

**Lakeland Ltd. Response to Ofcom's Consultation documents "Securing the Universal Postal Service" published on 20<sup>th</sup> October 2011 & "Review of Regulatory Conditions – Postal Regulation" published on 13<sup>th</sup> December 2011.**

Dear Sir/Madam,

I write in response to the above consultations. I write on my behalf of my employer, Lakeland Limited, a retailer of kitchenware and related home-wares selling to the public via catalogues, the internet and a nationwide chain of shops.

We note that Ofcom is seeking to protect the provision of the "Universal Postal Service" while also ensuring the viability of the organisation delivering it, Royal Mail. Our comments are independent of any potential changes to the ownership structure of Royal Mail, applying whether or not the company remains in public ownership, since the long term financial viability of Royal Mail will be necessary in either case in the absence of any other scale "end to end" service provider.

The consultation document contains strong signals that the cost to end users levied by Royal Mail for the provision of postal services will substantially increase, while also discussing the importance of improving the efficiency of provision. For example in the Summary to the consultation it states, "...There are, however, also significant risks with giving Royal Mail commercial freedom. Most obvious is the risk that Royal Mail uses this as a means of shying away from the efficiency challenge in favour of simply increasing prices. [1.36] If the new regulatory framework did not lead to increased efficiency, it would have failed one of its fundamental goals. A reliance on price rises alone would reduce demand further, exacerbating the risk of the sector falling into an inescapable spiral of decline."

It is our view that the changes being proposed by Ofcom risks accelerating the "downward spiral" in terms of postal volumes and will therefore fail to deliver the regulator's stated objectives. Lakeland makes extensive use of catalogues as a form of advertising for our products, to support our mail order business (including our website) and our physical stores. As such we are, apparently, one of Royal Mail's "Top 50" customers. Our business will therefore be materially impacted by the changes being proposed.

We ask that Ofcom gives due consideration to the following:

1. It is proposed that a benchmark price for postal services be established by reference to the price of a 2<sup>nd</sup> class stamp. This is currently 36p for a letter under 100g. The consultation suggests a band for such prices of 45p to 55p, representing a 25% to 53% increase. Given the relatively low weekly household expenditure on stamps such a rise would, we expect, be tolerated. However if the pricing of "bulk mail" services, such as "mailsort" were to continue to be by reference to the 2<sup>nd</sup> class "standard", such a rise would be intolerable, leading to a radical reduction in the level of usage of direct mail. The consultation document assigns insufficient weight to the risk that the price rises being indicated will further accelerate the year on year reductions in mail volumes. **It is essential that the pricing by Royal Mail of services for business users are independent of changes to the public tariff.**
2. The provision of the "Universal Service" is currently subsidised by profits on "bulk mail" services such as those used by large volume direct mailers such as Lakeland.. While competition from electronic media is acting to reduce mail volumes, the primary factor determining mail volume is the economics of the channel: prices are rising faster than response rates, reducing returns on investment. Mail volumes are very sensitive to this return on investment equation. Further price rises will render substantial volumes of mailing activity uneconomic, causing faster decline in use of

the mail service than has previously been the case. **It is important therefore that the pricing of “bulk mail” services is more cost reflective than is currently the case.**

3. The consultation accepts without question the current pricing structure operated by Royal Mail, in particular the definition of “letter” and “large letter”. Items that exceed the tolerances for “letter” format become “large letter” and consequentially there is a very large step between the prices of the two services. An item that complies with the specification for “letter” but exceeds the 100g weight limit by 1g incurs a huge increase in price. The marginal price of that 1g is therefore enormous even though the marginal cost to Royal Mail of that 1g is negligible, perhaps even zero. Our choice of formats for our catalogue mailings is polarised: we either restrict ourselves to the 100g limit or else might as well fill the pack up to 250g as after the 100g threshold there is no cost penalty until the 250g limit is reached. I believe that this 100g threshold is arbitrary and that Royal Mail has demonstrated an ability to efficiently sort heavier items (“large letter” items) on the same machinery as the “letter” items. The regulator should examine whether the 100g limit is indeed a key driver of Royal Mail costs, or whether an increase in this limit could be accommodated to mitigate the impact on businesses of the intended price increases, without transferring a cost burden to Royal Mail. For example altering the limit to 175g would, we believe, make viable a considerable amount of direct mail currently being eliminated as uneconomic. **We argue that any increase in the cost of “letter” format mail be mitigated by a change in the definition of what constitutes a “letter”. In order to address the issues faced by Royal Mail the regulator should seek adjustments to the regulatory regime that stimulate use of the service rather than regard sustained reductions in mail volumes as inevitable.**
4. It is proposed that the notice period Royal Mail are required to give with regards changes to tariffs and related services be reduced from three months to one. This proposal should be amended so that the three months notice remains in place for price increases, while price reductions or new services can be introduced more quickly. The reason for this is that the production cycle for a direct mail campaign is approximately three months, from conception to posting. It is important when a business chooses to make an investment in a mailing campaign that the cost of undertaking the posting is known at the point the decision is made. The service provider for the mailing must be selected at the time of creating artwork for the campaign in order that the correct “PPI” be assigned. It would be inappropriate to award the work to a service provider only for the price charged to alter in the period between the award and the posting. Very few comparable services can apply tariff increases with less than three months notice; Royal Mail should not be able to do so. The incentive to innovate, and the option to bring new services to the market quickly, should be retained but not at the expense of introducing considerable uncertainty into the market for the provision of postal services. **Were the proposed change to tariff notice periods be implemented it would disrupt business planning and reduce confidence in direct mail as an advertising medium.**
5. It is proposed that regulation of access prices by “Down Stream Access” providers be replaced by a “margin squeeze test”. We are not persuaded that this will advance the cause of effective competition nor that the proposed accounting separation will provide adequate safeguards. This question is of particular importance to businesses using direct mail as an absence of effective competition in the market for injecting post into ‘Inward Mail Centres’ will mean Royal Mail lacks incentive to improve the efficiency of its operation. Royal Mail remains a monopolist at the level of the “last mile delivery operation”. In theory it ought to be agnostic as to whether its own distribution operation or that of a down stream access provider provides this “last

mile operation” with work, and if there was a “level playing field” for access it ought not to matter. However the way in which Royal Mail is structured means that it does matter and Royal Mail enjoys privileged access to the “last mile”. The regulator must ensure that the access price by which Royal Mail and other operators accesses this “last mile” is identical. **It seems to us that this can only be achieved by separation of Royal Mail into independent business units, one delivering to customers, and one collecting, sorting and distributing mail, each focused on efficiency and customer service in their own operations. The absence of this proposal in the Consultation is disappointing.**

We trust that Ofcom is consulting in good faith and will thus take full account of our responses received, including our concerns, before coming to a final decision on these proposals. We would be happy to discuss these matters at greater length with Ofcom if this were felt to be helpful.

Sincerely,

Mr A. Preedy  
Director of Marketing  
Lakeland Ltd.