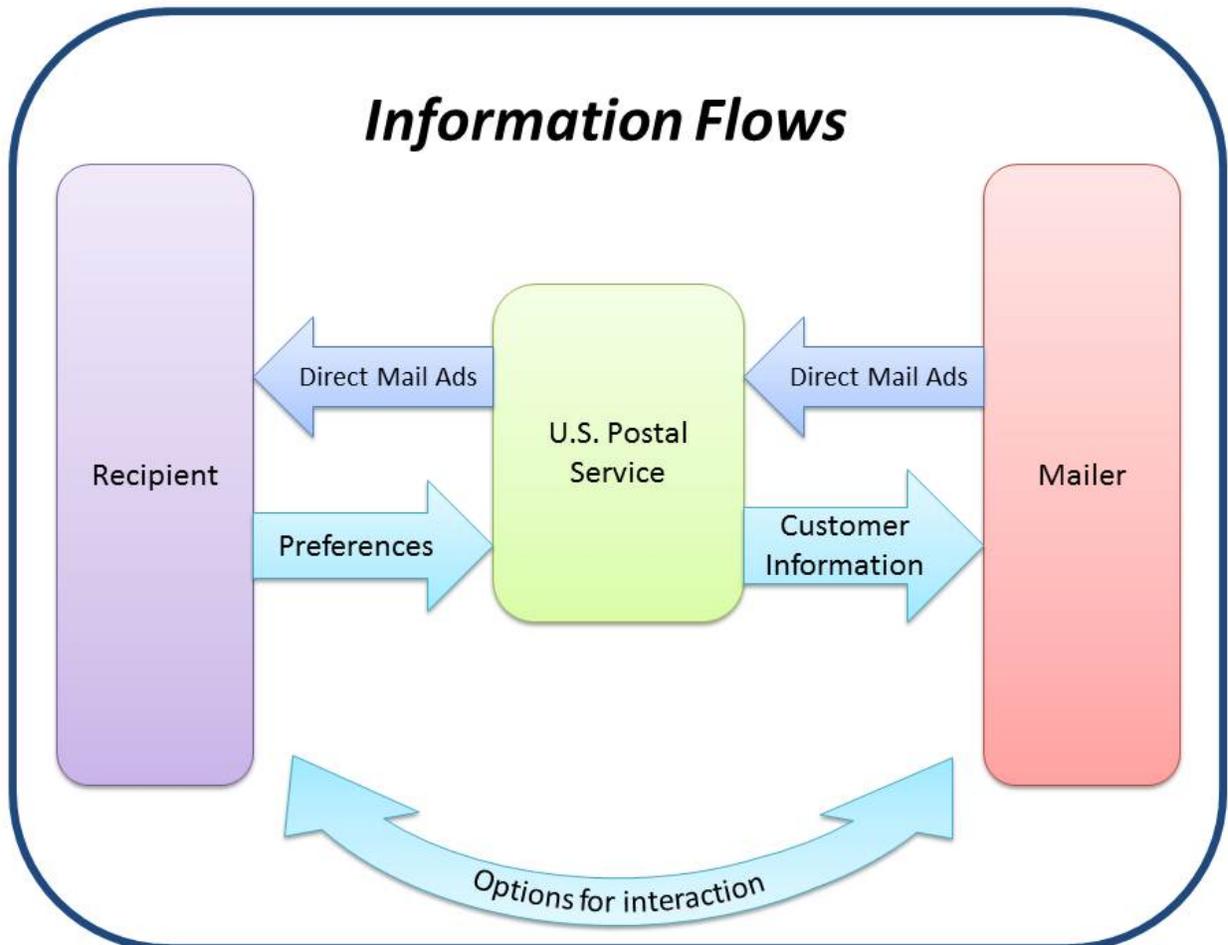




Strengthening Advertising Mail by Building a Digital Information Market

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Advertising mail is a significant source of revenue for the Postal Service. It generated \$16.9 billion in fiscal year 2013. Moreover, advertising mail has so far maintained its market share, despite radical changes in the advertising market. However, this resilience may not continue forever. Some digital methods of advertising offer more robust ways than direct mail to gather recipient feedback. The Postal Service cannot afford to be complacent.

A key part of advertising is gaining individuals' attention, and the study of attention and its role in the economy is known as attention economics. The U.S. Postal Service Office of Inspector General asked two experts in attention economics, Marshall Van Alstyne of Boston University and Geoff Parker of Tulane University, to analyze the advertising mail market and suggest ways to strengthen advertising mail.

They identified the lack of a robust digital feedback loop between recipients and senders as a critical gap. They suggest expanding the Postal Service's hard copy platform for advertising mail into a digital information market. Participation by recipients would be voluntary, and there would be clear privacy guidelines. Recipients could scan a code or symbol on advertising mail pieces with their smart phones or tablets and access an interactive system for providing feedback on the mail piece. Those recipients who gave feedback would receive an

Highlights

Maintaining the health of advertising mail is a strategic imperative for the Postal Service.

Advertising mail has important strengths, particularly tangibility. However, the ability to build a two-way link to recipients is not as robust as in digital advertising.

The Postal Service could digitally enable hard copy mail by building a digital information market. Mailers would place a code or symbol on advertising mail pieces. Recipients would be rewarded for scanning the code with their smart phone and providing feedback.

The information market would encourage recipients to share their preferences, using clear opt-in and privacy guidelines. It could provide a "win-win-win": increasing the value of the mail to the mailer, recipient, and Postal Service.

Information Coupon (Info-Coupon) that could be redeemed for merchandise or services from a variety of vendors participating in the program.

A digital information market would improve the value of the advertising mail channel for senders, recipients, and the Postal Service. Mailers could use the feedback to determine recipients' preferences about particular forms of advertising. This would allow mailers to target more precisely and improve their return on investment. Recipients would be rewarded for participating in the market through the Info-Coupon. The direct mail they received would also better reflect their interests. The Postal Service would benefit from the improved value of the advertising mail channel. If the market were well structured, its creation could be a win-win-win for everyone.

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Strengthening Advertising Mail by Building a Digital Information Market

Advertising mail, also known as direct mail, is one of the Postal Service's core products. Standard Mail, which includes both advertising and nonprofit solicitations, generated \$16.9 billion in revenue and represented more than half of mail volume in fiscal year (FY) 2013.¹ As First-Class Mail continues to decline, Standard Mail will become increasingly important to the sustainability of the Postal Service's network.²

Three Current Strengths of Advertising Mail

Surprisingly, despite the radical disruption of the advertising market unleashed by the Internet, advertising mail has held its market share against other forms of advertising remarkably well. The digital revolution has significantly disrupted many traditional vehicles for hard copy advertising, such as newspapers and magazines, yet Standard Mail revenue has held steady at approximately 10 percent of total advertising spending for the past 20 years.³

Despite the radical disruption of the advertising market, advertising mail has held its market share remarkably well.

The secret of this success lies in advertising mail's three distinct characteristics:

1. **Tangibility** – Many recipients like to hold or touch catalogs, coupons, and offers. This tangibility is a significant asset. Neurological research has shown that the brain has a stronger physical reaction to hard copy mail than the same information presented electronically.⁴ Advertising mail shares tangibility with other forms of print media.
2. **Targetability** – Mailers can send their ads to customers with whom they have a previous business relationship, or they can seek prospective new customers by using demographic information to select mail recipients. They can also send ads to recipients in a particular geographic area, which is especially useful for local businesses who are trying to attract and retain local customers. Targetability is

¹ U.S. Postal Service, Form 10-K Fiscal Year 2013, <http://about.usps.com/who-we-are/financials/10k-reports/fy2013.pdf>, pp. 23-24.

² Although the vast majority of advertising mail is sent via Standard Mail, First-Class Mail also contains some advertisements and may offer an additional opportunity.

³ U.S. Postal Service, "Responses of the United States Postal Service to Questions 1-9 of Presiding Officer's Information Request No. 1," Postal Regulatory Commission Docket No. R2013-11, October 30, 2013, <http://www.prc.gov/Docs/88/88168/POIR.1.Resp.pdf>, 4(c).

⁴ U.S. Postal Service Office of Inspector General, *Enhancing Mail for Digital Natives*, Report No. RARC-WP-14-001, November 18, 2013, http://www.uspsoig.gov/sites/default/files/document-library-files/2013/rarc-wp-14-001_enhancing_mail_for_digital_natives.pdf, p. 5.

also a feature of digital media. Other forms of advertising are targetable to a lesser degree.

3. **Measurability** – Mailers collect data on who responded to their advertising campaign. Some mailers, or third party firms, merge response and purchasing information with other customer data to predict specific customer responses to different campaigns. The sophistication of measurements varies. At the high end, measurability can involve complex analytics, using proprietary company data and software. More basic forms of measurability can simply involve counting the number of coupons redeemed at a local shop. Digital media is highly measurable, as advertisers can easily create a two-way link to gather feedback from those they target.

Direct mail's unique combination of tangibility, targetability, and measurability creates a strong product that has been resilient, despite the fast-paced growth of newer advertising channels. However, the Postal Service cannot afford to be complacent about the future of advertising mail. As individuals become increasingly comfortable with digital media and digital advertising channels continue to develop, paper advertising sent through the mail may start to lose market share to other forms of media. Moreover, because direct mail is tangible, it has a greater physical presence in people's lives. This presence is often positive, but poorly targeted, unwanted advertising can appear wasteful to recipients and lead to concerns about mail's environmental impact.

Direct mail's combination of tangibility, targetability, and measurability creates a strong product.

Finally, the two-way link that can be easily established when a digital ad is opened is a real benefit that does not exist today with direct mail. Mailers receive inquiries or orders from a small percentage of mail respondents,

but in most cases, they do not know how an individual recipient has reacted to their ad. Is the offer interesting, but the timing wrong? Does the customer want more options or information on other products or services? Or is the customer just not interested at all; was the envelope even opened?

The Postal Service and the direct mail community can strengthen advertising mail and improve the experience for both senders and recipients by developing a stronger feedback loop that provides more detail on recipients' preferences, allowing for more precise customer targeting. This feedback loop could increase mailer revenues and customer satisfaction, while simultaneously maximizing postal revenues and minimizing unwanted mail and waste.

The Value of the Feedback Loop

Information about customer preferences is critical to advertisers. It allows them to target their advertising more precisely to those customers who are more likely to buy something and avoid wasting advertising on those who do not appear interested. Digital advertising offers several options to provide two-way feedback on specific advertising campaigns. For example, email advertisers can determine not only whether recipients

respond to their email offers but also whether they open the emails. Search engines, social media, and other new mechanisms induce customers to reveal information about their interests and what they want to buy. Search engines can provide advertisers precise information on their click rates for various search terms, allowing a business to buy only those terms that are likely to result in customer responses. Cookies allow advertisers to follow customers across the web, so advertisers can see their customers' other interests and develop profiles about them. This behavioral tracking has been controversial and spurred "Do Not Track" campaigns.

The two-way feedback from mail is not as robust as some digital feedback options.

Mailers of hard-copy advertisements expend significant effort to target mail to those most likely to buy, but the two-way feedback loop from mail is not as robust as some digital feedback options. Typically, advertising mailers only receive feedback when customers attempt to place an order or make a donation, with response rates typically running at 2 to 6 percent.⁵ There is no information flowing back to the mailer from the remaining 94 to 98 percent of targeted customers. Although the mailer may know that the recipient did not respond to a specific campaign, the mailer has no idea know why. At present, customers who *want* more information about a certain item or service have limited ways to make mailers aware of their wishes. This "information asymmetry" reduces the value of the advertising mail network. If mailers had better access to recipients' feedback on specific mailings, they could better target their mail, sending more mail that is of value to the recipients and less that is of no value.

Two-Sided Markets, Attention, and the Postal Platform

To understand how enhancing the feedback loop could benefit senders, recipients, and the Postal Service, the concept of a two-sided market is important. A two-sided market is a market that joins two distinct types of customers in a way that takes advantage of network effects and creates value.⁶ The company or group linking the two customers is called a platform. In advertising, two-sided markets are common. Newspapers and magazines sell to readers and advertisers. Broadcast television serves both viewers and advertisers. The platform often mediates between the two sides of the market, and sometimes participation by one side of the market is discounted or even free in order to encourage participation. For example, broadcast television is free to viewers and paid for by advertisers, and for many years, newspaper delivery was heavily discounted to build circulation numbers and raise advertising rates.

The Postal Service is an example of a two-sided market platform.

⁵ The Direct Marketing Association, *DMA 2013 Statistical Factbook*, August 2013, and industry interviews.

⁶ Often one or both sides of the market benefit from the presence of more participants on the other side of the market. For a discussion of two-sided markets, see Jean-Charles Rochet and Jean Tirole, "Platform Competition in Two-Sided Markets." *Journal of the European Economic Association*, Vol. 1 (2003), pp. 990–1029. For more information on the role of network effects, see Geoffrey Parker and Marshall W. Van Alstyne, "Two-Sided Network Effects: A Theory of Information Product Design," *Management Science*, Vol. 51, No. 10, (September 29, 2010), pp. 1494–1504, available at SSRN at <http://ssrn.com/abstract=1177443>.

The Postal Service is also an example of a two-sided market platform.⁷ Senders pay for advertising mail, but ultimately senders use the direct mail medium because they care about reaching recipients and getting their attention. Advertisers track the response rates and return on investment (ROI) from campaigns. If recipients stopped paying attention to advertising mail, ROI would drop and advertisers would soon disappear from the mail. It is in the interest of the Postal Service and senders that recipients find advertising mail relevant and respond.

The study of individuals' attention and its importance in the economy is called attention economics. In this field, attention is considered a scarce commodity, one whose role has been fundamentally altered by the Internet. Recognition of the value of this commodity, and the development of techniques to gain control over it, are providing new insights into advertising markets.

The U.S. Postal Service Office of Inspector General asked two prominent experts in two-sided markets and attention economics, Marshall Van Alstyne of Boston University and Geoff Parker of Tulane University, to analyze the advertising mail market and suggest ways to strengthen the Postal Service's advertising mail product. Building on new research in the area of attention economics and interviews with key stakeholders in the mailing industry as well as on their previous work, Van Alstyne and Parker, together with Tushar Shanker, a Ph.D. student at Boston University, present an interesting approach and some fresh perspectives on the enhancement of advertising mail. A paper describing the results of their research appears in the appendix.

Building a Digital Information Market

Van Alstyne, Parker, and Shanker identify the lack of a robust feedback loop, or two-way link, as an important gap in the business model underlying the Postal Service's strategic approach to advertising mail. They propose that the Postal Service move beyond operating solely as a platform for hard copy mail to act also as a digital platform for information that mail recipients volunteer to provide and share. Participation by recipients on the digital platform would be strictly voluntary. The Postal Service would only release information to mailers as authorized by mail recipients, under clear privacy guidelines.

Van Alstyne, Parker, and Shanker propose that the Postal Service move beyond operating solely as a platform for hard copy mail.

The authors suggest a redeemable Information Coupon (Info-Coupon), which would reward mail recipients for giving feedback.

To incentivize the establishment of a two-way link, the authors suggest a redeemable Information Coupon (Info-Coupon), which would reward mail recipients for giving feedback. Participating mailers would use some type of

⁷ For a discussion of mail as a two-sided market, see Christian Jaag and Urs Trinkner, "Pricing in competitive two-sided mail markets," in *Competition and Regulation in the Postal and Delivery Sector*, edited by Michael A. Crew and Paul R. Kleindorfer (Massachusetts: Edward Elgar Publishing, Inc., 2008), pp. 136-149.

code or symbol — such as a Quick Response (QR) code, Image Recognition code, or Intelligent Mail Barcode — on the front of the mail piece. Recipients could scan the code or symbol and access an interactive system on their smartphone or tablet where they could provide information about their preferences and their response to the mail piece. In return for their feedback, recipients would receive a digital Info-Coupon. The Info-Coupon would be in the form of points redeemable for merchandise from a variety of vendors.

Mailers could use the feedback to determine whether recipients strongly liked or disliked receiving particular forms of advertising. This feedback would increase advertising mail's measurability — allowing more precise targeting, improving direct mail's ROI, and strengthening the value of the direct mail channel. Recipients could choose whether to participate in the information market and digitally reveal information about their preferences. Those who did participate would receive compensation through the mechanism of the Info-Coupon. As conceived by Van Alstyne, Parker, and Shanker, the information market could begin with a simple digital feedback loop. In time, the Postal Service could enhance it by developing new applications and soliciting other types of customer information.

The study of information mechanisms such as the feedback loop started as a response to the problem of unwanted spam cluttering the email channel, drowning out the ability of recipients to pay attention to advertising messages from responsible senders and personal emails. To address this problem, spam filters were developed, and prominent computer experts such as Bill Gates suggested charging for email.⁸ Research suggests that a feedback loop is more economically efficient than filters or blunt “Do Not Spam” or “Do Not Mail” lists for ensuring that customers receive the information they want. A perfect filter can filter out wanted information, depressing potential economic growth.⁹ In the case of advertising mail, some advertising information is desired and useful to customers. However, if recipients have to review and reject many other mailpieces before finding what they want, some may decide not to give any mailpieces their attention. As a result, mail recipients may miss opportunities for purchasing, while mailers may miss opportunities to sell more goods and services. A feedback loop allows mailers and interested recipients to find one another more easily.

Win-Win-Win

While direct mail remains an effective advertising medium, it could be significantly enhanced by the creation of a digital information market tied to hard-copy mail. Such a market would provide a means to add the measurability of digital advertising while

⁸ Saul Hansel, “Gates Backs E-Mail Stamp in War on Spam,” *The New York Times*, February 2, 2004, <http://www.nytimes.com/2004/02/02/technology/02spam.html>.

⁹ The work of Thede C. Loder, Marshall Van Alstyne, and Rick Wash suggests that applying a signaling and screening mechanism for email can create more value for consumers than depriving consumers of all information, including advertising, which they would have found helpful. See Thede C. Loder, Marshall W. Van Alstyne, and Rick Wash, “Information Asymmetry and Thwarting Spam,” (January 14, 2004), available at SSRN at <http://ssrn.com/abstract=488444> or <http://dx.doi.org/10.2139/ssrn.488444>. In their paper in the appendix, Van Alstyne, Parker, and Shanker assert that this principle can also apply to hard-copy mail.

improving targetability and keeping the tangibility that makes hard-copy mail so successful.

Senders would benefit from enhanced targeting and improved information about customer preferences.

Tightening budgets make reducing costs for effective advertising list management and prospecting even more important today than in the past. With better-targeted lists and higher response and conversion-to-order rates, a static budget can yield more orders and a higher ROI. Recipients would benefit from advertising mail targeted more precisely to their interests as well as the existence of a market to compensate them for revealing their preferences.¹⁰ The Postal Service would benefit from a more robust, higher-value advertising mail product. This is the essence of a win-win-win solution.

Direct mail could be significantly enhanced by the creation of a digital information market tied to hard-copy mail.

The proposal from Van Alstyne, Parker, and Shanker is one potential solution to digitally enable direct mail and minimize information asymmetries, but there are others under development by private business, some in discussion with senior management at the Postal Service.¹¹ The Postal Service, with its

Closing the information feedback loop would yield great benefits.

reputation as the most trusted public agency and a centuries-long track record of guaranteeing privacy and prosecuting security breaches, is well positioned to be an honest, trusted mediator and custodian of customer preferences. It could determine the rules for participation in and enforcement of the system, with clear guidelines and robust privacy policies.

The Postal Service is also the most appropriate entity to investigate and conduct additional research in this area. Closing the information feedback loop to better understand and act on what mail recipients want to receive would yield great benefits, not only for the participants in the postal market, but also for the postal network and the products the Postal Service offers.

¹⁰ Further, the information feedback loop can give users more control over their ecommerce metadata and hence, better privacy protection.

¹¹ Industry stakeholder interviews, August 2013, and Postal Service executive and staff interviews, September 2013.

Appendix One Approach

The following paper, “A Redeemable Information Coupon Mechanism for Advertising Mail: One Strategy for a Postal Information Ecosystem” by Marshall Van Alosty, Geoff Parker, and Tushar Shanker presents one approach for building a digital information market for advertising mail.

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