

Software Provision and the Impact of Market Integration: A Note

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Abstract

Both deeper market integration and advances in digital technology have driven particularly large decreases in the costs of inter-market software provision. In this note, we first explain the mechanism of how trade costs influence the software provision decision of software firms. Then, we investigated the transformation of production/trade patterns given gradually decreasing trade costs for software products. It is shown that, given that two incompatible hardware exist, deeper market integration may *reduce* the variety of hardware technologies. It is also shown that, if the variety of hardware technologies is reduced by deeper integration, some consumers are made worse off. In other words, deeper market integration, which forms the basis for an easier access to software products may work as a catalyst for Pareto inferior outcomes.

Key Words: software provision; indirect network effects; hardware/software systems; market integration; Pareto inferior outcome

JEL Classification: D43, F12, R12

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