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# Amazon Whole Foods Merger

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## ABSTRACT

*The Amazon-Wholefoods Takeover is an interesting study as to how the Online Retail giant successfully initiated an undertaking to enter into the Brick and Mortar business by integrating Wholefoods into Amazon by issuing initiatives, and ensuring that this deal did not go south. The author would like to present an interesting perspective on the background of the merger, the legal connotations with regards to the present merger and what this merger meant to amazon with present time references to the then 2016-17 business environment. Amazon has been the world's most successful online retail giant, and that is not without credit, its successful navigation of the arena and diverse approach has made Amazon an indisputably efficient machine catering to the different needs of its consumers. The Approach wherein Amazon Places the needs of its consumers at the forefronts is extremely important and needs to be considered. The Author would be presenting her perspective on the aspects that led to the success of this mega-deal.*

**Keywords:** Amazon-Wholefoods, Merger, Vertical Mergers, Goldman Sachs, Brick & Mortar

## I. INTRODUCTION

In March 2017 Amazon announced Amazon Fresh Pickup, a drive-in type grocery store for Amazon Prime subscribers<sup>3</sup>. In January 2018, Amazon started up offline retailing Amazon Go, first brick-and-mortar convenience food store on Amazon. However, its grocery margins were low, and its goods were difficult to deliver considering their perishability nature. Amazon Go store's technology faced problem in tracking over 20 people<sup>4</sup>. It wanted to transform this dynamic. Thus, the Amazon wholefoods deal transcribed when Amazon sensed the need for having its footprint in the physical stores combined with online stores. Amazon saw a grocery business as an emerging business opportunity<sup>5</sup>. The author would like to analyse the amazon-

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<sup>3</sup> Alvarez, José B., David Lane, and Joni Coughlin. "Amazon Buys Whole Foods." Harvard Business School Case 518-056, December 2017. (Revised May 2018.)

<sup>4</sup> Simon, Hermann, 'Whole foods is becoming Amazon's brick and mortar pricing lab.', Harvard Business Review, <https://hbr.org/2017/09/whole-foods-is-becoming-amazons-brick-and-mortar-pricing-lab>.

<sup>5</sup> Turner, Nick, Selina Wang and Spencer Soper. 2017. "Amazon to Acquire Whole Foods for \$13.7 Billion". *Bloomberg*. <https://www.bloomberg.com/news/articles/2017-06-16/amazon-to-acquire-whole-foods-in-13-7-billion-bet-on-groceries>.

wholefoods merger by firstly, broaching upon the details of the merger and the kind of merger amazon-wholefoods was as regards the lines of production and distribution<sup>6</sup>. Secondly, there were several antitrust concerns that were raised when the merger was announced initially in 2017 and the Federal Trade Commission's approval of the merger would be discussed to analyse the scenario when the deal transcribed<sup>7</sup>.

### **(A) Research Methodology**

The Research Methodology is in the form of doctrinal Research, wherein the Secondary Sources used to collect information is through research papers, journals, research articles, insurance law books, Newspaper and other Online resources. This paper is strictly limited to the theoretical underpinning as regards the present topic.

### **(B) Research Objectives**

The Author has researched on the present topic to understand the nuances of a Successful Merger, the reasons why conglomerates enter into mergers, the Legal Points and Lacunae in the amazon-wholefoods merger. The Author would like to study how vertical integrations work in the world as compared to horizontal integrations. The Author in her present paper has provided a unique perspective on the Amazon-Whole Foods Takeover.

## **II. REASON'S FOR THE MATERIALISATION OF A SUCCESSFUL TAKEOVER**

Amazon's decision to Acquire Whole Foods may be looked at in different ways, firstly the two companies are operating in unrelated industries and this might challenge the integration process. It might be extensive when two companies in unrelated industries decide to merge and this might be due to a weakness in the overlap of knowledge<sup>8</sup>. But, in the Amazon Whole Food's deal and the strategy behind the deal we observe several complementary resources and capabilities. Such as,

**A Fast entry in the Organic Foods Industry:** The Organic Food Industry in the US is fast-growing with an increase in the consumer base. Amazon has its contact with a foods distribution network already with its earlier initiative Amazon Fresh but Amazon Fresh was insignificant in the Organic Food Industry when compared with other players such as the Grocery chains. Amazon to become successful in the Organic Food Industry had two options

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<sup>6</sup> Walsh, Mark. "The future of e-commerce: bricks and mortar". 2017. The Guardian. <https://www.theguardian.com/business/2016/jan/30/future-of-e-commerce-bricks-and-mortar>

<sup>7</sup> Zacks Investment Research. "An Illustrated Timeline of Amazon's Biggest Mergers and Acquisitions". 2017. *NASDAQ*. <http://www.nasdaq.com/article/an-illustrated-timeline-of-amazons-biggest-mergers-and-acquisitions-cm806540>

<sup>8</sup> Alanna Rose Harding, *Accretion Analysis Of The Amazon – Whole Foods Acquisition*, The Pennsylvania State University Schreyer Honors College, 2017.

to either acquire an established company in the industry or grow organically, If Amazon Acquired Wholefoods this would provide Amazon with instant access to more than 460 physical stores and more access to different spectrums of products<sup>9</sup>. Another aspect to be considered is the fact that they require a certification from the U.S. Foods and Drug Administration, and extra care in terms of hygiene, different kinds of cooling system and there are other such requirements which whole foods guarantees that can be utilized by Amazon.

Further, there exist certain surveys which indicate a considerable overlap between the consumers for the two companies which especially consist of millennials<sup>10</sup>. Through this merger Amazon would not only have access to whole Foods loyal consumer base but through this deal it would be able to create its own batch of loyal consumers.

**Expanding Amazon's Distribution Channels:** Whole Foods stores can function as warehouses for Amazon's consumer's orders. This could provide Amazon the opportunity to attract consumers in the Population centres and also provides an option to its consumers to collect or return their Amazon Orders to a Whole Foods Store<sup>11</sup>.

This also helped Amazon learn about the '**Offline Behaviour**' of its consumers. Amazon's strongest feature is its ability to predict what its online consumers want to buy. The data obtained from wholefoods can be served as a test for Amazon's future moves into 'offline' businesses.

### III. THE STOCK MARKET REACTION ON ANNOUNCEMENT OF THE ACQUISITION

Amazon's stock prices rose when the Amazon-Wholefoods merger was announced and the stock of its competitors such as Kroger's, Ahold Delhaize and Costco took a massive hit. This drastic reaction was due to the fact that it was a terrifying prospect for these businesses to compete with Amazon.<sup>12</sup> Amazon introduces schemes where it may suffer losses but wherein it manages to attract a loyal consumer base and the grocery chains already operate on thin margins of profit, thus the entry of Amazon into grocery was not received with enthusiasm by its competitors in the arena.

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<sup>9</sup> AGREEMENT AND PLAN OF MERGER by and among AMAZON.COM, INC., and WHOLE FOODS MARKET, INC. Dated as of June 15, 2017. <https://www.sec.gov/Archives/edgar/data/1018724/000119312517205287/d352949dex21.html>

<sup>10</sup> Phillips-Connolly and Connolly, When Amazon ate Whole Foods: big changes for Big Food, International Food and Agribusiness Management Review Volume 20 Issue 5, 201.

<sup>11</sup> Andrejs Čirjevskis, The Transformation of Business Models in Technology-Enabled M&A: A Case Study of Amazon, Strategy and Behaviors in the Digital Economy, IntechOpen, pp.1-18.

<sup>12</sup> Sarah Whitten, *Whole Food stock rockets 28% on \$13.7 billion Amazon takeover deal*, CNBC (June 16, 2017, 1:00PM EDT), <https://www.cnbc.com/2017/06/16/amazon-is-buying-whole-foods-in-a-deal-valued-at-13-point-7-billion.html>

#### IV. DETAILS OF THE TAKEOVER

The amazon-wholefoods takeover was a friendly merger with amazon offering to buy wholefood shares at \$ 42 per share at 13.7 billion at a 27 percent premium. This is an example of a vertical merger wherein two firms (or more) who provide services at different parts of a supply chain come together for a common good or service<sup>13</sup>. In the present case this vertical merger provides the online retailer physical stores to render its grocery services. Initially amazon did not own local grown produce or food distributors, but after this deal Amazon has a distribution centre and a company that has contracts in place for local, organic produce. Instead of contracting with other companies that do something similar so that it can sell the products online, it owns the distribution channel to do that itself<sup>14</sup>.

#### V. ANTI-TRUST CONCERNS & LEGAL ISSUES

The anti-trust concerns raised in the present case was that amazon acquiring wholefoods could cause amazon acquiring monopolistic power due to economies of scale. The scale of amazon's business increased after the \$14 merger with a 460-store acquisition<sup>15</sup>. An increase in the product (scale) will lower the average cost per unit and this would in turn create economies of scale. This will give amazon more market power pushing it to economies of scale. Section 7 of the Clayton Act prohibits mergers and acquisitions where the effect may substantially lessen competition or tend to create a monopoly. Amazon initially faced anti-trust issues because it was nearing monopoly status<sup>16</sup>. Nonetheless the deal was ultimately passed by the Federal Trade Commission because the anti-trust laws on this particular topic were on amazon's side.

In *United States v. Grinell Corp.*<sup>17</sup>, stated that antitrust law favoured firms which obtained market share due to a superior product or better business acumen. And in the present case Amazon's consumer reach was in a large part due to the offering a superior product in the form of easy-to-use interface for both buyers and sellers as well as business acumen in the development of a superior system of distribution and logistics, as well as the historic accident of being an early entrant into the market during the dot-com boom. Further, wholefoods only

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<sup>13</sup> Griswold, Alison. "Amazon and Whole Foods have very different customers, and that's great news for both of them". 2017. *Quartz Media*. <https://qz.com/1077662/amazon-prime-could-double-whole-foods-shoppers-over-the-next-five-years-morgan-stanley/>

<sup>14</sup> Tim Barrett. "AMAZON.COM INC IN RETAILING". 2017. *Euromonitor International*.

<sup>15</sup> Mark Zandi and Adam Ozimek, *Where Amazon's Next Headquarters Should Go*, Moody's Analytics (Oct. 12, 2017), <https://www.economy.com/dismal/analysis/commentary/298321/Where-Amazons-Next-Headquarters-Should-Go/>.

<sup>16</sup> Winerman, Marc. "THE ORIGINS OF THE FTC: CONCENTRATION, COOPERATION, CONTROL, AND COMPETITION." *Antitrust Law Journal*, vol. 71, no. 1, 2003, pp. 1-97.

<sup>17</sup> *United States v. Grinell Corp.*, 384 US 563 (1966).

held a 3.5 percent market share. Additionally, the FTC tends to look more favourably upon companies which vertically integrate than horizontal integrations<sup>18</sup>. To address monopoly concerns it is important to note that the economies of scale Amazon is developing, it can lower prices, creating “a net positive for consumers.” Regulators are unlikely to call a company a monopoly if it lowers prices for consumers. A possible hang-up is curbing innovation, as new barriers to entry are created.

It is to be noted that Vertical integrations, such as the one between Amazon and Whole Foods, do not lessen competition but, rather, just add a step in the production process. Through the FTC’s history, many deals have succeeded because of this distinction<sup>19</sup>. A stellar example would be the Disney-Pixar merger of 2006 where Disney purchased Pixar for \$7.4 billion. Disney, which produces entertainment through many mediums, saw Pixar as a tool for its “flagging animation ambitions.” Pixar would be the designer for Disney’s animation studio, in which its products could be produced and completed through Disney’s chain. The contract between the two studios was ending, and the merger made the relationship permanent. This is a clear example of a vertical integration and, as such, did not face any problems with the FTC<sup>20</sup>.

There have been a few mega-deals that were not as lucky as the Amazon-Whole Foods deal. The key is to look for a decrease in competition<sup>21</sup>. In 2002, two of the United States’ largest satellite companies i.e. EchoStar and DirecTV wanted to merge, creating a horizontal merger. EchoStar tried to purchase DirecTV for \$15 billion, and had the deal been successful, EchoStar would have served one-fifth of U.S. households as the nation’s only satellite provider. Regulators, however, struck the deal down because it would “replace a vibrant competitive market with a regulated monopoly.”<sup>22</sup> Then in 2011, AT&T attempted to purchase T-Mobile for \$39 billion, but it was struck down by the FTC because it would “substantially lessen competition.”<sup>23</sup> The FTC has thus been clear that when a merger significantly decreases competition, it will be barred by antitrust law<sup>24</sup>. As for Amazon, its merger with Whole Foods does not lessen competition; it just adds a step to the process making it a vertical merger. Amazon is a customer-centric company, constantly evolving and testing all aspects of its

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<sup>18</sup> *Rebel Oil Co. Inc v. Atlantic Richfield Co.*, 808 F. Supp. 1464. (D. Nev. 1992)

<sup>19</sup> Rakesh Chinata, “Disney Pixar – A Strategic Merger”- A Case Study, Harvard Strategic Management, 2018.

<sup>20</sup> <https://www.icmrindia.org/casestudies/catalogue/business%20strategy/Disney's%20Acquisition%20of%20Pixar.htm>. ‘Disney’s Acquisition of Pixar.’

<sup>21</sup> *Supra* n. 9.

<sup>22</sup> <https://www.fcc.gov/general/echo-star-directv-merger-page>. EchoStar and Direct TV Merger Declined, Federal Communications Commission.

<sup>23</sup> <https://www.fcc.gov/proceedings-actions/mergers-transactions/att-and-t-mobile>. AT & T and T-Mobile Merger Declined, Federal Communications Commission.

<sup>24</sup> *United States v. H&R Block, Inc.*, 833 F. Supp. 2d 36, 81 (D.D.C. 2011).

operations in pursuit of fulfilling its customers' desires. They are now able to provide a missing category of product to customers, thus increasing an already large annual spend. For competitors, retaining or attempting to capture new market share will be challenging.

#### Current Status of the Acquisition – Integration of Amazon Prime in Whole Foods

Today, Amazon's Prime program is fully integrated in the Whole Foods stores. Amazon has started selling its devices such as Echo at the Whole Food stores. The Prime members have several new services available to them such as 60-minute delivery service, curbside pickup of Whole Foods online orders, Amazon lockers for online order pickup as well as special discounts, cashbacks and loyalty programmes.<sup>25</sup>

Closer analyses of the statistics show a significant overlap between the target market demographic of Amazon Prime and Whole Foods. Whole Foods had a niche but well-established customer base of loyal consumers belonging to a high spending demographic commonly referred to as 'urban influencers'. This demographic includes highly educated, high-income consumers mostly comprising of women and millennials who often spend more time and money shopping online compared with other segments of the population.<sup>26</sup>

## VI. 2018-2019 MARKET SHARES: A BRIEF PERSPECTIVE

At the end of 2019, Walmart and Kroger were the top two leaders in the grocery sector. Walmart's market share amounted to 21.3%, Kroger ranked second with a share of 9.9% and Costco ranked third with a share of 5%. Amazon and Whole Foods, by comparison, accounted for only 2.2% of the US grocery market in 2019, which shows a significant increase from 1.4% in 2017, at the time of the acquisition.<sup>27</sup>

When Amazon's acquisition of Whole Foods was announced, many analysts had speculated that Amazon would become the top market player and dominate the grocery sector both online and offline. However, the drastic increase in the share prices of Amazon when the acquisition was announced was temporary overreaction.

It is pertinent to note that the acquisition significantly expanded Amazon's reach offline. In the past few years, the consumers have demonstrated a growing appetite for buying groceries

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<sup>25</sup> Steve Banker, *How Amazon Changed Whole Foods*, Forbes (June 25, 2019, 09:02AM EDT), <https://www.forbes.com/sites/stevebanker/2019/06/25/how-amazon-changed-whole-foods>

<sup>26</sup> Russell Redman, *Whole Foods- Amazon steams ahead with Prime*, U.S. Supermarket news (Sept. 26, 2018, 11:00AM) <https://www.supermarketnews.com/online-retail/whole-foods-amazon-steam-ahead-prime-now>.

<sup>27</sup> Hayley Peterson, *The grocery wars are intensifying with Walmart and Kroger in the lead and Amazon poised to 'cause disruption'*, (Jan. 31, 2020, 00:18 IST), <https://www.businessinsider.in/tech/news/the-grocery-wars-are-intensifying-with-walmart-and-kroger-in-the-lead-and-amazon-poised-to-cause-disruption/articleshow/73781449.cms>

online, and the online sales and ecommerce's share of total sales continues to climb for supermarket chains. Within the first few months of the acquisition, Walmart had managed to capture 30% of the online grocery sales in the US which is as much as all the grocery stores combined. This number almost doubled in 2020, at the time of the Pandemic. Amazon's acquisition proved to be an incredibly smart decision currently where a large percentage of customers have shifted online for grocery shopping.

## **VII. IMPACT ON THE RETAIL GROCERY SECTOR**

Gaining access to Whole Foods' network of food suppliers and distributors has increased Amazon's influence in vendor negotiations by pushing competitors' profit margins down. Amazon's power to negotiate ever-lower prices with suppliers means food deflation pressures which negatively impact profit margins for competitors while still benefiting consumers.

That fear motivated some of the largest grocers and mass merchants to amp up their grocery services in the years following the acquisition. For example - in November 2017, grocery chain operator Albertsons Cos. Inc. started online grocery delivery for orders on JewelOsco.com in select markets, in addition to its home delivery program for its Safeway grocery stores. In the past year, grocery stores have slowed their new store growth and instead focused on acquisitions of technology or platforms. Walmart bought Indian e-commerce company Flipkart, Target bought delivery service Shipt, Kroger invested in British online supermarket Ocado and bought meal kit company Home Chef, and Albertsons also bought a meal kit company, Plated. Although many grocery chains continue to invest heavily in technology, the reality is that playing catch-up with an e-commerce giant is extremely challenging.

## **VIII. CONCLUSION**

While the retailers consider both defensive and partnering strategies with Amazon, navigating toward the success of true north likely need not be a solo journey. Instead of trying to compete on individual effort, technological investments, acquisitions, and isolated operational improvements, retailers should consider calculating the benefits of joining or forming an ecosystem of complementary partners with expertise in delivery, social media, digital payments, e-commerce, and distribution platforms. The goal could be to create a virtual, transaction-based dream team of superheroes that can be dedicated to surviving and thriving. Only then will they have a chance at competing with a giant like Amazon.

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