Avon Products 1964-2014: The Slippery Slope of Direct Selling

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Research Purpose:
This research explores the gradual departure of Avon Products, founded in 1886, from the traditional direct selling business model. From its peak years of the 1960s, the company tried various methods to sustain its success—from diversification to adopting a multilevel marketing compensation plan. By 2014 an underperforming Avon would withdraw from the Direct Selling Association, of which it was a founding member, with an unclear path forward.

Source Material:
The research relies on publicly available company documents and secondary data such as academic research and public sources.

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The Institute of Management Science's Third Annual International Meeting in 1957 gathered academics and practitioners from top universities and businesses, including: Stanford, MIT, Brown, Carnegie Institute, Case Institute, Columbia, George Washington, NYU, Purdue, UCLA, De Paul, Johns Hopkins, the Rand Corporation, the Departments of the Air Force and Navy, E.I. DuPont de Nemours, Lockheed, Litton, Kaiser Steel, Ramo-Wooldridge (i.e., TRW), Electricite de France, International Business Machines, Sperry, and Avon Products (*Report of the Third Annual International Meeting*, 1957). Avon's presentation (on forecasting and inventory planning) at a conference comprised of leading firms is an indicator of the company's growing success and, albeit it short-lived, dominance of the cosmetics industry.

By 1964 Avon's record was impressive. That year the company booked record sales and earnings, and in 1967 the then 81-year-old direct seller became the most profitable company in the United States (Dworsky, 1968). Between 1965 and 1968 Avon experienced a fifty nine percent increase in sales (Davidson, 1970). An investment of $16,000 in Avon stock in 1957 would be worth $385,000 ten years later (Hammer 1967). The door-ringing retailer of mostly proprietary products had become the largest cosmetics company in the nation. Their success continued well into the 1970s and soon the company, flush with money, it would begin looking for acquisition targets.

Although unrelated to Avon at the time, the 1970s saw a rapid increase in multilevel marketing (MLM), a business model promoted as an alternative form of direct selling. The MLM model shifts the recruiting and training of new sales people onto the existing sales force. Compensation for recruiting distributors then derives from purchases made by those they recruit (referred to as "a downline"). The MLM business model proved to be: 1) rapidly growing and 2) at times, a "pyramid scheme" business fraud (in the U.S. all forms of pyramid schemes are illegal). In the late 1940s Nutrilite established the MLM business model and also the tendency for MLMs to provoke regulatory displeasure (*The New York Times*, 1951). In 1973 the New York Times reported product-based pyramid schemes to be "the number one consumer fraud in the metropolitan area" (Lichtenstein, 1973). In the coming years, the MLM model would eclipse traditional direct selling, eventually forcing companies like Avon and Mary Kay to adapt.

After years of increasing sales and profits, in 1979 Avon purchased Tiffany's the upscale jewelry retailer (Barmash, 1981). Costume jewelry had become an increasing part of Avon's product line, accounting for 18 and 21 percent of revenue and profits respectively in 1978 (*The New York Times*, 1980). Owning Tiffany's would diversify jewelry profits across multiple markets. In 1981 Avon acquired Mallinckrodt Inc., a company that manufactured health-care products, fragrances, flavors, and chemicals. As part of its diversification strategy, Avon would also come to own Foster home health care and an interest in Retirement Inns of America. However, managing a diversified portfolio proved challenging. In 1984 Avon sold off Tiffany's and in 1985, in a move to restructure, Avon sold Mallinckrodt, just three years after the acquisition. Foster and Retirement Inns would also be sold.

After a failed period of acquisitions, Avon's financial performance continued to slide. Throughout the mid-1980s an industry-wide slump affected every major traditional direct seller with Avon, Tupperware, and Mary Kay each experiencing significant declines. For example, in the first quarter of 1985 Avon's domestic sales and operating profits declined by fifty percent and from 1983 to 1984 Shaklee's operating income went from $65.2 million to $24.5 million. Weakness in the industry was attributed to difficulty in recruiting as the percent of women aged 18 to 44 employed outside the home rose to 64 percent (*The New York Times*, 1985).

No decade demonstrates the relative differences between traditional direct selling and the MLM business model better than the 1980s. In an effort to reduce debt, by the end of the decade Avon needed to sell its Japanese clothing division and put its catalog unit on the market. As traditional direct sellers reeled, MLM companies thrived. At least five new MLM companies—Sunrider, Herbalife, Advocare, Nu Skin, and Melaleuca—were founded and experienced significant growth during this period. In 1989 Amway, the largest MLM company, initiated a hostile takeover of Avon. Highlighting the tension between the competing business models, Avon called Amway "an admitted criminal" (Freitag, 1989). Amway soon withdrew its bid.

Earlier, in 1981, Avon adjusted its compensation plan by providing a percent of sales to approximately 25,000 group leaders. This effort to tweak the traditional direct selling structure failed to stem the decline in sales. As a result, in 1991 the company finally considered adopting an MLM structure under an initiative labeled "Leadership" and promoted by Rick Goings, an Avon executive. The CEO James Preston rejected the move and Goings left the company (Hwang, 1994). There is some evidence, however, that the model was offered as an option for at least a portion of the existing sales force (*New Hampshire Business Review*, 2000).

During the 1990s Avon quietly shifted away from it traditional sales structure, joining the ranks of major MLM companies such as Amway and Nu Skin. Despite its early criticism of the model, Avon could not sustain it performance with traditional selling. In 1999 a New Hampshire "Avon lady" reported annual sales of $6.8 million derived from a downline of 1,400 sales people/distributors (*New Hampshire Business Review*, 2000). Even in 2014, however, the company's commitment to the model appears more quiet than proud, with the role of recruiting understated in its promotional material.

A world brand, Avon developed a reputation for responding to the needs of multiple cultures. An early entrant to global markets, the company opened its Montreal office in 1914. By 1960, over $10 million in sales came from markets other than the U.S. and Canada. International sales played an important role in offsetting an increasingly uncertain the domestic market. Avon's global reputation also benefitted from it commitment to women's issues, ranging from the economic independence of women in developing countries to the presence of women in corporate boardrooms (Scott, et al., 2012; Adler, 1997). These positive images helped Avon retain its reputation despite disappointing financial performance.

This too would change. As the first direct selling company to enter China, a country wary of the approach, Avon was well positioned. However, to gain acceptance, from 2004 to 2008 executives repeated violated the Foreign Corrupt Practices Act, hiding $8 million in gifts given to Chinese government officials. Under new leadership, in 2014 the company agreed to a $135 million settlement (Neumeister, 2014).

During this same time period the MLM model came under intense scrutiny in U.S. and China. Nu Skin would be forced by the Chinese government to temporary halt recruiting, and a hedge fund CEO in the U.S. publicly accused Herbalife of operating a pyramid scheme. The entire MLM industry received unwanted attention. Sending a ripple through the industry, in the fall 2014 Avon responded by withdrawing from the Direct Selling Association, an organization it helped found.

The picture of Avon in 2014 is one of a storied company trying to find its way. A global company with a long history and a record of supporting women and the community, Avon found its image tarnished by bribery and operating a business model under intense public scrutiny. Ironically, to distance itself from other MLM companies it has now publicly called on the industry trade association to update its ethics (Heinonen, 2014).

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