

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

FIRST-CLASS PACKAGE SERVICE (FCPS)
SERVICE STANDARD CHANGES, 2021

Docket No. N2021-2

**DIRECT TESTIMONY OF
THOMAS J. FOTI
ON BEHALF OF THE
UNITED STATES POSTAL SERVICE**

(USPS-T-3)

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AUTOBIOGRAPHICAL SKETCH

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As the Vice President of Product Solutions for the United States Postal Service, I am responsible for leading the strategic development and management of enterprise-wide product solutions to address customer needs. I oversee the management of product lines and services, including the development of strategies, policies, and business plans.

I have over 32 years of experience with the Postal Service working in many functional areas. I have had executive leadership roles including product management and development, domestic and international package strategy, and technology planning and analysis.

I hold a Master of Business Administration degree in finance from the University of Maryland and a Bachelor's degree in management from the State University of New York at Geneseo.

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ASSOCIATED LIBRARY REFERENCES

2

I sponsor the following non-public USPS Library Reference that is associated

3

with my testimony: USPS-LR-N2021-2-NP3.

EXECUTIVE SUMMARY

Background: Many of the trends in consumer behavior observed during the COVID-19 pandemic in 2020 and 2021, including growth in the e-commerce market, are expected to continue in the coming years. In developing the Postal Service's Integrated Financial Plan, we forecasted that e-commerce would grow by 32.7 percent in FY 2020 and 5.1 percent in FY 2021.¹ We observed volume growth of 18.8 percent in FY 2020 across our Shipping and Package volumes, and expect the growth of e-commerce will sustain higher package volumes relative to pre-pandemic.² In addition to e-commerce growth, package volumes increasingly originate closer to end customer locations, as retailers fulfill their products closer to the end consumer.³

The Postal Service's First-Class Package Service ("FCPS") product is part of our domestic competitive product and solutions portfolio. FCPS is an "ounce-based" product, meaning it competes in the less-than-one-pound space and is priced by ounce and by zone.⁴ Historically from FY 2014 to FY 2019, FCPS volumes have grown at approximately 10 percent every year.^{5,6,7} In FY 2020, FCPS volumes increased by 32.2 percent compared to the prior year.⁸ Revenue and volume increased due to the surge

¹ USPS Fiscal Year 2021 Integrated Financial Plan, Nov. 24, 2020, p.3 (<https://www.prc.gov/dockets/document/115156>) (hereinafter "USPS FY 2020 Integrated Financial Plan").

² USPS FY 2020 10-K, p. 27 (<https://about.usps.com/what/financials/10k-reports/fy2020.pdf>) (hereinafter "USPS FY 2020 10-K").

³ USPS Delivering for America - Our Vision and Ten-Year Plan to Achieve Financial Sustainability and Service Excellence, p. 22 (https://about.usps.com/what/strategic-plans/delivering-for-america/assets/USPS_Delivering-For-America.pdf) (hereinafter "USPS Delivering for America").

⁴ FCPS was made a zone-based product in Docket No. CP2019-3.

⁵ USPS FY 2020 10-K, p. 28.

⁶ USPS FY 2017 10-K, p. 21 (<https://about.usps.com/what/financials/10k-reports/fy2017.pdf>).

⁷ USPS FY 2014 10-K, p. 18 (<https://about.usps.com/what/financials/10k-reports/fy2014.pdf>).

⁸ USPS FY 2020 10-K, p. 29.

1 in e-commerce from the pandemic.⁹ The Postal Service projects that FCPS will continue
2 to show modest growth, driven by its competitiveness in both price and service.¹⁰

3 As described by witness Hagenstein (USPS-T-1), the Postal Service is proposing
4 modifications to current FCPS service standards by integrating FCPS into a more
5 efficient coast-to-coast First-Class Mail (“FCM”) surface network and reducing the use
6 of air transport.¹¹ The changes to the service standards will affect FCPS volumes as
7 follows: approximately 32 percent of FCPS volumes, predominantly in higher shipping
8 zones, will shift from a 3-day service standard to a 4 or 5-day service standard. 64
9 percent of volumes will not experience changes to their service standards and would
10 continue to receive a 2 to 3-day service. In addition, the reach of the 2-day service
11 standard would be expanded. The remaining 4 percent of volumes will upgrade from a
12 3-day service to a 2-day service.

13 These modifications will enable network improvements to enhance our overall
14 on-time delivery and reliability, and meet the Postal Service’s stated goal to achieve 95
15 percent on-time performance.¹² It will also reduce operating costs. My testimony
16 describes the lightweight market landscape and the volume impact that we expect from
17 these proposed service standard changes.

18 **Summary of the Impact of Proposed Service Standard Changes:** First-Class
19 Package Service currently offers the best value proposition of fast delivery times and
20 low prices within the lightweight market. We expect FCPS will continue to show modest

⁹ *Id.*

¹⁰ USPS Fiscal Year 2021 Integrated Financial Plan, p. 4.

¹¹ Direct Testimony of Stephen B. Hagenstein on Behalf of the United States Postal Service (USPS-T-1), PRC Docket No. N2021-2 (June 17, 2021) (hereinafter “Hagenstein Direct Testimony”).

¹² USPS Delivering for America, p. 5.

1 growth over the coming years.¹³ We believe that the majority of current FCPS
2 customers choose FCPS for its price leadership, and will continue using FCPS after the
3 proposed service standard changes because of the enhanced reliability that will come
4 from these service changes and our competitive price in the marketplace.

5 **I. BACKGROUND**

6 **A. Definition of First-Class Package Service**

7 The Postal Service provides a shipping product portfolio that caters to the varied
8 needs of shipping customers. Our lightweight, less-than-one-pound shipping products
9 consist of First-Class Package Service, which consists of Retail (“FCPS-Retail”) and
10 Commercial (“FCPS-Commercial”) price categories, and Parcel Select Lightweight
11 (“PSLW”).

12 FCPS-Retail and FCPS-Commercial are full network offerings, which use the
13 end-to-end Postal Service network. FCPS-Retail is available to customers shipping
14 packages weighing less than 13 ounces at Post Office locations. FCPS-Commercial is
15 available to commercial and online customers shipping packages weighing less than 16
16 ounces. Both FCPS-Retail and FCPS-Commercial are priced according the zone-based
17 distance from the origin of the package to the destination delivery location. FCPS
18 service standards are currently 2 to 3 days within the contiguous United States. FCPS
19 packages have been historically transported by both ground and air transportation, with
20 42 percent of FCPS parcels transported via air.¹⁴

¹³ USPS Fiscal Year 2021 Integrated Financial Plan, p. 4.

¹⁴ USPS Delivering for America, p. 11.

1 PSLW is our commercial-based less-than-one-pound economy last-mile solution
2 for customers who prepare and enter packages into our network closer to the
3 destination. This service is primarily designed for large and medium-sized shippers
4 looking for an economical ground delivery service for the last-mile, whereas FCPS is an
5 end-to-end shipping solution.

6 **B. Trends within E-Commerce Market**

7 During the pandemic, the package market has experienced significant e-
8 commerce growth due to changes in consumer behavior and expectations. We
9 forecasted that e-commerce would grow by 32.7 percent in FY 2020 and 5.1 in FY
10 2021.¹⁵ We experienced an increased volume growth of 18.8 percent in FY 2020 across
11 our Shipping and Package volumes.¹⁶ This growth was driven by increasing consumer
12 reliance on the safety and convenience of e-commerce.¹⁷ We expect this new normal
13 within e-commerce to sustain package volumes at elevated levels relative to prior-year
14 trends.¹⁸ These trends have contributed to the volume growth of our lightweight
15 products, particularly from commercial customers.¹⁹ In FY 2021, Quarter 2, USPS'
16 ounce-weighted products represented approximately 60% of the Postal Service's total
17 domestic package growth in the quarter vs. the same period in FY 2020.²⁰

¹⁵ USPS FY 2020 Integrated Financial Plan, p. 3.

¹⁶ USPS FY 2020 10-K, p. 27.

¹⁷ USPS FY 2020 10-K, p. 21.

¹⁸ *Id.*

¹⁹ USPS FY 2020 10-K, p. 29.

²⁰ USPS Revenue, Pieces & Weight (RPW) Quarter II FY 2021.

1 Across shipping products, the top driver of shipping satisfaction for commercial
2 shippers in FY 2020 is high reliability.²¹ According to external market research, the
3 drivers of satisfaction with greatest importance for shippers are: 1) reliability, 2) offering
4 the best end-to-end service; 3) delivering items to destination as fast as possible; 4)
5 delivering packages on the exact day that I expect it; and 5) offering my business the
6 tracking information we need to assist customers.²² These drivers of satisfaction
7 remained the same as the previous year. We expect that reliability will continue to be a
8 key driver of satisfaction for our shipping customers. Therefore, as we improve our
9 service reliability for our FCPS product, we believe opportunity exists to capture
10 additional package volume and drive incremental market share.

11 **C. Trends in First-Class Package Service Volume**

12 Historically, FCPS demonstrated consistent growth across FCPS-Retail and
13 FCPS-Commercial volumes. In FY 2020, FCPS volumes totaled 1.8 billion.²³ The
14 majority of FCPS volume is driven by the FCPS-Commercial price category. FCPS
15 volumes have increased by 10.6 percent in FY 2018, 9.2 percent in FY 2019, and 32.2
16 percent in FY 2020.^{24, 25} The Postal Service projects a modest increase in FCPS
17 volumes, driven by its competitiveness in both price and service.²⁶

²¹ USPS Market Research & Insights Q1 FY21 Brand Health Tracker – Shipping Services.

²² *Id.*

²³ USPS FY 2020 Annual Report, p. 25 (<https://about.usps.com/what/financials/annual-reports/fy2020.pdf>) (hereinafter “FY 2020 Annual Report”).

²⁴ USPS FY 2020 Annual Report, p. 25.

²⁵ USPS FY 2019 Annual Report, p. 13 (<https://about.usps.com/what/financials/annual-reports/fy2019.pdf>).

²⁶ FY 2020 Integrated Financial Plan pg. 4.

1 Key customer segments that use FCPS include marketplaces, pharmaceutical
2 companies, mass merchants, and apparel retailers. Two of our largest FCPS customer
3 segments are online marketplaces and pharmaceutical companies. Marketplaces make
4 multiple products available to shoppers by consolidating merchants on their platform.
5 Marketplaces are a key conduit for small and medium-sized businesses to access our
6 FCPS product. Pharmaceutical companies are another key customer segment that use
7 FCPS to ship packages (generally prescriptions) weighing less than a pound.

8 **D. Proposed Changes to First-Class Package Service Standards**

9 The Postal Service plans to shift portions of First-Class Package Service
10 volumes to an enhanced ground network to improve on-time reliability for our customers
11 and reduce costs in our network. As described by witness Hagenstein (USPS-T-1), the
12 Postal Service proposes that 31 percent of the FCPS volume that currently flies on air
13 will shift to surface transportation. We aim to achieve 95 percent on-time reliability and
14 improve the current reach of 2-day volumes, which aligns with the key customer
15 demand driver of reliable, consistent, on-time delivery, and the importance of regional
16 delivery in today's marketplace. Under this model, approximately 32 percent of current
17 FCPS volumes with a 3-day service standard would have a 4-day or 5-day service
18 standard. Four percent of current FCPS volumes with a 3-day service standard would
19 upgrade to a 2-day service standard. This would leave 64 percent of FCPS volumes
20 with unimpacted service standards.

21 **II. ESTIMATE OF IMPACT ON FIRST-CLASS PACKAGE SERVICE**

22 **A. Methodology**

23 To evaluate the impact of changes to FCPS service standards on current users
24 of FCPS – Commercial, the Postal Service retained The Colography Group to conduct

1 primary survey research titled the First-Class Package Service Transit Commitment
2 Survey (“FTC Survey”). The objectives of this survey were to assess if, and how much,
3 volume would switch to other delivery services if transit time commitments for volume
4 shipped to farther zones were slowed by 1 to 2 days, but if on-time performance were to
5 increase to 95 percent across all zones.

6 The survey compiled results from 458 respondents that currently use FCPS. The
7 survey stratification was designed to encompass FCPS shippers across industrial
8 divisions and average daily shipping frequency. A portion of the sample was sourced
9 from The Colography Group’s CY 2020 National Survey of U.S. Expedited Cargo with
10 the following selection criteria: respondents that affirmed using FCPS to ship packages,
11 or respondents that ship packages that weigh less-than-one-pound via 2 or 3-day air or
12 ground parcel across any Postal Service competitive shipping products. A sample of
13 Postal Service First-Class shippers was used to supplement the study across average
14 daily volume categories and industry segments.

15 **B. First-Class Package Service Findings**

16 The Postal Service provides price-competitive rates for packages that weigh
17 less-than-one-pound. FTC Survey respondents most frequently cited price as the
18 primary reason for using FCPS.²⁷ FCPS is positively differentiated by its price compared
19 to other market offerings with similar service standards, and we expect FCPS will
20 continue to be highly price-competitive in the lightweight package market in the future.

21 Based on this research, after the proposed changes to FCPS service standards,
22 we expect that we will maintain current FCPS volumes due to our highly competitive

²⁷ The Colography Group’s “First-Class Package Service Transit Commitment Survey,” Apr. 2021.

1 prices and improved reliability in meeting service expectations. We expect to maintain
2 current FCPS-Retail volumes given these factors and the convenience to retail
3 customers of accessing our package products through our extensive retail network. If
4 FCPS-Retail customers seek a faster delivery time, they have the option of choosing
5 our Priority Mail product, and thus able to readily substitute at one of our retail locations.
6 Regarding FCPS-Commercial volumes, FTC Survey results show that the majority of
7 sampled FCPS-Commercial shippers stated they would maintain or, in some cases,
8 increase FCPS volumes with these proposed changes.²⁸ Analysis from the survey
9 responses provides a foundation to estimate that the directional impact on commercial
10 FCPS volumes will be relatively insignificant. Therefore, we expect that FCPS volumes
11 will not be materially affected after the proposed changes to FCPS service standards
12 are implemented. This expectation could be conservative because as noted above we
13 believe there could be opportunities to capture additional package volume and drive
14 incremental market share through greater reliability. Given the overall trends in the
15 lightweight package market, we expect FCPS will continue to show modest growth over
16 the coming years.

17 **III. CONCLUSION**

18 The Postal Service aims to provide more reliable service for lightweight packages
19 by moving volumes historically transported via air to the ground. We aim to improve
20 transportation efficiency and reduce costs to serve through the proposed service
21 standard changes. According to current market trends, we predict a sustained e-
22 commerce growth and growth among local volumes. Additionally, given FCPS' value

²⁸ The Colography Group's "First-Class Package Service Transit Commitment Survey," Apr. 2021.

- 1 proposition in offering price-competitive ounce-based rates at improved reliability, in
- 2 conjunction with these market trends, we estimate there will be no net impact on FCPS
- 3 volumes within our network.