

Volume	3	Starting a Company
Chapter	02	Approaching Investors
Section	04	Financial Model
Key Word Tags	Adoption Rates, Market Access	
Stage	Needs to raise money	

## FORECASTING MARKET SHARE: TOO BIG OR TOO LITTLE

File No. 3.020408 | 2017-06-01

Quick Summary: Set realistic expectations about gaining market share in a large, expanding market.

**Abstract:**

*Market Share as a single number can be distracting and not even indicative of a company's underlying value. Understanding what drives the number and the well-defined target market are far more important than the number itself. Over or under-forecasting can be an immediate turn-off for potential investors. It is hard to get it "right."*

Here is a quiz: Which do you think a potential investor would rather hear:

- A) "We can be highly successful with only 3% of this giant market."
- B) "We can easily see the company dominating the market with at least 80% of the market within the forecast period."

The answer is "None of the Above". In the first case, who wants to attract only 3% of any market? In the second case, total market dominance only happens in rare cases and does not last long before others offer better, faster, cheaper products or services. So, what is the correct answer? It depends; the only correct answer is one that passes the common sense test. It must be based on both logical assumptions and a considerable amount of speculation. Without a doubt, the largest variant will be the adoption rate of the offered product or service by the target market.

The adoption rate is only one factor. The size of the target market is equally important to the overall revenue economics. Obviously, a lower adoption rate in a large market can be far better than a high adoption rate in a small market. The tongue-in-cheek comment often made when non-common sense forecasts are presented is, "if we could only sell one pair of shoes to everyone in China, think about how big the business would be."

There are many factors that will drive the adoption rate in any market segment. You must understand each of them. One of the most critical issues is to understand "second-time buyers" or "repeat customers." A new restaurant is an illustrative example of the need to understand this factor. If the new restaurant has excellent results during its first week or month of its opening, its success could easily be forecasted based on those results. However, the real measure is how many repeat customers are there or will there be? Or, how many customers will tell their friends about their experience, good or bad? Carefully examining initial traction is critically important in predicting longer-term take rates. Quite often, early adopters are not indicative of long-term adoption rates.

Another factor that requires equal scrutiny is the “want versus need” value proposition associated with the product or service. At first, many early adopters will “want,” but not necessarily “need” the product or service. The larger, later market may not be so inclined to base their buying decisions on “wants,” but rather the product's or service's actual usefulness or utility. New smartphones or computers are good examples; many initial buyers are more interested in being the first to have the product rather than buying it to fulfill some basic need.

Finally, the market size must be carefully considered. For example, does the market consist of the entire U.S. population, or is it targeted at first-time expectant, college-educated mothers living in select suburban areas in the southeast?

The three factors described above only represent the in-depth analysis a company must do before predicting market share and adoption rate. Pricing, availability, advertising, seasonal variation, and a host of other factors must be considered and analyzed to determine a reasonable and justifiable market share target. Just stating a number without thinking about these factors is far worse than saying, “I don’t know.” At least with an “I don’t know” answer, you will not lose your credibility and may have an opportunity to do some homework and then address the issue.

A company must first determine if market share should be a driving metric. Apple, the world’s most valuable company, year in and year out, wins awards for its Mac PCs, yet it is only fifth in worldwide market share percentages. Clearly, Apple is focused on other metrics.

So, before even discussing market share and whether it is too small or too big, think about what is behind this one number and if it is even relevant to the business.

One final point: the cost of customer acquisition requires careful scrutiny. That factor, weighted against the total lifetime value of a customer (LTV), could significantly impact the overall market share strategy.