

# Report: The Reverse Logistics Opportunity For 3PLs

Contributed by Paul Rupnow  
Thursday, 26 February 2004

CEOs and the senior management of 3rd Party Logistics Providers (3PL's) and Outsourced Service Providers (3PSP's) need to take a close look at Reverse Logistics as an excellent strategic source of value added revenues. To help you understand Reverse Logistics Services we have created an introductory report:

The Reverse Logistics Opportunity - What Is Reverse Logistics, Who Needs Help, And Why You Need To Do It

Part 1 - The Reverse Logistics Opportunity

What Is Reverse Logistics, Who Needs Help and Why You Need To Do It

It is time to rethink Returns. Reverse Logistics is an excellent strategic source of value added revenues. Manufacturers, Distributors and Retailers are struggling with the Reverse Supply Chain. Industry experts suggest the annual costs of Reverse Logistics total \$35 billion. Product Returns handling is an important process of the supply chain that is not well handled. Economic pressures for corporate profits are forcing manufacturers and retailers to look very hard at cost controls. Reverse Logistics is one of the few remaining opportunities that has NOT yet received much attention.

Many Manufacturers and Retailers are looking to outsource Reverse Logistics and Product returns since it is not a strategic part of their business. They currently have very inefficient, slow and expensive processes for handling returns. Few tools or systems exist to assist in handling returns effectively. Considerable value is lost when these Returned Assets are not processed quickly and completely.

3rd Party Logistics Providers and Outsourced Service Providers are ideally suited to manage Reverse Logistics since the skill sets used to process forward and reverse logistics are similar. Reverse Logistics, however, encompasses much more than accepting inbound shipments from your client's customers.

Traditionally, Product Returns are something that 3PL's try to avoid. However, with a solid understanding of Reverse Logistics needs and processing, Reverse Logistics represents a quick and excellent source of high volume transaction fees that can be generated from your existing facilities and skill sets.

"As companies strive to wring every cent out of their logistics costs, they're increasingly taking a hard look at their reverse logistics practices. And no wonder - they may find a mother lode waiting to be mined." (Getting Started in Reverse, Leslie Hansen Harps, Inbound Logistics, January 2002)

Reverse Logistics Services is an opportunity for outsource providers to:

- Provide Additional Services for new revenues from your Existing Customers
- Differentiate your Company's services from those of your competitors
- Attract New Clients to these Services
- Enhance your status in the Global Supply Chain

What Is Reverse Logistics?

The Reverse Logistics Executive Council is a collaboration of manufacturers, retailers and academics. They have defined Reverse Logistics as follows:

Reverse Logistics is the process of moving goods from their typical final destination to another point, for the purpose of capturing value otherwise unavailable, or for the proper disposal of the products. Reverse Logistics activities include:

- processing returned merchandise for reasons such as damage, seasonal, restock, salvage, recall, or excess inventory;
- recycling packaging materials and reusing containers;
- reconditioning, remanufacturing and refurbishing products;
- obsolete equipment disposition;
- hazardous material programs;
- asset recovery.

With most companies, handling Product Returns also includes an important transaction with the customer who is returning the goods. This may involve the shipment of a replacement in the case of goods returned for a warranty issue. For other customers, it may also involve the issuance of a credit or refund.

The SCOR Model (Supply Chain Optimization Review) developed by the Supply-Chain Council now includes Reverse Logistics.

Traditional Supply Chain improvement strategies have tended to focus on the forward logistics processes. New forces and an understanding of the connection to revenue and customer satisfaction are moving Reverse Logistics higher in the supply chain agenda.

Reverse Logistics is an Important Emerging Issue

Companies and Industry associations are developing groups and panels to address key Reverse Logistics topics, for example:

- Joint Unsaleables Management Conference by the Grocery Manufacturers of America, Food Distributors International and the Food Marketing Institute
- Unauthorized Deductions Management (Matching Returns to retailer claims) Session at the NCA National Candy Association State of the Industry Conference
- Panel Discussion - "Taming the \$10 Billion Beast: Reducing the Costs of Taking Back Product" at the Consumer Electronics Association (Fall Conference 2002)
- 'Managing Returns in a High Return Industry' and 'Warehousing's Role in Reverse Logistics' at the WERC Conference 2002 (Warehousing Education and Research Council)

Who Needs Help Managing Returns

Industry experts suggest the annual costs of reverse logistics totals \$35 billion according to "Going Backwards: Reverse Logistics Trends and Practices" book published by the Reverse Logistics Executive Council.

"When it comes to returned product, there's a fair amount of money often left on the table," says Dr. Dale Rogers, the Director of the Center for Logistics Management and a Professor of Supply Chain Management at the University of Nevada. "Manufacturers need to be aggressive in managing what happens. They need to have a plan and make good decisions to get value out of returns" (Industry Week, Apr 16, 2001)

Source: Going Backwards: Reverse Logistics Trends and Practices book published by the Reverse Logistics Executive Council

Many products are returned to the Retailers shortly after a consumer purchases the product, and as a result Retailers have a large problem managing returns. As well, Manufacturers must deal with returns from Retailers, the channels of distribution, or end customers with warranty issues.

For example in 2001 there were about 40 million desktops and mobile Personal Computers sold. About 9 million (23%) of these were sold through Retail Stores. The Retailer experienced a Return Rate of about 10% or 900,000 Units. Each of these units is estimated to cost the Retailer \$40-\$50 to process and ship back to the manufacturer or to dispose of the units. The manufacturers estimate that each Return costs them about \$500 each. This adds up to a whopping \$486 million. Each return is taking the manufacturers from 4 to 12 weeks to fully process. (Source: Ease of Use / PC Quality Roundtable)

Returns are a small percentage of sales for the retailer or manufacturer, however, in high volume environments like consumer goods, this small percentage adds up to a large reverse logistics problem.

The Returns Process

The Returns processes can be summarized in the diagram below. In processing a returned unit, 2 groups need to be satisfied: the end customer who returned the unit and the company that now needs to handle the returned unit and try to recapture value from it.

An overview of the returns process is as follows:

**Retailers:**

Retailers need to handle returns from their customers. These returns arrive in a variety of conditions, many with open boxes, some with defective units and many with no faults. A retailer needs to process these returns and maximize value from these returned items by getting them back on the store shelf, returning them to the manufacturer for credit, liquidating them through some other channel or scrapping them.

**Manufacturers:**

Manufacturers need to handle returns from multiple sources such as end-user customers, retailers, value added resellers or distributors. The manufacturers typically require their customers to obtain an approved RMA (Returned Materials Authorization) or RA (Return Authorization) before accepting any product returns. These returns arrive in various quantities. The returns may be new stock, damaged stock, open box or defective. The manufacturer's main concern is to satisfy the customer or distribution channel partner who is returning the goods by exchanging the unit, repairing the unit or issuing a credit. The returned units need to be processed and then returned to inventory, repackaged, returned to vendor, repaired or scrapped. The manufacturer needs to maximize value on these returned units by processing them quickly to yield the highest price through secondary market channels.

**Why Customers Want To Outsource Product Returns**

Currently most retailers and manufacturers struggle with handling and processing returns internally.

Many manufacturers will conclude that handling product returns is not a strategic core competency and will look for an outsourced provider, as they have done with Forward Logistics

Most retailers and manufacturers struggle with returns for many reasons such as:

- it is a small part of their business processes
- their focus is getting new products to customers
- they have difficulty understanding and controlling costs

- there is poor or no systems for managing the Returns processes
- a lack of systems results in slow processing of the returns and the returned inventory
- inability to track or monitor inventory levels of Returned stock
- few good channels exist to get value from their returned and processed units
- Returns  
can be a significant problem if not managed well. Without good systems in place significant individual attention is often required to manage a single return to competition.

#### Why 3PL Providers Can Help

Outsource Logistics providers and 3PLs are ideally suited to help handle Reverse Logistics and generate significant savings since Reverse Logistics is an easy extension of the existing business services of 3PL operations:

- Many of your existing customers likely already need help
- You are already masters at many of the required processes
- You are experts at managing outsourced projects
- You are experts at tracking and managing inventory
- You are already doing minor inspection work
- You are already doing minor reconditioning or repackaging
- You are likely to generate significant savings in Shipping
- Your ability to rapidly process transactions solves their key problem of slow processing

#### Goals of Reverse Logistics Services

To be successful you need to satisfy the goals of your customer and the goals your company:

Client Goals For 3PLs  
Your Company Goals

- Satisfy their customers
- Maximize Asset recovery
- Maximize Returns processing speed
- Minimize processing costs
- Minimize inventory levels
- Monitor activity
- Monitor costs
  
- Smooth processes and workflow
- Rapid inventory movement resulting in processing and transaction fees
- Profitable fees for processing
- High level of customer satisfaction

#### What Do Customers Want?

Outsourcing Reverse Logistics should be handled like other outsourcing decisions. The customers will be looking for:

- Cost Savings - monthly costs, one time savings
- Easy management
- Regular status updates
- One Stop Shopping - one provider who can handle as many of their requirements as possible
- A Partnership - the nature of Returns will require a close working relationship

Specific to Reverse Logistics handling Clients will be looking for:

- Quality Service for their Customers -you may be an extension of your client's customer service group and will need to respond to their end customer's needs and requests
- Rapid cycle time -through create, receive, ship or credit, inspect, recondition, recover
- Accuracy - correct handling of units through each step of the required processes
- Inventory Management and Minimization - of both Finished Goods and Good in Process
- No misplaced or unhandled units
- Visibility -status of a unit or RMA at any given time
- Timely Data updates - i.e. to process customer credits based on receipts
- Reports
- Detailed billing

How Reverse Logistics Differs From Forward Logistics

Logistics typically refers to moving product in the forward direction. Reverse Logistics involves moving the product in the reverse direction, from the customer or channel partners back to the manufacturer. The biggest differences are as follows:

- Open box
  - the units are usually being returned due to a problem, dissatisfaction or warranty issue. The warranty units could be 3 or even 5 years old.
- Single units - the returned units often do not arrive in bulk on pallets. They are single units often in non-standard packaging.
- Verification at Receiving - since the returning product is not in "new" condition, additional verification must be performed at receiving to ensure the expected product from a customer matches the actual received product.
- Inspection and Grading - since the returned units are in various conditions they need to be processed through inspection or grading to determine where

to stream the unit to recover the highest value.

- Reconditioning
  - many returned items just require basic testing and repackaging. (well within the existing capabilities of most logistics providers). Some units require more advanced repair work. The units are streamed back to the original manufacturer or to a service center for repair.
- Tradition and New Realities

Historically

Logistics providers avoid Product returns and reverse logistics. Returned goods are viewed as inventory no one wants, collecting dust in the back corner of the warehouse, with no transaction fees, no storage fees and lots of hassle to get the client to make a quick decision on disposal.

While this scenario will never change for many logistics customers, the reality of today's economic, retail and manufacturing environment is forcing many companies to handle their product returns more carefully.

Tradition  
New Realities

Returned Inventory has little value

A  
high percentage of returns products have no defects and therefore have high value especially if processed quickly and resold (i.e electronics industry returned goods)

Returned Inventory is costly to just hold in a warehouse

Proactive  
services and procedures for handling returned goods enable the goods to be processed immediately, instead of being set aside. This means transaction fees.

It is costly to handle small packages; need to move pallets to be economical.

Many  
customers with returns problems have very large volumes of returned goods (100, 1000, 10,000 per day). These volumes become economical logistics business.

Handling returns requires many processes not currently in place

Often  
a high percentage of returned goods for high volume customers are not defective and only require minor processing to recondition for resale. Skills such as sorting and repackaging are already value added services offered by most Logistics providers. Sophisticated skill requirements often represent a very small percentage of the returned goods and can be arranged with your customer or third party partnerships.

## Why Returns and Reverse Logistics Are Profitable, Value Added Business For 3PLs

The current challenge for most companies is just getting a Return fully processed, never mind effectively, inexpensively or in a timely manner. The management of Reverse Logistics is a painful process for manufacturers and retailers. It also represents a small part of their business and they are often not willing to commit the people, systems or resources to this area to manage it well. Few standards exist to define how to process and manage returns, but these processes are related to forward logistics processes. As a result, it is an easy extension of the existing 3PL business, creating a lot of value for your customers. This translates into profits. Since there is room for improvement at your customers operations, the emphasis will be on organized delivery of good Reverse Logistics services, not on price.

### Who Is Providing Reverse Logistics Services Now

While many 3PL's and Outsource service providers claim to provide Reverse Logistics Services, few are doing more than very basic receiving of a small volume of returned goods. There are several companies that have specialized in handling returned goods. Many of these companies appear to be very successful and growing.

### Key Messages for The CEOs Of Outsourced Logistics Providers

Reverse Logistics is a significant strategic opportunity for your company:

- A new value added revenue source of transaction fees and storage fees
- A large number of clients with a big need and a lot of pain - manufacturers and retailers struggle with handling Returns and viewing them as a non-strategic part of their business
- Within your capabilities - complementary processes to many of the forward logistics process and services you are performing today
- Low cost of entry since you can utilize existing facilities and staff
- Profitable customers - ALL retailers and manufacturers have to deal with returns - with so many that need help it is easier to target the ones where you can make the largest financial impact for them (such as high volume, high value returned goods)
- Few Competitors - there are few competitors providing sophisticated Reverse Logistics Services. This translates into better margins.

