

TAM, SAM, and SOM: fundamental market size metrics

From: <https://www.lean-case.com/tam-sam-som/>

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Do you need to raise funding but have difficulty convincing investors? Do you want to include the TAM, SAM, and SOM concept in your pitch? Did your investor just ask you to provide the size of your TAM, SAM, and SOM?

For every founder, taking a new business off the ground is an exciting but challenging experience. For every investor, evaluating new business concepts bears high risk and it is hard to compare business plans and elevated pitches.

Just having a great Minimum Viable Product (MVP) is not good enough. It is equally important to present the feasibility of your product or service through accurate market size numbers in your business plan to win investor trust.

In this post, you learn about TAM, SAM, SOM concept as fundamental market size metrics.

Why is it so important to include accurate Market Sizing in the business plan or investor deck?

The most daunting task is to convince investors that your business idea is economically feasible and that they should fund it. Since their money is at stake, investors mostly think about the numbers you present to them regardless of the personal throws you're about to make.

Investors are mainly interested in generating a guaranteed return on their investment. This requires scrutiny in market research answering 3 questions associated with the TAM, SAM, SOM concept.

- **TAM (Total Addressable Market) - What is the maximum market size/revenue a business idea can generate by selling a service or a product?**
- **SAM (Service Addressable Market) - How big is the market segment within the TAM which can be targeted by your services?**
- **SOM (Service Obtainable Market) - How big is the realistic market portion within the SAM which your company can capture with its services in 4-5 years?**

This can best be described by developing excellent Market Size metrics as a part of the Revenue Predictions in your Business Plan. TAM, SAM and SOM are three magical metrics to help you determine the value and viability of your entrepreneurial idea and to demonstrate them to decision makers.

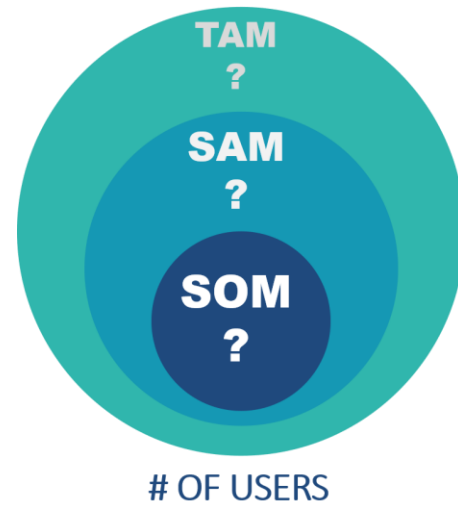
They are relevant metrics for you to cover when building a sustainable business model. You want to avoid that the numbers in your business plan are not in line with the numbers of a realistic market sizing. Communicating numbers which are much higher than realistic market size estimates hurt your credibility dramatically. Communicating numbers which are much

lower, shows that you are not on top of your plan. You can easily get lost in metrics. That's why you should make sure that you understand and apply them correctly.

Let's explore TAM vs. SAM vs. SOM one by one - what they mean and why they are crucial. At the same time, we give you a hands-on example with simplified figures for my start-up Lean-Case to show you how to calculate the revenue potential linked to TAM, SAM and SOM.

TAM SAM SOM Example Lean-Case - Briefing

- Lean-Case substitutes the use of Excel for business planning, financial forecasting and revenue forecasting
- **Markets for verticalized SaaS applications** such as Lean-Case are **new global markets, with eventually high volume and high growth rates.**
- Lean-Case targets everyone who wants to sell or evaluate a startup or project idea and present numbers which matter to decision makers and who - so far - used to do this with Excel (e.g., startup founders, business line managers, program managers in accelerators and incubators, Sales VPs in software companies, investors, consultants, etc.)
- Lean-Case sells globally with a focus on English and German speaking markets



Let's explore all details to calculate estimates for the TAM, SAM and SOM

Total Addressable Market (TAM)

TAM stands for the **Total Addressable Market**, also known as the **Total Available Market**, and refers to the total market demand for a product or a service. It allows potential investors to estimate the size of a market segment which is maximum revenue a business idea can generate by selling a service or a product in a specific market.

Two main methods can be used to calculate TAM – top-down and bottom-up approaches.

- The **top-down approach** uses industry research from such companies as Forrester, Gartner, and others, which can be obtained from open sources to estimate the population that comprises the target market. Then you should logically apply geographic, demographic, and economic assumptions to eliminate irrelevant segments and narrow down the large part to a specific market segment.
- The **bottom-up approach** is more reliable because it is based on primary market research. You should count / estimate the total number of customers in a market by adding up the number of customers that each company has and multiply that number by the average annual customer revenue in this market.

TAM reflects the full market potential, but realistically, no company can ever capture 100% of the total available market.

Why is TAM crucial for your business plan?

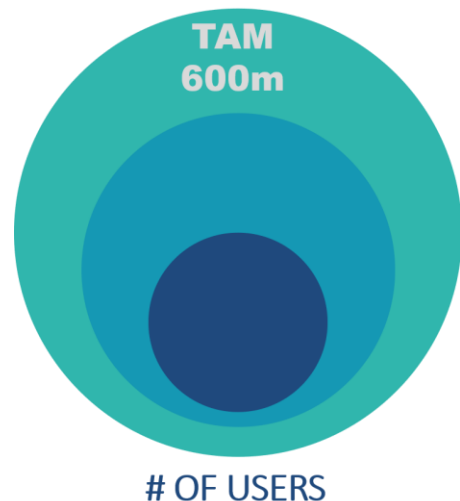
TAM has high relevance because it helps to determine,

- The total market size of your product/service
- Possible business growth
- The competitiveness of your product/service
- The untapped customer segments left untouched by your
- Maximum revenue, a company could ever achieve when it is in full swing!

Chances are that you are not the only business in the market, and part of the market share is already captured by competitors. So, customers who need and can pay for your product/service would be your ideal market which is referred to as SAM.

Example Lean-Case: TAM of 600m users

- Research provides that Microsoft serves 600k companies with Office products worldwide with more than 1.2b Microsoft Office users
- Assuming that every second user of Microsoft Office also uses Excel, any of those could buy Lean-Case for very simple calculations yielding a TAM of 600m users globally



Serviceable Addressable Market (SAM)

SAM (Serviceable Addressable Market or Serviceable Available Market) is the part of the total addressable market that can be reached. SAM can be defined as the total sales volume of a particular product (or service) that can be sold by all vendors on the market within a specific territory that your company can service. Usually, there is already some competition that will help you root your estimations in something real. It's the portion of TAM you will target.

Comparing TAM vs. SAM, we should note that they are both addressable markets.

What is the addressable market? It's a marketing concept that refers to specific groups of people who you can address to get them interested in your product or services and who can potentially become your future customers.

Why is SAM crucial for your business plan?

SAM determines the share of revenues that can be obtained in the short and medium-term. It helps you discover your niche market by differentiating your customer segment based on demographics, such as age, gender, income levels, technology, geography, etc.

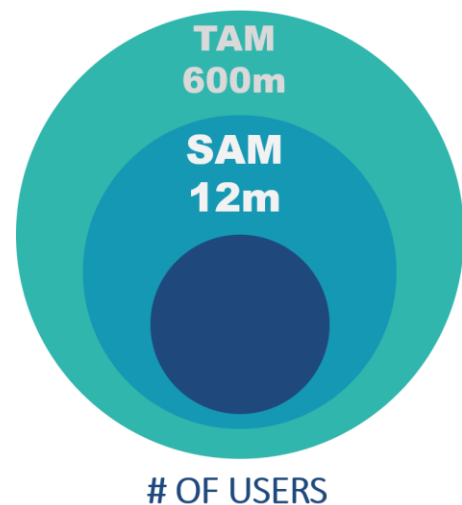
This is important to remember as it doesn't matter how big your TAM is if you don't have a mechanism to grow your SAM inside that TAM. McDonald's had the Speeded Service System, Facebook had its software-based network effect, and Uber had a fleet management innovation.

Those mechanisms are the reasons why these are globally known companies rather than merely a local burger joint, a Harvard networking site, or a taxicab company.

So that's the audience you should be able to serve best, assuming you could reach them

Example Lean-Case: SAM of 12m users

- We estimate that only 2% of all Excel users worldwide reflect our current target users who use Excel for business planning, revenue forecasting and idea valuation purposes
- Based on the TAM of 600m users, this yields a **SAM (market segment which can be targeted by Lean-Case)** of 12m users in 60k companies globally



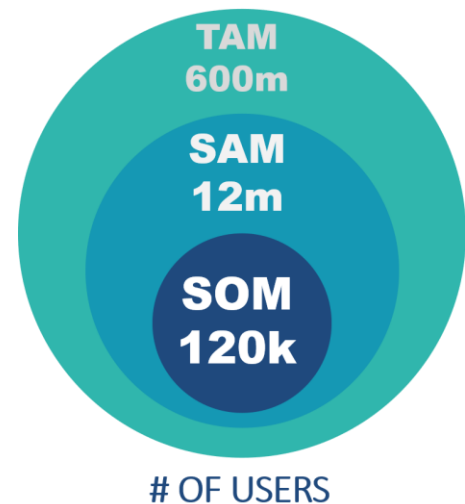
Serviceable Obtainable Market (SOM)

It will be difficult for a startup to penetrate the entire SAM, so you will need to set realistic goals and target a subset of SAM that you can realistically reach during your business's first few years. That's SOM or serviceable obtainable market. Being your short-term goal, SOM is the one that matters the most. If you seek funding, your investors will expect you to have a realistic objective and judge you on your ability to achieve that objective.

To estimate your SOM correctly, look at the competition in your precise niche and the total niche volume. Compare your product, marketing, pricing, and sales plans to the competition to estimate which part of the niche you may get.

Example Lean-Case: SOM of 120k users

- Given our limited resources, we believe that we can only target users in selected markets and business segments
- Within the next 2-4 years, it is possible to sell Lean-Case to 1% of 12m users in specific segments in the SAM yielding a **SOM (realistic market portion we can capture in 2-4 years)** of 120k users in 6-10k companies.
- Given the large number of consulting firms, corporate innovators and accelerators in Europe, we estimate the **European share** of the SOM to be around **50%**. Applying an average revenue of €300 per user per year, we are looking at a large global **€3.75B market** (SAM) and a Lean-Case **revenue potential of 37.5M** (SOM).



Why is it important to calculate TAM, SAM, SOM to win investor's trust?

The more you can prove that your SOM is attainable, the more it will increase your investors' confidence. You will be able to win investor trust by creating a business plan calculation which is in line with your SOM estimate.

When and why you must include TAM SAM SOM in your business plan?

Put yourself in the shoes of investors. It is necessary to provide investors a target return that implies both:

- a low-risk early investment (i.e., understand if the startup has a market by spending as little money as possible) and
- investment in opportunities that offer considerable upside potential (i.e., huge market size).

The SOM and SAM help to reduce the investment risk, while the TAM allows you to assess the upside potential. The Serviceable Market is your short-term goal and, therefore, the one that matters most: if you fail to succeed on a fraction of the local market, chances are you will never capture many parts of the global market.

Investors expect you to have a realistic goal, and they will judge you on your ability to achieve that goal.

For the investor, the ability to reach your SOM means that he will not lose his shirt. In this context, The SAM numbers act as a good business plan health check to assess the likelihood of achieving the implicit Serviceable Obtainable Market and as a substitute for your company's short-term growth potential.

If you can deliver SOM on time, you are capable and credible, and you might be able to increase market share and achieve greater SAM penetration that would provide a good return on your investment.

How will the most accurate figures on TAM, SAM, and SOM help investors determine how much they can invest in your company?

Well, if you know the size of your SOM - then you have an idea how the numbers in your business model should look like. Beyond the TAM-SAM-SOM estimation, an investor still expects you to provide a business model with numbers which are in line and consistent with numbers you provided for the SOM. A business plan should answer 4 questions

- What is your revenue potential?
- Is your business model viable? (Is Customer Lifetime Value higher than Cost of Customer Acquisition?)
- When are you becoming profitable?
- How much investment do you require?

If you want to explore how an investor friendly business model looks like, click and browse in the menu below. Even create your own model.

Why is it essential to get the right definition of your company's business potential to get the right TAM?

Let's take the example of Uber. Uber's play wasn't just to be a taxi company. Internally, Uber's market was seen as every meter traveled. This means taxis, delivery services, haulage, and more. We're seeing this now with UberEats and UberFreight, which is currently expanding across Europe.

The TAM for Uber is not just the size of the global taxi market, but transportation more generally.

When you're trying to understand your total addressable market, you need to think of how you define your company and where you believe it can go.

Which factors should you focus on in your business plan to show investors how to maximize SOM?

The following factors determine why customers would choose you over others. You can use them to your advantage to maximize your SOM:

- Unique value proposition
- Better Prices
- Proximity and Localization

- Personalized services
- Outstanding customer service, etc.

What is the most crucial information that you must accurately calculate to get your SOM size accurate?

To calculate the size of your SOM correctly, you should prepare assumptions about

- Pricing plans
- Profit margin
- Frequency of transactions/purchases.
- Average Amount per transaction/purchase in your industry

The number of customers you plan to attract within a certain period – could be a few months or one year and so on.

TAM SAM SOM example

TAM, SAM, and SOM represent different subsets of the market. Are you still confused about these metrics? Let's take a look at another TAM SAM SOM example.

Let's say you are a tech startup launching new CRM software. Your TAM will be the total CRM software market worldwide. Any person that interacts with customers could buy your new product. But if your CRM software is only in English and you are targeting tech companies with sales teams, your SAM will be people from sales and customer services of tech companies worldwide that use the English language for their business. Your SOM will be a realistic market share that your company can capture in the first 2 or 4 years after launch.

This part of the analysis is harder to calculate because you should consider the features of your CRM software and customers' needs. You'll need to narrow your market one more time and, for example, target small and medium sales teams with simple selling cycles

As you see, TAM, SAM and SOM are fundamental metrics in business planning and important decision criteria for investors. They will be your starting point in building a sustainable business model. With Lean-Case you can get a quick grasp of the TAM SAM and SOM and take it further to develop your winning financial model.

How to calculate an accurate TAM, SAM, SOM revenue forecast in 3 minutes

So, we've seen what the different terms mean, and you've probably noticed that there are a whole bunch of other areas you'll have to research to build this all out properly.

Now we want to show you how you can build a revenue forecast which is in line with your TAM-SAM-SOM model in 3 minutes. In Lean-Case, we provide a Blueprint (Business Case

Template) that you can leverage for this purpose. It forecasts your revenue potential in line with your TAM SAM SOM estimates over 5 years.

The video below outlines how to do this in 5 steps. We are using the sample data outlined for the Lean-Case example described above

1. **Add Funnel Stream for TAM with forecast of users** - A funnel stream allows you to model the market volume of users. Based on our example, enter a forecast of 6M users in the first month
2. **Add Funnel Stream for SAM** The second funnel stream enables you to model the conversion of TAM users into SAM users
3. **Add ONE-TIME Conversion from TAM to SAM - With** conversion rules, you define the conversion of 2% of TAM into SAM users. A one-time conversion only happens at exactly one point in time, which is right at the beginning of the business case - i.e., 2% of users are becoming SAM users immediately
4. **Add Revenue Stream for SOM revenue potential** - A Revenue Stream allows you to model revenue streams for different types of revenues like subscription, one-time or pay-per use revenues. In our example, we assume subscription revenue per user of \$25 per user per month
5. **Add Monthly Conversion from SAM to SOM** - In the last step, we model that every month a small share of SAM users become SOM users which already generate revenues. In the example, we assumed that a total of 1% of SAM users would make up our SOM. To get to this number of users over time we assume that every month 0.03% of SAM users convert into SOM users. After 3 years, the number of SOM users has reached the 1% threshold ($0.03\% \times 36 \text{ months} = 1.08\%$) and continues to grow.

With all the excitement that comes with starting a new company or project and gauging its industry's profit potential or forecasting a revenue goal for your business, you must remember to root these figures in reality. Let us know if we can help you to build your revenue models in line with your TAM-SAM-SOM.

