

FLATS STRATEGY

This document outlines the Postal Service's Flats operational and pricing strategies. In its FY 2009 Annual Compliance Determination, the Postal Regulatory Commission (PRC) expressed concern over cost coverage for a number of flat-shaped products, and directed the Postal Service to address those issues. In particular, the PRC directed the following:

- [t]he Postal Service [to] develop and present a plan explaining how it intends to increase Periodicals cost coverage to a reasonable level in its next notice of general price adjustments for market dominant products, or its next annual compliance report.
- the Postal Service to devise a plan to improve the cost coverage of the Standard Mail Flats product. This plan should include any operational or mail preparation changes that the Postal Service deems necessary, as well as a specific timeline for achieving a positive contribution for the Standard Mail Flats product. The plan shall be included in the next ACR or the next general market dominant price adjustment, if it precedes the ACR.
- the Postal Service file a plan at the time of the next ACR or the next general market dominant price adjustment if it precedes the ACR that outlines how it anticipates addressing the revenue shortfalls of the Package Services class and each of the products that did not produce sufficient revenues to exceed attributable costs.... The plan should also address, if necessary, any impact the ongoing network distribution center activation process will have, and any other information the Postal Service deems necessary to ensure adequate revenues in the future.

FY 2009 ACD at pages 75, 87, 95. This document responds to the PRC's directives by providing a description of the strategies the Postal Service has implemented and intends to implement in the future to address these issues. The discussion is in two sections; the first covers operational changes and enhancements, and the second covers pricing strategies.

OPERATIONS

This section is divided into three parts covering transportation, mail processing, and Post Office operations and delivery. Within each section, strategies for improvement are presented, along with a qualitative estimate of each program's overall impact on cost, a brief discussion of the initiative, its actual or expected implementation status, and, where applicable, an indication of the products it will primarily affect.

There are a mix of strategies and approaches included here. Some, such as the implementation of the Network Distribution Center (NDC) network and the roll-out of Flats Sequencing System (FSS), are transformative, with immediate and easy-to-see impacts. Others are evolutionary, including efforts to maximize efficiency in current operations and improve existing processes. But even though their affects are not as immediately dramatic, these evolutionary changes are equally important, as they reinforce, support, enable, and enhance the systemic changes necessary for Postal Operations to adapt to the changing landscape. Process improvement, equipment and space optimization, and other ongoing reviews allow the Postal Service to take full advantage of the potential of new technologies and systems in order to improve efficiency and lower cost.

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Transportation

The primary focus of the transportation strategies is to maximize the utilization of space. This effort begins by filling handling units (trays, tubs, sacks, etc), then containers (rolling stock, pallets, air containers, etc), and finally trucks, planes and rail cars. These strategies not only reduce the amount of transportation necessary, but also the handling costs associated with moving handling units and containers throughout the network. These efforts, along with the NDC transition, will also allow the Postal Service to optimize the shape of the overall network, all of which will help to reduce overall transportation cost.

- Improving Handling Unit/Container Density (2010-2011) – *LARGE Opportunity*
 - Facility Optimization – The consolidation of outgoing operations either through Area Mail Processing (AMPs) or other initiatives, for example the NDC implementation, allows for the aggregation of mail, increasing the weight of handling units and providing the opportunity to create denser containers. This reduces the amount (and therefore the cost) of transportation required to move this volume to destination.
 - Equipment Consolidation – Tour compression and maximizing utilization of sortation equipment (see Mail Processing section) support aggregation of mail, which leads to fewer, fuller containers, increasing the weight of handling units and expanding the opportunity to create denser containers.

- Eliminate Periodical and Standard Mail Flown (2010-2011) – *SMALL Opportunity*
 - “Do Not Fly” effort — Eliminate Periodicals and Standard Mail on air transportation. The goal is reduce the transportation cost as volume can be absorbed on existing surface transportation. In order to capture savings, the Postal Service is currently monitoring plant sort program runs to ensure sites that are supposed to be consolidating volume at another facility are in compliance. Also monitoring sort programs not run to identify plants consolidating mail classes on sortation equipment resulting in upgraded transportation for mail classes that are supposed to use surface transportation. Alerts are distributed daily. Utilization of Intelligent Mail Barcode (IMb) data is planned in future to identify these opportunities.

- Transportation Utilization (2010-2011) – *LARGE Opportunity*
 - Redesign NDC Mail Transportation Equipment (MTE) – Goal is to maximize the cube utilization of the trailer by utilizing containers that can be double stacked. Current MTE design is focused on easy trailer loading and unloading (more use of rolling stock vs. palletized loads) rather than on maximizing load. Stackable cardboard containers utilized in outgoing operations will increase floor to ceiling trailer utilization opportunities.
 - Consolidation/Deconsolidation Concept – Increase trailer utilization by consolidating volume in the most efficient manner (including bed loading trailers) to reduce the number of required loads within a lane. Focus will be on the NDC network initially.
 - Quarterly Reviews – Provide a sustained focus on increasing trailer utilization through review of opportunities to reduce weekend trips, eliminate redundant

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trips, and consolidate trips, as well as adjust scheduled departure and arrival times to improve NDC network efficiency.

- Network Optimization (2010-2012) – *MEDIUM Opportunity*
 - NDC/Surface Transportation Center (STC) Integration – the floor space gained by consolidating distribution within the NDC network has created adequate space to co-locate some STCs with NDCs. This enables previously underutilized transportation to be maximized with other classes of mail (thus reducing the number of trips in the system), and eliminates redundant networks.

Mail Processing

Opportunities in mail processing operations include several activities with concentration in two main areas. The first is facility optimization, where consolidation of operations can yield significant benefits, primarily in terms of improving efficiency of operations by achieving economies of scale and increasing mailflow densities. The second main focus is on improving equipment utilization and minimizing the amount of non-automated processing. This should particularly benefit flat-shaped mail, as the roll-out of FSS and the minimization of manual handling will significantly improve the efficiency of flats processing.

- Facility Optimization (Ongoing) – *LARGE Opportunity*
 - Area Mail Processing (AMP) – The Postal Service continually reviews the feasibility of consolidating all originating and/or destinating mail processing operations from two or more offices. An AMP study presents the business case for centralization of mail processing resources and takes advantage of state-of-the-art technologies available at the gaining facility.
 - Eliminate annexes – This initiative will reduce handlings, overhead, and transportation by consolidating processing operations, thereby capitalizing on underutilized facilities, which can result in the disposal of real estate through either lease termination or the sale of property.
 - Other facility optimization initiatives – The Postal Service is evaluating the consolidation of other operations and functions at network facilities, including Airport Mail Centers, Logistics & Distribution Centers (LDCs), and NDCs that allow for co-locating operations to maximize efficiencies and promote other concurrent initiatives.

- Equipment optimization (2011 and beyond) – *MEDIUM Opportunity*
 - Automated Package Processing System (APPS) utilization – By focusing on maximizing the amount of mail processed on the most efficient equipment, the Postal Service is implementing strategies to ensure the APPS is fully utilized. This may require shifting volume from less productive older equipment or even manual operations, for example by taking mail from the Small Parcel and Bundle Sorter (SPBS) or other non-automation operations. Weekly telecons stress optimal APPS performance. In addition, weekly machine performance indicators are disseminated and appear in the Mail and Image Reporting System (MIRS).
 - Automated Flats Sorting Machine (AFSM) 100/Upgraded Flats Sorting Machine (UFSM) 1000 utilization – *MEDIUM Opportunity* – To focus on maximizing the

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amount of mail processed on the most efficient equipment, the Postal Service is implementing strategies to ensure the AFSM100 is fully utilized. Because there has been a decrease in flats volume system-wide, and, where possible, flats are being moved "up the ladder" to FSS, there is an opportunity to optimize utilization of AFSM 100 equipment by assessing the amount of equipment needed in each processing site to meet workload demands. This rightsizing effort will reduce maintenance costs for equipment removed from service, or provide for more automated processing of flat mail in the case of relocated equipment, particularly where the UFSM 1000 is still in use. Further, the majority of flat mail processed on UFSM 1000s is AFSM 100 compatible and can be moved into the more efficient AFSM processing environment. AFSMs and FSSs can remotely barcode mail, thereby keeping flats in an automated mail stream. In addition, the Postal Service intends to evaluate the feasibility of enhancing excess AFSM 100 equipment to sequence additional flat mail not covered by the initial 100 Flats Sequencing System machines.

- Future FSS enhancements and processing modes (2012 and beyond) — *MEDIUM Opportunity*
 - Various efforts are underway to enhance machine performance, including introduction of alternative processing modes. A new high-speed feeder is being pursued along with the potential of every-other-day sequencing.
- Automated Flats Preparation (AFP) (Begin 2013) — *MEDIUM Opportunity*
 - The Automated Flats Preparation processor is automated equipment that eliminates the manual unbundling of flat mail and automatically places the mail in containers ready for feeding to flat sorting equipment (both FSS and AFSM 100).
- Automated Package and Bundle Sorter (APBS) (through Oct 2011) — *MEDIUM Opportunity*
 - APBS extends the life and enhances performance of existing Small Parcel and Bundle Sorter equipment by replacing the control system and adding Optical Character Reader (OCS) / Bar Code Sorter (BCS) technology. This latter upgrade will increase machine throughput, producing significantly higher processing productivity.
- Material Handling (2011-2016) — *LARGE Opportunity*
 - Deployment of existing material handling technology along with next generation technology utilizing a new family of containers to drastically reduce the approximately \$4 billion spent annually on moving mail (letters, flats, and packages) into, through, and out of processing plants. Near-term efforts will be accomplished over the next 1 to 3 years and rely on new management techniques for aligning staffing with workload, along with deployment of traditional material handling systems. Longer-term efforts will utilize new containers and state-of-the-art technology to further reduce costs in the 3 to 5 year timeframe.

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- Flat Recognition Improvements (2011 and beyond) – *SMALL Opportunity*
 - There are continued improvement efforts in flats recognition equipment to improve accept rates and lower error rates which will reduce the amount of manual keying needed at Remote Encoding Centers and reduce rehandling of incorrectly coded mail pieces. The next upgrade is scheduled for September 2011 with additional improvements expected over the following several years.

- Automated Flats Forwarding (2013 and beyond) – *SMALL Opportunity*
 - Similar to letter-size mail, technology efforts are being considered to intercept undeliverable-as-addressed mail en route passively and utilize high speed automated equipment for applying new address labels.

- Using IMb data to determine letters processed on flat sorting equipment – (2011 and beyond) – *SMALL Opportunity*
 - There are two concepts possible for detecting letter mail being processed on flat sorting equipment. The first utilizes the mail piece image during optical character reading. Software algorithms will be incorporated to calculate height and length of each piece. Rapid implementation will provide this information via log files that will be collected and manually processed on a periodic basis. Longer-term, mail piece size data will be incorporated into existing data paths for automatic generation of summary reports by location and machine. The second approach is to leverage IMb information along with Full Service information provided by the customer. Mailer ID, service type, and unique piece serial information read on flat automation equipment would be matched to rate and mail type provided by the mailer as part of Full Service. Pieces identified as letters would be reported by each location and machine. The data collected will then be used to optimize sorting operations, minimizing inefficient use of existing equipment.

- Electronic Condition-Based Maintenance (2011 and beyond) – *SMALL Opportunity*
 - Introduction of software used to generate maintenance tasks for automated equipment (letters, flats, and parcels) which reduces maintenance costs of this equipment. The software release is set to begin in 2011.

- Utilize a single Incoming Secondary run for all flats – (2011 and beyond) – *SMALL Opportunity*
 - Sorting flats to the carrier route level is often performed on separate runs for preferential mail (First-Class Mail and Periodicals) and, to a lesser extent, Standard Mail. This, in turn results in lower throughput and higher cost than could be achieved if a longer single run were used. However, introduction of this process reduces the ability to curtail Standard Mail on heavy volume days at delivery units.

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- Monthly Periodicals – merge with Standard Mail service standards – (2011 and beyond) – *SMALL to MEDIUM Opportunity*
 - In an effort to support every-other-day processing and more efficient mail flows, there will be a growing need for alignment of the service standards for monthly Periodicals with Standard Mail. This also supports co-palletization and possible co-mailing programs. Mixed-class co-palletization accepts pure Periodicals and pure Standard Mail bundles combined on the same pallet. In concept, mixed-class co-mail would allow mailers to combine Periodicals and Standard Mail Flats into the same bundle and on the same pallet. Mailers could generate more volume in one mailing, allowing for finer presort and more drop-shipped mail. Mixed-class co-mail can be viewed as the next step beyond single-class co-mail, which mailers and publishers have been doing for many years. The mixed-class co-mail bundles and pallets are created at the mailer’s site.
Both mixed-class co-mail and co-palletization are important steps in creating a more efficient flats processing stream. They also allow publishers of monthly publications (or less frequent) to get better postage rates through co-mailing, while mailing under Standard Mail service levels.

One significant net benefit to the Postal Service is a reduction in sacks entered when the mailings are mixed classes. It’s estimated that more than 260,000 sacks will be removed from the system at current volumes. Another benefit is the creation of a more efficient single mail flow; rather than having separate flows for each class.

- Distribution compression – (2011 and beyond) – *LARGE Opportunity*
 - Using continuous improvement methods and inventory driven planning, distribution operations will be compressed to achieve maximum efficiency. This will require the evaluation of mail availability, operating windows and equipment requirements before the assignment of employee resources. Once facility specific operational modeling is completed, scheduling and staffing will be modified to ensure anticipated workhour savings are achieved.

- Reduce mixed-states consolidation processing locations (L009) and optimize mixed states flow – (2010-2011) – *MEDIUM Opportunity*
 - The number of USPS locations that process mixed-state residual Periodicals and Standard Mail flats is being reduced to achieve savings in distribution and transportations costs. The number of sites that processed this mail prior to consolidation was 40. When consolidation is completed, the number of sites processing this mail will be 18. The consolidation effort results in greater processing efficiency by reducing the number of machines and run time necessary to process the volume. Processing this volume on fewer machines also generates fewer handling units to be transported through the network.

- Realign operating and transportation plan to improve utilization (ongoing) – *MEDIUM Opportunity*

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- Mail Processing Operating Plans (MPOPS) are being reviewed and updated to ensure mail processing and transportation are optimized. Clearance Times (CTs) and Critical Entry Times (CETs) must fall within designated parameters to meet operating windows. These clearance time windows are fed to systems such as Facility Access and Shipment Tracking (FAST) and Service Performance Measurement. Once all plans are evaluated and approved, transportation adjustments will be made to improve utilization.

- Periodicals Lean Six Sigma (LSS) end-to-end value stream mapping project (ongoing) – *Opportunity not yet defined*
 - This LSS project will focus on three major areas: 1) creation of a Value Stream Map (VSM) for Periodicals; 2) data analysis of CETs; and 3) streamlining processes and standardizing Periodicals work and mail flows, along with identification of non-value added steps. Focus on these efforts will likely lead to other project initiatives. The current timeline is to complete the VSM by end of August 2010 and complete baseline impacts of CET by mid-September 2010. The project will evaluate establishing a national critical entry time for Periodicals (as opposed to the current practice of locally-established critical entry times). Assessment will consider the pros and cons of a national versus local CET as well as the need for FSS versus non-FSS CETs. If locally established CET remains a policy, the Postal Service will work collaboratively to define parameters for establishing a local CET. Additional areas to evaluate include eliminating use of “Hot 2C” practices (that is, preferential manual handling of Periodicals mail) by both USPS and mailers; and eliminating management of in-home dates for both Periodicals and Standard Mail.

- Refine work methods to improve Business Mail Entry Unit (BMEU) / Plant load handoff to mail processing – (2010-2011) – *LARGE Opportunity*
 - To meet the obligations for compliance with the Sarbanes-Oxley Act, a new approach for conducting business, a Lean Mail Acceptance Process (LMAP) was developed, implemented, and replicated in BMEUs throughout the country. LMAP applied Six Sigma and Lean principles to the processes used in the BMEUs. The procedures were largely designed to ensure that the Postal Service receives proper payment for mail that is inducted at the BMEU and subsequently processed, transported, and delivered. However, a key process in LMAP was to define staging areas, signage, and enforcement of clearance documents for mail that was cleared to be released to operations. These processes provided a cleaner transfer of mail from the BMEU to Plants and NDCs (by tier level) as well as by mail type. The effort reduces volumes processed through Plant bullpens or opening units prior to dispatch, and drives better container utilization thereby reducing the number of handling units.

- Sort Plan Optimization (SPO) for flats – (ongoing) – *SMALL opportunity*
 - Flats account for approximately 9 percent of total operating volume, largely processed in the Area Distribution Center (ADC) network instead of the extended

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Automated Area Distribution Center (AADC). Presently, sites can perform the full ADC distribution on a single sort program. Some offices have already started combining low-volume destinations and dispatching this mail to consolidation sites as a means to improve flats tray (tub) densities. Development of requirements for bringing flats into SPO has already begun with an anticipated software release possible in the third quarter of Fiscal Year 2011.

- Continuous Improvement (ongoing) —
 - The Postal Service is aggressively exploring opportunities to reduce costs and improve efficiencies. To meet these challenges, USPS is using its Continuous Improvement plan and Lean Six Sigma tools to examine operational processes, standardize, and remove waste from the system with an overall focus on improving customer satisfaction. Value Stream Mapping and other tools to evaluate end-to-end processes are being applied to ongoing projects, such as reducing the changeover time on APPS machines, improving APPS throughput, increasing flat tray (tub) density, and reducing AFSM double-feeds.

Post Office and Delivery Operations

Post Office operations efforts focus on optimizing the amount of in-office time spent by distribution personnel, retail associates, and letter carriers, and the support and supervisory effort needed to oversee these operations. Opportunities surrounding delivery operations focus on the impact of maximizing street time (the flip side of minimizing in-office time) and on optimizing carrier routes due to the dramatic decline in volumes and continued growth in the number of delivery points each year. To some extent, these efforts are supported by, and dependent on, the implementation of mail processing changes, but other independent efforts are also underway.

- Business Plan Staffing and Scheduling Reviews (2010-2011) – *LARGE Opportunity*
 - Staffing and schedule reviews are enhanced in the short term with the implementation of automated tools. These tools allow for greater oversight of the entire process and automate the staffing and scheduling review. Tools are built into the system to drive the process of reassignment and identification of redundant and unnecessary assignments. Staffing is built within arrival and productivity constraints.
- Shifting distribution from Post Office Operations (Function 4) to Mail Processing Operations (Function 1) – (2010 and beyond) – *MEDIUM Opportunity*
 - Manual workload reductions along with other improvement strategies associated with improved containerization, mail arrival flows, quality, and studies of machine readability and workflow, allow for continuous improvement. For example, given the dramatic volume declines, Post Office operations and mail processing equipment utilization can be better optimized when mail processing facilities absorb letter-sorting processing from Post Office Operations facilities.
- Customer Service Unit Optimization – (2011-2012) — *MEDIUM Opportunity*

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- Customer Service unit optimization efforts include consolidation of customer service facility distribution operations into larger facilities to gain economies of scale and improve the salary and benefit cost per workhour ratio. This process includes a transfer of carrier operations between offices without disturbing existing retail operations. Candidate offices will be reviewed based on criteria such as physical space, scheme capacity, staffing, and the time/distance traveled between delivery areas. The transfer of carrier and supporting distribution operations from one office to another is expected to increase operating efficiencies by more fully utilizing the existing workforce at the gaining location. Administrative changes to management and unit levels may occur as a result of adjustments to workload and changes in staffing levels in units with increased/decreased workloads. While initiatives are currently in place for these activities, no formal process is nationally deployed at this time; although final preparations are being completed and testing may begin prior to the end of FY10.

- FSS work methods – (2010 and beyond) — *LARGE Opportunity*
 - Delivery benefits: FSS processing significantly reduces the amount of office time for carriers resulting in the need to adjust routes to ensure an 8 hour workload. A Memorandum of Understanding (MOU) between the National Association of Letter Carriers (NALC) and the Postal Service (Sept 2007) established procedures for route adjustments. These route adjustments will be one of the main savings opportunities from FSS operations. The flats sequencing system deployment schedule will determine when the savings will be realized. In anticipation to implementing FSS, another agreement was reached with the NALC that established approved work methods for handling multiple bundles on those routes operating under a three-bundle limitation. Without this agreement, a majority of city carrier routes would have had to continue to case FSS mail instead of handling mail as a separate bundle.
 - Post Office Operations (Function 4) in-office benefits: The FSS system provides two opportunities for reducing Function 4 costs. First, savings accrue by reducing the distribution clerk workhours in delivery units required to handle and distribute bundles and containers of flats mail to letter carriers. Instead, sequenced flats arrive (prepared in order of delivery) in street-ready trays that can be loaded directly into delivery vehicles. Second, AFSM 100 capacity is freed up as mail moves from this machine to FSS equipment. In turn, this provides the opportunity to shift mail currently in delivery units, due to capacity constraints, to a much more efficient automated processing on AFSM 100 machines.

- Route Adjustments Joint Alternate Route Assessment Process (JARAP) / Carrier Optimal Routing (COR) — *MEDIUM Opportunity*
 - The Postal Service has entered into an MOU regarding a JARAP with the National Association of Letter Carriers to maintain city delivery routes throughout the year using a quick, data-driven process. This MOU provides the parties a process to evaluate and adjust routes quickly based on changes in mail volume. This MOU is the third in a series of agreements to evaluate and adjust

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city delivery routes. During the first two MOUs the Postal Service has shown a net reduction in city delivery of over 11,000 routes, or the hours equivalent of 12,473 routes. The most recent JARAP MOU is a continuation of the previous two MOUs and should provide an additional reduction of approximately 2 percent for the routes being evaluated and adjusted. Furthermore, the JARAP process takes into consideration the change in mail volume during the evaluation process. As the flat volume decreases, the amount of office time related to the drop in volume is considered and adjustments are made accordingly. Overall, JARAP and COR matches carrier routes with workload, resulting in reduced number of needed carrier routes.

- Route Optimization 100 Percent Street routes – (2011 and beyond) — *LARGE Opportunity*
 - As total cased volume declines, letter carrier casing will be concentrated on a few assignments, while most carriers will only perform street duties. A “caser” would prepare and pull down all cased mail, while a deliverer would load the mail and deliver it to a greater number of customers. This concentration will produce savings in fixed office time. It is projected that route reductions will result from this initiative. Also, vehicle savings will be generated through street route reductions.

- Facility Optimization – (2010 and beyond) *SMALL Opportunity*
 - FO is a comprehensive review of facilities and operations in an effort to identify both cost saving and revenue generating opportunities. This is being done where operations can be combined, excess space and capacity eliminated, lease agreements altered or eliminated, and under-utilized property sold. The net effect will reduce the number of facilities under USPS ownership or obligation.

PRICING STRATEGIES

The Postal Service will implement pricing strategies for these products that, in concert with the operational improvements discussed above, should drive significantly enhanced cost coverages.

Periodicals

The price changes proposed in this filing, which are significantly above the average increase, go some way towards ameliorating the profitability issues surrounding these products. In addition, the changes to flats processing, transportation, and delivery described above should reduce costs on an ongoing basis. The Postal Service finds it prudent to evaluate the actual effects of those changes before embarking on more radical changes to Periodicals pricing, but anticipates that the implementation of FSS in particular may provide an opportunity to revise mailing standards and preparation requirements in a way that both ensures the recognition of potential Postal Service efficiencies and reduces total cost to mailers and mail preparers. This, in turn, may lead to further

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revision of pricing structures to bring embedded incentives into line with current Postal Service practices.

Standard Mail

The Postal Service believes that Standard Mail volumes are potentially sensitive to large price increases, which may precipitate “rate shock,” given that this mail is primarily composed of marketing material and other discretionary activities. At the same time, because of its importance to the postal system as a whole, Standard Mail needs to be priced to yield large, consistent benefits to the Postal Service. As a result, care needs to be exercised in implementing both structural and level changes to pricing, and such changes need to be well-planned and thought out. The Postal Service believes that opportunities for optimizing Standard Mail pricing are inherent in the NDC transition program, FSS implementation, and transportation optimization programs. In particular, as with Periodicals, there appears to be an opportunity to enhance mailing and preparation standards and optimize or revise the current pricing structure to both recognize operational benefits and drive desired behavior in a way that will ultimately benefit both mailers and the Postal Service.

Package Services

As with Periodicals, the Postal Service has proposed fairly large changes in Package Service prices in this filing, specifically to address cost coverage issues. The operational strategies discussed above, particularly those related to transportation, facility optimization, and APPS utilization, should also help to reduce costs, further improving cost coverage. As it has done in the two previous changes under the price cap, the Postal Service will continue to focus on improving the profitability of those Package Services products with low cost coverages.