Retail Tenet #3: "We relentlessly lower our costs. We will serve each vendor by being its most efficient and innovative retail channel. We will improve total terms for each vendor every year." Today we provide year-to-date (YTD) progress (through October) on 2010 S-Team goals related to CoGS Cost Out and progress made through the Vendor Negotiation SME.

2010 S-Team Goals - Deliver Vendor Margin Cost Out:

A) US Vendor Margin per Retail unit served increased from $6.65 in 2009 to $7.02 in 2010, an improvement of $0.37 on a mix neutral basis to OP2.

B) Int'l Vendor Margin per Retail unit served increased from $5.88 in 2009 to $6.14 in 2010, an improvement of $0.26 on a mix neutral basis to OP2.

Overall, the **US** goal is green while the **Int'l** goal is yellow through October.

US vs. OP2: YTD US Vendor Margin is favorable to OP2 by $147.6M (+8.2%), $99.3M related to volume and $48.4M to rate (calculated based on the change in per unit Vendor Margin). US Vendor Margin per unit is $7.29 or $0.20 (mix neutral) ahead of OP2. US Media is $115.5M favorable to OP2, with a rate variance of $92.3M due mostly to less aggressive competitor pricing in US Books vs. OP2. Books customer discount is up 150bps YoY, but is 70bps lower than OP2. On a per unit basis, US Media Vendor Margin is $4.76 or $0.52 (mix neutral) ahead of planned OP2 per unit of $4.24. US EGM is $32.2M favorable to plan despite the fact that rate is unfavorable to plan by -$44.0M or -$0.43 per unit (mix neutral). This rate un-favorability is driven primarily by lower ASP across categories and increased price matching in Electronics.

US vs. 2009: YoY through October, US Vendor Margin increased by $450.5M (+30.2%) with $478.8M of volume related margin partially offset by an unfavorable rate variance of -$28.3M coming mostly from Electronics due to ASP declines in TVs and GPS. Vendor Margin per unit in 2009 was $4.71 in US Media and $12.41 in US EGM, and is $4.76 and $12.16 YTD in 2010.

Int'l vs. OP2: Int'l Vendor Margin is unfavorable to OP2 by -$89M (-4%), -$2M related to volume and -$87M to rate. Int'l vendor saving per unit is $5.93 or -$0.28 (mix neutral) behind planned OP2 of $6.21. Int'l Media is -$42M unfavorable to plan, with a rate variance of -$46M due mostly to aggressive competitive pricing in UK Media vs. plan (-$31M) and prior year (-$54M). On a per unit basis, Int'l Media is $5.13 or -$0.17 (mix neutral) behind planned OP2 of $5.30. Int'l Media rate unfavorability (-$46M) is largely driven by our inability to offset price competition shown in PPP (-$64M) with Vendor Funded Contra CoGS (+$19M). Int'l EGM is $47M unfavorable to OP2 due to volume (-$6M) and rate (-$41M) or -$0.65 (mix neutral) per unit ($8.64 against the OP2 plan of $9.29). Rate variance in Int'l EGM is driven by pricing with PPP (-$42.8M), Vendor Funded Contra CoGS is also unfavorable (-$8.0M) and offset by Price Protection (+$5.4M).

Int'l vs. 2009: YoY through October, Int'l is +$414M (+21%) above the Vendor Margin of YTD 2009, with an unfavorable rate variance of -$100M coming completely from the UK. Vendor Margin YTD is unfavorable to 2009 by $0.24 (mix neutral). Overall, although international year over year growth in Vendor Funded Contra CoGS including Price Protection of 44% has outpaced revenue growth of 33%, Pure Product Profit has increased only by 19% driven by aggressive competitive pricing. **For more details on performance by country, see Appendix A.**

Vendor Negotiation (VN) SME Update: VN SME partners with Retail Systems and Finance. We also work with global Retail and non-Retail teams with vendor relationships, like Ops and AdZinia. To execute on our tenets (Appendix B) we highlighted two types of best practices in our last review: **measuring and benchmarking vendors** and **evolving our vendor relationships**. Here, we add two key supporting efforts to enable faster progress: **increasing automation and efficiency** and **sharing best practices** and **positive surprises**.

Vendor Negotiations Vision

Our Vision is for Retail teams to set goals and strategies aligned with opportunities and threats based on complete data. Vendor Managers spend the majority of their time negotiating increased value and strategic relationships with vendors, sharing best practices and developing these skills on their teams. VN SME coordinates vendor service offerings across Amazon, facilitates global best practice sharing, helps plan strategy for key vendor negotiations, and provides robust requirements so systems continue to learn and gain best in class terms for all vendors. Systems provides complete internal data, benchmarking, goal setting and recommendations in a user friendly way. They prioritize opportunities and provide workflows with feedback loops for continuous improvement. Again, this is the vision, and we are Day 1 in truly realizing it.

To make progress on this vision, we need to build systems that automate workflows and facilitate data-driven decision making. By way of analogy, our initial efforts, Holistic Vendor View (HVV) and Vendor Goal Automation System (VEGAS) (discussed below), are similar to CMT in the early days. For CMT, we collected and aggregated pricing (and related data like shipping) to provide to category teams to make pricing decisions. HVV does something similar by aggregating and presenting internal vendor data to allow categories to identify negotiation opportunities. We need to develop vendor negotiations systems analogous to Pricing Rules to automate certain negotiation opportunities (e.g., price protection or AP days improvements) or make recommendations where judgment is required (e.g., goals and asks based on internal benchmarking, category or S-Team goals, and historical trends). These system improvements will give Vendor Managers (VMs) time for higher-value activities, like negotiating, by improving overall productivity. See Appendix C for further detail on these efforts.

1. <u>Measuring and Benchmarking Vendors</u>

We need to provide VMs the right Information: To enable goal setting and effective negotiation, VMs need the ability to review a vendor's performance (vendor scorecard) and evaluate a vendor versus its peer group (benchmarking). This requires complete and accurate data. In an early 2010 survey, VMs highlighted a lack of reliable data sources and difficulty in putting the data together. VMs requested a Vendor Negotiations portal which summarizes financial metrics, provides tools for negotiating and integrates with workflows. We launched HVV and VEGAS which begin to address these needs.

<u>A. Holistic Vendor View (HVV) and Vendor Goal Automation System (VEGAS).</u> HVV provides standard reports, allows vendor comparison, and includes metrics to calculate direct free cash flow (FCF) at a vendor level. We increased our user base from 545 in June to at least 701 users (note that users with other DW privileges can access HVV and are not captured) with an average of 122 users using it weekly. The population of potential users is approximately 1000 globally (VMs, In-Stock and Finance). We continue to add functionality. Since June, we added Inbound Receipt Defects and rolled out Global Company Reports. (See Appendix D for a sample.) Before June 2010, a "vendor" was represented by many codes in Vendor Master without complete mapping of the relationships. In June, we introduced the concept of an overall "Company" which allows us to understand complete vendor relationships. We provided Retail with self-service tools to map vendors across geographies and product lines. We are proceeding cautiously, working with teams globally to ensure each hierarchy we map represents the global view. We incorporated vendor hierarchies into HVV.

Peer benchmarking has been a powerful tool to identify negotiation opportunities. A recent **UK** success (built on **US Books** approach) benchmarked terms by looking at vendor profitability down to FCF, identified opportunities, and provided guidance on prioritization. The result was large gains (Disney (£671k FCF), Universal (£729k FCF), Microsoft (£600k FCF), Nintendo (£547k FCF), Random House (£1.2m FCF.) UK identified Fox as an under-indexing DVD vendor and is working on a 3-year commitment to get "best in class" economics. To scale peer benchmarking, we created a prototype system, "VEGAS," testing an automated vendor peer benchmarking and Vendor Tiering framework (e.g., Platinum, Gold, etc.,) in a more user-friendly interface than HVV. To date, VEGAS has 180 users but hasn't had dedicated development resources. HVV was built on OBIEE/ESSbase and as a result, has speed, scalability and flexibility limitations. To address, we are combining development for HVV and VEGAS (since both support negotiation) into one team that will build a Vendor Negotiation portal with design goals of speed and flexibility. We are locating this team in New York to access a large technology talent pool. Our recruiting pitch reflects the opportunity to build sophisticated decision support and apply automated algorithms to negotiations. (You will remember in June you challenged us to be more creative on hiring in this important area.) Since November, we made four offers (three accepted) and an internal Seattle transfer is relocating. To instill our culture, we are pairing employees with a Seattle mentor and requiring managers to interview experienced Amazon leaders on applying the leadership principles.

<u>B. Contribution Profit (CP).</u> In 2010, we launched CP for FBA and 3P in the US, an important improvement to understand the ASIN level CP of the 30%+ of our business not previously captured. Int'l will launch Q1 2011. We made progress in closing gaps between the CP tool and the allocated financials (net variance is about 2%). Some CP elements such as free reps and c-returns are estimated out of necessity at the time of shipment. Another source of variances related to the impact of Contra-CoGS agreements entered after the start date (45% of agreements). Starting mid-November 2010, we began continuously backfilling US CP data with actuals, allowing us to correct assumptions or predictions in the model, and implement an ASIN level CP accuracy metric. (We will backfill Int'l CP Q1 2011.) This metric compares CP calculated at time of customer shipment with the value for the same shipment 90 days later once ASIN level transactions are backfilled with actuals (product cost, contra-CoGS, customer returns, liquidation, etc.) This allows accuracy measurement for components where we have ASIN level transactions (See Appendix E). The CP team will prioritize projects based on how they improve ASIN level accuracy. For vendor negotiations, we plan to develop a variation of CP incorporating cost of capital, reflecting the impact of the cash flow cycle, FC fixed and capital costs. VMs can then evaluate the benefit of reducing lead times and increasing payment days.

C. Cost Saving Opportunities. With ~65M cost changes per year, it is not feasible for VMs to manage these updates. As we push for better Contra-CoGS, we risk vendors increasing product cost to compensate. The workflow for product costs with high % increases is currently crude and generates false positives. As a result, VMs tend to approve in bulk. To rectify, we are integrating a rules engine, allowing us to improve the sophistication of cost checks. We will compare cost with prior moving averages to detect outliers and situations where a cost increase will lead to below average CP. First delivery will be in Q1, 2011 and will focus on identifying drop-shippers with outlier costs.

D. Offline Pricing Data. Starting 2010, we captured and matched in-store offline CE and DVD prices. In Q4, we extended to H&G, Sports, Auto, and Tools monitoring 4K ASINs and generating 8K pricing recommendations QTD (approval rate 77%). We also began collecting pricing data for VG, Watches, Books and Music. Next steps are adding Int'l starting with UK DVD & CE, expanding NA, and are exploring using mobile apps to assist.

In-Store Price Matching - Quarter To Date

GL	# ASINs Monitored	# Low Priced Recommendations	# Approved	% Approved
DVD	1509	1464	1397	95%
CE	1407	2241	1291	58%
Grocery	623	4214	3478	83%
Kitchen*	156	53	29	55%
Tools*	70	30	18	60%
Garden*	35	16	12	75%
Sporting*	133	71	46	65%
Automotive*	51	67	36	54%
Total	**3984**	**8156**	**6307**	**77%**

* Price matching began on 11/26/10

2. Increasing Automation and Efficiency

Increasing our automation and efficiency will accelerate progress on improving vendor negotiation results. We identified foundational elements required. The first is having our vendor financial terms contracts online. The second is functionality to allow us to handle groups of vendors as a block both for negotiation and efficiency gains. More details in Appendix C. We also found providing global vendor communication support leads to efficiency gains.

A. Online Contract Approval of Contra-CoGs Agreements. In October, we launched this workflow, eliminating the need to track agreements via email. VMs see pending contracts, select and send them in bulk, track vendor approvals and rejections, and send follow-ups. (See Appendix F). This process eliminates vendor email confirmation and the need for Finance to check these emails correspond to the agreement. Also, it establishes an archive recording the time and date of vendor acceptance of Contra-CoGS terms. This functionality allows VMs to track which contracts vendors approved. We are piloting through Q4, allowing teams to elect whether to go online. The pilot exceeded expectations with more US agreements approved since launch using this process than Vendor Setup Workflow (32.4% of approved in this period). CA is at 14% adoption, EU is under 10% (JP launches Q1). These improvements are big controllership gains. See additional workflow efforts in Appendix G.

B. Automate renewals and create agreements for portfolios of vendors. We recognize a productivity opportunity exists with bulk creation, renewal, and distribution of Contra-CoGS contracts. VMs negotiated over 36K US vendor agreements YTD and 76K globally. Of those, approximately 19K US and 36K globally renew annually (Accrual, DA, or VIR). We can greatly reduce this burden by building workflows to support automated annual renewal of these agreements. We will handle tiers of vendors as a portfolio, allowing VMs to take actions on a group like increasing AP days. Retail portfolio wins in Appendix H.

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4. Sharing Best Practices and Positive Surprises

Best practice sharing is a focus. We developed a Category Leader Module and Deep Dive on Vendor Negotiations for 2010 that we will extend for 2011. We launched our internal newsletter, "The Negotiator," to share successes, systems updates, pitches and other helpful information (Appendix I). We lead best practice sharing in CCO meetings (materials shared with Int'l). We discuss our efforts to support annual negotiations below and in Appendices. Our pushback against MAP similarly works across categories. The Negotiation Bar Raiser Program (NBR) is our newest best practice sharing vehicle.

A. Customer Trust – MAP/TV Low Price Guarantee (LPG): We created new detail page displays which allow us to show below-MAP prices on Comp Shops (overriding the default that shows the MAP price when priced below MAP). Showing our price gave us an OPS lift of over 70% via the Comp Shop channel, and in over three months since implementation, we received no vendor complaints. (See Appendix J.) Improvement is estimated at over $36M in incremental US sales annually. Over 97% of items assigned to MAP are set to this treatment. We work with impacted teams to reduce MAP Enforced asins. In two months, we freed up $1.5M in obsolete, aging inventory from MAP restrictions and reduced MAP Enforced asins from 247K to 49K asins (down 80%) – **US HL, SL, Consumables, SW & VG**. We created a new treatment which shows below-MAP prices on comp shops and eliminates price-hiding for identified Prime customers. Over 60% of MAP Enforced asins are now set to this treatment. We drove a 2010 MAP Holiday for Black Friday-Cyber Monday where we suspended most MAP-related pricing and display restrictions and systematically exposed below-MAP pricing via Comp Shops – our disruptive idea from the last update. We provide VMs an SOP to remove MAP Enforced settings, a list of MAP assignments, and analysis. Each team managed their data loads. Catalog flags to override MAP treatment for Prime and 1-Click customers are scheduled for January. We provide VMs regular, mandatory training on antitrust issues and our Vendor Pricing Communication Guide focused on addressing MAP. In October, we launched **TV (LPG)** to build customer trust that Amazon offers competitive prices, despite MAP restrictions limiting display of our retail prices on the detail page. Modeled after Endless' guarantee, LPG allows customers to claim a refund on the price difference between what they paid on Amazon.com and any lower Amazon or online competitor price within 14 days. Since launch, over 1200 customers made a claim, in line with expectations. For 2011, we plan to match offline with the guarantee and may expand to other products that face aggressive MAP policies.

B. Negotiation Bar Raiser Program (NBR): NBR is piloting resources to help VMs prepare for negotiations. VMs can email negotiators@ for advice from experienced retail negotiators or attend office hours with representatives from VN SME, Finance, Retail Systems, and Retail. We hosted two brown bags so far. One on scalable methods to improve AP terms and a second on preparing for annual negotiations. Over 40 US VMs attended each session. We shared materials with Int'l. **DE** and **China** are using some approaches. An upcoming topic is **Countering Vendor Price Increases** to arm buyers to respond appropriately. We started a **Vendor Negotiation Toolkit** to become the handbook for best in class negotiation. (See Appendices K and L.) NBR will include tradeshow preparation. We assisted US CE with negotiation preparation for the last two Consumer Electronics Shows. We plan to build on these efforts and provide similar support prior to important tradeshows. Better preparation leads to results. For example, **US Baby** attended the All Baby & Child Show in October. Baby segmented Brands into groups: 'selection hold-outs', 'co-op opportunity brands', and 'tail selection'. For 'selection hold-outs', Baby had focused meetings with eight key brands and signed five (remaining three were positive conversations). For 'co-op opportunity brands,' Baby partnered with AdZinia to sign three accounts ($1M incremental funding) in 2011. Baby had positive intro meetings with Kolcraft, Dorel, Phillips, RC2, and Britax. For 'tail selection' brands, Baby held three "Amazon 101" with 40-60 attendees each and explained how to work with Amazon to a large groups of potential vendors.

C. CCO Best Practice Sharing: We led a US focused effort (materials shared with Int'l) to better prepare teams for upcoming annual negotiations. UK took a similar approach. We encouraged focused preparation that leverages successful efforts shared by other teams. Ops also participated with Vendor Cost Out Opportunities. See Appendix M. We highlighted two retail examples shared. Annual Terms Best Practice Sharing is in Appendix H. **Correct AP terms to exclude transit time:** Our AP process looks at invoice date for when to start the clock on payment terms. With net 30 terms, we pay 30 days after the invoice date. Most vendors date invoices when the product leaves their facility. For a vendor that pays for shipping ("They Pay"), the clock should start when we take possession at our FC. **US CE** adjusted terms to account for transit days to 188 vendors with ~$500M of annual CoGs. Many large vendors (Samsung, Canon) already accounted for it. CE now has $1.7B of annual CoGs accurately reflecting transit time. **US Books** implemented for 60 vendors and expects AP to be $1.3M higher. **EU** also initiated this approach. **Evaluate We Pay Agreements:** In 2010, Inbound Transportation expenditure where shipping is paid by Amazon ("We Pay") is forecasted to be approximately $125M. We are creating a vendor level P&L to track the inbound costs and freight allowance. With the help of Transportation data, **US CE** reviewed the We Pay P&L to see if we were getting enough funding to offset our cost. CE found 68% of inbound units did not have a specific freight allowance in place, 12% had insufficient funding to cover costs, and 20% had sufficient funding. Where no allowance is in place, CE is reviewing to identify if we received funding another way or if we need an agreement. Ingram is one We Pay vendor that did not have a freight allowance. They agreed to They Pay resulting in annual savings of ~$1.3M. **Other HL categories** are evaluating vendors with low Net PPM and freight costs not offset by freight terms and negotiating large opportunities. If negotiated freight allowance doesn't offset break-even freight terms, they will move to convert to They Pay. For new vendors, we may move default terms to They Pay unless we account for our costs. In our annual Q4-Post Mortem, we discuss what worked and what didn't, including where we lived up to our tenets and where we didn't. We plan to evaluate Q4 vendor interactions and capture decisions where we may have compromised one tenet in service of another. For example, price matched in November but ran out of stock in early December; gating to get selection and being uncompetitive on a portion of the selection.

VN SME Priorities for Next 6 Months: Our priorities are to continue to battle MAP (and other vendor demands that undermine customer trust); develop more workflows to support negotiations; develop the Vendor Negotiations portal; support variations better in ARA Premium and our negotiation tools; establish a credible measurement of ASIN level CP accuracy; expand support of strategic relationships and develop new ones; grow incremental funding through One Amazon and expanded vendor services; and continue to facilitate best practice sharing though all vehicles with particular focus on expanding the NBR Program.