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TECH

Amazon Notches Third Record Profit in a Row

Shares slide in after-hours trading as company flags uncertainty in India and possible uptick in spending

Amazon's fast-growing businesses such as its cloud-computing division, advertising offerings and the services it provides to sellers have helped offset the lower margins from its traditional retail business. PHOTO: LEON NEAL/GETTY IMAGES

By Laura Stevens

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Amazon.com Inc. AMZN **2.89%** ▲ recorded a third straight record profit, but uncertainty in India and a possible uptick in spending threaten to cut short that streak.

For the all-important holiday quarter, Amazon reported its profit topped $3 billion for the first time, jumping 63% from a year earlier. The company has been taming its operating costs, and profitable businesses like cloud computing, advertising and the services it offers sellers on its site have helped offset the lower margins of its traditional retail business.

Amazon has few financial trouble spots. But the company on Thursday warned that government restrictions in India could crimp its revenue there. And it cautioned that spending is likely to increase this year as it continues to build out its warehouses and other infrastructure.

While the Seattle retailer's revenue remains double what it was three years ago, growth has slowed for three straight quarters. Revenue in 2018's final period rose 19.7% to $72.38 billion, the smallest quarterly jump since 2015.

Amazon forecast revenue of $56 billion to $60 billion for the current quarter, below a consensus analyst estimate of $60.83 billion, according to FactSet. On the low end of Amazon's range, revenue would be up only about 10% from a year earlier. That would amount to its worst showing since 2001, though analysts caution Amazon is often conservative with projections.

Following the report and analyst call, Amazon's shares fell nearly 5% in after-hours trading Thursday.

"The guidance is disappointing," said Kian Salehizadeh, senior analyst for Blockforce Capital, which holds shares in Amazon. Investors are "concerned about the global macroeconomic headwinds that they're going to face, along with the impact of the costs associated with higher minimum wage" and other factors, he said.

Amazon in recent quarters has demonstrated stronger financial discipline, leading to record profits despite spending aggressively to deliver more of its packages and stretch into new industries like groceries and health care. Investors have rewarded the company by boosting its stock. As of Thursday's market close, Amazon held the crown of the world's most-valuable public company; last year it briefly touched $1 trillion in market value before a broad selloff in technology stocks.

But Amazon and the biggest technology companies are entering a new phase of unevenness after a few years of runaway success.

Apple Inc. on Tuesday recorded its first holiday-quarter decline in revenue and profit in over a decade, while Microsoft Corp. warned chip shortages are eating into its core Windows business. Facebook Inc. last quarter signaled its growth was slowing after a year of data-privacy controversies, but on Wednesday posted record quarterly profit.

In particular, companies flagged concerns about uncertainty tied to international expansion. Worries about a slowdown in China's economy are putting pressure on some companies' sales, including at Apple and chip makers Qualcomm Inc. and Nvidia Corp.

For Amazon, the unease is in India. The country is tightening restrictions on foreign e-commerce companies operating there, enforcing a rule that keeps them from holding or shipping their own inventory. The government on Feb. 1 is eliminating a loophole that allowed non-Indian online sellers to sell via affiliated local companies. India also is no longer permitting exclusive online sales agreements, like one Amazon had for OnePlus smartphones, a popular Chinese brand.

“We do believe that India remains a good long-term opportunity,” Amazon’s financial chief, Brian Olsavsky, said in an interview with media. “As far as the change of this rule, these regulations, we’re still evaluating them and there’s a bit of uncertainty at this point.”

Amazon has been a leader in India’s e-commerce market since launching there in 2013, and Chief Executive Jeff Bezos previously pledged $5 billion to expand operations there. The market is expected to boom to $72 billion in 2022, from about $33 billion last year, according to eMarketer.

Despite the trouble in India, growth in Amazon’s international sales accelerated in the fourth quarter to 19%, from 15% three months earlier, excluding foreign-currency effects. Amazon is also relying more heavily on independent merchants selling on its site, which is increasing its product selection, and in many cases, improving profitability.

The company said 52% of units sold on the site in the quarter were via merchants. Amazon typically takes in a 15% cut of sales, plus warehousing fees and advertising revenue. That business can be cheaper than selling an item itself; plus it can reduce risk of holding inventory that doesn’t sell.

Third-party seller services grew 27% to $13.38 billion in revenue. While revenue is booming, the company has struggled to eliminate scammers trying to game the site’s algorithm that ranks products based on reviews, sales and other factors.

As the site continues to expand, Amazon is having to build out its warehouses to meet the surging retail demand. The company spent heavily in recent years, resulting in tight profit margins. It took a breather in 2018, but Mr. Olsavsky warned on the analyst call that Amazon could pick up spending again.

“in a lot of ways, 2018 was about banking the efficiencies of investments in people, warehouses, infrastructure that we had put in place in 2016 and ‘17,” Mr. Olsavsky said. “I would expect those investments to increase relative to 2018.”

Mr. Bezos has never been shy about his strategy to think long-term and invest heavily to promote growth. Every year he attaches his 1997 missive to shareholders touting that mantra to his annual shareholder letter.

“This really isn’t a change in strategy, and honestly I would be more concerned if Amazon didn’t have a lot of growth opportunities that require spending,” said Colin Sebastian, an analyst with Robert W. Baird & Co.

Meanwhile, the company is pushing further into physical retail, a business that can prove costly. It has opened several cashier-less Amazon Go stores and bookstores, and acquired the Whole Foods grocery chain in August 2017. Amazon has been pushing Prime deals and price cuts at Whole Foods. Revenue for its physical stores segment—mostly Whole Foods—fell 3% to $4.4 billion in the latest period.

Mr. Olsavsky said lower revenue at Whole Foods was attributable to the year-earlier quarter having more calendar days. On a comparable basis, the chain would have reported 6% sales growth, he said.

That figure doesn’t include the new delivery and pickup services the grocery chain has added, which are tallied under online sales.

World-wide shipping costs rose 23% to $9.04 billion in the quarter, a lower percentage than a year earlier. Mr. Olsavsky pinned some of the rise in costs on a wider offer of free shipping during the quarter, as well as speedier delivery options.

“As we continue to expand our Amazon Logistics deliveries, we’re seeing very high delivery estimate accuracy and competitive costs.”

Sales in Amazon Web Services, which rents computing power to companies and the government, rose 45% to $7.43 billion. The growth was in line with previous, a promising sign after Microsoft reported slowing sales growth in its cloud business. Amazon effectively invented the category and had a big head start before facing competition from Microsoft and Google. It has lowered some prices to stay competitive in the market.

Amazon is also taking a share of the digital-advertising business, albeit small, away from Google and Facebook as brands advertise more on the online retailer’s site. Amazon’s “other” category, which is primarily derived from advertising, nearly doubled to $3.39 billion.

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