

To FedEx Team Members

This month marks the 75th anniversary of the disappearance of Amelia Earhart. You may have seen news stories about how we donated shipping for the high-tech tools being used by the team trying to find out what happened to her on the last leg of her pioneering around-the-world flight. Cutting-edge technology may yet answer one of the most-discussed mysteries in aviation history.

Though Amelia Earhart did not complete her flight, her legend as an iconic aviator has continued to grow. She, like many great explorers, moved outside her comfort zone, accepting new challenges and taking calculated risks. She is justly celebrated for that.

Over the years, a lot of people have talked about FedEx as a company that takes on new challenges and carefully calculated risks. Not at the expense of safety, of course, but often at the expense of our own comfort level. As both history and current headlines tell us, complacent companies lose their edge.

That constant adjustment and anticipation, backed by the dedicated efforts of you, our team members, in your daily delivery of the Purple Promise is why FedEx is a stronger company today. It's also why we had a solid performance in FY12, despite economic headwinds. Thank you for stepping up!

Yet changes occur constantly, and we must anticipate and respond quickly to them. The success of our company depends on it.

In my January letter, I shared some troubling market trends, including Europe's debt difficulties and slower growth in China. These concerns have become reality. Add the wild cards of high, fluctuating oil prices and slower U.S. trade growth, and you can see that customers everywhere face a tough and uncertain environment.

One business decision many of our customers have made is to trade speed for savings. Though that decision may be partly driven by the current economy, it's a mistake to think that it's temporary. We have seen a steady shift from priority services to deferred or from express services to ground, especially in the United States. This trend is likely to continue as many customers are recalibrating their supply chain decisions. The good news for FedEx is that we have a full menu of services to offer and can keep this volume in our "family."

This mode shift isn't new. We saw it starting to unfold years ago, and we made smart investments to adapt and take advantage of it. For instance, we've long focused FedEx Express on the global market and have continually invested in our international express network. Many of the high-tech, high-value-added products that 10 years ago we might have moved in the domestic express market are now moving internationally from a foreign origin point to a domestic location or between emerging markets. Our strategy has been to substantially increase our Express international revenues, with the U.S. being just one (albeit a very important one) node on that vast international network.

Another good example is FedEx Ground. Over the past eight years, we have combined cutting-edge technologies and a passion for efficiency to reduce transit times by at least one full day in 69 percent of its continental U.S. transit lanes. FedEx Ground is now faster to more locations than any other ground carrier. And its service levels are at an all-time high. With that kind of dedication to efficiency, it's no wonder FedEx Ground has taken market share for 49 straight quarters!

We also see ocean freight starting to become more competitive with international air freight for selected shipments. That's why FedEx Trade Networks is growing, and we are continuing to increase our investments in this business. As technologies develop to keep perishable shipments fresh for weeks instead of days, this trend could accelerate. But, as in the case of Ground, we are prepared for it.

This is precisely why we began expanding the FedEx portfolio beyond our traditional express/air cargo services. Customers will always make decisions based on the factors most important to them at that moment. By offering best-in-class choices across the board, we keep their business "in-house." The alternative, of course, is losing it to competitors.

These mode shifts illuminate a big difference in this recovery from previous ones. In the past, a big recession produced a big recovery. But the bounce-back isn't so resilient this time. The U.S. economy is growing, but not at the pace we hoped for.

In response, we must maintain a laser focus on reducing our costs, working smarter for more efficiency, and sustaining our historical commitment to innovation.

From the Chairman

JULY 2012

Lowering costs while improving efficiency

Simply put, our cost structure is too high in certain parts of the corporation. The changes we see in customer preferences and expectations will not disappear even when the economy turns upward. So we must adjust the way we do business. We're investing in efficiency to save us many millions of dollars for many years to come while strengthening our competitive position. At FedEx Express, we'll permanently retire 50 inefficient aircraft this year, which will be replaced by new aircraft that are less costly to operate, with significantly reduced fuel consumption and emissions, better reliability and less maintenance expense. Express is also accelerating its purchases of more efficient, cleaner trucks, including all-electric and hybrid-electric vehicles and thousands more new-generation diesel trucks as well.

FedEx Ground and FedEx Freight are opening new terminals to further improve our network advantages. Freight is implementing routing and scheduling changes to save customers time and move their traffic more efficiently. FedEx Office is refreshing, rightsizing, and relocating stores as well as aggressively negotiating savings on leases, equipment and supplies. In all these investments, greater efficiency is a key goal.

Quality Driven Management (QDM) is one of the most powerful weapons in our search for efficiency. Remember: Better quality equals lower costs. FedEx Ground, for instance, used QDM to save \$72 million in claims costs over the past four years. FedEx Express reduced its U.S. domestic Wrong Day Lates by about 14 percent. FedEx Freight teams in three cities collaborated to reduce one customer's high exception rate by 80 percent, almost twice their goal. FedEx Office is automating its inventory management process and improving tools, training and packaging to reduce damage claims.

I'm proud of the 600 Quality Action Teams (QATs) at work throughout the company. Their smart actions will pay off even more in FY13.

Innovating to stand out

We've all had those "wow" moments, when we saw a new product or service that went beyond what we thought was possible. We've created more than our share of those at FedEx over the years. But yesterday's innovation is today's commodity. Tell a teenager what a miracle it is they can order something like an iPad, engraved with their name, and receive it in a few days all the way from China, and you'll likely get a blank stare. It might be a miracle to my generation; it's a "so what" to my grandkids.

Innovation is an endless process. Without it, you're nothing special. That's why we need to do more of it.

Our IT organization is focusing hard right now on a "clean sheet" approach to harnessing the latest technologies to make it as easy as possible for customers to use all our services. In today's world, where customer loyalty can be a fleeting thing, the stakes here are high. Converting just one percent of disloyal customers to loyal can add \$100 million to our annual revenue.

IT is also creating a much more efficient and engaging platform for team members to collaborate and share information effectively, based on some principles of social media. In today's world, we simply cannot allow the continuation of "silos" where individuals or small groups don't share their expertise. Rolling out later this year is our enhanced intranet, called Purple Hub, which will make it easier to share across opcos and regions and leverage our entire team's strengths.

Culture as a competitive differential

As important as technology is to innovation and differentiation, it's you, our team members, who truly set us apart. Your spirit and teamwork—the culture of FedEx—cannot be duplicated by competitors. And our unique culture is more important than ever in the face of this challenging marketplace. "Half the difference in operating profit between organizations can be attributed to effective cultures," says Professor Emeritus James Heskett of the Harvard Business School.

In the coming months, we will talk extensively about our culture and its components—our brand and company beliefs, People-Service-Profit, the Purple Promise, and our corporate mission. I urge all of you, whether you joined FedEx 30 years ago or three days ago, to determine how these values play out in the jobs you do every day, from loading planes to driving trucks, from calling on customers to managing work groups.

One example of how we're strengthening our culture can be seen in the stories that specially trained P-S-P facilitators in FedEx Services are sharing. (See video at fromthechairman.com.) I am proud to have such eloquent and committed people on the FedEx team.

Winning strategies for FY13 and beyond

Beyond our drive for efficiency, cost control and innovation, broad business strategies are particularly important in helping us meet our goals. One is our plan for growth in the Europe/Middle East/India subcontinent/Africa (EMEIA) region and another is our small- and medium-size customer strategy.

From the Chairman

JULY 2012

Just a few highlights from the past fiscal year from EMEA:

- FedEx Express has opened 38 stations, and FedEx Trade Networks has opened seven offices in EMEA, giving them a total of 30 in that region.
- We're always looking for strategic acquisitions and recently added companies in France and Poland. (We also have acquired a fine Brazilian company for our Latin America and Caribbean division.)
- In addition, as customers often opt for more economical, slower service in a low-growth market, we're seeing gains in FedEx Express international economy services in Europe and around the world.

We are confident our strategies will boost our competitive position in Europe over the long term.

Small business, big opportunities

There are about 125 million micro, small and medium enterprises worldwide. In most places, they are a primary growth engine for the economy. And we are doing more to make them a growth engine for FedEx as well.

In recent research, small business people rated "designed for my needs" as the most important factor when buying something for their business. Second on the list was "high value." "Leading brand" was dead last.

We're intensifying our efforts to delight small business people with new programs and features. We know that time is the most precious commodity to them. So we're focusing on saving them time in their dealings with us, from streamlining online billing

to handling international documents. We're also building loyalty with a program called My FedEx Rewards, which awards points for eligible FedEx Express and FedEx Ground shipments. It's been very successful in retaining and driving revenue, and no competitor has anything like it.

Fear of change can be fatal in a business like ours. If the world stood still, it wouldn't need FedEx. That's why we are constantly looking over the horizon to anticipate where the world is headed—so we can help it move in productive directions.

One recent change is U.S. healthcare. The U.S. Supreme Court recently upheld the Patient Protection and Affordable Care Act (PPACA), signed into law by President Obama in 2010. This decision has significant impact on the cost of providing health benefits by employers of every size, including FedEx. We are carefully evaluating the effects of the law on our U.S. healthcare plans and our strategy to address the requirements of the PPACA. It's very likely we'll have to make changes in our plans over the next few years because of the new law. Of course, you will be informed well in advance of any changes and what they mean to you and your family.

We know we have to become more efficient and stay ahead of changes in our marketplace, just as we know we have to adjust our networks to new customer needs. To do this, we must continually improve our ability to share and leverage the knowledge and experience of our team members everywhere. We can, and must, find new ways to work more efficiently and delight our customers by delivering the Purple Promise under all circumstances. In this way, we will keep FedEx on a successful course however the winds of change may blow.



Frederick W. Smith
Chairman and CEO