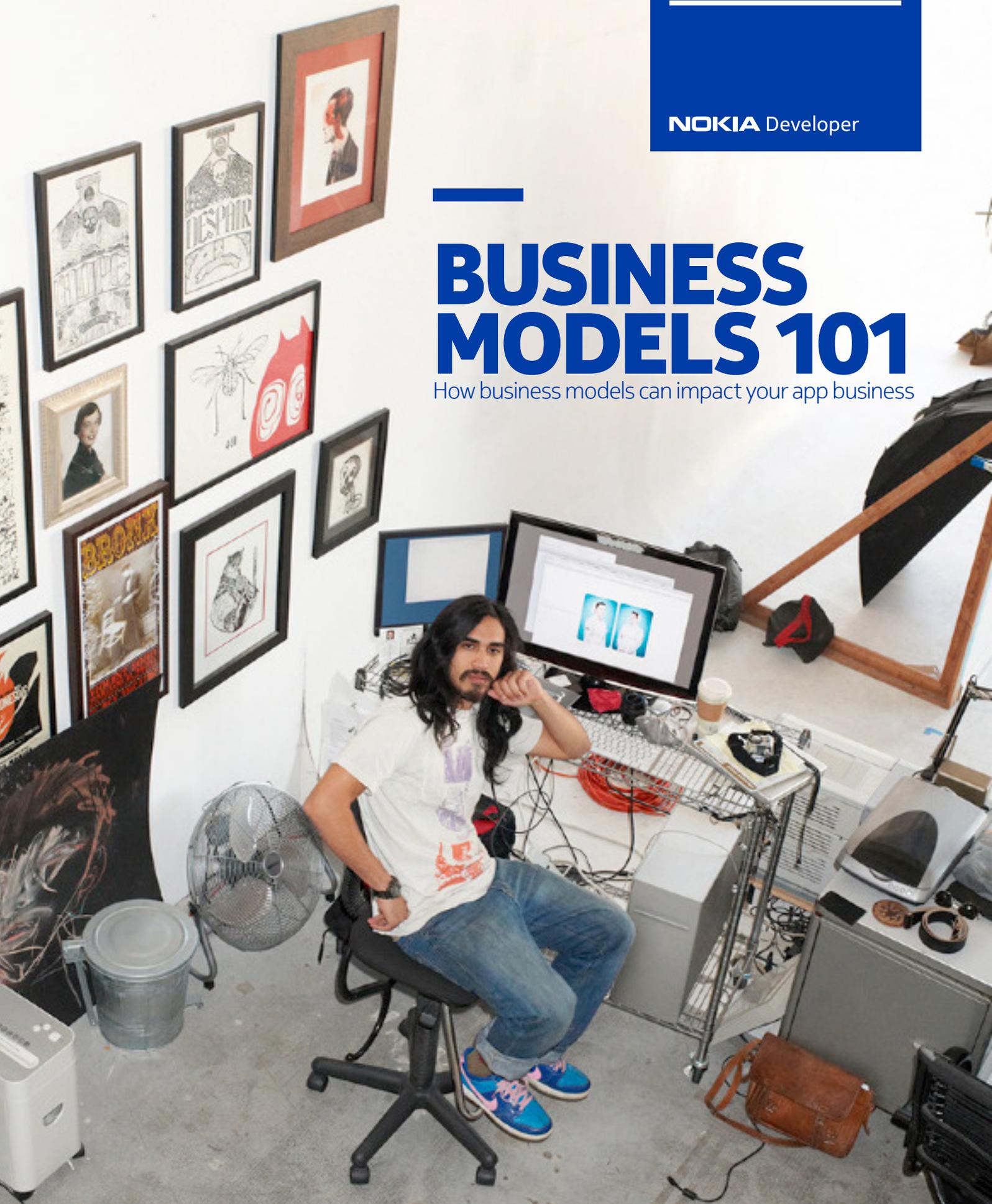


INSIGHTS AND
MASTERCLASSES

NOKIA Developer

BUSINESS MODELS 101

How business models can impact your app business



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BUSINESS MODELS 101 — How business models can impact your app business

Evolving business models and customer reactions to app prices.

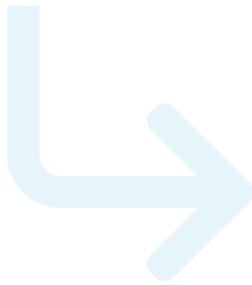
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01

BUSINESS MODELS — what they are & what they do

Business models for mobile apps are increasingly coming under the spotlight as developers ask how they can make money in such a competitive marketplace. At the heart of the question lies the business model, and which one is most appropriate for a particular app, at a particular time.

This report will go into detail about the pros and cons of different business models and offer practical tips to help developers choose the best one for their app.



“This is an exciting area right now. As everything moves into mobile, it opens up opportunities for different business models and room for experimentation. It’s a pretty exciting time as everyone tries to figure out how to participate and position themselves in the mobile space”

— **Saul Kaplan, Business Innovation Factory**

A business model describes how an organization creates, captures and delivers value to its customers – basically, it is the way in which the business intends to make money.

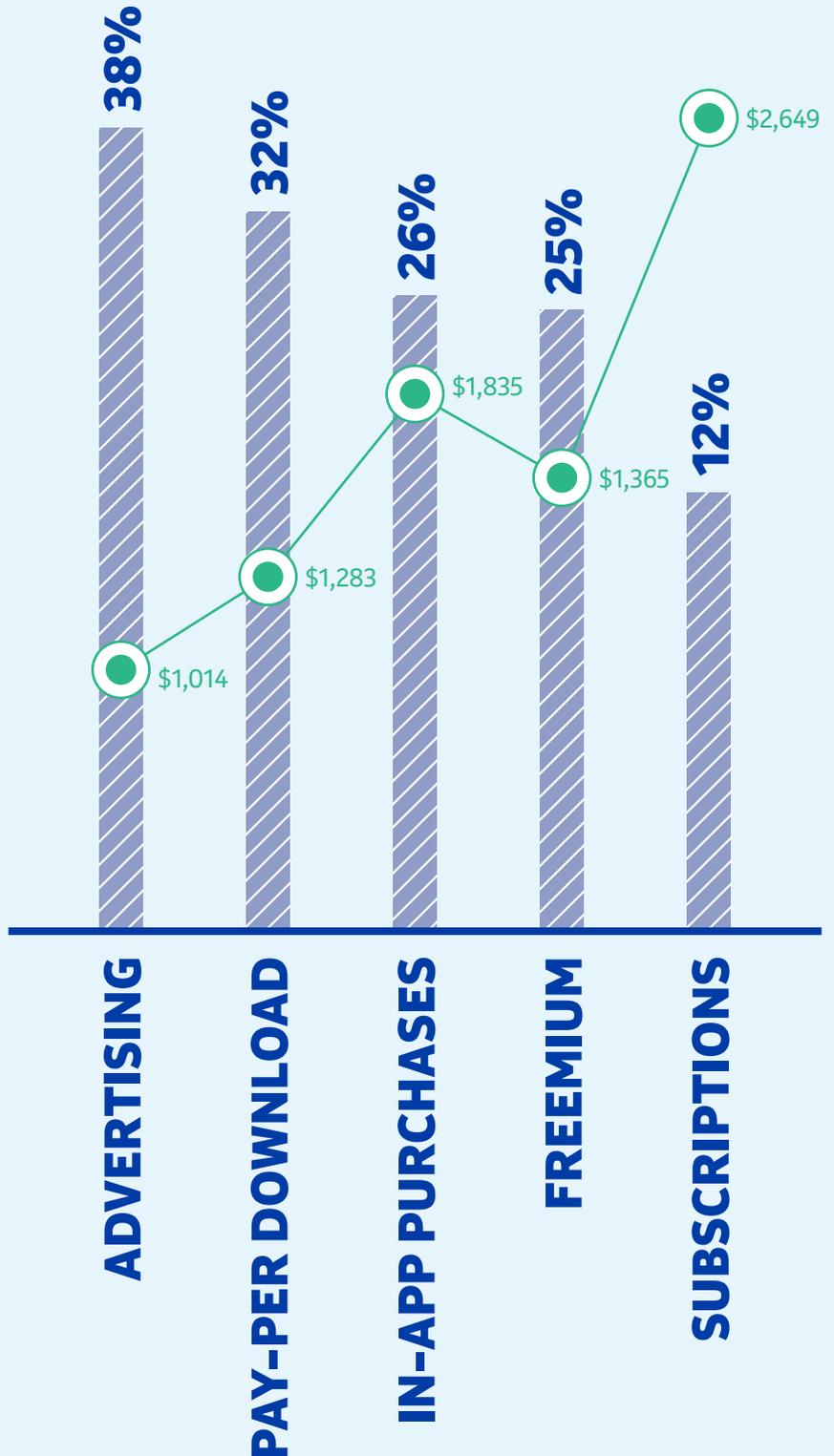
02

Types of business model

According to Developer Economics 2013, advertising is the most popular revenue model, having overtaken pay-per-download. But it makes less money than other revenue models, bringing in on average \$1,014 per app, per month. Subscription-based apps bring in the highest revenue per app, per month - \$2,649.

\$2,649

Subscription-based apps bring in the highest average revenue per app, per month

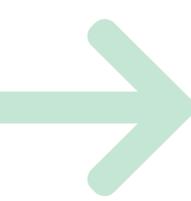


Popularity of business models¹

 % of developers using each revenue model

 Average revenue per app, per month

1. Vision Mobile 'Developer Economics' (2013)



\$1.7 BILLION

In 2012, in-app advertising revenue rose to \$1.7bn across USA and the major western European markets, overtaking revenue from display ads on the mobile web (\$934.5M). Global advertising revenue through mobile grew 85.4% between 2011 and 2012²

In-app advertising

'Sticky' apps can gain revenue by displaying advertising within them.

 If the target audience is broad enough, there is serious money to be made from this business model.

 But it is important to remember that in-app advertising can make for a bad user experience. One way to get around this is to offer a paid version of the app, without advertising. In-app advertising is also much more unpredictable than some premium models due to variations in advertising spend, types of user and the app category.

In-app advertising also allows developers to use innovative advertising networks which offer users more – and so create more chances to earn revenue. Tapjoy for example allows users to select personalized adverts offering virtual rewards or premium content. SponsorPay goes a step further – it is a value-exchange advertising platform that combines brand engagement, user acquisition and direct response ad campaigns.

Pay-per-download

Users pay an up-front fee before downloading the app. This is one of the most frequently used business models.

 In theory, this is the quickest way to earn money, and climb the top-grossing charts. Developers will not need to interact with third parties, and they can set a price that they deem acceptable.

 But pricing is critical. If users do not agree with the developer's assessment of the app's value, they will not download it.

+27%

The market for paid downloads reached \$8bn in 2012 – a 27% increase since 2011. However, the average revenue for paid apps decreased from \$26,720 in 2011 to \$19,560 in 2012³

Free, free trial/light version

To boost uptake, developers can offer their app completely free of charge, or provide a trial version. The trial lasts for a finite period of time and may have restricted functionality. But developers can drive downloads from the outset, and it is ideal for showcasing the hard work they have put in.

 The major benefit of this business model is that it sidesteps buyer's remorse. If the developer is confident the user will like the app, this is the ideal method of demonstrating how.

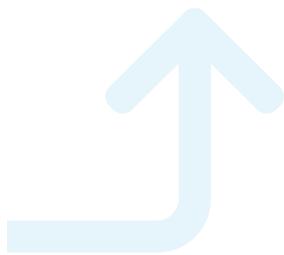
 But it is important to note that users may often feel that the end of the trial spoils their experience and puts them off downloading the full version. The move from trial to paid must therefore be very carefully managed. Users need to be clear about the length of the trial and which functionality if any will be restricted. Users will not like it if the end of a trial period 'creeps up' on them.

2. Strategy Analytics 'Global Mobile Media Revenues To Touch \$150 Billion In 2012' (2012)

3. Research2Guidance 'In 2012 Smartphone Users Spent US\$ 8 billion for Paid Apps in the Top 5 App Platforms' (2012)

\$2.1BN- \$4.8BN

Virtual currency is expected to double between 2011 and 2016 going from \$2.1bn to \$4.8bn



Freemium

The basic app is provided free of charge, but developers charge a premium for advanced features or functionality.



Freemium is particularly attractive because the user escapes having to pay up front for the app, but does not have to worry about a specific date when the app will stop functioning. In most cases, the basic version has a reduced feature set but with enough capabilities to persuade users to download the full app.



The freemium model provides more opportunities to entice users and generate upsell opportunities. But maintaining a balance between the free and paid-for elements is critical. Give the user too little, and their interest may burn out too early. But give them too much, and there is no incentive for them to pay.

In-app purchases

The foundation may be a

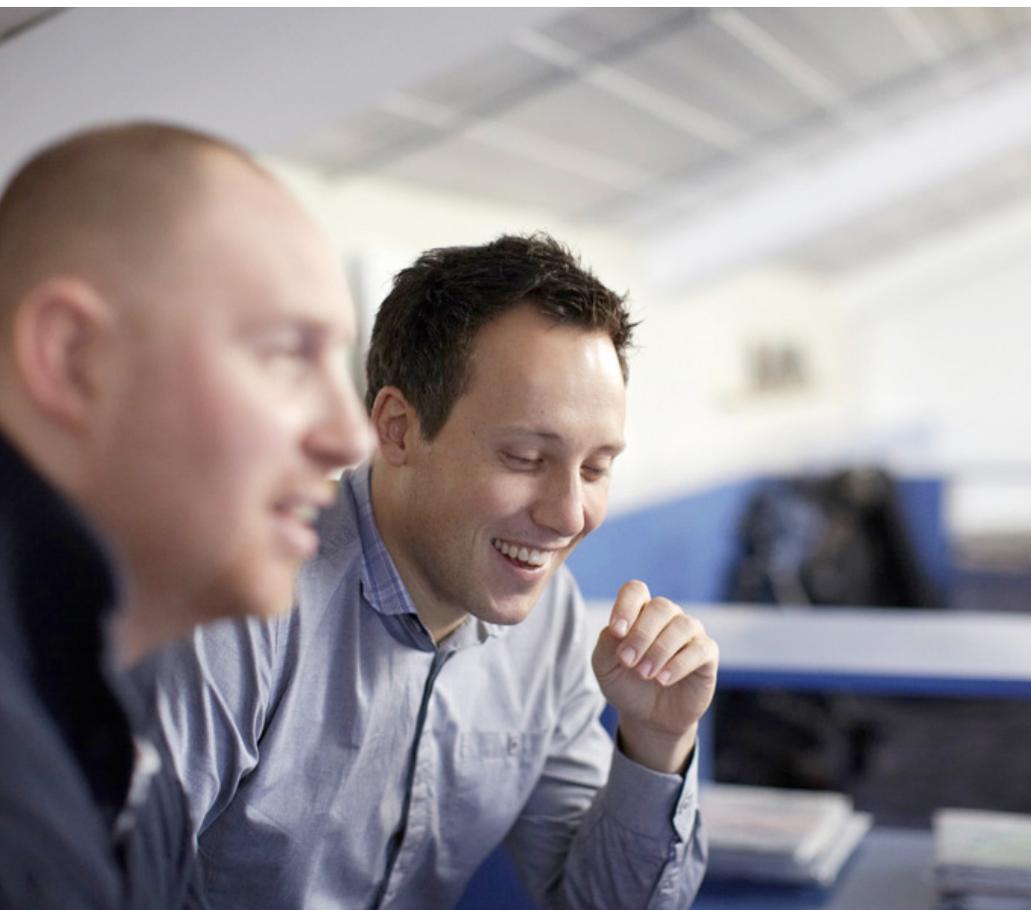
paid app, but is more often a basic free app, with in-app purchases available as higher value additional features. Virtual currency is becoming an important trend in this space, either earned through conventional gameplay over time or paid for with real money. Virtual currency is expected to double between 2011 and 2016 going from \$2.1bn to \$4.8bn⁴. Supercell and My Country are good examples of this.



In-app purchasing is often the best of all possible variations. It breaks down the initial usage barrier and delivers more value on an ongoing basis after the initial download. This essentially converts free apps into apps that can generate a lot of revenue.



The key is to get the correct balance of free and paid-for content so that users want more. Other elements of the user experience can be brought into the game – for example ‘liking’ specific items and sharing stories through social networks can accumulate rewards. But developers must take care not to overburden the user with purchases. They could face a backlash in product reviews if users have to pay too much or too often for essential functionality.



4. Juniper Research 'Mobile virtual currency market to hit \$4.8bn by 2016' (2012)

Subscription

Depending on the kind of engagement an app requires, subscription may be the most appropriate model – weekly, monthly or annually.



Subscription often works in conjunction with content providers.

However, content aggregators and long-tail developers can also use it if there is enough differentiation. Examples of a subscription app would include magazines and more general content but also travel apps, where updated charts and information are regularly made available.



The main consideration is having a big enough brand to justify

charging a subscription in the first place. If there is, developers can get revenue payments on a regular basis, aiding the cash flow for their business. The cost to users can also be spread over time, making individual payments less burdensome.

Indirect business models

Other business models can also generate money indirectly:

- The app as a distribution channel:**
 The mobile app can be just a part of a business's wider portfolio. For example, Lastminute.com uses its mobile app as an additional channel to reach customers.
- The app as a brand and communication channel:**
 Similarly, the app can be used to simply increase the presence of a brand. Apps such as Gucci Style provide a meaningful extension to the existing brand.
- The app is the business:**
 Sometimes, the app itself is the business. For example Task Rabbit, where trusted individuals complete errands for paying customers.

Quick facts

13.4BN DOWNLOADS

In Q1 2013, the top four app stores worldwide accounted for 13.4bn downloads, with \$2.2bn in paid app sales, in-app purchases and subscriptions.

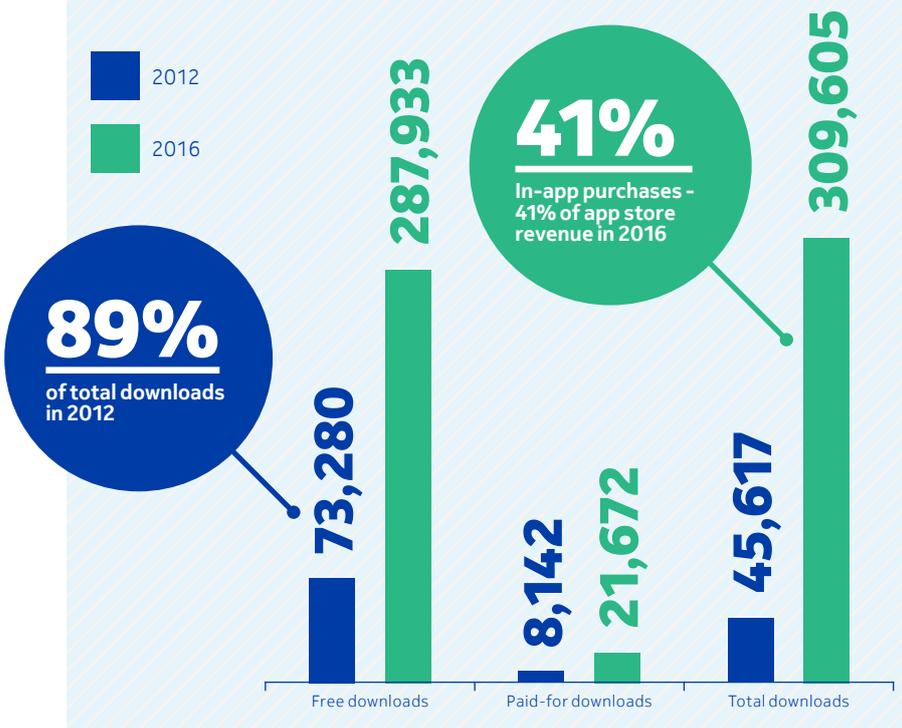
99¢ — \$2.99

Lower priced apps are expected to be more popular in future. Gartner predicts that apps between 99 cents and \$2.99 will account for 87.5% of paid-for downloads in 2012, and 96% by 2016.

76% IN-APP PURCHASE

In-app purchase is the most prolific revenue generator for apps – particularly on Apple's App Store. It has reached 76% of all revenue in the App Store in the US and is above 90% for many Asian countries.

Worldwide mobile app store downloads, 2010-2016 (M)⁵⁶⁷



- Gartner 'Gartner Says Free Apps Will Account for Nearly 90 Percent of Total Mobile App Store Downloads in 2012' (2012)
- Canalys 'App Stores In Q1 2013 Hauled In \$2.2B In Sales On 13.4B Downloads, Google/Apple Duopoly Leading The Way: Canalys' (2013)
- Distimo 'Apps With In-App Purchase Generate the Highest Revenue' (2013)

03

The future evolution of app business models

There are many ways in which business models might evolve in the near future:

PAY-PER-DOWNLOAD

Apps could be bundled together to encourage users to buy more than one at a time. This sometimes happens already, but only at the instruction of the app store. In future developers will have more freedom to explore further options.

FREEMIUM AND IN-APP PURCHASES

Real-world purchases within apps offer further money-making opportunities for developers. A restaurant review app could allow the user to book a table, but if game elements are added, users might be able to win the table at a reduced rate.

IN-APP ADVERTISING

In-app ads could become more engaging with high-quality animation or video. There is also the opportunity to make ads more specific to the user. So they might receive a specific number of messages per session, or exempt themselves from future ads for a limited period by reading an entire web page.

FREE TRIAL / LIGHT VERSION

Offering alternative versions of apps means that developers have to create apps with multiple layers, but apps that are built this way from the start are in a better position to appeal to users. Offering a choice widens the appeal for first-time users and gives them the opportunity to progress to the full version at a later date, when they are ready.

SUBSCRIPTION

In our increasingly choice-oriented world, users could be able to pick specific elements of an app or service to subscribe to. A magazine app could allow users to subscribe to specific categories, columns or even time periods in a year. Students for instance may only be able to afford a subscription during term time, or only be interested in a specific subject.

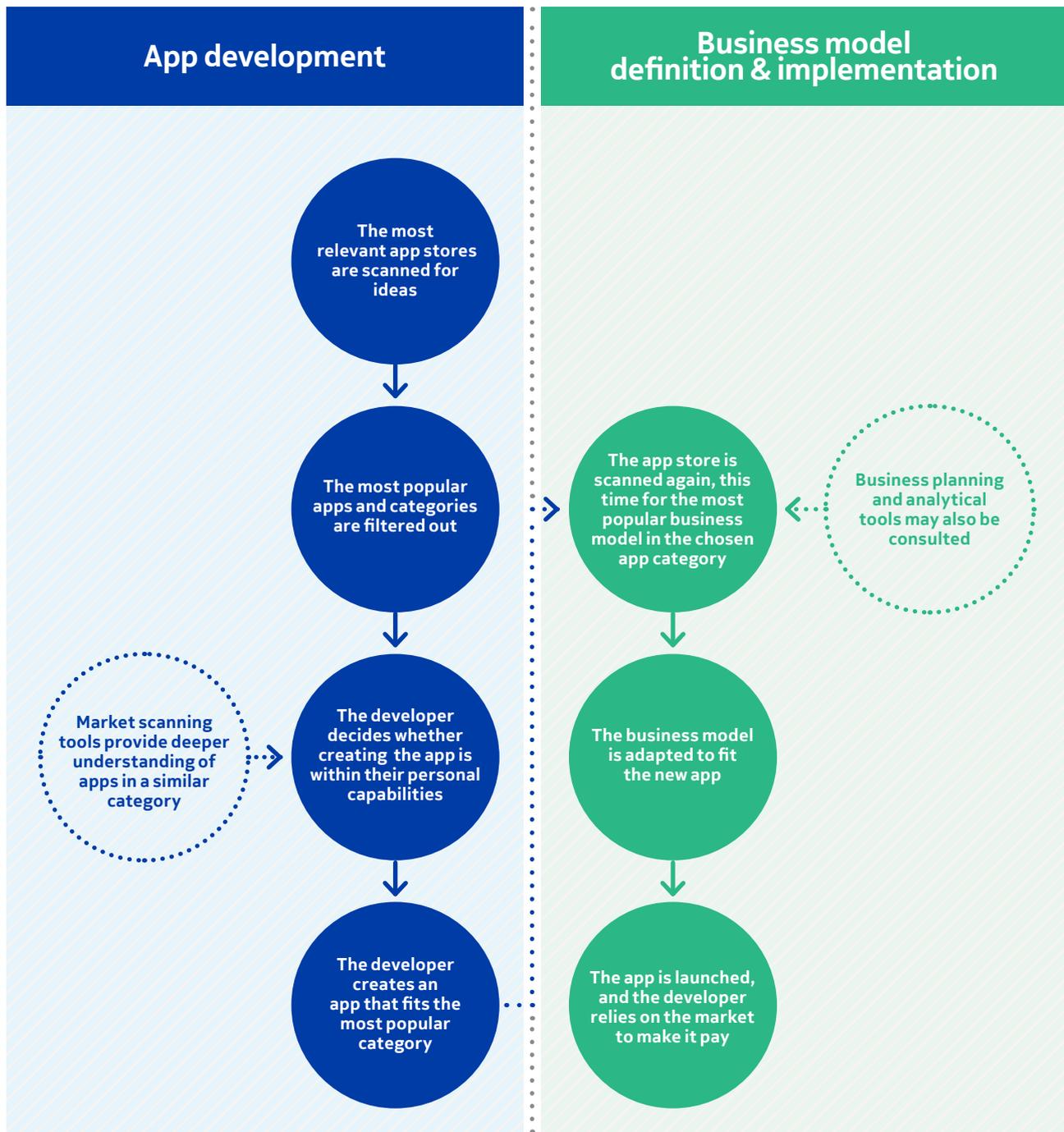
04

Process, process, process

For a lot of developers, the process of choosing their business model is probably not where their passion lies, so they do not spend enough time thinking about it. This diagram shows how developers tend to choose their business model.

This process will be familiar to many developers. But it is an insular view that needs to change – simply copying the business model from the most popular apps is not going to make a new app successful. To break this cycle it is important that developers learn new techniques to develop their business models.

Developers' business model selection process – plenty of room for improvement



05

What happens if you change your mind?

Apps, like fashion and public taste, change with time. User interfaces get better, functionality becomes more intuitive, bugs are ironed out. Equally, business models will change over time and evolve in their own right. Developers therefore have the freedom to

evolve the business model and change their mind if the initial approach does not work. Here are a few examples of apps where business models have changed, for varying reasons⁸.

Avocado

Couples' app Avocado launched in mid-2012, available for download on mobile devices for \$1.99.

Features include couple-orientated messaging, shared to-do lists, a shared calendar, private photos, tight security encryption and an open API for third-party developers.

Free to download

In late 2012, Avocado changed its business model from paid download to freemium. Users can now download the app for free but pay to access additional functionality. A subscription fee of \$19.99 per year unlocks all functionality.

Gears of change

The company had a change of plan because it felt it needed a business model to support the plethora of new ideas it wanted to try, while minimising any impact of these changes on its users.

One of the principles the company has developed is to 'only ask for money after we have fairly demonstrated value to users.' With that in mind, the team changed its model so that users did not have to pay for the app before it actually added value to their lives.

“We changed the business model because of a combination of user feedback, adoption curves, and an increasing understanding of our nascent business opportunity.”

— Chris Wetherell, Avocado



“It’s a longer-term strategy, to be sure, which means financial rewards will be longer to recoup, but we’re already seeing renewed and deepened relationships with our most active customers as a result.”

— Chris Wetherell, Avocado

8. Quora 'Why did Avocado move to subscriptions?' (2013)



Track My Life

The award-winning location-based app Track My Life from Ceseros launched in mid-2012 across multiple platforms. It records users' location every thirty minutes and gives them a map of their travels and overall statistics.

From free to freemium

When launched on the Windows Phone 7 platform, the app was initially free. However, when Windows Phone 8 launched, Track My Life took advantage of the opportunity to incorporate in-app purchases.

Change pays

Track My Life did experience some resistance, with some users expressing their frustration at having to pay for additional elements. But it also experienced a jump in overall purchasing conversion beyond expectations, which were around 1%. After the freemium option was introduced, there was an 8% conversion. The implication is that the payoff behind changing of business models may be worth some of the backlash from users.

8% CONVERSION RATE

“I’m actually quite happy with how it evolved. When I started I expected to get a maximum conversion of 1%. But it turned out that the conversion rate is 8%. Conversions for those who keep using the app are really much higher than that. I’m very happy with this model.”

— Alexander-Derek Rein, Ceseros

06

Choosing the right business model

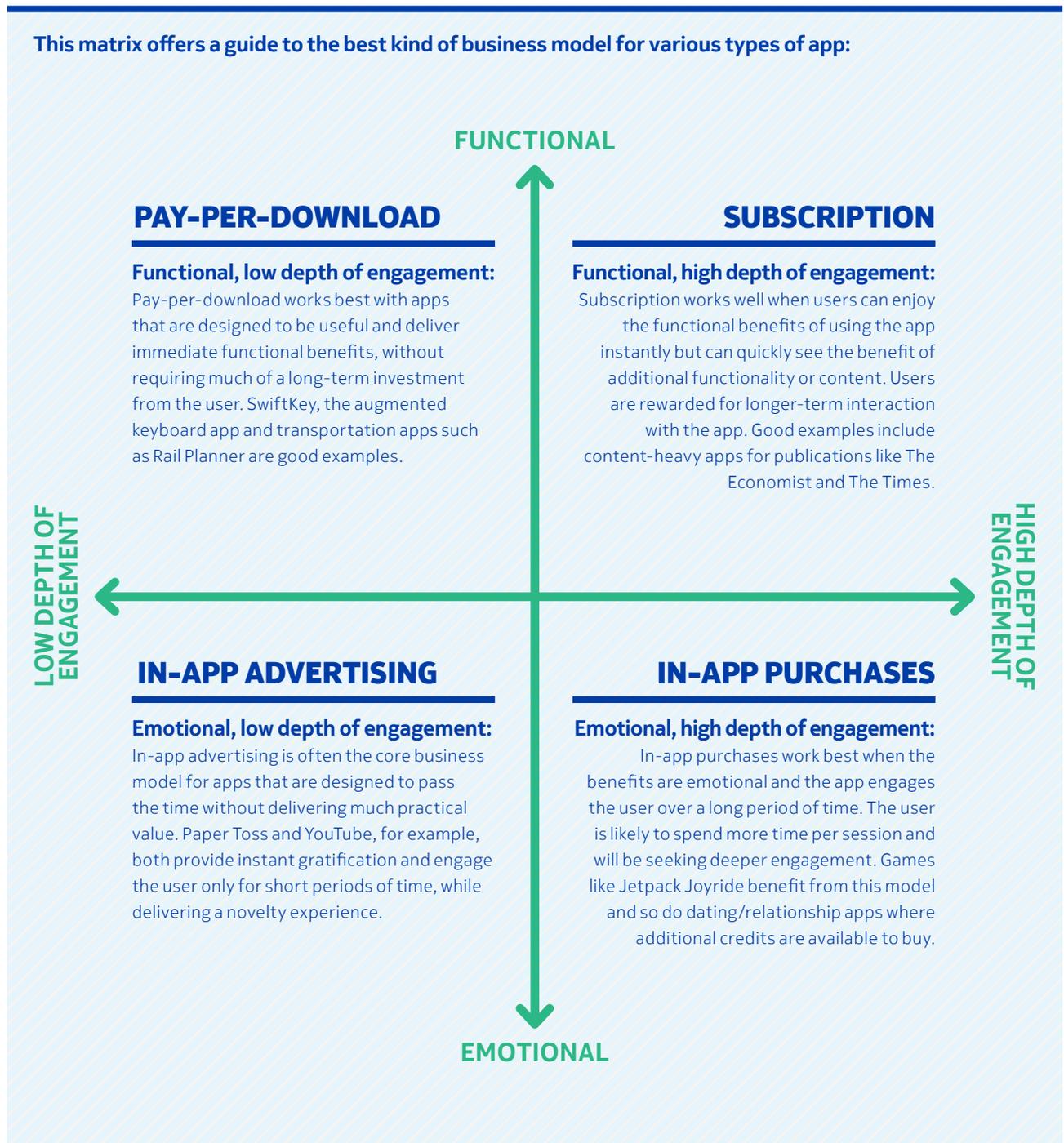
Given the huge amount of information available on business models, anyone could be forgiven for feeling lost when trying to figure out precisely which one is most appropriate for any given app.

Two points to consider are:

01 Functional vs emotional - whether users want the app for its practical benefits (functional) or the sentiments, emotions and engagement it triggers (emotional).

02 Depth of engagement - the propensity for new content or functionality to be revealed over time.

This matrix offers a guide to the best kind of business model for various types of app:



07

As well as considering the pros and cons of each business model how can developers maximize their chances to succeed?

01 Experimentation is key

The business model not only helps developers create and capture value, it should also define the way that value is delivered. Developers must consider how much value is being delivered to the user and whether that delivery method is unique enough. Simply copying an existing business model won't necessarily yield the biggest return. The best app developers experiment, and put themselves in the position of the user. By doing something different, they might just start a revolution.

02 Plan all components of the app

Another important point is not to leave the business model as an afterthought. Granted, each app has different objectives, but for those designed to make money, the business model should be decided up front. At this stage, planning is key and there should be some thought given to the market and whether users will accept the proposed business model.

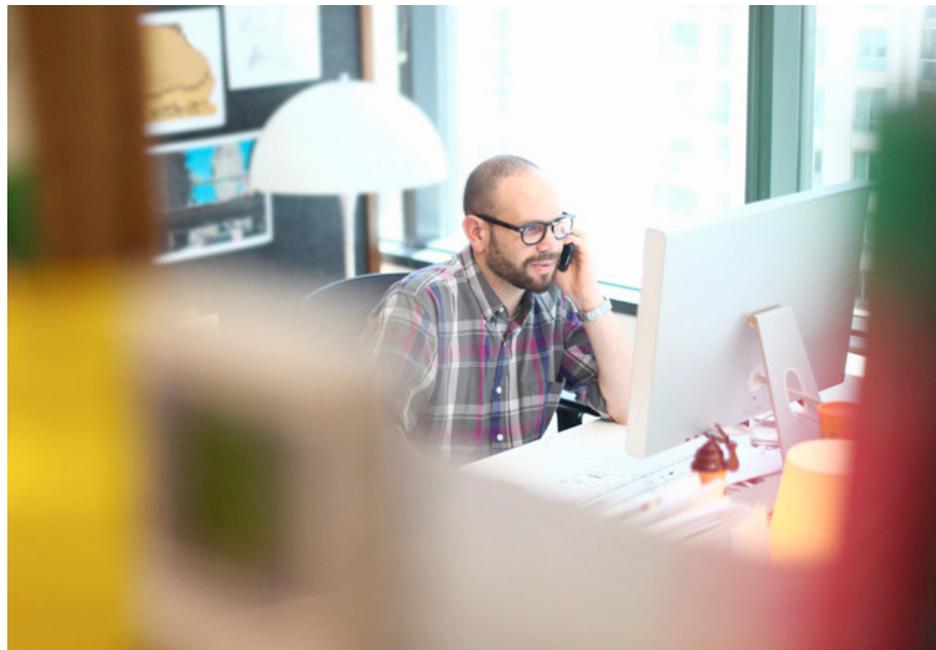
03 Be inspired by the real world

The world of mobile apps does not fundamentally differ from the real world. Developers should look at adjacent industries such as entertainment or retail for inspiration on their business model ideas. The app can be the central point of interaction for users, but it does not have to be the only one.

Implications for developers

“We definitely like to try different things. We try to align our business models with the different app categories and see which model works best in each category. We like to assess and review the different trends in the market and make a decision based on this.”

— Rama Mohan, Stella Nova



“Far too much emphasis is put on the technology or the application itself. Not enough is placed on the business model. I believe that you start with the business model and develop the application to enable it. The app should be designed and built to support the business model. It's really important to experiment and to play with lots of different business model options, to quickly move toward ones that might be stable and scalable.”

—Saul Kaplan, Business Innovation Factory

04 Consider user reactions to app prices⁹

Advertising

WINDOWS

53%

ANDROID

45%

Pay-per download

BLACKBERRY

53%

In-app purchases

APPLE

37%

Freemium

BLACKBERRY

31%

ANDROID

27%

Subscriptions

HTML 5

22%

People's response to pricing is determined by more than the value delivered. Users often have a reference or benchmark price in mind which they use to evaluate the price of any similar product. Discounts, promotions and product bundles can help make apps more appealing and increase uptake. Recent research from Distimo¹⁰ revealed that a drop in price can lead to a growth in downloads of 1665% over a five-day period. On the other

hand, a price increase may lead to a decrease in downloads of 46%.

It is also important to look at how different platforms affect business models. The graph above shows the level of popularity of the models on some platforms. For example, in-app advertising is deployed by 53% of Windows Phone developers and 45% of Android developers – it is a model that is popular with the users on those platforms. Developers can also consider variations to their pricing strategies, though any changes need to be implemented carefully and with a clear view of what they are meant to achieve. The balance between freemium and in-app models is also crucial. Developers have to strike the right balance between paid-for and free components to make sure the free elements drive downloads and usage while paid-for components foster revenue potential for the future.

05 Track and analyse

Implementing business models is a cyclical process. Once they have settled on a model, developers should consistently analyse and try to improve it using intelligence and analytics. Key metrics that should be tracked include:

- **Customer Lifetime Value (CLV)**
- **Average Revenue Per App User (ARPAU)**
- **Conversion rates**
- **Efficiency of promotional channels**

To help analyse the data, developers should devise a simple calculator for the return of revenue on their business model like the example below.

This can help to illustrate the lifetime value of each user and develop a better understanding of the effectiveness of the model:

Freemium Model	Advertising Model
Conversion Rate	eCPM
	Sessions Per User
Paid Price	Ads Per Session
	Ads Per User

9. Vision Mobile, 'Developer Economics' (2013)

10. Distimo 'The Impact Of Price Changes' (2013)