

Amazon's influence

Wait and see may no longer be an option

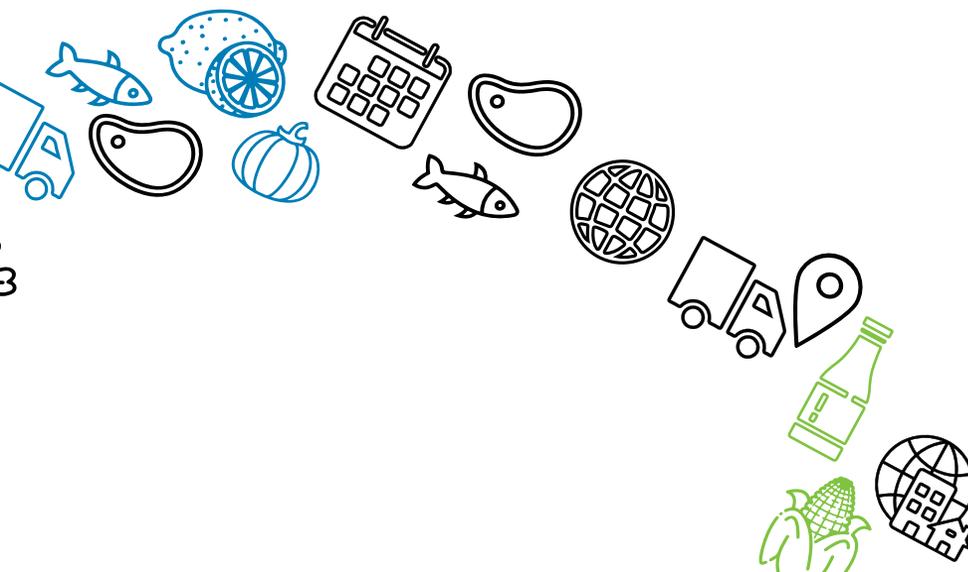


The Amazon-Whole Foods acquisition is a wake-up call for retailers who've downplayed the impact of Amazon's past strategic moves. It's time to face facts: Jeff Bezos has disrupted the retail landscape (again). Business leaders need to accept the competitive realities of a combined Amazon-Whole Foods business and respond with bold, strategic moves of their own.

Amazon's \$13.7 billion purchase of Whole Foods, a grocery chain with more than 450 retail stores and extensive domain expertise, has elicited a range of reactions from various retail players and their investors. Not surprisingly, Amazon's stock price rose on this news while that of grocery retailers such as Kroger's, Ahold Delhaize (parent company of Food Lion and Giant supermarkets), Sprouts Farmers Market, Supervalu, and Costco all declined.¹ An estimated \$22 billion of share value just disappeared from grocery-related stocks in one day based on the knowledge of how a combined Amazon-Whole Foods go-to-market play might disrupt traditional grocery performance measures—and the performance measures of other retailers as well.²

Heated debates are underway around boardroom tables in many conference rooms. Will brick and mortar retail eventually give way to a click-and-mortar business model?³ Will every retailer eventually evolve into a click-only presence? What does Amazon's expansion into both physical stores and new retail categories mean for my business, and how best should we prepare to defend our market share and brand?

Perhaps it is time for retailers to confront the competitive challenges presented by Amazon head-on rather than submit to the five stages of grief.⁴



In hindsight, we know that the competitive reactions to Amazon have typically proven to be ineffective. Reactions such as:

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Skepticism on financial performance
It's not fair . . . Wall Street doesn't pressure them.
- 

Refusal to acknowledge competition
Amazon is really a technology company, not a retailer.
- 

E-commerce imitation
We will launch a website to drive channel sales.
- 

Delivery denial
Their value chain won't support rapid delivery.
- 

Defensiveness on Amazon's delivery expansion
My category is different . . . they don't understand.
- 

Defiance on subscription loyalty programs
Customers are unwilling to subscribe for free shipping.

Six impending competitive realities for retailers



Reality #1: Amazon storefronts are the new normal for many grocery retailers

Entering the grocery category presented Amazon with a large opportunity to buy into a physical store presence—the reverse of Walmart's acquisition of Jet.com for its e-commerce expertise. In acquiring Whole Foods, Amazon captures a highly prized urban footprint located in one of mass market retailers' remaining areas of growth.

Not only has Amazon gained storefronts, it has added 11 food storage centers to its expanding network of 450-plus distribution centers to support expansion of its services.⁵



Reality #2: Amazon is anticipated to grow its share of wallet from its Prime and Whole Foods customer bases

At its core, Amazon is a customer-centric company, constantly evolving and testing all aspects of its operations in pursuit of fulfilling its customers' desires. Knowing how to organize and operate around how its customers wish to interact—and essentially innovating from the outside in⁶—has been a key component in Amazon's success.

This acquisition is no different. They are now able to provide a missing category of product to customers, thus increasing an already large annual spend.⁷ Adding fuel to this contest, there is an existing strategic overlap between Amazon Prime and Whole Foods consumer demographics.⁸ With an overlapping customer base, Amazon will likely expand into a new category from a position of strength. For competitors, retaining or attempting to capture new market share from these customers may prove challenging.

However, it should be acknowledged that both Amazon Prime and Whole Foods customers have higher incomes.⁹ The question is, could reality #3 shift this?



Reality #3: Operational competitiveness is only likely to ramp up

Gaining access to Whole Foods' network of food suppliers and distributors is expected by many to increase Amazon's influence in vendor negotiations by pushing competitors' profit margins down. Amazon's power to negotiate ever-lower prices with suppliers means food deflation¹⁰ pressures are likely primed to negatively impact profit margins for competitors while still benefiting consumers.¹¹ Keeping prices low will likely only strengthen loyalty by Prime members.

Although many grocery chains continue to invest heavily in technology, the reality is that playing catch-up with an e-commerce giant is typically a never-ending story without a happy ending. When it comes to competing on operational performance, such as consumers' preferences for "buy online, pick up in store" (BOPIS), "buy online, return in store" (BORIS), and other mass fulfillment initiatives,¹² Amazon's delivery platform already surpasses many retailers.



Reality #4: Acquiring grocery may not be the end

To continue its growth trajectory, Amazon is likely to enter categories that up to this point have been relatively immune to its influence. Amazon has been beta testing services in the following areas:

- Home improvement services¹³
- B2B and DIY food kits

Amazon recently filed a trademark for meal kits: “We do the prep. You be the chef.”¹⁴ Separately, but worth noting: Amazon is now delivering same-day meal kits by Martha & Marley Spoon,¹⁵ a partnership with Martha Stewart. The kits can be ordered with an Amazon Fresh membership and do not require individual subscriptions. Publisher Vice Media recently entered this hyper-competitive meal kit business model as well.¹⁶ Among other supermarket chains selling meal kits are Giant Eagle, Coborn's To the Table fresh meal kits, and Whole Foods, which has begun selling Purple Carrot meal kits, as reported by *Progressive Grocer*.¹⁷

Even highly regulated markets such as liquor or chemicals could be considered potential targets for Amazon's merger and acquisition aspirations. For many retailers and distributors, the question is not if Amazon will become a direct competitor, but *when*—and how should we proactively prepare?



Reality #5: Retailers may leverage Amazon for advantage

CNBC estimates that Amazon accounted for 53 percent of US e-commerce growth in 2016.¹⁸ Leveraging Amazon's marketplace platform as a 3P vendor¹⁹ in addition to its nascent physical store presence may prove quite lucrative for retailers desiring to provide consumers with an easily accessible omnichannel experience day or night. The power of Amazon's extensive consumer purchase history, combined with shopper analytics and advertising revenue, is apt to be an equally compelling reason for retailers to contemplate a partnership that would likely extend their reach and share of consumer wallet.



Reality #6: Waiting may no longer be an option

Even businesses not significantly impacted by this acquisition should seriously consider planning ahead as tepid responses may not be enough to ensure longevity. While we encourage retailers to consider both defensive and partnering strategies with Amazon, navigating toward the success of true north²⁰ likely need not be a solo journey.

Instead of trying to compete on individual effort, technological investments, acquisitions, and isolated operational improvements, retailers should consider calculating the benefits of joining or forming an ecosystem of complementary partners with expertise in delivery, social media, digital payments, e-commerce, and distribution platforms. The goal could be to create a virtual, transaction-based dream team of superheroes that can be dedicated to surviving and thriving where no retailer has gone before.²¹

Next steps for retail?

Consider focusing on strategic responses by recasting the value proposition and operating model to holistically address and deliver on the implicit as well as explicit desires of the customer. Consider that these responses are often disruptive in nature and may require time to remodel how the customer's influence should evolve within the scope of an ecosystem. For example, strategic responses should strive to be customer-centric, so consider focusing on how the behavioral dynamics of consumers may shift for each category rather than on how the customer interacts with the brand in question. Recalibration of certain business levers may include:

- Customer behavior analysis
- Value proposition recalibration
- Operational model redesign

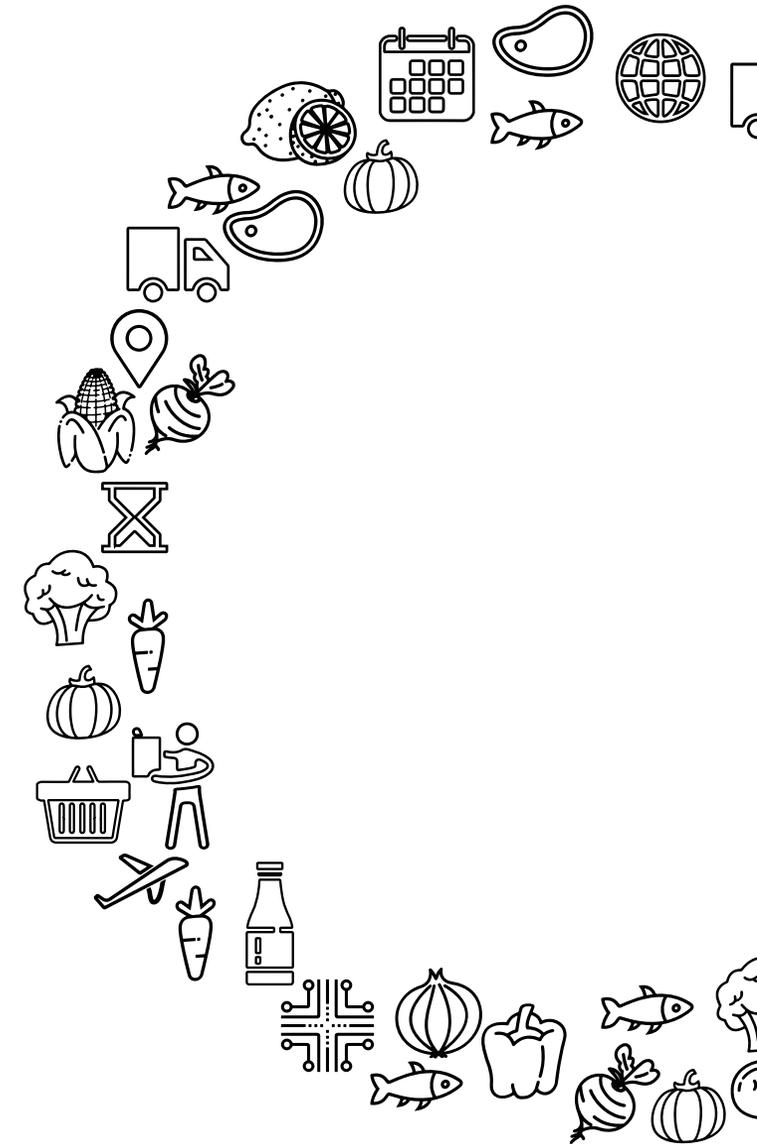
Strengthening tactical operations to better fortify strengths and competitiveness through operational responses may also yield benefits. For example, operational responses should focus on capability creation and incremental improvements that resolve gaps in consumer demands or improve the retailer's ability to deliver. Easier to define with explicit execution and market activation plans, operational responses often encompass:

- Services expansion
- Center-store optimization
- Store space rationalization



Endnotes

- ¹ "Grocery stocks are getting clobbered after Amazon-Whole Foods deal," June 16, 2017: 4:17 PM ET, <http://money.cnn.com/2017/06/16/investing/walmart-target-stocks-plunge-whole-foods-amazon/index.html>.
- ² "Grocery stocks are getting clobbered after Amazon-Whole Foods deal."
- ³ Click and mortar is a type of business model that includes both online and offline operations, which typically include a website and a physical store.
- ⁴ Elisabeth Kübler-Ross, © 1969, *On Death and Dying*. The five stages—denial, anger, bargaining, depression, and acceptance are a part of the framework developed by Kübler-Ross.
- ⁵ "Amazon Will Likely Cut Warehouse Jobs First at Whole Foods," © 2017, <http://www.grubstreet.com/2017/06/amazon-will-cut-whole-foods-warehouse-jobs-first.html>.
- ⁶ *Outside In: The Power of Putting Customers at the Center of Your Business*, © 2012 Harley Manning, Kerry Bodine, Josh Bernoff, Brilliance Audio, Inc.
- ⁷ "How Much the Average Amazon Prime and Non-prime Member Spends Each Year," ©2017, Fox Business News. <http://www.foxbusiness.com/markets/2017/04/29/how-much-average-amazon-prime-and-non-prime-member-spends-each-year.html>.
- ⁸ "Amazon's Whole Foods Strategy: It's Not What You Think," *Forbes, Inc.*, June 23, 2017.
- ⁹ "Amazon Has Upper-Income Americans Wrapped Around Its Finger," ©2016 *Time Inc.* All rights reserved. http://infoscout.co/retailer/whole_foods; <http://time.com/money/4294131/amazon-prime-rich-american-members>.
- ¹⁰ "Food deflation good for consumers, but pinching grocers," CNBC, August 2016.
- ¹¹ "Food Price Deflation Cheers Consumers, Hurts Farmers, Grocers and Restaurants," Heather Haddon and Julie Jargon, *Wall Street Journal*, August 2016.
- ¹² Buy Online Return In Store (BORIS) and Buy Online Pickup In Store (BOPIS): The Two Acronyms All Small Businesses Should Know, © 2015, *Inc. Magazine*.
- ¹³ Amazon.com: Contracting - Home Improvement: Home & Business, <https://www.amazon.com/Contracting-Services/b?ie=UTF8&node=11525237011>.
- ¹⁴ "Amazon files meal-kits trademark, treading on Blue Apron's turf," © 2017 CNBC.
- ¹⁵ Martha & Marley Spoon.
- ¹⁶ "Vice Media Enters the Hyper-Competitive Meal-Kit Business. The publisher, which was on track to do \$850 million in revenue last year, aims to generate more cash with food on-demand," © 2017 *Inc. Magazine*.
- ¹⁷ "Kroger's Meal Kits Could Make A Meal of The Industry", *Forbes, Inc.*, May 2017.
- ¹⁸ "Amazon captured more than half of all US online sales growth last year, new data shows," © 2017 CNBC.
- ¹⁹ Sell third-party to consumers through the Amazon marketplace, using the Seller Central interface (whether the brand sets up its own 3P seller account, or works with partner 3P sellers focused on the brand), © Jan. 25, 2016.
- ²⁰ *Leadership Intelligence: Navigating to Your True North*, Wanda Maulding Green, Rowman & Littlefield Publishers, © 2016.
- ²¹ Mission of the starship Enterprise. Space: the final frontier. These are the voyages of the starship Enterprise. Its five-year mission: to explore strange new worlds, to seek out new life and new civilizations, to boldly go where no man has gone before.



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