The Early Stages Of A Retail Revolution

Two stories in this issue about Amazon.com bring news that will simultaneously cheer and concern independent retailers. Let's deal with the concerns first. The online giant abruptly bumped up the sales commission fees it charges to third-party retailers listing products on its site, to 15% from 12%. The move has made Amazon a less attractive e-commerce platform, but more significantly, it signals Amazon's intent to aggressively pursue the music and audio market itself, rather than outsourcing it to other retailers. Spokesmen from the company didn't respond to requests for clarification, but financial analysts who follow Amazon say the current move is consistent with long-term company strategy.

Starting a decade ago, Amazon began inviting thousands of specialty retailers to list products on its site as "affiliates." The move helped increase traffic to the Amazon site, made the retailer into a one-stop shop for everything, and produced a nice stream of free cash flow in the process. (Some plausibly make the case that revenues from Amazon's "referral fees" are greater than its net profit.) The affiliate program also allowed Amazon to monitor sales rates, inventory turns, and margins on thousands of different products. Now it would appear that Amazon has begun targeting those products where it can be effective, such as m.i. gear, and has begun stocking and selling them in earnest. Expect the competitive landscape to become even more crowded.

On the positive side, however, Amazon has come out in favor of the Marketplace Fairness bill, a bi-partisan piece of legislation that would enable states to collect sales tax on online purchases. Why would the world's biggest online retailer support a law that sacrifices a key pricing advantage and "levels the playing field" with brick-and-mortar competitors? Amazon spokesman Scott Stanzel says cryptically that "the debate has progressed and it has matured." Another explanation might be that as the retailer has expanded its network of distribution centers, it has established a physical presence in more states, and thus has become liable for collecting sales tax. After opening a massive new facility in Texas last month, the company agreed to collect the Lone Star State's 6.25% sales tax. Similar agreements have been inked in seven other states, and it looks like by year end Amazon will collect sales tax in ten states, including the major population centers of California and New York. Apparently, they figure they will eventually have to pay the tax, so they might as well help shape the laws.

Mike Mazerov, a senior fellow at the Center on Budget and Policy Priorities, speculates that Amazon's deals to collect sales tax will improve the prospects of a national sales tax collection bill. "When you have more consumers understanding that these taxes are due, it increases the momentum for a federal bill that applies to most, if not all, online retailers." So, somewhat ironically, as Amazon gears up to compete in the m.i. market, it is also helping to pass the legislation that independent retailers have been clamoring for for decades: laws that compel online retailers to collect and remit local sales taxes.

In 2000, five years after Amazon opened for business, and a year before it would turn its first profit, the "dot.com" bubble burst. We weren't perceptive enough at the time to predict that the retailer would grow into a $48 billion juggernaut. Thus, we hesitate now to speculate on the long-term ramifications of either pending sales tax legislation or Amazon's push into the m.i. market. Political experts predict that the sales tax legislation will eventually pass, and we would conjecture that higher costs will drive retailers away from Amazon's e-commerce platform. However, the fact that we're writing an editorial on the implications of a Seattle-based internet company reflects just how much the market has changed.

When Henry Ford brought cars to the masses in 1908 with the Model T, people marveled at his brilliant design and his ingenious application of mass production techniques. It took another five decades to fully appreciate how his invention would transform the way we live, shop, and work. The mobility provided by the car prompted the migration to the suburbs, single family housing, the rise of shopping centers, and the creation of the supermarket, to cite just a few effects. The car was also the final nail in the coffin for many once large and prosperous downtown music stores, including Lyon & Healy in Chicago, Grinnell Brothers in Detroit, and Whittle Music in Dallas. These industry leaders were eventually done in by suburban competitors.

We suspect that the internet is in the early stages of a similarly profound transformation, one filled with opportunities and peril. George Hines, president of George's Music sums it up best when he says we are in the midst of a "retail revolution," and the "primary challenge of the day is figuring out how to profitably integrate bricks and mortar and the internet." It is a major challenge, but as our columns have demonstrated, the story of retailing has been one of perpetual upheaval. This is just the latest chapter.

Brian T. Majeski
Editor
brian@musictrades.com