

# Freemium Model: A Beginner's Guide to The Freemium Business Model

More and more, the marketing world sees companies shifting away from traditional marketing strategies toward trusting [product-led growth](#).

This approach to marketing aims to build [brand awareness](#) by introducing a high-quality product to a large audience of users. With the right product, the experience speaks for itself.

The freemium business model falls into the category of product-led growth and continues to increase in popularity among internet-based companies. But what is the freemium model, and how can businesses use it to their advantage?

Here, we present a beginner's guide to freemium and how you can start implementing it with your products.

## What is Freemium?

Freemium combines the words “free” and “premium” to describe a particular type of business model.

Companies started using freemium models back in the 1980s, though the term was only coined in 2006.

This unique practice for acquiring users and customers is especially popular among software, internet-based companies, and gaming companies.

In 2019, [54% of app developers used the freemium model](#), with 33% of them generating the most revenue through this practice.

Several well-known companies like LinkedIn, Evernote, and Spotify use freemium as the basis of their business, and its success revolves around customer usage.

It's an acquisition model that brings in users to a new software product and, if used correctly, urges frequent users to upgrade to premium versions.

# How Does a Freemium Model Work?

The basic premise of the freemium model means a company offers a product, often software, with basic features at no cost.

However, this product has limitations that, in some cases, cause the user to want more from the service.

Beyond the free version of the product lies a premium version, with more available resources, services, and advantages if the customer pays a subscription fee.

The freemium model aims to develop a foundation of trust between the customer and the company while demonstrating the value of the offered product.

Users have the opportunity to experience the product in its most basic form for as long as they need in order to understand its value.

While companies anticipate that some people won't upgrade to the premium version, they hope that the limitations of the free product will compel users to pay for the premium version.

## The Difference Between Freemium and Free Trials

Now, many people confuse the principles of free trials and freemium. Free trials often only last a week or 30 days, creating a firm deadline by which the customer needs to decide if they want to pay for the product.

Within that time frame, they enjoy full access to all or most of the product's features and experience its maximum value.

This model has several benefits for companies that use it. With a free trial, companies can generate more revenue; since at the end of the day, they are left with paying users.

A free trial also more effectively converts users into paying customers, with a typical conversion rate of 30% or higher.

The downside of using free trials is the expiration date. Customers can become spooked by the end date

of the trial.

If they don't have enough time to experience the full value of the product in their daily lives, they won't convert to a paying user.

In this case, freemium wins out, since customers can use the free version indefinitely and upgrade to premium at any time.

## **What Are The Advantages And Disadvantages of Freemium?**

Like any business model, freemium comes with upsides and downsides that a company must prepare for. These points may help your company decide if the freemium model is worth it.

### **Advantages**

While freemium does generate revenue in the long run, it works best as a customer acquisition model.

Using it, your company attracts a wide audience of curious users and builds a relationship with them in a pressure-free environment.

Happy users who want more from the product can — when they're ready — then upgrade to the premium version in their own time.

The scale factor of freemium works extremely well in its favor. When users first arrive, they might not need the product's comprehensive list of potential features. As they incorporate the product into their daily life and work, the limitations on the free version become more restrictive.

Customers decide for themselves what functions they need to use, and if their needs evolve, this leads to conversions.

Freemium models appeal to companies who feel comfortable foregoing traditional marketing tactics and allowing customers to take on marketing responsibility.

Users learn about the product through first-hand experience, then refer it to others who might need it, generating invaluable brand awareness.

Remember, as a customer acquisition model, freemium should attract users without your marketing team expending too much time or energy.

While converted users generate revenue, the free version of the product still allows companies to collect user information and data.

This gives insight into user habits and interests. Companies can then show targeted ads to generate more revenue and enhance the application with newfound knowledge.

## **Disadvantages**

One particular downside of freemium concerns a company's resources. Free users, while helping to serve as an unofficial marketing team, also put a strain on server space and customer service.

Your company has to prepare for the cost of supporting a majority of free users with the revenue earned through few paying customers.

The main drawback to freemium, though, is that free users may never decide to pay for the premium product.

Companies have to strike a careful balance between offering just enough services to hook people without providing too many benefits in the free version.

Certain factors out of your control might also lead to low conversion rates. Luckily, there are tactics you can implement to convert a free user into a premium one.

## **How to Convert a Free User to A Paying User?**

Since freemium revenue hinges on conversions, you need to know the right strategies for nudging free users toward premium products.

To start, make it abundantly clear how users can benefit from premium by spotlighting key features with in-app prompts, notifications or emails. If customers don't know what they miss out on by only using the free product, then they will never convert.

Next, carefully select the right limitations to put on your free product. To better understand this, look up companies like yours that use a freemium model and take notes on how they approach it.

You can also assess where your customers find the most value in your product and advance from there.

These limitations should cause just enough frustration among users that they want to pay for upgrades, but not enough that they abandon your services altogether.

You want them to experience the value of your product and understand the potential they could discover with premium.

Conversion rates for freemium usually fall between 2% to 5%. This, coupled with lots of traffic, is the balance you want.

## **How to Build a Freemium Model For Your Company?**

Freemium models inherently have tiers of services. A company might have a basic, advanced and premium product, letting customers decide based on their needs which they want to use.

If you want to create a freemium model for your business, examine how you would divide your services into appropriate tiers.

Start simple, with one key difference between your free and premium product, and enrich the premium features as your business grows.

Your company should expect to adjust and innovate the features offered with each product as time goes on.

For example, plenty of traffic is a good sign. However, if it doesn't lead to conversions, you have to cut back on features available to free users.

These adjustments serve as a healthy and productive response to product performance. Ultimately, with research and care, you will achieve that ideal balance between traffic and conversions.

## **Knowing if a Freemium Model Works For You**

Your decision to implement a freemium model depends on the specific goals of your company.

If you've recently started out with the hopes of gaining brand awareness or acquiring new customers, a freemium model could serve you well.

On the other hand, if you mainly want to generate revenue and [increase conversion rates](#), other viable business models can help you achieve those goals.

Freemium also thrives when used with particular services and products. High-quality products that attract a wide customer base while remaining low on cost are perfect candidates for a freemium model.

Services that people use on a consistent basis, whether for work, entertainment, or creative hobbies, also do well.

Since you would put the emphasis on [customers engaging](#) with your product on their own, without additional customer service, also consider whether your product is intuitive to use.

## What Are The Best Examples of Freemium Models?

If you believe that a freemium model would benefit your business, you have different options you can pursue depending on your product.

The most traditional choice puts limits on available features, as we've discussed before, and users have to pay for supplementary services.

You can also opt to limit the capacity for free customers to use your software, which works well if you offer storage space.

If you provide services to other companies, you can create tiers for your products that focus on the size of the business using them.

Maybe the small businesses choose the free option, and as their brand grows, they will feel the need to upgrade to premium services.

Another popular option incorporates ads as a way to generate revenue. The premium services, in this

case, include an ad-free experience.

## Examples of Companies that Use Freemium Model

A lot of software, gaming, and internet-based companies opt for freemium business models, including Spotify, King, Hinge, Slack, Asana, and Dropbox.

Spotify might count as the most successful one, with an incredible [45% conversion rate](#). For comparison, Dropbox boasts a 4% conversion rate among its users.

With Spotify, the difference between their free and premium services feels like night and day.

Free users can stream most albums, playlists, and certain radio stations on shuffle play, with ads every few songs. These users cannot skip to specific songs they like, a limitation that proves effective at reminding people what they lack without premium.

Premium users, though, can select the song they want to listen to, skip as many songs as they like, experience better sound quality and have access to offline playlists.

For people who want to discover new music and want to have control of their experience, these upgrades are well worth it.

Dropbox also represents a successful example for freemium. Back in 2008, the company established itself mainly as a service for backing up files.

Now, they offer a basic plan with [2G of storage](#), in addition to personal and business tiered products, with free trials for their business versions. The limitation on storage and other services compels users to upgrade to more comprehensive plans.

Developing the right marketing strategy and business model can revolutionize your company.

**And, if you want to keep learning [the best conversion techniques](#), download now our complete guide on the theme!**