

Hey! You! Get Off My Cloud: Incumbent vs. Challengers in the Software Services Market

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Incumbent firms are frequently toppled by low-price alternatives in emerging markets. Incumbent software firms also have to deal with the ubiquitous threat of product piracy and constantly invest in and monitor their piracy control strategies. Using the office productivity market as the context, this study examines the impact of challenges from open source (OpenOffice) and cloud computing (Google Docs) *free* alternatives on the willingness-to-pay (WTP) and demand for Microsoft Office. We empirically demonstrate that the incumbent proprietary software producer can maintain the demand derived from its preexisting network effect in the face of competitive pressures from free alternatives and software piracy by: 1) *reducing prices*, 2) *maintaining strong piracy controls*, and 3) *extending the existing product line into the market of the emerging platform*. Surprisingly, we observe that appearance of challengers can lower consumer surplus even when the alternatives are offered for free.

Keywords: Incumbents, challengers, radical innovation, software piracy, cloud computing, open source software, willingness-to-pay.