

**Supplemental Comments of
RR Donnelley**

Submitted to

**The President's Commission
on the
United States Postal Service**

**Concerning
Protecting the Health and Viability of
The United States Postal Service
into the 21st Century**

Wednesday, February 12, 2003

At the request of Dennis Shea, Executive Director of the President's Commission on the United States Postal Service, we respectfully submit this supplemental document which details our analysis of the savings potential available to the United States Postal Service through employing standardized productivity programs, consolidating the existing distribution network and strategically outsourcing upstream processing capabilities to the private sector through extended worksharing programs.

According to the USPS' 2001 Costs and Revenues Analysis, attributable upstream costs in FY 2001 exceeded \$23.7 billion – nearly 35% of the Postal Service's total cost for FY 2001, and 52% of total attributable cost.

These costs reflect the operating expenses for mail processing, supervision and overhead functional areas in the postal stream – the Bulk Mail Centers, the Processing and Distribution Centers, Sectional Center Facilities and the transportation between them and to the Destination Delivery Units.

The breakdown of expense is as follows*:

<u>Cost Category</u>	<u>Expense</u>
Processing	\$12.1B
Transportation	\$ 4.7B
<u>Overhead & depreciation</u>	<u>\$ 6.9B</u>
Total	\$23.7B

*NOTE: for detailed analysis, see attachment "Presidential_Commission_Data.xls"

These are the expenses associated with approximately 500 upstream processing facilities. These are also the facilities and expenses focused on by the USPS' Network Integration and Alignment Project (NIA), which targets \$20 billion of processing costs and \$5.5 billion of transportation costs for reduction.

Worksharing has ramped up over the years to a current estimated annual savings/cost avoidance by the USPS of \$17 billion. At the same time, postal volumes have now leveled off, and flats automation has been introduced. This confluence of factors offers a significant new opportunity to reduce costs through additional worksharing offered in conjunction with the consolidation of facilities and network realignment.

Benefits would be achieved in a number of ways: First, productivity and performance across these facilities varies widely. There are several approaches to improve productivity:

1. Standardize processing procedures (i.e. Best Practices)
2. Use process improvement tools and measurements such as Process Variability Reduction and Six Sigma methodologies to increase productivity of all facilities, with special emphasis on "below average" facilities. These tools can also be used to improve safety performance and service quality.

Within R.R. Donnelley, these techniques have yielded productivity improvements of up to 35% on our binding lines, which produce and process magazines and catalogs (flats).

Dramatically improving operating results will increase the USPS' ability to reduce the number of processing facilities it uses for upstream processing.

By optimizing processing and ground transportation, a significant number of facilities can be consolidated within the network while maintaining service standards. This process allows for facility overhead to be reduced in addition to the processing cost reductions achieved.

Recently within R.R. Donnelley, we have had to undertake a consolidation of our own to reduce our cost structure in the face of industry overcapacity and price degradation. While remaining capacity neutral, we have been able to take out 10% of our structural cost. As part of our ongoing business operations, structural costs are reviewed regularly. Since the USPS has not widely applied such practices, this leads us to conclude that an even greater reduction of structural cost should be expected. A redesign of the BMC network, to get to the minimum few, would be a good place to start, since the BMC network costs approximately \$8 billion per year to operate.

Turning to transportation, there will be countervailing activities. First, reducing facilities can yield better truckload factors because of less origin-destination pairs. However, mileage per trip may actually increase. The Postal Service can better utilize transportation equipment by monitoring and measuring equipment load factors between facilities, and better utilizing information technology and a private electronic transportation exchange to reduce its overall cost of ground transportation. Additionally, at origin BMC facilities, the Postal Service in some cases still uses postal equipment to provide pick up service from the mailer for delivery to the BMC. Stopping this practice will provide immediate savings.

The mailing industry would benefit from having fewer facilities to ship to, which will improve route density, but will also likely create increased linehaul distances. This dynamic should make existing drop ship discounts to Sectional Center Facilities more attractive with the result being increased worksharing that drives volume deeper into the system.

Additionally, the USPS should better match their pricing with their operational strategies. In a revenue neutral manner, the USPS could further incent drop shipping by passing along 100% of the cost savings derived. With transportation cost rising, a larger differential from the BMC to the SCF and to the DDU would push more mail downstream. In addition, other classes of mail could be incented with worksharing discounts. Business mail within first class mail could follow the same success model that has been applied to Standard letters, and Standard packages could be incented with the same success model implemented for Parcel Select a few years ago. Magazines, if given the same handling and entry parameters as standard mail catalogs, would see increased drop shipping as well.

When combined, the impacts of productivity, consolidation and extended worksharing can reduce the current attributable costs in upstream processing by 25% or in excess of \$6 billion. In private industry, savings of this magnitude would trigger additional reductions in corporate overhead.

There is a paradigm shift that the USPS, the mailing industry, Congress and labor must accept regarding the USPS network. That is, the postal system should not be a fixed or static network, but a dynamic and flexible one that adjusts to meet changing needs resulting from population shifts, mail volume and mix changes, and technological advancements, to name a few variables. It must not take a Presidential Commission, or act of Congress, to realign and optimize the upstream processing network. This must be done routinely in the normal course of business.