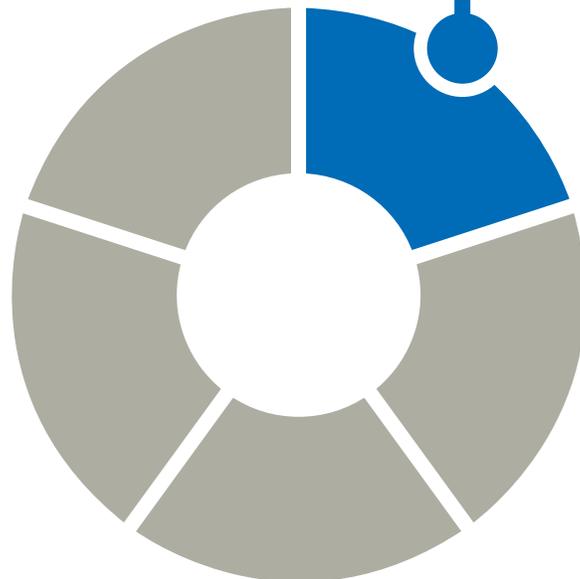


# The 5 Keys to Estimating Market Size for Strategic Decision Making



Understanding market size is a critical component of any strategic initiative, and can help you prevent costly mistakes. Yet reliable market size estimates can be difficult to come by, especially when looking at niche product categories or using specific market definitions tailored to your business goals. This task can be particularly challenging for industrial or B2B markets, where statistically significant consumer surveys or direct measurement (e.g., retail scanner data) is impossible. However, a number of techniques exist to develop an accurate picture of the market to support growth initiatives.

## 1. Why should I calculate market size?

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Incorrect guidance on the market size can result in missed opportunities, if market potential is underestimated—or excessive losses, if demand is overestimated—so investing the time and resources to obtain reliable data is critical to the success of any business.

Understanding the market size, segmentation and forecasts are important pieces of market intelligence for supporting decisions related to:

- New market entry
- Geographic expansion
- New product development
- M&A due diligence
- Large-scale capital investment
- General strategic planning

## 2. How should I scope a market sizing exercise?

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Market size is a measure of the volume or value of a product sold annually, and represents the total opportunity available for companies supplying those goods. There are many ways to look at market size, with demand being segmented by:

- Product
- Geography
- Vertical/End-use
- Channel

A key consideration in any market sizing exercise is to specifically define your scope. For instance, a well-defined product scope for industrial bags would first look at the type of product (paper, plastic or other) and then look at the bag size (0-10kg, 11-25kg, 26-50kg). Note that the sample bag sizes do not overlap in an effort to avoid double counting. A strong geographic scope will lay out what countries are included in what region. For example, Mexico is sometimes included in North America and sometimes in Central and South America, while Turkey is sometimes included in Europe and sometimes in the Middle East.

Other factors to take into account when you are scoping a market size analysis is the level of accuracy required and the level of granularity being sought. As a general rule, the more detailed the analysis, the more time that will be required to complete it. Establishing top-line global demand for cement is a relatively straightforward process, but once demand begins to be segmented by region and each region is segmented by product type and each product type is segmented by end market, the process can become significantly more complicated and time consuming. Furthermore, if accuracy is required within a narrow confidence interval, this will be more time consuming than directional ranges.

### 3. What resources should I rely on for establishing market size?

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Primary and secondary resources are the main information sources used in a market sizing estimate. Utilization of both types of resources will help manage the accuracy of compiled information.

A primary resource is a person who is involved in the market you are trying to size. This resource will ideally have significant exposure to the market. When covering industrial B2B industries, the most effective primary research technique tends to take the form of a 30-60 minute in-depth interview with an industry expert. Other primary research methodologies include focus groups, surveys and ethnographic observations.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Provides a view of demand held by participants in the market.</li> <li>• Viewpoints tend to be more granular than those available via secondary sources.</li> <li>• A good method for estimating demand when no other top-line estimates exist and the market does not lend itself to other forms of demand analysis.</li> </ul>	<ul style="list-style-type: none"> <li>• Dependent on imprecise estimates provided by respondents.</li> <li>• Respondents may be hesitant/unable to provide quantitative estimates for the size of the market.</li> <li>• Respondents may provide widely varying estimates, making it difficult to develop a consensus view.</li> <li>• Tends to be more time consuming.</li> </ul>

Secondary sources include information from government statistic offices (such as the US Census Bureau’s Annual Survey of Manufacturers (ASM)/Census and Eurostat), trade statistics (from sources like the US International Trade Commission (USITC) and UN Comtrade), trade association data and publications, press releases, investor presentations and analyst reports, among others.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Government and trade statistics are widely available for a variety of industries.</li> <li>• Provides insights on views held by others knowledgeable of the market.</li> <li>• Can provide a good sense-check for estimates developed through different approaches.</li> </ul>	<ul style="list-style-type: none"> <li>• The scope and segment definitions in secondary sources may not align with those desired.</li> <li>• Access to the assumptions used to develop estimates published in secondary sources is typically limited, making the accuracy of such sources more difficult to assess.</li> </ul>

## 4. What technique should I use for market size estimation?



There are fundamentally two different approaches to sizing a market: top-down analysis or bottom-up analysis. Ideally, in any market sizing exercise, both of these methodologies should be used to ensure the appropriate reliability of the data and to point out any areas requiring further research for reconciliation.

- In a top-down approach, the starting point is an existing (or easily developed) estimate of total demand for a given product that needs to be further segmented or refined based on the outlined scope of the exercise.
- In a bottom-up approach, demand is calculated by applying usage assumptions to an indicator or statistic that directly relates to the product being consumed (ie, a direct indicator).

**Top-Down Analysis**

When deciding whether to use this form of market sizing analysis, it needs to be determined if a reliable top-line demand estimate is available. There are numerous sources that one can turn to in search of a top-line demand estimate, each of which have advantages and disadvantages that need to be balanced in the performance of this analysis. Often times, more than one of these techniques can, and should, be used in conjunction with one another.

**Option #1: Multi-client research from publishers such as [The Freedonia Group](#), [Kalorama Information](#), [Packaged Facts](#), and [Simba Information](#).**

There are an increasing number of publishers on the market offering products with varying degrees of underlying research and accuracy. As such, if you choose to use this method, it is important to source your information from reputable sources, such as the MarketResearch.com publishing brands above.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Often the quickest way to get an estimate of demand.</li> </ul>	<ul style="list-style-type: none"> <li>• Multi-client studies are intended to provide a broad overview of large industries.</li> <li>• The scope and segment definitions in multi-client studies may not align with those desired.</li> </ul>

**Option #2: Apparent consumption calculated from government production and trade statistics.**

If reliable industry shipment/production statistics and import/export data exist for a given product, via the ASM and USITC, respectively, it may be possible to estimate demand by estimating apparent consumption, which is calculated using the following formula:

$$\text{Apparent Consumption} = \text{Domestic Production} - \text{Exports} + \text{Imports}$$

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Government and trade statistics are widely available.</li> <li>• Government statistics bureaus are trusted sources of data.</li> <li>• Often, time series data is available for a number of historical years, making forecasting easier.</li> </ul>	<ul style="list-style-type: none"> <li>• Statistics are often limited to highly aggregated industries.</li> <li>• Apparent consumption does not take into consideration inventory held by end users.</li> <li>• Use of trade codes may vary by country (i.e., a product may be classified according to different codes depending on the country).</li> </ul>

**Option #3: A production census of leading suppliers in markets with a concentrated supply base.**

When the supply base is sufficiently concentrated (e.g., fewer than 10 suppliers), top-line demand estimates can be developed by summing the sales (or production) of leading manufacturers of the product being researched.

**Bottom-Up Analysis**

The bottom-up approach is typically taken when no reliable sources of top-line demand exist or when a more reliable estimate can be developed by analyzing product consumption as it relates to a direct indicator. This approach can be more time consuming than a top-down methodology and is sensitive to seemingly small assumptions that can cascade through the analysis. In deciding whether or not to pursue a bottom-up approach, several questions should be asked:

- Does product demand correspond intuitively to a direct indicator, such as houses, vehicles or households?
- Is there a readily available source for these direct indicators?
- Will it be possible to develop usage assumptions that may be applied to the direct indicator based on primary or secondary sources?

Product	Indicator	Assumption	Demand Estimate
Windows	During 2017, 1,200,000 new homes were constructed in the United States.	Newly constructed homes require on average 15 windows each.	Demand for windows was some 18.0 million units in 2017.
Paper Towels	In 2017, there were 240,000 quick service restaurants.	An average quick service restaurant spends \$500 per year on paper towels.	Demand for paper towels used in quick service restaurants was some \$120 million in 2017.

As noted, a bottom-up approach is sensitive to small changes in the underlying assumptions. As a result, it is generally good practice to independently validate the results of such analysis. Possible methods for validating results include cross-checking against other top-line estimates or testing the results with primary respondents.

## 5. How can I estimate future market size?



Methods of forecasting will vary depending on the demand estimation approach and data availability. However, forecasts are generally driven by an indicator that closely relates to product demand and assumptions on how product demand will evolve relative to that indicator.

For instance, future demand may be estimated in conjunction with a forecast for an underlying measure or indicator like the number of new homes constructed or the number of quick service restaurants. Furthermore, a forecasting exercise can be further refined by incorporating assumptions on product specific trends into the model. For example, adjusting the assumption for the average number of windows from 15 to 14 to account for a trend toward smaller homes or that quick service restaurants will spend less on paper towels due to the increasing prevalence of automatic hand dryers.

One additional factor to consider in forecasting, especially annual forecasting, is the stability of the industry being analyzed. All else being equal, the difficulty of assessing and forecasting demand increases as expected volatility rises. An extreme example would be capital equipment in a highly volatile industry like oil and gas, where oilfield drilling rigs purchases can vary by an order of magnitude over a 3–5 year period.

While each of the market research techniques outlined above can be helpful in estimating market size, it is the process of combining a number of these methodologies that sets Freedonia Custom Research apart. Our analysts average more than five years of experience in market intelligence, with a diverse set of technical and business-related backgrounds that give us flexibility in our approach to each project. Additional valuable information related to market sizing and opportunity identification that can be compiled via Freedonia Custom Research's primary and secondary research techniques include competitive intelligence/market share and value chain information, as well as voice-of-market insights.

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