
THE WALL STREET TRANSCRIPT

Questioning Market Leaders For Long Term Investors

Network Hardware Resale, LLC



CHARLES "CHUCK" SHELDON is CEO and co-Founder of Network Hardware Resale, LLC (NHR). Prior to its incorporation in 1996, he bought and sold used IBM computers and communications equipment as a part-time project while pursuing a political career as Mayor of Hermosa Beach, California. NHR now employs over 100 people in the United States and Europe, and has enjoyed over 36 consecutive quarters of growth and profitability. Prior to NHR, Mr. Sheldon had a varied career with IBM in marketing and sales management, as a business writer and real estate broker.

TWST: What is Network Hardware Resale?

Mr. Sheldon: Network Hardware Resale is the largest reseller of pre-owned Cisco in the world, with three offices worldwide and growing. Our headquarters is in Santa Barbara, California, as is our main warehouse facility. We have an office in the New York/New Jersey area and an office in Amsterdam, The Netherlands. We are currently investigating an office in Asia. Our value proposition is relatively simple. We provide enterprises, large and small, and service providers high-quality, pre-owned network equipment from the leading manufacturers — including Cisco Systems, Juniper Networks and Extreme Networks — at up to 95% off list price. We deliver most product overnight and all equipment comes with a standard one-year, advanced replacement warranty. We procure our inventory — which currently stands at around \$100 million, list price — from current or previous Cisco users that have excess equipment due to canceled projects, recent network upgrades, network outsourcing, mergers/acquisitions or downsizing. Our ability to purchase directly from our clients for cash or trade, and in any quantity, is another compelling reason our clients turn to us. About 40% of the hardware we purchase is unused in the original box. We have a staff of 30 professionals in the US and Europe, who test every single port, every single card, every single module,

run data and pass data through every chassis to ensure it is in good working and physical condition. If the equipment needs a little touching-up, say if it has a scratch, we will paint it. An important distinction between us and others, is that we are not in the fix-it business; we don't repair anything. Our experience tells us that a broken unit never performs the same and ultimately fails. We will not deal in that end of the market.

TWST: What is the competitive landscape at this point?

Mr. Sheldon: There are many competitors throughout the world; however, none are anywhere near our size. In 2004, we generated approximately \$80 million in revenue. What's interesting about our industry, though, is that our competitors are also our clients. About 20% of our business is done in what we call wholesale, which means we both sell to our competitors and we buy from our competitors in the instances when we do not have something we need in stock. When we buy hardware from our competitors/wholesale clients, we treat it in the exact same fashion as we do when we purchase from our retail clients. We assume nothing. We bring it in, we test it thoroughly, refurbish it as necessary, and usually turn it around the same day it arrives. So, in any case, we are able to fill the orders completely with the advantage of the general and wide community of dealers throughout the world.

TWST: What is the actual market space from the perspective of the universe of companies that may be expanding current capabilities with matching equipment that you could supply as opposed to the migration to new generations of equipment and technology?

Mr. Sheldon: A very good question. At Network Hardware Resale, we have the entire product line of mature to newer technologies/products available from Cisco, Juniper and Extreme. And, with some exceptions, we have most of the latest and greatest technologies/products available. If a product was announced by the manufacturer within the last three months, it is unlikely we would have it in inventory or be able to get it. However, anything beyond that is typically available on the secondary, or pre-owned, equipment market. We have tremendous product in stock. In Cisco, we have SUP 720s and 6509s and Fabric Enabled Gigabit and 10 Gig blades, and the latest GSR equipment including Engine 3 Gigabit and OC-48 cards. We have Juniper M160 chassis, M40E chassis and all interfaces up to OC-192 — all ready to ship. So it's somewhat of a misnomer, and understandably so, that one would expect us to only have older products. Of course, we have end-of-life products from all of the manufacturers, which we sell every day. Our clients — primarily network managers/engineers — aren't always looking to migrate to a newer technology every time Cisco or Juniper announces the latest and greatest box. Many are looking to extend their current network capabilities, buy what they are currently using, or "spare" their networks. In some cases, the products they are seeking — the 7200 series, 3640s, 6509s — are three and four years old or more. The savings is greatest, the older the hardware. However, our clients can still save somewhere between 30% to 50% on the latest technologies.

TWST: What is your agenda? What are your priorities for the next 12 to 24 months? What would make that time frame a success?

Mr. Sheldon: We are ramping up our sales force in Europe and the East Coast of the US. As I said, we are investigating opening an office in Asia and we continue to evaluate the opportunity to grow through acquisition. We are also contemplating expanding our product offerings over the next 12 to 24 months to include storage products. Our priority is to continue to ensure the highest quality product and client satisfaction. We believe the demand is out there. By our estimations, the second-hand, or pre-owned network equipment market is somewhere around \$2 billion per annum. That leaves a lot of room for growth.

TWST: What has been the funding history of Network Hardware?

Mr. Sheldon: We are self-funded and have no debt. We have a large credit line, which we use on occasion for large buy packages. We have, in the past, purchased several million-dollar packages at once. Our ready access to capital really separates us from most of our competitors.

TWST: Introduce us to your top-level management team, the leadership, and professional credentials you have. Are there areas there you're looking to add or augment?

Mr. Sheldon: This is a family-owned business. My two sons are in the business and they are my Sales Managers. Both Mike and John are experienced in all aspects of the business and share ownership with me. Our CFO, Karen Anne, is an MBA and a CPA with 10 years of auditing experience. She has been with the company for five years and is a very important cog in the management team. Rick Stevens is our VP, Marketing who brings over 20 years of marketing experience in the network industry, previously holding Senior management positions with such industry leaders as Nortel, Extreme and Alcatel. I also have a very competent and experienced seven-year employee, Glenn, who manages the Amsterdam office. The manager of our East Coast office, Julie, also rose up to management through the sales department. I have just employed a sales trainer, who I have charged with the responsibility of getting down to the real heart of great salesmanship and time management, and is on board right now. And I think over the next 24 months, we will probably add a second-level of management in Amsterdam. That operation now has some 30 people and it has two managers. We will probably add a manager there.

TWST: What are the sales and marketing channels that you have today and how will they continue to change and evolve?

Mr. Sheldon: We are a direct sales organization. All salesmen are charged with the responsibility of drilling down on potential network equipment users and they do that mostly over the phone. That model will continue; there's no reason to change it. We are, however, budgeting a significant amount of money this year and ongoing to visit more of our clients. Since we are a worldwide organization, we need to visit our clients more often and that will happen. We spend a lot of time on client visitations in Europe. You might be interested that in Europe we have approximately three nationals for every major country. It was an important priority for me when we opened the European office two-and-a-half years ago, that we have a French national selling into France, a German national selling into Germany, etc. We just hired our first salesmen to cover Scandinavia and Italy. We will continue to grow our sales force country-by-country based on the opportunity. In Europe, we see the greatest opportunity in the UK, more than all of the other countries combined in Europe.

TWST: Does this area of the industry have room for consolidation? Is that a valid growth channel or strategy?

Mr. Sheldon: I think there is going to be some consolidation and we are currently looking at some opportunities. Interestingly, until five years ago, this industry was dominated by maybe five to 10 dealers, including NHR. Today, there are likely thousands of very small dealers in the business. My guess is that consolidation will take place among the original 10. Consolidation is an interesting subject in this industry. I hearken back to what I said before; our competitors are also our clients. Frankly, I welcome the competition. I welcome a dealer who has something in inventory that I don't have, that I can buy

to fill orders for my own clients. I believe most feel the same way. Our business has benefited from competition, not suffered.

TWST: From the client's perspective, is this strategy then to look for a one-stop shop type of supplier where they can find a full panorama of equipment or are they generally looking to fill a specific need?

Mr. Sheldon: Good question. That really depends on the client. For certain of our small- to medium-sized clients, we are their one-stop source for equipment. For our larger enterprise or service provider clients, we complement their existing Cisco relationships. These organizations purchase from Network Hardware because they can realize significant savings without sacrificing quality, performance or service. In addition, most of the original equipment manufacturers often have long lead times of six to eight weeks, on average. NHR can deliver most products overnight. That obviates price in most cases. Many of our Fortune 1000 clients initially turned to us for this reason. Over time, we have moved these relationships along to handle more of their needs.

TWST: Is this simply a US focused market for you? Is it a global market? What are the opportunities and can you address them?

Mr. Sheldon: Today, the US represents about 60% of our business. Outside of the US, most of our business is in Europe. We see enormous growth opportunities in all locations, but particularly in Europe. As I said, by the end of this year or early next year, we expect to have a full operation in Asia. We already generate several millions of dollars a year in Asia — all by e-mail. Once we have a presence there and we hire nationals who can understand the culture and the language of specific countries, we expect this office to be a significant contributor. We firmly believe that our ability to grow and to grow profitably is only constrained by management talent. We need to make sure that our span of control and controls in general are in place before we expand. It is the death knell of many businesses. They expand too quickly without the controls and management talent in place. As long as I'm careful about that, I believe the opportunity is unlimited.

TWST: Companies that say they are going into Asia or mention China, historically it takes some kind of relationship or partnership in the local area to be a success. How have you approached the opportunities there? Is there a timetable for your development in China or in the broader Asia marketplace?

Mr. Sheldon: I think you have to separate China from the rest of Asia in answering that question. We do not believe there is a business model difference in the way we do business in Korea, Taiwan, Japan, Malaysia or Australia and our experience there has been very positive. Our initial focus in Asia will not be China. However, over time — and as we understand the market better — we might consider a presence in China. Our strategy is not to begin there. There are many other powerful countries in Asia that already welcome our value proposition. When and if we move into China, it will likely be through a partnership. But it is not my first priority.

TWST: What would be a value add that Network Hardware Resale provides on the refurbishment and testing? Do you tend to upgrade at all?

Mr. Sheldon: In the hardware arena, we regularly upgrade power supplies, modules, memory, etc. However, we do not upgrade and will not touch the software. The software that comes on a chassis goes out with the chassis. We never attempt to convince a client to buy anything other than what he wants to buy because he cannot accomplish what he wants to buy within the second-hand market. Our clients are not getting a lesser configuration or making some kind of compromise or sacrifice by doing business with us. We are, in almost all cases, providing them exactly the configuration that they want and need.

TWST: Thank you.

CHARLES "CHUCK" SHELDON

President & CEO

Network Hardware Resale, LLC

26 Castilian Drive, Suite A

Santa Barbara, CA 93117

(805) 964-9975

(800) 451-3407 - TOLL FREE

(805) 964-9405 - FAX

www.networkhardware.com

Corporate Profile

Network Hardware Resale

Corporate Headquarters
26 Castilian Drive, Suite A
Santa Barbara, CA 93117

Phone: (800) 451-3407
Fax: (805) 964-9405
Web: networkhardware.com

Corporate Officers

Chuck Sheldon
President & CEO

John Sheldon
Vice President, Sales

Mike Sheldon
Vice President, Sales

Karen Anne Platt, CPA
Chief Financial Officer

Glenn Fassett
General Manager, Europe

Rick Stevens
Vice President, Marketing

Bryan Siever,
Vice President, Sales Development

John Ready
Warehouse Manager

Network Hardware Resale is the World's Leading Provider of Pre-owned, Used and Refurbished Cisco

Network Hardware Resale (NHR) was formed in 1986 by former IBM-executive and Hermosa Beach, California mayor, Chuck Sheldon. In the early 1990's, Chuck and his son John, decided to re-orient the business to focus exclusively on pre-owned, used and refurbished networking equipment - principally from Cisco. The duo - now regarded as pioneers of the secondary Cisco equipment market - soon saw their business skyrocket.

Today, NHR is the world's leading provider of pre-owned, used and refurbished Cisco, Juniper and Extreme. Over 4000 organizations worldwide, including the Global 1000, small and medium enterprises, service providers and government entities, have turned to NHR for high-quality, reliable networking equipment.

5-Star Quality

INTEGRITY

NHR has operated successfully for nearly 20 years by offering our clients a trusted, reliable, and knowledgeable resource for high quality networking solutions. We conduct our business ethically and fairly, which is why our clients and resale partners turn to us first.

QUALITY

NHR guarantees the highest-quality product. Our technical team physically inspects and rigorously tests every piece of equipment that we sell in our own state-of-the-art testing facility. Prior to shipment, all products are re-tested and packaged with static-free materials in sturdy, custom boxes. NHR products are guaranteed to arrive in excellent physical and working condition with valid serial numbers.

GUARANTEE

NHR offers its retail end-users added comfort by offering a standard one-year warranty* on all products sold by NHR. Under NHR's warranty program, overnight advanced replacement and ongoing technical support from certified technicians come standard with every piece of equipment.

EXPERIENCE

NHR is the leader in pre-owned and used CISCO equipment; you will not find a more knowledgeable resource in the secondary networking

equipment market. Our A+ and CISCO-certified technical support staff including certified technicians, are available to answer your product-related questions or help you troubleshoot your network. Call or email us with your questions and we will return your query no later than the next business day.

SERVICE

NHR believes that we are only as good as our ability to deliver for you. That's why we are constantly looking for ways to better serve our customers before and after the sale. We continue to introduce value-added programs / services in step with our clients ever-changing needs, including equipment buy-back programs, leasing services, and IT consulting / network integration services. To learn more about these services, contact a sales representative today.

Online searching, ordering, and tracking made easy with networkhardware.com

Whether you're researching information on the overall secondary networking equipment market, on current generation, hard-to-find or end-of-life Cisco routers or switches, finding information has never been easier at networkhardware.com thanks to intuitive navigation and design. Browse through NHR's vast online product catalog, add items to a quote cart and submit a request for quote on individual products or components or product bundles; average response time is under 24 hours. You can even submit a bid to sell your own equipment. Networkhardware.com, offers an online account management feature that allows NHR clients to view recent orders and track packages online. NHR clients can also contact sales and technical support directly through the site.

Key destinations on NHR website:

Why buy pre-owned Cisco?:

www.networkhardware.com/WhyBuyPreOwned.aspx

NHR Value proposition:

www.networkhardware.com/ValueProposition.aspx

NHR Quality Assurance:

www.networkhardware.com/quality.aspx

Product Guarantee, One-year Standard Warranty:

www.networkhardware.com/PoliciesAndWarranty.aspx#Warranty

Pre-owned Cisco Products:

www.networkhardware.com/Cisco.aspx

Request a Quote:

www.networkhardware.com/RequestQuote.aspx

Sell Your Equipment:

www.networkhardware.com/WeBuy.aspx