The history of avon products inc

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About the Company

Avon Products Inc. is an American company manufacturing and selling beauty and related products all over the world. It started operations in 1886, and the contemporary company was established in the State of New York in 1916. The company's main product categories are: Beauty, Fashion and Home. The products of Beauty division are from the categories of skin care, colour cosmetics, personal care and fragrances. Fashion consists of accessories, watches, fashion jewellery, footwear, apparel, and children's products. In the Home category we can find decorative products, gift, house wares, leisure and entertainment products and nutritional products. (AVON, 2011)

The company's segments are based on geographic location in five regions: North America; Latin America; Western Europe, Middle East & Africa; Central & Eastern Europe; and Asia Pacific. The company has sales operations in 65 countries and territories, and it distributes its products in further 42 countries and territories. The company sells its products through direct-selling channel, employing about 6. 4 million independent Representatives. These Representatives are independent contractors, who earn profit through buying products directly from Avon on a discount price, and selling it to the end customers on a price showed in catalogues. The Representative contacts the customers directly, so the brochure and the Representative together are the main intermediaries between Avon and the customer. (Avon, 2011)

Avon manufactures and packages the majority of its Beauty products. Raw materials like chemicals, essential oils, packaging components and containers and are purchased from different suppliers. Most of its Fashion and Home products are obtained from different third-party suppliers. Furthermore, the company designs the brochures that are used to sell its products by Representatives. Packages are designed as well by artists and designers staffed by Avon. Their work is affected by the availability and cost of materials like glass, chemicals and plastics. The company tries to implement an ERP (enterprise resource planning) system on a global basis. It is expected to make the supply chain and financial transaction processes more efficient. The company plans to implement it more phases over the next years. In their most significant markets it has been already applied. (Avon, 2011)

Porter's 5 Forces

The components of Porter's 5 Forces Model are: Threat of Entry, Industry Competitiveness, Buyer Power, Supplier Power and Threat of Substitutes.

Threat of Entry

The threat of new entrants to this market is insignificant. To manufacture cosmetics they would need expertise and licence. The economies of scale play an important role as well. Companies in this industry have a great past, and during this time they have built valuable networks and relationships with suppliers, retailers and customers. To establish a plant it would have huge capital requirement and would cover the demands of only a small segment or region.

Industry Competitiveness

Avon is working in a highly competitive market segment. They face strong competition in beauty and beauty-related products both domestically and internationally. The degree of competition and the number and strength of competitors varies from country to country. The company has to compete against companies that are selling their products as well through direct-selling or through Internet (Oriflame, Mary Kay), and against companies whose products are sold through the prestige retail channels (The Body Shop) and mass market channels (L'Oreal). The company's principal focus is on the competitors who are using direct-selling channel, and secondary they compete with other companies who are selling through retail establishments and other channels. They also have many competitors concerning the two other product categories like gift shops, department stores, specialty retailers, few large and many small companies who sell fashion jewellery. But as the Beauty segment is creating around 70% of net sales, Avon doesn't tries to pay much attention to the competition in other segments. (Avon, 2011) The exit barriers are huge in the industry: lot of investments are made into long-term assets, especially plants, buildings, etc. At Avon the amount of non-current assets is about the half of total assets.

Buyer Power

Avon's customers have weak or rather no bargaining power. Their concentration on the market is small. As I mentioned before the company has about 6. 4 million independent Representatives, and none of them is responsible for more than 10% of net sales. Customers are loyal to the brand; sometimes they build tight relationship with their Representative. The switching costs are low, as we consider not only money but time and efforts as well. Although the quality of the product is really important to them: if it turned out that Avon is using chemicals that can cause skin damage, allergic reactions, or that they are experimenting on pets, they would boycott buying their products.

Supplier Power

Avon has several suppliers for its Beauty, Fashion and Home products. Avon is manufacturing its goods itself, so it needs raw material supplies in Beauty segment, product supplies in Home and Fashion segments and packaging supplies for all the segments. Although the quality of raw materials and ingredients are very important, the loss of any supplier wouldn’t have a material impact on the company’s ability to source the necessary raw materials, packaging materials or products for Fashion and Home. (Avon, 2011)

Threat of Substitutes

The threat of substitutes is high, as the customer can choose among several brands ranging from cheap and bad quality products through cheaper products but mainly in the same quality to expensive and higher quality products. In the skin care industry there are not only the competitor’s products threatening, but several “ home practices” (like honey or cucumber packs, etc.) that are cheaper or more natural solutions to the same problem. In the Home segment again there are some home-made substitutes as well. As we talk about fashion and jewellery there are some homemade items, but people can buy fashion goods with traditional motives supporting domestic products.

To sum up I can state that the appropriate strategy based on Porter's 5 Forces for Avon would be to differentiate its products from the competitors by making an effort to make them more natural. The company tries to differentiate itself by supporting foundations, and showing itself as a socially and environmentally responsible company, but this strategy is easy to copy, and in the next years it might be a basic expectation of customers to all companies. The company might try to reduce costs, to offer their products cheaper, but not on the expense of the quality, because it is more important for customers.

SWOT Analysis

Strengths-S

Established brand name

Long history

One of the leading companies in manufacturing and selling cosmetics

Customer loyalty

Innovative company

Pricing Power (strong bargaining power against customers and suppliers)

Weaknesses-W

Low Research and Development activity

Not diversified product portfolio

Using only direct-selling channel

Not developed or consistent ERP system

High advertising costs

Decreasing presence net sales in North American market

Opportunities-O

Innovation: new products, new manufacturing technologies, new combination of ingredients, more efficient products

Developing more natural products

Involving students in marketing or innovations from higher education through contests or championships

Raising money from financial markets (stock exchange, debt, etc.)

Acquiring new markets

To be more efficient through ERP system (after complete implementation)

Use Representative's selling data for customer information

Threats-T

Strong Competition

Dependence on third-party suppliers in Home and Fashion segment

Price war

Disadvantageous changes in currency exchange rates

External changes (taxes, legal, politics, regulations, government, etc.)

Too dependent on the knowledge and attitude of Representatives

Financial Analysis/ Ratio Analysis

In the next part I am going to analyze the company with the help of ratio analysis.

Liquidity ratios

The company's liquidity is not satisfying, but steadily improving, as it is shown in Table 1. For all ratios the number are getting better since 2007. The current ratio should be around 2, but the company's numbers don't reach that amount. The Quick ratio is considered to be good between 1 and 2. In Avon's case it is below this figure. The Cash Ratio is low, but it doesn't mean necessarily a bad strategy, because this means as well, that there are few cash and cash equivalents which aren't in use and which don't create value. This low Cash ratio is dangerous if it jeopardizes the company's solvency. The company prefers long-term debt to short-term debt especially in the last three years. The company should pay more attention to its liquidity strategy, especially concerning cash and cash equivalents.

Table 1: Liquidity ratios

liquidity. png

Source: Own calculations based on Avon's Annual Report 2011, 2009, 2008

Working Capital Management

The ratios in Table 2 show the management of Working Capital. The Net Working Capital is growing year by year since 2007. In 2009 there is a projecting value. The inventory period is longer year by year. This means that since 2008 inventories are on stock 7 days longer. This can reflect on a poor inventory management, because inventories spend in average around 1/3 of the year in stock. There is an urgent need for implementing a company-wide ERP system. The company is collecting receivables from customers within one month, but paying for suppliers in 5-6 months. This reflects on its strong bargaining power both against suppliers and customers. The company's strategy is to collect money on a steady, 1 month basis, to be able to calculate with revenues, and to postpone accounts payable as long as possible, to be able to invest that money. In my opinion the working capital management of the company is good; it is utilizing its strength in the supply chain.

Table 2: Working Capital Management

wcmgmt. png

Source: Own calculations based on Avon's Annual Report 2011, 2009, 2008

Asset Management

Table 3 shows Avon's Asset Management ratios which can reflect on its asset management strategy. Total Asset Turnover is around 1. 5 times per year. Working capital turnover is around 5 times per year and fixed asset turnover is around 3 times per year and it slowed down since 2008. I already mentioned that its accounts receivable turnover is very satisfying, especially compared to payment turnover, but inventory management should be improved. The company's strategy in asset management is to keep it on a constant level, there are no projecting numbers. This strategy's advantage is that the future is easy to predict, and it is easy to calculate with historical data.

Table 3: Asset Management

assetmgmt. png

Source: Own calculations based on Avon's Annual Report 2011, 2009, 2008

Investments and Cash Flow

Avon's Investments and Cash Flow ratios are shown in Table 4. According to the numbers the company has significant Free Cash Flows at the end of the year, but its reinvestment rate is very low. Depreciation is at a steady low level as well, so there weren't significant investments into fixed assets. It turns out from the data that the company has not efficient reinvestment strategy that would be necessary for building a base for further expansion, continuous growth and development.

Table 4: Investments and Cash Flow

inv&cf. png

Source: Own calculations based on Avon's Annual Report 2011, 2009, 2008

Profitability

Table 5 shows that the company's profitability is steady and it is easy to predict. There are no projecting numbers again, which shows that Avon is a reliable company with steady and high quality of earnings and balanced operations. Return on Assets (ROA), Return on Equity (ROE) and Return on Invested Capital (ROIC) ratios show that the profitability is low. So investing in the company is primarily recommendable for investors who are rather risk avoiding and don't expect high return on invested capital.

Table 5: Profitability

profitability. png

Source: Own calculations based on Avon's Annual Report 2011, 2009, 2008

Growth

Avon's Growth ratios are shown in Table 6. The numbers in the table show that the company is growing really slowly. Sales even dropped in 2009.

Table 6: Growth

growth. png

Source: Own calculations based on Avon's Annual Report 2011, 2009, 2008

Conclusion

After looking over Avon's strategic and financial analysis it can be stated that the company has high potentials. It has very good opportunities to expand its markets or to launch some innovative products. Its reputation and loyal customer base can be guarantee for its success. The company has a very good supplier chain management strategy; it uses its bargaining power to enforce its Collection-Payment strategy. The highly competitive environment of the industry is a real threat and is limiting the company's opportunities, especially growth opportunities. The company should invest more in R&D and ERP system to improve its inventory management and to be able to find a niche in which it could differentiate itself and in which direction it could grow.