

Development of competition in the European postal sector

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Final study

The authors take full responsibility for the contents of this report. The opinions expressed do not necessarily reflect the view of the European Commission

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Table of contents

Preface	11
Executive summary	13
1 Introduction	33
1.1 Objective of the study	33
1.2 Policy context	33
1.3 Sources of information and activities undertaken	34
1.4 Research method and outline of the report	35
2 Description of the postal market	39
2.1 Introduction	39
2.2 Segmentation of the postal market	39
2.2.1 Market segmentation along postal products	39
2.2.2 Market segmentation using other criteria	40
2.3 The postal value chain	41
2.3.1 Traditional postal supply chain	41
2.3.2 Modern postal value chain	42
2.3.3 The supply chain of express and courier services	43
2.4 Regulation of the postal sector in the Member States	44
2.4.1 Postal directives 97/67/EC and 2002/39/EC	44
2.4.2 Provision of universal services	45
2.4.3 Liberalisation of postal markets in the Member States	45
2.5 Mail volumes in the Member States	48
2.6 Summary and conclusion	53
3 Potential for competition in the postal sector	55
3.1 Introduction	55
3.2 The five forces model of Porter	55
3.2.1 Risk of new competitors entering the industry	56
3.2.2 Threat of potential substitutes	57
3.2.3 Bargaining power of buyers	58
3.2.4 Bargaining power of suppliers	59
3.2.5 Degree of rivalry between existing competitors	59
3.2.6 Government regulations	59
3.3 Preliminary assessment of contestability of market segments	61
3.3.1 Introduction: barriers to entry and contestability	61
3.3.2 Which market segments are contestable?	61
3.3.3 Natural barriers to entry	63

3.4	Network access: justification and economic rationale	68
3.5	Summary and conclusion	72
4	Development of competition in the EU Member States	75
4.1	Introduction	75
4.2	Development of competition in the Member States	75
4.2.1	Overview of the development of competition in the Member States	75
4.2.2	Some country examples	81
4.3	Factors that influence the development of effective competition	87
4.3.1	Legal barriers to entry	87
4.3.2	Strategic barriers to entry	90
4.3.3	Level playing field	92
4.4	Effects of competition on the market	94
4.5	Summary and conclusion	94
4.5.1	Development of competition in the Member States	94
4.5.2	Key factors influencing the development of competition	96
4.5.3	Disputes and role of a postal sector regulator	96
5	Strategies of competitor and national postal operators	99
5.1	Introduction	99
5.2	Considerations of customers of postal operators	99
5.3	Strategies of competitor postal operators	105
5.3.1	Case study 1: new entrants in the advertising mail segment	105
5.3.2	Case study 2: new entrants in the domestic addressed mail market segments	107
5.3.3	Case study 3: developments in countries with network access	110
5.3.4	Summary of strategies and business models of competitor postal operators	113
5.3.5	When do competitor postal operators break even?	114
5.4	Strategies of national postal operators	115
5.4.1	Facts and figures for national postal operators	115
5.4.2	Strategic orientation of the national postal operator	117
5.4.3	Economies of scope between mail, express and logistics	119
5.4.4	Legal status of the national postal operators - searching for outside investors	119
5.5	Summary and conclusion	123
6	Likely development of competition in a liberalised environment	127
6.1	Introduction	127
6.2	Expected market developments	128
6.2.1	Expected volume developments per mail segment	128
6.2.2	Expected technological developments	129
6.3	Likely business models of competitor postal operators	130
6.3.1	The development of a full service concept	130
6.3.2	The development of a low cost model	131
6.3.3	The development of activities in part of the value chain	132
6.3.4	The development of niche markets	132
6.3.5	Technology of the production process and value added services	133

6.4	Expected strategic behaviour of national postal operators	133
6.4.1	Strategic behaviour of national postal operators on domestic markets	133
6.4.2	Strategic behaviour of national postal operators on markets of other EU Member States	134
6.5	Expected competitive entry in a liberalised environment	134
6.5.1	Pattern of competitive entry	134
6.5.2	Scale of competitive entry	136
6.5.3	Expected competitive entry under alternative scenario's	141
6.6	Likely effect on the postal sector in the Member States	143
6.6.1	Entry, contestability, and type of postal operators active on the market	143
6.6.2	Expected effect on market structure	145
6.6.3	Expected effect on services	146
6.6.4	Expected effect on prices	146
6.6.5	Expected effect on the universal service provision	148
6.7	Summary and conclusion	149
6.7.1	Pattern and scale of competitive entry	149
6.7.2	Entry, contestability and effect of liberalisation on market structure	151
6.7.3	Expected effect on market performance	153
7	Conclusion	155
7.1	Introduction	155
7.2	Summary of main findings and conclusions	155
7.2.1	Postal products and market segmentation	155
7.2.2	Liberalisation of postal markets until date	156
7.2.3	General development of internal competition until date	156
7.2.4	Strategies of postal operators	157
7.2.5	Key factors influencing the development of competition until date	159
7.2.6	Expected pattern of competitive entry in a liberalised environment	162
7.2.7	Expected scale of competitive entry in a liberalised environment	163
7.2.8	Entry, contestability and effect of liberalisation on market structure	164
7.2.9	Likely effect of liberalisation on market performance	166
7.3	Overall conclusion and recommendations	167
7.3.1	Overall conclusion	167
7.3.2	Recommendations	168

Annex I

- Appendix 1: Mail volumes by sender/receiver
- Appendix 2: Indicators for the five disciplinary forces of Porter
- Appendix 3: Authorisation and licensing
- Appendix 4: Regulation of network access
- Appendix 5: Opinion survey report
- Appendix 6: Overview of population density and urbanisation
- Appendix 7: Direct mail volumes
- Appendix 8: Market shares in the (liberalised) market for addressed mail
- Appendix 9: List of interviewed people and organisations
- Appendix 10: List of organisations that responded to the questionnaire

Annex II (separate document)

Country information sheets for the 25 EU Member States

Preface

The project team would like to thank all postal operators, policy makers, postal sector regulators and other organisations and experts that contributed to this study through completing our questionnaires, responding to specific questions and providing us with relevant documents and information.

We are also grateful for the constructive cooperation with the European Commission, DG Internal Market, and others within the Commission. In particular we wish to thank Mr. Jörg Reinbothe (Head of Unit), Mr. Hughes de la Motte, Mr. Jonathan Read, and Ms. Dominique Scheerens from the Postal Unit, DG Internal Market, for their comments and support.

We want to stress that the authors take full responsibility for the contents of this report and that the opinions expressed do not necessarily reflect the view of the European Commission.

Executive summary

Objective of the study

This report is the result of a study that has been carried out for the European Commission, DG Internal Market, by ECORYS Nederland BV in cooperation with Business Consult BV from November 2004 to July 2005.

The aim of the current study is on the one hand to describe the development of competition in the postal market and on the other hand to consider the possible future evolution of competition in a liberalised environment and provide documented and substantiated conclusions and recommendations.

The study concentrates on developments in the letter mail market with a particular emphasis on the addressed mail market segment, acknowledging the fact that other segments have by and large already been liberalised and that a further liberalisation of the postal market concerns in particular the addressed mail market segment.

Policy context

The postal sector has undergone a significant transformation during the last decade. Many of the former traditional postal administrations have changed into corporations and in some cases have even been privatised or there are plans to do so. The business approaches of the national postal operators are changing and more explicit attention than before is given to cost efficiency and customer responsiveness. Technological developments influence the provision of postal services as well as the developments in adjacent markets, such as the communication market, the advertising market, and the express market.

The above developments are reflected in the regulatory policy that has been set out by the European Commission through the directives 97/67/EC and 2002/39/EC. The purpose of Community policy in the postal sector is “to complete the internal market for postal services and to ensure, through an appropriate regulatory framework, that efficient, reliable and good-quality postal services are available throughout the European Union to all its citizens at affordable prices.” Both directives aim for a gradual and controlled market opening of the postal sector throughout the European Union.

The 2002 directive, in comparison to the previous one, further limits the postal services that can be protected from competition. According to the directive, the area that may be reserved to the national postal operator will be limited to addressed mail weighing less

than 100 grams and costing less than three times the basic tariff as from 1 January 2003 and weighing less than 50 grams and costing less than two-and-a-half times the basic tariff as from 1 January 2006. Finally, directive 2002/39/EC sets 1 January 2009 as a possible date for the complete liberalisation of postal services.

In the context of a gradual liberalisation of the postal sector, it is important to understand the current and expected development of competition and the impact this has on market structure and market performance, including on the provision of universal services. In this way, the current study aims to contribute to well informed and reasoned decision making on the further steps that can be taken to liberalise the postal sector and to support the development of effective competition on the various segments of the postal market.

Sources of information and activities undertaken

The analysis presented in this study is based on the following activities that have been undertaken to collect relevant information on the development of competition in the postal markets of the EU Member States:

- An analysis of existing studies, statistical publications, annual reports of postal operators, and other information that is publicly available;
- Questionnaires that have been developed and sent out to six respondent groups in all Member States to obtain additional and updated information;
- Visits to five countries where in-depth interviews were conducted with postal sector regulators, policy makers, national postal operators, competitor postal operators, and customers (France, Germany, Italy, the Netherlands, and Poland);
- An opinion survey that has been undertaken under more than 20 stakeholders and industry experts from seven different countries on the likely development of competition in a liberalised environment and the likely impact of competition on market structure and market performance;
- E-mail contact and telephone interviews with organisations in the different respondent groups in the Member States to discuss issues that remained unclear and to obtain missing information;
- Presentations of the research methodology and the preliminary results and conclusions at two stakeholder workshops organised by the European Commission, at 18 January 2005 and 26 April 2005, respectively.

For each Member State, a country information sheet has been prepared presenting the development of competition in the postal market of each country. These 25 country information sheets are included in Annex II to this report. Although we have tried to analyse the development of competition in each of the Member States as thoroughly as possible, it should be stressed that it is beyond the scope of this study to prepare full fledged country reviews for each of the Member States. Rather, the aim of the country information sheets is to provide sufficient background information for the more general analysis of the development of competition presented in this report. Apart from the five countries that were visited by the project team, we paid relatively much attention to describing the developments in Spain, Sweden and the United Kingdom.

Outline of the study

Chapter 1 introduces the objective of the study, the policy context in which this study is taking place and presents the sources of information and activities undertaken by the research team as well as the research method and outline of the report. In Chapter 2 we give a short description of the postal market. The chapter discusses the market segmentation and terminology, the postal value chain, the current status with regard to the liberalisation of postal markets in the Member States and presents figures on total and per capita mail volumes for the main mail categories. The liberalisation and volume data concern collated information and figures from different sources, supplemented and updated through the questionnaires and interviews that were undertaken in this study. Chapter 3 presents the conceptual framework that we use for analysing the development of competition. In particular, the five forces model of Porter is discussed, a preliminary assessment is made which market segments are contestable and the justification and economic rationale to regulate network access is examined.

Chapters 4 and 5 then turn to the discussion of the actual development of competition on the postal market in the EU Member States until date. The purpose of these chapters is twofold. The first purpose is to present an overview of relevant developments to date, including the strategies and business models that are being employed by the national and competitor postal operators. The second purpose is to gain insight in the factors that facilitate or hamper the development of competition, and herewith, to pave the ground for a well founded analysis of the likely development of competition after full liberalisation of the mail market – the topic of discussion in Chapter 6. Chapter 7 summarises the main findings of this study and presents our conclusions and recommendations.

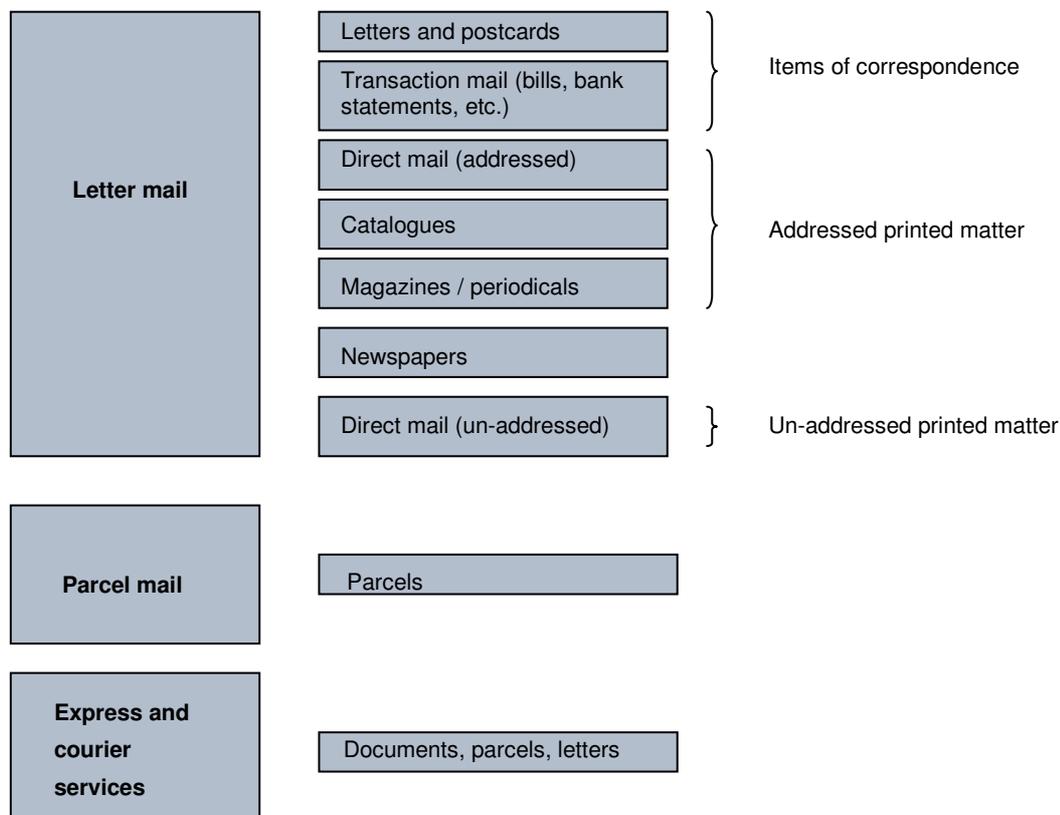
Summary of main findings and conclusions

Postal products and market segmentation

The postal market can be segmented along different dimensions that reflect the characteristics of postal service provision and form the basic ingredients of a variety of strategies and business models that can be chosen by new and existing postal operators. The most important of these dimensions are postal products, the nature of the sender and receiver of mail, time sensitivity and predictability of mail flows and the size of the mail sending.

In statistical publications and reports, different definitions are often used posing challenges to data collection and making comparisons between data sources and countries far from a straightforward exercise. In this report letter mail comprises of items of correspondence, addressed printed matter, newspapers and un-addressed printed matter with a weight of maximum two kilograms per item and adhering to certain restrictions with regard to size. Items of correspondence include personalised letters and postcards as well as transaction mail such as bank statements. Addressed printed matter comprises of direct mail, catalogues, magazines and periodicals. Addressed mail refers to items of correspondence plus addressed printed matter. The above segmentation of the postal market along postal products is represented in Figure I.

Figure I Segmentation of the postal market along postal products



The often used term advertising mail does not fully comply with these definitions, but includes a large part of the direct mail, certain catalogues and sponsored magazines. Addressed advertising mail hence largely equals addressed printed matter. In addition, a further separation between national and international mail and an extension to value added services like hybrid mail and logistic services is possible.

Historically, parcel mail and express and courier services are considered part of the postal sector. Express and courier services concern value added services with door-to-door delivery. During the last decades, express and courier services developed into a separate industry. Parcel mail concerns items above 2 kilograms with a maximum of 20 kilograms and items below 2 kilograms that do not adhere to the size restrictions for letter mail. Parcel mail has become less specific to the postal sector, as it is also handled by the express and logistics industry in addition to mail order companies and postal operators.

Liberalisation of postal markets until date

The liberalisation of postal markets until date differs markedly for the different Member States, although all of them have embarked on implementing the postal directives. Liberalisation is most advanced in Estonia, Finland and Sweden that have fully liberalised their postal markets. Germany, the Netherlands, Slovakia and the United Kingdom have taken decisions to follow suit in the near future, a couple of years earlier than the possible

date for full liberalisation set in directive 2002/39/EC. Also Norway, neighbouring the European Union, has taken this decision.

A second group of countries have liberalised a relatively large segment of the mail market (up to circa 50% of the total addressed mail volume), in particular countries that have liberalised both the delivery of direct mail and outgoing cross border mail (Czech Republic, Germany for direct mail batches above 50 items, the Netherlands, Slovenia, and Spain). Particular cases are Denmark that has liberalised the delivery of items of correspondence and direct mail above 50 grams, Spain that has never included intra-city mail in the reserved area and the United Kingdom that has liberalised the delivery of bulk mail (more than 4,000 identical mail items in one batch).

Some countries take an intermediate position by either liberalising direct mail (Italy), outgoing cross border mail (Austria, Belgium, France, Ireland, Lithuania), or incoming cross border mail (Slovakia). The other nine Member States have maintained a large reserved area of around 80% to more than 90% of the total volume of addressed mail and have not (apart from magazines and periodicals) liberalised the delivery of addressed mail below 100 grams for any of the postal products. From this group, Poland has a transitional regime reserving the delivery of mail below 350 grams to the national postal operator.

General development of internal competition until date

The market shares of the competitor postal operators in addressed mail delivery are still very small. The countries that have liberalised a relatively large part of the addressed mail segment show the highest market share for competitor postal operators: this market share is around 7-11% for Spain, 5-7% for Czech Republic, Estonia, the Netherlands, and Sweden, and 3-5% for Denmark and Germany.

In the other countries there have not emerged competitor postal operators that are challenging the position of the national postal operator until date. In general it can be concluded that the liberalisation of addressed mail above 100 grams is insufficient for the development of any meaningful competition if this is not accompanied with the complete liberalisation of the delivery of certain postal products with substantial market volumes.

The United Kingdom and France have a somewhat special position with regard to the development of competition. In both countries, competition in end-to-end services is very limited until date. France has maintained a relatively large part of addressed mail delivery in the reserved area but has liberalised the upstream market a long time ago. Mail consolidation has developed rather strongly here, with mail consolidators and large customers having three points of upstream and downstream access for final delivery by La Poste. In the United Kingdom the delivery of bulk mail has been liberalised in 2000 and in the beginning of 2004, after a period of negotiations, an access agreement was reached between Royal Mail and three competitor postal operators. Although the volume of mail handled by these competitors has grown considerably during the last year (UK Mail alone handled more than 23 million items in the first half a year since May 2004 and in March 2005 was already handling 250 million items on an annualised basis), the final delivery is undertaken by Royal Mail.

Strategies of postal operators

The empirical evidence shows that there is a large variety of business models that are used by competitor postal operators. These business models vary as much within one country as between the Member States. All these business models have in common that they differ markedly from the business model of the national postal operator and that the size of the networks that they have developed is substantially smaller than the size of the networks of the national postal operators. This observation supports the view further touched upon below that for these cases sufficient economies of density can be obtained as long as the network size is kept relatively small. More detail on the business models that competitor postal operators are using is given in the section on the expected pattern of competitive entry below.

Although data on the financial results of competitor postal operators are often not available, it appears that most of these operators need 3-5 years before they start to make the first profits. The results of companies that focus on the B2X market segments and have developed a network for two times per week delivery, like Sandd and Selekt Mail in the Netherlands and CityMail in Sweden, show that in these countries a 2-5% market share in the addressed mail market (involving the delivery of 100-200 million mail items) is sufficient to break even. Companies that focus on the B2B market segment (such as MailMerge and BusinessPost in the Netherlands) or on (other) niche or local markets need significantly less volume to break even.

Competitor postal operators that fully rely on access for final mile delivery need less time, probably only 1-3 years. The investments needed for the business model taken by UK Mail that fully relies on Royal Mail for the final mile delivery are clearly less than the investments needed if a parallel delivery network is developed. As a consequence, the point to break even is more easily reached. UK Mail is a clearly successful entrant employing this strategy and is reaching break even after one full year of operation and expecting to become profitable during its second year of operation. The annualised mail volume handled by UK Mail one year after start up is around 250 million mail items, or almost 1.5% of the total addressed mail market in the UK.

The strategies of the national postal operators are influenced by a number of relevant developments. First, the traditional revenue base is getting smaller. The emerging competition in an addressed mail market that in most Member States is stagnating (in terms of mail volumes for addressed mail) means that the mail volumes traditionally handled by the national postal operators are shrinking. Further, prices for bulk mail are under pressure, in particular in countries that have liberalised large segments of the letter mail market. Second, and related to the above, although there are a couple of notable exceptions, the financial results of quite some national postal operators show rather limited returns on sales. Third, EU legislation forbids continuous state subsidies. As a consequence, there is a clear need to operate profitably. Fourth, the competition from the communication and advertising sectors as well as the needs of the customers require the continuous development of new products and processes. Finally, in certain market segments of the domestic market it is most effective to compete through subsidiary companies that are run separately and use their own network. This is the case for the delivery of un-addressed mail and mail consolidation (for example, the French consolidators Datapost, Mikros and Dynapost are subsidiaries of La Poste), but not yet

implemented for the delivery of for example addressed bulk mail (TNT announcing that in future it may use Netwerk VSP for delivering addressed bulk mail in addition to un-addressed mail that Netwerk VSP is delivering currently is the first sign that a subsidiary will become active on this market segment as well).

The effect of the above developments is that there is a general need to improve the efficiencies in postal service provision and to broaden the revenue base, either in the domestic market (value added services, express, logistics, and/or financial services) or internationally (mainly express, logistics, and activities on foreign letter mail and parcel mail markets) or both. Often substantial investments are needed to achieve this and in many cases these can only be realised through attracting capital from outside.

By far the most active players on the addressed mail markets in the Member States are TNT (the Netherlands) and DPWN (Germany). Through joint ventures and takeovers of competitor postal operators that entered into the market these companies have secured positions in the addressed mail markets in each others markets as well as in total in eight other Member States. Both are searching for possibilities for joint ventures and takeovers and are not considering Greenfield investments to establish competing collection and delivery networks from scratch.

DPWN and TNT also showed interest in buying the stakes in the national postal operators of Austria, Belgium and Denmark that were announced for possible sale, but this did not materialise for several reasons. Eventually, the UK investment firm CVC Capital Partners acquired a 22% stake in Denmark Post. The capital injection will enable Denmark Post to invest into diversifying its revenue base and will most likely strengthen its position towards internal competitors and the national postal operators in the region. Apart from providing capital, a strategic investor like CVC Capital Partners can support in general management, but it does not necessarily provide strengthening of best practice postal management. The question remains if they will have a longer term contribution to postal sector restructuring or provide mainly mid-term solutions to prepare postal operators for future full privatisation.

From a company wide perspective and including the operations in express and logistics, DPWN, La Poste, Royal Mail and TNT are pursuing a pan-European or global corporate strategy. A number of other national postal operators seem to pursue a regional strategy (in particular the Nordic countries Denmark, Estonia, Finland and Sweden as well as the Central European countries Austria and Slovenia) and the majority a strategy focusing on their home markets more or less exclusively, at least for the time being.

Key factors influencing the development of competition until date

A number of key factors appear to influence the development of competition until date, each of which is discussed below.

Natural barriers to entry

Natural entry barriers are related to the economics of the postal market and cannot, unlike legal or strategic entry barriers, easily be influenced or be taken away by liberalisation, regulation or decisions by the postal sector regulator or the competition authority. This set

of entry barriers will continue to exist after the complete liberalisation of the postal sector and ultimately determine whether market segments are contestable or not. Natural barriers to entry are related to both the demand side and the supply side of the postal market.

The analysis of the *demand side* of the letter mail market shows that the demand side put a number of restrictions on the development of competition, but also create a number of important opportunities for new entrants, not at least because of the considerable expenses that large customers incur for postal services. Reputation and portfolio effects pose challenges to competitors and imply that for a certain type of large customers the national postal operator or a competitor postal operator linked to one of the leading European postal operators has a competitive edge over other competitor postal operators. For other customers an internationally operating postal operator can offer interesting business solutions and for handling international cross border mail postal operators with an international network have a competitive edge as well. This currently applies to not more than 5% of the addressed mail market but will become more important as a result of the increasing internationalisation of economic activities. The wish for an improved customer orientation and tailor made services as well as the general desire to have a choice between postal operators create opportunities for competition. Also a trade-off between price and quality (in terms of speed or frequency of delivery) is broadly accepted.

In general, customers demand an encompassing business solution and most ask for a full chain of postal services. Also the coverage of the delivery network is considered important by many. In a study of Berger (2004) among 549 business customers in the UK referred to in Chapters 4 and 5, the coverage of the delivery network is almost three times as important as the reputation of the postal operator, price, and the conditions for delivery and collection (the relative importance of the last four attributes being almost the same). Still, there is room for local and regional operators, as around 20% of the respondents send their mail mainly to specific regions and 41% of the mailings are posted and delivered within 50 miles.

The most important *supply side* natural entry barrier is the importance of economies of density that apply to all parts of the postal supply chain. Economies of density are obtained because the average cost of mail handling decreases when mail volumes rise given a fixed size of the network. In contrast, economies of scale refer to the cost advantages that can be achieved by increasing the network size and the mail volume that is processed through this network at the same rate (this distinction between economies of density and scale is particularly relevant for network industries).

The entry of competitor postal operators and the business models that they employ support the results of an earlier study by NERA (2004) that there are no economies of scale for end-to-end mail processing, at least not in the 'old' 15 Member States. An important implication of this result is that a competitor postal operator with a (considerably) smaller postal network can enjoy the same cost advantages based on economies of scale as the national postal operator, even at (considerably) lower mail volumes.

Economies of scope range from very low to high dependent on the combination of products offered through the same network. Economies of scope are particularly important for the products within the addressed mail segment (in particular between transaction mail that can be planned in advance, periodicals, magazines and addressed direct mail), but less for combining addressed mail and parcel delivery, addressed mail and un-addressed mail, and addressed mail and newspaper delivery, and virtually nonexistent for combining addressed mail and express delivery at a national level. At international level, however, a presence in express or logistics in a certain country offers opportunities for handling outbound B2X cross border mail as well.

Sunk costs of investments are not present in transport and delivery, but exist in sorting equipment and establishing a collection network, although these depend on the business model chosen. It is in our view fair to conclude that the postal sector is not characterised by the existence of substantial sunk costs of investment.

Legal barriers to entry

The fact that 50% to over 80% of the delivery of addressed mail is still reserved to the national postal operators has been the most important legal entry barrier to date. An important implication of the reserved area that acted as a barrier to the development of competition is that competitor postal operators are hampered in their ability to offer a comprehensive business solution to their customers. This means that, even in the liberalised mail segments, it is difficult to gain market share. In Member States where the liberalisation of the postal market is confined to the delivery of addressed mail above 100 grams, in fact only competition in niche markets is possible. In the UK, the liberalisation of bulk mail consignments of more than 4,000 items in fact means that a business model focusing on firstly establishing a position on the B2B market segment is practically impossible, because B2B mailings are predominantly below 4,000 items. The business model should focus on the B2C segment with nation wide delivery although the liberalised market segment only covers around one third of the addressed mail volumes. Developing a parallel delivery network under these conditions is very difficult, partly explaining why a number of competitors have sought access to the delivery network of Royal Mail. The full liberalisation of the delivery of addressed direct mail offers much better opportunities for new entrants to offer a comprehensive business solution for their prospective clients, as witnessed by the fact that competition is taking off in particular in the countries that have liberalised this market segment (such as in the Netherlands and in Spain and more recently in Czech Republic and in Estonia).

The main other legal barriers to entry that can be observed in the Member States at present or have caused a slowdown in the development of competition in the past are licence requirements that are overly restrictive for the business model that competitor postal operators can employ (such as in Estonia and Finland; the main restrictions relate to demanding [almost] national coverage and a high frequency of delivery), regulatory uncertainty in general and with regard to definitions in particular (creating uncertainty whether or not certain products are included in the reserved area or not), and the time that it has taken for competitors to obtain access to the P.O. Boxes and the redirection of mail.

Strategic barriers to entry

The behaviour of the national postal operators has resulted in a variety of strategic entry barriers including (attempted) predatory pricing, vertical foreclosure, litigation, use of trade marks, patent protection, and the practical (and changing) conditions under which access can be obtained. What can be generally observed is that the national postal operators try to protect their markets and deter entry as much as possible, in particular through raising non-price strategic barriers.

Absence of a level playing field

For a number of reasons there is not yet a level playing field. In many Member States competitor postal operators are in a worse position than the national postal operator because of the VAT exemptions that apply. Moreover, in countries as Austria, France and Poland the competitors do not have access to (part of) the private letterboxes, in particular in apartment buildings that have the letterboxes behind a closed front door. There is further not a level playing field between competitors and customers, as in many cases the non-discrimination clause is not applied. In effect, small mailers are in this case partially or fully deprived of the possibility to obtain better prices through mail consolidation. In turn, the business model of the national postal operators is restricted because of the universal service obligations and the principle of uniform prices for postal products in the entire country.

Dispute settlement

The issues mentioned above have given rise to a lot of disputes that have in general, by the opinion of the competitor postal operators, taken too much time to resolve. The most common disputes that are observed in many of the Member States relate to regulatory uncertainty (in particular the definition of postal products and whether or not these products are included in the reserved area), alleged predatory pricing and cross subsidisation by the national postal operators, and vertical foreclosure (alleged attempts of the national postal operators to protect the market through price discrimination, refusal to handle mail of competitor postal operators, and the access conditions for delivering mail for competitor postal operators). In some countries and in a number of cases the lack of an adequate regulatory framework and/or the absence of an independent postal regulator severely hampered the ability to deal with disputes appropriately. We do not want to suggest that the competitor postal operators are always right in these disputes, but do want to stress that timely resolving of any disputes very much contributes to reaching the kind of regulatory certainty and transparency that is needed for the development of competition to take off.

Expected pattern of competitive entry in a liberalised environment

The main drivers for competition will change after liberalisation. They will no longer be strongly influenced by the regulatory framework and in particular the extent to which market segments are liberalised but will be geared at grasping the opportunities and synergies that can be obtained in the postal market. Also the position of many national postal operators will change from a defensive strategy to a more offensive strategy.

The (non exclusive) business models that we observe at the moment and expect for the future can be classified as:

- Full service providers;
- Low cost providers operating in certain market segments or certain geographical areas (focusing on addressed bulk mail and/or networks of local operators);
- Providers offering services in part of the value chain (consolidators, upstream operators, downstream operators);
- Providers of services in niche markets (heavy documents, document exchange, same day delivery in urban areas, spot operators).

Activities in niche markets and in local markets will be undertaken by a relatively large number of operators but will in itself not pose a real competitive threat to the national postal operators in their home markets. Examples of companies that currently are employing niche activities are ADREXO in France (direct marketing packages, heavy documents) and Hays in the UK (B2B document exchange). The combined market share that niche operators will achieve in the addressed mail market will remain relatively modest because of the fact that niche operators target only part of the market and that most customers ask for a full chain of postal services that these players are unable to offer. The study by Dietl and Waller (2001) indicates that in Germany operators offering only local mail services have in total access to about 30% of the addressed mail market and the study by Berger (2004, p.96) shows that only 14% of the UK respondents prefer a specialised (niche service) postal operator and 66% an operator offering the full chain of postal services (a full service or low cost operator).¹

It is not expected that, apart from isolated cases, competitor postal operators will develop into national full service providers. This strategy is only profitable in countries where the national postal operator provides low quality services.

Much more likely business models that will be employed are low cost models focusing on addressed bulk mail not requiring next day delivery and the establishment of interregional networks that exchange mail between more or less independent local operators. The delivery frequency is expected not to exceed 2-3 times per week. Many of the existing competitor postal operators are pursuing this strategy, such as Sandd and Selekt Mail (the Netherlands), CityMail (Sweden), EP Europost (Germany) and Unipost (Spain). Unipost is a good example of competition through establishing interregional networks, but also the other mentioned companies cooperate with local partners and have outsourced part of their activities. Although these models do not target the entire market for addressed mail, they pose a competitive threat to the national postal operator and are in principle able to capture a substantial share of the market. The same applies for models focusing on last mile delivery by entrants that already have developed a delivery network through their activities in un-addressed mail or in magazines and periodicals (publishers).

Mail consolidation and a focus on upstream activities in general are also business models that can be observed in practice and are likely to be employed. Examples are Dimar in the Czech Republic, a wide variety of mail consolidators in France (including subsidiaries of La Poste and DPWN that recently took over KOBAs), and Mailland and Euromail in the Netherlands. The nature and magnitude of these models depend on the access conditions for the final delivery of mail and, for mail consolidation, on the level of price

¹ See Chapter 3, footnote 17, for the full references to these studies.

discrimination between small and large senders of mail. Favourable access conditions will in general delay the development of low cost delivery models, in particular if such access is possible at the time that no parallel delivery networks for addressed mail delivery have (yet) been developed. Although some value added will be lost for in potential substantial mail volumes, these models may be less threatening to the national postal operator (as final delivery is more likely retained) than the low cost models, depending on the anticipated impact of these low cost models on the market share of the national postal operator and revenues.

The new entrants employing these business models will be both national and international companies that, in particular for the low cost models, have some sort of delivery network already and can establish such a network by involving a variety of existing companies. The likely national new entrants into addressed mail at the national level are publishers, un-addressed mailers and new postal operators targeting specific mail flows requiring limited investments and a small network. Express companies are not expected to enter into the addressed mail market with the possible exception of outbound cross border mail.

The likely international new entrants are mainly the national postal operators that have adopted a pan-European or global strategy and operators that are pursuing a regional strategy. The former group of companies, most of all DPWN and TNT, will target countries with high mail volumes and countries and market segments with substantial unfulfilled demand. The strategy for the other smaller countries will be to engage in high end value added services. The latter group of companies will focus their attention on their neighbouring countries. It is further expected that these entrants are not interested into developing niche markets or local markets.

Expected scale of competitive entry in a liberalised environment

The scale of competitive entry and, more generally, the competitive pressure that is posed on the national postal operator through existing competitor postal operators, expected entry and the threat of new competitors entering the market will vary from country to country. In other words, it is expected that effective competition will develop at different speed in the Member States.

We examined these country differences by looking at their respective total addressed mail volumes, per capita addressed mail volumes, the potential for growth in direct mail volumes, the degree of urbanisation and the population density. When relatively high, these factors have a positive impact on the business case of new entrants by making it relatively easy to secure sufficient volumes to operate their networks in a profitable manner.

Existing competitor postal operators that are (partly) owned by one of the (major) national postal operators may profit from the reputation of the mother company, its international network, its expertise in running a business in the postal sector and its support with human resource management and staff training. The existence of such competitor postal operators is conducive to the development of competition. This factor was taken into account as well.

A summary score for the speed and intensity of the level of competition in the medium term was obtained, disregarding any remaining differences between the Member States regarding other barriers to entry that may continue to exist.

Based on this analysis we expect that, disregarding any remaining barriers related to the existence and application of country specific regulation, the potential for the development of competition in a liberalised environment in the medium term will be:

- Highest in Belgium, France, Germany, the Netherlands and the UK;
- Relatively high in Denmark, Italy, Luxembourg, Spain and Sweden;
- Moderate in Austria, Czech Republic, Finland, Hungary, Malta, Poland, Portugal, Slovakia, and Slovenia;
- Relatively low in Cyprus, Estonia, Greece, Ireland, Latvia, and Lithuania.

Entry, contestability and effect of liberalisation on market structure

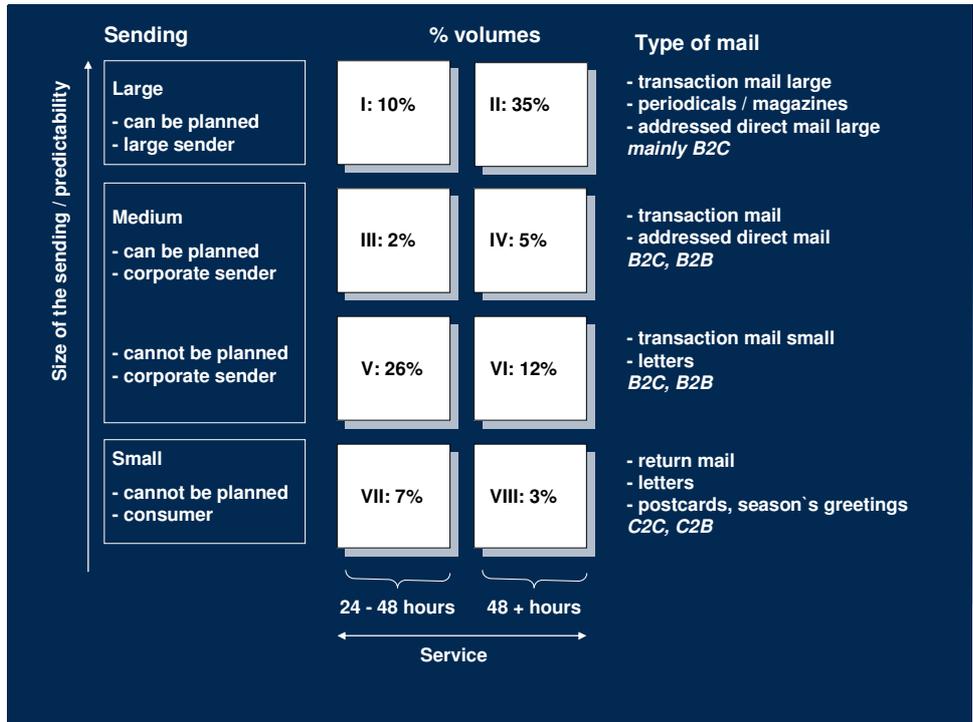
For an analysis of entry and contestability, there are so many relevant dimensions of postal service provision and different possible business models that it is impossible to make a graphic representation incorporating all relevant aspects. Figure II shows the market segmentation that we have used for assessing in which market segments entry is likely and the market segments that we regard contestable. Figure III shows our actual assessment. Note that this analysis as well as the discussion in this section focuses on business models that develop their own delivery network. Obviously, all market segments in which we expect entry are contestable as well.

The volume percentages in Figure II are indicative figures for the Netherlands. Other studies come up with comparable figures, although at higher level of aggregation. For Germany, Dietl and Waller (2001) estimate the size of the market for a mass mail provider to be 40-50% of the total addressed mail market. Such a provider focuses on market segments II and IV and targets segments I and III as well. For the UK, Berger (2004) estimates that 55% of the domestic mail items are not time critical (48+). For top 500 customers this percentage is 61%. For the Northern countries the Dutch data can, albeit very cautiously, be applied for illustrational purposes.

Countries that have relatively large C2B and C2C market segments such as Italy and Slovakia, will have in total around 10% higher shares in segments VII and VIII and in total 10% less in segments I-VI.

We expect that in a liberalised environment with a larger variety of price/quality (speed of delivery) options in the market, the percentage of mail requiring D+1 or D+2 delivery (in some countries D+1 is considered first class, in some D+2) will decrease and the percentage of mail that is not time sensitive (but often is time certain) will increase.

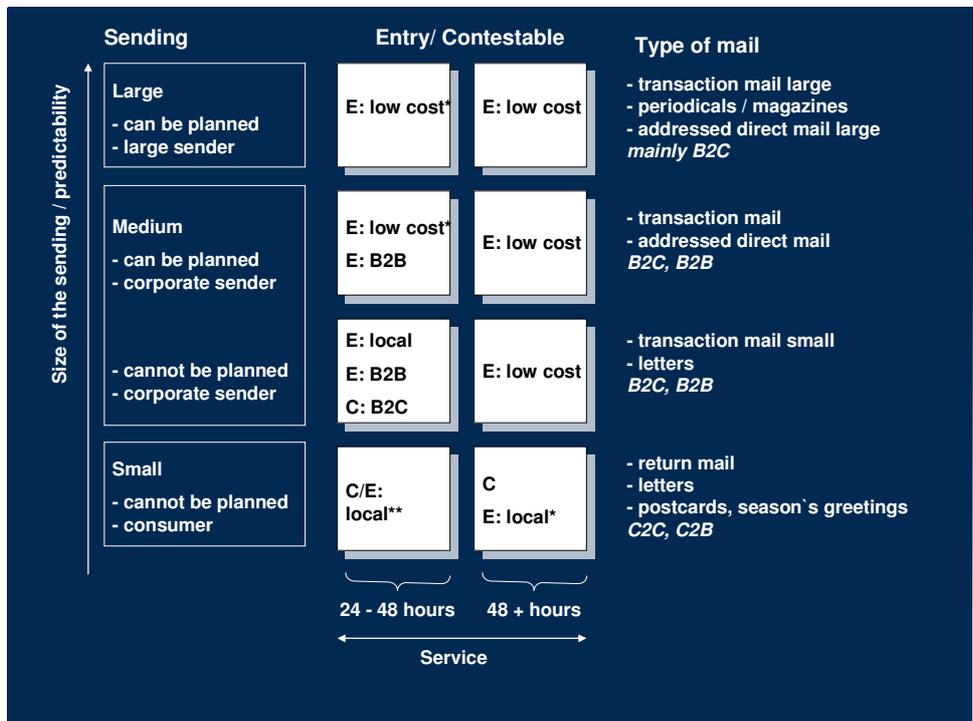
Figure II Potential market segmentation for the analysis of potential entry



Note: The volume percentages refer to the Netherlands and have indicative value only.

Source: ECORYS based on IG&H (2003, see Chapter 3 for a full reference)

Figure III Contestability (C) and expected entry (E) in market segments



Note: E (: low cost) denotes that entry is likely in this market segment by a low cost operator. * indicates that entry requires adaptations either by the competitor postal operator (more frequent delivery) or by the customer (adapting the moment that mail is produced). ** Only potential and actual entry in local markets.

Entry by low cost models is firstly expected in segments II and IV (B2B and B2C mail that can be pre-sorted and planned in advance with a 48+ hours service level) and possibly in segment VI as soon as sufficient mail volumes have been acquired, provided that some investments in sorting equipment will be made. Entry can also be expected in segments I and III, but this requires adaptations either by the competitor postal operator (more frequent delivery to offer a 24/48 hours service level) or by the customer (adapting the moment that mail is produced). Entry in segment V (individual business mail that requires a 24/48 hours service level) is only expected for B2B and in local markets. However, this market segment is contestable, as low cost operators may enter this market segment if the national postal operator is not efficient or not delivering a reliable service.

Segments VII and VIII, the collection and delivery of consumer mail, both have natural monopoly characteristics. In segment VIII, consumer mail that is not time sensitive, we expect entry at local levels but not on a national scale. In addition to the investments needed in sorting equipment for entering segment VI, also a dense collection network should be developed. Entry is easier to organise for the Season's Greetings in the short period around Christmas and New Year. The segment is anyhow contestable however, as the sunk costs for the needed investments are limited and entry is potentially possible. Finally, in segment VIII we also expect entry only to take place at local level. We regard this segment in practice not contestable. The only exception is the case that one of the competitor postal operators will outperform the national postal operator and will develop a full service model basically replacing the national postal operator.

Given the importance of economies of density and the need for a sufficient mail volume to become an efficient postal operator, there is limited room for low cost and full service operators. It is expected that in most of the Member States in addition to the national postal operators not more than one or two postal operators will operate a low cost model or, in case of an inefficient national postal operator, possibly a full service model with a delivery network covering the entire country. In addition to these operators, a small number of low cost operators with a smaller network (active in only part of the country) and a larger number of players targeting at niche markets and local markets will be active as well. The choice for relatively favourable access conditions in the UK will most likely deter the development of a parallel delivery network and the emergence of low cost operators.

In Finland and Sweden, large countries with a very low population density, a competitor with a national covering delivery network may not emerge and may be confined to the larger cities and more densely populated parts of the country. For example, CityMail, the main competitor of Sweden Post, is not aiming to reach national coverage. Also in the countries where the potential for the development of competition is relatively low (Cyprus, Estonia, Greece, Ireland, Latvia, and Lithuania) there may not emerge a low cost operator with a nation wide delivery network. The economics of postal service provision may not allow for two operators operating a nation wide delivery network profitably at the same time. In these countries we expect competition in value added services and in niche markets and local or regional markets. However, on the other extreme, if the national postal operator does not manage to work efficiently and deliver good service, the possibility exists that a new entrant can eventually outperform the national postal operator and takes its place

Overall, the national postal operators are expected to preserve their dominant position in their home markets and in general a market structure resembling an oligopoly will emerge. The market share of the national postal operators for the delivery of addressed mail is expected to become around 60-90% in the medium term. The market share will be highest (close to 100%) for consumer mail requiring next day delivery (segment VII), relatively high (80-95%) for segments V (individual business mail requiring next day delivery) and VII (non time sensitive consumer mail), a bit lower but still high for segments I, III, and VI, and lowest for addressed bulk mail that can be planned in advance with a 48+ service level (II and IV). For these segments the market share of the national postal operator may well fall to levels like 30-50% if credible competitor postal operators will have made an entry to the market.

The market shares that national postal operators can retain further relate to whether or not uniform tariffs will be still imposed as part of the universal service obligations, in particular for bulk mail. In general, it is for competitors easier to gain market share if there are uniform tariffs than if there are no uniform tariffs.

From a European perspective, the concentration process in the EU letter mail market that already started will continue leading to a limited number of leading Pan-European postal operators, supplemented with a larger number of regional postal operators and a larger group focusing on their home markets.

Likely effect of liberalisation on market performance

Expected effect on services

The customer orientation of the postal operators is expected to (further) improve and the number of different services is expected to grow. Both value added services will be more strongly developed and the quality of service better related to the needs of the customer. A clear differentiation of service levels is foreseen (like quick and reliable, normal, and slow and cheap). New technologies will be developed and employed, in particular in relation with developments in electronic communication. Developments that can be felt the last decade are likely to continue.

The increasing range of value added services will be mainly developed for B2X, such as new sorting concepts, data management of addresses and mail room management, hybrid mail, computer generated business mail, letter preparation, mail consolidation, track & trace and 2nd delivery.

Expected effect on prices

In general it is expected that prices of postal products will become more related to the underlying cost structure of these products. Further, the competitive pressure on prices will be relatively high for segments where competition is expected to take off and relatively low for segments where this is not the case.

The expected effect on the prices for addressed bulk mail is that they will go down or that they will stay at competitive level. Participants of the opinion survey expect on average the prices may go down by 10-15%. Evidence in Sweden and the Netherlands indicate

that prices may go down even a bit further. In countries that currently have a uniform tariff for the delivery of bulk mail and where the cost of delivery in rural areas is substantially higher than in urban areas, the expected price decreases for the delivery of bulk mail in urban areas will be relatively high and may reach levels of 20-25%.

Prices for consumer mail, in particular the mail requiring next day delivery, will not go down and may rise instead. New entry is not expected, and certainly not in the short term, but the potential of substitution (through internet and other means of communication) poses a certain disciplinary force on the pricing policies of the national postal operators.

There will also be a pressure to raise prices for individual business mail requiring next day delivery, but this pressure is less than for consumer mail. The prices for non time sensitive individual business mail will probably go down, but less than for bulk mail, in particular if actual entry on this segment will take place or if small business mailers can make use of services of mail consolidators for (part of) their mail.

Expected effect on the universal service provision

The expected effect of full liberalisation on the universal service provision depends on the exact form that the universal service and the universal service obligations will have in future. In general there is a relation between the development of competition and the definition of the universal service.

One of the historic reasons for preserving an area that is reserved to the national postal operator was that in this way the national postal operator could generate sufficient mail volumes for profitably providing the universal service. The losses of mail volumes of the national postal operators will vary between the Member States as well as the general cost of postal service provision. The impact on the financial results remain to be seen keeping in mind that the national postal operators will most probably remain the only operator with a full service model that is attractive to a large group of customers.

Having said this, the funding of the universal service obligations is under relative pressure if the definition remains unchanged. Both the playing field that is not level (to the detriment of the national postal operator in this case) and the form in which any universal service burden is shared have an impact on the development of competition. For example, the distortions to competition are minimised if general tax income (and not a specific tax levied on certain companies or certain postal products) would be used to finance a compensation fund or provide the funds for a direct contract with a postal operator to ensure the provision of certain of the universal services.

The funding of the universal service is still under pressure if the universal service would be limited to the (overnight) delivery of single item mail compared to the current day situation, but less than above. The way how the universal service funding would be shared becomes less important for competition. A limitation of the universal service to the (overnight) delivery of single item mail would make the playing field more level than if the current definition is maintained.

If the universal service is limited to 2-3 times per week delivery the problems with funding the universal service would be minimal if at all existing. Sharing funding the

universal service is not an issue anymore. If the universal service is limited to 2-3 times per week delivery there would in effect be a level playing field in this respect and the development of competition wide open. It will have a (further) upward price effect on overnight mail for small mailers. This scenario seems rather unlikely at the moment given the resistance by different stakeholders.

We do not think that decreasing the scope of the universal service obligations will have a negative effect on overall mail volumes because lower service levels would be offered and substitute products would become more attractive. First, it is to be expected that the delivery frequency will in most Member States not go down and that first class delivery will still be offered, also when it is not required in a universal service obligation. Second, the expected lower prices for second class mail may well generate the opposite effect and may improve (for example) the position of direct mail vis-à-vis other channels for marketing.

Overall conclusion and recommendations

Overall conclusion

It is important to realise that the level of effective competition in the postal market is not only determined by the number of competitor postal operators active in the market and their market shares, but also by the existence of potential substitutes, the bargaining power of customers and the risk of new competitors entering the postal industry. The continuing technological developments in particular in electronic communication will strengthen the competitive threat of substitutes to postal products and will cause a transformation of traditional postal products to products that further integrate postal services and electronic communication. Both the bargaining power of large customers and the risk of new competitors entering the industry will increase after a full liberalisation of the postal sector. Although the experiences in other sectors show that often the actual entry of new competitors has a real impact on market performance, also the combination of buyer power and potential entry is an important factor that the national postal operator has to consider seriously.

It is hence likely that in the largest part of the letter mail market effective competition will emerge within a couple of years after liberalisation, even if the national postal operator will maintain a dominant market position in the addressed mail market.

It is also important to realise that for private individuals and small companies the postage costs represent a very small part of the total expenses on means of communication including telephony and internet.

From the perspective of this study, we therefore see no reason to change the time path for the complete liberalisation of the postal market as set out in the postal directives. We conclude that liberalisation is the right way forward and see no urgent reason why customers should not be allowed to freely engage in agreements with postal operators of their own choice if these are able to propose a better business proposition in terms of price, quality or adaptation of the services to their specific needs.

Effective competition will however not emerge automatically, as the main conclusions with regard to the wide variety of factors that still hamper the development of competition show. Rather, the development of competition should be actively nurtured and supported in various ways. This should in our view be done primarily through creating a level playing field and not by favouring certain postal operators over others. In line with this view, we are in favour of policies that strengthen the development of competition in the medium to longer run rather than of policies that stimulate competition in the short run to the detriment of medium and longer term developments. These considerations form the basis for the recommendations that we make in the section directly below.

Recommendations

We have a number of recommendations to improve the functioning of the internal market and to support the development of competition:

- The policy maker and the sector regulator should undertake actions to create a playing field that is as much as possible level to all postal operators. For the development of competition it is of crucial importance that competitor postal operators can operate in the same conditions as the national postal operators. The wish to reach an agreement with the national postal operator to continue to provide universal services in the future will involve that certain restrictions will be posed on the business model that the national postal operator is able to operate. This should not be considered a major problem with regard to the level playing field, but restrictions to the operations of the national postal operators should be kept to a minimum;
- License or authorisation requirements to offer postal services must not be overly restrictive. As for the development of competition it is crucial that postal operators are able to operate relatively small networks, no restrictions should be posed to the delivery frequency and also (almost) nation wide delivery should not be required. General requirements related to business practices can be made, such as that postal operators should adhere to the quality of service levels that they put in the market (fulfilment of promise);
- The current uncertainties regarding the prevailing and future regulatory framework at EU and more importantly at Member State level should be reduced as much as possible. Also there is a clear need in different Member States to provide clear guidance on the definitions of postal products that are, or may possibly be, included in the national regulatory frameworks. In case of a partial liberalisation of the letter mail market it should be as clear as it possibly can which postal products have been liberalised and which postal products still fall under the reserved area;
- Upcoming disputes between market participants should be resolved as quickly and effectively as possible. Given the type of problems observed and the current stage of development of competition in the postal market this calls, at least for a number of years to come, for an independent and well resourced postal regulator in addition to a competition authority that can effectively and quickly resolve existing and upcoming disputes. More in general, the danger of strategic entry barriers should be understood and dealt with using general competition law;
- In addition to settling disputes and through this removing existing regulatory uncertainties, the role that a sector regulator in a transitory period should play is to ensure that access is guaranteed at reasonable conditions to the P.O Boxes and the

letterboxes, the postal code system, information on address changes, and the possibility to return mail through the network of the national postal operator. Also, the regulator should play a role on making the existing and future (negotiated) access conditions to the network of the national postal operator transparent and non-discriminatory (see also below). If necessary, the regulatory framework should be adapted to ensure that access conditions will be applied for mail consolidators, customers, and competitor postal operators in a non-discriminatory way;

- We do not recommend ex ante regulation of the access conditions to the facilities of the national postal operators. The full liberalisation of the postal market accompanied by concerted actions to support the development of competition and the creation of parallel networks of different forms and sizes is in our view the best route to go. We expect that after liberalisation a variety of (small) competitors will emerge as well as one and possibly two low cost postal operators with a nation wide delivery network or at least covering a substantial part of the country. The reason why such operators in some countries and regions may *not* emerge is because of the natural monopoly characteristics of B2C delivery in these countries or regions, and not because of the sunk cost character of the needed investments (these are not prohibiting entry). The national postal operators do have first mover advantages, but this does not prohibit entry as well;
- Rather than regulating access ex ante, it should be ensured that there is no discrimination between customers and competitors with regard to the terms of agreements for mail handling. Any access conditions should be applied in a non-discriminatory way. To safeguard that non-discrimination is applied and can be enforced if necessary, it is recommended that the national postal operators should have a public offer for their services. This public offer should not only be open and transparent, but also comprehensive. Agreements that fall outside the scope of such a comprehensive public offer should be possible as long as they do not aim to circumvent the public offer or can be considered as an abuse of dominant market position in terms of competition law. In our view this type of access will be sufficient to ensure that the network of the national postal operator can be used by competitor postal operators as a matter of last resort for part of the deliveries and that mail consolidation and upstream activities are viable economic activities contributing to product and service development;
- The postal regulator is recommended to focus their attention to market segments where effective competition is limited and where at the same time the interests of competitor postal operators and/or customers may be substantially at stake;
- In particular after the full liberalisation of the postal market there is a need to define relevant markets. Using these relevant markets the existence of any dominant position of a market participant can be established;
- Ex ante regulation should in our view be applied very cautiously. If (recurrent) abuse of dominant market position is very likely to happen and has a severe detrimental impact on the position of competitors or customers, ex ante regulation can be considered.

1 Introduction

1.1 Objective of the study

This report is the result of a study that has been carried out for the European Commission, DG Internal Market, by ECORYS Nederland BV in cooperation with Business Consult BV from November 2004 to July 2005.

The Terms of Reference for this study stipulate a dual objective and a number of main results that should be achieved by the Contractor:

On the one hand, it aims to describe, analyse and explain the segmented development of competition and, on the other hand, it aims to use this analysis and extensive discussions with stakeholders to consider the likely future development of competition in a liberalised postal market.

The study should identify actual and potential competition to underpin the analysis for the study of the impact on the universal service of the full accomplishment of the internal market as required in the Article 7 of the revised postal Directive.

The study should identify key factors influencing the development of competition in the postal services market, show how they interrelate and assess how each has influenced the development of competition in the Community.

Further it should consider the possible future evolution of competition in the postal market and, as a result of the analysis provide documented and substantiated conclusions and recommendations.

The study concentrates on developments in the letter mail market with a particular emphasis on the addressed mail market segment, acknowledging the fact that other segments have by and large already been liberalised and that a further liberalisation of the postal market concerns in particular the addressed mail market segment.

1.2 Policy context

The postal sector has undergone a significant transformation during the last decade. Many of the former traditional postal administrations have changed into corporations and in some cases have even been privatised or there are plans to do so. The business approaches of the national postal operators are changing and more explicit attention than before is given to cost efficiency and customer responsiveness. Technological developments influence the provision of postal services as well as the developments in

adjacent markets, such as in the communications market, the advertising market, and the express market.

The above developments are reflected in the regulatory policy that has been set out by the European Commission through the directives 97/67/EC and 2002/39/EC. The purpose of Community policy in the postal sector is “to complete the internal market for postal services and to ensure, through an appropriate regulatory framework, that efficient, reliable and good-quality postal services are available throughout the European Union to all its citizens at affordable prices.” Both directives aim for a gradual and controlled market opening of the postal sector throughout the European Union.

The 2002 directive, in comparison to the previous one, further limits the postal services that can be protected from competition. According to the directive, the area that may be reserved to the national postal operator will be limited to addressed mail weighing less than 100 grams and costing less than three times the basic tariff as from 1 January 2003 and weighing less than 50 grams and costing less than two-and-a-half times the basic tariff as from 1 January 2006. Finally, directive 2002/39/EC sets 1 January 2009 as a possible date for the complete liberalisation of postal services.

In the context of a gradual liberalisation of the postal sector, it is important to understand the current and expected development of competition and the impact this has on market structure and market performance, including on the provision of universal services. In this way, the current study aims to contribute to well informed and reasoned decision making on the further steps that can be taken to liberalise the postal sector and to support the development of effective competition on the various segments of the postal market.

1.3 Sources of information and activities undertaken

The analysis presented in this study is based on the following activities that have been undertaken to collect relevant information on the development of competition in the postal markets of the EU Member States:

- An analysis of existing studies, statistical publications, annual reports of postal operators, and other information that is publicly available. In particular, this study makes extensive use of two studies on the postal market that have been conducted for the European Commission in 2004: *Economics of postal services* by NERA Economic Consulting and *Main developments in the European postal sector* by WIK;
- Questionnaires that have been developed and sent out to six respondent groups in all Member States to obtain additional and updated information (policy makers, postal sector regulators, national postal operators, competitor postal operators, large customers, and consumer representative organisations);
- Visits to five countries where in-depth interviews were conducted with regulators, policy makers, national postal operators, competitor postal operators, and customers (France, Germany, Italy, the Netherlands, and Poland);
- An opinion survey that has been undertaken under more than 20 stakeholders and industry experts from seven different countries on the likely development of competition in a liberalised environment and the likely impact of competition on

market structure (entry, development of market shares) and market performance (services, prices);

- E-mail contact and telephone interviews with organisations in the different respondent groups in the Member States to discuss issues that remained unclear and to obtain missing information;
- Presentations of the research methodology and the preliminary results and conclusions at two stakeholder workshops organised by the European Commission, at 18 January 2005 and 26 April 2005, respectively.

For each Member State, a country information sheet has been prepared presenting the development of competition in the postal market of each country. These 25 country information sheets are included in Annex II to this report. Although we have tried to analyse the development of competition in each of the Member States as thoroughly as possible, it should be stressed that it is beyond the scope of this study to prepare full fledged country reviews for each of the Member States. Rather, the aim of the country information sheets is to provide sufficient background information for the more general analysis of the development of competition presented in this report. Apart from the five countries that were visited by the project team, we paid relatively much attention to describing the developments in Spain, Sweden and the United Kingdom.

1.4 Research method and outline of the report

In *Chapter 2*, we provide a brief description of the postal sector and introduce the terminology that we will use throughout this report. In particular, we discuss the market segmentation and postal products and provide figures on mail volumes for the different segments for each of the Member States. Further, we briefly discuss the postal value chain, touch upon the supply chain of the express industry, and provide a short overview of the current regulation of the postal sector in the Member States. With regard to regulation, our focus is to identify which market segments have been opened for competition and which are still reserved for the national postal operator.

The five forces model of Porter is discussed in *Chapter 3* as well as the question to what extent segments of the postal market are contestable. The conceptual framework of Porter is particularly useful since it provides an elegant way to list, describe and analyse the competitive forces an operator in a particular industry has to deal with. Moreover, it shows the extent to which an industry is competitive and is offering opportunities for new business. By analysing the competitive forces step-by-step and valuing them on the basis of market information, a clear picture of the actual and the potential of competition can be obtained.

The contestability of market segments in fact focuses on one particular force governing competition in an industry: the risk of competitors entering the industry. In many sectors, the entrance of new competitors proved of crucial importance to the (change in) market behaviour of the existing competitors and on the dynamics of competition in the market. To what extent market segments are contestable and whether or not entry will take place obviously depends on regulation but also on a range of market barriers.

Finally, in Chapter 3 we analyse the rationale and justification to regulate access to the facilities of the national postal operators, which is very much related to the discussion on contestability of market segments.

Chapters 4 and 5 discuss the actual development of competition in the postal sector in the Member States. In *Chapter 4* we present an overview on how competition has developed in the Member States and summarise the key factors that appear to facilitate or hamper the development of competition.

Chapter 5 continues the discussion of competition in the EU Member States by analysing the strategic behaviour of postal operators and potential entrants and the requirements and considerations of the customers of postal operators. Three case studies are presented that highlight relevant developments until date and the strategies of both the (newly emerged) competitor postal operators and the national postal operators are discussed. One of these case studies deals with the experiences of a number of countries with granting competitors (mostly negotiated) access to certain facilities of the national postal operator.

In *Chapter 6*, the analysis of Chapters 3-5 is combined with the information on market volumes in Chapter 2 to predict the business models that are most likely to be employed in a liberalised environment. Again, attention is paid to both (potential) competitor postal operators and national postal operators.

The analysis in Chapter 6 continues with an assessment of the expected competitive entry in a liberalised environment and briefly assesses the expected competitive entry under alternative scenarios. In particular we compare the anticipated effects of liberalisation of addressed mail above 50 grams and different access regimes with the baseline scenario of full liberalisation without regulating access. A structured analysis of the results of Chapters 2-5 is used to analyse the expected future development of competition in a coherent manner for the various mail segments and the postal sector as a whole. The discussion in Chapter 6 further incorporates the results of the opinion survey on the likely development of competition in a liberalised environment.

The existing situation and expected development with regard to market structure (including entry and the development of market shares per market segment) and market performance (the effect of existing and expected competition on services, prices) is subsequently analysed. Hence, in our methodology we make use of the structure-conduct-performance paradigm (SCP) to conceptualise different aspects related to competition rather than using the SCP paradigm as a causal relationship from structure to conduct to performance. The analysis of the expected effect of competition on market performance includes an initial assessment of the effect of market liberalisation on the provision of universal services. It should be stressed that a full analysis of the impact of liberalisation on universal service provision is beyond the scope of this study and will be subject of an upcoming study that will be commissioned by the European Commission.

It should further be stressed that the analysis of the impact of the expected development of competition on market structure and market performance leads to indicative results, presented in the form of certain band widths. One should keep in mind that this analysis

concerns assessing the *likely effect or impact* on the market of the *expected* strategic behaviour of firms.

Finally, we summarise in *Chapter 7* the main findings of this study and present our conclusions and recommendations.

This report further includes two annexes.

Annex I contains a number of appendices with information on the organisations that responded to the questionnaires that have been sent out and the people and organisations that have been interviewed, as well as certain summary or other tables that are referred to in the main text and the results of the opinion survey.

As mentioned above, *Annex II* contains country information sheets for each of the 25 Member States presenting the development of competition in the postal market on a country by country basis.

2 Description of the postal market

2.1 Introduction

In this chapter the market for postal services is briefly described. In Section 2.2 we discuss the market segmentation and introduce the definitions that are used throughout the report. The postal value chain and the supply chain of the express industry are briefly discussed in Section 2.3 and the current regulation of the postal sector in the Member States in Section 2.4. The main aim of the analysis in Section 2.4 is to identify which market segments have been opened for competition and which are still reserved for the national postal operator. In Section 2.5 we provide figures on mail volumes for the different segments for each of the Member States, both total mail volumes and volumes measured per capita. Section 2.6 presents the main conclusions.

2.2 Segmentation of the postal market

2.2.1 Market segmentation along postal products

Figure 2.1 below shows a segmentation of the postal market along the line of postal products. Letter mail comprises of *items of correspondence*, *addressed printed matter*, *newspapers* and *un-addressed printed matter* with a weight of maximum two kilograms per item and adhering to certain restrictions with regard to size.² Newspapers take a special position within letter mail, as in some countries the delivery of newspapers almost completely takes place outside the postal sector and is not included in statistical figures.

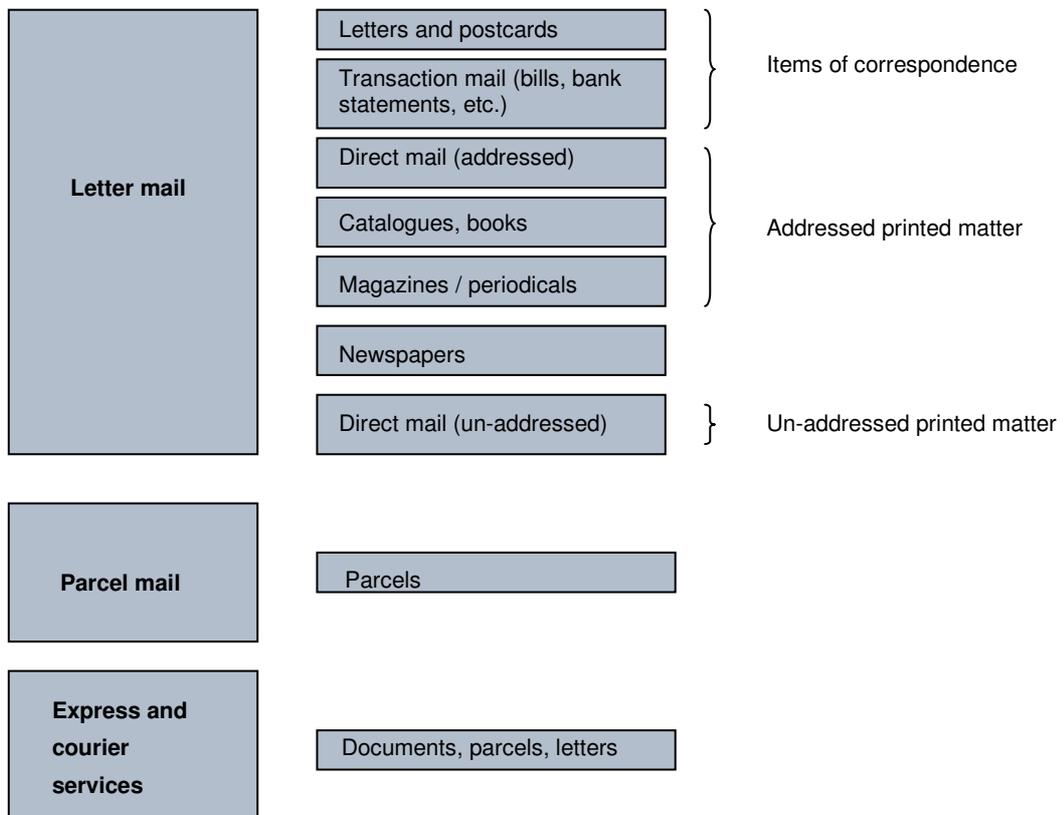
Parcel mail concerns items above 2 kilograms with a maximum of 20 kilograms and items below 2 kilograms that do not adhere to the size restrictions for letter mail. In practice, and represented in regulatory frameworks as well, items above 20 kilograms are considered to be outside the postal sector.

Express and courier services concern value added services with door-to-door delivery. During the last decades, express and courier services developed into a separate industry. Currently, the core business of the express industry is the provision of value-added, door-to-door transport and deliveries of next-day or time-definite shipments, including documents, parcels and merchandise goods.³

² For instance, it should be possible to deliver items of correspondence and direct mail through the letterbox.

³ *The Economic Impact of Express Carriers in Europe*, Oxford Economic Forecasting, October 2004, p.5.

Figure 2.1 Segmentation of the postal market along postal products



In addition, a further separation between domestic and cross-border mail and an extension to value added services like hybrid mail and logistic services is possible.

The distinction between items of correspondence and printed matter is based on the extent to which an item is personalised. The content of a letter contains information that is specific to the addressee, whereas the content of direct mail and other printed matter does not contain such information, apart from the name and address of the addressee. Un-addressed printed matter does not even contain name and address information.

Throughout this report, the term *addressed mail* refers to items of correspondence plus addressed printed matter. Newspapers are not included in addressed mail unless stated otherwise. The term *advertising mail*, used in several publications and sometimes referred to in different parts of the report, does not fully comply with the segmentation of the postal market in postal products presented above, but includes a large part of the direct mail, certain catalogues and sponsored magazines.

2.2.2 Market segmentation using other criteria

The postal market can also be segmented using other criteria. These criteria concern other dimensions of postal services and are in fact additional to, or a further specification of, the segmentation along postal products described above.

A first commonly used alternative (or additional) segmentation is one that makes a distinction between the type of sender of mail and the type of receiver of mail. Usually, a distinction is made between businesses (B) and consumers (C), leading to the following segmentation of the postal market:

- B2B: business to business;
- B2C: business to consumer;
- C2B: consumer to business;
- C2C: consumer to consumer.

A second way to segment the postal market is to consider the *time sensitivity* of the delivery as well as whether or not the submission of mail for delivery can be *planned in advance* or not. Some mail streams require next day delivery (D+1) and some do not (D+2, D+3, etc). In addition, for some mail streams the certainty that the mail will be delivered on a certain day (for instance on a Saturday) or within a specified (usually short) time period is more important than the actual speed of delivery. The requirements to the network infrastructure (the production process) of the postal operator further depend on whether or not mail streams can be planned in advance. Clearly, mail that was not anticipated and should be delivered the next day poses other restrictions to the business model of the postal operator than mail that could be anticipated or that need not be delivered the next day.

A third dimension that is used to segment the market considers the quantities of mail that are submitted and how the mail is, or could be, produced. Specifically, a distinction can be made between individual mail items and bulk mail that is computer generated. Bulk mail can consist of various postal products, but one at the time. Transaction mail and direct mail is usually sent in bulk and is computer generated.

It should be mentioned that the market segmentation along the dimensions presented above does not correspond to the definition of relevant markets in the postal sector that would be used in competition policy while assessing, for example, future proposed mergers or complaints on the abuse of a dominant position of a postal operator. It does however in our view provide a good starting point for defining relevant markets.⁴

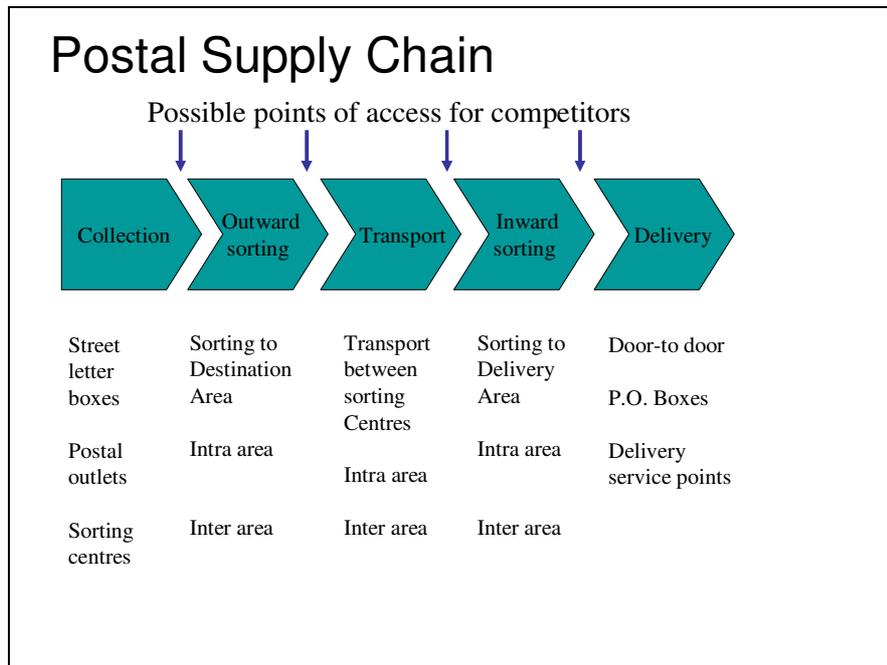
2.3 The postal value chain

2.3.1 Traditional postal supply chain

The traditional postal supply (or value) chain is build around the core mail handling operations of postal services, such as collection, transport, sorting and delivery. Figure 2.2 shows the traditional postal supply chain and indicates points where competitors or customers could in principle have access to.

⁴ To our knowledge a serious analysis with regard to defining relevant markets has yet to be made for the postal sector. Though it is not one of the objectives of the current study to define relevant markets (in the sense of competition policy), the analysis presented in the study provides much of the background information that is necessary to do so, although the ultimate analysis has to be done on a country by country basis.

Figure 2.2 The traditional postal supply chain



Historically, the national postal operators maintain a nationwide distribution network for the collection and delivery of mail to business and private addressees with a frequency of collection and delivery of at least five days per week. The postal network consists of post offices and mail handling operational units, dealing with integrated mail operations throughout the network. While the post office network used to combine front office operations (post office mail and financial service transactions to individual customers) with back office operations (mail sorting and delivery to P.O. Boxes), the provision of new services with different requirements has increasingly led to a separation of mail and other post office operations in a new range of service points to target groups of business customers and individual customers.

2.3.2 Modern postal value chain

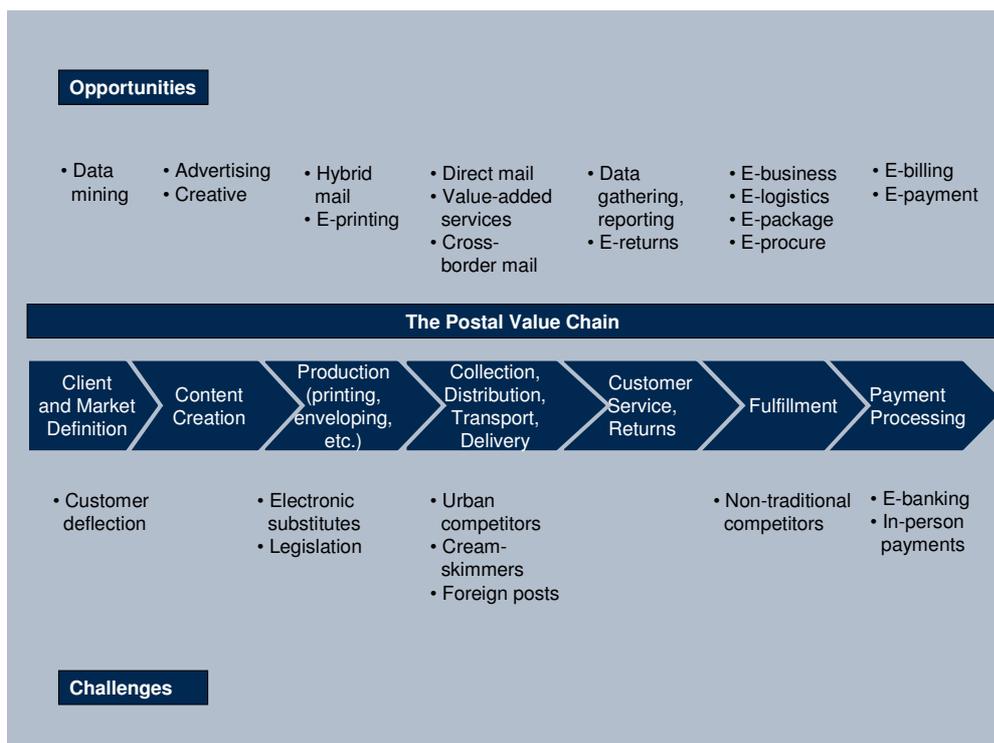
Over the last two decades, the postal sector has transformed from a process-oriented industry to a market and customer-oriented industry. This has given rise to a redefinition of the postal value chain. The modern postal value chain is not any longer defined in terms of the core mail handling operations (collection, transport, sorting and delivery), but is defined in terms of functions or contributions to the market and customers (see Figure 2.3).

The transformation involved a process of forward and backward integration of activities around the core value chain of 'postal' operational processes:

- *Forward integration* through the development of value added services, organising returns of shipments for the mail order and other industries, postal services linked to e-commerce, including fulfilment of web-based service transactions and full integration of postal and financial services;

- *Backward integration* through the development of databases, using the postal code for market segmentation and improvement of sorting and optimising distribution; content creation in cooperation with the advertising industry and last but not least pre-mailing activities, such as printing and enveloping and the use of hybrid mail services.

Figure 2.3 The modern postal value chain



Source: presentation "A changing postal world", Fouad H. Nader, PalExpo, Geneva, October 2000

2.3.3 The supply chain of express and courier services

Express and courier services have traditionally been part of the postal sector, but, as mentioned above, the express industry has developed into a separate industry. The express industry has developed from the delivery of documents and parcels to specialist items such as high-tech products, semiconductors and general airfreight commodities.⁵ The types of goods transported are typically high value/low weight items such as electronic components and pharmaceutical products.

The supply chain of express services involves door-to-door collection and delivery while controlling the entire process. Usually, the item is collected at the end of the work day at the premises of the sender, transport and (if applicable) customs clearance is taking place in the evening and night, and the item is delivered at the premises of the receiver in the

⁵ *The Economic Impact of Express Carriers in Europe*, Oxford Economic Forecasting, October 2004, p.6.

morning. The sender has access to information on the progress of the shipments from collection to delivery and is provided with proof of delivery. The express industry focuses mainly on B2B services.

Four companies that are referred to as *integrators* are the leaders of the global express industry: DHL (part of DPWN), FedEx (USA), TNT (the Netherlands), and UPS (USA). Many other smaller companies are active in this sector, sometimes as local partners of the integrators.

2.4 Regulation of the postal sector in the Member States

2.4.1 Postal directives 97/67/EC and 2002/39/EC

The regulation of the postal sector in the Member States of the European Union influences the opportunities for new postal operators to enter postal markets and to compete with the national postal operator. The European Commission has set the regulatory landscape via two directives, directives 97/67/EC and 2002/39/EC. Both directives aim for a gradual and controlled market opening of the postal sector throughout the European Union. The 2002 directive, in comparison to the previous one, further limits the postal services that can be protected from competition. The directives established regulatory provisions including the definition of a minimum universal service, a maximum reserved area, the conditions governing the provision of non-reserved services and access to the network, tariff principles and the transparency of accounts, quality of service requirements, the harmonisation of technical standards, and deal with the consultation of interested parties. Directive 97/67/EC further required the creation of a national regulatory authority that is independent from the postal operators.

The process of the creation of an internal market for postal services and the corresponding harmonisation of postal legislation in the Member States has probably been one of the most important drivers for changes in national postal regulation and herewith for the development of competition on national postal markets.

In comparison with directive 97/67/EC, directive 2002/39/EC further limits the postal services that can be protected from competition. According to the directive, the area that may be reserved to the national postal operator will be limited to items of correspondence that:

- Weigh less than 100 grams and cost less than three times the basic tariff as from 1 January 2003;
- Weigh less than 50 grams and cost less than two-and-a-half times the basic tariff as from 1 January 2006.

Furthermore, all outgoing cross-border mail is set to be open to competition as from 1 January 2003, although exceptions are possible if these are deemed necessary to maintain the universal service. For example, if the revenue from cross-border mail is necessary to finance the domestic universal service or where the national postal service in a given Member State has specific characteristics.

Finally, directive 2002/39/EC sets 1 January 2009 as a possible date for the full liberalisation of the postal markets, to be confirmed (or changed) by a co-decision procedure, with the agreement of both the European Parliament and the Council.

2.4.2 Provision of universal services

The postal directive 97/67/EC defines the minimum requirements with respect to the scope of the universal services, access conditions, delivery requirements and the quality of service, as well as complaints and redress procedures. In general, the universal service obligations that are posed on/agreed with the national postal operator ensure that every citizen can make use of postal services on reasonable conditions and at a uniform tariff for each postal product of a certain weight class.

In practice, the scope of universal services and delivery requirements do not deviate much between the Member States. The universal service includes the collection, sorting, transport and delivery of addressed mail up to 2 kilograms and of parcels up to 10 or 20 kilogram, as well as services to register or to insure an item. Collection and delivery takes place five or six days per week with a few exceptions for certain rural regions.

The situation with regard to access conditions and quality of service does however differ from country to country. Access conditions refer to the service points of the postal network, like the street letter boxes, post offices and other outlets that provide postal services. The regulatory requirements with regard to the density of these access points vary from nonexistent to detailed guidelines on the location of access points to density, distance, population, or community related criteria.⁶

Like regulation in general, universal service obligations pose restrictions on the universal service provider and have an impact on its strategic behaviour and the development of competition in the postal sector. How the universal service obligations interact with the development of competition is discussed in Chapters 4 and 6 of this report.

2.4.3 Liberalisation of postal markets in the Member States

All Member States have implemented the postal directives 97/67/EC and 2002/39/EC or are in the process to complying with these directives. Table 2.1 shows for each of the Member States for which postal product and weight class the postal market has been liberalised. It should be kept in mind that the liberalisation concerns the delivery of these postal products, as the reserved area does not apply to any of the upstream activities in the postal supply chain.

From Table 2.1 can be observed that some of the Member States have liberalised their markets more than the minimum requirements set by the directives, while others have

⁶ Source: WIK (2003, 2004). Another issue concerns the regulation of postal outlets and the requirements for their staff. For instance, in Germany only post offices may deliver postal services and post office staff should be employed by the national postal operator.

made use of the possibility to temporarily maintain a reserved area for outgoing cross border mail or have a transitional regime (Poland).

A further opening of the postal markets has been achieved along a number of dimensions that are briefly discussed below:

- The weight limit of postal products;
- Postal products;
- The size of the mail sending;
- Geographical indicators.

Liberalisation of postal products with lower weight limits

Three countries have completely abolished the weight limits for the reserved area and have fully liberalised their postal markets (Estonia, Finland and Sweden). In Denmark, the weight limit has already been reduced to 50 grams. As a result, the delivery of items of correspondence, addressed direct mail and incoming cross border mail above 50 grams has been liberalised. In addition, Germany and United Kingdom have set 1 January 2006 as the date for fully liberalising their postal markets, three years in advance of the possible date mentioned in directive 2002/39/EC. The Netherlands are reconsidering the time path for complete liberalisation that most probably will take place not later than 1 January 2007 and possibly, in line with the decisions in Germany and the United Kingdom, one year earlier. Also Slovakia (per 1 January 2007) and Norway, neighbouring the EU, have decided to fully liberalise their postal market in advance of the time path in the postal directives.

Liberalisation of certain postal products

Almost none of the countries have a reserved area for the delivery of magazines and periodicals, except France (under 100 grams) and Poland (under 350 grams). Important for the development of competition on the addressed mail segment is the fact that six countries make an explicit distinction between items of correspondence and addressed printed matter, while the other countries do not. The Czech Republic,⁷ Germany (for mail volumes above 50 items), Italy, the Netherlands, Slovenia, and Spain have liberalised the delivery of addressed direct mail although they currently have reserved the delivery of items of correspondence below 100 grams to their respective national postal operators. Adding to that the full liberalisation of the postal markets in Estonia, Finland and Sweden and the (general) liberalisation of bulk mail in the UK, ten of the 25 Member States have effectively liberalised the delivery of addressed direct mail.⁸

⁷ In the Czech Republic there have been attempts to put the delivery of direct mail again under the reserved area but this gave rise to opposition (amongst others by the European Commission) and did not materialise.

⁸ Also other services that are distinct from the universal services can be liberalised, in particular value added services. See for example the discussion related to Germany in Chapter 5.

Table 2.1 Are competitor postal operators allowed to deliver this postal product?

	IC > 100 grams	IC > 50 grams	IC > 0 grams	Outbound CBM	Inbound CBM > 100 grams	Inbound CBM < 100 grams	DM >100 grams	DM <100 grams	Periodicals/ Magazines	UDM
Min. standard	Yes	No	No	Yes	Yes	No	No	No		Yes
Austria	Yes	No	No	Yes	Yes	No	Yes	No	Yes	Yes
Belgium	Yes	No	No	Yes	Yes	No	Yes	No	Yes	Yes
Cyprus	Yes	No	No	No (< 100 gr)	Yes	No	Yes	No	Yes	Yes
Czech Republic	Yes	No	No	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Denmark	Yes	Yes	No	Yes	Yes	Yes (> 50 gr)	Yes	Yes (> 50 gr)	Yes	Yes
Estonia	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Finland	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
France	Yes	No	No	Yes	Yes	Yes	Yes	No	Yes	Yes
Germany	Yes	No	No	Yes	Yes	No	Yes	Yes (> 50 gr amso 50)	Yes	Yes
Greece	Yes	No	No	No	Yes	No	Yes	No	Yes	Yes
Hungary	Yes	No	No	No (< 100 gr)	Yes	No	Yes	No	Yes	Yes
Ireland	Yes	No	No	Yes	Yes	No	Yes	No	Yes	Yes
Italy	Yes	No	No	No	Yes	No	Yes	Yes	Yes	Yes
Latvia	Yes	No	No	No (< 100 gr.)	Yes	No	Yes	No	Yes	Yes
Lithuania	Yes	No	No	Yes	Yes	No	Yes	No	Yes	Yes
Luxembourg	Yes	No	No	No (< 100 gr.)	Yes	No	Yes	No	Yes	Yes
Malta	Yes	No	No	No	Yes	No	Yes	No	Yes	Yes
Netherlands	Yes	No	No	Yes	Yes	No	Yes	Yes	Yes	Yes
Poland	No (< 350 gr)	No	No	No (< 350 gr)	No (< 350 gr)	No	No (< 350 gr)	No	No (< 350 gr)	Yes
Portugal	Yes	No	No	No (< 100 gr)	Yes	No	Yes	No	Yes	Yes
Slovakia	Yes	No	No	No (< 350 gr)	Yes	Yes	Yes	No	Yes	Yes
Slovenia	Yes	No	No	Yes	Yes	No	Yes	Yes	Yes	Yes
Spain	Yes	Yes, icmo	Yes, icmo	No (< 100 gr)	Yes	No	Yes	Yes	Yes	Yes
Sweden	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
United Kingdom	Yes	Yes (amso 4000)	Yes (amso 4000)	Yes	Yes	No	Yes	Yes (amso 4000)	Yes	Yes

Note: IC = Items of (ordinary) correspondence, CBM = cross border mail, DM = Direct mail, Per. = Periodicals, UDM = Un-addressed mail, amso = at minimum size of ... items, icmo = intra-city mail only, Min. standard is the minimum standard set by the postal directives.

Outgoing cross border mail has been liberalised in a small majority of the Member States. The ten countries that have liberalised the delivery of direct mail have also liberalised the handling of outgoing cross border mail, with Italy being the only exception. In addition to this group of countries, also Austria, Belgium, Denmark, France, Ireland and Lithuania liberalised outgoing cross border mail. The countries that have decided not to liberalise the handling of outgoing cross border mail below 100 grams have a relatively high share of cross border mail in total mail volumes (like Cyprus, Luxembourg, Malta) and fear the impact of liberalisation on the universal service obligations or for other reasons aim to protect the national postal operator from competition on this market segment.

Liberalisation of bulk mail

In the United Kingdom the delivery of bulk mail (defined as mailings of more than 4.000 items) has been taken out of the reserved area. This applies to items of correspondence (in particular transaction mail) as well as to direct mail.

Liberalisation of intra-city mail

In Spain, intra-city mail has never been part of the reserved area. The delivery of all postal products within cities is hence open to competition.

The liberalised segment of the addressed mail market is hence 100% for Estonia, Finland and Sweden. For the other countries our best estimate is varying from less than 10% for countries with relatively large reserved areas (such as Poland, Lithuania and Malta) to almost 50% for Czech Republic, Germany and the Netherlands (see Annex I, appendix 8, for the figures for the Member States).

2.5 Mail volumes in the Member States

Figures 2.4-2.9 present figures for each of the Member States on total mail volumes and per capita mail volumes for the following categories:⁹

- Addressed mail;
- Items of correspondence;
- Addressed printed matter.

The figures show that France, Germany and the United Kingdom have by far the highest total volumes for addressed mail. Spain, Italy and the Netherlands also have high volumes. A group of countries ranging from Sweden, Austria, Belgium, Poland, Denmark, and Finland to Portugal take a position in the middle of the spectrum and the other countries have relatively low addressed mail volumes.

Most of the countries that have high total addressed mail volumes also have relatively high per capita volumes. Exceptions to this are Italy and Spain with relatively low per capita addressed mail volumes and Luxembourg that has very high per capita volumes. Slovenia, Ireland and to a lesser extent Malta have moderate per capita volumes although their total volumes are rather low.

⁹ See the country information sheets in Annex II for the detailed sources of the mail volumes presented.

When we turn to the addressed printed matter market segment the situation is comparable. The high per capita figures for Austria and Belgium are interesting to observe, as well as the fact that the ten countries that have the lowest per capita figures for addressed printed matter have not liberalised this market segment (except Estonia where these mail volumes have risen since the liberalisation of this market segment in 2002). From the countries that did liberalise the delivery of addressed direct mail, the per capita figures for Italy, Czech Republic, and Spain are relatively low.

The largest part of the addressed mail volumes concern business mail (B2X). The not weighted averages for the Member States for which figures are available (see Annex I, appendix 1) of the relative share of mail volumes segmented by type of sender and receiver are:

- B2B: 22%;
- B2C: 61%;
- C2B: 8%;
- C2C: 9%.

For the ten countries with highest per capita volumes for addressed printed matter, B2X mail volumes constitute between 85% and 93% of total addressed mail volumes. For the other countries this share varies between 76% and 90%.¹⁰

¹⁰ With the exception of Cyprus and Hungary that reported lower figures.

Figure 2.4 Total number of addressed mail items delivered

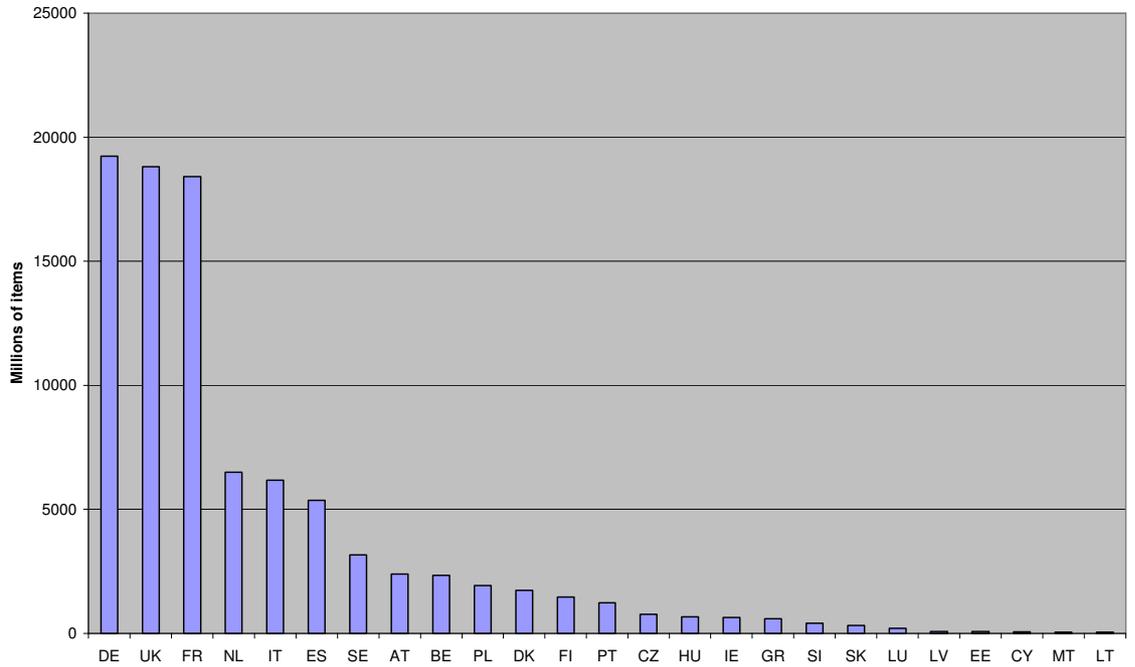


Figure 2.5 Number of addressed mail items per capital

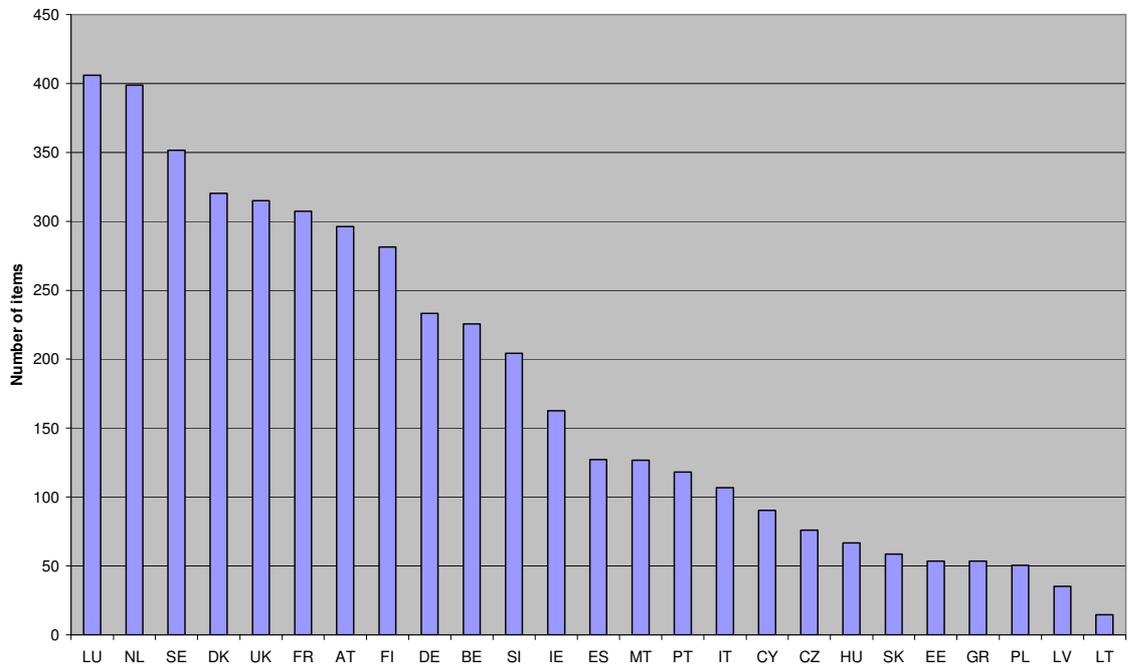


Figure 2.6 Total number of items of correspondence delivered

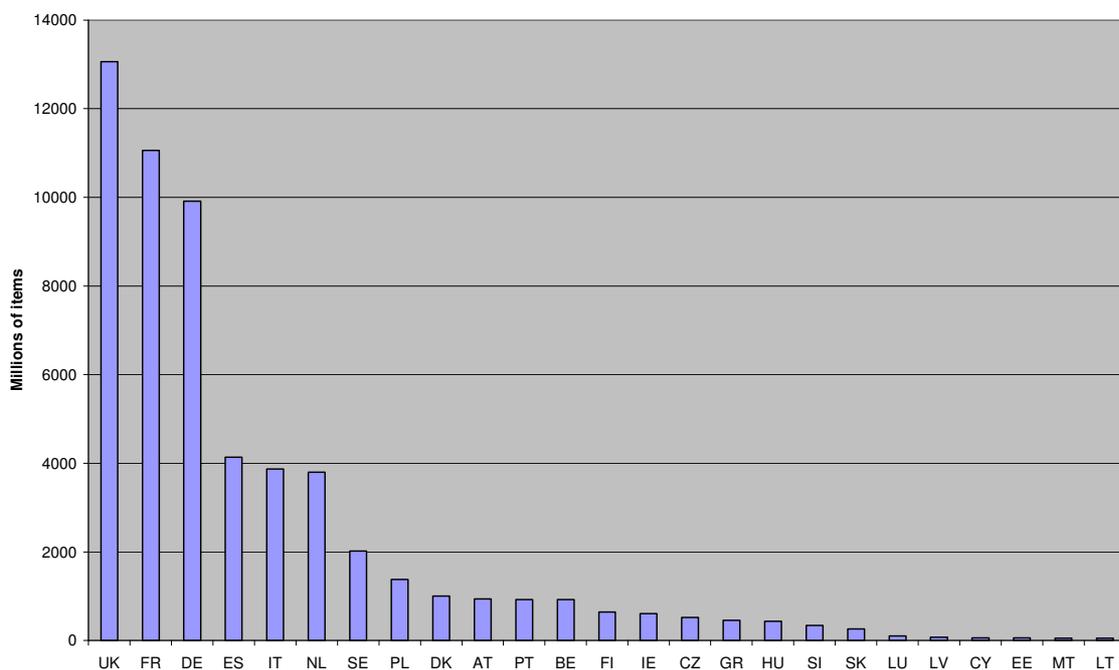


Figure 2.7 Number of items of correspondence delivered per capita

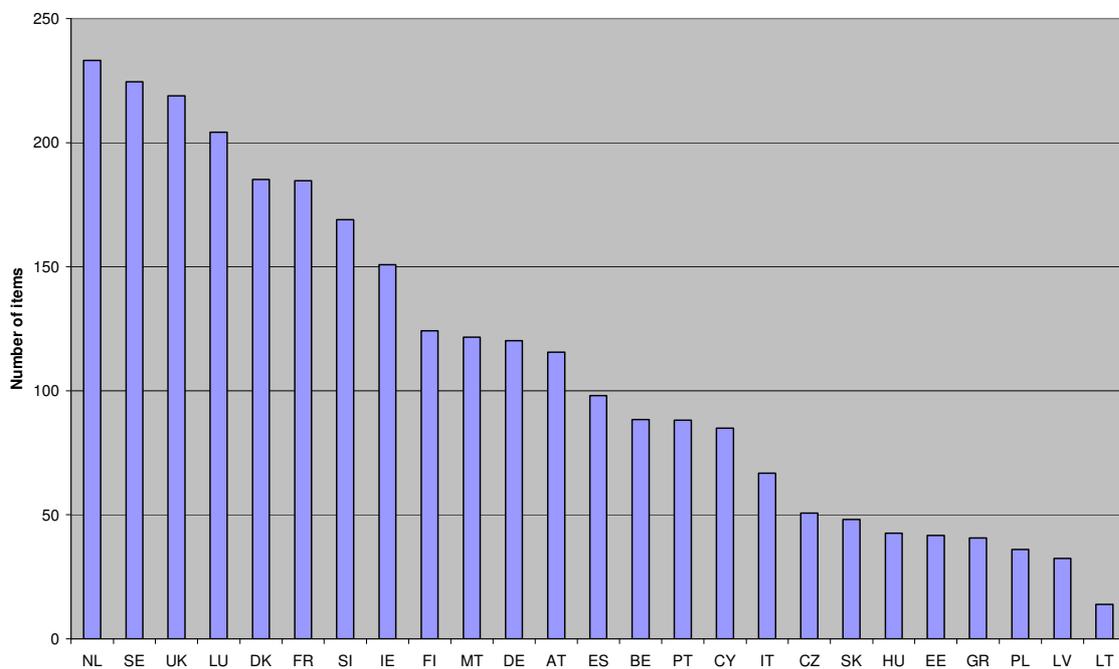


Figure 2.8 Total number of items of addressed printed matter delivered

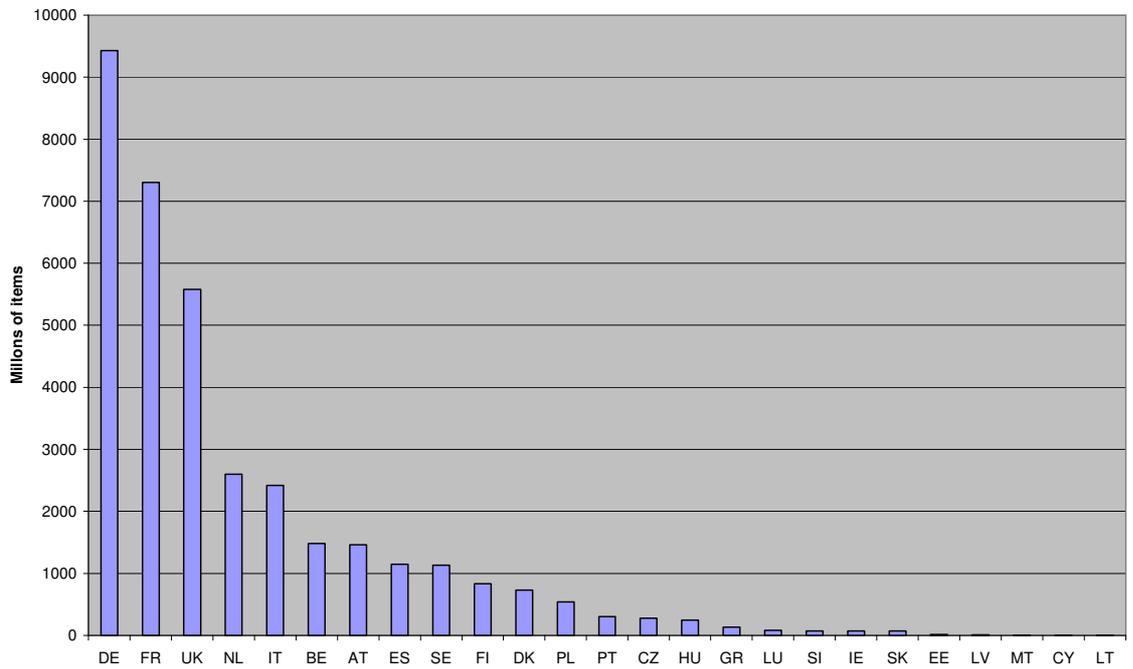
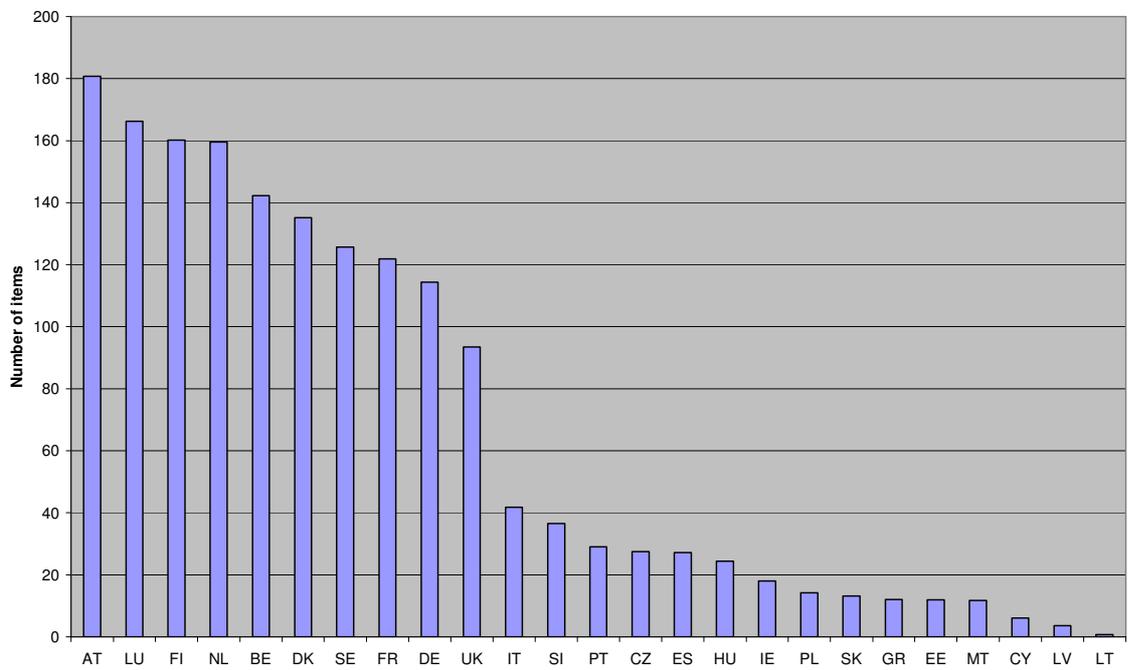


Figure 2.9 Number of items of addressed printed matter delivered per capita



2.6 Summary and conclusion

The postal market can be segmented along different dimensions that reflect the characteristics of postal service provision and form the basic ingredients of a variety of strategies and business models that can be chosen by new and existing postal operators. The most important of these dimensions are postal products, the nature of the sender and receiver of mail, time sensitivity and predictability of mail flows and the size of the mail sending.

The developments in the postal value chain show that, although the traditional supply chain encompassing collection, sorting, transport and delivery of mail has remained intact, the business orientation is changing from an orientation on processes to an orientation on markets and customers. Further, technological developments have an important impact on postal services and the environment in which the postal sector operates. Examples of new services are services linked to e-commerce, database management and hybrid mail services.

The liberalisation of postal markets until date differs markedly for the different Member States, although all of them have embarked on implementing the postal directives. Liberalisation is most advanced in Estonia, Finland and Sweden that have fully liberalised their postal markets.

A second group of countries have liberalised a relatively large segment of the mail market, in particular countries that have liberalised both the delivery of direct mail and outgoing cross border mail (Czech Republic, Germany for direct mail batches above 50 items, the Netherlands, Slovenia, and Spain). Particular cases are Denmark that has liberalised the delivery of items of correspondence and direct mail above 50 grams, Spain that has never included intra-city mail in the reserved area and the United Kingdom that has liberalised the delivery of bulk mail. Of these countries, Germany, the Netherlands, Slovakia and the United Kingdom have taken decisions to follow suit in the near future, a couple of years earlier than the possible date for full liberalisation. Also Norway, neighbouring the European Union, has taken this decision.

Some countries take an intermediate position by either liberalising direct mail (Italy), outgoing cross border mail (Austria, Belgium, France, Ireland, Lithuania), or incoming cross border mail (Slovakia). The other nine Member States have maintained a large reserved area and have not (apart from magazines and periodicals) liberalised the delivery of addressed mail below 100 grams for any of the postal products. From this group, Poland has a transitional regime reserving the delivery of mail below 350 grams to the national postal operator.

It should be stressed however that the formal liberalisation of postal market segments, though an obvious prerequisite for competition, is only one of the factors that have an impact on its development. One of the other factors that influence the development of competition are the mail volumes on the different market segments, both total mail volumes and mail volumes per capita.

The presented figures on total and per capita mail volumes show that countries that have by far the highest total volumes for addressed mail are France, Germany and the United Kingdom. Spain, Italy and the Netherlands also have high volumes. A group of countries ranging from Sweden, Austria, Belgium, Poland, Denmark, and Finland to Portugal take a position in the middle of the spectrum and the other countries have relatively low addressed mail volumes.

Most of the countries that have high total addressed mail volumes also have relatively high per capita volumes. Exceptions to this are Italy and Spain with relatively low per capita addressed mail volumes and Luxembourg that has very high per capita volumes. Slovenia, Ireland and to a lesser extent Malta have moderate per capita volumes although their total volumes are rather low.

The largest part of the addressed mail volumes concern business mail (B2X). For the ten countries with the highest per capita volumes for addressed printed matter, B2X mail volumes constitute between 85% and 93% of total addressed mail volumes. For the other countries this share varies between 76% and 90%, with the exception of Cyprus and Hungary that reported lower figures.

3 Potential for competition in the postal sector

3.1 Introduction

The aim of this chapter is to analyse the potential for the development of competition in the postal sector mainly from a theoretical perspective. Which forces are influencing the state of competition in the postal sector? Which market segments are contestable? Or, in other words, in which market segments can entry be expected or feared for (by existing postal operators) and in which market segments is entry unlikely? Is regulating access to the facilities of the national postal operators a necessary prerequisite for the development of effective competition in a liberalised environment?

The five forces model of Porter is discussed in Section 3.2. The discussion continues with an analysis in Section 3.3 to what extent the different segments of the market are contestable. This analysis incorporates the outcomes of the study by NERA (2004), in particular the results of their econometric analysis on the factors that explain the cost functions of national postal operators.¹¹ In Section 3.4 we subsequently analyse the rationale and justification to regulate access to the facilities of the national postal operators. A summary and conclusion is given in Section 3.4.

3.2 The five forces model of Porter

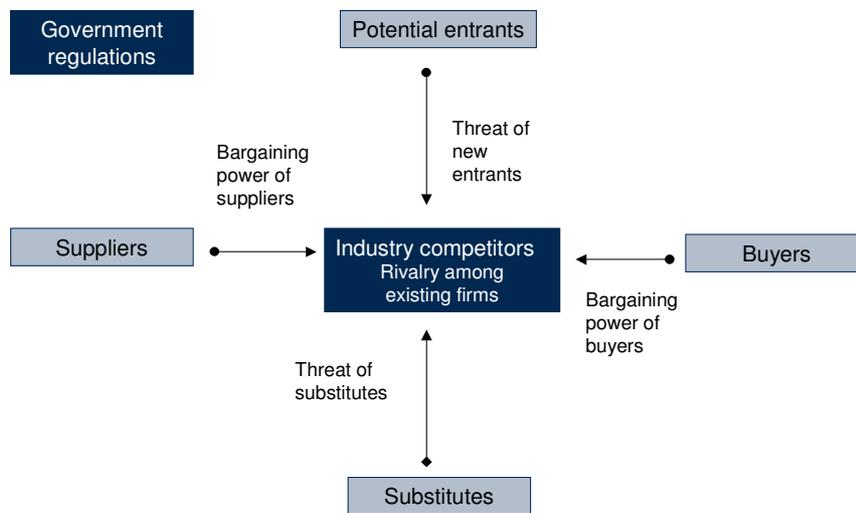
For analysing the actual and expected development of competition we make use of Porter's model of forces governing competition in an industry (see, for example, Porter 1998).¹² In this section we briefly present the five forces model of Porter and briefly discuss the relevance of the different forces for the postal sector. Porter's conceptual framework is subsequently used in the discussion in Chapters 4 and 5 and, amongst others, underlies the recommendations and conclusions presented in Chapter 6.

The state of competition, according to Porter, depends on five basic forces: the risk of *new competitors* entering the industry, the threat of potential *substitutes*, the bargaining power of *buyers*, the bargaining power of *suppliers*, and the degree of rivalry between the *existing competitors*. In Porter's initial model government regulations were not taken into account but later on added to the model. Clearly, government policy influences entry, prices and investment conditions and strategic behaviour of companies (see Figure 3.1 for a graphical representation of the model and Annex I, appendix 2, for an overview of appropriate indicators for the intensity of the five forces governing competition).

¹¹ See Section 1.3 for the specific reference.

¹² Michael E. Porter, *On competition*, Harvard business review book series, 1998.

Figure 3.1 Porter's five forces model



Source: Porter (1985), *Competitive advantage: creating and sustaining superior performance*.

The conceptual framework of Porter is particularly useful since it provides an elegant way to list, describe and analyse the competitive forces an operator in a particular industry has to deal with. Moreover, it shows the extent to which an industry is competitive and is offering opportunities for new business. By analysing the competitive forces step-by-step and valuing them on the basis of market information, a clear picture of actual and potential competition can be obtained.

Below, we concentrate the analysis on the addressed mail segment (items of correspondence plus addressed printed matter) although (parts of) the analysis is also valid for other segments of the mail market.

3.2.1 Risk of new competitors entering the industry

The risk of new competitors entering the postal sector and the way in which this influences the state of competition in the postal sector and impacts the strategic behaviour of existing postal operators is discussed at length in various sections further in this report.

Obviously, potential entry of new competitors is first of all related to the regulatory framework. For segments that are in the reserved area, there is neither a threat of entry nor actual entry of new competitors. Further, the threat of entry depends on whether or not postal market segments are contestable.¹³

¹³ This is discussed in detail in section 3.3 below. Further justification of the preliminary conclusions is then obtained while comparing this analysis with the actual empirical developments in Chapters 4 and 5.

In principle, there is potential entry of companies that are set up for this sole purpose and develop a collection and delivery network from scratch, as a Greenfield investment.¹⁴ However, given the importance of acquiring sufficient mail volumes for establishing a successful business case, more often entry of firms in the addressed mail segment can be expected from companies that are already active in certain (liberalised) mail segments, adjacent markets, or are linked to a certain stage of the postal value chain. Examples are companies that are active in delivery of un-addressed mail, large mailers, mailing houses, publishers, and address database providers. Also, there is potential entry of postal operators from other countries that wish to expand their business beyond their (traditional) home market.

3.2.2 Threat of potential substitutes

Potential substitutes have a substantial influence on the state of competition in the postal market. Figure 3.2 below depicts the postal industry in relation to the communication market, the advertising market and the transportation/logistics market.

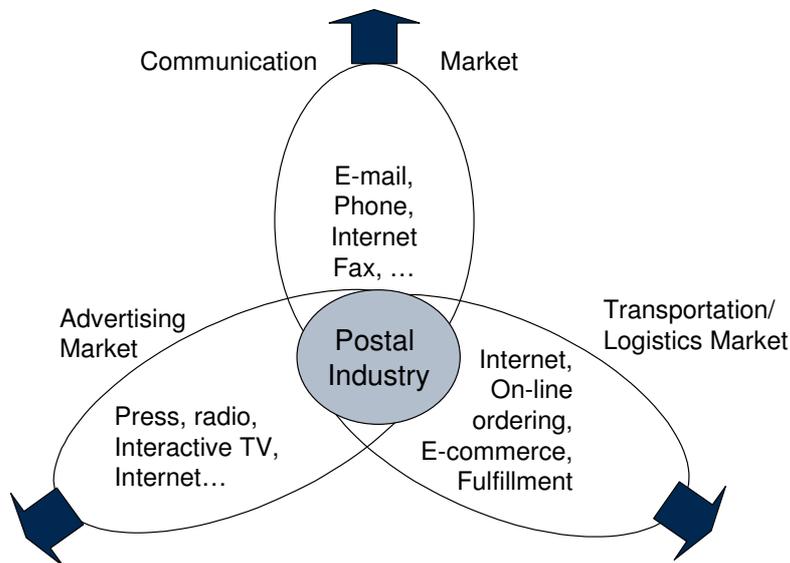
In many market segments there is increasing substitution by other channels of communication like telephony, fax, e-mail and internet. For example, regarding C2C mail, alternative modes of communication are telephony, SMS and e-mail. On the B2C segment the internet is an alternative channel of communication, in particular for transaction mail (e-billing, electronic banking).

The advertising market offers important substitute products for direct mail, such as advertisement on television and radio or in newspapers and magazines, as well as on the internet. On the other hand, there are also some opportunities because of potential complementarities. For example, parcel delivery has experienced growth because of the developments in marketing on internet and e-shopping and additional mail is generated as well (confirmations, bills, payments). Also, some marketing campaigns are based on an integrated approach, combining for instance internet, direct mail and call centres to approach their customers.

Technological and market developments will contribute to rising disciplinary pressure that substitutes will have in the coming years, in particular in the B2X markets and in countries where the use of internet is not yet widespread and is expected to increase substantially during the next decade.

¹⁴ A Greenfield investment is an investment from scratch to establish an undertaking. For example, if an entirely new production site is built (on a green and empty field), this is a Greenfield investment. Realising a new production site using existing buildings and facilities is not a Greenfield investment.

Figure 3.2 The strategic location of the postal services market



Source: Communication notice 632, European Commission, 25 November 2002 (on the application of the Postal Directive)

3.2.3 Bargaining power of buyers

The competitive force of buyers of postal services (the suppliers of mail) is particularly large in the B2C and, to a somewhat smaller extent, the B2B segment of the postal sector. Large customers such as banks, insurance companies, utilities and publishers possess buying power and demand value for money.

Large customers can put pressure on postal operators as they can potentially downscale the frequency of delivery (for example of bank statements), take care of the delivery of their own internal mail or can look for additional modes of communication with their clients. Another way for customers to exercise buyer power is to combine correspondence and herewith raise the weight above the weight limit for the reserved area. Although often not very practical at the moment, this may become a real possibility for a certain group of customers after the liberalisation of addressed mail above 50 grams.

On the C2C market there is very little buyer power. The situation in the C2B market is mixed, as in this segment the businesses (including large customers) may be interested to put pressure on the postal operators. Further, an important part of the C2B mail is reply mail to the businesses in envelopes that need no stamp and are paid for by the respective businesses.

The competitive force of large customers will increase after a full liberalisation of the postal sector. This is particularly true if there are competing postal operators on the market, but also the combination of buyer power and potential entry is an important disciplining factor.

3.2.4 Bargaining power of suppliers

Suppliers of inputs to postal operators (like the producers of sorting equipment or means of transport) are not particularly disciplining the behaviour of postal operators in terms of their price setting, frequency of delivery or coverage of the delivery network. They do however influence the business model of postal operators through developing state of the art technology for the postal industry as further explained in Box 3.1 below.

3.2.5 Degree of rivalry between existing competitors

The current and expected degree of rivalry between existing competitors is the main theme of this report. We do not discuss this important issue here, but only mention it for the sake of comprehensiveness.

3.2.6 Government regulations

For the existence and development of competition, the prevailing regulatory environment is crucial (and *vice versa*: sometimes market developments are the main reason to changes in the regulatory environment) as well as the entry barriers that exist irrespective of the regulatory environment. In various parts of this report we discuss at length the impact of government regulations on the development of competition.

Box 3.1 Interaction between suppliers and postal operators

In the last decade international fairs on postal technology (such as PostExpo and Postal Forum) have become in fashion, bringing together decision makers from all national postal operators in the world and increasingly private sector competitor postal operators as well. Often these fairs are supplemented with lectures and presentations of best practice and examples of mail solutions applied in the postal industry. In addition, postal congresses (like CRRRI Rutgers, IEA, US national postal forum) have been organised often financed by leading suppliers and postal operators and giving insight in postal sector developments in technology as well as in business development. Postal technology can provide the competitive edge over competitors and suppliers are keen to provide new solutions based on the latest technology available.

Leading suppliers such as for example Elsag Bailey/Italy, Siemens Dematic/Germany, Neopost/France, NEC& Toshiba/Japan, Pitney Bowes and Solystic-Northrop Gruman/USA and many more suppliers show their new and continuous updated technology solutions in sorting, for letter mail sorters and flat sorters for parcel mail, character recognition systems for reading of postal codes and bar codes, in database management, mailroom management and mailroom equipment and many more different types of machines/equipment to be used in modern mail processing.

Development of, and extensive communication on, postal technology has an impact on the postal industry in many different ways:

- Pressure on postal management to improve mail processing and provide new mail processing solutions;
- Benchmarking (parts of) the mail processes in terms of cost and quality, initially of letter mail and parcel sorting, but increasingly of collection, (digital) transport of hybrid mail, and delivery as well;
- Bringing down unit cost of mail handling by substituting increasingly expensive manual sorting by machine sorting;
- Implementing new forms of cooperation between leading postal operators and large mailers in the postal industry to realise win-win deals for both of them keeping postal services at edge with electronic media;
- Setting industry standards for data (postal code, barcode) and mail processing, which also contribute to exchange of mail processing in international mail exchange;
- Giving opportunities to new entrants to pass by large scale physical mail processing and provide new solutions in collection, sorting, and delivery enabling entry in domestic mail markets.

This development has considerable impact on the business model of the postal operators as it becomes clear that future mail processing will not be a dominant physical process anymore, but will increasingly use machine technology and electronic media in mail processing often combined with physical mail in so called hybrid mail solutions.

In the answers to the questionnaires and the interviews in this study many new entrants distinguish themselves from the traditional business model of the national postal operator in providing tailor-made solutions for larger customers. The benchmarking discussed above is increasingly leading to a Greenfield approach by completely changing the traditional production process.

3.3 Preliminary assessment of contestability of market segments

3.3.1 Introduction: barriers to entry and contestability

Contestable markets are markets in which inefficient firms or firms that earn excess profits are likely to be driven out by more efficient or more price competitive rivals. A market can be contestable even if it is dominated by a single firm. As already mentioned above, the contestability of market segments in fact focuses on one of the forces that according to Porter govern competition in an industry: the risk of competitors entering the industry. This risk depends on the barriers to entry that potential entrants face.

The Directorate-General Competition of the European Commission defines entry barriers as follows:¹⁵

“Barriers to entry are factors which prevent or hinder companies from entering a specific market. Entry barriers may result for instance from a particular market structure (e.g. sunk cost industry, brand loyalty of consumers to existing products) or the behaviour of incumbent firms. It is important to add that governments can also be a source of entry barriers (e.g. through licensing requirements and other regulations).”

In general, and in confirmation with the definition presented above, entry barriers can be subdivided into barriers of a legal, natural and strategic nature. For establishing whether or not certain market segments are contestable, it is in our view important to make a distinction between entry barriers that are related to the economics of postal service provision and barriers that are related to regulation or the behaviour of the national postal operator. The first set of barriers will continue to exist after the complete liberalisation of the postal sector and cannot easily be influenced by government policy, while the second set of barriers can be influenced or be taken away by liberalisation, regulation or decisions by the postal sector regulator or the competition authority.

The contestability of postal market segments will ultimately depend on this first set of barriers, which consist of the *natural barriers to entry*, and possibly on some of the other entry barriers if these cannot effectively be taken away through sector regulation or executing competition policy. In this section we therefore focus our attention to the natural barriers to entry. The prevailing *legal and strategic entry barriers* are discussed in Chapter 4 based on the analysis of the actual development of competition to date.

3.3.2 Which market segments are contestable?

Before we turn to the discussion of natural entry barriers, it is useful to briefly repeat the postal supply chain as well as the several dimensions along which the postal market can be segmented (see Chapter 2).

The postal supply chain includes seven components:

¹⁵ See http://europa.eu.int/comm/competition/general_info/glossary_en.html#top; European Commission, *Glossary of terms used in competition related matters*, 2003.

- Collection from street letter boxes, business premises, post offices or other collection points;
- Transport from collection points to an outward sorting centre;
- Outward sorting of mail;
- Transport between sorting centres;
- Inward sorting of mail;
- Transport to local post office;
- Delivery to service points, P.O. Boxes or addresses (door-to-door).

The dimensions along which the postal market can be segmented are:

- Along postal products (letters, transaction mail, direct mail, etc.);
- Along sender/receiver (B2B, B2C, C2B, C2C);
- Along time sensitivity/predictability (next day delivery, slow mail, yes/not predictable, etc.);
- Along the size of the mail sending (individual items, bulk mail).

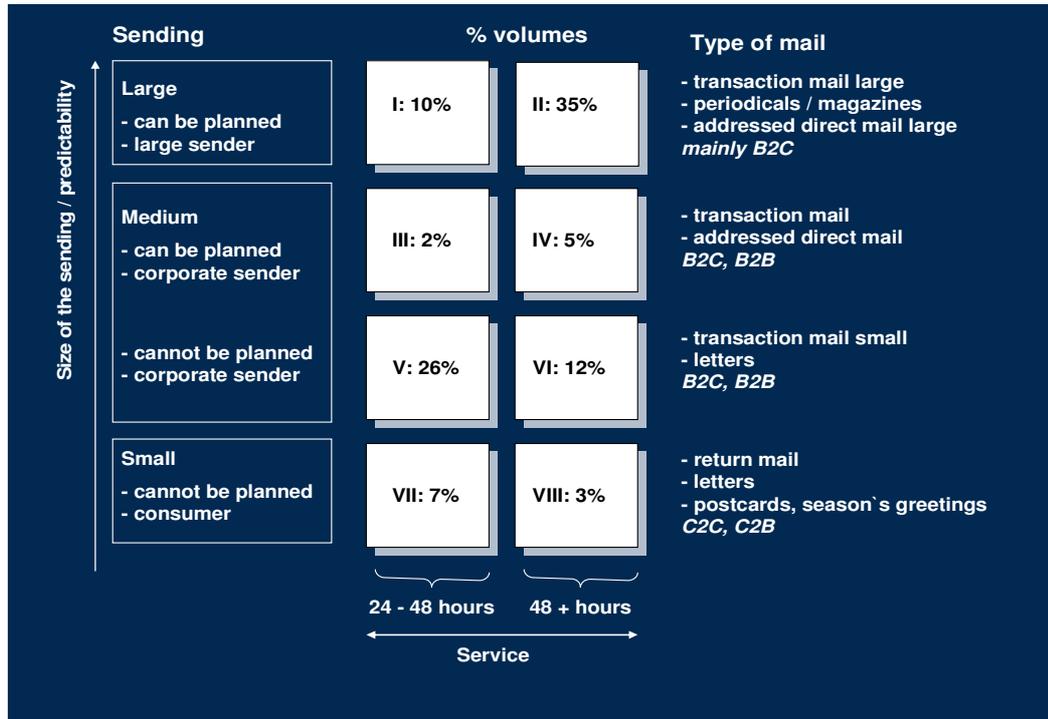
Based on the supply chain and the dimensions identified above, a multi dimensional matrix can be constructed. Entry barriers can be related to each of these cells in such a matrix or to a subset of these cells. Hypothetically, entry can take place in each of these cells. In practice however, a profitable business case can only be developed by entering in a range of cells at the same time. Acknowledging that there are too many dimensions for a visualisation of such a multi-dimensional matrix, Figure 3.3 shows the market segmentation that we use here and further in Chapter 6 to discuss whether market segments are contestable as well as the pattern of expected entry. For illustrative purposes, an estimate of the relative importance of the eight cells for the Netherlands is given in Figure 3.3 as well.

The actual entry barriers are further influenced by the business model that is employed or the type of new entrant:¹⁶

- Technology: production can be relatively labour intensive (e.g., hand sorting) or more capital intensive (e.g., machine sorting, acceptance of pre-sorted mail only);
- The new entrant may outsource part or most of the work and employ a large part of their employees on a flexible basis;
- Entry may be on a national scale or may be local or regional (at first). Consequently, entrants may only serve urban areas, or focus on rural areas;
- Entry may occur by firms with different backgrounds. Foreign national postal operators as well as existing (postal) service providers have experience with postal service provision and may already have some kind of infrastructure at their disposal. Entry can also take place by an entirely new entrant that has to build up its network from scratch;
- The type of products offered may vary from basic services to services of a more “value added” nature;
- The frequency of delivery and collection may differ from what is offered by the national postal operator.

¹⁶ See <http://www.postcomm.gov.uk/Index2.html>, http://www.euroexpress.org/cmr?portal_skin=Printable, see SEO (2003) as well.

Figure 3.3 Potential market segmentation for the analysis of potential entry



Note: The volume percentages refer to the Netherlands and have indicative value only. For Germany, Dielt and Waller (2001) estimate the size of the market for a mass mail provider to be 40-50% of the total addressed mail market. Such a provider focuses on market segments II and IV and targets segments I and III as well. For the UK, Berger (2004) estimates that 55% of the domestic mail items are not time critical (48+). For top 500 customers this percentage is 61%.¹⁷

Source: ECORYS based on IG&H (2003)¹⁸

3.3.3 Natural barriers to entry

Natural barriers to entry can be related to the demand side and to the supply side of an industry. Of the following natural entry barriers that can be identified for the postal sector, the first four refer to the demand side¹⁹ and the others to the supply side:

- Reputation effects;
- Quality or product range requirements (portfolio effects);
- Costs of switching;
- Countervailing power of buyers;
- Sunk costs of investments;
- Economies of scale;
- Economies of density;
- Economies of scope;

¹⁷ *Monitoring developments in the postal market – market survey*, report for Postcomm, Roland Berger Strategy Consultants, April 2004; Helmut M. Dielt and Peter Waller, "Competing with Mr. Postman: business strategies, industry structure and competitive prices in liberalized letter markets", research paper, *University of Paderborn*, version 13 June 2001, p.8.

¹⁸ *Marktontwikkelingen en praktijkcases tonen toegankelijkheid van de Nederlandse postmarkt aan*, IG&H Management Consultants, 2003.

¹⁹ See Section 5.2 for a discussion of the demand side of the postal sector based on the questionnaires and interviews with customers.

- Network effects.

Reputation effects

Reputation effects, if customers prefer to do business with postal operators with an established reputation, can be a formidable hurdle for new entrants to take. Although this entry barrier does in our view play a role in the scale and pattern of the development of competition in the mail market, it is in our view possible for new competitors to overcome these barriers.

Reputation effects are probably stronger for downstream activities (delivery) than for upstream activities (pre-mail activities, mail consolidation), more important for next day delivery than for second class mail, and more important for transaction mail than for addressed direct mail.

Quality or product range requirements (portfolio effects)

Some customers demand next day delivery while others do not. There may also be a demand for value added services such as track and trace and proof of delivery. Also customers may have requirements regarding the product range that postal operators offer. Customers may for instance derive benefits from ‘one stop shopping.’ This may make it difficult for new entrants to enter the market, especially if entrants offer only niche products.²⁰

These requirements do in our view play a role in the scale and pattern of the development of competition in the mail market (see also in Section 5.2 where we elaborate on the considerations of the customers of postal operators), but do not seem to be insurmountable for new competitors. At first sight, portfolio effects appear more relevant for large mailers than for small mailers.

Costs of switching

If customers face positive costs of switching from one to another postal service provider, barriers to entry are higher. In practice, these costs exist but are not prohibiting entry. In particular for small mailers and individual items switching costs are relatively small.

Countervailing power of buyers

Businesses that send high volumes of mail may be able to offer the kind of leeway necessary for a new entrant to actually enter the market. Contracts with only a couple of them may be sufficient to enter the market successfully. This particularly applies for B2X bulk mail that can be computer generated and planned in advance.

Sunk costs of investment

Sunk costs refer to specific investments needed to enter an industry that are essentially lost at the moment that this new entrant would leave the industry. Examples of investments involving substantial sunk costs are the network for fixed telephony or the national railway infrastructure.

²⁰ Incumbents may also offer discounts if a large volume of services is consumed, this may make partial shifting costly.

Are investments of new entrants in the postal sector characterised by substantial sunk costs? It appears that most investments needed to run a full service providing postal operation are reversible, which limits the sunk character of investments significantly. In order to establish a postal operator, investments in a collection network, inward and outward sorting, transport and delivery network are necessary. Sunk costs (irreversible investments) exist in developing a detailed collection network (letter boxes) and in sorting equipment, but these are not prohibiting entry.²¹ A certain level of logistics expertise is required to start postal service provision, but a large number of potential entrants already possess this kind of expertise. Labour, buildings and transport facilities are generally non-specific to the postal sector.

The P.O. Boxes at the post offices probably form an exception to the above. Competitors that do not have access to P.O. Boxes as final points of delivery are in a disadvantageous situation compared to the incumbent that has established that infrastructure.²²

Economies of scale

In this report we make the same distinction between economies of scale and economies of density as in NERA (2004). This distinction is particularly relevant for network industries.²³

Economies of scale in this definition refer to the cost advantages that can be achieved by increasing the network size and the mail volume that is processed through this network at the same rate. The network size in the postal sector typically depends on the number of collection points, sorting offices, transport routes and delivery points.

The results of the study by NERA (2004) based on data of the national postal operators show that there are no economies of scale for end-to-end mail processing in the old Member States, although there seem to be economies of scale in the new Member States (see Box 3.2 for a review of the main outcomes of the econometric analysis presented by NERA).

An important implication of this result is that a competitor postal operator with a (considerably) smaller postal network can enjoy the same cost advantages based on economies of scale as the national postal operator, even at (considerably) lower mail volumes.

²¹ In addition, the choice of a specific business model can reduce the needed investments in collection and sorting equipment considerably.

²² In this case access may be regulated, and, as the infrastructure has been developed by the national postal operator, a fair price may be charged.

²³ It should be noted that the term 'network industry' is often used rather loosely and that there are marked differences between for instance the postal sector and the telecommunications or the energy sector.

Box 3.2 Estimations of cost functions of national postal operators by NERA (2004)

NERA estimated several cost functions for addressed letter mail and parcel mail based on data of the national postal operators of the Member States. Separate estimates were made for the total cost function, the collection cost function, the sorting cost function, the transport cost function, and the delivery cost function. It should be mentioned that the estimation results have to be treated with care, given the difficulties that NERA experienced with collecting accurate and relevant data.

Overall, and not surprisingly, the wage level and mail volumes proved to have a significant positive impact on the (total, not average) cost of postal service provision in the estimates of all cost functions.

In addition, for *total costs*, the number of households (as a proxy for the number of delivery points) has a positive impact on cost, whereas the percentage of the urban population of total population has a negative impact on cost. A quality target for D+1 delivery of above 95% also has a positive impact on cost. The results show that there are no economies of scale: average cost remains the same when both the mail volume and the network size increase, although for the new Member States moderate economies of scale do seem to exist. The estimates show however that there are economies of density both in the old and in the new Member States: "... a ten percent increase in the volume of letters and parcels, given a fixed network size, would increase costs in these countries by 6.5 percent" (NERA 2004, p.124-125).

Also for the *cost of collection*, the percentage of the urban population has a negative impact on cost. The number of collection points, as measured by the number of post (letter) boxes, appeared to have a positive impact on cost. The estimates show economies of density and suggest no economies of scale, except for the new Member States.

The estimates for the *sorting cost function* show that the number of sorting offices has a moderately positive impact on cost: a 10% decrease in the number of sorting offices would lead to a reduction of 2.9% in sorting costs. There appear to be substantial economies in density in sorting and moderate economies of scale that are again higher for the new Member States. According to NERA, the presence of pre-sorting companies further underlines the conclusion that mail processing operations are not characterised by strong economies of scale.

Transport costs are positively influenced by the number of post offices and the surface area of the country. Again, the estimates show economies of density and in this case also economies of scale. The results should be taken with caution, but probably reflect the results of other studies showing economies of scale in short haul transportation and only very small economies of scale in long distance transportation.

Finally, the *cost of delivery* is just like total costs positively affected by the number of households and negatively by the percentage of the urban population. The estimates show substantial economies of density and moderate economies of scale, although the hypothesis of constant returns to scale could not be rejected for the old Member States.

Economies of density

Economies of density are obtained if the average cost of mail handling decreases when mail volumes rise given a fixed size of the network. Economies of density are related to the cost structure underlying the production function of postal operators. The cost structure is related to the total mail volume handled through the network, but also to the geographical conditions of a country. For example, in countries where little mail per capita is sent and vast areas are thinly populated and difficult to approach (because of hills, mountains, lakes or other geographical conditions), delivery costs will be relatively high and economies of density are relatively important.

Economies of density prove to be important in the postal market and apply to the various parts of the supply chain. The NERA study does not make a distinction between postal products or market segments. It appears however, that economies of density are particularly relevant to the C2X segment, given the number of collection points and the economies of density in collection. In the B2B segment, economies of density are probably achieved relatively quickly. In the B2C segment the economies of density are higher, given the number of delivery points and the economies of density in delivery. It should be mentioned however, that the mail volumes that can be achieved in the B2C segment are higher than in the B2B segment, mitigating the relative importance of economies of density a bit.

In addition, there are marked differences between postal products, in particular between individual item mail (that is heterogeneous and needs sorting) and bulk mail that can be computer generated and pre-sorted. For the latter type of mail, there are probably no economies of density for collection and neither for sorting. Table 3.1 summarises the above observations.

Table 3.1 Probable economies of density in various segments

	C2C	C2B	B2C	B2B
	Individual item mail			
Collection	Large	Large	Moderate	Moderate
Sorting	Moderate	Moderate	Moderate	Moderate
Delivery	Large	Moderate	Large	Moderate
	Computer sorted mail			
Collection	Not relevant	Not relevant	None/Small	None/Small
Sorting	Not relevant	Not relevant	None	None
Delivery	Not relevant	Not relevant	Large	Moderate

Source: based on SEO (2003), *Tante Pos krijgt concurrentie – effecten van de liberalisering van de postmarkt*

In general, although economies of density are important for the postal sector, it is not an insurmountable barrier to entry. Further, the discussion above shows that employing business models that are very different from the traditional business model of the national postal operators can mitigate the importance of economies of density.

Having said this, the discussion on economics of scale and density do reveal that a number of market segments show natural monopoly characteristics (see Box 3.3 for a

brief discussion of natural monopoly and its impact on the development of competition). This particularly applies to segments that require a very elaborate network and have relatively large unit costs, such as C2X mail with a D+1 service level (cell VII in Figure 3.3) and the daily collection and delivery to households in rural areas (parts of all other cells in Figure 3.3 and a relatively large part of cell V).

Box 3.3 Natural monopoly

A natural monopoly would exist in the mail market or one of its market segments if the cost function is such that one firm can produce a given output at no greater cost than that incurred by two or more firms whose total productions equal the same given output. If there would be only homogenous products, a natural monopoly would imply that only one firm would supply the whole market. If however there would be product differentiation, competitors can enter the market and gain a certain market share. Further, if the investments that are needed to enter the market do not involve sunk costs of any significance, high (monopoly) prices may induce a competitor to enter the market, make a profit, and leave the market once prices have gone down.

Economies of scope

Economies of scope could be regarded as a particular form of economies of density warranting specific attention. Economies of scope refer to the cost advantages that may be enjoyed if several services or products are provided using the same network infrastructure, such as delivery of both transaction mail and direct mail or the delivery of both addressed mail and un-addressed mail. These economies of scope cannot be reaped by entrants that only provide a single or small number of services and may act as a barrier to entry. However, costs can be shared if it is possible for new entrants to combine their new activities with already existing activities, such as newspaper delivery or sharing collection points.

The analysis in Chapter 5 shows that economies of scope (and herewith economies of density) are particularly important for the products within the addressed mail segment, but less for combining addressed mail and parcel delivery or addressed mail and un-addressed mail, and virtually nonexistent for combining addressed mail and express delivery.

Network effects

Finally, network effects can act as an entry barrier. A product features network effects if additional consumers of the product increase the attractiveness of the product for other consumers. If any, these effects are limited in the postal sector, but would make small scale entry less viable.

3.4 Network access: justification and economic rationale

In many countries there is discussion whether or not access to the facilities of the national postal operator is a prerequisite to the development of competition in the postal market and whether or not there should be *ex ante* regulation to safeguard this access. The latter

point is of importance because access to (certain) facilities of the national operator can also be assured through negotiations, where the competitor postal operator reaches an agreement with the national postal operator on the terms on which the latter provides this access. In this respect it should be noted that for all services under the universal service obligations there is in practice access, albeit access at terms that are equal to other customers and not necessarily at discounted rates compensating for the level of mail preparation that has already taken place by the competitor postal operator. Further, an important point of discussion is about the role that the postal sector regulator should play. Should the regulator actively stimulate that there is access? Should the regulator be involved in the negotiation process? How should it react if the negotiations between the postal operators fail or drag on for a long time?

In short, the discussion concerns the pros and cons of *regulated access* and *negotiated access* and positions are taken on a spectrum varying from mandatory access with ex ante regulation of the access conditions (access points, terms, prices) to freely negotiated access with dispute settlement based on general competition law. A position between these extremes is that access is mandatory, that the conditions for access are negotiated between the market participants and that the postal sector regulator plays a more or less active role in the process and resolves disputes if no agreement can be reached.

This spectrum of possibilities is in fact reflected in practice in the Member States. Germany is the only example of ex ante regulation of the access conditions, with discounts to the retail price varying from 3% to 21%. Further, there are a number of Member States that have mandatory access (such as Slovenia and the United Kingdom) and/or have regulators that are taking their role further than that of a mediator in the negotiation process and are actively solving disputes if access is denied or if no agreement could be reached (see Annex I, appendix 4, for information for the Member States based on the questionnaire responses). It should be stressed, however, that most of these dispute settlements concerned issues like access to the P.O. Boxes and the possibility to return wrongly delivered mail via the national postal operator and not access to the delivery network.

We will discuss a number of empirical examples in Chapter 5 and confine the discussion here to the main arguments in favour and against regulated access, without reviewing the extensive literature on access at great length.²⁴ Moreover, we restrict the discussion to access to the delivery network (the “last mile”) of the national postal operators.

A number of arguments can be given in favour of access to the delivery network of the national postal operator:

1. Access is needed for the development of the upstream market for mail preparation and mail consolidation;
2. Access in fact concerns work sharing. Competition and product development in upstream markets strengthens the mail sector in its battle with the advertising and

²⁴ See for example Annex II, country information sheet Germany; RBB Economics, *Entry barriers in the Dutch postal market – a report for OPTA*, February 2003; T. Walsh, Downstream access to European postal networks, lessons from the UK experience, *CERP Plenary*, Vilnius, Lithuania, 24-25 November 2004; M. Benz, *Briefmarkt auf den den Weg zu mehr Wettbewerb, Win-Win potentiale im postmarkt durch work-sharing*, IBM Business Consulting, Berlin, March 2005; see also the references mentioned in the next footnote.

communication sectors and is good for the generation of mail flows. Combining the last mile delivery provides economies of density for both postal operators and customers, creating a “win-win” situation;

3. National postal operators may not be aware of this “win-win” situation or may act irrationally, calling for access regulation in society’s best interest;
4. The delivery network with national coverage is an essential facility that cannot be duplicated by a (would be) competitor postal operator;
5. The national postal operators enjoy a *first mover advantage* related to the development of their networks under a legal monopoly. Because of the economies of density in delivery and the high mail volumes that are needed to develop a profitable business the needed investments for establishing a delivery network are very high and prohibiting entry;
6. Even if duplication is possible, this is not desirable because less economies of density will be obtained and it may result in underutilisation of existing capacity;
7. Access is needed as “a last resort” to facilitate that competitors that not (yet) have a delivery network with full national coverage can offer attractive business propositions and one stop shopping to their customers.

Not all of these arguments are sufficient justification for regulating access to the delivery network of the national postal operators. In general, there should be very good reasons to regulate access to the facilities of a particular company in any industry. On the one hand, without this access it should be impossible for competition to develop and on the other hand this competition should be of benefit to the final consumer. This latter point is important: the question is not so much whether a competitor should be granted access, but whether the consumer will benefit from regulated access. In this analysis, the short run and the longer run effects should be carefully considered. For example, the immediate short run effect may be beneficial for the consumer but the effect in the longer run may be negative because of the potential negative impact of regulated access on innovation and dynamic efficiency.²⁵

To assess the justification for regulating access, the first question that should be answered is hence whether competition on the addressed mail market can develop without such access. Although some normative answers to this question can be given based on the type of analysis presented in the section on contestability, essentially the empirical evidence is conclusive for answering this question. If it is highly unlikely that competition will develop on the addressed mail market or on certain smaller segments of this market, for assessing the potential longer term benefit of the final consumer from regulated access the next question that should be answered is why competition would be unlikely to develop:

- Are there substantial sunk costs of investment prohibiting entry? If yes, this often justifies access regulation;
- Is the market segment characterised by strong natural monopoly characteristics? This in itself does not justify access regulation;

²⁵ See for example Van Damme and Verboven, ‘Het nieuwe toezicht op ondernemingen: economische aspecten van marktwerking en regulering’ [The new supervision of companies: economic aspects of competition and regulation], *Preadviezen van de Koninklijke Vereniging van de Staathuishoudkunde 2001; Herpositionering van ondernemingen*, p.139-185, and TILEC, *Towards a liberalised postal market*, Tilburg University, 2003, chapter 3.

- Is it because of first mover advantages although the market is not a natural monopoly? This may justify (temporary) access regulation;
- Are other natural entry barriers prohibiting the development of competition? This may justify (temporary) access regulation;
- Are there other barriers to entry that may be taken away by the policy maker, the regulator and/or the competition authority? This calls for action to reduce these other barriers and does not justify access regulation.

From the perspective of competition law, access should only be granted to those facilities that can be considered essential facilities or monopolistic bottlenecks. DG Competition defines essential facility as follows:²⁶

“Facility or infrastructure which is necessary for reaching customers and/or enabling competitors to carry on their business. A facility is essential if its duplication is impossible or extremely difficult due to physical, geographical, legal or economic constraints. Take for example a national electricity power grid used by various electricity producers to reach the final consumers. Since it would not be viable for these producers to build their own delivery network, they depend on access to the existing infrastructure. Denying access to an essential facility may be considered an abuse of a dominant position by the entity controlling it, in particular where it prevents competition in a downstream market.”

The discussion in the previous section on natural entry barriers shows that the facilities of the national postal operators probably do not constitute essential facilities. There are no large sunk costs of investments and the natural entry barriers on the demand side as well as network effects do exist to a smaller or larger extent, but do not seem to prohibit entry.

The key issue that is worth further analysis is the impact of economies of scale, scope and density on the market. In particular for offering (daily) delivery services in (the largest part) of the country, economies of density are large and may be difficult to achieve. It is not unlikely that the (daily) delivery in mountainous or in any other sense remote areas has strong natural monopoly characteristics. The duplication of a delivery network in these areas then may prove unfeasible from an economic point of view: a competitor postal operator cannot develop a profitable business case and will not enter this market segment. What should be analysed in this case is to what extent this situation deprives these customers of the benefits of competition in the upstream market and what should be the most appropriate remedy for this.

We turn to this question and to the other issues raised above after our discussion of the actual development of competition in Chapters 4 and 5.

Although it is not entirely clear whether the issues below do constitute essential facilities, with regard to the postal sector a consensus is developing that access on reasonable terms and against reasonable prices should at least be guaranteed to the following:²⁷

²⁶ See http://europa.eu.int/comm/competition/general_info/glossary_en.html#top; European Commission, *Glossary of terms used in competition related matters*, 2003.

²⁷ Note that a number of the issues listed here refer to the creation of a level playing field, not to access as such (apart from access to the P.O. Boxes and the possibility to return mail). In the new postal law that has recently been approved in France, exactly these four issues are mentioned.

- Access to the P.O. Boxes in postal offices and the letterboxes in apartment buildings (in the big cities of some countries the letterboxes of apartment buildings are not accessible from the public road and many apartments have security codes at the entrance door);
- Access to the postal code system (linking postal codes with exact addresses);
- Access to the information on changes in addresses;
- Possibility to return (forward) mail through the national postal operator.

3.5 Summary and conclusion

Using the five forces model of Porter, we have made a first assessment of the respective forces on the state of competition in the postal sector. In particular the threat of potential substitutes for communication and advertisement and the bargaining power of large customers have a disciplining effect on the behaviour of postal operators. In a fully liberalised market the combination of bargaining power of large customers and potential and actual entry positively influences the level of effective competition on the market. The other factors were merely introduced for the sake of comprehensiveness, as the risk of new competitors entering the industry, the degree of rivalry between existing postal operators and the impact of regulation on the development of competition is discussed at length in the remainder of this report.

The discussion on the contestability of market segments focused on the natural barriers to entry. Obviously, legal and strategic entry barriers also determine whether entry is likely and whether or not markets are contestable in the short term. However, many of these barriers can be removed in the medium term by proper regulation and effective actions by the policy maker, sector regulator or the competition authority. As the natural entry barriers are related to the economics of the postal sector and cannot easily be influenced in this way, we decided to separate the entry barriers discussion in two parts and to deal with legal and strategic entry barriers in the next chapter after having analysed the actual development of competition in the Member States.

A preliminary assessment of the natural entry barriers is presented in Table 3.3.

If we assess the importance of the natural entry barriers on the different market segments that hypothetically can be constructed (relating the dimensions postal products, sender/receiver, time sensitivity/predictability and size of mail sending to the postal supply chain) we arrive at a positioning of market segments on a continuum, ranging from markets to which entry is relatively easy to markets to which entry is unlikely. Some of the latter markets may prove not contestable.

Table 3.3 Summary of natural barriers to entry

Entry barrier	Preliminary assessment
Demand side	
Reputation effects	Exist and influence the pattern of competition. Probably stronger for downstream than for upstream activities but can be overcome.
Quality/portfolio effects	Exist and influence the pattern of competition. More relevant for large mailers than small mailers.
Costs of switching	Exist but are limited. No switching costs for small mailers and individual items.
Countervailing power of buyers	Create opportunities for new entry, in particular for B2X mail that can be computer generated and planned in advance.
Supply side	
Sunk costs of investments	Not in transport and delivery, exist in sorting equipment and collection network, but these depend on the business model chosen.
Economies of scale	Not in the old MS, present in new MS: average costs are stable if the network size and the mail volumes processed through the network increase at the same rate.
Economies of density	Important and apply to all parts of the supply chain.
Economies of scope	Range from very low to high dependent on the combination of products offered through the same network.
Network effects	Limited, may make small scale entry less viable.

Note: MS refers to EU Member State

Entry is most likely on segments that do not require a large fixed network. Network requirements are also less when entry takes place in only parts of the supply chain. For entrants:

- Bulk mail is more attractive than individual item mail;
- Homogenous standardised mail is more attractive than heterogeneous mail;
- Mail that allows own pre-sorting is more attractive than mail requiring sorting;
- Mail that does not need to follow the whole postal supply chain is more attractive than mail that does;
- Value added services are more attractive than services that are standard offered through the network of the national postal operator (product differentiation);
- B2X is more attractive than C2X (collection network, mail volumes);
- Mail that is not time sensitive is more attractive than mail requiring next day delivery;
- Mail volumes that can be planned in advance are more attractive than mail volumes that cannot be planned in advance if these mail volumes are time sensitive;
- P.O. Box delivery and delivery to densely populated areas is more attractive than nation wide coverage (delivery network);
- Delivery a couple of times per week is more attractive than delivery five or six times a week.

To assess the justification for regulating access, the first question that should be answered is whether competition on the addressed mail market can develop without such access. Apart from the normative analysis undertaken in the section on contestability, essentially the empirical evidence is conclusive for answering this question. If it is highly unlikely that competition will develop in the addressed mail market or in certain smaller segments

of this market, for assessing the potential longer term benefit of the final consumer from regulated access the next question that should be answered is why competition would be unlikely to develop.

The discussion on natural entry barriers shows that the facilities of the national postal operators probably do not constitute essential facilities. There are no substantial sunk costs of investments and demand side natural entry barriers as well as network effects do exist to a smaller or larger extent, but do not seem to prohibit entry.

The reasons why competition may not develop are hence related to either the natural monopoly characteristics of (segments of) the postal market (this in itself does not justify access regulation), the existence of strong first mover advantages although the market is not a natural monopoly (this may justify [temporary] access regulation), or other barriers to the development of competition (this may only justify access regulation if this is the only remedy because these barriers cannot be taken away by the policy maker, the regulator and/or the competition authority). The analysis of these essentially empirical issues will be undertaken in the remainder of this report.

4 Development of competition in the EU Member States

4.1 Introduction

This chapter presents an overview of the development of competition in the postal market in the different EU Member States to date. Specific attention to the strategies of competitor postal operators and national postal operators is given in Chapter 5. The purpose of this chapter is twofold. The first purpose is to present an overview of relevant developments to date. The second purpose is to gain insight in the factors that facilitate or hamper the development of competition and herewith, together with the analysis in Chapter 5, paving the ground for a well founded analysis of the likely development of competition after full liberalisation of the mail market – the topic of discussion in Chapter 6 of this study. The analysis presented in Chapters 4 and 5 is based on detailed information that has been gathered for each of the 25 EU Member States. This information has been summarised in 25 country information sheets, included as Annex II to this report.

The discussion below starts in Section 4.2 with an overview of the development of competition in the Member States. In Section 4.3 we summarise the key factors that appear to facilitate or hamper the development of competition. Finally, in Section 4.4 the effects of competition on the postal markets are discussed while Section 4.5 concludes and summarises the main findings.

4.2 Development of competition in the Member States

4.2.1 Overview of the development of competition in the Member States

Table 4.1 presents an overview of the competitor postal operators that are active on the letter mail market in the Member States, with a focus on the market segment for addressed mail. The information in the table further focuses on those operators that have entered into delivery of items of correspondence or addressed direct mail, or have an explicit aim to do so, and hence disregards, for example, publishers that distribute their own magazines. Only the major competitors are mentioned by name, although in some countries there are many small postal operators.

Table 4.1 Overview of main competitors on the addressed mail market segment in the Member States

Country	Competitor	Brief description (business model, turnover)	Market share
Austria	Redmail (TNT) Feibra (Austria Post)	27 mln items of addressed mail (items of correspondence, printed matter, newspapers), turnover 55 mln euro Un-addressed market shares: Austria Post 80%, its subsidiary Feibra 18%, Redmail 2%	1.6%
Belgium	BD Various small	Several local distributors in local addressed mail; some in catalogues/magazines; Ciblex, BD addressed mail; DHL, Spring cross border mail Un-addressed market shares: Belgische Distributiedienst (BD) 81%, the remainder for La Poste / De Post and Deltamedia (La Poste / De Post)	<2%
Cyprus	None	No active competitors in addressed mail, distributor of newspapers and magazines to retail outlets is active Un-addressed mail delivered by small local companies, market share USP is high	0%
Czech Rep.	Mediaservis Agentura Pro Distribuci a Marketing, s.r.o. (ADM) (TNT)	30 mln items of addressed mail (magazines and direct mail), turnover 25 mln euro; also active in un-addressed mail, dominant operator in delivery of newspapers (147 mln items) Largest operator in un-addressed mail delivery, owned by TNT, with 6,000 deliverers active in large part of country (2.8 mln households), also active in upstream activities Un-addressed market share of USP is 58%.	4.5%
Denmark	Bladkompagnet Forbrugerkontakt	100 mln magazines, 135 employees, 6,000/7,000 deliverers through 35 subcontractors, 7 times a week delivery to 300,000 households Delivery of un-addressed items, entire Denmark, two times a week, market share of USP between 50-60%	3-5%
Estonia	AS Express Post OÜ Kirilind	4.5 mln items of addressed mail, 9 mln items of un-addressed mail; turnover 2.4 mln euro 2 mln items of addressed mail (rough estimate)	5-6%
Finland	Local newspaper delivery organisations Suomen Suoramainonta Oy Letterbox Distribution Finland Oy	Local newspaper delivery organisations in total deliver a large part of total newspapers delivered Un-addressed mail, 450 million (volume), 7,000 deliverers, 2 deliveries a week, nationwide service, applied for a licence to provide addressed mail delivery but never entered due to licence conditions. Around 200 million, 5,000 deliverers, delivery once a week, almost nationwide delivery due to subcontractors Un-addressed mail market share of USP is between 40 and 50%	0.5-1% (newsp. Excl.)
France	Adrexo	7.5 bln items un-addressed mail (catalogues, magazines); 25 mln items of addressed mail, turnover of circa 200 million euro, 26.000	<2%

Country	Competitor	Brief description (business model, turnover)	Market share
	Various	employees, 220 distribution centres; delivery at least three times per week in urban areas and one-two times per week in rural areas; strong position in un-addressed and parcels Many companies active in upstream activities (mail consolidation), including subsidiaries of La Poste and DPWN (KOBAs, recent takeover)	
Germany	PIN AG EP Europost (TNT) Various city mail operators, regional publishers, such as WAZ , with network and DPS	140-170 mln items of addressed mail, turnover 35 mln euro, 1000 employees, 3 distribution centres, delivery of addressed items in three German cities (Berlin, Köln and Leipzig) items of addressed mail unknown, turnover consolidated in TNT figures, active in B2C distribution, say to be say in entire Germany, coverage 75%, delivery via distribution network of publishers, use of network of 150 city mail operators, and Hermes network Entry in postal market mainly local or regional, co-delivery via publishers network	4%
Greece	DeltaPost	Leading deliverer of un-addressed mail, 3.5 mln households covered, 170 mln items delivered annually No active competitors in addressed mail with exception of couriers and express operators offering a substitutable service, distributors of newspapers are active on local scale	0-0,5%
Hungary	Dimar, Student organisations	Courier and express operators are main competitors In distribution of un-addressed items, Dimar and student organisation's deliver un-addressed mail, market share USP between 20 and 30%	0%
Ireland	Leaflet company Ireland	No operators active in addressed mail apart from international consolidators for international mail Many companies active in upstream activities, Leaflet Company leading distributor of un-addressed mail, USP market share around 50% (rough estimate)	0%
Italy	Rinaldi Espresso (TNT) Romana Recapiti	Several small operators active in direct mail, items of correspondence above 100 gr. and un-addressed mail in the main cities and local villages, Rinaldi is a large company, owned by TNT, and active in Milano and Roma. Romana Recapiti is a similar operator, but smaller. No existence of integrated service of city operators	1-2%
Latvia	Reklamas Pasts	Only publishers possessing a delivery network for the delivery of their magazines exists, such as Reklamas Pasts, Rautakirja and Preses Serviss. Distribution mostly to sales outlets, part to letterboxes. Reklamas Pasts delivers un-addressed mail	<1%

Country	Competitor	Brief description (business model, turnover)	Market share
Lithuania	None	No active competitors in addressed mail, international consolidators active and most important competitors, press distributor UAB Impress Teva active in delivery to sales points In un-addressed mail around 28 small operators active	0%
Luxemburg	Dintec Lux	Active in all liberalised services in Luxemburg, only competitor active besides couriers, turnover 2 mln euro, over 3 mln items In un-addressed mail single competitor operator is Lux, market shares of USP over 90%	1-2%
Malta	None	No (large) active competitors in addressed nor in un-addressed mail, small local companies active in distribution of un-addressed mail	0%
Netherlands	Sandd Selekt Mail (DPWN) Various	130 mln items of addressed mail annually (magazines, periodicals, direct mail), growing fast; turnover 32 mln euro (2004), 650 employees (excl. delivery), 6500 deliverers, 90 distribution centres, 100% nationwide coverage, 2-3 delivery rounds/ week; delivery of pre-sorted bulk mail handed over by large customers Ca. 100 mln items of addressed mail annually (magazines, direct mail), growing fast; turnover ? mln euro, 5000 deliverers, 120 distribution centres, distribution of addressed mail with a minimum volume of 5000 items, 100% nationwide coverage, 2 delivery rounds/ week MailMerge and Royal Mail deliver printed matter to P.O. Boxes, Royal Mail inbound UK; city delivery services, Swiss Post (intern. mail)	5%
Poland	None	Very small operators active in Warsaw and regions, un-addressed items	0%
Portugal	Noticias Direct S.D.I.M.	Distribution of books, catalogues, newspapers and periodicals Distribution of books, catalogues, newspapers and periodicals In un-addressed mail, various small local operators and six larger are active, market share USP is around 45%	<1%
Slovakia.	Schiculka & Macatch (TNT), Surema, Studentsky servis	No operators active in the distribution of addressed mail, except for courier and express operators Un-addressed mail is offered by a few large operators, i.e. Schiculka & Macatch (TNT), Surema, Studentsky servis, the market share of the UPS in un-addressed mail is claimed to be low	0%
Slovenia	None	No operators active in the distribution of addressed mail, only express and courier operators (to our knowledge) Un-addressed mail not clear but not offered by large national providers	0%
Spain	Unipost (DPWN) Several local operators	Network of 12 private operators active in intra-city letter mail, magazines, direct mail, collaboration with other local operators, 500 million items claimed currently, alternative local operators have less than 200 million items combined Un-addressed mail competition mainly local, market share unknown	7-11%
Sweden	CityMail	216 mln items of addressed mail annually (letters, magazines, periodicals, direct mail, outbound cross-border) in 2003, active in urban	7%

Country	Competitor	Brief description (business model, turnover)	Market share
	SDR, S Post	areas of Sweden, 1100 employees, a number of local newspaper delivery organisations are active Un-addressed mail delivered by SDR and S Post, market share of USP is 64%	
UK	UK Mail, Speedmail (DPWN), TNT, DX, Express Ltd.	Around 10 competitors active in addressed mail, very small combined market share in delivery of addressed mail; agreement on access conditions reached early 2004: UK Mail, Speedmail and TNT focus on collection and pre-sorting of bulk mail of business customers for final sorting and delivery by Royal Mail, substantial and growing volume of (upstream) mail volumes handled by these competitors	<1%

Source: see Annex II (country information sheets) for detailed references.

Notes: This overview does not include courier and express delivery and neither newspaper delivery. Market share refers to the estimated (approximate) total combined market share of competitor postal operators in addressed mail delivery (measured in no. of items delivered). The market shares concern the total addressed mail market, including both the reserved and the non-reserved areas. Competitor postal operators that have gained substantial volumes in addressed mail delivery are indicated in bold. Turnover data are annual figures. The market share figures for the total addressed mail market and the estimated market shares on the liberalised market segment only, are graphically represented in Annex I, appendix 8.

From Table 4.1 it can be observed that competition between postal operators in addressed mail still is very limited and that all national postal operators have maintained a market share above 90% in addressed mail delivery. It can also be seen that some national postal operators have lost considerable market share in the delivery of un-addressed mail.²⁸

The countries that have liberalised a relatively large part of the addressed mail segment show the highest market share for competitor postal operators: this market share is around 7-11% for Spain, 5-7% for Czech Republic, Estonia, the Netherlands, and Sweden, and 3-5% for Denmark and Germany.

The United Kingdom and France have a somewhat special position with regard to the development of competition. France has maintained a relatively large part of addressed mail delivery in the reserved area and in general has been rather slow in implementing the European directives. Only recently, a new postal law has been adopted establishing (amongst others) an independent postal regulator that will come into force by the end of 2005. However, the upstream market has been liberalised a long time ago and mail consolidation has developed rather strongly, with mail consolidators and large customers having three points of upstream and downstream access for final delivery by La Poste. The estimated market size of mail consolidation in 1998 was around 5 billion euro. At that time the 22 largest consolidators had a combined market share of about 55%.²⁹

In the United Kingdom the delivery of bulk mail has been liberalised in 2000 and in the beginning of 2004, after a period of negotiations, an access agreement was reached between Royal Mail and three competitor postal operators. Although the volume of mail handled by these competitors has grown considerably during the last year, the final delivery is undertaken by Royal Mail. Hence, the market share of competitor postal operators in the delivery of addressed mail has remained very small.³⁰ Some information on one of these competitors, UK Mail, is given in Box 4.1.

In the other countries there to date no competitor postal operators have emerged that are challenging the position of the national postal operator. To a large extent this is related to the relatively large reserved area that has been maintained in these countries. For example, Poland has opted for a transitional regime under which all addressed mail <350 grams falls under the reserved area. Likewise, Cyprus and Malta for which cross border mail is relatively important have kept the largest part of this segment in the reserved area.³¹

²⁸ Also in parcel delivery the national postal operators have lost considerable market share. The same is true for the express industry that in the last two decades developed into a separate industry with a high level of competition among market players.

²⁹ See Annex II, country information sheet France. We have no more recent figures on the size of the mail consolidation market.

³⁰ In Chapter 5 the developments in a number of countries that have *de facto* network access are further discussed.

³¹ See Chapter 2 for a discussion of the reserved areas in the Member States.

Box 4.1 Example of a competitor postal operator: UK Mail

Since the UK Postal Service Act in 2000, combined mailings over 4.000 items are open to competition and have given opportunities to new entrants in the postal market such as UK Mail and Speedmail. The parent company of UK Mail, Business Post, was established in 1971. Currently, Business Post has an estimated 7% share of the premium express delivery market, making it the fourth largest operator in the sector. Over 90% of its UK parcel business is for next day delivery and around 90% is business-to-business. Its subsidiary UK Mail was one of the first companies to be licensed by the Postal Services Commission to provide business mail services throughout the UK. UK Mail offers a nationwide two day mail delivery service, operating in both the business-to-consumer and business-to-business markets. Features of the service are track-and-trace up to the point of hand-over to Royal Mail for final mile delivery and flexibility of collection for large mailers. UK Mail commenced trading in May 2004, and has moved over 23 million items in the first half a year, securing customers in the telecoms, utilities, government and retail sectors. Market penetration has been achieved at a faster rate than expected and in March 2005 UK Mail was already handling 250 million items (on an annualised basis),³² with an expectation to become profitable during the second half of the current financial year (2005). In March 2005, UK Mail has obtained a contract to provide upstream mail services to The Royal Bank of Scotland group, one of the UK's largest mailers. Upstream mail services comprise the collection and national distribution of mail (with associated management information and IT) for next day delivery to Royal Mail for local sorting and final delivery. The agreement with Royal Bank of Scotland has been concluded between both UK Mail and Royal Mail.

4.2.2 Some country examples

In this section some examples are discussed to show how competition developed in a number of countries that have liberalised their postal markets to a relatively large extent.

A review of these developments is relevant as it can provide valuable insight in what can be expected to happen in countries that have reserved a relatively large area of the addressed mail market to the national postal operator until date. First, we discuss the developments in three countries that have fully liberalised the mail market. We briefly touch upon the developments in Estonia and Finland and describe the developments in Sweden that like Finland officially abolished the postal monopoly and reserved area already in 1993. Further, we turn to the development of competition in the Netherlands and finally discuss the developments in Spain.

Estonia and Finland

Estonia and Finland liberalised their mail markets per 1 January 2002 and 1 January 1993, respectively. In both countries, an important requirement for potential entrants to obtain a license for the provision of postal services is that the postal services should be provided in the whole territory of the country, with the exception of the Åland islands in Finland.³³ In Finland, there is also the possibility to obtain a restricted license, but new

³² *Promoting competition and higher quality service*, IEA presentation, Nigel Stapleton, March 2005.

³³ In fact, the Åland islands and the rest of Finland are treated as two distinct territories; Posten på Åland is a licensed universal service provider operating only in the Åland islands.

entrants with such a license are charged with an additional turnover tax of 5-20%, depending on the territorial coverage of mail delivery.

In Finland, there are no competitor postal operators that have obtained a license for the provision of services in the universal services area. As a result, Finland Post still enjoys a de facto monopoly position in the largest part of the addressed mail market. A number of consolidators are active in handling inbound cross border mail and the large express operators (DHL, FedEx, TNT, UPS) are active in outbound cross border mail, but the impact on competition in the addressed mail market is limited. Further, three nation wide distributors having around 70 local distributors are active in the delivery of un-addressed mail.

Also in Estonia potential entrants did not show interest to provide postal services in the universal services area under the given conditions for licensing. With regard to the delivery of direct mail there existed uncertainties concerning the licence requirements. These uncertainties were taken away when, during the course of 2002, the Estonian National Communications Board reached a decision that the delivery of this type of mail should be provided without (the above mentioned licensing) limitations. Apart from the national postal operator Eesti Post, two competitor postal companies (AS Express Post and OÜ Kirilind) have been registered and have acquired a small but significant market share in addressed advertising mail (direct mail, also catalogues and magazines, see Table 4.1) combined with a somewhat larger market share in un-addressed mail. In addition, around 20 competitor postal operators are active in the provision of courier services.

Sweden

In Sweden there are no restrictive license requirements for entering into delivery of addressed mail and no license requirements at all for the delivery of catalogues, magazines and un-addressed mail. More than ten years after the complete liberalisation of the addressed mail market the national postal operator, Posten AB, still maintains a very dominant position in the letter mail market. In the delivery of addressed mail, the market share of Posten AB in 2003 was 92.9%, with CityMail having a market share of 6.6% and 26 other active competitor postal operators sharing the remaining 0.5%.³⁴ Moreover, Posten AB has a market share of 64% in un-addressed mail, followed by Svensk Direktreklam (SDR) with 30%, S-Post with 5% and a number of small local distribution companies and sports associations with the remaining 1%. In Box 4.2 some information on CityMail is presented and for more detailed information the reader is referred to the country information sheet for Sweden in Annex II to this report.

Although the combined market shares of the competitor postal operators have remained fairly modest and none of the competitor postal operators in the addressed mail segment have national delivery coverage or have the ambition to develop this, a recent study assessed the results of the liberalisation rather favourably.³⁵ The positive results mentioned are the adaptation of products and services to demand, the fact that prices

³⁴ See also Table 4.1. The information on Sweden in this section is largely based on the study "Postmarknad i förändring" on the developments of competition in the postal market in Sweden, conducted on behalf of the Swedish government and the Swedish postal regulator that was published in January 2005.

³⁵ See previous footnote.

better reflect costs and a favourable price development on the sub-market deliveries. The latter in particular reflects pre-sorted or bulk mail delivery of economy letters, first-class letters, addressed advertising mail and addressed magazines. A rough estimate is that, from the early 1990s to the early 2000s, prices for sending a 50 gram letter in this category went down 30% in nominal terms and 50% in real terms. For individual letters the price for the overnight delivery of a 20 gram letter went up by 50% (and by 90% including VAT) from 1993 to 2003.

Box 4.2 Example of a competitor postal operator: CityMail (Sweden)

After having faced many difficulties and a number of (almost) bankruptcies since its set up in 1991, CityMail has emerged as the main competitor of the national postal operator Posten AB and has acquired a market share of 6.6% in 2003 in the addressed mail market segment. In 2004 the market share increased to 7.5%. CityMail delivers mail in Stockholm, Gothenburg, the Malmö region and the island of Gotland covering 40% of the Swedish households. The company currently employs just over 1,000 persons, and handles almost 200 million postal items per year. The company is showing positive financial results since 2001.

The company's business concept is to distribute, with great accuracy, large volumes of pre-sorted mail at low cost. The business model is based on offering tailor-made solutions for optimal administrative solutions of the postal flows of their customers, without having to use a fixed infrastructure as Sweden Post. CityMail outsourced part of the activities to sub-contractors, while maintaining the overview over the supply-chain. The company has no ambition to build such an infrastructure. Traditionally mail was sorted manually or by machine, but CityMail introduced electronic sorting on postal code, while it is preparing for electronic sorting on type of distribution channel in the future, in this way contributing to value added services and decrease of costs for its customers. The main postal products that it delivers are administrative mail, addressed advertising mail and newspapers and magazines.

The main problems that CityMail faced in the 1990s appear to have been the absence of a clear regulatory framework in the early 1990s and the disputes on access to address change notifications, mail redirection and the P.O. Boxes that were all ultimately resolved in 1999.

Initially established as a private company in 1991, CityMail was taken over by Posten AB to avoid bankruptcy in 1995. The take over was supported as a temporary solution by the regulatory body and approved by the competition authority in an attempt to preserve the developing competition on the liberalised Swedish postal market. After partial ownership (11% in 1998) and later on a rather unsuccessful joint venture with Royal Mail from end 1999, CityMail is since 2002 owned by Norway Post (57%), Bror Anders Månsson (the founder of CityMail, 29%) and OptiMail (the successor of the holding company of CityMail, City Mail Group, 14%). It is foreseen that Norway Post acquires a 100% share in the first quarter of 2006.

CityMail's financial data are consolidated in the figures of OptiMail. The net turnover of OptiMail has grown from just over 100 million Swedish kronor in 1996 to 428.8 million SEK in 2004, reflected in a rise in market share in addressed mail from 1.5% to 6.6% by CityMail in the same period. Turnover figures show that a sharp rise in 1996-1999 was followed by a steep decline from 374.1 million SEK in 1999 to only 170.2 in 2001, probably reflecting that the joint venture with Royal Mail was not very successful, but also that turnover has grown considerably over the last three years.

In addition, the requirements of the universal postal service have been fulfilled during this period without a noticeable detriment to Posten AB. On the contrary, the nation wide coverage of Posten AB and the ability to deliver a high percentage of mail the next day, means that Posten AB can offer business solutions to a wide variety of customers. Further, the liberalisation and emerging competition on the Swedish postal market are generally believed to have had a positive effect on customer orientation and cost efficiency of Posten AB.

The developments in Sweden seem to suggest that there are a number of reasons for the slow development of competition in addressed mail delivery in Sweden. First, the legislation in the postal sector was initially not adapted to support or create the preconditions for competition. Second, during certain periods the apparent internal problems of CityMail have made it difficult for this main competitor of Posten AB to develop its business in the best possible way. This view is supported by the growth of the market share of CityMail since these apparent problems have been overcome. It should be noted that this growth in market share was realised in a generally shrinking market: during the period 1996-2003 the total number of addressed mail items delivered went down by 4.4%. Third, the barriers to develop a nation wide delivery network in a large country with a low population density like Sweden are relatively high and may not provide the preconditions for developing a successful business case for new entrants, in particular when the national postal operator works efficiently, which Posten AB seems to do.

The Netherlands

Table 4.2 presents an overview of competitor postal operators that are active on the Dutch market. Together they have a market share of around 5% of the delivery of addressed mail, equalling a market share of about 10% of the liberalised part of the addressed mail market. Given the relatively short period that has elapsed after the previous liberalisation step and the generally considered well performing national postal operator TNT (in terms of cost efficiency and quality of service), this is an achievement that should not be disregarded easily. More information on the business models that a number of these competitor postal operators have chosen is presented in Chapter 5.

The two competitor postal operators mentioned by name in Table 4.1, Sandd and Selekt Mail, have developed delivery networks to the letterboxes with national coverage. MailMerge and BusinessPost have developed delivery networks focusing on P.O. Box locations, with more than 90% coverage. Selekt Mail is a joint venture of DPWN (51%) and Wegener (49%), a Dutch publisher. The other companies have been set up by former employees of TNT and private investors.

Table 4.2 Overview of competitor postal operators active on the Dutch market

Postal operator	Products	Service level	Coverage
Sandd	Items of correspondence, addressed direct mail, periodicals, sponsored magazines	2 times a week, 48-72 hours	100%
Selekt Mail Nederland (Wegener, DPWN)			
City mail services		2 times a week	Local
Swiss Post International, Spring, De Post, DHL	International		
Royal Mail	Inbound UK, addressed direct mail		30-40%: cities in western Netherlands (<i>Randstad</i>)
Media Express (TNT)	Periodicals, magazines		100%
Audax/Betapress			
PCM Distributie	Newspapers	6 times a week	100%
Wegener, GBB de Nieuwsbrengrers			
DPD (La Poste, France)	Parcels	All	100%
Selektvracht DPWN	Parcels	All	100%
Intermediaries P.O. Boxes			
MailMerge	Un-addressed, printed matter	2 times a week	92% of P.O. Box locations
Royal Mail	Un-addressed, printed matter, parcels, delivery by BusinessPost	5 times a week	65% of P.O. Box locations
BusinessPost		(at least) 2 times a week	95% of P.O. Box locations
Upstream activities			
Mailing houses such as Mailland, Euromail	Addressed printed matter		
Un-addressed mail delivery			
Netwerk VSP (TNT)	Ca. 3.0-4.0 billion items	3 times a week	100%
Interlanden Spreigroep (DPWN, Wegener)	Ca. 4.0 billion items	3 times a week	100%
DistriQ	Ca. 400-500 million items of periodicals/magazines, newspapers, un-addressed	7 times a week	100%

Source: ECORYS (2005) based on Annual reports and presentations TNT, OPTA Annual Reports, SEO (2004), IG&H Management Consultants (2003)

An interesting development is that several of the competitor postal operators have entered into partnerships and negotiated access agreements, for example:

- Selekt Mail cooperates with MailMerge for the delivery of addressed mail to P.O. Boxes and with DPWN for its international mail. In return, Selekt Mail is delivering addressed letterbox mail for MailMerge;
- Royal Mail cooperates with BusinessPost for the delivery of addressed mail to P.O. Boxes and with TNT for the delivery of letterbox mail not covered by their delivery network. BusinessPost uses TNT and Royal Mail for the letterbox deliveries.

Sandd and Selekt Mail have the ambition to offer services that are currently under the reserved area and express the confidence that they can capture 20% of the Dutch addressed mail market within five years time.

In response to the increasing competition on the Dutch postal market, TNT recently announced that it is likely to expand the activities of its secondary delivery network operated by Netwerk VSP. In future, in addition to un-addressed mail, also addressed bulk mail may be delivered through this network against prices that are potentially 30% lower than those offered by TNT at the moment.³⁶

Spain

As described in Chapter 2, the regulatory framework in Spain diverges in several ways from the framework in other Member States. Most importantly, the delivery of domestic intra-city letter mail is not part of the reserved area and in addition the delivery of direct mail has been liberalised. There are no specific access regulations in Spain.

For competitor postal companies, a specific or a general authorisation is required to perform postal activities. The conditions for the specific authorisations are strictest, as these refer to activities that are carried out within the universal services area. General authorisations are essentially not more than mere registrations. At the end of 2004 444 specific and 2,682 general authorisations had been approved.

No changes are currently underway in the postal sector policy regarding future liberalisation of the postal markets other than already laid down in the EU postal directives with possible complete liberalisation of the postal market in 2009.

A large number of authorisations have been given to competitor postal operators. These competitors are mainly active in intra-city mail, direct mail, parcel delivery, logistics and express. The emergence of competitor postal operators delivering intra-city mail and the relatively large express and courier market in Spain is generally considered to be related to the relatively low service and quality level that the national postal operator, Correos y Telégrafos (in short Correos), was able to offer in practice. This performance has improved over the last years as a result of large investments in the infrastructure of the network and a further automation of the logistic process.

At present, the main competitor of Correos in the addressed mail market segment is Unipost. Unipost unites 12 of the main private postal operators in Spain and records an annual turnover of 500 million letter mail items and a delivery network covering 70% of the Spanish population. It is the ambition of Unipost to reach 100% nation wide delivery coverage by 2009 (see Box 4.3 for additional information on Unipost).

³⁶ Reuters, 30 May 2005.

Box 4.3 Example of a competitor postal operator: Unipost (Spain)

The main competitor of the national postal operator in Spain (Correos) is the postal service group Unipost, comprising a network of 12 of the main private postal operators in Spain. Unipost is focusing on intra-city mail, addressed mail >100 grams and advertising mail and is serving almost 15,000 companies and other clients. It is currently handling over 500 million letter mail items annually. With regard to intra-city mail, 95% of the mail is delivered D+1 and 100% within 48 hours. The quality of service offer for inter-city mail for D+1, D+2, D+3 and D+4 respectively is 70%, 90%, 97% and 100%.

Unipost operates three logistic platforms, 46 production sites and 200 service outlets across Spain and has 4,000 own staff and another 2,000 employees of independent partner companies. Delivery is made in more than 1.100 municipalities and/or business areas within cities, covering about 70% of the Spanish population. The aim is to increase the coverage of the delivery network to 80% in 2005 and to 100% of the Spanish population in 2009. Revenues are approaching € 100 million in 2005 after € 87 million in 2003 and € 73 million in 2002. In September 2004 DPWN expanded in the Spanish mail market through the acquisition of a stake of 38% in Unipost. In general, the ambition of Unipost is to establish itself as the second largest postal operator in Spain.

4.3 Factors that influence the development of effective competition

A first set of factors that influence the development of effective competition in the postal market is related to the existence of entry barriers to (would be) competitors and a second set to the circumstances under which competitors in the postal market operate. The latter refers to the existence of a playing field that is level to all operators.

In Chapter 3 we discussed the Porter model and the natural barriers to entry, in this section we present the observations for the Member States with regard to existing legal entry barriers and strategic entry barriers, before discussing the level playing field.

The discussion below is based on the information of the country information sheets, incorporating the interviews held with competitor postal operators and their responses to the questionnaires (13 competitor postal operators from nine countries contributed actively to the study).

4.3.1 Legal barriers to entry

Reserved area

The main legal barrier to entry to date is the fact that in most countries the provision of a substantial set of services is reserved to the universal service provider, the national postal operator. As the overview in Chapter 2 showed this mainly concerns the delivery of items of correspondence and addressed printed matter below 100 grams and three times the basic tariff, but in some cases also concerns more specific products, like the delivery of registered mail.

An important barrier to the development of competition is that, given the respective definition of the reserved area, competitor postal operators are hampered in their ability to

offer a comprehensive business solution to their customers.³⁷ This means that, even in the liberalised mail segments, it is difficult to gain market share. In Member States where the liberalisation of the postal market is confined to addressed mail above 100 grams, in fact only competition in niche markets is possible.

In the UK, the liberalisation of bulk mail consignments of more than 4,000 items in fact does not facilitate competitors to offer comprehensive business solutions as well. First, 94% of all mailings do have less than 4,000 items. Small and medium sized companies rarely send mailings of over 4,000 mail items and even for relatively large customers (with an annual spending of up to 500,000 GBP) these mailings only constitute 3% of their mailings.³⁸ For the largest, top 500, customers, mailings above 4,000 constitute 35% of their mailings, leaving 65% of their mailings that anyhow cannot be handled by a competitor postal operator. Second, batch sizes below 500 items per mailing are predominantly B2B (68%), whereas batch sizes above 4,000 items per mailing are predominantly B2C (81%). This means that a business model focusing on firstly establishing a position on the B2B market segment is practically impossible and that the business model should focus on the B2C segment with nation wide delivery although the liberalised market segment only covers around one third of the addressed mail volumes.³⁹ Based on the above, Berger (2004, p.38, see footnote 33) concludes that:

“Taking these facts into account, a strategic misfit exists between the opened market segment with its specific customers demands for nationwide service (B2C) and the services and products new entrants are able to offer today.”

The full liberalisation of the delivery of addressed direct mail offers much better opportunities for new entrants to offer a comprehensive business solution for their prospective clients, as witnessed by the fact that competition is taking off in particular in the countries that have liberalised this market segment (such as in the Netherlands and in Spain and more recently in Czech Republic and in Estonia). The indication that companies more easily give their direct mail to a new entrant than their other types of mail is a further explanation of the importance of liberalising this market segment for the development of competition. In the study by Berger (2004, p. 93) for the UK, on the question “Which area(s) of your business is/are very likely to be given to a new market entrant?” 62% of the respondents answered direct mail. Other types of mail were answered less often, varying from individual mail (35%), other bulk mail (24%) and international mail (18%) to internal mail (14%, several answers were possible).

Regulatory uncertainty

Although the anticipated gradual liberalisation of the mail market will remove these legal entry barriers, any uncertainty regarding the timing and exact conditions for the liberalisation and remaining regulation acts as a barrier to the development of competition, at least in the short run. In the words of one of the interviewed competitor postal operators: “no sound company can make investment decisions on the type of

³⁷ The considerations of the customers of postal operators are analysed in Section 5.2.

³⁸ See Chapter 3, footnote 17, for a full reference.

³⁹ Based on the data of 549 customers of different size, Berger (2004), p.39, estimates that mailings >4,000 items constitute 36.9% of the mail volume of all mailings.

investments needed for preparing for bulk mail delivery as long as the regulatory environment is unclear and the requirements to obtain a licence for the delivery of bulk mail are not yet determined.”

Another barrier to the development of competition is the regulatory uncertainty with regard to the exact definition of postal products and their inclusion in the reserved area that currently exist in a number of Member States. This has often caused disputes in the Member States.

Licence requirements

Another *de facto* legal entry barrier are the requirements for obtaining a licence for the delivery of mail, which may hamper the development of competition on the market (see Annex I, appendix 3, for detailed information on the postal products for which a license or authorisation is required in the EU Member States). The most restrictive requirements are related to the minimum number of times per week that delivery should take place and the required national coverage of the delivery network, as these requirements eliminate a number of the most prospective business models that new entrants would like to use (for example two times per week delivery of computer sorted mail in part of the country and potentially expanding the delivery coverage over time).

The licence requirements in Estonia and Finland stipulate that for obtaining a licence, operators must provide all services under the universal service obligations. In these two cases, one can speak of cosmetic liberalisation as the reserved area is replaced by another barrier that in effect safeguards the dominant position of the national postal operator.⁴⁰ The additional turnover tax of 5-20% that is charged to competitor postal operators with a restricted license for delivery in only part of the country has raised the barriers to entry as well.

The Netherlands is one of the few countries where no license or authorisation is required for the delivery of mail outside the reserved area. The general understanding underlying this choice is that the general legislation with regard to sound entrepreneurship is regarded a sufficient quality requirement for (new) postal operators.

Access to the P.O. Boxes

An important barrier to the development of competition is the granting of downstream access to the P.O. Boxes of the national postal operators as well as the practical problems with the actual access hereafter. Access to the P.O. Boxes had to be fought for by the competitor postal operators in for example Germany and the Netherlands, where it was ultimately regulated in 2001. Also in Sweden the development of CityMail was hampered eventually because access to the P.O. Boxes was not taken care of. Access prices then gave rise to disputes that were settled satisfactorily later on (in Germany through a decision of the Ruling Chamber, in the Netherlands through negotiations by TNT and the competitor postal operators).

⁴⁰ In Estonia, the decision in 2002 that the delivery of addressed printed matter does not have to meet these requirements has led to competition in the addressed printed matter segment, showing the impact of licence requirements on the development of competition as well.

4.3.2 Strategic barriers to entry

The national postal operators can employ a number of strategies to raise the entry barriers for new entrants. These strategies can be related to their pricing policies and to other actions that are not related to their pricing policies. The discussion below shows that the latter type of strategies most of all have created entry barriers in the postal markets of some Member States until date.

Cross subsidisation and predatory pricing

The national postal operator may use its pricing strategy to prevent the entry of competitors into specific segments or the postal market at large. If the incumbent has ‘deep pockets’, or is able to cross-subsidise across different activities such a strategy may (temporarily) prevent entry of new players into the market. The ability to do so is related to tariff regulation and the requirements with regard to separation of accounts, as further explained in Box 4.4.

Box 4.4 Tariff regulation and separate accounts

The tariffs of postal products are regulated on the basis of cost-based or incentive based regulatory methods. Both methods can be implemented differently in practice. Of importance is the fact if the universal service provider is allowed to make a large profit on the universal service or is able to allocate a large cost base to the reserved area. If the universal service provider earns a lot of profit on the reserved service it can use these profits to deter new entrants in market segments that have been liberalised. If the costs of postal service provision are divided between the reserved and non reserved services in a disproportional way, the universal service provider has a cost advantage for the non reserved services. In a liberalised environment, high tariffs for postal products in market segments in which entry is very unlikely can generate the financial reserve to cross subsidise other services. In itself cross subsidisation is rather common within an enterprise and not necessarily negative. It becomes negative for the development of competition if cross subsidisation is used with the prime aim to force competitors to exit the market after which prices are raised again.

A strategy of predatory pricing is easier to pursue and maintain for an extended period if fixed costs are high relative to variable costs and if the market segment where predatory pricing is pursued is relatively small compared to the market segments where the postal operator makes relatively high margins. An example is the alleged reaction of Posten AB to the entry of CityMail in Stockholm (Sweden) to reduce the prices in the capital while increasing prices in the rest of the country.⁴¹

Bundling and tying

An incumbent may try to tie certain services with services that fall within the reserved area. If such a strategy is successful, this has a negative impact on entry. In 2000 in Spain the national postal operator Correos required that smaller postal operators would let Correos handle at least 10% of their intra-city mail volume as a condition for providing discounts for the handling of the inter-city mail (not liberalised for items of

⁴¹ See Chapter 3, footnote 17, for a full reference.

correspondence under 100 grams) of these operators. In two cases the Spanish competition authority have ruled in favour of competitor postal operators claiming unfair competition and discriminatory practices on the part of Correos, but no indications were given how to resolve the situation – the new terms and conditions are still subject to negotiation.

Vertical foreclosure

Firms may also tie vertically related services, for example, linking collection and delivery. This may be achieved by signing exclusivity contracts with customers or to the terms of network access offered to competitors. Discounts related to postal volume may also serve this purpose. Most of the examples in practice of vertical foreclosure are on the denial of access, the discrimination of competitors over customers with regard to the access conditions, and the practical conditions under which access can be obtained. Both the conditions themselves and eventual changes of these conditions over time can substantially impede the development of competition. Practical examples of (alleged) vertical foreclosure of this kind can be found in the country information sheets for Austria, France, Germany, Luxembourg and the Netherlands (see also Section 5.3 on network access).

Other non price barriers (litigation, patent protection)

Incumbents may use legal tactics to prevent or limit entry of competitors. By using trade marks and patents for the use of which payments have to be made, costs of competitors may increase. Dispute settlement is also more expensive for smaller firms, both in terms of actual costs, and in terms of the possibility to attract potential customers. In addition, incumbents may sue potential entrants over the possible abuse of patents and trade marks. In particular in Germany competitor postal operators have complained about this type of behaviour of DPWN.

In Table 4.3 an overview is provided of what disputes have arisen in the postal markets of the Member States of the European Union in the last ten years.

Table 4.3 Main disputes related to the strategic behaviour of the national postal operators

Strategic behaviour	Disputes occurred in country
Predatory pricing / cross subsidisation	Austria, Czech Republic, Denmark, Finland, Germany, Luxembourg, Spain, Sweden
Bundling / tying	Spain
Vertical foreclosure (price discrimination, refusal to deal, access conditions)	Austria, Denmark, Estonia, Finland, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Slovenia, Spain, Sweden, United Kingdom
Non price barriers	Germany

Note: The country information sheets included in Annex II provide more information on specific disputes.

Source: ECORYS

4.3.3 Level playing field

The development of competition can be further hampered because of a lack of a level playing field.⁴² This may be the result of differences in the regulatory environment for various players or related to the (non) enforcement of existing regulations.

VAT exemption of postal services

At the moment, the sixth directive on VAT exempts the supply of postal services of VAT. The scope of this exemption differs from country to country.⁴³ Nevertheless, the development of competition is hampered and distorted as the result of this exemption (see Box 4.5 for a discussion on this issue in the UK). The universal service provider does not have to levy VAT, which makes its services cheaper than those of its competitors. On the other hand, it cannot reclaim paid VAT on its inputs. Operations in the postal sector are labour-intensive, which ensures that the actual amount of VAT on inputs is likely to be small. Relative price differences (after VAT) exist between national postal operators and competitors. If postal services are sold to customers that have to levy VAT on their products and services, this price difference is minimised, however, as these customers can reclaim back VAT on their inputs including postal services. The current VAT exemption for certain services provided by the national postal operator thus benefits the incumbent in providing services to customers that are VAT exempt.

Two refinements may be added to this discussion. First, the distinction between inputs used in the provision of exempt services and non-exempt services is difficult. Too much or too little can thus be reclaimed, resulting in distorted prices. Second, due to the exemption, the incumbent operator has an incentive to perform as many activities as possible in house, as these activities do not carry VAT that cannot be reclaimed, even if in house productivity in the provision of these services is low.

Access to letterboxes, change in address notifications

In a number of Member States, only postmen from the national postal operator are able to enter certain apartment buildings, with a lock on the front door, in which private letterboxes are located. This is a severe barrier to entry in delivery, as competitors are unable to deliver their mail in these letterboxes. This situation applies to Austria, France and Poland (in Poland usually also the letterbox itself should be opened with a key which only the tenants and the postmen of the national postal operator have).

Changes in address-notifications are important for all postal operators. If this information is not available to all operators, undue delays in the processing of mail items may occur. This information has public good characteristics, however, as the information is non-rival. Some form of regulation may be needed to ensure that this information is available at the right price for all competitors.

⁴² We here refer to a *rules-based level playing field*, meaning that all firms in a market are treated the same in equal circumstances with regard to legislation, taxes, subsidies etc., and not to an *outcome-based level playing field*, meaning that all firms in a market have the same expected profit (which implies that, in case firms are heterogeneous, the government compensates the disadvantaged firms, for instance with subsidies).

⁴³ See WIK (2004) for an overview of the scope of these exemptions.

Royal Mail's VAT Status

The industry regulator Postcomm called in January 2004 for Royal Mail to start charging value added tax. In a consultative document the regulator said that Royal Mail's VAT-exempt status distorted competition with private postal operators, who are required to charge VAT at 17.5 per cent, and should be "reviewed as a priority, with the aim of levelling the playing field". Rival operators welcomed the announcement but cautioned that any change to Royal Mail's VAT status would have to be approved by the Treasury and would require primary legislation. Postcomm stressed that if the Royal Mail's VAT-exempt status were abolished, it would not necessarily result in stamp prices rising by 17.5 per cent overnight. The aim would be to set it at a rate, probably in lower single figures, which was "revenue neutral". Because Royal Mail is VAT-exempt, it cannot claim back the VAT it pays on bought-in goods such as vehicles. Postcomm's preference is to set the tax at a rate that allows Royal Mail to absorb any increase in prices from the savings it makes in its own VAT bill. However, the Treasury is likely to be concerned at an overall loss of tax revenues if VAT on postal services is set at a lower rate. In a letter last year to a group of private postal operators led by UK Mail, TPG, Hays and Deutsche Post, the Treasury said it would require an EU directive for national postal operators to start charging VAT and this could take years. However, Postcomm pointed out that Brussels had already suggested member states could set rates of VAT for their own postal networks. The requirement for private postal operators to levy VAT has frozen them out of the bulk mail market in financial services, worth an estimated £700m a year, because banks cannot reclaim the VAT they would have to pay. Postcomm's move on VAT is part of a review of Royal Mail's "special privileges". Royal Mail objects to the Postcomm VAT plan claiming that it will lead to an increase in the price of stamps. In a report to Postcomm, Royal Mail says consumers would lose. "It is unlikely that the vast majority of our customers, who would suffer a real price increase as a consequence of the introduction of VAT, would be impressed by the apparent conceptual strength of the 'level playing field' argument," says Royal Mail.

In Sweden, after a period of disputes that were eventually resolved in 1999, a private solution has been adopted: City Mail and Posten AB have established a firm that deals with these issues. In Germany, DPWN initially denied access to its address management system emphasizing that there is a danger that other postal operators could make commercial use of this access by selling the information to other companies. It even rejected to implement the rulings of the Ruling Chamber of the German regulator RegTP referring to data protection concerns. Instead, DPWN developed and implemented a new so called "black box access variant" (providing the transmission of address change data in an encrypted form) with the aim to replace the existing access variants.

The obligation to provide universal services

The obligation to provide universal services puts restrictions on the business model of the universal service provider and on its freedom to take decisions. Of particular relevance are the restrictions that it poses on the size of the network (daily collection and delivery of mail throughout the country) and the requirement to apply tariffs that are uniform for the entire country. With the exception of Estonia, Finland and Sweden the universal service obligations hold only for the universal service provider in return to which the universal service provider is granted an exclusive right to perform certain services (the reserved area). After full liberalisation, the exclusive right of universal service providers will be ended, but the restrictions may be maintained.

The requirement of uniform pricing for the national postal operators makes entry into certain areas more attractive than in others. If a country has a significantly large rural area, with relatively high costs of collection and delivery, prices in urban areas have to be relatively high in order to charge an average uniform price that is not loss making. The urban segment is then attractive to enter. This changes of course if uniform pricing is abolished. In the UK the principle that Royal Mail may abandon uniform nation wide tariffs and introduce different prices for different zones has been accepted, but the practical implications of this decision are not yet clear. In general, a system of non-uniform prices is more difficult to administer for postal operators, in particular for consumer mail, and possibly also more difficult to market.⁴⁴

4.4 Effects of competition on the market

Given the relatively large part of the addressed mail market that has been kept in the reserved area and the current state of competition, it is difficult to fully assess what the effects have been of competition on the market. Tentatively, the effects that can be observed on the behaviour of national postal operators and on market performance are:

- The liberalisation in Sweden is regarded to have led to better performance of Sweden Post in terms of customer orientation and cost efficiency. Also in the Netherlands and Spain liberalisation contributed to performance improvements of TNT and Correios, respectively;
- Prices for overnight delivery of individual item mail have increased in Sweden, prices for other products have by and large gone down;
- The position of large customers towards the national postal operators have strengthened for postal products in liberalised segments;
- The price/quality ratio for (addressed) direct mail has improved as a result of the development of new products and business models. The attractiveness of (addressed) direct mail compared to other means of advertisement or communication has improved contributing to growth in mail volumes in this market segment (for instance in the Netherlands);
- In general, postal services have increased in scope and in the price/quality ratio.

4.5 Summary and conclusion

4.5.1 Development of competition in the Member States

The analysis in this chapter shows that the market shares of the competitor postal operators in addressed mail delivery are still very small. The countries that have liberalised a relatively large part of the addressed mail segment show the highest market share for competitor postal operators: this market share is around 7-11% for Spain, 5-7% for Czech Republic, Estonia, the Netherlands, and Sweden, and 3-5% for Denmark and Germany.

⁴⁴ For example, in the UK 56% of the top 500 customers considered price differentiation a very bad idea, as opposed to 13% that considered it a very good idea. For all customers taken together, the figures are 29% (very bad idea) and 12% (very good idea). See p.72 in Berger (2004); see Chapter 3, footnote 17, for the full reference.

The United Kingdom and France have a somewhat special position with regard to the development of competition. In both countries, competition in end-to-end services is very limited until date. France has maintained a relatively large part of addressed mail delivery in the reserved area but has liberalised the upstream market a long time ago. Mail consolidation has developed rather strongly here, with mail consolidators and large customers having three points of upstream and downstream access for final delivery by La Poste.

In the United Kingdom the delivery of bulk mail consignments of more than 4,000 items has been liberalised in 2000. Though opening up the market for competition, the liberalisation of bulk mail in fact does not facilitate competitors to offer comprehensive business solutions. Only the largest customers have mailings above 4,000 items and these are predominantly B2C (81%). This means that a business model focusing on firstly establishing a position on the B2B market segment is practically impossible and that the business model should focus on the B2C segment with nation wide delivery right from the start. Given the fact that the liberalised market segment only covers around one third of the addressed mail volumes, competitors face high barriers to develop a parallel delivery network. Instead, a number of new entrants started negotiations with Royal Mail on obtaining access to its delivery network. In the beginning of 2004, with the backing of the regulator at various stages of the negotiation process, an access agreement was reached between Royal Mail and three competitor postal operators. Although the volume of mail handling by these competitors has grown considerably during the last year, the final delivery is undertaken by Royal Mail. The experiences with access in a number of countries are further discussed in Chapter 5.

In the other countries there have not emerged competitor postal operators that are challenging the position of the national postal operator until date.

The developments in three countries that have either fully liberalised its letter mail market (Sweden) or to a relatively large extent (the Netherlands and Spain) show that it seems possible for new entrants to enter into addressed mail delivery and to secure a market position of any substance. In a number of countries competitor postal operators have managed to develop a delivery network that is covering a large part or the entire country, albeit that delivery usually takes time not more than 1-3 times a week.

The developments in Sweden indicate that the delivery in a substantial part of a large country with very low population density may well have natural monopoly characteristics. On the contrary, the developments in the Netherlands show that in a small country with a high population density it is possible to develop a parallel delivery network for addressed mail with national coverage. In fact, apart from TNT, both Sandd and Selekt Mail deliver two times a week all over the country.

In general it can be concluded that the liberalisation of addressed mail above 100 grams is insufficient for the development of any meaningful competition if this is not accompanied with the complete liberalisation of the delivery of certain postal products with substantial market volumes. The full liberalisation of the delivery of addressed direct mail offers much better opportunities for new entrants to offer a comprehensive business solution for their prospective clients, as witnessed by the fact that competition is taking off in

particular in the countries that have liberalised this market segment (such as in the Netherlands and in Spain and more recently in Czech Republic and in Estonia).

4.5.2 Key factors influencing the development of competition

The fact that an often substantial part of the delivery of addressed mail is reserved to the national postal operator obviously restricts competition. This is however by far not the only factor that is hampering the development of competition until date. Apart from the natural entry barriers already discussed in Chapter 3, these factors are related to legal barriers to entry, strategic barriers to entry and to a playing field that is not yet level to all players.

The main legal barriers to entry that can be observed in the Member States at present or have caused a slowdown in the development of competition in the past are overly restrictive licence requirements (such as in Estonia and Finland), regulatory uncertainty in general and with regard to definitions in particular (creating uncertainty whether or not certain products are included in the reserved area or not), and the time that it has taken for competitors to obtain access to the P.O. Boxes.

The behaviour of the national postal operators has resulted in a variety of strategic entry barriers including (attempted) predatory pricing, vertical foreclosure, litigation, use of trade marks, patent protection, and the practical (and changing) conditions under which access can be obtained.

For a number of reasons there is not yet a level playing field. In many Member States competitor postal operators are in a worse position than the national postal operator because of the VAT exemptions that apply. Moreover, in countries as Austria, France and Poland the competitors do not have access to part of the private letterboxes, in particular in apartment buildings that have the letterboxes behind a closed front door. There is further not a level playing field between competitors and customers, as in many cases the non-discrimination clause is not applied. In effect, small mailers are in this case partially or fully deprived of the possibility to obtain better prices through mail consolidation. In turn, the business model of the national postal operators is restricted because of the universal service obligations and the principle of uniform prices for postal products in the entire country.

4.5.3 Disputes and role of a postal sector regulator

The issues mentioned above have given rise to a lot of disputes that have in general, by the opinion of the competitor postal operators, taken too much time to resolve. The most common disputes that are observed in many of the Member States relate to regulatory uncertainty (in particular the definition of postal products and whether or not these products are included in the reserved area), alleged predatory pricing and cross subsidisation by the national postal operators, and vertical foreclosure (alleged attempts of the national postal operators to protect the market through price discrimination, refusal

to handle mail by competitor postal operators, and the access conditions for delivering mail for competitor postal operators).

Given the type of problems observed and the stage of development of competition in the mail market, the existence of many disputes calls, at least for a number of years to come, for an independent and well resourced postal regulator in addition to a competition authority that can effectively and quickly resolve existing and upcoming disputes. In addition to settling disputes and through this removing existing regulatory uncertainties, the role that a sector regulator in a transitory period should play is to ensure that access is guaranteed at reasonable conditions to the P.O Boxes and the letterboxes, the postal code system, information on address changes, and the possibility to return mail through the network of the national postal operator. Also, the regulator should play a role on making the existing and future (negotiated) access conditions to the network of the national postal operator transparent and non-discriminatory (see also below). If necessary, the regulatory framework should be adapted to ensure that access conditions will be applied for mail consolidators, customers, and competitor postal operators in a non-discriminatory way.

5 Strategies of competitor and national postal operators

5.1 Introduction

In this chapter we continue the discussion of competition in the EU Member States by focusing on the strategic behaviour of postal operators and potential entrants. Before we turn to this issue, we analyse in Section 5.2 the requirements and considerations of the customers of postal operators. Section 5.3 focuses on the strategies and business models of the competitor postal operators. The discussion starts with three case studies that highlight relevant examples of these strategies and business models until date. Following this discussion, we summarise the findings on the strategies of competitor postal operators and present some results when these competitors are able to break even. In Section 5.4 we turn to the strategies of the national postal operators. A number of these national postal operators are entering foreign markets and compete with the respective incumbents in these countries. In that section, we also present some facts and figures on the national postal operators, like data on revenues, employment and profitability. Section 5.5 concludes.

5.2 Considerations of customers of postal operators

Around twelve, mainly large, customers replied to the questionnaires that were sent out or were interviewed by the project team. Also four customer representative organisations sent back the questionnaires and one small customer was interviewed. Finally, FEDMA, the association representing national direct marketing associations and a number of large direct marketing companies was interviewed. Though this group cannot be regarded to represent all customers in the 25 Member States, the feedback from the questionnaires and interviews provides valuable qualitative information on the considerations and requirements of the demand side of the postal market. Box 5.1 contains a brief summary of two of these interviews.

In addition, information on the demand side of the postal market is obtained from the interviews with competitor postal operators and their responses to the questionnaires. Finally, a couple of studies on customer needs are used, including the study by Berger (2004) on behalf of Postcomm.⁴⁵ This study concerned the UK postal market and involved twelve in-depth interviews as well as 549 structured interviews using a conjoint methodology with small, medium, large, and top 500 customers of postal operators.

⁴⁵ See Chapter 3, footnote 17, for a full reference.

In general, a number of issues came up that are important for the users of postal services. These issues are discussed below.

Box 5.1 Demand for mail services by a large and a small customer

Large customer

The annual expenditure on domestic postal services of a large bank is 142 million euro, involving more than 200 million mail items (estimate) sent per year. Around 54% of the mail produced concerns bank statements. 36% of total mail concerns other items of correspondence, 7% direct mail, 1% international mail and 2% express mail.

At the moment, the bank does not have a choice for the delivery of addressed letter mail and addressed advertising mail. Mail >100 grams is very rare and mail >50 grams rather uncommon. The delivery of international mail does not fall under the area that is reserved to the national postal operator, but the national postal operator is still handling this mail for this customer. In 2006, it is intended to study the opportunity to use another postal operator. Recently, the national postal operator made a better offer for handling international mail, so the outcome of the enquiry is not clear beforehand.

Given the importance of reliable delivery of bank statements and other correspondence, the bank prefers a contract with a well known company with a good reputation, such as TNT or DPWN, if it would decide to cancel the contract with the national postal operator. Apart from price, the service provision by the postal operator is considered important. For example, the latest moment on a day that mail is accepted by the postal operator for next day delivery is important (the later, the better), as well as timely access to a database in which mail streams between the different branches are registered. With regard to the latter, the expected impact on mail streams is valuable information for reorganising and optimising the structure and processes of back offices.

Small customer

A small private company in the Netherlands is specialised in conducting surveys by telephone and by mail. Total staff consists of four permanent staff members and 100-120 employees that are working on a flexible contract. On a yearly basis the company sends approximately 30.000 mail items. 95% of these items are sent in bulk for specific projects, the other 5% are individual letters. The annual expenditure for sending these items is estimated at € 15,000.

Although there is a possibility to make use of competitor postal operators, the company still uses the services of the national postal operator. One of the reasons for this is the fact that several services are obtained from the national postal operator, such as a P.O. Box for the company and a free reply address. They expect that using other postal operators for sending mail will lead to an increase of coordination costs which will not outweigh any possible advantages that may be obtained. For the same reason the company expects that also in a liberalised postal market they will keep on using the services of the national postal operator. The liberalisation of the postal market is however welcomed. For the company especially the liberalisation of bulk mail is considered of importance. Bulk mail and advertising mail are considered the most important postal items for certain SMEs. With the liberalisation of the postal market the company expects that competition will increase and that the prices for postal services will go down.

Commercial importance of mail handling and quality of service

The annual expenditure of large customers of postal services is substantial, varying for most of our respondents between 20 million euro and 150 million euro. The number of mail items sent varies for this group between 30 million to over 200 million per year. Even larger customers, from which we did not obtain feedback, like the largest banks, utilities and telecommunication companies in the largest Member States have even higher annual expenditures and mail volumes. Clearly, moderate mailers have lower expenditure, varying from less than a million to a couple of million euros per year. Private consumers, on the other hand, spend relatively little on postal services, both in absolute and in relative terms: the expenditure on postal services is usually very small compared to the expenditure of private consumers on (mobile) telephony, SMS, and internet.⁴⁶

The expenses on postal services of medium and large customers are hence substantial and a potential 5% or 10% decrease in these expenses has an impact on the financial results of these companies.

The quality of the mail handling itself has a commercial importance as well. It is important that postal items such as bills and bank statements are delivered to the right addresses and at the service level that has been agreed upon (fulfilment of promise). For senders of advertising mail (part of direct mail and catalogues and sponsored magazines) it is important that the postal operator can guarantee when the delivery takes place (the frequency of delivery is not so much an issue for this group of customers).

A quick scan among a number of customers that generate a substantial volume of transaction mail in the Netherlands indicated that most of their mail needs not to be sent with a D+1 service level.⁴⁷ A large bank indicated that a D+1 service level is needed for circa 10% of their mail volume, for the Dutch tax authorities 10-20% of their mail currently requires a D+1 service level. Both organisations are investigating options to reduce this percentage in the coming years. An internationally operating foundation replied that they send less than 1% of their mail with a D+1 service level and that in general e-mail is more and more used, reducing the volume of mail that is sent.

With regard to the opinion of *individual consumers* in the Netherlands, a recent study by TNS NIPO Consult concluded that the daily delivery of mail most of all appears to have an emotional value.⁴⁸ 72% of the respondents regard a reduction of the delivery frequency to four days a week or less not acceptable. However, mail is chosen as instrument for communication mainly because it is tangible (for mail to businesses) or personal (for mail to private contacts) and not because it is delivered the next day – only 1% of the respondents mention that the speed of post is the reason to select this communication channel.

⁴⁶ In Sweden, for private customers postal expenditures constituted 3% of the total communication costs in 2000 (see Annex II, country information sheet Sweden).

⁴⁷ Internal memorandum, Ministry of Economy, the Netherlands, 2005.

⁴⁸ *Betekenis en belang van postdienstverlening, kwantitatieve consultatie van de Nederlandse bevolking*, study on behalf of the Dutch Ministry of Economy, TNS NIPO Consult 2004, p.20.

Reputation of the postal operator

In a number of interviews with customers as well as with competitor postal operators the importance of having an established reputation for acquiring new clients was stressed. New entrants clearly have to invest into developing such a reputation. *Ceteris paribus*, the existence of reputation effects is a competitive edge for some new entrants above others, if they have gained an established reputation in other countries (foreign national postal operators) or other sectors or market segments (publishers). Also in the study by Berger (2004, p.14, p.95) for the UK, the respondents indicate that they have a certain preference for a competitor postal operator with an established reputation, like foreign national postal operators or a well known provider of CEP (courier, express, parcel) services.⁴⁹

Box 5.2 Reputation effects

In several interviews with competitor postal operators, the relevance of having an established reputation for acquiring new clients was stressed. One medium sized competitor postal operator mentioned that it was difficult to obtain mail contracts of large companies, as these companies prefer to do business with large postal operators. Other competitor postal operators noted reluctance among customers to change from the national postal operator to its competitors. A number of large customers indicated that they want to do business with postal operators that have a good reputation. In this light, it is more likely that they would accept an offer by one of the large foreign postal operators (or its subsidiaries) than an offer of one of the new competitors on the market that is not linked to one of the established national postal operators.

In some of the interviews it was however also indicated, that many customers would like to have an alternative to the network of the national postal operator and that some of them might be willing to help alternative postal operators invest into developing their capacity to handle addressed bulk mail and to target the services to their needs.

Demand for value added services and full range of postal services (portfolio effects, one stop shopping)

There are differences between customers that demand more or less standard services and focus on the cost of postal services and customers that demand value added services and focus on an attractive price/quality ratio. Especially the larger customers often want to do business with a postal operator that is able to provide the full range of postal services, including in particular end-to-end services and various value added postal services. In addition, some of these customers want to deal with only one postal operator for all types of mail (transaction mail, advertising mail, individual mail, etc.) or with only one postal operator for all mail in the various countries in which this customer undertakes its business activities. In the extreme case, a customer might want to conclude an agreement with the same postal operator for handling their mail as well as their logistics and express mail. The term *one stop shopping* refers to the above phenomenon (see also Box 5.3).

⁴⁹ See Chapter 3, footnote 17, for a full reference.

Box 5.3 Example of feedback on one stop shopping in Germany

In an increasing global world the larger corporations are looking for best practice solutions that are provided by (leading) postal operators that have shown to be able to integrate IT in their business model, either in the last available update of sorting technology or in new products and services.

The competitor postal operators in Germany mentioned during the country visit that they are developing fast. It was however indicated that especially global customers are more eager to work with well known postal providers that offer a wide range of state of the art integrated services. The competitor postal operators point out that this development is reflected in the customer base (international versus local customers, corporate customers versus smaller SMEs) as well as in the growth of their mail volumes.

A preference for one stop shopping in one or other form has an impact on the development of competition in the mail market. It should be kept in mind, that the dominant part of the mail volume is generated by the business sector and that in most countries large bulk mailers account for over 50–60% of volumes and SMEs account for around 30% of mail volumes. Therefore, one stop shopping is potentially relevant to a substantial part of the mail market and reduces the chances of smaller postal operators that offer a more limited scope of business propositions. Moreover, one stop shopping increases the switching costs for customers, which may lead to rigidities on the mail market.

The interviews indicate that one stop shopping is sometimes aimed at, but usually not in its extreme form mentioned above. For instance, the most of the respondents have no problems in working with a small number of postal operators simultaneously. For some, it is even a deliberate policy to stimulate competition and prevent being locked-in by one postal operator. Clearly, this applies for liberalised market segments only.⁵⁰ However, customers do not want to separate mail streams for (one set of) postal products between two postal operators and demand an encompassing business solution.⁵¹ FEDMA stresses that generally speaking it is important that a postal operator can guarantee national coverage for mailings by companies engaging in direct marketing.

The study of Berger (2004, p.75) shows that for customers in the UK the coverage of the delivery network is more important than the other attributes that were considered in their conjoint analysis: coverage is almost three times as important as the reputation of the postal operator, price, and the conditions for delivery and collection (the relative importance of the last four attributes being almost the same). Still, there is room for local and regional operators, as around 20% of the respondents send their mail mainly to specific regions and 41% of the mailings are posted and delivered within 50 miles (Berger 2004, p.49 and p.62).

Large international companies expressed that in the future there may be an advantage to working with international postal operators rather than to working with postal operators that work on a national level only, if this will give cost or other advantages. One company

⁵⁰ An example is the delivery of the yellow pages in France that is done by three postal operators.

⁵¹ This observation is also made by competitor postal operators.

mentions the possibility to consolidate bulk mail volumes from different countries in one country and herewith to achieve efficiency gains and to obtain better prices.

Customer orientation of postal operator

The respondents are in general not very positive about the level of consumer orientation of the national postal operators. In particular they stress the lack of responsiveness for developing tailor made (value added) services that go beyond the standard services that are delivered through the supply chain of the national postal operators. One example is the interest in database development on postal streams. For example, access to up to date information on postal mail flows can be helpful for (re)organising the structure of front offices and back offices of large organisations with many branches.

Countervailing power: customers would like to have a choice

Discussions with large customers reveal that by and large they will be receptive to proposals by competitor postal operators, if these operators can propose a better price or services that are better targeted to their particular needs. The latter refers to both value added services, technical issues like the cut off time (the latest moment in the day that mail can be given to the postal operator for [next day] delivery), and a joint analysis to develop the most appropriate business solution.

Given the business importance of mail transactions for large customers, some of these large customers may also be interested to facilitate competitor postal operators invest into developing their capacity to handle addressed bulk mail.

The respondents almost univocally are in favour of a complete liberalisation of the mail market and expect that their companies will benefit from this in terms of more consumer orientation, better, tailor-made services and/or lower prices.⁵²

Switching behaviour

Information on price competition between postal operators and actual switching behaviour of customers in the Netherlands is presented in Box 5.4 below.

For the UK, the results of the in-depth interviews by Berger (2004, p.14) suggest that most of the UK customers are risk averse, but also that a trade-off between price and quality is broadly accepted. The majority does not want to take the first-mover risk and can only imagine switching if the new entrants prove their reliability. Up to a 25% price discount would be required to encourage switching. The conjoint analysis under 549 customers, however, shows that switching is an option for many of the customers.⁵³ On the one hand, 40% of all respondents and 30% of the top 500 respondents say that they cannot imagine switching. On the other hand, provided with the option of a 10% cheaper offer by a new supplier with the same quality level as Royal Mail, 80% of the respondents indicate that they will either switch immediately (9%), start negotiating (28%) or will listen to the offer (43%). About 26% expect to have switching costs when switching to a new entrant, 72% do not expect switching costs and 2% do not know. The key factors for possible switching in the future are lower costs, better service and higher reliability.

⁵² Two of the respondents did not want to comment on this (one partly, one fully).

⁵³ The figures below can be found on pages 88, 92, 93 and 101 of Berger (2004, see footnote 17 for the full reference).

Box 5.4 Price competition and switching behaviour in the Netherlands

The websites of the main competitor postal operators in the Netherlands (Sandd, Selekt Mail) indicate that their tariffs are 17% to 20% lower than those of the national postal operator, TNT. BusinessPost, a smaller competitor postal operator, indicates that the savings on cost for their customers can increase to 30%. The tariffs for large bulk mailings are however agreed upon in separate contracts and the price differentials are not publicly available. The mentioned price differences probably reflect the upper side of a band-with existing in practice that also includes smaller price differences.

According to one of the respondents Sandd and Selekt Mail entered the market in the Netherlands by offering prices for bulk mail delivery that were around 20-25% below the prices for bulk mail delivery of the incumbent. In response, TNT has lowered its prices with circa 5% over the last years. Also, TNT responded through offering multi annual contracts to its clients. This strategy proved to be relatively successful, as some of the clients want to avoid possible fluctuations in the costs of mail handling and concluded such contracts with TNT.

Notwithstanding the latter observation, a large number of customers switched to one of the competitor postal operators over the last few years. Sandd and Selekt Mail alone have concluded contracts with around 700 business customers, many of which are well known companies in the Netherlands. The satisfaction among customers with the achieved quality levels and in general with the provided services has grown and is fairly good at the moment.

5.3 Strategies of competitor postal operators

The following three case studies that are particularly relevant for the understanding of the recent developments of competition in the postal sector as a whole and in the mail segment in particular are examined:

1. New entrants in the advertising mail segment;
2. New entrants in the domestic addressed mail market segments;
3. Developments in countries with network access.

The three case studies were developed through desk research of relevant reports and documents and interviews with relevant postal operators and other stakeholders, in particular with those in the countries that were selected for in-depth interviews.

5.3.1 Case study 1: new entrants in the advertising mail segment

In most countries the first new entrants can be observed in the advertising mail segment. The business development often starts with the delivery of un-addressed mail and later on expanding to the delivery of addressed mail. In those countries where in regulation a distinction is made between items of correspondence on the one hand and addressed printed matter on the other (and where the latter is hence not included in the reserved area), this second step involves covering the whole of direct mail operations and finally the full range of professional value added services. In countries where this distinction is not made, the second step involves the delivery of addressed printed matter of higher weight classes, such as catalogues.

Box 5.5 Example of a company in the advertising mail segment entering in addressed mail delivery

ADREXO

In France, the main competitor of La Poste and its daughter company Media Post in the un-addressed mail, catalogues, magazines, and newspaper segments is ADREXO, part of SPIR. Amongst others, SPIR publishes different newspapers and magazines and has five printing plants. The activities of SPIR are mainly concentrated in France, but also comprise publishing and delivery activities in countries like Belgium, the Netherlands, Switzerland and the UK (in particular real estate magazines/newspapers).

ADREXO focuses on the last mile delivery and has an almost complete territorial coverage with delivery to around 23.5 million from the in total 25 million letterboxes in France. Corsica is not covered.

ADREXO has around 26.000 employees and an annual turnover of circa 200 million euro. Delivery takes place at least three times per week in urban areas and one to two times per week in rural areas. The customers bring their mail to one of the distribution centres of ADREXO. There are 220 distribution centres at the moment with the aim to increase this number to 300 in the coming years. In 2004, 7.5 billion un-addressed mail items were delivered as well as 25 million addressed mail items, including small parcels.

ADREXO was established in the early 1970s as a distribution company specialised in free weekly press and magazines around Aix-en-Provence. At first, only the magazines of SPIR were distributed. Later on, also the distribution of magazines of other publishers was taken care of by ADREXO – at the moment ADREXO covers around 175 titles. Further, un-addressed mail, catalogues and small parcels were added to the product portfolio. ADREXO has established itself successfully in a number of niche markets and developed a particular edge in the delivery of heavy documents. All distributors have their own cars and can take 400 kg on each delivery round. For example, ADREXO is one of the three distributors of the *Yellow Pages*, with a 30-40% market share for this particular product, and has a strong position in the delivery of certain small parcels (free gifts to consumers as part of the direct marketing of companies).

Ambition

It is the ambition of ADREXO to become the first private postal operator in addressed mail in France and to compete with La Poste. ADREXO wants to enter into delivery of addressed bulk mail in the business to business and business to consumer areas as soon as the market is liberalised. They have not an interest to start delivering consumer mail. Their strategy is to maintain their focus on the last mile delivery and to cooperate with (pre-sorting) consolidators and transport companies. ADREXO is also interested to develop business relationships with foreign companies, for example on the delivery of advertising mail.

Postal service providers having positioned themselves in un-addressed mail develop economics of scale and a network (including *last mile delivery*) enabling them to cope with addressed mail as well at a later stage. The business model of this type of postal operators focusing on last mile delivery is usually based on 1-3 times delivery per week, low fixed costs through outsourcing, flexible labour contracts and involving relatively cheap labour (students, housewives, pensioners), and the development of certain value added services. An example illustrating the above is presented in Box 5.5.

Also TNT seems to pursue this strategy in a number of countries. For instance, in Belgium its subsidiary Belgische Distributiedienst has acquired a 87% market share in

un-addressed and is delivering addressed mail as well. In Austria, Redmail (a joint venture between TNT and Styria Medien AG) delivers both addressed and un-addressed mail and in Czech Republic TNT became the market leader in un-addressed mail delivery (through Agentura Pro Distribuci a Marketing – Dimar).

Competitor postal operators that are active on the direct mail segment often focus on “*the first mile*.” In some cases they also partly or fully deliver the mail themselves and in other cases they hand over the mail to other postal operators, usually the national postal operator, depending on the country specific regulation and the chosen business model of the competitor postal operator. In some countries direct mail still has a great growth potential. Addressed advertising mail and direct mail is handled for several types of business clients, not only for large customers offering bulk mail but also for small and medium enterprises.

The first mile refers to all the relevant, value enhancing support that can be provided while the information is still in digital form. Examples are pre-sorting activities using database software, printing, computer generated mailings and other pre-mailing activities. At this stage, support is given to customers and the distributor to make their processes more efficient. Herewith, the distribution of information to the end recipient can become more efficient and cheaper in overall terms.

An important value added service is the continuous development of databases containing data on consumer characteristics enabling the business clients to target their mail campaign to the defined target group. Two examples for Sweden and the Netherlands are given in Box 5.6.

5.3.2 Case study 2: new entrants in the domestic addressed mail market segments

The main objective of changes in the regulatory framework for the postal sector is the establishment of the internal market for postal services. Liberalisation of the postal sector at large has in recent years mainly been implemented in cross-border mail, express mail, logistics and value added services. But increasing liberalisation is affecting the domestic addressed mail market segments as well. Already, international postal operators are preparing for increasing competition by positioning themselves through subsidiaries and co-operation agreements with national postal operators.

Examples of new entrants in the domestic addressed mail market segments include companies that, through offering value added services, can circumvent the weight and price limitations related to the reserved area, such as in Germany. Other examples are competitor postal operators that originally focus on addressed direct mail and have developed a distribution network. Some of these companies are already targeting letter mail above 100 grams and have the ambition to deliver bulk transaction mail once the market has been fully liberalised (see Box 5.7).

Sweden

OptiMail, the holding company of CityMail in Sweden, is a small, independent player in the large European letter market. Using new technologies, OptiMail aims to provide new, innovative services to its customers. The common denominator in many of these services is that they focus on *the first mile*. Within the first mile OptiMail sees a trend within direct advertising in which the customers demand an increased degree of outsourcing for the production of the information, file production, printing and packaging. The customer wants to retain control over the creative step in the process and wants to rest assured that made costs are minimal throughout the process. Recently, OptiMail showed its largest increase in mail volumes and turnover in years with an increase of circa 40%. With its subsidiary CityMail it is the only competitor for the national postal operator in Sweden in the (liberalised) market segment for addressed mail.

The Netherlands

Euro Mail was initially established in 1989 as a small company through a former employee of the incumbent PTT Post. The founder of the company was of the opinion that concerning bulk mail, companies could be served better and cheaper. Euro Mail started with pre-postal activities, such as preparation of mailings, printing, cutting, packaging, folding and sealing and pre-sorting activities. Delivery was initially fully done through PTT Post. The company made its margins through mail consolidation, generating mail streams from SMEs in advertising mail. Larger companies often already developed such activities in a professional way, but SMEs faced more difficulties in this respect and moreover handled their direct mail in different ways. Euro Mail supported their customers by making more homogeneous mail streams, ready for sorting and delivery.

During the 1990s many of similar smaller companies started in the Netherlands as the advertising mail market showed steady increasing volumes. These companies were active in both un-addressed and addressed advertising mail. It is estimated that there are now over 40 of such smaller companies in the Netherlands. Euro Mail gradually developed into *Euro Mail Group* through networking with these independent local postal operators. Most of these companies worked already in geographical segmented areas and by networking, national coverage could be reached with clear advantages for all involved. The parent company is responsible for key support functions such as purchasing, sales, marketing, IT support, development of software and hardware, using track & trace information, and invoicing.

Euro Mail Group also provides web based uploading and downloading through access to a centralised connectivity server with FTP access and a unique access code for its customers. Access can be provided through analogue and ISDN connections. New activities were added such as e-billing and e-commerce development and fulfilment activities. Also web mailings are provided as an integral part of direct marketing development. The participating companies also used the name of the parent in local establishments such as Euro Mail Apeldoorn and Euro Mail Amsterdam. Euro Mail Group also developed its own supporting equipment for mailrooms and SMEs with Dutch based suppliers. As computer generated mailings were becoming more important the company established after 1995 alliances with specialised support companies delivering IT concepts and IT support for all related participants in the Euro Mail Group. After 2000 also distribution activities were added and Euro Mail Group could provide "one stop shopping" to its customers by delivering mail to the P.O. Boxes. In 2004 Euro Mail Group realised a turnover of € 17 million with handling of circa 40 million mail items. Euro Mail Group works with around 200 permanent staff and over 500 staff working from their homes in ten locations in the Netherlands. For providing optimal solutions to their customers, Euro Mail Group works with three different competing postal operators with national coverage in the Netherlands (TNT, Sandd and Selekt Mail Nederland) for its mail deliveries.

Germany

In recent years, in Germany licences have been granted to those postal operators that are offering value added postal services. Although the effect to date is still limited many new entrants have emerged. Some of these new entrants are offering regional and local mail services and some already national mail services. A total of 1000 different licenses have been issued, most of them for courier and express mail companies operating in local and regional markets. Also some operators are targeting national postal markets.

Operators such as DBS (Deutsche Brief Service), WPS (Westdeutsche Allgemeine Zeitung), PIN-AG in Berlin and recently Suddeutsche Zeitung Logistik of the German publisher Suddeutscher Verlag are building up their strengths for competition in mail services, while subsidiaries of global postal operators are also building and expanding their network and services, such as already established EP Europost (TNT) and Royal Mail, which has recently announced to restart in Germany.

In the period 2003-2006 competitive postal operators are not allowed to provide mail services up to 100 grams and a price of three times the price of DPWN for the first weight step of the fastest weight category. In practice, because the new postal service providers offer value added services they are managing to overcome these weight/price limitations and have build up a market share of 4% of the large German postal mail market. Indicating the increased need for value added services in the market, most operators have reported steady growth and further ambitions for the near future considering recent decisions to develop a fully liberalised postal market in Germany. According to information of the postal regulator the parties mentioned are building up their network capacities and will take a greater market share of the German postal market in the near future

The Netherlands

In the Netherlands a number of new entrants have established their position in the direct mail and printed matter segments providing national delivery coverage, two times per week delivery and value added services. The main operators are Selekt Mail (a subsidiary of DPWN), MailMerge cooperating with Selekt Mail, RM Netherlands (a subsidiary of Royal Mail) and Sandd. These operators are focused on bulk mail, printed matter, periodicals and sponsored magazines. The strategic advantage of the new operators is a different business model than the incumbent targeting at pre-sorting of highly homogeneous B2B and B2C mail without needing a vast network of interlinked sorting centres with mail processing throughout the complete traditional postal value chain. Collection is done by electronic media, sorting is still mainly manual based on post code areas and delivery implemented in contracts with private sector transport companies covering certain areas.

The leading competitor postal operators Sandd and Selekt Mail have build up a reasonable market share of each circa 4% of the liberalised part of the addressed mail market segment in 2005 and aiming at a market share of 20% at the start of liberalisation. As Selekt Mail is a subsidiary of DPWN it is in a position to provide services for larger corporations especially regarding transaction mail in the near future, adding to the development of necessary volumes to be efficient in postal services provision in the Netherlands.

The networks of competitor postal operators that are already delivering addressed direct mail are better suited for the delivery of bulk transaction mail than networks developed for the delivery of un-addressed mail. As can be seen in Table 5.1, most of the network requirements for addressed direct mail and (predictable) transaction mail are the same, only the requirements for the reliability of delivery are higher for transaction mail than for direct mail.

It is much more difficult to start delivering individual business mail as well (mainly unpredictable transaction mail). This type of mail needs sorting and if a D+1 service level is required, 2-3 times per week collection and delivery is no longer sufficient.

Table 5.1 Network and service requirements for different postal products

Group	Postal product	Able to plan	Scale of operations	Complexity in organisation	Service level: desired transit time	Service level: reliability	Pre-sorting possible
1	Letters (C2X)	No	High	High	High	High	No
	Postcards (C2X)	No	High	High	High	High	No
	Unpredictable transaction mail B2X	No	High	High	High	High	No
2	Books	No	High	High	High	High	No
	Newspapers / journals (B2X)	Yes	High	High	High	High	N.r.
3	Predictable transaction mail B2X	Yes	Moderate	Moderate	Moderate	High	Yes
	Periodicals, magazines (B2X)	Yes	Moderate	Moderate	Moderate	High	Yes
4	Addressed direct mail (B2X)	Yes	Moderate	Moderate	Moderate	Moderate	Yes
5	Addressed catalogues (B2X)	Yes	Low	Low	Moderate	Moderate	Yes
6	Un-addressed mail (mainly B2C)	Yes	Low	Low	Low	Low	N.r.

Note: the scores high, moderate, and low reflect the network requirements that these postal products pose and can be read as most difficult to offer (if high) and less and least difficult to offer (if moderate and low, respectively). N.r. means not relevant. Newspaper delivery has a special position given the special requirements for delivering on a specific moment of the day because of the relatively heavy weight of newspapers.

5.3.3 Case study 3: developments in countries with network access

With an increasing number of competitor postal operators and the limited effect that these operators generally have had on the competition in the addressed mail market, network access has become an important issue in the policy debate. A differentiation can be made

in upstream access (with pre-mailing or first mile activities and transfer of the mail to the *outward* sorting centre of the national postal operator for further processing) and downstream access (pre-mailing activities, sorting and transport to the *inward* sorting centre or *delivery branch* of the national postal operator for “last mile” delivery). Sometimes both options are applicable. So far, within the EU Member States, different arrangements have been made to grant access or not. It is of interest to analyse the impact these different arrangements regarding access have had on the development of competition.

It should be mentioned that apart from access to the P.O. Boxes and for returning mail through the network of the national postal operator, this access is not regulated *ex ante*, but is the result of rather recent negotiations or, as in France, historic developments. A rather mixed situation has emerged in the Member States with countries that have made access arrangements and countries that have not, different terms of these access arrangements and the extent to which the postal regulator was (or had to be) involved in the negotiation process. Box 5.8 briefly discusses the arrangements regarding upstream and downstream access in France, Germany, the Netherlands and the United Kingdom.

It is premature to assess the impact on the development of competition of the various negotiated access arrangements, but the following observations can be made:

- The long history in France with regard to upstream access has led to a mail consolidation industry that is relatively strongly developed. This is also related to the difficulties of La Poste in the 1970s to process all the mail offered, which was one of the reasons to develop concrete conditions for upstream access at the time. At the same time, at least one competitor postal company (ADREXO) that is active in last mile delivery of mail not falling under the reserved area has expressed ambitions to enter into delivery of addressed mail below 100 grams once the reserved area has been removed;
- In Germany the options that are available to large customers with discounts to the retail price varying between 3% and 21% are in practice not granted to the competitors of DPWN and corresponding litigation is pending to the national and European courts. In the mean time, a number of competitor postal operators are developing their delivery networks in Germany;
- In the Netherlands the fact that TNT was reluctant to conclude detailed access agreements with its competitors has given rise to the development of two parallel networks for addressed mail delivery with almost national coverage. By now, the competitors see no need for regulating access by the postal operator;
- In the UK, relatively favourable terms for access for the competitor postal operators have been agreed between Royal Mail and UK Mail, TNT and DPWN. The access price seems to lie closer to a cost-plus tariff than a retail-minus tariff. At least for the time being, the result is that the competitor postal operators do not invest into developing their own delivery network but rather concentrate on upstream activities;

France

Upstream activities have for a long time been liberalised in France and mail consolidation is relatively strongly developed. Large customers, mail houses or mail consolidators can deliver their mail at different level sorting centres of La Poste (at national level, ca. 100 department levels, and at ca. 40.000 postal code levels at discounted prices. The terms of delivery are negotiated and non-discriminatory, although there has been a complaint that La Poste granted its own subsidiaries (Datapost, Mikros and Dynapost) discounts on prices and differential access conditions which were not available to third parties.⁵⁴ The main activities are to collect, pre-sort and to consolidate various mail streams and to hand over this mail to La Poste for the final delivery. In recent years La Poste launched a number of new bulk mail products in an attempt to integrate part of these upstream activities and to secure additional value added. Recently, DPWN took over the French pre-sorting company KOBA. In a press release, DPWN announced that this take over should not be regarded (by La Poste) as an aggressive move, and that there was no intention to enter into last mile delivery.

Germany

In the German postal law options are given for mail consolidation under the exclusive license for DPWN, but in practice the options for customers are not given to competitors. RegTP has repeatedly indicated that the opportunities in practice for upstream and downstream access are limiting competition in Germany. In the postal law it is not clearly stated whether or not competitors of the incumbent have the right to consolidate letters from different senders below the weight and price limits under the exclusive licence (reserved area) of DPWN at the same discounted prices as (large) customers obtain. Corresponding litigation is pending before the national and European law courts.

The Netherlands

With increasing liberalisation of direct mail and after the new postal law of June 2000 mail consolidation became standing practice for a number of local postal operators in the Netherlands, except for the reserved area of items of correspondence up to 100 grams. The main competitors of TNT are not showing much interest in upstream and downstream access, with the exception of access to P.O. Boxes. The main reason is that these competitors use another business model than the standard supply chain and have been able to develop delivery networks with national coverage. Computer generated mailings do not need the vast network of collection points and mail sorting from businesses cannot be compared with mail sorting of single items and can be done much more effectively and efficiently providing better cost/quality options for customers. The competitor postal operators mainly choose to make solutions by negotiated access (in particular for 'last resort' delivery for deliveries not covered by their own network) and see no need for regulated access by the postal regulator.

United Kingdom

In the absence of an access code it is up to third parties to negotiate access with Royal Mail. If an agreement cannot be reached then either party can request a determination of the terms of access from Postcomm. Postcomm has put effort in establishing third party access to Royal Mail's network, although the final agreement was reached by the postal operators alone. In January 2004 UK Mail became the first private company to gain access to Royal Mail's delivery network, with TNT and DPWN to follow. The conditions are for each the same, that is 13 pence for every letter handed over for final sorting and delivery by Royal Mail. All competitor postal operators target business customers with bulk mail of over 4.000 letters per day and transfer already partially sorted mail to Royal Mail. Postcomm is currently considering whether a mandated access code is required and whether access prices should be included in Royal Mail's price control.

⁵⁴ The European Commission addressed an Article 86 decision (OJ 2002 L 120/19, 23 October 2001) on this so called SNELPD case to France after concluding that the then existing legal framework was not sufficient to monitor the conflict of interest between La Poste and private mail preparation firms. The Commission referred France to the European Court of Justice in September 2004 for the failure until then to revise and improve their legal framework.

- When comparing the number of years that it takes for competitor postal operators to gain market share and become profitable, the information on companies like Sandd and Selekt Mail (the Netherlands), CityMail (Sweden) and UK Mail would suggest that this is easier when there is access to the last mile on reasonable conditions – as what could be expected *a priori*;⁵⁵
- Negotiated access as in the UK can be regarded as a work sharing agreement that might ultimately benefit also the national postal operator. The incentive for developing parallel networks with national coverage is reduced and the mail volumes for last mile delivery in the B2C segment can more likely be maintained at a high level;
- Access agreements are a potential source for conflict of interest (if these agreements are concluded with both subsidiaries of the national postal operator and competitors) and a potential source for disputes if the national postal operator unilaterally wants to change the terms of the agreement in due time. Given the impact that these matters have on the level playing field and the development of competition, an appropriate legal framework and effective executing bodies (postal regulator and/or competition authority) have to be in place to resolve these disputes.

5.3.4 Summary of strategies and business models of competitor postal operators

The discussion in Chapter 4 and in this section shows that the competitor postal operators have various strategies and apply different business models to realise their strategies. All these different business models have in common that they differ markedly from the business model of the national postal operator and that the size of the networks that they have developed is substantially smaller than the network of the national postal operators.

The strategies and business models employed appear to differ from each other in a number of aspects:

- *Ownership*. Some competitor postal operators have already fully or partially been taken over by one of the large national postal operators or have an explicit objective to be taken over in due time (like Sandd in the Netherlands).⁵⁶ Other competitor postal operators have expressed the aim to remain independent, such as ADREXO in France. In general, the latter type of competitor is most likely linked to companies that have their core business in markets other than (but relatively close to) the postal market, such as publishers or mail order companies;
- *Focus of activities*. Some competitors focus on upstream activities, some on downstream activities and some on both;
- *Scope of activities*. Some of the competitors have the ambition to establish themselves as a strong player in the addressed mail market and many more do not aim for more than a strong position in certain niche markets and/or in local and regional markets within one country;
- *Development of a delivery network*. With regard to developing a distribution network for addressed mail, both a top down and a bottom up approach can be observed. A top down approach is for example used by EP Europost in Germany with a core national

⁵⁵ Cf. the various country information sheets in Annex II.

⁵⁶ Recently, the business bank NIB Capital and Fortis Bank acquired minority stakes in Sandd (*De Volkskrant*, 29 June 2005)

unit that offers centralised support (IT, marketing, billing) to local operators that carry out the mail delivery at local and regional level. A bottom up approach is for instance taken by certain publishers in Germany. In this case there is a core regional unit supplemented with expanding operations in other regions. The aim is to expand the business scope (for example mail in addition to magazines) as well as the coverage of distribution to more regions. Finally, competitor postal operators that focus on upstream activities and have concluded access agreements with (usually national) postal operators for final delivery are not developing delivery networks, such as UK Mail.

5.3.5 When do competitor postal operators break even?

Although data on the financial results of competitor postal operators are often not available, it appears that most of these operators need 3-5 years before they start to make the first profits. Competitor postal operators that fully rely on access for final mile delivery need less time, probably only 1-3 years.

In the Netherlands, Sandd reached positive financial results after four years of operation with a mail volume of 130 million items which is around 2% of the Dutch addressed mail market. Selekt Mail, that started its operations in November 2002 and was in 2004 handling around 100 million mail items expects to become profitable either in 2005 or in 2006.

Although no financial data are available, the point to reach break even for the competitor postal operators such as MailMerge and BusinessPost focusing on the B2B market segment is reached at much lower mail volumes, probably at 15-25% of the mail volumes mentioned above for Sandd and Selekt Mail.

In Sweden, for reasons discussed in Chapter 4 it took more than ten years before CityMail became profitable from 2001 onwards. In that year they were handling less mail than the 216 million addressed mail items (representing a market share of 6.6% in addressed mail delivery) that were reported for 2003.⁵⁷

The investments needed for the business model taken by UK Mail that fully relies on Royal Mail for the final mile delivery are clearly less than the investments needed if a parallel delivery network is developed as in the examples mentioned above. As a consequence, the point to break even is more easily reached. UK Mail is a clearly successful entrant employing this strategy and is reaching break even after one full year of operation and expecting to become profitable during its second year of operation. The annualised mail volume handled by UK Mail one year after start up is around 250 million mail items, or almost 1.5% of the total addressed mail market in the UK.

⁵⁷ We do not have exact mail volume data for 2001 for CityMail.

5.4 Strategies of national postal operators

5.4.1 Facts and figures for national postal operators

Table 5.1 presents figures on total revenues for the national postal operators in the Member States, split into revenues on mail, express, logistics, and other, mainly financial, services. It further contains data on the number of employees, the operating result, and the current scope of the corporate strategy of the national postal operator (see Box 5.9 for an explanation of the applied terminology for the corporate strategy).

The figures on total turnover show that the four largest national postal operators (DPWN, La Poste, Royal Mail and TNT), as measured by total turnover, generate around 70% of the total turnover generated by the national postal operators in the Member States. Almost half of the turnover of DPWN is generated in markets other than the German home market.⁵⁸ The figures also show that these four companies generate substantial turnover in mail, express, as well as in logistics.⁵⁹

For the other countries, only the national postal operators in Sweden, Finland, Estonia and to a lesser extent Hungary and Slovenia engage in logistic services. Some more national postal operators have a relatively strong position in express (such as in Spain, Czech Republic, and Denmark, but not in Finland and Sweden), whereas a substantial minority of the national postal operators predominantly focus on mail activities and often also provide financial services.

⁵⁸ See country information sheet Germany, Annex II.

⁵⁹ Royal Mail has a different market position in logistics, but is participating in General Logistics Systems International Holdings (GLS) based in the Netherlands with a network in ca. 33 countries. In particular DPWN (including DHL and DHL Solutions) and TNT have strong positions in express and logistics worldwide.

Table 5.2 Turnover and other data for the national postal operators in the Member States

Country	Turnover (million euro)	Division of turnover by activities (%)				Operating result (mln euros) 2003	Number of employees	Current strategic focus
		Mail	Express or Express and Parcel	Logistics	Other			
Austria ¹	1,602	73	10		16	47	28,845 / 26,995 ⁴	Regional
Belgium ¹	1,965	82	2		16	-40	39,002	National
Cyprus ¹	17	95	5			8	1,752	National
Czech Republic ¹	273	85	15			27	38,923	National
Denmark ¹	1,419	81	12		7	211	27,682 / 21,847 ⁴	Regional
Estonia ²	41	63	11	15	10	2	4,237	Regional
Finland ²	1,235	64		34	2	74	23,740	Regional
France ¹	18,004	58	13	6	23	141	285,802 ¹	Global
Germany ²	44,674	29	40	15	16	2,976	340,667 ⁴	Global
Greece ²	447	88	5		7	21	11,402 ¹	National
Hungary ²	463	64	1	1	34	13	41,527	National
Ireland ²	750	63	7		29	-43	10,444	National
Italy ¹	8,150	42	5		53	438	150,746	National
Latvia ¹	38	60	8		31	2	7,316	National
Lithuania ¹	50	62	3		35	2	8,030	National
Luxembourg ²	539	23			77		2,796 / 1,782 ⁵	National
Malta ³	15	77	1		21	4	647	National
Netherlands ²	12,635	33	35	31	1	820	162,244	Global
Poland ²	1,463	58	2		40	41	100,760	National
Portugal ²	745	74	9		17	53	15,273 ¹	National
Slovakia ²	163	64	1		35	4	17,459	National
Slovenia ¹	163	73	8	1	19	10	6,094	Regional
Spain ¹	1,749	74	26			144	63,476	National
Sweden ²	2,674	69		28	3		37,905	Regional
UK ³	12,714	75	3	10	11	103	218,638	Pan-Eur.

Note: The turnover data apply to total turnover of the respective national postal operator, generated in the national home market as well as in foreign markets. Please note that the distinctions between express and / or parcels and the category mail and logistics are not always clear to draw. See Box 5.9 for an explanation of the strategic focus. ¹ 2003; ² 2004 (for Luxembourg, other is mainly telecommunication); ³ 2003-2004; ⁴ in full time equivalents; ⁵ postal operations only. Due to rounding, the percentages may not add up to 100%.

Source: Annual Reports of universal service providers, ECORYS questionnaire responses (2005), assessment of ECORYS (strategic focus).

Box 5.9 Scope of corporate strategy by the national postal operator

National strategy

Within a national strategy, the main focus is on their own country with the dominant revenues from mail and financial services as compared with revenues from express and logistics. Further, the main focus is on exchange through the UPU network. Alliances and cooperation agreements are concluded mainly for international mail.

Regional strategy

Here, the main focus is on (a small number of countries in) a region with a broadening revenue base in other countries for mail, express and logistics. There are own branches and operations in neighbouring countries as well as alliances and cooperation agreements with third parties in other countries for the full range of business activities.

Pan-European strategy

The main focus within a pan-European strategy is on Europe with a broad revenue base in mail, express and logistics. There are own branches and operations in all countries of Europe as well as alliances and cooperation agreements with third parties in all EU countries for business activities.

Global strategy

The main focus is to be active in many, and preferably all, countries around the globe. There is a broad revenue base in mail, express and logistics with own branches and operations in many countries. Alliances and cooperation agreements are concluded with third parties covering the globe.

5.4.2 Strategic orientation of the national postal operator

The strategies of the national postal operators are influenced by a number of relevant developments. First, the traditional revenue base is getting smaller. The emerging competition in an addressed mail market that in most Member States is stagnating (in terms of mail volumes for addressed mail) means that the mail volumes traditionally handled by the national postal operators are shrinking. Further, prices for bulk mail are under pressure, in particular in countries that have liberalised large segments of the letter mail market. Second, and related to the above, although there are a couple of notable exceptions, the financial results of quite some national postal operators show rather limited returns on sales. Third, EU legislation forbids continuous state subsidies. As a consequence, there is a clear need to operate profitably. Fourth, the competition from the communication and advertising sectors as well as the needs of the customers require the continuous development of new products and processes. Finally, in certain market segments of the domestic market it is most effective to compete through subsidiary companies that are run separately and use their own network. This is the case for the delivery of un-addressed mail and mail consolidation, but not yet implemented for the delivery of for example addressed bulk mail (TNT announcing that in future it may use Network VSP for delivering addressed bulk mail in addition to un-addressed mail that Network VSP is delivering currently is the first sign that a subsidiary will become active on this market segment as well).

The effect of the above developments is that there is a general need to improve the efficiencies in postal service provision and to broaden the revenue base, either in the

domestic market (value added services, express, logistics, and/or financial services) or internationally (mainly express, logistics, and activities on foreign letter mail and parcel mail markets) or both. Often substantial investments are needed to achieve this and in many cases these can only be realised through attracting capital from outside.

International strategies

The four largest national postal operators are implementing a pan-European or global strategy (DPWN, Royal Mail, TNT and La Poste) and six others a regional strategy. Malta Post may also develop a broader strategy after its joint venture with New Zealand Post that may offer possibilities to strengthen the activities in international mail. Through joint ventures, alliances and cooperation agreements the national postal operators of these countries have become active on the express and logistics markets of other Member States. This applies to the mail markets as well, although to a smaller extent.⁶⁰

In quite some cases these (foreign) national postal operators have developed into one of the main competitors of the incumbent. For example, TNT is under the umbrella European Mail Networks employing activities in addressed mail in Austria (through a joint venture in Redmail), Belgium (through its subsidiary Belgische Distributiedienst, BD)⁶¹, the Czech Republic (upstream direct mail activities through the Dimar Group), Germany (for instance through a joint venture in EP Europost), Italy, Slovak Republic (Dimar Group) and the United Kingdom. In Belgium, TNT has recently expanded its activities through introducing a new parcel service (see Box 5.10).

DPWN is active on the addressed mail markets of France (through its take over of the mail consolidator KOBA), the Netherlands (through its subsidiary Selekt Mail)⁶², Spain (a stake of 38% in Unipost), and the United Kingdom (through its subsidiary Speedmail).

Royal Mail is active in the Netherlands (mainly delivery of printed matter and parcels to P.O. Boxes) and entered in 2000 into a joint venture with TNT and Singapore Post for international cross border mail (Spring, or officially G3 Worldwide Mail). In this joint venture TNT has a majority share (51%) and Royal Mail and Singapore Post equal minority shares (of 24.5% each; unfortunately regarding Spring no volume or other data are openly available).

The European activities of La Poste mainly concern parcel delivery services.

⁶⁰ See the various country information sheets for more detailed information.

⁶¹ BD is also active in delivery of un-addressed mail where it has obtained a market share of 87%.

⁶² Interlanden, one of the main companies in un-addressed mail in the Netherlands, is a subsidiary of DPWN as well.

Box 5.10 New activities of TNT in Belgium

The Dutch postal company TNT and the press distributor Agence et Messageries de la Presse (AMP) are from 1 July 2005 introducing a new parcel service for consumers and SMEs in Belgium. This is a further expansion of TNT's existing business in the Belgian postal market. The new service offers delivery of parcels within 24 to 72 hours in Belgium and the rest of Europe. From 1 July 2005 customers will initially be able to tender their parcels to 15 newsagent shops in the Brussels municipalities of Ixelles and Etterbeek. By the end of the year, the service will provide nationwide coverage through more than 600 newsagent shops.

Source: website TNT

5.4.3 Economies of scope between mail, express and logistics

At a national level, there are very little economies of scope to be gained by engaging in express and logistics in combination with mail. The demands that are posed on the respective operations differ to such an extent that the activities are carried out through completely separate networks. At international level, however, a presence in express or logistics in a certain country offers opportunities for handling outbound B2X cross border mail as well. TNT is offering this service for instance. Usually, this cross border mail would be handed over to the national postal operator of the countries considered, unless the express (logistics) operator itself would have a local subsidiary or partner to deliver this mail. In this way, outbound cross border mail can be targeted very effectively by internationally operating companies.

5.4.4 Legal status of the national postal operators - searching for outside investors

Linked to the changing business context and in the framework of EU regulation for the postal sector stipulating the separation of the roles of the policy maker, the postal sector regulator and the postal operator(s) almost all of the national postal operators in the Member States have gone through a change in their legal status.⁶³ The current position of the national postal operators is indicated in Table 5.2.

⁶³ The establishment of separate postal regulators is not yet fully implemented in all Member States. Examples are France where the postal regulator will come into force at the end of 2005; Austria, Cyprus and Spain where the Ministry acts as both the policy maker and the sector regulator and Latvia where the Public Utilities Commission acts as regulator.

Table 5.2 Legal status of the national postal operators in the EU Member States

Country	Company	Legal status	Government share	Others	Free Float	Development
Austria	Österreichische Post	Incorporated March 1999	100%		0%	Has searched for strategic partner
Belgium	De Post NV	Incorporated	55,7%	FPM 44,3%	0%	Looking for strategic partner taking a possible stake of 25-49%
Cyprus	Dpt. Postal Services	Government Department	100 %		0%	No change
Czech Republic	Česká Pošta	State Enterprise	100%		0%	No change
Germany	DPWN	Privatised	7.3%	KfW 37.4%	55.3%	Policy to increase free float announced
Denmark	Danmark Post	Incorporated July 2002	100%		0%	Acquired strategic partner CVC Capital Partners in 2005 (22%)
Estonia	Eesti Post	Incorporated 1991	100%		0%	No change
Greece	ELTA	Incorporated	100%		0%	Has searched for strategic partner
Spain	Correos y Telégrafos	Incorporated	100%		0%	No change
France	La Poste	Incorporated	100%		0%	Political discussion on legal status
Hungary	Magyar Posta	Incorporated	100%		0%	First step for privatisation scheduled for 2005
Ireland	An Post	Incorporated	100%		0%	No change
Italy	Poste Italiane	Incorporated	65%	CDP 35%	0%	Political discussion on legal status
Lithuania	Lietuvos Paštas	Incorporated	100%		0%	No change
Luxembourg	PTT Luxembourg	Incorporated	100%		0%	No change
Latvia	Latvijas Pasts	Incorporated	100%		0%	No change
Malta	Maltapost	State Enterprise	100%		0%	35% share by New Zealand Post
The Netherlands	TNT	Privatised	10%		90%	10% will be sold after full liberalisation in the Netherlands
Poland	Poczta Polska	State Enterprise	100%		0%	Now in process of incorporation (scheduled December 2005)
Portugal	Correios Portugal	Incorporated	100%		0%	No change
Sweden	Sweden Post	Incorporated	100%		0%	No change
Finland	Finland Post	Incorporated	100%		0%	No change
Slovenia	Poste Slovenije	Incorporated 1998	100%		0%	No change
Slovak Republic	Slovenská Pošta	Incorporated	100%		0%	No change
United Kingdom	Royal Mail	Incorporated	100%		0%	Political discussion on legal status

The distinctive phases of the legal status of the national postal operators are:

1. *Government department*: the national postal operator is an integral part of a ministry and/or a public administration. In all Member States with the exception of Cyprus, the national postal operator is no longer a government department but a separate postal entity;
2. *State enterprise*: the national postal operator has a distinct legal status and is a separate entity from a government department. In the early days of postal reform starting in the 1990s most postal companies have initially been established as a state enterprise, with decisions on pricing, investments and infrastructure development still needing approval of the State. In Czech Republic and Malta the national postal operator has the status of a state enterprise. Poland is aiming to incorporate Poczta Polska at the end of 2005;
3. *Incorporation*: the national postal operator is established as a public enterprise that is exclusively state owned. A corporate company gives more powers and independency to the postal management to run the postal services, while in addition to the regulatory authority the government maintains (certain) shareholder influence over the business decisions of the company. This process has been implemented in most Member States.⁶⁴;
4. *Privatisation*: the transfer (sale) of shares of the (incorporated) national postal operator to the private sector. As increasingly postal services are seen as commercial services the recent trend is a clear development towards private sector involvement or privatisation of postal companies. Clear examples are Germany (DPWN) and the Netherlands (TNT).⁶⁵ With a shrinking impact of universal service revenues on total revenues this trend is likely to be continued. Other reasons supporting this trend are explained further below.

Impact of legal status on (new) business development and results

As postal services are increasingly seen as commercial services providing products and services with different customer needs and the need to provide different price/quality of service ratio's, postal management has been seeking more independence in business operations with a focus on:

- Determination of service levels and product development;
- Choice of investments;
- Tariff policy;
- Social policy and wage conditions;
- Strategic alliances and/or joint ventures;
- Choice of suppliers.

In general it can be noticed that:⁶⁶

- Independence creates a more clear position towards the choice of investments, tariff policy and social policies. If the main results are still based on the provision of

⁶⁴ In Luxembourg, PTT Luxembourg still combines telecommunications and post.

⁶⁵ The Dutch government recently reduced its share in TNT to 10%. It however also owns a so-called 'golden share' designed to block any fundamental changes to the company structure. The European Commission took the Netherlands to the European Court of Justice (ECJ) in December 2003 over this provision, alleging it infringed the free movement of capital within the EU. An ECJ decision is still pending.

⁶⁶ The authors would like to stress that the issues discussed do not imply a normative viewpoint from our side in terms of what we consider to be good or bad.

universal services less independence can be realised. If the financial results are limited the choice of investments is limited as well. In state owned companies labour unions have more influence on maintaining civil service benefits and have limited (if only in time) increases of efficiency, flexibility and productivity;

- Incorporated postal companies have been more successful in implementing new business strategies than state enterprises;
- Incorporated postal companies are showing improved operational and financial results. Incorporation is realised to establish independency from government budgets and postal management is generally keen to improve their quality of service and financial results. If business results are good, the postal company has more opportunities to invest abroad. If not, it works the other way as criticism of Royal Mail investments in CityMail Sweden has shown in a time that Royal Mail was struggling with operational performance at home; Privatised postal companies have moved even faster in (new) business development and in strategic alliances/joint ventures. Also there is additional shareholder pressure to improve the cost efficiency and the financial results.

Incorporation and increasing privatisation will continue to be important as the postal companies need to increase investments in (new) business development, new (sorting) technologies, new IT systems and other supporting systems, alliances and joint ventures, in response to increasing competitive pressures and stagnating core markets. These investments are both considerable in size and take a number of years of preparation and implementation.⁶⁷ As EU legislation forbids continuous state subsidies the postal enterprises have to look for expanding their market position through attracting investment capital from the private sector.

Examples of this development are:

- ELTA (Greece) offering a 25% stake in express mail and the core mail markets to private investors in 2002. The process was not materialised with partners losing interest in the offer in the process of negotiations;
- Post Danmark (Denmark) in government decisions to transform the postal company to a limited liability company and to sell off 25% to private investors in 2004. DPWN and TNT showed interest but did not succeed in buying the stake. The process was recently completed with the sales of 22% shares to CVC Capital Partners with an estimated purchase price of € 200 million (see Box 5.11 for some information on this company; 2.5% of the shares will be held for an employee share programme and 0.5% will be reserved for an incentive programme for senior staff of Post Danmark);
- De Post/La Poste (Belgium) preparing for the sale of a stake of 25% to 49% to private investors in 2004. DPWN and TNT, that was preparing an offer together with La Poste (FR), have withdrawn their offers in the process of negotiations. TNT has stated in the past that, under the right conditions it would be interested in a stake in the De Post/La Poste. TNT has recently stopped investigating the possibilities to enter into a partnership and immediately after this announced new business development efforts in Belgium (see Section 5.4.2, Box 5.10).⁶⁸ Recently, the Belgium government

⁶⁷ For instance, the new "Briefpost 2000" structure in the Netherlands took five years of preparation and another five years for full implementation, saving 6.000 sorting jobs and contributing to reduce unit cost in mail handling.

⁶⁸ Source TNT website, 27 June 2005; announcement of new business activities made on 30 June 2005.

said it would open in-depth talks with Denmark Post/CVC over the sale of a 50% stake minus one share in De Post/La Poste;

- Österreichische Post (Austria) preparing for sales of 25% to private investors in 2005. This process was not materialised with potential partners including DPWN losing interest;
- Poste Italiane is also heading for partial privatization, possibly in 2006;
- Privatisation of UK's Royal Mail, in contrast, appears to be off the political agenda for the near future.

Box 5.11 Outside investors: CVC Capital Partners

A new player in the postal industry is CVC Capital Partners, with their take over of 22% shares in Denmark Post and its very recently shown interest in a shareholding in De Post/La poste in Belgium. CVC Capital Partners is an independent investment and advisory company dedicated to private equity. The company buys (stakes in) companies to build businesses in partnership with the existing management. In addition to providing a capital injection, a strategic investor like CVC Capital Partners can support in general management, but it does not necessarily provide strengthening of best practice postal management. The question remains if they will have a longer term contribution to postal sector restructuring or provide mainly mid-term solutions to prepare postal operators for future full privatisation.

5.5 Summary and conclusion

The analysis of the *demand side* of the letter mail market shows that the demand side put a number of restrictions on the development of competition, but create also a number of important opportunities for new entrants, not at least because of the considerable expenses that large customers incur for postal services. Reputation and portfolio effects pose challenges to competitors and imply that for a certain type of large customers the national postal operator or a competitor postal operator linked to one of the leading European postal operators has a competitive edge over other competitor postal operators. For other customers an internationally operating postal operator can offer interesting business solutions and for handling international cross border mail postal operators with an international network have a competitive edge as well. The wish for an improved customer orientation and tailor made services as well as the general desire to have a choice between postal operators create opportunities for competition. Also a trade-off between price and quality (in terms of speed or frequency of delivery) is broadly accepted. In general, customers demand an encompassing business solution and most ask for a full chain of postal services. Also the coverage of the delivery network is considered important by many.

The case studies presented in this chapter and the analysis presented in Chapter 4 show that there is a large variety of business models that are used by competitor postal operators. These business models vary as much within one country as between the Member States. All these business models have in common that they differ markedly from the business model of the national postal operator and that the size of the networks that they have developed is substantially smaller than the size of the networks of the

national postal operators. This observation is fully in line with the discussion on contestability in Chapter 3, in particular the part on economies of scale and density.

Although data on the financial results of competitor postal operators are often not available, it appears that most of these operators need 3-5 years before they start to make the first profits. The results of companies that focus on the B2X market segments and have developed a network for two times per week delivery, like Sandd and Selekt Mail in the Netherlands and CityMail in Sweden, show that in these countries a 2-5% market share in the addressed mail market (involving the delivery of 100-200 million mail items) is sufficient to break even. Companies that focus on the B2B market segment (such as MailMerge and BusinessPost in the Netherlands) or on (other) niche or local markets need significantly less volume to break even.

Competitor postal operators that fully rely on access for final mile delivery need less time, probably only 1-3 years. The investments needed for the business model taken by UK Mail that fully relies on Royal Mail for the final mile delivery are clearly less than the investments needed if a parallel delivery network is developed. As a consequence, the point to break even is more easily reached.

The strategies of the national postal operators are influenced by a number of relevant developments: the traditional revenue base is getting smaller, the prices for bulk mail are under pressure, in particular in countries that have liberalised large segments of the letter mail market, the financial results of quite some national postal operators show (with a couple of notable exceptions) rather limited returns on sales, and the competition from the communication and advertising sectors as well as the needs of the customers require the continuous development of new products and processes. The effect of the above developments is that there is a general need to improve the efficiencies in postal service provision and to broaden the revenue base, either in the domestic market (value added services, express, logistics, and/or financial services) or internationally (mainly express, logistics, and activities on foreign letter mail and parcel mail markets) or both. Often substantial investments are needed to achieve this and in many cases these can only be realised through attracting capital from outside.

Further, in certain market segments of the domestic market it is most effective to compete through subsidiary companies that are run separately and use their own network. This is the case for the delivery of un-addressed mail and mail consolidation (for example, the French consolidators Datapost, Mikros and Dynapost are subsidiaries of La Poste), but not yet implemented for the delivery of for example addressed bulk mail (TNT announcing that in future it may use Netwerk VSP for delivering addressed bulk mail in the Netherlands in addition to un-addressed mail that Netwerk VSP is delivering currently is the first sign that a subsidiary will become active on this market segment as well).

Linked to the changing business context and in the framework of EU regulation for the postal sector stipulating the separation of the roles of the policy maker, the postal sector regulator and the postal operator(s) almost all of the national postal operators in the Member States have gone through a change in their legal status. Only in Cyprus the postal business is still run as a government department and in Czech Republic, Malta and

Poland (until end 2005) as a state enterprise. All other national postal operators have been incorporated, or, in case of DPWN and TNT been privatised.

By far the most active players on the addressed mail markets in the Member States are TNT (the Netherlands) and DPWN (Germany). Through joint ventures and takeovers of competitor postal operators that entered into the market these companies have secured positions in the addressed mail markets in each others markets as well as in total in eight other Member States. Both are searching for possibilities for joint ventures and takeovers and are not considering Greenfield investments to establish competing collection and delivery networks from scratch.

DPWN and TNT also showed interest in buying the stakes in the national postal operators of Austria, Belgium and Denmark that were announced for possible sale, but this did not materialise for several reasons. Eventually, the UK investment firm CVC Capital Partners acquired a 22% stake in Denmark Post. The capital injection will enable Denmark Post to invest into diversifying its revenue base and will most likely strengthen its position towards internal competitors and the national postal operators in the region. Apart from providing capital, a strategic investor like CVC Capital Partners can support in general management, but it does not necessarily provide strengthening of best practice postal management. The question remains if they will have a longer term contribution to postal sector restructuring or provide mainly mid-term solutions to prepare postal operators for future full privatisation.

From a company wide perspective, DPWN, La Poste, Royal Mail and TNT are pursuing a pan-European or global corporate strategy. A number of other national postal operators seem to pursue a regional strategy (in particular the Nordic countries Denmark, Estonia, Finland and Sweden as well as the Central European countries Austria and Slovenia) and the majority a strategy focusing on their home markets more or less exclusively, at least for the time being.

6 Likely development of competition in a liberalised environment

6.1 Introduction

What will be the likely development of competition in the letter mail market once the restrictions for competition have been lifted and the market has been fully liberalised? Especially for the addressed mail market segment, the focus of this study, this is not an easy question to answer. Showing the similarities and differences of this expected development for each of the Member States is an even more difficult task to undertake. In this respect, one should keep in mind that in many of the Member States the largest part of addressed mail delivery still falls under the reserved area and that, by default, little competition has developed so far on this market segment.

Keeping the above caveats in mind, the developments in the various Member States until date, and in particular in those Member States where segments of any substance have been liberalised already, do provide valuable information for a well-founded and reasoned analysis of these expected developments. The analysis presented below builds on the analysis of Chapters 4 and 5 as well as on the theoretical observations made in Chapter 3. In addition to this we make use of the interviews that we had with a variety of stakeholders in different countries, the information that we obtained through the questionnaires, and the results of the opinion survey among more than 20 stakeholders from seven Member States that focused on the likely development of competition and its impact on the postal market. Though neither of these sources of information provides conclusive evidence of what can be expected to happen, they all point in the same direction and give support for the analysis presented below.

In Section 6.2 we start with a brief review of expected market developments. A categorisation of the business models that are likely to be employed by competitor postal operators is presented in Section 6.3 and the expected strategic behaviour of national postal operators in Section 6.4. Section 6.5 then continues with an assessment of the expected competitive entry in a liberalised environment. In this section we also compare the anticipated effects of liberalisation of addressed mail above 50 grams and different access regimes with the baseline scenario of full liberalisation without regulating access. The expected development with regard to market structure and market performance is subsequently analysed in Section 6.6. This section includes an initial assessment of the effect of market liberalisation on the provision of universal services. A summary of the main observations and a conclusion is given in Section 6.7.

6.2 Expected market developments

6.2.1 Expected volume developments per mail segment

The size of the mail market (in terms of total mail volume) is expected to show a moderate decline the coming years or to be stable at best. An example of an analysis of the main external factors (from the perspective of a national postal operator) that influence mail volumes in different market segments are given in Table 6.1 below. The report from which this table is taken has been produced three years ago, but the information provided is still relevant.

Table 6.1 Influence of external factors on postal volumes

	Marketing pressure through Internet	Cost savings large consignors	General e-mail use	E-business/ e-delivery	New marketing mix/ other distributors
Banks	Moderate	Strong		Strong	
Other business mail			Strong	Moderate	
Direct mail	Strong	Moderate			Strong
Business reply items	Strong		Moderate		
Magazines					Strong
Stamped mail	Moderate		Strong	Moderate	

Source: TPG Post, *Towards competition without frontiers*, August 2002.

Throughout the EU, the volume for transaction mail is expected to go down the coming year because of electronic substitution. Assessments vary between -1% and -25% for bank statements and between -1%/-2% and -20% for bills from large customers.⁶⁹ Also single items of correspondence are expected to show a moderate decline (varying between 0% to -15%). The volumes for magazines and catalogues are, with a few exceptions, expected to remain stable and for addressed direct mail the expectations are that the volumes will remain stable or will grow.

Though these data should be treated with care and should not be seen as the most accurate market forecasts, in our view the observation can be made that the market volumes for items of correspondence, and in particular transaction mail, will be under pressure the coming years, whereas the market volumes for addressed printed matter will stabilise or grow, mainly dependent on the potential further development of addressed direct mail. The total volume for addressed mail is expected either to decrease moderately or to remain stable, depending on the extent to which the positive developments in addressed direct mail volume will offset the negative trends for items of correspondence. The consequence of these expected volume developments is that the market segment in which competition is (and will be) relatively strong will increase its relative share of the market.

⁶⁹ These and following figures are taken from the response on the questionnaires by the (national and competitor) postal operators. The only country that expects a small increase in the volumes of these postal products is Spain (+2%).

6.2.2 Expected technological developments

The development of postal technology has showed much progress over the last decade. Sorting technology based on postal codes or bar codes has improved considerably contributing to substitution of labour into integrated mail handling systems. This substitution not only brings cost down, but also increases the quality of service.

Further technological developments in electronic communication can be expected in the coming years. This will strengthen the competitive threat of substitutes to postal products and will cause a transformation of traditional postal products to products that further integrate postal services and electronic communication. Examples of developments in recent years were given in Chapter 3 (Box 3.1) and of some product offerings in Box 6.1 below.

Box 6.1 Product offerings by suppliers to the postal industry

One of the leading suppliers in sorting technology Siemens Dematic from Germany provides different sorting solutions tailor made to the postal service provider as indicated in the product offer below:

- Facer canceller machines;
- Culler facer canceller machines;
- Integrated reading & video coding system;
- Delivery barcode sorter;
- Final sorting machine;
- Carrier sequence sorter;
- Compact reader sorter;
- Mixed mail sorter;
- Flats sorting system.

The contribution of technology in the postal business is increasingly targeting the whole value chain from information to database development, specific branch or customer information and client data either in physical, digital or combined formats.

An example of this development is the intelligent mail concept provided by one of the leading suppliers Pitney Bowes, basically using a unique mail piece identifier, data capture and collection architecture, market analytics and decision support systems. The mail type identifier in either a postal code or barcode or any other unique ID is decisive for this integrated approach. Through this technology, data will be generated, analysed and packaged to support the decision making process. Capacity forecasts and performance measurements can be produced and key information is provided for network optimisation.

It is just in these areas that new entrants have tried to find new solutions not using the traditional postal processes (physical collection, sorting, transport, and delivery), but using new technologies replacing one or more of these stages with a digital process.

Use of intelligent mail concepts implicates review of Operations Management and Supply-chain management in postal companies leading to complete overhaul of current structures and processes.

6.3 Likely business models of competitor postal operators

The discussion in the previous chapters clearly shows that new entrants on the postal market do not aim to copy the business model of the national postal operators and that the size of the networks that they have developed is substantially smaller than the network of the national postal operator. Their business models focus on certain segments of the postal market that are open to competition already and involve production processes that are geared partly at value added services and more importantly at low cost production and targeted at the needs of those customers that they aim to serve.

Also after full liberalisation of the postal sector it is not expected that competitor postal operators or new entrants will try to copy the production process of the national postal operators. Moreover, existing and new competitor postal operators will most likely develop a phased approach: establishing a position in one market segment first, and then, after having acquired certain mail volumes and having developed better service levels, entering the next market segment.

Below, we discuss a number of business models that are likely to be employed in a liberalised environment:

- The development of a full service concept;
- The development of a low cost model in certain market segments or certain geographical areas;
- The development of activities in part of the value chain;
- The development of niche markets.

It should be stressed that these business models are not mutually exclusive, some can also be combined. Finally, in the final part of this section, some attention is paid to the technology of the production process and the development of value added services that are relevant to many of the business models that are likely to be employed.

6.3.1 The development of a full service concept

Phase 1

The business model to develop a full service concept starts with entering the addressed bulk mail segment. This segment concerns mail of large and medium sized customers (in terms of the mail volumes that they produce) that can be planned in advance and does not require next day delivery.⁷⁰ The mail itself concerns transaction mail (such as bank statements and bills of telecom and energy companies, salary statements), advertising mail (direct mail, magazines) and other mail (such as company newspapers).

The addressed bulk mail segment can be entered by existing competitor postal operators, but can also be targeted by new entrants: this market segment can be commercially developed as a stand alone business model.

⁷⁰ Or the moment of the production of the mail is to a certain extent flexible and can take place the day before delivery.

For handling transaction mail, investments in sorting equipment, at least for outward sorting, are needed, whereas for advertising mail pre-sorting technologies can be sufficient. In this phase, delivery will usually take place two or three times per week. The coverage of delivery does not need to be nationwide from the start, but will include the P.O. Boxes and the (major) urban areas in the country. If necessary, agreements will be concluded with the national postal operator and/or other operators to ensure delivery in those parts of the country that are not yet covered by the delivery network.

Phase 2

Once sufficient mail volume has been secured to operate the business efficiently, the coverage of the delivery network will be extended to (almost) 100% and other mail segments will be targeted. In this phase, these segments concern the unplanned, individual business mail that does not require next day delivery and possibly consumer mail not requiring next day delivery (in particular the Season Greetings' mail with Christmas and New Year – for the Netherlands this type of mail constitutes around 50% of the C2C market segment in terms of mail volumes and around 35% in terms of revenues).⁷¹

Phase 3

The third phase in the development of the full service concept is to extend the delivery frequency to five times per week and to enter the mail segment for business mail requiring next day delivery.

Given the small size of the market and the additional complexity of daily collection, it is not expected that a competitor postal operator will engage in the collection and delivery of individual consumer mail requiring next day delivery.

6.3.2 The development of a low cost model

Within the full service concept, eventually a range of business propositions can be offered for different types of customers and for different types of mail. Through realising economies of density and scope it is aimed to offer these business propositions at competitive prices while offering quality levels that are superior to these of the national postal operator.

Low cost models typically aim to compete on price through running a low cost production process and through realising economies of density. Rather than offering full service, competitor postal operators employing a low cost model will specialise on certain market segments and will try to keep investments and fixed cost to a minimum. In principle, two low cost models can be developed for addressed bulk mail not requiring next day delivery: one for transaction mail (requiring investment in sorting equipment) and one for (mainly) addressed printed matter (not requiring investments in sorting

⁷¹ The volume figure is mentioned in several publications; the revenue figure is an estimate by ECORYS based on the difference in average price between sending Season's Greetings cards and ordinary items of correspondence. See for a recent survey result *Betekenis en belang van postdienstverlening, kwantitatieve consultatie van de Nederlandse bevolking*, study on behalf of the Dutch Ministry of Economy, TNS NIPO Consult 2004, p.9.

equipment). In practice, however, we expect that low cost models will be developed for the entire addressed bulk mail segment, combining transaction and advertising mail.⁷² Low cost models will typically not go beyond phase 1 described above. Delivery will not take place more than two or three times per week and a full national coverage of the delivery network will not necessarily be aimed at. Examples of competitor postal operators that have employed this kind of business model are Sandd (the Netherlands) and CityMail (Sweden) showing that in these countries a mail volume of 100-200 million mail items is needed to break even.

Another low cost model that can be employed is the establishment of interregional networks that exchange mail between more or less independent local operators. The network provides sorting and transportation and usually also carries out a number of support functions (IT, marketing, billing), while collection and delivery is undertaken by the local operators.⁷³ Unipost in Spain and EP Europost in Germany are developing this type of model.

6.3.3 The development of activities in part of the value chain

Other business models will focus on activities in part of the value chain and will not aim at end-to-end collection and delivery. One business model is to focus on the last mile and to cooperate with mail consolidators and (pre-)sorting companies. Companies that have developed a delivery network through un-addressed delivery or delivery of magazines and catalogues may opt for such a business model. ADREXO in France is an example here of a competitor postal operator that is focusing on the last mile and has developed a strong position in a number of niche markets at the same time.⁷⁴

Another business model is to focus on the first mile and to cooperate with other postal operators for delivery. Examples are mail consolidators such as in France, the Netherlands and other countries that amongst others are targeting small businesses not targeted at in the low cost models. Other examples are companies like UK Mail and other operators in the UK that position themselves primarily as a competitor postal operator but have concluded access agreements with the national postal operator for the final delivery.

6.3.4 The development of niche markets

In a liberalised environment, there will continue to be potential for business models that focus on certain niche markets or on certain local markets. The exact focus of these business models is very difficult to predict. Niche markets that can be observed in

⁷² For Germany the size of this market is estimated to be 40-50% of the addressed mail market by Helmut M. Dietl and Peter Waller (2001, p.6; see Chapter 3, footnote 17, for a full reference). They refer to this business model as mass mail service provider.

⁷³ Dietl and Waller (*ibid*) indicate that operators offering only local mail services have in total access to about 30% of the addressed mail market whereas local operators that unite forces in a network have access to 80% of the addressed mail market.

⁷⁴ As discussed in Chapter 5, ADREXO has expressed the ambition to enter into the delivery of addressed (bulk) mail under 100 grams once this segment of the market is liberalised in France expanding their current business model with the first type of low cost model discussed above.

downstream markets in practice include the delivery of heavy documents, delivery to P.O. Boxes and same day delivery in urban areas. Also document exchanges focusing on B2B customer groups with close mutual relationships can be regarded as a niche market, with Hays in the UK as a prominent example. Finally, spot operators that do not run a regular network but hire postmen for the few occasions that it distributes action mailings like mail order catalogues operate in a niche market.

6.3.5 Technology of the production process and value added services

Within the expected diverging range of price/quality ratios for postal products competitor postal operators will hence focus on low cost services and value added services (such as proof of delivery, second time delivery, tracking systems, etc.) at the same time. As mentioned several times above, the production process will not copy that of the national postal operator but will be such that the network size remains limited using various existing and new technologies. Also the national postal operators will more and more develop value added services and will need to invest in updating their 'old' techniques because their logistic structure is linked to the universal service provision requiring collection and delivery five to six times a week. Apart from this, through setting up subsidiary companies, the national postal operators will be able to use the same type of networks and technologies as their competitors in certain market segments (value added services, upstream activities and possibly even the delivery of second class bulk mail as TNT expressed it was intending to do).

6.4 Expected strategic behaviour of national postal operators

In this section, an analysis is made of the expected strategic behaviour of the national postal operators, both on their own domestic markets and on the markets of other EU Member States.

6.4.1 Strategic behaviour of national postal operators on domestic markets

The behaviour of the national postal operators is influenced by the general need to improve the efficiencies in postal service provision and to broaden the revenue base, either in the domestic market (value added services, express, logistics, and/or financial services) or internationally (mainly express, logistics, and activities on foreign letter mail and parcel mail markets) or both. Substantial investments are needed to achieve this and in more and more cases it will become clear that these can only be realised through attracting capital from outside. The search for outside investors described in Chapter 5 is likely to continue and even to intensify if the financial results remain limited.

The national postal operators in most countries will aim to consolidate their position on the domestic market. They will continue to try to protect their markets and deter entry as much as possible, in particular through raising non-price strategic barriers. In general the national postal operators will seek to compensate for the diminishing mail volumes as a result of competition, substitution and rationalisation (of large customers) by offering

additional services (such as address management and hybrid mail) and/or through diversification and regional expansion (see 6.4.2).

There will be a continued tendency of national postal operators to set up or take over subsidiaries to compete on specific market segments, in particular when the legal status of the national postal operator or the regulator or competition authority puts restrictions on the implementation of certain business models or when it is for other reasons better to use another production process (for example for mail consolidation and un-addressed mail).

6.4.2 Strategic behaviour of national postal operators on markets of other EU Member States

The discussion in Chapter 5 revealed that only a limited number of national postal operators adopted a pan-European or global strategy: DPWN, TNT, Royal Mail and La Poste. These companies aim to increase their market share in those markets where they are present already through organic growth, joint-ventures and takeovers, and aim to establish positions in new markets through joint ventures and takeovers. Of these four companies, only DPWN and TNT have established positions in the letter mail market in more than a few countries. Further, DPWN and TNT have shown consistent interest in taking a stake in other national postal operators. This interest will most likely continue to exist, in particular if acquiring such a stake will lead to a real influence on the management of these national postal operators.

The largest national postal operators have not shown interest into setting up competing collection and delivery networks from scratch. Rather, their policy has been to takeover attractive new competitor postal operators or to establish joint ventures with companies that already possess a delivery network. It is expected that this behaviour will not change the coming years.

It is clear that not all Member States will be targeted at the same time and to the same extent. Countries that will be targeted first are the countries with relatively big home markets and/or with good growth potential (in particular in direct mail). Moreover, in particular the largest national postal operators will try to establish good positions in cross border mail and aim to create synergies with their own delivery structures for the delivery of the volumes of outbound cross border mail that are obtained in other countries.

The national postal operators with a regional corporate strategy will focus most of all on their neighbouring countries.

6.5 Expected competitive entry in a liberalised environment

6.5.1 Pattern of competitive entry

Most of the likely business models of competitor postal operators discussed in Section 6.3 will be simultaneously employed in a liberalised environment. Activities in niche markets and in local markets will be undertaken by a relatively large number of operators but will in itself not pose a real competitive threat to the national postal operators in their home

markets. The combined market share that these operators will achieve in the addressed mail market will remain relatively modest because of the fact that these operators target only part of the market and that most customers ask for a full chain of postal services that these players are unable to offer. The study by Dietl and Waller (2001) indicates that in Germany operators offering only local mail services have in total access to about 30% of the addressed mail market and the study by Berger (2004, p.96) shows that only 14% of the UK respondents prefer a specialised (niche service) postal operator and 66% an operator offering the full chain of postal services (a full service or low cost operator).⁷⁵

It remains to be seen whether competitor postal operators will develop into national full service providers. This strategy is only profitable in countries where the national postal operator provides low quality services. For the vast majority of the Member States we do not expect the development of a full service concept, although it cannot be fully excluded that in an isolated case such a competitor postal operator will emerge and may even outperform the national postal operator.

Much more likely business models that will be employed are low cost models focusing on addressed bulk mail not requiring next day delivery and the establishment of interregional networks that exchange mail between more or less independent local operators. Many of the existing competitor postal operators are pursuing this strategy. Although these models do not target the entire market for addressed mail, they pose a competitive threat to the national postal operator and are in principle able to capture a substantial share of the market. The same applies for models focusing on last mile delivery by entrants that have already developed a delivery network through their activities in un-addressed mail or in magazines and periodicals (publishers).

Mail consolidation and a focus on upstream activities in general are also business models that can be observed in practice and are likely to be employed. The nature and magnitude of these models depend on the access conditions for the final delivery of mail and, for mail consolidation, on the level of price discrimination between small and large senders of mail. There is further a relation between the development of low cost delivery models, models focusing on upstream activities and access conditions that will be further explored in Section 6.5.3 below. Although some value added will be lost for in potential substantial mail volumes (in case the access conditions are relatively favourable), these models may be less threatening to the national postal operator (as final delivery is more likely retained) than the low cost models, depending on the anticipated impact of these low cost models on its market share and revenues.

Within all the business models discussed above, there will be attention for developing value added services and tailor made services dependent upon the specific needs of the customer.

The new entrants employing these business models will be both national and international companies that, in particular for the low cost models, have some sort of delivery network already and can establish such a network by involving a variety of existing companies.

⁷⁵ 20% of the respondents did not know or did not answer this question. See Section 6.3.2 and Section 5.2 for the full references.

The likely national new entrants into addressed mail at the national level are publishers expanding into the mail market (like the ones that already started activities on the German market), un-addressed mailers developing into addressed advertising mail and possibly transaction mail as well (such as potentially Belgische Distributiedienst, ADREXO, and Netwerk VSP in Belgium, France and the Netherlands, respectively) and new postal operators targeting specific mail flows requiring limited investments and a small network. Express companies are not expected to enter into the addressed mail market with the possible exception of outbound cross border mail for some companies.

The likely international new entrants are mainly the national postal operators that have adopted a pan-European or global strategy and operators that are pursuing a regional strategy. The former group of companies, most of all DPWN and TNT, will target countries with high mail volumes in which they have limited presence so far (for example France and Italy), countries and market segments with substantial unfulfilled demand (such as Czech Republic, Hungary and in the medium term Poland), and countries that provide opportunities through a mixture of reasons like Belgium that has rather favourable country characteristics (high degree of urbanisation, high population density, relatively high addressed mail volumes per capita) and a national postal operator that needs to invest into reaching a higher level of efficiency. The strategy for the other smaller countries such as Latvia and Lithuania will be to engage in high end value added services. The latter group of companies will focus their attention on their neighbouring countries. It is further expected that these entrants are not interested into developing niche markets or local markets.

6.5.2 Scale of competitive entry

The scale of competitive entry and, more generally, the competitive pressure that is posed on the national postal operator through existing competitor postal operators, expected entry and the threat of new competitors entering the market will vary from country to country. In other words, it is expected that effective competition will develop at different speed in the Member States.⁷⁶ In Table 6.2 we aim to make a prediction of these speed differences, primarily through looking at a number of factors that have an impact on the likely entry of new competitors and the growth potential of existing competitors.

Before introducing Table 6.2 into more detail, a methodological point that we want to stress is that we most of all look at (potential) entry, given the current underdeveloped level of competition in the postal market and the importance of entry for the development of competition in the medium term. This can be at odds with the short run effect of certain developments on competition. An example may be helpful to illustrate this. Internal competition is (*ceteris paribus*) more intense when the market is static or declining than when the market is booming and when operators face an easy task to increase their turnover and revenues. The short run effect of declining market volumes for addressed mail is hence that it intensifies internal competition. On the opposite, substantial (potential) growth in for instance addressed direct mail volumes will be

⁷⁶ In the analysis in this section we focus on internal competition and (potential) entry, disregarding the influence of substitutes and bargaining power of buyers on the level of effective competition for the moment.

conducive to entry of new competitors in this market segment and will contribute to the development of competition in the addressed mail market in the medium term.

High total mail volumes, high per capita mail volumes, a potential for growth in direct mail volumes, a high degree of urbanisation and high population density have a positive impact on the business case of new entrants by making it relatively easy to secure sufficient volumes to operate their networks in a profitable manner.

Existing competitor postal operators that are (partly) owned by one of the (major) national postal operators may profit from the reputation of the mother company, its international network, its expertise in running a business in the postal sector and its support with introducing new technologies, human resource management and staff training. The existence of such competitor postal operators is conducive to the development of competition.⁷⁷

⁷⁷ Given the fact that setting up joint ventures and realising takeovers take time and that setting up competing collection and delivery networks from scratch is not considered by the main national postal operators, this puts the countries where foreign NPOs are present ahead of the other countries with regard to the expected development of competition in the medium term.

Table 6.2 Expected development of competition in the Member States relative to each other in the medium term (disregarding any remaining barriers related to the existence and application of country specific regulation)

Member State	Total mail volume	Mail per capita	Direct mail potential	Urbanisation	Population density	Foreign NPOs	Relative score
Austria	+/-	+	+/-	+/-	-	++	+/-
Belgium	+/-	+	+/-	++	++	+	++
Cyprus	--	-	+	+/-	-	-	-
Czech Rep.	-	-	++	+	+/-	+	+/-
Denmark	+/-	++	+	++	+/-	+/-	+
Estonia	--	--	+	+/-	--	+/-	-
Finland	+/-	+	+/-	-	--	+/-	+/-
France	++	++	+	+	+/-	+	++
Germany	++	+	+/-	++	+	++	++
Greece	-	--	+	-	-	-	-
Hungary	-	-	++	+/-	+/-	+/-	+/-
Ireland	-	+/-	+	-	--	+/-	-
Italy	+	+/-	+/-	+/-	+	+	+
Latvia	--	--	+	+/-	--	-	-
Lithuania	--	--	+	+/-	--	-	-
Luxembourg	-	++	+/-	++	+	+	+
Malta	--	+/-	+	+/-	+	-	+/-
Netherlands	+	++	+/-	-	++	++	++
Poland	+/-	--	++	--	+/-	-	+/-
Portugal	+/-	+/-	+	--	+/-	+	+/-
Slovakia	-	-	+	--	+/-	+	+/-
Slovenia	-	+	+	+	-	+	+/-
Spain	+	+/-	+	++	-	++	+
Sweden	+/-	++	+/-	++	--	++	+
UK	++	++	+/-	+/-	+	++	++

Notes: Mail volumes are for addressed mail delivered. The scores reflect the position of the Member States on the chosen indicators relative to each other and do not have an absolute meaning. A plus in this table indicates that the factor in the respective column has, ceteris paribus, a (relatively) positive contribution to the viability of business models that can be employed by new entrants or, in case of the factor 'foreign NPOS' that a foreign NPO is active as a competitor on the addressed mail market or the likelihood that it will enter the market in the short term. The last column under relative score summarises the expected impact on the development of effective competition through the expected entry and development of competitors and the disciplining force that the threat of entry poses on the existing postal operators. See Box 6.1 for a brief explanation of the individual scores and the data sources.

Box 6.1 Explanation of relative scores and data sources of Table 6.2

The scores reflect the ranking of the Member States on the respective indicator and by grouping comparable values into one and the same score. Per indicator, a maximum of five different scores varying from ++ to – were given. The scores on total addressed mail volume (total number of mail items delivered) are based on Figure 2.4 and the scores on per capita addressed mail volume on Figure 2.5. The data for urbanisation and population density are presented in Annex I, appendix 6.

The scores on direct mail potential reflect the assessment by ECORYS using data on per capita direct mail volumes (see Annex I, appendix 7). The per capita volumes of countries that have a mature direct mail market such as the Netherlands are taken as a benchmark. Countries that have liberalised the delivery of direct mail already for a number of years and/or have high per capita volumes were scored as +/- . Other countries received a +; countries that have relatively low per capita volumes at the moment and have country characteristics that enable the development of the B2C segment (degree of urbanisation and/or population density is at least moderate) obtained a ++ score.

The scores for the influence of foreign NPOs are based on the information presented in Chapters 4 and 5. The score ++ was given if (one of) the main competitor postal operator in the addressed mail market segment is partially owned or controlled by a foreign NPO. In case of a +, a foreign NPO partially owns or controls a competitor postal operator that is active on the mail market, but mainly in unaddressed, magazines, or upstream activities that has a real potential to enter into addressed letter mail delivery (direct mail, transaction mail). A score +/- is given if a foreign NPO partially owns or controls a competitor postal operator that is engaging in activities on the mail market, but this postal operator does not operate an extensive B2C delivery network and/or does not process mail volumes of any substance in case of upstream activities. In countries with the score -, there are no competitor postal operators active on the mail market that are partially owned or controlled by a foreign NPO.

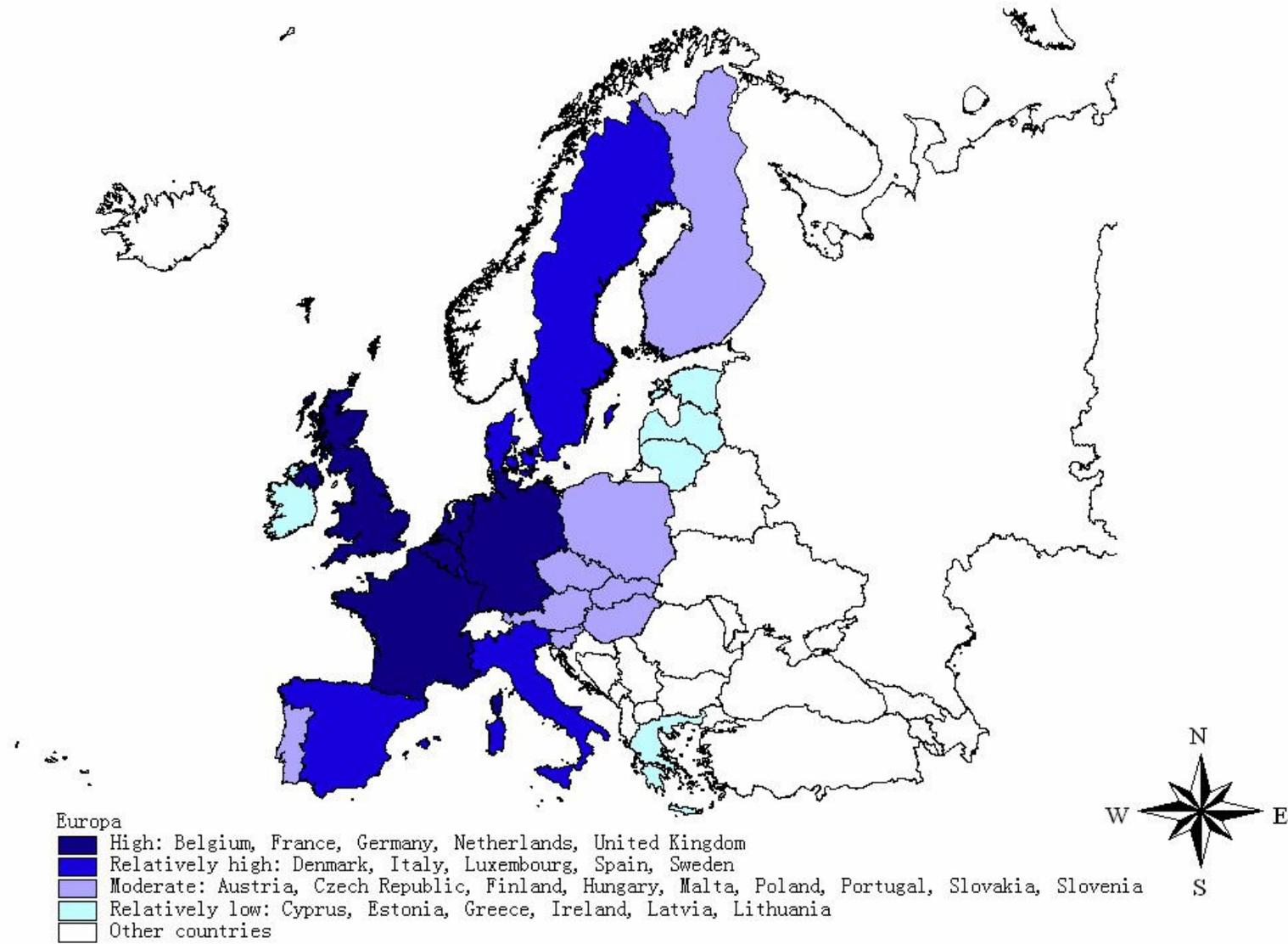
The 'final' relative score is obtained through ranking the not weighted average of the six scores and through clustering the countries into four groups.

The last column in Table 6.2 summarises the expected development of competition (or competitive pressure on the national postal operator) in the Member States relative to each other. Clearly, this summary disregards any remaining differences between the Member States regarding other barriers to entry that may continue to exist, depending on country policies, the position and actions of the postal regulators, differences in country specific regulations and so on. In Box 6.1, an explanation of the value of the individual scores is given and reference is made to the data sources.

Based on this analysis we expect that, disregarding any remaining barriers related to the existence and application of country specific regulation, the potential for the development of competition in a liberalised environment in the medium term will be (see also Figure 6.1):

- Highest in Belgium, France, Germany, the Netherlands and the UK;
- Relatively high in Denmark, Italy, Luxembourg, Spain and Sweden;
- Moderate in Austria, Czech Republic, Finland, Hungary, Malta, Poland, Portugal, Slovakia, and Slovenia;
- Relatively low in Cyprus, Estonia, Greece, Ireland, Latvia, and Lithuania.

Figure 6.1 Potential for the development of competition in the Member States in the medium term



6.5.3 Expected competitive entry under alternative scenario's

In this section we briefly touch upon the expected competitive entry in two scenarios other than our baseline scenario of full liberalisation of the postal market. Alternative scenario 1 concerns the liberalisation of the delivery of mail between 50 and 100 grams that is anticipated to take place throughout the EU per 1 January 2006. Alternative scenario 2 examines the impact of different regimes of access to the facilities of the national postal operator in addition to the full liberalisation of the mail market.

Alternative scenario 1: liberalisation of the delivery of mail above 50 grams

The liberalisation of the delivery of addressed mail above 50 grams increases the market open to competition by about 10%. The biggest part of addressed direct mail and of transaction mail in particular is below 50 grams and is hence not affected by this step in the liberalisation process. This implies that for the majority of the Member States the reserved area will still constitute (considerably) more than 50% of the addressed mail market.

The experiences in the countries that in the past have fully liberalised certain segments of the addressed mail market clearly show that competition is taking off in particular in these segments and much less so in the addressed mail above 100 grams with the exception of certain niche markets. This is in our view related to the fact that competitor postal operators need to be able to offer comprehensive business solutions for their prospective clients. For example, direct marketing companies can be effectively approached if the delivery of addressed printed matter is fully liberalised, whereas competitor postal operators have little to offer to banks, insurance companies or utilities if they can only deliver mail above 100 grams. The liberalisation of mail above 50 grams will not help much in this respect: also in this case competitors cannot propose appropriate business solutions to the latter type of clients.⁷⁸

For addressed printed matter the prospects for competitors to gain additional market share are better than for items of correspondence. There are certain products in this segment that weigh between 50 and 100 grams and certain mail campaigns involve mail in this weight category as well or may be combined to reach this weight category. For example, one of the interviewed competitor postal operators sees some potential for acquiring part of the delivery of small catalogues of between 50 and 100 grams.

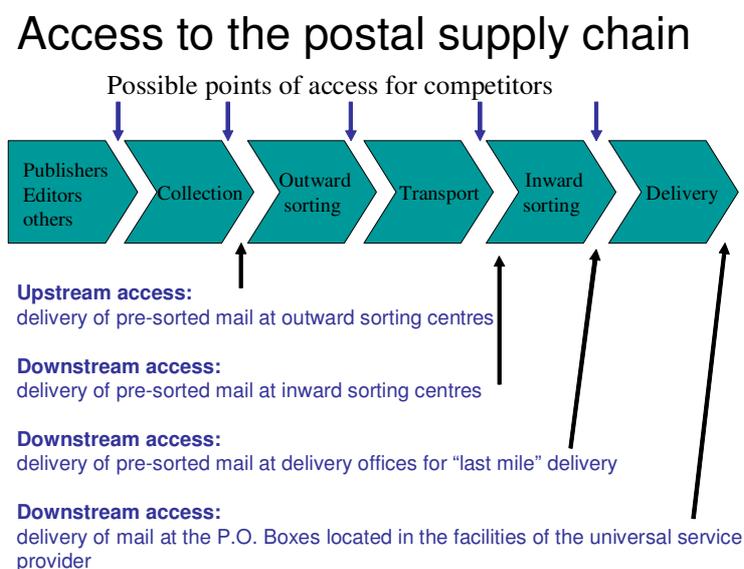
The conclusion that the liberalisation of the delivery of addressed mail above 50 grams does not constitute a real breakthrough for the development of competition in the postal market is widely shared among stakeholders as evidenced in the replies obtained in the questionnaires, interviews and opinion survey. The fact that quite a number of national postal operators indicate that they would like the liberalisation process to stop at the level of 50 grams further underlines that the competitive threat of existing and potential competitor postal operators is only strongly felt after a full liberalisation of the postal market.

⁷⁸ Also the limited development of competition in Denmark, that liberalised the delivery of addressed mail above 50 grams already and did not liberalise the delivery of direct mail under 50 grams, supports this line of reasoning.

Alternative scenario 2: full liberalisation of the mail market plus network access

With regard to the impact that access to the network of the national postal operator has on the expected competitive entry and on how competition is most likely to evolve it is important to realise that it is not so much important whether access has been regulated or not, but much more on the actual conditions of enabling this access. Having said this, in general an active position of the sector regulator is proven to help generate relatively favourable access conditions.

Figure 6.2 Possible points of access to the postal supply chain



Access is possible at a number of points of the network (see Figure 6.2) and there can be different reasons or purposes for arranging access:

- First access can be sought as a matter of last resort: a competitor postal operator that is operating a delivery network that is not (yet) fully covering all customers may want to hand over part of the mail of their customers to the national postal operator for final delivery;
- Second, access can be sought by mail consolidators who primarily realise their business case because of the price discrimination of the national postal operator between small and large customers;
- Third, access for final mile delivery can be sought by companies that position themselves as postal operators and want to deliver services in a smaller or larger part of the value chain. These operators tend to focus on large customers.

For the first two groups of companies, application of the principle of non-discrimination between (large) customers and competitors has proven to be generally sufficient. This type of access is compatible with the development of parallel delivery networks as experiences in the Germany, the Netherlands, Spain and Sweden have shown.

If downstream access is regulated (or such as in the UK negotiated with the backing of the postal regulator) on a cost plus basis and hence on relatively favourable terms,

companies of the third type can enter the market.⁷⁹ This type of access will generally be detrimental to the efforts of competitors to invest into developing a parallel delivery network. Low cost models will less likely be developed but it creates opportunities for mail consolidators. In the short run, upstream competition will be created fairly easily as the investments needed are relatively low and the point to break even more easily reached. UK Mail is reaching break even already during its second year of operation.

It is too early to say whether this type of access will eventually lead to UK Mail and likewise competitors to set up its own delivery network once substantial mail volumes have been reached.

In practice access has given rise to a wide variety of disputes that may not have arisen if there would be a parallel delivery network and the freedom to deliver all types of mail. For example, the problems in France with regard to the changing access conditions and the alleged favouring of its subsidiaries by La Poste would be much less if the mail consolidators would have the option to turn to another postal operator for last mile delivery. The same applies to the various disputes that there have been in different countries on the sudden high tariff rises for the delivery of certain postal products (such as newspapers).

6.6 Likely effect on the postal sector in the Member States

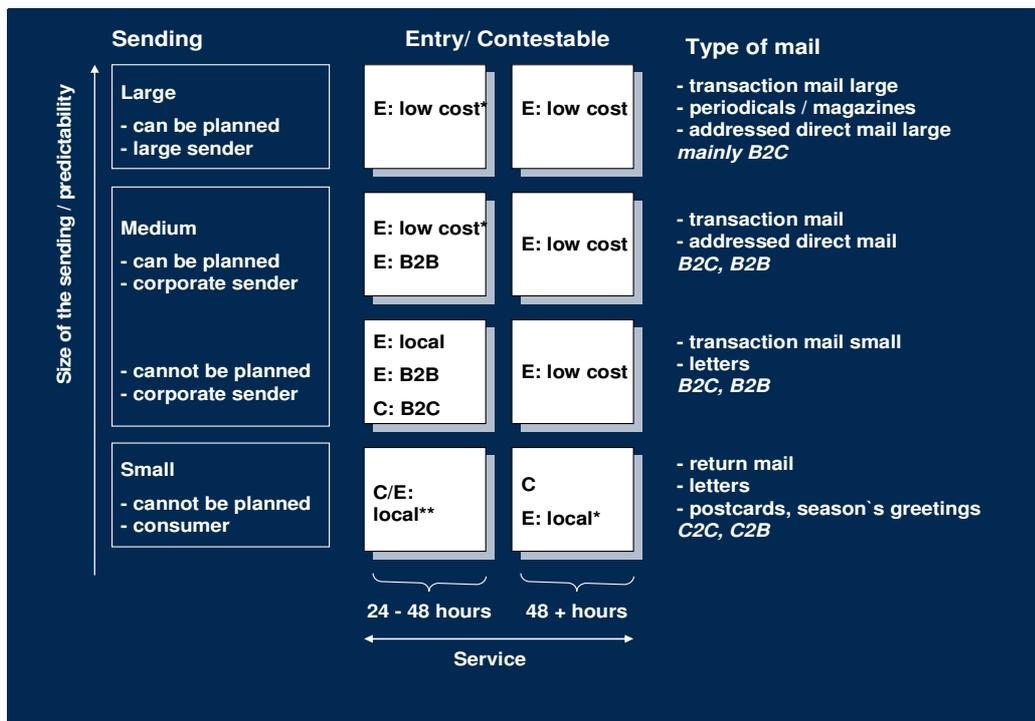
6.6.1 Entry, contestability, and type of postal operators active on the market

Figure 6.3 shows our assessment of likely entry and contestability of market segments using the same market segmentation as in the section on the preliminary assessment of contestability of market segments in Chapter 3. Note that this analysis as well as the discussion in this section focuses on business models that develop their own delivery network. Obviously, all market segments in which we expect entry are contestable as well.

Denoting the upper left segment, segment I, the upper right segment II and so on (see also Figure 3.3 in Section 3.3) entry by low cost models is firstly expected in segments II and IV (B2B and B2C mail that can be pre-sorted and planned in advance with a 48+ hours service level) and possibly in segment VI as soon as sufficient mail volumes have been acquired, provided that some investments in sorting equipment will be made. Entry can also be expected in segments I and III, but this requires adaptations either by the competitor postal operator (more frequent delivery to offer a 24/48 hours service level) or by the customer (adapting the moment that mail is produced). Entry in segment V (individual business mail that requires a 24/48 hours service level) is only expected for B2B and in local markets. However, this market segment is contestable, as low cost operators may enter this market segment if the national postal operator is not efficient or delivering a reliable service.

⁷⁹ The prime difference between cost plus and retail minus access tariffs is that in the former tariff no compensation is included for the fixed costs of the network of the national postal operator upstream of the point of access.

Figure 6.3 Contestability (C) and expected entry (E) in market segments



Note: E (: low cost) denotes that entry is likely in this market segment by a low cost operator. * indicates that entry requires adaptations either by the competitor postal operator (more frequent delivery) or by the customer (adapting the moment that mail is produced). ** Only potential and actual entry in local markets.

Segments VII and VIII, the collection and delivery of consumer mail, both have natural monopoly characteristics. In segment VIII, consumer mail that is not time sensitive, we expect entry at local levels but not on a national scale. In addition to the investments needed in sorting equipment for entering segment VI, also a dense collection network should be developed. Entry is easier to organise for the Season’s Greetings in the short period around Christmas and New Year. The segment is anyhow contestable however, as the sunk costs for the needed investments are limited and entry is potentially possible. Finally, in segment VIII we also expect entry only to take place at local level. We regard this segment in practice not contestable. The only exception is the case that the competitor postal operator will outperform the national postal operator and will develop a full service model basically replacing the national postal operator.

Given the importance of economies of density and the need for a sufficient mail volume to become an efficient postal operator, there is limited room for low cost and full service operators. It is expected that in most of the Member States in addition to the national postal operators not more than one or two postal operators will operate a low cost model or, in case of an inefficient national postal operator, possibly a full service model with a delivery network covering the entire country. In addition to these operators, a small number of low cost operators with a smaller network (active in only part of the country) and a larger number of players targeting at niche markets and local markets will be active as well. The choice for relatively favourable access conditions in the UK will most likely deter the development of a parallel delivery network and the emergence of low cost operators.

In Finland and Sweden, large countries with a very low population density, a competitor with a national covering delivery network may not emerge and may be confined to the larger cities and more densely populated part of the country. For example, CityMail, the main competitor of Sweden Post, is not aiming to reach national coverage. Also in the countries where the potential for the development of competition is relatively low (Cyprus, Estonia, Greece, Ireland, Latvia, and Lithuania) there may not emerge a low cost operator with a nation wide delivery network. The economics of postal service provision may not allow for two operators operating a nation wide delivery network profitably at the same time. In these countries we expect competition in value added services and in niche markets and local or regional markets. However, on the other extreme, if the national postal operator does not manage to work efficiently and deliver good service, the possibility exists that a new entrant can eventually outperform the national postal operator and takes its place

From a European perspective, the concentration process in the EU letter mail market that already started will continue leading to a limited number of leading Pan-European postal operators, supplemented with a larger number of regional postal operators and a larger group focusing on their home markets.

6.6.2 Expected effect on market structure

In most cases, the national postal operators are expected to preserve their dominant position in their home markets and in general a market structure resembling an oligopoly will emerge. The market share of the national postal operators for the delivery of addressed mail is expected to become around 60-90% in the medium term. The market share will be highest (close to 100%) for consumer mail requiring next day (or D+2, depending on the service level in the country) delivery, relatively high (80-95%) for individual business mail requiring next day delivery and non time sensitive consumer mail, a bit lower but still high for bulk mail that needs next day delivery and individual business mail that is not time sensitive, and lowest for addressed bulk mail that can be planned in advance and is not time sensitive. For the latter type of mail the market share of the national postal operator may well fall to levels like 30-50% if credible competitor postal operators will have made an entry to the market.

The market shares that national postal operators can retain further related whether or not uniform tariffs will be still imposed as part of universal service, in particular for bulk mail. In general, it is for competitors easier to gain market share if there are uniform tariffs than if there are no uniform tariffs.

In sum, the national postal operator is expected to preserve their dominant position and in general a market structure resembling an oligopoly will emerge. This however does not preclude the development of effective competition on the postal markets. First, most market segments are contestable and all postal operators face the risk of new competitors entering the postal industry. Second, both the threat of potential substitutes and the bargaining power of large customers pose real constraints on the behaviour of postal operators and positively influence the level of competition on the market.

6.6.3 Expected effect on services

The customer orientation of the postal operators is expected to (further) improve and the number of different services is expected to grow. Both value added services will be more strongly developed and the quality of service better related to the needs of the customer. A clear differentiation of service levels is foreseen (like quick and reliable, normal, and slow and cheap).

New technologies will be developed and employed, in particular in relation with developments in electronic communication. Developments that can be felt the last decade are likely to continue.

The increasing range of value added services will be mainly developed for B2X, such as:

- Other sorting concepts;
- Data management of addresses and mail room management;
- Hybrid mail, computer generated business mail, letter preparation;
- Mail consolidation;
- Track & trace, 2nd delivery.

6.6.4 Expected effect on prices

In general it is expected that prices of postal products will become more related to the underlying cost structure of these products. Further, the competitive pressure on prices will be relatively high for segments where competition is expected to take off and relatively low for segments where this is not the case.

The expected effect on the prices for addressed bulk mail is that they will go down or that they will stay at competitive level. This market segment is very attractive directly after liberalisation, but new entry will have a downward effect on prices and likewise a downward effect on the margins that can be made in this market segment. Moreover, the risk of potential entry is relatively high as well as the bargaining power of large customers. Participants of the opinion survey expect on average the prices may go down by 10-15% (see Box 6.1 for a short summary and Annex I, appendix 5, for the complete results of the opinion survey). Evidence in Sweden and the Netherlands indicate that prices may go down even a bit further. In countries that currently have a uniform tariff for the delivery of bulk mail and where the cost of delivery in rural areas is substantially higher than in urban areas, the expected price decreases for the delivery of bulk mail in urban areas will be relatively high and may reach levels of 20-25%.

Q1: In which markets or market segments will entry, with competition as a result, be most likely?

Entry is most likely in the B2X segment and within that segment in addressed letter mail as well as in advertising mail. The B2C segment appears to be the most attractive due to higher volumes in that specific market segment. For some entrants, B2B may, nevertheless be attractive as less investment is required to build up a distribution network. The same reasoning applies for the low attractiveness of the C2X market segment: apart from a delivery network, a collection network has to be built as well. International mail is generally limited in volume; therefore, it is not a very attractive segment to be active in, unless a delivery system in other countries is present, e.g., in the case of foreign incumbent operators. The possibility to offer services of 'lower' quality (like slow delivery) is attractive for both businesses (lower prices) and for postal operators (requires a less extensive network). A less extensive network may take the form of a more labour-intensive production process (e.g., manual sorting), less frequent delivery, etc. Such a network would be considerably cheaper.

Q2: What will be the market shares of new competitors in these market segments?

Market segment	B2B	B2C	C2B	C2C
Items of correspondence	40%	30%	5-10%	
Advertising mail	35-40%	30%		
International mail	70%			
Total market	10-40% (depends on timing)			

If the requirement for uniform pricing is abolished the market share of competitors is likely to grow less. Providing second round feed-back, a small number of respondents points out that the percentages for B2B, C2X, and international mail should be lower. Some respondents argue that these numbers are only feasible with well-designed access regulations.

Q3: What will the consequences for prices be? Can you explain your answer in more detail?

Market segment	B2B	B2C	C2B	C2C
Items of correspondence	-10%		Prices are not likely to fall, may even go up. This holds for households and SMEs	
Advertising mail	-15%			
International mail	In some countries, large potential for decrease, in others hardly any potential			

The behaviour of the regulator will have an important impact on prices, felt predominantly in the C2X segment. Also important is whether or not a differentiation of prices throughout the country is allowed.

Q4: What will the consequences for the supply of value added services be?

Currently, incumbents (especially in countries with a less developed mail, or more in general, services sector) do not offer the full range of services that business customers are interested in. Hence, more VA services will be offered as a result of liberalisation, mostly in the B2X segment. This broader range of services includes services across various dimensions, like slow service, guaranteed overnight delivery, flexibility, track-and-trace service, urgency, registered mail, 2nd daily delivery, mail room management, archiving, letter preparation, address checking, consolidation, hybrid mail.

Prices for consumer mail, in particular the mail requiring next day delivery, will not go down and may rise instead. New entry is not expected, and certainly not in the short term, but the potential of substitution (through internet and other means of communication) poses a certain disciplinary force on the pricing policies of the national postal operators. Another reason for the tendency of the prices of consumer mail to go upward, is that after liberalisation there is much less room for cross subsidising consumer mail by the income generated from business mail. The prices for consumer mail falling under the universal service obligations will most probably continue to be regulated, but also in this case there will be pressure on the regulator to (eventually) accept price rises.

There will also be a pressure to raise prices for individual business mail requiring next day delivery, but this pressure is less than for consumer mail. The prices for non time sensitive individual business mail will probably go down, but less than for bulk mail, in particular if actual entry on this segment will take place or if small business mailers can make use of services of mail consolidators for (part of) their mail.

6.6.5 Expected effect on the universal service provision

What is the expected effect of full liberalisation on the universal service provision? In other words, will it be possible to offer a basic package of services of good quality to everyone for (possibly) uniform, affordable prices in a profitable manner? The answer to the last question will be most probably yes for some countries like for example Sweden and the Netherlands but is less clear for other countries.

More in particular the answer to the above questions depends on the exact form that the universal service and the universal service obligations will have in future. In general there is a relation between the development of competition and the provision of the universal service that is briefly discussed below.

If the definition of the universal service remains unchanged

One of the reasons for preserving an area that is reserved to the national postal operator was that in this way the national postal operator could generate sufficient mail volumes for profitably providing the universal service. The losses of mail volumes of the national postal operators will vary between the Member States as well as the general cost of postal service provision. The results on the financial results remain to be seen keeping in mind that the national postal operators will most probably remain the only operator with a full service model that is attractive to a large group of customers.

Having said this, the funding of the universal service obligations is in this situation under relative pressure and related to the efficiency and product range of the national postal operator. This pressure is also related to the per capita mail volumes that the national postal operators are handling at the moment: with relatively low mail per capita volumes, losses in mail volumes have a relatively strong (upward) effect on the average cost of mail handling. Both the playing field that is not level (to the detriment of the national postal operator in this case) and the form in which any universal service burden is shared have an impact on the development of competition as previous sections have shown. For example, the distortions to competition are minimised if general tax income (and not a

specific tax levied on certain companies or certain postal products) would be used to finance a compensation fund or provide the funds for a direct contract with a postal operator to ensure the provision of certain of the universal services.

If the universal service would be limited to the (overnight) delivery of single item mail

The funding of the universal service is still under pressure compared to the current day situation, but less than above. The way how the universal service funding would be shared becomes less important for competition. A limitation of the universal service universal service to the (overnight) delivery of single item mail would make the playing field more level than if the current definition is maintained.

If the universal service universal service is limited to 2-3 times per week delivery

In this case the problems with funding the universal service would be minimal if at all existing. Sharing funding the universal service is not an issue anymore. If the universal service is limited to 2-3 times per week delivery there would in effect be a level playing field in this respect and the development of competition wide open. It will have a (further) upward price effect on overnight mail for small mailers. This scenario seems rather unlikely at the moment given the resistance by different stakeholders.

We do not think that decreasing the scope of the universal service obligations will have a negative effect on overall mail volumes because lower service levels would be offered and substitute products become more attractive. First, it is to be expected that the delivery frequency will in most Member States not go down and that first class delivery will still be offered, also when it is not required in a universal service obligation. Second, the expected lower prices for second class mail may well generate the opposite effect and may improve (for example) the position of direct mail vis-à-vis other channels for marketing.

6.7 Summary and conclusion

The main drivers for competition will change after liberalisation. They will no longer be strongly influenced by the regulatory framework and in particular the extent to which market segments are liberalised but will be geared at grasping the opportunities and synergies that can be obtained in the postal market. Also the position of many national postal operators will change from a defensive strategy to a more offensive strategy. The background to these changes is an addressed mail market that in most countries will show a moderate decline or be stable at best and continuing technological developments that influence the production process in the mail market.

6.7.1 Pattern and scale of competitive entry

The (non exclusive) business models that we observe at the moment and expect for the future can be classified as:

- Full service providers;
- Low cost providers operating in certain market segments or certain geographical areas (focusing on addressed bulk mail and/or networks of local operators);

- Providers offering services in part of the value chain (consolidators, upstream operators, downstream operators);
- Providers of services in niche markets (heavy documents, document exchange, same day delivery in urban areas, spot operators).

Activities in niche markets and in local markets will be undertaken by a relatively large number of operators but will in itself not pose a real competitive threat to the national postal operators in their home markets. The combined market share that these operators will achieve in the addressed mail market will remain relatively modest because of the fact that these operators target only part of the market and that most customers ask for a full chain of postal services that these players are unable to offer.

It is not expected that, apart from isolated cases, competitor postal operators will develop into national full service providers. This strategy is only profitable in countries where the national postal operator provides low quality services.

Much more likely business models that will be employed are low cost models focusing on addressed bulk mail not requiring next day delivery and the establishment of interregional networks that exchange mail between more or less independent local operators. The delivery frequency is expected not to exceed 2-3 times per week. Many of the existing competitor postal operators are pursuing this strategy. Although these models do not target the entire market for addressed mail, they pose a competitive threat to the national postal operator and are in principle able to capture a substantial share of the market. The same applies for models focusing on last mile delivery by entrants that already have developed a delivery network through their activities in un-addressed mail or in magazines and periodicals (publishers).

Mail consolidation and a focus on upstream activities in general are also business models that can be observed in practice and are likely to be employed. The nature and magnitude of these models depend on the access conditions for the final delivery of mail and, for mail consolidation, on the level of price discrimination between small and large senders of mail.

Favourable access conditions will in general delay the development of low cost delivery models, in particular if such access is possible at the time that no parallel delivery networks for addressed mail delivery have (yet) been developed. Although some value added will be lost for in potential substantial mail volumes, these models may be less threatening to the national postal operator (as final delivery is more likely retained) than the low cost models, depending on the anticipated impact of these low cost models on its market share and revenues.

The new entrants employing these business models will be both national and international companies that, in particular for the low cost models, have some sort of delivery network already and can establish such a network by involving a variety of existing companies. The likely national new entrants into addressed mail at the national level are publishers, un-addressed mailers and new postal operators targeting specific mail flows requiring limited investments and a small network. Express companies are not expected to enter into the addressed mail market with the possible exception of outbound cross border mail.

The likely international new entrants are mainly the national postal operators that have adopted a pan-European or global strategy and operators that are pursuing a regional strategy. The former group of companies, most of all DPWN and TNT, will target countries with high mail volumes and countries and market segments with substantial unfulfilled demand. The strategy for the other smaller countries will be to engage in high end value added services. The latter group of companies will focus their attention on their neighbouring countries. It is further expected that these entrants are not interested into developing niche markets or local markets.

The scale of competitive entry and, more generally, the competitive pressure that is posed on the national postal operator through existing competitor postal operators, expected entry and the threat of new competitors entering the market will vary from country to country. In other words, it is expected that effective competition will develop at different speed in the Member States.

We examined these country differences by looking at their respective total addressed mail volumes, per capita addressed mail volumes, the potential for growth in direct mail volumes, the degree of urbanisation and the population density. When relatively high, these factors have a positive impact on the business case of new entrants by making it relatively easy to secure sufficient volumes to operate their networks in a profitable manner.

Existing competitor postal operators that are (partly) owned by one of the (major) national postal operators may profit from the reputation of the mother company, its international network, its expertise in running a business in the postal sector and its support with human resource management and staff training. The existence of such competitor postal operators is conducive to the development of competition. This factor was taken into account as well.

A summary score for the speed and intensity of the level of competition in the medium term was obtained, disregarding any remaining differences between the Member States regarding other barriers to entry that may continue to exist.

Based on this analysis we expect that, disregarding any remaining barriers related to the existence and application of country specific regulation, the potential for the development of competition in a liberalised environment in the medium term will be:

- Highest in Belgium, France, Germany, the Netherlands and the UK;
- Relatively high in Denmark, Italy, Luxembourg, Spain and Sweden;
- Moderate in Austria, Czech Republic, Finland, Hungary, Malta, Poland, Portugal, Slovakia, and Slovenia;
- Relatively low in Cyprus, Estonia, Greece, Ireland, Latvia, and Lithuania.

6.7.2 Entry, contestability and effect of liberalisation on market structure

Entry by low cost models is firstly expected in B2B and B2C bulk mail that can be pre-sorted and planned in advance with a 48+ hours service level and possibly for individual business mail as soon as sufficient mail volumes have been acquired, provided that some

investments in sorting equipment will be made. Entry can also be expected in bulk transaction mail with a 24/48 hours service level, but this requires adaptations either by the competitor postal operator (more frequent delivery to offer a 24/48 hours service level) or by the customer (adapting the moment that mail is produced). Entry in the delivery of individual business mail that requires a 24/48 hours service level is only expected for B2B and in local markets. However, this market segment is contestable, as low cost operators may enter this market segment if the national postal operator is not efficient or not delivering a reliable service.

The collection and delivery of consumer mail has natural monopoly characteristics. For consumer mail that is not time sensitive, we expect entry at local levels but not on a national scale. In addition to the investments needed in sorting equipment for entering the individual business mail segment, also a dense collection network should be developed. Entry is easier to organise for the Season's Greetings in the short period around Christmas and New Year. The segment is anyhow contestable however, as the sunk costs for the needed investments are limited and entry is potentially possible. Finally, for consumer mail requiring a 24/48 hours service level we also expect entry only to take place at local level. We regard this segment in practice not contestable. The only exception is the case that the competitor postal operator will outperform the national postal operator and will develop a full service model basically replacing the national postal operator.

Given the importance of economies of density and the need for a sufficient mail volume to become an efficient postal operator, there is limited room for low cost and full service operators. It is expected that in most of the Member States in addition to the national postal operators not more than one or two postal operators will operate a low cost model or, in case of an inefficient national postal operator, possibly a full service model with a delivery network covering the entire country. In addition to these operators, a small number of low cost operators with a smaller network (active in only part of the country) and a larger number of players targeting at niche markets and local markets will be active as well. The choice for relatively favourable access conditions in the UK will most likely deter the development of a parallel delivery network and the emergence of low cost operators.

In Finland and Sweden, large countries with a very low population density, a competitor with a national covering delivery network may not emerge and may be confined to the larger cities and more densely populated part of the country. For example, CityMail, the main competitor of Sweden Post, is not aiming to reach national coverage. Also in the countries where the potential for the development of competition is relatively low (Cyprus, Estonia, Greece, Ireland, Latvia, and Lithuania) there may not emerge a low cost operator with a nation wide delivery network. The economics of postal service provision may not allow for two operators operating a nation wide delivery network profitably at the same time. In these countries we expect competition in value added services and in niche markets and local or regional markets. However, on the other extreme, if the national postal operator does not manage to work efficiently and deliver good service, the possibility exists that a new entrant can eventually outperform the national postal operator and takes its place

Overall, the national postal operators are expected to preserve their dominant position in their home markets and in general a market structure resembling an oligopoly will emerge. The market share of the national postal operators for the delivery of addressed mail is expected to become around 60-90% in the medium term

The market shares that national postal operators can retain further relate to whether or not uniform tariffs will be still imposed as part of universal service, in particular for bulk mail. In general, it is for competitors easier to gain market share if there are uniform tariffs than if there are no uniform tariffs.

From a European perspective, the concentration process in the EU letter mail market that already started will continue leading to a limited number of leading Pan-European postal operators, supplemented with a larger number of regional postal operators and a larger group focusing on their home markets.

6.7.3 Expected effect on market performance

The customer orientation of the postal operators is expected to (further) improve and the number of different services is expected to grow. Both value added services will be more strongly developed and the quality of service better related to the needs of the customer. A clear differentiation of service levels is foreseen (like quick and reliable, normal, and slow and cheap). New technologies will be developed and employed, in particular in relation with developments in electronic communication. The increasing range of value added services will be mainly developed for B2X, such as new sorting concepts, data management of addresses and mail room management, hybrid mail, computer generated business mail, letter preparation, mail consolidation, track & trace and 2nd delivery.

In general it is expected that prices of postal products will become more related to the underlying cost structure of these products. Further, the competitive pressure on prices will be relatively high for segments where competition is expected to take off and relatively low for segments where this is not the case.

The expected effect on the prices for addressed bulk mail is that they will go down or that they will stay at competitive level. Participants of the opinion survey expect on average the prices may go down by 10-15%. Prices for consumer mail, in particular the mail requiring next day delivery, will not go down and may rise instead. There will also be a pressure to raise prices for individual business mail requiring next day delivery, but this pressure is less than for consumer mail. The prices for non time sensitive individual business mail will probably go down, but less than for bulk mail, in particular if actual entry on this segment will take place or if small business mailers can make use of services of mail consolidators for (part of) their mail.

The expected effect of full liberalisation on the universal service provision depends on the exact form that the universal service and the universal service obligations will have in future. Although in countries like the Netherlands and Sweden the universal services may be provided in a profitable way, the funding of the universal service obligations is under relative pressure if the definition remains unchanged. Both the playing field that is not

level (to the detriment of the national postal operator in this case) and the form in which any universal service burden is shared have an impact on the development of competition.

The funding of the universal service is still under pressure if the universal service would be limited to the (overnight) delivery of single item mail compared to the current day situation, but less than above. The way how the universal service funding would be shared becomes less important for competition. A limitation of the universal service to the (overnight) delivery of single item mail would make the playing field more level than if the current definition is maintained.

If the universal service is limited to 2-3 times per week delivery the problems with funding the universal service would be minimal if at all existing. Sharing funding the universal service is not an issue anymore.

It is not expected that decreasing the scope of the universal service obligations will have a negative effect on overall mail volumes. First, it is to be expected that the delivery frequency will in most Member States not go down and that first class delivery will still be offered, also when it is not required in a universal service obligations. Second, the expected lower prices for second class mail may well improve (for example) the position of direct mail vis-à-vis other channels for marketing.

7 Conclusion

7.1 Introduction

In this chapter we present the main conclusions on the current and expected development of competition in the European postal sector. Below, we present a summary of the main findings and conclusions and, finally, our overall conclusion and recommendations.

7.2 Summary of main findings and conclusions

7.2.1 Postal products and market segmentation

The postal market can be segmented along different dimensions that reflect the characteristics of postal service provision and form the basic ingredients of a variety of strategies and business models that can be chosen by new and existing postal operators. The most important of these dimensions are postal products, the nature of the sender and receiver of mail, time sensitivity and predictability of mail flows and the size of the mail sending.

In statistical publications and reports, different definitions are often used posing challenges to data collection and making comparisons between data sources and countries far from a straightforward exercise. In this report *letter mail* comprises of items of correspondence, addressed printed matter, newspapers and un-addressed printed matter with a weight of maximum two kilograms per item and adhering to certain restrictions with regard to size. *Items of correspondence* include personalised letters and postcards as well as transaction mail such as bank statements. *Addressed printed matter* comprises of direct mail, catalogues, magazines and periodicals. *Addressed mail* refers to items of correspondence plus addressed printed matter. The often used term *advertising mail* does not fully comply with these definitions, but includes a large part of the direct mail, certain catalogues and sponsored magazines. Addressed advertising mail hence largely equals addressed printed matter. In addition, a further separation between national and international mail and an extension to value added services like hybrid mail and logistic services is possible.

Historically, parcel mail and express and courier services are considered part of the postal sector. *Express and courier services* concern value added services with door-to-door delivery. During the last decades, express and courier services developed into a separate industry. *Parcel mail* concerns items above 2 kilograms with a maximum of 20 kilograms and items below 2 kilograms that do not adhere to the size restrictions for letter mail.

Parcel mail has become less specific to the postal sector, as it is also handled by the express and logistics industry in addition to mail order companies and postal operators.

7.2.2 Liberalisation of postal markets until date

The liberalisation of postal markets until date differs markedly for the different Member States, although all of them have embarked on implementing the postal directives. Liberalisation is most advanced in Estonia, Finland and Sweden that have fully liberalised their postal markets. Germany, the Netherlands, Slovakia and the United Kingdom have taken decisions to follow suit in the near future, a couple of years earlier than the possible date for full liberalisation set in directive 2002/39/EC. Also Norway, neighbouring the European Union, has taken this decision.

A second group of countries have liberalised a relatively large segment of the mail market (up to circa 50% of the total addressed mail volume), in particular countries that have liberalised both the delivery of direct mail and outgoing cross border mail (Czech Republic, Germany for direct mail batches above 50 items, the Netherlands, Slovenia, and Spain). Particular cases are Denmark that has liberalised the delivery of items of correspondence and direct mail above 50 grams, Spain that has never included intra-city mail in the reserved area and the United Kingdom that has liberalised the delivery of bulk mail.

Some countries take an intermediate position by either liberalising direct mail (Italy), outgoing cross border mail (Austria, Belgium, France, Ireland, Lithuania), or incoming cross border mail (Slovakia). The other nine Member States have maintained a large reserved area of around 80% to more than 90% of the total volume of addressed mail and have not (apart from magazines and periodicals) liberalised the delivery of addressed mail below 100 grams for any of the postal products. From this group, Poland has a transitional regime reserving the delivery of mail below 350 grams to the national postal operator.

7.2.3 General development of internal competition until date

The market shares of the competitor postal operators in addressed mail delivery are still very small. The countries that have liberalised a relatively large part of the addressed mail segment show the highest market share for competitor postal operators: this market share is around 7-11% for Spain, 5-7% for Czech Republic, Estonia, the Netherlands, and Sweden, and 3-5% for Denmark and Germany.

In the other countries there have not emerged competitor postal operators that are challenging the position of the national postal operator until date. In general it can be concluded that the liberalisation of addressed mail above 100 grams is insufficient for the development of any meaningful competition if this is not accompanied with the complete liberalisation of the delivery of certain postal products with substantial market volumes.

The United Kingdom and France have a somewhat special position with regard to the development of competition. In both countries, competition in end-to-end services is very limited until date. France has maintained a relatively large part of addressed mail delivery in the reserved area but has liberalised the upstream market a long time ago. Mail consolidation has developed rather strongly here, with mail consolidators and large customers having three points of upstream and downstream access for final delivery by La Poste. In the United Kingdom the delivery of bulk mail has been liberalised in 2000 and in the beginning of 2004, after a period of negotiations, an access agreement was reached between Royal Mail and three competitor postal operators. Although the volume of mail handled by these competitors has grown considerably during the last year (UK Mail alone handled more than 23 million items in the first half a year since May 2004 and in March 2005 was already handling 250 million items on an annualised basis), the final delivery is undertaken by Royal Mail.

7.2.4 Strategies of postal operators

The empirical evidence shows that there is a large variety of business models that are used by competitor postal operators. These business models vary as much within one country as between the Member States. All these business models have in common that they differ markedly from the business model of the national postal operator and that the size of the networks that they have developed is substantially smaller than the size of the networks of the national postal operators. This observation supports the view further touched upon below that for these cases sufficient economies of density can be obtained as long as the network size is kept relatively small.

Although data on the financial results of competitor postal operators are often not available, it appears that most of these operators need 3-5 years before they start to make the first profits. The results of companies that focus on the B2X market segments and have developed a network for two times per week delivery, like Sandd and Selekt Mail in the Netherlands and CityMail in Sweden, show that in these countries a 2-5% market share in the addressed mail market (involving the delivery of 100-200 million mail items) is sufficient to break even. Companies that focus on the B2B market segment (such as MailMerge and BusinessPost in the Netherlands) or on (other) niche or local markets need significantly less volume to break even.

Competitor postal operators that fully rely on access for final mile delivery need less time, probably only 1-3 years. The investments needed for the business model taken by UK Mail that fully relies on Royal Mail for the final mile delivery are clearly less than the investments needed if a parallel delivery network is developed. As a consequence, the point to break even is more easily reached.

The strategies of the national postal operators are influenced by a number of relevant developments: the traditional revenue base is getting smaller, the prices for bulk mail are under pressure, in particular in countries that have liberalised large segments of the letter mail market, the financial results of quite some national postal operators show (with a couple of notable exceptions) rather limited returns on sales, and the competition from the communication and advertising sectors as well as the needs of the customers require the

continuous development of new products and processes. The effect of the above developments is that there is a general need to improve the efficiencies in postal service provision and to broaden the revenue base, either in the domestic market (value added services, express, logistics, and/or financial services) or internationally (mainly express, logistics, and activities on foreign letter mail and parcel mail markets) or both. Often substantial investments are needed to achieve this and in many cases these can only be realised through attracting capital from outside.

Further, in certain market segments of the domestic market it is most effective to compete through subsidiary companies that are run separately and use their own network. This is the case for the delivery of un-addressed mail and mail consolidation (for example, the French consolidators Datapost, Mikros and Dynapost are subsidiaries of La Poste), but not yet implemented for the delivery of for example addressed bulk mail (TNT announcing that in future it may use Netwerk VSP for delivering addressed bulk mail in the Netherlands in addition to un-addressed mail that Netwerk VSP is delivering currently is the first sign that a subsidiary will become active on this market segment as well).

The effect of the above developments is that there is a general need to improve the efficiencies in postal service provision and to broaden the revenue base, either in the domestic market (value added services, express, logistics, and/or financial services) or internationally (mainly express, logistics, and activities on foreign letter mail and parcel mail markets) or both. Often substantial investments are needed to achieve this and in many cases these can only be realised through attracting capital from outside.

By far the most active players on the addressed mail markets in the Member States are TNT (the Netherlands) and DPWN (Germany). Through joint ventures and takeovers of competitor postal operators that entered into the market these companies have secured positions in the addressed mail markets in each others markets as well as in total in eight other Member States. Both are searching for possibilities for joint ventures and takeovers and are not considering Greenfield investments to establish competing collection and delivery networks from scratch.

DPWN and TNT also showed interest in buying the stakes in the national postal operators of Austria, Belgium and Denmark that were announced for possible sale, but this did not materialise for several reasons. Eventually, the UK investment firm CVC Capital Partners acquired a 22% stake in Denmark Post. The capital injection will enable Denmark Post to invest into diversifying its revenue base and will most likely strengthen its position towards internal competitors and the national postal operators in the region. Apart from providing capital, a strategic investor like CVC Capital Partners can support in general management, but it does not necessarily provide strengthening of best practice postal management. The question remains if they will have a longer term contribution to postal sector restructuring or provide mainly mid-term solutions to prepare postal operators for future full privatisation.

From a company wide perspective and including the operations in express and logistics, DPWN, La Poste, Royal Mail and TNT are pursuing a pan-European or global corporate strategy. A number of other national postal operators seem to pursue a regional strategy (in particular the Nordic countries Denmark, Estonia, Finland and Sweden as well as the

Central European countries Austria and Slovenia) and the majority a strategy focusing on their home markets more or less exclusively, at least for the time being.

7.2.5 Key factors influencing the development of competition until date

A number of key factors appear to influence the development of competition until date, each of which is discussed below.

Natural barriers to entry

Natural entry barriers are related to the economics of the postal market and cannot, unlike legal or strategic entry barriers, easily be influenced or be taken away by liberalisation, regulation or decisions by the postal sector regulator or the competition authority. This set of entry barriers will continue to exist after the complete liberalisation of the postal sector and ultimately determine whether market segments are contestable or not. Natural barriers to entry are related to both the demand side and the supply side of the postal market.

The analysis of the *demand side* of the letter mail market shows that the demand side put a number of restrictions on the development of competition, but also create a number of important opportunities for new entrants, not at least because of the considerable expenses that large customers incur for postal services. Reputation and portfolio effects pose challenges to competitors and imply that for a certain type of large customers the national postal operator or a competitor postal operator linked to one of the leading European postal operators has a competitive edge over other competitor postal operators. For other customers an internationally operating postal operator can offer interesting business solutions and for handling international cross border mail postal operators with an international network have a competitive edge as well. This currently applies to not more than 5% of the addressed mail market but will become more important as a result of the increasing internationalisation of economic activities. The wish for an improved customer orientation and tailor made services as well as the general desire to have a choice between postal operators create opportunities for competition. Also a trade-off between price and quality (in terms of speed or frequency of delivery) is broadly accepted.

In general, customers demand an encompassing business solution and most ask for a full chain of postal services. Also the coverage of the delivery network is considered important by many. In a study of Berger (2004) among 549 business customers in the UK referred to in Chapters 4 and 5, the coverage of the delivery network is almost three times as important as the reputation of the postal operator, price, and the conditions for delivery and collection (the relative importance of the last four attributes being almost the same). Still, there is room for local and regional operators, as around 20% of the respondents send their mail mainly to specific regions and 41% of the mailings are posted and delivered within 50 miles.

The most important *supply side* natural entry barrier is the importance of economies of density that apply to all parts of the postal supply chain. Economies of density are obtained because the average cost of mail handling decreases when mail volumes rise

given a fixed size of the network. In contrast, economies of scale refer to the cost advantages that can be achieved by increasing the network size and the mail volume that is processed through this network at the same rate (this distinction between economies of density and scale is particularly relevant for network industries).

The entry of competitor postal operators and the business models that they employ support the results of an earlier study by NERA (2004) that there are no economies of scale for end-to-end mail processing, at least not in the 'old' 15 Member States. An important implication of this result is that a competitor postal operator with a (considerably) smaller postal network can enjoy the same cost advantages based on economies of scale as the national postal operator, even at (considerably) lower mail volumes.

Economies of scope range from very low to high dependent on the combination of products offered through the same network. Economies of scope are particularly important for the products within the addressed mail segment (in particular between transaction mail that can be planned in advance, periodicals, magazines and addressed direct mail), but less for combining addressed mail and parcel delivery, addressed mail and un-addressed mail, and addressed mail and newspaper delivery, and virtually nonexistent for combining addressed mail and express delivery at a national level. At international level, however, a presence in express or logistics in a certain country offers opportunities for handling outbound B2X cross border mail as well.

Sunk costs of investments are not present in transport and delivery, but exist in sorting equipment and establishing a collection network, although these depend on the business model chosen. It is in our view fair to conclude that the postal sector is not characterised by the existence of substantial sunk costs of investment.

Legal barriers to entry

The fact that 50% to over 80% of the delivery of addressed mail is still reserved to the national postal operators has been the most important legal entry barrier to date. An important implication of the reserved area that acted as a barrier to the development of competition is that competitor postal operators are hampered in their ability to offer a comprehensive business solution to their customers. This means that, even in the liberalised mail segments, it is difficult to gain market share. In Member States where the liberalisation of the postal market is confined to the delivery of addressed mail above 100 grams, in fact only competition in niche markets is possible. In the UK, the liberalisation of bulk mail consignments of more than 4,000 items in fact means that a business model focusing on firstly establishing a position on the B2B market segment is practically impossible, because B2B mailings are predominantly below 4,000 items. The business model should focus on the B2C segment with nation wide delivery although the liberalised market segment only covers around one third of the addressed mail volumes. Developing a parallel delivery network under these conditions is very difficult, partly explaining why a number of competitors have sought access to the delivery network of Royal Mail. The full liberalisation of the delivery of addressed direct mail offers much better opportunities for new entrants to offer a comprehensive business solution for their prospective clients, as witnessed by the fact that competition is taking off in particular in

the countries that have liberalised this market segment (such as in the Netherlands and in Spain and more recently in Czech Republic and in Estonia).

The main other legal barriers to entry that can be observed in the Member States at present or have caused a slowdown in the development of competition in the past are licence requirements that are overly restrictive for the business model that competitor postal operators can employ (such as in Estonia and Finland; the main restrictions relate to demanding [almost] national coverage and a high frequency of delivery), regulatory uncertainty in general and with regard to definitions in particular (creating uncertainty whether or not certain products are included in the reserved area or not), and the time that it has taken for competitors to obtain access to the P.O. Boxes and the redirection of mail.

Strategic barriers to entry

The behaviour of the national postal operators has resulted in a variety of strategic entry barriers including (attempted) predatory pricing, vertical foreclosure, litigation, use of trade marks, patent protection, and the practical (and changing) conditions under which access can be obtained. What can be generally observed is that the national postal operators try to protect their markets and deter entry as much as possible, in particular through raising non-price strategic barriers.

Absence of a level playing field

For a number of reasons there is not yet a level playing field. In many Member States competitor postal operators are in a worse position than the national postal operator because of the VAT exemptions that apply. Moreover, in countries as Austria, France and Poland the competitors do not have access to (part of) the private letterboxes, in particular in apartment buildings that have the letterboxes behind a closed front door. There is further not a level playing field between competitors and customers, as in many cases the non-discrimination clause is not applied. In effect, small mailers are in this case partially or fully deprived of the possibility to obtain better prices through mail consolidation. In turn, the business model of the national postal operators is restricted because of the universal service obligations and the principle of uniform prices for postal products in the entire country.

Dispute settlement

The issues mentioned above have given rise to a lot of disputes that have in general, by the opinion of the competitor postal operators, taken too much time to resolve. The most common disputes that are observed in many of the Member States relate to regulatory uncertainty (in particular the definition of postal products and whether or not these products are included in the reserved area), alleged predatory pricing and cross subsidisation by the national postal operators, and vertical foreclosure (alleged attempts of the national postal operators to protect the market through price discrimination, refusal to handle mail of competitor postal operators, and the access conditions for delivering mail for competitor postal operators). In some countries and in a number of cases the lack of an adequate regulatory framework and/or the absence of an independent postal regulator severely hampered the ability to deal with disputes appropriately. We do not want to suggest that the competitor postal operators are always right in these disputes, but do want to stress that timely resolving of any disputes very much contributes to reaching

the kind of regulatory certainty and transparency that is needed for the development of competition to take off.

7.2.6 Expected pattern of competitive entry in a liberalised environment

The main drivers for competition will change after liberalisation. They will no longer be strongly influenced by the regulatory framework and in particular the extent to which market segments are liberalised but will be geared at grasping the opportunities and synergies that can be obtained in the postal market. Also the position of many national postal operators will change from a defensive strategy to a more offensive strategy.

The (non exclusive) business models that we observe at the moment and expect for the future can be classified as:

- Full service providers;
- Low cost providers operating in certain market segments or certain geographical areas (focusing on addressed bulk mail and/or networks of local operators);
- Providers offering services in part of the value chain (consolidators, upstream operators, downstream operators);
- Providers of services in niche markets (heavy documents, document exchange, same day delivery in urban areas, spot operators).

Activities in niche markets and in local markets will be undertaken by a relatively large number of operators but will in itself not pose a real competitive threat to the national postal operators in their home markets. Examples of companies that currently are employing niche activities are ADREXO in France (direct marketing packages, heavy documents) and Hays in the UK (B2B document exchange). The combined market share that niche operators will achieve in the addressed mail market will remain relatively modest because of the fact that niche operators target only part of the market and that most customers ask for a full chain of postal services that these players are unable to offer. The study by Dietl and Waller (2001) indicates that in Germany operators offering only local mail services have in total access to about 30% of the addressed mail market and the study by Berger (2004, p.96) shows that only 14% of the UK respondents prefer a specialised (niche service) postal operator and 66% an operator offering the full chain of postal services (a full service or low cost operator).⁸⁰

It is not expected that, apart from isolated cases, competitor postal operators will develop into national full service providers. This strategy is only profitable in countries where the national postal operator provides low quality services.

Much more likely business models that will be employed are low cost models focusing on addressed bulk mail not requiring next day delivery and the establishment of interregional networks that exchange mail between more or less independent local operators. The delivery frequency is expected not to exceed 2-3 times per week. Many of the existing competitor postal operators are pursuing this strategy, such as Sandd and Selekt Mail (the Netherlands), CityMail (Sweden), EP Europost (Germany) and Unipost (Spain). Unipost

⁸⁰ See Chapter 3, footnote 17, for the full references to these studies.

is a good example of competition through establishing interregional networks, but also the other mentioned companies cooperate with local partners and have outsourced part of their activities. Although these models do not target the entire market for addressed mail, they pose a competitive threat to the national postal operator and are in principle able to capture a substantial share of the market. The same applies for models focusing on last mile delivery by entrants that already have developed a delivery network through their activities in un-addressed mail or in magazines and periodicals (publishers).

Mail consolidation and a focus on upstream activities in general are also business models that can be observed in practice and are likely to be employed. Examples are Dimar in the Czech Republic, a wide variety of mail consolidators in France (including subsidiaries of La Poste and DPWN that recently took over KOBA), and Mailland and Euromail in the Netherlands. The nature and magnitude of these models depend on the access conditions for the final delivery of mail and, for mail consolidation, on the level of price discrimination between small and large senders of mail. Favourable access conditions will in general delay the development of low cost delivery models, in particular if such access is possible at the time that no parallel delivery networks for addressed mail delivery have (yet) been developed. Although some value added will be lost for in potential substantial mail volumes, these models may be less threatening to the national postal operator (as final delivery is more likely retained) than the low cost models, depending on the anticipated impact of these low cost models on the market share of the national postal operator and revenues.

The new entrants employing these business models will be both national and international companies that, in particular for the low cost models, have some sort of delivery network already and can establish such a network by involving a variety of existing companies. The likely national new entrants into addressed mail at the national level are publishers, un-addressed mailers and new postal operators targeting specific mail flows requiring limited investments and a small network. Express companies are not expected to enter into the addressed mail market with the possible exception of outbound cross border mail.

The likely international new entrants are mainly the national postal operators that have adopted a pan-European or global strategy and operators that are pursuing a regional strategy. The former group of companies, most of all DPWN and TNT, will target countries with high mail volumes and countries and market segments with substantial unfulfilled demand. The strategy for the other smaller countries will be to engage in high end value added services. The latter group of companies will focus their attention on their neighbouring countries. It is further expected that these entrants are not interested into developing niche markets or local markets.

7.2.7 Expected scale of competitive entry in a liberalised environment

The scale of competitive entry and, more generally, the competitive pressure that is posed on the national postal operator through existing competitor postal operators, expected entry and the threat of new competitors entering the market will vary from country to country. In other words, it is expected that effective competition will develop at different speed in the Member States.

We examined these country differences by looking at their respective total addressed mail volumes, per capita addressed mail volumes, the potential for growth in direct mail volumes, the degree of urbanisation and the population density. When relatively high, these factors have a positive impact on the business case of new entrants by making it relatively easy to secure sufficient volumes to operate their networks in a profitable manner.

Existing competitor postal operators that are (partly) owned by one of the (major) national postal operators may profit from the reputation of the mother company, its international network, its expertise in running a business in the postal sector and its support with human resource management and staff training. The existence of such competitor postal operators is conducive to the development of competition. This factor was taken into account as well.

A summary score for the speed and intensity of the level of competition in the medium term was obtained, disregarding any remaining differences between the Member States regarding other barriers to entry that may continue to exist.

Based on this analysis we expect that, disregarding any remaining barriers related to the existence and application of country specific regulation, the potential for the development of competition in a liberalised environment in the medium term will be:

- Highest in Belgium, France, Germany, the Netherlands and the UK;
- Relatively high in Denmark, Italy, Luxembourg, Spain and Sweden;
- Moderate in Austria, Czech Republic, Finland, Hungary, Malta, Poland, Portugal, Slovakia, and Slovenia;
- Relatively low in Cyprus, Estonia, Greece, Ireland, Latvia, and Lithuania.

7.2.8 Entry, contestability and effect of liberalisation on market structure

Entry by low cost models is firstly expected in B2B and B2C bulk mail that can be pre-sorted and planned in advance with a 48+ hours service level and possibly for individual business mail as soon as sufficient mail volumes have been acquired, provided that some investments in sorting equipment will be made. Entry can also be expected in bulk transaction mail with a 24/48 hours service level, but this requires adaptations either by the competitor postal operator (more frequent delivery to offer a 24/48 hours service level) or by the customer (adapting the moment that mail is produced). Entry in the delivery of individual business mail that requires a 24/48 hours service level is only expected for B2B and in local markets. However, this market segment is contestable, as low cost operators may enter this market segment if the national postal operator is not efficient or not delivering a reliable service.

The collection and delivery of consumer mail has natural monopoly characteristics. For consumer mail that is not time sensitive, we expect entry at local levels but not on a national scale. In addition to the investments needed in sorting equipment for entering the individual business mail segment, also a dense collection network should be developed. Entry is easier to organise for the Season's Greetings in the short period around Christmas and New Year. The segment is anyhow contestable however, as the sunk costs

for the needed investments are limited and entry is potentially possible. Finally, for consumer mail requiring a 24/48 hours service level we also expect entry only to take place at local level. We regard this segment in practice not contestable. The only exception is the case that one of the competitor postal operators will outperform the national postal operator and will develop a full service model basically replacing the national postal operator.

Given the importance of economies of density and the need for a sufficient mail volume to become an efficient postal operator, there is limited room for low cost and full service operators. It is expected that in most of the Member States in addition to the national postal operators not more than one or two postal operators will operate a low cost model or, in case of an inefficient national postal operator, possibly a full service model with a delivery network covering the entire country. In addition to these operators, a small number of low cost operators with a smaller network (active in only part of the country) and a larger number of players targeting at niche markets and local markets will be active as well. The choice for relatively favourable access conditions in the UK will most likely deter the development of a parallel delivery network and the emergence of low cost operators.

In Finland and Sweden, large countries with a very low population density, a competitor with a national covering delivery network may not emerge and may be confined to the larger cities and more densely populated parts of the country. For example, CityMail, the main competitor of Sweden Post, is not aiming to reach national coverage. Also in the countries where the potential for the development of competition is relatively low (Cyprus, Estonia, Greece, Ireland, Latvia, and Lithuania) there may not emerge a low cost operator with a nation wide delivery network. The economics of postal service provision may not allow for two operators operating a nation wide delivery network profitably at the same time. In these countries we expect competition in value added services and in niche markets and local or regional markets. However, on the other extreme, if the national postal operator does not manage to work efficiently and deliver good service, the possibility exists that a new entrant can eventually outperform the national postal operator and takes its place

Overall, the national postal operators are expected to preserve their dominant position in their home markets and in general a market structure resembling an oligopoly will emerge. The market share of the national postal operators for the delivery of addressed mail is expected to become around 60-90% in the medium term

The market shares that national postal operators can retain further relate to whether or not uniform tariffs will be still imposed as part of the universal service obligations, in particular for bulk mail. In general, it is for competitors easier to gain market share if there are uniform tariffs than if there are no uniform tariffs.

From a European perspective, the concentration process in the EU letter mail market that already started will continue leading to a limited number of leading Pan-European postal operators, supplemented with a larger number of regional postal operators and a larger group focusing on their home markets.

7.2.9 Likely effect of liberalisation on market performance

The customer orientation of the postal operators is expected to (further) improve and the number of different services is expected to grow. Both value added services will be more strongly developed and the quality of service better related to the needs of the customer. A clear differentiation of service levels is foreseen (like quick and reliable, normal, and slow and cheap). New technologies will be developed and employed, in particular in relation with developments in electronic communication. The increasing range of value added services will be mainly developed for B2X, such as new sorting concepts, data management of addresses and mail room management, hybrid mail, computer generated business mail, letter preparation, mail consolidation, track & trace and 2nd delivery.

In general it is expected that prices of postal products will become more related to the underlying cost structure of these products. Further, the competitive pressure on prices will be relatively high for segments where competition is expected to take off and relatively low for segments where this is not the case.

The expected effect on the prices for addressed bulk mail is that they will go down or that they will stay at competitive level. Participants of the opinion survey expect on average the prices may go down by 10-15%. Prices for consumer mail, in particular the mail requiring next day delivery, will not go down and may rise instead. There will also be a pressure to raise prices for individual business mail requiring next day delivery, but this pressure is less than for consumer mail. The prices for non time sensitive individual business mail will probably go down, but less than for bulk mail, in particular if actual entry on this segment will take place or if small business mailers can make use of services of mail consolidators for (part of) their mail.

The expected effect of full liberalisation on the universal service provision depends on the exact form that the universal service and the universal service obligations will have in future. Although in countries like the Netherlands and Sweden the universal services may be provided in a profitable way, the funding of the universal service obligations is under relative pressure if the definition remains unchanged. Both the playing field that is not level (to the detriment of the national postal operator in this case) and the form in which any universal service burden is shared have an impact on the development of competition.

The funding of the universal service is still under pressure if the universal service would be limited to the (overnight) delivery of single item mail compared to the current day situation, but less than above. The way how the universal service funding would be shared becomes less important for competition. A limitation of the universal service to the (overnight) delivery of single item mail would make the playing field more level than if the current definition is maintained.

If the universal service is limited to 2-3 times per week delivery the problems with funding the universal service would be minimal if at all existing. Sharing funding the universal service is not an issue anymore.

It is not expected that decreasing the scope of the universal service obligations will have a negative effect on overall mail volumes. First, it is to be expected that the delivery

frequency will in most Member States not go down and that first class delivery will still be offered, also when it is not required in a universal service obligations. Second, the expected lower prices for second class mail may well improve (for example) the position of direct mail vis-à-vis other channels for marketing.

7.3 Overall conclusion and recommendations

7.3.1 Overall conclusion

It is important to realise that the level of effective competition in the postal market is not only determined by the number of competitor postal operators active in the market and their market shares, but also by the existence of potential substitutes, the bargaining power of customers and the risk of new competitors entering the postal industry. The continuing technological developments in particular in electronic communication will strengthen the competitive threat of substitutes to postal products and will cause a transformation of traditional postal products to products that further integrate postal services and electronic communication. Both the bargaining power of large customers and the risk of new competitors entering the industry will increase after a full liberalisation of the postal sector. Although the experiences in other sectors show that often the actual entry of new competitors has a real impact on market performance, also the combination of buyer power and potential entry is an important factor that the national postal operator has to consider seriously.

It is hence likely that in the largest part of the letter mail market effective competition will emerge within a couple of years after liberalisation, even if the national postal operator will maintain a dominant market position in the addressed mail market.

It is also important to realise that for private individuals and small companies the postage costs represent a very small part of the total expenses on means of communication including telephony and internet.

From the perspective of this study, we therefore see no reason to change the time path for the complete liberalisation of the postal market as set out in the postal directives. We conclude that liberalisation is the right way forward and see no urgent reason why customers should not be allowed to freely engage in agreements with postal operators of their own choice if these are able to propose a better business proposition in terms of price, quality or adaptation of the services to their specific needs.

Effective competition will however not emerge automatically, as the main conclusions with regard to the wide variety of factors that still hamper the development of competition show. Rather, the development of competition should be actively nurtured and supported in various ways. This should in our view be done primarily through creating a level playing field and not by favouring certain postal operators over others. In line with this view, we are in favour of policies that strengthen the development of competition in the medium to longer run rather than of policies that stimulate competition in the short run to the detriment of medium and longer term developments. These

considerations form the basis for the recommendations that we make in the section directly below.

7.3.2 Recommendations

We have a number of recommendations to improve the functioning of the internal market and to support the development of competition:

- The policy maker and the sector regulator should undertake actions to create a playing field that is as much as possible level to all postal operators. For the development of competition it is of crucial importance that competitor postal operators can operate in the same conditions as the national postal operators. The wish to reach an agreement with the national postal operator to continue to provide universal services in the future will involve that certain restrictions will be posed on the business model that the national postal operator is able to operate. This should not be considered a major problem with regard to the level playing field, but restrictions to the operations of the national postal operators should be kept to a minimum;
- License or authorisation requirements to offer postal services must not be overly restrictive. As for the development of competition it is crucial that postal operators are able to operate relatively small networks, no restrictions should be posed to the delivery frequency and also (almost) nation wide delivery should not be required. General requirements related to business practices can be made, such as that postal operators should adhere to the quality of service levels that they put in the market (fulfilment of promise);
- The current uncertainties regarding the prevailing and future regulatory framework at EU and more importantly at Member State level should be reduced as much as possible. Also there is a clear need in different Member States to provide clear guidance on the definitions of postal products that are, or may possibly be, included in the national regulatory frameworks. In case of a partial liberalisation of the letter mail market it should be as clear as it possibly can which postal products have been liberalised and which postal products still fall under the reserved area.
- Upcoming disputes between market participants should be resolved as quickly and effectively as possible. Given the type of problems observed and the current stage of development of competition in the postal market this calls, at least for a number of years to come, for an independent and well resourced postal regulator in addition to a competition authority that can effectively and quickly resolve existing and upcoming disputes. More in general, the danger of strategic entry barriers should be understood and dealt with using general competition law;
- In addition to settling disputes and through this removing existing regulatory uncertainties, the role that a sector regulator in a transitory period should play is to ensure that access is guaranteed at reasonable conditions to the P.O Boxes and the letterboxes, the postal code system, information on address changes, and the possibility to return mail through the network of the national postal operator. Also, the regulator should play a role on making the existing and future (negotiated) access conditions to the network of the national postal operator transparent and non-discriminatory (see also below). If necessary, the regulatory framework should be adapted to ensure that access conditions will be applied for mail consolidators, customers, and competitor postal operators in a non-discriminatory way;

- We do not recommend ex ante regulation of the access conditions to the facilities of the national postal operators. The full liberalisation of the postal market accompanied by concerted actions to support the development of competition and the creation of parallel networks of different forms and sizes is in our view the best route to go. We expect that after liberalisation a variety of (small) competitors will emerge as well as one and possibly two low cost postal operators with a nation wide delivery network or at least covering a substantial part of the country. The reason why such operators in some countries and regions may *not* emerge is because of the natural monopoly characteristics of B2C delivery in these countries or regions, and not because of the sunk cost character of the needed investments (these are not prohibiting entry). The national postal operators do have first mover advantages, but this does not prohibit entry as well;
- Rather than regulating access ex ante, it should be ensured that there is no discrimination between customers and competitors with regard to the terms of agreements for mail handling. Any access conditions should be applied in a non-discriminatory way. To safeguard that non-discrimination is applied and can be enforced if necessary, it is recommended that the national postal operators should have a public offer for their services. This public offer should not only be open and transparent, but also comprehensive. Agreements that fall outside the scope of such a comprehensive public offer should be possible as long as they do not aim to circumvent the public offer or can be considered as an abuse of dominant market position in terms of competition law. In our view this type of access will be sufficient to ensure that the network of the national postal operator can be used by competitor postal operators as a matter of last resort for part of the deliveries and that mail consolidation and upstream activities are viable economic activities contributing to product and service development;
- The postal regulator is recommended to focus their attention to market segments where effective competition is limited and where at the same time the interests of competitor postal operators and/or customers may be substantially at stake;
- In particular after the full liberalisation of the postal market there is a need to define relevant markets. Using these relevant markets the existence of any dominant position of a market participant can be established;
- Ex ante regulation should in our view be applied very cautiously. If (recurrent) abuse of dominant market position is very likely to happen and has a severe detrimental impact on the position of competitors or customers, ex ante regulation can be considered.

Development of competition in the European postal sector

MARKT/2004/03/C

Annex I

Client: European Commission, Internal Market DG

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Table of contents

Appendix 1	Mail volumes by sender/receiver	177
Appendix 2	Indicators for the five disciplinary forces of Porter	179
Appendix 3	Authorisation and licensing	181
Appendix 4	Regulation of network access	183
Appendix 5	Opinion survey report	185
Appendix 6	Overview of population density and urbanization	193
Appendix 7	Direct mail volumes	195
Appendix 8	Market shares in the (liberalised) market for addressed mail	197
Appendix 9	List of interviewed people and organisations	201
Appendix 10	List of organisations that responded to the questionnaire	203

Appendix 1 Mail volumes by sender/receiver

Table 1.A Estimated shares of addressed mail volumes by type of sender and receiver (percentages)

	B2B	B2C	C2B	C2C	Total
Austria	No information available				
Belgium ^a	52	33	10	5	100
Cyprus ^b	27	30	15	28	100
Czech Republic ^a	10	80	5	5	100
Denmark ^a	85		15		100
Estonia	No information available				
Finland ^a	21	68	1	10	100
France ^{d,f}	15	70	10	5	100
Germany ^g	85		15		100
Greece	No information available				
Hungary ^c	20	30	30	20	100
Ireland ^a	30	58	4	8	100
Italy ^a	15	65	8	12	100
Latvia ^c	10	75	5	10	100
Lithuania ^e	29	47	6	18	100
Luxembourg ^a	34	51	11	4	100
Malta ^c	2	75	9	14	100
Netherlands ^c	34	58	4	4	100
Poland ^{a,h}	18	66	4	12	100
Portugal ^b	28	61	5	6	100
Slovak Republic ^a	37	42	9	12	100
Slovenia	No information available				
Spain	No information available				
Sweden ^a	26	67	3	4	100
United Kingdom ^{a,i}	27	60	3	9	100
Average (not weighted)	22	61	8	9	100

Notes: ^a 2004; ^b 2003; ^c 2003/4; ^d 2002; ^e 2000. ^f Includes parcels. ^g Refers to domestic addressed letter mail (not including advertising mail, magazines, catalogues). ^h Refers to ordinary letters, domestic only. ⁱ Main exclusions are: special delivery, international, redirections. See Annex II, country information sheets, for the respective sources.

Appendix 2 Indicators for the five disciplinary forces of Porter

Table 2.A Indicators for the five disciplinary forces of Porter

Disciplinary force	Indicator
Internal competition	<p>Internal competition is relatively high when:</p> <ul style="list-style-type: none"> There are more competitors; The growth of the market is static or declining; There are large differences in the costs of competitors; There is a large excess capacity; Products are homogeneous and the switching costs of buyers are low; There are no price agreements between competitors and there is no price leader; Exit barriers are high.
Potential entry	<p>The disciplinary effect of entry is relatively low when:</p> <ul style="list-style-type: none"> There are significant economies of scale; Reputation and branding is important; Entrants have difficulties to gain access to important inputs, like distribution channels, resources, required technology and skills, or suitable locations; Experience in a sector is of huge importance for firms to be successful; There are network externalities; Government rules protect the incumbent(s); Incumbents have a reputation to act aggressively to entrants.
Substitutes (and complements)	<p>The disciplinary effect of substitutes and the support of complements are dependant on:</p> <ul style="list-style-type: none"> The availability of substitutes and complements; The characteristics of these substitutes, like price and quality; The price elasticity of demand for the product itself.
Supplier power	<p>Supplier power is relatively large when:</p> <ul style="list-style-type: none"> The suppliers of a firm are concentrated; The size of the orders of a company are low; There are no substitutes available for the required input; The company has made specific investments in their relationship with certain suppliers; Suppliers can take over the company; Suppliers can realise price discrimination.
Buyer power	<p>Buyer power is relatively large when:</p> <ul style="list-style-type: none"> Suppliers of a company are concentrated; The orders of suppliers are large; There are many substitutes available for the product; The company had made special investments in their relationship with buyers; Price elasticity of demand for a product is high; The buyer can take over the company.

Based on D. Besanko, D. Dranove & M. Shanley, Economics of Strategy, 2nd ed., New York etc.: John Wiley & Sons, 2000: pp. 360-365 and 380-382.

Appendix 3 Authorisation and licensing

Table 3.A Licensing and authorisation requirements for the delivery of postal products

	Items of ordinary correspondence < 100 gram	Items of ordinary correspondence > 100 gram	Outgoing cross border mail	Incoming cross border mail < 100 gram
Austria	Lic USP	No	No	No
Belgium	Lic USP	Lic	Lic	No
Cyprus	Lic USP	Lic	Lic USP	No
Czech Republic	Lic USP	Lic	Lic	No
Denmark	Lic USP / Auth	Auth	Auth	No
Estonia	Lic	Lic	Lic	No
Finland	Lic	Lic	Lic	No
France	Lic USP	No	No	No
Germany	Lic USP	Lic / No (> 350 gr)	Lic	No
Greece	Lic USP	Lic	Lic USP	No
Hungary	Lic USP	Lic	Lic / Lic USP	No
Ireland	Lic USP	Indiv. Auth	Indiv. Auth	No
Italy	Lic USP	Lic	Lic USP	No
Latvia	Lic USP	Lic	Lic USP	No
Lithuania	Lic USP	Lic	Lic	No
Luxembourg	Lic USP	Indiv. Auth	Lic USP	No
Malta	Lic USP	Lic	Lic USP	No
Netherlands	Lic USP	No	No	No
Poland	Lic USP	Lic USP / Lic (> 350 gr)	Lic USP / Lic (> 350 gr)	No
Portugal	Lic USP	Lic	Lic / Lic USP	No
Slovakia	Lic USP	Indiv. Auth	Lic USP	No
Slovenia	Lic USP	Indiv. Auth	Lic USP / Indiv. Auth	No
Spain	Lic / Lic USP	Lic	Lic	No
Sweden	Lic	Lic / No	Lic	No
United Kingdom	Lic USP / Lic	Lic	Lic	No

Note: Auth means general authorisation, Indiv. Auth means individual general authorisation, Lic means licence, Lic USP means licence to operate reserved services, No means None

Source: ECORYS (2005), WIK (2004)

Table 3.A Licensing and authorisation requirements for the delivery of postal products (continued)

	Incoming cross border mail > 100 gram	Direct mail <100 gram	Direct mail >100 gram	Magazines / Periodicals and newspapers
Austria	No	Lic USP	No	No
Belgium	Lic	Lic USP	Lic	Lic
Cyprus	Lic	Lic USP	Lic	Lic
Czech Republic	Lic	Lic	Lic	Lic
Denmark	Auth	Lic USP / Auth	Auth	Auth
Estonia	Lic	Lic	Lic	Lic
Finland	Lic	Lic	Lic	Lic
France	No	Lic USP	No	No
Germany	Lic / No (> 350 gr)	Lic USP / Lic	Lic / No (> 350 gr)	Lic / No (> 350 gr)
Greece	Lic	Lic USP	Lic	Lic
Hungary	Lic	Lic USP	Lic	Lic
Ireland	Indiv. Auth	Lic USP	Indiv. Auth	Indiv. Auth
Italy	Lic	Lic	Lic	Lic
Latvia	Lic	Lic USP	Lic	Lic
Lithuania	Lic	Lic USP	Lic	Lic
Luxembourg	Indiv. Auth	Lic USP	Indiv. Auth	Indiv. Auth
Malta	Lic	Lic USP	Lic	Lic
Netherlands	No	No	No	No
Poland	Lic USP / Lic (> 350 gr)	Lic USP	Lic USP / Lic (> 350 gr)	Lic
Portugal	Lic	Lic USP	Lic	Lic
Slovakia	Indiv. Auth	Lic USP	Indiv. Auth	Indiv. Auth
Slovenia	Indiv. Auth	Indiv. Auth	Indiv. Auth	Indiv. Auth
Spain	Lic	Lic	Lic	Lic
Sweden	Lic	Lic	Lic	No
United Kingdom		Lic	Lic	No

Note: **Auth** means general authorisation, **Indiv. Auth** means individual general authorisation, **Lic** means licence, **Lic USP** means licence to operate reserved services, **No** means None.

Source: ECORYS questionnaire (2005), WIK (2004)

Appendix 4 Regulation of network access

Table 4.A Competition or work sharing in upstream activities: are access conditions ex ante regulated?

	Outward sorting	Inward sorting	Last mile	P.O. Box delivery ex ante regulated access	Solving disputes denial of access / that means more than mediator function
Austria	No	No	No	No	No
Belgium	No	No	No	No	No
Cyprus	No	No	No	No	No
Czech Republic	No	No	No	No	No
Denmark	No	No	No	No	Yes
Estonia	No	No	No	No	Yes
Finland	No	No	No	No	Yes
France	No	No	No	No	No
Germany	Yes	Yes	No	Yes	Yes
Greece	No	No	No	No	No
Hungary	No	No	No	No	Yes
Ireland	No	No	No	No	Yes
Italy	No	No	No	No	No
Latvia	No	No	No	No	No
Lithuania	No	No	No	No	No
Luxembourg	No	No	No	No	No
Malta	No	No	No	No	No
Netherlands	No	No	No	Yes	Yes
Poland	No	No	No	No	No
Portugal	No	No	No	No	Yes
Slovakia	No	No	No	No	No
Slovenia	No	No	No	No	Yes
Spain	No	No	No	No	No
Sweden	No	No	No	Yes	Yes
United Kingdom	No	No	No	No	Yes

Source: ECORYS questionnaire (2005)

Appendix 5 Opinion survey report

As part of the project, an opinion survey was held under a number of experts (people working at regulators, incumbents, competitors and sector experts) in a number of countries. The complete list of participant of the opinion survey is given in Annex 5.

The opinion survey was held through a two-step iterative procedure, meaning the answers obtained in the survey were presented to the participants of the survey to give them the possibility to adjust their opinion. To prevent any negative group interaction the Delphi method was used, meaning the answers were made anonymous and averaged before sending them to the participants.

The answers in some cases diverged significantly. Nevertheless, we feel that the opinions expressed here represent the average opinion of the respondents pretty well. With respect to the potential market shares that may be gained by competitor postal operators, some respondents argued that they could not judge the results, as the results are averaged over the EU.

Participants

The following persons participated in the opinion survey:

Table 5.A Participants in the opinion survey

Country	NRA	Policy maker	USP	Competitors	Other
Belgium	X		X		
Czech republic	X	X	X	X	
France		X	X	X	
Germany	X	X	X	X	
Poland	X			X	X
Slovenia			X	X	

Result of the opinion survey

The questions are stated in **blue**, whereas the answers are stated in regular normal font. Any additions in the second survey round are presented in *italic*.

Question 1:

In which markets or market segments will entry, with competition as a result, be most likely?

Entry is most likely to occur in the B2X segment, and within that segment, entry is most likely to occur in addressed letter mail, as well as in advertising mail. The B2C segment appears to be the most attractive due to higher volumes in that specific market segment. For some entrants, B2B may, nevertheless be attractive as less investment is required to build up a distribution network. This latter observation is one of the main reasons for the low attractiveness, in terms of potential entry, of the C2X market segment. Apart from a delivery network, a collection network has to be built as well. International mail is generally limited in volume; therefore, it is not a very attractive segment to be active in, unless a delivery system in other countries is present, e.g., in the case of foreign incumbent operators.

A number of more detailed remarks:

- Mail volumes that are offered at a certain, foreseeable, time are more attractive to process;
- The volume in B2X is much larger (75-85%) than the volume in C2X;
- Collection costs are much higher for C2X (requires physical presence, i.e., a network of post offices or letter boxes). B2X mail can be collected from business premises, and/or delivered to a limited number of delivery points;
- The possibility to offer services of 'lower' quality (like slow delivery) is attractive for both businesses (lower prices) and for postal operators (requires a less extensive network);
- *A less extensive network may take the form of a more labour-intensive production process (e.g., manual sorting), less frequent delivery, etc. Such a network would be considerably cheaper. A network that offers less frequent, but time-certain delivery would not be much cheaper than an existing network;*
- Offering hybrid mail services is attractive as well (saves on, e.g., transportation costs, although these costs are relatively low (around 5% of total costs).
This saves time as well.
- Economies of scale and scope (also via consolidation) are easier to reach in the B2X segment;
- B2B segment is attractive in some countries due to the relatively high volume and low costs;
- In some countries the infrastructure is poorly developed, in that case, it is costly to become active in anything other than B2X;
- In some countries, densely populated ones, with a small number of remote areas, entry in the C2X segment may also occur;
This requires a collection network, however. Such a network is expensive. Placing collection boxes at strategic locations may help.
- Within B2C addressed letter mail may be most attractive as the market size is largest;
- Mail differs from parcels. Mail stagnates; parcel market grows due to e-commerce;

- If B2C is offered, small step to do B2B as well, vice versa is not possible.
If there are clients, starting up a postal business may be attractive. Start ups take place in the segments where the clients are.
International mail is attractive mostly to foreign incumbents, despite the relatively low volumes.

Question 2:

What will the market shares of new competitors in the market segments defined in question 1 be? Can you explain your answer in more detail?

Future market shares depend among others on the following issues:⁸¹

- *Market share gain depends on the pricing strategy that is allowed for the incumbent;*
- *If uniform pricing is abolished market share of competitors is likely to grow less;*
- *Big customers (banks, utilities etc.) force lower prices for bulk mailing activities. There is also increased demand for hybrid mail (if offered). These services can easily be offered by new providers;*
- *Consolidation has been suppressed so far, but is likely to develop more progressively.*

Average estimation:

Market segment	B2B	B2C	C2B	C2C
Addressed letter mail	40%	30%	5-10%	
Advertising mail	35-40%	30%		
International mail	70%			
Total market	10-40% (depends on timing)			

Note: The answers relate to a period of liberalisation +5.

- *A small number of respondents points out that the percentage for B2B, C2X, and international mail should be lower;*
- *Some respondents argue that these numbers are only feasible with well-designed access regulations.*

Question 3:

What will the consequences for **prices** be? Can you explain your answer in more detail?

- *Prices will be lower, predominantly in the B2X market and even more so in international mail (with the possibility of geographical distinctions). Prices in urban areas are likely to fall by more than those in rural areas. Prices in the C2X segment **may** go up, but demand-side substitution **may** occur (in some countries, prices are already high, however, which will eliminate this effect);*

⁸¹ See the answer to question 8 as well

- *B2X advertising mail down by most. Addressed less, C2X up. In several niches (e.g., for SMEs) prices may go up as well;*
- **Prices will go down slightly in addressed letter mail (B2C);**
- *Prices down by 10 to 15%;*
- *Result may be different prices for local, regional, national (extra-regional) and international mail. Requires changes in business model for incumbent, however;*
- **Future USO regime is important, mainly the potential changes in uniform price obligation. No changes in advertising mail market (already competitive and also part of a broader commercial market).**

Average estimation:

Market segment	B2B	B2C	C2B	C2C
Addressed letter mail	-10%		Prices are not likely to fall, may even go up. This holds for households and SMEs	
Advertising mail	-15%			
International mail	In some countries, large potential for decrease, in others hardly any potential			

The percentages relate to average prices, price differences may exist if services of varying quality are provided.

- *The behaviour of the regulator will have an important impact on prices. The effects of the actions of regulators will be felt predominantly in the C2X segment;*
- *Another important dimension is whether or not a differentiation of prices throughout the country is allowed.*

Question 4:

What will the consequences for the **supply of value added services** be? Can you explain your answer in more detail? (Examples are first and second (and third) class mail, etc.)

- *Consumers (active in the C2X market, this includes SMEs) are predominantly interested in price;*
Some respondents argue that consumers are also (predominantly?) interested in reliability.
- *Currently, incumbents (especially in countries with a less developed mail, or more in general, service sector) do not offer the full range of services that customers (business) are interested in. Hence, more VA services will be offered as a result of liberalisation, but mostly in the B2X segment. This broader range of services includes services across various dimensions, like slow service, guaranteed overnight delivery, flexibility, track-and-trace service, urgency, registered mail, 2nd daily delivery, mail room management, archiving, letter preparation, address checking, consolidation, hybrid mail;*
Value added services are offered in the more advanced countries, but to a far lesser extent in less advanced MS.
- *Mostly changes in letter and advertising mail expected;*
- *Three business models may be distinguished:*
Premium (quick and reliable),

Normal,

Slow and cheap;

- *D+2 is feasible for incumbents (no night-shifts). This decreases costs.*

Question 5:

What changes in the above if **full liberalisation** will **not occur**, for example, if liberalisation stops at 50 grams (or in any other dimension, e.g., ex ante access regulation)?

- *Full liberalisation is most likely to occur. In some countries, political resistance may result in slower changes. Most respondents believe that full liberalisation will occur. Reciprocity is an issue in EU. Even half-hearted liberalisation offers an attractive potential volume already;*
- *Some respondents argued that privatisation might be important as well;*
- *There are already ways to circumvent the monopoly as value added services are not in the monopoly in all cases. In addition, it is quite easy to make a letter slightly heavier to let it fall outside the (reduced) US.*

As from these questions, the answers will mainly relate to the B2X segment, unless stated otherwise.

Question 6:

What are the **characteristics** of the new, expected, **entrants**?

- Postal operators from abroad.
 - Existing postal operators in alliances/ joint ventures with other operators.
 - New operators e.g., from Publishing sector, Transport sector, other sectors.
 - Any other?
 - How many operators will result due to liberalisation? What is their background (see a-d)?
- *Full entry is most likely to occur in the form of existing postal service providers (possibly alliances of regional players, maybe linked up with postal operators from abroad) and from the publishing sector (e.g., magazines, newspapers). Some transport companies also offer postal services. Couriers may also extend their range of services. Small niche players may also become active, e.g., in closed loops.*
 - *Entry of foreign incumbents is not very likely, unless in the form of acquisitions. Some foreign incumbents are already active in international mail, however, as this market has already been liberalised.*
 - *Letter-shops may enter, as may small local players.*
 - *More operators will be active after liberalisation. The number of full service providers will be low.*
 - *Not too many competitors will result. Approximately ten will be really active and pose some competitive threat.*

- *Nationwide no more than 3 or 4 operators will be active. In smaller and less densely populated Member States, and in countries with specific geographic conditions, this number may be lower.*
- On a regional level, the number of operators may be higher.
- Some private start ups operate under the umbrella of larger companies.
- There is a positive relationship between unemployment and (local) start ups.

Question 7:

How will the market be entered?

- In full (a full service provider will enter).
- Only segments will see entrance (e.g., collection, inward sorting, transport, outward sorting, delivery).
- Other.

Full service provision (duplication of the existing network) is unlikely to happen according to some, but others point out that in the long run 2 or more networks may co-exist. In France, this is already the case (large scale collection is not offered, however). Entry in delivery only is unlikely to occur, collection may be attractive. Most entry will be related to offering VA services. Upstream services already used (e.g., in banking), relatively low investments required. Consolidators are often already active. Entry in specific local markets (mostly large cities) has already occurred.

Question 8:

What are the main (legal and non-legal) impediments to entry to new entrants?

Legal:

- The uniform pricing scheme for operators makes certain areas more attractive to enter, as incumbent prices can be undercut (in urban areas, even more so in countries with varying geographical conditions, e.g., France (Corsica, large rural areas).
- Licences (and compensation funds). This includes administrative procedures.
- Litigation, patent protection, etc.
- Price caps.
Price caps may keep prices artificially low, which impedes entry.
- VAT (on the table in Brussels, unlikely to change in the short run, however, Sweden and Finland already levy VAT).

Despite the VAT issue, in a number of MS, competitors are already active, and are able to charge competitive prices that include VAT.

Economic and strategic:

- Volumes,
- Scale economics,
- Fixed vs. variable costs,
- Sunk costs,

- Predatory pricing,
- Small market size (for small countries).
- Access to letterboxes, P.O. Boxes, change in address notifications.
- Access beyond closed apartment doors.

Question 9:

In which **time frame** you expect liberalisation to have impact on (more) competition in the postal market in your country?

*Soon, liberalisation **already** has an impact on competition, but only in a limited number of countries, and in specific segments. Impact will be **progressive**. So far, progress has been fairly limited (some liberalisation has occurred, market share of competitors still only 5-10%.*

Question 10:

Do you think that liberalisation will have impact on the **growth** of the total mail market or mail **volumes** in your country?

- No, it will only lead to reallocation of market shares without growth of volumes.
- Yes, total market and mail volumes will grow because of improved services, new services and more value added services. Please answer in the form of: growth will be ...% of ... specific market (per/over ... time period).

Two main factors have to be distinguished here. One is the autonomous growth of mail activities, e.g., as the result of GDP growth. In the countries that recently accessed the EU, this autonomous growth is likely to remain. Second, in countries with a more saturated mail market, like France and Germany, the mail market is shrinking, with the exception of a (modest) increase in B2X mail. More and more substitute products are available.

- Specific sub-segments are likely to show more volatility:
- Billing will decrease in size (electronic substitution).
- Advertising mail will increase in (relative) volume, addressed down. Substitution to other media may play an important role, but also one that is difficult to foresee.

Question 11:

What will be the **impact** of liberalisation on the market position of the **National Postal Operator**? (Timing: currently 2009 (or earlier if market is fully liberalised prior to 2009) + 2-3 years.)

- National Postal Operator will maintain market share? Why?
- National Postal Operator will lose market share? How much? Why?

Lose market share, for sure, estimates vary from not much: 5% to up to 50% in selected markets. See the more detailed answer to question 2 as well.

Question 12:

Which **conditions** are important upon **full liberalisation** of the postal market?

- a. Safeguarding Universal Service? (i.e., uniform pricing, quality prescriptions, affordable prices, ...)
- b. Access regulation?
- c. Price of postal services?
 - i. For individual consumers/households?
 - ii. For businesses?

- *Uniform pricing will be under pressure (or quality if uniform pricing is the rule). Access is already regulated in one way or the other in most countries.*
- *Number of outlets may be under pressure, political problem (real concern in France and Germany).*

About half of the respondents indicated that all aspects of USO (includes frequency, retail network and time) are important. A large number of other respondents indicated that there is no need for a USO (if regional price differences are acceptable).

Question 13:

Do you expect that competition on the postal market in the **EU at large** will **diverge** from the development of competition in **your country**? The answer may be focused around the characteristics of entrants (question 6), the way in which markets will be entered (question 7), and the impediments to entry (question 8).

- Diverging experience between North and South of Europe. But businesses will force process ahead.
- *A Northern European market will certainly be established.*
- Will depend on the (remaining) differences in regulation (and regulatory strictness of regulators).
- And country characteristics, such as prevalence of rural areas.
- A limited number of Pan European operators will emerge.
- Employment protection may be an important aspect in the postal reform debate in some Member States.
- State interference possible in some countries. What is important is access to existing networks (not necessarily of the incumbent operator, newspaper delivery may be an option as well).
- Country characteristics, like mail per inhabitant, density, etc. are also important factors that may explain differences in the potential for competition.

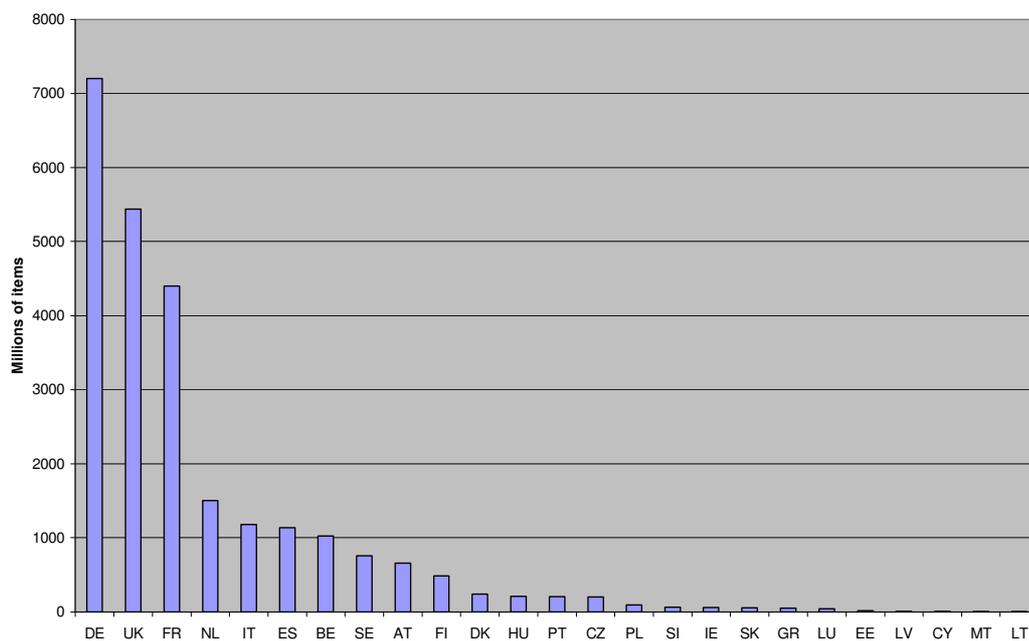
Appendix 6 Overview of population density and urbanization

Country	Urbanization	Relative score ¹	Population density	Relative score ¹
Austria	65,8	+/-	96,5	-
Belgium	97,2	++	341,0	++
Cyprus	69,2	+/-	81	-
Czech Rep.	74,3	+	129,3	+/-
Denmark	85,3	++	125,3	+/-
Estonia	69,4	+/-	31,0	--
Finland	60,9	-	17,1	--
France	76,3	+	110,1	+/-
Germany	88,1	++	231,1	+
Greece	60,8	-	83,6	-
Hungary	65,1	+/-	108,6	+/-
Ireland	59,9	-	56,9	--
Italy	67,4	+/-	192,2	+
Latvia	66,2	+/-	35,6	--
Lithuania	66,7	+/-	52,1	--
Luxembourg	91,9	++	192,3	+
Malta	65,8	+/-	1265,8	+
Netherlands	61,9	-*	480,8	++
Poland	54,6	--	122,3	+/-
Portugal	57,4	--	114,3	+/-
Slovakia	50,8	--	110,2	+/-
Slovenia	76,5	+	98,5	-
Spain	83,4	++	83,6	-
Sweden	89,1	++	21,9	--
UK	65,8	+/-	244,9	+

¹ See par. 6.5.2 of the main report. A plus in this table indicates that the factor in the respective column has, ceteris paribus, a positive contribution to the viability of business models that can be employed by new entrants. Source: Eurostat (2005), UN (2003)

Appendix 7 Direct mail volumes

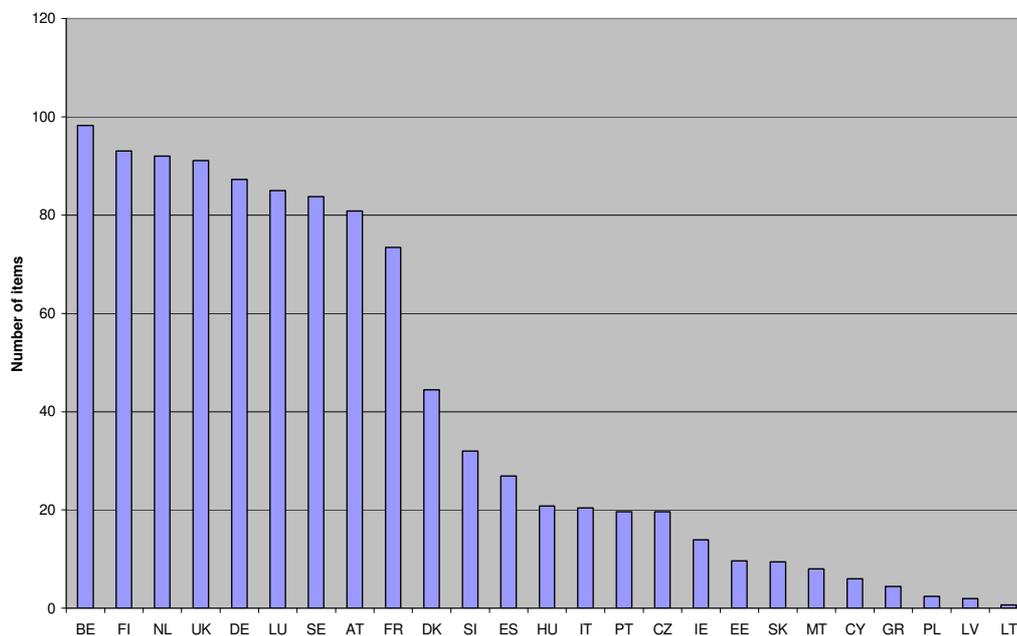
Figure 1.A: Total number of addressed direct mail items delivered



Note: estimations based on various sources, data need to be handled with caution

Source: ECORYS

Figure 2.A Number of addressed direct mail items delivered per capita

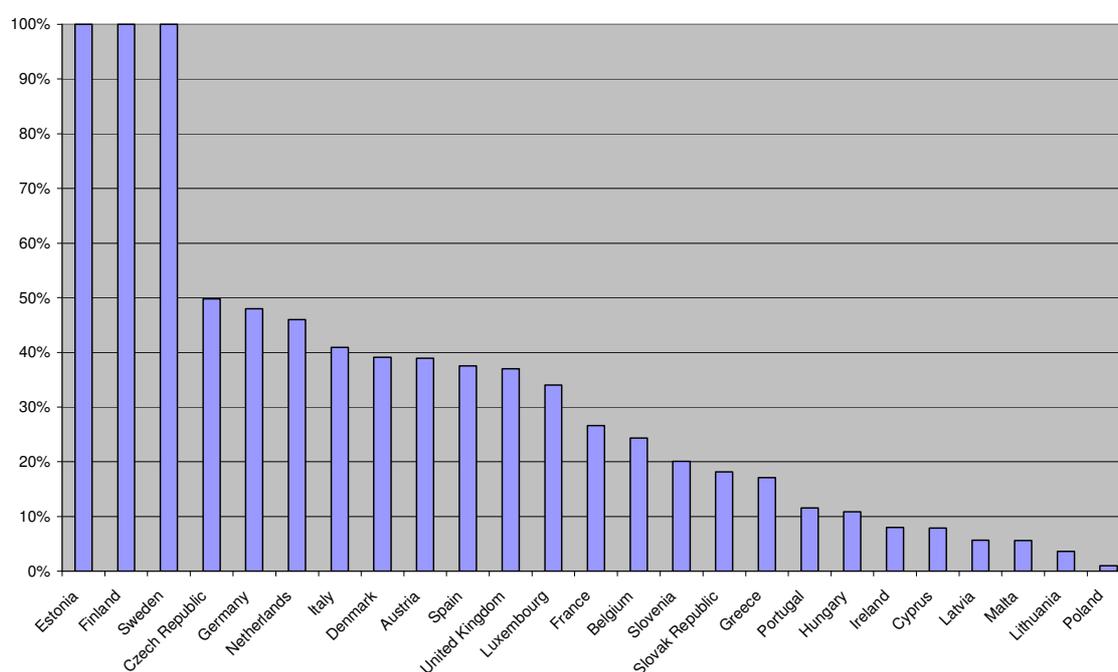


Note: estimations based on various sources, data need to be handled with caution

Source: ECORYS

Appendix 8 Market shares in the (liberalised) market for addressed mail

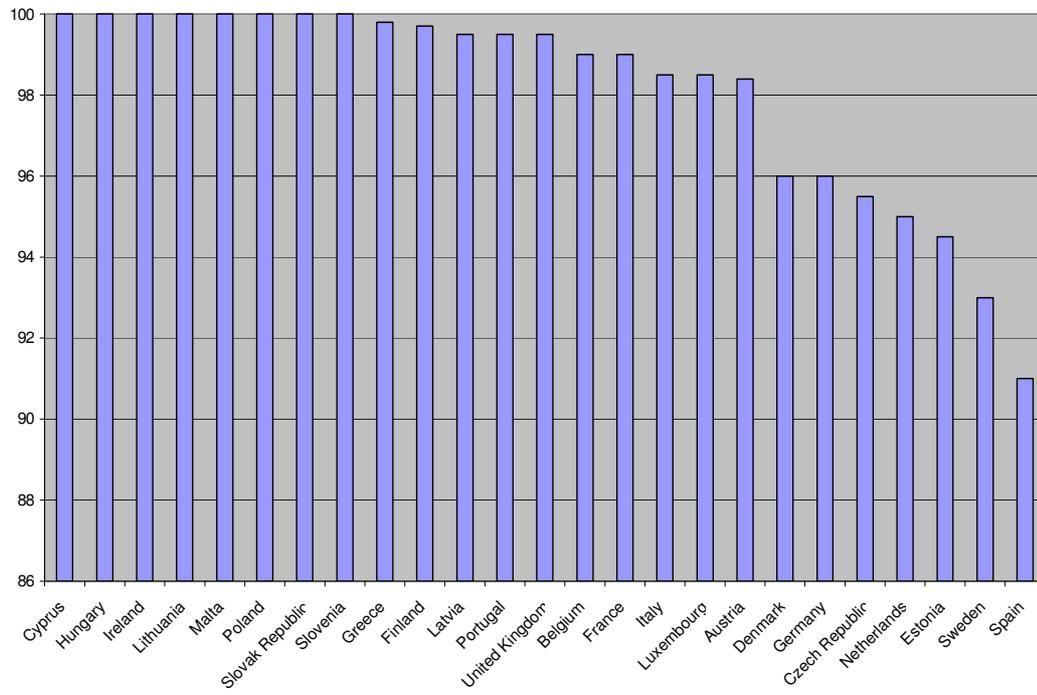
Figure 3.A: Share of the market for addressed mail (excl. newspapers) liberalised (in terms of volume)



Note: The percentages indicate the share of the total market for addressed mail (excl. newspapers) that is open to competition. The percentages of the share of the market of addressed mail that is liberalized are based on the data about volumes of addressed mail delivered, collected by ECORYS. The data exclude the volumes delivered by express and courier operators. As the underlying data needs to be approached carefully, the same applies to these figures.

Source: ECORYS (2005)

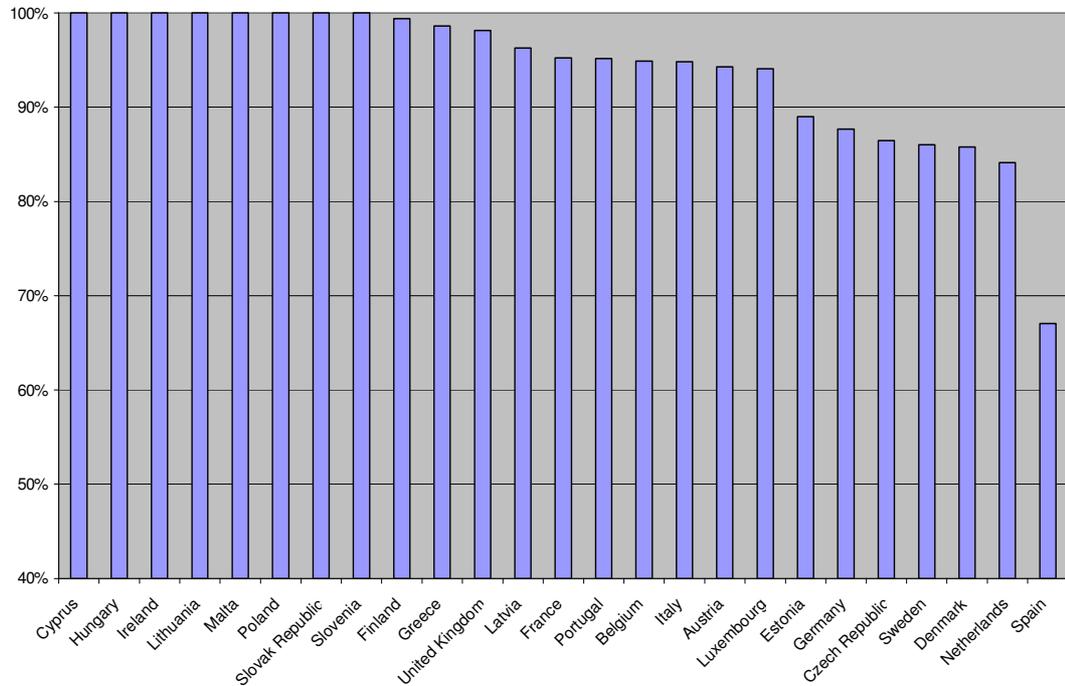
Figure 4.A: Market share of the universal service provider (in terms of volume) in the delivery of addressed mail (excl. newspapers)



Note: the percentages indicate the market shares in the total market for addressed mail (excl. newspapers). The percentages are based on the data about volumes of addressed mail delivered, collected by ECORYS. The data exclude the volumes delivered by express and courier operators. As the underlying data needs to be approached carefully and is sometimes based on best estimates (see the country information sheets), the same applies to these figures.

Source: ECORYS (2005)

Figure 5.A: Market share of the universal service provider (in terms of volume) in the market for delivery of addressed mail that is liberalised



Note: the percentages indicate the market shares in the liberalized market for addressed mail (excl. newspapers), that is the market share of the USP in the particular market segments that are open to delivery for competitors. The percentages are based on the data about volumes of addressed mail delivered, collected by ECORYS. The data exclude the volumes delivered by express and courier operators. As the underlying data needs to be approached carefully and is sometimes based on best estimates (see the country information sheets), the same applies to these figures.

Source: ECORYS (2005)

Appendix 9 List of interviewed people and organisations

Table 7.A Interviewed people and organisations

Country	NRA	Policy maker	USP	Competitors	Other
France	X	X	X	X	X
Germany	X	X	X	X	
Italy	X	X	X		X
The Netherlands	X	X	X	X	X
Poland	X	X	X		X
EU wide		X		X	X

Note: the EU-wide organisations include Fedma, EEA and the European Commission, DG Competition, other relates to (large) corporate customers, competition authorities and consumer representative organisations.

Appendix 10 List of organisations that responded to the questionnaire

From the following organisations, we received a response to our questionnaire:

Country	NRA	Policy maker	USP	Competitors	Corporate customers	CRO
Austria	X	X	X	X	X	
Belgium	X	X	X		X	X
Cyprus	X	X	X			
Czech republic	X	X	X	X		
Denmark	X	X	X		X	X
Estonia	X	X	X	X		X
Finland	X	X	X			
France	X	X	X	X	X	
Germany	X	X	X	X		
Greece	X	X	X		X	
Hungary	X	X	X			
Ireland	X	X	X			
Italy	X	X	X			
Latvia	X	X	X			
Lithuania	X	X	X			
Luxembourg	X	X	X	X		
Malta	X	X	X		X	X
Netherlands	X	X	X	X	X	
Poland	X	X	X			
Portugal	X	X	X			
Slovakia	X	X	X		X	X
Slovenia	X	X				
Spain	X	X	X			
Sweden	X	X	X	X		X
United Kingdom	X	X	X	X	X	

Note: NRA = national regulatory authority, USP = universal service provider, CRO = Consumer representative organisations