



The affordability of universal postal services

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Section 1

Summary

- 1.1 The Postal Services Act 2011 and the EU Postal Services Directive 1997 require universal postal service prices to be affordable.
- 1.2 In March 2012, we published our decision on the new regulatory framework for the postal sector ('the March 2012 statement').¹ This granted Royal Mail significantly more pricing flexibility to help secure the ongoing provision of the universal postal service, subject to certain key safeguards. These included safeguard caps on Second Class stamp Letters² and Second Class stamp Large Letters³ and packets up to 2kg to ensure vulnerable consumers could afford a basic universal postal service.⁴
- 1.3 Another safeguard was a commitment to an effective and ongoing monitoring regime to track Royal Mail's performance in respect of progress of efficiency, quality of service and the affordability of universal postal services. As part of that monitoring regime, we also committed to give further consideration to our approach to assessing whether universal postal services are affordable.
- 1.4 This report explains:
 - our approach to assessing whether universal postal services are affordable;
 - our findings following work to understand better consumers' use of and needs for post; and
 - how we will monitor affordability of universal postal services on an ongoing basis.
- 1.5 Our analysis has focused on those residential consumers and businesses that we consider are most likely to be at risk of not being able to afford universal postal services. For residential consumers this comprises consumers who have low income, and consumers who may be particularly reliant on postal services including, for example the elderly and disabled, or those who lack internet access. For businesses, this comprises small and medium businesses for which postal services are a critical input.
- 1.6 We have drawn on a variety of inputs and information sources to inform our assessment of the affordability of universal postal services, including existing and specially commissioned market research, input from consumer and industry stakeholders, and advice from social policy experts.

¹ Ofcom statement *Securing the Universal Postal Service* March 2012 available at: <http://stakeholders.ofcom.org.uk/binaries/consultations/review-of-regulatory-conditions/statement/statement.pdf>

² "Letters" means any item up to length 240mm, width 165mm, thickness 5mm and weighing no more than 100g.

³ "Large Letters" means any item larger than a Letter and up to length 353mm, width 250mm, thickness 25mm and weighing no more than 750g.

⁴ The safeguard cap on Second Class stamp Letters came into effect on 1 April 2012 and can be found at: <http://stakeholders.ofcom.org.uk/binaries/consultations/review-of-regulatory-conditions/statement/annex7.pdf>. The safeguard cap on Second Class stamp Large Letters and packets up to 2kg came into effect on 20 July 2012 and can be found at: <http://stakeholders.ofcom.org.uk/binaries/consultations/postal-service-letters-packets/statement/statement.pdf>.

- 1.7 In summary, the evidence we have collected indicates that universal postal services are affordable for both residential consumers (including low income and other vulnerable consumers) and businesses (including small and medium businesses) at current prices. We have reviewed the price changes that are due to take effect from 2 April 2013 (as announced by Royal Mail in March 2013), and consider that universal postal services will continue to be affordable following these changes.

Key findings for residential consumers

- 1.8 Overall, our findings suggest that universal postal services are affordable for almost all residential consumers, including low income and other vulnerable consumers, at current prices and prices to take effect in April 2013. We note that our research findings indicate that there are some very limited circumstances where a consumer could be at risk from not being able to afford universal postal services. These circumstances are where a consumer suffers both significant financial difficulty or very low income, and has a frequent need to send post items they consider to be essential. This reflects very particular circumstances and severe financial hardship. It is likely that consumers in such circumstances would unfortunately have concerns about the prices of universal postal services, even at much lower prices.

Key findings for businesses

- 1.9 Overall, our findings suggest that universal postal services are affordable for UK businesses, including small and medium businesses, at current prices and prices to take effect in April 2013. Although we found that a very small proportion of businesses might be at risk of being unable to afford universal postal service prices,⁵ we have not found (nor has it been raised with us) any evidence to show that such businesses are in fact unable to afford universal postal services or that the commercial viability of businesses would be significantly impacted by current prices or prices due to take effect from April 2013.

Next steps

- 1.10 We will continue to monitor affordability through our general monitoring regime to track Royal Mail's performance.⁶ In particular, we will continue to carry out our quantitative 'tracker' research for residential consumers and businesses to monitor post use, and to assess the affordability of universal postal services, value for money and satisfaction with post and postal prices. We will also commission further consumer research to explore consumer views and experience concerning affordability if we consider that this is necessary to supplement our ongoing monitoring.
- 1.11 We continue to welcome engagement on this important topic, in particular if stakeholders have evidence of universal postal services being unaffordable.

⁵ These would be specific types of business which have low turnover, low spend on mail, and where mail is 'core' to their business.

⁶ Ofcom *Annual monitoring update on postal the market* November 2012. Available at: <http://stakeholders.ofcom.org.uk/binaries/post/monitoring-update2011-12.pdf>

Section 2

Introduction

Importance of postal services

- 2.1 In 2011-12, fifteen billion items⁷ were delivered to more than 29 million addresses in the UK, and Royal Mail was responsible for delivering over 99% of these.⁸ The universal service obligation, fulfilled by Royal Mail, is central to the role that post plays in society and is relied upon by many residential consumers and small and medium businesses. The universal postal service requires Royal Mail to collect and deliver Letters six days a week to all addresses in the UK.⁹ The universal service obligation also requires that universal postal service prices be affordable and uniform throughout the UK.
- 2.2 Businesses generally use post for activities such as sending and receiving goods and communicating with their customers. Residential consumers generally receive significantly more post than they send and their average weekly expenditure on post is low. However, residential consumers continue to place significant value on a functioning and high quality postal service.
- 2.3 In recent years there have been significant decreases in mail volumes due in part to consumers and businesses switching to electronic forms of communication. Since 2006, overall market volumes have fallen by over 25%. In addition, there have been changes in product mix with many customers switching to lower cost alternatives, further reducing Royal Mail's revenue. We expect post to continue to play an essential role within the wider communications landscape, however, mail usage has yet to reach a new steady state and the future is highly uncertain.
- 2.4 It is within this context that we have explored approaches to assessing affordability of universal postal services.

Legal framework

- 2.5 We set out the details of the new regulatory framework for the postal services sector under the Postal Services Act 2011 ('the Act'), including our various duties and the framework for assessing any regulatory safeguards applicable to postal services, in the March 2012 statement.
- 2.6 In addition to that general framework, specific legal obligations apply to ensure the affordability of the universal postal services. These obligations and the obligations that Ofcom has in turn imposed on Royal Mail as the universal service provider are as follows:
- i) European Postal Services Directive;¹⁰

⁷ Inland addressed volumes – Royal Mail's 2011/12 annual report and financial statements (http://www.royalmailgroup.com/sites/default/files/Annual_Report_2012.pdf)

⁸ Royal Mail's 2010-11 annual report.

⁹ It is required to deliver packets five days a week.

¹⁰ Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service as amended by Directive 2002/39/EC, and Directive 2008/6/EC.

Article 3(1) requires Member States to “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”.

Article 12 requires Member States to take steps to ensure that the tariffs for each of the services forming part of the universal service comply with a number of principles, including that “prices shall be affordable”.

ii) Postal Services Act 2011;

Section 31 sets out various requirements that as a minimum must be included in a universal postal service, including a requirement for services at affordable prices in accordance with a uniform public tariff.

Section 36 gives Ofcom the power to impose a designated universal service provider condition on a universal service provider. Ofcom has the power to make provision as to the tariffs to be used for determining prices for universal postal services and, in exercising that power, must seek to ensure that, among other things, the prices are affordable.

iii) Universal Postal Services Order;¹¹

The Act requires Ofcom to make a Universal Postal Services Order¹² setting out a description of the services that it considers should be provided in the UK as a universal postal service and the standards with which those services are to comply. The Universal Postal Services Order requires the universal postal service to include end-to-end services¹³ at affordable prices.

iv) Designated Universal Services Provider (USP) Condition 1;¹⁴

Designated USP Condition 1 applies to Royal Mail as universal service provider and sets out various obligations on Royal Mail including an obligation to provide the end-to-end services listed in Designated USP Condition 1.6 at affordable prices.

Objective and scope of this report

- 2.7 In March 2012, we introduced a new regulatory framework for the postal sector.¹⁵ This moved away from a detailed price control regime and instead gave Royal Mail greater pricing freedom, subject to certain safeguards, to provide it with greater commercial flexibility to respond to changes in the market and address the financial sustainability of the universal postal service. To help ensure all consumers can access a basic, affordable universal postal service, we put in place safeguard caps

¹¹ SI 2012 No. 936 The Postal Services (Universal Postal Service) Order 2012.

¹² Under section 30 of the Act.

¹³ Schedule 1 of the Universal Postal Services Order lists the services that are end-to-end services. They comprise a single piece service, priority services, standard services, registered and insured services, return to sender services, outgoing European Union services, outgoing rest of world services, incoming European Union services and incoming rest of world services.

¹⁴ <http://stakeholders.ofcom.org.uk/binaries/consultations/review-of-regulatory-conditions/statement/annex7.pdf>

¹⁵ See footnote 1.

on Second Class single piece item prices (Second Class stamp Letters, Large Letters and packets up to 2kg).¹⁶

- 2.8 As part of the new regulatory approach, we committed to an effective and ongoing monitoring regime to track Royal Mail's performance in respect of progress of efficiency, quality of service and affordability of universal postal services. In addition, we also committed to give further consideration to the affordability of universal postal services and whether future changes to prices of universal postal services continue to be affordable.
- 2.9 In the light of our commitment and our legal duties, we have considered further:
- approaches to assessing the affordability of universal postal service;
 - our findings, following work to better understand consumers' use of and needs for post; and
 - how we intend to monitor affordability of universal postal services.
- 2.10 We have drawn on a variety of inputs and information sources to assist us with our review including commissioning research, holding meetings with consumer and industry stakeholders, consulting with social policy experts¹⁷ and considering the approaches of postal regulators in other EU Member States.
- 2.11 It is important to note that the current universal postal service obligation requires Royal Mail to provide a range of services at affordable prices including:
- standard and priority services (e.g. First and Second Class stamps for Letters);
 - registered and insured services (which Royal Mail provides through its Special Delivery service); and
 - international services.
- 2.12 However, usage of, and spend on, the different services is diverse. For example both residential consumers and many small and medium businesses use a small sub-set of Royal Mail universal postal service products. In particular, First and Second Class standard Letters, Large Letters and packets up to 2kg comprise the bulk of mail by volume and value for these users. However the precise mix of these products may vary greatly with some consumers and businesses using First Class almost exclusively while others prefer Second Class. Use of international services will also vary considerably, depending on preferences and circumstances in the case of a consumer and the scope and nature of trade in the case of a business.
- 2.13 Our approach in setting our scope of analysis has been to consider:
- residential postal send and spend patterns in particular to identify if and which consumers might be vulnerable to price increases in general terms; and

¹⁶ See footnotes 2, 3 and 4.

¹⁷ We commissioned Professor David Gordon at the Centre for the Study of Poverty and Social Justice (Bristol University) and Professor Glen Bramley from Heriot-Watt University to provide advice on our approach to the consumer research undertaken by Ipsos-MORI.

- small and medium business send and spend patterns to identify if and how affordability concerns may arise.¹⁸
- 2.14 Postal services offered by companies other than Royal Mail do not fall within the scope of the universal postal service obligations and the associated affordability provisions. Accordingly we have not explored issues relating to the prices of sending post via companies other than Royal Mail as part of this report.
- 2.15 We have not taken into account effects of postal prices on consumers receiving post, e.g. where goods are bought online or through a catalogue for delivery to homes. These are outside the scope of our affordability review for the following reasons:
- most delivery options are subject to competitive provision and provided by a variety of postal operators and not necessarily using universal postal services;
 - postage is generally negotiated between the postal operator and the sender, not the purchaser of the good; and
 - postage costs for the delivery of the good are difficult to identify because postage and packaging are often presented as a single price to the purchaser of the good.

Price changes: April 2013

- 2.16 Royal Mail announced in March 2013¹⁹ prices to apply from 2 April 2013. Regarding the following universal postal service products:
- prices for First and Second Class stamps for standard and Large Letters will remain unchanged;
 - prices for 'Royal Mail Signed For' services, will increase from 95p to £1.10;
 - prices of 'Royal Mail Special Delivery Guaranteed' will increase slightly, with the increase dependent on size and weight; and
 - prices for sending Letters using Franking services will increase, for example by just under 7% for standard Letters, First and Second Class (i.e. 44p to 47p and 31p to 33p respectively).
- 2.17 Regarding universal postal service parcels, Royal Mail intends to modify its parcel formats by moving from pricing based solely on weight to pricing based on size and weight. This is because Royal Mail has calculated that the cost of delivery is driven more by the size of a parcel than its weight. For example, while small parcels can be delivered by post men and women on their standard delivery round, bulkier parcels have to be delivered by van, which is more expensive.
- 2.18 Accordingly, from April 2013, Royal Mail will offer two new parcel formats, 'Small Parcel' and 'Medium Parcel'.²⁰ In addition Royal Mail has made an exception to allow

¹⁸ In cases where information and indicators apply to postal spend in general, we have assumed a broad correspondence between residential or business spend and the set of universal postal service products required to be affordable.

¹⁹ http://www.royalmail.com/prices-2013?intcampaignid=Promo_H_tariff_Mar13

²⁰ 'Small parcel' no bigger than: 45cm length x 35cm width x 8cm depth, no heavier than 2kg

small cubes²¹ to be sent as a 'Small Parcel'. The introduction of small cubes addresses concerns raised by the Federation of Small Businesses, that the depth for the 'Small Parcel' format would be restrictive, particularly for customers sending relatively small items where the depth dimension is greater than 80mm.

- 2.19 Prices for 'Small Parcels' up to 1kg will be £3.00 (First Class) and £2.60 (Second Class), and up to 2kg, £6.85 (First Class) and £5.60 (Second Class). These changes mean for example that the price of sending a parcel weighing up to 750g, which fits the 'Small Parcel' dimensions, will rise from £2.70 to £3.00 (First Class) and £2.20 to £2.60 (Second Class). The price of sending a parcel weighing just under 2kg, but still fitting the 'Small Parcel' dimension, will fall from £8.30 to £6.85 for First Class but will increase from £5.30 to £5.60 for Second Class. Assuming parcels meet 'Small Parcel' dimensions and are sent Second Class, prices will change as follows:

Formats and prices applying prior to 2 April 2013		Equivalent 'Small Parcel' formats and prices to apply from 2 April 2013		Price change %
Format	Price	Format	Price	
Packet Second Class 0-750g	£2.20	'Small Parcel' Second Class up to 1kg	£2.60	+18.2%
Packet Second Class 751g-1kg	£3.50	'Small Parcel' Second Class up to 1kg	£2.60	-25.7%
Standard parcel Up to 2kg	£5.30	'Small Parcel' Second Class up to 2kg	£5.60	+5.6%

- 2.20 Prices of 'Medium Parcels' will be £2.05 to £2.65 above those for 'Small Parcels', for weights up to 2kg (First Class and Second Class). This means that the price of sending an item that is relatively bulky but light will see a correspondingly larger increase following Royal Mail's April 2013 price changes. For example, a parcel weighing just under 2kg, with dimensions just under 61cm length x 46cm width x 46cm depth, would currently be classed as a 'Standard Parcel' and cost £5.30. From April 2013, such a parcel will be classed as a 'Medium Parcel' and cost £8.00 (Second Class), implying a price increase of 51%.
- 2.21 Royal Mail has indicated that just over 70% of current parcel volumes will fit the 'Small Parcel' weight and size requirements and that this proportion may become higher to the extent that consumers choose to pack their items to meet the 'Small Parcel' dimensions.²² On this basis, consumers will see a maximum price increase of 18% when sending parcels Second Class.
- 2.22 In addition, to support smaller businesses, Royal Mail is reducing the minimum volume threshold enabling them to qualify for contract parcels prices from 5,000 items a year to 1,000 items a year. Contract parcels prices are significantly discounted on stamped prices.²³ Business customers who do not qualify for contract prices but use franking machines also benefit from discounts of up to 18% on stamp prices for parcels.
- 2.23 Our assessment of the affordability of universal postal services has used data and evidence that relates to the period prior to Royal Mail's price announcement. However we have taken into account the likely effects of prices to apply from April 2013 in the light of evidence we have collected and in forming our overall

'Medium parcel' no bigger than 61cm length x 46cm width x 46cm depth, no heavier than 20kg
For more details see: <http://www.royalmail.com/parcels-made-easy>

²¹ 16cm cubed, weighing no more than 2kg.

²² <http://www.royalmailgroup.com/regulation/consultations>

²³ To qualify for contract mail and parcel prices, a customer must spend a minimum of £5k a year on postage. This can be made up of postage spend on a combination of letter and parcel products.

conclusions. The reasoning concerning prices to apply from 2013 and affordability for residential consumers and businesses respectively is set out in sections 4 and 5.

Structure of the rest of the document

2.24 The rest of this document is structured as follows:

- Section 3 sets out our approach to assessing the affordability of universal postal service prices for residential consumers and small and medium businesses.
- Section 4 summarises our findings in relation to the affordability of universal postal service prices for residential consumers.
- Section 5 summarises our findings in relation to the affordability of universal postal service prices for small and medium businesses.
- Section 6 sets out our overall conclusions and how we will monitor the affordability of universal postal services.
- Annex 1 provides more detail on the approaches to affordability.
- Annex 2 provides more detail on the residential consumer findings.
- Annex 3 provides more detail on the business consumer findings.
- Annex 4 provides a detailed summary of the findings on consumer research undertaken by Ipsos-MORI. The full Ipsos-MORI report is published separately to this document.

Section 3

Our approach to assessing affordability

- 3.1 This section sets out our approach to assessing whether universal postal services are affordable for residential consumers and businesses. This approach is designed to take account of the way in which these consumers use universal postal services. In developing our approach we have taken into account the way in which Postcomm and Ofcom have previously assessed the affordability of universal postal services as well as stakeholder views. We have also considered the approaches to assessing affordability in other sectors, as well as the way in which regulatory authorities in EU member states have assessed whether universal postal services are affordable.
- 3.2 The section is structured as follows:
- approaches used previously by Postcomm²⁴ and Ofcom;
 - stakeholder views;
 - our approach to assessing the affordability of universal postal services for residential consumers; and
 - our approach to assessing the affordability of universal postal services for small and medium business consumers.
- 3.3 Annex 1 sets out a brief review of approaches that have been used by researchers and in academic literature to assess affordability, and a summary of approaches taken by regulators responsible for post regulation in the various EU member states. We took all of these different approaches into account in developing our approaches to assessing affordability of universal postal services.

Approaches used previously by Postcomm and Ofcom

- 3.4 In February 2011, Postcomm issued a discussion paper on the affordability of universal postal services.²⁵ As part of its analysis, it considered approaches that had been used in the water and energy sectors. Postcomm proposed defining affordability for residential consumers on the following basis:
- “A universal postal service product, for example, a First Class stamp, would be ‘unaffordable’ if a potential residential customer was entirely excluded from purchasing it or faced significant hardship from purchasing it because of the price.”
- 3.5 Postcomm focussed on First and Second Class stamps for Letters and concluded that prices were affordable for residential consumers at that time and for the foreseeable future. This view was based on the following observations:
- postal spend accounted for less than 0.15% of average household expenditure and less than 0.25% of low income household expenditure (2009 data);

²⁴ Prior to their transfer to Ofcom in 2011, responsibilities for regulation of Royal Mail and postal services rested with Postcomm.

²⁵ See *The building blocks for a sustainable postal service Universal service - Discussion paper on affordability* February 2011 <http://stakeholders.ofcom.org.uk/binaries/post/1809.pdf>

- Postcomms's 2010 Customer Interest Forums had found no evidence that affordability was an issue. Affordability was generally understood to mean '*having enough money to make a purchase without getting into too much difficulty*'.
- 3.6 Ofcom, in our consultation on 'Securing the Universal Postal Service' ('the October 2011 consultation')²⁶ and the March 2012 statement,²⁷ took a similar approach. We noted that average weekly household spend on post is low, for example, less than one twentieth of that on other utilities such as telephone services, electricity and gas. We also noted that, since spend on post accounted for around 0.1% of income for each decile of household income, post could be considered to be affordable for most residential consumers.
- 3.7 Regarding business consumers, Postcomm noted that businesses and business models vary extensively in their use and reliance on post and so it did not reach any conclusion on the appropriate test of post affordability for business consumers. In our October 2011 consultation, we put forward the working hypothesis that if prices were affordable for consumers they would also be affordable for small businesses.
- 3.8 However, in recognition that some stakeholders disagreed with that hypothesis, our March 2012 statement reviewed evidence of businesses' use of and spend on mail. We noted for example that small businesses tend to spend relatively little on post and that, to the extent that a smaller business is more reliant on post, alternatives and cheaper substitutes were available. We also noted that respondents to the consultation had not suggested that current prices were unaffordable. We concluded that we did not consider that the proposed prices for Second Class stamps (of 45p to 55p) were likely to be unaffordable for small business users.

Stakeholder views

- 3.9 The Business, Innovation and Skills ('BIS') Select Committee in February 2012 looked at Ofcom's proposed approach to regulating Royal Mail's postal services. Its report²⁸ raised concerns over the effect that price increases could have on vulnerable consumers and small and medium businesses. The report recommended that the consequences of price increases should remain a priority for Ofcom and that Ofcom should explore whether vulnerable consumers have extra money to spend on stamps at periods of peak spending (such as at Christmas). It also recommended that Ofcom reconsider its approach to assessing affordability for small and medium businesses (as set out in Ofcom's October 2011 consultation), in recognition of the fact that they have diverse needs and operate on tight margins.
- 3.10 Consumer Focus commented that Postcomm's February 2011 paper lacked detail and depth, particularly for business consumers, and that it did not assess the affordability of registered and insured products. It suggested that the regulator should consider the affordability of international mail. It also suggested that:
- a wider definition of affordability might be more useful, such as relating affordability to the cost of a reasonable level of regular services usage such as a year; and

²⁶ Ofcom consultation *Securing the Universal Postal Service* October 2011 available at: <http://stakeholders.ofcom.org.uk/binaries/consultations/securing-the-postal-service/summary/condoc.pdf>

²⁷ See footnote 1.

²⁸ Business Innovation and Skills Committee: *Stamp Prices: Fifteenth Report of Session 2010 – 2012* 1 March 2012 available at: <http://www.parliament.uk/business/committees/committees-a-z/commons-select/business-innovation-and-skills/Publications/previous-sessions/Session-2010-12/>

- it was necessary to have regard to potentially vulnerable consumers, such as those in rural locations, on low incomes, older consumers, and those without access to the internet.

3.11 The Communications Workers' Union expressed concerns to the BIS Select Committee about the effect of stamp prices on vulnerable consumers. It criticised Ofcom's analysis of affordability based on post spend as a proportion of income, by noting that "*A tenfold increase in postage costs would still constitute a very small proportion of average expenditure, but may well make the service unaffordable for many users*". It instead referred to an alternative approach to affordability outlined by the Joseph Rowntree Foundation 'Minimum Income Standard'. This suggested that around £3 per week from a minimum income budget is reasonable to cover postage costs, including the cost of three First Class stamps.

Our approach to assessing the affordability of universal postal services for residential consumers

3.12 Below, we set out our approach to assessing the affordability of universal postal services for residential consumers.

3.13 In developing our approach, we have been guided by views expressed by stakeholders, advice received from our commissioned social policy experts, and a review of relevant approaches to affordability taken by academics and other researchers. Annex 1 sets out this review. Overall we conclude that no one approach can be definitive about whether the price of a good or service may be considered to be affordable or not, since different approaches offer different advantages.

3.14 However we consider that a key guiding principle in assessing the affordability of universal postal services is 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. Universal postal prices may be considered unaffordable for a consumer were the consumer frequently to suffer significant adverse consequences as a result of the cost of sending post (e.g. because this means foregoing spend on other items) or, as a result of not sending post and foregoing the value of the communication.

3.15 This principle:

- reflects insights from methods used in poverty research, as set out in Annex 1;
- builds on the definitions of affordability considered by Postcomm (see section 2) which focused on "*having enough money to make a purchase without getting into too much difficulty*" and whether or not a consumer "*faced significant hardship from purchasing it [a postal product] because of the price*";
- reflects the fact that affordability will vary according to a consumer's individual circumstances and views; and
- addresses stakeholder concerns that some consumer groups may be more vulnerable than others in relation to the affordability of universal postal services.

3.16 An approach based on this principle is independent of the size of consumer expenditure or income. This is particularly relevant for post since average spend on post is small and so income based measures of affordability are not likely to be fully informative here. For example, some low income consumers spend relatively little on

sending post, but this does not necessarily mean that universal postal services are affordable for those consumers, since they may be suffering detriment either as a result of sending those items or not sending more items.

- 3.17 This contrasts to other items or services such as electricity, gas and housing where household expenditure is generally high relative to income. In such cases the more conventional income based approaches to affordability where necessary consumer spend on an item is assessed against consumer income are more meaningful indicators of the direct consequences for consumers of price levels or price increases in these kinds of services.
- 3.18 For these reasons, in assessing the affordability of universal postal services for residential consumers, we have considered a range of evidence, as set out below. In particular, we have gathered detailed evidence on the behaviour and attitudes of different types of consumers, especially those who may be particularly reliant on postal services or have low incomes. In addition we have considered the use of postal services at Christmas, since this is a period in which usage of postal services may be particularly high for some residential consumers. Such evidence helps to inform us whether universal postal service prices create significant detriments, or whether expenditure on post is unduly constrained by income.
- 3.19 The range of evidence we have examined to assess the affordability of universal postal services for residential consumers is as follows:
- data on consumers' postal send and spend patterns, broken down by consumer type and over time;
 - data that compares expenditure on postal services against expenditure on other 'comparator' items and household total expenditure, broken down by consumer type and over time; and
 - qualitative consumer research that we have commissioned to explore whether low income and vulnerable consumers face constraints on their ability to send post and, if so, whether they suffer detriment as a result.
- 3.20 We describe the evidence that we have considered in more detail below. We note here that the available data on consumer use of and spend on postal services from the Office of National Statistics' ('ONS') Living and Food Cost Survey may include expenditure on postal services which are not universal postal service products (e.g. sending parcels with postal operators other than Royal Mail). Furthermore the data from all our sources is not always linked to specific universal postal service products. However, since residential post use in the main relates to universal postal services, we consider that this data is informative for our assessment of the affordability of universal postal services in general terms.
- 3.21 Before describing the evidence we have considered, we first describe the consumer groups we have particularly focused on.

Consumer groups of interest

- 3.22 Consumers vary considerably in their use of, and need to send, post, as well as in their income and other characteristics. Our previous approach took into account some of these variations by comparing spend on post by income decile. However, in this report we have gone further and particularly identified and had regard to a number of consumer groups because:

- some consumer groups may be particularly vulnerable with respect to sending post, either because they have a particularly high need to send universal service post products, and/or because they lack the means to do so;
- if the evidence suggests that vulnerable consumers are in general able to afford universal postal services, we can be more confident that all consumers on average can afford universal postal services; and
- stakeholders suggested that there are vulnerable consumer groups who merit particular attention and research.

3.23 We have particularly focused on the following consumer groups:

- those with low income;
- those living in rural areas (as they may have a higher reliance on post); and
- other consumers who may be particularly reliant on postal services. For example, those who are aged over 65, or who have a disability, or who have no or limited access to the internet,²⁹ or recent immigrants to the UK.

3.24 There is some significant overlap between some of these groups. For example our Review of User Needs research 2012³⁰ consumer research suggests that 30% of those aged over 75 and 23% of those aged between 65 and 75 have annual income below £11.5k, compared to 18% of the overall population. For this reason we have also looked at the lower income portion of households containing someone aged over 65.

3.25 We note that our focus on these groups also aligns with our obligations under the Communications Act 2003 to have regard to certain consumer groups in performing our statutory duties.

Send and spend indicators

3.26 We have examined data on consumers' use of, and spend on, postal services, using consumer research undertaken by Ofcom; principally the Review of User Needs research and our residential tracker surveys from quarter 3 and 4 of 2012.³¹

3.27 This data enables us to assess which services are used most frequently, and to understand the relative importance of services for different consumer groups. Some data is also available on use of post at the Christmas peak demand period and for which consumer groups this is most important.

Comparator spend and income data

3.28 We have examined data on consumer expenditure on postal services and other household expenditure over time that is collected in the ONS' Living Costs and Food Survey. We use this data to examine the relative importance of postal spend for different consumer groups, and also to analyse how consumer expenditure on postal

²⁹ In this report, references to 'no internet' mean that consumers have no broadband access at home.

³⁰ See Annex 2 for a fuller description and the report *Postal User Needs Quantitative Research*, October 2012 is available at:

<http://stakeholders.ofcom.org.uk/binaries/research/post/quantitative-oct2012/report.pdf>

³¹ <http://stakeholders.ofcom.org.uk/market-data-research/statistics/>

services changes over time relative to expenditure on other items, and also to change in total expenditure.

Consumer research

- 3.29 As noted above, we commissioned qualitative consumer research designed to focus specifically on the behaviour and attitudes of low income and other vulnerable consumers to inform our assessment of whether universal postal services are affordable for these groups. Our objectives for this research included:
- to explore how and why low income and vulnerable consumers send post;
 - to explore what the potential consequences or detriments are (if any) of sending fewer items of post because of its price and/or doing without other goods/services in order to send post; and
 - to understand how usage may vary across the year, particularly at Christmas.

Our approach to assessing the affordability of universal postal services for small and medium businesses

- 3.30 We consider that the concept of post affordability for businesses should reflect the fact that postal services are used as an input by a wide range of businesses. As a consequence, the price of universal postal services may affect the cost and, potentially, the commercial position, of businesses.
- 3.31 In view of this we consider that universal postal services may be ‘unaffordable’ for a business if the prices of these services jeopardised the commercial viability of the business on an ongoing basis in ways that the business is unable to avoid.
- 3.32 With this in mind, our approach considers the extent to which the prices of universal postal service products might materially harm a business’ commercial position. This would depend on three conditions, namely that:
- universal postal services are a critical input to the business’ commercial proposition (e.g. without access to a postal service, the business’ ability to operate commercially would be significantly compromised);
 - there is a lack of good alternatives to universal postal services available to the business (e.g. where a business has no or limited scope to make use of cheaper postal services or alternative forms of communication);
 - the cost of universal postal services is important for the business’ financial position (e.g. universal postal service costs are a significant proportion of the business’ total operating expenditure and the business is operating on thin margins coupled with a limited ability to pass through universal postal service price increases to its customers).
- 3.33 Potential concerns about the affordability of universal postal services would only be expected to arise where a business meets all three of these conditions.

Section 4

Residential consumers

4.1 This section sets out our assessment of whether universal postal services are affordable for residential consumers. As described in section 3, we have examined a range of relevant evidence to form our assessment, and have focused in particular on those consumer groups that we consider are most likely to experience difficulties in relation to the affordability of universal postal services.

4.2 This section is set out as follows:

- prices of universal postal services since 2000;
- consumers' use of and spend on universal postal services;
- comparator household spend;
- Ipsos-MORI research and findings;
- use of universal postal services at Christmas;
- prices to apply from April 2013; and
- our conclusions.

Supporting evidence and information is set out in Annex 2.

Prices of universal postal services since 2000

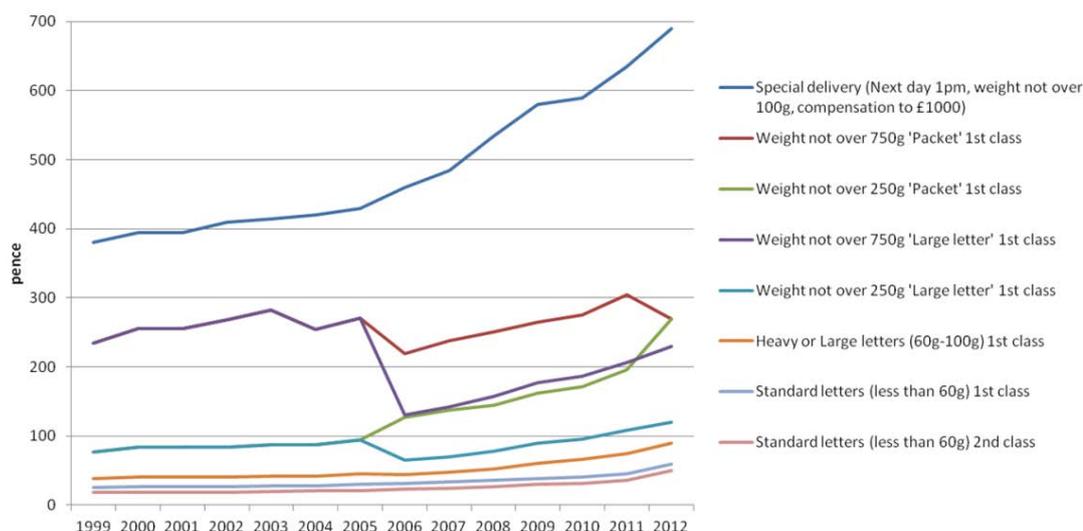
4.3 An assessment of prices is clearly fundamental to any assessment of affordability. We briefly review here how prices of illustrative Royal Mail universal postal service products have developed since 2000 (the year Postcomm was established and the mail market began to be liberalised) and the illustrative impacts of these price rises on different consumer groups. Annex 2 provides a more detailed description of price changes over this period.

4.4 Figure 1 below shows the evolution of the nominal prices of a range of universal postal services (including standard Letters, Large Letters, a selection of maximum weight packets sent by First and Second Class) since 2000. The figure highlights the significant increase in stamp prices that occurred in April 2012, in particular for First and Second Class stamps:

	Old 2012 prices	New 2012 prices	% Change
First Class stamp	46p	60p	+30%
Second Class stamp	36p	50p	+39%

4.5 Figure 1 also shows that Royal Mail has increased the prices of parcels weighing up to 750g relatively quickly since 2006, to bring them into line with the price for medium weight items (i.e. 750g).

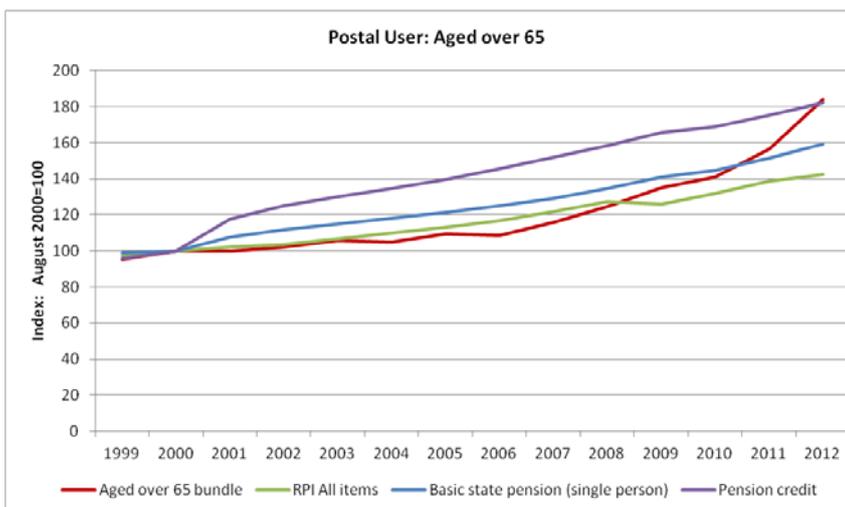
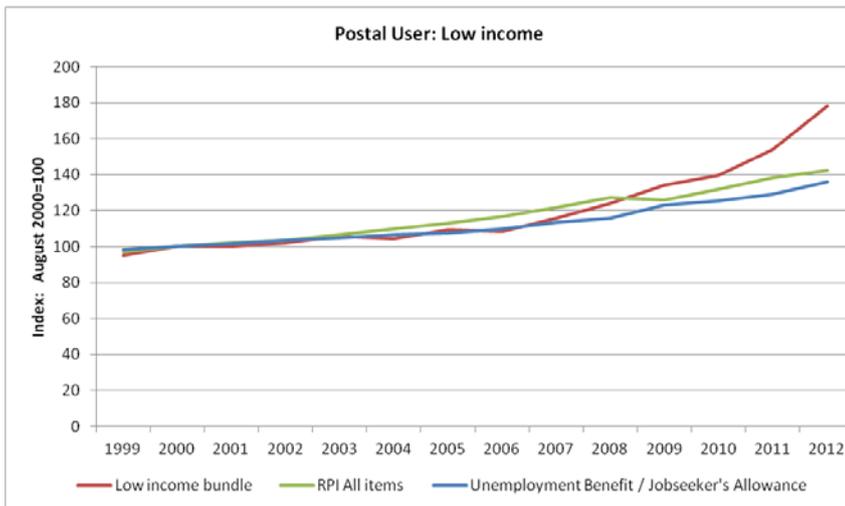
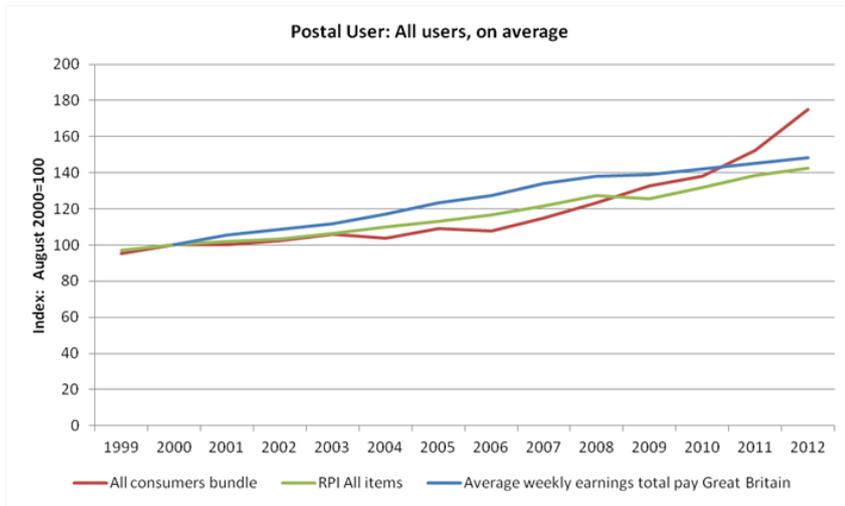
Figure 1: Prices of universal postal services



- 4.6 To examine the potential impact of price changes on different consumer groups, we have focused on the following three broad consumer groups:
- all consumers;
 - low income consumers,³² and
 - consumers aged over 65.
- 4.7 Figure 2 below demonstrates how the total annual cost of a 'representative bundle' of universal postal service products for each of these groups has changed since 1999. The representative bundle of universal postal services for each group reflects the average pattern of consumption for the group, and includes standard Letters, Large Letters and packets. Figure 2 also shows how possible income measures for the different groups have changed since 1999.
- 4.8 Recent price increases have clearly increased the total annual cost of universal postal services consumed by each of these groups, particularly in comparison to the relatively slow growth in income across all consumers and for low income consumers. The price rises in April 2012 had a particularly noticeable effect.
- 4.9 Figure 2 also illustrates that changes in the prices of universal postal services may affect consumer groups differently, in part because of the different way in which these groups use postal services. In particular, this analysis suggests that price increases may have impacted those aged over 65 less than users on average or low income, given the variations in relative income growth and the mix of postal products typically purchased.
- 4.10 We note that this analysis must be interpreted with care, and it is clearly the case that there may be significant variation in both the postal needs and the income of consumers within each of the three broad groups we have considered. In the remainder of the section we discuss more detailed evidence that explores the impacts of postal use for different consumer groups.

³² 'low income' was defined as a consumer with annual income below £11.5k.

Figure 2: Illustrative effect of price changes



Consumers' use of and expenditure on universal postal services

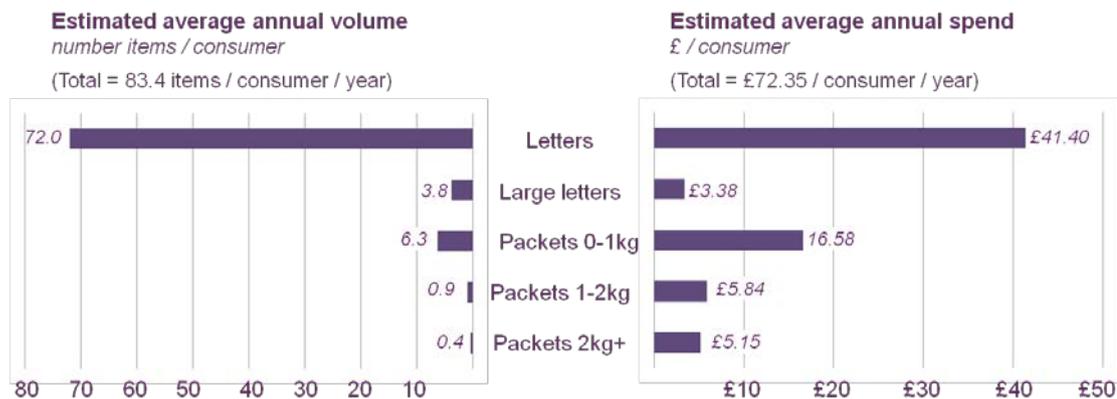
- 4.11 In this section we discuss the way in which residential consumers currently use postal services. In this regard, we have considered both the number of items that are sent, and the annual expenditure on universal postal services. We have also assessed the extent to which usage differs between different consumer groups and in particular consumers who may be considered to be vulnerable.
- 4.12 Information on residential consumers' postal usage is provided principally through our Review of User Needs research, our tracker survey and from the ONS' Living Costs and Food Survey. We have also had regard to our omnibus consumer research study from December 2011.³³ Annex 2 provides more detail on these sources as well as a description of the main findings and detailed tables of results.
- 4.13 In summary, our tracker survey suggests that on average each residential consumer sends around seven items of post per month,³⁴ with around 85% of these being letters and cards. Around 20% of consumers say they sent no post in the last month. ONS data suggests that spend on post is around 54p per week per household (2012 prices) across all households, which is around 0.1% of total consumption expenditure. Ofcom tracker survey suggests average spend on post per person is about £1.70 per week.³⁵
- 4.14 Figure 3 below shows estimates for the average composition of items sent annually per consumer, in terms of standard Letters, Large Letters and parcels (by weight) sent. We have derived these estimates by combining tracker survey data with Royal Mail data on volumes sent. We have also estimated annual consumer expenditure on each type of item, using prices applying from April 2012. The figure shows that, although about 90% of items sent are Letters or Large Letters, in expenditure terms these account for only around 60% of total postal spend (i.e. £44.38 against £72.35). The remainder is on higher unit cost items sent much less frequently such as parcels.
- 4.15 The research also shows that residential consumers make some use of other universal postal services which are sent infrequently. Our Review of User Needs research for example found that 40% of consumers said they had used 'recorded delivery' in the last year, and 31% had used 'Special Delivery'. Nevertheless frequency of use of these services within the year tends to be low compared with other universal postal services such as standard Letters and parcels. The research undertaken by Ipsos-MORI suggests that consumers have low awareness and low usage of products such as 'Recorded Delivery' and 'Special Delivery'.

³³ <http://stakeholders.ofcom.org.uk/binaries/research/post/post-omnibus-data-tables.pdf> and <http://stakeholders.ofcom.org.uk/binaries/research/post/post-omnibus-methodology.pdf>

³⁴ Based on the question "Approximately how many items of post – including letters, cards and parcels – have you personally sent in the last month?"

³⁵ Measured between July and December, so annual average may be biased upwards by higher spend in December. Differences in estimated spend on post may reflect the different methodologies used by the ONS Living Costs and Food Survey and the Ofcom consumer research. The Ofcom research for example is focused purely on post spend and so may elicit higher estimates of spend from participants compared to the ONS research where post is one item among all items of household spend that participants are asked to record.

Figure 3 – Estimated usage of and expenditure on postal products 2012³⁶



Source: Ofcom consumer market research ('tracker') Q3 2012 and Q4 2012, combined with Royal Mail data.

4.16 There are significant differences in usage of, and expenditure on, postal services by consumer group. ONS data and our consumer research³⁷ consistently show that:

- younger (particularly aged under 24), low income,³⁸ those in socio-economic group DE, and those without access to the internet send fewer items and spend less than average. They are more likely to send no post, and use Signed For (sometimes referred to as 'recorded') and Special Delivery services less frequently;
- older (those aged over 65) and/or higher income³⁹ consumers tend to send more items of post and spend more in total than average. For higher income consumers,⁴⁰ spend as a share of their total consumption expenditure at around 0.1% differs little from other consumers. However, for pensioner households postal spend accounts for a higher share of budget (0.2% to 0.25%);
- the evidence is mixed for rural consumers, with our Review of User Needs research suggesting they tend to send more items than average, but our tracker survey data suggesting they send fewer. Both pieces of our research suggest that rural consumers are more likely to make use of Signed For and Special Delivery services. Our tracker survey data suggests that their average total spend on postage is smaller than average; and
- our Review of User Needs research suggests that those with a disability sent more post compared to that of the population as a whole, although ONS data suggests that households containing someone receiving disability benefits spend about the same on post as all households.

4.17 Findings for consumers with no internet access are very similar to findings for low income consumers. That is, both groups send less post than average and make less use of universal postal services.

³⁶ Based on six months data which asked 'what did you send in the last month'. This includes December spend.

³⁷ Our Review of User Needs research and Q3 and Q4 2012 tracker survey.

³⁸ From Review of User Needs research, consumers with annual income less than £17.5k tend to send fewer items of post than average.

³⁹ From Review of User Needs research, consumers with annual income greater than £30k tend to send more items of post than average.

⁴⁰ From ONS data, those consumers in the top quintile of income.

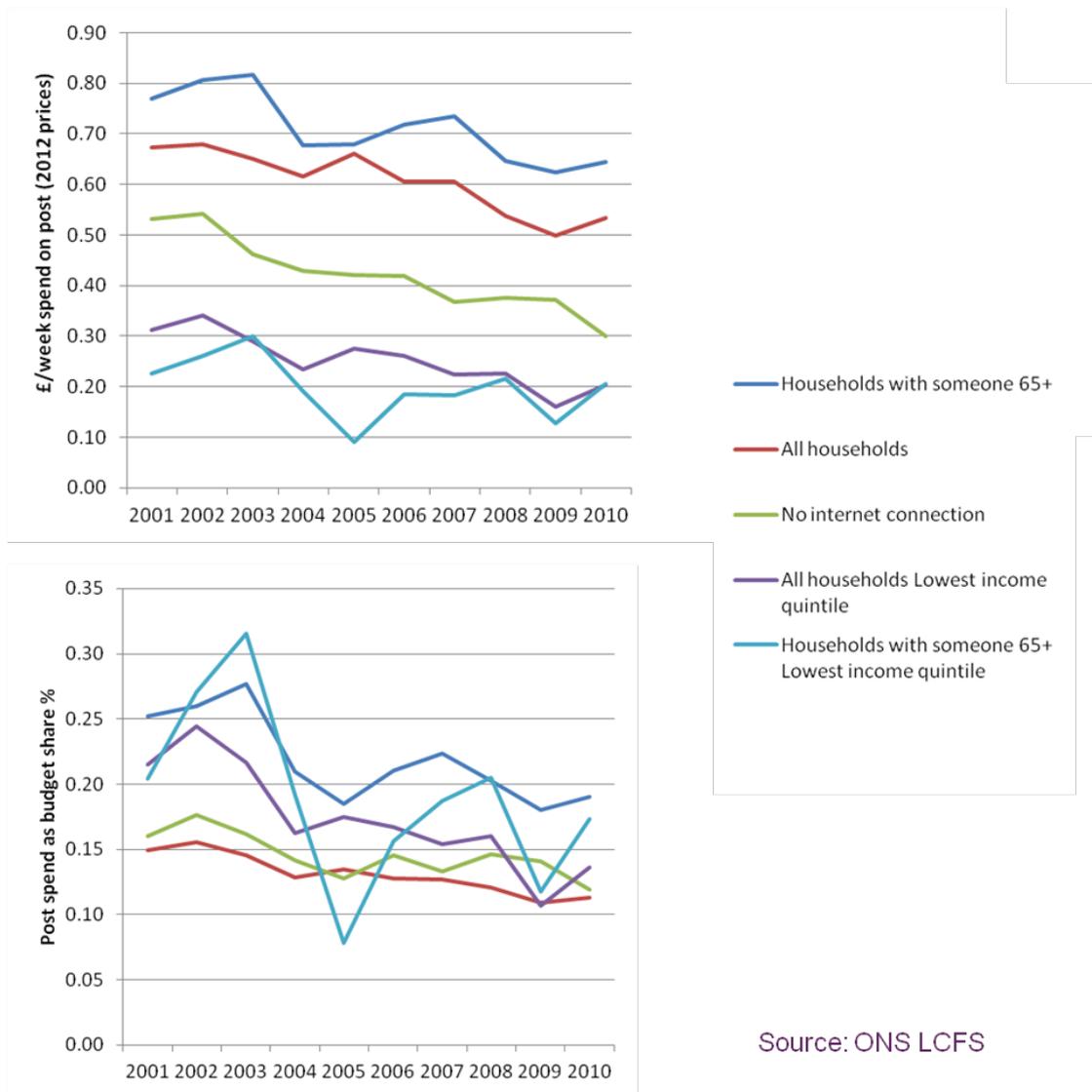
4.18 Using ONS data, we have estimated household expenditure on post and what proportion of total household expenditure it accounts for ('budget share') for five illustrative consumer groups. These groups are:

- all households;
- low income households, i.e. those in the lowest fifth ('quintile') of income;
- households with someone aged 65 or over;
- lowest income fifth of households with someone aged 65 or over; and
- households with no internet connection.

4.19 Our estimates show that:

- average household weekly spend on post in 2010 was about 53p per week (in 2012 prices), and formed a budget share of about 0.11%. This compares to spend on all communications services of about £13; and
- average weekly postal spend has in general fallen both in absolute terms and as a share of budget for the five groups. For example, for all households spend on post fell 20% from 68p (rebased to 2012 prices) in 2001 to 54p in 2010. As a share of budget, postal spend fell from 0.15% to 0.11%. Figure 4 charts the changes for the five groups.

Figure 4: Spend on post over time, level and budget share



Comparator household spend

4.20 We also consider that it is instructive to compare changes in expenditure on postal services against changes in expenditure on other products and services as well as total expenditure, at the household level.⁴¹ For example, if a consumer's expenditure on post remains stable or falls while the consumer's total expenditure rises, this is indicative (other things equal) that expenditure on post was not initially constrained by insufficient income. This might also be the case in respect of expenditure during December (i.e. in respect of Christmas). We might also infer that expenditure on post was not unduly constrained if expenditure on post falls while expenditure on non-discretionary items (i.e. items not considered essential) increases.

⁴¹ This section examines expenditure at the household level using ONS data on actual household spend. This contrasts to figure 3, where we estimated expenditure on postal services using current prices and an assumption about levels of usage of post.

4.21 Household spend data from the ONS' Living Costs and Food Survey gives estimates of weekly household expenditure on post and other items and total expenditure over time. Table 1 shows the changes in weekly expenditure between 2001-03 and 2008-10 for each of these expenditure categories, broken down by:

- all households;
- all households, lowest income quintile;
- households with someone aged over 65; and
- households with someone aged over 65, lowest income quintile.

4.22 Annex 2 sets out in more detail the ONS data we have compiled both for the period 2001-03 to 2008-10 and in respect of spend in December.

Table 1: Real terms changes in weekly expenditure on post against changes in total expenditure and expenditure on other items

Change in spend between 2001-03 and 2008-10, £/week (2012 prices)	All households	All households, lowest income quintile	Households containing someone aged over 65	Households containing someone aged over 65, lowest income quintile
Post	-0.14	-0.12	-0.17	-0.08
Total expenditure	-37.59	+1.67*	+14.40	+12.23
Mobile telephone	+1.50	+0.57	+0.52	+0.09
Satellite TV subscriptions	+0.60	+0.36	+0.70	+0.48

Source: ONS Living Costs and Food Survey data

*Change not statistically significant at the 5% level (t-test)

4.23 Broadly speaking, and on the basis of these changes alone, there is little to suggest that expenditure on post was or is constrained for these consumer groups. For the two low income groups, spend on post fell while total household expenditure rose or remained broadly constant. For all four groups, reductions in spend on post over the period were exceeded by increases in spend on mobile telephones and spend on satellite TV subscriptions. Given that households in all four groups appeared on the basis of these figures to have allocated increased total expenditure or expenditure to items other than post, it would appear that expenditure on post was not initially constrained, nor has it become so.

Ipsos-MORI research and findings

4.24 We commissioned consumer research to examine the behaviour and attitudes of low income⁴² and vulnerable consumers in relation to their use of universal postal services. Ipsos-MORI undertook this research during the autumn of 2012. Annex 4

⁴² All participants in our qualitative consumer research were on low incomes ('low income' was defined as 70% of the median household before housing costs income adjusted for size of household using the OECD equivalisation scale. Participants were also asked to identify with a series of adult deprivation statements), except disabled consumers who were on a mix of low, medium and high incomes

summarises its approach and findings. We have published Ipsos-MORI’s full report⁴³ alongside this report.

4.25 Ipsos-MORI noted that participants see some post items as ‘essential’ and others as ‘non-essential’. In line with our approach set out in section 3, i.e. that we use consumer research to explore the potential consequences or detriments of sending or not sending post, this means that concerns about the affordability of universal postal services may arise where either:

- the consumer did send item(s) of post he or she considered to be essential, at prevailing post prices, but suffered significant detriment as a consequence (e.g. giving other things up in favour of sending the post); or
- the consumer did not send item(s) of post he or she considered to be essential, because of prevailing post prices, and suffered significant detriment as a consequence of not sending the post (e.g. not maintaining contact with family or friends);

Conversely, concerns about affordability are less likely to arise where essential post was sent but no significant detriment arose as a result of foregoing other spend, or where the consumer chose not to send post but there were no significant consequences of this for the consumer.

4.26 Table 2 below illustrates Ipsos-MORI’s findings in these terms. Overall Ipsos-MORI found that the reported experiences suggested that only consumers in quite limited circumstances would be at risk from not being able to afford universal postal services. These circumstances are where a consumer suffers both significant financial difficulty or very low income and has a frequent need to send post items they consider to be essential.

Table 2: Ipsos-MORI findings in context of affordability

	<u>Affordability unlikely to be an issue</u> Illustrations of circumstances or views where consequences and detriment tend to be less significant	<u>Affordability a possible issue</u> Illustrations of circumstances or views where consequences and detriment tend to be more significant
Low income and vulnerable consumers <u>did</u> send post they considered ‘essential’ post, at prevailing prices	<ul style="list-style-type: none"> • A general view prevailed that prices and so cost of sending post were simply too low to be of consequence, e.g. prices and costs often not consciously considered • Frequency of use is low, again meaning overall costs are considered to be low • Where use of First Class is frequent, as it was for many participants, the price premium is not an issue or detriment 	<ul style="list-style-type: none"> • Few direct examples of detriment suffered, or illustrations of the circumstances in which this has arisen • Some indirect examples where participants felt prices and costs were ‘high’. For example one participant said: <i>“It’s a lot of money but I can’t really figure it all out so I don’t think about it too much, just pay up!”</i>
Low income and vulnerable consumers <u>did not</u> send post they considered ‘essential’	<ul style="list-style-type: none"> • Participants noted circumstances where they managed to find alternatives to post; they often saw this as part of a bigger trend to email and other digital communication – and in general they considered these methods to be equally acceptable to sending post, so reported suffering little detriment 	<ul style="list-style-type: none"> • Few direct examples of participants reporting detriment suffered • Where participants did report detriment, this illustrated the circumstances under which such detriment may arise. They

⁴³ <http://stakeholders.ofcom.org.uk/binaries/research/post/post-affordability.pdf>

<p>post, because of prevailing prices</p>	<ul style="list-style-type: none"> • Some concerns for some participants where needs arise to send higher cost items such as Special Delivery or larger parcels but where the participant chose to send fewer or lighter parcels instead. However in these circumstances participants reported little evidence of significant detriment suffered as a result. 	<p>include those in extreme financial difficulty such as those who are unemployed or recent immigrants. For example one participant said:</p> <p><i>“Eight or nine months ago I was broke, I’d just lost my job and I had to send off a few applications and I couldn’t afford the stamp so I walked to the employers.”</i></p>
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- 4.27 Furthermore, when discussing the concept and definition of affordability, both in general terms and more explicitly for post, most participants saw their use of post as too infrequent and the unit cost too low for ‘affordability’ to be a concern for them.
- 4.28 Overall, the Ipsos-MORI research supports the finding that post appears to be generally affordable for low income and vulnerable consumers.

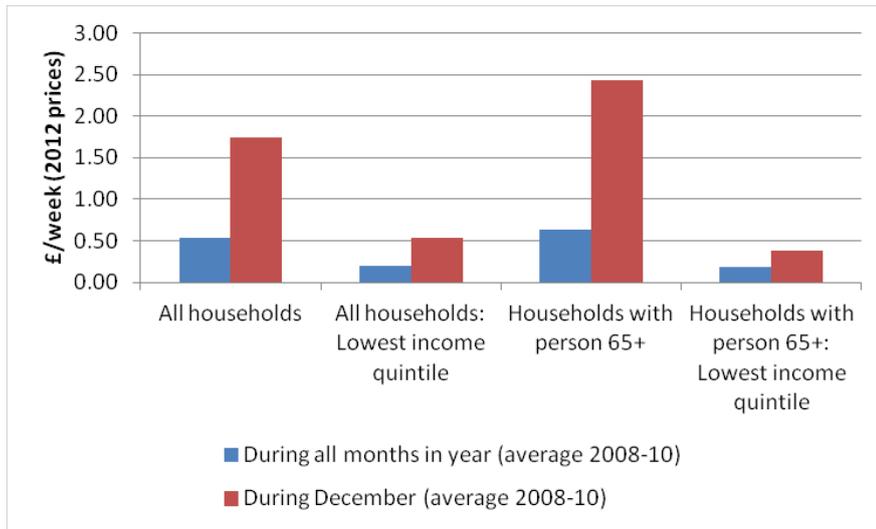
Use of universal postal services at Christmas

- 4.29 Consumer use of postal services is particularly pronounced at Christmas, with consumers typically spending around double or triple the amount on post compared to their average weekly spend on post during the year. The BIS Select Committee identified peak spend on post at Christmas as a time when post affordability might be more likely to be a concern for vulnerable consumers.
- 4.30 For these reasons, we have separately identified consumer send and spend patterns in December, using the evidence set out above. We also describe Royal Mail’s Christmas 2012 discounted stamp offer for vulnerable consumers and the use made of it.

Consumer spend in December

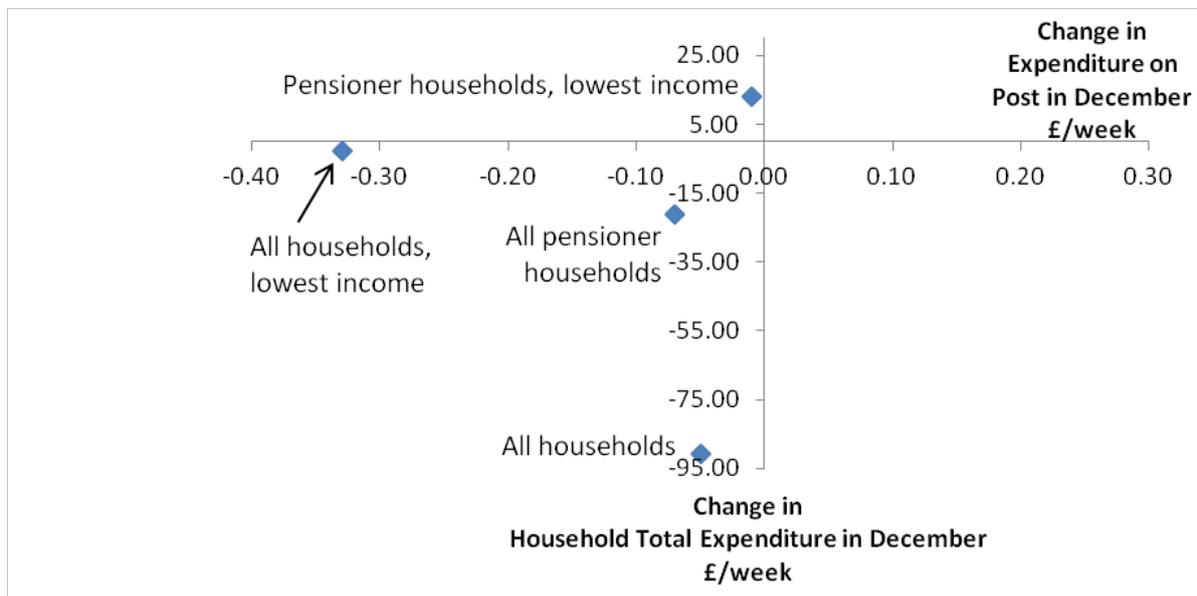
- 4.31 ONS data on postal spend clearly indicates that household spend on post is higher in December, and this is true for most consumer groups, including low income and vulnerable consumers. Figure 5 compares average weekly spend on post in December across 2008 to 2010 against average weekly spend during the year, for four illustrative consumer groups (all households, all households (lowest income quintile), households with someone over 65 and households with someone over 65 (lowest income quintile)). The graph shows that in particular, older households’ weekly spend on post in December is almost four times weekly spend at other times of year.
- 4.32 Expenditure on post in December has, contrary to general trends in expenditure on post, tended to remain static in real terms, or to decline only slowly over time. For all households, for example, weekly spend on post in December fell from £1.80 per week across 2001 to 2003, to £1.75 per week across 2008 to 2010 (all prices expressed in real terms as at 2012 prices), while for the lowest income pensioner households this change was 39p per week to 38p per week.

Figure 5: Weekly spend on post in December, compared to rest of year (2008-10)



- 4.33 Over the same period, weekly total household expenditure in December across all households has declined, and in households containing someone over 65. Households in the lowest quintile of income ('All households, lowest income') have retained roughly stable spend, while spend in the lowest income quintile of households containing a person aged over 65 ('Pensioner households, lowest income') has increased modestly.
- 4.34 Figure 6 illustrates these changes against changes in postal spend in December, between 2001-03 and 2008-10, using the data presented in Annex 2. For households in the lowest quintile of income and lowest income quintile pensioner households, static or reduced expenditure on post at Christmas coupled with static or increased total household expenditure around this time is consistent with the idea that expenditure on post at this time of year was not constrained.

Figure 6: Change 2001-03 to 2008-10 in weekly household expenditure on post and household total expenditure, in December



Ipsos-MORI consumer research

- 4.35 Ipsos-MORI found that sending cards and parcels at Christmas is important for many low income and vulnerable consumers. As a result, these consumers are generally more reliant on post and aware of its cost in the Christmas period.
- 4.36 Ipsos-MORI found that, although some consumers may be frustrated by the cost of sending post, *“it did not have a notable impact on their usage, usually because they were not sending enough at Christmas time for it to be an issue.”* Ipsos-MORI also noted that many consumers adopted a number of strategies to manage or accommodate additional postal costs at Christmas (e.g. switching to using Second Class stamps).
- 4.37 Ipsos-MORI also found that the cost of sending post at Christmas was not equally important to all consumers, and that this depended in part on their willingness to consider alternatives. Younger consumers in particular tended to use other channels to communicate and so send fewer Christmas post items than others. Consumers’ views of the importance of Christmas post were influenced by their views about tradition, their personality and their age.

Royal Mail Christmas 2012 stamp offer

- 4.38 Royal Mail pledged to mitigate the impact of 2012 stamp price increase for customers receiving Pension Credit, Employment and Support Allowance or Incapacity Benefit at Christmas 2012 by giving them the option to buy up to 36 First or Second Class stamps at 2011 prices over a limited period prior to Christmas. In order to buy stamps at the reduced prices, eligible consumers were required to provide proof at the point of purchase that they were in receipt of qualifying benefits.
- 4.39 The offer was announced earlier in the year, was the subject of a leaflet detailing the scheme to every household in the UK in October and was heavily promoted by Royal Mail throughout November and December 2012. The promotion included point of sale information at every Post Office, newspaper adverts and promotion of the scheme to MPs, Age UK and other agencies accessed by potentially eligible customers. In addition Royal Mail’s press and broadcast campaign generated over 200 stories with an audience reach of around 24 million.
- 4.40 Royal Mail reported that the take up of the offer was in line with expectations and believe that the take-up is broadly in line with similar schemes aimed at people on low incomes:
- around 8% of eligible consumers took up the offer
 - participating consumers bought around 32 stamps each on average

Conclusions on use of universal postal services at Christmas

- 4.41 Sending post at Christmas is clearly important for many consumers, including low income and other vulnerable consumers, and average spend patterns for December against the rest of the year demonstrates this. However, the available evidence does not suggest that consumers in general, or low income and vulnerable consumers in particular, have been unduly constrained in the sending of post at Christmas. The 8% take up of Royal Mail’s Christmas 2012 stamp offer in particular is consistent with this evidence.

Prices to apply from April 2013

- 4.42 Section 2 set out that in March 2013, Royal Mail announced the prices to apply to universal postal services from 2 April 2013. Prices of standard and Large Letters, First and Second Class, are to remain unchanged and price changes for packets and parcels will vary depending on the new size and weight formats.
- 4.43 Given that standard and Large Letters account for the majority of postal usage by volume for residential consumers, including low income and vulnerable consumers, these price changes are unlikely to have a significant impact on consumer expenditure on post overall. Any effects will be through the increased prices of packets and parcels, which will, naturally, vary according to individual consumer usage of these products.
- 4.44 We note here that our Ipsos-MORI research found that the price of these products may be a concern for some consumers (low income and vulnerable) but also that since these consumers choose to purchase these items relatively infrequently, they do not in general feel constrained in their use of such products by the price. We consider that the size of Royal Mail's announced price increases for packets, together with Royal Mail's estimate that around 71% of packets are likely to fit the new 'Small Parcel' format, will not alter this finding.

Conclusions

- 4.45 We have considered a range of evidence to inform our assessment of whether universal postal services are affordable for residential consumers. We have particularly focused on consumer groups we consider are more likely to be vulnerable to the price of universal postal services.
- 4.46 Ofcom consumer research⁴⁴ and ONS household spend data suggests that, on average, consumer spend on sending post is small, in a broad range between £0.54 and £1.70 per week, and very small relative to average incomes. In addition, post spend both in absolute terms and relative to incomes continues to decline across many consumer groups.
- 4.47 Ofcom consumer research suggests that the amount of post that residential consumers send is low, on average. However, there is significant variation in post use and expenditure on post. For example:
- older consumers are likely to send more post than average, and perhaps be more reliant on post, particularly at Christmas;
 - younger consumers, low income consumers and those with no access to the internet tend to send less post and spend less on post than average;
 - consumers in rural areas tend to spend less on post than average;
 - consumers who are disabled tend to send higher amounts of post; and
 - for most residential consumers, expenditure on post at Christmas remains significantly higher than at other times of the year.

⁴⁴ See footnotes 30 and 31.

- 4.48 Our analysis of changes in household expenditure on post against changes in household total expenditure and on other items between 2001-03 and 2008-10 suggests that reductions in expenditure on postal services between these periods were exceeded by increases in expenditure on mobile telephone services and satellite TV subscriptions. This pattern was consistent across all of the consumer groups that we considered, including low income and households with someone aged over 65. This evidence suggests that expenditure on post was not initially constrained and nor has it become so.
- 4.49 The Ipsos-MORI research explored how and why low income and other vulnerable consumers send post, whether their use of post was unduly constrained by its price and if and how they may have suffered detriment as a result of any constrained use (including at Christmas). In general, the research found that such consumers were able to send the post they wanted to, without significant detriment, including at Christmas. This was because of the low unit costs of the most frequently used postal services (First and Second Class standard Letters) and a low reliance on post in general, including parcels. Some participants did identify higher cost universal postal services, in particular parcels, as an issue. However, in these cases the research found that these consumers can generally manage these costs as their need to use such higher cost services is infrequent.
- 4.50 The main exception to this general finding was that some consumers in very limited and specific circumstances could be at risk from not being able to afford universal postal services. These circumstances are where a consumer suffers both significant financial difficulty or very low income, and has a frequent need to send post items they consider to be essential.
- 4.51 We consider that prices to apply from April 2013 are unlikely to affect our findings, in particular given that prices remain unchanged for the most widely used standard and Large Letter format services (First and Second Class). We acknowledge that some consumers will see price rises for parcels; however our consumer research findings suggests that consumers do not in general find themselves unduly constrained from purchasing these items, since they are purchased infrequently.
- 4.52 Overall, our findings suggest that universal postal services are affordable for almost all residential consumers, including low income and other vulnerable consumers, at current prices and prices to take effect in April 2013. We note that our research findings indicate that there are some very limited circumstances where a consumer could be at risk from not being able to afford universal postal services. These circumstances are where a consumer suffers both significant financial difficulty or very low income, and has a frequent need to send post items they consider to be essential. This reflects very particular circumstances and severe financial hardship. It is likely that consumers in such circumstances would unfortunately have concerns about the prices of universal postal services, even at much lower prices.

Section 5

Business consumers

- 5.1 Post is an important method of communication for many businesses, whether used for communicating with customers or suppliers, or for delivering goods. There is a range of post products and services available to businesses, with a number of postal operators providing competitive alternatives to Royal Mail for the larger scale or bulk delivery postal services. Nevertheless, many smaller businesses continue to use Royal Mail universal postal services to send most of their Letters and smaller packet items, either because the volumes involved are too small to enable use of competitors to Royal Mail, or because they choose to.
- 5.2 This section sets out our assessment of the extent to which universal postal services may be considered to be affordable for businesses, with a particular focus on small and medium businesses.
- 5.3 This section is structured as follows:
- approach;
 - analysis of evidence;
 - prices to apply from April 2013; and
 - our conclusions.

Approach

- 5.4 As set out in section 3, we consider that the concept of affordability for businesses is different to that for residential consumers. We consider it is appropriate to characterise affordability of universal postal services for a business in terms of the extent to which the cost of universal postal services might materially harm a business' ongoing commercial viability.
- 5.5 We consider that for any one business this would depend on three conditions, namely that:
- universal postal services are a critical input to the business' commercial proposition;
 - there is a lack of good alternatives to universal postal services available to the business; and
 - the cost of universal postal services is important for the business' financial position.
- 5.6 Potential concerns about the affordability of universal postal services would only be expected to arise where a business meets all three of these conditions.
- 5.7 The rest of this section analyses evidence and findings available to us to gauge the extent to which UK businesses might be at risk of finding universal postal service unaffordable.

Analysis of evidence

- 5.8 A number of evidence sources are available to assess affordability issues for businesses on the basis of the approach set out. In particular our Review of User Needs research⁴⁵ provides data on how and why businesses use post. Annex 4 sets out in more detail our evidence sources and relevant findings.

Overview of business postal use

- 5.9 In brief, the data that we have gathered demonstrates that UK businesses comprise mainly small businesses. Of the 4.5 million UK private enterprises, around three quarters or 3.2 million are small sole trader businesses with average annual turnover of about £60k.
- 5.10 Across all UK businesses, our Review of User Needs research found that average (median) spend on post is around £18 per month, with use of, and spend on, post strongly correlated to the size of business. Businesses with up to two employees for example have a median post spend of about £9 per month, as do businesses with an annual turnover of under £50k.
- 5.11 Small businesses are more likely to use Royal Mail postal services, with around 90% of small businesses (i.e. those with up to two employees, or with annual turnover under £50k) spending almost all to around three quarters of their post spend with Royal Mail. When sending post with Royal Mail, small businesses in the main use universal postal service products. For example, when sending post with Royal Mail, 93% of businesses with up to two employees use stamps (a universal postal service), and only 2% use bulk mail products (which are not a universal postal service). On this basis, we estimate that around 90% of small businesses principally use Royal Mail universal postal service products.
- 5.12 The Review of User Needs research gauged business reliance on post by asking whether mail was 'core' to a business. Around 16% of all businesses say that mail is 'core' to their business, falling to around 11% for firms with annual turnover of less than £50k. For those businesses where mail is 'core', mail spend is correspondingly higher, with median spend at £76 per month. Companies for whom mail is 'core' to their business are more likely than other businesses to send parcels/packets (84% of businesses send these at least once a month compared to 44% of all businesses).
- 5.13 Notwithstanding the fact that the majority of small businesses principally use Royal Mail universal postal service products, there appears to be scope for many to substitute either to alternative (and cheaper) universal postal service products, and some willingness and ability to substitute from post to other forms of communications.⁴⁶ For example, the average proportion of mail sent using First Class by the small businesses (those with up to two employees) is about 70%, while just over 20% of these businesses say that, of Letters sent First Class, all or almost all have to arrive the next day. This suggests that a significant proportion of mail sent using First Class could be sent using Second Class. Evidence from our tracker

⁴⁵ <http://stakeholders.ofcom.org.uk/binaries/research/post/quantitative-oct2012/business.pdf>

⁴⁶ We note where value and volume of mail usage are high enough a business could use another postal operator, although a business with mail usage and levels of spend on mail similar to those outlined in Table 3 may not find any financial benefit from moving to another postal operator.

survey for Q4 2012⁴⁷ also suggests an ability and willingness of many businesses to switch Royal Mail products in reaction to price increases.

- 5.14 Alternative and more cost effective universal postal service options include in particular the possibility to use a franked (sometimes called 'metered') postal service. This is available from Royal Mail and currently offers discounts to standard First Class stamps of 16p per item, and 19p per item Second Class. Given the need to purchase or rent franking equipment and other ancillary costs, this can become a cost effective substitute where spend on Letters reaches or exceeds, broadly speaking, around £80 per month or around 120 Letters per month or five or six Letters per working day (assuming an average mix of First and Second Class Letters).

Assessment of possible affordability issues

- 5.15 As explained above, our approach is to identify businesses which are potentially (but not necessarily) at risk of finding universal postal services unaffordable by reference to three conditions (see paragraph 5.5 above). We have estimated the number of businesses that might pass these three conditions by specifying how our business research Review of User Needs research data can be used to apply the conditions. Table 3 sets out the conditions and how the research data can be used.

Table 3: Conditions for identifying businesses potentially at risk

	Explanation of Condition	Test in terms of consumer research data
Condition 1	Universal postal services are a critical input to the business' commercial proposition.	We assume this is the case for a business where it denotes its mail spend as 'core' to the business.
Condition 2	There is a lack of good alternatives to universal postal services available to the business.	We assume this is the case for a business where its mail spend is below £100 per month (£1,200 per year). At this level of expenditure, alternatives such as franking are unlikely to be significantly cheaper.
Condition 3	The cost of universal postal services is important for the business' financial position.	We assume that this is more likely to be the case for a business where its mail spend is high relative to its turnover. Since under condition 2 we assume that mail spend is at a maximum of £1,200 per year, these costs are only likely to be significant for a business with a relatively low annual turnover. We focus on businesses with a turnover of less than £50k per year. This is a conservative approach (i.e. more businesses are likely to meet this test and so be potentially at risk from post affordability issues) because in practice annual post costs of £1,200 are only likely to be a significant issue for businesses with annual turnover substantially less than £50k

⁴⁷ Data due to be published in July 2013.

		(given that £1,200 is only 2.4% of £50k).
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5.16 In selecting these test parameters we have been partly guided by the data available to us. We have no direct indicators available for example of whether an unavoidable increase in postal spend would have a significant negative impact on the financial position of businesses. We consider that our approach is conservative, because for example we assume businesses cannot pass through cost increases and that the £50k annual turnover threshold is in practice reasonably high. Consequently in practice our test parameters are likely to overstate the extent to which the prices of universal postal services might affect the commercial viability of businesses.

5.17 Using our Review of User Needs research, we have estimated the proportion of businesses that might be in these circumstances and so meet these tests. Figure 7 below illustrates this. Research results indicate that the possibility of affordability issues might apply to between 1% to 4% of UK businesses (i.e. around 45,000 to 180,000 UK businesses), with a central estimate of around 2.4%, or 100,000 of UK businesses.

Figure 7: Illustration of maximum extent to which affordability issues might occur



5.18 It is important to stress that this is an estimate of the maximum number of UK businesses that may be at risk from facing problems with the affordability of universal postal services, rather than an estimate of the actual number at risk. There are a number of reasons to believe that, in practice, the number of UK businesses at risk is likely to be considerably smaller than our estimate of the maximum. We summarise our overall views here in the conclusions below.

Additional evidence

5.19 We have also considered a number of other pieces of indirect evidence to assess whether postal services are affordable for businesses. In particular:

- the failure rate of small businesses compared to larger businesses;
- the recent sales performance of businesses that are reliant on internet sales and hence on postal services; and
- a survey by the Forum of Private Business on small businesses' views about important cost pressures.

We consider that this evidence, whilst indirect, does not suggest that the price of universal postal services is having a significant impact on the commercial viability of most small businesses.

Business failure rate

5.20 Analysis of recent UK insolvencies by Cork Gully⁴⁸ suggests that, although the recent recession has increased the number of insolvencies, as might be expected, the 2011 business failure rate for firms with up to two employees was lower than the failure rates for larger sized businesses. For these purposes smaller companies are those with lower annual average turnover (typically £50k to £60k) and consequently those notionally more at risk from price increases to universal postal services. This evidence therefore indicates that businesses notionally more at risk from increases to postal prices appear to have suffered less from the recent economic downturn.

Internet sales

5.21 Cork Gully analysis of recent insolvencies noted that “*internet retail sales values in March 2012 were 15.2% higher than a year ago.*” Royal Mail research found that just over half of small and medium online retailers’ surveyed saw an increase in sales in 2012 and two-thirds are confident that sales will increase this year. These indicators together suggest that those businesses dependent on internet sales, and hence more likely to be susceptible to mail costs, have been successful in increasing sales.

Forum of Private Business

5.22 The Forum of Private Business surveyed its members in August/September 2012⁴⁹ regarding the cost of doing business. Concerning cost pressures facing businesses and those of most concern, it found:

- whilst prices have risen faster for micro, small and medium businesses than for the rest of the UK, small businesses already face high business costs with 95% seeing an overall increase in costs e.g. transport, energy, marketing, VAT; and
- the main cost pressures reported by businesses were transport, raw material, staff, energy and property costs. However, around 4% of businesses surveyed did report that marketing costs due to postage prices were the main cost pressure to their business.

This suggests that the price of post is not the principal cost concern for most businesses.

Prices to apply from April 2013

5.23 In section 2 we set out that Royal Mail has recently announced the prices to apply from 2 April 2013. Section 2 explained that prices of standard and Large Letters, First and Second Class, are to remain unchanged but price changes for parcels will vary depending on the new size and weight formats. We also noted that prices for sending Letters using Franking services will increase by just under 7% for standard Letters, First and Second Class (i.e. 44p to 47p and 31p to 33p respectively).

⁴⁸ Cork Report Analysis of corporate insolvency trends in the United Kingdom over the next four years Cork Gully LLP June 2012, available at:

<http://www.corkgully.com/wp-content/uploads/2012/06/Cork-Report-Analysis-of-Corp-June-2012W.pdf>

⁴⁹ http://www.fpb.org/images/PDFs/research/Referendum_201_report.pdf

- 5.24 These price changes do not significantly change our conclusions. To the extent small businesses use these Royal Mail products, and given that average postal spend by small businesses is small, most small businesses are likely to see only small or modest increase to their postal costs (where usage levels remain stable). We also consider that Royal Mail's price changes are unlikely to alter significantly our estimate of the maximum number of potentially affected businesses. In particular, even with increased prices for franking relative to stamps, franking is likely to continue to be a more cost effective option where a business' spend on post exceeds £100 per month on Letters.
- 5.25 Regarding parcels, we note that Royal Mail's decision to introduce new parcel formats and prices will result in some significant price increases, particularly for items which are relatively light but bulky. We noted in Section 2 one example where the price of a light but bulky parcel will effectively increase by 51%. We have received representations from two business consumers particularly concerned about such increases.
- 5.26 We note in this regard that Royal Mail's new pricing structure for parcels moves to a more cost reflective pricing structure. By far the largest part of the costs of delivering a parcel relates to the 'final mile'. While small parcels can be delivered by postmen and women on their standard delivery round, bulkier parcels have to be delivered by van, which is more expensive. Royal Mail's new prices reflect this difference in delivery cost.
- 5.27 Furthermore consumers may be able to mitigate against the price increases either by adapting their packaging, or taking advantage of Royal Mail's contract prices for parcels, or both. Businesses sending 1,000 parcels or more per year can take advantage of Royal Mail contract parcel prices, following Royal Mail's reduction of this minimum volume threshold from 5,000 items.⁵⁰
- 5.28 We also note in this context that the Forum of Private Business' survey on small businesses' views about important cost pressures found that the price of post is not the principal cost concern for most businesses.

Conclusions

- 5.29 The majority of UK businesses are small (in terms of number of employees or annual turnover) and their expenditure on post is correspondingly small. Of the 4.5 million UK businesses, around three quarters (3.2 million) are types of sole trader with no other employees, with an average annual turnover of £60k. Our consumer research shows that:
- a) small business spend on post is low. For example, businesses with up to two employees have median spend of £9 per month and mean spend of £133 per month;
 - b) around 90% of small businesses (those with up to two employees, or with annual turnover under £50k) spend the majority of their mail budget on Royal Mail, with around 90% of Royal Mail universal postal services;
 - c) only a small proportion of small businesses say that mail is 'core' to their business, and this is smaller than the average for all businesses;

⁵⁰ To qualify for contract mail and parcel prices, a customer must spend a minimum of £5k a year on postage. This can be made up of postage spend on a combination of Letter and parcel products.

- d) postal spend for businesses that say mail is 'core' is higher than for those where it is 'non-core';
 - e) many small businesses, along with businesses in general, are choosing to shift at least some communications to non-post alternatives; and
 - f) many businesses are willing and able to switch at least some of their postal use to different or cheaper universal postal services (e.g. from First Class to Second Class).
- 5.30 We have framed our approach to the question of whether universal postal services are affordable for a business in terms of whether the prices of these services might jeopardise the commercial viability of businesses which rely on them. This might be the case where a business meets three conditions (low turnover, low spend on mail, and where mail is 'core' to their business). This is because such a business would have a relatively high reliance on post in terms of mail spend relative to turnover but coupled with a limited ability to switch to cheaper postal products or providers, because their absolute level of spend on or usage of mail is relatively low.
- 5.31 Given that small businesses are more likely to be using Royal Mail and universal service products, and that their spend on post is more likely to be small in absolute terms but high relative to turnover, in selecting data and evidence we have particularly focused on the experiences of small businesses (particularly those with up to two employees, or with annual turnover under £50k).
- 5.32 Our approach was to identify those businesses potentially at risk of finding universal postal services unaffordable based on the above three conditions. We estimate that on this basis, there could be up to 100,000 (2.4%) UK businesses for whom the prices of universal postal services could in principle have a material impact on commercial viability. This is an estimate of the maximum number of UK businesses that may be at risk, rather than an estimate of the actual number at risk.
- 5.33 It is reasonable to believe that the extent of any affordability issues will in practice be smaller than this estimate. For example, unavoidable postal costs are unlikely to be the main determinant of a failure of commercial viability. Also, the Forum of Private Businesses' survey findings indicated that the price of post is not the principal cost concern for most businesses as only around 4% of businesses surveyed reported that marketing costs due to postage prices were the main cost pressure to their business.
- 5.34 We acknowledge that Royal Mail's move to more cost reflective pricing for parcels may mean some consumers face substantial price increases (if sending light but bulky parcels). However, whilst we have been made aware of two businesses expressing concerns about the likely impact of the April 2013 parcel price changes (due to them sending light but bulky items) we do not consider that this means there are widespread problems of businesses being able to afford universal postal services.
- 5.35 On this basis our findings suggest that universal postal services are affordable for UK businesses, including small and medium businesses, at current prices and prices to take effect in April 2013. Although we found that a very small proportion of businesses might in principle be at risk of being unable to afford universal postal

service prices,⁵¹ we have not found (nor has it been raised with us) any evidence to show that such businesses are in fact unable to afford universal postal services or that the commercial viability of businesses would be significantly impacted by current prices or prices due to take effect from April 2013.

⁵¹ These would be specific types of business which have low turnover, low spend on mail, and where mail is 'core' to their business.

Section 6

Overall conclusions and future monitoring

6.1 This section sets out:

- our conclusions on the affordability of universal postal services including an overview of our findings for residential consumers and business consumers; and
- how we will monitor affordability issues through our more general monitoring regime for Royal Mail.

Conclusions on affordability of universal postal services

6.2 The evidence we have collected indicates that universal postal services are affordable for both residential consumers (including low income and other vulnerable consumers) and UK businesses (including small and medium businesses) at current prices. We have reviewed the price changes that are due to take effect from 2 April 2013 (as announced by Royal Mail in March 2013), and consider that universal postal services will continue to be affordable following these changes.

Overview of findings: residential

6.3 Overall, our findings suggest that universal postal services are affordable for almost all residential consumers, including low income and other vulnerable consumers, at current prices and prices to take effect in April 2013. We note that our research findings indicate that there are some very limited circumstances where a consumer could be at risk from not being able to afford universal postal services. These circumstances are where a consumer suffers both significant financial difficulty or very low income, and has a frequent need to send post items they consider to be essential. This reflects very particular circumstances and severe financial hardship. It is likely that consumers in such circumstances would unfortunately have concerns about the prices of universal postal services, even at much lower prices.

Overview of findings: business

6.4 Overall, our findings suggest that universal postal services are affordable for UK businesses, including small and medium businesses, at current prices and prices to take effect in April 2013. Although we found that a very small proportion of businesses might be at risk of being unable to afford universal postal service prices,⁵² we have not found (nor has it been raised with us) any evidence to show that such businesses are in fact unable to afford universal postal services or that the commercial viability of businesses would be significantly impacted by current prices or prices due to take effect from April 2013.

Monitoring regime

6.5 In the March 2012 statement, as part of the new regulatory approach, we committed to an effective and ongoing monitoring regime to track Royal Mail's performance in

⁵² These would be specific types of business which have low turnover, low spend on mail, and where mail is 'core' to their business.

respect of progress of efficiency, quality of service and affordability of universal postal services.

- 6.6 As part of our duties, we will continue to monitor affordability through this general monitoring regime to track Royal Mail's performance.⁵³ In particular, we will continue to carry out our tracker research for residential consumers and businesses to monitor post use, and to assess the affordability of universal postal services, value for money and satisfaction with post and postal prices. We will also commission further consumer research to explore consumer views and experience concerning affordability if we consider that this is necessary to supplement our ongoing monitoring.
- 6.7 We continue to welcome engagement on this important topic, especially if stakeholders have evidence of affordability issues in relation to universal postal services.

⁵³ See footnote 6.

Annex 1

Approaches to affordability

A1.1 This annex summarises relevant approaches to affordability that have been taken elsewhere, for example by academics and researchers into poverty issues. We have had regard to a number of these approaches and have adopted some similar approaches in carrying out our current analysis of affordability, as outlined in section 3.

A1.2 This annex is structured as follows:

- general approaches to assessing affordability for residential consumers;
- European Union Member State approaches to assessing affordability of universal postal services.

General approaches to assessing affordability for residential consumers

A1.3 A number of approaches to assessing affordability have been identified in principle and some have been employed in practice for a range of goods and services (e.g. housing, energy and water). We outline and discuss below those approaches that are potentially more relevant to assessing affordability where, as is the case for universal postal services, there is low consumer spend.

Income methods

A1.4 A common approach to defining and assessing affordability is for the price of the service in question to be defined as ‘affordable’ if expenditure on acquiring the necessary or socially desirable quantity of the service at that price leaves a consumer or household with sufficient remaining income or spending power to meet its other requirements (e.g. to buy food). The Public Utilities Access Forum⁵⁴ has for example suggested that affordability of utilities can be broadly defined as:

“The ability to pay for necessary levels of consumption within normal spending patterns.”

A1.5 Variants of this approach have been used to assess affordability of gas, electricity, water and housing. For example, one way that ‘fuel poverty’ (i.e. spend on electricity and gas may present an affordability issue) has been assessed is to define a household as being in ‘fuel poverty’ where it needs to spend more than 10% of its income on fuel to achieve a sufficient level of heating.

A1.6 This type of approach is useful in that it links affordability to the overall set of resources a household may need, and the extent to which necessary spend levels for the service in question compares to other necessary household requirements. This can also reflect the individual consumer’s or household’s circumstances.

⁵⁴ Public Utilities Access Forum *Towards defining and measuring affordability of utilities – a discussion paper* available at:
<http://www.puaf.org.uk/docs/news/Affordability-%20a%20discussion%20paper.pdf>

A1.7 In practice however it may not be straightforward to gauge these effects. The consequences for other household requirements is likely to depend on household income, which can be measured in a number of ways (e.g. before or after housing costs) and no full consensus exists on what the necessary level of residual income should be.

Direct methods

A1.8 Some insights are provided by research on poverty.⁵⁵ One method to gauge poverty for example, is to identify or determine the number of those whose needs are unsatisfied, for example those who suffer from an enforced lack of necessities. More recent research on poverty and social exclusion has used this approach, among others, to inform research.⁵⁶

A1.9 Related questions arise in terms of the extent to which any lack of necessities may be enforced and the degree to which any lack may constitute living in poverty. Measurement issues also occur about the extent to which self-reported perceptions of any lack of necessities should be accepted.

A1.10 Nevertheless the central insight here is that a direct assessment of the impact on an individual's or household's welfare arising from a lack of access to particular resources is a valid way of gauging poverty. It can be translated to the question of affordability by assessing the extent to which a consumer suffers detriment either as a result of not purchasing an item because of its cost or foregoing other spend in order to purchase the item in spite of its cost.

A1.11 This has advantages in that it takes into account the circumstances of the individual or household. It is independent of income measures or any assessment of the level of sufficient remaining income or spending power to meet a consumer's other requirements (e.g. to buy food), following any necessary expenditure on the item in question. It may be useful for example where items of interest may be low cost but potentially high value to consumers. However, a drawback of direct methods of assessing affordability is that they are necessarily subjective.

Consumer research

A1.12 An approach related to direct methods may be to ask consumers directly about their experience of, or views about, affordability. Consumer research can be used to understand current usage patterns, reasons for current usage patterns, views on prices and any consequences for consumers as a result of usage or prices. For example, the Public Utilities Access Forum⁵⁷ suggests asking questions such as:

- Do you find x affordable?
- Do you buy as much of x as you feel your household needs?

A1.13 Consumer research may also help provide an understanding of the extent to which consumers or different consumer groups are aware of prices and how much they regard existing or potential prices as a constraint on their use of a service.

⁵⁵ See for example chapter 6 "Poor Britain" Joanna Mack and Stewart Lansley, available at: <http://www.poverty.ac.uk/sites/poverty/files/poor-britain-Mack%26Lansley.pdf>

⁵⁶ See for example the Poverty and Social Exclusion in the UK research project <http://www.poverty.ac.uk/definitions-poverty/consensual-method>

⁵⁷ See footnote 53.

A1.14 This type of approach is reasonably straightforward to implement, and may be particularly useful in identifying differences in views and experiences between consumer groups. However, there are potential drawbacks in that both questions and answers are highly subjective; different consumers may understand ‘affordability’ in different terms or conflate views about affordability and value for money.

Implications for our approach

A1.15 We consider that the above approaches to assessing affordability all have some useful advantages, but that it would not be appropriate to rely on any one of them alone. For example, income methods are useful in gauging affordability for the average consumer with an average income level, or where spend on the item in question is high relative to income, meaning that any adverse consequences of that spend may be clearer. They may be less useful for providing insight to the experiences of households where, as for post, spend may be low relative to income but the value of post and/or consequences of being unable to afford universal postal services may be significant. We therefore consider that income methods can be usefully supplemented by direct methods and consumer research to help to add this insight, particularly in identifying and gauging any consumer detriment.

European Union Member State approaches to assessing affordability of universal postal services

A1.16 Article 3 of the Directive requires prices of universal postal services to be “affordable”, but does not specify how affordability is to be measured. This is left to the discretion of Member States.

A1.17 We asked other regulators in EU Member States about their approaches to affordability in light of the EU Directive requirement. Table 4 below provides a brief summary of these approaches and shows that there is a variety of approaches to assessing affordability including:

- comparators: e.g. post spend versus income or household spend;

Postal prices may be held to be affordable where they account for, on average, a very low proportion of average income.

- consumer research/consultation.

Consumer research can be used to seek consumer views directly about whether prices or proposed prices may be affordable.

- price cap/cost orientation;

Postal prices may be said to be *de facto* affordable where a regulator caps postal prices or sets them with reference to underlying or future expected costs, since prices that are lower than these would imply either financially unsustainable postal services or some form of subsidy of postal usage.

- international benchmarking;

Postal prices in any one country may be considered to be relatively affordable where they are either below, or not significantly above, prices for similar products in comparable countries.

Table 4: Summary of approaches to affordability

Country	Summary of country's approach to affordability
France	Affordability is evaluated against the value of the service for consumers. It can be assessed through the behaviour of demand, taking into account the level of cost and the price of comparable services.
Ireland	In general affordability is assessed by reference to studies, surveys, and views of postal service users.
Italy	Ensures affordability through ex ante price cap to set cost oriented tariffs.
Norway	Price cap in place. Prices were cost orientated at the start of the price cap and no complaints have been received to say that prices are unaffordable.
Portugal	The affordability of universal postal services is currently being assessed. If a price cap for all or some postal services is considered to be needed, the price cap and the principle of cost orientation will be considered when assessing affordability. Portugal also compares the price of some services (e.g. prices of items weighing 20g) with other EU countries alongside available information on household spending on postal items and market research.
Slovakia	Regulate prices as maximal prices which cannot be exceeded. Slovakia recently agreed a price increase above rate of inflation as prices are cost-oriented, the decline of volume means the unit costs have increased more than inflation and growth of average wage.
Spain	Compare in absolute terms, Spain's letter prices with prices of basic services from other EU countries. Also compare against the economic conditions of each country through the ratio $\times 10.000 \text{ Price} / \text{GDP}$. Also compare the relationship between the price of the letter and the average wage in each country.
Sweden	As annual postal expenditure is minimal (EUR 46 per household – 0.14% of total household expenditure), no explicit measure of affordability. Price cap in place for standard letter (prices cannot increase more than the consumer price index). Also carry out an annual customer survey and compare letter and parcel prices with several comparable countries in order to evaluate how "reasonable" the Swedish prices are.

Implications for our approach

A1.18 Regarding approaches by EU Member States, we consider that approaches using comparator spend and consumer research are helpful in terms of our research objectives. However we suggest that approaches based on price caps or cost orientation would not be appropriate in the UK given that our regulatory regime gives Royal Mail pricing freedom, with some universal service products not being subject to any price cap. We also consider that inter-country postal price

comparisons are less useful in the UK context, given that they provide little insight into UK consumers' experiences in using or affording post and the diversity of experience across consumer groups.

Annex 2

Residential consumer findings

A2.1 This annex summarises relevant Ofcom research and data concerning prices, and residential consumers' use of, and expenditure on, universal postal services, with the aim of demonstrating how different consumer groups' use might be impacted by the affordability of universal postal services.

A2.2 Our principal data source is consumer research undertaken by Ofcom, in particular:

- Review of User Needs Research 2012: As part our Review of Postal Users' Needs, Ofcom undertook consumer research of residential and business postal needs, with fieldwork in April to June 2012.⁵⁸
- Ofcom residential tracker surveys: Ofcom also carries out quarterly quantitative surveys of consumers ('trackers'), including their use of postal services. The latest results available are for quarters 3 and 4 of 2012,⁵⁹ referred to as 'tracker data' below.

A2.3 We have also had regard to:

- estimates of spend on post derived by combining consumer market research results, price data and data from Royal Mail regarding relative volumes of some items of post sent; and
- data from the ONS' Living Cost and Food Survey which compiles data on household spend. We refer to data as 'ONS data' below.

Prices of universal postal services

A2.4 Prior to August 2006, pricing of stamps and parcels depended entirely on weight, regardless of the dimensions of the item to be posted. Items weighing up to 60g for example could be posted using a First or Second Class stamp. In August 2006, Royal Mail significantly rebalanced prices and terms, with new formats introduced for:

- standard Letter;
- Large Letter; and
- packet.

A2.5 Royal Mail also increased the prices of lighter packets (100g-500g), not classed as the new 'Large Letter' dimensions, relatively quickly, bringing them into line with heavier packets (e.g. 750g) not classed as 'Large Letter'.

A2.6 In April 2012, Royal Mail made some significant price increases, for example, increasing the price of a First Class stamp by 30% (46p to 60p) and a Second Class stamp by 39% (36p to 50p).

⁵⁸ See footnotes 30.

⁵⁹ See footnote 31.

A2.7 Figure 8 shows the evolution of the nominal prices of a range of universal postal service products, including standard Letters, Large Letters and a selection of maximum weight packets sent by First and Second Class. Figure 9 expresses these same price developments but adjusted for inflation and with each price rebased to an index of 100 in 2000, so prices relative to each other are illustrated more clearly. The effect of tariff rebalancing from 2006 is particularly clear in figure 9; in particular prices of First and Second Class stamps for standard Letters have risen in real terms.

Figure 8: Prices of illustrative universal postal services

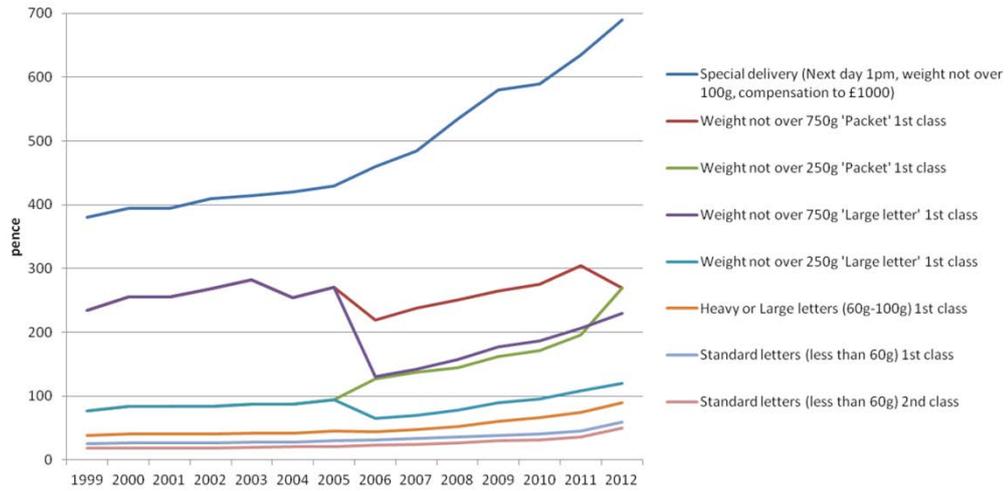
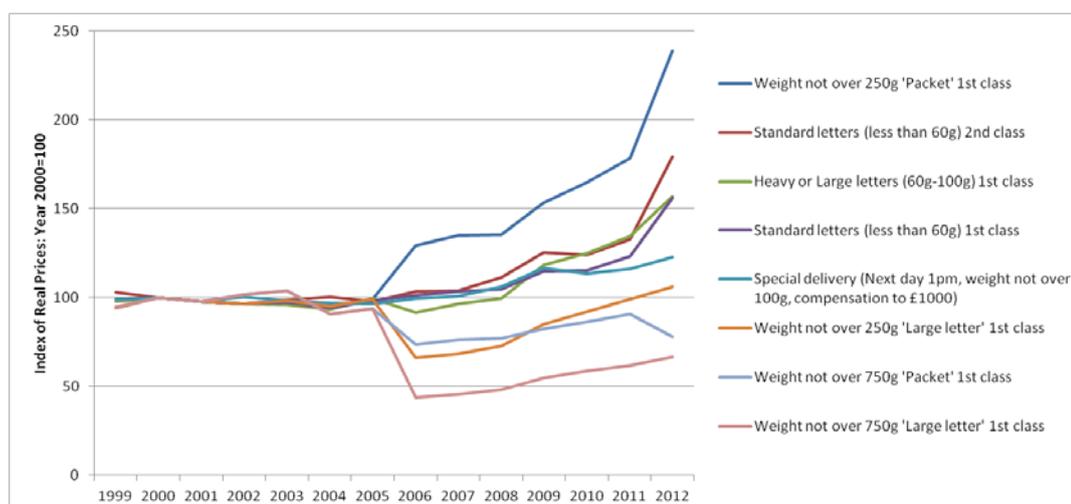


Figure 9: Price indices for illustrative universal postal services



Consumer sending of, and expenditure on, post

- A2.8 Our tracker data suggests that on average each residential consumer sends around seven items of post per month⁶⁰, with around 85% of these being letters and cards.
- A2.9 Table 6 sets out estimates of annual usage of and expenditure on postal products based on the tracker data combined with price and Royal Mail volume data.

⁶⁰ Based on the question “Approximately how many items of post – including letters, cards and parcels – have you personally sent in the last month?”

Table 6: Estimated usage of and expenditure on postal products 2012

Format and weight step	All residential consumers			Lower user consumers*		
	Average annual volume	Average annual spend	Spend %	Average annual volume	Average annual spend	Spend %
Letters	72.0	£41.40	57%	55.0	£31.63	56%
Large Letters	3.8	£3.38	5%	3.1	£2.72	5%
Packets 0-1kg	6.3	£16.58	23%	5.1	£13.37	24%
Packets 1-2kg	0.9	£5.84	8%	0.8	£4.71	8%
Packets 2kg+	0.4	£5.15	7%	0.3	£4.15	7%
Total	83.4	72.35	100%	64.3	£56.58	100%

Source: Ofcom consumer research ("tracker") Q3 2012 and Q4 2012, combined with Royal Mail data

*Based on usage of postage by consumers in socio-economic group DE

ONS' Living Costs and Food Survey

- A2.10 The main source of individual and household level data on spending in the UK is the ONS data. The basis of the spending data is a two week expenditure diary completed by each household member. Each person in the household compiles a record of each item of spending in a particular fortnight. From these diaries it is possible to calculate average weekly amounts of household spend on particular goods or services, including post.⁶¹ Data is presently available on a consistently defined basis from 2001 to 2010. We consider that this data set gives a suitable time horizon over which to gauge trends and changes.
- A2.11 The ONS data can give a more refined breakdown on household spend by consumer group, including those that may be more likely to be vulnerable. We set out results for post and other spend items below, providing data for 2010, followed by trends, and then December (Christmas) spend.

Spend in 2010

- A2.12 Table 7 sets out results for 2010 and shows that average spend on postal services in 2010 was around 50p per week across all households (or about 54p when rebased to 2012 prices). The *Average weekly spend* column is for all households and so includes those who recorded no spend on post. The *Average weekly spend, if anything* column excludes households where the spend diary records no spend on post, which may reflect the fact that the household chose not to purchase postal items that week, or that the household rarely or never purchases postal products.

⁶¹ Postal services spend given in ONS data is Classification of Individual Consumption by Purpose ('COICOP') category 8.1.1.1.1. This covers 12 categories of spend, including stamps, parcel post, recorded and registered post, air mail letters and postage.

Nevertheless the measure gives supporting insight into variations between consumer groups.

Table 7: Postal spending in 2010 (nominal prices)

Group	Average weekly spend	Proportion with any recorded spend on post	Average weekly spend, if anything	Sample size (households)
All households	£0.49	16.2%	£3.03	5,263
Households, someone aged 65+	£0.59	21.2%	£2.80	1,545
Households, someone aged 75+	£0.64	22.1%	£2.91	694
Households with someone receiving disability benefits	£0.49	14.2%	£3.43	739
<i>No internet</i>	£0.28	12.4%	£2.22	1,377
Area type illustrations*				
Countryside	£0.69	21.0%	£3.15	651
Prospering suburbs	£0.65	21.8%	£3.06	897
Constrained by circumstances	£0.26	21.3%	£2.47	643
City living	£0.63	12.2%	£3.01	252
Quintile of consumption spending, All households				
Lowest	£0.18	9.1%	£2.01	1,023
2	£0.29	13.2%	£2.19	1,082
3	£0.34	13.7%	£2.51	1,082
4	£0.60	19.4%	£3.09	1,059
Highest	£1.04	25.7%	£4.05	1,017
Quintile of consumption spending, Households with someone aged 65+				
Lowest	£0.19	10.6%	£1.79	267
2	£0.41	17.1%	£2.41	293
3	£0.38	19.3%	£1.96	319
4	£0.71	25.4%	£2.80	331
Highest	£1.28	33.7%	£3.79	335
Sample quarter				
Jan to Mar	£0.35	15.7%	£2.26	1,280
Apr to Jun	£0.33	14.2%	£2.30	1,342
Jul to Sep	£0.44	15.5%	£2.86	1,363
Oct to Dec	£0.84	19.2%	£4.31	1,278
<i>Of which: December</i>	£1.49	26.2%	£5.69	388
Social class				
Professional	£0.65	19.1%	£3.40	1,525
Intermediate	£0.52	14.5%	£3.57	915
Routine	£0.18	8.5%	£2.11	736
Students	£0.29	14.2%	£2.05	100
Not classified	£0.49	17.9%	£2.73	1,987
Country				
England	£0.51	16.5%	£3.10	4,387
Wales	£0.19	13.7%	£1.36	261
Scotland	£0.49	14.5%	£3.36	468
Northern Ireland	£0.40	16.7%	£2.37	147

Source: analysis of ONS Living Costs and Fodd Survey 2010 data, weighted by *weighta*. Quintiles of spending are equally sized when considering the weighted numbers. Numbers based on fewer than 50 households will be unreliable.

*UK Census Output Areas describe 7 Area Types. We provide illustrations for four:

Countryside	Rural and semi-rural residents, many working from home.
Prospering suburbs	Generally established, prosperous
City living	Urban residents, more likely to have been in higher education
Constrained by circumstances	Areas in which consumers are more likely to be marginalised or on welfare benefits

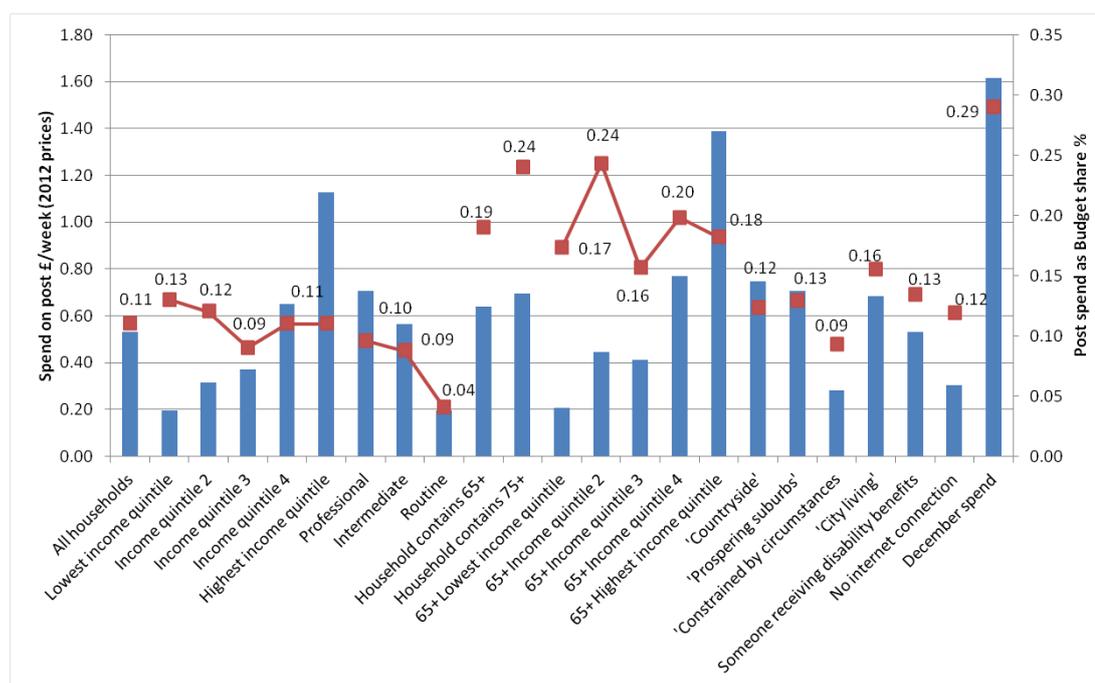
A2.13 ONS data enables postal spend by consumer group to be estimated, as well as postal spend as a proportion of total household expenditure (i.e. 'budget share'). Figure 10 illustrates, for the year 2010, expenditure on post in £ per week and budget share terms by demographic and between consumer groups, and for December 2010.

A2.14 There are significant variations across consumer groups, with:

- low income and those without internet spending less on post;
- older and higher income groups generally spending more on post; and
- households with a person receiving disability benefit spending broadly the same on average as all other households on post.

A2.15 It is also clear that average weekly spend on post in December 2010 (£1.49, nominal prices) was significantly higher than average weekly spend during the remainder of the year. Moreover just over one in four households recorded spend on post in December. This is significantly higher than the proportion that recorded any spend on post at other times of the year by most of the individually identified consumer groups, as set out in table 7.

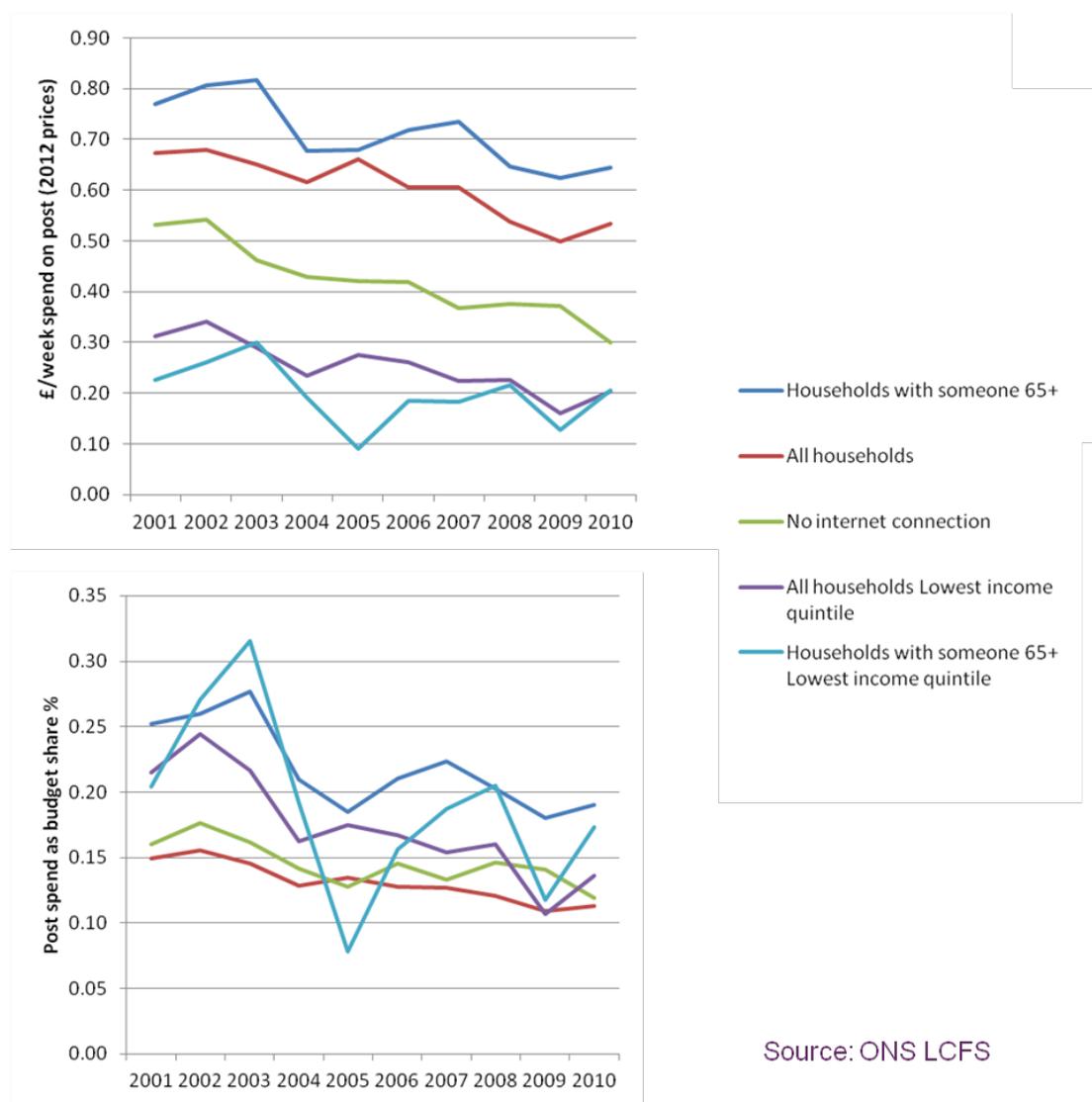
Figure 10: ONS data on household expenditure on post spend, and as a proportion of total household expenditure ('budget share'), for 2010



Changes in postal spend between 2001 and 2010

- A2.16 There has been a downward trend in expenditure on post over time, both in terms of £ per week (after adjustment for inflation) and budget share. We have examined these trends for five consumer groups of interest:
- all households;
 - all households, lowest income quintile;
 - households with someone aged 65 or over;
 - households with someone aged 65 or over, lowest income quintile;
 - households with no internet connection.
- A2.17 Figure 11 charts how levels of weekly spend on post and budget share has generally declined for these groups over the period 2001 to 2010. Spend on post has been re-based to 2012 prices using the Retail Price Index. It is worth noting that estimates of means for sub-groups of the population are based on correspondingly smaller sample sizes and so are likely to be subject to greater sampling error. Nevertheless, changes and trends in means remain as useful indicators of consumer behaviour.
- A2.18 Expressed in 2012 prices, average weekly spend on post for all households has fallen from about 68p in 2001 to about 54p in 2010. For poorer pensioner households (defined here as lowest income fifth (quintile) of households with someone over 65), changes in average weekly spend have been more variable and smaller over the whole period, reducing over the whole period from about 23p to about 21p. Changes in budget share for this group have been correspondingly variable. The variance here may reflect the lower sample size for this group and greater variability in this group's total consumption expenditure.

Figure 11: Spend on post over time, level and budget share



Comparator expenditure

A2.19 Changes in expenditure on post compared to changes in household total expenditure and expenditure on comparator items can provide useful indicators and inferences about whether expenditure on post was or is constrained. The paragraphs on ‘comparator spend’ in Section 3 sets out how this data might be used to draw such inferences. We have looked at changes over the period 2001-03 to 2008-10 and by comparing December spend to averages for the year.

Weekly spend and changes over time

A2.20 We have chosen a range of comparator spend items that represent to some degree both discretionary and non-discretionary spend:

- total household expenditure,
- mobile telephones; and

- satellite TV subscriptions.

A2.21 Table 8 sets out the data for these items and changes in expenditure. Most changes are statistically significant at the 5% level (using standard statistical “t-test” of comparison of means); the table indicates instances where this is not the case.

A2.22 Figure 12 provides charts on how spend on these items has changed between 2001-03 (averaged over these years) and 2008-10 (averaged over these years), for different consumer groups, rebased to 2012 prices using the Retail Price Index.

Figure 12: Change 2001/03 to 2008/10 in weekly expenditure on post against total expenditure and expenditure on comparator items, 2012 prices

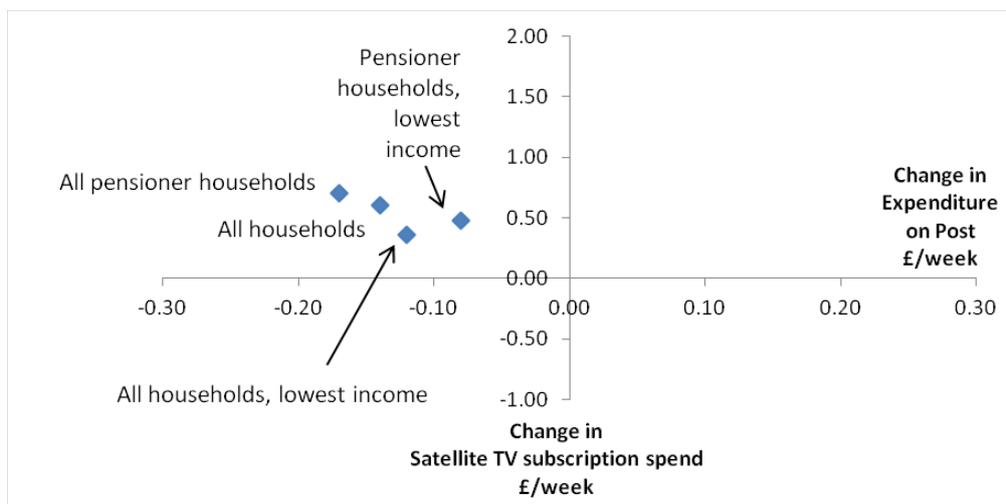
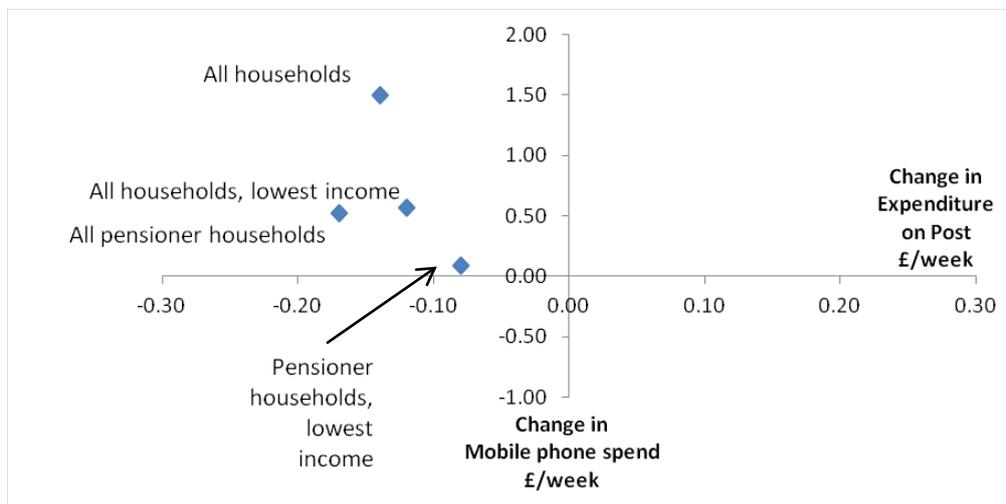
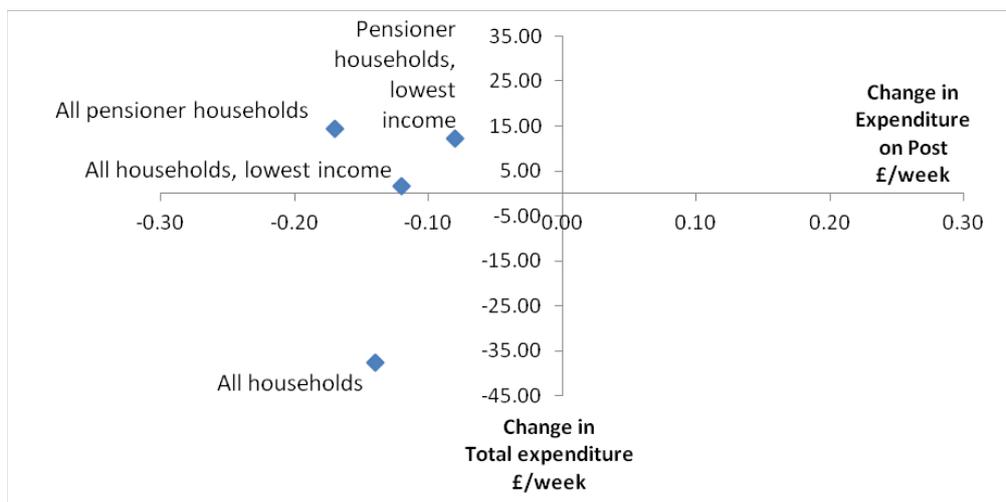


Table 8: Real terms expenditure and changes in expenditure

£/week, 2012 prices	Total consumption expenditure	Post	Mobile telephone	Satellite TV sub- scriptions	All communi- -cations less post
Group	£/week	£/week	£/week	£/week	£/week
All households					
2001-03	559.77	0.67	3.20	2.20	13.96
2008-10	522.18	0.53	4.70	2.80	13.17
<i>Change</i>	-37.59	-0.14	+1.50	+0.60	-0.79
All households, lowest income quintile					
2001-03	140.93	0.32	0.23	0.58	5.90
2008-10	142.60	0.20	0.80	0.94	6.19
<i>Change</i>	+1.67*	-0.12	+0.57	+0.36	+0.29
All households, contain someone aged over 65					
2001-03	329.32	0.81	0.50	1.04	7.84
2008-10	343.72	0.64	1.02	1.74	8.52
<i>Change</i>	+14.40	-0.17	+0.52	+0.70	+0.68
All households, contain some aged over 65, lowest income quintile					
2001-03	95.58	0.27	0.02	0.22	4.91
2008-10	107.81	0.19	0.11	0.70	5.15
<i>Change</i>	+12.23	-0.08	+0.09	+0.48	+0.24*

*Change not statistically significant at the 5% level (t-test)

Expenditure in December

- A2.23 Expenditure on post is generally two to three times higher during December than for the rest of the year, for all consumer groups, and it is clear that sending post at Christmas is important for many. Figure 13 illustrates the differences. We have averaged spend data over 2008 to 2010 to provide larger sample sizes for estimating spend in December.
- A2.24 For comparison, Figure 14 also illustrates changes in total household expenditure in December, averaged across 2008-10. Broadly speaking for low income groups, there is little change in December in total spend compared to the rest of the year, although expenditure on post increases.
- A2.25 Table 9 sets out estimates of mean spend on post and total household expenditure in December over the two time periods 2001-03 and 2008-10, and changes in these. Figure 15 charts changes in expenditure on post against changes in total household expenditure for four illustrative groups of interest (all households, all households in the lowest income quintile, households with a person over 65, households with a person over 65 in the lowest income quintile). Taking into account whether changes were statistically significant at the 5% level, it appears that for low income households real expenditure was roughly constant but post spend was lower, while for low income pensioner households expenditure on post in December was broadly constant while total expenditure increased.

Figure 13: Weekly expenditure on post in December, compared to rest of year (2008-10)

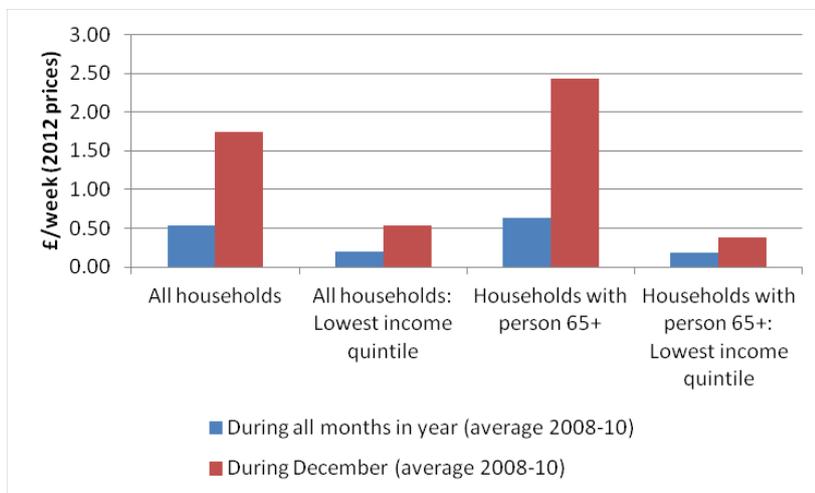


Figure 14: Weekly household total expenditure in December, compared to rest of year (2008-10)

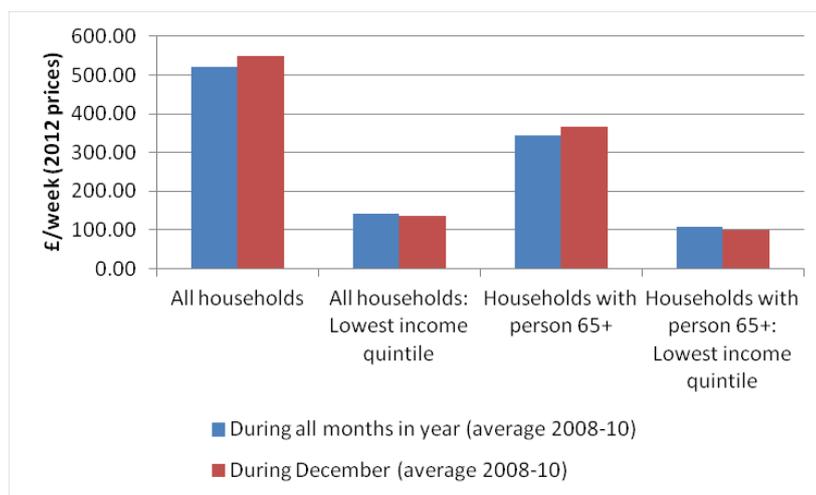
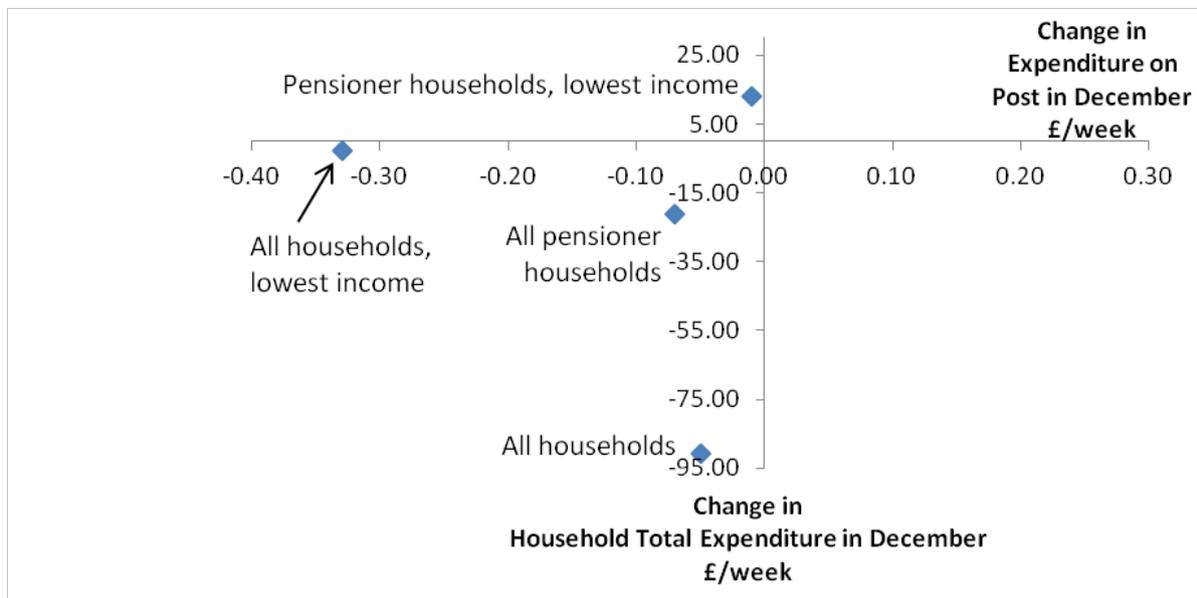


Table 9: Expenditure on post, Total expenditure in December

£/week, 2012 prices	Post	Total spend
Group	£/week	£/week
All households		
2001-03	1.80	639.48
2008-10	1.75	548.81
Change	-0.05*	-90.67
All households, lowest income quintile		
2001-03	0.87	138.25
2008-10	0.54	135.54
Change	-0.33	-2.71*
All households, contain someone aged over 65		
2001-03	2.50	387.42
2008-10	2.43	366.39
Change	-0.07*	-21.03*
All households, contain some aged over 65, lowest income quintile		
2001-03	0.39	87.00
2008-10	0.38	100.06
Change	-0.01*	+13.06

*Change not statistically significant at the 5% level (t-test)

Figure 15: Change 2001-03 to 2008-10 in weekly household expenditure on post and household total expenditure, in December



Ofcom consumer research

- A2.26 Our Review of User Needs research data is based on extensive market research to inform our understanding of the reasonable needs of postal users. This included a survey⁶² of just over 4,000 residential consumers during April to June 2012 concerning their use of postal services. We have used the Review of User Needs research to inform our assessment of affordability.
- A2.27 Table 10 sets out the main findings concerning the sending of postal items and use of postal services by residential consumers, and how this varies by key demographics and consumer groups. It is clear that younger and low income consumers and those without access to the internet tend to use postal services less than average. More than half of those aged under 35, on low income, or without access to the internet say they send *no* post in an average month.
- A2.28 This pattern of sending post is confirmed and partly explained by examining the types of post different consumers send. Table 11 sets out the data. Sending personal communications to friends and family (letters, cards, invitations etc.) is more prevalent among older consumers,⁶³ those in the AB socio-economic group and those in rural areas. Disabled consumers have higher than average post send for personal communications, but differ little from the average for other types of postal send. Reflecting lower use of post in general, those consumers who are younger, on low incomes, without access to the internet, or in socio-economic group DE are considerably more likely than the average to send none of the types of post in table 11.
- A2.29 We also undertake regular consumer research of the postal market, via our quarterly tracker survey. Table 12 sets out the main results for residential expenditure on post. Across all consumers (i.e. those who have and those who have not sent post), average monthly spend on post is £7.73 (or £1.78 per week). As might be expected, post spend patterns in general mirror spending patterns, with younger consumers and those on low incomes spending less. By contrast those in rural areas spend less on post, though the number of items sent is found by the Review of User Needs research data to be greater than average.

⁶² Full result data tables available at:

<http://stakeholders.ofcom.org.uk/binaries/research/post/quantitative-oct2012/residential.pdf>

⁶³ Forty-nine per cent of consumers aged 75+ send personal communications via post at least once a month, compared to 22% of those aged 16-24 (Source: Review of User Needs 2012. Base: All adults in UK).

Table 10: Items of post sent, postal services used

Group	Average number of items ⁶⁴ sent per month	Proportion who send <i>no</i> post in an average month	Proportion who have used the following Royal Mail services in the last 12 months			
	Number	%	Recorded %	Special delivery %	Standard parcel %	None %
All households	6.4	45	40	31	44	29
Age						
16-24	2.3	66	30	24	39	35
25-34	4.0	51	43	38	46	22
35-44	9.2	43	47	38	46	20
45-54	7.4	40	47	33	46	26
55-64	6.7	38	42	32	47	25
65-74	7.5	36	36	23	41	38
over 75	7.4	42	18	10	32	56
Household contains person with a disability	7.8	43	33	26	37	41
Socio-Economic Group (SEG)						
AB	9.4	31	52	42	57	16
C1	5.7	46	46	34	47	23
C2	7.2	44	37	27	42	30
DE	4.4	56	25	20	31	45
Annual Income						
Less than £11 500	4.7	51	29	24	36	39
Greater than £50 000	10.0	30	57	51	60	12
Internet						
Household has access to internet	6.6	43	44	34	47	24
Household does not have access to internet	5.3	54	20	15	26	53
Rural / Urban						
Rural	8.1	37	49	33	48	28
Deep rural ⁶⁵	8.7	37	47	38	55	22
Urban	5.9	48	37	30	42	30

Source: Review of User Needs 2012. Base: All adults in UK

⁶⁴ Including letters, postcards and parcels.⁶⁵ The deep rural classification varies from country to country, based on ONS/NRS/NISRA definitions. Broadly speaking, 'deep rural' includes small hamlets, isolated dwellings, very remote locations, or locations far from an urban centre.

Table 11: Types of mail sent at least once a month by post

Group	Personal communi- cations %	General correspond- ence %	Parcels / packets %	Payment for bills %	Other %	None %
All households	35	31	20	19	-	29
Age						
16-24	22	22	18	12	-	39
25-34	29	29	25	17	-	27
35-44	34	34	27	17	-	26
45-54	36	37	21	19	-	23
55-64	40	36	19	22	-	27
65-74	43	26	15	22	1	34
over 75	49	27	9	26	-	34
Household contains person with a disability	41	29	19	19	-	31
Socio-Economic Group (SEG)						
AB	44	40	28	19	-	20
C1	34	34	22	16	1	26
C2	35	29	22	24	-	25
DE	29	20	13	18	-	41
Annual Income						
Less than £11 500	31	24	16	19	-	34
Greater than £50 000	39	45	26	16	1	16
Internet						
Household has access to internet	35	33	23	18	-	26
Household does not have access to internet	34	20	10	22	-	41
Rural / Urban						
Rural	40	35	23	24	-	24
Deep rural	40	38	23	28	-	23
Urban	33	29	20	17	-	30

Source: Review of User Needs 2012. Base: All adults in UK

Table 12: Spend on postage, including letters, cards and parcels

Group	Proportion spending amount in last month:				Mean spend in last month £	Mean spend per week £
	Up to £1	£1.01 to £4	£4.01 to £10	Over £10		
	%	%	%	%		
All households	12	22	19	19	7.73	1.78
Age						
16-34	13	21	14	20	6.28	1.45
35-54	12	22	19	23	10.61	2.45
over 55	11	24	25	14	6.23	1.44
Socio-Economic Group (SEG)						
AB	9	23	26	22	9.84	2.27
C1	10	22	22	22	8.07	1.86
C2	13	23	16	15	7.11	1.64
DE	16	22	13	16	5.88	1.36
Employment status						
Not working	12	24	20	14	5.92	1.37
Working	12	21	19	23	9.15	2.11
Internet						
Household has web access at home	11	22	20	21	8.38	1.93
Household does not have web access at home	17	22	17	11	4.70	1.08
Rural / Urban						
Rural	12	25	25	17	6.93	1.60
Urban	12	22	18	19	7.87	2.81

Source: Ofcom consumer survey "Residential consumer postal tracker"
Quarters 3-4 2012 (July to December 2012). Base: All respondents

Annex 3

Business consumer findings

A3.1 This annex summarises the relevant research and data that Ofcom has compiled concerning businesses' use of, and spend on, universal postal services, to inform our assessment of whether the universal postal services provided by Royal Mail are affordable.

Information sources

A3.2 Our principal data source is consumer research carried out by Ofcom, in particular:

- Review of User Needs Research 2012: As part our Review of Postal Users' Needs, Ofcom undertook quantitative consumer research of business postal needs, with fieldwork in April to June 2012⁶⁶.
- Ofcom business tracker surveys: Ofcom also carries out quarterly quantitative surveys of businesses ('trackers'), covering their use of postal services. The latest results available are for quarters 3 and 4 of 2012,⁶⁷ referred to as 'tracker data' below.

A3.3 We have also had regard to:

- Ofcom Postal Users' Needs Qualitative Research August 2012.⁶⁸

Types of business

A3.4 Concerns voiced by stakeholders about the affordability of universal postal service products for businesses have principally related to small and medium businesses. We note that smaller businesses may in principle be more likely to be at risk of post affordability issues given that their expenditure on post may be relatively high compared to turnover and they may not have access to cheaper substitutes. In addition, some businesses in rural areas or businesses operating from home premises are particularly reliant on using postal services to reach customers or suppliers. For these reasons we have particularly focused on selecting data and indicators that relate to, or contextualise, the experience of small businesses, in particular businesses:

- with up to two employees;
- with annual turnover less than £50k;
- that operate from 'home' as opposed to 'business' premises; and
- in 'rural' or 'deep rural'⁶⁹ locations.

⁶⁶ See footnote 30.

⁶⁷ Data due to be published in July 2013.

⁶⁸ See <http://stakeholders.ofcom.org.uk/binaries/research/post/deliberative-oct2012/main.pdf>

⁶⁹ The deep rural classification varies from country to country and was based on ONS/NRS/NISRA definitions. The deep rural designation in England and Wales was "hamlets and isolated dwellings", in Northern Ireland it was "small hamlets (with less than 1,000 inhabitants)" and in Scotland "very

- A3.5 We have also had regard to the importance of post to a business' operations. The Review of User Needs research asked respondents which of the three following statements best described their business:
- i) 'mail is core to our business operations';
 - ii) 'mail is critical for our customer communications and statements but not core to our business';
 - iii) 'mail is used mainly for our administrative needs and is not core to our service delivery.'
- A3.6 The Review of User Needs research also asked businesses whether they thought mail would be 'core' to them in three years time. We have particularly focused on businesses where mail is presently 'core'.

Overview of UK business landscape

- A3.7 There are around 4.5 million private enterprises in the UK. Most of these are small businesses. Around 75% for example have no employees (i.e. are types of sole trader businesses) with average annual turnover of £60k. A further 20% of the 4.5 million private enterprises employ between one and nine people with an average annual turnover of £417k.⁷⁰

Ofcom research on post use by businesses

- A3.8 Based on our Review of User Needs research data, we set out below results concerning spend on postal services and use of Royal Mail services, and the importance of post to businesses. Review of User Needs and tracker data provided data on businesses' willingness or ability to substitute to other services.

Spend on mail and use of Royal Mail services

- A3.9 Table 13 sets out data on spend by size and type of business. Review of User Needs research data shows that median monthly spend on post across all UK businesses is estimated to be relatively small, at about £18 per month, though mean spend is higher, at about £245 per month. The difference in these averages implies that a small number of businesses have very high mail spend.
- A3.10 Review of User Needs research data also shows that postal spend is strongly related both to the size of the business and how important post is for the business. Ninety-five per cent of businesses with an annual turnover under £50k for example spend less than £100 per month on post. Median spend on post for businesses for whom mail is 'core', at £76 per month, is higher than median spend for all businesses at £18 per month.
- A3.11 Moreover smaller businesses are very likely to spend the bulk of their post budget with Royal Mail, and to rely on stamps or other universal postal service products. Ninety-two per cent of businesses with up to two employees, and 88% of businesses with annual turnover under £50k, spend almost all or around three quarters of their mail spend with Royal Mail. These smaller businesses are also much more likely to use stamps than larger businesses, as illustrated in Figure 16.

remote" or "remote rural" (fewer than 3,000 inhabitants and a 30 minute drive or more from an urban centre).

⁷⁰ Business Innovations Skills Business Population Estimates for the UK and regions 2011.

The affordability of universal postal services

Consequently they are more likely to be using Royal Mail universal postal service products, i.e. products which are required to be affordable.

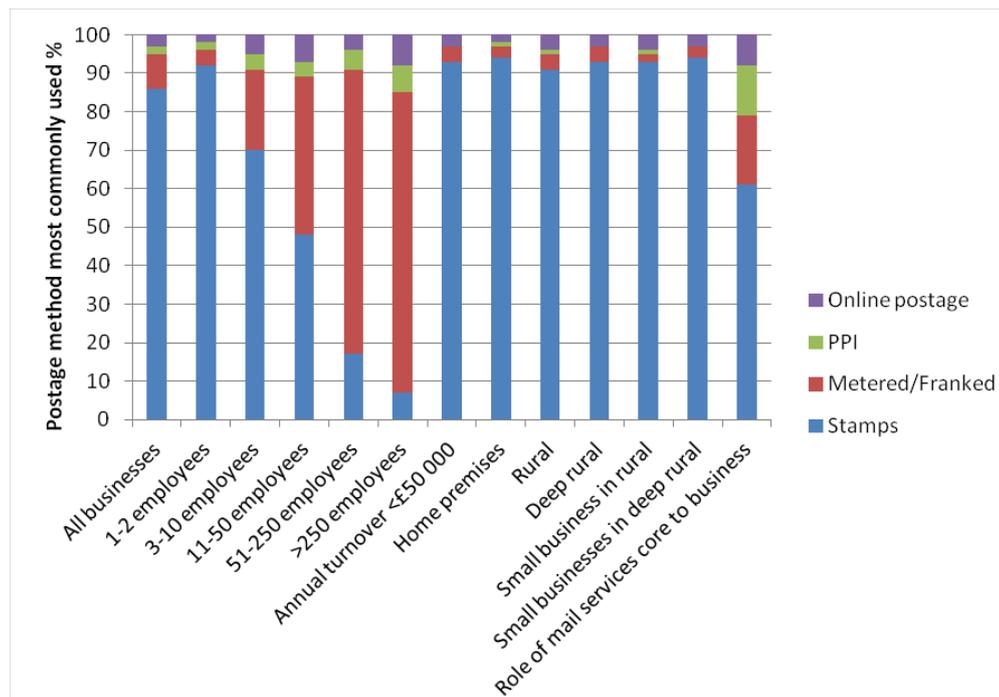
Table 13: Monthly spend on post by business size and importance of post, nominal prices

Type of business	under £10 %	£10-£25 %	£26-£50 %	£51-£100 %	£101-£449 %	£450-£999 %	over £1000 %	Mean Spend £	Median spend £
All businesses	45	21	14	9	6	3	2	£245	£18
Number of employees									
1-2*	51	23	13	5	3	2	3	£133	£9
3-10	28	15	16	21	16	2	2	£203	£38
11-50	8	14	20	16	19	15	9	£1668	£76
51-250	1	4	10	19	25	17	24	£2651	£275
over 251	1	3	4	4	21	12	56	£9387	£1750
Annual turnover									
under £50 000	62	20	8	4	3	2	1	£63	£9
£50k - £99k	32	38	15	6	4	5	1	£80	£18
£100k-£249k	35	18	25	13	6	1	2	£107	£18
£250k-£499k	11	10	19	29	8	0	23	£1115	£76
£500k-£999	40	9	9	28	8	1	4	£222	£38
over £1m	13	13	23	6	23	11	11	£2077	£76
Mail is 'core' to business									
Is 'core'	9	17	14	15	14	13	18	£1206	£76
Is 'critical'								£156	£38
Is not 'core'	60	22	10	3	4	1	0	£45	£9
Premises									
Home	56	25	9	3	2	2	2	£73	£9
Business	34	18	18	14	9	4	4	£409	£18
Rural / Urban									
Rural	45	24	16	12	2	0	1	£78	£18
Deep rural	22	40	17	7	7	6	1	£136	£18
Urban	46	20	13	8	7	3	3	£289	£18

*Includes sole traders

Totals may not be 100% due to rounding
Source: Review of User Needs 2012

Figure 16: Postage methods most commonly used when sending post with Royal Mail



Source: Review of User Needs 2012

Importance of post to businesses

- A3.12 Review of User Needs research data suggests that 16% of all businesses reported mail was 'core' to their operations. The proportion is greater for larger businesses, for example mail is 'core' for 36% of businesses with 51-250 employees and 30% of businesses with more than 250 employees. Mail is 'core' to business for 14% of businesses with up to two employees and 11% of businesses with annual turnover below £50k.
- A3.13 Figure 17 illustrates this across a range of business types. It includes views on whether businesses consider that mail will be 'core' to their business in three years time. Most businesses tend to the view that mail will become less important over time, i.e. a smaller proportion consider that mail will be 'core' in three years time than at present.

Willingness or ability to substitute to other services

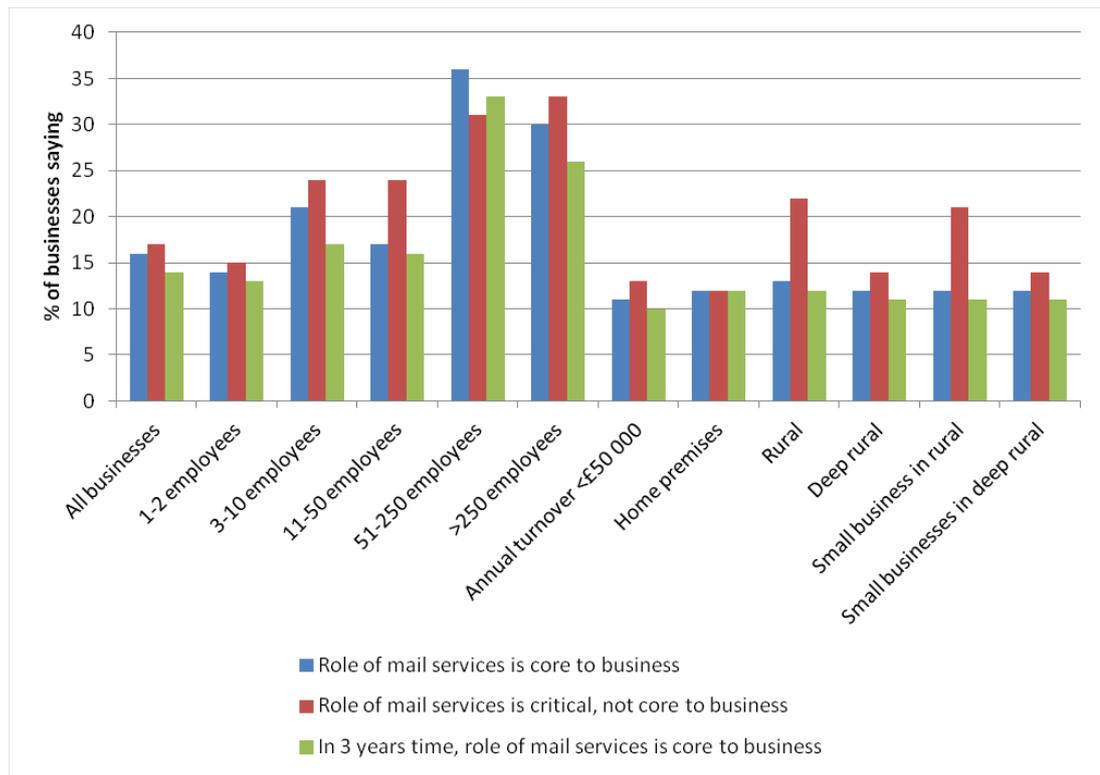
- A3.14 Businesses, whether mail is 'core' or not for them, in principle have a number of options to shift mail usage in response to price changes. They might for example:
- substitute between Royal Mail postal products, such as from First or Second Class stamps, or from stamps to franking;⁷¹ or
 - move to other methods of communication, such as email or other electronic or digital methods.

We note that where value or volumes are high enough, businesses could move to other postal operators,⁷² although, as noted in Section 3 of this report, a business with mail usage and levels of spend on mail similar to those outlined in Table 3 of this report may not find any financial benefit from moving to another postal operator.

⁷¹ Franking is an alternative to stamps and requires equipment at the premises of the business. The price per item sent is lower than the corresponding stamp price.

⁷² For example, Paragraph 7.51 of our October 2011 consultation on the new regulatory framework (<http://stakeholders.ofcom.org.uk/binaries/consultations/securing-the-postal-service/summary/condoc.pdf>) noted that "it is clear that access competition has led to large bulk mailers directly getting significant price savings by undertaking certain activities themselves and by taking advantage of better terms from other operators in the provision of upstream activities. In addition, access competition has now led to smaller customers gaining the benefits of lower prices. Our evidence suggests that access operators will now collect mail from customers with as few as 250 items per posting".

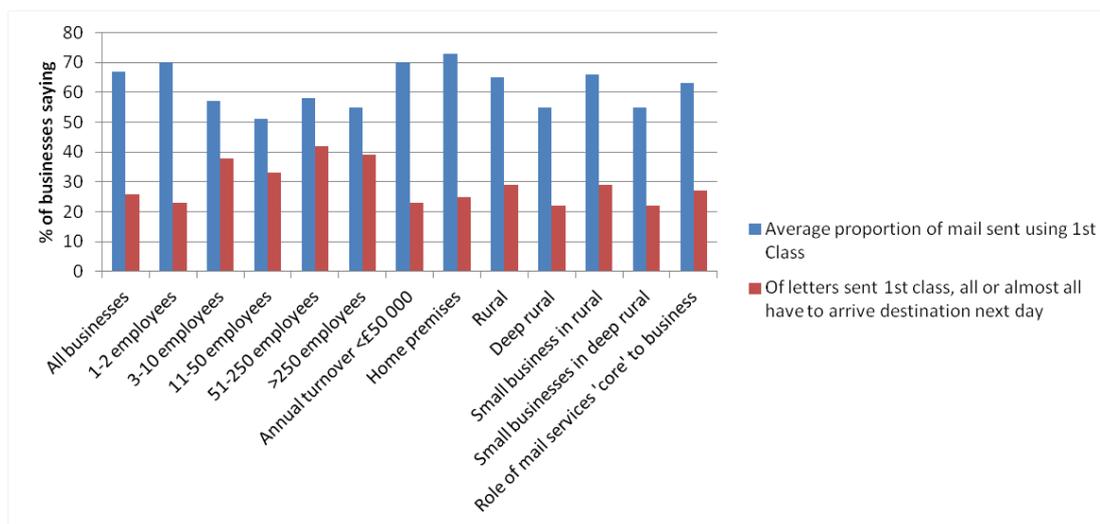
Figure 17: Importance of post to businesses



Source: Review of User Needs 2012

A3.15 The Review of User Needs research data and tracker data show that there is some ability and willingness among businesses to substitute in these ways. Figure 18 sets out the Review of User Needs research data on the extent to which businesses use and say they need to use First Class post. Differences are particularly marked for smaller businesses, suggesting there is a reasonable degree of scope to substitute.

Figure 18: Business use of, and need for, First Class

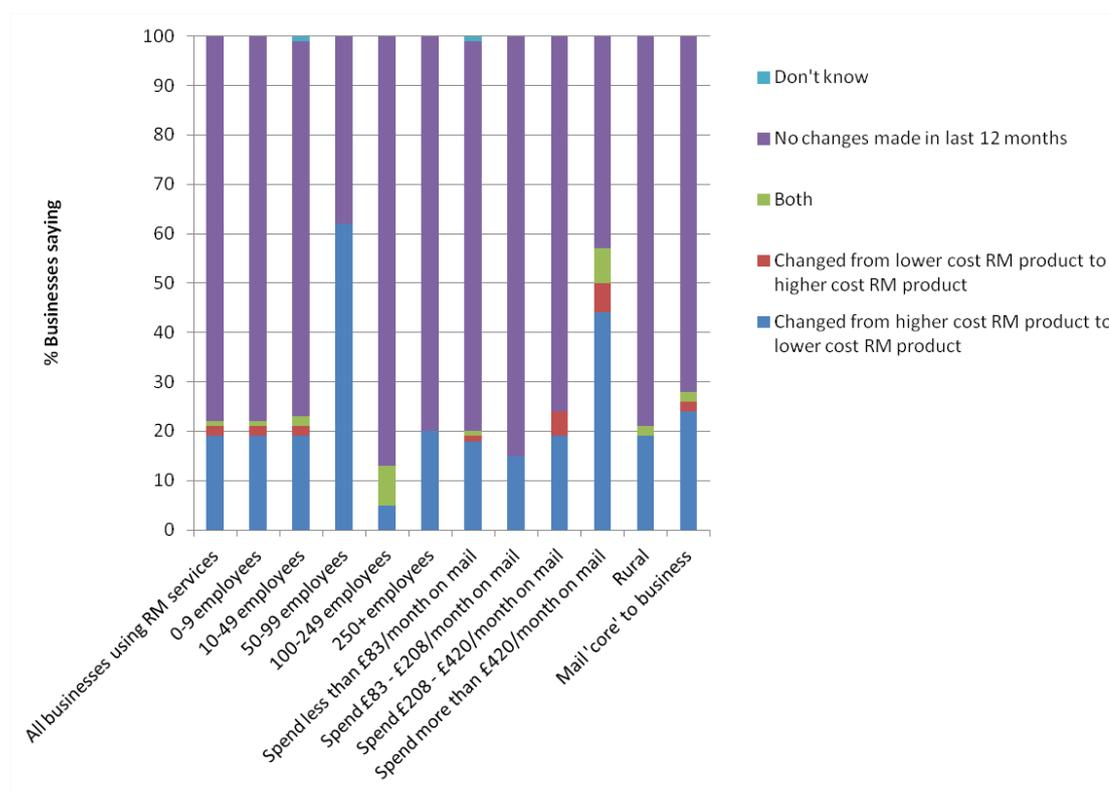


Source: Review of User Needs 2012

A3.16 Figure 19 sets out tracker data on businesses' shifts in using Royal Mail products by business type, using results from our quarter four 2012 tracker. Of those

respondents who changed Royal Mail services, around 80% said they did so because of Royal Mail price increases.

Figure 19: Shifts in last 12 months



Source: Ofcom tracker data Q4 2012

A3.17 Our Review of User Needs research also included qualitative research of residential consumers and businesses, published in August 2012 as *Postal User Needs Qualitative Research*. Key findings included that:

- both residential and business participants in the research stated that;
 - “they are increasingly substituting the postal service with electronic methods. Email, telephone, online document sharing and video calling are all being regularly used to meet core communication needs.”
- businesses;
 - “are increasingly automating key correspondence, invoicing, billing and marketing, and some businesses predict they will be doing more and more transactions online in the future, particularly due to higher demand for online shopping and fulfilment.”
- although a number of businesses, however;
 - “felt that they had ‘gone online’ as much as is possible, predicting that their future use of post would remain as it is now.”

- A3.18 This suggests that many businesses are already following established trends, by shifting communications from post to other formats.

Annex 4

Ipsos-MORI report on consumer research

- A4.1 In September 2012, Ofcom commissioned Ipsos-MORI to examine the behaviour and attitudes of low income and vulnerable consumers in relation to their use of universal postal services. The study was intended to provide a snapshot of vulnerable and low income consumers' experience of using postal services, in general and also at the Christmas period of peak demand, with the specific aim of exploring their views on the affordability of sending post and whether this is an issue for them.
- A4.2 This annex summarises Ipsos-MORI's approach and findings. We have also published Ipsos-MORI's full report on their research alongside this report.⁷³

Research objectives

- A4.3 The overall aims of the consumer research were to:
- understand all **usage of postal services** and behavioural patterns of vulnerable and low income groups of consumers, including how this may vary across the year (e.g. Christmas);
 - explore which services and usages may be considered by these groups as '**essential**' and assess the perceived impact of not being able to send something by post;
 - understand how **substitutable** usage of the post is with other forms of communication;
 - identify perceived and/or actual **barriers to usage** (if there are any) and how surrounding constraints might impact usage and attitudes towards the post;
 - explore what the potential **consequences or detriments** are (if any) of sending fewer items of post and/ or doing without other goods/ services in order to send post; and
 - inform Ofcom's understanding of what **affordability** means to these groups of consumers and how affordable they perceive postal services to be.

Consumer groups and participant sample

- A4.4 We set out in paragraph 3.22 in the main body of our report that, in assessing the affordability of universal postal services, we consider it important to consider the experiences of different consumer groups, particularly those more likely to be vulnerable.
- A4.5 Accordingly Ipsos-MORI consumer research explicitly included the following consumer groups:
- Low income consumers
 - Rural and very rural (mix of ages)

⁷³ <http://stakeholders.ofcom.org.uk/market-data-research/market-research/>

- Unemployed
- Old (65-74) and very old (75+)
- Recent immigrants
- Disabled
- Some with no internet

Approach

- A4.6 There is considerable experience of researching consumer issues around affordability, poverty and social exclusion. Lack of ability to send post (either due to cost or other reasons) for example can in principle contribute to social isolation and consumer detriment. To access research experience in this area and to help us in developing our method and approach to the consumer research undertaken by Ipsos-MORI, we engaged two academics specialising in empirical poverty research to advise us: Professor Glen Bramley (Heriot-Watt University) and Professor David Gordon (Centre for the Study of Poverty and Social Justice, University of Bristol).
- A4.7 As the research objectives were to explore consumer behaviour (how and why post is sent) and potentially sensitive topics of affordability, Ipsos-MORI took a qualitative approach using a combination of in-depth interviews, discussion groups and friendship pairs. Ipsos-MORI supplemented these with follow up telephone interviews in the first week of December to explore Christmas post usage and views.
- A4.8 Participants were asked to complete a task prior to the interview including writing down recollections of sending post and a five day diary of post sent. This aimed to encourage participants to think about when, how and why they send post. The interviews and discussion groups were guided by a facilitator and structured around a discussion guide aimed at exploring the research objectives. Views were particularly sought regarding the actual experiences of participants rather than views about how others might hypothetically be affected by the affordability of universal postal services. Participants were also asked for their views on the following two definitions of ‘affordability’:
- i) A postal product e.g. a First Class stamp would be unaffordable if I frequently had difficulty finding the money to pay for it;
 - ii) A postal product e.g. a First Class stamp would be unaffordable if I frequently had to give something else up in order to pay for it.
- A4.9 Ipsos-MORI undertook fieldwork during October and November 2012, with follow up telephone interviews in the first week of December. Table 14 summarises the participant sample, methods and interview approach. Full details are given in the Ipsos-MORI report published alongside this report.

Table 14: Key elements of Ipsos-MORI market research

Participant sample	Method	Interview approach
Participants were low income groups of consumers and other key vulnerable groups: <ul style="list-style-type: none"> • Disabled • Old (65-74) and very old (75+) • Unemployed • Rural and very rural (mix of ages) 	Ipsos-MORI undertook fieldwork in October and November 2012: <ul style="list-style-type: none"> • 25 Depth interviews (¾ hour to 1 hour each) • 10 Friendship pairs (1 hour each) 	Ipsos-MORI recruited and elicited views from respondents as follows: <ul style="list-style-type: none"> • Screening questionnaire designed to select low income and other vulnerable group participants • Each participant asked to

<ul style="list-style-type: none"> • Recent immigrants • Some with no internet access <p>In a mix of rural, suburban, urban locations:</p> <ul style="list-style-type: none"> • England: Devon (rural), Norwich, London • Northern Ireland: Belfast (suburban) • Scotland: Aberdeenshire (rural), Glasgow (suburban) • Wales: Swansea 	<ul style="list-style-type: none"> • Focus groups (2 hours each) supplemented in early December 2012 with: • Telephone interviews on Christmas posting behaviour (15 minutes each) <p>There were 110 respondents in total.</p>	<p>complete a pre-interview task concerning recollections of postal use, and a 5 day diary of post sent</p> <ul style="list-style-type: none"> • Depth interview, friendship pair and focus group discussions guided by Group discussion guide • Telephone interviews guided by Topic guide
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Main findings

A4.10 We summarise here Ipsos-MORI's main research findings.

Overall view and perceptions of post

A4.11 As for most consumers, vulnerable consumers' views and awareness of the postal service and sending post are varied. Consumers' use of post and their choice of postal service (e.g. use of First Class instead of Second Class stamps) are often determined by habit or not driven by conscious or fully rationalised knowledge or decisions of their relative merits. Awareness and knowledge of postal services can be quite low, e.g. there is a low awareness of the price of stamps, or the differences between Special Delivery and Signed For services.

Vulnerable consumers' use of post and how this is changing

- A4.12 Low income and vulnerable consumers report that they send post in a variety of ways and for a variety of reasons, reflecting their individual and family circumstances. Those aged over 65 for example tend to send more post than others to family and friends, and recent immigrants to the UK tend to use international mail more, to send letters, small packets and parcels.
- A4.13 In line with wider consumer trends, vulnerable and low income consumers' use of or reliance on the post is beginning to reduce or change. Younger people (on low incomes) in particular report limited reliance on post for maintaining social relations since they tend to use mobile phones or other digital media. Increased online trading by this group means that sending of parcels and packets has increased. Older people (those aged over 65) retain a high but decreasing reliance on post for maintaining social relations, and tend to have a higher reliance on post for official purposes.
- A4.14 Ipsos-MORI found that changing use of post means that many vulnerable and low income consumers participating in the research send items by post infrequently and do not rely on post enough for access or cost to be a key consideration.

'Essential' and 'non-essential' post

- A4.15 In probing respondents' views about use of post and affordability, Ipsos-MORI found that respondents' views on post items could be classified in terms of whether items of post were 'essential' or 'non-essential' to the respondent, with two variants on 'essential', so giving three broad types of post item:

'Essential'	'Type 1'	Items which a consumer is prompted or required to send by post because of official or commercial requirements	E.g. sending original documents
	'Type 2'	Items which a consumer is prompted or required to send by post because of social or family commitments or convention	E.g. letters/ cards to family and friends
'Non-essential'	'Type 3'	Items which the consumer could easily choose not to send by post either because he or she is happy with a cheaper or more convenient alternative or because not sending the post would not cause inconvenience or upset to the sender or recipients	E.g. Christmas cards to people never seen or not close to

- A4.16 It is important to stress that the type is chosen by the consumer in question; so an item considered 'essential' by one consumer may be considered 'non-essential' by another. Ipsos-MORI found that 'Type 1' use was very infrequent for most research participants. They also found that perceptions about what falls into 'Type 2' differed and were usually a reflection of an individual's personal and social life, with the types of correspondence they value the most seen as the most essential.
- A4.17 Vulnerable and low income consumers felt it was important that they were able to send both types of 'essential' post.

Managing and coping strategies

- A4.18 Ipsos-MORI found that respondents dealt with or managed the costs of post in a number of ways. Some respondents for example noted that their usage of post was too infrequent to be accounted for in their monthly budget plans and that spend of this kind came from a 'reserve pot' of money kept aside for unplanned expenditures.
- A4.19 More broadly, Ipsos-MORI found that "*most low income and vulnerable consumers had their own ways of managing postage costs, which had typically developed over several years rather than being a direct response to recent price rises.*" Ipsos-MORI reported that three broad types of coping strategy emerged:
- adjusting the item being sent;
 - becoming less reliant on post altogether; and
 - switching to another Royal Mail service or provider for those familiar with these alternatives.
- A4.20 Ipsos-MORI stressed that it was important to bear in mind that "*consumers did not always articulate that they were making these changes to their behaviour because they could not afford postal services. Often they were shifting their habits because alternatives appealed more or were perceived as better value for money, irrespective of whether post was affordable for them.*"

Sending of post at Christmas

- A4.21 Ipsos-MORI's telephone interview follow ups explored sending of post by low income and vulnerable consumers at Christmas. This found that Christmas is a special case for many, in that it is important for them to send Christmas post and parcels. For many of these consumers, it is the one time of year when they become more reliant on post and more aware of postage costs. Ipsos-MORI found that though some vulnerable and low income consumers may be frustrated by the cost of sending post, "*it did not have a notable impact on their usage, usually because they were not sending enough at Christmas time for it to be an issue.*"
- A4.22 Some consumers described ways of managing the cost of post at Christmas. Sending fewer cards was the most common example, though Ipsos-MORI noted that, "*while cost was a factor for some, this reduction was usually tied up with other considerations linked to the wider changes in how Christmas is celebrated... such as increasing reliance on technology.*" Other examples included planning ahead e.g. by buying books of stamps in advance, or using Second Class post even where they would more usually use First Class.

Value for money versus affordability

- A4.23 In discussing prices and 'affordability', Ipsos-MORI paid attention to identifying and probing separately views that were more concerned with 'value for money' from those more linked to 'affordability'. Ipsos-MORI in particular noted that the economic downturn led to participants questioning costs of products and services and wanting to maximise value for money, with "*post being another example of how everything is getting more expensive.*"

A4.24 Ipsos-MORI found that, while affordability was not seen as a concern, cost and value for money were. Ipsos-MORI characterised value for money concerns in two main ways:

“i) Relative to the value or size of the item being sent, particularly for larger spend items (parcels or international mail). Vulnerable consumers will often make a judgement about whether the cost is proportionate to the value of sending an item and may make adjustments to what or how they send something as a result. Our findings were that most respondents in this situation chose to implement their decision to post the item.

ii) Relative to the level of service that they perceive the post offers them. Vulnerable consumers will, similar to residential consumers more generally, make a judgement on this based on the level of service they perceive the post offers them.”

A4.25 That is, consumers may take a view on whether or not it is worth sending an item of post based on their perception of whether it offers value for money, rather than because they perceive it to be affordable or not affordable.

Definitions of affordability

A4.26 With a view to triggering participant opinions and thoughts about the affordability of sending post, Ipsos-MORI directly probed and tested participants' understanding of the concept of affordability by seeking views on the following two definitions of affordability:

- i) a postal product, e.g. a First Class stamp, would be unaffordable if I frequently had difficulty finding the money to pay for it; and
- ii) a postal product, e.g. a First Class stamp, would be unaffordable if I frequently had to give something else up in order to pay for it.

A4.27 Ipsos-MORI noted that the majority of participants considered the first definition to be better in terms of the general concept of something being 'unaffordable'. For example, participants said it implied a person already in substantial financial difficulty who would struggle to pay for basic items. To this extent participants said they thought this definition was not appropriate in the context of postal services. Participants tended to view the second definition in opposite terms, i.e. that it was more relevant for post since it better reflected how they managed their budget and made decisions about post, but less relevant for defining something as being unaffordable in general terms.

A4.28 Ipsos-MORI found overall during these discussions on the concept of affordability that consumers' *“limited reliance on postal services for sending post and the relatively small cost of most postal products meant that this concept was not usually considered relevant, even by those on very low incomes”*.