Fixed costs and operating leverage

Amazon letters: 2002, 2001 · Difficulty: Intermediate

> *"With customer experience costs largely fixed (more like a publishing model than a retailing model), our costs as a percentage of sales can shrink rapidly as we grow our business." (2002)*

1. Fixed costs are $100 million. Sales grow from $500 million to $1,000 million and fixed costs stay the same. Fixed costs as a percent of sales fall from 20% to what percent? **10**

2. When most of a company's costs are fixed, as sales grow…

   A. operating income grows slower than sales

   B. costs grow faster than sales

   C. the operating margin falls

   D. operating income grows faster than sales

Source: Jeffrey P. Bezos, Letters to Amazon.com Shareholders: 2002, 2001 (ir.aboutamazon.com). Quotation © Amazon.com, Inc., all rights reserved; reproduced in part for non-commercial teaching. Numbers in the questions are made up unless stated.