

END THE GUARANTEE

ON-TIME DELIVERY GUARANTEES have existed for more than 30 years for express and 17 years for ground service, but the time has come for parcel carriers to put an end to them. Those on the front lines at shippers and even carriers would welcome such a move, with the only unhappy people being those who created a business based on recovering refunds for service failures.

Why should carriers eliminate the guarantee? When Federal Express introduced it in the early 1980s, it was in response to UPS's entry in the express overnight delivery segment. Although FedEx had quashed several competitors, it viewed UPS's entry as a more serious challenge because Big Brown had strong relationships with hundreds of thousands of shippers for a ground parcel service that FedEx didn't offer.

In 1982, FedEx was charging \$12.50 to transport an overnight letter just blocks from where it was picked up (compared with 20 cents for first-class postage) and generating huge margins to support such a guarantee. The guarantee also was a great marketing move to gain shipper confidence for FedEx's superior on-time performance achieved by a dedicated hub-and-spoke air network compared to UPS's dependence on passenger airlines.

For shippers, the guarantee was such a compelling value proposition that UPS and Airborne Express also had to offer it. But the carriers knew shippers had limited opportunity to seek refunds for service failure, because there was practically no visibility into deliveries that didn't arrive on time. As a result, carriers experienced minimal cost for refunds.

Then came the groundbreaking January 1997 article, "Transforming the Parcel Industry as the Speed of Business," in *Traffic World* magazine (which merged with *The Journal of Commerce* in 2008). That article helped prompt UPS to extend the delivery guarantee to ground

service in May 1998, and RPS followed two months later. At the time, the Internet was taking off, making the status of a parcel delivery readily available via carrier websites.

On-time service was about 95 percent for UPS and FedEx Ground. With ground service volume many times larger, it quickly became more appealing for shippers to seek refunds for service failures. This created an opportunity for businesses to offer a refund-recovery service on a gain-share basis, resulting in carriers paying even more for service failures.

Retailers allow consumers to return merchandise because the cost of processing those returns is built into the cost of product sold. Parcel carriers, however, failed to include the cost of offering the guarantee.

In addition to refunding a large amount for service failures that wasn't budgeted in the rates, the carriers face additional administrative cost of verifying and processing requests for refunds. The carriers have responded appropriately by allocating resources to improve on-time performance for ground service, which is now about 99 percent.

Another not-so-friendly approach the carriers have taken to reduce cost of service failures includes denial of refunds using hundreds of exceptions. The number of codes for excluding parcels from service failure refunds has tripled to 450 in 2015 from 150 in 2000. Some codes have been added, justifiably, for reasons beyond carrier control, such as weather and bad addresses.

With the simplified refund-filing process, and with costs of processing those requests increasing, the parcel carriers started to seek waivers in contracts from the guaranteed provision of the service. This approach appealed to shippers, who rightly took the easier path and waived the guarantee in exchange for slightly lower rates. As such, more than 70 percent of parcel volume now is exempt from the service failure refund.

The U.S. Postal Service, meanwhile, took a different approach: Although it guarantees its express service, it chose not to do so for its more popular Priority Mail and other parcel services.

With the successful "If it fits, it ships" marketing campaign targeted at small and medium-sized shippers, Priority Mail volume has grown from 2012 to 2014 at a compound annual growth rate of 7.2 percent, compared with 2.5 percent (UPS) and 5.9 percent (FedEx) for the guaranteed parcel services. This faster growth for Priority Mail is additional evidence that guaranteed delivery is no longer of much value to even smaller shippers if claiming the refund for service failures is as cumbersome as it is now.

The lack of interest in the guaranteed feature also is reflected in the recent enhancement of Priority Mail service, which changed the delivery expectation from two to three days to a day-specific promise of one, two or three days while not offering the money-back guarantee.

Shippers' lack of need for guarantee is further evidenced by their willingness to switch from the carriers' guaranteed ground service to non-guaranteed hybrid services such as FedEx SmartPost and UPS SurePost. This realization isn't lost on the world's largest parcel shippers. Amazon ships about 4 million parcels a day using multiple carriers, yet almost all of its deliveries are made without having a guaranteed delivery commitment.

The time has come for the parcel industry to eliminate its money-back guarantee for express, deferred and ground service, or just offer shipper-friendly automatic refunds for failures. **joc**

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