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## Startup School: Wired Editor Chris Anderson On Freemium Business Models

Posted Oct 24, 2009 by [Jason Kincaid \(@jasonkincaid\)](#)

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Wired Editor-in-Chief [Chris Anderson](#)

[Anderson](#) is now speaking at Y Combinator's Startup School about Freemium Business Models. Anderson likened freemium to handing out muffins on the street to entice people to start eating your muffins. But with muffins there's a significant cost to giving away each muffin. With digital goods, you can give away 90% of your product for free, without any cost for those goods.

He says 'free users' aren't free loaders, and that it's okay to let the minority (paid users) subsidize the majority. Because the free users will recommend to friends, it's a great form of marketing. And for those paid users, many of them are very strong customers — they may be price insensitive, with very little churn.

Anderson says that for Wired, the magazine is sold in various forms (news stand, subscriber, digital form online). And there's price segmentation on this — lots of distribution given away for free, the bits are free. The 'atoms' (physical good) are the premium. 90,000 customers for newstand edition, 800,000 at \$1/month subscription.

Anderson then started talking about the ve to play. Parents are used saying no to cred they're on Club Penguin, they see the child But if you pay, you can get into the cool igk card that way, because it's clear that the cl ad.

What will people pay for? They will pay to s than money. Older people have more mon

Anderson then outlined some of the mode

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giun, which is free on TV. But if their friends, etc. over the credit at they saw in an

ave more time

models.

### Feature limited

Gives users real utility initially, then they convert if they want it even better. But this also means that you have to build more features (things people would want to pay for). And you have to maintain multiple products.

### Time Limited

Easy to do. But there's less commitment and engagement.

### Capacity limited

Easy to do (e.g. limit the number of megabytes in a Email box), but it doesn't always work for a product.

### Seat limited

Easy to do. But it doesn't work for every product, and people can 'cheat' by only purchasing a few seats, or segmenting company into lots of 5 person teams so they're free.

### Customer Class Limited

Bizspark is free to businesses if you're under 3 years old, less than a million in revenue. Once you graduate you pay. This is easy to implement, but harder to enforce. Anderson says that Chinese Pirates had a similar model with Microsoft — Bill Gates said that China was developing, if they were going to steal software, they'd rather they steal Microsoft's software, so they develop for Microsoft.

As one last example, Anderson spoke about Open Source Hardware, brought up his company 3D Robotics, which makes DIY Drones. Open-source unmanned vehicles. They give the 'bits' away (the software) and plans so you can build your own. This helps build a community. And then it sells finished goods on the store. Charges 2.6x what it

costs. Need two 40% margin — one for you, one for retailers, who you want to have sell your stuff.

Q: Free was available on the iPhone, I got it for free. And they took it back and I had to pay \$10.

A: I didn't know about that. That sucks. I have no idea how that happened. Free for four weeks on Scribd, free on Google Books, free forever audio form, free in other places as well.

Q: One risk with freemium that I've experienced as consumer is feeling that free version is crippled. Yahoo Mail, they can get away with it because people keep sending to your old address. Unless you have that kind of lockin. How would you do that?

A: I recommend not having crappy products, even free ones. If your free version is crippled, it won't work as advertised, won't work as a form of marketing.

## CrunchBase Information

Chris Anderson

Information provided by [CrunchBase](#)

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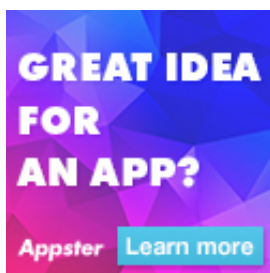


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vacuum forming · 4 years ago

hi,

wow good business model....i appreciate it

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**Paramendra Kumar Bhagat** • 5 years ago

What one calls freemium another calls marketing.

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**Anders** • 5 years ago

The Freemium model is a great model increasingly used foremost for digital products but there are examples such as Aravind that uses the Freemium model to provide free eye surgery for the poor in India. Read more here: <http://bit.ly/d5pM6>

I have put together some videos relating to the Freemium model on TBMDDB such as the debate between Chris Anderson and Guy Kawasaki from SxSW 2009 here: <http://bit.ly/M7mG4> or the NIN case, making \$1.6 Million in a week for music given away for free here: <http://bit.ly/16bSz5>

Another interesting collection of posts and videos on the subject is Peter Frobergs [www.freemium.org](http://www.freemium.org)

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**Tim** • 5 years ago

A great summary of an insightful presentation. One of the most interesting points Chris made was that paying customers for a freemium service statistically have a far lower rate of turnover than customers of other business models.

With most businesses deriving the large sum of their revenue from existing customers, this is an important datapoint to track. Coupled with the low cost of acquiring a new customer with this model, it makes quite a compelling case for leveraging "free".

Chris went into more detail about the quality of premium customers as well, and I put my responses together here: <http://blog.recurly.com/>

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**LLL** • 5 years ago

Free is a compelling business model, especially in a digital economy. Taking a dispassionate look at the internet giant Google's business model provides a tremendous validation for this. Gmail is free and exceptional, that's why I wouldn't mind paying \$99/yr to use it.

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**Daniel DiRico** • 5 years ago

This is a nice summary of the major freemium business models used today.

Lately I am seeing a lot of freemium+subscription models out there and fewer one-time purchase prices for software.

At the end of the day though, you still need a low entry barrier and a high exit barrier - of

which could be in the form of switching costs, as pointed out by the Yahoo mail scenario.

^ | v • Reply • Share ›



WTF → Daniel DiRico • 5 years ago

Anderson's idealistic perspective shows considerable lack of real world business experience. His ideals wouldn't even hold water in the vacuum where they were conceived. Wired is an epic fail.

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