

## Masters of Scale Episode Transcript: Katia Beauchamp

“The beauty of emphasizing the obvious”

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**DON PAPSON:** We always kid that Mr. Hershey is the original experiential marketer. Mr. Hershey in 1905 creates a town with streets named for chocolate-making regions and cities of the world. So his crossroads in this town are Chocolate and Cocoa. His streets are Trinidad, Bahia, Granada, and so on and so forth. And so Mr. Hershey creates a town based upon a vision that he has, that he wants to immerse people into chocolate.

**REID HOFFMAN:** That's Don Papson, president of the M.S. Hershey Foundation. And he's helping us picture the town of Hershey, Pennsylvania. It was founded by the famous chocolate maker as a place for his employees to work, rest, and play.

Back in 1905, the area was nothing but farmland, which was exactly what Hershey wanted.

**PAPSON:** He decides that because milk is a key ingredient to milk chocolate, he's going to basically place his factory here so he's closer to fluid milk.

And he's creating an advantageous situation for the farmer and for himself.

**HOFFMAN:** But what about the workers that Hershey needed to turn that milk and cocoa into bars, kisses, and cups? Well for them, the draw included modern homes with electricity, heating, a transit system, and great schools for their kids.

When it came to selling his vision to the wider world, Hershey did it in a way that was almost as irresistible as the chocolate he sold.

**PAPSON:** Between 1909 and 1918, Mr. Hershey creates 75 million postcards that, basically, are inserted in his standard milk chocolate bar. And these postcards were just incredibly unique. They talked about his beautiful town.

He created an entire phenomenon around the postcard.

**HOFFMAN:** Hershey created a vision that has stood the test of time.

But to make his unconventional dream a reality, he laid out the distinct benefits for each different group – suppliers, workers, and visitors – in a way they could understand.

I believe you need to show people how your unconventional ideas will have an obvious benefit for each and every one of them.

## [THEME MUSIC]

**HOFFMAN:** I'm Reid Hoffman, co-founder of LinkedIn, partner at Greylock, and your host. And I believe you need to show people how your unconventional ideas will have an obvious benefit for each and every one of them.

Every 200 to 300,000 years or so, the Earth's magnetic field fluctuates, then flips. North becomes south. South becomes north. And we're about 500,000 years overdue for the next inversion.

The last time a flip happened, homo sapiens had yet to emerge on the world stage – and our hominid ancestors may not have noticed anything different. But for modern humanity, the change would, at least, be disorientating. Compasses would point in the opposite direction, we'd need to flip our maps 180 degrees, and Australia would have to relinquish its title of "the land down under."

Like a flip in the Earth's magnetic poles, a great idea can flip the orientation of a whole market. It sends everyone scrambling to make sense of the new order of things. Before it appears, the new product will be unimaginable to many people. To convince them that it is something they need in their lives, you'll need to show them clearly how it will improve their specific situation.

I wanted to talk to Katia Beauchamp because she introduced a new business model that flipped the beauty industry and influenced a slew of other industries.

Her company, Birchbox, sends out a monthly box of beauty product samples to its subscribers. Customers can then buy full-size versions of the samples – and many other beauty products – through Birchbox's online store.

Once the Birchbox model caught on, it rapidly spread through the beauty industry and beyond and created a whole new approach to sales. Now you can get sample boxes for anything from pet treats to underwear.

Katia's vision for how this new business model could transform the entire beauty industry seemed obvious... to her. But when Katia and her co-founder, Hayley Barna, came up with the idea in late 2009, they struggled to get anyone else to share that vision.

**KATIA BEAUCHAMP:** Just doing very cursory internet research, we discovered that beauty hadn't arrived to the internet and it was 2010, and we were shocked. And that was the first moment, I thought, what? Okay, why not us? It was so natural. I really had this thought, why not us? Why couldn't we figure this out? And of course, then the next thought was, well, why hasn't this happened yet?

**HOFFMAN:** Two things I want you to notice in what Katia said. First, when she says that beauty hadn't arrived on the internet in 2010, she doesn't mean it was impossible to buy beauty

products on the internet – rather, no one had done much more than scratch the surface of the full scale potential of beauty sales compared to other things like clothing and travel.

The second thing I want you to notice is when Katia says: "Why not us?" It's a quintessential moment that we always love to share with our guests on this show. And whenever you ask that question, you should always do what Katia did – and immediately follow it by asking: "Why hasn't this happened yet?"

Your vision may seem obvious to you. But there could be any number of reasons why others haven't seen it. And in getting people to come along, the first step is to understand why they're unable to see what you see.

**BEAUCHAMP:** We came up on our own with two simple reasons, and that was the second a-ha moment. One was that people really did want to touch and try beauty. It was tactile. It has a scent. I mean the design of the texture and the smell and the sheen, the internet struggled to really give you an engaging experience with beauty. And so the idea of trial felt very inherent to beauty shopping.

And the second thing that we felt as consumers was that beauty was already incredibly hard to shop for in the real world. You walk into a store, there's, not joking, a thousand options of moisturizer, and you think, what am I doing here? And the internet actually made it worse. So at least a store was confined by the four walls and the internet wasn't, and this was this other a-ha moment like, oh, we get the problem. We understand the problem. All we have to do is figure out how to get you to try it and limit the options.

**HOFFMAN:** It was 2009, the e-commerce promise of unlimited choice was just coming into its own. Working to limit choice was the counterintuitive twist that unlocked the full potential of the idea for Birchbox.

**BEAUCHAMP:** In 24 hours, we had the business model that is honestly the business model you see today. It was founded on the concept of bite-size discovery that's personalized, plus content, plus e-commerce, and the idea being full-funnel to generate demand and capture demand and blinders. I know I had really bad tunnel vision after that.

**HOFFMAN:** Remember that phrase Katia uses: "bad tunnel vision." We'll come back to it in a moment. But before we do so, let's break down the Birchbox business model.

This is the business model that Katia had "bad tunnel vision" for:

One: Provide sample boxes to users for a subscription fee.

Two: Build a community powered by the excitement of discovering the new.

Three: Encourage users to buy the full-size versions of the samples – and other things! – through the Birchbox online store.

Doing this would help grow sales for the suppliers who provided the samples, while delighting customers with a new sample box every month.

First, Katia and Hayley went to their business school teachers with the idea.

**BEAUCHAMP:** And they were like, "That's a bad idea." And started pitching brands and similarly brands were like, "You're so naive. Consumers don't pay for product."

**HOFFMAN:** Remember, this criticism is very specific to the beauty industry. By "product," the critics were referring to the free samples that were part and parcel of selling lipstick, mascara, and skin cream. Buyers expected to be able to walk into a store and sample anything before handing over any cash. It was an entrenched part of the beauty product experience that no one could imagine changing.

What Katia was imagining was a world in which customers pay a subscription to Birchbox for sourcing and curating a monthly box of samples.

The upside for the suppliers? Far more visibility and uptake of their samples which would convert into more sales.

**BEAUCHAMP:** So we take the sample, and we translate that into customer acquisition efficiently. That was the vision. That was the dream for the business is that it could really be a win for all.

**HOFFMAN:** So they took their pitch to a group of people they thought would get their vision: angel investors.

**BEAUCHAMP:** It was so disheartening. I mean, everybody took the meeting. Most people weren't listening, the ones who were just started thinking about how they would do it. Does it need a box? Do you need to send it together? Can you send one at a time every week? My wife doesn't use beauty products, like what about her?

**HOFFMAN:** This is where it's important to know not just what your vision is, but who you are pitching to and how you can help them to see it.

**BEAUCHAMP:** We thought this is legit, but we couldn't get anybody to really take the leap. Everybody was looking for somebody else to validate it first.

**HOFFMAN:** The idea wasn't hard to understand. However, this was 2010. People were not used to having multiple monthly subscriptions – just one or two subscriptions felt like a real commitment.

On top of this was the fear of the untested. Katia and Hayley just couldn't get these investors to share their sense of surprise and delight at having a curated box of samples arrive at their houses each month. But to them it was so obvious. So they needed to find another angle to describe it.

**HOFFMAN:** So when you did the pitches to these early investors and the investors said, "No," what was your conclusion from those no's? What learnings did you take away? What did you think?

**BEAUCHAMP:** It was a range from "too bad for you, you're going to miss something huge" and a little bit more self-actualized realization of I think I need to consider how to say it differently. Because I don't question the idea, but maybe the message isn't right. Maybe I'm not framing it right.

**HOFFMAN:** Note how Katia was unwavering in the faith in her idea. She could have put the refusals down to a lack of vision on the part of investors. And this is a valid approach – up to a point. We often talk about the "chorus of no's" that almost every pitching entrepreneur faces. Overcoming it is partly to do with grit. But it's also to do with finessing your pitch so it will prick the ears of your potential investors. Even if that pitch puts what excites you the most into a softer focus.

**BEAUCHAMP:** So I'm a woman, and I'm launching a business in beauty. And apparently that means I love beauty, and I really didn't. I loved the business of beauty. I definitely thought beauty served a purpose. It's not that I couldn't find joy from it, but I was never and I'm still not somebody who would spend discretionary time learning about beauty. And that was the whole point. And I felt as though when we were starting to pitch the concept of the problem in the beauty industry, it was almost a glaze over of "these young women who really love beauty are trying to be beauty entrepreneurs or beauty business women." And I was frustrated by that thinking, "We really don't."

**HOFFMAN:** What is so smart about Katia's approach here is how she imagines herself as the investor. Because she's not only imagining what they're looking for in a company, or a founder. She's also imagining how their preconceptions and prejudices shape their judgment. She had to make her vision seem obvious to them.

Katia wasn't passionate about creating a product in the beauty sector; she was passionate about having a transformative effect on an entire industry that would be a net gain for suppliers and customers – and of course, anyone who would invest in her idea. So she put her industry-flipping idea into more conventional terms that would appeal to an investor audience.

**BEAUCHAMP:** We see this incredible industry that has incredibly high margin, that has 2% of sales on the internet, and we believe that there is a willingness to pay for... The customer will pay to be acquired. Why is nobody listening to that?

So, yeah we really needed to shift talking about it to language and words that were more of the moment. Machine-learning and personalization and yes, this idea of customers paying to be acquired, really having this dynamic shift on the potential monetization. And we had to learn that.

**HOFFMAN:** I told Katia why I lit up when I first learned about Birchbox.

**HOFFMAN:** This is what I first tracked about Birchbox that I thought was genius about what you guys were doing, because one of the under-commented things about entrepreneurship is it isn't just innovation on a product or service or a change of technological platform or change of market. All of which are of course important, but it's also the invention of business models. And you guys had come up in solving this problem with actually in fact, a important shift in business model as a way of thinking about it. Not just subscriptions, but the notion of a selected subscription that leads to a further relationship, leads to further commerce, ties content around it and so forth. And you were at least the first that I had seen about that. And that struck me as extremely exciting. And it's funny that some investors might be so blinded by their own pre-theoretic conception of the world, not to jump on that part, which is the most interesting part of the original thing. And that invention of the business model was I thought genius.

**BEAUCHAMP:** Thank you. That's so nice. I mean, truthfully, we thought so too. When we realized what this could be, we were looking around thinking, how did we figure this out? I mean, yes, we're smart, but how did this not seem obvious to a lot of people?

**HOFFMAN:** After the initial knockbacks from the angels, Katia and Hayley took their idea to another group of investors: venture capitalists. To get investors solidly on board, Katia laid out the wider untapped opportunity that lay in online beauty sales.

**BEAUCHAMP:** We shifted a lot more to the TAM, the total addressable market in beauty, the fact that it was under-penetrated on the internet and just tried to start speaking the language of irrefutably something is going to happen here because 2% penetration on the internet for beauty in 2010 is definitely not going to be where it sticks.

**HOFFMAN:** Note how Katia hadn't given up on selling her vision for the new business model; she was just broadening the picture she was painting.

**BEAUCHAMP:** And so instead of saying, "Well do you believe in everything that we're doing?" It's like, well you don't have to believe in everything we're doing. And by the way, there's probably going to be some changes, but you do easily say yes to is beauty going to penetrate harder into the internet? Of course. And does this seem like a way that might overcome why it hasn't? Maybe. Because we identified the problem of why it hasn't as: it makes the problem of too much choice worse. The internet says there's infinite things, and the internet takes away all the magic of the touch, the smell, and also

the story and coming to life and seeing the packaging, and all of that is a part of what consumers have signed up for in beauty. We have agreed, we understand the cost of goods is a lot less and we say, "Take us on this journey of why it's fun to use these products as we get ready every day."

**HOFFMAN:** This "obvious" approach got VCs on board, and solved Katia's funding problem.

**BEAUCHAMP:** One of the gifts of venture capital that we don't talk about a lot is that their ability to suspend disbelief is high because they have the idea of so many different vats and large funds, and it isn't going to make or break their lives to get behind something in a meaningful way. So once we shifted and we were more open to the people versus the industry, we did have options. And I should say that. Then it was actually well received.

**HOFFMAN:** It's worth noting here that new business models are harder and more complex to pitch than products or services. Even though the potential upsides are huge, it takes a particular kind of investor – one who thinks in terms of interlocking systems – to buy into it.

Birchbox had found investors who were prepared to go in on the vision for a new business model. Next up: they needed to find a way to make their unconventional take on selling beauty products seem like an obvious win to suppliers and consumers.

**[Ad break]**

**HOFFMAN:** We're back! Before the break, we heard how Katia and her co-founder Hayley brought skeptical investors around to their vision for a radical new business model. Now it was time to convince the suppliers and the customers.

**BEAUCHAMP:** The supplier conversation was really challenging, and honestly the first four years of BirchBox was a supply problem. And it was extremely frustrating because it started as, "This will never work. Consumers don't pay for samples. That's not a thing."

**HOFFMAN:** Even though it was a huge upside with little downside for the suppliers, getting them onboard was a long, slow process of building relationships and proving out the vision, little by little. And it was a frustrating process.

**BEAUCHAMP:** And then when we had a little bit of traction, they said, "That is interesting, but you're too small." And then we went viral, and they said, "That is interesting, but you're too big. So we can get you something in two years." And I was like two years? We'll be much bigger then so placing an order for that now is also not helpful. So it was really challenging.

**HOFFMAN:** Katia's experience speaks to the constant struggle you can face getting people to see the magic of your product or service. It's not a case of striking upon the one, magical pitch

that sells everybody. You're going to have to do that again and again for different stakeholders at different stages of scale.

**BEAUCHAMP:** One of the things I was attracted to about the beauty industry is it doesn't respond to changes in the economy. It's always strong.

But I think one of the things I underestimated was trying to say, "Well, things are going to change. Come with it. Let's change together," proved to be really hard. Really hard.

**HOFFMAN:** Birchbox was up and running, and making the most of its first-mover advantage. But very soon competitors small and large were imitating the Birchbox model.

**BEAUCHAMP:** It was so terrifying. We were seven months in, and a business ran by the Samwer Brothers, who are famous for copying American businesses, raised over \$30 million to create copycats all over the world for Birchbox. And then later Amazon and Allure Magazine joined forces to also launch a competitive product. And everything you can imagine happened, we were so scared.

**HOFFMAN:** Once your unconventional new vision becomes obvious to everyone, then, obviously, you get copied!

Once you launch an innovative business model that proves itself, you will face a deluge of competitors – startups and existing brands. The doorbell to your party of one will start ringing incessantly, and it will open up to a motley crew of unwelcome gatecrashers.

**BEAUCHAMP:** We were talking to lawyers. Is there anything we can do? Of course there's not. There's nothing you can do. And I think what saved us was being so overwhelmed by demand that though we could look, we couldn't dwell. We had to take the gifts and the challenges of being the first mover and run as fast and hard as we could. And fortunately that I think really did benefit us, just focusing on what we were doing for a long time.

**HOFFMAN:** This is why you can't rely solely on first mover advantage, especially if your product is a business model that can't be kept as a trade secret. As soon as you start moving, your competitors will see where you're going – and be hot on your heels.

But at first, Katia didn't see this obvious risk.

**BEAUCHAMP:** We had really focused on trying to create a business model that was sustainable for us and that made sense for our brand partners. But as competition came into the market, they were just throwing money at the situation to get supply, which we were really dogmatic that that's not the way this should work because we are investing in creating customer acquisition through a sample. So there was a tipping point on the

supply side when all of a sudden samples became things that were for sale because they really hadn't been prior.

**HOFFMAN:** Competitors started paying for samples, instead of getting them for free. Katia could have followed them. But this went against the Birchbox model, or so it seemed. It would drive up her costs. But Katia was determined to keep the magic of her approach alive.

**BEAUCHAMP:** We had to get really creative, we had to get to know all the sample manufacturers in the world that you could imagine, we had to get brands who weren't sampling, sampling, we had to get brands who were sampling, sampling more. So we were super focused on dealing with supply because we had no issues with demand.

**HOFFMAN:** Then, beauty giant Sephora jumped onto the sample box bandwagon. I asked Katia how that felt.

**HOFFMAN:** And so when Sephora launched a competitor, because you get these intense high quality brand now coming straight at you with this stuff, it reminded me of one of the things that my friends who went into entrepreneurship did before I did, which is he sent me a one-line email saying, "Welcome to where 15 minutes is the difference between exaltation and terror." "We're going to make this whole industry work. Oh my God, we're going to die." What was the reaction and the thinking to Sephora?"

**BEAUCHAMP:** Yeah, I think you're right that Sephora really represented a moment. I thought this is a really bad business model for Sephora, and let me tell you why. Sephora is the destination for the obsessed beauty consumer, and they are Anna Wintour of beauty. They anoint the trend, they set the trend. They are for people who want to be early to trends, on trend. That top 20% of consumers who's obsessed, Sephora is their haven. And the interesting thing about that consumer is that they want to consume, and they want to consume fast. "Don't slow me down. I'm here to buy a \$25 mascara. I'm ready to buy."

And I thought this is not the product for them because they are going to put a speed bump in front of the most obsessed consumers, and instead of jumping right into a \$25 mascara, they're going to spend \$10 and then think, "I don't know if I want that mascara." And I thought it's a bad move. That's what I thought. But I also thought, "This is so annoying because customer acquisition cost is going to go up."

**HOFFMAN:** People will take your vision and run with it in what may seem to you like the wrong direction. If this means they fail, then hey, that's one less competitor. But if it means they are endangering your entire business model, then you have a fundamental problem. And this is what Katia was really concerned about.

**BEAUCHAMP:** It created supply challenges again. Everyone's going after the same samples. And Sephora has so much power in that dynamic and telling people not to

work with us or all sorts of things that were fun. And now, in order to have better product and compete on having a great product for consumers, our cost of goods were going up too.

**HOFFMAN:** Now I would argue that this is the part of the story where Katia's passion for her vision gets the better of her. Recall what Katia said before about when they came up with the Birchbox model:

**BEAUCHAMP:** In 24 hours, we had the business model that is honestly the business model you see today. It was founded on the concept of bite-size discovery that's personalized, plus content, plus e-commerce – and the idea being full-funnel to generate demand and capture demand and blinders. I know I had really bad tunnel vision after that.

**HOFFMAN:** That tunnel vision had made her blind to the obvious realities of the market. She firmly believed that a fundamental part of this new business model was sourcing samples for free from suppliers.

The rise in costs was destroying Katia's vision for the business model. And more immediately, it was threatening to destroy her business.

**HOFFMAN:** So what did that cause for you and for the business? How did the retrenchment go?

**BEAUCHAMP:** I mean it was so painful. It went from really resisting, anger, denial, “This isn't fair,” to “I think I might be earning my stripes moment,” to “Okay, Katia, you signed up.” And the one thing I said, I mean believe it or not, was that I just really dreamt of building a forever business. I just really, really was interested in the substance of something that could last and that wasn't just a here today, gone tomorrow thing, a fad. And so I thought that's what this is. I mean anybody who's trying to build a forever business, whether they reach these inflection points earlier or later, they reach them.

**HOFFMAN:** There's a big difference between a forever business and a static business. And forgetting this is deadly. Because a business that stops evolving will wither. Katia tried to deal with the new reality of increased costs, and she was determined not to pass them on to her customers. So it meant making painful cuts in other areas.

**BEAUCHAMP:** It was obviously making cuts, changing the spend in the business dramatically, cutting the team, a few rounds of layoffs. It was also bringing in new talent and rethinking our approach to things. We cut into the bone of things that we then realized wasn't okay, and then that led me to fall out of love with the product.

**HOFFMAN:** This came at a particularly difficult time for Katia personally.

**BEAUCHAMP:** I found out I was pregnant. And then I ended up having this complication, I had to move to the hospital for a hundred days away from my family. And it was dark. And I think it was just this incredible lesson of, "What are we all doing here? Why are we doing it?"

**HOFFMAN:** I talk a lot about the Valley of the Shadow that, as a founder, you'll need to pass through at least once – and probably multiple times. For Katia it was a transformative experience.

**BEAUCHAMP:** And I had this realization that everything bad that had happened at Birchbox was this gift. And I started to mentally thank all of these people who I had been angry at, just for the gift of my career, for this gift of even getting to try. And I just felt so grateful to be alive, facing potentially dying in childbirth. And I emerged really dedicated to not hate hard things. I just needed to see this as, this was when exponential growth always came. And so, "Hi, welcome. Welcome, bad day. Welcome, horrible month. Welcome, impossible thing." I don't know what's on the other side, but I am going to be better on the other side.

**HOFFMAN:** Katia and her team took the bold move to refinance the company. But their new majority investor brought something more important than money to the table.

**BEAUCHAMP:** So a minority investor became a majority investor, Viking Capital, they're some of the smartest people I've ever worked with, and they just looked at me, and they just said, "You got to change the price." And I was like, "We can't change the price. The whole market's at this price. That's going to kill us. That's going to be the nail in the coffin." And they said, "You have a brand, and a powerful brand becomes more powerful when they prove they can take price."

**HOFFMAN:** This investor was saying the costs of your business are higher than you'd expected, and so you have to pass on that higher cost to consumers. You have no choice. It was the obvious move to make. But Katia was worried that it would destroy her business model.

**BEAUCHAMP:** In I think four or five months, we changed the price 50%. And that was so scary. And that allowed us to build something that we were proud of and to start this journey of building back the heart of the business, and it's been the best part of the experience for me, which is a really strange thing to admit.

**HOFFMAN:** Was there any particular moment, because I love your language on this, where you fell back in love with the product? Was there some point where you went, "Ah, we're back."?

**BEAUCHAMP:** I started to understand what the market was valuing, what the specific casual consumer was valuing.

**HOFFMAN:** Katia's adjustment, at the darkest moment for her company, worked. The Birchbox model helped flip the magnetic poles of the beauty industry, and then Katia adjusted that model again to keep the magnetic field in place.

**BEAUCHAMP:** The gravitational pull used to come from the companies and the brands, and that's the way industry used to work, and like it or not, the gravitational pull now comes from consumers. I think that's exciting.

**HOFFMAN:** It may seem obvious that consumers come first. But all successful business-model flips seem obvious in hindsight. The power of Birchbox's change in polarity was illuminated anew when the Covid pandemic hit. Online beauty purchases jumped, and so too did demand at Birchbox.

**BEAUCHAMP:** All of a sudden there's this surge in demand. It was whiplash.

I think if there's one thing that we could all agree on from the pandemic, consumers can change their behavior incredibly quickly. And it's powerful to see that and know that, and that gets me excited.

**HOFFMAN:** Katia's words are a reminder that, even in the most turbulent of times, an unconventional idea can capture people's imagination – and inspire hope for the future.

I'm Reid Hoffman. Thank you for listening.