Annex

SUMMARY OF POSTCOMM'S ANSWERS TO QUESTIONS 1 TO 13 ON TERM OF REFERENCE 1 AND 14 TO 19 ON TERM OF REFERENCE 2

	Questions about Term of Reference No1 "assess the impacts to date of liberalisation of the UK postal services market, including on the Royal Mail, alternative carriers and consumers"
Q.1	What do you consider to be the essential aims of, and vision for, a postal service in the 21st century?
A.1	Postcomm has for some time, in order to clearly articulate what it is aiming to achieve in the discharge of its functions, set out its vision for the postal market. Our vision is: *A range of reliable, innovative and efficient services, including a universal service reflecting the needs of users, valued by customers, and delivered through a successful Royal Mail and a sustainable competitive market.* We believe that this vision serves as an appropriate statement of the essential aims of, and vision for, the postal service as a whole in the 21st century. See paragraph 5.1.
Q.2	What has been the impact of liberalisation, so far, on: (a) social consumers sending and receiving mail; (b) SMEs sending and receiving mail; (c) large companies sending and receiving mail. in terms of the price of services, the choice of services to suit particular needs, and the quality of service.
A.2	Business and social consumers have benefitted from an improvement in Royal Mail's quality of service (principally end-to-end transit times). The experience of senders of mail varies depending on the volumes of mail they send. Senders of large volumes have also experienced improved choice and customer service, and a reduction in real price. These benefits are beginning to extend to SMEs. Senders of small volumes including social consumers have not been adversely affected, other than facing higher, but affordable prices, but they have not yet seen increased choice. There has been some deterioration in the service specification, with the elimination of second deliveries and later delivery and earlier collection times. Our assessment of the impact of liberalisation is set out in Chapter 3 paragraphs 3.1 to 3.6.

Q.3	What has been the impact of liberalisation, so far, on: (a) people in rural areas; (b) people with disabilities; (c) senior citizens; (d) people in areas which receive relatively little mail.;
A.3	As senders of mail, customers in these groups will have experienced higher quality of service levels. While prices have risen these prices remain affordable and research shows that mail continues to be perceived as offering good value. Special Delivery services continue to be provided and there has been no change in the provision of postal services for blind and partially sighted customers. As recipients of mail, customers in these groups will also, as have all recipients of mail, experienced the loss of the second delivery, and, in some cases, later delivery and earlier collection times. Indeed some members of these groups such as those in rural areas may have benefited from the reduction in those addresses which do not receive deliveries to the door six days a week, due to difficulty of access of health and safety reasons. See paragraph 3.4 to 3.6.
Q.4	What has been the impact of liberalisation on Royal Mail?
A.4	The impact of liberalisation on Royal Mail has been in terms of the regulatory environment in which it has had to operate as well as in responding to competition. The impacts can be seen in terms of: • price control limiting its ability to raise prices above an agreed level, although in practice Royal Mail has not fully exploited the price limits set, partly due to the impact of competition and partly due to the threats from e-substitution; • as part of the price control framework Royal Mail has been incentivised to improve efficiency, quality of service and mail integrity. Efficiency, quality of service and mail integrity have all improved during the period of liberalisation and Royal mail has returned to profitability; • under the regulatory regime, and because Royal Mail still has 99% of all delivered mail, over 75% of upstream mail and competition is in its early stages, it is subject to a level of ex-ante scrutiny that, if not properly planned, can lead to delays in product and price launches; and • competition has directly, through Access, seen a 20% reduction in upstream volumes, but there has been a small decline in competitors delivering in the final mile. Competition has also challenged Royal Mail to respond through innovation and improved efficiency. See paragraphs 3.22 to 3.38.

Q.5	What has been the impact of liberalisation on alternative carriers?
A.5	Alternative operators have for the first time been able to compete in the letters market. The market presents significant challenges for new entrants these include Royal Mail's advantages of scope, scale and the VAT exemption which makes Royal Mail's unit costs lower than those of its competitors. Despite these challenges there were in March 2008 XX licensees in addition to Royal Mail. It has been estimated that the net annual economic benefits to the UK of opening the mail market to competition have already been £229 million and a net additional 3,300 jobs with new entrants have been created in such areas of the UK as Edinburgh, Runcorn, Leeds, Birmingham, Greenford, Croydon, Barking, Newcastle, Bristol and Swindon. The unregulated UK express industry has become a significant employer and now helps to support around 72,000 jobs. Employment in the UK express industry has been rising at an average rate of 6% a year since the mid-1990s. See paragraphs 3.7 to 3.21 and 3.39 to 3.46.
Q.6	To what extent has competition emerged since postal services were liberalised, and what kind of competition has developed? Please consider: (a) the collection and delivery of letters, packets and parcels (b) transactional mail, direct mail, social mail and publications (c) services for large businesses, SMEs and social consumers
A.6	Around 20% of all letters are now carried over at least part of their journey by carriers other than Royal Mail. Competition in the UK addressed letters market takes two forms: • upstream or Access competition - whereby operators offer an alternative to Royal Mail for its upstream collection from mail customers, processing the mail and trunking it to the Mail centre closest to the delivery destination. Royal Mail handle the final delivery, for which they are paid a price negotiated between Royal Mail and the operators; and • delivery (end-to-end) competition whereby operators offer an end-to-end service involving delivery to the customers' door or another pre-agreed delivery point. Competition in letters is most developed in the upstream collection of bulk business mailings. Letter delivery remains virtually a Royal Mail monopoly. The collection of social mail also remains a de facto Royal Mail monopoly. There has been competition in packets and parcels for many years. See paragraphs 3.7 to 3.21.

Q.7	Has liberalisation made an impact on any other groups?
A.7	In addition to the groups already identified, employees both within Royal Mail and in its competitors have been affected by liberalisation. A reduction of employees at Royal Mail has coincided with liberalisation and with an increase in employees in Royal Mail's competitors. See paragraphs 3.33 to 3.46. Within the mails industry there are businesses which are not always obviously visible, such as mail preparation and fulfilment, manufacturers of postal equipment such as letter and parcel sorting equipment, franking machines, trays and trolley, and IT suppliers. Impacts on these different groups are varied, depending on their exposure to the postal market, the particular issues that liberalisation raises for them and their flexibility in responding to those issues. The impact of liberalisation on these groups is not specifically addressed in Postcomm's response because Postcomm anticipates that the Panel will want to concentrate on the more clearly identifiable and major issues which face the postal industry.
Q.8	Have Royal Mail and new entrants been able to compete effectively and fairly?
A.8	Ensuring that effective and fair competition can take place has been a major priority for Postcomm and a lot remains to be done. Royal Mail has significant advantages of scope and scale and the privilege of a VAT exemption. Royal Mail's potential ability to abuse its dominant position through anti-competitive behaviour such as raising barriers to entry or offering more favourable terms for Access to the delivery network for its own upstream products than those offered to other operators, could frustrate many of the potential benefits from the introduction of competition. The current structure of Royal Mail's business operations and the current lack of a combination of adequate cost transparency and commercial or wholesale equivalence are also factors which limit the effectiveness of Postcomm's decisions and therefore the ability of Postcomm to facilitate the development of competition. See paragraphs 3.7 to 3.32 and 4.15, and 6.1 to 6.12.
Q.9	What can we learn about liberalisation in the UK from international experience?
A.9	Liberalisation has progressed in different ways in countries both within and outside of the EU. While it is important to be cautious when making comparison between the regulatory regimes (in part because of the very different political and geographic contexts) it is apparent that liberalisation whether full or partial has delivered significant benefits. The most important conclusions that Postcomm draws from international experience are that: • it is possible for incumbent national postal operators to be very much more efficient in liberalised markets • liberalisation does not negatively affect the ability to provide profitable nationwide postal services at reasonable price, and • in liberalised markets incumbent operators can work with other operators to provide customer focussed and innovative products which help to maintain the relevance of physical mail. See paragraphs 3.47 - 3.64.

Q.10	Which changes in the communications market do you consider have had an impact on postal services: (a) internet; (b) email; (c) text messaging on mobile telephones; (d) others?
A.10	Electronic services are now a real alternative to some forms of mail. There are however, because of the nature of the different forms of mail, factors which may encourage or discourage e-substitution. We also see significant growth in fulfilment mail, packets and parcels arising from the rapid growth in online shopping, which potentially provides a high added value opportunity to replace the likely loss of lower value but higher volume letter mail. The extent of the constraints on Royal Mail's ability to respond to liberalisation have become increasingly apparent as the growth of digital media has impacted more obviously on the mail market. See paragraphs 2.5, 3.23 and 5.1 to 5.12
Q.11	Can you quantify these changes?
A.11	It is possible to identify broad trends in mail volumes and these are referred to throughout Postcomm's response. The identification of specific causes for these trends is extremely difficult and Postcomm doubts if it is possible to quantify accurately the relative impact of, for example, non-e-mail internet changes as compared with e-mail changes.
Q.12	What is the relationship between e-fulfilment and e-substitution in terms of their impact on: (a) volume of postal business? (b) value of postal business?
A.12	Broadly, e-fulfilment increases the volume of postal business and e-substitution reduces the volume of postal business. In value terms, because e-fulfilment involves the conveyance and delivery of physical items, which are heavier and attract a higher postage than letters, the value of e-fulfilment is likely to compensate significantly for e-substitution and may, in due course, exceed it. However, different sorting equipment may be needed and there could be an issue as to what a postman physically can carry. See paragraphs 5.1 to 5.12

Q.13	What has been the impact of e-fulfilment and e-substitution for the following: (a) social consumers sending and receiving mail; (b) SMEs sending and receiving mail; (c) large companies sending and receiving mail; (d) Royal Mail; and (e) alternative carriers?
A.13	To the extent that these changes can be meaningfully identified, quantified and differentiated, they are dealt with in Chapter 5.
	Questions about Term of Reference No 2: "explore trends in future market development and the likely impact of these on Royal Mail, alternative carriers and consumers"
Q.14	What does international experience tell us about the challenges and opportunities facing the UK market?
A.14	We believe that as set out in response to Question 9 above and in Chapter 3 of our submission that liberalisation while presenting challenges also presents significant opportunities which will allow Royal Mail to become a more efficient, innovative and customer focussed operator. See paragraphs 3.47 - 3.64.,
Q.15	What factors might encourage – and discourage – the use of electronic services as an alternative to the postal service, for: (a) transactional mail; (b) direct mail; (c) social mail; (d) publications (such as magazines); (e) other purposes?
A.15	Both social and transactional mail is under pressure from e-substitution. The costs of electronic services, such as for customer acquisition, are lower than for physical mail. We believe, however, that there are aspects of mail that valuably differentiate it from other media and the extent to which these can be capitalised upon by product/service innovation. These include the personal and highly targeted characteristics of hard copy communication, together with the universality and accuracy of its address lists. Direct mail can for example be carefully targeted to customers using good quality mailing lists and is a reliable, hand delivered service, which is highly valued at a time when interaction is increasingly through the screen or the telephone. Also direct mail allows the customer to have a closer experience with some types of product than e-mail direct marketing, for example through product samples. Many consumer magazines are now offered online and companies increasingly are creating and publishing online digital magazines. However, many companies still see the benefit of sending customers a physical magazine which they can easily pick up and put down, share with friends and keep for as long as they wish. See paragraphs 2.5 to 2.14 and 5.1 to 5.12.

Q.16	In particular: (a) what advantages might consumers ascribe to paper mail, as the volume of electronic mail increases? (b) how far is environmental policy and regulation likely to affect the market, in either a positive or negative way? (c) to what extent can the postal sector successfully provide complementary services to other media channels, including broadcasters and companies advertising on the internet? (d) what innovations are likely, or possible, in the development of IT hardware and software, with implications for the postal sector?
A.16	For the purpose of this summary Postcomm draws the attention of the Panel to (a) the personal and physical characteristics of paper mail together with the highly targeted characteristics, universality and accuracy of address lists. See paragraph 5.3, (b) environmental pressures are becoming more relevant. These include the impact of vehicles for trunking and delivery, use of air for first class mail and waste implications of direct mail. See paragraph 2.8, (c) many postal users have experience of the advantages of co-ordinating physical and electronic mailings. In addition not everything can be digitised and products bought on line must be delivered. See paragraph 2.9 to 2.14, and (d) IT innovations include: the ongoing development of spam filters capable of screening out much of the promotional material sent over the internet, integration of mail systems with customers CRM databases to enable better targeting of mail, the provision of software solutions able to determine for customers the most cost effective postage packages for customers and the development of hybrid mail printed close to point of delivery. See paragraphs 2.9 – 2.14.
Q.17	Is it possible to provide evidence for these factors, as a basis for preparing projections for the future of the mail market?
A.17	The evidence of these factors that is available to Postcomm is set out in its submission and in the documents provided to the Panel since its appointment. Although it can difficult to use this evidence as a basis for preparing projections for the future of the mail market, because cause and effect cannot always be clearly established, Postcomm has no doubt that the Panel's intentions in this area are right and stands ready to provide the Panel with whatever assistance it requires.

Q.18	What factors may limit the ability of companies to enter the market, or their market share: (a) in providing upstream services? (b) in providing a downstream service? (c) other services?
A.18	Access operations have contributed to the health of the mail market. Access operators (upstream competitors) feel that they are treated as competitors by Royal Mail despite being Royal Mail’s largest customers. Access operators also believe that there are a number of issues that are perceived as impediments to the efficient management of Access agreements. There are large costs involved in putting in place a delivery network. A number of issues have been identified which seem likely to affect the success or otherwise of competition in delivery including market uncertainty, distortions introduced by the current VAT regime and Royal Mail’s considerable economies of scale and scope. See paragraphs 3.7 - 3.21.
Q.19	Are there three broad scenarios which you believe would provide a useful framework to test policy options? (Scenarios should focus on economic, environmental, social and technological changes outside the mail market, assuming that current policy is maintained in relation to the postal sector). Please give your own projections for the volume and cost of mail under each.
A.19	Postcomm identifies three broad scenarios in chapter 4 of its submission. Projections are made in relation to two of them, managed decline and transformation. Without significant changes the most probable outcome for Royal Mail is one of accelerating but managed decline. Postcomm does not believe that such an outcome would be either desirable or inevitable.