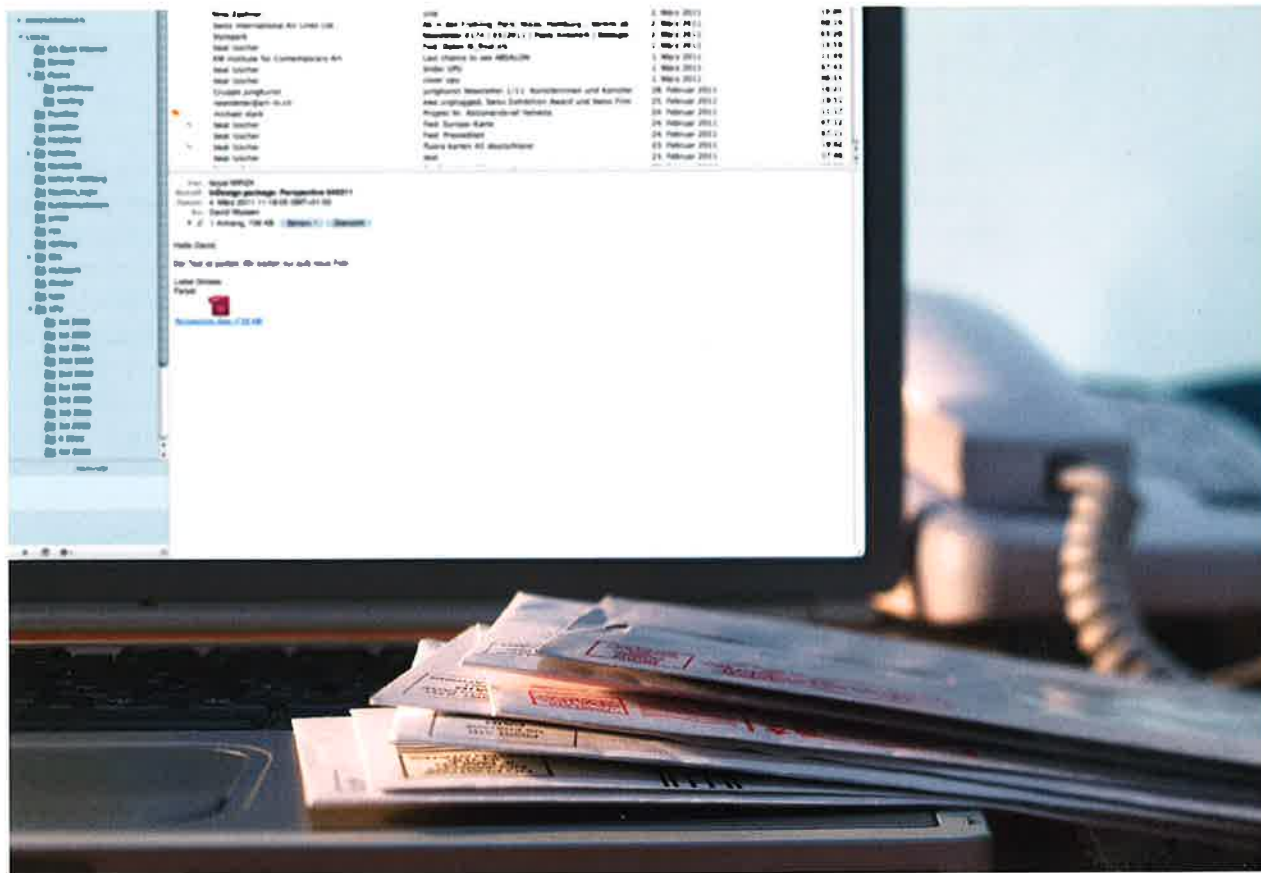


Electronic substitution: a shifting story

Nearly all Posts would agree that the email era has been a game-changer for the business. But what shapes and sizes does electronic substitution come in?

By
Tobe Freeman





When Heikki Nikali of Finland's Itella began studying electronic substitution of letter mail in the 1990s, conventional wisdom said that substitution would proceed as a single, steady wave of progress. Early on, Nikali revealed that things were more complicated than this simple prognosis implies. Fast forward to the UPU Mail and Express Economics Forum in November 2010 and a wealth of evidence that substitution proceeds in fits and starts, relies on a menagerie of different technologies and is driven by the distinct preferences of mail senders and receivers.

There is little doubt that electronic technologies pose a threat to letter mail. Nikali expects overall letter volumes in Finland to decline by 40 per cent in the coming decade and argues that this forecast could apply to many developed countries around the world. A veteran of nearly two decades of rigorous research on the topic, Nikali is focused on the practical task of providing guidance to Itella's business managers.

Impact size

A major challenge is to distinguish between the effects of electronic substitution and the impact of other factors on letter volumes, for example the general level of economic activity. Certainly, the business cycle has an impact on letter demand. Consider commercial mail users as an example. Many firms cut direct marketing budgets during recessions and direct mail makes up a sizable share of the letters sent to private individuals.

Yet, according to Frank Rodriguez of OXERA, an economics consultancy, forecasts that rely too heavily on economic data have become progressively less reliable. Analysing data from Royal Mail, Rodriguez finds that letter volumes and economic activity up until 2002 were highly correlated. However, between 2002 and 2007, letter volumes at the British postal operator declined during a period when the overall economy

performed strongly. Observations such as this have prompted some to ask whether the relationship between macroeconomic factors and total letter volumes has broken down completely.

Rodriguez claims that the technologies replacing letters can disrupt this relationship in unpredictable ways, making forecasting difficult. To confront this challenge, he analyses, separately, individual volumes of first and second class mail and different types of mail content. This breakdown of the data enables better forecasting of electronic substitution for invoices and other transactional business mail. And it has yielded a better understanding of the shift from direct mail to online marketing.

Closer interaction

Substitution of letter mail by online marketing is the special interest of Jonathan Margulies of Winterberry Group, a marketing consultancy. Margulies estimates that United States' spending on direct mail declined almost 17 per cent in 2009. This slide came despite perceptions among marketing executives that direct mail is more effective than online display advertising, television and radio placements.

According to Margulies, marketers are drawn to electronic channels by the promise of closer interaction with their target audience. He predicts rising investment in social media and mobile marketing applications, where coupons and other marketing messages can be delivered to smart-phone users when they arrive at particular locations or perform specific online-search queries.

Direct mail is not entirely on the losing end of these developments. The evolution of online marketing has brought vast improvements to marketing metrics and the strategies used to target customers. Margulies believes that these improvements feed back to the



Try sending this by email. A direct-marketing campaign for a small car by Tequila, Australia, went to innovative lengths to catch consumer attention.

practice of direct marketing and may ultimately strengthen the business case for direct mail.

Not what it seems

The idea that new technologies simply replace letters is deceptive, according to Nikali, and measuring substitution in terms of a direct decline in letter volumes can be misleading. In the 1990s, letters accounted for 60 per cent of all messages in Finland written to a specific individual. Now this figure is estimated at 10 per cent. Thus, the contribution of letters to the total volume of targeted communication has plunged, even if demand has not declined so dramatically. "That is one of the reasons why substitution is difficult to understand and even more difficult to measure," Nikali explains.

To pin down how letter demand will evolve, Nikali identifies specific market-conditions that have the effect of speeding up or slowing down electronic substitution. Substitution in Finland has not progressed evenly across the various sender and receiver segments. The pervasive spread of email has contributed to steady substitution in the communication between private individuals. And business-to-business transactional mail has also been digitised to a substantial degree.

Getting started

Yet, according to Nikali, substitution of mail sent from businesses to consumers (B2C) has barely begun. He supports this prediction with evidence that consumers and businesses have very different preferences when

they communicate with each other. Businesses are highly sensitive to price, readily substituting one service for another if substitution leads to a reduction in cost. Consumers, on the other hand, are motivated by factors beyond price. In particular, consumers place special value on the practicality of the service, its ease of use, trustworthiness and reliability.

If these preferences have slowed electronic substitution in the B2C segment, Nikali predicts that the situation will not remain static. Eventually, consumers are likely to embrace electronic transactions with businesses, leading to a future wave of substitution within this segment.

Amid the hype about electronic communications, managing letter services today might seem like arranging deck chairs aboard the Titanic. But reliable forecasting is essential for the normal operation of Posts, and letters remain socially and economically important even as communications have become increasingly digital. More importantly, research into electronic substitution offers an insight into the future of targeted communication.

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