Eckert   Juliane Matussek

Example 1:
Maximising vs. Satisficing

Maximising vs. Satisficing (1/2)

The first example of decision-making rules is something we can recognise from our own behaviour, and that of others: Those **who, when deciding, always want the best**: They make special requests when ordering at a restaurant, they insist on looking in a second or third shop to check whether there's something more suitable, or the huge choice offered online means they can't decide because there might be a handbag or suit that looks even better. **Then there's another strategy for deciding on a product**: The first shirt that is suitable is bought and the search is over. The first option that meets the requirements is a done deal, or the brand is trusted and it's bought without any thought or need for more details. **Nobel Prizewinner Herbert Simon characterises these two decision-making strategies as *Maximising* and *Satisficing*.** The comparison table below shows the components of these strategies:

Maximiser	Satisficer
• Only the best will do	• Good enough will do
• Always concerned that they haven't got the very best	• Not worried that they might not have the best
• Happy only if they have the best	• Happy if their needs are met – it doesn't have to be the best

Maximiser means never being satisfied, always searching for the optimal solution and being ready to make more effort for its purchase.

Satisficers take the first choice that's just good enough. They don't want to look for a long time and don't expect any significant added value from a longer, more time-consuming search.

Depending on the subject, product category or time available, sometimes we're Maximisers, e.g.. with our hobbies, and sometimes Satisficers.

Maximising vs. Satisficing (2/2)

The great advantage of distinguishing between Maximisers and Satisficers is that this applies **directly to customers' decision-making**. It establishes a closer connection to buying patterns. A study by the well-known consumer researcher Ratneshwar showed this for online shopping: **Maximisers search more intensively for information, and browse product sites for much longer than Satisficers. Satisficers look at less information and, on the whole, are more superficial in evaluating offers.**

The decision-making strategy has a direct implication for the most effective way to market an offer. Maximisers need lots of options from which to choose whereas for Satisficers a reduction in the number of offers, or providing a preselection, increases the probability of a purchase. It's helpful for Maximisers to have the opportunity to compare options, while for Satisficers this is counterproductive. If you're not able to distinguish between these two groups, e.g. via surveys or tests, then you'll end up with an average offer that's not ideally suited to either of the two segments and/or decision-making strategies.

It is important that this is not a distinction of (personal) typologies in the traditional sense, but a **distinction between decision-making strategies**. The same person can prefer a Maximising strategy in one product category and a Satisficing strategy in another. So for fashion and clothing someone may buy the first jeans that come along, but with consumer electronics they only want the best. **So Maximiser and Satisficer behaviour can differ by product category.**

Maximising vs. Satisficing:
Implications for Marketing Practice (1/2)

Since Maximisers and Satisficers are clearly differentiated in their behaviour, it's important to recognise these two decision-making strategies and to tailor our marketing to them.

If a category consists of a large number of **Satisficers** – particularly the case for highly-developed, mature, markets – **incremental innovations engender much less elasticity** than in categories where Maximisers are in the majority. For Satisficers it's less motivating if something is marketed as *better* or *improved*, because they are happy with the existing solution. They don't go for the best, but are interested in minimising their risk and outlay. **Many innovations collapse because they're aimed at Maximisers, when actually Satisficers dominate in these product categories**. Rory Sutherland, Vice Chairman of Ogilvy Group in the UK, puts it like this:

*"Most people, in most fields of consumption, most of the time are NOT maximisers at all. They are something completely different. They are satisficers. What they are doing is not using insane amounts of mental energy to attempt to optimise every decision. They are instead simply trying to avoid making a decision that is actually bad or which might cause them to look or feel foolish. For those people, good enough generally is. (…) **The vast bulk of the money in any market at any time is in the hands of Satisficers**."*

It can be profitable to reduce product features for Satisficers and to pass on the lower production costs as a saving to customers. The success of Aldi or McDonalds is based on this principle: They don't have the best products or the best taste, but the quality is good enough. Consumption is often not about get ting the best, but about avoiding the risk of disappointment.

Yet there is a challenge: If you ask customers what they want, the Maximisers always seem to dominate. The classic kind of customer survey **invokes the maximisation strategy**. **Behaviour-based approaches**, for example **monitoring real seeking and buying behaviour,** are helpful in avoiding this distortion. To find out the Maximiser / Satisficer ratio in a product category, various, validated measuring tools and scales can also be drawn on.

Maximising vs. Satisficing:
Implications for Marketing Practice (2/2)

Segmentation by the rules of decision-making can be a springboard for **optimising the offer** (e.g. the number of options or product variants advertised), and also for the **sales process** itself: For example, buyers with a maximising strategy feel under pressure if a seller wants to persuade them to buy a specific product. So the sales process is more efficient if the seller adapts to the customer's preferred decision-making strategy.

This has important consequences for **After Sales** too. Studies show that advertising is primarily processed by people who have just bought the product or just used the service. So, as a rule, Maximisers are more dissatisfied with their decision ("..maybe I should have…") and messages have to reassure Maximizers about the good things about their decision and the advantages over other options. Overall, various studies show that Maximisers are less loyal and/or have to be specifically appealed to in order to become or remain loyal.

decode
implicit marketing

Example 2:
Persuasive Profiling

Persuasive Profiling (1/3)

Let's imagine we want to buy a book. We rummage through the offers, in a shop or online, to make a decision. There are lots of options so the choice isn't easy. Not only do the books' titles and contents differ, but also the **selling points** given to the books are diverse: Some books stay on the best-seller list, others go straight on price promotion, others are almost out of print or recommended by authors we hold in high regard. Research now shows that it's not only the book itself - or a product generally – but also these peripheral selling points that play an **important role in the decision to buy**.

People differ as to which selling point they react to most strongly. Some react more strongly to the best-seller argument. Others are persuaded by an expert's recommendation. But it's interesting that this disposition is stable across product categories, i.e. If we react more strongly to the bestseller argument with books, then we do the same with other products.

That's what Persuasive Profiling is all about: **Segmenting the buying public according to the basis of their (implicit) preferences for certain selling messages.** Offers are advertised differently, according to preference, in order to increase the probability of a decision to buy.

Persuasive Profiling (2/3)

To understand this fascinating approach better, let's take a look at the psychological process behind it. The central concept is **automated rules of decision-making (heuristics)**. These rules of decision-making are – like habits – activated by a signal and then *automatically* influence the subjective attractiveness of the products and, hence, influence the probability of purchase. Research has revealed a whole series of these heuristics, many of which have long been applied in marketing practice. Let's look at some examples:

Social proof heuristic: Buying what others are buying and/or recommending.

Authority heuristic: Buying what experts recommend.

Scarcity heuristic: Buying what is only on offer for a short time or in limited quantities.

The idea of segmenting customers according to how strongly they react to the particular heuristic and adapting how offers are presented is new. Heuristics exist in all of us and, if activated, automatically influence our behaviour. Some of us react particularly strongly to experts' recommendations, others to what other customers have bought etc. If we measure the reaction of customers to the various types of heuristic, we can get a persuasive profile for every customer.

Example of a persuasion profile: The profile shows how strongly a customer reacts to various types of heuristic. This example shows that the authority heuristic (expert recommendation) has the smallest effect and the consensus heuristic finance (what other customers recommend) has the strongest effect. So the offer can be specifically tailored for these preferences.
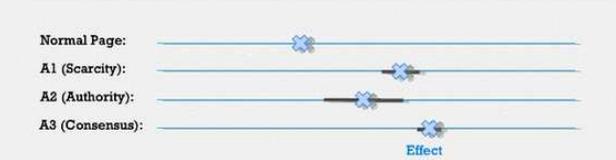
Persuasive Profiling (3/3)

The following example illustrates the principle of Persuasive Profiling: Philips Direct Life is a programme with which customers can check their physical activity, in order to lead a more healthy life. A customer's activity data, captured with special equipment (e.g. number of steps per day), is uploaded. Customers are e-mailed regularly as a reminder to upload / update their data and thereby use the service effectively. **The texts of the emails are adapted to fit to the customer's Persuasion Profile**. If someone is known to react strongly to the *Social Proof* heuristic, the email tells him how many other customers are participating in the programme and how often they upload their data on average. If someone reacts more strongly to the *Authority* heuristic, the email focuses on expert statements or recommendations (e.g. From doctors). Adapting the emails to the individual user's Persuasion Profile sigificantly raised the response rate (more than doubled!).

Reminder E-Mail   Persuasion Profile   Adapted Text Modules
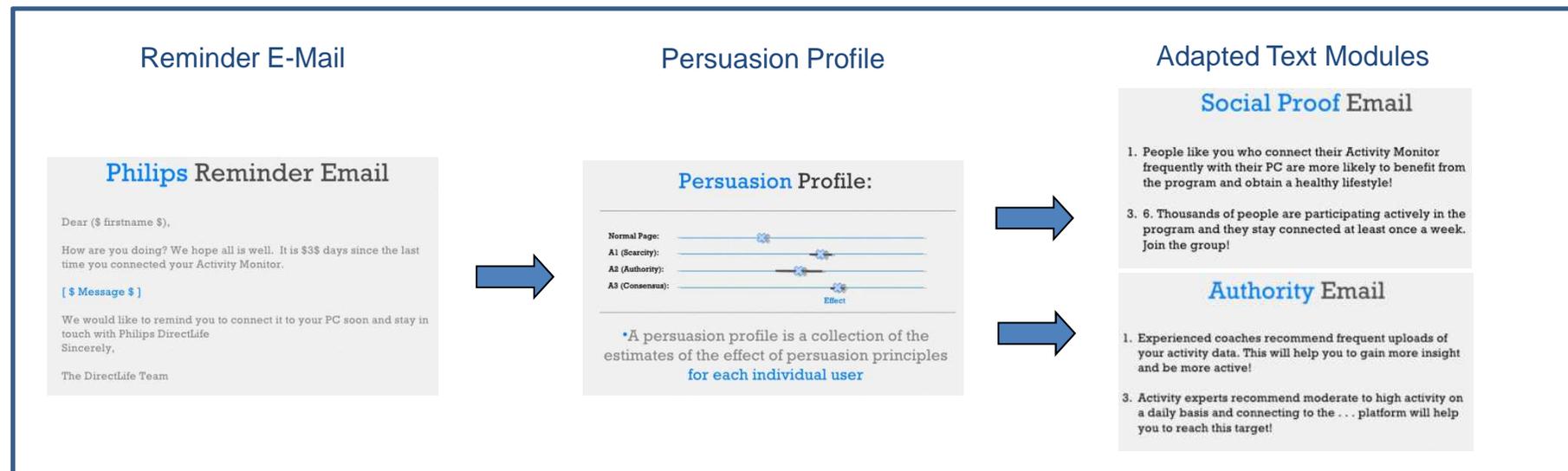
Implications for Marketing

Segmenting according to preferred rules of decision-making and/or heuristics gives us an additional segmentation approach that offers concrete ways for implementation (e.g. the design of emails, websites or promotions) and one which is directly applicable to the buying decision.

In the **Shopper Marketing** area this has some implications for the **mechanics of promotions**. If a producer knows for example that REWE (a German retailer) customers react strongly to the *Scarcity* heuristic, promotions can be signalled correspondingly (e.g. "*Offer only available till Monday*" , "*only 4 per person*" etc.). On the other hand, if most of its customers react more strongly to the *Social Proof* heuristic, the promotion or display can be designed accordingly. This can extend to the number of Facebook Likes for a product being shown in the deal, as C&A did in Brazil.

Example for using the *Social Proof* heuristic: C&A branches in Brazil display how many Facebook Likes an item of clothing gets, and hence how popular it is with other customers.

The most far-reaching implications are for **E-Commerce**. This is different from the offline world as, in the online world, the Persuasion Profile of a single individual can be identified. If an online trader or provider of information knows to which selling points or heuristic a user reacts most strongly, he can very easily direct advertising and present offers specifically for that user.

As the research shows that our preferences for certain heuristics are stable across product categories, online traders can also use profiles like this to go further. If you know what selling points someone reacts to for books, you can also use these for selling other product categories, e.g. clothing. Hence, Persuasion Profiles can have a substantial monetary value.

Further Tips & Literature

WIRED / MAGAZINE

Welcome to the Brave New World of Persuasion Profiling

Article in WIRED on Persuasion Profiling.

http://www.wired.com/magazine/2011/04/st_essay_persuasion_profiling/

Journal of Interactive Marketing
Volume 26, Issue 3, August 2012, Pages 176–188

ELSEVIER

INTERACTIVE MARKETING

A current study on Persuasive Profiling. It shows that individual profiles are important (and why), in order to increase the results of online marketing.

Heterogeneity in the Effects of Online Persuasion
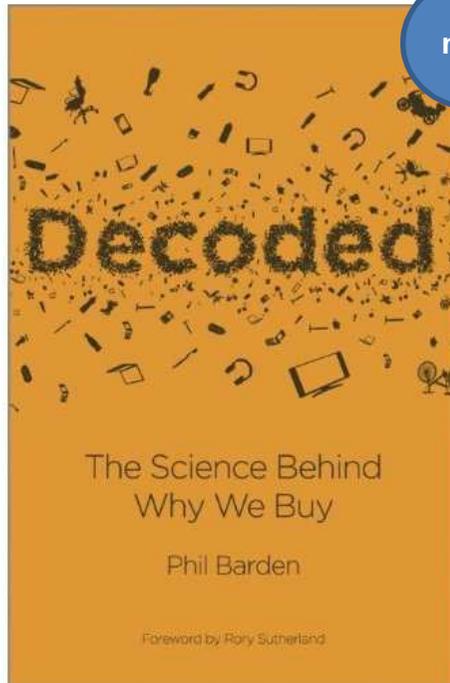
Maurits Kaptein[a, b], Dean Eckles[c]

[a] Eindhoven University of Technology, The Netherlands
[b] Philips Research, The Netherlands
[c] Stanford University, USA

http://www.sciencedirect.com/science/article/pii/S1094996812000035

On a Personal Note: New Book(in English)

new

In collaboration with Phil Barden, Managing Director of decode UK, we have completed a **new book**. It outlines the **latest findings from science** on why we buy what we buy:

- **Decision Science** – What determines our decisions.
- **Occasion Based Marketing** – How the situation influences buying patterns.
- **Behavioural Economics** – What insights behavioural economics provide.
- **Perception** – How attention is gained.

The latest research, and its implications for marketing practice, is based on many examples and **case studies – from product development to interactive media.** Rory Sutherland, the well-known pioneer in marketing thinking has written the Foreword.

Decoded – The Science Behind Why We Buy comes out in February 2013 from the renowned Wiley Publishers (ca. 250 pages).

We'd like to let you know as soon as the book is available. Just send us a short email with the subject heading *Decoded Book* to info@decode-online.de.

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Welcome to Dialogue

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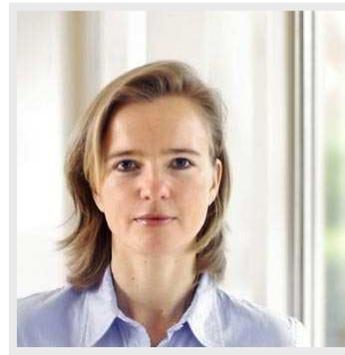
Graumannsweg 19
D – 22087 Hamburg
Telefon: 040 / 227 59 208

info@decode-online.de

www.decode-online.de

Dr. Christian Scheier
Joint Managing Director

Dirk Held
Joint Managing Director

Cornelia Bruns
Customer Relationship Management