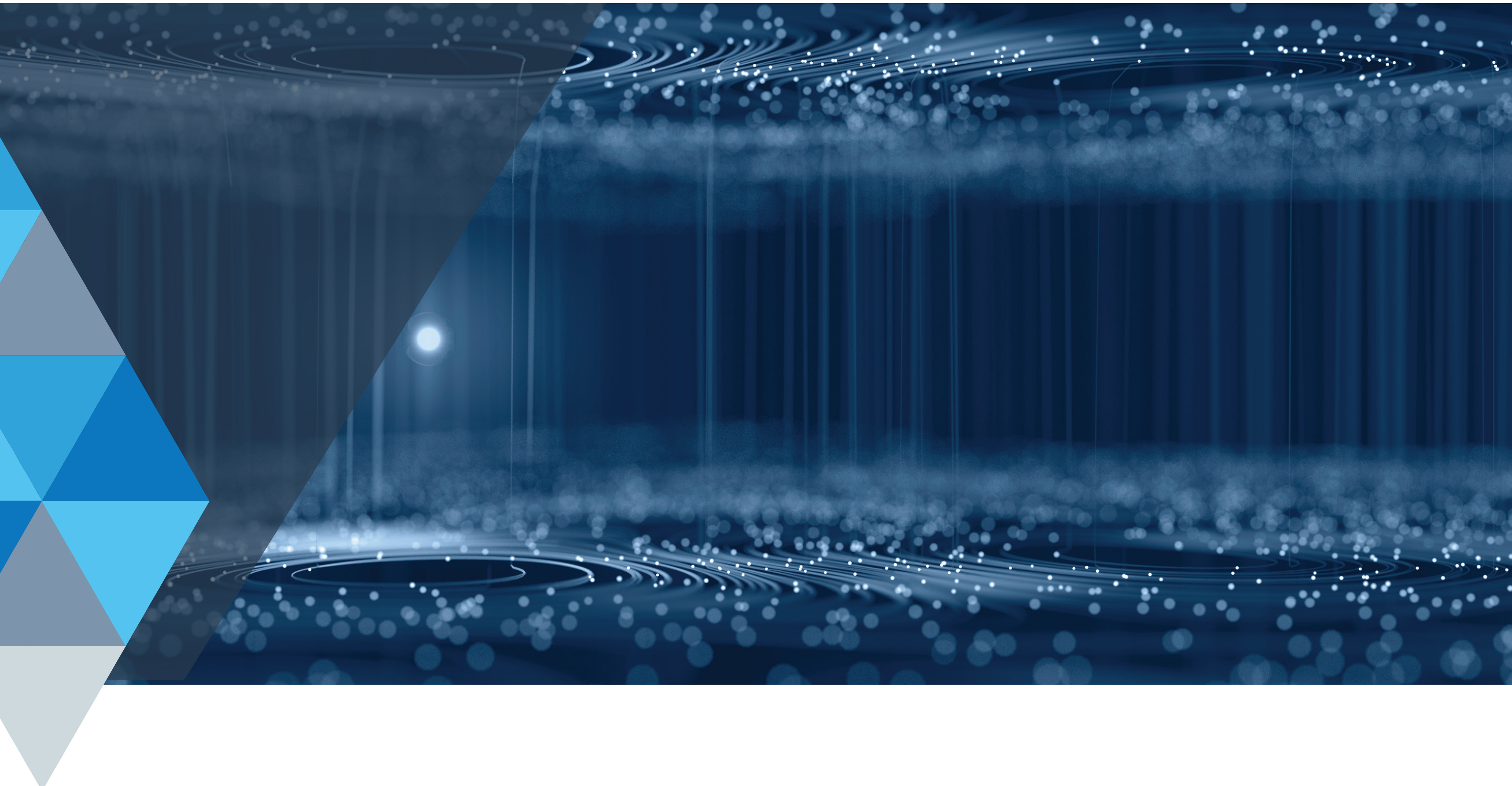
EBOOK

THE MSP GUIDE TO HIGHER GROWTH:
PRICING FOR PROFITABILITY



A successful managed services business relies on a solid business strategy and service delivery model, as well as finding the right technology for its needs.

Determining Service Offerings

MSPs around the globe offer a wide variety of services to their clients. Those operating primarily in a confined location, for example, a city, county, or region, generally offer services based on client needs and the level of competition. Some MSPs find they can do well by delivering only minimal managed service capabilities, such as remote monitoring and patching, while the bulk of their revenues come from time and materials contracts. Others, generally in larger cities and more competitive environments, find that clients are looking for MSPs to not only smooth their IT spending by offering consistent or fixed monthly rates but also to take on the risk of IT service delivery by offering service level guarantees.

Wherever you are, you are likely to find that clients look to trusted MSPs to offer more and more capabilities.

As the pace of technology innovation continues to expand, it becomes harder for IT personnel within SMB to keep up. Not because they are not capable, but simply because they do not have time or opportunity to learn about new capabilities to the level required for adoption. For example, many SMBs are not able to optimize their virtualized environments, preferring to err on the side of caution rather than efficiency. Similarly, many have little knowledge of cloud services beyond the SaaS offerings their peer group use.

MSPs have a great opportunity to bridge this knowledge and resource gap and to provide cost-effective solutions to SMBs while increasing their own efficiency levels and offering profitable and valuable services.

Managed Services Offered by MSPs

The managed service provider market is not uniform. Not all MSPs have the same needs, and each has unique characteristics. While a less mature MSP would be offering break-fix services, a more mature one would be offering strategic planning and support. Based on such unique needs, MSPs broadly fall into four distinct categories.

General Support Services

These include remote help desk support for technological issues and user support issues, as well as break-fix services where staff are deployed to client locations from a centralized pool of technicians to perform remedial actions.

General Managed Services

- ✔ Endpoint and network management
- ✔ Audit and discovery
- ✔ Compliance
- ✔ Remote monitoring
- ✔ Backup and disaster recovery
- ✔ Network security
- ✔ Patching and updates
- ✔ IT service level management
- ✔ Service-level agreements
- ✔ Cloud services (IaaS, PaaS, SaaS)
- ✔ Unified communications (a.k.a. VOIP)

Administration Services

These services include responsibilities that require planning and coordinating on a defined set of services to be provided to the client such as:

- ✔ Technology requirements management
- ✔ User administration (e.g., access management), device configuration and onboarding
- ✔ End-user training

Strategic Planning and Support

An MSP that offers strategic planning and support functions as a virtual CIO, providing services like strategy consulting, business management, budgeting, and management (board) level reporting.

Understanding Your Abilities

Each of these categories requires different sets of skills and investments. Typically, MSPs start out offering general support services such as break-fix capabilities that support equipment and software they have sold as resellers.

As the number of contracts grows and the number and skill set of the support staff increases, additional services can be added. Familiarity with each specific customer's business and an increasing level of client trust and satisfaction are vital. Eventually, the most trusted MSPs may be asked to play the role of virtual CIO, helping the business to achieve its goals by intelligently leveraging appropriate information technologies, i.e., becoming an IT services broker rather than a reseller.

The services you offer must match the technical capabilities of your organization, your ability to make data center investments, the capabilities of the IT management solutions that you use, and of course, the needs of your target customers.

While some service elements may have become commoditized (e.g., remote monitoring), remember that SMB clients will most likely prefer bundled services. Bundle commodity services with other elements, and differentiate your offerings based on the bundle composition.

Tips for Creating High-Value Service Bundles

Providing multiple services in bundles helps you streamline your entire business operation framework and optimizes your overall customer service. By implementing a range of services, you will be able to engage with customers frequently and build lasting relationships.

When choosing which new services or service bundle components to add to your current services, consider the following:

Do you need to add new service components to be competitive? How will you differentiate your version of the new services?

- Hint: Clients are interested in results. How can you better guarantee the results, even if the nature of the service is similar to competitive offerings?

How large will be the demand for your new service?

- When will the demand arrive? Currently, cybersecurity is the number one priority for businesses.[1] With the rise of the cost of data breaches, companies understand the importance of security and are looking for MSPs to provide the right cybersecurity solution. Services like backup and disaster recovery, multi-factor authentication, two-factor authentication, single sign-on, and password management can all be managed centrally on behalf of your clients.

  Regulatory compliance is another demand MSPs should take into account. The necessity for meeting compliance requirements has been rising for the past year. With compliance being a tricky and complex area, businesses are seeking compliance automation services from MSPs.

What will the adoption of the new service do for your business valuation?

- As an MSP, your business valuation is dependent on your monthly recurring revenue (MRR) stream and your profitability. Some services may add more to revenue but less to profitability. Some may be more easily differentiated and sustainable than others. Typically, those requiring a higher level of investment and commitment, such as hosting services, will add more to your valuation than reselling other vendor's services, even though these can be lucrative in the short term.

Strategize on how to replace clients' on-premise investments with cloud or hosted solutions that make it easier for you to add new and advanced service capabilities such as unified communications.

- This is important for two reasons: 1) the closer the service delivery point, the easier the service is to maintain (i.e., on your premises vs. your clients') and the more efficient you can be; and 2) hosted services are likely to prove far stickier — which is one reason they can improve your business valuation.

How many of your clients will buy or use the new offering?

- If only one or two, is it worth the investment in time to develop the service? Remember, it is easier to sell to current customers first but only if they have or will have a need. The cost of attracting new customers can be five or six times the cost of selling to existing ones.

  Your goal should be to steadily increase sales to existing customers while increasing the size of new contracts because of your growing services portfolio, while at the same time becoming ever more efficient and differentiated in your sales and marketing approach.

Price for Profitability Growth

According to a recent Forrester industry analysis, the average MSP margin fell to 17 percent.[2] What could be the cause of this significant drop-off? One of the reasons MSPs are seeing a decline in the margin is their inability to move to a flexible business model. The other reason is the need to provide niche expertise – to have an advantage over their competitors.

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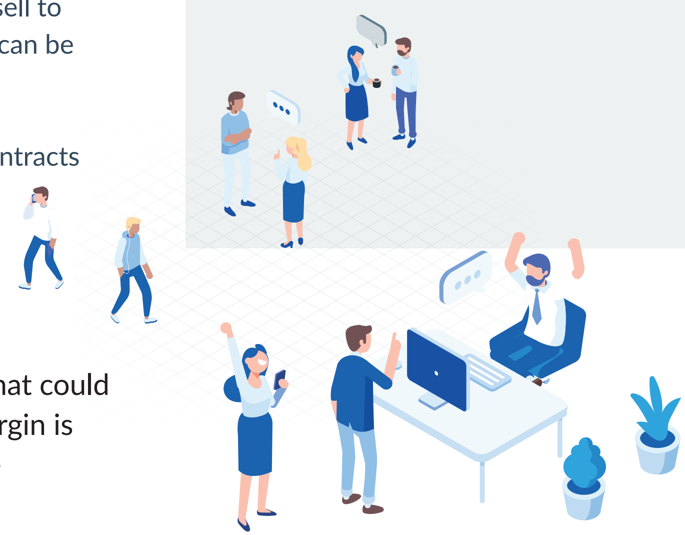


Most MSPs provide almost the same services, but what differentiates them is the level of service and the pricing model. Value-based pricing has been the most popular choice among our MSP Benchmark Survey Report respondents for at least four years. And when considering per-device and per-user pricing models, MSPs are split between the two. In the Kaseya 2019 MSP Benchmark Survey, about 27 percent of the respondents said more than 50 percent of their customer base is charged on a per-device model, and another 25 percent said more than 50 percent of their customer base is charged on a per-user model. Only 16 percent of the respondents had more than 50 percent of their customer base charged on a per-hour model.[3]

The pricing of managed services, like the pricing of any complex solution, is a topic to which we could devote an entire book. Our goal in this guide is to provide some general guidelines to increase your profitability and to identify key areas for consideration for it. As with most pricing decisions, there is no single correct answer or approach. Much depends on the nature of the services in question, your reputation within your target marketplace and customer set, and the level of competition you face.

Plan How You Will Manage Unexpected Workloads

An important success factor for growing a profitable managed services business is managing and controlling unplanned and unexpected workloads. What this means, in reality, is being confident that the resources allocated to manage the services contracted by each client will be adequate to meet their needs. Knowing what resources will be needed, together with the cost of those resources, means that you can price your services profitably.

Also, understanding how much technical and engineering staff time is needed leads to optimized utilization-enabling your staff to reliably service multiple customers per time period. Finally, by constantly working on staff productivity, you will be able to support new service offerings and generate more revenues, from both new and existing customers, without big increases in your workforce.

Eliminate Unplanned Work

Numerous steps can be taken to minimize unplanned work. They are:

- Take a proactive stance to end-user training particularly to security and new application deployments. Consider producing simple written guidelines to address common issues, such as password management, that can be easily accessed and readily understood. A large portion of help desk calls relate to lost or forgotten passwords.

- Standardized device configurations (including the actual devices) and software sets as they are much easier to manage, troubleshoot, and rebuild when issues do occur.

- Standardized policies and processes for software updates and downloads – restrict end-user administrative rights. By strictly controlling end-user actions and the applications that can run on their devices through policy management and governance, you can avoid a significant number of security and other issues.

- Test all major patches before deployment and roll them out under central management.

- Review trouble ticket logs regularly to identify any systematic issues that can be dealt with proactively.

- Secure system/device access with multi-factor authentication to make knowledge of passwords alone inadequate; secure sensitive information using encryption and containerization; implement a robust system for single sign-on and one-time-use-only passwords.

Automate as many tasks as possible to reduce the possibility of human errors. Be more efficient. Deploy policy-based automation with proactive remediation to increase productivity. Automate deployment of software, manage patches, and proactively resolve issues across your complete environment.

Why Use a Value-Based Pricing Strategy?

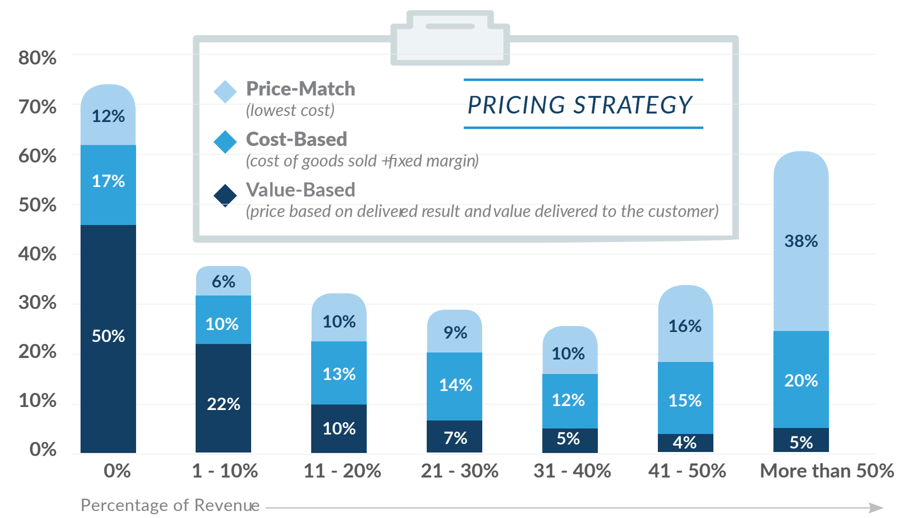
Knowing how to optimize your service delivery to maximize both staff productivity and client satisfaction is important to understanding and managing your service delivery costs. But there are a few more factors to be considered before you can successfully price your services. For example, who are your customers? What are their expectations of your services and pricing? What outcomes are they seeking to achieve?

An oft-quoted analogy is that no one wants to acquire drill bits. They buy drill bits to create holes! (In reality, the problem is more complex – the desired outcome is more likely related to assembling or building something. How much you are willing to spend on the drill bit might depend on the number of items being built or the material to be drilled).

In the case of managed services, potential clients may be seeking a variety of possible outcomes: access to expert resources, support for tasks that they do not have the skills to address, efficiency of operation, freeing up time to address more strategic issues such as helping with business innovation, organizational change, achieving agreed to service availability and performance levels, etc.

The value of these outcomes will likely differ depending on the prospect's business and also on the size of the company. Think back to the drill bits: Do consumers buy the same bits as construction companies? Do they pay the same prices? Before pricing any service, it is important to determine the needs of your target market. Smaller companies have lower revenues in general and constrained in their ability to fund expensive services. They look for low-priced offerings providing basic levels of support. Nevertheless, all businesses are interested in getting the best value for their investments (read largest ROI), and most will favor higher value, versus a lower price if the value price fits within their budgetary constraints.

Not surprisingly, the approach is quite popular among service providers. According to the 2019 Kaseya MSP Benchmark Survey Report, about 38 percent of participants said that more than 50 percent of their revenue comes from a value-based pricing strategy.



For value-based pricing model, the price is based on the value of the service provided to the customer, while cost-based pricing is based on the cost the MSP has incurred to provide the service.

Value-based pricing is more focused on customers, meaning they are determined by what customers perceive the value of the services offered, and cost-based pricing is mostly determined by efforts put in by an MSP for the service.

The biggest value of a managed service to a small company may be doing things they do not have the skills or resources to do themselves. In this case, your differentiation must focus on how effectively you will provide the service and why you are so much better than your rivals. Do your skill levels provide a more certain outcome? Will you be quicker or just more effective than your competition? Will you pass on knowledge or help train internal personnel?

Buying an ongoing service requires a level of trust; customers will pay more for providers they trust to provide good service. Pay attention to competitive price ranges, but do not be fooled into thinking that the lowest price always wins. It does not. Faster growing MSPs will tell you that the best value service usually wins.

In comparison, midsize companies will likely pay more for managed services. However, they also have more complex needs. As companies grow, their risks increase and they develop requirements that small service providers find harder to fulfil. They may need proof of regulatory compliance or training, liability insurance coverage for service provider — staff visiting their locations, guaranteed service levels and any number of other items.

If midsize companies are your target market, understand their needs, and do not be phased by low-priced bids from much smaller (low overhead) companies. In general, there is a significant correlation between the (employee) size of clients and the size of their service providers. Bigger companies find it easier to trust larger service providers because they see the increased maturity and professionalism that develop with growth and size. Understand the value of your service to your target audience and price accordingly.

Determining an Optimal Pricing Model

Choosing the right pricing model for your business is also important. While the tiered pricing model remains the most popular among MSPs, per-endpoint and per-user pricing are also available as options.

Tiered Services Model

For many MSPs, the best strategy is to offer two or three service bundles with the more comprehensive bundle priced the highest. The rationale is twofold.

Most businesses prefer to buy higher-value services versus cheaper ones, especially when it comes to managing critical IT infrastructure. A great deal of trust is required to outsource to a third party.

Low price can signify low quality, and that is not desired when buying managed IT services. Consequently, there will be a tendency to favor a better value service bundle. Secondly, MSPs position the more comprehensive service bundle as the least risky/most reliable.

If other providers or internal resources manage infrastructure elements, time, and efficiency may be lost. Looming issues may be missed. Inevitably, there will be some form of finger-pointing when issues do occur. But more importantly, it will be harder to automate tasks and troubleshoot issues, which will lead to more trouble tickets and lower levels of client satisfaction. In general, MSPs deliver better quality services when they manage more of the client's IT capabilities.

Per-Endpoint Pricing Model

As the name says, the client pays a flat fee for each billing cycle for each endpoint you support. Per- endpoint pricing is flexible for both parties and you can price the endpoint based on its type. Most MSPs that opt for this model do so because it becomes easy to scale as the company grows. Some clients tend to favor this model, as it enables them to plan the total budget earlier without having to worry about a surprise at the end of the billing cycle.

Per-User Pricing Model

The per-user pricing model takes the same approach as the per-endpoint model, except that the flat fee is charged per user. This makes it easier to figure out the contract pricing unless your client has fluctuations in the number of users. To adopt this model, you would have to come up with a total cost for all services provided per user. Once this is set, it becomes easy to know your numbers and reach your profit accordingly.

Contract Size and Complexity

These guidelines are general in nature. Despite the need to standardize service elements to minimize unplanned work and maximize professional staff productivity, each client environment will employ a different mix of technologies, including a different number of devices, and represent a different level of complexity. Each client will insist that its needs are unique. Take advantage of this in your pricing strategy.

Provide each customer with a value-based, customized price (monthly or annual service contract) for the service tier they want, based on the unique value you will deliver. The price should be derived from standard bundled tier pricing and your average cost per user or endpoint but modified to meet each prospect's particular needs. Also, consider how you might offer a fixed-price contract for the duration of the contract term. This is often very much appreciated by clients that do not have to find additional, often unbudgeted, funds when changes occur, such as needing to add devices or users during the contract period. If you do accommodate changes without increasing your fees, you will likely benefit from a considerable amount of goodwill at contract renewal time. Our most successful MSP customers suggest -being flexible yet consistent with pricing.

A word of caution: Understand how your services compare to the competition and do not overprice. If your service capabilities are average compared to other MSPs, then price near the median. If you offer significant value-add, you will be able to price successfully at higher pricing levels.

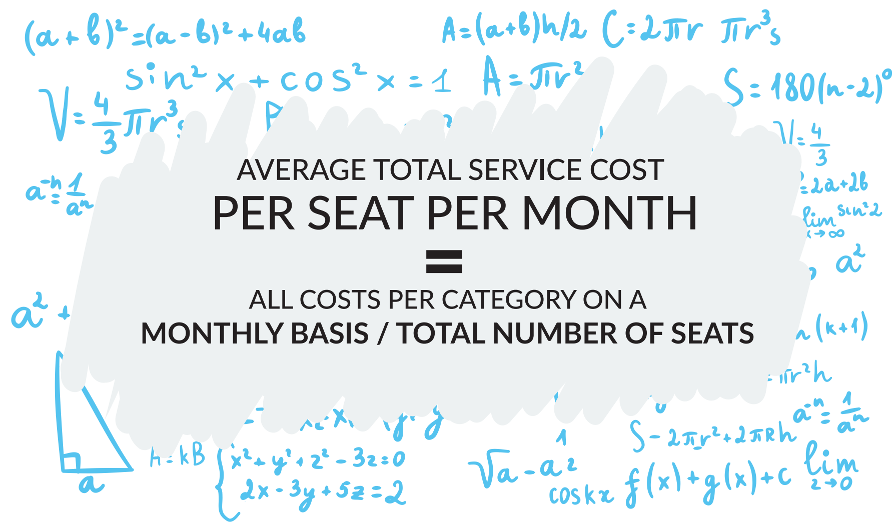
Using a value-based pricing strategy will ensure that you are maximizing profits, but you must know the cost of your service delivery efforts first.

Calculating Existing Service Delivery Costs and Gross Margins

The cost of service delivery is the sum of the (monthly) cost of your billable employees plus the monthly (amortized) cost of your infrastructure and other expenses. These two costs then can be added and divided to determine an average cost per user or per endpoint per month. For ease of description, we will refer to this as "cost per seat, per month" and leave it to you to decide if that means per user or per endpoint.

It is important to have a full understanding of your service delivery costs- so you can pick a pricing approach that maximizes your profit. It is useful to first allocate your services to categories, as described previously, as each category requires different skill levels, tools and other expenses:

1. **GENERAL SUPPORT**
2. **CENTRALIZED MONITORING, MANAGEMENT AND REMEDIATION**
3. **ADMINISTRATIVE**
4. **STRATEGY AND PLANNING**



While you may price based on your per-endpoint costs today, consider developing a per-user approach for the future. Increasingly, employees have multiple endpoints that need to be managed. But the costs of supporting additional endpoints are marginal versus the cost of supporting additional users.

Next, calculate your current average monthly revenue per seat by category. In an ideal world, this would be your current price, but if you have multiple service elements within a category or you allow discounting, the average revenue may differ from your standard price.

Your gross profit margin is the difference between the revenue and cost, divided by the revenue.

(Revenue - Cost) / Revenue = Gross profit margin

It is also helpful to know what your overall average cost and revenue per employee is and how additional services will affect those averages.

AVERAGE COST PER EMPLOYEE

=

TOTAL COST OF RUNNING YOUR BUSINESS (PAYROLL AND EXPENSES) / NUMBER OF EMPLOYEES INCLUDING YOURSELF)

YOUR AVERAGE REVENUE PER EMPLOYEE

=

TOTAL REVENUE FROM SERVICES AND SERVICE-RELATED ACTIVITIES / TOTAL NUMBER OF EMPLOYEES

That is all employees, not just your technical team. Include all sales, marketing, finance, admin and management staff, and others.

New services should add to your average revenue per employee as quickly as possible without adding significantly to your average cost per employee. That way you know you will be increasing your gross margins. If you are investing in new skills to expand your services, how quickly will the average new services revenue per employee add to the overall average?

Any plan to add new employees that only increase service revenues from new customers or only a portion of existing customers needs to be carefully considered. Ideally, new services will quickly be taken up by both established and new customers and will raise the overall average revenue per employee.

Conclusion

Developing an efficient pricing strategy to maximize profits might take some trial and error. MSPs should deliver the kind of service that sets them apart from their competitors. They should focus on the value they bring to the client to grow their business.

Need to decide which services to offer? Learn from our **whitepaper 2019 MSP Benchmark Survey.**

Need to make few pricing decisions? **Download our eBook PSA and RMM: Buyer's Guide to Integrated, Powerful MSP Solutions.**

REQUEST A DEMO OR START A FREE 14-DAY TRIAL TODAY!

Sources

1. 2019 Kaseya State of IT Operations for Small and Midsize Businesses
2. What I See Coming For The Channel In 2019, Forrester Analysis
3. 2019 MSP Benchmark Survey Results Report, Kaseya

About Kaseya

Kaseya® is the leading provider of complete IT infrastructure management solutions for managed service providers (MSPs) and internal IT organizations. Through its open platform and customer-centric approach, Kaseya delivers best in breed technologies that allow organizations to efficiently manage, secure, automate and backup IT. Kaseya IT Complete is the most comprehensive, integrated IT management platform comprised of industry leading solutions from Kaseya, Unitrends, Rapidfire Tools, Spanning Cloud Apps, IT Glue and ID Agent. The platform empowers businesses to: command all of IT centrally; easily manage remote and distributed environments; simplify backup and disaster recovery; safeguard against cybersecurity attacks; effectively manage compliance and network assets; streamline IT documentation; and automate across IT management functions. Headquartered in Dublin, Ireland, Kaseya is privately held with a presence in over 20 countries. To learn more, visit www.kaseya.com.

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