# Learning from Amazon's Operating Model
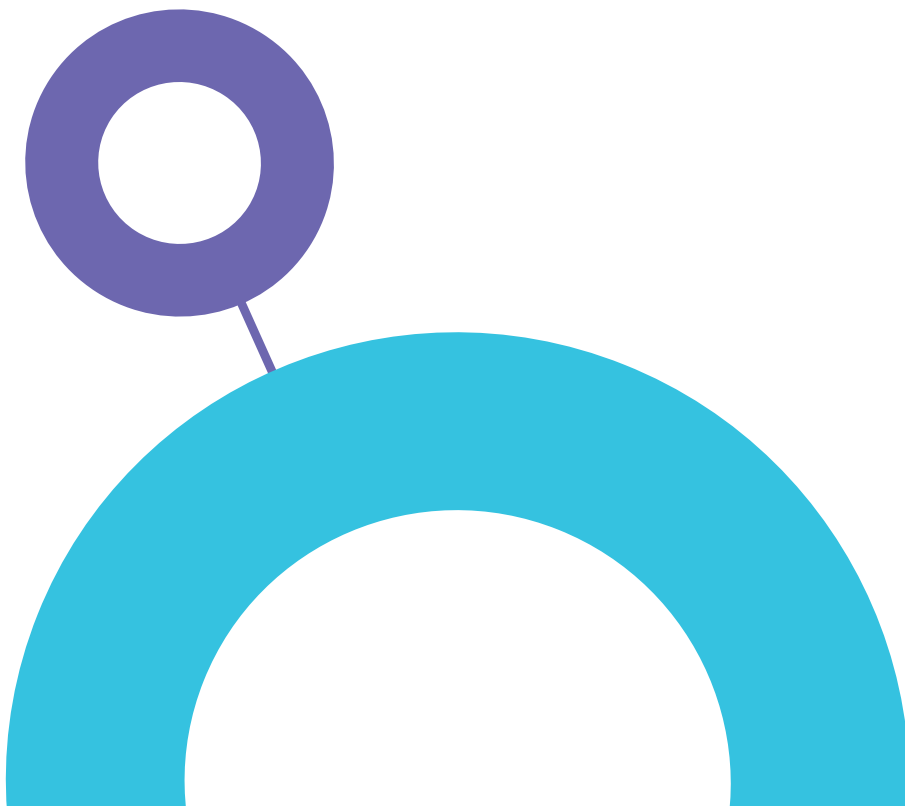
## Engineering a customer-centric transformation

By **Michael Ross**, Co-Founder and Chief Scientist, DynamicAction

**Over 25 years, Amazon has developed a strategic approach that is firmly centered on its customers and powered by data. So how can you leverage Amazon's experience in creating and operating a customer-focused model in your business?**

**For the 4 core characteristics of Amazon's successful model and 12 rules for putting it into practice, read on.**

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## Learning from Amazon's operating model
## How to engineer a customer-centric transformation

Like it or loathe it, Amazon is a colossus that can't be ignored. In 2018, Amazon did $117b in first party sales and $160b in third party sales for a total of $277b in gross merchandise volume . Many naysayers complain that Amazon doesn't make any profits—this is simply not true. Amazon made over $3b in profits last year. Even more importantly it takes a very long-term view of customer profitability, with a model that allows it to navigate the trade-off between growth vs. profitability.

Over 25 years, Amazon has developed a strategic approach that is firmly centered on its customers, and powered by data. All retailers need an "Amazon strategy," and we believe this has **two fundamental components**:

1. **A value proposition** based around exclusive products, service and experience that gives a sustainable point of difference.

2. **An operating model** that takes the best bits of the Amazon approach.

## So how can you apply some of this Amazon-style customer-focused model to your business?

### Setting the scene: how consumer data changed the world

Profit in retail has always been driven by customers. But historically, they have mostly remained anonymous, with the exception of local, traditional forms of retail where a shopkeeper knows each customer by name. Retailers have been able to make good enough business decisions just by looking at the profitability of a channel, store, product or category.

Today, digitally-enabled consumers have changed the economics and dynamics of retail. With almost unlimited choice and immediate access, consumers are empowered and redefining the shopping experience. They are seamlessly shifting between a range of devices, and are researching, shopping and even returning in new and complex ways. Importantly, they also now leave a "digital exhaust"—a cross-channel breadcrumb trail made up of every impression, click, purchase, loyalty credit, basket addition and return.

This dynamic drives intense competition for every potential customer. As well as Amazon, other obvious winners are Google, FedEx and, of course, consumers. The critical challenge for retailers and brands is to find a profitable path, work out how to make sense of all their data and rethink their approach to making decisions.

*Data is the new oil—it needs to be extracted, processed and refined to be turned into something useful.*

Dr. Andreas Weigend,
former Chief Scientist at Amazon and Advisor at DynamicAction

## The so what: a seismic shift in the fundamentals of retail

These changes in consumer behavior are catalyzing massive shifts in the fundamental economics of retailing. Retailers who have been accustomed to analyzing hundreds of stores, or thousands of products, suddenly have to contend with understanding millions of individual customers.

- **New revenue drivers:** Revenue is now driven by customer acquisition and retention, a more complex dynamic than traditional comp sales (like-for-likes). It is critical to understand which customers are high value (hang on to them, and find more like them); and which lose money (find out why and/or stop doing business with them).

- **New costs:** A new set of variable marketing costs (per impression, per click, per transaction), and variable "per order" costs (picking, packing, postage, returns) are replacing the more predictable costs of staff and rent. Crucially, profit no longer correlates with revenues.

- **New data and decisions:** Consumers create deep lakes of data that managers can use—each shopper's digital exhaust has millions of data points. Managers need to collate massive and messy data sets to fully understand customer profitability, and keep pace with the inexorable trend towards surgical, semi-automated decision making.

- **New organizational interconnection:** Actions and decisions were once relatively easy to understand and could be assessed within a functional silo, by store or by region (which drove the evolution of traditional retail organization structures). Now they are more complex and interconnected. Merchandisers, marketing and store/site operations must triangulate to decide how the next dollar will be made or spent on products, marketing or customers.

*Data is only valuable if it helps you make a decision.*

**Dr. Barney Pell**,
artificial intelligence pioneer and DynamicAction Advisor

*DynamicAction empowers us to make decisions and take action quickly and promptly as a merchant team. I look at opportunities across all functional areas to pick the opportunities that make the most sense at that point in time.*

**Kamlah Frances**
Web Analytics Specialist

## The Amazon way: a customer-focused operating model

Retailers are beginning to recognize that the traditional operating model no longer works. It is incredibly easy NOT to make money—to design propositions that customers love, shareholders hate, and that drain working capital from the  business. The Amazon approach effectively adds a customer dimension across the business. This new operating model has four core characteristics.

# 4 Core Characteristics of the Amazon Model

## 1 Consumer Profit

**OLD MODEL**
- Focused on revenues, which made sense when costs were mostly fixed (e.g., rent, staff) and discounts and promotions were tightly controlled.

**AMAZON MODEL**
- Deep understanding of profit by customer and by SKU.
- Focused on lifetime customer profitability.
- Comprehensive view of the purchase process across channels, from first marketing touch to delivery and returns.

## 2 Surgical Actions

**OLD MODEL**
- Actions are blunt, based on sparse data and reliant on physical execution.
- Predominantly taken at the broad level of stores, categories or customer segments.

**AMAZON MODEL**
- Focused on specific actions and applied at the right level of granularity: customer, SKU, keyword, site page, store and transaction level.
- Developed model of "high value actions" where they understand the impact of customer actions on long term value.
- Approach to type 1/2 decisions where focus is on speed to action for reversible actions.

## 3 Customer Centered Metrics

**OLD MODEL**
- Comp sales and outcomes are used to tell a simple story.

**AMAZON MODEL**
- Measurement of things that matter to customers to drive the right conversation (controllable input metrics).
- De-averaging of metrics and reports, with the focus on exceptions and outliers.
- Celebration of waste as an opportunity to improve

## 4 Automated & Coordinated Execution

**OLD MODEL**
- Physical execution within silos, driving "good-enough" results.

**AMAZON MODEL**
- Semi-automated execution across silos enabled by workflow/APIs, as well as coordinated action across internal teams.
- Leaders are trained to manage hybrid teams of humans + AI.

# 12 rules for operating like Amazon

## Focus on customer profit

1. Build your plan based on customer acquisition and retention. Review performance and customer cohorts by month, and against the plan.

2. Understand which customers make or lose you money, and how (e.g. by channel, offer, basket).

3. Design a value proposition, such as delivery options, free delivery, promotions or markdowns, aligned to customer profitability.

## Take surgical actions

4. Add a customer-focused lens to strategic decisions around range, stores and marketing. What are the products, brands or keywords that acquire and retain high-value customers?

5. Take tactical actions at product/SKU, customer and customer/SKU level. Avoid using blunt discounts and broadcast promotions to solve a SKU overstock.

6. Profit-hunt with precision across keywords, landing pages, transactions, sessions, etc.

## Discuss customer-centric metrics

7. Measure customer outcomes, but focus on controllable, actionable input metrics rather than catching every data point.

8. Design reports that de-average performance to focus on outliers, failures and anomalies you can learn from.

9. Develop insight that recognizes the distribution of customer lifetime value.

## Semi-automate execution

10. Recognize the need for connected teams, data and action.

11. Automate the trivial and the repetitive, and ensure that the entire tech stack is powered by clear and connected data.

12. Empower team members to act quickly and decisively.

# About DynamicAction

DynamicAction is a retail analytics guidance system that leverages cloud software and a proven success program to catalyze the new customer-first operating mindset in retail. DynamicAction empowers retailers with a clear path to navigate their transformational journeys with AI-powered metrics. It enables faster, better decisions to deliver profit, analytics and visualizations for immediate insights, prioritized opportunities and prescribed actions to take online and in-store.

Forward thinking retailers across the globe rely on DynamicAction's advanced analytics and retail-built practices to holistically run more efficient organizations and formulate laser target strategies to uncover their most profitable customers. Forrester Research recommended DynamicAction as the key prescriptive analytics technology to replace predictive analytics in retail, and the National Retail Federation awarded DynamicAction for its ability to "significantly improve or radically alter how retailing is done."

Headquartered in Silicon Valley, DynamicAction has offices in London, Sofia and Dallas.

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