THE SAAS PRICING SPECTRUM

An in-depth look at the various pricing models for SaaS businesses.

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INTRODUCTION

"Pricing is the main tool you have to align customers, the value of your product or service, and your goals. At least one person in your company should be obsessing over it."

Ariela Bitran Rich,
Director of Pricing Strategy at Chargebee

Pricing is proven to be a critical growth lever for scaling businesses.

According to McKinsey, pricing transformations can generate margin improvements of up to **7% in as little as 3 months**, and sustain those improvements into the long term. Get pricing right, and you stand a much better chance of gaining loyal users and growing market share. Get it wrong, and you risk leaving money on the table, losing deals, and being left behind by competitors.

Adapting pricing models at regular intervals can help accelerate the scaleup growth trajectory, and put your business on the path to profitability. Businesses that update their pricing at least once every 6 months see **nearly twice the Average Revenue Per User gain** of those who update it less regularly.

But knowing when to evaluate pricing models and how to adapt them can be challenging. In the early days of a startup, the priority is acquiring customers at any price. As businesses scale, building out processes and infrastructure to manage pricing strategically is critical – but often overlooked. Research shows that some businesses only spend **six hours on their pricing strategy** across their entire lifetime.

Pricing isn't a 'set it and forget it' activity: as the product evolves and expands, and as the business enters new markets and targets new segments, pricing should be updated accordingly. Finding the optimal model depends on product type, market, organizational structure, business goals and more. In this guide, we'll weigh up three of the most common pricing models, explaining how they work, why businesses might choose to use them, and how they drive growth.

RANGE OF PRICING MODELS

FIXED SUBSCRIPTION

Historically the go-to model for SaaS businesses, subscription models lock customers into a set, periodic price for a predefined package of features.

salesforce
Adobe
NETSUITE
workday.

CONSUMPTION

This has become more popular as businesses look for ways to add and create value through their pricing model. Consumption models (like usage-based pricing, or pay-as-you-go) mean customers only pay for what they use.

snowflake
twilio
elastic
DATADOG

HYBRID

Usually a subscription package with overlaid consumption elements, such as overages or usage-based add-ons.

The emerging model for scaling businesses, hybrid offers new ways to monetize products outside of core recurring revenue. Hybrid pricing models enable businesses to move customers up and down the pricing scale more flexibly, and to personalize pricing according to what customers value, and what they can afford to pay.

zapier
HubSpot
shopify
ATLASSIAN

Effectively managing pricing is a whole-business initiative, requiring input from leadership, Product, Customer Success, Sales and Finance teams. It also requires infrastructure and tooling – first to obtain customer-level usage data to inform the pricing strategy, and then to operationalize into workflows, invoices and CRM data. Implementing these things early turns pricing into an active motion that can drive significant and long-term benefits for the business.

SAAS PRICING MODELS

There are a number of ways in which SaaS businesses might choose to package and price their products. Different combinations can help reach different audiences, with different needs and use cases.

Increasingly, businesses are getting creative with the way they consider pricing – but to get you started, below are some of the most common, market-tested pricing models.

1. FIXED SUBSCRIPTION

Businesses that use this model

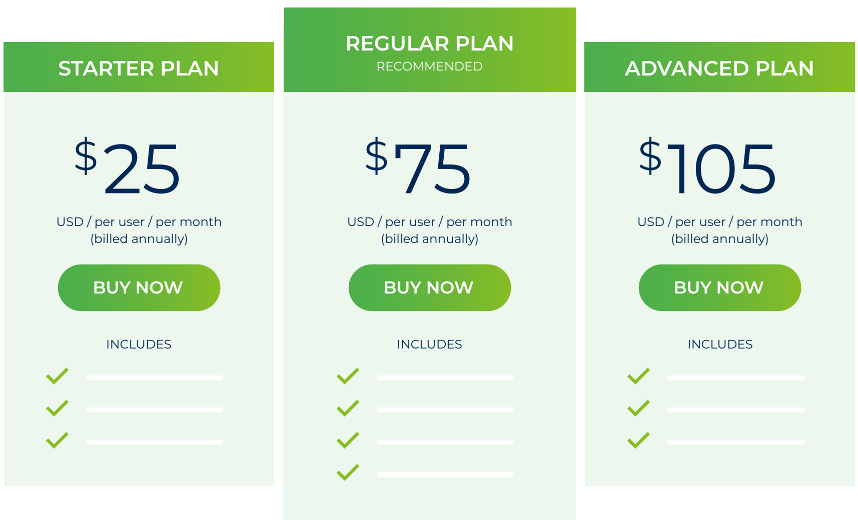
What is fixed subscription pricing?

Historically, fixed subscription pricing has been the go-to model for SaaS businesses.

Fixed subscriptions are usually tiered. Vendors offer a small range of 'good, better, best' options, each at a different price point and delivering different features and functionality.

Customers can choose the package that best suits their needs, and subscribe for access to the product over a defined duration. Customers may pay for several licences in their subscription: the price is usually per seat or location. Customers pay the same set price for the subscription at regular intervals (monthly, annually), irrespective of how much of the product they use, or how often they use it.

Example:



What are the pros of fixed subscription pricing?

- **Simple to understand and implement:** No complicated usage tracking or variable invoicing.
- **Clear correlation between price and value:** The more customers pay, the more access they get.
- **Regular and predictable cashflow:** Costs stay the same for customers, revenues stay the same for vendors.
- **Grows revenue:** Price per subscription can be increased as functionality is added and the product evolves.
- **Grows loyalty:** Existing customers are likely to need more subscriptions as they grow headcount, increasing product stickiness.

What are the cons of fixed subscription pricing?

- **Inflexible:** Customers pay the same amount irrespective of how much they use the product. Features are often bundled, so price can include costs for analytics, security, infrastructure and more 'invisible' features that customers may not value.
- **Subscription bloat:** The average business has over 130 SaaS subscriptions. Getting sign-off for more is becoming increasingly difficult as businesses seek to control costs and manage shelfware.
- **Missed opportunities:** Customers who don't fit into a prescribed tier are likely to look for alternative providers.
- **Barrier to growth:** Scaled businesses with a static subscription model may struggle to retain or grow market share. They can't monetize new features or functionality if customers are already on an all-you-can-eat package.

How does fixed subscription pricing drive growth?

In order to drive growth with a fixed subscription model, vendors need to add new customers. The only way to drive revenue is to sell the product to more people, as opposed to encouraging more usage within the same customer base.

There are three key metrics vendors should track to understand whether their fixed subscription model is helping them scale:

1. **New Bookings:** this is a forward-looking metric that indicates the amount of year-one recurring revenue the business will earn from contracts signed with new customers in a given period.
2. **Net Revenue Retention:** this indicates the total revenue generated by existing customers in a given period, minus churn from subscription expirations, cancellations, or downgrades. It's a useful indicator of future revenue potential.
3. **Logo Retention:** this indicates the percentage of customers who renewed their contracts in a given period. It's closely aligned to Net Revenue Retention. If logo retention is trending downwards, vendors should seek to understand why customers are cancelling subscriptions. Churn due to high costs, low usage or looking for alternatives with more specialized feature sets are signs pricing may need to be adjusted.

Which businesses should use fixed subscription pricing?

Fixed subscription pricing works well if the product delivers value through individual usage – those that help sales reps or designers work more efficiently or be more productive, for instance. It is not a good fit for products where the value is generated via systems, such as ecommerce or data infrastructure.

Businesses that leverage fixed subscription pricing models include Salesforce, Netsuite, Workday, and Adobe.

"Per seat pricing can increase if functionality is added, and total revenue can grow if your customers are growing their headcount. Likewise, if you charge a subscription based on locations, revenue can grow with added functionality, or locations being added by your customers."

Todd Gardner, Managing Director of SaaS Advisors

2.

CONSUMPTION

Businesses that use this model

snowflake

twilio

elastic

DATADOG

What is consumption pricing?

Consumption pricing has become more popular in recent years, as businesses have looked for ways to add and create value through their pricing model.

There are several different ways to set up and manage consumption models, including credit systems (e.g. 1 credit = 10 API calls), pre-payment limits and pay-as-you-go usage.

However it's structured, the core of any consumption model is that rather than paying a fixed price for a product based on the capacity they predict they will need, customers only pay for what they actually consume. Though payment intervals remain regular, the amount customers pay can vary from period to period.

Example:

PRODUCT	BILLING UNIT	BILLED ANNUALLY Recommended	BILLED MONTHLY	ON DEMAND
Data product	*Per device, per month*	$5	$6	$7.20
Infrastructure	*Per host, per month*	$15	$18	$18
Infrastructure Enterprise	*Per host, per month*	$23	$27	$27
Database Monitoring	*Per database host, per month*	$70	$84	$86
Synthetic API Tests	*Per 10K API tests, per month*	$5	$6	$7.20
Workflow Automation	*Per 100 Workflow Executions, per month*	$10	$12	$14
Cloud SIEM	*Per GB of analyzed logs, per month*	$0.20	$0.24	$0.30
Testing Visibility	*Per active Git committer (3 times per month), per month*	$20	$24	$29

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What are the pros of consumption pricing?

- **Low risk and commitment:** If customers don't use the product, they won't pay for it.
- **Low friction:** Avoids lengthy subscription approvals processes.
- **Reduces churn:** Customers can scale back usage to cut down on costs, instead of churning altogether.
- **Clear correlation between price and value:** Costs only grow once customers see the value of the product and start to use it more.
- **Promotes virality:** No requirement to buy additional subscriptions means more users and teams within the customer organization can use it.
- **Grows revenue:** No subscription cap on spending, or complex negotiations to move customers up another tier. Net Revenue Retention is usually higher.
- **Clear CTAs for customer-facing teams:** Sales and Customer Success teams can refer to usage data to proactively drive conversations around customer usage fluctuations, such as product adoption strategies or renegotiating for higher thresholds.

What are the cons of consumption pricing?

- **Unpredictable cashflow:** Both customer and vendor can struggle to forecast costs and revenues.
- **Prohibitive costs:** Exponentially increasing costs can lead to less, not more usage, if vendors are not proactive about responding to fluctuations in customer behavior.
- **Low commitment:** Customers are not sticky and scalability is hard to predict.
- **Complex to understand and implement:** Accurate metering and billing requires substantial infrastructure investment, which traditional subscription tooling cannot support.
- **Complex sales incentivization:** The size and value of the customer is hard to gauge up-front. Incentivization structures should be designed around ongoing adoption as well as upfront commitment.

How does consumption pricing drive growth?

The Rule of 40 is a popular tool for measuring growth among SaaS vendors, calculated as operating margin plus growth rate, with an ideal outcome of over 40%.

There are two ways vendors can drive growth with a consumption pricing model. One is to add new customers (as with fixed subscription models), the other is to expand within their existing customers by encouraging them to use the product more.

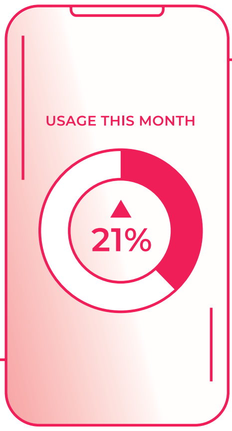
One of the major benefits of consumption pricing is that it allows for frictionless expansion.

Customer usage and revenues may start small, but can expand automatically and exponentially without the need for deal renegotiation. This frictionless growth is particularly profitable for vendors because there are no sales and marketing expenses. Consumption pricing models are therefore a popular choice among vendors seeking to grow revenue and minimize costs.

Frictionless growth doesn't mean sales and marketing teams can be entirely hands-off. When leveraging consumption pricing as part of a Product Led Growth strategy, sales teams will need to be trained at the outset to ensure they have a strong technical understanding of the product, and can drive adoption. Marketing will also have to build a Product Led Growth go-to-market strategy, and while this makes it easier for customers to grow their own value further down the line, all teams will need to be aligned to Customer Success to help customers thrive and ensure ongoing frictionless growth.

Metrics tracking can be somewhat more complicated for consumption pricing models. Vendors should look to measure:

1. **New Bookings:** while New Bookings are still important, it can be hard to measure because the first year's revenue is unknown at the point the deal is closed.
2. **Expansion Rate:** this indicates the annual percentage increase in revenue being driven by existing customers. A high Expansion Rate suggests customers are seeing value from the product. A low Expansion Rate may mean the product has not achieved the predicted 'virality', or that fear of uncapped costs is limiting usage.
3. **Net Revenue Retention:** Expansion Rate and Logo Churn both impact Net Revenue Retention. It is therefore a more complex metric in a consumption pricing business than a fixed subscription business, because there is likely to be much greater expansion within the existing customer base.



Which businesses should use consumption pricing?

Consumption pricing is best when other value metrics aren't available. It's typically used by businesses whose solutions sit lower in the stack, for instance computing and storage, but is also seen in middleware and applications in growing numbers. Customers understand that those services are valuable and expensive, but they're utilities, not value-drivers. For consumption pricing models to work well, usage needs to be both trackable, and predicted to grow. There's more detail on evaluating usage-based pricing in our blog **here**.

Consumption pricing makes sense for vendors pursuing Product Led Growth strategies. Consumption models enable them to remove barriers to entry, with free or low-cost trials, and expand usage and revenue from there without having to negotiate a deal.

Businesses that leverage consumption pricing models include **Snowflake**, **DataDog**, **Elastic**, **Clickhouse** and **Twilio**.

> *"We typically see use usage or consumption based pricing models if/when: a) consumption is trackable, b) consumption metric is expected to grow, c) down-trade risk is low, d) market acceptance is high, e) there is a clear link to value, f) there is a clear link to cost / other methods have too material a risk of not recovering cost.*
>
> *To effectively implement a usage based pricing model, companies need to think about the different activities required across the business. This includes the impact on the sales organizational structure and specifically the importance of a Customer Success function, sales incentivization, KPI tracking, refreshed sales collateral as well developing a new tracking and billing capability."*
>
> **Avi Sethi, Senior Director at Simon-Kucher & Partners**

3.

HYBRID

According to [research by Openview](), about two thirds (61%) of companies are leveraging hybrid pricing models.

Businesses that use this model

zapier

HubSpot

ATLASSIAN

shopify

What is hybrid pricing?

Hybrid pricing is essentially a combination of subscription and consumption pricing models. Usually, vendors will sell a subscription package with overlaid consumption elements, such as overages or usage-based add-ons.

For this reason, hybrid pricing is sometimes referred to as 'usage-based subscriptions'. Some companies are testing usage-based pricing elements, some have 'largely' usage-based pricing models, and over a third offer usage-based subscriptions.

One way to think about hybrid pricing is as a very sophisticated tiering system. Because there are so many different ways to dice up, repackage and price different elements of the product, vendors can offer a custom 'tier' to suit nearly every market segment.

Example:

FREE	STANDARD	PREMIUM	ENTERPRISE
$0	$7.5	$15.5	BILLED ANNUALLY
per user $0 monthly total	per user $75.00 monthly total	per user $155.00 monthly total	Switch the Billing cycle to Annual to view Enterprise pricing.
GET IT NOW	START TRIAL	START TRIAL	CONTACT US
INCLUDES	INCLUDES	INCLUDES	INCLUDES

What are the pros of hybrid pricing?

- **Security and scalability:** Delivers the security and cashflow predictability of a subscription model, alongside the potential scalability of consumption pricing.
- **Product monetization:** Vendors can monetize their product outside of core recurring revenue, e.g. price core product as a subscription, and supplementary products on a usage basis.
- **Nuanced correlation between price and value:** Complex products may deliver value through both users and usage. Hybrid pricing allows each feature to be monetized most effectively.
- **Larger market:** Wider range of right-sized pricing packages reduces the risk of customers looking elsewhere.
- **New markets:** Repackaging market-specific product features can help vendors reach new audiences.
- **Flexibility:** Customers can dial up or down a tier when they need to, without having to make a big step up to the next subscription tier, or losing control of consumption costs.

What are the cons of hybrid pricing?

- **Complex design:** Difficult to optimally balance subscription and consumption elements. Vendors may give away too much or too little functionality in the core subscription package, curtailing potential growth.
- **Sales challenges:** Selling based on long term value and technical metering can muddy the narrative, and make it hard for customers to predict future pricing.
- **Long sales process:** More stakeholders will need to be involved to clarify and approve metering and costs.
- **Unclear costs:** Understanding how their bill has been calculated can seem like a black box for customers.

"Hybrid models are a great way of having your cake and eating it. Businesses can stick with the 'good, better, best' subscription model, and start layering in usage elements, typically around allowances or bundles. They either allow you to monetize additionally outside core recurring revenue, or use usage to move people up and down a sophisticated set of subscription tiers."

Marek Rubasinski,
VP, Business Development & Partnerships at m3ter

How does hybrid pricing drive growth?

Hybrid pricing models can drive growth in a number of different ways, depending on the different elements vendors choose to leverage, and how they work together. Hybrid models may depend on new customers, expansion within the customer base, or both, and can also open up new revenue streams by enabling vendors to target new markets or segments.

Hybrid pricing models enable vendors to monetize outside of their core product and diversify revenue streams. They offer stability and scalability: subscription elements ensure ongoing financial security, while consumption elements leave headroom for unlimited growth. The recent pivot in the SaaS funding landscape from 'growth at all costs' to efficient growth – where top- and bottom-line growth are balanced – means hybrid pricing models are becoming more popular.

Which businesses should use hybrid pricing?

At scale, the majority of leading SaaS businesses can offer hybrid pricing to serve enterprise clients. Businesses that leverage hybrid pricing models include **Zapier**, **Hubspot**, **Atlassian** and **Shopify**.

HOW TO BEGIN A PRICING TRANSFORMATION

As businesses scale and start to serve bigger customers, it's wise to put processes in place that allow for ongoing adaptation of pricing models.

> *Startups can afford to wait until later in their growth journey to refine their pricing model. Rigorous pricing strategies are a lesser priority than winning early customers and understanding product market fit. Keeping pricing simple in the early days means the widest possible market can access the product, giving businesses the opportunity to gather feedback and understand product value. These insights inform the growth strategy and in turn, the pricing strategy.*
>
> Andreas Panayiotou, Director, Pricing & Monetization at Notion Capital

When to review pricing

So, when is the right time to get strategic about pricing?
There are a few indicators that businesses should assess and adapt:

CUSTOMER FEEDBACK:

If customers tell you directly that the product is too expensive, or start to churn to competitors that are cheaper or cover less surface area, it may be time to consider repackaging and re-pricing.

RENEWALS:

Flexing pricing at the point of renewal can help reduce customer churn. It may reduce revenues in the short term, but provides space for customers to grow in the long term.

NEW MARKETS:

Pricing models that work for one business size, industry or use case won't necessarily work for them all. Different customers may want to consume your product in different ways. Enterprise customers may have more need for cost certainty than early-stage businesses, and prefer a fixed rate element, for example.

NEW PRODUCT LINES:

Product launches are a good time to consider and transition to alternative pricing models. Instead of selling a complete package, you may be able to increase your footprint in certain sectors by repackaging the product into its most relevant feature sets.

How to implement new pricing models

Pricing transformations are whole-business transformations. They're not just technology processes, but also operational and cultural processes – and they don't happen overnight. A considerable amount of operational change management is required, as well as input and collaboration from several core teams.

LEADERSHIP:

Moving to a new pricing model changes the revenue model of the entire business. It therefore needs to be a top-down decision.

PRODUCT:

Metering, tracking and billing usage elements is complex. Careful system design is required to ensure metering is accurate, integrated into your existing systems for invoicing, and transparent, i.e. that customers understand how, why and when they have reached usage thresholds.

CUSTOMER SUCCESS:

Where consumption pricing is concerned, getting customers to see product value quickly is critical to retain them. More Customer Success resources may be required to get new customers onboarded and ramped-up at speed. Customer Success is also a critical stakeholder in managing the transition to a new pricing model with customers. Handled poorly, changing pricing can cause conflict, and result in churn rather than revenue growth.

SALES:

Sales teams will need to be re-trained to understand how to sell, especially if transitioning to a hybrid model where narratives about value and price can become complicated. Margins are narrower where consumption elements are involved, and this can make discounting and deal-closing difficult. Sales compensation needs to be carefully considered and aligned so that sales teams remain motivated, and understand how they will be remunerated.

FINANCE:

Billing accuracy and reconciliation processes need to be flawless to ensure money is not lost, especially where consumption and metering elements are involved. This can be resource-intensive, especially in usage-based pricing models where costs are often calculated and billed manually.

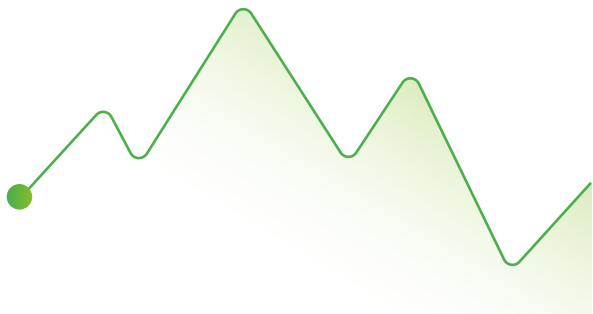
> *If you want to move to a new model, the whole revenue model changes. The decision has to come from the very top, as it changes the monetization plan. It won't happen overnight, and it has to be designed as a solution. Transitioning existing customers to the new plan is a particularly complex balancing act. Nobody wants to lose a customer over a pricing model, so businesses need to work out how best to how to protect them and their revenues."*
>
> **Shah Choudhury, Senior Manager, Pricing Strategy at Salesforce**

Getting started with a SaaS pricing transformation

For SaaS leaders, pricing transformations offer an opportunity to get creative and take control of growth, even in uncertain economic conditions. A thoroughly considered (and regularly reviewed) pricing strategy can open up new revenue streams, and create headroom for ongoing scale in competitive markets.

It's critical to understand the spectrum of different pricing models, and how they connect to business growth. With an informed strategy in place, growth businesses can start to build out the teams, processes and tooling to support it.

m3ter can help.



CONTRIBUTORS

Ariela D Bitran Rich

Monetization Strategy Director at Chargebee

Ariela is the Monetization Strategy Director at Chargebee. She is an expert in Pricing and Packaging Strategy, with 10 years' experience driving top-line growth in B2B settings across a variety of industries. With a passion for educating executives around pricing best practices, Ariela has become an authority on achieving cross-functional alignment to maximize results.

Todd Gardner

Managing Director of SaaS Advisors

Todd Gardner is the Managing Director of SaaS Advisors and the founder and former CEO of SaaS Capital. Previously a partner at Blue Chip Venture Company and a management consultant with Deloitte, Todd has worked with hundreds of SaaS companies across pricing, M&A, metrics, valuations, and more.

Avi Sethi

Senior Director at Simon Kucher & Partners

Avi is a specialist in commercial strategies for business services and B2B recurring revenue businesses, with 8 years experience in consulting and 3 years as a Director of Strategy for a B2B AI business. At Simon Kucher, he is focused on sales excellence and pricing optimization.

CONTRIBUTORS

Marek Rubasinski

VP, Business Development & Partnerships at m3ter

Marek is an experienced commercial, innovation and business development leader in corporates and startups, with a strong understanding of new digital products and disruptive technologies. He previously ran Sky Ventures, a CVC that made investments in and developed commercial partnerships with startups. At m3ter, Marek leads business development, partnerships and strategy work.

Andreas Panayiotou

Director, Pricing & Monetization at Notion Capital

Andreas is an expert in pricing and monetization, supporting exceptional founders on their extraordinary journeys at Notion Capital. He has worked extensively across consulting, corporate and now the early stage B2B cloud software ecosystem, helping commercial leaders to transform pricing capabilities and develop winning monetization strategies.

Shah Choudhury

Senior Manager, Pricing Strategy at Salesforce

Shah helps tech companies achieve top-line growth through crafting SaaS monetization and growth strategies. He has experience working as a strategist, project manager, consultant and engineer across different geographies in four Fortune 500 companies along with leading strategy consultancy Simon Kucher.

m3ter

m3ter powers every variation of usage-based pricing by integrating data, applying pricing, and generating error-free bills for companies at all stages of growth - enabling you to deliver great customer experiences and accelerate revenue growth.

Click here to learn more.