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TRANSACTION OR HUMAN CONNECTION?

RETAILERS MUST CHOOSE WHICH SHOPPING EXPERIENCE THEY WILL OFFER.

By Jay Jacobowitz

HEARTS

Ever play hearts? It is an odd card game because there are two ways to win: ending with the fewest, or no points; or winning all the points. Each heart is worth one point. No other card is worth a point, except the queen of spades, which is worth 13.

By winning all 26 points, you “shoot the moon,” but this requires subterfuge. Early on in the play of the hand, you must fool your opponents into thinking you don’t want hearts. So, you moan and groan each time your opponents discard a heart onto your winning trick. Then, in the later stages, when you are holding high cards that can win all the rest of the tricks, your opponents are helpless to stop you.

I think Jeff Bezos is a hearts player, I think he wants to shoot the moon, and the hand he holds is Amazon.

HUNGRY FOR PROFITS

Amazon is most famous for its consumer website offering millions of products, many delivered within a day or two, with over 100 million subscribers worldwide. About 87% of Amazon’s total sales come from these retail, subscription, and advertising services. What is less well known is that most of the company’s profits have always come from Amazon Web Services (AWS)—wholesale cloud storage and computing services to corporations and governments—which make up the other 13% of Amazon’s sales.

According to reporting in the *Wall Street Journal*, after years of focusing on growing retail sales, Amazon executives wanted to boost retail profitability. One way to do that, these retail executives figured: Boost the search results of Amazon’s 10,000 private label products—which are more profitable because Amazon controls the manufacture, distribution, and marketing costs, eliminating the middleman—potentially placing Amazon-brand products’ search ranking ahead of other brands that might be better sellers.

PUTTING PROFIT AHEAD OF CUSTOMERS’ BEST INTERESTS

Historically, when shoppers searched for a product on Amazon, the default sort-filter setting for the secret algorithm that controls the search and ranking functions was “relevance.” To always return the most relevant results first, the algorithm used a product’s leading sales performance to predict likely customer satisfaction, which was a requirement for a high search ranking.

Consumers largely believe that an Amazon search is a neutral function—one that operates purely in their best interests. But in an effort to boost the profitability of its consumer business, Amazon retail executives began asking algorithm programmers to also consider a product’s profitability for Amazon, something the algorithm had never done before in determining customer relevance. This did not sit well with the A9 team (the internal name for Amazon’s algorithm programmers).

AN INTERNAL BATTLE

The programmers felt having profitability compete with what was most relevant to the shopper violated the company’s long standing principle of doing what is best for the customer. A9’s search executives reminded retail executives that Amazon’s first of 14 leadership principles requires managers to focus on earning and keeping customer trust above all, and states in part, “Leaders start with the customer and work backwards.”

A former Amazon search executive said, “We fought tooth and nail with those guys, because of course they wanted preferential treatment in search.” Another revealed, “This was definitely not a popular project. The search engine should look for relevant items, not for more profitable items.” After the *Wall Street Journal* inquired (1), Amazon took down its A9 website, which had for about 15 years proclaimed, “One of A9’s tenets is that relevance is in the eye of the customer and we strive to get the best results for our users.”

THE LAWYERS GET INVOLVED

Amazon’s lawyers warned against directly adding Amazon’s profit-per-product to the search algorithm, reminding executives of the multibillion dollar fine European regulators had levied against Alphabet Inc.’s Google for favoring Google’s preferred products in its comparison-shopping service.

To satisfy the lawyers, Amazon’s A9 engineers instead began testing other product variables (such as weight and dimensions, we imagine) that indirectly affect profits, to see which ones improved profitability. Because the new variables were only indirectly linked to profitability, a bystander unaware of this connection might not be able to tell.

An internal committee that reviews and approves all additions to the algorithm—which includes hundreds of variables—rejected some newly proposed variables that returned a lower score on the new profitability metric, according to people who worked on the project. As one person put it, the new variables were essentially “proxies” for profit. “You are making an incentive system for engineers to build features that directly or indirectly improve profitability,” the person said. “And that’s not a good thing.”

Amazon told the *Journal* it sometimes adds variables that hurt profitability, such as boosting discoverability of products that can be delivered the same day. And in an email, Amazon spokeswoman Angie Newman said, “We have not changed the criteria we use to rank search results to include profitability.”

DEFAULT SORT-FILTER NOW “FEATURED,” NOT “RELEVANCE”

Although Chief Executive Jeff Bezos is famous throughout the company for his “customer obsession” mantra, the CEO’s apparent approval of the algorithm change suggests shifting priorities. After years of operating independently from retail operations, which are in Seattle, and reporting to its own Silicon Valley CEO in Palo Alto, Calif., the A9 search team now reports to Senior Vice President North America Consumer, Doug Herrington, and to Amazon Worldwide Consumer CEO, Jeff Wilke, essentially making search answerable to retail.

Last summer, without publicizing the change, Amazon replaced the default sort-filter option on its website to “featured” instead of the long-time default option, “relevance.” Users who wish instead to sort by relevance will not be able to find it as an option in the drop-down menu at the top right of the page.

OTHER VOICES

Any change to Amazon’s search algorithm can impact the ranking of third-party companies that sell through Amazon and, according to marketing analytics firm Jumpshot, Amazon’s search bar is the most common way U.S. shoppers find items online.

In the comments section of the *Journal* article, a subscriber to the newspaper stated:

“Amazon uses its site to identify high moving high profit items that they can buy and put in their warehouses. I used to sell on Amazon and I sold over \$2,000,000 per year. A few years ago I realized Amazon had the same product I had and was selling for less than me. I lowered the price and they lowered their price within an hour. I lowered my price again and they then took my product off and sent me a very nice e-mail saying they wanted to let me know that I might be losing money on this product. They put my product back on, but they lowered their price below mine, at which time I did lose money. Over time, I realized they were doing that to a lot of my products. I’m sure they were doing it to other sellers as well.”

JEFF BEZOS BELIEVES IN BRICKS-AND-MORTAR

Amazon is aggressively increasing its bricks-and-mortar retail presence under several banners including Amazon Books, Amazon 4-Star, Amazon Go, Presented by Amazon, and of course, Whole Foods. Altogether, store count is pushing 600 units, made up mostly by nearly 500 Whole Foods stores. But the company has announced plans to dramatically increase Amazon Go, the company's cashierless small footprint convenience play, to 3,000 units by 2021.

POLAR OPPOSITE BUSINESS MODELS

Amazon Go is arguably the polar opposite business model of Whole Foods. Whole Foods traditionally offered a large-store, high-touch, sensory-rich shopping experience, with cheesemongers, wine sommeliers, and expert butchers all available to offer advice and tailor purchases to individual customer needs. Amazon Go is a small-store, no-touch, technology-driven, prepackaged grab-and-go shop, designed for quick in-and-out transactions with zero human contact.

In September, Amazon announced it was cutting health insurance benefits to about 1,900 Whole Foods part-time employees who work at least 20 hours per week. Whole Foods executives told *Business Insider* the company was making the change “to better meet the needs of our business and create a more equitable and efficient scheduling model.”

This is no surprise. Ever since Amazon took over Whole Foods in 2017, the conflicting business models pitted Amazon's efficiency against Whole Foods social consciousness. Remember, Whole Foods CEO John Mackey wrote a best-selling book about why companies should have a social conscience, while Amazon corporate principles say good leaders, “do not compromise for the sake of social cohesion.”

The comparatively slim benefits packages for most of the nearly 650,000 Amazon employees were ultimately always going to determine what the benefits looked like at Whole Foods. There is no way Amazon could risk having the super generous health care benefits of 1,900 part-timers at Whole Foods infect the entire Amazon workforce. Too expensive!

INSPIRATIONAL SHOPPING

Will Amazon's efficiency-first business model eliminate the high-touch, human-interaction-rich shopping experience? For insight into the answer, Trader Joe's former national president, Doug Rauch, spoke with *The Shelby Report* in July (2).

Rauch said, “I think, yes, online is a challenge to every retailer that isn't clear as to what their purpose is and how they can differentiate themselves from a transactional experience. Trader Joe's is famous for their staff, their crew members, as they call them, and making sure they deliver a customer experience that is warm, friendly, knowledgeable. So, in theory, whenever someone walks out, they feel a little better than when they walked in. That, I think, is a winning formula for any brick-and-mortar—to make sure you have a reason why they should go there. Because if you don't, they won't.

Trader Joe's, Rauch told *The Shelby Report*, has long recognized that their relationship with the customer is more than just a transactional relationship. “It is one where you really form bonds around values,” he said. “It's not just the value you're getting by saving so many cents, but it's the values you represent.” You want your customers to feel well treated, understood and aligned with your brand—and that type of relationship, Rauch said, can't be formed simply through a transaction.

It's also generally not the kind of relationship that can be achieved online, Rauch noted, pointing to our desire for human connection. “I think the story is there's a great opportunity for retail to step into and create that place where people can feel validated, they can feel seen, they can socialize, they can get things they can't get on the internet, which is primarily a human experience. Retail anchors a human experience.”

SHOOT THE MOON?

Does Jeff Bezos, hearts player, hold the queen of spades in his hand? In 2012, Bezos applied for a U.S. patent on anti-showrooming technology that would defeat online search from mobile or other internet-connected devices located inside bricks-and-mortar stores.

The patent, called “Physical Store Online Shopping Control,” enables a physical retailer's Wi-Fi network to intercept search queries related to price comparisons, and respond in any one of several ways including:

offer a matching price, provide a coupon, suggest complementary items, or alert a salesperson—or virtual assistant—to assist the shopper, among other things, including blocking the request altogether, preventing an in-store shopper from checking prices at all. The patent includes the ability to collect historical information on customer purchases.

Coincidentally, in June of 2017, in the interim between Amazon’s April offer to buy Whole Foods and the deal closing in August, the U.S. granted Amazon’s patent. So, let’s see, Amazon now holds the license on technology that other retailers could have used to keep their shoppers from comparing prices online, and at the same time can deploy that anti-showrooming technology in any of Amazon’s stores.

WHY MISSION MATTERS

Costco, the big-box discounter, has a single, founding principle: sell at cost. Its net profit equals, but does not exceed, the annual membership fee it charges customers to shop, working out to about two percent of sales. Discussing the competition, management likes to say Costco wants to be the first to lower prices, and the last to raise them. Were Costco to decide to make more profit, it would abandon its one founding principle, damaging customer trust in the process.

Amazon has 14 leadership principles, and CEO Bezos reportedly has his customer obsession mantra. But are 14 principles, plus a mantra, as sturdy as a single mission? The recent shift in search function to emphasize profitability breaks at least one of Amazon’s principles: earning and keeping customer trust above all. And Bezos’s customer obsession mantra appears not to rise to mission level. So what is Amazon’s mission? We don’t know. Will customers notice or care? Time will tell. **JJ**

References:

- 1) “Amazon Changed Search Algorithm in Ways That Boost Its Own Products”
“<https://www.wsj.com/articles/amazon-changed-search-algorithm-in-ways-that-boost-its-own-products-11568645345> Posted 9/16/19; Accessed 9/27/19
- 2) “Former Trader Joe’s President Shares Views On Today’s Grocery Business” by Treva Bennett;
www.theshelbyreport.com/2019/08/26/former-trader-joes-president-shares-views/. Posted 8/26/19; Accessed 9/27/19

EPILOGUE: A LITTLE BIT OF CONVENIENCE

In late September, Amazon announced “an array of new programs, devices, and features that make it easier than ever for customers to find, setup, and enjoy connected devices in their homes.” The new program, dubbed Certified for Humans, will work seamlessly with Amazon’s voice assistant, Alexa, and with Echo, accessing home Wi-Fi systems, Amazon Smart Oven, and Alexa Guard, to help automate large pieces of household chores, like reordering products, and control home safety and security. You can even have Amazon earbuds and, by invitation-only on an experimental basis, Amazon eyeglasses and a finger ring.

Recent revelations that Apple’s Siri device eavesdropped on millions of users; Google’s YouTube fined \$170 million for illegally collecting kids’ personal information; and Amazon itself in June sued for Alexa illegally recording children’s conversations without their consent, suggest that placing our unconditional trust in technology companies to always do the right thing may not be the wisest choice. To borrow from Benjamin Franklin’s warning about sacrificing liberty for safety: Those who would give up essential Privacy, to purchase a little temporary Convenience, deserve neither Privacy nor Convenience. **JJ**