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LOGISTICS

Three-Way Partnership Finds Greater Return in Surplus Merchandise

Drug store chain, logistics company and liquidity firm work together to dispose of products from returns, closeouts and overstocks

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Surplus products from returns, closeouts and overstocks not only represent losses in themselves, but also clog up the distribution system and consume valuable warehouse, shipping and personnel resources. Moreover, the three key parties in surplus transactions – sellers, buyers and shipping firms – are frequently not very efficient in making the connections needed in the disposal process.

Recently, however, a new concept has emerged, in which a liquidation and a logistics company have partnered with a major drug store retailer to develop a cooperative solution to a pressing problem that all too often has been addressed only as an afterthought.

The three companies are Liquidity Services, Con-Way Logistics and a major drug store chain that asked not to be identified. The retailer describes itself, however, as one of the three top national drug chains, with more than 3,000 stores and sales in excess of $10 billion a year.

In July of last year, the retailer approached Liquidity with its surplus problem. Seeing the scale of the situation, Liquidity contacted Con-Way, and the two companies developed a system during the fourth quarter of 2001. The retailer went from a test mode to mainstreaming the process through all eight of its distribution centers early this year.

Within two months, $1.5 million of the drug chain's surplus was sold, according to the vendor companies. The chain saw a 30 percent to 50 percent increase in revenues compared to earlier sales, as well as savings from hidden costs for warehousing, shipping and personnel.

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The success of this experiment "demonstrates that this solution is applicable to any type of retail chain that has large amounts of unwanted inventory," says Bill Angrick, chairman and chief executive officer of Washington, D.C.-based Liquidity Services.

Following are descriptions of the process being used, told from the perspective of the three participants.

Drug Retailer:
Maximizing Surplus Value

"We have a big engine, and tend to throw off a lot of discontinued merchandise that does not fit into our assortment," says a general manager of the drug store chain. "We needed a way to expand our overall penetration into the secondary market to sell our goods."

Significant problems were resulting from the need to store these goods, the manager explains. The products tended to be returned to the company warehouses, where they would often sit for months at a time before they could be sold, thus clogging up the space needed for the forward movement of goods to the stores.

"One way to think of it is that distribution is focused on serving the stores, and so is forward looking," says the retailer. "But getting rid of surplus is backward looking, so the two procedures tend to run into each other."

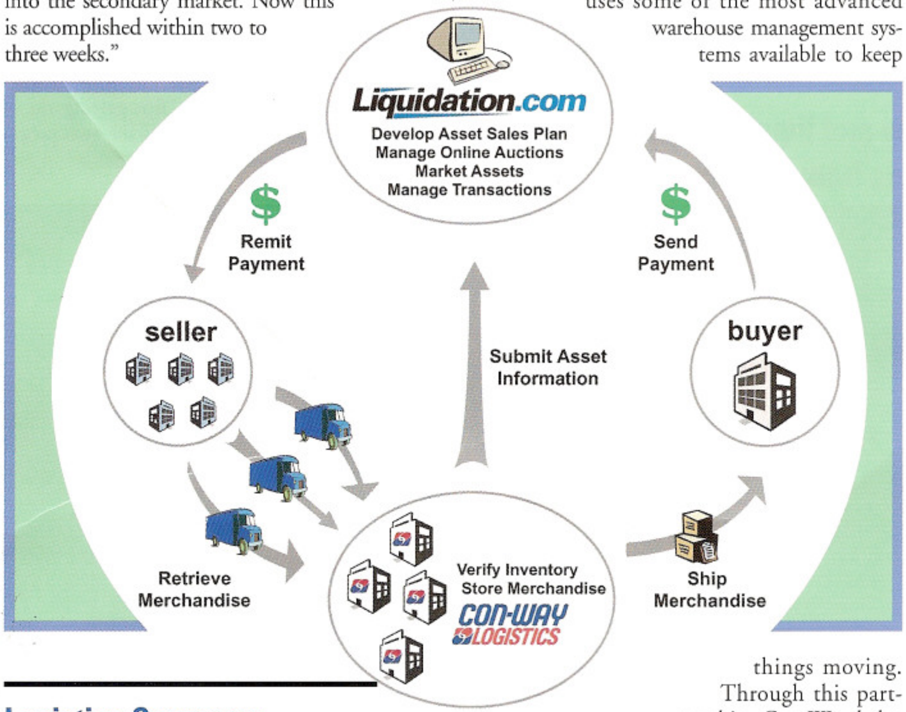
The chain recognized a weakness, the general manager continues, in that "we were not maximizing the value of these surplus goods for sale in the secondary market.

"We would be selling a lot of mixed goods, which would be less desirable, since buyers would want some of the products but not others."

One service that his partners now perform, he says, "is breaking the lots into targeted shipments to specific customer profiles." He adds that Con-Way, in providing its own trucking and warehousing, relieved the chain of that burden.

As a result of the experiment, the executive says, "We've had pretty good success with bringing in more customers for our displaced goods, and have seen significant increases over our traditional recovery rates. One good example is that in our highly consumable commodity categories, we've virtually doubled our recovery. On the fringe areas, we have not doubled our recovery, but still have done significantly better."

A big benefit, the general manager adds, "is turnaround time. Depending upon the size and condition of the inventory, and the marketplace, it could take up to six months to move goods into the secondary market. Now this is accomplished within two to three weeks."



Logistics Company: *Optimizing Recovery*

"One of the real drawbacks in the conventional model of surplus and liquidation is that once products enter the supply chain, to be returned, they have to go back through the supply chain to warehouses to be resorted and resold," says Michael Bare, vice president/general manager of Chicago-based Con-Way Logistics. "What we do is optimize recovery by entering the surplus supply chain at an earlier point."

While other logistics companies offer similar services, Bare says his company's system is unique because of its eight national warehouses and 30 flow-through centers spread throughout the country. "From time to time someone will open up a specific sortation center in a single geographical region next to a large retail chain," he says. "But, as the chain grows, that may not be the best solution. We have the infrastructure and flexibility to optimize the best results."

The single large sortation center tends to remain static, Bare continues. The dispersed solution used by Con-Way, by contrast, still allows large quantities to be handled, but with more possibilities. The partnership of Con-Way with Liquidity increases these possibilities, since clients of both companies have access to a wide range of supply-chain management services, such as warehousing, pick-up, delivery, inventory control and verification, labeling, fulfillment, bar coding, merchandising and consolidation.

Although there are many overlapping functions, Con-Way's role in the process is as the logistics arm, while Liquidity's primary task lies in the sale of the merchandise. Con-Way also uses some of the most advanced warehouse management systems available to keep things moving. Through this partnership, Con-Way helps customers maximize their logistics variables, while eliminating infrastructure and technology investment, and allows Liquidity to provide more effective merchandising, faster pick-up and fulfillment of orders.

Many people tend to look at the loss on a surplus product as only the difference between the cost and the surplus sales price, Bare notes. "But it's the other costs in disposing of the product that really cost you money. If you can draw away 8 percent to 10 percent of those costs, that's a significant savings."

The Con-Way system also provides clients with full Internet-based visibility. "The more transparent the product is, the more you remove risk," Bare says. "If the purchaser is empowered to know fully what the product is, he is more likely to pay more. And if the surplus provider is more knowledgeable as to what he is offering, he can demand a better price."

Taking this a step further, the transparency remains once the goods pass beyond the four walls of the warehouse. "The customer can track shipments through the web page," Bare says. "He knows at just what spot the goods are in the transaction, whether on the shipping floor or in the truck or half-way to the destination. He has all this information at his fingertips."

Bare adds that the system already in place can also extend services. Instead of just waiting to be called to pick up a surplus shipment, his company is becoming more pro-active in terms of looking at how long products have been sitting in a warehouse and how many turns they should have, thus suggesting an earlier liquidation of products that are not moving.

Liquidity Firm: *Consolidate and Reconsolidate*

"The market for obsoleted inventory in the United States is $150 billion," says Angrick. "We are a service company that has identified this market and devised ways to help retailers dispose of their surplus goods."

A retailer must devote its main energies to moving products forward through the supply chain, and so is generally not well equipped to move them back, Angrick says. "We provide a very focused full service solution. We arrange the shipments to the logistics centers, and use that warehouse space for our core, first of all to identify the inventory, which is critical, to collect relevant information, and to consolidate and reconsolidate.

"When selling pallets of mixed goods, it's very easy to sell goods the buyer doesn't want. We make sure this doesn't happen. And, by doing so, we can legitimately raise the price," he adds.

Asad Haroon, vice president of business development, explains that when the drug store chain first contacted Liquidity last year, "They had a lot of surplus, and only a limited group of buyers. They had goods sitting in their warehouses for months, up to a year. They wanted a better dollar recovery rate, a faster solution and a more cost-efficient way of managing this unwanted inventory."

The magnitude of this problem is a key reason why Liquidity sought out its partnership with Con-Way, so that it had a truly nationwide network to provide cost-effective solutions. "With our partnership with Con-Way, we now have a rapid fulfillment of orders, and can ship them to the buyers within 48 hours," Haroon says.

Liquidity has developed a buyer base of about 50,000 participants, through which goods are sold through on-line auctions, sealed bids and negotiated sales in a matter of seven days or less. Moreover, the goods are sold outside the normal retail channels, so the drug chain is not forced to compete against itself. **STORES**