Freemium Model in Cloud Computing

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Abstract

Software as a Service (SaaS) is the most mature and popularly adopted cloud services, and freemium is a widely used business model in SaaS. Freemium, combining "free" and "premium", involves giving away for free a certain level or type of consumption, while making money on premium consumption. For example, SaaS vendors offer their basic version products for free while they charge for the premium features in their full version products. Many SaaS vendors have jumped on the freemium bandwagon fast. However, not every companies work the freemium model successfully. The conversion rate from free users to paying customer are typically very small, roughly 3%~5% in successful cases. Many companies found the "freemium" strategy is turning out to be a costly trap, leaving them with higher operating costs and lots of freeloaders.

SaaS vendors thus, are eager to know how to increase the conversion rate. What are the key factors that make free users become paying customers? What are the key differences between the two groups? How do the two groups of users see their SaaS products or services differently, in terms of quality, value, and satisfaction? To what extent should the quality or functionalities be embedded into free version to appropriately convert free users to paying customers? To answer these questions, this study builds on IS success model, which provides a theoretical foundation to understand the relationship between software quality, perceived value, satisfaction and customers' intention to pay. Our study aims to explain a phenomenon that can't be answered well by extant literature: why some users perceive high value of SaaS, are satisfied with SaaS, but they still have very low intention to pay for SaaS.

Our study departures from extant SaaS literature by proposing two user specific characteristics -- *fit* and *price consciousness* that will moderate the well-examined relationships in the IS success model. Different from extant studies that argue each of the perceived benefits, user needs, or satisfaction simply has a direct impact on users' intention to pay, our study proposes that it is the "fit" between users' needs and perceived value that will determine users' final intention to pay. Moreover, users' price consciousness will strongly moderate the impact of user satisfaction on their intention to pay. We plan to empirically test our proposed model by collecting 638 SaaS users.