Amazon.com (NASDAQ: AMZN)

David Gardner | September 1, 2002 | Buy Recommendation

CURRENT PRICE: AMZN $ 2773.08 ↑ $ 59.26 (2.2%)

Quick quiz: What "dot-com" is actually up 40% this year while the Nasdaq is down 30%?

Answer: My recommendation for this month, Amazon.com (NASDAQ: AMZN).

Just a year or two after many analysts had left its shares for dead, Amazon.com has emerged as the biggest pure-play in e-commerce. The company is generating billions of dollars in annual sales and—the key for us going forward—these are finally *profitable* sales.

I've owned this company's stock through thick (very thick) and thin (very thin) since 1997. Over that time, I believe Amazon has proven that it's a mass-market leader in an important segment—online retail of entertainment products (the traditional "BMV" of books, music and videos). As a market leader, Amazon has squished its competition and carved out a healthy customer base numbering some 30 million. Outgunned in revenues by a ratio of about 8-to-1, competitor Barnes & Noble.com announced in mid-August that it's facing a Nasdaq delisting. At last check, much-vaunted Walmart.com is featuring refrigerators and desks on its top page.

The question appears less and less to be, "Will anyone ever surpass Amazon.com?" and more and more to be, "How much can Amazon.com profit from its endeavors?" After a long swim in red ink, the company will finally deliver profits this year—an estimated nickel per share in 2002, ramping up to 22 cents next year. And *Forbes* recently estimated Amazon's 35 year annualized earnings-per-share growth at 34%.

AMAZON.COM, INC. IN 1 MINUTE

What It Does

Amazon.com is virtually synonymous with online retail, selling its own inventory while also offering third-party sales and fulfillment. It also has fast-growing operations in subscriptions, advertising, and Web hosting.

Company Guide

- **Industry:** Internet and Direct Marketing Retail
- **Asset Class:** Large
- **Region:** US
- **Price on June 21, 2020:** $ 2713.82

Key Data

- **Headquarters:** Seattle, WA, US
- **Sector:** Services
- **Market Cap:** $6B

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What's behind the success? A company fanatically focused on customer satisfaction, and a brilliant, entrepreneurial CEO. What's the major obstacle ahead? A constant effort on the part of competitors, and even the company itself, to lower prices, which harms profit margins.

As it matures, Amazon's sales mix might surprise you. What used to be Amazon's only business, domestic sales of its Books, Music, and Videos entertainment products, is now just half of its sales. Of the $805 million in revenues the company generated in its June quarter, only $411 million (or 51%), came from domestic BMV. Compare that with some of its presently unprofitable divisions like its International business, which clocked in at just over $218 million in sales (27%). The Electronics, Tools, and Kitchen business, also unprofitable, generated another $128 million (16%).

Then there's the promising Services segment, with higher profit margins. Last quarter, this division delivered sales of just $47 million. But for the future, the Services division will represent increasing potential as Amazon works with retailers like Target (coming online with Amazon this quarter) and others to run their e-commerce for them.

Further, hidden within those numbers above, are an increasing number of "third-party transactions"—namely Amazon's auctions (its competition against eBay). For the June quarter, these transactions came to 35% of all North American orders. And the international business, still in its infancy, has a very high growth rate—jumping 70% over the same quarter last year.

All of this helps to explain why Amazon.com has way outperformed the Nasdaq in 2002 and, from a longer-term perspective, the market overall. And while paying 75X next year's earnings brings with it some real risk, I believe that Amazon.com is a keeper stock for the long term, as it leverages its brand and online savvy toward greater profits—by itself and in cahoots with its partners. I'll buy that!