



OFCOM'S REVIEW OF REGULATION – CALL FOR INPUTS

MAIL USERS' ASSOCIATION – FORMAL RESPONSE

Introduction

MUA seeks to champion the interests of the UK's large users of mail services.

MUA members represent UK companies who are senders of large volumes of mail originating from financial services, magazine publishers, mail producers, and mailing equipment and system providers. Collectively, MUA members account for in excess of 10% of the annual volume of mail posted in the UK.

MUA seeks an open and efficiently competitive market for mail services, which offers a wide choice of services with specifications, service quality and pricing that encourage the use of mail as a communications medium between businesses and their customers.

Given the high market power of Royal Mail and its monopoly in delivery of mail, MUA members believe effective regulation to mitigate that market power is a vital requirement for a healthy mail market, while ensuring the continuing, sustainable provision of the Universal Postal Service.

In that respect, we note Ofcom's statutory regulatory duties:

- to further the interests of consumers, where appropriate by promoting competition (Communications Act 2003); and
- to secure the provision of a universal postal service ... for the provision of a universal postal service to be financially sustainable ... for the provision of a universal postal service to be efficient and for its provision to continue to be efficient (Postal Services Act 2011)

MUA welcomes the opportunity to comment on Ofcom's Regulatory Review – Call for Input. Members have considered this in the context of Ofcom's 2020 Annual Monitoring Report, Ofcom's continuing work to understand the needs of mail users, and due consideration of the future regulatory framework for post.

Approach to Regulation

Question 3.1: Do you consider that Ofcom's overall regulatory approach remains appropriate for regulating postal services over the 5-year period (2022-2027)? If not, please explain the areas where you think changes should be made, with supporting evidence.

Although MUA members make comparatively less use of Royal Mail's USO services, than of Royal Mail's contract/non-USO services, they clearly see



that their use of non-USO services is a very large contributor to the revenue Royal Mail needs to sustain provision of the Universal Service. In essence, it is MUA members' use of non-USO services that significantly supports provision of USO services.

Ofcom's regulation of the UK postal market in general, and Royal Mail in particular, is therefore of keen interest to MUA. In that context, MUA Members would emphasise to Ofcom its statutory duties in relation to mail users. Ofcom refers to its statutory duty under the Postal Services Act 2011 'to secure the provision of a universal postal service, while having regard to its financial sustainability and efficiency'¹.

However, Ofcom also has a duty under that Act for Royal Mail's provision of the USO to 'be efficient before the end of a reasonable period and for its provision to continue to be efficient at all subsequent times'². MUA Members believe that, ten years on from the Act, it is clear Royal Mail's USO provision is not efficient and that Ofcom needs now to take regulatory steps to require efficiency improvement by Royal Mail.

MUA believes Ofcom must now have proper regard to its other primary statutory duty, under the Communications Act 2003, to further the interests of consumers in the markets that it regulates – including mail and the interests of major users such as MUA members.

As major users of mail, MUA members believe competition in the mail market is vital to the health of the market, leading to keener pricing and improved quality of service. However, under the present regulatory regime, Royal Mail has a monopoly in mail delivery. The only large-scale competitor (Whistl, then TNT Post) ceasing its final delivery operations as a result of Royal Mail's pricing behaviour, which Ofcom's existing regulatory regime did not prevent, and which the Regulator subsequently concluded was illegal. Hence, competition to Royal Mail is essentially confined to being through downstream access.

Furthermore, whilst the proportion of mail carried through downstream access has increased since the implementation of the present regulatory regime, there are now fewer access operators, than in 2012. As a result, choice for large mail users has lessened, not improved, and it can be said that competition (as far as it relates to choice for mail users), has declined during Ofcom's regulation. Also, the highly competitive nature of the upstream market has to a limited degree mitigated the increases in Royal Mail's prices for downstream access. However, MUA members believe the profit that can be earned by access operators is now at such slim margins, that their ability to invest in improved services is minimal.

In MUA Members' view, they would therefore state they consider the existing regulatory regime does not provide sufficient incentive for Royal Mail to

¹ Review of Regulation – Call for Inputs - Page 8 Para 2.19

² Review of Regulation – Call for Inputs - Page 8 Para 2.20



improve efficiency, or sufficient constraint on its behaviour, its ability to exercise its market power, and its terms and conditions, and does not enable effective competition.

Ofcom states in its Call for Input document that 'In 2012, we (The Regulator) explained our view that market conditions and shareholder discipline would be more likely to be effective in securing an efficient and financially sustainable universal postal service rather than imposing more regulation, such as wholesale or retail price controls and/or efficiency targets which could potentially increase the risk of regulatory failure³. And Ofcom maintained that view in the last Regulatory Review. Ofcom then goes on to say 'However, we also recognised that Royal Mail might have the incentive and ability to increase prices or decrease service levels, to the detriment of consumers, instead of taking on the efficiency challenge. This might be done in a way that resulted in a detriment to the universal service in the longer term by, for example, accelerating the market decline of letters⁴.

MUA Members would state they believe this is precisely where the Industry now finds itself. In an environment of year-on-year in some cases double digit price increases, against a backdrop of Royal Mail failing to meet efficiency performance targets, with consequent nominal improvements in quality of services levels.

MUA Members would also make the point that this is based on evidence from the results of Ofcom's year-on-year monitoring and analysis⁵, which consistently appear to indicate that there is a need for more regulatory control to constrain Royal Mail pricing policies, and equally the need for increased efficiency within the postal service, more generally. Members would state this is further exacerbated by concerns held by industry that as Royal Mail is clearly behind the curve on the rapidly growing area of its parcels business, the letters business appears to be taking the brunt of the efforts being made to support developments in the parcels sector.

In short, MUA members believe Ofcom's regulatory regime thus far, has not gone far enough to: sufficiently incentivise Royal Mail to drive forward efficiencies (including greater transparency); push the national carrier to enable development of competition through access; or offer protection to users through greater controls to ensure Royal Mail does not utilise revenue gained from the declining letters market, to support its ambitions in the parcels sector.

MUA members would therefore strongly urge Ofcom to consider further regulatory provision, such as some form of RPI-X pricing formula based on a price control/constraint covering a basket of bulk mail products and efficiency improvements, as a means of redressing this imbalance, and the changing market conditions.

³ Review of Regulation – Call for Inputs - Page 10 Para 3.10

⁴ Review of Regulation – Call for Inputs - Page 10 Para 3.11

⁵ Annual Monitoring Update on Postal Services Financial Year 2019-2020



Financial sustainability and efficiency

Question 4.1: Do you consider that Ofcom's current approach to financial sustainability and efficiency of the universal postal service will remain appropriate going forward? If not, please explain what changes you think should be made, with supporting evidence.

MUA members have been dismayed to see that Royal Mail has repeatedly failed to achieve its own, very modest targets for improved efficiency/productivity. Clearly, pressure to improve efficiency and pressure to limit price increases are related, and both would be present in a normally competitive market, but Royal Mail is not subject to such market pressures in relation to mail as it has extreme market power through its monopoly in mail delivery. Therefore, MUA members believe there is clear need and justification for Ofcom, as the regulator, to consider the application of external targets on Royal Mail for efficiency improvement.

MUA believes the key findings of Ofcom's most recent Annual Monitoring Review 2019-20, clearly show Royal Mail is not improving its efficiency as it needs to and/or could do, as there was no efficiency improvement in 2019/20 and efficiency actually worsened in 2018/19. Nor is Royal Mail improving its quality of service sufficiently, while using high price increases to provide support for its profits. As a result, Royal Mail's profitability trend raises great concern for the sustainability of Universal Service Provision, in the long term.

However, Ofcom to date has pursued a minimal regulatory intervention policy, believing the best approach is instead to allow time for Royal Mail's 5-Year strategy to be followed and achieved. MUA members are very concerned by this approach, given that Royal Mail's most recent financial announcement has cast much doubt on its ability to meet targets in its Journey 2024 plan, with increased likelihood that the part of Royal Mail which provides the Universal Service will be loss-making in 2020/21. It seems Ofcom is content to rely on Royal Mail's promises for future improvement, rather than any measures to require such improvement.

Ofcom's most recent Annual Monitoring Update, also highlights there has been a further 7.6% fall in mail volumes since 2019/20, with Royal Mail expecting a similar decline this year and next, yet price increases have largely offset the volume decline, such that mail revenue decline is less than half of volume decline at 2.9%. Royal Mail also did not achieve its productivity target of 2%, achieving instead only 1%, with efficiency performance remaining a real concern with real costs increasing by 1.4%, with no underlying efficiency improvements, excluding transformation costs.

In light of these concerning statistics, MUA Members strongly believe this is further evidence that in order for Ofcom to show it is acting in line with its statutory duties, it must seriously consider the need for, and means to, apply new regulatory measures that will set efficiency improvement targets for Royal Mail, and constraints on the level of price increases for bulk mail services.



Ofcom has the relevant information, and so is best placed to decide what the framework of any such provisions would look like.

Universal Service Obligations

Minimum Universal Service Requirements

Although recognising this matter doesn't fall within the direct scope of Ofcom's jurisdiction, it is clear to MUA that the Regulator's review of postal regulation and its informative research carried out on User Needs have, in turn, stimulated an equally important debate around the future scope of the USO delivery requirement.

MUA Members are, of course, cognisant of the fact that such decisions are a matter for Government/BEIS, but would nevertheless wish to formally make a statement regarding this, believing the two issues have important links to the subject matter of Ofcom's review.

This relates to the potential of an Industry stakeholder making a future case for the removal of Saturday from the Universal Service Provider's six-day requirement for the delivery of letters. This matter has been intimated in various discussions MUA has conducted with Ofcom, and has been briefly discussed with representatives of BEIS, as a result.

It is generally recognised that marketing mail attracts higher response rates when the letter is delivered on a Saturday, than on a weekday. There are also other types of mail, such as certain periodicals, where receipt of the item on a Saturday is an important feature of the service provided to the consumer. For other important correspondence (e.g. medical results or appointment notifications), delivery on 6-days including Saturday can make an important difference to the service offering.

When Ofcom published its User Needs Report, MUA (amongst other stakeholders) believed Ofcom had not properly considered such factors as these, and had looked too much at the needs of consumers and SMEs, when larger business users of mail were unlikely to have the same needs, and would see real impact if Saturday delivery were dropped.

Ofcom has subsequently responded that they were required to research the needs of USO users, and larger businesses don't use USO services. Whilst this may be true (to a degree), as previously stated it is the revenue Royal Mail gets from large businesses' use of non-USO services, that funds USO provision and RM offers non-USO services on the same service basis as USO services - so MUA members would argue it is erroneous of Ofcom to consider consumer/SME use of USO services, without also giving full consideration to how large mailers' use of non-USO services would be affected.



Whilst it is true consumers and SMEs are much less likely to be active users of mail on a Saturday (as many small businesses are not open for business on the weekend), many large volume mailers reciprocally consider Saturday delivery to be an important feature of the product offering.

MUA members understand from discussions with Ofcom that the Regulator has concluded dropping Saturday would have a significant financial benefit for Royal Mail, but there appears to have been little consideration to date of how this would impact large volume users (sending or receiving, USO or non-USO, larger users or small), or indeed what benefits might be offered to consumers for a degradation in the service offering.

MUA Members would suggest, therefore, that if a reduction in delivery days is to be considered, a full cost analysis and consideration of the pattern of mail delivery across the 6-day delivery window should be explored in greater detail. As initial indications from industry research suggest dropping a week day rather than Saturday, may be a more sensible option.

Question 5.4: Do you consider Ofcom's approach to regulating USO services, including access requirements, Special Delivery Guaranteed by 1pm, Signed For and Meter mail will remain appropriate going forward? If not, please explain what changes you think should be made, with supporting evidence.

In relation to paragraphs 5.71 – 5.73 where previously access operators have argued for the removal of metered mail from the universal service. MUA members would make the point that Metered mail is of course a payment channel and does support USO and non-USO products, in the same way as stamps are a payment channel.

Access operators have a threshold of collecting 250 letters, therefore to state that the removal of Meter mail will lead to more competition, does not stand up to scrutiny. They are not interested in collecting single piece mail. The majority of Metered mail users are from the SME community and value this channel with 14% using a franking machine, versus the 2% that use bulk mail services provided by other postal operators. 85% of SME Meter mail users stated that this method of sending mail was "important" or "very important" to their business. In a community that has been hard hit over the past year, making changes to the way they conduct their business would not be seen to be supportive to their organisations.

MUA would also make the point that from franking industry survey's, it has been found that the prime reason SME's use Meter mail is convenience, as for single piece mail there is little or no sortation and depositing the mail at a Post Office, Royal Mail collection, or inserting into a pillar box make the process simple. Some franking machine users do generate larger volumes, and for convenience, management information and flexibility, like to frank their mail.



This channel has been a feature of the postal market for almost 100 years and works very well for its users, and MUA is therefore of the view that it does not need to be further regulated or removed from the universal service.

More generally, MUA believes that Royal Mail needs to set out its general approach to barcoding, and likely policy and pricing about this. Whilst the trials of second-class stamp barcoding have been well publicised⁶ the overall approach and wider strategy remains unclear.

Question 6.4: Are there any changes to the universal service obligations required for parcels, such as including tracking for First/Second Class services? If so, please provide your views with supporting evidence.

MUA Members would like to highlight the lack of a tracked parcel product within the Meter channel USO portfolio, as Meter mail users are disadvantaged with the pricing of Special Delivery versus the products available via Click & Drop. Whilst Tracked 24/48 are not direct comparisons and fall outside the USO, the industry has seen an increase in the use of Signed For and Special Delivery during the pandemic, and MUA believes lobbying for a tracked 1st /2nd class product for parcels needs to be within the Ofcom scope of this call for inputs.

Access regulation

Question 7.2: How well is our approach to access price regulation working in supporting access-based competition? Are there any improvements or changes that we should make? If so, please provide your views with supporting evidence.

MUA has been and continues to be gravely concerned at the series of very large price increases imposed by Royal Mail for its contract mail services over the past several years. Many significantly above the rate of inflation; the most recent price increase, of nearly 10%, will have severe impact on the business of MUA members, and is most likely to lead only to an increased rate of decline in their use of mail. This fact is alluded to by Ofcom in its Call for Input document: that 'in some instances, price rises may risk accelerating the market decline of letters and potentially undermine the universal service in the longer term.'⁷

It is clear to MUA members that the absence of any large-scale competition to Royal Mail in the delivery of mail means Royal Mail is under no direct competitive threat that would cause it to limit its price increases. While there is

⁶ <https://postandparcel.info/135325/news/parcel/royal-mail-to-be-one-of-the-first-postal-authorities-to-add-unique-barcodes-to-stamps/>

⁷ Review of Regulation – Call for Inputs - Page 17 Para 4.10



indirect competition through e-commerce and e-billing/e-statements, it is apparent to us that such competition is not a sufficient control on Royal Mail price increases – especially in the area of business mail, which is of most importance to MUA members, and where Royal Mail has imposed the greatest price increases. MUA members therefore believe that in the absence of sufficient market forces to limit price increases, Ofcom as the Regulator should be actively considering whether and how appropriate price controls could be applied.