DOCKET SECTION

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

RECEIVED
SEP 30 4 49 PM '97
POSTAL RATE COMMISSION
OFFICE OF THE SECRETARY

POSTAL RATE AND FEE CHANGES, 1997	Docket No. R97-1

RESPONSE OF UNITED STATES POSTAL SERVICE
WITNESS BERNSTEIN TO INTERROGATORY OF
ADVO, INC.
(ADVO/USPS-T31—1)

The United States Postal Service hereby provides the response of witness Bernstein to the following interrogatory of Advo, Inc.: ADVO/USPS-T31—1, filed on September 16, 1997.

The 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

Eric P. Koetting

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260-1137
(202) 268-2992; Fax -5402
September 30, 1997

RESPONSE OF POSTAL SERVICE WITNESS BERNSTEIN
TO INTERROGATORIES OF ADVO

ADVO/USPS-31-1. USPS Witness Thress has estimated a cross-volume elasticity of 0.04 for First-Class nonworkshare mail with respect to the Enhanced Carrier Route (ECR) mail.

a. Has this cross-volume elasticity been included into your Ramsey price calculation for ECR mail? If not please explain fully.

b. Please confirm that the positive cross-volume effect estimated by Witness Thress can be considered a negative cross-price effect between these two types of mail (a lower response of First-Class Mail to a higher rate for advertising-related ECR mail). If you cannot confirm, please explain fully.

c. Please confirm that the negative cross-price elasticity of First-Class Mail with respect to ECR mail can be derived through the chain rule of calculus as the positive elasticity of the cross-volume effect multiplied by the negative own-price elasticity with respect to Enhanced Carrier Route mail. If you cannot confirm, please explain fully.

d. Do you agree that incorporating this negative cross-price effect in your analysis lowers the Ramsey price of ECR mail? Please explain.

RESPONSE:

a. Cross-volume effects between the volume of Standard A ECR mail or Standard A Regular mail and the volume of First-Class nonworkshared mail were not included in my Ramsey price calculations. Although the positive cross-volume effect can be mathematically converted into a negative cross-price effect, the cross-volume effect does not conform to the usual features of a cross-price elasticity. Please see the response by witness Thress to NAA/USPS-T6-4 for a discussion of the difference between a cross-volume elasticity and a true cross-price elasticity.

However, in retrospect, it appears that the cross-volume elasticity should have been included in my volume forecasts. Since total Standard A mail under Ramsey rates is greater than total Standard A mail volume under the non-Ramsey rates, inclusion of the cross-volume effect would have caused an increase in First-Class letter volume under Ramsey pricing. This increase in letter volume would have produced additional net revenues, meaning that the Ramsey prices of all mail products could have been reduced somewhat from the levels presented in my testimony. All the same, the effect is not large given the small value of the cross-volume elasticity.

b. Please see the response to NAA/USPS-T6-4.

c. Please see the response to NAA/USPS-T6-4.

d. I can confirm that under Ramsey pricing, a negative cross-price elasticity causes the Ramsey price of a product to be lower. The lower Ramsey price results because price increases produce more leakage when a negative cross-elasticity exists. The rise in price causes a decline in the volume of the product experiencing the own-price increase and also a decline in the volume of the product that has a negative cross-price elasticity.

As I stated in sub-part (a) of this response, I chose not to include the cross-volume effect in my Ramsey price calculations because I do not view it as a cross-price elasticity in the traditional sense. Moreover, even if one were to convert the cross-volume effect to a cross-price elasticity and include it in the Ramsey price calculations, the likely effect on the Ramsey prices would be small owing to the small value of the implied cross-price elasticity.

DECLARATION

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

(Signed)

9/29/97
(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.

Eric P. Koetting

475 L'Enfant Plaza West, S.W.
Washington, D.C. 20260–1137
September 30, 1997