Postal Monopoly: Playing by Different Rules

BY ROBERT CARREIRA

Once again the U.S. Postal Service (USPS) is seeking to use its monopoly power to defy the economic law of demand. On April 8 the USPS requested an increase in the first-class letter rate from 37 to 39 cents, a 5.4 percent jump. Between 2000 and 2004, the price of first-class postage increased 12.1 percent, compared to an inflation rate of 9.7 percent. (The postal-rate history is online at www.prc.gov.)

But this is nothing new. From 1920 to 2004 the price of mailing a first-class letter grew at more than twice the rate of inflation. Inflation during this period, as measured by the consumer price index, was a mere 844 percent, while the price of a postage stamp increased 1,750 percent.

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In each decade since the 1920s, with the exception of the 1940s, postal-rate increases outpaced inflation. In the 1920s, when the price of a postage stamp remained unchanged, prices deflated by 16.5 percent. In the 1930s, which again saw price deflation—this time by 16.2 percent—the price of a first-class stamp increased by 50 percent. Only in the 1940s, when the price of stamps remained unchanged and inflation was at 72.1 percent, did the postal increase not exceed inflation. But this of course was after the 50 percent hike in the previous decade.

In the 1950s inflation was 22.8 percent, while the price of a postage stamp jumped 33.3 percent. In the 1960s inflation was 31.1 percent and the price of a stamp increased 50 percent. In the 1970s, with inflation at a whopping 112.4 percent, the postal service would not be outdone: the price rose 150 percent. Inflation was reeled in during the 1980s, ending the decade at only 58.6 percent. The postal service's response was a 66.7 percent increase in the price of a stamp. In the 1990s inflation was 31.8 percent, and the first-class postal hike was 32 percent.

Now we have the postal service asking for yet another 5.4 percent.

The postal service is seeking this latest increase to make up for lost business that has accompanied its rate hikes in recent years. Between 1998 and 2003 the price of mailing a first-class letter jumped 15.6 percent, well ahead of the 12.9 percent rate of inflation. Also during that time, the number of first-class, single-piece letters people entrusted to the postal service *dropped* from 54.3 billion to 46.6 billion—a decrease of 14.2 percent (www.usps.com/financials/rpw/welcome.htm).

The postal service's loss of business should come as little surprise. The law of demand tells us that, all else equal, as prices increase, quantity demanded decreases. Thus producers must lower their prices to increase sales and achieve market equilibrium—the point at which the quantities supplied and demanded are equal. At least that is what happens in a free market.

A business that tries to raise revenue simply by raising prices soon learns its lesson, since consumers will take their business to competitors or switch to alterna-

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tive products. In a free market a producer who refuses to accept this basic economic law is soon out of business.

But USPS bureaucrats believe they are exempt from the law of demand, just as they are exempt from competition in the delivery of first-class mail. They are indeed partially shielded from the law of demand, because government restricts the more cost-effective alternatives that would arise in an unfettered market. If the private sector had been allowed to compete in the delivery of first-class mail, the USPS losses of the past few years would have been even greater.

However, the postal service is not completely exempt from the law of demand. As the USPS has raised prices, the private sector has responded with several alternatives to first-class mail, including fax, e-mail, and electronic bill-paying.

About 65 million consumers in the United States have turned away from first-class mail in favor of paying at least some of their bills online (www.postinsight.pb.com/files/Levy_Cork.pdf). But as is often the case, the government monopoly remains a huge hurdle for those in the nation's lower-income brackets. While those who can afford fax machines, computers, and the Internet can escape, at least somewhat, the inefficiency of the postal monopoly, the poor remain trapped in this system of government incompetence and have little choice but to pay the higher prices commanded by postal planners.

Since the late 1800s, government has increasingly intervened in the economy in the name of antitrust. The ostensible justification for antitrust legislation is that monopolies may, among other things, increase their prices in the absence of competition and alternative products, leaving consumers powerless in inelastic markets. There is, however, a dearth of evidence of such occurrences in the free market.

In the case against Microsoft—a favorite target of government antitrust crusaders in recent years—Judge Thomas Penfield Jackson noted: "Microsoft enjoys so much power in the market . . . that if it wished to exercise this power solely in terms of price, it could charge a price for Windows substantially above that which could be charged in a competitive market. Moreover, it could do so for a significant period of time without losing an unacceptable amount of business to competitors."

When this decision was written, the price of Windows 98 was $169, compared to Windows 95, which a year earlier sold for $185. (See Stan J. Liebowitz, "A Defective Product: Consumer Groups' Study of Microsoft in Need of Recall," Competitive Enterprise Institute, February 9, 1999, www.cei.org/gencon/004%2C01559.cfm.) Thus the effect of Microsoft's private-sector "monopoly" was a price decrease of 8.6 percent in a single year for a vastly improved product. Likewise, Carnegie and Rockefeller, the so-called "robber barons" of the 1880s, with their "monopolies" of steel and oil that ushered in the era of antitrust laws, brought consumers lower prices that dropped steadily as their market shares increased. (See Benjamin Powers and Adam Summers, "Antitrust Is Anti-Consumer," *Economic Education Bulletin*, July 2002, http://home.san.rr.com/adamsummers/Antitrust.pdf.)

Government Monopolies Are Different

Why then do government officials insist they must protect consumers from successful businesses that persuade people to buy their products? Perhaps it is because of their own experience with the postal monopoly. The government's monopoly, when it fails to provide its services efficiently, simply raises its prices to compensate—just as it is seeking to do now. But what government officials do not seem to realize is that so-called monopolies in the private sector cannot operate in the same manner as government monopolies. In the free market, when a single seller raises its prices, it creates an incentive for increased competition. Government monopolies, on the other hand, play by different rules. The postal service can raise the price of first-class postage because the government has outlawed competition.

For a business in the free market to achieve and maintain a large market share, it must offer consumers the best possible product at the lowest possible price. Unfortunately, this is not so for the U.S. Postal Service, as its monopoly pricing over the past hundred years has shown.