How to build an effective pricing strategy

Leading founders and investors talk about how to build an effective pricing strategy

Pricing is top of mind for many startups. In our recent survey of more than 1,500 founders and business leaders, we learned that 80% of leaders believe recurring revenue is more important than ever, and 40% are planning to evolve their pricing model in 2024.

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But figuring out pricing for a software startup is tough. There's a lot to think about, from changing user expectations and monetization to packaging and distribution. Whether you're just getting started or wondering how to iterate in the current market, we've created this guide to help guide software founders like you through the journey of pricing your product.

The guide is built around interviews with top venture investors, software founders, and Stripe employees, and is organized around five phases of the pricing journey:

- Customer discovery in order to build up a rounded picture of who your customers are
- Creating your value proposition so that those customers know you're addressing their problems
- Figuring out how to price your product
- Packaging your product into something purchasable
- Learning how an investor might assess the quality of your pricing strategy

Each section begins with a brief overview, followed by excerpts from interviews with experts about that stage of the pricing journey.

Key Takeaways

If you only have a few minutes to spare, here are the key takeaways from the interviews:

- **Customer discovery and pricing are continuous processes:** Don't underestimate the amount of work that goes into identifying and understanding a customer demographic and its pain points before you think about building the solution. But even once you have a product in the market, and even if you reach product-market fit, the market and the customers within it are in a constant state of flux. Your product and pricing will likely need to evolve as the market's needs and expectations change.
- **Your pricing says a lot about your brand:** The price of your product is a signal of quality. Customers often place lower value on something they're getting for free. If you're giving away products or services through a freemium model or at a very low cost, this can be detrimental to your brand perception if engineered in the wrong way. Inversely, if your product is expensive, customers will have higher expectations.
- **Your pricing strategy heavily influences how you build your business:** You can't build a bottom-up, product-led growth business if your pricing involves multiyear, high-value contracts. The way you build your go-to-market strategy and hire a team around it will be heavily influenced by the price of your product, as well as the type of buying process it invites.
- **Economically quantify user pain points and align your price to the realized value:** An effective pricing strategy successfully aligns the price of your product with the value a customer extracts from using it. If your product is an essential component of a process that leads to thousands or even millions in savings or new revenue for a user, you're leaving too much money on the table by charging them $10 a month. Aim to extract 10%–15% of the economic value your product delivers.
- **Complexity kills:** Complexity in your product and pricing is sometimes wrapped under the guise of optionality. Understanding all of those options often requires a high amount of effort from the customer to read, research, and think. Many customers simply won't do that, and therefore they'll likely miss out on pockets of value that your product brings. Keep things simple in the early stages.

Customer Discovery

Great products are born from the most acute user pain points—you need to intimately understand a problem before you can build the optimal solution.

Configuring pricing requires a similar mindset. You need to identify and understand a customer demographic and its pain points, and then be able to economically quantify those pain points. This all starts with customer centricity and market research.

An interview with Nick Telson

Nick Telson-Sillett is the cofounder of Trumpet and Sequel. He previously exited his first startup, DesignMyNight, in 2019 for $30M+. Sequel allows the world's best athletes to invest in the world's best startups, and Trumpet helps global sales teams close deals faster with digital sales rooms. As a multi-founder, Nick has had a lot of experience deeply understanding a problem before building a solution.

In our interview we talk about the process behind customer discovery, and how to build an effective understanding of the problem before you build the product.

Nick Telson-Sillett
cofounder
Trumpet and Sequel

Before your product was in the market, how did you gather the user insights and feedback that influenced how you thought about building and pricing your product from Day 1?

I always start with my experience. Is this a pain point I've personally felt, or observed through someone close to me? If you just set out to solve a problem, without directing your thinking, the universe of opportunity is so endless you often struggle to land on something that you're uniquely positioned to solve. Prior to Trumpet, I founded and exited DesignMyNight, a discovery and booking platform for people looking to plan a night out. I used the experience of building DesignMyNight as a starting point, which eventually became Trumpet. We ran DesignMyNight for 10 years, and often noticed the sales process from outreach all the way to deal close wasn't optimized. This thinking is what brought us to Trumpet.

Once we identified the problem space we were curious about, we kicked off the concept phase. Here we captured everything we thought about this problem into a single page, documenting what we're trying to solve, and a very high-altitude view of the potential solution. Using this document, we tried to dissuade ourselves from the idea in every possible way. A lot of founders try to do the opposite: they'll often go out into the market and try to confirm that their intuitions and assumptions are correct. We wanted to prove ourselves wrong.

How did you gather feedback on this early concept?

We sent the one-page overview to sales leaders, mostly via cold outreach, asking them for their thoughts: "why this was a bad idea?", "what negatives do you see here?" By avoiding open-ended questions like "what do you think of this?" and specifically angling for the negatives, we could cut directly to the potential objections. All of this feedback ended up living on Notion.

A tactic we used to increase the success of our cold outreach was to offer asynchronous and synchronous feedback. We gave the person the option of completing a short form, indicating how long it would take to fill out, or to book a call directly with us to talk through it. Cold outreach is hard, and there's no silver bullet here, so we just had to do the hard yards. We found that the people you gather positive feedback from also become your waitlist and early adopters further down the line, so it's worth spending the time to find the right people to gather feedback from.

What if no one likes your idea?

If an overwhelming amount of feedback you receive is negative, perhaps rethink the idea. Thankfully a good portion of the feedback we received was positive, so we took our thinking to the next level. This involved expanding our one-page document into a multipage document, adding a deeper dive on what a minimum viable product (MVP) would look like. We circulated the more detailed document with the most responsive and excited people we sought feedback from previously for another round of opinion gathering.

> "We spent months gathering feedback. It informed the product we built, who we built it for, and enabled us to build up a waitlist of eager adopters."

How did you think about the value of the problem you were looking to solve?

When it came to economically quantifying the value of our potential product, we relied heavily on our gut. Most companies in the world have some sort of sales team, and we knew this was a big idea. We felt that unless we were going after a niche market, where the user profile was really, really specific, we didn't need to spend endless hours analyzing the market. It was only when we went to raise money from venture investors that we really had to be more specific about the market size and potential value.

How long did you spend gathering this feedback?

We spent months gathering feedback, and it's worth mentioning we didn't even have a logo or a company name at this point. We felt as soon as you landed on a name or logo, you anchored your thinking. Without a name or logo, you're more easily able to evolve your thinking as new feedback comes in. Our feedback informed the product we built, who we built it for, and enabled us to build up a waitlist of eager adopters.

> "We spent months gathering feedback. It informed the product we built, who we built it for, and enabled us to build up a waitlist of eager adopters.

Creating your value proposition

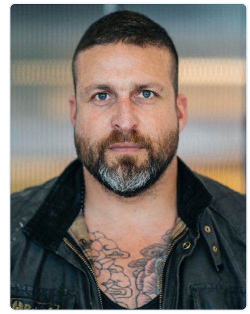
Once you have a good understanding of who you're building for, you can think about how to position your product and articulate its value.

Positioning is all about creating context around your product and the value it brings to users. It's often handy to differentiate between the company you're targeting and the individual operators within that company—who will be either the buyer or user of your product. How you describe your product's value at the company, manager, and operator levels might be different.

Articulating your value proposition is a nonnegotiable step toward pricing your product. It's certainly not fixed, it evolves as your product improves and your understanding of the user gets more sophisticated. How you communicate your product's value proposition speaks to the needs of your user, the value you deliver, and the quality of your brand. All of this is a precursor to pricing.

In this section, we interviewed two venture capitalists to gather their observations on the importance of brand and customer discovery when building your value proposition.

An interview with Gabbi Cahane



Gabbi Cahane
partner
Stride.vc

Gabbi Cahane is a partner at Stride.vc. He has spent almost three decades branding, building, and backing companies—from early-stage startups to global megacorporations—as a founder, funder, strategist, and storyteller. He was previously cofounder of the strategy firm Multiple, advising startups such as Pipedrive, Curve, TrueLayer, and WeTransfer, as well as funds such as Kindred Capital, Connect Ventures, and 2150 across brand, culture, growth and fundraising. He is a board member of Knowunity, Anotherblock, Screenloop, and DeepOpinion.

In our interview, we discuss how to think about the relationship between your customers, brand, and pricing.

When building a value proposition, where do you start?

It all starts with your brand. Brand is everything you make, say, do, or provide. It's a constant work in progress, so we like to think of it more as a sense of narrative. It's a story that has a beginning, a middle, and an end. Stories have the flexibility to develop over time. They're not brittle or fixed; they can evolve.

Your brand, your product, and your pricing are tightly linked. These elements can't be built in isolation; it's the customer that brings them all together.

A lot of founders and investors talk about an Ideal Customer Profile (ICP), but we like to think of it a bit differently. We talk about your Disproportionately Influential Customer. This could relate to the role they play in decision-making, budget control, or the reach they might have. These are the "yes" or "no" people.

It's critical to define this individual precisely. It's less about the number of them, and more about the quality of influence that they actually have on the ability for your product to succeed in an organization you're looking to work with.

Once you feel like you have an understanding of who this Disproportionately Influential Customer is, how do you go about gathering insight?

There are no hacks here. You simply need to spend as much time as possible in a room with these influential customers. You'll need to graft outbounding them, tapping up your networking, speaking with them, and really just building relationships. This takes time, and it can't be skipped.

To help make things easier, you can ensure your question set is relevant, powerful, and useful. Be aware of confirmation bias. You shouldn't be asking questions or looking for information that confirms your assumptions—instead ask the questions that seek to prove you wrong.

Some of your questions will be rational. What do they look for when considering a solution like yours? What features do they require? Which team members will be most active in the product? We call these things the "reals." The bigger challenge is how you figure out the "feels." This isn't about what your product functionally does, but what it allows them to do. Even in B2B, you're always selling to people. These people have their own challenges, goals, and ambitions. How does your product help them achieve that? And what does choosing your product say about them? Are they an innovator? A steady pair of hands? Someone that's driving the business forward? There's a lot B2B can learn from B2C here.

Ensuring you develop a sophisticated understanding of both the rational and emotional purchase factors enables you to more clearly articulate the product's total value to this influential customer.

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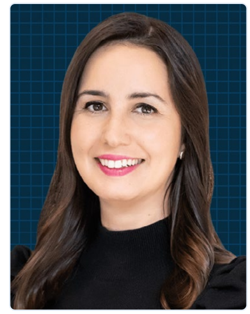
Further thoughts from Tugce Erten

Tugce Erten works for **Andreessen Horowitz**, a venture capital firm, where she helps its portfolio companies think through product pricing and packaging strategies. Prior to a16z, Tugce was an operator at large companies such as Atlassian and PagerDuty, where she focused on strategy, pricing, analytics, and operations.

In our interview we explore how a value proposition might evolve once you see how a customer is using your product.



Tugce Erten
partner
Andreessen Horowitz

How have you seen founders in your portfolio approach defining their product's value proposition?

Generally the founder starts with a hypothesis around the problem they're trying to solve. In reality, you'll likely never get this right the first time. For example, maybe the starting hypothesis behind Uber was the ease of ordering a black luxury car, and enjoying that experience. But then, when the product got into the people's hands, the value turned from luxury transportation to simply getting from A to B. The value flipped to saving time, rather than having an experience.

This pattern is common for many founders and their products. The recommendation here is to come up with an MVP, get it into people's hands, pay close attention, and be open about asking them what value they're getting from the usage.

Even with established companies, people might end up using your product in totally different ways. Atlassian started JIRA as a bug tracking tool for software developers. Eventually, they saw IT and customer support teams using it, which inspired them to create an entirely different product called JIRA Service Desk, tapping a totally different market with a different pricing structure and user persona.

This was only made possible by constantly talking with customers in order to unlock the value that you're not seeing.

While gathering this feedback, keep in mind that different personas and company types will observe value from different angles. While enterprises may care about security, availability, and reliability, startups might be more concerned with speed and costs. Each of them will likely deliver feedback through a lens that matches their company objectives, and it's on you to acknowledge that and react accordingly.

Figuring out your price point

Understanding the relationship between cost and value is central to an effective pricing strategy. You can't achieve product market fit without a price point that's agreeable to potential users.

Finding a sensible starting price point is all about weighing the tradeoffs between your competitive dynamics, underlying costs, and the economic value your product creates for users.

Figuring out your price point by looking at value, competition, and underlying costs is really just about understanding the general bracket in which your pricing should fall. Patrick Campbell, the founder of ProfitWell, said it best:

“You should first be figuring out the range you're in: a $10 product, $100 product, $1K product, etc. Don't waste time debating $500 vs. $505, because this doesn't matter as much until you have a stronger foundation beneath you.”

Focus on the order of magnitude to begin with. As you develop a better understanding of your users, and how they're taking value from your product, you can slowly iterate towards a more sophisticated pricing model. These are some of the most important pricing vectors to consider.

Competitive pricing

A great question to ask yourself when trying to map the competitive landscape is: "what would customers do if my solution didn't exist?"

This question invites you to not only think about directly comparable products, but also indirect competition in the form of behaviors, cultural norms, and simple solutions like spreadsheets. These alternatives could even be things like "hiring an intern to do it."

In some cases, you might also find that customers would simply do nothing. This could be because they're not aware of the problem, or that a better solution could exist. This dynamic often exists for really innovative products that are looking to change the status quo.

If you find that the majority of potential users are "doing nothing," it's likely you'll have to spend more time in your sales and marketing efforts in the early days talking about the problem and building awareness in the market around it.

Once you've mapped out the total universe of competition, taking into consideration both directly and indirectly comparable alternatives, you'll build up a reasonable understanding of how well known this problem is, how users have been handling it to date, and what they're currently willing to pay for the existing solutions. You'll also be able to figure out if your proposed solution is a linear improvement on the existing ones, or a nonlinear step-change.

Cost pricing

With cost pricing, you're looking to understand the link between how your costs will increase as product usage increases. What you ultimately charge shouldn't be divorced from how your costs will scale. This is particularly relevant if you're looking to sell to both small and large users, or want to offer some form of freemium or unlimited access.

Software can often be replicated at an extremely low cost of goods sold. This allows SaaS founders to only really focus on their customer acquisition costs (CAC), which often makes up the majority of expenses. As long as CAC is tamed, your other costs are typically less significant.

Value pricing

Value-based pricing focuses on value creation to define the product's price point. For many SaaS companies, the value created for users will be one of the following:

- Increased revenue: by providing access to new markets or end users
- Reduced costs: through process efficiency or cutting out other product needs
- More time: through process efficiency and enabling end users to do more with less

The primary challenge here is that oftentimes your product is just one part of a chain of actions that leads to an outcome. This makes it difficult to correlate the use of your product with a valuable outcome. Your value proposition should align with the desired outcome, but for a lot of SaaS companies, it's harder to align your pricing to it.

Importantly there needs to be an appropriate correlation between what you charge and the value a user extracts. If your product is an important component of a process that leads to thousands or even millions in savings or new revenue for a user, you're leaving too much money on the table by charging them only $10 a month.

An interview with Nirman Dave

Nirman Dave is the cofounder and CEO of Obviously AI, which lets anyone build their own AI models without code in minutes. Its vision is to turn every company into an AI company. He's built over 200 web apps in his career, many of which have gone on to be used by over one million people. He sold his previous startup to Intel before founding Obviously AI.

In our interview, we talk about the iterative journey Obviously AI has gone through in order to land on its current pricing model.

Nirman Dave
cofounder and CEO
Obviously AI

How did you think about pricing from Day 1?

We wanted to have a low barrier to entry for customers in order to gather feedback, so initially the pricing was free. We then moved this up to $500 per month for "all-you-can-eat" to assess a foundational level of willingness to pay. Our plans worked, but we soon realized we had a problem. Lots of people signed up, and many even signed annual contracts, but their product usage dropped very quickly after the first use. Something was up.

How did you respond to that?

We simply had to speak with as many customers as possible. Our customers were on a Slack channel, and so we just started to message them. We'd say, "I notice you're not using the product—is there anything we can do to help?" Some people responded, and others required a bit of incentive like a $100 Amazon gift card. Through that process we learned that the Obviously AI solution worked well, but in order to use it, you first had to solve another problem. This problem was the step before our platform could be used—the data needed to be properly structured and clean. At the time, we had no way of solving this, so it meant that the product was dropped as soon as customers realized they couldn't get the models to do what they wanted.

How did this learning impact your pricing strategy?

We tried to build software that helped with the data and formatting problem, but it didn't really work. After spending a ton of time with users, we realized they simply needed their own data scientist to help them clean up their data before they could use the Obviously AI platform effectively. This was our aha moment, so we rolled out implementation engineers that would help customers clean data as an onboarding step, and baked that within our pricing model. This was a game changer for us. It meant that we could unlock monetization for the long term as customers were able to get to highly accurate AI models faster than they could assign internal resources for data prep, and deliver on the biggest pain point our customers had.

It sounds like you favored starting with super simple pricing in order to get users onto the product, and maximize customer feedback signals. Over time, how did these insights encourage you to change your pricing?

Early on we did the classic startup hack of simply watching what users did, and then slowly gating certain sections of the product behind a paywall or premium offering. We saw that a lot of our users wanted to add team members, or add more rows to the data, and once we spotted this trend, we could lock this extra value behind increased pricing. Whenever they wanted to do more beyond the core of the product, they were prompted to pay more.

In the end, this proved to be a really frustrating experience for users. They'd get really excited about the product, and that excitement would dwindle when they were inhibited

> Early on we did the classic startup hack of simply watching what users did, and then slowly gating certain sections of the product behind a paywall or premium offering. In the end, this proved to be a really frustrating experience for users.

from doing more with the product because of a paywall. At first it wasn't intuitive to figure out the link between this pricing structure and the growing frustration because users would simply reach out asking about the product, or they'd have feature requests, without correlating this back to the cost. Eventually, we made the link, and decided to rethink our pricing strategy.

How did you go on to change the pricing model?

Instead of having a one-size-fits-all entry price, and then various incremental feature based pricing layered on top, we flipped to offering three simple pricing tiers that had a much broader scope of features within them. We also split out the software and services parts of Obviously AI, so that users can select either or both of them depending on their existing in-house data science resource.

Our entry price point was still kept very low, while giving users a broad enough feature set so that they could really understand the value of the product. Instead of having different feature sets per tier, we had mostly the same feature sets that were differentiated by quantum. And so graduating into higher paid tiers meant unlocking more of the same value, rather than getting to experience a new set of values altogether.

We felt that by artificially restricting the value users could get from our product by hiding great features behind a paywall meant that they didn't fall in love with our product as easily.

As our understanding of user needs has increased, we've slowly started to introduce new features for the higher tiers that align more closely with the needs of specific personas with different budgets.

Further thoughts from Tomasz Tunguz

Tomasz Tunguz is a former Google product manager turned venture capitalist. He's a general partner at Theory Ventures, where he invests between $1M and 25M in early-stage software companies that leverage technology discontinuities into go-to-market advantages. Prior to this, Tomasz was a managing director at Redpoint Ventures. He is also a board member of Looker, ERPLY, Electric Imp, AxialMarket, Quantifind, Expensify, and more.

In this part of our interview we talk about some observations Tomasz has had around pricing products aligned with value.

Tomasz Tunguz
general partner
Theory Ventures

What are your thoughts on value-based pricing from an investor perspective?

Value created generally falls into two main buckets. You're either helping your users to increase their revenue, or reduce their costs. A simple rule of thumb is that companies will typically be able to capture 5%–15% of the additional value created. In other words, if you're helping them to deliver $100 of new revenue, or save $100 on some other costs, then you can reasonably expect to take home $5–$15 of that.

> “A simple rule of thumb is that companies will typically be able to capture 5%–15% of the additional value created.

The important thing when trying to understand the relationship between value and cost is to not neglect the human element within this value-creation process.

For example, say you're selling to a VP of product at a scaleup. They'll likely need to justify the spend to the CPO. I've often seen startups that are offering value in the form of cost reductions signal that their product would enable the VP of product to forgo hiring that new person, or even reduce the headcount requirement across the team. On paper, this sounds excellent! People often make up a huge portion of the cost of running a company, and it's easy to measure the impact of not needing to hire someone new.

However, while headcount reduction might make business sense on paper, in reality, you've likely not thought about the ambitions of the individual you're selling to. Part of the game the VP of product is likely playing includes hiring more people, expanding their reach, and adding influence through additional reports. If your value proposition isn't aligned to the operational reality and ambitions of the buyer, despite how logical it is, you'll likely not convert their interest.

What other traps have you seen? Is there anything founders neglect to factor into their price when pitching to a potential new user?

One approach to be mindful of when articulating value is the concept of Total Cost of Ownership (TCO). This cost calculation goes beyond the core cost of the product itself, and factors in the indirect costs—for example, how much it costs to integrate the product, manage, and withdraw it. If someone is assessing your product in this way, it needs to be much much better than alternatives, versus marginally better with a similar cost structure. The costs of replacing existing processes or solutions with another are often significant, and therefore the net new value creation needs to be equally significant.

Pricing packaging

Packaging is how you bring pricing and product together into a purchasable offering.

In your early customer research, you might find there are several different user types or personas that could take value from your product. They may also have different budgets and price sensitivity.

Persona preferences and their relative willingness to pay will influence the packaging archetype you use. There are many ways to package: tier-based, good-better-best, usage-based, per seat, flat rate, feature based or a hybrid of all of them.

A good pricing and packaging structure should offer an obvious choice for each user persona, avoid value dilution and offer good upsell paths.

For this section we've interviewed an expert from Stripe and added further comments from venture capitalist Tomasz Tunguz.

An interview with Bill Bedsworth

Bill Bedsworth
head of pricing
Stripe

Bill is currently head of pricing at Stripe, where he leads both the product pricing and deal pricing teams. Prior to Stripe, Bill was VP of operations, insights, and pricing at Zendesk, creating a brand new pricing organization and completely overhauling Zendesk's pricing models. Prior to Zendesk, Bill spent 10 years at Adobe Systems, first leading the business strategy function and eventually running the global Enterprise business for Document Cloud. During his time at Adobe, he was involved in a number of significant pricing efforts, including leading the transition to recurring revenue and redesigning product packaging for the Document Cloud business.

In our interview, we talk about the core elements of pricing, and a few strategies you should keep in mind when packaging your product.

What do you absolutely need before you can even begin to package your product into something purchasable?

You need to deeply understand who you're packaging for. A well-defined customer profile and a clear articulation of how the product brings value to them are absolutely essential.

Packaging by its nature is all about putting a number of things into a package that speaks to solving a problem for whoever is buying it. If you don't continually ask "who is this for?", you're not going to be able to package effectively.

Do you have an example of a valuable lesson you've learned around packaging?

While at a large and very innovative company before Stripe, I ran a project that incubated 42 new product ideas with the intention of monetizing them and potentially launching them within the broader product suite. Out of these 42 projects, only two were successful.

After auditing seven years worth of these projects, a few things really stuck out. The first was that none of these projects failed because they couldn't turn an idea into a functioning product. Every concept was built. But almost all of them failed because they lacked a target customer, which then made it impossible to build the right product. This has a knock-on effect all the way down to pricing and packaging.

Let's say you have that foundational customer understanding. What steps can you take toward effectively baking this knowledge into your pricing?

You can start by choosing your product tiering strategy. In other words, whether you choose to have multiple feature-driven tiers designed to engage different customer profiles, or a single tier designed for all customers.

A single-tier strategy is suitable when your product features are broadly applicable across user types and any attempt to reduce features would limit the attractiveness of the core product. In this case, willingness to pay is driven by usage, rather than features. A multitier strategy involves using two to three tiers, each with a different allocation of features and price.

Choosing between these two strategies will be informed by your customer research, and whether your product serves multiple personas with different feature needs and budgets. Each tier should relate specifically to a customer profile or use case (i.e., you should know who you are building that tier for).

It also really helps to have appropriate naming for each of these tiers. If you have a product marketing team, get them involved immediately! Effective naming is designed to make the decision easier for the potential user. Choose a name that speaks specifically to their business type or use case.

At the center of your tiering strategy is a value metric. This is a measurable thing that ideally aligns as closely as possible to the value your product creates. For example, at Stripe, in the context of our payments products, we use payment volume as our value metric. Getting paid is the desired outcome when using this product, so we charge based on that positive outcome. The idea here is to try and create a correlation between value creation for both parties—the more they take value from your product, the more you take value from that usage.

If you opt for a multitier strategy, the value metric should still sit at the center of each tier as the measurable outcome at the core of the pricing.

You know the customer and you know what to charge them by, but how do you go about actually charging them?

There are several well known pricing structures in SaaS but they really boil down to two: pay-as-you-go and entitlement-based subscriptions.

Pay-as-you-go aligns the price directly to usage, with no up-front commitment for the user. This is excellent for price-sensitive users where you want a low barrier to entry in order to get them to try your product. Typically this works well if you're trying to win smaller users like early-stage startups.

Entitlement-based subscriptions require the user to commit to an up-front fixed fee in return for a usage entitlement, such as seats, transactions, amount of data, or some other measurable metric. These subscriptions generally include some accounting for ovarages, which then charges users a pay-as-you-go fee on top of the subscription for any usage over the allowance. This type of packaging is preferred by larger users, or anyone that really favors a degree of predictability and needs to forecast their costs.

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In your packaging, you want to try and architect some kind of laddering. In other words, users feel a pull to unlock more value creation by graduating into more expensive tiers and unlocking more features or consumption entitlement.

Are there any core things to keep in mind when packaging at the early stages?

This is particularly important at the early stages: try to reduce complexity as much as possible. We often see complexity delivered under the guise of "optionality," but customers don't really like it. They like to be told what to do with your product. Users spend far less time thinking about your product than you do, they're looking to you for guidance. Particularly if you're vertical SaaS serving a specific demographic, they want to hear from you what best-in-class users are doing with your product.

À la carte or atomized packaging is great if your customer has an intimate working knowledge of your product, but they often don't. The cognitive load required to build this knowledge is often too great, and they end up underutilizing your product because they don't fully know what you have on offer.

Do you have any thoughts on freemium pricing models?

Freemium isn't really a pricing model; it's a go-to-market strategy. Its sole focus is to acquire users, with the intention of creating a marketable database of contacts, which you can then upsell into your paid tiers. It might seem attractive early on to opt for this strategy. More users surely means more data and a clearer path to product-market fit? This might not always be the case. Freemium is an excellent acquisition strategy when you deeply know how users take value from your product, and the levers you can pull in order to encourage them to pay for it.

Further thoughts from Tomasz Tunguz

Tomasz Tunguz
general partner
Theory Ventures

Are there any traps or pitfalls you've observed when it comes to packaging in the early days of a startup?

When deciding which features to bundle, one mistake I've seen is when the open-source version—in other words, the lowest or freemium tier—has too many features. It gives too much of the product away, which ultimately cannibalizes the paid tiers. What you're really looking to do with this entry tier is figure out the minimum viable feature set in order to drive enough value that leaves the user wanting more.

Packaging aside, have you noticed any other pitfalls around pricing?

I also think some founders underestimate the impact pricing has on the perception of your product or service. Early on perhaps you're looking to optimize for market penetration. Acquire as many users as quickly as possible, in order to build up a lot of data that might help you build a better product. This often means you're giving it away for free, or at a very low price. This might not always be a good strategy. I've seen startups struggle to acquire customers when the price was free, but then this changes when they increase the price. The price increase alters how customers perceive the product, it suddenly becomes more useful and trustworthy. There's a degree of comfort in buying from a company that you know is making revenue, and therefore more likely to not only survive, but continuously improve its product.

Measuring success through an investor lens

For startups looking to play the venture funding game, it's worth mentioning that your price point signals your market potential to investors. Sizing your market is an equation of price multiplied by volume. Once you have a reasonable foothold on price, and you know who you're selling to, you can scope out the size of the market you're going after and signal that potential to investors.

Investors, therefore, care a lot about your pricing strategy. And so should you if you're looking to raise capital from them. We've interviewed an investor to understand how they go about assessing the quality of a startup's pricing model.

An interview with Morgane Zerath

Morgane Zerath is a principal at Crane Venture Partners. Before joining Crane, she built the sales function from scratch at Tessian, a cybersecurity company in email security. Because of her sales background, she's now working very closely with Crane's portfolio companies to figure out the right GTM motion, pricing being a core element of both PLG and top-down motions.

In our interview, we talk about how Morgane and Crane VC assess a founder and their pricing model at the early stages.

Morgane Zerath
principal
Crane Venture Partners

When a SaaS founder approaches you for investment, what things are you looking for when it comes to their pricing model?

There are really two things, and they're likely not what you think.

Number one: we're looking to see if they've even thought about their pricing model at all. Crane often invests at the pre-seed stage, before they've even monetized, so having a degree of forethought is a really good signal. Number two: we want to understand how they think about pricing, and the quality of thought that's gone into that thinking.

At the earliest stages, founders are often so excited to create a great product first and foremost that pricing often comes further down their list of priorities. But really, it should be right at the top. Thinking about pricing forces you to really think about the buyer on the other end, and what sort of business you need to build in order to deliver the product to the market in the most effective way.

We don't expect to see a hyper-sophisticated and well-crafted pricing model at the earliest stages, but even a simple one indicates the depth of knowledge a founder has about the potential of the business, and the market they're selling into.

We'll look into the variables the founder has used to think about pricing, and whether these make sense for the business and the market.

Can you elaborate further on the point around pricing being a forcing function for the business a little more?

If you want to build a product-led growth business, you're putting yourself in a bad position if your pricing is bundled into large multiyear contracts. The way you price your product will determine how you build your team, and the muscles you build on the go-to-market side.

It's sort of a chicken and egg dynamic. Thinking about the type of business you want to build, such as a bottom-up, self-serve approach, or a top-down sold motion, will heavily influence how you'll need to package your pricing. And how you think you can reasonably price your product will influence your strategy to grow the business. Pricing is often the better of the two to start with. You can ask customers about pricing, but you can't really ask them how to structure your company for scale.

Are there any red flags you watch out for when speaking with founders and looking into their pricing model?

There are several. The main one is where you see that price isn't aligned with value. The amount you charge needs to be deeply correlated with the value the user is extracting from using your product. This can be hard to do straight away, but we want to see that you're thinking in this way and inching towards that alignment.

Competition-based pricing can also be a bit of a red flag. When we ask founders how they landed on this price, we often get an answer along the lines of competition: "our competitors price this way," "we wanted to keep with market rates," or "we wanted to undercut competition to gain market share." Pricing by competitors is one vector to use, but we feel it shouldn't be your main one.

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Another one is complexity. If we can't understand your pricing, a user isn't going to. This is true even when you hide complexity in the form of hidden costs. Simplicity also needs to be transparent.

Equally, oversimplification can be an error as well. One-size-fits-all pricing means you're likely going to leave a lot of money on the table, because you're not differentiating between user types who might need different things, or perhaps have varying abilities to pay.

Inversely, are there any green flags or positive signals that suggest a founder is thinking in the right way?

It's always a good signal on the first meeting with a founder when they lead with the pain point rather than the product. We like to see that a founder is obsessed with the problem in the market, and of course, that it's a big, valuable problem to solve.

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> It's always a good signal on the first meeting with a founder when they lead with the pain point rather than the product.

We like to see founders who show an obsession with gathering feedback and speaking with users frequently in order to understand user types and use cases more intimately. User-centricity tends to translate across to a better product, and a more accurate pricing model. Users are the ones who own the truth; speaking to them gives you access to it.

Do you have any final takeaways or quick tips for founders?

If your users aren't even commenting on your pricing, you're probably not charging enough.

And finally, pricing always changes. It's in a constant state of flux. This is what makes it so challenging. Markets change, customers change, and your pricing should change accordingly. Keep it top of mind and consistently revisit your pricing to ensure you're evolving it with the market.

How Stripe can help

More than 200,000 businesses, from startups like **Songbox** to enterprises like **Atlassian**, use Stripe Billing to collect one-time or recurring payments. We built Stripe Billing to make it easier for businesses to:

- **Offer new pricing models:** Stripe Billing offers **flexible billing logic** for everything from per-seat pricing to metered billing out of the box. In addition, support for **discounts**, **free trials**, **prorations**, and **installments** is built in.
- **Expand into new markets:** Use a single API integration to deploy faster and offer subscribers the payment options that are available in their local currencies.
- **Enable your customers to self-manage their subscriptions:** With Stripe Billing's **customer portal**, you can enable your customers to self-manage their payment and subscription details. In the customer portal, customers can update their payment methods, and upgrade, downgrade, or cancel their subscriptions with ease.
- **Minimize accounting errors and reporting oversights:** Reduce costs and risk with a single platform for unified reporting and accurate accounting. **Revenue recognition** and **reconciliation**, as well as robust **analytics capabilities**, are built into Stripe Billing.
- **Automate tax collection on your recurring transactions:** **Tax calculation and collection** is also built into Stripe Billing. Know where to register, automatically collect the right amount of tax, and access the reports you need to file returns.

To learn how you can accelerate your growth by capturing recurring revenue, **contact our sales team** or **sign up for an account**.