Frosting

# The Case for Shipping O'Hare with Frosting

Alec Saunders, Feb. 10 1995

The O'Hare team in PSD has been working on a series of internet extensions for Windows 95 that will ship about the same time Windows 95 does. O'Hare will consist of the standard Internet clients (FTP, WWW and Gopher) extended and integrated with Windows 95 features, MAPI drivers for Internet mail and news (from another project code-named Route 66), plus extensions to Windows 95 to allow URL's to be treated in the same fashion as other files in the Windows 95 filespace, and a Wizard to help the customer configure TCP/IP and, potentially, connect to an internet service provider such as the Microsoft Network.

O'Hare could be packaged in a number of different ways. Proposals currently being examined include:

1. Bundle O'Hare with a book from MS Press about the Internet
2. Deliver O'Hare as part of the Microsoft Network
3. Give O'Hare away, (free of charge) via bulletin boards and FTP.
4. Add O'Hare to the Windows 95 add-on product called *Frosting*.

There are a number of considerations we should use to evaluate these alternatives.

**Impact to MSN.** The Microsoft Network is building a worldwide TCP/IP network which O'Hare will take advantage of. We must consider which packaging alternative impacts positively or negatively on future MSN business.

**Competitive Products.** IBM, Lotus, and Novell have all declared their intention to deliver products similar to O'Hare in the near future, and in fact IBM is already delivering their product. Moreover, 38% of OS/2 Warp customers are using OS/2 Warp to connect to the Internet. Clearly Microsoft must respond, and it is in Microsoft's interest to proliferate our internet components widely as a foundation for future commerce products, and as sockets for the future BSD *Catapult* product.

**Revenue Impact.** Although many internet components are available at no charge to the customer today, recent research by PSD demonstrated that we nearly double frosting unit volume and revenues, by including O'hare in the box. This incremental revenue should be traded off against any long term neagitve revenue impact to MSN.

**Risk to Schedule.** Schedule of MSN is not a sure thing, so putting MSN on the frosting critical path introduces un-needed risk. Failing to deliver, or delaying the delivery of an open internet client puts the Microsoft Systems business at risk.

## *Packaging Alternatives*

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### Bundle O'Hare with a book from MS Press about the Internet

In this scenario, O'Hare would be delivered as a disk of Internet utilities from Microsoft, bound into a book to be published by the Microsoft press.

Benefits:

- Detailed manuals would mean that there would less PSS costs associated with delivering Internet support.

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- Different channel, a potentially different customer, and potentially broader distribution

Downside:

- Low distribution. Books rarely achieve the same level of distribution as software. If one of our goals is to widely proliferate our internet clients, binding them into a book is not a reasonable way to accomplish this goal.
- Low profitability. A book is a more expensive distribution vehicle than traditional software, and typically sells for less.

Risks:

- Essentially none.

### *Deliver O'Hare as part of the Microsoft Network*

In this scenario, customers of the Microsoft Network who wish to use the internet would download the O'Hare client from MSN, and use MSN as the vehicle to connect themselves to the internet. The client would configure itself on the customers computer, effectively giving the customer 1 button access to the internet.

Benefits:

- No media costs and reduced PSS costs due to easy/on-line setup.
- Revenue stream from customer use of MSN. Making it easiest for customers to get internet access through MSN helps to enlarge the customer base for MSN, which has the potential to create substantial revenues over time.

Downside:

- No Operating System response to OS/2 Novell/Lotus internet products/features.
    - IBM has chosen easy internet access as one of the top OS/2 Warp features to emphasize heavily in television, radio and print advertising. Every IBM Warp ad has their tagline - *"Introducing OS/2 Warp. The new 32-bit, multitasking, multimedia, Internet accessed, Windows-friendly, easy-to-install, totally cool way to run your computer"*. Today 38% of Warp users are using it for that purpose.
    - Lotus and Novell have each declared their intention to enter this market with clients of their own - Lotus's based on Notes, and Novell's tied to Netware 4.
- Proprietary solution. Microsoft loses the customer who has already chosen an ISP, or who does not wish to use MSN. Ultimately this makes it harder to propagate catapult sockets, the Microsoft e-commerce solution, and other technologies we may be developing where it is advantageous for us to have market share on the client side.
- No client-side revenues. PSD market research shows that a Frosting/O'Hare bundle will nearly doubly Frosting revenues.
- Route 66 components get orphaned. Since MSN provides e-mail and net news services, the route 66 components are orphaned. They only make sense in an environment where the customer doesn't have an e-mail connection to the Internet.

Risks:

- MSN schedule. At this point MSN intends to deliver MSN over IP by the end of CY95. It isn't clear whether this is a realistic or optimistic schedule. Linking O'Hare to the MSN schedule is a competitive risk for the systems business at Microsoft.

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Distribute the O'Hare components freely via bulletin boards and FTP.

In this scenario, Microsoft copies other companies who are vying for share in the internet client market, and delivers the O'Hare components free for the download from existing download sites on the nets.

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Benefits:

- 0 incremental COGS, although an argument could be made that we should deliver this on a fulfillment disk also.

Downside:

- Accessible only to customers who are already on the internet. This means no incremental growth of the internet.
- No incremental revenues.

Risks:

- None

**Add O'Hare to the Windows 95 add-on product called *Frosting*, which is currently under development.**

In this scenario, customers would purchase the Frosting pack at retail. In the Frosting pack are all of the O'Hare components described above, with one-button sign-up via MSN and other ISP's (if MSN's schedule prevents them from delivering this service at the time Frosting ships).

Benefits:

- Revenue. A study conducted in January 1995 by PSD shows that we can nearly double frosting sales by including O'Hare in the Frosting pack. Attach rate to Windows 95 increased from 16% to 30% when we included a "one-button sign-up to the internet and browser tools like the World Wide Web". This increases Frosting year 1 sales from an estimated $81MM to $151MM, with marginal incremental COGS, and incremental profits of $61MM.

| | Frosting | Frosting + Ohare | Incremental |
|---|---|---|---|
| Estimated Unit Sales | 2,121,764 | 3,978,308 | 1,856,544 |
| Revenues | $ 80,627,035.90 | $ 151,175,692.31 | 70,548,656 |
| COGS | $ 9,017,497.44 | $ 18,220,649.23 | 9,203,152 |
| **Profits** | $ 71,609,538.46 | $ 132,955,043.08 | 61,345,505 |

- Open solution. We can deliver a credible internet client for any ISP customer, expanding the number of Microsoft clients on the internet to include customers using another service provider. This means capturing new business for MSN.
- Competitive response. O'Hare delivered in a high volume package like Frosting is the most effective way to respond to Novell, Lotus and IBM's offerings while balancing incremental revenue and risk.
- Marketing opportunities for MSN. Delivering a Microsoft client to customers on the internet who have another ISP is a marketing opportunity for MSN, both in the frosting box, and in content on an O'Hare home page. Capturing desktop clients now is an opportunity for Microsoft to market MSN to those customers regardless of MSN's delivery date. The study PSD conducted in January shows:
    - 49% of customers with Frosting capable PC's are already using an on-line service (AOL 46%, Compuserve 49%, Prodigy 23%, and others). Many are subscribed to multiple services.
    - Customers already using one on-line service are also most likely to purchase Frosting with O'Hare (34% said they would definitely purchase Frosting with O'Hare, vs. 26% among those who weren't already using an online service).

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- Build sockets for Microsoft e-commerce and Catapult projects. Capturing desktops now builds us sockets to install e-commerce solutions in the future, whether the customer is on MSN or any other provider. In the corporation, it gives us an opportunity to dislodge Novell when the Catapult product ships early next year.
- A home for Route 66. Route 66 is yet another attack point for us to be able to propagate our internet solution onto the corporate desktop. Frosting is a good vehicle to deliver this technology.

Downside:

- Potentially lower MSN sales. This is balanced by the opportunity that MSN will have to market to customers from competing services.
- Potentially confusing to customers. Microsoft's internet strategy needs to be rationalized in the frosting box. We need to deliver one client for MSN and all other ISP's, which includes the Word Internet Assistant (positioned as a great tool for creating HTML content).

Risks:

- O'Hare schedule vs. Frosting schedule. Some concern has been raised that merging these two projects creates risk that we will not be able to deliver the product on time. Conversations wi program management on O'Hare indicate that we could ship the O'Hare components now if we had to.

## *Recommendation:*

(1) Scoop incremental revenue from the frosting product. Use O'Hare to generate an estimated 61MM in incrementa profits for PSD in the first 12 months of shipping. Evaluate moving to other distribution vehicles after Frosting's initial delivery.
(2) Reduce schedule risk to systems business. Modify the O'Hare sign-up Wizard to prominently promote MSN as the one button sign-up ISP of choice, however, allow sign-up via other ISPs. .
(3) Aggressively work to grow the MSN internet customer base. Develop marketing programs in conjunction with MSN to make MSN attractive to customers who are using other ISP's. Some suggestions:
    - A cool O'Hare home page with WWW links into MSN content
    - Develop an Internet Mystery promotion which includes content on MSN
    - Use WinNews to communicate that MSN is the easiest and most cost effective way for the customer to access the internet
(4) Eliminate customer confusion. Ship Frosting with O'Hare and put the Word Internet Assistant on the CD ROM version of Frosting. All of the tools you need to get to the internet are in one package.
(5) Deliver an open solution. Document the one-button sign-up protocol and let anyone create a back-end for it.

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| Frosting Optimal Machines | | 13,261,026 | | |
| Current Frosting | | | | |
| | Projected Attach Rate | 16% | | |
| | COGS (3.5") | $ 5.25 | | |
| | COGS (CD) | $ 3.25 | | |
| Frosting + Ohare | | | | |
| | Projected Attach Rate | 30% | | |
| | COGS (3.5") | $ 5.91 | | |
| | COGS (CD) | $ 3.25 | | |
| | | | | |
| | | Frosting | Frosting + Ohare | Incremental |
| | Estimated Unit Sales | 2,121,764 | 3,978,308 | 1,856,544 |
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