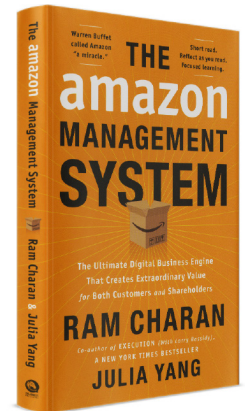


# The Amazon Management System

The Ultimate Digital Business Engine That Creates Extraordinary Value for Both Customers and Shareholders

by **Ram Charan and Julia Yang**



## Contents

Building Block 1: Customer-Obsessed Business Model

Page 2

Building Block 2: Continuous Bar-Raising Talent Pool

Page 3

Building Block 3: AI-Powered Data and Metrics System

Page 4

Building Block 4: Groundbreaking Invention Machine

Page 5

Building Block 5: High-Velocity and High-Quality Decision-Making

Page 6

Building Block 6: Forever-Day-1 Culture

Page 7

## THE SUMMARY IN BRIEF

The arrival of the digital pioneers, such as Amazon's founder and CEO Jeff Bezos, has disrupted corporate leadership models of the past. Amazon's trillion-dollar success is the envy of everyone but achievable by anyone. What has propelled their record streak of growth? Their management system, and it can do the same for you no matter what business you are in or what level.

Soon, all companies will be digital, which means traditional command-and-control management will no longer be relevant. Learning Amazon's system is as simple as six building blocks distilled by *New York Times* best-selling author and global CEO advisor Ram Charan and Julia Yang, in *The Amazon Management System*.

From high-velocity decision-making to top talent-hiring practices, the insider secrets behind Amazon's success are now within anyone's grasp, block by block. Whether you are an established CEO or a recent college grad, *The Amazon Management System's* concise, actionable advice will help your business win in a new digital era that demands nonstop innovation.

## IN THIS SUMMARY, YOU WILL LEARN:

- The six building blocks of Amazon's management system.
- Why customer obsession is Amazon's number-one principle.
- How Amazon defines, motivates, and retains the right talent.
- How the company continuously generates groundbreaking inventions.

## Introduction

Our 21st century prevailing management systems are still largely inherited from the oldest forms of human organization, such as the military and the church. They were designed for the purpose of command and control in an age when there was no internet, no smartphone, and none of the various forms of digital technology such as big data, algorithms, and AI, and when personal supervision was the only way to keep an eye on employees.

This old management approach has become obsolete in the digital age. Amazon is one of the biggest reasons why.

At the heart of all Amazon's business endeavors is the Amazon management system, a digital engine composed of six building blocks, that has been continuously and relentlessly empowering Amazon for more growth and more exploration into the unlimited sky of the digital age.

### It's a Must, Not Optional

Going forward, all companies will be digital. Every company will have a platform of its own and/or be connected to someone else's platform. For founders and business owners, the good news is that most of your legacy peers have not started down this path yet, so if you get a head start on embarking on the digitization journey, you may improve your chances to take the lead.

The choice is yours to make: to die or to digitize and achieve exponential value creation.

For senior executives, in the digital age your job will change radically. Instead of spending most of your time supervising others and attending endless reviews, meetings, and committees, your job will be to study consumers directly (not through filters) and drive continuous innovation for them.

As more companies make the transition to the kinds of Amazon management practices described here, leaders will remove management layers, requiring junior to middle managers to reimagine their jobs and rebuild their competence.

There has never been a better era for new talent—the young and fresh. The more you understand the Amazon management system, the more contributions you can make, and the more successful you will be in your career, whether you are working for a company or starting your own.

The point is not to advocate a blind replication of all and

everything in the Amazon management system but to help you understand how it works and pick the valuable ingredients and inspirations for your own digital way.

Let's now learn the six building blocks of Amazon's management system.

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## Building Block 1: Customer-Obsessed Business Model

The first principle that Amazon founder and CEO Jeff Bezos stated in his famous nine-point management and decision-making approach published in his first Shareholder Letter in 1997 is, "We will continue to focus relentlessly on our customers." Among all 14 Leadership Principles, Customer Obsession ranked number one and has remained at the top ever since.

Why has Bezos been so obsessed with the customers? Customers are the central piece in Amazon's flywheel and in the entire Amazon platform. Why is Amazon able to aggressively and successfully expand into more and more categories? Because they have customers who would like to buy more. Why are third-party sellers attracted to the Amazon platform? One of the most obvious reasons is that there are hundreds of millions of customers, and by leveraging the Amazon platform, they can scale up much faster.

Customers' trust is an earned privilege, not a long-term benefit to be taken for granted. Trust takes years to build, seconds to break, and forever to repair. That's probably why Bezos emphasized, "Our pricing objective is to earn customer trust, not to optimize short-term profit dollars."

### Invent for the Customers

As Bezos put it, "One thing I love about customers is that they are divinely discontent. Their expectations are never static—they go up. It's human nature." How do we not just meet but stay ahead of customers' ever-rising expectations? The only way to do this is through continuous innovation and relentless invention. In this way, the divinely discontent customers became the sources of continuous inspiration for Amazon's invention machine.

Unlike traditional companies that primarily use technology for cost reduction, Amazon focuses on using technology to totally transform the existing customer experience and to imagine an experience that does not exist today, and invent on behalf of the customers.

# Why is long-term thinking so important for Amazon? The secret is in the very nature of its business model.

In the spirit of this relentless drive to invent, Amazon single-handedly created entirely new markets with huge global potential, such as cloud services (AWS) and smart speakers (Echo). As Bezos pointed out, “No one asked for AWS. No one. Turns out the world was in fact ready and hungry for an offering like AWS but didn’t know it. We had a hunch, followed our curiosity, took the necessary financial risks, and began building—reworking, experimenting, and iterating countless times as we proceeded.”

## Long-Term Thinking

In his first shareholder letter, Bezos said that Amazon “will continue to make investment decisions in light of long-term market leadership considerations rather than short-term profitability considerations or short-term Wall Street reactions.”

Why is long-term thinking so important for Amazon? The secret is in the very nature of its business model. Amazon is all about platform and infrastructure. So it is, in essence, a scale business characterized by high fixed costs and relatively low variable costs.

So how to drive the return on such a massive investment? Scale and speed really matter here. According to company shareholder letters, increasing scale “spreads fixed costs across more sales, reducing cost per unit, which makes possible more price reductions.”

Once the scale passes a certain threshold, what Bezos calls the “tipping point,” it “allows us to launch new e-commerce businesses faster, with a higher quality of customer experience, a lower incremental cost, a higher chance of success, and a faster path to scale and profitability than any other company.”

Second is speed. Platform and infrastructure are a technology game. Prior investments and faster movements captivate a larger customer base earlier and accumulate historical data earlier, which translates into significant first-mover advantages in data analytics, algorithm enhancements, and AI-driven solutions. In short, all these elements combined create Amazon’s digital core competencies.

## Building Block 2: Continuous Bar-Raising Talent Pool

If you ask Bezos what the most important decision is at Amazon, his answer will be and has always been from the very beginning: hiring the right talent.

So what has Amazon done to make sure that they only attract and retain the right talent? In the first place, what is “right” by Amazon’s standards? Bezos looks for builders who can make things happen, who can think and behave like owners—the type of people who display a sense of “true ownership.”

In his 2018 Shareholder Letter, he wrote, “Builders are people who are curious, explorers. They like to invent. Even when they’re experts, they are ‘fresh’ with a beginner’s mind. They see the way we do things as just the way we do things now. A builder’s mentality helps us approach big, hard-to-solve opportunities with a humble conviction that success can come through iteration: invent, launch, reinvent, relaunch, start over, rinse, repeat, again and again. They know the path to success is anything but straight.”

Amazon is now a burgeoning 750,000-people organization, so how to reinforce such rigor and maintain such a high bar—not only across the globe but also down to each new hire?

## The Bar Raisers

Bar raisers are carefully selected individuals who are meticulously trained to be the stewards of Amazon’s leadership principles. Their mission is to ensure that the bar is never lowered due to pressing business urgency, to make the final and right hiring decisions, and to strive for continuous raising of the bar. In many ways, they act on behalf of the Amazon leadership team as the final line of defense in recruiting.

Bar raisers have three tasks. The first is to evaluate, using Amazon’s Leadership Principles as the yardstick, whether candidates have long-term potential at Amazon and whether they can raise the bar. The second is to conduct the post-interview drilling with each interviewer, as Bezos did before, so that all observations, assessments, considerations,

and doubts can be fully explored and thoroughly examined to arrive at a correct decision. The third is to help hiring managers and other interviewers prepare for interviews, to ensure consistency in the high bar, and most importantly, to provide written feedback.

Given that recruiting the right talent is regarded as the most important decision at Amazon, the company has made huge investment, in terms of teams' time and energy, into getting this right.

## Motivate and Retain the Right Talent

Given that Amazon's bar is so high and continuously rising and the short-term cash compensation is not so lucrative, how can Amazon motivate and retain the real builders with true ownership and mental toughness on a long-term basis? The answer lies in two aspects: what they love and what they hate.

What do builders hate most? Bureaucracy. It is slow; it is suffocating; and in many cases it prevents them from making things happen in the way they like. Such an atmosphere is anathema to builders, who love to invent and to try unconventional ways. They have little patience and want to jump in and make things happen. For Bezos, the abhorrence of bureaucracy is personal.

Above all, builders love challenges. The problems that appear to be hard to solve or even impossible for many people represent something entirely different to the real builders. They see these problems as exciting opportunities, the best thrills, and the most fun part of the job.

At Amazon, new hires are pleasantly surprised at how much ownership they can have from the start. When they are assigned to a project team, they will be exposed to and engaged in all functions involved, and make decisions and build products that could potentially impact millions of customers.

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## Building Block 3: AI-Powered Data and Metrics System

Running Amazon, the gigantic business empire with unprecedented complexity from drastically different businesses, from vastly spanned geographies worldwide and from the massive size and scope of operations, is no doubt a daunting challenge for many.

Without digitization, one could not do that. Bezos' secret lies in Amazon's world-class standard-setting AI-powered data and metrics system, in which everything that matters

can be tracked, measured, and analyzed, with insights generated and routine decisions automated.

## The Answer Starts With Numbers

Jeff Bezos is a man of numbers. This is his unique way of understanding the world, having fun in life, and running business at Amazon. Bezos has unique standards to define what the robust data and metrics are.

**Ultra-detailed.** Execution is about knowing and delivering details. Amazon's level of details for data and metrics is magnitudes beyond many people's wildest imagination. If you were asked to pick a location for a new data center, how many factors would you consider? About five, 10, 20, or dozens? Amazon used a checklist of 282 metrics when choosing its first data center in China.

**End to end.** In most traditional companies, data collection is broken down by silo, by layer, and by actual involvement. Each division or function can see data generated and collected only within its own domain of business operations.

At Amazon, a small team is bestowed with the end-to-end responsibility for one product or one service. How to ensure that this team does a good job? After ensuring the selection of the best people, the next most important crucial enabler is the availability of end-to-end data that is not segregated by silo nor by function. Without such data support, running a business would be as difficult as maneuvering in a pitch-dark mansion.

**Real time.** In many companies, business reviews are held quarterly or monthly, with a delay of 10 days or more due to the time needed for accounting proceedings. At Amazon, such data is tracked on a real-time basis with no time lag. Relevant people can review the results daily, hourly, or by the second.

**Track inputs.** This is probably the most unique aspect of Amazon's data and metrics system. When setting goals, most companies focus on revenue growth, margins, and net profits. Amazon believes that to ensure good outputs, one needs to get to the bottom of the issue and seriously track the inputs. Why does Amazon track the time required to load a webpage? Because according to Brad Stone in *The Everything Store*, its data analytics shows that "even a minuscule 0.1-second delay in a webpage loading can translate into a 1 percent drop in customer activity."

**Trust but verify.** At Amazon, each claim needs to be supported by data and metrics. Unfounded promises will not fly.

## The AI-Powered Tools

Bezos' personal passion for technology and signature spirit of imagining and inventing have become one of Amazon's underlying characteristics. The applications of this approach are countless and inform virtually all key decisions made by Amazon. How does Amazon pick the location of its next fulfillment center? The answer is Mechanical Sensei, a software system "that simulated all the orders coursing through Amazon's fulfillment centers and predicted where new FCs would most productively be located," according to Stone.

How does Amazon ensure its competitiveness in pricing? Pricing bots. Stone writes that these are "automated programs that crawled the Web, spied on competitors' prices, and then adjusted Amazon's prices accordingly, ensuring that Bezos' adamant demand that the company always match the lowest price anywhere, offline or online, would be met."

How does Amazon drive more consumption from each consumer? Personalized recommendations. And who at Amazon decides which items to recommend to which customers? Actually . . . no one. An algorithm-enabled system fully automates personalized recommendations for each individual consumer.

How does Amazon develop options and decide the fastest and cheapest delivery option for each order? By the early 2000s, an Amazon fulfillment software system could run millions of such decisions every hour. Given Amazon's relentless pursuit of improvement, its highly sophisticated fulfillment software systems have been on a never-ending treadmill of iterations ever since creation.

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## Building Block 4: Groundbreaking Invention Machine

What makes Amazon an outlier above all others is the sheer power of its identity as an invention machine: one that is able to deliver continuously, and at an ever-accelerating pace, groundbreaking, game-changing, and customer behavior-shaping inventions that create new market spaces and economic opportunities of massive magnitude.

That's probably why *Fortune* described Bezos as "the ultimate disruptor" in 2012, *Fast Company* named Amazon the world's most innovative company in 2017, and *Forbes* put Amazon on its list of World's Most Innovative Companies in 2018.

All great inventions need to start with an idea, a brilliant one, a revolutionary one, or a seemingly impossible one.

So how does Amazon continuously generate new ideas and meticulously pick which ones to pursue?

**Seek big ideas continuously.** Amazon invented the "idea tool," to tap into employees' creativity and imagination. Anyone who has an idea can submit his or her thoughts without filters of layers of managers or concerns about feasibility from either technical or financial points of view. In addition to the people inside Amazon, Bezos also seeks ideas from those outside.

What makes Amazon an outlier above all others is the sheer power of its identity as an invention machine.

At Amazon, the ideal adventure to create is not aimed at merely 100 or 1000 people. Bezos seeks inventions that speak to billions of customers and millions of enterprises worldwide. Why so big? Because of the risky nature of invention, in which failure and invention are inseparable twins. What could offset the numerous failures along the way? A big win, such as AWS.

The company must invent on behalf of customers, and the idea must be distinctly differentiated. Amazon Go is the perfect example. This venture, as described in Amazon Shareholder Letters, called for a complete re-imagination of a whole new customer experience: walking into a store, picking up what is needed and just walking out, without "annoying and lasting-forever checkout lines" anymore. Many customers describe the experience of shopping at Amazon Go as "magical."

**Build the idea patiently.** It all starts with the press release, an internal document that looks at what the future would be like with the successful execution of the idea being proposed. Three things play pivotal roles in such releases:

- Who are the customers? How will they use it? What is their new experience? Which existing experience will it replace? What changes will it require them to make? Why will they prefer it? What are the benefits in the

eyes of the customers?

- What are the goals? They need to be bold, specific, and measurable. What drives creativity? It's the challenges. If something gets too easy, people's true creativity will be left underutilized or even untapped.
- What are the hurdles? To convert a big idea—one that is distinctively differentiated, uniquely Amazon, and even seemingly impossible—into reality is never easy. After all, there must be almost insurmountable hurdles that prevent others from trying or even imagining the possibility of success.

**Construct the team carefully.** Amazon has a well-known approach to drive project development: the two-pizza team, or as Amazon refers to it, 2PT. As Bezos repeatedly pointed out, if you can't feed a team with two pizzas, the team is probably too big.

At Amazon, a project team with a clear mission and specific goals needs to be cross-functional, full-time, and co-located. It's a total immersion experience, with the team constantly working together, hour upon hour, days and nights, and in some cases, months and years.

Why? Creativity comes from people's interactions; inspiration comes from intensive concentration. Just like a start-up, the initial founding team huddles together in a garage, experimenting, iterating, discussing, debating, trying and retrying, again and again.

Pick the right team leader. The right leader may not guarantee success, but the wrong leader will surely guarantee failure. In each of Amazon's major breakthroughs, you will find a strong leader.

At Amazon, the project team is held accountable end to end, meaning their ownership extends all the way from concept, to design, to development, to testing, to launch, and to post-launch operation. Why? Bezos believes in the principle of "eat your own dog food." This is a forcing mechanism of enforcing crystal clear accountability for everyone with nowhere to hide, no one at whom to point the finger.

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## Building Block 5: High-Velocity and High-Quality Decision-Making

Amazon's decision-making is not only high in both velocity and quality but also high in scale, with a set of clearly articulated principles and a uniquely designed methodology enforced with striking consistency throughout the organization.

How can Amazon upgrade its decision-making and achieve the three seemingly conflicting goals of speed, quality, and scale at the same time?

Bezos has categorized all decisions into two types and designed different kinds of decision-making processes depending on whether they are a Type 1 or Type 2 decision. As noted in a company Shareholder Letter, Type 1 decisions refer to those that "are consequential and irreversible or nearly irreversible—one-way doors . . . . If you walk through and don't like what you see on the other side, you can't get back to where you were before."

Because of the long-term implications, Bezos suggested that Type 1 decisions should go through a heavyweight process to ensure they are of high quality. However, most decisions aren't like that.

### Type 2 Decisions: Speed Matters

Type 2 decisions refer to those that "are changeable, reversible—they're two-way doors. If you've made a suboptimal Type 2 decision, you don't have to live with the consequences for that long. You can reopen the door and go back through."

Applying the heavyweight process on Type 2 decisions will lead to slowness, risk aversion, failure to experiment sufficiently, and diminished invention. As CEO, you should identify and delegate the Type 2 decisions, as they "can and should be made quickly by high judgment individuals or small groups."

Don't wait for all the information. In business, Bezos used a 70–90 rule instead. He stated that "most decisions should probably be made with somewhere around 70 percent of the information you wish you had."

Let the metrics owner make the call. At Amazon, each operation has a set of metrics to ensure operational excellence, and each metric has one designated metrics owner. In this way, the metrics owner is the single point of accountability, so no more finger-pointing; the owner has full access to all the relevant data and analytics, so no more being handicapped by partial information; and the owner has clear authorization to take corrective initiatives, with maximum one-level of approval, so no more heavyweight decision-making.

The company also digitizes math-based routine decisions. One typical example: how to manage inventory purchasing. Given the availability of vast amounts of historical data about customer orders, seasonal volatility, replenishment speed of vendors, and all the AI-powered analytics and pre-

# Customer obsession and Day 1 thinking are inextricably linked twin drivers of the Amazon management system.

diction tools, this is a typical math-based routine decision that can be largely digitized.

## Scale Up Good Decision-Making

Here comes the billion-dollar question: how to scale high-velocity and high-quality decision-making. The first step is to crystallize consistent principles.

In his first Shareholder Letter, Bezos offered an unambiguous manifesto, specific, observable, and verifiable, that enabled shareholders to make informed investment decisions regarding Amazon. It also provided customers with the company's decision catechism, so that they would be more willing to build a trust-based long-term relationship with Amazon.

But most importantly, this transparent and widely shared set of principles is for all current and future Amazon employees: a set of crystal-clear guidelines so that every single one of them can understand the decision-making logic and be able to make the right choice when duty calls.

**Specify consistent methodology; narratives.** June 9, 2004 witnessed a brilliant innovation in human management practices. It all started with an email from Bezos: No PowerPoint presentations from now on at Amazon's core executive team. From that day on, Amazon embarked on a journey towards what came to be known as "Six-Page Narratives."

Writing six-page narratives forces the author to conduct complete analysis, to distinguish between subtle nuances, to articulate the inner logic and set priorities for various ideas, and take full accountability for specific proposals. There is no wiggle room, no hiding place, and no safe haven. Everyone must put "skin in the game" and is to be held accountable for it.

## Enforce a consistent approach in every decision.

It is tough to make good decisions and even tougher to crystallize decision-making principles. The toughest part is to walk the talk and consistently apply the stated principles when making every single decision. Julie Weed wrote in the foreword of *The Amazon Way*, Amazon's "principles aren't slogans printed on wall posters and coffee mugs. They

are lived and breathed every day by Amazonians from the CEO on down."

## Building Block 6: Forever-Day-1 Culture

If you read through all the Shareholder Letters that Bezos meticulously wrote over the past 22 years (1997–2018), the phrase "Day 1" appeared an amazing 22 times, with striking consistency. For the past 10 years, every Shareholder Letter has ended with the same line: "As always, I attach a copy of our original 1997 letter. Our approach remains the same, and it's still Day 1."

Why Day 1? At the early stage of any startup, the founder (or the small founding team) runs everything, from design to production, to sales, to delivery, to bookkeeping. If luck is on their side, the business will soon outgrow the capacity of the founding team, and they will need to expand the team and build an organization.

Normally, in the beginning, the organization will still function with speed, nimbleness, and a risk-acceptance mentality, but as the business grows bigger, complexity starts increasing and layers begin creeping in, and the once-nimble startup inevitably falls into the trap of so called "large organizations" characterized by slowness, rigidity, and risk aversion.

Bezos' evocative and sticky model of "Day 1 vs. Day 2" captured his aspiration for Amazon to grow aggressively in scale and scope while preserving the entrepreneurial vitality of a startup and building on the numerous advantages of a large company at the same time. Customer obsession and Day 1 thinking are inextricably linked twin drivers of the Amazon management system. Amazon has to improve continuously in everything it does, in everyone it has, and with accelerating speed and agility.

## How to Build a Forever-Day-1 Culture

First, operationalize the culture. Today, Amazon uses a set of 14 Leadership Principles to define its corporate culture: customer obsession; ownership; invent and simplify; are right, a lot; learn and be curious; hire and develop the best;

insist on the highest standards; think big; bias for action; frugality; earn trust; dive deep; have backbone—disagree and commit; deliver results.

For each leadership principle, Amazon specifies the expected behavior. For example, what does “Customer Obsession” really mean? Leaders start with the customer and work backwards. They work vigorously to earn and keep customer trust. Although leaders pay attention to competitors, they obsess over customers. Once you bring these principles down to clear and specific behaviors on the ground, they become operational, and everyone and anyone can start practicing them accordingly.

**Create forcing mechanisms.** Amazon has created a system of simple but effective forcing mechanisms to ensure that everyone in the organization really lives and breathes the stated values and principles. Let’s take Amazon’s favorite and perennial number-one principle, Customer Obsession, as an example.

Every week, Bezos asks his executives the same question: What can we do better for the customers? He asks this every week. No exception.

Each year, some managers are required to participate in a two-day training session at a call center. This direct interaction with customers is designed to help them gain a first-hand understanding of customers’ frustrations and pain points and also to provide them with the precious humility to recognize that despite its widely applauded success, Amazon still needs to continuously improve.

Given that in the digital age, a seemingly random post can go viral in no time, and if not handled properly in time, the damage from a negative post could be disastrous, Amazon

has invested millions to build a system to systematically track customer feedback in real time.

If a service or product provided is discovered to be subpar, instead of waiting for customer complaints posted online or communicated via the call center, Amazon can detect the glitch and take the initiative to refund customers via its automated systems.

The most powerful forcing mechanism has to do with personally modelling the behavior expected from everyone.

Why does the Amazon Management System work so well for Amazon? Because it best fits the personal values, principles, characters, and styles of Jeff Bezos, Amazon’s founder and CEO, and his core team; it also best fits the nature of Amazon’s platform and infrastructure business.

What works for you? What fits you and your business best? No one has the perfect answer. You will have to experiment, iterate, and invent your own.

Always remember: It is still Day 1.

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Ram Charan’s 27 books have sold over 3 million copies and include the *New York Times* best-seller **Execution**. He is a world-renowned business advisor, author, and speaker who has spent the past 35 years working with many top companies, CEOs, and boards. Julia Yang is a trusted advisor to entrepreneurs, founders, CEOs, and executives, a reputation earned during nearly 20 years of relevant practice. She currently works with Ram Charan to serve business leaders and explore new management practices in the digital age.



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