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SWORKIT: TAKING THE FREE OUT OF FREEMIUM?

Michael A. Stanko wrote this case solely to provide material for class discussion. The author does not intend to illustrate either effective or ineffective handling of a managerial situation. The author may have disguised certain names and other identifying information to protect confidentiality.

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No clear consensus came from the leadership of the health and fitness app[[1]](#footnote-1) Sworkit after a lengthy October 2017 online Slack chat. The leadership group was debating the app’s pricing model and whether it needed drastic change. A decision would have to wait until the conference call the group had scheduled for the next week.

Sworkit had a large, devoted user base and was on track to be profitable in 2017. Despite this, Ben Young and Greg Coleman, the chief executive officer and president of Nexercise Inc., the Maryland-based company that owned Sworkit, felt there was a better way to capture value from their app. As Young and Coleman left the chat, it seemed there was a real possibility that Sworkit might abruptly depart from the business model that had allowed it to reach 1.5 million users in the past month.

“SIMPLY WORK IT”: A BRIEF HISTORY OF SWORKIT

Towards the end of his time as a captain in the US Army, Ryan Hanna decided to learn to write code. He decided on a project he would use himself: an app to help him build workout routines, with randomized exercises to keep his workouts fresh. His first goal was a modest 100 downloads. Version 1.0 of Sworkit, which launched in 2012, used graphics of Hanna himself performing the workouts, with voice instructions by his wife. This was a fun, learning side-project at the beginning; Hanna already had a “real job.” A tweet Hanna sent to the blog *Lifehacker* caught on, and Sworkit’s growth accelerated, far surpassing Hanna’s original goal and propelling Sworkit past one million downloads. A Sworkit pro version, including extra features, was launched in 2014 and sold for a one-time price of $3.99[[2]](#footnote-2); the free version showed ads, which provided another revenue source.

Later in 2014, Hanna partnered with Young and Coleman, both graduates of the Wharton master of business administration program at the University of Pennsylvania. Young and Coleman’s company, Nexercise, had experience with fitness apps through a previous successful product in this space (the product was also called Nexercise). Said Hanna, “I’m a developer and a product person. They can make this a business. . . . that’s where Ben and Greg come in.”[[3]](#footnote-3) The partnership provided additional resources for customer acquisition as well as improved multimedia production quality in a completely revamped version of the app. Sworkit’s users could now target particular muscle groups or fitness goals, allowing for personalized workout routines, with no equipment required. Hanna became vice-president of product for the company and began recruiting additional developers. The team was distributed globally; Hanna now lived in the United Kingdom, while Coleman and Young worked out of a Rockville, Maryland, technology park.

Sworkit’s interface was similar to that of a music app: it allowed users to skip exercises they didn’t feel like doing using a format that was familiar to customers. “We’ve created a video workout player that’s built on the same principles as a music player and people understand that,” said Young. “Instead of just watching a video, you’re having an interactive experience.”[[4]](#footnote-4) Sworkit was featured in the Apple App store and Google Play and was mentioned regularly by media outlets such as *Cosmopolitan* and the *Washington Post*. It also received awards such as *SELF* magazine’s award for Best Bodyweight/High Intensity Interval Training Workout App. Loyal users praised Sworkit’s intuitiveness and the way it made workouts easy and fun.[[5]](#footnote-5)

“In the early days, we were following the Silicon Valley playbook: Get as big as you can, get as many eyeballs as you can, figure out how to monetize them later. We were still thinking of advertising as the primary opportunity for revenue generation,” said Coleman. While most customer acquisitions came organically, the company also used a variety of paid online advertising tactics to grow Sworkit’s downloads (see Exhibit 1). In addition to efforts to garner media mentions, Sworkit’s promotional tactics also included an active presence on social media platforms, particularly Twitter. Target customers were busy individuals who didn’t always have time to get to the gym, those who were intimidated by the gym, and people who simply didn’t want to think about which exercises to do and preferred to let Sworkit expertly plan their anytime, anywhere, no-equipment-required workouts. Workouts were organized under four categories: strength, cardio, yoga, and stretching.

While the addition of a few new employees enabled the leadership team to focus more on strategic matters, the atmosphere was still very much one that required “all hands on deck.” As Coleman explained, “On any given day, I might be doing payroll, legal documents, marketing plans, bookkeeping, onboarding a new employee, HR [human resources], handling benefits, and more.” Both Hanna and Coleman had served in the US military, and Coleman was still involved through the National Guard:

I’m a colonel in the Air National Guard. In a month, I may do 20 hours of military service. . . . The biggest asset I bring from my military career is perspective. Whatever happens, the sun is going to come up the next day. A lot of start-up founders go through an emotional roller coaster. The company is going to go through very high highs and very low lows. You need to keep your emotions measured.

As of 2015, the company had attracted $2.1 million in outside investment at a total valuation of $11 million. Late in 2015, Young and Coleman had appeared on the television show *Shark Tank*, seeking further investment and a partner to help them continue Sworkit’s growth.[[6]](#footnote-6) Young and Coleman requested $1.5 million for 8 per cent of the company from the sharks. Their pitch was well received: one *Shark Tank* observer commented that they had an “excellent understanding of monetization. . . . These guys are doing it right, from the way they developed and marketed and then presented their product. . . . People should take notes.”[[7]](#footnote-7) During the taping of the show, the two agreed to basic terms with Mark Cuban to sell 10 per cent of Sworkit plus some unused advertising capacity in exchange for $1.5 million. After the taping, there were “a lot of other terms that [weren’t] discussed” on the show, Young said.[[8]](#footnote-8) Unfortunately, a few weeks after the episode aired in February 2016, the deal had fallen apart—a common outcome during the due diligence period. Sworkit’s leadership still viewed their *Shark Tank* experience as positive, as downloads spiked when reruns of their episode aired.

Shortly after the *Shark Tank* appearance, Sworkit adjusted its premium offering to make it a subscription service. As in the (now retired) one-time purchase pro version, subscribers did not see in-app advertising, and they could also access additional features and customization controls. Premium subscriptions launched at $2.99 per month or $19.99 per year. Purchasers of the previous one-time fee pro version were transitioned to subscriptions. Said Hanna, “Consumers have come around to subscription pricing.”[[9]](#footnote-9) Many content apps used subscriptions—for instance, music apps such as Spotify, news apps like the *Wall Street Journal*, and language-learning apps like Duolingo. Consumers also increasingly purchased non-digital products such as razors, food, and wine through subscriptions. Negative feedback was minimal as customers were transitioned to the subscription offering. Sworkit was regularly listed as one of the top 10 health and fitness apps on the Apple App store, and it spent several days in 2015 and 2016 in the number-one spot (i.e., most downloaded). Sworkit revenues for 2016 (the first year under the subscription model) surpassed $1 million, which was similar to revenues the prior year. However, 2017 revenues were on track to double as recurring subscriber revenue came in alongside revenue from new customers. By the summer of 2017, Sworkit had been downloaded 25 million times. Prices for the premium subscription were raised to $7.99 per month or $59.99 per year. The fact that Sworkit had been used to help so many people get fit and stay fit was a point of pride in the growing organization, which now had seven employees and four contractors.[[10]](#footnote-10) A free (no advertising) children’s version was developed to further the cause of exercise and activity.

FREEMIUM BASICS

Nothing attracted consumers quite like the word “free,” and this was the logic behind the freemium pricing model: users got access to a basic product for free, but they had to pay for additional features.[[11]](#footnote-11) For instance, Dropbox Inc. allowed users up to two gigabytes of free cloud storage. When customers had used nearly all of this capacity, they were offered subscription accounts that included larger amounts of storage. This model was used extensively for video games, where users were often asked to pay for competitive advantages (for instance, power-ups or weapons). Even entertainment offerings, such as Home Box Office Inc.’s (HBO) *Last Week Tonight*,used a form of freemium, where one segment of each episode was posted for free viewing on YouTube, while the entire episode was only available to paying HBO viewers. A constant challenge with the freemium model was converting free users into paying premium customers. The large majority of free users resisted upgrading. Generally, making apps available for one-time purchases led to 4–8 per cent of free customers converting. Subscription purchase options generally led to 1–4 per cent of customers converting from free usage.[[12]](#footnote-12) “The free experience is enough for the average person,” commented Coleman in the *Shark Tank* episode.

Once customers converted to subscriptions, retaining them was a key concern. “It’s fitness. Retention is always a challenge in the fitness industry,” said Coleman. Customer churn tended to have a consistent pattern, with the most churn in the first billing period. “If you can hold on to customers for a few periods, you tend to be able to hold on to them a lot longer,” explained Coleman. In the fitness app industry, 30 per cent subscriber retention over the course of a year was considered good. These realities led to pricing options such as discounts for customers who prepaid for a full year.

Although Sworkit used an advertising mediation platform (MoPub, owned by Twitter Inc.) to ensure the highest possible advertising revenue per free user, revenue from each premium subscriber far surpassed the advertising revenue from each free user. Overall, advertising amounted to approximately one-quarter of the app’s total revenue even though the vast majority of users were free users. “The challenge with advertising is that it is unpredictable,” said Coleman. “It is very difficult to predict your revenue from one month to the next. The same amount of traffic will have different financial results depending on fluctuations in the bid rates offered by advertising platforms.” For instance, advertisers tended to spend heavily in the final months of the year (between Black Friday and Christmas), while Sworkit’s usage tended to be heavier in January, just as many gyms were crowded. On average, advertising revenue ranged from $0.03 to $0.08 per month for each active free user, which meant that a massive quantity of free users was needed to generate substantial advertising revenues. Free users also generally exhibited a lower commitment to the product in terms of frequency of workouts and retention, both of which tended to be considerably lower than for paid subscribers. (A 20 per cent annual retention for free users was considered good.) Coleman explained,

We had this idea: instead of serving up other people’s ads, let’s serve up some of our own ads to get customers to upgrade to premium. We saw a dramatic increase in the number of new subscribers. By advertising to the free users, we were actually making more money off of the upgrades to subscriptions than we were from the ads that otherwise would have been showing.

There was also a message carried with the free price: “Being available for free causes people to devalue what you are offering.” There was no denying that the ads detracted from free users’ experience, distracting them from their workouts. All of this created frustration and forced the leadership team to reconsider whether they wanted to be in the advertising business.

In terms of metrics, Sworkit tended to focus on the so-called pirate metrics: acquisition, activation, retention, referrals, and revenue (AARRR). “There is no silver bullet,” said Coleman. “I’m a pilot. There is no one instrument I can stare at the entire time. If I did that, I’d crash.” That said, the team watched the number of monthly active users closely. “If you are playing the advertising game, it is a monthly active users’ game,” said Coleman.

aPP STORE ECONOMICS

Sworkit was available in 13 languages via the Apple App Store and Google Play, with the majority of revenue generated through the Apple App Store. Both the Apple App Store and Google Play’s terms of service required all in-app purchases, even subscriptions, to be processed through these intermediaries, which had 30 per cent margins. Advertising revenue was not channelled through the app store; Sworkit received advertising revenue directly from MoPub.

Since 2012, health and fitness app downloads and total revenue had grown by approximately 17 per cent each year, outperforming the app market as a whole. Over time, the health and fitness category became more crowded (see Exhibit 2), making it more challenging to consistently place in the top-10 category of downloads. Competitors included MyFitnessPal (acquired by Under Armour Inc. in 2015), which tracked users’ progress towards diet and exercise goals and included a free offering plus a premium subscription tier. Nike Training Club provided free access to performance drills and exercises. In other segments of the health and fitness app category, there were numerous popular yoga and meditation apps with a variety of pricing plans (many including free options, such as temporary trials).

While numerous competitive apps had sprung up, over 95 per cent of active health and fitness app users made use of only one app, tending to use that app multiple times per week. App use was similar to traditional gym use: weekdays had higher usage than weekends with peak times in the morning and evening. Interestingly, app users tended to work out earlier in the morning and later in the evening than traditional gym users.[[13]](#footnote-13) Within this competitive context, Sworkit was conscious of trying to acquire customers profitably and had continued to reduce its spending on paid online advertising. “As we get away from this eyeball game, we’re not just trying to grow as fast as possible. We’re trying to grow in a profitable manner and build a sustaining company where the user economics actually work,” said Coleman.

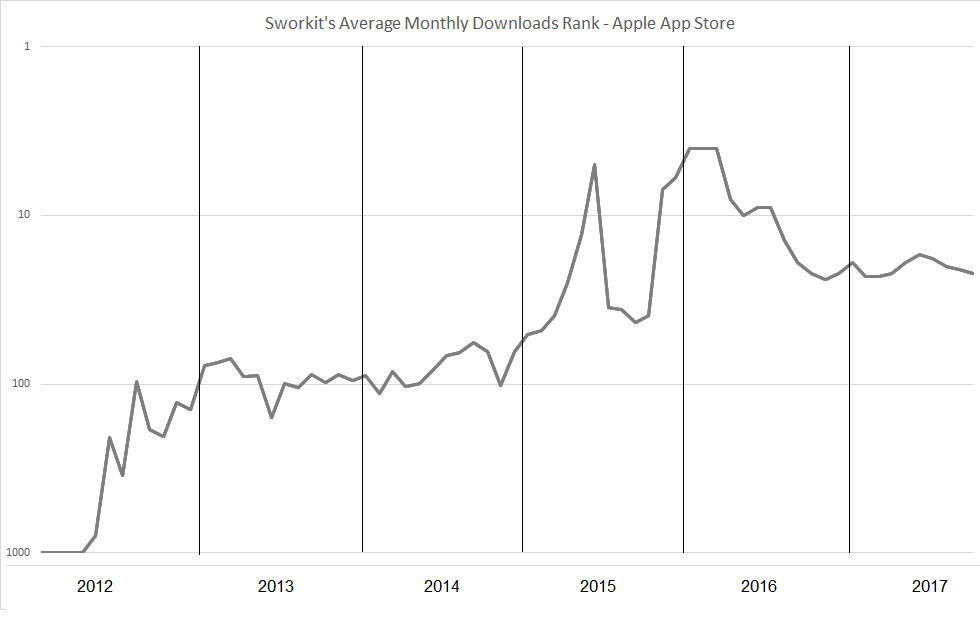
TO CHARGE OR NOT TO CHARGE: THAT IS THE QUESTION

Throughout 2017, frustrations around the advertising business increasingly led the leadership team to reconsider the freemium model. These concerns were coming to a boil as the leadership team began to agree that the current Sworkit model encouraged usage, but perhaps at the expense of revenue and profit. “I have a membership to Life Time Fitness. They’re not just going to let me go there for free. Why should we be giving away our product for free forever?” asked Coleman. Some free users had been using Sworkit for years without paying a cent. Despite these concerns, the freemium model seemed to be working as intended: Downloads were consistently high, meaning a steady introduction of new users who could potentially convert to premium subscribers. Sworkit was profitable and had no pressing need for further investment.

The leadership conference call was lively, covering a wide range of questions: If Sworkit eliminated free access, could the company convert a larger portion of customers to subscriptions? On the other hand, would a shift away from the freemium model lead to fewer downloads and a much smaller funnel of users to potentially convert to subscriptions? Was it possible to compete with freemium offerings without a free option? Would the steady flow of valuable publicity stop if there wasn’t a free offering available? How could Sworkit’s pricing and promotion be tailored to ensure a sustainable, profitable outcome? Would keeping a free version available but drastically reducing its functionality make converting to subscriptions more compelling, or was the company better off continuing with its current approach?

Coleman tried to focus the conversation, saying to his colleagues, “It’s risky, but to me, it comes down to the question: What type of company are we? Are we an advertising company that’s based on eyeballs? Or are we a fitness company that’s based on helping people improve their fitness and health through an exchange of value for value?”

Exhibit 1: Sworkit Download Rank within the Apple App Store, Health and Fitness Category



Note: The health and fitness category grew at approximately 17% per year over this period, both in terms of downloads and revenue. Since this plot shows rank within the health and fitness category, a horizontal line (i.e., rank remaining constant) corresponds with this 17% category growth. Assume a 10% internal rate of return (i.e., interest rate) for calculations such as customer lifetime value.

Source: Prepared by the case author with assistance from Curtis Pouncy, based on data from “App Analytics & ASO: The Tools You Need to Monitor, Optimize and Get More Downloads,” App Figures, accessed December 14, 2018, www.appfigures.com.

Exhibit 2: A Sampling from the 2017 Health and Fitness App Competitive Landscape

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **App** | **Description** | **Free Offering** | **Premium Price** | **Ads in Free Version?** |
| Cyclemeter | Tracks and collects cycling activity data | Reduced functionality | $9.99, one time | Yes |
| Endomondo | Tracks activity, calculates fitness statistics, and offers coaching | Reduced functionality | $5.99/month | Yes |
| MyFitnessPal | Tracks steps and calorie consumption | Reduced functionality | $9.99/month | Yes |
| Sworkit | Provides customized workouts | Reduced functionality | $7.99/month or $59.99/year | Yes |
| ACTIVEx | Provides personalized and group-based workout routines | Reduced functionality | $3.99/month | No |
| Couch to 5k | Develops training activities to prepare for a 5K race | Not available | $2.99, one time | Not available |
| PEAR Personal Coach | Provides personal fitness coaching | 14-day free trial | $5.99/month | No |
| Strava | Provides running and cycling analytics | Reduced functionality | $7.99/month | Yes |
| Nike+ Training Club | Provides workouts and tutorial videos | Full functionality | No premium upgrade | No, but app can browse Nike products |
| Argus | Tracks fitness and sleep, and provides fitness challenges | Reduced functionality | $9.99/month | Yes |
| Lose It | Counts calories and tracks fitness | Reduced functionality | $39.99/year | Yes |
| Lifesum | Counts calories | Reduced functionality | $21.99/three months | No |
| Fitocracy | Acts as a personal coach for fitness goals | Reduced functionality | $4.99/month | Yes |
| FitStar | Provides customized workouts | Reduced functionality | $7.99/month | No |
| MapMyRun | Tracks running data and shows other runners’ routes | Reduced functionality | $5.99/month | Yes |

Note: All currency amounts are in US dollars.

Source: Prepared by the case author with assistance from Curtis Pouncy, based on individual app websites and “Top 20 Best Health and Fitness Apps of 2017,” *Great Performers Academy* (blog), accessed February 11, 2019, <https://greatperformersacademy.com/health/top-20-best-health-and-fitness-apps-of-2017>.

1. App = application. [↑](#footnote-ref-1)
2. All currency amounts are in US dollars. [↑](#footnote-ref-2)
3. “Ryan Hanna: Sworkit: From Side Project to Full Time Venture,” YouTube video, 33:15, posted by “PhoneGap,” July 26, 2017, accessed February 11, 2019, https://youtu.be/uIQXYwoJ\_JY. [↑](#footnote-ref-3)
4. Katie McNally, “Second UVA Alumnus on ‘Shark Tank’ Earns Record-Setting Investment,” UVA Today, March 1, 2016, accessed February 11, 2019, https://news.virginia.edu/content/second-uva-alumnus-shark-tank-earns-record-setting-investment. [↑](#footnote-ref-4)
5. Kevin Loria, “A Guide to the Free Fitness App Sports Scientists Just Called the Best,” Business Insider, August 19, 2015, accessed February 11, 2019, www.businessinsider.com/one-free-fitness-app-has-made-a-huge-difference-for-me-and-researchers-say-it-works-too-2015-8. [↑](#footnote-ref-5)
6. *Shark Tank*, Season 7, episode 18. [↑](#footnote-ref-6)
7. “Shark Tank Breakdown – Ep 8 – SWORKIT, Clean Sleep, TUTUblue, NOHBO,” YouTube video, 6:24, posted by “Jeremy JasonA,” February 22, 2016, accessed February 11, 2019, https://youtu.be/dmJ-m09Y-fM. [↑](#footnote-ref-7)
8. Sara Gilgore, “Mark Cuban ‘Shark Tank’ Investment Falls Through for Local Startup,” *Washington Business Journal*, May 18, 2016, accessed February 11, 2019, www.bizjournals.com/washington/blog/techflash/2016/05/mark-cuban-shark-tank-investment-falls-through-for.html. [↑](#footnote-ref-8)
9. “Ryan Hanna,” op. cit. [↑](#footnote-ref-9)
10. Sara Gilgore, “This Md. Startup Lost Out on Mark Cuban’s ‘Shark Tank’ Investment. Now It’s Back with a New Plan,” *Baltimore Business Journal*, August 1, 2017, accessed February 11, 2019, www.bizjournals.com/baltimore/news/2017/08/

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12. “Ryan Hanna,” op. cit. [↑](#footnote-ref-12)
13. Lali Kesiraju and Toby Vogels, “Health & Fitness App Users Are Going the Distance with Record-High Engagement,” *Flurry Analytics* (blog), September 7, 2017, accessed February 12, 2019, https://flurrymobile.tumblr.com/post/165079311062/health-

    fitness-app-users-are-going-the-distance. [↑](#footnote-ref-13)