

# IN SEARCH OF GREATER PROFITS



At a time when businesses are exploring almost every option to help them stay profitable, many are ignoring the big gains that can be made by tackling grey market trading, says Richard Bergner.



In these challenging economic times, one preoccupation dominates business owners' minds: how to increase their bottom line. Some cut back on spending; others close down operations to reduce overhead and labour costs. But there is one solution that most corporations overlook, which could potentially increase their bottom line by millions of dollars.

The process does not entail the tightening of corporate belts, but rather the closer scrutiny of a company's supply chain and a willingness to engage in any action needed to ensure that merchandise is not being diverted for sale to grey markets.

In late 2008, a global healthcare company doing large amounts of business in Africa and the Middle East was unaware that large amounts of its products were being 'U-boated.' In other words, the merchandise was not leaving the US; instead, it was being diverted by distributors for grey market sales.

After Professional Investigating & Consulting Agency investigators identified the redirected product, which amounted to \$10 million over several years, the healthcare company took action to stop the activity. It quickly saw its domestic sales soar by \$3.0 million as a direct result.

Product diversion carves out an enormous portion of commerce and trade around the globe, and it is growing at an ever-increasing rate.

Third parties undercut a company's price for a product and then harvest gigantic profits in the process. It's going on everywhere, from the local auto parts dealer to the superstore chain down the block, and it includes all manner of goods, from brand-name batteries to band instruments.

In the US alone, diverted products are estimated to account for tens of billions of dollars in sales annually. Virtually every manufacturer faces the potential of lost sales, tarnished reputations and ill will from customers due to products sold through illicit trade chains.

The bad news is that many manufacturers are oblivious to what is going on and the fact that millions of dollars, literally, can be squeezed out of their supply chains.

The good news is that it is also within reach of these corporates to adopt some best practices that will unearth the diverters and put a stop to this costly activity.

At a time when world economies are on a tumultuous roller coaster, the prospect of adding millions to corporate profits is an opportunity that should not be ignored.

Unfortunately, many companies do turn a blind eye to these practices. In part, this is because diversion is often a problem that has its roots firmly



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planted internally within an organisation. In other words, the perception is that the problem is due more to a manufacturer’s carelessness in terms of who they sell to, rather than “bad people doing bad things out there”. That can be a tough pill for company executives to swallow.

Also, because this practice may have been going on for so long, many manufacturers view the problem as a cost of doing business.

Another reason why corporates can be sluggish to react is the fact that product diversion is often not illegal, unless fraud is present. For instance, a retailer may sell off to a third party discounted products that it was unable to move from its store, without a manufacturer’s knowledge. But doing that does not break any laws.

One area where fraud can often be found, however, is where ‘ex works’ shipments are used. This is an agreement whereby the seller fulfills its contractual obligations when it delivers the goods to the buyer at its premises. Ex works basically relieves a seller of all other responsibilities. This agreement, however, does not necessarily serve the seller’s best interests, because it eliminates any control over the final destination of the merchandise.

Many diverters take advantage of the loopholes in ex works agreements. Goods meant for overseas emerging markets never leave the US, but instead, disappear into the ever-willing grey market.

Illicit traders have polished their practices since the old days of building networks through trade shows, word of mouth and ‘fax blast’ advertisements. The *modus operandi* for many diverters now is 21st century state-of-the art, high-tech and computer-driven.

With the ease of a mouse click, dozens of business-to-business online trading platforms provide instantaneous access to global commerce. These are legitimate websites, which can be, and are, easily used by counterfeiters, grey marketers or scam artists. Those seeking to sell merchandise outside

of authorised corporate channels don’t even have to leave their homes to do it.

This state of affairs in grey market enterprise is also about much more than lost profit and loss of trust from angry customers who may question why your company’s goods can be found cheaper elsewhere. It can be downright perilous, too.

These illicit trades have no pedigree or traceability history because they are unauthorised sales outside of the manufacturer’s supply chain. As products move around the world, they are often stored in unsanitary and dangerous environments. The products’ use-by dates may have expired or may even be counterfeit. In several instances, cell phones and laptop computers have exploded or burst into flames due to counterfeit batteries purchased through grey markets. And for medical patients, bogus medicines can be, and have been, deadly.

But manufacturers are by no means helpless in the battle to stop the theft of their merchandise from their supply chains. The best practices for your business to adopt include:

- Identifying weaknesses through a review of your channels from the point of manufacture to the point of loss of visibility
- Conducting due diligence investigations on new and existing customers
- Analysing incoterms being used and requiring proof of export on all ex works shipments
- Training key staff members to identify warning signs and to report them when apparent
- Investigating diverters to identify their supply chains and to cut off the sources of goods
- Implementing a strong anti-diversion programme and getting buy-in from the entire enterprise.

With the current economic conditions, the practice of product diversion has an eager multitude of distributors and retailers looking for ways to save money. Customers want brand names and quality products, and this feeds into the value that grey marketers can offer.

That’s why all businesses must be more diligent than ever to ferret out and stop the diversion of products from the supply chain. In the long run, the money saved will more than pay for the implementation of an anti-diversion strategy and the return on investment will be reflected in the bottom line.

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