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Network marketing- reality, myth, dream or a success mechanism: a review

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ABSTRACT: As the Business Enviornment become more and more competetive, companies are forced to push themselves to very edge of their capabilities. Ultimately the success of companies relies on their human resources and business and marketing strategies wich can help them to show up in global markets. So Network Marketing has become increasingly used method in order to ehance the small and large logistic companies performance. Multi-level marketing is a marketing approach that motivates its participants to promote a certain product among their friends. The popularity of this approach increases due to the accessibility of modern social networks, however, it existed in one form or the other long before the Internet age began (the infamous Pyramid scheme that dates back at least a century is in fact a special case of multi-level marketing). The India Direct Selling Association (IDSA) has projected that the network marketing industry will be around Rs 9000 crores by 2013 end.

The purpose of this paper is to provide better understanding of how Network Marketing is used as Marketing strategy and tool to develop logistic companies business in new millennium. The idea is to seek roots in localised practices in rapidly unfolding globalisation and thus paving the way for ―globalisation‖.

Key Words: Network Marketing, Logistic, Globalization, Customers, Mechanism.

1. INTRODUCTION

Network marketing refers to the technique that allows network-marketing decisions to be made based on the results of the collection and analysis of user profiles. Business organisations have long relied on direct marketing to target customers without spending a lot of money on retail distribution. However the Network (Multilevel) Marketers have taken the direct model one step further, i.e. not only they do the sales, but recruit and train new distributors i.e., independent sales persons who are members in the network marketing company. This ‗ingenious' method was first popularized by Amway in 1950's. The fundamental idea behind multi-level marketing is that Alice, who already purchased the product, is rewarded for referrals, i.e., for purchases made by Bob as a result of Alice's promotion. The reward mechanism associated with multilevel marketing may take various forms. In particular, Alice may be rewarded for both purchases made by Bob and for Bob's own referrals in a recursive manner. The potential to accumulate small rewards from each person to a sizable sum is important as it allows advertisers to attract early adopters and trendsetters that are of great value to them. On the downside, the possibility of gathering a large sum has also inspired more illicit versions of multi-level marketing, namely pyramid schemes. The big draw card in network marketing is the commission paid not only for direct sales made by the salesperson , but also from the sales made by the recruits made by him. That is, if you get friends and relatives to join up, you get a commission not only from the products your friends and relatives purchase, but also from the sales they make to their friends. This ‗wonderful' opportunity attracts prospective candidates to join network marketing companies. Studies reiterate the fact that a 100 percent annual turnover rate among sales personnel in certain network marketing company is not unusual. According to the Direct Selling Association in the United States, 70% of the revenue from the direct selling industry was generated by network marketing companies and most of this came from the better known companies, such as Amway, Nuskin or Shaklee, that use multilevel instead of single level compensation plans.

In the case of India, network marketing momentum was conspicuous in India during mid 90‘s followed by the establishment of the Indian arm of Amway Corporation. The total turnover of network marketing companies in India was estimated at Rs.30,104 crores in 2005 with an annual growth rate of 25% (Tribute, 2006). Amway India, Avon, Tupperware, Oriflame and localised companies like Modicare, Hindustan Lever Network are the major network marketing players in the Indian market. Indian Direct Selling Association (IDSA) facilitates membership to genuine network marketing companies. The IDSA projection for 2013 for the network marketing industry is Rs.9000 crores. According to National Council of Applied Economic Research, the Indian middle class was projected to grow from 1.1 crore households in 2001-02 to 1.7 crore households in 2005-06 and the figure is fixed to 2.8 crore by 2009-10. The above figures justify the rosy picture of network marketing in India.

There are three parties in network marketing: the main company that manufactures the products, the net worker or retailer, who sells the products, and the customer, who buys the products. In network marketing, a network of independent retailers manages the organization‘s marketing and selling. Network marketing salespeople arrange different face-to-face presentations and interact directly with consumers. They also recruit new retailers to the organisation from their social networks. Thus, the multiplying effect on network marketing will expand when these distributors continue their recruiting or sponsoring efforts. This multiplying effect, an important element in the recruiting or sponsoring function, makes the network marketing quite different from other types of direct selling involving paid sales persons.

The sunflower and pyramid are the two common business models in network marketing. In sunflower model (Unilevel model), each distributor can develop as many nodes as possible, whereas in pyramid model (binary model) each distributor enrolls only just two people and they in turn do the same. In the Unilevel model a distributor gets a business share of the total volume in his team and not money on registration. The product purchased is considered as the first registration. In binary model money is made through registration and the main income is from the dropouts.

Mainly due to internationalisation and globalisation of freight forwarding and logistic service providers, it has generally been accepted that network marketing is significant for many companies business progress.

2. COLLECTING PERSONAL PROFILES

Collecting a personal profile is the key step toward one-to-one marketing. Basic attributes in a personal profile for a person include age, sex, nationality, habits, purchasing power, etc. In a broader sense, the profile also includes a person‘s answers to various consumption questions that can reflect one‘s purchasing behaviour. However, how much data can be used to describe a person and how much of the intended data can be collected explicitly? On top of the personal profiles collected, an equally important issue concerning one-to-one marketing is the integration of profile data for long-term user data collection. Although each marketing survey geared to a particular marketing objective may have its particular set of attributes, many of these surveys share common attributes. In order to take advantage of the shared attributes, an integration process that avoids repetition in subsequent collecting is highly desirable. For instance, the Passport system 2 by Microsoft aims to provide, for each sign-on, an integrated view of the customers‘ data. In line with the design philosophy, we have proposed an interactive questionnaire mechanism that incorporates the idea of excluding redundant data collection. Meanwhile this design approach also integrates all personal attributes in a single profile database to suit different marketing objectives. With an analysis profile engine installed to suit a particular marketing objective, this integrated database can then be analyzed to produce more precise data for network-marketing decision making.

2.1 Profile Analysis

Profile analysis aims to analyze the relations between attributes in order to predict the possible value of other unfilled attributes. In this, we are concerned with which attribute values will lead to the target attribute value. For example, we would like to know who is willing to purchase product A. The analysis will first define ―having purchased product A = yes‖ as the *target attribute value* and try to find the related attribute values for members who have already purchased product A. An attribute is called a *related attribute* for a target attribute value if most of the people having the target attribute value also have the same value for the related attribute. In other words, the related attribute can be treated as the cause and the target attribute value as the effect so that the related attribute will result in the target attribute value. If a person has the related attribute value (cause) but has not purchase product A (the effect), then he/she will be our marketing subject.

Tthe concentration factor of an attribute for determining its relation with other attributes can also be defined. For a given set of members, we would like to examine whether the value of each attribute concentrates on a specific one. If so, this common feature could be the cause of a target attribute value. We assume that all of our attributes are discrete so that the number of answers for an attribute is finite. For example, attribute Y has two possible answers (y1, y2), and attribute Z has three possible answers (z1, z2, z3). Assume that in the current database we have 100 records that contain 75 records of Y=y1 and 25 records of Y=y2. Similarly, there are 50 records of Z=z1, 30 records of Z=z2, and 20 records of Z=z3. It may look correct that Y=y1 is more concentrated than Z=z1 since it has more records. However, it is not fair for such a comparison since attribute Z has three options while attribute Y has only two. Therefore, a normalization processing on the results is necessary for making meaningful comparisons.

3. CHARACTERISTICS OF NETWORK MARKETING ORGANIZATION

Network marketing is fast expanding and controversial form of direct selling. Network marketing refers to a manner in which NM companies organize their direct selling functions. Marketing channel of a NM company consist of independent sales people which create and maintain a network type of sales organization. Network marketing sales people (NM distributors) genuinely build their business on their social networks by introducing, training and motivating new members in their organization. To a significant extent, distributors are responsible for and have the control over customer and distributor portfolio of the NM company. NM distributors are *independent contractors* (i.e. non-employees) of a principal company. Distributor contracts detail the conditions for allowed performance within the organization, as well as the rights and obligations following particular performance. Distributors are typically allowed to purchase the products on a discount, retail them to end-customers and receive sales bonuses in return and introduce new members into their down-line and receive bonuses based on their sales volume. Relationships between distributors have some specific characteristics as well. Most importantly, the relationship between a focal distributor and a new distributor is informal i.e. no formal contracts whatsoever are involved. However, a new distributor is ‗positioned' on the first level of the down-line of a focal distributor that has ‗recruited' him. The focal distributor thus becomes his ‗sponsor', and is expected to introduce the company policy to him (the term mentor might be more illustrative). On

return, the principal company rewards the sponsor financially for the sales generated by new member. Although no legal obligations are involved, these _sponsorship‘-relations form financial ties between distributors in the network.
However, no specific behaviours are required from the sponsor in the process of creating down-line organization. Certain amount of personal selling is required in order to receive network bonuses, but in terms of acting with the down-line, passive and active sponsors are on the same line. Thus, financial rewards are based purely on sales performance rather than behaviour. Following that no obligations relate to the membership of the organization as such, and no organizational (i.e. legal) authority relates to the distributor relationships, all performed distributor behaviours – sales related as well as other behaviours- are discretionary by definition. As distributors are independent contractors (i.e. non-employees) of NM company, they decide themselves into which organizational role and in what manner they start to aim after joining the organization.

4. From Chains To Networks

An overview of the development of logistics from 1960‘s upto present shows the whole to be optimized has changed considerably. In 1960‘s and 70‘s companies did not talk about logistics as it is defined today. They took care of physical goods because they had to and they did it with technical approach related tologistic operations such as transport,warehousing and handling, resulting in very local optimizations. In the beginning lf 1980‘s companies tried to optimize goods flow in order to cut logistics costs. They developed a three step approach including the improvement of outboud (distribution), internal (production) and inbound (supply) flows. It has become important that the management dimension of those questions was important as technical ones. Step by step companies understood the strategic power of logistics but the optimization was then restricted to borders of the company. While developing integrated logistics, industrial and commercial firms began to outsource logistic operations to gain cost control and flexibility. They gradually left transport, storage, warehousing and order recieving in logistics provider care. Further it became obvious that in order to improve the overall logistic service offered to the end customer at minimum cost and with high flexibility, companies should cooperate and coordinate their activities.

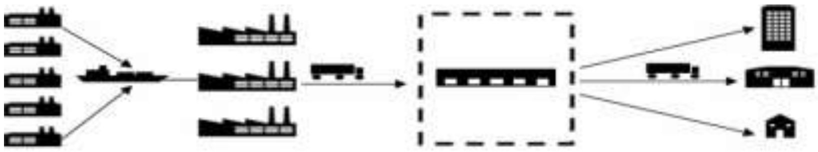

Fig 1. Supply Chain Map and Role of Logistics

5. THE REFERRALS TREE MODEL.

There are many possible ways to take the social network that forms the basis of the referral process into account. In principle, one may wish to consider the times at which promoting messages were sent from one user to another, to consider referrals that were not followed up by a purchase of the product being promoted, or even to consider the social links along which a referral was not made. However, all of this information may not be available to the original seller. We therefore take the straightforward approach of looking only at the structure of successful referrals. For each buyer, we mark only a single referrer for introducing the product to her (in reality, this would typically be specified at the time of purchase). The induced structure of referrals forms a collection of directed trees, each rooted at a node that corresponds to some buyer that has purchased the product directly from the seller. We shall refer to this tree collection as the referrals forest, denoted T , and to the rooted trees in T as the referrals trees. We find the assumption that T can be maintained by the seller sufficiently weak. It should be clarified that the referrals forest corresponds to a single multi-level marketing campaign (typically associated with a single product). Moreover, social network users that did not purchase the product are not represented in T even if some of their friends attempted at promoting the product to them. For ease of presentation, we assume that T is fully known when the rewards are to be distributed, although all the mechanisms explored are also suited for incremental payments performed online. It will also be convenient to identify the buyers with their corresponding nodes in T , denoting the reward of (the buyer corresponding to) node u under the referrals forest T by RT (u).

6. CONSTRAINTS ON THE REWARD MECHANISM.

The reward mechanism is essentially a function that maps the referrals forest T to the non-negative real rewards of its nodes. However, not every such function should be considered; specifically, we impose three constraints on the reward mechanisms.

The first one is the subtree constraint: R_T (u) is uniquely determined by T_u, namely, by the subtree of T rooted at u. This is sensible, as each user u can really be credited only for bringing in users she promoted the product to, either directly (the children of u in T) or indirectly (lower level descendants of u). Moreover, a dependence of R_T (u) on the position of u within T (rather than on T_u only) may result in an undesirable behaviour on behalf of u, In some cases u is better off delaying the purchase of the product after receiving a referral in hope for a better offer i.e. for a referral that would place u in a better position within T . One of the consequences of the subtree constraint is that there is no point in dealing with the referrals forest T in full, but rather focus on trees which are rooted at the nodes whose reward we are trying to calculate. In other words, the reward mechanism is completely specified by the function R(T) that maps the rooted tree T to the non-negative real reward of its root (which may be an internal node within the whole referrals forest).

The second constraint that we impose on the reward mechanism is the budget constraint: the seller is willing to spend at most a certain fraction $\alpha \leq 1$ of her total income on rewarding her buyers for referrals. Given that the price of the product is β, this means that the total sum of rewards given to all nodes is at most $\alpha.\beta(T)$. We assume without loss of generality that β and α are scaled so that $\alpha.\beta=1$. Thus, $\sum R(T_u) \leq [T]$, such that u is subset of T.

The third constraint is the unbounded reward constraint: there is no limit to the rewards one can potentially receive even under the assumption that each user has a limited circle of friends in the underlying social network (imposing a limited number of direct referrals). Formally, the unbounded reward constraint dictates that there exists some positive integer d (a property of the reward mechanism) such that for every real R, there exists some tree T of maximum degree d (i.e., every node has at most d children) such that $R(T) \geq R$. In particular, this constraint implies that the reward mechanisms we consider must take indirect referrals into account.

7. NETWORK MARKETING JOURNEY IN INDIA

MLM was the fastest growing sector of the direct selling industry worldwide. In 1988, the total revenue generated by MLM was $ 12 billion, which doubled to $ 24 billion by 1998. The direct-marketing industry in India was about Rs 6 billion in 1999. This was a growth of 62% over the previous year. In the pre-liberalization era, network marketing in India was usually in the form of various chit fund companies like Sahara India. These had a system of agents, who simultaneously mobilized deposits and appointed sub-agents for further deposit mobilization. Companies such as Eureka Forbes and Cease-Fire pioneered the direct selling system in the country with a sales force that was trained to make direct house-to-house sales. Oriflame International was the first international major to begin network marketing operations in India in 1995. This was followed by the entry of Avon India in late 1996.

Tupperware, with a product portfolio comprising plastic food storage and serving containers, also entered India in 1996. Later, Avon's decision to opt out of the MLM setup came as a major setback to the industry.3 The first homegrown MLM major was Modicare, started by the house of Modis in 1996. Modicare's network was spread across northern and western India. Commenting on the Indian MLM experience, S.K.Gupta, COO said, "The concept is especially relevant for India because of the highly fragmented retail structure, high brand proliferation which limits shelf-space and massive brand wars both at the trade and advertising level." The direct selling industry in India was in its initial stages even in early 2001. Besides Amway, Oriflame Avon and Tupperware, other players included Lotus Learning, LB Publishers and DK Learning, all selling books. All the direct selling companies were members of the Indian Direct Sellers' Association (IDSA), and were bound by its code of conduct. While in international markets, a wide range of products was successfully sold directly to homes, this was not the case in India. In the mature economies, customers were fully aware of the competing products available, whereas in developing economies such as India, awareness levels were comparatively low. Industry observers commented, "The way the market is booming, no direct sale company can meet all its customers only through its own sales force." However, MLM companies opted for direct selling as against the high visibility retail set up for competitive cosmetics players such as Revlon, aiming to get an image of exclusivity. There was some resistance to the network-marketing concept in India, as Indians preferred the security of a job. Being a salesperson in an MLM setup did not provide this security. This hampered the company's ability to attract competent personnel. The problem was aggravated by the fact that companies treated direct selling as 'just another' promotional tool, while it was mainly about motivation. One positive aspect of network selling was that it was very convenient for women as the job could be done part-time and at hours of their convenience.

Also, the products sold also usually targeted at women, and this made it easier for the Indian women to accept the distributorships. Most Indian direct selling failures stemmed from the fact that they did not understand the concept thoroughly. Companies who opted for advertising in the media soon found that it had a negative impact. Advertising created a suspicion in the mind of the salesperson that the company was taking direct orders and thus, reducing commissions.

In some cases, it also negated the impact of demonstrations. Eureka Forbes handled this carefully, when it advertised not its product, but the salesperson as a friend of the customer. Advertising went hand in hand with retail, as people ought to be told where to go and get the product. In an MLM setup, advertising was not the best way to spend money. Though this did sometimes result in inadequate product exposure, the money which would have been spent on advertising was usually diverted into training and motivating the salesperson to contact as many customers as possible. Though Oriflame and Avon did advertise, it was mainly attributed to their being prima-facie into cosmetics and personal care, thereby involving an image factor. Amway, which was into home care products in a big way, had decided not to go in for advertising on a scale as large as adopted by Oriflame and Avon. Competition was intensifying in the industry in the early 21st century. Amway seemed to be faring better than competitors like Modicare - a fact attributed mainly to its premium brand image. Both Amway and Modicare were not the typical door-to-door selling companies, as they sold only to customers known to their distributors.

While Amway targeted only the upper section customers, Modicare targeted the middle and the upper middle class customers. Some of Modicare's products were priced at one-fourth of the price of Amway's products. Modicare sources said this was because its products were priced for the Indian market, while Amway's pricing was more in tune with i ts global counterpart. Modicare was even willing to reduce its margins in certain cases. Also, Modicare offered 100% refund even when the product had been used, unlike the 75% refund offered by Amway. This could turn out to be a cause for concern for Amway in the long run.

10. CONCLUSION

Only through a Network, Company is able to truly achieve worldwide coverage for its clients. People join the network marketing mainly because of persuasion by friends and relatives. Network members who were in the business for the last two years, contacted relatives more than friends and colleagues to join as channel members while those who had more than two years experience contacted friends more than relatives and colleagues. Network Marketing Strategy also points to offer complex global logistic services to interconnect the world market via global network and finally the scheme aims to integrate the firm‘s abilities into the net and to facilitate their access to the logistic services by a common platform.

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