
Review of Second Class safeguard caps 2024

Proposed price caps for Second Class universal services

CONSULTATION:

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1. Overview

This document sets out Ofcom’s proposals for retail price caps on Royal Mail’s universal postal services to apply from 2024 to 2029. The main aim of our proposals is to ensure that universal postal services remain affordable for consumers. In developing these proposals we have also taken into account the impact of any caps on the financial sustainability of the universal service obligations (USO).

Postal services continue to play a vitally important role in our society. They are used by almost everyone in the UK on a regular basis, from online shopping deliveries, to receiving important medical correspondence, to sending cards to friends and relatives.

The universal service obligations require Royal Mail to deliver and collect letters six days a week, and parcels five days a week, at an affordable and uniform price throughout the UK. Ofcom took over regulation of post in 2011 and in 2012 we imposed caps on Second Class letters and small parcels in order to ensure that access to postal services is affordable for all consumers. We last reviewed these caps in 2018-19 and the current caps are due to expire on 31 March 2024.

We have provisionally concluded that Ofcom should continue to maintain a safeguard cap regime to ensure that consumers retain access to affordable postal services. We have also provisionally concluded that we are able to simplify the regime given the competitive pressure on Royal Mail in the area of parcels.

What we are proposing – in brief

- **Retain a safeguard cap on Second Class standard and large letters.** This is because Royal Mail continues to be a near-monopolist in the provision of letters and we cannot rely on competition to ensure that prices remain affordable without a control on these Second Class letter services.
- **Remove the safeguard cap from parcels.** We consider that a safeguard cap on Royal Mail’s parcel services is no longer necessary. Competition in this market appears to be effectively constraining Royal Mail’s ability to raise prices, therefore ensuring that they remain affordable. Royal Mail will continue to be required to set a single price for these services across the UK.
- **Allow the safeguard caps on letters to rise with inflation (CPI), but no higher.** Our evidence indicates that current prices are affordable for most consumers, but that real-terms increases are likely to risk making them unaffordable for more consumers, given the increase in the cost of living.
- **Create a single basket cap for Second Class standard and large letters.** This will give Royal Mail slightly more commercial flexibility in setting prices between standard and large letters as long as the basket price (a weighted average) rises no faster than CPI.
- **Continue to limit the safeguard caps to Second Class letter services.** We have identified no evidence that there is an affordability concern with respect to other services given the nature of their use and the alternative access provided by Second Class services.

The overview section in this document is a simplified high-level summary only. The proposals we are making and our reasoning are set out in the full document.

Next steps

We invite responses to the questions raised in this consultation, which are summarised in Annex 4, by 5pm on 1 September 2023. Details on how to respond to this consultation are set out in Annex 1. We intend to publish our statement setting out our final decisions on the safeguard caps by the end of 2023.

2. Background

- 2.1 In this section, we set out our powers and duties in relation to postal services and imposing safeguard caps on Royal Mail, our approach to postal regulation, and the background on the safeguard caps we currently impose. We also set out how the prices of the safeguarded services have changed since the start of the current cap period (2019), a summary of key developments since then, and finally, the results of our impact assessment, equality impact assessment, and Welsh language assessment.

Powers and duties

Ofcom's statutory duties in relation to postal services

- 2.2 Our principal duty under the Communications Act 2003 (the "CA 2003") is to further the interests of consumers and citizens across all of our different functions, including post, where appropriate by promoting competition.¹
- 2.3 In relation to post, section 29(1) of the Postal Services Act 2011 (the "PSA 2011") says that we must carry out our functions in a way that we consider will secure the provision of a universal postal service. The provision of a universal postal service includes the provision of a number of end-to-end services at affordable prices.² We must also have regard to the need for the universal postal service to be financially sustainable (which includes the need to make a reasonable commercial rate of return) and efficient before the end of a reasonable period and to continue to be efficient at all subsequent times.³
- 2.4 In performing our principal duty under the CA 2003, we must also have regard to the interests of consumers and citizens in respect of choice, price, quality of service and value for money. In all cases, we must additionally have regard to the principles that regulatory activities should be transparent, accountable, proportionate, consistent, and targeted only at cases in which action is needed, and any other principles appearing to us to represent the best regulatory practice.⁴
- 2.5 Where it appears to be relevant, we must also have regard to the considerations listed in section 3(4) of the CA 2003, including (but not limited to) the needs of persons with disabilities, of the elderly and of those on low incomes.
- 2.6 Where possible we must treat our duties under the CA 2003 and PSA 2011 equally, with the latter taking priority if there is a conflict between them.⁵

¹ Section 3(1) of the CA 2003.

² Section 31 of the PSA 2011.

³ Section 29(3) & (4) of the PSA 2011.

⁴ Section 3(3) of the CA 2003.

⁵ Section 3(6A) of the CA 2003.

Regulatory framework

- 2.7 We designated Royal Mail Group Limited (“Royal Mail”) as the universal service provider in 2012. As the universal service provider, we imposed upon Royal Mail designated universal service provider (“DUSP”) conditions using our powers under section 36 of the PSA 2011.
- 2.8 It is by the DUSP conditions that we require Royal Mail to provide the universal service. The universal service must include at least the services contained in an Order made by us under section 30 of the PSA 2011 setting out a description of the services we consider should be provided as part of the universal postal service, as well as the standards with which those services are to comply.⁶ These include, amongst other things, a six day a week letter service and a five day a week parcel service. Consumers must be able to send letters and parcels by a priority (First Class) or standard (Second Class) service and those services must be offered at affordable, uniform prices.
- 2.9 We may also impose DUSP conditions in order to set tariffs to be used for determining the prices of the universal postal service or a part of it.⁷ We have used this power to impose the current safeguard caps on Royal Mail. When setting such tariffs, we must seek to ensure that the price of the relevant universal postal service:
- a) is affordable;
 - b) takes account of the costs of providing the service; and
 - c) provides incentives to provide the service efficiently.⁸
- 2.10 In order to impose, modify or revoke a regulatory condition, including the DUSP conditions, we must be satisfied that the imposition, modification or revocation in question:
- a) is objectively justifiable;
 - b) does not discriminate unduly against particular persons or a particular description of persons;
 - c) is proportionate to what it is intended to achieve; and
 - d) is transparent in relation to what it is intended to achieve.⁹
- 2.11 In order to impose, modify or revoke a condition, we must publish a notification setting out our proposal. We must consider every representation made to us about the proposal before we publish a final notification setting out the imposed, modified or revoked condition.¹⁰
- 2.12 Our power to impose, modify or revoke a regulatory condition is also subject to our specific postal duty in section 29(1) of the PSA 2011.

⁶ To fulfil its duties under PSA 2011, Ofcom made The Postal Services (Universal Postal Service) Order 2012 (the Order) which is available here: <https://www.legislation.gov.uk/uksi/2012/936/contents/made>

⁷ Section 36(4) of the PSA 2011.

⁸ Section 36(5) of the PSA 2011.

⁹ Paragraph 1 of Schedule 6 to the PSA 2011.

¹⁰ Paragraph 3 of Schedule 6 to the PSA 2011.

2.13 We explain in section 7 how we have met the above legal tests and duties when making our proposals. The legal and regulatory framework relevant to this review is set out more fully in Annex 6.

Approach to postal regulation

2.14 While we prescribe the services that must be provided as part of the universal postal service, our overall regulatory framework affords Royal Mail commercial flexibility (in pricing and operational terms) as to how these services are provided. We established this regulatory framework upon assuming our role in post and have carried out periodic reviews since then, the most recent of which concluded in July 2022.

2.15 Our approach ensures that Royal Mail can make its own commercial decisions based on the issues it faces, supporting the provision of a financially sustainable and efficient universal postal service.

2.16 This framework is underpinned by a number of safeguards. These include:

- a) our active monitoring regime to understand the changing needs of users, the changing market dynamics and the financial sustainability and efficiency of the universal service, and any risks to these;
- b) quality of service standards on certain universal services, including delivery targets on First and Second Class mail; and
- c) to ensure affordability, we undertook in the 2022 review to review the safeguard caps on Second Class letters and parcels up to 2kg.¹¹

2.17 As set out above, one of our duties is to support competition in the postal market as this helps ensure good consumer outcomes. We therefore promote competition by imposing minimal intervention in increasingly competitive areas of the postal market.

2.18 Consistent with Ofcom's general regulatory principles,¹² our approach to postal regulation is to intervene in the postal market only when appropriate, for example, where there is an a risk of user need which is not being met by the market, or of consumer harm more generally. While we operate with a bias against intervention, we are prepared to intervene promptly and effectively where required.

Services subject to a safeguard cap

2.19 The safeguard caps were introduced in 2012. Our objectives for these caps were to: seek to ensure a basic universal service is available to all at affordable prices; and to ensure that users of postal services, especially vulnerable consumers, are protected from significant price increases. We first decided to impose a safeguard cap on Second Class standard letters set at 55p for 2012-13. This represented a 53% increase on the stamp price at the

¹¹ The safeguard caps apply to parcels weighing up to and including 2kg. We use the term 'parcels up to 2kg' throughout this document to refer to parcels weighing up to and including 2kg.

¹² Ofcom: [Policies and guidelines](#)

time which was 36p (2011-12 prices). The cap was to apply for seven years and was subject to indexation at CPI. We considered that capping Second Class alone (i.e. not also on First Class) was sufficient to ensure access to an affordable postal service.

- 2.20 We decided in July 2012 to extend the scope of the safeguard caps to create an additional, separate basket cap¹³ comprising Second Class large letters and small and medium parcels up to 2kg. We set the level of this basket cap to allow for up to a 53% increase in the overall price of services within the cap. Thereafter, the basket cap increased each year by CPI, in line with the level of annual additional price increase allowed for under the standard letter cap.
- 2.21 Following a review in 2018-19, we decided to raise the level of the Second Class standard letter cap by 5% in real terms, which took the upper limit of the cap from 60p to 65p. This meant Royal Mail could price Second Class standard letters up to a maximum of 65p from 1 April 2019 to 31 March 2020. The cap continues to increase by CPI each year on 1 April and this price cap regime is in place until 31 March 2024.
- 2.22 We also decided not to adjust the level of the cap for Second Class large letters and parcels up to 2kg, which has continued to increase each year by CPI on 1 April. Royal Mail had considerable pricing flexibility of approximately 29% under this cap at the time of our statement in January 2019, so we decided not to increase the cap level further.
- 2.23 Consequently, several Royal Mail services are currently subject to a safeguard cap. Second Class standard letters are subject to a single cap, as set out above. The basket cap is imposed on Second Class large letters (of which there are four weight steps) and parcels up to 2kg. The total weighted average price for these services is allowed to rise by 29.4% from 2018-19 weighted average prices plus the cumulative increase in inflation since 2018-19. Prices of services within the basket range from £1.15 for the lightest large letter to £5.49 for a medium parcel purchased offline. The caps apply to stamped services purchased online and offline.

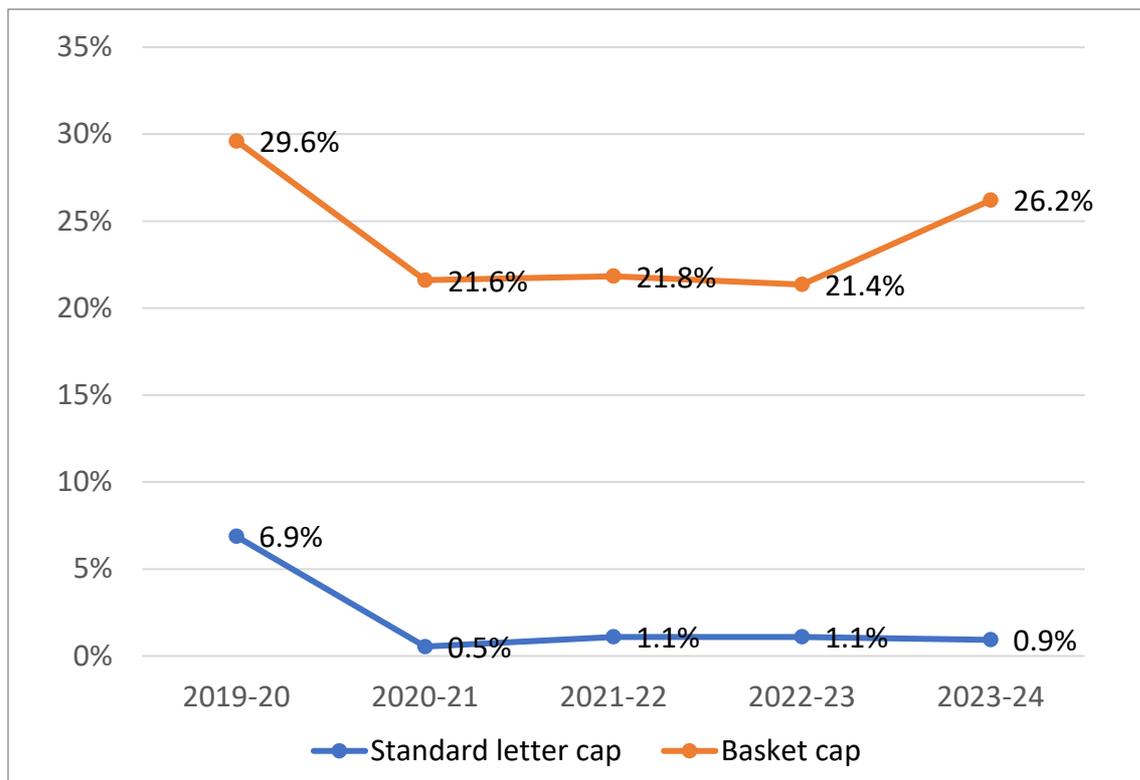
Royal Mail's pricing behaviour since 2019

- 2.24 Royal Mail has priced Second Class standard letters at the safeguard cap¹⁴ in recent years (since April 2021). In contrast, it has priced Second Class large letters and parcels within the basket cap considerably lower than the cap.

¹³ The basket cap is a cap on the weighted average prices of the services in the basket cap. As there may be multiple large letter and parcel services (for different sizes and/or weight steps), there will be different prices for each. The basket cap allows for Royal Mail to have pricing flexibility, to adjust price levels between these services, as long as the weighted average is not above the basket cap.

¹⁴ Royal Mail theoretically has a very small amount of headroom under the cap, but is unable to use it as the price must be rounded to the nearest pence.

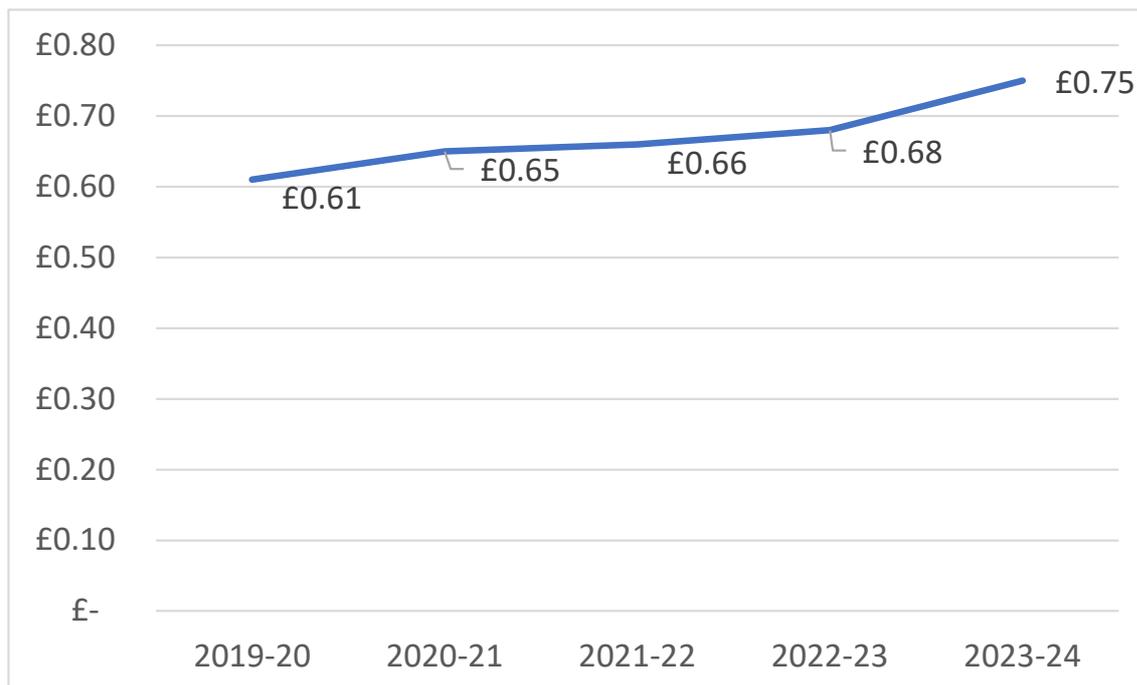
Figure 1: Percentage headroom under the standard letter cap and basket caps, 2019-20 – 2023-24



Source: Second Class safeguard cap compliance submissions as part of Royal Mail Regulatory Financial Reporting Information.

2.25 Royal Mail has increased the price of a Second Class standard letter over the past four years, from £0.61 in 2019-20 to £0.75 in 2023-24 (see Figure 2 below).

Figure 2: Nominal price of Royal Mail Second Class stamped standard letters, 2019-20 – 2023-24



Source: Royal Mail Price Guides.

2.26 Nominal prices of Second Class large letters within the basket cap have increased throughout the current cap period, with the exception of the 501g-750g service which has remained constant since 2021. Prices have also increased in real terms (by around 20%), with the exception of the 501g-750g weight step which has remained steady in real terms since the start of this cap period.

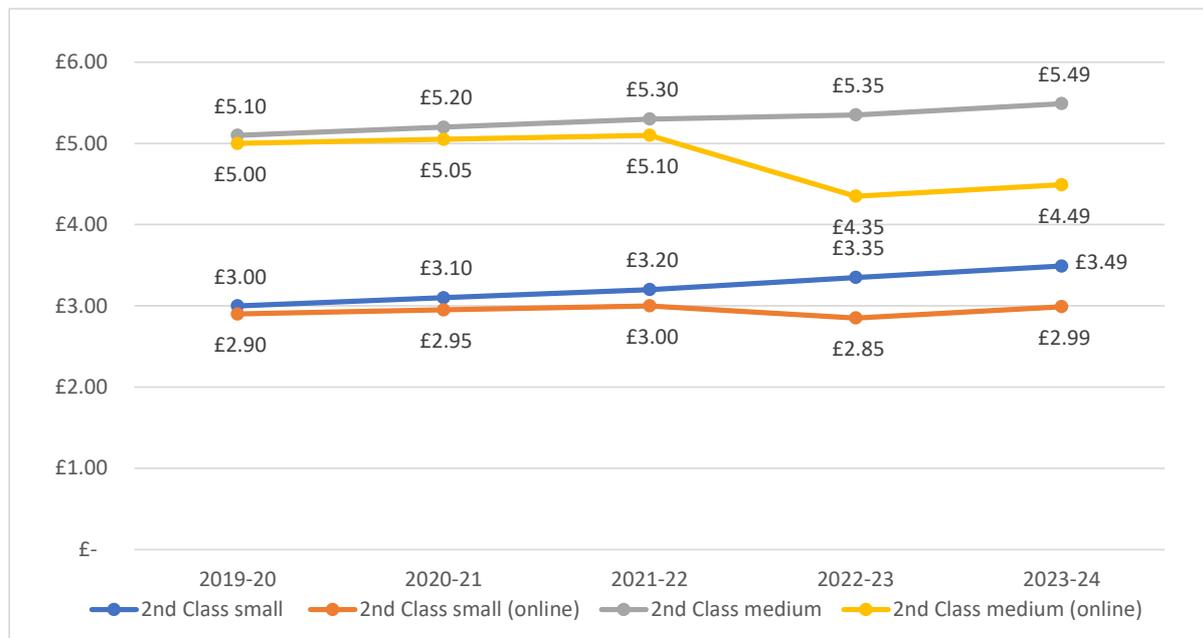
Figure 3: Nominal prices of Second Class stamped large letters, 2019-20 – 2023-24



Source: Royal Mail Price Guides

2.27 The prices of most Second Class parcels within the basket cap (see Figure 4) have risen slightly in nominal terms since 2019. In real terms, prices have decreased since 2019, although by more for those purchased online than at a Post Office (by -12% for small and -23% for medium for those purchased online, compared to -1% for small and -8% for medium for those purchased at a Post Office).

Figure 4: Nominal prices of second class parcels up to 2kg, 2019-20 – 2023-24



Source: Royal Mail Price Guides

Key developments since 2018-19 review

Covid-19 pandemic

- 2.28 The Covid-19 pandemic has had a significant impact on the postal sector. Royal Mail, like other postal operators, had to deal with elevated absence rates as a result of sickness, shielding and self-isolation, and social distancing requirements – all of which had a detrimental effect on its ability to provide services and meet its quality of service targets.
- 2.29 In addition, there was a significant change in the mix of traffic through Royal Mail’s network. The closure of non-essential physical retail locations and self-isolation meant that online shopping boomed and letter volumes decreased. At the time of this consultation document things have settled back to pre-covid trends, with parcel revenues now exceeding letter revenues.

Royal Mail's financial situation and outlook

- 2.30 On 18 May 2023 Royal Mail published its full-year results for 2022-23,¹⁵ which included an adjusted operating loss for the UK business of £419m. It forecast further losses for the UK business, with a view to returning to profit for the year 2024-25,¹⁶ and noted that revenue growth is reliant on improving quality of service and achieving efficiencies through operational change. It cited the impact of the industrial dispute; an inability to deliver productivity improvements; lower Covid-19 test kit volumes, and a weaker online retail market as contributing factors to its performance.
- 2.31 Royal Mail faced 18 days of industrial action by CWU members in 2022-23. After several months of negotiations between Royal Mail and the Communication Workers Union, an agreement was reached, with a deal that the CWU's Postal Executive Committee currently recommends that its members accept.¹⁷
- 2.32 Royal Mail's quality of service (QoS) has also deteriorated in recent years. In 2021-22 we decided that it would not be appropriate to find Royal Mail in breach of its QoS targets, because of the impact of Covid-19 on its operations.¹⁸ Royal Mail missed its QoS targets for 2022-23 and, on 15 May 2023, we opened an investigation into Royal Mail's compliance with the targets for this period.¹⁹

Increase in the cost of living

- 2.33 CPI inflation in the UK is at its highest level for more than 40 years, reaching 11.1% in October 2022.²⁰ It remains high, although it appears to have peaked since then (dropping to 8.7% in May 2023), and the Office for Budget Responsibility (OBR) forecasts that it will decrease significantly in 2023-24.²¹ Energy and food prices in particular have risen significantly, although inflation appears to have slowed recently. Gas price inflation was 36% in the year to April 2023, while electricity price inflation was 17%, and food price inflation was 19%.²²
- 2.34 UK households have been under increasing financial strain as a result. The ONS found in June 2023 that more than half of UK adults said that they are using less fuel in their homes because of the cost of living (56%), while half (49%) said that they are buying less when

¹⁵

International Distributions Services plc, Unaudited Preliminary Results for the 52 week period ended 26 March 2023. See: <https://www.internationaldistributionsservices.com/media/12036/ids-plc-fy-2022-23-results-rns-18-5-23.pdf> [accessed 15/06/2023].

¹⁶ Excluding voluntary redundancy costs.

¹⁷ <https://www.cwu.org/rmgstrikeinfo>

¹⁸ Ofcom, 2022. [Investigation into Royal Mail's quality of service performance in 2021-22](#)

¹⁹ Ofcom, 2023. [Investigation into Royal Mail's quality of service performance in 2022-23](#)

²⁰ ONS, CPI Annual Rate 00. See: <https://www.ons.gov.uk/economy/inflationandpriceindices/timeseries/d7g7/mm23> [accessed 21/06/2023]

²¹ OBR, CPI Inflation. See: <https://obr.uk/forecasts-in-depth/the-economy-forecast/inflation/#CPI> [accessed 15/06/2023]

²² <https://www.ons.gov.uk/economy/inflationandpriceindices/articles/costofliving/latestinsights>

food shopping (49%). Around two-thirds of adults (65%) are spending less on non-essential items in response to the rising cost of living.²³

Impact assessment

- 2.35 Impact assessments provide a valuable way of assessing different options for regulation and show why the preferred option was chosen. They form part of best practice policymaking. This is reflected in section 7 of the CA 2003, which means that generally we must carry out impact assessments where our proposals would be likely to have a significant effect on businesses or the general public, or when there is a major change in our activities. However, as a matter of policy, we are committed to carrying out and publishing impact assessments in relation to the vast majority of our policy decisions.
- 2.36 Specifically, pursuant to section 7, an impact assessment must set out how, in our opinion, the performance of our general duties (within the meaning of section 3 of the CA 2003) is secured or furthered by, or in relation to, what we propose.
- 2.37 In March 2023, we consulted on changes to our impact assessment guidance to align it with new legal obligations as well as best practice.²⁴ The proposed changes included maintaining our bias against intervention while clarifying that the law may require us to intervene, updating how we present our impact assessments to stakeholders, and an increased recognition that qualitative impacts are an important part of assessing some policy decisions. Although this guidance has not yet been confirmed, and is therefore still subject to change, we have sought to take account of it in our assessment of the impact of our proposals, in addition to using our existing guidance and approach.²⁵
- 2.38 We have considered the impact of our proposals on:
- a) consumers in the UK, in particular vulnerable consumers; and
 - b) Royal Mail.

The key components of our impact assessment are therefore in section 5 (assessment of affordability) and section 6 (financial sustainability). We also set out our proposals in the round, taking into account the impact both on consumers and Royal Mail, in section 7.

Equality Impact Assessment

- 2.39 Section 149 of the Equality Act 2010 (the “EA 2010”) imposes a duty on Ofcom, when carrying out its functions, to have due regard to the need to eliminate discrimination, harassment, victimisation and other prohibited conduct related to the following protected characteristics: age; disability; gender reassignment; marriage and civil partnership; pregnancy and maternity; race; religion or belief; sex and sexual orientation.

²³ ONS, 16 June 2023. Cost of living latest insights. See:

<https://www.ons.gov.uk/economy/inflationandpriceindices/articles/costofliving/latestinsights> [accessed 19/06/2023]

²⁴ Ofcom, 2023. Consultation: [Draft impact assessment guidance](#)

²⁵ Ofcom, 2005. [Better policy making: Ofcom’s approach to Impact Assessment.](#)

- 2.40 The EA 2010 also requires Ofcom to have due regard to the need to advance equality of opportunity and foster good relations between persons who share a protected characteristic and those who do not.
- 2.41 Section 75 of the Northern Ireland Act 1998 (the “NIA 1998”) also imposes a duty on Ofcom, when carrying out its functions relating to Northern Ireland, to have due regard to the need to promote equality of opportunity and regard to the desirability of promoting good relations across a range of categories outlined in the NIA 1998. Ofcom’s Revised Northern Ireland Equality Scheme explains how we comply with our statutory duties under the NIA 1998.²⁶
- 2.42 To help us comply with our duties under the EA 2010 and the NIA 1998, we assess the impact of our proposals on persons sharing protected characteristics and, in particular, whether they may discriminate against such persons or impact on equality of opportunity or good relations.
- 2.43 We do not consider that our proposals will discriminate in any way against persons with protected characteristics. Retaining a safeguard cap on standard and large letters will help to ensure that these services remain affordable, including for people with protected characteristics. Prices for parcels weighing up to 2kg should also be affordable due to the availability of competitive offerings and the greater competitive constraints on Royal Mail’s parcel prices.
- 2.44 We consider that there are three main groups with protected characteristics who could be particularly affected by increases in postal prices: older people (those aged 55+); people in ethnic minority groups; and people with disabilities.
- 2.45 Data from the ONS shows that people aged 55+ spend more than average on postal services and therefore may be particularly affected by any increase in the price of these services. However, our quantitative research shows that older people are significantly less likely than average to report affordability issues.
- 2.46 Our quantitative research did however find that people in ethnic minority groups and disabled people were more likely to report affordability issues. Our further examination of the issues in the qualitative research indicate that concerns about affordability appeared to relate to general economic conditions rather than relating specifically to post. While this research did suggest that post prices at current levels did not have a significant impact on these households’ costs, it did highlight the sensitivity of these groups to price rises and the need to ensure postal prices remain affordable.
- 2.47 Therefore, we consider that the evidence suggests that a retention of a safeguard cap remains in the interest of many of the protected groups but there is no specific evidence that these groups have a different set of affordability concerns from the general community.

²⁶ Ofcom, 2014 (updated 2019). [Revised Northern Ireland Equality Scheme for Ofcom](#).

2.48 We accordingly consider that our proposals will not discriminate against any groups with protected characteristics. We are therefore satisfied that we have complied with the public sector equality duty in the EA 2010, and the NIA 1998, in making the proposals set out in this consultation.

Consultation question

Question 1: Do you agree with our assessment that our proposals will not discriminate against any groups with protected characteristics? Please state your reasons and provide evidence to support your view.

Welsh language impact assessment

2.49 We have considered our proposals on safeguard caps for universal postal services under the Welsh Language Policy Making Standards.²⁷ These standards require Ofcom to assess (a) opportunities for persons to use the Welsh language, and (b) treating the Welsh language no less favourably than the English language when formulating a new policy, or reviewing or revising an existing policy, including conducting research to support our policymaking.²⁸

2.50 Our proposed revisions to the existing policy on safeguard caps for postal services are aimed at ensuring that post will remain affordable and therefore accessible to all consumers across the UK. In our view, the implementation of our proposed approach would help to ensure that there would be no adverse effects, but instead some likely positive effects, on the use and treatment of the Welsh language. This is because our policy seeks to ensure that consumers across the UK can continue using post as a form of communication, which is likely to have positive effects on the Welsh speakers who wish to communicate in Welsh through this form. We welcome stakeholders' views on our proposed assessment under the Welsh Language Policy Making Standards.

Consultation question

Question 2: Do you agree with our assessment under the Welsh Language Policy Marking Standards? Please state your reasons and provide evidence to support your view.

Structure of this consultation

2.51 The remainder of this document is structured as follows:

- Section 3 sets out the review objectives and approach

²⁷ Standards 84 to 86 and 91 to 93 as set out in: [Hysbysiad-Cydymffurfio44-Y-Swyddfa-Gyfathrebiadau-en.pdf \(ofcom.org.uk\)](#)

²⁸ In addition to considering how our research can assist our policy making to take account of the Welsh Language Policy Making Standards, we offered all participants an opportunity to use Welsh in research interviews conducted by Ofcom, as is our standard practice.

- Section 4 contains an analysis of the market context and constraints on Royal Mail's pricing for the services to which safeguard caps currently apply. This analysis contributes to our proposal for the services which more likely are required to be subject to a safeguard cap.
- Section 5 sets out our approach to assessing the affordability of postal services, which informs how we seek to meet our duty to ensure the provision of universal postal services at affordable prices. We apply this approach to those services currently subject to safeguard caps and also set out an assessment of whether safeguard caps on any other universal postal services are needed to ensure they are affordable.
- Section 6 examines the impact of the capped services on the financial sustainability of the universal service, as well as considering Royal Mail's costs and efficiency incentives.
- Section 7 sets out the safeguard caps that we propose will apply from 1 April 2024, and how we consider that they meet our policy objectives.

2.52 Finally, Annex 5 sets out the draft DUSP condition imposing the safeguard caps on Royal Mail from 1 April 2024.

2.53 The consultation questions are set out in Annex 4.

3. Our review objectives and approach

Objectives of our review

- 3.1 This section sets out our proposed policy objectives for this review. Our objectives aim to demonstrate clearly to stakeholders what we are trying to achieve and how we have interpreted our legal duties with regard to postal services in the context of this review. They provide a clear and transparent framework against which we assess the available evidence and make proposals.
- 3.2 When we introduced the safeguard caps in 2012, we adopted objectives of ensuring affordability, protecting vulnerable consumers, enabling Royal Mail to make a reasonable commercial rate of return, and minimising the effect of safeguard caps on Royal Mail's pricing freedom.
- 3.3 These objectives still form the core of our approach to reviewing the safeguard caps. However, we are conscious that they were first set in 2012 and that the postal market has undergone significant change since then. Accordingly, we consider that the objectives should be revisited to ensure that they continue to be relevant and effective in light of our duties and make clear our approach to determining the scope of the safeguard caps and their level in the current market context.
- 3.4 We propose to use the following objectives for our review of safeguard caps:
- Ensure universal services are affordable, particularly for vulnerable consumers;
 - Provide protection to consumers where such protection is unlikely to be provided by competitive markets;
 - Ensure any safeguard cap takes into account the costs of providing the capped service(s); and
 - Minimise the impact of any safeguard cap on the financial sustainability of the universal service, while retaining incentives for Royal Mail to operate efficiently.
- 3.5 We set out below our rationale for each of our proposed objectives. Whilst the proposals in this consultation are made with the aim of fulfilling each of these objectives, we recognise that, in some cases, there may be tension between them and that therefore we will have to exercise our regulatory judgement in order to reach a decision that strikes the most appropriate balance. In particular, we need to consider the best way to ensure affordability for consumers in the context of challenges to the long term financial sustainability of the universal service. We discuss how we have balanced these objectives in developing our proposals for both the services to which we consider the safeguard caps should apply, and the level of these caps, in section 7.

Ensure universal services are affordable, particularly for vulnerable consumers

- 3.6 This objective reflects our duty to perform our functions in a way that we consider will secure the provision of a universal postal service, which includes the provision of a number of services (known as ‘universal postal services’) at affordable prices. When exercising our power to set price caps for any universal services, we must seek to ensure that the prices are affordable.
- 3.7 We have chosen to highlight explicitly the need to ensure affordability for vulnerable consumers, reflecting our duty (in section 3(4) of the CA 2003) to have consideration to the needs of vulnerable people (specifically, the needs of people with disabilities, of the elderly and of those on low incomes). In general, we consider that it is against the needs of vulnerable groups that questions of affordability are most acute. We discuss which groups of consumers are more likely to be vulnerable in relation to the affordability of postal services in section 5.
- 3.8 More generally, we consider that, as in our previous review, if a universal service is affordable for vulnerable consumers then it will be affordable for the wider set of postal users (both residential consumers and small and medium businesses (“SMEs”)).
- 3.9 We discuss our proposed approach to assessing the affordability of universal postal services, and our evidence on the affordability of such services, in section 5.

Provide protection to consumers where such protection is unlikely to be provided by competitive markets

- 3.10 This objective aims to provide a clear and transparent way for stakeholders to understand how we decide which services are more likely to be subject to a safeguard cap. This is because, where Royal Mail’s prices are not constrained by competition, it is more likely that it will raise prices to the extent that they become unaffordable. In particular, our approach makes explicit the assumption that effective competition:
- a) protects consumers from the high prices which a monopoly provider might otherwise impose; and
 - b) in general, delivers as affordable a price as the cost of delivery of a service allows.
 - c) more generally, it also sets out that price caps are not the only means of ensuring that prices are affordable, and that effective competition can instead ensure this.
- 3.11 However, the objective includes the acknowledgement that simply the presence of some degree of competition is not necessarily sufficient to constrain prices and ensure affordability, and that further protection (i.e. a safeguard cap) may therefore be necessary in some instances.
- 3.12 In developing this objective, we have taken into account our duty to further the interests of citizens and consumers, where appropriate by promoting competition, and our general approach to regulation to operate with a bias against intervention. This objective also

aligns with our regulatory objectives for the postal sector, set in our 2022 Review of Postal Regulation, which include supporting effective competition in postal services for the benefit of consumers.²⁹

- 3.13 Finally, this objective ensures a degree of consistency in our approach to reviewing the safeguard caps, where in the past we have considered both the existing and potential demand- and supply-side constraints on Royal Mail's pricing. We have previously chosen to impose a safeguard cap where we consider that the competitive constraints are insufficient to stop Royal Mail from pricing its universal services unaffordably.³⁰ This is also the approach we take in this review.

Ensure any safeguard cap takes into account the costs of providing the capped service

- 3.14 This objective reflects our duty, when setting price caps, to ensure that they take account of the costs of providing the service. It is also consistent with our duty to act in such ways as we consider will secure the provision of a universal postal service. An important element of this is having regard to the financial sustainability of the universal postal service.
- 3.15 We note that this objective necessarily interacts with our objective of ensuring affordability. Whilst we may impose a safeguard cap to ensure that Royal Mail does not exploit its retail market power such that prices become unaffordable, we consider the requirement that the universal service be affordable does not mean that prices should be set below efficiently-incurred incremental costs, in particular as this could cause market distortion. Consumers have a number of options to choose from for their communications services, of which post is one. If prices are set below Royal Mail's costs then this could incentivise consumers to choose to send an item by post where they otherwise would have chosen a different, lower-cost method.
- 3.16 Similarly, in a competitive market in equilibrium, prices will reflect costs, such that a fully competitive market should lead to the best possible outcome for consumers. Therefore, having regard to the cost of the provision of the service in setting a safeguard cap means that our intervention can approximate the consumer benefits of a competitive market.³¹

Minimise the impact of any safeguard cap on the financial sustainability of the universal service, while retaining incentives for Royal Mail to operate efficiently

- 3.17 This objective reflects the fact that we must have regard to the need for the universal service to be financially sustainable (including the need to make a reasonable commercial

²⁹ See Ofcom, 2022. [Statement: Review of Postal Regulation](#), paragraph 2.38.

³⁰ See, for example, Ofcom, 2019. Statement: [Review of the Second Class Safeguard Caps 2019](#), paragraph 3.3.

³¹ Ofcom has taken a similar position in telecoms – we deregulated the retail telephony market in 2009 once it was clear that the markets was effectively competitive, and have regularly withdrawn charge controls from wholesale markets as competition has increased to the point of constraints on charges – see treatment of Wholesale Broadband Markets under Ofcom since 2005.

rate of return) and efficient, when carrying out our general duty to secure the provision of a universal postal service. It also reflects our duty to ensure that any price cap we set provides Royal Mail with efficiency incentives.

- 3.18 It acknowledges the fact that a price cap will reduce Royal Mail's commercial flexibility and could therefore adversely affect the financial sustainability of the universal service. Consequently, we aim to impose safeguard caps only to the extent appropriate to protect consumers and ensure affordability, thereby minimising the impact on the financial sustainability of the universal service.
- 3.19 With regard to efficiency, as we have set out previously, the safeguard caps are not intended in and of themselves to provide efficiency incentives to Royal Mail.³² Our view is that Royal Mail remains incentivised to pursue efficiency improvements given the wider commercial pressures that it faces, and in light of the shareholder discipline to which it is subject as a privatised company. However, this objective aims to ensure that any caps are set at such a level as not to create incentives for Royal Mail to rely on price rises rather than efficiency improvements to increase its revenues.

SMEs

- 3.20 We consider that, if postal prices are affordable for residential consumers, then they are likely also to be affordable for small and medium sized enterprises ('SMEs'). This is because SMEs, unlike residential consumers, are able to absorb at least some of their postage costs as they can pass them on to customers. Further, our research makes it clear that SMEs make greater use of non-USO services and alternative suppliers to Royal Mail for sending their post than residential users.
- 3.21 We recognise that absorbing increased postage costs is likely to be more difficult for smaller SMEs than larger SMEs, because (for example) smaller SMEs are less able to benefit from economies of scale in negotiation with alternative postal operators. But we consider that small SMEs are effectively, therefore, more closely aligned to consumers. Therefore, the approach we have taken in this review is to focus our analysis on vulnerable residential consumers rather than SMEs. This is because we consider that if post is affordable for vulnerable residential consumers who in general are less able to absorb costs than SMEs, it is likely also to be affordable for SMEs.³³

Consultation question

Question 3: Do you agree with the objectives we propose to use for our review of safeguard caps? Please state your reasons and provide evidence to support your view.

³² See, for example, Ofcom, 2019. Statement: [Review of the Second Class Safeguard Caps 2019](#), paragraph 6.41.

³³ This approach is line with that taken in our previous review of safeguard caps. See Ofcom, 2019. Statement: [Review of the Second Class Safeguard Caps 2019](#), paragraph 4.63.

4. Market analysis

Introduction

- 4.1 This section first sets out our assessment of the market context and constraints on Royal Mail's pricing for the services to which safeguard caps currently apply, specifically Second Class standard letters, large letters and parcels weighing up to 2kg. We particularly consider the extent to which the market context and competitive constraints have changed since our last review.
- 4.2 As discussed in section 3, Royal Mail faces fewer constraints on its pricing for services where there is little or no competition from other providers. This in turn makes it more likely that Royal Mail could raise prices such that they become unaffordable for consumers. The analysis set out in this section therefore enables us to identify which universal postal services are more likely to need to be subject to a safeguard cap to ensure that they are affordable.
- 4.3 We note that, in exercising our powers under section 36 of the PSA 2011 to impose or modify the safeguard caps under the DUSP conditions, we are not required to carry out a market analysis or to assess market power in accordance with the principles of competition law. We have, however, undertaken an assessment of market conditions sufficient to support our understanding on the competitive constraints on Royal Mail's pricing and the risks to the provision of an affordable service.
- 4.4 We focus instead on an assessment of the extent of competitive constraints in the market segments in question, particularly to inform our understanding of the degree to which market forces might impact Royal Mail's setting of the prices for the services covered by the safeguard caps. We first consider standard USO letters, followed by large USO letters, and then USO parcels up to 2kg.³⁴ For each of these services we assess the demand- and supply-side constraints on Royal Mail's pricing.

Standard letters

Context

- 4.5 In this section, we focus on single piece end-to-end standard letter services that Royal Mail is required to offer under the USO.³⁵ Royal Mail defines standard letters as letters which do

³⁴ Unless otherwise stated, letters, large letters and parcels refer to USO services purchased using stamps.

³⁵ We refer to single piece services (both letters and parcels) as any delivery service which is available for purchase by any member of the public and can be used for sending an individual parcel. Single piece letter services account for the majority of non-bulk end-to-end letters services provided by Royal Mail. End-to-end refers to letters collected and delivered by Royal Mail. Bulk mail involves Royal Mail collecting large volumes of mail directly from larger businesses (or other organisations) and then using its network to sort, distribute and deliver these. Bulk mail is not part of the USO and therefore out of scope of this review. Access mail letter services, i.e. bulk mail collected by competing access operators from larger businesses and organisations which is then inserted into Royal Mail's network for delivery, are also out of scope of this review.

not exceed 24.5cm in length, 16.5cm in width, 0.5cm in thickness and 100g in weight. We note from the outset that there remains a lack of competition in end-to-end delivery of single piece standard letters, as Royal Mail continues to be the only provider of such services.³⁶

- 4.6 Royal Mail provides a range of USO letter services (e.g. First Class, Second Class, Redirections and Special Delivery Guaranteed). Customers can pay for universal postal services in two main ways: stamp and meter.³⁷ We focus our analysis on stamped letters that consumers or SMEs send via post boxes and Post Offices (e.g. birthday cards or invoices), which are collected and delivered by Royal Mail. Stamped letters accounted for around half (50%) of all standard letter volumes in 2022-23.³⁸ Paying by meter (e.g. via a franking machine) allows customers to access cheaper prices, but is usually suitable only for high-volume users (e.g. businesses) as they require an initial investment.³⁹ As noted in paragraph 2.23, Second Class standard letters purchased using a stamp are subject to the safeguard cap.⁴⁰
- 4.7 Overall, letter volumes have been in decline for a number of years. This includes stamped letter volumes, which have been in decline since our last review of the safeguard caps. Figure 5 summarises how Royal Mail's end-to-end letter volumes have evolved since our last review.⁴¹

³⁶ There are some residual end-to-end services offered by operators other than Royal Mail who account for just 0.3% of total addressed letters volumes. However, these are bulk operators.

³⁷ Some universal postal services can also be purchased via an account.

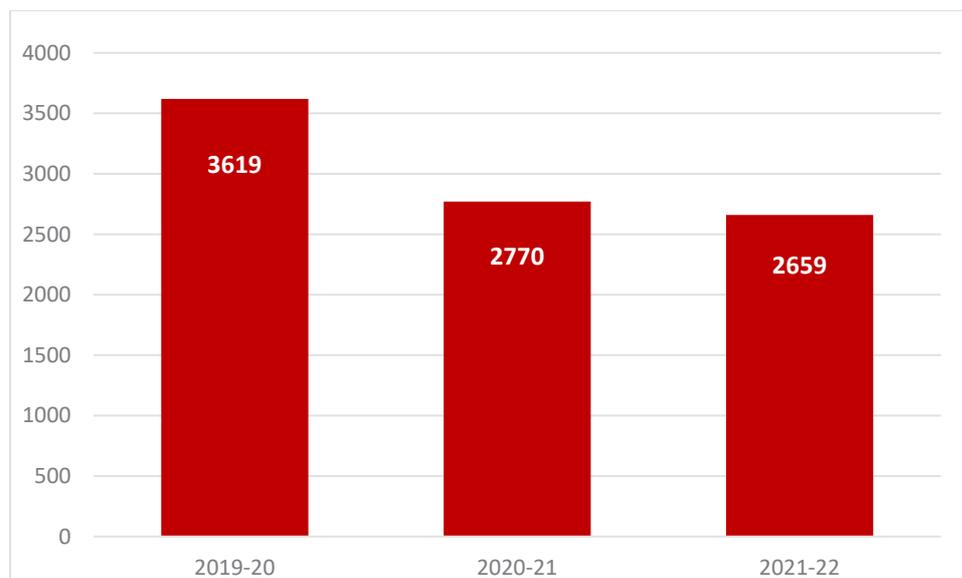
³⁸ Royal Mail Regulatory Financial Reporting Information.

³⁹ For meter customers an investment in a franking machine is required whereas on account customers have to incur the costs of setting up a business account with Royal Mail.

⁴⁰ We expect that the stamp price cap will act as an indirect cap on discounted services like metered mail and 'on account'.

⁴¹ End-to-end letter volumes declined by 27% between 2019-20 and 2021-22. Total addressed letter volumes i.e., end-to-end and access volumes, declined by 23% over the same period.

Figure 5: Royal Mail’s end-to-end letter volumes by financial year, millions



Source: Ofcom/Royal Mail data. *Royal Mail end-to-end is an Ofcom calculation and refers to Royal Mail total letters, excepting access. Figures exclude international.

4.8 The decline in letter volumes largely reflects the replacement of communications previously sent by mail with electronic alternatives (i.e., e-substitution). This is a structural change in consumer behaviour that has occurred as technology has enabled alternative means of communicating. We expect this trend to continue.⁴²

Demand-side constraints

4.9 A consumer or SME considering sending a letter of standard dimensions using a Second Class stamp has, in theory, the following mail or non-mail alternatives:

- sending the item using a different Royal Mail service (e.g., First Class stamp, signed for, tracked, or Second Class meter if sending sufficient volumes or Royal Mail or third party access provider etc.);
- send by courier/parcel delivery company/local end-to-end provider; and/or
- not sending the item by mail, instead sending it using an alternative electronic form of communication.

Sending the item using a different Royal Mail service

4.10 As of April 2023, the price for a standard letter Second Class stamp is £0.75, which is the cheapest mail option available. For example, the price for a First Class stamp is £1.10, whereas the price for Second Class “signed for” service is £2.25. The constraint exerted by these and other Royal Mail services is therefore likely to be weak as, in most

⁴² For example, we note the finding in the 2022 Residential Postal Tracker that the proportion of residential participants saying that they are sending less than two years ago was higher than the proportion reporting that they are sending more, for all types of mail tested (see paragraph 5.20). This trend has been ongoing for some years (see previous Annual Monitoring Updates, section 4).

circumstances, consumers would be unlikely to respond to a price increase in Second Class stamps by switching to a more expensive alternative.

- 4.11 The other Royal Mail letter delivery services available provide additional quality attributes relative to a Second Class delivery service, including being delivered faster or with more information about when a service is delivered or assurance that it has been delivered, which is reflected in their higher prices. However, if a user would have been content with the Second Class service that does not offer these additional attributes, then the price differential to these other services means that they are less likely to provide attractive alternatives.
- 4.12 Moreover, given that Royal Mail's other letter delivery services are not constrained by alternatives not involving Royal Mail (i.e., Royal Mail is also the only provider of these services),⁴³ they are unlikely to exert an effective competitive constraint on Royal Mail's Second Class stamp price.
- 4.13 Metered Second Class letters are cheaper than stamped Second Class letters. However, as mentioned previously, alternative payment methods would only be a viable alternative for high volume users due to the initial investment required. In addition, they are only offered by Royal Mail such that the prices of these alternative payment methods are not effectively constrained by competition.⁴⁴ Hence, alternative payment methods are also unlikely to exert a meaningful competitive constraint on Second Class standard letter stamp prices.

Sending the item by courier, parcel delivery company or local end-to-end provider

- 4.14 Royal Mail is currently the only national scale provider of end-to-end delivery of single piece standard letters. Though local partnerships may offer comparable services for some consumers in some geographic areas, these are unlikely to exert a meaningful competitive constraint on Royal Mail given their limited scale.
- 4.15 A consumer may also consider using a courier or a parcel delivery company for sending a standard letter. However, given the significantly higher cost of such services they would likely only present a viable alternative in certain circumstances. The constraint exerted by these services is therefore likely to be weak as consumers would in general be unlikely to respond to a price increase in Second Class stamps by switching to a significantly more expensive alternative.

E-substitution

- 4.16 E-substitution refers to the replacement of communications previously sent by mail with electronic alternatives (e.g. emails or electronic file transfers). It is a structural change in consumer behaviour that has occurred as technology has enabled alternative means of communicating. As we concluded in our previous review, e-substitution is one of the

⁴³ Except in very limited cases of smaller scale end-to-end operators delivering in specific geographic areas.

⁴⁴ For higher volume users, Royal Mail's meter services may face some competition from operators using access services. However, this indirect constraint is not likely to be strong as only a small subset of customers would send sufficient volumes of mail to make them attractive to a competing access provider.

factors responsible for the observed decline in single piece standard letter volumes, including Second Class stamps.

- 4.17 E-substitution could act as a constraint on Royal Mail's pricing behaviour if higher stamp prices made post a less attractive option and triggered further e-substitution, such that Royal Mail would have to keep prices low (or even reduce them) in order to prevent further losses to e-substitution. However, we consider that, to a large extent, the e-substitution trend is not driven by changes in the price of letters but rather reflects changes in consumer preferences in response to changes in communications technology and the willingness of individuals and businesses to adopt electronic communications methods.
- 4.18 Once in place, electronic alternatives have a substantially lower cost per item to users than post.⁴⁵ Further moderate price increases in post would therefore be unlikely to trigger substantial additional switching for those customers that have electronic alternatives in place, as there is already a significant differential between post and electronic alternatives. As only 6% of households do not have internet access,⁴⁶ this is likely to be the case for the majority of consumers.
- 4.19 This is further substantiated by the fact that, despite Royal Mail's internal documents on its pricing decisions in relation to business mail demonstrating a consideration that larger price increases may have a greater risk of triggering extra e-substitution,⁴⁷ relatively moderate price increases are seen as profitable.⁴⁸ We therefore consider that the impact of relatively small stamp price increases in triggering material e-substitution is relatively limited and that the likelihood for further e-substitution is unclear.
- 4.20 In addition, there may be several factors that affect the likelihood of e-substitution for certain customers or mail types. For example:
- a) Many users have a revealed preference for using physical post over electronic communications for those items they continue to send via post, despite the substantial differences in the relative per unit costs of each. This may go beyond preference in the case of a user with a physical or other disability, which impacts on the use of electronic services.
 - b) A lack of e-literacy could be a barrier to some consumers or SMEs using electronic alternatives (though this is relevant for a very small and diminishing proportion of customers).
 - c) Additionally, it is likely that there will remain a proportion of letters for which digital alternatives are not a good alternative (e.g. due to Government and regulatory

⁴⁵ Switching to a digital alternative may have upfront costs for some consumers – for example buying a smart phone or putting in place an electronic customer communications platform (such as a business investing in new systems). However, for consumers who already have the means of using an electronic alternative, the incremental cost is very low and would be substantially cheaper than using postal services.

⁴⁶ Ofcom, 2022. [Digital exclusion: A review of Ofcom's research on digital exclusion among adults in the UK](#), p. 5.

⁴⁷ Royal Mail has informed us that the impact of price changes on volumes and revenues is being carefully monitored.

⁴⁸ See, for example, paragraph 4.25.

requirements for certain types of paper correspondence). We also note that Royal Mail has estimated that e-substitution rates are higher for transactional and advertising mail than for social mail,⁴⁹ suggesting that e-substitution is more likely for certain letter types.

- 4.21 Based on the above, absent very significant price increases, it is not clear that Royal Mail's prices have a significant impact on the rate of e-substitution. We therefore have limited evidence that e-substitution represents a meaningful constraint on Royal Mail's pricing.

Price sensitivity

- 4.22 To the extent that consumers are so sensitive to price increases that it would be unprofitable for Royal Mail to increase its Second Class stamp price, this could act as a constraint on Royal Mail's pricing behaviour. We have therefore considered the available evidence on whether consumers would respond to stamp price increases by materially reducing their use of Second Class letters, such as to make the price increase unprofitable. Consumers may respond to the price increase by switching to a different service, by substituting to electronic communications, or may alternatively respond by choosing not to send any communication.
- 4.23 We have primarily considered Royal Mail's own estimates of price sensitivity (i.e., the price elasticity of demand).⁵⁰ Royal Mail's own price elasticity estimates suggest that social and transactional mail are price inelastic, meaning that, for example, a 5% increase in price would reduce this source of demand for mail by less than 5%, which suggests that such a price increase is likely to be profitable.^{51 52}
- 4.24 This estimate suggests that Royal Mail's prices are not constrained due to consumers' price sensitivity. However, the estimate does not specifically assess Second Class mail. It is also based on data from 2019 and Second Class stamp prices have increased since then, while letter volumes have fallen further. Therefore, it may not accurately indicate current pricing constraints on Royal Mail's Second Class stamp prices.
- 4.25 Nevertheless, the fact that Royal Mail has increased its Second Class standard letter prices over time (prices have increased in nominal terms by 23% since 2019) indicates that these price increases have been profitable. Indeed, according to Royal Mail's internal documents, price increases for standard letters are generally expected to be profitable. For example:
- a) [REDACTED].
 - b) [REDACTED].⁵³

⁴⁹ Royal Mail response dated 23 January 2023 to s.55 Notice, [REDACTED]

⁵⁰ This is defined as the ratio of the percentage change in volume to a percentage change in price.

⁵¹ [REDACTED]

⁵² [REDACTED]

⁵³ Royal Mail response dated 23 January 2023 to s.55 Notice, [REDACTED]

Supply-side constraints

- 4.26 Given declining volumes and structural changes in consumer behaviour with respect to sending letters, we consider it unlikely that there will be another end-to-end entrant of sufficient scale and scope to provide a significant competitive constraint to Royal Mail in the foreseeable future. Following Whistl's exit in 2015, there has not been any material entry to end-to-end delivery of standard letters at a national scale.

Provisional conclusion on standard letters

- 4.27 Royal Mail continues to face limited competitive constraints on its pricing of standard letters. It remains a monopolist in the provision of end-to-end services for single piece standard letters and we have no evidence that another end-to-end entrant of sufficient scale and scope would provide a competitive constraint to Royal Mail in the foreseeable future.
- 4.28 The constraint exerted by alternative services is not meaningful as these services either do not present appropriate alternatives for the majority of consumers (e.g., metered mail) or are not constrained by alternatives that do not involve Royal Mail at retail or wholesale levels (e.g., First Class stamped), or both.
- 4.29 Moreover, whilst Royal Mail may be cautious in implementing large price increases to avoid incentivising consumers to send their communications by alternative electronic means, the evidence we have reviewed suggests that e-substitution does not represent a meaningful constraint on Royal Mail's ability to profitably raise prices for single piece letters (particularly with respect to smaller price increases).
- 4.30 We therefore remain of the view that, overall, Royal Mail faces only limited constraints on its prices for standard letters. As a result, we consider that we cannot rely on competition alone to protect consumers from significant price increases in Second Class stamps for standard letters, such that there is a risk that prices could become unaffordable. We go on to assess affordability in section 5 below.

Large letters

Context

- 4.31 The term 'large letter' refers to Royal Mail letter services weighing no more than 750g and with maximum dimensions not exceeding 35.3cm in length, 25cm in width, and 2.5cm in thickness. As well as being used to deliver larger paper items, large letters are also used for sending other lightweight, flat items.
- 4.32 Services within the large letter sector mirror those set out above for standard letters, i.e., there are stamped (First and Second Class), meter and online variants. Large letters

accounted for a relatively small proportion (around [X]%) of total letter volumes in 2022-23.⁵⁴

4.33 Only Second Class stamped large letters are currently subject to the safeguard cap. However, Second Class large letters are currently part of a basket cap along with Second Class small parcels up to 2kg, unlike Second Class stamped standard letters (which are subject to a cap that applies only to them).

4.34 The prices of large letter services vary by weight step, as shown in Table 1.

Table 1: Prices for Second Class large letters by weight step, 2023-24

Weight	Price (£) – online and offline		
	First Class (standard delivery)	Second Class (standard delivery)	Second Class (Signed For delivery)
0-100g	£1.60	£1.15	£2.65
101-250g	£2.25	£1.85	£3.35
251-500g	£2.95	£2.40	£3.90
501-750g	£3.30	£2.70	£4.20

Source: Royal Mail online and Post Office Price Guides, effective from 3 April 2023

4.35 Royal Mail remains a near-monopolist in Second Class stamped large letters, with an estimated volume share of over 96% in end-to-end delivery. Since 2019-20, large letter volumes have been relatively volatile. They peaked in 2020-2021, likely caused by the increase in e-commerce during the pandemic,⁵⁵ but are now lower than in 2019-20. Volumes of large letters are significantly higher for the lowest weight steps (up to 250g) than the higher weight steps (in 2022-23, large letters [X] accounted for [X]% of total large letter volumes).⁵⁶

Demand-side constraints

4.36 A consumer or business considering sending a Second Class large letter using a stamp has, in theory, the following main alternative options:

- sending the item using a different Royal Mail service (e.g., First Class stamp, signed for, tracked, or Second Class meter/on account if sufficient volumes);
- reformatting the item so that it can be sent as a standard letter;
- sending by courier / alternative parcel operator; and/or
- not sending the item by mail, for example instead sending it by an alternative electronic form of communication.

⁵⁴ Total standard and large letter volumes (stamped and meter). Royal Mail Regulatory Financial Reporting Information.

⁵⁵ Large letters are used to send documents as well as physical services that fit the specified dimensions and weight limits.

⁵⁶ Across both First and Second Class. Royal Mail Regulatory Financial Reporting Information.

Sending the item using a different Royal Mail service

4.37 As for standard letters, the First Class stamp, “signed for” and tracking alternatives are more expensive for all weight steps (see Table 1 above) and are thus likely to exert a weak constraint on Second Class stamped prices for large letters. Alternative Royal Mail payment methods for Second Class large letters are only suitable for customers with higher volume mail needs. In any case, and as for standard letters, these alternative services are provided by Royal Mail, rather than other postal operators. They would therefore not be expected to place an effective competitive constraint on Royal Mail’s Second Class stamped large letter pricing.

Reformatting the item

4.38 Consumers sending a large letter-sized item may be able to reformat the item so that it could be sent as a cheaper standard letter. Standard letter prices may therefore, to some extent, constrain the prices for large letters. It should be noted, however, that this lower cost alternative is only a suitable option for some items sent by large letter (and would not be suitable for, say, A4 official or legal documents which should not be folded). Moreover, this option would only be an alternative for documents/objects not exceeding 100g in weight (i.e. the maximum weight of a standard letter). We accordingly consider that reformatting presents an alternative on very limited occasions.

4.39 As of April 2023, the differential between a Second Class standard letter and a large letter weighing up to and including 100g is 53% (40 pence). Large letter volumes have shown some increase during this time despite a widening price differential (although as noted above, are now lower than in 2019-20), such that people sending large letters appear to prefer that service even though it has become proportionately more expensive than a standard letter. We would therefore expect that further moderate widening of the price differential between these service sets is unlikely to trigger significant additional reformatting. We accordingly consider the constraint on large letter pricing from standard letters is likely to be weak.

4.40 In addition, standard letters are provided by Royal Mail rather than other postal operators, and so (as above) would not be expected to place an effective competitive constraint on Royal Mail’s Second Class large letter stamp pricing.

Sending the item using an alternative operator

4.41 Consumers sending a large letter sized item could instead use an alternative parcel delivery service provided by an alternative operator. These services are typically more expensive than Royal Mail’s large letter services (see Table 3 below) and are therefore unlikely to act as a constraint in the majority of cases.

4.42 Evri has recently launched a ‘postable’ parcel delivery service, which it describes as “anything that fits easily through a letterbox”, particularly “letterbox-friendly parcels and

large letters”.⁵⁷ Evri has confirmed that one of the reasons for introducing the ‘postable’ service was to compete with Royal Mail.⁵⁸

- 4.43 The maximum dimensions of Evri’s postable service are similar to Royal Mail’s,⁵⁹ but it has a higher weight limit (1kg) and a tracking facility. Evri’s service is priced exactly the same as a Second Class 750g large letter, at £2.70.⁶⁰ This service is also available for a discount, at £2.62, for delivery to an Evri pick up point rather than the recipient’s address.⁶¹ However, Evri does not offer lower-priced versions of this service for smaller sizes or lower weight steps and is therefore unlikely to act as a significant constraint on Royal Mail’s pricing in relation to its smaller and lighter large letter services.
- 4.44 There is some evidence from Royal Mail’s internal documents that alternative operators act as a constraint on Royal Mail’s pricing of large letters, in particular for the heavier weight steps. For example, in one internal document Royal Mail makes a direct comparison between its large letter prices and similar offerings provided by alternative parcel operators.⁶²

E-substitution

- 4.45 As discussed in the context of standard letters, e-substitution could act as a constraint on Royal Mail’s pricing behaviour if higher stamp prices could make post a less attractive option, thus triggering further e-substitution. Although we expect that the trend of letter users migrating to online alternatives also affects large letters to some extent, we believe that the constraint from e-substitution is likely to be even weaker for large letters than for standard letters. This is because consumers and businesses are more likely to use large letters to send documents that have to be sent via post (e.g., formal documents they do not wish to fold) or to post small, flat physical items. Likewise, marketplace sellers⁶³ are likely to use large letters to post purchased items.
- 4.46 Absent very large price increases, it is not clear that Royal Mail’s prices have a significant impact on the rate of e-substitution for large letters. Indeed, the significant increases in stamped large letter prices (around 40% in nominal terms for the three weight steps up to 500g since 2019) do not appear to have led to a marked increase in e-substitution.

⁵⁷ See <https://www.evri.com/our-services/postable> [accessed 13/06/2023].

⁵⁸ Evri response dated 16 May 2023 to s.55 Notice.

⁵⁹ For Evri maximum width is 23cm (vs 25cm for Royal Mail); maximum length is 35cm (vs 35.3cm for Royal Mail) and; maximum thickness is 3cm (vs 2.5cm for Royal Mail).

⁶⁰ Price correct as of June 2023. See <https://www.evri.com/our-services/postable> [accessed 13/06/23]

⁶¹ Evri’s network of pick-up and drop-off points has been expanding but still falls behind that of Royal Mail’s (see Table 4). Evri has recently entered a trial for a partnership with the Post Office which allows consumers to both drop off and pick up Evri parcels from selected Post Office branches (see paragraph 4.74).

⁶² Royal Mail response dated 23 January 2023 to s.55 Notice, [🔗]

⁶³ Marketplace sellers are consumers who run an online business selling items through platforms such as eBay, Amazon or Vinted.

Price sensitivity

- 4.47 Market research suggests that many residential customers are not particularly price sensitive. Royal Mail elasticity estimates are also low (see paragraph 4.23 above). This suggests that Royal Mail could implement further price increases without having a significant impact on volumes.
- 4.48 Figure 3 above summarises how Royal Mail's nominal prices for large letters have evolved over the past five years. As that chart demonstrates, prices have increased significantly compared to 2019 across all weight steps, which suggests that these price increases have been profitable.
- 4.49 Further, Royal Mail's internal documents suggest that, as for standard letters, price increases for large letters are generally expected to be profitable. For example:
- a) [REDACTED]
 - b) [REDACTED]
 - c) [REDACTED].⁶⁴

Supply-side constraints

- 4.50 Despite some evidence of nascent competition in the large letters segment (i.e., Evri's expansion into this segment with its postable service and similar pricing to Royal Mail's heaviest large letter service), Royal Mail remains a near-monopolist in Second Class stamped large letters with an estimated volume share of over 96% in end-to-end delivery. Other providers do not provide similarly priced services to Royal Mail's lower size/weight step large letter services, despite significant price increases by Royal Mail since 2019.
- 4.51 We therefore consider that Royal Mail's pricing of stamped Second Class large letters is not constrained by existing competitors, nor by the threat of future entry or expansion.

Provisional conclusion on large letters

- 4.52 Royal Mail remains a near-monopolist in the provision of end-to-end services for single piece large letters. Despite some evidence of nascent competition, particularly at the highest weight step, we consider that Royal Mail's pricing of stamped Second Class large letters continues to be unconstrained by current competitive forces or the threat of future entry and expansion.
- 4.53 As discussed above, alternative services or e-substitution are unlikely to pose a meaningful constraint on Royal Mail's pricing of large letters. As a result, we consider that we cannot rely on competition alone to protect consumers from significant price increases. We consider, therefore, that there is a risk that prices could become unaffordable without a safeguard cap. We go on to assess affordability in Section 5 below.

⁶⁴ Royal Mail response dated 23 January 2023 to s.55 Notice, [REDACTED]

Parcels

Context

- 4.54 The parcels market can be split into three segments⁶⁵:
- a) **Consumer to business/consumer (C2X)** – these are largely single piece items from consumer to consumer (C2C), or consumer to business (C2B). The C2C segment covers parcel delivery services that can be used for sending an individual parcel and are available for purchase by individual consumers.⁶⁶ For example, a person sending a birthday present to a relative or an individual online marketplace seller⁶⁷ sending an item to a buyer.⁶⁸
 - b) **Business to consumer (B2C)** – these are deliveries from business to consumer, for example an online retailer sending items bought by online customers. These are generally deliveries that are part of bulk contracts between a business and a parcel operator.
 - c) **Business to business (B2B)** – these are generally bulk deliveries from a business to other businesses, for example a clothes manufacturer receiving fabric from a supplier, or a publisher receiving paper and ink in bulk.
- 4.55 The parcels market has been fast-growing, and the main focus of competition continues to be found in the B2C segment, reflecting the growth in online shopping. As we concluded in our 2022 Review of Postal Regulation, the B2C segment is broadly competitive.
- 4.56 The C2X segment is relatively small compared to B2C, but still accounts for approximately 10% of total parcels volumes across operators and is also growing (but at a slower rate than B2C).⁶⁹ Royal Mail is required by its universal service obligations to provide a service for the collection and delivery of single piece parcels up to 20kg (and within specified maximum dimensions). Such parcels fall within the C2X segment (see Figure 6 below for a summary of these services).
- 4.57 We noted in our 2022 Review of Postal Regulation statement that in the C2X segment, competition has grown in recent years, and we expect that it will continue to grow. While

⁶⁵ For the purposes of the data presented in this section, we have defined a parcel as an addressed postal item that is delivered end-to-end and: (a) is not a letter or a large letter; (b) weighs no more than 31.5kg; and (c) can be lifted by a single average individual without mechanical aids. Parcel services form part of a broad set of delivery services used by residential and business consumers in the UK, such as two-person and pallets delivery (for large and heavy items) and more generally the logistics services that are used for business supply chains. In contrast to parcel services, these other services do not involve postal items.

⁶⁶ This definition also includes services that are sold through parcel reseller websites, such as Parcels2Go, as well as parcels services that are resold to users at a discounted price through marketplace websites, such as eBay, Etsy or Vinted. This definition excludes items sold on Amazon Marketplace that are delivered by Amazon Logistics. This is because Amazon Logistics delivery services are only available to those selling services through the Amazon website and are also required to be purchased in combination with other Amazon services (such as warehousing).

⁶⁷ 'Marketplace sellers' refers to consumers who sell items

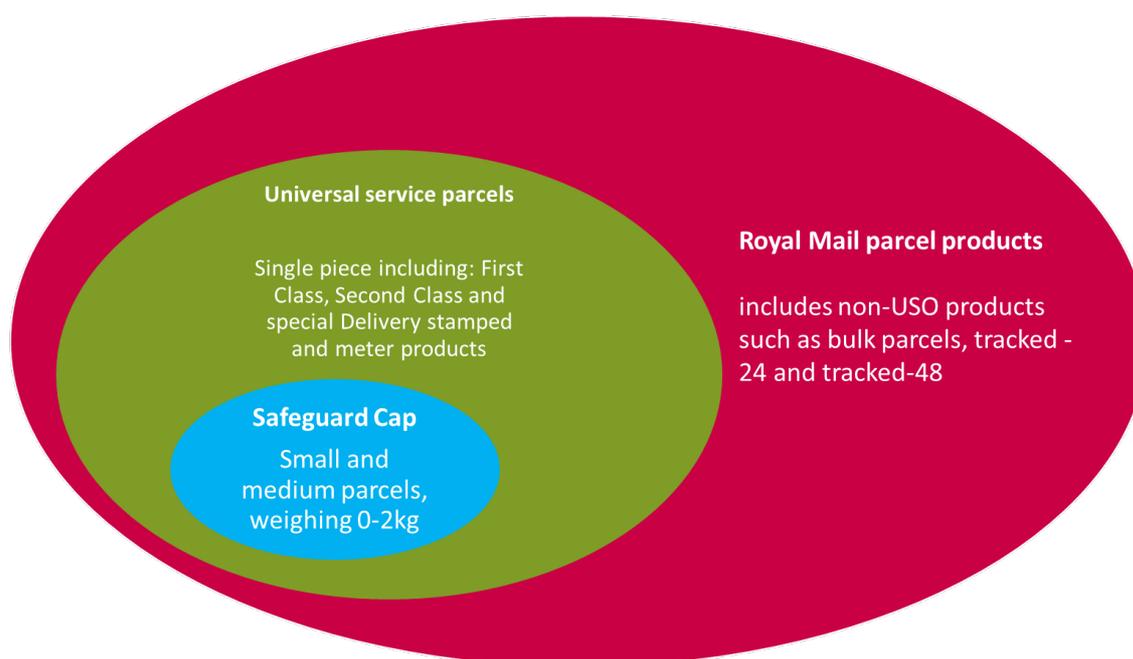
⁶⁸ This definition also includes returns of items purchased online to the extent that these do not represent returns that are pre-paid by the retailer or marketplace seller, which are typically considered as B2C.

⁶⁹ Ofcom, 2022. [Statement: Review of Postal Regulation](#), paragraph 6.11

Royal Mail still retains significant competitive advantages, alternative operators have capitalised on the growth of smaller online and marketplace sellers to scale up their operations in C2X.⁷⁰

- 4.58 In our 2018-19 review of safeguard caps, we concluded that Royal Mail enjoyed a significant degree of pricing power in small and medium parcels up to 2kg and, in particular, small and lightweight items that can fit through a letter box.⁷¹ We concluded that, absent regulation, there were insufficient competitive constraints to prevent Royal Mail from materially raising prices. We therefore decided that single piece Second Class parcels up to 2kg should be subject to a safeguard cap.

Figure 6: Royal Mail parcel services by category (not to scale)



- 4.59 We are aware that, since our 2018-19 review, competition in the C2X segment of the parcels market, and in particular in the lighter weight steps, has grown. As such, in our market assessment below, we are particularly conscious of the need to understand whether alternative operators have grown to a point where they may now be considered to exert a meaningful competitive constraint on Royal Mail and, if so, the potential impact of those constraints on Royal Mail's pricing.

⁷⁰ Ofcom, 2022. [Statement: Review of Postal Regulation](#), paragraphs 6.38-6.46.

⁷¹ Royal Mail segments its parcel offerings as small parcels (up to 2kg and with maximum dimensions 45cm x 35cm x 16cm) and medium parcels (up to 20kg with maximum dimensions 61cm x 46cm x 46cm). The safeguard cap applies to all single piece Second Class stamped small parcels and to medium parcels that weigh up to 2kg.

The relevance of other operators has increased since our 2018-19 review

Alternative operators have increased their volume shares in lighter C2X parcels

- 4.60 Royal Mail is the main provider of single piece parcel services serving the C2X segment, especially in relation to services weighing up to 2kg. Besides Royal Mail, operators including Evri, DHL, Yodel and DPD offer a range of C2X services across weight steps with varying delivery timescales, maximum dimensions and additional features, such as tracking facilities and proof of delivery.
- 4.61 However, while these alternative providers offer C2X services, it is not their key area of focus; they tend to focus more on B2C services. There is also variation between them in the extent to which they serve the C2X market, particularly for smaller parcels.
- 4.62 As of 2021-22, Royal Mail continues to account for a high (if declining), percentage ([X]%) of total volumes for single piece parcels weighing <2kg. Evri is Royal Mail's closest competitor in single piece C2X parcels (and, in particular, in relation to the types of parcels which are subject to the safeguard cap). Evri accounts for approximately [X]% of volumes. All other operators have individual volume shares well below [X]%.

Table 2: Volume shares of parcels up to 2kg by parcel operator, 2019-20 to 2021-22

[X]

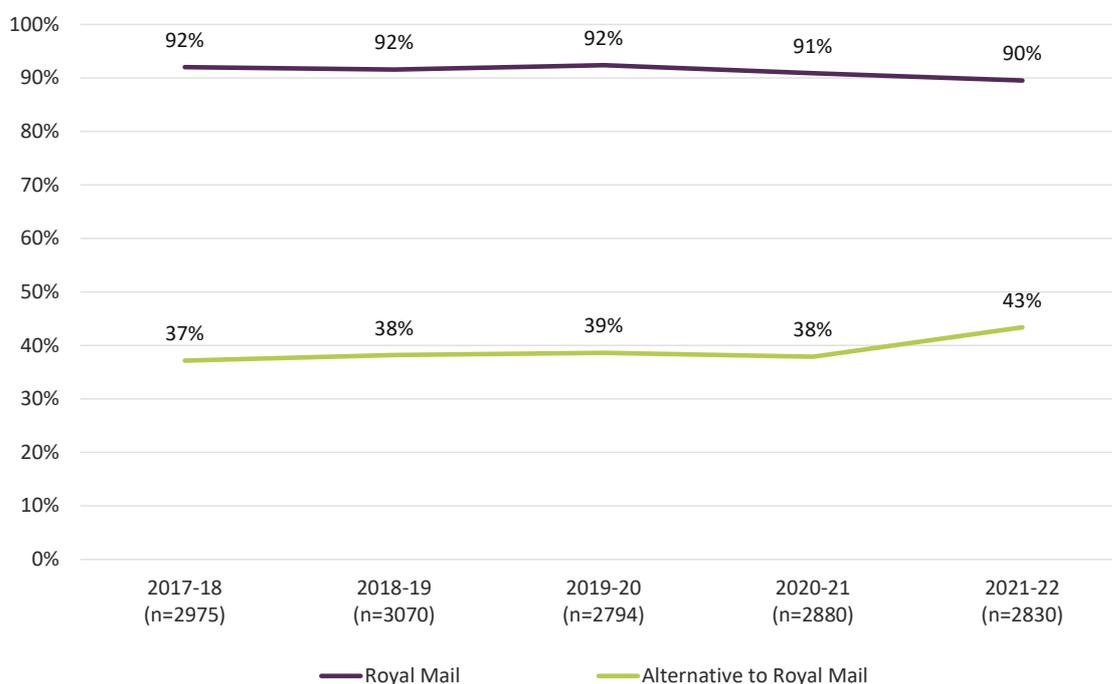
Source: Ofcom analysis of volume and revenue data submitted by Royal Mail and other operators.

Reported use of alternative operators has increased

- 4.63 The increased competition in the C2X segment is also borne out in recent consumer research, which shows that postal users are increasingly using alternative parcel operators to Royal Mail.⁷²

⁷² Throughout this consultation, when referring to the results of our Residential Postal Tracker, we use the term 'postal users'. This is because consumers who say they never use the postal service are excluded from the sample.

Figure 7: Reported usage of parcel operators for sending parcels in the past month, 2017-18 – 2021-22



Source: Residential Postal Tracker, QD5 (Which of the following companies have you used to send parcels in the last month?). Base: Those sending parcel post in the last month – sample sizes shown in chart.

4.64 Figure 7 above shows that reported usage of Royal Mail for sending parcels has remained stable since 2017-18, while usage of alternative operators (i.e. any non-Royal Mail operator) significantly increased between 2020-21 and 2021-22. Marketplace sellers are particularly likely to report using alternative operators to Royal Mail to send a parcel (71% report having done so).

Competing operators have raised their profile with consumers

4.65 Royal Mail has an incumbency advantage as the universal service provider, with alternative operators being relatively new to C2X parcels by comparison. Royal Mail has therefore had a longer period to build its brand and reputation in this area. Royal Mail’s own market research shows that [✂].

4.66 However, awareness of other operators has grown significantly in recent years, driven in part by increased interactions with other operators when purchasing services online. For example, the Residential Postal Tracker shows that the proportion of postal users who remember receiving a parcel or a letter delivered by an alternative operator to Royal Mail

has increased since 2017-18, while the proportion who remember receiving a parcel or letter delivered by Royal Mail has decreased during the same time period.⁷³

Alternative operators offer comparable, competitively priced alternatives to Royal Mail’s parcel services

4.67 Alternative operators have been able to respond to the emergence of more price-sensitive C2X senders (in particular online marketplace sellers) by offering comparable, competitively priced alternatives to Royal Mail at weight steps up to 2kg (as set out in Table 3 below).⁷⁴

Table 3: Cheapest delivery prices for comparable C2X parcel services⁷⁵

	Royal Mail Second Class small (2-3 days)	Royal Mail Second Class medium (2-3 days)	Evri (2-4 days, tracked)*	Yodel (within 2 days, tracked)	DPD Local (1-2 days, tracked)**	DHL Parcel UK (Next day, tracked)***
0-1kg	£2.99	£4.49	£2.99	£2.91	£7.67	£7.89
1-2kg	£2.99	£4.49	£4.44	£3.91	£7.67	£7.89

Source: Operators’ websites (correct as of June 2023). Royal Mail prices correspond to online prices. The respective prices for small and medium parcels purchased at the Post Office are £3.49 and £5.49.

*Evri offers a cheaper option for these services (£2.78 for 0-1kg and £3.88 for 1-2kg) if the recipient collects the parcel from an Evri pick-up point. As noted above, Evri also offers a cheaper ‘postable’ service for parcels weighing up to 1kg that will fit through a letterbox (£2.70 for delivery direct to the recipient’s address, £2.62 for delivery to an Evri pick-up point).

** DPD Local offers a cheaper option (£4.79) if the recipient collects the parcel from a DPD pick-up point.

***The weight limit for DHL parcels at this price is 15kg. DHL also offers cheaper options (ranging from £2.79 to £5.89) depending on where the parcel is dropped off or collected.

4.68 Similarly, operators have differentiated their services to attract different customer types, in particular marketplace sellers.⁷⁶ For example, the standard services offered by competing operators all include tracking, which is not available on Second Class parcel services subject to the safeguard cap. For reference, Royal Mail’s prices for its tracked services are more expensive (£3.45 for small parcels up to 2kg and £5.15 for medium parcels up to 2kg) than the comparable Yodel and Evri services.⁷⁷

⁷³ Between 2017-18 and 2021-22, the proportion of postal users who remember having received a parcel or letter delivered by Evri (previously Hermes) increased from 45% to 59%. For DPD, the proportion increased from 35% to 44%, for DHL from 33% to 40%, and for Yodel from 35% to 39%. For Royal Mail, the proportion decreased from 84% to 72%. See Residential Postal Tracker (2017-18 and 2021-22), Q12.

⁷⁴ For example, an internal document of Evri’s describes microshippers (i.e., users that are concentrated around hobbyists, small enterprises and side hustlers) as price sensitive. Another internal document sets out that Evri’s current strategy is to target microshippers as opposed to those sending ad hoc gifts and occasional marketplace sales. Evri, response to s.55 Notice dated 16 May 2023.

⁷⁵ Royal Mail’s prices for the services included in this table are VAT exempt. Listed prices for other operators include VAT.

⁷⁶ For example, an internal document of Evri’s mentions that tracking is one of the service characteristics valued by “microshippers.” Evri, response to s.55 Notice dated 16 May 2023.

⁷⁷ Online prices for Royal Mail’s ‘Tracked 48’ service.

- 4.69 Additionally, DPD, DHL and Yodel provide delivery services which have delivery speeds that are generally faster than Royal Mail's Second Class services, as shown in Table 3 above.
- 4.70 As such, depending on a consumer's preferences, the prices set out in Table 3 do not fully reflect the ways in which alternative providers may provide an increasing competitive constraint on Royal Mail for C2X parcels, including those up to 2kg. For example, for customers who value tracking, the availability of competitively priced tracked parcel delivery services from other providers significantly constrains Royal Mail's pricing of the Second Class service.

Alternative operators have materially expanded their networks of access points

- 4.71 Royal Mail's network of access points, from which users can send single piece parcels, remains the most extensive. Users can send Second Class small- and medium-sized parcels up to 2kg through the Post Office, which has around 11,500 locations across the UK. In addition, consumers can send parcels via a postbox if the parcel fits and they have been able to pay the correct postage, substantially increasing the number of Royal Mail's access points.⁷⁸ Royal Mail also allows for collection of parcels from Delivery Offices if they have not been successfully delivered to the delivery address.
- 4.72 In contrast, the networks of alternative providers are smaller than that of Royal Mail. In particular, alternative networks tend to have lower coverage in rural areas compared to urban areas and, as a result, Royal Mail is often likely to still be the most easily accessible option in many rural areas. Even outside of rural areas, consumers will often know the location of their local Post Office but may be less aware of the collection or delivery point for an alternative provider.⁷⁹
- 4.73 Nevertheless, alternative parcel operators have been growing their network of access points substantially, as shown in Table 4 below. Indicatively, DPD's network of access points has more than doubled since 2019 and Evri's network has increased by more than 50% over the same time period.
- 4.74 In addition, the Post Office no longer has an exclusivity agreement with Royal Mail. This has led the Post Office to partnering with other operators to offer 'click and collect' services in at least 5,000 branches across the UK.⁸⁰ The Post Office has also more recently started a trial with Evri to offer a variety of services, including enabling customers to select

⁷⁸ Royal Mail's network also includes around 1,350 Parcel Postboxes that can be used for dropping off parcels with maximum size 44cm x 35cm x 16cm. See <https://www.royalmail.com/d8/parcel-post-boxes> [accessed 06/06/23]

⁷⁹ Evri's internally commissioned research on Royal Mail's advantages over Evri found that Evri's main advantage is brand reputation and reliability. Evri, response to s.55 Notice dated 16 May 2023.

⁸⁰ In August 2021, the Post Office signed an agreement with DPD to provide Click and Collect services in approximately 1,500 branches across the UK (see: <https://www.onepostoffice.co.uk/secure/latest-news/general-news/post-office-partners-with-dpd-to-roll-out-click-and-collect-services/>). In September 2021, the Post Office also signed a contract with Amazon to provide Click and Collect services (see: <https://www.onepostoffice.co.uk/secure/update-on-amazon-pudo-trial-september-2021/>). In September 2022, the Post Office also partnered with DHL Express to provide Click and Collect services (see: <https://www.onepostoffice.co.uk/secure/latest-news/our-business/introducing-carrier-3/>).

a Post Office branch as a drop-off or pick-up location for Evri parcels.⁸¹ [REDACTED]. Evri's initial target is for its services to be available in 500 branches by June 2023, with an aspiration of [REDACTED] in future.⁸²

- 4.75 Furthermore, customers' sending behaviour is changing as they become more willing to purchase delivery services online, where Royal Mail's physical network advantages and long-established position of incumbency may play a reduced role. This would be consistent with increased consideration of alternative providers.
- 4.76 According to Royal Mail's own consumer research, the proportion of customers paying for postage at the Post Office declined between Q4 2020-21 and Q2 2022-23 (from [REDACTED]% to [REDACTED]%), while the proportion using Royal Mail's app or website to purchase postage has increased over the same time period (from [REDACTED]% to [REDACTED]%). Marketplace sellers appear particularly likely to use Royal Mail's app or website to purchase postage ([REDACTED]% of them report doing so in Q2 2022-23).⁸³

⁸¹ More specifically, Evri entered into a trial agreement with the Post Office in December 2022 to trial PO locations acting as an Evri ParcelShop. See: https://corporate.postoffice.co.uk/en/blogs/2023_01/post-office-secures-new-agreement-with-evri

⁸² Evri, response to s.55 Notice dated 16 May 2023.

⁸³ Royal Mail response dated 23 January 2023 to s.55 Notice, [REDACTED]

Table 4: Number of access points (changes since 2019 in parentheses)

	Parcel operator	# of access points	Access points location
Post Office	Royal Mail/ParcelForce, and some services from other operators in some branches	11,500 ⁸⁴	Post Office branches/outlets
CollectPlus	Yodel, DHL, DPD, FedEx, InPost	10,000 (+3,000)	Newsagents, convenience stores, supermarkets, petrol stations
Evri ParcelShop	Evri	7,000 (+2,500)	Convenience stores, lockers
DPD Pick Up	DPD	6000 (+3,500)	Convenience stores, pharmacies, retail shops
UPS Access Point	UPS	2,800	Convenience stores, supermarkets, petrol stations
InPost parcel lockers	InPost, DHL, Evri	4,300 (+3,100)	Convenience stores, supermarkets, petrol stations
DHL Parcel UK Service Points	DHL Parcel UK	3,500	Convenience stores
DHL Express Service Points	DHL	1,300 (+100)	High street/retail outlets

Source: Parcel operator websites (correct as of June 2023).

Assessing the strength of the competitive constraints

Royal Mail’s prices for single piece Second Class parcels up to 2kg reflect competitive constraints

4.77 Figure 4 in Section 2 shows nominal prices of Second Class parcels (purchased online and at the Post Office) since 2019. This shows that increases in parcel prices have been relatively modest. This is particularly the case when comparing the price increases for parcels to

⁸⁴ People can also use postboxes and parcel postboxes to send parcels, provided that the parcel fits, they have purchased the appropriate postage, and are happy not to receive proof of postage. Postboxes are not included in the reported number. Several operators also offer home collection for parcels.

those for standard letters and large letters. This is understandable as the volume of parcels has been growing, which supports economies of scale while the volume of letters has been falling. In addition, the pattern of pricing suggests growing competitive constraints.

4.78 Not only have price increases been relatively modest, but Royal Mail has decreased its prices for small and medium sized parcels when the consumer pays online for the service, rather than using stamps.⁸⁵ We consider that this is indicative of a strengthening of the competitive constraints on Royal Mail in this area. We note however that Royal Mail's internal documents suggest that it offers lower prices on its online platforms as its costs of providing services online are lower.⁸⁶

4.79 In addition, even though Royal Mail has increased large letter prices significantly, its prices for parcels up to 2kg have been such that the basket cap does not appear to have had any substantive impact on its pricing. Indeed, as shown in Figure 1 in section 2, Royal Mail has had, and continues to have, significant headroom under the basket cap (over 20%) since the start of the current cap period.

The threat of using an alternative parcel operator constrains Royal Mail's pricing

4.80 As discussed above, there is evidence that the position of competitors in the C2X market, and their ability to compete against Royal Mail, including in the lighter weight parcels segment, has improved. Royal Mail's internal documents show that the threat of consumers switching to competing providers is one of the factors considered by Royal Mail in setting its pricing for parcels.

4.81 For example, [REDACTED].⁸⁷

4.82 [REDACTED].⁸⁸

4.83 Royal Mail's internal documents also show that Royal Mail closely monitors the prospect of expansion of its competitors in the single piece parcels sector and how its prices compare to those of its competitors. For example, [REDACTED].^{89 90}

4.84 This suggests that the competition Royal Mail faces in the market forces it to price so as not to lose customers to competing operators.

Other constraints

4.85 We have also considered whether alternative Royal Mail services (e.g., First Class, tracked or "Signed For" services) might pose a meaningful constraint on Royal Mail's Second Class parcel services. Given that these services are typically more expensive, and are also more

⁸⁵ The prices shown in the chart are nominal prices. Adjusting for CPI inflation, prices have fallen, for both small and medium parcels and whether paid for online or offline, since 2019.

⁸⁶ Royal Mail response dated 23 January 2023 to s.55 Notice, [REDACTED]

⁸⁷ Royal Mail response dated 23 January 2023 to s.55 Notice, [REDACTED]

⁸⁸ Royal Mail response dated 23 January 2023 to s.55 Notice, [REDACTED]

⁸⁹ Royal Mail response dated 23 January 2023 to s.55 Notice, [REDACTED]

⁹⁰ Royal Mail response dated 23 January 2023 to s.55 Notice, [REDACTED]

expensive than the comparable services offered by competing providers (see Table 3 above), we consider that alternative Royal Mail services exert only a weak constraint.

4.86 Likewise, meter services are also only likely to pose a weak constraint as they are an appropriate alternative only for high volume users due to the initial investment required.

4.87 Moreover, as parcels are typically used for sending physical services, substitution to electronic means of communication is unlikely to be a suitable option for the majority of users (except perhaps in certain circumstances where digital alternatives are available such as electronically transferring content as opposed to sharing content via a physical CD or DVD transmissible by post). As a result, the constraint posed by e-substitution is unlikely to be meaningful.

Provisional conclusion on Second Class parcels weighing up to 2kg

4.88 The evidence we have reviewed suggests that, although Royal Mail retains a strong position in the segment of the market related to parcels up to 2kg, the relevance of competing operators, notably Evri, has materially grown. This suggests that the market has become more competitive since our 2018-19 review and we expect that competition will continue to grow. Royal Mail's pricing behaviour over the past four years supports this.

4.89 We therefore consider that competition in the market would suffice to protect consumers from significant price increases, thus ensuring that prices remain affordable for the majority of consumers.

Consultation questions

Question 4: Do you agree with our analysis of the market in relation to Second Class standard letters and large letters? Please state your reasons and provide evidence to support your view.

Question 5: Do you agree with our analysis of the market in relation to Second Class parcels up to 2kg? Please state your reasons and provide evidence to support your view.

5. Assessment of affordability

- 5.1 In this section we set out our approach to assessing affordability of postal services. We then set out our evidence on affordability which we use to inform our assessment, followed by our conclusion on the affordability of current postal prices. This section constitutes the portion of our impact assessment where we consider the effect of potential changes in the price of the safeguarded services on consumers.
- 5.2 The analysis presented in this section informs our view on whether safeguard caps continue to be necessary in order to ensure the affordability of universal postal services. It also informs our view on the level at which the cap(s) should be set to ensure that the capped services remain affordable for consumers.
- 5.3 We have used the following sources of evidence to inform our assessment of affordability:
- a) Our Residential Postal Tracker (2022 results) quantitative research. In particular, we use this to understand how, and how frequently, consumers use postal services, and to understand the proportion of consumers who may experience affordability issues in relation to post.
 - b) Qualitative research (in-depth interviews with consumers, with a focus on consumers on lower incomes) to better understand any postal affordability issues consumers are facing. The research also provides additional context to the findings of the Residential Postal Tracker.⁹¹
 - c) Data from the ONS on household disposable income and expenditure.⁹² We use this to understand how much consumers spend on post as a proportion of their expenditure, how this differs by demographic group, and how incomes have changed since our previous review.

Approach to assessing affordability

Previous approach

- 5.4 In our 2013 review of postal affordability, we set out a consideration of how to understand whether postal services were generally affordable.⁹³ Our chosen test was to have regard to the consequences for a consumer of either sending post at current prices or choosing not to send post because of current prices. We noted that postal prices may be considered unaffordable for a consumer if they were to frequently suffer significant adverse consequences as a result of (a) the cost of sending post (for example, because of foregoing

⁹¹ We conducted 44 one-hour depth interviews (half online and half face-to-face) across the UK between March and May 2023. The sample included participants from a range of backgrounds but with a focus on those from lower incomes. We have published the qualitative research report alongside this consultation. [See Jigsaw, 2023. Residential Postal Affordability Research.](#)

⁹² ONS, 2022. [Family spending in the UK](#) (expenditure). ONS, 2023. [The effects of taxes and benefits on household income, disposable income estimate](#) (disposable income).

⁹³ Ofcom, 2013. [The affordability of universal postal services](#), section 3.

spend on other items); or (b) as a result of not sending post and foregoing the value of the communication.

5.5 We considered that a reduction in spending on essential items to afford post, or a reduction in spend on post to afford essential items, were appropriate proxies for understanding whether consumers had experienced significant detriment because of postal prices. The main source of evidence we used to understand this is our regular Residential Postal Tracker.⁹⁴ For this survey, consumers are asked (among other questions) whether they have had to:

- reduce their use of postage stamps in the past three months in order to afford essentials like food or heating; or
- cut back on essentials like food or heating in the past three months in order to afford postage stamps.

5.6 We also used this test in our 2018-19 safeguard caps review, alongside a consideration of other evidence including average disposable incomes, frequency of postal usage and average expenditure on postal services.

Our approach for this review

5.7 As we have previously noted, no single approach to affordability can be definitive about whether the price of a good or service is affordable or not.⁹⁵ This is, in part, because incomes and usage, and the extent to which consumers consider their usage to be essential, varies significantly between consumers. This makes it difficult to determine at a broad level whether something is affordable for consumers.

5.8 When assessing the affordability of postal services, it is important to consider the specific features of postal services compared to other essential services. These include the fact that average spend on postal services is significantly lower than on other essential services (and other communications services). Average expenditure on post represents 0.19% of total expenditure, while expenditure on telephone services (landline and mobile) is 1.81% and on energy 4.8%.⁹⁶ Further, postal users are not signed up to long term contracts with standing charges and can purchase services as a single item.

5.9 We consider that our previous test, that post is unaffordable for someone if they suffer significant detriment as a result of current prices, continues to be the most appropriate way to assess affordability in postal services. We also consider that understanding whether someone has reduced their spending on post because of the price of postal services, or has continued to purchase postal services but has had to cut back on other essential expenditure, remains an appropriate proxy for determining whether they have experienced significant detriment.

⁹⁴ See Ofcom, [Statistical Release Calendars](#), Residential Postal Tracker. Data for calendar year 2022 was published on 1 March 2023.

⁹⁵ See, for example, Ofcom, 2019. [Review of the Second Class Safeguard Caps 2019: Statement](#), paragraph 4.8.

⁹⁶ ONS, 2022. [Family spending in the UK](#).

- 5.10 This is because the results of this test can be interpreted taking into account that post represents a very small proportion of average spend, that affordability will vary according to a consumer's individual circumstances and views, and that some consumer groups may be more vulnerable than others in relation to the affordability of universal postal services.
- 5.11 However, the application of this test in practice is challenging. For example, we need to take account of the long term trends in letter volumes which have been declining year-on-year for a number of years and will likely continue to do so. This trend suggests that letters are already being substituted by other forms of communications, even during periods where the cost of letters is more or less static. Thus, a reduction in expenditure on post or a willingness to send post may be a weaker indicator of affordability than in the past.
- 5.12 We also recognise that the application of this test is made more complex by the wider economic environment and the increase in the cost of living. While inflation appears to have peaked, it remains high and it has led to a general increase in the cost of living, particularly for essential items such as energy and food.⁹⁷ Average total pay has not kept pace with inflation - total pay fell in real terms by 2% on the year in February to April 2023.⁹⁸
- 5.13 When prices of essential items increase, people typically seek to cut down on their discretionary spending to absorb these increases. Accordingly, the ONS found in May 2023 that more than two thirds (68%) of adults whose cost of living had increased report cutting back on non-essential items in response.⁹⁹ We know that postal users consider at least some of their spend on post to be discretionary or non-essential,¹⁰⁰ and we would therefore expect at a time of high inflation to see consumers reducing their spend on it, along with other non-essential items.
- 5.14 An increase in the proportion of consumers reporting a reduction in their spend on stamps to afford essentials may therefore not indicate an increase in postal affordability issues, but rather broader financial concerns arising from the increased cost of living. Similarly, it is difficult to determine whether there is any connection between changes in consumption and increases in postal prices. This is particularly important for us to consider because any changes we make to the safeguard caps must be led by the impact of changes in postal prices on affordability and not by the impact of prices of other items or services on affordability of postal services.

⁹⁷ ONS, [Cost of living insights](#) [accessed 19/06/2023].

<https://www.ons.gov.uk/economy/inflationandpriceindices/articles/costoflivinginsights/food>. Electricity prices rose by 67%, gas prices by 130%, and food prices by 18% between February 2022 and February 2023.

⁹⁸ ONS, 13 June 2023. [Average weekly earnings in Great Britain: June 2023](#) [accessed 13/06/2023].

⁹⁹ ONS, [Cost of living insights: Spending](#) [accessed 13/06/2023].

¹⁰⁰ For example, 42% of postal users agree that they only use the post to send greetings cards (Residential Postal Tracker 2022, QC3_6). Our qualitative research also found that many participants did consider postal services important, but not essential for day-to-day communication (see Jigsaw, 2023. Residential Postal Affordability Research, section 3.1)

- 5.15 As noted in more detail below, postal services represent both a very small proportion and a very small absolute amount of consumers' total expenditure; on average, 0.19% of weekly household expenditure.¹⁰¹
- 5.16 This means that even a significant reduction of 30% to the standard letter safeguard cap would save a household that purchases on average six Second Class stamps per month around £16 per year.¹⁰² In contrast, the energy price cap that will apply from 1 July 2023 means that the average household energy bill (for those on the energy price cap) will be £2,074 per year.¹⁰³
- 5.17 Given the above, it is clear that that postal prices at their current level are not a major determinant of consumers' costs of living, and that it is not possible for an adjustment to postal prices to materially redress existing wider cost of living concerns. As noted above, we have a duty to carry out our functions in a way that we consider will secure a universal postal service, and to have regard to the need for the universal service to be financially sustainable. However, we are also conscious that real-terms increases in postal prices would likely further contribute to wider cost of living concerns.
- 5.18 As regards the aspect of our affordability test which asks whether consumers have cut back on essential items to afford postal services, this also presents some challenges to interpretation given the low average spend on post.
- 5.19 Notwithstanding the challenges discussed above, we have conducted further consumer research to give us a deeper understanding of postal affordability issues consumers may be facing, and to provide us with context to the Residential Postal Tracker findings on affordability.

Consultation question

Question 6: Do you agree with our approach to assessing affordability of postal services? Please state your reasons and provide evidence to support your view.

Assessment of affordability

Use of and expenditure on postal services

- 5.20 Our consumer research shows that consumers perceive that they are sending fewer items in the post over time.¹⁰⁴ In our Residential Postal Tracker, participants were asked if they were sending more, less, or the same amount of mail as two years ago. For each of the eight types of mail asked about, the proportion of participants saying that they are sending less than they were two years ago was higher than the proportion reporting that they are

¹⁰¹ ONS, 2022. [Family spending in the UK](#).

¹⁰² This as an illustrative example, and is not intended to reflect the average number of stamps purchased by a household in a month.

¹⁰³ Department for Energy Security and Net Zero, May 2023. [Policy paper: Energy Price Guarantee](#) [accessed 13/06/2023].

¹⁰⁴ The findings are based on survey participants' own recollections, which are unlikely to be precisely accurate, so should be treated with some caution.

- sending more. The net decrease was particularly high for personal letters (-21), invitations/greetings cards/postcards (-20), formal letters (-19) and payments for bills/invoices/statements (-18). Parcels have seen a smaller net decrease (-7 for larger parcels and -6 for smaller parcels).¹⁰⁵
- 5.21 Consumers' perceived reduced use of postal services is borne out by actual volumes from Royal Mail. Standard letter volumes decreased by [X]% per year on average between 2019-20 and 2022-23, while volumes of large letters and parcels weighing up to 2kg also decreased, but by a smaller amount ([X]% for both).¹⁰⁶
- 5.22 The qualitative research also echoed these findings. There was general agreement among participants that their use of letters has declined in recent years, mainly driven by the use of alternatives such as email, messenger services and video calling, which are faster, more reliable and cheaper. The Covid-19 pandemic was generally considered to have accelerated this trend.¹⁰⁷
- 5.23 However, while people consistently report sending fewer items in the post than they did previously, our quantitative research shows that most people have used the post to send an item in the past month. Around four in five people (79%) report doing so, with more people reporting having sent a letter than a parcel (66% vs 48%).¹⁰⁸ The average number of postal items people report sending in the past month is just over 6,¹⁰⁹ while the reported average number of letters sent in the past month is just under 4.¹¹⁰
- 5.24 Compared to 2017, more consumers say they have not sent any post in the past month (21% in 2022 vs 14% in 2017),¹¹¹ although the average number of items consumers report having sent in the past month is similar to 2017 (around 6 in both time periods).
- 5.25 Consumers most frequently send items that are social in nature, such as invitations, greetings cards and postcards; 49% of people report sending at least one of these in the past month.¹¹² More than two in five consumers agree that they *only* use the post to send greetings cards (42%).¹¹³ A significantly smaller proportion of consumers send items in the post for more formal purposes; 26% report sending a formal letter in the past month and 19% a bill payment or invoice.¹¹⁴

¹⁰⁵ Residential Postal Tracker 2022, QE2.

¹⁰⁶ Royal Mail Regulatory Financial Reporting Information. Figures relate to stamped volumes for both First and Second Class.

¹⁰⁷ Jigsaw, 2023. Residential Postal Affordability Research, section 3.1

¹⁰⁸ Residential Postal Tracker 2022, QG1. In the Residential Postal Tracker, 'Letters' includes invitations/greetings cards/postcards, personal letters, formal letters to organisations or individuals, and payments for bills/invoices/statements.

¹⁰⁹ Average number of parcels and letters sent, including those who say they have not sent any.

¹¹⁰ Residential Postal Tracker 2022, QG1. We note that people find it difficult to accurately estimate their usage of a service, therefore these findings should be interpreted with caution.

¹¹¹ Residential Postal Tracker 2022, QG1. We reported in the 2018 safeguard caps consultation that 28% of respondents reported sending no items of post in the past month in 2017. This was an error, and the correct figure for 2017 is 14%.

¹¹² Residential Postal Tracker 2022, QG1_1.

¹¹³ Residential Postal Tracker 2022, QC3_6.

¹¹⁴ Residential Postal Tracker 2022, QG1_3 and QG1_4.

- 5.26 A considerable proportion of consumers appear to send items in the post only out of necessity. Just under half (45%) agree that they only use post if there is no alternative, while around seven in ten (68%) agree that they prefer to send emails rather than letters whenever possible.¹¹⁵
- 5.27 Our qualitative research found that post remains important to people and is highly valued in some circumstances. For example, participants cited the important role of sending and receiving physical cards for birthdays and other occasions, such as Christmas and Easter. It was also noted that it is a tangible way of keeping in touch with family and friends, particularly those who are less able to use, or feel less confident using, digital alternatives. For a minority of participants, sending cards was considered essential for emotional reasons.¹¹⁶
- 5.28 There was also an acknowledgment in our research that, while use of post for non-leisure purposes is declining, it is still sometimes necessary. Examples cited included needing to send supporting information or forms to an official body or provider, for example, about benefits. Use of the post for these reasons was mentioned in particular by those with lower digital literacy or low trust in digital services. Some participants also noted the ‘reassurance’ that sending physical letters in the post for official purposes can provide.¹¹⁷
- 5.29 Taken together, these findings suggest that many people do not have a frequent *need* to send letters in the post, as most banking, bill-paying and communicating with organisations can be done via other methods (e.g. online, by email, or by phone). However, there continue to be occasions on which people do need to use it for non-leisure or essential purposes. Sending and receiving post for personal or leisure reasons is also widely valued.
- 5.30 We consider that the following demographic groups were more likely to be vulnerable in relation to the cost of post:
- a) Older people, as they tend to use post more than average;
 - b) People on low incomes, as they could be more negatively affected by price increases than average;
 - c) People in rural areas, as they may have a higher reliance on post; and
 - d) People without internet access, as again they may have a higher reliance on post.
- 5.31 We observe some differences in use of postal services by consumer group:¹¹⁸
- a) While overall there are not significant differences by age group in terms of whether or not they have sent any items in the past month, older people aged 55+ are more likely to have sent a letter (71% vs 63%), and less likely to have sent any parcels (40% vs 55%)

¹¹⁵ Residential Postal Tracker 2022, QC3_4 and QC3_2.

¹¹⁶ Jigsaw, 2023. Residential Postal Affordability Research, section 3.1

¹¹⁷ Jigsaw, 2023. Residential Postal Affordability Research, section 3.2

¹¹⁸ All figures cited in this paragraph are from Residential Postal Tracker 2022, QG1.

than younger people aged 16-34.¹¹⁹ The higher proportion of younger people sending parcels appears to be driven, at least in part, by marketplace sellers, who are younger than average.¹²⁰ There are not significant differences by age group in terms of the average number of items reported to have been sent in the past month.

- b) People on the lowest incomes (less than £11,500 per year) are more likely than average to have sent no items in the past month (27% vs 21%), although there are no significant differences across other income groups. Those in the social grade DE are also more likely than average to have sent no items in the past month (27% vs 21%), and to have sent fewer items overall (just under 5 compared to just over 6).
- c) Those in the most rural areas are less likely than average to have sent no items in the post in the past month (11% vs 21%) and report having sent more items than average (around 9 vs just over 6).

5.32 The finding that people on lower incomes tend to send fewer items than average in the post, and that people living in rural areas send more, is in line with our findings in our 2018-19 safeguard caps review.¹²¹ However, unlike the finding we set out in our 2018-19 review, younger people are now as likely as older people to have sent at least one item in the post in the past month.

Expenditure on post has increased as a proportion of total expenditure, although it remains very low in absolute terms

5.33 In both absolute terms and as a proportion of total household expenditure, expenditure on postal services remains low. According to the ONS, in 2020-21 the average household spent £0.90 per week on postal services, representing 0.19% of total weekly expenditure, which is equivalent to around £3.90 per month (see Figures 8 and 9 below).¹²² Weekly expenditure on postal services, as a proportion of total weekly expenditure, has increased from 0.10% in 2018-19.

5.34 It is important to note that the ONS figure includes spend on all postal services, i.e. Royal Mail USO services (e.g. First and Second Class letters and parcels, Special Delivery), Royal Mail non-USO services (e.g. 'Tracked 24' and 'Tracked 48' parcels), and non-Royal Mail services (e.g. delivery charges for items purchased online, or single piece parcels using postage purchased from a parcel operator such as Evri or DPD). Average weekly spend on the capped services will therefore be less than £0.90.

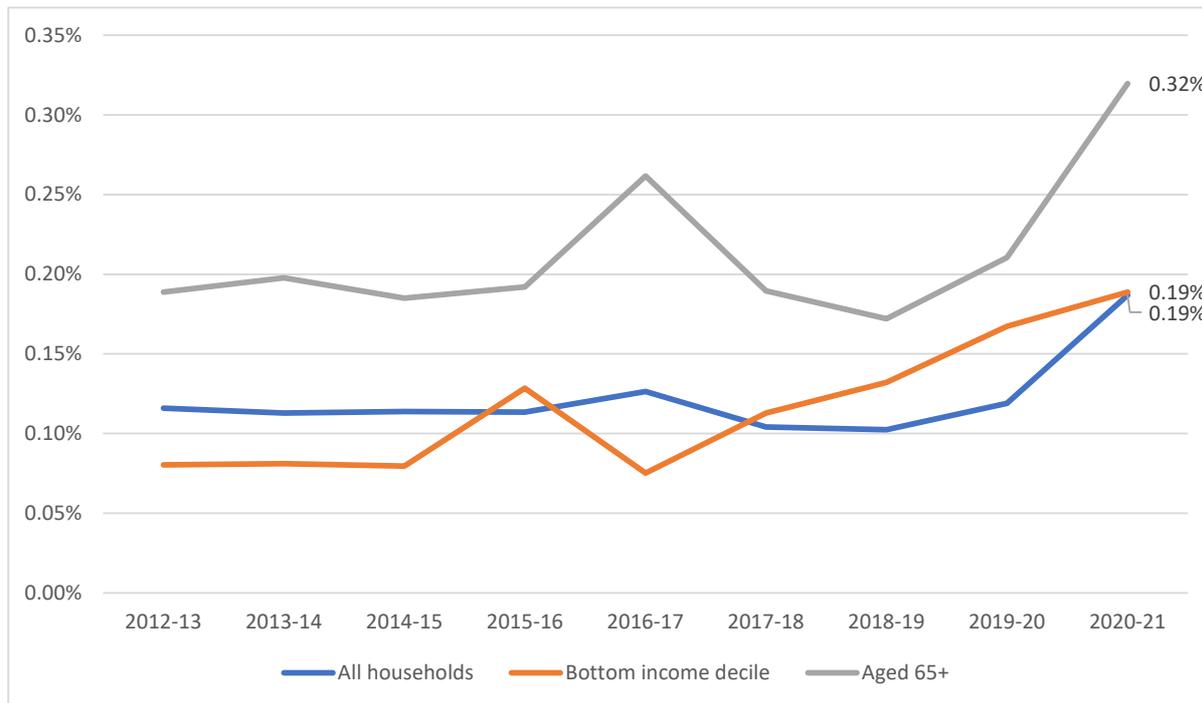
¹¹⁹ As well as being more likely to have sent at least one letter in the past month, consumers aged 55+ report sending on average more letters than younger consumers (4.84 vs 3.45). Similarly, younger people (aged 16-34) report sending on average more parcels in the past month than older consumers (1.15 vs 2.01).

¹²⁰ Residential Postal Tracker 2022, Q22. Just 5% of those aged 55+ say that they run an online business selling services, compared to 24% of those aged 16-34.

¹²¹ Ofcom, 2019. Statement: [Review of the Second Class Safeguard Caps 2019](#), paragraph 4.37.

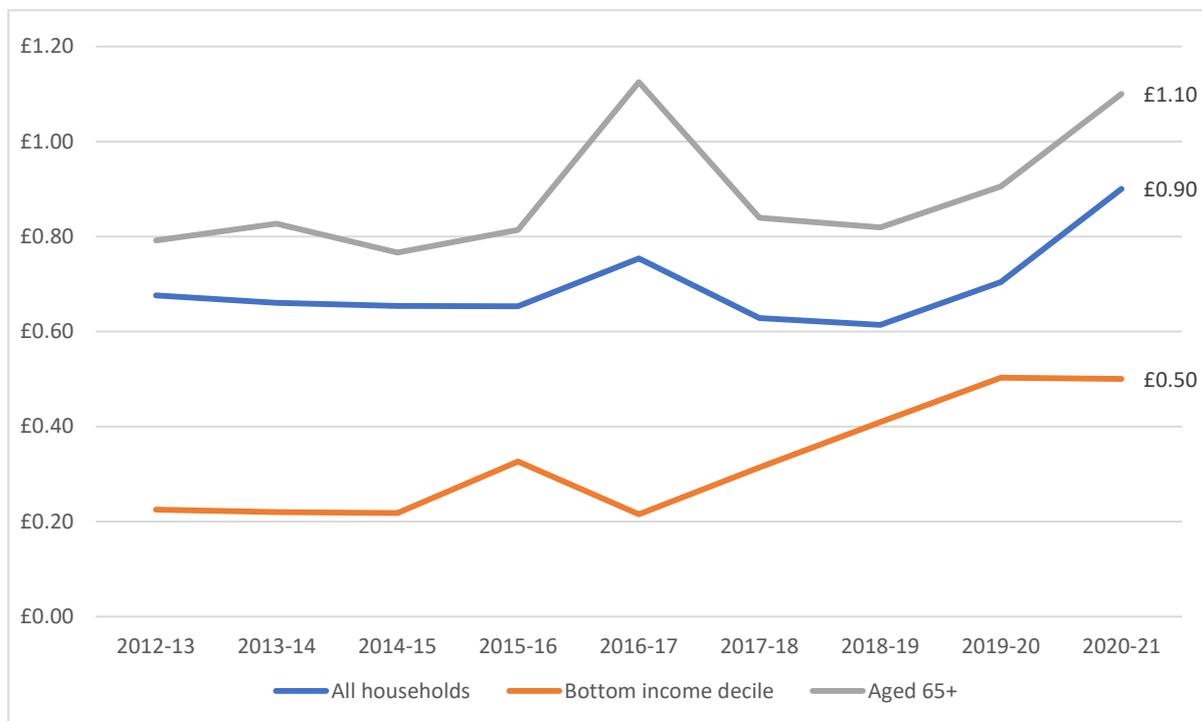
¹²² The ONS published expenditure data relating to 2021-22 before the publication of this consultation, but we have not been able to fully incorporate it into our analysis. We do however note that average weekly household expenditure on post in 2021-22, as a proportion of total weekly household expenditure, was 0.13% (lower than in 2020-21 and slightly above 2018-19). We intend to fully incorporate the 2021-22 data in our final statement on our decision.

Figure 8: Weekly household expenditure on post as a share of total weekly household expenditure, by consumer group, 2012-13 to 2020-21



Source: Ofcom analysis of ONS data (ONS: Family spending in the UK)

Figure 9: Weekly household expenditure on post by consumer group, 2012-13 to 2020-21



Source: Ofcom analysis of ONS data (ONS: Family spending in the UK), 2020-21 prices, adjusted using CPI

- 5.35 We also note that the 2020-21 expenditure data was affected by the Covid-19 pandemic and should therefore be interpreted with caution. After being relatively steady in real terms since 2012-13, total weekly expenditure on all items fell by 19% (£106.40) between 2019-20 and 2020-21. As noted by the ONS, this fall coincided with the Covid-19-related restrictions on social contact and economic activities.¹²³ The increase in spend on postal services is therefore likely to be driven by increased spend on parcel postage in particular, because there was a significant increase in the proportion of goods bought online due to the closure of many physical shops.¹²⁴
- 5.36 As noted in the 2021-22 AMU, ONS data shows that the proportion of retail sales made online has reduced since the large spike in 2020,¹²⁵ but is now increasing steadily in line with the pre-Covid-19 trend.¹²⁶
- 5.37 As in 2018-19, spend on post as a proportion of total spend by people aged 65+ is higher than average, although it is still low (0.32% of total weekly household expenditure). Households in the bottom income decile spend the same proportion of their expenditure on postal services as the average (0.19% of total weekly household expenditure).
- 5.38 We also consider (in Table 5 below) the proportion of households' income spent on postal services after essential items such as housing, energy, water and food. This provides a clearer picture of spend on post by those on lower incomes because people in lower income deciles spend a significantly higher proportion of their income than average on essential services such as housing and energy.

¹²³ ONS, 2022. [Family spending in the UK: April 2020 to March 2021](#) [accessed 15/06/2023]

¹²⁴ We note that it is likely that spend on B2C services was likely to have been more affected than spend on C2X services by the increase in the proportion of goods bought online.

¹²⁵ Ofcom, 2022. [Annual Monitoring Update for Postal Services](#), Figure 3.3.

¹²⁶ ONS, [Internet sales as a percentage of total retail sales](#) [accessed 13/06/2023].

Table 5: Spend on postal services as a proportion of monthly disposable income by each decile of income distribution, net of essential spending, 2020-21

	Lowest	Second	Third	Fourth	Fifth	Sixth	Seventh	Eighth	Ninth	Highest
Disposable income ¹²⁷	£764	£1,436	£1,784	£2,113	£2,451	£2,800	£3,224	£3,759	£4,581	£8,441
Housing ¹²⁸	-£288	-£412	-£420	-£427	-£464	-£503	-£541	-£612	-£968	-£1340
Energy ¹²⁹	-£91	-£91	-£94	-£93	-£104	-£103	-£100	-£105	-£106	-£119
Water ¹³⁰	-£35	-£38	-£36	-£40	-£38	-£49	-£46	-£45	-£49	-£55
Food and drink ¹³¹	-£212	-£256	-£262	-£275	-£286	-£309	-£306	-£342	-£351	-£400
Total remaining income	£138	£639	£971	£1,277	£1,559	£1,837	£2,232	£2,655	£3,107	£6,527
Postal services	-£2.17	-£2.60	-£2.60	-£3.90	-£4.33	-£3.90	-£4.33	-£5.20	-£4.77	-£5.63
Spend on post as a % of remaining income	1.57%	0.41%	0.27%	0.31%	0.28%	0.21%	0.19%	0.20%	0.15%	0.09%

Source: Ofcom analysis of ONS data (ONS, 2022: Family spending in the UK and ONS, 2022: The effects of taxes and benefits on household income, disposable income estimate).

5.39 This analysis shows that households in all income deciles, except the bottom decile, spend 0.41% or less of their disposable income net of essentials on postal services. However, while still low in absolute terms, households in the bottom income decile spend considerably more of their remaining income (1.57%) than all other deciles on postal services, nearly three times as much as the second income decile.¹³²

Household income

5.40 Household incomes increased by 2.8% in real terms between 2018-19 and 2021-22. However, changes in real incomes varied considerably between different consumer groups,

¹²⁷ This consists of all income, plus direct benefits, minus direct taxation. We have used equivalised income, therefore income adjusted for household composition.

¹²⁸ We have accounted for rent and mortgage payments, and spend associated with the purchase, maintenance, and repair of dwellings. We have excluded housing benefit and council tax, as they are accounted for already as a deduction from income to generate disposable income figures.

¹²⁹ Inclusive of spend on gas, electricity and other fuels.

¹³⁰ Inclusive of spend on water services to the premise and miscellaneous services relating to the dwelling.

¹³¹ Inclusive of spend on food and drink, except for spend on alcoholic drinks.

¹³² Our analysis is based on average incomes and expenditure on postal services within each decile. We therefore note that postal services could account for a higher proportion of income for some within the lowest decile.

and more financially vulnerable households (those in the lowest income decile and income quartile) have seen a decrease in real incomes (-12% and -5% respectively).

- 5.41 Retired households have also seen their incomes reduced by 5% in real terms. Retired households in the lowest income decile have seen a particularly large drop in their income (-18%). As noted above, both older consumers and those on low incomes are more likely to be vulnerable in relation to the cost of post.
- 5.42 This data covers the time period up to March 2022. CPI inflation has increased rapidly since then, leading to a significant increase in the cost of living. As noted above, more recent data shows that, average total pay has not kept pace with inflation - total pay fell in real terms by 2% on the year in February to April 2023.¹³³ At the time of our previous review of safeguard caps, we found that real incomes had increased in the period since we had previously set the caps, including for those in the lowest income decile.
- 5.43 It is also worth noting that, most benefits typically rise with inflation annually, while the State Pension typically rises by CPI, average earnings, or 2.5% (whichever is higher). Most recently, most benefits and the State Pension were increased by CPI (10.1%) in April 2023.¹³⁴ This affects two potentially vulnerable groups in particular – people on low incomes, and people aged 65+. There has also been additional targeted support with the cost of living from the Government for people who are eligible for certain benefits or who receive a pension.¹³⁵

Table 6: Cumulative growth in real disposable incomes by group, 2018-19 to 2021-22

	Bottom decile	Bottom quintile	All incomes
All households	-12.3%	-5.3%	2.8%
Non-retired households	-10.8%	-2.6%	4.2%
Retired households	-18.1%	-12.5%	-4.7%

Source: Ofcom analysis of ONS data (ONS, 2023: *The effects of taxes and benefits on household income, disposable income estimate*). We use equivalized household incomes to control for the effect of changes in household size. 2021-22 prices, adjusted using CPI.

Market research on affordability

The proportion of consumers reporting post affordability issues on our Residential Postal Tracker has increased since our last review

- 5.44 While noting the drawbacks of our test of affordability discussed above, we set out first the findings from our Residential Postal Tracker in relation to postal affordability. We also set

¹³³ ONS, 13 June 2023. [Average weekly earnings in Great Britain: June 2023](#) [accessed 13/06/2023].

¹³⁴ HM Treasury, November 2022. [Cost of living support Factsheet](#).

¹³⁵ HM Treasury, November 2022. [Cost of living support Factsheet](#).

out the relevant findings of our qualitative research, which provides useful context to the Residential Postal Tracker results.

- 5.45 We made some changes to the affordability questions asked in the Residential Postal Tracker in 2022 to better understand the potential source of postal affordability issues. Instead of asking about only stamps, we asked about three categories: letters and cards, parcels, and letters and cards by First Class post. Participants were asked whether, in the last three months, they had reduced their spend on these to afford essentials, or if they had cut back on their essentials to afford to send the same number of these items.¹³⁶
- 5.46 While the changes to the questions mean that the findings are not directly comparable with those reported in our previous review of safeguard caps, there has been an increase in people reporting potential affordability issues since our last review. In 2017, 10% of users reported experiencing any post affordability issues. In 2022, 32% reported experiencing any affordability issues with any of the three categories of post (letters and cards, parcels and First Class items).
- 5.47 More specifically, in 2022, just under a quarter said that they have had to reduce the number of letters and cards they send so that they can afford essentials (23%). For parcels, this figure was the same (23%), and for First Class post it was just over a quarter (27%).¹³⁷
- 5.48 In 2022, the proportion of postal users who reported cutting back on post to afford essentials is higher than the proportion who report cutting back on essentials to afford post (29% vs 22%).¹³⁸
- 5.49 Overall, the picture is mixed when looking at whether potentially vulnerable groups are more likely to report an affordability issue with post. In 2022, older people (aged 55+) are significantly less likely than average to report any post affordability issues (22% vs 32%), and this is even lower among those aged 65+ and 75+ (both 20%). Those in rural areas are no more likely than average to report affordability issues.¹³⁹ The groups most likely to report affordability issues are marketplace sellers (52%), younger people aged 16-34 (47%), and those in the AB social grades (39%).
- 5.50 However, those on the lowest incomes (the lowest two categories, with income under £11,500 per year and £11,500 - £17,499 per year) are more likely than average to report affordability issues (38% and 41% respectively), as are those who receive benefits (43%).¹⁴⁰
- 5.51 We recognise that these figures suggest that a considerable, and increasing, minority of consumers are experiencing affordability issues in relation to post. However, our qualitative research, the results of which are set out below, suggests that the increase is

¹³⁶ We also made two other changes to the questions. In 2022, participants are no longer prompted with 'food or heating' as examples of 'essentials', and, for the second question, are now asked whether they have cut back on essentials so that they can afford to send the *same number of* letters and cards, letters and cards by First Class post, and parcels.

¹³⁷ Residential Postal Tracker 2022, QG2.

¹³⁸ Residential Postal Tracker 2022, QG2.

¹³⁹ Residential Postal Tracker 2022, QG2.

¹⁴⁰ Residential Postal Tracker 2022, QG2.

likely due to the wider increase in the cost of living rather than postal prices alone.¹⁴¹ We also note that some vulnerable groups (in particular, those aged 65+) are less likely than average to report affordability issues.

Our qualitative research suggests that the increases in reported affordability issues are likely to be driven by wider cost of living pressures rather than postal prices

- 5.52 Our qualitative research provides additional insights into the increase in postal users reporting affordability issues observed in the Residential Postal Tracker.
- 5.53 This found that the increased cost of living was causing participants to take a wide range of actions to reduce their spending across the board (both essential and non-essential spending). Many participants were cutting back on their spend on postal services as part of spending reductions across all or most household spend categories, because other costs had increased. Post was considered just another area with potential for spend to be reduced.¹⁴²
- 5.54 There was little evidence from the qualitative research to suggest that, where participants were cutting back on postal services, they frequently experienced significant detriment as a result. This was because most participants in the qualitative research did not see postal services as essential to their day-to-day communication, which meant that they found it easier to cut back on postal services than other things.¹⁴³ However, as noted above, a small number of participants did consider at least occasional use of post essential to them, because sending cards and letters was an important aspect of their social life.
- 5.55 Participants had different views on what affordability of postal services meant to them, which depended on their personal circumstances. The extent to which a participant might consider post not to be affordable depended on a combination of three factors – their own financial situation, their reliance on post in a given period, and (for a minority) an emotional connection with sending cards and letters.¹⁴⁴
- 5.56 With this in mind, when asked whether they considered post (and stamps in particular) affordable, few participants felt that sending the occasional letter or card was unaffordable to the extent that they could not send them. Further, participants generally did not feel that cutting back on postal services would affect their overall ability to afford essentials and did not make a clear connection between cutting back on postal services and being better able to afford a specific essential item or bill. This is likely because average spend on

¹⁴¹ We also need to take into account changes in both methodology and question wording since our previous review. In 2020, we moved to 100% online self-completion surveys (from a combination of online and face-to-face interviews) because of Covid-19 restrictions (although from 2023 onwards we are re-introducing face-to-face interviewing as part of the research methodology for the Residential Postal Tracker). Online respondents who complete the survey without an interviewer being present are historically more likely to agree with these question statements. The change in wording may have also had an effect on responses, including the fact that from 2022, participants were not given examples of ‘essentials’. We know from the qualitative research that definitions of ‘essential’ vary significantly, potentially affecting the responses to this question. However, we also note that the increase in the proportion of participants reporting affordability issues appears to have begun in Q4 2021, before these changes were made.

¹⁴² Jigsaw, 2023. Residential Postal Affordability Research, sections 3.5 and 4.1

¹⁴³ Jigsaw, 2023. Residential Postal Affordability Research, section 4.3

¹⁴⁴ Jigsaw, 2023. Residential Postal Affordability Research, section 4.1

post is very low and represents only a very small proportion of total household spending commitments.¹⁴⁵

- 5.57 Nevertheless, and in line with other areas of spending, the research showed that participants were very conscious of their spending and were taking a range of actions to reduce their spend on postal services in order to save money or to be better able to afford essentials. The most common action taken within our sample was switching from First Class to Second Class. This was generally felt to have little or no impact on them in terms of meeting their needs, and generally amounted to inconvenience rather than detriment (for example, switching from First to Second Class and as a result needing to plan further ahead to ensure items arrived on time).
- 5.58 Some people were reducing the number of cards, letters and parcels they sent, which, particularly for those for whom sending post is an important part of their social lives, could result in a sense of loss or sadness.¹⁴⁶
- 5.59 While the research found that spending on postal services did not generally require sacrifices to be made, it identified that this may not be the case in two situations – if a consumer had cashflow pressures, and/or if they had an increased demand for postal services in a given period. With respect to cashflow pressures, some participants on a very low income reported needing to be very conscious of their spending at certain times of the month (for example, when bills were collected from their bank account, or at the end of the month just before being paid). This could mean that if they needed to send an item in the post during such a period, it could cause stress or lead the consumer to find an alternative way to send it (for example, borrowing money from friends or family), or delaying sending the item.
- 5.60 The Christmas period (a time when consumers typically spend more on postal services compared to the rest of the year) was also identified as a time when post could become unaffordable for some. Several participants said they had cut back on the number of Christmas cards they were sending, and most stated that those being sent were done so by Second Class rather than First Class post. Unlike other periods, participants did not feel they had a choice about the timing of sending Christmas cards and this could cause some detriment.¹⁴⁷
- 5.61 However, at the most severe end, a very small number of participants recalled having had to make a trade-off between sending an important letter or card and purchasing essential food items or heating. The research also identified that some participants had needed to ask friends or family for money when sending certain items of post (this seemed to be more common in relation to ‘Signed For’ post).

¹⁴⁵ Jigsaw, 2023. Residential Postal Affordability Research, section 4.1

¹⁴⁶ Jigsaw, 2023. Residential Postal Affordability Research, section 3.1

¹⁴⁷ Jigsaw, 2023. Residential Postal Affordability Research, section 4.2

- 5.62 With regard to parcels, our quantitative research suggested that postal users do not find parcels any less affordable than letters.¹⁴⁸ While our qualitative research was more focused on letters than parcels, we found that parcel costs were more ‘front of mind’ for participants than letter costs, likely reflecting the fact that parcels are more expensive to send than letters.¹⁴⁹ There was also a perception that sending parcels is a more frequent activity than sending letters. People considered that sending gifts to relatives or friends was important to them and more emotionally rewarding than (for example) giving money via a bank transfer.¹⁵⁰
- 5.63 It is relevant to our assessment of the affordability of parcels that, as set out in section 4, there is evidence of growing competition in the C2X parcels segment, and that (relatedly) parcels to which the safeguard caps apply have reduced in price in real terms since our previous review.
- 5.64 Overall, the qualitative research found that, generally, post affordability issues were most likely to occur for consumers with specific sets of overlapping personal circumstances, for example:
- a) Being on a low income and lacking digital skills or confidence;
 - b) Being on a low income and having an emotional attachment to sending greetings cards;
 - c) Having a condition that impacts their mobility and lacking digital skills or confidence; or
 - d) Being on a low income and relying on selling low-value items online to boost income.¹⁵¹
- 5.65 When participants in the qualitative research were asked whether they had cut back on essential items in order to afford post, some were surprised at the question as doing so had not occurred to them, and almost all said that they had not.¹⁵² Similarly, and as set out above, most participants said that they had not cut back on postal spending specifically to afford essentials, but had done so in line with other areas of spending in response to the increased cost of living.
- 5.66 Participants were asked why they might answer yes to the affordability questions asked in the Residential Postal Tracker. There was a range of answers provided by participants, which included: people being frustrated at current price increases everywhere and using questions in this survey to express their frustration; generally agreeing with the sentiment of the question; not reading the question properly; how they were feeling on the day (for example, if they had had a recent large expense); seasonal timing; and the respondent’s definition of ‘essentials’.

¹⁴⁸ As noted in paragraph 5.47, just under a quarter of postal users said that they have had to reduce the number of letters and cards they send so that they can afford essentials (23%). When asked about parcels specifically, this figure was the same (23%).

¹⁴⁹ We note that, unlike for letters, there are more options for sending parcels than just Royal Mail’s USO services, and therefore when discussing them they may not be thinking about USO parcels (or indeed parcels subject to a safeguard cap). This means that the results of our qualitative research in relation to parcels should be treated with caution.

¹⁵⁰ Jigsaw, 2023. Residential Postal Affordability Research, section 3.3

¹⁵¹ Jigsaw, 2023. Residential Postal Affordability Research, section 4.4

¹⁵² Jigsaw, 2023. Residential Postal Affordability Research, Appendix A

- 5.67 As noted above, although we are conscious of the increase in number of respondents on the Residential Postal Tracker reporting affordability issues with post, these findings suggest that the proportion of people experiencing post affordability issues is likely to be overstated (although we recognise that there are nevertheless consumers who are indeed experiencing affordability issues).
- 5.68 Overall, the qualitative research indicates that the significant increase in affordability issues observed in the Residential Postal Tracker is not driven by postal prices specifically, but by the broader financial challenges many consumers are currently experiencing. It identified that most consumers find current postal prices affordable, but that some consumers, in particular those who are vulnerable, are occasionally experiencing detriment in relation to the cost of post.

Other USO services

- 5.69 We set out below an assessment of the affordability of USO services which are not currently subject to a safeguard cap. With the exception of First Class, use of these services is not sufficiently frequent or consistent for us to be able to apply our usual test of affordability set out above. Therefore, when assessing the affordability of these services, we consider, amongst other things: frequency of use; need for the service; and the availability of competitive alternatives.
- 5.70 We can impose a safeguard cap on any universal service if we consider it appropriate to secure the provision of a service as described in the universal postal service order (including that the service be affordable).¹⁵³ However, as explained below, we consider that it is not currently necessary or appropriate to impose additional safeguard caps on any services beyond those which are already capped.

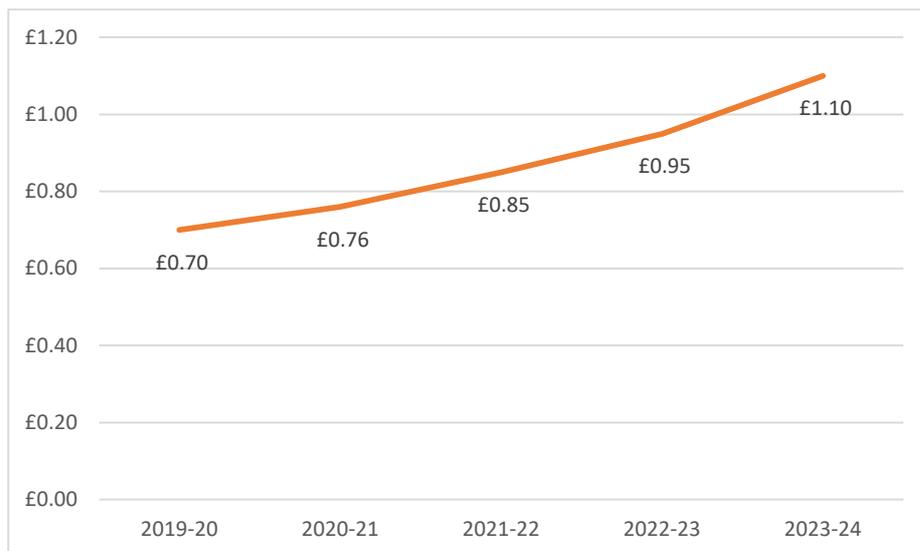
First Class services

- 5.71 Royal Mail is required to offer a *priority* letter service as part of the universal service which it does through its First Class standard letter, large letter and parcel services.¹⁵⁴ These services are offered with the same features as the *standard* letter service (Second Class) equivalents, but with a faster delivery time of within one working day of collection (known as 'D+1'), compared to within three working days of collection (known as 'D+3') for Second Class.
- 5.72 First Class standard letter prices have increased significantly since our previous review of safeguard caps (see Figure 10 below) and are now 34% higher in real terms than in 2019-20, and 57% higher in nominal terms.

¹⁵³ Section 36(3) of the PSA 2011.

¹⁵⁴ DUSP 1.6.1(a).

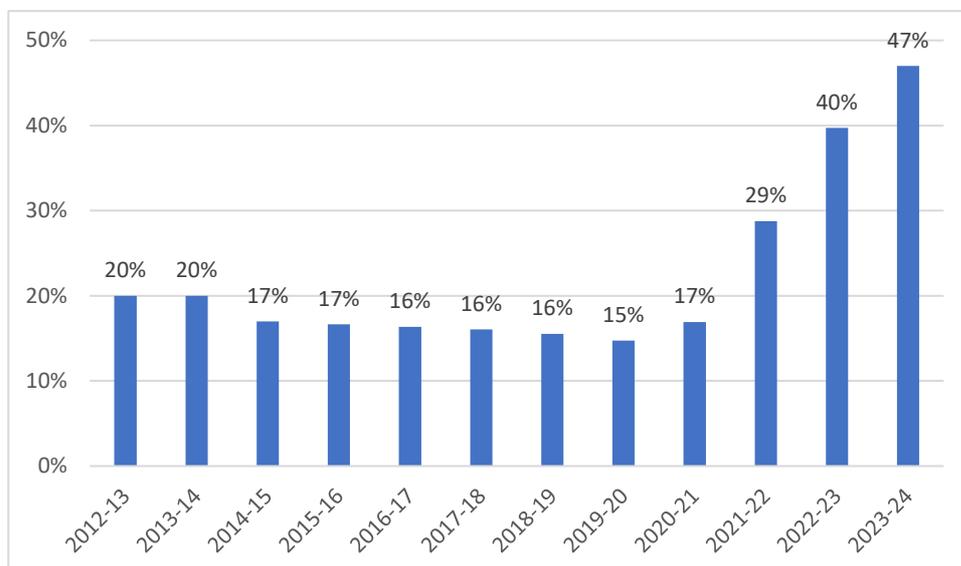
Figure 10: Nominal price of Royal Mail First Class stamped standard letters, 2019-20 – 2023-24



Source: Royal Mail Price Guides

5.73 First Class services as the priority services are naturally more expensive than Second Class. The price differential between First and Second Class standard letters was 15%-20% between 2012 and 2020, but since then has increased. In 2022, the differential was 40% while in 2023 it was 47% (see Figure 11).

Figure 11: Differential between First Class and Second Class stamped standard letter prices, 2012-13 – 2023-24



Source: Ofcom analysis of Royal Mail Price Guides

5.74 The higher price of First Class services relative to Second Class services reflects both the higher cost of providing the First Class service and the higher willingness to pay of those who choose to use First Class because of the faster speed.

- 5.75 We note that, in recognition that it is more challenging for Royal Mail to deliver items within a shorter timeframe, there are slightly lower Quality of Service targets for First Class than for Second Class. Royal Mail is required to deliver at least 93% of First Class mail within one working day of collection, and to deliver at least 98.5% of Second Class mail within three working days of collection.
- 5.76 As explained further in section 5, our test for affordability in postal services is whether current prices cause users significant detriment. This could be either because the prices cause users to cut back on essential items in order to afford post, or because they need to reduce their spend on post in order to afford essential items, and experience significant adverse consequences as a result. As noted above, in 2022 we asked specifically about First Class letters and cards in the affordability questions in our Residential Postal Tracker. We found that 27% of consumers said that they have had to reduce the number of letters and cards they send so that they can afford essentials. This is slightly higher than the proportion of those who said this about letters and cards more generally (23%). This suggests that, at face value, consumers do not find First Class standard letter prices significantly less affordable than Second Class.
- 5.77 Furthermore, it appears that, in general, First Class is infrequently needed. Our consumer research indicates that many users of First Class services do not appear to *require* the priority of faster delivery than would be achieved through the standard Second Class service. Our 2019 quantitative Postal User Needs research tested the acceptability of a single class of delivery for both letters and parcels, delivered either slightly faster than Second Class (D+2), or at the same speed (D+3).¹⁵⁵ This research found that the vast majority (96%) of residential users would consider their needs met by a single D+2 service, while a slightly smaller proportion (but still the vast majority at 94%) would consider their needs met by a single D+3 service.¹⁵⁶
- 5.78 Further, our 2019 qualitative consumer research found a ‘strong acknowledgment’ that most letters are not urgent and, as such, speed of delivery was rarely critical. There were a small number of exceptions to this (for example, needing to send documentation for a house purchase or to renew a passport), but participants noted that First Class could not necessarily be relied on in such circumstances.¹⁵⁷
- 5.79 We note that the most common reason cited by postal users who use First Class all or most of the time in our 2022 Residential Postal Tracker is the speed of delivery (59%). They also cite a perception that the item is less likely to be lost or that it will be treated better (18%), security (16%), and ‘image’ related reasons (7% say they do not want people to think that they don’t use First Class).¹⁵⁸

¹⁵⁵ Ofcom, 2020. [Review of Postal User Needs](#), figure 30. The research presented scenarios where the same speed and reliability of service applied to both letters and parcels, and so results presented here are on this basis.

¹⁵⁶ These figures were slightly lower for SMEs, at 92% and 87% respectively.

¹⁵⁷ Jigsaw, 2020. [UK Postal User Needs: Qualitative Research Report](#), section 4.3.1. The research was conducted in 2019 and published in 2020.

¹⁵⁸ Residential Postal Tracker 2022, QH8.

- 5.80 The evidence from our 2019 qualitative research suggests that use of First Class is likely to be out of habit or preference for the speed, rather than need. The main reasons cited in that qualitative research as to why participants used First Class over Second Class services were the fact that the price differential between the two was small (particularly for letters),¹⁵⁹ certainty of service and perceived service quality, and that First Class can act as a signifier of the importance of the recipient.¹⁶⁰
- 5.81 Our 2023 qualitative research found that, in general, participants who used First Class stamps were switching to Second Class.¹⁶¹ This was in line with our finding that participants were cutting back on spending where possible across the board, because of the increase in the cost of living. The switch from First to Second Class did not seem to cause participants detriment beyond some additional forward planning to account for slower delivery times. Most participants were aware that the price had recently increased to over £1 and some considered this to be ‘too much’. However, this appeared to cause annoyance or inconvenience to participants (for example, needing to plan further ahead to take into account the longer delivery time for Second Class), rather than affordability issues.¹⁶²
- 5.82 Based on our research, we consider that, for a consumer in any given year, there would be very few occasions on which the priority First Class service would be essential or particularly important, and for whom the First Class price would be unaffordable. The standard Second Class services, which are significantly lower in price and (for letters) constrained by a safeguard cap, also act as a ‘backstop’. They ensure that consumers will continue to have access to a lower cost alternative that should, in most cases, meet their needs. In summary, the combination of the low price in absolute terms, the fact that First Class appears to be essential or important only infrequently and that Second Class therefore meets consumers’ needs in the majority of cases, suggest that First Class is affordable for most consumers.
- 5.83 We do however acknowledge that there will always be some cases when the First Class delivery time is needed and that this, combined with the First Class premium, may cause affordability issues for a consumer. However, as we have acknowledged in the past, it is likely that such a consumer would be experiencing a limited set of circumstances where they suffer both significant financial difficulty or have a very low income, and have a frequent need to send post items they consider to be essential and which need to arrive the next day. We recognise that the increased First Class prices could have negative impacts on these consumers, though unfortunately postal services may be unaffordable for some even if their prices were reduced significantly.

¹⁵⁹ We note that our more recent qualitative research (albeit with consumers with affordability issues) indicates that the recent First Class price rise has affected consumers’ perceptions of the relative value of First to Second Class. At the time this research was conducted (2019), the differential between First Class and Second Class was considerably lower than it is now.

¹⁶⁰ Jigsaw, 2020. [UK Postal User Needs: Qualitative Research Report](#), section 5.1.

¹⁶¹ We note that the qualitative research began several weeks after the announcement of Royal Mail’s 2023 price increases (see International Distributions Services plc, 3 March 2023, [press release](#)) and associated media coverage, thereby potentially increasing awareness amongst participants of current stamp prices.

¹⁶² Jigsaw, 2023. Residential Postal Affordability Research, sections 3.4 and 4.3

5.84 For the vast majority of consumers, the evidence suggests that the *need* for First Class is infrequent. Therefore, our view is that the budget impact of the First Class premium (above Second Class prices) is likely to be very small and that, as such, First Class services are likely to be affordable for most consumers.¹⁶³

Special Delivery

5.85 Royal Mail is required to offer a registered and insured next-day delivery service with a target delivery time of 1pm.¹⁶⁴ It meets this obligation with its ‘Special Delivery Guaranteed by 1pm’ service (referred to as ‘Special Delivery’ below).¹⁶⁵ Royal Mail offers this service at a number of weight steps (between up to 100g and up to 20kg) and compensation amounts (up to £750, £1,000 and £2,500). It can be purchased online or offline at a Post Office, with offline prices around 6% higher than online prices.

5.86 Prices are significantly higher than standard and Signed For services, reflecting the additional features provided by Special Delivery, namely guaranteed delivery time, ability to track the item, and the amount of compensation that can be claimed in the event of loss or damage.

5.87 Special Delivery is used infrequently compared to letters and parcels. Our 2022 Residential Postal Tracker found that 13% of postal users report having sent a Special Delivery parcel in the past month, and 6% report having sent a Special Delivery Guaranteed by 1pm parcel.¹⁶⁶ By contrast, and as set out above, 66% of postal users report having sent a letter in the past month. While the price of Special Delivery is significantly higher than other USO services, the fact that it is only infrequently used suggests that it is likely to be affordable for most consumers.

5.88 Between 2019-20 and 2023-24, offline and online Special Delivery prices have on average remained steady (i.e. increased by 0% in nominal terms). In real terms, prices have decreased. For example, for items weighing up to and including 100g and with up to £750 of compensation, the offline price has decreased by 11%, while the online price has decreased by even more (18%).¹⁶⁷ The average real-terms price decrease for the services in Figure 12 below was 15%.

¹⁶³ While we recognise that there are occasions on which people need to send items quickly, we also note that First Class may not always be the most appropriate service for doing this. This is because people sending time-critical items such as legal documents, identity documents or grant applications, are likely to also want additional assurance about the delivery. While most First Class items are delivered within one day, this is not guaranteed (given the QoS target is 93%), and First Class does not include other ‘peace of mind’ features such as tracking and a signature on delivery.

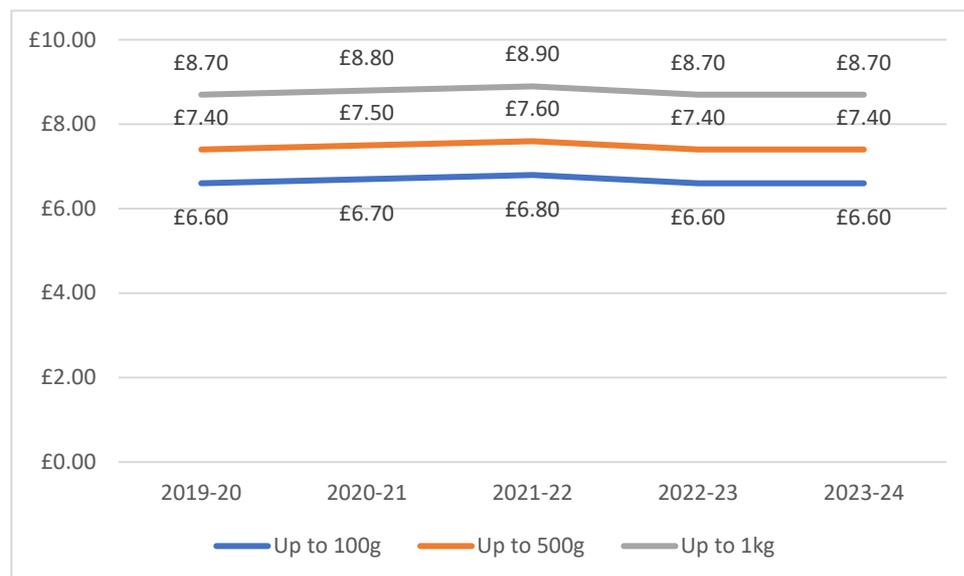
¹⁶⁴ DUSP 1.6.1(d). The target time is 1pm unless this is not reasonably possible (DUSP 1.6.1(d)(b)).

¹⁶⁵ Royal Mail also offers a ‘Special Delivery Guaranteed by 9am’ service on a commercial basis.

¹⁶⁶ Residential Postal Tracker 2022, Q14.

¹⁶⁷ At the same time, Royal Mail has increased the minimum level of compensation offered from £500 to £750.

Figure 12: Special Delivery nominal prices for services weighing up to 100g, up to 500g and up to 1kg, 2019-20 – 2023-24



Source: Ofcom analysis of Royal Mail Price Guides. Royal Mail increased the minimum compensation amount for Special Delivery services in 2023 from £500 to £750. Therefore, 2023-24 prices are for services with £750 compensation, prices before that date are for services with £500 compensation. All prices shown are an average across online and offline.

5.89 We note that a number of other parcel operators offer a next-day delivery service with tracking. While these services do not generally offer all of the features of Special Delivery (for example, the compensation element), consumers have access to a range of similar services from a number of different operators.¹⁶⁸ Royal Mail’s internal documents indicate that it monitors its competitors’ offerings and how Special Delivery compares to those. [3<].¹⁶⁹

5.90 The infrequency of use of Special Delivery, and the existence of competition and the corresponding constraints on Royal Mail’s pricing, means that we do not consider that a safeguard cap on Special Delivery would be appropriate to ensure affordability. With that in mind, we note our objective to provide protection to consumers where such protection is unlikely to be provided by competitive markets. We consider that competition is providing protection in respect of Special Delivery, alongside the fact that it is an infrequently used service.

International delivery services

5.91 Royal Mail offers a number of international letter and parcel delivery services, including tracked and signed for options as well as a cheaper and slower parcel delivery service

¹⁶⁸ For example, DPD, Evri and DHL offer a next-day delivery service with tracking. For a 1kg parcel, the price ranges from £4.72 (Evri, with delivery to an Evri pick-up point) to £9.35 (DPD Local). All operators enable the customer to add compensation cover to the price if desired (for a fee), and Evri’s service includes a signature on delivery.

¹⁶⁹ Royal Mail response dated 23 January 2023 to s.55 Notice, [3<]

known as 'International Economy'. International services are more expensive than their domestic equivalents, reflecting the longer distances involved.¹⁷⁰

- 5.92 Our Residential Postal Tracker does not include questions about use of international delivery services. However, volume data from Royal Mail shows that international letter volumes are significantly lower than domestic letter volumes (international letter volumes represented [X] % of total letter volumes in 2022-23).¹⁷¹ This suggests that international letter services are used less frequently than domestic letter services, and therefore, as for Special Delivery, that they are likely to be affordable for most consumers.
- 5.93 We recognise that certain groups of consumers are likely to use international mail services more than others – for example, recent immigrants to the UK. However, we also note that there are free or low-cost alternatives for communication with people in other countries, for example, messenger services such as WhatsApp and video calling services such as FaceTime. Further, where alternatives to postal services are less able to be used (i.e., for parcels), competition is likely to help to constrain those prices (see paragraph 5.95 below).
- 5.94 The higher price for international mail reflects the fact that, when mail is sent from one country to another, the universal service provider in the sending country must pay a fee to the universal postal service provider in the destination country to compensate them for the costs associated with the handling, transporting and delivering of the item. These fees (known as 'terminal dues') are set by international agreements, overseen by the Universal Postal Union (UPU). Royal Mail is therefore not responsible for all of the costs it incurs to handle and send international mail.
- 5.95 Royal Mail faces competition for international parcel services, although not for letter services. A number of parcel operators provide these services and offer comparable prices to Royal Mail, and some operators (e.g. FedEx, UPS and DHL) specialise in international delivery. The existence of these alternatives is likely to constrain Royal Mail's international parcel prices.
- 5.96 We consider that the infrequency of use of international delivery services means that they are likely to be affordable for most consumers. We also do not consider that it would be appropriate to impose a safeguard cap on international delivery services as Royal Mail is not able to control all of the costs it incurs to provide them. Finally, we note our objective for the safeguard caps to provide protection to consumers where such protection is unlikely to be provided by competitive markets. We consider that competition is providing sufficient protection in respect of international parcels.

Redirections

- 5.97 Redirections services enable consumers to divert their mail from one address to another address, for a specified period. Royal Mail offers the service for three time periods, three

¹⁷⁰ Royal Mail is required to provide international postal services by DUSP 1.6.1(f) to (h).

¹⁷¹ Royal Mail Regulatory Financial Reporting Information. Stamped letter volumes.

months (at a price of £36 for a single adult household), six months (£53) and twelve months (£76).^{172 173}

- 5.98 We expressed concerns in our 2021 Review of Postal Regulation consultation about the affordability of the Redirections service for financially vulnerable consumers.¹⁷⁴ Our consumer research suggested that, while the majority of postal users found Royal Mail's Redirections service to be affordable, financially vulnerable consumers had encountered significant affordability issues, notwithstanding the introduction by Royal Mail of a discounted service in 2019.
- 5.99 We had therefore intended to propose a new targeted price cap on Redirections services for financially vulnerable consumers but, following an announcement from Royal Mail that it would make several significant changes to the scope and scale of its discounted service, we decided not to. We considered that the amended discount (known as Concession Redirections) largely addressed our affordability concerns.¹⁷⁵
- 5.100 To ensure that Redirections continue to be affordable, we are monitoring prices, promotion, and uptake of the concession scheme through our monitoring programme, as well as the standard prices of the Redirections service over the coming years. We intend to report on this in future Annual Monitoring Updates.

Keepsafe

- 5.101 Royal Mail's Keepsafe service meets its obligation to provide 'retention' services.¹⁷⁶ A Keepsafe allows a customer to have their post delivered to a location other than their home address, for example when they are away from home. The price varies by length of time the customer wishes their post to be delivered to the alternative location. A residential Keepsafe service costs £18 for ten days, rising to £90 for 100 days.¹⁷⁷
- 5.102 Although we have not conducted a full assessment of the affordability of Keepsafe services, we are not aware of any affordability concerns in relation to these services. We consider that they are affordable on the basis that they are likely to be infrequently needed given the structural decline in letter volumes, and therefore the amount that consumers spend on them in any given year is low and unlikely to affect their ability to afford essential items.

Provisional conclusion on our analysis

- 5.103 As noted above, it is challenging to determine whether specific price points are affordable for consumers, and we must weigh up the available evidence in the round in order to make a judgement. In particular, we are conscious that a small proportion of consumers are

¹⁷² Royal Mail is required to provide redirection services by DUSP 1.7.1(a).

¹⁷³ Prices correct as of June 2023.

¹⁷⁴ Ofcom, 2021. [Consultation: Review of Postal Regulation](#), pp. 55-72

¹⁷⁵ Ofcom, 2022. [Statement: Review of Postal Regulation](#), p. 82.

¹⁷⁶ Royal Mail is required to provide retention services by DUSP 1.7.1(c).

¹⁷⁷ Prices correct as of June 2023.

likely to face affordability issues at current prices, and that the increased cost of living is likely to have worsened these issues.

- 5.104 An affordability assessment against the backdrop of unusually high inflation and an increase in the cost of living is clearly challenging. However, based on the evidence, our assessment is that most consumers do not experience significant detriment as a result of postal prices, and therefore that current prices are affordable for most consumers, including those who are vulnerable. As we have set out previously, we recognise that there are some consumers in particular circumstances who may face affordability issues at current prices, but that, for these consumers, even a significant reduction in postal prices may not ensure that they are affordable.
- 5.105 Further, our assessment is that real terms increases (i.e., above CPI) in the prices of the capped services are likely to lead to a larger proportion of consumers, in particular vulnerable consumers, experiencing incidences of significant detriment in relation to the cost of post more frequently.
- 5.106 We have come to this view for the following reasons:
- a) There is a general recognition that, for most consumers, post is only occasionally essential and that sending of letters in particular is declining. However, a majority of consumers report sending at least one letter in the past month and, while sending letters for social reasons is falling particularly quickly, sending letters for non-leisure purposes will continue to be necessary in some circumstances. Many people also value using the post for social and emotional reasons (for example, sending cards to friends and family).
 - b) Overall, average incomes increased slightly in real terms between 2018-19 and 2021-22, but reduced considerably for more vulnerable households, including those in the lowest income decile and those who are retired. In addition, more recent data shows that average pay has not kept up with CPI inflation and incomes are therefore likely to have declined in real terms in the last year. However, we also note that most benefits and the State Pension typically rise with inflation annually.
 - c) Average expenditure on post remains very low, but represents a considerably higher proportion of disposable income for households in the lowest income decile, once spend on essentials is taken into account. However, even for these households, average spend on post represents around 1.6% of their income after essentials.
 - d) There has been a significant increase in the proportion of consumers who say that they have cut back on post to afford essentials or who have cut back on essentials to afford post. However, our qualitative research found that the increased cost of living appears to be driving the increases we observe, rather than postal prices themselves.
 - e) There are some indications that certain vulnerable groups (consumers on low incomes and consumers who claim benefits) are more likely to experience affordability issues. Our qualitative research however suggests that these groups are mostly (although not always) able to absorb these costs without experiencing significant detriment.

5.107 Finally, we consider that other USO services remain affordable for consumers on the basis of the choices available to them and the frequency of their use, and, in some cases, the constraint on Royal Mail's pricing posed by competing operators.

Consultation question

Question 7: Do you agree with our assessment of the affordability of Second Class postal prices? Please state your reasons and provide evidence to support your view.

6. Financial sustainability

- 6.1 Our key concern with any safeguard caps is that they ensure that the services to which they apply remain affordable, in particular for vulnerable consumers. We have reflected this in two of our objectives – specifically, to ensure universal services are affordable, particularly for vulnerable consumers, and to provide protection to consumers where such protection is unlikely to be provided by competitive markets.
- 6.2 We must, when carrying out our functions in relation to post have regard to the financial sustainability of the universal service, and, when setting a safeguard cap, seek to ensure that it takes account of the costs of providing the service. These requirements are reflected in our other objectives, specifically to minimise the impact of any safeguard cap on the financial sustainability of the universal service, while retaining incentives for Royal Mail to operate efficiently, and to ensure any safeguard cap takes into account the costs of providing the capped service(s).
- 6.3 Therefore, in this section, having considered the affordability of current prices and the extent to which competition is protecting consumers, we consider the impact of any cap on the financial sustainability and efficiency of the universal service.

Financial sustainability and efficiency of the universal postal service

- 6.4 To inform our assessment of financial sustainability of the universal postal service, we consider whether the part of the UK business that delivers the universal postal service (which we call the Reported Business) can expect to earn a reasonable commercial rate of return. The Reported Business includes most of Royal Mail’s UK activities, and also delivers non-universal services such as access and bulk mail.
- 6.5 We consider that an Earnings Before Interest and Taxes (EBIT) margin of 5 to 10% is consistent with the need for the provider to make a reasonable rate of return. Margins consistently below 5% could indicate that the universal service faces sustainability issues, but 5% does not represent a “target” return.
- 6.6 We set out in our 2021-22 AMU that the Reported Business EBIT margin has for the last five years remained below the lower bound of the 5-10% range, and noted our increasing concerns about the long-term sustainability of the USO.¹⁷⁸
- 6.7 Royal Mail has since published its full year results for 2022-23, which included an adjusted operating loss for the UK business of £419m.¹⁷⁹ It explained that its deterioration in financial performance was due to a combination of: the impact of the industrial dispute; an

¹⁷⁸ Ofcom, 2022. [Annual Monitoring Update for Postal Services](#), paragraph 6.26.

¹⁷⁹ International Distributions Services plc, Unaudited Preliminary Results for the 52 week period ended 26 March 2023. See <https://www.internationaldistributionservices.com/media/12036/ids-plc-fy-2022-23-results-rns-18-5-23.pdf> [accessed 15/06/2023].

inability to deliver productivity improvements; lower Covid-19 test kit volumes; and a weaker online retail market. The Reported Business EBIT margin for 2022-23 was [X]%.¹⁸⁰

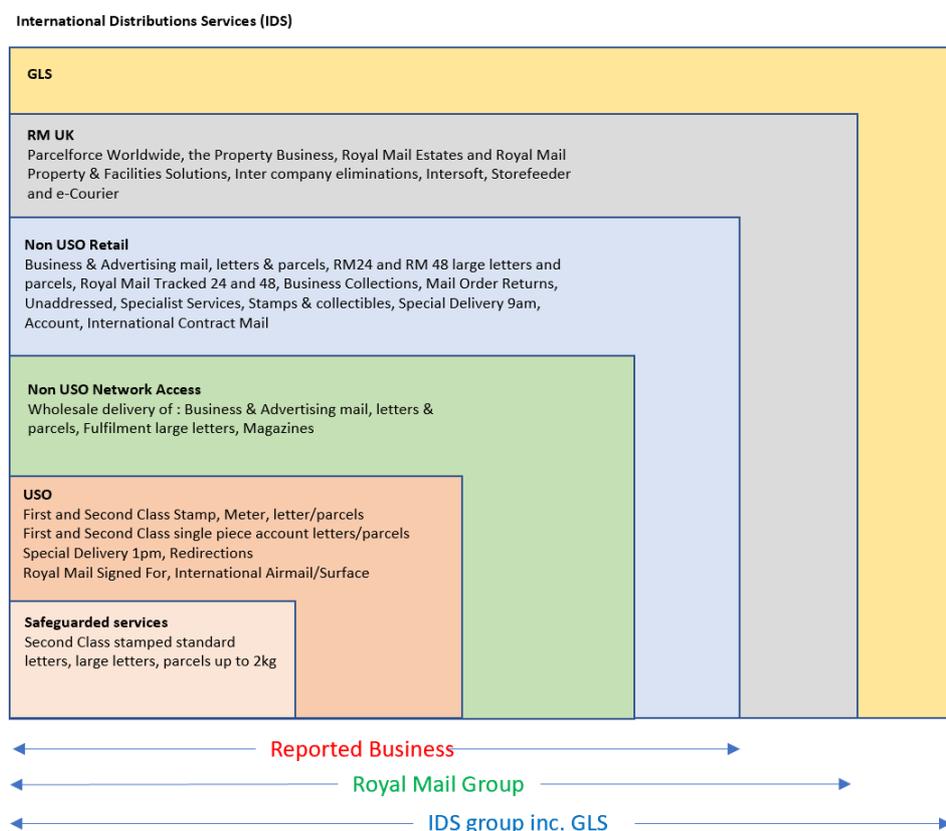
6.8 In its 2022-23 results announcement, Royal Mail forecast further losses for the UK business, with a view to returning to profit for the year 2024-25,¹⁸⁰ while noting that revenue growth is reliant on improving quality of service and operational change efficiencies.

6.9 Given the uncertainties about securing a reasonable commercial rate of return, we remain concerned about the long-term financial sustainability of the universal service.

Financial sustainability and costs

6.10 Figure 13 below sets out how the USO fits within the Reported Business, Royal Mail Group and International Distributions Services (IDS). Royal Mail’s Reported Business recorded revenues of £6,972m in 2022-23 and £7,121m in 2017-18. In 2022-23, 31% (£2,182m) of this revenue was attributed to universal services, while in 2017-18, the equivalent proportion was 40%. Therefore, the USO accounts for a relatively small, and declining, proportion of revenues for Royal Mail Group as a whole.

Figure 13: Reported Business, Royal Mail Group, International Distributions Services (IDS) (not to scale)



¹⁸⁰ Excluding voluntary redundancy costs.

- 6.11 The safeguard caps apply to a small proportion of USO services (and, therefore, to a smaller proportion of Reported Business revenue). In total, the services directly controlled by a safeguard cap (Second Class stamped standard letters, large letters and parcels weighing up to 2kg) accounted for £[X] in revenue in 2022-23, or [X]% of Reported Business revenue. Within this, Second Class standard letters accounted for £[X] or [X]% of total revenue, Second Class large letters for £[X] ([X]%), and Second Class parcels weighing up to 2kg for £[X] or [X]% of total revenue. Second Class standard and large letters combined represented <5% of total Reported Business revenue.
- 6.12 The safeguard caps would only impact on Royal Mail's revenues to the extent that they lead Royal Mail to set lower prices than it would do otherwise. Royal Mail has consistently priced substantially below the basket cap for all services within the basket, but it has in recent years priced Second Class standard letters close to or at the level of the cap, as shown in Figure 1 in section 2. The standard letter cap has therefore constrained Royal Mail's pricing for most of the current cap period.
- 6.13 We therefore requested analysis from Royal Mail demonstrating the impact on its revenues of different scenarios in which the standard letter cap was increased. This analysis entailed Royal Mail modelling a number of scenarios for both First Class and Second Class standard letter prices for the next five-year period, which was assumed as the period over which the safeguard caps would be in place. Most of the scenarios were chosen by Royal Mail. [X]¹⁸¹
- 6.14 The scenarios modelled by Royal Mail in the two submissions provided alternative approaches to price rises. These included [X]
- 6.15 [X]
- 6.16 While it is difficult to make a comparison to future Reported Business revenue, we note that the average annual additional revenue that Royal Mail's chosen theoretical pricing scenario would provide represents a very small proportion (<[X]%) of current (2022-23) Reported Business revenue.¹⁸²
- 6.17 We recognise that any increase in revenue would be welcome. However, given the small proportion of Reported Business revenue that the capped services contribute, and the analysis that demonstrates that even a significant real-terms increase in the standard letter cap would have a relatively small impact on total revenue, we consider that the caps are unlikely to have a significant impact on the financial sustainability of the universal service.
- 6.18 We have also had regard to the impact of any cap on Royal Mail's ability to cover the cost of providing the service, and specifically whether the price for Second Class letters covers the cost of delivering Second Class letters.

¹⁸¹ Royal Mail submissions to Ofcom, dated 8 March 2023 and 22 May 2023, [X]

¹⁸² [X]

- 6.19 There are several factors that will determine how the costs incurred to deliver Second Class letters will change over time. These include the impact of inflation on Royal Mail's costs (which on average will not necessarily move in line with CPI, i.e., they could be lower or higher), the impact of changes in volumes on its costs (which will depend on the extent to which costs vary in line with volumes or are more fixed in nature) and Royal Mail's ability to reduce costs by becoming more efficient.
- 6.20 It is therefore difficult to predict how the costs of providing Second Class letters will change relative to CPI. However, given the relatively common nature of Royal Mail's costs across its network,¹⁸³ we consider that, were prices allowed to remain constant in real terms (i.e., with CPI) and future volume declines stayed broadly in line with historic trends over the past five years, this would likely be sufficient to cover the incremental cost of providing the service.

Safeguard caps and efficiency incentives

- 6.21 As noted above, the future costs of providing Second Class letters will depend to a significant extent on Royal Mail's ability to make efficiency improvements. More generally, and as noted in our recent AMUs, it is essential for Royal Mail to become more efficient if it is to secure a commercial rate of return.
- 6.22 As a general point, we note that, if Royal Mail is able to increase prices in markets where it is not subject to effective competitive constraints, then its incentives to operate efficiently could be reduced. Therefore, price caps can play a role in increasing efficiency incentives. However, as we set out in the 2018-19 safeguard caps review, the safeguard caps are not intended, in and of themselves, solely to provide efficiency incentives to Royal Mail.¹⁸⁴ The safeguard caps apply only to a small proportion of the revenues of the Reported Business and the efficiency challenges faced by Royal Mail are considerably broader.
- 6.23 We continue to consider, as set out in our 2022 Review of Postal Regulation statement, that market conditions and shareholder pressures provide Royal Mail with incentives to make efficiency gains in order to maximise profits. Indeed, our analysis in that statement suggested that efficiency gains are critical for the USO to be sustainable, as Royal Mail cannot rely on revenue increases alone.¹⁸⁵

Provisional conclusion on our analysis

- 6.24 Revenues from Second Class standard and large letters account for only a small proportion (<5%) of Reported Business revenue. Therefore, even a significant uplift in the standard letter cap (which is currently constraining Royal Mail's pricing) would only have a relatively

¹⁸³ We have taken account of Fully Allocated Cost data provided by Royal Mail (on a confidential basis) in the Granular Data Extract file. As explained in our 2018 statement on Amendments to the Universal Service Provider Access Condition in relation to the margin squeeze control, we use 50% of fully allocated costs as a proxy for LRIC for the purposes of the margin squeeze control, but noted that Royal Mail considered a lower proportion was appropriate.

¹⁸⁴ Ofcom, 2019. Statement: [Review of the Second Class Safeguard Caps 2019](#), footnote 16.

¹⁸⁵ Ofcom, 2022. [Statement: Review of Postal Regulation](#), paragraphs 3.27 and 4.38.

small impact on total Reported Business revenue. Accordingly, we consider that retaining a cap is unlikely to have a significant impact on the financial sustainability of the universal service. We consider, in Section 7, the balance of the impact of the proposed safeguard caps on Royal Mail, and the protection of consumers by ensuring affordability.

- 6.25 Given the relatively common nature of Royal Mail's costs across its network, we consider that, if prices were allowed to remain constant in real terms for standard letters, then this would continue to be sufficient to cover the incremental cost of providing the service.
- 6.26 We set out our proposals on how the impact of any safeguard caps on the financial sustainability of the universal service should inform any safeguard caps in section 7.

Consultation question

Question 8: Do you agree with our analysis of the impact of the caps on the financial sustainability of the universal service? Please state your reasons and provide evidence to support your view.

7. Our proposals

- 7.1 In this section we set out our proposals for which Royal Mail services should be subject to a safeguard cap from April 2024, and the design, level and duration of this cap. This section makes proposals based on our analysis in sections 4, 5 and 6 in order to form part of our wider impact assessment.
- 7.2 Following our assessment in the preceding sections, we propose to:
- a) continue to impose a safeguard cap on Second Class standard and large letters but combine these into a single weighted basket cap;
 - b) remove the safeguard cap from Second Class parcels up to 2kg; and
 - c) set a CPI cap on the weighted basket of Second Class standard and large letters for a period of five years.
- 7.3 We are also setting out in this section how we would cap parcels weighing up to 2kg, should we consider, as a result of the consultation, that a cap is required on those services. This enables stakeholders to understand the impact of any change in our proposed approach to parcels.
- 7.4 Finally, following our consideration in section 5 of the affordability of other USO services, we continue to consider that safeguard caps on these services are not needed to ensure these services are affordable.
- 7.5 Annex 5 sets out the draft DUSP condition imposing the proposed safeguard cap on Royal Mail from 1 April 2024.

USO services subject to a safeguard cap

Impact of competition on services

- 7.6 As set out in our analysis in section 4, our provisional view is that Royal Mail continues to face very limited competitive constraints on its pricing of standard and large letters. It remains a monopolist in the provision of end-to-end services for single piece letters and we have no evidence that another end-to-end entrant of sufficient scale and scope would provide a competitive constraint to Royal Mail in the foreseeable future.
- 7.7 We reached a different provisional conclusion with respect to parcels under 2kg. Notwithstanding the continuing large market share of Royal Mail in this segment, the evidence suggests that competition by alternative parcel operators imposes a material pricing constraint on Royal Mail, effectively requiring Royal Mail to price at market levels.

Affordability considerations

- 7.8 In section 5, we considered the affordability of postal services. We noted that, while an affordability assessment at this time is challenging due to the significant increase in the cost of living, the evidence suggests that the current prices appear affordable for the large

majority of consumers, including those who are financially vulnerable, although we accept that there are some consumers in specific circumstances who will find the cost of a service to be unaffordable. We also noted that, in the current circumstances, real term price increases in services are likely to lead to some consumers experiencing incidences of significant detriment in relation to the cost of post for the first time or more frequently.

7.9 In section 5, we also reviewed the affordability of First Class services, Special Delivery and other USO services. Our conclusion was that these services remained affordable for consumers on the basis of the choices available to them and the frequency of their use.

Our proposal

7.10 We propose that Second Class standard and large letters should continue to be subject to a safeguard cap as our analysis suggests that:

- a) Royal Mail is not subject to effective competitive constraints on its pricing for letters; and
- b) above-inflation (i.e., above CPI) increases in letter services are likely to lead to a larger proportion of consumers, in particular vulnerable consumers, experiencing incidences of significant detriment more frequently.

7.11 We provisionally conclude that parcels should not be subject to a safeguard cap given the competitive constraints on pricing in this sector, which has led to prices reducing in real terms. We note that these parcel services will remain subject to the general requirement for universal services to be affordable. It also remains open to us to reimpose a safeguard cap on these services, if we found Royal Mail were able to use its pricing freedom to set prices at an unaffordable level.

Design, level and duration of the Second Class standard and large letter cap

The design of the cap

7.12 Since 2012, standard letters have been subject to a separate safeguard cap from large letters and parcels. However, given that we propose to remove the safeguard cap from parcels, we consider that it is appropriate to reconsider the structure of the safeguard caps on standard and large letters.

7.13 We consider that there is a good case for imposing a basket safeguard cap covering both standard and large letters. This is for the following reasons:

- a) Letters, regardless of size, share a common cost base and operational management;
- b) Standard and large letters operate in very similar market conditions, with Royal Mail holding a near-monopoly position in these markets;
- c) We have no evidence on the mix of different letter types (standard versus large letters) in a given period that an individual consumer uses, but it does not seem unreasonable

to consider that individual consumption is broadly aligned with the relative volumes of the different letter types. Accordingly, a weighted average basket cap for letters capped at an appropriate rate should have the impact of ensuring that consumers' overall consumption of letters is affordable; and

- d) Capping all letters in a single basket would allow Royal Mail to accommodate pricing changes to reflect cost changes and differences in demand sensitivity within a single control, giving Royal Mail some additional commercial flexibility, relative to individual caps on standard letters and large letters, to manage returns against the common cost base.
- 7.14 As the basket cap would be weighted by service volumes, the volume weighting of a service in the basket strongly determines the pricing freedom available to Royal Mail. We note in particular that large letter volumes are significantly lower than standard letter volumes. Based on 2022-23 volumes, large letters would account for a relatively small proportion (just over 3%) of the volume of all letters in the basket.¹⁸⁶
- 7.15 As the basket works by establishing average price changes weighted by volumes of each service, then as standard letters would make up a high proportion of letters in the basket, a change in their prices would have a significantly bigger impact than a change in other prices. This restricts the amount of flexibility Royal Mail could have for standard letters as increases in standard letters would weight strongly the overall movement in prices in the basket.
- 7.16 Conversely, Royal Mail would have greater pricing freedom for large letters if it constrained increases to the price of standard letters. However, we note that, although Royal Mail has increased prices for large letters significantly over the current cap period, the current basket cap provided scope for further price increases which Royal Mail has not utilised. This appears to indicate that Royal Mail is already pricing at its desired level and may have started to reach the limit of its ability to increase Second Class large letter prices profitably.
- 7.17 Given that we would expect consumers to buy a mix of standard and large letters, we consider it unlikely that Royal Mail exercising the pricing freedom it would have in respect of the services in the basket would pose a risk to affordability. In any event, the weighted structure of the basket naturally more tightly constrains price increases on the more commonly used standard letters than on large letters.
- 7.18 We also considered whether it would be appropriate to set a single safeguard cap on standard letters and a basket cap for large letters (the price of large letters varies by weight). This would provide tighter constraints on all services. However, we wish to maximise Royal Mail's commercial flexibility, including its ability to respond to variation in cost of supply and consumer demand between services, conditional on ensuring affordability. This is consistent with our objective to minimise the impact of the safeguard caps on the financial sustainability of the USO. Accordingly, we provisionally consider this to be a less appropriate option.

¹⁸⁶ Royal Mail Regulatory Financial Reporting Information.

Our proposal

- 7.19 We propose that stamped Second Class standard and large letters are subject to a single basket safeguard cap, weighted by volumes.

The level of the cap

- 7.20 The cap must be set at a level which we consider will be affordable for consumers, consistent with our objective to ensure that universal services are affordable, particularly for vulnerable consumers.
- 7.21 As we noted in Section 3, any price cap will reduce Royal Mail's commercial flexibility and could therefore adversely affect the financial sustainability of the universal service. Consequently, we aim to impose safeguard caps only to the extent appropriate to protect consumers and ensure affordability, thereby minimising the impact on the financial sustainability of the universal service.
- 7.22 As discussed above and in section 5, we consider that current letter prices are affordable for the large majority of consumers, including those who are vulnerable. However, we also recognise that there are some consumers in particular circumstances who may face affordability issues at current prices, but that, for these consumers, even a significant reduction in postal prices may not ensure that they are affordable.
- 7.23 Our analysis in section 5 leads us to the conclusion that by keeping letter prices constant in real terms, the frequency with which consumers experience significant detriment (which appears to be infrequent) should not increase. Accordingly, we consider that consumers should not be materially disadvantaged if prices were to increase by CPI, but that real-terms increases could risk an increase in consumers, in particular vulnerable consumers, experiencing incidences of significant detriment in relation to letter prices, more frequently.
- 7.24 On this basis, we consider that the basket of standard and large Second Class letters should be capped at current prices, plus annual increases of CPI starting in year 1.
- 7.25 To ensure that this intervention is consistent with our duties with respect to having regard to the financial sustainability of the USO, we have considered the impact on Royal Mail. As set out in section 6, we note that standard and large letters together contribute a small proportion of total Reported Business revenue. In our provisional view, therefore, setting the cap at this level is unlikely to have a significant impact on the financial sustainability of the universal service, as it will remain the same in real terms. The additional revenue that Royal Mail considers it could achieve through its chosen theoretical pricing scenario would have a relatively small impact on the financial sustainability of the universal service, but would risk an increase in the number of consumers, in particular vulnerable consumers, experiencing affordability challenges more frequently.
- 7.26 We have also considered whether a one-off adjustment in the level of the cap is necessary to ensure Royal Mail can manage increases in costs due to volume decline. We note that in our 2018-19 review, we applied a one-off 5% adjustment to the level of the standard letter

cap in real terms. This was to grant Royal Mail sufficient headroom under the cap and improve its ability to respond to unforeseen market developments which could threaten the sustainability of the universal service.

- 7.27 Unlike in 2018-2019, however, consumers now face a considerably higher cost of living and, in some cases, lower incomes in real terms, and, as noted above, we consider that increasing the caps beyond CPI would risk an increase in consumers, in particular vulnerable consumers, experiencing incidences of significant detriment in relation to the cost of post more frequently. Further, and as noted in section 6, given the relatively common nature of Royal Mail's costs across its network, we consider that if prices were allowed to remain constant in real terms for letters (i.e. increase by no more than CPI), this would continue to be sufficient to cover the incremental cost of providing the service. This means that we also see no evidence for the need for a cap structure that allows for ongoing increases in the cap beyond CPI.
- 7.28 We also note that (as set out above) the use of a basket cap for standard and large letters will allow Royal Mail greater commercial flexibility, including the ability to respond to variation in cost of supply and consumer demand between services.
- 7.29 However, we note that this conclusion is based on our current expectations that standard letter volumes will continue to decline in line with long term trends, and that the consequential rate of change of unit costs for standard letters will be consistent with these trends. Should the rate of decline in standard letter volumes persistently differ substantially from long term trends or we see a material and sustained downward trend in volumes for large letters, we may need to re-examine our assumptions on cost recovery and potentially reappraise the appropriateness of the cap level.
- 7.30 Currently, the level of the basket cap on large letters and parcels is determined based on the price of each service within the basket, weighted by the volumes of each service measured two years prior to the new price being set. This allows Royal Mail to make its pricing decisions in sufficient time before the start of a new financial year. We consider that this approach should also be used for the new letter prices.
- 7.31 We consider that the starting prices for services assumed in the basket should be the prices as at the date on which we publish our final statement on the safeguard caps.

Our proposal

- 7.32 We propose that the basket cap, containing Second Class stamped standard and large letters, should be capped at prices as at the date on which we publish our final statement, plus annual increases of CPI starting in year 1. We propose that the level of the cap should be weighted by the volumes of each service measured two years prior to the new price being set.

The duration of the cap

- 7.33 In our 2012 Statement on the postal regulatory framework, we decided to impose the regulatory framework for a period of seven years, in order to provide a sufficient period of

regulatory stability for the management of Royal Mail to fully address the challenges facing the business at that time. We imposed the safeguard caps for the same period but noted that we would review the level of the cap at an earlier date, if required.¹⁸⁷

- 7.34 In 2017, we decided to maintain the 2012 approach to regulation for a further five years, on the basis that we thought that a significant change in our regulatory approach would be inappropriate and that maintaining the approach adopted in 2012 would best achieve our duties under the CA 2003 and the PSA 2011.¹⁸⁸
- 7.35 In 2019, we considered setting the cap on an indefinite basis but, following Royal Mail's representations that this approach would not take adequate account of changes in the nature of affordability and demand, we decided that the caps would expire on 31 March 2024.
- 7.36 We provisionally consider that it remains appropriate for the safeguard caps to apply for a defined period, and that five years would provide regulatory certainty while also allowing us to have reasonable insight into the financial and sustainability impacts of the cap over time.
- 7.37 However, we note that defining the duration of the safeguard caps would not preclude us from taking prompt action in the event of material concerns regarding affordability for consumers or Royal Mail's ability to finance the universal postal service, particularly in the event of a substantial change in consumer demand. We consider that in such events we could take steps to respond quickly.

Our proposal

- 7.38 We propose that the basket cap on standard and large letters should be in place for five years, meaning that it would apply from 1 April 2024 to 31 March 2029.

Second Class parcels up to 2kg

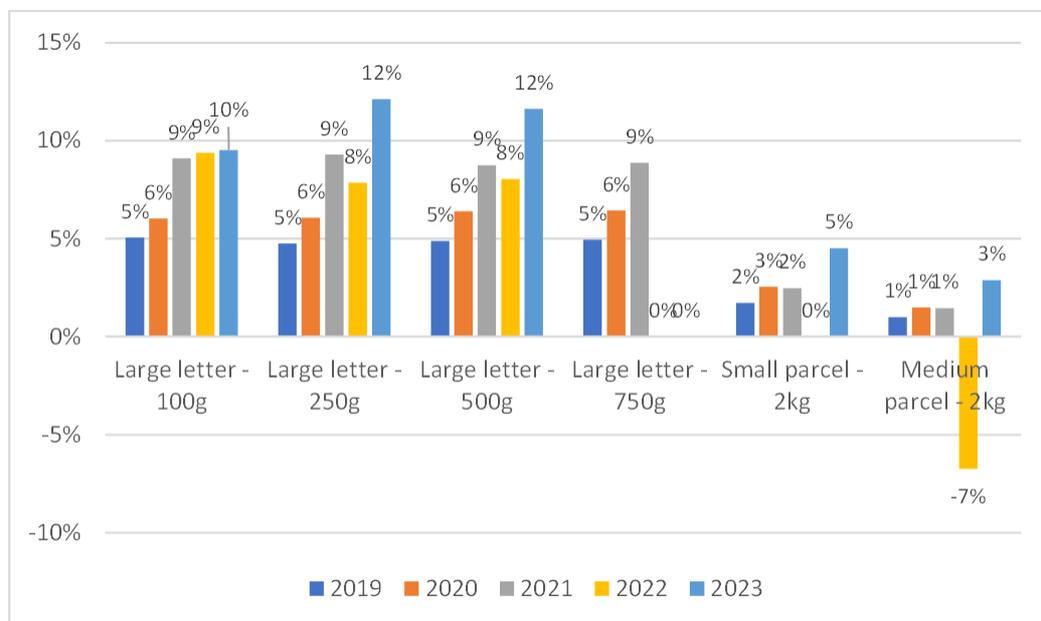
- 7.39 Our analysis in section 4 makes it clear that parcels operate in a different competitive environment from letters and that Royal Mail is subject to a material pricing constraint. Consequently, we consider that it is no longer appropriate for these services to be subject to a safeguard cap.
- 7.40 However, as noted above, we consider that it may be useful to stakeholders to set out a position on a possible safeguard cap for parcels in the event that, following consultation and contrary to our current provisional conclusion, we instead conclude that parcels should remain subject to a safeguard cap.
- 7.41 Royal Mail's pricing behaviour over the past few years suggests that it considers that it has greater scope to increase the pricing of large letters than that of parcels. This has led to substantial differences in the percentage increases in large letters compared to parcels in

¹⁸⁷ Ofcom, 2012. [Securing the Universal Postal Service: Decision on the new regulatory framework](#).

¹⁸⁸ Ofcom, 2017. [Review of the Regulation of Royal Mail: Statement](#).

the basket, to the extent that we consider the basket has proved increasingly ineffective in ensuring that the prices of large letters are constrained by the basket cap. These pricing changes can be seen in Figure 14 below.

Figure 14: Year-on-year nominal price change, large letters and small and medium parcels, 2019-20 – 2023-4



Source: Ofcom analysis of Royal Mail Price Guides. As parcel prices vary by whether they are purchased online or offline, the figure presented here is an average across both.

7.42 Accordingly, were we to change our provisional view on the need for a safeguard cap on parcels, we would propose setting a simple basket cap covering parcels weighing up to 2kg. We would also propose that the cap would increase by CPI annually for the same reasons set out above on the level of the proposed basket cap on standard and large letters.

Royal Mail targeted stamp discount scheme

7.43 We are aware that Royal Mail is considering the viability of a targeted stamp discount scheme, with a particular focus on vulnerable consumers.¹⁸⁹ Royal Mail has yet to provide us with a developed proposal and accordingly we are not able to take account of its potential at this stage of our review of the safeguard caps.

7.44 Royal Mail is currently considering whether a direct distribution of free stamps to vulnerable consumers would address affordability concerns, but has expressed a desire to work with Ofcom and other stakeholders to refine the proposed target audience and determine what an appropriate value of stamps distributed should be. Royal Mail would expect, as part a targeted scheme, that it should have greater pricing freedom for letters.

¹⁸⁹ We note that such schemes exist elsewhere – see, for example, AustraliaPost’s discounts for concession card holders and charities <https://auspost.com.au/about-us/supporting-communities/services-all-communities> [accessed 13/06/2023]

- 7.45 In the event that we receive a proposal during the review or after its completion, we will consider it and the potential implications (if any) on our proposed structure and level of safeguard caps, including whether there is scope for such a scheme to fully or partially replace the safeguard caps.
- 7.46 We would welcome, in support of future discussions with Royal Mail, stakeholders' views on who might be the target groups for such a scheme, how such a scheme might best be structured – free stamps or discounted stamps for example – and how access to, or take up of, such a scheme might be best promoted, noting the challenges of take-up of other existing consumer schemes (for example, the telecoms social tariff schemes).¹⁹⁰

How our proposals meet our objectives

- 7.47 We set out below how we consider that our proposals meet our policy objectives.

Ensure universal services are affordable, particularly for vulnerable consumers

- 7.48 As per our conclusions in section 5, we consider that most consumers do not experience significant detriment as a result of postal prices, and therefore that current letter prices are affordable for most consumers, including those who are vulnerable. We do however recognise that, there are some consumers in particular circumstances who may face affordability issues at current prices, but that, for these consumers, even a significant reduction in postal prices may not ensure that they are affordable.
- 7.49 We expect that setting our proposed basket safeguard cap for Second Class standard and large letters at current prices plus annual increases by CPI will mean there should not be an increase in consumers, in particular vulnerable consumers, experiencing incidences of significant detriment more frequently.

Provide protection to consumers where such protection is unlikely to be provided by competitive markets

- 7.50 We propose to continue to provide the protection of safeguard caps to consumers in respect of services for which we have found that protection is unlikely to be provided by competition in the market, namely Second Class standard and large letters.
- 7.51 We consider that the growing competition in the C2X parcels segment will ensure that USO parcel prices remain affordable. Accordingly, we believe a safeguard cap on parcels weighing up to 2kg is no longer appropriate. We also note that competition appears to be providing protection to consumers in respect of Special Delivery, international parcel prices and other universal services.

¹⁹⁰ [Social tariffs: Cheaper broadband and phone packages - Ofcom](#)

Ensure any safeguard cap takes into account the costs of providing the capped service(s)

- 7.52 As per our analysis in section 6, we have taken into account the costs of providing the capped services. It is difficult to predict how the costs of supplying the capped services will evolve over time, as this will depend on factors such as letter volumes, input costs, and Royal Mail's ability to become more efficient. Nonetheless, we are confident (subject to volumes remaining broadly aligned with recent historic trends over the past five years) that prices remaining constant in real terms will be sufficient to cover the incremental costs of providing the relevant services. We therefore propose to allow the proposed basket cap on Second Class letters to rise by CPI and no more.
- 7.53 We consider that combining Second Class standard and large letters in a single basket will allow Royal Mail some greater commercial flexibility to respond to variations in the cost of supply or changes in demand on letters, but that this flexibility will not be excessive.

Minimise the impact of any safeguard cap on the financial sustainability of the universal service, while retaining incentives for Royal Mail to operate efficiently

- 7.54 As noted above, while it is not possible to fully predict how the costs for these services will evolve over the next 5 years, given the relatively common nature of Royal Mail's costs over its network, we are satisfied that, were prices allowed to remain constant in real terms (i.e., rise with CPI) and any future declines in volumes are broadly in line with historic trends over the past five years, this would be sufficient to cover the incremental cost of providing the service.
- 7.55 We consider we have minimized the impact of the safeguard caps on the financial sustainability of the universal service by imposing them only to the extent appropriate to protect consumers and ensure affordability.
- 7.56 Further, the capped services account for a small proportion (<5%) of Reported Business revenue. The safeguard cap would only cause Royal Mail to forego the revenue arising from any difference between the safeguard cap and the price it would set in the absence of a cap. Royal Mail's modelling suggests that this additional revenue could account for a very small proportion of Reported Business revenue, which we consider is unlikely to have a significant impact on the financial sustainability of the USO.
- 7.57 We also note that combining standard and large letters in a single basket cap should afford Royal Mail some additional commercial flexibility to help it to encourage a balance in demand which can be managed more effectively and efficiently, and to have sufficient commercial flexibility to recover costs across these services.
- 7.58 We note that efficiency gains are critical for the USO to be sustainable, as Royal Mail cannot rely on revenue increases alone. While the safeguard caps are not intended, in and of themselves, solely to provide efficiency incentives to Royal Mail, setting the letters cap at current prices plus CPI should ensure that Royal Mail's incentives are not reduced.

Legal tests

- 7.59 Pursuant to paragraph 1 of schedule 6 to the PSA 2011, we may modify or revoke a regulatory condition only if we are satisfied that the modification or revocation:
- a) is objectively justifiable;
 - b) does not discriminate unduly against particular persons or a particular description of persons;
 - c) is proportionate to what it is intended to achieve; and
 - d) is transparent in relation to what it is intended to achieve.
- 7.60 We consider our proposals to modify DUSP 3 and revoke DUSP 2 satisfy these tests for the following reasons:
- a) We believe our proposals to be **objectively justifiable**. Firstly, they take into account the experience of consumers as regards the affordability of the universal postal service, as discussed in section 5. Our analysis suggests that any real increase in the price of letters would make postal services unaffordable for more consumers. We are therefore proposing that both standard and large letters remain subject to a safeguard cap (which is proposed to be permitted to rise in line with CPI), which we believe will protect consumers and should not increase the proportion of consumers finding postal services to be unaffordable. Royal Mail has reduced its parcel prices in real terms, suggesting that the increasing competitive constraints to which Royal Mail is subject to with respect to parcels are keeping prices affordable. We therefore consider that the safeguard cap on parcels can be removed. Further, we are making these proposals recognising that taking Royal Mail's costs of provision into account and granting Royal Mail an appropriate degree of commercial flexibility is important to ensuring the universal service is financially sustainable, and balancing that against the need to ensure Royal Mail is incentivised to operate efficiently. With those factors in mind, we consider the most appropriate way forward to be a basket cap for standard and large letters. We believe these proposals strike the right balance between our policy objectives.
 - b) We consider our proposals are **not unduly discriminatory** as they affect only Royal Mail, reflecting its unique position as the provider of the universal postal service in the UK. We have not identified any particular groups that would be disproportionately negatively impacted by our proposals.
 - c) We believe our proposals to be **proportionate** as they only impose requirements on Royal Mail as far as is appropriate and they do not go beyond what is necessary to achieve our objectives and to secure an affordable universal postal service. We have struck what we consider to be the right balance between ensuring that the universal postal service is affordable for consumers, that it is financially sustainable, and that Royal Mail remains incentivised to operate efficiently.

d) We consider our proposals to be **transparent** as they clearly set out the obligations we intend to impose on Royal Mail in its capacity as the designated universal service provider. The reasons for making our proposals are set out in this consultation document.

7.61 In making our proposals, we have also addressed in this consultation the requirements set out in section 36(5) of the PSA 2011. This states that, where we are exercising our power to impose a DUSP condition that makes provision as to the tariffs to be used for determining prices in accordance with which part of a universal postal service is to be provided, we must seek to ensure that prices are affordable (as to which see section 5), take account of costs (as to which see section 6), and provide incentives to provide the service efficiently (which forms part of our objectives).

7.62 We believe we have acted in accordance with our specific duty in section 29 of the PSA 2011 to carry out our postal functions in a way that we consider will secure an affordable universal postal service. As required under section 29, we have had regard to the financial sustainability of the universal service, including the need to make a reasonable commercial rate of return. This is why we have ensured our proposals take into account costs and grant Royal Mail an appropriate degree of commercial flexibility, whilst maintaining the affordability of the universal service. We have also had regard to the need for the provision of the universal service to be efficient and this is reflected in our objectives. Although we have granted Royal Mail some commercial flexibility in setting the prices of the services subject to the safeguard caps, we have sought to ensure that this flexibility does not enable Royal Mail to increase prices rather than seek to improve its efficiency in order to increase its revenues.

7.63 Finally, we consider we have complied with our general duties in section 3 of the CA 2003. In particular, we have had regard to those consumers we have identified as potentially vulnerable as regards postal matters and how our proposals may affect them. Taking account of the impact our proposals may have on consumers and Royal Mail, we are of the view that our proposals will further the interests of citizens and consumers in accordance with our principal duty set out in section 3(1) of the CA 2003.

Consultation questions

Question 9: Do you agree with our proposal for the structure of the safeguard cap to be based on a single basket which includes Second Class standard and large letters? Please state your reasons and provide evidence to support your view.

Question 10: Do you agree with our proposal to set the basket cap for Second Class standard and large letters at current prices plus CPI? Please state your reasons and provide evidence to support your view.

Question 11: Do you agree with our proposal to set the cap for five years? Please state your reasons and provide evidence to support your view.

Question 12: Do you agree with the structure of the basket set out in Annex 5 in which stamp prices are weighted by volumes of each service type based on the volumes measured two years prior to the control? Please state your reasons and provide evidence to support your view.

Question 13: Do you agree with our proposal to remove the safeguard cap from Second Class parcels up to 2kg? Please state your reasons and provide evidence to support your view.

Question 14: Do you consider that there is value in developing a targeted scheme focussing on vulnerable consumers? If yes, your views on characteristics of such a scheme including target groups, nature of support and delivery options. Please state your reasons and provide evidence to support your view

Question 15: Do you have any others comments on the proposed modifications to the relevant DUSP conditions through which we propose to implement our proposals, attached in Annex 5? Please state your reasons and provide evidence to support your view.

A1. Responding to this consultation

How to respond

- A1.1 Ofcom would like to receive views and comments on the issues raised in this document, by 5pm on 1 September 2023.
- A1.2 You can download a response form from [our website](#). You can return this by email or post to the address provided in the response form.
- A1.3 If your response is a large file, or has supporting charts, tables or other data, please email it to safeguardcaps@ofcom.org.uk, as an attachment in Microsoft Word format, together with the [cover sheet](#).
- A1.4 Responses may alternatively be posted to the address below, marked with the title of the consultation:
- Safeguard caps review team
Ofcom
Riverside House
2A Southwark Bridge Road
London SE1 9HA
- A1.5 We welcome responses in formats other than print, for example an audio recording or a British Sign Language video. To respond in BSL:
- send us a recording of you signing your response. This should be no longer than 5 minutes. Suitable file formats are DVDs, wmv or QuickTime files; or
 - upload a video of you signing your response directly to YouTube (or another hosting site) and send us the link.
- A1.6 We will publish a transcript of any audio or video responses we receive (unless your response is confidential)
- A1.7 We do not need a paper copy of your response as well as an electronic version. We will acknowledge receipt of a response submitted to us by email.
- A1.8 You do not have to answer all the questions in the consultation if you do not have a view; a short response on just one point is fine. We also welcome joint responses.
- A1.9 It would be helpful if your response could include direct answers to the questions asked in the consultation document. The questions are listed at Annex 4. It would also help if you could explain why you hold your views, and what you think the effect of Ofcom's proposals would be.
- A1.10 If you want to discuss the issues and questions raised in this consultation, please contact the team at safeguardcaps@ofcom.org.uk.

Confidentiality

- A1.11 Consultations are more effective if we publish the responses before the consultation period closes. In particular, this can help people and organisations with limited resources or familiarity with the issues to respond in a more informed way. So, in the interests of transparency and good regulatory practice, and because we believe it is important that everyone who is interested in an issue can see other respondents' views, we usually publish responses on [the Ofcom website](#) at regular intervals during and after the consultation period.
- A1.12 If you think your response should be kept confidential, please specify which part(s) this applies to, and explain why. Please send any confidential sections as a separate annex. If you want your name, address, other contact details or job title to remain confidential, please provide them only in the cover sheet, so that we don't have to edit your response.
- A1.13 If someone asks us to keep part or all of a response confidential, we will treat this request seriously and try to respect it. But sometimes we will need to publish all responses, including those that are marked as confidential, in order to meet legal obligations.
- A1.14 To fulfil our pre-disclosure duty, we may share a copy of your response with the relevant government department before we publish it on our website. This is the Department for Business and Trade (DBT) for postal matters, and the Department for Culture, Media and Sport (DCMS) for all other matters.
- A1.15 Please also note that copyright and all other intellectual property in responses will be assumed to be licensed to Ofcom to use. Ofcom's intellectual property rights are explained further in our [Terms of Use](#).

Next steps

- A1.16 Following this consultation period, Ofcom plans to publish a statement by the end of 2023.
- A1.17 If you wish, you can [register to receive mail updates](#) alerting you to new Ofcom publications.

Ofcom's consultation processes

- A1.18 Ofcom aims to make responding to a consultation as easy as possible. For more information, please see our consultation principles in Annex 2.
- A1.19 If you have any comments or suggestions on how we manage our consultations, please email us at consult@ofcom.org.uk. We particularly welcome ideas on how Ofcom could more effectively seek the views of groups or individuals, such as small businesses and residential consumers, who are less likely to give their opinions through a formal consultation.
- A1.20 If you would like to discuss these issues, or Ofcom's consultation processes more generally, please contact the corporation secretary:

Corporation Secretary
Ofcom
Riverside House
2a Southwark Bridge Road
London SE1 9HA
Email: corporationsecretary@ofcom.org.uk

A2. Ofcom's consultation principles

Ofcom has seven principles that it follows for every public written consultation:

Before the consultation

- A2.1 Wherever possible, we will hold informal talks with people and organisations before announcing a big consultation, to find out whether we are thinking along the right lines. If we do not have enough time to do this, we will hold an open meeting to explain our proposals, shortly after announcing the consultation.

During the consultation

- A2.2 We will be clear about whom we are consulting, why, on what questions and for how long.
- A2.3 We will make the consultation document as short and simple as possible, with an overview of no more than two pages. We will try to make it as easy as possible for people to give us a written response.
- A2.4 We will consult for up to ten weeks, depending on the potential impact of our proposals.
- A2.5 A person within Ofcom will be in charge of making sure we follow our own guidelines and aim to reach the largest possible number of people and organisations who may be interested in the outcome of our decisions. Ofcom's Consultation Champion is the main person to contact if you have views on the way we run our consultations.
- A2.6 If we are not able to follow any of these seven principles, we will explain why.

After the consultation

- A2.7 We think it is important that everyone who is interested in an issue can see other people's views, so we usually publish the responses on our website at regular intervals during and after the consultation period. After the consultation we will make our decisions and publish a statement explaining what we are going to do, and why, showing how respondents' views helped to shape these decisions.

A3. Consultation coversheet

BASIC DETAILS

Consultation title:

To (Ofcom contact):

Name of respondent:

Representing (self or organisation/s):

Address (if not received by email):

CONFIDENTIALITY

Please tick below what part of your response you consider is confidential, giving your reasons why

Nothing

Name/contact details/job title

Whole response

Organisation

Part of the response

If there is no separate annex, which parts? _____

If you want part of your response, your name or your organisation not to be published, can Ofcom still publish a reference to the contents of your response (including, for any confidential parts, a general summary that does not disclose the specific information or enable you to be identified)?

DECLARATION

I confirm that the correspondence supplied with this cover sheet is a formal consultation response that Ofcom can publish. However, in supplying this response, I understand that Ofcom may need to publish all responses, including those which are marked as confidential, in order to meet legal obligations. If I have sent my response by email, Ofcom can disregard any standard e-mail text about not disclosing email contents and attachments.

Ofcom aims to publish responses at regular intervals during and after the consultation period. If your response is non-confidential (in whole or in part), and you would prefer us to publish your response only once the consultation has ended, please tick here.

Name

Signed (if hard copy)

A4. Consultation questions

- A4.1 We have included a number of specific consultation questions throughout this document and we would like you to consider these when responding. We have set out these questions below for ease of reference. However, we are not seeking to limit the issues on which respondents may wish to comment and respondents are invited to include representations on any issues which they consider to be relevant.

Question 1: Do you agree with our assessment that our proposals will not discriminate against any groups with protected characteristics? Please state your reasons and provide evidence to support your view.

Question 2: Do you agree with our assessment under the Welsh Language Policy Marking Standards? Please state your reasons and provide evidence to support your view.

Question 3: Do you agree with the objectives we propose to use for our review of safeguard caps? Please state your reasons and provide evidence to support your view.

Question 4: Do you agree with our analysis of the market in relation to Second Class standard letters and large letters? Please state your reasons and provide evidence to support your view.

Question 5: Do you agree with our analysis of the market in relation to Second Class parcels up to 2kg? Please state your reasons and provide evidence to support your view.

Question 6: Do you agree with our approach to assessing affordability of postal services? Please state your reasons and provide evidence to support your view.

Question 7: Do you agree with our assessment of the affordability of Second Class postal prices? Please state your reasons and provide evidence to support your view.

Question 8: Do you agree with our analysis of the impact of the caps on the financial sustainability of the universal service? Please state your reasons and provide evidence to support your view.

Question 9: Do you agree with our proposal for the structure of the safeguard cap to be based on a single basket which includes Second Class standard and large letters? Please state your reasons and provide evidence to support your view.

Question 10: Do you agree with our proposal to set the basket cap for Second Class standard and large letters at current prices plus CPI? Please state your reasons and provide evidence to support your view.

Question 11: Do you agree with our proposal to set the cap for five years? Please state your reasons and provide evidence to support your view.

Question 12: Do you agree with the structure of the basket set out in Annex 5 in which stamp prices are weighted by volumes of each service type based on the volumes measured two years prior to the control? Please state your reasons and provide evidence to support your view.

Question 13: Do you agree with our proposal to remove the safeguard cap from Second Class parcels up to 2kg? Please state your reasons and provide evidence to support your view.

Question 14: Do you consider that there is value in developing a targeted scheme focussing on vulnerable consumers? If yes, your views on characteristics of such a scheme including target groups, nature of support and delivery options. Please state your reasons and provide evidence to support your view.

Question 15: Do you have any other comments on the proposed modifications to the relevant DUSP conditions through which we propose to implement our proposals, attached in Annex 5? Please state your reasons and provide evidence to support your view.

A5. Statutory notification: proposed revocation of DUSP 2 and modification of DUSP 3

NOTIFICATION OF PROPOSAL TO REVOKE DESIGNATED USP CONDITION 2 AND TO MODIFY DESIGNATED USP CONDITION 3 PURSUANT TO SECTION 36 OF, AND IN ACCORDANCE WITH SECTION 53 OF, AND SCHEDULE 6 TO, THE POSTAL SERVICES ACT 2011

BACKGROUND

(A) On 1 October 2011, responsibility for postal regulation transferred to Ofcom under the Act. Ofcom subsequently imposed on Royal Mail, as the designated universal service provider, certain designated USP conditions to make provision for matters set out in sections 36 and 37 of the Act. These conditions included DUSP 2,¹⁹¹ which put in place a safeguard cap for Second Class letters, and DUSP 3, which put in place a basket safeguard cap for Second Class large letters and parcels up to 2kg.¹⁹²

(B) Ofcom has since modified DUSP Conditions 2 and 3.¹⁹³ The most recent modifications were made on 17 January 2019, when Ofcom published a statement¹⁹⁴ setting out its decision to modify DUSP 2 so as to put in place a 5% real-terms increase to the level of the safeguard cap on Second Class standard letters and to make some minor modifications for clarity and to reflect the new period for which the cap would apply.¹⁹⁵ Ofcom also decided to make some minor modifications to DUSP 3.¹⁹⁶

PROPOSALS

1. Ofcom hereby proposes, in accordance with section 53 of, and Schedule 6 to, the Act, and pursuant to its powers under section 36 of the Act, to revoke DUSP 2 in its entirety and to modify

¹⁹¹ See Schedule 2 to the statutory notification published in Annex 7 of Ofcom's Statement of 27 March 2012: https://www.ofcom.org.uk/_data/assets/pdf_file/0019/71812/annex7.pdf

¹⁹² See Schedule 1 to the statutory notification published in Annex 1 of Ofcom's Statement of 20 July 2012: https://www.ofcom.org.uk/_data/assets/pdf_file/0015/72042/statement.pdf

¹⁹³ https://www.ofcom.org.uk/_data/assets/pdf_file/0022/50566/statement.pdf;
https://www.ofcom.org.uk/_data/assets/pdf_file/0032/108869/financial-reporting-Royal-Mail.pdf;
https://www.ofcom.org.uk/_data/assets/pdf_file/0026/108872/Annex-3.-DUSP-Modification-Notification.pdf

¹⁹⁴ https://www.ofcom.org.uk/_data/assets/pdf_file/0019/133660/Statement-Review-of-the-Second-Class-safeguard-caps-2019.pdf

¹⁹⁵ See the version of DUSP 2 currently in force: https://www.ofcom.org.uk/_data/assets/pdf_file/0018/133605/DUSP-Condition-2.pdf

¹⁹⁶ See the version of DUSP 3 currently in force: https://www.ofcom.org.uk/_data/assets/pdf_file/0019/133606/DUSP-Condition-3.pdf

DUSP 3 as set out in paragraph 2 of this Notification, in order to make further provision for matters set out in section 36 and to impose DUSP 3 on the universal service provider, Royal Mail.

2. The proposed modifications to DUSP 3 are specified in Schedule 1 to this Notification, marked up against the current DUSP 3 to show the changes that Ofcom is proposing to make. New text is in red font and highlighted in yellow. Deleted text is in black font, struck out, and highlighted in yellow.¹⁹⁷ For the avoidance of doubt, these markings do not form part of the proposed modifications. A version of the modified DUSP 3 without any markings is at Schedule 2 to this Notification.
3. As we are proposing to revoke DUSP 2 in its entirety, we have not included it as a Schedule to this Notification.
4. The proposals referred to in paragraphs 1 and 2 of this Notification are proposed to come into force on the date, provisionally 1 April 2024, specified in a notification setting out Ofcom's decisions on these matters in accordance with section 53 of, and paragraph 3(1) and (2) of Schedule 6 to, the Act.
5. The effect of, and Ofcom's reasons for making, these proposals are set out in the accompanying consultation document. In summary, Ofcom is proposing to reformulate the safeguard cap structure to a single basket cap on Second Class standard letters and large letters and to remove the safeguard cap in respect of Second Class parcels up to 2kg. Ofcom considers that the clearest and most appropriate way to achieve its intentions is by modifying DUSP 3, which is the current basket cap on Second Class large letters and parcels up to 2kg, so as to remove the latter from its scope and bring Second Class standard letters within its scope. This means DUSP 2, which places a safeguard cap on Second Class standard letters, is no longer needed, such that it can be revoked in its entirety.¹⁹⁸

OFCOM'S DUTIES AND LEGAL TESTS

6. Ofcom is satisfied that these proposals satisfy the general test in paragraph 1 of Schedule 6 to the Act.
7. In making these proposals, Ofcom has considered and acted in accordance with its duties in the Act and its general duties in section 3 of the Communications Act 2003.

MAKING REPRESENTATIONS

8. Representations may be made to Ofcom about the proposals set out in this Notification by no later than 1 September 2023.

¹⁹⁷ Please note that formatting changes are not indicated.

¹⁹⁸ For the avoidance of doubt, DUSP Condition 1 is unaffected by these proposals.

9. Copies of this Notification and the accompanying consultation document have been sent to the Secretary of State in accordance with paragraph 5(1)(a) of Schedule 6 to the Act.

10. Except insofar as the context otherwise requires, words or expressions shall have the meaning assigned to them in this Notification and otherwise any word or expression shall have the same meaning as it has been ascribed for the purpose of Part 3 of the Act.

11. In this Notification—

(a) “Act” means the Postal Services Act 2011 (c.5);

(b) “DUSP 2” means Designated USP Condition 2 referred to in recital (A) to this Notification, as amended by the modifications referred to in recital (B);

(c) “DUSP 3” means Designated USP Condition 3 referred to in recital (A) to this Notification, as amended by the modifications referred to in recital (B);

(d) “Ofcom” means the Office of Communications; and

(e) “Royal Mail” means Royal Mail Group Ltd, whose registered company number in England and Wales is 04138203.

12. For the purpose of interpreting this Notification—

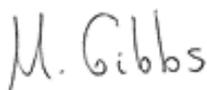
(a) headings and titles shall be disregarded;

(b) expressions cognate with those referred to in this Notification shall be construed accordingly; and

(c) the Interpretation Act 1978 (c. 30) shall apply as if this Notification were an Act of Parliament.

13. Schedules 1 and 2 to this Notification shall form part of this Notification.

Signed by



Marina Gibbs

Director of Post

A person duly authorised by Ofcom under paragraph 18 of the Schedule to the Office of Communications Act 2002

26 June 2023

SCHEDULE 1

DUSP 3 with modifications marked up

DESIGNATED USP CONDITION 3

SAFEGUARD CAP PRICE CONTROL FOR SECOND CLASS STANDARD LETTERS AND LARGE LETTERS AND RELEVANT PACKETS

3.1. Application, Definitions and Interpretation	
DUSP 3.1.1	This designated USP condition (“ DUSP Condition ”) shall apply to the <u>universal service provider</u> .
DUSP 3.1.2	<p>In this DUSP Condition—</p> <p>(a) “Base Year” means the period beginning on 1 April 20182023 and ending on 31 March 20192024;</p> <p>(b) “Basket” means the services of sending Standard Letters and Large Letters and Relevant Packet products by Second Class Post that the universal service provider currently provides (as set out in the Appendix to this DUSP Condition);</p> <p>(c) “Consumer Prices Index” means the index of consumer prices compiled by an agency or a public body on behalf of Her Majesty’s Government or a governmental department (which is the Office for National Statistics at the time of publication of this Notification) from time to time in respect of all items and which, at the time of publication of this Notification, is indexed against the year 2015;</p> <p>(d) “Large Letter” means a letter weighing up to 750 grams that is no more than 25 millimetres thick and up to 353 millimetres in length and up to 250 millimetres in width;</p> <p>(e) “Relevant Packet” means any item greater than a Large Letter in dimensions but weighing no more than 2kg;</p> <p>(ef) “Relevant Year” means any period of 12 consecutive months beginning on 1 April and ending on 31 March, the last period of which begins on 1 April 20232028 and ends on 31 March 20242029; and</p> <p>(fg) “Second Class Post” means a service of sending a stamped item by post where the universal service provider aims to deliver the item no later than the third working day after it was posted. For the purposes of this DUSP Condition, it does</p>

	<p>not include services which are not universal services or which include charges in respect of additional registered, insured, tracked or recorded services; and</p> <p>(g) “Standard Letter” means a letter weighing up to 100 grams that is no more than 5 millimetres thick and up to 240 millimetres in length and up to 165 millimetres in width.</p>
<p>DUSP 3.1.3</p>	<p>For the purpose of interpreting this DUSP Condition—</p> <p>(a) except in so far as the context otherwise requires, words or expressions shall have the meaning assigned to them in DUSP 3.1.2 above and otherwise any word or expression shall have the same meaning as it has been ascribed for the purpose of Part 3 of the Postal Services Act 2011;</p> <p>(b) headings and titles shall be disregarded;</p> <p>(c) expressions cognate with those referred to in this DUSP Condition shall be construed accordingly;</p> <p>(d) the Interpretation Act 1978 (c. 30) shall apply as if this DUSP Condition were an Act of Parliament; and</p> <p>(e) references in this DUSP Condition to “stamped” postal items (or mail) are references to traditional postage stamps or other types of labelling affixed to such items to indicate the amount of postage paid including where the postage has been sold online.</p>
<p><u>3.2 Maximum price to be charged for specified services</u></p>	
<p>DUSP 3.2.1</p>	<p>This DUSP Condition specifies the maximum prices that the <u>universal service provider</u> shall be permitted to charge for the group of services within the <u>Basket</u> in each <u>Relevant Year</u>.</p>
<p>DUSP 3.2.2</p>	<p>In each <u>Relevant Year</u> (which is represented as “<i>t</i>” in the formulas below), the price of services in the <u>Basket</u> (where each service in the Basket is represented as “<i>i</i>”) shall be set such that—</p> $\frac{\sum_i P_{i,t} V_{i,t-2}}{\sum_i V_{i,t-2}} \leq \left(\frac{\sum_i P_{i,0} V_{i,t-2}}{\sum_i V_{i,t-2}} \times X_t \right)$ <p>where—</p>

	<p>$X_t = (1 + 29.4\%) \times \frac{CPX_t}{CPX_0}$</p> <p>$P_{i,t}$ is the maximum price charged for sending a single Large Letter or Relevant Packet by Second Class Post each service in the Basket in Relevant Year t;</p> <p>$V_{i,t-2}$ is the volume delivered by the <u>universal service provider</u> in the twelve consecutive months from 1 April to 31 March in the year $t-2$, for each type of a Large Letter or Relevant Packet by Second Class Post service in the Basket (which is represented as "i") as calculated by the <u>universal service provider</u> using a reasonable methodology which has been disclosed to <u>OFCOM</u>;</p> <p>$P_{i,0}$ is the price as listed in the Appendix to this DUSP Condition charged for sending a single Large Letter or Relevant Packet by Second Class Post each service in the Basket as at 17 January 2019 [date of publication of Ofcom's final statement in this review] (which is represented as "0");</p> <p>CPX_0 is the <u>Consumer Prices Index</u> for the month of September immediately before the beginning of the a Base Year (rounded to one decimal place), the figure of which is 104.1 123.8; and</p> <p>CPX_t is the <u>Consumer Prices Index</u> for the month of September immediately before the beginning of a <u>Relevant Year</u> (rounded to one decimal place).</p>
<p>DUSP 3.2.3</p>	<p>Where the <u>universal service provider</u> makes a material change (other than to a charge) to any product or service which is subject to this DUSP Condition or there is a material change in the basis of the <u>Consumer Prices Index</u>, DUSP Conditions 3.2.1 and 3.2.2 shall have effect subject to such reasonable adjustment to take account of the change as <u>OFCOM</u> may direct to be appropriate in the circumstances. For these purposes, a material change to any product or service which is subject to this DUSP Condition includes the introduction of a new product or service wholly or substantially in substitution for that existing product or service listed in the Appendix to this DUSP Condition.</p>
<p>DUSP 3.2.4</p>	<p>The <u>universal service provider</u> shall record, maintain and supply to <u>OFCOM</u> in writing, within one month of the coming into effect of any price increase, the data necessary for <u>OFCOM</u> to monitor compliance of the <u>universal service provider</u> with the requirements of this DUSP Condition.</p>
<p>DUSP 3.2.5</p>	<p>This DUSP Condition shall not apply to such extent as <u>OFCOM</u> may direct.</p>
<p>DUSP 3.2.6</p>	<p>The <u>universal service provider</u> shall comply with any direction <u>OFCOM</u> may make from time to time under this DUSP Condition.</p>

Appendix

	Description of postal item product or service	Maximum price as at 17 January 2019 [date of publication of Ofcom's final statement in this review]
1.	<u>Second Class Post, Standard Letter</u>	[price]
1- 2.	<u>Second Class Post, Large Letter, 0-100 grams</u>	£0.79[price]
2- 3.	<u>Second Class Post, Large Letter, Second Class Post, 101-250 grams</u>	£1.26[price]
3- 4.	<u>Second Class Post, Large Letter, 251-500 grams</u>	£1.64[price]
4- 5.	<u>Second Class Post, Large Letter, 501-750 grams</u>	£2.22[price]
5.	<u>Second Class Post, Relevant Parcel not exceeding length 45cm x width 35cm x depth 16cm (small parcel), 0-2kg</u>	£2.95
6.	<u>Second Class Post, Relevant Parcel not exceeding length 45cm x width 35cm x depth 16cm (small parcel), 0-2kg, (sold online only)</u>	£2.85
7.	<u>Second Class Post, Relevant Parcel not exceeding length 61cm x width 46cm x depth 46cm (medium parcel), 0-2kg</u>	£5.05
8.	<u>Second Class Post, Relevant Parcel not exceeding length 61cm x width 46cm x depth 46cm (medium parcel), 0-2kg, (sold online only)</u>	£4.95

Table of terms defined in the Postal Services Act 2011

This table is provided for information and does not form a part of this DUSP Condition. We make no representations as to its accuracy or completeness. Please refer to the Postal Services Act 2011.

Defined term	Section of the Postal Services Act 2011
OFCOM	90
universal service provider	65(1) and Schedule 9 paragraph 3(3)

SCHEDULE 2

Modified DUSP 3 with no markings

DESIGNATED USP CONDITION 3

SAFEGUARD CAP PRICE CONTROL FOR SECOND CLASS STANDARD LETTERS AND LARGE LETTERS

3.1. Application, Definitions and Interpretation	
DUSP 3.1.1	This designated USP condition (“ DUSP Condition ”) shall apply to the <u>universal service provider</u> .
DUSP 3.1.2	<p>In this DUSP Condition—</p> <p>(a) “Base Year” means the period beginning on 1 April 2023 and ending on 31 March 2024;</p> <p>(b) “Basket” means the services of sending <u>Standard Letters</u> and <u>Large Letters</u> by <u>Second Class Post</u> that the <u>universal service provider</u> currently provides (as set out in the Appendix to this DUSP Condition);</p> <p>(c) “Consumer Prices Index” means the index of consumer prices compiled by an agency or a public body on behalf of Her Majesty’s Government or a governmental department (which is the Office for National Statistics at the time of publication of this Notification) from time to time in respect of all items and which, at the time of publication of this Notification, is indexed against the year 2015;</p> <p>(d) “Large Letter” means a letter weighing up to 750 grams that is no more than 25 millimetres thick and up to 353 millimetres in length and up to 250 millimetres in width;</p> <p>(e) “Relevant Year” means any period of 12 consecutive months beginning on 1 April and ending on 31 March, the last period of which begins on 1 April 2028 and ends on 31 March 2029;</p> <p>(f) “Second Class Post” means a service of sending a stamped item by post where the <u>universal service provider</u> aims to deliver the item no later than the third working day after it was posted. For the purposes of this DUSP Condition, it does not include services which are not universal services or which include charges in respect of additional registered, insured, tracked or recorded services; and</p>

	<p>(g) “Standard Letter” means a letter weighing up to 100 grams that is no more than 5 millimetres thick and up to 240 millimetres in length and up to 165 millimetres in width.</p>
DUSP 3.1.3	<p>For the purpose of interpreting this DUSP Condition—</p> <p>(a) except in so far as the context otherwise requires, words or expressions shall have the meaning assigned to them in DUSP 3.1.2 above and otherwise any word or expression shall have the same meaning as it has been ascribed for the purpose of Part 3 of the Postal Services Act 2011;</p> <p>(b) headings and titles shall be disregarded;</p> <p>(c) expressions cognate with those referred to in this DUSP Condition shall be construed accordingly;</p> <p>(d) the Interpretation Act 1978 (c. 30) shall apply as if this DUSP Condition were an Act of Parliament; and</p> <p>(e) references in this DUSP Condition to “stamped” postal items (or mail) are references to traditional postage stamps or other types of labelling affixed to such items to indicate the amount of postage paid including where the postage has been sold online.</p>
<p>3.2 Maximum price to be charged for specified services</p>	
DUSP 3.2.1	<p>This DUSP Condition specifies the maximum prices that the <u>universal service provider</u> shall be permitted to charge for the group of services within the <u>Basket</u> in each <u>Relevant Year</u>.</p>
DUSP 3.2.2	<p>In each <u>Relevant Year</u> (which is represented as “<i>t</i>” in the formulas below), the price of services in the <u>Basket</u> (where each service in the <u>Basket</u> is represented as “<i>i</i>”) shall be set such that—</p> $\frac{\sum_i P_{i,t} V_{i,t-2}}{\sum_i V_{i,t-2}} \leq \left(\frac{\sum_i P_{i,0} V_{i,t-2}}{\sum_i V_{i,t-2}} \times X_t \right)$ <p>where—</p> $X_t = \frac{CPX_t}{CPX_0}$ <p><i>P_{i,t}</i> is the maximum price charged for each service in the <u>Basket</u> in <u>Relevant Year</u></p>

	<p>t;</p> <p>$V_{i,t-2}$ is the volume delivered by the <u>universal service provider</u> in the twelve consecutive months from 1 April to 31 March in the year $t-2$, for each service in the <u>Basket</u> as calculated by the <u>universal service provider</u> using a reasonable methodology which has been disclosed to <u>OFCOM</u>;</p> <p>$P_{i,0}$ is the price as listed in the Appendix to this DUSP Condition charged for each service in the <u>Basket</u> as at [<i>date of publication of Ofcom’s final statement in this review</i>] (which is represented as “0”);</p> <p>CPX_0 is the <u>Consumer Prices Index</u> for the month of September immediately before the beginning of the <u>Base Year</u> (rounded to one decimal place), the figure of which is 123.8; and</p> <p>CPX_t is the <u>Consumer Prices Index</u> for the month of September immediately before the beginning of a <u>Relevant Year</u> (rounded to one decimal place).</p>
<p>DUSP 3.2.3</p>	<p>Where the <u>universal service provider</u> makes a material change (other than to a charge) to any service which is subject to this DUSP Condition or there is a material change in the basis of the <u>Consumer Prices Index</u>, DUSP Conditions 3.2.1 and 3.2.2 shall have effect subject to such reasonable adjustment to take account of the change as <u>OFCOM</u> may direct to be appropriate in the circumstances. For these purposes, a material change to any service which is subject to this DUSP Condition includes the introduction of a new service wholly or substantially in substitution for that existing service listed in the Appendix to this DUSP Condition.</p>
<p>DUSP 3.2.4</p>	<p>The <u>universal service provider</u> shall record, maintain and supply to <u>OFCOM</u> in writing, within one month of the coming into effect of any price increase, the data necessary for <u>OFCOM</u> to monitor compliance of the <u>universal service provider</u> with the requirements of this DUSP Condition.</p>
<p>DUSP 3.2.5</p>	<p>This DUSP Condition shall not apply to such extent as <u>OFCOM</u> may direct.</p>
<p>DUSP 3.2.6</p>	<p>The <u>universal service provider</u> shall comply with any direction <u>OFCOM</u> may make from time to time under this DUSP Condition.</p>

Appendix

	Description of postal service	Maximum price as at [date of publication of Ofcom's final statement in this review]
1.	<u>Second Class Post, Standard Letter</u>	[price]
2.	<u>Second Class Post, Large Letter, 0-100 grams</u>	[price]
3.	<u>Second Class Post, Large Letter, Second Class Post, 101-250 grams</u>	[price]
4.	<u>Second Class Post, Large Letter, 251-500 grams</u>	[price]
5.	<u>Second Class Post, Large Letter, 501-750 grams</u>	[price]

Table of terms defined in the Postal Services Act 2011

This table is provided for information and does not form a part of this DUSP Condition. We make no representations as to its accuracy or completeness. Please refer to the Postal Services Act 2011.

Defined term	Section of the Postal Services Act 2011
<i>OFCOM</i>	90
<i>universal service provider</i>	65(1) and Schedule 9 paragraph 3(3)

A6. Legal and regulatory framework

A6.1 Our principal duty across all of our different functions is to further the interests of consumers and citizens. In relation to post, we must perform our functions in a way that we consider will secure the provision of a universal postal service. The provision of a universal postal service includes the provision of a number of end-to-end services (as defined in the legislation) at affordable prices. In carrying out this duty, we must also have regard to the need for the universal service to be financially sustainable (including the need to make a reasonable commercial rate of return) and efficient.

Statutory basis for postal regulation

A6.2 The [Postal Services Act 2011](#) (the “**PSA 2011**”) contains the statutory basis for the requirement to establish a universal postal service in the United Kingdom. The PSA 2011 currently implements the EU Postal Services Directive (the “**Directive**”).¹⁹⁹

A6.3 Section 31 of the PSA 2011 sets out various requirements that, as a minimum, must be included in the universal postal service:

- a) At least one delivery of letters every Monday to Saturday and of other postal packets²⁰⁰ every Monday to Friday to the home or premises of every individual or other person in the United Kingdom or to such identifiable points as approved by Ofcom.
- b) At least one collection of letters every Monday to Saturday and of other postal packets every Monday to Friday for the purpose of onwards transmission in connection with the provision of the universal service (including onwards transmission outside of the United Kingdom).
- c) A service of conveying postal packets from one place to another by post at affordable prices determined in accordance with a public tariff which is uniform throughout the United Kingdom (including conveyance outside of the United Kingdom).
- d) A registered items service²⁰¹ at affordable prices determined in accordance with a public tariff which is uniform throughout the United Kingdom.

¹⁹⁹ Although EU Directives no longer apply to the United Kingdom following Brexit, the PSA 2011 is a piece of United Kingdom legislation and is still in force. The Directive therefore remains relevant to the interpretation and application of the PSA 2011. The Directive was introduced to, amongst other things, establish a universal postal service providing a minimum range of services of specified quality in all Member States of the EU at an affordable price for the benefit of all users, irrespective of geographical location (recital 11).

²⁰⁰ “Postal packets” means a letter, parcel, packet or other article transmissible by post (section 27(2) of the PSA 2011).

²⁰¹ “Registered items service” means a service of conveying postal packets from one place to another by post which provides—

- e) An insured items service²⁰² at affordable prices determined in accordance with a public tariff which is uniform throughout the United Kingdom.
- f) The provision free of charge of such postal services as are specified in the universal postal service order to such descriptions of blind or partially sighted persons as are so specified.
- g) A service of conveying free of charge qualifying legislative petitions and addresses.^{203 204}

Ofcom's duties

Duties in relation to post

- A6.4 Our principal duty under the [Communications Act 2003](#) (the "CA 2003") when carrying out our functions, including in relation to post, is to further the interests of citizens and of consumers, where appropriate by promoting competition.²⁰⁵
- A6.5 When performing our duty to further the interests of consumers, we must have regard, in particular, to the interests of those consumers in respect of choice, price, quality of service and value for money.²⁰⁶
- A6.6 The PSA 2011 also imposes on us a specific duty in respect of post, which we must treat equally to our duty under the CA 2003 where possible. That duty is to carry out our functions related to post in a way that we consider will secure the provision of a universal postal service.²⁰⁷
- A6.7 "Provision of a universal postal service" is not defined in the PSA 2011 but the legislation says that this phrase must be read in accordance with sections 30 to 33.²⁰⁸ These sections require us to, by order, set out the services that must be provided as part of the universal service (as to which see paragraphs A1.17 to A1.19 below). These services must include at

-
- (a) for the registration of the packets in connection with their conveyance by post, and
 - (b) for the payment of an amount determined by the person providing the service in the event of the theft or loss of or damage to the packets (section 32(4) of the PSA 2011).

²⁰² "Insured items service" means a service of conveying postal packets from one place to another by post which, in the event of the theft or loss of or damage to the packets, provides for the payment of an amount up to the value of the packets as declared by the sender (section 32(1) of the PSA 2011).

²⁰³ The Explanatory Notes to the PSA 2011 confirm that section 31 complies with the requirements of Article 3(1) of the Directive, which states that "*Member States shall ensure that users enjoy the right to a universal service involving the permanent provision of a postal service of specified quality at all points in their territory at affordable prices for all users*".

²⁰⁴ Section 33 of the PSA 2011 sets out exceptions to the minimum requirements, which include postal packets whose weight exceeds 20 kilograms or whose dimensions fall outside of certain minimum and maximum dimensions as laid down by the Universal Postal Union; delivery and collection on bank holidays; delivery and collection in such geographical conditions or other circumstances as Ofcom considers to be exceptional; where a service is interrupted, suspended, or restricted in an emergency; and where individual agreements on price are concluded with customers.

²⁰⁵ Section 3(1) of the CA 2003.

²⁰⁶ Section 3(5) of the CA 2003.

²⁰⁷ Section 29(1) of the PSA 2011.

²⁰⁸ Section 65(2)(a) of the PSA 2011.

least the minimum requirements referred to in paragraph A1.3 above.²⁰⁹

- A6.8 In performing our duty under the PSA 2011, we must have regard to the need for the provision of the universal postal service to be: (a) financially sustainable; and (b) efficient before the end of a reasonable period²¹⁰ and for its provision to continue to be efficient at all subsequent times.²¹¹
- A6.9 The reference to the universal postal service needing to be financially sustainable includes the need for a reasonable commercial rate of return to be made on any expenditure incurred for the purpose of, or in connection with, the provision of the universal postal service.²¹²
- A6.10 The PSA 2011 does not require that we give more weight to one of those considerations than the other. We must take them both into account in arriving at a judgement as to how best to carry out our functions.

Other considerations under the CA 2003

- A6.11 There are a number of factors that we must also take into account when exercising our principal duty under the CA 2003.
- A6.12 We must have regard, in all cases, to the principles under which regulatory activities should be transparent, accountable, proportionate, consistent, and targeted only at cases in which action is needed, as well as any other principles appearing to us to represent the best regulatory practice.²¹³
- A6.13 Those principles include ensuring that our interventions are evidence-based, proportionate, consistent, accountable and transparent in both deliberation and outcome; that we seek the least intrusive regulatory mechanisms to achieve our policy objectives; and that we consult widely with all relevant stakeholders and assess the impact of regulatory action before imposing regulation upon a market.
- A6.14 Where they appear to us to be relevant in the circumstances, we must also have regard to considerations including (but not limited to):
- a) the needs of persons with disabilities, of the elderly and of those on low incomes;
 - b) the opinions of consumers in relevant markets and of members of the public generally;

²⁰⁹ Section 30(2) of the PSA 2011.

²¹⁰ "A reasonable period" is defined in section 29(5) PSA 2011 as such period beginning with the day on which the relevant provisions of PSA 2011 come generally into force as Ofcom considers, in all the circumstances, to be reasonable.

²¹¹ Section 29(3) of the PSA 2011.

²¹² Section 29(4) PSA 2011.

²¹³ Section 3(3) of the CA 2003.

- c) the different interests of persons in the different parts of the United Kingdom, of the different ethnic communities within the United Kingdom and of persons living in rural and in urban areas; and
- d) the extent to which, in the circumstances of the case, the furthering or securing of the interests of citizens and of consumers (as referred to in paragraph A1.11 above) is reasonably practicable.²¹⁴

A6.15 Although where possible we must treat our duties under the CA 2003 and PSA 2011 equally, the latter would take priority if there were conflict between them.²¹⁵

Implementation of the regulatory framework

A6.16 We have the following powers and duties to secure the provision of a universal postal service:

- a) We must define the scope of a universal postal service in secondary legislation;
- b) We have the power to designate one (and in certain circumstances more than one) postal operators as universal service provider(s); and
We have the power to impose regulatory obligations on the postal operator(s) in the form of designated USP conditions (“**DUSP Conditions**”).

Universal Service Order

A6.17 As noted above, we are required under the PSA 2011 to make an order setting out a description of the services we consider should be provided in the United Kingdom as part of the universal postal service, as well as the standards with which those services are to comply.²¹⁶

A6.18 We therefore made the Postal Services (Universal Postal Service) Order 2012²¹⁷ (the “**Order**”) to fulfil that duty. The services that Royal Mail must provide as part of the universal postal service are set out in Article 5 of the Order and capture the minimum requirements set out in section 31 of the PSA 2011. They include a number of end-to-end services at affordable prices,²¹⁸ as follows:

²¹⁴ Section 3(4) of the CA 2003.

²¹⁵ Section 3(6A) of the CA 2003.

²¹⁶ Section 30(1) of the PSA 2011.

²¹⁷ <https://www.legislation.gov.uk/ukxi/2012/936/contents/made>

²¹⁸ These services are described more fully in schedule 1 to the Order. The other services that must be provided are the delivery services described in Article 6 and the collection services described in Article 7 of the Order (which for the most part are consistent with the first and second minimum requirements contained in section 31 of the PSA 2011 respectively); the free end-to-end services described in schedule 2 to the Order; and the addressee services described in schedule 3 to the Order.

- a) A priority single piece service²¹⁹ (i.e. 1st Class) for the conveyance of postal packets other than insured items, with a routing time of D+1;²²⁰
- b) A standard single piece service (i.e. 2nd Class) for the conveyance of postal packets other than insured items, with a routing time of D+3;²²¹
- c) A registered and insured service for items weighing no more than 10 kilograms with a routing time of D+1;
- d) A return to sender service;
- e) Incoming and outgoing services for the conveyance of postal packets to and from the EU; and
- f) Incoming and outgoing services for the conveyance of postal packets to and from the rest of the world.

A6.19 These end-to-end services must be provided at affordable prices determined in accordance with a public tariff that is uniform throughout the United Kingdom and on fair and reasonable terms.²²²

Designation of a universal service provider

A6.20 Pursuant to our duty to secure a universal postal service, we have designated Royal Mail Group Limited (“**Royal Mail**”) to provide the universal postal service throughout the United Kingdom.²²³

DUSP Conditions and the safeguard caps

A6.21 In order to secure the provision of the universal postal service, section 36 of the PSA 2011 empowers us to impose DUSP Conditions, as well as modify or revoke existing DUSP Conditions.²²⁴ The DUSP Conditions are regulatory obligations to secure the provision of the universal service (i.e. the services set out in the Order) and therefore form part of Royal Mail’s universal service obligations.

A6.22 In particular, we may impose or modify DUSP Conditions in order to set tariffs to be used for determining the prices of the universal postal service or a part of it.²²⁵

²¹⁹ Paragraph 1 of schedule 1 describes a “single piece service” as a postal service for the conveyance of an individual postal packet to the addressee, which is not subject to certain discounts.

²²⁰ This refers to a routing time of one working day (which includes Saturdays), i.e. the target maximum time for conveying the postal packet from the access point (e.g. a post box) to its delivery point is one working day.

²²¹ Similarly, this refers to a routing time of three working days.

²²² Article 8 of the Order.

²²³ Section 35 of the PSA 2011.

²²⁴ Paragraph 2(1) of schedule 6 to the PSA 2011 confirms that our power to impose a regulatory condition includes the power to revoke or modify the condition.

²²⁵ Section 36(4) of the PSA 2011.

Substantive requirements

- A6.23 We may only impose, modify or revoke a DUSP Condition where we consider it is necessary to do so in order to secure the provision of a service described in the Order, in accordance with the standards set out in the Order.²²⁶
- A6.24 We must be satisfied that the imposition, revocation or modification of a DUSP Condition: (a) is objectively justifiable; (b) does not discriminate unduly against particular persons or a particular description of persons; and (c) is proportionate and transparent in relation to what it is intended to achieve.²²⁷
- A6.25 Further, when exercising our power to set tariffs to be used for determining the prices in accordance with which a universal service, or part of a universal service, is provided, we must seek to ensure that the prices: (a) are affordable; (b) take account of the costs of providing the service or part of a service; and (c) provide incentives to provide the service or part of a service efficiently.²²⁸
- A6.26 Our power to impose, modify or revoke DUSP Conditions is subject to our duty to carry out our functions in relation to postal services in a way that we consider will secure the provision of a universal postal service²²⁹ (and, as noted above, when performing that duty we must have regard to the need for the universal service to be financially sustainable and efficient).²³⁰

Procedural requirements

- A6.27 The procedure for imposing, revoking or modifying a condition is set out in paragraph 3 of schedule 6 to the PSA 2011:
- a) Before imposing, modifying or revoking a condition, we must publish a notification: (i) stating our proposal; (ii) setting out the effect of our proposal; (iii) giving our reasons for the proposal; and (iv) specifying the period within which representations about the proposal can be made (which must be at least one month beginning with the day after the day the notification is published).
 - b) We may then only give effect to a proposal where we have: (i) considered every representation made to us; and (ii) had regard to every international obligation of the United Kingdom notified to us by the Secretary of State.

²²⁶ Section 36(3) of the PSA 2011.

²²⁷ Paragraph 1, schedule 6 to the PSA 2011.

²²⁸ Section 36(5) of the PSA 2011.

²²⁹ Section 29(2) of the PSA 2011.

²³⁰ Section 29(3) of the PSA 2011.

- c) We must then publish a notification setting out the imposition or modification or stating that the DUSP Condition has been revoked in a manner which is appropriate for bringing its contents to the attention of the persons who we consider are likely to be affected by its contents.

Safeguard caps

A6.28 We have exercised our condition-setting powers and have imposed a set of DUSP Conditions on Royal Mail as the designated provider. These regulatory obligations include the following two requirements in respect of tariffs charged by Royal Mail, which are referred to as safeguard caps:

- a) DUSP Condition 2²³¹ sets out the maximum amount that Royal Mail can charge for sending a single standard Letter by Second Class post. Following our 2019 review, in April 2019 the cap was set at 65.2p, to increase by CPI each year until the cap expires on 31 March 2024. The current price of a Second Class standard letter is 75p.
- b) DUSP Condition 3²³² sets out the maximum amount that Royal Mail can charge for services falling within the “Basket”, which includes Second Class large letters and small and medium parcels weighing up to 2 kilograms. The maximum prices for the Basket services are contained in the Appendix to DUSP Condition 3. They also increase by CPI each year and expire on 31 March 2024.

²³¹ https://www.ofcom.org.uk/_data/assets/pdf_file/0018/133605/DUSP-Condition-2.pdf

²³² https://www.ofcom.org.uk/_data/assets/pdf_file/0019/133606/DUSP-Condition-3.pdf