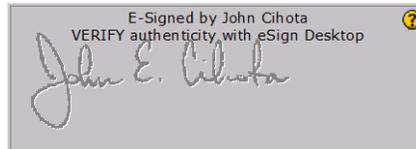




September 23, 2019

MEMORANDUM FOR: SHARON D. OWENS
ACTING VICE PRESIDENT, SALES



FROM: John E. Cihota
Deputy Assistant Inspector General
for Finance and Pricing

SUBJECT: Management Alert – Issues Identified in the Outbound
International Mail Market (Report Number CP-MT-19-001)

This management alert presents Issues Identified in the Outbound International Mail Market (Project Number 19BG003CP001). These issues came to our attention during our ongoing audit of Costing Best Practices (Project Number 19BG003CP000). The objective of this management alert was to provide U.S. Postal Service officials immediate notification of the issues identified during our ongoing audit. The issue requires immediate attention and remediation.

We appreciate the cooperation and courtesies provided by your staff. If you have questions or need additional information, please contact Sherry Fullwood, Director, Cost and Pricing, or me at 703-248-2100.

Attachment

cc: Postmaster General
Corporate Audit Response Management

Introduction

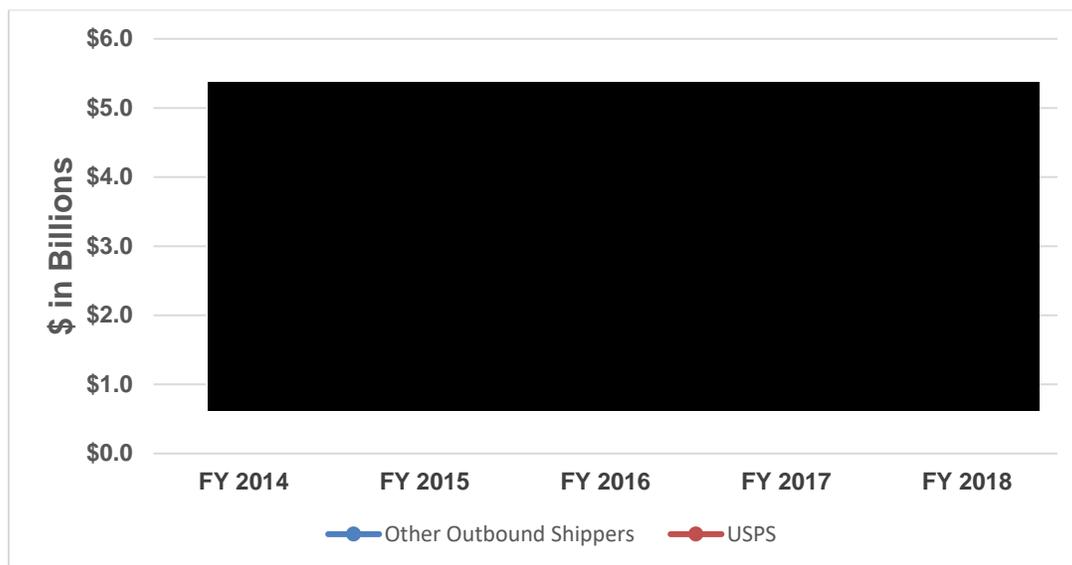
The purpose of this management alert is to highlight [REDACTED] of U.S. Postal Service outbound international mail volume and revenue (Project Number 19BG003CP001). We identified these trends during our Costing Best Practices audit (Project Number 19BG003CP000). While conducting extensive financial analysis of competitive product cost and pricing data, we reviewed processes and methodologies impacting international competitive product costs and prices from fiscal year (FY) 2014 through FY 2018.

Our analysis identified a [REDACTED] in competitive product outbound international mail volume and revenue over the last five years, while industry international volume and revenue has grown during the same time period. Specifically, the Postal Service experienced a [REDACTED] in competitive product outbound international mail volume from FY 2014 through FY 2018. This volume loss has resulted in a [REDACTED] percent revenue loss, reducing competitive product outbound international mail revenue from [REDACTED]. We identified several factors that are contributing to this [REDACTED] in volume and revenue loss. Although the Postal Service may not have control over certain contributing factors, it is imperative the Postal Service take action to develop mitigating strategies to [REDACTED]
[REDACTED]

Outbound International Mail Trends

In FY 2014, the Postal Service [REDACTED] in competitive product outbound international mail volume. Over the last five years (FY 2014 through FY 2018), this mail volume and revenue has [REDACTED] even though this market has experienced growth. For example, some others that ship outbound internationally have experienced revenue growth between [REDACTED] percent and [REDACTED] percent during this time. However, the Postal Service has experienced a [REDACTED] percent [REDACTED] in competitive product outbound international mail revenue over the same time period (see [Figure 1](#)). Specifically, the competitive product outbound international mail revenue [REDACTED]
[REDACTED].

Figure 1. Outbound International Mail Revenue for Selected Shippers (in Billions)



Source: Industry and contractor data from annual reports; Postal Service *Revenue, Pieces, and Weight (RPW)* reports from FY 2013 to FY 2018;¹ and Decision Analysis Partners proprietary data.

There are four major outbound international mail classes for the Postal Service, and three of them are competitive products: Outbound Priority Mail International, Outbound International Expedited Services, and Other Outbound International Mail. Between FYs 2014 and 2018, mail volume for the three competitive outbound international mail classes [REDACTED]:

- Outbound Priority Mail International² — [REDACTED]
- Outbound International Expedited Services³ — [REDACTED]
- Other Outbound International Mail⁴ — [REDACTED]

For FYs 2017 and 2018, we found the three competitive product mail classes [REDACTED] by about [REDACTED]. We estimate that over the next three years (FY 2019 through FY 2021), the Postal Service’s volume for the same classes [REDACTED] of international

¹ The RPW reports come from the Origin Destination Information System - RPW system, which is a probability sampling system used to assist in estimating Postal Service revenue, volume flow, and weight. The Postal Service uses this information to develop rates, prepare the budget, conduct management studies, and support management decisions concerning mail flow and service performance in transportation and operations.

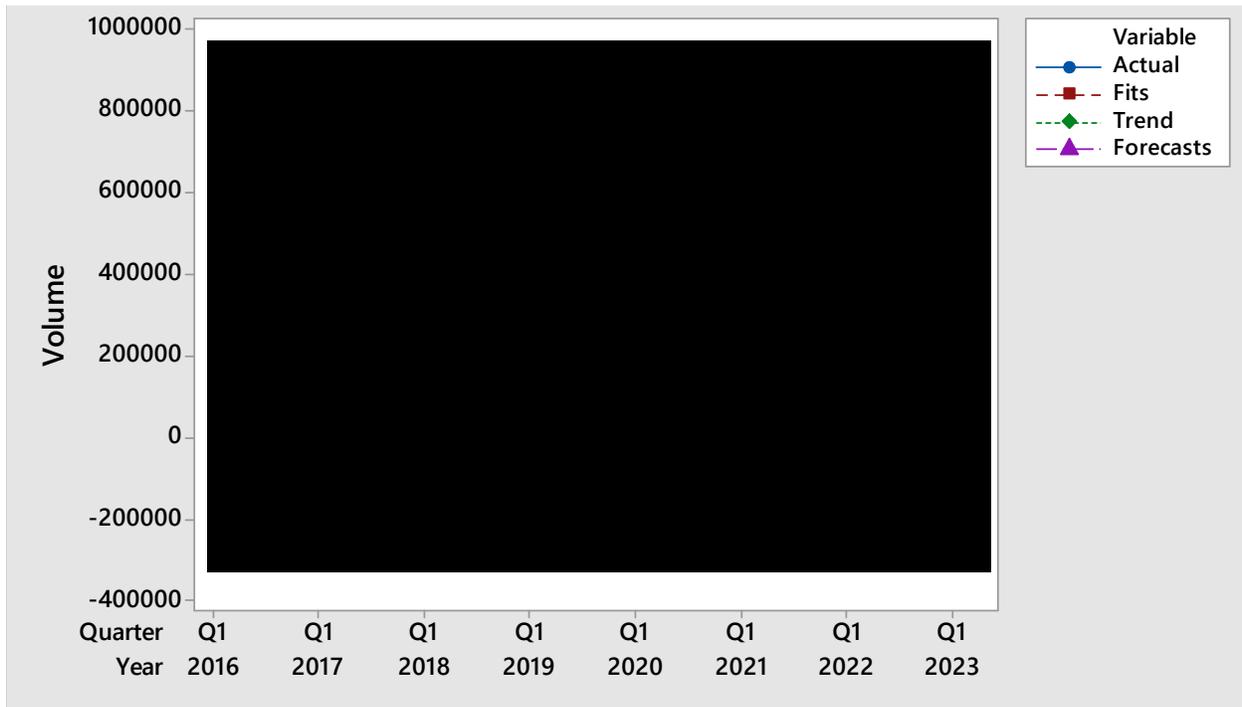
² Outbound Priority Mail International may be mailed as Priority Mail International Flat Rate Envelopes, Priority Mail International Flat Rate Boxes, or Priority Mail International Parcels.

³ Outbound International Expedited Services (Global Express Guaranteed and Priority Mail Express International) provide expedited service to designated outbound international destinations.

⁴ Other Outbound International Mail include products such as First-Class Package International Service, International Priority Airmail, International Surface Airlift, and International Direct Sacks-M Bags.

[REDACTED] We recognize that the uncertainty of the U.S. participation in the Universal Postal Union (UPU)⁶ as of October 1, 2019, [REDACTED]

Figure 2. Outbound International Mail – Expedited Services⁷



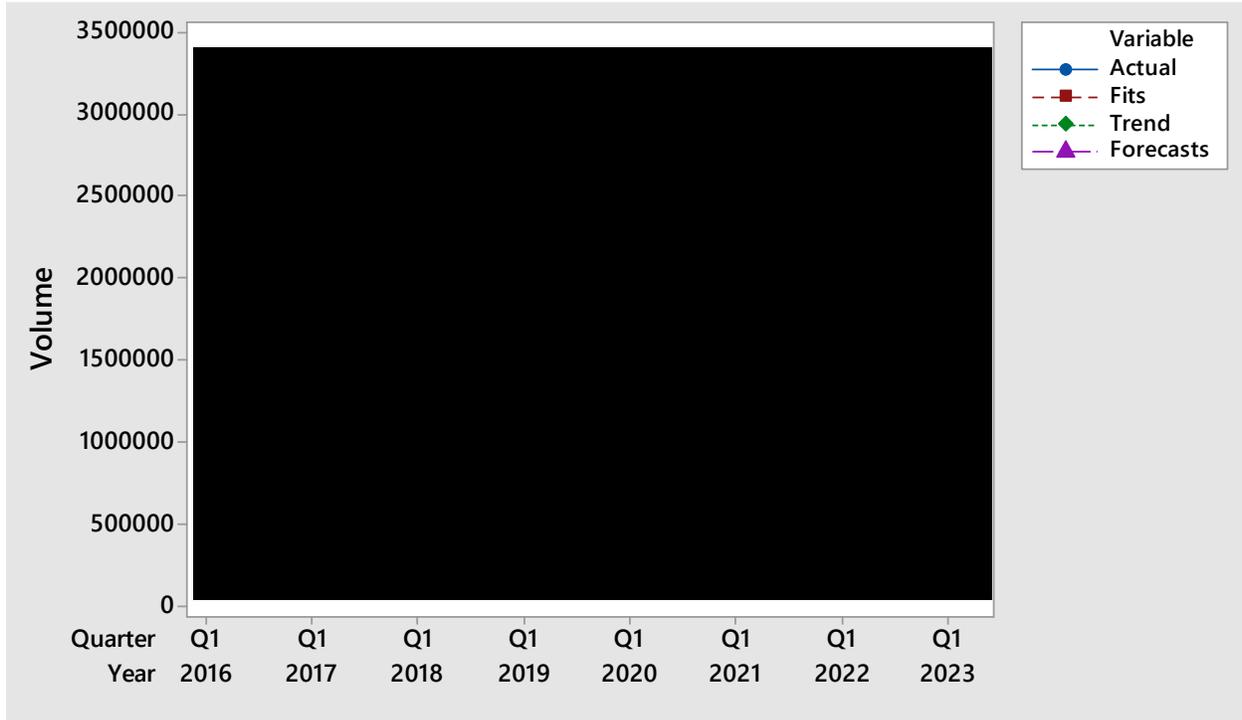
Source: U.S. Postal Service Office of Inspector General (OIG) analysis using RPW reports (FY 2016 – FY 2019, Quarter (Q)1-Q3).

⁵ We conducted a time-series analysis to project possible future competitive product outbound international mail volume and revenue [REDACTED]

⁶ The primary forum of cooperation between postal sector players. It sets the rules for international mail exchanges and makes recommendations to stimulate growth in mail, parcel, and financial services volumes, and improve quality of service for customers.

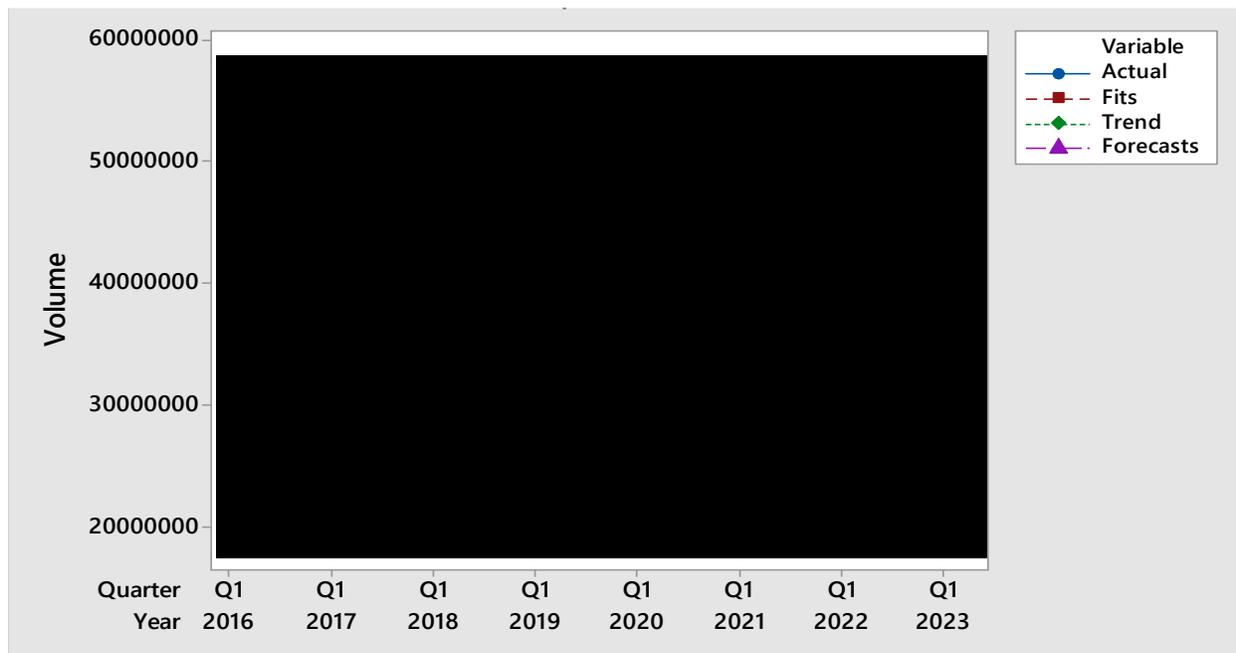
⁷ Fits (or Fitted Trend) describes how the variable measured changes over time. The fitted trend equation is an algebraic representation of the trend line.

Figure 3. Outbound International Mail – Priority Mail



Source: OIG analysis using RPW reports (FY 2016 – FY 2019, Q1-Q3).

Figure 4. Other Outbound International Mail

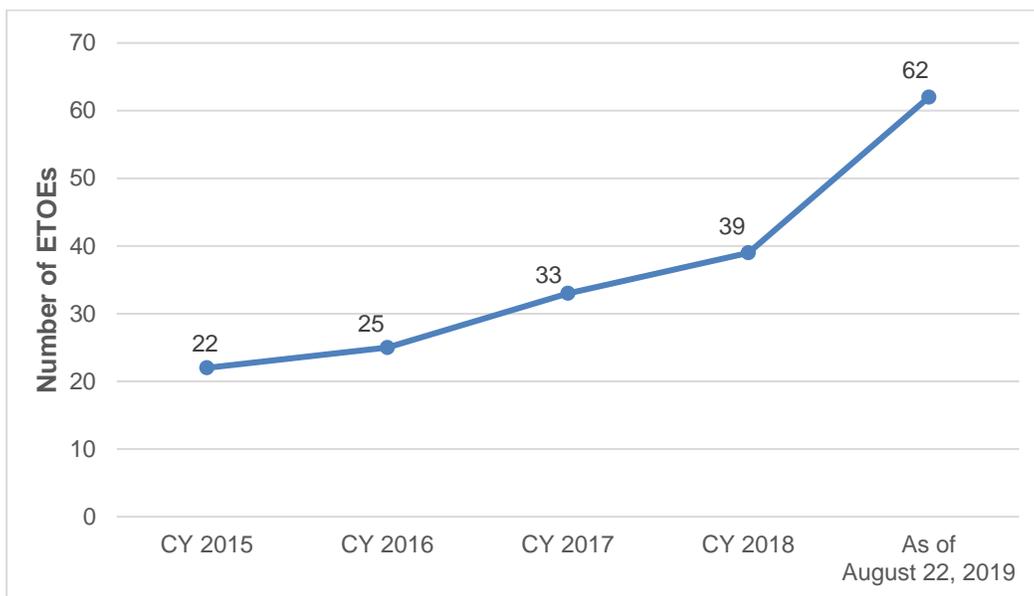


Source: OIG analysis using RPW reports (FY 2016 – FY 2019, Q1-Q3).



- Extraterritorial Offices of Exchange (ETOE): The Postal Service faces increasing outbound international mail competition from foreign posts with operations in the U.S. In 1986, the Postal Service suspended laws that restricted processing and delivery of outbound international letters by organizations other than the Postal Service. This change was intended to foster competition in the international mailing and shipping industry and ultimately created an opportunity for ETOEs to operate in the U.S. ETOEs perform a wide range of postal functions that can vary by country but generally includes consolidating, documenting, and transporting outbound international mail for their host country. From calendar year (CY) 2015 to August 22, 2019, the number of ETOEs in the U.S. has increased from 22 to 62 offices, as shown in [Figure 5](#). The Postal Service has been facing competition from ETOEs and other providers within the U.S. This competition could grow significantly depending on changes in the international mail market regarding U.S. participation in the UPU (discussed later).

Figure 5. Extraterritorial Offices of Exchanges Trend⁸



Source: Postal Service International Postal Affairs.

- **Postal Service Consolidators:** The Postal Service may be losing outbound international mail volume to third-party consolidators. The Postal Services enters into agreements with third-party consolidators to ship mail internationally in a workshare-type environment. Consolidators may be ETOEs, third-party logistics, or wholesale companies. Some outbound international mailers use Postal Service consolidators to ship their merchandise overseas. These consolidators are Postal Service partners and sell Postal Service commercial outbound mail products to end users. This allows mailers and shippers to take advantage of worksharing; however, some consolidators also offer products or services of Postal Service competitors. Customers choose their products based on price and the services provided, and
- **Strength of the U.S. Dollar:** When the U.S. dollar (USD) is strong, the USD is relatively more valuable compared to foreign currencies. As a result, overseas ecommerce customers may not want to purchase goods that are relatively more expensive. This can reduce the demand for Postal Service products exiting the U.S., thus reducing the Postal Service’s volume and revenue. A strong USD may not have the same impact on global logistics providers if the provider is able to move goods around the world or source from countries that have lower currency values to reduce the impact of the exchange rates.
- **Withdrawal from the UPU:** The potential U.S. withdrawal from the UPU is likely causing uncertainty in the Postal Service’s participation in the international postal

⁸ Postal Service officials stated that the steep increase in CY 2019 could have been influenced by some countries anticipating the potential U.S. departure from the UPU.

marketplace. The UPU develops and maintains international postal regulations and standards to facilitate the exchange of postal-related information, including that of the Postal Service. As the U.S. moves closer to either exiting the UPU or renegotiating the terms of its participation to move towards self-declared rates, some mailers may be moving their mailing business from the Postal Service to other logistics operators to ensure any disruptions are minimized. These uncertainties are relatively recent (began in FY 2019) but may cause additional reductions in volume and revenue moving forward.

- Global Delivery Network: Other commercial providers that ship outbound mail internationally have developed a global network that allows them to ensure certain service performance. The Postal Service is reliant on foreign posts to delivery outbound Postal Service international products in the destination country. Outbound Postal Service products [REDACTED] the destination country's postal operator and system. If [REDACTED] the Postal Service's outbound products suffer. For example, customers have indicated they would like more destination countries added to the Outbound Commercial ePacket product offering, but the Postal Service will not add a country until it can [REDACTED] at [REDACTED] percent.

[REDACTED]

During our audit, we identified other factors that may contribute to the [REDACTED] identified. For example, unlike others in this market, the law generally requires the Postal Service to use U.S. flag carriers where available to transport international mail, which may not offer the lowest rates in the marketplace. Additionally, it does not use foreign-based postal facilities to leverage international mail delivery. Foreign posts with offices of exchange in the U.S. produce cost savings by occasionally redesigning their network to reduce international mail transport, delivery costs, and consolidate their mail volumes. Several foreign posts and key service providers have offices in New York, San Francisco, Los Angeles, Chicago, and Miami. This strategic placement [REDACTED]

[REDACTED]

Figure 6. Foreign Post Facilities in the U.S.



Source: OIG analysis.

Although the law does not permit the Postal Service to establish operations in foreign countries, other than diplomatic outposts or military installations, it does grant the Postal Service the authority to enter into contracts, including commercial contracts related to international postal services. During this audit, management stated [REDACTED]

Digital technologies have created a borderless, worldwide marketplace for even the smallest businesses. Global ecommerce – using the Internet to buy and sell goods and services on an international scale – is rapidly booming, as is the need for transporting those products from seller to buyer. An previous OIG report⁹ stated that global ecommerce topped \$1.3 trillion in 2014 – exceeding 2013 levels by 24 percent – and was expected to grow another 20 percent in 2015. This growth had a profound effect on small and medium-sized enterprises (SME), as it allowed them to participate in and help drive international trade in ways similar to their larger counterparts. The report further stated that SMEs are gaining unprecedented access to international customers, helping the nation’s economy in the process. The Postal Service, however,

[REDACTED]

[REDACTED]

Recommendation #1: We recommend the **Acting Vice President, Sales**, develop a plan to increase outbound international sales and strengthen competitiveness in the outbound international mail market.

Management’s Comments

Management agreed with the findings and recommendation to develop a plan to increase outbound international sales and strengthen competitiveness in the outbound international mail market but disagreed with the monetary impact. Management stated they will provide a copy of a written plan once they know more about product offerings, pricing, and geographic coverage. The target implementation date for the plan is July 31, 2020. Regarding the monetary impact, management stated that given the

[REDACTED]

See [Appendix A](#) for management’s comments in their entirety.

Evaluation of Management’s Comments

The OIG considers management’s comments responsive to the recommendation and corrective actions should resolve the issues identified in the report. Regarding the monetary impact, the OIG recognizes there is uncertainty in the future international mail market, however, we based monetary impact projections on historical data and trends to

⁹ *Small Business Exports* (Report Number [MS-WP-15-002](#), dated August 26, 2015).

demonstrate the possible amount the Postal Service could [REDACTED]. The OIG used a Mini Tab Statistical Software to develop a “time series analysis,” which is the study of observations recorded at regular intervals over time. This type of analysis reveals patterns in historical data that can be reliably extrapolated into future forecasts or projections. The OIG believes the projections reasonably demonstrate potential future revenue the Postal Service could achieve.

The recommendation requires OIG concurrence before closure. The OIG requests written confirmation when corrective action is completed. The recommendation should not be closed in the Postal Service’s follow-up tracking system until the OIG provides written confirmation that the recommendation can be closed.

Appendix A. Management's Comments

SHARON OWENS
VICE PRESIDENT, SALES



September 17, 2019

LAZERICK C. POLAND
DIRECTOR, AUDIT OPERATIONS

SUBJECT: Issues Identified in the Outbound International Mail Market
(Report Number CP-MT-19-DRAFT)

Management agrees with the findings indicating a volume [REDACTED] but disagrees with the monetary references. [REDACTED]

[REDACTED] we do not agree a time [REDACTED]. The changes in products, pricing and geographical coverages are not known at this time but will [REDACTED] within the outbound market. Once we are able to identify these market influencers better data will be available for analysis.

Recommendation:

We recommend the Acting Vice President, Sales, develop a plan to increase outbound international sales and strengthen competitiveness in the outbound international mail market.

Management Response/Action Plan:

Agree - [REDACTED]

[REDACTED] We will provide a copy of the written plan once we know more, relative to product offerings, pricing and geographic coverage.

Responsible Official:

Director, International Sales

Target Implementation Date:

July 2020


Sharon Owens

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