

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

Notice of Price Adjustment
Standard Mail Incentive Pricing Program

Docket No. R2010-3

CHAIRMAN'S INFORMATION REQUEST NO. 2

(Issued March 22, 2010)

To clarify the basis of the Postal Service's estimates underlying its Standard Mail Incentive Program set forth in its Notice of Market Dominant Price Adjustment (Notice), the Postal Service is requested to provide written responses to the following questions. Answers should be provided to individual questions as soon as they are developed, but no later than March 24, 2010.

1. Please refer to files attached to the Response to CHIR No. 1. For each of three scenarios, the file "Summer Sale 2 (using 7.07% loyalty) Links to CHIR1.xlsm" estimates the "Loyalty Growth Mitigated By 2 Check Months" multiplying the "Incremental Volume From SPLY (With Sale)" for "Growing Customers" by two times the "Percentage of total rebate volume mitigated by check month adjustment" ($17.74\% = 2 \times 8.87\%$).
 - a. Please confirm that the 8.87% mitigation factor is the ratio of "Rebate Volume Net of Oct Adjustment" to "Rebate Volume (before Oct Adj)" for all participants in the 2009 Summer Sale. If not confirmed, please explain.
 - b. Please explain why it is appropriate to apply a factor developed from the results of all participants to the smaller group of "Growing Customers." Please also confirm that "Growing Customers" are defined as those participants that are expected to earn discounts.

- c. Please explain why it is appropriate to apply a factor developed from “Rebate Volume” (*i.e.*, volume above a discount threshold) to the total volume of mail above SPLY, which includes mail below the proposed discount thresholds.
 - d. Please explain the basis for the assumption of a linear relationship between the number of months for which an adjustment factor is applied and the percentage of “Rebate Volume” mitigated by the adjustment factors. Please also discuss the magnitude of the effect of alternate assumptions about this relationship on the estimated financial impact of the scenarios presented (*e.g.*, if a factor of 1.5 or 1.0 is used instead of 2).
2. Please refer to files attached to the Response to CHIR No. 1. For each of three scenarios, the file “Summer Sale 2 (using 7.07% loyalty) Links to CHIR1.xlsm” presents estimates of after-rates volume and the volume that is credited to the program (*i.e.*, the response attributable to the discount incentive). The following table reproduces these figures, as well as the before-rates volumes they imply. It also presents the implicit own-price elasticity of the “Growing Customers” calculated two different ways, assuming a linear demand curve and assuming a demand curve with a constant elasticity. In previous discussions of methods of estimating volume responses to discount incentives, the Commission has acknowledged the weaknesses of using subclass average elasticities, but has concluded that they represent a reasonable starting point from which deviations may be appropriately justified and explained.¹ For each scenario, please explain the basis for assuming the implicit own-price elasticity is a more accurate estimate of the actual response of “Growing

¹ See, *e.g.*, Order No. 299, Docket No. R2009-5, Order Approving First-Class Mail Incentive Pricing Program, September 16, 2009, at 15.

Customers” than the average current own-price elasticity (weighted by the product mix of eligible mailers) from the FY 2009 USPS Market Dominant Demand Analysis Materials, filed January 20, 2010.

	Low Growth	Middle Growth	High Growth
Before Rates Volume	3,683,656,058	3,624,592,276	3,565,528,494
Incremental Volume Due to Price Change	311,639,243	703,644,301	1,095,649,358
After Rates Volume	3,995,295,301	4,328,236,576	4,661,177,851
Percent Change in Volume	8.5%	19.4%	30.7%
Implied Linear Own-Price Elasticity	-0.282	-0.647	-1.024
Implied Constant Own-Price Elasticity	-0.228	-0.497	-0.751

	Percent of Eligible Volume	Current Own- Price Elasticity
High Density and Saturation Letters	6.20%	-0.178
High Density and Saturation Flats and Parcels	15.06%	-0.178
Carrier Route	12.07%	-0.178
Standard Regular Letters	57.14%	-0.129
Standard Regular Flats	9.53%	-0.129
Weighted Avg. Current Own-Price Elasticity		-0.145

By the Chairman.

Ruth Y. Goldway