

# Microsoft antitrust paper 1659



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Viewed together, three main facts indicate that Microsoft enjoys monopoly power. First, Microsoft's share of the market for Intel-compatible Personal Computer (PC) operating systems is extremely large and stable. Second, Microsoft's dominant market share is protected by a high barrier to entry. Third, and largely as a result of that barrier, Microsoft's customers lack a commercially viable alternative to Windows, the operating system of all PC's.

Microsoft enjoys so much power in the market for Intel-compatible PC operating systems that if it wished to exercise this power solely in terms of price, it could charge a price for Windows substantially above that which could be charged in a competitive market. Moreover, it could do so for a significant period of time without losing an unacceptable amount of business to competitors. In other words, Microsoft enjoys monopoly power in the relevant market.

Microsoft possesses a dominant, persistent, and increasing share of the world-wide market for Intel-compatible PC operating systems. Every year for the last decade, Microsoft's share of the market for Intel-compatible PC operating systems has stood above ninety percent. For the last couple of years the figure has been at least ninety-five percent, and analysts project that the share will climb even higher over the next few years. Even if Apple's Mac OS were included in the relevant market, Microsoft's share would still stand well above eighty percent.

Microsoft's dominant market share is protected by the same barrier that helps define the market for Intel-compatible PC operating systems. As explained above, the applications barrier would prevent an aspiring entrant

into the relevant market from drawing a significant number of customers away from a dominant

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incumbent even if the incumbent priced its products substantially above competitive levels for a significant period of time. Because Microsoft's market share is so dominant, the barrier has a similar effect within the market: It prevents Intel-compatible PC operating systems other than Windows from attracting significant consumer demand, and it would continue to do so even if Microsoft held its prices substantially above the competitive level.

Microsoft's actual pricing behavior is consistent with the proposition that the firm enjoys monopoly power in the market for Intel-compatible PC operating systems. The company's decision not to consider the prices of other vendors' Intel-compatible PC operating systems when setting the price of Windows 98, for example, is probative of monopoly power. One would expect a firm in a competitive market to pay much closer attention to the prices charged by other firms in the market. Another indication of monopoly power is the fact that Microsoft raised the price that it charged Original Equipment Manufacturer's (OEM's) for Windows 95, with trivial exceptions, to the same level as the price it charged for Windows 98 just prior to releasing the newer product. In a competitive market, one would expect the price of an older operating system to stay the same or decrease upon the release of a newer, more attractive version. Microsoft, however, was only concerned with inducing OEMs to ship Windows 98 in favor of the older version. It is unlikely

that Microsoft would have imposed this price increase if it were genuinely concerned that OEMs might shift their business to another vendor of operating systems or hasten the development of viable alternatives to Windows.

Finally, it is indicative of monopoly power that Microsoft felt that it had substantial discretion in setting the price of its Windows 98 upgrade product (the operating system product it

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sells to existing users of Windows 95). A Microsoft study from November 1997 reveals that the company could have charged \$49 for an upgrade to Windows 98 -- there is no reason to believe that the \$49 price would have been unprofitable -- but the study identifies \$89 as the revenue-maximizing price. Microsoft thus opted for the higher price.

Microsoft's first response to the threat posed by Netscape Navigator was an effort to persuade Netscape to structure its business such that the company would not distribute platform-level browsing software for Windows.

Netscape's assent would have ensured that, for the foreseeable future, Microsoft would produce the only platform-level browsing software distributed to run on Windows, Internet Explorer. This would have eliminated the prospect that non-Microsoft browsing software could weaken the applications barrier to entry. Executives at Microsoft received confirmation in early May 1995 that Netscape was developing a version of Navigator to run on Windows 95, which was due to be released in a couple of months.

Microsoft's senior executives understood that if they could prevent this

version of Navigator from presenting alternatives, the technologies branded as Navigator would cease to present an alternative platform to developers. Even if non-Windows versions of Navigator exposed Internet-related Application Programming Interfaces (APIs), applications written to those APIs would not run on the platform Microsoft executives expected to enjoy the largest installed base, i. e., Windows 95. So, as long as the version of Navigator written for Windows 95 relied on Microsoft's Internet-related APIs instead of exposing its own, developing for Navigator would not mean developing cross-platform. Developers of network-centric applications thus would not be drawn to Navigator's APIs in

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substantial numbers. Therefore, with the encouragement and support of Gates, a group of Microsoft executives commenced a campaign in the summer of 1995 to convince Netscape to halt its development of platform-level browsing technologies for Windows 95.

Most harmful of all is the message that Microsoft's actions have conveyed to every enterprise with the potential to innovate in the computer industry. Through its conduct toward Netscape, IBM, Compaq, Intel, and others, Microsoft has demonstrated that it will use its prodigious market power and immense profits to harm any firm that insists on pursuing initiatives that could intensify competition against one of Microsoft's core products. Microsoft's past success in hurting such companies and stifling innovation deters investment in technologies and businesses that exhibit the potential to threaten Microsoft. The ultimate result is that some innovations that would

truly benefit consumers never occur for the sole reason that they do not coincide with Microsoft's self-interest.

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