Monday, August 8, 2005

Code war heats up between Microsoft and Adobe

By DAN RICHMAN
SEATTLE POST-INTELLIGENCER REPORTER

What happens when a smaller software maker enters a collision course with giant Microsoft Corp.? Adobe Systems Inc., a San Jose-based company with a large presence in Fremont, is poised to find out.

Redmond-based Microsoft just announced two products that will compete with offerings from Adobe, and Adobe is about to buy a company with products that challenge Microsoft's.

After that purchase, Adobe will practically own a rich market: software used by photographers, artists and Web developers to manage photos and graphic images and print them or create Web sites incorporating them.

Microsoft is active in just about every market except that one. And, as always, it's seeking ways to tweak its slowing revenue growth.

Microsoft says it's no threat. Some analysts don't believe that.

"For Microsoft to continue to grow at the rate it wants, it needs to be conquering new markets, and Adobe's is the biggest, juiciest prize right now," said Jesse James Garrett, a director at consultancy Adaptive Path.

The potential for a competitive clash began this spring.

In late April, Microsoft demonstrated software code-named Metro and now renamed the XML Paper Specification. It's digital-document software that in some respects competes with Adobe's market-dominating PDF format and its Acrobat family of products that produce or read that format.
Both companies' offerings allow creating documents that retain the quality of the included photographs, graphics and type and allow opening and reading the document dependably in multiple operating systems.

XML Paper Specification is planned as part Microsoft's Windows Vista operating system, released in beta form Wednesday.

Also part of Vista is the Windows Presentation Foundation, which incorporates Microsoft's XAML language for making documents and data automatically readable by multiple programs running on different operating systems.

That software could pose a competitive challenge to Flash, a well-established product from Macromedia Inc. Adobe in mid-April announced plans to spend $3.4 billion in stock to buy San Francisco-based Macromedia, in a deal set to close by this fall.

Vista plus XAML don't add up to Flash, exactly, but "they could obviate the need for Flash," said Gary Hein, an analyst with the Burton Group.

Macromedia also produces Dreamweaver, among the most popular products for building Web sites -- except for Microsoft's FrontPage and more sophisticated Visual Studio.

The fourth and final swerve toward a collision occurred last month, when Microsoft released Acrylic, the code name for a new, free graphics program.

The Acrylic Web site even echoes Adobe's distinctive packaging.

Early users say Acrylic includes some features of three Adobe programs designed for creative professionals: bit-mapped photo manager Photoshop and vector-based graphics managers Illustrator and Freehand.

Summing up these product developments, Hein observed: "It's almost like if you go down the list of products and abbreviations the companies are using, there's nearly a one-to-one mapping of what Adobe and Microsoft are providing."

At the moment, Adobe has a huge competitive advantage, holding between 75 percent and 90 percent of the market with each program it
But that kind of lead alone doesn't ensure continued success, said Piper Jaffray analyst Gene Munster. What will determine when, or whether, Microsoft's software can equal Adobe's, he said, is simply this: "How hard does it want to go after the creative community?"

In the business-software segment, Microsoft is also poised to make inroads.

Whereas Adobe sells printer-makers the right to print documents using its Postscript type technology, Microsoft plans to give its equivalent technology away, Munster said. That gives it a better chance of edging into Adobe's market.

But two Microsoft executives maintain Adobe has nothing to fear from Redmond.

Conceiving of the two companies as being on a collision course is "a much more black-and-white way of looking at the world than exists in the space we're in," said John Montgomery, a director in Microsoft's developer division.

"Yes, there's competition -- and there's collaboration. Our relationship with Adobe has many layers. We all need to work together, because what we're all trying to do is advance the state of the art and make money by building better products."

And, he said, Acrylic isn't meant to compete with Adobe products.

"It's less a competitive product than a cooperative product," he said. "You'd probably use them (Acrylic and Photoshop) with each other."

Windows boss Jim Allchin in an earlier interview said Metro isn't intended to challenge Adobe's PDF format, though he acknowledged some will see it that way.

Adobe spokeswoman Katie Juran said no executives were available to comment.

Microsoft's reassurances don't carry much weight to those who remember how encounters with Microsoft have proved hazardous to smaller companies' health.

In the late 1990s, Netscape's once-dominant Navigator browser was savaged by Microsoft's Internet Explorer. Though Navigator still exists, its influence and market share are minuscule. Seattle's RealNetworks Inc. in 2003 sued Microsoft for antitrust violations over including Media Player within Windows. In federal filings, it says such inclusion has "substantially affected" its business.

How can Adobe stave off whatever competitive threat Microsoft might
The company must reconcile itself to some market-share erosion from Microsoft, said Karen Haus, an analyst with WR Hambrecht + Co.

To increase Acrobat's appeal, Adobe could try bundling additional products with it and offering fixed prices over long periods in exchange for buying commitments, because corporate buyers tend to be price-sensitive, she said.

Adobe will have an easier time protecting its lead among creative professionals, she said. That's especially true if it bundles some of those products into "creative suites," as it already has with Photoshop, its Bridge browser and ImageReady, a Web preparation product.

Adobe has the additional advantages of an excellent reputation for quality and the Mac-oriented, anti-Microsoft bent of some in the artistic community, she said.

The biggest risk to Adobe would be getting diverted by the pending purchase of Macromedia, said analyst Garrett.

"I'd say the risk in a merger situation like this is avoiding confusion and disarray and the stagnation of product lines," he said. "Microsoft is not going to wait until Adobe is ready before it starts going after them."

THE BATTLEFIELD

As products from Microsoft and Adobe, which is about to buy Macromedia, become increasingly competitive, the two companies seem more likely to clash.

Adobe/Macromedia | Microsoft
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.PDF and Acrobat | XML Paper Specification
Flash | Windows Presentation Foundation
Dreamweaver | FrontPage and Visual Studio
Photoshop, Illustrator, Freehand | .Acrylic

P-I reporter Dan Richman can be reached at 206-448-8032 or danrichman@seattlepi.com.
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