

# HOW TO CREATE YOUR LEAN CANVAS

Capture your business model in a portable 1-page diagram. The Lean Canvas is the perfect format for brainstorming possible business models, prioritizing where to start, and tracking ongoing learning.

The best way to illustrate the use of the canvas is through an example. I'll describe the thought process that went into building a Lean Canvas for the companion business model hypotheses testing tool - also called Lean Canvas.

*Brainstorm Possible Customers*

*Sketch Multiple Lean Canvases*

*Prioritize Where to Start*

## Case-study: Lean Canvas

### Background

In the course of applying Customer Development and Lean Startup principles to my products, I inevitably needed to document my business model hypotheses. I started with the worksheets at the end of Steve Blank's book: "The Four Steps to the Epiphany".

While this was a great exercise, the output was a collection of documents and spreadsheets that become hard to manage and share with other team members over time. I then ran into Alex Osterwalder's work on Business Model Canvas. While I really liked the portability and clarity of a 1-page business model, I found some of his canvas elements too general and started toying with an adaptation that eventually became the Lean Canvas. The scope of the problems I was addressing also grew from just documenting hypotheses, to measuring and communicating progress over time.

When I started, I envisioned the Lean Canvas being a replacement for worksheets and business plans which led to the following "possible customers" brainstorm list:

**Really broad category:** Anyone that uses a business plan today

### More Specific Possible Customers:

1. Startup founders (bootstrapped, funded)
2. Startup accelerators
3. Investors (Angels, VC)
4. Large companies

Since this was a "scratch my own itch" kind of problem, I decided to build my first Lean Canvas for **startup founders**.

<p><b>Problem</b></p> <p>Top 3 problems</p> <p><b>1</b></p>	<p><b>Solution</b></p> <p>Top 3 features</p> <p><b>3</b></p>	<p><b>Unique Value Proposition</b></p> <p>Single, clear, compelling message that states why you are different and worth buying</p> <p><b>2</b></p>	<p><b>Unfair Advantage</b></p> <p>Can't be easily copied or bought</p> <p><b>7</b></p>	<p><b>Customer Segments</b></p> <p>Target customers</p> <p><b>1</b></p>
<p><b>Key Metrics</b></p> <p>Key activities you measure</p> <p><b>6</b></p>		<p><b>Channels</b></p> <p>Path to customers</p> <p><b>4</b></p>		
<p><b>Cost Structure</b></p> <p>Customer Acquisition Costs Distribution Costs Hosting People, etc.</p> <p><b>5</b></p>			<p><b>Revenue Streams</b></p> <p>Revenue Model Life Time Value Revenue Gross Margin</p> <p><b>5</b></p>	

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#### **4. Hone in on possible early adopters**

With these problems in mind, get more specific on the customer segment. Narrow down the distinguishing characteristics of your prototypical customer.

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

As an example, my last product, CloudFire, was a photo and video sharing service targeted at parents. Further refinement got me to define my early adopters as “first-time moms with kids under the age of three”.

### **Case Study: Lean Canvas - Problem and Customer Segments**

#### **Customer Segment: Startup Founder**

##### **1. Top 3 problems**

###### **Problem 1: Business Models need to be more portable**

Business Plans are too static and don't get read or updated enough. A lot of entrepreneurs skip this step altogether which is NOT the solution.

###### **Problem 2: Measuring progress is hard work**

Customer Discovery is a qualitative process and requires a lot of work (documenting interviews, aggregating results, etc.) to yield actionable insights.

###### **Problem 3: Communicating learning is critical**

The biggest mind shift when practicing a Lean Startup methodology is being objective and instilling a culture of continuous learning and improvement by holding ourselves accountable to internal and external stakeholders.

<b>Problem</b> Business Models need to be more portable Measuring progress is hard work Communicating learning is critical Existing alternatives: Intuition, business plan, spreadsheets	<b>Solution</b>	<b>Unique Value Proposition</b>	<b>Unfair Advantage</b>	<b>Customer Segments</b> Startup Founders (Creators) Advisors/Investors (Collaborators) Early Adopter: Familiarity with Lean Startups, Customer Development, Business Model Canvas
	<b>Key Metrics</b>		<b>Channels</b>	
<b>Cost Structure</b>		<b>Revenue Streams</b>		

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## How to Craft a Unique Value Proposition

I highly recommend getting a copy of the classic book on marketing by Al Ries and Jack Trout: “Positioning: The Battle For Your Mind”. Ries and Trout are considered the fathers of modern advertising. This is an “easy-read” and the best crash course on marketing I’ve ever come across.

### **Be different, but make sure your difference matters**

The key to unlocking what’s different about your product is deriving your UVP directly from the #1 problem you are solving. If that problem is indeed worth solving, you’re more than halfway there already.

### **Target early adopters**

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

### **Focus on finished story benefits**

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 focusses on the benefits your customers derive **after** using your product.

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

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

## **Create a high-concept pitch**

Another useful exercise is to create a high-concept pitch popularized by VentureHacks in their e-book “Pitching Hacks”. A high-concept pitch usually builds on other familiar concepts to quickly get an idea across and make it easily spreadable. Unlike a UVP, a high-concept pitch is best used in conjunction with something else that sets the right context such as an elevator pitch.

Examples:

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

## **Case Study: Lean Canvas - Unique Value Proposition**

In the case of startups and business models, while Lean Canvas might provide an immediate benefit of offering a better process for testing business models, the finished story benefit is finding a business model that works and eventually building a successful product.

Unique Value Proposition:

### **Lean Canvas - Business Model Validation Software**

Help startups raise their odds for building successful products

I also jot down a few high-level concepts:

- **Github Meets Weight-watchers for Business Models**
- **The Startup Report Card**



## *Solution*

You are now ready to tackle solution possibilities.

As all you have are untested hypotheses, I don't recommend getting carried away with fully defining a solution just yet. Rather simply sketch out the top features or capabilities next to each problem.

*Bind a solution to your problem as late as possible.*

### **Case Study: Lean Canvas - Solution**

For each of the problems outlined earlier, here is a feature or capability that solves the problem:

**Problem:** Business Models need to be more portable

**Solution:** Use the Lean Canvas format for capturing hypotheses on 1 page

**Problem:** Measuring progress is hard work

**Solution:** Provide a simple way to “dashboard” experiments

**Problem:** Communicating learning is critical

**Solution:** Need a sharing feature to facilitate sharing lessons learned





## *Channels*

The good news is that following a “Customer Discovery/Interview” process forces you to build a path to customers early. Unfortunately, unless you are in a direct sales business, that path may not scale beyond Problem/Solution Fit.

In addition to defining the right product to build, it’s just as critical to start finding, building and testing a significant path to your customers from day one.

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.

I typically look for the following characteristics in my early channels:

### **FREE’er versus PAID**

First of all there is no such thing as a free channel. Channels we normally associate as being free like SEO, social media, and blogging, have a non-zero human capital cost associated with them. Calculating their ROI is complicated because unlike a paid channel which is used up after you pay for it, these channels keep working for you over time.

A commonly cited paid channel is search engine marketing. Eric Ries has written about how he tested his early product on \$5 a day using Google Adwords - driving 100 clicks at a CPC of 5 cents. If you can pull this off

### **Direct versus Indirect**

Another area where startups waste energy is prematurely trying to establish strategic partnerships. The idea is to partner with a larger company to leverage their channels and credibility. The problem is that until you have a proven product, you won't get the right level of attention from the bigger company's sales reps to make this work. Given the choice of selling what you know or an unproven product to make your quota, which would you choose?

*First sell yourself, then let others do it.*

The same principle allow applies to hiring external salespeople. While a salesperson can probably outsell you on the execution of a sales plan, they can't create that plan.

### **Retention before Referral**

Many startups are obsessed with building virality and referral/affiliate programs into their product from day 1. While referral programs can be very effective in spreading the word about your product, **you need to have a product worth spreading first.**

*"Build a remark-able product."*

- Seth Godin  
Purple Cow

<p><b>Problem</b></p> <p>Business Models need to be more portable</p> <p>Measuring progress is hard work</p> <p>Communicating learning is critical</p> <p>Existing alternatives: Intuition, business plan, spreadsheets</p>	<p><b>Solution</b></p> <p>Lean Canvas</p> <p>Progress Dashboard</p> <p>Sharing Learning</p> <hr/> <p><b>Key Metrics</b></p>	<p><b>Unique Value Proposition</b></p> <p>Helps startups raise their odds of success.</p> <p>High level concept:</p> <p>Github Meets Weight-watchers for business models.</p> <p>Startup report card.</p>	<p><b>Unfair Advantage</b></p> <hr/> <p><b>Channels</b></p> <ol style="list-style-type: none"> <li>1. Blog/Book/Workshops</li> <li>2. Startup Accelerators / Investors</li> </ol>	<p><b>Customer Segments</b></p> <p>Startup Founders (Creators)</p> <p>Advisors/Investors (Collaborators)</p> <p>Early Adopter:</p> <p>Familiarity with Lean Startups, Customer Development, Business Model Canvas</p>
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What you charge for your product is simultaneously one of the most complicated and most important things to get right. Not only does your pricing model keep you in business, it also signals your branding and positioning. It determines your customers.

*Your price is part of your product.*

Although there is a lot of science around pricing, pricing is more art than science. For a great primer, I highly recommend getting a copy of Neil Davidson's free e-book on software pricing: "Don't Just Roll the Dice".

Pricing is not unlike any other business model hypothesis and should be tested using the same criteria we covered earlier when building validated learning loops - create a testable hypothesis, time-box the experiment, and validate qualitatively, then verify quantitatively.

The strategy I've found that meets all these criteria is **starting with a single "Free Trial" pricing plan.**

Let's see why.

**Take your costs into account**

The ultimate goal is finding a scalable business model so it should go without saying that you also need to keep an eye on what it would cost you to deliver your solution and ensure you have a healthy margin built in.

One rule of thumb for building a successful business is ensuring the lifetime value of your customers exceeds the cost of customer acquisition by at least a factor of three.

It's hard to accurately calculate these at this stage so instead do a back-of-the-envelope calculation based on your people/hardware costs and subscription revenue to find your break-even point.

## **The Problem with Freemium**

### **Low or no conversions**

Many services make the mistake of giving away too much under their free plans, which leads to very low or no conversions. One reason for this is that creatives (artists, musicians, developers) are especially known to undervalue their own work and are really bad at setting price.

*Pricing should be set with the buyer in mind, not the seller.*

But the main reason is something we covered in the last section. You don't yet have enough usage data to correctly define the FREE plan so that users naturally outgrow it at some predictable time in the future.

### **Long validation cycle**

Even the best Freemium services report conversion rates in the 0.5-5.0% range which leads to long validation cycles. Time is the most valuable resource for a startup and you can't afford such long learning cycles on something as critical as price.

### **Focus shifts to the wrong metric**

Because "FREE" can be irrationally appealing, Freemium has a tendency to cause a premature shift in focus from user retention to user acquisition (sign-ups). Unless you have built the right product, getting more sign-ups is waste. You don't need a lot of traffic to build the right product - just the right initial customers.

*Your free users are not your customers (yet).*

## How to Approach Freemium

### **Start with the premium part of Freemium first**

Once you recognize Freemium as a marketing tactic and make a conscious decision to shorten the validation cycle, it makes sense to start with the premium part of Freemium first and use a single pricing plan your customers will bear.

Since your eventual goal is to charge for your product anyway, why not start there? Pick features and a plan based on what customers will pay for today and sign them on as your first customers. Not only is this simpler to build but it's also simpler to measure.

Then, once you have learned how your customers are using your product, you can always offer a Free plan if you want to. You would have collected valuable usage data along the way which puts you in the best position to design multiple upstream and downstream plans.

### ***Case Study: Mailchimp***

Mailchimp is frequently cited as one of the Freemium model success stories, but too often people fail to recognize that Mailchimp didn't start with a free plan. In fact they spent years building a powerful, affordable (but not free), profitable product first, with years of pricing experimentation, before backing into a free plan.

### **What is a good Free plan?**

A good Free plan should ideally behave similarly to a Free Trial. The difference is that while a Free Trial is time-based, Freemium is usage-based. If you understand the usage pattern of your product, you should be able to design the Free plan so that a user naturally outgrows it at some point X in the future that you can reasonably predict.

from this list and am currently building Lean Canvas with them - Lukas Fittl (Austria), Ross Hale (Santa Barbara), and Andrew Elliott (Santa Barbara). They are all seasoned entrepreneurs in their own right and have a passion for Lean Startups.

We came to an agreement to spend just enough effort to get the Minimum Viable Product built over 2 weeks and evaluate how we move forward after that. We agreed not to pay ourselves till the service had positive cash flow.

That said, I still used the following analysis to figure out the opportunity cost for building and testing the MVP and more importantly determine my break-even point.

### Costs

Problem/Solution Fit:

2 interviewers \* (50 interviews \* 30 min per interview) = 50 hours

Effort to get ready for interviews (mockups, scripts, etc.) = 40 hours

Build MVP:

2 developers \* 2 weeks \* 20 hours per week = 80 hours

Cost to launch = 170 hours \* \$65/hr = \$11K

Ongoing People costs = 4 ppl \* 10 hours per week \* \$65/hr = \$10,400/mo

Hosting costs currently \$0 (thank you heroku)

### Revenue

Break-even point @\$14/mo = \$10,400K / \$14/mo = 743 paying customers

Break-even point @\$24/mo = \$10,400K / \$24/mo = 434 paying customers





## *Key Metrics*

*“Find the key number that tells you how your business is doing in real time, before you get the sales report.”*

*- Norm Brodsky and Bo Burlingham  
The Knack*

Startups are inherently chaotic, but fortunately, there are only a handful of key metrics that drive a web startup. We’ll cover five key startup metrics (Dave McClure’s Pirate Metrics) a little later but for right now document the one or two key activities you think will drive usage of your product.

So for example, if you are a blogging platform writing a blog post would be the key activity.

### **Case Study: Lean Canvas**

**Creating a lean canvas** is the first key activity users would complete but using the tool to **track running experiments** is the ongoing key activity that will drive use of the tool.



## *Unfair Advantage*

This is usually the hardest section to fill which is why I leave it for last. Most founders list things as competitive advantages that really aren't. An interesting perspective, via Jason Cohen, to keep in mind is that anything worth copying will be copied. So imagine your co-founder steals your source code, sets up shop in Costa Rica, and slashes prices. Do you still have a business?

You have to be able to build a successful business in spite of that which leads to the following definition:

*"A real unfair advantage is something that cannot be easily copied or bought."*

- Jason Cohen

A Smart Bear

You may initially have to leave this box blank but it's here to have you really think about how you can make yourself different and make your difference matter. Some examples of unfair advantages - insider information, the right "expert" endorsements, personal authority.

### **Case Study: Lean Canvas**

In the course of writing my blog and book, I have been able to attract a growing and active audience of readers and "experts" interested in Lean Startups which has taken me over a year to build. Only time will tell if this "reputation" and channel proves to be an unfair advantage.

## *Prioritize Where to Start*

Once you have your Lean Canvases sketched for each customer segment, lay them side by side and select the best business model to start with.

Your objective is to find a **big enough market** you can **reach** with customers who **need your product** that **will pay a price** you can build a business around.

Here is the weighting order I use (ranked from highest to lowest):

### **1. Customer pain level**

Pick customer segments that need your product the most. The goal is to have one or more of your top three problems as must-haves for them.

### **2. Ease of reach**

Building a path to customers is one of the harder aspects of building a successful product. If you have an easier path to one segment of customers over others, take that into consideration. It doesn't guarantee you'll find a problem worth solving or a viable business model, but it will get you out of building faster and speed up your learning.

### **3. Price**

What you can charge for your product is largely driven by the customer segment. Pick a customer segment that allows you to maximize on price. The more you can charge, the fewer customers you need to reach break-even (assuming your gross margins don't change).

## Now it's Your Turn

Documenting your Plan A is a prerequisite for moving on. 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.

The important thing is sharing it with at least one other person when you are done.

*Note: The boxes on the Lean Canvas are intentionally small because it forces you to be concise. You may find it easier to free-form your answers first like I did in the last section and then fill out the canvas.*