On Microsoft, Standard Oil and Trustbusters

Business World

By Holman W. Jenkins Jr.

While much legalized shouting lies ahead, the Justice Department's assault on the Windows "monopoly" has already come a cropper.

Over the weekend, the antitrust division failed to persuade Microsoft to honor its distinction between the market for browsers and the market for operating systems. But then even the famous antitrust skeptic who recently resurfaced on the Netscape payroll, Judge Robert Bork, couldn't bring himself to prejudge the "tying" issue.

Instead he tried to make himself useful by offering the *Lorain* precedent to suggest that Microsoft may harm consumers by preventing competitors from reaching them. *Lorain* involved a dominant newspaper that refused to sell space to local businesses that advertised on a start-up radio station in the area.

Hiring Judge Bork was perhaps a testament to Netscape's desperation, since at his press conference he admitted he was hoping his wife would teach him about the web. He also seemed to have the weird idea that Windows was designed to prevent people from loading Netscape.

The *sine qua non* of an operating system is to serve as a universal platform for software. Anybody can download the Netscape browser using Microsoft's own browser, and install it without difficulty. Even with its recent reverses, Netscape still commands 60% of the browser market to Microsoft's 40%.

The *Lorain* argument collapses for a pretty simple reason. Despite Microsoft's undoubted control over what appears on the computer screen the first time you boot up, in our world TV, radio, newspapers, direct mail and the advertising blimp still exist. America Online did not need guaranteed placement on the desktop to achieve most of its 12 million members. There are plenty of ways of reaching consumers.

To be sure, when novice computer users boot up, they will most likely go first to the browser and internet service provider and whatever other software and services Microsoft puts in their face. For many this may be all they ever need, a fact that looms large in Justice's inverted telescope.

In reality, the value proposition in computing is rapidly migrating from the desktop to the Web. Five years ago, the desktop constituted most of known cyberspace. Now Microsoft and its works are shrinking to just a small corner of that rapidly expanding universe.

Here is where Microsoft really resembles Standard Oil. John Rockefeller took a disorganized, inefficient and shambolic oil industry, and applied the techniques to make oil products cheap, abundant and of uniform quality. In doing so he laid the foundation for autos, plastics, pharmaceuticals, and cosmetics, all built on petroleum as a feedstock.

But once he had picked the low-hanging fruit by uniting and modernizing the refining industry, competition began to emerge to drive the industry toward new efficiencies. By the time the Supreme Court broke up the company, Standard Oil's market share had already dropped to 70% from 90%.

It was these efficiencies, not those he introduced during his "monopolist" phase, that finally made him a billionaire.

Bill Gates has seen his billions mount up faster even as Microsoft goes into relative eclipse in the vast computing universe. In less than 15 years, 200 million personal computers have proliferated throughout the world economy, giving rise to hundreds of new companies and whole industries. Without a standard PC operating system—and without somebody to invest billions in upgrading that operating system in such a way as to protect the world's sunk investment in existing software and stored data—it wouldn't have happened. Microsoft takes a razzing over "bloatware" and using the public to debug early releases, but it has been an awesome achievement.

As with Standard Oil, the critics have a hard time disentangling cause and effect of Microsoft's monopoly. Listen skeptically in the weeks ahead as Justice catalogs all the evil practices by which Microsoft maintains its business. Rockefeller was demonized for getting special rates from railroads, and for accepting "drawbacks" when they shipped oil for his competitors.

John D. Rockefeller

But the rail barons of the day, Jay Gould and Commodore Vanderbilt, were not fools. Any company shipping as much oil as Standard became, in effect, an investor in the railroad. Gould and Vanderbilt were not about to make huge outlays for locomotives and track on the mere hope of business from a single customer. They agreed to rebates and drawbacks to give Rockefeller an incentive to plan his own shipments efficiently so the rail lines could make the best use of their assets.

Justice first attacked Microsoft over its practice of charging computer makers a license fee for every machine shipped, rather than just those actually shipped with Windows. But the only competitor for Windows was a copy of Windows loaded illegally. In protecting itself Microsoft was protecting its honest customers from free-riders.

Now the focus has shifted to control over what appears on the screen when a user boots up. By taking this power away from Microsoft and giving it to computer makers, Justice would take away Microsoft's intellectual property, stripping the company of any incentive to keep investing in Windows. That's the idea: The world would supposedly look to the Netscape-Java clique for future advances.

Nothing qualifies the Justice Department to dictate such a sweeping and speculative industrial policy. But Joel Klein, the antitrust chief, fits well into the Clinton administration: tentative and reserved at first, his grandiosity overflows if it meets no resistance.

Somehow we just keep being drawn to comparisons between the Clinton and Nixon administrations.

In Nixon's day, the antitrusters were aflame over "conglomerization." His division chief Richard McLaren sharpened his lance and picked out a target, ITT, not noticing that the world was already changing. The market was dying, conglomerization was falling out of favor. His attack threatened to do more harm than good.

Nixon had a better grasp of the public interest than his antitrust chief did. "There is not going to be any more antitrust actions as long as I am in this chair," he was taped saying. "I do not want McLaren to run around prosecuting people, raising hell about conglomerates, stirring things up at this point." ITT's Harold Geneen was suitably grateful, contributing $400,000 in soft money to the Republicans.

Mr. Clinton shares the Nixonian nose for a fundraising opportunity but lacks the Nixonian sense of responsibility to curb the bumptious crusades of his underlings. But at least Bill Gates is learning. He's begun paying soft money.

A Case Built on Wild Speculation, Dubious Theories

By George L. Priest

Yesterday's suit by the Justice Department against Microsoft (joined, in a needless piling on, by 20 state attorneys general) threatens to damage or even cripple a company that has brought billions of dollars of value to consumers around the world. Microsoft is a classic example of what even the Supreme Court regards as a good monopoly: a firm that has gained monopoly power not through merger or collusion, but business skill and acumen in creating a clearly superior product.

To be sure, Microsoft's leasing practices are not entirely beyond reproach. Provisions prohibiting licensees from advertising competing software—heavily criticized by my friend Robert H. Bork—cannot easily be defended. But these provisions are probably harmless in practice and can equally harmlessly be stopped. Mr. Bork relies entirely on the 1951 *Lorain Journal* case, in which the Ohio town's single newspaper was found guilty of monopolization for refusing to deal with firms that advertised on a competing radio station. That case supports the prohibition of Microsoft's advertising restrictions. But the case has little to say about the broader Justice Department claims against Microsoft.

Most troubling is the Justice Department's effort to define for Microsoft which services Windows 98 ought to include—for example, compelling it to offer Netscape's Navigator as an alternative browser to Microsoft's own Internet Explorer or to constrain Microsoft from incorporating a WebTV site or an e-mail program. Here the Justice Department's lawsuit is based on theories of monopolization that have been discredited for decades and on wild speculation about the course of future software innovation.

The most popularly accepted theory is that Microsoft insists on incorporating its own browser program, as opposed to Netscape's, as a mechanism for extending or leveraging its 80% market power over general operating systems to additional services. If Microsoft incorporates such services, the theory runs, it forecloses opportunities for sales by smaller software manufacturers that would otherwise be its competitors.

But consider the example of General Motors, which in the 1960s was the dominant player in the domestic auto market, with a market share of 50%. Could GM increase its monopoly profits by including a car radio as standard equipment? Including the radio surely foreclosed sales by independent radio installers, but the gain to General Motors above the price it was earlier charging for the car could be no more than the additional value of the radio.

Does it make a difference that Microsoft, unlike GM, is itself the producer of Internet Explorer, so that the profits it gains are its own? Again, only insofar as Internet Explorer is of value to consumers. Put differently, if Netscape Navigator is a better browser than Microsoft Internet Explorer, requiring its inclusion in Windows 98 will *reduce* Microsoft's competitive advantage over rival operating systems. The Justice Department, thus, has the case exactly backwards. If Internet Explorer is superior to Navigator, the effect of a successful prosecution will be to harm consumers. If Navigator is superior, the prosecution will overrule Microsoft's mistaken decision and shore up its market power, which would otherwise decline.

The Justice Department is concerned about other programming services that Microsoft includes or might include in future versions of Windows. But does anyone believe that bureaucrats or judges can know how to define the optimally integrated product in the fast-changing computer software market?

Concern about the foreclosure of potential competitors cannot provide an answer. Should the only hotel in a small town be accused of foreclosure if it offers free soap or toiletries—foreclosing competing grocery and drug store sales? A free ironing board—foreclosing laundry services? Its own minibar—foreclosing liquor and snack sales? Microsoft's definition of what Windows will include is no different.

The second ground of the Justice Department's attack is no more convincing. It rests upon pure speculation about the future of software innovation. The thought is that Microsoft's foreclosure of smaller programming competitors removes from the market entrepreneurs who, though small today given their niche markets, may at some future time generate ideas that are sufficiently innovative to challenge Windows in its entirety. This romantic hope is totally speculative. Is the next Bill Gates more likely to invent an alternative to Windows if Microsoft is forced to carry his current niche program or if Microsoft's success forces him to develop something different? The latter alternative is at least equally plausible.

The Microsoft lawsuit is reminiscent of the Justice Department's persecution of an earlier monopolist, the United Shoe Machinery Corp. As late as the 1950s, United Shoe possessed 75% to 85% of the domestic shoe-machinery market, at a time when shoemaking was dominated by American firms. In that case, too, the Justice Department attacked a set of leasing practices that it did not well understand. And with no greater understanding, the courts struck those practices down, leading United Shoe to decline and ultimately to drop out of the market. The results: The price of shoe machinery went up, and foreign firms began to enter the market. Foreign companies now dominate the market both for shoe machinery and shoemaking itself. There was no clear benefit to consumers whatsoever. Those are the stakes in the attack against Microsoft.

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Microslop

The Justice Department's antitrust chief Joel Klein threw the hail mary yesterday. It will be a long time before this ball comes down, and by then the stands will be empty and the fans will have gone home.

Quite apart from intellectual confusion, this is the problem of antitrust in the information age: It moves too slowly. One federal judge has already pronounced the department to be living in a "time warp." That was just a week ago, when the D.C. Circuit Appeals court tossed out a moldering injunction that might have blocked the release of Windows 98. Justice was upset because it still hasn't finished litigating over whether an older version, Windows 95, was being used illegally to advance the fortunes of a separate product, Microsoft's browser.

But that was then, and this is now. In Windows 98, the two products have been seamlessly integrated, and Mr. Klein has been forced to loft the ball in a completely different direction. Now he argues that Microsoft is using its browser to illegally defend its Windows monopoly.

At least we're getting to the heart of Justice's hidden industrial policy. Its larger agenda is to promote Netscape as an alternative "platform" to the Microsoft operating system.

The hail-mary nature of the play is revealed by the crowbar Justice sought yesterday. It will ask the court to force Microsoft to distribute Netscape Navigator with every copy of Windows. This is where the ball sails over the head of the collected wisdom of the antitrust community. Never mind that anybody can already easily download Navigator for free from the Web. There is little precedent for any company being made to promote and distribute a competitor's product.

More to the point, by the time any court decides, the issue will long since have become moot. In the next few days Windows 98 with the built-in browser goes out to the world. What the lawyers are arguing about will have become irrelevant to everyone else.

If we were Bill Gates, we would set up an annuity to pay the lawyers and forget the whole thing. Go back to the business of running a software company. The IBM antitrust case lasted 13 years before being dismissed by the courts as hopelessly brainless. Thirteen years is roughly the period between the Apple II and Windows 95—the stone and bronze ages of the PC.

The AT&T case, technically a "win," percolated for 10 years until the Bell decision to surrender its government-created monopoly. In 10 years Marc Andreessen went from being a seventh grader to becoming a multimillionaire in Netscape's public offering.

Even the Standard Oil lawsuit dragged on for a decade in those less lawyer-clogged days. In short, we don't see much history being made here. It's already too late. Regulators never got their hands around the computer industry, and now the technology is moving so fast they never will.