

STUDY

Requested by the TRAN committee

Postal services in the EU



Transport and Tourism



RESEARCH FOR TRAN COMMITTEE

Postal services in the EU

Abstract

This study aims at providing the European Parliament's TRAN Committee with an overview of the EU postal services sector, including recent developments, and recommendations for EU policy-makers on how to further stimulate growth and competitiveness of the sector.

This document was requested by the European Parliament's Committee on Transport and Tourism.

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LIST OF ABBREVIATIONS

AGCOM	Autorità per le Garanzie nelle Comunicazioni, regulator for the communication industries in Italy
An Post	Universal service provider in Ireland
AT	Austria
Austrian Post	Universal service provider in Austria
B2B	Business-to-business
B2C	Business-to-consumer
B2G	Business-to-government
B2X	Business-to-consumer/business/government
BE	Belgium
BG	Bulgaria
bpost	Universal service provider in Belgium
Bulgarian Post	Universal service provider Bulgaria
C2B	Consumer-to-business
C2C	Consumer-to-consumer
C2G	Consumer-to-government
C2X	Consumer-to-consumer/business/government
CLA	Collective Labor Agreements
Correos	Universal service provider in Spain
CTT	Universal service provider in Portugal
CY	Cyprus
Cyprus Post	Universal service provider in Cyprus
CZ	Czech Republic
Czech Post	Universal service provider in the Czech Republic
D+1	Routing time where mail is delivered the first working day after posting
D+2	Routing time where mail is delivered the second working day after posting
D+3	Routing time where mail is delivered the third working day after posting
D+4	Routing time where mail is delivered the fourth working day after posting
D+5	Routing time where mail is delivered the fifth working day after posting
DE	Germany
Deutsche Post	Universal service provider in Germany
DK	Denmark

DKK	Danish kroner
EBIT	Earnings Before Interest and Taxes
EE	Estonia
EL	Greece
ELTA	Universal service provider in Greece
ERGP	The European Regulators Group for Postal Services
ES	Spain
EU	European Union
EUR	Euro
FedEx	Federal Express (Courier company)
FI	Finland
FR	France
G2B	Government-to-business
G2C	Government-to-consumer
G2X	Government-to-consumer/business
GDP	Gross Domestic Product
GDPR	General Data Protection Regulation
HR	Croatia
Hrvastke Poste	Universal service provider in Croatia
HU	Hungary
IE	Ireland
IT	Italy
La Poste	Universal service provider in France
Latvijas Pasts	Universal service provider in Latvia
Lietuvos Paštas	Universal service provider in Lithuania
LT	Lithuania
LU	Luxembourg
LV	Latvia
Magyar Posta	Universal service provider in Hungary
Malta Post	Universal service provider in Malta
MFA	Multi frequency analysis
MT	Malta
NL	Netherlands
NRA	National Regulatory Authority

Omniva	Universal service provider in Estonia
Österreichische Post	Universal service provider in Austria
PL	Poland
Poczta Polska	Universal service provider in Poland
Post Luxembourg	Universal service provider in Luxembourg
Poșta Română	Universal service provider in Romania
Posta Slovenije	Universal service provider in Slovenia
Poste Italiane	Universal service provider in Italy
Posti	Universal service provider in Finland
PostNL	Universal service provider in the Netherlands
PostNord	Universal service provider in Denmark
PostNord	Universal service provider in Sweden
PSD	Postal Service Directive
PT	Portugal
PUDO	Pick-Up Drop-Off
RFID	Radio Frequency Identification
RO	Romania
Royal Mail	Universal service provider in the United Kingdom
SE	Sweden
SGEI	Services of General Economic Interest
SI	Slovenia
SK	Slovakia
Slovenská Pošta	Universal service provider in Slovakia
TNT	International courier delivery company, subsidiary of FedEx
UK	United Kingdom
UPS	United Parcel Service, a logistic delivery company
UPU	Universal Postal Union
USO	Universal Service Obligation
USP	Universal Service Provider
VAT	Value Added Tax

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EXECUTIVE SUMMARY

KEY FINDINGS

- The EU postal and delivery sector is significant to the EU economy, but should not be taken for granted, given the important transformations it is going through.
- Digitalisation has been dictating the main transformations of the postal sector in recent years, leading to a decrease in letter post volumes and an increase in e-commerce parcels.
- In response to the developments of the EU postal sector, postal operators have been innovating their business models and national postal regulations have changed substantially.
- To ensure that there is a viable postal operator going forward, the postal regulatory paradigm must be kept in sync with changing market realities, shifting the priority of policies from the promotion of competition to the sustainability of the sector, accounting for national market realities.

EU postal sector main developments

The postal and delivery sector is generating revenue of EUR 79 billion per year¹ and employing around 1.7 million people across the EU².

At the same time, the postal industry is being disrupted by technological developments. Digital transformation is affecting the postal sector on two fronts. On one side, digital means of communication are replacing paper-based ones³, decreasing the demand for letters. On the other side, the possibility of shopping online and having goods delivered is increasing the demand for parcels and packets.

These contrasting pressures underpin different challenges for all stakeholders in the postal sector. Whereas the decline in the volume of letters has created challenges for the postal sector and continues to drive changes, the growing e-commerce industry creates new opportunities and demands for the postal sector to respond to and to minimise the negative impact of the decline in the volume of letters⁴.

The competitive landscape of the EU postal sector is evolving as a consequence of the digital transformation. The letter segment is still highly concentrated, but is shrinking overall, as digital communication alternatives compete with letter post products.

The situation in the parcel segment is different: markets are fragmented, universal service providers' (USPs') shares of deliveries are relatively low, and new delivery players enter the parcel segment, challenging incumbents' business models and profitability.

¹ Data for 2017.

² Data for 2018.

³ The so-called "e-substitution".

⁴ Copenhagen Economics (2018), Main Developments in the Postal Sector 2013-2016.

At the same time, more attention is paid to the impact of industries on the environment. The postal sector is an important stakeholder in driving carbon efficiency, although its net impact on the environment has not been appraised in a facts-based analytical manner.

In response to these developments and due to declining profitability, postal operators are in a phase of transformation. They increasingly provide new services and products and use new business models, including more efficient technologies, environmentally friendly ways of transportation, and new employment contracts.

In several instances, digital transformation has also called for substantial changes in postal regulation.

EU postal sector policy debates and responses

Market developments vary across countries and over the past decade we have seen three main trends in policy debates and responses in the various Member States and at the EU level.

First, the financial viability of the USPs comes under pressure because the growth in the parcel segment does not outweigh the decline in revenue for letters for most USPs. The policy debate considers whether this requires a fundamental change in the prioritisation of policy objectives, and usually evolves in two stages. First, reduce the burden of the Universal Service Obligation (USO) by giving the USP more operational and/or pricing flexibility. Second, shift the prioritisation of the policy objectives from stimulating competition to the sustainability of the USO.

Second, changing user needs have challenged the role of the USO. The policy debate evolves around what the appropriate scope of state intervention in the postal sector is, questioning what the needs are that the market cannot meet, and whether there are any new needs that emerge.

Third, with the increase in cross-border e-commerce shipments, policy-makers are debating whether and how to adapt regulatory frameworks to ensure an efficient cross-border parcel delivery. This policy debate considers international postal regulations and non-postal regulations impacting the postal sector, such as rules on transportation and customs procedures.

Challenges and opportunities for the EU postal sector

The transformations in the EU postal sector create challenges and opportunities. On the one hand, the EU postal sector faces many challenges that make it fragile:

- The sector is transforming at a different pace in each of the Member States, making it challenging to regulate and impossible to apply a one-size-fits-all solution. At the same time, the needs of postal users are changing, questioning the scope of the USO.
- Changing the USO raises the challenge of how to safeguard consumers who might still need access to basic postal services and who should pay for it.
- The postal sector's network is still made up of people, as opposed to sectors such as telecoms, meaning that (1) if its sustainability is not viable it cannot be resold to the next buyer, and (2) it will be a challenge to shift the postal workforce to other jobs.
- Different delivery operators are subject to different rules and exemptions, such as customs, VAT, transport rules and State funding. At the same time, the EU postal sector faces pressures from outside the EU and from other sectors' regulations, such as environmental targets and employment conditions, raising the challenge of creating a level playing field.

On the other hand, the EU postal sector can reap the opportunities that arise:

- Growing e-commerce increases the demand for packets and parcels delivery, representing an opportunity for postal operators to increase profits.
- The value of the USPs' network and brand can be used to provide other commercial services, e.g. banking, and publicly-relevant services on behalf of the Member State, in a more efficient way than the Member State would itself.
- Finally, new operational technologies, e.g. robotics, can improve postal operators' efficiency without sacrificing service quality.

Recommendations for EU postal policy-makers

Based on the developments analysed, we propose three main recommendations for EU postal policy-makers both at national and EU level.

First, provide flexibility to ensure a sustainable USO and define its role in light of changing user needs. Changing user needs and developments in the EU postal sector have an impact on the sustainability of the USO and challenge its role in the society. Furthermore, different Member States experience these developments and challenges at different pace. Some countries have displayed a steep decline in the volume of letters and extensive e-government use, e.g. Denmark, while others have had a more stable volume of letter post development, e.g. Germany.

Consequently, policies at EU level should provide flexibility for Member States to design postal policies at national level. These may include reviewing and reducing the scope of the USO where needed. Moreover, policies at EU and national level should provide more flexibility to USPs on how to provide and price the USO.

Furthermore, we expect that State Aid rules will play an important role in securing the sustainability of universal postal services. In this regard, State aid rules should ensure a speedy provision of funds, given the high pace of change of the postal sector, without harming competing non-USP operators.

Second, mind the impact on the environment and social conditions when designing postal policies. Postal policies can (i) be a driver of the environmental footprint and (ii) have an impact on social conditions. (i) USO requirements may increase the environmental impact per postal item if they require the USP to offer other services or structure its operations differently than it would have done without the USO. (ii) Policies that promote competition as the main focus may encourage the entry of players that offer poor conditions to their postal workers.

Consequently, the impact on the environment and social conditions should be considered and measured when designing postal policies.

Third, create an international level playing field for the EU postal and e-commerce sector. Beside EU and national postal regulations, the EU postal sector has to comply with global postal regulations⁵ and policies external to the postal sector⁶. These policies might constrain the EU postal sector's profitability and impact social welfare:

⁵ Such as the Universal Postal Union (UPU) system for terminal dues.

⁶ Such as transport and taxation regulations.

- (i) Assessing the EU-wide impact of the significant reforms introduced to the UPU terminal dues system, as well as a future united position of EU Member States in the UPU is likely to bring a better understanding on how to protect EU consumers' needs and provide a stronger negotiating position.
- (ii) It should be ensured that any exemptions granted to USPs in transportation regulations, VAT, and customs procedures are economically justified and do not harm competing postal operators. Also, it is important to ensure that differences in national policies do not create unfair competition and degradation of social conditions within the EU.
- (iii) It should be ensured that any regulations in related areas do not create barriers for innovation and development of new technologies and services.

1. MAIN DEVELOPMENTS IN THE EU POSTAL SECTOR

KEY FINDINGS

The EU postal and delivery sector is an important sector and is significant to the EU economy. At the same time, the sector is going through important transformations in terms of:

- digitalisation: more users communicating digitally and shopping online;
- change in product mix: a decline of volumes in letter post and an increase in parcel volumes;
- changes in the competitive landscape: digital communication alternatives competing with letter post products and new delivery players entering the parcel segment;
- more focus on the environment: the postal sector is an important stakeholder in driving carbon efficiency and its net impact on the environment has not been appraised;
- transformation of postal operators: postal operators providing new services, using more efficient technologies and transforming their business models.

Copenhagen Economics has been commissioned by the European Parliament's Committee on Transport and Tourism (TRAN) to conduct a study on "Postal services in the EU", which fall under the remit of the TRAN Committee.

The main objective of the study is to provide the TRAN Committee with an overview of the status quo, future challenges and emerging opportunities for the European postal services sector. In particular, by describing the current status of the postal services sector in the EU, including the main developments and trends relevant to EU policies concerning postal services, and providing recommendations for EU policy-makers on what could be done at EU level to further stimulate growth and competitiveness of the sector.

The project has relied extensively on the sector expertise of the team at Copenhagen Economics, on past postal sector studies, as well as interviews and case studies from different postal sector stakeholders. We are grateful for the support and interest we have received from all the different stakeholders and for the constructive discussion with the project team at the Policy Department for Structural and Cohesion Policies of the European Parliament.

The study is structured around four chapters. In the first chapter we provide an overview of the postal services sector in the EU, including the current status and the main developments and trends we have seen in recent years. The second chapter presents important policy debates and responses in the EU postal sector. The third chapter draws from the previous two to identify the main challenges and opportunities that the sector faces. Finally, the fourth chapter provides recommendations for EU postal policy-makers.

1.1. The postal and delivery sector is significant to the EU economy

The EU postal and delivery sector contributes to the economy of the Union in various ways:

- the sector generates revenues of EUR 79 billion per year, which corresponds to 0.5 per cent of the EU's total GDP;⁷

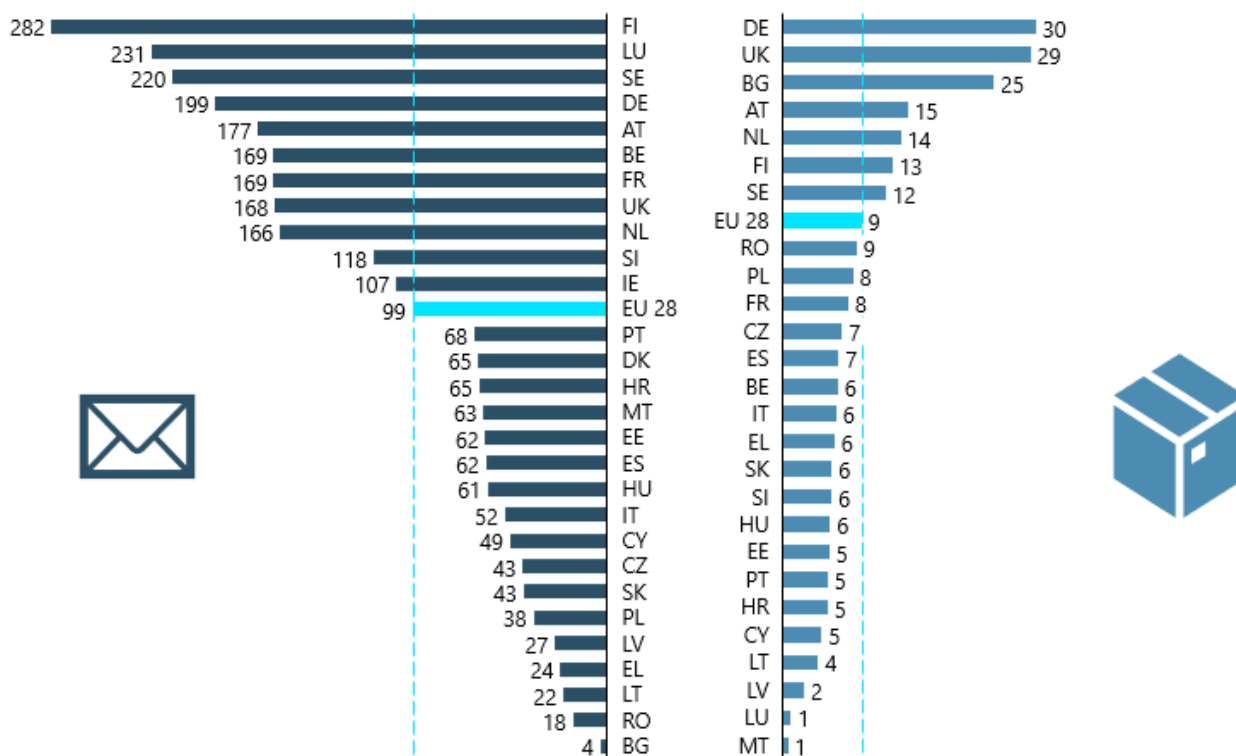
⁷ Revenue and GDP data for 2017, for EU28 excluding Finland and Romania. Sources: Data from European Commission *DG GROW statistics* accessed on 16/07/2019 (https://webgate.ec.europa.eu/grow/redisstat/databrowser/view/POST_CUBE1_XSPOST_FIN_1/default/table?category=GROW_CURRENT); Eurostat, [*nama_10_gdp*], accessed on 16/07/2019; Copenhagen Economics (2018), *Main Developments in the Postal Sector 2013-2016*.

- the postal and delivery sector employs around 1.7 million people across the EU, corresponding to 0.8 per cent of the employed population.⁸ The incumbent postal operators (universal service providers, see Section 1.1.1) are usually one of the biggest employers in their countries;
- the postal and delivery sector is an enabler of e-commerce domestically, intra-EU and globally – a fast growing industry in Europe and currently worth EUR 344 billion;
- the postal and delivery sector also plays an important role in some niche segments, e.g. in the delivery of medications in rural areas or to elderly people, as done by La Poste in France;
- many players are active in the postal and delivery sector in the EU. They include the universal service providers, competing providers active in the letter delivery business, logistics and express providers (e.g. UPS and FedEx), and alternative delivery operators (e.g. Amazon).

In 2017, 99 letters and 9 parcels per capita were delivered on average in EU Member States, see Figure 1. However, the demand for letter post and parcel services at national level varies significantly across Member States.⁹

Figure 1: The size of the letter post and parcel sectors by country, 2017

Items per capita



Note: The figure includes total volumes for domestic letter mail services and parcel services. Letter volumes for DK, EE, IE, NL, SK, SI, and parcel volumes for EE, NL, SK, SI, are from 2016

Source: European Commission, *Data for 2017 from European Commission DG GROW statistics accessed on 16/07/2019* ([https://webgate.ec.europa.eu/grow/redisstat/databrowser/view/POST_CUBE1_X\\$POST_DTR_1/default/table?category=GROW_CURRENT](https://webgate.ec.europa.eu/grow/redisstat/databrowser/view/POST_CUBE1_X$POST_DTR_1/default/table?category=GROW_CURRENT)); data for 2016 from *Copenhagen Economics (2018), Main Developments in the Postal Sector 2013-2016*

⁸ Data for 2018. The number of people employed in the postal and delivery sector in the EU decreased by 0.11 per cent compared to 2017. Source: Eurostat, *[lfsa_eqa22d] Postal and courier activities*, (accessed, 24 Jul 2019); Eurostat, *[lfsi_emp_a] Total employment by sex and age*, (accessed, 24 Jul 2019).

⁹ See the Figure 2 for a classification of mail products.

1.1.1. The EU postal sector is subject to the universal service obligation

In order to understand the regulation and the functioning of the postal sector, it is important to understand that universal service obligations play a key role in how national postal operators can run their business.

To ensure that a basic level of postal services is provided on equal terms for all citizens, governments across the world impose a so-called Universal Service Obligation on providers of postal services. The postal USO entails certain requirements, such as the obligation to collect and deliver specific types of postal items, collect and deliver mail a specific number of days per week, ensure that prices for sending mail are affordable and uniform across the country, and that mailings arrive within a certain number of days after being posted. The obligation to provide some postal services through the USO aims at covering a social need that would otherwise not be covered by the market on commercial terms, absent regulation.

The provider of the USO in a given country is called a Universal Service Provider and is usually designated by the national government (the process of designation of the USP varies by country, and in some countries the provision of the USO is tendered, e.g. in Poland).

In the EU, the Postal Services Directive¹⁰ sets minimum requirements (although subject to certain exceptions) for the providers of the USO. The elements of the USO have been unchanged since 1997, but each Member State is free to choose the precise scope and size of the USO at a national level, as long as it fulfils the minimum requirements set out in the Postal Services Directive. The minimum requirements set by the Postal Services Directive are the following:

- one collection per day from appropriate access points;
- one delivery per day to all addresses or to appropriate installations;
- collection from access points and delivery every working day and not less than five working days per week;
- according to Annex II of the Postal Services Directive, 85 per cent of intra-community cross-border mail must be delivered within D+3.

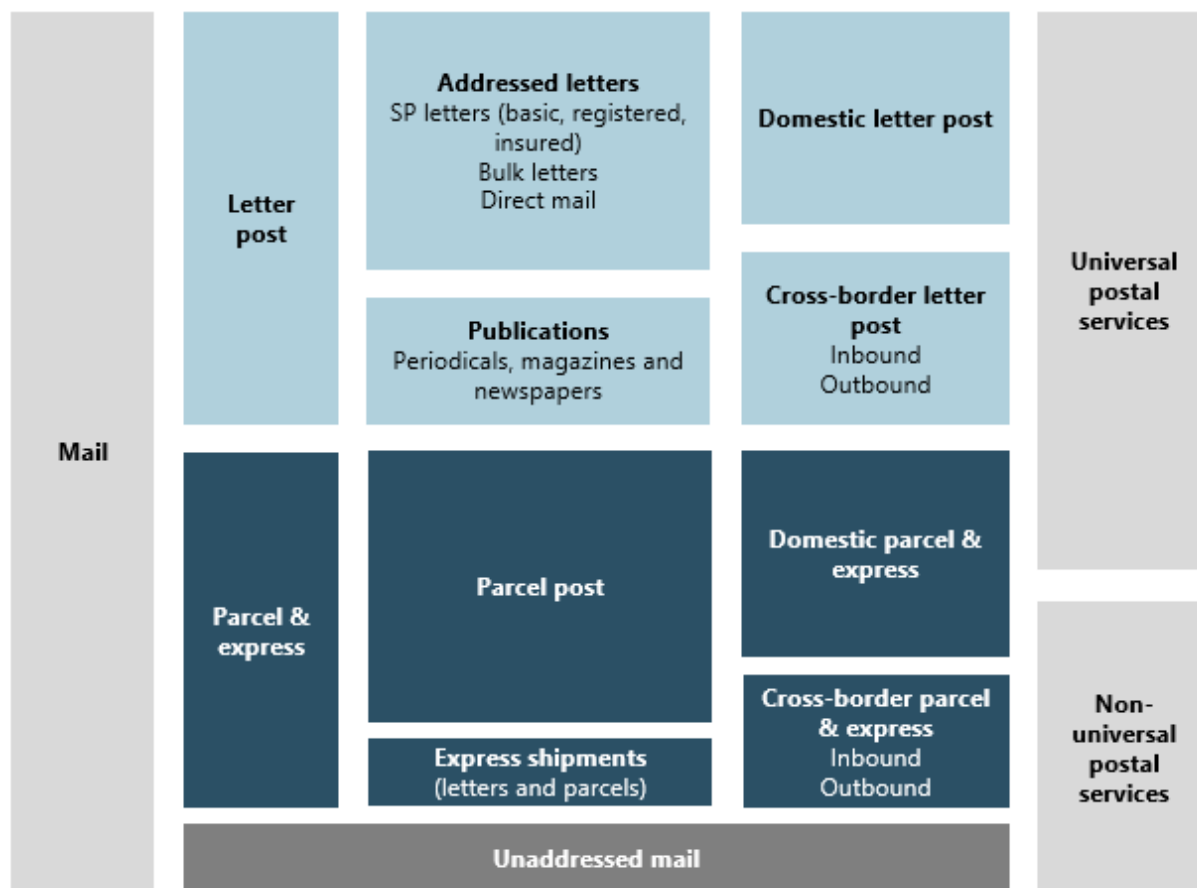
The Postal Services Directive also determines a minimum set of postal products/services:

- postal items up to 2 kilograms;
- postal parcels up to 10 kilograms;
- services for registered and insured items.

Above this minimum level Member States have flexibility to decide what exactly constitutes a universal service in terms of postal products and requirements, e.g. frequency of delivery, to fit their domestic circumstances. Postal services comprise different products, that can be classified in different categories, see Figure 2.

¹⁰ European Commission (2008), *Directive 2008/6/EC*.

Figure 2: Postal services classification



Source: Copenhagen Economics

The product scope of the USO and the product specifications (speed and weight) vary by Member States, see Table 1.

Besides the Postal Services Directive, the EU VAT Directive¹¹ also applies to some USO products (see Table 1) exempting them from the value-added tax (VAT) as activities provided in the public interest. The presence of VAT exemption for certain postal services has often been motivated by consumer protection, since the burden of VAT, which is a consumption tax, falls on the end-user.

¹¹ European Commission (2006), *Council Directive 2006/112/EC*.

Table 1: Product scope of the USO and VAT exemption, 2018

	First-class letter, domestic	Second-class letter, domestic	Bulk letters	Basic parcel (domestic)	Bulk parcels	Cross-border letter post	Cross-border parcels
AT	D+1, 2kg	D+4, 2kg	2kg	10kg	10kg	2kg	10kg
BE	D+1, 2kg		2kg	10kg		2kg	20kg
BG	D+1, 2kg	D+2, 2kg		20kg		2kg	20kg
HR	D+1, 2kg	D+3, 2kg		10kg		2kg	10kg out, 20kg in
CY	D+1, 2kg	D+3, 2kg	2kg	20kg		2kg	20kg
CZ	D+1, 2kg			10kg		2kg	10kg out, 20kg in
DK	D+5, 2kg			20kg		2kg	20kg
EE	D+1, 2kg			20kg		2kg	20kg
FI	D+4, 2kg			10kg		2kg	10kg out, 20kg in
FR	D+1, 2kg	D+2, 250g	2kg	20kg		2kg	20kg
DE	D+1, 2kg		2kg	20kg	20kg	n/a	n/a
EL	D+1, 2kg	D+3, 2kg	2kg	20kg	20kg	2kg	20kg
HU	D+1, 2kg	D+3, 2kg	2kg	20kg	20kg	2kg	40kg
IE	D+1, 100g		100g	20kg		100g	20kg
IT	D+1, 2kg	D+4, 2kg	2kg	20kg		2kg	20kg
LV	D+1, 2kg	D+3, 2kg	2kg	20kg			20kg
LT	D+1, 2kg	D+2, 2kg		50kg		2kg	20kg
LU	D+3, 2kg		2kg	10kg	10kg	20kg	20kg
MT	D+1, 2kg		2kg	20kg	20kg	2kg	20kg
NL	D+1, 2kg			20kg		2kg	20kg
PL	D+1, 2kg	D+2, 2kg		10kg		2kg	20kg
PT	D+1, 2kg	D+3, 2kg	2kg	10kg	10kg	n/a	20kg
RO	D+1, 2kg	D+2, 2kg		10kg		10-20kg	10-20kg
SK	D+1, 2kg	D+2, 2kg	2kg	10kg	10kg	2kg	10kg
SI	D+1, 2kg			10kg		2kg	10kg
ES	D+3, 2kg		2kg	20kg	20kg	2kg	20kg
SE	D+2	D+3					
UK	D+1, 750g	D+3, 750g		20kg		750g	2kg

Note: First-class is the fastest letter product available. Second-class is the letter product that is slower than first-class. Blue cells mean the product is defined as universal service by law and falls within the scope of VAT exemption. Light grey cells mean the product is defined as universal service by law only. Empty cells mean the product is outside the USO scope. The weight indicated is the upper weight limit. Cells with "n/a" mean no answer was given. Weights separated by comma refer to two possible limits. Weights separated by "-" refer to an interval. Weights with "out" refer to outbound products, "in" to inbound. DK – bulk parcels are in theory VAT exempted, but not in practice, see discussion in the Danish Parliament (<http://dtl.eu/presserum/nyheder/nyhedsarkiv-2012-2018/2017/skatteminister-momsfritagelse-af-post-danmarks-pakker-var-uhjemlet/>). FI - Cross-border parcels obligation only for parcels sent abroad. LT - upper weight limit for non-EU inbound and outbound parcels is 10kg. PT - cross-border parcels from EU. ES - bulk letters part of the USO de facto. SE – domestic second-class letter and bulk letters are part of USO de facto. UK - cross-border parcels may be under USO up to 5kg for certain destinations if the parcel contains printed materials/ books

Source: Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*

1.1.2. International postal and non-postal regulations govern postal flows

Beside national postal laws and regulations, the EU postal sector is governed by international postal regulations and regulations stemming from other sectors. Some of these regulations have raised debates in recent years, as further discussed in Chapter 2.

a. Postal regulations on cross-border mail flows

Cross-border letter and parcel services within the EU are subject to different postal regulations.

First, the Postal Services Directive regulates cross-border letters sent between Member States. The Directive states that 85 per cent of cross-border letter mail is to be delivered within three days.¹²

However, the performance is challenged by the declining volume in letters, which make it difficult for postal operators to maintain the high quality service requirements. In the last three years the performance of cross-border letter post within the EU has been below the objective set in the Postal Services Directive, with 83.2 per cent, 79.5 per cent and 78.7 per cent of cross-border letter post delivered within three days in 2016, 2017 and 2018 respectively.¹³

Second, the EU Regulation 2018/644 regulates cross-border parcel delivery within the EU. Cross-border parcel delivery services have been increasingly important in recent years, due to the increase in e-commerce. However, high prices and the inconveniences of cross-border parcel delivery were identified as some of the main obstacles to enhance e-commerce among European consumers and retailers. In response to these challenges, the EU Regulation 2018/644 entered into force in May 2018 with the purpose of increasing transparency of cross-border parcel delivery services in the EU.¹⁴ The regulation requires parcel delivery providers to provide information about products, market data, prices and quality of services to the EU postal regulators, who in this way gain further authority to collect data about parcel delivery services provided nationally. The impact of this regulation remains to be seen, since it has only entered into force very recently.

Finally, the Universal Postal Union system for terminal dues regulates cross-border postal services between designated operators worldwide. We discuss this further in Section 2.3.1.

b. Non-postal regulations apply to EU postal operators

EU postal operators are subject to other, non-postal regulations, such as transport rules, customs procedures, aviation sector regulations, VAT rules, etc.

Policy debates have been evolving around the impact of non-postal rules on EU postal operators, as we discuss further in Section 2.3.3.

1.2. Digital communication is transforming the postal industry

The postal industry is not immune to technological disruption. In fact, it is probably one of the industries that is affected the most. Digital transformation is affecting the postal sector on two fronts. On one side, digital means of communication are replacing paper-based ones (the so-called “e-substitution”), decreasing the demand for letters. On the other side, the possibility of shopping online and getting goods delivered is increasing the demand for parcels and packets.

1.2.1. E-substitution and development of letter post volumes

E-substitution happens when electronic means of communication replace traditional letter post communication. For example, when banks send monthly statements through online banking instead of sending a paper copy via post. As a consequence of this trend, demand for letter post decreases.

Businesses and public entities have historically been the biggest senders of letter post, to communicate among themselves and with citizens. However, the possibility for businesses and citizens to

¹² European Commission (2008), *Directive 2008/6/EC*, as stated in European Commission (1997), *Directive 97/67/EC*, Annex.

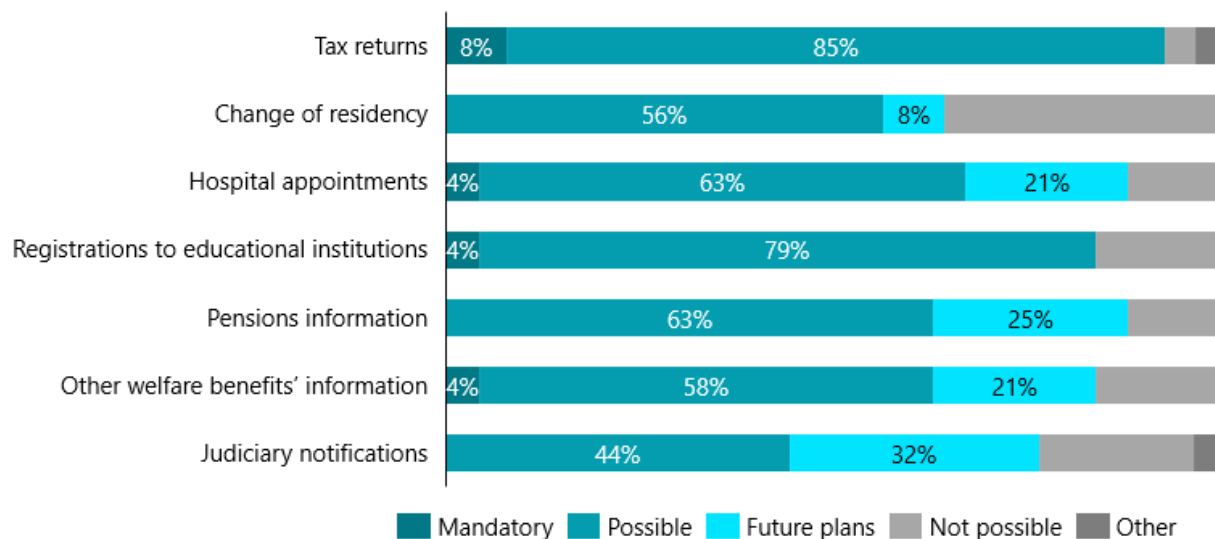
¹³ IPC (2018), *International Mail Quality of Service Monitoring*.

¹⁴ Regulation (EU) 2018/644 (https://ec.europa.eu/growth/sectors/postal-services/parcel-delivery_en).

communicate electronically with government institutions is quickly becoming commonplace in many Member States. Almost all main communications with the public sector can be conducted electronically in the majority of Member States and future plans exist in several of the other countries, see Figure 3.

Figure 3: Electronic communication with public institutions, 2018

Share of countries



Note: The chart contains data from the EU28 countries

Source: Copenhagen Economics based on Copenhagen Economics (2018), *Main Developments in the Postal Sector 2013-2016*

The speed and extent of e-substitution still varies across countries, depending on the willingness of users to substitute from traditional letter post to electronic communication and on the convenience of doing so, e.g. given different technological conditions (broadband penetration, use of the internet at home, etc.) and policy conditions (requirements on digital vs physical communication with public authorities). The government and its plans to digitalize processes (e.g. e-voting) and communication (e.g. digital interaction with the government) play an important role in the development of e-substitution.

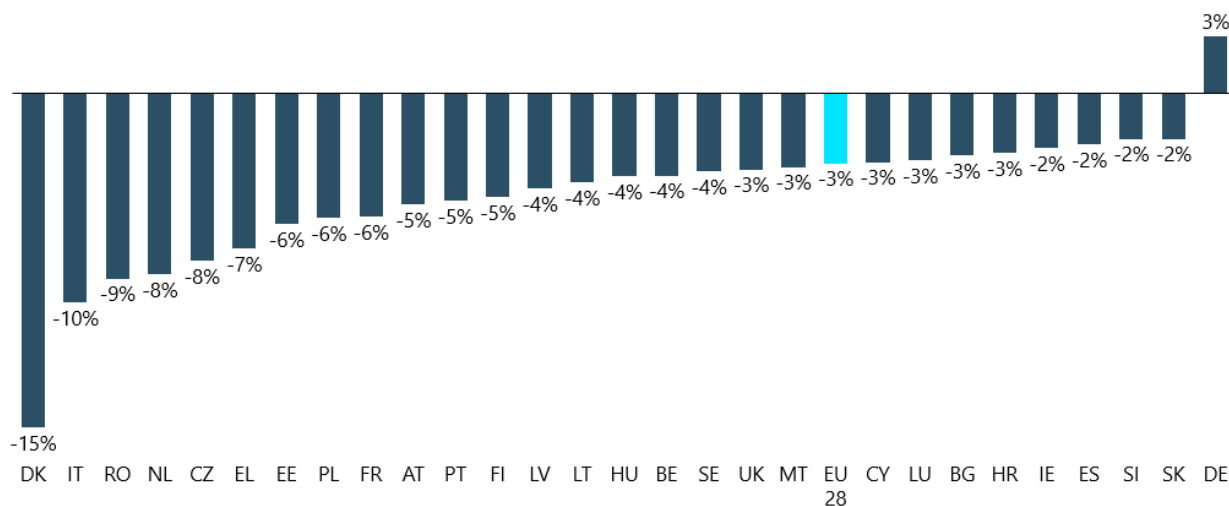
Denmark represents the most prominent case of e-substitution. The strong digitalization of communication with the government (e-government), mandatory since 2014, caused the steepest volume decline in the EU. Volumes for the basic letter product in Denmark declined by 93 per cent from 2010 to 2017.¹⁵

Other Member States have experienced different degrees of e-substitution and letter post volume decline in recent years. In the EU, letter post volumes declined on average by 3 per cent annually, see Figure 4. Germany is an exception where, primarily due to digital security concerns, letter post is still one of the main official channels of communication between citizens, government and businesses.

¹⁵ PostNord, *annual reports*.

Figure 4: Development of domestic letter post volume by country

Annual change in 2013-2017



Note: Data for DK, EE, FI, IE, NL, SK, SI is for 2013-2016. The EU 28 average is calculated as the annual change of total EU 28 countries volumes between 2013 and 2017. Since for DK, EE, FI, IE, NL, SK and SI we use 2016 volumes, the average annual change for EU 28 slightly underestimates the actual decline.

Source: European Commission, DG GROW statistics accessed on 16/07/2019

([https://webgate.ec.europa.eu/grow/redisstat/databrowser/view/POST_CUBE1_X\\$POST_DTR_1/default/table?category=GROW_CURRENT](https://webgate.ec.europa.eu/grow/redisstat/databrowser/view/POST_CUBE1_X$POST_DTR_1/default/table?category=GROW_CURRENT)) and Copenhagen Economics (2018), *Main Developments in the Postal Sector 2013-2016*

1.2.2. E-commerce and development of parcels volumes

Digital innovation has also opened the possibility for consumers to shop online. The e-commerce segment in Europe is currently worth EUR 344 billion,¹⁶ with 69 per cent of European internet users shopping online in 2018.¹⁷

The B2C e-commerce sector in the EU has been growing, with more consumers shopping online, making more of their purchases online and more frequently.

As a consequence of the increased e-commerce, volumes of parcels, express items and packets¹⁸ have been growing throughout Europe, both domestically and cross-border.

Domestically, parcel and express volumes have been growing by an average ten per cent per year between 2013 and 2017, see Figure 5.

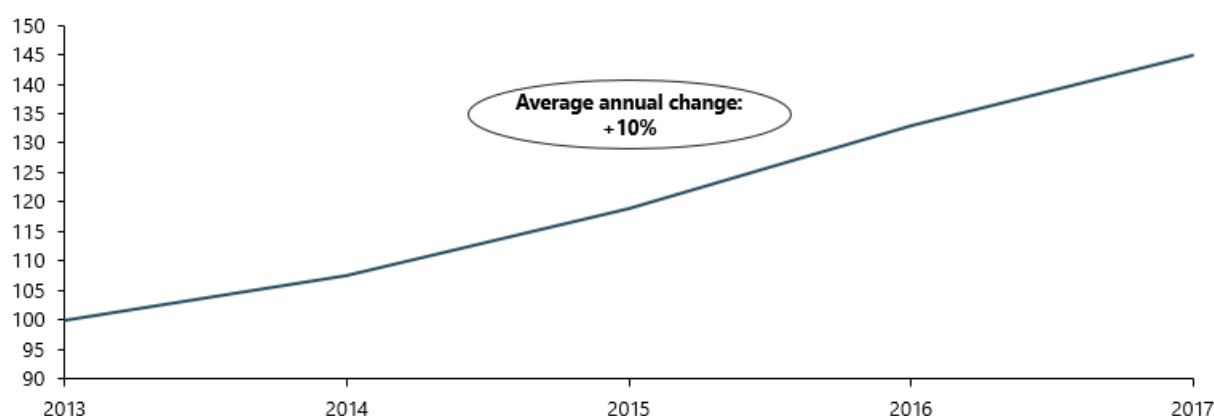
¹⁶ Data for 2019, source: <https://www.statista.com/outlook/243/102/ecommerce/europe?currency=eur>.

¹⁷ https://ec.europa.eu/eurostat/statistics-explained/index.php/E-commerce_statistics_for_individuals#E-shopping:_biggest_increase_among_young_internet_users.

¹⁸ Packets are bulky letters weighing less than 2 kg, as defined by the Universal Postal Union, and usually delivered by USPs.

Figure 5: Evolution of parcel & express services volumes, domestic, 2013-2017

Index (2013=100)



Note: Includes EU28 countries, except for IE and RO

Source: European Commission, DG GROW statistics accessed on 16/07/2019

([https://webgate.ec.europa.eu/grow/redisstat/databrowser/view/POST_CUBE1_X\\$POST_DTR_1/default/table?category=GROW_CURRENT](https://webgate.ec.europa.eu/grow/redisstat/databrowser/view/POST_CUBE1_X$POST_DTR_1/default/table?category=GROW_CURRENT)) and Copenhagen Economics (2018), *Main Developments in the Postal Sector 2013-2016* and Bundesnetzagentur (2019), *Annual report 2018 – 20 years of responsibility for networks*

The growth of shipments was faster cross-border than domestically.¹⁹ International shipping in Europe was worth more than EUR 16 billion in 2016, comprising 720 million items²⁰, and this number is expected to reach more than 900 million items by 2019.²¹

Small packets account for a growing share of cross-border shipments. The share of small packets in cross-border letter post increased from 11 per cent in 2005 to 18 per cent in 2015, mainly driven by B2C e-commerce.²²

Delivery companies are benefitting from this development and today's most successful USPs are those that have successfully mitigated letter volume decline and taken advantage of the growing e-commerce business domestically and/or internationally.

It should be mentioned that numbers regarding cross-border flows need to be taken with a pinch of salt, since there are no accurate statistics about cross-border deliveries in Europe and the published data often underestimates the actual volumes, excluding e.g. parcels resulting from direct injection, i.e. when mail is transported as cargo from one country to another country and then deposited locally as domestic mail^{23, 24}

¹⁹ WIK (2019), *Report on Development of Cross-border E-commerce through Parcel Delivery*, A study for the European Commission.

²⁰ Estimates based on 13 European countries including Russia.

²¹ WIK (2019), *Report on Development of Cross-border E-commerce through Parcel Delivery*, A study for the European Commission, based on AT Kearney.

²² UPU (2016), *Research on Postal Markets, Trends and Drivers for International Letter Mail, Parcels and Express Mail Services*.

²³ An example is Amazon's use of warehouses in Poland and the Czech Republic to deliver orders in Germany. These deliveries to German customers are not reflected in any official statistics.

²⁴ WIK (2019), *Report on Development of Cross-border E-commerce through Parcel Delivery*, A study for the European Commission.

1.3. The competitive landscape is evolving

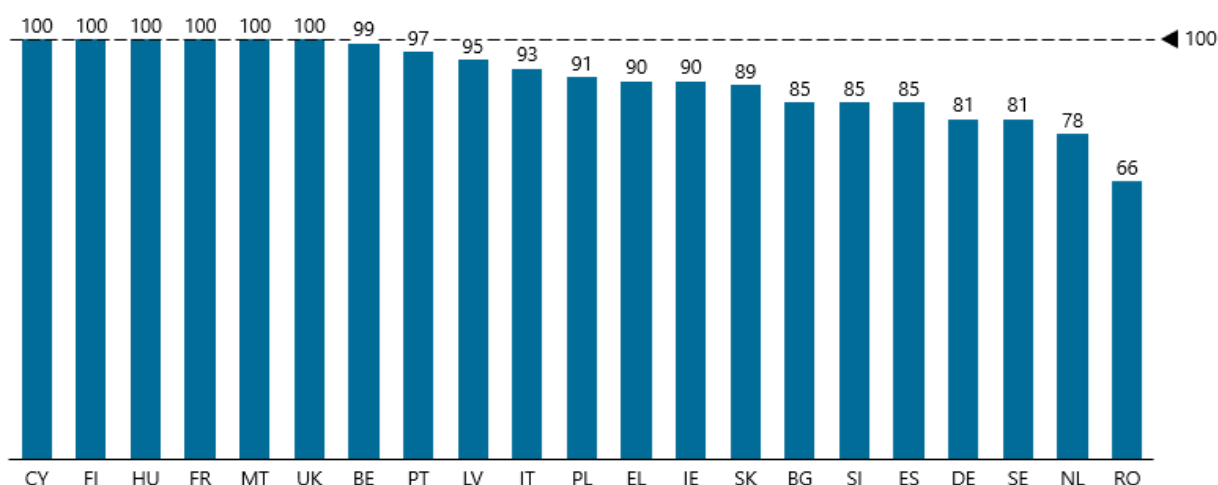
The digital transformation described above impacts the competitive landscape of the EU postal sector, bringing new players into the traditionally concentrated segments and forcing incumbents to innovate.

1.3.1. Competition on letter delivery

EU letter segments are still concentrated, with the universal service providers accounting for a high share of the domestic letter delivery segment, see Figure 6.

Figure 6: Incumbent’s share of domestic addressed letter deliveries in 2016

Per cent



Note: The shares are approximations based on volumes and they refer to different types of competition: end-to-end, i.e. a competitor with a fully developed delivery network, from pick-up to drop-off, or upstream, i.e. a competitor that collects mail but then utilises the incumbent’s delivery network for the last-mile, therefore using downstream access. SI - downstream access. UK – downstream access; access operators accounted for 61 per cent addressed letters volumes. BG, FI, IE, MT, SI - based on SP letters segment. FR - based on SP and bulk mail segments. IT, LV, PT, EL, PL, SK, BG, ES, DE, SE, NL, RO – have end-to-end competition. AT, BE, HR, CZ, DK, EE, LT - confidential information. ES - data for addressed items includes addressed and unaddressed

Source: Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*

However, USPs face strong competition from digital alternatives, such as e-mail, certified e-mail and online banking. Digital competition disciplines incumbents’ pricing and forces them to be innovative and efficient and to diversify their activity, see Section 1.5.

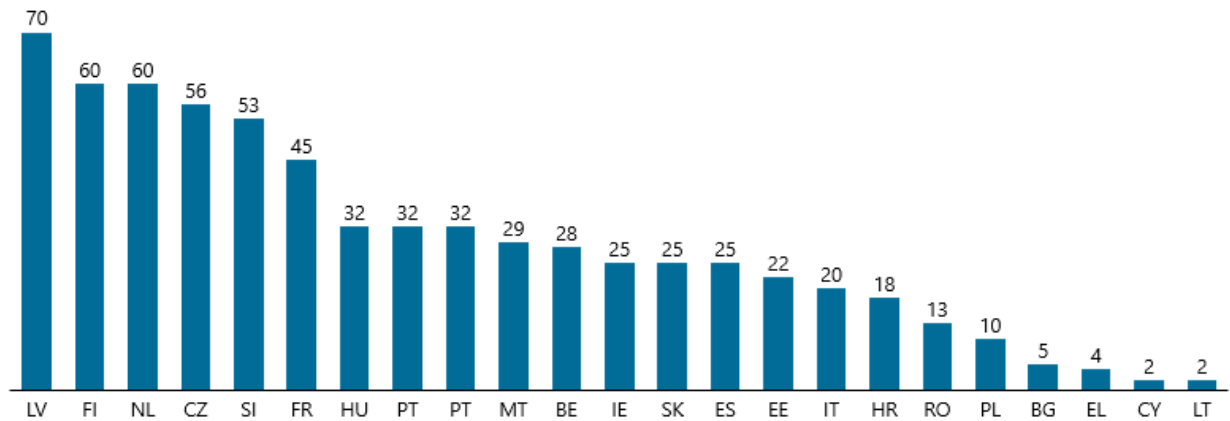
This poses the policy question of whether promoting competition in the letter segment, e.g. through access regulation, should still be a priority for policy-makers. We present this policy discussion in Chapter 2.

1.3.2. New entrants and new business models in the parcel segment

The increase in e-commerce volumes attracts new entrants into the parcel segment, making it very competitive. This is reflected in the lower share of parcel deliveries of the incumbents, see Figure 7.

Figure 7: Incumbent's share of domestic parcel & express deliveries in 2016

Per cent



Note: Composition of products can vary by country and it is subject to the interpretation of the national regulatory authority (NRA). The share represents the approximate share of the incumbent's volumes or revenues. BE, DK, UK - confidential information. DE, IS, LI, SE - information not provided. NL – based on ACM's estimate, the figure does not include express services. HR, CZ, EE - source is ERGP report. EE is based on revenues. FR - according to Xerfi. IT - including own courier SDA, based on revenues

Source: Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)* and ERGP (2016) 38, *Report on core indicators for monitoring the European postal market*

The new players that enter the parcel segment often use new business models, such as new technologies and different employment contracts, see Box 1.

Box 1: Definitions of types of employment

Part time employment – refers to an employee whose normal hours of work, calculated on a weekly basis or on average over a period of employment of up to one year, are less than the normal hours of work of a comparable full-time worker.

Temporary employment (Fixed-term) – a person having an employment contract or relationship entered into directly between an employer and a worker where the end of the employment contract or relationship is determined by objective conditions such as reaching a specific date, completing a specific task, or the occurrence of a specific event.

Performance-related pay contracts – contracts with payment scheme based on items delivered. Such contracts may also include a fixed guaranteed payment, irrespective of quantity of items delivered, but at least 50 per cent of the salary should be performance-related.

Flexible employment (Casual work) – a type of work where the employment is unstable and continuous, and the employer is not obliged to regularly provide the worker with work, but has the flexibility of calling them in on demand, e.g. on-call work (i.e. workers with no guaranteed working hours that can be called-in on the same or next day, if needed); mini contracts (contracts with no guaranteed working hours, where workers can be called-in on an ad hoc basis for a limited period, e.g. during a peak season).

Self-employment contracts – any person on the labour market who cannot be considered as an employee/worker, e.g. contracts with private persons who are registered as freelance workers.

Subcontracted workers (Temporary agency work) – form of work where the worker has a contract of employment or an employment relationship with a temporary-work agency with a view to being assigned to a user undertaking to work temporarily under its supervision and direction. (Note the difference with subcontracted or outsourced work (or commonly referred to as a “subcontractor”), which relate to contracts with legal persons for the provision of services, e.g. the clearance, sorting, transport or distribution of parcels for the parcel delivery service provider).

Source: European Commission (1997), *Directive 97/81/EC*; European Commission (1999), *Directive 1999/70/EC*; European Commission (2008), *Directive 2008/104/EC*.

Amazon is an example of a new player using new business models, see Box 2.

Box 2: Amazon using new business models

Amazon has been continuously improving its warehouse and delivery operations using innovative solutions and alternative employment contracts. In its warehouses, for example, Amazon uses robots to carry and group items needed for a specific order, reducing the time spent by manual labour for this operation. In last-mile delivery, Amazon uses self-employed carriers and small subcontractors, coordinated through a delivery platform. This means that it only takes having a vehicle, a smartphone and being available for shifts ranging between one and four hours to become a self-employed carrier.

Source: WIK (2019), Report on Development of Cross-border E-commerce through Parcel Delivery, A study for the European Commission

Incumbent operators, including USPs, that still play an important role in the parcel segment, and international logistic companies such as UPS and FedEx/TNT, have been expanding their B2C e-commerce delivery. This was mainly driven to respond to the increase in e-commerce volumes and increased competition. Hence, postal companies are transforming their network from B2B to B2C and expanding their activities into new countries to deliver e-commerce cross-border. UPS is an example of an international integrator originating from the B2B delivery segment that has expanded its operations into the B2C segment in response to growth in e-commerce, and Deutsche Post DHL is an example of a USP active in multiple countries and in the e-commerce cross-border delivery, see Box 3.

Box 3: UPS and Deutsche Post DHL expanding into new markets

In recent years, UPS has expanded its infrastructure in Europe to enhance its e-commerce cross-border delivery services, expanding existing facilities, building new ones, and investing in new parcel sorting centres and hubs. Furthermore, UPS expanded its B2C delivery services through acquisitions such as Kiala (with a network of Pick-Up Drop-Off (PUDO) points in Belgium, the Netherlands, Luxembourg, Spain and France) and the Irish parcel carrier Nightline Logistics (owning a parcel locker network called "Parcel Motel"). In 2017, UPS' International Packet segment, which includes small packet operations, made up 20 per cent of UPS' total revenues, and around half of international revenue (around EUR 6 billion) are attributable to European operations.

Deutsche Post DHL is active in multiple countries and in the e-commerce cross-border delivery, through its express division DHL Express. DHL Express's main focus is on express services for high value e-commerce items on global scale. In this segment, DHL Express' global revenues were EUR 15.049 million in 2017 of which 44 per cent are attributable to its European operations. At the same time, DHL Express has been expanding its services into the B2C segment, targeting small and medium-sized e-retailers, and in selected European markets.

Source: UPS Annual report 2017; UPS Pressroom (2017) *UPS To Acquire Ireland-Based Nightline Logistics Group*; UPS Pressroom (2014) *UPS Begins Rebranding Kiala Locations and Expands B2C Cross-Border Delivery Options*; DHL Press Release (2017) *DHL extends its European parcel network to include four additional countries*; Deutsche Post DHL Annual report 2017.

1.4. More attention is paid to the impact on the environment

The Paris Climate Agreement – adopted by 195 countries in December 2015 – sets out a global action plan to limit global warming to well below 2°C in order to avoid the most dangerous climate change impacts.²⁵

In this context, the postal sector is an important stakeholder in driving carbon efficiency and achieving relative carbon reductions across all aspects of the supply chain. Furthermore, changes in the product mix (from letters to parcels) have important implications for postal operators' environmental footprint because parcel delivery requires significantly more logistical and transportation capacity than letters, creating a challenge for postal operators to reduce their environmental footprint.

The true net effect of the postal and e-commerce delivery sector on the environment has however not been appraised. Delivery vans replace consumers' cars and supermarkets' middle mile trucks, and the digital transformation shifts activities and logistics processes to other sectors. Thus, in order to assess the net effect of growing e-commerce volumes, different countervailing factors need to be taken into

²⁵ United Nations (2015), *Paris Climate Agreement*, http://unfccc.int/files/essential_background/convention/application/pdf/english_paris_agreement.pdf (accessed, 11 Dec 2017).

consideration and it is important to include all effects from both the delivery sector and from the consumers' own transportation.

1.5. Universal service providers respond to market trends in various ways

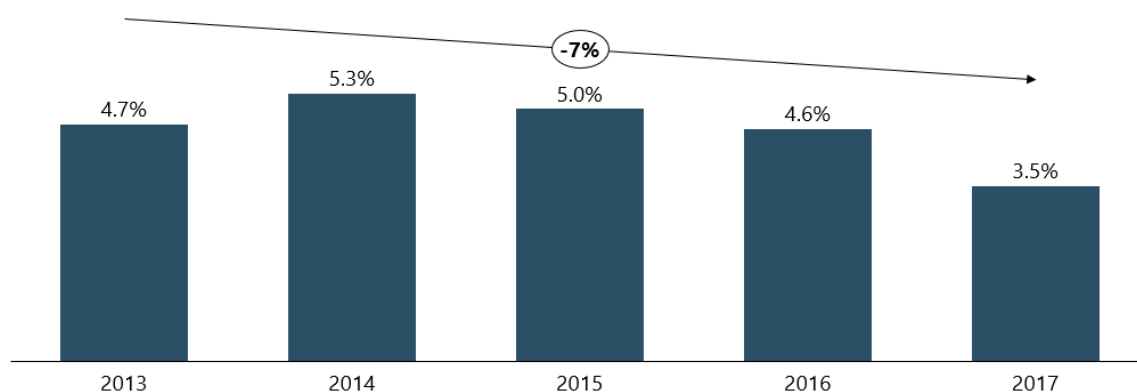
The trends described in the previous sections have had an impact on the profitability of universal service providers and forced them to transform and innovate. In particular, USPs responded by adapting prices, entering new markets, offering new products, innovating and using new business models. At the same time, the market trends sparked debates on regulatory changes and triggered modifications to the postal regulatory framework.

1.5.1. Financial performance of universal service providers

The changing demand behaviour in the letter post segment has had a negative impact on the financial situation of postal operators. The unweighted average EBIT margin²⁶ of USPs in the EU has been declining by an average 7 per cent per year between 2013 and 2017, going from 4.7 per cent in 2013 to 3.5 per cent in 2017, see Figure 8.

Figure 8: Development of USPs' profitability in the EU, 2013-2017

Average EBIT margin



Note: EBIT of USPs' total business. The figure contains data from the following 23 countries: AT, BE, BG, CY, CZ, DE, DK, EE, EL, ES, FI, FR, HU, IE, IT, LT, MT, NL, PT, SE, SI, SK, UK

Source: USP annual reports and UPU, database (accessed, 06 Aug 2019)

When looking at data for 2018 (which is available for 15 postal operators), we see that the majority of postal operators experienced a decline in profitability, while for some profitability increased or remained stagnant, see Table 2.

²⁶ EBIT stands for Earnings Before Interest and Taxes. The EBIT margin is calculated as the ratio of EBIT over total revenues and is a commonly used measure of profitability.

Table 2: Development of USPs' profitability in the EU, 2013-2018

Country	EBIT margin						Total change in EBIT margin (on available years, percentage points)	From year to year
	2013	2014	2015	2016	2017	2018		
AT	7.9%	8.3%	3.7%	10.0%	10.7%	10.8%	2,9 p.p.	2013-2018
BE	18.4%	19.5%	19.4%	20.5%	16.3%	10.2%	-8,2 p.p.	2013-2018
BG	-13.0%	-13.0%	-1.9%	-14.9%	-12.6%	N/A	0,4 p.p.	2013-2017
CY	15.3%	15.1%	15.0%	16.4%	14.5%	N/A	-0,8 p.p.	2013-2017
CZ	1.3%	0.9%	1.3%	1.1%	0.6%	-1.3%	-2,6 p.p.	2013-2018
DE	5.2%	5.2%	4.1%	6.1%	6.2%	5.1%	-0,1 p.p.	2013-2018
DK	1.7%	0.9%	1.4%	-2.8%	-0.3%	-2.3%	-3,9 p.p.	2013-2018
EE	4.2%	4.6%	3.7%	11.0%	0.6%	N/A	-3,6 p.p.	2013-2017
EL	-1.4%	1.2%	N/A	N/A	0.2%	N/A	1,6 p.p.	2013-2017
ES	3.7%	16.7%	-2.9%	-2.8%	-10.1%	N/A	-13,8 p.p.	2013-2017
FI	0.5%	0.3%	3.3%	1.9%	-1.7%	0.4%	-0,1 p.p.	2013-2018
FR	3.5%	3.2%	3.8%	4.2%	4.2%	3.7%	0,1 p.p.	2013-2018
HR	3.5%	8.2%	10.6%	8.0%	N/A	N/A	4,5 p.p.	2013-2016
HU	0.2%	0.3%	1.9%	2.0%	0.2%	N/A	0,0 p.p.	2013-2017
IE	-1.4%	0.3%	0.6%	-1.7%	0.6%	4.2%	5,6 p.p.	2013-2018
IT	5.3%	2.4%	6.8%	8.6%	8.4%	8.4%	3,0 p.p.	2013-2018
LT	6.4%	1.0%	1.6%	1.5%	3.0%	5.7%	-0,7 p.p.	2013-2018
LU	8.3%	7.1%	3.8%	4.0%	N/A	N/A	-4,4 p.p.	2013-2016
LV	8.0%	3.0%	5.3%	4.5%	N/A	N/A	-3,5 p.p.	2013-2016
MT	9.2%	11.5%	12.5%	9.9%	7.6%	6.1%	-3,1 p.p.	2013-2018
NL	9.6%	11.6%	9.8%	8.5%	10.4%	6.7%	-2,9 p.p.	2013-2018
PL	0.6%	2.5%	1.9%	0.6%	N/A	N/A	0,0 p.p.	2013-2016
PT	12.4%	18.9%	18.3%	17.6%	12.5%	N/A	0,1 p.p.	2013-2017
RO	-2.5%	3.1%	-2.7%	N/A	N/A	N/A	-0,2 p.p.	2013-2015
SE	1.7%	0.9%	1.4%	-2.8%	-0.3%	-2.3%	-3,9 p.p.	2013-2018
SI	-7.6%	3.3%	3.3%	3.8%	3.4%	4.3%	11,8 p.p.	2013-2018
SK	1.4%	1.4%	1.3%	0.9%	0.5%	N/A	-0,9 p.p.	2013-2017
UK	17.6%	3.8%	1.8%	2.4%	2.3%	4.5%	-13,1 p.p.	2013-2018

Source: Copenhagen Economics

Moreover, these EBIT margins include other activities too, such as the delivery of parcels and express items and in some cases financial services. When looking only at the profitability of the postal activity, some USPs have experienced a loss, e.g. USPs in Bulgaria (all five years), Denmark (from 2016) and Spain (from 2015).

However, as a response to changing demand behaviour many USPs have reinvented themselves or are in the process of doing so. Where regulatory frameworks and governance have allowed it, USPs have been offering new products to diversify their revenues, adopting new business models and using new employment contracts.

1.5.2. USPs diversifying revenues by offering new products

Declining volumes in letter post urge some postal operators to pursue economies of scope through diversification strategies in order to sustain the economic viability of their dense postal networks.

Postal operators in Europe have been actively pursuing growth opportunities in new business areas. The most popular diversification strategies of USPs are express services, retail services, printing and

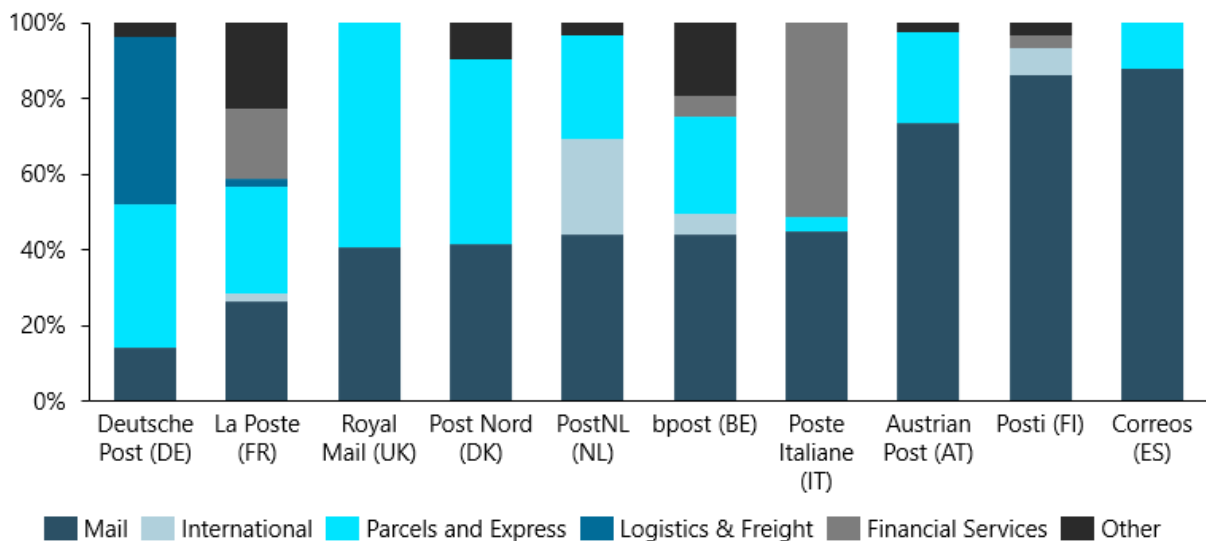
mail preparation, hybrid mail²⁷, freight and logistics services²⁸, and financial services²⁹. Although less popular, information services and telecommunications are other important ways of diversifying services at USPs. Examples of these are e-government services and virtual delivery networks^{30, 31}.

Some of the services offered by USPs are services of general economic interest (SGEI) and as such are financed by the State. We show more of these examples in Chapter 2.

Many of these additional services provided by USPs represent a big share of USPs' revenues, see Figure 9.

Figure 9: Diversification of revenue among USPs, 2017

Per cent of total revenue



Note: Mail refers to the letter post segment. Some USPs might be delivering some services through other companies of the group and so do not appear in this chart, e.g. DHL Express

Source: PostNL (2019), *European postal markets – 2019 an overview*

Poste Italiane is an example of a USP that relies mainly on revenues from financial services, which represent almost 50 per cent of Poste Italiane Spa's total revenues.³²

PostNord Denmark is an example of a USP providing e-government services, with its secure electronic mailbox service E-Boks.³³

²⁷ Hybrid mail refers to items that are dispatched in electronic form by the sender and are subsequently printed, packed, sorted and delivered by the postal operator to the recipient.

²⁸ Services such as cargo and other custom transport services.

²⁹ Including money transfers and other banking services.

³⁰ Virtual mail refers to the digitalisation (scanning) by the postal operator of a paper-based item dispatched by the sender and its electronic delivery of the item to the recipient.

³¹ Copenhagen Economics (2018), *Main Developments in the Postal Sector 2013-2016*.

³² Poste Italiane Spa is one of the companies under the Poste Italiane Group. Beside financial services, other companies of the Poste Italiane Group provide insurance services, which in 2018 generated more than 13 per cent of the Group's total revenues. Source: Poste Italiane (2018), *Annual report 2018*.

³³ Copenhagen Economics (2018), *Main Developments in the Postal Sector 2013-2016*.

Le Groupe La Poste went even further into the digital space, offering to e-commerce companies services such as website development, e-logistics, web marketing and online payments.³⁴

In addition, part of the diversification agenda has been driven by mergers, acquisitions and divestments. For instance, in 2017, PostNL expanded its parcels services with overnight delivery by acquiring PS Nachtdistributie. In the same year, bpost acquired Radial – the US based provider of integrated e-commerce logistics. It allows bpost to scale its existing presence in the US market and expand its product offering into value-added activities that cover the entire value chain in e-commerce logistics, including the Benelux and European markets.

1.5.3. Postal operators are using new business models, new technologies and environmentally friendly ways of transport

As a response to e-substitution in the letter post segment, increased competition in the parcel segment and other factors disciplining the postal sector, such as environmental targets, incumbent postal operators are innovating their processes and increasing their efficiency, e.g. by using new technologies and redesigning their networks.

a. Use of new technologies

Many postal operators invest in new operational technologies to reduce costs and increase operational efficiency. Postal operators use the following main technologies in different steps of the postal value chain:

- *Barcoding* – allows for the scanning of labels on letters and parcels, improving handling speed in sorting facilities;
- *Sensors and machine vision* – used to weigh and measure mail items and to read off parcel labels in the sorting process;
- *Label learning and fingerprinting* – allow to read non-standard labels and identify parcels without a label through visual patterns;
- *Optical character recognition and video coding* – to read hand-written labels;
- *RFID technology* – identifies parcels through radio frequencies instead of barcodes, improving postal logistics processes;
- *Robotics* – used in parcel sorting to assist in repetitive tasks or heavy lifting and automate transport in warehouses;
- *Personal digital assistants and route optimization* – allow for digitalisation of the delivery process (signatures and delivery confirmation) and optimize the number of delivery routes;
- *Automated vehicles with self-driving features* – have the potential to increase safety and efficiency in the delivery process;
- *Drones* – have the potential to replace human workers and other means of last-mile delivery transport by delivering by air to the customer's door step, thus making last-mile delivery more cost efficient.

³⁴ Copenhagen Economics (2018), *Main Developments in the Postal Sector 2013-2016*.

The extent of the use of these technologies varies by postal operator and by step of the postal value chain. Technologies like barcoding, sensors and RFID are used largely in the mail sorting phase, while the use of last mile innovations, such as autonomous vehicles and drones, is scarcer.

Going forward, postal operators' investments will probably go to autonomous vehicles and other innovative delivery models, particularly for parcel and express services, given that last-mile delivery activities constitute the largest cost for postal operators.³⁵ As an example, Deutsche Post is currently testing artificial intelligence, virtual reality, blockchain and eMobility technologies for postal services. The speed of this development also depends on the legal framework, since in many countries it is not currently legal to test automated vehicles and drones.

If on the one hand the use of new technologies brings efficiency, on the other it also leads to a reduction in the share of manual work and employment in the delivery chain. This is the case with technologies such as sorting machines, RFID technology, drones, and artificial intelligence.

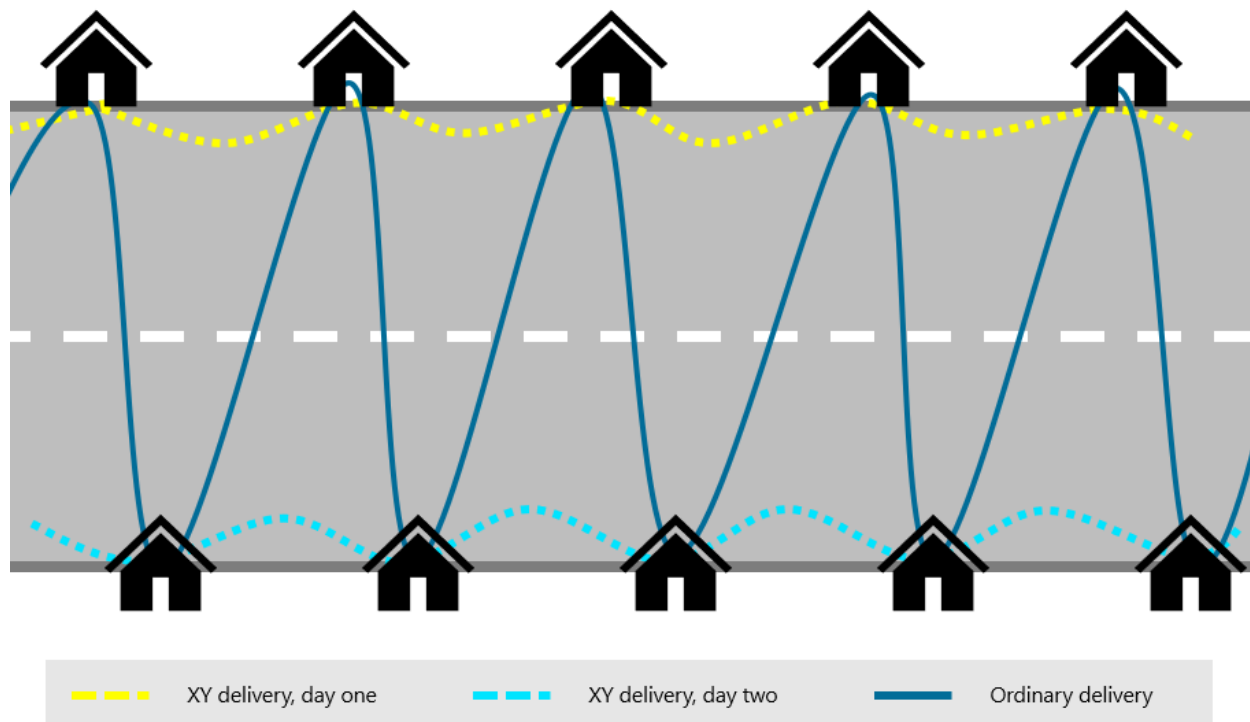
b. Redesigning the delivery networks

Many postal operators are redesigning their delivery networks to improve the efficiency of their operations in response to a changed mail mix. Some examples are:

- *Centralization and automation of sorting centres.* In Belgium, bpost consolidated all parcel sorting activities at a single new sorting centre. Correos in Spain removed manual sorting centres and created big automated parcel sorting centres in Madrid and Barcelona. Additionally, it integrated logistics and technologies with key clients who employ different kinds of mail pre-sorting, in order to increase efficiency. In Germany, Deutsche Post implemented modern technologies to improve the performance of the 34 German parcel centres and raised the sorting capacity to 32,000 shipments per hour. This was made possible for example by including scanners that can read addresses on all six sides of a parcel, partially automated vehicle unloading and a new sorting technology that minimizes the risk of damage.
- *Centralization of distribution offices.* bpost again increased the centralization and automation of all preparatory mail distribution tasks and rationalized the number of distribution offices from more than 400 to around 60 Mail Centres. Additionally, it tested a new distribution model based on the centralization of preparatory mail delivery tasks. The Greek USP also merged some delivery centres in the last three years.
- *Introduction of alternate day (XY) delivery.* The intuition behind XY-delivery can be explained as if the postperson delivers letter on one side of the street one day and on the other side of the street the next day. This is different from ordinary delivery where the postperson visits all households every day, see Figure 10. XY delivery allows the postperson to bring more items to each household per delivery thereby reducing unit cost. Different variants of XY delivery have been implemented in many countries following the decline in letter volumes, for example in Denmark, the Netherlands and Italy.³⁶

³⁵ McKinsey (2016), *Parcel delivery – The future of last mile* tried to predict and forecast the technologies that will dominate the postal industry in the future, concluding among other things that in the next ten years autonomous vehicles will deliver 80 per cent of parcels.

³⁶ For example, in Italy the XY model means that the USP is not going to specific towns on some days, while in Denmark the USP is going through all towns and routes every day, but only on one side of the street.

Figure 10: Illustration of the XY delivery model

Source: Copenhagen Economics

- *Integration of parcels and letters into one delivery stream.* One way to redesign the network is to merge the delivery of letters and parcels. However, the efficiency gain from this reorganization is not straightforward. In the EU, 15 USPs concluded that it is more efficient to integrate individual (or all) steps of the production chain for letters and parcels, while 8 USPs did not.³⁷ The conclusion depends on multiple market and company specific conditions, e.g. the share of parcel volume in the total mail volume.
- *Introduction of more efficient distribution channels,* such as parcel lockers, post-in-shop networks, and collaborations between different operators. The majority of USPs in Europe uses parcel lockers and pick-up points. In France, La Poste deployed pick-up stations with parcel lockers at post offices and in high traffic areas. In addition, different operators collaborate to improve efficiency in the value chain. For instance, Dutch PostNL combines logistics flows from other companies to reduce the volume of traffic in city centres.³⁸
- *Move from brick-and-mortar to mobile post offices.* The introduction of mobile post offices is one of the solutions to declining demand in rural areas. A mobile post office is a motorised postperson providing virtually all traditional postal services, incl. collection and delivery of postal items, periodicals, payment services, pensions and social contributions as well as retail services. Mobile post offices provide two types of point of contact: first, a time slot in a fixed location based on a published schedule (typically near the old post office in a town centre); second, a personal visit to customers' homes on request. In Lithuania, the USP is moving to mobile post offices, see Box 4.

³⁷ Five USPs answered "other" or did not answer. Source: Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*.

³⁸ Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*.

Box 4: Mobile post offices in Lithuania

In Lithuania, up to 300 post offices in rural areas are planned to be closed and services to be moved to mobile post offices. The main motivation is two-fold: extremely low service volumes (5-7 customers per day) and high fixed costs in real estate maintenance and labour costs in these areas. Mobile post offices are expected to bring a number of benefits to the postal operator: higher productivity (Lithuanian Post estimates that one postal worker will be able to conduct 100-150 transactions per day and cover a route of 100-130 km per day), lower labour costs (the number of postal workers in rural areas can be reduced by 20-30 per cent while increasing wages for remaining employees), financial boost (from sale of real estate and reduction in maintenance costs), offer of new social services (e.g. check in on elderly people). The main challenges are: (1) *Resistance from specific client segments* who are attached to a physical post office and who fear that their access to postal services will be restricted. In Lithuania, to mitigate customer resistance to mobile post offices, the USP ensures that a mobile post office is available near the old post office for at least 15-30 minutes every day at a given time. Otherwise, customers can always order a mobile post office to their home by calling the customer service. The USP guarantees that all customers will be visited no later than the next day. (2) *Regulatory barriers* in relation to network density requirements, if the national USO defines a point of contact as a permanent establishment. We note that Article 3, par. 2 of the Postal Services Directive provides enough flexibility to define the point of contact: “Member States shall take steps to ensure that the density of the points of contact and of the access points take account of the needs of users”. (3) *Fixed start up investment* needed in vehicles, tablets and IT systems’ integration. (4) *Provision of services* involving higher amounts of cash or more complex operations, e.g. retail banking services, may be restricted.

Source: Interview with Lietuvos pastas, the Lithuanian USP.

c. Use of environmentally friendly ways of transport

Postal operators are integrating climate change and energy considerations into operational policy, strategy, and long-term planning, mainly because of reputational, regulatory and financial reasons.

Best practice examples in environmental sustainability carried out by postal operators include:

- *Reducing energy usage and emissions of their buildings*, by increasingly relying on renewable electricity and enhancing building’s energy efficiency.
- *Setting environmental targets on their own operations*. For example, in Germany Deutsche Post set the goal to reduce all transport-related emissions to net zero by 2050.
- *Introducing environmentally friendly vehicles in addition to the traditional delivery by foot and bicycle*. Many postal operators are employing new electric modes of delivery, such as electric bicycles and electric vans and cars.
- *Educating drivers in ‘green’ driving behaviour* is another common measure to reduce environmental impact, for example by selecting routes that enable reduction in mileage, as done by PostNL in the Netherlands.
- *Compensating for unavoidable CO2 emissions*, as done by Austrian Post.
- *Setting sustainability requirements on sub-contracted and outsourced activities*. For example, introducing stringent sustainability requirements within postal operators’ procurement procedures and through their supply chain management practices, as done by bpost in Belgium.³⁹

³⁹ Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*.

1.5.4. The postal and delivery sector is using new employment contracts

Developments in technology, user needs, competition and postal business models change employment conditions and the demands on postal operators' workforce. Postal sector stakeholders⁴⁰ identified the following four most prominent recent developments in employment conditions:

- *Even more pressure on reducing expensive employment contracts*, e.g. civil servants, which have been decreasing in number at a rate of -6.7 per cent annually in average across Europe from 2013 to 2016, against a -1.7 per cent average annual rate of decline of overall employment;⁴¹
- *Use of new employment models*, such as on-call work, temporary agency work, outsourcing, sub-contracted workers, and self-employment (see Box 1 for definitions of types of employment);
- *More performance-related pay*, e.g. pay based on the number of delivered mail items and parcels per day. These types of contracts are used by one third of European USPs, although their share in total employment does not exceed 13 per cent;
- *Modernisation of USPs' salary structures*, although such changes have been more prominent where collective labour agreements (CLA) could be redefined and become more flexible. An example is the Deutsche Post case from 2015, where Deutsche Post planned to remunerate DHL parcel workforce according to the CLA specific to logistics (which provides lower remuneration than the CLA for post), instead of the postal CLA. The announcement triggered significant opposition by the trade unions, which in the end obtained higher salaries for the logistics employees.⁴²

⁴⁰ Copenhagen Economics based on interviews and past studies, e.g. Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*.

⁴¹ Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*.

⁴² Reuters (2015), *Update 1 – Deutsche Post to create thousands of jobs on lower pay*, <http://www.reuters.com/article/2015/01/22/deutsche-post-workers-idUSL6N0V11G120150122> (accessed, 1 May 2015).

2. EU POSTAL SECTOR POLICY DEBATES AND RESPONSES

KEY FINDINGS

Market developments vary across countries and both postal operators and regulators chose different strategies to respond to the market trends discussed in Chapter 1. The policy debate in the various Member States and at the EU level over the past decade can be summarised in three main trends:

- The financial viability of the universal service providers comes under pressure because of letter volumes decline and hence, there is an increased focus on the sustainability of the USO. The policy debate evolves around whether this requires a fundamental change in the regulatory paradigm and in the prioritisation of policy objectives.
- Changing user needs have challenged the role of the USO and its definition. What are the needs that the market cannot meet? And are there any new needs that emerge? As a result, there is a policy debate about the appropriate scope of state intervention in the postal sector.
- With the increase in cross-border e-commerce shipments, policy-makers are debating how to adapt regulatory frameworks to ensure an efficient cross-border parcel delivery.

In the following sections, we discuss each of the three policy debates in detail.

2.1. Ensuring a sustainable USO

Two central objectives in the Postal Services Directive are to promote effective competition and to ensure the provision of universal services. There can be a trade-off between these two objectives. On the one hand increased competition can force universal service providers to become more efficient, but on the other hand increased competition will reduce the volume for the universal service provider, which increases the challenges of maintaining a sustainable business in an industry where economies of scale are crucial. It is natural and necessary that the balance between these two objectives changes over time as the use of postal services changes due to digitalisation.

Securing an efficient and financially sustainable universal service provision is one of the key challenges of the postal sector. Declining letter volumes in combination with unchanged regulatory requirements might imply even bigger challenges to ensure the financial sustainability of the USO.

The cost of providing universal services can increase to levels where it is impossible to provide universal services on commercial terms due to (i) volume decline, which increases fixed costs per unit; (ii) rising input costs, e.g. fuel costs, salaries; (iii) network competition, which reduces the number of letters going via the USP's network; (iv) pressure to maintain prices low from electronic alternatives of communication.

However, there is a limit to how much the market is willing to pay for universal services. Hence, ensuring a sustainable USO has been the centre of different policy debates and responses, which usually evolve around two stages. The first stage is to reduce the burden of the USO by giving the universal service provider more operational and/or pricing flexibility. The second stage is to shift the prioritisation of the policy objectives from stimulating competition to sustainability of the USO. In the past years, we have observed the following three main directions of policy responses by operators and regulators:

- Allowing USPs to improve efficiency through higher operational flexibility;
- Allowing USPs to price more flexibly;
- Putting the sustainability of the USO in front of other policy objectives, such as competition rules.

We discuss each of these policy responses below.

2.1.1. Allowing USPs to improve efficiency through higher operational flexibility

Policy-makers across EU Member States are providing USPs with higher operational flexibility by allowing them to reduce their delivery frequency and their network. These changes are often combined with more than one modification to the postal regulation e.g. changes to the price regulation.

a. Allowing USPs to decrease the frequency of delivery

The current USO regime requires USPs to be capable of delivering five or six days per week throughout the country (except in exempted areas, where special conditions apply). Five days per week is the minimum requirement set in the Postal Services Directive. However, under specific market circumstances, operators have introduced regulatory-compliant network designs (delivery models) which – for most traffic – imply an effective delivery frequency reduced to e.g. 2-3 days per week throughout the country, while safeguarding the capability to deliver faster letters and deliver at least 5 days per week. To satisfy market demand features (service levels for letters and parcels) and comply with regulation, in some countries, the USP introduced additional layers of delivery (parallel delivery networks in specific areas) to balance efficiency and effectiveness of the service.

Delivery frequency is linked to the delivery speed of postal products (the existence of some D+1 letters in the mail mix requires the postal operator to maintain the capability to deliver mail almost every day). Thus, changes in the effective delivery frequency are often combined with changes in the delivery speed enshrined in the service levels (Quality of Service indicators) for key products.

Reducing the delivery frequency enables USPs to implement more efficient operational models. Under certain circumstances, the cost saving potential from reducing delivery frequency can be very large and have significant impact on the net cost of the USO (we explain the concept of net cost of USO in Section 2.1.3). The large cost saving potential from reducing delivery frequency comes from the ability to increase *drop density*, i.e. the number of letters delivered per visit at the letterbox. If a mail-man can deliver the same amount of mail but go fewer days with more mail items each day, the postal operator can save cost on the delivery activity.

Reducing speed of delivery would also bring about cost savings because postal operators do not have to rely on air transportation but can use rail or road transport to get letters from one end of the country to the other. This can also potentially reduce the **environmental impact** per mail product.

Cost savings from operational changes however may result in reductions of number of **employees** in the postal industry, given for example reduced use of overnight sorting or increased automatisations.

A number of Member States have allowed the USP to reduce its delivery frequency, such as Denmark, Finland, Italy and the Netherlands. In Romania the government has just modified the postal law to allow for decrease in delivery speed.

In **Denmark**, as a reaction to a steep decline in letter volumes sent through PostNord DK (a total 75 per cent between 2003 and 2016)⁴³, the postal regulator allowed a number of changes to PostNord DK's obligation, to provide more operational flexibility. One of these changes has been the decrease in delivery frequency.

In 2009, PostNord DK introduced the XY-delivery model (see Section 1.5.3.b for explanation). No regulatory change was necessary to introduce XY delivery, however price increases of the fastest letter product (A-letters) were needed to induce a shift from A-letters to more flexible B- and C-letters.⁴⁴

In 2016, A-letters were removed from the USO, the delivery speed for B-letters was decreased from D+3 (delivery three days after posting) to D+5 (delivery five days after posting) and the overall delivery frequency was decreased from six to five days per week. PostNord has estimated that these changes reduced the burden of the USO by EUR 44 million.⁴⁵

Finally, in 2018, letter and parcel delivery have been integrated in the same network and the delivery frequency of standard letters was set to once per week.

The postal regulator in **Finland** has also allowed a decrease in delivery frequency in areas with early morning newspaper delivery from five to three days per week to respond to the steep decrease in addressed mail volumes (30 per cent from 2011 to 2016)⁴⁶. The delivery frequency requirements in areas with no early morning newspaper delivery are unchanged at five days per week.⁴⁷ The changes to the delivery frequency took effect in July 2018,⁴⁸ although the USP has not yet fully implemented them.⁴⁹

In **Italy**, from 2011 to 2015, the addressed mail volume delivered by Poste Italiane declined by 38 per cent.⁵⁰ As a consequence, regulatory and legislative changes in 2014 and 2015 allowed Poste Italiane to implement an XY delivery model in the most rural areas of the country, where mail is delivered on Mondays, Wednesdays and Fridays during the first week and on Tuesdays and Thursdays in the second week.⁵¹ The remaining areas have a frequency requirement of five-day delivery.

In the **Netherlands** addressed mail volumes delivered by PostNL decreased by 36 per cent from 2011 to 2015.⁵² One of the actions taken by Dutch policy-makers in 2014 has been to reduce the frequency of delivery from six to five days, with delivery from Tuesdays to Saturdays.⁵³ Monday delivery was discontinued immediately.

The government in **Romania** has modified the postal law, including decreasing the delivery speed of the fastest letter product from D+1 to D+2 and of the second-fastest product from D+3 to D+4.

⁴³ PostNord, *annual reports*.

⁴⁴ Copenhagen Economics and Post Danmark – *PostNord Presentation on 6th December 2011*, http://www.wik.org/fileadmin/Konferenzbeitraege/2011/13th_Koenigswinter_seminar/S3_1_Sondrup.pdf.

⁴⁵ PostNord, *Annual and Sustainability Report 2016*.

⁴⁶ PostNL (2017), *European Postal Markets*; Posti, *Annual Reports*.

⁴⁷ Finlex (2011), *Postlag 415/2011: 15 § Postförsändelser som ingår i de samhällsomfattande tjänsterna*.

⁴⁸ Posti (2017), *Posti's delivery day reform will proceed during the summer – the number of delivery days will not change*, https://www.posti.fi/english/current/2017/20170531_postis-delivery-day-reform-will-proceed-during-the-summer.html.

⁴⁹ Interview with Posti.

⁵⁰ PostNL (2017), *European Postal Markets*.

⁵¹ Italian Law (2014), *n. 190*; AGCOM, *Decision 395/15/CONS*.

⁵² PostNL (2017), *European Postal Markets*.

⁵³ Dutch Ministry of Economic Affairs (2014), *The Dutch Postal Market and the Postal Directive*, http://www.ancom.org/en/uploads/links_files/2_Jeroen_Sas_-_The_Dutch_Postal_Market_and_the_Postal_Directive.pdf.

b. Allowing USPs to reduce their network

Decreasing the network, i.e. closing down post offices, is another action to decrease USPs' operating costs.

In **Denmark** the postal network density is one of the main drivers for the USO's net cost, together with the delivery frequency and the scope of the universal service. To drive down costs PostNord DK shifted its post offices to post-in-shop facilities, e.g. post office counters in supermarkets.

Finland is characterized by large geographical distances and difficult terrain (e.g. mountains), making its postal network expensive to maintain. Consequently, the Finnish postal operator has on the one hand reduced the number of traditional post offices, closing some down⁵⁴ and moving others to post-in-shop (i.e. outsourced retail offices, e.g. in grocery stores), and on the other hand increased the number of parcel lockers.⁵⁵

Maintaining a large postal network is expensive also for countries with high population density. In 2015, the postal regulator in the **Netherlands** allowed a reduction in the number of USP's postal branches from 2 000 to 1 000 and a reduction in the number of mailboxes from 19 000 to 8 700.⁵⁶

In **Lithuania** the USP and the NRA are currently discussing the possibility of replacing permanent physical post offices with mobile post offices (see Section 1.5.3.b) to comply with the network coverage requirement.

The impact on **environment** of reducing the postal network is ambiguous, since the postal operator drives different routes, which might have a lower impact on the environment, but consumers might drive the routes themselves instead.

Reducing the network may result in reductions of number of **employees** that used to work in the post offices.

2.1.2. Allowing USPs to price more flexibly

The reduction in the scope of USO alone is often not sufficient to the sustainability of USPs. Policy-makers across the EU have provided ways for USPs to sustain the recovery of fixed network costs by allowing price increases and by compensating them (as we discuss in Section 2.1.3.a).

Letter volume decline and changed user needs require USPs to adjust prices and match them with customers' willingness to pay. Changes in postal regulation across the EU have allowed price changes and price increases (e.g. for the first-class letter product).

In **Denmark**, the postal regulator provided PostNord DK with more flexibility in pricing and price increases have been an integral part of PostNord DK's restructuring of its business towards putting more emphasis on slower mail products. In 2010, the price cap on B-letters was removed, leading to price increases of B-letters. In 2011, the prices of both A- and B-letters increased by 45 and 20 per cent respectively. This induced a substitution to products with lower costs: A-letters are substituted with slower products that allow for a more flexible delivery structure.⁵⁷ Throughout the period 2013-2016, the price for a 20g domestic single piece letter increased by 138 per cent, from EUR 1.07 to EUR 2.55.

⁵⁴ The number of post offices was reduced by more than 30 per cent between 2013 and 2016. Source: Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*.

⁵⁵ IPC (2019), *Interview with Posti*; <https://www.ipc.be/news-portal/operations-logistics/2019/06/06/08/12/posti-to-increase-the-number-of-service-points-up-to-2800-some-of-postis-own-shops-to-be-closed>.

⁵⁶ WIK (2016), *Future scenario developments in the Dutch postal market*, A Study for the Ministry of Economic Affairs.

⁵⁷ Copenhagen Economics (2012), *Pricing behaviour of postal operators*, <https://www.copenhageneconomics.com/dyn/resources/Publication/publicationPDF/0/210/0/06209%20Pricing%20behaviour%20of%20postal%20operators.pdf>.

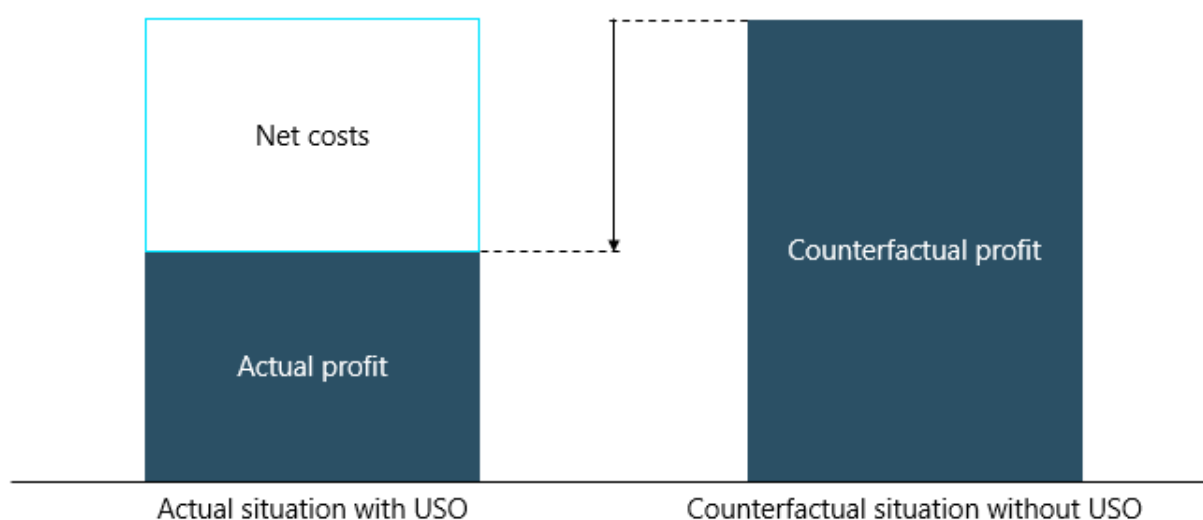
2.1.3. Putting the sustainability of the USO in front of other policy objectives

Price increases are not necessarily always an effective way to reduce the USO burden, especially when higher prices lead to lower demand and in turn to significantly lower volumes and hence, the net effect of a price increase is negative.

In these cases, other measures might be necessary to sustain the USO. As the financial burden of the USO has increased due to volume decline, we have seen two fundamental changes in the policy approach:

First, increased use of compensation for the net cost of the USO. The obligation to provide the universal service can force postal service providers to structure their business in a way which they would not have done without the USO. As a result, the profit earned with the USO may be lower than the profit the operator would have earned without the USO. This difference in profits is called USO net cost, see Figure 11.

Figure 11: Illustration of the USO net cost



Source: Copenhagen Economics

The question that emerges from this policy approach is: What is the most efficient and least distortive way to compensate for the financial burden of the USO?

Second, reducing regulation to put the sustainability of the USO in front of the promotion of competition. This emerges in the context of an ongoing debate about whether the EU requires a new industrial policy. An example emerging from this discussion is whether incumbents should be allowed to acquire their competitors, leading to the question: Should postal operators be allowed to merge and create national, regional or European champions?

We expect that these two policy responses will also inform the policy debate at the European level in the coming years.

a. What is the most efficient and least distortive way to compensate for the financial burden of the USO?

If the provision of universal services leads to a financial burden, Member States are allowed to compensate the USP. There are different ways for compensation and national governments play a key

role in defining a method for compensation. In this regard, there are three questions that governments need to ask:

First, who should pay for the provision of the universal services if this leads to a financial burden (i.e. the USO net cost)?

The options available are limited to compensations by either other industry players (through a so-called 'compensation fund'), consumers of other services (i.e. profitable services cross-subsidise non-profitable services) or government funds (i.e. taxpayer money). This is challenging because (i) market players may not have sufficient financial reserves to compensate the USO (and in any event, the compensation often is split by market share, such that the USP itself should cover more than 90 per cent of its own losses); (ii) cross-subsidies from non-competitive to competitive services are generally seen as distortive, (iii) state subsidies, i.e. taxpayers' money, might not be popular among citizens.

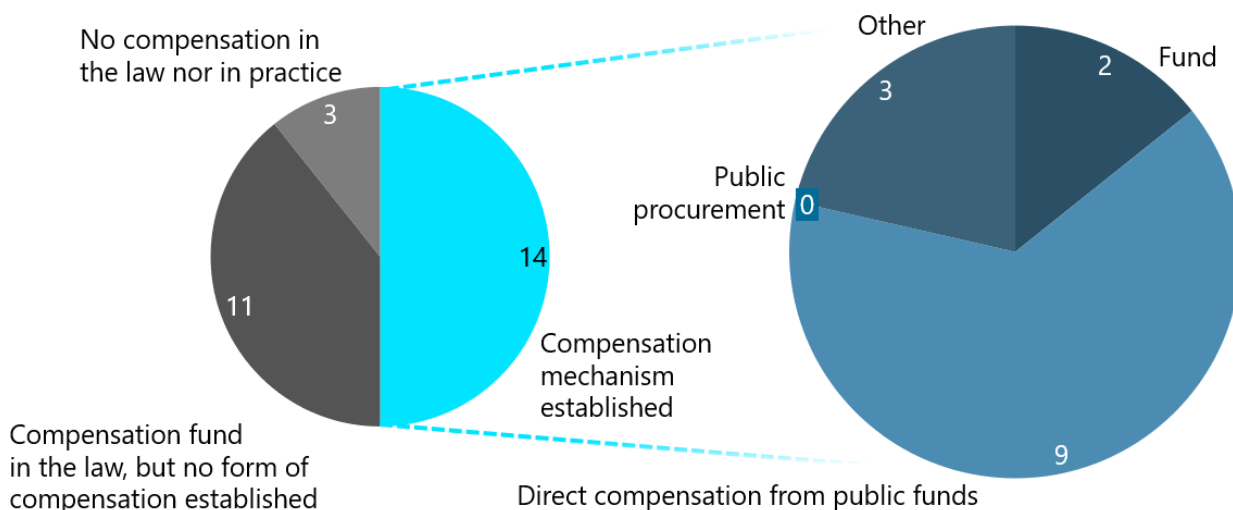
Second, what socio-economic benefits correspond to the funding of the USO? National governments play a key role in defining the level of the USO and hence, the financial burden, because as 'buyers' of universal services they set USO requirements.

The USO is a solution to ensure that social needs that would not be covered by market forces are provided for those who need it. However, if these social needs are changing over time the USO may become obsolete in its shape and size. Thus, it is conceptually clear that the regulatory framework should ensure the USO definition according to contemporary needs.

Third, what is the most efficient and least distortive way to compensate for the financial burden of the USO? We note that around half of European operators receive compensation, usually through direct compensation from public funds, see Figure 12.

Figure 12: Compensation mechanisms

Number of countries



Note: Includes EU 28 countries. In some countries more than one compensation mechanism is established.
 Source: Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*

Poland and Slovakia are the only two countries where a compensation fund to compensate the USO net cost has been established in practice, see Box 5 for the Polish case.⁵⁸

Box 5: The compensation fund in Poland

To finance the universal postal services carried out by Polish Post from 2013 until 2015, the Polish authorities set up a compensation fund. The fund was set to be financed by contributions of a maximum of 2 per cent of the revenues earned by all postal providers in Poland, including Polish Post (around EUR 20.4 million), on universal postal services as well as other postal services that are equivalent to universal services from a customer's point of view (around EUR 1 million). If necessary, this financing will be complemented by direct grants from the state budget (around EUR 1.5 million).

The European Commission has found the compensation granted by Poland to Polish Post to be in line with EU State aid rules. In particular, the Commission approved the measure because the compensation paid to Polish Post was limited to the additional costs it faced to fulfil its public service mission (USO). Moreover, the Commission found that the design of the mechanism to finance the compensation did not lead to a significant distortion of competition in the Polish postal sector.

Source: European Commission (2015), *State aid SA.38869 (2014/N)*.

In **Denmark**, the owners of PostNord, i.e. the Danish and Swedish state, decided a compensation package that would enable the company to implement a restructuring plan. The plan included laying off a large part of civil servants. In 2016, PostNord DK employed almost 3 000 civil servants. In May 2018, part of the restructuring package was cleared by the European Commission. The decision allowed to compensate PostNord by up to DKK 1.2 billion in 2019. Commissioner Margrethe Vestager, in charge of competition policy, said: "Easy access to postal services is vital for all EU citizens. Today's decision enables PostNord to continue performing its fundamental social and economic role and important public service mission, without unduly distorting competition."⁵⁹ There are still ongoing cases where the Commission is examining other parts of the restructuring plan.

Some universal service providers get compensated for providing SGEI. We discuss this further in Section 2.2.2.

b. Should postal operators be allowed to merge and create national, regional or European champions?

At the EU level, there is an ongoing debate about whether the EU requires a new industrial policy. One of the main triggers is the notion of an unlevel playing field and lack of reciprocity which put EU businesses at a disadvantage in Europe and abroad. The EU postal sector is also affected by similar challenges:

First, the EU e-commerce players and postal operators alike face ever-fiercer competition as foreign competitors such as Alibaba and Amazon move rapidly up the value chain.

Second, a fragmented Single Market (particular for intra-EU cross-border and last-mile delivery services) limits the potential for EU postal operators to negotiate a better deal with foreign e-commerce giants. Instead, the EU postal operators are turned to compete against each other for the prospect of getting a larger share of international e-commerce flows. The competition between operators in different countries (A, B) to serve flows to a third country (C) is not per se a challenge for EU socio-economic

⁵⁸ Copenhagen Economics (2018) *Main Developments in the Postal Sector (2013-2016)*, a study prepared for the European Commission.

⁵⁹ Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*.

welfare if it is on the merits. The question is, however, whether other layers of regulation, such as UPU terminal dues, customs rules or access rules, distort efficient pricing of services and thus create regulatory bottlenecks or arbitrages that promote country A operator over country B even when their efficiency would be the same.

Third, diminishing EU's ability to shape rules and standards governing the postal sector – for example, the UPU terminal dues system where EU countries are not united – which is crucial both for industrial leadership and profitability.

One of the points for discussion in relation to the new industrial policy for the EU is whether European companies should be allowed to merge to create European champions that can compete globally with e.g. US-based fully integrated competitors and Chinese companies that play outside competition rules. We find that the policy debate in the EU postal sector has not started yet or it is at an infant stage in these regards. In one recent instance, at a national level, it has been discussed whether large postal operators should be allowed to merge to benefit from synergies and scale economies and sustain the provision of basic postal services.

In the **Netherlands**, there has been a debate on whether the incumbent postal operator, PostNL, was allowed to merge with its main competitor in the letter post segment, Sandd. In September 2019, the Deputy Minister of Economic Affairs and Climate Policy in the Netherlands approved the merger of the PostNL and Sandd postal networks. Sandd and PostNL were by far the two largest operators in the letter segment in the Netherlands. The decision to allow the merger was a political decision, which overruled the decision by the competition authority to block the merger. The competition authority was concerned that the merger would lead to significant price increases. However, the politicians found it to be necessary to allow the merger in order to ensure sustainability of the USP: “The combination of both postal networks is necessary to ensure continuity. As a result, postal services throughout the Netherlands will continue to be reliable, accessible and affordable, while also benefiting the job security of thousands of mail deliverers.”⁶⁰

In **Sweden** and **Denmark**, we have seen a merger in the postal sector, between the Danish Post Danmark (now PostNord) and the Swedish PostNord. However, it has been difficult for the company to harvest large synergies from the merger. In 2018, the Danish and Swedish states had to compensate PostNord for the cost of providing the USO and the European Commission is currently investigating the capital injections.

We expect to see more debates along these lines in the future following the market developments presented in Chapter 1.

2.2. Defining postal policies in light of changing user needs

Postal service users are moving away from letter post products and using digital forms of communication instead. At the same time, other social developments such as increased urbanisation and aging population increase the role of the USO, demanding a basic postal service level for vulnerable users in less-populated rural areas, or elderly that don't have access to digital alternatives of communication. The policy questions that emerge from this situation are: How can policy-makers change the postal USO in light of changing user needs? Does the level of disruption call for a “green field” approach (i.e. drafting regulation from scratch) or an incremental adjustment of a current framework?

⁶⁰ Post & Parcel *POSTNL AND SANDD MERGER APPROVED*, 2019 (<https://postandparcel.info/115016/news/postnl-and-sandd-merger-approved/>)

Besides the USO, new social needs may have evolved during this time and the USP can serve as the State's arm to provide services that cover these new needs. The policy question that emerges from this situation is: Can USPs provide other SGEI to cover new social needs?

2.2.1. How can policy-makers change the postal USO in light of changing user needs?

The ongoing technological, economic and societal developments are continuing to change the use of and need for postal services in the future. Policymakers at national level are increasingly reviewing postal policies to ensure that the current USO regulations are not becoming obsolete.

At the same time, there might be a need to protect vulnerable consumers, i.e. users that are dependent on postal services. In **Denmark**, where it is mandatory to communicate digitally with the public administration and businesses such as banks, still around 8-9 per cent of the population is eligible to receive paper-based communication because of handicaps or other impediments.⁶¹

A number of Member States have been reviewing and adjusting the scope of the USO in recent years.

In **Denmark**, many adjustments have been made to adapt to the developments in the postal sector. Throughout this process of changing the postal regulation, the Danish regulator considered user needs in different ways.

Danish citizens have historically sent a large number of letters. In 2003, 282 letters per capita were sent in Denmark. However, the Danish government undertook a number of e-government initiatives, culminating in 2014 with the obligation for citizens to communicate digitally with the government. Consequently, people started to use increasingly digital communication, leading to a steep decline in letter post volumes.

In 2014, the Danish regulator carried out a consumer survey on the usage of postal services by private individuals and companies. The survey found that both companies and private users decreasingly relied on letters, showing an average 32 per cent decline per annum in letter volumes over the period 2010-2017. Besides, people who sent letters more frequently had at the same time access to the internet and thus an alternative to the use of postal services. Based on these findings, the regulator concluded that an increase in the price of letter post product and a decrease in the speed of the non-priority letter product would not harm users.

In line with its conclusion, the regulator made the non-priority letter the new standard postal product and shifted on this letter product the focus of price regulation, abolishing the price cap on A-letters.⁶²

In **Italy**, the Italian postal regulator agreed to the introduction of a slower D+4 letter post product (Posta4) in 2015 as the new standard letter product, given changed user needs in terms of need for speed of letter post products. At the same time, the fastest D+1 product, Posta1, was maintained and kept within the USO scope but given more flexibility.⁶³

⁶¹ The State defines the citizens eligible to receive communication via letter post based on defined criteria. Source: interview with the Danish Consumer Council.

⁶² Voxmeter (2014), *Analyse af danskernes brug af posttjenester*.

⁶³ Copenhagen Economics (2018), *Main Developments in the Postal Sector (2013-2016)*; AGCOM, *Decision 395/15/CONS*.

2.2.2. Can USPs provide other Services of General Economic Interest to cover new social needs?

While the importance of paper-based communication may slowly be eroding, new social needs may have evolved during this time. This brings attention to the potential benefit of including new services in the obligation to the universal service provider. The existing postal network can be utilised to provide other kinds of SGEI, as an alternative to reducing the network.

In **France**, the USP provides four SGEI for which it receives compensation by the French State:

Firstly, it ensures a stable quality of service for universal postal products, where the new focus is on user satisfaction and tracking domestic and international shipments. Secondly, La Poste ensures a high-density postal coverage throughout France, over and above the universal service obligation, particularly in rural areas, through approximately 17 000 postal outlets.⁶⁴ Thirdly, La Poste takes part in the distribution of the press, i.e. print media, with privileged postal rates granted to newspaper publishers. Finally, it makes banking accessible to all, through La Poste's branch La Banque Postale, by providing banking services to vulnerable users (so-called "Livret A" savings accounts).⁶⁵

Currently La Poste's compensation is determined by a 5-year contract, from 2018 to 2022. It receives a financial compensation of EUR 174 million for the provision of contacts points throughout France and a financial compensation of EUR 210 million (in 2017) for the provision of banking services to vulnerable users. Furthermore, La Poste was granted a tax relief of EUR 850 million in total to ensure a high density of postal services over the period 2013-2017. Besides, it received a payment of EUR 597 million in total to fund La Poste's task of transporting and delivering the press over the period 2013-2015.

In addition, La Poste provides other public services, although they are not considered SGEI and are purely commercial. These are:

- Public administration services, e.g. written driver's licence exam;
- Social services to seniors (regular visits/checks; delivering groceries, medications and meal trays; installing home electronic devices such as satellite TV devices);
- Environmental services, supporting: (1) Energy renovation: raising property owners' awareness regarding energy renovation challenges, conducting energy assessments at private homes; (2) Recycling, e.g. recovering of paper, electronics, textiles and batteries; (3) Sustainable mobility consulting ("Bemobi").⁶⁶

In **Belgium**, the state has defined an SGEI mission in the 6th Management Contract for the period 2016-2020. It includes 14 different specific service obligations categorised into three categories:

- Retail network SGEI
- Day to day SGEI
- Ad hoc SGEI

⁶⁴ Post offices are gradually being replaced by partnerships with local shops and town halls as contact points that are cheaper to run and will therefore help to gradually reduce costs. Source: European Commission (2018) *Press release: State aid: Commission approves compensation granted by France to the French post office for its territorial coverage*.

⁶⁵ In addition, La Poste provides other public services, although they are not considered SGEI and are purely commercial, such as public administration services (e.g. written driver's licence exam), and social services to seniors (e.g. regular visits/checks, delivering groceries, medications and meal trays).

⁶⁶ Copenhagen Economics based on European Commission, *decision SA.36512 26-5-2014* and La Poste (2017), *2016 Annual Report*.

bpost's SGEI include various services, from the provision of a post office network and financial services, to the home payment of pensions.⁶⁷ The home delivery of pensions allows people with limited moving capabilities and old people to receive their benefits and pensions at home. This service is offered over the entire territory of the country at no additional charge.

In addition to the 6th Management Contract, bpost concluded concession agreements with the Belgian State following a tender procedure for the press distribution SGEI (2016-2020).

bpost receives compensation by the Belgian State for the provision of these SGEI. It receives financial compensation, ranging from EUR 92 million in 2016 to EUR 100 million in 2020 for the 6th Management Contract and from EUR 173 million in 2016 to EUR 166 million in 2020 for the press concessions. The European Commission reviewed bpost's compensation according to its state-aid rules. It noted that the Belgian State had confirmed the essential social and economic role of the public services entrusted to bpost and that the compensation is based on a robust methodology, which ensures that it will not exceed the net cost of the public service mission. This compensation mechanism also includes incentives for bpost to increase the efficiency and quality of its public services.⁶⁸

Additional SGEI might be ones related to digitisation. Examples may be the provision of digital mail boxes for digital communication with e.g. public authorities, and training and support in the use of digital forms of communication to vulnerable users, taking advantage of the USPs capillary presence in the Member States' territory. This comes in the natural trade-off between supporting digitisation and supporting the USP in handling the losses caused by digitisation.

2.3. Adapting regulatory frameworks to ensure efficient cross-border e-commerce delivery

The development of international e-commerce sectors creates new challenges of adapting existing regulatory frameworks, which have traditionally been focused on letter communication, and finding a balance with regulations outside the postal sector, such as transport and customs rules. European policy-makers have been discussing the following topics in these regards:

- What is the impact of the UPU terminal dues system?
- What is the impact of the VAT de minimis removal?
- What is the impact of non-postal rules on EU postal operators?

2.3.1. What is the impact of the UPU terminal dues system?

Most designated postal operators are only active in their national markets, so they must cooperate to deliver mail cross-border. The UPU system is an international inter-governmental set of agreements that regulates cross-border postal services between designated operators worldwide. A key element in the UPU system is the terminal dues, that governs payments between designated postal operators for the transport, sorting, and delivery of cross-border letter post items in the destination country.

The current UPU system for terminal dues is a two-tiered system: countries are divided into six groups belonging to two different systems called the *transitional system* and the *target system*:

⁶⁷ For example, Article 141 §1 of the Law of 1991 entrusts bpost with the execution of the service of doorstep payment of old age and surviving dependents' pensions and benefits for people with limited moving capabilities. This SGEI is further detailed in Art. 28 of the 6th Management Contract.

⁶⁸ Interview with bpost; https://europa.eu/rapid/press-release_IP-13-390_en.htm.

- The *transitional system* mainly applies to exchanges of international letter mail to, from, or between designated operators in countries traditionally considered ‘developing’.
- The *target system* mainly governs the exchange of letter post items between designated operators in countries and territories previously thought of as ‘industrialised’. In 2010, countries and territories classified as ‘developing’ started to join the target system. In 2016, China joined the target system, but it has maintained the terminal dues rates applicable to the transitional system.⁶⁹

Terminal dues rates, i.e. the payments between postal operators, are based on the UPU regulation set out in the 26th UPU Congress for the period of 2017 through 2020 and adjusted during the Third Extraordinary Congress that took place in Geneva in September 2019. The rates are different for the *transitional system* and the *target system* and are designed so that operators in the transitional system (i.e. postal operators from developing countries, such as African countries), do not pay a price that would be prohibitive for them when delivering mail to countries in the target system.

Hence, the terminal dues rates often differ from the compensation that the postal operators would require in a situation without the UPU terminal dues system in place. This has raised debates among postal sector stakeholders worldwide in recent years.

On one hand, the system creates synergies and overcomes transaction costs. The UPU system for terminal dues is an example of global multilateral coordination. Multilateral coordination, i.e. organised decision-making via an entity such as an international organisation (UPU in this case), overcomes the costs associated with unilateral coordination, i.e. pure market interaction between individual entities.⁷⁰

On the other hand, the system creates distortions. First, it creates a burden for some USPs. When a postal operator in a developing country, like Chinese Post, pays a price for final delivery in a developed country that is below cost, the USP in the developed country performing the final delivery loses money on those shipments.

Second, it distorts competition on cross-border shipments. The price below cost creates a competitive disadvantage for delivery companies like UPS that are not part of the system, and for national retailers if it becomes cheaper for consumers in developed economies to buy goods from developing countries as opposed to local sellers.

During the Third Extraordinary Congress in Geneva, the UPU member countries approved a compromise deal (Option V) designed to ‘save’ a single global postal system. Under this agreement, UPU member countries that meet certain requirements – including inbound letter post volumes in excess of 75 000 metric tons based on 2018 data – would be able to choose to self-declare their rates starting from 1st July 2020.⁷¹

The European Commission has now commissioned a study on the impact of the current UPU terminal dues system on the postal services sector, especially for e-commerce items.

⁶⁹ Copenhagen Economics (2017) *Terminal Dues. Impact on financial transfers among designated postal operators of the Universal Postal Union 2018-2021 cycle agreements*.

⁷⁰ According to transaction cost economics, following Nobel laureate Williamson. Source: Copenhagen Economics (2019), *Throwing away the baby with the bathwater? Economic literature on global coordination vs unilateralism: relevance to the UPU remuneration system and the future of the postal industry*.

⁷¹ I.e. increase their terminal dues rates, although according to certain parameters, including the 70% maximum compared to domestic tariffs. Sources: UPU 25.09.2019 - *Member countries attending the Universal Postal Union's third Extraordinary Congress today reached an agreement on international remuneration rates* (http://news.upu.int/no_cache/nd/upu-member-countries-reach-unanimous-agreement-on-postal-remuneration-rates/); CEP Research (2019) *USA claims “total victory” in UPU compromise deal*.

2.3.2. What is the impact of the VAT de minimis removal?

Cross border shipments entering the EU are subject to VAT. These shipments are exempt from VAT payments if their value is below a certain threshold (less than EUR 10-22, depending on the product category). This is called “VAT de minimis” and, in the EU as elsewhere in the world, is a relief given because of the relatively high transaction costs of tax collections on small value items.

However, given the increased flow of low value items from countries such as China, in December 2016, the European Commission proposed to modernise VAT rules for cross-border B2C e-commerce. The proposal is a bundle of policies, one of which is the removal of the de minimis VAT exemption.

The removal of the VAT de minimis has sparked debates in the EU postal sector, since it has potential implications on the sustainability of the USO (and consequently postal employees and funding of the postal operator), on customs processes, and e-commerce consumer experience.

The policy objective of removing the VAT de minimis is to create a fully level playing field. However, in practice this may come at a high cost, questioning the efficiency of this proposal. There are potential several negative consequences of removing the VAT de minimis.

First, for low value items, the cost of collecting VAT exceeds the collected revenue by a wide margin, and the removal of the de minimis would make it even worse. This is because the collection of VAT for each item is associated with administrative costs, which do not vary with the value of the item.

Second, these administrative costs are borne by delivery operators, custom authorities and e-sellers. The delivery industry would be significantly affected by the additional processing cost and postal operators in particular, since traditionally they handle the lion’s share of low-value items. This has consequences on the sustainability of the USO, postal employees and funding of the postal operator.

Third, EU households will ultimately pay a large share of this new administrative burden. The increased administrative cost will result in higher prices for consumers or loss of profit for businesses, both to the disadvantage for European welfare. Furthermore, customs agencies are public sector entities and the delivery industry includes several postal operators which are publicly owned. Thus, the implications of the EU VAT reform, which is about to be implemented, is that, once the new setup comes live, this brings additional costs to the national taxpayers, as well as to industry.⁷²

2.3.3. What is the impact of non-postal rules on EU postal operators?

The EU postal sector is shaped by policies and regulations in different related areas. These areas include the following:

- *Rules governing transportation* of goods such as requirements on working conditions for truck drivers may represent an obstacle for postal operators in country A if they compete with drivers from country B that need to comply with looser requirements. For instance, different delivery operators might have to comply with different rules depending on whether they are registered as postal operators or logistics operators. An example is the case between DPDHL and UPS in Germany.⁷³
- *Customs procedures and rules* such as duties on imports/exports or free trade agreements may represent a burden for postal operators because they decrease the demand for cross-border shipments and increase the handling costs of duty collection. Moreover, any exemptions applied to universal service providers risk creating an unlevel playing field among postal operators within the EU.

⁷² Copenhagen Economics (2017), *Effects of removing the vat de minimis on e-commerce imports*.

⁷³ Interview with UPS; Pikamäe, P. (2019), *Schlussanträge des Generalanwalts Priit Pikamäe*.

- *Aviation sector regulations*, such as restrictions on flying objects, may represent a barrier to e.g. testing delivery by drones.
- *Environmental regulations* may restrict postal operators' mode and place of delivery. For example, mobility plans in cities, which impose car-free zones in order to reduce congestion in city centres and encourage the use of electric vehicles and bicycles, may result in increased costs for postal operators, both for the vehicles and for the recharging infrastructure.
- *Regulations on consumer privacy and safety*, such as the General Data Protection Regulation (GDPR), can represent an increased burden for postal operators.
- *Digital agendas* that mandate the public sector to move to digital-only communication can have a negative impact on letter post volumes.

3. CHALLENGES AND OPPORTUNITIES FOR THE EU POSTAL SECTOR

KEY FINDINGS

The sector faces many challenges that make it fragile and not to be taken for granted:

- The sustainability of some postal operators is at risk, given the letter volume decline and the competitive pressures from both digital alternatives and parcel sector players;
- The sector is transforming fast and at different paces in different Member States, making it challenging to regulate and not possible to apply a one-size-fits-all solution;
- User needs are changing, questioning the scope of the USO;
- Changing the USO raises the challenge of how to safeguard consumers who might still need access to basic postal services and who should pay for it;
- The postal sector's network is made of people, as opposed to sectors such as telecoms, meaning that (1) if its sustainability is broken it cannot be resold to a next buyer, and (2) it will be a challenge to shift the postal workforce to other jobs;
- Different delivery operators are subject to different rules;
- The EU postal sector faces pressures from outside the EU and from other sectors' regulations.

On the other hand, the EU postal sector can reap the opportunities that arise:

- The growing e-commerce and consequent increase in packets and parcels volumes;
- The USPs' network and brand value, that can be used to provide other services than postal;
- New operational technologies that can improve postal operators' efficiency.

3.1. Challenges facing the EU postal sector

The EU postal sector is an important sector that is going through important transformations in terms of digitalisation, changing user needs, presence of competing players, changes in business models, and changes in policies, as seen in the previous chapters. From the analyses in the previous chapters we have identified five main challenges that the EU postal sector and its stakeholders face.

The first challenge for the EU postal sector is **how to ensure the providers of the universal service can be profitable in the future.**

The postal sector is characterised by high economies of scale. This means that when letter volumes decline, the cost of processing and delivering the remaining letters does not decline as much.⁷⁴ Consequently, the unit cost per letter increases.

⁷⁴ The relationship between volume and cost decline is defined by the cost elasticity.

If the cost elasticity is 0.4⁷⁵, a 10 per cent volume decrease would only imply a decline in costs of 4 per cent. The total cost the operator is still facing to process and deliver the remaining letters is now divided across less letters, so the unit cost of one letter increases.

As consequences of letter volume decline, the postal operator has to:

- Cut costs. The postal sector is labour intensive, so cost cuts would usually translate in laying postal workers off. This connects to challenge 4: how to shift the postal workforce to other jobs.
- Increase prices. To cover the increased costs the operator has to increase its prices. This often requires changes in regulation, as we have seen in Chapter 2.

Price increases mean the remaining buyers will pay more. This will possibly induce them to buy even less letters, accelerating the volume decline. Hence, price increases may not be feasible to rely to ensure a viable mail operation.

The second challenge policy-makers at both EU and national level face is **what regulation level and forms to have for a sector that is transforming very fast and at different pace across the EU**. In these regards, national and EU regulators face challenges both in the letter and e-commerce segments. In the former, on whether and **how to adapt the USO to changing user needs**, as postal users are switching to digital alternatives and the USO might become obsolete. In the latter, on whether and how to regulate a new segment, where using the same conceptual frameworks as in the postal world may not be the answer that delivers the most socio-economic value for the EU.

Additionally, different EU countries are experiencing postal developments at different paces, making it challenging for EU policy-makers to adapt postal regulation at EU level. National postal sectors are structurally different – and hence, adapt differently – with respect, inter alia, to:

- The level of digitalisation of communications, e.g. communication with the government;
- Letter post volumes size and development;
- Size and scope of domestic and international e-commerce segment, which depends on the adoption by consumers, the level of digitisation, and the trust in e-commerce and payment systems;
- The costs the postal operators face, given e.g. different mail developments and level of automation;
- The level of competition in the sector;
- The type and composition of customers;
- The role of the State and the relationship between State and USP;
- The extent of other policies the national postal sector has to comply with.

The third challenge is **how to safeguard vulnerable users**, who might still need access to basic postal services at affordable rates if the USO is decreased and prices increased.

We find that users of postal services across Europe generally consent to having a slower delivery service for non-urgent items, with the option of a faster express delivery service for urgent, important items, e.g. medicine. Moreover, decrease in USO service level might represent an issue for users with addresses in sparsely populated and remote areas, who might be more dependent on fast delivery of

⁷⁵ Proposed by WIK Consult, see Figure 3-22 in WIK (2013), *Main Developments in the Postal Sector (2010-2013)*, a study for the European Commission.

physical letters than is the case in densely populated areas. This may be related to the demographics (e.g. higher share of elderly) in such areas or the possibility to use electronic alternatives (e.g. low degree of connectivity in such areas). Lastly, price increases of postal products might not be affordable for vulnerable users that are dependent on them. However, we note that letter affordability is not a general concern for regulators and policymakers anymore due to the decline in mail usage and the increased digitalisation of communications.

It is worth noting that initiatives from governments and consumer organizations, such as “Keep me posted” in the UK, advocate that postal consumers should maintain a free choice of receiving their communication from businesses and the government (bulk mail) in a physical form.

A number of initiatives can compensate for the decrease in USO:

- Initiatives that allow USPs to reach users in remote areas more efficiently. Examples are the use of mobile post offices (see the Lithuanian case in Section 1.5.3.b) and the use of virtual mail services. In **Finland**, between 2010 and 2013, the Finnish postal operator undertook several pilots for electronic delivery in rural areas, scanning letters and daily newspapers and delivering them in digital form. The pilot was successful from the user point view, but the scanning was too expensive for the postal operator, who decided not to roll-out the service on a broader basis.⁷⁶
- Subsidized envelopes or vouchers⁷⁷ could be used to support low-income vulnerable consumers in specifically hard circumstance.

*The fourth challenge is **how to shift the postal workforce to other jobs**.* The reduction in the USO (reduction of delivery frequency and post offices) and the increased use of new technologies that replace manual labour raise the challenge of how the many postal workers that will lose their jobs can become ready to take on other jobs.

*The fifth challenge is **how to ensure a level playing field for competing delivery operators*** when it comes to exemptions from certain rules (e.g. customs, VAT, transport) and State funding for universal service providers. The purpose of exemptions and funding is to support the USP in the provision of the USO. However, other delivery operators consider these exemptions as distortion of competition and urge to consider every channel of funding given to USPs as State aid and so subject it to scrutiny by the competent competition authority.

*The sixth challenge for EU policy-makers is **how to create a level playing field outside the EU*** for the EU online merchants and postal operators, in face of international rules, competition from outside the EU, and other policy objectives designed outside the postal sector (such as environmental targets and employment conditions).

An example of the policies designed outside the postal sector is the Member States’ Digital Agenda and the challenge is how to avoid Digital Agendas having a strong impact on the postal sector by mandating the public sector to move to digital-only in its communications with consumers and businesses. The Danish digital agenda has had a significant impact on the Danish postal sector, leading to the strongest letter volume decline in recent years (-12 per cent on average per year)⁷⁸.

⁷⁶ Itella Annual Reports 2010, 2013; Itella (2011) *Universal service and electronic delivery in Finland: Conclusions from Itella’s field experiment*, presentation at the 13th Koenigswinter Seminar on Postal Economics.

⁷⁷ As Ofcom, the UK regulator argued. Source: Ofcom (2013) *The affordability of universal postal services*.

⁷⁸ Between 2013 and 2017. Sources: European Commission, DG GROW statistics accessed on 16/07/2019 ([https://webgate.ec.europa.eu/grow/redisstat/databrowser/view/POST_CUBE1_X\\$POST_DTR_1/default/table?category=GROW_CURRENT](https://webgate.ec.europa.eu/grow/redisstat/databrowser/view/POST_CUBE1_X$POST_DTR_1/default/table?category=GROW_CURRENT)) and Copenhagen Economics (2018) *Main Developments in the Postal Sector 2013-2016*.

3.2. Opportunities arising for the EU postal sector

Along with the challenges, we see three main opportunities that arise from the current status of the EU postal sector.

The first opportunity for the EU postal sector is the **growing e-commerce industry** that increases the demand for lightweight packets and parcels delivery. If on one side postal operators are losing letter volumes, on the other they can take advantage of the increased flows of packets and parcels.

The second opportunity for both USPs and Member States is that the **USPs' network and brand value** can be used to provide other services than postal. If on the one hand owning a large network of post offices represents a burden for many USPs, on the other that network can be used to sell additional commercial services, such as banking. Additionally, the network infrastructure can be the "retail arm of the State", delivering publicly-relevant services – SGEI, the provision of a digital mailbox – in a more effective and efficient way than the State would itself. The provision of these services to the population is facilitated by the fact that the USP's brand is trusted by consumers.

The third opportunity are the **new operational technologies** that allow postal operators to improve their efficiency without sacrificing service quality. These are for example robotics for parcel sorting, automated vehicles with self-driving features, and drones, as described in Section 1.5.3.a.

4. RECOMMENDATIONS FOR EU POSTAL POLICY-MAKERS

KEY FINDINGS

Based on the developments analysed in previous chapters, we conclude on three recommendations for EU postal policy-makers both at national and EU level. Each recommendation represents a synthesis of market insights provided by different market stakeholders:

- Provide flexibility to ensure a sustainable USO and to define its role in light of changing user needs;
- Mind the impact on the environment and social conditions when designing postal policies;
- Create an international level playing field for the EU postal and e-commerce sector.

4.1. Provide flexibility to ensure a sustainable USO and to define its role in light of changing user needs

The developments in the EU postal sector described in the previous chapters have an impact on the sustainability of the USO and challenge its role in the society:

- Changing postal user needs challenge the role of the USO. Is the current USO still delivering social needs that would otherwise not be covered by the market on commercial terms? And are there other social needs that should be included (e.g. other SGEI)?
- The USO represents a burden for many universal service providers, given the pressures these operators are subject to, such as declining letter post volumes and competition from digital alternatives.
- Different Member States experience these developments and challenges at different paces. Some countries have displayed a steep letter volume decline and extensive e-government use, such as Denmark, while others have had a more stable letter post volume development, such as Germany.

Consequently, the postal regulatory paradigm must be kept in sync with changing market realities. The priority of policies should shift from the promotion of competition to the sustainability of the sector, taking into account national market realities. The future challenge in many Member States will not be to tame a profitable and inefficient monopoly (an old battle resonating more with the sector's performance back in the 80s and 90s), but to ensure that there is a viable postal operator, and different Member States are reaching this future at different paces.

As a result, the regulatory framework should provide enough flexibility for postal service providers to adapt to changing user needs as well as consider the increased need for compensation of the universal service providers. This has two implications for policies at the EU and national levels:

First, policies at EU level should provide **flexibility for Member States** to design postal policies at national level. These may include reviewing and reducing the scope of the USO where needed. The European Group of Postal Regulators (ERGP) supports this conclusion.⁷⁹ Moreover, policies at EU and national level should provide **more flexibility to universal postal operators** on how to provide and price the USO.

Second, we expect that **State aid rules** will play an important role in securing the sustainability of universal postal services. In these regards, State aid rules should ensure fast provision of funds, given the high pace of change of the postal sector, without harming competing non-USP operators.

4.2. Mind the impact on the environment and social conditions when designing postal policies

Postal policies and in particular the USO can be a driver of environmental impact, beside postal sector developments such as the change in product mix (less letters, more parcels).

The universal service obligation requires the USP in each country to deliver certain services at certain frequencies and speeds. This means that the USO causes environmental impact if it requires the USP to offer other services or structure its operations differently than it would have done absent the USO.

Furthermore, USO requirements, and in particular the required delivery frequency, may become an increasingly large driver of environmental impact per postal item in the future. This is likely to occur if letter mail volumes, and consequently letter mail revenues, decline significantly while delivery costs remain relatively unchanged.

Consequently, **the environmental footprint should be taken into account when evaluating changes to postal policies**. Maintaining a high delivery frequency in a sector with steep letter volume decline for example implies an increase in the environmental footprint per letter.⁸⁰

This means that first the **environmental impact of the postal sector should be measured**, since its true net effect is unknown. This is not a simple exercise and implies taking into account not only the impact of the postal operator, but also the impact from the behaviour of other market participants and consumers. A shorter route driven by the postal operator might imply that same route is driven by consumers instead, and vice versa.

Postal policies can also have an impact on social conditions. The postal sector is labour intensive and policies that promote competition as the main focus may encourage entry of players that offer poor conditions to their postal workers.

Following the change in the mail products mix and the strong competition in the parcel segment, we have observed (1) an increase in new and more flexible employment models (such as on-call work, temporary agency work, performance-related pay contracts) as well as outsourced models (such as subcontracted workers and self-employment), and (2) changes in employment conditions (e.g. performance pay).

Employee organizations have signalled that social conditions have been degrading, while postal operators see the change in employment contracts a natural adaptation following changes in user needs and use of new technologies.

⁷⁹ ERGP (2018), *Report on developments in the postal sector and implications for regulation*.

⁸⁰ In our study Copenhagen Economics (2017), *Effects of changing the USO in Norway*, we found that halving the delivery frequency would halve the need for vehicles, the time spent, and the fuel consumed in delivery, reducing the environmental impact.

Consequently, **social conditions should be taken into account when evaluating changes to postal policies**. The need for a postal license to operate in the postal sector is an example of a measure aimed at safeguarding fair competition. We also note that social conditions in the postal sector may be investigated further.

4.3. Create an international level playing field for the EU postal and e-commerce sector

Beside EU and national postal laws and regulations, the EU postal sector has to comply with global postal regulations, such as the UPU system for terminal dues, and policies external to the postal sector, such as transport and taxation regulations, both at EU and national level.

These policies might constrain the EU postal sector's profitability and impact social welfare:

First, the UPU system for terminal dues represents a burden for many universal service providers. Assessing the EU-wide impact of the significant reforms introduced at the UPU extraordinary Congress (September 2019), as well as a future united position of EU Member States in the UPU is likely to bring a better understanding on how to protect EU consumers' needs and provide a stronger negotiating position.

Second, it should be ensured that any **exemptions granted to USPs** in transportation regulations (e.g. sleep and rest requirements), VAT, and customs procedures are economically justified and do not harm competing postal operators. Also, it is important to ensure that differences in national policies do not create unfair competition and degradation of social conditions within the EU.

Third, it should be ensured that any **regulations in related areas** do not create barriers for innovation and development of new technologies and services. For example, *aviation sector regulations*, such as restrictions on flying objects, should be assessed with respect to whether they represent a barrier to either innovative business models (e.g. testing delivery by drones), as well as delivery models that rely on air fleet conveyance for domestic or international items. Also, *environmental regulations* should be designed in a way to promote postal operators to introduce innovative and more environmentally friendly modes of delivery. For example, mobility plans in cities, which impose car-free zones in order to reduce congestion in city centres and encourage the use of electric vehicles and bicycles, may result in increased costs for postal operators, both for the vehicles and for the recharging infrastructure.

4.4. Concluding notes

We are confident that both the reader familiar with the workings of the postal sector and the reader who is more novel will have found many insights and developments that are surprising and signal the peculiar nature of the sector. The postal sector (supply- as well as demand-side) is "living in interesting times".

The policy-minded reviewer of the postal sector should thus abandon preconceptions. It is key to go beyond the experience that each of us has as sender of C2C items (letters and parcels) and keep in mind that the vast majority of postal items are either bulk mail or bulk parcels procured out of a small number of wholesale customers. This is an important sensitivity factor for the sector, since the decisions of few buyers (the largest) can shape the market outcome for the sector as a whole – perhaps even more than the intervention of public authorities.

The observer of the postal sector can admire the extent of ongoing diversification and reinvention of long-storied businesses – a process the extent of which probably has no par when comparing to other network industries. This is unsurprising, since most other network industries feature different industrial

structures (more sunk costs, more capital needed, unlike the labour-heavy postal sector) and different barriers to entry and exit.

It is thus valuable for policymakers to consider how they can best accompany the postal sector along its trajectory of innovation, business experimentation and management of market and regulatory risk. Given the dynamics (and potential instability) of the sector, policy-makers should be aware of the possibility that any new sectoral laws and policies may fail to be future-proof, as well as the risk of regulatory failure.

That notwithstanding, the writing is not on the wall for the postal sector. In fact, never as before, postal operators can be masters of their own destiny and many have embraced the possibilities that change can bring. The sector is in the midst of a journey of transformation. For this journey to succeed, it is important that the policymakers ensure regulation is appropriate to our times and provides sufficient flexibility for this transformation to take place.

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This study aims at providing the European Parliament's TRAN Committee with an overview of the EU postal services sector, including recent developments, and recommendations for EU policy-makers on how to further stimulate growth and competitiveness of the sector.

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