



Annual monitoring update on
the postal market
Financial year 2011-12

Market update

Publication date: 20 November 2012

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Section 1

Introduction

Summary

- 1.1 On 1 October 2011, responsibility for regulation of the postal sector transferred to Ofcom from Postcomm under the Postal Services Act 2011 ('the Act'). Our primary duty is to secure the provision of an efficient universal postal service.
- 1.2 On 27 March 2012 we published a statement – *Securing the Universal Postal Service, Decision on the new regulatory framework* ('the March 2012 statement').¹ In that document we set out the approach that Ofcom was taking to regulating the postal sector. This included the decision to give Royal Mail greater pricing freedom so that it is able to return the universal service to financial sustainability, subject to certain safeguards.
- 1.3 One of these safeguards was an effective and ongoing monitoring regime to track Royal Mail's performance in respect of quality of service and affordability for universal services, and progress on efficiency. As part of the monitoring programme, we also committed to publishing key postal market data in an annual update. This update is intended to set out the key trends in the sector, and in particular, the progress that is being made in terms of securing the provision of the universal service.

Setting a baseline for measuring the outcomes of Ofcom's new regulatory regime

- 1.4 This report sets out information about the postal market, and Royal Mail in particular, for the financial year that ended in March 2012, the last year under the old regulatory framework. This will form a baseline position for our future monitoring. It will also provide a baseline against which Ofcom can measure whether the new regulatory regime is achieving the desired outcomes.
- 1.5 The report covers the four key areas that the March 2012 statement said that we would focus on, namely:
 - Section Two - Royal Mail's financial performance
 - Section Three - Royal Mail's efficiency
 - Section Four - Customers and consumers
 - Section Five - Competition

¹ <http://stakeholders.ofcom.org.uk/binaries/consultations/review-of-regulatory-conditions/statement/statement.pdf>

The monitoring programme

1.6 Our monitoring programme includes:

- regular internal review of data and indicators for the four key areas set out above (including through our internal governance process);
- industry stakeholders providing market specific information and identifying any concerns with how the regime is operating and potential market developments;
- annual external statement setting out our view of how the regime is meeting our duty to secure the provision of a universal service (in the annual report); and
- increasing transparency by:
 - external publication by Royal Mail of some annual financial data;
 - publication of prices and changes to non-price terms and conditions by Royal Mail;
 - summary of market developments in Ofcom's annual Communications Market and International Communications Market reports; and
 - publication of additional key postal market data (subject to confidentiality) in an annual market update (of which this report is the first).

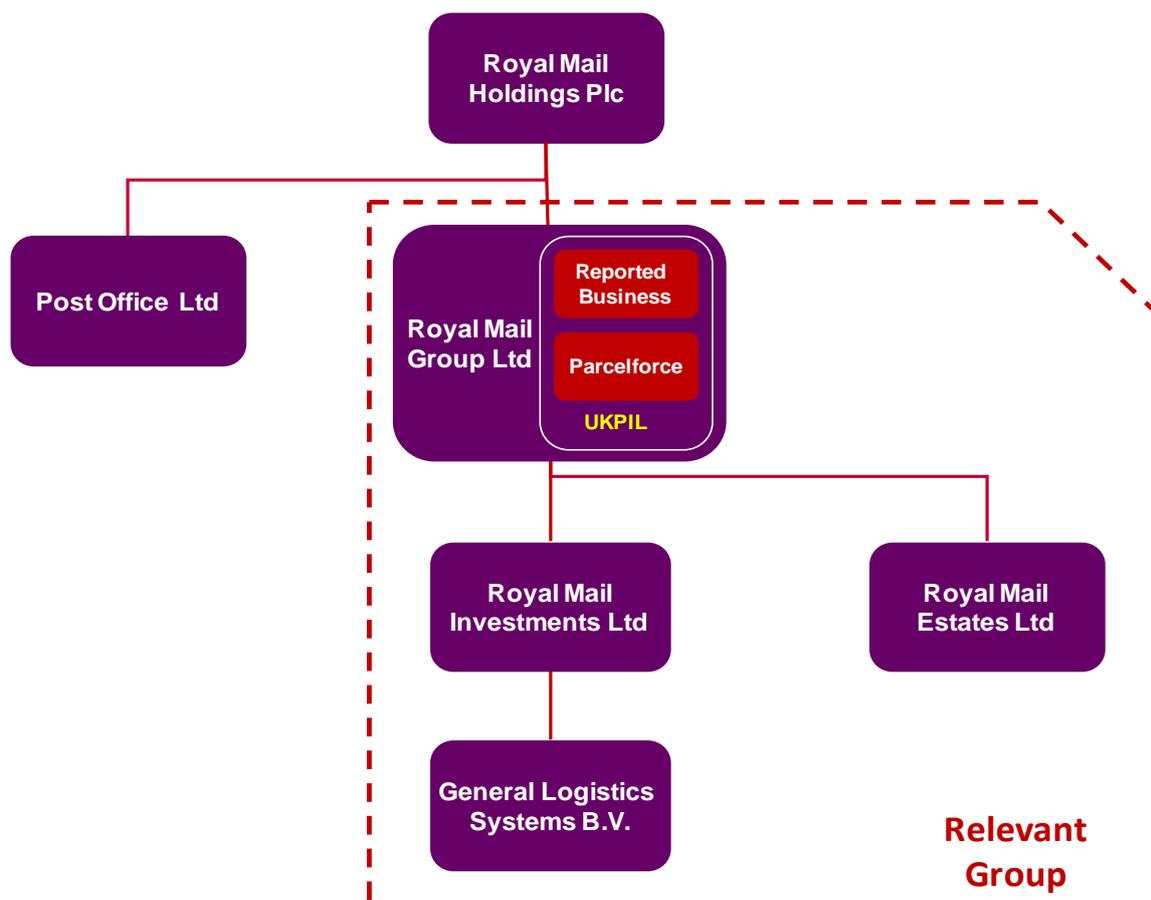
1.7 Royal Mail (along with other postal operators) provides to us a range of data on a confidential basis. Although the confidential nature of this data means that we cannot publish it, it will nonetheless inform our ongoing internal monitoring programme, and be used to identify any potential or emerging problems in relation to the ongoing provision of the universal service.

1.8 So that stakeholders are aware of the information that we gather, a list of data that we currently collect, some of which is not published for confidentiality reasons, is listed in Annex 1 to this report.

1.9 The focus of our monitoring is Royal Mail. Royal Mail is the designated universal service provider in the UK. It is the only postal business in the UK which currently operates a network capable of delivering letters and parcels to all 29 million business and household addresses nationwide.

1.10 However, not all of Royal Mail's business falls within our regulatory remit. The parts that are regulated are known as the 'Reported Business', which sits within a group of business units referred to by Royal Mail as UK PIL (UK Parcels, International and Letters). This, in turn, sits within a wider group of companies – the 'Relevant Group'. The structure of Royal Mail Group is shown in Figure 1.1 below.

Figure 1.1 – structure of Royal Mail Holdings plc



- 1.11 As the designated provider of the universal postal service, Royal Mail is subject to certain minimum requirements, as set out in the Act and the Postal Services (Universal Postal Service) Order 2012.² These requirements include providing priority (next day) and standard (within three days) delivery services and minimum quality of service targets. The Reported Business includes all universal services,³ as well as retail bulk mail⁴ and access products which also use the universal service network.
- 1.12 Royal Mail published its annual report for this same period at the end of June 2012. We are publishing our monitoring statement now for two reasons. First, Royal Mail's regulatory reporting is carried out after the completion of its management and statutory reporting because requiring simultaneous publication of statutory and regulatory would be a disproportionate burden on Royal Mail. Instead Royal Mail submits its annual regulatory reporting 120 days after financial year end. Second, this is the first year for which we have published a monitoring report and, therefore, we have had to consider the information received from Royal Mail and design the current publication. In subsequent years we expect to publish our annual monitoring updates in September or October.

² <http://www.legislation.gov.uk/ukxi/2012/936/made>

³ <http://www.royalmailgroup.com/regulation/how-were-regulated/universal-service-obligation>

⁴ Retail bulk mail is a service provided by Royal Mail, serving final customers that is subject to volume or presentation discounts. It represents bulk mail collected and delivered by Royal Mail itself, as opposed to bulk mail delivered by Royal Mail under the access framework. Further information about access is set out in Section 5.

Section 2

Royal Mail's financial performance

- 2.1 This section summarises Royal Mail's financial results and position in the five financial years up to 2011-12. This period pre-dates the current regulatory framework and consequently represents a baseline against which we will be comparing future performance.
- 2.2 Under the new regulatory framework, we will receive new data which provides further accounting separation within the Reported Business, quarterly cash headroom reports for the Relevant Group, and an Accounting Methodology Manual which will increase the transparency of Royal Mail's regulatory financial reporting.⁵ Royal Mail's existing published Costing Manual has also been expanded to cover its zonal costing methodology.⁶ We expect to be able to provide more detail in this respect in the next annual update in 2013, the first that will look at performance following the introduction of the new regulatory regime.
- 2.3 Our decision to allow Royal Mail more commercial freedom through removing traditional price controls was informed by our primary duty to secure the provision of the universal service in the context of a significant reduction in revenue over the period of the last price control (2006-2011). In discharging this duty, we are required to have regard to the need for the provision of the universal postal service to be financially sustainable.

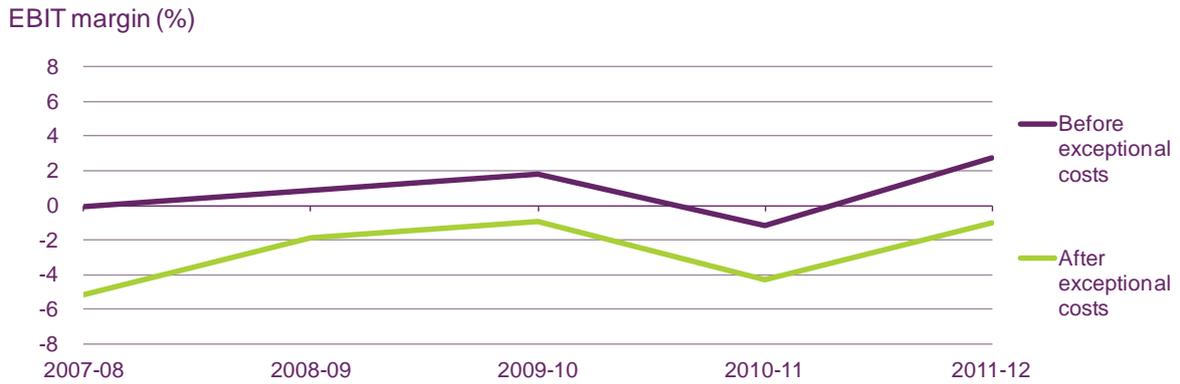
Profit margins

- 2.4 In the March 2012 statement, we set out our view that financial sustainability of the universal service should take into account the need for the universal service provider to be able to earn a reasonable commercial rate of return in connection with the provision of the universal service. We confirmed that an indicative EBIT margin range of 5% to 10% would be appropriate and consistent with this need.
- 2.5 Figure 2.1 sets out the EBIT margin for the Reported Business both before and after exceptional costs for the five years up to and including the period. In the March 2012 statement, we expressed our intention for the referenced EBIT margin to be a pre-exceptional measure of profitability, and that we would not expect restructuring or redundancy costs, likely to recur year on year, to be included in exceptional items. We understand that Royal Mail has included redundancy costs within exceptional items, and we therefore set out both margins, pre-and post-exceptional items, below.

⁵ In the Accounting Methodology Manual, Royal Mail sets out the regulatory accounting methodology it uses to comply with the Regulatory Accounting Guidelines.

⁶ The Costing Manual contains Royal Mail's detailed description of its costing methodology, and identifies all sources of data, and empirical data used for the assumptions that underlie its costing model.

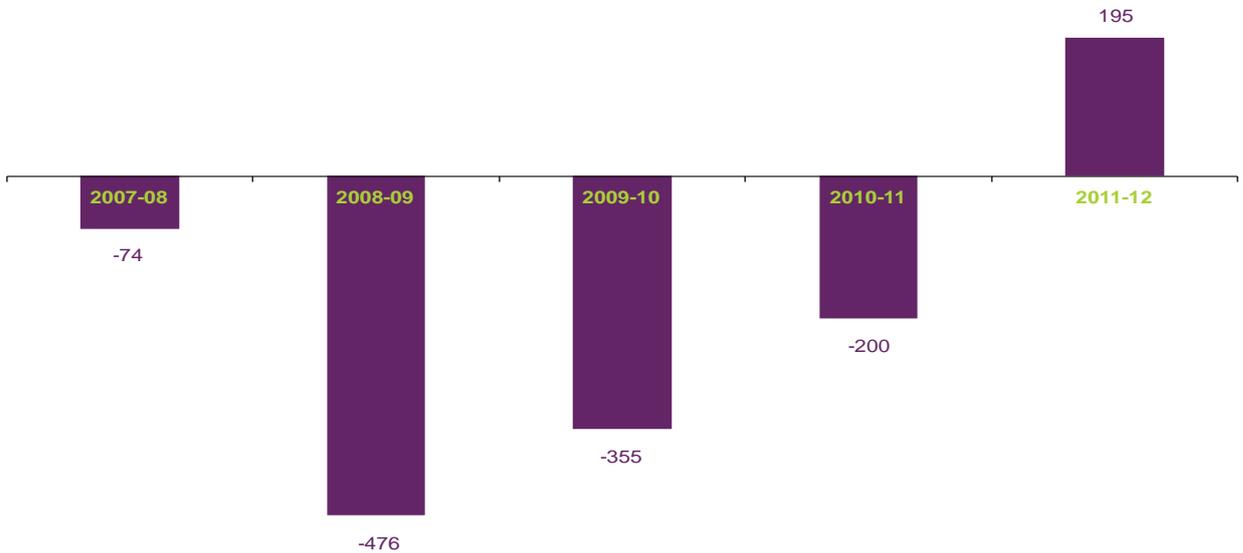
Figure 2.1 – Reported Business operating profit margins before and after exceptional costs



Source: Royal Mail (2010-11 and 2011-12 figures have been constructed for regulatory purposes and are unaudited.)

- 2.6 In the March 2012 statement, we also set out that the financial sustainability of the universal service was linked to the financial position of Royal Mail as the universal service provider.
- 2.7 In light of this, Figure 2.2 sets out the free cash flow of the wider Relevant Group (as explained at Figure 1.1 above). The cash flow of the Relevant Group improved considerably across the period, turning positive for the first time in a number of years. Key reasons for this improvement are an increase in revenue, and the removal of the pension deficit payment (following the transfer of that liability to the Government after a payment of £272m into the pension scheme in 2010-11). Royal Mail also made a number of asset disposals in 2011-12, accounting for £240m cash.

Figure 2.2 – Relevant Group free cash flow*



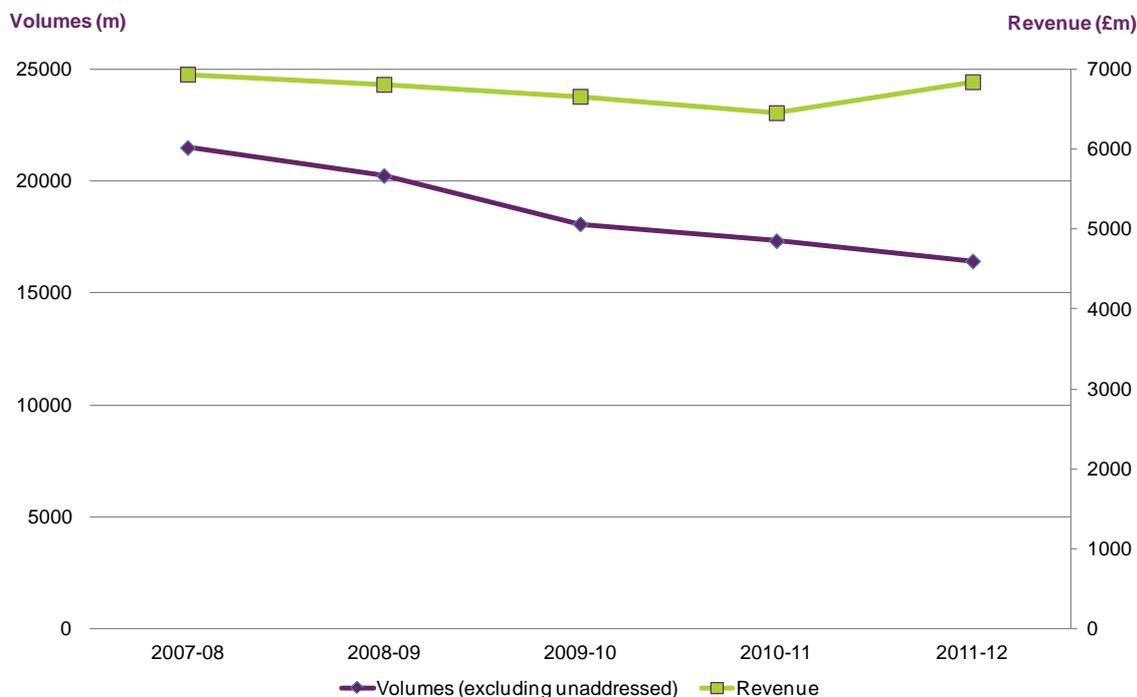
Source: Royal Mail 2011-12 Statutory Accounts
 *Free cash flow: net cash flow before financing activities (except finance costs paid), less the net cash purchase/sale of financial asset investments

Volumes, revenue and costs

- 2.8 The increase in revenue which contributed to the positive cash flow over the period can be seen in Figure 2.3, which shows the revenue and volumes of the Reported Business over the five years up to the end of the period.

2.9 The revenue of the Reported Business was declining steadily until recently, largely as a result of the declining volumes set out below. The upturn in revenue during the period is mainly attributable to price rises in business mail and access products, and to the changing product mix – specifically, the increasing number of higher revenue parcels being handled by Royal Mail.

Figure 2.3 – Reported Business total volumes and revenue



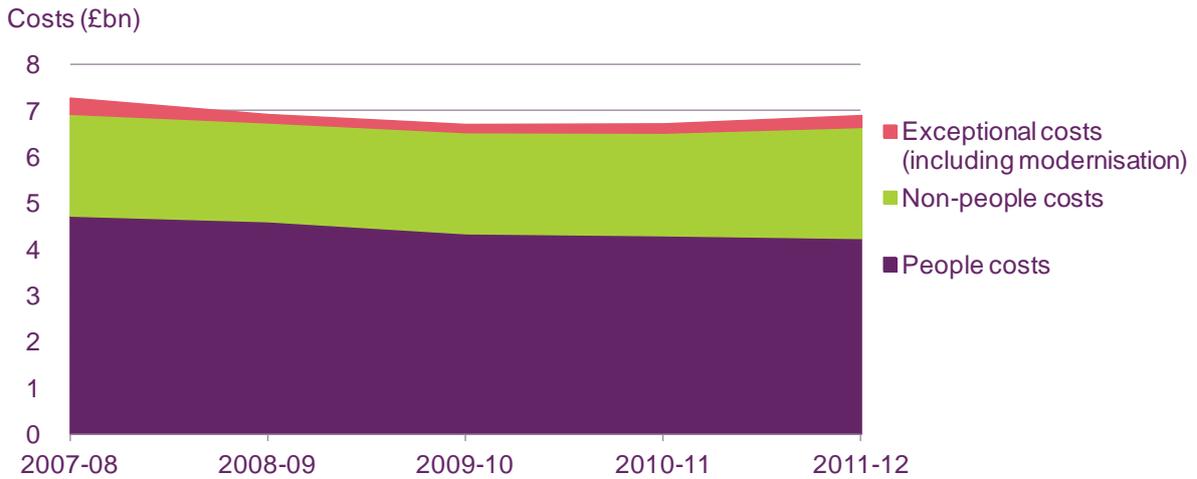
Source: Royal Mail Regulatory Accounts (2010-11 and 2011-12 revenue figures have been constructed for regulatory purposes and are unaudited.)

2.10 In March 2012 the European Commission approved the UK’s plans to provide pension relief (by removing the historic pension deficit) and restructuring aid to Royal Mail Group.⁷ As Royal Mail’s owner, the Government has therefore moved Royal Mail’s historic pension deficit assets and liabilities to the Treasury, in an effort to ensure the long-term viability of the business. As a result, Royal Mail is expected to see an improvement in cash flow which includes a benefit of approximately £300m per annum from the removal of the pension deficit payments.

2.11 In addition to increasing revenue, costs for the Reported Business have remained relatively flat in the five years to the end of the period. A rise in non-people and exceptional costs (£0.2bn and £0.1bn respectively) was somewhat counteracted by a reduction in people costs (£0.1bn) over the period.

⁷ Commission Decision of 21 March 2012 on the measure SA.31479 (2011/C) (ex 2011/N) which the United Kingdom plans to implement for Royal Mail Group, Decision available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:279:0040:0068:EN:PDF>

Figure 2.4 – Reported Business costs



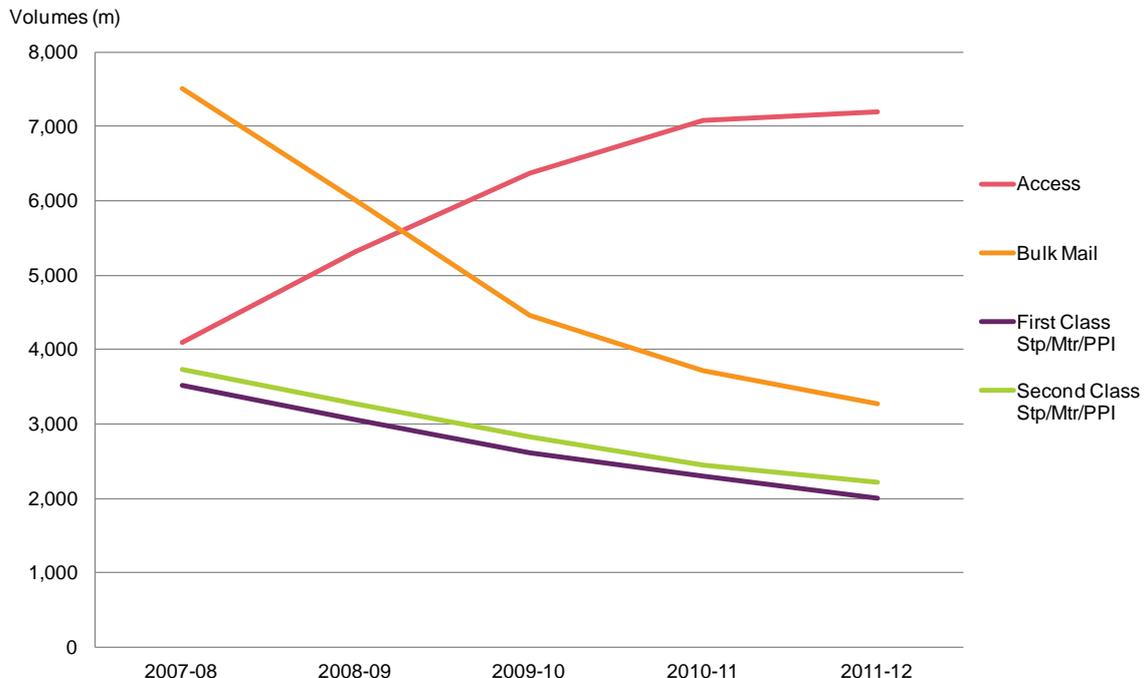
Source: Royal Mail (2010-11 and 2011-12 figures have been constructed for regulatory purposes and are unaudited.)

Changes in product mix, and the impact on revenue

2.12 The impact of the price rises in business mail and access that have contributed to increased revenues can be seen in Figures 2.5 and 2.6.

2.13 Figure 2.5 shows how Royal Mail’s retail bulk mail volumes have declined rapidly, due to volumes lost to competitors such as TNT and UK Mail. This has led to a corresponding increase in access volumes – the loss of retail bulk mail for Royal Mail is therefore only a loss in the upstream market, as access providers still rely on the downstream part of Royal Mail’s network for final delivery. Both First and Second Class single-piece mail volumes have declined steadily since 2007-08.

Figure 2.5 – Volumes split by product group - First and Second Class, access, bulk

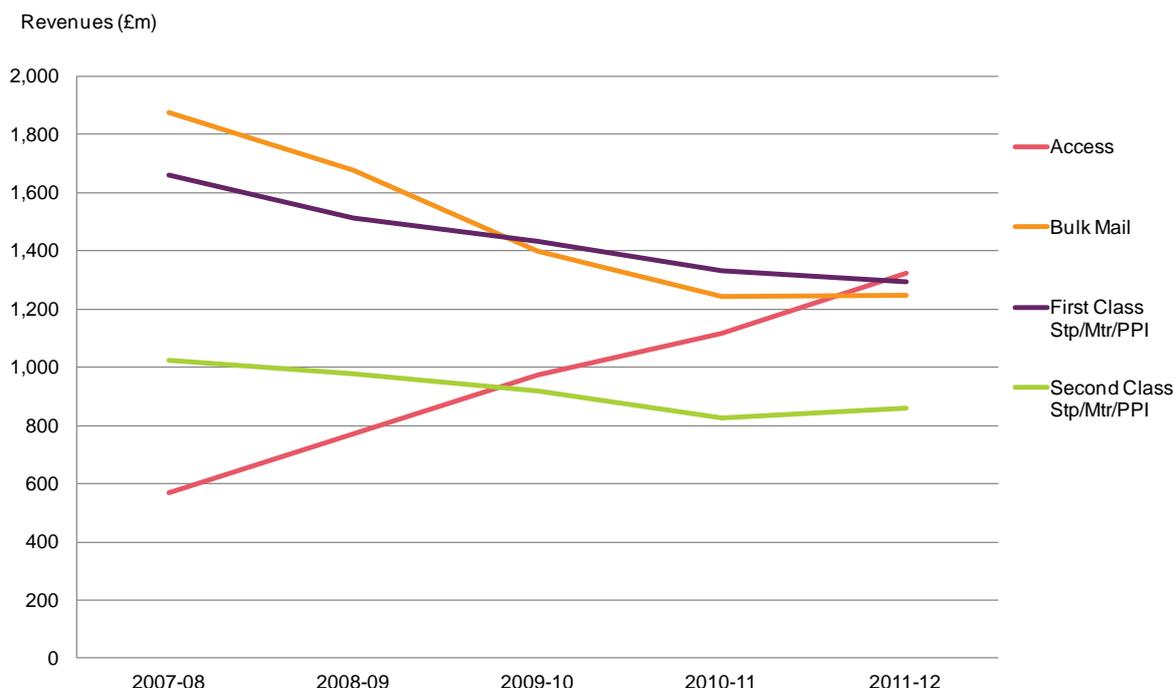


*Products included in Bulk Mail: Mailsort, Walksort, Presstream, Mail Media, Packetpost & Cleanmail

Source: Royal Mail - Revenue-derived volumes

- 2.14 Figure 2.6 shows the corresponding revenues, where the impact of price rises in access is clear – access volumes have almost doubled, whilst revenue from the same products has almost trebled.
- 2.15 Despite the steady decline in volumes, revenue for First and Second Class single-piece mail has not declined to the same extent. Again, this is due to Royal Mail increasing prices, set out in further detail in Section 4.

Figure 2.6 – Revenue split by product group - First and Second Class, access, bulk



*Products included in Bulk Mail: Mailsort, Walksort, Presstream, Mail Media, Packetpost & Cleanmail

Source: Royal Mail - Revenue-derived volumes

- 2.16 As well as increased revenue from these price rises, revenues are being boosted by the changing product mix. Figure 2.7 sets out the Reported Business volumes, broken down by format, namely, Letters, Parcels and Other formats.⁸ Since 2009-10, Letter volumes have fallen. Parcel volumes have increased slightly (from 731m in 2009-10 to 784m in 2011-12), and Other item volumes have fallen slightly.

⁸ 'Parcels' includes all Packet format items, Packetpost & Packetsort Large Letters and some ancillary services; 'Other' includes International, Door to Door, Central Functions income, Data and innovations income; 'Letters' includes other Letter and Large Letter items and most of the ancillary services.

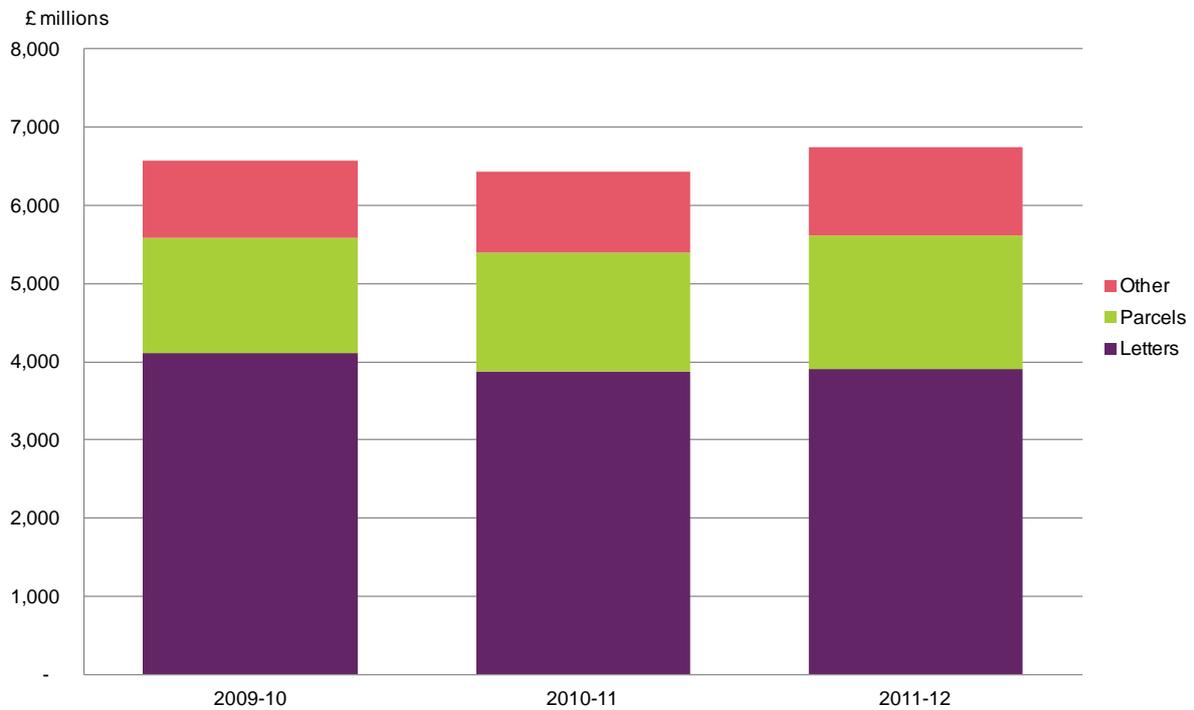
Figure 2.7 – Volumes split by format – Letter, Parcel and Other items



Source: unpublished submission provided to Ofcom, October 2012. Volumes shown are UKPIL excluding Parcelforce

2.17 The proportionately higher revenue derived from Parcel products is clearly shown in Figure 2.8, which sets out the corresponding revenue. The increase in revenue from Parcel products outweighs the reduction in revenue from Letter products.

Figure 2.8 – Revenue split by format – Letter, Parcel and Other items

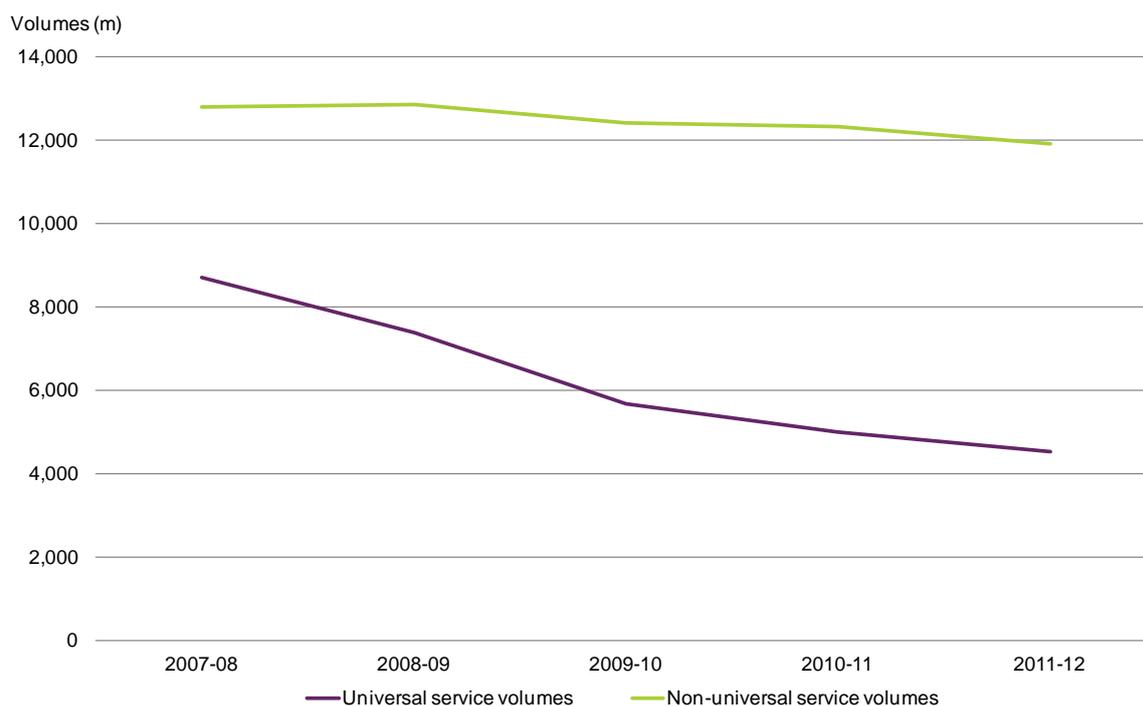


Source: unpublished submission provided to Ofcom, October 2012. Revenue shown is UKPIL excluding Parcelforce

The universal service

- 2.18 As set out in Section 1, the Relevant Group includes all universal service products, as well as other products which use the universal service network (for example, retail bulk mail and access products).
- 2.19 Figure 2.9 shows the Reported Business volumes, broken down into universal service and non-universal service products. The volume of universal service products has declined steadily;⁹ the volume of non-universal service products less so.

Figure 2.9 – Volumes split by universal service and non-universal service products

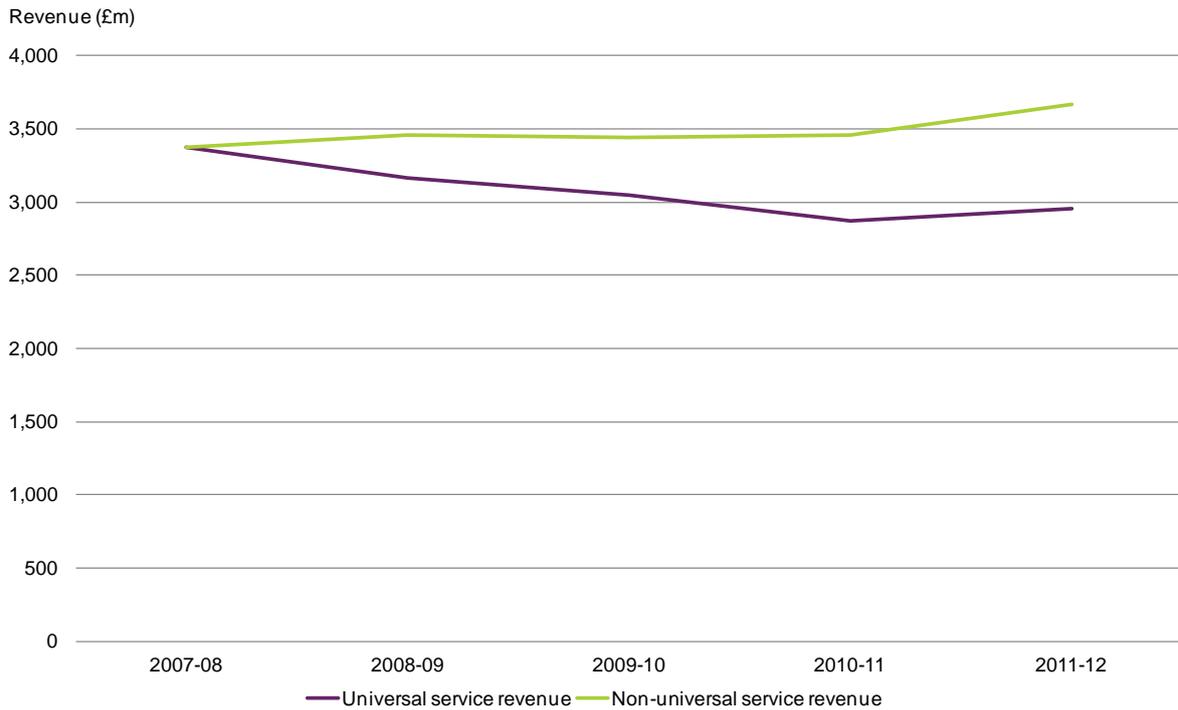


Source: Royal Mail Regulatory Accounts, addressed volumes

- 2.20 Figure 2.10 sets out the corresponding revenue for the Reported Business.

⁹ Some of the decline in universal service products may be due to some products being removed from the scope of the universal service during the period set out in Figure 2.9.

Figure 2.10 – Revenue split by universal service and non-universal service products



Source: Royal Mail Regulatory Accounts

2.21 The revenue from universal service products within the Reported Business has not declined as quickly as volumes, largely because of price rises. This is particularly true of 2011-12, in which universal service revenue rose slightly, whilst volumes declined.

Section 3

Efficiency

- 3.1 In our March 2012 statement, we emphasised the importance of Royal Mail achieving significant efficiency gains. We said that we would focus on Royal Mail's progress in terms of reducing costs, whilst monitoring quality of service to ensure that service levels were not degraded at the same time.

Royal Mail's modernisation plans

- 3.2 In order to improve efficiency, Royal Mail has implemented a large-scale modernisation plan. This modernisation plan affects all parts of the postal process, and has resulted in the closure and consolidation of a number of Mail Centres, and changes to the operation of local Delivery Offices. Much of the postal process has been automated: Mail Centres now make greater use of sorting machines, and walk sequencing machines have been installed in both Mail Centres and certain Delivery Offices. This has resulted in a reduction in the manual sorting of mail and the time taken to sequence the mail into delivery order.
- 3.3 Royal Mail has shared with us its business plan which sets out its plans to reduce costs and improve efficiency. Given much of this plan is commercially sensitive, we have not disclosed any of the detail in this report, though it will inform our ongoing monitoring of Royal Mail's efficiency moving forward.

Efficiency measures

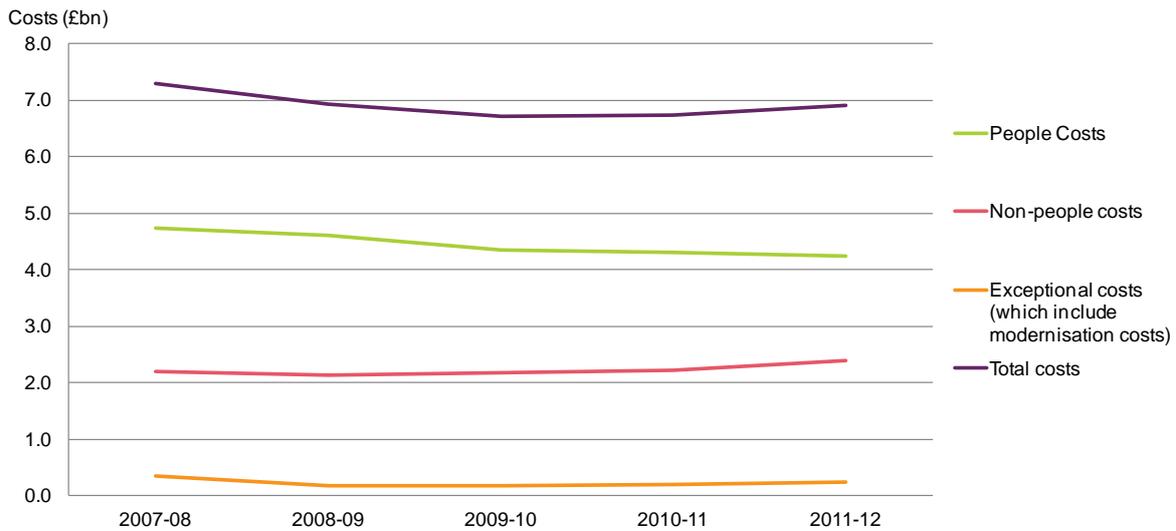
- 3.4 This section looks at Royal Mail's performance against a number of potential indicators of efficiency. In the March 2012 statement, we set out that operating performance is an important element in the monitoring programme, and that we would focus on cost reduction when considering the operating performance of Royal Mail. We set out that there are a range of factors we may need to consider to help understand and interpret operating performance, such as volumes and mix, and modernisation investment.
- 3.5 In our recent draft guidance on end-to-end competition in the postal sector, we set out our intention to undertake work to determine how to assess what constitutes a reasonable rate of efficiency improvement by Royal Mail.¹⁰ We are considering the specific scope for that work at present; it will seek to develop a framework for assessing the usefulness of different benchmarks that might be used to assess Royal Mail's efficiency performance over time. We anticipate that stakeholders will have the opportunity to contribute to this work at the appropriate point.
- 3.6 In light of this upcoming work, we do not set out here a detailed analysis of Royal Mails' efficiency. Instead, we set out below a summary of key performance indicators, which we may consider useful in considering Royal Mail's efficiency overall.

¹⁰ The draft guidance can be found here: <http://stakeholders.ofcom.org.uk/binaries/consultations/e2e-guidance/summary/e2e-guidance.pdf>

Costs

3.7 Total costs for the Reported Business from 2007-08 to the period reported are set out at Figure 3.1. These costs are broken down into people costs, non-people costs and exceptional costs, the latter of which include modernisation costs (for example, the cost of upgrading sorting machines). People costs have reduced since 2007-08, indicating the impact of Royal Mail’s modernisation programme. At the same time, non-people costs have increased. Royal Mail understand this to be the impact of an increased proportion of parcels, which cost more to deliver. Exceptional costs remained relatively flat.

Figure 3.1 – Reported Business costs



Source: Royal Mail (2010-11 and 2011-12 figures have been constructed for regulatory purposes and are unaudited.)

- 3.8 The increase in parcels has also had an impact on the revenue per item processed by Royal Mail. Figure 3.2 shows the average revenue and cost per item; in 2011-12, revenue per item overtook cost per item by a small margin, most likely due to parcels attracting proportionately higher revenues than other products.
- 3.9 The data in Figure 3.2 relates to items that fall within a group of products called ‘Total Mails’. Total Mails sits within, and comprises the majority part of, the Reported Business, and includes all posted items, but does not include non-mail products such as Address Management Centre, Customer Management, Royal Mail Specialist Services, Stamps & Collectables. We have excluded these items in order to better represent the revenue and cost per item of posted mail.

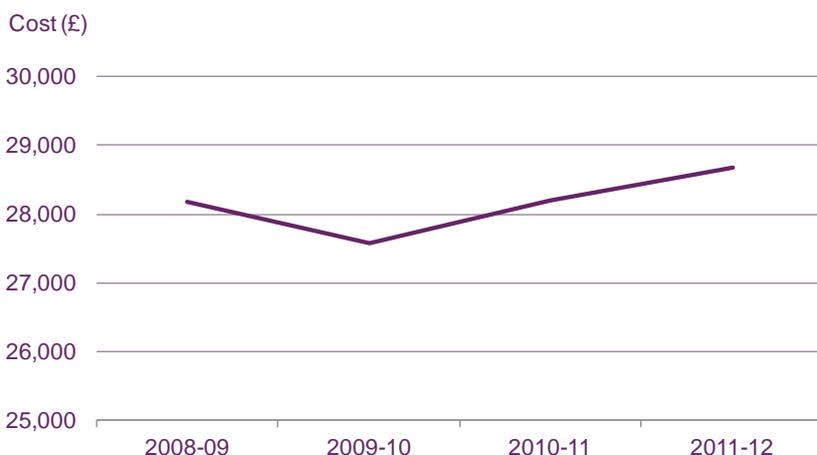
Figure 3.2 – Total Mails revenue and cost per item



Source: Royal Mail (analysed by Ofcom)

3.10 Whilst people costs have gone down, the number of full-time equivalent employees (FTEs)¹¹ within the Reported Business has also gone down – from 152,784 in 2010-11 to 148,183 in 2011-12. Figure 3.3 shows the change in people cost per FTE since 2008-09. In 2011-12, the average people cost per FTE has risen, but by less than inflation.¹²

Figure 3.3 – Reported Business people cost per FTE



Source: Royal Mail (analysed by Ofcom)

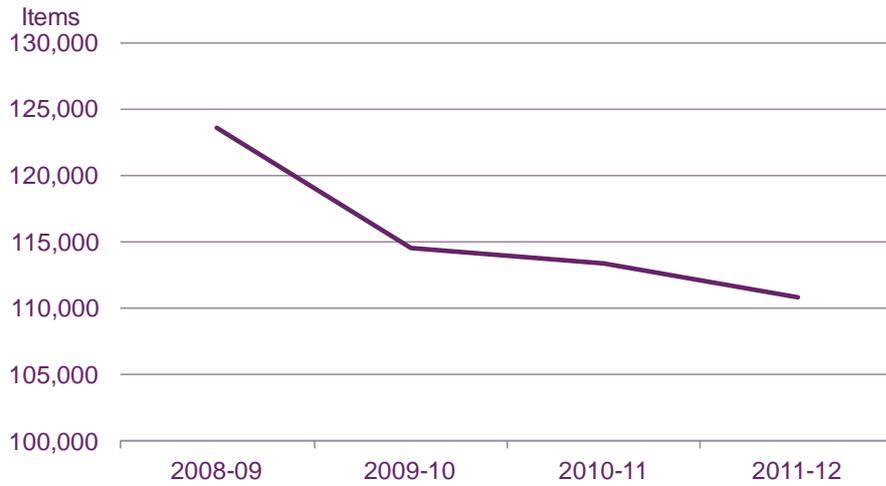
Operational metrics

3.11 Royal Mail report that the increase in the proportion of parcels being delivered has an impact on their operational performance in conjunction with their costs – in particular, that postmen and women are to deliver fewer items when a larger proportion of those items are parcels, compared to previous reporting periods. Figure 3.4 shows the average number of items delivered per FTE each year since 2008-09.

¹¹ FTE data for Reported Business staff is calculated on a 40-hour week for frontline staff; management staff figures provided by Royal Mail are calculated on a headcount basis.

¹² As a measurement of inflation, we use the Consumer Price Index, which was 3.5% to the end of March 2012.

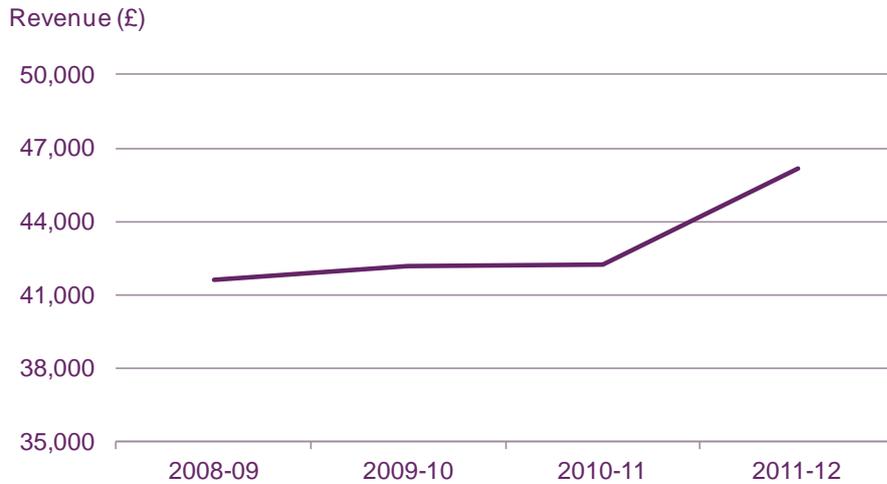
Figure 3.4 – Reported Business items per FTE



Source: Royal Mail (analysed by Ofcom)

3.12 With regard to revenue, Figure 3.5 shows the average revenue per FTE for the Reported Business each year since 2008-09. Royal Mail saw an increase in revenue per FTE during the period, due to increased revenues and fewer FTEs.

Figure 3.5 – Reported Business revenue per FTE



Source: Royal Mail (analysed by Ofcom)

Section 4

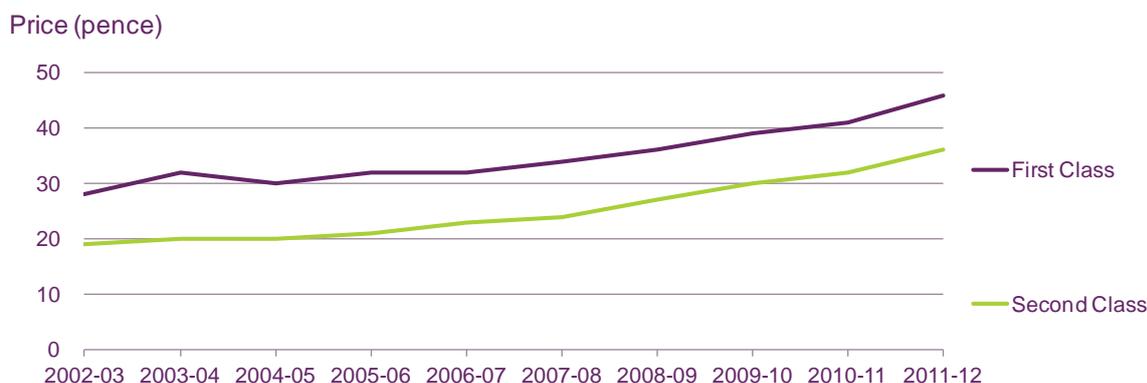
Customers and consumers

4.1 In this section we have considered the impact of Royal Mail's pricing and operational decisions on its customers and consumers. Prices of universal service products can significantly impact customers – particularly those that rely intensively on postal services. In the March 2012 statement, we stated that we would also monitor price rises, as well as the quality of service achieved by Royal Mail in the provision of universal services.

Prices

4.2 Since 2002, Royal Mail has implemented a series of price increases to First and Second Class stamps.

Figure 4.1 – Standard Letter First and Second Class stamp prices



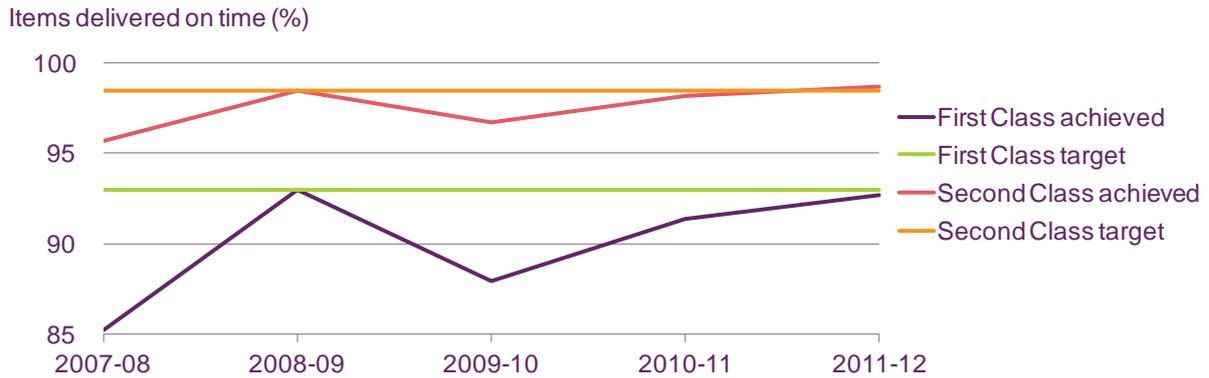
Source: Royal Mail

4.3 In April 2012, shortly after the end of the financial year to which this report relates, Royal Mail increased the price of First and Second Class stamps for a standard letter to 60p and 50p respectively.

Quality of service targets

4.4 Royal Mail is subject to a number of service level performance targets. It is targeted to deliver 93% of all First Class retail letters (single piece, metered and prepaid) on the day after collection, and 98.5% of all Second Class letters within three days of collection. In 2011-12, Royal Mail narrowly missed its First Class target, reaching 92.7%; it exceeded its Second Class target with 98.7%.

Figure 4.2 – Retail First and Second Class targets



Source: Royal Mail Quality of Service data, 2007 - 2012

4.5 Postcode Areas (PCAs) are the geographic areas into which the UK is divided by Royal Mail for operational purposes.¹³ There are 121 in total. Within 118 of these PCAs, Royal Mail is expected to deliver 91.5% of all First Class stamped and metered mail the day after collection.¹⁴ The PCA target measures in how many of the 118 PCAs Royal Mail met this target. This is important, because it monitors the extent to which Royal Mail provides a good level of service across the UK – not just in those more densely populated areas, where delivery is more cost-effective, but also in less densely populated areas and those where addresses may be more remote or harder to reach.

Figure 4.3 – PCA target



Source: Royal Mail Quality of Service data, 2007 - 2012

4.6 In 2011-12, Royal Mail achieved this 91.5% target in 97 of its 118 PCAs. The postcode areas in which this target was missed broadly correspond to areas affected by Mail Centre closures and other modernisation works undertaken by Royal Mail during this reporting period.

4.7 Also included within the universal service are Standard Parcels, European International Delivery and Special Delivery (Next Day) Services. At least 90% of Standard Parcels should be delivered three days from collection; 85% of European

¹³ The postcode area is the largest geographical unit used by Royal Mail for mail processing purposes, and forms the initial characters of the alphanumeric UK postcode; for example, Cardiff postcodes begin 'CF', Glasgow postcodes 'G', and Leicester postcodes 'LE'.

¹⁴ Three of the PCAs are excluded from the PCA target. These are HS (Hebrides), KW (Kirkwall, Orkney) and ZE (Lerwick, Shetlands).

International items should be delivered three days from collection; 99% of Special Delivery (Next Day) items should be delivered on the next delivery day.

Figure 4.4 – additional universal service products¹⁵



Source: Royal Mail Quality of Service data, 2007 – 2012

4.8 In 2011-12, Royal Mail exceeded the targets both for Standard Parcels and for European International items, but narrowly missed the target for Special Delivery items.

4.9 In addition to the above product-related targets, Royal Mail has a number of service-oriented targets: it should serve 99.9% of its collection points each day, from Monday to Saturday; it should complete 99.9% of its delivery routes each day, from Monday to Saturday; and it should deliver 99.5% of items correctly each day.

Figure 4.5 – collection and delivery targets



Source: Royal Mail Quality of Service data, 2007 - 2012

4.10 In 2011-12, Royal Mail met the target for collection points, narrowly missed the target for delivery routes, and met the target for correctly delivered items.

4.11 We note that Royal Mail has missed some of its Quality of Service targets, as set out above. Royal Mail has explained to us that this is a result of the transformation process needed to ensure the ongoing viability of the universal service. We will continue to monitor closely the impact of transformation on quality of service to ensure that Royal Mail continues to make all reasonable efforts to maintain acceptable quality of service.

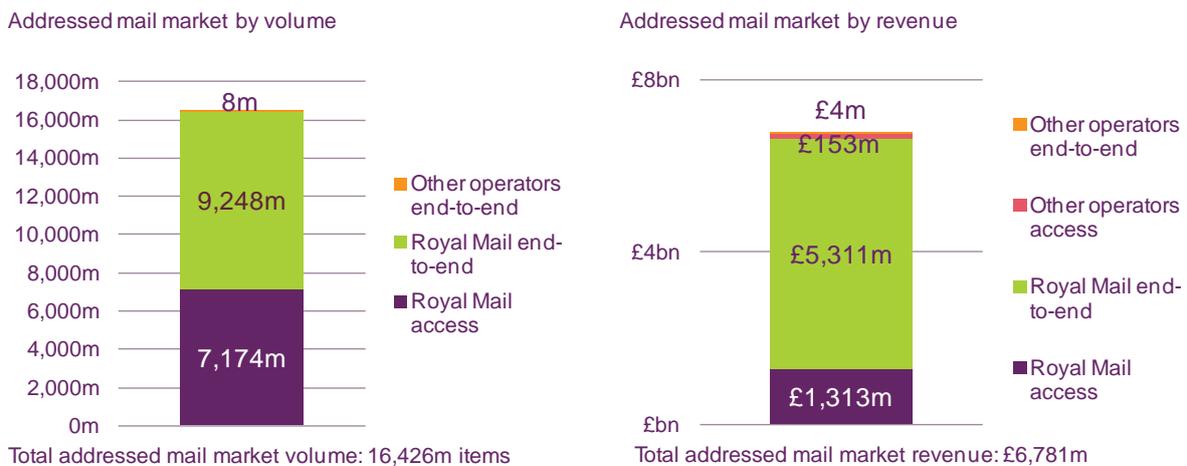
¹⁵ These results are calculated by the International Post Corporation, based on the UNEX measurement data. They cover the flows between UK and the other 26 EU Member states. These results do not include the Christmas period, defined as one month from early December to early January, and are therefore not comparable to the UNEX Results published annually by the International Post Corporation on behalf of its European Members.

Section 5

Competition

- 5.1 As set out in the March 2012 statement, competition in the postal market has a number of potential benefits for customers. This includes providing incentives for Royal Mail to become more efficient and to innovate. However, we also recognised that competition also has the potential to raise a threat to the sustainability of the universal service by removing proportionately greater amounts of revenue from Royal Mail.
- 5.2 Within the postal sector, there are two main forms of competition: end-to-end and access.
- 5.3 Access competition is where the operator collects mail from the customer, sorts it and then transports it to Royal Mail's Inward Mail Centres, where it is handed over to Royal Mail for delivery. Royal Mail is subject to a regulatory condition to continue to offer access to its Inward Mail Centres. This enables other operators to offer postal services to larger business customers without setting up a delivery network. Access has been the predominant form of competition in the UK since the first access contract was signed in 2004.
- 5.4 End-to-end competition is where an operator other than Royal Mail undertakes the entire process of collecting, sorting and delivering mail to the intended recipients.
- 5.5 Together, the total market comprises three parts: mail collected and delivered by Royal Mail ('Royal Mail end-to-end'); mail collected by other operators and delivered by Royal Mail ('Royal Mail access'); and mail collected and delivered by other operators ('Other operators end-to-end'). 'Royal Mail access revenue' is the revenue paid to Royal Mail by other operators for the delivery of access mail; 'other operators access revenue' is that paid to other operators by customers under the access process, minus the portion of that revenue paid to Royal Mail for delivery. Figure 5.1 shows the total mail market volumes and revenue by type of operator in these terms.

Figure 5.1– Total mail market volumes and revenue by type of operator

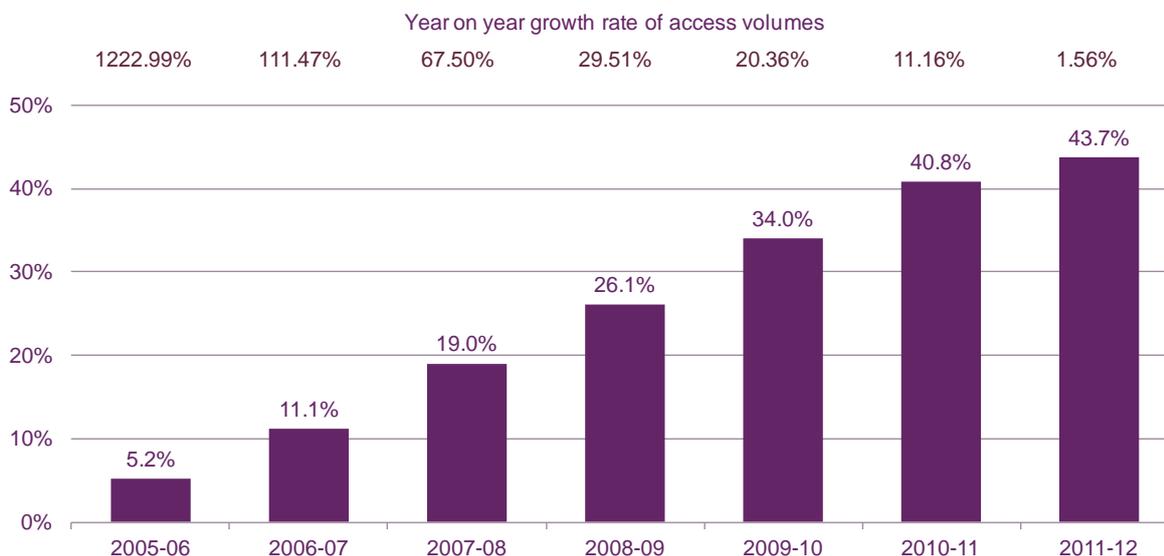


Source: Royal Mail Group Ltd. Regulatory Financial Statements 2011-12; Operators returns to Ofcom

Access competition

- 5.6 Currently, access represents a significant portion of the market by volume (around 44% of all delivered mail), though the proportion of revenue retained by other operators from access is much smaller (£153m out of a total market revenue of £6,781m).
- 5.7 Though access has grown rapidly since 2005, there is evidence that its growth is slowing. Access grew from just under 41% of the market by volume in 2010-11, to account for just under 44% of the market by volume in 2011-12. This suggests that the customers who might make costs savings by taking services from other operators via the access process have now largely done so.
- 5.8 Figure 5.2 shows the proportion of access total mail volumes accounted for by access. As shown in the graph, the volume of access mail had increased significantly since its introduction in 2005.

Figure 5.2 – Proportion of access products compared to total mail volumes



Source: Royal Mail Wholesale, Royal Mail Regulatory Financial Statements

End-to-end competition

- 5.9 To date, there has been very little end-to-end competition in the UK letters market (unlike some other European countries where end-to-end competition is the main form of competition). In 2011-12, other operators delivered just 8 million letters¹⁶ out of a total addressed volume of more than 16 billion. In practice this has largely comprised of cycle couriers and local delivery services. Figure 5.3 shows the volume of other operators' end-to-end products.

¹⁶ This figure includes all letter products, and excludes parcels.

Figure 5.3 – Other operators' end-to-end delivered volumes

Source: Operators' returns, based on former licensed area delivered volumes

- 5.10 There is significantly more end-to-end competition in the delivery of packets and parcels and for closed user group services (i.e. DX mail used by solicitors and other professional customers). We are looking to collect more information on the development in the growing packet and parcel markets and are intending on reporting on this in future annual updates.

Recent competitive developments

- 5.11 TNT Post began trialling end-to-end delivery operations in West London in April 2012. It expects that this pilot will enable it to carry out further testing, refine its delivery operations and trial new systems. TNT Post is offering a value-added service that includes scanning on delivery and provision of management information to customers. TNT Post is planning to roll out a broader end-to-end service to selected parts of the country, once TNT Post has analysed the pilot, the impact of VAT on access products and other market conditions.
- 5.12 On an equivalent basis end-to-end competition has a significantly higher impact on the universal service as Royal Mail retains 85-90% of the total revenue for access mail. It is therefore important that we continue to monitor the development of end-to-end competition in the postal market.¹⁷ To provide greater clarity to the market, we recently published draft guidance on Ofcom's approach to end-to-end competition in the postal sector.¹⁸

¹⁷ As set out in our July 2012 update on Ofcom's position on end-to-end competition in the postal sector. See <http://stakeholders.ofcom.org.uk/binaries/post/update.pdf>.

¹⁸ <http://stakeholders.ofcom.org.uk/binaries/consultations/e2e-guidance/summary/e2e-guidance.pdf>

Annex 1

Information collected as part of the monitoring programme

Information for financial monitoring	Frequency
Relevant Group consolidated income statement, balance sheet, and cash flow statement	Annually
Royal Mail Strategic Business Plan and Annual Budget	Annually
Reported Business income statement, product profitability statements, capital employed statement, and cash flow statement (including accounting separation)	Annually
RM data on compliance with the safeguard cap	Annually
Relevant Group consolidated cash flow projections	Quarterly
Reported Business income statement, and product profitability statements (including accounting separation)	Quarterly
RM Costing Manual (including zonal costing) and Accounting Methodology Manual	Quarterly
Other operators' volume and revenue data split by product	Quarterly
Reported Business Revenues and Volumes report	Monthly
Relevant Group Monthly Management and KPI Performance Pack	Monthly

Information for monitoring impact on customers and consumers	Frequency
RM quality of service reporting	Annually/quarterly*
RM Mail integrity reporting	Annually/quarterly
RM changes to latest delivery and collection times	Three months before change
RM request to change terms and conditions for USO products	One month before proposed change
RM request to change prices for USO products	One month before proposed change
RM notification of changes to terms and conditions for non-USO products	One month before change
RM notification of changes to prices for non-USO products	One month before change
RM change to compensation policies	One month before change