

Revised Market Opening Timetable 2004

MUA Response to Postcomm's Consultation

1. OVERVIEW OF MUA

Mail Users Association was formed in the 1970's when a number of major business mailers joined forces to fight for the restoration of postal services at a time of escalating prices and deteriorating quality of service.

MUA is Britain's only independent association of business users concerned wholly with postal affairs. Its members are drawn from a wide range of business interests including Direct Mail, Banking and Finance, Communications, Publishing and postal related industries.

MUA's primary objective is to secure a healthy and cost effective set of postal services for all domestic and business users. This not only applies to physical mail, but also includes electronic and hybrid mail areas.

2. POSTCOMM'S REVISED MARKET REVIEW

2.1 Introduction

MUA thanks Postcomm for the opportunity to respond to its Revised Market Opening Timetable consultation, and have reviewed the Regulator's proposals alongside the related Competitive Market Review consultation. This document should be considered as MUA's formal response to both documents. This is in recognition of the fact that whilst the latter is viewed by members as providing extensive information about the postal services market, they did not consider there are substantive consultation issues contained within it, which could not be dealt with in the former consultation.

MUA would start by stating its mutual support for Postcomm's vision for the market, stated as being 'to attain a range of reliable, innovative and efficient postal services, including the universal postal service, valued by customers, and delivered through a competitive market'. MUA's long held view as an organisation shares similar sentiments, and its members remain committed to attaining this goal.

Members would caveat this statement, however, by noting that they do not consider Postcomm should preclude the possibility in the future of there being more than one provider of universal services present in the market, i.e. a competing postal operator in a position to provide an equally comprehensive end-to-end product to Royal Mail, at a competitive price.

3. MAIN PROPOSALS

3.1 Market Opening

MUA would state that its members generally show support for the Regulator's proposal to revise its timetable for market opening. They concur with Postcomm's view that its existing strategy has allowed only the minimal market development, and that the absence of developing competition (estimated by Postcomm as being only 0.3% of a growing market), has been due to a number of significant barriers to entry that have deterred other postal operators from entering the market.

MUA believes the most significant of these barriers is Royal Mail's VAT exempt status. Members believe this is where the Regulator must focus its full energy, for as long as Royal Mail's VAT exemption remains in place, full and realistic competition on a level playing field, will be limited.

In the meantime, MUA members believe Royal Mail will retain significant market share, and their ability to provide the universal service is unlikely to be affected by full market opening, particularly given that until sustainable end-to-end delivery networks are in place, Royal Mail will continue to receive mail under access agreements (negotiated on commercial terms) which the Industry must assume is still profitable for Royal Mail at 13/13.75p per item. Indeed, as Postcomm states even Royal Mail have 'now accepted that access can make a profitable contribution to its business and it is a strategic advantage to maintain its competitive position in delivery'¹.

In so far as other barriers to entry are concerned, MUA members also support the following statements made in Postcomm's Competitive Market Review document:

- Postcomm's proposal to ensure there is a greater degree of separation by pipeline activity in Royal Mail's regulatory accounts;
- Postcomm's continuing advice to government that a solution needs to be found for Royal Mail's VAT exempt status, and that a reduced rate applied to postal services might be one way to achieve this;
- Postcomm's plans to take a more proactive approach to ensuring anti-competitive behaviour does not occur (or is dealt with quickly), by increasing resources devoted to this issue;

¹ Postcomm Consultation document – Page 20 – Paragraph 2.47

- and, Postcomm's intention to undertake a programme of visits and events aimed at raising customers' awareness of the market opening timetable and competition.

MUA also fully supports Postcomm in its intention to review its licensing regime in advance of full market opening, in order to revitalise postal users' confidence in the operators that provide their postal services and guard against future mail integrity mishaps that compromise customers appetite for 'switching'.

3.2 Licensing

MUA believes wherever necessary, new entrants must have the support of the Regulator to facilitate entry and innovation in developing their businesses, without arbitrary regulatory restrictions on their business models. Members therefore also support the concept of a 'light touch' approach to Postcomm's licensing regime, so that it does not act as a barrier to entry itself, and the establishment of a benchmark Code of Practice with which licensed operators will be required to comply.

This having been said, however, once sufficient competition has entered the market and customer confidence is high, members believe the market will self-regulate, eliminating operators who fail to comply to industry standards, and consequently a less formal 'registration' system is all that will be required. Bulk mailers would argue this on the grounds that the terms and conditions of customer/operator agreements will ensure appropriate standards of mail integrity are maintained.

On the other hand, members would also support Postcomm's view that where there is no effective competition in the market, licensing would be necessary to facilitate competition and innovation, and to protect the interests of consumers.

3.3 Royal Mail Pricing

As stated in MUA's response to Postcomm recent 'Payment by Channel' consultation, MUA members in general support the principle of more cost reflective pricing. They can also identify with Royal Mail's desire to be able to price more flexibly in order to respond to competitive developments and act in a commercial manner.

Members would however strike a cautionary note in respect of the thin line between the pricing strategies proposed by Royal Mail to rectify price alignment with the costs of handling mail, and those that arguably verge on anti competitive behaviour. By its own admission, Postcomm has yet to get a full handle on Royal Mail's price allocation system², and MUA's very real concern is that Royal Mail in their endeavour to 'fight for every letter'³, might walk too closely to the line.

In the case of Payment Channel discounts, MUA members with supply side interests have pointed out that the proposals could be interpreted as having anti competitive motives. Stamped mail is likely to be the area subject to the least competitive pressure and thus likely to retain the highest price elasticity. The metered mail sent typically by small businesses already faces some competition which can be expected to increase further, whilst large business PPI mail is likely to see the lion's share of interest from competitors. Members consider it is therefore fair to question the motives of Royal Mail in making such a move, particularly in light of the fact that they have not at the same time chosen to better align their prices to costs in the 2nd class Metered/PPI mailstreams.

The main point MUA members are trying to make here is that it is therefore particularly important that Royal Mail's arguments for these changes on cost reflectivity grounds are based on cost data which is as transparent as possible, and in which Postcomm is able to express full confidence. Members therefore fully support the substance of Postcomm's statement that it 'needs to ensure Royal Mail does not abuse its pricing flexibility to foreclose the market to competition'⁴.

With regard to Geographic Pricing, the potential benefits to large volume mailers of Royal Mail geographically de-averaging non-universal service products prices is difficult to assess without a pricing matrix and cost allocation model being available. However members are generally of the view that in what is presently an all but captive market, the disadvantages are likely to outweigh the benefits. Suffice to say it would be dependent on an individual company's geographic fall-to-ground profile.

Members would also point out to Postcomm that it should be mindful of the administrative burden, mail acceptance procedures, and overall complexity of manifesting and rating the mail that zonal based solutions could place on customers.

² Postcomm's Revised Market Opening consultation document – Page 32 – Paragraph 3.31

³ Postcomm's Revised Market Opening consultation document – Page XV – Paragraph S.60

⁴ Postcomm's Revised Market Opening consultation document – Page 33 – Paragraph 3.35

3.4 Bulk Mail

As stated in MUA's formal submission to Postcomm's 'Universal Service' consultation in March 2004, members continue to have concerns around the scope of the universal service, and the knock on effect product removal will have in an uncompetitive market. On balance members continue to believe the most appropriate approach is to retain a comprehensive range of bulk mail products in the universal service. Their argument being that products can then be released from the universal service obligation under license, as and when sustainable competition emerges and becomes effective.

MUA therefore has strong reservations in Postcomm's proposals to remove all but Mailsort 1400 from Royal Mail's bulk mail universal service obligation, on the basis that without such competition being present, there is a very real risk that certain sectors of the market, may be disadvantaged by doing so, and consequently have nowhere else to turn to but to other forms of alternative media (e.g. electronic substitution). For instance, until viable competition emerges, an SME mailer (mailing Mailsort 120 items) may find themselves in a position whereby they are compromised in pricing terms by geographically de-averaged pricing, and in costs terms by being forced to move to 1400 way sortation.

Member would therefore strongly recommend Postcomm carry out further analysis on a product by product basis, in order to ascertain which sectors of the market will be most impacted by its proposed way forward. Members would also suggest that it might also be more sensible to hold off from decisions on bulk mail provision until either the next formal review of the constituent parts of the USO, or Royal Mail's market share has demonstrably fallen below an agreed level⁵.

MUA would also recommend a compromise position whereby products falling outside the universal service obligation (i.e. in Postcomm's Category 2 'within the scope of the universal service' category), receive uniform geographic pricing mandates until such time as sufficient competition has entered the market for Royal Mail to make a viable case for needing to move to geographic pricing. Until such a point, in light of the evident rewards Royal Mail are presently reaping from the constituent

⁵ A membership suggestion being that if the top 30 customers accounts for 25% of the market, then a level could be set based on the assumption that the market would be seen to be open if Royal Mail's market share fell to X%

parts of its 'Renewal Program'⁶, MUA members consider it is certainly in a strong enough financial position to support its activities in the face of such limited competition.

3.5 Access

MUA members agree with Postcomm that the barriers to entry experienced by entrants to the market 'have been compounded by the uncertainty caused by the considerable delay in Royal Mail agreeing terms with other operators over downstream access to its delivery network'⁷. As stated in previous consultation responses, MUA members would again emphasise the importance of Postcomm playing an active role in the development of benchmark network access arrangements.

Members are therefore reassured to see Postcomm's stated commitment to a full review of interoperability arrangements and access pricing, along with the work it is carrying out with Royal Mail and presumably other operators to develop fair and practical arrangements for sharing the advantages of the established postal infrastructure. For the time being, in the absence of a universally agreed access code, members would also argue strongly that access pricing needs to be subject to regulatory oversight.

Finally, at the expense of perhaps stating the obvious, MUA members believe Postcomm has a duty to ensure that the access regime works, given that it will be sometime before end-to-end competition to Royal Mail has developed to the extent necessary to ensure that Royal Mail is forced to respond to real market forces.

⁶ These being Single Day Delivery, the Transport Review, and the Mail Centre Review (Ref Postcomm's Revised Market Opening consultation document – Page V – Paragraph S.20, & Page 13 – Paragraph 2.23

⁷ Postcomm Revised Market Opening consultation document – Page IV – Paragraph S16
