

# Amazon.com (AMZN) Q2 2016 Results - Earnings Call Transcript

Jul. 28, 2016 10:43 PM ET | **Amazon.com, Inc. (AMZN)** | 11 Comments

## Q2: 2016-07-28 Earnings Summary

Slides

10-Q

10-Q

EPS of \$1.78 **beats by \$0.66** | Revenue of \$30.40B (31.14% Y/Y) **beats by \$852.03M**

Amazon.com, Inc. (NASDAQ:[AMZN](#)) Q2 2016 Earnings Call July 28, 2016 5:30 PM ET

### Executives

Darin Manney - Director, Head of Investor Relations, Amazon

Brian T. Olsavsky - Senior Vice President and Chief Financial Officer

### Analysts

Mark A. May - Citigroup Global Markets, Inc. (Broker)

Douglas T. Anmuth - JPMorgan Securities LLC

Gene Munster - Piper Jaffray & Co.

Heath Terry - Goldman Sachs & Co.

Carlos Kirjner-Neto - Sanford C. Bernstein & Co. LLC

Brian Nowak - Morgan Stanley & Co. LLC

Mark Mahaney - RBC Capital Markets LLC

Youssef Squali - Cantor Fitzgerald Securities

Ray McDonough - Oppenheimer & Co., Inc. (Broker)

Colin A. Sebastian - Robert W. Baird & Co., Inc. (Broker)

Brian J. Pitz - Jefferies LLC

Justin Post - Merrill Lynch, Pierce, Fenner & Smith, Inc.

Ross Sandler - Deutsche Bank Securities, Inc.

Eric J. Sheridan - UBS Securities LLC

Victor Anthony - Axiom Capital Management, Inc.

## **Operator**

Good day, everyone, and welcome to the Amazon.com Q2 2016 Financial Results Teleconference. At this time, all participants are in a listen-only mode. After the presentation, we will conduct a question-and-answer session. Today's call is being recorded.

For opening remarks, I will be turning the call over to the Director of Investor Relations, Darin Manney. Please go ahead.

## **Darin Manney - Director, Head of Investor Relations, Amazon**

Hello, and welcome to our Q2 2016 financial results conference call. Joining us today is Brian Olsavsky, our CFO. We'll be available for questions after our prepared remarks.

The following discussion and the responses to your questions reflect management's views as of today, July 28, 2016 only, and will include forward-looking statements. Actual results may differ materially. Additional information about factors that could potentially impact our financial results is included in today's press release and our filings with the SEC, including our most recent annual report on Form 10-K and subsequent filings.

As you listen to today's conference call, we encourage you to have our press release in front of you, which includes our financial results, as well as metrics and commentary on the quarter. During this call, we will discuss certain non-GAAP financial measures. In our press release, slides accompanying this webcast and our filings with the SEC, each of which is posted on our IR website, you will find additional disclosures regarding these non-GAAP measures, including reconciliations of these measures with comparable GAAP measures. Please note, unless otherwise stated, all comparisons in this call will be against our results for the comparable period of 2015.

Now I'll turn the call over to Brian.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Thanks, Darin. I'll begin with comments on our second quarter financial results. Trailing 12-month operating cash flow increased 42% to \$12.7 billion. Trailing 12-month free cash flow increased to \$7.3 billion, up from \$4.4 billion. Trailing 12-month free cash flow less lease principal repayments increased to \$3.9 billion, up from \$2.4 billion. Trailing 12-month free cash flow less finance lease principal repayments and assets acquired under capital leases increased to \$2.5 billion, up from an outflow of \$492 million. Worldwide revenue increased 31% to \$30.4 billion or 30%, excluding the \$166 million favorable impact from year-over-year changes in foreign exchange. Worldwide paid unit growth was 28%. Worldwide seller units represented 49% of paid units.

Now I'll talk about our segment results. North America revenue grew 28% to \$17.7 billion. North America operating income was \$702 million, a 4% operating margin compared with \$348 million in the prior year. This includes \$5 million of favorable impact from foreign exchange. International revenue grew 30% to \$9.8 billion. Excluding the \$184 million year-over-year favorable foreign exchange impact, revenue growth was 28%.

International operating loss was \$135 million compared with the loss of \$189 million in the prior year. This includes \$40 million of favorable impact from foreign exchange.

Amazon Web Services' revenue grew 58% to \$2.9 billion. Amazon Web Services' operating income was \$718 million, a 24.9% operating margin compared with \$305 million in the prior year.

Our operating income was \$1.3 billion or 4.2% of revenue, up approximately 220 basis points year-over-year. This includes \$45 million of favorable impact from foreign exchange. Net income was \$857 million or \$1.78 per diluted share compared with a net income of \$92 million or \$0.19 per diluted share.

I'll conclude my portion of today's call with guidance. For Q3 2016, we expect net sales of between \$31 billion and \$33.5 billion or growth of between 22% and 32%. This guidance anticipates approximately 30 basis points of favorable impact from foreign exchange rates.

Operating income to be between \$50 million and \$650 million compared with \$406 million in third quarter 2015. We're grateful to our customers and remain heads-down focused on driving a better customer experience. We believe putting customers first is the only reliable way to create lasting value for shareholders. Thanks.

And with that, I'll hand it back to Darin.

### **Darin Manney - Director, Head of Investor Relations, Amazon**

Thank you, Brian. Before we move to questions, I need to remind you that our guidance incorporates the order trends that we've seen to date and what we believe to be appropriate assumption. Our results are inherently unpredictable and may be materially affected many factors, including fluctuations in foreign exchange rates, changes in global economic conditions and customer spending, world events, the rate of growth of the Internet, online commerce and cloud services and the various factors detailed in our filings with the SEC.

Our guidance also assumes that we don't conclude any additional business acquisitions, investments, restructurings or legal settlements and that foreign exchange rates remain approximately where they have been recently. It is not possible to accurately predict demand for our goods and services and, therefore, our actual results could differ materially from our guidance.

With that, let's move to the Q&A portion of the call. Operator, please remind our listeners how to initiate a question.

### **Question-and-Answer Session**

#### **Operator**

At this time, we will now open the call up for questions. In the interest of time, we ask that you limit yourself to one question. [Operation Instructions] Thank you. Our first question is from Mark May of Citi. Please proceed.

**Mark A. May - Citigroup Global Markets, Inc. (Broker)**

Thanks for taking my question. We've noticed some data points out there that suggest that you're kind of accelerating your build-out of fulfillment capacity in North America and obviously also in India. Can you give us a sense of what sort of impact that, that might have in the near to mid-term on your CapEx, depreciation and ultimately CSOI, especially as it relates to your Q3 guidance? And then just kind of a maintenance question, how much is FX impacting your Q3 guidance? Thanks.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Okay. Thanks, Mark. Yeah, let me talk a little bit about guidance and I'll incorporate the answer to the fulfillment question. So, you'll notice on the top line guidance of \$31 billion to \$33.5 billion or 22% to 32% growth incorporates the Prime Day results and I can talk more about that later. But Prime Day was very successful for us. It was up 60% on a worldwide basis over the prior year, and it was also a record day for our Amazon devices, as well as sellers and customers alike.

In the bottom line, you'll need to remember that Q3 is a typically a lower operating income quarter as we prepare for Q4, the holiday peak. It's a little bit more exaggerated this year in that we're opening 18 fulfillment centers this quarter. To put that in perspective, we launched six in Q3 of last year. This will bring us up to 21 net FCs for the year by the end of Q3 and that compares with 10 fulfillment centers for the first three quarters of last year on a net basis. So, why are we expanding so much? If you remember back to Q4 and the capacity constraints we had in Q4, primarily due to really strong FBA growth, we talked a lot in the Q4 call about the operational cost of that in Q4. Customers well taken care of, but we had additional fulfillment costs from being so tight on capacity.

This year, with that in mind and then knowing that our growth rate is actually accelerating on a unit basis, we are – Q2 was 28% unit growth for paid units, but fulfilled by – units Fulfilled by Amazon is much higher than that due to the growth of Prime and FBA. That compares with last year in Q2 when we saw 22% unit growth, so we're 600 basis points faster growth in Q2 this year than last year and that 22% last year turned into 26% in Q4. So it ramped up in the back end of the year.

So a lot of data points there, but the bottom line is that there's a large step up in the amount of fulfillment capacity in Q2 – excuse me, Q3 versus Q2. There's a couple of other factors while I'm at it for guidance. We are also nearly doubling our content spend in the second half of this year versus the second half of 2015. We have a great slate of new Amazon Originals coming out later this year, both in the U.S. and internationally. And we're nearly tripling our number of new Amazon Original shows – TV shows and movies compared with the second half of last year.

There are other investments certainly that are increasing sequentially. I'd point to India and AWS, but primarily the two biggest issues in Q3 guidance I would say are the operational ramp and also the increase in digital content spend.

**Darin Manney - Director, Head of Investor Relations, Amazon**

And, Mark, to follow up on the other question, our net sales guidance anticipates approximately 30 basis points of favorable impact from foreign exchange rates.

**Mark A. May - Citigroup Global Markets, Inc. (Broker)**

And, Brian, where does that bring your video content spend to with the doubling in the second half if we look at it on an annualized basis?

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

We're not disclosing that at this time.

**Mark A. May - Citigroup Global Markets, Inc. (Broker)**

Thanks.

**Operator**

Our next question comes from Douglas Anmuth from JPMorgan. Please state your question.

**Douglas T. Anmuth - JPMorgan Securities LLC**

Thanks for taking the questions. I just want to go back to Prime Day for a minute. I didn't hear any commentary around new Prime members in particular. Obviously a lot of other metrics that you gave but hoping you could provide a little bit more color around that. And then also, is there anything else that kind of stood out in terms of what you learned around operations and systems ahead of the holiday season? And then just going back to the 3Q guide, what's the right way for us to think about stock-based comp in the third quarter? And if we looked at your 2Q numbers, is that kind of a fair assumption for what you're thinking about? Thanks.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Sure. Let me circle back on Prime Day. So again, it was the biggest global day ever for Amazon and was up 60% on a order product sales basis versus Prime Day 2015. It was a record day for Amazon devices. It was a great day for small businesses and sellers who saw great year-over improvement in their sales. And more importantly, it was a great day for customers. Globally they saved over double what they had saved in Prime Day 2015. So we're very pleased with the results of Prime Day, and the impact of Prime Day is factored into this guidance. As far as new customers and new Prime members, we're not disclosing that, but suffice to say that it was a great day for both existing Prime members and also new customers who were trying us out for the first time.

**Darin Manney - Director, Head of Investor Relations, Amazon**

And on the stock-based compensation, you'll recall beginning in Q1 this year, we began allocating stock-based compensation and other operating expense to our North America, international and AWS segments. So we're including that in our guidance on operating income and have not separately guided to stock-based comp and other income expense this quarter.

**Operator**

Our next question comes from Gene Munster from Piper Jaffray.

**Gene Munster - Piper Jaffray & Co.**

Hey. Good afternoon. First, love the conference call format here. Get right to it. In terms of questions, the customer count, can you give us a little bit of guidance on that? And then also talk about the theme of automated consumption and separately, the importance of Prime Now and how you can kind of grow those SKUs. Thanks.

**Darin Manney - Director, Head of Investor Relations, Amazon**

Hi, Gene. This is Darin. I'll start with the customer accounts. As we noted again in our Q1 release, our active customer accounts exceeded 300 million. However, today we're not going to update that number.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

To your question on Prime Now, so I will point out Prime Now is now in more than 40 metro areas worldwide. In the past quarter we expanded further internationally to Germany, Spain and France, so it's a global program, again, offering free two-hour delivery on tens of thousands of items. We also have in the same vein of, I think what you called maybe automated consumption, the same day has expanded. Now we've added 11 metro areas, bringing the total to 27 metro areas that are qualified for same day. So, yeah, we think this is an important part of our Prime offering. We know customers love it. We're very happy with their order patterns from Prime Now, and very happy with it. Of course, we do always talk about – we always usually get asked about profitability and it is a very hard service to deliver and make money on, but we know customers love it and we're in a great position to do this because of our long-term approach, our drive of greater efficiencies and our proximity to the customer with our vast global FC network.

**Operator**

Our next question comes from Heath Terry from Goldman Sachs.

**Heath Terry - Goldman Sachs & Co.**

Great. Thanks. I was wondering as it relates to the Q3 guidance, can you give us a bit of a sense of just how we should think about margins in the AWS business, especially as the next eight availability zones roll out? Presumably that kind of increase in capacity likely has an impact on margins, but would appreciate sort of any direction you can share on how to think about that.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Sure. We don't give – obviously we don't give segment-based guidance. But to your question about AWS, we actually see nine availability zones in four regions coming out in the next – in the coming year. The impact on short-term is pretty much indistinguishable from the growth that we're seeing in our expansion of our base customers in our existing regions, so we don't see a large step-up from the addition of new regions relative to the large and rapid growth in the business itself.



We do think that it does pay benefits both for ourselves and for our customers because of the expansion, and we're happy to have added the region in Mumbai this past quarter. We think when we expand geographically, existing customers will run more of their workloads on AWS. Sometimes they have local latency concerns or security issues that require them to run things in their country, so that helps. And we also open up to new customers when we add these regions. So not a large impact on Q3 guidance, but certainly an exciting investment for our customer base.

## **Operator**

Our next question comes from Carlos Kirjner with Bernstein.

## **Carlos Kirjner-Neto - Sanford C. Bernstein & Co. LLC**

Thank you. Two questions if I may. As I look at your tech and content expense as a percentage of revenues, we see year-on-year decline for the last two quarters, which is something we hadn't seen since mid-2010, and of course it's reflected in the AWS margins. Can you help us understand what has driven this significant change in relative trajectory in tech and content expenses? And the second question is, why is it that the rate at which you are deploying Prime Now is so much greater or faster than the rate at which you are deploying Fresh? What's different between them and how is it that you are deploying Fresh in new markets but not as fast as Prime Now, and what drives the difference? Thank you.

## **Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Sure. On tech and content, that's going to be a combination of our people cost related to many areas of the website and also the infrastructure cost to run it, at both the Amazon Web Services and also the Amazon site. We've been seeing some great efficiencies in our infrastructure, both internally as Amazon and also as part of AWS. We have great people working on not only better efficiency, but also driving cost out of our acquisition prices. So, there's a lot of great work going on there and I think that's what you're seeing reflected in the tech and content line. Again, this can fluctuate quarter-to-quarter, but we're happy with the current trend and you see it in the AWS margins.

On Prime Now versus Fresh, they are separate – sorry. The – we'll point out in Q2 that we added London and Boston as two new sites in London for AmazonFresh, and that was the first international location. But we've been running AmazonFresh for seven years, or excuse me, since 2007 in Seattle and what you've seen as we've been testing the model, we've been expanding in North America and more so we've been expanding within the cities that we're in, adding zip codes, adding additional customers. So, the move into Boston and also now into London give us some really good data points and as – it's a great customer feature for the Prime offering.

Prime Now is a little bit easier to build up from scratch, I would say. The – it has a different purpose, although some of the products overlap. Again, this is more about immediacy of one-hour and two-hour delivery of a curated list of important products that people need in a short period of time. So, they have different roles. Some of the products overlap, of course, but we're happy with both, and we think that customers like both of them.

## **Operator**

Our next question is from Brian Nowak from Morgan Stanley.

## **Brian Nowak - Morgan Stanley & Co. LLC**

Thanks for taking my questions. I have two. The first one is on the Echo. Anything you could share at all on some of the most commonly used searches? How are consumers using the Echo as of now most commonly? And then anything on uplift in purchase behavior from Echo households? And the second one on Prime, on AWS margins, can you just walk us through some of the puts and takes that have been driving the AWS margin expansion we've seen in the first half of this year? Is it utilization, product mixes? What's been driving the margin expansion? Thanks.

## **Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Sure. Well, in Echo, again, we continue to build out the list of devices, launching the Dot and Tab and Fire TV skills this past year. And now we have 1,900 third-party skills for the Alexa, including new skills from Kayak, Lyft, NBC, Honeywell and more. So there's a lot of uses that we're seeing for Echo. A lot ties into our Prime Music offering. It's just a great way to access Prime Music and more and more the Amazon site. We don't have anything to disclose on physical orders from – through – excuse me, orders through Echo.

On Amazon Web Services margin, again, this is primarily due to efficiencies gained on our infrastructure, better utilization, better cost out. There is a – certainly a mix of products and services. I don't have a bridge for you on whether that's helpful or hurtful, but the – these margins in AWS will fluctuate from quarter-to-quarter, and that's what you're seeing. But we're very happy with the year-over-year improvement.

## **Operator**

Next question is from Mark Mahaney from RBC Capital Markets.

## **Mark Mahaney - RBC Capital Markets LLC**

Okay. Hey, Brian, could you give us some wise as to the revenue growth acceleration that you're seeing, a little more color about the revenue growth acceleration in North American retail and in international retail? I remember last quarter you called out really starting to see, kind of I don't know, critical mass tipping point, whatever the buzzword is, from Prime and from FBA in international markets. Is that what's continuing, I assume, to kind of drive that re-acceleration? And any geographic country comments behind that? Thanks a lot.

## **Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Sure. Yeah, I have the same buzzwords for you, Mark. It's really the flywheel of Prime is definitely working. It's simple as that. The low prices, vast selection and convenience continue to resonate with customers. Prime membership increases and selection through FBA makes Prime more valuable. So it's a bit as simple as that in the consumer business in North America and international, we are seeing great acceptance of Prime and usage of Prime benefits. We continue to expand the list of Prime benefits for customers to make it more valuable, and none is more valuable than FBA, which we've talked a lot about the value of Prime to FBA and vice-versa.

FBA is bringing more Prime-eligible selection to Prime and then the growth of Prime and the type of customers that utilize Prime and their buying behavior is a great traction for other FBA sellers. So that is essentially what we're seeing, and we're certainly pleased with the customer response to those offers globally.

## **Operator**

Our next question comes from Youssef Squali from Cantor Fitzgerald.

## **Youssef Squali - Cantor Fitzgerald Securities**

Thank you. Two questions, please. Brian, your operating income has been come in stronger than expectations, but more importantly, stronger than your own guidance, at least in the last couple of quarters. I was just wondering as you look back at where you guided relative to actual, where do you think that delta was most pronounced? Why wouldn't we assume that maybe, at least on the margin, the investment intensity in the business has maybe decelerated a bit?

And second, on Prime Video, just was wondering, considering what the main competitor there is doing, i.e., expanding aggressively around the world, you guys have been growing in a more measured manner, is that still the plan or are you guys interested in maybe instead of moving into a few countries, kind of expand globally in one fell swoop? That's it. Thanks.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Sure. Let me start with the second question first. So on Prime Video, again we're very happy with the customer adoption of Prime Video, and we know the customers love it. We like the results that we see, particularly with the free trial conversion, the renewal rates for subscriptions. So it's clearly working. I mentioned earlier how we're doubling the investment rate in the second half of the year versus last year's second half, and we're tripling the Amazon Originals content.

That Originals content for TV and movies, that content can be used globally. We've talked a bit about our Prime launch in India, and alluded to the fact that we'll be having video soon in India, but local content and also Amazon Originals. So, stay tuned for that. I don't have any more to announce on that today. On the variance to guidance, what I'll say is, we came in the very high end of our revenue guidance. I would say that our business model usually reacts well to high volume as we get a really good leverage on our fixed expenses. So that's part of what we saw, very strong operating efficiencies as we hit essentially the highest end of our revenue guidance.

But we do have a lot of diverse profit streams here at Amazon and a lot of investments going on at any point in time. I think I heard a question there about level of investment. We continue to invest heavily. In fact, I just called out a few things that are going to be stepping up in investment levels in Q3, mostly ops and digital content. So we continue to invest on behalf of customers. But we also work very hard at efficiencies and scaling the businesses that we have. So we take both roles very seriously around here, investing on the right – in the right things, seeing results on behalf of customers, and also driving efficiencies. And there can be timing, quarter-to-quarter, the operating margin and levels of investment can fluctuate, but certainly continue to expand.

## **Operator**

Our next question comes from Jason Helfstein from Oppenheimer. Mr. Helfstein, your line is live.

## **Ray McDonough - Oppenheimer & Co., Inc. (Broker)**

Hi. Sorry about that. This is Ray McDonough on for Jason Helfstein. Just on the AWS side, we've been hearing a lot of talk and especially a lot of media reports that larger customers tend to use AWS, they might use Google and Microsoft Azure in tandem in sort of a multi-cloud kind of architecture. Just wondering your thoughts on how you see AWS fitting in the overall ecosystem and kind of your place longer term in the ecosystem.

## **Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Sure. Well, first of all, we believe customers will choose AWS primarily for three factors, the functionality and pace of innovation that we bring to the table, our partner and customer ecosystem and our experience. We've been in this business longer than anyone. Having said that, there are room – there's plenty of room for multiple vendors in this business. What we focus on is innovating on behalf of customers and expanding the geographic footprint to make our services more widely available.

You can see us continue to invest in things like new application services, higher up the stack, additional technologies that will make integrating with AWS seamless for those companies that have a hybrid IT environment and then continuing to add functionality for data analytics, mobile, Internet of things, machine learning offerings, things like that, that will add greater and greater value for AWS customers. And I would say the rapid pace of innovation continues to stretch our lead in that dimension. We have had 422 new significant services and features added in the first half of this year. That's a faster pace than last year when we added 722 services and features. So we feel good about the business position we're in and our position with customers.

## **Operator**

Our next question comes from Colin Sebastian from Robert W. Baird.

### **Colin A. Sebastian - Robert W. Baird & Co., Inc. (Broker)**

Okay. Thanks, guys. As another follow up on the margins, I was hoping you could comment on any impact from the investments and build out of enhanced transportation capabilities including the air cargo leases. And then secondly, was hoping you could identify any categories within EGM that are becoming more meaningful drivers of growth or at least are an increasing focus on the retail side? Thank you.

### **Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Yeah, sure. First, on EGM, I'll just say the growth is across a lot of different products, none to exactly call out here, and we think that a lot of it is, of course, driven by the growth of Prime itself. EGM in North America grew 32%, which was higher than the revenue growth rate, and also grew 36% internationally. So when people join Prime, they are certainly buying EGM in strong quantity. So that continues to grow with the growth of the Prime program.

On transportation, I think your question was about whether that's impacting our short-term results. No. The answer is no. We are certainly expanding our service offerings in the transportation side and we have been for many years, things like sortation centers and delivery methods. The plane deal that we were talking about is essentially planes that we're going to be leasing from other companies, and you'll hear more about that as we go forward, but that is to essentially take on the demand for internal flights as we move product around. It certainly will be well utilized.

## **Operator**

Our next question comes from Brian Pitz from Jefferies.

**Brian J. Pitz - Jefferies LLC**

Thanks for the questions. First, on FC build out, is the cost of building centers scaling over time given the use of Kiva, other technologies or general learnings, or are those costs still relatively consistent? And also, we noticed some device sellout in the next four to five weeks, post-Prime Day. Was this a bit of a planned inventory reduction for some of the devices or did volumes take you by surprise here?

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

I will start with the second question. So I would just say Prime Day had enormous impact on the device business and devices were well featured and also well adopted by customers. So it was the largest device sales day that we've ever had and essentially pretty much across all of our device types, E-readers, tablets, Fire TV and Echo.

And I'm sorry. Your first question was around – the cost of fulfillment centers. Not disclosing that we do continue to change our fulfillment centers. We've changed, again, the automation, the size, the scale many times and we continue to learn and grow there. So no general trends I can point to on cost per fulfillment center to start up because they do vary in size and mission and some have fully outfitted in using Amazon Robotics, others – some don't for economic reasons. Maybe the volume is not perfect for robot volume. But yeah. But, yes, so I can't give you any real distinct trends there.

**Operator**

Our next question is from Justin Post from Merrill Lynch.

**Justin Post - Merrill Lynch, Pierce, Fenner & Smith, Inc.**

Great. Thank you. First on the customers, I'm guessing – I'm wondering why you aren't giving the number, a lot of people use it for their models. And then second thing, when you look at the U.S. Prime penetration versus total U.S. customers, how do you feel about that and do you think there's still a lot of room for Prime growth in the U.S.? Thank you.

**Darin Manney - Director, Head of Investor Relations, Amazon**

Hi, Justin. This is Darin. I'll comment on the customer accounts again. We may consider updating that in the future, but really we encourage you and our investors to look at our free cash flow measures, our revenue and our GAAP operating profit since our customer purchasing behavior can vary.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

And on Prime penetration, of course, we haven't released Prime subscription levels. We have talked about growth certainly globally and in North America. What I can tell you there is we still think there's a lot of room in Prime. We've tailored programs to students. We've tailored video programs. We've rolled out monthly plans. We have plans with grocery delivery. So there's a lot of different flavors of Prime and we are aggressively looking for a perfect Prime for everybody. We know that, again, when customers try Prime, they like it. So it's really just about getting them to try Prime and continuing to deliver great Prime benefits and great low prices and selection.

**Operator**

Our next question comes from Ross Sandler from Deutsche Bank.

**Ross Sandler - Deutsche Bank Securities, Inc.**

Thanks, guys. I just had two. First as a follow up on the logistics topic. So, in addition to the cargo planes you just mentioned for in-network moving products around, you guys have registered and received a U.S. Maritime license to operate as a freight forwarder and you recently announced this partnership with the UK for drone delivery that you've been working for a couple years. So I guess at a high level, can you just talk about the overall logistics strategy is evolving from trucks and fulfillment centers to incorporate some of these new methods and how that might impact your unit costs going forward?

And then the second question's on AWS. So you continue to put up really strong results. And you guys obviously talk to a lot of customers across lots of different verticals. Just a high level, what percent of enterprise workloads do you think have shifted to the public cloud at this stage? Is it low-single digit to mid-single-digit? And any color there on where we are in terms of penetration in the space. Thank you.

**Darin Manney - Director, Head of Investor Relations, Amazon**



So thank you, Ross. This is Darin. Let me take that first question on Prime Air in the UK, we've been working with and developing Prime Air for some time to develop a rapid delivery system that is safe, environmentally sound and it really enhances the services that we provide for millions of customers. And we're extremely happy to partner with the UK government to advance the safe use of drones for small parcel delivery. This is providing us with permission to trial new methods in the space, including beyond line-of-sight operation, sense-and-avoid technologies and flights where one person operates multiple drones.

So we definitely appreciate the pragmatic and forward-looking approach on this topic with the UK and we're going to continue to work with regulators and policy makers in many countries, including the U.S. So we're excited about there. As for the ocean-going licenses, we have no comment on that today.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

As far as AWS, essentially penetration question you asked. We think still very early. Again, we like our position, our industry leading position in the cloud space, and we're working on things that would incent more and more customers to accelerate their cloud conversion. The lower prices and services that we offer, and as I said, we'll work on things that will make it easier and easier for customers to work with us with their hybrid data centers or transfer their volume to us.

**Operator**

Our next question comes from Eric Sheridan from UBS.

**Eric J. Sheridan - UBS Securities LLC**

Thanks for taking the questions. Maybe one clarification and one big picture topic. On the clarification, appreciate the disclosure on content and how that'll double year-on-year in the second half. For purposes of just making sure we sort of can understand the trajectory, is there any way to frame it within second half of this year versus first half of this year, just so we can sort of try to triangulate on a gross margin basis from the content spend? And the bigger picture topic would be China, hasn't come up yet on the call. Wanted to understand your latest thoughts there on either the competitive landscape relative positioning in China and how you think about investments in China. Thank you.

**Darin Manney - Director, Head of Investor Relations, Amazon**

So, hi, Eric. This is Darin. I'll take the second question on China. So we continue to operate well in China. We see China as a – and the way we're approaching China as a way to – a trusted avenue for our Chinese customers to access authentic international brands and we'll focus on those global brands and bringing those to Chinese customers. Offerings like the Amazon Global Store where Chinese customers can access those international brands on the China website and have them shipped directly to their houses is something we're focused on. So, yeah, it's still early days and some of those experiments that we're doing, but we're seeing good traction on those things and we like that.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Yeah and on the content spend, I think the only other data point I can give you is probably a dated one at this point, but we spent \$1.3 billion in 2014, that's the last number that we disclosed and we continue to add content. The best I can give you at this point is that it will be double, nearly double what we spent in the second half of 2015.

**Operator**

Our final question will come from Victor Anthony from Axiom Capital.

**Victor Anthony - Axiom Capital Management, Inc.**

Thanks for putting me on. Maybe I'll just ask a question about India. You called out India was – you had the most visited e-commerce site as well as the most downloaded mobile app, and you also launched Prime. So maybe you could just talk about the opportunities and the challenges that you see in that market. And second, there was some press reports that you invested about \$500 million of incremental capital in Italy. I was wondering what are you seeing in that market that justifies that level of investment.

**Brian T. Olsavsky - Senior Vice President and Chief Financial Officer**

Sure. So India, we're very encouraged by what we've seen so far in India, both with customers and also sellers; that's a (40:18) third-party seller market. You heard that we launched the Prime program this week, which will be a whole new experience for Indian customers. In hundreds of cities we'll now have unlimited free one-day and two-day delivery, and we also mentioned that Prime Video is coming there, both Indian and global content. We're also starting to see exclusive online sales partnerships. Recently, we've had partnerships with Motorola, Samsung, Lenovo on select phones. But more importantly, again, we really like the opportunity in India. We like the initial results that we see from customers and also sellers. We really like our team there. We have a great team of Amazonian's who've been very inventive in India.

Every time there's an obstacle or something that's different from the U.S. or another major business they'll invent around it, whether it's a shipping method or a payment method or whatever. So, very creative and the customer response has been really strong. So we are very excited about the Prime program. We think it'll enter into a new chapter in India, and we've seen great success every country in the world that we've launched Prime, and we feel India is going to be no different. So we're looking forward to seeing what we can do on behalf of the Indian customer.

**Darin Manney - Director, Head of Investor Relations, Amazon**

And hi, Victor, this is Darin. On Italy, yes, we continue to invest in Italy and really throughout Europe to keep pace with the strong customer demand we see. Since opening Italy in 2010, we've invested over €450 million and created 1,700 jobs in Italy, and this increased investment will be to add future FC near Rome and other infrastructure assets. So, yes, this is really to support both the customers that we have there in Italy and throughout Europe, and we'll continue to invest in the coming years.

**Darin Manney - Director, Head of Investor Relations, Amazon**

So thank you for joining the call today and for your questions. A replay will be available on our investor website at least through the end of the quarter. We appreciate your interest in Amazon.com and look forward to talking with you again next quarter. Thank you.