BEFORE THE

POSTAL REGULATORY COMMISSION

SIX-DAY TO FIVE-DAY STREET DELIVERY AND RELATED SERVICE CHANGES, 2010	Docket No. N2010-1

NALC-LR-N2010-1/3:

Michael E. Motley, Associate Director, Government Business Operations Issues, General Government Division, General Accounting Office, Testimony Before the Committee on Post Office and Civil Service, House of Representatives (May 24, 1994)

United States General Accounting Office

GAO

Testimony

Before the Committee on
Post Office and Civil Service
House of Representatives

For Release
on Delivery
Expected at
9:30 a.m. EDT
Tuesday
May 24, 1994

POSTAL SERVICE

Role in a Competitive Communications Environment

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GAO/T-GGD-94-162

060006/151740

THE POSTAL SERVICE'S ROLE IN A COMPETITIVE COMMUNICATIONS ENVIRONMENT

SUMMARY OF THE STATEMENT OF MICHAEL E. MOTLEY, ASSOCIATE DIRECTOR GOVERNMENT BUSINESS OPERATIONS ISSUES

GAO's testimony focuses on the impact of emerging communication technologies on the Postal Service's ability to provide universal mail service at affordable rates. It also addresses the status of the postal automation program and the state of labor relations in the Service.

While the Postal Service expects mail volume to continue to grow for the foreseeable future, the rate of growth appears to be slowing. The majority of First Class Mail, which comprises about half of the Service's volume and revenue, is vulnerable to the fast growing technologies such as fax, electronic mail, and electronic data interchange. The Service believes that because of these technologies, there has been a significant decline in its business-to-business mail. Its share of the correspondence and transactions market is 54 percent this year, down from 77 percent in 1988. Forecasters have predicted that it will decline even further to 35 percent by the year 2000. The Postal Service may ultimately have to reduce its size as the new technologies mature. While this may be some years away, the Service has historically had difficulty in adjusting its workforce to meet volume changes.

To adapt to the changing market the Service reorganized its marketing department to focus more on emerging technologies and is considering and participating in new projects. Related issues that are likely to be brought before Congress include whether the Service should attempt to offer nontraditional services, and whether it has the flexibility needed to respond to changes in the communications marketplace.

For fiscal year 1993, work hours in the Service's functions that are expected to be most affected by automation increased by nearly 5 percent, or about 16,500 positions whereas mail volume grew less than 3 percent. Full implementation of the program, originally scheduled for 1995, has slipped to 1997. It will be difficult to complete the program by then because of complex problems that are yet to be resolved.

Employee commitment is crucial to the Service's success. According to a recent employee survey, employees generally like their work, but most also believe there is an atmosphere of intimidation in the workplace. Most also believe there is a lack of recognition of good performance and that employees are not held accountable when they perform poorly. The National leadership, including postal management and unions, is taking steps to improve communication at the national level. What is needed next is a strategy for improving relations locally, on workroom floors.

Mr. Chairman, Mr. Myers, and Members of the Committee:

We are pleased to be here today to participate in the Committee's oversight hearings on the future role of the U.S. Postal Service. As you requested, our testimony will focus on the impact emerging technologies may have on the Postal Service's ability to provide universal mail service at affordable rates. I will also provide some observations from our recent work on postal automation and labor relations.

The risk to the Postal Service posed by competition and changing technology is very real. The Service has already lost a significant part of its business. We pointed out in a March 1992 report to Congress that parcel post and overnight mail declined substantially because the Postal Service could not compete on price and service[1]. The Service's share of the parcel market declined from about 65 percent in 1971 to 6 percent in 1990. The Service introduced overnight mail service in 1971 but saw its share of that market decline from 100 percent to 12 percent in 1990. Together, these two services now comprise only about 4 percent of postal mail revenue. While growth in letter mail has more than compensated for these losses in the past 20 years, and is substantially protected from competition by law, it is partially vulnerable to alternative forms of delivery and entirely unprotected from diversion to other technologies. Figure 1 shows mail volume since the Postal Service became independent in 1971. It does show a slowdown in growth during the last few years. Rate increases in 1988 and 1991, totaling 38 percent, have made alternatives more attractive and encouraged some postal customers to actively seek other means of communication. Moreover, the widespread publicity and high expectations over the developing electronic information superhighway create the impression that large-scale diversion of the mail is almost certain. More importantly, the Service is likely to lose the more automation-compatible business mail that is the easiest and cheapest to handle and be left with costlier personal correspondence and miscellaneous mail. Should this occur, the tradition of universal mail service at affordable rates will be at risk. The Postal Service would be deprived of much of the revenue needed to maintain its post offices, delivery routes, and transportation network. The likely consequences of this scenario include higher postal rates, reduced service, and/or federal subsidies. The Postal Service expects total mail volume to continue to grow for the foreseeable term, but it is likely to grow at a slower rate than other forms of communication.

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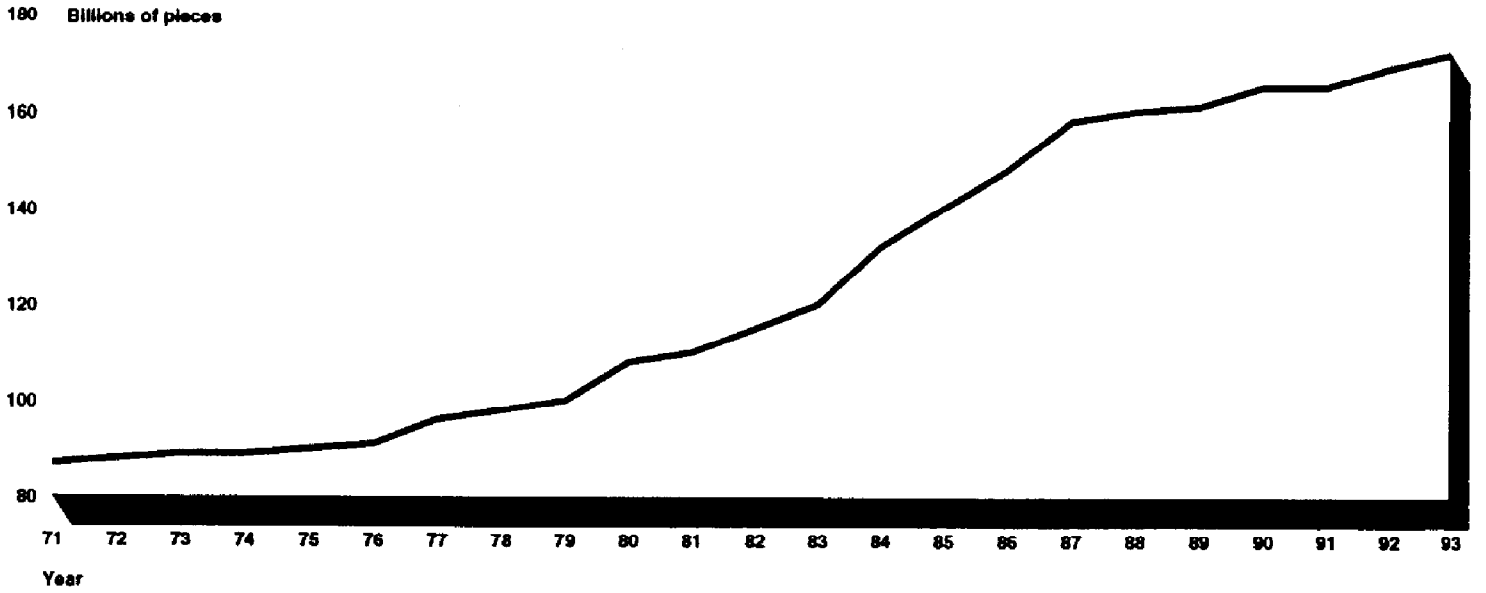
[1]U.S. Postal Service: Pricing Postal Services in a Competitive Environment (GAO/GGD-92-49, Mar. 25, 1992).

Figure 1: Total Mail Volume 1971 - 1973



Source: Postal Service's Pieces and Weights Reports (RPW).

CORRESPONDENCE AND TRANSACTIONS PRODUCT LINE IS VULNERABLE

The correspondence and transactions product line[2] comprises the largest volume and generates the most revenue of any product line. In 1993 it accounted for 49 percent of the total Postal Service mail volume and 53 percent of the total revenue. It is this product line that is most vulnerable to electronic diversion. Over 90 percent of this product line's mail involves businesses.

The correspondence and transactions product line competes with alternatives that are growing rapidly:

-- Electronic mail (e-mail), with both private and public networks, is growing 25 to 30 percent a year.

-- Facsimile (fax) is growing 20 to 30 percent a year.

-- Videotext, provided by remote computing services such as CompuServ and Prodigy, is growing 30 to 40 percent a year.

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[2]This product line consists of First Class Mail (excluding First Class advertising). Other product lines include advertising, expedited delivery, standard packages, international mail, publications, and retail services.

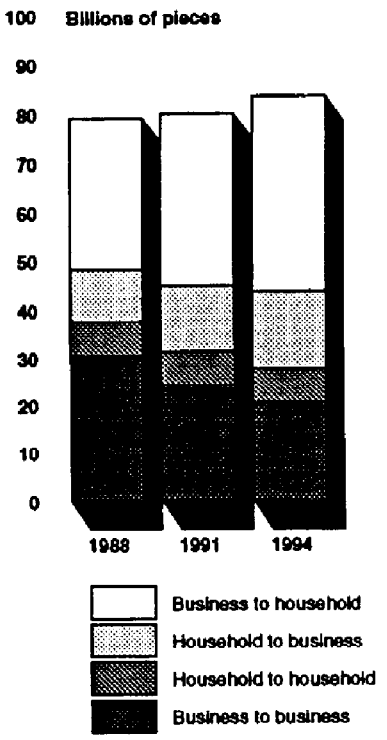
-- Electronic data interchange, the computer-to-computer transfer of data between businesses, is growing 30 to 40 percent a year.

Other alternatives include 800 and 900 telephone lines, now in common use for product ordering and inquiries, and electronic funds transfer, which includes a variety of methods for transferring funds between parties.

The growth in these electronic alternatives is diverting mail from the Postal Service's correspondence and transaction product line. The Service estimates that volume in this product line grew only about 5 percent from 1988 through 1993. As a result, the Postal Service's share of the market decreased from 77 percent in 1988 to an estimated 54 percent this year. The Service believes that the shift to alternative forms of communication amounted to about $1.8 billion in lost revenue from 1988 to 1991. A Postal Service consultant predicted that even though mail volume will increase somewhat, the Service's share of the correspondence and transactions market could decline to 35 percent by the year 2000 as businesses make greater use of alternatives a maturing technology provides them.

It should be noted that despite the decline in mail between businesses, correspondence and transactions mail has still increased. As indicated in figure 2, increases in business mail both to and from households (about 14 billion pieces) more than offset the business-to-business loss. The Service attributes the increase mainly to the increase in the number of households nationwide. While this mail is also vulnerable to diversion to electronic technology, the threat is not as immediate as it is with the business-to-business mail. Businesses are looking for the most cost effective means of handling their correspondence and transactions. They are, therefore, more likely to adopt new electronic communication technologies earlier than households.

Figure 2: Correspondence and Transaction Mail Volume by Household and Business, 1988 to 1994



Source: Postal Service's Marketing and Sales Department.

While the loss of revenue could largely be mitigated by a commensurate reduction in costs, we have reported[3] that the Postal Service has historically had difficulty in adjusting its workforce for improved productivity when volume changes. As I will discuss in a moment, the automation program is not generating the savings anticipated.

How The Postal Service is Responding

Postal officials generally believe that the Service must compete to stay financially viable and find a role for itself, rather than concede its remaining markets. To this end, the Service recently reorganized and strengthened its marketing organization. It hired a vice president for technology and applications with expertise in telecommunications. His responsibilities include determining how the Service can use technology to be more competitive. The new organization includes an advanced

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[3]Financial Performance of the United States Postal Service (GAO/T-GGD-90-16, Feb. 7, 1990)

U.S. Postal Service: Priority Mail at Risk to Competition if Double Postage Rule is Suspended (GAO/GGD-92-68, May 7, 1992).

engineering research office for development of new postal products and services. Advanced engineering research had previously been directed to internal mail processes and systems.

For the long term, Service officials hope to capitalize on the traditional strengths of the organization--its widespread recognition and acceptance among the public, the security of the mail, the Service's political and business neutrality, and its national address coverage. The Service sees a role for itself in the future and has a number of specific projects under early consideration including:

-- entry into the electronic data interchange market, where the Service offers package shippers a preclearance service through Customs and electronic notification of duty amounts,

-- e-mail routing and addressing,

-- interactive information kiosks at post offices for the public to obtain information about federal programs,

-- development of an electronic commerce system for federal agencies,

-- participation in ePost, an electronic/paper delivery system developed by European postal administrations, and

-- involvement in (1) optical scanning of information sent between customers and marketers and (2) improving the efficiency of remittance processing of transactions between customers and financial institutions.

The electronic communications revolution will present new challenges and new opportunities. The Postal Service may see a growing parcel and expedited mail market if, as envisioned, the public shops from home. As you have heard it described by earlier witnesses, the Service will participate in the Time Warner Cable interactive television test project in the Orlando, FL area. Among the services offered to viewers will be next-day delivery by the Postal Service of merchandise ordered over the network.

Effect of Diversion on the Postal Service

Predicting what will happen to mail volume and the Postal Service is an exercise in speculation. Well-reasoned predictions made in the early 1980s were wrong. Electronic mail was by now to have caused a significant decline in mail volume and the size of the Postal Service.

Nevertheless, there is a consensus among those interested in the mail side of the communications market, including postal

officials, that the Postal Service will not continue to grow as fast as it has. Moreover, even with the Service's efforts to develop new services, it will eventually be smaller. Message diversion will occur, and new services are likely to be less labor intensive. Further, we question whether any revenue that might be generated by the new services would replace amounts that can potentially be lost by large-scale mail diversion.

Any significant impact on the size of the Service appears to be several years away. The many electronic technologies and systems that are being considered will be in competition with each other for some time. No one knows which will succeed or fail or how long this weeding-out process will take. The public's acceptance and economic feasibility of the planned new technologies are not known. As I mentioned, the most pressing threat to the Service would appear to be the adverse consequences of the diversion of business mail on costs and revenues. In any case, to its credit, the Service is researching the communication market and assessing the threat to it.

CONGRESSIONAL ACTION MAY BE REQUIRED

The Service appears to be taking these trends seriously. It has not sought action from Congress; however, issues will surface that may require Congress' attention and action as the Postal Service begins to introduce new products and services. These include

-- whether the Service should offer new services or stick to its traditional mission,

-- how the anticipated changes in mail volume and mix will affect the ability of the Service to maintain universal mail service at affordable rates; and

-- whether the Service has the necessary flexibility to make timely adjustments of policies, services, and rates to effectively respond to changes in technology and the marketplace.

Regarding the issue of flexible policies, services, and rates Postmaster General Runyon recently announced plans to begin the process of reclassifying postal services for rate purposes this fall. We believe that rate reform is needed and overdue.

The services for moving merchandise and more urgent correspondence are parcel post, Express Mail, and Priority Mail (heavy First Class Mail). However, as I mentioned at the beginning of my statement, the Service is not competitive in parcels and overnight mail because it has not offered quality service at competitive prices. Private companies, such as United Parcel Service and Federal Express, face fewer constraints than

the Postal Service; fewer constraints enable these private companies to be more aggressive players in the package and overnight market. For example, they are able to offer new services and price them without the constraint of regulation in this market.

The Service is taking steps to improve the quality and type of services offered in the parcel and overnight mail markets. However, even if successful, it will still be at a disadvantage. The Service's inability to offer volume discounts and adjust rates quickly prevents it from competing with the private sector in the profitable business-to-business and business-to-household merchandising market.

Our 1992 report recommended that if Congress wishes the Postal Service to compete effectively in this growing market, it should reexamine provisions of the Postal Reorganization Act dealing with the rate-making process and rate-setting criteria. No action has been taken on our recommendation. As the Postal Service begins its reclassification process, congressional action may be required.

POSTAL AUTOMATION

We have reported in the past that postal automation was not having a significant impact on operating costs, and that it was unclear whether this would change.[4] It is becoming evident that while automation is capable of producing some savings, the amount involved is not consistent from year to year, nor does it compare to the overall growth in Postal Service costs. In 1993 the Service again missed its work hour reduction goals. In the work functions expected to be most affected by automation, work hours increased by nearly 5 percent (equivalent to about 16,500 positions) although mail volume increased by less than 3 percent. The work in these functions cost $816 million more, or 6 percent more than the year before.

Over the last 5 years, not counting wage and salary increases and the cost of the equipment, the Service has on average done a little more with a little less, handling about 1 percent more mail per work hour each year. However, it is difficult to determine the extent that this gain in labor efficiency is due to automation rather than other factors such as mailer presorting.

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[4] Postal Service: Automation Is Restraining but Not Reducing Costs (GAO/GGD-92-58, May 12, 1992).

Postal Service: Restructuring, Automation, and Ratemaking (GAO/T-GGD-93-15, Mar. 25, 1993).

Completion Date Has Slipped

You have heard from earlier witnesses that the original goal to barcode virtually all letter mail by 1995 has now slipped to 1997. Some postal officials have indicated to us that they are not altogether optimistic that it can be done by 1997. We believe that implementation delays have stemmed from the time it took to settle the question of contracting out the remote barcoding jobs and a general deemphasis of automation during the recent postal reorganization. The remote barcoding jobs issue has been largely resolved, and a central office to oversee automation implementation has been reestablished. However, other issues exist that are not likely to be resolved quickly. This includes the difficulty in making route and workforce adjustments to achieve greater efficiency in carrier operations. In addition, the current rate structure favors presorting of mail by customers. While some level of presorting will always be desirable, the automation program, to be fully effective, needs the mail to be barcoded. Finally, the Postal Service does not have an overall plan for completing the program by 1997.

LABOR RELATIONS

A key to the Postal Service being successful in an increasingly competitive environment will be employee commitment. We are near completion of a review of labor-management relations in the Postal Service, which confirmed that employees are generally dissatisfied with their work environment. Service surveys conducted in 1993 and our work showed that, in mail processing plants and post offices, many employees work in an atmosphere of intimidation and tension that is too often characterized by the use of (1) discipline to correct employee problems, (2) grievance processing to obtain relief from disciplinary actions, and (3) arbitration to resolve the ensuing conflict.

The 1993 Service surveys showed that more than two-thirds of all employees enjoyed their work, liked their pay and benefits, and were proud to be a part of the Service. However, most craft employees felt that managers and supervisors did not treat them with respect or dignity. Most believed that the organization is insensitive to individual needs and concerns. Most also believed that performing well just gets you more work and that high levels of performance were not being adequately recognized or rewarded. The negative opinions were more prevalent in mail processing plants than customer service operations and more prevalent in large post offices than small ones.

Under Postmaster General Runyon, some positive steps are being taken at the national level to improve communication. This is where change must start. What is needed next is a strategy for improving relations locally, on workroom floors.

We will be issuing a report soon that will discuss in detail our findings and past and current Service improvement initiatives. We will also make recommendations to the Postal Service, unions, and management associations.

Mr. Chairman, this concludes my prepared statement. I have attached a list of our Postal Service reports issued since the Committee's last oversight hearing in March 1993. I would be pleased to respond to questions.

(240149)

POSTAL RELATED GAO PRODUCTS SINCE 1993
COMMITTEE ON POST OFFICE AND CIVIL SERVICE
OVERSIGHT HEARINGS

Postal Service: Planned Benefits of Iowa Automated Mail Facility Not Realized (GAO/GGD-94-78, Apr. 8, 1994).

Postal Service: Issues Related to Settling a Disputed Contract Award for Air Transportation (GAO/GGD-94-92, Mar. 24, 1994).

U.S. Postal Service: Newly Designed Retail Store Revenues Exceed Operating Costs (GAO/GGD-94-85, Feb. 4, 1994).

Financial Management: Estimate of Interest on Selected Benefits Received by Postal Service Retirees (GAO/AIMD-93-11, July 29, 1993).

Postal Service: 1992 Olympic Sponsorship--Profit or Loss Is Unknown (GAO/GGD-93-89, July 23, 1993).

Priority Mail: Advertised 2-Day Service is Not Guaranteed (GAO/GGD-93-122, July 16, 1993).

Postal Procurement: Information on Bid Protest Activities (GAO/GGD-93-79FS, Apr. 29, 1993).

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