

An Analysis of Amazon's Internal and External Environments

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Abstract. In the vast landscape of global commerce, Amazon, globally renowned as a premier retailer and a leading provider of cloud services, operates within a dynamic framework shaped by both external and internal forces. This paper meticulously scrutinizes the multifaceted environments in which Amazon operates, shedding light on the intricacies of its challenges and opportunities. Delving into an exploration of Amazon's financial landscape, the study employs a comprehensive financial ratio analysis. This analytical approach serves as a tool for stakeholders, particularly investors, to glean deeper insights into Amazon's financial performance. By deciphering key ratios, this analysis aims to empower decision-makers with the requisite information for making informed and strategic choices. Specifically, the essay endeavors to provide a discerning projection of Amazon's revenue growth rate. This predictive endeavor is undertaken with a cognizant awareness of the complexities inherent in market dynamics, offering stakeholders a foundation upon which to formulate prudent and well-informed decisions.

Keywords: Amazon, Internal and External Environments, Risk Assessment.

1. Introduction

Amazon is a leading e-commerce company that provides customers with a wide range of products, including books, music, DVDs, electronics, clothing, and more. The company was founded in 1994 by Jeffrey P. Bezos and has since grown into a global powerhouse with a presence in over 200 countries. Amazon's success can be attributed to its focus on customer experience, fast and reliable delivery, and innovative technologies such as Alexa and Prime. The company also operates a number of other businesses, including cloud computing, streaming services, and advertising. With its vast product offerings and customer satisfaction commitment, Amazon remains a dominant player in the retail industry.

Amazon has organized its operations into three segments: North America, International, and AWS. The method of making these segments needs to be clarified, consisting of the geography and business type. North America is Amazon's main segment. There are different predominant operations in this area, including retail sales of consumer products and subscriptions through North America-focused online and physical stores. Especially, Canada and Mexico are also incorporated in this segment. For the International segment, it is obvious that areas except countries in North America part are allocated in the segment. This segment includes export sales from internationally focused online stores besides the basic business, like retail sales and subscriptions. Importantly, this export type only includes sales from these online stores to customers in the U.S., Mexico, and Canada instead of sales from our North America-focused online stores. When it comes to AWS, it is part of the amounts earned from global sales of computing, storage, database, and other services for start-ups, enterprises, government agencies, and academic institutions.

Revenue plays an important role in a company's analysis. For Amazon, there are seven parts in revenues. Figure 1 illustrates the composition of Amazon's revenue sources in the year 2022. It is noticeable that sales from online stores are by far the highest rate, about 43% of the whole revenues. Xue states that the sales from physical stores are around 4%, with an absolute figure of \$18,963 million. That means the rest of the total sales are from online operations, so Amazon is obviously an Internet company [1]. This view is reasonable but is not accurate. In other words, the type of Amazon does not have a big influence on the analysis of Amazon. Learning about the primary source of revenues is essential.

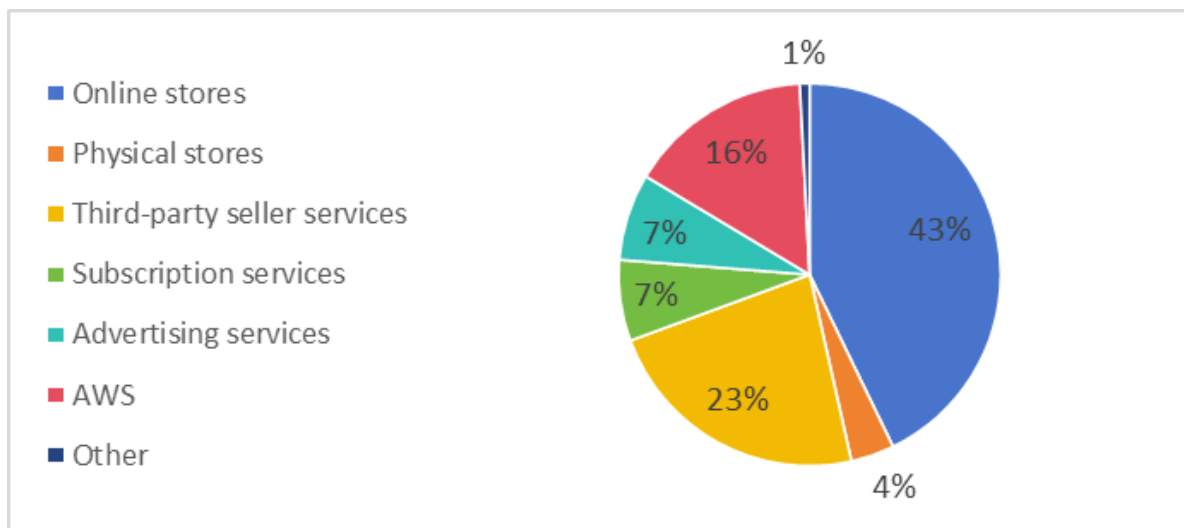


Fig. 1 Net sales composition of Amazon in 2022 (Picture credit: Original)

2. External Environment Based on the Five Forces Framework

Using Porter's five forces analysis framework can be a marvelous way to understand better the external environment Amazon faces. Developed by renowned business strategist Michael E. Porter, it identifies five primary factors influencing the intensity of competition in any given market. This framework gives a clear angle of view to give a comprehensive analysis and can also help a firm to make proper decisions across various levels of a business.

For industry rivalry the e-commerce industry is highly competitive, with many large and small players vying for market share. Amazon faces competition from other e-commerce companies, such as Walmart and eBay, as well as traditional retailers that are expanding their online presence. And many competitors are equal in size and power. Their operations are also diverse. However, Amazon has a strong competitive advantage due to its vast selection of products, fast delivery, and competitive pricing. For example, Amazon provides an e-retail platform for consumers to purchase more conveniently. In the meantime, constructing information systems will maintain relatively low charges, increasing its profits, which plays a central role in enhancing Amazon's holistic competition [2].

Regarding the threat of substitutes, the online shopping industry is highly competitive, and many substitute products and services are available, such as brick-and-mortar stores and traditional mail-order catalogs. So, the threat is high overall. In addition, cheap switching costs for customers are another way to increase the risk of substitutes. However, Amazon has developed a wide range of proprietary services, such as Amazon Prime, to decrease the loss and threat of this replacement. In the meantime, due to the COVID-19 pandemic, most consumers are loath to shop in physical stores, which has lowered the threat of substitution to Amazon and other retailers [3].

Another aspect of this model is the bargaining power of suppliers. Amazon benefits from the bargaining power of suppliers. Due to Amazon's size and large buying volume, the bargaining power of suppliers is low. Amazon can pressure suppliers to get discounts and more preferential policies, which helps reduce costs and improve profitability. Furthermore, Amazon's strong brand and good reputation make suppliers want to get a spot on Amazon's website [4]. Additionally, Amazon's suppliers are not concentrated, which number is large. The factors above show suppliers have moderate bargaining power for Amazon.

For the bargaining power of customers, the level is middle and high. Amazon's customers are price-sensitive and have many options when it comes to buying products online. Customer switching costs are low due to many competitors. However, the company has developed a strong brand reputation and a loyal customer base, which gives it some bargaining power in negotiations with customers. Additionally, Amazon's Prime service offers free shipping and other benefits that can make it more attractive to customers.

The final point is the threat of new entrants. Although there are numerous small retailers in the e-commerce industry and less and less capital is needed to enter this industry, they do not have a big influence on giant companies like Amazon. So, the threat of new entrants could be higher for Amazon. , the recession resulting from the COVID-19 pandemic makes it challenging to finance funding with billions of dollars to compete with Amazon [3]. More importantly, Amazon has a strong brand reputation and a vast customer base, which makes it difficult for new competitors to contend. Additionally, the company has economics of scale, which can decrease cost per unit and push the new entrants to accept a cost disadvantage or enter at scale.

3. Internal Environment Based on Financial Ratios

Financial modeling is all about providing a correct mathematical output of previous work [5]. Ratio analysis is a quantitative method of gaining insight into a company's liquidity, operational efficiency, and profitability by studying its financial statements, such as the balance sheet and income statement.

Table 1. Financial ratios of Amazon

Financial ratio	2020	2021	2022
Gross profit margin(%)	39.57%	42.03%	43.81%
Current ratio	1.05	1.14	0.94
Quick ratio	0.86	0.91	0.72
Working capital cycle(days)	-38	-29	-24

Growth profit margin shows 39.57%, 42.03% and 43.81% of sales left over after taking away costs of buying in materials and relating to processing the materials in 2020, 2021 and 2022. Generally, GPM is increasing from 2020 to 2022. It is a good news that suggests Amazon has control over quantity, selling price and cost of raw materials. As a result of a strategic decision made by Jeff Bezos twenty years ago, Amazon maintains low e-commerce margins, eschewing low pricing to customers [6]. However, because Amazon has developed other high- profit business these years like AWS, the gross profit margins in recent years have increased and been stable above a middle to high level.

Current ratio is a mean of illustrating the relationship between current assets and current liabilities, which reflects the solvency of a company. From Table 1, the ratio, respectively 1.05, 1.14 and 0.94, shows the ability to pay debt of Amazon in years 2020, 2021 and 2022. A common current ratio is above 2, while for these three years, none of it is above the standard. To give more accurate analysis, using quick ratio to take away inventories is a good method. Generally, quick ratio is above 1. In Table 1, the results still can't be fine. But it may not be the bad news. Recent years, Amazon takes actions to extend its business and enter more new market like computing, which has cost lots of capital and investment [7].

It is interesting that Amazon's working capital cycle is negative in 2020, 2021 and 2022, which is -38, -29 and -24 days. The negative figures mean that Amazon collects cash faster than it paid off suppliers [8]. So it is a free source of finance. The reason that Amazon has negative working capital cycle figures may be the suppliers have special relationship with Amazon and Amazon has power to negotiate to extend the payment days. It also shows that the strong power of bargaining and operations. Another factor responsible for the favorable working capital cycle of Amazon is the cash on delivery of her products and taking advantage of more third-party deal, which allows it to continue to grow as it can invest in new ventures with the free cash [8].

4. Strategy & Risks

After the analysis of environment Amazon faces, it is clear that though the industrial situation is complex, Amazon's partners and leaders have taken actions and achieved some goals. On the one hand, they strengthened the brand reputation and provided clients with a vast range of products and

services. On the other hand, an efficient distribution system was built to deliver goods in time. The two achievements have a big influence on Amazon's success.

Amazon's customer-centric strategy is a critical aspect of its business model that differentiates it from competitors. This strategy revolves around gaining deep insights into customers' needs, desires, and challenges and using these insights to create personalized and relevant solutions. Through advanced data collection and analysis systems, Amazon tracks customer behaviors and purchasing habits to tailor its product recommendations, pricing strategies, and advertising campaigns accordingly.

According to Bezos and leaders in Amazon, all of them devote themselves to making Amazon the Earth's most customer-centric company. Looking through Amazon's annual report, it gives information on the traditional strategy. They offer all kinds of clients products and services, such as consumers, sellers, developers, enterprises, content creators, advertisers, and employees. Human capital is an essential part of Amazon. For instance, regarding developers and enterprises, Amazon provides a wide variety of on-demand technology services, AWS. Through AWS, all developers and enterprises enjoy advanced services like computing, storage, databases, analytics, machine learning, etc. In addition, Amazon also manufactures and sells electronic devices for clients in need. Another key component of Amazon's customer-centric approach is its unwavering commitment to top-notch customer service. From its 24/7 support and straightforward return policy to its comprehensive feedback system encouraging customer input, Amazon goes above and beyond to ensure satisfaction. The other meaning of customer-centric is innovation on behalf of the customers [9]. According to Amazon, this aspect points to searching for what the customers don't know they want and distributing it to them.

Amazon's logistics strategy is central to its business model and has enabled it to dominate e-commerce. The strategy revolves around speed, efficiency, and customer satisfaction. It is commonly acknowledged that a fast and efficient distribution system can evoke the thinking of shopping. Speed of delivery is as important as the product quality for a customer. It would not be wrong to say that logistics could be the defining factor for the success of e-commerce companies in retaining their consumers [10]. Especially for online shopping, when customers visit the website and desire to get one of the commodities, they are bound to hold the beloved one immediately instead of three days or even one week later. It is vital for online retailers to construct a highly efficient logistic system.

To further enhance its logistics capabilities, Amazon has launched several initiatives. One such initiative is Amazon Flex, which enlists independent contractors to deliver packages using their own vehicles. Amazon Flex is currently part of Amazon's one-hour delivery service, called Prime Now. This service is available in 13 cities and offers one-hour deliveries for \$8, with no additional fee for deliveries within two hours or longer. It is only accessible to Amazon Prime members, who pay an annual fee of \$99. This method reduces delivery costs, increases flexibility, and speeds up deliveries.

When it comes to the topic of risks, there are a lot of risks that a firm may potentially take. For Amazon, there are twenty pages to describe the risks they face, such as legal risks, business and industry risks, and so on. Furthermore, Amazon is famous for its third-party operation model. It is notable that the uncertainty of third-party behavior is also a potential risk for Amazon. Amazon is responsible for supervising the actions of third parties and paying attention to the change of law and policies of the country in which the third party is located.

In addition, being a transnational company, Amazon faces internal interest and foreign exchange risks. Recently, in the context of the Federal Reserve Board raising interest rates it caused the appreciation of the U.S. dollar and more violent fluctuations in exchange rates. In a short time, the behavior of the FED favors the dollar's value. Meanwhile, the dollar may devalue after the peak of rising interest rates. In the meantime, people may have a negative expectation for the value of the U.S. dollar. According to expectancy theory, the trend will be true. This change may influence the international segment of Amazon reflected in its financial statements.

5. Conclusion

Overall, Amazon has achieved marvelous goals and become the leader in the e-commerce industry, though the market is changing and complicated. For the next five years, a brief forecast is made about the growth percentage of Amazon's revenue.

In the North American segment, due to no foreign exchange risks, 10% growth will be forecast for the next five years, while it will be 13% in 2022. The reasons include the revival of global economics from the COVID-19 pandemic and the rising of Prime member's prices. As for the latter, customers may not cancel the service for a price increase because of the excellent resources on Prime. In addition, according to the third party's forecast, the advertising service will be expanded in the coming years. So, the increase in advertising revenue will also increase the whole revenue in this segment and even another international segment. For the International segment, the average growth may be 12% in 5 years, higher than that in 2022 with a negative 8%. The U.S. dollar is predicted to be devalued over a long period for foreign exchange risks. The reason is analyzed in the former context. So, the figures in the annual report may be increased because the local currencies are used in international segments and because of the devaluation of the U.S. dollar.

In terms of the AWS segment, the growth may be around 15% in the future. There are several reasons explaining the predicted proportion. Firstly, especially in recent years, more and more companies become Amazon's customers for AWS. So, there is a rapid speed in the growth of AWS. Secondly, the rapid speed will not keep up in the next five years through growth in 2022 with 29% and regular development. In the meantime, AWS faces short-term headwinds right now as companies are being more cautious in spending given the challenging, current macroeconomic conditions. One of the many advantages of AWS and cloud computing for customers is that they can seamlessly scale up when their business grows. Conversely, if their business contracts, they can choose to give us back that capacity and cease paying for it. The payment is not perpetual. So, the average growth may be lower than that in 2022. In conclusion, all investors can comprehensively consider the factors above about Amazon and make proper decisions.

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