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Marketing Segmentation Practices and Performance of Nigerian Commerical Banks

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Abstract

The paper examines the impact of marketing segmentation practices on the performance of selected Nigerian commercial banks in the post consolidation era 2005 to date.

Data employed were mainly secondary while the research design was exploratory in nature relating such basic variables as market segmentation practices of market share; pricing and geographical branch location to performance. Statistical test using Herfindahl Hirschman Index was used as surrogate for market concentration which was tested against performance. Findings indicate that banks with high level of market share demonstrate high customer retention ability and lower overall unit operating expenses.

Keywords: Market segmentation; Customer Retention Capability, Operating expense and Market share.

1.0. Introduction

Bank financial institutions make immense contributions to the advancement and development of an economy especially through their fund mobilization and intermediation roles. Commercial banks' capacity for resource allocation and smoothing of the payment system is considered of paramount importance that government in both developed and developing economies design special regulatory frameworks to control their activities; Mckinnon (1973) Shaw (1973), Day (1980), Soyibo (2002) and Oboh (2005). Prominent among such regulatory reforms in the Nigerian financial system are the deregulation and liberalization of the banking sector in 1986 as well as the recently concluded bank consolidation exercise of December 2005. Such reforms according to Soyibo (2002) have the potentialities for generating innovations, product development, new service packaging, institutional transformation and higher competitive practices among banks within the system. The resulting competitive pressures have also brought out the needs for banks to know and understand the customers so well that the product or services created fit and makes them ready to buy. In spite of these identified needs for product marketing, Kotler (2002) opined that a marketer can rarely satisfy everyone in a given market. The success of modern product marketing therefore hinges not on the ability of seller to influence the level, timing and composition of demand but more significantly the skill to partition the attributes that consumers posses as a means for targeting product offering to them.

Multi-attribute segmentation practice have been adopted in relation to bank-service offering in many countries on the basis of such variables as level of income, saving pattern, risk preferences professional calling or demographic characteristics, (Day, 1984 and SteeKamp et. at., 2002). In Nigeria, markets for financial services have been segmented based on consumption or buying pattern hence the use of personal and business clients. Market segmentation as a survival strategy has proved successful for non-banking firms especially where it is possible to isolate certain sectors of the total market and products created are so uniquely designed that no immediate competition exist, (Kotler, 2002).

In a service industry such as a bank, incidences of rising overhead expenditures are known to be associated with market segmentation. This occur because where the product is profitable for a given bank other competing banks within the industry will soon copy the products with negative impacts on the original bank bottom-line; (Sanusi, 2000).

Disparities also exist between marketing of bank financial services physical product and even the services provided by other firms outside the bank. The special case of bank service marketing according to Kotler (2002) lies in its two-sided nature; namely, the needs to attract customers to sell deposits to and source clients who will buy the credit facilities to be created from the deposits. Inappropriate market design and drives by Nigerian banks have created large-volume of bank deposit and liquidity in the past. Similarly, report of rising toxic –assets in the Nigerian banking system is not unconnected with poor credit administration. For instance the percentage of non-performing loans to total credit of insured Nigerian banks was as high as 72.64% as at September 2005 (Sanusi 2005).

Recent audit carried out by the Central Bank of Nigeria (CBN) in August 2009 which indicated some levels of distress within the Nigerian banking system cast a lot of doubts on the success of market practices being adopted by the sector. This study therefore examines; among others what market segmentation practices are adopted by a typical Nigerian commercial bank? What relationships exist between market segmentation practices and performance of the sampled commercial banks?

The extent to which market segmentation practices of selected banks has ensured customer brand-loyalty for typical bank product, is also in doubt. This study also makes an enquiry as to the extent to which market segmentation practices influence customers loyalty to a bank product offerings.

2.0. Conceptual Clarifications

2.1. Definitions and Concepts

Various definitions have been used in literature to describe the concept of market segmentation. Some have perceived it as the process that a company adopt to divide the market into distinct group on the basis of needs, wants, behaviour or taste for its different products or services; (Day 1984). Rather than offer the same marketing mixes to vastly different customer, segmentation enables a firm to design product for specific target market and thus satisfy customers needs better.

One of the primary aims of segmenting a business sales programme is to focus on the subset of prospects that are mostly likely to purchase its offering. According Salami and Adewoye (2006), market segmentation when done properly will maximize returns for a given marketing expenditure. Essentially business needs for segmentation are often determined by the needs to match the benefits offered by the product and requirements of the prospects (customers). Some ‘needs’ categories for segmentation range from improvement in cash flows, manufacturing quality, service delivery, employee working condition to market share or competitive position. Other business segments are designed as a means for reducing expenses, or achieve the goal especially of serving a given market or social better group or simply to create a market 'niche'.

Whatever the needs for embarking on such market partitioning, segmentation can only be practically feasible where the target market segment is easily identifiable, accessible, and respond differently to the different marketing mixes offered. A good market segmentation will result in segment member that are internally homogeneous and externally heterogeneous, that is as similar as possible within the segment but as different as possible between segments.

Segmentation of banking product in Nigeria has followed the usual consumer product market-partitioning with emphasis on such characteristics as geographic, demographic, psychographic and other socio-cultural behaviour.

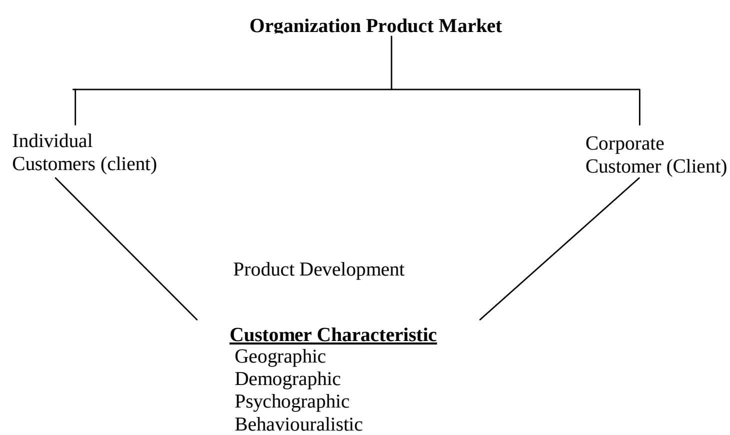
The attainment of market segmentation goals has been viewed as a major starting point for achieving organizational success. This view was supported by Salami and Adewoye (2006) in a study on the efficacy of market segmentation among Nigerian manufacturing companies. Previous findings by Wind and Cardoso (1974) as well as Agbo and Onu (2000) have found causality between customer retention (brand loyalty) and business profitability. This paper therefore evaluates how the Nigerian banking industry utilizes this tool to manage its product offering in a dynamic financial service market.

2.2. Market Segmentation, and Bank Service Offering

A market segment is simply a group of present or potential customers with some common characteristics that are relevant in explaining their response to suppliers' market stimuli; (Kotler,2002). Doyle (2004) viewed market segmentation as a homogeneous group of customers each reacting differently to promotion, distributional communication, pricing and other variables of marketing mixes. When these views are applied to segmentation of bank product market, the implication is that it affords the marketer to distinguish portions of the market from one another say in terms of customer needs and so achievement of corporate profit target. Success in a market segmentation process is premised on the ability of a bank to identify individual differences and similarities within segments that have significant impact on purchasing patterns. Nigerian banking environment has witnessed tremendous competitive changes and regulatory dynamics; thus making segmentation practices imperative determinants in product development and offering to its complex clients.

Several theoretical frameworks abound for the design of a workable segmentation process in bank product offering. Brassington and Petit (2006) and Steenkamp and Hofstede (2002) suggested the two-stage process while Wind and Cardozo (1974) identified a three-stage design based on selected characteristics:

Two-Stage Segmentation Process



Source: Adaptation of two –stage ideal market segmentation process Brassigton and Petit (2006)

Brassington and Petit (2006) stated that an ideal market should follow at least two stages; the macro-segment which is based on buyers (or buying situation). and the micro-segments that have substantial influence on the decision-making characteristics. The macro-segment represent the purchasing sectors whose decisions are based largely on micro-units; that is individual decision-making units who are usually components members of the macro-unit determining the success of any product developed and subsequently offered in the market place. Pride and Ferrell, (1985) based their categorization of the market into industrial and consumer segments to achieve the same objective while size; location and usage rate are the basis adopted by Wind and Cardozo (1974). Focuses of most theorists are to provide a closed match between specific product features, individual consumer needs and the requirements of the target market.

Salami and Adewoye (2006) identified profit maximization; increased market share, product positioning and enhanced turnover as some of the reasons why Nigerian banks embark on market segmentation.

When bank products are specially designed to meet customers expectations especially the demand of heavy users within a market segment mass customization organizational performance and customer retention will be enhanced; (Cooper (1993), and Ovia (2004). The implication of these findings is that every potential segment has its own strength and characteristics and its imperative for bank product marketer to study each segment in line with the quality and type of product or services being rendered. This will play significant roles in achieving the desired corporate goals.

2.3. Bank Performance-Customer Retention Causality

Performance in the context of a bank operation according to Peter and Sylvia (2008) refers to how adequately a bank meets the needs of its stakeholders; owners, employees, depositors, and the borrowing customers. Indicators of the quality and quantity of a bank performance are determined by the extent of a business profitability and (or)risk which provide surrogates for evaluating the extent to which the bank achieves its objectives of maximizing owners wealth (Adeoti and Salami, 2007). Nigerian banks since the commencement of the consolidation programme in 2004 have demonstrated great awareness of the linkage between performance and customer retention. This realization has informed series of product bundling, cross selling, loyalty programmes and integrated computer system employed to attract clients. Furthermore, the development of strong loyalty to a bank product offering has been traced among others to quick-delivery services, nearness to client business outfits, corporate image built overtime, customer/ employee relation, relaxed account opening formalities, referral and accessibility (Adewuyi 2008). Some analysts premise success of a corporate value maximization effort on the extent of the rise in its stock prices. The approach is premised on interrelationship between market prices of an organization stocks; and changes in operational efficiencies, interest or exchange rates and the economy in general. White the behaviour of a stock price is in theory the best indicator of a bank performance and a reflection of how market evaluates it; salient variables required for the calculation of this parameter might not be readily available for most Nigerian commercial banks. This is why this study adopts the adoption of profitability ratio in this study as surrogates for market – value indicators.

Profitability in the form of retained earnings according to Klee and Fabio (2005) is one of the key sources of bank capital generation. A sound banking system is built on profitable and adequate capitalized banks. Profitability is also a revealing indicator of a bank's competitive strength within its market and a measure of its management quality. The use of ratios in evaluating performance might cover a wide ranging spectrum including return on capital profit margin; size of turnover, earnings or dividend per share. In the banking sector interest income, profit after fax net interest margin are given special relevance as they influence return on capital employed (equity).

Key profitability ratios being applied to determine the extent of a bank success in this study are those reflective of the impacts of adopting market segmentation practices on operations. In particular Haffindal Hirschman index (HHI), Return on equity (ROE), Net operating margin and Net interest margin are employed as parameters for determining effects of market segmentation practices on operational performance.

3.0. Research Design and Method

The study relates basic variable of market segmentation practices with selected bank performance customer retention (loyalty) indices.

The exploratory nature of the study informs an examination of sampled bank market segmentation practices in relation to their effect on performance variables Day (1990). Seven banks are purposefully selected out of the twenty-four consolidated banks that constitute the entire Nigerian commercial banking sector within the study period constituting twenty-nine percent of the entire population.

Data employed are generated both from secondary and primary sources. Bank performance variables and market segmentation targets such as market share; operating expense, profit and turnover are sourced from selected bank annual reports for 2008 and 2009. A questionnaire was also administered to determine relationship between selected bank customers attachment (branch loyalty), organizational product development and targeting.

Collected secondary data are subjected to statistical test using Herfindahl Hirschman Index (HHI) a means for determining bank market concentration (business footholds) using deposit size as a measure of success for adopting market segmentation practice. Calculated indices are further correlated with other performance variables using spearman's rho test. The test is a non-parametric equivalent of a test of correlation for matched pairs of data. For instance if Y, represent market share or business footholds as calculated using Herfindal Hirschiman Index (HHI) and X_1 is rate of profitability among sampled banks; then a bivariate random sample of size n (X_1,Y_1), (X_2Y_2)………(X_nY_n) can be determined. The calculation by this token thus rank HHI index for i =1,2,3, ……………n period with return on Equity ROE; Net Interest Margin; and Net operating margin for the respective operational period of the sampled banks. This is mathematically defined as;

$$P= \frac{\sum_{i=1}^{n}\left[R(X_1)-\frac{n+1}{2}\right]-\frac{n-1}{2}\left]R(Y_1)-\frac{n-1}{2}\right]}{n(n^2-1)12} = \quad (1)$$

Where P = Spearman's correlation coefficient

$R(X_1)$ = Rank of variable X_1

$R(Y_1)$ = Rank of variable Y_1

n = Sample size

An equivalent but computationally convenient form is given by;

$$P=1- \sum \frac{[R(X_1)-R(Y_1)^2}{n(n^2-1)} \quad (2)$$

Questionnaire was also designed to source customers' opinion on the effect of market-segmentation practices on bank Customer Retention Ability (CRA).

4.0. Result and Discussion

The result of the Herfindahl Hirschman Index (HHI) estimated are presented in table 1. The table indicated four of the seven banks in the sample benefited greatly from the adoption of bank segmentation practices. In particular bank (7) scored an index of more than half for all the banks within the sample indicating dominant position in contrast with banks (3) and (5) respectively. The index scores of less than One-hundred points implies a very weak position while indexes above one thousand indicate a near monopoly of the market or excellent result in the market practices adopted.

Table 1: Deposit and Market Share Among Sampled Banks

S/No	Bank	Deposit in 2008 Annual Report	Market Shares in total Deposit (Al)%	Square of each Bank Market Share $A^2{}_1$%
1.	Unior Bank Plc	649	17.55	308
2.	FBN Plc	661	17.87	319.34
3.	Stanbic Plc	98	2.65	7.02
4.	Diamond Plc	403	10.90	118.81
5.	Afribank plc	278	7.52	56.55
6.	Access Bank plc	351	9.49	90.06
7.	UBA plc	1258	34.02	1157.4
	Total	**3698**	**100**	**2057.18**

Source: Banks Annual Report 2008

Scores above 100% indicate beneficial effects of adopting market segmentation practice while other scores; mostly below hundred points indicate signs of poor result from segmentation.

Relationship between bank performance and market segmentation practices is tested using the Spearman Roh test. The extent of relationship between the variables according to the findings indicates some level of significant relationship between the market shares of selected companies and their overall expenses. The relationship was 0.571 which by implication indicate a significant portion of the market share was as a result of the overall expense, incurred by the sampled banks in the study. This result was based on the individual market position of each bank within the sample consisting of both dominant and less dominant members of the industry.

The effects of the overall expenses on the market share of each of the sampled banks were examined by testing several functional models ranging from linear logarithm, quadratic and exponentional functions. The result observed that quadratic function accounted for the highest fit that is a contribution of 30.9% in the market share variation. Others are not as significant. The conclusion drawn from this finding is that as overall market expenses increase through various market – segmentation practices adopted by Nigerian commercial banks; the market share of the sampled banks increase until a peak is achieved at 37.0%. Further increases in the overall expense beyond this point indicated diminishing affect. At that level the market share diminishes thus increasing overall market expenses accounts. In other words when segmentation expenses account for as high as 37.0% of total operating expense; benefits derivable will peak and further commitment of funds in this direction will lead to negative market share dominance.

Questionnaire was administered to determine the effects of market-segmentation practices on bank customer-retention strategy. Opinions sourced evaluate the success of each of the sampled bank method adopted in ‘customer valuation’ (whether financial or strategic), and corrective plans employed to win back defecting customers through employee practices. These criteria surrogate bank Customer Retention Ability (CRA) and management of customer defection ratio. The CRA for a sampled bank measures the number of customers at the end as a percentage of customers at the beginning of a period; otherwise it determines the chances of a customer full patronage of a bank branch without defection throughout the sample period. Findings for the seven-banks under study is presented below:

Table 2: Customer Retention Ability (CRA) for the Sampled Banks

Banks	Customer with Active Account Beginning of Period	Sample Customer with active Account of period	Degree of customer Retention %
1	50	21	42
2	50	35	70
3	50	25	50
4	50	40	80
5	50	20	40
6	50	37	74
7	50	47	94

Source: Field Survey based on Questionnaire administered to test customer loyalty to bank branch/ product. 2010

Findings from the table corroborate the HHI index, on market share as banks with high market shares also demonstrate high Customer Retention Ability except for bank one (Union Bank Plc) whose customer retention is low. The explanation for this might not be unconnected with bank ‘recovery efforts’ at replacing defecting customer with new ones thus maintaining market share despite ’defection’.

5.0. Summary and Conclusion

This study has examined the impact of market segmentation practices among Nigerian commercial banks. Emphasis has been on the forms of segmentation practices adopted, the extent to which their performance have been influenced and customers loyalty secured. The study found among others that segmentation has benefited some sections of the industry more than others thus enabling dominance of the market share and customer patronage. It is however discovered that there is a threshold point beyond which further commitment of funds into market-segmentation practices by a bank will result in negative result. On the basis of these findings the study recommends that a bank should undertake a careful analysis of its operating market for an efficient partitioning of its client-pool in order to effectively design its product offering.

In a highly competitive and dynamic environment such as Nigerian banks operate survival and success can only be assured through an efficient market segmentation practices which encompass a clearly defined ‘customer valuation’ process. Apart from segmenting the market for product offering, continuous customer loyalty and retention process also require creation of customer centered operating premise through quick service delivery, acceptable corporate image; customer-employee relation, relaxed account opening formalities, effective use of referrals among others.

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