

MAIN DEVELOPMENTS IN THE POSTAL SECTOR 2013-2016

Presentation at SDC plenary meeting

Study for the European Commission
Brussels
December 2018



Our background

| | |
|--|--|
| Copenhagen Economics  | <ul style="list-style-type: none">• Offices in Brussels, Copenhagen, Helsinki and Stockholm• 85+ economists |
| Postal sector experience  | <ul style="list-style-type: none">• User needs and future USO• Calculation of USO net costs• E-commerce and parcel delivery• Terminal dues• Tariff regulation• Cost allocation and pricing• Access regulation• Antitrust and regulatory cases |
| Studies for the European Commission  | <ul style="list-style-type: none">• Main developments in the Postal Sector 2008-2010 & 2013-2016• Pricing behaviour of postal operators (2011)• E-commerce and Delivery (2012)• Other studies |
| Other services in Copenhagen Economics  | <ul style="list-style-type: none">• Competition• Digital economy• Dispute support• Energy & Climate• Finance & Tax• Healthcare• IP valuation and transfer pricing• Tender & Auction support• Trade & Internal market• Transport |

Thanks to the project team



Henrik Ballebye Okholm



Bruno Basalisco



Anna Möller Boivie



Marjolein Geus
(partner, Bird & Bird)



Martina Facino



Mindaugas Cerpickis



Jimmy Gårdebrink



+ analysts and research
assistants that supported
the project team

This has been a long journey...

130+

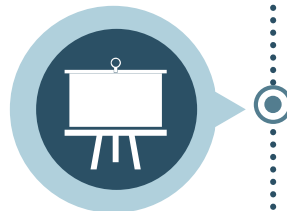
Literature references

10 Public workshops

- European Commission events
- ERGP events
- PostEurop events
- SDC and PDC meetings

40 Case studies

USP practices, NRA decisions,
Ministries policies, Court decisions..



81 Questionnaires

=

41,800 Data points

from NRAs, USPs and Trade unions

20+ Interviews

NRAs, USPs, competitors, SDC,
ministries, consumer associations,
e-commerce associations, and
trade union associations

We are thankful for all the input

1.300+
Emails in our Inbox



500+
**Comments to draft versions
of the Study from the
Commission...**



330+
**Participants in 3 public
workshops**



1 Important market developments

2 The competitive landscape in the postal sector

3 Employment and environmental developments

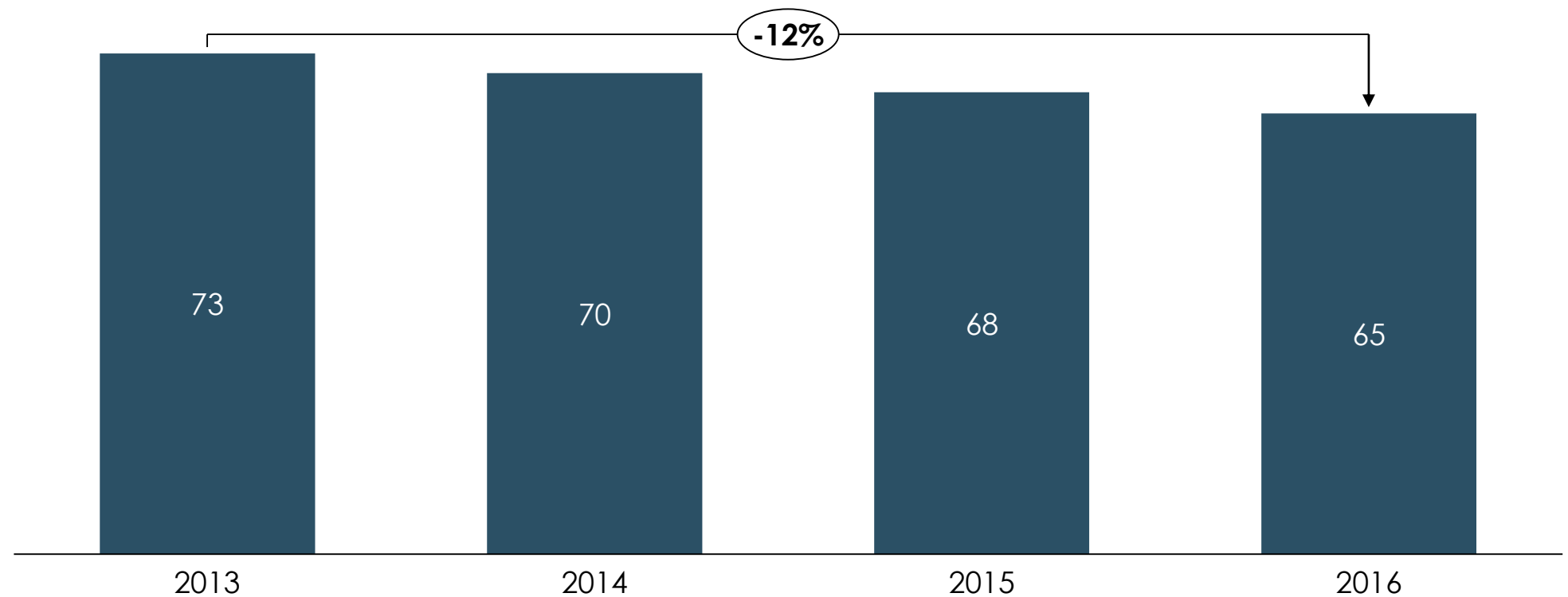
4 Developments in universal service

5 Scenarios for the future provision of the USO

Total number of addressed letter post items dropped by 12% in three years

Letter post volume decline, domestic, 2013-2016

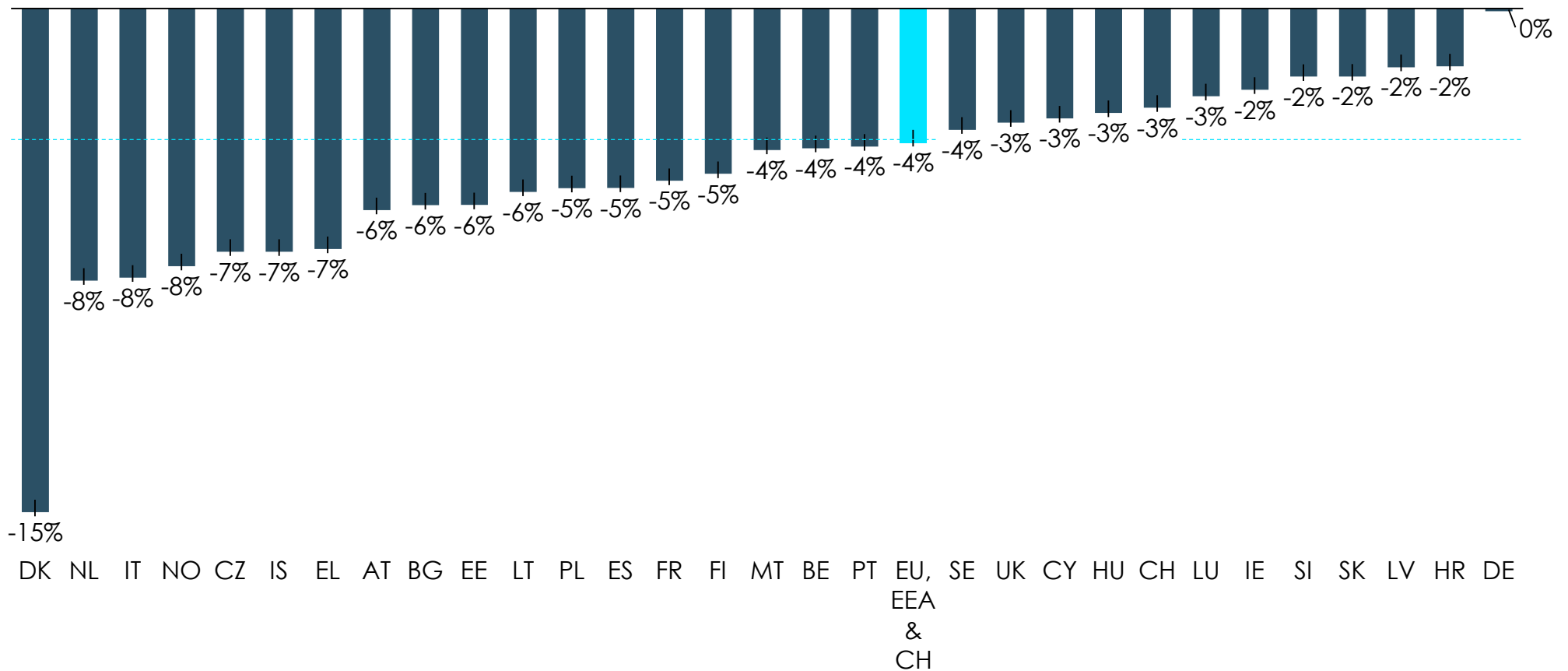
Billion items



Addressed letter demand declined by four per cent annually in 2013-2016

Development of domestic letter post volume by country, 2013-2016

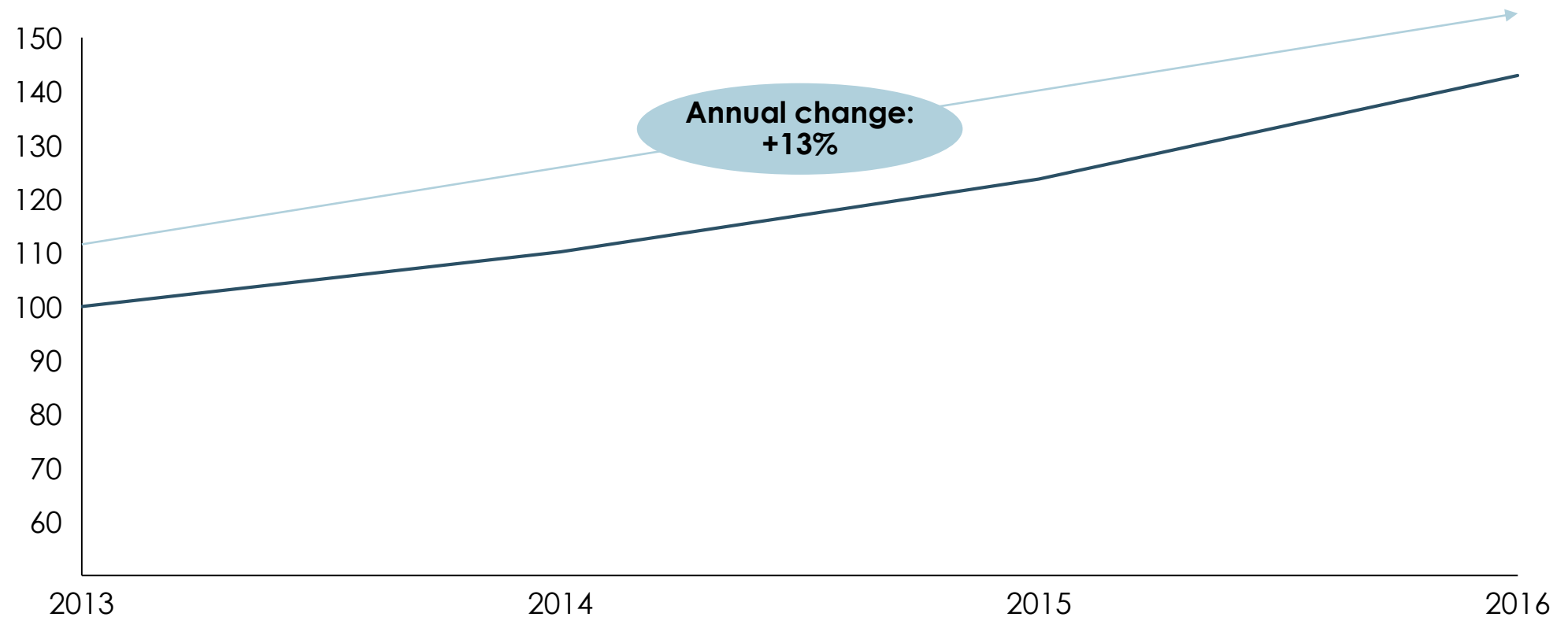
Annual change



In contrast to letters, parcel and express volumes grew by 13 per cent annually

Evolution of domestic parcel & express services volumes

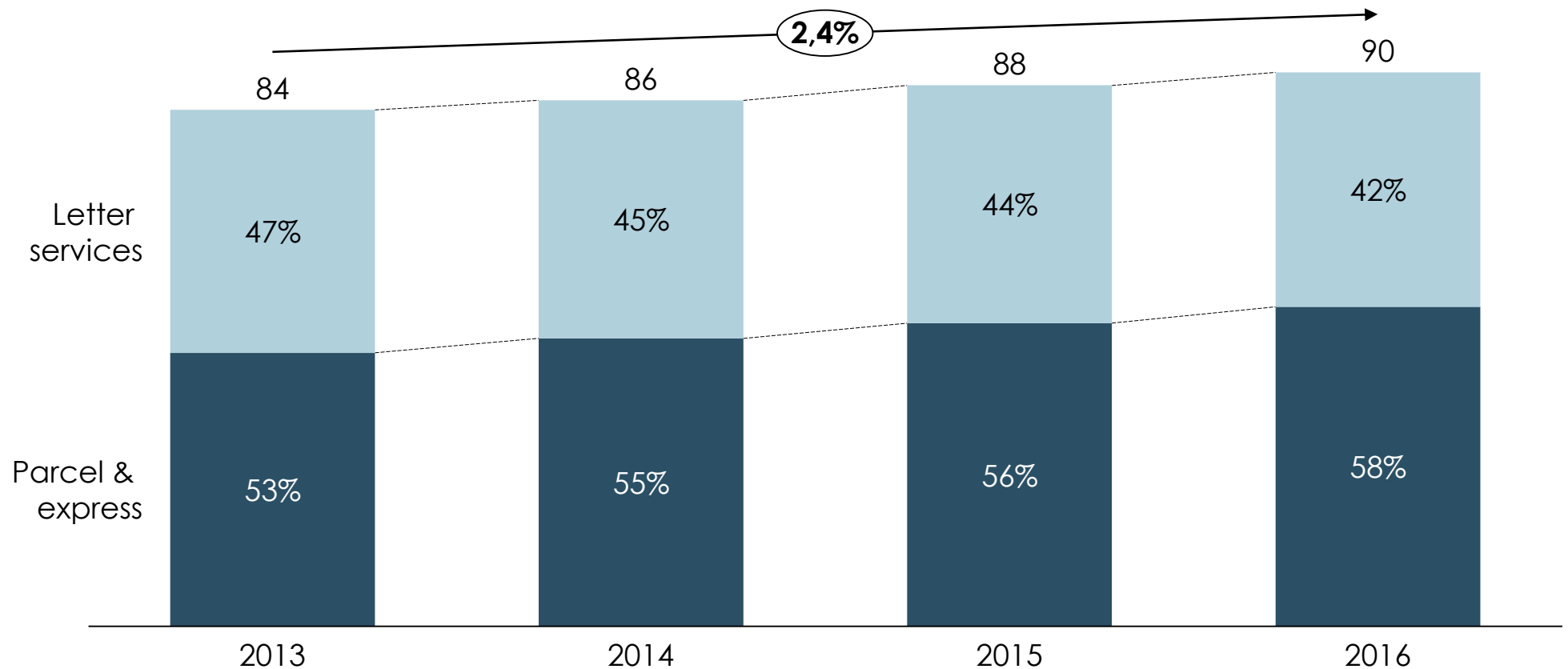
Index (2013=100)



Postal and delivery market in the EU, EEA & CH area produced €90 billions in 2016

Development of revenue in letter post and parcel & express segments

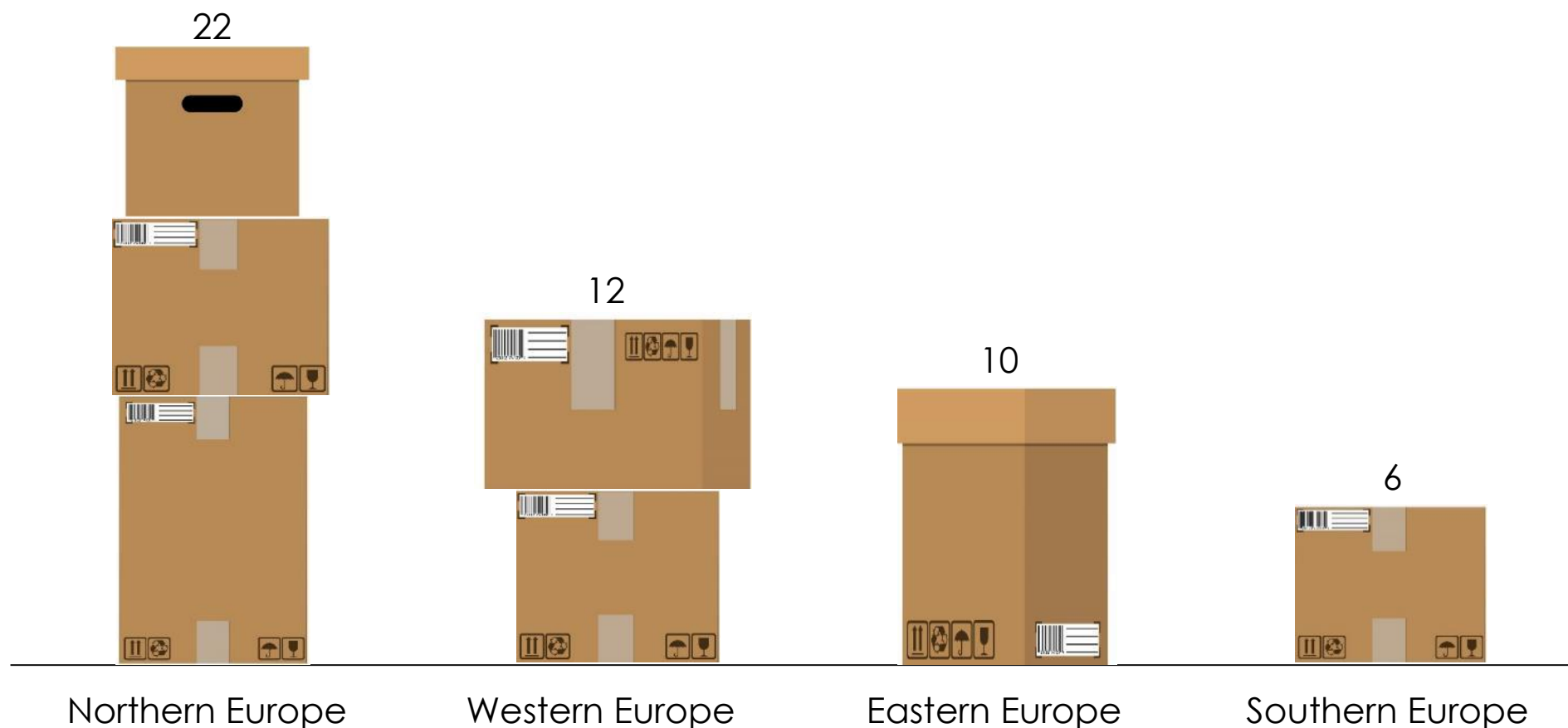
Billions Euro



Demand for parcel and express services varies up to four times regionally

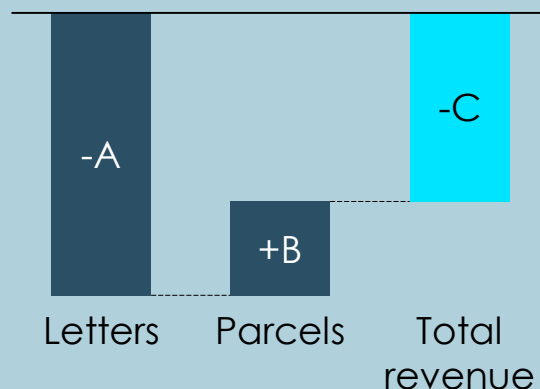
Domestic parcel & express items per capita, 2016

Items per capita per year



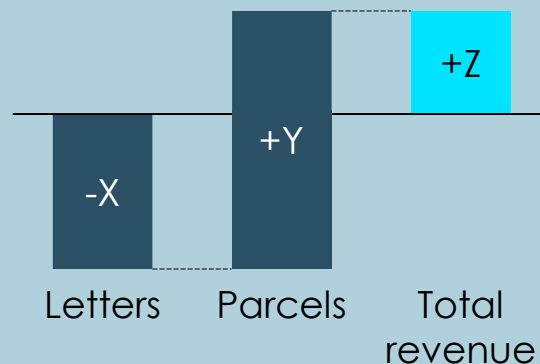
The growth in parcel & express segment does not outweigh letter revenue decline for most of USPs

14 USPs



Parcel revenue growth **did not outweigh** letter revenue decline

7 USPs

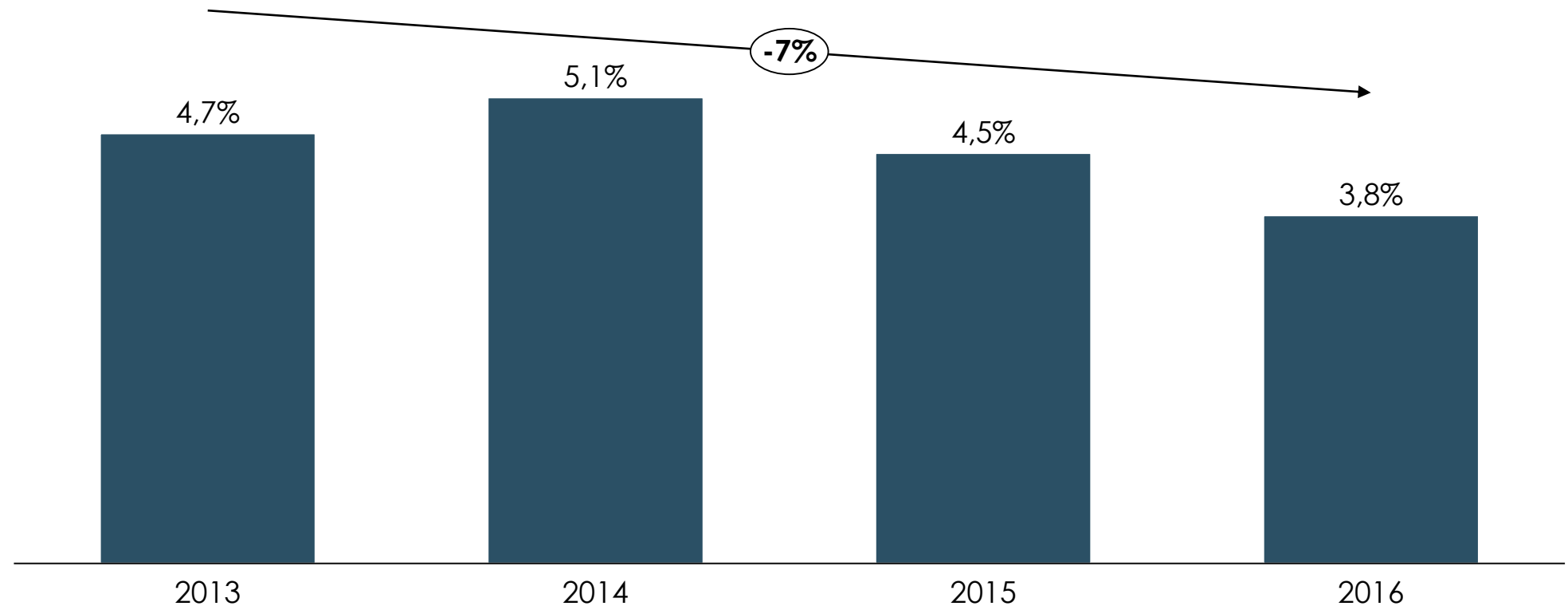


Parcel revenue growth **has outweighed** letter revenue decline

USPs' profitability has been declining, going from around 5 to 4 per cent

Development of USPs' profitability in the EU, EEA & CH area

Average EBIT %





Main challenges for postal operators

Declining demand for letter mail creates pressure to increase prices

Price changes for 20g FSC domestic letter product, 2013-2016

Price index (2013 = 1)

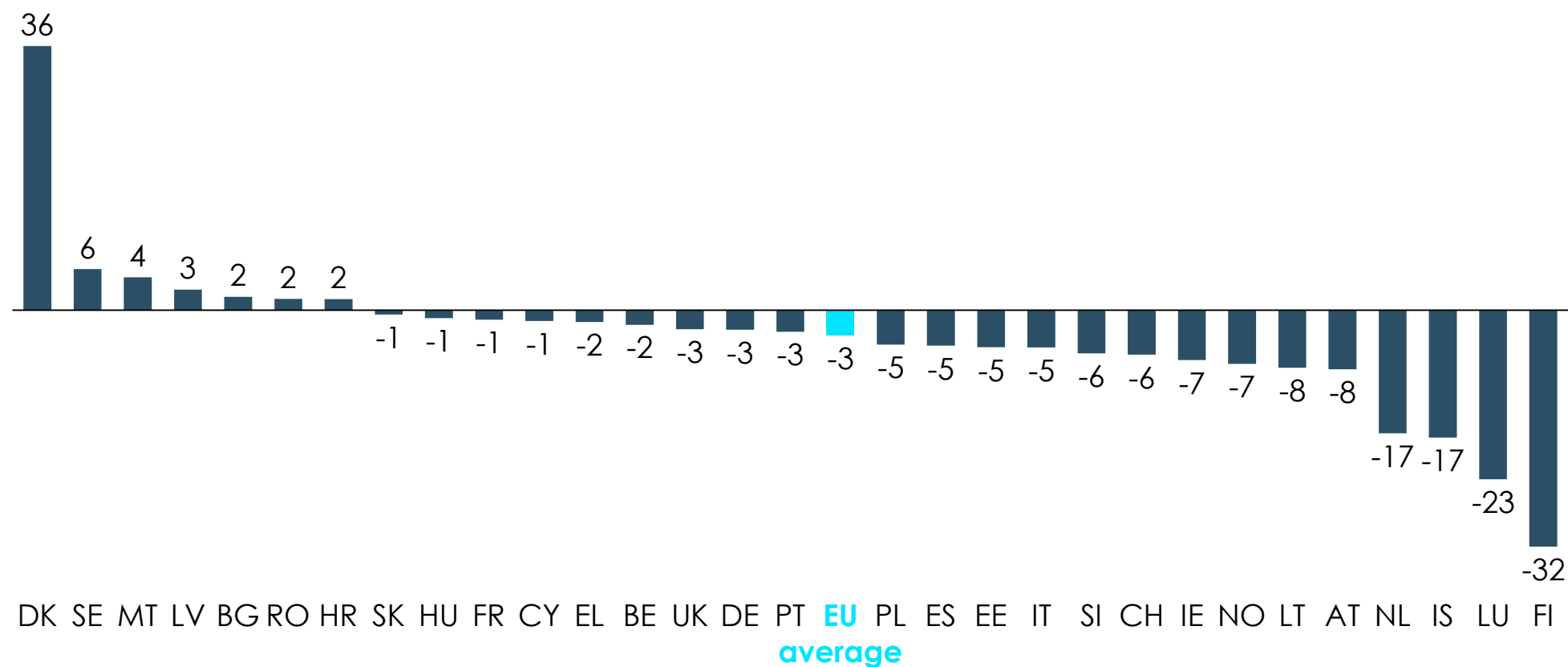


* Includes express service features, e.g. track-and-trace

... pressure to reduce fixed costs by, for example, closing down post offices

Development of post office and post-in-shop network, 2013-2016

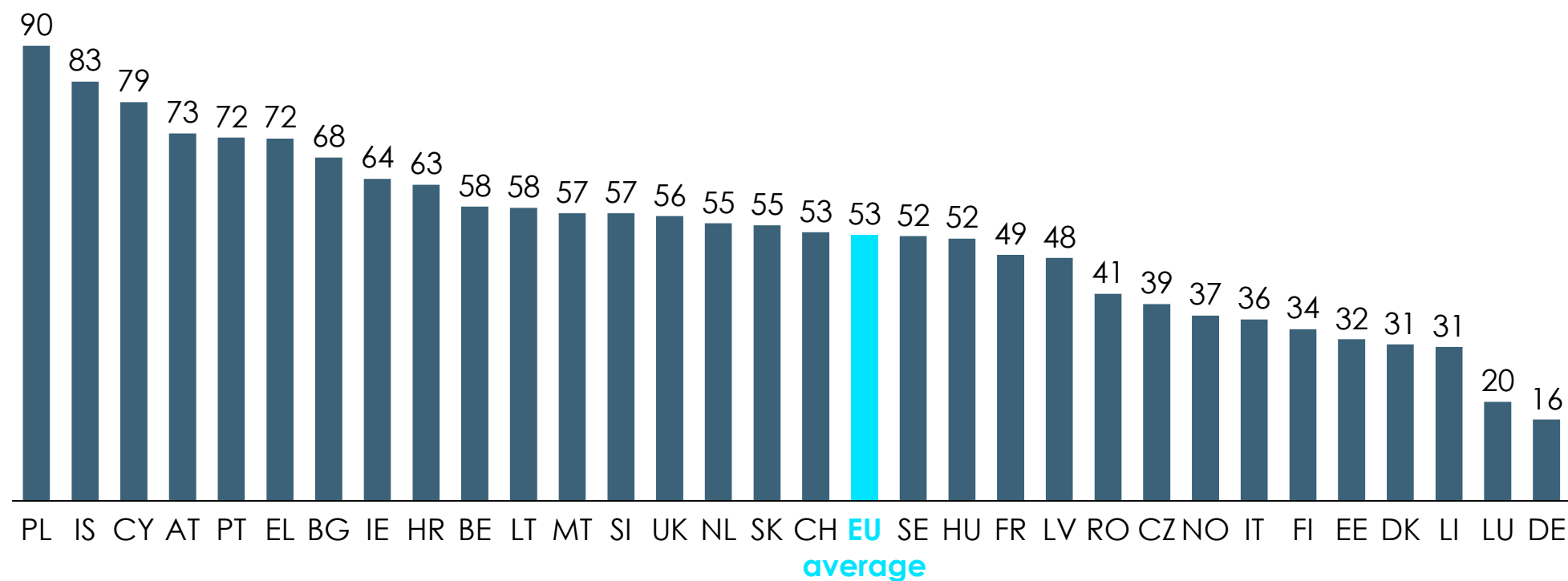
Percentage change of a number of post offices and post-in-shops



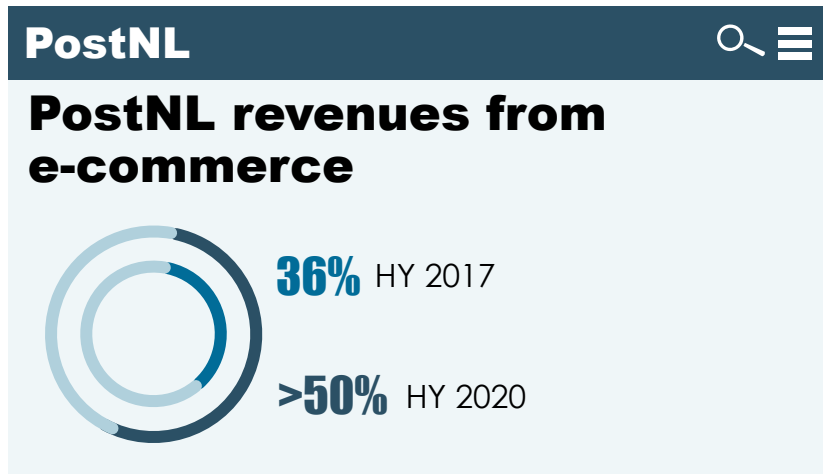
...pressure to diversify revenues

USP revenue diversification, 2016


% letter post revenue in USP's total revenue



Growing e-commerce packet and parcel volume leads to...



Accelerating transformation towards e-commerce

PostNord 

“Important steps towards a more modern postal distribution system”

Interim Report January-March 2018



Pressure to develop a nationwide network centred around parcel delivery

1 Important market developments

2 The competitive landscape in the postal sector

3 Employment and environmental developments

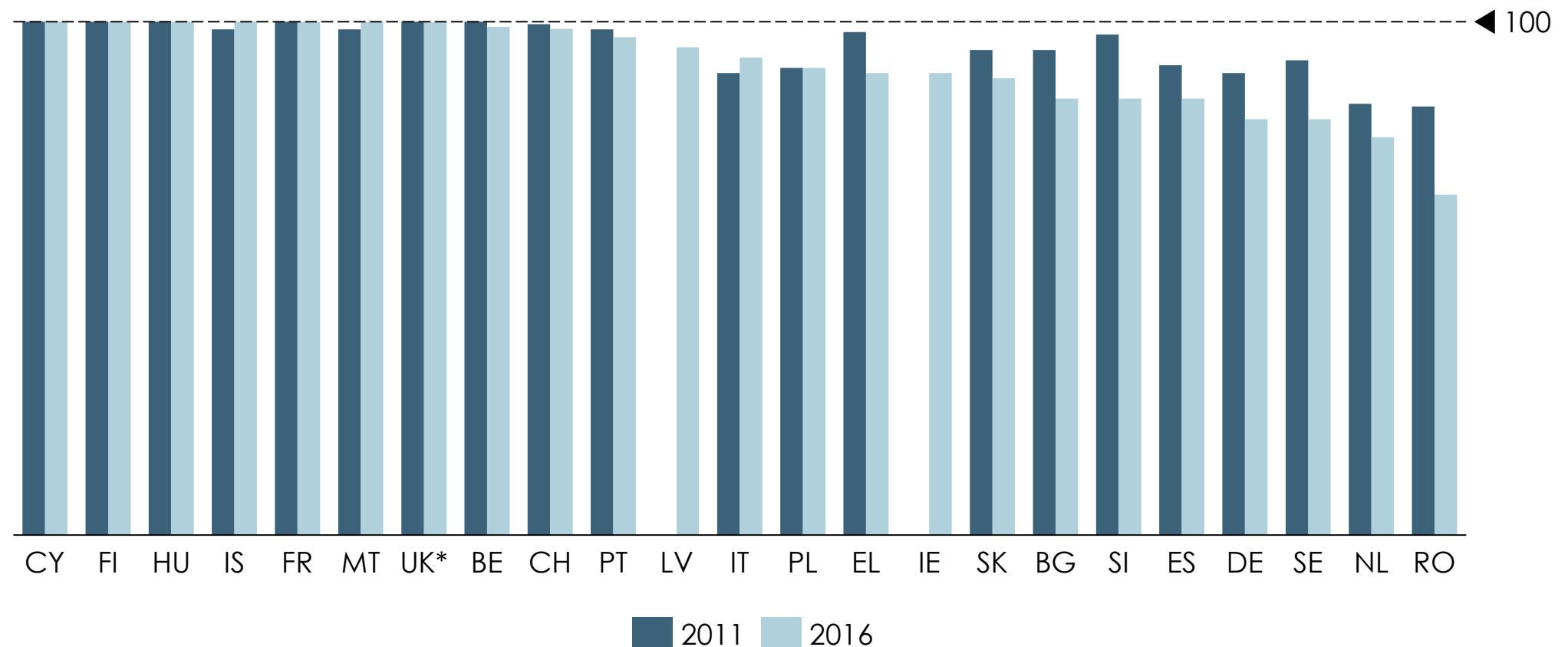
4 Developments in universal service

5 Scenarios for the future provision of the USO

Although USPs' market shares declined, letter markets are still concentrated

Market share of the incumbent in the addressed letter market

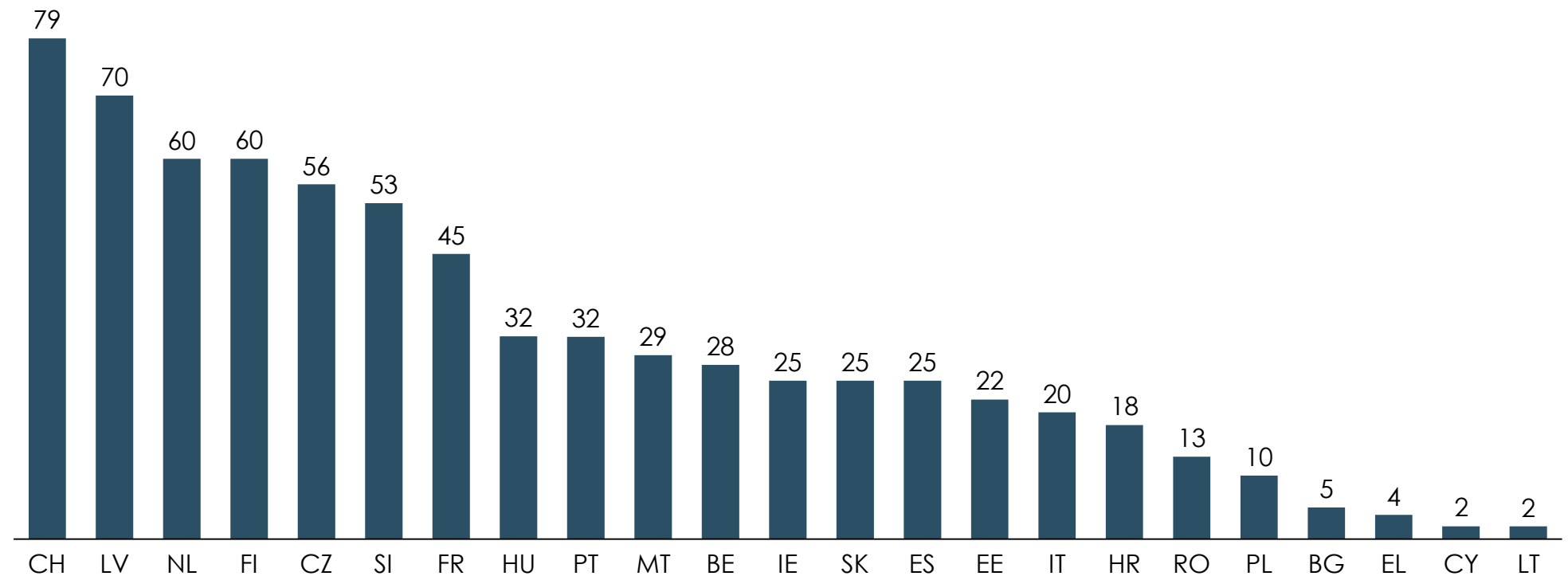
%, market share based on volumes



On the other hand, parcel markets are fragmented and more competitive

Market share of the USP in the parcel & express market, 2016

%, market share based on volumes



A number of regulatory, state aid and competition legal cases have taken place in the postal sector in 2013-2016



Pricing Practices



Mergers



USO Financing (State-aid)



Network Access Conditions



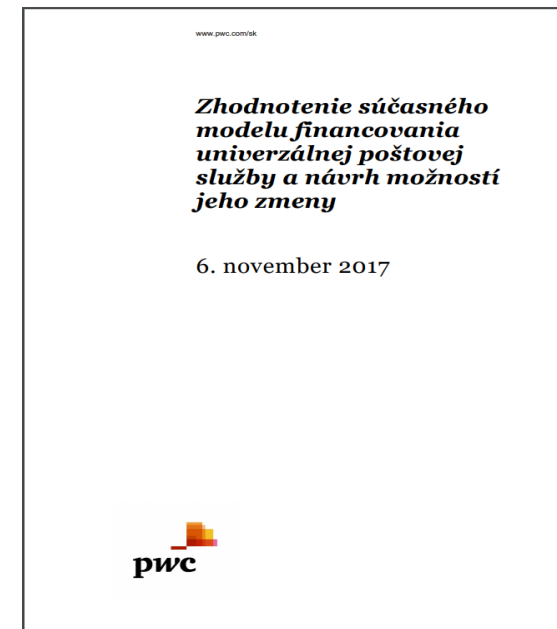
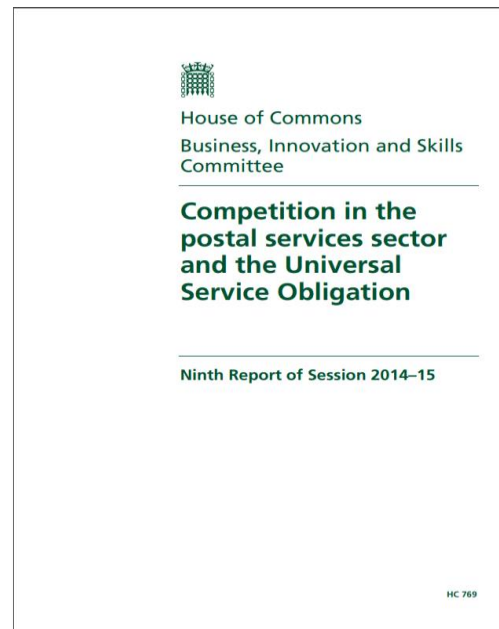
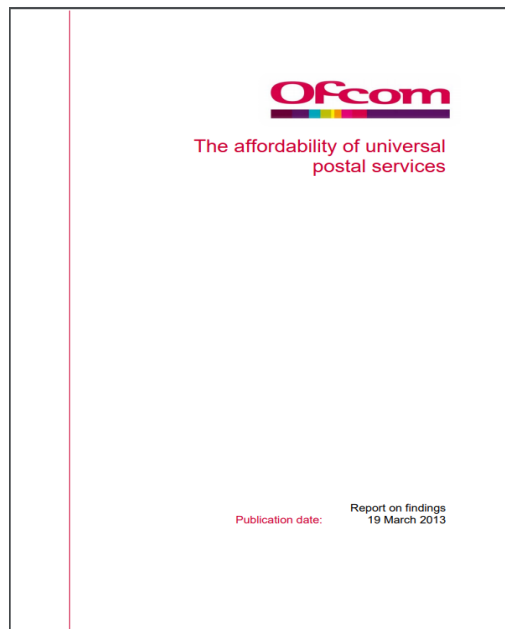
VAT Treatment



Main challenges for policymakers and regulatory authorities

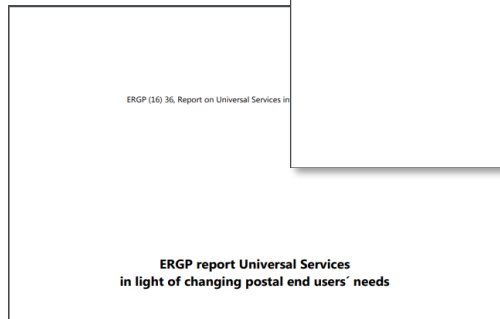
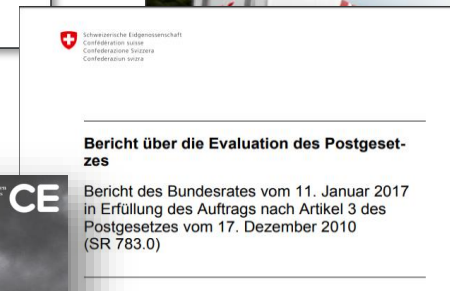
#1

Ensuring affordability and sustainability of the USO



#2

Defining the scope of the USO in light of changing user needs



#3

Adapting regulatory frameworks to ensure efficient cross-border parcel delivery

1



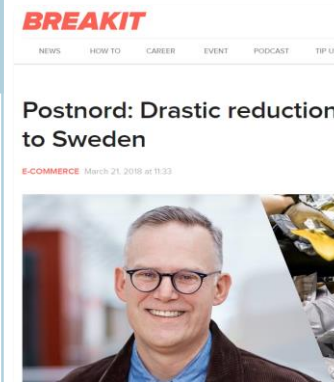
What are the user needs and is there a market failure?

2



Clear definition of key concepts (who is “the postal op.?”)

3



Implications of the removal of VAT de minimis

4



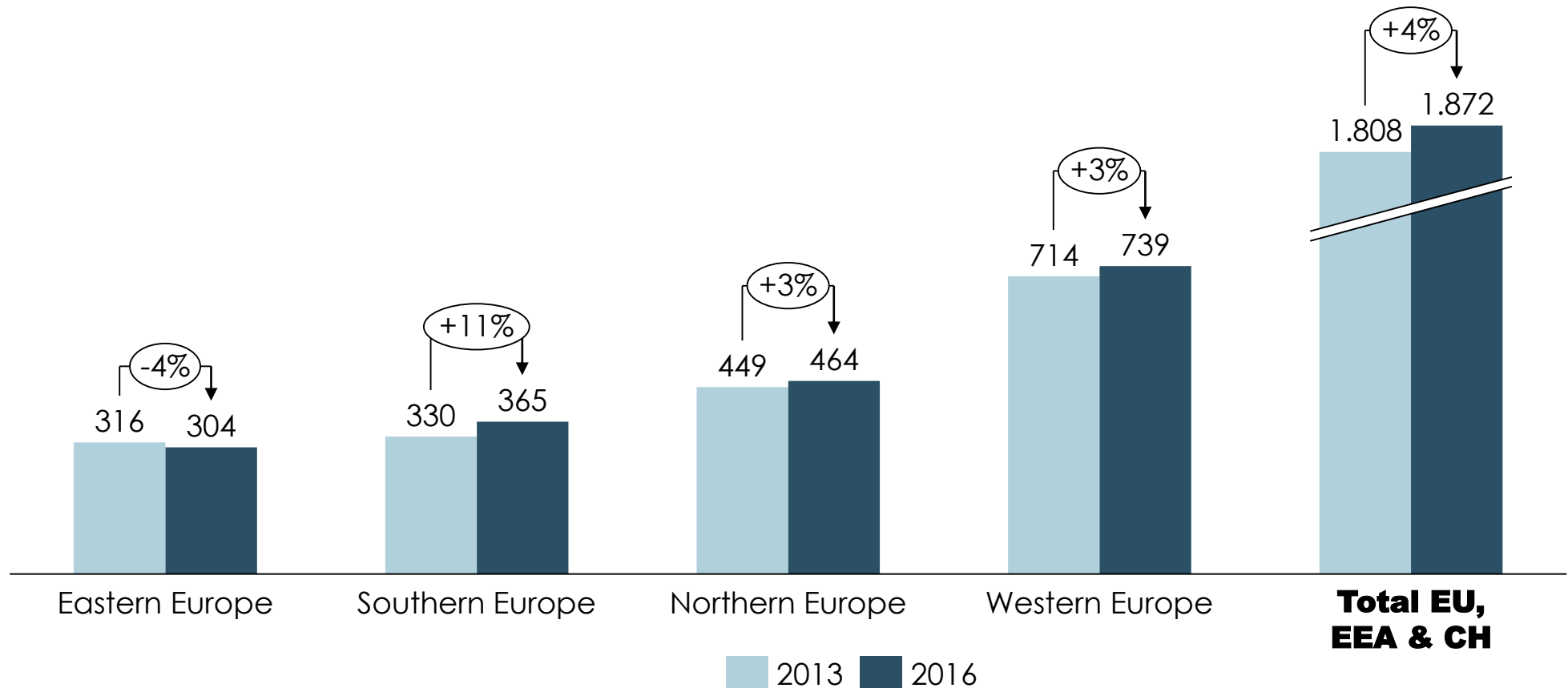
Fixing the UPU terminal dues issue

- 1** Important market developments
- 2** The competitive landscape in the postal sector
- 3** Employment and environmental developments
- 4** Developments in universal service
- 5** Scenarios for the future provision of the USO

Overall postal and courier sector employment increased, however...

Evolution of postal and courier sector employment, 2013 vs 2016

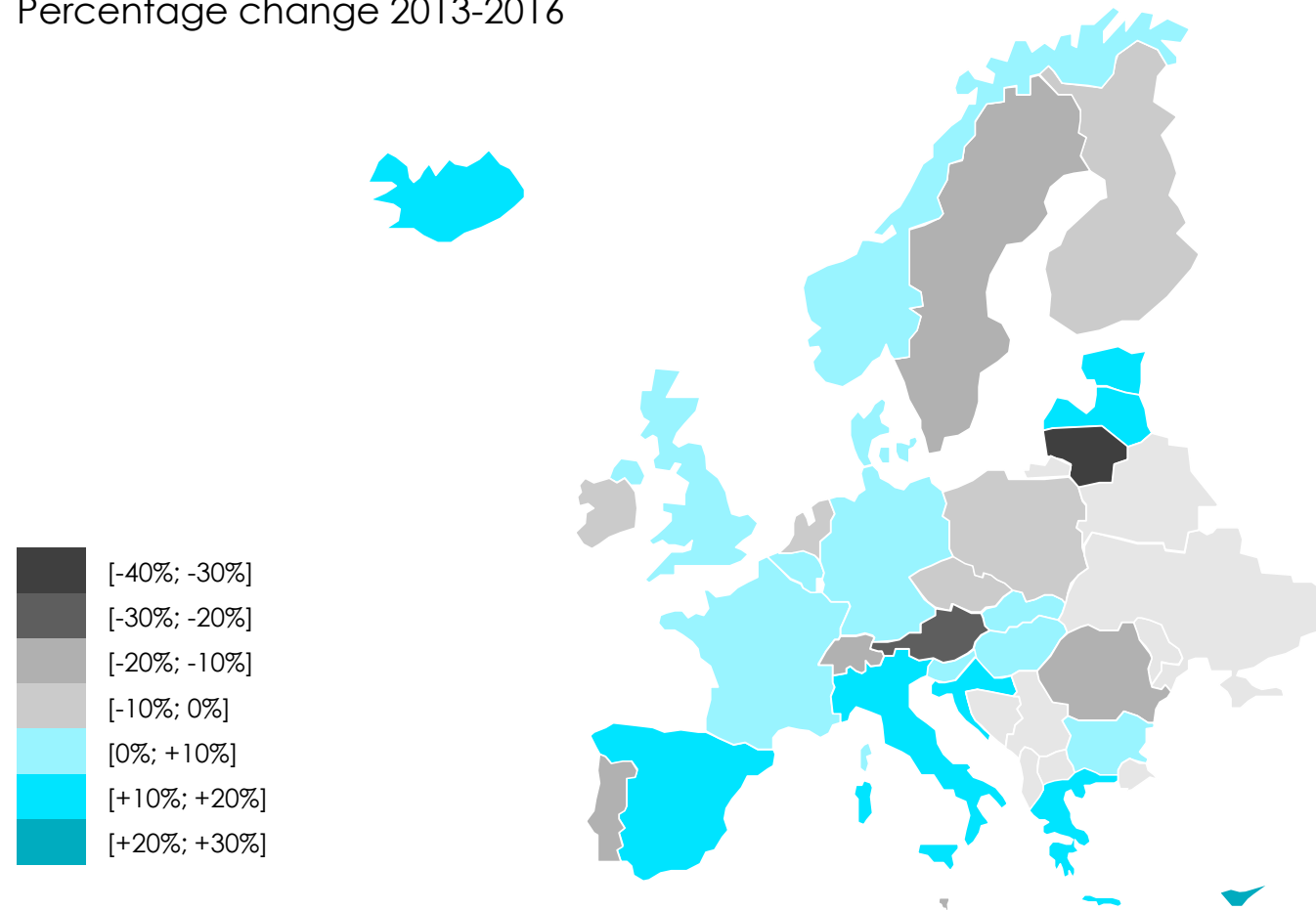
Headcount, thousands



Increases in postal employment are most visible in the South and West

Overall percentage change of the postal and courier sector's total employment, 2013-2016

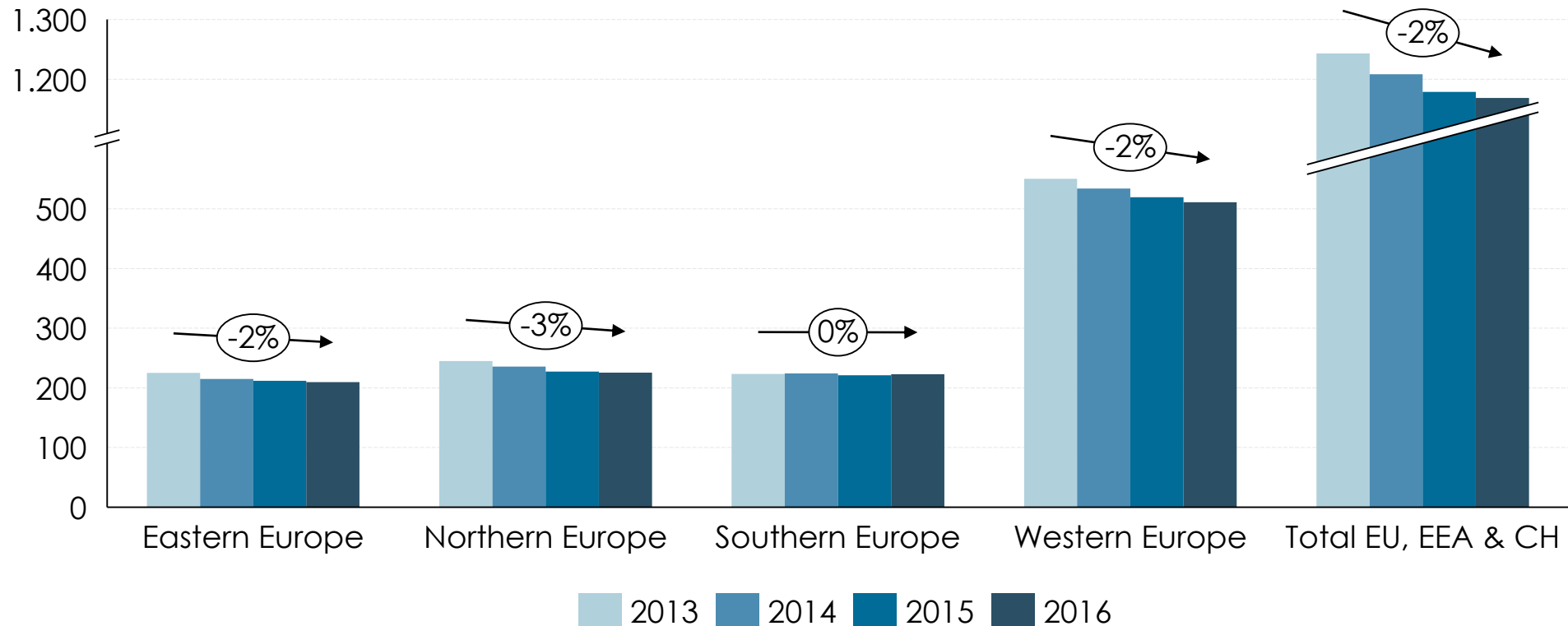
Percentage change 2013-2016



Employment at USPs decreased by 2%...

Evolution of USP employment

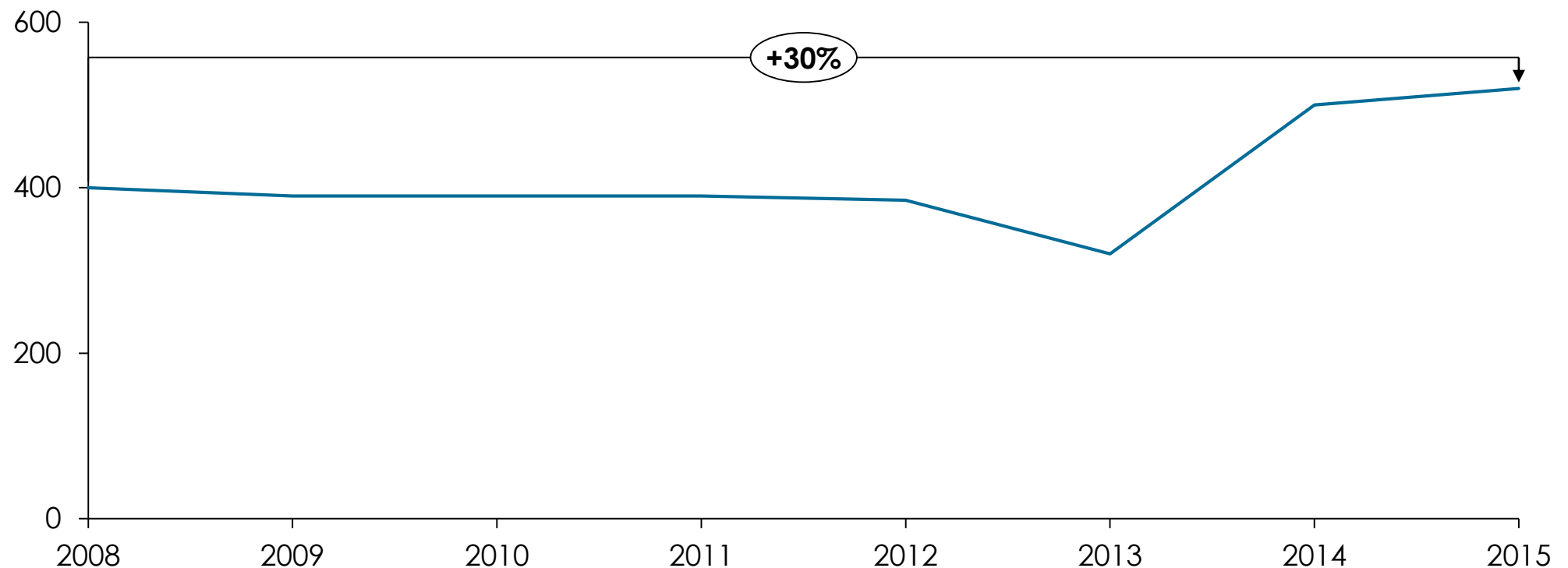
Staff employed in the home country, headcount, thousands



...but number of workers at other postal operators increased

Total employment by other postal providers, 2008-2015

Headcount, thousands

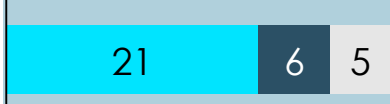
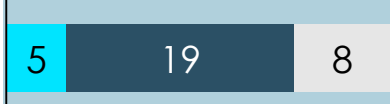
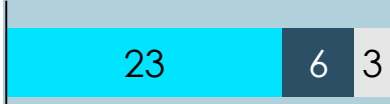



Source: ERGP (16) 38 Report on core indicators for monitoring the European postal market

We notice an increase in new and more flexible employment models

Extent of outsourcing and-subcontracted employment at USPs, 2016

Number of USPs

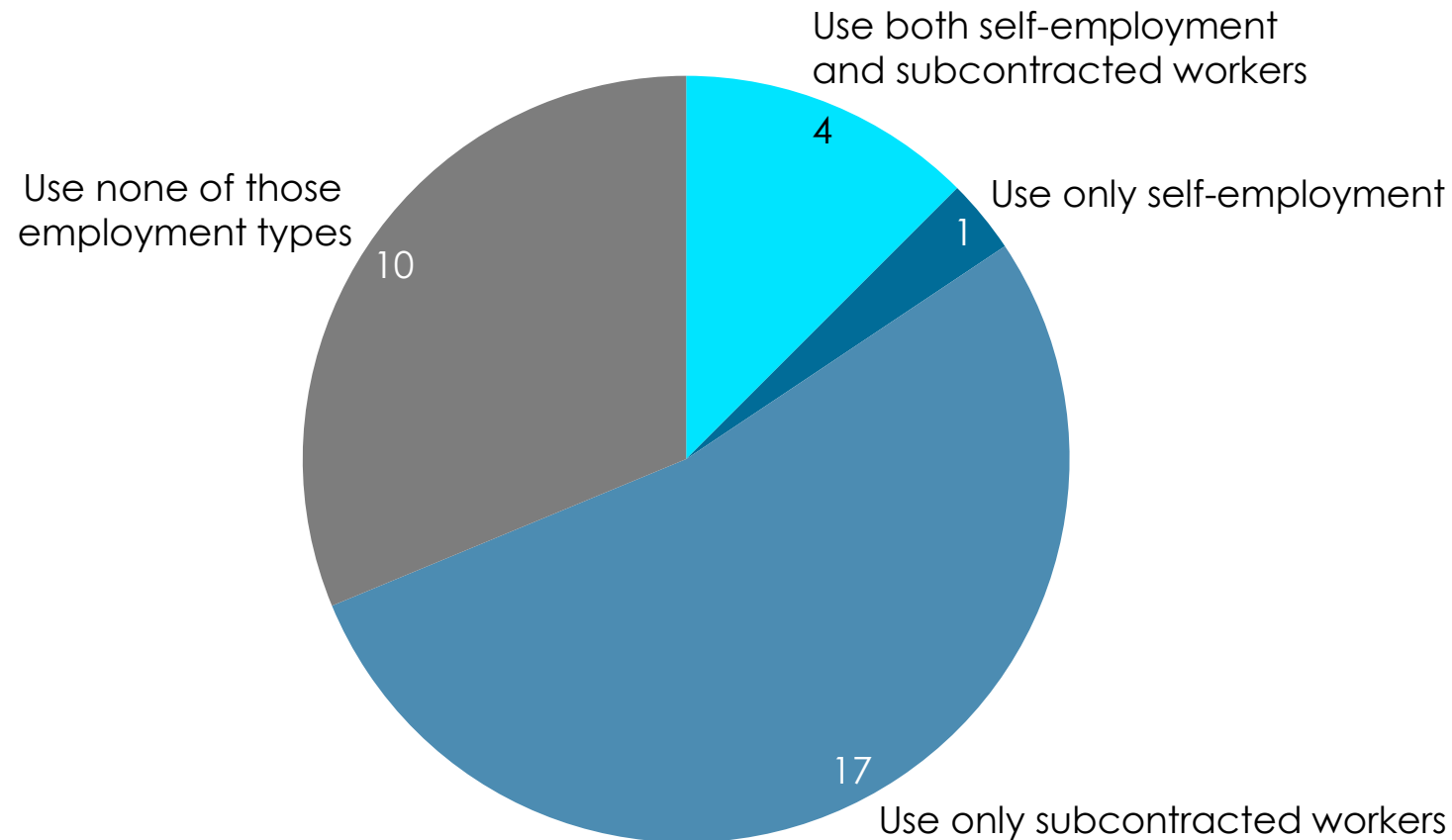
| Employment model | Number of countries | Share in total employment, min and max, 2016 | Average total change 2013-2016 |
|-----------------------------------|--|--|--------------------------------|
| Subcontracted workers |  | 1-13% | +36% |
| Self-employment contracts |  | <1% | +33% |
| Temporary employment |  | 1-50% | +10% |
| Performance-related pay contracts |  | 1-13% | +3% |

 Use
  Not use
  n/a

Around two thirds of USPs use at least one of the new employment models

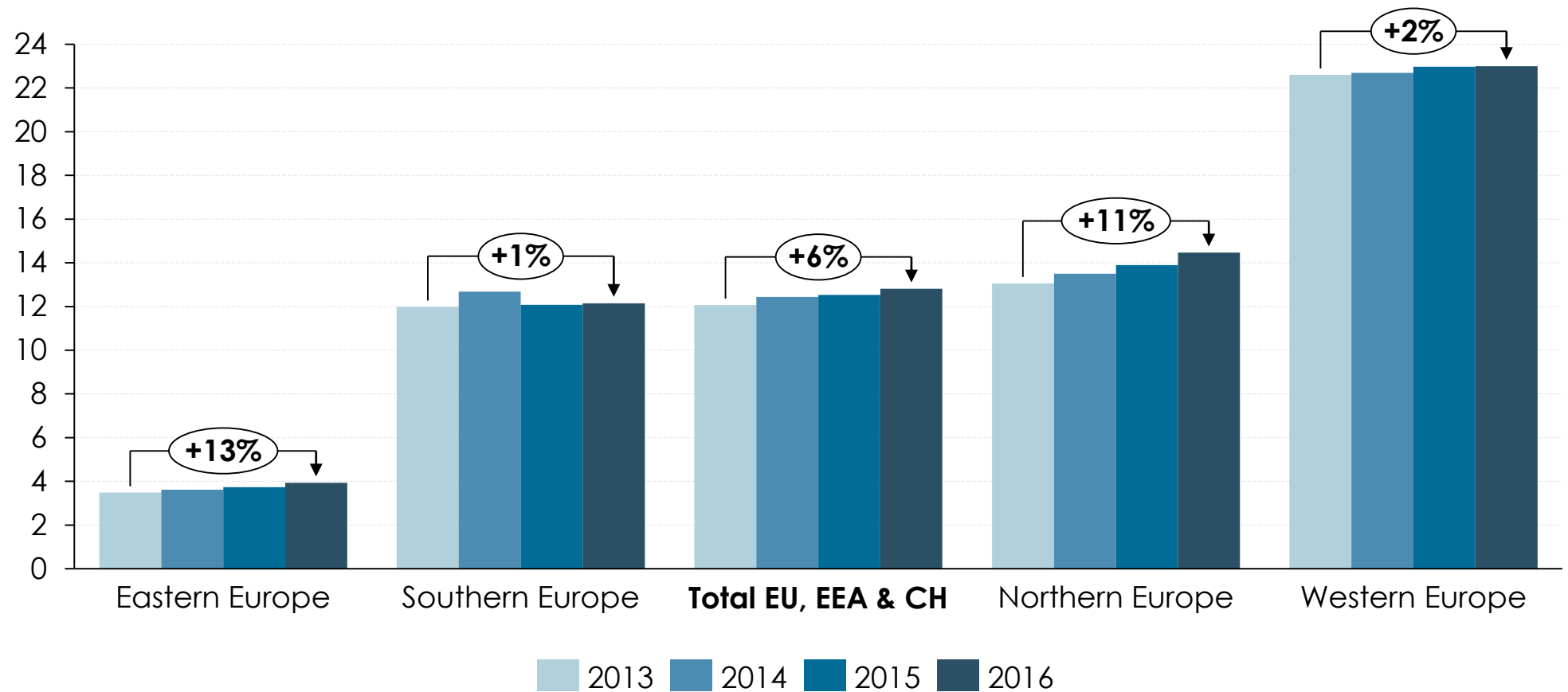
Extent of outsourcing and subcontracted employment at USPs

Number of USPs



The average wage for postal workers varies significantly across regions

Average nominal hourly wages for postal workers employed by USP
EUR/h

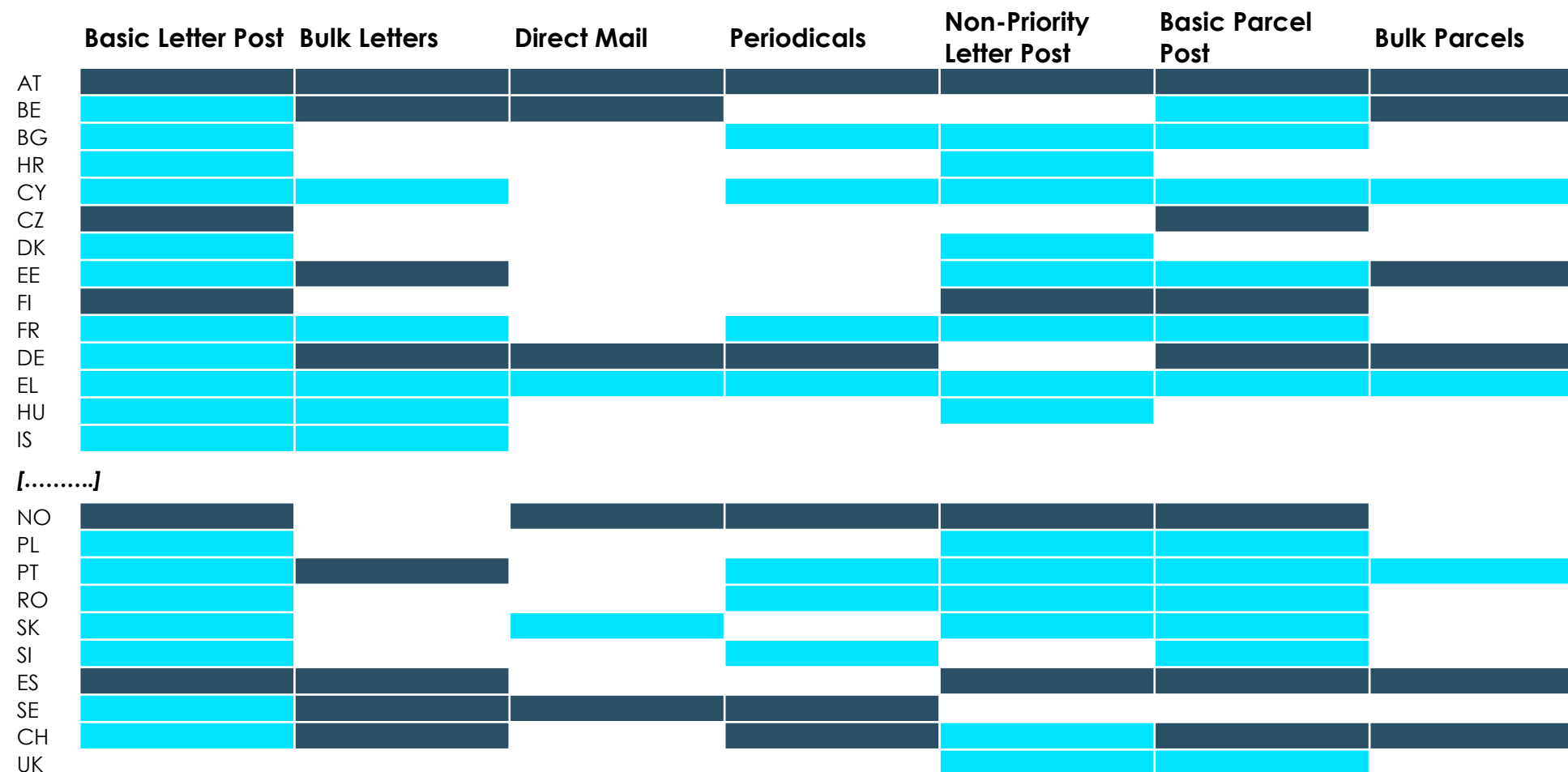


- 1** Important market developments
- 2** The competitive landscape in the postal sector
- 3** Employment and environmental developments
- 4** Developments in universal service
- 5** Scenarios for the future provision of the USO

Regulatory measures applied vary significantly across countries (1)

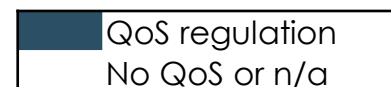


Method of price regulation



Regulatory measures applied vary significantly across countries (2)

Product scope of quality measurement



| | FSC Basic Letter | SSC Basic Letter | Bulk Letters | Registered Mail | Insured Mail | Direct Mail | Publications | Basic Parcel | Bulk parcels | Cross-border letter | Cross-border parcel |
|---------|------------------|------------------|--------------|-----------------|--------------|-------------|--------------|--------------|--------------|---------------------|---------------------|
| AT | QoS | QoS | QoS | | | QoS | | QoS | QoS | QoS | QoS |
| BE | QoS | | | QoS | QoS | | | QoS | | QoS | |
| BG | QoS | QoS | | | | | | QoS | | QoS | |
| HR | QoS | QoS | | | | | | QoS | | QoS | |
| CY | QoS | | | | | | | | | QoS | QoS |
| CZ | QoS | | | QoS | QoS | | | QoS | | QoS | QoS |
| DK | | QoS | | | | | QoS | | | | |
| EE | QoS | QoS | | | | | | | | | |
| FI | | QoS | | | | | | | | QoS | |
| FR | QoS | QoS | | QoS | | | QoS | QoS | | QoS | |
| DE | QoS | | | QoS | QoS | | QoS | QoS | QoS | | |
| EL | QoS | | | | | | | | | QoS | |
| HU | QoS | QoS | QoS | QoS | QoS | QoS | | QoS | QoS | QoS | |
| IS | QoS | QoS | | | | | | | | QoS | |
| [.....] | | | | | | | | | | | |
| PT | QoS | QoS | QoS | QoS | QoS | | QoS | QoS | QoS | | QoS |
| RO | QoS | | | | | | | | | QoS | |
| SK | QoS | QoS | | | | QoS | | QoS | | | |
| SI | QoS | | | | | | QoS | QoS | | QoS | |
| ES | QoS | | QoS | | | | | QoS | | | |
| SE | QoS | | | | | | | | | | |
| CH | QoS | QoS | | | | | | QoS | | | |
| UK | QoS | QoS | | QoS | QoS | | | QoS | | QoS | QoS |

Interpretations of the PSD vary significantly across countries

Interpretation of the cost orientation principle by NRAs



**Individual price
point = FAC +
reasonable profit**

**USO revenues as a
whole = FAC +
reasonable profit**

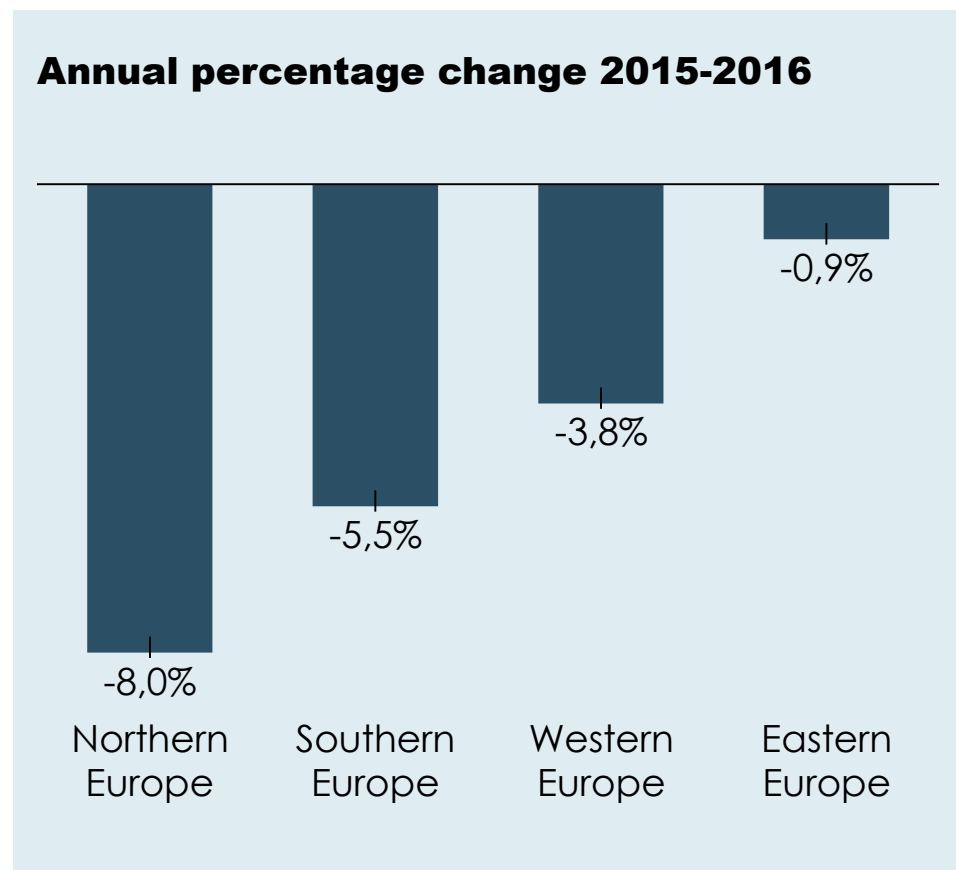
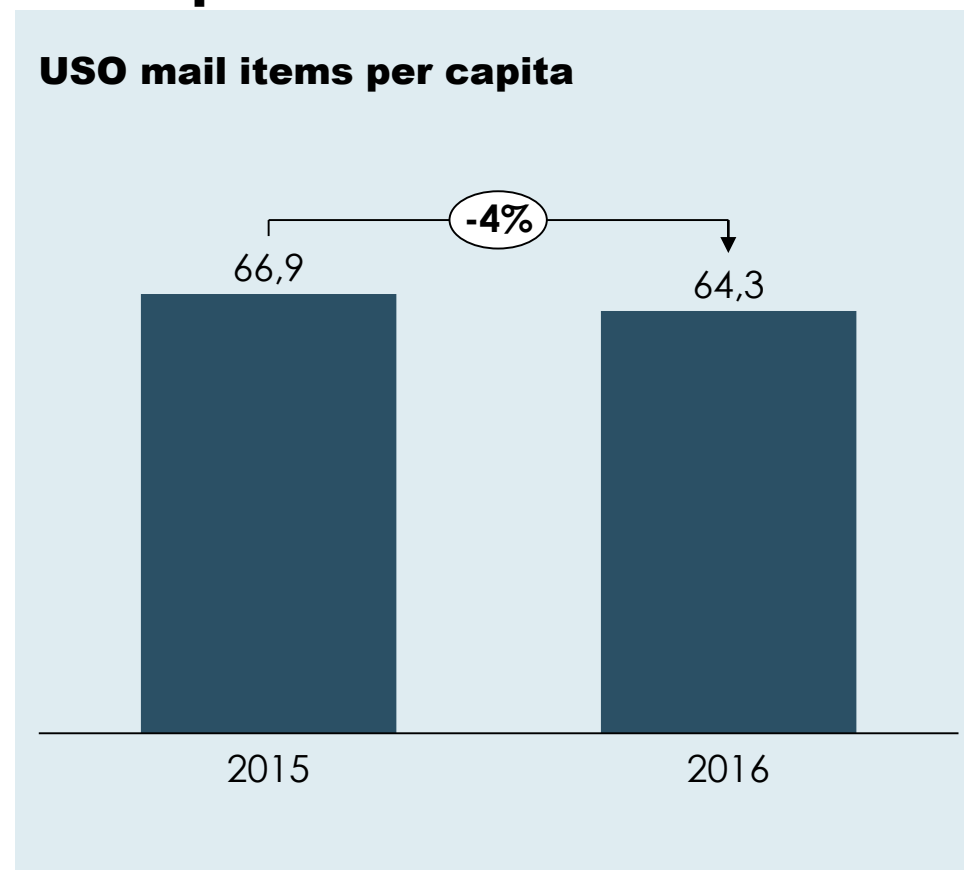
Article 12 of Directive 97/67 is not to be interpreted as imposing an obligation on universal service providers that each individual service that is part of the universal service must be cost-oriented.



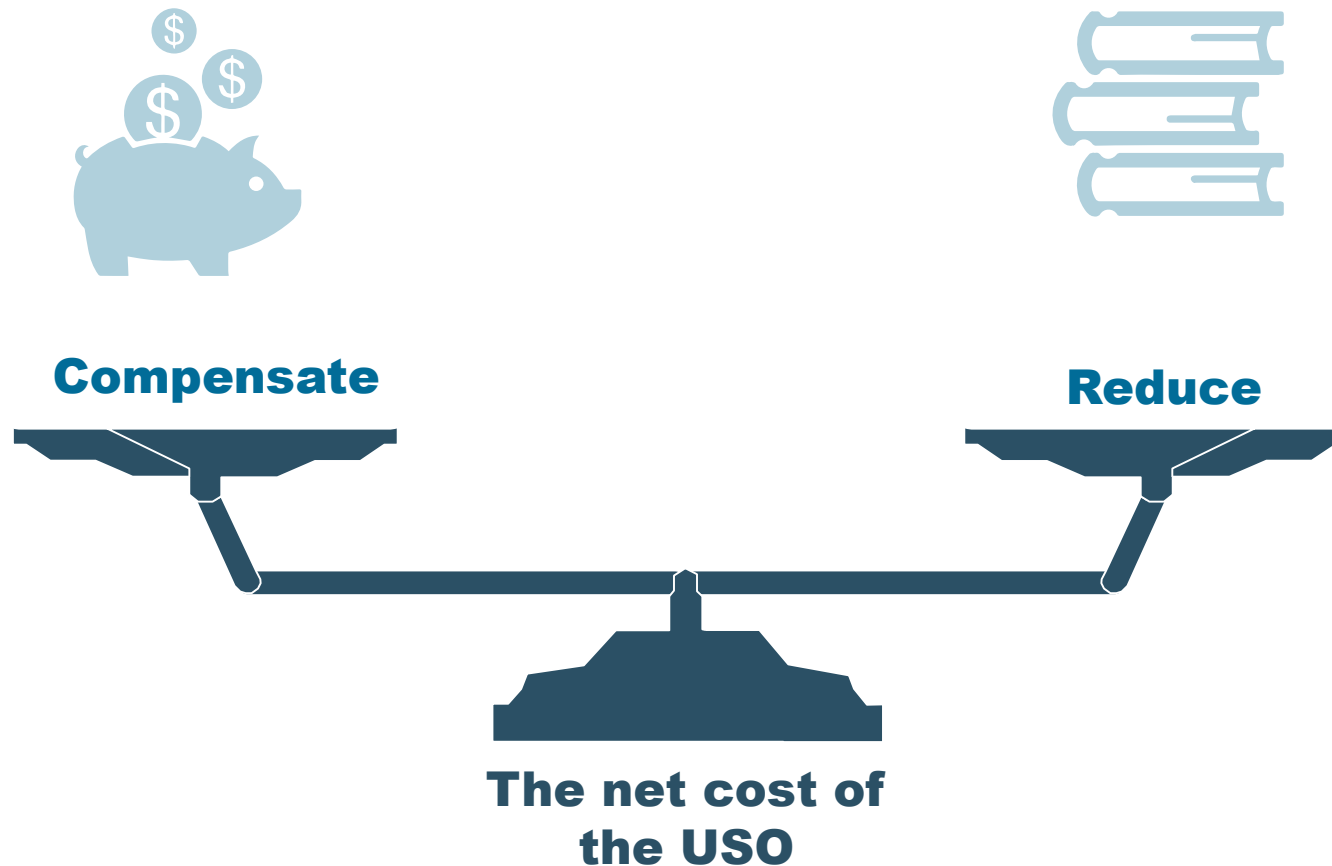
[Opinion of advocate general Wahl, delivered on 20 June 2018]

Changes in user preferences challenge USO sustainability

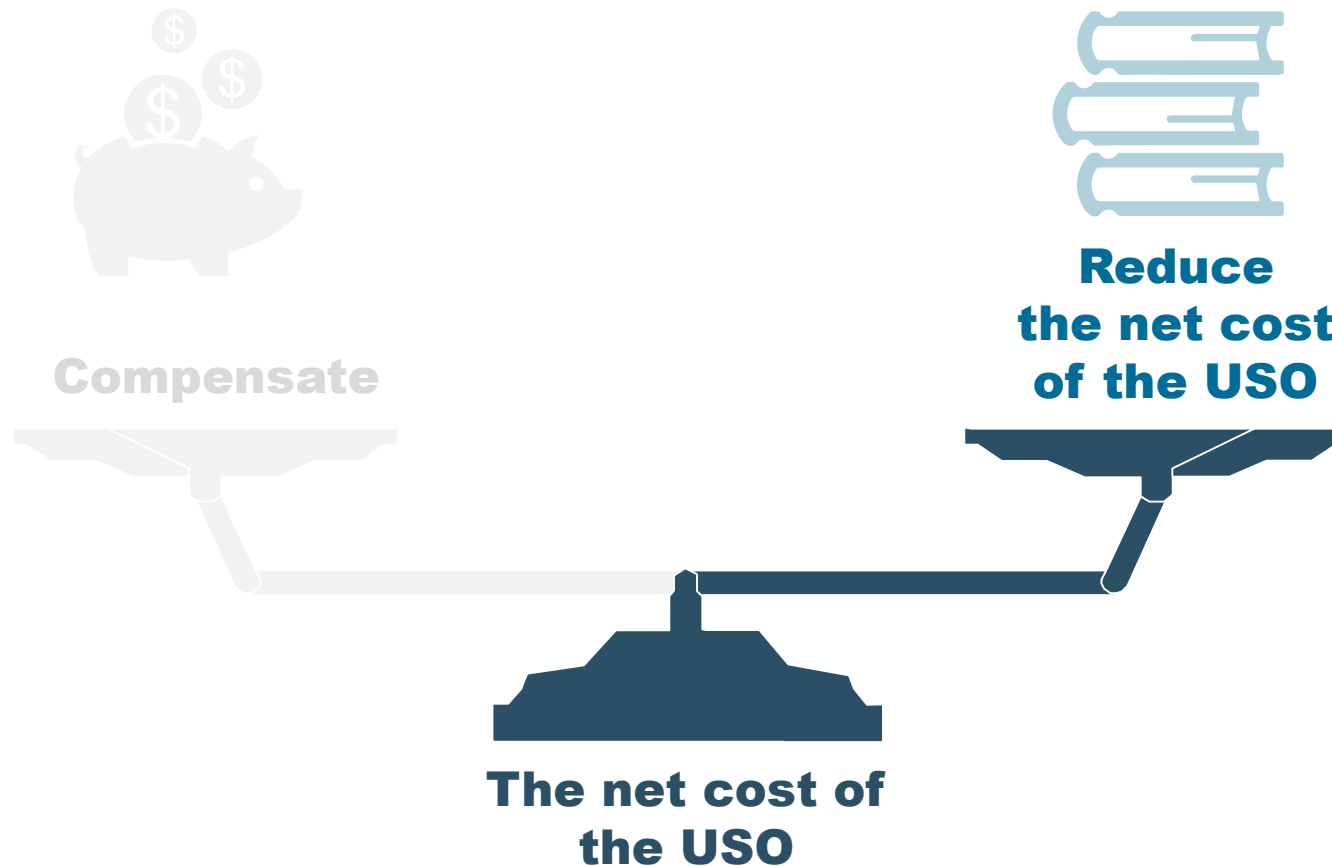
Development of USO volumes



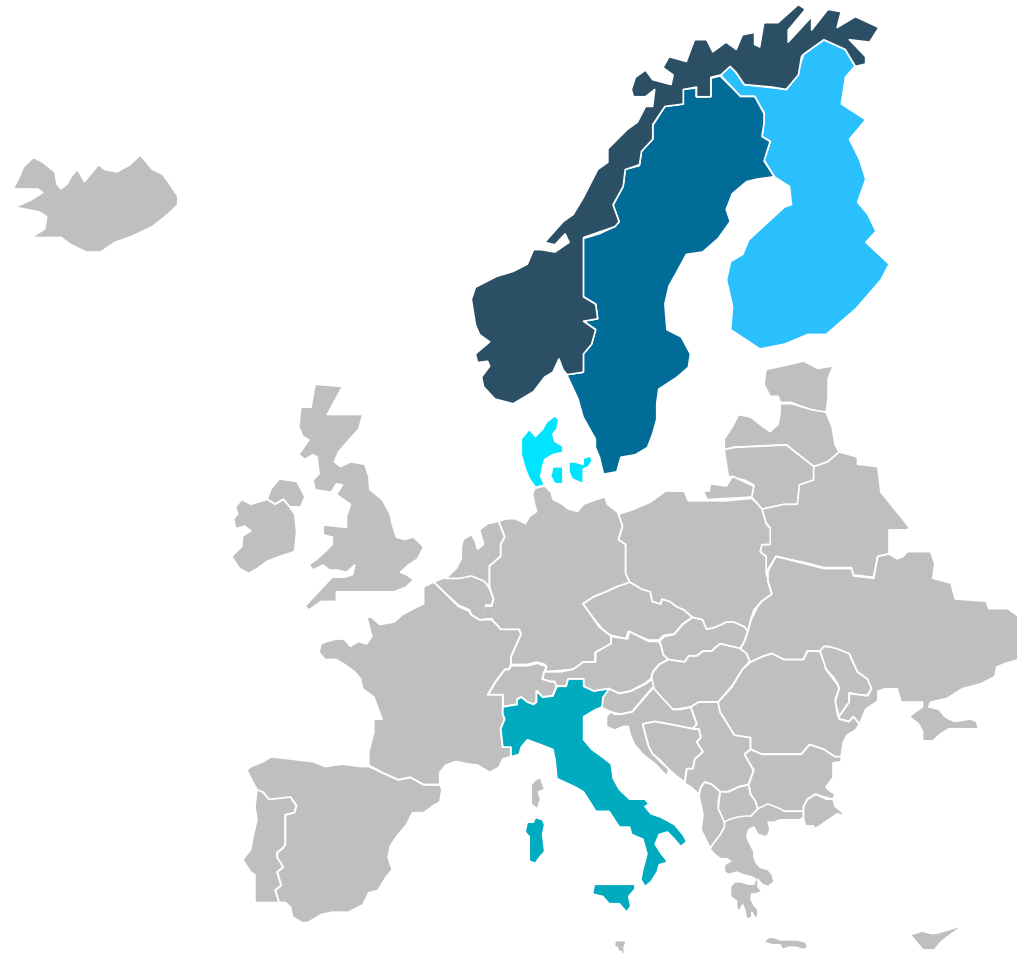
Policymakers and regulators are searching for the appropriate reaction to market developments



Policymakers and regulators are searching for the appropriate reaction to market developments



Some governments responded by reducing the delivery speed



Merging of A and B letters, creating a D+2 standard service (2018)



D+2 replacing D+1 as standard product (2018)



Merging of A and B letters, creating a D+2 standard service (2017)



Elimination of first class letters from the USO and decreased delivery speed for B-letters (2016)



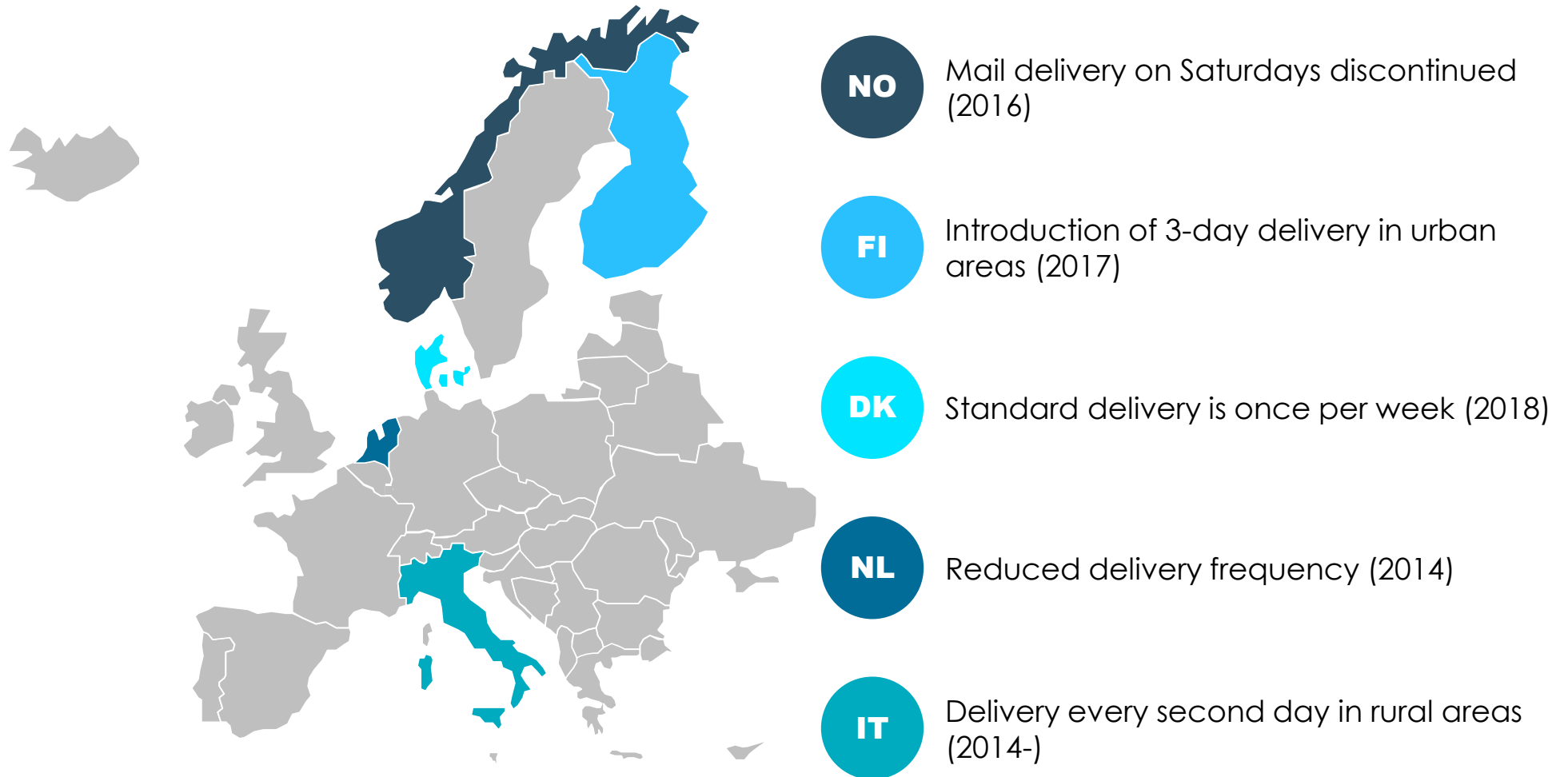
Introduction of slow letter mail product, D+4 (2015)

The beloved D+1 is not a universal service in six countries

Fastest letter product in the USO, where delivery speed is lower than D+1

| | | |
|-------------------|-----|------------------------------|
| Denmark | D+5 | Since 2016 |
| Finland | D+4 | Since 2017 |
| Luxembourg | D+3 | |
| Norway | D+2 | Since 2018 |
| Spain | D+3 | |
| Sweden | D+2 | Since 2018 |
| Romania* | D+2 | * Intention, not implemented |

Some governments responded by reducing the frequency of delivery



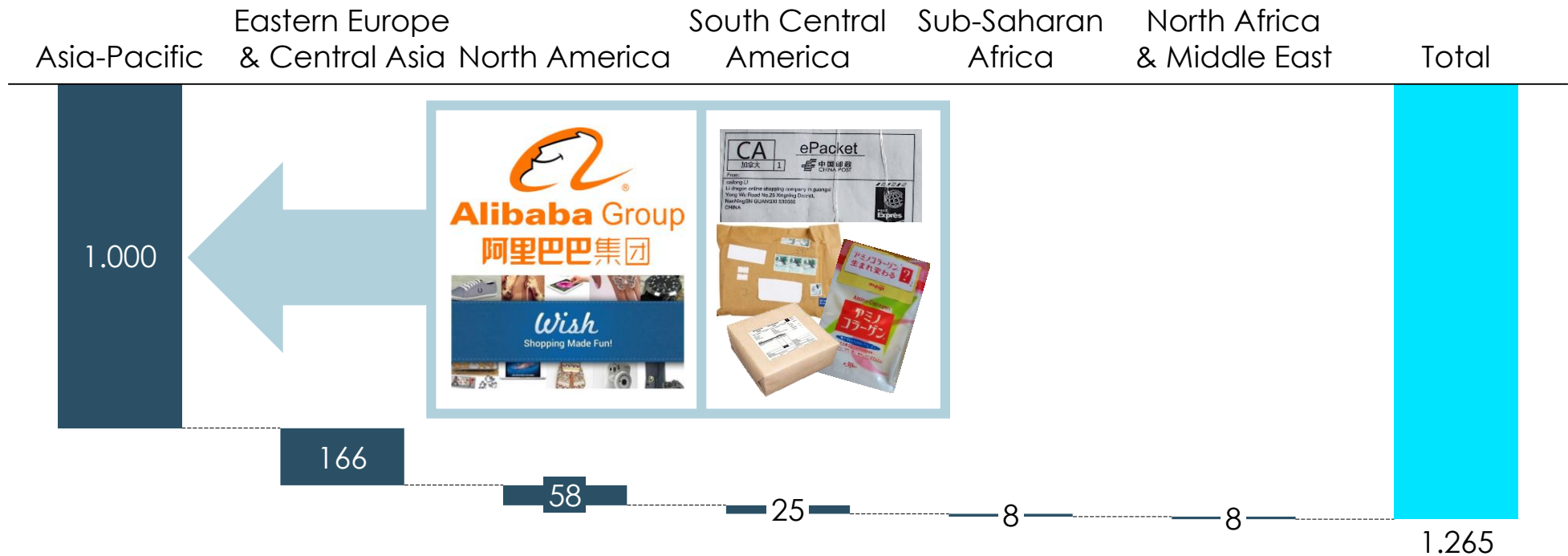


Rapid growth of e-commerce creates challenges...

#1

UPU terminal dues add to the financial burden of some USPs

Western Europe net financial transfer from terminal dues, 2018
Million EUR



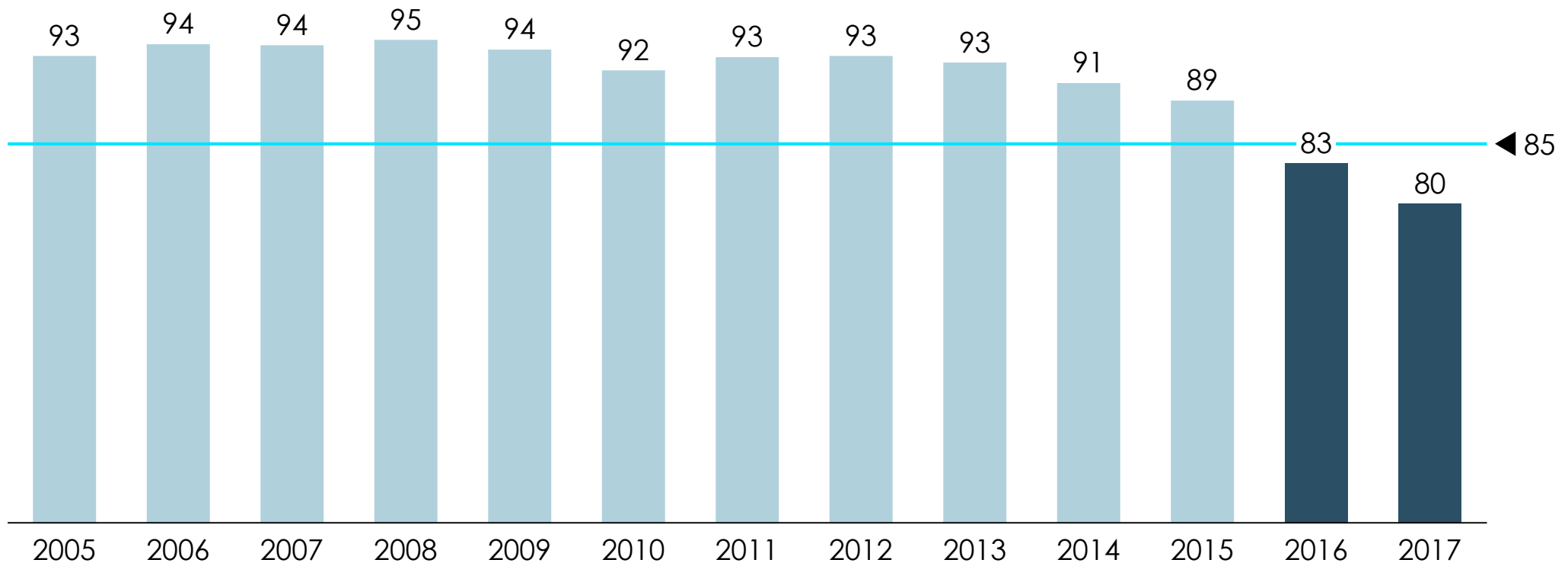
Source: Copenhagen Economics (2017) A study for the U.S. Postal Regulatory Commission. Impact on financial transfers among designated postal operators of the Universal Postal Union 2018-2021 cycle agreements.

#2

Fewer cross-border items are delivered on target

Transit time performance for international European priority letter mail

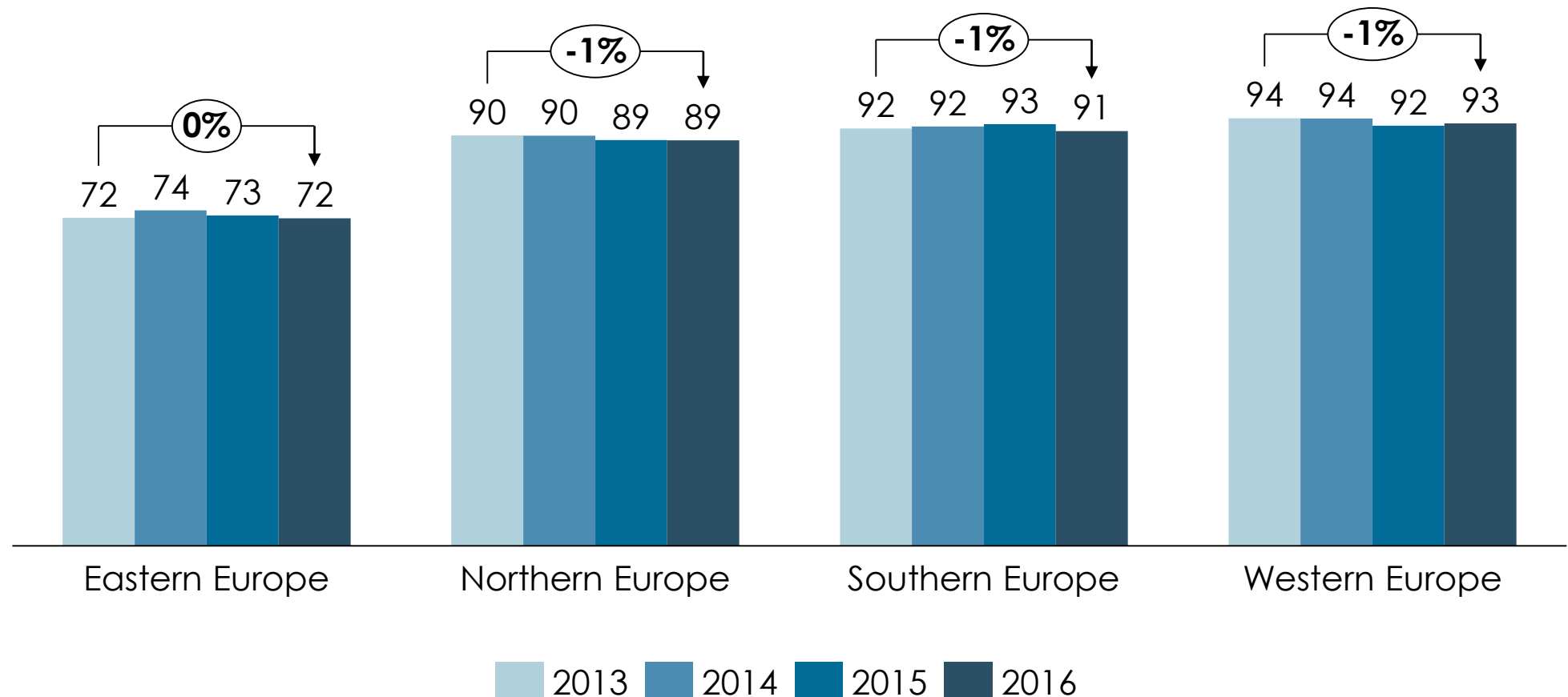
Transit time performance, %



However, transit time performance of domestic D+1 letters remained stable

Evolution of domestic quality of service for priority letter

% letters arrived in D+1

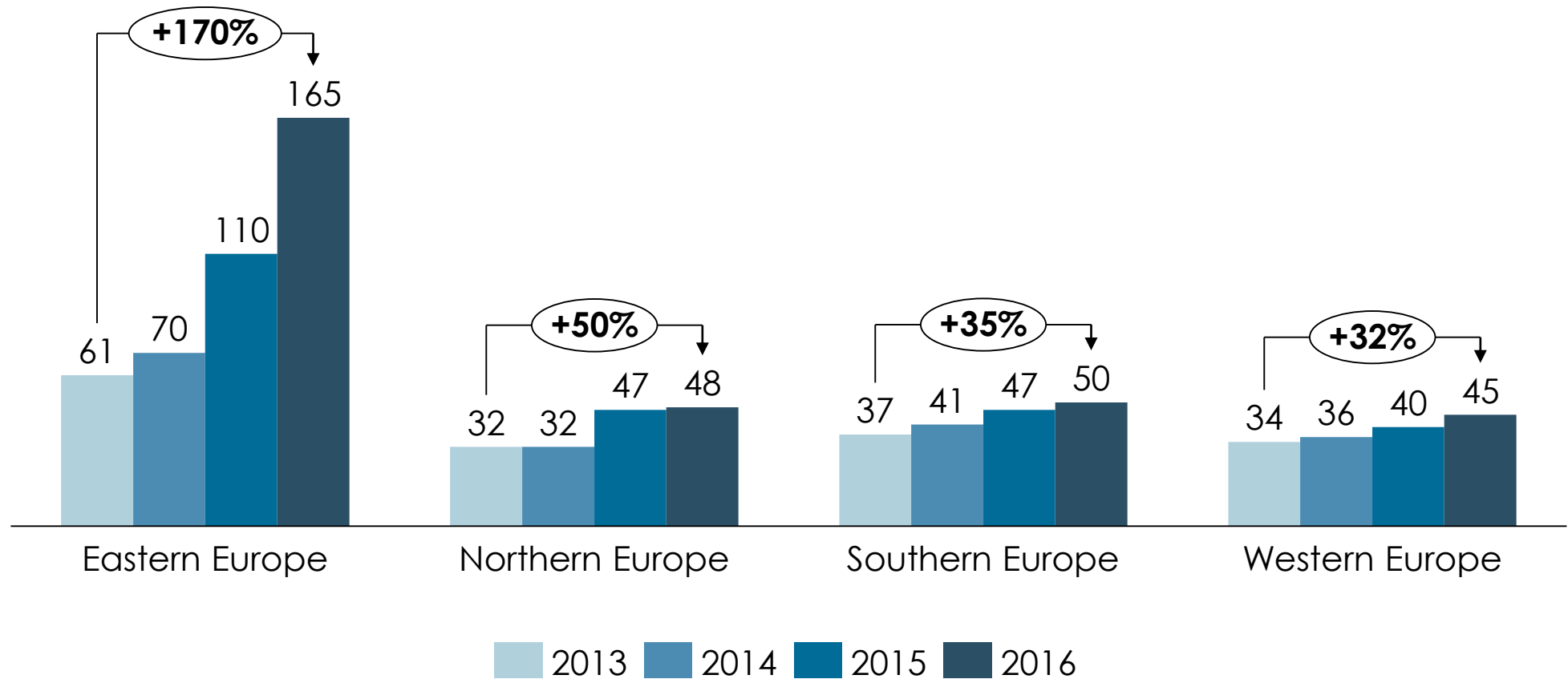


#3

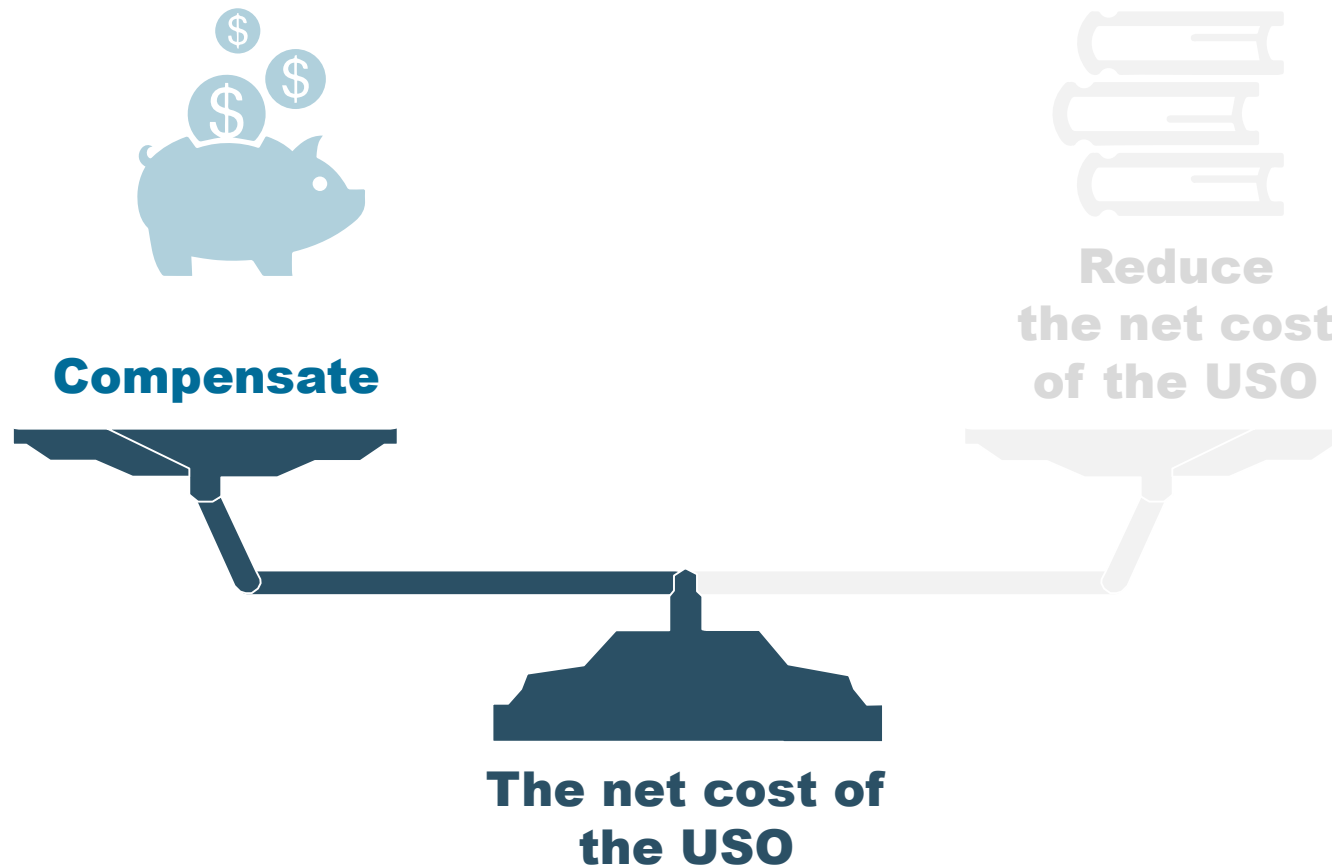
Large increase in user complaints across the board

Evolution of user complaints sent to NRA and USP

Average number complaints per 1 million domestic letter post items



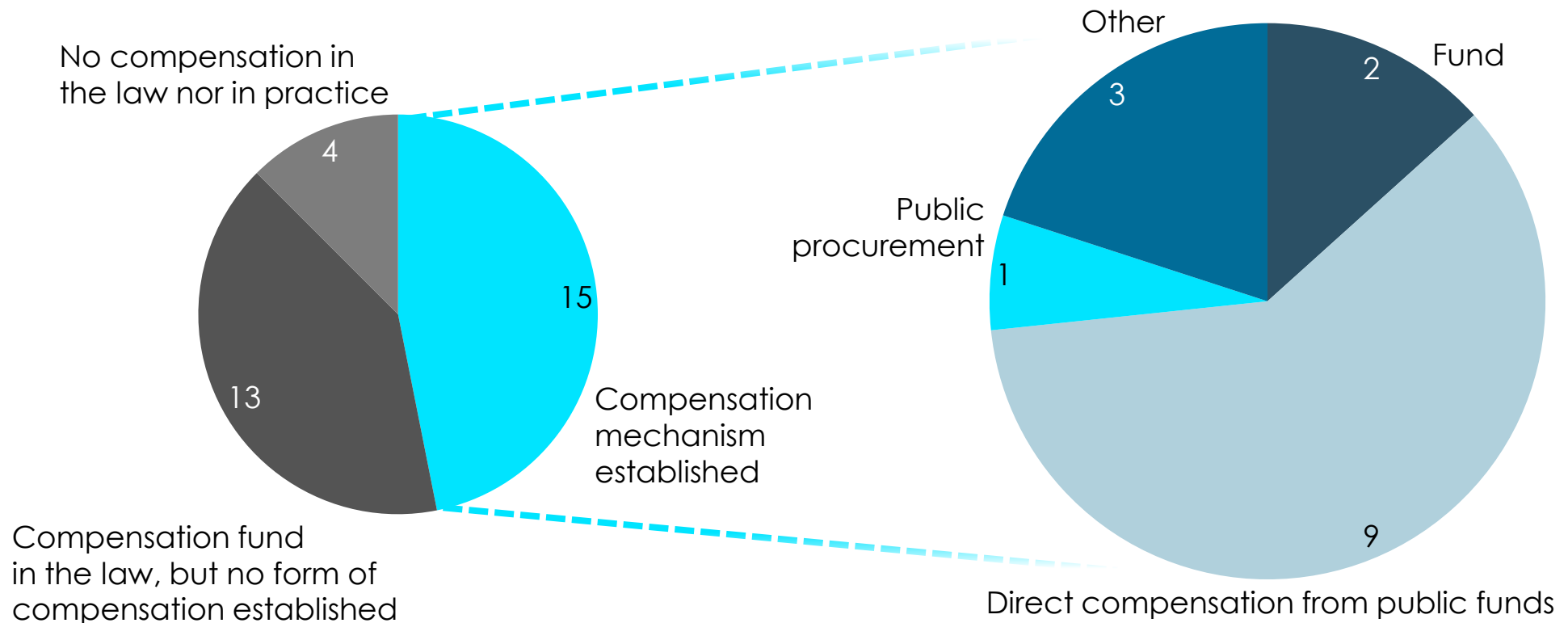
Policymakers and regulators are searching for the appropriate reaction to market developments



Half of the governments compensate the USP for the financial burden imposed by the USO

Compensation mechanisms authorized in the law and established in practice

Number of USPs

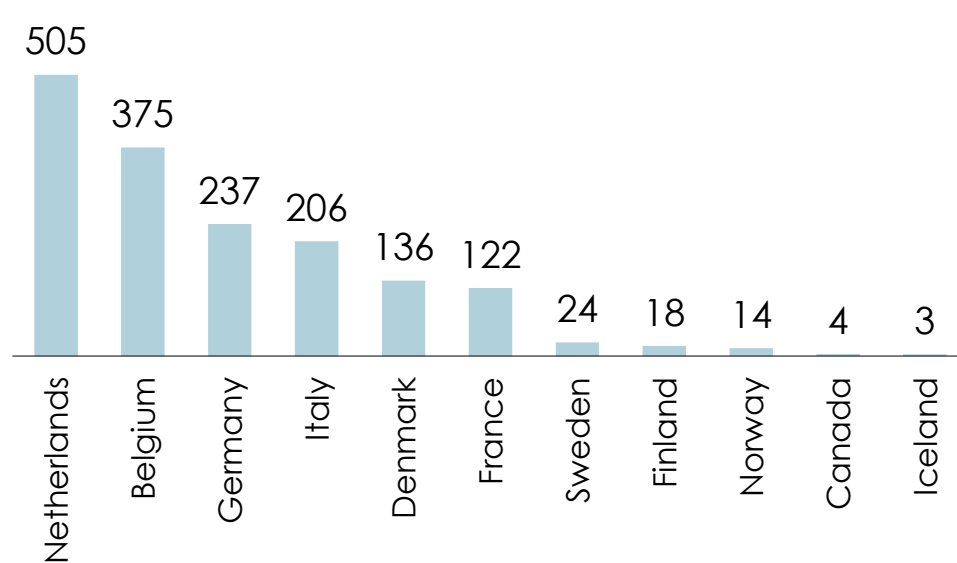


- 1** Important market developments
- 2** The competitive landscape in the postal sector
- 3** Employment and environmental developments
- 4** Developments in universal service
- 5** Scenarios for the future provision of the USO

Low population density and few items per capita make mail delivery expensive

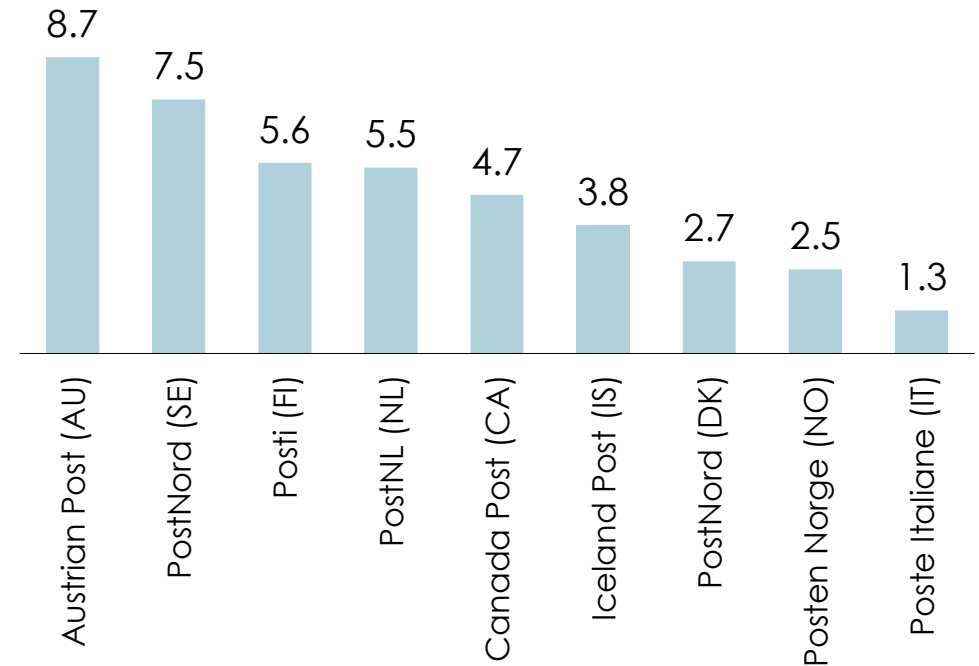
Population densities, 2016

People per sq. km of land area

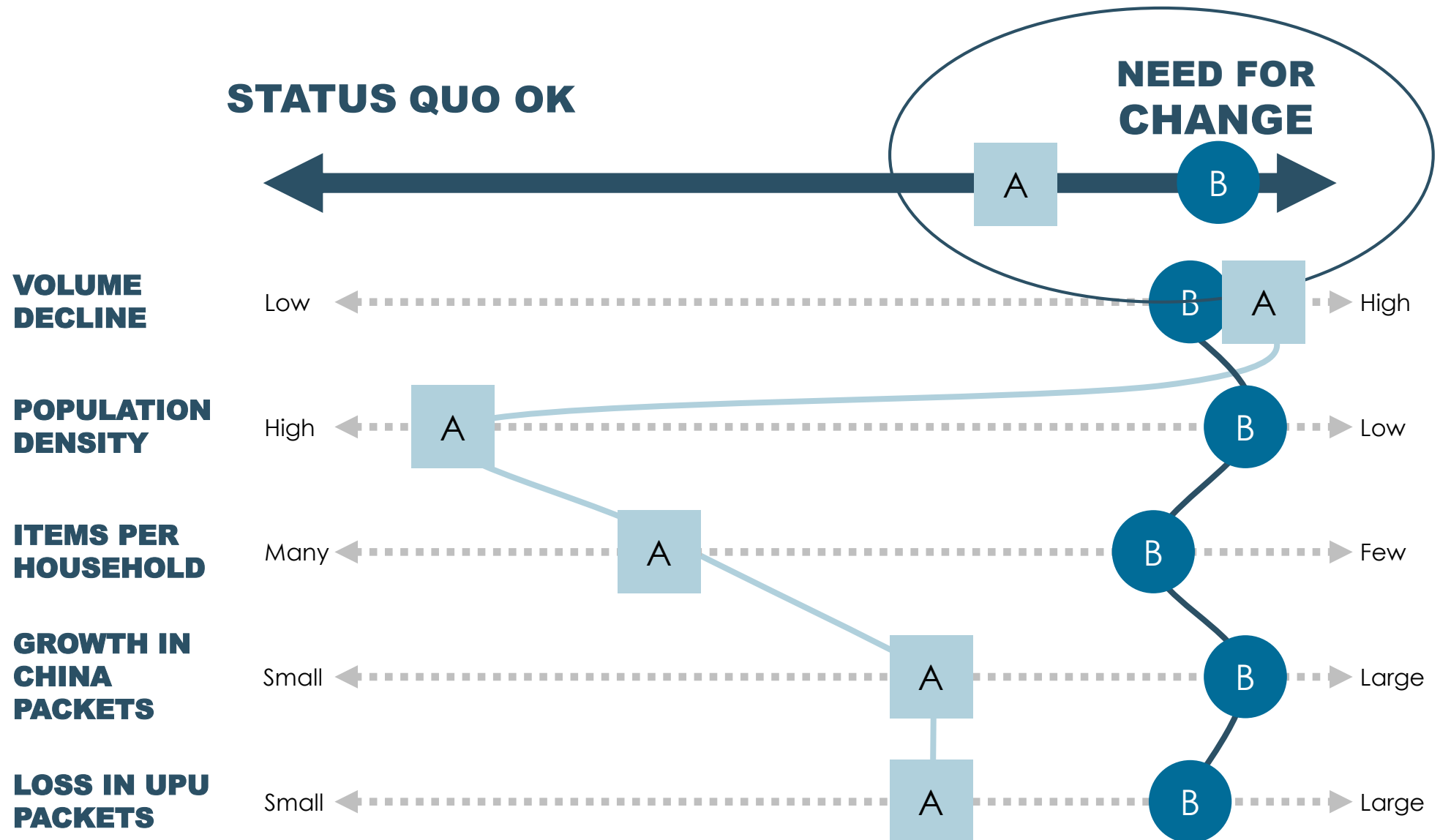


Addressed mail items per household per week, 2016

Items



The scoreboard



Roadmap to impact assessment



Define potential scenarios for the future provision of the USO



Assess the impact on net costs of USO



Assess impact on users, employees and other stakeholders

Roadmap to impact assessment



Define potential scenarios for the future provision of the USO

1. Define current national USO requirements
2. Define regulatory options based on the initial screening of costs and benefits



Assess the impact on net costs of USO



Assess impact on users, employees and other stakeholders

Step 1: Define potential scenarios for the future provision of the USO

| | |
|---|---|
| 1 Status quo | <ul style="list-style-type: none"> • Maintain the current scope and minimum requirements of the USO |
| 2 Reduce delivery frequency | <ul style="list-style-type: none"> • From 6 to 5 days nationwide • From 5 to 2.5 days nationwide • From 5 days nationwide to 3 days in rural areas, 5 days in urban areas • From 5 days nationwide to 3 days in urban areas, 5 days in rural areas |
| 3 Reduce speed of delivery | <ul style="list-style-type: none"> • From D+1 to D+2 • From D+2 to D+5 |
| 4 Allow different forms of delivery | <ul style="list-style-type: none"> • From delivery to the door, delivery to the street • From delivery to the street, delivery to the post office • From delivery to the street, delivery to the communal centre |
| 5 Remove uniform prices requirement | <ul style="list-style-type: none"> • Remove the price uniformity requirement, i.e. allow geographic price differentiation for SP and bulk letters |
| 6 Relax ubiquity (accessibility) requirement | <ul style="list-style-type: none"> • Reduce the required number of post offices in rural areas by 25% to 50% • Reduce the required number of post offices in urban areas by 25% to 50% • Allow alternative models, e.g. mobile post offices, franchise model |

Roadmap to impact assessment



**Define potential scenarios
for the future provision
of the USO**



**Assess the impact on
net costs of USO**

1. Assess cost effects
2. Assess revenue effects
3. Assess effects on intangible benefits



**Assess impact on users,
employees and other
stakeholders**

Step 2: Assess the impact on net costs of USO

Net cost of the USO, 2016 Million EUR



| | Cost effect | Revenue effect | Value of intangible benefits | Net effect |
|----------------------------------|-------------|----------------|------------------------------|-------------|
| Delivery speed and frequency | 68 | - 56 | - | 12 |
| International mail | - | 73 | - | 73 |
| Delivery in the most rural areas | 42 | - 5 | - | 36 |
| Shipments for the blind | - | 2 | - | 2 |
| Reserved area | - | - | - 23 | - 23 |
| Total | 110 | 13 | - 23 | 100 |

Step 2: Assess the impact on net costs of USO

Counterfactual scenario, 2018 Million EUR

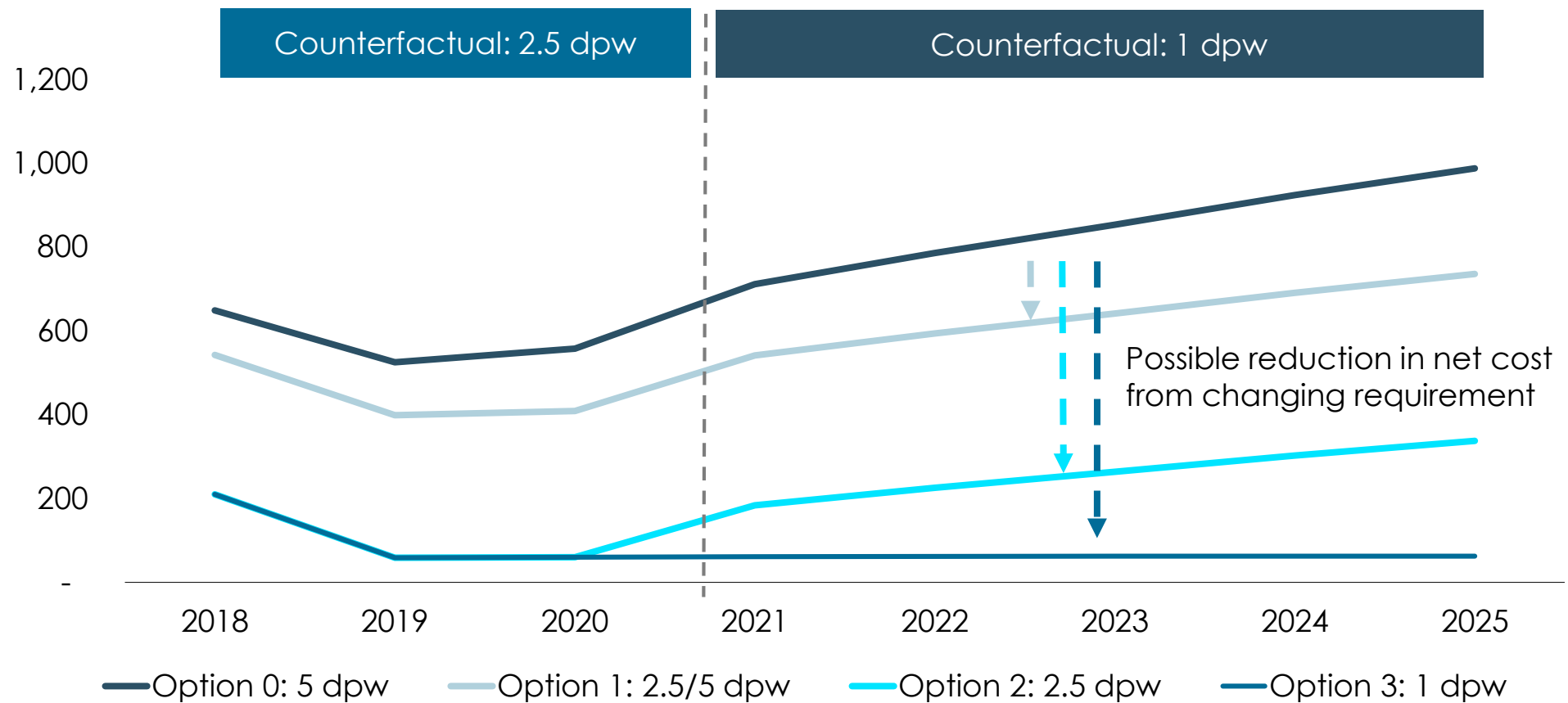


| | Net Cost 2018, MEUR (% of total) |
|--------------------------|----------------------------------|
| Delivery Speed | 16 (22%) |
| Delivery Frequency | 60 (70%) |
| International mail | 3 (5%) |
| Delivery to blind people | 2 (<3%) |
| Basic bank services | 1 (<3%) |
| Total | 73 |



Development of USO net costs largely depends on the delivery frequency

USO net costs (MNOK) 2018-2025



Roadmap to impact assessment



**Define potential scenarios
for the future provision
of the USO**



**Assess the impact on
net costs of USO**



**Assess impact on users,
employees and other
stakeholders**

1. Identify services affected
2. Identify vulnerable users
3. Identify targeted measures providing the best cost-benefit



Step 3: Assess impact on users and other stakeholders

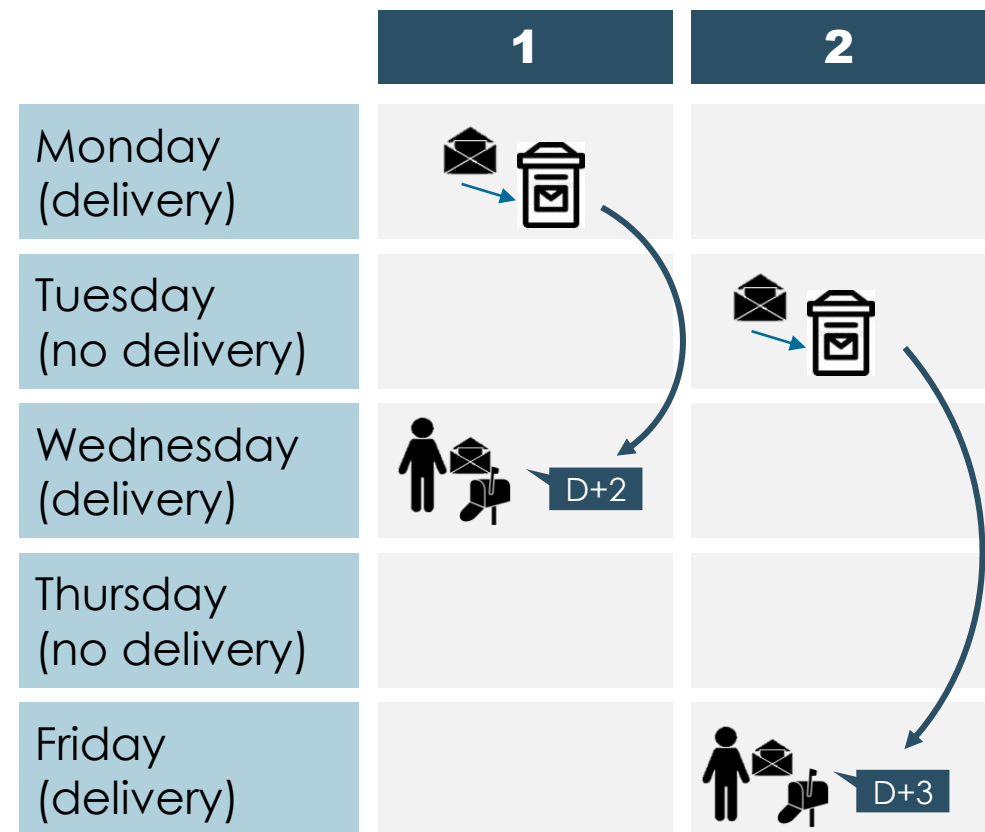
Clear international pattern regarding users most negatively affected by reduced delivery frequency:

- Elderly citizens,
- Citizens in rural areas,
- SMEs (primarily in rural areas)
- Other frequent senders of mail

Interviews to investigate in detail how different user groups are affected:

- Association for the blind
- Pensionist association
- Norwegian farmer association
- Industry association

Illustration of effects of delivery every second day





Some specific deliveries may be candidates for targeted measures



Newspapers

- Promote alternative technologies (tablet) or use of alternative networks (public transportation)
- Limited number of vulnerable users dependent on Posten for accessing news (conservative estimation)



Home delivery of medicines

- Monetary compensation (for express delivery) or use of alternative network (home care assistance)



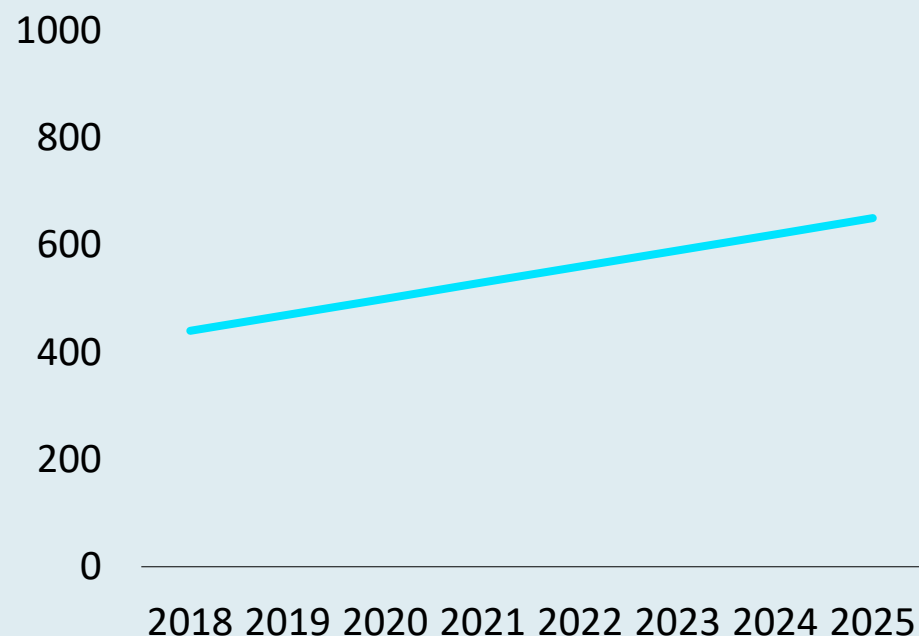
Urgent hospital notifications or invoices (at delivery 1 dpw)

- Electronically and express service



2.5 deliveries per week: Large cost savings will likely outweigh costs for targeted measures

440-650 MNOK reduction in net cost relative to status quo



Negative effect on some users in rural areas

- Negative effect on immobile/elderly citizens in rural areas
 - Difficulties to access existing alternative service offerings
- 2 critical services in rural areas w/o alternative networks
 - Delivery of newspapers to non-digital citizens
 - Urgent delivery of medicines to elderly and disabled citizens
- Limited number of vulnerable users

The full report is available online

Hyperlinks:

Main report

http://publications.europa.eu/publication/manifestation_identifier/PUB_ET0318267ENN

Country fiches

http://publications.europa.eu/publication/manifestation_identifier/PUB_ET0318268ENN



Q&A



THANK YOU!