Module 4. Market sizes and types

Unit 4. 1 Market concept for new start-ups

Do you remember the manifesto for customers development method that was developed in reading 3 from course 2? According to Blank and Dorf (2013): "Choosing the type of market changes everything". (p. 195).

According to Blank y Dorf (2013), that manifesto is one of the main pillars in their entrepreneur manual.

These authors claim from the beginning that start-ups are different from traditional companies, but they are also different from each other, due to the relationship that each of their new products has with their market (Blank, y Dorf, 2013). A bad choice in the type of target market could affect the development stages later, linked beforehand with the creation of customers. Although it is a decision that is generally delayed, we recommend you to work, at least, on assumptions on the type of market to which you target, because this will allow you to anticipate future problems when discovering customers.

According to Blank (2013), the type of market has an impact on the whole start-up, depending on the characteristics of both of them. This impact can affect the following elements:

- **Market:** when its size changes, the cost for entering the market might also change, which can affect the product launching, its positioning, and description, among other things.
- **Sales:** the sales model is totally altered since you will have to define if your sales will be direct or not, the sales cycle and the time allotted the limits, the benefits, etcetera.
- **Finance:** it is related to the earnings and the profitability you will need; it can vary depending on how long the startup will be profitable.
- **Customers:** it affects the different customers, their problems, and their needs.

Having said that, we will get deeper into the product-market relation and we will make a distinction between the four types of market entry.

1) Entering into an existing marker with a product with a bigger performance or with better attributes

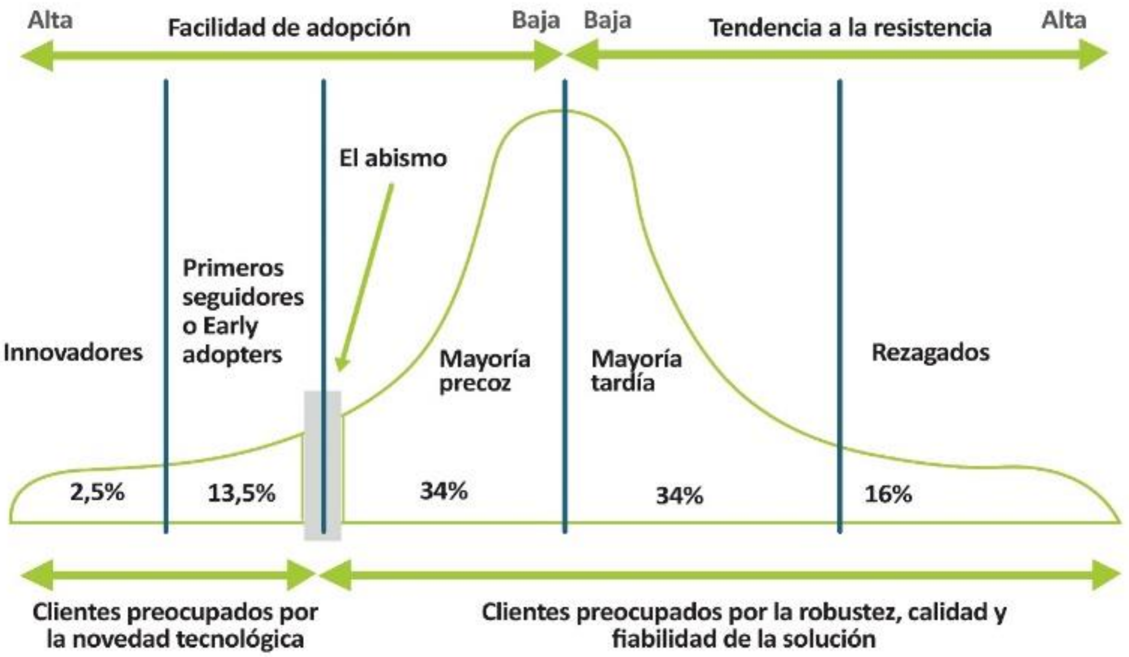
A market is existing when the product already exists as such, but the new start-up product's features are better than the ones offered at the moment of entering. This means that it is a product or service that works better or quicker than others or that it improves substantially what already exists in the market. In this case, users and the market are already known, but so is the competitor.

Blank recommends searching on the curve for technology adoption lifecycle proposed by Geoffrey Moore in his book Crossing the Chasm (2015) since he considers it is very useful for start-ups.

You should find the first people that are willing to test your ideas, inside the 15% that is represented by early customers.

In the next graphic (figure 1) we can observe that innovative customers, the first followers, and the early adopters represent 15% of the market; they are the ones who can easily adopt new solutions and who are informed and predisposed to novelty. Inside that 15%, you should find the first group of people willing to test your ideas. Once you can get most of the customers inside that group, you could find a chasm, which is the stage in which you may find difficulties to start escalating. Finally, under the assumption that the product or service is successful, the late majority and the stragglers will be ready to test your solution, even though they show resistance.

Figure 1: Diffusion of innovations or early adopters curve



Source: Prim y Hernández, n. d. https://bit.ly/3gNNmAt

Alta	High
Baja	Low
Facilidad de adopción	Easy adoption
Tendencia a la resistencia	Tendency to resistance
Innovadores	Innovators
Primeros seguidores o Early adopters	Early adopters
El abismo	Chasm
Mayoría precoz	Early majority
Mayoría tardía	Late majority
Rezagados	Stragglers
Clientes preocupados por la novedad tecnológica	Customers that care about the technological novelty
Clientes preocupados por la robustez, calidad y fiabilidad de la solución	Customers that care about the solution's robustness, quality, and reliability

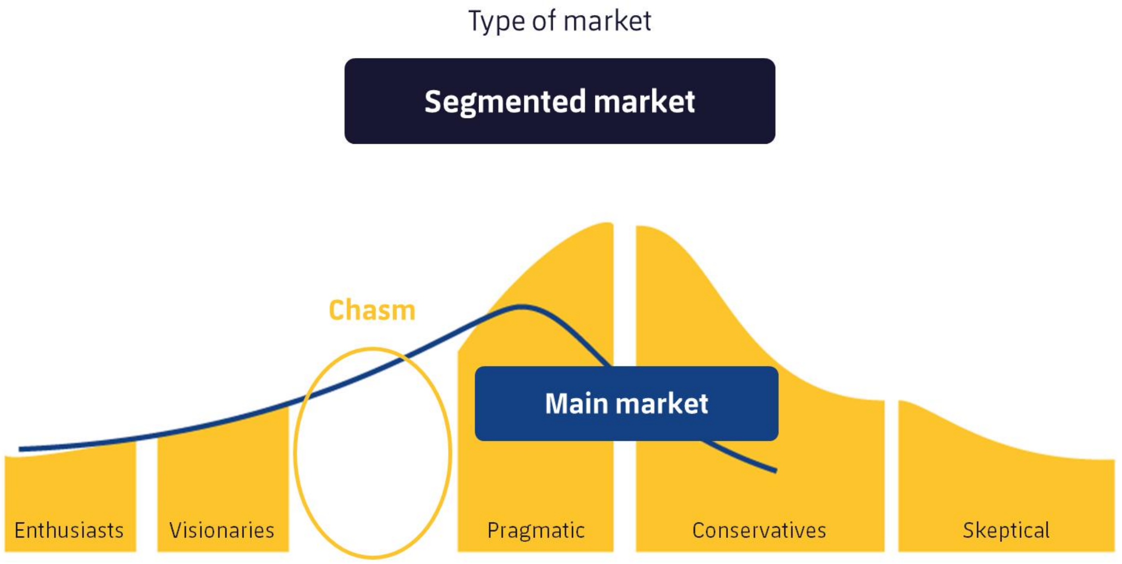
The best way to detect early adopters, innovators, or first potential customers is to first validate if the problem they are trying to solve is real if they recognize it, if they already have a solution, even though if it is home-made, and finally, if they have a budget to adopt a personalized solution in accordance with their problem.

2) **To segment an existing market again:** Re-segment the market by applying strategies for identifying new low-cost niches. This technique is useful when it is practically impossible to attack the leader of that market. How is it achieved? By identifying a market opportunity the competitor has not detected, with a market and customers that are well known by the start-up.

   The low-cost strategy is a market segmentation that targets that group of customers that are at the base of an already existing market and who are willing to get a product functioning smoothly, at a lower price, which they can afford. According to Blank and Dorf "...a low-cost strategy explains itself. Are there customers at the bottom of an existing market who would buy something "good enough" at a substantially lower price?" (2013, p. 199).

   The segmentation by market niches tries to convince a group of customers with certain new product characteristics (make this new product attractive enough, a product that changes the rules and formalities in an existing market, etc). Unlike low-cost segmentation, the niche market one goes after an existing market segment that would be profitable.

Figure 2: Sales curve on re-segmented markets



Source: own creation

3) Create a completely new market

Sometimes there are context changes, new technologies emerge, or simply change of paradigms opportunities. So, there appears a big opportunity for creating a new need for a "new" market, for customers that either did not consume certain products before or did not feel a certain shortage. So, by fostering a true innovation, by creating something that has not existed, we can create a new type of consumer, a new market.

In the Blue Ocean Strategy book (2005) by W. Chan Kim and Renée Mauborgne they claim that most companies compete against each other (inside what they call "red oceans") and that strategy offers less and fewer possibilities for generating profitable growth in the future. Therefore, they claim that future leader companies will not be successful competing against their competitors, but by creating "blue oceans", which he defines as strategic movements focused on creating new markets based on providing big quality jump, not only for companies but also for customers; this will make the difference, in relation to competitors.

The good news in a new market is that the characteristics detailed on the product are irrelevant at the beginning because there are no competitors. The bad news is that the users and the market are not defined, nor limited. Nobody knows the product, nor its utility and, therefore, creating demand is difficult, since for Blank and Dorf "...the product is unknown for users and the market is not defined, nor known and its development is expensive" (2013, p. 198). In order to create this market, you will need a lot of willpower and money, besides the word of mouth spreading. An example that makes this market understandable is Groupon, which created a completely revolutionary way by using everyday sales.

This way, following Blank and Dorf "…the line that divides the new and existing is the base for the type of market definition" (2013, p. 198).

4) Creating a clone market or copying a business model from another country or zone

It is a useful strategy when business was tested and consolidated in a country, but it was not introduced in another one yet. Therefore, different countries´ start-ups, each with their idiosyncrasy and with local conquered markets, can adopt or copy a successful business model consolidated in another country and adapt it to the local language, culture, and local consumption (Blank and Dorf, 2013). Blank y Dorf mention some like the following: "Baidu in China and Yandex in Russia are the equivalent to Google in their respective markets. And Qzone, RenRen, Pengyou, and Kaixin are China´s Facebook, while Vkontakte and Odnoklassniki play the same role in Russia" (2013, p. 201).

Table 1: Type of markets alternatives

	Existing market	Re-segmented market (low cost or niche)	Newmarket	Clone market
Customers	Existing	Existing	New/new uses	New
Customers´ needs	Performance	- Cost - Need/problem perception	Simplicity and accessibility	New idea tested in another place
Product´s performance	Better/quicker	1- Enough for a bottom end 2- Enough for the new niche	Low in normal characteristics Improved according to customers´ new metrics	Enough for the local market
Competitors	Existing	Existing	There is/are no other start-up(s)	There are no original manufacturers
Risks	Existing	Existing Niche does not work	Adoption	Cultural adoption

Source: Blank, and Dorf, 2013, p. 388.

The type of market the company attacks is decisive.

Strategies and tactics that work for a type of market, rarely work for another, since the type of market determines the type of activities for collecting information, for getting new customers, and for start-up expenses. Changes are in customers´ needs, approval rates, product characteristics, and positioning, as well as strategies, channels, and launching activities. In summary, different types of markets need a discovery, an MVP, and commercial and marketing strategies that are radically different (Blank, y Dorf, 2013).

Conflict for entrepreneurs is that not only many start-ups are not in existing markets, but they neither know their customers, since they do not know who they are, unlike the traditional model in which products are introduced in existing markets, with known customers, channels, and markets.

Unit 4. 2 Methodology to estimate the size of the market

Once the type of market is chosen, the first thing to analyze is its potential market: Is there a market opportunity? How many potential customers in the world have this problem and would be willing to pay for solving it?

How many potential customers in the world have the problem you want to solve and would be willing to pay for solving it?

These hypotheses help you to identify the opportunity dimension. In this sense, it is worth to remember that market opportunities grow thanks to three ingredients:

1) a big number of active users or potential customers;
2) growth expectations for potential users in a market that grows quickly and unpredictably;
3) ability to conquer active customers.

Figure 4: Market sizes

Source: own creation

Having analyzed the potential market, the next step is to estimate the market size, the available market, and the target market as a starting point to materialize the market size hypothesis. To assess an existing or re-segmented market, an option is to consider adjacent markets, from which customers could come. For example, millions of Blackberry users changed their devices when the iPhone was launched. In the case of the new markets, in which there is no specific information, estimating the opportunity based on indicators and adjacent markets is the only alternative. Likewise, to make these estimations, we use three indicators; they are described in-depth in the following paragraphs.

Total Addressable Market or TAM: it is useful to know how big is the market to which you target, to know if it is accessible to your product or service, and to know how big the business opportunity is. That is why we should study the total market size. To calculate it, we can use different resources, such as the following:

- Bibliography on the size of the existing market. We can consult statistics, market studies, indirect data from the existing demand, etc.
- Market assessment on economic terms; that is, getting value data that is generated by the market size to a company as the one you want to create, trying to use metrics that you might consider correct (currency, physical units, web metrics, etc.) (Macías, 2014).

An example of a total addressable market in a country could be a billing of 30.000.000.000 USD or 150.000.000 units.

Serviceable Available Market or SAM: This estimation´s goal is to get a notion of the market size you can target with your resources (technology and business model you are generating), that is, the portion of the market you aim at. It is useful for estimating how much your company can grow with the products and services you count on, on the conditions they are currently. According to Macías (2014), it is appropriate to consider that there are limitations linked to the following elements:

Competitors: What is the offer position that will be created in relation to existing positions or competitors´ ones? (Macías, 2014,https://bit.ly/2XPVtoN). The first thing you should do is to question the plus that is offered to your customer and that has an incidence on their perception. In case you do not find it, then, it is very likely that you are sharing the market portion with competitors.
Entry obstacles: Which obstacles can you identify for your products or services to enter the market? And, which obstacles are derived from the relation with customers? Access to customers, the existence of vetoers or conservative prescribers is a very important restriction element in the market portion, as intangible entry obstacles.

Relation with your customers: it is essential to understand which are the distinguishing marks that customers perceive when you aim to a bigger portion of the market. (Macías, 2014).

Following the previous example, this business´ SAM, according to the start-up business model, would be 7. 333% of the total market, that is 2 200 000 000 USD or 11 000 000 units. To get better calculations, the 7. 333 % should be calculated as 11/150.

Serviceable Obtainable Market or SOM :

It exposes the real market size to which you can access with your resources and take your products and services to your customers´ segments. Therefore, it is the most important indicator and it is also the most difficult to calculate due to the following reason:

> It is useful to value the short/medium-term potential that, realistically, we can get with the resources we are going to invest for getting customers; that is, it is important not only to value the current market size, but also the market portion or percentage we can seize with the resources we have, and with our current catching strategy. (Megías, 2014,https://bit.ly/3acHOwW).

Consequently, this indicator estimation will be subject to the start-up capacity, to customers´ needs, and to the environmental limitations that can affect it, as the market entry obstacles.

Macías (2014) suggests some estimation methods when there is no reliable information or statistics about the market goal. One of them is through an "accessible portion hypothesis on our SAM, to validate it with our potential customers" (Macías, 2014, https://bit.ly/2DNEuMx). The other alternative is to do an over/under your goal market, to estimate an approximate number of customers that you will be able to assist every month and year, taking into account your daily operational capacity. For that purpose, you will be able to use information about the area and the market, journalistic news about competitors, conversations with potential customers or investors who would allow you to get information to estimate the total size.

For example: let´s see the case mentioned by Steve Blank about entrepreneurs that made calculations about their different market sizes, to start a professional football t-shirts sales or rent start-up.

Table 2: Example of calculation of market size

Total Addressable Market in USD		
TAM (industry billings)	USD (American dollars)	Number
	30 000 000 000 USD	150 000 000
Serviceable Obtainable Market in New York		
Chosen technology impact	100 %	
Business model impact	7 %	
SAM	USD	Number
	2 200 000 000 USD	11 000 000
	7.333 %	7.333 %
Serviceable Obtainable Market at the Yankee Stadium		
Available sources impact in the short term	50 %	
Available channels impact in the short term	50 %	
Localization impact in the short term	12 %	
Other relevant variables impact in the short term	100 %	
SOM	USD	Number
	64 350 000 USD	321 750
	0 %	0 %

Source: own creation

The conclusion is that your Serviceable Obtainable Market would be 64 350 000 USD or 321 750 t-shirt units, exclusively for the Yankee Stadium in New York.

Below, we share a chart to compare market sizes, in which differences are summarized and some examples are given.

Table 3: Differences and examples for market sizes

Total Addressable Market (TAM)	Serviceable Available Market (SAM)	Serviceable Obtainable Market (SOM)
It includes the total volume of operations performed in that market.	It describes a wide market, but a more precise one, on which a value proposition can be applied.	It describes a concrete customer segment with high potential.
Normally very generic. Easy to estimate.	More difficult to estimate, without being complicated.	It is often not easy to estimate.
Examples: **mobile applications;** **amount of energy needed;** **health and well-being.**	Examples: health mobile applications for athletes; renewable energy domestic generation; health and well-being at work.	Examples: mobile applications to monitor high-performance training for professional athletes; photovoltaic solar panels for generating domestic energy; health and well-being programs for companies with more than 250 workers.
TAM, SAM, and goal market in relation to customers´ segment concrete needs.		

Source: own adaptation based on Macías, 2014.

The ideal thing is to calculate market sizes in euros or dollars. Nevertheless, as this is not always a possibility, knowing the number of customers in that market is also useful for calculating the business volume you will be able to reach. Likewise, the market growth (or drop) percentage could be very useful, since these variables get modified with time and they allow for measuring evolution by making an annual analysis of 3 to 5 years. On the other hand, these estimations are quite relevant to look for investors, since these figures will allow you to think about the project potential globally and get a notion of the total way you will possibly go.

Final recommendations

Built a unique product with no competitors.
The brand, the scale, the network effect, and the technology combined somehow define a monopoly; anyway, for these factors to work, you need to choose your market carefully and make it grow deliberately.
Start small.

Every start-up is small at the beginning. Nobody dominates the whole portion of its market. Therefore, every start-up should start with a very small market. Always be too small. The reason is simple: it is easier to dominate a small market than a big one. If you think your initial market is too big, it may probably be.
The perfect goal market for a start-up is a homogeneous small group of people supplied by few or no competitors. Entering a market that is already supplied by competitors' companies is risky. This is the reason why it is always a hot problem when businessmen talk about getting 1 % of a market of 100 000 million dollars. In practice, a big market will frustrate a good starting point or that point will be open to competitors, then it is always difficult to get to that 1 %.
To know when to escalate.
Once you have created and dominated a niche market, you should start to expand gradually to related and slightly bigger markets.
Sequencing markets correctly is something underestimated and there is a need for discipline to expand gradually. Most successful companies make progression (first dominating a specific niche and then escalating to adjacent markets) a key part of their foundational narrative.

Source: own adaptation based on Thiel, 2014, pp. 73-79.

To sum up, the type of market determines the uncertainty level with which you will work. The market size will help you to project how interesting is the market you are chasing. The following spreadsheet will guide you in this process.

Table 4: Process to estimate the size of the market

Market size and type		
Goal	To estimate the market opportunity and specify which type of market it is	
Process	To estimate the market size.	TAM or Total Available Market
		SAM or Serviceable Available Market
		Target Market
	To determine the adequate metrics to measure the market size.	Units, dollars, visits, and other measures.
	Market research to evaluate the opportunity.	To read reports that analyze the industry, market researches, reports from competitors, etc.
		To talk to investors and customers.
		To identify similar companies.
		To estimate the industry growth.
	Type of market	Is there a new product in an existing market?
		Is there an aspiration to clone an existing market?
		Is there a need to redefine or segment a market?
		Is there an aspiration to create a new market?
		Is the product a substitute for something the customers already have?
		Does it replace it?
		Is it a variant from something that already exists, but that it can become something new?
		Is it something that is brand new?
	Positioning in an existing market	To define bases for competitors.
		Who manages the existing market?
		Which are the advantages you have?
		Are there strategies for vertical or horizontal arrangement?
	Positioning in an existing market you want to re-segment.	Define the basis for how you want to change the market.
		Who is the leader in the market you want to re-segment?
	Positioning in a new market	How will be the new market created?
		To estimate the market creation cost.
Deliverable	The written report of market opportunity and estimation of how much the company can catch. List of hypotheses about the type of market.	

Source: own adaptation based on Blank, y Dorf, 2013.

References

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