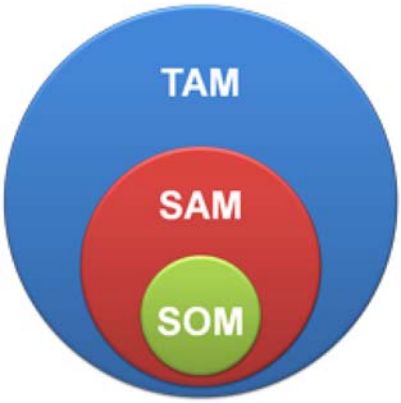
TAM SAM SOM - what it means and why it matters



When doing their market analysis (https://www.thebusinessplanshop.com/blog/en/entry/market_analysis_for_business_plan) start-ups often refer to TAM, SAM, and SOM but what do these acronyms mean and why are they useful to investors when assessing an investment opportunity?

TAM SAM SOM definition

TAM, SAM and SOM are acronyms that represents different subsets of a market.

- **TAM** or Total Available Market is the total market demand for a product or service.
- **SAM** or Serviceable Available Market is the segment of the TAM targeted by your products and services which is within your geographical reach.
- **SOM** or Serviceable Obtainable Market is the portion of SAM that you can capture.

Still confused about TAM SAM SOM? Let's take an example.

Let's say you are starting a fast food chain. Your TAM would be the worldwide fast food restaurant market. Potentially, if you were present in every country and had no competition you would generate TAM as revenues.

Sorry but that's not going to happen!

Let's be more realistic. You are starting your restaurant chain in two cities where the demand for fast food can be estimated based on: the population, their food habits, and the revenues generated by fast food restaurants in other cities having similar demographics.

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That is your Serviceable Available Market: the demand for you type of products within your reach. In other words if you were the only fast food in town you would generate revenues of SAM.

Now you are probably not the only fast food in town...

So realistically you can hope to capture only a fraction of your SAM. Most likely you will attract fast food aficionados living or working close to your restaurants and a fraction of the people located further away that are willing to give your chain a try for the sake of fast food diversity. This is your SOM.

Ok, now let's look at why and when they matter.

TAM SAM SOM, when do they matter and why?

Put yourself in an investor shoes. You need to deliver a target return to your own investors which implies both de-risking the investment early (i.e. figuring with the minimum possible of capital if the start-up has a market) and investing in opportunities which offer substantial upside potential (i.e. huge market size).

The SOM and SAM help de-risking the investment while the TAM enables to assess the upside potential.

The Serviceable Obtainable Market is your short term target and therefore the one that matters the most: if you cannot succeed on a fraction of the local market chances are that you will never capture a large part of the global market.

As an investor I expect you to have a realistic objective and I will judge you on your ability to deliver that objective.

To be realistic your SOM needs to factor in:

- your product: people will want to buy your goods
- your marketing plan and the identified distribution channels: you have a clear plan to reach a large portion of your target customers
- your SAM and the strength of your competition: chances are that you are not going to take 50% market share within 6 months. Therefore your SOM needs to be a reasonable fraction of your Serviceable Available Market.

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For the investor the ability to reach your SOM means that he will not lose his shirt. In that context SAM acts as a good sanity check to assess the likelihood of achieving the market share implied by the Serviceable Obtainable Market and as a proxy for the short term upside potential of your business.

If you can deliver SOM in time then you are capable and credible, and you might be able to increase the market share and reach a more important penetration of the SAM which would deliver a good return on investment.

And then comes the Total Available Market.

Once you have demonstrated your ability to penetrate a local market and de-risked the investment, the investor can start looking at how you can expand and increase the company's penetration within the TAM.

Let's illustrate this with a numerical example. You come to pitch an investor who has a target return of 10x. You are seeking a £250k investment in exchange for 20% of the start-up's equity.

Based on your market research and business plan we can reasonably assess that:

- TAM = £2bn
- SAM = £100m
- SOM = £5m within 2 years and £12m within 4 years
- EBITDA margin = 25%
- Valuation at exit = 8x EBITDA based on the value of listed companies within the sector

What happens if you deliver your plan?

Well, once you deliver £5m in revenues the EBITDA is £5m revenues x 25% margin = £1.25m and the company is worth 8 x £1.25m EBITDA = £10m. The investor return on investment is £10m x 20% ownership / £250k investment = 8.0x.

When you reach £12m of revenues the EBITDA is £12m x 25% = £3m and the company is worth 8 x £3m = £24m. The investor return on investment is £24m x 20% ownership / £250k = 19.2x.

Clearly here if you can capture your SOM the investor will meet his target return and he is then left with a company that has achieved 12% market share on a segment that represents 5% of the TAM of £2bn (£100m SAM / £2bn TAM).

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If you decide to expand the company and scale internationally, the company revenues potential (assuming you can reach a similar market penetration at scale) becomes 12% market share x £2bn TAM = £240m. Which would imply a £60m EBITDA (25% margin) and therefore a potential valuation of £60m x 8 = £480m. The investor could therefore offer to invest a up to £48m in the company in year 4 in order to meet his target return on investment of 10x.

As you can see TAM SAM SOM have different purposes: SOM indicates the short term sales potential, SOM / SAM the target market share, and TAM the potential at scale. All play an important role in assessing an investment opportunity and the focus should really be on getting the most accurate numbers rather than the biggest possible numbers.

I hope this article helped you get a better understanding of these acronyms. If you found it useful please share it and if you have any questions get in touch or leave a comment below.

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