PokerStrategy.com
The Professional Poker School

Underlying flaws of the affiliate rakeback model

1. Introduction

In the classical sense, affiliate marketing is a form of online marketing in which an affiliate sources traffic and customers to a partner site and is compensated for it in terms of CPA or revenue share deals. In the context of the poker industry, poker rooms gain a variety of advantages by employing affiliate marketing. They are able to cheaply market to many different markets, can outsource areas such as real money player conversion and gain access to large communities of poker interested individuals.
The mainstay of poker affiliates therefore concentrates on fulfilling one of a number of roles in which they supplement the poker rooms and round off the overall playing environment for casual or high volume poker players:

- Marketing / SEO
- News / Information
- Education
- Entertainment
- Communication platforms

This added value is most often provided in areas in which poker rooms either lack the required resources or sufficient know-how. Yet an ever increasing part of the affiliate industry has begun occupying a niche in which they no longer just supplement the poker rooms – but have become their indirect competitors. They are the so called ‘rakeback’ affiliates.

The effects of this competition was recently put in the spotlight when Full Tilt poker decided to reduce the margin of its rakeback affiliates to an effective 3%, which spurred heated discussion in the affiliate industry.

This article will investigate the background behind this step, the underlying problems of the affiliate rakeback model and why the affiliate and poker industries need to adapt in order to meet the upcoming challenges. To start off we will look at the most predominant affiliate business models that exist in today’s industry.

Disclaimer
This document deals with flaws in “affiliate based rakeback” models, which refers to the constellation in which players sign’s up via an affiliate and in turn receive part of the affiliate’s commission – while they would not have received anything, or less, had they signed up without an affiliate.
These flaws do not apply to centralized rakeback or loyalty systems in which the sites gives rakeback (either flat or via some type of VIP program) to players regardless of whether they sign up through an affiliate or not.
It is therefore not criticism towards the general concept of rewarding player loyalty by giving back part of their rake. It critiques the affiliate based model through which this is currently being done at many poker rooms.

2. Two different Business Models

Each affiliate has a clear goal: maximise revenues generated through revenue share and CPA deals. The big difference between affiliates therefore doesn’t lie in the basic revenue model, but in the characteristics that determine the fashion in which they motivate their players to produce rake at their partner sites. Depending on the nature of their business models, one can classify affiliates as fitting into one of two categories.

2.1 Contributing affiliates

As their name suggests, these are affiliates that contribute to the growth of the industry. They target a broad audience and focus on bringing new players to poker. They use their own core capabilities to attract new players and convert people interested in poker into real money players. Most provide players with some type of value added unique selling proposition that goes beyond simple monetary incentives. Such offers include news or educational content, entertainment, or the provision of functionality as a communication platform.
Typical examples of contributing affiliates are poker news providers, poker schools, poker communities, as well as entertainment and infotainment portals (e.g. PokerNews.com, PokerListings.com, PokerStrategy.com, PokerTube.com, Donkr.com).
Although many of these affiliates forcedly also compete in the area of bonuses & monetary incentives, they have separate business models that allow them to source traffic for their own sites.

2.2 Cannibalistic affiliates

Instead of focusing on new traffic, these types of affiliates concentrate mainly on cannibalizing existing traffic by sending players from room A to room B and vice versa. Their business model generally revolves around being able to offer better monetary incentives than other affiliates or than the poker room itself.

The mainstay of cannibalistic affiliates doesn’t actively target non-poker players or try to convert people into poker players but focuses on people who are already playing poker at a leisurely to frequent basis. By offering them better cash incentives than they currently receive, they try to attract players who are currently playing through other affiliates or at other poker rooms. The result is that most cannibalistic affiliates don’t actually generate unique or new traffic (something that they are often not even aware of themselves). Most of their traffic consists of knowledgeable players that use affiliates to boost their effective return from poker rooms. The most common form of cannibalistic affiliates are pure rakeback affiliates.

Why affiliates employing this type of business model need to adapt, in order to offer a long-term benefit for the industry, is further explained in later parts of the article.

3. The Rise and Decline of Cannibalistic Models

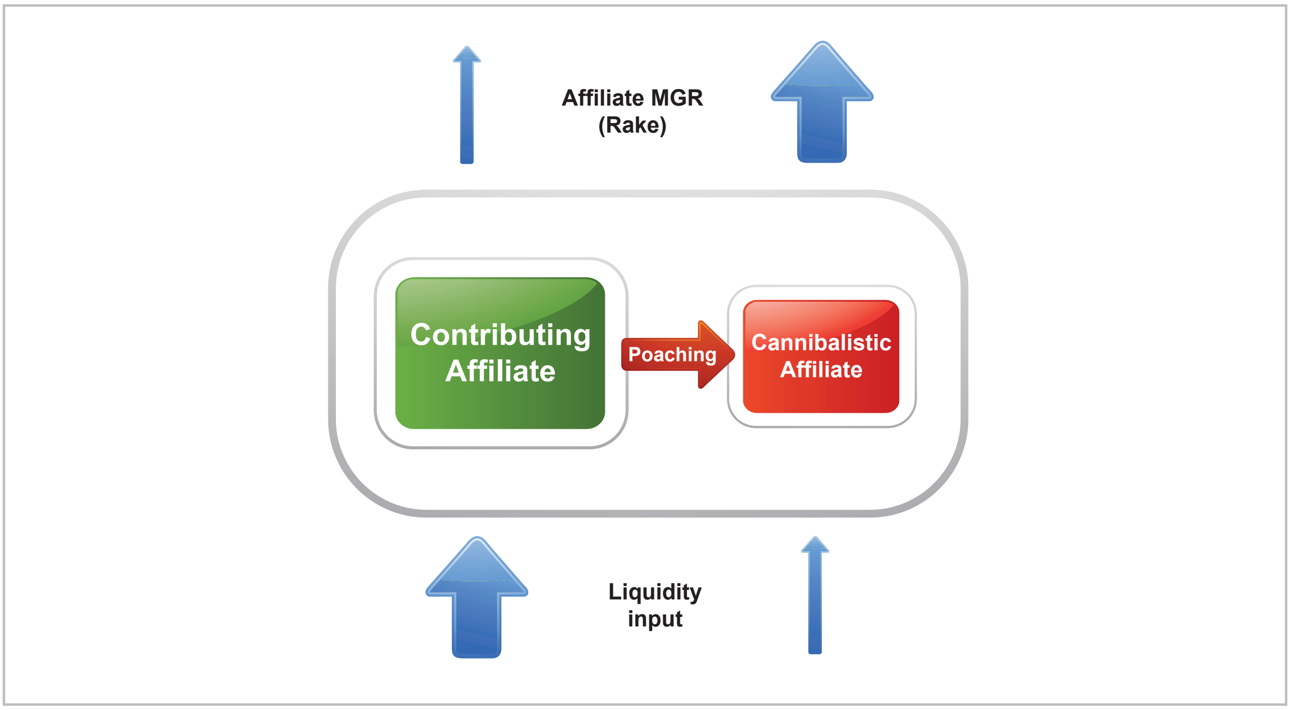
A common question asked by people that disagree with the evaluation that rakeback is bad for the industry and that cannibalistic affiliates don't actually actively contribute to its growth, is; "Why did the rakeback industry then manage to grow to the size that it has"?

There are several factors that allowed the rakeback industry to flourish like it did and in order to fully answer this question we will start off by going back to the times when rakeback started, in order to address an issue that is directly related to it: the topic of player valuation.

3.1 The evolution of player valuation

3.1.1 Network Ecology: From when MGR was king and how networks evolved

For a long time the value of a player has been calculated by looking at the amount of rake he produces in a given timeframe; the so called monthly gross rake (MGR). If a player produced a lot of rake he was considered equally valuable to that amount and by relation, if an affiliate or skin was providing a lot of MGR, he was also valued equally valuable. This led to a lot of skins and affiliates going for the most efficient effort to benefit ratio, by putting their focus on attracting few yet high volume players via monetary incentives, in order to attain high MGR figures.



The Network Dilema: Liquidity Input to Rake Output disparity

On a network level this caused a plethora of problems, as the result was the rise of many small skins with extremely attractive VIP programs which attracted the network's high MGR sharks while not having any recreational players. These sharks then fed on the fish pool brought in by the large sportsbooks and casinos, who themselves lost their high volume players to the small skins. The result was that the small skins extremely high MGR would drain all of the profit from the contributing skins that brought in all the liquidity with expensive marketing or cross selling. Although their MGR numbers looked good on paper, they were only able to produce such results, since other skins were bringing in the fish that their sharks fed on. They were functioning as pure parasites.

In recent times many networks started to realize their folly and began weeding out such skins by introducing balancing mechanism and penalties for skins that were only concentrating on high volume winning players. In some cases these skins were also simply kicked from the network. The effect of these changes could be observed in the recent updates on the iPoker network and the policy changes it introduced at the start of this year. The iPoker network was not alone though, as other large networks such as Ongame and Boss Media have also been upgrading their valuation models or imposing penalties on non-contributing skins. The most famous example of a network that didn't adapt was the now defunct Cryptologic network, which lost all of its contributing skins to cannibalization and ultimately collapsed without the influx of fresh liquidity.

3.1.2 Affiliate Ecology: Evolution in progress

During the same time, similar events were happening on an affiliate level. While contributing affiliates were doing marketing in order to bring in the fish, small specialist affiliates started targeting high volume players. In order to convince high volume players to play tracked through them, instead of through the site directly, they offered a part of their commission back to the player: the birth of "rakeback".

From a player perspective, receiving a certain amount of rake back is better than getting none back, so the concept proved successful in signing many high volume players. Soon rakeback affiliates were providing poker rooms with high MGR trackers and everything seemed beautiful, as a lot of sites jumped onto the affiliate rakeback train. Yet as time went on cracks started appearing in the affiliate rakeback model, as the poker rooms realized everything was not as great as it seemed on paper.

There are several key flaws in the structure of affiliate rakeback which became apparent through the course of time:

1. Players are forced to sign-ups via affiliates in order to receive full benefits
2. A player's value cannot be expressed through MGR alone
3. Inter-affiliate competition leads to dwindling margins for everyone
4. Poaching makes it unprofitable for contributing affiliates to market the rooms

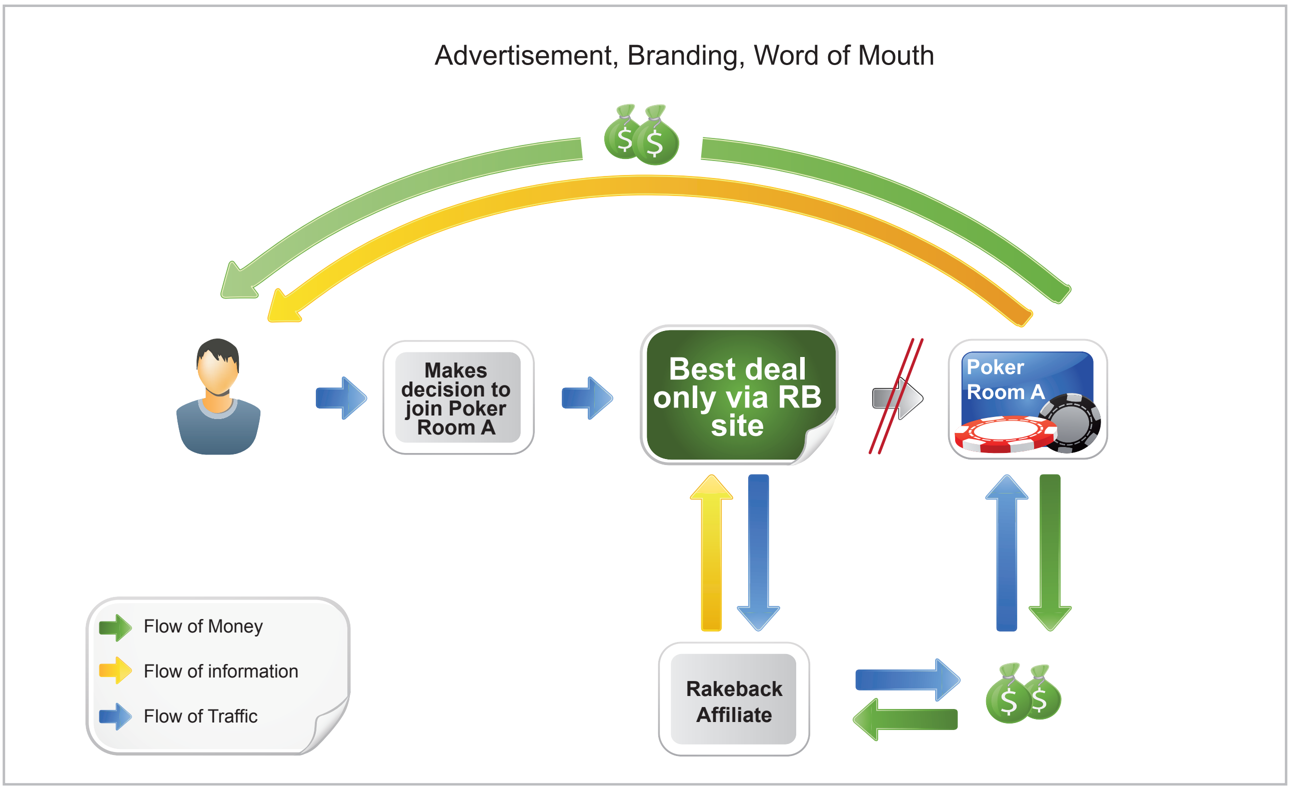
These will be discussed in detail in the next section.

4. The downsides of Cannibalistic Models

4.1 Traffic that rooms pay for once too often

The first main fault in the affiliate rakeback model is probably also its biggest: a poker room that has its own marketing campaigns and a strong brand name, but relies on affiliate rakeback as its VIP system (instead of centralizing its incentives system), ends up paying for its VIP players several times.

It pays the first time when it invests capital into creating a strong brand that gets recommended by word of mouth or in forums (cost for creating good software, providing tables full of fish, having a good customer support, famous pros, etc.). It then pays again when it advertises via print, television or internet. Finally, it pays for the players once more when it **forces** potential VIP players who were attracted to them through their initial marketing efforts, **to sign up via a rakeback affiliate** (that has ironically done very little to bring the players to the room).



The Case of player XYZ

This can be illustrated with an example: Poker player XYZ is an active poker player currently playing at Poker Room A. He knows what rakeback is and is active on a poker forum. He knows Poker Room B, since it has a strong brand name and has seen their television and magazine advertisements. Additionally, he knows from word of mouth that the room has great software. He decides to create an account. He checks on the internet and quickly discovers from various affiliates that he won't get rakeback or VIP bonuses if he signs up directly and that he needs to sign up via a special affiliate to receive rakeback. He therefore searches for a rakeback affiliate that offers the best deal and signs up through it.

He did **not** however sign up at Poker Room A **because** of the extra monetary incentive offered by the Rakeback Affiliate. Quite the contrary; he signed up at the rakeback affiliate because he wanted to play at Poker Room A! (This is in stark contrast to the claims of many rakeback affiliates that are now complaining about Full Tilt's actions – since according to them it was 'their' traffic that made the site as big as it is today).

In the above scenario, the poker room is essentially acting as the affiliate and sending players that it attracts through its own branding and marketing, to rakeback affiliates that then take care of processing VIP & loyalty payments. On top of this it is paying the affiliate the same kind of margins that it is giving to affiliates that actually do expensive fish marketing.

The entire situation is counter-intuitive on several levels. If a poker room invests money into building a strong brand, good software and further invests into print or media advertisement, why would it **force** high volume players to sign up through affiliates, when it could simply centralize such a powerful tool as its VIP system and sign these players directly? Why would it also pay such high premiums for a service that is as simple as payment processing, when it is actually the room, or other affiliates that footed the bill for branding, marketing or real money conversion?

4.2 Player Value and Unique traffic

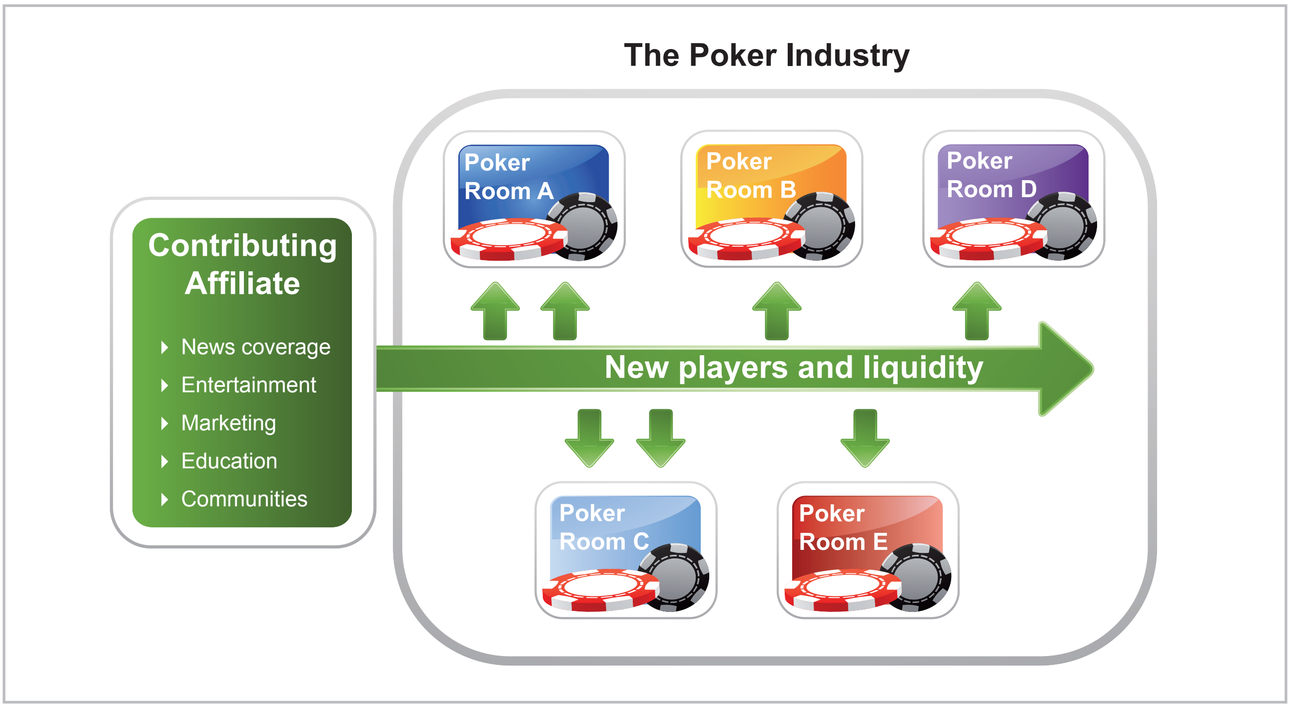
Another main problem that cannibalistic affiliates face is the true value of the traffic that they are sending. We established above that rakeback affiliates generally target high MGR traffic and winning players. Yet as the following section will illustrate; it is the acquisition and retention of casual and losing players that is the most expensive, but also most important aspect of a maintain successful poker room. In order to stay competitive cannibalistic affiliates while have to come up with ways to diversify the kind of traffic that they are sending to poker rooms.

As most networks have already realized, "rake" and player value is more complex than simply looking at MGR numbers. Rake is the product of liquidity which has been put in motion by being played with. Liquidity is therefore the direct pre-requisite for rake, and without a continuous influx of fresh liquidity the liquidity pool would dry up and no new rake could be produced. Liquidity is generated by players who deposit more than they cash out, contrary to most high volume players, who generally cash out more than they deposit. The truth of the matter is that the bulk of high MGR players are paying their rake with the money they win off losing players. It is these losing players that are the true source of rake, while high volume players simply ensure that this liquidity is converted faster.

This is best illustrated with an example: If player A deposits $100 and plays 100 hands in which he produces $5 of rake and loses his entire deposit, he adds $100 into the room's liquidity pool which will later be turned into rake by other players. His true value is therefore much closer to $100 than it is to $5. So even though he rakes only a fifth of player B, who deposits $100, plays 500 hands and wins $100 while producing $25 of rake and then cashes out $200 – he is essentially more valuable to the overall ecosystem.

4.2.1 Unique vs. Cannibalized Traffic

With this in mind let us look at the two affiliate types and the type of traffic and thus contribution they provide to the poker industry.



Function of Contributing Affiliates in the Poker Industry

As can be seen from the above illustration, contributing affiliates use marketing to bring new players to the market. These players are mainly the fish and the beginners that are the livelihood of the industry. They are also the player base which is most expensive to market to. In terms of practical examples:

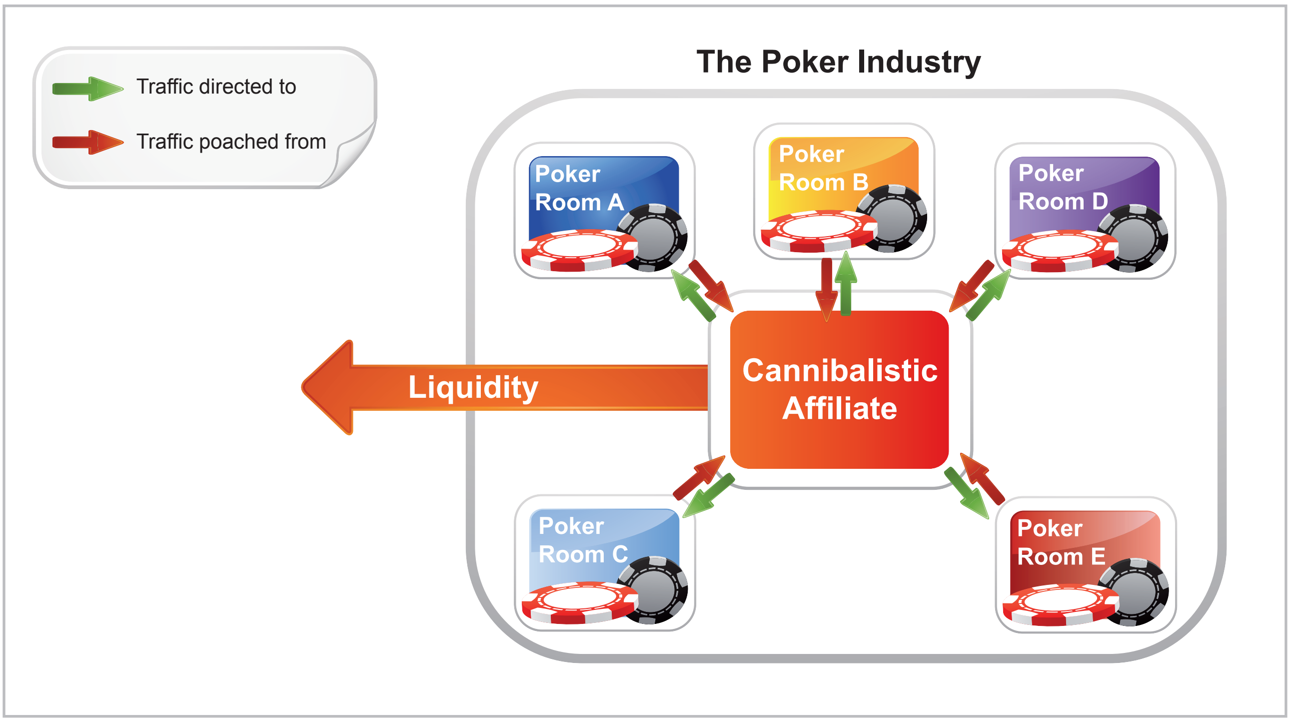
1. **PokerNews.com:** provides live and video coverage of events. They invest in content, manpower, translating and serve a generic function in the poker industry. By being linked and sought after, they generate traffic and successfully convert their visitors to real money poker players. They target the casual market and as such many casual and play money poker players.

2. **PokerListings.com** is an SEO company which allows poker rooms to purchase publicity on a heavily trafficked site. Their main skill is to acquire top ranks for high-volume keywords such as 'online poker' or 'poker' in many of the world's leading markets. They do this cleanly by building their link strength, but also by delivering services and content that is of real interest to their visitors. These include live updates, blogs, strategy, videos and statistics

3. **PokerStrategy.com** is the biggest poker community world-wide and offers a comprehensive education and communication platform to its users. It also offers news and software, as well as entertainment, and targets people that are completely new to (real money / online poker).

4. **PokerTube.com** is a video hosting site which focuses on poker related material. They popularize poker by allowing users to watch interesting shows and provide a communication platform for users wishing to upload their own videos.

These companies have a positive influence on the poker industry as a whole since they invest a lot of resources into the acquisition of new liquidity.



Function of Cannibalistic Affiliates in the Poker Industry

The above illustration depicts the current approach of most cannibalistic affiliates. Instead of generating new traffic their main focus is on converting existing traffic to their own trackers. Yet the poaching of active poker players from room to room via offering better monetary deals, doesn't create traffic, it simply cannibalizes it. Since these affiliates target mainly high volume and experienced poker players their traffic usually consists of:

1. A high density of players that have a high MGR
2. Players that drain liquidity from the system since they are winning players

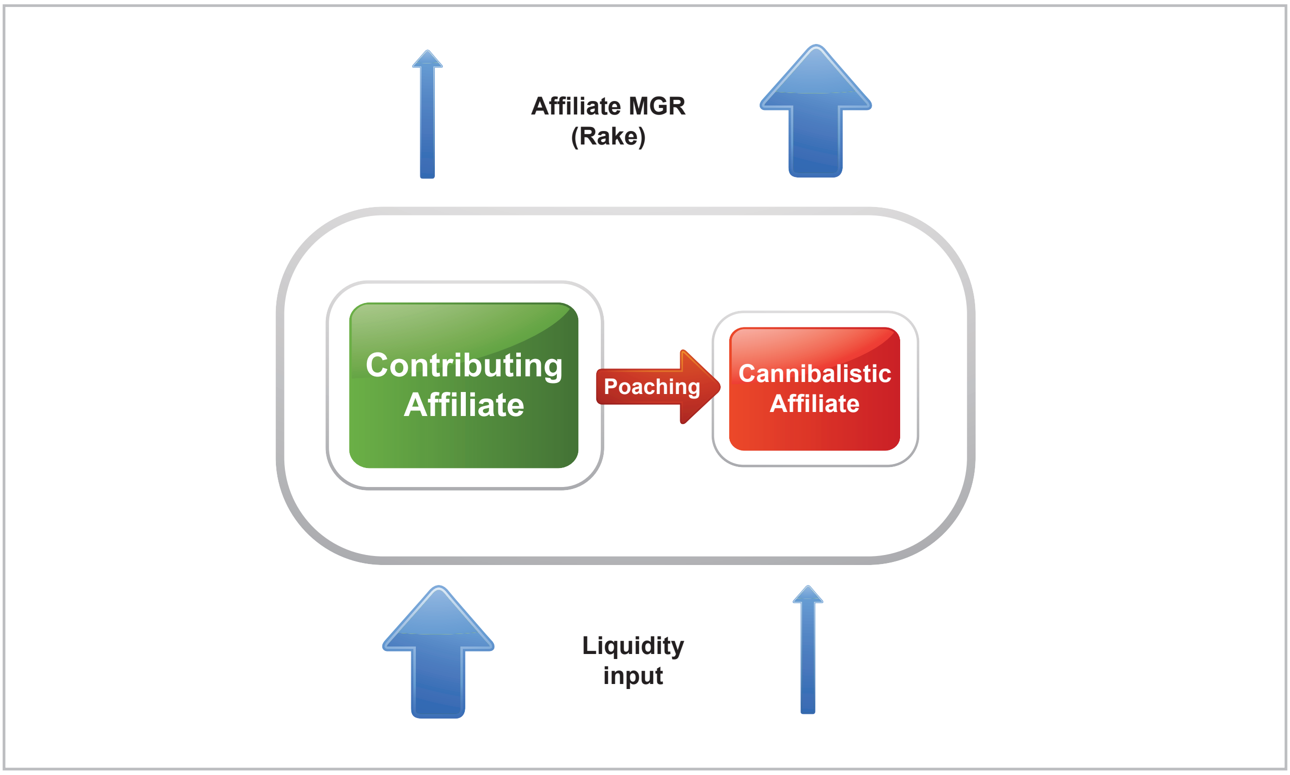
Although this cannibalistic traffic initially looks good on paper; it not only drains liquidity and decreases the profit margins but is also traffic that doesn't actually require expensive marketing campaigns to attract to the room. Winning players are naturally attracted by good incentive systems and liquidity. **If a poker room has its own incentive system it will successfully attract such players even without rakeback affiliates**. If on the other hand it allows affiliates to offer monetary rewards that are superior to those offered at the room itself, effectively outsourcing one of its key tools for player retention, **it forces players to sign up through affiliates**.

Affiliates that currently operate in a purely cannibalistic fashion need to realize that high margins for limited value traffic cannot continue forever. Just as parasitic skins are either adapting or disappearing from major networks, cannibalistic affiliates will need to adapt in order to continue being viable, well paid, partners for poker rooms.

4.3 Erosion of Margins through Inter-Affiliate Competition

The next large problem caused by cannibalistic affiliate price wars is an overall erosion of margins. Affiliates that belong to category 1, so contributing affiliates, generally don't compete with each other at all, or when they do, only compete within the boundaries of their own offers; e.g. two communities competing in terms of size, two educational sites competing in quality content, or two news sites competing in the quality of their news pieces.

In contrast, the second category lives mostly off players who search for the best deals and are therefore in a constant price war over the best rakeback, rake races and other promotional offers.



Distribution of Marketing Costs vs. MGR in a Poaching Environment

High volume players are very knowledgeable and well connected. If a poker room allows its own affiliates to compete against each other through better and better monetary incentives (rakeback, races and special offers), we have seen that players will usually sign-up through the affiliate with the “best deal”. This immediately gives rise to competition between rakeback affiliates: they will want to offer better and better deals to their players in order to compete for traffic.

In some cases, this will even lure a poker room’s best (and already existing) customers to illegally try and re-track themselves to the rakeback affiliate with the best offer. Some sites even suggest the registration of a second account under a friend’s of family member’s name, to players who are not tracked in order to bypass room regulations. This aggressive poaching and illegal re-tracking creates an environment in which the margins and profits of poker rooms and contributing affiliates alike are continuously eroded through the actions of cannibalistic affiliates, which usually, have low marketing and fix costs and can afford to settle for smaller margins.

Yet contributing affiliates and poker rooms, who both undertake the majority of expensive fish marketing and real money conversion, are not the only victims of margin erosion and poaching. Cannibalistic affiliates also suffer from poaching (especially affiliates who turn to offering illegal rakeback often successfully steal members from established ‘legal rakeback’ affiliates) and often end up having to settle for margins which are much lower than what they could be earning in a healthy industry.

At the end of the day the final victims are the players. As both types of affiliates send players to the room where they expect the highest return on investment, it means that if certain rooms allow cannibalistic affiliates to flourish, **they will become less and less attractive for contributing affiliates who will not be able to profitably market them**. In the long run these poker rooms will thus receive less new players and fish, making them less attractive for sharks and ironically also more unattractive for cannibalistic affiliates. As the influx of fish and liquidity decreases, the games get tighter and tougher, and ultimately unprofitable for winning players, who no longer have access to the fish, which they need in order to beat the rake.

A healthy industry, with focus on long-term growth and sustainability is in the interest of all parties; poker rooms, affiliates and players alike.

5. Solutions and Prevention

Some poker rooms have already taken a variety of steps to prevent or regulate the problem. The undoubtedly most well known and effective approach is employed by PokerStars:

1. Using a centralized monetary incentive scheme
2. Regulating “additional affiliate” promotions to avoid competition

By keeping its monetary incentives centralized, PokerStars retains control over one of the most powerful tools available for maintaining loyalty over its players. The money it saves from the increased amount of direct instead of affiliate traffic, allows it to make the VIP system highly competitive. Additionally it doesn't allow any of its affiliates to offer rake races or additional monetary incentives, and thus prevents the issue of players needing to sign up via affiliates in order to receive 'the best deal'.

From an affiliate standpoint a centralized monetary system minimizes inter-affiliate competition and many "rakeback affiliates" have been successfully advertising PokerStars VIP system as "rakeback" to its high volume clientele. For all rakeback affiliates with a genuine business model and of course all contributing affiliates it means:

- they can advertise the benefits of the room in a fashion that targets their players
- they can be sure of healthy margins in the long term
- they will know that once they refer a player, he is not going to get poached.

For the players it means that they can play on a healthy poker room that directly benefits from its marketing, has extremely high liquidity, and still receive high return on their rake.

5.2 What is being paid for?

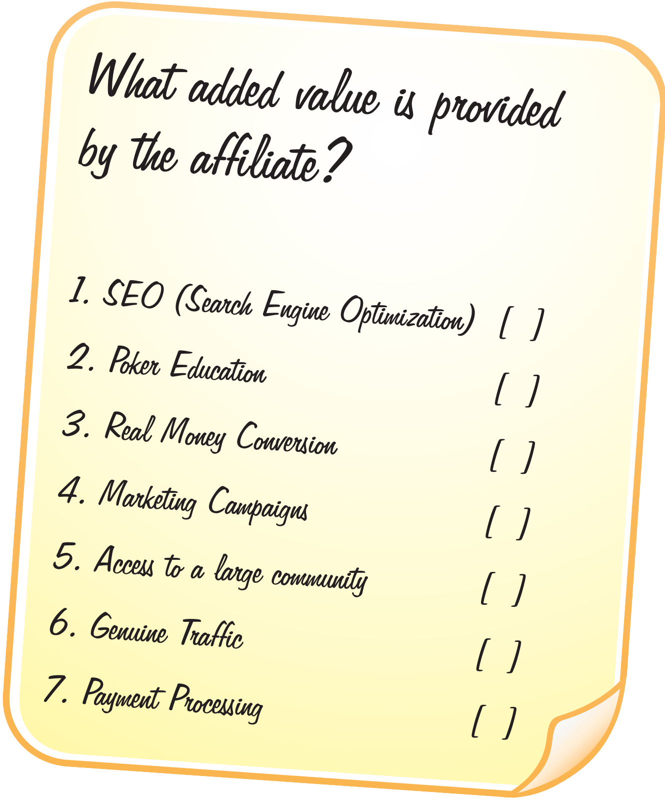
As Full Tilt Poker has shown, rooms are becoming aware of what they pay for. Not all traffic is equal and not all affiliates are currently contributing equally. While it is expensive and resource intensive to attract new real money players, it is somewhere between free and cheap to cannibalize existing traffic. From the viewpoint of the poker room there are even hidden costs in cannibalized traffic, since it is traffic that they generated through their own marketing efforts yet continue paying for through revenue share.

Once more poker rooms start evaluating the hidden costs of cannibalized traffic compared to genuine new traffic they can put price tags on the added value. Payment processors such as moneybookers generally have margins around 2%. So if payment processing is this is the only service provided by an affiliate, why should they continue to pay for more? Full Tilt has already taken action on this topic and it is only a matter of time until the overall margin erosion and heightened competition forces other rooms to take similar steps against cannibalistic models.

5.2.1 If you are a poker room

As a poker room you should be asking yourself; what added value am I paying for and how much is it worth to me? By assessing the true added value of all of your partners and activities you will be able to better use your resources to build a profitable and healthy playing environment for your players.

Below is a check-list of some of the usual value added methods provided by many affiliates. Combining these to assess the true value of traffic should enable you to tailor cost efficient models for your affiliate programs.



5.2.2 If you are an affiliate

Just as poker rooms are currently re-evaluating the value of players and affiliates, affiliates should be aware of what kind of added value they are actually providing and prepare for the times ahead. The poker boom resulted in tremendous growth, huge margins and plenty of new players. With the market beginning to stabilize and competition growing, especially the larger poker rooms are tightening up their expenditures and becoming more careful with what they pay for. For affiliates this means that they need to adjust to the changes in the market and take appropriate action.

If the ability to provide rakeback and better monetary incentives was suddenly taken from you, how would you provide value to your players? If you don't have a good answer to this question it is probably a good time to think about diversifying the way you operate.

6. Conclusion

In this document, we have shown that not all affiliates actually contribute in the same way. While many do in fact source genuine traffic to poker rooms, some affiliates simply take advantage of the current state of the industry and live of cannibalizing existing traffic. Since these affiliates rely on offering a superior incentive system compared to the poker room or other affiliates, they are constantly driving down the overall margins of the industry in their ever constant price war against other cannibalistic affiliates.

With the market maturing, the competition hardening and the margins steadily declining this cannibalistic model is becoming less and less sustainable. Just as poker rooms needed to re-evaluate their player valuation models, cannibalistic affiliates will need to re-evaluate their business models in order to stay attractive to poker rooms.

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