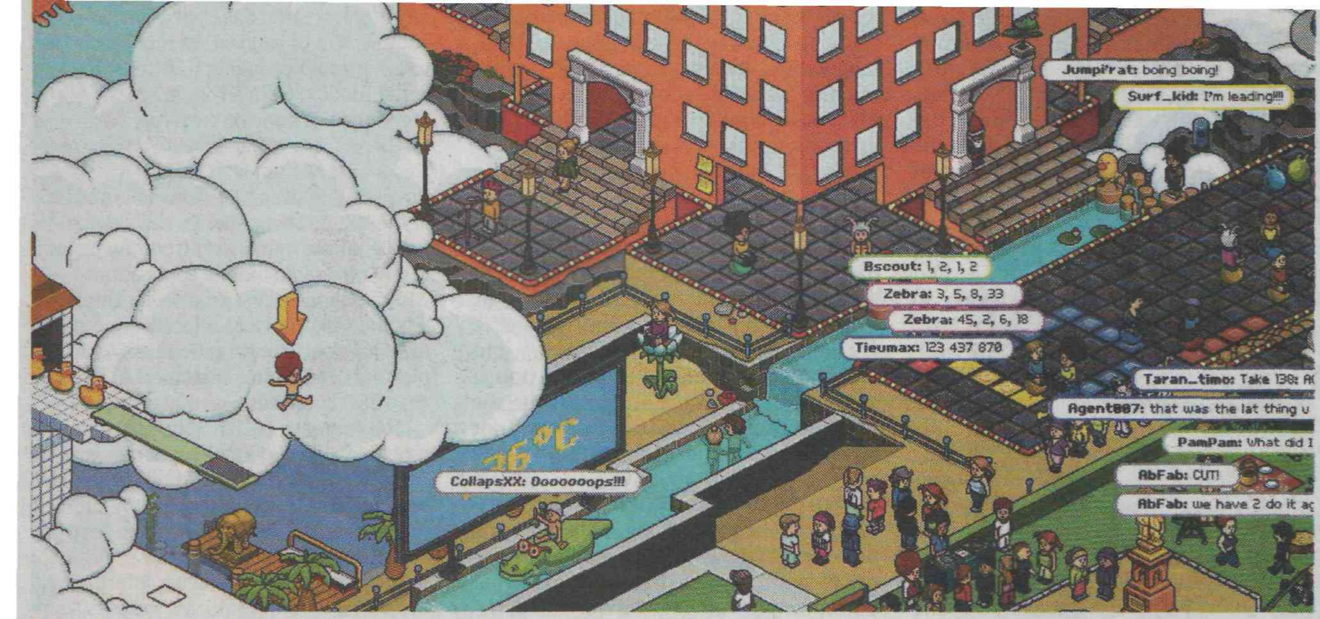

The virtual world, Habbo Hotel, gives away part of its service for free, enticing users to pay for an enhanced experience

Free or fee?

Web-based companies remain reluctant to make their users pay – so how can they secure the revenue they need?

Robert Andrews

The saying "there ain't no such thing as a free lunch" was popularised by science fiction writer Robert A Heinlein. But the science fact is that most of the online services and content we use today are a free ride.

It is a growing trend. Despite pulling in 5% less traffic than transaction-based websites three years ago, free content sites are now 73% more popular, according to data from Hitwise.

Indeed, this article was written using email that's made free by exposing me to ads, and supplied free over WiFi by a cafe happy to satisfy my cappuccino habit. That's the quid-pro-quo of the "cross-subsidies" model identified in Wired editor Chris Anderson's new book, Free: The Future Of A Radical Price, a limited version of which is available to download for free.

But it's something users have been familiar with for all of the web's 15 years in the spotlight, and from the heydays of "shareware" trial downloads long before. By declaring he "will be followed by all the media" in charging for online newspapers next year, Rupert Murdoch is going against the entrenched internet grain. While papers introduce payments, the music business, for example, is going in the opposite direction, making songs free to fans - but funded by ads or small payments - in an effort to stem years of piracy.

But, with so much free stuff, how do developers make money any more? Daniel Ek, chief executive of much-hyped music service Spotify, says virtual world Habbo Hotel, the Red Hat operating system, database platform MySQL and dating site Match.com, which all give away some part of their services to win paying customers, each inspired his quest to give away free tunes - and profit from other income streams.

"We're very much a 'free-mium' company," Ek says. "We do believe that the majority of our users will use our ad-supported service. The big question is, how you package music so that fans are prepared to pay for it? We believe convenience, experience and even, to some extent, exclusivity are the main elements you need [in order] to get people to pay for music again."

Ek hopes mobile applications and early-release albums will convince people to pay £9.99 a month for ad-free streaming. But, so far, a question mark hangs over Spotify's chances of success, which may be supported by a multi-million pound investment and by favourable label agreements as much as by actual fee payers.

In an ideal "free-mium" system, such services would take money from a mere 5% of their users, according to Anderson's thesis. But that's not enough for Rahul Power, who helped develop the partly free mobile music identification application, Shazam, and who now runs his own app consultancy, Apsmart.

"Generally speaking, free is great for people who want to raise brand awareness, usage stats or drive traffic to their site. But, for all but a handful of very sticky applications, monetisation via traditional mobile banner advertising compromises the user experience and does not make real money at this point," Powar says. "Direct monetisation of the app is currently the best way to make money off the property, either via charging [for the] app outright or via subscription if it is a content play."

Until the credit crunch, web services and publishers alike had confidently depended on the boom in online advertising to pay their way. But the ad downturn is now making direct payments a higher priority for proprietors.

Newspapers such as the Financial Times - which gives away 10 free articles each month but is already successfully profiting from its high-end business news with a pay wall costing up to £207 per year - are holding out hope for an iTunes-style pay-per-view payment system, replicating the popularity that has made Apple the US's biggest music retailer and the biggest distributor of mobile applications. But equivalent micropayment technology is scarce and, to many, newspaper articles are not exactly on a par with even the latest JLS single or iFart app.

One thing's for sure - users, especially during a recession, would rather continue their free ride. An Entertainment Media Research study in June found that, if pirated content was taken offline, fewer than half of consumers would start paying for the legal equivalent.

Free fall When is the right time to charge?

Mark Rock, chief executive, BestBefore Media, on AudioBoo

A phone service that lets users upload short audio clips to the web, AudioBoo has been free to its 75,000 users since March. But it is incurring growing bandwidth bills and hopes companies will pay up to £5,000 a year for additional features such as playlists.

Mark Rock, chief executive of developer BestBefore Media, says: "We need the content from the 95% to populate the service and give us the user base to then be able to go to companies, media and brands and charge them for additional functionality like channels or private groups. In the short term, this is through an AudioBoo Pro account. The ink is just dry on me signing the first contract for the Royal Opera House."

Rock also expects 10% of consumer-level free users to take out a £30-a-year Pro account, coming in October.

Andrew Fischer, chief executive, Shazam

The mobile app that identifies song titles by listening to audio had only modest success for eight years, but it doubled its userbase to 35 million between September and May, thanks to its free iPhone app. After that success, Shazam is now charging BlackBerry users £5 and Nokia users £4.

"Due to the many mobile platforms we support and the inconsistency in billing capabilities across different app stores, we run a variety of business models with advertising-funded versions of our application as well as paid-for services with additional features," says chief executive Andrew Fischer.

"The paid model tends to be more profitable today, given mobile advertising is still relatively immature, but it remains to be seen how the free model will play out in the long run as the advertising market begins to pick up."

Jof Arnold, entrepreneur and co-founder of GymFu

Unlike many iPhone apps, which tempt customers with free demos, all bar one of Jof Arnold's five personal workout assistants sell for £1.79 on iTunes; there's no "lite" version in sight.

"We're not about one-off app sales," he says. "While sudden App Store success would provide us with extra capital, which is always welcome, it's more important, long-term, to serve and communicate with a small band of loyal users. We chose £1.79 as a price point that not only reflected the great value we're offering but put us out of the £0.59 bargain-basement apps that get lots of installs but few active users. I'm pleased to say our users are very active. But I would not recommend this strategy if you wanted to make a quick buck from the app store." **RA**

Jof Arnold will speak at next month's Tech Media Invest event in London