Trends in Direct Mail

White Paper

Direct Mail Service Providers Must Provide Flexibility to Succeed in a Growing Market

By any measure, the direct mail industry is thriving. Direct mail marketing is expected to grow by 7.5 percent in 2007, according to a new forecast report issued by Universal McCann, one of the largest advertising agencies in the world. Direct mail now accounts for more than one out of every five dollars spent by U.S. advertisers.

With the single exception of Internet marketing, which is predicted to grow by 15%, all other media – including television, radio, magazines, newspapers and yellow pages – will be outperformed in terms of growth by direct mail in 2007, predicted Robert J. Coen, Senior Vice President and Director of Forecasting at Universal McCann, New York.

"The only major traditional medium showing strong growth has been direct mail, which is probably the only medium to clearly provide short-term accountability measures," said Mr. Coen who adds that he fully expects that the trend will continue despite higher postal rates and higher paper, printing, and handling costs.

The reason for this growth is fairly simple: according to USPS® statistics, consumers read 78 percent of the advertising mail they receive, nearly 10 percent respond to offers, and 21 percent bring coupons and ad mail with them when they shop. Statistics further show that mail delivers a strong return on investment. "In recent years, marketers have exerted extreme pressure on all parts of their marketing budgets, and they have intensified their efforts to try to get some accountability or ROI evidence for all outlays," according to Mr. Coen. In other words, direct mail is growing because advertisers get a quantifiably strong return for each dollar they spend.

Yet even as expenditures on direct mail marketing will surpass $64 billion this year, mail service providers in the direct mail industry continue to experience price pressure from their constituent advertising agencies and marketers. Acquisitions – some of them quite large – are a continuing trend in the industry. Profit margins are reportedly lower now than a decade ago and while a great deal of money is being made by service providers, few would describe current conditions as very favorable.

This report, commissioned by Pitney Bowes Document Messaging Technologies, strives to evaluate the current condition of the direct mail market and make recommendations for mail service providers specializing in this mail segment. The method employed in this paper includes outreach to a dozen top direct mail service providers in addition to close readings of existing industry research. Direct in-depth interviews with leading mail service providers formed the basis for many of the findings. Most important, a consensus on the key issues facing direct mail service providers was reached without prompting, which speaks to the ubiquity of these issues across the industry.

Direct Mail Trends and Issues

Every direct mail executive interviewed concurred that the compensation mail service providers currently receive from their clients is close to or perhaps a percentage below what they were receiving for their services a decade ago, despite the sizable increase in direct mail volume over the past five years. This prompts the question: why have service prices flattened out at a time when the marketers and advertising agencies have increased the mix of direct mail in their budgets?

It was also agreed across the board that in order to share in the growth of the industry, mail service providers were under pressure to add technology and competencies beyond traditional mail processing operations. This is one driver for the continuing trend toward mergers and acquisitions: large mailers have a strategic interest in gaining the expertise of smaller, niche players. At the same time, there's also a growing trend toward providing solutions for specific vertical markets and for achieving geographical reach to efficiently serve markets across the United States and Canada.

It is equally clear that for these executives mail is a high volume business. Although even the largest shops have all the work they can handle and are very rarely idle, job preparation is increasingly time-consuming and costly. Economies of scale must be leveraged in order to amortize pre-production expenses and compensate for set-up periods that are not directly bringing in revenue. Jobs are also increasingly complex to process as marketers strive for new ways to gain the attention of consumers. Where once a few inserter systems were adequate, mailers find themselves more and more involved with foils, plastic packaging, wraps and three dimensional mailings. Because of this, there is more pressure to increase the utilization of every asset, as each piece of equipment purchased to handle a particular segment of a job must be leveraged to gain the most from the investment.

Personalization and Target Marketing

The trend toward fewer, more highly targeted direct mail pieces makes it difficult to take advantage of economies of scale. For example, a mass market campaign that used to involve millions of pieces of mail might be broken into smaller, more finely tuned segments. In addition, as the direct mail market shifts from a mass market high to a more fine-tuned, targeted and lower volume market, advertisers are pressuring mailers to fit as much material into a single envelope as possible. A trend toward more personalization means that specific name and address information must be included on mail pieces, with some companies leveraging customer relationship management tools to increase their ability to cater to the specific needs and preferences of their most highly coveted targets.

In addition, the trend toward targeting means that mail service providers are forced to accept a shrinking volume of mail to process, which further lowers fees that mail service providers can expect.

The trend toward what is currently called transpromo mail – a crucial element of customer communication management – adds complexity to mail pieces and is leading to more emphasis on using bill and statement mail to gain more wallet share of existing customers, which takes funds away from traditional direct mail as a tactic for new customer acquisition.

Finally, virtually every mailer interviewed commented that the new breed of marketers they work with are better educated in terms of the types of mail processing equipment on the market, as many attend print and mail trade shows and gain knowledge of the latest improvements in equipment. As the marketers ply their newly minted knowledge, mailers are forced to provide an ever widening equipment list for them to review as they plan their next campaigns. This, too, leads to more mergers, as equipment lists and floor space are continually refined and expanded.

As competition and other factors drive down profit margins, service providers will be compelled to offset the decrease in volume, diversify their technology mix and gain the abilities and technologies through mergers and acquisitions.

Postage Pressure

Even as business mailers were still absorbing the 5.4 percent rate increase in 2006, the USPS® filed for a rate increase with the Postal Rate Commission (PRC) to take effect in June or July 2007. For business mailers, the proposal means increases in postage from 7-18 percent, based on averages for various mail classes: a First-Class stamp would climb to 42 cents, Standard Mail rates would raise about 8-9 percent, depending on size and shape. What effect will the next postage rate have on the direct mail market?

If history is any guide, marketers will not slow down the rate of mailing but will instead try to compensate for the expense more creatively. Unfortunately for mail service providers, this includes downgrading the amount they are willing to pay in service fees. According to one mail service provider, if a marketer loses a penny to postage, they will take it from another part of their operation to remain even.

Looking at the last rate hike, it is very apparent that the postage increase did not slow the growth of direct mail, because statistics show that the volume of direct mail rose. Instead, direct marketers tried to leverage each envelope for more content. They looked for ways to insert more material into a single envelope. This too placed a heavy burden on service providers and stretched the limits of their inserter systems.

The next postal rate increase could be another story. If the next increase causes direct marketers to create fewer, more highly targeted mailings it could in turn force the USPS® to offset reduced volume with even higher postal rates: "a vicious cycle" in the words of one mailer; a "death spiral" in the opinion of another.

Caught in the middle of this whirlpool will be the mail service providers.

The best recourse a mailer has is to better understand how to obtain postal discounts and pass that savings on to the customer. Another tactic is to learn how to add value to the mail piece by using targeted messaging on the envelope and other eye-catching gimmicks to increase the read rate of the mail.

Fortunately, technology exists for the various mailing efficiency products and worksharing programs offered by the USPS®. And more granular targeting helps offset postage by providing better response rates. Unfortunately, the technology for more granular targeting and mailing efficiency software has its own cost and therefore further decreases their margins. This will be a growing trend: as the direct mail process becomes more complex and technology-driven, the elements that come into play to create a direct mail campaign compete for those funds. In other words, the dish of pennies may be larger, but there will be more hands reaching into it.

Direct Marketers and Technology

Direct marketers are becoming smarter about mail. Once content to sit in their offices and get creative, they now attend the MFSA and CDMA shows and have a better understanding of what technology is available to process mail more efficiently. No longer satisfied with just taking responsibility for the creative, direct marketers are driving a hard bargain by becoming experts on processing equipment.

This trend has added pressure on mailers, who are compelled to find new ways to add value to their services. Mail service providers traditionally want to sell the service before obtaining the technology. Very often, this translates to a significant investment in new technology and a reliance on mail equipment vendors to quickly provide them with systems that offer greater flexibility in terms of the kind of jobs they can do.

A quick scan of service providers listed on the MFSA web site shows that the lists of equipment they have available – an indicator of the variety of jobs they can process – have increasingly moved to more prominent locations on their sites: in many cases, even onto the home page.

In other words, as marketers have gotten more educated about the variety of jobs mail service providers can process, mailers have been compelled to invest more in technology and more prominently advertise that aspect of their business. Mail systems providers consequently have had to provide new technology that adds significant value to mail operations as direct mail continues to grow.

Hot Technologies

So what are the new hot technologies and how are they being used?

Inside/outside matching is a consensus favorite, as integrity has become an issue for direct marketers who try to craft messages for specific customers. The integrity issue for direct mailers isn't as important as it is for transactional mailers, especially those in the health insurance and financial services verticals, but it is becoming a factor.

Getting the envelope to look like a piece of personal mail is another. There's a lot more emphasis on the look. Stamps are beginning to be used more often than permits and metering. Messaging on the outside of the envelope that catches the eye and is personal is growing. Teasers are popular.

Highly capable equipment is another. Floor space is at a premium and operator costs are a heavy burden on margins, so mailers must attempt to replace these factors with technology. One prominent mail service provider claimed outright that he was betting the future of his company on Pitney Bowes DMT, specifically on the FlowMaster® inserting series high-speed inserter. "We're going from three FlowMasters to 17 of them in a seven-year span. The reason is the ability of the FlowMaster to process numerous types of jobs with very little time spent on changeovers, which competitor inserter systems could not match."

"We have 5,000 piece jobs and we have two million piece jobs and we need to be able to do both. You have to gain the flexibility to do the jobs as they arrive in queue with as little downtime as possible. The question becomes how many jobs can be done in the least amount of time using the least amount of square footage possible."

The more variety a mail service provider can squeeze out of a single piece of equipment, the smaller the footprint. "If you can do away with a staging area and the personnel needed to produce the mail, you can reduce your overhead and process mail at a higher margin."

In another mailer's opinion, increasing the amount of automation from the data stream to induction in the mail stream was the only way to reduce the price pressure on his operation. This mailer understood that the key to success is to streamline operations: by reducing the number of separate steps and human touches in the process, one can raise one's profit margins. From end to end the process must be automated.

Conclusion

Direct mail is the healthiest sector in the mailing industry, showing continued growth as it generates respectable results at an efficient cost. Yet mail service providers see increasing threats to their direct mail business. Some mail service providers are trying to add size and capacity to ensure their viability. More strategic service providers acknowledge a need to be able to provide a variety of services, for example, to the transactional mail market, in addition to the traditional direct mail market. Adding technology that extends the flexibility of the mail operation is clearly an important investment. In the meantime, mail service providers grapple with shorter jobs, the demand for faster turnarounds, 1:1 variable data messaging and digital color and the continued need to add technology and more value-added services.

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