

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 TOLLEY TO INTERROGATORIES OF
THE ASSOCIATION OF AMERICAN PUBLISHERS
(AAP/USPS-T6-1-13, 15-18)

The United States Postal Service hereby provides the responses of witness Tolley to the following interrogatories of AAP: AAP/USPS-T6-1-13, 15-18, filed on February 18, 2000. Interrogatories AAP/USPS-T6-14 and 19 were redirected to witness Thress.

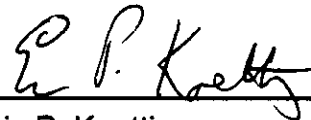
Each interrogatory is stated verbatim and is followed by the response.

Respectfully submitted,

UNITED STATES POSTAL SERVICE

By its attorneys:

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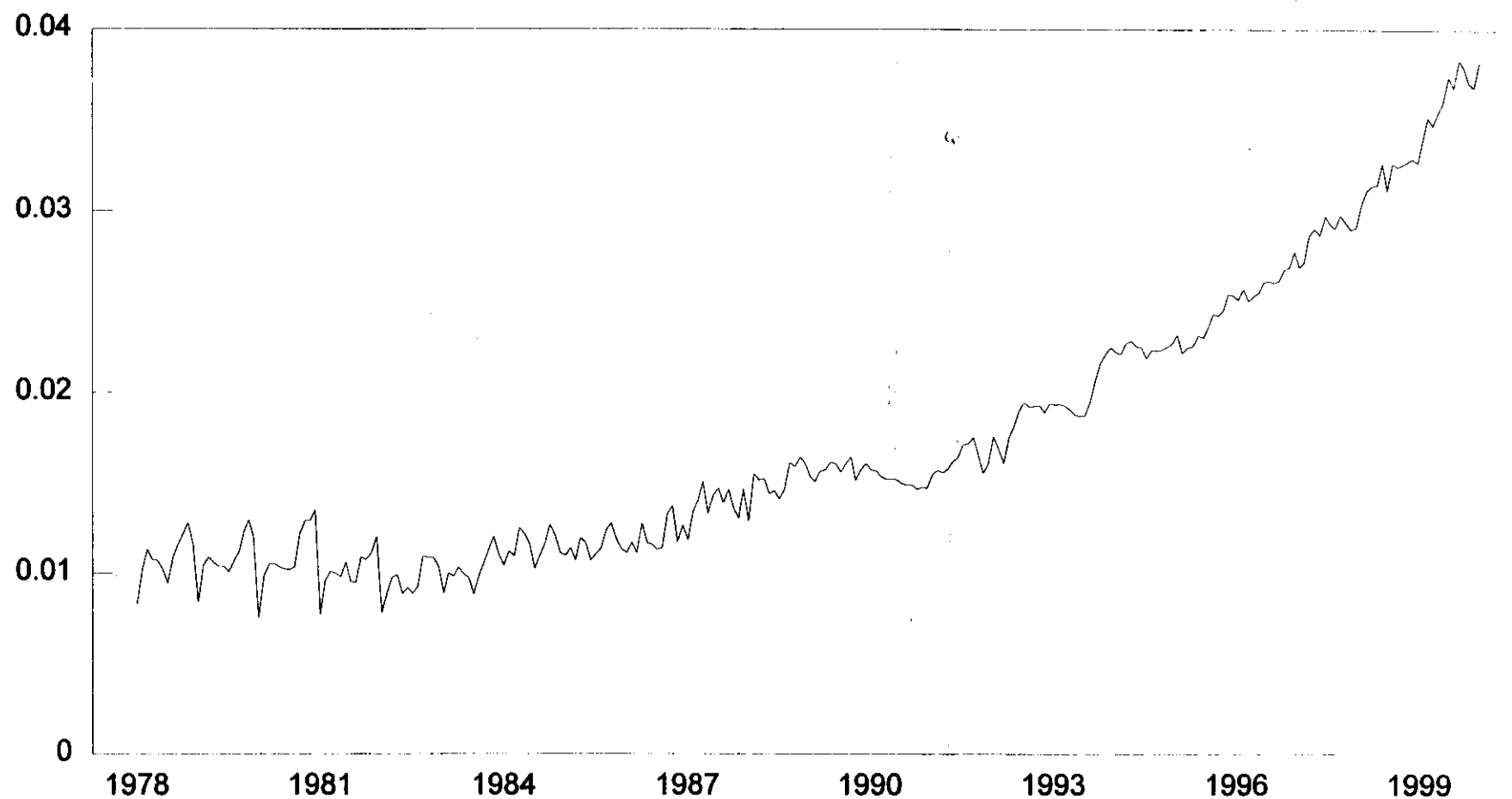
RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
INTERROGATORIES OF ASSOCIATION OF AMERICAN PUBLISHERS

AAP/USPS-T6-1 On pages 167 and 168 of your testimony, you state that "Much of this long-term growth in Bound Printed Matter ("BPM") volume is due to the mail order boom and the expansion of the catalog industry." Please identify and provide all studies, reports, data or other evidence that you relied upon to support this statement.

RESPONSE:

Since bound printed matter contains catalogs and mail-order deliveries, an expansion of the mail-order and catalog industry can be expected to lead to an increase in bound printed matter volume. The attached chart shows real per-capita mail-order retail sales from 1978 through 1999, indicating that real per-capita mail-order retail sales have increased by a factor of four since 1978.

Figure accompanying response to AAP/USPS-T6-1
Real Mail-Order Sales per Adult, Seasonally Adjusted



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AAP/USPS-T6-2 On page 168 of your testimony, you state that the "pattern of volume growth of Bound Printed Matter is consistent with a market penetration Z-variable."

(a) Please explain fully, with numerical examples, how volume growth in BPM is consistent with "a market penetration Z-variable."

(b) Please explain in particular what "market" is being analyzed using a "market penetration Z-variable" for BPM.

(c) Please provide a complete explanation with supporting references of the theoretical basis you relied upon to justify this use of a "market penetration Z-variable" used for BPM.

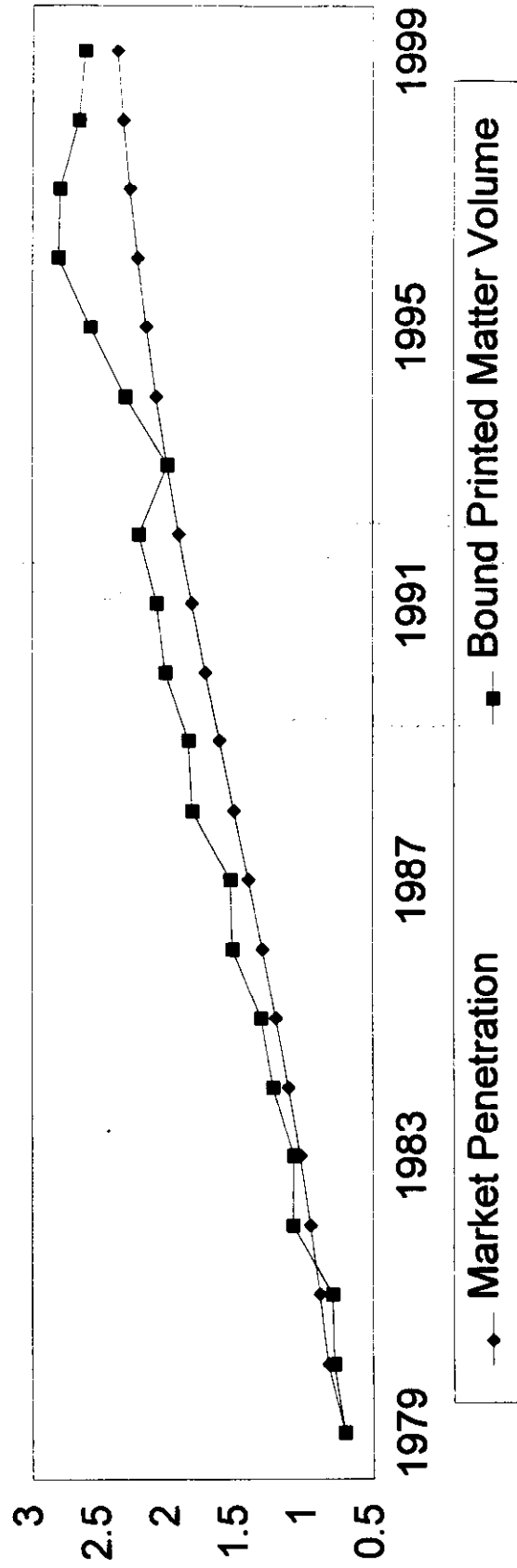
RESPONSE:

(a) Please see the attached figure which presents bound printed matter volume per adult as well as the "market penetration Z-variable" used to forecast bound printed matter volume for the time period 1979 through 1999. It is apparent that the market penetration variable tracks bound printed matter volume relatively closely. The market penetration variable is not the only factor affecting bound printed matter volume, which is also affected by permanent income, the price of bound printed matter, and several dummy variables, as described in my testimony.

(b) The "market" here represents the market for bound printed matter.

(c) Please see the testimony of witness Thress, USPS-T-7, in this case, at pages 124 through 128, for a description of the market penetration variable. This "market penetration Z-variable" construction is based on the marketing theory of new product diffusion. This theory is discussed, for example, in "New product diffusion models in marketing: A review and directions for research" by V. Mahajan, E. Muller, and F. M. Bass, in Journal of Marketing, 54, 1 (January, 1990), pp. 1 - 26.

Figure accompanying response to AAP/USPS-T6-2(a)



**RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAP/USPS-T6-3 On page 170 of your testimony, you state that "Ultimately Sears replaced its large catalog with smaller catalogs, many of which were also sent as Bound Printed Matter."

(a) Please identify and provide copies of all documents, studies, reports, data or other evidence relied upon to support this statement.

(b) Please state how many smaller catalogs were sent as BPM in 1996, 1997, 1998 and 1999.

RESPONSE:

(a) In January of 1993, Sears announced that they were ceasing publication of their main catalog. From the second quarter of 1993 through the first quarter of 1994 (note that Postal years begin in September of the previous calendar year; the time period cited here, 1993Q2 through 1994Q1, went from December 12, 1992 through December 10, 1993), bound printed matter volume declined by 8.6 percent over the same period one year earlier. This decline in bound printed matter volume was attributed to the cancellation of the Sears catalog.

The following four quarters (1994Q2 through 1995Q1), bound printed matter volume grew by 22.0 percent. This phenomenon is apparent in the figure accompanying my response to interrogatory 2 above.

The quote which you cite on page 170 represents my hypothesis to explain this phenomenon.

(b) I do not have these figures.

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AAP/USPS-T6-4 On page 170 of your testimony, you state that "Bound Printed Matter Volume experienced a sudden decline beginning in 1998q1." Please provide an explanation for the decline. If no explanation can be provided by you, identify any other USPS witnesses who may be able to provide the explanation for the decline.

RESPONSE:

I am unaware of the cause of this decline. I am unaware of any Postal Service witnesses who would be able to provide an explanation.

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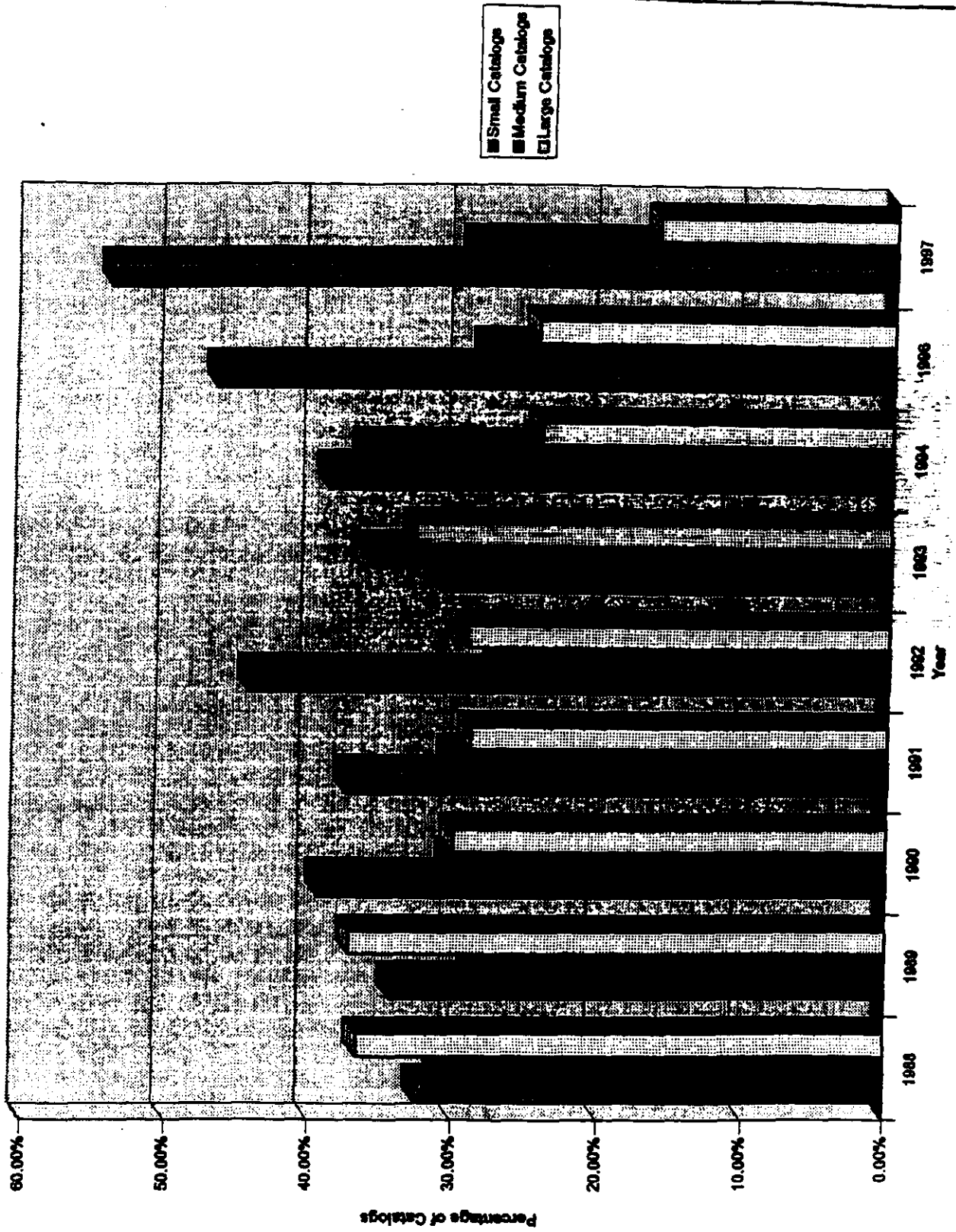
AAP/USPS-T6-5 Please identify and provide all documents, studies, reports, data or other evidence upon which you relied to conclude that the "Other Factors" described at page 171 of your testimony related in any way to the delivery trends in catalogs you describe on pages 171 and 172 of your testimony.

RESPONSE:

Included in the discussion of "Other Factors" are references to articles from *Traffic World* and *Traffic Management* (provided in my response to your interrogatory 7), a discussion of employment trends (provided in my responses to your interrogatories 8 and 9), and a review of information regarding the shift from larger to smaller catalogs obtained from several of the Direct Marketing Association, *Statistical Fact Books* and summarized in the table accompanying this response.

Figure accompanying response to AAP/USPS-T6-5

NUMBER OF PAGES IN PRIMARY CATALOG



**RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAPP/USPS-T6-6 On page 171 (lines 6-7) of your testimony, you state that "One of the major components of Bound Printed Matter is catalogs weighing between one and ten pounds." With respect to this statement:

- (a) Please list all of the other known components of BPM.
- (b) Please state the volume of BPM that consists of catalogs for each of the years 1994-1999. Include source references to support your response.
- (c) Please state the volume of BPM that consists of books for each of the years 1994-1999. Include source references to support your response.
- (d) Please state the volume of BPM that consists of components that are not catalogs and are not books for each of the five years (1994-1999). Include source references to support your response.

RESPONSE:

- (a) In addition to catalogs, another component of bound printed matter is books. Matter which is bound and printed, but would not be characterized as either catalogs or books, can also be sent as bound printed matter.
- (b) According to the Household Diary Study, the following percentage of bound printed matter received by households was characterized as catalogs for each year from 1994 through 1998 (the 1999 Household Diary Study is not available at this time).

**Percentage of Bound Printed Matter
That Are Catalogs**

1994	27.5%
1995	39.3%
1996	36.8%
1997	44.3%
1998	29.4%
1994 - 1998	35.6%

- (c) According to the Household Diary Study, the following percentage of bound printed matter received by households was characterized as books for each year from

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1994 through 1998 (the 1999 Household Diary Study is not available at this time).

**Percentage of Bound Printed Matter
That Are Books**

1994	66.0%
1995	41.9%
1996	41.7%
1997	44.1%
1998	63.7%
1994 - 1998	50.7%

(d) According to the Household Diary Study, the following percentage of bound printed matter received by households was characterized as neither catalogs nor books for each year from 1994 through 1998 (the 1999 Household Diary Study is not available at this time). The numbers in 1994 sum to greater than 100 percent because 1.2 percent of bound printed matter was classified as both catalogs and books that year.

**Percentage of Bound Printed Matter
That Are Neither Catalogs Nor Books**

1994	7.7%
1995	18.7%
1996	21.5%
1997	11.6%
1998	6.9%
1994 - 1998	14.0%

RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAP/USPS-T6-7 Please provide the *Traffic World* and *Traffic Management* articles cited on page 171 of your testimony.

RESPONSE:

These reports accompany this response.

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Mail order business
Delivery services

Expanding mail-order delivery business creates opportunity for carriers, post office

by Ann Saccomano

The mail-order business just may be the stuff that dreams are made of, at least for carriers and logistics providers. It's a market that is delivered at least twice, first as a catalog and again as a packaged product. Sometimes companies even get a third bite, when merchandise is returned.

Today those segments are attracting a lot of attention from private carriers and the U.S. Postal Service, which are competing for a competitive edge through offers of better service and lower rates.

The U.S. Postal Service generated 7.3 million in revenue, according to a Direct Marketing Association, the 99.4 million Americans shopping from home—a number that will increase as cable television and line shopping services reach more people.

The Postal Service has 95 percent of the catalog distribution business, adding 14 billion catalogs in various mail classes, said Kent E. Smith, a USPS marketing specialist. On the direct delivery side, USPS has 40 percent of the business-to-household market, while United Parcel Services leads in the business-to-business segment.

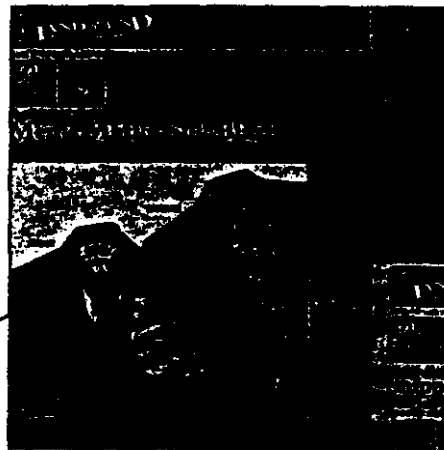
"It's the call vs. the mail."

— FedEx's Datzell

There's a little deception in the post office's ironclad grip on the front end, however. Truckers and small parcel carriers are finding success in "zone skipping." The practice takes its name from the Postal Service's eight nationwide delivery zones, which are used to determine rates for third- and fourth-class mail. They take on the job of consolidating catalogs into full truckloads

and then hauling them to the USPS distribution center nearest the point of delivery. USPS picks it up from there to make the final delivery.

The practice has taken a surge within the last three years, according to Sidney Klavatt, senior vice president of



marketing at The Sharper Image, which distributes 35 million catalogs a year. He dates the popularity of zone skipping to the 1991 postal increase, which made it cheaper for shippers to work with private carriers with than USPS.

Surprisingly, zone skipping is just fine with the Postal Service, which actively encourages the practice and even offers to sit down with shippers and help them figure out a way to do it. The motive stems from a fear of actually turning a profit, explain USPS spokesman Mark R. Saunders. "By law we're not allowed to make a profit; we're only allowed to break even. That's the price we pay for having a monopoly on first-class mail."

The savings can be sizable. Saunders estimates shippers who use zone skipping, along with USPS work-sharing discounts and bar coding can save as much as 50 percent on their mailings over standard bulk mail.

One company that has been doing just that is CTC Distribution Services in St. Paul, Minn. With nine processing centers across the country, CTC consolidates and distributes both catalogs

and filled orders. Through zone skipping and discounts, the company maintains it was able to save its customers \$56 million last year, handling a total of 55 million packages. "Our customers can save from 7 to 19 percent. That will vary based on the zone and the weight of the parcel," said Sheri Reis, a CTC spokeswoman.

And it's cost, not speed, that counts at the front end of the mail-order business. In the past, shippers thought the timing of catalog deliveries was crucial to garnering sales. That's not true today, noted Thomas

Dromey, a vice president of PMC Logistics Inc. of Plymouth, Mass. PMC counts 10 catalog suppliers among its 50 clients. "At one time the number of days it took to deliver was really important. Now we know if it gets there in four days instead of two it's not going to affect sales. People were using the overnight couriers, but that became expensive, so they started to look for other ways to deliver the mail."

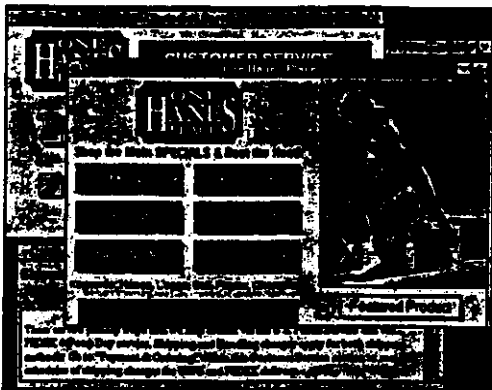
Where speed does count is at the back end. Once a customer places an order, instant gratification is the name of the game. People are less likely to cancel an order or return an item if it's delivered quickly. The longer an order stays unfilled, the more time for buyer remorse and second thoughts about the purchase. In that regard, home shopping's biggest competitor is local businesses.

It's "the call vs. the mail," Rob Datzell, a managing director of sales at Federal Express Corp., says of shoppers' priorities.

On the business-to-business end, direct marketers compete with local suppliers on quality and convenience.

BIS

Unfortunately for the post office, that's the general opinion of its bid for the two-day delivery window. Historically, USPS has not been able to guarantee that end of the service, but the agency plans to change its reputation



with an outsourcing partnership that is still taking shape. USPS has teamed

Taking the number one spot in mail-order package delivery is an ambitious goal for USPS, but it does reflect the agency's turnaround in emphasizing the quality of its operations, according to PMC's Dromey. "One of the things we've noticed over the past few years is that USPS is becoming more competitive. The postal service used to think it was in business for itself, but they've changed their outlook 100 percent."

THE UNITED STATES POST OFFICE

1. The first step in the process of the investigation is the identification of the problem. This is done by the investigator, who is usually a member of the research team. The investigator will identify the problem by looking at the data and trying to find out what is going on.

2. The second step is to define the problem. This is done by the investigator, who will define the problem in terms of the research question. The research question is a statement that describes the problem and what the investigator wants to find out.

3. The third step is to design the study. This is done by the investigator, who will design the study in terms of the research question. The study design is a plan that describes how the investigator will collect and analyze the data.

4. The fourth step is to collect the data. This is done by the investigator, who will collect the data in terms of the research question. The data collection is the process of gathering information about the problem.

5. The fifth step is to analyze the data. This is done by the investigator, who will analyze the data in terms of the research question. The data analysis is the process of looking at the data and trying to find out what it means.

6. The sixth step is to interpret the results. This is done by the investigator, who will interpret the results in terms of the research question. The interpretation is the process of looking at the results and trying to find out what they mean.

7. The seventh step is to write the report. This is done by the investigator, who will write the report in terms of the research question. The report is a document that describes the results of the investigation.

8. The eighth step is to present the results. This is done by the investigator, who will present the results in terms of the research question. The presentation is the process of showing the results to the research team.

9. The ninth step is to discuss the results. This is done by the investigator, who will discuss the results in terms of the research question. The discussion is the process of talking about the results and trying to find out what they mean.

10. The tenth step is to conclude the investigation. This is done by the investigator, who will conclude the investigation in terms of the research question. The conclusion is the final step in the process of the investigation.

[illegible][illegible]

1. The information contained in this document is unclassified and will remain so unless and until the information is determined to require classification in accordance with the provisions of the National Security Agency's (NSA) policy on the classification of information.

Dr. Ann Saccomano

Shipment of goods

Shipment of goods - How much
Shipment of goods - Carrier

1998

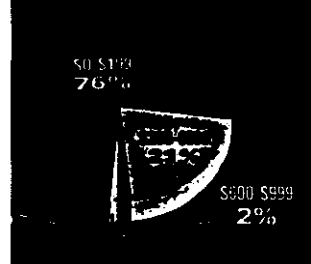
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Range of 1994 Transportation Expenditures

Billions of Dollars



Over three-quarters of the respondents spend less than \$200 million on freight transportation, but the amount they spend varies much more.

Is a "Giant"?

There is no dispute that the respondents of this year's Giants survey represent companies that are, indeed, giants. They report annual company sales in excess of \$9 billion. Another 17 percent of their company's annual sales fall between \$3 billion and \$9 billion. Only 17 percent of others put the figure at \$1 billion and \$3 billion. The remaining respondents report annual sales of less than \$1 billion.

Respondent companies also represent a cross-section of American industry. For instance, 34 percent of the respondents are from the industrial manufacturing sectors. 17 percent come from the paper or printing industries. Approximately 9 percent of the Giants represent the electronics and another 7 percent each come from the wholesale/retail, mining/petroleum, food-processing industries. The respondents' total annual transportation expenditures are consistent with what you'd expect for their company size. The average transportation expenditure for the respondents is a whopping \$647. Though the majority of the respondents (76 percent) report spending less than \$200 million a year on transportation, a fifth spend between \$200 million and \$999 million each year. (See Figure 1.) An additional 2 percent of the respondents spend between \$600 million and \$999 million a year. Finally, one respondent, a true giant, reports annual company transportation expenditures of over \$1 billion.

The Survey Methodology

As with the three previous Giants of Shipping research projects, the pool of respondents for this year's survey came from the list of the 500 largest U.S. companies identified each year by *Fortune* magazine. From that list, the research staff identified the 247 biggest manufacturers.

The research team then turned to *The Official Directory of Industrial and Commercial Traffic Executives*, popularly known as the "Blue Book," to determine the highest-ranking logistics executive at each of those corporations. After a preliminary mailing to verify addresses, the researchers were left with 216 usable names.

Each of those 216 logistics executives was contacted by phone and invited to participate in the survey either by mail or fax. From that pool of 216, the researchers received 78 completed surveys, representing an impressive 36-percent response rate. "While this is slightly lower than last year's rate, it is still well above average for such a long and detailed survey document," notes Dr. Karl Man-

rodt, director of the University of Tennessee's Office for Customer Responsiveness Studies and one of the leaders of the annual Giants research effort.

Manrodt also reported that of the 76 respondents, 42 percent indicated they had also participated in last year's survey. If this trend continues, he says, the project will gain even more value because it will be able to track responses over a period of time. "Valid tracking requires a high similarity in the respondent base from year to year," he notes.

Once the surveys were completed, Manrodt and his University of Tennessee graduate students forwarded them to Mercer Management Consulting for tabulation and analysis. Mercer then sent the results on to *Traffic Management* for further analysis and publication in this issue. The results also will be presented by representatives of the magazine, Mercer, and the University of Tennessee at this month's annual meeting of the Council of Logistics Management in San Diego.

Transportation Expenditures as a Percentage of Revenue

of Corporate Revenue
Spent on Freight

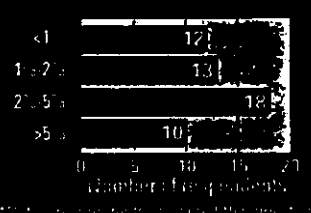


FIGURE 3 Though many managers report that their annual freight bill chews up between 2 and 5 percent of their company's annual revenues, the responses were fairly evenly split over a relatively wide range.

Measured another way, of the 53 survey respondents who provided information on their companies' annual transportation expenditures as a percentage of annual sales revenue, 18 (34 percent) fell in the 2- to 5-percent range. Ten of the respondents (19 percent) said their transportation bill chewed up more than 5 percent of annual sales. The remainder put that figure at under 2 percent. (See Figure 3.)

When asked whether the amount their companies spent on domestic freight transportation was increasing, decreasing, or holding firm, 65 percent of the respondents said the amount was on the rise. Eighteen percent found themselves in the enviable position of seeing their costs drop, while another 17 percent saw the amount holding at current levels.

How the Giants Cut Costs

Just because the Giants of Shipping are the biggest spenders in the country where freight transportation is concerned doesn't mean they aren't cost-conscious. In fact, just the opposite is true.

The nation's largest shippers employ a

wide variety of techniques to reduce their freight transportation expenses. The most popular practice, as indicated by 67 of this year's respondents (86 percent), is to form close partnerships with a few selected core carriers. Typically, the shippers guarantee large freight volumes to these carriers. In return, the carriers generally offer significant volume-based price breaks on freight rates.

Similarly, many shippers are formalizing negotiations with service providers—whether core carriers or not. More than two-thirds of the respondents reported that they had adopted a more structured approach to carrier negotiations as a way to keep costs down.

Another cost-reduction technique popular with this year's survey respondents is shipment consolidation. Fifty-nine respondents (76 percent) reported that they saved money by consolidating outbound shipments. And 46 (59 percent) said they had reduced their costs by doing the same with inbound freight.

Shippers also are saving money by shifting freight from one mode to another. Fifty-eight respondents (74 percent) said they had used this technique to keep costs in line.

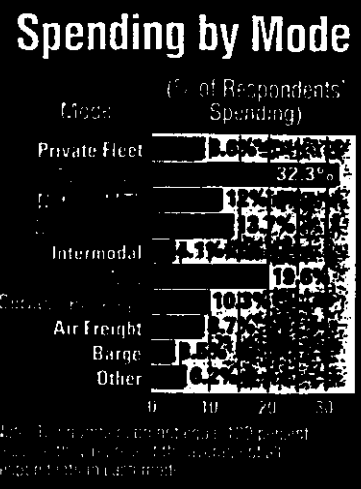
Other cost-cutting activities mentioned by respondents include accepting increases in transit time in certain lanes,

FIGURE 4 Over three-quarters of every freight dollar spent by the respondents goes to some sector of the motor freight industry.

improving use of technology, redesigning their transportation network, and developing a "continuous move" strategy, wherein carriers arrive at and leave the shippers' facilities with full loads of freight.

Spending by Mode

Consistent with the three previous Giants of Shipping reports, this year's findings show that motor freight consumes by far the largest share of the transportation dollars spent by the nation's biggest shippers.



How the Giants Measure Logistics

Though in past years, the Giants of Shipping research has focused primarily on overall freight transportation costs, changes on the U.S. business scene clearly indicate that companies are developing a broader perspective on logistics and its associated costs. This year's survey, for the first time, asked questions designed to gauge just how widespread this move toward an integrated logistics function is among the nation's biggest shippers. First, respondents were asked whether or not they currently measured total logistics costs for their corporation. Thirty-eight reported they did measure those costs; 24 said they did not, and 12 noted they expected to in the future. The Giants then were asked to identify those activities and costs they viewed as part of their overall logistics activity and to rate the level of difficulty of capturing cost data for each of the activities they identified. (See chart.)

Logistics Activities and Their Costs

Activity	No. of Respondents Identifying as a Logistics Cost	No. of Respondents Who Track the Cost	Level of Difficulty to Capture the Data
Freight transportation	38	38	3
Warehousing	38	38	3
Order fulfillment	38	38	3
Inventory management	38	38	3
Customer service	38	38	3
Other	38	38	3

The activities listed above were identified by the respondents as part of their Total Logistics Costs. Column Three shows how many respondents currently track these costs. The last column shows the level of difficulty of capturing cost data for each activity. (1 = Not Difficult, 5 = Very Difficult).

Overall, the survey shows that 40 percent of the money on trucking services (For purposes of the survey, motor freight services are defined as truckload, regional and national full-truckload services.) A detailed breakdown of spending across all modes is shown in Figure 4.

Accounting for the share of the market. The Giants say that they spend, on average, 19.6 percent of their freight dollars on rail services. Keep in mind that intermodal, on which the survey respondents spend another 4.1 percent of their transportation budget, generally represents a joint rail-truck move. Thus, the actual share held by motor freight and rail may be even higher than these figures suggest.

accounts for 8.1 percent of the Giants' transportation spending, while barge represents 3.5 percent. Though modal use varies markedly among industry segments, motor freight still grabs the largest share overall. In fact, with the exception of

3PLs' Role Still in Flux

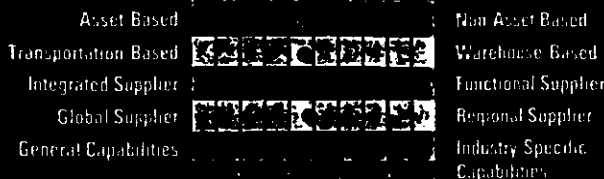
Recognizing the steadily increasing role of third-party (a.k.a. contract) logistics-service providers in the industry, the survey team asked this year's respondents for their views on various types of third-party providers and for input as to what specific logistics functions they were most likely to outsource.

When asked to identify the characteristics that will likely lead to a 3PL's success, the respondents were fairly evenly split in some key areas. For instance, roughly one-half of the respondents predicted that so-called asset-based 3PL companies (those that use their own—or a subsidiary's—equipment and facilities to serve customers) would enjoy success in the future. The other half believed that non-asset-based providers (those that do not perform any of the work themselves) would be more successful.

The responses broke down along similar lines when the respondents were asked to predict whether transportation-based or warehouse-based 3PL companies were more likely to be successful. They also were fairly evenly split when asked whether the most successful providers would be integrated suppliers offering a broad range of services or functional suppliers offering specific logistics outsourcing services as a specialty. And they were similarly divided on whether the future was brighter for providers with global capabilities or for those that limit service to a specific region. (See graph titled "What Do You Look for in a 3PL?")

The Giants did express consensus on one matter, how-

What Do You Look for in a 3PL?



Respondents were asked to predict what types of third-party logistics service providers will be most successful in the future, based on some general characteristics. If they preferred a characteristic listed on the left side, they circled either 1 or 2. If they preferred a characteristic listed on the right, they circled either 4 or 5. If they had no preference, they circled 3. The chart above shows the averages for each category.

ever. They indicated a distinct preference for those providers with industry-specific capabilities, as opposed to those with broad, general capabilities.

Current and Future Outsourcing

This year's survey respondents also were asked to identify those logistics activities they currently outsource and those they consider likely candidates for outsourcing in the future.

More than half of the 78 respondents currently outsource their company's freight bill audit and payment activity. Further, 22 more respondents say they are considering these activities for outsourcing in the future.

Another logistics function receiving frequent mentions was warehousing. Forty-four of the Giants said they already outsourced warehousing activity. Thirty others said they were considering it for the future (see chart at left).

On the other end of the spectrum, only two respondents currently outsource order entry/processing activity. Similarly, just five Giants outsource inventory management activities.

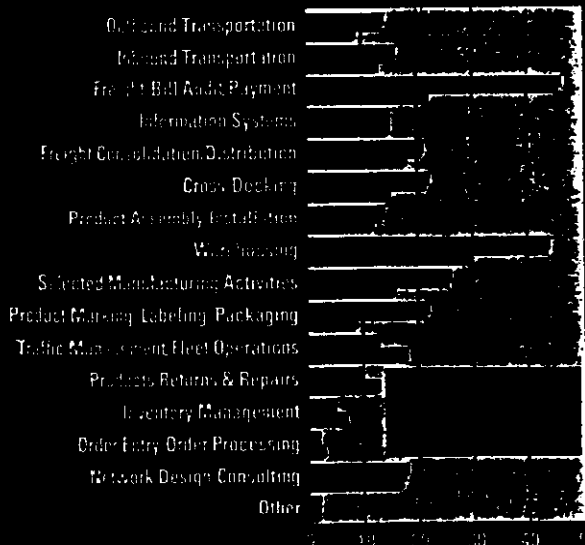
According to one of the lead project researchers, Dr. Mary Holcomb of the University of Tennessee, the selection of outsourcing candidates varies markedly from company to company. "Those activities that a firm deems part of its core competencies may be somewhat difficult for a third party to take over," she notes. "There is an aspect of control that must be addressed. It would be difficult for some companies to release certain functions that make them competitive in the marketplace."

Fellow researcher Barry Jennings, a principal of Mercer Management Consulting, agrees. "It really comes down to a question of ability and who can best manage these functions," he explains. Nonetheless, Jennings notes, an increasing number of senior managers are taking a close look at various functions to determine

whether or not they truly are core competencies. "When they ask themselves that question, and the answer comes up 'No,'" he says, "the search for a third-party provider begins." **Warehousing and freight bill audit/payment were the top vote getters when respondents were asked what they currently outsource and what they were considering outsourcing.**

What Are the Giants Outsourcing Today

(and What Will They Outsource Tomorrow)?



GIANTS

respondents from the mining and petroleum industries, who prefer rail, nearly all other industries represented in the survey named some aspect of trucking as their mode of choice.

When asked to identify the modes they were most likely to spend more on in the future, the respondents cited truckload, regional LTL, intermodal, and surface package. By contrast, the mode most often cited as likely to see a decrease was national LTL. (See Figure 5.)

The Corporate View

Continuing past practice, this year's survey also delved into attitudes and opinions of the nation's top transportation managers on logistics' role in their corporations. Despite the growing evidence that logistics is gaining stature with top management these days, many of our respondents (47, to be exact) indicated that their corporations still viewed transportation as a cost center. On the bright side, 20 respondents reported that their companies looked upon transportation as a strategic contributor to overall corporate operations. And four respondents went so far as to say that transportation in their companies was viewed as a profit/revenue center.

This year, the respondents also were asked to explain how well their logistics operation was integrated with other key corporate functions. Overall, the respondents identified distribution as the function with which their operation was best integrated. Next came purchasing, followed closely by

Outlook for Future Modal Use

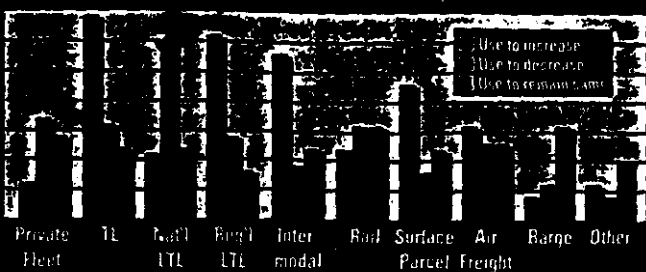


FIGURE 5: 47% of respondents expect their future modal use to increase, 20% expect it to decrease, and 33% expect it to remain the same. The modes most likely to see an increase are truckload, regional LTL, intermodal, and surface package.

manufacturing. Sales and management-information systems also received numerous mentions.

The generally solid level of integration between logistics and other corporate functions corresponds to some extent with the emergence of traffic councils in big companies. These councils, typically either a group of logistics executives or a cross-functional executive team representing logistics and other key corporate areas, plan logistics strategy and make logistics "buy" decisions. Use of traffic councils has steadily gained popularity since 1992, when we conducted our inaugural Giants of Shipping report.

This year, a full 54 percent of respondents said their companies used these councils to at least some extent. An additional 12 percent said they were considering using traffic councils in the future.

Whether it is accomplished through the formation of traffic councils or some other management practice, the trend toward integrating logistics with other corporate functions is expected to continue. The reason is simple: logistics is the backbone of a company's overall operations.

"Transportation will get increasing visibility in companies because it is a major enabler of cycle-time efficiency," notes Barry Jennings, a principal at Mercer Management Consulting and one of the leaders of the Giants of Shipping research project. "Transportation has a direct impact on things like cycle-time performance, cost, and quality of delivery. More companies are recognizing that, and as a result, focusing more attention on transportation and other logistics functions."

TM

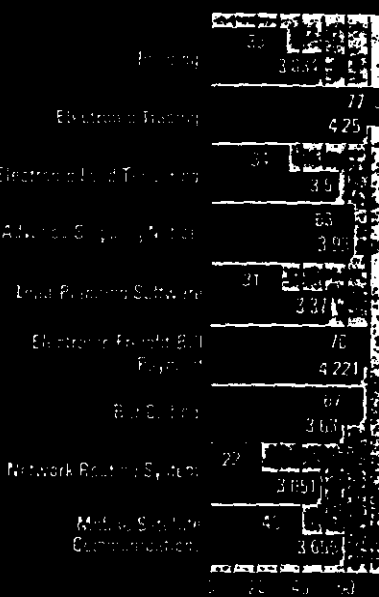
Going High Tech

There's no question that state-of-the-art technology has gained a solid foothold in the logistics industry. The responses to this year's survey indicate that the nation's largest shippers have greeted recent technological advances with enthusiasm.

The results also show that as these shippers move to take further advantage of technology in their operations, they expect their logistics-service providers to match their march down the technological highway step for step. As the accompanying chart shows, the vast majority of the Giants currently use such technology as electronic tracking, advance shipment notice, electronic freight-bill payment, and bar coding in their operations. The chart also makes clear that respondents consider it highly important that their logistics-service providers have capabilities in these and other technological areas so that a direct and efficient systems interface is possible.

Which Technologies Do You Use?

88% Currently Using; 88% Important to Respondents



Respondents were asked to indicate which of the above technologies they currently use, and to rate—on a scale of 1 to 5 (5 = Most Important)—how important it is for a service provider to have these capabilities.

RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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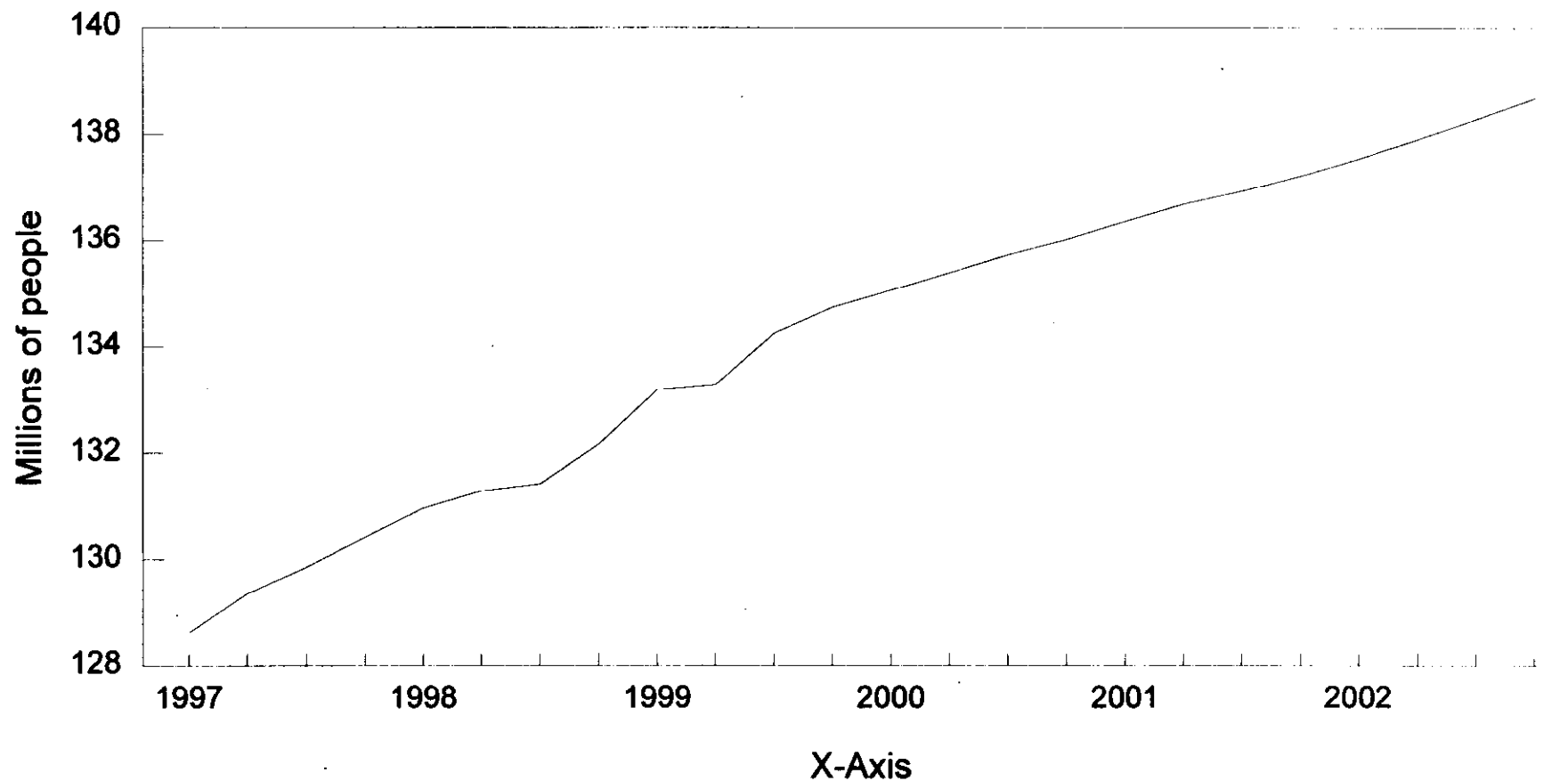
AAP/USPS-T6-8 On page 171 (lines 18-19) of your testimony you state that employment is "predicted to continue to increase in the future." Please identify and provide all documents, studies, reports, data or other evidence that you relied upon to support this statement.

RESPONSE:

The attached figure presents DRI/McGraw-Hill's forecast of total civilian employment through 2002.

Figure accompanying response to AAP/USPS-T6-8

Total civilian employment, 1997 - 2002, as forecasted by DRI/McGraw-Hill



**RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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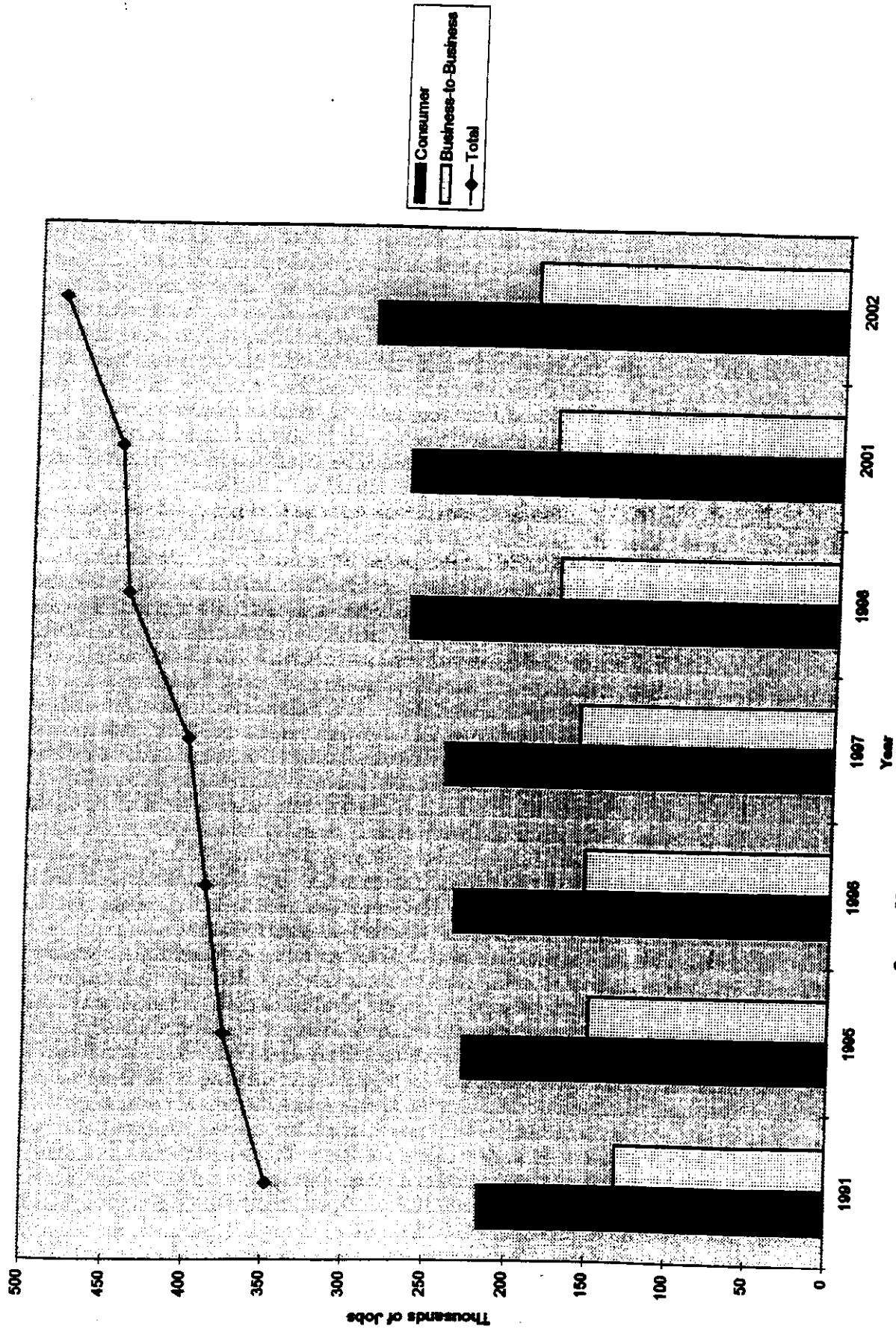
AAP/USPS-T6-9 On page 171 (lines 19-29) of your testimony, you state that "[d]espite the predicted growth in the Internet and other high tech sales media, catalog employment is still expected to increase." Please identify and provide all documents, studies, reports, data or other evidence that you relied upon to support this statement.

RESPONSE:

The accompanying figure shows projections of U.S. catalog employment from the Statistical Fact Book of the Direct Marketing Association.

Figure accompanying response to AAP/USPS-T6-9

U.S. CATALOG EMPLOYMENT BY MARKET



Source: "Statistical Fact Book", Direct Marketing Association

RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAP/USPS-T6-10 On page 3 of your testimony, you present two sets of forecasts of mail volumes, one forecast pertaining to current rates and the other to proposed rates. With respect to both forecasts for BPM:

(a) Please provide the exact value of each forecasted variable that was used in conjunction with the USPS econometric equations to develop the Test Year Before-Rates (TYBR) and Test Year After-Rates (TYAR) forecasts for BPM sponsored by your testimony.

(b) Please provide mathematical examples demonstrating that these values, when used in the BPM econometric equations, result in the TYBR and TYAR volumes predicted by your testimony.

RESPONSE:

(a) These values are provided in workpaper 1 accompanying my testimony.

(b) The forecasting methodology used to forecast bound printed matter is described in the Technical Appendix accompanying my testimony. A numerical example of the forecast for First-Class single-piece letters and presort nonautomated cards is presented in workpaper 2 accompanying my testimony.

The spreadsheets used to forecast bound printed matter are found in Library Reference LR-I-121, files VF_BR (before-rates) and VF_AR (after-rates). Quarterly volume forecasts of bound printed matter are found in these two spreadsheets on sheet Forecast Vols. in column BE. The exact calculations used to generate the bound printed matter forecasts can be found there.

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AAP/USPS-T6-11 Please provide the BPM forecasting equations and BPM
TYBR and TYAR forecasting values recommended by you in R97-1.

RESPONSE:

From R97-1, please see USPS-T-6, pp. 6, 158 - 163, and A-57, as well as
Workpaper 1 accompanying USPS-T-6, and USPS-T-7, pp. 92 - 95, 99, and Workpaper
1 accompanying USPS-T-7. (Note that both my testimony and that of witness Thress
had the same numerical designation in Docket No. R97-1 as they do in this case,
USPS-T-6 and USPS-T-7, respectively.)

**RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAP/USPS-T6-12 Please provide any analyses that compare the BPM forecasting equations and predicted values for the variables in the equations with actual BPM volumes.

RESPONSE:

Please see Appendix Table A-21 on page A-53 of my Technical Appendix, which provides a forecast error analysis for in-sample forecasts of bound printed matter over the past five years.

**RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAP/USPS-T6-13 With respect to the "market penetration Z-variable" for BPM, please state the causal factors which you believe have brought about changes in the value of this variable for the period 1994 through 1999.

RESPONSE:

Growth in mail order sales and shifts from Standard B Special Rate mail may have contributed to changes in the value of the z-variable over this period.

**RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAP/USPS-T6-15 Please state whether and how you gave specific consideration to recent trends in E-commerce in developing the forecasted values used for the individual variables that appear in the econometric model of BPM in order to derive the TYBR and TYAR BPM volumes set forth in your Testimony. Please identify and provide all documents, studies, reports, data or other evidence you relied upon in this regard.

RESPONSE:

I did not develop the forecasted values of the individual variables that appear in the bound printed matter econometric model used in the volume forecast of bound printed matter. These values are projected by DRI, with two exceptions. First, the postage rate that is proposed by the Postal Service. Second, values of the z-variable were extrapolated to future time periods using the econometrically estimated parameters describing the path of the z-variable. As noted in my response to your interrogatory AAP/USPS-T6-13, growth in mail-order sales has apparently contributed to the z-variable and almost surely reflects trends in E-commerce.

RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAP/USPS-T6-16 On page 11 of your testimony you state "[t]he testimony is based on the belief that past behavior of mail volumes provides the most valuable source of information about what is likely to happen in the future, particularly if the reasons for past volume changes can be understood and used as the basis for forecasting." With respect to this statement as it applies to your volume forecasts for BPM, please explain how you determined that the reasons for past volume changes in BPM could now be used as the basis for forecasting future BPM volumes in R2000-1. Provide any statistical tests used or relied upon in making this determination.

RESPONSE:

The econometric demand equation for bound printed matter estimated by Postal Service witness Thress provides an explanation of the past volume behavior of bound printed matter. The t-values for estimated elasticity coefficients of income, price, and the Z-variable are in excess of 2.0 and are thus highly statistically significant. The adjusted r-squared of the equation is 0.97 indicating that the variables included explain 97 percent of the historical variation in bound printed matter volumes.

My discussion of "Factors Affecting Volume" beginning at page 168, line 4, shows how each variable has impacted bound printed matter volume in the recent past. In addition, the Forecast Error Analysis results for bound printed matter, presented in Table A-21 of my Technical Appendix, support the reliability of the estimated demand equation. Taken together, this analysis suggests that the past responses of bound printed matter volume to changes in real postage rates, income, and population, along with the estimated impact of the market penetration Z-variable can be used to reliably predict the future response of the volume of this subclass to changes in these variables.

**RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAP/USPS-T6-17 On page 12 of your testimony you state that developments in electronic communications are "having both negative and positive effects on mail volumes." With respect to this statement:

(a) Please explain whether such developments are having negative, positive or both negative and positive effects on BPM volumes.

(b) Please explain how these developments have been quantified in your equations and forecasts of TYBR and TYAR volumes for BPM.

RESPONSE:

(a) Electronic communication generally refers to E-mail, fax, electronic funds transfers (EFT), and electronic data interchange (EDI). I have not found reason to expect that bound printed matter volume is particularly affected by developments in these areas.

On the other hand, if electronic communication is taken to refer to E-commerce more generally, E-commerce can be expected to have both positive and negative impacts on bound printed matter volume. On the positive side, E-commerce may increase the total volume of mail order sales (of books, for example) leading to increases in bound printed matter. However, as discussed in the section of my testimony on Standard A Regular mail at page 120 to 123, catalog shipments may have been negatively affected by greater use of the Internet and company Web pages as a means for ordering advertising and merchandise.

(b) As stated in my response to (a), the effects of electronic communication and E-commerce have been both positive and negative. The effects of electronic communication and the Internet on bound printed matter are among the influences reflected in the z-variable.

RESPONSE OF POSTAL SERVICE WITNESS TOLLEY TO
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AAP/USPS-T6-18 On page 13 of your testimony, you describe the *Household Diary Study* which give cross-sectional data at a point in time. Please provide complete copies of the three most recent *Household Diary Studies*.

RESPONSE:

The Study for 1998 has been filed as USPS-LR-I-116. The Study for 1996 will be filed as USPS-LR-I-215, and the Study for 1997 will be filed as USPS-LR-I-216.

DECLARATION

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


(Signed)
03-01-00
(Date)

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.

A handwritten signature in black ink, appearing to read "E. P. Koetting", written over a horizontal line.

Eric P. Koetting

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March 3, 2000