



Mike Beckham @mikebeckhamsm Sun Jan 16 20:29:40 +0000 2022

Our brand sells millions of units through Amazon each year. Contrary to public sentiment, they've been a great partner to our business.

But 2022 is a major crossroads because Amazon retail will likely shrink this year

My thoughts on what's wrong and how to fix it (1 of many)

First, Amazon's retail sales numbers from Q3 were only up 4% YOY over 2020.

It's easy to write that off as really difficult comps caused by COVID, but, our data says that Q4 was flat.

The bigger issue is that Q1 seems extremely sluggish YOY, but the worst comps are ahead...

March and April were amazing last year as a result of copious amounts of helicopter money being doled out by the government. I would expect these months are going to be big negatives for everyone YOY.

There's one more thing to keep an eye on with Amazon...

Their fulfillment costs per \$ of retail sales have skyrocketed.

Amazon has been very aggressive in rolling out programs like free tuition for warehouse employees. I love the way these initiatives impact working families, but they are going to cost Amazon significantly. <https://t.co/Wb8CkGswqo>

| | Q3 2020 | Q3 2021 | YOY |
|-----------------------------------|------------------|------------------|-------|
| Net Product Sales | \$52,774,000,000 | \$54,876,000,000 | 4.0% |
| Fulfilment | \$14,705,000,000 | \$18,498,000,000 | 25.8% |
| | | | |
| Fulfilment Per \$ of Sales | \$0.28 | \$0.34 | 21.0% |

Right now here's the e-commerce fulfillment landscape

- UPS and FedEx are raising prices
- Skyrocketing industrial real estate prices
- Intense competition for industrial employees

@ChadCarleton and others in the 3PL world are feeling all these things

The natural reaction for Amazon is going to be to charge higher fulfillment rates for its marketplace sellers and ask for higher margins from its wholesale vendors.

On the marketplace side, this will lead to higher prices. That's not going to help the revenue grow.

Also...

On the wholesale side, they will be negotiating with brands that have had shipping costs decimate their 2021 profitability.

These brands are not going to have much motivation to give Amazon better pricing. Especially when top-line sales on

Amazon are likely to decrease YOY.

In the midst of all this, Walmart and Target have stepped up their game considerably. There was a time when it seemed a foregone conclusion to many that Amazon would eventually cannibalize the brick and mortar giants. Over the coming months, we may see the opposite.

Since the beginning of Q4 2020, TGT is up 40% while Amazon and Walmart are flat. In addition to being a large partner of Amazon's, we have also been a major partner with Target. Internally, we've been really impressed with their execution over the past few years. <https://t.co/GeZhTO94Yk>



I think that the coming quarters are probably the most important (and potentially dangerous) ones that Amazon has faced in its history.

Among all these other challenges, they have an iconic founder who has stepped back from the business.

What should Amazon do?

My advice to Amazon leadership would be 2-fold

1. They are being out merchandised by Target and Walmart.
2. They have leaned too heavily on advertising to generate profit.

First, let's talk about why they are being out merchandised by physical retailers.

Historically, getting into a mass retailer required going through a buyer. Buyers serve as gatekeepers who decide what goes on shelves and negotiate prices.

This came with all the natural downsides of gatekeeping.

-It is less agile, so it is harder for physical retailers to be on the front end of new trends.

-It can rely too much on salesmanship and not enough on consumer preference

-It is hard for smaller companies to break-in

There's also the reality that in physical retail the shelf space is limited. [@zackkanter](#) does a great job of breaking down how the Amazon algorithm helped them to develop the "infinite shelf"

<https://t.co/USzEWf0xx6>

The Amazon ranking algorithm was a breakthrough that prioritized customer behavior over everything else.

The easiest way to know what customers want is that watch what they do. One of the things I like to say is, "People vote with their wallets."

Generally, I'm a huge fan of the Amazon algorithm. It played a big role in the launch and growth of our company.

Over time, 2 problems have emerged with the algorithm.

The first is that it is totally opaque. No one can tell you how the algorithm works. Amazon's army of data scientists is completely off-limits to everyone - even other departments within the company.

The second is that when you use an algorithm people will tirelessly work to game the system. [@Molson_Hart](#) [@ShinghiD](#) and others can share the countless black hat tactics that are used by sellers on Amazon to lift their listings and sabotage competitors.

Some prominent examples:

Leaving negative reviews on competitor listings

Upvoting legitimate negative reviews

Paying for good reviews on their products

Reporting false IP infringement

Bribing others to put competitors in incorrect categories (like adult toys or pesticides)

The way this has played out over time is that many categories have been taken over by Chinese marketplace sellers with nonsensical brand names that are just random letters strung together.

In addition, the review profiles on these items are mostly fake. They were bought.

To give you an idea of how endemic the abuse was, last year Amazon took down literally thousands of Chinese marketplace sellers in a huge review manipulation enforcement.

I'm here for it! But unfortunately, there is still plenty of incentive to game the system.

As sellers game the system, the user shopping experience degrades. They see worse merchandising options and become more likely to just browse the few known options the next time they are at Wal-Mart or Target.

There's one other merchandising piece here worth mentioning: safety

Anytime a product is sold in physical mass retail it has to go through a rigorous testing process. This doesn't happen with most Amazon marketplace products.

Safety is one area where gatekeepers can be really helpful.

Merchandising matters. Target's success is due in large part to its outstanding merchandising. I think Amazon has reached the point where it needs to layer on more curation to compete.

The other major dysfunction going on with Amazon right now is an overdependence on advertising revenue on its platform. Nothing has fueled the spectacular rise in Amazon's profits like the increases in insanely high margin advertising revenue.

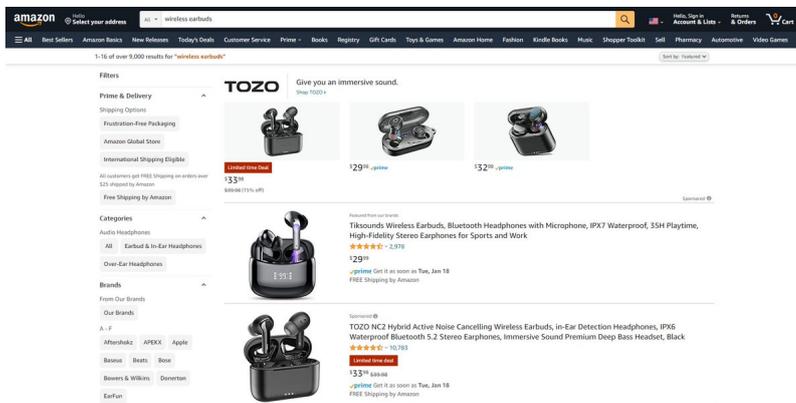
Amazon's ad revenue went from \$9.3 billion in 2020 to \$21.5 billion in 2021. We know that sales were flat a lot during that period - so how did they accomplish that growth?

By cramming more sponsored links on each page.

Here's the problem with that...

Even if you set aside the problems with the algorithm, every time Amazon crams another sponsored link on the page it cannibalizes an organic result from the algorithm. This leads to even less relevant search results.

In many search results, you won't even see a non-ad result above the fold. Here are the results for "wireless earbuds"
<https://t.co/D1qTFpG7R1>



Marketing is trading people's time and attention for money, but that's not supposed to be Amazon's core value proposition.

It is supposed to be saving me time, adding convenience, and helping me find the best product. We are seeing the results of misaligned incentives.

I'm a huge fan of Amazon and owe so much to [@JeffBezos](#) and the Amazon team. Selling on its platform has literally changed my life.

I once wrote a letter to Jeff [@amazon.com](mailto:amazon.com) telling him how much my family and my company had benefited as a result of what he had built.

I'm hopeful that over the years to come they can fix some of the areas of their product that are holding them back from truly being the most customer-centric company on the planet.

/end

A couple of clarifications I would like to make since this is blowing up

1. Amazon's gross merchandise value sold will definitely increase this year. Their revenue from selling merchandise (1p+3p) could be flat or decline.
2. My main point is that the Amazon shopping experience has qualitatively declined during a critical juncture. I think that makes them more vulnerable to competition.