



# AMAZON STRATEGIC ALTERNATIVES

## Strategic Alternatives

### Statement of Primary Issue

From online streaming to grocery shopping, Amazon has offered service to its customers across multiple markets. As a result, Amazon's competition is coming from numerous directions. In other words, the primary issue that Amazon is facing is intense competition from other industry giants, including but not limited to Disney, Walmart, Whole Foods, and Google.

Amazon's competition came from its multichannel distribution; Walmart, for example, has competed with Amazon directly. In addition to the direct competition, Amazon must keep an eye on indirect competitors, such as Google's user experience optimization. Furthermore, even though Amazon's value proposition might seem to be unique at first, other competitors, such as Walmart, have already duplicated Amazon's key value proposition, the free two-day shipping. Lastly, Amazon needs to continue to expand its value proposition through online streaming, as its competitors will be entering this market segment, such as the new online streaming service that Disney introduced.

In sum, Amazon's key issue is to adopt market strategies to further differentiate themselves from both direct and indirect competitors in order to attract and retain customers. Three strategic alternatives that could possibly help Amazon are presented below.

### Strategic Alternative 1

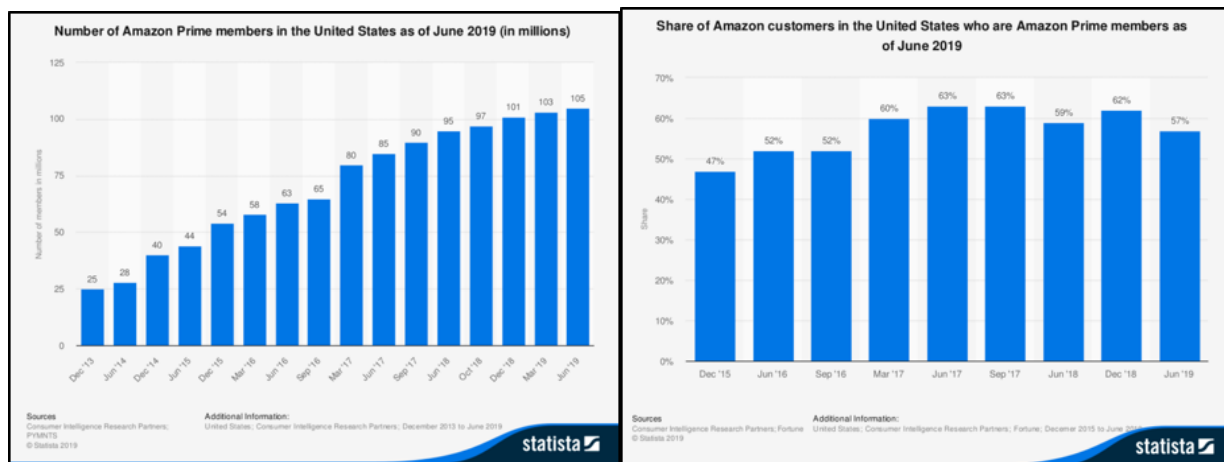
Amazon could adopt Strategic Withdrawal Strategy to maintain its current market share. Amazon holds a market share of 37.7% of the entire online commerce and is the largest online retailer in the world. As a result, Amazon should maintain its strength in the online market as this provides a highly competitive advantage. However, Amazon has created a multichannel distribution, but Amazon could adjust their multichannel distribution to a smaller scale, since the complexity of the multichannel distribution is a crucial potential problem. Specifically, although the brick and mortar store that Amazon launched allowed Amazon to reach a broader range of audiences, the risk of resulting in unsatisfied customer experience may severely harm Amazon's brand image and lead to a negative word of mouth. As an online market leader that needs to defend themselves from numerous competitors, strengthening customer relationships is a must, not to mention the risk to sacrifice the customer relationship as the multichannel distribution might potentially result. Explicitly, Amazon could withdraw from all Amazon Go stores

and instead invest in optimizing the deals that Prime members could get on Whole Foods and online grocery product offerings.

The advantages of this strategy include the reduced investment on distribution channels and potential increase in customer satisfaction, which is a critical component to increase or maintain the current customer base. On the other hand, this strategy also contains some drawbacks. Withdrawing from all Amazon Go stores might potentially result in a decrease in revenue. However, as an online market leader, if Amazon keeps outperforming its competitors in the online market segment, this does not seem to be a huge issue.

In the short-term, Amazon would be able to defend themselves from Walmart and other strong competitors and maintain its current standing of the largest online retailer in the world. In the long-term view, perhaps the reduction of the investment in Amazon's brick and mortar stores could be invested in Amazon's online offerings, thus further expand Amazon's market share in the online segment and the profitability.

### Market Potential Estimation – Chain Ratio Method



Until June 2019, there are approximately 105 million Amazon Prime users, which account for 57% of the total Amazon customers in the United States (Key, et al., 2019). From here, we could know that there are currently 184.2 millions of Amazon customers, calculated by  $105 / 0.57 = 184.2$ .

We could estimate that there are 79.2 million Amazon customers who are not Amazon Prime members.

Assumption one:

Assume that Amazon withdraws all their investment from Amazon Go and further invest in optimizing their deals in places like Whole Foods or online groceries. 30% of the Amazon customers who are not Prime users are estimated to give Amazon Prime a try. Hence, 23.76 million of Amazon Customers who are not Prime users will subscribe to Amazon Prime if aware, calculated by  $79.2 \text{ million} \times 30\% = 23.76 \text{ million}$ .

Assumption two:

Safely assume that 35% of Amazon customers will be aware of this improvement, then roughly 8.316 millions of Amazon customers who are not Prime users will subscribe to Amazon Prime if they look into what good deals that Amazon has to offer at Whole Foods / online grocery. (calculated by  $23.76 \text{ million} \times 0.35 = 8.316 \text{ million}$ )

Assumption three:

Assume that 65% of Amazon customers in the United States do look into what deals Amazon has to offer on Whole Foods / online groceries, then approximately 5.41 millions of Amazon customers who are not Prime users will subscribe to Amazon Prime. (calculated by  $8.316 \times 0.65 = 5.41 \text{ million}$ )

Therefore, by the end of 2020, Amazon would be able to have approximately 5.41 millions of new Prime members, which represents a 6.83% of conversion rate, calculated by  $5.41 \text{ million} / 79.2 \text{ million} = 0.0683$ .

Amazon's subscription service is mainly constituting Amazon Prime, and it had generated 5.0 billion in revenue at its third fiscal quarter of 2019. (Protalinski, 2019) Moreover, Amazon Prime members spend an average of \$1,400 on the online shopping platform every year while non-Prime users only spend an average of \$600 every year (Key, et al., 2019). As a result, if Amazon adopt the Strategic Withdrawal strategy, by the end of 2020, Amazon would possibly generate \$7.574 million in revenue, calculated by  $\$1,400 \times 5.41 \text{ million} = \$7.574 \text{ million}$ .

Similarly, the market potential estimation for the year 2021 is calculated as follow:

$73.8 \text{ million (Amazon customers who are not Prime users)} \times 30\% \text{ (will subscribe if aware)} \times 35\% \text{ (will subscribe if they look for good deals through Amazon)} \times 65\% \text{ (estimate percentage of Amazon customers who look into the deals)} = 5.03 \text{ million}$   
(numbers of new Prime members in the year 2021, the conversion rate is 6.8%).  
Similarly, Amazon would possibly generate about \$7.042 million in revenue. ( $\$1400 \times 5.03 \text{ million} = \$7.042 \text{ million}$ )

As for the year 2022, the market potential estimation is as follow:

$68.77 \text{ million} \times 30\% \times 35\% \times 65\% = 4.69 \text{ million}$  (numbers of new Prime members in year 2022, the conversion rate is 6.82%). Amazon would possibly generate additional \$6.566 million in revenue. ( $\$1400 \times 4.69 \text{ million} = \$6.566 \text{ million}$ ).

### Strategic Alternative 2

Amazon could utilize the Flanker Strategy to defend itself by attacking its competitors. Walmart, as a large retailer, has always been a direct competitor for Amazon. Not only did Walmart duplicate Amazons' free two-day shipping but also did they start to pull market share away from Amazon by offering potential customers similar deals.

Amazon could actively attack Walmart in the grocery segment while in the meantime, defend themselves. Although Amazon is still the largest online retailer in the world, Walmart remained at the top with \$270 billion made in the grocery segment. To compete in the grocery segment, Amazon has purchased Whole Foods and introduced Amazon Fresh Delivery and Amazon Prime Now, which should be paid careful attention since the potential of creating a poor customer experience could erode the Amazon brand. However, Amazon could invest more to compete with Walmart in the grocery market, since Whole Foods owns a more affluent customer base. Amazon could create a private label brand that is only available online but offers low-cost products. This private label brand is a fighting brand for Amazon, and it allows Amazon to compete with Walmart in the grocery segment. Furthermore, this fighting brand for the grocery market should also focus on the quality and consistency of its service while carefully protecting customer satisfaction.

The advantages of focusing on the flanker brand include allowing Amazon to more effectively expand its customer base in the grocery segment, the increase in the quality and consistency of Amazon Prime Now, higher customer satisfaction, and effectively attacking Walmart in the grocery segment. The drawbacks of using flanker strategy include the challenges in brand management and the significant investment in market research and advertising in order to more effectively target Amazon customers' expectations. In short-term, focusing on flanker strategy will allow Amazon to counterattack Walmart, whom is their most direct competitor. From the long-term view, Amazon might be able to maintain its loyal customers while attracting a considerable amount of Walmart's customers and pull market share away from Walmart.

## Market Potential Estimation – Chain Ratio Method

Walmart is still dominating in the grocery segment. Walmart owns a 23% market share in the grocery market, and it is 2.5 times the second largest retailer (Mahoney, 2019). Walmart also generate revenue in e-groceries, 17% of the customers indicate that they ordered from Walmart.com in 2018 (Mahoney, 2019). There are an average of 275 million customers and Walmart members visit Walmart's brick and mortar store as well as Walmart's e-commerce website every week (BENTONVILLE, 2019).

Assumption one:

Assume that Amazon launches its fighter brand with low cost offerings to compete with Walmart in the grocery segment in 2020. 20% of the Walmart's customers are attracted by and decided to shift to Amazon's new fighter brand because of the low-price deals. Hence, 55 million of Walmart customers or members will shift to Amazon's new fighting brand, calculated by  $275 \text{ million} \times 20\% = 55 \text{ million}$ .

Assumption two:

Safely assume that 15% of Walmart customers or Walmart members will be aware of this new brand that Amazon launches, then roughly 8.25 million of Walmart customers or members will shift to Amazon's new fighter brand if aware of the better deals for Amazon's fighting brand. (calculated by  $55 \text{ million} \times 0.15 = 8.25 \text{ million}$ )

Assumption three:

Assume that 40% of Walmart customers or members are motivated by Amazon's low-cost offering, then approximately 3.3 million of Walmart customers or members will shift to Amazon's fighter brand. (calculated by  $8.25 \times 0.4 = 3.3 \text{ million}$ )

Therefore, by the end of 2020, Amazon would gain approximately 3.3 million of Walmart's customers or members. As mentioned, Amazon Prime members spend an average of \$1,400 on the online shopping platform annually (Key, et al., 2019). If Amazon launched its fighting brand, then Amazon is likely to generate at least additional \$4.620 million in revenue by the end of 2020.

Similarly, the market potential estimation for the year 2021 is calculated as follow:

$271.7 \text{ million (Walmart customers or members)} \times 20\% \text{ (will shift to Amazon if aware)} \times 15\% \text{ (will shift to Amazon if they look for better deals through Amazon)} \times 40\% \text{ (estimate percentage of Walmart customers who look into better deals on Amazon)} = 3.26 \text{ million (numbers of Walmart customers or members who shift to Amazon's new)}$

fighter brand) By the end of the year 2021, Amazon is likely to generate at least \$4.564 million in revenue, calculated by  $\$1,400 \times 3.26 \text{ million} = \$4.564 \text{ million}$ .

As for the year 2022, the market potential estimation is as follow:

$268.44 \text{ million} \times 20\% \times 15\% \times 40\% = 3.22 \text{ million}$  (numbers of Walmart customers or members who shift to Amazon's new fighter brand) By the end of the year 2022, Amazon is likely to generate at least \$4.508 million in revenue, calculated by  $\$1,400 \times 3.22 \text{ million} = \$4.508 \text{ million}$ .

### Strategic Alternative 3

Amazon offers a series of online services with great variability. Therefore, being the largest online retailer in the world, the Position Defense Strategy seems to be optimal. Perhaps the most critical issue that Amazon is facing is the loss of uniqueness in the Amazon Prime value proposition since other competitors are offering similar services. In addition, the annual membership fee increased from \$99 to \$119 which has caused consumers to question the value of Amazon Prime. As a result, the retention of Amazon Prime users has become a critical issue for Amazon.

More investment could be made to execute Position Defense Strategy. For instance, increase switching costs for Amazon Prime users or introducing new loyalty programs might be optimal ways to retain current Amazon Prime users. In the short-term, utilizing Position Defense could potentially make Amazon more impregnable, considered the direct attack from large retailers, such as Walmart. From the long-term view, Amazon could not only maintain their current market share in the online market, but also drive engagement and conversion rate of Amazon Prime, if they add incentives periodically. Furthermore, Amazon should maintain its passion for innovation and commitment to the consumer in order to make the position defense strategy more effective.

Some advantages of using Position Defense include maintaining the existing customer base while adding in more benefits for Amazon Prime users to drive conversion rates. Nevertheless, some potential drawbacks of Position Defense include the significant rise in cost to maintain the number of current Prime users and the overwhelming challenge of taking care of every step of the customer's purchase journey to ensure a positive experience and avoid negative word of mouth.

### Market Potential Estimation – Chain Ratio Method

As mentioned in Strategic Alternative 1, until June 2019, there are approximately 105 million Amazon Prime users in the United States (Key, et al., 2019), and there are

currently 184.2 millions of Amazon customers in the United States. We could estimate that there are 79.2 million Amazon customers who are not Amazon Prime members.

Assumption one:

Assume that Amazon decided to emphasize on locking down its existing customer base by increasing switching cost and provide incentives through its new loyalty programs in 2020. Aside from the existing customers, there are 20% of the Amazon customers who are not Prime users attracted by the rewards that Amazon provides in its loyalty program. Hence, 15.84 million Amazon customers who are not Prime users will subscribe to Amazon Prime if aware, calculated by  $79.2 \text{ million} \times 20\% = 15.84 \text{ million}$ .

Assumption two:

Safely assume that 15% of Amazon customers will be aware of the new incentives offered by Amazon for its loyalty program, then roughly 2.376 million of Amazon customers who are not Prime users will subscribe to Amazon Prime. (calculated by  $15.84 \text{ million} \times 0.15 = 2.376 \text{ million}$ )

Assumption three:

Safely assume that 45% of Amazon customers in the United States do look into the rewards offered in Amazon's loyalty programs, then approximately 1.07 million of Amazon customers who are not Prime users will subscribe to Amazon Prime. (calculated by  $2.376 \times 0.45 = 1.07 \text{ million}$ )

Therefore, by the end of 2020, Amazon would be able to have at least approximately 1.07 million new Prime members. In other words, Amazon is likely to generate at least \$1.498 million in revenue, calculated by  $\$1,400 \times 1.07 \text{ million} = \$1.498 \text{ million}$ .

Similarly, the market potential estimation for the year 2021 is calculated as follow:

$78.13 \text{ million} \times 20\% \times 15\% \times 45\% = 1.05 \text{ million}$  (numbers of new Prime members in the year 2021) Amazon is likely to generate at least \$1.470 million in revenue by the end of the year 2021, calculated by  $\$1,400 \times 1.05 \text{ million} = \$1.470 \text{ million}$ .

The market potential estimation for the year 2022 is as follow:

$77.08 \text{ million} \times 20\% \times 15\% \times 45\% = 1.04 \text{ million}$  (numbers of new Prime members in the year 2022) Similarly, Amazon is likely to generate at least \$1.456 million in revenue by the end of the year 2022, calculated by  $\$1,400 \times 1.04 \text{ million} = \$1.456 \text{ million}$ .

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