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Amazon in 2020

The global pandemic of 2020 was a mixed blessing for Amazon. Online demand surged as more people stayed at home, but even with its massive logistics infrastructure, Amazon could not meet all the demand and restricted its two-day delivery to essential items for several weeks. This allowed Amazon's competitors, such as Walmart, to get a stronger foothold in the ecommerce market. For many years, Amazon had ventured into several seemingly unrelated businesses like Amazon Studios. Was it time for Amazon to focus on its core ecommerce business?

Evolution of Amazon

Amazon launched its website in July 1995 to sell books online. Bezos' idea was to provide low prices, vast selection, and convenience to customers by creating a virtual store with unlimited inventory and low fixed costs. Soon it expanded its product line into music, movies, electronics, and general merchandise. In November 2000, Amazon launched its marketplace to allow third-party merchants to use its platform to sell their products. At the end of Q1 2020, marketplace sellers accounted for 52% of the units sold by Amazon.¹

In 2002, the company launched *Amazon Web Service* (AWS) to provide cloud-computing services to a large number of companies. AWS provided firms an elastic information technology infrastructure that could be expanded at a low cost on a need basis. Bezos continued to invest heavily in AWS even though financial analysts questioned his decision. In 2019, AWS generated over \$35 billion in revenue and \$9.2 billion in operating income – almost 80% of the company's net income (see **Exhibits 1 and 2** for Amazon's revenues and net income).² The cloud computing market was growing rapidly and it was highly competitive, with large technology players such as Microsoft vying for a dominant share.

In 2005, Amazon launched *Prime*, which offered free two-day shipping for a \$79 annual subscription fee. In 2014, it launched *Prime Music*, an ad-free music streaming service for Prime subscribers. That same year, the price of Prime went up from \$79 to \$99. Despite the increase, Prime membership grew 53% in 2014 and 35% in 2015.^{3,4} In May 2018, Amazon increased the Prime membership fee in the U.S. to \$119 per year but the membership continued to grow. By the end of 2019, Amazon had 112 million Prime subscribers in the U.S. and over 156 million members globally⁵ who spent more than four times what non-Prime customers spent.⁶ In several U.S. cities, Amazon introduced *Prime Now*, a free delivery

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service that would allow Prime members to choose from tens of thousands of daily essentials through a mobile app for delivery within two hours.

In 2006, Amazon launched *Unbox*, later called *Video-on-Demand*, which allowed consumers to instantly stream videos. Amazon Instant Video, later called *Prime Video*, offered a large selection of movies and TV shows to consumers. In 2011, Amazon launched *Amazon Studios* to produce original content for movies and shows. Later, it formed multi-year, multi-billion-dollar licensing agreements with Viacom to bring hundreds of TV shows to its video service. In 2014, Amazon paid HBO over \$200 million to make select shows available on Prime Video; it also paid nearly \$1 billion to acquire Twitch, a live-streaming site for gamers.⁷ A year later, Amazon announced that its Studios would begin making feature films. In 2018, Amazon Studios was recognized with 10 Golden Globe Award nominations and two wins.⁸ However, this success came at a significant cost as the streaming war intensified. In 2019, Amazon spent an estimated \$6 billion, compared to \$15 billion by Netflix and \$6 billion by Apple TV+, and this expense was expected to increase rapidly in the future.⁹

In 2007, Amazon introduced *Kindle*, which was priced significantly lower than the iPad and other tablets. It provided a convenient way for consumers to shop and download digital books and movies from Amazon's store. Amazon also built an AppStore that was available to millions of consumers in nearly 200 countries and which rivaled Google and Apple's AppStores for apps and games. In July 2014, Amazon launched *Fire* phone, which included 3D-like images and a "Firefly" button to identify objects that could be purchased from Amazon. Only three months later, disappointing sales led Amazon to announce that it would take a \$170 million write-down on the Fire Phone.¹⁰

Soon after the failure of its phone, Amazon launched *Echo*, a device with a voice-activated virtual assistant that answered questions and placed orders on Amazon. By 2018, Amazon sold 100 million Echo devices, and this number doubled by the end of 2019.¹¹ In early 2015, Amazon introduced *Dash Replenishment Service* that enabled connected devices to order goods when supplies were running low, e.g., a coffee maker could automatically order more coffee beans. The same quarter, the company also launched *Dash Button* - a small button that Prime customers could place in their homes to reorder frequently used household items. However, due to weak demand, Amazon discontinued this service in 2019.

In its early days of e-commerce, Amazon had pioneered the recommendation system that allowed it to suggest books, music, and videos to its customers based on the purchases of other customers with similar preferences and buying patterns. In 2011, Amazon launched its own advertising network to serve targeted ads to customers. A customer who visited Amazon for, say, a camera, but did not buy, could be tagged and served a camera ad later when that customer visited a camera- or photography-related site. In 2019, Amazon generated \$9.85 billion in U.S. digital ad revenue from its ad network.¹²

In 2012, Amazon entered the \$7.2 trillion U.S. wholesale and distribution market¹³ with *AmazonSupply*, later called *Amazon Business*, which offered products for business clients (including janitorial supplies, medical supplies, and mechanical parts). Amazon's easy-to-use website, 24-hour delivery, and low prices were relatively unique in the wholesale business, which was primarily composed of regional, family-run businesses that boasted superior client relationship through personal selling. By 2014, Amazon's catalogue had increased to 2.2 million items compared to 1.2 million products in the catalogue of the market-leader, W.W. Grainger.¹⁴ By 2019, Amazon Business was estimated to generate \$10 billion in revenue, which some analysts forecasted to grow to over \$30 billion by 2023.¹⁵

In March 2015, Amazon announced its new *Home Services* business for Amazon consumers to select vetted and insured professionals to perform plumbing, electrical, pet care, and other home services. Amazon consumers could view price and scheduling information for those services during the regular checkout process.¹⁶

In June 2016, Amazon launched *Amazon Inspire*, an online marketplace with free lesson plans, worksheets, and other instructional materials for school teachers. Rohit Agarwal, general manager of Amazon K-12 Education said, “Every teacher should be able to use the platform with zero training. We are taking a big step forward to help the educator community make the digital classroom a reality.”¹⁷

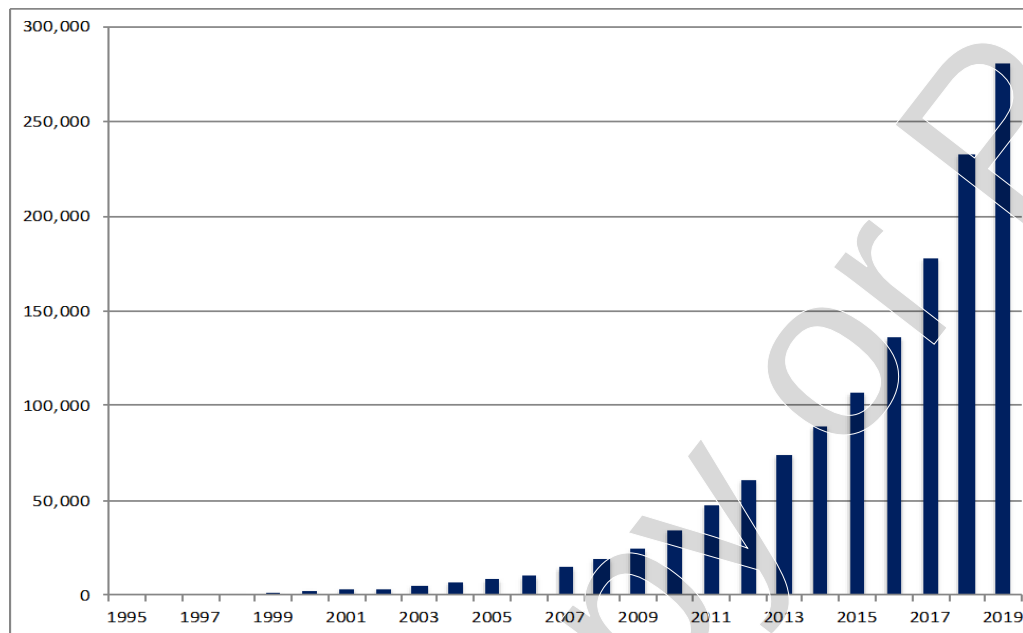
In June 2017, Amazon shocked the retailing industry by acquiring Whole Foods, an upscale grocery chain in the U.S., for \$13.4 billion, a 27% premium over its trading value. The grocery industry, a large market with an estimated annual spending of about \$800 billion in the U.S, was not new to Amazon. Almost a decade ago Amazon introduced *AmazonFresh*, but until now it had achieved limited success. With Whole Foods acquisition, Amazon would get access to Whole Foods’ 460 stores and high-income customers. Many experts believed that this would help Amazon penetrate grocery market where it had limited success until now. However, Whole Foods had only a 1.2% share in this market that was dominated by Walmart with a 14.5% share. The grocery industry was highly competitive and even Amazon could not get more than 0.2% share in the last ten years.¹⁸ As a result of intense competition and razor thin margins, most grocery retailers, including Whole Foods, were struggling. Did it make sense for a technology company with stratospheric stock price to enter this thin margin industry?

In 2016, Amazon unveiled Amazon Go stores, a cashless convenience store where an Amazon consumer could simply pick up an item and walk away and his or her credit card with Amazon would automatically be charged for that item. By the end of 2019, Amazon operated 25 Go stores.¹⁹

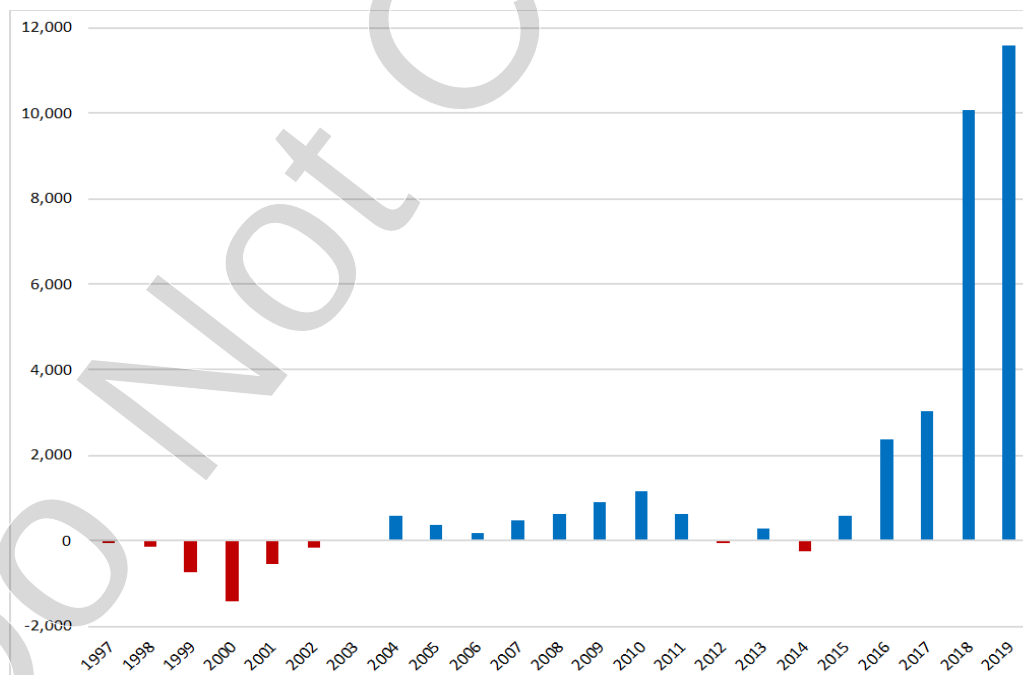
Although Amazon had been very successful so far, experts started questioning if the company was spreading itself too thin. They were reminded of Sears that grew rapidly for decades by expanding into many businesses, only to file for bankruptcy in 2018.

Impact on Retailers

The rapid growth of Amazon was causing a major disruption for traditional retailers. By 2019, Amazon had become the digital giant with over \$280 billion in revenue and 840,000 employees worldwide.²⁰ Brick-and-mortar retailers continued to lose business to Amazon and were fighting for their survival. Traditional bookstores like Barnes & Noble or electronic chains like Best Buy were becoming Amazon’s *showroom*, such that customers would see, say, a television in Best Buy, get all the advice and information from Best Buy’s sales person, but later buy it at a cheaper price at Amazon. Was this the end of traditional retailers, or could they find a new strategy to survive?

Exhibit 1 Amazon's Revenue 1995 – 2018 (\$ millions)

Source: Compiled from company annual reports, accessed June 2020.

Exhibit 2 Amazon's Net Income 1997-2018 (\$ millions)

Source: Compiled from company annual reports, accessed June 2020.

Endnotes

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