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Is Amazon.com a monopoly?

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Summary

Starting as an online bookstore in 1995, Amazon has now evolved into a global-spanning e-commerce colossus offering more than 562 million products online. Their annual membership program has upwards of 85 million subscribers, equivalent to two-thirds of US households, and in 2017 they held 44% of all e-commerce sales. However, Amazon's rapid expansion has engendered continuing opposition from observers who believe that the company is monopolizing online retail. This case study will analyze the plausibility of this claim by first discussing Amazon's innovations and growth before examining in what specific manners the company's monopolistic power is to be found. We argue that while Amazon is not a monopoly by textbook definition, its imposing dominance does indeed limit room for competition and innovation.

Introduction

It is no doubt that Amazon.com, Inc. is a leader in online retail. The company first began as an online bookstore, but it now offers more than 562 million products on its website (as of January 2018),[1] ranging from fashion to intelligent personal assistant devices to name a few. By harnessing innovation and disrupting industries, the company achieved a prominent presence in other sectors as well, such as logistics, media, payments, hardware and data storage. Its vast range of products and services have led many to join Amazon as the 'Everything Store.'[2]

Today, the company is a popular choice for online shopping in the country, as it boasts a large pool of customers in US online retail. Amazon's $99-a-year signature membership program, Prime, has around 85 million subscribers—equivalent to two-thirds of US households.[3] Its popularity can be seen further where 55% of US online shoppers begin their product searches on Amazon, while only 26% for Google and 16% for other online retailers.[4] The company even managed to capture 44 percent of all US e-commerce sales throughout 2017, surpassing all its other competitors.[5]

However, Amazon's lead in online retail has led many to argue that the company is monopolizing retail. Observers of retail such as advocacy groups for community-rooted enterprises[6] and open market think tanks[7] believe that Amazon currently represents a monopoly that is bad for the economy. The monopolistic claims brought upon Amazon is that the company is becoming too dominant in the online retail market, especially with its commanding amount of retail sales and other businesses' dependence on Amazon's services. Amazon is further accused of being a monopoly because it is harming competition and caused a decline in the number of independent retail businesses. It is difficult for these businesses' products and creators to find an audience because of Amazon's dominance.

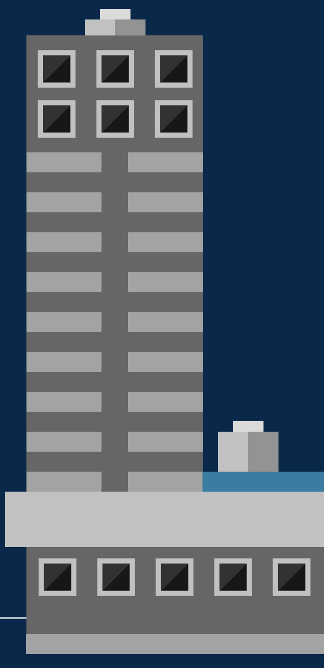
With the issue in mind, this case study will answer the question of whether Amazon is a monopoly by looking at both sides of the argument and exploring key statistics. By analyzing secondary data through a desk research, this case study will firstly examine Amazon's business model and growth to help understand how the online retail giant does its business. Then, in the next section, we will dive further into Amazon's monopoly accusations and see whether this is true. This case study will then be concluded with several key takeaways of the issue at hand.

The extraordinary size of Amazon

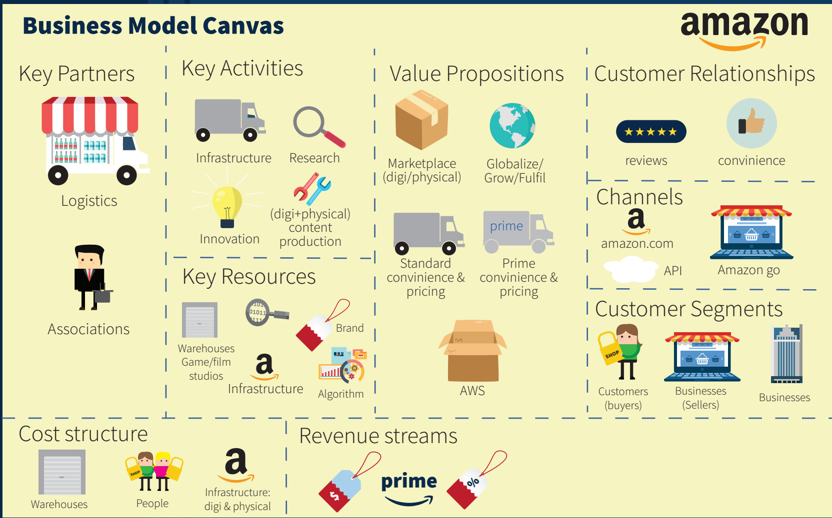
1. Business model

Being one of the largest companies in e-commerce that also covers a wide array of services, Amazon incorporates a hybrid of several business models that work together with clockwork precision. As an online retailer, their first and foremost model is Business-to-Customer (B2C), where they offer a diverse range of products to purchasers through their online platform. Profit is made through the addition of small markups on their products that are still low enough to make their prices highly competitive on the market.[8] Additionally, Amazon also generates profit through Amazon Prime, their exclusive yearly membership program. The B2C model is also used to connect different accomplice retailers with potential customers where they sell products that are usually less common goods with high price tags. This strategy allows Amazon to keep their stock moving at a constant rate in order to avoid economic losses, whilst also retaining commission for every sale of a product.[9]

Moreover, Amazon implements a Customer-to-Customer (C2C) business model through their Marketplace. Here online users are given a platform to make transactions with other users through the sale and purchase of personal products. A Business-to-Business (B2B) model is also applied, where Amazon acts as an intermediary between businesses who look to cater to more specific professional requirements during their transactions.



The principal elements that are in Amazon's business model can be understood through the canvas below:



Graph 1. Amazon's business model canvas.[1]

2. Innovations

Since Amazon's humble beginning as a garage-based online platform for selling paper books in 1995, Jeff Bezos had already strived to make the company revolve around continuously unparalleled innovations such as the "recommendation engine" and the online user reviews feature. It was these technological ingenuities that allowed Amazon to ship ordered books to all of the country's 50 states and also to 45 other countries within only its first 30 days of business, and after just two years in the running, the company had already gained a market capitalization of around $438 million.[11] In the ensuing years, Amazon also initiated several other innovations that established highly convenient and uncomplicated purchasing procedures.

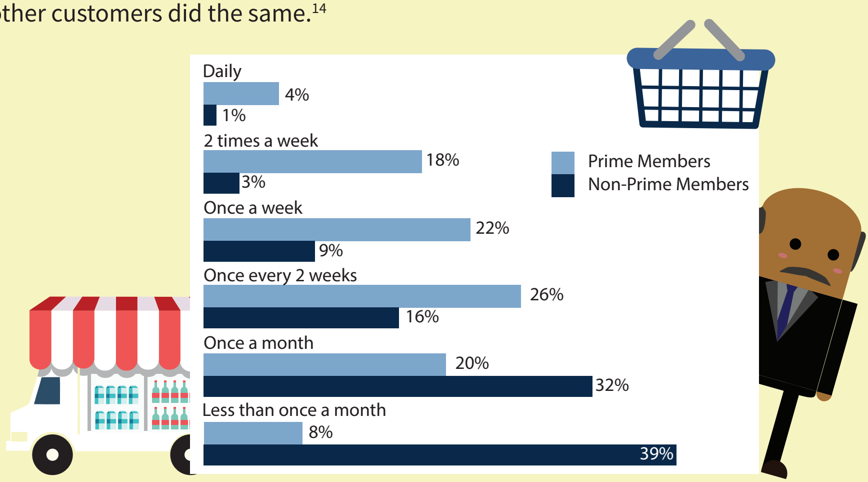
a. One-Stop Shopping Experience

The company's rapid commercial success eventually allowed it to expand its market far beyond its modest bookstore origins in which it gradually evolved into a prodigious e-commerce colossus that started to sell everything from toddler toys to bakery and bread. By encompassing such a heterogeneous inventory of products, Amazon aspired to offer a one-stop shopping experience for its customers, unreservedly transforming how people utilized the internet to fulfill their needs and ultimately revolutionizing the entire e-commerce industry during the process.

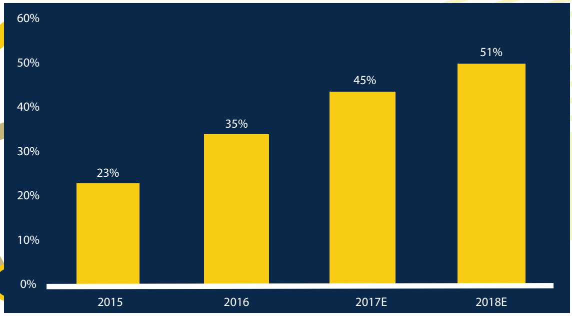
b. Amazon Prime

Driving forward Amazon's growth up until today are numerous carefully crafted innovations which aim to set Amazon apart from its e-commerce rivals--and with continued success in doing so. One of Amazon's most thriving and lucrative innovations is Amazon Prime, an annual membership program that initially only offered free two-day shipping for a wide range of goods and services. Launched in 2005, Prime swiftly became one of the company's biggest success stories as more and more customers made Amazon's website their default destination for online shopping destination due to the existence of the program. Naturally, Prime's biggest appeal was the unlimited free shipping that it offered for only $99 per year, which was the first of its kind in e-commerce.[12] Over the years Amazon then added several other services to Prime such as unlimited instant streaming to thousands of movies and television episodes, access to exclusive products, Alexa voice shopping as well as free same-day delivery for specific products.

Statista found that Prime’s success is underlined by how, for the past few years, the average annual spend of a typical Prime customer is almost two-fold of that of a non-Prime customer ($1.300 versus $700).[13] Meanwhile, Morgan Stanley estimated that between the period of September 2016-September 2017 alone, the average Prime subscriber spent $2.486 compared to only $544 for ordinary customers. Furthermore, a research carried out by Feedvisor discovered that Prime customers are more frequent visitors to Amazon, with 31% of them opening the website on a daily basis - compared with only 11% of non-subscribers. In addition to this at least 18% of Prime members were found to make purchases on Amazon at least twice per week, while only 4% of other customers did the same.[14]

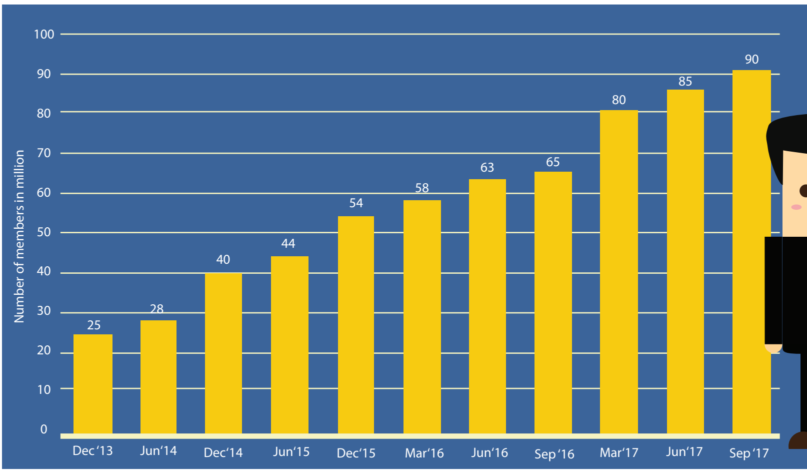


Graph 2. Comparison of purchase frequency between Prime and non-Prime members.[15]



Graph 3. Percentage of US households with at least one Prime subscriber. [16]

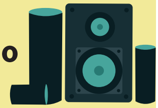
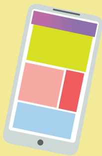
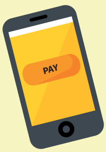
Amazon Prime's statistics become even more impressive when we take a look at its explosive growth in recent years. From only 25 million members in December 2013, Prime has since expanded to a stupefying 90 million in September 2017 and therefore rendering a compound annual growth rate of 29.2% over the last five years. As an effect of this growth, it is also predicted that more than half of all households in the US (around 51%) will be Amazon Prime subscribers in 2018 - an increase from an already impressive percentage of 45% from the previous year.[17]



Graph 4. Number of Amazon Prime members in the US as of September 2017 (in millions). [18]

c. Products

Other than Prime, Amazon also has several innovations, such as the cashierless Amazon Go store, the personal assistant Amazon Echo, and the social media-esque Amazon Spark.

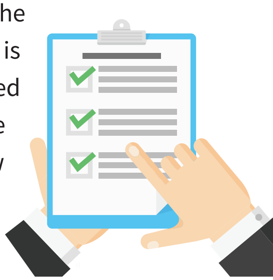
Name of Innovation	Year Released	Description
Amazon Echo 	**2014**	A brand of hands-free smart speakers that connect to the voice-controlled personal assistant service Alexa.
 **Amazon Dash**	**2015**	A consumer product ordering service where customers can use small Wi-Fi connected devices (Amazon Dash Buttons) to order specific goods through a button press.
Amazon Spark 	**2017**	An Instagram-inspired feature integrated within the Amazon application where users can “follow” certain product brands and categories to discover images of new items.
 **Amazon Go**	**2018**	A cashier-less store that utilizes high-end technology to automate the majority of the purchase, check out, and payment steps of a retail transaction.
Amazon Prime Wardrobe 	**2018**	A Prime-exclusive program where customers order a box filled with three or more clothing items of their choosing and are then given seven days to try the items at home to decide which clothes they want to purchase.

d. “Recommended for You”

In addition to their novel creations, the historic technological innovations that have been implemented since Amazon's early days also remain to be used today, despite several developments. For example, the recommendation engine that was pivotal to Amazon's growth in its initial years now accounts for at least 35% of total product purchases online.[19] Using recommendations as a targeted marketing tool, Amazon effectively establishes a highly personalized shopping experience that is unique to every customer through an ‘item-to-item collaborative filtering’ mechanism. The “Recommended for You” feature, for example, leads customers to a page filled with products from categories that have recently been browsed, while the “Frequently Bought Together” section suggests complementary items that customers might want to purchase along with what they already have in their shopping cart.

e. Customer Satisfaction

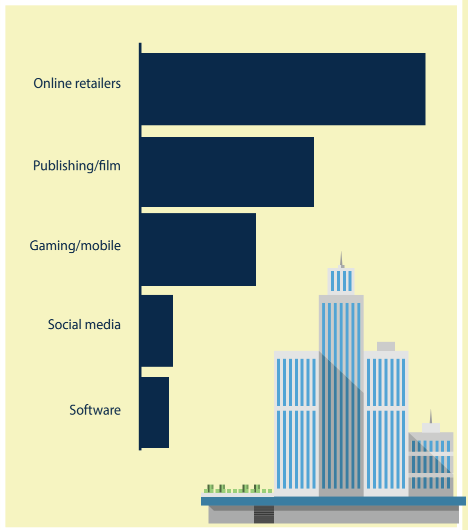
However, Amazon’s remarkable accomplishments are not solely due to their continuous use of innovations. An even more crucial aspect to the business model is their high emphasis on customer satisfaction, in which they aim to become the ‘largest customer-centric company in the world’. Key to this principle is ensuring that the needs of Amazon’s customers are always prioritized ahead of innovations. Innovations will not be carried through if they are deemed to not place customers as the main priority, regardless of how economically profitable it may seem for the company.



3. Acquisitions

Amazon has made acquisitions of at least 82 companies since its founding in 1995, with the largest of them being on retail-based companies that have allowed Amazon to expand their market into new product categories.[20] They made their first acquisition in April 1998 when they carried out a joint $55 million purchase for IMDb, Telebook, and Bookpages. Amazon proceeded to make acquisitions of nine other companies before the millennium.[20]

During the subsequent decade, Amazon made another 22 acquisitions with most of them being horizontal business integrations of other similar online retailers. The company made its largest (at the time) acquisition in 2009 when it paid $1.2 billion to obtain Zappos.com, an exclusively online shoe seller. Amazon also focused on expanding its arsenal of digital content by acquiring entertainment-based companies in the movie, music, gaming, and audiobook industries.



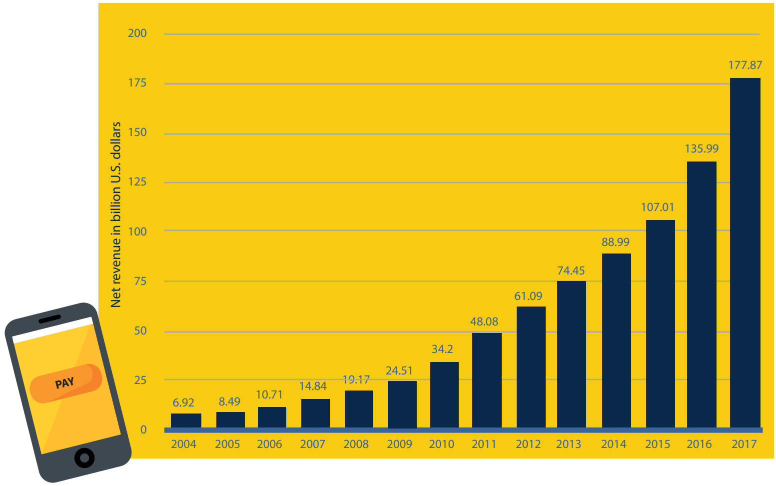
Graph 5. Type of Amazon acquisitions between 2000-2009.[22]

Following this period, Amazon's acquisitions became much more frequent as the company's total worth continued to grow exponentially year by year. A total of 48 acquisitions have been made since 2010, amounting to at least $17 billion worth of market value - including the $650 million acquisition of Souq, an e-commerce company regarded as "the Amazon of the Middle East."[23] However, the overall variety in the type of companies that Amazon has acquired since 2010 has highlighted their eagerness to venture into previously uncharted industries, as they have moved away from their traditional acquisitions of digital content and online shopping towards acquisitions of companies specializing in next-generation technology. This includes the $800 million purchase of Kiva Systems, a manufacturer of mobile robotic fulfillment systems, and the $370 million purchase of Annapurna Labs, a semiconductor chip designer.

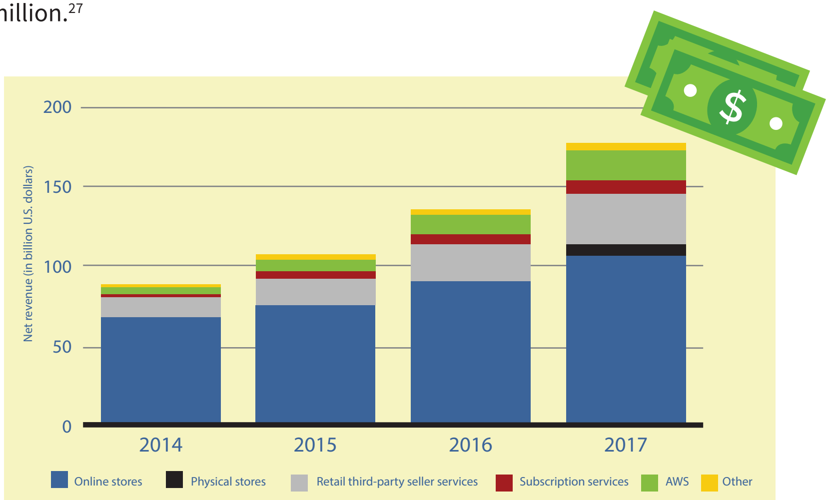
Despite this, Amazon's most startling move came when it acquired Whole Foods for a record-breaking bet of $13.7 billion, making it the company's largest purchase in history (with their previous largest acquisition being only a tenth of that amount).[24] The surprising nature of this vertical acquisition was not only due to its astronomical valuation but also due to the fact that it effectively guaranteed Amazon an instant and robust foothold into grocery, which was considered the largest untapped category of online retail.

4. Company growth

After twenty years since its first public valuation at a modest $438 million in 1997, Amazon has now grown into a global-spanning e-commerce behemoth worth at least $458 billion on the market. This translates to a return of around 50.000% for shareholders who invested in Amazon when it was first listed.[25] In terms of net revenue, the multinational e-commerce company posted a total of $177 billion in 2017 - a staggering 2.800% increase from 2004.



Unsurprisingly, Amazon's online stores have accounted for the majority of their revenue over the years, which is mostly helped by the success of Amazon Prime. Most recently, the online stores made up $108 million of Amazon's total revenue, followed by the contributions of retail third-party seller services at $31 million, Amazon Web Services (AWS) at $17 million, and subscription services (income from Prime fees) at $9 million.[27]

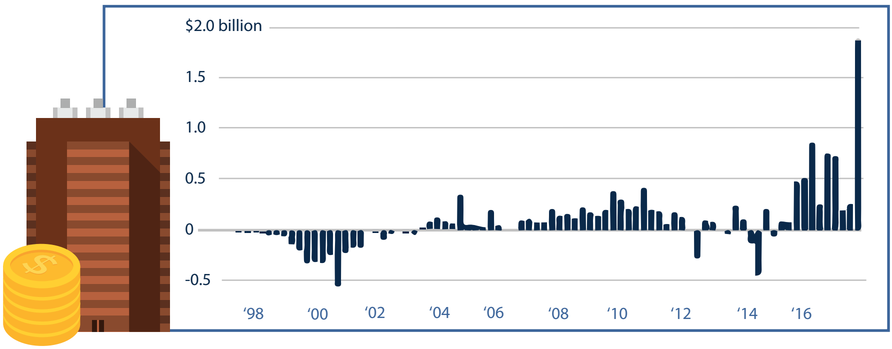


Graph 7. Amazon net revenue based on a segment from 2014-2017.[28]

Nonetheless, Amazon's impressive growth in market value and net revenue is in stark contrast with its achievements in its annual and quarterly profit. Compared with nine other companies with the largest market valuations in the US, Amazon has accumulated the least amount of net profit with only $5 billion over the past 20 years. In comparison, while Wells Fargo has just over half of Amazon's market value at a mere $262 million, their net profit of $244 billion is 4.800% of that of Amazon's. Meanwhile, Exxon Mobil, the most profitable of the 10 companies, has managed to acquire more than 100 times of Amazon's profit at an impressive accumulation of $597 billion over the past 20 years.[29]

Graph 8. Market value and accumulated profit of US' 10 largest companies. [30]

Amazon's struggle to generate profit is correlated with the company's emphasis on large expenditures for long-term growth and goals, in which they sacrifice financial profitability for overall expansion of the company. This high-risk business model led Amazon to continuously lose money in its first four years of going public. The e-commerce giant has only very recently been able to produce a fairly substantial amount of profit when it announced a surplus of $1.8 billion at the end of last year. While a quarterly profit of just under $2 billion is by no means spectacular when juxtaposed with those of other large companies in the US, it is worth noting that it took Amazon 14 years since going public in 1997 to generate the same amount of profit that it did in the fourth quarter of 2017 alone.[31]



Graph 9. Amazon quarterly profit and losses, starting from the third quarter of 1997.[32]

Is Amazon a monopoly?

Now that we have understood Amazon's enormous reach and impact, let's examine whether the company is a monopoly. Even until now, there is an ongoing and heated debate on this issue. On one side, critics warned that Amazon's dominance resembles a monopoly and that its growth must be stopped through government action. But on the other side, many denied this way of thinking and argued that Amazon only holds 15% of the e-commerce market and that Amazon is "the reverse of a monopoly" with low prices and almost-zero profits.[33]

These arguments only give us a slight understanding of the facts and statistics at hand, as there are still plenty of other aspects that we can explore. Therefore, in this chapter we will examine three aspects that can help answer whether Amazon is a monopoly; by analyzing the Amazon business through the definition of a monopoly, Amazon's commercial domination, and its impact towards competition in the country.

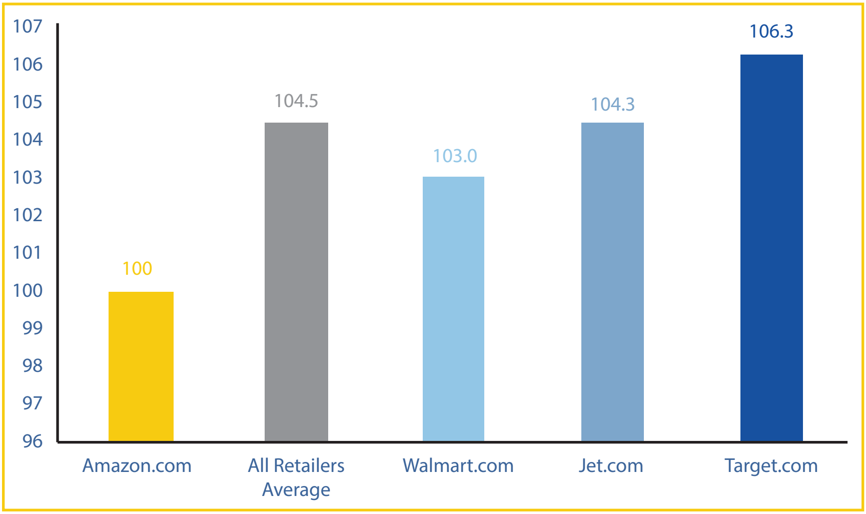
1. How monopolies are defined

Monopoly power is defined by the regulations that are set out in the Sherman Antitrust Act (US antitrust law) through the US Federal Trade Commission. The Sherman Act states that:

> *"Monopolization is when a business has the power to control prices in the relevant market; and when it conducts anticompetitive practices, as opposed to growth as a result of a superior product or business acumen"*[34]

From this definition, business is categorized as a monopoly when it can control prices and create an anticompetitive environment. However, the main purpose of the Sherman Act during its creation was to protect consumers – not competitors – from its anticompetitive practices, so to focus on Amazon's dominance towards its competitors would be misleading. Therefore, based on the Sherman Act, businesses become a monopoly – and violate the US antitrust law – when they monopolize the industry and set high prices for its consumers, which in turn harms consumer welfare.

So, what are the prices of Amazon's products like? In 2018, the e-commerce pricing analytics firm Profitero found that Amazon remains the online price leader with prices averaging 10% less than Walmart, Jet.com, and Target. The following chart illustrates the comparison between the top four online retailers in the US.



Graph 10. Price index comparison between Amazon and other retailers.[35]

Amazon's status as the cheapest online retail in the country is not a surprise to most people since they have held this position for long periods since the company went public. Due to its Prime membership program along with its various benefits and offers, Amazon is well-perceived by the public to be the cheapest e-commerce platform in the US. By offering competitive bargains, and with two-thirds of the US population subscribed to Prime, Amazon is not in a position to harm its consumers.

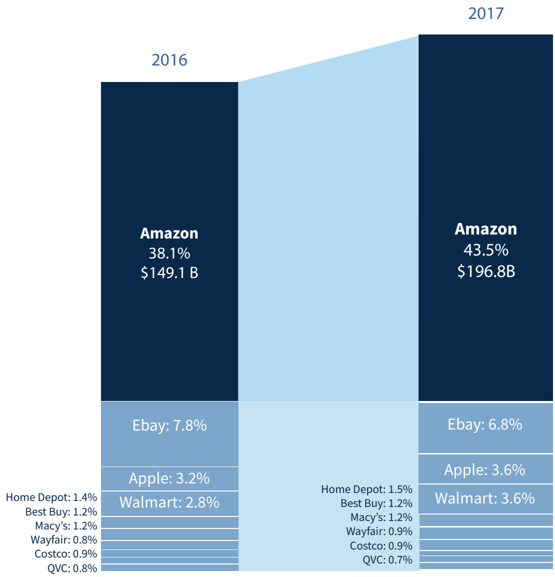
When monopolistic companies exert their power on the market, it is usually done by increasing prices to gain more money from the sales. In Amazon's case, despite its impressive growth and popularity, the company lost money roughly half the time in the first twenty years of its business.[36] In 2016 alone, it earned a weak 1.7 percent net profit margin overall for a business of its scale.[37] At that year as well, Amazon suffered huge losses in online retail but was spared through its other more profitable products, such as Amazon Web Services (AWS). Therefore, Amazon clearly did not increase the prices of its online products to reap more profits, contrary to what a monopoly usually does.

Looking at Amazon from the standpoint of definition, the company have not violated the current US antitrust laws. Amazon's pricing strategy is very much the opposite of what monopolistic businesses do, as it offers low, favorable prices for its products and maintained consumer welfare. They have also spent more money than they earn in previous years, meaning that Amazon does not portray the classic definition of a monopoly if we were only to look at this case from a single perspective.

2. Market domination

Another way to assess whether a business is monopolistic is by looking at its domination; both market-wise and structure-wise. For an e-commerce retail platform like Amazon, we can compare its position in the overall retail and online retail market. In 2017 the company only made up 4% of total retail revenue in the US, despite Amazon's impressive scale.[38] This is because Amazon faces plenty of competition from other retail companies that have had a significant foothold in offline retail such as Walmart, Costco, and Kroger.

In online retail, however, the scenario is quite different where Amazon holds a commanding lead over the likes of eBay, Apple, and Walmart. The following graph depicts Amazon's e-commerce market share compared with its competitors.



Graph 10. Price index comparison between Amazon and other retailers.[35]

With almost 44% of all US e-commerce sales coming from its platform, Amazon's position is near untouchable at the top. e-Bay only has 6.8% online retail market share, while Apple and Walmart both have 3.6%. It is no wonder because statistically, the majority of US online shoppers begin searching for products on Amazon.com, rather than through other search engines or online stores, meaning more people will likely be purchasing from Amazon. It is because of this online market domination that many critics accuse Amazon of being a monopoly by reaping market share that far outnumbers its competitors.

Besides market share, Amazon's power and dominance are also visible in the structural advantages that it enjoys. Amazon scoops tons of market insight from its third-party Amazon Marketplace, where over 30% of its total goods are sold through the site.[40] Data from its market insights greatly improve Amazon's marketing and pricing strategies, giving them robust leverage over their competitors. For instance, if Amazon sees that Wonder Woman costumes are popular on a marketplace seller's page, it will start selling these directly and then lower the price compared to the original seller. It's worth to note that in this digital era, data is considered as 'the new oil' and Amazon's possession of this trove of data is why many believe Amazon deserve anti-monopoly attention.

Amazon's structural advantage also comes under scrutiny each time it acquires another company. Since 1998, Amazon has bought more than 70 companies both horizontally (similar e-commerce platforms) and vertically (companies in other levels of production).[41] These rampant acquisitions, particularly the vertical ones, raised concerns for the future of commerce. Its competitors are growing weary hat each level of production in the US, from manufacturing to delivery, could be handled by companies that are owned or supported by Amazon in the future.

Does Amazon's dominance mean that it is a monopoly? After we have understood their broad reach and structural advantages, the argument of Amazon exercising monopolistic power seems plausible. No wonder many have voiced for Amazon to be split up into smaller companies to prevent them from becoming a true monopoly in the future.

3. Impact on competition

The final aspect to examine is whether Amazon's business success has had a negative effect on competition. A good question to ask is "has the number of small businesses reduced since Amazon entered the market?" since the number of small businesses is vital for a healthy and competitive environment.

According to US Census Bureau data, the number of new business launches (or startup rate) dropped to a 10-year low in 2015 at only 414,000 – a massive drop from 558,000 back in 2006.[42] This decline is bad for the economy since new businesses

account for virtually all new job creation. While this decrease might not be directly correlated with Amazon, many startup founders are blaming big tech companies, particularly Jeff Bezos' company itself. As one startup founder – who wished to remain anonymous – put it:

"People are not getting funded because Amazon might one day compete with them. If it was a startup versus startup, it would have been a fair fight, but startup versus Amazon and its game over."[43]

As Amazon grew over the years, they became capable of developing similar products to its competitors and undercut them on price. When this happens, Amazon has reduced competition by making it harder for new products, startups, and creators to find an audience. Small businesses are then faced with limited options, particularly two: be acquired by Amazon to sustain its business or perish from not being able to grow large enough to compete with the big tech. In theory, it leaves little room for new entrepreneurship and innovation in the marketplace, and the existence of a startup decline could support that theory.

Amazon's significance is not only that it has blocked competitors, but it has also made them vulnerably dependent. A report by Forrester Research noted that many businesses who fear Amazon as its competitor in online retail, in fact, use Amazon's services such as Marketplace and AWS.[44] By using said services, these businesses provide a steady flow of information to Amazon while at the same time, ironically, trying to gain an advantage over Amazon.

However, it is not all bad for every Amazon competitor that uses its services. For some that choose to be a third-party seller on Amazon, they might enjoy sales growth that they could not have previously achieved if they were to sell products solely on their website. Amazon's larger consumer base might be what these small businesses need to grow and become more profitable.

When we place our focus of assessment on the competitors, clearly Amazon seems to exercise monopoly power. The decrease in startup rate and competitors, along with creating an environment where other businesses are dependent on Amazon has supported the claim that the tech giant is harming competition altogether. These findings could support the wider claim that Amazon is a monopoly and that it deserves anti-monopoly attention.

Conclusion

Amazon's stupefying growth since its establishment in 1995 has paved a path for it to become one of the most prominent players in online retail. However, such growth has entailed remarks from several observers who argue that Amazon is monopolizing e-commerce. Upon further inspection, these claims are not completely unfounded. While it is permissible that Amazon's pricing strategy is not what a monopoly would ordinarily implement – in the sense that Amazon does not utilize its dominance to increase the prices of their products – they do in fact very much dominate online retail. As of 2017, Amazon is in possession of 43.5% of the e-commerce market share, far beyond their closest competitor eBay at just 6.8%.

On top of this, the company has also carried out far-reaching acquisitions of at least 80 other businesses, some of which were seen as potential e-commerce competitors, while others operated within different industries and levels of production. Moreover, it is found that Amazon's imposing presence has in actuality discouraged the emergence of new startups and creators. Existing competitors, on the other hand, often have no choice but to use the services that Amazon provide such as the Marketplace and AWS. From here it seems reasonable to believe that Amazon does indeed hold monopolistic power in online retail – in particular when we evaluate how its presence negatively affects the businesses around them.

Nonetheless, Amazon's current dominance in the market also offers several constructive lessons to be learned. John Bezos has gained success in leading Amazon to where it is today due to several key factors, most notably the company's emphasis on prioritizing customer's needs and convenience along with their continuous creation of unprecedented innovations. Under Bezos' leadership, Amazon has also shown the willingness to take high-risk decisions that place long-term company growth before short-term profit, whilst simultaneously incorporating state-of-the-art technology within how they conduct business. Furthermore, it may also be argued that while Amazon has unparalleled online retail supremacy, their innovations have only served to improve market outcomes and have encouraged competitors to reevaluate their business models in a positive manner. Amazon's presence has prompted other players in the e-commerce market to offer increased efficiencies and value for consumers, thus majorly limiting the harm that Amazon's monopolistic power actually ensues.

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