

Unbundling Microsoft Windows

by Alex Singleton

Neelie Kroes, the European Commissioner for Competition, has suggested that in a competitive market there should be “a significant drop in market share” for Microsoft Windows, highlighting her frustration that the operating system market does not seem to foster competitive spirits. “Recent years have certainly seen innovation in high technology markets,” Ms Kroes says, “but largely in areas that Microsoft does not control.”

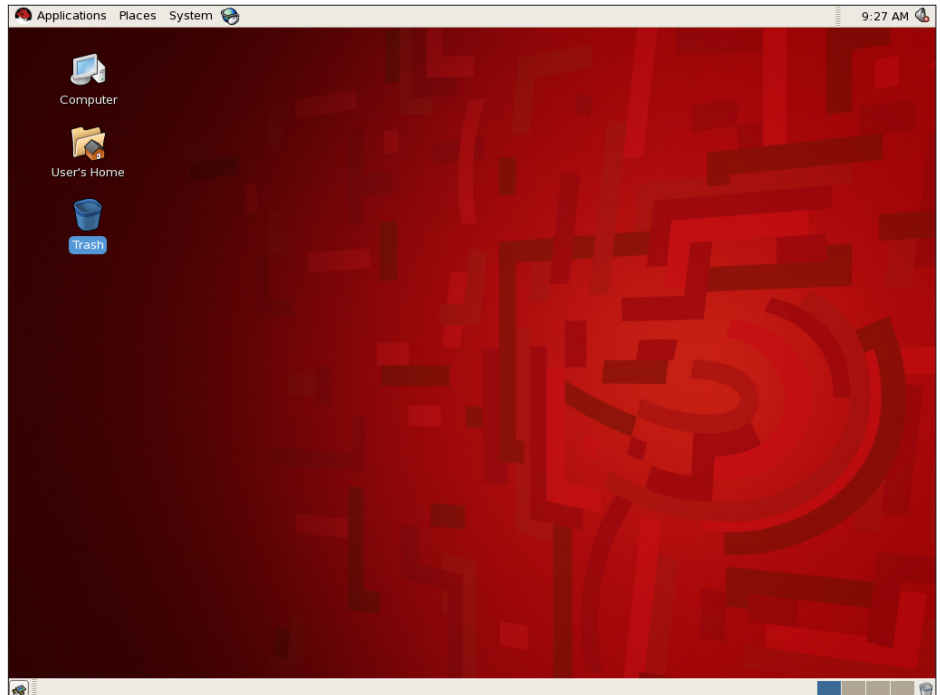
Thus far, the Commission has concentrated its antitrust action on Microsoft’s server products and on the bundling of Windows Media Player with Windows. The Commission’s success on 17 September 2007 in the European Court of First Instance, which upheld its antitrust action against Microsoft, will embolden the Commission’s resolve on competition matters.

Examining a more central issue – the lack of choice in desktop operating systems – is now needed if the Commission is to encourage a marketplace in which Ms Kroes’ vision of thriving competition is enacted. This briefing argues for the Commission’s thinking on Microsoft’s operating system monopoly to go to its logical conclusion and support the “unbundling” of Windows from desktop computers.

What limits competition on the desktop?

The vast majority of computers sold are commodity products. While manufacturers compete on styling and brand reputation, in addition to specification, no manufacturer or component manufacturer is the sole choice for consumers. Intel processors compete with those from AMD; memory comes from numerous suppliers; hard drives come from a range of suppliers like Seagate, Hitachi and Western Digital; and so on.

There is no reason why there should not be diversity in operating systems, too. Hardware competition does not stop broad compatibility: hardware manufacturers follow standards, which evolve over time, like SerialATA and USB to ensure that products work with all computers. When new components work in a way computers do not expect, manufacturers provide drivers to ensure their hardware works will all systems. There is significant innovation in hardware



Windows’ competitors, like Red Hat Linux (pictured), are cheaper but locked out by bundling

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– gamers will testify to ferocious leapfrogging in the graphics card market. It is competition that is the principal driver of innovation.

But on the software side, the general customer, who walks into a PC World or PC City, is not able to purchase a commodity PC without automatically paying for Windows. The result is that consumers who, given the choice, would opt

for a cheaper operating system, find themselves automatically buying the market leader.

There is no meaningful competition between operating systems for commodity computers. Microsoft’s dominant position is not in the public interest. It limits the market and has slowed technical development to the prejudice of consumers.

Yet operating systems are not a natural monopoly. Just as evolving standards in hardware allow the combination of competition and compatibility, in a competitive operating system market, there would be broad compatibility between different competitors’ operating systems.

Or, to put it another way, if there are ten major operating system vendors, independent software houses are going to write their software using coding tools and “programming libraries” that will enable their software to work on all the systems, rather than just one. Competition would encourage open standards and interoperability as vendors would, for competitive reasons, want their products to interact with other vendors’ products.

To be clear, this paper deliberately concerns itself with the commodity computer market, where products are aimed at the mass market. We consider the Mac to be a premium, niche product, like a Bang and Olufsen television, which is difficult to justify in the business world outside of the publishing sector. We therefore do not think that the Mac, despite claims of its superiority, provides a meaningful competitive threat to Microsoft.

Costs on EU business

The Windows monopoly imposes an extra cost on virtually every EU business, as the price of operating systems would drop in a more competitive market. Moreover, there are other costs: some argue that support costs are higher for Windows than other operating systems, particularly when one considers security vulnerabilities that have plagued Windows systems. Encouraging competition would help EU businesses, lowering their costs.

Ways of unbundling

We examined several ways to give consumers a choice in the operating system market. One was to insist that computer manufacturers always offer customers a choice of bundled operating system. This would work well for online purchases, such as online orders with firms like Dell, where consumers would be able to choose the option from a list. However, it would cause logistical problems on the high street. We thought it impractical to insist that shops stock multiple versions of each computer, in case customers want a particular operating system.

We also considered insisting that customers are given the option of keeping Windows when they first switch on their new computer. Customers would then receive a rebate by cheque or bank transfer. However, this might end up being bureaucratic, and there might be a question of how the size of the rebate is calculated.

Unbundling Windows

Instead, we decided that the best way to approach competition was simply to insist that operating systems are purchased separately from desktop and laptop computers.

This, we believe, would have a significant effect on the market share of Windows, providing the competitive marketplace that Ms Kroes has called for. Price conscious consumers, including many students, would opt for cheaper operating systems.

We do not believe this would add complexity for consumers. Consumers would simply be



asked to insert an operating system DVD when they first turn on a new computer, which would then automatically configure itself.

Manufacturers would be able to bundle special hardware drivers with their computers (which might be needed to gain the very best performance), and manufacturers would still be able to recommend particular operating systems. It is likely that PC manufacturers would compete by listing multiple operating systems that their systems had been “certified” to run properly, rather than simply listing Windows compatibility.

A possible objection

Microsoft might argue that the measure would increase piracy, but it is worth noting that Windows already has “software activation”, which prevents users installing the product on

multiple computers. Companies like Adobe and Symantec are very successful without needing bundling to prevent piracy. The threat to Microsoft is not that price-sensitive consumers would pirate, but that they would switch to lower-cost or free alternatives.

Policy recommendation

This paper’s recommendation is that the European Commission should require all desktop and laptop computers sold within the EU to be sold without operating systems.

For two decades, Microsoft has enjoyed monopolistic power in the operating system market. The Competition Commissioner has signalled the desire to see more competition in this sector. Unbundling would foster a competitive market, increase consumer choice and reduce prices.