Amazon Aggregators: Breakdowns Research

By: **Shiv Socrates Kapoor**

Key Research Sources

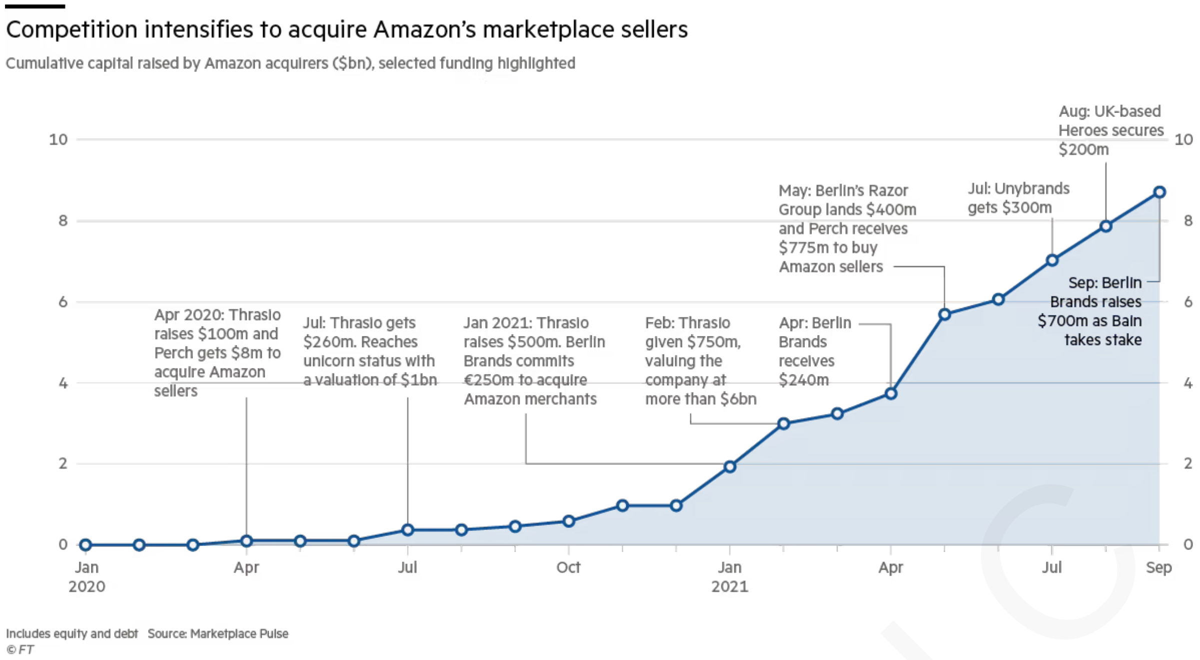
- CrossStack article by Ali Hamed
- Marketplace Pulse - Acquirers and Funding
- Marketplace Pulse - 2020 Year in Review
- Claret Capital memo
- On Aggregators and Disaggregators by Gad Allon

Quick Facts & Figures

- Amazon Third Party Seller GMV is ~$295 billion, or 62% of worldwide Amazon retail GMV
- Thrasio is the fastest profitable unicorn in US history, acquiring that status in only two years
- Amazon third party aggregators have raised a cumulative ~$10 billion in capital till date; there are at least 80 active ones worldwide

Industry History

- While rollups aren't new (PE has been doing them since the 1980s across a range of industries), and digital-first consumer brand rollups have also been around since at least 2010 (e.g., Elements Brands), Amazon third-party aggregators really originated in 2018 with the founding of Thrasio.
- Thrasio is the largest acquirer of Amazon third-party private-label businesses, having raised ~2.3bn in debt and equity, and paid ~$600mm for over 150 acquisitions and 200+ brands to date. It is on track to generate ~$1bn in revenue this year.
- Per the latest estimates from MarketPlace Pulse, ~$8-$10bn in capital (debt and equity) has been raised by Amazon third-party aggregators, with at least 80 active Amazon aggregators worldwide. Most are based in the U.S., though there's been a spate of activity across Mexico, France, India, Germany, Spain, United Kingdom, and other countries. 40 aggregators have announced funding rounds, of which 26 have raised at least $100 million.

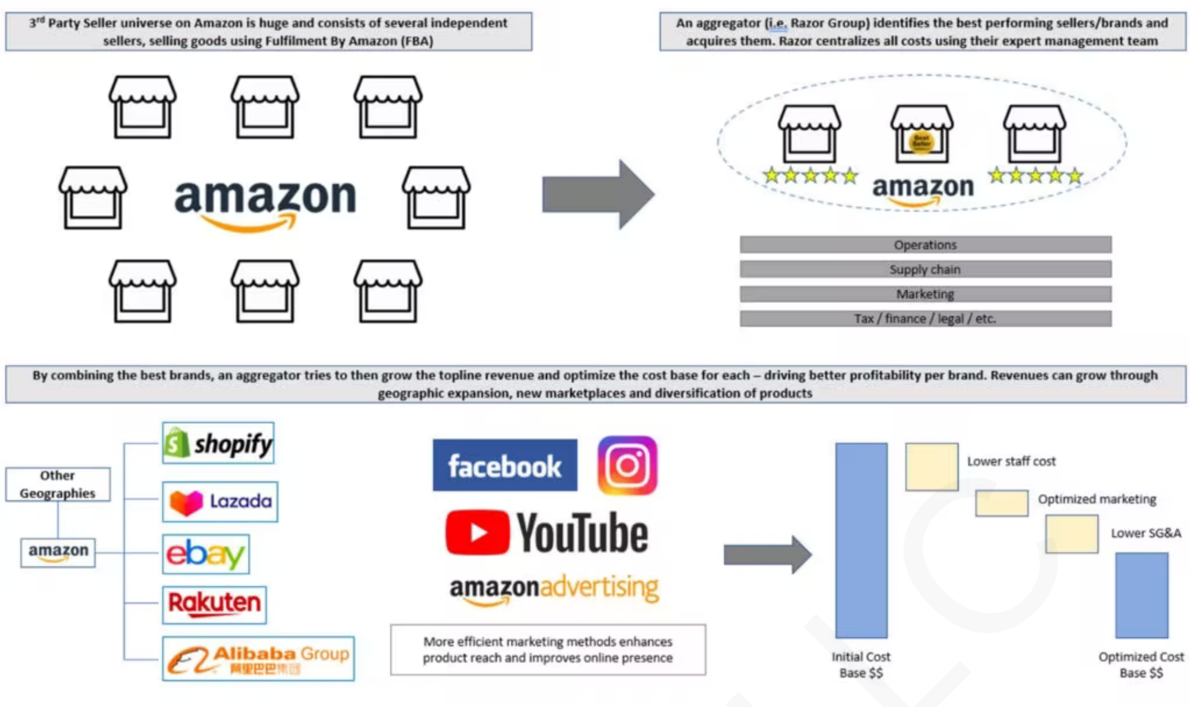


Source: FT

Business Model & Secret Sauce

Value Proposition

- Amazon Third-Party Retail is a huge and growing asset class
  - Two-thirds of US shoppers typically start their search for new products on Amazon (eMarketer 2019)
  - GMV for third-party sellers is estimated at ~$295bn in 2020, or 62% of Amazon Retail's $475bn worldwide GMV (up from 60% in 2019 and 58% in 2018)
  - ~1.5 million active sellers globally, with ~500K added in the last year alone
    - Two-thirds of sellers use Fulfillment by Amazon (FBA) exclusively, and over 90% are estimated to use FBA in total (in combination with Fulfillment by Merchant, or FBM)
  - Thrasio estimates that there are at least 50K sellers with more than $1mm in sales on FBA
- The Aggregator Playbook
  - In a nutshell, the modus operandi is to acquire under-optimized businesses in a fragmented but growing industry, rationalize costs and realize synergies while scaling up the brand. Then rinse and repeat. In general, they use leverage, stay away from competitive categories such as fashion, electronics and fads (e.g., supplements), and execute at breakneck speed closing transactions in 30 days or less.
  - Their speed is enabled by a powerful analytics engine. On the acquisition side, aggregators scrape Amazon APIs and public marketplace data to ensure proprietary sourcing of brands with the "right" characteristics (for instance, Thrasio has a 503-point checklist that they use to evaluate each acquisition). On the execution side, they deploy best-in-breed supply chain & sourcing practices, implement search engine optimization and other marketing efficiencies at scale, and provide financing / other business services that help accelerate brand growth.



Source: Claret Capital

- Benefits to Sellers
  - **Mitigates Competitive Risk and Operational Complexity:** Amazon TPS brands are typically under-capitalized, over-levered and carry significant key man risk. Moreover, it becomes harder to scale beyond a certain point in a hyper-competitive space. Operational complexity increases non-linearly and margins contract. The "return on invested brain damage" on managing supply chains, navigating Amazon policies on returns and customer reviews, etc. just isn't there, and it becomes rational to seek liquidity.
  - **Instant Liquidity, Favorable Terms, Smooth Process:** Aggregators provide upfront liquidity to motivated sellers, offering an attractive, pain-free alternative to the vagaries of an increasingly hard-earned, uncertain revenue stream. In addition to the upfront cash exit, founders of the better brands may also be offered an earnout linked to the future potential of the business - a "free" option on the upside if you will (Thrasio claims that its payout rate is over 90%)

Source: AcquCo

- Benefits to Amazon
    - **Industrialization:** Aggregators deepen and "industrialize" the ecosystem, providing growth capital and services for businesses that may be too small to be serviced by Amazon directly (e.g., Yardline seeded and acquired by Thrasio, is a Capital-as-a-Service provider for FBA businesses)
    - **Professionalization:** Increased competition is a good thing for the customer. Customer service standards go up, stockouts become fewer, a proliferation of higher quality brands ensues, and in the short to medium term, Amazon would prefer dealing with a fewer number of larger sellers.

Investment Thesis for Aggregators (Secret Sauce)

> *"There is a reason why the aggregators are initially focusing on Amazon FBA sellers. By enabling sellers to leverage its e-commerce infrastructure (storage, fulfilment, shipping, customer support etc.), Amazon has created an ecosystem of highly standardized assets that can be operated with reduced requirements for staff, marketing capabilities etc. This allows aggregators to rapidly identify, diligence and integrate multiple such assets in parallel.* ***The model can therefore reach scale much faster than a typical Private Equity roll-up play. And the cherry on top: Well-run FBA sellers typically operate at very attractive EBITDA margins and cash flows from Day 1."*** *– Christoph Gamon, Claret Capital*

Similar to private equity, the recipe for value creation is "cheap, small, levered", with one additional vital ingredient - the Amazon Platform advantage.

- Multiple arbitrage: Likely the biggest source of "alpha" in this strategy. Acquisitions have historically been made at 2-4x EBITDA multiples (plus earnout). Combining these assets into a fast-growing conglomerate of digital-native brands could potentially merit a high teens or beyond multiple in the public markets.

- ☐ Operational value creation: As discussed previously, there's usually plenty of low-hanging fruit in terms of operational improvements in these small businesses, addressing which drives value creation on both the demand and supply-side.
- ☐ Leverage: As long as you can be reasonably confident that EBITDA is sustainable, and that you can service and quickly pay down debt (the likelihood of which increases materially at cheap acquisition prices), this is a bet worth taking. Without leverage, it would not be possible to scale these businesses at their current rates. Venture debt firms have begun warming up to this reality - it's estimated that roughly half of the total capital raised in the space is debt.
- ☐ The Amazon Platform Advantage:
  - **Deep, Fragmented Ecosystem** - The largest aggregator in the space accounts for *only a third of a percent* of Amazon's ~$295bn TPS GMV - there's room for *several* winners across categories.
  - **'Composability'** - Standardized logistics and customer support infrastructure from Amazon for FBA sellers makes these assets attractive (as opposed to a cross-platform DTC brand roll-up play), reducing complexity on the backend while integrating disparate products into a combined entity.
  - **Intrinsic Platform Growth** - Amazon third-party sellers effectively exist "rent-free" on the largest, busiest digital mall in the world, which continues to see double-digit growth in traffic. Demand-gen is the biggest problem for small businesses (eCommerce businesses spend between 20-30% of revenues on marketing). Listing on Amazon defrays this expense to an extent as customers don't shop at the seller, they shop at Amazon (Since discoverability is what matters here as opposed to brand, there are still marketing costs that need to be incurred, but you'd imagine that net-net, sellers of a certain scale come out ahead on a growing platform that's increasing share in retail)
  - **Favorable Cost Structure Businesses** - because of the plethora of services that Amazon offers, third-party sellers tend to be predominantly variable cost businesses (this characteristic may not hold true at higher scales though, as aggregators look to centralize and move service capabilities in-house). One of the Thrasio founders noted in an interview that the gross margins of their targets is in the range of 30-45%.

Competitive Position

Industry

- The ecosystem does ~$50bn in EBITDA but, to date, funding in this space has only reached ~$8bn. Competition for TPS and dollars to acquire them has increased in the last 12-18 months, however, with at least 80 active aggregators having raised.
- PE firms and strategic acquirers are also entering the fray. These firms are better capitalized and able to execute deals faster than a number of aggregators, most of which have been founded in the last year or so. Strategics would also have the advantage of more easily realizable synergies.
- In addition to sophisticated capital, there are smaller acquirers sourcing deals through brokers such as QuietLight

Source: Hahnbeck.com

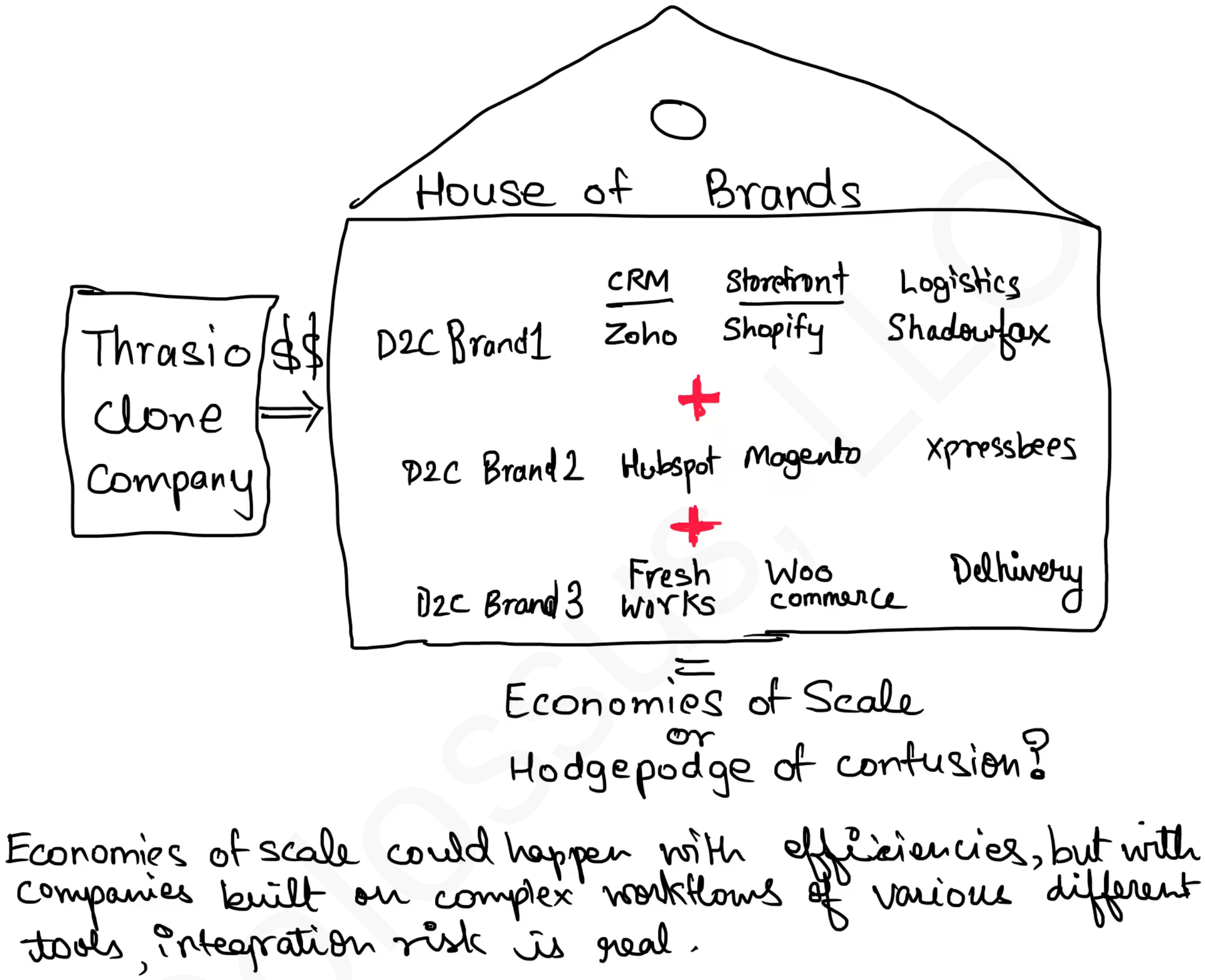
- TPS typically sell for low multiples but is this changing? If so, worth evaluating how much is on account of increased competition and price discovery, and how much stems from a revenue reduction caused by recent supply chain issues.
  - 2-4x EBITDA is quoted as the generally accepted range (see graphic), but this Fast Company article from October 2021 notes how the multiple for well-run brands could go as high as three times revenue (~15x EBITDA, assuming 20% margins)
  - Multiples can vary by geography and approach - GlobalBees, a Softbank-backed aggregator in India, recently acquired a Peloton-like brand in India at 15x EBITDA
- COVID-19 Supply chain impact
  - eCommerce supply chain costs have shot through the roof recently along with stockouts, and this has particular ramifications on FBA aggregators (see thread). A triple whammy of lower synergies, increased costs and decreased revenues, with debt repayments looming.
    Thrasio recently saw its cofounder leave and shelved plans to go public via a SPAC.
- Competition outside of Amazon
  - Other Platforms - FBA-inspired aggregators are coming to Shopify as well (e.g., OpenStore, WeCommerce), each with a different take on sourcing and execution; some ETSY plays may also be in the works
  - Amazon FBA brands are using Amazon as a launchpad, and have expanded across platforms offering goods and services. Anker was one of the early examples; Packable, an eCommerce marketplace enablement platform, recently announced that it is going public via a SPAC
  - Rollup companies are going international and cross-platform, seeking marketplace-native brands in general
  - There are also "Accelerators" such as Pattern Brands, whose approach is to figure out growth and execution instead of aggregation. Their contention is that to be successful, aggregators will need to become accelerators
  - Similar to how WeCommerce invests in service partners in the Shopify ecosystem, aggregators will probably expand out beyond sellers into service providers. We're already seeing inklings of that (Thrasio/Yardline)

Risks

- **Low base rates of success** for levered roll-ups of disparate brands (Newell, Spectrum; recently $ATER, though perhaps for other reasons too in ATER's case)
  -

"Brands are like capturing lightning in a bottle" (excellent thread from Italic founder Jeremy Cai) - it is hard to determine ex-ante which brands will succeed in scaling up. You also invariably run into high CACs past a certain point. Technology can likely only take you so far; the juice may be in the execution.

- **Coordination Friction** - One of the biggest criticisms of the aggregator model is *dis*economies of scale and exponential complexity in coordinating the integration of a disparate collection of brands from mattress protectors to pet deodorizers. No one seems to have cracked this model yet, especially at the speed at which these aggregators are gobbling up brands. Potentially hard to stay focused on integration, if team is focused on acquisition.



Source: Mincemeatnotwords

- **Financial Risk** - Should the business encounter any potholes, as is the wont of businesses, the leverage might kill some aggregators. Sustainability of EBITDA is a critical assumption to this model (linked to covenants and expansion of credit lines if required).

- **Acquisition Prices -** Getting 'em cheap is a key tenet of this model. The FCF yield is very sensitive to acquisition prices. Additionally, growth rates may be mean reverting post-pandemic and buyers run a risk of overpaying as competition heats up and capital floods this space. This dynamic is reminiscent of the early days of Private equity, highlighted by Dan Rasmussen on an early ILTB podcast (emphasis mine):

> ***As you increase the purchase price, you're increasing debt levels and you're increasing interest payments... Any increase in valuation actually has almost an exponentially negative effect on free cash flow yield.*** *Conversely, as you get cheap, the cheap levered equity is, the 1980s, 1990s LBOs, done at seven times EBITDA. In those cases, you had the increase in leverage far outweighing the increase in interest payments. But there's essentially this exponential curve as you increase valuation.* ***That's what makes private equity much more price-sensitive, is that the expensive companies are at a higher risk for bankruptcy, their interest payments are substantial relative to their free cash flow. That means***

> ***that you have a lot more downside in those expensive LBOs*** *than you might in an expensive public equity that's not levered.*

> *"I went back and read all Mitt Romney's early letters when he was investing. I found one from, about 10 years into his career. He said,* ***"Prices this year are getting more expensive. We used to buy things at four to six times EBIT, but we're having trouble finding things at those valuations, which worries us about our ability to generate alpha at higher valuations. We're seeing some of our competitors get involved in auctions, which just seems crazy to us."****...*
> ***Did Mitt Romney and Kravis and Roberts and all these guys, did they succeed because they were the best stock pickers in the world, or because they found a corner of the market that was deeply undervalued?*** *I think that when you then think about these reference classes of these great investors, they were* ***finding places that were undervalued, where other people weren't doing this****, "Uh, I don't know, it seems crazy to go out of the public equity market and buy small private companies with debt. I don't know, it sounds really risky to me," or "Gee, putting insurance money into common equity. I don't know. That sounds really, really risky."*

  - **Platform Risk**
    - ▫ In the short term, there is low risk. Aggregators are filling a gap in the market that only helps serve Amazon's customers better. In the medium term, as aggregators become larger, Amazon may find ways to decrease their relative power in the ecosystem by unilaterally changing the rules. It has played rough in the past, e.g., Honey, or Nike (Nike was able to counter a couple years later by terminating the pilot because of its strength of brand - significant execution risk here on whether aggregators are able to build similarly powerful brands)
    - ▫ In the long-term however, as Wharton professor Gad Allon argues, aggregators are between two points of the Shih Smiling curve and will get squeezed unless they succeed in differentiating themselves. As Ben Thompson argues, the objective of aggregators is after all to commoditize brands/content.
    - ▫ Amazon might respond with arbitrary rules to mitigate the adverse selection problem of brands using Amazon to launch while they're small but going direct/brick and mortar once bigger (this might be a straw man argument though; I suppose retail is large enough that sufficient distribution is achievable through other channels in the absence of Amazon - unlike App store/Epic)

- **Exit Strategy**
  - If acquisition prices get prohibitive, or if brands don't scale soon enough, you get into an asset-liability mismatch and debts may become unserviceable. Using IPO proceeds to pay down debt may be the only viable path for several of these businesses if that's the case. A lot depends on market environment - it's interesting to ponder that the biggest game in town had to shelve its going public plans in a "hot" market (well, maybe no longer for SPACs)

> *"If we exited at $10 billion, I'd give myself a C-minus, at $25 billion, B-plus. If we exited at $50 billion to $100 billion, A-minus."* - Josh Silberstein, (former) co-founder of Thrasio

Useful Resources

Title	Type	What You Will Learn (140 Characters)	URL (Must be https://)
Carlos Cashman - Lessons from the Amazon Ecosystem	Podcast	Colossus interview with the Thrasio founder covering Thrasio's business model and execution strategy.	https://www.joincolossus.com/episodes/28372673/cashman-lessons-from-the-amazon-ecosystem?tab=transcript
Thrasio Co-CEO Josh Silberstein on mastering the Amazon marketplace, operating 60+ brands	Video	In-depth interview with Thrasio founder covering finance strategy and Amazon tactics	https://youtu.be/xN86AwK5qil
The Amazon Third Party Seller Ecosystem may be the Most	Article	Ali Hamed's foundational piece explaining the investment thesis behind the FBA aggregator	https://crossstack.substack.com/p/the-amazon-third-

Important Thing since the App Store		model	party-seller-ecosystem
Don’t Let Platforms Commoditize Your Business	Article	Discusses competitive strategy dynamics of smaller businesses versus platforms	https://hbr.org/2021/05/dont-let-platforms-commoditize-your-business
Gad Allon - On aggregators and disaggregators	Article	In-depth exploration of the pros and risks of the aggregator model	https://gadallon.substack.com/p/on-aggregators-and-dis-aggregators
Platform economies	Article	Ali Hamed discusses the evolution, value capture dynamics and investability of platform economies.	https://alibhamed.medium.com/platform-economies-65d6714ca768
Fullfilled by Amazon – powered by growth debt	Article	Discusses the importance of debt in FBA aggregator business models.	https://www.claret-capital.com/fullfilled-by-amazon-powered-by-growth-debt/
The Internet is Rockin' with Rollups - what's so special about them?	Article	Crossbeam’s Sakib Jamal discusses the evolution and investability of Amazon TPS as an asset class	https://crossstack.substack.com/p/the-internet-is-rockin-with-rollups
Want to Become a Unicorn? Buy it, Don’t Build it	Article	A good overview of the basics and implications of Thrasio’s aggregator business model	https://every.to/napkin-math/want-to-become-a-unicorn-buy-it-dont-751248