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# Postal privatization and the transformation of the global logistics industry



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## RÉSUMÉ

La tendance mondiale à la privatisation et à la déréglementation des services postaux nationaux a connu une croissance rapide au cours des dernières années. Le processus de privatisation en matière de collecte et de tri du Service postal des États-Unis, le plus important au monde, présente un cas des plus intéressants. Cet article examine comment les intérêts des entreprises et les stratégies d'affaires influencent ce processus. Les changements dans le secteur postal américain se produisent dans le contexte de ceux qui sur la scène mondiale s'appliquent au secteur de la logistique. En dépit des nombreuses législations en matière de réforme des services postaux, les stratégies d'affaires à l'origine des partenariats public-privé n'ont donné lieu qu'à une seule forme de privatisation des services postaux – celle qui a reçu l'aval des entreprises privées – une privatisation qui restreint la concurrence.

Mots clés : stratégies d'entreprise, changement institutionnel, restructuration du secteur public, services postaux.

## ABSTRACT

The global trend to privatize and deregulate national postal services has grown rapidly in the past several years. The process of privatization of the US Postal Service (USPS) presents an interesting case in which the world's largest national post has privatized significant portions of its collection and sortation network. This paper examines the influence of corporate interests and business strategies on the privatization process of the US postal sector. These changes are taking place in the context of transformative changes in the global logistics industry. Despite years of failed postal reform legislation, business strategies creating public-private partnerships have driven a unique form of postal privatization – one preferred by private businesses – privatization that constrains competition.

Keywords: business strategies, institutional change, public sector restructuring, postal services.

## RESUMEN

La tendencia mundial a la privatización y a la desregulación de los servicios postales nacionales ha experimentado un crecimiento rápido en el curso de los últimos años. Un caso interesante es el proceso de privatización de una parte significativa de la recolección y la clasificación del servicio postal federal estadounidense, uno de los más voluminosos del mundo. En este artículo se examina la manera en que los intereses de las empresas y las estrategias de negocios influyen en dicho proceso. Esos cambios en el sector postal se producen en el contexto mayor de los cambios que afectan a toda la industria logística. A pesar de los sucesivos fracasos de la legislación en materia de reforma de los servicios postales, las estrategias de negocios que han originado asociaciones entre lo público y lo privado han conducido a una forma única de privatización postal: la privatización que recibe el aval de la empresa privadas y que limita la competencia.

Palabras claves: estrategia de empresa, cambio institucional, reestructuración del sector público, servicio postal.

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The popular image of postal letter carriers braving sleet and rain to deliver the nation's mail has long represented government-operated postal services. The United States Postal Service (USPS) network reaches into every small town and urban neighbourhood across the country. Six days a week, every household and business in the US interacts with this government delivered service. Indeed, national postal services have been the symbol of universal government service and a measure of advanced economic development (Baxter, 1994; Batstone *et al*, 1984). This ubiquitous public good has historically connected individuals and communities through a universal public communications network at an accessible, uniform rate.

The delivery of these public services is changing substantially however, as the postal network in the US and the global mailing industry in general, are undergoing profound transformations. A few national posts have moved towards private ownership including Germany and the Netherlands.

In Japan, the debate over postal privatization forced the government to collapse in 2005 (Onishi, 2005). The subsequent Japanese government immediately established plans to privatize the world's second largest postal service beginning in 2007 (Putzger, 2006). Other countries, such as Sweden and New Zealand have fully deregulated the postal sector (Campbell, 2002). The European Union member states officially began postal deregulation in 1997 with plans to reach a liberalized internal market by 2009 (Campbell *et al*, 2005). Although only a handful of national posts have privatized to date, the phenomenon of postal de-regulation, liberalization, and corporatization is nearly universal (Campbell, 2002). While these trends have generated a great deal of debate over the implications of privatization and liberalization on the provision of universal postal service (Crew and Kleindorfer, 2000), there has been less attention given to the consequences that privatization strategies have on the structure of the mailing industry. Furthermore, the

changes sweeping public postal authorities are part of a broader transformation of the global logistics services industry driven, in part, by firm competitive strategies.

This paper examines the dynamic changes taking place in the global logistics industry in general and the US mailing industry in particular. The central aim of this paper is to show how the business strategies of global logistics corporations and other private firms are driving the changes taking place in the postal services industry. Private firms are not simply reacting and adapting to global economic changes, rather management strategies such as acquisitions and political lobbying have actively restructured the industry. The impacts of these business strategies are especially evident in the privatization process of the USPS. The nature, extent, and process of privatization of the USPS present an interesting case of postal privatization. Unlike other models of postal network privatization, such as in Germany where the former national post has emerged as a publicly-traded powerhouse in the global logistics industry, the US case illustrates the influence and importance of private sector corporations and their preference for a model of privatization that controls, rather than promotes, competition.

The restructuring process of the global logistics industry includes the consolidation, integration, privatization, and de-unionization of transportation networks. A handful of large, global firms such as United Parcel Service (UPS), Federal Express (FedEx), DHL, and TNT have captured a significant share of the global market through acquisition strategies. Traditional transportation segments, such as air cargo and package delivery, have become blurred as these global giants seek greater market power and efficiency through the integration of these distinct transportation networks. New technologies have also blurred industry boundaries as major printers such as RR Donnelley and Quebecor now provide logistics, distribution, and direct mail marketing services. National postal authorities have contributed to these changes. Deutsche Post, the German postal authority, is the parent company of DHL, now the world's largest logistics services provider following the acquisition of Excel. However the German government now owns a minority stake in Deutsche Post, reflecting the global trend of liberalization and privatization of postal services. In the US, where the government postal agency has a union density rate nearly ten times greater than the private sector, de-unionization is an essential feature of the privatization process.

The findings also suggest how firm strategies influence postal managers who must balance the contending interests of greater economic efficiency against protecting the public good of universal service (Hefetz and Warner 2004; Clark and Bickerton 2002). The US model of public-private partnership in the provision of postal services has resulted in the privatization of major portions of the postal network. While this has arguably introduced competition in the upstream sectors of the industry, the process has been

careful to constrain the competitive power of the USPS. In short, private corporate interests have inserted a third set of goals into the contested terrain of privatization—pulling the process in a direction that results in industry restructuring to improve their own market power while constraining the level of competition. What has been criticized by opponents of privatization as market failure (Starr, 1987; Sclar, 2000) is the outcome of private companies behaving rationally and strategically.

The first section following this introduction places the case of the US mailing industry within the larger public policy debates concerning the privatization of public services. Next, the paper provides a brief overview of the structure and governance network of the USPS. Despite years of stalled postal reform legislation, postal administrators have introduced profound changes in the network through various initiatives designed to promote public-private partnerships. The third section of the paper examines these reforms in more detail by focusing on the introduction and implications of worksharing. As the name implies, worksharing is a practice in which the USPS “shares” work with the private sector by providing rate discounts to mailers who present mail that has already been pre-sorted or mailed closer to its point of delivery. The fourth section concludes by highlighting some of the impacts of the privatization process on the US mailing industry and discussing some of the broader implications of this case.

#### **BUSINESS STRATEGIES AND NEW POSTAL MANAGEMENT**

While there is a vast literature on business strategy (Montgomery and Porter, 1991; Drucker, 1954; Porter, 1980), a consistent and central theme in the literature has focused on competitive strategies. In Porter's model (1980), competitive strategy is directed at the five structural determinants of industry competition: potential entrants, buyers, suppliers, substitutes, and industry competitors. As in contingency theories (Donaldson, 2001) Porter often argues that a firm needs to position itself appropriately, given the competitive environment. However, Porter takes strategy one step further, beyond adaptive capabilities, to show that a critical element of firm strategy is to influence the five sources of competitive pressures. According to Porter, “The goal of competitive strategy for a business unit in an industry is to find a position in the industry where the company can best defend itself against these competitive forces or can influence them in its favour” (Porter, 1980, p. 4).

According to this strategic logic, businesses have a strong incentive to develop anti-competitive strategies (Sclar, 2000). This includes creating barriers to potential market entrants and strengthening one's bargaining power vis-à-vis suppliers and customers. Taming the competitive pressures from suppliers or buyers may involve vertical integration

or reducing rivalry among existing firms through mergers and acquisitions. In addition to constraining competition, acquiring resources (Barney, 1996) and developing key relationships with outside stakeholders, such as political allies, are other important areas of competitive strategy. The transformations taking place in the global logistics industry in general and postal services in particular reflect these competitive theories. Global firms such as UPS and FedEx have simultaneously consolidated the industry through acquisitions while striving to constrain the competitive abilities of national postal authorities. Both firms are major competitors of the USPS, while at the same time they are also major contract service providers. For companies like UPS and FedEx, political debates over postal reform are not a simple question of the privatization of government enterprises. Indeed, many private firms in the US mailing industry look at the German example of a privatized Deutsche Post and its rapid rise to global competitive strength with trepidation.

The transformation of Deutsche Post from a government operated postal authority to a global leader in logistics services was rapid. In 1995, regulatory reforms split the government operations of postal, financial, and telecommunication services into three distinct stock companies. For Deutsche Post, this reform marked the beginning of a rapid expansion of its operations through acquisitions and mergers. By the end of the decade, Deutsche Post had acquired major air freight companies Danzas and DHL International. As an independent government enterprise, Deutsche Post purchased the government owned shares of Deutsche Postbank. In 2000, the initial public offering of Deutsche Post stock was the largest in Germany and the third largest in the world (Hickey *et al*, 2005). The sale of 29 percent of the company's stock generated 6.6 billion Euros in new capital and fuelled the acceleration of acquisition and expansion activity after 2000. In the North American market, Deutsche Post, through its DHL brand subsidiary, purchased Airborne and a number of pre-sort mail service providers including Smartmail and Quickpak. In 2005, the now global firm bought the largest logistics services provider, Excel Plc. That same year, the German government became a minority stockholder. Over the span of ten years, Deutsche Post had transformed itself from a national postal authority into the world's largest global logistics corporation.

The comparative differences between the US case of postal privatization and the trajectory of Deutsche Post raises two intriguing questions. First, the formal liberalization and privatization of German postal services appears to contradict some of the well-developed claims of the varieties of capitalism literature (Hall and Soskice, 2001; Streeck and Thelen, 2005). Germany, an ideal type for the coordinated market economy, has fully embraced liberalization and privatization of postal services. In contrast, in the US, despite being the quintessential liberal market economy, postal reform has been much more constrained.

The differences in state structure and in the adoption of the principles of public management reform (Pollitt and Bouckaert, 2004) may provide some insights into the divergent trends. However, the role of private firms in constraining the competitive ability of government enterprises provides a more compelling explanation. Specifically the roles of major global firms in the US like UPS, FedEx, and Pitney Bowes, as well as smaller, national actors like APX Logistics show how private firms impact the transformation process.

UPS, with annual revenues exceeding \$36 billion, is the largest package delivery company in North America, employing some 380,000 workers, most of whom are unionized. FedEx is the largest express delivery company in North America, employing some 200,000 mostly non-union workers. While the two package delivery giants are fierce competitors, they cooperated to limit the competitive threat of DHL. FedEx and UPS tried to block DHL's purchase of Airborne, claiming that such a purchase would violate US aviation rules that prohibit foreign ownership of domestic air carriers. In order to meet the regulatory requirements, DHL bought Airborne's ground operations on the condition that Airborne's air operations would be separated into an independent entity, ABX Air (DHL, 2003).

This was not the first time that UPS had tried to constrain the German postal operator. In 1994, UPS filed a complaint with the European Commission alleging that Deutsche Post cross-subsidized its non-reserved, competitive services, such as parcel and express delivery, from revenues derived from its highly profitable regulatory monopoly (Dunne and Wolffe, 1999). After the European Commission's director general declined to take up the case against the German post office, UPS brought its complaint before the US Justice Department, urging it to invoke the US-European Union antitrust agreement against Deutsche Post. The continued pressure worked. In 2001, the European Commission ruled that the German postal service had illegally used profits from its monopoly protected operations to subsidize its parcel and package delivery services (Andrews, 2001). As a result, Deutsche Post agreed to pay a fine of 24 million euros, and to separate its monopoly business in letters from its competitive operations in parcel delivery.

In April 2000, UPS filed suit against the Canadian government under provisions of Chapter 11 of the North American Free Trade Agreement, seeking some USD \$156 million in damages (UPS Sues Canada, 2000). As in the German case, UPS alleged that Canada Post's express rates were lower than the costs of delivery because of cross-subsidization from its monopoly protected first-class mail (Brooks, 2001). In 1993, Canada Post had obtained a majority interest in Purolator Courier, which had the largest share of the Canadian courier market. The lawsuit claimed that the Canadian government unfairly allowed Canada Post Corporation to expand beyond its monopoly-protected mail delivery business into competitive sectors.

Smaller, private firms like APX Logistics have driven similar trends of reducing competition through consolidation and industry restructuring. APX Logistics was the largest parcel and package workshare partner of the USPS (APX 2002; Malloy 2004). This privately-held company was a third-party logistics supplier, specializing in business-to-consumer package delivery through the USPS worksharing program. APX consolidated and sorted packages from over 260 catalogue retailers and other direct marketers. By combining the packages into larger shipments and delivering them directly to the destination post office for final delivery by USPS letter carriers, APX profited from workshare discounts. In this way, APX was a creation of privatization and workshare practices.

Financial control of the company rested with the private equity firm Heritage Partners, based in Boston, Massachusetts. Heritage specializes in the acquisition of mid-sized privately held firms with high growth potential. Upon acquiring a majority stake in APX in 1996, Heritage financed a string of consolidations that more than quadrupled APX's operations. In 2004, Heritage financed the acquisition of RR Donnelley Logistics, making APX a fully integrated business-to-consumer delivery network, with nationwide coverage and over \$770 million in revenue (Malloy 2004).

Pitney Bowes has been associated with the US mailing industry since 1920. Long-known as the company that manufactures and leases postage meter machines, Pitney Bowes remains a trendsetter in the global mailing industry. While postage meters and other mailing machines remain the core of Pitney Bowes' operations, the company is expanding its reach throughout the mailing industry. Pitney Bowes has pursued complementary economic and political strategies to boost its market power and constrain competitive threats in North America and around the world. The business strategy, in the words of CEO Michael Critelli, is "to touch as many pieces of mail as possible, at as many points in the mailstream as we can and add value at each step in the process" (Fischer 2005). Pitney Bowes is not only a critical economic partner of the USPS, but CEO Michael Critelli has been one of the highest profile advocates of postal reform.

The USPS has not been sheltered from the fierce debates over the nature and role of public management that reached a crescendo in the 1990s and continues today. In a way, the USPS was a precursor to these debates following the Postal Reorganisation Act of 1970, when the Post Office was transformed from a governmental department into a commercial enterprise. While political support for complete privatization of the USPS has been limited (Adie, 1989; Geddes, 2002) pressure for significant reforms has grown substantially in the last ten years. The debate over the appropriate role of the USPS in the mailing industry reflects the much larger debate over the role of the government as an economic actor and market regulator (Christensen, 2002; Savas, 2000; Sclar, 2003; Starr, 1987).

The global wave of postal reform and privatization efforts are driven, at least in part, by the rise of neo-conservative political activists (Campbell, 2002). Markets, according to this broad group of government reform advocates, provide a better mechanism for funding and managing the provision of services than government monopolies (Savas, 2000; Adie, 1989). Critiques of privatization and market-based government reform efforts have contended that market solutions like privatization not only fail on measures of efficiency, but also raise concerns over equity, democracy, and the preservation of public goods (Miraftab, 2004; Milward and Provan, 2000; Warner and Hefetz, 2002). Similarly, debates over postal reform generally fall into two opposing viewpoints; those who want to eliminate the government monopoly in order to increase economic efficiency, versus those who want to retain it in order to protect universal service (Crew and Kleindorfer, 2003). Neither camp defends economic inefficiencies or the erosion of public service, while both can point to such negative effects in the strategies of their opponents. However, this simple bifurcation of contending perspectives does not capture the complex interests at work in the transformation of the Postal Service. Private corporate interests can be shown to place unique pressures on public managers that do not fall into the simplistic frames of economic efficiency versus the protection of public goods.

In addition to the larger, macro-organizational trends of commercialization and privatization, USPS managers initiated a number of micro-organizational changes consistent with the ideas promoted by advocates of New Public Management (Savas, 2000). In April 2002, postal managers published a "Transformation Plan" in response to growing political pressures for postal reform and significant losses in operational performance (United States Postal Service, 2002). Management strategies included the continued adoption of automation and other productivity enhancing technologies. Postal managers targeted significant efficiency gains in the transportation and delivery networks, especially through the consolidation of distribution hubs and the closing of revenue-losing postal facilities. However, not all of the efficiency-based strategies focused solely on internal operations. Postal managers also raised the need to explore new workshare and other mail preparation opportunities with private companies. Finally, the plan outlined a number of human resource management strategies to reduce costs and enhance productivity in the workforce. In combination, these strategies have resulted in a significant reduction in the number of employees, despite the continuing growth in the size of the postal network.

#### US MAILING INDUSTRY

The USPS is one of the largest government entities, employing over 700,000 career employees, one quarter of the total federal workforce, and posting revenues of some \$70 billion per year (USPS, 2006). As part of its current

Universal Service Obligation (USO), the USPS reaches over 142 million delivery points six days a week, except on federal holidays (USPS, 2006). Access to the postal network in all communities is provided through some 37,000 post offices. The USO also mandates service standards, product categories, and uniform pricing of First-Class letter mail regardless of geographic location. Not only is the USPS the largest national post in the world, but even compared to the private sector, it represents one of the largest commercial enterprises. The Postal Service is the centre of a much larger mailing industry in the US that is estimated to generate \$900 billion (USD) in domestic economic activity and employ nearly 9 million workers (Mailing Industry Task Force, 2002).

In simple terms, the USPS moves letters and parcels from point A to point B. The actual network is far more complex, particularly when private sector access to the network is added to the mix. However, the mailing industry constitutes much more than the postal network used to transport first class letters. The industry ties together a vast conglomeration of manufacturing firms and service providers, an international network of government agencies and commercial enterprises and large, multinational private firms. From advertising agencies to paper manufactures and transportation service providers to individual citizens, the mailing industry is comprised by a diverse network of industry segments. The “upstream” portion of the mailing industry includes mail drivers, such as advertising and billing, physical mail production, collection, and initial sortation and distribution. Transportation between distribution centers is typically considered a transitional stage. “Downstream” activities then include destination sortation, distribution, and delivery. An increasingly important component of the mailing industry’s downstream operations includes returns and customer service management. Key actors in each of these industry segments have caused incremental changes in the industry’s institutional arrangement.

As a result of these efforts to build public-private partnerships in order to reduce costs through worksharing, outsourcing, and contracting, the USPS network is an almost completely open system. The only portion of this network that remains closed to private sector access is the final delivery by a USPS letter carrier. However, even in this segment of the postal network, postal managers have clashed with postal unions and their political allies over the right to contract out the last mile delivery services. Worksharing practices, discussed in more detail in the next section, allow private companies to collect, sort, and transport mail to the destination delivery unit (DDU), which is typically the local post office from which a recipient’s mail is delivered.

Major mail users like the Readers’ Digest had unsuccessfully requested rate discounts for mail preparation from Congress in the 1960s, prior to the Postal Reorganization Act and the 1970 creation of the Postal Rate Commission (PRC). Large mailers had already been

engaged in pre-sorting activities prior to the implementation of discount rates in order to improve the delivery speed of their products. In 1973, the PRC began reviewing the first request by the USPS to initiate discounted rates for workshared mail. In 1976, the PRC recommended and the USPS Board of Governors approved a one cent discount for pre-sorted First Class mail. At the time, only about 44 percent of letters were sorted on automated equipment at the USPS, so worksharing helped “bridge the gap” between manual processing and automated sortation. What initially began as a management strategy to phase in new sortation technologies has evolved into a major marketing strategy to increase volumes from large mailers. Since its inception in 1976, worksharing discounts have extended to nearly all classes of mail and various levels of sortation and insertion.

Another major form of private sector activity in the postal network involves direct contracting with private companies for various products and services. In 2004, USPS contracted some \$1.4 billion with private air carriers. Most of this was paid to Federal Express which has had the exclusive contract to provide air cargo services for the USPS’ priority mail product (USPS, 2006). While this paper focuses on worksharing, outsourcing and contracting-out represent major areas of public-private interaction accounting for over \$15 billion (Elcano *et al.*, 2000).

In addition to suppliers and contract service providers, major generators of mail volume, such as financial institutions and direct marketing and advertising firms, are key economic actors in the mailing industry. USPS publications promote the mail as a public communications medium, however the emphasis increasingly focused on the commercial value of mail in customer relations management (USPS, 2002 and 2006). Major mailers have become the citizens for whom the public good of postal services is designed to serve. This complex web of economic relations forms an important part of the overall governance structure of the USPS. Private firms not only influence USPS administrators through economic means, they are also highly organized political actors within the USPS governance structure.

As an independent entity of the US Executive branch, the USPS’ formal administrative structure is comprised of the Board of Governors and the Postmaster General, who serves as the chief executive officer of the enterprise. The President of the United States appoints the nine members of the Board of Governors, who in turn select the Postmaster General. Managing authority of the USPS rests with the Board of Governors, which is modeled after the private sector board of directors for publicly traded firms. The Postal Service is regulated by a separate government entity, the Postal Rate Commission (PRC), an independent regulatory review agency whose five members are also appointed by the President of the United States. Changes in rates, mail

classification, public service levels, or other items covered under regulatory statutes require review by the PRC.

These public hearings provide mailers, unions, and other government agencies the opportunity to engage in public policy debates over postal reforms. In this way, the USPS governance structure is comprised of a broad network of economic and political actors, from both the private and the public sectors. Evidence of the influence of this diverse governance network is seen in the ascendance of a commercial orientation and the adoption of corporate strategies among postal administrators. This “corporatization” of the postal administration is characterized by the promotion of public-private partnerships, the dominance of efficiency concerns in human resource and operations management, and the centrality of commercial value to its mission of public service.

Political debates over the nature and direction of postal reform have intensified over the past decade. In the 2006 legislative session, the Senate passed postal reform legislation that closely resembled a similar bill that passed the House earlier (Stevens 2006). Although initially supportive of the reform bills, the USPS has since voiced opposition to the reform bills. The White House has expressed differences with the reform bills and USPS administrators (Stevens, 2006). Such differences between political officials and postal managers had emerged in earlier debates. A special report issued in 2003 by President Bush’s Commission on the United States Postal Service contained recommendations more controversial than USPS managers have been willing to embrace (President’s Commission, 2003).

The President’s commission consisted of several top industry managers and included a special subcommittee on private sector partnership. This subcommittee recommended that “those Postal Service functions that can be performed better and at a lower cost by the private sector be outsourced to the private sector” (President’s Commission 2003, p. 173). However, the most controversial recommendations of the Commission emerged from the workforce subcommittee, which called for significant workforce reductions, fiscal constraints to the collective bargaining process, and the elimination of the perceived postal wage premium (Stevens, 2006). The Commission recommended expanding worksharing discounts and Negotiated Service Agreements that provide discounts to individual major mailers. However, the recommendations did not call for any fundamental changes in the Postal Service’s basic structure as a government commercial enterprise or towards a private ownership structure. Compared to the reforms underway at other national posts, the changes recommended by the President’s Commission suggest a more controlled transformation of the mailing industry, constraining the competitive flexibility of the USPS.

## WORKSHARING

The practice of granting worksharing rate discounts to private companies who perform preparation work on mail that otherwise would be done by the Postal Service has driven some of the most substantial changes in the mailing industry over the past thirty years. As a form of public-private partnership, the impacts of worksharing on the mailing industry provide valuable insights into the role of private companies in postal reform and the impacts of privatization on the industry. This section provides a brief overview of worksharing practices in the US mailing industry. To examine the goals and impacts of private companies in more detail, this section focuses on two key worksharing partners, Pitney Bowes and APX Logistics. Both of these companies have specific interests that they pursue through their partnerships with the USPS. These interests have shaped the nature and extent of postal reform and contributed to the transformation of the industry.

Worksharing enjoys broad political support, while critics tend to focus on the technical issues related to the size of the discounts rather than the practice itself (Kolin, 2000). Proponents of this model of public-private partnership, including USPS managers, major mailers, and service providers, claim that worksharing improves economic efficiency by introducing competition in the postal network’s upstream segments of collection and distribution, while protecting universal service at the downstream point of delivery (Haldi and Olson, 2004).

Critics of the practice, including the American Postal Workers Union (APWU), claim that certain rate discounts exceed the costs avoided and therefore provide an unfair subsidy to major mailers that other mail users, especially individual citizens, are forced to cover (Ryan, 2000). USPS managers are very conscious of this political balance. In response to the 2003 GAO study of worksharing, the USPS’ chief marketing manager, Anita Benzitto stated, “From the inception of worksharing discounts, the Postal Service and the PRC have been concerned with both equity and economic efficiency,” (US GAO 2003, p. 48).

While the size of the discounts remains politically contested, the practice has created some of the most substantial and dynamic changes in the mailing industry. Worksharing practices involve more than simple pricing strategies by the USPS; ultimately it constitutes a piecemeal form of privatization of the Postal Service network. Combined with outsourcing and other contracting practices, worksharing has made the US postal network one of the most privatized in the world (Elcano *et al*, 2000). As described by PRC advisor, Robert Cohen, “worksharing is essentially the exporting of work that otherwise would be performed by the Postal Service to mailers or third-party consolidators,” (Cohen *et al*, 2004, p. 122). However, worksharing creates a peculiar form of privatization, much different than the type of privatization experienced by

other national posts (Campbell, 2002) and most other US governmental agencies.

Currently, worksharing activities replace only the upstream segments of the Postal Service network, including sortation and transportation. The USPS' last mile delivery network remains unaffected. In this way, worksharing provides a mechanism for privatizing segments of the US mail stream and exposing the USPS to competitive pressures. At the same time, unlike the privatization models in Germany and the Netherlands, worksharing promotes liberalization of the industry without turning the USPS into a competitive threat to private firms.

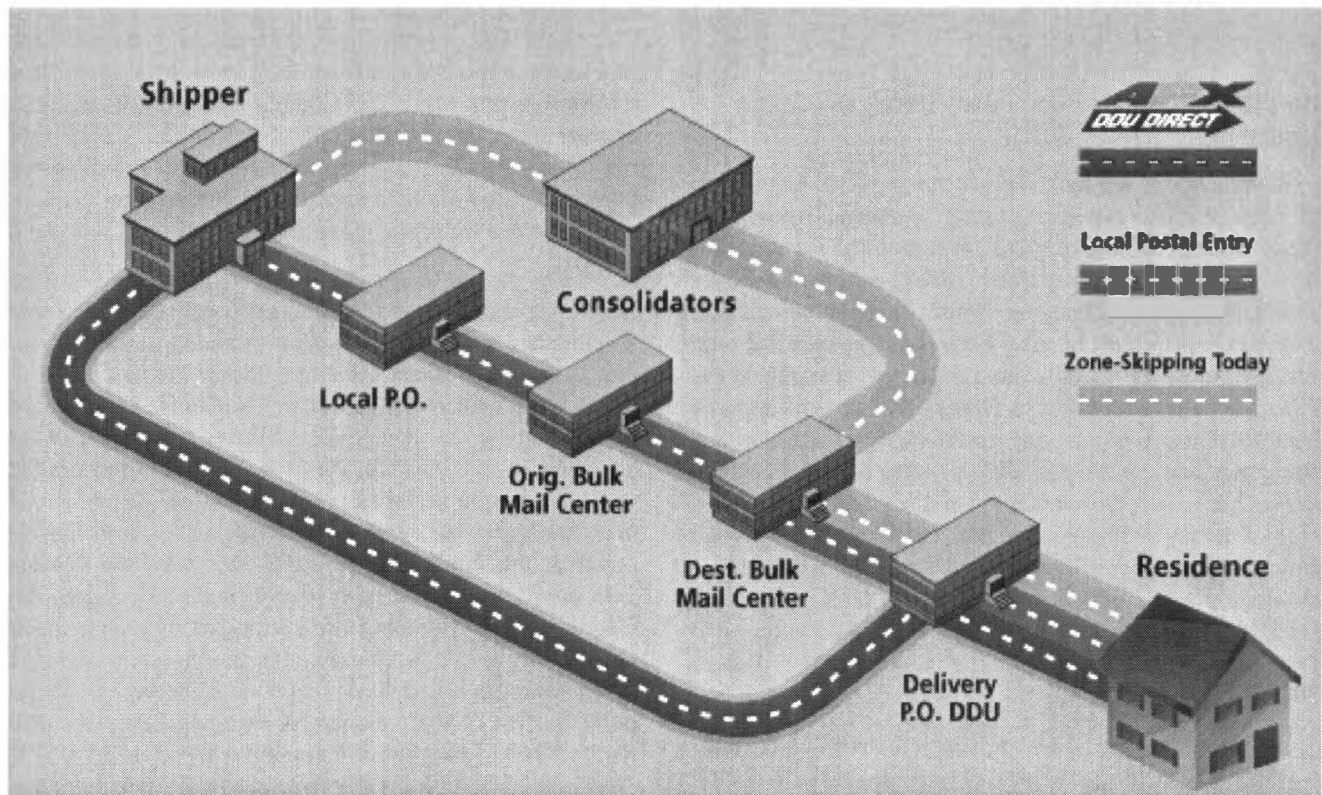
The most common form of worksharing rate discounts involves private companies pre-sorting and bar-coding mail in 3-digit or 5-digit zip code order prior to entering it into the USPS system. In exchange for this preparation work, mailers receive rate discounts of 7.8 cents or 9.2 cents on First Class pre-sorted mail (US GAO, 2003). Other types of worksharing activities include barcoding mail so that it can be handled by automated sortation equipment, pre-sorting mail in zip code or even letter carrier walk sequence order, and entering mail at a Postal Service facility close to its final destination. Figure 1 gives a graphical representation of this third form of worksharing, often called "dropshipping." Rather than presenting mail at the local post office and

having the postal service transport it through the system and eventually deliver it to the end customer, mailers receive discounts for inserting the mail further into the mail stream.

Economies of scale are critical to achieve distributive density, therefore shippers must handle sufficient volume to sort and deliver closer to the point of delivery. This is often achieved through consolidation from several different catalogue houses or major mailers. Direct mail marketing firms make the most use of dropshipping discounts. ADVO Corporation, the largest USPS customer (Hickey *et al*, 2005), sends some 80 million pieces every week by entering them into the mailstream at the Destination Delivery Unit (DDU). Overall, workshared mail has grown, while the volume of non-workshared mail has remained flat or declined. Figure 2 shows the overall trends in volume of workshared and non-workshared mail since the discounts were first introduced in 1976 (US GAO, 2003).

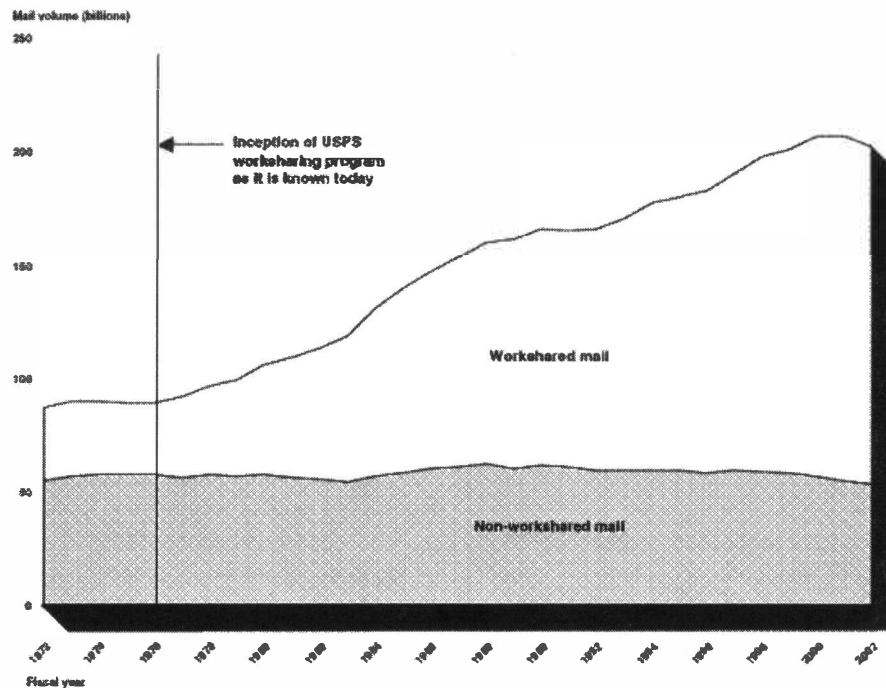
Currently, most mail delivered by the USPS is first handled by private sector firms. Some 74 percent of all mail in 2002 was workshared (US GAO, 2003). As a result, most of the mailing industry's upstream activity now takes place in the private sector. Standard mail, such as advertisements and catalogues, comprise the bulk (58 percent) of workshared mail. Thirty-four percent of workshared mail

**FIGURE 1**  
**Privatization through worksharing**



Source: APX Logistics Inc., [www.shipapx.com](http://www.shipapx.com)

**FIGURE 2**  
**Workshared mail volumes 1970-2002**



Source: Government Accounting Office (GAO), 2003

is First-Class, while periodicals and packages comprise seven percent and one percent respectively. In 2003, for the first time, workshared First-Class mail exceeded individual, single piece, First-Class letters.

### Partners and competitors: Pitney Bowes and ABX Logistics

These trends not only reflect the growing dominance of large mailers, but worksharing companies have been consolidating the industry and promoting the privatization process. This is especially true in the pre-sort mail industry which is rapidly changing from local mom-and-pop lettershop operations, to subsidiaries of large multinational firms. Leading the consolidation of the pre-sort industry is Pitney Bowes. According to Henry Daboub, president of National Presort, a company that manufactures presorting equipment and used to provide presorting services, "Pitney Bowes came into the market, hit me over the head with a sack of money and bought me out" (Centor 2004). Daboub added, "all of the smaller players in the industry will either close shop or be bought out within the next two years." In 2004, Pitney bought PSI Group, which was at the time the largest presort company in the industry (Pitney Bowes 2002).

Pitney Bowes' CEO, Michael Critelli, has been instrumental in the political organization of the industry. Along with the former deputy postmaster general John

Nolan, Critelli formed and continues to lead the Mailing Industry Task Force, an industry organization dedicated to promoting and improving the value of mail in society. Due to the lobbying limitations placed on that task force as a result of the USPS affiliation, Critelli also established the Mailing Industry CEO Council as a spin off to focus entirely on political action and postal reform. Companies like Pitney Bowes, large mailers, and other private firms organized into various industry associations form peculiar political allies for postal managers.

Pitney Bowes has a symbiotic relationship with the Postal Service. It is in the company's interest to promote a viable and growing government-provided postal service. However, at the same time that Pitney Bowes seeks to expand the mailstream, they seek to limit the scope of USPS activity to "universal physical mail service at affordable rates" (Critelli, 2003). Critelli has been critical of German style privatization measures, speaking against privatization of the USPS, but expansion of worksharing practices (Hickey *et al*, 2005). In this way, the debates over postal reform and privatization in the US display the distinct influence of competitive strategies by private firms. On the one hand, firms recognize the commercial value of universal, public delivery network. However, given the public nature of the commercial enterprise, they are able to effectively constrain the competitive threat of the USPS. As a result, the process of privatization has been gradual, focused more on constraining the competitive abilities of

the USPS than on promoting economic efficiency in the provision of public services.

For another major workshare partner and political ally of the USPS, management strategies in the APX case included not only the consolidation of the newly privatized market but also the reduction of labour costs in the mailing industry through de-unionization. Non-union subcontracting arrangements were a key part of APX's business model. APX contracted much of its transportation work with truck drivers who own and operate their own vehicles or through brokers who leased the owner-operators to APX. Since the US trucking industry was deregulated in the early 1980s, owner-operators have faced hyper-competition and deteriorating working conditions (Belzer, 2000). Labour unions have challenged the classification of these workers as independent businesses which makes collective bargaining on their behalf a potential violation of the US Sherman Anti-Trust Act. These contracting arrangements have not only contributed to the de-unionization of the industry, but such industry restructuring creates inefficiencies as much of the economic risk of inefficiency is shifted to individual workers.

The business interests of the private equity firm that owned APX displayed a conflicted partnership with postal managers. As a private equity firm, Heritage's business model has been to invest in mid-sized, family owned companies, finance their growth, and sell their equity stake for a profit. The company's typical investment target window is three to seven years. Exit strategies include sale back to management, an initial public offering on a public stock exchange, or sale to another company. However, in March 2006, the General Partners at Heritage chose a very different strategy, bankruptcy and liquidation. The abrupt demise of APX left postal customers scrambling and major companies like FedEx and DHL, which both have their own worksharing parcel divisions, taking customers and pushing up prices (Boyd, 2006). In the end, the public good in this public-private partnership between APX and the USPS fell victim to internal disputes among senior partners at a private equity firm in Boston (Morris, 2006)

### **Private firms, public partnerships, and competition**

Private firms like Pitney Bowes and APX Logistics have been important allies to postal managers, providing both economic resources and political support to the USPS. At the same time, these partners have been careful to push postal reforms in a direction that limits the competitive discretion of postal managers. These cases highlight three features of the influence of private firms in the transformation of the US mailing industry.

First, the process of privatization is more complex than the simple shift of economic activity into the private sector. In these cases, privatization created new markets, promoted industry consolidation and increased the interdependence of public and private enterprises. Second, partnerships between private firms and public managers is

also a complex, and at times, contradictory relationship. Postal managers have benefited from the political supports of industry associations like those organized by Pitney Bowes. This support comes at the cost of having the public good of postal services increasingly shift towards the private interests of commercial value. Finally, in contrast to the advocates of New Public Management who promote privatization as a mechanism for increasing competition, Pitney Bowes, APX and other private firms have explicitly tried to limit competition and have turned privatization into a tool to do so.

### **CONCLUSIONS**

The global logistics industry in general and the US mailing industry in particular are in the midst of a major transformation. Many factors contribute to the transformation including changes in technology and communications systems, as well broader marketing and economic trends. This paper has focused on the role and influence of private firms on the industry's transformation through public-private partnerships with the USPS. The core argument of the paper is that the influence of private firms has tended to pull the process of privatization and postal reform in a direction that reflects their distinct business strategies and corporate interests. Examining the process of privatization simply by whether it improves market efficiencies or threatens the universal provision of public goods misses the critical role played by these private actors.

The transformation of the mailing industry has featured consolidation, de-unionization, and the constraint of competition. The case provides evidence to suggest that these changes can be attributed to distinct interests in the private sector that seek to limit competitive threats as a top business priority. Pitney Bowes is a strong advocate for universal mail services, but it also works hard to limit the competitive flexibility of the USPS. Before bankruptcy, APX provided low-cost package services, funnelling a million packages a day into the USPS delivery network. However, these lower costs, achieved through de-unionization of the mailstream, did not survive the industry's consolidation, a trend that APX, even in its demise, helped promote. As a result of the abrupt closure, postal managers were forced to act as customer service agents for the defunct APX, steering the former customers not to the regular USPS network, but instead to FedEx, DHL, and UPS.

For public managers and public administration scholars, the case of the US mailing industry suggests that if public enterprises are any less efficient and competitive, it may not be because of self-serving bureaucratic interests, but a result of the competitive strategies of private firms. The governance network of the USPS provides private firms with numerous mechanisms to influence and constrain the competitive abilities of postal managers. The US mailing industry case raises important questions for future research into the practice of public-private partnerships.

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