

Case Study: From Concept to Continuity Amazon.com, Inc. and its Kindle

BACKGROUND

In May 1994, 30-year-old Jeff Bezos was working in Manhattan, exploring the still immature Internet as part of his on-going efforts to uncover promising new business opportunities for D.E. Shaw, a global investment and technology development firm. Bezos learned that Internet usage was growing at a rate of 2,300% per year. Clearly, he thought, there was money to be made on that growing phenomenon. At the time there was very little e-commerce and, in fact, the term then was unknown.

Bezos studied several mail order companies for insights before choosing books. Books already were among the most highly databased items. Most book wholesalers had transferred their catalogs to CD-ROMs. Products organized electronically could readily be sold on-line, Bezos surmised. But his employer wasn't interested in pursuing it, so Bezos left Shaw to start the business himself, selecting Seattle as a base of operations to tap its computer-savvy talent pool.

Amazon grew slowly but steadily in the late 1990s while other Internet companies grew fast and burned out just as quickly, most of them imploding when the dot-com bubble burst. Amazon turned its first profit in the fourth quarter of 2001. Over the years, Amazon expanded beyond books into other categories, including music CDs, DVDs, software, consumer electronics, tools, and more. The company made a brief foray into on-line auctions, but failed to dent the dominance of industry pioneer eBay, and exited the business.

The Kindle

On November 19, 2007, Amazon launched the Kindle e-book reader. The first offering sold out in five-and-a-half hours and the device remained out of stock for five months. The original device featured a six-inch (diagonal) 4-level grayscale display and retailed for \$399. Amazon later lowered the price to \$359. The 250 MB of internal memory in the original Amazon Kindle held approximately 200 non-illustrated titles. By the end of 2008 Amazon claimed its on-line e-book library had grown to 200,000 titles.

In February 2009, Amazon introduced the Kindle 2, with a 16-level grayscale display, improved battery life, 20 percent faster page refreshing, and a text-to-speech option to read the text aloud. Overall thickness was reduced from the original's 0.8 inches to 0.36 inches.

The Kindle 2 has 2 GB of internal memory. Amazon says the Kindle 2 will hold about 1500 non-illustrated books. This model remains available as an alternative to the newer but larger Kindle DX (introduced in May 2009). In July 2009, Amazon reduced the price of the Kindle 2 to \$299. In October, the price was further reduced to \$259.

The Kindle DX (\$489) is the first Kindle model with an accelerometer, automatically rotating pages between landscape and portrait orientations if the device is turned on its side. It has a 4 GB storage capacity, holding approximately 3500 non-illustrated e-books, a 9.7-inch display, and a battery life of up to one week.

Though the company does not release sales numbers, industry analysts estimate that, as of the end of 2009, about 1.5 million devices had been sold. They expect that the company will have

sold about 2.5 million Kindles by the end of 2010. Sales of Amazon e-books overtook sales of print books for first time on Christmas Day 2009.

The Kindle quickly became the sales leader and the standard for e-book readers. The only competitive product with significant sales so far is Barnes & Noble's nook. Reports indicate that Barnes & Noble would sell about 60,000 nook e-book readers by the end of 2009.

It's noteworthy that Amazon introduced the Kindle DX in New York on May 6, 2009, at Pace University. A report in *Business Week* at the time noted that college textbook publishers were a target audience, adding that Amazon had initiated talks with several. An on-line video included a brief interview Amazon's Jay Marine, director of product development, who cited the new model's larger screen as being advantageous for larger format books, such as cookbooks and college science texts.

An attendee at the event, identified as "DMcCunney," reported in a May 6, 2009, blog report on MobileRead.com that Amazon CEO Jeff Bezos introduced the DX at the event. McCunney wrote the following:

Another market Bezos saw as natural for the Kindle was education. He stated that Amazon had agreements in place with textbook publishers Pearson, Cengage Learning, and Wiley, who between them account for 60% of the textbooks published. He announced partnerships between Amazon and five universities – Arizona State University, Case Western Reserve, Princeton University, Reed College, and the Darden School of Business at the University of Virginia – to integrate the Kindle into the learning process.

Bezos introduced Barbara Snyder, president of Case Western Reserve, who said that her university would be conducting a research project on the device involving two groups of students: one group with the DX and the other a control group with conventional texts. Snyder was also quoted in the *Business Week* story, saying, "In the long run, we think students will be able to save money" buying textbooks on the Kindle DX.

THE COMPETITIVE ENVIRONMENT

Though not the first e-book reader on the market, the Kindle captured everyone's imagination and quickly became the market share leader. It now faces growing competition on a number of fronts. The many models of e-book readers vary in features, size and price. Most are incompatible with one another – i.e., an e-book downloaded from Amazon may not be compatible with other devices and vice versa.

Sony — The global electronics titan was the first with an e-book reader in 2006 with its "Reader." Sony has subsequently introduced six different models, with screen sizes ranging between five and six inches, priced from \$199 to \$399. Like the Kindle, it is a dedicated e-book reader using E-ink for maximum battery life. It is more compact and portable than the Kindle, but that portability means a much smaller screen.

Barnes & Noble — Amazon's long-time competitor came late to the Internet and has never really caught up with Amazon in that space. B&N also followed Amazon's lead with its own e-book reader, the "nook," which became available in November 2009. The company, however, had difficulty fulfilling all its pre-Christmas orders. The nook is roughly the same size as the Kindle 2 with comparable features and price, retailing for \$259.

Bookeen — The Cybook from Bookeen is also a dedicated e-book reader, with comparable features and size as the Kindle. It is available in two models, at \$350 and \$450, respectively.

Apple — On January 24, 2010, Apple CEO Steve Jobs introduced the iPad at Apple's annual Macworld conference in San Francisco. The introduction featured Jobs' usual casual flare, accompanied by a splashy multimedia presentation before an audience of fawning acolytes, who cheered each feature as it was presented. Jobs excels at these events, which he has used effectively to introduce new products, including various iterations of the iMac, iPod, and iPhone. A free Podcast of the entire event was available the next day on iTunes, while the iPad headlined the Apple web site's home page – even though the device wouldn't be available for another two months.

More than just an e-book reader, the iPad offers multiple functions that neither the Kindle nor most competitive e-book readers have, including video, email, photos, music (iTunes), some conventional computer applications, a full-sized touch screen keyboard, and the many thousands of “apps” available for the company's iPhone and iPod Touch.

In fact, the iPad is essentially a large version of the iPod Touch, with a touch screen measuring nearly 10 inches diagonally. The iPad also comes with a significantly higher price than the iPod Touch. The base model is \$499 while the fully loaded version is \$829. The iPad is expected to be available by late March. At that time, Apple will also launch its “iBook” on-line bookstore, an equivalent of its iTunes Store, where users will be able to buy and download e-books.

Lenova — In June 2010, Lenova is expected to introduce a \$999 hybrid device called the IdeaPad U1, which splits into two pieces. Combined, the two pieces comprise a full-power laptop with keyboard. The top separates and becomes a color touch screen tablet that can be used for reading e-books and browsing the web.

New Competitive Level

Industry observers say the iPad launch will move the competitive landscape to a new level. In fact, the announcement of the iPad apparently stimulated other players to begin talking about their own potential entries in the tablet market, including Dell, Acer, H-P, Microsoft and Sony. A story in the February 18, 2010, issue of the Wall Street Journal said, “H-P has discussed selling a version of the Slate – similar to the iPad in size and features and including a cellular connection.” It would be priced comparably to the iPad's mid-range model.

Dell, Acer and Sony are reported to be “watching Apple as they refine their own products. And Microsoft has a secretive team working on a two-screen tablet device.” Clearly, the iPad is the new standard in this category, principally for its range of functions.

The central issue may well evolve into a consumer choice between multi-functional devices like the iPad and the IdeaPad U1, or single purpose devices like the Kindle, Reader, Cybook and nook. Apple CEO Steve Jobs says the iPad fills the gap between the MacBook laptop computer and the iPhone. Consumers will confirm that assumption – or not.

Amazon may be inching into iPad's territory, showing interest in touch screen technology. As the New York Times reported on Feb. 3, 2010, “In a sign that Amazon wants to upgrade its Kindle e-reader to compete head-on with the Apple iPad, Amazon has acquired Touchco, a start-up based in New York that specializes in touch-screen technology...”

Another competitive difference is the price of downloadable e-books. Whereas Amazon imposes an across-the-board price of \$9.99 for all e-books it sells, Apple's pricing will give publishers greater leeway to charge what they want.

On the heels of the iPad announcement, publisher Macmillan sought new pricing conditions with Amazon, too. In response, Amazon suspended all Macmillan products – both print books and e-books – but soon relented and announced new pricing policies. The news likely foretells additional challenges to Amazon's two-year dominance of the market.

Significantly, Amazon concluded an open letter to customers on January 31, 2010, regarding the Macmillan situation by saying, "*Kindle is a business for Amazon, and it is also a mission. We never expected it to be easy!*" (Full letter is attached.)

It remains to be seen whether Apple, noted for its design execution and marketing prowess, as well as market dominance with most of its products, will overtake the Kindle with the iPad, or whether their functional differences mean they will co-exist with distinctively different target markets.

Other facts about Kindle

According to ireaderreview.com, Amazon formed Payne LLD, a front company, when Kindle was in its developmental stage to manage contracts and such. Lab 126 is an Amazon-owned company based in Cupertino, CA (also home to Apple), that designed and developed the Kindle and its subsequent iterations. Its web site includes the following vision statement:

We envision wireless electronic reading devices that embrace a traditional book's simplicity, utility, and the ability to disappear as we read, but offer consumers capabilities that are only possible through digital technology and wireless connectivity. Starting with Kindle, which enables consumers to think of a book, newspaper or blog and be reading it in less than a minute, we will build tightly integrated products that bring together great devices, powerful software, Amazon services, and unmatched content selection.

Suppliers include elnk Corporation that makes the Visiplex imaging film used in the Kindle (as well as Sony's Reader). They created the technology and own it. Prime View International, a Chinese manufacturer, makes the screen for the Kindle. Kindle's "brain" is an Intel PXA255 processor. FoxConn, trade name of the Hon Hai Precision Industry Company, is the manufacturer of the Kindle.

FoxConn also makes the iPod and iPhone for Apple, Intel-branded motherboards, the PlayStation 2 and PlayStation 3 for Sony, the Wii for Nintendo, the Xbox 360 for Microsoft, and cell phones for Motorola.

Jay Marine is Amazon's director of product management for the Kindle. Marine holds an MBA from Kellogg School of Management, Northwestern University, and a bachelor's degree from University of Michigan.

Demographics

A study by Mediamark Research & Intelligence (MRI) released in December 2009 provides some useful insights into e-book reader owners.

- 56.3% of e-book reader owners are men.
- Adults aged 35-54 represent the prime demographic. They are 20% more likely to own an e-book reader than any other age group.

- E-book reader owners are 11% more likely than the average adult to own their home and are 87% more likely to have an annual household income of more than \$100k.
- They are 111% more likely than the average adult to have a Bachelor's or post-graduate degree.

Amazon.com, Inc. — Additional background

- Number of employees worldwide — 24,300
- Amazon 2009 sales — \$24.509 billion
- Amazon 2008 sales — \$19.166 billion
 - 1-year sales change — 27.88%
- Market capitalization — \$56.026 billion
- Locations:
 - Headquarters in Seattle
 - Nine software development centers: UK, Ireland, India, South Africa, Romania, Japan, China and US
 - 20 North American fulfillment and warehousing facilities
 - Eight European fulfillment and warehousing facilities
 - Six Asian fulfillment and warehousing facilities

SITUATION

Can Amazon create for itself an enduring success story and identity around the Kindle, on par with what Apple has done with the iPod, iTunes and iPhone? Can Amazon and Kindle do for publishing what Apple and the iPod/iTunes combination did for the music business, and what the iPhone did for smart phones? To do so in the face of growing competitive threats, Amazon's challenge going forward is to sustain and build on its market leadership in the category, and increase its penetration into additional demographic and geographic markets.

You are part of a multi-functional team whose goal is to build on the successful commercialization of Kindle and move forward to bolster and defend its turf against competitors like the nook, iPad and Sony Reader.

In addition to the vice president of Corporate Communications, the multi-functional team will include the vice presidents from Human Resources, Finance, Marketing, Manufacturing, and Design/R&D.

The Socratic panel at the Arthur Page Society meeting will focus on how communications fits in with other functions; what the organization and its functions should deal with in their respective areas to move the organization forward in light of the issues raised in the case. The success of this effort will depend on the promotion and encouragement of a multi-functional environment.

January 31, 2010 Letter from Amazon to its customers:

Dear Customers:

Macmillan, one of the "big six" publishers, has clearly communicated to us that, regardless of our viewpoint, they are committed to switching to an agency model and charging \$12.99 to \$14.99 for e-book versions of bestsellers and most hardcover releases.

We have expressed our strong disagreement and the seriousness of our disagreement by temporarily ceasing the sale of all Macmillan titles. We want you to know that ultimately, however, we will have to capitulate and accept Macmillan's terms because Macmillan has a monopoly over their own titles, and we will want to offer them to you even at prices we believe are needlessly high for e-books. Amazon customers will at that point decide for themselves whether they believe it's reasonable to pay \$14.99 for a bestselling e-book. We don't believe that all of the major publishers will take the same route as Macmillan. And we know for sure that many independent presses and self-published authors will see this as an opportunity to provide attractively priced e-books as an alternative.

Kindle is a business for Amazon, and it is also a mission. We never expected it to be easy!

Thank you for being a customer.

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