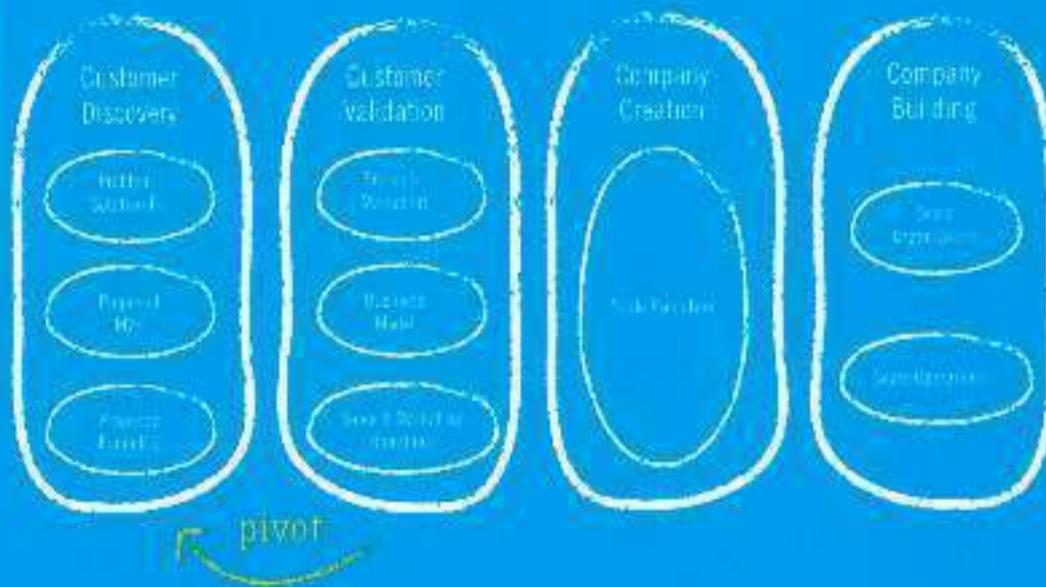


The Entrepreneur's Guide to Customer Development

A "cheat sheet" to *The Four Steps to the Epiphany*



by Brant Cooper & Patrick Vlaskovits
Foreword by Steven Gary Blank

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Foreword

A lot has happened with the Customer Development process since I published *The Four Steps to the Epiphany*. When I first conceived of the concept, I was attempting to articulate a common pattern I recognized in successful startups. I did this because I wanted to change the way startups were built—without completely depending on serendipity and at a much lower cost.

Today, thousands of students have heard my lectures and more than twenty thousand have read my book on Customer Development. Hundreds, if not thousands, of startups are practicing some elements of Customer Development today. Many in the venture capital community have come to embrace the concepts, encourage and, in some cases, require their portfolio companies to adhere to the Customer Development principles.

In addition to growing adoption of Customer Development, is its advancement. A former student of mine and intrepid entrepreneur, Eric Ries, combined Customer Development with Agile development methodologies to form the powerful concept of a “Lean Startup.” In little more than a year’s time, there are now over 3,500 members in Lean Startup Groups in 27 cities and 9 countries. Dave McClure’s AARRR metrics represent the quintessential method for measuring progress through Customer Development for web startups. In a series of deeply insightful blog posts, Ash Maurya extended my work by building a Web Startup version of Customer Development.

Before I began writing and speaking about the Customer Development model, I thought it paradoxical that these methods were employed by successful startups, yet articulated by no one. Its basic propositions were the antithesis of common wisdom yet they were followed by those who succeeded.

“It is the path that is hidden in plain sight.”

No longer is it hidden. Clearly, Customer Development has lit a fire.

What I find perhaps most gratifying is this: Customer Development continues to be advanced by practitioners, mentors, entrepreneurs and investors who endeavor to build successful startups into scalable businesses. Customer Development is not one book. It's not a religion. It is a malleable, customizable, and bespoke methodology for dealing with the chaos of the real-world. And I am proud to note, it is growing and evolving.

This book, *The Entrepreneur's Guide to Customer Development* represents another milestone. Not only is it the first "third party" book about Customer Development, it raises the bar. Authors Brant Cooper and Patrick Vlaskovits have integrated the thinking of leading Customer Development practitioners and evangelists so any entrepreneur can apply them to his or her startup. They have distilled Customer Discovery into a series of steps illustrated with clear examples, concrete action items, and traps to avoid.

This is a must read for all startups and their stakeholders.

– **Steven Gary Blank**
Menlo Park, CA
April 2010

Acknowledgements

Without Steve Blank and his book, *The Four Steps to the Epiphany*, this book would have been, of course, impossible. Steve's shared "epiphany" of Customer Development practices and processes has inspired countless entrepreneurs, investors and other business leaders to take a hard look at the way they build new businesses. Not only do we want to thank Steve for the generous insights he has provided through his books, on his blog and in his classroom, but also for the support and encouragement he has offered us in our endeavor to write this book.

We would like to acknowledge the leading thinkers and supporters of Customer Development and its like-minded principles, specifically Eric Ries, Sean Ellis, Dave McClure and Andrew Chen. We would also like to thank those big-brained entrepreneurs and practitioners who continue to discuss and debate these ideas on Rich Collins' Lean Startup Circle Google group and elsewhere. Most importantly, these individuals put their ideas into action, share their experiences, and advance the Customer Development discipline vigorously: Ash Maurya, Babak Nivi, Cindy Alvarez, Dan Martell, David Binetti, Giff Constable, Kent Beck, Kevin DeWalt, Rich Collins and Sean Murphy. Discussing the day-to-day tactics with these people as they implement Customer Development practices has been instrumental to our own thinking reflected in this book.

Further, thanks to the following individuals for participating in our Customer Development efforts on the book and for providing valuable feedback: Adam Harris, Ann Miura-Ko, Anne Rozinat, Ash, Giff, Bill Earner, Dave Concannon, Jeff Widman, Kevin Donaldson, Kyle Matthews, Matthew Grall and Pete Mannix.

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Finally, we would like to thank Fabrice Grinda, Bruce Moeller, Ranjith Kumaran and Jeff Smith for sharing their stories with us.

— **Brant Cooper and Patrick Vlaskovits**

● *Introduction*

Why this book? 11

Who Should Read This 11

● *Customer Development*

What Customer Development Is 13

What Customer Development Is Not 13

Three Levels of Learning 13

Getting Started 13

● *Case Study: Naive Thinking*

● *Concept Definitions*

Early Adopters/Early Evangelists 15

Segmentation 15

Market Type 15

"Non-Traditional" Business Model 15

Positioning 15

Product-Market Fit 15

Minimum Viable Product (MVP) 15

Lean Startup 15

Pivot 15

Getting Out of the Building 15

5 *Case Study: Multiple Pivots*

6 *Know Thy Business*

[To the Whiteboard](#)

[An Example](#)

[Know Thyself](#)

7 *Case Study: On Customer-Centric Cultures*

8 *8 Steps to Customer Discovery*

[Overview](#)

[Step 1. Document C-P-S Hypotheses](#)

[Step 2. Brainstorm Business Model Hypotheses](#)

[Step 3. Find prospects to talk to](#)

[Step 4. Reach out to prospects](#)

[Step 5. Engaging Prospects](#)

[Step 6. Phase Gate I Compile | Measure | Test](#)

[Step 7. Problem Solving Fit/MVP](#)

[Step 8. Phase Gate II Compile | Measure | Test](#)

9 *Case Study: Testing Towards a Scalable Business Model*

10 *Conclusion*

[Summary](#)

[Resources](#)

[About the Authors](#)

Why this book?

Steve Blank's book, *The Four Steps to the Epiphany*, changes the game. In a business world full of marketing "fluff," "get-rich-quick", self-help guides and analytical tomes that predict history with undeniable accuracy, Blank's book lays out an actionable framework for starting and building new startups, based on the insight that **most startups fail because they didn't develop their market, not because they didn't develop their product.**

Steve Blank published *The Four Steps to the Epiphany* in 2005 not as a "traditional" business book, but as a compilation of lecture notes for the business school classes he taught at Stanford University and UC Berkeley. Tens of thousands of people have purchased this "non-marketed" book. Its dog-eared pages, highlighter-marked paragraphs and note-filled margins prove its value like few other books because it doesn't get put away – it remains on the desk, never quite reaching the bookshelf.

The Four Steps to the Epiphany (referred to as *The Four Steps* throughout this book) is not a grand, conquer-the-world strategy, or a set of "tried and true" tactics, or collection of catchy business aphorisms. It is a malleable process of testing, learning and iterating upon the fundamental business assumptions you hold about your product, customers and market.

So, then, why this book? The objective of this "non-fiction novella" is to remove the barriers to understanding and implementing Customer Development (referred to as CustDev throughout this book) and take *The Four Steps* to another level. We hope to provide the following insights:

-
1. "Boil the content down" to an even simpler, more straightforward, actionable guide to CustDev practices.
 2. Summarize and unite the ideas of modern CustDev "thought leaders" who have emerged since *The Four Stops* was published.
 3. Put a "stake in the ground" to create standards with respect to common CustDev terms and concepts.
 4. Demonstrate the flexibility of CustDev when applied to any business model.
 5. Make the CustDev process available in an ebook format.

We have made it our goal to **get to the point**, but also **not get to the wrong point**. While debate is healthy, and we can only hope that people will discuss this book, we hope to minimize "paralysis by analysis." Participation in debates over terminology, semantics, or history - particularly in high-tech culture - often is an excuse for *not taking action*. We feel Customer Development does not need to be at the center of such a debate. You can, of course, take it or leave it. But more to the point, you can further it, change it, and even mold it to your business, your vision, and your values.

As Steve Blank says, "Customer Development is not just one idea, but the sum of Customer Development itself. It's more than one smart guy sitting on the beach in Hawaii writing a business book. It is what it preaches."

Who Should Read This

The Customer Development framework is not tied to a particular business type, market segment, or product category. Company size, revenues, or location are immaterial, as long as the company is planning on launching a new product.

Anyone can benefit from Customer Development thinking. The philosophy applies to all entrepreneurs even though specific Customer Development processes are typically associated with those businesses just “starting up.”

Although our background is working with high-tech companies and that has formed our primary frame of reference, the Customer Development model is broad and flexible, and can be applied to various industries and markets. This book focuses on the first step of Customer Development, namely Customer Discovery. Therefore, we will focus on startups.

The reality is that Customer Development methods become more difficult to implement the “further along” your business has been established. The further along you are, the more difficult it is to question and test fundamental business assumptions upon which you may have already built an organization. If, for example, you must report revenue growth to your investors next month, it may be a difficult proposition to stop what you’re doing in order to question your fundamental business assumptions. Even though taking a “time-out” to go through a set of processes that might explain why your growth is slower than projected might be exactly what you need, your board is likely to think you took the wrong turn at Albuquerque and ended up in Taos! Such a drastic step typically requires a little bit of desperation and a lot of sympathetic Directors. It might even be said, that The Four Steps was born out of just such a predicament.

Regardless of the stage your business is in, those of you most likely to pick up this book are significantly involved in a startup technology company, either as a developer, product manager, or founder. Fundamentally, this is a book for entrepreneurs who are willing and able to question their most tightly-held business assumptions; it is for this group of people this book will benefit the most.

"[SuperMac was] one of the first companies to sell an external disk drive for the original Mac; they had the first 'color paint programs' for the Mac; and when the Mac was just black and white they had the first color graphics boards and large screen color monitors for the Mac. And with all of that they had gone broke, out of business and into Chapter 11... no one inside the company had a profound belief in who the company was and why they existed. They had no model of who their own customers were and what it would take to make those customers bang down their doors to buy their products.

Nothing I couldn't fix. I took the job."

-- Steven Blank

In *The Four Steps*, Steve recognizes specific cases where CustDev may be inappropriate. Some businesses face technology risk, but little or no market risk. Steve Blank states that:

| "the risk in biotechnology companies is in the front-end of Product Development; [in] taking a research hypothesis and developing [it] into a successful and effective drug, not in the back-end of customer acceptance and adoption."

Another example when CustDev may be inappropriate is in a bubble - when investors or capital markets are throwing money at any startup with "a pulse". In such instances, Steve recommends "throwing Customer Development out the window." We would caution, however, that rather than defenestrating Customer Development altogether, you may want to keep it on the shelf. Bubbles, by definition, are short-lived.

What Customer Development is

Customer Development is a four-step framework to discover and validate that you have identified the market for your product, built the right product features that solve customers' needs, tested the correct methods for acquiring and converting customers, and deployed the right resources to scale the business.

At an abstract level, Customer Development is simply about questioning your core business assumptions. It applies an engineering, or scientific method, to what is really not a scientific endeavor (building a business). Your process will resemble the scientific method by following these steps:

- Observing and describing a phenomenon
- Formulating a causal hypothesis to explain the phenomenon
- Using a hypothesis to predict the results of new observations
- Measuring prediction performance based on experimental tests

This process is used to discover and validate the following business-related information:

- A product solves a problem for an identifiable group of users (Customer Discovery)
- The market is saleable and large enough that a viable business might be built (Customer Validation)
- The business is scalable through a repeatable sales and marketing roadmap (Company Creation)
- Company departments and operational processes are created to support scale (Company Building)

There's an old sales adage that says "maybe" is the worst answer you can get from a customer. This applies to Customer Development as well. The first desired outcome of implementing Customer Development is a thriving, successful company; all Customer Development can promise is to maximize the potential to succeed.

The second most desired outcome is the realization that there is no market, or that the market is insufficient upon which to build the business you desire. The iterative aspect of Customer Development is designed to eliminate the middle ground between these two end points. At each phase gate, you "pivot" - change your assumption(s) - in order to test another path. Ultimately, you either find the path, or realize that the market has spoken and close the business.

Customer Development

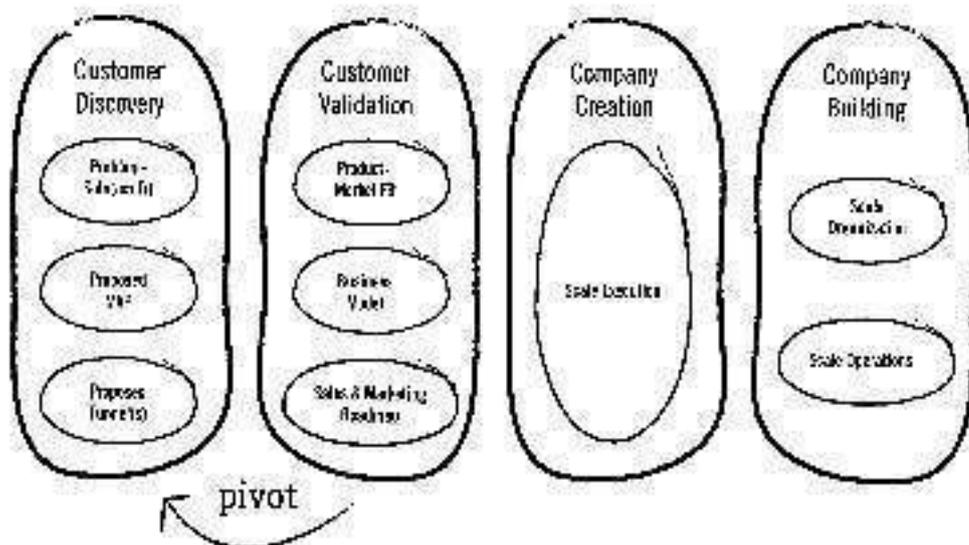


Figure 1: Steve Blank's Four Steps of Customer Development

What Customer Development is Not

Customer Development is neither a rigid set of actions that leads to business success, nor is it a "high-falutin'" philosophy that requires deep contemplation and adherence to laws brought down from "nigh", lest you be cast away into startup hell. To wit, Customer Development is neither authoritative nor dogmatic.

Customer Development grew out of Steve Blank's experience: "distilled from things I got right, and things I screwed up," as well as by his observations of the practices of successful companies.

Successful implementation of Customer Development, let alone simply believing in it, will not guarantee success for your business. Customer Development will help you – force you – to make better decisions based on tested hypotheses, rather than untested assumptions. The results of the Customer Development process may indicate that the assumptions about your product, your customers and your market are all wrong. In fact, they probably will. And then it is your responsibility, as the idea-generator (read: entrepreneur), to interpret the data you have elicited and modify your next set of assumptions to iterate upon.

Many "airport business books" urge entrepreneurs to never give in. They tell them to persist in their dream of building a great product and/or company, no matter what the odds are or what the market might be telling them – success is just around the corner. They tend to illustrate this sort of advice with inspiring stories of entrepreneurs who succeeded against all odds and simply refused to throw in the towel. While maintaining persistence and willpower is certainly good advice, Customer Development methodologies are designed to give you data and feedback you may not want to hear. It is incumbent upon you to listen. There are no billion-dollar companies who will proclaim to you that Customer Development was the model they used to achieve success. On the other hand, most billion-dollar companies have practiced some element of Customer Development, regardless of whether they knew what it was or what they may have called it.

Three Levels of Learning

There are three levels to discussing Customer Development:

1. Understanding the philosophy.
2. Applying the principles to your specific business.
3. Laying out the concrete steps to take.

Philosophy

If you put down this book having learned only one thing, we hope that it would be simply this: **"Question Your Assumptions"**.

Separate the zeal of entrepreneurship from the blindness of hubris. Pivot your way to achieving your vision or let the market guide you to a different conclusion. Most successful companies have done this.

Principles

Applying CustDev principles to your specific business is perhaps the toughest task you will face. If you have a simple business model, you're likely good-to-go. Testing your assumptions regarding the right product for the right customer, how to best deliver the product, and how to most efficiently reach and convert your customers is a fairly straightforward process. But the more complex your model and your business ecosystem, the more difficult it is to figure out the order in which to test assumptions, who to test them against, and how. There are no right or wrong answers, but as you dig deeper into all the variables you must evaluate, you will realize how high your "house of cards" actually is.

The Steps

If you can navigate how to apply these principles to your business model successfully, working through the actual steps outlined in this book will be relatively easy to understand, if not surprisingly difficult to implement. Hopefully our exercises and "pitfalls to avoid" will help you navigate through the obstacles encountered when actually getting out and doing it.

Getting Started

Customer Development, as a framework, must be tailored to your business. In order to help you accomplish this goal, we have structured this book as follows:

- We provide you with our interpretation of key concepts and definitions related to marketing, Customer Development, and "Lean Startups"
- Next, we help you "describe" your business, including your vision, model, product and target market, in a way that prepares you for Customer Development
- Finally, we provide you with the steps to take in order to complete the first step of Customer Development: Customer Discovery

Future books will attempt to tackle other portions of the Customer Development process - believe us when we say that Customer Discovery is more than enough to "bite off" at one time.

Naïve Thinking

SonicMule makes mobile products for a new phenomenon called "social music." While SonicMule founders Jeff Smith and Dr. Ge Wang's vision of their business was clear, how to actually realize it was anything but. We spoke with CEO Jeff Smith about how their diligence toward testing turns guesses into facts.

As we were setting up for the interview, we were chatting about our own music playing, which dovetailed into our formal conversation:

Author: My own music playing, regardless of my skill or lack thereof, is about playing with my brothers.

Jeff: Before recording was invented, all music was about playing and usually socially. The philosophy of our company, the vision for us is that music is a social experience. Music, today, is ripe for being redefined - and by redefined I really mean being returned back to its roots as a social experience.

Author: So that's a really big vision - where do you start?

Jeff: Well, we knew we wanted to go mobile, but being a B2B enterprise software guy, what did I know? So we approached the market with "naive thinking", which means we would have to test a theory and iterate and test again and that's how we have gone at it since day one. Test if the technology works, if the distribution works, if there's a value proposition.

Author: It seems that you have built a slew of products in a short period of time. Were you searching for the right application?

Jeff: We developed specific "mini products", each of which tested different components. Actually, the first thing we built was a mobile analytics engine that would allow us to figure out exactly what people were doing with the products and why. And as we got users, we interacted directly with them in order to calibrate some of the data we were getting out of the analytics. Later, it helped us calibrate our research of marketing conversions.

But the very first product we built was a virtual cigarette lighter for the iPhone. It was cool. The flame was rendered at 30 frames per second and you could play with the flame; you could blow it out. Our feeling was that if you didn't get to the demo within thirty seconds, forget about it. So, blowing out the flame became a classic word of mouth demo. In fact, you could click on the world and see where other people were igniting their flames at that point in time. It was this crazy social experience around awareness, but the whole point of the exercise was to see if some of these pieces of functionality would work - the technology to simulate blowing out the flame, the viral distribution. The product was a great success, though we found only 3% of our users igniting one phone to another.

Author: And 3% wasn't going to cut it...

Jeff: Right, so we did a course correction half way into Tech Boom to improve that number and when we launched Tech Boom, a virtual fire cracker to test if people would do phone-to-phone networking (over sound), that number was up to 20%.

The next day I came in to work and said if we don't have a latency problem on the phone, it would open up a whole dimension of what our value proposition could be. The next day we launched Sonic Vox, which allows you to turn your voice into Darth Vader in real-time. This was a one-day application.

Three weeks later, we launched Ocarina to test whether we could move sonic networking from an impersonal state, as in igniting one phone with another, to a personally self-expressive state through the creation and sharing of Ocarina songs.

Author: A huge percentage of iPhone applications are free. Did you go with a free or paid model?

Jeff: All of our apps required payment from the beginning. This was the only way we felt we could truly test our value proposition. We're now up to 4M paid users.

Author: How does this become really big? Are you in search of a business model that makes you a truly scalable business?

Jeff: We're not out of the woods yet, there are still questions we need answers to. But we're pretty confident about the future of social music. What we found is:

1. Everyone cares about social music
2. It's fantastic from a marketing standpoint because it puts our users to work for us. We believe the data is in, this is real, so we're doubling down.

Author: So you've tested and proven the technology, tested and proven there's a potentially huge market, tested and optimized appropriate channels, and are now in the test and iterate the business model phase.

Jeff: Yes. We did much more testing on market channels in the second half of '09. Now we are moving on to business model and engagement. We are expanding the model to better monetize our base of 4M users. How do we increase monetization per user? Can we open up social music capability to partners?

Concept Definitions

Early Adopters/Earlyvangelists

Segmentation

Market Type

“Non-Traditional” Business Models

Positioning

Product-Market Fit

Minimum Viable Product (MVP)

Pivot

Getting Out of the Building

For each of the definitions, we draw upon our knowledge from a "Customer Development" context. We have not studied Japanese lean manufacturing (Kaizen); we didn't search for the original source of the term "Minimum Viable Product;" we didn't interview Mark Andreessen about Product-Market Fit. Our intent here is to synthesize recent thinking on these subjects and "put a stake in the ground" as to what these terms mean in today's startup community. You may not agree with our definition of a concept, but at least you'll know what we mean when we use one of the terms. You can argue whether a particular tactic is "lean" or is "not lean," but be forewarned, we're going to interpret that as an excuse to avoid "getting out of the building."

Early Adopters/ Earlyvangelists

In a Nutshell: *Passionate, early users of new technology or products who understand its value before mainstream markets. Acquiring early adopters is important to jumpstart product adoption.*

Geoffrey Moore, in his 1992 book *Crossing the Chasm* adapted and popularized the concept of the "Technology Life Cycle Adoption Curve," whereby technology is adopted in five phases categorized by the type of buyer:

- **Innovators** – aggressively pursue new technology, often out of pure interest in technology.
- **Early adopters** – are the first to pursue technology for its intrinsic benefits.
- **Early majority** – rely on benefits of new technology, but will wait for others to work out the kinks.
- **Late majority** – not interested in technology per se; waits for established leader to emerge, buys de facto standard.
- **Laggards** – don't want anything to do with technology; uses technology when it's without knowledge of its existence.

The movement to each phase is hindered by a gap caused by the difference between a product's requirements and the buying habits of customers from the subsequent phase. Moore's book concentrates on the gap between early adopters and the early majority – a gap that is so wide and deep, it's best described as a chasm. *CustDev* concentrates on getting to and preparing to cross the chasm.

The Revised Technology Adoption Life Cycle

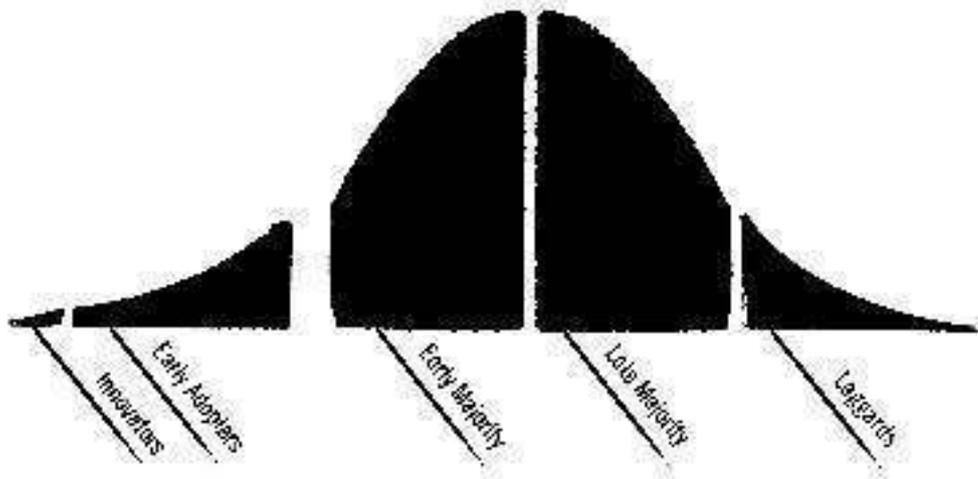


Figure 2: Moore's Revised Technology Adoption Life Cycle Curve

Early adopters are important to startup companies because they:

- Seek out new technology to solve their (or their companies') problems, not just for the sake of owning the newest technology.
- Don't rely on references from others to make buying decisions. While they are influenced by other early adopters, their main concern is solving a known problem.
- Early Adopters want to help you and (here is the best bit) want you to be successful. Early adopters enjoy opportunities that allow them to be heroes, by solving real problems.

Segmentation

In a Nutshell: *The practice of breaking down a larger market into smaller identifiable group of users who share specific needs and who reference each other.*

Market segmentation is often confused with customer profile or industry verticals. The definition is a bit more sophisticated: Market segments are comprised of like people, who share a common interest, **who have access to each other and who look to one another as a trusted reference**. If a customer prospect in California shares a need with a prospect in Zaire, **but they do not share a means of communication**, they are in separate segments. Similarly, if both prospects are in New York, but work in very different industries and have different responsibilities, they are likely to be in different segments. You treat them that way, because typically, your marketing and sales must target each differently.

The point isn't that the individuals within a segment do communicate with each other, but rather that they "have access" to do so.

The reasoning is:

1. Word of mouth regarding products works best among those who share a need and a means to communicate a solution.
2. "Access to each other" indicates a common methodology to reach them.
3. Indirect knowledge (e.g., PR, testimonials, etc.) of like individuals buying a product is a powerful influence.

One of the basic tenets of Moore's *Crossing the Chasm* is that one should choose one segment with which you establish a "beachhead on the shores" of the early majority. Attempting to scale a business when forced to customize products, tailor marketing activities and execute sales processes for multiple segments is a difficult proposition.

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