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PRICING LESSONS FROM STARTUPS

An Agile Approach to Pricing Innovation for Large Enterprises

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Using practical, best-practice-based approaches that deliver fast results, he is helping B2B companies - large and small – to sustainably improve their profitability with better pricing.
He provides support and coaching for startups, scale-ups, and other high-growth teams to define their pricing strategies and tactics. He has worked with over 70 fast-growth SMB, many through the Swiss government's Innosuisse startup coaching program.
Among other senior positions, he worked as Head of Pricing for Syngenta, Pricing Transformation Leader for Medtronic and Head of Pricing for Vendavo. Before that, he was a consultant for McKinsey & Co.
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ABSTRACT

Fast-growing Startup and Scale-up companies face many challenges in setting their pricing, most notably a lack of market information and resources. In our work with over 70 fast-growing SMBs over the last five years, we have developed a process to help them quickly define and price their solutions using a structured hypothesis-driven approach. This allows teams to quickly build out offers and pricing models that attract their early customers but also tell a compelling story to their investors.

In this paper, we will explain how pricers and product managers at large corporations could benefit from the techniques adopted by fast-growing SMBs, avoiding common pricing mistakes and driving faster market adoption and higher value capture.

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EPP PRICING PLATFORM®

Getting to and maintaining great pricing outcomes in large companies is hard! As shown in Figure 1, the organisation needs to have the following:

1. VISIBILITY It is essential to have visibility and insights into customer value across multiple product and service offerings, channels and geographies in near-real-time to support effective pricing decisions. In practice, this involves tracking end-customer trends and competitors.

2. CAPABILITIES Distributed commercial teams must have the capabilities to make well-informed pricing decisions at the speed of the market. With specialised teams (sales, marketing, product, etc.) and pricing decisions delocalised across the organisation, needed pricing skills vary by function.

3. CONTROLS Controls must be in place to minimise unnecessary price leakage, drive price discipline amongst decision-makers, and ensure that the implications of key decisions are appropriately evaluated (e.g. low prices that could 'leak' into a neighbouring market). Given the distributed pricing decisions, balancing fine control with agility is often challenging.

4. OWNERSHIP This must all be supported by leadership that takes ownership of pricing: good pricing often requires tough decisions and risk-taking. If you win every deal, pricing is not optimal. Strong commercial leadership is demonstrated by investing in a team of dedicated pricing professionals who are well respected in the organisation and have appropriate tools and systems to support pricing decisions.

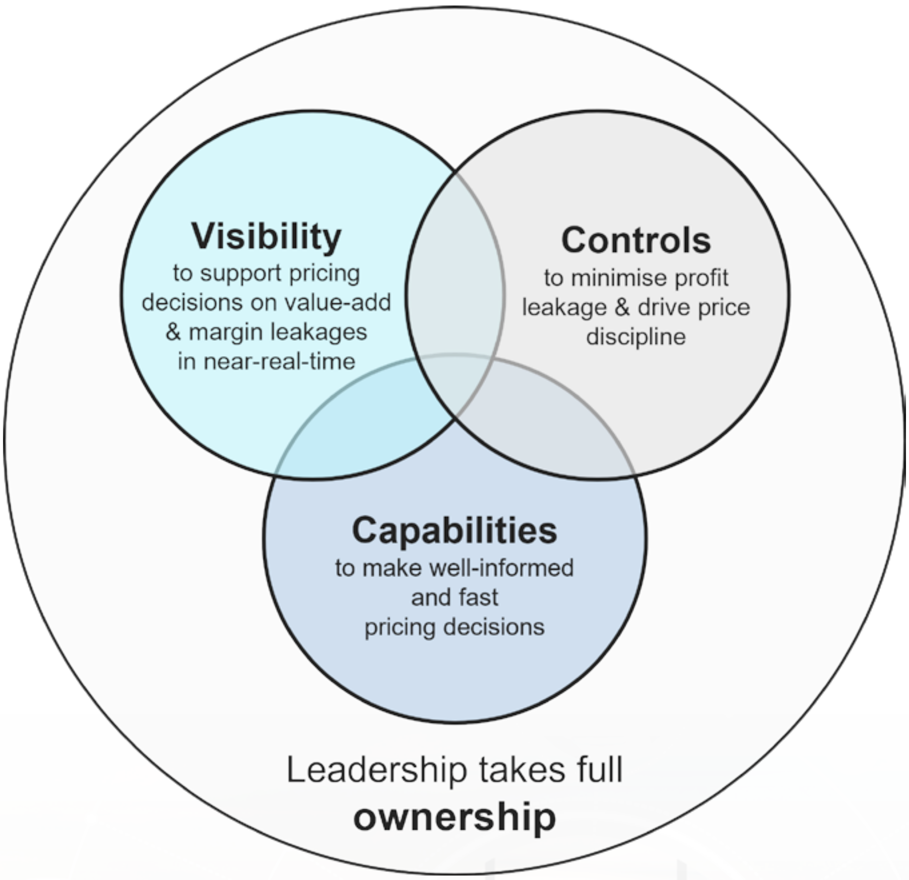


Figure 1
Effective pricing at large companies requires these four elements

However, for high-growth startups and scale-ups, pricing challenges are, in practice, quite different. Hard facts are scarce, as are money and time. The startup emphasis is on moving fast, with broad team skills that are strong where it counts and good enough elsewhere. Small teams mean control is easy, and pricing ownership by leaders is clear, but how to decide on the price model and price points is often challenging.

From our work with innovative startups and scale-ups across all major industries, we have seen patterns that have implications for mature, slower-growth companies, particularly when they attempt to launch innovative and disruptive solutions and business models.

What can mature companies learn from pricing used by startups? We break down the insights into five areas: mindset, process, tools, customer value, and price model design. Note that the recommendations here are far from exhaustive, but rather focus on those areas where mature companies can learn from their younger and nimble competitors.

HAVE AN EXPERIMENTAL MINDSET

Mature companies have the means to access extensive market and price data (even if they sometimes choose not to invest!). However, for companies getting started, and teams driving disruptive solutions, hard data is in short supply, leading them to act very differently. The right mindset means:

- **Be clear about goals and context.**
  Where do you want to be in 5 years' time? What is the value proposition that will get you there? Why is it compelling? What is the 'secret sauce' for your new offering, and how defensible is it? Getting alignment on these questions is key!
- **Take a hypothesis-driven approach.**
  It is so much faster and more efficient to think-through pricing based on assumptions and then validate these key assumptions rather than "boiling the ocean" to see what the data says. Write down the assumptions: this gives your colleagues a chance to challenge them openly, improving alignment and understanding. And, of course, make sure they validate the key hypotheses.
- **Learn by doing.**
  Work iteratively and quickly, trying new things and 'fail fast'. Embrace any failures as an opportunity to learn.
- **Take more calculated risks.**
  While mature companies need to be careful with their brand image in ways that do not constrain smaller companies, taking carefully-considered pricing risks in controlled situations (like smaller markets or customer segments) yields so much information and faster progress.
- **Start focused, expanding the vision over time.**
  Your innovation's business plan may be talking about millions of dollars of revenue from thousands of customers in 5 years' time, but you will get there by selling to one customer first, then the next 10, the next 100, and so on. It is vitally important to understand why those early customers are going to buy your solution.
- **Focus on the end customer.**
  All the value created will start with them. Work backwards from end-customer value.

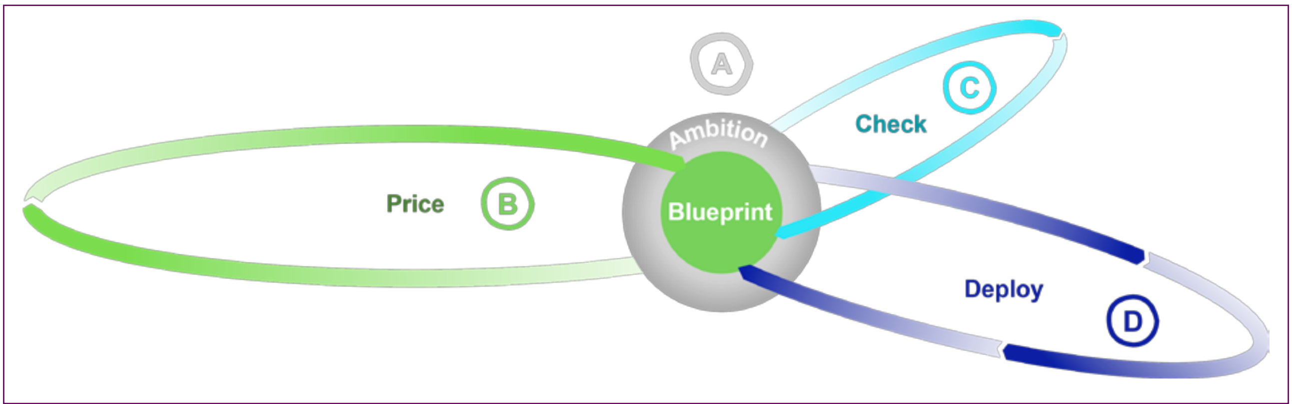
PROCESS

Designing new pricing is different from maintaining existing pricing: there is a much greater level of creativity and risk-taking required, which does not fit well with mature company pricing processes.

With our startups and scale-ups, we use a four-step ABCD approach (Figure 2) that focuses on working on addressing the right questions in the right order and iteratively as new insights emerge.

- Ambition and context. As mentioned previously, this is about ensuring you know what the goals are, what context you are in (both internally and externally), and where you are going.
- Blueprint the pricing design. Coming up with a concrete proposal for pricing will focus the team on the highest-priority assumptions on which the design rests.
- Check key hypotheses. Using a hypothesis-driven approach is efficient, but it is vital that key assumptions are validated before launch.
- Deploy your new pricing. This includes how value and prices will be communicated and how prices to channel partners will be decided.

Figure 2: ABCD process for pricing innovative & disruptive solutions



TOOLS

A couple of go-to tools are particularly helpful for startups before they get to pricing. The first is the Where to Play framework, and it is Market Opportunity Navigator (Figure 3). This helps organisations identify, evaluate, and prioritise opportunities. Using a hypothesis-driven approach is a powerful way to make sure you are going after the opportunities with the greatest potential payback and pricing power.

- Starting with the Market Opportunity Set, based on your technologies and capabilities, list out the possible market opportunities you could address
- For the most interesting opportunities, evaluate them for their potential to deliver value to your organisation
- After prioritising the top market opportunity, identify backup and expansion opportunities that will be kept open, and relegate other opportunities to storage

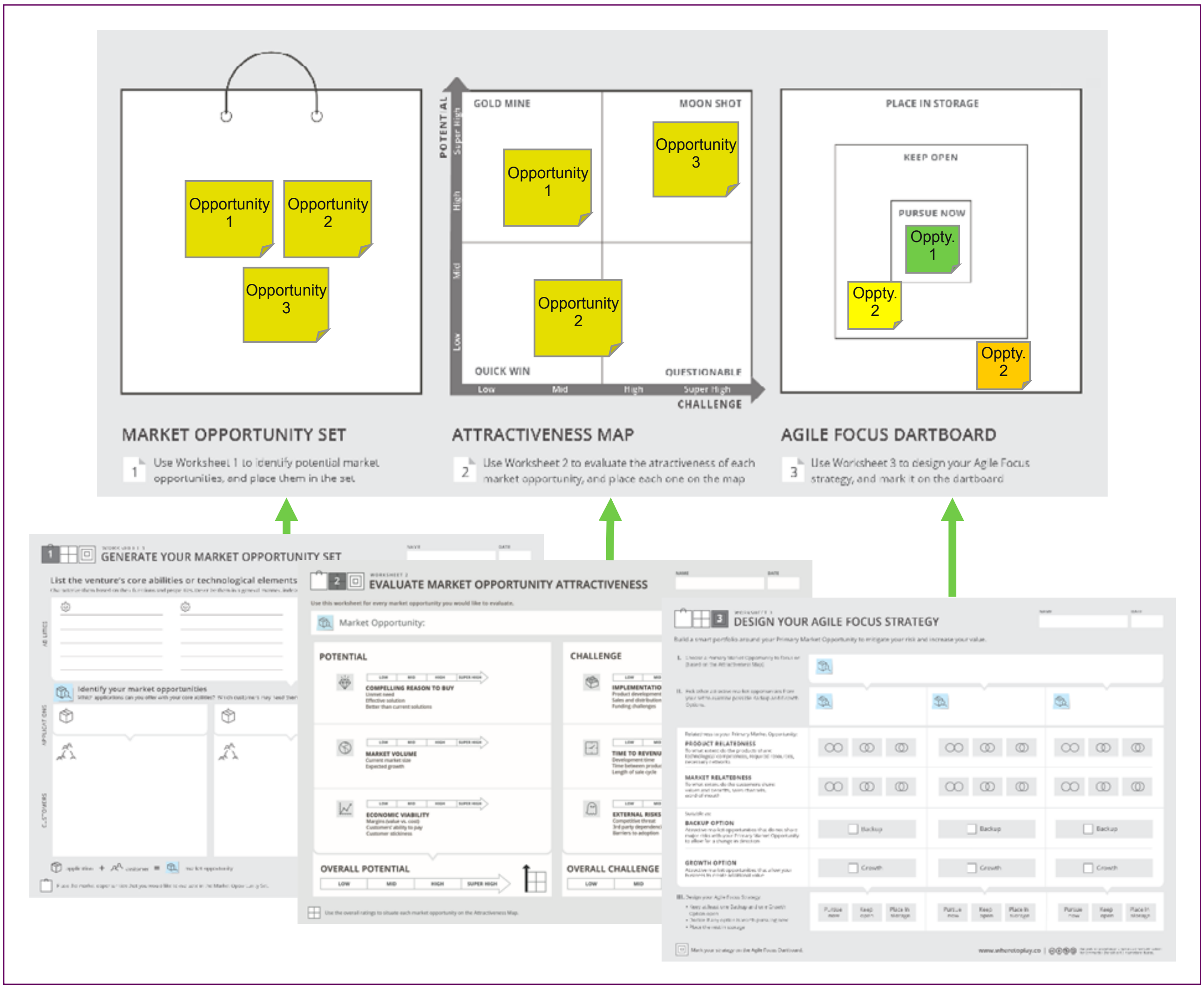


Figure 3 - Where to Play's Market Opportunity Navigator and supporting worksheets

While a simple approach, taking a systematic and documented approach brings a level of focus that eliminates distractions.
Once the opportunity is identified, the Business Model Canvas is an excellent, 1-page summary of how you see the business working. The canvas helps brings clarity to complex business models.

CUSTOMER VALUE

Understanding and playing to customer value should be the key element of all pricing decisions. This sounds very simple, but in practice, there are multiple elements in play. To break this down, walk through the CON-VERT steps to understand how early customers will choose to buy your offering.

CON stands for Customer, Offer, and Next Best Alternative.

Start by describing the Ideal Customer: These are the customers who should be most excited about your offer and whom you should be most excited to sell to. What urgent and important problem are you solving for them? Which stakeholders will be involved? What industry and geography are they in? Are they small or large players in their market? Amongst the best or struggling? Are there any particular technologies they use that make them a strong fit? What is their cultural orientation? How are they going to evaluate and buy your offer? As you can see, initially, taking a very narrow focus ensures you can identify and prioritise pricing for these very early adopters.

Next, we need to outline the Offer for these customers. Again, be specific and detailed. In addition to the core elements of the product, what are the included services wrapped around the offer? Are there any optional products, features, or services they could also choose? Do not wait until the actual offer is fully defined: use your best guess of the early MVP (Minimum Viable Product) and use that. When things change, it is usually much easier and faster to adjust from a specific starting point.

One last step before we get to the customer's evaluation criteria: what will they be comparing our offer to? What is their Next Best Alternative (NBA)? Obvious NBAs include directly competing offers, but for innovative solutions, this might be indirect competitors, self-build solutions, or (most commonly), carrying on as today.

Having defined the initial CON, we move on to considering the VERT. We start with Value but also need to assess the negatives a customer is likely to face with a new solution: Effort, Risk and Time-to-Value.

What is the Value that the ideal customer will get from your offer versus their NBA? Value is a slippery topic that even your customers are likely to struggle to define. In a B2B setting, your new solution can add value in 5 ways:

1. REDUCING THE CUSTOMER'S SHORT-TERM COSTS

Perhaps your solution is just less expensive or requires less setup and configuration or training.

2. REDUCING CUSTOMER'S LONG-TERM COSTS

Electric vehicles fall into this category, requiring much less expensive energy, but savings can also come from reduced operating costs (people) or maintenance.

3. INCREASING THE CUSTOMER'S REVENUE AND PROFIT

Perhaps you help them sell more? Or sell more at a higher price? Alternatively, sell a more profitable mix of their products. Maybe you help them increase customer satisfaction, increasing their customer's lifetime value.

4. INCREASING THE CUSTOMER'S INDIRECT VALUE

Now, things get a bit more difficult to put a price on; these include reduced risk or helping them meet their environmental goals.

5. ASSESS THE CUSTOMER'S INTANGIBLE VALUE

The emotional value of buying something new and cutting-edge fits here, as does the opportunity to improve their personal reputation (and get their next job).

Note that your offer will not be positive in all these areas, and this is not a marketing exercise. Place yourself in the customer's shoes, and document both your advantages and disadvantages. Repeat for other customer segments, offers and NBAs as needed. A clear view of all aspects of customer value is critically important.

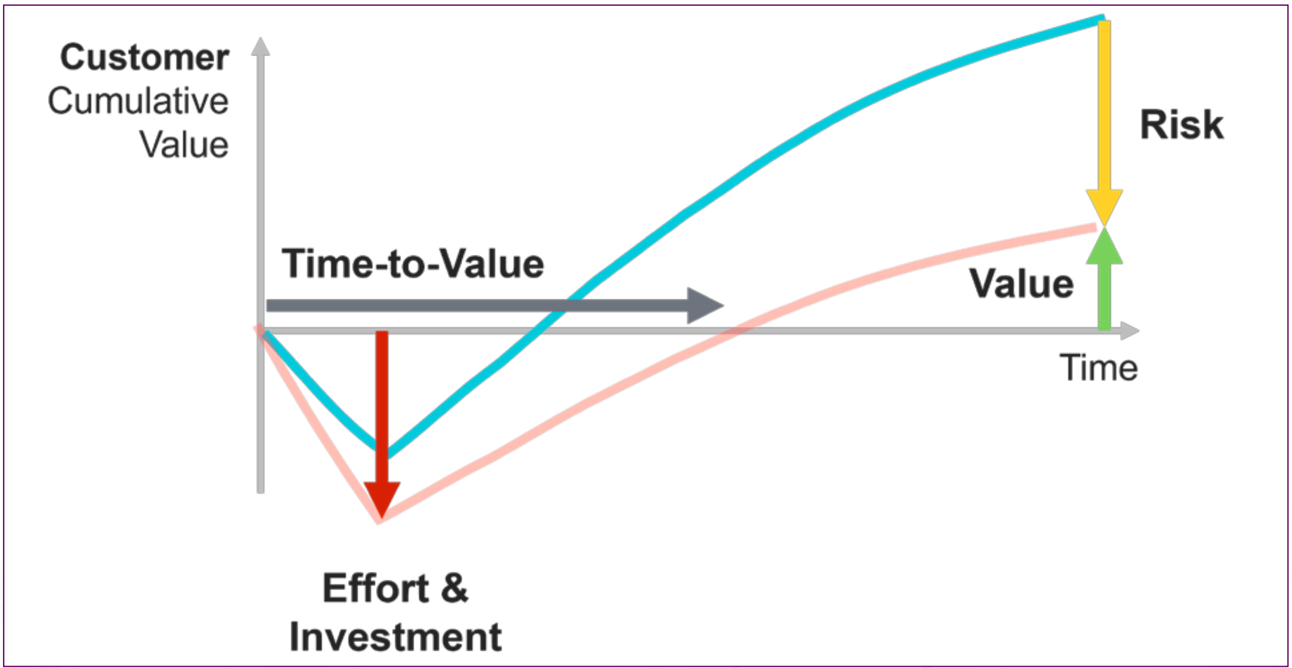
After value, we move to Effort. Almost all innovative solutions require upfront costs, changed procedures, etc., that loom larger in the customer's assessment compared to more everyday purchase decisions.

Risk is the second big factor that buyers consider. While a startup's risks of failure will not be a factor for larger companies, customers have significant fears of change. As a result, they are likely to overweight these compared to the expected benefits. In addition, user adoption, reliability, fitness for purchase, and other factors need to be considered.

The effort and risk can all drive a longer customer Time-to-Value. This tends to increase as the size of the change increases. Unfortunately, many innovators, large and small, fail to assess just how long customers are likely to take before they can see the benefits.

These four factors together create the "checkmark" curve, as shown in Figure 4. Understanding the shape of this curve will allow.

Figure 4
Mapping out the four drivers of customer buying decisions for innovative solutions



PRICE MODEL DESIGN

Now it is time to design the pricing model and set prices. Having understood the customer side of the equation, we use pricing to capture a fair share of the value created (Figure 5).

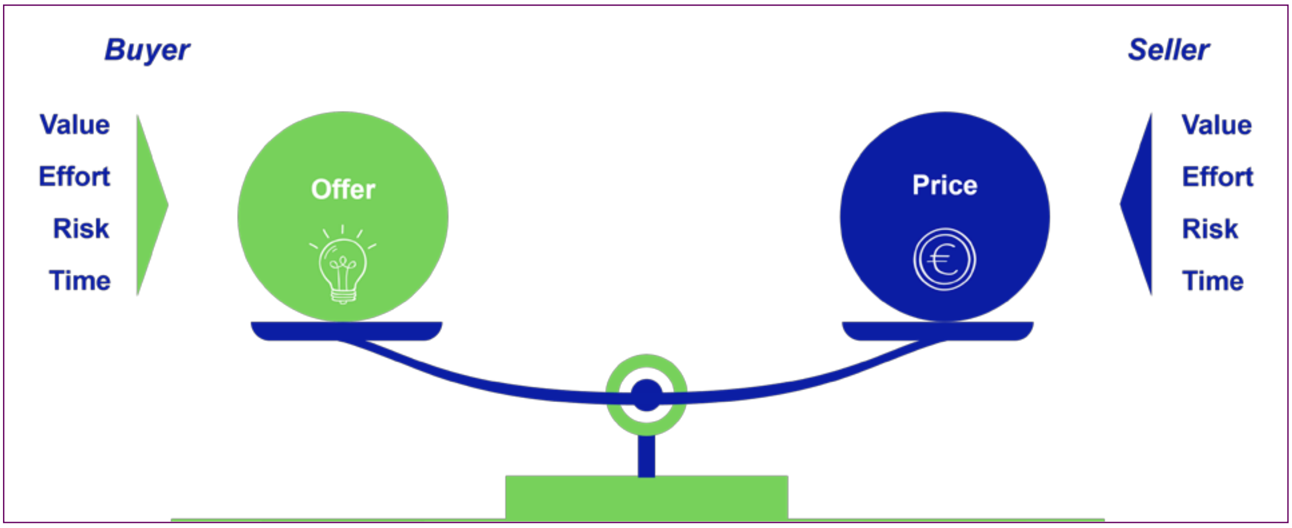


Figure 5: Mapping out the four drivers of customer buying decisions for innovative solutions

The more innovative the solution, the more likely an innovative business model is to make sense. The key element here for startups is deciding what you will charge for - the price carriers. Consider price carriers in 4 groups:

1. Upfront, one-time - capital equipment purchases and initial configuration services and training fall into this category.
2. Subscriptions are set in advance but paid over time based on the planned number of users, or modules, or other metrics.
3. Pay-per-Use is similar to subscriptions in that they are paid over time, but the amount of the payments depends on some metric around usage, like the # of transactions, users, etc.
4. Outcome-based pricing is also set after the fact (sometimes long after the fact!) and is most closely aligned with customer value.

Each of these four types of price carriers has its own pros and cons (generally, value capture potential increases as you go down the list, but so does the effort required, the risk transfer to the seller, and the seller's time-to-value). So, while there is no one 'best' price model, having followed the steps above, you are in great shape to design a price model that balances value capture, effort, risk and time between you and your customers.

CONCLUSION

Large enterprises can significantly benefit from adopting the pricing strategies and techniques used by fast-growing SMBs for pricing high-growth solutions. Embracing an experimental mindset, implementing a structured process, utilising effective tools, focusing on customer value, and designing innovative pricing models can together lead to greater market adoption and value capture for large corporations.

By learning from startups, mature companies can avoid common pricing mistakes and better position themselves in the market when launching innovative and disruptive solutions. In today's rapidly evolving business landscape, taking calculated risks and remaining agile is essential for staying competitive and capturing value.

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