Module 4. Empathizing with the client

Unit 4.1 Lean Startup Method: Remove What Does Not Generate Value

Eric Ries, the entrepreneur who had Blank as an advisor and investor and then became his disciple, deployed his own method known as lean startup which derived from the customer development method.

Having founded (and merged) several companies, Ries decided to investigate other ways of developing ventures through a systematic method, one that would involve less risk than the ones he had gone through in his experience. This is how the author came across lean manufacturing or lean production, a Japanese method used in Toyota—whose creators were Taiichi Ohno and Shigeo Shingo—, and he adapted it to his own startup concepts.

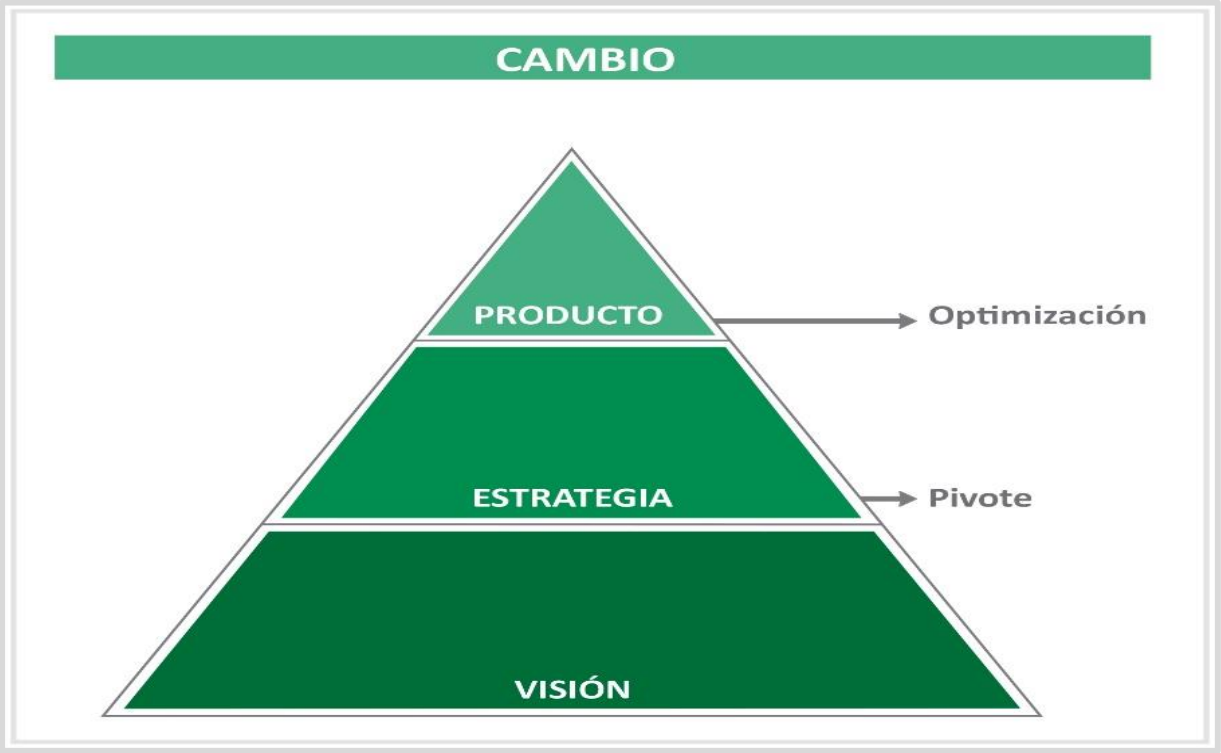
His goal was to apply lean thinking to the innovation process, recognizing that everything that generates a benefit for the customer is value; the rest is waste and has to be ruled out (Ries, 2013).

The core concept of Lean Production is based on eliminating the sources of waste through learning, which motivated Ries to adapt these ideas to tools that would increase the possibilities of creating a successful startup. This method does not guarantee the success of the project, but, when properly applied, it reduces risks and allows pivoting in time. Eric Ries explains that "the goal of a startup is to figure out the right thing to build, the thing customers want and will pay for, as quickly as possible" (p.20).

It is important to remember that, according to this author, as we mentioned in the first course, a startup is an institution designed to create (innovate in) a new product or service (a value proposition) under conditions of extreme uncertainty, understanding innovation as a discovery, a change in the existing product or business model (Ries, 2013).

Considering this definition, Ries (2013) suggests that a startup is divided into three parts, forming a pyramid, as shown in the image below.

Figure 1: Pyramid chart representing a startup



Source: Ries, 2013, p. 23.

The English translation of this image is below.

CAMBIO	CHANGE
PRODUCTO	PRODUCT
ESTRATEGIA	STRATEGY
VISIÓN	VISION
Optimización	Optimization
Pivote	Pivot

The *vision* is the basis of the startup because it indicates how far the founders want to go. It is the foundation on which the project will be built and that will allow the entrepreneur and their team to face the contingencies.

The *strategy* makes reference to the decisions that the entrepreneur makes according to their business model, making the necessary pivots to make it grow and taking account of the competitors and the customers they will have to identify.

While the *product*, as a result of the strategy, can be optimized over time—using this method—, by adding and changing the characteristics pointed out by the customers as we get to know them and learn with them.

Thus, a startup faces a range of activities during the day (serving current customers while seeking to identify new ones, creating product benefits, organizing operations and

marketing, etc.) that hinder its ability to innovate, so Ries (2013) suggests balancing all these activities so as not to lose focus on innovation.

4.1.1 Build-Measure-Learn Feedback Loop

One of the central principles of lean startup[1] has to do with build-measure-learn. Ries (2013) states that "the fundamental activity of a startup is to turn ideas into products, measure how customers respond and learn whether to pivot or persevere" (pp. 13-14), trying to minimize the total time or accelerate through the loop so that the project is successful. Therefore, learning from this process means saving time and money.

Going back a little further, we said that this method seeks to focus on getting to know the client due to the learning obtained by the application of the method so as to avoid the waste that besets startups. But how do we begin to apply this method?

All research is born out of assumptions about the object of study that Ries calls "leap-of-faith assumptions that cry out for rigorous testing" (2013, p. 15). Therefore, the process begins with the proposal of hypotheses that allow obtaining information to continue the process and, in this case, to be able to develop a minimum viable product that validates the presumptions raised. In this case, Ries (2013) formulates two types of hypotheses:

Value hypotheses: They serve to check whether the value proposition is valuable for the customers who buy or use it. And, in to corroborate them, experiments are designed and the results of these experiments resolve this concern, that is, being able to measure and learning if the product generates value for the customer and how much, namely: your startup. Does it generate value for the customers?

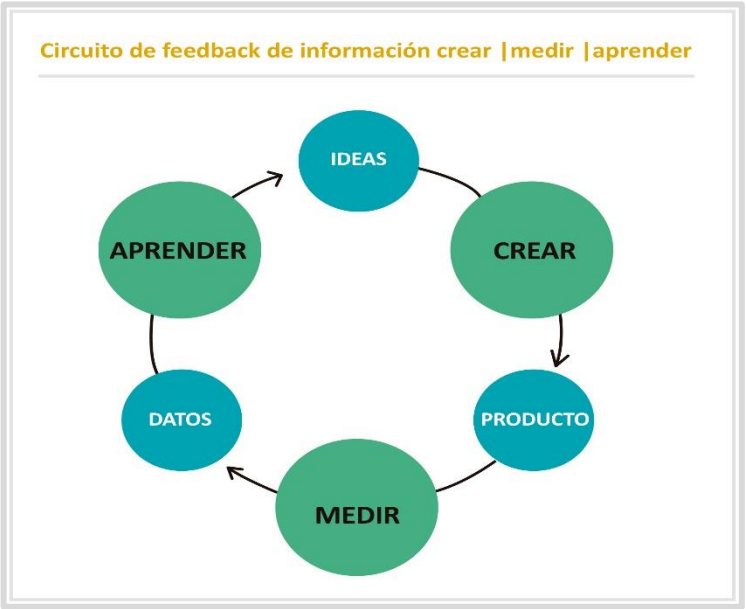
Growth hypotheses: They serve to test how new customers are attracted and how to make them aware of the value proposition that is offered. So, is your startup going to be big enough or efficient enough to solve the customer's problem?

A large part of the Lean Startup method is based on designing experiments and collecting empirical evidence to test or refute the hypotheses proposed.

A large part of the lean startup method is based on designing experiments and collecting empirical evidence to test or refute the hypotheses proposed. These are the starting point that will motorize the build-measure-learn feedback loop, the core of the lean startup method, similar to the Deming circle mentioned before–Module 3.

[1] Ries defines five principles of the lean startup method. In this text, we will only work on some of them, but we share all of them with you, below, in case you want to read them further: 1- entrepreneurs are everywhere; 2- entrepreneurship is management; 3- validated learning; 4- build-measure-learn; 5- innovation accounting.

Figure 2: Build-Measure-Learn feedback loop



Source: Ries, 2013, p. 65.

The English translation of this image is below.

Circuito de feedback de información crear|medir|aprender	Build-Measure-Learn Feedback Loop
APRENDER	**LEARN**
IDEAS	IDEAS
CREAR	**BUILD**
PRODUCTO	PRODUCT
MEDIR	**MEASURE**
DATOS	DATA

The loop is simple (Figure 2): a startup seeks to transform ideas (problems) into products (solutions) which, in this instance, are experiments. To do this, entrepreneurs are in contact with the customers in order to obtain quantitative information—if the product satisfies the customer, for example—and quantitative information by asking, for example, about the suggested price. From this feedback between the entrepreneurs and the client, the former learn and thus create their successful business model. This path is the core of the lean startup method.

We will explain each part of this framework specifically:

- **Ideas**: It is the business opportunity that will be translated into the business model through the canvas—topic of the course 4—and based on hypotheses that will have to be to be contrasted with customers. In this stage, it is really useful to apply the design thinking method that you learned in the previous course.

- **Build**: Even though the Spanish version defines it as creating, the idea of building is more appropriate, since it means the elaboration of a first version or prototype of the product or service.
- **Product**: It makes reference to the minimum viable product (MVP) whose characteristics will be developed in course 3.
- **Measure**: It is necessary to try the MVP out, test it and measure the results according to the objectives to be achieved. From this instance, valuable information will be obtained to move forward or backward with the value proposition.
- **Data**: information that will allow us to approach and understand the needs of our clients, after having tested the first version of the product.
- **Learn**: the purpose of the loop lies in this stage, according to Ries (2013), since learning will allow the improvement of the product. If the adjustments are minor, they can be repaired with some iterations. However, if the changes are big, it will be necessary to make pivots in the business model. If the latter occurs, the circuit makes a loop, that is, it starts again until the sustainable business model is obtained, having reduced the uncertainty to a minimum.

Once we have completed a lap of the circuit, the things we have learned should be the basis for new ideas that promote the beginning of a new loop, which in turn will allow us to be closer and closer to what the client needs.

Likewise, it is necessary to be careful with a common mistake that is made when going through the circuit which is related to focusing on a single element—because of knowledge, taste, challenge, etc.—, since none is primordial by itself. This can cause us to lose focus on learning and, therefore, to lose time and resources.

It is important to consider that the potential of the method lies in the validated learning that is obtained and, therefore, it is useless to start the startup by ignoring the information collected or by selecting only the information that is useful to reaffirm the position of the entrepreneur. As we said before, learning has to refute assumptions. In this learning journey, it is very likely that we will have to change the desired business model—and do it fast.

Learning must refute assumptions.

In summary, although this method does not guarantee success, it proposes a way to validate hypotheses before executing them, minimizing risk and, fundamentally, generating useful learning for the future of the enterprise. In future courses, we will talk about this in detail so that you are able to put it into practice in your business.

Building a Minimum Viable Product (MVP)

Although this topic will be developed in detail in the following course, we can say that the minimum viable product is a preliminary version of the product, a prototype that allows us to complete a lap of the build-measure-learn loop with the least amount of effort,

resources and development time possible, since any effort in the development of the product that is not necessary for the process and for learning will be a waste of time.

This first version will have few features and will differ from the final product or service, but it is important to know that the objective is to measure how it works when the entrepreneur shows it to the client. This measurement is based on what Ries (2013) calls the innovation accounting method, whose purpose is to define learning milestones that allow us to know whether or not we are making progress in the learning process.

Therefore, an MVP can be simple or complex in relation to what we want to test. What is important about it is that it be a source of information and data about what we need to improve or change.

Measuring with Innovation Accounting

Once again, the purpose of the MVP is to provide proof to the client that what you are developing will allow you to measure their reaction so as to make the necessary adjustments. This is where Ries (2013) highlights the disciplined and systematic approach of the lean startup method by proposing a system called innovation accounting—different from the traditional accounting system. The value of this system lies in its ability to measure whether we are making progress and obtaining validated learning, depending on the achievement of a series of learning milestones that have been previously defined.

Innovation accounting is intended to face the danger of the myth of the entrepreneur's perseverance and the optimism (the typical entrepreneur in love with their idea) when they want to continue supporting and investing in their idea, even when it is evident that it does not work.

Ries argues that this method "enables startups to prove objectively that they are learning how to grow a sustainable business. Innovation accounting begins by turning the leap-of-faith assumptions ... into a quantitative financial model" (2013, p. 99). And he proposes three learning milestones or stages to put it into practice:

1. First: Obtain a clear image of the current situation from the MVP that allows you to collect real data about the phase in which the company is in that moment, no matter how far it is from the objective. To define this first learning milestone or baseline situation, you could...

- Do a pre-purchase test or what Ries (2013) calls a smoke test by offering the product to potential customers in order to see if they are willing to try it.
- Build the MVP.
- Build multiple minimum viable products around a hypothesis to see how customers react to that factor of the model.

2. Second: It is necessary to "tune the engine" (Ries, 2013, p. 101) so as to be able to apply the modifications that you have discovered during the build-measure-learn process, by carrying out the necessary iterations from the identified starting point to the proposed ideal.

3. Third: Once we have a defined proposal that has been with the clients, we reach the decisive point: to pivot or to persevere. If the path to the ideal is progressing in the right way, it means that the startup is learning and using that learning properly and, in that case, it is advisable to persevere. Otherwise, the decision should be to pivot if the product strategy has serious mistakes by defining a new starting point to start the whole process again.

Finally, in order to finish with the innovation accounting method, it is important to recognize that there are two types of metrics in this process:

Vanity metrics: metrics we use to measure progress and prove that we are growing. However, these metrics can be misleading and useless for actually measuring whether you are growing or at least learning. In any case, they will probably make you feel good, but you will not have a clear guidance on how to proceed. The alternative to improve these measurements is the one we will see next.

For example, if the sales variable grows, it does not indicate whether the *problem/solution fit* (PSF) and *product market fit* (PMF) were found in the current business model. There are countless examples where attraction and conversion grew at rates of 22% per month, and retention and loyalty dropped at a slightly slower speed and, at the end of the day, they showed an increase in sales and concealed the shortfalls.

Actionable metrics: metrics whose results allow you to make decisions, continue experimenting, and learn through valuable information about your client.

A useful metric, according to Ries (2013), complies with the three A's rule:

- **Actionable**: it must demonstrate clear cause-effect relationship between what is done and the data shown by the tests, otherwise it is a vanity metric. In addition, it has to produce a unit of measurement useful for analysis.
- **Accessible**: that is to say, that they are easy to understand for anyone who needs to learn from it. Ries states that "the easiest way to make reports comprehensible is to use concrete and tangible units" (2013, p. 119).
- **Auditable**: the metric used should be able to be tested in the place where it is applied, with the real customers.

Some of the techniques used to obtain valid results from actionable metrics are the following:

- **Cohorts and split-tests:** they are divided into groups to apply experiments in which different versions of a product are offered at the same time. In this way, one can observe the reaction of the customer groups and make various inferences about the impact of the experiment and its variations. Cohort analysis is the key concept to be understood and put into practice by entrepreneurs who want to optimize their time and money. In the following courses, we will see practical examples of identification and creation of cohorts.

- **Kanban or capacity constraint:** it comes from the lean manufacturing and it serves to prioritize processes. The aim is to establish stages through which each iteration has to pass. The stages are the following:
  - Pending products.
  - Products in progress.
  - Built products.
  - Validated products. In this last case, we can consider, as an example, those elements whose functioning we have validated by testing and implementing them with a split-test.

Validated Learning

To reduce the uncertainty in which a startup is built, Ries (2013) states that it is essential to learn from the tests and experiments carried out with customers. He calls this learning *validated learning*, since it results from a process of empirical demonstration of business hypotheses. It basically means being able to make decisions based on quantitative results to reduce the risk of failure.

In this sense, we recommend reading about Ries' experience with his company IMVU (chapter No. 3 of the book *The Lean Startup*, 2013). He recounts how he worked with his team to develop the first version of the product that, in the end, nobody used, since they had developed it assuming that the attributes it had were important for people, but they never tested it. Therefore, they were forced to leave their offices, step outside their comfort zone and talk to people to find the pivots of their business model.

Unit 4.2 Integration of Methodologies

Throughout these courses, we will use different tools, integrating the methodologies of Ries and Blank, along with tools of design thinking and others, so you can apply them in your sports business.

That is why we wanted to introduce you to all the methodologies so that you understand their fundamental principles and the importance of each one. This way, you will get a better understanding of the intention behind each tool.

For projects that already have an advanced idea, that is, projects that have already begun to design and develop the prototype, it is difficult to go back to examine the hypotheses and validate the problem; however, it is highly recommended. At this stage, most entrepreneurs do not want to change their product or service, as they are convinced that it will work.

There is nothing wrong with having conviction and perseverance, but they should be accompanied by a lot of flexibility so as to be able to change and adapt to the needs of the market. Therefore, we propose carrying out a “day in the life exercise” even in businesses that already have a product/service working with active clients and growing in sales, because this activity will provide them with valuable information to improve their product/service, their sales strategy and the commitment of their clients. In short, we recommend improving business and even generating competitive advantages.

The use of these methodologies is constant in startups, even in their growth and scaling stage, in which more tools related to management by metrics are applied.

The ideal of every startup is to become a great company with a startup spirit and culture, in order to continue innovating and remain competitive in a market of exponential changes.

References

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