

# How red hat linux was violently taken over by microsoft corporation

[Business](#), [Company](#)



## **Marketing Plan**

### **Microsoft Corporation Hostile Take Over of Red Hat Linux**

Microsoft, the leading manufacturer of personal computer software with its windows based operating systems and application software, has decided to expand its influence beyond windows into the Linux freeware operating system world. The means for entry into this rapidly growing segment of the server operating system market is through a takeover of the Red Hat Linux Company. Currently Microsoft Corporation now owns 51% of the stock for Red Hat Linux. This expansion directly into the Linux arena will provide Microsoft with the ability to attack competitors in the network server market with the Windows NT and Windows 2000 operating systems on one flank and with the extremely stable Linux operating system on the other flank.

Microsoft expects to use this one-two punch to significantly gain market share in the server market and to shape the future of business LANs, WANs and the internet. Additionally, Microsoft expects to gain a controlling market share of the Linux office application suite with a Linux version of its Microsoft Office application suite.

Red Hat Linux is one of the recognized pioneers and leading distributor of the freeware operating system called Linux. Although Red Hat Linux does not have wide name recognition outside of the computer industry, the name is synonymous with Linux among computer professionals. Red Hat Linux is the preferred operating system for the network server program Apache, an extremely stable server program that currently runs on 49% of the internet servers. The current Red Hat Marketing strategy has been to stress three

basic points to consumers. First, Linux is the most stable operating system available. Second, Linux is easy to use and has user friendly graphic user interfaces that facilitate the functionality of the operating system. Third, Red Hat is the 'David' competing against the 'Goliath' Microsoft. This approach has huge appeal for the 'free thinkers' of the computer world.

Microsoft's strategy for maintaining market dominance in the computer software industry clearly rests in its ability to develop or control the operating software for the majority of the computer market. This strategy has propelled Microsoft to the dominant position in the personal computer operating system market and, with the acquisition of Red Hat Linux, now has the opportunity to decisively control the network server market. Ultimately, Microsoft will use both the Windows and the Linux operating systems to force its major competitors, such as Sun Microsystems and Hewlett Packard to either consolidate or exit from the server operating system market. A key element of the two pronged attack on competitors is Microsoft's decision to provide a Linux version of Microsoft Office applications for distribution to Red Hat Linux customers. In addition to creating additional revenue for Microsoft, this move will ensure application compatibility between businesses using the Windows operating system and the Linux operating system.

Red Hat Linux, who already controls a significant share of the Linux distribution and services market, is in the position to leverage the Microsoft distribution system, financial resources and suites of application software to gain market share and achieve market dominance in the Linux distribution and services segments.

The takeover of Red Hat Linux by Microsoft Corporation has necessitated that a marketing plan be created to capitalize on this opportunity. This marketing plan will outline the current Situation Analysis, Financial and Marketing Objectives, marketing strategy, action programs to execute the programs and a projected profit and loss statement.

## **Current Marketing Situation**

### **Industry Structure**

The system-level software industry comprises operating systems, operating systems enhancements, and data center management software. Its worldwide market increased 15% in 1998, to \$41 billion. This figure should exceed \$68 billion by 2002, implying a 13.5% compound annual growth rate. The competitive intensity of the computer operating system industry is extremely high. Although there are considerable incentives for competitors to enter the market, the industry is characterized by significant expenses for up-front development, marketing, and technical support infrastructure for initial versions of software products. Subsequent products based on the first version become much less expensive to develop. The software products within this industry often enjoy gross margins of 70 to 80 percent. The capital support costs to support a software company are relatively small, with labor for software development comprising the largest expense item. Development often involves working in multiple teams of 6, 12, or even 100 persons with long lead times between different versions of software. The most significant entry barrier, however, is the entrenchment of currently used operating systems. Selection of previous versions of a specific

computer operating system by a computer user has a tremendous influence on the buyer. The operating systems for computers are not compatible and operate application programs exclusive of each other. The choice of operating system determines the type of supplemental application programs that are chosen and installed. The expenditure of individual capital for operating system specific application programs creates a monetary incentive for the customer to remain loyal to the selected operating system. This 'financial loyalty' plus software compatibility issues and high entry costs combine to create a very large entry barrier to companies attempting to penetrate the market with alternative operating systems. A unique aspect to the computer operating system industry is the lack of influence by suppliers. The product produced is software, intellectual property, written and published by an individual or company. Supplier influence is limited to the producers of the media that the software is published on and the availability of trained personnel to physically write the computer code. Currently there is no shortage of either, although exceptionally high quality computer programmers are sought after by software companies. The cost of a premium programmer, however, is miniscule in comparison to the profit margin on mass produced magnetic media. Buyer influence in the market is likewise tempered. Once the investment for an operating system and applications has been expended, there has to be a huge difference in perceived value for the buyer to switch to another operating system. In the software industry a typical buyer response is simply choosing not to upgrade to a new product. This response, however, is constrained by the requirement to remain compatible with the rest of the computing/business world. This

pressure is becoming more critical as technology and e-commerce evolves. Eventually the buyer is forced to upgrade or fall behind competitively. This is not to say that software companies can fix prices with impunity, the challenge to the software vendor is develop the pricing for their product that does not cause the buyer to delay upgrading and is not so exorbitant that the perceived value of a competitor's software becomes attractive. Industry wide, software is distributed through streamlined distribution networks to software wholesalers and retailers. Microsoft has refined their distribution into a new integrated distribution model combining the best of both indirect and direct sales. The resulting hybrid model allies the supply channel and vendors into a supply channel paradigm that leads straight to the customer.

### **Product/Product Line and Market position**

Microsoft is the industry giant, completely dominating the personal computer operating system market and office productivity software suite applications segment. Microsoft Windows 98 and Windows 95 are installed on 79.6% of the world's personal computers; Microsoft Office suite is used by 79% of the market. Prior to the acquisition of Red Hat Linux, Microsoft held a slim advantage in the network operating system's market with 37% of the servers running Windows NT. The addition of Red Hat Linux to the Microsoft stable of operating systems brought an additional 17% of the network operating systems that currently use Linux into the fold. Currently the Microsoft family of server operating systems controls 54% of the server market.

### **Major Customers and Market Segments Served**

Microsoft has an extremely wide customer base, as one would expect with the market dominance that they enjoy. Major customers for the operating systems market include Compaq, Dell, Gateway, IBM, Hewlett Packard, Micron Enterprises, and CompUSA. Within the network operating system segment Microsoft has aggressively sought out the full market spectrum of small, medium and large companies, advertising the scalability of their Windows NT software. To complement the scalability of the operating system Microsoft utilizes a Value-Added Provider (VAP) program to provide the customer with a total package of network management, network security, legacy system integration, web design and integration, and project management and e-mail servers. This strategy seems to have paid off, especially among network servers in manufacturing plants. Among operating systems in plants Microsoft NT is currently operating on 50% of the platforms . Additionally, Microsoft has made significant inroads into the governmental and educational server sectors by stressing cost effectiveness of the windows based systems, legacy program integration and application software compatibility. Historically Microsoft had a difficult time penetrating the internet web server software segment, controlling 22% of the market share among the internet servers . The acquisition of Red Hat changed the playing field. Red Hat is the leading Linux provider of open source software and services, controlling 60% of the Linux distribution . Most significant, however, is that Linux gave a Microsoft operating system the ability to run Apache Server, the dominate internet server software. Currently Apache Server is operating on 49% of the internet servers. In addition to operating

Apache Server, the growth potential for Linux is huge. Growing by 212% in 1998, Linux now controls nearly 20% of the commercial server market. . This growth is expected to continue at a 25% annual rate until the year 2003 .

### **Other Products/Product Lines**

Microsoft offers a wide variety of computer software products to support the personal computing market. These products can be categorized as operating systems, business software, development tools and programming languages, internet development and browsers, entertainment, home productivity, reference software and peripheral hardware. Microsoft recently reorganized their company along product support lines. To support their products Microsoft is divided into the following main groups, this includes the recent addition of the Linux Development and Support division:

- Business and Enterprise
- Streaming Media
- Consumer Windows
- Business Productivity
- Developer
- Consumer and Commerce
- Linux Development and Support

The Business and Enterprise group focuses on the information technology needs of large organizations and development of the Windows 2000 product line. The Streaming Media Division develops and markets Windows® Media Technologies.

The Consumer Windows Division strives to improve the Windows platform for the end user. Products influenced by this division include Windows 98. The Business Productivity Group focuses on meeting the needs of the “knowledge worker,” defined as the worker who constantly needs access to data to accomplish his or her job. These products include Microsoft Office, Project, Publisher, FrontPage®, BackOffice®, Small Business Server, Exchange, and Windows CE. The Developer Group focuses on products and services for the developer customer. These products include SQL Server, COM+, Visual Basic®, Visual C++®, Visual Studio®, and MSDN™. The Consumer and Commerce group focuses on making it easier for businesses and customers to work together online. Products covered by this group include various MSN™ offerings, WebTV, and Commerce Server. The Worldwide Sales and Support group concentrate on developing and directing the enterprise, education and organization of customer units. The Retail Products Group, focuses on products such as games, input devices and Microsoft’s reference products. The latest addition to the Microsoft organization is the Linux Development and Support division. Microsoft is positioning Red Hat Linux as the premiere provider of the total Linux solution. To support this position Red Hat has developed a complete family of Linux tools, server applications, commercial augmentations programs, Linux technical support packages, office applications and suites, programming and development tools, networking solutions, and an on site consulting program. Additionally, Red Hat is aggressively moving into the e-commerce arena with the acquisition of Hell’s Kitchen, Inc., a leading provider of e-commerce credit card point of sale verification programs. In the months prior to the

acquisition by Microsoft Red Hat acquired Cygnus Solutions, a privately held developer of cross platform programming tools.

## **Opportunity and Issue Analysis**

### **Internal:**

### **Strengths (A) Weaknesses (B)**

- History of innovative software developments.
- History of providing the consumer with an extremely effective and stable operating system.
- Financially Microsoft is the strongest company in the industry with annual net profits of \$8. 7 billion.
- Continually shapes and recognizes new trends within the technology and consumer markets.
- Revamped distribution system increases efficiency and reduces costs.
- The tremendous growth that the company has experienced in the last 10 years has created a huge corporation that is becoming unwieldy.
- A large number of separate software and hardware product lines hamper customer support
- Institutional arrogance (we know what is best for the consumer) has begun to blur the company's vision.

## **Opportunity (C) Threat (D)**

- **Use the company's position as the primary force in technology to undercut the alternative server operating systems.**
- **Use the VAP to present total solutions to small or medium businesses.**
- **Create complete, easy to implement and maintain server solutions.**
- **Provide free training for a company's IT personnel if they implement a complete Microsoft Server Solution.**
- **Use the size, deep pockets and collective expertise of the company to gain market share in the web server market.**
- **The institutional growth and size of the company will continue to decrease customer responsiveness and become inefficient.**
- **Internal institutional friction will become more pervasive as each of the company's subdivisions either evolve or are eliminated. This will be especially true for the rivalry between the Windows 95, Windows 98, Windows NT and Windows 2000 divisions. Four operating systems being fielded under one corporation is way too many.**

**External:**

## **Strengths (E) Weakness (F)**

- **Credited with being a fundamental force in the PC revolution.**

- Brand Awareness and Loyalty
- Once a customer has adopted a Microsoft based operating system, considerable barriers are present to prevent the customer to switch to a competitor.
- Provides the consumer with a ' total software solution' ranging from the operating system to office suites and other applications.
- Recently lost an anti-trust lawsuit concerning Microsoft's business practices in marketing Internet Explorer.
- Perceived institutional arrogance by consumers.
- Customer support has been declining. Microsoft now charges for customer support packages that previously were free of cost.
- The fierce competitiveness of Microsoft is perceived as draconian business tactics.

### **Opportunity (G) Threat (H)**

- Use the financial resources of the company to invest in the key players in the internet infrastructure. Not only will this provide Microsoft with immediate insight into the needs of the industry, but it will allow Microsoft to help shape the future and ensure their position in the future.
- Use the company's resources to create complete, user friendly web server solutions.
- Use the resources of the company to collect customer-sampling data. Use this data to improve customer relations and develop future products.
- A break up of the company as a result of the anti-trust lawsuit.

- Sun Microsystems has now reduced their price for the Solaris operating system to \$75 and is offering StarOffice, a Unix based office application suite, for free.
- A bare bones Linux operating system is offered of free over the internet. If a consumer requires a little more technological help, a complete CD-ROM version is available from Red Hat, Inc. for \$50.

## **Opportunities Cross-Matrix**

### **Leverage (match A+G) Problem (B attacked by H)**

Allow the development of web solutions that embrace the ‘total package’ concept; ease of use, training, implementation and cross platform computability. Institutional arrogance by a monopolistic organization leads to a drop in perceived customer value or relative perceived value (the perceived value of one product versus the perceived costs of another).

Constraints (unable to capitalize on G because of F) Vulnerability (Threat H to A)

Any movement by Microsoft to use its position to improve its server operating system market share will be viewed as anti-trust movements by government regulators. The computer industry has always been filled with free thinkers and independent people. The appeal of a ‘under-dog’ free operating system competing with the market behemoth has an irresistible quality for them.

SWOT Summary: While Microsoft has attained market dominance in the computer software industry, the ground swelling insurgence of operating

systems outside of the Windows family necessitates immediate action if market share and profitability are to be maintained.

Competitors and Their Strengths and Weaknesses.

Microsoft has developed a reputation for being a fierce competitor in the market, using every possible aspect of their market dominance to ensure profitability and market share. Their competitors in the OS segment are Apple Computer, Silicon Graphics, Hewlett Packard (Unix), Sun Microsystems (Unix) and the competitors to Red Hat Linux.

## **Competitor Strengths Weaknesses**

### **Apple Computer**

- Strong Market share among educational institutions
- Perceived as the best platform for graphics, digital photo manipulation and video work
- Computer interface sets the standard for ease of use
- Lack of market share
- Closed box architecture limits the number of non-apple vendors who can develop applications and peripherals for the platform
- Company is slow to react to competitor attacks and innovations.

### **Silicon Graphics**

- Phenomenal ability to process, edit and produce 3D production quality graphics and video.
- Produces top quality high-end desktop, servers and supercomputers.
- Provides a complete suite of application programs.

- Uses IRIX, a Silicon Graphics produced variation of UNIX, as its operating system.
- Workstations and servers are expensive, often 2-3 times the cost of a Dell or Compaq.
- Specificity of the IRIX operating system has precluded outside vendors from producing a wide variety of supporting applications.

## **Sun Microsystems**

- Long established history in the networked environment
- Developer of JAVA, a cross platform programming language that is being used for everything from web sites to toasters.
- Producer of premium UltraSparc based workstations and servers.
- Recently developed and released a UNIX/LINUX office application suite of programs.
- Uses Solaris, a sun produced variation of UNIX, as its operating system. This operating system historically had been designed to operate only on sun computer platforms.
- Sun computers are expensive, often 2-3 times the price of a Dell or a Compaq.(\$1, 995 for a 360Mhz basic configuration).
- Specificity of the Solaris operating system has precluded outside vendors from producing a wide variety of supporting applications.

## **Linux competitors to Red Hat Linux**

- Currently competitors control 40% of the Linux support market .

- Linux is growing in popularity, 29% of IT professionals who use Windows NT as their server software are considering switching to Linux.
- Linux is a fast growing operating system. In 1998 alone it increased shipments by 15.8%.
- Financially, Linux support companies are barely breaking even.
- All source code for the Linux operating system is 'open', available to whom ever desires to use it.
- Currently there are a limited number of high quality business applications for Linux.

## **Objectives**

### **Sales Objectives**

In the next three years the Microsoft/Red Hat Linux entity is planning to gain 10% of the Linux distribution market, achieving a 70% market share of the total Linux market by December 31, 2003. This translates into \$74.14 million in sales by the end of the target date. In conjunction with the Linux revenue, Microsoft expects to generate sales of one million units of the new Linux version of Microsoft Office the first year, followed by an annual increase of 250,000 units per year. This is expected to generate \$425 million in sales for the new version the first year.

### **Profit Objectives**

Initially Microsoft/Red Hat Linux is expecting to break even. Profit targets for the Linux distribution for next two years to the target return on investment (ROI) of 20%. In addition to the targeted profits for the Linux subdivision,

Microsoft is expecting to generate \$103.8 million in profits on \$425 million in sales of the Linux version of the Microsoft Office application suite. The targeted profits will require close, coordinated marketing efforts on the part of both Microsoft and the Red Hat Linux subdivision. While this marketing effort will be extensive and expensive, these costs have already been factored into the profit estimates.

## **Customer Objectives**

Microsoft/Red Hat Linux is targeting information technology professionals, independent thinking home users, and the computer purchasing personnel of small, medium and large companies. The Microsoft goal is to provide the customer with a complete computer technology solution from the operating system to the office application suites required for productivity, regardless of the size of the company or the operating system required. While this is certainly an ambitious goal, Microsoft is clearly in the position to deliver.

## **V. Marketing Strategy**

### **Product Strategy**

Microsoft/Red Hat Linux will simultaneously offer two products to consumers, a Red Hat Linux distribution of Linux complete with a complete set of device drivers and patches for computer peripherals and a Linux version of Microsoft Office. Buyers of the Red Hat Linux distribution will receive a trial version of Microsoft Office and a coupon to upgrade to the full version at a 15% discount off of the retail price to other customers. Microsoft will also offer the Office suite of programs to other Linux users, but only at the premium pricing scheme through retail outlets. To provide customer support,

Microsoft will establish a Linux website that will provide free patches, drivers and updates along with a customer FAQ database and online technical support.

### **Pricing Strategy**

Initial pricing of both the Linux operating system and the Microsoft Office suite will be critical. Competitors in the Linux segment of the software market are expected to aggressively cut their prices in an effort for maintain their market share. The promotional pricing for both the operating system and the Office suite will be maintained until the initial target sales goal for the year has been met and the competitors have been forced to begin to raise pricing. The pricing strategy will then shift to competitive pricing designed to price the operating software and the application suite at a level comparable with the competition's. Once the targeted market share has been reached the pricing strategy will shift to a premium pricing strategy, with the application suite priced slightly higher than the competition. The subsequent market share standings for both the Linux operating system and the Microsoft Office application suite should be monitored closely. If the market share begins to fall, Microsoft should respond with promotional pricing to maintain their share.

### **Distribution Strategy**

The new products will be distributed to consumers using Microsoft's existing new integrated distribution model combining the best of both indirect and direct sales. The resulting hybrid model allies the supply channel and vendors into a supply channel paradigm that leads straight to the customer.

From the consumer's perspective they can either purchase the products from a computer retail vender or they can purchase the software from an e-commerce site and receive the software via conventional delivery mechanisms, such as FedEx, or via electronic transfer means.

### **Promotional Strategy Action Programs**

There will be a two pronged promotional strategy. The first prong will be aimed at the home computer user through the promotional pricing and advertising of the Red Hat Linux distribution. The second prong will be aimed at the IT professionals and will stress the stability, functionality and the compatibility of Red Hat Linux and Microsoft Office. Additionally, each product will be mutually cross-supportive. When a customer purchases a copy of Red Hat Linux, he will receive a trial version of Microsoft Office and when a customer purchases Microsoft Office for Linux she will receive a coupon and a trial version of Red Hat Linux. This cross pollination effectively will enforce a pull promotional strategy. Market research will be conducted at the one month, six months and one year points to determine market penetration and to confirm the customer satisfaction levels of the two products. The objective at each of these points would be to steadily increase both measurements until they reach the targeted levels.

All actions relating to the promotion of the Microsoft and the Red Hat Linux products will be coordinated and executed by the Microsoft marketing division. Initially, prior to the release of the products, the means of promotion will be through interviews and product previews in the trade magazines and by publishing trial testing and results in the industry

consumer magazines, such as PC World. As the release date nears, a total of \$102 million dollars (30% of expected 1st year profits) will be spent over the duration covering the month immediately prior to the release date of Microsoft Office for Linux through the second month following the release. During this timeframe, 65% of the marketing budget will be spent on the mainstream media such as television (television, radio, and print ads), 25% will be earmarked to support promotional activities and the final 20% will be to fund tradeshow and Microsoft for Professionals seminars. Following the first two months, the marketing budget will be targeted at 10% of the gross sales amount for each of the two programs. The delivery media for this advertising will closely follow the initial promotional strategy, but can be tailored to fit any unique situations.

## **Profit and Loss Statement**

Microsoft is willing to initially accept an initial breakeven operation on the part of Red Hat Linux, using this operation as the spring board for the release of it's Microsoft Office for Linux applications suite. Initially, the Red Hat Linux will be priced at \$29 per copy and the Microsoft Office for Linux will be priced at \$450 per copy for the full suite. The Windows version of this product normally sells for \$650. In the first year the sales, Microsoft Office for Linux is expected to generate over \$450 million in sales and \$340 million in profits. In the following years, Red Hat Linux and Microsoft Office for Linux are expected to increase profits by 25% per year as the company garners more market share. Immeasurable in the profit figures is the influence that Microsoft will be able to influence on the future of the networked computer.

With a combined market share of 54% of the network server market and over 80% of the personal computer operating system market, Microsoft can continually position itself in a profitable position for years in the future.

## **Controls**

There will be two phases of market research designed to measure the marketing campaign effectiveness. The first phase will be conducted by in-house assets on a weekly basis, beginning one month prior to the release of the Red Hat Linux/Microsoft Office for Linux combined campaign and extending through the sixth month following the release. These efforts will include random interviews, telephone interviews and online surveys. To complement these in-house efforts a private firm will be commissioned to perform Market research at the one month, six months and one year points to determine market penetration and to confirm the customer satisfaction levels of the two products. The results of the survey data will then be compared to the actual and projected sales data to confirm the effectiveness of the marketing strategy. The objective at each of these measurement points would be to steadily increase both measurements until they reach the targeted levels stated in the marketing strategy.

## **Conclusion**

The takeover of Red Hat Linux by Microsoft Corporation has created a very unique opportunity to substantially increase the influence of Microsoft in both the network server market and in the personal computer operating system market. The challenge to both companies is to effectively merge their products and efforts into a synergistic campaign that will achieve

targeted profits and gain in market share. Through the successful application of this marketing plan these goals and estimates can be achieved.