WHITE PAPER

Why Pricing Optimization can be a Financial Lifeline for FinTechs

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Introduction

Pricing has a direct and material impact on a company's objectives, making it one of the most potent value creation levers. Despite its critical nature, many organizations struggle to implement a successful, analytics-driven pricing approach, particularly those in complex and rapidly evolving industries. A primary example is undoubtedly the financial services industry, where fast-growing innovations, digital technology and information processing have transformed the core business of traditional banks. This has also generated opportunities for new entrants to deliver expanded sets of products and attract new customer segments, enhancing their experience and affecting behavior. In fact, this has led to a reshaping of the entire market structure.

FinTech companies have experienced a boom in recent years, but the arrival of challenging conditions has added pressure to those that are yet to adopt an effective pricing strategy. This article explains why formulating a thoughtful, intentional pricing approach is an essential value creation lever for FinTechs, especially given the macroeconomic conditions impacting the industry today.

Section 1. The FinTech industry is in a rough patch

In 2021 the FinTech industry saw a massive influx of capital pouring into companies of all subsegments and stages, with 25% more deals than in 2020. However, data registered up to June 2022 suggests a very different picture is unfolding in the current year with FinTech funding already down >20% by Q1 and projected to continue its downward trajectory.

Higher interest rates, cost pressures from economic uncertainty, and fear of an impending recession have had outsized negative implications for the FinTech industry. Reduction in valuation and funding has led to pressure to launch viable products on a shorter capital runway. Products like BNPL have struggled immensely given their business models and dependency on lower interest rates. In anticipation of cost pressures and a possible recession scenario, some FinTech players have started to announce significant layoffs of their workforce this year, laying off around 20-40% of their staff in some cases.

The confluence of these factors results in a challenging environment for FinTechs to succeed, and the need becomes imperative for industry players to double down on identifying strategies to reliably improve their financial positions. Yet many FinTech companies are very shy to adjust pricing due to several main reasons:

- **Overestimated customer price sensitivity –** many think "in a dog-eat-dog market if prices are raised, clients will flee"
- **Lack of pricing transparency –** most CEOs know their sales volumes for last month but have no clue how to measure price realization or productivity
- **Technology and data limitations –** tech stacks are not ready to execute personalized pricing and there is a lack of real data from past experimentation to enable risk / propensity based pricing

Section 2: Pricing is an important lever

Pricing is one of the most powerful value creation levers: pricing impact is material and directly affects the bottom line. A robust pricing strategy can deliver a rapid and high return on investment compared to more capital and resource intensive transformations. Pricing to value in the short term defines whether a FinTech can close a key deal; in the long term, it defines whether a FinTech can build a sustainable business model and long-term profitability.

Companies are often biased towards volume and capturing share and tend to underprice their offerings. This is often due to companies overestimating customer sensitivity and underestimating their differentiation. A commodity mindset sets in, even in differentiated market leaders.

This often results in a balancing act where FinTechs underprice their offerings to aid customer acquisition from traditional brick and mortar financial services providers, while attempting to navigate a shorter capital runway precipitated by higher interest rates and decreased funding.

An additional nuance to consider is the inherent differences between B2C and B2B pricing. In B2C pricing there is limited one-on-one negotiation while B2B prices are almost always negotiated, leading to all flavors of bespoke pricing and price leakage. In many cases products themselves are also customized for B2B versus mores standardization for B2C, further impacting the pricing discipline.

A comprehensive pricing strategy can help to thread this needle by reorienting the enterprise on capturing the full value of their products and services. Prior BCG pricing engagements have shown that enhancements to Packaging & Pricing models can drive revenue growth of anywhere from 7-25% based on experience with clients, with Revenue Management further impacting the bottom line by 2-8%. Pricing work for wholesale banks has seen NIMs increase by 25%; and on the retail side 20% higher net risk adjusted income with differential pricing.

Section 3: Pricing frameworks & opportunities in FinTech

Our robust opportunity set of pricing levers allows for an organization to capture benefits from various angles of their pricing strategy (see Exhibit 1). Pricing can be utilized for multiple business reasons, further determining which specific lever will be most effective. A few examples may include:

Achieve higher price productivity:

- Raising overall prices - *based on the perceived value of your product to customers, driving up the list price*
- Rationalizing discounts - *especially in the B2B world*
- Pricing model - *changing the basis of pricing or the underlying monetization model when it works to your unique advantage (e.g., bps per transaction to bps per AuM or vice versa)*
- Optimizing price discrimination - *by customer segmentation, recognizing that all clients are not equal and their price elasticities vary*

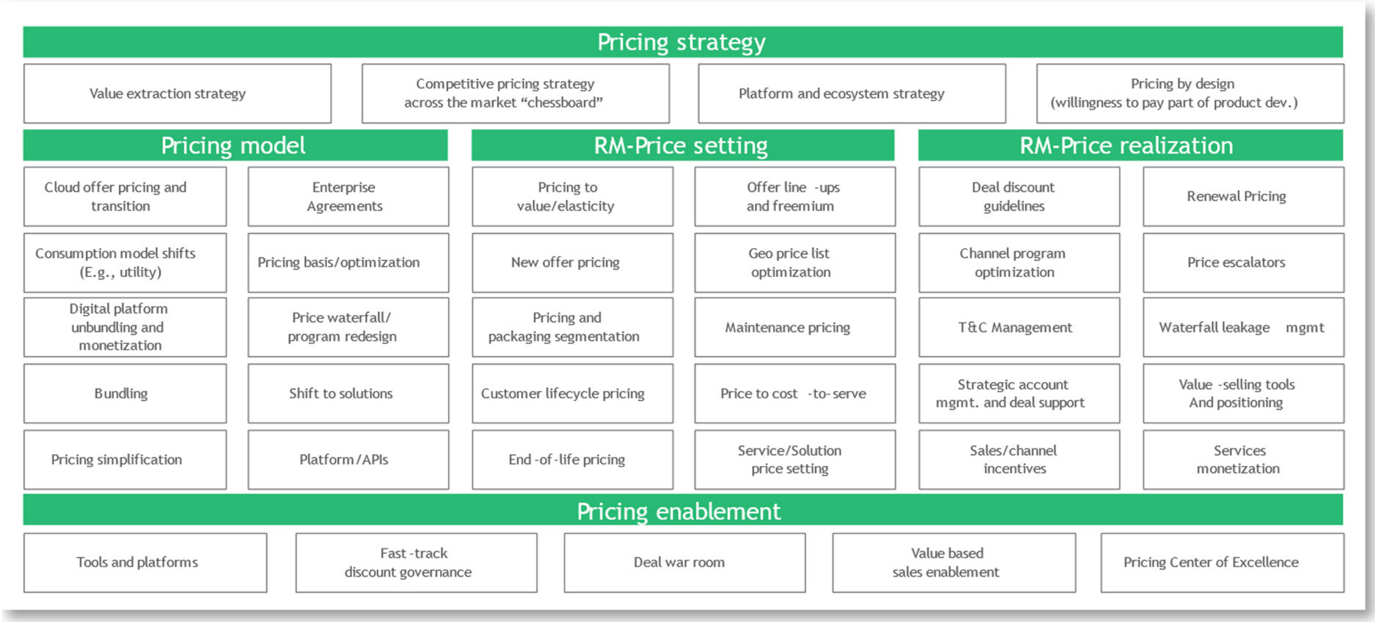
Deepen wallet and increase customer stickiness by selling the full franchise:

- Pricing & packaging architecture - *how you modularize, tier, and bundle your offers in a way that customers perceive significantly more value from a higher bundle while the incremental cost remains low for providers*
- Monetization strategy - *what you choose to monetize and what you choose to give away for free to drive adoption of higher value services*

Smoothen revenue profile:

- Pricing model - *changing the basis of pricing from price per widget to price per subscription for example*

Exhibit 1: Battle-tested pricing framework and range of levers for consideration



3.1 Case Studies:
Some examples of BCG work in the FinTech space

BCG has firsthand experience identifying pricing opportunities and delivering pricing solutions for clients across the FinTech and broader Growth Tech space, giving us an expansive view of industry best practices with material impact on our clients. Below are three examples of prior BCG engagements where a refinement of pricing strategy delivered long term value.

In the case of a leader in the merchant acquiring industry, BCG explored paths via a pricing strategy to enhance revenue growth in a context where an inconsistent pricing model was in place. The pricing strategy was not aligned to customer's KPI and incentives, lacked pricing tools with clearly defined guidelines, and was open to discretionary changes from the sales and retention teams, which created large price dispersion for like-to-like merchants. BCG designed a new pricing strategy leveraging deep analytics to inform definitions of merchant clusters and aligned senior leadership by coaching, training, and enabling the team on a new playbook on pricing tools and merchant communications. By the end of its implementation, our client calculated a revenue uplift opportunity of over ***10% of in-scope revenue net of negotiations and attrition***.

BCG engaged a SaaS market leader facing significant pricing complexity and delivered a simplification of their SaaS pricing model to increase annualized contractual value. This effort had three main goals. First, simplify and future-proof the pricing model by reducing the types of pricing meters from more than 20 to 4. Second, develop a pricing model and a strategy for monetizing high-value transactions. And third, create an enterprise subscription agreement to improve and accelerate enterprise-wide adoption and cross sell. At the end of its implementation, ***our client saw more than a 12% increase in annualized contractual value***.

As a third example, a leading provider of property, mortgage, and consumer information, analytics, and intelligence services engaged BCG to explore the feasibility of a subscription model pricing shift from a regulatory and market participant perspective. Based on a baseline analysis, internal SME interviews and belief audits with market participants, one major business unit and several specific products were identified as the greatest near-term opportunity for a subscription shift. ***42% of the in-scope revenue was shifted to a subscription model, significantly enhancing the revenue profile and cash flow.***

Section 4: What it takes to capture the benefits?

Multiple paths exist for FinTechs considering a pricing recalibration. To start, an in-depth pricing diagnostic should be launched to identify whether and where there may be pricing opportunity. Some key attributes of the business that suggest an opportunity include:

- Price variability across customers – *do you have customers quite similar in nature paying significantly different amounts due to contract negotiations, special discounts, sales practices, timing of customer acquisition, etc..?*
- Leakage in price waterfall – *what are the key sources of leakage in the price waterfall overall and by customer, are they being actively managed and minimized?*
- Under-managed price ladder – *is pricing appropriately tailored to align with value by segment? Is there adequate differentiation, upselling, tiers, ..?*

Additional pathways to revamping a pricing strategy include a pricing model redesign, consisting of applying the levers discussed above and developing a detailed pricing model with several options to back test against historical data. This approach typically requires significant collaboration and workshops with key stakeholders.

However, even the best laid strategies do not translate into results without a robust implementation roadmap. In crafting the way forward, consider a pilot or phased approach to ensure the direction is sound. Do not underestimate the importance of a test and learn, experimental approach. Place a premium on trainings and communications to achieve internal alignment. Ensure managers do not underestimate the importance of people, processes, and tools.

The time to act is now. Identifying shortcomings and developing a data-driven, thoughtful approach to achieve sustainable pricing can truly be a lifeline for FinTechs in this time of economic turbulence. To learn more please do not hesitate to reach out.

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