

POSTAL TRENDWATCH

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Postal TrendWatch
Q2, FY08

Q2: USPS Addresses Labor Costs, Service Metrics, Pricing

Executive Summary

Although volume in all categories of mail declined in Q2 of FY 2008 (when compared to Q2 2007), USPS revenues continued to climb. Nonetheless, the agency posted a \$707 million loss in the three months ending March 31. In a noteworthy change from the previous two quarters, over half of Q2's revenue came from First Class Mail.

One consequence of recent quarterly losses has been a renewed effort to cut labor costs. The Postal Service has gradually thinned its workforce, particularly since 2002. This quarter, work-hours fell 2.2 percent, and postal employment dropped 2 percent. USPS now employs fewer workers than at any time since 1987.



Overview

The Postal Service posted yet another net financial loss this quarter. High-level postal officials have attributed this to soaring fuel prices and instability in the housing and credit markets. The increase in revenue in Q2 was attributed to the May 2007 postage price hikes. USPS predicts that volume will likely continue falling for several quarters because of the ailing economy.

Long-term Trends Continue: USPS Revenues Rise while Mail Volume Falls

Total mail volume fell by 1.7 billion pieces -- a 3.3 percent drop when compared with Q2 2007. Total postal revenue, on the other hand, rose by \$584 million, an increase of 3.2 percent from Q2 2007.

This quarter, revenue from First Class Mail accounted for more than half of total postal revenue, reversing a brief trend from the previous two quarters where First Class revenue was slightly less than half of total revenue. First Class Mail has traditionally accounted for more than half of total revenue, and so time will tell if the previous two quarters' revenue figures stand out as historical anomalies.

Postmaster General John Potter blamed the loss on *"weakness in the housing and credit markets, both of which are heavy users of mail."*

In Q2, First Class revenue rose 2.4 percent compared to the same period last year, despite a 3.1 percent drop in volume. Similarly, Priority Mail revenue was up by 8.6 percent, and Standard Mail was up 2 percent. Both categories experienced a drop in volume, by 4.2 percent and 3 percent, respectively.

Periodicals were no different. Volume fell 4.3 percent while revenue rose by 4.7 percent compared to Q2 2007. USPS suspects that falling periodical volume may be linked to the 3.4 percent drop in average weight per periodical that has resulted from the weak advertising market.

The only outlier was Express Mail, which experienced a 3.3 percent drop in revenue as well as a massive 14.3 percent drop in volume.

Even though total revenues increased in the three months ending March 31, USPS suffered a net loss for the second straight quarter. Postmaster General John Potter blamed this on "weakness in the housing and credit markets, both of which are heavy users of mail." Rising fuel prices were also cited as a culprit for this quarter's losses.

Given that mail usage is dependent on the overall state of the U.S. economy, USPS predicts "several more quarters of flat or decreasing volume before a return to sustained growth."

Households Account for Bulk of Mail Delivery

The FY 2007 Household Diary Study was released during Q2. Domestic Mail to and from households formed the bulk of mail volume last fiscal year, accounting for 79 percent of pieces sent or received. Households received more than seven times as much mail as they sent. Total mail sent or received by households was 166.2 billion pieces.

First Class Mail volume consisted largely of transactional mail and advertising. Correspondence accounted for 21 percent of First Class Mail sent or received by households. Correspondence amounted to only 9 percent of the total mail volume sent or received by households.

The chart on the right breaks down the numbers.

USPS Sweetens the Pot on Express and Priority Mail

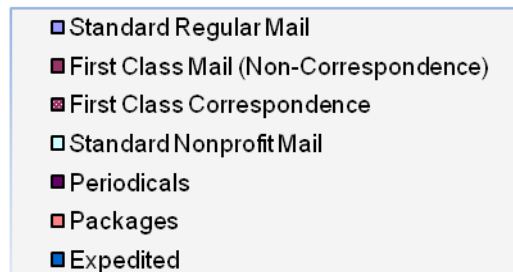
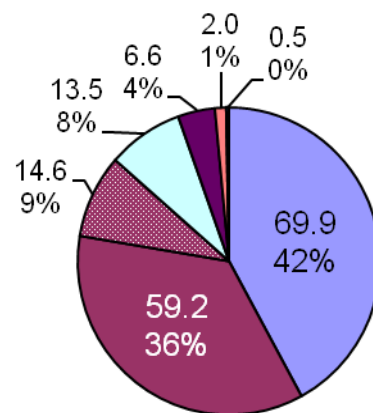
Eager to counteract low Express Mail volume and lagging Priority Mail usage, USPS announced in Q2 that it would offer price discounts to make both categories more attractive to businesses and consumers.

Under the new plan, which took effect in conjunction with the rate increase in Q3 2008 [May 12], customers who purchase Express Mail or Priority Mail shipping services online or through corporate accounts will pay below-retail prices. Express Mail customers can save three percent and Priority Mail customers an average of 3.5 percent.

Quarterly rebates will also be distributed to customers who meet a minimum mail-volume requirement.

The challenge for USPS will be to ensure that these discounts on competitive products result in higher volume without sacrificing revenues. This plan represents one of the Service's first attempts to exercise the pricing flexibility it was granted in the Postal Accountability and Enhancement Act.

Mail Sent or Received by Households (Billions of Pieces)



Faced with a Financial Slowdown, USPS Cuts Labor Costs

In light of recent monetary losses, the Postal Service made a concerted effort to cut labor costs in the three months ending March 31. The result was a reduction in work hours by 2.2 percent (eight million hours) compared with the same period in 2007.

This included four-million-hour reductions in mail processing work, customer service, and retail work. City delivery hours were cut by one million and rural delivery hours by 1.5 million.

Work hours were not the only target of cost-cutting. Postmaster General John Potter has made trimming the size of the labor force a hallmark of his tenure, and this quarter was no exception.

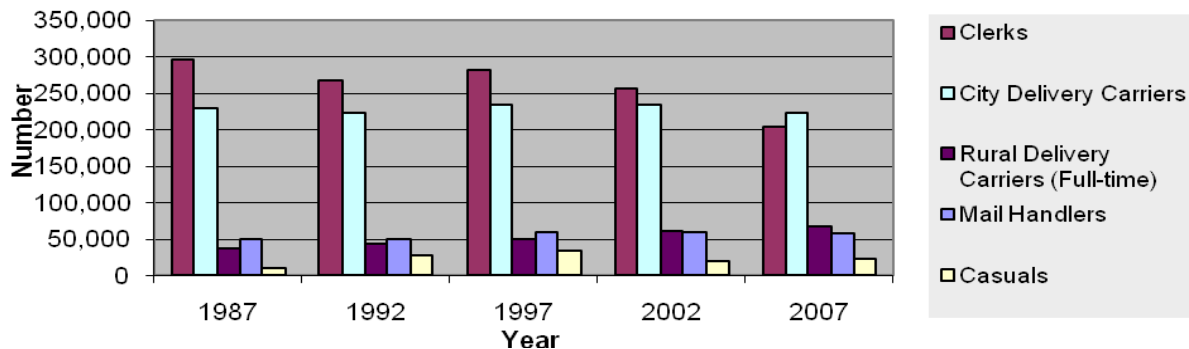
There are now 674,912 career employees -- 13,628 fewer (2 percent) than the total at the end of Q2 FY 2007.

Good News on Service Metrics

The Postal Service reported some good news for consumers in Q2 by achieving new second-quarter records for on-time delivery of First Class Mail. First Class Mail with a next-day delivery commitment held at 96 percent for the fourth consecutive quarter. First Class with a two-day commitment rose to a new high of 94 percent, and mail with a three-day commitment increased four points to a 92 percent success rate.

Postmaster General John Potter revealed that service in the notoriously inefficient Chicago district has also

Number of USPS Employees in Key Categories



In the last decade, the size of the postal workforce has declined to its approximate size in 1987. The number of career employees has declined 8.8 percent in that time. During the same period, the ranks of non-career employees have more than doubled. The number of clerks has declined by 31.1 percent since 1987, accounting for the bulk of the decline. On the other hand, the number of rural carriers has jumped nearly 85 percent, and the number of mail handlers has increased 18.4 percent.

In this quarter, the workforce was reduced by 6,171.

improved in the last year. Overnight First Class Mail delivery is up five points to 95 percent, and two-day mail has reached the national average of 94 percent -- an improvement of 13 points. Three-day mail soared 21 points higher, to 90 percent.