Socio-Economic Impact of Direct Selling: Need for a Policy Stimulus

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The Background

- India - fastest growing economies in the world
  - Expected to be the 12th largest economy by 2015
- Growing Consumer Market
  - India ranked 12th largest consumer market in 2007, expected to be the 5th largest by 2025
- Different distribution channels are evolving, modern retail growing – India has become an attractive destination for foreign retailers and manufacturers, entry of Indian corporates into retail
- Many store and non-store formats have evolved
- Direct selling: one of the fastest growing non-store format

  Direct selling refers to selling of goods and services to the consumers away from a fixed retail outlet, generally in their homes, workplace, etc., through explanation and demonstration of the product by direct sellers
- One of the most labour-intensive segment

Objective of the Study

- *To examine the socio-economic impact of direct selling in India, focusing on how the benefits can be leveraged through appropriate policies*
- Methodology: Primary survey of over 2,500 individuals covering direct selling companies, direct sellers, consumers, supply chain agents, manufacturers, policymakers and legal experts. The survey was conducted in 2009-10 and it covered 24 cities

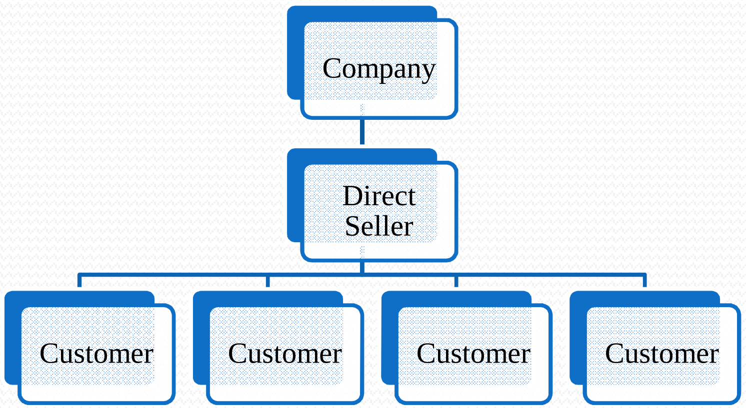
Structure of the Report

- ✓ Chapter 1 covers definition of direct selling and its difference from other multi-level marketing schemes
- ✓ Chapter 2 presents the global overview of direct selling
- ✓ Chapter 3 presents an overview of direct selling in India
- ✓ Chapter 4, 5 and 6 summarize the survey findings
- ✓ Chapter 7 presents the key conclusions and the way forward

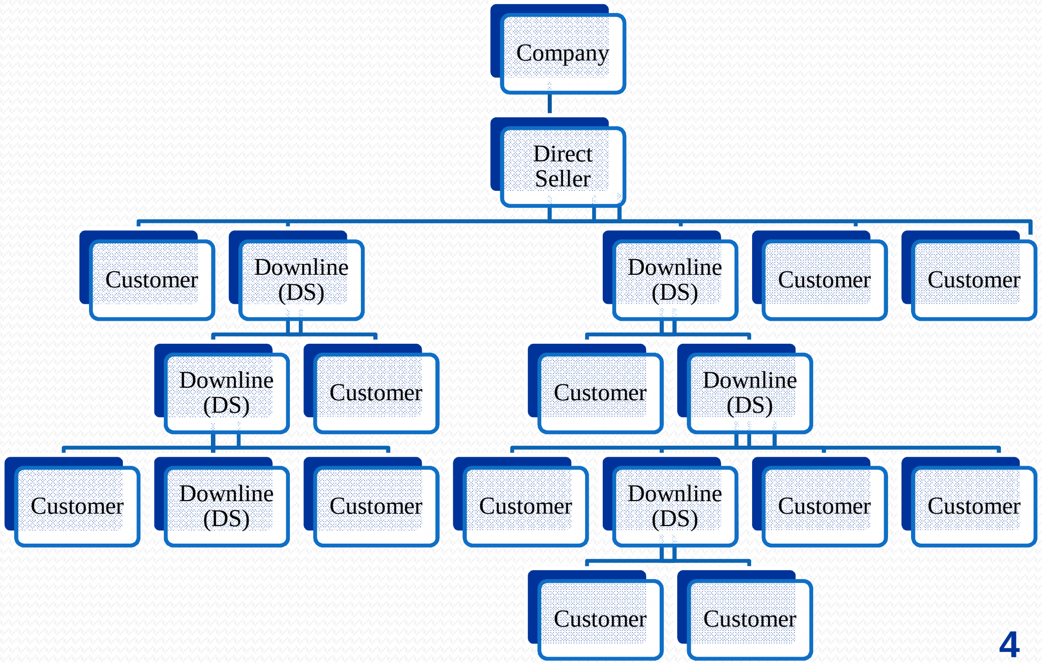
What is Direct Selling?

- No uniform definition
- Wholesale, retail or a separate line of distribution?
- UNCPC Version 2 (code 624) classifies it under non-store retail format
- Key components :
  - It involves B2B and B2C operations
  - Sales made through personal explanation and demonstration by sales representative
- Different models of direct selling:

Single-level marketing (SLM)



Multi-level marketing (MLM)



Direct Selling *versus* Other Fraudulent MLM Schemes

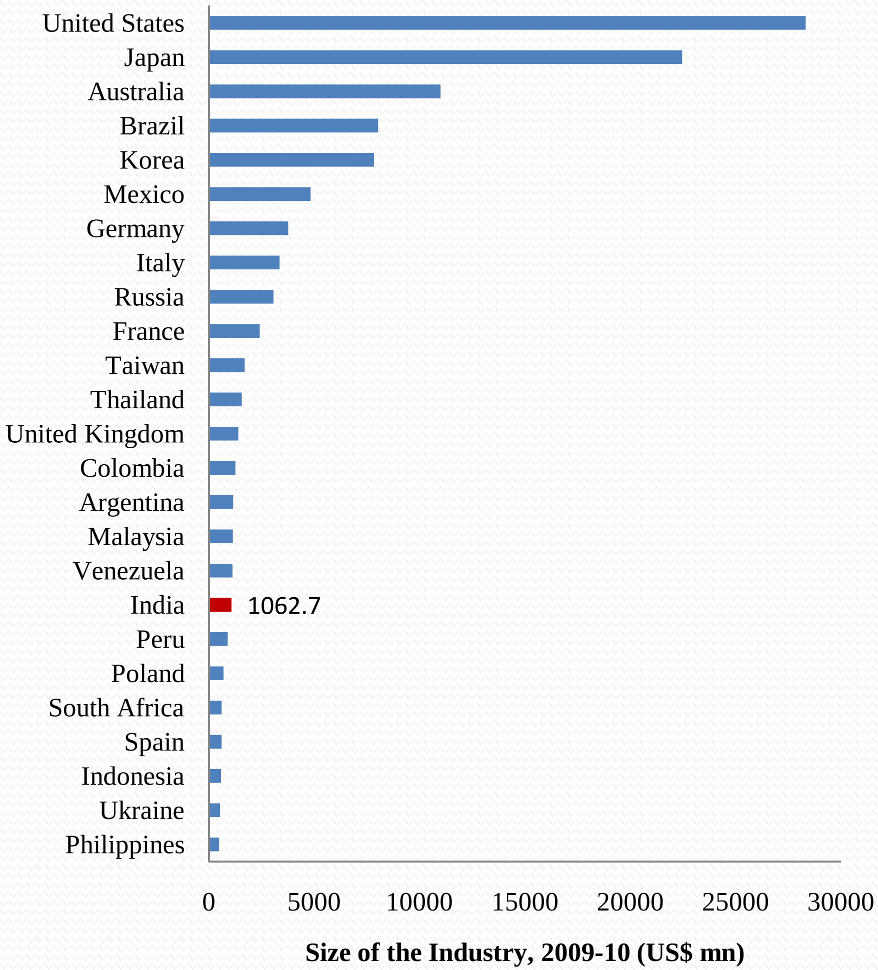
- Pyramid schemes emphasize on vertical expansion of network, wherein a person receives commission irrespective of converting a sale.
- Ponzi schemes involves money laundering across a network of people and does not involve a sale component.

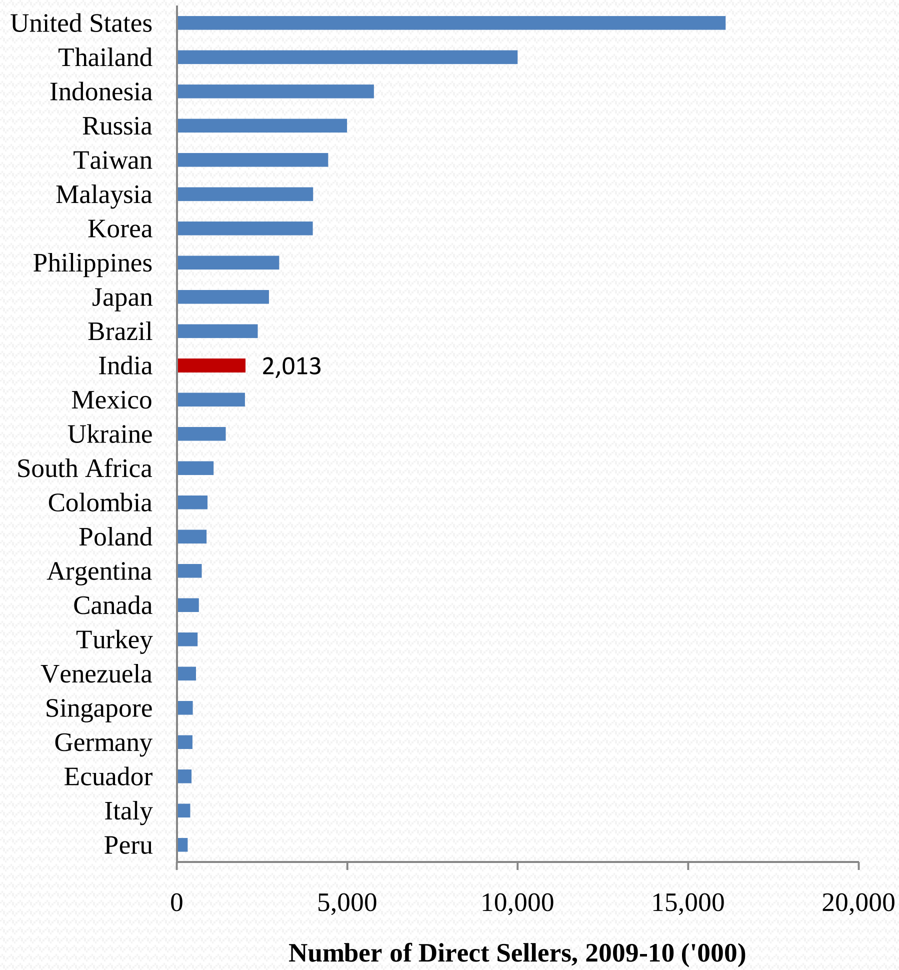
Direct Selling	Pyramid Schemes
Direct sellers at all stages have equal opportunity to make money	Money is made largely by early entrants
Compensation is based on sale of goods and/services	Compensation based on recruitment rather than on sales
Returns are dependent on motivation and come slowly	Returns are easy and quick
The price of the product is according to the value of the product	"Push competition" is encouraged as products are mostly overpriced and may not justify their intrinsic value
Products are supplied to meet genuine demand and direct sellers are encouraged to hold minimal inventory and replenish as and when need arises	"Front loading" is encouraged. Therefore, products are thrust upon the direct sellers, irrespective of their abilities to sell the product and the actual market demand
The initial cost incurred is low	The initial cost incurred is high
Buy-back facility is offered	Buy-back facility is not offered

Global Overview

- Started in the US in 1900s, grew in the 1970s and 1980s
- Globalised in the 1990s
- Major markets – US, Japan, Germany
- Fast growing markets – Brazil, Korea, Russia
- India's ranking in terms of size of the sector improved significantly: 18^{th} in 2009-2010 from 25^{th} in 2008-2009
- Despite global slowdown, number of direct sellers in India increased between 2008-09 and 2009-10, ranked 11^{th} in 2009-2010
- Sales revenue per direct seller is low for India – ranked 47^{th}
- Global Slowdown
  - Less impact on direct selling as compared to retail
  - Even in countries like US, the number of direct sellers has increased

Global Overview Contd.





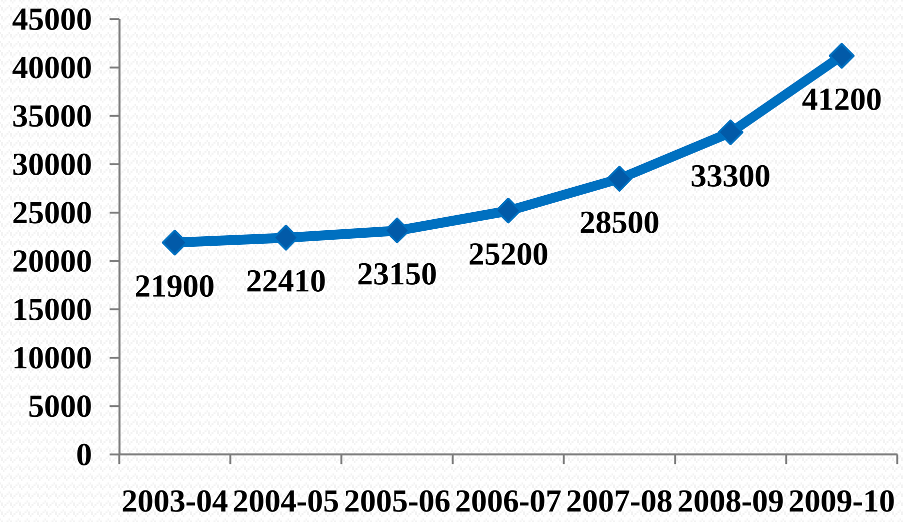
Sector is globally evolving – technological innovation, different operating models

Global Regulations

- Varies across countries
- Code of conduct (largely voluntary), formulated by Direct Selling Associations
- Regulations: US, Malaysia and Singapore
- Some key features of regulations:
  - Identify genuine direct selling companies
  - Differentiate between legitimate and non-legitimate practices - ban fraudulent practices
  - Consumer protection
  - Product-specific regulations – additional clearances required
  - Licensing and/or registration of direct selling companies
  - Sector-specific regulations – Malaysia
  - Treatment of direct sellers – self-employed

Overview of Direct Selling in India

- Started in 1980s – gained momentum in 1990s with the entry of foreign companies
- Size of the sector has grown by 60% between 2003 and 2010
- Products diversified from consumer durables to health and wellness, cosmetics, personal and household products
- From Tier I cities penetration into Tier II and III cities, now targeting rural areas
- Growing at 20% – expected to reach ₹71,200 million by 2012-13



- Number of direct sellers increased from one million in 2001-02 to three million in 2009-10
- Genuine direct selling companies in India – only 30 (excluding insurance companies)

Regulatory Structure

- No **Nodal** ministry
- DIPP – FDI policy, Ministry of Consumer Affairs, Food and Public Distribution – internal trade and consumer welfare
- A ‘State’ subject under Indian Constitution
- Governed by over 30 regulations at the centre, state and local levels
- No sector-specific Act
- **Consumer Protection Act, 1986 and the Consumer Protection (Amendment) Act, 2002:** protects consumers of both goods and services from unfair or restrictive trade practices, redressal of grievances of consumers
- **Prize Chits and Money Circulation Scheme (Banning) Act, 1978:** checks prize chits and similar financial schemes based purely on money circulation without any sale of goods and services
    - In states like Andhra Pradesh, Sikkim and Kerala, direct selling companies were mistaken to be ‘money circulating companies’ and were charged for violating the Act

Survey Findings: Direct Selling Companies

- Primary survey of 16 direct selling companies
- Majority of the companies have pan-India presence and long-term commitment in the Indian market
- 80% foreign companies have wholly-owned subsidiary
- 75% follow multi-level marketing structure
- Presence in Tier I (43% share), Tier II (38%) and Tier III (19%) cities
- Investment: 70% in equipment, followed by manufacturing facilities
- Investment in R&D is low
  - Survey found that if a stable operating environment is provided, companies could invest in R&D and develop India as a R&D hub
- Majority of expenditure in organising events and product promotion
- Own manufacturing facilities - account for 30-35% of the products sourced, rest contract manufacturing largely through SMEs
- Average spending on training of direct sellers – ₹8.6 million per annum and on training of employees – ₹1.5 million per annum

Employment

- Direct Employment – direct sellers and employees of direct selling companies
- Indirect Employment – in sectors like manufacturing, packaging, etc.
- On an average, a company with pan-India presence employs 200 employees
  - Majority are in urban areas at non-managerial positions
  - Majority of the employees are skilled and have permanent employment contract
- Self-employment option – direct sellers
- 13 companies had more than 3 million registered direct sellers of which 1.07 million are active direct sellers
- Direct sellers are compensated through commissions, bonuses, non-cash equivalents, etc.

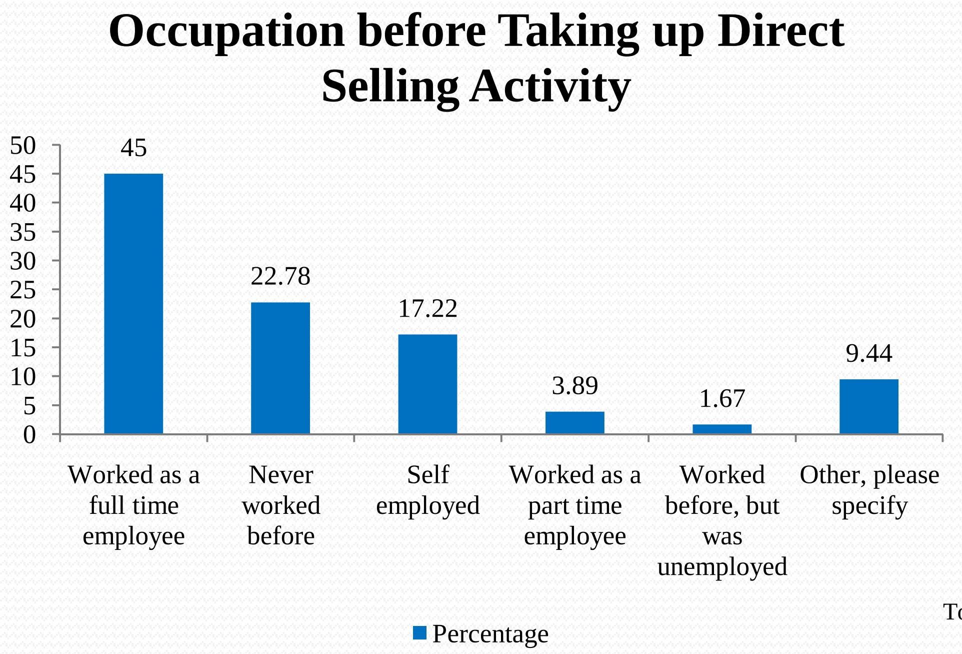
Other Benefits

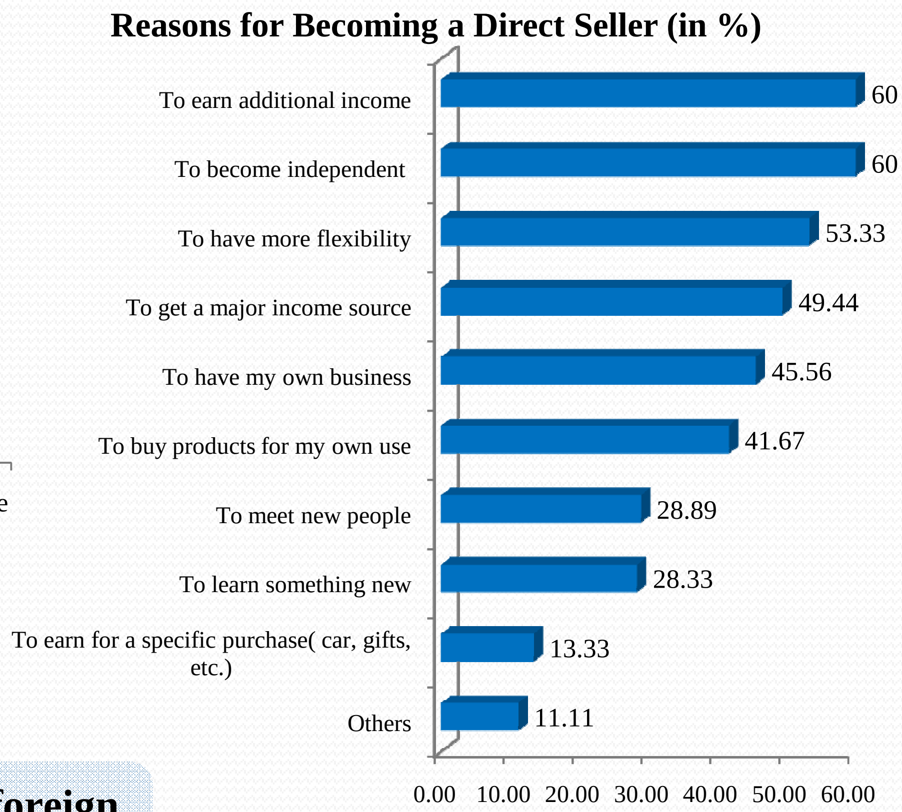
- **Tax contributions**
- **Reduction in intermediaries in supply chain**
- **Training and skill development**
- **Sourcing from SMEs leading to technology percolation**

Survey Findings: Direct Sellers

- Majority are graduates, fall in the monthly income category of ₹40,000-70,000, fall in age group of 35-49 years, followed by 18-34 years
- Over 68% have small families - convenience of working from home
- Around 64% take it up as their sole activity, 26% have additional job
- Network expansion; essential part of their operations – almost 80% work in close contact with their downlines
- The 180 direct sellers surveyed had 1.28 lakhs downlines, out of which over 10,000 joined in 2007-08
- Margins are around 25%

Survey Findings: About Direct Sellers

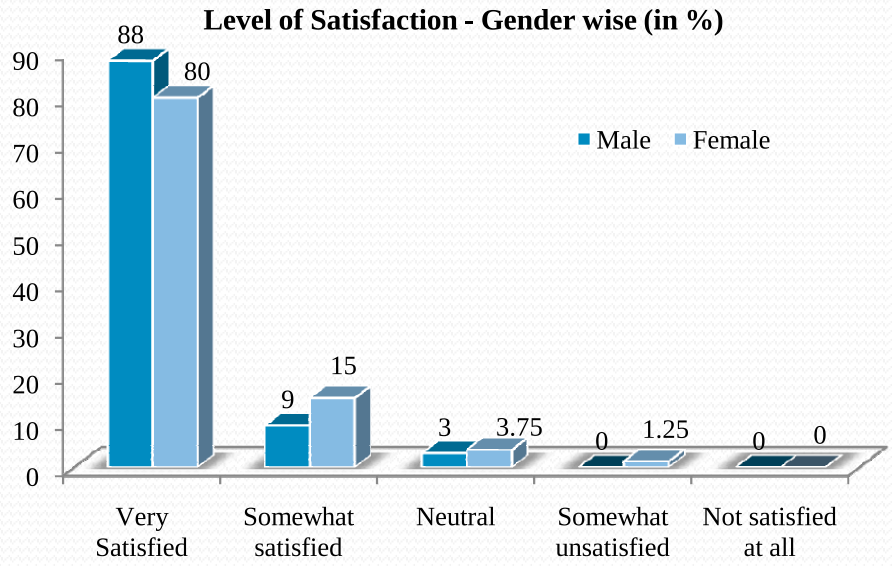


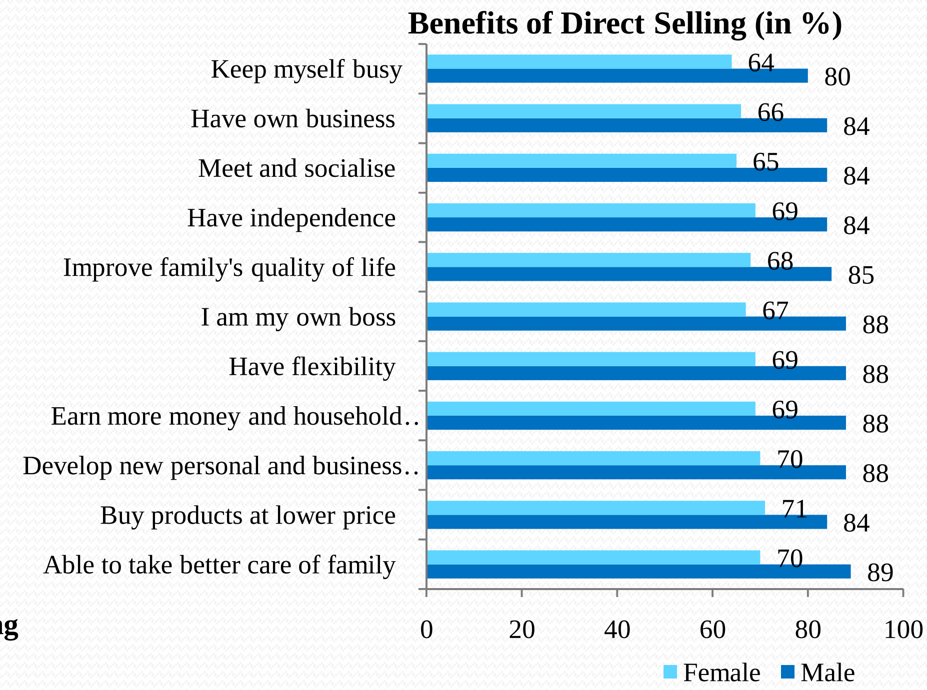


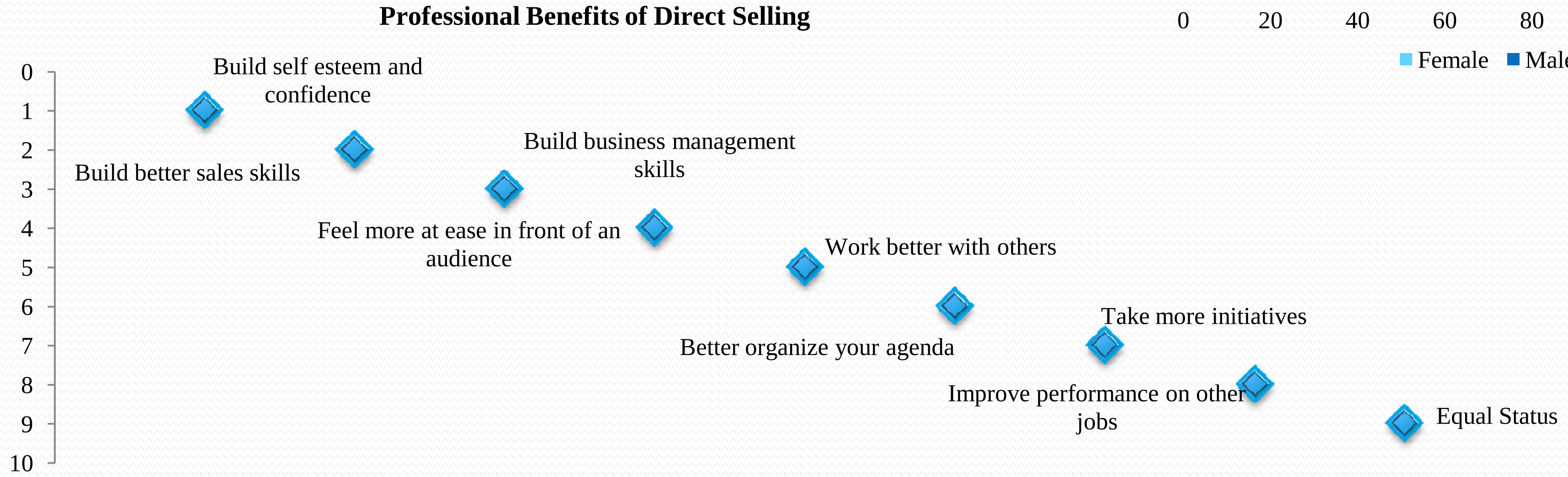
Incentives to direct sellers- receive commissions, foreign and domestic travel and awards and recognitions

No major start-up cost

Impact on Direct Sellers

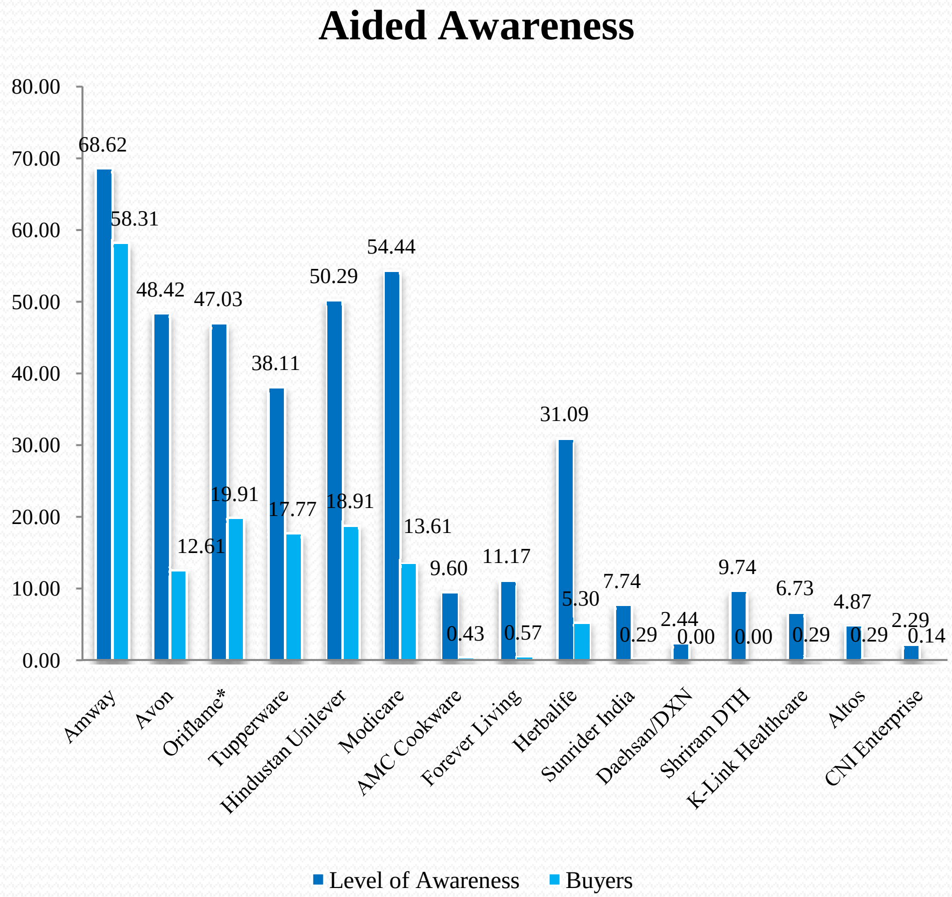


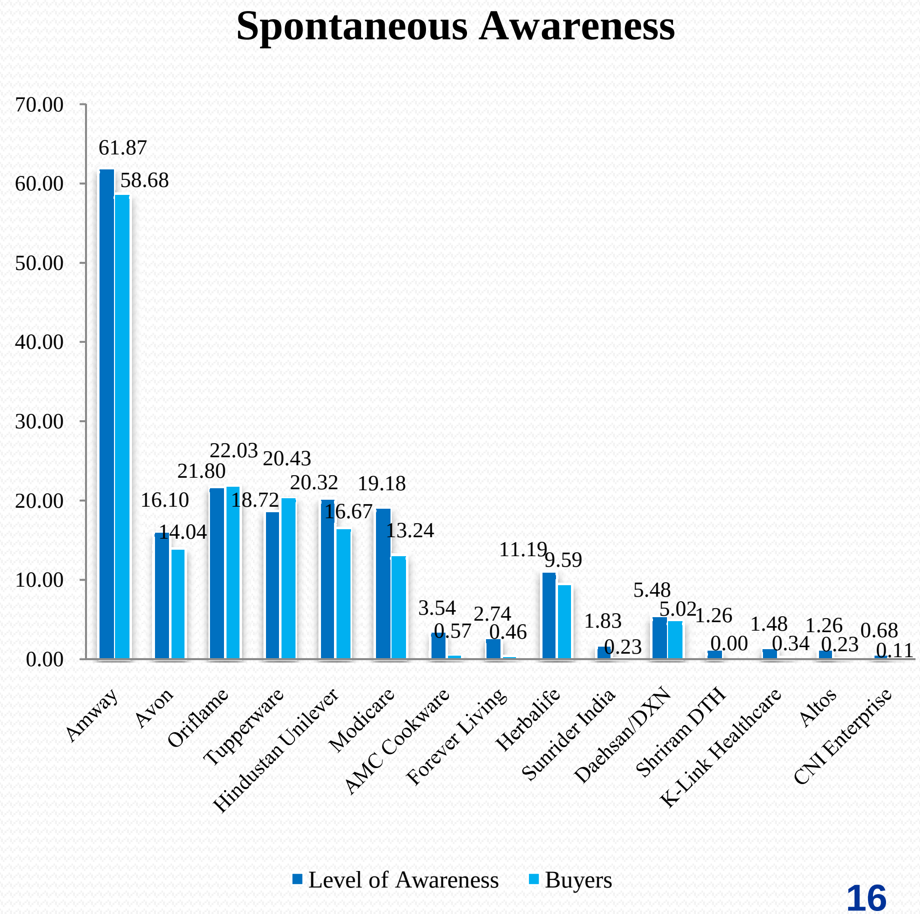




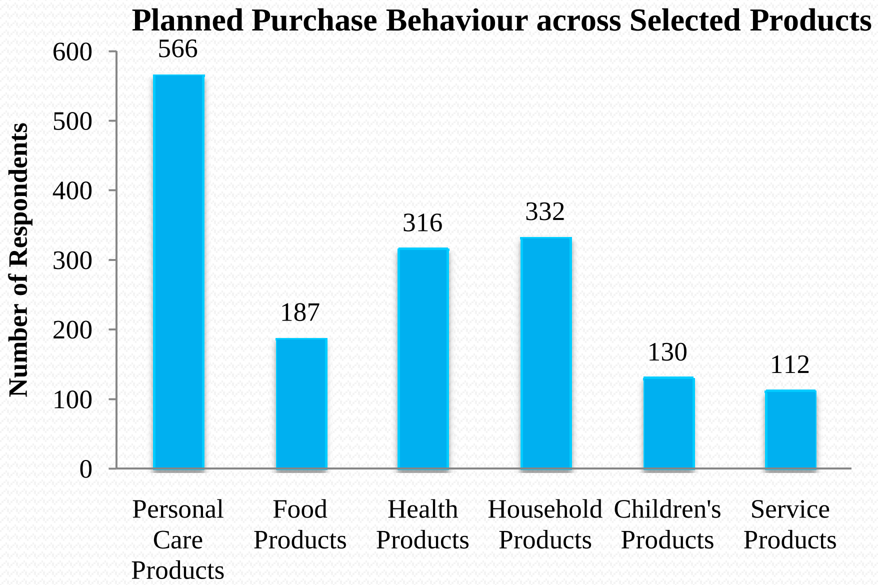
Survey Findings: Consumers

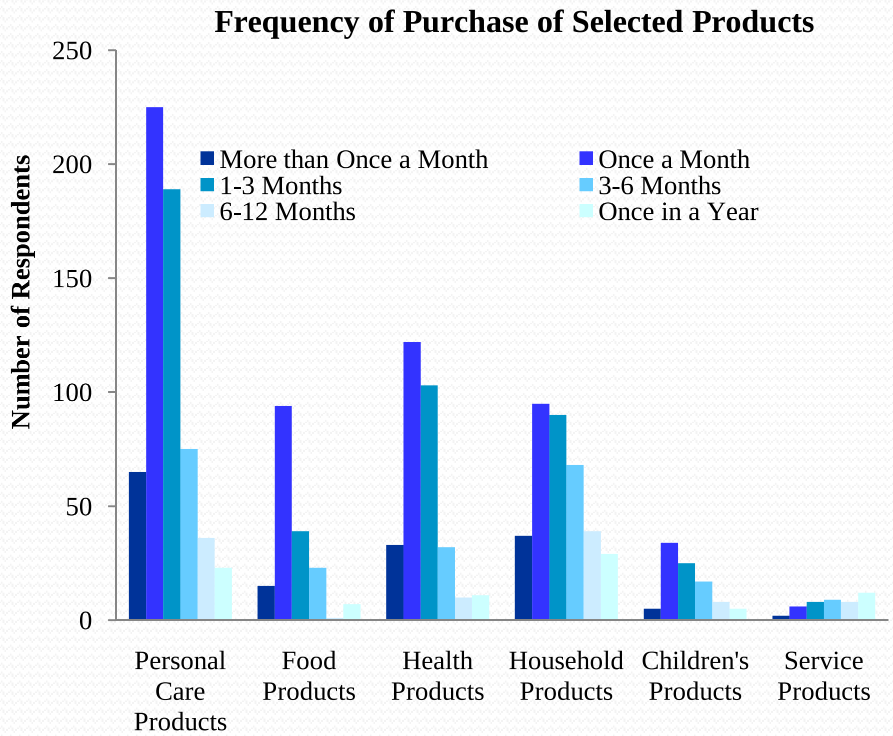
- Out of 2079 randomly selected consumers, 698 used direct selling. Total consumers – 698+178 (in-depth interviews) = 876, from SEC A and B

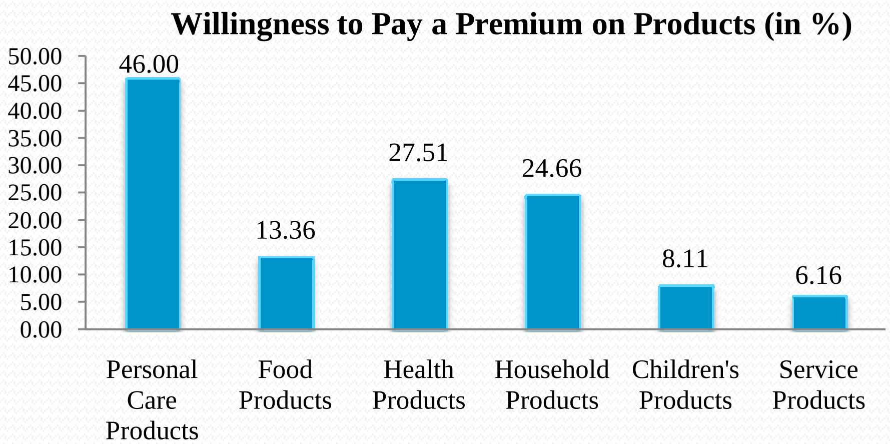




Survey Findings: Consumers Contd.

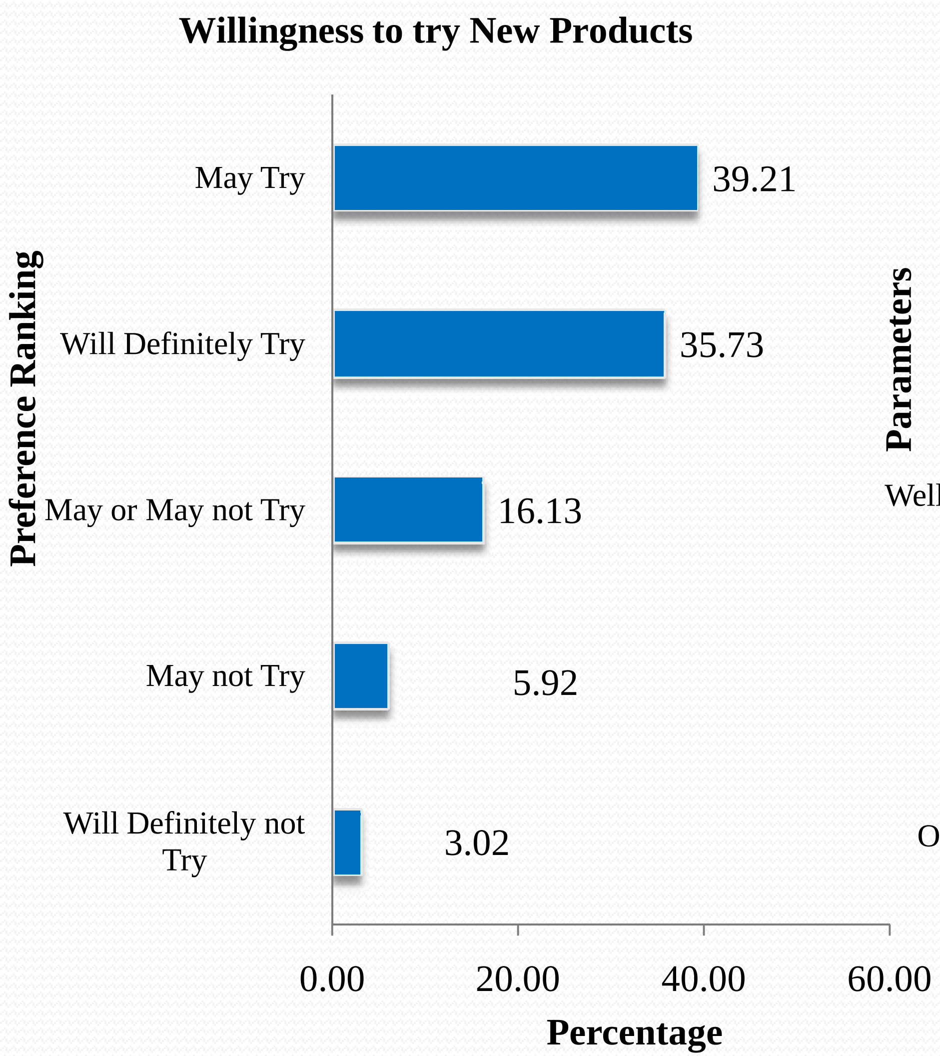






- Expenditure on purchase through direct selling is less than 10% of total expenditure
- 53% of total expenditure is for household consumption, rest for personal consumption

Survey Findings: Consumers Contd.



Consumers' Survey Findings: Benefits of Direct Selling

- Convenient, time saving
- Discounts and offers
- Personalized service
- Good quality products
- Can take joint family purchase decisions
- Increased brand awareness

Concerns and Policy Recommendations

A Recap

- Direct Selling is one of the fastest growing sectors - companies are exploring smaller cities and rural markets, diversifying products
- Is labour-intensive, number of direct sellers doubled between 2001-02 and 2008-09
- Has positive socio-economic impact
- Benefitted allied industries
- Has benefitted women – but the impact is different from that of the rest of the world. It has helped them to have financial independence but Indian women have not yet achieved equal status with men
- Women empowerment
- Provided a safety net during global slowdown

Concerns

- Lack of a proper definition of the sector – wholesale, retail or separate line of distribution
- Lack of clarity of the concept of direct selling and regulations pertaining to this sector - Limited knowledge among government and consumers
- Misinterpretation of existing regulations by different governing authorities
- How to identify a genuine direct seller?
- How to protect the interest of consumers from fraudulent multi-level marketing companies?

Others: Direct Selling Companies

- Setting up of manufacturing unit is not easy, difficult to operate on a hub and spoke model
- India is not a homogenous market
- Competition from store formats/retailers
- High import duties, multiple taxes, lack of single-window clearance procedures, etc.
- Quality of direct sellers – lack of skilled manpower, internet penetration, low brand awareness, multiple languages, etc.

Concerns Contd.

Direct Sellers

- Authentication of direct sellers
- Lack of product marketing and advertising
- Lack of adequate training for direct sellers
- Uncertainty about the sector
- Grey market problems – retailers are also direct sellers

Consumers

- Products are costly and may not be available in varied sizes
- Delivery takes long time
- Tester/sample may not be available
- Only few products are available and variety is also limited
- Direct sellers can be persuasive
- Lack of knowledge about this business model
- Inability to locate a genuine direct seller

What Companies should do?

- Offer more variety
- Better product marketing
- Streamline supply chain
- Make basic training mandatory
- Product customization
- Knowledge sharing
- Follow certain procedures for appointment of direct sellers such as the person should have PAN card, no criminal record, etc.

What Government Should do?

- Clear definition of retail and wholesale
- Transparent FDI policy and entry route
- There will be benefits if:
  - 100% FDI in single brand retail
  - Partial FDI in multi-brand retail
- Regulation is needed – delink regulation from FDI policy
- There should not be a discriminatory regulation
- Formulate a governing legislation – centre can have a model legislation
- The legislation should lay down mandatory guidelines for identification of genuine companies

What Government Should do? Contd.

- Streamline multiple legislation, regulation should focus on development of pan-India supply chain/sourcing network
- Modify Consumer Protection Act, 1986 and the Consumer Protection (Amendment) Act, 2002 : guidelines for consumer protection
- Need for an “Industry Status”?
- Regulator *versus* Nodal Agency

Any policy decision should take into consideration the impact on employment in a country where unemployment rates are high

Thank You!