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Don’t overlook your pricing model strategy; your margin is everything!

This week, Caroline Franczia, founder of Uppercut-First, takes us to Las Vegas with Ocean’s Eleven to demonstrate that a well executed pricing strategy is like a good robbery: it takes planning.

With funding on the rise in Europe, startup founders are forgetting the basics; it has become acceptable, if not normal, for a startup – no matter the series – to burn through cash. Worse still, it is commonly acknowledged that they might not be cash flow positive for… a while.

> *Saul Bloom: “I can assure you, Mr Benedict, that your generosity in this matter will not go overlooked.”*

This scares me a bit, because yes, we now have a number of great unicorns in Europe, but valuation is rarely based on actual revenue: it is almost solely based on the amount of money that’s been raised. The press around a startup is also unfortunately much louder after a beautiful round of funds than it is when customers are won.

> *Saul Bloom: "You expect us to just walk out the casino with millions of dollars on us?"*
>
> *Danny Ocean: "Yeah."*

Nevertheless, in the long run, revenue is an essential differentiator. It will decide whether a startup's exit is excellent or average. Metrics such as churn rate, renewal rate, growth, average size, annual contract value, and largest annual contract value are essential in determining true potential, otherwise known as total addressable market.

> *Livingston Dell: "They'll be watching you like hawks. Hawks with video cameras."*

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As a founder, the pressure to:

1. win customers and credibility
2. recruit exceptional talent at the right price
3. determine a long-term roadmap that will differentiate you from competition
4. gain additional market share

5. and manage cost efficiently

is, to say the least, intense.

In my humble opinion, you can reduce pressure levels by thinking carefully about a sustainable pricing model early on – a pricing model that should not drastically change after a few years to avoid potentially disappointing existing customers.

> *Terry: “Who the hell is this?”*
>
> *Rusty: “The man who’s robbing you!”*

Margin = revenue – cost

When your story begins, being cash flow positive seems like mission impossible. However, it should be a goal at all times, and for this, you must set the right pricing model from the start. In doing so, consider all of your costs – not just operating costs, but also recruitment, people and scaling costs. Don’t just rely on future funds.

> *Danny:“You gotta walk before you crawl.”*
>
> *Rusty: “Reverse that.”*

Step 1: Ask yourself the tough questions

How many customers do you need at your average ARR to break even? To become profitable?

Is this number of customers reachable? In a year? In 5 years? Ever? How many resources will you require?

Are you measuring other metrics than revenue and new logos quarterly?

Have you appointed a gatekeeper, such as a sales operation professional, to guide you and your team in the proposal process?

How will you invest to grow the customers that you have won and avoid churn? Is this expense (customer success/support) included in your price? Is it valued by your customer?

Danny: "That's why we're going to have to be very careful. Very precise."

Rusty: "Mmm, well-funded."

Customer Segmentation Issues

Price per user per unit (per server, per user, per... use case?) has become the standard. That's ok, provided you set it right.

Problem 1:

You arrive with a solution to disrupt an industry that has an experience of doing things a certain way and is used to a certain price.

Typical behaviour:

You set a very low price that does not differentiate you from your 'old' competition, even if you bring more flexibility, more ease of use, more productivity, more digital, andmore modernity to the table.

Negative consequences:

You need to raise funds until you have won enough customers to break even, diluting your value further.

Danny: "Thirteen million and you drive this piece of *shit cross country to pick me up?"*

<u>Rusty</u>: "[sarcastically] Blew it all on the suit."

Problem 2:

You arrive with a new solution that no one has ever used.ou solve problems but you must educate the market first on why they need you and what you will change for them.

Typical behaviour:

You guesstimate a price, because of the lack of data.

Negative consequences:

The price is often set too low. This allows you to win customers in the short term but means you get caught up quickly by new competition, which does what you do better and faster.

*Reuben: "You guys are pros. The best. I'm sure you can make it out of the casino. Of course, lest we forget, once you're out the front door, you're still in the middle of the f***ing desert!"*

When you set a price, you send a message to the entire market that you target. It tells people who you are, your value, your current and future positioning. It requires a profound transformation, even for a startup, to move from mid market size deals to enterprise size deals. And the issue is rarely that the solution is not good enough or not scalable enough. Rather, the price is often plainly too 'cheap'.

> *Danny: “Cause the house always wins. Play long enough, you never change the stakes. The house takes you. Unless, when that perfect hand comes along, you bet big, then you take the house.”*
>
> *Rusty: “Been practising this speech, haven’t you?”*
>
> *Danny: “Little bit. Did I rush it? Felt I rushed it.”*
>
> *Rusty: “No, it was good, I liked it.”*

Everything is in the price per unit issue

Yes, your solution is a SaaS solution and as such, your customer pays for a service that includes bug fixes, updates and upgrades. It does not, however, mean that all additional features and functions should be included by default. Some of these features (security, privacy, customer success) should be considered as options that allow for additional recurring revenue. The maths is simple: to provide a service of quality, you must hire people – forward thinking developers, caring expert customer success…all of whom are on an annual salary.

> *Rusty: “You’d need at least a dozen guys doing a combination of cons.”*

Here is an industry secret and the conclusion of this message: the ones who make it are never the ones offering the cheapest solutions. If you come in cheap, you are already at risk of churn. If you are cheap and bringing a lot of value you will regret it: soon enough, you will have some serious difficulty in maintaining the same level of service without raising money again. To maintain your value, set the price. It is as simple as that.

> *Rusty: "I need the reason. Don't say money. Why do this?"*
>
> *Danny: "Why not do it?"*

Caroline Franczia is a regular columnist for Maddyness and the founder of Uppercut First. Experienced in working for large companies such as Oracle, Computer Associates, and BMC, Caroline also lived in Silicon Valley for four years before moving to startups (Sprinklr, Datadog, Confluent) where she witnessed on the ground the benefits of a well-thought sales strategy. These are the foundations of UF: a structure that accompanies the European startups in their sales strategy by giving them an undeniable advantage in their go-to-market.

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