

The Challenge for the Presidential Commission

By

Michael J. Riley¹

“The Commission's objective is to advise the President on the state of the United States Postal Service, prepare a report articulating a vision for the future of the United States Postal Service, and recommend the legislative and administrative steps necessary to enact reform needed to ensure the viability of postal services.”

In fulfilling its mission the Commission should examine what happened to the U S Postal Service during the period 1993 through 1998. This was a period during which the Postal Service thrived financially and accomplished many of the objectives that now seem to be articulated for the future. It made sizeable profits. The Service reduced its debt significantly, and thereby was able to achieve debt levels well below its borrowing ceiling. Measures of customer satisfaction grew and were extremely high. Investment in plant and equipment rose while the accumulated deficit since postal reorganization declined significantly. Actions were taken to improve employee morale by eliminating problems.

The lesson should be learned that a change in the law is not required to permit the Postal Service to thrive and prosper.

Perhaps as the Commission explores this successful time period it can learn from it and recommend changes that will allow the same success to occur in the future. It can also take note that this success occurred with the existing legislation but with a significant departure in the mindset of the management team and eventually with the Board of Governors. Perhaps the Commission will also take note of some other key measures that currently fascinate many people and realize that these are the measures that caused significant harm to the Postal Service and resulted in poor service, inadequate facilities, and financial distress.

This paper is divided into 5 sections: I. Run it Like a Business, II. Good Results in the Mid-1990s, III. Nine Successful Strategies and Tactics, IV. Successful Strategies and Tactics Abandoned, V. Failed Policies and Counterproductive Claims, and VI. Recommendations. I believe that this Commission can confine its recommendations to merely administrative changes as legislative changes often become enmeshed in areas that change more than originally desired.

I offer these observations for the Commission's consideration so that it can fulfill its mission and ***“recommend the legislative and administrative steps necessary to enact reform needed to ensure the viability of postal services”***. That is the challenge.

¹ Michael Riley was CFO of the Postal Service from August 1993 to July 1998. Previously he held positions as CFO of Lee Enterprises, a newspaper and TV company, and CFO of United Airlines. He is President of Riley Associates LLC and a Professor at the University of Maryland University College. Riley earned his Doctor of Business Administration degree from Harvard University.

I. Run it Like a Business

The management of the Postal Service in the mid to late 1990's not only claimed to run it like a business -- the Postal Service, in fact, did run like a business. Financial business decisions were made with the longer term in mind and ultimately the Board of Governors adopted a policy that virtually assured financial health. Unfortunately, by the late 1990's those policies were abandoned and with them went the profits, the low level of debt, and the high customer satisfaction ratings. Interestingly at the same time that the Postal Service headed downhill, measures which had been erroneously used to measure progress such as Total Factor Productivity (TFP) once again began to rise, output per work hour again began to increase and the total number of employees began to decrease. Perhaps conventional wisdom regarding these measures as control objectives are WRONG and prudent planning for the future should learn from what has worked at the Postal Service in the past.

Because TFP measures only inputs and outputs, it does not deal with changes in service levels. In 1993, the gain in TFP was very high as service deteriorated dramatically. TFP does not reasonably allow for the time lag and learning curve of capital investments that require system changes. TFP is simply one measure out of many possible measures. A good business plan, not TFP, should drive business decisions.

There is no impediment in the current law to producing good results. The Postal Service can have profits, debt reduction, very high customer satisfaction among the people who receive mail, and strong and improving employee morale.

II. Good Results in the Mid-1990s

Commenting from the prospective of the Chief Financial Officer during most of Marvin Runyon's term as Postmaster General, I can attest to what is and was important. The record of the Postal Service under Mr. Runyon was outstanding: He turned losses into strong net incomes after just two years. The Postal Service reduced debt and undertook initiatives to improve productivity (not necessarily total factor productivity) through automation, to improve customer satisfaction, and to better manage employees.

The table below shows the results of these actions upon net income through the end of the third quarter of 1998 when Mr. Runyon stepped down as Postmaster General. Also, the full year 1998 is included. The difference of just one quarter indicates how quickly poor financial performance can drag down net income and adversely affect other key areas such as the level of debt:

Dollars in Billions

Year	Profit or (Loss)
1993	(1.8)
1994	(0.9)
1995	1.8
1996	1.6
1997	1.3
1998 YTD Q-3	1.4
1998	0.6

At the same time, debt was reduced dramatically:

Dollars in Billions

Year	Total Debt
1992	9.9
1993	9.7
1994	9.0
1995	7.3
1996	5.9
1997	5.9
1998	6.4

It should be noted that if the Postal Service had ended the year in 1998 with earnings of \$1.4 billion, it would have further reduced debt to \$5.6 billion.

The Postal Service accomplished this with a price increase of ten percent in January 1995, just 3 months into its fiscal year. It had been four years since the last price increase, which had been delayed too long. And, despite the size of the increase, it was well below inflation. One of the lessons learned is that delaying rate increases to gain mailer approval typically only causes later increases to be larger and less predictable. It also results in an increase in the size of accumulated losses and can often cause increased pressure for debt to be increased as well.

Mr. Runyon's objective was to run the Postal Service like a business. His recovery plan included an incentive system, debt reduction and restructuring, measuring and rewarding customer satisfaction, employee evaluation of their management, and strong controls. His overall first priority was profits.

III. Nine Successful Tactics & Strategies

The strategies that brought success were innovative and creative, but well known. In general they were the following: Cost Controls rather than cost reduction, Incentives rather than intimidation, Profits rather than break even, Debt Reduction by increasing rates in a timely fashion, Wise Capital Spending rather than spending freezes, Boosting Employee Morale rather than employee bashing, Adding Experienced Business Executives where appropriate, Price Increases when needed, and Customer Satisfaction Initiatives rather than reducing lobby hours and attempting to go to five day delivery. Of these, the most important are and were a focus on **Profits, Customer Satisfaction, and Employee Morale.**

Cost Controls:

Mr. Runyon joined the Postal Service in May 1992 and studied the situation for a short period before taking action. He realigned management, reducing about 23,000 jobs and offered early retirement that was accepted by 48,000 people. He cut the number of Vice-Presidents in half and brought in a number of new Officers from the business community. He retained only 6 of 42 Vice-Presidents. The heads of Quality, Purchasing, Facilities, Strategic Planning, Marketing and Finance were hired from "outside." The goal was to take a reduction deep

enough to eliminate all of the pain in one action and to learn from the results. There were continual evaluations and many positions were added back later.

The number of employees was capped not frozen. Hiring above the cap was possible but required specific approval from Headquarters. Major spending was similarly constrained, but each Postmaster and Plant Manager received credit cards allowing them to purchase up to \$10,000 in capital equipment and \$10,000 in expenses at any one purchase. Many supervisors were also issued cards. The floor for capitalizing equipment was raised from \$1,000 to \$5,000. In short the focus was shifted away from what one senior executive called “travel, training and toilet paper” as a way to save money. We allowed managers discretion in doing what was needed, but kept control of significant spending. We used smart incentives to guide managers’ behavior.

Each officer and executive was asked to sign two letters. One attested to the correctness of the accounting statements within their control and another acknowledged their fiduciary responsibilities for the future.

Unlike prior practices Area (Operating) Vice Presidents and executives at Districts and Headquarters were promised that if they under-spent their budgets they would get the money back the following year. The “use it or lose it” philosophy was abandoned.

Incentives:

Stern Stewart was engaged to customize and implement their trade marked Economic Value Incentive (EVA) System including a “banking” provision to create long-term positive results in February of 1994. A scaled down version, hurriedly was prepared by 4 Postal executives and implemented in March of 1994 as a reaction to 6 months of poor financial results. The Postal Rate Commission (PRC) predicted that the Postal Service would lose \$2.5 billion in fiscal 1994. Instead results turned to “better than budget” by April 1994 and the Postal Service lost “only” \$913 million. It beat its budget by over \$300 million and the PRC’s April estimate by \$1.5 billion in fiscal 1994.

The incentives used EVA and positive change in EVA to set the amount of the immediately available payments and the addition to the long-term “bank.” There were 3 items that were measured: EVA, Employee evaluations of their managers and Customer Satisfaction as measured by surveys. There were provisions to deny payment to bad performers and after the first year, payments were contingent upon the Postal Service earning a net income.

Profits:

The Board of Governors were asked to approve a resolution requiring that the Postal Service plan to earn profits each year. These profits were to be used to pay down debt, recover prior years losses, provide a cushion against emergencies, and fund expanded capital spending for automation, replacing old facilities and building new Post Offices in new communities. The resolution required management to file a rate increase request with the Postal Rate Commission whenever Profits were likely to drop below the \$900 million level, the level of prior years loss recovery from the 1994 rate case.

Survey results revealed that the majority of senior career Postal executives thought that profits were inappropriate for the Postal Service. We undertook an education campaign to explain the need for profits and the legal requirement for a contingency that could only be met by earning profits. Many were surprised to learn that the ratemaking process provided for prior years loss recovery, contingencies to cover emergencies and certain non-expense items such as paying off debt. The Board resolution was an important part of this program because it signified the Board's commitment.

Debt Reduction:

The Board of Governors was asked to pass another resolution calling for the continued reduction in total debt. At the same time the Postal Service, with Board approval, implemented a complete restructuring of debt and cash management.

The U. S. Treasury adopted dramatic change in the methods it used to fund the Postal Service's needs allowing the savings of hundreds of millions of dollars. This action eliminated the need for a Postal Service request to borrow from U. S. financial markets. It allowed the Postal Service to have a same day line of credit of \$300 million and a \$3 billion line of short-term debt with 48 hours notice. Previously, the Postal Service used long-term borrowings at high rates to meet short-term needs.

Employee Morale:

Management believed that it was important to pay market-based wages. In 1994, we determined that the Postal Service paid wages at rates above market especially in rural areas of the country. This was addressed in the 1994/1995 labor negotiations. The 1995 labor arbitration provided for lump sum payments and a combination of cost of living and base rate increases that increased wage levels by 4 percent over 4 years. By 1997, our internal data showed that wage levels were at or below market in urban environments. I personally helped Operations Vice Presidents get increases to starting wages when the Postal Service proved unable to attract and hire qualified people.

Surveys were taken regularly (roughly once each year) to determine employee evaluations of managers. Efforts were begun to address the two major complaints from employees: the lack of negative consequences for problem employees and the lack of reward for good results. Managers scoring poorly were counseled and given training and/or re-assignment. The Board of Governors received regular reports regarding these activities.

It was our belief that business success required good employee morale. This was especially true for the one arm of the U. S. Government that touches everyone in the country 6 days a week. The primary factor was the approach of management. Managers and national programs need to be attuned to listening to employees, solving their problems, and improving working conditions. Also, we began a program to replace and/or rehab older facilities, some of which were in horrible shape as a reaction to valid employee complaints.

Customer Satisfaction:

Customer Satisfaction surveys were conducted regularly and a number of initiatives started to make the Postal Service more convenient. Many of these actions **reduced productivity** as hours were extended and counter people were added to reduce line wait. The

concept of the “Postal Store” was started to let the customer use self-service for purchasing commemorative stamps and other merchandise. Employees were added in operations to eliminate processing bottlenecks.

Finance implemented the deployment of 60,000 terminals that accepted credit, debit, and ATM cards as a convenience for customers. It proved to be a very popular program as it eliminated a source of annoyance for employees and customers alike although it required an increase in expenditures.

Research has shown that the key to the long-term success of the U. S. Postal Service has been over 200 years of strong customer satisfaction. In 1993 and 1994, Congress held hearings and numbers of its members called and visited the Postal Service to stress the importance of satisfying their constituents. Service declines in 1993 led to angry town hall meetings in Chicago and the suburbs of Washington.

Customer satisfaction involves dependable mail delivery. It also means having Post Offices available everywhere; having short line waits; as well as being open when people want to mail packages, certified mail, and letters; and providing secure reliable delivery. It means safeguarding the mail with the Postal Inspection Service. It means trust, safety, reliability, and secure mailboxes to prevent identity theft. It also means delivery six days each week and pick up of mail from businesses and public drop boxes at the end of the business day. Marketing surveys show that the Postal Service has one of the strongest brands in the country and that the U. S. population likes the service that it gets.

The U. S. Postal Service compares favorably with the Posts of most major countries in terms of service, safety, security, trust and efficiency. In annual negotiations at the Universal Postal Union in Bern, Switzerland, about fees for the exchange of mail, we had frequent, positive comments about the trust and the public support that the U. S. Postal System enjoyed. In another example, Mr. Runyon and I personally hosted a delegation of 8 representatives of Japan’s Post when they visited to learn how the U. S. Postal Service could have such strong customer satisfaction and a stamp price of 32 cents compared to their 80-cent equivalent price for a First-class letter.

Wise Capital Spending:

The Postal Service had been scrimping on capital spending for its entire life. By focusing excessively on short term cost reductions while absorbing costs that Congress continued to legislate, it allowed facilities to deteriorate and the infrastructure to become outdated. We increased the Capital Budget and asked the Board of Governors to commit to earning profits to pay for the needed spending. Money was included to build Post Offices in new communities around the country, an upgrade of the computer network and communication system, and even the introduction of robotics.

Adding Key Business Executives:

One key element of success was recruiting and hiring experienced business executives and officers from the private sector. They brought a different prospective that added to the experience base and allowed the Postal Service to prosper.

Career Postal people are bright, hard working capable individuals. However, they frequently lack business experience in profit making enterprises. The Postal Service has had losses in more years than profits. The team that was created by combining the experience of career people with the new business perspectives had great success. Of course, the vast majority of executives were career employees and they were very strong.

Price Increases:

The Postal Service needs small regular price increases.

There were and are conflicting pressures about price. Many called for extending the rate cycle to 4 years. Others preferred small annual increases. Most wanted price increases less than inflation. A few demanded no price increases. The Postal Service had mistakenly committed to 4 years without a price increase in 1991. The 1995 increase of 10.3% was below the inflation rate by over 2%. The 1997 rate case designed for implementation in 1998 was for rate increase of 4.5%, roughly 1.5% per year in a 3% inflationary environment. The delay to implementation in 1999 and the reduction to only a 2.9% increase led to abandoning the key Board resolutions and a return to dire financial problems for the Postal Service.

The Postal Service is a service business. Like most service businesses, it is labor intensive and requires regular price increases. The people who work at the Postal Service need and expect increases in their pay that keep up with inflation. The government has committed to these increases as a policy for its military personnel and civilian workers. Suggestions that the Postal Service can never again increase its prices are utter nonsense. It would be similar to saying that Universities can never again raise tuition, that doctors and hospitals can never again increase fees, or that the price of a haircut can never rise.

There is no prohibition to annual rate cases, which would result in small yearly increases in the worst-case scenario. The only constraint to ensuring annual profits, continuing declines in the accumulated deficit, and the provision of good service is self-imposed by the Postal Service and its Board of Governors. Another reason for annual price increases is to quickly respond to changing costs and provide appropriate pricing signals. For example, the costs avoided by having mailers presort and/or put bar codes on mail have been declining. Annual adjustments serve to buffer what otherwise becomes a large change in price. Also, it prevents losses from this portion of the business from growing and harming the Postal Service.

During my time as CFO of the Postal Service, I did what I could to limit the size of discounts for presort and work-share mail equal to, or slightly below, the costs saved by the Postal Service. It seemed ridiculous that pre-sort shops claimed great cost advantages over the Postal Service and then complained about needing higher discounts than the costs avoided by the Postal Service. At the same time their representatives have testified before the Postal Rate Commission that they must give "the lion's share" of the rate discount to the originator of the mail piece. This seems counter productive if the pre-sort shops were creating the cost savings. Excessive discounts are a major cause of the current financial problems of the Postal Service.

IV. Successful Strategies and Tactics Abandoned

The Postal Service has abandoned most of the key strategies and tactics that brought it prosperity. The Board of Governors effectively reversed its policies about earning profits, reducing debt and the need to timely file and implement rate cases in order to achieve these important objectives.

It drastically modified its incentive plan by reducing incentives for profit and allowing bonus payments in years with losses based on an indexing system. It dropped EVA as a measure and switched to Total Factor Productivity (TFP) with negative consequences. At the request of management, it changed goals from customer satisfaction to speed of mail delivery as measured by an outside firm. It abandoned surveys of employees and substituted numerous other measures thereby weakening the incentive program.

As a way to increase service scores, some Postal managers canceled late pick-up of business mail, and re-scheduled the last pick up from some boxes earlier in the afternoon. The Postal Service also reduced the distance that was promised overnight delivery. These actions clearly negatively impacted the quality of service provided but did not change the speed of delivery. However, it affected the speed-of-service measure (EXFC), positively.

Spending soared due to lack of control and many initiatives failed to produce monetary returns or increases in customer satisfaction. It is no wonder that the Postal Service has fared badly.

Saving the Postal Service from Disaster:

Of necessity, the Postal Service made major efforts to lower costs and it deserves praise for avoiding bankruptcy. The current management of the Postal Service has reversed a situation that nearly brought disaster after the triple shocks of 9/11, Anthrax and the Recession. Mr. Potter and Mr. Strasser deserve great credit for their action to save the Postal Service from its dire financial straits. Mr. Strasser and Mr. Tayman deserve even more credit for their persistence and success in convincing OPM and Congress to finally eliminate overcharges in the older pension plan, CSRS.

Yet it would be a great mistake to set a course for the future that does no more than continue the focus on exclusively cutting costs and unnecessarily delaying rate requests as many have suggested.

Needless Problems:

However, the Postal Service need not have gotten in financial trouble in the first place. By losing momentum and by letting costs get out of control due to Board decisions in 1998 and beyond, it has had to resort to 4 price increases in 4 years.

After making decisions that caused a financial reversal, the Postal Service has asked for legislation to solve a problem that it, itself, created. Sadly, the changes requested will have little positive effect and many have potentially disastrous consequences.

V. Failed Policies and Counterproductive Claims

There is a great deal of advice that has already been given to The Presidential Commission. Much of it is illogical and suggests new approaches to failed policies. Several common themes are listed below.

Contracting Out:

Numerous initiatives to contract out Postal Service work failed to achieve the anticipated savings and generally resulted in both reduced service and reduced customer satisfaction. After initially accepting claims of huge savings to be derived from pay rate differentials, the Postal Service reversed itself on most major initiatives. Promised savings never materialized. Careful analysis of the Priority Mail Processing Center proposal discovered that initial estimates of savings were false. The Postal Service and its Unions have achieved market based pay through the arbitration process and the claimed “lower wage employees” produced less output with less quality.

(NOT) Earning Too Much Profit:

In 1998, the lobbyists for many large mailing companies, hoping to delay implementation of the recently recommended rate increase, argued that the Postal Service was earning too much profit and that it was supposed to break even at best. Despite the fact that the recommended increase averaged only 1.2 percent per year, was far below inflation, and was designed to cover significant and needed increases in spending, the lobbyists prevailed and the increase was delayed. The Governors voted to delay the increase to 1999 and at the same time approved significant spending increases in both capital and current expenses.

Board policies to reduce debt and earn profits were effectively negated. The word went out to spend as much as possible in fiscal 1998 in order to prepare for a tough 1999. The Postal Service lost approximately \$0.8 billion in its last fiscal quarter ending September 30, 1998. Total debt began what became a dramatic increase. The Postal Service’s financial situation declined rapidly.

Selling Retail Items:

The Postal Service attempted to use its retail outlets as stores to sell merchandise and lost money. People were not anxious to buy merchandise from a service provider. Numerous initiatives promised much and delivered only problems and bad publicity. Suggestions that the Postal Service can enter new businesses to contribute profits are a triumph of hope over experience.

Price is (Not) All That Matters:

Uninformed people speculate that the recent price increases have hurt mail volume and are the reason for the decline of 2.5% in mail volume from 2000 to 2002. Nothing can be further from the truth. Perhaps the best example is Priority Mail and Express Mail. The table below shows one example of a calculation I performed for a friend using published prices from the web sites of Fed-EX, UPS and the Postal Service:

Costs of 10- Pound Package sent from
Fairfax, VA 22032 to Los Angeles, CA 90210²

	U. S. Postal Service	Fed-EX	United Parcel Service
2 or 3 day	Priority Mail \$19.20	Express Saver (3 day) \$28.09	3 Day Select \$39.02
Overnight	Express Mail \$37.50	Standard Overnight \$51.51	Next Day Air Saver \$63.14

While it is true that Priority Mail rates have increased over the last four years, there is still a significant saving compared to each of the major alternative carriers. Prices cannot explain the 18% decline in Priority volume from 2000 to 2002 or the 15% decline for the Quarter 2, 2003 compared to the same period of 2002.

It is worth noting that both Fed-Ex and UPS have seen overall volume decline from 2001 to 2002. It is a misstatement of the facts for the Postal Service to use the “boogeyman” of electronic diversion as a reason for a change in its law. Its decline in total volume of 2.5% is in line with that of Fed-Ex and UPS volumes which are not likely to have been affected by electronic diversion. In any case, electronic diversion has been a fact of life since the Telegraph was invented in the mid 1800s. Of course, there is no price low enough to convince the public to abandon E-mail for letters through the mail.

Productivity Conflicts with Customer Satisfaction:

In the 1990s, total Factor Productivity was continued as a measurement, but discarded as a management tool and/or goal. Management continued to brief the Board of Governors but management believed that other factors were more important. Service improvement initiatives and capital spending for new facilities served to lower the productivity measure while increasing the long-term health of the organization.

In a major move, outdated equipment was removed first in the Sun Coast district and then nationally. Prior standards about obtaining maximum throughput per machine were discarded in favor of increasing machine utilization. The new electronic sorting machines were faster and more accurate than older mechanical models. This required expanding the time in which they were used and increasing time when employees were waiting for mail to arrive. Despite improved finances and less miss-sent mail, it gave fuel to those who complained about “non-productive time.”

The table below shows that when the Postal Service Earned Profits, productivity stagnated. When the Postal Service struggled to survive and cut expenditures to provide for its future, productivity grew steadily.

² Owner supplied packaging

Comparison of US Postal Service
Total Factor Productivity Growth
With
Net Income

Fiscal Year	Net Income (Millions)	TFP Growth Percent
1993	(\$1,765)	3.8
1994	(\$913)	(0.2)
1995	\$1,770	(1.9)
1996	\$1,567	(1.3)
1997	\$1,264	1.3
1998	\$550	(1.0)
1999	\$363	(0.1)
2000	(\$199)	2.4
2001	(\$1,680)	1.3
2002	(\$676)	1.1

Wages Premium:

There are many estimates about the amount that could be saved if only the Postal Service were to pay market-based wages. Yet every initiative that promises to save money by contracting out work to take advantage of the purported wage differential has failed to achieve the promised savings. In every contract negotiation, both the Postal Service and its unions start with positions that say the Union workers are either under paid or over paid depending on which side makes the case. As the main Postal Service witness in the 1994 –1995 labor arbitration hearings, I can testify that the Postal Service pays market-based wages. Any excess was wrung out in that contract that provided the smallest increase in base pay for union workers in the history of the Postal Service. In fact, as the contract continued, a number of operations managers asked for and received supplemental budgets to increase pay for new hires because they could no longer attract capable and qualified candidates. It is possible to find less expensive labor, but the service problems of 1993 convinced me that these jobs required skill.

The current labor arbitration required in the law is a major benefit to the Postal Service. It ensures the payment of market-based wages. Earlier in my career, I was CFO of United Airlines and I believe that the airline-type law that the Postal Service has requested would be a grave mistake. The Postal Service is like any other large organization. Its wage rates are set by the market or in the Postal case by a prestigious panel of Arbitrators chosen jointly by unions and management.

To those who argue that the Postal Service needs to fight with its unions about lowering wage costs, I point to the comparison of United Airlines and Southwest Airlines. Both are unionized but only one has employees who are very productive and enjoy their work. I joined United Airlines just after it tried to force pilots into major wage concessions and failed in an attempt to replace all of its pilots. The business has been declining ever since. The Postal Service cannot afford the disruption that inevitably occurs from major efforts to reduce labor costs by either a strike or by contracting out large portions of its work.

Public-Private Partnership, an Unfulfilled promise:

The Public - Private Sector Partnership has been and continues to be all promise and almost no results as far as having new initiatives that actually help the Postal Service. Examples include: Call Centers, Remote Encoding Centers, Priority Mail Processing Centers, Remitco (a remittance processing venture that failed), the sale of Warner Brothers merchandise along with other merchandise, and the FED-EX “partnership” that was recently implemented.

The two that succeeded financially brought tiny profits and huge amounts of bad publicity. A partnership with Mexico’s second largest bank wired funds from the U. S. to families in Mexico avoiding the theft rampant in the Mexican Post earned a modest contribution to profit. It was roundly criticized for the high cost of the transactions.

Selling phone cards in a joint partnership with American Express brought about \$8 million per year in contribution and when the venture was sold a capital gain of about \$30 million. The purchaser ultimately filed for bankruptcy protection.

Labor as a Percentage of Total Costs:

Another strange measure seems to be circulating. Some have commented that it is wrong to have a high percentage of labor costs compared to total costs. Of course, the percentage of labor costs is a function of the service provided. In universities and barbershops the percentage is high. In fact, when Fed-Ex implemented its contract with the Postal Service, it was able to use some of its airplanes that had been idle during the day. It hired more pilots, crewmembers and ground people and its percentage of labor costs compared to total costs increased. I teach students that higher capital utilization is good, not bad.

Customers are the People, Not the Mailers

This Commission has not heard from the true customers of the Postal Service. Because the mail is as much a part of life as clean water from the tap, people do not get excited about the Postal Service until something changes. One member of Congress told me that closing small Post Offices generates more mail than anything else.

The companies and associations who have generated comments are valued clients of the Postal Service and need to be treated with care and consideration. However, they have an economic interest in switching costs to other groups and an interest in cost minimization for themselves. Instead customers want service, convenience, safety, security from identity and mail theft, and pleasant experiences in retail establishments.

If customers did not want mail, business would abandon the mail in a heartbeat. Mailing agencies who print, sort and enter the mail of other businesses are simply intermediaries who make a large profit by convincing the Postal Service to hurt itself financially through excessive discounts. Large companies that mail bills, statements and advertisements are clients, but not the ultimate customer. To be sure, these companies need attention and service, but the choice to mail is driven by what individual customers want.

Pricing Flexibility:

I see little to be gained from the pricing flexibility that the Postal Service desires. If it keeps profits at a level sufficient to provide for the contingency for emergencies written in its current legislation, it can absorb short-term increases in oil prices or other expenses. If it reduces its debt, it will provide more of a contingency.

My worry is that pricing flexibility will become the means to offer larger discounts to current customers for current business because they lobby effectively. It will likely hurt the bottom line with no positive long-term benefit. It is the United Airlines approach to pricing. At the moment, the Postal Service has the Southwest Airlines approach to pricing. There is a business lesson in this comparison.

Electronic Diversion:

Diversion of mail to electronic transmission has been a fact of life since the telegraph. The telephone accelerated the diversion of letters. Fax machines have done more and most young people have been using E-mail for a decade. Diversion will continue and mail volume will continue to grow steadily. It would be a mistake to try to fix a perceived problem with a non-solution.

VI. Recommendations

I would ask that you NOT recommend a change in the law. Too many unintended consequences come from well-intentioned law changes. These changes could destroy the Postal Service. None of the proposals is likely to help the bottom line or the long-term business prospects. Pay heed to the lessons learned from the 1990s.

The Postal Service needs to be governed by individual board members that would meet the intent of Sarbanes-Oxley legislation. The Board needs to concern itself with its fiduciary responsibilities to the American people. They are entrusted with the oldest and most successful business. It is a business that is also the only U. S. government agency that touches the lives of the American people 6 days a week. The vast majority of people like their mail service and wish only that Post Offices would be made more convenient.

Administrative Action, Not a New Law:

I suggest that this commission recommend to the President that the Postal Service Board of Governors focus on running the Postal Service as a service based business. Also, you should recommend that they return to the practices of the mid 1990s and pay attention to earning profits, building customer satisfaction with the American people, re-installing an incentive system for creating Economic Value Added, and take measures to improve the morale of its work force. This approach worked before and I believe it will work again.