**INTRODUCTION**

Avon Products is an iconic American brand of beauty products marketed directly to women. The company has a rich history and broad global reach, but social, economic, and demographic shifts have given the company’s leaders cause to rethink Avon’s business model and strategic direction.

After a brief introduction, the case describes how the company was founded and evolved throughout the twentieth century. To support an internal analysis, the case reviews Avon’s products and brands; vision, mission, and values; supply chain practices; competitive and selling strategies; top executive leaders; and financial reports. The external environment is also covered, including general environmental conditions and information on the industry and competitors.

Over the past decade, Andrea Jung has attempted to reshape Avon’s strategy to better fit present times. Her initiatives have achieved mixed results and somewhat limited success. Seeing the need to re-correct, the company’s board of directors has again decided to bring in new leadership at the top. As Sherilyn McCoy begins her tenure as Avon’s new CEO, this case analysis is suited to determine strategic fit and to address corporate governance mechanisms needed to ensure that the company operates in ways that will best serve its shareholders’ interests.

* Conduct a SWOT analysis to highlight the most important factors that should be considered when formulating Avon’s strategy.
* Compare and contrast Jung’s strategy with McCoy’s new strategy.
* Did Jung’s strategy fit the situation? Why or why not? Does McCoy’s strategy fit the current situation? Explain your answer. What suggestions can be derived from the analysis to enhance McCoy’s strategic plans?
* Discuss Avon’s decision to retain Jung as the chairman of the board. Do you believe this is a good decision? What is the potential downside of keeping the former CEO in this leadership role?

**ANALYSIS**

* ***Conduct a SWOT analysis to highlight the most important factors that should be considered when formulating Avon’s strategy.***

The case includes extensive material on Avon’s internal environment. The company’s organizational strengths and weaknesses are outlined on the following pages; and selective entries from Avon’s balance sheet and income statement are noted to support the analysis.

|  |
| --- |
| **Strengths** |
|  |
| World’s largest direct seller – history as the leading global beauty company |
|  |
| 6.4 million active sales representatives worldwide |
|  |
| Extensive product line of beauty, fashion, and home products – beauty segment represents 73% of revenue – gift, decorative, and apparel products are complementary |
|  |
| Differentiation through personalized selling model – relationship marketing |
|  |
| Focus on empowering and serving women |
|  |
| Ability to build connections and customer loyalty |
|  |
| $10 billion in sales (2008) |
|  |
| Celebrity endorsements and product offerings |
|  |
| Global reach – 83% of revenue generated outside of the U.S. – strong position in international markets |
|  |
| In-house manufacturing and packaging of beauty products |
|  |
| Global supplier orientation – efficient, cost-sensitive ERP system – economies of scale used to sustain value price points |
|  |
| Innovative, proprietary products – delivery of “first-to-market” products with visible consumer benefits – research and development capabilities |
|  |
| Representative Value Proposition (RPV) – supportive online technologies |
|  |
| Mergers and acquisitions to diversify product lines |

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| --- |
| **Weaknesses** |
|  |
| Share price – down more than 50% over past 2 years – decline in shareholder equity\* |
|  |
| High legal fees and costs – corruption and compliance charges |
|  |
| Business design based on by-gone social structure – adjustments inadequate to sustain a competitive advantage |
|  |
| Less than 10% of sales generated in Asia Pacific region – largest and fastest growing economy in the world |
| **(*cont.*)** |
| **Weaknesses (*cont.*)** |
|  |
| Higher costs associated with operating in some foreign countries |
|  |
| Difficulties recruiting quality representatives |
|  |
| Instability of product line – frequent changes are impacting service, product knowledge, confidence, and loyalty |
|  |
| Dependence on highly competitive beauty segment (73% of revenue) |
|  |
| Difficulties implementing ERP in Brazil |
|  |
| Diminishing brand and representative image in U.S. |
|  |
| Loss of domestic representatives\*\* – ineffective policies, poor relationships and product knowledge, and disadvantaged and discontented sales force |
|  |
| Poor financial performance and profitability\*\*\* – falling income, weakened cash flow, rising costs of sales (as a percentage of revenue), diminished margins, and waning profitability |
|  |
| Little attention to local cultures and trends in international markets – vulnerable to competitors and unidentified or evolving needs |

**Balance Sheet**

|  |  |  |  |
| --- | --- | --- | --- |
| (USD $) In Millions, unless otherwise specified | 2012 | 2011 | % Chg |
| Current Assets |  |  |  |
| Cash, including cash equivalents of $762.9 and $623.7 | $1,209.60 | $1,245.10 | -2.9% |
| Inventories | 1,135.40 | 1,161.30 | -2.2% |
| ***Total current assets*** | 3,928.90 | 4,098.80 | -4.1% |
| Property, plant and equipment, net, total | 1,550.20 | 1,571.50 | -1.4% |
| Goodwill | 374.9 | 473.1 | -20.8% |
| Other assets | 1,408.20 | 1,311.70 | 7.4% |
| ***Total assets*** | 7,382.50 | 7,735 | -4.6% |
| Debt maturing within one year | 572 | 849.3 | -32.7% |
| ***Total current liabilities*** | 2,704.60 | 2,891 | -6.4% |
| Long-term debt | 2,623.90 | 2,459.10 | 6.7% |
| Employee benefit plans | 637.6 | 603 | 5.7% |
| ***Total liabilities*** | 6,149.20 | 6,149.80 | 0.0% |
| Additional paid-in capital | 2,119.60 | 2,077.70 | 2.0% |
| Retained earnings | 4,357.80 | 4,726.10 | -7.8% |
| **\***Total Avon shareholders' equity | 1,217.10 | 1,570.40 | -22.5% |
| ***Total liabilities and shareholders' equity*** | $7,382.50 | $7,735 | -4.6% |

|  |  |
| --- | --- |
| \*\*Direct Sales Representatives – U.S. | |
| Avon | 420,000 |
| Mary Kay | 1,700,000 |
| Arbonne | 365,600 |

**\*\*\*Income Statement – Percentage of Sales Comparisons**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| (USD $) In Millions, except Per Share data, unless otherwise specified | | | | | | |
|  | ***Dec. 31, 2012*** | | ***Dec. 31, 2011*** | | ***Dec. 31, 2010*** | |
| Net sales | $10,546.10 | 100.0% | $11,112.00 | 100.0% | $10,731.30 | 100.0% |
| Other revenue | 171.00 | 1.6% | 179.60 | 1.6% | 131.50 | 1.2% |
| Total revenue | 10,717.10 | 101.6% | 11,291.60 | 101.6% | 10,862.80 | 101.2% |
| Costs, expenses and other: |  |  |  |  |  |  |
| Cost of sales | 4,169.30 | 39.5% | 4,148.60 | 37.3% | 4,041.30 | 37.7% |
| Selling, general and administrative expenses | 5,980.00 | 56.7% | 6,025.40 | 54.2% | 5,748.40 | 53.6% |
| Impairment of good-will and intangible asset | 253.00 | 2.4% | 263.00 | 2.4% | 0 | 0.0% |
| Operating profit | 314.80 | 3.0% | 854.60 | 7.7% | 1,073.10 | 10.0% |
| Interest expense | 104.30 | 1.0% | 92.90 | 0.8% | 87.10 | 0.8% |
| Interest income | -15.10 | -0.1% | -16.50 | -0.1% | -14.00 | -0.1% |
| Other expense, net | 7.00 | 0.1% | 35.60 | 0.3% | 54.60 | 0.5% |
| Total other expenses | 96.20 | 0.9% | 112.00 | 1.0% | 127.70 | 1.2% |
| Income from cont’g operations, before taxes | 218.60 | 2.1% | 742.60 | 6.7% | 945.40 | 8.8% |
| Income taxes | 256.80 | 2.4% | 216.20 | 1.9% | 350.20 | 3.3% |
| (Loss) income from cont’g operations, net of tax | -38.20 | -0.4% | 526.40 | 4.7% | 595.20 | 5.5% |
| Discontinued operations, net of tax | 0 | 0.0% | -8.60 | -0.1% | 14.10 |  |
| Net (loss) income | -38.20 | -0.4% | 517.80 | 4.7% | 609.30 | 0.1% |
| Net income from noncontrolling interests | -4.30 | 0.0% | -4.20 | 0.0% | -3.00 | 5.7% |
| Net (loss) income attributable to Avon | -42.50 | -0.4% | $513.60 | 4.6% | $606.30 | 0.0% |

COS and SGA expenses are falling in absolute dollars, but they are rising as a percentage of revenues. This is negatively affecting gross and operating margins. Operating profit fell 20.4% in 2011 and another 63.2% in 2012. After other expenses and taxes, Avon had a net loss in 2012.

**\*\*\*Income Statement – Year-to-Year Changes**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| (USD $) In Millions | 2012 |  | 2011 |  | 2010 |
| Net sales | $10,546.10 | -5.1% | $11,112.00 | 3.5% | $10,731.30 |
| Other revenue | 171.00 | -4.8% | 179.60 | 36.6% | 131.50 |
| Total revenue | 10,717.10 | -5.1% | 11,291.60 | 3.9% | 10,862.80 |
| Costs, expenses and other: | |  |  |  |  |
| Cost of sales | 4,169.30 | 0.5% | 4,148.60 | 2.7% | 4,041.30 |
| Selling, general and administrative expenses | 5,980.00 | -0.8% | 6,025.40 | 4.8% | 5,748.40 |
| Impairment of good-will and intangible asset | 253.00 | -3.8% | 263.00 | - | 0 |
| Operating profit | 314.80 | -63.2% | 854.60 | -20.4% | 1,073.10 |
| Interest expense | 104.30 | 12.3% | 92.90 | 6.7% | 87.10 |
| Interest income | -15.10 | -8.5% | -16.50 | 17.9% | -14.00 |
| Other expense, net | 7.00 | -80.3% | 35.60 | -34.8% | 54.60 |
| Total other expenses | 96.20 | -14.1% | 112.00 | -12.3% | 127.70 |
| Income from cont’g operations, before taxes | 218.60 | -70.6% | 742.60 | -21.5% | 945.40 |
| Income taxes | 256.80 | 18.8% | 216.20 | -38.3% | 350.20 |
| (Loss) income from contin’g operations, net of tax | -38.20 | -107.3% | 526.40 | -11.6% | 595.20 |
| Discontinued operations, net of tax | 0 | -100.0% | -8.60 | -161.0% | 14.10 |
| Net (loss) income | -38.20 | -107.4% | 517.80 | -15.0% | 609.30 |
| Net income attributable to noncontrolling interests | -4.30 | 2.4% | -4.20 | 40.0% | -3.00 |
| Net (loss) income attributable to Avon | -42.50 | -108.3% | $513.60 | -15.3% | $606.30 |

Looking to the external environment, the following opportunities and threats can be identified.

|  |
| --- |
| **Opportunities** |
|  |
| Internet technology-driven connectivity – new social networking structures and tools – could have enormous implications for sales representative performance |
|  |
| International markets – especially in the rapidly-expanding Asian Pacific region |
|  |
| Product innovation – Avon has a strong R&D capability to deliver relevant new products to its markets |
|  |
| Niche markets – such as “smarter women” attracted to high-quality, value-priced products, working women, aging women, new mothers, young women, etc. |
|  |
| Cross-selling to clientele of acquired, stand-alone brands |
| **Threats** |
|  |
| Economic challenges |
|  |
| Exchange rate fluctuations |
|  |
| Unfriendly foreign government policies – i.e. Venezuela |
|  |
| Potential fines for non-compliance with FCPA and SEC regulations |
|  |
| Competition and rivalry in the beauty industry – primary sources: other direct sellers, Internet shops, mass-market retail channels |
|  |
| Inability to recruit quality sales representatives |
|  |
| Supplier pricing and quality |
|  |
| Entry of new rivals – expansion of large, diversified companies leveraging technologies and economies of scope |
|  |
| Imitation and price undercutting of proprietary products |
|  |
| Insufficient protection of niche markets – particularly in emerging nations |

**STRATEGY**

* ***Compare and contrast Jung’s strategy with McCoy’s new strategy.***

Avon’s vision, mission, and organizational objectives are not dissimilar for Jung and McCoy. Both leaders are responsible for developing and executing all of the company’s long-term growth strategies. They are charged with restoring Avon as a premier direct seller of beauty products, shaping the women’s brand to fit the modern world. Their central focus is fostering relationships with women, both by creating internal opportunities for female representatives and by meeting the external needs of a predominantly female market.

A comparison of the two leaders’ approaches based on critical strategic elements is presented below.

|  |  |  |
| --- | --- | --- |
|  | **Jung** | **McCoy** |
| ***Product*** | Up-scaled high-end beauty lines | Premium brands (i.e. Anew) |
| ***Market*** | Trendy, educated, professional, high-end clientele | Status and demographics matched to sales representatives’ social network |
| ***Process*** | Pull marketing – media advertising | Revitalized sales force |
| ***Capabilities/ Investments*** | Innovation (R&D) – new product development | Streamlined operations and product offerings |
|  | Efficiency | Efficiency |
|  | Brand diversity through acquisitions | Updated information systems  Digital and social media selling tools |
| ***Competitive Position*** | Against large-scale, mass-market producers (i.e. L’Oreal, P&G) | Against direct seller competitors (i.e. Mary Kay, Arbonne) |
| ***International*** | Standardization (Global) | Restructure, with focus on priority markets |

Out of the gate, McCoy has devised a restructuring plan to quickly reverse falling revenue, rising costs of sales, margin instability, and recent losses. Lowering costs will have an immediate effect on profitability, which should improve share prices. Her withdrawal from low priority or underperforming international markets will divert focus to struggling priority markets and to a new direction for the company.

While McCoy will maintain emphasis on Avon’s premium brands and achieving operational efficiencies, she will shift market focus and competitive positioning with a reemphasis on the company’s traditional selling strategy. At this point, it does not appear that the McCoy will pursue growth through an acquisition strategy, but by investing in technologies to support a push marketing strategy. Her international strategy will enable Avon to progress toward a transnational strategy to increase local responsiveness.

* ***Did Jung’s strategy fit the situation? Why or why not? Does McCoy’s strategy fit the current situation? Explain your answer. What suggestions can be derived from the analysis to enhance McCoy’s strategic plans?***

Using the strategic elements identified in the previous comparison to assess fit reveals that Jung’s strategy was well-suited to existing conditions. (This assessment is presented in the table on the following page.) However, she did deviate from a successful business formula; and in doing so, Jung led the company down an unsustainable path.

|  |  |  |  |
| --- | --- | --- | --- |
|  | **Jung** | **Fit** | **Comments** |
| ***Product*** | Up-scaled high-end beauty lines | Yes | Maintained core beauty and skin care line, upgrading products to differentiate and to attract new customers and higher gross margins |
| ***Market*** | Trendy, educated, professional, high-end clientele | Yes | Pursued working and professional women, a rising demographic |
| ***Process*** | Pull marketing – media advertising | No | Adopted approach that disadvantaged the company and abandoned its competitive advantage |
| ***Capabilities/ Investments*** | Innovation (R&D) | Yes | Invested in new product development to differentiate Avon from its rivals |
|  | Efficiency | Yes | Invested in ERP system to improve cost structure and price competiveness against mass-market beauty manufacturers and online rivals |
|  | Brand diversity through acquisitions | Yes | Attempted to reduce over-dependence on single product line – introduced new products to Avon’s line-up |
| ***Competitive Position*** | Against large-scale, mass-market producers (i.e. L’Oreal, P&G) | No | Moved into market position where the company would be at a distinct disadvantage against large rivals with enormous scope and extensive organizational resources |
| ***International*** | Standardization (Global) | Yes, but… | Used a suitable approach for entry to establish and strengthen Avon’s position in emerging markets, but clearly will not be able to sustain a lead in these markets without adopting region-specific product and distribution strategies |

A troubling sign under Jung is that Avon’s earnings expectations were not being met at a time when the industry was growing. She began to receive criticism that the influence of her own style and profile did not align with the company’s core values and vision. Objectively, the analysis shows that Jung’s pull marketing strategy did not match the company’s core competencies. Developing a high-end product line did not take into account the company’s inability to reach that niche segment of women through Avon’s existing direct selling and personal marketing approach. Substituting media advertising to overcome this disconnect (even by increasing advertising dollars year over year) was ineffective. In addition, it eventually became obvious that pitting the company directly against mainstream beauty product companies was a losing proposition. The resource gap was just too great. In contrast, the relationship marketing model remained productive in emerging markets. Additionally, the product development capabilities and the efficiency gains achieved by trying to compete against large-scale competitors will benefit Avon moving forward.

Using the same approach to assess McCoy’s strategy gauges whether her plans fit the current situation and adequately address Avon’s present weaknesses.

|  |  |  |  |
| --- | --- | --- | --- |
|  | **McCoy** | **Fit** | **Comments** |
| ***Product*** | Premium brands (i.e. Anew) | Yes | Maintains core beauty and skin care line, upgrading products to differentiate and to attract new customers and higher gross margins – takes advantage of premium lines developed through Jung’s innovation initiatives |
| ***Market*** | Status and demographics matched to sales representatives’ social network | Yes | Recognizes the need to align process with Avon’s distinctive core competencies and the realistic reach of a quality sales team |
| ***Process*** | Revitalized sales force | Yes | Recommits to the push marketing strategy tied with Avon’s brand and past success – draws upon a competitive advantage built on entrepreneurship and personal marketing |
| ***Capabilities/ Investments*** | Streamlined operations and product offerings | Yes | Addresses issues associated with confusing product line and frequent product introductions – support, product knowledge, service, confidence, motivation, customer loyalty |
|  | Efficiency | Yes | Continues to focus on need to achieve operational economies that enable value product-price offerings to compete with mainstream products |
|  | Updated information systems  Digital and social media selling tools | Yes | Identifies an investment area that, when combined with Avon’s unique relationship marketing strengths, has enormous potential to improve the performance and reach of sales representatives  Provides representatives with contemporary selling tools that will broaden their reach, and shows commitment to restoring representative opportunities and relationships |
| ***Competitive Position*** | Against direct seller competitors (i.e. Mary Kay, Arbonne) | Yes | Removes Avon from an impossible market position where it is disadvantaged against large rivals with enormous scope and extensive organizational resources  Returns the company to a market position where it has advantages and greater potential for success |
| ***International*** | Restructure with focus on priority markets | Yes, but… | Improves the ability to stop declining profits in priority markets; but Avon’s international business is an area of strength with immense growth and profit potential, and withdrawal must be done with caution  Does not increase attention on or influence of local cultures and trends |

McCoy’s strategy appears to be very promising for Avon. It corrects the missteps of the former strategy, returning the company’s emphasis to the intangible advantages provided by its direct sales approach. Competitors cannot replicate 125 years of personal selling experience; and by integrating exciting new social networking and technology tools, the power of its representatives can be dramatically impacted. Some suggestions to enhance McCoy’s strategic plans include:

* Use an upgraded image to attract quality representatives who are professional, upbeat, friendly, helpful, and qualified to satisfy, individualize, and meet the needs of today’s women. The profile will be a demographic of women who are inspired to work hard and achieve success. The network reach of the sales force should be the target market for which new products are developed.
* Use the potential of technological network systems to expand marketing reach, create superior earnings opportunities, and attract top quality representatives.
* Devise specific action steps to address falling income and increase competitiveness in North America. Avon’s domestic strategy should:
  + Remember what works to make Avon unique: samples, convenience, and personal attention. This is critical competitively because online and retail channels can achieve lower costs (therefore prices) but cannot deliver on these service qualities.
  + Improve competitiveness against Mary Kay (with its similar business model and equal focus on empowering women). The major domestic rival now has four times Avon’s number of domestic representatives.
  + Sustain focus on new technology and product innovation to deliver first-to-market products with visible consumer benefits (anti-aging, healthy ingredients, etc.) and priced to attract mass appeal. New products should be beneficial to the defined target market and be quality products that would otherwise not be attainable by the average household. They should be products that Avon’s sales representatives can believe in and know well.
  + Improve relationships with sales representatives; their satisfaction ultimately impacts customer relationships. Actively address their grievances. Help them extend their reach with new tools. Consider policies that better reward the achievements of strong performers. Other revenue, valued at 1.6% of sales on the income statement, shows a category of income that primarily consists of shipping and handling and order processing fees that are billed to representatives. While its impact on profits is minor, it represents $171 million that can be used to incentivize sales representatives.
* Despite the need to reverse downward trends in the U.S., be careful not to design a strategy more suitable to the U.S. market than to international consumers who generate 83% of Avon sales.
* Initiate efforts to increase local responsiveness in international markets. Over the long-term, Avon’s global strategy will be ineffective against increasing competition and changing market-specific needs.
* Pay close attention to the direction of Perez-Ayala. She has significant responsibilities as Senior Vice President and Chief Marketing Officer. In these roles, she is accountable for managing consumer insights and analytics, commercial and digital marketing, product category strategy and execution, research and development outside of the U.S., and the integration of the Liz Earle product line.

Ultimately, McCoy’s task comes down to modernizing direct selling. Through technology, Avon is in a strong position to be able to discover exciting new ways to rejuvenate and enhance its valuable selling model.

* ***Discuss Avon’s decision to retain Jung as the chairman of the board. Do you believe this is a good decision? What is the potential downside of keeping the former CEO in this leadership role?***

Upon Sherilyn McCoy’s arrival at Avon in April, 2012 the company’s board of directors decided to retain former CEO Andrea Jung as the chairman of the board. Keeping Jung in this oversight position is intended to provide McCoy with strategic leadership support.

Jung’s intelligence, experience, innovativeness, and evident willingness to support her successor are all qualities that can be exploited as McCoy establishes herself at the helm of the company. McCoy has a track record of successfully achieving results and driving change across highly diverse operating units with widely varied product lines, customers, distribution channels, and business models. Her ability to see beyond existing structures and systems, to draw from her experience, and to incorporate new ideas will be a valuable addition amongst the leadership ranks of the company. And Jung should be able to help the new leader adjust to Avon’s direct selling business, which is competitively different than the consumer distribution models of her past company.

Generally, separating the CEO and Chairman of the Board roles is a good move. CEO duality is commonly believed to interfere with a board’s ability to monitor top-level managers’ actions and decisions, particularly with respect to financial performance. However, potential problems inherent in this leadership structure could arise if Jung and McCoy are unable to effectively collaborate. Jung could resist new direction or decisions that reverse her previous strategic initiatives. Is she likely to properly address any lapses in performance and accountability? Jung is equipped to provide resources to assist McCoy, but how forceful will Jung be in her oversight? Who will oversee Jung? How will they strike a successful leadership balance?

It is crucial for Avon’s board to establish proper governance mechanisms to address these concerns. The company has already tangled with ineffective internal controls, as the takeover bid by Coty revealed. In fact, ongoing investigation of the board’s failure in fiduciary duty indicates that some change is in order. The board will need to strengthen systems and evaluation processes to ensure that its oversight responsibilities are properly fulfilled and shareholder interests are protected.