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The Global Excess Inventory Market

An Aggregation of Research Reveals How Corporations & Internet Technology Have Created New Business Opportunities

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Report Summary

This report *The Global Excess Inventory Market* presents the latest research on the current state and future outlook of the asset recovery market - a market that has gone through radical transformation in a little over a decade. Conservative estimates for this market range from $60 billion to $80 billion. It is not just the size of the market that is investigated in this report, but the important role that asset recovery has carved out in the retail world.

Productivity growth, and the U.S.'s import-oriented economy, have created a new retail space that is highly price-competitive and consumer-centric. Retailers now handle greater volume merchandise with seemingly ever shortening product cycles and more competitive pricing. In turn, this has made hanging onto excess inventory that much more costly. The incredible growth in the consumer electronics industry over the past decade - especially in computers - and its downward price competition is the prime illustration of these trends. Therefore, this retail sector is the focus of this report. For computers alone, an estimated $1.3 billion of excess inventory is sold annually in the U.S. Non-computer consumer electronic asset recovery is at least $600 million annually.

The findings in *The Global Excess Inventory Market* report discuss the ongoing sources of excess inventory in today's retail environment.

- The inherent difficulty in predicting ups and downs of retail sales.
- A world of tighter margins – an increasingly competitive environment.
- Consumers are sharper, savvier, and more demanding.

Furthermore, the report looks in depth at how increased economic volatility is shaping the excess inventory market. Overall global economic problems reinforce factors affecting excess inventory and lead to lower average selling prices. Electronic component producers are cutting growth and showing smaller gains in producing chips and other components. But with prices falling faster, continued production will still lead to excess inventory.

- PC shipment growth estimates reveal that all signs point to a U.S. market that will remain extremely prone to excess inventory issues.
- Consumers will continue to benefit from lower ASPs, maintaining pressure on retail inventory.
- Consumer spending and retail sales are – and will remain - down, increasing pressure on retailers.
- Retail sales have dropped for 5 consecutive months.
- As last reported on December 12, 2008, holiday sales will be barely better than last year (although electronics remains popular).
- Tight credit margins are likely to lead to increased inventory pressure.

Needless to say, the ongoing financial crisis has presented, in stark terms, the challenges facing the retail sector. These trends, discussed in Chapter 2 of the report, though much greater in magnitude, reflect underlying inventory problems that many quality companies face today. With most indicators pointing to the U.S. economy heading into a deep recession, all of these factors will remain key to how the retail sector will fare throughout 2009. Whether government stimulus efforts boost demand or the market is in for a period of belt-tightening, finding solutions for excess inventory will be more important than ever for companies stockpiled with brand-new, quality, consumer-attractive products.

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The New Landscape

Until the late 1990s, the nature of the liquidation industry had changed very little. Distressed merchandise was handed off at a steep discount to be resold, generally in an odd lot store. Liquidation businesses have traditionally focused primarily on alleviating excess inventory that was taking up a distributor's warehouse space. Overstock has always been a necessary part of the inventory supply chain. Products go unsold, styles change, inventories get over-ordered when demand is dropping, or a store goes bankrupt. When it came to the wholesale and retail supply chain, however, the liquidation industry was primarily an afterthought, a necessary inconvenience affecting the bottom line, not an integral element in inventory planning. After all, planning to have overstock is a little bit like planning to fail.

In little over a decade, however, asset recovery has become a much more important industry. Upper end estimates now put the market as high as $80 billion. According to D.F Bumberg Associates Inc., a logistics and consulting research firm, revenues are expected to climb to more than $63.1 billion by year-end 2008, a 65% increase from the $38.5 billion recorded in 2004. The growth of the internet as a marketplace gets much of the credit for this sea change, and certainly the number of liquidation businesses currently online is impressive. However, focusing on the internet overlooks a fundamental issue – it's not just the method of finding buyers for distressed inventory that has changed, the economic landscape that liquidators now operate in has shifted. The new terrain certainly presents vastly greater opportunities, but in terms of providing inventory solutions it places much greater demands on liquidators.

The retail and wholesale worlds have witnessed changes of revolutionary proportions. The realization of the globalized economy, along with the advent of e-commerce, unleashed tremendous growth opportunities for trade, which may have delivered much greater consumer satisfaction, but fundamentally changed the retailers and distributors ability to manage inventory. This report provides an analysis of the changes in the past decade as these trends have moved the liquidation industry into a key position relative to modern commerce's ability to maintain profitability.

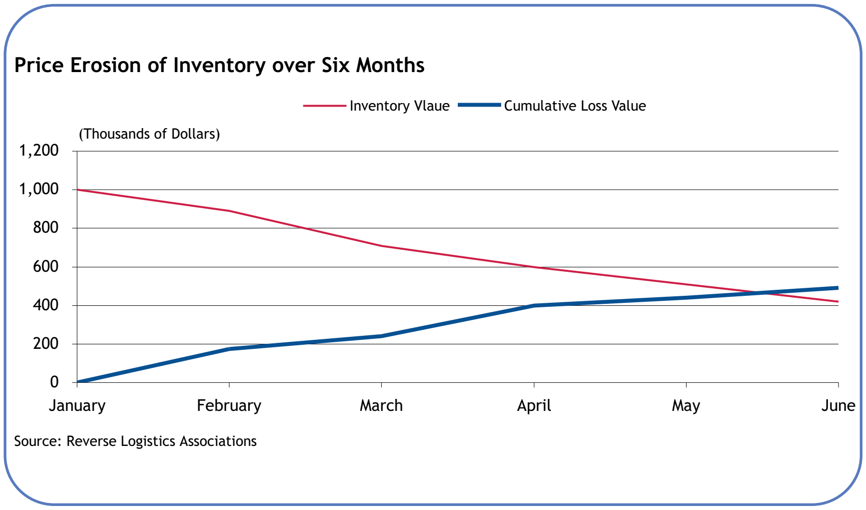
The Global Excess Inventory Market

When the dot-com industry crashed in 2001 and the U.S. economy slid into recession, the high-tech sector became a major catalyst for the liquidation industry. Ultimately, some 1,500 discount and department stores closed, presenting a considerable amount of merchandise for liquidation. Between 1999 and 2002, Bradlees Inc., Montgomery Ward &Co., and Kmart Corp. filed for bankruptcy. The shake-out in this sector plus the internet as a new sales channel gave the liquidation industry a sudden and powerful boost. Numerous e-businesses sprang up, ready to transform the asset recovery landscape. The comic strip Doonesbury even ran a series about a company called e-Vulture. However, like many aspects of e-commerce, the initial visions of revolutionary change didn't quite pan out and e-liquidation did not constitute a new business model. But the fact that the internet was well suited to the auction business model, which has long been a prominent model for asset liquidation, and the leftover dot-com inventories certainly invigorated the industry.

A 2000 survey by the National Association of Wholesalers, representing the largest wholesale distributors in the country, indicated that more than 80 percent of its members ranked disposal of excess inventory of "high importance". More than 70 percent were unsatisfied with their company's current means for disposal. More recent NAW research, information that is obtainable on their website, indicates that these concerns persist and this issue continues to be monitored by the association.

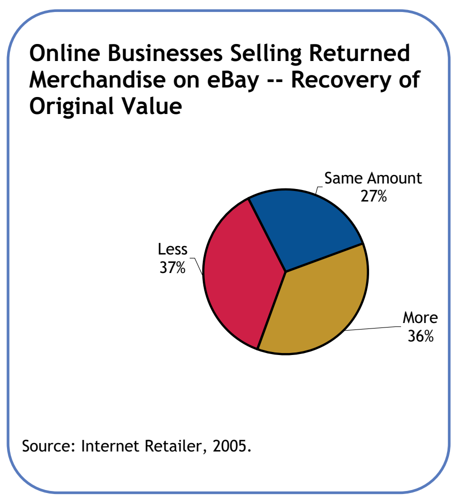
As product cycles accelerate, the shelf life of merchandise becomes much shorter. There is considerable incentive for retailers and wholesalers to move excess inventory quickly. Unsold merchandise faces considerable value erosion — the longer it sits in a warehouse, the less it is worth. The Reverse Logistics Association estimates value erosion can run as high 15% a month for high-turnover merchandise, such as consumer electronics. (See chart page 7)

Furthermore, as the value of the merchandise goes down, the expense of hanging on to it mounts – the costs include warehousing, standard revision, and tied-up capital. As the U.S. economy moves into troubled waters, the premium on quickly moving excess inventory is all that much greater.



Within a few years, however, it became clear that internet-based liquidation was showing its limits. This was most evident in eBay, which quickly attracted a great deal of excess inventory. For example, a survey of 286 online merchants by Internet Retailer (2005) found 39.5% turning to eBay to sell returns. Of this group, 20% managed to sell more than 50% of their returned goods, with a strong majority of 65% selling less than 10%. Their success at recouping costs also showed mixed results.

Further eBay experience points to limitations the auction model has as a retail platform. After all, most buying is not done through auctions. Callaway Golf Pre-Owned, a company that sells Callaway clubs that have been traded-in by golfers purchasing new clubs from Callaway, was doing well in 2003 selling used clubs on eBay. However, when it tripled its listings by integrating its inventory system with eBay's, with the latter's encouragement, the actual number of listings that found buyer's dropped to 50% from 90%. ReturnBuy, a liquidation company, attempted to use eBay as a major liquidator outlet and fairly quickly went out of business. eBay's auction model is structured around many small and medium sellers of an extremely broad range of goods. Too many identical items can flood the market for a given auction category and depress prices participants are willing to bid. The conclusion to be drawn is that simply putting excess inventory online does not constitute a solution.



The problem essentially was that the traditional ad hoc approach to solving inventory problems had simply been shifted to the internet. In fact, the entire retail landscape had undergone tectonic shifts. A number of overlapping factors have contributed to the changed relationship among manufacturing, inventory, and sales. These include:

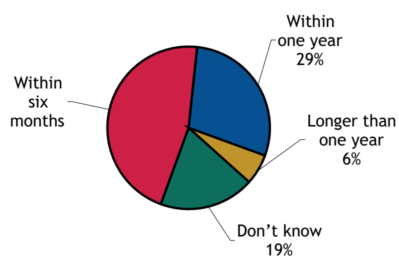
- China's arrival as the dominant exporter in the world. Along with the Asian Tigers, China's productivity provides massive volumes of lower priced goods that have increased competition for the consumer's dollars as well as accelerated product cycles.
- Logistics, especially container shipping, now moves vastly more products to more locations while demand cycles have accelerated, increasing the need for faster turnover.
- The growth of big box retail – epitomized by Wal-Mart – greatly increases price competition. At the same time, specialized chain stores like Best Buy, increase consumer awareness of more sophisticated products, such as consumer electronics.
- Retail channel growth adds further to retail competition. This includes the internet, catalog shopping, outlets, and various combinations thereof.
- Changing consumer expectations: greater competition among sellers naturally benefits consumers. They not only demand lower prices and greater convenience but the ability to return goods with no questions asked – policies that began with catalog merchants and e-commerce, but soon became standard.
- Economic volatility – take-overs and bankruptcies among large retail firms wreak even more havoc with stable inventory management. This will only increase as the U.S. economy moves through the current economic downturn.

These issues are all interrelated and are mutually influential. The bottom-line, however, is that the incredible productivity growth and the U.S.'s import-oriented starting in the early 1990s economy have created a retail space that is highly price competitive and consumer centric. The effect of these factors, discussed further in this document, was to put retailers in a bind – greater volume with shorter product cycles and lower prices – increasing the need to clear goods. This is especially true in the consumer electronics and computer sectors.

The growth of big box stores and discount chains needs to be kept in mind in understanding the volume and price factors that ultimately drive the liquidation market. It is most clearly seen in the computer and consumer electronics sectors. In the past, consumers shopping for these items used to go to smaller, more specialized tech boutiques, largely for the knowledgeable sales staff and for tech support. It's a much more tech-familiar population now, and price and variety are now the main drawing cards. To varying degrees this phenomenon has been repeated across numerous retail categories. Wal-Mart's ability to under price the competition provides a kind of anchor holding down retail prices – it has been estimated that Wal-Mart accounts for almost 10% of China's exports to the U.S.

This process interacts with a greatly accelerated product cycle – improvements in consumer electronics, for example, now reach the market faster, but also diffuse throughout the market more quickly. New features and capabilities in the entire range of consumer electronic items and computers are accessible to consumers much more quickly than a decade and a half ago when the adoption process began in specialty stores and gradually moved to larger generalized merchandisers. These products are likely to show up in Best Buy, or even Target, as quickly as a specialized retail establishment. A 2007 survey among CE executives by Twice (This Week in Consumer Electronics) points to how fast the process has become. (See chart.)

How long does it take for a product similar to an existing one to enter the market?



Source: Twice. Survey of consumer electronics manufacturing executives, 2007.

Another complicating factor is found in changed consumer attitudes on customer service – especially when it comes to returns. Unprecedented volumes of goods are now returned, no questions asked. This trend started with the growth of the catalog channel, since size and color often did not meet expectations. LL Bean, in fact, built its reputation on accepting return on any item pretty much regardless of condition. E-commerce has accelerated this trend many fold. The brick-and-mortar world must keep up as well – the competitive low margin marketplace pretty much demands it. Thus, customer returns have added a new dimension to traditional inventory headaches. In fact, customer service and quality assurance have not become integral elements for the liquidator as well.

THE GLOBAL EXCESS INVENTORY MARKET

Estimates from the Reverse Logistics Association for customer returns range from 4%–6% of retail sales, which currently, using Department of Commerce figures, equals roughly $60 billion. The rate of return varies greatly over category, with consumer electronics at an approximate 20% rate consistency during 1994–2004. Over the same period, retail return activity for consumer electronics grew an astonishing 309%.

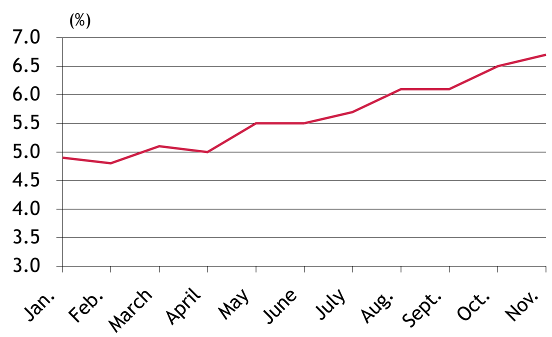
The liquidation industry has always been a solution provider to retailers and distributors – adopting an internet-centric model didn't really change the fundamentals. The issue was and remains: how does the industry respond to the economic business and economic factors that underlie the inventory and supply chain problems of retailers and wholesalers?

Asset Recovery in a Recessionary Environment

The greater economic volatility that has accompanied globalization has been a key driver in the changing nature of the liquidation industry. Alan Greenspan expressed this phenomenon in the title of his book, *The Age of Volatility*. The recent economic crisis, which most economists have characterized as the worst since the Great Depression, has made clear how extreme such volatility is. The crisis had its roots in the U.S. housing market, which in the 2000s saw astronomic growth, enough to create a bubble. By 2007, the housing market could not be sustained, and falling prices triggered a chain reaction of worsening calamities.

September and October of 2008 saw the collapse of both credit and stock markets. After rising 2.8% in the second quarter, U.S. GDP decreased at an annual rate of 0.3 percent in the third quarter of 2008, according to advance estimates released by the Commerce Department. Growth in the unemployment rate is another indicator pointing to further recessionary concerns.

U.S. Unemployment Rate 2008



Source: U.S. Department of Labor

The Institute of Supply Management Manufacturing Index, released in October, fell to 38.9%, the lowest reading since 1982. Any doubts that the economy was heading into a recession were put to rest. The remaining question was how long and deep the contraction would be.

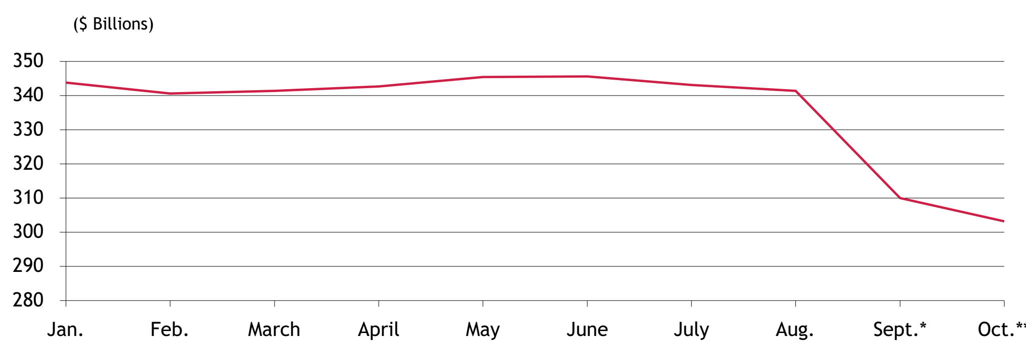
Consumer retail spending has been further hurt by tightened lending from banks. The Federal Reserve, in a survey of 55 U.S. banks found that 60% had raised standards on credit card debt and 65% done the same for other types of consumer loans in the past three months. One-fifth of the banks had even tightened their standards on prime customers, indicating how risk-averse financial institutions have grown during the credit crisis.

Several recently released consumer confidence surveys reveal a fairly bleak outlook. The Conference Board reported the Consumer Confidence Index plummeted in October to an all-time low of 38 points from 61 points in September. Lynn Franco, Director of the Conference Board Consumer Research Center, stated that “the impact of the financial crisis over the last several weeks has clearly taken a toll on consumers' confidence,” and further noted that the 23 point decline in the Index was its third largest single drop ever. These results were matched by the University of Michigan Consumer Confidence Index, which fell to 57.5, down from the 70.3 reported in September.

Consumer confidence has weakened toward the consumer electronics sector as well. The CEA-CNET Index of Consumer Technology Expectations, which has been tracking consumer spending expectations in the CE sector since January 2007, dropped for a third consecutive month to 76.2 basis points. This is down 11 points from October 2007, and the second lowest score recorded (75.2 was recorded in May 2008).

Not surprisingly, these conditions have had substantial impact on retail activity. A record October 2008 drop in consumer retail spending presents the most direct evidence of how the current economic turmoil will affect the excess inventory market. The U.S. Census Bureau estimated U.S. retail and food services sales were $363.7 billion (including automotive and gas purchases) in October. This represents a 2.8% slump from the previous month, or 4.1% below October 2007. Auto sales (down 6.2%) accounted for much of the decline, but electronics and appliance stores also fell 2.5%.

U.S. Retail Sales 2008

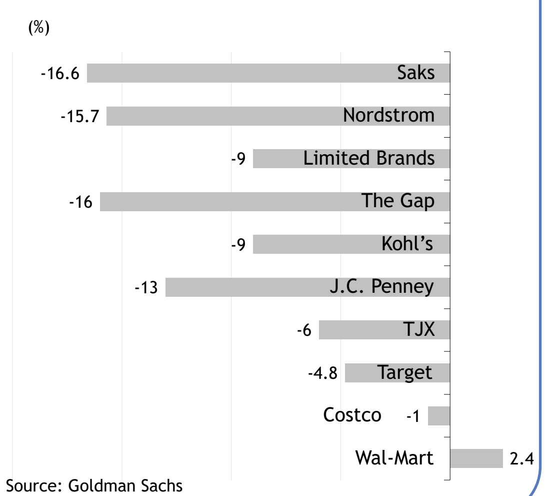


*Premlinary. **Advance. Note: Does not include auto, gas, and related items. Source: Bureau of Economic Analysis

The cumulative effect made October 2008 retail sales one of the worst in memory. However, as the graph below indicates, high-end retailers were hit much harder than discount and value oriented venues. Wal-Mart bucked the trend among top retailers and showed modest growth. Nordstrom and Saks, however, saw precipitous declines.

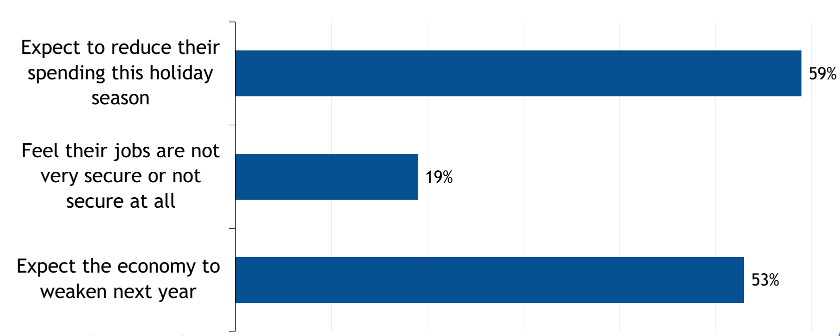
November has seen no let up in worsening conditions for retailers. On November 10, the big box consumer electronics retailer Circuit City filed for Chapter 11 bankruptcy. Several days later, one of its largest rivals, Best Buy announced greatly lowered sales expectations for the year. On the other hand, falling gas prices brought a slight uptick to consumer confidence, according to a Reuters/University of Michigan November survey, from 57.9 points from 57.6 points in October.

Change in Same-Store Sales (Oct. 2007 vs. Oct. 2008)



Source: Goldman Sachs

Consumer Attitudes

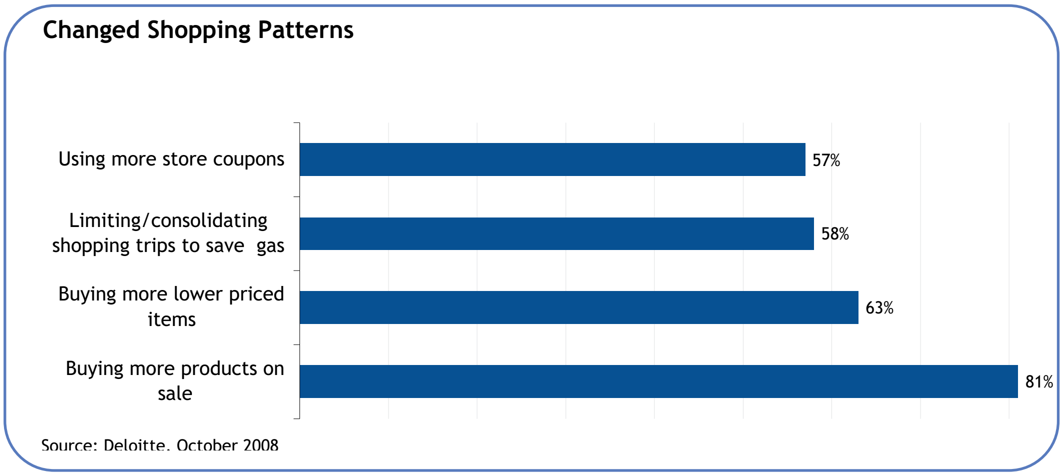


Source: Deloitte, October 2008

Consumer Behavior

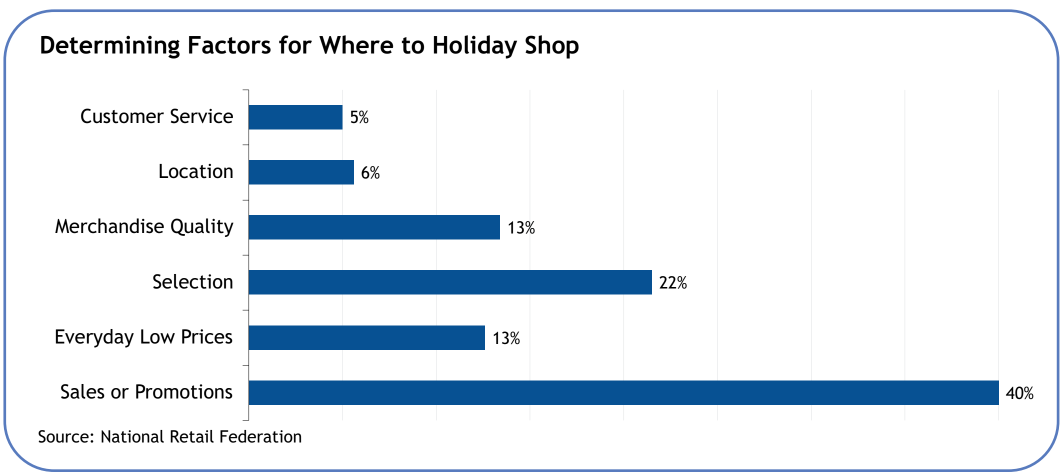
Deloitte's Annual Holiday Survey, which has gauged consumers' outlook, year-end holiday expectations, and related spending and purchase patterns since 1985, found that a record number of consumers were pessimistic about the economy. American consumers were adapting their purchasing patterns in response to current economic conditions.

The Deloitte study also found that 68% of consumers planned to change the way they shop due to economic concerns.



The bottom line was that finding value was the top priority for most consumers, with 73% stating that the best value will determine their choice of retailers for the season and 72% saying low prices were key.

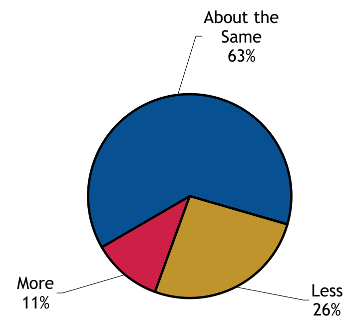
Certainly, the credit crisis, stock market turbulence, and general economic malaise hit at a particularly awkward point in the fiscal year: just in advance of the holiday shopping season. Sales occurring in the fourth quarter, especially following Black Friday/Cyber Monday, provide a disproportionate share of retailers' revenue for the year – for some retailers, as much as 50%. The National Retail Federation's 2008 Holiday Consumer Intentions and Actions Survey found that consumers planned to spend only 1.9% more in 2008 over 2007 (an average of $832 versus $817). Cost savings were predictably the driving factor as to where consumers plan to make their purchases.



Furthermore, 70% planned their shopping in discount stores. The NPD Group found similar concerns about spending in its Annual Holiday Survey.

Despite the bleak consumer outlook, the retail slump did not fall equally on all retail sectors. On November 11, the Consumer Electronics Association forecast 3.5% fourth quarter growth for CE – citing flat-panel TV sets, mobile phones and GPS systems as likely to do well among holiday shoppers. Indeed, the NPD Group noted that September flat-panel TV sales by unit volume were up 20% from the prior year. Two other CE categories showed revenue growth in September — notebook computers (9.0%) and digital SLRs (9.5%).

Holiday Spending Plans



Source: The NPD Group

Productivity declines and lower consumer spending clearly pointed to a recession. The question remained how deep? The key determining factor would be how quickly the credit markets revived. This crisis has had a direct effect on short-term borrowing, largely through the commercial paper market, that is essential to maintaining retail inventories.

It is impossible to say how deep and how long the ongoing economic downturn will be. The $700 billion bailout package passed by Congress has yet to take hold. The Treasury Department quickly re-focused its targets in the bailout beyond buying distressed assets of the large financial institutions that underpin the credit market. On November 12, Treasury Secretary Paulson announced the government would inject capital into the non-bank financial institutions providing consumer credit. As Paulson stated: "The important markets for securitizing credit outside of the banking system also need support. Approximately 40% of U.S. consumer credit is provided through securitization of credit card receivables, auto loans and student loans and similar products. This market, which is vital for lending and growth, has for all practical purposes ground to a halt."

THE GLOBAL EXCESS INVENTORY MARKET

The overwhelming economic consensus is that massive fiscal stimulus from the federal government is the most effective way to spur the slumping retail sector. The NPD Group found that the previous stimulus in May 2008 gave a definite boost to consumer electronic sales. It is a sector, along with computers, for which there is still considerable consumer demand in terms of discretionary spending – which points to an important takeaway. The same principles that have driven the great shift in the liquidation industry over the past decade are still very much in operation today. In fact, the premium that was put on excess inventory management following the 2001 recession is even greater now. The tighter credit market, in particular, means that unsold inventory will only be a greater drag on the bottom line. The climate in 2009 is likely to prove extremely unpredictable and retailers and wholesalers – whether focused on consumer or B2B markets – will have to remain very responsive. The stakes are much higher and inventory solutions could well be crucial to survival.

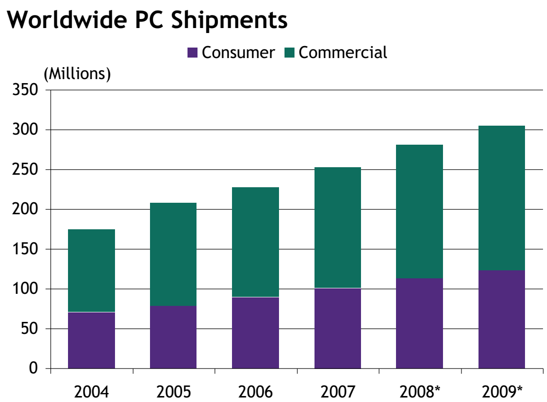
3.

Computers and Consumer Electronics

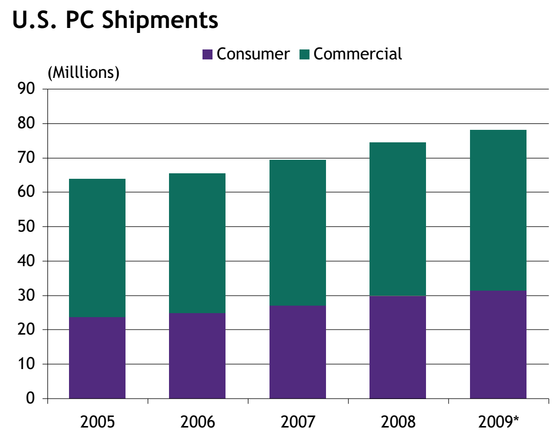
Although the factors listed previously cut across the entire retail spectrum, the impact has fallen more heavily on certain product categories. The two product areas most sensitive to these changes are consumer electronics and computers, which saw significant if not spectacular growth through the 1990s. Both areas are particularly well suited to offshore manufacturing methods in Asia. Both are logistic intensive, involving assembling component parts from diverse sources. Most importantly, this market sector has a short product cycle; consistent hardware improvement and introduction of new software push consumers to buy newer versions every few years. By the end of the 1990s, computers in particular had dropped in price, and their use had been adopted widely at work, school, and home. This was of course only accelerated by the rise of the internet. For these reasons, these two market sectors provide very useful illustrations of the dynamics of the current liquidation situation.

The great bulk of computers that are sold in North America come from the other side of the Pacific. Production facilities in China and Taiwan are responsible for assembling most of the computers for Hewlett-Packard, Dell, and Lenovo, among many others. This volume is the chief reason, of course, for steady downward glide of the cost of computers and other electronics. This presents a severe dilemma. Despite strong retail sales, manufacturers faced persistent price wars that lowered revenue. For example, in 2005, the U.S. laptop market experienced year-over-year unit growth of 46%. But from December 2004 to December 2005, the average selling price (ASP) dropped 17%. ASPs for all PCs fell 8% from 2006 to 2008, while volume grew close to 10%.

What is surprising is that the market continued to grow steadily, despite the struggle for net income. Furthermore, as the charts indicate, the worldwide shipments grew much faster than those from the U.S.

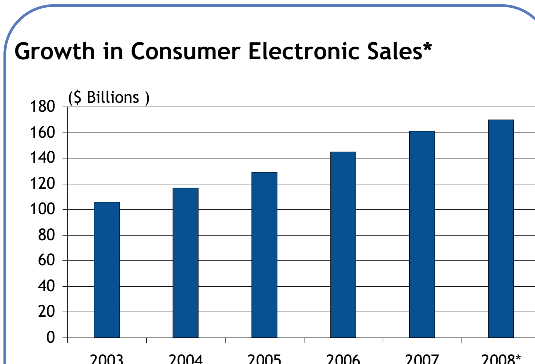


Source: IDC. *Forecast data Shipments are in millions of units. PCs include Desktop, Notebook, Ultra Portable, and x86 Server



Source: IDC. *Forecast data Shipments are in millions of units. PCs include Desktop, Notebook, Ultra Portable, and x86 Server

In the years following the 2001 recession, consumer economic products went through a steep decline in prices before leveling out and rebounding in 2004, according to The NPD Group's Consumer Electronics Price Watch. Initiated in January 2003, the watch follows a basket of the most frequently purchased electronic products in that sector, including televisions, PCs, cameras, and media players. Prices in the market basket showed a 25 percent drop by June 2004. The steepest drop was from June 2003 to June 2004, roughly 16%, when price erosion slowed greatly. Price declines were seen 19 of 27 categories. Nonetheless, the sector continued to grow. (See chart.)

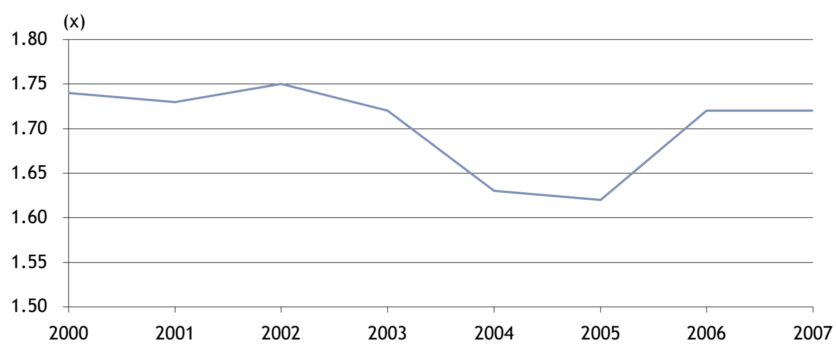


*Includes computer sales. Source: Consumer Electronic Association.

Essentially, as the U.S. economy struggled out of the recession, sluggish consumer spending caused retailers to lower prices and clear inventory. This is reflected in consumer inventory ratios depicted in the chart below. Note that the inventory category measured by the Census Bureau is somewhat broader than just consumer electronics. The ratio is derived from dividing the dollar value of inventories by the dollar value of sales, tracked monthly. It is a good indication of retailer expectation in that it measures reserves. For example, a ratio of 2.0 means the retailer has excess inventory for a full additional month. Throughout the 1990s, the ratio remained close to 2.0. After fluctuating lower in 2000 and 2001, retailers went through a three-year period of minimizing their inventories.

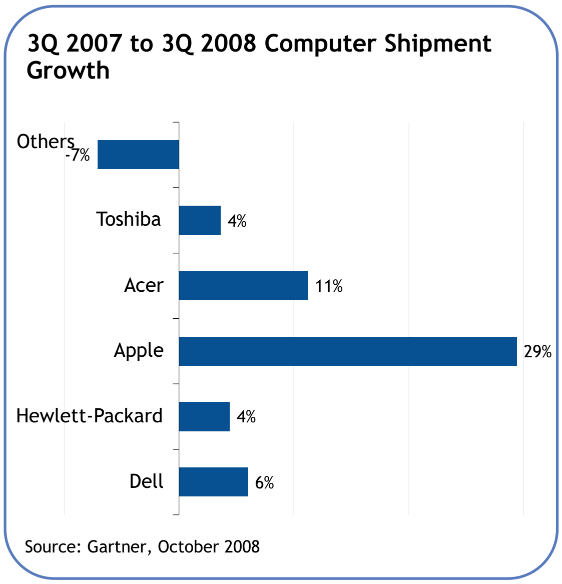
Bear in mind the inventories measured include furniture and home furnishings, which have a longer shelf life traditionally exhibit greater price stability than consumer electronics. The ratio's precipitous 2002—2004 fall coincided with steep price drops, which points to a need to clear inventories of electronics goods and appliances. Some of that was in response to earlier liquidations that began as the dot-com bubble burst, some of it reflected continued manufactures coming to the U.S. market. This corresponded to a period of accelerated growth of online liquidators.

Ratio of Retail Invoices to Sales — Furniture, Home Furnishings, Electronics, and Appliance Stores

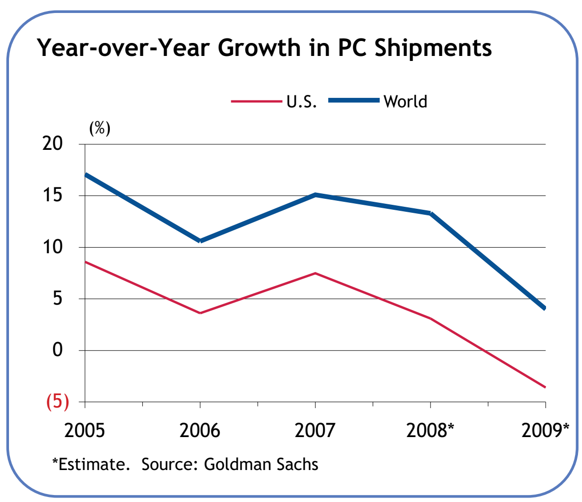


Source: U.S. Census Bureau, Monthly Retail Sales Survey

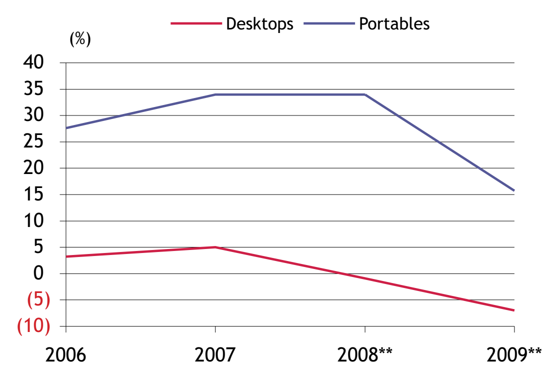
Through the first three quarters of 2008, the computer sector maintained very credible growth in the face of the slackening economy.



However, growing evidence of continued weakness in consumer demand in this sector has prompted Goldman Sachs to lower its estimates of PC shipments for 2008 and 2009. U.S. shipments are expected to grow a mere 3.1% in 2008 and then shrink in 2009 by 3.6%. Shipment growth worldwide, previously with robust double-digit numbers, will drop to 4.0% in 2009.



The main driver in PC growth will remain notebooks. Desktop computers will see their share of the market shrinking.

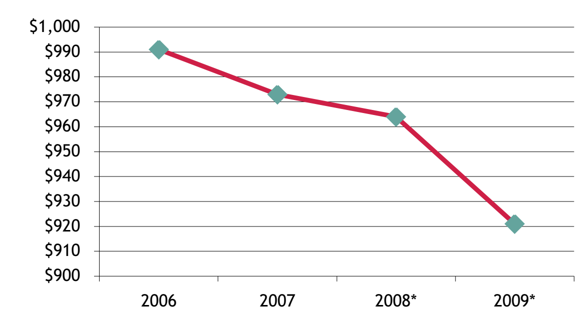


*Portables comprise laptops and netbooks. **Estimate.
Source: Goldman Sachs

In general, PC growth will come from emerging markets, with the mature markets in the U.S and Europe generally declining. In addition to geographical factors, product mix will play a major role. Consumers will be searching for lower cost models among notebook computers – the so-called netbooks. These are simpler, less powerful laptops that are expected to make substantial inroads into the notebook market – with considerably lower ASPs. Goldman Sachs projects that netbooks will capture an astonishing 96.2% of the year-over-year growth in the 2009 notebook market.

Consumer flight to less costly alternatives will mean that ASPs will not keep pace with the growth in shipments – pointing to continued supply outpacing demand.

All signs point to a U.S. PC market that will remain extremely prone to excess inventory issues. Consumers will continue to benefit from lower ASPs, maintaining pressure on retail inventory.



*Estimate. Source: Goldman Sachs

No Cures for Unpredictable Demand

The fundamental problem in coming to grips with excess inventory is the inability to predict demand. Manufacturers have to predict future demand by relying past sales figures. However, the further from the point of sale the manufacturer is, the fuzzier the information becomes. A small up tick in orders from retailers to distributors, which may be part of normal demand fluctuation, is likely to be magnified by the time it reaches the manufacturer, since the distributor may well want to adjust its reserve stock upward as well. The manufacturer then ramps up production, but by the time product has moved back through the supply chain to the retailer, demand has fluctuated back down.

Logistics and supply chain management technologies continue to improve both manufacturing productivity and the ability of suppliers to get the merchandise to the store. Unfortunately, predicting how much and of what product the consumers will buy, remains more art than science. Not that the commercial world didn't try: according to IDC, companies spent $19 billion demand forecasting software in 2002 alone. The results have been meager. A 2003 Booz, Allen & Hamilton survey of 196 senior executives found that nearly half felt that supply chain technology in general had not met their expectations; 56 percent specifically blamed demand forecasting software.

U.S. Census Bureau researchers analyzed 87 inventory-to-sales ratios in 45 manufacturing, wholesale distribution, and retail trade industries for the 12-year period from January 1992 through December 2003. They found that less than half of the ratios showed statistically significant declines in the amount of inventory to sales. Information technology may indeed have improved inventory management, but this improvement is not reflected in inventory-sales ratio data for many U.S. industries. In a further case study of the pharmaceutical supply chain, the same researchers demonstrated that relevant technological investments, in fact, led to an extended period in which inventory-to-sales ratios increased.

The key take-away is that this chronic problem of matching supply with demand is only made more difficult under the conditions of today's economy, thus resulting in greater swings to over production and excess supply.

The Excess Inventory Market – Assessing Opportunity

The asset recovery industry has been estimated at roughly $60 billion-$80 billion annually. Some skepticism is in order since this is a standard figure that is fairly frequently cited, but seldom broken down. It is usually used as a ballpark figure. Actually estimating the value of liquidated inventory is extremely problematic for several reasons. The first is that this information is not tracked systematically and there are hundreds of businesses engaged in liquidation, with extremely broad range in volume and revenue. Furthermore, businesses generally don't want to draw attention to what they are incapable of selling at the expected retail price. An even more glaring difficulty in assessing this market is that by its nature there is no actual set value on the goods sold. Obviously the merchandise was below demand at a given price point, or possibly was sold and returned.

Using very liberal ballpark figures for the five largest liquidators for which there is information available — uBid.com, Overstock.com, Liquidation.com, Bidz.com, and Big Lots – approximates $950 million. All have revenue over $100 million. The liquidation-specific revenues from Gordon Bros., another large firm, are not publicly available, although the firm's total revenues are generally estimated in the billions of dollars. This would leave a very great number of smaller firms making up the difference in the total $60 billion market. This suggests that the figure is not particularly useful in assessing the potentials the market offers.

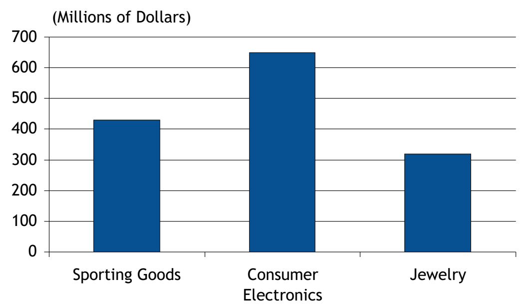
Another approach is to look at product categories and estimate what percentage of inventory cannot be sold at retail or through discounters or outlets. A somewhat simpler way of getting an understanding of the market potential is to estimate how the current retail categories are faring.

According to Gartner, Inc., there were roughly 64 million PCs shipped to the U.S. in 2007. The NDP Group estimates an average 2008 selling price (ASP) of $734 for desktops and $1,093 for laptops, or a combined $914. Goldman Sachs projects a slightly higher $964. Taking an average of the two estimates of $939 and multiplying by units sold, yields $62 billion. This estimate depends, of course, on all the PCs selling at the ASP, so actual dollar value might have been lower. The next question is how much of this market could be sold as excess inventory? Assuming a modest 3 percent of units shipped become excess inventory, that equals 6.4 million computers. If these units are liquidated at 30% of the ASP, then computer liquidation alone comes to $1.3 billion.

THE GLOBAL EXCESS INVENTORY MARKET

Using data from Plunkett's, the Consumer Electronics Association, and Jeweler's Circular Keystone, and adjusting for annual growth rates, allows pro forma estimates of $43 billion, $65 billion, and $32 billion, respectively, for sporting goods, consumer electronics, and jewelry markets in 2007. Applying the same hypothetical excess inventory and discounts suggests the following potential market volume.

Pro Forma Potential Liquidation Market Values



Source: Galati+Jackson.

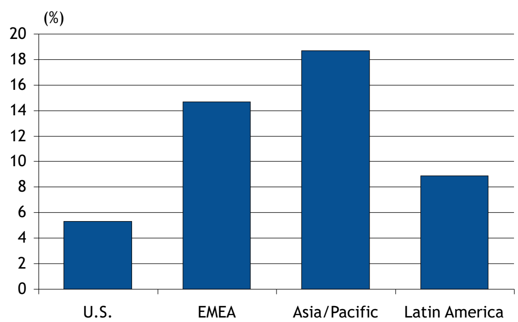
These estimates are likely quite conservative and are only suggested as the lower end of the ball park. Two of the variables – excess inventory and discount percentage – will shift a great deal depending on many different factors. The key drivers of excess inventory will remain the massive supply of imported goods and the competitive landscape of U.S. retail. This will assure a very large, if volatile, liquidation market.

The Demands of the New Liquidation Environment

Traditionally, a liquidator and his suppliers didn't have to be too concerned about where the merchandise was liquidated. A high-end retailer probably didn't worry too much that distressed inventory on discount in a warehouse-sized facility on the other side of town would draw too many of his customers. Now that the internet has erased much of the geographic aspects of commerce, the same merchant needs to very careful he doesn't go into competition with himself. A liquidator has to have access to other markets and the awareness about them to know that stock shipped won't interfere with his supplier.

In fact, liquidators today are going to have to function increasingly on a global level. As argued, globalization is a key factor in creating the inventory problems that retailers face. It only makes sense that it would be part of the solution. Furthermore, the degree of market saturation in the U.S. is a big part of the problem. Foreign markets are becoming increasingly attractive. This is especially true of the computer sector, where growth is currently growing at a much higher rate than in the U.S. Similarly, brand protection is a much higher priority than ever before. This is primarily a function of the degree major brands now are in excess inventory stream.

Worldwide PC Growth by Region -- 2007



Source: Gartner, Inc.

These issues point to several conclusions about how liquidators must re-focus themselves in today's world:

Coverage: The more clients the better, across as many sectors as possible. This report has focused on only two sectors of the excess inventory market. The same economic issues are present to varying degrees in almost all consumer and B2B sectors. And even within just consumer electronics and computers, there is an ever increasing diversity of submarkets. This means that different product spaces must be covered in depth as well as in breadth. This includes having markets available in which to dispose excess merchandise.

Integration: It's time to stop thinking of liquidators as an afterthought, but as part of the entire supply chain process, albeit the very last part. This means ongoing partnerships.

Flexibility: Inventory demand will always remain unpredictable. If anything, the uncertainty will only grow in today's more volatile international economy.

Conclusion

This report has examined how the liquidation industry has evolved over the past decade from a simple traditional model to one that meets the challenges of a greatly more complex retail economy. Asset recovery in the global economy requires comprehensive and integrated solutions. At press time, the U.S. and many other nations are weathering a period of severe economic downturn. However, the underlying forces that have shaped current economic conditions have also played a central role in giving excess inventory management a critical role in many retail sectors. Therefore, asset recovery solutions will undoubtedly continue to evolve and serve those organizations affected by this unexpected retail tsunami.

In today's business world, margins will be squeezed as prices respond to the recessionary environment. In many retail sectors, especially electronics, consumers have come to expect consistently higher quality coupled with affordability. This will require constant turnover of inventory, a process that necessarily, sooner or later, results in the need to liquidate distressed merchandise. In addition, tighter credit will make moving inventory even more critical. As Business Week reported in its November 22nd issue, retailers have already filed for bankruptcy in 2008 – including many big names. However, bankruptcy may no longer provide the protection allowing businesses to re-emerge intact: "You can't get the financing to reorganize, so we are in a world of liquidation," stated Howard Davidowitz, chairman of retail consultancy Davidowitz & Associates.

In the final quarter of 2008, economic indicators continued to point to greater uncertainty, and all business sectors, not just retailers, are hoping to find a port in the storm. However, the turbulence will certainly continue. On November 19th, the Labor Department reported that consumer prices plunged 1 percent in October, the biggest one-month decline since 1947. Expectations for the 2008 holiday shopping season, which began earlier than ever before, have already dropped accordingly. Most retailers are hoping just to make it into the black. The economy is sailing into uncharted waters for the coming year and it's too early to say when solid financial results will start to provide any accurate forecasts.

In the meantime, as this report reveals, the asset recovery industry is well positioned not to just ride out the storm, but to seize the opportunity. Since the liquidation industry has low barriers to entry, there is likely to be considerable competition among liquidators as well. Many, however, will retain instincts more attuned to traditional inventory solutions. The asset solutions provider that understands the importance of partnerships and established relationships among distributors, retailers, and manufacturers will have a strong competitive advantage to best meet the needs of the changing business environment.

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About Enable Holdings, Inc.

Enable Holdings, Inc. is a leading asset recovery solutions company for the world's most trusted brands. Enable Holdings connects brand names with excess inventory solution needs to customers through its multi-channel asset-recovery solution that includes online auction platform uBid.com, fixed-price online commerce solution RedTag.com, offline excess inventory solution RedTag Live!, business-to-business solution Dibu Trading Corporation, and upcoming private auction software solution Commerce Innovations.

Enable Holdings' comprehensive solution set efficiently matches sellers and buyers through its various commerce solutions. Enable Holdings has helped thousands of businesses sell over $2 billion of excess inventory over the past 10 years and has saved consumers hundreds of millions of dollars in the process.

- **uBid.com:** Auction website increases speed of sales without channel conflict.
- **RedTag.com:** Fixed-price website maximizes cash recovery by letting sellers set prices.
- **RedTag Live!:** Live warehouse sales move product at fixed prices without channel conflict.
- **Dibu Trading Corporation:** Business-to-Business wholesale division moves large volume of inventory lots worldwide.
- **Commerce Innovations:** Custom software platform facilitates secure, private sales of excess inventory.

Through these sophisticated channels brand name sellers are able to reduce excess inventory more efficiently and profitably than ever before. However they choose to buy, shoppers now have a connection to the world's most trusted brands at prices far below retail.

Enable Holdings is trading under ticker symbol ENAB.OB
on the NASDAQ OTC bulletin board.

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This report is intended to present an unbiased opinion of the excess liquidation market. The report, released by Enable Holdings was researched and produced by Galati+Jackson, in conjunction with Galati Lines Bermuda.

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