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ASH MAURYA

RUNNING LEAN

Iterate from Plan A to a Plan That Works

Early Release

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THE **LEAN** SERIES
ERIC RIES SERIES EDITOR

Running Lean

THIRD EDITION

Iterate from Plan A to a Plan That Works

With Early Release ebooks, you get books in their earliest form—the author's raw and unedited content as they write—so you can take advantage of these technologies long before the official release of these titles.

Ash Maurya

Running Lean

by Ash Maurya

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Introduction

A NOTE FOR EARLY RELEASE READERS

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A Tale of Two Entrepreneurs

I'm going to start by telling you a story about two entrepreneurs.

Let's call them Steve and Larry.

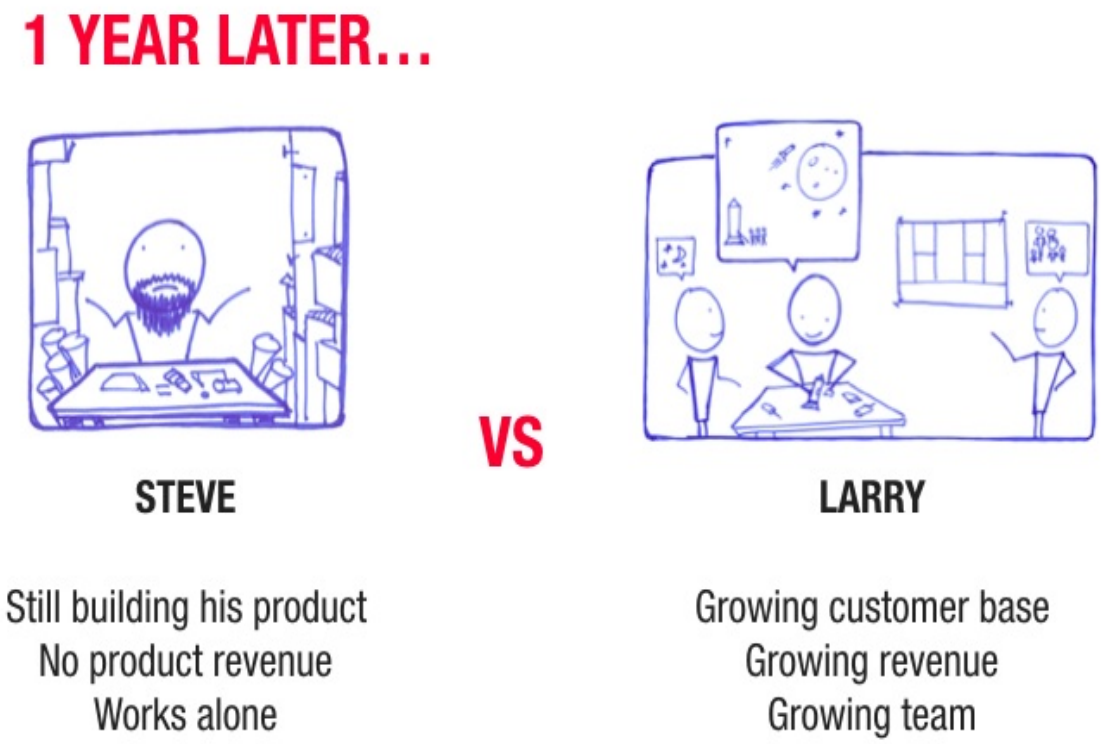
Both of them studied at the same university, got good grades, and after graduation, both went on to work at a high-tech startup where they quickly grew into key roles.

After a few years, they both get hit with an idea for a startup and decide to quit their jobs and venture out on their own.

Even though I've given them names to make them more personable, I want to emphasize that what makes them similar isn't their age, gender, or geography, but that they both got hit with a "big idea" and decided to act upon it…

Entrepreneurs are everywhere.

They look quite similar at the outset, but what differentiates them is how they look a year later.



A year later, Steve is still building his product. He has **no product revenue** and relies on part-time freelancing work to fund his product development. And he **works alone**.

Larry, on the other hand, has a **growing customer base, growing revenue, and a growing team**.

How did each of them end up in such a different place?

To answer that question, let's take a flashback…

A Build-First or Investor-First Approach is Backwards

1 year ago…

Steve is at this desk lost in thought. Earlier that day, his manager told him that their parent company (from a recent acquisition) would be shutting down their offices in a couple of months. And Steve was given a choice to either relocate to

headquarters or take a severance package.

Steve reads this as a sign.

He had always planned on starting his own company when the timing was right. After graduating from university, he made a conscious decision to join a promising startup in order to gain some first-hand experience, before venturing out on his own. Even though his startup had a few bad product starts, they did eventually manage to get acquired. Steve felt really proud to have been part of the core team.

“This may be as good a time as any…” he thinks to himself. He decides to take the evening to think things over.

Steve estimates that if he keeps his expenses in check, the severance package and his savings would provide him with a year of runway to get something off the ground. He does have this one augmented reality (AR) / virtual reality (VR) idea that he’s been noodling around in his head for a few months already…

The next day, he decides to take the plunge and accepts the severance package.

Off to the races…

Steve wastes no time getting to work and immediately starts building out his product. He anticipates that if he stays focused and works full-time without distractions, he should be able to launch the first version of his product in three months.

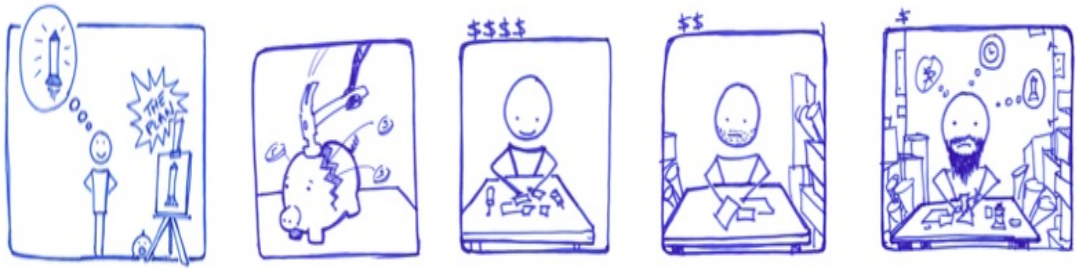


Figure I-1. Steve in the metaphorical garage

He wants to build his product the “right way”, so like a craftsman, he

meticulously goes about designing and building his product.

But little things start taking longer than expected and begin to add up — weeks quickly turn into months.

6 months later…

Steve is starting to get nervous. The product isn't up to his standards and his revised estimates put the product out at least another three months…maybe even six months.

He'll be out of money by then.

He realizes he needs help.

He hits up some of his close friends and tries to recruit them — offering up generous equity in exchange. But they don't see what he sees, and find it hard to justify leaving their well-paying jobs.

Figure I-2. Nobody sees what Steve sees

Steve attributes this setback to a **"lack of vision"** on his friends' part, and is **even more determined** to find a way to finish his product.

He decides to hit the pitching circuit and **raise money**.

He starts by contacting his previous startup's founder, Susan, who readily agrees to meet with Steve. Susan likes the idea and offers to introduce Steve to a number of investors.

She leaves him with this advice: "Make sure you put together a bullet-proof business plan first."

Steve has never written a business plan before. So he downloads a few templates

and picks one he likes. As he starts writing, he finds that he doesn't know the answer to many of the things being asked, but does his best anyway to complete the plan.

He's especially encouraged by the financial forecast spreadsheet.

The more he plays with the numbers, the more he's convinced that he's on to something really big. He even has to tweak a few numbers down to downplay the fantastic model he has created.

He knows a lot is riding at stake, so he spends many more days developing his elevator pitch, outlining his product roadmap, and polishing his 10-page slide-deck.

He reaches out to Susan a few weeks later who helps him set up half a dozen meetings with investors. Steve is a nervous wreck during the first few meetings but thinks they went okay. He starts to get more comfortable with practice and feels a lot better about his later meetings.

He doesn't get an instant yes. But at least he doesn't get an outright rejection either. He debriefs Susan later who reluctantly bursts his bubble.

> *…Sorry Steve, but "you're too early for us" and "let's touch base in six months" are code for "we're not interested, but too polite to say no"…*

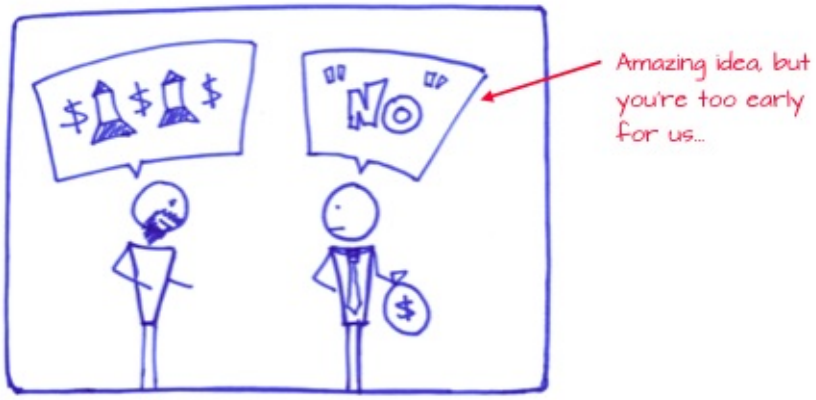


Figure I-3. Investors have mastered the art of the polite no.

Catch-22

Steve is in a classic Catch-22. He can't make people see his vision until he

completes his product, but investors won't give him the resources to complete his product.

What is he to do?

Figure I-4. Catch-22

Steve still believes in his product and is determined to build it.

He retreats back into his metaphorical garage and decides to self-fund his idea with part-time freelancing.

Progress is slow, but at least he's still working on his product, nights and weekends, towards moving his idea forward…

Larry too was hit by an awesome idea a year ago, but unlike Steve, **he doesn't start with a build-first or an investor-first approach**.

A Traction-first Approach is the New Way Forward

Larry recognizes that this approach used to work at a time when building products was really hard and expensive, but the world has changed.

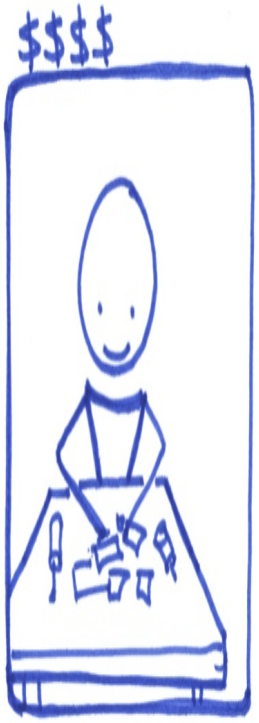
Investors used to value intellectual property and funded teams that demonstrated they could build stuff. But this is no longer the case…

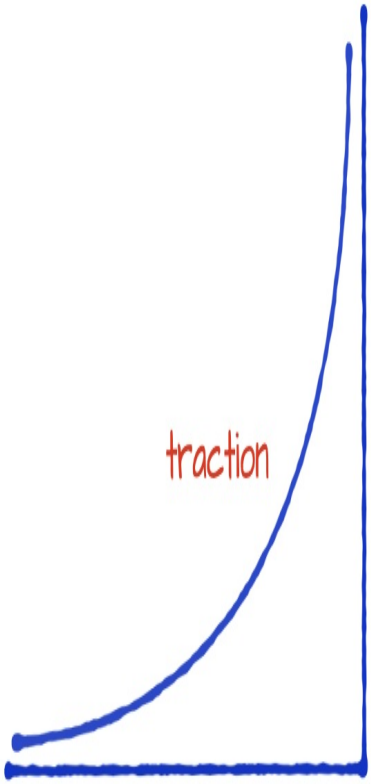
Also, because building products was prohibitively expensive, teams that managed to raise funding used to have a significant unfair advantage over others

because they could get to market faster and learn faster than their competitors. Even if they got the product completely wrong the first time around, they could still manage to course-correct and get back on track because there were very few competitors nipping at their heels.

But the world is quite different today…

WE ARE LIVING IN A NEW WORLD





OLD WORLD

Hard to build products

Not too many competitors

Few choices for customers

NEW WORLD

Easier to build products

A lot more competition

Lots of choices for customers

Figure I-5. We are living in a new world

We are living through a global entrepreneurial renaissance. Today, it is cheaper and easier than ever to build a product, which means that there are many more people “starting up” all over the world.

> *There were 100M new startups created globally in 2018. That’s 1 new startup every 3 seconds!*
>
> —Global Entrepreneurship Monitor

While this explosion in startup activity represents an incredible opportunity for all of us, it comes with a dark cloud: More products translate to more choices both for investors and customers — making it harder to stand out.

Investors today don’t value intellectual property, but *traction*. Traction isn’t about being first to market, but first to market *adoption*.

Traction is evidence that people other than yourself, your team, and your mom care about your idea — aka customers. More importantly, traction is evidence of a working business model.

Investors today don’t fund solutions that work; they fund business models that work.

But how do you demonstrate traction without a working product? Aren’t we back to the Catch-22? Not really, because Larry knows that customers today are constantly bombarded with a multitude of product choices. When customers encounter a half-baked product, they don’t turn into beta-testers and give you feedback, *they leave*.

Without customer feedback, it’s too easy to fall prey to the “build trap” where breakthrough always seems one killer feature away but remains ever-elusive. You end up spending needless time, money, and effort **building something nobody wants until you run out of resources**.

Larry has experienced this build-trap one too many times before with his past products, and this time decides to level up his game and start with a better foundation for his product. A fundamental mindset shift for doing that is starting with problems before solutions.

Customers don’t care about your solution but their problems.

He understands that if his product doesn’t solve a big enough problem for his customers, no amount of technology, or patents, or giveaways can save his business model.

This leads to a number of epiphanies for Larry:

MINDSET #1: The business model is the product.

MINDSET #2: Love the problem, not your solution.

MINDSET #3: Traction is the goal.

Larry spends half an afternoon sketching out a business model design for his idea using a 1-page template (Lean Canvas) that was recommended to him by one of his trusted mentors.

He then tests the viability of his business model using a quick back-of-the-envelope calculation, and from there builds out a traction roadmap that highlights his key milestones. This helps him map out a bottoms-up go-to-market validation strategy.

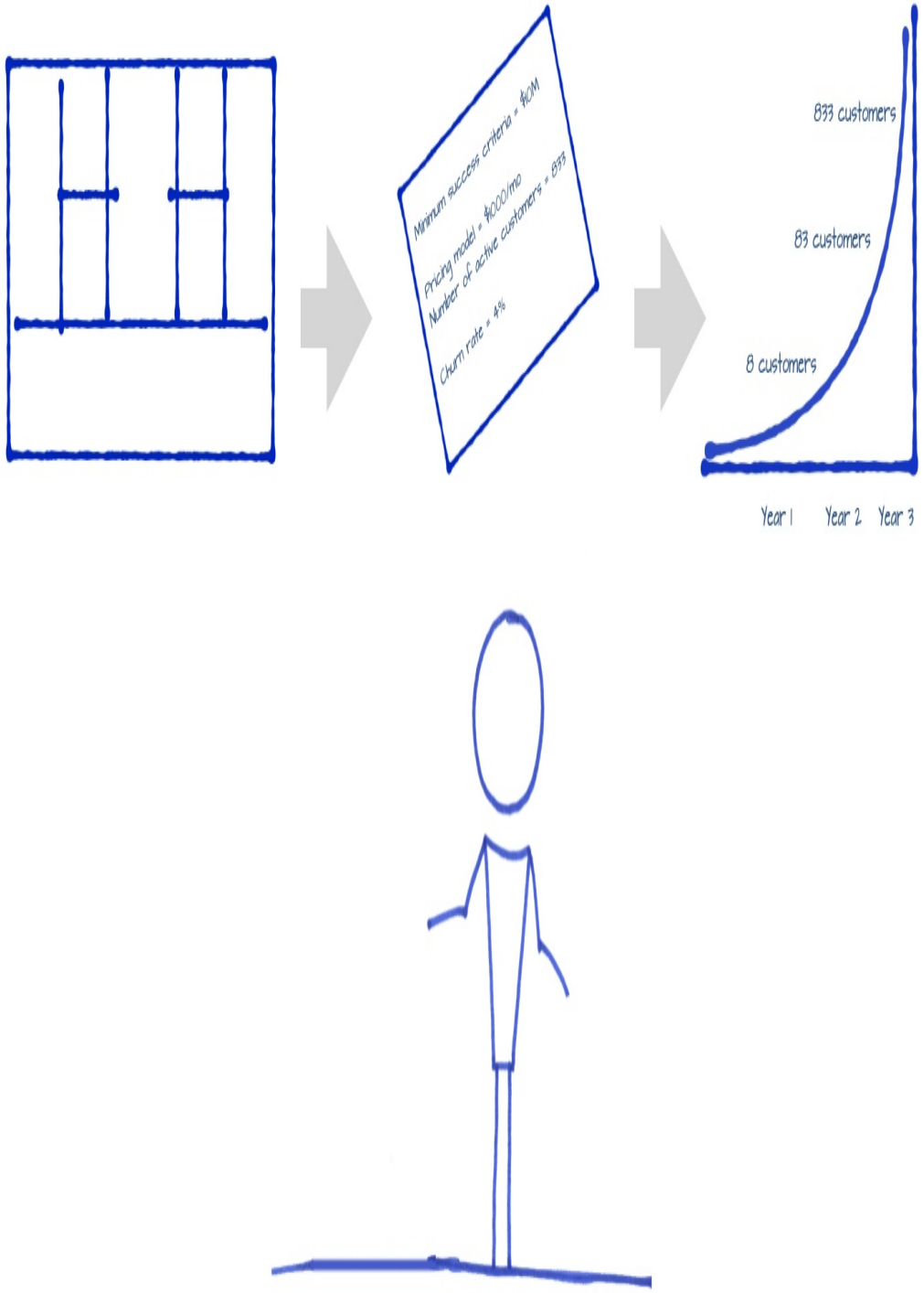


Figure I-6. Larry does some quick business modeling of his idea

A key difference in his validation strategy from Steve's is that he prioritizes

testing what's riskiest versus what's easiest in his business model.

Larry correctly recognizes that in the new world what's riskiest for most products has shifted from technical risks to customer and market risks.

The challenge question today isn't asking: "Can we build it?" but: "Should we build it?".

This is why he decides to take a traction-first approach versus a build-first or investor-first approach.

MINDSET #4: Right action, right time.

And here's the really counterintuitive bit…You **don't need a working product** to uncover problems worth solving and get even acquire your first batch of paying customers.

Unlike Steve, who is still perfecting and polishing his product a year later, Larry manages to define his minimum viable product (MVP) in less than 8 weeks with a growing customer pipeline.

A minimum viable product (MVP) is the smallest solution that creates, delivers, and captures customer value.

Following this approach, Larry avoids spending needless time, money, and effort building a product **he *hopes* customers will buy** and instead builds a product **he *knows* customers will buy**.

Steve is following a BUILD-DEMO-SELL playbook, while Larry is following a DEMO-SELL-BUILD playbook.

This puts Larry's idea on solid footing and he spends the next 4 weeks building out the first version of his solution aimed not at everyone, but at his ideal early adopters. Once his MVP is ready, he doesn't do a big-bang marketing launch, but rather soft launches his product to just 10 early adopters and starts **charging them from day one**.

His logic for starting small and making a bold promise is putting his money where his mouth is. He thinks to himself: "If I can't deliver value to my first 10 handpicked customers, what makes me think I'll be able to do that with thousands of customers trying the product on their own?"

MINDSET #5: Rollout in stages.

A nice side-effect of starting small is that Larry can afford to provide a high-touch customer experience, which lets him sidestep a few shortcomings of his MVP and still over-deliver on value — while maximizing learning from his customers.

> *Do things that don't scale.*
>
> —Paul Graham

His first batch of customers are blown away by Larry's attention to detail and responsiveness to their needs. He manages to convert all of them into true fans while continually refining his MVP.

Even though Larry is a jack-of-all-trades, he recognizes that he can't scale his business on his own. So he invests a third of his time pitching his vision to potential co-founders. He doesn't look for people just like him, but rather searches for people with complementary skill sets to his, because he knows that

- good ideas are rare and hard to find,
- good ideas can come from anywhere, and
- that finding good ideas requires lots of ideas.

The fact that Larry already has happy paying customers (early traction) and a growing customer pipeline allows him to attract and recruit his dream team.

Too many teams take a divide-and-conquer approach to testing their business model where they split their focus based on individual team member strengths. For example, hacker types focus on product and hustlers focus on customers. This spreads the team thin across many different priorities, and is sub-optimal for good idea generation.

Larry instead meets with his team on a 2-week cadence (lean sprints) to

1. Align around a set of key goals, assumptions, and constraints in order to dive the focus of the entire team on their riskiest assumptions.
2. Solicit a diversity of possible solutions from the entire team and place bets on the most promising ideas based on evidence-strength versus opinions.

3. Use small and fast experiments to quickly kill off bad ideas and double-down on good ideas.

MINDSET #6: Place Many Small Bets.

He uses these lean sprints to instill a validation framework across his entire team built on the following additional mindsets:

MINDSET #7: Make evidence-based decisions.

MINDSET #8: Discovery before validation.

These mindsets allow his team to systematically search for a repeatable and scalable business model. The journey isn't a straight-shot to success. There are twists and turns, dead-ends and back-tracking. But because his team is moving fast and constantly learning, they avoid huge big-bang failures by making many small course-corrections along the way.

MINDSET #9: Breakthrough requires unexpected outcomes.

By the end of the year, his customer base is growing, his revenue is growing, and so is his team. His business model is on track to achieving product/market fit.

What Determines Success Isn't Differing Skill Sets But Differing Mindsets

The difference between Steve and Larry is not differing skill sets but **differing mindsets**.

Steve is operating like an Artist and is primarily driven by his love for his product (solution).

You can easily substitute Artist with Software Developer, Designer, Creative, Maker, Writer, Author, Hacker, Inventor…

He takes a build-first approach which in today's world is highly risky.

Larry, on the other hand, is operating like an Innovator.

Innovators turn inventions into working business models.

He recognizes that we are living in a new world where the rules have changed.

Today, it is no longer enough to simply build what customers say they want, because by the time you build that, you learn that what they really wanted was something quite different.

In this new world, **the only way to ensure you build what customers want is to engage them continuously**.

The stakes are much higher this time

The old way of building products used to work at a time when there were huge barriers to entry and few competitors. Even if you got the product completely wrong, you had time to course correct and get back on track.

But fast forward to today, it has become cheaper and faster than ever to introduce new products which means there is **a lot more competition than before**—both from incumbents and new companies starting up all over the world.

In the old world, failing to deliver what customers wanted led to failed projects. But in the new world, continually failing to deliver what customers want, leads to total business model failure.

This is because customers today have **a lot more choices** than they did before. If they don't get what they want from your product, they simply **switch to something else**.

On the other end of the spectrum, the most successful companies today realize that good ideas are rare and hard to find. And that the best way to find the next big idea is to **quickly test lots of ideas**.

While the early adopters for this new way of working were certainly high-tech startups like AirBnb and Dropbox, over the years continuous innovation has been increasingly applied in many different domains and it works even at massive scale.

Some of the most valuable companies in the United States like Google, Netflix, Amazon, Facebook, etc. all practice a culture of continuous innovation.

Speed of learning is the new unfair advantage.

Companies that continuously learn fast, outlearn their competition and get to

build what customers really want.

This is the essence of **Continuous Innovation** and the approach that Larry takes. When you're going really fast under conditions of extreme uncertainty, you can't afford to spend long cycles analyzing, planning, and executing your idea. You need a more iterative approach.

Larry powers his search for a repeatable and scalable business using a Model-Prioritize-Test flywheel.

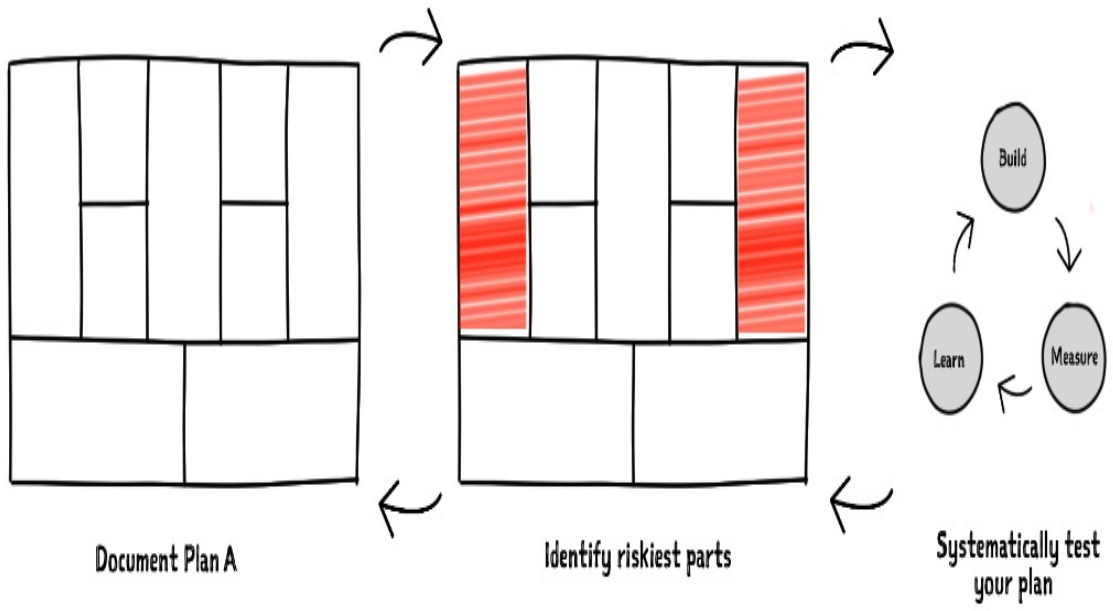


Figure I-7. Model-Prioritize-Test

He starts by

- deconstructing his idea as a business model,
- identifying what's riskiest in his business model, and
- systematically testing his business model.

Succeeding in the new world requires new mindsets

Too many people fail at Continuous Innovation because they start in the wrong place - cherry-picking on tactics without first internalizing the underlying

mindset behind the tactic.

Mindsets describe how we perceive the world around us and act.

If you believe that we are indeed living in a new world, then it should naturally follow that a new world requires new mindsets.

Here are the ten mindsets that power the Continuous Innovation Framework described in this book:

MODEL

- **MINDSET #1: Your business model is the product.**
- **MINDSET #2: Love the problem, not your solution.**
- **MINDSET #3: Traction is the goal.**

PRIORITIZE

- **MINDSET #4: Right action, right time.**
- **MINDSET #5: Rollout in stages.**
- **MINDSET #6: Place many small bets.**

TEST

- **MINDSET #7: Make evidence-based decisions.**
- **MINDSET #8: Discovery before validation.**
- **MINDSET #9: Breakthrough requires unexpected outcomes.**

You Can’t Afford to Wait For An Idea Whose Time Has Come

It’s been a little over 18 months since Steve quit his day job and ventured out on his own. Even though, his savings ran out 6 months ago, he has hit a comfortable groove using freelance consulting to keep his product development going.

He’s come to terms that bringing his vision to life is going to take its due course,

but he’s not in a hurry. Rome, after all, wasn’t built in a day.

It’s a Tuesday morning and Steve is in line waiting to order his morning coffee before heading to a client site for a meeting. He gets a text message from an old buddy of his:

> Have you seen what Virtuoso X just launched? It’s your idea Steve!!!

Steve clicks through the link, scans the page, then goes white…

Virtuoso X does look very similar to what he has been working on for the last year and a half. They just got covered by Techcrunch and announced a big fundraise.

He starts feeling sick to his stomach and leaves the coffee shop. He reschedules his client meeting from his car and heads back to his home office instead.

There, he spends the rest of the day poring through Virtuoso X site, trying out their app, and searching online for anything he can find on them. After several hours, he concludes that while the idea is indeed similar, Virtuoso X’s implementation of the idea is quite different from his.

Steve feels a bit relieved because he believes he still has the more elegant solution. But that relief is short-lived as a new anxiety sweeps over him: “What good is a better solution if I launch too late or never get to launch it?”

He needs to kick things back into high gear.

Maybe now he can get the support of his developer friends who failed to see his vision earlier? Or maybe now he’s have an easier time raising funds from investors?

A million ideas start racing through his head. Where should he start?

He decides to reach out to Mary for advice.

Steve used to report to her in his previous startup. Like him, she too had taken the severance package after their startup got acquired and then shut down. He had run into her at an event a few months back and learned that she had also started a new company with a few other co-workers. And by all accounts, they seemed to be doing quite well. They already had over 30 employees, paying

customers, and venture funding.

He shoots her an email, briefly outlining his situation, and asks to meet for lunch.

He gets a near-instant reply:

> Let’s meet for tacos tomorrow at noon—usual spot.

Steve learns about Minimum Viable Products

Steve gets to the restaurant a few minutes before noon and grabs a quiet table in the back. As he settles in, he notices a text message:

> Sorry, running 10 minutes late—deployment day.

He takes the extra time to organize his thoughts and doodles out a high-level plan in his journal:

1. Secure seed funding.
2. Hire 3 developers.
3. Finish and launch platform in 3 months!

Just then, Mary walks over.

“Sorry for being late Steve. We have a big rollout this week and we have been fighting several production issues all morning. I would normally have rescheduled, but your email sounded urgent. What’s up?”

Steve pulls out his phone, hovers it over the table for a few seconds, and then asks Mary to take a look. A bewildered expression flashes across Mary’s face and she stretches out her hand as if to grab something on the table, but her hand just waves through air. She bursts out laughing.

“This is the most realistic AR (augmented reality) app I’ve ever seen. This coke can and glass of ice sitting next to it is so inviting. It’s making me thirsty.”

“I’m glad you think so. I’ve developed a way to render any real world object as a 3D model inside an AR or VR (virtual reality) application without having to write any code or use complex modeling software. All you need to do is take a few pictures of the real world object using the phone’s camera and the rendering engine builds the 3D model in a couple of minutes. I generated these models while I was waiting for you.”

Mary nudges Steve to go on.

Steve takes the next 5 minutes to summarize what he’s been up to over the last year, the Virtuoso X launch, and his high-level plan for moving forward.

Mary listens patiently and then asks him a simple question:

“Would you rather spend the next 6 months pitching to investors or pitching to customers?”

Seeing the puzzled look on Steve’s face, she goes on to explain that even in the best case scenario, raising money without traction is typically a six months process and a full-time job:

“…during that time you’re not going to make much progress on your product. So given your estimates, you’re probably looking at 9 months to a launch.”

“I can’t afford to wait 9 months!” blurts out Steve.

“Virtuoso X has the first mover advantage. By then, they would have cornered the entire market!”

Mary adds: “I know this will sound cliche, but… competition is a good thing. Competition helps validate a market and most first movers really have a disadvantage, not an advantage. Facebook, Apple, Microsoft, Toyota…I can keep going… weren’t first movers. They were all fast followers.”

Steve isn’t convinced, but nods his head anyway.

“Okay…but I still need to launch something sooner than 9 months.”

“That, I definitely agree with. Yes, you do.”

“But for that I need more developers. And I can’t hire more developers without money…”

Mary cuts him off. “You need to get to an MVP that customers want.”

“An MVP?”

“A minimum viable product.”

“Is that like a beta?”

“Sort of…but not really…a minimum viable product is the smallest solution you can build that delivers monetizable value to your customers. I know you have a big platform vision in mind, but customers don’t care about platforms. At least, not at the beginning… They care about solutions that solve their immediate problems. You need to find the smallest solution that solves a big enough customer problem and deliver that. To do that, you have to really narrow down on your ideal early adopters first and not go too broad. When you’re trying to market to everyone, you reach no one.”

Just then Mary’s phone goes off and she glances at the screen.

“Sorry, I’m needed back at the office. My best advice for the moment is to read up everything you can on MVP. Investors today don’t fund ideas, or product development, but traction. And you need customers to demonstrate traction.”

Steve interjects. “How much traction is enough?”

“If you can demonstrate any traction at all, it sets you apart from the pack. That’s what we did before we spoke to any investors. Having just 5 paying customers gave us leverage and completely changed the dynamics of fund raising for us. Today, we have ten times that number of customers, but without those first five, our pitch would have just been a bunch of promises. Let’s meet again once you have defined your MVP.”

Steve thanks Mary for her time as she takes one last bite of her lunch and then storms out of the restaurant.

Don’t Start With an MVP

It’s been 3 weeks to the day since Steve’s meeting with Mary. He’s meeting with her again to give her an update.

“I followed your advice. I read up on MVPs and since I had already built out quite a bit of the product, I was able to launch my MVP within a week…but I don’t think it’s working.”

He pauses for a second, then goes on:

“I’ve got lots of users signing up everyday, which is great, but no one has upgraded yet, and retention is quite low—most users never come back after the first day. I’ve been running all kinds of A/B tests and even pivoted a few times. I’ve concluded that my MVP isn’t good enough. The product is still missing several core features. Though I think I’ve finally figured out the killer feature and I’m planning on building that next…”

Mary cuts off Steve:

“Let’s back up a bit…Who are these users? And where are they coming from?” Mary asks.

“I announced my product launch in a few online communities, like Product Hunt and Hacker News. That announcement generated some buzz. Some of the traffic is still coming from there. The rest are coming from online ads. I set up a small budget of $10/day.”

“Okay. And who are these users? Have you talked to them?”

Steve looked a bit surprised.

“Talked to them? No. But I’ve been measuring everything they do using analytics. That’s how I know retention is really low.”

“I see… we made a similar mistake after our MVP launch. We stopped talking to our customers and relied solely on metrics to guide us. The problem with metrics is that they can only tell you what’s going wrong, but not why. We kept guessing at what was going wrong, but nothing we did worked. It was only when we started talking to our customers again, that we were able to truly understand why things weren’t working, and turn things around. You have to keep talking to your users, Steve.”

Steve cleared his throat. “Keep talking to my users? I’ve never talked to any of them.”

It was now Mary’s turn to look confused.

“Huh? Then, how did you define your MVP?”

“Well, I had really built up so much of the platform already that I was able to quickly launch a small reference application that showcased the power of the

platform. You said I needed to ship something. Isn't the premise of the MVP to rush to ship a first release, which kicks off the learning cycle… then use fast experiments to iterate and refine the product?"

Mary sighs.

"Sorry Steve, I should have warned you that MVP is quite a loaded term with many different definitions and approaches out there. Yes, a lot of people subscribe to that approach. And to be fair, it's still a better approach than spending a year building out a more complete product—only to find out that you've overbuilt or worse built something nobody wants."

Mary notices that Steve blushes a bit at her last comment. She chooses to ignore it and goes on:

"But, simply throwing your best guess at a solution, no matter how small, over the fence, and calling that an MVP, doesn't guarantee any better results."

"Doesn't the Lean Startup Build/Measure/Learn loop help you iterate and refine the MVP?" Steve asks.

"In theory yes, but a lots of teams just get stuck. Think of the Build/Measure/Learn loop as a fast idea validator. If you put a reasonably good idea in AND manage to attract early adopters, it is possible to iterate and refine your MVP as you describe. But if you start with a bad idea, all you learn is that your idea sucks. And then you're stuck."

"Why is that?" Steve asks.

"Because customers today have lots of choices. If your MVP fails to resonate with them, they don't turn into testers and patiently deliver you feedback on how to improve your product… they simply leave—a lot like your low retention users. You are then left guessing why things aren't working which kicks off the search for the mythical killer feature—the one that always feels like it's just around the corner. Sometimes you get a lucky break, but more often than not, you find yourself going around in circles, trying out one idea after another, but are never able to break through. The build trap ensues."

Steve's eyes widen as Mary just succinctly summarized his situation.

He then asks her the obvious question: "If success is predicated on the quality of the starting idea, how does one start with a reasonably good idea?"

“That is the right question, Steve. You do that by focusing on problems before solutions. The challenge today isn’t building more features, but uncovering what to build.”

A puzzled look comes over Steve, so Mary adds:

“Think of it this way… starting with a solution is like building a key without a door. Sure, you can build a great looking key quickly, but then you spend the rest of the time searching for the right doors to open. You might get lucky or brute force your way in, but where you end up is usually not where you expected to be…”

She waits for a nod from Steve, then goes on:

“If you simply flip this around and start with doors, or problems worth solving, key building becomes a lot easier. You start building keys to doors that actually take you places.”

“And, there is a process for doing this?” Steve inquires.

“Yes. That was what I was hoping you’d find in your research on MVP. We didn’t start with building an MVP in our startup, but an offer. We first sketched out several variants of our idea on a Lean Canvas which is a rapid idea modeling tool. That helped us identify and home in several promising customer-problem-solution possibilities. We then set up some two dozen customer interviews to validate our customer and problem assumptions. Once we did that, defining the solution was a piece of cake. But even then, we didn’t rush to build out an MVP. We built a demo instead and assembled an offer that we delivered to prospects over many more interviews. Only when we got enough customers to buy into our offer, did we start building out the MVP. What we eventually built looked very different from what we thought we’d build.”

Mary pulls out her phone and looks up the image below that she shows to Steve.

“Ah, so that’s what you meant the last time by ‘define’ an MVP?”

“Exactly. You raise your odds of success significantly by spending the requisite time first defining the MVP, then validating it using an offer, before building it. Think of it as Demo-Sell-Build versus the more traditional Build-Demo-Sell approach.”

“And how long did all of this take you? It seems like a lot of steps.”

“It took us about 90 days to go from just a napkin sketch to problem/solution fit where we secured our first 5 paying customers. And yes, there are more steps than simply rushing to build an MVP, but if you follow the process and stay disciplined, you end up with a mafia offer.”

“A mafia offer?”

“Yes. An offer your customers cannot refuse. You know, from the movie: Godfather. Unlike the movie you don’t strong-arm your customers, but instead show them something so compelling, they just can’t turn it down. At the end of the 8 weeks, we ended up with 5 paying customers who were pushing us to deliver them the MVP quickly versus the other way around.”

“Hmm…This is a very different approach to product development than I’m used to, but I’m starting to see the logic of it. But I’ve already launched my product and have users. Can I still apply this process to my product or do I have to start all over from scratch?”

“You can definitely apply this process to an existing product provided you’re willing and open to trying a new way. As you just pointed out, this approach is different and different often feels uncomfortable. The biggest obstacle for us was unlearning old product development habits and instilling new mindsets across the entire team. The good news is that the learning and results come quickly so you don’t have to run on faith alone.”

“I still have a hundred tactical questions on how to actually do any of this. How do get users to talk to you? How many people do you talk to? What do you say to them? You’ve been very generous with your time, but can you guide me a little further.”

“Definitely Steve. This process, like any, has its fair share of sand traps and pitfalls. The biggest one is our own bias or love for our solution - our Innovator’s Bias. We selectively, and even unconsciously, choose to only pay attention to what justifies building the solution we’ve already envisioned. Shifting to a problem first mindset sounds simple, but it isn’t easy.”

“Are there tools or resources you can point me to?” Steve asks.

Mary smiles.

“Oh yes. I’ll send you a list of resources, tools, and actual customer interview scripts we used and continue to use to train our team. Uncovering problems worth solving isn’t limited to just the MVP phase… it’s key for everything that comes next also. I’ll warn you again that this will feel a bit weird and even uncomfortable at first. The key is to be patient, follow the process, and the results will come.”

“At this point I’ve spent 18 months doing things my way and it hasn’t worked. I’m open to trying, no testing, anything”.

Mary smiles again.

“Great—Let’s plan on talking again in 90 days… or less.”

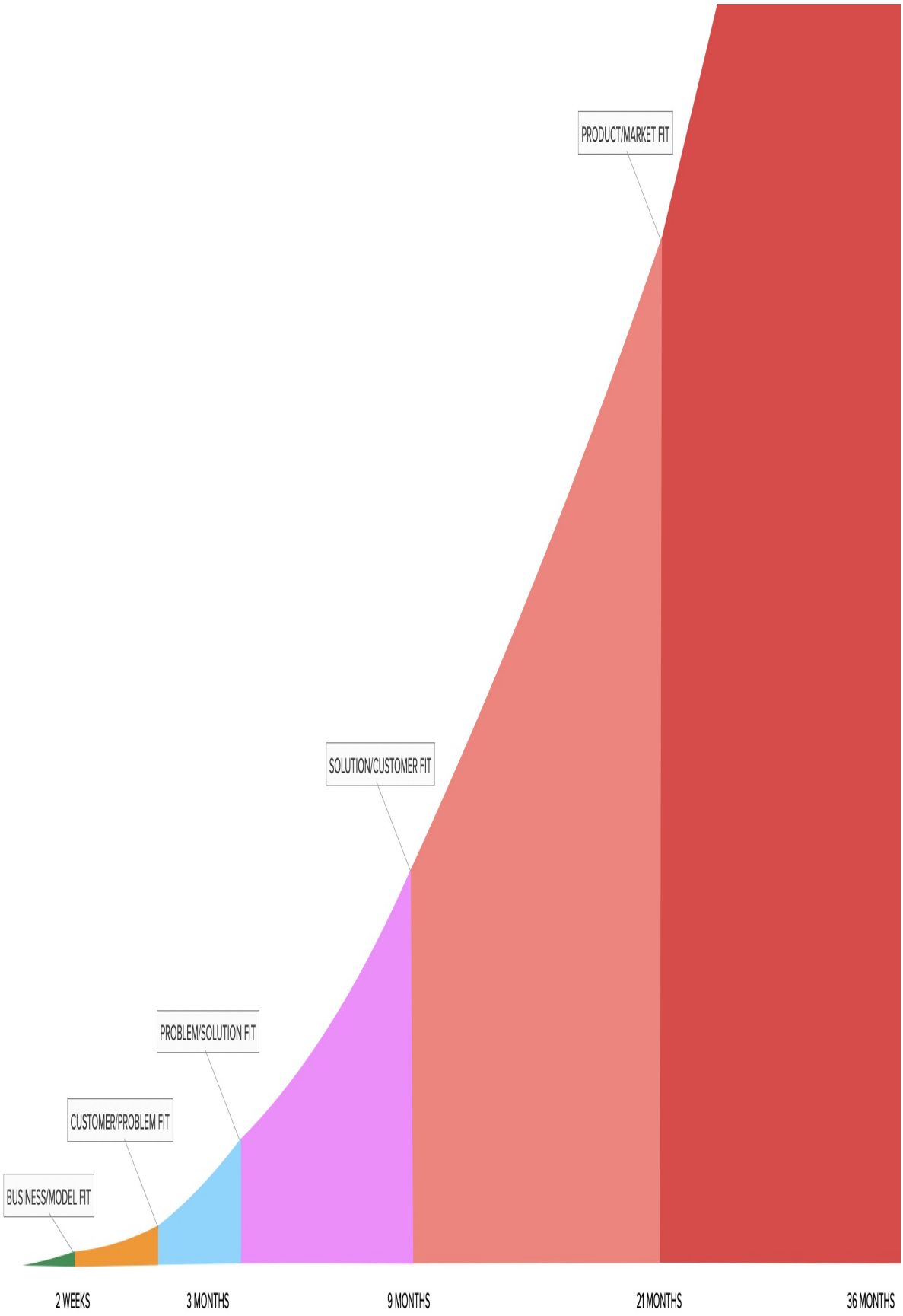
There is a Systematic Approach to Entrepreneurship

On his drive back to the office, Steve can’t help but replay his last conversation

with Mary in his mind.

Is it really possible to build what customers want (what Mary described as a mafia offer) just by interviewing customers? He ponders.

Sure enough, when he gets back to his office, he finds an email from Mary waiting in his inbox. As promised, she had sent him an extensive list of resources and a high-level roadmap:


PRODUCT/MARKET FIT
SOLUTION/CUSTOMER FIT
PROBLEM/SOLUTION FIT
CUSTOMER/PROBLEM FIT
BUSINESS/MODEL FIT
2 WEEKS
3 MONTHS
9 MONTHS
21 MONTHS
36 MONTHS

Steve quickly recognizes **Product/Market Fit** on the roadmap but a lot of the other terms are foreign to him.

He then reads Mary's email:

> *Hi Steve -*
>
> As promised, here are the links to the Continuous Innovation Framework and the playbooks we use.
>
> *There are lots of dots to connect so be patient.*
>
> The Continuous Innovation Framework uses 90-Day Model-Prioritize-Test cycles so be sure to start at the beginning and be sure to start with the modeling work. Then work your way through the other stages.
>
> *Lastly, remember that learning anything new often requires unlearning old habits. Apply and test the framework rigorously.*
>
> If you get stuck, you know where to find me.
>
> Mary

Steve gets to work and over the course of several weeks, he learns:

- How to deconstruct his idea into a business model.
- How to test whether his idea is worth pursuing.
- How to identify and prioritize the riskiest assumptions in a business model.
- How to stress test his riskiest assumptions using small and fast experiments.
- How to use customer interviews to learn from customers.
- How to achieve traction without a product.
- How to pitch to customers so they buy.
- How to operate and make decisions under conditions of extreme

uncertainty.

Over the next several months, Steve manages to bring his product back on track with paying customers, growing revenue, and a growing team.

This book shows you how.

Running Lean will outline a step-by-step process for iterating from Plan A to a business model that works, before running out of resources.

About Me

Hi, my name is Ash Maurya and I'm the founder of LEANSTACK and the creator of the popular business modeling tool: Lean Canvas. I too used to be a Steve. I too was hit by an awesome idea. An idea so good I never told anyone but close friends sworn into secrecy.

I spent a year building out my "big idea" in stealth. And, like Steve, I too struggled to get other people to see what I saw.

It took me roughly seven years to transition from Steve to Larry, and there's been no looking back ever since.

I attribute all the success and attention I've received over the years with my books and tools to this new way of thinking and approaching products.

LEANSTACK was founded to help the next generation of entrepreneurs avoid these same mistakes.

From here on out, this isn't a story of two entrepreneurs, but just one entrepreneur: Steve.

Steve, not Larry, is the hero of our story.

How This Book is Organized?

This book is organized into 3 parts.

PART 1: MODEL

Part 1 walks through the process of deconstructing your initial vision (or Plan A) into a business model and getting others to see what you see.

Part 2: PRIORITIZE

Part 2 helps you identify the riskiest parts of your business model that you should tackle first and formulate a validation strategy.

Part 3: TEST

Part 3 outlines a systematic process for stress testing your business model and shows you how to iterate from your Plan A to a business model that works in stages.

Is This Book For You?

Running Lean is for

- Aspiring and serial entrepreneurs,
- Corporate innovators and intrapreneurs,
- Product managers,
- Makers and visionaries who want to level up and build the next generation of products that matter.

Practice Trumps Theory

Everything in this book is based on first-hand experiential learning and experimentation on my own products and across thousands of other products built by teams I have advised and coached over the last 10 years.

I encourage you to rigorously test and adapt these principles for yourself.

No framework can guarantee success. But a good framework can provide a feedback loop for making better evidence based decisions in the face of extreme uncertainty.

That is the promise of this book.

Let’s begin.

Part I. Model

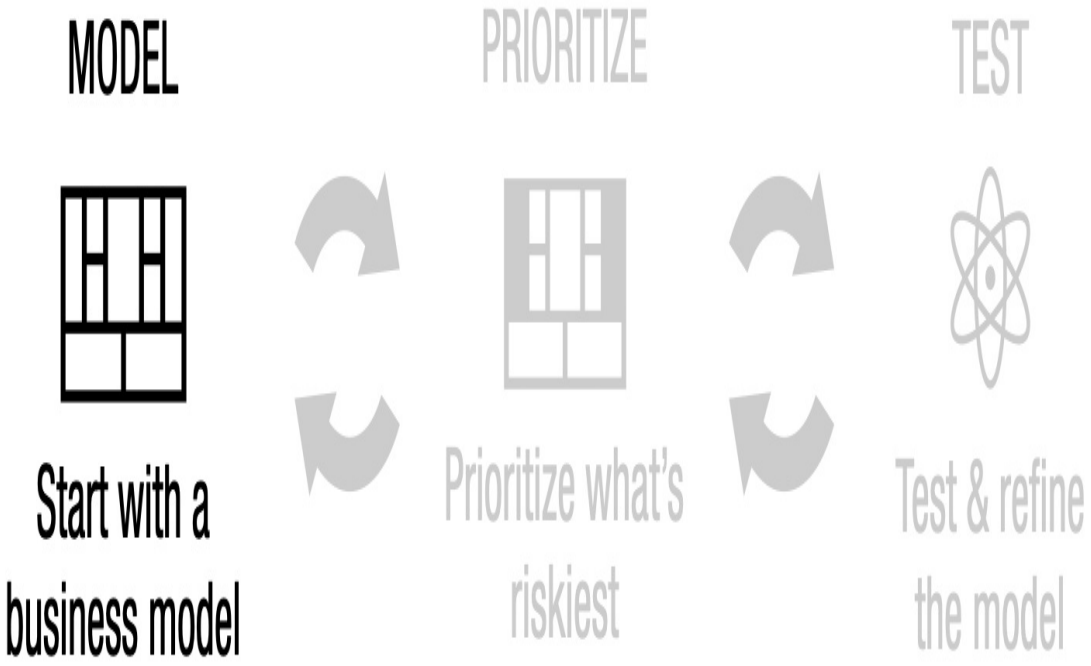


Figure I-1. Simple models help deconstruct the complex.

Too many founders carry their ideas in their heads alone which, while the fastest way to iterate, only helps to further their own "reality distortion fields". While passion and determination are attributes that are essential in order to drive a vision to its full potential, if they are left unchecked, they can also turn the journey into a faith-based one driven by dogma.

Reasonably smart people can rationalize anything but entrepreneurs are especially gifted at this.

The first step to driving clarity around your idea is deconstructing your big idea

into a set of clearly articulated assumptions. Traditionally, we have used business plans for this purpose.

Have you ever written a Business Plan? Did you enjoy the process? I have posed these two questions to thousands of makers, entrepreneurs, and innovators around the world and here's what I found: Only 30% of them had ever written a business plan and less than 2% enjoyed the process.

I posed a different question to the investors (and stakeholders) in the room: "Do you read the entire business plan?" Again, less than 2% admitted to doing so—citing a preference for the 1-page executive summary, 10-page slide-deck, or 30-second elevator pitch.

Why then are we still forcing people to spend weeks writing a 40-page document that no one reads and is seldom kept up to date?

The problem with traditional business plans are:

1. They take too long to write

   In order to get your idea green-lit, you are often asked to write a 30-page business plan, create a 5-year financial forecast, and an 18-month product roadmap. This can easily take up weeks, likely months, of your time.

2. They are best guesses at best

   The reason entrepreneurs and innovators choose to forgo the heavyweight business plan isn't because they are lazy. Rather it's because at the earliest stages of any new project, many assumptions are simply unknowable.

At the earliest stages of a product, you don't know what you don't know.

When you're going really fast and under conditions of extreme uncertainty, as required for Continuous Innovation, you can't afford to rely on static plans — you need dynamic models. The Lean Canvas is one such dynamic model.

A Lean Canvas replaces long and boring business plans with a 1-page business model that takes 20 minutes to create and that actually gets read.

In Part 1 of this book you'll learn how to use a Lean Canvas to:

- Chapter 1: Deconstruct Your Idea into a Business Model
- Chapter 2: Stress Test Your Business Model
- Chapter 3: Pitch Your Business Model

Chapter 1. Deconstruct Your Idea into a Business Model

A NOTE FOR EARLY RELEASE READERS

With Early Release ebooks, you get books in their earliest form—the author's raw and unedited content as they write—so you can take advantage of these technologies long before the official release of these titles.

This will be the 1st chapter of the final book.

> *A business model describes how you create, deliver, and capture value (get paid) from customers.*
>
> —Saul Kaplan

When taking on a complex project, like say building a house, you wouldn't start by putting up walls. You'd start with some kind of an architectural plan or blueprint — even if it's just a sketch.

Building and launching an idea is no different.

The Lean Canvas is a rapid idea capture tool that helps you deconstruct an idea into a set of key assumptions. A Lean Canvas can be used to describe a business model, a product release, or even a single feature — making it a highly popular business planning and product management tool used by millions of people around the world.

Here's what one looks like:

PROBLEM
List your top 1-3 problems.

SOLUTION
Outline a possible solution for each problem.

UNIQUE VALUE PROPOSITION
Single, clear, compelling message that states why you are different and worth paying attetion.

UNFAIR ADVANTAGE
Something that cannot easily be bought or copied

CUSTOMER SEGMENTS
List your target and users.

KEY METRICS
List the key numbers that tell you how your

CHANNELS
List your path to customer (inbound or

EXISTING ALTERNATIVES
List how these problems are solved today

HIGH LEVEL CONCEPT
List your X for Y analogy (e.g. YouTube = Flickr for videos)

EARLY ADOPTERS
List the characteristics of your ideal customers

COST STRUCTURE
List your fixed and variable costs

REVENUE STREAMS
List your sources of revenue

Lean Canvas is adapted from The Business Model Canvas and is licensed under the Creative Commons Attribution-Share Alike 3.0 Un-ported License.

LEAN CANVAS

Figure 1-1. Lean Canvas

If you have ever written a business plan or created a slide deck for investors, you'll immediately recognize most of the building blocks on the canvas. We'll cover these blocks in more detail in the next section. A key point I'd like to drive home though is the first continuous innovation mindset:

Mindset #1: Your business model is the product.

I purposely made the solution box less than one-ninth of the entire canvas because, as entrepreneurs, we are most passionate about the solution box and what we are naturally good at.

But as we saw earlier

- your solution, while important, typically isn't what's riskiest,
- investors don't care about your solution, but traction (customer engagement),
- customers too don't care about your solution, but their problems.

Your job then isn't just building the best possible solution, but owning the entire business model and making all the pieces fit.

Recognizing your business model as a product is empowering. Not only does it let you own your business model, but it also allows you to apply well-known techniques from product development to building your company.

The first step to building a complex project is starting with a blueprint or sketch. The next step is tackling the riskiest (versus easiest) parts first.

If you take a step back, you'll see that the Model-Prioritize-Test process is nothing more than product development principles applied to business model development.

A Lean Canvas helps you deconstruct your business model into twelve distinct boxes that are then systematically tested, in order of highest to lowest risk.

Sketching Your First Lean Canvas

In this section, I'll outline the process of sketching a Lean Canvas.

Sketch a canvas in one sitting.

While it’s tempting to iterate endlessly on the whiteboard, your initial canvas should be sketched quickly - in less than 20 minutes. Unlike a business plan, **the goal with a Lean Canvas isn’t to achieve perfection, but to take a snapshot.**

Avoid group think.

If you’re part of a team, avoid creating a Lean Canvas as a group exercise. Instead, have each team member create their own snapshot first. Then get together as a group and reconcile your canvases into a single Lean Canvas. Not only will this encourage more independent perspectives and avoid groupthink, it will also save you time.

Know that it’s okay to leave boxes blank

If you’re unsure about a particular box, it’s okay to leave it blank. We’ll cover these boxes in more detail in subsequent sections.

Follow the 1-page rule

If you can’t describe your idea on a single page, it’s still probably too complex to explain to someone else. Describing your idea on a single page is not about using smaller fonts, but fewer words. It’s a lot easier to describe something in a paragraph than in a single sentence. The space constraints of the 1-page canvas are a great way to distill your business model down to its essence.

Think in the present

Business plans try too hard to predict the future, which is impossible. Instead, ground your canvas on the present. Based on your current stage and what you know right now, what are the next sets of hypotheses you need to test to move your product forward?

Remember there is no right order for sketching a Lean Canvas

Sketching a Lean Canvas is like putting together a jigsaw puzzle. There is no

right place to start or specific order to follow. So start with whatever box you think you understand the best and build out the rest of the canvas from there.

If you still can’t decide, use the sample ordering in Figure 1-2 to get going. We’ll look at each of the boxes in detail.

PROBLEM

List your customers top 3 problems

2

SOLUTION

Outline possible solution for each problem

4

UNIQUE VALUE PROPOSITION

Single, clear, compelling that turns an unaware visitor into an interested prospect

3

UNFAIR ADVANTAGE

Something that can't be easily copied or bought

9

CUSTOMER SEGMENTS

List your target customers and users

1

EXISTING ALTERNATIVES

List how these problems are solved today

KEY METRICS

List key numbers telling how your business is doing today

8

HIGH LEVEL CONCEPT

List your X for Y analogy (e.g. YouTube = Flickr for videos)

CHANNELS

List your path to customers

5

EARLY ADOPTERS

List characteristics of your ideal customer

COST STRUCTURE

List your fixed and variable costs

7

REVENUE STREAMS

List your sources of revenue

6

Figure 1-2. A suggested fill order for the Lean Canvas

Customer Segments

As the Customer Innovation Framework is heavily customer-driven, the customer segment box is a natural starting point.

Distinguish between customers and users.

If you have multiple actors in your business model, aim to first identify your customers.

A customer is someone who pays for your product. A user does not.

Then identify any other actors (users, influencers, etc.) that will interact with this customer.

Examples:

- In a blogging platform, the customer is the blog author while the user is a reader.
- In a search engine, the customer is the advertiser while users are people running searches.

Model multiple perspectives

It helps to view your idea from the perspective of each actor in your business model. Each will likely have different problems, channels to reach them, and value propositions. For example, an advertiser working with a search engine may be struggling with driving awareness to their product, while the people running searches are really looking for answers to specific questions. I recommend keeping these perspectives on the same canvas and using a different color or tag to identify each actor perspective.

Home in on early adopters

You need to simultaneously communicate a big market opportunity while staying razor focused on your early adopters.

Your objective is to define an early adopter, not a mainstream customer.

Your customer segment should represent the total addressable market (TAM) for your idea, while your early adopters represent a specific subset of your TAM that make up your ideal starting customer segment (also called your ideal customer profile).

Problem

Problems, not solutions, create spaces for innovation. The Problem box is where you list the specific problems you are going to tackle with your product.

List the top one to three problems.

While it's tempting to brainstorm and list many possible problems, prioritize your top 1-3 problems that you believe are most pressing for your customers.

List existing alternatives.

Document how you think your early adopters currently address these problems today. Unless you are solving a brand new problem (unlikely), most problems have existing solutions. Many times these solutions may not be from an obvious competitor.

Steve Tackles the Customer Segment/ Problem Quadrant

Before Steve takes on sketching his first Lean Canvas, he digs up the original vision statement he wrote down a year ago:

> *To create an alternate virtual world as vast and rich as the real world and make it universally accessible and useful.*

He is tempted to put down "everybody" under customer segments but remembers Mary's advice against defining "too broad a customer segment".

"When you're trying to market to everyone, you reach no one."

He instead turns his focus to who he considers his ideal initial customer segment and writes down "Software developers". While he envisions that his platform

will eventually allow anyone to create rich immersive AR/VR applications, it would be easiest to start with software developers that already build or want to build these kinds of applications.

Under his overall Customer Segment, he lists various industries that are prime to adopt AR/VR technologies over the next several years.

Next, he turns his attention to listing out the top problems he plans to address. This is what his Customer Segment and Problem boxes look like (see Figure 1-3):

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating augmented/virtual reality (AR/VR) apps is hard. - Requires coding skills. - Takes too long. - Expensive.				Software developers / agencies Marketers Retail Construction Travel Education Healthcare
	KEY METRICS		CHANNELS	
EXISTING ALTERNATIVES Google AR/VR, Apple ARKit, Vuforia, MaxST, Unity.				EARLY ADOPTERS Software developers / agencies who build AR/VR apps for clients.

COST STRUCTURE	REVENUE STREAMS

Figure 1-3. Problem and customer segments

Unique Value Proposition

Dead center in the Lean Canvas is a box for your unique value proposition (UVP). This is one of the most important boxes on the canvas and also the hardest to get right.

The Unique Value Proposition forces you to answer the question: Why is your product different and worth paying attention to?

Before paying for your product with money, customers pay you with attention. Your UVP is hard to get right because you have to distill the essence of your product in a few words that can fit in the headline of your landing page. Additionally, your UVP also needs to be different in order to stand out from the competition, and that difference needs to matter to your customers.

The good news is that you don't have to get this perfect right away. Like everything on the canvas, you start with a best guess and iterate from there.

Here's how to craft a unique value proposition:

Connect to your customer's #1 problem.

The key to crafting an effective UVP is connecting it to the number-one problem you are solving for your customers. If that problem is indeed worth solving for them, you're more than halfway there already.

Target early adopters.

Too many marketers try to target the "middle" of their customer segments, in the hopes of reaching mainstream customers, and in the process they water down their message. Your product is not ready for mainstream customers yet. Your sole job should be to find and target early adopters, which requires bold, clear, and specific messaging.

Focus on outcomes.

You've probably heard about the importance of highlighting benefits over

features. But benefits still require your customers to translate them to their worldview. A good UVP gets inside the head of your customers and focuses on the benefits your customers derive after using your product — desired outcomes.

So, for instance, if you are creating a résumé-building service:

- A feature might be “professionally designed templates.”
- The benefit would be an “eye-catching résumé that stands out.”
- And the finished story benefit would be “landing your dream job.”

Keep it short.

Most advertising platforms limit the number of characters on the primary headline field to 120 characters. Pick your words carefully and avoid empty fillers.

Answer: what, who, and why.

A good UVP needs to clearly answer the first two questions — what’s it for and who’s it for. The “why” is often hard to fit in the same statement. That’s what a sub-headline is often used for.

Here is an example:

> Product: Lean Canvas
>
> Headline: Communicate Your Idea Clearly and Concisely to Key Stakeholders.
>
> Sub-headline: Lean Canvas replaces long and boring business plans with a 1-page business model that takes 20 minutes to create and gets read.

Create a high-concept pitch.

Another useful exercise when crafting a UVP is creating a high-concept pitch. High-concept pitches are used heavily by Hollywood producers to distill the

general plot of a movie to a memorable sound bite. The high-concept pitch was also popularized as an effective pitching tool by Venture Hacks in its ebook, *Pitching Hacks*[1].

Examples:

- YouTube: “Flickr for video”
- Aliens (movie): “Jaws in space”
- Dogster: “Friendster for dogs”

The high-concept pitch should not be confused with a UVP and is not intended to be used on your landing page. There is a danger that the concepts the pitch is based on might be unfamiliar to your audience. For this reason, the high-concept pitch is more effective when used to quickly get your idea across and make it easy to spread, such as after a customer interview. We’ll cover this specific use of the high-concept pitch in Chapter 7.

Steve crafts his UVP

Given that all the existing alternatives require technical know-how and coding knowledge, Steve decides to use “ease-of-use” as the “difference that would matter” for his UVP and “no-code” as the key words to position around (see Figure 1-4).

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating augmented/virtual reality (AR/VR) apps is hard. - Requires coding skills. - Takes too long. - Expensive.		Create Rich Immersive AR/VR Experiences - No Coding Required.		Software developers / agencies Marketers Retail Construction Travel Education Healthcare
	KEY METRICS		CHANNELS	
EXISTING ALTERNATIVES Google AR/VR, Apple ARKit, Vuforia, MaxST, Unity.		HIGH-LEVEL CONCEPT No-code VR apps.		EARLY ADOPTERS Software developers / agencies who build AR/VR apps for clients.

COST STRUCTURE	REVENUE STREAMS

Figure 1-4. UVP

Solution

You are now ready to tackle your solution.

Know that it is fairly common for your customer problems to get reprioritized or completely replaced with new ones after just a few customer conversations. For this reason, I recommend not getting carried away with fully defining your solution just yet. Rather, simply sketch out the simplest thing you could possibly build to address each problem listed on your Lean Canvas.

Bind a solution to your problem as late as possible.

Steve defines a Solution

Based on his list of problems, Steve creates a short-list of top features that address each problem (see Figure 1-5).

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating augmented/virtual reality (AR/VR) apps is hard. - Requires coding skills. - Takes too long. - Expensive.	- Scan a physical space or object with your phone to create a 3D model. - Quickly customize your 3D model. - Deploy your app with a single click.	Create Rich Immersive AR/VR Experiences - No Coding Required.		Software developers / agencies Marketers Retail Construction Travel Education Healthcare
	KEY METRICS		CHANNELS	
EXISTING ALTERNATIVES Google AR/VR, Apple ARKit, Vuforia, MaxST, Unity.		HIGH-LEVEL CONCEPT No-code VR apps.		EARLY ADOPTERS Software developers / agencies who build AR/VR apps for clients.

COST STRUCTURE	REVENUE STREAMS

Figure 1-5. Solution

Channels

If a product is launched in a forest, does it make a sound? Failing to build a significant path to customers is among the top reasons why startups fail.

The initial goal of a startup is to learn, not to scale. So, at first it's OK to rely on any channels that get you in front of potential customers.

The good news is that following a "customer discovery /interview" process forces you to build a path to "enough" customers early. However, if your business model relies on acquiring large numbers of customers to work, that path may not scale beyond the initial stages, and it's quite possible you'll get stuck later.

For this reason, it's equally important to think about your scalable channels from day one so that you may start building and testing them early.

While there are a plethora of channel options available, some channels may be outright inapplicable to your startup, while others may be more viable during later stages of your startup.

Steve outlines some possible paths to customers

Since Steve plans on targeting software developers and agencies as early adopters, he plans to start with conferences and trade shows as starting channels and possibly scaling later using advertising (see Figure 1-6).

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating augmented/virtual reality (AR/VR) apps is hard. - Requires coding skills. - Takes too long. - Expensive.	- Scan a physical space or object with your phone to create a 3D model. - Quickly customize your 3D model. - Deploy your app with a single click.	Create Rich Immersive AR/VR Experiences - No Coding Required.		Software developers / agencies Marketers Retail Construction Travel Education Healthcare
EXISTING ALTERNATIVES Google AR/VR, Apple ARKit, Vuforia, MaxST, Unity.	KEY METRICS	HIGH-LEVEL CONCEPT No-code VR apps.	CHANNELS Warm Referrals Direct Sales Conferences Tradeshows Ads	EARLY ADOPTERS Software developers / agencies who build AR/VR apps for clients.

COST STRUCTURE	REVENUE STREAMS

Figure 1-6. Channels

Revenue Streams and Cost Structure

The bottom two boxes, labeled “Revenue Streams” and “Cost Structure,” are used to model the viability of the business. Rather than thinking in terms of three- or five-year forecasts, here we take a more grounds-up approach.

First, model the runway you will need to define, build, and launch your MVP. Then, revise after you get there.

Revenue Streams

A lot of startups choose to defer the “pricing question” because they don’t think their product is ready. Something I hear a lot is that an MVP is, by definition, embarrassingly minimal. How can you possibly charge for it?

First, an MVP is not synonymous with a half-baked or buggy product. Your MVP should address not only the top problems customers have identified as being important to them, but also the problems that are worth solving. By that definition, you should plan to deliver enough value to justify charging.

But there is another line of reasoning that is frequently cited for deferring pricing: to accelerate initial learning. The argument goes that pricing creates unnecessary friction that should be avoided early on.

The mindset most of us have when we’re launching a new product is one of lowering signup friction. We want to make it as easy as possible for the customer to say yes and agree to take a chance on our product, hoping the value we deliver over time will earn us the privilege of their business.

Not only does this approach delay validation of one of the riskier parts of the model (because it’s too easy for a user to say yes), but a lack of strong customer “commitment” can also be detrimental to optimal learning.

Furthermore, you don’t need a lot of users to support learning—just a few good customers.

I believe that if you intend to charge for your product, you should charge from day one.

Here’s why:

Price is part of the product.

Suppose I place two bottles of water in front of you and tell you that one costs 50 cents and the other costs 2 dollars. Despite the fact that you wouldn’t be able to tell them apart in a blind taste test (the products are similar enough), you might be inclined to believe (or at least wonder) whether the more expensive water is of higher quality.

Here, price has the power to change your perception of the product.

Price defines your customers.

More interesting is the fact that the bottled water you pick determines your customer segment. From the existing market for bottled water, we know there is a viable business for bottled water at both price segments. What you charge signals your positioning on which customers you want to attract.

Getting paid is the first form of validation.

Getting a customer to give you money is one of the hardest actions you can ask them to take and is an early form of product validation.

One technique for setting initial pricing is pricing against the list of existing alternatives from the Problem box. These alternatives provide reference price anchors against which your offering will be measured.

(For more specific techniques for pricing Software as a Service SaaS products, including when to use freemium pricing, see “How to Set Pricing for a SaaS Product” in the Appendix.)

Cost structure

First, list the operational costs you will incur while taking your product to market. It’s hard to accurately calculate these too far into the future. Instead, focus on your most immediate short-term milestones three to six months from now:

- What will it cost you to define, build, and launch your MVP?

- What will your ongoing burn rate look like, such as salaries, office rent, etc.?

Steve thinks through his cost structure and revenue streams

While Steve had found a comfortable groove of self-funding his project through consulting revenue, the competitor launch (Virtuso X) was his wake up call to speed things up. Steve sets a goal to get his MVP launched within the next six months and outlines his costs, which is mostly his time.

Steve had never given any serious thought to his pricing model up until now, but decides to heed the advice of “not deferring his pricing model to later”. He decides to anchor his pricing against other software development tools and finds that they vary from free to several hundred dollars a month. He decides to go down the middle and picks the most popular entry level pricing of $50/mo.

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating augmented/virtual reality (AR/VR) apps is hard. - Requires coding skills. - Takes too long. - Expensive.	- Scan a physical space or object with your phone to create a 3D model. - Quickly customize your 3D model. - Deploy your app with a single click.	Create Rich Immersive AR/VR Experiences - No Coding Required.		Software developers / agencies Marketers Retail Construction Travel Education Healthcare
EXISTING ALTERNATIVES Google AR/VR, Apple ARKit, Vuforia, MaxST, Unity.	KEY METRICS	HIGH-LEVEL CONCEPT No-code VR apps.	CHANNELS Warm Referrals Direct Sales Conferences Tradeshows Ads	EARLY ADOPTERS Software developers / agencies who build AR/VR apps for clients.

COST STRUCTURE	REVENUE STREAMS
Hosting costs People costs - 40 hrs * $65/hr = $10k/mo	30-day free trial $50/mo for unlimited apps

Figure 1-7. Cost structure and revenue streams

Key Metrics

What is the one metric that both you and your investors care about? Traction.

Walk into any investors office with the beginnings of a hockey-stick curve and you'll immediately grab their attention. But while traction is the best objective measure of a working business model, it's not enough to pass off any metric that is growing as traction. For instance, plotting the cumulative number of users over time has nowhere to go but up and to the right. A more sophisticated investor will see right through this facade of vanity metrics.

So how do you define and measure traction? Successful businesses are more alike than unalike. They share a common universal goal, irrespective of business model type: To make happy customers.

Making happy customers is NOT the same thing as making customers happy. Making customers happy is easy. Just give them lots of stuff for free. But that doesn't lead to a working business model. Making happy customers, on the other hand, is not just about making customers feel good. It's about making customers achieve results (desired outcomes).

Happy customers get you paid.

The work of making happy customers happens in a customer factory. The customer factory represents everything inside your business: Your marketing, sales, customer service, and product. Throughput in a customer factory is the rate at which you create happy customers. This is synonymous with traction.

Traction is the rate at which a business model captures monetizable value from its users.

At a basic level, a customer factory takes in unaware visitors as input (raw material) and turns them into happy customers (finished product).

This process can be further broken down into 5 macro steps that can be found in all businesses: acquisition, activation, retention, revenue, and referral.

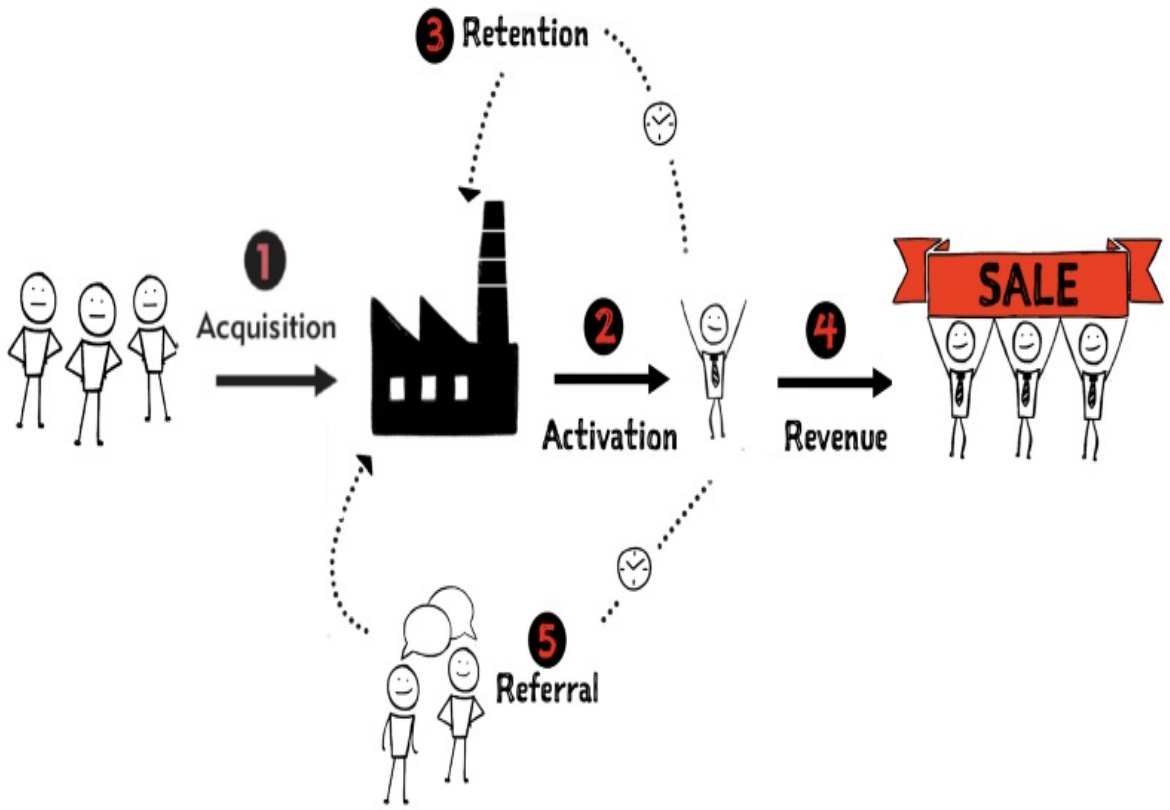


Figure 1-8. The Customer Factory Blueprint

The five macro steps represent the key metrics that can be used to measure any kind of business. Let's walk through each step using a flower shop and a software product as examples.

Step 1. Acquisition

Acquisition describes the point when you turn an unaware visitor into an interested prospect.

In the case of the flower shop, getting someone walking by your window to stop and come in to your shop is an acquisition event.

On a product website, getting someone to do anything other than leave your website (abandon) is a measure of acquisition. I specifically measure successful acquisition as getting my visitors to view my signup page.

Step 2. Activation

Activation describes the point when the interested customer has his first

gratifying user experience.

In the case of the flower shop, if the prospect found the shop in disarray once he comes inside, there would be a disconnect with the promise made at the front of the store. That wouldn't be a gratifying first user experience.

On the product site, once the prospect signs up, you have to make sure you get the customer to a point where he can connect the promise you made on your landing page (your UVP) with your product.

Step 3. Retention

Retention measures "repeated use" and/or engagement with your product.

So, in the case of the flower shop, the action of coming back to the store—and in the case of the product website, the act of logging back in to use the product again—would count toward retention.

As we'll see in Part 3 of the book, this is one of the key metrics to measuring product/market fit.

Step 4. Revenue

Revenue measures the events that get you paid.

These could be buying flowers or buying a subscription for your product. These events may or may not occur on the first visit.

Step 5. Referral

Referral is a more advanced form of a user acquisition channel where your happy customers refer or drive potential prospects into your conversion funnel.

In the case of the flower shop, this could be as simple as telling another friend about the store.

For the software product, this could range from implicit viral or social sharing features (like Share with a friend), to explicit affiliate referral programs or Net Promoter Score.

Steve aligns on his key metrics

Under the Key Metrics box, Steves takes a stab at mapping his customer actions

to each of the key metrics described in the last section.

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating augmented/virtual reality (AR/VR) apps is hard. - Requires coding skills. - Takes too long. - Expensive.	- Scan a physical space or object with your phone to create a 3D model. - Quickly customize your 3D model. - Deploy your app with a single click.	Create Rich Immersive AR/VR Experiences - No Coding Required.		Software developers / agencies Marketers Retail Construction Travel Education Healthcare
EXISTING ALTERNATIVES Google AR/VR, Apple ARKit, Vuforia, MaxST, Unity.	KEY METRICS Number of trials Paid conversion rate LTV / CAC	HIGH-LEVEL CONCEPT No-code VR apps.	CHANNELS Warm Referrals Direct Sales Conferences Tradeshows Ads	EARLY ADOPTERS Software developers / agencies who build AR/VR apps for clients.

COST STRUCTURE	REVENUE STREAMS
Hosting costs People costs - 40 hrs * $65/hr = $10k/mo	30-day free trial $50/mo for unlimited apps

Figure 1-9. Key metrics

Unfair Advantage

This is usually the hardest section in the canvas to fill, which is why I leave it for last. Most founders list things as competitive advantages that really aren't—such as passion, lines of code, or features.

Another frequently cited advantage in business models is the "first-mover" advantage. However, it doesn't take much to see that being first can actually be a disadvantage, as most of the hard work of paving new ground (risk mitigation) falls on your shoulders, only to be potentially picked up later by fast-followers unless you're able to constantly outpace them with a real "unfair advantage." Again, none of these companies were first movers: Ford, Toyota, Google, Microsoft, Apple, or Facebook.

An interesting perspective (via Jason Cohen) to keep in mind is that anything worth copying will be copied, especially once you start to demonstrate a viable business model.

Imagine a scenario where your cofounder steals your source code, sets up shop in Costa Rica, and slashes prices. Do you still have a business? How about if Google or Apple launches a competitive product and drops the price to $0?

You have to be able to build a successful business in spite of that, which led Jason Cohen to offer the following definition of "unfair advantage":

> *A real unfair advantage is something that cannot be easily copied or bought.*
>
> —Jason Cohen, A Smart Bear blog

Here are some examples of real unfair advantages that fit this definition:

- Insider information
- The right "expert" endorsements
- A dream team
- Personal authority
- Network effect

- Platform effect
- Community
- Existing customers
- SEO ranking

A great illustration of the difference between real unfair advantage from a weak one is the difference between organic SEO ranking versus paid keywords for search engine marketing. Keywords can be easily copied and bought by your competitors, while organic ranking has to be earned.

Some unfair advantages can also start out as values that become differentiators over time. For example, Zappos CEO Tony Hsieh believed strongly in creating happiness for his customers and employees. This manifested itself in many company policies that, on the surface, didn't make much business sense, such as allowing customer service representatives to spend as much time as was needed to make a customer happy and offering a 365-day return policy with two-way paid shipping. But these policies served to differentiate the Zappos brand and build a large, passionate, and vocal customer base that played a large role in the company's eventual $ 1.2 billion acquisition by Amazon in 2009.

What do you do if you don't have an unfair advantage on day one?

Most entrepreneurs don't have an unfair advantage at the outset of their idea. Consider Mark Zuckerberg. He wasn't first to build a social network and a number of his competitors already had a huge head start with millions of users and millions of dollars in funding. That didn't prevent him from building the largest social network on the planet.

Start with an unfair advantage story.

While Mark didn't have an unfair advantage day one, he had an unfair advantage story. He knew his unfair advantage needed to come from large network effects. This clarity of focus helped Facebook develop a systematic launch and growth strategy that helped them eventually realize this advantage.

Leave the unfair advantage blank.

If an unfair advantage story isn’t readily apparent, it is always better to leave the unfair advantage box blank rather than stuffing it with a weak unfair advantage.

Embrace obscurity.

The good news with unfair advantages is that you don’t need one from the outset. When you are just starting out, embrace obscurity to build something valuable without calling out competitor attention. And keep searching for a true unfair advantage.

Steve ponders his unfair advantage story

Steve would have normally put down software IP (intellectual property) as his unfair advantage but after reading the last section, he decides instead to rely upon an unfair advantage story built on “platform effect”.

If he can get enough software developers and agencies to build enough killer apps, that would accelerate his vision of creating a massive reusable library of 3D objects — creating a flywheel that would make it easier for everyone to build more apps faster and establish his platform as the platform-of-choice for AR/VR applications.

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating augmented/virtual reality (AR/VR) apps is hard. - Requires coding skills. - Takes too long. - Expensive.	- Scan a physical space or object with your phone to create a 3D model. - Quickly customize your 3D model. - Deploy your app with a single click.	Create Rich Immersive AR/VR Experiences - No Coding Required.	Platform effect	Software developers / agencies Marketers Retail Construction Travel Education Healthcare
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COST STRUCTURE	REVENUE STREAMS
Hosting costs People costs - 40 hrs * $65/hr = $10k/mo	30-day free trial $50/mo for unlimited apps

Figure 1-10. Unfair advantage

Refine Your Lean Canvas

Sketching out a Lean Canvas quickly is a great first step for taking stock of your big idea and visualizing your business model as a set of assumptions.

That said, most entrepreneurs either go too broad or too narrow with their first canvases.

This is a Goldilocks problem.

If you struggled to fit your idea on a single page, chances are you went too broad. When you go too broad, your canvas becomes watered down and undifferentiated.

While you might be aiming to build a mainstream product, you need to start with a specific customer in mind. Even Facebook, with its now 500 million+ users, started with a very specific user in mind: Harvard University students.

At the other extreme, when you go too narrow, the danger is falling into a local maxima trap and not finding the best possible market for your idea.

This is illustrated below as the hill-climbing problem:

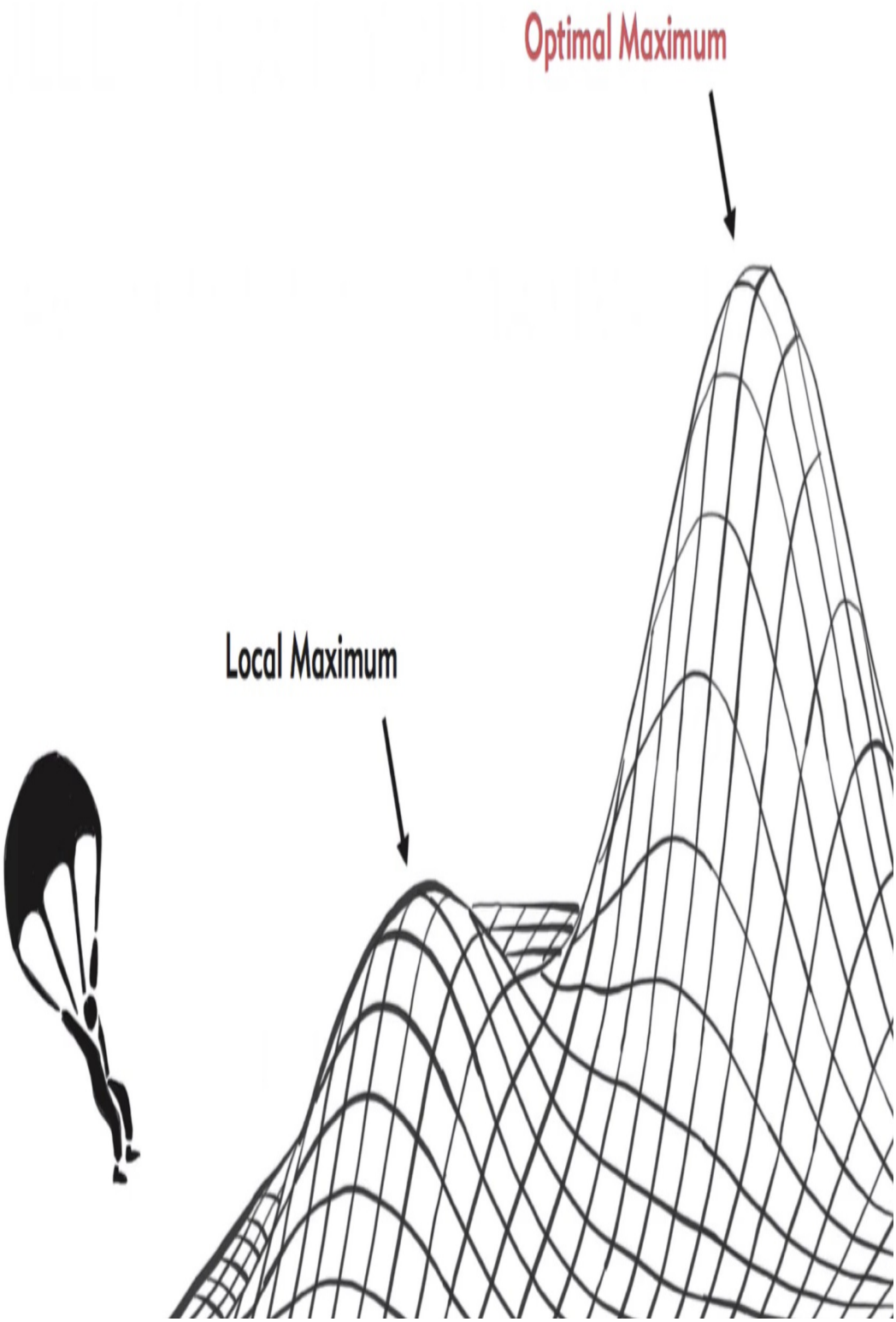

Optimal Maximum
Local Maximum

Figure 1-11. Hill-climbing problem

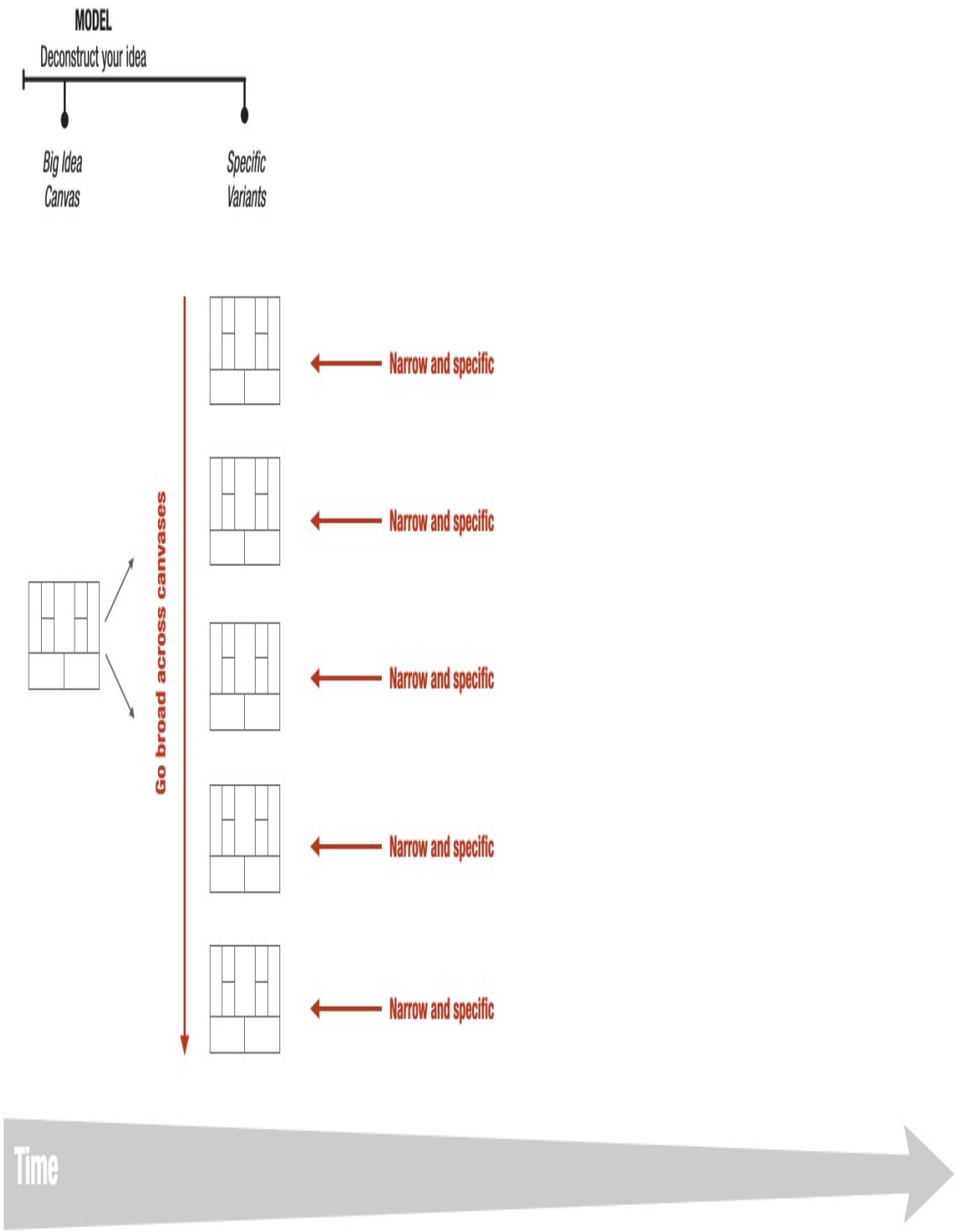
Here's the scenario: Imagine you are blindfolded and given the task of finding the highest point in this landscape.

You might be able to fumble your way to the top of the small hill and declare it the highest point — only to find out, once your blindfold is off, that there is a neighboring mountain right next to you that you missed.

So how do you avoid the Goldilocks problem?

You need a strategy that allows you to simultaneously go broad and narrow at the same time.

The way you do this is by splitting your first Lean Canvas (your "big idea canvas" into additional canvases (Figure 1-4).



Each of your additional canvases needs to be narrow and specific but you can and should go broad across these canvases by sketching out multiple possible variants of the same idea.

For example, a photo-sharing service could be targeted at consumers or businesses. Within businesses, there could be many possible business models to consider. Each of these variants can and should be explored on a different canvas.

While there's no guarantee you'll uncover a mountain with this approach, you can probably appreciate that casting a wider net and staying open to all possibilities early, avoids getting tunnel-visioned around a single implementation of your idea.

After you shortlist your best variants, you then systematically prioritize and test your ideas over time.

Building a business model requires a search versus execution mindset.

How do you know when to split your Lean Canvas?

The reason most Lean Canvases become too broad is that they try to capture too many business model stories on a single canvas. Your objective should be to describe a single business model story per Lean Canvas.

There are 3 basic business model archetypes: Direct, multi-sided, and marketplace. If you find yourself mixing multiple models on one Lean Canvas, split them into separate canvases.

Direct

Direct business models are the most basic and widespread type of business model. They are one-actor models where your users become your customers. Starbucks is an example of a direct business model.

Starbucks - Starbucks

PROBLEM

People have few choices for freshly brewed high quality coffee.

SOLUTION

Bring Italian coffeehouse tradition to the U.S.

UNIQUE VALUE PROPOSITION

A third place between work and home.

UNFAIR ADVANTAGE

Community, convenience, and accessibility.

CUSTOMER SEGMENTS

Coffee drinkers

KEY METRICS

Number of cups served

Number of customers

Average revenue per customer

CHANNELS

Retail stores

Supermarkets

Advertising

EXISTING ALTERNATIVES

Supermarket coffee

Dunkin Donuts / McDonalds

Home brewed coffee

HIGH-LEVEL CONCEPT

McDonalds for coffee

EARLY ADOPTERS

People who brew their coffee at home

COST STRUCTURE

People

Retail store costs

REVENUE STREAMS

Coffee: $3 / cup

Coffee beans: $10 / bag

Lean Canvas is adapted from The Business Model Canvas (BusinessModelGeneration.com) and is licensed under the Creative Commons Attribution-Share Alike 3.0 Un-ported License.

Figure 1-12. Starbucks Lean Canvas

On your Lean Canvas, you should strive to capture your total addressable segment as a single entry in the customer segment box and your ideal starting sub-segment in the early adopter box.

Multisided

In a multisided model, the goal is still to create, deliver, and capture value from users, but that value is monetized through different customers. These are two-actor models made up of users and customers.

Users typically don’t pay for usage of your product with a monetary currency but with a derivative currency. This derivative currency, when aggregated across enough users, represents a derivative asset that your customers pay to acquire. Facebook is an example of a multisided model, with advertisers being the customers and college students being the users.

Facebook - Advertisers + College Students

PROBLEM

Existing online social networks fail to deliver on core promise and are characterized by:

1. Friends as badges versus true friends

2. Low quality of conversations

3. Low user engagement

Advertisers want a highly targeted and active audience. #customer

EXISTING ALTERNATIVES

Friendster, Myspace #user

Banner ads, Google Adwords, Yahoo #customer

SOLUTION

Instead of trying to create a new social network, remove friction from pre-existing social networks such as those on college campuses.

KEY METRICS

$100m valuation in 2 years

#customer traction metric: Impressions, clicks, conversion

#user traction metric: DAU/MAU/Page views

UNIQUE VALUE PROPOSITION

Connect and Share with Your Friends (Not Strangers) #user

Reach a highly segmented audience of active users with a high ROI #customer

HIGH-LEVEL CONCEPT

Friendster for college students #user

UNFAIR ADVANTAGE

High user engagement through network effects translates to more clicks for advertisers #customer

CHANNELS

Viral usage model #user

Seed ivy league schools #user

Auction based platform #customer

Direct sales #customer

CUSTOMER SEGMENTS

College Student #user

Advertisers #customer

EARLY ADOPTERS

Ivy league schools starting with Harvard University #user

Advertisers that want to reach college students #customer

COST STRUCTURE

People: unpaid

Hosting costs: $85/mo

REVENUE STREAMS

Derivative Currency: 300 average monthly page views per #user

Advertising revenue: $1 CPM, $X CPC, $Y CPA #customer

Derivative Currency Exchange Rate: ARPU = $0.30/month

User lifetime value = ARPU * 4 years lifetime = $14.40

Lean Canvas is adapted from The Business Model Canvas (BusinessModelGeneration.com) and is licensed under the Creative Commons Attribution-Share Alike 3.0 Un-ported License.

Figure 1-13. Facebook Lean Canvas

On your Lean Canvas, you should model your idea from the perspective of both your users and your customers.

Marketplace

Marketplace models are a more complex variant of the multisided model that warrant their own category. Like multisided models, marketplaces are multi-actor models made up of two different segments. This time, those two segments are buyers and sellers. Airbnb is an example of a marketplace model.

Airbnb - Airbnb

PROBLEM

Looking for a room to rent when hotels are sold out #buyer

Earn extra cash by renting a room in your house / apt #seller

EXISTING ALTERNATIVES

Hotel rooms #buyer

Couch surfing #buyer

Stay with friend #buyer

Can only rent out entire apt #seller

SOLUTION

Marketplace that connects guests with hosts

KEY METRICS

Guest nights booked

Number of listings #seller

Number of searches #buyer

UNIQUE VALUE PROPOSITION

Earn extra cash #seller

Find a hotel room alternative #buyer

HIGH-LEVEL CONCEPT

Couchsurfing for professionals

UNFAIR ADVANTAGE

CHANNELS

Billboards

Online ads

Word of mouth

CUSTOMER SEGMENTS

Guests #buyer

Hosts #seller

EARLY ADOPTERS

Travelers attending events/conventions #buyer

People with extra rooms they are willing to rent #seller

COST STRUCTURE

Website

Advertising

People costs

REVENUE STREAMS

Booking fee

Lean Canvas is adapted from The Business Model Canvas (BusinessModelGeneration.com) and is licensed under the Creative Commons Attribution-Share Alike 3.0 Un-ported License.

Figure 1-14. Airbnb Lean Canvas

Here too, you should model your idea from both the perspective of the buyer and the seller.

Note: It is possible to find more complex models in practice that layer these bas ic archetypes. The thing to keep in mind is that even these more complex models started with a basic model at the outset.

> **Gall's Law**
>
> A complex system that works is invariably found to have evolved from a simple system that worked.

Strive for simplicity, not complexity. Simple is hard enough.

Steve Splits His Big Idea Canvas into Specific Variants

Steve revisits his Lean Canvas and immediately recognizes that he has too many customer segments on his canvas.

"Do they all belong to the same business model?" he wonders.

After a few minutes of staring at his Lean Canvas and using his newly acquired knowledge on business model archetypes, he starts to recognize distinct business models intertwined on his Lean Canvas.

His original plan was building a general purpose platform for software developers who in turn build vertical VR/AR applications for their clients. But as he stares down the list of possible customer segments for AR/VR apps, it dawns on him that building a general purpose platform is just one way of moving forward.

He could alternatively focus his platform around building apps that serve a single vertical use case like construction or retail. While he's predisposed to building a platform for software developers, he decides to keep an open mind and gets to work splitting his original canvas into separate canvases and comes up with his top three most promising variants:

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating augmented/virtual reality (AR/VR) apps is hard. - Requires coding skills. - Takes too long. - Expensive.	- Scan a physical space with your phone to create a starting model. - Quickly customize your model with prebuilt assets. - Deploy your app with a single click.	Create Rich Immersive AR/VR Experiences - No Coding Required.	Platform effect	Software developers / agencies
EXISTING ALTERNATIVES Google AR/VR, Apple ARKit, Vuforia, MaxST, Unity.	KEY METRICS Number of trials Paid conversion rate LTV / CAC	HIGH-LEVEL CONCEPT No-code VR apps.	CHANNELS Direct Sales Conferences Tradeshows Ads	EARLY ADOPTERS Software developers / agencies who build AR/VR apps for clients.

COST STRUCTURE	REVENUE STREAMS
Hosting costs People costs - 40 hrs * $65/hr = $10k/mo	30-day free trial $50/mo for unlimited apps

Figure 1-15. AR/VR Software Developer Platform Lean Canvas

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating virtual reality (VR) renderings for clients is hard. - Requires technical modeling skills. - Takes too long. - Expensive.	- Scan a physical space with your phone to create a starting model. - Quickly customize your model with prebuilt assets. - Deploy your app with a single click.	Create Rich Immersive AR/VR Models - No Coding Required.		Architects #customer Homeowner #user
EXISTING ALTERNATIVES BIM and CAD tools: SketchUp, Autodesk.	KEY METRICS Number of trials Paid conversion rate LTV / CAC	HIGH-LEVEL CONCEPT No-code AR/VR models.	CHANNELS Direct Sales Conferences Tradeshows Ads	EARLY ADOPTERS Architects who build 3D model renderings for their clients.

COST STRUCTURE	REVENUE STREAMS
Hosting costs People costs - 40 hrs * $65/hr = $10k/mo	30-day free trial $100/mo

Figure 1-16. AR/VR Construction Lean Canvas

PROBLEM	SOLUTION	UNIQUE VALUE PROPOSITION	UNFAIR ADVANTAGE	CUSTOMER SEGMENTS
Creating 3D models for an eccomerce store requires techical skills and is expensive. #customer #Consumers shopping for furnture online struggle with visualizing and measuring if the furniture will fit their space.	- Scan a physical object your phone to create a starting model. - Quickly customize your model with prebuilt assets. - Embed your object on your ecommerce store.	Quickly embed 3D models to enhance online shopping experience.		Retailer #customer Consumers #user
	KEY METRICS Number of trials Paid conversion rate LTV / CAC		CHANNELS Direct Sales Conferences Tradeshows Ads	
EXISTING ALTERNATIVES Build in-house, hire a software development agency, Houzz,		HIGH-LEVEL CONCEPT Ikea Place for your furniture.		EARLY ADOPTERS Furniture retailers.

COST STRUCTURE	REVENUE STREAMS
Hosting costs People costs - 40 hrs * $65/hr = $10k/mo	$1/rendered object/year

Figure 1-17. AR/VR Retail Lean Canvas

He can immediately appreciate that these variants have a lot more clarity and specificity than his original big idea canvas.

Now It's Your Turn

Documenting your Plan A is a prerequisite for moving on. As I stated at the start of the chapter, too many founders carry their hypotheses in their heads alone, which makes it hard to systematically build and test a business. You have to draw a line in the sand.

Here's how you can create your first Lean Canvas:

1. Go to http://leanstack.com and create a free account.
2. Set a timer for 20 minutes and take a quick snapshot of your big idea on the Lean Canvas tool.
3. Next, refine your idea into one or more specific variants.

---

1 \Pitching Hacks (link)

Chapter 2. Stress Test Your Business Model

A NOTE FOR EARLY RELEASE READERS

With Early Release ebooks, you get books in their earliest form—the author's raw and unedited content as they write—so you can take advantage of these technologies long before the official release of these titles.

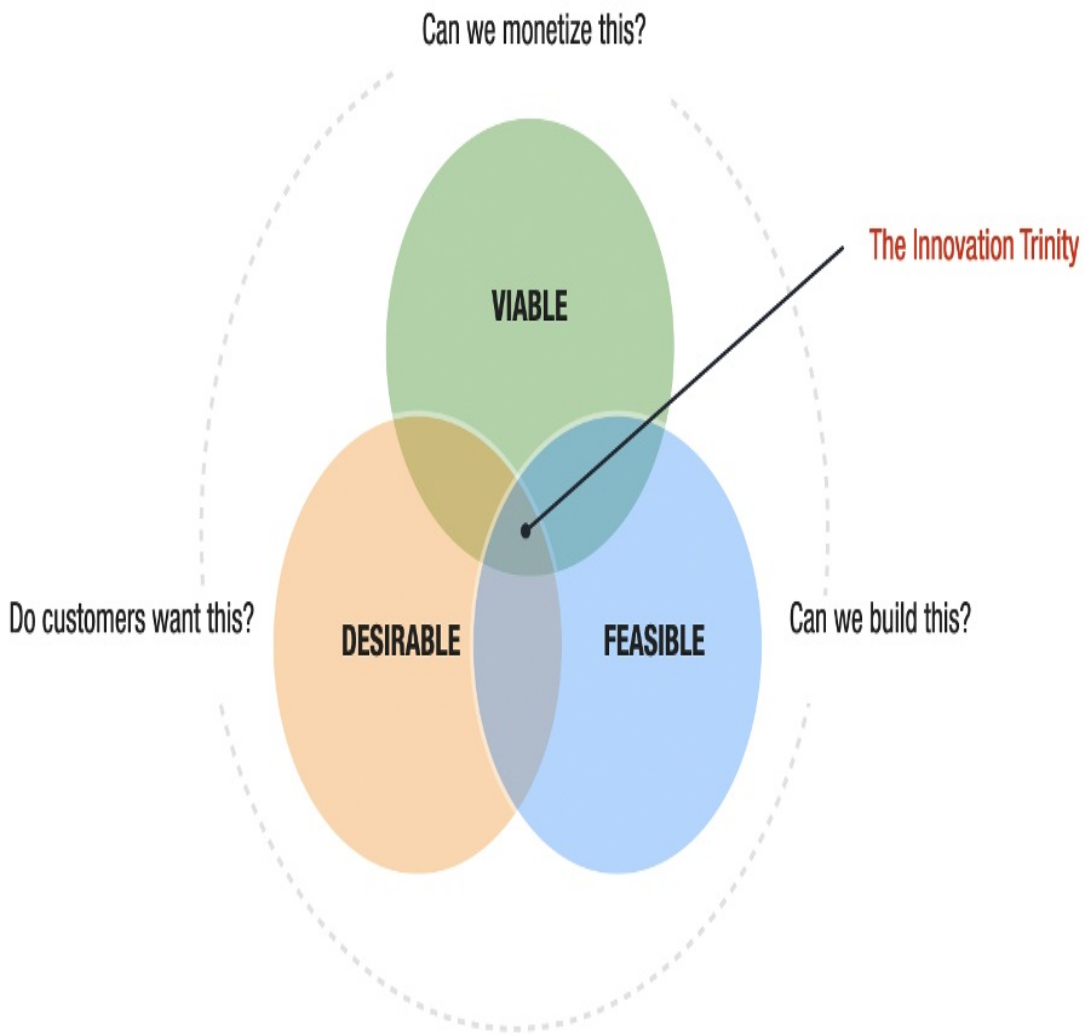
This will be the 2nd chapter of the final book.

It's tempting to "rush out of the building" after your first Lean Canvas sketch and immediately start testing out your business model on customers. It's even possible to quickly find clusters of problems, pitch an offer, build a quick MVP, and charge your customers from day one -- which sounds exactly like what we should do.

So what's wrong with this approach?

The danger is getting stuck with a sub-optimal business model six or nine months down the line that doesn't match your ambition or one that you can't scale.

For an idea to be successful, it needs to constantly balance three types of risks: customer risks, market risks, and technical risks. These risks can be more easily visualized through the lenses of desirability, viability, and feasibility as popularized by IDEO.



Before engaging in several weeks and months of customer validation, it's prudent to spend a few more hours (inside the building) stress testing your business model and tightening up any obvious cracks or flaws in your thinking.

You do this by subjecting your models to three tests that check for:

1. Desirability - Do customers want this?
2. Viability - Can you monetize this?
3. Feasibility - Can you build this?

Stress Testing Desirability

The key question to answer here is: Do customers want this? Our goal is to build *better* products, which begs the question: What does *better* even mean?

Defining *better* starts with recognizing that *customers don't care about solutions, but achieving desired outcomes*.

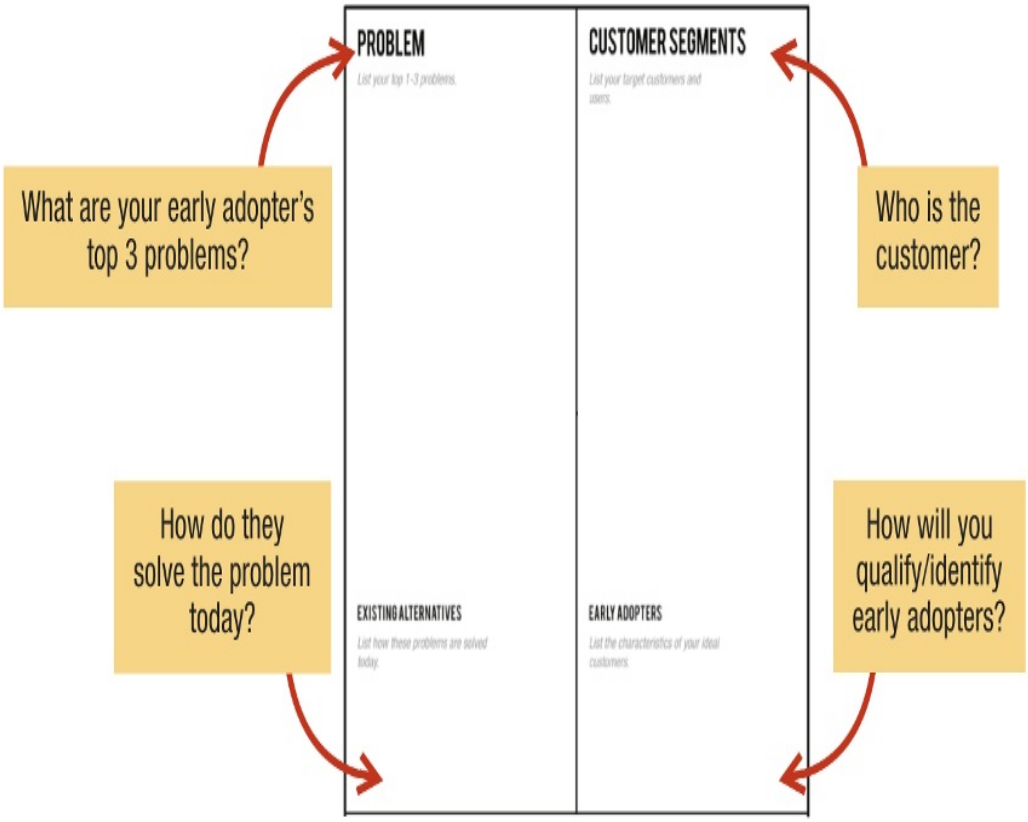
The best way then to get a customer's attention is not by pitching your solution at them, but first getting razor focused on **who you are targeting** and then **understanding the obstacles (problems) that stand in the way of them achieving their desired outcomes.**.

On the Lean Canvas, this is captured on the **Customer segment and Problems** boxes. If you get these assumptions wrong, it's easy to see how everything else in your business model falls apart.

- You end up describing a solution that no one wants (not desirable).
- Even if you manage to build this solution (feasible), no one buys it (not viable).
- Your channels and unfair advantages don't offer any respite.

CI Mindset #2: Love the Problem, Not Your Solution.

This is why desirability is one of the first stress tests to subject upon your business model. The customer/problem quadrant (Figure 2-2) make up the outer pillars that hold up your business model, and so ensuring these assumptions are solid is key to building a strong desirability story.



The problem with problems

While the concept of starting with problems versus solutions is simple, it isn't easy. When pressed to think in terms of problems, entrepreneurs often unconsciously invent, or even fake, problems in order to justify the solution they already have in their mind. Instead of asking: "What problem do my customers have?", they ask: "What problem could my solution solve?".

When you've already decided to build a hammer, everything starts looking like a nail.

This is our Innovator's Bias in action. And don't worry, it happens to everybody. I'm going to show you the perfect antidote to the Innovator's Bias — something I call the **Innovator's Gift**.

The Innovator’s Gift

The basic premise of the Innovator’s Gift is simple: New problems come from old solutions.

When searching for an innovative idea, while you need an innovative solution, you don’t want an innovative problem — one that no one understands or cares about. The secret is framing problems in terms of the obstacles **with their old solutions** that prevent customers from achieving their desired outcomes .

The Innovator’s Gift is realizing that there is no such thing as a perfect solution. Problems and solutions are two sides of the same coin. And new problems worth solving come from old solutions.

Sound too simple? Let’s consider a familiar example.

Place yourself somewhere on the product timeline above and think back to what caused you to switch from that solution to the next one.

It’s tempting to say it was for *better* sound quality, but while sound quality went up when we moved from cassettes to CDs, it went down from there. There was something else at play.

The reason we switched from cassettes to CDs wasn’t because of better sound quality but the ability to instantly play a song. Cassette tapes were just fine until CDs came along and broke the cassette tape by making a problem that was always there: “rewinding and forwarding to find your favorite song” — this was a problem worth solving.

The reason we then switched from CDs to MP3 players wasn’t better sound quality either, but the ability to buy just the songs we wanted — and not the entire CD.

The reason we switched from MP3 players to the cloud was because “a thousand songs in my pocket” was no longer enough. We now wanted access to 40 million songs in the cloud that we don’t even own, but rent on-demand.

Can you see the common thread here?

Each of these are massive switching stories and sure there are new solutions and technologies at play. However, what caused the switch wasn’t solving new problems, but solving old problems (and pet peeves) that were always there. We tolerate and even work around these problems for a while, until one day we encounter a *switching triggering event* that breaks our current solution, and *causes a switch* to a new solution.

This is the story of all successful innovation.

1. New problems worth solving come from old solutions. There is always an old way.
2. Innovation is fundamentally about causing a switch from the old way to your new way.
3. The best way to cause this switch is by anchoring new solutions against problems caused by old solutions i.e. breaking the old way.

Here’s how to apply the Innovator’s Gift:

1. What old way are you aiming to replace?

Many startup founders manage to convince themselves that they have no competition. But this is often because they aren't looking broadly enough, and instead defining their competition solely in terms of their solution or product category.

Your true competition transcends categories.

If you are building cutting-edge collaboration software, for instance, your immediate competitor might not be the shiny startup down the street, but email.

Email is free and ubiquitous and the de facto collaboration platform. Sure, you may think you have superior and better technology, but your job is getting people to stop using email and start using your product instead.

That is your true competition.

Email and spreadsheets have killed more startups than other startups.

That is why you won't find a "Competition" box on the Lean Canvas, but the more general "Existing Alternatives" box instead.

Every successful product ever built had competition in the form of an existing alternative.

Make sure you're in full alignment with this fundamental tenet because it's key towards applying the Innovator's Gift.

2. Is your product *better enough* to cause a switch?

Another key area to address is whether your product is better than the existing alternative and more specifically, how much better?

If your product is only incrementally better, the incumbent always wins.

They win because they have an already established relationship with customers. In other words, it's easier for customers to trust an existing alternative, even with some problems, than your new untested risky solution.

Better the devil you know than the devil you don't.

In order to cause a switch your unique value proposition needs to be significantly better. Think 3x-10x better.

Additionally, too many entrepreneurs position their unique value proposition (UVP) around being functionally better. But it's often far more effective to position your UVP around being emotionally better.

"Functionally better" is where needs live.

"Emotionally better" is where wants live.

Being functionally better aims to address unmet needs. Positioning your product this way can be enough to cause a switch if these unmet needs are well understood by your customers as obstacles standing in the way of achieving their desired outcomes (what they want). If that isn't the case, it's far more powerful to switch your positioning to address their desired outcomes.

For example,

- "We help you create a business plan faster" is positioning around being functionally better.
- "We help you create a business plan that gets read" is positioning around being emotionally better.

A great way to direct your thinking towards being emotionally better is focusing on the bigger context. Every product lives in two contexts: the solution context and the bigger context.

The solution context is where your product's features and benefits live. The bigger context is where your customer's desired outcomes live.

> *Don't focus on building a better X.*
>
> *Focus on building a better user of X.*
>
> —Kathy Sierra

3. Expose the elephant in the room

During product pitches, most entrepreneurs never bring up their competition. This is a mistake because your customers are sophisticated and they will shop around. Would you prefer that they compare you to the competition without you in the room when you'll have no say in the comparison?

Your true competition is the elephant in the room, and it's your job to expose it

and diffuse it.

A good product pitch acknowledges the popular existing alternatives (your true competition), then goes on to demonstrate how it is better by anchoring against problems with these existing alternatives — thereby breaking the old way for customers.

Steve Realizes He Has a Hammer Problem

As Steve takes another scan of his Lean Canvas, it dawns on him that his entire canvas is centered around his solution-specific category: AR/VR.

For example, in his Software Developers Lean Canvas:

- his early adopters are software developers who build AR/VR apps for their clients,
- the existing alternatives are other AR/VR platforms,
- his UVP is built on a functional benefit of making it easier and faster for software developers to build AR/VR apps.

But is AR/VR really want his customers want? He now sees that build an AR/VR app is a functional outcome that might be enough to cause a switch if it building these apps were in high demand. But, that isn't the case, at least yet.

AR/VR technology is a promising, yet emerging and largely unproven, technology. An AR/VR app isn't what end-customers really want. They want what comes after the app like

- selling more billable project work for software developers,
- selling more clothes online for retailers, and
- helping clients visualize their dream home for architects.

Steve had been stuck in the solution-context all this time and realizes that he need to instead focus on the bigger context of end-customer desired outcomes.

Run the Innovator's Gift Test on Your Idea

It’s time now to take another pass on your Customer/Problem quadrant with the Innovator’s Gift mental model.

This time around I want you to go around these boxes in a very specific order starting with Customer Segments, then reviewing your Early Adopters, then considering Existing Alternatives, and finally your Problems. It helps to imagine putting together pieces in a jigsaw puzzle.

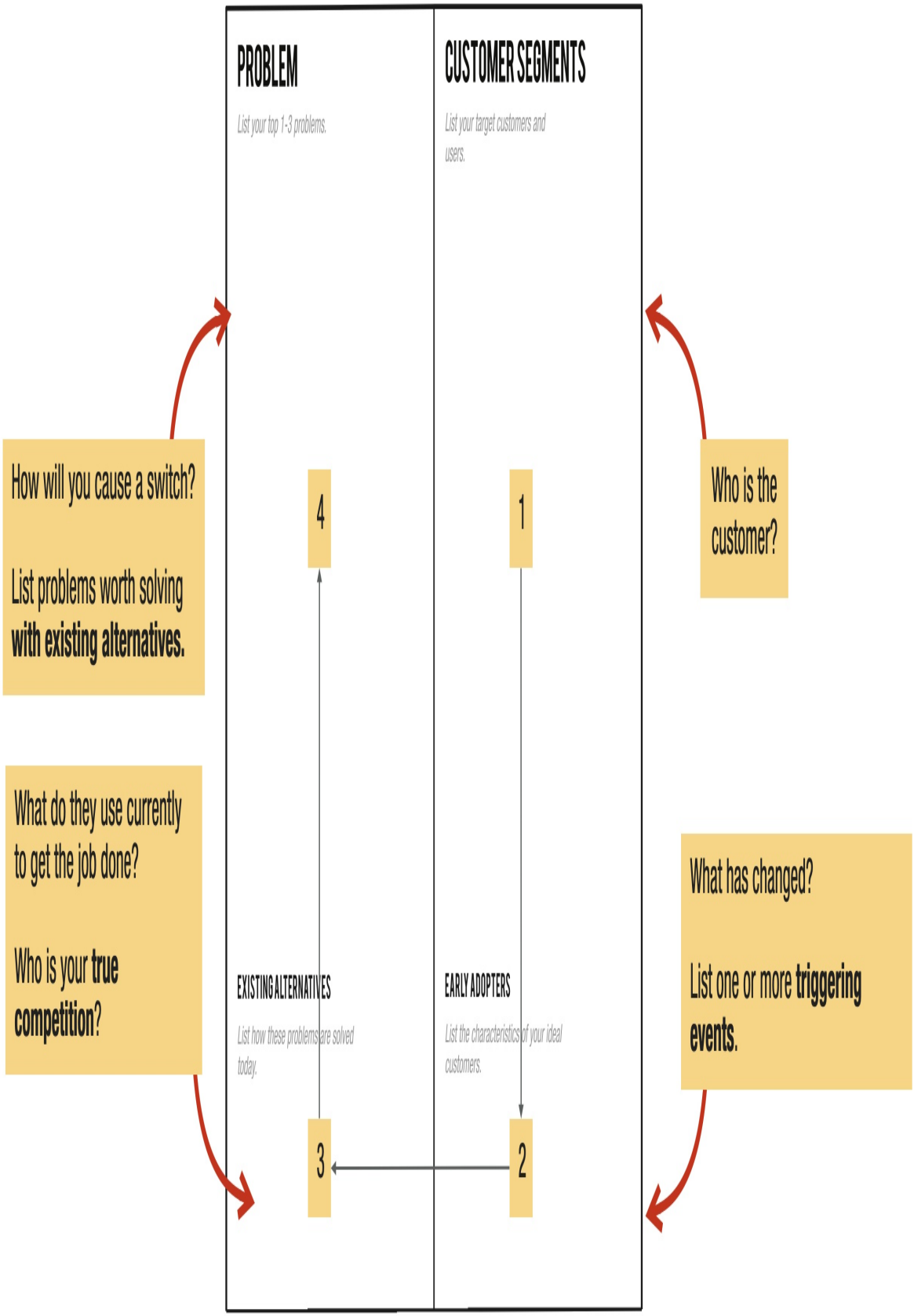

PROBLEM
List your top 1-3 problems.
CUSTOMER SEGMENTS
List your target customers and users.
How will you cause a switch?
List problems worth solving with existing alternatives.
4
1
Who is the customer?
What do they use currently to get the job done?
Who is your true competition?
What has changed?
List one or more triggering events.
EXISTING ALTERNATIVES
List how these problems are solved today.
EARLY ADOPTERS
List the characteristics of your ideal customers.
3
2

Figure 2-1. The Innovator's Gift Test

Like a prosecutor in court, you need to be able to make the case for the problems listed in this quadrant without relying on your solution.

How do you do that?

By describing problems with respect to your customer's existing alternatives instead. In other words, don't focus on problems you can solve with your solution. Rather focus on problems your customers encounter when using existing alternatives.

Anchoring your unique value proposition, pricing, and solution against these problems is the secret to crafting an effective UVP that grabs attention and causes a switch — because it's **specific, familiar, and compelling**.

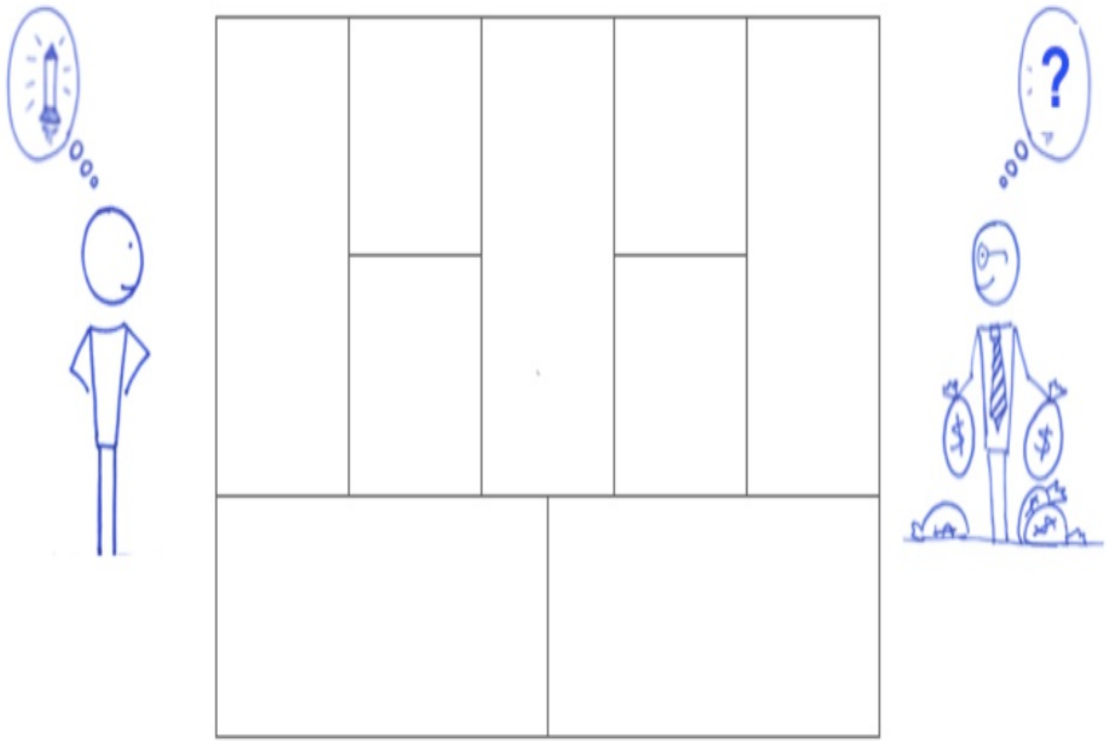
This subtle change in perspective is often the difference between *inventing* problems to justify your solution, and *uncovering* real problems worth solving.

And remember:

Make your case for problems without relying on your solution, but rather relying on problems with old solutions.

Stress Testing Viability

While a Lean Canvas is a great way to deconstruct your early stage idea into a more coherent business model story, your stakeholders (investors or budget gatekeepers) probably still struggle to see what you see. A business model story (even with early customer validation) just doesn't cut it for them.



A Lean Canvas is not enough

Why is that? Because investors are in the business of getting a return on their investment and they need to see the numbers side of the business model story. Before you discount this as just an investor-only perspective, you too need to learn how to see your idea as through the lens of an investor.

Why? Because you are Investor #1 in your idea. While you may not be investing with lots of money, you invest with your time -- which is more valuable than money. Money can go up and down, but time moves only in one direction -- down. All ideas, especially good ones, consume years of your life. Do you really want to spend the next three years of your life on an idea with a “Let’s see what happens” approach?

For this reason, you need to be even harsher on your idea than a professional investor. Ultimately, both you and your investors want the same thing: **Help turn the idea into a "*big enough* business” to make it worthwhile.**

So how do you determine this?

Up for some Excel magic?

In order to get more clarity on your business model outcome story, investors often push you towards building a financial forecast spreadsheet. Anyone who's been to business school knows that the best spreadsheets get funded. So you start off with a spreadsheet template and spend countless hours punching in numbers with the goal of creating an ambitious, yet just-believable model.

But like a business plan, the financial forecast takes too long to create and you are left with a big spreadsheet that **masks your riskiest assumptions in layers of compounding lies**.

If you've ever created one of these, you know it's very easy to get lost in the numbers. But more importantly, you end up back in the old world: **executing a plan**.

Your investors start measuring the performance of your startup against your forecasts. They care about growth, but you care about product and learning. This creates a dichotomy of progress stories. The story we tell our stakeholders is not the same as the story we tell ourselves. They both start out the same but diverge significantly over time because each uses a different definition of progress.

You can't learn and move fast if you're still stuck executing and defending a plan -- especially when your input assumptions start getting challenged over time, which they will. So there is a problem: Unless you can completely break away from the waterfall business planning process, you'll be hard pressed to effectively practice continuous innovation.

The key do doing this is aligning yourself *and your investors* around the one metric that both of you care about: Traction.

Mindset #3: Traction is the goal.

What is Traction?

While traction is a popular concept, it's poorly understood and largely misused to mean any convenient metric that happens to be going up and to the right. Here's a stricter definition:

Traction is the rate at which a business model captures monetizable value from its customers.

Don’t create a financial forecast. Start with a Fermi Estimate instead.

To solve this drowning-in-numbers/Excel-magic problem, I devised a simple **back-of-the-envelope business model test** that takes less than 5 minutes to do. It’s built on a Fermi estimate, which is used widely in physics for doing quick order-of-magnitude calculations.

The mistake we make with financial projections at the business model planning phase is that we spend a disproportionate amount of time focusing on the output of our models when it’s the *inputs* that really matter.

A Fermi estimate, on the other hand, takes a bottom-up approach where you start with a set of inputs, roughly estimate them to your best ability, and then test the viability of your idea using these input assumptions. As long as your input assumptions aren’t off by an order of magnitude (power of 10), the resulting estimate will be accurate enough to make a go or no-go decision.

The first input to nail down is your **minimum success criteria**.

If you don’t know where you are going, any road will take you there.

—Adapted from Alice in Wonderland, Lewis Carroll

The quote above highlights the importance of starting with a rough ballpark destination or goal for your idea. We need this ballpark number to justify the business model story—first to ourselves and then to our internal and external stakeholders (team, investors, budget gatekeepers, etc.).

Your minimum success criteria isn’t the same thing as the maximum upside potential which is a number that is very hard (if not impossible) to estimate at the early stages of an idea.

If, for instance, you had asked the Airbnb, Google, or Facebook founders when they were first starting out whether they thought they would go on to build billion dollar companies, they would probably have laughed at you.

> *We built it and we didn't expect it to be a company, we were just building this because we thought it was awesome.*
>
> —Mark Zuckerberg

It's important to define your minimum success criteria independently from your idea. Most people start with an idea and then assess how big it could become? This is backwards. Why would you ever want to work on an idea that couldn't hit your minimum success criteria?

Start by setting your minimum success criteria constraint instead. Let's cover how next.

1. Set a Minimum Success Criteria Constraint

So how do we define the minimum success criteria?

Your minimum success criteria (MSC) is the smallest outcome that would deem your project a success 3 years from now.

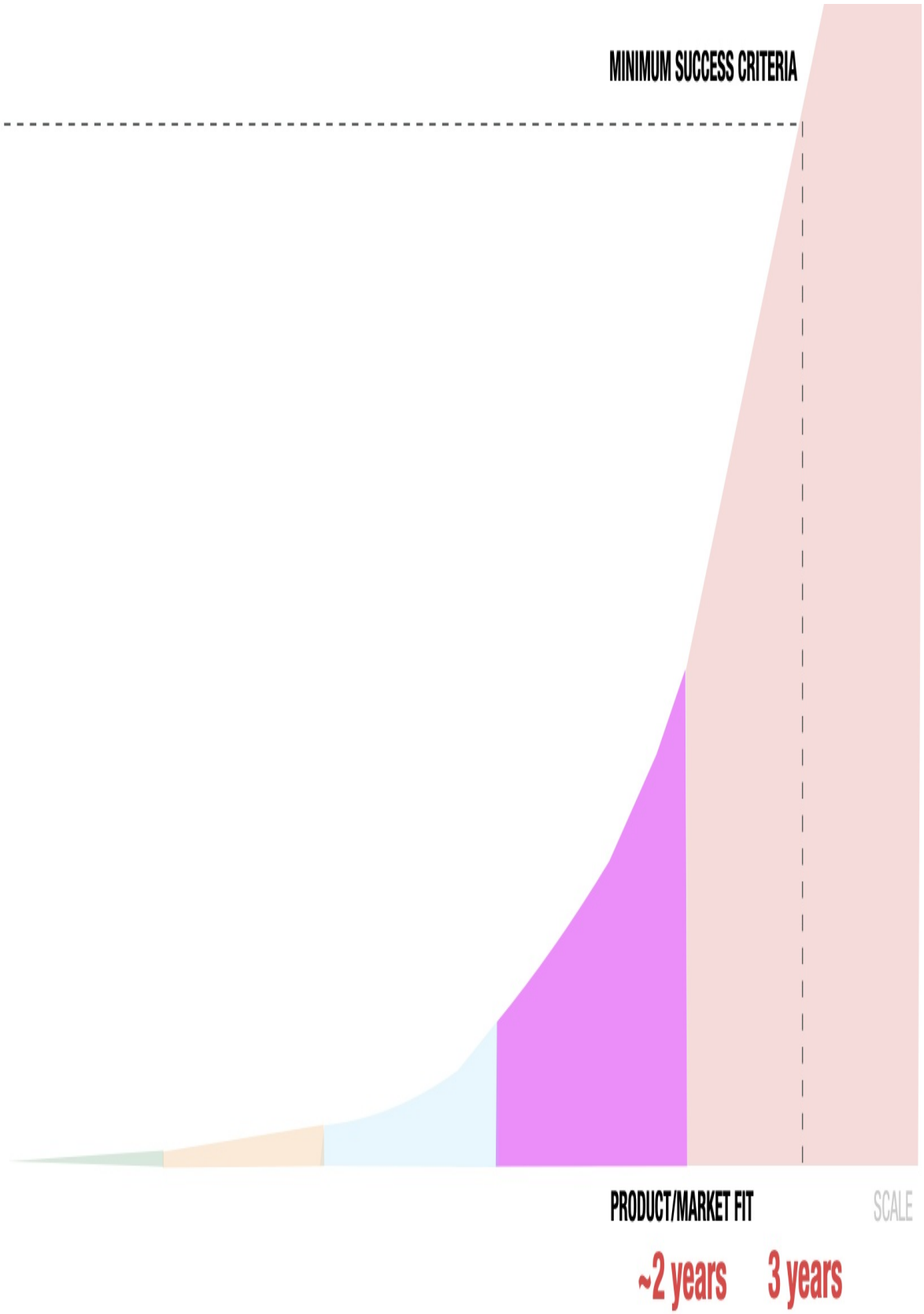

MINIMUM SUCCESS CRITERIA
PRODUCT/MARKET FIT
SCALE
~2 years
3 years

Figure 2-2. Minimum Success Criteria

Why 3 years?

3 years is easier to visualize than 5 years

While most forecasts ask for 5-7 year plans, it's near impossible to see that far. With a little effort, every one can visualize the first 3 years.

3 years is usually enough time to get to Product/Market Fit

Most products average about 2 years to achieve product/market fit. That is when your business model is largely de-risked and the focus shifts to growth. That is also when you can see further and make 5-7 year financial forecasts.

How do you measure business model outcomes?

Frame your outcome in terms of yearly revenue

I recommend using a revenue goal versus profit or company valuation. Yearly revenue has fewer inputs which keeps the model simple.

Profit and valuation are derivatives of revenue. So as long as you buffer accordingly, you should be okay.

Example: If you are building a SaaS business, most are expected to run at >80% profit margins by product/market fit. If you assume you'll be no different, then adjust your revenue goal with that assumption in mind.

What if I'm building an impact-driven business?

All businesses, even impact-driven ones need revenue to deliver on their value proposition.

Revenue is like oxygen. We don't live for oxygen, but we need oxygen to live.

The difference between a for-profit business and a non-profit, is that the latter reinvests excess revenue (profit) into delivering more impact. If you want to deliver more impact, you need to generate more revenue.

How do you determine the smallest outcome, or your minimum success criteria?

Your expected minimum outcome is often already set for you

If you are a startup, ask yourself if you'll be raising money from investors. If the answer is yes, study how your target investors value companies at product/market fit and that will give you some specific benchmarks to use in your modeling.

If you don't intend to raise money from investors and bootstrap all the way, ask yourself

- How big is the company you'd like to build?
- How many employees will your company have?

The answers to these questions can help ballpark your revenue target.

> *"You need to build a life plan, before your business plan."*
>
> —Bo Burlingham

If you work in a big company, ask your stakeholders now (versus three years from now) how they define success. If they aren't sure, benchmark your minimum success criteria against the top ten products your company has launched. If you can promise to beat their three-year revenue trajectory by 2-3X, you should be able to get your stakeholders onboard.

Don't chase three-digit precision

The purpose of this exercise is ballparking a rough 3-year annual revenue estimate. It's helpful to start estimating your desired revenue outcome using powers of 10.

- $100K/yr revenue: Roughly enough to quit your day-job
- $1M/yr revenue: A small 2-3 person company
- $10M/yr revenue: A VC back-able business

Adjust accordingly from here.

Setting a minimum success criteria is critical to testing whether your idea is worth pursuing. I wouldn't advise continuing until you have at least some ballpark number in mind.

There is no right or wrong number for your minimum success criteria but you should have a number.

Steve Sets His Minimum Success Criteria

Every major publication that covers AR/VR technologies predicts that this technology is going to change entire industries and the market for AR/VR is valued in the billions of dollars. There are already major players, like Microsoft, Apple, Google, Facebook, and Amazon deploying this technology.

As Steve has his sights set on building a key enabler platform for this technology, he recognizes that while he can get started on his own, he will eventually require venture capital in order to scale his vision and establish his platform effect unfair advantage.

Steve decides to set his minimum success criteria ballpark to $10M ARR (annual recurring revenue) in 3 years.

With your minimum success criteria set, you then test your business model's ability to hit your minimum success criteria.

2. Test Your Business Model Against Your Minimum Success Criteria Constraint

With your MSC set, you then test the viability of your idea against your goal. You test this by determining how many customers you would need to acquire in order to hit and sustain your MSC goal three years from now.

Here's how we execute this test.

1. Determine how many active customers you will need?

In order to determine how many active customers you'll need to hit your Year 3 revenue goal, the next input assumption you need is your pricing model. From there you can determine the average yearly revenue per customer and calculate the number of active customers.

The number of active customers is already a more telling number than your revenue goal.

It helps to answer the following questions:

- Is your customer segment big enough?
- Is your early adopter segment big enough?

Steve Determines How Many Active Customers He'll Need

Steve decides to model out his Software Developer business model first. Given his MSC is hitting an annual recurring revenue (ARR) of $10M/yr using a subscription model (SaaS) that charges $50/mo, Steve determines that he'll need 16,667 active customers ($10M/yr / ($100/mo x 12 months)) by year 3.

He's a little surprised by that number and does a quick online search for "Top VR/AR app companies" which returns 2,286 firms. That makes him a little nervous because that only accounts for 14% of his required number of customers. Granted this number only represents his early adopter segment, he wonders if the pace of AR/VR adoption will grow to account for the missing 86%? While he's hopeful that his no-code platform will turn non-software developers into customers, there is a lot of ground to cover which makes him uneasy.

2. Determine your minimum customer acquisition rate for growth?

Life would be really great if all we had to do was work really hard just for just 3 years, hit our revenue goal, and then collect an annuity for life. We could retire on a beach!

But unfortunately it doesn't work out that way because of customer attrition or churn.

All businesses have churn.

This means that at some point customers will start leaving and you'll need to replace them — not to grow your business, just to sustain it. This represents your minimum customer acquisition rate. If you want to grow your business beyond your MSC, your actual customer acquisition rate needs to be greater than your minimum customer acquisition rate.

For example, if you have 10,000 active customers and 5% monthly churn, every month you will lose 500 customers on average. You'll need to acquire at least 500 new customers a month (6,000 new customers a year) just to maintain your business model and more than that to grow.

While most people understand the concept of churn, they struggle with estimating it. A more practical approach is using the inverse of churn: Customer lifetime.

Customer lifetime: How long (in months or years) do you expect to keep your customers on average?

Once you estimate your average customer lifetime, use the table below to determine your monthly churn rate.

$$\text{Churn rate} = \frac{1}{\text{Customer Lifetime (in months)}}$$

Lifetime in years	Monthly Churn rate
1	8.33%
2	4.17%
3	2.78%
4	2.08%
5	1.67%

Figure 2-3. Monthly Churn Rates

Steve Determines His Minimum Customer Acquisition Rate

Steve does a quick look-up on average customer lifetime for SaaS companies and finds that 4 years is considered a good target. From the table above, that represents a 2.08% monthly churn rate.

If at year 3, he has 16,667 active customers, he'll start losing 347 customers/mo. That means he'll have to acquire at least 347 customers/mo just to maintain his business model.

Your minimum customer acquisition rate at your 3-year mark is often the first dose of reality when testing ideas. But we still have one more step to take to get the full picture.

3. Determine how many leads you'll need to attract?

No customer acquisition funnel converts at 100%. So in order to test the viability of the market against your goal, you need to also ballpark how many leads and trials/pilots you might need.

The input assumption you need to determine this is your paid conversion rate metric. With a little research, it's fairly easy to find typical conversion rates for your type of product.

Steve's Business Model Falls Apart

Steve uses the 1% paid conversion rate for SaaS to realize that in order to acquire 347 new customers per month, he would need to attract 34,700 leads/mo. And this is just to maintain his annual recurring revenue — not to grow it. As VC's expect a 10X return in the subsequent 2-4 years after product/market fit, that means he'll need to find a way to eventually attract 347,000 leads/mo (or 4m+ leads / year). That leaves a knot is his stomach.

He draws a quick sketch visualizing these numbers:

Steve's business model has fallen apart.

If your business model doesn't work, adjust the business model.

3. Adjust Your Business Model

Even though what we're creating is a rough estimate, any estimate is better than none. If your model doesn't have a chance of working on paper, it's not going to work in the real world either.

It's much better to invalidate your model in 5 minutes than spending 5 months pursuing a flawed model.

The power of Fermi estimates, is that unlike a spreadsheet, they are built using just a small number of input assumptions. This makes is a lot easier to understand why a model fails, and more specifically, what levers to pull in order to fix the model.

When looking for levers, small incremental adjustments seldom fix the model. You're looking for either one 10x lever, or more realistically, a series of levers that add up to 10x.

Steve Fixes His Business Model

Steve goes over his back-of-the-envelope calculations and lists out the input assumptions he used.

He finds that his model fell apart with just 4 key metrics:

1. MSC: $10M ARR in 3 years
2. Pricing (Revenue): $50/mo
3. Customer Lifetime (Retention): 4 years
4. Paid Conversion Rate (Paid Acquisition): 1%

Next, he goes over each one and tries to find a 3x-10X lever.

He recognizes that his MSC is set by his ambition and is non-negotiable so he skips that. He feels the same about his customer lifetime assumption. Sure, he might be able to keep good customers for an additional 1-2 years, but there's no way he can guarantee they'll stay 3x-10x times longer!

All of a sudden, it dawns on him that the most actionable lever in his control is pricing. The reason he picked $50/mo was to make his product highly appealing to software developers in order to drive adoption. But could a software

developer justify paying 10x?

Most of the existing alternatives on his Lean Canvas are free to use but they require the software developer to then spend hundreds of hours of coding to build an app. A typical app takes 200 hours to build, and at a billing rate of $50-75/hr, that represents $10-15K.

Steve believes that his platform could easily shed off 10x the app development time — taking 20 hours/app versus 200 hours/app. Using that anchor he would surely be able to justify charging at least 5x the price ($250/mo). Could he charge 10x the price ($500/mo)? Maybe.

- With 5x the price, he would need 1/5th the number of customers.
- With 10x the price, he would need 1/10th the number of customers.

He then turns his attention to the other canvases. He wonders

- how much a retailer would value a solution that helped them sell 3-10X more stuff online?
- how much an architect bills a client for a 3D rendering?

These are the right questions to be asking in order to determine value-based pricing. Remember, that customers don’t care about your solution, but their problems. They definitely don’t care about what your solution costs to build. The best way, then to set pricing for your product is not by anchoring it against the cost of building your solution, but by anchoring against

- the cost of how they are solving these problems today, and
- the value you promise to deliver (your unique value proposition).

Isn’t this just funny math?

Not really, because this exercise exposes the input assumptions that make your business model work.

When Steve started this exercise, all he had was a business model story with a set of qualitative assumptions, which seemed like a promising start for an early stage product.

However, after running the Fermi estimate exercise, he found out that even in a best case scenario his Software Developer business model would not hit his minimum success criteria goal of $10m ARR. In order to have a chance of hitting the goal, he needed to raise his pricing by at least 5x ($250/mo) and his model would be even better at 10x ($500/mo).

His pricing model just become his riskiest assumption — one that he can and should test sooner versus later.

Run the Back-of-the-envelope Test on Your Idea

While we all need a ballpark destination to justify the journey, it's not the destination itself but the starting assumptions and milestones along the way that inform whether we are on the right path or need a course-correction.

Ballpark your business model by following the 3-step process outlined below.

1. Set a Minimum Success Criteria Constraint

Remember this can be a deep why question but it's critical to use your MSC to constrain your idea versus the other way.

2. Can your idea deliver on your goal?

Use your pricing model, customer lifetime, and conversion rate assumptions to estimate how many customers you'll need to hit and sustain your goal.

While the Fermi estimation math is easy enough to do by hand, check out the **online traction modeler tool** at http://TractionModeler.com which helps you quickly run through various scenarios and visualize a 3 year traction roadmap.

3. Adjust your Business Model

If your idea falls short of your minimum success criteria goal, identify the key levers that broke your model and see if they can be dialed in to fix your model. These key levers are typically also the first set of assumptions you should test. The deliverable from this Fermi estimation exercise is creating a business model that works on paper. Don't forget to add these input assumptions to your Lean Canvas.

If you have a multisided or marketplace model, the steps are the same but you

need to consider both sides of the model.

Stress Testing Feasibility

The key question here is: “Can this be built?”. Only once your model can potentially deliver on your three year minimum success criteria goal, should you then focus on feasibility:

- What kind of solution would you need to build?
- Is such a solution even possible to build?
- What skillsets would you need to build such a solution?
- How big of a team would you need to build your solution?

Remember, you’ve got three years to get to your minimum success criteria and all product journeys go through a J-curve where profit trails revenue, and revenue trails traction..

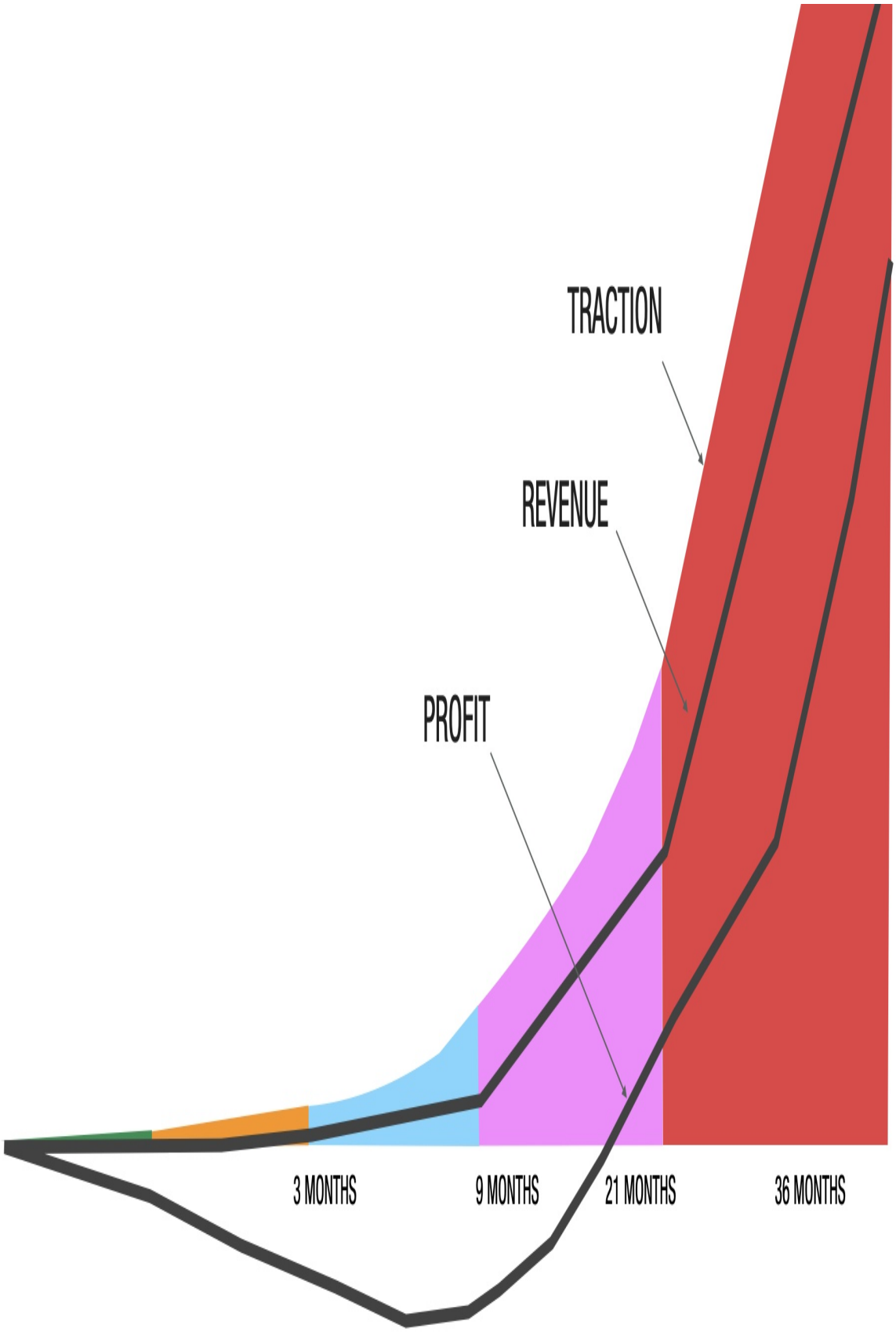

TRACTION
REVENUE
PROFIT
3 MONTHS
9 MONTHS
21 MONTHS
36 MONTHS

Figure 2-4. The Product J-curve

Be prepared for this to be an iterative journey and don’t overthink feasibility at this stage.

Chapter 3. Pitch Your Business Model

A NOTE FOR EARLY RELEASE READERS

With Early Release ebooks, you get books in their earliest form—the author's raw and unedited content as they write—so you can take advantage of these technologies long before the official release of these titles.

This will be the 3rd chapter of the final book.

The #1 reason why products fail is building something nobody wants. The #2 reason why products fail is not getting the right buy-in from key stakeholders.

Your key stakeholders include your founding team members, early customers, advisors, and investors.

If you're incubating your idea in a large company, you're asked to write a 60-page business plan with a 5-year financial forecast and an 18-month product roadmap. For new innovative ideas, these things are simply unknowable at the outset. As a result, these ideas seldom get past the gatekeepers.

If you're a startup (or part of an innovation team with a mandate to innovate), getting started is a bit easier. But then you get stuck shortly thereafter when trying to secure additional resources to grow your product and team. You need to pitch your idea in order to get others to see what we see, to buy into our world view, join our mission, and invest with time, money, and/or effort.

We saw how Steve struggled to get others to see what he saw with his idea. He wasn't able to convince others to get behind his vision which led to a classic Catch-22. Even if you're bootstrapping your idea, and not seeking investors, you'll eventually need additional resources like co-founders, equipment, etc. to grow an idea.

Pitching is a key skill all entrepreneurs need to learn. You don't just pitch for investment. You pitch to acquire customers, co-founders, and advisors. In this

chapter you'll learn how to communicate your idea clearly and concisely to others so they buy-in.

The Different Worldviews of an Idea

In his groundbreaking book: *All Marketers Tell Stories*, Seth Godin defines a "worldview" as the set of rules, values, beliefs, and biases people bring to a situation. Good marketing is NOT about changing a person's worldview, but rather framing your story in terms of their pre-existing worldview.

The same is true in entrepreneurship.

Good entrepreneurship is NOT about brute-forcing your solution, but rather framing a business model story in terms of your audience's pre-existing worldview. Your audience, in this case, comprises of investors, customers, advisors, and even competitors.

The first step to developing an effective pitch is understanding these worldviews.

The Story We Tell Ourselves

When we get hit by an idea, the thing we most clearly see is our solution. We spend a disproportionate amount of time talking about the uniqueness of our product features or its underlying technology breakthroughs. And we believe that if we simply build out this solution, everything else will work itself out.

What typically keeps us up at night are

- building an awesome solution,
- securing enough runway to bring our awesome solution to life, and
- building enough defensibility against competition.

By now, you should be able to recognize this as our Innovator's Bias at work.

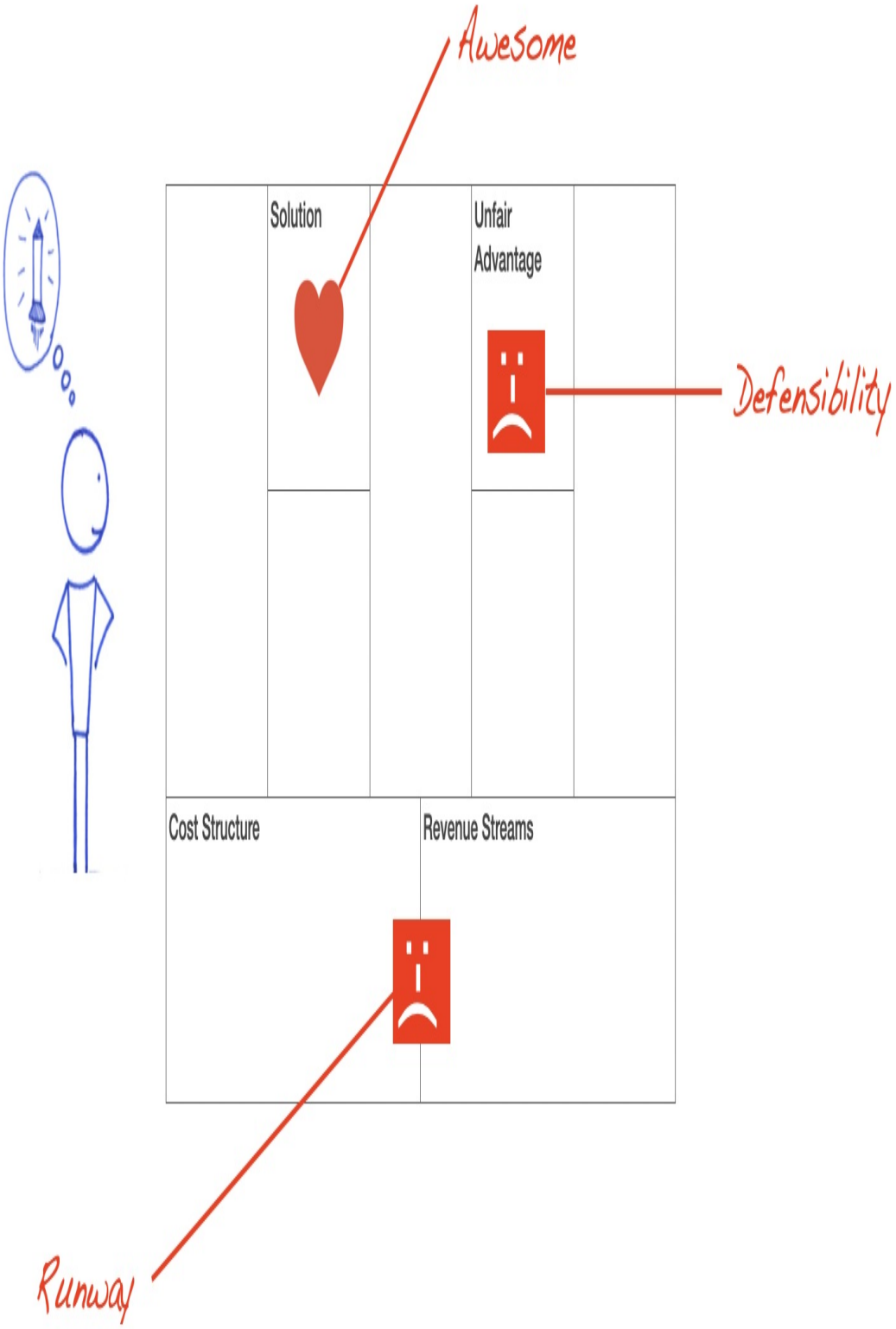


Figure 3-1. The Entrepreneur Worldview

The bigger and more immediate problem though is that other people don’t see what you see (yet). In order to get them on your side, you have to frame your story differently.

The Investor Story

Investors don’t care about your solution, but a business model story that promises them a return on their investment within a set time frame.

This is what they really want to know:

- How big is the market opportunity? They don’t care who your customers are, but how many—your market size.
- How will you make money? They want to understand the intersection of your cost structure and revenue streams—your margins.
- And finally, they want to know how you will defend against copycats and competition who will inevitably enter the market if you are successful—your unfair advantage.

But what gets an investor’s attention above everything else is traction. If you walk into an investor’s office with the beginnings of a hockey-stick curve, you’ll trigger a Pavlovian response—they’ll sit you down and try to understand the rest of your business model story.

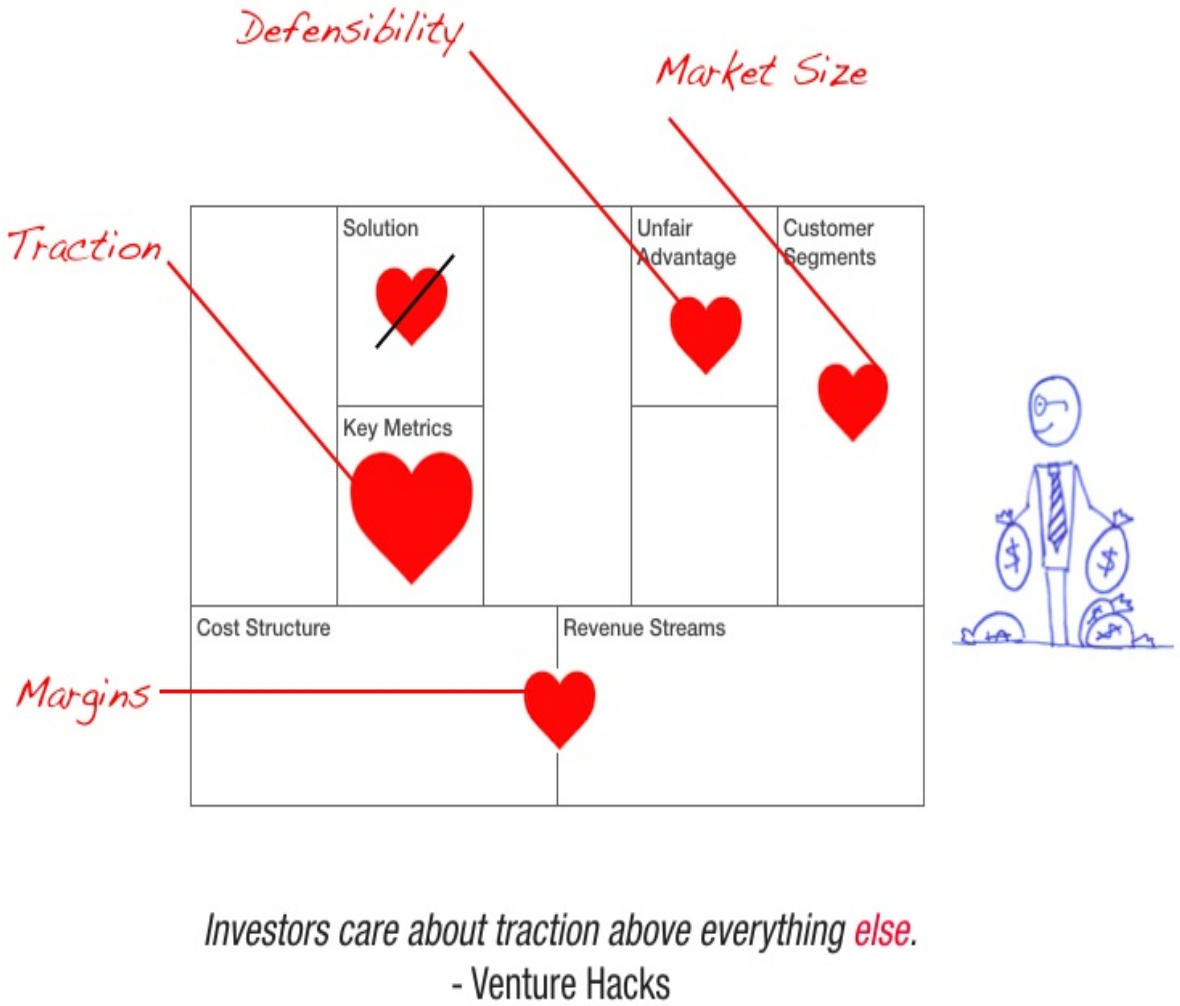


Figure 3-2. The Investor Worldview

The Customer Story

Customers don't care about your solution either, but the problems (or obstacles) that keep them from achieving a desired outcome or getting a job done.

You probably didn't wake up today with a burning desire to buy a mobile app or to sign up to a website built on Wordpress. On the other hand, if you were looking for a job, you might have signed up for a job listing service that used the headline: "We help you find your dream job in 30 days or your money back".

Getting a customer's attention is the first battle. That's the job of the unique value proposition (UVP). The headline above is an example of an effective UVP that communicates, not your solution, but the finished story benefit one gets after

using your solution.

If your promise connects, then only do you have permission to tell your customer more about your solution—typically through a demo.

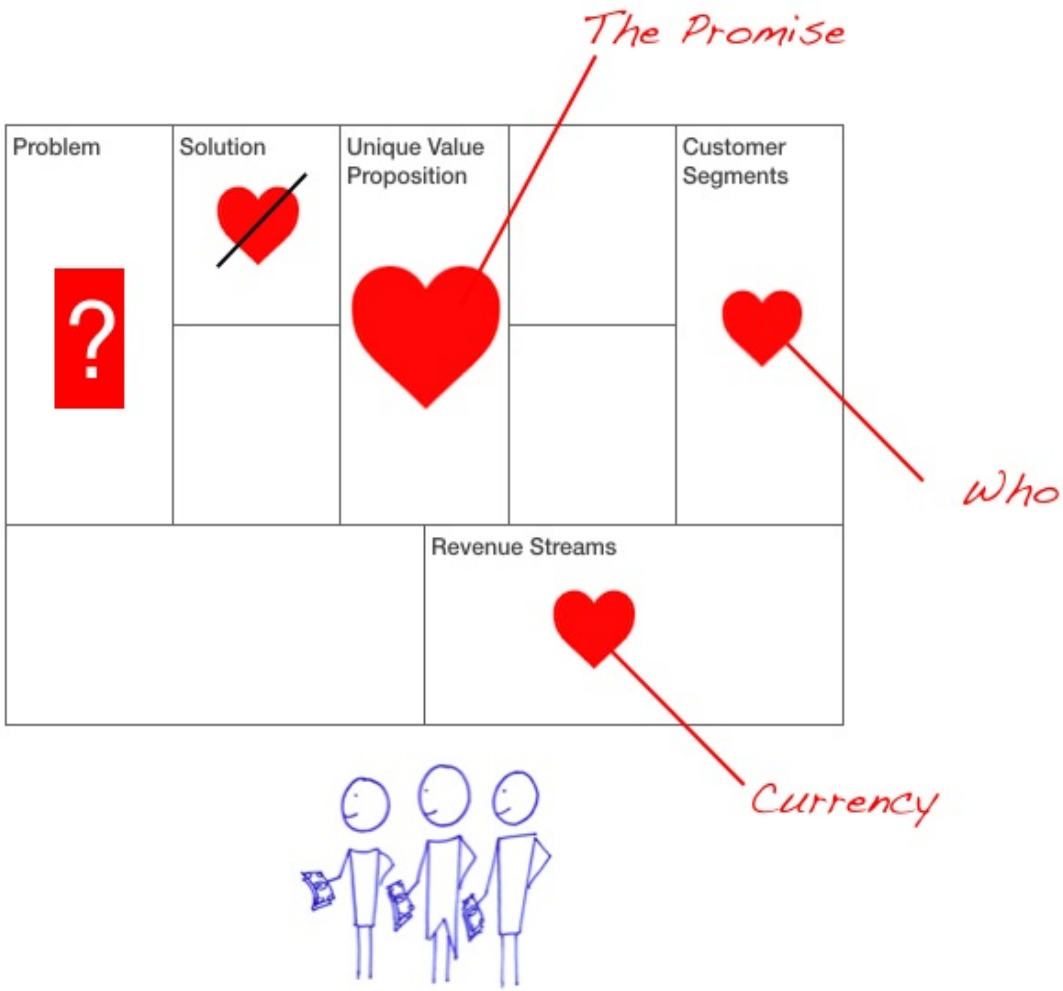


Figure 3-3. The Customer Worldview

A demo is a carefully scripted narrative that helps the customer visualize how they go from point A (riddled with problems) to point B (problems removed by your solution). If you deliver a compelling demo, the only thing left to address is what you want in return—the currency exchange captured under revenue streams. In a direct business model, this may be a direct money exchange. But in multi-sided models, this may instead be a derivative currency (like attention) that is then converted to money through a secondary transaction (with advertisers).

These are the two big business model stories to tackle first. You always want to

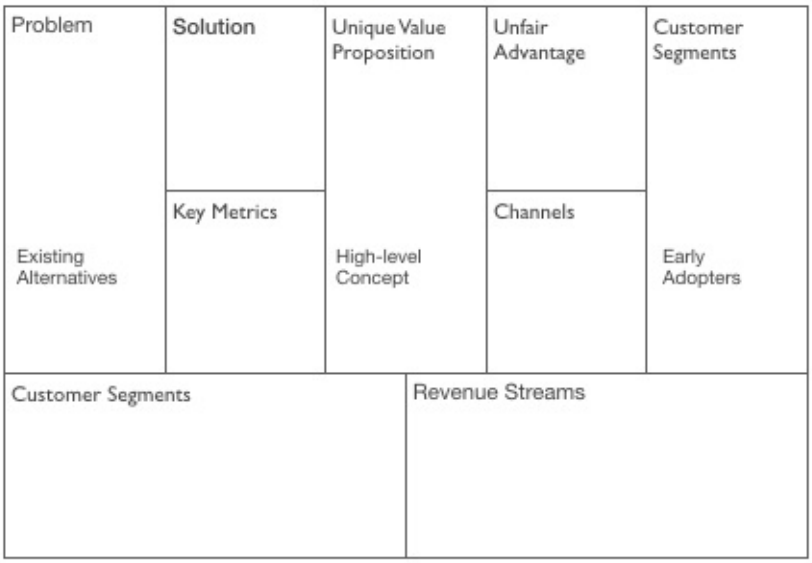
lead with your strongest foot forward. With investors, this is with a strong traction lede. With customers, this is with a strong promise lede.

The next conversation is a bit different.

The Advisor Story

We all need people other than ourselves to guide us, call our B.S., and hold us externally accountable—aka advisors.

Advisors too bring a unique worldview to the conversation, but unlike the others, their worldviews are driven by their past experiences and interests. That is why it is important to surround yourself with complementary advisors AND to be as open and honest with them. When you simply practice “success theater” with them (where you only share good news), while it may result in a pat on the back, it misses out on a huge opportunity for learning.



Help me help you.
- Jerry Maguire

Figure 3-4. The Advisor Worldview

When talking with advisors, I find it best to provide a quick business model progress walkthrough (5 mins or less) using the Lean Canvas as a visual storytelling aide. Then I shut-up and just listen. I listen for objections (risks) and ideas (possible solutions)— without getting defensive or trying to change their mind.

No one has a crystal ball and you alone "own" your business model. Your job isn't to blindly follow the advice given, but rather to rigorously test the most promising ideas—and make them your own.

There is one more story…

The Competitor Story

We also have conversations with our competitors. These are not your nice "sit downs over coffee" types of conversations. Rather these conversations test your marketing, pricing, and positioning of your business model. Good stories serve as deterrents against competitors and amplify your unfair advantage.

I put this one at the end because I find that too many entrepreneurs prematurely pay attention to their "competitors" too early. This is predicated on the fact that your supposed competition has a clue. What if they are as clueless as you are Simply positioning against your competition guarantees a different approach, not the right approach.

Your true competition is NOT determined by who you think they are, but who your customers think they are.

This is something you uncover from your customers, not through a SWOT (Strengths, Weaknesses, Opportunities, and Threats) analysis. Once you understand the existing alternatives your customers hire today to get their jobs done, by all means anchor, price, and position against these existing alternatives which is the most effective technique for getting customers to switch to you.

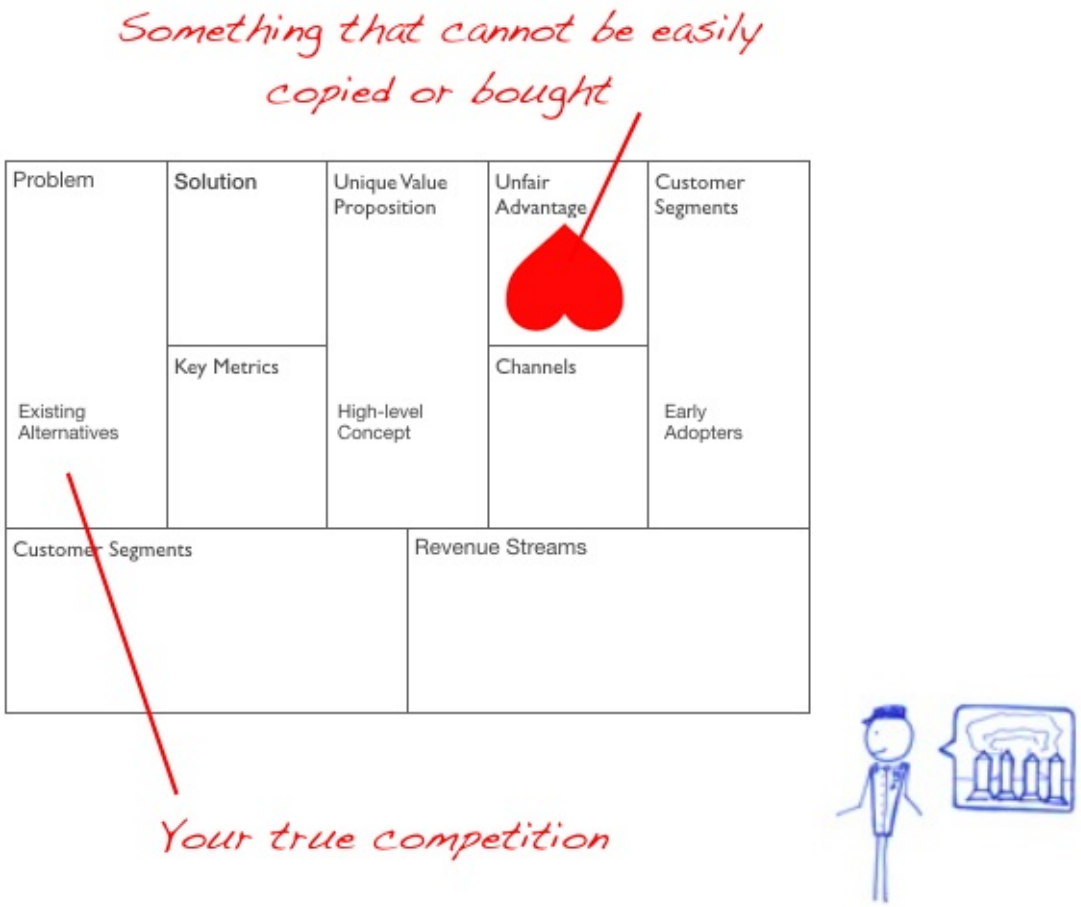


Figure 3-5. The Competitor's Worldview

So where do you start? The lowest common denominator across all these worldviews is traction. When you have traction, it's easier to attract customers, team members, advisors, investors, and even competitors. As traction is nothing more than your product's engagement with customers, it follows to start with your customer story. From there, we will layer on additional elements to build up to a full-blown business model pitch that you can share with your advisors and investors.

Start With An Elevator Pitch

An elevator pitch is meant to be a quick overview of your idea in the event you find yourself in an elevator with an investor or customer and have just 30 seconds to pitch them.

The problem with most elevator pitches is that they sound like this:

> *We build a blockchain-driven logistics company that is powered by machine learning and artificial intelligence.*

They are often a barrage of buzzwords that leave you flummoxed as to what the company really does. The better ones sound like this:

> *We build lightsabers.*
>
> *We train jedis.*
>
> *We help jedis fight the evil empire.*

While these elevator pitches don't drown you in buzzword bingo, they still assume too much and often fall flat. Why? They are too solution-centric and have no story.

An elevator pitch is NOT about your solution

The mistake many entrepreneurs make is **trying to explain their solution** in their elevator pitch.

That's not the job of an elevator pitch.

The job of an elevator pitch is to pique interest. And if you're successful, to prompt the other person to ask for more (versus making an excuse to leave).

Think of it as a teaser to a blockbuster movie. They don't show you the entire movie but get you excited enough to want to watch it. No one cares about your solution yet. So you have to start somewhere else. You have to start by first setting the context that creates the space for a solution like yours to exist. Even blockbuster Hollywood movies do this.

An elevator pitch is the beginning of a good story

Our brains are wired for stories.

As a civilization, we have used stories for generations as a way to pass along information. A good story engages us and has the power to drive us to action.

Of all the types of stories, there is one type of story that stands out -- The Hero's

Journey. Joseph Campbell found a pattern that runs through many mythological stories that he codified in his book, *The Hero with a Thousand Faces*.

The Hero's Journey is the most popular story arc that is used even today in almost all Hollywood blockbusters. Star Wars, Harry Potter, Cinderella -- all share this story arc. This same story arc can also be used to deliver a compelling idea pitch.

Here's how:

Define The Characters in Your Business Model Story

All stories need characters.

So what do you think are the essential characters for a Hero's Journey story? Yes, a hero and a villain.

Who's the hero of your story?

It may come as a surprise... but you aren't the hero of the elevator pitch story, nor is your product.

It's your customer.

You don't actually want to be the hero in this story. Think back to movies like Harry Potter or Star Wars. The hero journey story is a transformation story that begins with a struggling protagonist that reluctantly accept the call to become a hero.

How about the villain?

This one is easier. Yes, this is your competition. But as you'll see later, it's far more effective to frame your competition not as an obstacle that prevents you from succeeding, but instead as an obstacle that prevents your customers from succeeding. More on that later...

So, where do you fit in?

You are the person that guides the hero through their transformation from ordinary to hero.

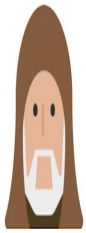
You are the guide character.

This is Obi-wan in Star Wars, Dumbledore in Harry Potter, and the Fairy

Godmother in Cinderella.

Where does your product fit in?

Your product is the gift you give the hero that makes this transformation possible.



YOU

This is your customer

This is your competition

YOUR PRODUCT

Figure 3-6. The Cast of Characters

Let’s see how the Hero’s Journey story arc works using the original Star Wars movie as an example.

A STAR WARS TEASER PITCH

The movie introduces our hero character, Luke, as a regular young adult who is bored out of his mind on a remote planet in the galaxy (BEFORE).

Then something happens (TRIGGERING EVENT).

Storm Troopers show up looking for secret plans hidden by a princess in a droid (R2-D2) that we see earlier on Luke’s planet. Luckily, Luke is off on an errand when the Storm Troopers reach his village, but unfortunately, his uncle and aunt aren’t spared.

These plans are the key to stopping a large weapon (the Death Star) from being built. Once the weapon is completed, the entire galaxy could come under the rule of the evil empire (WHAT’S AT STAKE).

While Luke would like to help, he has no special powers and cannot overcome the powerful dark lord villain who commands the evil empire - Darth Vader (PROBLEM).

Then our hero gets a gift - a light saber (PRODUCT) from our guide character, Obi-Wan (THIS IS YOU).

Our hero reluctantly accepts the call to action, and encounters several setbacks along the way. But eventually transforms himself into a powerful jedi. This gift and jedi-training (Unique Value Proposition) helps our hero destroy the Death Star and save the day.

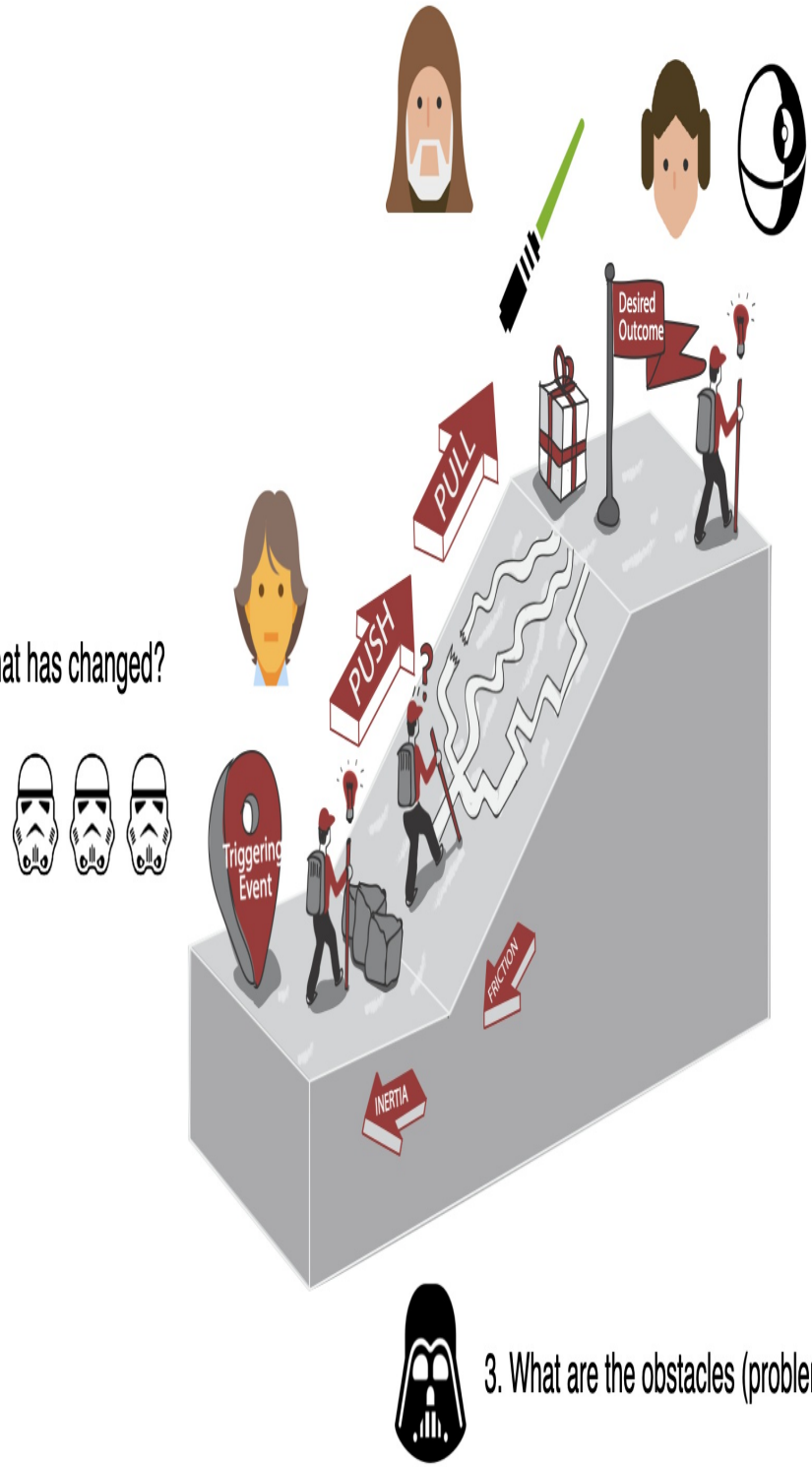
I’ve intentionally skipped a lot of story details because it doesn’t belong in the elevator/teaser pitch.

It’s time to craft your elevator pitch

The picture below (see Figure 3.7) shows the story arc steps that you can use to craft your elevator pitch.

4. What is your UVP?

2. What are the stakes?



1. What has changed?

3. What are the obstacles (problems)?

Figure 3-7. The Customer Story Pitch

Here's a fill in the blanks template:

> *When **customers** encounter a **triggering event**,*
>
> *they want to achieve a **desired outcome**.*
>
> *They would normally use **existing alternatives**,*
>
> *but these **existing alternatives** have **these problems**. If these problems are left unaddressed, this is **what's at stake**.*
>
> *So we built a solution that helps **customers***
>
> *achieve **unique value proposition**.*

Here's an example of an elevator pitch from one of my own products:

> *When **entrepreneurs** get hit with a killer idea,*
>
> *they often **need to raise money to get their idea off the ground**.*
>
> *They are asked to write **a 40-page business plan**,*
>
> *but **business plans** take **too long to write and no one even reads them**. If no one engages with their idea, they don't get the necessary resources to bring their idea to life, and **their idea withers away**.*
>
> *So we built a solution that helps **entrepreneurs***
>
> ***clearly and concisely communicate their idea in under 20 minutes and get buy-in from key stakeholders** so they can **spend more time building versus planning their business**.*

Notice that no where in this pitch do I name the product: Lean Canvas.

Outline Your Origin Story

Everyone gets hit with ideas. Entrepreneurs choose to act on them.

Your origin story is the backstory of your idea, and you are the hero in this story.

Your backstory not only humanizes your pitch but answers two critical questions: “Why now?” and “Why You?”.

Investors typically get pitched the same idea over and over. What they want to know is:

- What has changed that makes this an idea whose time has come (why now)?, and
- What prompted you to act (why you)?

Think back to what triggered you to act on your idea. What was the source of the idea spark that set you in motion?

Your origin story is also the perfect place to introduce your founding team — how and why you came together as a team?

Craft a 5-minute Business Model Story Pitch

It’s time to bring it all together into a business model pitch. Plan on delivering this pitch in 5 minutes using a 10-page slide deck that follows the same desirability, viability, feasibility ordering that you used earlier when modeling your idea.

Here’s what to address on each slide:

Desirability

Slide 1: Why now - TRIGGERING EVENT

What has changed in the world that makes this the right time for your idea? This is often a well-known macro change or trend such as climate change, the invention of the Internet, a global pandemic.

Slide 2: What’s at stake - THE MARKET OPPORTUNITY

If things are left the way they are (doing nothing), what’s at stake? An opportunity can be framed in terms of either a pain (loss) or a gain (aspiration). While it helps to do both, remember that people are more loss averse than gain seekers.

Slide 3: What’s broken - THE PROBLEM

This is where you introduce the existing alternatives and outline why they aren't fit to adapt to this triggering event. Your job here is to break the existing alternatives as a viable solution.

Slide 4: How do you fix the problem - YOUR SOLUTION

You now introduce your super-power solution and describe how you address the problem differently (your solution) and help your customers achieve their desired outcomes (your UVP).

Viability

Slide 5: What's your moat - UNFAIR ADVANTAGE

Once investors are able to contextualize your solution and understand your unique value proposition, they want to know how you'll defend against copy cats and competition. This is where you state your

- unfair advantage if you already have one,
- unfair advantage story if you are working towards one, or
- come clean and declare that you don't have an unfair advantage but are searching for one.

Slide 6: How do you make money - REVENUE STREAM

Next you explain how your business model works. You do this be describing who are your customers (if you have a multiple actors in your business model) and how monetizable value is captured (revenue streams).

Slide 7: What are your key milestones - KEY METRICS

State your 3-year minimum success criteria goal and translate it in terms of the number of customers you'll need to achieve the goal. Your goal is here is communicating that the market opportunity is both viable and achievable.

Feasibility

Slide 8: Baseline your current progress - CURRENT STATE

Summarize your current progress to date.

- What have you done so far?
- What’s working?
- What’s not working?

Slide 9: Can you pull this off - THE TEAM

This is a good place to share your origin story and introduce your founding team.

Slide 10: Call-to-action - THE ASK

What you do here is largely dependent on who you’re pitching and your goal. If you’re seeking advice, ask for feedback. If you’re seeking buy-in, be clear on what you need next.

Get Feedback on Your Business Model Story Pitch

The best way to test your pitch is by pitching it to others. Here are some guidelines for doing this:

Who to target

It’s best to start with advisors. I use the term “advisor” loosely. These could be fellow team members, peer entrepreneurs, friendly domain experts, investors, and coaches. Notice I didn’t include customers on this list. Customers don’t care about your business model. They only care about a subset that pertains to them. We’ll cover a separate script for pitching to customers later.

Use a 20/80 Rule

Spend 20% of the time (about 5 minutes) setting the context for your idea. And the remaining time soliciting feedback.

Use a combination of slides and handouts

Your Lean Canvas makes a perfect handout while you lead your audience through your 10-page slide deck.

Walk them through your business model pitch in 5 minutes

The goal of the pitch isn’t to dive deep but give your audience a clear and

concise description of your business model.

Then listen

After your 5-minute overview is done, ask for their feedback and listen. See if they were able to understand your idea. If they got confused and ask for clarification, make notes of where.

Ask specific questions

Ask them what they think about your validation plan and your assessment of riskiest assumptions. Do they have an alternate validation strategy in mind?

Be wary of the Adviser Paradox

Ask 10 people for advice, and you could get 10 very different prescriptions that are in conflict with each other. I see this all the time at accelerators. Your job isn't to follow all the advice you're given, but rather internalize them, and apply them.

Give anyone a soap box, and they become a critic.

If you do find someone giving your overly prescriptive solutions, try to get to their underlying chain of beliefs for suggesting so... Is it based on a leap of faith, anecdotal evidence, or deep learning?

Recruit good advisors

A good coach/mentor should be focused on asking the right questions versus trying to give you the right solutions. If you find one, try to keep them.

Entrepreneurship is a journey best taken with others.

Steve Reviews His Business Model Story Pitch With Mary

"Mind-blown. This Fermi estimation exercise was a crash course in startup growth metrics. Up until now, all I was solely focused on building a great product. Now I understand that you can't just expect growth to happen. You have to build for it."

Mary nods her head.

“Yup, it’s the best 5-minute investment you can make at the outset of any idea. The real power of this tool is that it helps you find *what constitutes a problem worth solving* which informs your solution versus the other way around.”

Steve takes a moment to process Mary’s point and adds: “Hmmm, I think I see what you mean. I guess I figured out that I need to find at least a $500/mo problem to make my business model work irrespective of who of the customers were and what problems I had initially on my Lean Canvases. For my software developer Lean Canvas especially, this was a significant jump from my initial $50/mo price point that I simply pulled out of thin air without much thought.”

Mary adds: “That’s exactly right. Price is such an under-utilized lever, and lots of entrepreneurs fall into the cost-based pricing trap versus thinking in terms of value-based pricing or anchoring against existing alternatives.”

She goes on: “The other big idea that hopefully you took away from the exercise is that it’s generally better to focus on building any business model around fewer high lifetime value (LTV) customers versus lots of low lifetime value customers…”

“…because of churn?” Steve interrupts.

“Yes.” Mary smiles.

Next, Steve walks Mary through his business model story pitch and uses his latest Lean Canvases to outline how he

- set his minimum success criteria goal,
- found the right levers to pull, and
- prioritized his top three canvases.

“This is pretty thorough, Steve… and a great starting point for your models.”

“I think so too, but I still have this nagging feeling that…”

Mary nudges Steve to go on.

He shifts uncomfortably in his chair, then goes on.

“While these models have helped me focus my product’s unique value

proposition around customer outcomes versus product features, they have also increased the scope of what I thought I initially needed to build. If I stick with just the software developer canvas, I'm at least 6 months, and more like 9 months away, from a working first release. I know that while three years seems like a long time and maybe I shouldn't worry about it… but getting to 1,700 paying customers by then frankly freaks me out. That's 500+ customers per year! I've already been on this project for over a year and I feel I'm just not going fast enough. If only I had more resources - another developer or two would greatly speed things up, and someone to handle marketing and sales…"

Mary glances at her watch.

"I've got to be in a meeting in 10 minutes so I'll leave you with a thought exercise to work through. First, I get your concern. Launching a new product is riddled with extreme uncertainty… and the natural tendency is to want to go fast on everything. But going fast on everything is just a recipe for getting lost faster."

Mary notices Steve wants to jump in, but she keeps talking:

"The first step in the continuous innovation framework is sketching a model that *can possibly work*. You've done that. The *next step* is prioritizing what's riskiest in your model and formulating a validation strategy."

Steve interjects: "I get that I have to focus on desirability and viability before feasibility, but the reality of having to build an actual product and roll it out to thousands of customers, in my case, is eventually going to catch up. Isn't it?"

"Maybe. But the key is tackling your risks systematically versus all at once… I've got just 2 mins left so let me share your homework. Imagine that you are an aspiring first-time restauranteur looking to open a new restaurant. It goes without saying that the food business is risky — most new restaurants don't survive their first year. Also, most restauranteurs, like entrepreneurs, typically have their solution figured out. They have the perfect menu, the silverware, and napkins all picked out… all they need is an investor to write them a big fat check and they'll be in business. The problem, of course, is that no one wants to take a chance on a first-time restauranteur because of all the risks associated with starting a new restaurant. Sound familiar?"

Steve smiles.

“The key to breaking this catch-22 is prioritizing, not what’s easiest, but what’s riskiest. Your homework is to come up with what’s riskiest for this restauranteur and to formulate an effective validation strategy.”

Mary waits for an acknowledgment from Steve then goes on.

“Since we’ll be talking food, maybe we could meet at the new Taco place that just opened around the corner for lunch tomorrow. I heard it’s pretty amazing.”

“I love that place… but we’ll need to get there early to beat the lines - otherwise it could easily be a one-hour wait.”

“11:30 works for me… I’ve got to run… see you then.”

About the Author

Ash Maurya is the author of the international bestseller *Running Lean: How to Iterate from Plan A to a Plan That Works* and the creator of the one-page business modeling tool “Lean Canvas”. His new book is *Scaling Lean: Master the Key Metrics for Startup Growth*. Ash is praised for offering some of the best and most practical advice for entrepreneurs and intrapreneurs all over the world. Driven by the search for better and faster ways for building successful products, Ash has developed a systematic methodology for raising the odds of success built upon Lean Startup, customer development, and bootstrapping techniques.

Ash is also a leading business blogger and his posts and advice have been featured in *Inc. Magazine*, *Forbes*, and *Fortune*. He regularly hosts sold-out workshops around the world and serves as a mentor to several accelerators, including TechStars, MaRS, Capital Factory, and guest lecturers at several universities including MIT, Harvard, and UT Austin. Ash serves on the advisory board of a number of startups, and has consulted to new and established companies.