



AMAZON.COM Expanding Beyond Books

Jeff Bezos, the CEO of Amazon.com, was pleased that his three year-old online start-up, www.amazon.com, had gone from being an underground sensation for book-lovers on the World Wide Web (WWW) to one of the most admired Internet retailers on Wall Street. To date, his attempts to transform the traditional book-retailing format through technology that taps the interactive nature of the Internet has been very successful. Although his company garnered rave reviews from respected Wall Street Analysts, Bezos clearly understood that this was not the moment to dwell on the past. In the fast moving world of the Internet, he and his firm continued to face many formidable challenges.

This case describes how Bezos has managed to build a rapidly growing retail business on the Internet and the challenges he and his top management currently face as other industry giants such as Barnes & Noble, and Bertelsman, the German Publishing Conglomerate, attempt to imitate his model of competition.

COMPANY BACKGROUND

In 1994, Jeffrey Bezos, a computer science and electrical-engineering graduate from Princeton University, was the youngest senior vice-president in the history of D.E. Shaw, a Wall Street-based investment bank. During the summer of 1994, one important statistic about the Internet caught his attention, and imagination—Internet usage was growing at 2300 percent a year. His reaction: “Anything that’s growing that fast is going to be ubiquitous very quickly. It was my wake-up call.”

He left his job at D.E. Shaw and drew up a list of 20 possible products that could be sold on the Internet. He quickly narrowed his prospects to music and books. Both shared a potential advantage for online sale: far too many titles for a single store to stock. He chose books.

There are so many of them! There are 1.5 million English-language books in print, 3 million books in all languages worldwide. This volume defined the opportunity. Consumers keep demonstrating that they value authoritative selection. The biggest phenomenon in retailing is the big-format store—the “category killer”—whether it’s selling books, toys, or music. But the largest physical bookstore in the world has only 175,000 titles. ... With some 4,200 US publishers and the two biggest booksellers, Barnes & Noble and Borders Group Inc., accounting for less than 12% of total sales, there aren’t any 800-pound gorillas in book selling.¹

This case was prepared by Associate Professor Suresh Kotha, University of Washington Business School, as the basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation. Copyright © 1998 Kotha. All rights reserved.

¹ “Who’s writing the book on web business?” *Fast Company*, October-November, 1996, p. 132-133.

In contrast, the music industry had only six major record companies that controlled the distribution of records and CDs sold in the United States. With such control, these firms had the potential to lock out a new business threatening the traditional record store format.

To start his new venture, Bezos left New York City to move West, either to Boulder, Seattle, or Portland. As he drove west, he refined and fine-tuned his thoughts as well as his business plan. In doing so, he concluded that Seattle was his final destination. Recalls Bezos:

It sounds counterintuitive, but physical location is very important for the success of a virtual business. We could have started Amazon.com anywhere. We chose Seattle because it met a rigorous set of criteria. It had to be a place with lots of technical talent. It had to be near a place with large numbers of books. It had to be a nice place to live—great people won't work in places they don't want to live. Finally, it had to be in a small state. In the mail-order business, you have to charge sales tax to customers who live in any state where you have a business presence. It made no sense for us to be in California or New York. ... Obviously Seattle has a great programming culture. And it's close to Roseburg, Oregon, which has one of the biggest book warehouses in the world.²

Renting a house in Bellevue, a Seattle suburb, Bezos started working out of his garage. Ironically, he held meetings with prospective employees and suppliers at a nearby Barnes & Noble superstore. Bezos also raised several million dollars from private investors. Operating from a 400-square-foot office in Bellevue, he launched his venture, Amazon.com, on the Internet in July 1995.

As word about his new venture spread quickly across the Internet, sales picked up rapidly. Six weeks after opening, Bezos moved his new firm to a 2,000-square-foot warehouse. Six months later, he moved once again, this time to a 17,000-square-foot building in an industrial neighborhood in Seattle. To fund further expansion, Bezos attracted \$8 million from Kleiner, Perkins, Caufield & Byers, a venture-capital firm based in the Silicon Valley that has funded firms such as Sun Microsystems and Netscape.

By the end of 1996, his firm was one of the most successful Web retailers, with revenues reaching \$15.6 million. (Revenues for a large Barnes & Noble superstore amount to about \$5 million on average per year.) With revenues surging quarter after quarter, Bezos decided to take his company public. However, just days before the firm's initial public offering (IPO) of three million shares, Barnes & Noble—the nation's largest book retailer—launched its online store and sued Amazon.com for claiming to be the world's largest bookstore. To entice customers to visit its web store, Barnes & Noble offered deeper discounts. Bezos retaliated with a counter lawsuit of his own.³

On May 14, 1997, Bezos took Amazon.com public. *The Wall Street Journal* noted that: "Amazon's May 1997 debut on the Nasdaq Stock Market came with no small amount of hype. On the first day of trading, investors bid the price of shares up to \$23.50 from their offering price of \$18. But the shares then fell, and within three weeks of the IPO they were below their offering price."

Despite this, customers have continued to flock to Amazon.com's web site. By October 1997 Amazon.com served its millionth "unique" customer. To keep pace with such growth, the firm expanded its Seattle warehouse and built a second 200,000-square-foot state-of-the-art

² *Fast Company*, October-November, 1996.

³ In October 1997, Barnes & Noble and Amazon.com settled their respective lawsuits by saying that they would prefer to get back to business and compete in the marketplace rather than in the courtroom.

distribution center in New Castle, Delaware. With these additions Amazon.com successfully increased its stocking and shipping capabilities to nearly six times its 1996 levels.

As the firm continued to expand its customer base, sales revenues have surged. The firm's revenues increased from \$15.7 million in 1996 to \$147 million in 1997 (see **Exhibit 1** for firm's income statement and balance sheet). Sales are now on pace to top \$550 million for fiscal 1998. In response to this revenue growth, the company's stock and market capitalization have proceeded to rise as well. As of July 1998, the company's capitalization was around \$6.4 billion, a number that represents the combined value of the nation's two largest retailers, Barnes & Noble and Borders Books & Music, whose combined sales are about 10 times that of Amazon.com's.

THE BOOK PUBLISHING INDUSTRY

The United States is the world's largest market for books, with retail book sales accounting for \$20.76 billion in 1997. With over 2,500 publishers in the US, the book publishing industry is one of the oldest and most fragmented industries.⁴ **Exhibit 2** shows the structure of the US publishing industry.

Publishers. Publishers sell books on a consignment basis and assume all the risk in this industry. They also accept returns on unsold books, thus guaranteeing their distributors a 100 percent refund on all unsold books. They provide money and contracts to prospective authors and decide how many copies of a book to print. Typically a "first-run" print for a book varies from 5,000 to 50,000 copies. However, best-selling authors' first-run prints are generally set at around 300,000 copies.

In practice, however, trade (adult and juvenile books) and paperback publishers print far more copies than will be sold. About 25 percent of all books distributed to wholesalers are returned and at times these percentages run as high as 40 percent for mass-market paperbacks. According to industry experts, 20-30 percent for hardcover book returns is considered acceptable and 30-50 percent is generally considered high. Anything above 50 percent is considered disastrous. In a process known as "remaindering" (offering books to discount stores, jobbers, and other vendors) publishers drastically reduce the price after a certain period. Apart from the material cost of returns and the lost revenue they represent, publishers spend millions of dollars each year transporting books back and forth. In this industry profit margins are driven by book volume, which in turn hinge on the size of each print run. Generally about 10 percent of titles make a profit, with 90 percent barely breaking even. **Exhibit 3** illustrates the margins on a typical hardcover book.

The "big three"—Warner Books, Simon & Schuster and Pearson—accounted for 21 percent of sales in 1995. The 20 largest book-publishing companies in the US command over 60 percent of all retail sales. Warner Books, a subsidiary of Time Warner, the United States entertainment giant, was the largest publisher, with sales of \$3.7 billion in 1995. Simon & Schuster, a division of Viacom Corporation, ranked second with sales reaching \$2.17 billion, and Pearson, a group that owns the *Financial Times*, ranked third with revenues of \$1.75 billion.

Wholesalers. Wholesalers distribute books. They take orders from independent booksellers and chains, and consolidate them into lot-orders for publishers. Publishers supply wholesalers who in turn supply the thousands of retail bookstores located throughout the United States. Wholesalers

⁴ Much of the information discussed in this section, and the section that follows, is drawn from *Amazon.com*, a Washington University Business School Case, by Suresh Kotha and Emer Dooley, 1997.

accounted for almost 30 percent of publishers' sales in 1996. Unlike publishing and retailing, wholesalers are highly concentrated, with firms like Ingram Book Co., and Baker and Taylor commanding over 80 percent of the market.

Competition in wholesaling revolves around the speed of delivery and the number of titles stocked. Ingram, for instance, receives more than 70 percent of its orders electronically and offers one-day delivery to about 82 percent of its US customers. In 1994 the average net profit per book for wholesalers was less than 1.5 percent. This figure was down from the traditional margins of about 2 percent a few years earlier.⁵

Technological advances have made warehouse operations more efficient which in turn has made it possible for wholesalers to provide attractive discounts to retailers. Also, the types of books wholesalers are supplying to retailers are changing. Bookstores are increasingly relying on wholesalers for fast-selling titles and less-popular backlist books.⁶ However, with the emergence of superstores, such large retailers as Barnes & Noble, and Borders Books & Music are no longer using wholesalers for initial orders of major titles. For example, Borders Books & Music currently buys over 90 percent of its titles directly from publishers.

Retail Bookstores. Retail bookstores, independents and general retailers accounted for between 35-40 percent of industry revenues (see **Exhibit 4**). From 1975 to 1995, the number of bookstores in the United States increased from 11,990 to 17,340. According to industry sources, the total sales for the nation's four largest bookstore chains—Barnes & Noble, Borders Books & Music, Books-A-Million, and Crown Books—rose 14.3 percent to \$5.68 billion for the fiscal year ended January 1998. This figure represented about 24 percent of all book sales (see **Exhibit 5**). Industry analysts point out that from 1992 through 1995, superstore bookstore sales grew at a compounded rate of 71 percent while non-superstore sales grew at a rate of 4 percent.

With the increasing growth of these superstores, experts cautioned that in smaller markets a shakeout was inevitable.⁷ Also, 1995 marked the first year in which bookstore chains sold more books than independents (see **Exhibit 6**).⁸ A spokesperson for the *American Booksellers Association*, noted:

In the three years from 1993 to 1995, 150 to 200 independent-owned bookstores went out of business—50 to 60 in 1996 alone. ... By contrast in the same period, approximately 450 retail superstore outlets opened, led by Barnes & Noble and the Borders Group, with 348 openings.⁹

Independent booksellers believed the growth of superstores might be reaching a saturation point. But even as Barnes & Noble and Borders entered city after city, as many as 142 US metropolitan

⁵ *Publishers Weekly*, January 1, 1996.

⁶ Although the best-selling books get the bulk of the attention and marketing dollars, "backlist" books are considered the "bread and butter" of the industry. A backlist is the publishing company's catalog of books that have already appeared in print. Estimates indicated that as much as 25 to 30 percent of a publisher's revenues come from this source. Backlisted books have predictable sales with occasional bumps, such as when a subject matter loses favor with consumers or when an author dies. Since these books require no editing and little promotion, they are generally profitable. Moreover, print runs are easier to predict, resulting in fewer returns to publishers.

⁷ *Publishers Weekly*, March 11, 1996. Superstores, originally confined to big metropolitan areas, were increasingly entering markets with populations of 150,000 or less. Industry estimates indicated that superstores had to make around \$200 a square foot to turn a profit. For example, a typical Barnes & Noble superstore needed \$3 to \$4 million in sales revenues to break even. Some industry observers questioned whether such cities can support these mammoth stores and whether superstores in these locations could sell enough books to turn a profit.

⁸ *Philadelphia Business Journal*, September 27, 1996.

⁹ "A Nonchain Bookstore Bucks the Tide." *The New York Times*, September 8, 1996.

markets still did not have a book superstore. According to Amy Ryan, a Prudential Securities analyst, the current rate of expansion could continue at least through the year 2000. This is because the United States could support about 1,500 such stores.

Institutions and Libraries. There are more than 29,000 private, public and academic libraries in the United States.¹⁰ This market is crucial to publishers because of its stability and size. Since libraries order only what they want, this lowers the overhead costs associated with inventory and return processing, making this segment a relatively profitable one for publishers. Moreover, as hardcover trade books have become relatively expensive, many readers now borrow them from libraries rather than purchase them outright. Industry experts observed that about 95 percent of general titles published in any year sold less than 20,000 copies; of that amount, about 55 percent were purchased by libraries. Libraries also frequently repurchase titles to replace worn-out and stolen books. By doing so, they keep the “backlist” sales healthy.

Mail Order and Book Clubs. The industry is witnessing a significant drop in the mail order book business. This drop in sales was attributed to the growth of large discount-sale retailers. Publishers’ book club sales on the other hand have risen steadily, gaining 9 percent in 1994 and in early 1995. This growth was attributed to the increasing popularity of specialized book clubs that focus on favorite baby-boomer interests such as gardening and computers.

The industry sells a variety of books that include trade, professional, mass market, El Hi (Elementary-high school) and college-text books, and others, and each of these categories varied in terms of sales, competition, profitability, and volatility (see **Exhibits 7 and 8**).

A survey commissioned by American Booksellers Association found that some 106 million adults purchased about 456.9 million books in any given quarter. The survey, which looked at book-buying habits of consumers during the calendar year 1994, revealed that six in 10 American adults say they purchased at least one book in the last three months. Annually that corresponds to 1.8 billion books sold, an average of 17 books per book-buying consumer a year. The average amount paid for the three most recent books purchased by consumers in the last 30 days was about \$15. According to another report by *Book Industry Study Group*, “1996 was a year of major transition and flux in the publishing industry with buyer and seller alike reexamining standard operating procedures to work together in order to adapt to recent changes including growth of retail space and the impact of the Internet.”

The Growing Presence of “Virtual” Bookstores

The two hardest challenges for book selling—physically distributing the right number of books to bookstores and getting the word about serious books out to potential readers—are getting a more than trivial assist from the new online technologies. The rapid growth of the online businesses is spreading to book publishing and retailing. According to Larry Daniels, director of information technologies for the National Association of College Stores:

Booksellers' concern revolves around the potential for publishers to deal directly with consumers and the media on the Internet. ... The phenomenon could mean the elimination of middlemen such as bookstores.¹¹

Moreover, Daniels notes that there is also the potential for publishers to be “disintermediated,” because computer-literate writers can now publish and distribute their own works online.

¹⁰ *Standard and Poors Industry Surveys*, July 20, 1995.

¹¹ *The Christian Science Monitor*, September 18, 1996.

However, the leading publishing houses are skeptical of electronic book-publishing capabilities and remain uncertain about the Internet's future with regard to physical books.

Despite industry skepticism and concern, a plethora of "virtual" bookstores are now selling books on the Internet. A cursory search on an Internet search-engine such as Yahoo! produced a listing of 475 online bookstores operating on the web (as of August, 1998). A search on Buyers Index (www.buyersindex.com), a mail order buyers' search engine, lists over 234 online bookstores. Many of these firms are relatively unknown compared to such online retailers as Amazon.com and Barnes & Noble. These two firms in particular have been growing at the self-reported double-digit rates and are fast becoming a formidable presence on the web. Book and music sales online accounted for \$156 million in 1997. Although this amount represented a small percentage of the overall retail book sales in 1997, it is projected to reach about \$1.1 billion in 2001.

COMPETING ON THE WORLD-WIDE WEB

Operating a Virtual Bookstore

At Amazon.com, unlike traditional bookstores, there are no bookshelves to browse. All contact with the company is either through its web site [www.amazon.com] or by email. At the firm's web site, customers can search for a specific book, topic or author, or they can browse their way through a book catalog featuring numerous subjects. Visitors can also read book reviews from other customers, *The New York Times*, the *Atlantic Monthly*, and Amazon.com's staff. Customers can browse, fill up a virtual shopping basket, and then complete the sale by entering their credit card information or by placing their order online and then phoning in their credit card information. Customer orders are processed immediately. Books in stock (mostly bestsellers) are packaged and mailed the same day. When their order has been shipped, customers are notified by email. Amazon.com places orders for non-best sellers with the appropriate book publisher immediately.

Shunning the elaborate graphics that clutter many web sites on the Internet, the firm loads up its customers with information instead. For many featured books, it offers capsule descriptions, snippets of reviews and "self-administered" interviews posted by authors. The firm has found a way to use the technology to offer services that a traditional store or catalog can't match. Notes Bezos:

An Amazon customer can romp through a database of 1.1 million titles (five times the largest superstore's inventory), searching by subject or name. When you select a book, Amazon is programmed to flash other related titles you may also want to buy. If you tell Amazon about favorite authors and topics, it will send you by electronic mail a constant stream of recommendations. You want to know when a book comes out in paperback? Amazon will email that too.¹²

Additionally, the firm offers space for readers to post their own reviews and then steps out of the way and lets its customers sell to each other. Notes Bezos:

There are so many things we can do on-line that can't be done in the real world. We want customers who enter Amazon.com to indicate whether they want to be "visible" or "invisible." If they choose "visible," then when they're in the science fiction section, other people will know they're there. People can ask for recommendations— 'read any good books lately?'— or recommend books to others. I'm an outgoing person, but I'd never go into a bookstore and ask a complete stranger to recommend a book. The semi-anonymity of the on-line environment makes people less inhibited.¹³

¹² *The Wall Street Journal*, Thursday, May 16, 1996.

¹³ *Fast Company*, October-November, 1996.

Value Propositions and Customer Service

When asked why people come to their site, Bezos responds:

Bill Gates laid it out in a magazine interview. He said, "I buy all my books at Amazon.com because I'm busy and it's convenient. They have a big selection, and they've been reliable." Those are three of our four core value propositions: convenience, selection, service. The only one he left out is price: we are the broadest discounters in the world in any product category. ... These value propositions are interrelated, and they all relate to the Web.¹⁴

At Amazon.com almost all books are discounted. Bestsellers are sold at a 30 to 40 percent discount and the other books at a 10 percent discount. Point out Bezos:

We discount because we have a lower cost structure than physical stores do and we turn our inventory 150 times a year. That's like selling bread in a supermarket. Physical bookstores turn their inventory only 3 or 4 times a year.

The firm's Seattle and Delaware warehouses are used to stock popular books items, and to consolidate and repack customer orders. Moreover, only after the firm receives a paid customer order does it request the appropriate publisher to ship the book to Amazon.com. The firm then ships the book to the customer.¹⁵ The firm owns little expensive retail real estate and its operations are largely automated. Its distribution center in Delaware, for example, uses state-of-the-art technology to consolidate and package books for shipment.

To keep customers interested in Amazon.com, the firm offers two forms of email-based service to its registered customers. "Eyes" is a personal notification service, in which customers can register their interests in a particular author or topic. Once customers register with Amazon.com, they receive information about new books published by their favorite author. "Editor's service" provides editorial comments about featured books via email. Three full-time editors read book reviews, pore over customer orders, and survey current events to select the featured books. These, and other free-lance editors employed by the firm, provide registered users with email updates on the latest and greatest books they've been reading. These services are automated and are available free of charge and customers subscribing to these services have certain guaranteed rights (see **Exhibit 9** for "Customer Bill of Rights").

According to Bezos, such services are vital for success on the Internet:

Customer service is a critical success factor for online merchants. If you make customers unhappy in the physical world, they might each tell a few friends. If you make customers unhappy on the Internet, they can each tell thousands of friends with one message to a newsgroup. If you make them really happy, they can tell thousands of people about that. I want every customer to become an evangelist for us. About 63 percent of the book orders come from repeat customers.

¹⁴ *Fast Company*, October-November, 1996.

¹⁵ Industry observers note that although Amazon discounts most books, it levies a \$3 service charge per order, plus 95 cents per book. And it can take Amazon a week to deliver a book that isn't a bestseller, and even longer for the most esoteric titles. Also, some people don't like providing their credit card number over the Internet.

Additionally, the firm's employees compile a weekly list of the 20 most obscure titles on order, and Bezos awards a prize for the most amusing. Amazon.com drums up all these orders through a mix of state-of-the-art software and old-fashioned salesmanship. When asked to differentiate his firm from potential rivals, Bezos notes:

People who just scratch the surface of Amazon.com say — 'oh, you sell books on the Web' — don't understand how hard it is to actually be an electronic merchant. We're not just putting up a web site. We do 90% of our customer service by email rather than by telephone. ... There are very few off-the-shelf tools that help do what we're doing. We've had to develop lots of our own technologies. There are no companies selling software to manage email centers. So we had to develop our own tools. In a way this is good news. There are lots of barriers to entry.¹⁶

Culture and Philosophy

Amazon.com had 800 employees in August 1998. A significant portion of the firm's employees manage "content" on the firm's web site, including such tasks as Web page updating and formatting book reviews for display. The firm also employs a large number of people to develop software tools for operating on the Internet and a large group of employees do nothing but answer emails from customers. Notes Bezos:

Amazon.com is committed to ingenuity and problem-solving. Almost nothing is off-the-shelf at Amazon.com: Our software engineers are developing programs that are the first of their kind; our editors create original content; our site team designs features that can't be found anywhere else. . . . Also, we have some of the best programmers, and the best servers in the world.

According to Amazon.com insiders: "This is a very driven place. Hours are typically 8 to 8 and many people work weekends. Jeff spends every waking hour on this business." Adds Bezos:

Everyone at Amazon.com works hard, long, and smart. We act like owners because we are owners—stock options give each of us an equity stake in the company. We are passionate about what we're doing. Because of that, we have fun at work, and it makes it easy for us to work hard. What we're building is unprecedented. We're not aspiring to a corporate model—we are creating the model. This to me is the most compelling reason for people to come to work here.

Continues Bezos:

There is no Amazon.com "type." There are Amazon.com employees who have three master's degrees and some who speak five languages. We have people who worked at Procter & Gamble and Microsoft, and people who worked at Rolling Stone and The Village Voice. We have a professional figure skater, two racecar drivers, a Rhodes scholar, a set of twins, a husband and wife, and their dog. We wear jeans to work, have meetings in the hallway, and we get excited about HTML-enabled email.

Bezos describes his firm's corporate philosophy as follows:

The Amazon.com corporate philosophy is simple: If it's good for our customers, it's worth doing. Our company mission is to leverage technology and expertise to provide the best buying experience on the Internet. Put another way, we want people to come to Amazon.com, find whatever they want, discover things they didn't know they wanted, and leave feeling they have a new favorite place to shop.

¹⁶ *Fast Company*, October-November 1996.

Operating Philosophy

The firm's operating philosophy is unlike traditional bookstores. At Amazon.com there are no salespeople. The firm is open for business 24 hours a day and has a global presence. Over 3 million customers from 160 countries have purchased books from the firm. The firm is devoid of expensive furnishings, and money is spent sparingly. Notes Bezos:

We made the first four desks we have here ourselves—all our desks are made out of doors and four-by-fours. ... My monitor stand is a bunch of old phone books. We spend money on the things that matter to our customers and we don't spend money on anything else.¹⁷

Amazon.com spends a substantial amount on Web advertising and marketing. According to Jupiter Communications, the firm spent over \$340,000 for the first half of the 1996 and ranked 34th in Web ad spending. Since then, however, these expenses have gone up significantly. This is partly because Amazon.com has entered into multi-year advertising agreements with Internet aggregators, such as Yahoo!, Excite and AOL. For the most recent quarter ending June 1998, the firm spent \$26.5 million on marketing, equivalent to 23 percent of sales.

Since Amazon.com is an Internet-only retailer, Web advertising gives it a unique opportunity to track the success of an ad by the number of click-throughs to the store's web site and the number of Internet surfers who actually purchase something. Industry analysts estimate that between 2 percent and 3 percent of people who see an ad on the Web will actually click-through to see more.

The firm advertises mainly in such large-circulation news papers as *The Wall Street Journal*, *New York Times*, and *San Jose Mercury News*, and on Internet search-engine sites such as Yahoo!, Lycos, the Microsoft Network (MSN) and Microsoft's *Slate* magazine. Amazon.com keeps its banner ads simple, with just a few words and a Web address. Recently, the firm has started advertising on radio, and television (e.g., CNN). It also hands out discount coupons in several cities to entice customer to use its services.

The decision to locate Amazon.com in Seattle appears to be paying off. The firm has been able to attract some Microsoft veterans and many highly qualified executives. See **Exhibit 10** for an illustration of how the firm is organized and **Appendix A** for a brief description the firm's top management.

Growth via Micro-Franchising

The firm is currently growing at a rapid pace each quarter. Part of the reason for this rapid growth is the firm's Associates Program. The program was designed to increase traffic to Amazon.com by creating a referral service from other web sites to Amazon.com's 2.5-million book catalog. An associates web site, such as Starchefs — which features cookbook authors — recommends books and makes a link from its Web page to Amazon.com's catalog page for the books. The associated web site then earns referral fees for sales generated by these links. Partners receive weekly referral fee statements and a check for the referral fees earned in that quarter. More than 90,000 sites have already signed up under this program and earn a commission sometimes up to 15 percent of the value of books bought by the referred customer. Notes Bezos, "[The] Web technology has made it possible to set up micro-franchises, and with zero overhead."¹⁸

¹⁷ *Upside*, October 1996.

¹⁸ "Amazon.com forges new sales channel," *Web Week*, August 19, 1996.

Since July 1995 Amazon.com has doubled in size every 2.4 months.¹⁹ By August 1996, sales were growing at 34 percent a month. The firm posted revenues of \$147.8 million for 1997, an 838 percent increase over the previous year. However, the net loss for fiscal 1997 was 27.6 million, compared to a net loss in fiscal 1996 of \$5.8 million. When the company was founded in 1995, the plan was to be profitable in five years. The firm claims to have exceeded expectations and has made its business plan more aggressive. Despite continuing losses, Wall Street's interest in the new venture has remained strong. Further, based on cybershare (and revenues), the firm is currently acknowledged to be the largest online bookstore on the web.

Moreover, Bezos is focused on expanding Amazon.com: "In the year 2000, our goal is to be one of the world's leading bookstores." Adds Bezos:

We believe we're expanding the market for books. With this new way of selling books on the Web we can expose people to far more books than before. People buy books from us that they won't find in bookstores. And we're growing rapidly in this stagnant market.

CHALLENGES FACING AMAZON.COM

Although Bezos is pleased that Amazon.com is well regarded by analysts on Wall Street, he acknowledges that many strategic challenges remain. Particularly, a few important challenges demand his immediate attention. They include: finding creative ways to fend off formidable new competitors; leveraging the firm's brand name to expand beyond just books, and meaningfully integrating the new acquisitions made by the firm.

Fending off Formidable Competitors

Competition between online book merchants is likely to become even more intense, with a growing number of publishers and retailers going online. For example, Ingram and other large publishers have begun experimenting with the WWW. Notes *The Wall Street Journal*: "In addition to Amazon and Barnes & Noble, publisher Random House Inc. sells books online and Viacom Inc.'s Simon & Schuster unit launched an Internet book-selling site grandly called "The SuperStore."²⁰

Barnes & Noble, the largest US book retailer, launched its online store in May 1997, a little less than two years after Amazon.com opened for business. Although Barnes & Noble finds itself in the unusual position of trailing a competitor, it claims that it holds the unique distinction of operating in four different channels – retail stores, the Internet, 1-800-THE-BOOK and mail order. Notes Stephen Riggio, vice chairman of Barnes & Noble, who is presiding over the new online venture:

How big is it [online sales] going to get? We're looking at \$100 million in sales this year [1998]. We're not being speculative about that range. We're going to be there. It's going to be bigger than a billion dollar business.

Barnes & Noble online sales for the year ending in 1997 amounted to \$14 million, a small fraction of the firm's overall retail book sales. However, according to a report in *Business Week*, Leonard Riggio, CEO of Barnes & Noble, is dead serious about the online segment:

¹⁹ *Financial Times*, October 7, 1996.

²⁰ *The Wall Street Journal*, October 21, 1997.

Riggio plans to spend \$40 million to ballyhoo the service in 1998. ... Riggio is already thinking ahead of how to integrate this technology into the shelves of Barnes & Noble. In the bookstore of the future, he says, customers could tap into millions of titles and print any part from these works on the spot. He talks about software programs that could point customers to specific lines in various books, threaded by a single topic, or ones that could ferret out and print obscure texts that never made it into book form. In short, Riggio envisions modifying what constitutes a published work.²¹

In July 1998, Borders Group Inc. (the parent corporation of Borders Books & Music) entered the fray with Borders.com, a newly formed subsidiary. At the Border's web site customers can purchase books, music CDs, and videos. The firm's web site described Borders' late entry as follows:

We're not content with being just another online bookseller. We want to do it right. Anyone who's been to a Borders store knows that selling books, music, and videos isn't just a business, it's a passion. . . . At Borders.com, we aim to provide the same high level of expertise and vast selection customers have come to associate with the Borders name. No other online bookseller can offer 10 million books, CDs, and videos—in stock and available now.

In late 1997 Ingram, the largest US-distributor of books, began experimenting with online retailing. It began testing an experimental service to create new online retailers. Notes *Business Week*: "All the would-be retailers had to do was lure the shoppers. Ingram handled everything else, from maintaining the web site to taking orders, processing credit-card billings, and shipping the books. In effect the virtual bookshops became little more than a retail façade of Ingram. However, after six months of test-marketing, Ingram quietly pulled the plug in early October."²²

Undaunted by Ingram's failure, Bertelsman, the German media conglomerate, announced in February 1998 that it planned to open an online store (tentatively called BooksOnline) that will sell books in English, French, Spanish, German and Dutch.²³ Bertelsman hoped to ship books to customers in Europe and the United States through its extensive distribution in both countries. In October 1998, however, the firm announced it was buying a 50 percent share in Barnesandnoble.com for \$200 million and both Bertelsman and Barnes & Noble are expected to spend other \$100 million each to strengthen their joint operation. Further, Bertelsman will abandon the US rollout of its BooksOnline service. Observes Maria Latour-Kadison, an online retail analyst at *Forrester Research*:

This is a real powerhouse combination: the retail power of Barnes & Noble and the fulfillment power of Bertelsman. ... They already have what Amazon is spending millions to acquire [a brand name and infrastructure]. There's a very steep learning curve associated with doing online retailing well, and Bertelsman will be able to leapfrog some of it because of Barnesandnoble.com's experience.²⁴

²¹ The Baron of Books, *Business Week*, June 29, 1998.

²² The reason why Ingram's experimental foray into online retailing floundered was because many of the new online entrants were unable to attract enough customers. Notes *Business Week*, "Ingram stirred a backlash among its existing clientele, who were clearly not happy with the prospect of having to compete with other low-cost clones."

²³ Bertelsman AG the world's third-largest media conglomerate with \$14 Billion in sales in 1997. In July 1998, Bertelsman acquired US-based Random House Publishing. This single largest publisher of English language books owns Doubleday, Bantam Books, Dell Publishing and several other publishing companies.

²⁴ *Internet World*, October 12, 1998.

Acknowledges Bezos: "Bertelsman can be a formidable competitor. They have 50 percent stake in AOL's German operations, over 35 million active book and music club members and significant warehousing and book distribution assets spread out internationally." However, he notes:

We are not competitor focused but customer focused. Figuring out what the customer wants is a never ending process. We differentiate along the following dimensions: selection (we are still the largest); ease of use; price; and discovery. Scale is important in e-commerce and so is 'ease of use.' Our innovations like '1-Click shopping' continue to make our web site far more attractive than competitors. We are working with interesting features such as 'book matcher,' using the latest collaborative filtering technology that we acquired from Net Perceptions. We believe such things greatly enhance the customer experience at our store. Discovery means understanding customers as individuals and finding ways to accelerate their discovery process while they are at the store. We are working on software that increases the odds that customers will find the right book that they are looking for when searching in our store. Discovery is powerful for customers.

Bezos's immediate concern therefore revolves around finding innovative ways to stay ahead of his competitors and he acknowledges that this will remain a continuing challenge.

Leveraging the Amazon.com Brand Name

In June 1998, Amazon.com expanded its product line to include music. The music store offers more than 125,000 titles, 10 times the CD selection of the typical music store, and everyday savings of up to 40 percent. The new music store features expert and customer reviews, interviews, an essentials lists, a list of the hottest CDs from around the country and the world, music news, and recommendations. Music fans can search for their favorite music by CD title, artist, song title, or label. Bezos describes the new venture as follows:

You can browse through nearly 300 styles ranging from Alternative to Zydeco (everything but Classical, which is on the way) or use "Essentials" (my favorite feature) to learn about the best CDs to help you start or build a collection in a particular style. And you can reduce guesswork by listening to some of our 225,000 song clips. ... It's a music discovery machine. Using the power of technology and the Internet, we're enriching the music experience for everyone, from casual to devoted listeners alike.

More importantly, he adds:

The music store was designed with the help of more than 20,000 customers who responded to our invitation to "build the music store of your dreams." Many of the features in our new music store are the direct result of these suggestions. Our customers told us they wanted a site that is as rich in musical selection and content as the Amazon.com bookstore—with the same great prices, features, and customer service.

The launch of Amazon.com's music store was accompanied by a major update of the firm's web site. Bezos describes the changes thus:

We didn't focus only on music. We've also redesigned our store to make it even easier to find the books you want. . . . The new store design permits customers to move easily between the book and music areas, making it fast and simple to find what they are looking for and to discover new titles. We now provide an integrated shopping cart, 1-Click ordering, and consolidated shipping across both books and music.

Unlike book retailing, many online music stores such as cdnow.com (www.cdnow.com) and n2k.com (www.n2k.com) have been in operations for more than a few years. Cdnnow.com, for

example, claims it is the world's leading online music store by offering over 250,000 music related items. N2k.com operates many music sites (called channels) including Music Boulevard on the WWW (see **Exhibit 11** for a partial listing of online music stores). In response to Amazon.com's entry into the Music Business, Cdnw and N2K signed an agreement in October to merge their two companies.

Notes Bezos: "We don't really view existing online music stores as our direct competitors. We are more focused on parties that already have a large portion of music sales." Some analysts are, however, skeptical about whether Amazon.com should compete in music business. Notes a report in *The Wall Street Journal*:

But the move [to offer music CDs] is risky too; Cyberspace is increasingly crowded with on-line superstores set up by Amazon's physical-world counterparts, companies with more marketing clout and track records of profitability. And Amazon could lose cachet with bibliophiles if its forays into other media dilute its reputation as a destination for booklovers. ... [M]ail-order giants Columbia House, a joint venture of Time Warner Inc. and Sony Corp., and Berterlsmann AG's BMG Entertainment have made Internet selling a top priority. Columbia House is taking orders from music-club members on one site; on a separate super-store site, Total E, it's moving straight into Amazon territory with plans to add books and CD-ROMs to its existing catalogue of videos and CDs.²⁵

Some analysts point out that the music business is "somewhere between a no-margin and a low-margin business" and therefore question the firm's recent move. But notes Bezos:

Amazon.com brand has to stand for something. For us the brand name means price, convenience, customer service, and a great selection. There is a huge advantage in expanding to other product categories. The customer acquisition costs are significantly lower and so are the costs related to the life time value of that customer. If we can successfully expand the brand, as we think we can, then there are significant economic benefits to expansion. . . . We recognize that the music business is a different environment than books. About half-a-dozen players control the entire distribution of music in this country and the likely implication of such control is lower margins. However, we like to emphasize the incremental dollar value of music sales to our existing customers.

International Expansion and Acquisitions

Capitalizing on increased market value, Amazon.com acquired three companies, Bookpages Ltd, Telebook Inc., and Internet Movie Database Ltd in April 1998. Notes Bezos:

With these we have accelerated our expansion into European e-commerce and acquired a foundation for a best-of-breed video store. These acquisitions will enable Amazon.com to offer a new set of consumers the same combination of selection, service and value that we now provide our US book customers. Fortunately, we were able to build an international brand name as a by product of operating on the Internet. People in Japan, Germany, and UK are very familiar with the Amazon.com name (about 22 percent of the firm's sales come from outside the United States currently).

Although Bezos remains quiet about his intentions regarding Internet Music Database Ltd, analysts speculate that *The Internet Movie Database* is likely to form the key underpinning for Amazon.com's eventual entry into online video sales.

In July 1998, Amazon.com signed agreements to acquire two additional firms. They include Jungle Corp and PlanetAll. PlanetAll, is a Cambridge, Massachusetts firm that provides a unique

²⁵ In Looking to Branch Out, Amazon Goes Out on a Limb, *The Wall Street Journal*, May 12, 1998.

Web-based address book, calendar, and reminder service. Jungle Corp., based in Sunnyvale, Calif., is a leading provider of advanced Web-based virtual database (VDB) technology that can help shoppers find millions of products on the Internet (see **Exhibit 12**). Discussing his firm's intention to acquire these two firms Bezos noted:

PlanetAll is the most innovative use of the Internet I've seen. It's simply a breakthrough in doing something as fundamental and important as staying in touch. The reason PlanetAll has over 1.5 million members — and is growing even faster than the Internet—is simple: it creates extraordinary value for its users. I believe PlanetAll will prove to be one of the most important online applications. . . . Jungle has assembled an extraordinary team of people. Together we'll empower customers to find and discover the products they want to buy.

Bezos, commenting on the recent expansion and acquisitions, argues:

Our product extension and geographic expansion is better late than early. Why better late than early? We had to first focus on the book business and grow that until we were comfortable with it. There are always numerous opportunities to expand. We try to err on the side of being slow. Fortunately, we are not capital constrained, but we are definitely people constrained. We only pursue opportunities when the people bandwidth is not constrained. . . . The single most important criterion that we use to acquire a new company is this: Who are the people behind this venture, and what is the people bandwidth of the acquired company going to be? We are looking for business athletes indoctrinated in this space and companies that have a culture that is common with ours.

However, notes a report in the *Wall Street Journal*:

In the end, though, neither specialization nor branding may determine who succeeds in the on-line sales game. In the physical world, hardcore-comparison shopping has been left to a highly motivated faction of consumers willing to trudge between stores. But on the web, it's become almost effortless. Today, a user can enter a title of a book on Yahoo! Inc.'s Visa Shopping Guide site which then queries multiple booksellers for prices and displays the result in a table. Hyperlink next to book prices lets users order the cheapest one at the click of a mouse. With comparison services proliferating elsewhere on the Web — and for dozens of other products — it's unclear whether a sterling brand like Amazon's will ultimately sway consumers when rock-bottom prices are so easy to spot.²⁶

Bezos concedes that many challenges still confront him and his top management team as they ponder the future moves by his firm. Acknowledges Bezos:

It is hard to provide great customer service and experience for the customer. It is hard to grow the business. But when you combine these two, the complexity of operating increases exponentially. We are expanding our product line and broadening our geographic reach simultaneously, and there is a lot of execution risk when you try to do this. Moreover, many of our new initiatives will continue to require aggressive investment and entail significant execution challenges. However, that is the nature of this business.

²⁶ *The Wall Street Journal*, May 12, 1998.

Exhibit 1

AMAZON.COM, INC. - CONSOLIDATED BALANCE SHEETS (unaudited)
(in thousands, except share and per share data)

	JUNE 30, 1998	DECEMBER 31, 1997
ASSETS		
Current assets:		
Cash.....	\$ 2,523	\$ 1,567
Marketable securities.....	337,396	123,499
Inventories.....	17,035	8,971
Prepaid expenses and other.....	12,487	3,298
	-----	-----
Total current assets.....	369,441	137,335
Fixed assets, net.....	14,014	9,265
Deposits and other.....	284	166
Goodwill and other purchased intangibles, net.....	52,398	--
Deferred charges.....	7,622	2,240
	-----	-----
Total assets.....	\$ 443,759	\$ 149,006
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable.....	\$ 47,556	\$ 32,697
Accrued advertising.....	9,971	3,454
Other liabilities and accrued expenses.....	13,713	6,167
Current portion of long-term debt.....	684	1,500
	-----	-----
Total current liabilities.....	71,924	43,818
Long-term portion of debt.....	332,225	76,521
Long-term portion of capital lease obligation.....	181	181
Stockholders' equity:		
Preferred stock, \$0.01 par value:		
Authorized shares -- 10,000,000 Issued and outstanding shares -- none		
Common stock, \$0.01 par value:		
Authorized shares -- 300,000,000 Issued and outstanding shares -- 49,669,601 and 47,874,338 shares, resp.	497	479
Additional paid-in capital.....	104,368	63,552
Deferred compensation.....	(1,301)	(1,930)
Other gains (losses).....	(35)	--
Accumulated deficit.....	(64,100)	(33,615)
	-----	-----
Total stockholders' equity.....	39,429	28,486
	-----	-----
Total liabilities and stockholders' equity.....	\$ 443,759	\$ 149,006
	=====	=====

Exhibit 1 (Continued)

AMAZON.COM, INC.-- CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

(in thousands, except per share data)

	QUARTER ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30	
	1998	1997	1998	1997
Net sales	\$ 115,977	\$ 27,855	\$ 203,352	\$ 3,860
Cost of sales	89,786	22,633	157,840	35,117
Gross profit	26,191	5,222	45,512	8,743
Operating expenses:				
Marketing and sales	26,452	7,773	45,955	11,679
Product development	8,060	2,808	14,789	4,383
General and administrative	3,262	1,708	5,225	2,850
Amortization of goodwill and other purchased intangibles	5,413	--	5,413	--
Total operating expenses	43,187	12,289	71,382	18,912
Loss from operations	(16,996)	(7,067)	(25,870)	(10,169)
Interest income	3,334	366	4,974	430
Interest expense	(7,564)	(4)	(9,589)	(4)
Net interest income (expense)	(4,230)	362	(4,615)	426
Net loss	\$ (21,226)	\$ (6,705)	\$ (30,485)	\$ (9,743)
Basic and diluted loss per share	\$ (0.44)	\$ (0.16)	\$ (0.64)	\$ (0.24)
Shares used in computation of basic and diluted loss per share	47,977	42,634	47,299	40,719

Exhibit 2
Book Publishing Market Structure

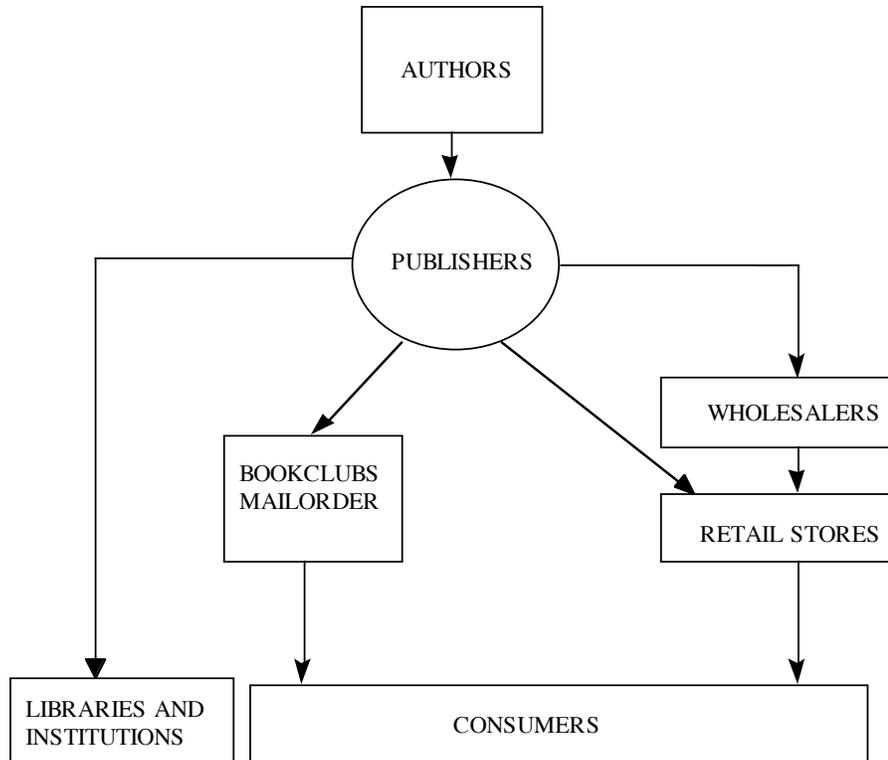


Exhibit 3
Profit Margins for a “Typical” Book.

Book List Price	\$19.95	
Revenue to Publisher (i.e. price paid by wholesaler or bookstore)	\$10.37	48% discount off suggested retail price
Manufacturing cost	\$ 2.00	Printing, binding, jacket design, composition, typesetting, paper, ink
Publisher overhead	\$ 3.00	Marketing, fulfillment
Returns and allowances	\$ 3.00	
Author’s royalties	\$ 2.00	
Total publishing costs	\$10.00	
Publisher’s operating profit	\$ 0.37	Returns amount for 3.7%

Exhibit 4

Book Sales in 1994 by Various Distribution Channels.

Channel	% of Total sales
Bookstore Chains, Independents and general retailers	35%-40%
Mail order and book clubs	21%
Sales to college book stores	17%
Schools	15%
Libraries and other institutions	10%

Exhibit 5

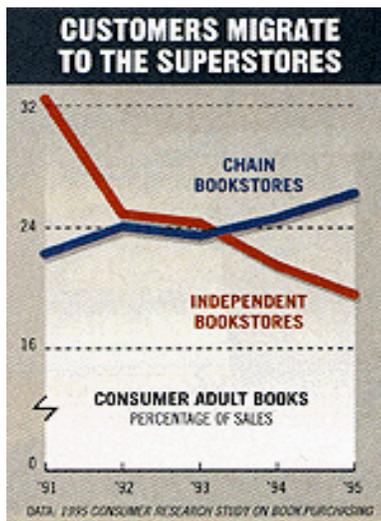
Bookstore Chain Sales (\$millions)

Chain	1998*	1997	% Change
Barnes & Noble	\$2,797.0	\$2448.0	14.2%
Borders Group	2,266.0	1,958.8	15.7
Books-A-Million	324.8	278.6	16.5
Crown Books	297.5	287.7	3.4
Total	\$5685.3	\$4,973.1	14.3%

Source: Publishers Weekly, March 23, 1998, p.17. * Estimates.

Exhibit 6

Growth of Independents vs. Chain Stores



Source: Business Week, 1998.

Exhibit 7

The Various Product Categories

Trade Books. This segment includes general interest hardcover and paperback books sold to adults and juveniles. Trade books accounted for almost 25% of book revenues in 1997. According to industry reports, books sold to adults increased by more than 30% between 1991 and 1995. Juvenile book sales, that showed a double-digit growth rate in the late 1980s and early 1990s leading to many publishers. However, juvenile hardcover book sales represented a 2.3% increase in 1997 over the previous year and juvenile paperback book sales fell by as much as 18.6 percent during the same time period. This slow growth was attributed to a decline in the number of popular titles and increased spending by children on toys and games.

Random House Inc., Bantam Doubleday Dell, Simon & Schuster, Harper Collins, and Penguin are some of the leading firms that competed in this product category.

Professional Books. Over 165 million profession books were sold in 1997 accounting for \$4.15 billion. Since 1991 professional book sales have grown at a compound annual rate of 3.0 percent (in units). Legal publishing was the largest segment of the professional-books category, with the scientific and technical category coming in second place. The long-term outlook for this category was good because employment in the medical, legal, scientific, and business profession were expected to grow strongly.

Thomson Crop's was the largest professional-books publisher with sales of \$1.99 billion. Professional book revenues comprised of 31% of Thomson's total revenues. Reed Elsevier ranked second with 1994 sales of \$1.63 billion, and was followed by Wolters Kluwer and Times Mirror with \$1.07 billion and \$775 million in sales respectively.

Mass Market Books. A large proportion of these books are sold through magazine wholesalers and outlets such as newsstands and drugstores. This category includes bestsellers that have shelf lives of about three to six weeks and in 1997 they accounted for about 7 percent of all books sold. Although the cost of acquiring the paperback rights to a best-selling hardcover title can cost millions of dollars, the per-unit fixed costs for printing are small because print runs were as large as 500,000. However, when return rates, which typically exceed 40% are factored in, profit margins tend to be less than 12%.

The largest publishers are Random House, Bantam Doubleday Dell, Simon and Schuster and Harper Collins.

El-Hi Text Books. El-Hi or Elementary-High school books accounted for 14 percent of all books sold in 1997 (they used to represent 30 percent of all books sold in 1994). Sales in this segment rose nearly 14 percent in 1997 and forecasts suggest that are likely to increase by 4.8% in 1998. El-Hi is driven by state adoption and enrollment levels and are sold to school systems on a contract basis. The development of materials for schools is a capital intensive process that typically takes up to five years to develop for most new programs. Per pupil expenditures as well as the number of students are expected to grow through the year 2000, implying moderate growth (3 to 4%) for this segment.

The big publishers are owned by media conglomerates such as News Corp. Times Mirror and Paramount. The largest el-hi publisher is McGraw Hill, followed by Paramount (the parent company of Prentice Hall and Silver Burdett), Harcourt Brace and Houghton Mifflin.

College Text Books. College publishing is the most profitable category. The cost of producing a college text is lower than in the El-Hi market, because the texts are typically prepared by university faculty members and used individually. However, the unit sales tend to be small and used text book sales generally accounted for 20%-40% of total sales. College textbook sales represented 12.8 percent of all book sales in 1997. Sales are estimated to increase 6.9% to \$2.85 billion in 1998.

Prentice Hall (owned by Paramount) is the largest college publisher, followed by HB College (owned by Harcourt General), International Thomson, Mc Graw Hill and Irwin (a division of Times Mirror).

Exhibit 8

Unit Sales (in millions) and Dollar Sales (in millions) by Product Category.

Product Category	1997 Units	1997 (\$mill)	1998* Units	1998* (\$mill)	Profit Margins in 1993
Trade Books					
Adults (Hardcover and paperbacks)	441.8	\$4095.2	438.9	\$4160.0	13.7%**
Juvenile (hardcover and paperbacks)	343.8	1358.0	355.9	1437.6	7.7%
Mass Market	473.2	1433.8	472.3	1480.3	3.1%
Book Clubs	137.7	1145.3	141.3	1207.2	
Mail Order	85.7	521.0	81.8	504.7	
Religious	166.6	1132.7	170.3	1178.0	12.4%
Professional (Business, medical, scientific, and technical)	165.2	4156.4	169.6	4404.6	8.0%
University Press	17.8	367.8	18.0	382.1	
Elhi (Elementary-High school)	286.5	2959.6	282.8	3102.4	14.9%
College (Textbook and materials)	168.2	2669.7	173.7	2852.8	15.8%
Standard Tests	-	191.4	-	204.3	
Subject Reference	1.2	736.5	1.2	766.9	
Total	2287.7	\$20,767.4	2305.8	\$21,680.9	

Source: Book Industry Study Group Trends, 1998

• Projected sales. **For hardcover books

Exhibit 9

Amazon.com's Customer Bill of Rights

Amazon.com's Bill of Rights claims that as a customer there is:

1. **No obligation.** Eyes & Editors Personal Notification Services are provided free of charge, and you are under no obligation to buy anything.
2. **Unsubscribing.** You can unsubscribe or change your subscriptions at any time.
3. **Privacy.** We do not sell or rent information about our customers. If you would like to make sure we never sell or rent information about you to third parties, just send a blank email message to never@amazon.com

Exhibit 10
Company's Organizational Structure

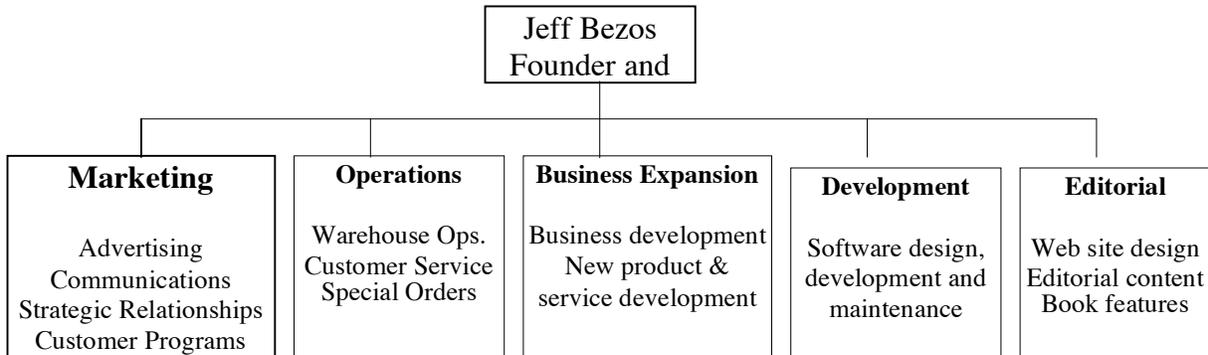


Exhibit 11
A Partial Listing of Online Music Stores

Cdnw* – The idea for this store was conceived in the summer of 1994 and was started by twin brothers Jason and Matt Olim in the their parents' basement in 1994. In 1997, the firm posted sales of \$15 million. It reported averages about 18% in operating margins.

Music Boulevard (www.musicboulevard.com) – Owned by n2k, Music Boulevard operates transaction sites in English, French, German, Japanese and Spanish. Started in September of 1996, n2k.com bills itself as “the premier online music entertainment company and the Internet’s only complete source for music content, community and comment.” In 1997 it reported revenues of \$11.7 million.

Musicspot (www.musicspot.com) – According to a recent 10-000-household PC-Meter survey, CUC’s musicspot ranked top among the top “Hot Storefronts.”

Tunes.com (www.tunes.com) – Berkeley California-based Tunes.com launched in November 1996, features 200,000 thirty-second music clips backed by collaborative filter, which matches visitors’ music interests to profiles created by people with similar tastes. The company, plans to have 1 million samples online by mid-1998, which will make it the largest music sampling source online.

Records Clubs. Record clubs are shaping up to be the Web’s most powerful retailers. An estimated 16.5 million customers belong to record clubs in the US. Columbia House and BMG both debuted web sites in 1995. Their sites now handle all club chores including administration, buying, status checking, and the commendable job of cyber-retailing.

*Cdnw and Music Boulevard signed an agreement on October 8, 1998 to merge their two companies

Exhibit 12

Recent Acquisitions by Amazon.com

Bookpages (www.bookpages.co.uk). As one of the largest online bookstores in the United Kingdom, the firm provides access to all 1.2 million UK books in print.*

Telebook (www.telebuch.de). This firm operating through its ABC Bücherdienst subsidiary, is Germany's number one online bookstore, with a catalog of nearly 400,000 German language titles.

Internet Movie Database (www.imdb.com). Originally launched in 1990, Internet Movie Database is a comprehensive repository for movie and television information on the Internet, and is an excellent example of genuine community on the Internet.

PlanetAll.com (www.PlanetAll.com). The firm launched in November 1996 reportedly has 1.5 million members, and reports that thousands of new members are joining each day to use the secure, free service to organize and automatically update information about friends, business associates, relatives, and alumni. Users accessing PlanetAll service have complete control over their own contact information and decide what information they want to share with others on a person-by-person basis. Moreover, PlanetAll's service is compatible with personal information managers (PIMs) and personal digital assistants (PDAs), such as Microsoft Outlook and 3Com Palm Pilot. Also, it has integrated its service within the sites of a number of Internet leaders, including Lycos and GeoCities, as well as numerous universities and professional associations. Amazon.com intends to operate PlanetAll as a wholly owned subsidiary located in Cambridge. Savage and the two cofounders will remain with the company.**

Jungle Corp (www.junglee.com). The firm was founded in June 1996. The firm's breakthrough virtual database (VDB) technology is based on founders' doctoral research carried out at Stanford University. Junglee's first deployment was CareerPost.com, the Washington Post Company's online recruitment site, in January 1997. Junglee carries more than 15 million items in the Junglee Shopping Guide and over 90,000 job listings in its Job Canopy. Junglee has developed breakthrough database technology that can dramatically enhance customers' ability to discover and choose from among millions of products online. To date, two of the markets it has targeted have been online retailing and online recruitment. Junglee's customers and partners in these markets include Yahoo!, Compaq, Snap!, six of the top seven newspaper companies, and many other new-media companies. All founders of Junglee are expected to remain with the company.

* Each of the acquisitions, Bookpages, Telebook and Internet Movie Database, will be accounted for under the purchase method of accounting. The company will incur total charges of approximately \$55 million in connection with all three transactions. Consideration was comprised of cash and common stock, and the company anticipates issuing an aggregate of approximately 540,000 shares of common stock as a result of these transactions.

** Amazon.com will acquire 100 percent of the outstanding shares and assume all outstanding options of Junglee and PlanetAll in exchange for equity having an aggregate value of approximately \$280 million. Amazon.com will issue approximately 800,000 shares and assume all outstanding options in connection with the acquisition of PlanetAll and anticipates accounting for this transaction as a pooling of interests. Amazon.com will issue approximately 1.6 million shares and assume all outstanding options in connection with the acquisition of Junglee and anticipates accounting for this transaction under the purchase method of accounting.

Appendix A: Amazon.com's Top Management Team

Jeffrey P. Bezos, *Founder and Chief Executive Officer.*

Jeff Bezos has always been interested in anything that can be revolutionized by computers. Intrigued by the amazing growth in use of the Internet, Jeff created a business model that leveraged the Internet's unique ability to deliver huge amounts of information rapidly and efficiently. In 1994 he founded Amazon.com, Inc., an Internet retailer of books and other information-based products that offers services that traditional retailers cannot: lower prices, authoritative selection, and a wealth of product information. Before heading west to start Amazon.com, Jeff worked at the intersection of computer science and finance, leading the development of computer systems that helped manage more than \$250 billion in assets for Bankers Trust Company. He also helped build one of the most technically sophisticated quantitative hedge funds on Wall Street for D. E. Shaw & Co. Jeff received a degree in electrical engineering and computer science, summa cum laude, from Princeton University in 1986. He is a member of Phi Beta Kappa.

George T. Aposporos, *Vice President, Business Development.*

George Aposporos joined Amazon.com in May 1997 as vice president of business development and is responsible for identifying and negotiating key strategic relationships for the company. Prior to joining Amazon.com, George was founder and president of Digital Brands, a strategic consulting and interactive marketing firm that has served clients such as Starbucks Coffee, Sybase, American Express, and BMG Entertainment. While at Digital Brands, he placed Starbucks in the first campaign to use animated advertising on America Online. From March 1994 to August 1995, George was vice president of I.C.E., a Toronto-based multimedia developer and corporate communications firm, where he spearheaded involvement in interactive media, including development of the company's interactive television and Internet capabilities. From 1989 to 1994, George was an independent producer in a variety of media, including television, video, and CD-ROMs. George was an Olin Scholar at Wesleyan University.

Rick Ayre, *Vice President and Executive Editor.*

Rick Ayre joined Amazon.com in September 1996 as vice president and executive editor and is responsible for the editorial content and design of the Amazon.com web site. Rick comes to Amazon.com from PC Magazine, the popular Ziff-Davis publication, where he served as executive editor for technology. Rick launched PC Magazine on the World Wide Web in March 1995. He was responsible for the print coverage of online technology, and he ran PC Magazine's online services, including the PC Magazine Online Web site and PC MagNet, part of ZD Net on CompuServe. During his five years at PC Magazine, Rick also held positions as the magazine's executive editor for software and as technical director for software in PC Magazine Labs, where he supervised all software product testing. Before joining PC Magazine, Rick served as chief of information resources management at the Highland Drive VAMC, a 750-bed hospital in Pittsburgh. He began his technology career while a Ph.D. candidate in psychiatric epidemiology at the University of Pittsburgh in the early 1980s. There he learned to program in Fortran to manipulate large data sets on an early DEC time-sharing system. When the IBM PC was born, he quickly adopted one and taught himself to program in Pascal and to use dBASE. He was soon logging on to local BBS systems, and he's been working online ever since.

Joy D. Covey, *Chief Financial Officer.*

Joy Covey joined Amazon.com in December 1996 as chief financial officer and vice president of finance and administration. She is responsible for financial and management systems and reporting, and she also manages planning and analysis, legal, administrative, investor relations, and human relations activities. Before joining Amazon.com, Joy was vice president of business development and vice president of operations, broadcast division, of Avid Technology, a leader in the digital media industry. From 1991 to 1995, she was the CFO of Digidesign, where she managed a successful IPO and eventual merger with Avid Technology. During her tenure, Digidesign achieved more than 50 percent annual growth and strong and consistent profitability and cash flow, and strengthened its dominant position in the digital audio production systems market. Before she worked at Digidesign, Joy was a mergers and acquisitions associate at the investment bank of Wasserstein Perella & Co. and a certified public accountant with Arthur Young & Co. (currently Ernst & Young). She holds both a J.D. and an M.B.A. from Harvard, where she was a Baker Scholar, and a B.S. in business administration, summa cum laude, from California State University, Fresno.

Richard L. Dalzell, *Chief Information Officer.*

Richard Dalzell joined Amazon.com in August 1997 as chief information officer and is responsible for all Amazon.com information systems, including corporate networks, logistics, electronic buying, accounting, and data warehousing. Before joining Amazon.com, Rick was vice president of information systems for Wal-Mart Stores. He managed all merchandising and logistics systems, led the development of world-class supply chain systems, set the standard for international retailing and merchandising systems, and was instrumental in establishing the world's largest commercial

decision-support and data-mining systems. From 1990 to 1994, Rick held several management positions within the information systems division at Wal-Mart. Prior to that, he spent three years as the business development manager for E-Systems and seven years as a teleprocessing officer in the U.S. Army. Rick received a B.S. in engineering from the U.S. Military Academy, West Point, in 1979.

Mary Engstrom Morouse, *Vice President, Merchandising.*

Mary Engstrom Morouse joined Amazon.com in February 1997 as vice president of publisher affairs and became vice president of merchandising in April 1998. She is responsible for managing supplier relationships and direct purchasing. Before joining Amazon.com, Mary served as general manager of the security business unit and vice president of product marketing at Symantec Corporation, a developer of information management and productivity enhancement software. In these roles, she managed the development, production, testing, manufacturing, distribution, and marketing of Symantec's line of antivirus and security products, including the Norton AntiVirus line. From July 1989 to September 1994, Mary held several management positions at Microsoft Corporation, including group product manager for Microsoft Access, group product manager for Microsoft Project, and director of marketing in strategic relations. Mary received her B.A. in economics from the University of California, Berkeley, in 1984 and her M.B.A. from the Anderson Graduate School of Management at the University of California, Los Angeles, in 1989.

Sheldon J. Kaphan, *Chief Technology Officer.*

Shel Kaphan has served as Amazon.com's vice president and chief technology officer since March 1997. In this role, Shel is responsible for technical architecture and directing technical efforts. From October 1994 to March 1997, Shel was vice president of research and development for the company and was responsible for developing Amazon.com's core software and maintaining the company's web site. Shel brings more than 20 years of experience in designing hardware and software systems and services to Amazon.com. Prior to joining the company, he held senior engineering positions at Kaleida Labs, Frox, and Lucid. Shel received a B.A. in mathematics, cum laude, from the University of California, Santa Cruz, in 1980.

John David Risher, *Senior Vice President, Product Development.*

David Risher joined Amazon.com in February 1997 as vice president of product development, responsible for developing new products and services. He was promoted to senior vice president of product development in December 1997 and now has overall responsibility for product development, marketing, editorial, and content licensing. Before joining Amazon.com, David served as founder and product unit manager for Microsoft Investor, Microsoft Corporation's web site for personal investment. From 1991 to 1995, he held a variety of marketing and project management positions within the Microsoft Access product team, including Microsoft Access team manager. In this role he managed all aspects of the product development team including design, development, branding, advertising, and customer research to produce Microsoft Access 95. From 1987 to 1989 David was an associate at the LEK Partnership, a corporate management consulting firm. David holds a B.A. in comparative literature, magna cum laude, from Princeton University and an M.B.A. from Harvard Business School.

Joel R. Spiegel, *Vice President, Engineering.*

Joel Spiegel joined Amazon.com in March 1997 as vice president of engineering and is responsible for all web site software. From March 1995 to March 1997, Joel held several positions with Microsoft Corporation, including Windows 95 Multimedia development manager, Windows Multimedia group manager, and product unit manager for information retrieval. From June 1986 to March 1995, he held a variety of positions at Apple Computer, most recently as senior manager, and was responsible for new product development in the Apple Business Systems Division. Prior to that he held software product development positions at a number of companies, including Hewlett-Packard and VisiCorp. During his career, Joel has had a hand in the development and delivery of a wide range of software products, including Windows 95 Multimedia, DirectX, Macintosh System 7 File Sharing, several versions of MacDraw, AppleSearch, Smalltalk-80 for the Macintosh, and VisiON. Joel holds a B.A. in biology, with honors, from Grinnell College.

Jimmy Wright, *Chief Logistics Officer.*

Jimmy Wright joined Amazon.com in July 1998 as vice president and chief logistics officer. He is responsible for all global supply chain activities, including managing the company's distribution centers, product purchasing, distribution, and shipping. Jimmy comes to Amazon.com with more than 26 years of experience in logistics management. He was recognized as one of the key logistics leaders within Wal-Mart Stores, the world's largest retailer and a company globally known for its logistics excellence. He joined Wal-Mart in 1985 and served as vice president of distribution from 1990 to his retirement in 1998. During that time he was responsible for more than 30 regional and specialty distribution centers, which accounted for 38 million square feet of retail distribution space, staffed by more than 32,000 employees. Jimmy's career in logistics management began at the Fina Oil and Chemical Company, a branch of Petrofina S.A. based in Brussels. From 1972 to 1985, he held a variety of positions, most recently as general manager of distribution. He received a B.B.A. in personnel management from the University of Texas in 1976.