The Amazon Factor: How Companies Are Contending With a Monster Competitor

By [Danielle Fugazy](), [Axial]()

What is your strategy for dealing with Amazon? That's a question an increasing number of companies in an increasing number of industries are being forced to ask themselves. No longer impacting just retail, Amazon has been throwing its weight around in various end markets including artificial intelligence, business and cloud services, clothing and accessories, financial services, food, hardware, home services, media and entertainment, publishing, transportation, and even healthcare.

This has big implications for private equity: "With every deal an investor has to ask itself what is the competitive set. In asking that question, you have to consider Amazon and its incredible strength. You can't ignore Amazon. If you are not comfortable you can make money with their presence, then this is not the right business for you," says Richard Kestenbaum, a partner with Triangle Capital, a middle market investment bank. "Amazon as a competitor is a monster. They are highly creative and have endless resources and fantastic human capital. They are hurting a lot of people and keeping others sharp."

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Amazon is willing to spend big to get ahead, and the market is rewarding the company. Amazon stock soared past its all-time high as the company crushed its first quarter earnings. Various reports indicate that Amazon spent more money on R&D in the last two years than the top 20 retailers combined excluding Wal-Mart (NYSE: WMT). And according to Inc. magazine, over the past two decades Amazon has invested in or bought 120 companies.

"There's a different take on Amazon in every sector, but most companies are either going to compete, collaborate, or copy Amazon. Regardless, every companies need to think about it in some way," says Aaron Cheris, head of Americas Retail with Bain Consulting. "The companies that are going to compete need to be ready."

Strategies in the Retail and Grocery Space

It's illuminating to look at how companies and investors are dealing with Amazon's strength in retail. Amazon already controls about 40 percent of the U.S. e-commerce market and is on track to own more than 50 percent of the market by 2021, according to Bain & Company's Global Private Equity Report 2018.

Some are choosing to compete directly, while others are taking advantage of the disruption Amazon is causing.

Cerberus Capital Management-owned grocery chain Albertsons Cos. is doing what it can to directly compete with Amazon. Albertsons is a grocery store chain with a presence in 35 states under 20 different banners, including Acme, Safeway, and Vons.

Albertsons' and Rite Aid Corp. have agreed to a merger — a deal which is valued at $24 billion and expected to close in the second half of 2018, but is currently awaiting regulatory approvals. The merger will make the combined company one of the largest grocery store chains and one of the larger health companies. It's a move that would further allow the grocery chain to compete more effectively against Amazon by offering more products to customers.

"As soon as Amazon started going to different states talking about selling prescription drugs, the drug world took notice. You started seeing merger activity aimed at protecting the sector. CVS' acquisition of Aetna and Albertsons' acquisition of Rite Aid are great examples of how companies are starting to work together to protect market share," says Cheris.

Albertsons has also opened a digital marketplace for third-party consumer product companies to sell their goods online — giving smaller vendors an opportunity to have their products reach a wider audience, while allowing Albertsons a chance to capture a larger share of sales that would have most likely gone to Amazon.

Taking Advantage of Amazon's Disruption

In 2014, the private equity firm HGGC paid $154 million for a controlling stake in MyWebGrocer (MWG). MWG gives brick-and-mortar grocery stores a fighting chance to defend their market share by allowing customers to shop 24/7 and get food delivered to their homes.

"We are always thinking about how we can help companies that are going to get dislocated and disintermediated by Amazon," says Richard Lawson, CEO of HGGC. "End markets everywhere are being changed by Amazon. As Amazon scales they will challenge all kinds of industries and it will have a cascading effect across all sectors. You are already seeing more companies trying to connect their brands with consumers in new ways."

MWG manages digital solutions for more than 140 retailers nationally, representing more than 10,000 stores and 200 major consumer packaged good brands, including well-known brands like McCormick, Kelloggs, Unilever, and Nestle.

However, the fight of the local grocers got harder when Amazon pushed directly into the space with the acquisition of Whole Foods Market and the launch of Amazon Go. MWG doesn't have a fleet of deliver trucks or warehouses filled with items like Amazon. Instead, the company provides web-based tools that lets grocery stores offer an internet presence.

"On one hand Amazon is bad for players like MWG because Amazon is already the number one seller of online groceries in the U.S. On the positive side, as the growth in the category accelerates, you will have more grocers looking for the solutions that players like MWG provide, but all grocers are going to have to step up their game to compete effectively," says Cheris.

Companies like MWG are banking on market growth to create competitive opportunities. E-commerce remains only a single-digit percentage of the $1 trillion grocery market.

"Amazon does a great job at putting items in front of consumers," says Lawson. "But traditional retailers have to keep fighting the battle. There are tactics that companies can use to fight back. It's a battle, and we are trying to help these retailers win."

The Danger of Data

The grocery business is particularly attractive because it offers true insight into purchases, which then allows companies to better understand preferences and purchased decisions. "Everyone uses a rewards card at the grocery store so you know exactly what they are purchasing and you can target customers with other offerings even outside of grocery," says Lawson.

Of course, this already a core part of the Amazon playbook. With an incredible amount of data, Amazon knows what people are buying, when they are buying it, and when to offer customer refills or competing products. With its grocery business growing since its purchase of Whole Foods, Amazon is in a prime position to mine the data and offer customers all kinds of products. The risk for competitors is that Amazon's data juggernaut lets them go from strength to strength.

Beyond Retail

Even if a business has substantial product overlap with Amazon, it doesn't mean all hope is lost. Given Amazon's daunting presence, firms need a systematic approach for understanding what Amazon is likely to do in a given sector and product category and work to differentiate themselves.

Consumers of baby products, for example, may opt for a retailer that offers a wide selection of high-quality goods deemed safe, chemical-free, and non-allergenic because they trust that retailer's specialized knowledge and experience.

The right assortment can work, but so can the right niche. Karine Philippon, a partner at the accounting and consulting firm Mazars USA, recently met with a client with a unique offering. Said Philippon, “They have very niche product that’s affordable. It’s not something you will find on Amazon. In some ways you can find everything and nothing on Amazon, because it’s common stuff. If you own that very nichey product you are less at risk.”

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Bain’s Cheris agrees. “Companies can compete, but they have to have something unique to break the flywheel. You have to have a unique selection, a compelling category tailored experience or lower prices. If a company can do better in one of those areas, it can compete. Wayfair is a great example with a lot of unique assortment and a compelling furniture-oriented experience,” says Cheris. “You can no longer say, the company is growing and the market is growing and draw a straight line up and to the right. You have to have a unique assortment, customer experience, value proposition and the ability to drive traffic to compete today.”