Chapter 6 – Notes

Opening Case: “Ad World”

- Startup wants to be a **B 2 B marketplace** matching firms ↔ ad agencies.
- **Wrong question**: “Which side should we charge to list/post?”
  Charging **at entry** adds friction → fewer listings, fewer matches, less data.
- **Better approach**:
  - **Subsidize onboarding** (tools, scraped starter profiles).
  - **Charge on success** (performance-based **completion fee**).
  - Consider **ancillary value**: e.g., **paid loss analysis** for agencies (why their bid lost) → recurring revenue, improves ecosystem quality.

Core Problem: Monetizing Without Killing Network Effects

- Charges can suppress participation:
  - **Access fees** → fewer users; **usage/production/consumption fees** → less activity/value.
- **Free** can jumpstart networks, but platforms must still capture value to survive.
- **Classic “free” models**:
  - **Razors–blades / device–consumables** (story debated historically, still a useful metaphor).
  - **Freemium** (free tier + paid upgrades).
  - **Two-sided pricing** (subsidize one side, monetize the other). Requires controllable link between sides (Netscape’s browser→server plan failed).

What Value Are We Capturing? (4 “Excess Value” Buckets)

1. **Access to value created** (consumers): YouTube videos, Android apps, Skillshare courses.
2. **Access to market** (producers): Airbnb hosts to travelers; LinkedIn recruiters to candidates; Alibaba sellers to buyers.
3. **Access to tools/services** (both): Kickstarter fundraising; eBay+PayPal storefronts.
4. **Access to curation** (both): Better matching = less search cost, higher relevance.

> Strategy: Identify where **excess value** exists and capture a **slice** without harming growth.

Not Just “More Users”: Quality & Monetization

Zvents (Local events)

- Huge traffic and **completeness expectation** meant no leverage to charge organizers.
- Paid prominence yielded only a **trickle**. Sold to eBay (StubHub).

Lesson: Large audience ≠ monetizable if the **value must be complete** and you lack a control point.

Meetup (Offline groups)

- Tried multiple models (lead-gen to venues, ads, premium)—weak results.

- Faced **negative network effects** (low-quality, noisy meetups).
- Moved **from free to fee**: charge **organizers** (~$19/mo) → activity down **95%**, but **success rate** up massively (quality ↑), and monetization works.

Lesson: Pricing can **reduce noise** and **improve quality**, strengthening net network effects.

Monetization Patterns

1) Transaction Fees (take rate)

- Charge per **completed transaction** (percentage or flat fee).
- Pros: Low entry friction; aligns with value realized.
- Risks:
    - **Disintermediation** (take interaction off-platform).
    - Mitigations: **Standardize** offers (Groupon), **ratings/trust** (Airbnb, Fiverr), **workflow + monitoring + payments** (Upwork time tracking; Clarity call billing) to **own the transaction**.
    - Local, simple services (plumbing/painting) are harder → may need other models.

2) Charging for Access (to a community)

- **Third parties** pay to reach users gathered for **non-commercial reasons**.
- Examples:
    - **Dribbble** jobs board (companies pay; designers stay free). Enhances core value.
    - **LinkedIn** recruiters/tools. More profile updates → healthier graph.
- Rule: Access monetization must **enhance**, not degrade, the core interaction.

3) Charging for Enhanced Access (placement/targeting/tools)

- Producers pay for **visibility** or **lowered barriers**.
- Examples:
    - **Yelp** premium listings; **Google Ads**; **Twitter/Tumblr** promoted content.
    - **Dating sites**: pay to unlock messaging/identity/contact.
- Guardrails:
    - **Transparency** (clearly label paid vs. Organic).
    - Avoid perceived **value clawback** (e.g., reducing organic reach to force ads).
    - Apply **curation standards** to paid content to prevent relevance decay.

4) Charging for Enhanced Curation (quality guarantee)

- When abundance overwhelms users, they'll pay for **quality filters**.
- Examples:
    - **Sittercity**: parents pay subscription; platform invests in **screening**.
    - **Skillshare**: per-class purchases **and** subscription for curated catalog; teachers earn "royalties."

Whom to Charge? (Heuristics for Two-Sided Pricing)

- **Charging everyone**: Rare; can work when fee **curates quality** (exclusive clubs). Use sparingly online.
- **Charge A, subsidize B**: When **A values B** more than vice versa (e.g., Ladies' Night; many dating sites).
- **Subsidize stars**: Attract **super-producers** (celebrity teachers, AAA game studios) to pull demand (e.g., EA on Xbox; malls discount anchors).
- **Price-sensitive side**: Subsidize the **more elastic** side. Context matters (e.g., Denver vs. Boston rental markets flipped who pays).

- **Workarounds**: If ideal model is impractical, **engineer incentives** (Alibaba early **membership fees** + big **sales commissions** to offset friction; later monetized via ads).

Designing for “Free → Fee” (Transition Principles)

- **Don’t charge retroactively** for value users already got for free (or cut free value) unless your network is strong enough to withstand backlash.
- Instead, **add new value** that merits a fee (and **guarantee** it—e.g., safety checks if you charge “safety”).
- **Architect for monetization from day one**:
  - If you’ll take a **transaction fee**, design to **control the transaction** (payments, workflow, dispute resolution).
  - If you’ll sell **access**, control **distribution and data**.
- **Monetize after value is proven** (“you never take first money”), but plan ahead so options stay open.

Quick Decision Checklist

- **What excess value** are we creating (access-to-value, market, tools, curation)?
- **Where can we charge** without throttling interactions?
- **Which side** is more **price-sensitive** / which side **creates pull**?
- How do we **prevent disintermediation** (own communication, workflow, trust, payments)?
- Will pricing **improve quality** (reduce noise) or **add noise** (paid spam)?
- Is the fee **aligned with success** (completion- or performance-based)?

Takeaways

- Platforms create **excess value** in four ways; monetization is capturing a **slice** without harming network effects.
- Viable models: **transaction fees**, **access fees** (third parties), **enhanced access**, **enhanced curation/subscription**.
- **Two-sided pricing** is context-specific: choose who pays, who’s subsidized, and **why**.
- Design choices **enable or block** future monetization—**plan early**, charge **later**, keep options open.