# Morgan Stanley Technology Conference

## Company Participants

- Tom Szkutak, CFO, SVP

## Other Participants

- Mary Meeker, Analyst, Morgan Stanley
- Unidentified Participant, Analyst, Unknown

## Presentation

### Mary Meeker {BIO 1505056 <GO>}

Thank you, all for coming. The format today is Tom Szkutak, Amazon's CFO, is going to go through a 15-ish minute presentation. If you don't have a copy, there are people walking around with copies of this. And it is just to give you a basic overview of Amazon.com and what the Company believes is important from a free cash flow perspective and an operating perspective. Then I am going to lead questions for about 10, 15 minutes and then turn it over to others. So Tom Szkutak, thank you for coming.

### Tom Szkutak {BIO 5025269 <GO>}

Thanks, Mary. As Mary said, what I would like to do is just spend about 15 minutes. I'm going to go through two things. I am going to walk through our most recent financial results just quickly. And then talk about how we look at the business.

Just some of this information may have some forward-looking statements. And so for a full list of our risks and uncertainties, please see our most recent 10-K and subsequent filings.

In terms of our financial focus, the way we look at it is we are focused on optimizing free cash flow, free cash flow per share. We look at return on invested capital. And we are all about maximizing profit dollars, not individual margins.

In terms of free cash flow, over the past 12 months ending December 31st, we had just under $1.4 billion of free cash flow. That was up 16% year-over-year.

In terms of how we leverage our free cash flow, we have -- if you look at our earnings and working capital, you've seen leverage over the past 12 months. You've also seen decent leverage in fixed investment. We are spending at a little bit above our depreciation-reinvestment ratio -- it's just a little bit over 1 -- but given the growth that we have, I think that is pretty good leverage.

In terms of our operating cycle, we have a negative operating cycle, for those of you who haven't followed us too closely. And what that means for us, if you look at year-end, we had approximately 30 days' worth of inventory on hand, we had about five days' worth of receivables. And we paid our suppliers, on average, about 61 days. So we had a 26-day negative operating cycle. So as we grew, we generated cash from working capital, which is included in the $1.4 billion I mentioned.

In terms of share count, again, we are efficiently managing dilution. If you take shares outstanding plus stock awards outstanding, we had about 446 million at the end of last year. That was up from 435 million in 2007. And if you go back several years to 2004, it was about 434 million. So relatively flat over the past several years.

Sales last year were just under $19.2 billion, up 29%, or 28% adjusted for the impacts of foreign exchange rates. When we show our results, we show it in two principle segments, North American and International. Then we broke out our sales between media, electronics and other general merchandise and other. Other includes Amazon Web Services, our Amazon Enterprise Solutions business, cobranded credit cards and other miscellaneous marketing agreements. And Other.

The mix of our business has been changing over the past several years. We were predominantly a media business a few years ago. Back in 2004, we were 74% media categories. And last year we were 58%. So we've grown our media business back in 2004 from $5.1 billion to a little over $11 billion, even though the mix has changed.

International revenue has grown nicely, was up 33% last year, or 31% excluding the impact of foreign exchange rate. A lot of that is driven by expanded selection. We continue to get better and better at pricing. And we've made it convenient for customers, including launching Amazon Prime in a number of geographies.

When we look at gross profit over the past 12 months, it was up 27% year-over-year. Consolidated segment operating income was up 29% year over year. So essentially on an annual basis, flat operating margins.

Our balance sheet is showing its efficiency. We ended the year with about $3.7 billion of cash and marketable securities. Continuing to get very good turns in inventory. And as I mentioned, payable days are at about 61.

Return on invested capital was 41% last year, down slightly -- down from the year before 55%. We use what we believe to be a conservative calculation for return on invested capital. We use trailing 12 month free cash flow divided by a five-point average of total assets minus current liabilities. And so the cash that we have that we have built up is certainly impacting that growth rate.

So that's it on the results side. I just want to spend a few minutes on strategy and how we think about our business. And then we will open it up to questions for Mary and then all of you.

The way we think about our business, we always start with the customer first and work backwards. We have three principal customers -- consumers, sellers and developers. I am just going to spend a few minutes talking about each one.

In terms of -- there are a number of different ways we leverage our platform. We have Amazon the seller, which in Q4 accounted for about 73% of our units. We have sellers, which -- third-party sellers, which accounted in Q4 for about 27% of our units, another way we leverage our platform. We have Amazon Enterprise Solutions, which is essentially our merchant.com business. It's where we power third-party websites. And again, another way we leverage our business. Then we have simple APIs in the form of Web Services. We leverage that technology by monetizing it externally, as well.

In terms of the consumer, the first customer set, which is consumer, the way we think about customer experience is we focus on price, selection and convenience. And always with a foundation on innovation. And we think about pricing. We are not one that discounts a small number of items. We really want to offer low prices every day and apply them broadly across our product range.

In terms of selection, we've added many new categories over the past couple of years, particularly in our international geographies. And selection is very key to growth. We are not only adding new categories, we are adding selection in each of the categories that we are in today. And so adding selection within categories, adding new categories within geographies that we are in certainly are growth drivers and over time, we will certainly add new geographies, as well.

One of the other things that we do for convenience is Amazon Prime. There are a number of things we do for convenience; Amazon Prime is certainly one of those. We offer Amazon Prime in most of our geographies today. We offer it in the US, the U.K., Germany, Japan and France. We offer free shipping in all of our geographies; again, convenience for customers.

In addition to adding a lot of physical categories over the past few years, we've certainly added digital delivery products as well, certainly digitally delivered content for Kindle, MP3 downloads and video on demand. So again, that is our customer, our consumer, which is our first customer set.

We also focus very heavily on our seller business. There are a number of things that we focus. We have a lot of programs on how do we make that experience better for sellers. An example of one would be Fulfilled by Amazon, where we do fulfillment for third parties. The benefit for them is they can focus on the other parts of their business and they can take advantage of our multi-node fulfillment network.

They can also have their items eligible for Prime and Super Saver shipping, once it is part of our network. So it is a great benefit for sellers. It is also a great benefit for customers as well, because they get to buy third-party items and can take advantage of free shipping and Prime on those third-party items. We have over 1.5 million sellers selling on Amazon.

In terms of Web Services, again, we have a number of different web services. And again, we focus very heavily from a customer perspective.

So with that, we will open it up for questions.

## Questions And Answers

### Q - Mary Meeker {BIO 1505056 <GO>}

Thank you for the overview. So what I would like to do is spend a few minutes just on the core business and then talk about some of the incremental stuff with Kindle and the media business.

But Amazon, much to shareholders' chagrin, to an extent, invested billions in the customer experience -- certainly hundreds of millions in the customer experience. And over the course of the last couple years, it has really begun to pay off with share gains. Your guidance -- you had 18% growth year-to-year in the Fourth Quarter. Your guidance is for 9% to 19% year-to-year growth in the First Quarter. Much higher than most other companies are experiencing. It appears as though the share gains are continuing.

A, are you still comfortable with your guidance? And B, any data that in sort of three points or less, in your view, why are you gaining that kind of share?

### A - Tom Szkutak {BIO 5025269 <GO>}

Sure. In terms of guidance, we have a long-standing practice of not updating our guidance intra-quarter. So I am not (multiple speakers) current trends. But just a little bit more on guidance and then answer your questions.

Keep in mind that we are looking at a growth rate too -- for Q4, our growth rate was 18%; on a local currency basis, it was 24%. The guidance that we gave for Q1 was 9% to 19%. We said it was approximately 600 basis points of exchange. So it would be a range of 15% to 25%.

But the reason why you are seeing the share gains that you are seeing -- that you saw in Q4 is really around some of the things I mentioned in the opening remarks. I wish it was -- it's focusing on the fundamentals. We have gotten much better in understanding -- being competitive on pricing, knowing where each product is competitively priced in each of the geographies that we are in. We have added a lot of selection.

And we focused on in-stock levels. We want to make sure that when customers come through our detail pages, that product is in stock, ready to ship right away. And that's been a great needle mover. Prime, which we invested in, as you're talking about, has certainly had an impact on us, as well as the other things I talked about. So it is certainly selection, convenience has gotten better through Prime. Being better -- understanding where we are in pricing from a lot of the tools that we have. All of those things have contributed to the growth that you are seeing.

## Q - Mary Meeker {BIO 1505056 <GO>}

Are there X number of products where you say, we must have the lowest price available anywhere?

## A - Tom Szkutak {BIO 5025269 <GO>}

No. It is -- again, the way we think about it is very, very broadly. We want to make sure that when a customer comes to Amazon, they are getting great value. And it is not on a small number. It is very, very broadly. And so some of the investment that we mentioned a few years back, when we were in the heavier investment phase of our business, was making sure that we had the right tools to measure those. And so that we could really make sure that we are offering the best value to the customers.

## Q - Mary Meeker {BIO 1505056 <GO>}

One of the things I've noticed in the last six months is that, one, your active seller numbers have accelerated. So that is a great indication of two things. One, you are either a great outlet to sell products, or people have more inventory they need to sell and are looking for new ways to find it. And you are just at the top of the list. And they don't know that you are the best. But they think you are good.

As a shopper, a thing that I've noticed is that my pricing is getting much better, in large part because of third-party sellers oftentimes. And so Amazon has increasingly become the lowest price purveyor in the last six months, in part because of your third-party seller business. How does that dynamic play out? And if you did a -- our view is that the average person doesn't think of Amazon.com as one of the leading discount retailers in the world. But the active customer has been feeling that way for two to three years. So the dynamic there is how important is that third-party growth in making sure you are the lowest priced provider? Question one.

And question two, in this environment, where there is more inventory to be liquidated at a faster pace. And retailers that need to get rid of stuff, it gives you a material competitive advantage, versus everyone else who can't sell that kind of stuff in their store.

## A - Tom Szkutak {BIO 5025269 <GO>}

Yes, I think it is -- to answer your question on the third-party piece, I do think is a very important part of our model. And for a number of reasons. For the reason you mentioned -- we have a lot of sellers who have great prices on our detail pages. And we not only -- oftentimes that's incremental selection that we don't have. Many times it's we are competing against that as a retailer, Amazon the retailer.

And I think it is great from a customer experience standpoint to be able to come onto our detail pages and to see multiple offerings of the same product. And customers knowing how we think about it -- we want to make sure we offer great prices from a retailer perspective. It is just -- it's one of the benefits of our model.

And I agree with you that as third parties have additional stock that they want to sell, we are a great outlet to sell it on. And that is why you are seeing, in Q4 even, the growth of third-party units as a percentage of our total grow again year-over-year.

## Q - Mary Meeker {BIO 1505056 <GO>}

Your founder and CEO, Jeff Bezos, has proven to be a great visionary and also willing to zig when others are zagging, which leads some to believe sometimes he is a little off kilter. But his track record has proven that he has been right more often than he has been wrong. And I say that in the context of in this environment, I would think that the message that this is our biggest opportunity to gain share because the economic environment is challenged is something that is pervading through the Company and that there is a view that you will gain more share in this environment than not.

## A - Tom Szkutak {BIO 5025269 <GO>}

You know, within the Company, we are actually extremely focused on just doing what is right for customers. And we think that will be what helps us to continue to grow better relative to others in this environment. And so in this environment, we are being -- we are still investing in the business. But we are being prudent, given the environment that we are in.

But the biggest focus internally is how do we make sure we make it even better for customers. And those things, the teams that we have across the world are just so relentlessly focused on all the things that I mentioned that drive growth on a daily basis.

## Q - Mary Meeker {BIO 1505056 <GO>}

You recently paid down debt. I think all in, it was $2.5 billion-ish. And now it is -- you paid it down. It is -- I'm not sure how many companies paid down all their debt in the last 12 months. I think it is a very small list. Why did you do it when you did it. And what should our interpretation of that be?

## A - Tom Szkutak {BIO 5025269 <GO>}

Right. It has been paid off over a period of a number of years now. And we just had a small amount that was left. Again, we thought it was the right thing to do. We certainly have also purchased back shares, as well. And we thought it was the right thing to do.

It is not to say we won't have debt over time. We just thought it was -- just as a reminder, for those of you who are not close to -- out two principle pieces of debt were convertible debt and we certainly had some of that be dilutive. But most of that not.

## Q - Mary Meeker {BIO 1505056 <GO>}

The biggest risk for Amazon, in addition to how do you handle the economy, has been the fact that the media business has decelerated. It was down -- it accounts for 50%-ish of the business, 50% plus. It was up 9% year-to-year in the Fourth Quarter. It decelerated from 19% year-to-year in the Third Quarter. And I think 31% in the Second Quarter.

How do you think about it internally? How concerned should we be about the slowdown in that paper-based, taped based, whatever you want to call it, environment? You know what I'm trying to ask (multiple speakers).

## A - Tom Szkutak {BIO 5025269 <GO>}

I think we have a very -- I think we have a very good media business. We did see, even though we had strong growth relative to others in our total business, we did see a deceleration in our total business in Q4 from what we saw in the first three quarters of last year and in Q4 of '07. But we feel good about our media business. And we feel very good about a lot of our digital offerings, Kindle being --.

## Q - Mary Meeker {BIO 1505056 <GO>}

Well forgetting about the Kindle for a minute, because I want to get to that. But the digital opportunity is there. But you have the -- when you do the math on -- what is the word I'm looking for? It is paper-based, it is tape-based, it's CD-based -- whatever we call -- that hard whatever I am trying to look for -- kind of --.

## A - Tom Szkutak {BIO 5025269 <GO>}

Physical.

## Q - Mary Meeker {BIO 1505056 <GO>}

Physical. Physical media -- thank you very much -- versus digital media, you have the trade-off of digital, which we'll talk about. But you also have the trade-off if you are selling the players for the physical media. And how does that ratio play out, when you look at it internally? Because we don't have any insight into that.

## A - Tom Szkutak {BIO 5025269 <GO>}

Yes, how it is going to play out over time, it is hard to tell. We are trying to make sure we offer what the customers want. And we will continue to offer physical media. It is still a strong business, still the growth rates that you mentioned in a challenging environment, still very solid. But we are going to focus on -- like we have, we are going to make sure that we offer physical delivery media products, both from a retail perspective -- we have a very solid third-party business as well on the physical side -- and we have the digital products, as well.

## Q - Mary Meeker {BIO 1505056 <GO>}

Given that I can't articulate what physical media is, I'm going to switch gears. But you've got 90 million-ish active customers. The iTunes store has 80 million active customers. You are selling what you are selling, a lot of physical stuff. They are selling a lot of tunes. You've got Netflix that has a 10 million active customer base, registered user base of people renting movies, largely in a physical way.

How do you look at the way your competitive set plays out for that 50% of your business over the next two to three years? Are those the two to watch? Can you operate symbiotically and in different places than Apple, i.e. they have their iTunes, they have their apps store for the iPhone. You can have an app store for everybody else.

## A - Tom Szkutak {BIO 5025269 <GO>}

We have a long-standing practice of not talking about individual competitors. Both of the categories that you mentioned, I think the space is very large, with a number of competitors in those spaces. And we have been focused on, again, trying to make sure that the customer experience is good. In the case of music, we have over 7 million songs available in an MP3 format. We are going to continue to grow selection there.

There's a number of things that we've made it more convenient for customers. On our detail pages, we also have a number of programs with third parties to make it more convenient for customers. For example, if you go to YouTube, you can purchase content on their detail --.

## Q - Mary Meeker {BIO 1505056 <GO>}

Did you like the stats you're seeing from those video downloads?

## A - Tom Szkutak {BIO 5025269 <GO>}

Sure. Again, we have a number of these. That happens to be one of them. We like what we've seen so far. It is still early. We have a number of them. The biggest reasons why customers will come to us, though, is because of the convenience and the selection and the pricing that we have. So all of those things are things that we are working on. Again, we still think we have a lot to do in those categories. And we will continue to work on making those experiences better.

## Q - Mary Meeker {BIO 1505056 <GO>}

So move into the digital stuff. So this is a Kindle. I read the Wall Street Journal on the Kindle. I learned that you have the Kindle available for your iPhone, for the iPhone. I downloaded the Kindle app on my iPhone this morning and I now have all my books on my iPhone. My 200-page books are now 1000 pages long. I'm not sure I'll read them. But I'm glad to know I have them. But the synching element is really powerful.

A couple questions. (Huawei) has the Android Phone, which has the Shop Savvy app that you click on Shop Savvy on any -- scan a barcode. You can do it with the Android Phone; you can't do it with the iPhone, because the camera is not powerful enough yet. But we have been stunned at how often the web-based product that comes up with a barcode, the lowest price is Amazon.com. And we've been stunned at how material the price difference is between the land-based option.

So the point of this is severalfold. You are way ahead of all your retail competition on the digital devices. Our view is that you are -- as continue to be -- that you are going to outship the iPod. You're going to get to 1 million units in the first -- it took them two years; you will get there before two years, which will be Thanksgiving of 2009 -- not that we are counting.

But when you get to 1 million -- the question is, when you get to 1 million, will you tell us? Why haven't you told us so far anything about it, number one? Number two, our view is that your market share on these mobile devices is going to be materially higher than it is on the PC, just because your apps are really cool, whether it is Amazon Remembers, where you can take a picture of something and send it to your Mechanical Turk and get pricing on it.

But we are talking with WebMD yesterday. And they had had 390,000 downloads of their WebMD app, their widget, on the iPhone. What is the early -- so when will you tell us when we get to 1 million Kindles? And what is the early data telling you about your potential market share in the mobile devices? And has the uptake of the Amazon which has surprised you and other things surprised you on the upside?

## A - Tom Szkutak {BIO 5025269 <GO>}

Good questions. In terms of the numbers, we actually -- and this is a long-standing practice we have. We haven't broken out the specific sales numbers of units.

## Q - Mary Meeker {BIO 1505056 <GO>}

Your inventory controls are so poor, you don't know how many you have shipped.

## A - Tom Szkutak {BIO 5025269 <GO>}

No. We haven't broken out the details of any categories -- in any of the categories that we operate in. And the reason that we haven't to date anyway is that we think that it might be competitively useful. And so it is not to say that we won't at some point say how many Kindles or other categories (multiple speakers). But to date, that has been our stance. And that is why.

But we are pleased with what we've seen so far. As you mentioned, mobile is a very interesting area. We have a number of things going on in the mobile space, including, as you mentioned, we announced this morning the Kindle app on the iPhone and iPod Touch. And I think it is -- for Kindle users, I think it is going to be a great companion to the Kindle. If you think about it this way, we have something called Whispersync. Mary was mentioning the synchronization; it is called Whispersync.

So the benefit is if you're a Kindle owner and you are reading your book on your Kindle and you leave your Kindle at your home or whatever and you are getting a coffee somewhere or in a grocery line, you can actually use your iPhone or your iPod Touch and it will pick up right where you left off. It will also have your bookmarks. And so it's a great companion.

It also opens up, obviously, the benefit of having customers who don't have Kindles the ability to get content, should they desire to do so, on their iPhone or iPod Touch.

So in terms of surprises, it's a good question. I wouldn't say there are a lot of surprises. But we are pleased with at least some of the initial things that we've done. We will see how this app does that was just announced this morning.

## Q - Mary Meeker {BIO 1505056 <GO>}

It works in this room, which is the only mobile technology that seems to work in this room. We are very safe here. It's the safest place in San Francisco, thanks to an earthquake many years ago.

But the Whisper -- just two more questions from me -- Whispernet, Whispersync, to my knowledge nobody else has deployed it. The data you have from your 80 million customers is a very, very powerful advantage. When you get your Kindle and turn it on for the first time, it says Tom's Kindle, Mary's Kindle, Sally's Kindle, Joe's Kindle, whatever. And it connects with your purchases of the past and provides a recommendation engine, which we think accounts for 25% plus of your business. If you want to provide us with that info, we would be thrilled.

But it sort of knows who you are. And the Whispernet and Whispersync technology, I have not seen deployed by other companies. One, you have the competitive advantage of having all your data. But two, nobody else has done it either. What's your lead time competitive advantage with that technology in these new devices? Then one more question and I'll turn it over to others.

## A - Tom Szkutak {BIO 5025269 <GO>}

Yes. It is a good question. Hard to say. Hard to know what kind of lead time that gives us. But it is -- for us, we think it is very powerful technology, as you were mentioning, in terms of just synching -- the Whispersync technology, it enables customers on Kindle to get the content in less than 60 seconds very conveniently. So again, hard to know on that piece.

## Q - Mary Meeker {BIO 1505056 <GO>}

Last question from me. You have very quietly invested in phone-based customer service. What have you learned from it and how important is it to customer satisfaction and ROI -- and how actively is it used?

## A - Tom Szkutak {BIO 5025269 <GO>}

Yes. It is -- we are still a very heavy e-mail-based customer service. We want to certainly make other modes available to customers. And --.

## Q - Mary Meeker {BIO 1505056 <GO>}

How many customers have had a customer support interaction with you? Is it -- you have 88 million, 90 million active. Is it 10 million, is it 5 million?

## A - Tom Szkutak {BIO 5025269 <GO>}

We haven't broken that out. And --.

## Q - Mary Meeker {BIO 1505056 <GO>}

Never mind. Let's turn it over to questions. Any questions?

## Q - Unidentified Participant

(technical difficulty) absolutely love it. The question is how do you get to triple-digit ROIC? How do you see that path? I know the physical versus virtual will do that.

Then do you think longer-term if you want to get those kind of high ROICs, how do you see in perspective what new things you are going to invest in? And eventually, does Amazon become a company where you kind of share with shareholders the glory of all this cash coming in rather than continuing to invest?

## A - Tom Szkutak {BIO 5025269 <GO>}

Right. Just in terms of the --

## Q - Mary Meeker {BIO 1505056 <GO>}

How long are you going to live?

## A - Tom Szkutak {BIO 5025269 <GO>}

In terms of the first part of your question, in terms of triple-digit ROIC, I certainly think that that is possible over time. We don't have a precise year or date to do that. But keep in mind when you look at the way we measure return on invested capital today, in the denominator, in our total assets, we have cash and marketable securities in that number. Which we believe is the right way to measure it, because we haven't returned that to shareholders. But it is a conservative approach.

But if you think about it over time, certainly one example would be we generate cash from operations. We think it is prudent to be, particularly in this environment, to be appropriately conservative with our cash during this environment. But I don't think we would have to retain as much cash, certainly, relative to our free cash flow over time, for example.

But again, we have a very high-ROIC business, given the model that we have. We are very pleased with that. And -- so we do think that it is possible over time to get to triple digits. It is not a target. But it is possible. And the second part of your question, sorry, was --?

## Q - Unidentified Participant

(technical difficulty)

## Q - Mary Meeker {BIO 1505056 <GO>}

There may be customers in Mars.

## A - Tom Szkutak {BIO 5025269 <GO>}

There is a lot of -- the question was around opportunities for future investments for return on invested capital. There is a lot of opportunity in our business right now. I talked about selection. We have a lot of categories that we are not in in many of our geographies. Those are opportunities for us to invest in. We have opportunities to grow our seller business further.

We have opportunities to add new geographies over time. We certainly think our digital business has a lot of opportunity for growth. Our Web Services business has a lot of opportunity for growth. So we think there is many levers for growth for the foreseeable future.

## Q - Unidentified Participant

Just a follow-up on the financial stuff. I can live with all the investments in R&D. I think it's the right thing to do, especially in this environment. But when I hear you use the word efficient with regard to your financials, it doesn't sound efficient at all. Because a lot of your cash flow is related to stock option benefits to your employees. And your share count is flat, I guess, to up. But you are giving a lot of the Company away to the employees, when you've got this great operating model going on.

So I guess I am curious to know why is -- what is the future trend? Are you going to keep issuing a lot of stock options? Should we look at a lot of your free cash flow as basically related to the stock option expense?

## A - Tom Szkutak {BIO 5025269 <GO>}

Let me make a clarification. We actually don't give stock options to employees.

## Q - Unidentified Participant

(inaudible)?

## A - Tom Szkutak {BIO 5025269 <GO>}

We give restricted stock. And if you look at our dilution, it is actually -- since 2004 through 2008. And you could look prior to that, it is actually pretty flat. And so the impact on free cash flow as you are describing it is -- I'm not quite following it, because it's --

## Q - Unidentified Participant

Well there is like about 200 and some odd million related to the amortization of restricted stock -- or, I'm sorry, the tax benefits. And another $400 million or $500 million related to the amortization, I guess. That's a big chunk.

## A - Tom Szkutak {BIO 5025269 <GO>}

It is actually a reduction. We removed it from free cash flow, because we classify it as a financing activity. So it actually has a negative impact on free cash flow, not a --

## Q - Unidentified Participant

Okay. So the free cash flow number you are defining is actually --

## A - Tom Szkutak {BIO 5025269 <GO>}

Essentially the way you should look at it is this. The way we included it in our -- that tax benefit, if you will, from excess stock-based compensation, it is actually -- the way you should think about it is it is almost as if we have applied an additional cash tax to be included in our free cash flow. That is the end result of how it is reflected in our free cash flow.

And if you have further questions on it, we would be happy -- (Kurt Fischer) is down here from Investor Relations, can actually show you those numbers.

## Q - Unidentified Participant

I had a question on the deal with iPhone. So when content is purchased or viewed on Kindle for iPhone, can you talk about the economics of that versus it being -- selling a Kindle device? And I know it (extends) in the market broadly; you don't just want to be on one device. But how should we think about the economic comparison?

## A - Tom Szkutak {BIO 5025269 <GO>}

We haven't disclosed the economics piece. But the purchase actually happens either through browser or on -- so it can be done on the iPhone browser, for example. It is not through the iPhones store -- excuse me -- the Apple store. It is through their browser or through browser on your laptop or PC.

Or, obviously, if you are a Kindle owner, it is a free app. And you would be looking at your content, as Mary was talking about.

## Q - Mary Meeker {BIO 1505056 <GO>}

But you don't have to pay the content provider an extra royalty for the second copy, because it is viewed as being one copy.

## A - Tom Szkutak {BIO 5025269 <GO>}

Correct.

## Q - Unidentified Participant

So is the margin on the content itself the same as it would be in the physical world?

## A - Tom Szkutak {BIO 5025269 <GO>}

Again, we haven't broken out the margins on physical or digital.

## Q - Mary Meeker {BIO 1505056 <GO>}

For what it's worth, our sense is that, near-term, it is potentially less. But long-term, it is potentially higher. The average book costs $15-$20. On Kindle, it is $9.99 -- I'm averaging and averaging and averaging. But there is no distribution costs. And we think net over time, it will be a net positive for the book producers and also for Amazon.

## A - Tom Szkutak {BIO 5025269 <GO>}

Other questions?

## Q - Unidentified Participant

I apologize if you've already talked about this. I came in late. So just to review, I think you guys have said when someone buys a Kindle, they end up purchasing 2.7 times as they did before. Is that correct?

## Q - Mary Meeker {BIO 1505056 <GO>}

It's something in the air.

## A - Tom Szkutak {BIO 5025269 <GO>}

Yes. The question is -- this is again on a units basis, customers' purchases of book units before versus after are 2.7 times. Excuse me -- after versus before, 2.7 times.

## Q - Unidentified Participant

(technical difficulty) steady as you see more and more data?

## A - Tom Szkutak {BIO 5025269 <GO>}

I'm sorry.

## Q - Unidentified Participant

Is that pretty steady as you've seen more and more data?

## A - Tom Szkutak {BIO 5025269 <GO>}

I'm sorry -- I don't know how to answer that question.

## Q - Unidentified Participant

Is that holding? Is that ratio holding up?

## A - Tom Szkutak {BIO 5025269 <GO>}

It is the data that we have. And as we -- it is the data that we've been fairly consistently providing since we started talking about it several months ago. And so, hard to say what it will look like going forward. But again, those customers are buying more books after -- substantially so.

## Q - Mary Meeker {BIO 1505056 <GO>}

We'll take one more question. And we need to be brief, because then we are out of time. You know what? Let's just -- we've got -- mic back there.

## Q - Unidentified Participant

I had a question about payment strategy. You guys ended up taking BML off your website at the end of last year. You guys give away a lot of value to merchant acquirers and also to the banks. What are you guys doing on the payment side?

## A - Tom Szkutak {BIO 5025269 <GO>}

Well we have a number of different payment applications right now. We have Checkout by Amazon. And we are continually doing things to make it better for customers, as well as doing some things with developers, as well. And so if you look at our offerings today, for example, for payment offerings from a customer perspective versus where we were three or four years ago, we have a number of different options that we didn't have -- for example, e-checks, as well as others.

And so the way we are thinking about it is certainly from a customer perspective, we are going to continue to try to do what is right for customers and add additional methods as we feel is appropriate and helpful for customers.

## Q - Mary Meeker {BIO 1505056 <GO>}

Thank you, Tom. Thank you, Kurt.

## A - Tom Szkutak {BIO 5025269 <GO>}

Thank you.