Mailers Hub News

August Summary *From the August 14 and 28 issues*

PQ III Results Noteworthy for the Wrong Reasons

After the Board of Governors met on August 8, the Postal Service released its *Form 10-Q*, reporting the results for the third quarter of fiscal 2023 (April-June). Continuing the trend of the year's first two quarters, PQ III volume and revenue fell while Postal Service leadership tried to divert attention by citing "progress" in implementing the Postmaster General's 10-Year Plan.

Despite price increases totaling over 10.7% since the end of June 2022, operating revenue continued to decline: down nearly 0.90% for PQ III and 0.75% for FY 2023 to date. The $1.736 billion net loss for PQ III brought the total loss for the fiscal year to $5.244 billion, not the results expected by the PMG's Plan.

Volume loss also continued for the quarter as ratepayers with the ability to move out of the mail exercised that option. The USPS stated that the loss of First-Class Mail volume was caused by "the on-going migration from mail to electronic communication and transaction alternatives," never acknowledging that climbing postage costs may be accelerating the trend.

The volume loss of high-contribution First-Class Mail was modest compared to the plunge in Marketing Mail; long the largest class of mail by volume, Marketing Mail shrank by 2.5 billion pieces compared to PQ III the previous year. Though it may not yield the greatest revenue per piece, Marketing Mail nonetheless provides the volume – pieces per stop – that strongly supports six-day delivery.

Meanwhile, competitive product volume has stagnated, despite predictions of growth in the PMG's Plan, and so is failing to provide the revenue needed to offset the loss of Market-Dominant mail.

In stark contrast to the downward trend in revenue, the trend in expenses continued upward. Compensation and benefits costs grew by 3.05% and, though transportation expense moderated, the bottom line was hurt by an adverse shift in the workers compensation liability, resulting in a 9.63% net increase in expenses. For the year to date, total operating expenses are up 9.91%.

Commenting on the increase in compensation costs, the USPS stated it was "primarily due to contractual wage increases, which include the inflationary impacts on related COLA." In other words, the problem is of its own making. Under current Deputy PMG and Chief HR Officer Doug Tulino, who's part of the leadership team bemoaning cost increases, the Postal Service has repeatedly failed to control cost escalation by continuing decades-old patterns of wage growth and, most problematically, the periodic cost-of-living increases that are unique to USPS labor agreements.

Coupled with the PMG's commitment to increasing the comparatively more expensive career workforce, and his reluctance to irritate the labor unions by reducing complement, it's difficult to understand how the agency will achieve cost reductions on the scale anticipated by the PMG's Plan.

Most puzzling is how DeJoy continues to expect more revenue from Market-Dominant products by simply maximizing price increases twice per year. As is becoming obvious in the Postal Service's own figures, any benefit of price increases is increasingly being offset by volume loss. While pieces remaining in the mail each might be yielding more revenue, the decrease in volume is pushing total revenue downward faster. Even if we were to accept DeJoy's attribution of decreased Marketing Mail volume to "on-going migration," it would seem logical to accordingly not further discourage investing in direct mail by hiking postage higher.

Meanwhile, for a group of allegedly sharp and independent business people, the governors have remained blindly submissive to DeJoy, regardless of reality, lulled into cooperation by the party line spoon-fed them by USPS management, and fully indifferent to any outside facts or perspectives.

USPS Requests PRC to Authorize Growth Incentives

The irony may not be lost on anyone. Even as the Postmaster General remains stubbornly committed to volume-killing semi-annual price increases, the Postal Service has asked the Postal Regulatory Commission to approve a proposed "growth incentive" for both First-Class Mail and Marketing Mail.

Filed August 11 as Docket R2023-3 (*First-Class Mail Growth Incentive and Marketing Mail Growth Incentive*), the proposal borrows from prior volume-based incentives and would reward mail owners who produce more mail in 2024 than in 2023. As the USPS stated in its filing:

> "The two incentives are substantially identical. A mailer is eligible for the First-Class Mail Growth Incentive when its combined volume of qualifying pieces in the incentive period, calendar year 2024, exceed the incentive threshold. Qualifying

> pieces are pieces mailed as First-Class Mail Presort Letters, First-Class Mail Presort Cards, or First-Class Mail Presort Flats.
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> "Similarly, a mailer is eligible for the Marketing Mail Growth Incentive when its combined volume of qualifying pieces in calendar year 2024 exceed the incentive threshold. Qualifying pieces are pieces mailed as Marketing Mail Letters and High Density/Saturation Letters, Marketing Mail Flats and High Density/Saturation Flats & Parcels, Marketing Mail Carrier Route, or Marketing Mail Parcels.
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> "Under both incentives, for every qualifying piece mailed in calendar year 2024 after the first million pieces, mailers receive a credit equal to 30 percent of the average per-piece price paid for mailing all qualifying pieces, unless the volume of qualifying pieces the mailer sent in the preceding fiscal year exceeded 1,000,000 pieces. In that case, credits accrue only after the mailer surpasses its fiscal year 2023 volume of qualifying pieces."

If approved, the "intended effective dates of both incentives is January 1, 2024, and the promotion – the incentive period – runs through December 31, 2024." While it's good that the USPS is trying to encourage growth, the PMG is also promising rate increases in January and July of 2024 and beyond. Giving vitamins to someone you're also starving would be similar, and equally contradictory.

USPS Files for Market-Dominant NSA

Late on Friday, August 11, the Postal Service submitted a request to the Postal Regulatory Commission seeking approval for a negotiated service agreement with Publishers Clearing House. Though the USPS files NSA requests many times a week, the August 11 filing was different in that it was for market-dominant mail, not competitive products as is typical. According to the USPS filing:

> "The PCH NSA is designed to give PCH a discounted initial mailing of one million pieces of USPS Marketing Mail letters, mailed at cost. This initial mailing is limited to one million dormant prospecting customer addresses, which PCH has not mailed to within the past three months. In exchange for these discounts, PCH has committed to certain performance targets for follow-on mailings, both from PCH to the addresses of this million piece mailing and to PCH from the addresses of this million piece mailing, that are expected to result from the initial mailing, also known as a 'multiplier effect.' PCH expects two million pieces will result from the initial mailing, mailed at published rates, within nine months of the date of the initial mailing. ..."

Proposed NSAs are filed by the USPS for review by the PRC. Generally, in order to approve an NSA, the PRC must conclude that its terms are beneficial to the USPS, such as by reducing costs and/or generating new volume and revenue. Most NSAs – thousands of them – have been for mailings of competitive products, such as Priority Mail or ground packages, and offered discounted prices in exchange for the ratepayer's shipping business; hundreds remain in effect.

By contrast, there has never been more than a handful of NSAs for market-dominant products (First-Class Mail and/or Marketing Mail), including agreements with Bank of America, Bradford Group, Bookspan, HSBC North America, Discover Financial Services, and PHI Acquisitions. Most expired over a decade ago; the last was PHI's that ended in 2018.

Like a competitive product NSA, a market-dominant NSA offers reduced prices or other benefits in exchange for volume commitments, such as by reaching or exceeding volume targets. However, it's been difficult for the Postal Service to overcome the PRC's "anyhow" bias, i.e., that the USPS is offering an incentive for market-dominant mail that would have been sent anyway, even without the discounted price.

The first indication of the commission's approach was not encouraging. In a four page "chairman's information request" filed August 23, the Postal Service was asked to obtain and supply details about PCH's marketing and advertising activity as well as its own data about the proposed and other potential NSAs.

The commission also questioned the Postal Service's statement that it would "consider NSAs on comparable terms to similarly situated mailers." Particularly, the PRC asked for "an analysis of 'similarly situated mailers' detailing the number of mailers that could possibly qualify and the estimated volumes for those mailers," as well as how NSAs with other "similarly situated mailers" would yield the "multiplier effect" mentioned by the USPS in support of the PCH NSA.

To many observers, the chairman's information request was an indication that the PRC remains unpersuaded that the mailings under the NSA eventually wouldn't have been prepared anyway. How either the Postal Service or PCH could dispel such a conviction isn't clear – there's no possible evidentiary answer to a hypothetical presupposition. Similarly unclear is whether the commission believes that, absent such proof, the NSA shouldn't be approved because, presumably, the mail would have been sent anyway even without a discount.

If so, it would reinforce the belief held by many in the commercial mailing industry that the PRC is less interested in exploring new ways to build (or preserve) mail volume than it is in preventing unjustified discounts and protecting the USPS from any level of financial risk. The USPS had taken pains to include provisions in the NSA to minimize such exposure that, even at its worst, would be reimbursed by PCH.

As noted, if the PRC disapproves the PCH NSA because its can't be disproven that the mailings would have occurred anyway, it would fatally discourage any future market-dominant NSAs and reinforce the Postal Service's reticence to explore innovative ways to sustain market-dominant volume. Similarly reinforced would be perceptions of the PRC as overly-cautious and bureaucratic, focused more on inflexibly applying its rules than on finding solutions to accommodate creative proposals.

GCA, USPS, Differ Over Information Request

In an August 14 filing with the Postal Regulatory Commission, the Greeting Card Association moved for the issuance of an official information request as part of the *Public Inquiry on Changes Associated with the Delivering For America Plan* (Docket No. PI2023-4). The GCA explained the reasons for its motion:

> "The DfA plan depends pervasively on certain projections. ... It postulates that by 2030 market dominant mail volume will decline by 37 percent and package volume will increase by about seven percent. The plans for reconfiguring processing, transportation, and delivery facilities and operations necessarily conform to these projections. At a finer level of detail, the DfA report (p. 42) states that the projected decline in market-dominant mail will result from substitution of electronic media for physical mail, and that the presumed rate of substitution is consistent with what the Postal Service has observed over the last decade. Why the same trend should be expected to continue is not discussed.
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> "Nowhere in the report are the assumptions, methods, and data sources underlying these projections disclosed.
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> "It is GCA's view that unless these projections are fully explained and the reasoning governing them made clear, the entire DfA plan cannot be evaluated. Not all aspects of the plan can be expected to come before the Commission in an advisory opinion case ... . Consequently, the projections should be explained and justified in this proceeding. ..."

As would be expected, the Postal Service promptly objected, claiming in a lawyerly August 17 response that

> "... GCA's Motion should be denied on the bases that the information requested is outside the stated purpose of these proceedings, would not advance a legitimate regulatory objective within the scope of the Commission's authority, unjustifiably intrudes on Postal Service managerial independence, and impermissibly seeks to revisit previously rejected arguments for regulating market dominant rates. ..."

The current docket was opened April 20 as a simple "inquiry" about The Plan, and not to render an advisory opinion or rule on any element of The Plan. The Postal Service did not appreciate the PRC's action or the visibility that it would provide, stating in a 33-page May 5 motion for reconsideration that the commission's order opening the docket

> "... fails to identify a statutory basis that would establish the Commission's authority for this unprecedented level of review and oversight. No such basis was identified because no such basis exists. ..."

Despite the Postal Service's overwrought outrage that the PRC would be so bold as to question The Plan, the commission rejected the USPS motion on June 21, stating that

> "As an initial matter, the Commission finds that the Postal Service's Motion is premature. The Commission has merely opened a docket, creating a forum to learn more about strategic plan initiatives that may have a significant impact on the postal community. ..."

Since then, as statutorily required, the USPS has followed the process for rate increases and has sought advisory opinions (which it has ignored) where mandated. Otherwise, the agency has been clever, framing The Plan as simply "a broad guiding vision" – nothing warranting PRC review – and has pursued each initiative included in The Plan individually.

In doing so, the USPS has sought to avoid having The Plan reviewed as a whole, as the GCA now wants done. In an upcoming decision, the PRC will decide whether the Postal Service's strategy to avoid transparency is succeeding.

Another Plan for Flats

The efficient processing of flat-shaped mail has been a goal that has chronically eluded the Postal Service. Installing a fleet of $100 million flats sequencing system machines exemplifies a once-favored strategy that failed to delivery expected results, arguably because of a conflict of institutional policy. Unfortunately, not long after the decision to purchase the FSS fleet, the USPS began to implement sharp increases in the rates for flats to improve cost coverage. The resulting decrease in flat mail volume soon upset the assumptions underlying the FSS purchase. Other strategies, such as programs to reduce bundle breakage and changes in containerization options, also yielded limited benefit.

In another effort to force development of effective flats processing methods, Congress included a provision in the Postal Service Reform Act of 2022 to require the USPS to:

> "(a) develop and implement a plan to remedy each inefficiency identified in the [Postal Regulatory Commission's] Flats Study ... ; and (b) if the Postal Service determines that remedying any such inefficiency is not practicable, provide an explanation why remedying such inefficiency is not practicable, including whether it may become practicable to remedy such inefficiency at a later date ... ."

Accordingly, on August 15, the USPS released its draft Postal Service Flats Plan Pursuant to Section 206 of the Postal Service Reform Act of 2022. The 28-page document, repeatedly invoking the Postmaster General's 10-Year Plan, reviews the past and present challenges of flats processing and outlines the latest efficiency and productivity improvements being implemented.

The availability of the document, and the opportunity for public comment, were noticed in the August 16 *Federal Register*. The document itself is available from the USPS at https://about.usps.com/psra-flats-study/usps-flats-plan.pdf. Written comments, including the name and address of the commenter, can be mailed to: Chief Counsel, Global Business & Service Development, Office of General Counsel, 475 L'Enfant Plaza SW, Washington, DC 20260–1135, or emailed to PCFederalRegister@usps.gov with the subject line "Flats Plan."

CPI watch

The release of the July CPI by the Bureau of Labor Statistics leaves only one more (the August CPI, on September 13) before the Postal Service finalizes its calculations for the next price filing, expected in early October, to be effective in January 2024.

After five of the six months between filings, the Postal Service's calculated CPI-based rate authority stands at 1.653%. The month-over-month change had been slowing until a slight uptick in July, but the trend still points to a figure after the August CPI in the 1.9%-2.0% range. The USPS had previously estimated it would have about 2% of pricing authority for the October filing.

The "adders" for "density," "retirement," and "non-compensatory" will not be available for the October filing, but are expected to significantly increase the subsequent filing expected in April 2024, for implementation in July 2024.