

The definitive guide to freemium pricing

Booklet



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Introduction to freemium pricing

Freemium pricing is a business strategy where a company offers their basic products or services to users at no cost and then charges a premium for supplemental or advanced features. The term “freemium” was coined in 2006 and came from a combination of the words “free” and “premium.” Although, the business model has been in use by software companies since the 1980s.

A freemium strategy is uniquely positioned to combine well with almost any other pricing model and can be used to build innovative, customer-centric approaches to billing. Many freemium software products utilize in-app purchases, ecommerce plug-ins, and targeted ad space to supplement earnings made from premium tiers. Not every business is suited to using a freemium model. Still, by exploring the wide variety of ways it’s applied to other industries, you can discover new methods and inspiration for your pricing model.

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A quick glance at the pros and cons



Low barrier to entry



Exponential growth



Low acquisition costs



Expand brand awareness



Minimal marketing budget



Multiple revenue streams



Collect user data



Increased operational costs



Requires huge user volume



Low conversion rate



Reduced value perception



Limits pricing of paid tiers



Higher churn rate

Understanding the **pros** of freemium pricing



Low barrier to entry

Little stands in the way of users signing up since they can access the products or services for free, making it easier to engage with your offering.



Exponential growth is possible with excellent strategy execution

The model can handle a massive volume of customers. As you build an extensive pool of active leads, you will have access to people already signed up for your services to upsell more advanced features and packages.



Customer acquisition costs are lower

It's easier to upsell your premium tiers to customers that already use the free model and scale with them as they develop brand loyalty.



Expand brand awareness

You will naturally grow your audience as more and more customers interact with your products or services. Like a pricing penetration strategy, a freemium model will allow you to cut through market saturation to effectively capture and upsell your audience.



Save on marketing expenses

You can significantly reduce marketing costs, especially if you're tapping into a newer market to source your customers. Freemium users are a great asset for word-of-mouth promotion.



The freemium model creates multiple revenue streams

It's still possible to generate revenue from elements like ads and in-app purchases to support the earnings from your main products and services.



Collect user data and utilize free beta testing

Data like this allows you to gain feedback that will help fine-tune your pricing tiers and marketing to attract the right buyer personas.

Understanding the **cons** of freemium pricing



Operational costs are higher to support offering a premium product for free

You will need to budget appropriately to maintain quality through an influx of not-yet-paying customers.



Return on investment (ROI) requires enormous volume

Freemium models rely on an astronomical number of active users to generate revenue.



The conversion rate is usually lower

Customers of all kinds are attracted to trying out the free version, perhaps resulting in lower conversions on higher tiers. A substantial portion of your users may not fit your buyer personas.



Customers might undervalue your offering

You may unintentionally educate the market that it's worth a lower price by marketing it as free.



Lower conversion rates often necessitate lower-priced premium tiers

Appropriate pricing is essential to upselling customers who are used to the free version. You also don't want to be combatting sticker shock.



Churn rates can be inflated

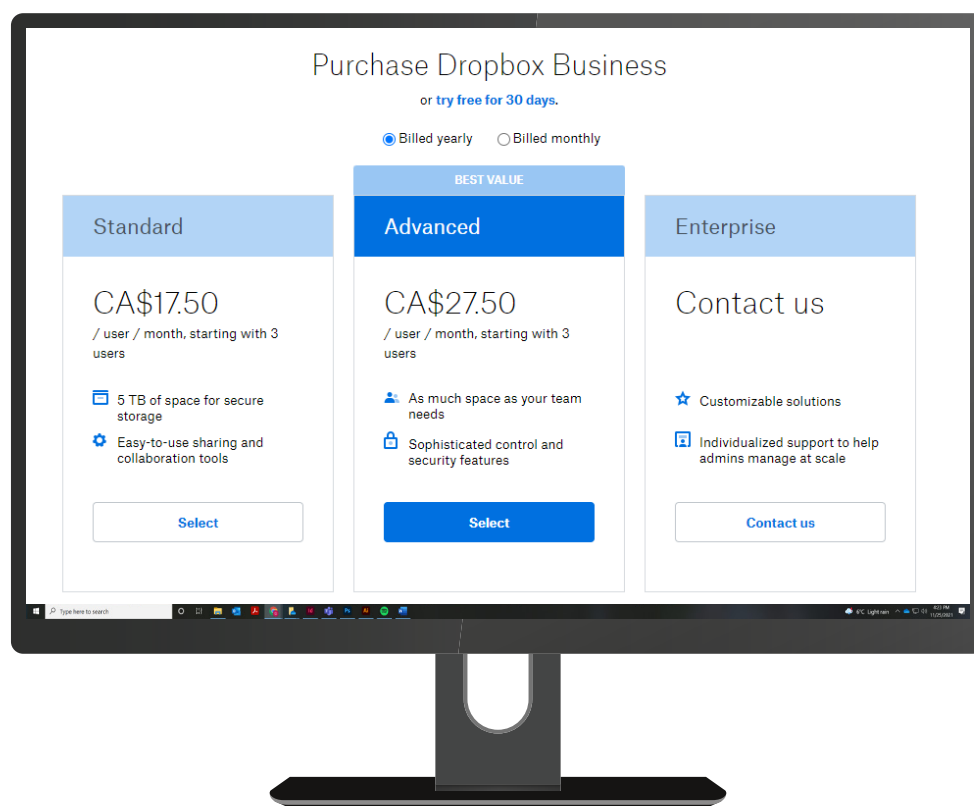
Potential customers might be turned off if your offering isn't extremely easy to use, and even customers who've decided to use your product or service might abandon your free version if they become bored with it. Casting a wide net will bring you more customers but will not guarantee stickiness. Confusing or complex elements are best kept for paid tiers where customers are already invested in learning.



Traditional freemium pricing (with example)

Traditional freemium pricing consists of an introductory free tier and a few paid tiers. Unlike a free trial or a demo, the free tier is available to the customer for free forever. Many companies will limit the functionality of the free tier to conserve their resources and direct their customers towards the premium tiers.

Dropbox is a file hosting service that offers cloud storage, file synchronization, personal cloud, and client software. They provide a basic free tier and then two upgraded plans that include more storage and users for personal use.

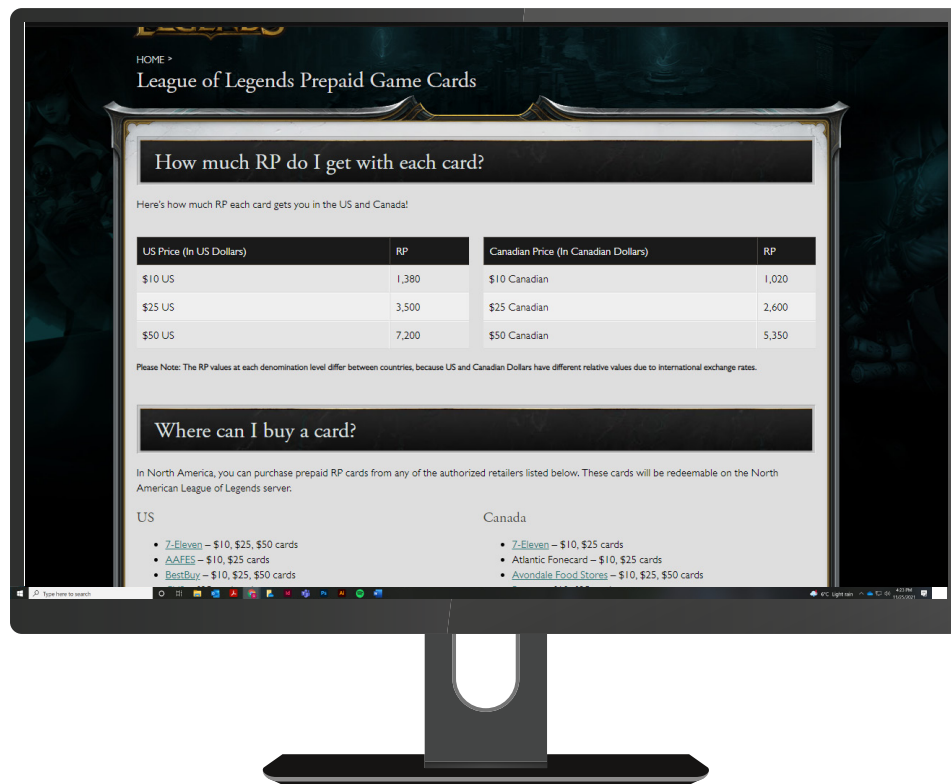


Freeware (with example)

Freeware refers to the practice of offering a fully functional product for free forever. The term comes from combining the words “free” and “software.” This pricing strategy has led some companies to tremendous success in the video game industry. Free online mobile games are often ad-supported, and many developers incorporate in-app purchases into their games for players to customize their characters or gain better in-game equipment.

League of Legends, often shortened to “League,” is a multiplayer online battle arena (MOBA) video game developed and published by Riot Games. The game is exceedingly popular with 150+ million registered players and about 120 million active daily users. In 2020, League generated \$1.75 billion in revenue.

One of Riot Games’ more lucrative revenue streams involve players purchasing Riot Points (RP), which work like in-game currency to buy specific “champions”, items to enhance their gameplay, or changes to the appearance of their character known as “skins”. Although many of these elements can be earned through completing challenges and milestones in-game, many players treat them like collectibles and would rather speed up the process by spending RP.



Land and expand (with example)

The land and expand strategy is a staple of the SaaS market, where a product or service is offered for free with account sign-up. When the customer reaches a specific threshold limit, the company then monetizes the product/service. Unlike in other freemium models, the free offering is usually a teaser for other goods and services.

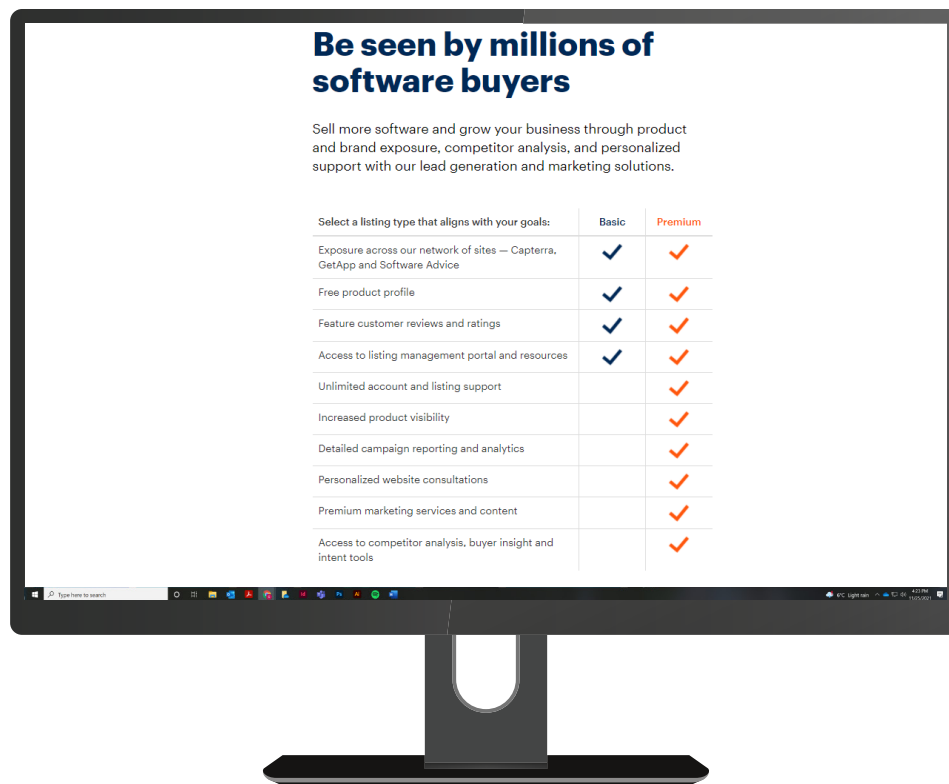
Yammer was an enterprise social networking service used for private communication within organizations and a historic example of a land and expand strategy. Yammer Basic was a free, smaller version of Yammer Enterprise for individual use. In 2017, Microsoft began to phase out Yammer Enterprise and re-integrate the network into Office365. At the height of its popularity, Yammer's conversion rate reported 15-20%.

Yammer Basic standalone	\$0
Yammer Enterprise standalone	\$3 per user per month
SharePoint Online (Plan 1) + Yammer Enterprise	\$4 per user per month
SharePoint Online (Plan 2) + Yammer Enterprise	\$8 per user per month
Office 365 E Plans 1–4 + Yammer Enterprise	\$8–\$24 per user per month

Ecosystem (with example)

Ecosystem pricing is when a company offers their base product or service for free forever and relies on revenue made through deals with third-party developers. Ecosystem models often work when your offering is the missing link to connect buyers with sellers and facilitate partnerships.

Capterra is a free online marketplace vendor that serves as an intermediary between buyers and technology companies within the software industry. They help customers select software by providing them with user reviews and research. Vendors pay Capterra whenever they receive web traffic and sales opportunities earned through the ecosystem, allowing buyers to use the service for free.

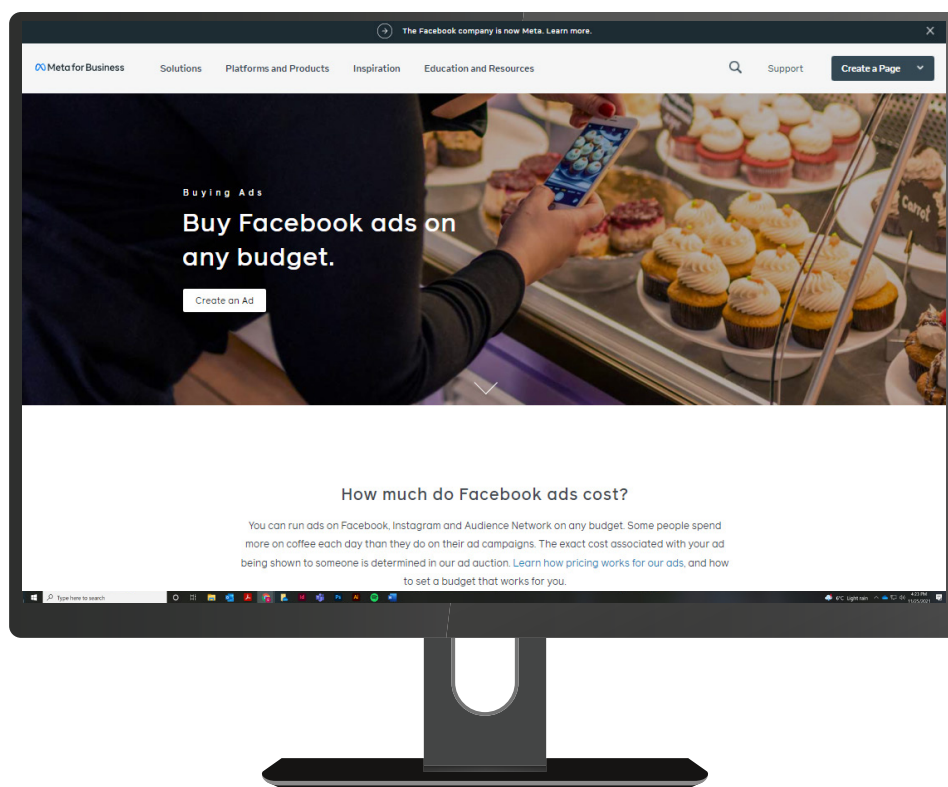


Network effect (with example)

The network effect is a type of pricing strategy where a company monetizes customer traffic and behavioural data. This can be done either through directly selling user data to third-parties or selling ad space for personalized ads—marketing that's tailored to a specific buyer persona constructed from user data.

Meta, previously known as Facebook, is a technology conglomerate and parent organization for social network subsidiaries Facebook, Instagram, and WhatsApp. Users gain free access to these products, but upon sign-up, also agree to permissions allowing Meta to share their user data with third parties and to receive personalized ads.

Meta for Business allows vendors to purchase advertisements to be displayed across one or more of Meta's daughter companies. When creating an ad, you can choose the objective, target audience, platforms, budget, and format. Meta's algorithm will then analyze user data and exhibit your ad in accordance with your selected goals. You can also manually track performance and edit your campaign in Ads Manager to ensure optimal outcomes.



Revenue recognition for freemium pricing



Freemium pricing strategies generate multiple revenue streams, so it's vitally important that you can correctly attribute earnings during revenue recognition. Errors in revenue allocation data can have wide-reaching consequences on your ability to make strategic, data-driven business decisions.

You could be left unsure of how much each revenue stream is generating and lost on how to handle third-party advertisements or in-app purchases. Not to mention without a robust recurring billing solution in place, it's much harder to maintain compliance with accounting standards like ASC 606 and IFRS 15.

Managing the complexity of freemium pricing

Avoid subpar management of your freemium strategy by familiarizing yourself with these three critical elements of the pricing model that will aid your growth journey.

The 3 critical elements of your freemium pricing strategy

1. Appeal to mass markets

To achieve a successful freemium model, you will need considerable volume, so your business must attract as many customers as possible. Freeness is often not enough. Your offering needs to be extremely easy to use and create increased customer stickiness. Invest in excellent quality assurance and user experience.

2. Balance resources and budget

Even at peak performance, the freemium pricing strategy demands higher operational costs to provide premium-level quality to not-yet-paying customers. That's why you must balance your resources and budget to forge a sustainable business model that can weather market fluctuations and higher churn rates.

3. Manage multiple revenue streams

A powerful recurring billing solution can automate revenue allocation while simultaneously helping you remain compliant with accounting standards like ASC 606 and IFRS 15. Tracking which earnings are being generated by what revenue stream doesn't have to be complex. The right system will also streamline any additions to your pricing model or updates to your customers' invoices, providing you with optimal agility to adapt to changes in the market.

Introducing Subscription Billing Suite

A comprehensive solution for billing, deferrals, and recognition that streamlines the entire quote to cash process at every step from billing and invoicing to reporting and forecasting. It provides consistent and reliable invoicing for a wide range of pricing models and allows you to take control of your pricing and billing schedules at the line-item level within Microsoft Dynamics 365 for Finance and Operations, Microsoft Dynamics 365 Business Central, and Microsoft Dynamics GP.

What our customers say

“ Wonderful, wonderful, wonderful. A joy to work with Binary Stream. Everyone was super helpful and positive, which had a big impact on the success of the implementation.



“ What makes Binary Stream different from other software companies we have worked with is their ability to truly listen to customer input and enhance their subscription solution to meet those needs.



“ Since I have come on board, Subscription Billing Suite has paid for itself more than once over. Having this solution to help us manage over 10,000 deferred contracts is an essential part of our financial processing.



“ I've long been a fan of Dynamics, and Subscription Billing Suite met and exceeded every feature of our previous solution. However, the factor that made this project a success is having a partner who augmented our internal integration efforts.





Start your subscription billing journey today

Learn more by reading our complete guide to subscription management, offering insights into billing models, pricing page psychology, and plenty more.

[Discover more](#)