

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

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POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

POSTAL RATE AND FEE CHANGES, 2000

Docket No. R2000-1

RESPONSE OF UNITED STATES POSTAL SERVICE
WITNESS MUSGRAVE TO INTERROGATORIES OF
THE DIRECT MARKETING ASSOCIATION, INC.
(DMA/USPS-T8-1-3)

The United States Postal Service hereby provides the responses of witness Musgrave to the following interrogatories of the Direct Marketing Association, Inc.:
DMA/USPS-T8-1-3, filed on February 9, 2000.

Each interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

Daniel J. Foucheaux, Jr.
Chief Counsel, Ratemaking



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February 23, 2000

**RESPONSE OF UNITED STATES POSTAL SERVICE WITNESS MUSGRAVE
TO INTERROGATORIES OF DIRECT MARKETING ASSOCIATION, INC.**

DMA/USPS-T8-1. Please refer to the PFY 2000, Accounting Period (A/P) 4 (12/4/99-12/31/99) Financial and Operating Statements and note that PFY 2000, A/P 4 Priority Mail volume was up 18.3 percent over the same period last year (SPLY) and that year-to-date Priority Mail volume was up 3.9 percent over SPLY.

- a. Please confirm that between PFY 1999, A/P 4 and PFY 2000, A/P 4, the Postal Service raised Priority Mail rates by six percent. If not confirmed, by what percent did the Postal Service raise Priority Mail rates.
- b. Please confirm that year-to-date (through A/P 4) average revenue per piece for Priority Mail was approximately ten percent more than SPLY. If not confirmed, by what percent did average revenue per piece increase.
- c. Please confirm that between PFY 1999, A/P 4 and PFY 2000, A/P 4, the transitional weight between First-Class Mail and Priority Mail increased from 11 ounces to 13 ounces.
- d. If the transitional weight between First-Class Mail and Priority Mail had not increased between PFY 1999, A/P 4 and PFY 2000, A/P 4, approximately how much higher would Priority Mail volumes have been in PFY 2000, A/P 4? How much higher would year-to-date Priority Mail volumes have been?
- e. If Priority Mail rates had not been raised between PFY 1999, A/P 4 and PFY 2000, A/P 4, approximately how much higher would Priority Mail volumes have been in PFY 2000, A/P 4? Approximately how much higher would year-to-date Priority Mail volumes have been?
- f. To what do you attribute the significant growth in Priority Mail volumes between PFY 1999, A/P 4 to PFY 2000, A/P 4? Do you believe that this is a trend or a one-time event?

Response:

(a)-(f) The Priority Mail model is based on quarterly postal volume data. I do not use Accounting Period (AP) data in the model and cannot respond on that basis. However, quarter one data are available, they would cover the first three APs, and they are the closest available data to your question. I can respond on that basis. Furthermore, going beyond that and attempting to ascertain the impact of one or several additional four-week AP periods is not recommended because the AP data are quite volatile and subject to revision.

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DMA/USPS-T8-1. Continued

I hasten to add that appraising a model's forecasts based on one or several quarters' data is equally problematic. For example, in R97-1, for the first forecast quarter (97:3), the forecast was 2.1 percent high. However, the test year PFY 1998 was 3.8 percent low. Using the quarter to appraise or adjust the test-year forecast would have been in the wrong direction. When the revised data were used (i.e., actual rather than forecasted values of the exogenous variables), the volume forecast for PFY 1998 was approximately 1,168 million pieces and the actual value also was approximately 1,168 million pieces, see my Technical Appendix E, page 6.

- a. The increase in the Priority Mail fixed-weight price index from 1999:1 to 2000:1 is approximately 8.2 percent.
- b. The increase in the average revenue from 1999:1 to 2000:1 is approximately 10 percent.
- c. The weight limit was increased from 11 to 13 ounces.
- d. The increase in volume would have been approximately 34 million pieces in 2000:1.

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DMA/USPS-T8-1. Continued

e. I have not made that calculation.

f. The "growth" in the first quarter has actually been negative, a decline of 1.9 percent in the volume between PFY1999:1 and PFY 2000:1. Two important volume reducing influences are the increase in rates and the increase in the weight limit. These influences are forecast to diminish in subsequent quarters and, combined with other factors, result in a positive growth for the year. Thus, I do not believe the first quarter's result is a trend.

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DMA/USPS-T8-2. Please refer to Page 6 of your testimony and note that you are only projecting a 1.5 percent volume increase for Priority Mail from PFY 1999 to PFY 2000. Also, please refer to your response to question 1 above.

- a. Please confirm that if Priority Mail volumes for A/P 5-13 increase by more than 0.3 percent over SPLY, PFY 2000 Priority Mail volumes will be underestimated. If not confirmed, please explain.
- b. In light of your response to question (1) above, do you expect PFY 2000, NP 5-13 Priority Mail volumes to grow by only 0.3 percent over SPLY. If yes, please explain in detail why you expect this given YTD performance of Priority Mail volumes. If no, by what percent do you expect A/P 5-13 volumes to grow over SPLY?
- c. In light of your response to part (b) of this question, what is your current forecast of PFY 2000 Priority Mail volume? Please explain the method you used to develop this forecast.

Response:

(a)-(c) As indicated in response to question 1, the use of AP data, as well as the use of partial year data, is problematic in evaluating the annual forecast. Also, it is very difficult to extend AP or partial year results to make or improve annual forecasts.

- a. Based on the first quarter's results of 282.715 million pieces, the subsequent three quarters could sum to 923.157 million pieces. In that case, the annual total would be equal to our PFY 2000 forecast of 1205.872. In this case, there would be no underestimate. These three quarters would be approximately 2.6 percent higher over SPLY. If they were the actual values, they would be within approximately 1.2 of the forecast of 934.148 million pieces in my testimony.

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DMA/USPS-T8-2. Continued

(b) and (c) Volumes in quarters two through four could grow at an average rate of 2.6 percent, over SPLY. I expect the volumes to be as stated in my testimony.

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DMA/USPS-T8-3. Please refer to your testimony. Does your model take into account the 1999 boom in e-commerce and the anticipated growth in e-commerce in 2000 and 2001? If so, please explain in detail how you have taken this into account. If not, please confirm that ignoring the growth in e-commerce would result in an understatement of FY 2000 and Test Year Priority Mail volume.

Response:

There are likely to be two principal e-commerce impacts on Priority Mail. One impact is to increase package volume via more merchandise shipments. The second impact is to decrease the correspondence and data volume via the substitution of electronic for paper-based communication. At the present time, it does not appear that one force dominates the other. Because of this, it is not possible, at this time, to determine the net impact of e-commerce on Priority Mail.

DECLARATION

I, Gerald L. Musgrave, declare under penalty of perjury that the foregoing answers are true and correct to the best of my knowledge, information, and belief.

G. Musgrave

Dated: 2/21/00

CERTIFICATE OF SERVICE

I hereby certify that I have this day served the foregoing document upon all participants of record in this proceeding in accordance with section 12 of the Rules of Practice.



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