Case Analysis of Amazon's Acquisition of Whole Foods

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Abstract: Since the 21st century, the process of economic globalization has accelerated the occurrence of various enterprise economic activities. Take the example of acquisitions, the number of occurrences in the world is increasing every year. Amazon's acquisition of Whole Foods is undoubtedly one of the most successful cases of the 2010s, whether in terms of economic benefits or the subsequent development of the two. This research first introduces the basic information of Amazon and Whole Foods Supermarkets to explain the conditions and timing of mergers and acquisitions; secondly, this research analyses various financial indicators of Amazon after acquiring Whole Foods supermarkets and analyses this acquisition behaviour financial synergies brought to Amazon; finally this research elaborated on the operational synergies and management synergies brought by this acquisition.

1. Introduction

Amazon, as one of the earliest and largest e-commerce companies in the United States and the world, has the highest market value among listed companies in the U.S industry monopolists. From its establishment in 1995 to 1998, Amazon's sales from a single product to the sale of multiple products consisted of discounts, low prices and even free delivery services. It relied on advanced logistics management systems to improve efficiency and reduce logistics costs. At the same time, Amazon creates its own identifier, ASIN, which was using a large number of codes to improve the management efficiency of goods. Initially, Amazon was cautious about setting up physical stores, but in December 2016, it created Amazon Go, an offline physical store, and then began to enter the offline physical industry. Judging from today's facts, such behavior will not make people feel that they are not providing trials for the acquisition of Whole Foods Supermarket, and intentionally expanding offline. Since 2017, due to the change of global economic situation as well as the large amount of products input from the developing countries, commercial real estate in the U.S domestic market has been sluggish, and the retail industry has also been in a slump, which has become one of the major market environmental factors for Amazon's entry into offline supermarkets. Before the time comes in the future, it is necessary for the managers of any farsighted enterprise to take precautions and to occupy the market share of the field that is going to undergo fierce competition in advance. In order to avoid becoming a constraint in the future O2O market share occupation, of course, Amazon must enter offline physical stores for its own development and changes.

Whole Foods Supermarket was founded in 1978 and has expanded rapidly in the past few decades. It has more than 400 offline stores, is facing the middle class, and follows the high-end elite consumption route. It is the first supermarket chain in the United States to operate natural organic food. However, with the popularity of natural and organic food, the advantages of Whole Foods supermarkets have declined, and the operation is in trouble. Whole Foods has struggled in recent years, as a result, its share price has been falling from $70 to nearly $30. Unsatisfied with the performance of stock price, the shareholders want it to be private. For Whole Foods, like other retailers, in order to control costs, a large number of offline stores have also been closed, and the speed of closing stores has gradually accelerated. So the Whole Foods purchase was unsurprising to experts who are familiar with the U.S. retail market, but simply they didn't expect amazon to be the buyer. In the more than 30 years from its creation to its acquisition, it has accumulated a comprehensive information management system, standardized supply chain, and implemented standard management, which coincides with Amazon's concept of standardized information management.

Under such an environment, Amazon and Whole Foods have complementary needs, and the double win cooperation has become a goal for both parties to seek development. On the evening of June 16 2017, Beijing time, the largest fresh and organic food in the United States announced that it has been acquired by Amazon, the largest e-commerce platform in the United States [1]. The acquisition of Whole Foods (including its net debt) at a price of $ 42 was $13.7 billion, and is expected to close in the second half of 2017.

2. Literature Review

There are various forms of studies on corporate mergers and acquisitions (M&A). Research scholars also divide them into different types of mergers and acquisitions to conduct research according to different classification basis, so as to obtain various lessons and enlightenment. This article will describe the literature review on M&A of Whole Foods and Amazon.

The academic circle has accumulated a lot of research on M&A theory. International scholars believe that M&A is an important way for enterprises to seek development. It is a prominent phenomenon in the history of modern enterprise economic development that enterprises achieve expansion through the acquisition of competitors [2]. But Chinese scholars believe that M&A significantly reduced the company's performance level by comparing the market response and the performance of the company's financial indicators before and after the M&A event [3]. However, the existing research cannot meet the practical needs of the rapid development of enterprises. Therefore, this paper reviews and discusses M&A again.

As a matter of fact, research on Whole Foods supermarkets is also increasing day by day, including research on standardized management and M&A strategies of Whole Foods supermarkets. Since its establishment, about one-third of the stores in Whole Foods have been acquired through acquisitions. While continuously expanding its market share through acquisitions, it has also clearly achieved synergies [4]. As a result, Whole Foods continues to grow and mature, but due to fierce competition from similar companies in recent years, the market share that was previously dominant has been increasingly decomposed, and Whole Foods has to seek a turnaround.

At the same time, Amazon, the world's number one e-commerce company, is marching offline and is also looking for opportunities. Amazon was founded in 1995. At the beginning, it was just an online bookstore. However, through just 20 years of development and expansion, Amazon is now the world's largest e-commerce website. The success of Amazon is inseparable from various forms of mergers and acquisitions [5]. They summarized the history of Amazon's major mergers and acquisitions—acquisition of audiobook companies to occupy the audio download market; mergers of audiobook companies to occupy the audio download market; mergers and acquisitions of self-publishing companies to expand business models; and merger stream automation to improve warehousing efficiency; M&A of screen display technology company, research and development of color Kindle; M&A of video game development company, want to enter the set-top box market, etc.

Throughout the history of Amazon's mergers and acquisitions, it is not difficult to see the strategic intent. The industries of the acquired companies are all Amazon is ready to enter. These companies have the conditions and status that Amazon needs to enter the industry [6]. Amazon's acquisition strategy is both offensive and defensive rather than defeating or confronting similar companies. It is better to buy what you need directly, which is also the highlight of Amazon's merger strategy. Similarly. Whole Foods is mainly engaged in organic fresh fruits and vegetables. For Amazon, this is a breakthrough in key categories. Chen Shu believes that for Amazon, the acquisition of Whole Foods can enhance its offline strength, pass online advantages to offline, integrate online and offline, and form an omni-channel retail model [7].

Based on the above research, in the following sections, we will discuss the acquisition from three aspects: financial synergy, operation synergy, and management synergy.

3. Synegies analysis

In this section, firstly this research uses the basic financial data, prime operating revenue, prime operating costs, gross profit and each of their year-on-year growth to discuss the influence which this acquisition towards the cash flow. Secondly, this research analyses the change of Amazon's stock price fluctuation before and after this acquisition. And then this research discusses the effect of Amazon's financial ratios that this transaction brought to. Next two parts describe the operation synergy and management synergy.

3.1 Financial Synegy

3.1.1 Basic Financial data

After the integration of the acquisition was completed, Amazon has more free cash flow from the company, reflecting the contribution of the acquisition store to the company's cash flow and profit, expanding the size of the company's assets and strengthening its capital strength.

Table 1. Basic financial data before and after Amazon bought Whole Foods

	2018/3/31	2017/12/31	2017/9/30	2017/6/30	2017/3/31
Prime Operating Revenue	51.04B	60.45B	43.74B	37.96B	35.71B
Year-On-year Growth	42.92%	38.21%	33.72%	24.84%	22.61%
Prime Operating Costs	30.73B	38.49B	27.55B	23.45B	22.44B
Year-On-year Growth	36.98%	36.32%	34.68%	28.62%	24.72%
Gross Profit	20.31B	21.96B	16.19B	14.50B	13.27B
Year-On-year Growth	52.98%	48.54%	41.39%	29.22%	29.35%

Data source: http://quotes.sina.com.cn/usstock/hq/balance.php?s=AMZN

Amazon announced on June 16, 2017 that it would buy Whole Foods Market, an offline retail supermarket, for $13.7 billion. Before the acquisition of Whole Foods, the worst thing Amazon sold online was food and beverages. So this acquisition is considered an important step for Bezos to expand its retail footprint. At the same time, the addition of Whole Foods Market has also driven Amazon's revenue. The acquisition was consolidated in 17Q3. It can be seen that due to the Whole Foods' drive in the quarter, revenue growth has increased significantly (Table 1). Through Amazon's July-September 2017 operating results announcement, it achieved a total of US $43.7 billion in operating income, an increase of nearly 34% over the same period last year, of which revenue from Whole Foods supermarkets was US $1.3 billion, accounting for 3% of overall revenue. And in the report data of 2017 and 2018, it has maintained a high growth rate. During the same period, Amazon's operating profit was $347 million, and $21 million came from Whole Foods, down 40% from the same period last year. Among them, the increase in income is the highest in five years.

3.1.2 Stock Price

Profit is a summary and re-presentation of the company's past operating performance and results, while the stock price more reflects investors' predictions of the company's future development prospects and profitability, and it also reflects whether the market is optimistic about the future of a company good response. As shown in the Figure 1, Amazon's stock price has fluctuated since 2012. At the beginning of 2012, Amazon's share price was about $149. At the end of 2017, Amazon's stock price rose 7% and returned to more than $1,000. The market value has also increased by approximately $30 billion. As of February 2018, Amazon's stock price has reached $1528.70 per share, an increase of 925.97% in more than six years. This alarming rise reflects the market's high expectations for the future development prospects of Amazon after the acquisition of Whole Foods. It can also be seen from the above figure that even though the profit data of the 2017 financial report reported by Amazon in February 2018 was not strong, the stock price still soared. This shows that the market is optimistic that Amazon trades short-term profits for the market and focuses on long-term development.

Figure 1. Amazon's stock price from 2012 to February 2018

3.1.3 Basic Financial Ratios

Table 2. Financial ratios before and after Amazon bought Whole Foods

	2013	2014	2015	2016	2017
Accounts Receivable Turnover	18.31	17.15	17.78	18.42	16.54
Inventory Turnover	8.06	7.99	7.73	8.13	8.14
Current Assets Turnover	3.24	3.18	3.16	3.31	3.36
Fixed Assets Turnover	8.27	6.38	5.52	5.34	4.56
Total Assets Turnover	2.05	1.88	1.78	1.83	1.66

Data source: http://quotes.sina.com.cn/usstock/hq/balance.php?s=AMZN

As shown in Table 2, there are five properties of financial ratios can be derived as the follows:

(1) Turnover rate of accounts receivable. The greater the receivables turnover rate, the shorter the time that Amazon's receivables are collected, the lower the probability of possible bad debt losses. Judging from these two tables, Amazon's accounts receivable turnover rate has been stable at around 17 for a long time, which is a median level in the industry. Amazon's accounts receivable turnover rate has been relatively stable, and has remained between 16% and 18.5% in the past five years. It declined slightly in 2017, which may be due to Amazon's estimated sale of $11 million in the Whole Foods supermarket "365 Select" The brand's natural and organic products are far lower than the private label of other supermarket competitors.

(2) Inventory turnover rate. As shown in the table above, Amazon's inventory turnover rate has been very good in the past five years as a whole, stable at about 8, and the inventory turnover rate in 2017 is at its highest level in the past five years. Reversing its worst sales decline since going public in 1992. It has four "Whole Foods 365 Supermarkets", which are cheaper to build and operate than traditional Whole Foods supermarkets, and also offer lower-priced products to young users.

(3) Turnover rate of fixed assets. It can be seen from the above table that Amazon's fixed asset turnover rate indicator has performed poorly, and has declined year by year, from 8.27 in 2013 to 4.56 in 2017. By analyzing the reasons for the poor performance of Amazon, it can be found that after Amazon acquired Whole Foods, due to the establishment of a large number of warehousing and logistics centers around the world and the purchase of a large number of equipment, its fixed asset turnover rate gradually decreased.

(4) Turnover rate of total assets. Amazon's total asset turnover rate is generally at a declining level, indicating that Amazon's total asset utilization performance is not very good. It may also be affected by this acquisition.

3.2 Operational Synegies

The acquisition of Whole Foods supermarkets not only means an increase in Amazon's source of income, but more importantly, it will collect more than 460 stores and transportation networks in prime locations where Whole Foods supermarkets are located, and let Amazon's series of online attempts floor space. Whole Foods is a leading natural food retailer in the United States, with 447 in the United States, 9 in the UK, and 12 stores in Canada. Whole Foods has 440 frozen warehouses, which can cover 80% of the population in 10 miles. Coupled with retail stores with freezer cabinets, it can reach 95% of Prime users. This means that even without any additional technological progress, just relying on these new distribution points, the operating rate of fresh food delivery can go up several steps. Due to the business model and brand concept of Whole Foods Supermarket, it is still relatively new to the American public, and it only has a small market share in the US market. According to Kantar Retail, less than 9% of U.S. households shop at Whole Foods each month, and 7% of them buy groceries at Whole Foods (0.63% of the total U.S. population). It is worth noting that 76% of Whole Foods customers shop on Amazon, and 12% of Amazon consumers will shop on Whole Foods. That is to say, Whole Foods Supermarket and Amazon's shoppers are highly coincident, and the consumer growth opportunities brought by this acquisition will be geometric.

3.3 Management Synegies

Whole Foods Supermarket is a good operator, but the system and technology investment is insufficient. Amazon knows how to use technology to solve problems. They mastered the technology of space travel, invented the Kindle reader, and deployed cloud computing. Making a grocery store better is not the most difficult problem they have ever encountered. Amazon will use its own technology to optimize Whole Foods supermarkets, such as Amazon Go's automatic checkout technology. In addition, Whole Foods has enriched the existing Amazon grocery categories, injecting new value into the Amazon prime embership system. In the near future, shoppers will be able to purchase Whole Foods items via Amazon voice assistant Alexa and enjoy Amazon Prime Now's 2-hour delivery service. Through a series of synergies generated by the complementary advantages of the two, Amazon can organically combine the three elements of convenience, value, and health to comprehensively improve the shopper experience.

4. Conclusion

Through the analysis of amazon's basic financial data and stock, we find that there are three areas of synergy: financial synergy, operation synergy, and management synergy. First of all, financial synergy shows that after the acquisition is completed, Amazon has more company free cash flow, which reflects the contribution of the acquisition store to the company's cash flow and profit, expanding the scale of corporate assets and enhancing capital strength. Secondly, operation synergy shows that Amazon's acquisition of Whole Foods Supermarket means the acquisition of a large number of offline stores and a developed transportation network. Finally, management synergy shows that Amazon uses its own company's technical advantages to make up for the lack of technology in supermarkets in the city, and fully stimulates the operation advantages of Whole Foods supermarkets. The combination of the two, taking advantage of the shortcomings, makes the operation synergy perform perfectly.

Amazon completed the acquisition of supermarkets in the city from the deployment of offline physical stores to the city's supermarkets, and finally completed the acquisition of Whole Foods on August 28, 2017 for $13.7B. After the acquisition, both sides of the merger and acquisition have shown huge positive performance, meeting the needs of both parties [8]. After Amazon completed the acquisition of Whole Foods, Amazon has more company free cash flow, which shows that the effect of this acquisition on Amazon's cash and profit growth is very considerable; after completing the acquisition of Whole Foods, Amazon also has a large number of stores, expanding the scale of assets and strengthening the strength of the company [9]; after Amazon completed the acquisition of supermarkets in the city, Amazon's stock price also increased significantly, such an amazing growth the speed and huge growth rate show that the market has very high expectations for Amazon's development prospects; after Amazon completed the acquisition of supermarkets in the city, Amazon has mastered the original stores in the city's more than 460 prime locations and developed transportation network , so that a series of Amazon products can have room for landing; after Amazon completes the acquisition of supermarkets in the city, the advanced management mode of supermarkets in the city can be effectively played [10], especially after Amazon has used its own advantages to complete the supermarket After the management technology update.

Until today, the corporate behavior of Amazon's acquisition of Whole Foods has become a topic often mentioned by people in the industry. Based on the price of corporate mergers and acquisitions and the outstanding performance of Amazon and Whole Foods after the merger, no one doubted that this was a successful merger. In addition, for increasingly powerful Chinese companies, especially Chinese e-commerce companies that have performed well in recent years, Amazon’s acquisition of Whole Foods can be said to be a very good lesson. The acquisition and integration of physical stores with fairly excellent locations and transportation methods can provide a higher platform for the development of e-commerce companies. However, whether it can also achieve the financial performance, management synergy and business synergy effects of Amazon in this case study is worth more people to investigate.

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