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

NOTICE OF PRICE ADJUSTMENT

Docket No. R2010-3

RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO CHAIRMAN'S INFORMATION REQUEST NO. 2
(March 24, 2010)

Chairman's Information Request (CHIR) No. 2 was issued on March 22, 2010.

The request sought answers no later than March 24, 2010. Attached are the Postal

Service's responses to Questions 1 and 2.

UNITED STATES POSTAL SERVICE

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March 24, 2010

RESPONSE OF THE UNITED STATES POSTAL SERVICE
TO CHAIRMAN'S INFORMATION REQUEST NO. 2

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 x 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).

RESPONSE:

1a)   The 8.87 percent mitigation factor is based upon the most current Summer Sale 2009 rebate data available to the Postal Service at the time the financial analysis was performed. This value represents "all volume exceeding threshold negated by the check month threshold" as a percentage of "all volume exceeding threshold."

Therefore, the calculation only includes participants that grew during the Summer Sale period, not all participants. This number was calculated from the file "(2010-01-13) Rebate round 3 status.xls" (filed with the response to CHIR 1) by dividing the sum of Column I "Rebate Volume Net Oct Adjustment" by Column H "Rebate Volume (before Oct Adj)" and subtracting 1 to arrive at a percentage.

1b)   Per the response to question 1a, this factor is developed from the results of only "growing customers." "Growing Customers" is defined as those customers who exceeded their individual volume threshold during the sale period, prior to any mitigation from the check month.

1c)   The Postal Service believes it is consistent to apply the 8.87 percent metric from Summer Sale 2009 to estimate the mitigated volume shift in Summer Sale 2010 because the basis of analysis for both programs is the volume level that each customer is expected to have mailed in the absence of a sale based on the economic factors present at the time of the sale

1d)   While the relationship between the number of check months and the output of the financial model appears to be a linear one in the model, this is not the actual intent. One could not simply sensitize on the basis of check month equivalents (i.e. substitute various values: 1, 1.5, 2, 2.5…etc) and realize a direct result. It is expected that if the number of check months changed, the underlying growth analysis would change as well. The input of "2" check months is only intended to be demonstrative of the volume

shift expected to be mitigated by check months due to the longer amount of lead time

that customers have to react to the sale as compared to Summer Sale 2009.

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 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

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

RESPONSE:

The Postal Service estimates are based on experience with the 2009 Summer Sale

program, evaluation of historical data, and discussions with customers, all of which

indicate that reliance solely on long-run historical estimates of total market price

elasticity for a program, which includes price changes of this magnitude and short

duration, may not yield a reliable estimate of volume change.