

Hermes UK response to Ofcom's Call for Inputs: Review of Postal Regulation

Introduction

Hermes UK is the second largest parcel company in the UK. We deliver parcels for some of the largest retailers, both online and on the High Street, including John Lewis, M&S, Next and Asos, as well as SME's and small independent sellers. In addition, we offer consumer to consumer parcel delivery and collection available from one of our 5,200 Parcel Shops or delivery to one of 1,100 lockers.

Hermes delivers to every address in the UK and provides services seven days a week. In 2019 we delivered 390 million domestic and international parcels. In 2020 this rose to 648 million parcels due to the impact of Covid-19 and the closure of non-essential retail. On our busiest peak day in 2020, we processed 3.5 million parcels, up 1 million on our busiest day in 2019.

Hermes has two parcel sorting hubs in, from where all our parcels feed into our network of 31 depots across the UK, for onward distribution to over 600 delivery units, from where our couriers collect parcels for final mile delivery. We also have a dedicated returns hub in Rugby. In September 2022 we will open a new parcel sorting hub in Barnsley, which will be able to process around 1 million parcels a day initially, increasing to 2.1 million by 2025.

Covid-19

In 2020 our parcel volumes rose by just over 60% compared with the previous year. This created some operational challenges which had to be overcome quickly so that the sorting and delivery of parcels could continue to meet the needs of our clients and consumers.

At the start of the pandemic in March 2020, we introduced measures to protect our couriers and consumers. One of these changes was to introduce contactless deliveries, where the consumer did not physically hand the parcel to the consumer but placed it on the floor for the consumer to pick up and took a photo to prove delivery. If a parcel required a signature, the courier would sign on behalf of the courier and take a photo to confirm delivery had taken place. We also introduced a £1 million courier support fund, to provide daily payments to couriers if they needed to self-isolate with Covid-19 symptoms so they would have access to a payment commensurate with statutory sick pay, so they would not feel compelled to work when unwell and potentially a risk to others.

We implemented social distancing and safe systems of work measures in our hubs, depots and delivery units, following government guidance and carrying out individual site-specific risk assessments. This included, but was not limited to, marking 2 metre spaces on parcel sorting belts, dividing the work space into zones to further reduce contact, creating one way walk ways, providing PPE, wipes and hand sanitiser to all sites, staggering start and end times of shifts to reduce the numbers of workers arriving and leaving at any one time and increasing the frequency of site cleans.

Productivity reduced by around 20% due to social distancing requirements which limited the number of people who could work closely to unload and sort parcels.

There was a noticeable change in the types of parcels being sent during the first lockdown, from small and lightweight clothing items, to bulkier items such as toilet rolls, pet food and cleaning equipment. These larger items reduced the capacity on our trailers by around 20%, meaning that we needed to

increase our fleet size to transport parcels to our sites, resulting in more trips and an increase labour resource to drive the vehicles.

The huge growth in parcel volumes during 2020 meant we accelerated planned investments and spent £100 million in expanding our network. This included opening more parcel sorting sites, including some short-term 'pop up' sites, recruiting 1,500 new staff and 10,000 self-employed couriers to accommodate the volumes and future proof our network for continued growth.

Response to Questions:

We have focussed our responses on questions where we have experience and/or a clear view to share.

Question 3.1: Do you consider Ofcom's overall regulatory approach remains appropriate for regulating postal services over the 5-year period (2022-27)?

- In competitive areas, such as the growing parcels segment of the postal market, Ofcom has introduced limited regulation only when necessary and appropriate. We welcome Ofcom's acknowledgment of the benefits of competition to consumers, including increased choice, service innovation and competitive prices.
- The parcels market is a highly competitive sector with multiple companies operating in it and offering end-to-end B2B, B2C and C2X services. We feel that the 'light touch' regulatory approach taken to date has allowed competition and innovation to thrive.
- Given the growth in the parcels sector in the last five years and the competitive nature of the market, which has delivered clear benefits for consumers in terms of choice, innovations and price, Hermes sees no immediate need for Ofcom to change its regulatory approach in this segment of the market.

Question 6.1: Do you think the parcels market is working well for all senders and receivers of parcels (such as online shoppers, market place sellers and/or small retailers)?

- As the call for inputs states, parcels are becoming more important to citizens and consumers in the UK and Covid-19 has accelerated volume growth.
- Research carried out by Citizens Advice in 2017, mentioned in the call for inputs, states that 94% of consumers report a satisfactory or high quality of parcel delivery services and Ofcom's 2020 residential postal tracker shows 84% of users of postal services are satisfied with the service.
- The parcels segment of the postal market is highly competitive, with many operators offering B2C and C2X services six and sometimes seven days a week. Consumers sending C2X parcels have wide choice between carriers and can access these services online as well as instore, in the case of Hermes ParcelShops.
- In the B2C segment while retailers select the delivery company, they too have a range of companies to choose from and many retailers use several delivery companies, often choosing one for next day and one for standard delivery. As already mentioned, in some cases retailers also give the consumer the choice between delivery companies, often based on price and standard/next day options.
- Consumers are kept well informed about the parcel journey with text and email updates and tracking. In the B2C segment, depending on the service purchased by the retailer, the consumer can be advised when their order is being processed, when it is dispatched to the delivery company, when the delivery company receives the parcel, when it is on its way to them as well as detailed information about the time of delivery. Hermes provides text and email data to consumers and consumers who download the Hermes app or use the web site

can access additional delivery options, such as 'in-flight' diversion and nominating a 'safe place' delivery option.

- Delivery and collection options in the parcel market has also evolved to offer more convenience to consumers. Consumers can choose to have a parcel delivered to a specified address (whether work or home), a ParcelShop or a locker. Those sending parcels with Hermes Send can take them to one of 5,200 Parcel Shops or arrange a collection from home from one of our couriers. Consumers can print labels and package items at home or print labels in a ParcelShop and we are currently trialling packageless deliveries, where consumers can bring their item to a ParcelShop with no packaging to send with Hermes.
- Consumers are long used to sending single piece items with Royal Mail via the Post Office. They might be less familiar with sending items with another company, even though they are likely to receive deliveries from them at home. The Hermes website aims to make this easy for consumers, walking them step by step through how to wrap a parcel, how to send a parcel, what they cannot send, differing levels of compensation, how to weigh a parcel and how to return a parcel. This kind of support and help will give consumers confidence in sending C2X parcels.
- The parcels market continues to innovate and develop new products and services to improve the experience of both clients and end consumers. These innovations include advances in tracking information, apps, delivery and sending options and locations and trials of new services. The competitive nature of the delivery sector means these types of innovations are important to ensure we give consumers and retailers more options in a crowded market.
- Our *My Places* service, available on the Hermes app and our website, allows consumers to set their home address, set a safe delivery place, set a preferred neighbour (or a neighbour to avoid) for alternative delivery if they are not home and set a map pin for an exact delivery location. Consumers can even upload a photo of their preferred delivery location, helping couriers to deliver to the right place and provide details of pin access codes to a garage or front porch. Soon they will also be able to choose a preferred ParcelShop or locker for delivery.
- In 2020 Hermes launched Hermes Play, a digital option which allows Hermes Send customers to send a personal video with their parcel which the recipient views by scanning a QR code via the Hermes app. Retailers can also use the option to communicate with their customers, sending videos with offers and promotions, or related to the product the recipient has bought. This innovation allows for more personalised parcel delivery for individuals sending parcels, especially when sending a gift, and for retailers to communicate directly with their customers, just as they would if they were making an in-store purchase.
- Hermes provides a comprehensive range of services for all elements of the parcel market, from C2X through to the range of B2C sellers, large omni channel retailers to SME's via online platforms.
- SME's with weekly volumes below 150 parcels can access our services via our website, which allows them to upload bulk parcel information. Parcels can either be collected by a courier or dropped off at a ParcelShop. When volumes exceed 150 parcels a week, senders become a business account, which offers bespoke account management and van parcel collection service.

Question 6.2: What is the nature and extent of detriment (if any) that consumers may suffer in the C2X or B2C segments of the parcels market?

Lost or damaged parcels:

- In any market there will always be some consumers who either have a poor experience or feel they have had one. In the parcels segment of the postal sector, the most common detriment consumers might experience are delayed delivery or lost or damaged parcels.
- Hermes delivered 648 million parcels in 2020. Sometimes parcels do get lost or damaged for several reasons: poor packaging which comes open, an address label becomes detached or a human or machine processing error sending the parcel to the wrong place.
- Where a consumer does have a poor experience, Hermes take steps to ensure that any detriment is minimal and resolved as efficiently as possible.
- Hermes offers varying levels of compensation for C2X customers so that should there be an issue such as loss or damage then the consumer sending the item will be compensated so they are not out of pocket. All items sent with Hermes are automatically covered to the value of £20 and this is included in the price of sending the item.
- We also have a maximum cover level of £300. If the consumer declares the value of an item to be more than £300 at the point of purchase they will be alerted that the item will only be covered for £300, so if they choose to send it with Hermes they do so at their own risk. This is made very clear to consumers and why we do encourage consumers to declare the true value of their item.
- We do sometimes incur issues with C2X consumers failing to insure their parcel for the correct amount. A consumer might opt for the basic £20 cover, then seek higher compensation for their parcel if it is lost or damaged or send an item with a value higher than £300 but fail to declare its true value. This can lead to an unhappy consumer experience, but not one caused by Hermes specifically or the wider parcels market and one which is entirely avoidable. We feel that we do all we can to be clear about levels of cover at the point of purchase and a consumer must enter the value of the item they are sending before they can purchase the service.

Geographical price differences:

- Another perceived area of detriment affecting some consumers is differences in delivery charges due to geographical location. This is something consumer bodies in Scotland and Northern Ireland have raised concerns about.
- Hermes works closely with consumer advocacy bodies, such as Citizens Advice, and we have signed up to their delivery charter for vulnerable users to access postal services and engaged directly with the Scottish Government on the topic of additional delivery charges for consumers in the Highlands and Islands of Scotland.

B2C services

- The geography of the UK makes the transport of goods to certain parts, including Northern Ireland and the Scottish Highlands and Islands more expensive. These areas have lower population density, meaning that the volumes of parcels being sent to these areas is lower, resulting in lower driver productivity and higher transportation costs, including ferry fares.
- The commercial agreements that Hermes has with retailers are negotiated individually and can be separated into two categories: A blended UK rate and a separate rate for certain areas and postcodes. These rates are negotiated based on several things: clients' preferences, volume forecasts of number of parcels predicted to be sent to areas of the UK, as well as the weight and/or volumetric measurements of the parcels.

- Retailers that opt for a blended UK rate may do so because their consumers are ordering from all over the UK in high enough volumes that having a standard rate with parcel operators is more cost efficient due to economies of scale. For example, a retailer sending tens of millions of parcels annually may opt for this as they may be offered a cheaper overall rate from operators.
- Retailers that have separate rates depending on geographical location may do so because their volumes are significantly lower to certain areas, with most of their volumes going to more highly populated urban areas. Therefore, having one cheaper rate for much of their volume and then a higher price for ad hoc/smaller volume is preferential. For a retailer sending less volume but whose consumers are in a more concentrated urban area due to target market then this approach would be more cost effective.
- The impact on consumers could be that a retailer which has different rates with their parcel operator may charge different delivery prices based on geographical location, whereas another retailer (who doesn't have different rates) may not – but any delivery charge to the consumer is ultimately set by the retailer.
- Consumers buying goods online are advised of any delivery charges at the point of sale. This is separate to the rates negotiated between Hermes and our clients. Some retailers may charge a flat rate, some may offer free delivery or charge less than they are paying their carrier, some may charge more than the rate the carrier charges to deliver the parcel, and some may factor delivery charges into the price of the goods and offer free delivery This is up to the retailer.
- As figure 6.3 demonstrates, parcel carriers negotiate with retailers on the rates that are agreed for parcel delivery, with retailers then setting the delivery prices for their customers. It is encouraging to see this important distinction acknowledged by Ofcom “that retail businesses ultimately set the charges for delivery to consumers”. There has been previous confusion that the parcel operator sets higher delivery rates for certain areas which are passed on to consumers.
- As also noted by Ofcom, “retailers always have a choice of at least two operators that do not vary their prices on the basis of geography”.

C2X services

- Hermes offers a consumer-to-anywhere (C2X) service, Hermes Send, allowing consumers to purchase delivery services via our website or our network of over 5,200 ParcelShops. The prices for the different services offered are publicly available on our website. Consumers enter the weight, value and contents of their parcel, choose next day or standard delivery and whether they want additional services such as a signature on delivery and are then quoted a delivery price.
- For Hermes C2X customers there is an additional service charge of £2.40 for delivering parcels to the Shetland Islands, the Hebrides, the Isle of Bute and the Isle of Man. This is a flat rate charge which is clear at the point of purchase due to the additional costs involved for parcel delivery and considering the reduced drop density in some areas.
- In April 2021 we introduced the additional charge of £2.40 for parcel delivery to and from Northern Ireland, this followed a review of all Hermes' C2X prices against the prices offered by other operators. The price increase also reflects additional customs information required for parcels moving from GB to Northern Ireland.
- Hermes' services, along with those of other parcel carriers, are available to consumers through various online resellers (e.g. Parcels2Go). Hermes does not control the prices that its services are re-sold to consumers at, therefore charges to anywhere in the UK can be higher or lower through re-sellers than by using Hermes's services directly.

Disabled consumers

- It is important that all consumers can access postal services, but this can sometimes prove challenging for disabled consumers. Consumers can book Hermes' parcel collections direct from home if this suits their needs and our couriers tend to get to know the consumers they regularly deliver to and their delivery preferences, whether this means allowing extra time to get to the door, not placing a parcel on the floor which a disabled consumer might have difficulty picking up or using a certain safe place for delivery.
- Hermes has signed up to Citizens Advice's delivery charter for operators pledging that our ParcelShops meet disability needs by having level access or ramps for wheel chair users and that these are reviewed annually and are also a requirement of new locations. We have also pledged that our website provides clear information on the accessibility features available (as well as services) at each Parcel Shop. The final pledge is that we will work with retailers to enable disabled consumers to specify additional delivery needs. This is something that Hermes C2X consumers are already able to do and we have and are continuing to work with clients on facilitating this for their consumers.
- We have also made changes to our website to allow for blind and visually impaired consumers to use screen readers or other assistive technologies. Consideration is also given to consumers with colour blindness and tunnel vision by ensuring contrast levels and content is designed to avoid causing seizures.

Question 6.3: How effective are the existing consumer protection measures for users of parcel services in particular CP3? Is a change in regulation needed to protect users of postal services (as senders and recipients) and if so, what measures?

- Consumer Protection Condition 3 outlines the obligation on postal operators in establishing a procedure for dealing with complaints. It also establishes a further, more detailed and rigorous obligation on the universal service provider, Royal Mail, on a full complaint handling procedure and redress for dealing with complaints of consumers of relevant postal services.
- It is our views that it is fair that Royal Mail is held to a different standard as the universal service provider.
- Hermes is currently making significant changes and improvements to our customer services facility. Early in 2020 we closed our call centre in India and brought all customer service provision back to the UK to improve quality. With all our operatives located in the UK, we took the opportunity to and create more localised customer service teams within our depots to be able to provide on the spot parcel information to consumers.
- We have invested £3million into a three-year consumer experience transformation project to provide more targeted support to consumers. We have taken customer service staff out of a central call centre and placed them in our depots. This allows enquiries to be dealt with by teams where the parcel is processed resulting in speedier resolutions, such as locating a parcel and getting it to a consumer.
- We have also made it simpler for consumers to contact Hermes and to find contact information on our web site. Consumers can now use an automated chatbot function on our website which asks a series of questions to obtain the required information which then directs the consumer's enquiry to the relevant customer service agents. This means that we are more available to consumers and there is a reduction in response and therefore resolution times for that enquiry. This service is open to all consumers regardless of whether they are a retailer customer or a Hermes' own customer. Previously our customer service staff assisted Hermes C2X customers and B2C consumers were directed back to the retailer they purchased from – sometimes at the retailers' request. For Hermes' own customers there is also a dedicated

telephone number. As changes to our service are relatively new, we are using consumer feedback and internal data to refine and improve systems.

- Preliminary findings, based on the first six months of the customer service changes shows that total resolution times have reduced by more than 50%, with resolution times reducing from an average of 5.1 days in September 2020 to 1.86 days in April 2021. In addition to this, 75% of consumer contacts are resolved first time. This means the consumer does not need to contact Hermes again after their initial contact.
- The competitive nature of the parcels market incentivises operators to provide a good, reliable service and to offer effective customer services to deal with and resolve enquiries when they arise.
- Postal operators work closely with their clients (retailers) on customer service issues around delivery and there is a contractual relationship between retailer and operator (based on retailer preference) where the consumer should go in the first instance. Some retailers ask Hermes to handle delivery related enquiries or complaints, whereas some retailers want to handle these themselves and then liaise with Hermes. This can cause confusion for consumers, who become frustrated when trying to contact the delivery company only to be sent back to the retailer.
- It is useful to make the distinction between enquiries and complaints when looking at consumer protection measures and complaints processes. Most contacts to Hermes are enquiries seeking an update of information on a parcel's location. These tend to be easily resolved and do not result in a complaint. Complaints tend to arise when a consumer has had a poor experience either sending or receiving a parcel which cannot be resolved to their satisfaction. It is important to distinguish between the two types of contact when looking at consumers' experiences of the market.
- Hermes recent and ongoing investment in our consumer experience transformation programme demonstrates our commitment to ensure consumers are well served by the parcels market and have course to redress if they feel poorly served. It is in our own best interest to invest in this area and ensure that it is accessible and effective for consumers. In addition to our current and ongoing transformation work we recently hired a Director of Consumer Experience. A new post which will oversee and shape the transformation work.

Question 6.4: Are there any changes to the universal service obligations required for parcels, such as including tracking for First/Second class services?

Tracked parcels

- Hermes is strongly against the inclusion of tracking for parcels in the USO. This would give Royal Mail an unfair competitive advantage over other parcel companies, allowing them to undercut competitors who offer tracking due to the absence of VAT on USO products, meaning Royal Mail would have a 20% price advantage. This would also mean reduced VAT receipts to the Treasury.
- Tracked services for parcels is already widely available from many other parcel companies at competitive prices and Hermes offers tracking as standard on all our parcels, whether purchased online or in one of our Parcel Shops.
- Ofcom's recent review of postal users' needs shows that most senders of C2X services currently choose non-tracked service and that tracking was not regarded as a priority issue for consumers when deciding which parcel operator to use.
- There is no clear reason to add to the USO something which the market is already providing at competitive rates. The USO suite of products is intended to ensure that, regardless of market developments, all consumers can access affordable postal services which meet their

reasonable needs. There is no evidence that consumers who wish to access tracked services cannot do so at affordable prices.

- There is a potential risk that if a tracked parcels service is included in the USO, that Royal Mail might choose to remove non-tracked services so that tracking becomes standard as is the case with other operators. Royal Mail may choose to charge more for this service, which would result in consumers paying more for a service that they do not see as a priority but having no access to a cheaper non-tracked option.
- With the VAT price advantage, Royal Mail would be able to demonstrate significant market power in the parcels market, damaging competition and consumer choice.

USO delivery days:

- Royal Mail is required to deliver specified parcel services five days a week. In reality, it delivers parcels six days a week, most likely (as Ofcom notes) as a result of its requirement to deliver letters six days a week. Royal Mail has stated that the best way to ensure that the USO continues to meet users' needs is to rebalance its service model towards parcels. This is, of course, an operational decision for Royal Mail. It is unclear if it has asked for the USO to be amended to reflect this desire to focus on parcels.
- Ofcom's user needs research shows that 98% of consumers would consider their needs met by 5-days a week parcel delivery, regardless of whether that included Saturday delivery or was limited to Monday to Friday delivery (figure 6.4 in the call for inputs). A similarly high number of SMEs also consider their needs met by five days a week delivery, 96% for Monday to Friday, rising slightly to 97% for five-day delivery which includes Saturday. Therefore, there is no clear consumer desire for six days a week parcel delivery which would support any changes to the USO on parcels.
- Most of Royal Mail's competitors already deliver six (or sometimes seven) days a week. As Ofcom notes, most of this volume is B2C, rather than the C2X volumes (which accounts for around 10-15% of volumes across all operators) which is what would be included in the USO.
- With the limited information available, it is unclear if Royal Mail is focussing on C2X USO parcels when thinking about rebalancing its service model towards parcels, or the more lucrative, higher volume B2C segment of the market. Changes to the USO on parcel delivery days would not benefit B2C volume as this is not part of the USO. We would like to understand more about what Royal Mail would like to see in terms of regulatory change.

Q 7.1 Does the current scope of access regulation remain appropriate or should this be changed and, if so, how and why?

- As Ofcom notes, some access operators have suggested that Royal Mail should be required by Ofcom to provide a lightweight parcels access service given its market position in the lightweight segment of the bulk parcels market. While the definition of lightweight varies between operators, we would consider this to be the 0 – 2kg weight category.
- Ofcom also notes that parcel operators are against this due to the damage a mandated parcels access service could have on end to end competition and the price advantage it might give to Royal Mail.
- Specifically, the potential damage to competition arising from this is based on a scenario where, if Ofcom were to mandate parcels access to Royal Mail's network and also impose a form of price control on this mandate, then the product would be VAT exempt and therefore it would give Royal Mail a cost advantage relative to end-to-end parcel operators who would continue to have to levy VAT.
- Given the competitive nature of the parcels market and number of operators offering a range of different products and services, it is clear to us that access operators can be served through

contracts they can (and do) negotiate directly with Royal Mail's competitors and this is an attempt to obtain competitive advantage over parcel operators.

- We would be very concerned to see any regulatory intervention of this nature which would have a negative impact on end to end delivery in the parcels market.
- Royal Mail already has significant market power in the lightweight parcels category. Introducing a lightweight parcels access service would further enhance this power and do nothing to facilitate competition in this part of the parcels market. It might even lead to operators exiting this weight category, reducing competition for all consumers if Royal Mail secures significant access volumes.

Additional comments on areas not included in the CFI

Second-Class Safeguard Cap:

- In 2018 Ofcom reviewed the Second-Class Safeguard Cap which is designed to allow Royal Mail to make a reasonable commercial rate of return on the safeguarded products. Hermes remains concerned that Royal Mail's prices are not fully cost reflective as Ofcom acknowledged at the time that Royal Mail is pricing well below the cap and had been for some time due to poor pricing decisions it made in 2013/4 which allowed competitors, such as Hermes, to gain a foothold in the single piece C2X market.
- There seems to be an inconsistency between Royal Mail pricing significantly under the cap and Ofcom's assertion that there is insufficient competition to protect consumers. Hermes contends that the main reason Royal Mail is pricing significantly under the cap – which it does not do for letters, where prices are increased each year in line with CPI and where it tends to be closer to the roof of the cap – is that it is sufficiently concerned by the level of competition in the parcels market that it keeps its prices as low as possible. Something it can do given the additional advantage of the VAT exemption on the suite of products in the universal service.
- The fact that Royal Mail is charging well under the cap for parcels and large letters does not suggest that, were the cap to be removed, it would rush to increase prices, leaving consumers without access to affordable services. Indeed, Ofcom recognised at the time in the consultation that concern about reputational damage and political concerns may be contributing factors to Royal Mail's reluctance to increase prices.
- Ofcom's own consumer research at the time of the consultation suggested that price responsiveness is relatively low in parcels. Just 9% of residential consumers indicated they would send fewer parcels in response to a 10% price increase, and 3% indicated they would not send any parcels. Just 10% said they would send fewer, and 4% said they would not send any, in response to a 20% price increase. Among business users, just 3% said they would send fewer parcels in response to a 10% or a 20% price increase.
- The consultation suggested that this price insensitivity would not provide a strong constraint on Royal Mail's pricing. However, as already stated Royal Mail already has significant pricing freedom under the safeguard cap yet continues to set prices significantly below this cap.