
Review of postal users' needs

An assessment of whether the minimum requirements of the universal postal service reflect the reasonable needs of the users of postal services in the United Kingdom

[Review of postal users' needs](#) – Welsh overview

Contents

Section

1. Overview	1
2. Introduction and background	5
3. Market and USO context	10
4. Overview of user research findings	23
5. Delivery frequency	41
6. Speed of delivery, quality of service, tracking and additional services	65

Annex

A1. International context and experiences	83
A2. Legal Framework	92
A3. Market research methodology	96
A4. Estimating impacts on user benefits	98
A5. Cost methodology	109
A6. Revenue methodology	126
A7. Glossary	132

1. Overview

Ofcom has undertaken a comprehensive review of the needs of postal users across the UK, to see if the requirements placed on Royal Mail reflect what people and businesses need today. We have looked in detail at how satisfied people and small businesses are with the current postal service, and what alternatives would meet their needs. This document explains our findings.

The universal postal service is relied upon by millions of people and businesses across the UK. As the postal regulator, our goal is to make sure postal users benefit from a universal service that meets their needs. In doing so we also consider whether the service is sustainable and efficient.

The minimum requirements of the universal service are set out in legislation. These include requirements on Royal Mail to deliver letters six days a week and parcels five days a week, at an affordable and geographically uniform price to every address in the UK. These requirements can only be altered by Government and Parliament.

We last reviewed postal user needs in 2012/13. Since then, there have been significant developments in the postal market. Letter volumes have fallen by more than 25%, with 53% of residential users now sending one letter or fewer per month. At the same time, growth in online shopping has seen parcel volumes increase at an annual rate of around ten per cent. These trends have been accentuated by the Covid-19 pandemic.

We conducted our main research at the end of 2019. We subsequently carried out further research in summer 2020 to assess how far users' views may have changed as a result of the pandemic.

Our main research findings

Users value some of the minimum requirements of the universal postal service

Our research found strong support from both residential and SME users (people or small businesses sending or receiving letters or parcels) for some of the minimum requirements of the current universal postal service:

- Users value the simplicity of a universal service with the same service levels and prices across the UK.
- 67% of residential users and 69% of SMEs agreed with the universal service provider charging the same price to all, regardless of where the letter or parcel is sent to within the UK.
- Affordability is the most important feature for residential users.
- Delivery to the door for letters and parcels was highly valued (with the large majority objecting to alternatives such as delivery to centrally located secure lockers).

People's views on changing minimum requirements

Our research looked at users' views and attitudes to a range of hypothetical changes to the minimum requirements of the universal postal service.

Our main findings in relation to the number of delivery days in a week are:

- The current USO service levels, including the six days a week (Monday-Saturday) letter delivery requirement, meets the needs of 98% of residential users and 97% of SMEs in the UK.
- Reducing the letters service to five days a week (Monday to Friday), but leaving all other elements of the service unchanged, would still meet the needs of 97% of residential and SME users.
- We found very little variation in users' views on five-day letter delivery across the UK, including the four nations of the UK or how remote users' locations are. Variation by other characteristics such as age, disability or whether users had access to the internet was also very limited.
- However, reducing the frequency of letter delivery to three days a week would have a significantly larger impact on users, meeting around 62-78% of SMEs and 79-85% of residential users' needs.
- The evidence suggests reducing the frequency of letter deliveries requirement to five days a week would reflect users' reasonable needs. It would also potentially allow Royal Mail to make net cost savings of around £125-225m per year in 2022/23 terms, assuming Royal Mail is able to realise these savings by modifying its operational delivery model.
- Although this saving could make a material contribution to the longer-term sustainability of the universal postal service, it would not be sufficient alone. Sustaining the universal service depends on Royal Mail's successful implementation of its transformation plans and ability to operate a more efficient parcels network in future.
- For parcels, our research found 98% of residential users' needs were met by the current six-day (Monday – Saturday) service, and we found no change in this percentage for a five-day service.

People's views on changing other features of the universal service

Beyond the minimum requirements, other features of the universal postal service are specified in legislation and regulatory conditions set by Ofcom. Although this review focuses on the minimum requirements, our research also sought users' views on these other features, including on hypothetical changes to them:

- Replacing First Class with a single class service offering a two-day delivery speed (which would be slower than First Class mail but faster than Second Class currently) would not have a large impact on users' acceptability of the service. However, it would have limited scope for cost savings and would risk reduced revenues.
- Reducing the quality of service levels (the percentage of mail required to arrive in the time it should, such as 93% of First Class mail arriving the next day), where we found that users valued certainty and reliability. Participants felt they needed to know when an item would arrive and be assured that an item would arrive in good condition. We also found relatively limited cost savings from reducing quality of service levels.

Next steps

This review contains our assessment of whether the minimum requirements of the universal postal service reflect the reasonable needs of users of postal services. It would be for the UK Government to determine whether any changes are needed to the minimum requirements and to bring any proposals before Parliament.

As set out in our Plan of Work¹, we are undertaking a review of the future regulatory framework for post. This will consider issues affecting the broader postal sector as people's reliance on parcels continues to grow. This is separate to this assessment of user needs.

We will engage with stakeholders on a range of issues, including access regulation for letters, consumer issues in the parcels and letters markets, and how regulation can support a modern well-functioning parcels market that delivers benefits to end users. We intend to publish a call for inputs on these issues in Q4 2020/21.

¹ Ofcom, 2020. Ofcom Plan of Work 2020/21, September update.

https://www.ofcom.org.uk/_data/assets/pdf_file/0018/203724/pow-2020-21-sept-update.pdf

POSTAL USERS' NEEDS 2020

LETTER VOLUMES on average each year 2015-20
↓ 5%

Over two-thirds

of all postal users think Royal Mail should charge the same price regardless of where the letter or parcel is sent in the UK.



↑ 10% on average each year 2015-20
parcel volumes

six-day vs. five-day service

98% of residential users believe a six-day letter service meets their needs (SMEs 97%).

97% of all users needs are met by a five-day letter service.

Most important features

- Affordability
- Simplicity
- Certainty
- Reliability
- Universality

40% of users would feel cut off from society if they could not send or receive letters most days (parcels: 36%).

Older people would feel more cut off without letters. Younger and middle-aged people would feel more cut off without parcels.



Delivery to the door or a central locker

76% of residential users and 82% of SMEs are against delivery of letters to a central locker instead of to the door (64% and 77% against for parcels).



2. Introduction and background

- 2.1 Ofcom is the regulator of postal services in the UK. The Postal Services Act 2011 (“the Act”) provides that we must carry out our functions in relation to postal services in a way that we consider will secure the provision of a universal postal service, having regard to its financial sustainability and efficiency.²
- 2.2 The key characteristics of the universal service are called the ‘minimum requirements’ and are set in the Act. They include the provision of a service at affordable and uniform prices, and the collection and delivery of mail everywhere in the UK every weekday (and on Saturdays for letters). These minimum requirements are set by the UK Parliament. Other features of the universal service are set by Ofcom in the Universal Postal Service Order (“the Order”).³ For example, the requirement to offer First Class services that take one working day from collection to delivery anywhere in the UK is set in the Order, which Ofcom could decide to amend following a review of users’ reasonable needs.

The nature of this report

- 2.3 We last conducted a review of users’ needs in 2012-13. Since our last review, increasing use of digital communications and online shopping has resulted in declining letter volumes and increasing parcel volumes. To reflect these evolving market conditions, we have updated our understanding of the current needs of users, how these might have changed over time and how these might change in the future.
- 2.4 While Ofcom does not have the power to change the minimum requirements in the Act, we do have a role in reviewing the extent to which these requirements reflect the reasonable needs of postal users. This document contains our review. As is required under Section 34 of the Act, we have provided a copy of this review to the Secretary of State for Business, Energy and Industrial Strategy (BEIS). It is for the UK Government to determine whether any changes are needed to the minimum requirements and to bring any proposals before Parliament.
- 2.5 Under Section 30 of the Act, Ofcom can amend the Order if we consider that necessary following an assessment of the extent to which the market for the provision of postal services in the UK is meeting the reasonable needs of the users of those services. While this document explains the findings of our research in relation to other features of the universal service (e.g. speed of delivery and quality of service), which are set in the Order and regulatory conditions, we are not making any proposals to modify the Order or regulatory conditions in this document.

² Section 29(1) and (3) of the Act. <https://www.legislation.gov.uk/ukpga/2011/5/contents>

³ The Postal Services (Universal Postal Service) Order 2012 (SI 2012/936).
http://www.legislation.gov.uk/uksi/2012/936/pdfs/uksi_20120936_en.pdf.

The current universal service

- 2.6 The Universal Service Obligation (USO) requires the designated universal service provider, Royal Mail, to deliver a range of postal services to homes and businesses. The services to be provided include the minimum requirements set in the Act, and further services specified in the Order.
- 2.7 Section 31 of the Act sets out the key characteristics which must be included, as a minimum, in the universal postal service in the UK. These minimum requirements, in summary, comprise of:
- At least one delivery of letters⁴ every Monday to Saturday, and at least one delivery of other postal packets every Monday to Friday;
 - At least one collection of letters every Monday to Saturday, and at least one collection of other postal packets every Monday to Friday;
 - A service of conveying postal packets from one place to another by post at affordable, geographically uniform prices throughout the UK;
 - A registered items service at affordable, geographically uniform prices throughout the UK;
 - An insured items service at affordable, geographically uniform prices throughout the UK;
 - The provision of certain free services to blind/partially sighted people; and
 - The free conveyance of certain legislative petitions and addresses.
- 2.8 Section 30(1) of the Act requires Ofcom to make an Order setting out a description of the services that we consider should be provided in the UK as part of the universal postal service and the standards with which those services must comply.
- 2.9 Royal Mail is the designated provider of the Universal Postal Service (UPS). This means that, under the Act, Ofcom can impose Designated Universal Service Provider (DUSP) conditions on Royal Mail. These conditions specify in greater detail the services that must be provided as part of the universal postal service. For instance, they include quality of service standards that Royal Mail must meet in respect of each of the specified services and require Royal Mail to notify and publish certain information, including delivery and collection times.
- 2.10 While providing USO services is a central part of Royal Mail's business, the majority of volumes and revenues come from its non-USO services.⁵ Non-USO Royal Mail products include: bulk and tracked parcel services, some same day services, advertising mail, business mail, among many others. Unlike USO services, these services are subject to VAT.
- 2.11 For example, banks, large businesses and public sector organisations sending large volumes of letters use bulk mail services offered by Royal Mail and other postal operators. For the most part, they do not use services which Royal Mail offers to meet its USO obligations.

⁴ The term 'letter' is defined in section 65(1) of the Act.

⁵ Ofcom, 2020. Annual monitoring update on the postal market: Financial year 2019-20,

https://www.ofcom.org.uk/_data/assets/pdf_file/0022/208219/2019-20-annual-monitoring-update-postal-market.pdf.

Meanwhile, a large proportion of parcels are not delivered by Royal Mail. The market for parcel delivery from businesses to consumers is more competitive, with a number of parcel operators providing these bulk services to online retailers. The services that Royal Mail provides to retailers for these purposes are not part of the USO.⁶

Our research on users' reasonable needs

- 2.12 To understand the needs of users of postal services, we have carried out a number of activities, including:
- **Residential and SME user research:** we commissioned Jigsaw Research to undertake a major programme of qualitative and quantitative research on our behalf among residential and SME users throughout the UK. We also undertook further research in summer 2020 to understand more about how the Covid-19 crisis may have impacted users' perspectives and behaviour.⁷
 - **Considering the potential effects of different changes to the USO:** we have looked at some of the potential costs and benefits associated with a number of possible changes to the universal service. This includes assessing the impact of potential changes on Royal Mail as well as users.
 - **Building our understanding of the market:** we have engaged with Royal Mail and other UK letters and parcels operators. We have also engaged with large postal users (e.g. banks, utilities and public sector organisations) to ensure that we have understood the potential impacts of any changes to the universal service on their use of mainly non-USO services.⁸
 - **International engagement:** we have spoken to national regulatory authorities from countries that have undertaken, or are in the process of completing, a review of users' needs. This engagement has helped to inform our review.

Our approach to reviewing users' reasonable needs

- 2.13 Our analysis considers the extent to which the minimum requirements of the universal service – or possible changes to those requirements – reflect the reasonable needs of postal service users. To help inform this we look at whether the additional benefits of a service to users exceed the additional costs of supporting that service. Therefore, we have considered the potential effect that changes to the minimum requirements may have on users, society as a whole, and Royal Mail (as provider of the universal service).

⁶ In the sub-2kg parcels market, Royal Mail is the dominant provider with 80-90% of the market share in terms of both volumes and revenues as of 2017/18. Source: Ofcom, 2019. Review of the Second Class Safeguard Caps 2019. https://www.ofcom.org.uk/_data/assets/pdf_file/0019/133660/Statement-Review-of-the-Second-Class-safeguard-caps-2019.pdf

⁷ For more detail on our research, see Section 4, Overview of our research findings; and Annex 3, Market research approach and reports. Our research covered both minimum requirement and non-minimum requirement elements of the current universal service. We consider findings on the latter provide helpful context for this review of minimum requirements.

⁸ For more detail on our market monitoring and stakeholder engagement, see Section 3, Market and USO context; and Section 6, Speed of delivery, quality of service, tracking and additional services.

- 2.14 We have carried out extensive market research to understand how important aspects of the current USO are to users, so that we can best understand what users, and society more broadly, need from the postal service. This included testing views on changes to the minimum requirements and other features of the service. We use this range of evidence from our market research to understand whether the minimum requirements – or possible changes to those requirements – reflect the reasonable needs of users.
- 2.15 We have also considered possible impacts of changes to the minimum requirements, and other features of the service, on the cost of providing the service and the revenue it generates. To do this, we have:
- used cost modelling to estimate the impact of changes in service on Royal Mail’s operational costs, as well as qualitatively considered potential one-off transitional costs that could be incurred in implementing changes; and
 - modelled potential impacts on Royal Mail’s revenues, by considering how user behaviour might change in response to changes in service.
- 2.16 While we have considered users’ reasonable needs in relation to all the minimum requirements, we have focused our analysis on the number of days of letter delivery required a week to homes and businesses. This is because we consider that the number of delivery days a week for letters is fundamental to users’ experience of high volume USO services, such as First Class and Second Class. Further, it is delivery (rather than collection) that makes up the largest proportion of Royal Mail’s costs of providing these services.
- 2.17 Other services which Royal Mail provides in order to meet minimum requirements, such as Special Delivery Next Day (Guaranteed by 1pm) and Signed For, and the free services (articles for the blind and legislative petitions and addresses) are lower in volume and comprise a smaller proportion of overall costs. Section 6 includes the findings of our market research in relation to these additional services, but these services are not the focus of this report.

The structure of this document

- 2.18 The rest of this document is structured as follows:
- **Section 3. Market and USO context:** summarises the wider market and USO context for our review, including outlining the changes to the UK’s postal market since our last review.
 - **Section 4. Overview of user research findings:** details the findings in regard to users’ views on sending and receiving letters and parcels as well as core characteristics of the universal service, such as uniform pricing across the UK and delivery to the door.
 - **Section 5. Delivery frequency:** this section details our assessment of the impact of a change in delivery frequency of letters (both five and three days) and parcels on user needs.
 - **Section 6. Speed of delivery, quality of service, tracking and additional services:** details our research findings on these additional features of the universal service, to provide further context for this review.

- **Annex 1. International context and experiences:** outlines assessments of changes to universal service obligations in other countries and includes case studies to provide greater context to this review.
- **Annex 2. Legal framework:** details the legal framework supporting our review of the minimum requirements.
- **Annex 3. Market research methodology:** summarises our market research methodology. We have separately published the qualitative, quantitative research reports and Covid-19 bespoke research slide pack from Jigsaw Research.
- **Annex 4. Estimating impacts on user benefits:** explains our approach to estimating the impact of potential alternative USO specifications on user benefits.
- **Annex 5. Cost methodology:** explains our approach to modelling the costs of Royal Mail's operations and assessing how alternative USO specifications could affect these costs.
- **Annex 6. Revenue methodology:** explains our approach to modelling the potential impact of alternative USO specifications on Royal Mail's volumes and revenue.

3. Market and USO context

Introduction

- 3.1 This section provides the market context for our review of postal users' needs. It explores the postal services market, particularly how letter and parcel volumes have changed in recent years, and the impact of recent events upon Royal Mail and the USO. We also provide an overview of Royal Mail's services, and its delivery network.
- 3.2 Since our last review of the users' needs in 2013, the UK postal service market has undergone significant change. Letter volumes and revenue have declined, driven by increasing digitalisation and e-substitution. In contrast, parcel volumes and revenue have grown steadily, driven by the rise of online shopping.
- 3.3 These trends have accelerated in 2020, in the immediate aftermath of the Covid-19 pandemic, which has had an impact on Royal Mail and other postal operators.

Overview of the letters market

- 3.4 The letters⁹ market consists of three main parts:
- 'Single piece' end-to-end services (mainly USO services): single letters (e.g. birthday cards) sent by individuals or SMEs using a post box or a post office, which are collected and delivered by Royal Mail;
 - Business retail end-to-end services (non-USO): where Royal Mail collects bulk volumes of mail directly from larger businesses (or other organisations) and adds it to its network for sortation, distribution and delivery; and
 - Business access mail services (non-USO): where competing access operators collect bulk volumes of mail from larger businesses (such as banks or insurance companies), public sector and voluntary organisations, transport it across the UK and insert it into Royal Mail's network for delivery.
- 3.5 Royal Mail is the only major provider of single piece letter services, which are mainly (but not exclusively) USO services. It provides a range of USO letter services, including First Class, Second Class and Special Delivery Next Day (Guaranteed by 1pm). There is no significant competition in single piece letters, either from end-to-end competitors or access operators (who focus on serving bulk mail business customers). Users of single piece letter services therefore continue to rely almost exclusively on Royal Mail to provide them with collection and delivery of letters as part of the universal service.
- 3.6 In addition to stamps (which can be bought in post offices, other retailers and online) as a method of payment for sending USO letters, Royal Mail offers metered or franked mail as an in-house postage and payment option. This allows businesses and other organisations to buy or lease franking machines that print the post mark directly onto letters (or to a

⁹ Including large letters.

lesser extent, parcels). Royal Mail offers metered mail services at discounted prices relative to regular stamped services, within the USO.

- 3.7 Meanwhile, some access operators as well as Royal Mail, offer ‘hybrid’ (or digital) mail services¹⁰ to businesses and organisations with lower volume needs, which may offer an alternative market option to franking machines for some mailings.
- 3.8 Beyond single piece end-to-end services, Royal Mail also provides a range of ‘non-USO’ bulk retail end-to-end letter services to businesses, such as business or advertising mail products.

Access mail

- 3.9 In contrast to single piece end-to-end letters, where Royal Mail accounts for almost all volumes, business bulk mail is more competitive. A range of access operators collect and distribute mail from business customers and then take it to Royal Mail sites for inclusion with other mail in their network for delivery.
- 3.10 To support this competition, Royal Mail is subject to a regulatory condition requiring it to offer access services at its mail centres (see Figure 8, below) to other postal operators and large customers for certain letters services. This enables other operators to offer postal services to their customers (normally large businesses) for these formats without setting up a delivery network.
- 3.11 Our regulation has helped ensure that alternative options are available to business senders of bulk mail. Access mail is the largest part of the letters market in the UK, accounting for 63% of all letter volumes in 2019-20.¹¹
- 3.12 Sales of non-USO products¹² and services underpin the majority of Royal Mail’s Reported Business¹³ revenue — £4.3bn in 2019-20, or around two-thirds of Royal Mail’s Reported Business revenue — and are delivered jointly over the same network as USO products.¹⁴

Trends in the letters market

- 3.13 With almost 10 billion addressed letters sent in 2019-20, the letters market is still significant despite the fall in volumes as customers move to digital communications.

¹⁰ This involves electronic copies of mailings being sent by the sender to the access operator, to be printed, produced and enveloped at a common print facility. This removes the need for the operator to incur the costs of collecting small volumes of letters from the business sites of multiple customers, while still allowing the sender to benefit from lower prices than stamps.

¹¹ Ofcom, 2020. Annual monitoring update on the postal market: Financial year 2019-20, https://www.ofcom.org.uk/data/assets/pdf_file/0022/208219/2019-20-annual-monitoring-update-postal-market.pdf.

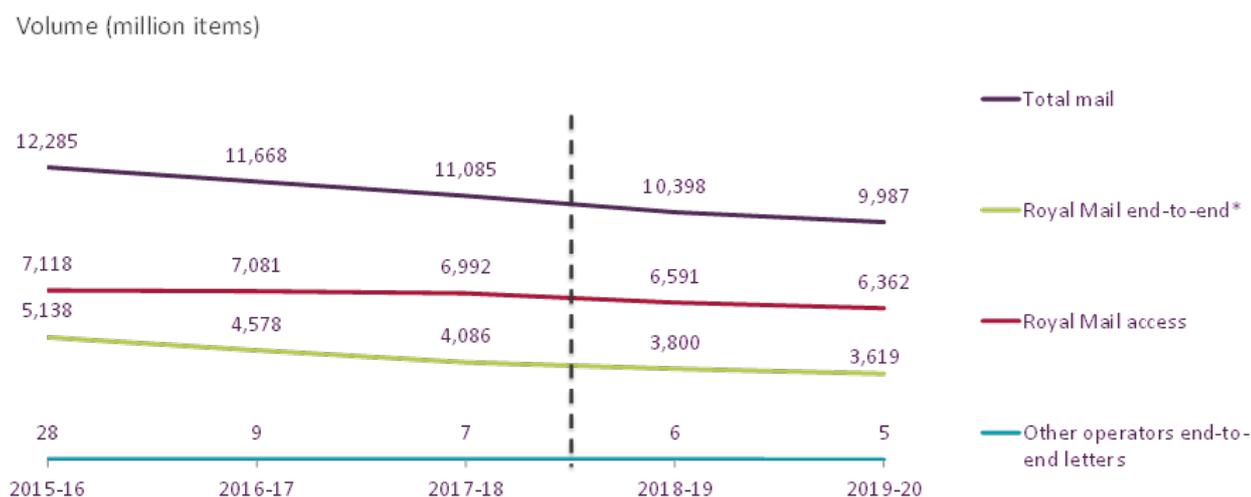
¹² Including access, bulk, international and unaddressed letters and parcels, and non-volume services.

¹³ The Reported Business is the regulated entity, defined by Ofcom, which delivers the USO. The services within the Reported Business include all universal service products and other ‘non-USO’ products which use the universal service network (for example, retail bulk mail and access).

¹⁴ Ofcom, 2020. Annual monitoring update on the postal market: Financial year 2019-20.

3.14 Royal Mail’s addressed letter volumes (excluding elections) fell by 7.6% in 2019-20, even before the Covid-19 pandemic had a significant impact in the UK.¹⁵ Meanwhile, inland addressed letter volumes (total end-to-end and access) fell by 3.9%, from £10.4bn in 2018-19 to £10.0bn in 2019-20, as shown in Figure 1.

Figure 1: Addressed letter volumes (m), 2015-16 to 2019-20¹⁶



Source: Ofcom Annual monitoring update on the postal market: Financial year 2019-20 data. Operator returns, Ofcom estimates. NB: 2018-19 Royal Mail data restated to reflect updated methodology. It is not possible to make direct comparisons between pre-and post-2018-19 on the data in the chart. The effect of the change in methodology has been to increase reported Royal Mail end-to-end letters volumes.¹⁷

*Royal Mail end-to-end is an Ofcom calculation and refers to Royal Mail total letters, excepting access. Figures exclude international. Access volumes include small volume of access parcels.

3.15 Royal Mail’s addressed letters revenue, including Royal Mail end-to-end and Royal Mail Access, has also declined by approximately 2% in real terms to £3.8bn in 2019-20.¹⁸ This decline in revenues has been less pronounced than the decline in volumes, partly due to the increased pricing flexibility Royal Mail has had since 2012.¹⁹

¹⁵ Ofcom, 2020. Annual monitoring update on the postal market: Financial year 2019-20. It is worth noting that the impact of Covid-19 in the UK was only significant in the final two weeks of the 2019-20 financial year.

¹⁶ In this graph, the total letters and large letters mail sector is broken into three parts: Royal Mail end-to-end (mail collected and delivered by Royal Mail, consisting of both bulk retail mail and single piece mail), Royal Mail access (mail collected by other operators and delivered by Royal Mail) and other operators’ end-to-end (mail collected and delivered by other operators).

¹⁷ For further details please see <https://www.royalmailgroup.com/media/10704/royal-mail-changes-in-external-reporting.pdf>

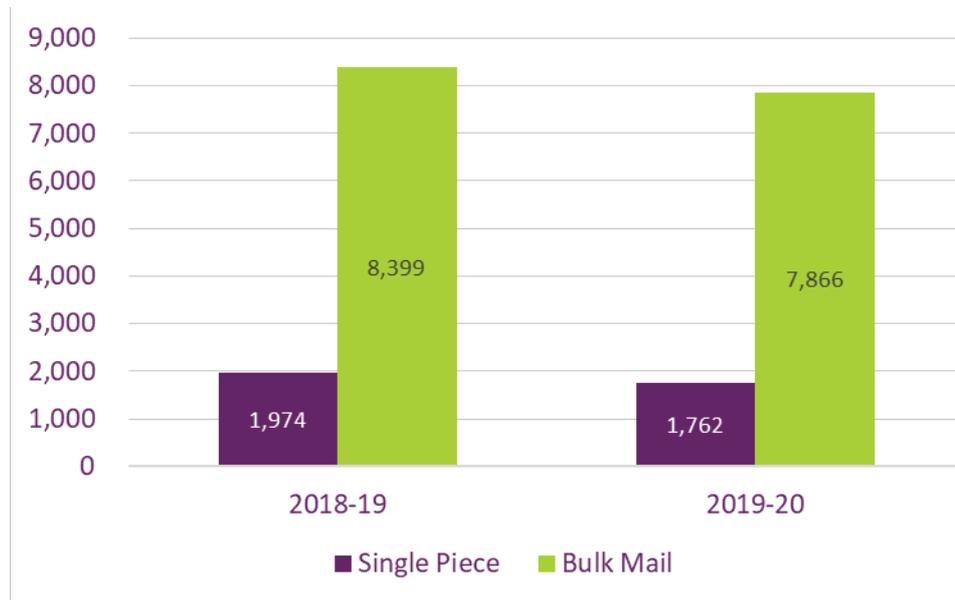
¹⁸ Ofcom, 2020. Annual monitoring update on the postal market: Financial year 2019-20.

¹⁹ In our 2012 Statement Securing the Universal Postal Service, we introduced a new regulatory framework that enhanced Royal Mail’s commercial freedom. We introduced safeguard caps on some core products (Second Class Letters, Large Letters and Second Class Parcels up to 2kg) but moved away from a price control based approach. This gave greater pricing flexibility to Royal Mail. Ofcom, 2012. Securing the Universal Postal Service.

https://www.ofcom.org.uk/_data/assets/pdf_file/0029/74279/Securing-the-Universal-Postal-Service-statement.pdf

3.16 As indicated in Figure 2, we estimate that single piece letter volumes²⁰ declined by 10.7% between 2018-19 and 2019-20. 2019-20 figures refer primarily to the pre-Covid-19 period.

Figure 2: Royal Mail single piece and bulk mail²¹ letter volumes (m)



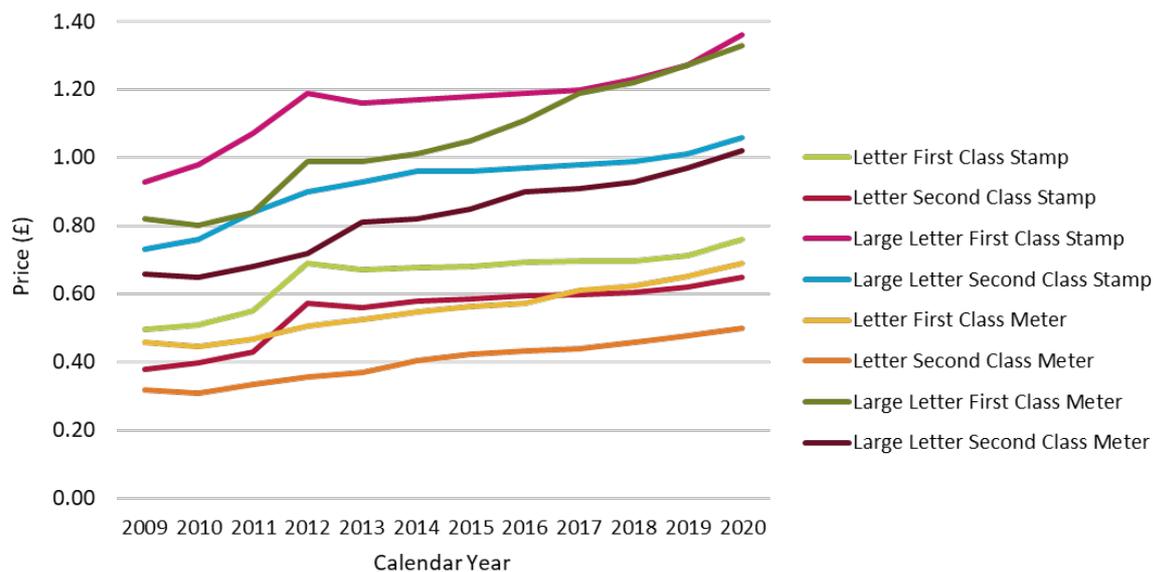
Source: Royal Mail 2018-19 and 2019-20 volumes report.

3.17 Stamps and mail meters are the primary methods of paying for USO letter postage. Since 2013 Royal Mail's prices for letters and large letters (both stamps and metered mail) have consistently risen, and First Class stamps have recently tracked 11p above Second Class stamp prices.

²⁰ Our estimates suggest that less than 1% of single piece letter volumes are non-USO products, so single piece letter volumes are virtually all USO letter volumes.

²¹ Consists of Royal Mail's end-to-end mail as well as access mail.

Figure 3: Royal Mail USO letter prices 2009 to 2020



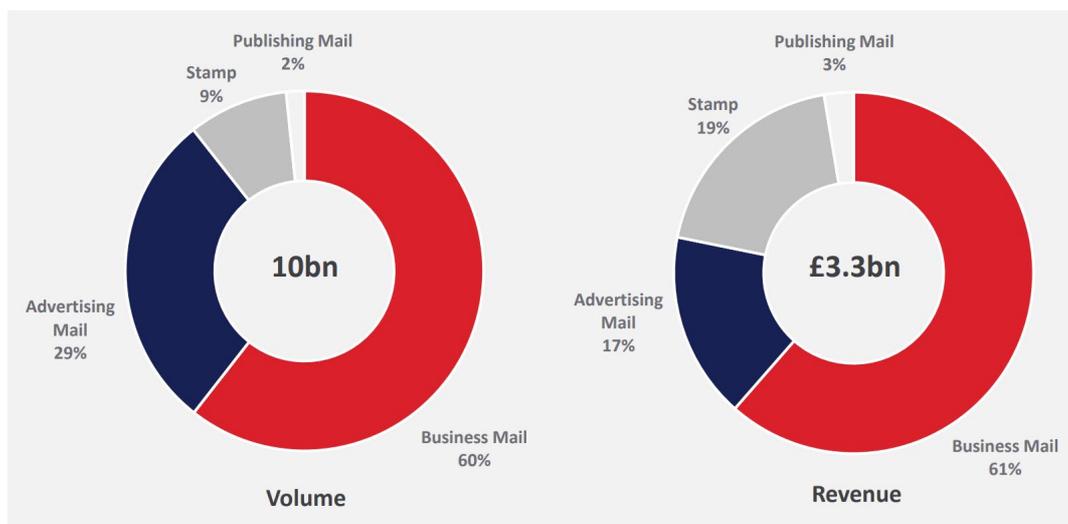
Source: Ofcom Annual monitoring update on the postal market: Financial year 2019-20 data.

- 3.18 Metered mail services account for [X]% of Royal Mail’s revenues for single piece domestic items. The total volume of metered mail was [X]m items in 2018/19. It has been declining by around [X]% per annum.²²
- 3.19 Non-USO letters make up most of both Royal Mail’s letter volumes and letter revenues.²³ As set out in Figure 4, below, a minority of Royal Mail’s addressed letter volumes and revenue is derived from stamped/single piece letters.

²² Ofcom analysis based on 2018/19 volumes and revenues data received from Royal Mail as part of its regulatory reporting requirements.

²³ Royal Mail, 2019. Journey 2024 presentation. <https://www.royalmailgroup.com/media/10705/fy-2018-19-results-and-strategy-presentation.pdf>

Figure 4: Royal Mail Addressed Mail, by product, volume and revenues²⁴



Source: Royal Mail, May 2019. Journey 2024 presentation.

3.20 The decline in the letters market is structural and the UK experience of declining letter volumes mirrors international trends (see Annex 1).

Parcels market

3.21 Under the USO Royal Mail must provide a collection and delivery service for single piece parcels²⁵ weighing up to 20kg, five days a week at affordable and uniform prices across the UK. It also offers other “non-USO” and bulk parcel services to businesses and residential consumers. There are a number of other parcel operators that provide end-to-end parcel services within the UK, including some single piece services.

3.22 Below, we provide an overview of the parcels market, before considering single piece parcel services within the consumer-to-business/consumer (C2X) segment of the market in more detail.

Overview of the parcels market

3.23 The UK parcels market is made up of the following segments:

- a) **Consumer-to-business/consumer (C2X):** deliveries of a single parcel sent by individual consumers or SMEs to another person or business (e.g. a person sending a birthday present to a relative, a consumer returning an item purchased from an online retailer²⁶, or an online marketplace seller fulfilling orders);

²⁴ Totals exclude elections, international and non-volume related products.

²⁵ Parcels for which the price per item is not discounted on the basis of volume, format or pre-sortation.

²⁶ Where the postage charge is covered by the online retailer, the return of items would be treated as B2C deliveries.

- b) **Business-to-consumer (B2C):** deliveries of items to end consumers made as part of bulk contracts agreed between businesses and parcel operators (e.g. an online retailer sending multiple items bought online by consumers);²⁷ and
- c) **Business-to-business (B2B):** mainly bulk deliveries of parcels between businesses (e.g. a car dealer with multiple sites receiving parts from a manufacturer).

3.24 Royal Mail provides services across all segments within the parcels market. In particular, it has a strong presence in the C2X segment, with its network initially being set up to provide single piece letters and parcel services. However, Royal Mail also provides extensive bulk parcel services, particularly within the B2C segment, which have grown rapidly with the growth in online shopping.²⁸ Single piece parcel volumes have remained broadly stable over the last couple of years, in contrast to the high growth of bulk parcel volumes. Royal Mail's focus on B2C services is likely to further develop as part of its transformation plan (see below).

Figure 5: Royal Mail single piece and bulk parcel volumes (m)

[✂]

Source: Royal Mail's 2018-19 and 2019-20 volumes report.

Single piece services

Royal Mail²⁹ is the leading provider of single piece parcel services in the UK

- 3.25 The UK parcels market consists of a number of operators, but most account for a very small share within the C2X segment. Royal Mail is by far the leading provider of single piece parcel services in the UK.
- 3.26 Within the USO, Royal Mail offers a next day (First Class) and standard (Second Class) 'untracked' delivery service for parcels weighing up to 20kg, and a Special Delivery Next Day (Guaranteed by 1pm) service, which incorporates tracking.³⁰ While, Royal Mail also provides Tracked 24 and 48 parcel services outside the USO,³¹ these services are not available at post offices and items can only be dropped off at Royal Mail delivery offices

²⁷ We provide more detail on B2C parcel services in the market developments section of our Annual monitoring update on the postal market: Financial year 2019-20.

²⁸ Office of National Statistics. Internet sales as a percentage of total retail sales (ratio) (%). <https://www.ons.gov.uk/businessindustryandtrade/retailindustry/timeseries/j4mc/drsi> [accessed 6 October 2020]. According to the ONS, internet sales accounted for 19.2% of total UK retail sales in 2019, up from 8.3% in 2016.

²⁹ In this sub-section, we make some references to Parcelforce. Parcelforce is part of the Royal Mail Group and it offers non-USO parcel services. It was created by Royal Mail as a separate function to handle some parcels. Royal Mail directs customers to Parcelforce's services if sending parcels that are heavier than 20kg.

³⁰ Royal Mail also offers Signed For as an add-on option to First Class and Second Class services, where the signature acts as proof of delivery. For pre-paid return items, the cost is 60p.

³¹ Similarly, Parcelforce provides a tracked service at all weight steps.

that have designated customer service points³² (or since October 2020, directly collected at an additional charge).³³

- 3.27 As of 2018/19, we estimate Royal Mail's share of single piece parcel deliveries was greater than 70% in terms of volumes.³⁴ The next closest competitor was Hermes which accounted for approximately 10-20% of volumes. This was followed by Yodel with less than 5% of total volumes and all other operators (which individually contributed to a negligible share of single piece parcel deliveries).³⁵

Some alternative operators offer single piece services at competitive prices relative to Royal Mail

- 3.28 While other parcels operators tend to focus more on B2C and/or B2B parcel services, some of them also offer next day and standard services to individual consumers. These services are available for purchase through operators' websites with home collections sometimes an option and/or drop-off at access points (e.g. parcel shops). The products offered by alternative operators all include tracking, which often encompasses additional features (e.g. 'inflight' delivery options³⁶).
- 3.29 In Figure 6 below, we illustrate the next day delivery prices of Hermes, Yodel and DPD (as the lowest priced alternative operators to Royal Mail). Alternative operators price competitively relative to Royal Mail's untracked and tracked prices for next day delivery services at certain weight steps. In particular, for the smaller volume of parcels weighing above 2kg, the gap between Royal Mail's prices and that of competitors widens, as competitors offer much lower prices.³⁷ We have observed that Royal Mail's share is lower in this part of the market.

³² Items can also be dropped off at parcel postboxes if weight/dimension requirements are met and the sender does not require proof of postage.

³³ In October 2020, Royal Mail launched a new Parcel Collect service, offering parcel collection directly from people's homes. The service operates six days a week (Sundays excluded) at a charge of 72p per parcel collection, plus delivery costs. For pre-paid return items, the cost is 60p.

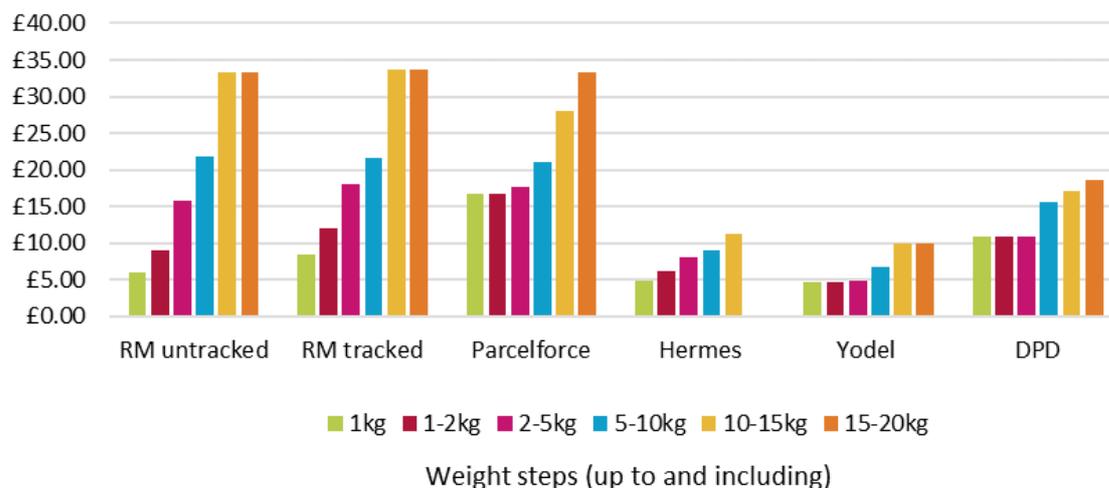
³⁴ These figures are inclusive of Parcelforce. Ofcom analysis based on Annual monitoring update on the postal market: 2018-19 data. We calculate these figures by using single piece service shares as a proxy for C2X service shares. Some operators were unable to accurately distinguish between their bulk and single piece parcels. Therefore, these figures should be treated as an approximation only.

³⁵ This includes volumes handled via Collect+. Yodel offers C2X services via the Collect+ service which is owned by PayPoint and provides store-based parcel delivery services. The other remaining operators are TNT/FedEx, DPD and DHL/UK Mail.

³⁶ A feature that allows customers to change their delivery options (e.g. re-direct parcels), while the parcel is inflight/in the process of being delivered. In June 2020, Royal Mail launched its own inflight redirections service, which is available with their Tracked 24, Tracked 48 and Special Delivery Next Day Guaranteed services.

³⁷ We also observe this when comparing prices for standard (Second Class) services. For Second Class services, a safeguard cap applies to parcels weighing up to 2kg, but Royal Mail has tended to leave considerable headroom between its pricing and the safeguard cap on Second Class parcels. As part of Ofcom's 2019 Review of Second Class Safeguard Caps, we concluded that Royal Mail should continue to be subject to our second class safeguard cap for parcels weighing up to 2kg, due to having a significant degree of pricing power. Ofcom, 2019. Review of the Second Class Safeguard Caps 2019.

Figure 6: Single piece parcel prices³⁸ for next day deliveries



Source: Ofcom desk-based research as of June 2020.

Royal Mail is the only provider of single piece parcels offering a universal service

3.30 Royal Mail’s universal provision of single piece parcel services, at the same price, across the UK, is a core part of the current USO. While some operators provide UK-wide single piece parcel services, there are geographic limitations to the services, prices and ease of access offered by alternative operators.³⁹

Service restrictions

3.31 Alternative operators impose some delivery restrictions on next day services in some locations, and certain postcode areas in the UK are not served on a next day basis by all of these operators.⁴⁰ Next day delivery variations are particularly prevalent in Northern Ireland, the Scottish Highlands and Islands, and other islands.

Geographic pricing

3.32 Alternative operators sometimes add geographic ‘surcharges’ to their standard C2X prices for deliveries to, and collections from, some locations on both their standard and next day services. For example, Hermes applies a flat rate additional charge of £2.00 when sending parcels to or from remote postcode areas in the Shetland Islands, Hebrides and the Isle of Man.⁴¹

³⁸ Prices are inclusive of VAT and shown for medium parcels as defined by Royal Mail (Length: 61cm, Width: 46cm and Depth: 46cm). Royal Mail’s Tracked 24 and 48 services are only available for purchase online. DPD’s next day price covers collection and delivery from/to the door, whereas the prices of all other operators include a drop-off and delivery to the door service (although Royal Mail, Hermes and Yodel do provide the option of collections at an additional charge).

³⁹ For information on geographic variations in B2C parcel delivery services, see the market developments section of our Annual monitoring update on the postal market: Financial year 2019-20.

⁴⁰ A small number of these postcode areas are also exempt from elements of the First Class quality of service delivery targets we impose on Royal Mail. Some postcode areas may not be logistically practical to fully serve on a next day basis by any operator.

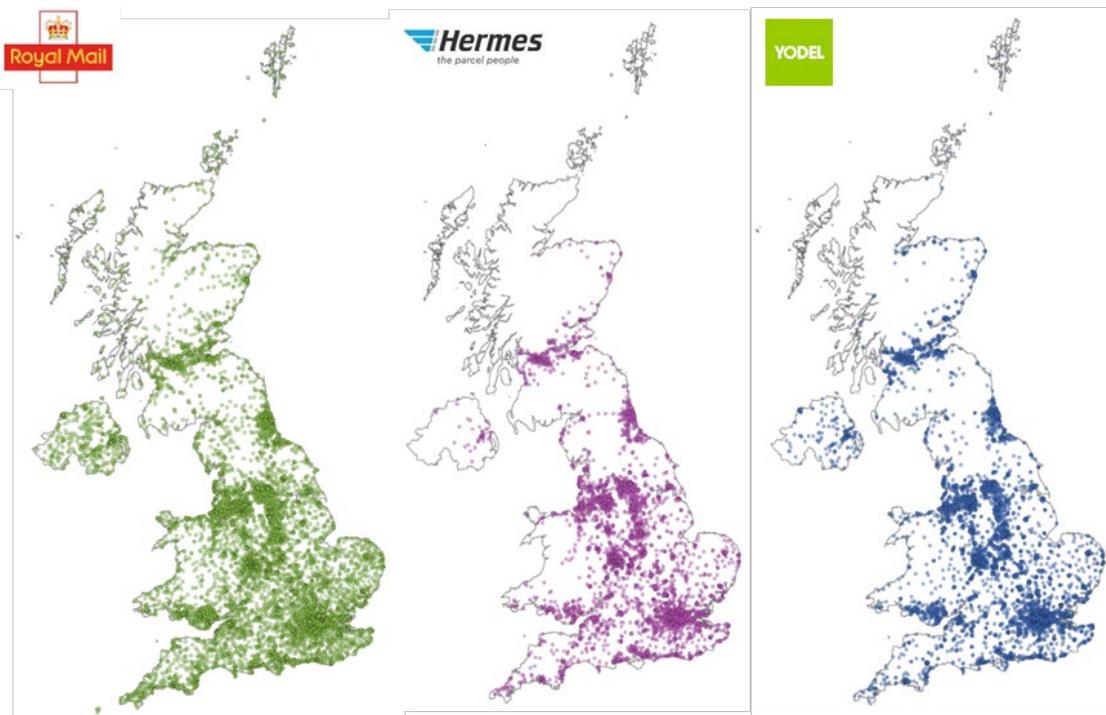
⁴¹ This applies to both home and parcel shop deliveries/collections. Ofcom analysis based on information provided by Hermes on 6 December 2019 in response to our s.55 information request.

Availability of access points

3.33 Post offices offer an extensive network of access points for Royal Mail's parcel services (11,600 post offices) across all parts of the UK. We calculate that 90% of premises⁴² have access to a post office within two miles. In comparison, Hermes had 4,500 access points (parcel shops) and Yodel had 7,100 access points (Collect+ stores) as of 2019,⁴³ which we estimate 76% and 79% of premises have access to within two miles, respectively.⁴⁴

3.34 Figure 7 below illustrates the geographic coverage of Royal Mail, Hermes and Yodel in terms of their access points across the UK. Although Hermes and Yodel have a large number of access points, Royal Mail provides a much denser network, covering both urban and rural areas across the whole of the UK.

Figure 7: Network of access points for single piece operators in 2019



Source: Ofcom analysis based on information provided by Hermes and Yodel in response to 2019 s.55 information request.

Overview of Royal Mail's services and the delivery network

3.35 Figure 8, below, sets out the structure of Royal Mail's UK end-to-end collection, processing and delivery network. Royal Mail collects both USO and non-USO letters and parcels from post offices, post boxes and businesses across the UK, which are then aggregated in Collection Hubs and Regional Distribution Centres (RDCs). From there, mail is sorted and

⁴² Households and SMEs.

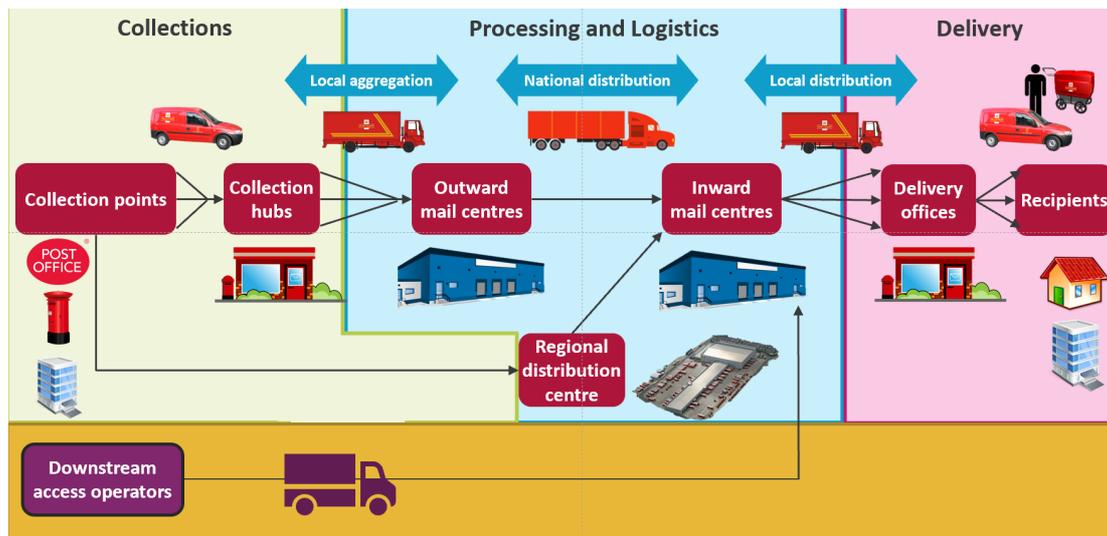
⁴³ Hermes and Yodel's response to our s.55 information request submitted on 6 December 2019 and 15 November 2019, respectively.

⁴⁴ Ofcom analysis based on information provided by Hermes and Yodel in response to our s.55 information request.

distributed through Outward Mail Centres and transported to Inward Mail Centres. From the Inward Mail Centres the mail is distributed to local Delivery Offices, and then delivered to the end recipients at over 30m residential and business addresses.

3.36 Meanwhile, access or bulk mail is collected from business senders by access operators who then inject it into Royal Mail’s network for ‘final mile’ delivery to recipients by Royal Mail.

Figure 8: Overview of Royal Mail’s UK operations



Source: Ofcom.

Developments impacting on Royal Mail and the USO

3.37 This section summarises developments relevant to Royal Mail and the USO, including its latest financial results and the impact of Covid-19, its strategic plan and public statements regarding the sustainability of the universal service.

Challenges facing Royal Mail

3.38 As set out above, since 2013 the UK postal market has seen structural decline in the letters market, and growth in the parcels market driven by increasing e-commerce. Royal Mail has been negatively impacted by the significant reductions in letter volumes, which has historically been its core business.

3.39 In the parcels market, while Royal Mail holds a significant portion of the market (for smaller parcels and/or single piece deliveries in particular), there is greater competition. This is particularly evident in relation to the high growth B2C parcels segment.

3.40 In May 2019, Royal Mail announced its transformation strategy, which set out a plan to become a parcels-led business⁴⁵ in response to these trends. Royal Mail said it would implement a UK transformation plan focused on improved service, efficiency and productivity, which was aiming to ‘turnaround and grow’ the UK business.

⁴⁵ Royal Mail, May 2019. Journey 2024 presentation.

3.41 However, as discussed in our Annual monitoring update on the postal market: Financial year 2019-20, Royal Mail's productivity (1.0%) and EBIT profitability margin (0.4%) for the Reported Business in 2019-20 was disappointing, even before the impacts of Covid-19 became apparent.

Royal Mail and the impact of Covid-19

3.42 Covid-19 had an immediate impact upon Royal Mail in the short term,⁴⁶ and it may accelerate the longer term market trends already observed. On 19 November 2020, Royal Mail reported that during the first six months of 2020-21 addressed letter volumes (excluding elections) were down 28% year-on-year, and letters revenues were down 20.5%.⁴⁷ By contrast, parcel volumes were up 31% and parcel revenues were up 33.2% year on year.

3.43 Royal Mail highlighted the substantial shift in the business from letters to parcels, which was driven by online shopping and demand for B2C parcel services. However, it noted that although this had realised better than expected revenues, the changing mix between parcels and letters had increased costs in the period by £95 million, alongside Covid-19 related costs of £85m.⁴⁸

3.44 On 25 June 2020, alongside its 2019-20 annual results, Royal Mail set out an updated transformation plan that took account of the impacts of Covid-19. It outlined plans to restructure management, accelerate operational change and work with stakeholders to ensure the USO reflects user needs and is modern, contemporary and sustainable.

Royal Mail and the USO

3.45 Royal Mail stated in June 2020 that it intended to engage with Ofcom and the Government to explore ways to ensure that the USO is financially sustainable, and meets consumers' changing priorities.

3.46 At a later trading update on 8 September 2020, Royal Mail set out some of its own research findings on the USO, which suggested that:

- Customers wish to retain USO universal pricing;
- Customers still value an affordable First Class letters service; and
- Customers want increased flexibility in terms of how they send letters and parcels – for example, online postage and parcel post boxes – and more frequent and convenient parcel deliveries.⁴⁹

⁴⁶ For example, Royal Mail announced on 28 April 2020 a temporary reduction in the frequency of letter delivery from six to five days a week, with the change removing the Saturday letter delivery. Royal Mail said this was in response to issues caused by the Covid-19 crisis, including high levels of absences and necessary social distancing measures.

⁴⁷ Royal Mail, November 2020. Results for the half year ended 27 September 2020.

<https://www.royalmailgroup.com/media/11354/royal-mail-group-half-year-results-19-november-2020.pdf>

⁴⁸ Royal Mail, November 2020. Results for the half year ended 27 September 2020.

⁴⁹ Royal Mail, September 2020. AGM Trading Statement.

<https://www.royalmailgroup.com/media/11260/royal-mail-plc-agm-trading-statement.pdf>

3.47 In November 2020, Royal Mail emphasised its view that the best way to ensure the Universal Service continues to meet its customers' needs is to rebalance its service model more towards parcels. Royal Mail added that it was continuing to engage with its customers and stakeholders about how it expects their needs to change in future.⁵⁰

⁵⁰ Royal Mail, November 2020. Results for the half year ended 27 September 2020.

4. Overview of user research findings

Key findings

- We found a marked **reduction in use of and reliance on letters** for both residential and SME users. However, there were some items that still needed to be sent by letter. In contrast, we found a large **increase in the use of parcels**, and an increased willingness to consider and use alternatives to Royal Mail, especially for SMEs.
- Post provides **social value to users**. A significant portion of users would feel cut off if they could not send or receive a letter (40% agree) or parcel (36% agree) almost every day. In general, older users seem more dependent on letters, and younger and middle-aged users more dependent on parcels.
- There was **strong support from users for core features of the USO**. This included maintaining the principles of universality. Users strongly endorsed a universal price and service across the UK. Users supported a service that was affordable and offered value for money, was certain and reliable, had delivery to the door and continued to provide a broad range of services.
- Our research also found that **users' needs are changing**, in particular a decline in the reliance and use of letters as a medium to communicate or conduct business. This is a trend that was discussed in our last review of user needs and has accelerated in the time since. We have therefore not concentrated our review on options that affect core features. We have instead focused on other features of the universal service, in particular, but not limited to, **the required number of letter delivery days**.

Introduction

- 4.1 Our research has looked at users' experience of the postal services and investigated the importance users attach to different elements of the universal service. We have looked at users' needs from postal services and have tested users' attitudes to potential changes to the universal service.
- 4.2 In this section, we begin with a brief summary of our research approach before detailing our research findings, covering the following topics:
 - Sending and receiving letters and parcels;
 - The importance of letters and parcels for users' connection with society; USO "core features", such as: universality and simplicity, affordability, certainty and reliability; delivery to the door, having a broad range of services; and
 - What our research findings mean for this review.

A summary of our research approach

- 4.3 We undertook comprehensive qualitative⁵¹ and quantitative⁵² research in order to understand the reasonable needs of postal service users in the UK.
- 4.4 In August and September 2019, we carried out in-depth qualitative research consisting of eight workshops, two additional focus groups in Northern Ireland and 16 face to face individual interviews with vulnerable users. Taking a similar approach to our research in 2012, we sought to ensure we covered both residential users and SMEs, as well as a wide range of communities in the UK including the nations and rural communities. Our 2019 qualitative research findings, then fed into the design of our quantitative research.
- 4.5 Our 2019 quantitative research was also split between residential and SME users. In addition to this split, we were able to assess impacts on individual nations within the UK, lighter and heavier users, younger and older users, those living in urban, rural and deep rural areas, as well as disabled people and users' with or without internet access. We undertook 4,596 30-minute interviews with UK adult residential users, of which 2,355 were face to face and 2,241 were online interviews. For SME⁵³ users, we completed 971 30-minute telephone interviews with users who were responsible for their organisation's post.
- 4.6 In Summer 2020, we completed supplementary research⁵⁴ and analysis to gain early insights into whether the Covid-19 pandemic and first lockdown period may have affected user behaviours and needs. This research only involved online interviews and therefore was not directly comparable with our main research.⁵⁵ However, the main findings appear largely in line with our quantitative research. The results are published alongside this document.
- 4.7 Finally, we drew on other research sources, such as our annual residential consumer and SME postal trackers and information gained from engagement with stakeholders including a series of interviews that we carried out with heavy users of bulk mail letters services e.g. public sector organisations, banks, utilities and publishers.

⁵¹ Jigsaw Research, 2019. UK Postal User Needs: Qualitative Research Report, https://www.ofcom.org.uk/_data/assets/pdf_file/0017/208214/2020-review-of-postal-user-needs-qualitative-report.pdf.

⁵² Jigsaw Research, 2019. UK Postal Users Research: Quantitative Research Report, https://www.ofcom.org.uk/_data/assets/pdf_file/0018/208215/2020-review-of-postal-user-needs-quantitative-report.pdf.

⁵³ SMEs are organisations with up to 249 employees.

⁵⁴ Jigsaw Research, 2020. Postal Needs Follow up Summer 2020 Research, https://www.ofcom.org.uk/_data/assets/pdf_file/0019/208216/2020-review-of-postal-user-needs-summer-research.pdf.

⁵⁵ We decided that an online-only methodology was the most appropriate survey methodology to use to ensure participant and interviewer safety during the pandemic. The survey therefore did not include people with no internet access and was not directly comparable with our main research.

Our research findings

Sending and receiving letters and parcels

- 4.8 We have reviewed the research, to better understand the main trends in behaviours and needs for residential, SME and large users of letters and parcels.
- 4.9 In summary, for letters, we found a clear decline in reliance on letters to communicate with others. There was an expectation, from the vast majority of users in different geographic and demographic groups, that this trend will continue into the future. Nevertheless, we found an on-going need to send and receive letters, and there are specific items that people feel need to be delivered via letter. We also found some indicative evidence that suggests that fast delivery of most items was not important to some users, although it still remains an important consideration for many users of First Class services. Moreover, the research supports an ongoing need for a guaranteed next day delivery.
- 4.10 In contrast to letters, the participants thought the UK's parcels market was growing strongly, largely fuelled by the expansion of online shopping. Although Royal Mail continued to be the main provider of parcel services for most residential users, there was some evidence of growing awareness of the alternatives and willingness to use them. This was especially the case for the heaviest users, and has been accelerated by Covid-19. Our research suggests that there was more widespread use of Royal Mail's competitors by SMEs than residential users.

Residential users are sending fewer letters, but expect an ongoing need for some uses into the future

- 4.11 Our findings suggest that a large proportion of users send letters infrequently. Our quantitative research showed that over half of residential users (53%)⁵⁶ sent one or fewer letters per month. Less than a quarter of residential users (24%) sent four or more letters a month.⁵⁷
- 4.12 Reliance on letters as a method to communicate continues to decline. For example, between 2016 and 2019 our postal tracker showed that the proportion of regular letter senders has declined across all age groups.⁵⁸ This was supported by our qualitative research, where participants considered the volume of letters they sent and received has generally declined, with some participants not engaging in this segment of the market at all.⁵⁹
- 4.13 This trend also reflects preferences for communication with friends, family and other organisations. Our tracker survey found the relative importance of post as a means to

⁵⁶ This is composed of 11% (none), 31% (less than one/month), and 11% (one/month). See, 2019 quantitative research, p.8.

⁵⁷ This is composed of 12% (six or more), 6% (five) and 6% (four). See, 2019 quantitative research, p.8.

⁵⁸ Residential postal tracker survey (2016-2019), QD1: Approximately how many of the following have you sent in the last month? All Letters / Parcels.

⁵⁹ 2019 qualitative research, p.15.

communicate with friends and family has declined across all age groups.⁶⁰ Most users also increasingly prefer to communicate with organisations via digital alternatives (e.g. email or instant messaging applications).⁶¹ ⁶² This extends to a decline in post being the preferred way to receive information from the council, utilities, and banks.⁶³

- 4.14 In both our qualitative⁶⁴ and quantitative⁶⁵ research, most participants expressed an expectation that these trends would continue into the future.⁶⁶
- 4.15 As shown in our postal tracker, there continues to be a perceived need for and a degree of reliance on a letters service for some users.⁶⁷ This reliance is noted in our section on the importance of letters and parcels in users' connection with society below.⁶⁸ Moreover, there are certain items, such as medical letters⁶⁹, cards and postcards, official documents, and letters that need a signature on receipt that will continue to drive a need.⁷⁰ Our research suggested that many people wish to have the ability to send letters when they need to, even if the number of letters that they actually send has declined.
- 4.16 There was also some evidence to suggest that speed of delivery of letters for residential users may have declined in importance. In our qualitative research, there was a strong view from participants that most letters were not urgent and therefore speed of delivery was rarely critical, although some notable exceptions were raised (e.g. late birthday cards or urgent documents).⁷¹ Our postal tracker also showed a decline in the percentage of people who said they mostly use First Class and an increase in those that said they mostly use Second Class stamps.⁷²
- 4.17 For those participants that used First Class services, when asked about their reasons for using the service, most of the responses had little to do with speed of the service. For many, factors such as "habit", a small price differential with Second Class, perceptions that

⁶⁰ Residential postal tracker survey (2016-2019), QC4: Thinking about how you communicate with family and friends, how important are each of these channels of communication?

⁶¹ Residential postal tracker survey (2012-19), QC1: Please think about communication from organisation that you have a relationship with. Which types of communication would you be happy to receive from.

⁶² The main exception being the older and/or the less internet savvy (2019 qualitative research, p.15).

⁶³ Residential postal tracker survey (2016-19). QC2: And which type of communication would you most like to receive from... Your bank or building society.

⁶⁴ 2019 qualitative research, p.15.

⁶⁵ 2019 quantitative research, p.38.

⁶⁶ This is consistent with the findings from our Covid-19 bespoke research, where participants noted that they were sending fewer letters and there had been a significant reduction in the number of letters received, and that this change is likely to be sustained. See slide 6.

⁶⁷ Residential postal tracker survey (2012-19), QC3: Here are some statements that other people have made about sending and receiving post. To what extent do you agree or disagree with each/ QG1. How much would you say you rely on the postal service for sending and receiving... Letters & Parcels.

⁶⁸ See Figures 12 and 13 below.

⁶⁹ Though we note that many medical letters will be provided outside of the USO.

⁷⁰ 2019 qualitative research, p.16.

⁷¹ 2019 qualitative research, p.16.

⁷² Between 2012 and 2019, there was a reduction in participants that tended to use First Class stamps (from 58% to 50%) and an increase in participants that tended to use Second Class stamps (from 19% to 25%). Residential postal tracker survey (2012-19), QF7: When sending letters or cards, which service do you tend to use?

First Class offered a higher quality of service and signalling effects on the receiver were often more important.⁷³

- 4.18 This finding contrasted somewhat with our quantitative research findings, where “normally gets there the next day”, was the main stated reason for using First Class (although many of the other factors mentioned in the paragraph above were also noted⁷⁴).⁷⁵ Therefore, although there are some indications that speed of delivery for letters may have reduced in importance for some users, it appears to be still be an important factor for others.
- 4.19 Though there was some evidence in the decline of importance of speed for letters, there was a strong need for a guaranteed next day delivery for certain urgent documents,⁷⁶ a position mirrored by SME participants.⁷⁷

SMEs are also less reliant on letters and are sending fewer letters but still need to contact some of their customers via mail

- 4.20 A decline in reliance on letters by SMEs was evident in our qualitative research.⁷⁸ It was supported by findings from our postal tracker that showed a marked decline in SMEs that say they send letters regularly. Between 2012-19 the percentage of SMEs that sent letters at least once a month declined from 92% to 60%.⁷⁹ There was also a fall in the percentage of SMEs that say post is critical or core to their businesses. Between 2012-19, the percentage of companies that stated that post was mainly used for administrative purposes and not core to their business rose from 51% to 62%.⁸⁰ Moreover, similar to trends for residential users, in every year since 2012 more than half of SMEs said they have moved some post to other communication methods.⁸¹
- 4.21 There was still a degree of reliance on letters to communicate with some customers. In our qualitative research, it was noted by some SMEs that they needed letters to communicate with, often older, users that were not online. An SME user in Caernarfon noted that, “*You still have to be able to send out invoices to some people. Not everyone is online, or responds to emails*”. Participants noted that letters were still needed for invoices, contracts, direct marketing, reminders and for items that require a signature on receipt.⁸²
- 4.22 Speed of delivery for letters also appears to be less important for SMEs. As with residential users, other factors were also important when choosing to use First Class instead of Second

⁷³ 2019 qualitative research, pp.19-20.

⁷⁴ For example, always used (27%), not much cost difference (16%), just what I have to hand (12%), value of item (11%), shows you care (7%) and looks more important (6%). 2019 quantitative research, p.12.

⁷⁵ 2019 quantitative research, p.1.

⁷⁶ 2019 qualitative research, p.16.

⁷⁷ For example, in our qualitative research, a heavy SME user in Oban noted, “*I’d be happy to go to a single class of service in two to three days as long as there was still Special Delivery if anything is really urgent and most post isn’t.*”

⁷⁸ 2019 qualitative research, p.4.

⁷⁹ See the SME postal tracker survey (2012-19), QV6a. Which of the following types of post does your organisation send regularly (this is once a month or more frequently than that)?

⁸⁰ See the SME postal tracker survey (2012-19), C7. Which one of the following statements best describes the role of postal services to your organisation?

⁸¹ SME postal tracker survey (2013-19), QF4. Over the last 12 months, has your organisation moved some post to other communication methods

⁸² 2019 qualitative research, p.16.

Class. In our quantitative research, although “speed of delivery” was the most important reason noted for using First Class letters by SMEs, only approximately two-thirds needed most or almost all letters to arrive the next day.⁸³

- 4.23 In our qualitative research, when SMEs were asked what was important when considering Royal Mail against its competitors, speed of delivery was not usually a factor. Price was the key stated factor when choosing between alternative providers.⁸⁴

Heavy letters users are also sending fewer letters, and expect this trend to continue

- 4.24 Heavy letters users are organisations such as banks, insurers, utilities and public sector organisations that primarily use bulk mail letter services to contact their customers. Bulk mail sent by heavy users represents a large majority of letters sent.⁸⁵ Bulk mail services are not part of the USO, but Royal Mail uses substantially the same delivery network to deliver both bulk mail and First Class and Second Class letters, and bulk mail makes an important contribution to covering the costs of this delivery network.
- 4.25 To develop our understanding of heavy users’ current and future mail usage we carried out a series of interviews with organisations from different sectors.⁸⁶ From our interviews, heavy users told us that they sent a range of content to people and businesses via post, however transactional letters (e.g. bills, bank statements) dominated.
- 4.26 Most heavy users’ use of letters had declined over the last five years, and they expected their use to continue to fall over the next two years. However, a handful of public sector organisations anticipated their usage would stay the same over this period. Moving to digital communications was the key reason for the decrease. It was noted that regulatory requirements, customer preference and the need to send physical items (e.g. bank cards, publications) meant that letters were likely to be needed for some time.
- 4.27 Heavy users opted to use standard services provided by their postal operator with a routing time of two working days or later for the majority of letters they sent. However, some also used Royal Mail First Class services for a minority of urgent, important letters (e.g. mortgage arrears, replacement bank cards, or when issuing fines). For many, the price of letters was a very important factor in their decisions, both in terms of speed of service selected and whether to use post over other methods of communication.

Residential users are sending and receiving more parcels, and tend to use Royal Mail, but are becoming more interested in using the alternatives

- 4.28 Most participants in our qualitative research said that they sent and received more parcels than they had previously. These responses varied across participants, and their use and

⁸³ 2019 quantitative research, pp.22-23.

⁸⁴ 2019 qualitative research, p.18.

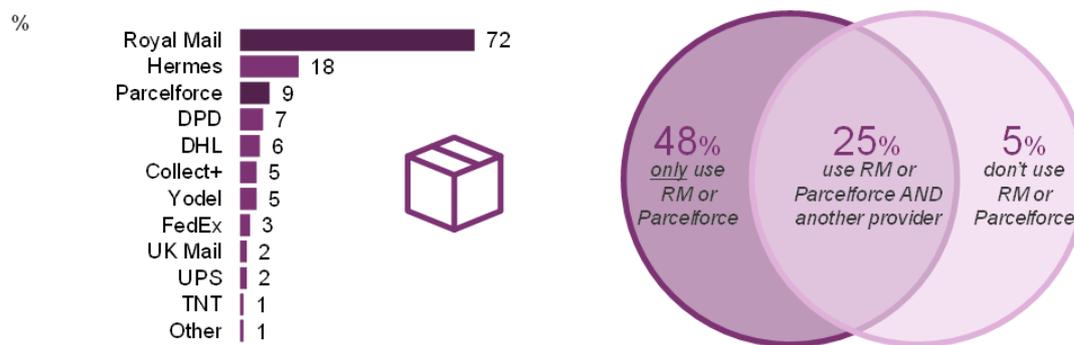
⁸⁵ In 2018-19, access letters accounted for 65% of total addressed letter volumes, and a large proportion of these volumes will be from bulk mail users.

⁸⁶ We spoke to representatives from organisations in the following sectors between April and August 2020: publishing, banking and financial services, utilities, telecommunications, public sector, printing and mailing houses, customer communications, and access operators.

dependence were closely linked to the volume of online shopping they did.⁸⁷ Also, participants in our quantitative research expected that they would either receive the same volume or more parcels in the future.^{88 89}

4.29 There was a strong preference among consumers to use Royal Mail for parcels. In part this may reflect familiarity with the Royal Mail service, with 72% of participants having used Royal Mail in the last 12 months. Although our research suggests there was clearly growing awareness of the alternatives and some willingness to use them⁹⁰, there remains a strong reliance on Royal Mail⁹¹, with 48% of participants solely using Royal Mail or Parcelforce.⁹² Our research found that Hermes was the most commonly used alternative to Royal Mail.

Figure 9: Consumer preferences when using postal services in the UK



Source: Jigsaw Market Research.^{93, 94}

In general, SMEs are sending and receiving more parcels and are more willing to use Royal Mail’s competitors

4.30 In our qualitative research, we found that most SME participants considered they sent and received more parcels. The importance of parcels to SMEs depended on the individual business. Some were reliant on sending and/or receiving physical items through the post as

⁸⁷ 2019 qualitative research, p.16.

⁸⁸ 2019 quantitative research, p.38.

⁸⁹ In our Covid-19 bespoke research users noted that they were sending broadly the same volume of parcels, but had seen a significant increase in the number of parcels received. In part, this can be explained by the increased use of online purchases. See slide 6.

⁹⁰ A trend which has been accentuated by Covid-19 according to our bespoke research. See slide 5.

⁹¹ We note that this reliance isn’t uniform. Over two thirds (68%) of those that send more than one parcel a month, say they sell items via online platforms (e.g. eBay, Etsy). These users are more willing to use alternatives to RM, with 76% saying that they use at least one of RM’s competitor parcel providers.

⁹² 2019 quantitative research, p.13.

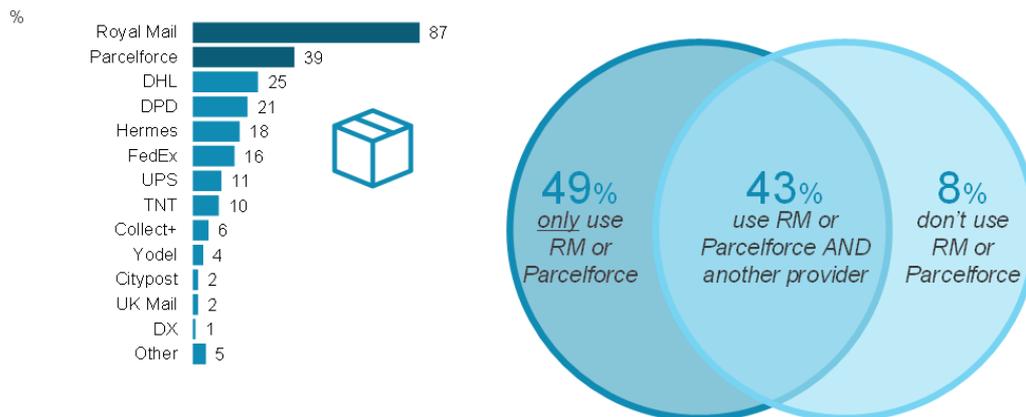
⁹³ The first question, represented by the bar chart, asks participants which (if any) of the companies it has used to send a parcel in the last 12 months. There are many participants that used multiple delivery companies, hence the sum is greater than 100%.

⁹⁴ The second question’s results, represented in the Venn diagram, do not add up to a hundred percent. This is because 22% of the residential base did not send parcels via any provider.

part of their business model. Others only received or sent parcels occasionally so had a much lower dependency on parcel services.⁹⁵

- 4.31 There continues to be a large proportion of SMEs that use Royal Mail or Parcelforce. However, SMEs make use of other providers to a greater extent than residential users, with over 40% having used Royal Mail or Parcelforce and another provider in the last 12 months.

Figure 10: SME preferences when using postal services in the UK



Source: Jigsaw Market Research.

- 4.32 The above finding is consistent with evidence from our postal tracker that shows a decline in the percentage of SMEs that send parcels who say that Royal Mail was their main provider for parcels or packets.⁹⁶

Heavy parcels users appear to prioritise cost effective, fast, reliable and convenient delivery

- 4.33 Heavy users of parcel delivery services (e.g. online retailers) use bulk contracts agreed with parcel operators who have their own end-to-end networks for collection, sortation and delivery. While this is an important and rapidly growing part of Royal Mail and competitors' businesses, bulk parcel services are not part of the USO (as with bulk letters services). However, it is important to understand the priorities of heavy users and their customers in this segment of the market for wider context.

- 4.34 We understand from our engagement with parcel operators that heavy users of parcel services in the business to consumer segment prioritise cost effective, fast (next day) and convenient delivery. Parcel operators think that their customers (i.e. online retailers) typically want to know when parcels will be delivered with a high degree of accuracy, have access to tools to track the delivery journey, and for parcels to be delivered securely and undamaged. Their customers also valued being able to offer end-consumers the choice of a

⁹⁵ 2019 qualitative research, p.17.

⁹⁶ Between 2016-18, the percentage of companies that stated that Royal Mail was its main provider for parcels and packets dropped from 72% to 66%. SME postal tracker survey (2016-18), QV5b.2 Which would you say is your organisation's main postal service provider for parcels and packets in terms of the value of your contract with them?

range of delivery options, e.g. home delivery, lockers, click & collect and the flexibility of being able to change their selection inflight.⁹⁷

The importance of letters and parcels for users' connection with society

- 4.35 Our research looked at the importance of these services to people's lives, including the social value it may have for them. Our research suggested that users consider the universal service provides some social value by helping some users feel connected to society. In the qualitative research, many participants felt that Royal Mail was a national institution that brought people together. Other participants valued the "personal touch"⁹⁸ provided by their local postal worker. They further reflected that there were some vulnerable people in communities across the country that remain reliant on the service.
- 4.36 This perception was less important for some younger participants as post, in particular letters, often did not play an important part in their lives.⁹⁹ For instance, a light user of postal services in London stated, *"I just never get any letters... other than junk mail that I don't want. I've gone paperless so I do all my banking online and I never get any statements. I've done that with everything because it's just easier, isn't it?"*
- 4.37 Finally, over a third of users felt that they would feel cut off from society if they did not have the ability to send or receive letters (40% agree) or parcels (36% agree) almost every day of the week.¹⁰⁰

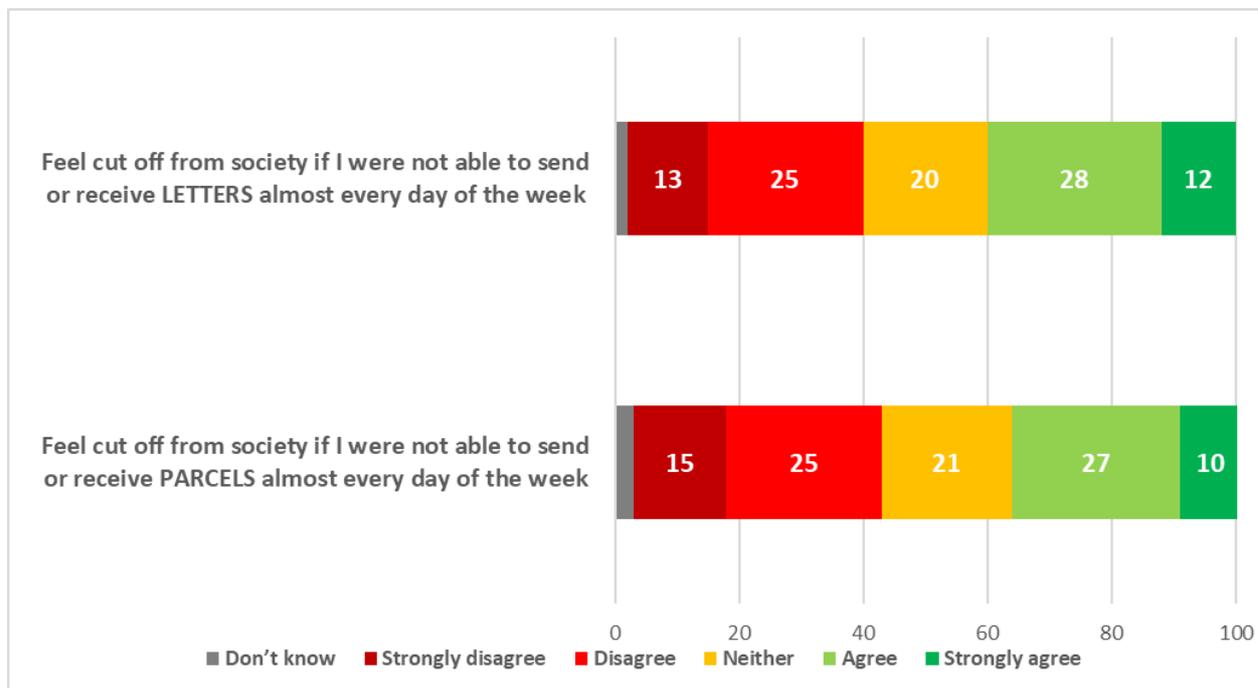
⁹⁷ We note that the evidence here is relatively limited, as we have not directly engaged with parcel operators' customers (i.e. online retailers). As such, we think it provides some useful context, but we have put little weight on it.

⁹⁸ For instance, knowing the habits or movements of users of their service. For example, in our qualitative research, one low mobility heavy user of postal services in Caernarfon noted, *"If I'm not in, the postie knows to bring my mail to Wetherspoons as that's where I am most mornings."*

⁹⁹ 2019 qualitative research, pp.13-15.

¹⁰⁰ We note that the findings from our Covid-19 bespoke research are consistent with the results here. See slide 13.

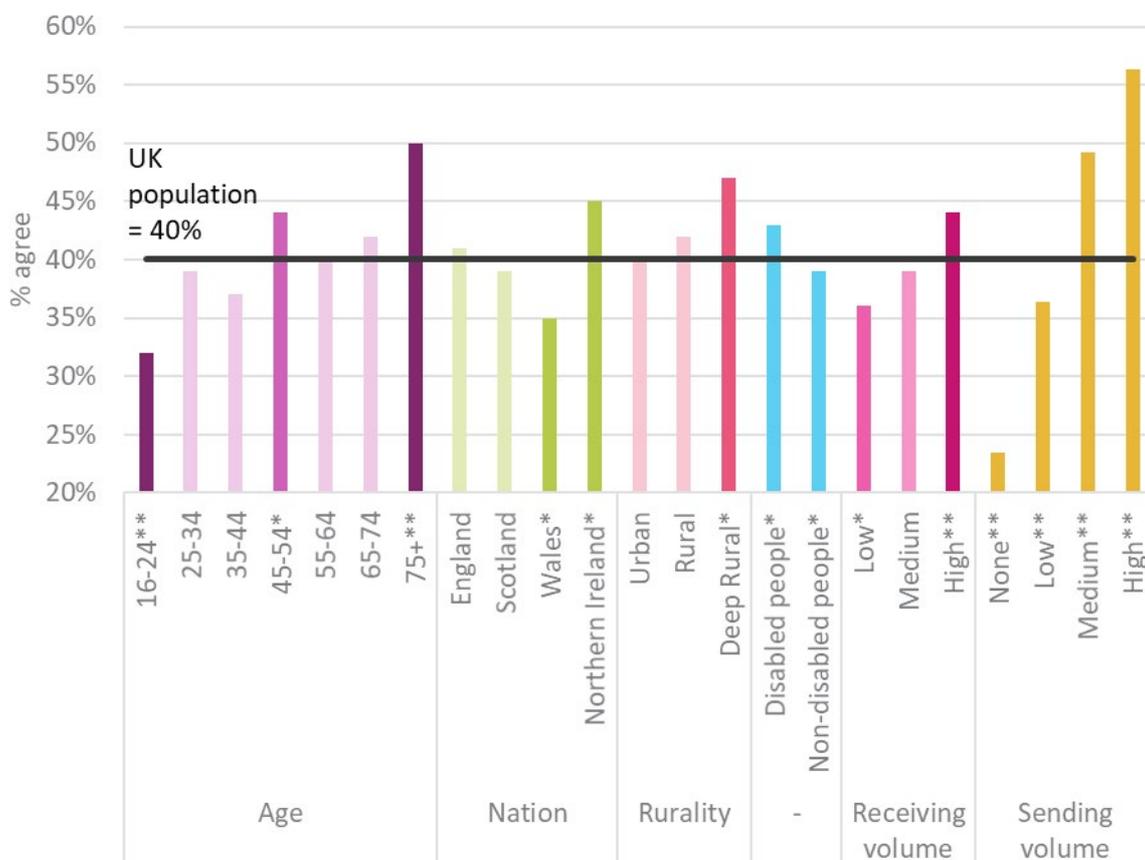
Figure 11: Agreement with statements about feeling cut off from society (%)



Source: Jigsaw Market Research.

4.38 For letters, it was the oldest subgroup (75+) that most valued the connection with society provided by regular almost daily deliveries, whereas the youngest demographic (16-24) valued it the least, with minor variation across the age groups in between. However, 32% of the 16-24 demographic thought this connection was important. There was some small variation across the nations, as Northern Irish users valued it slightly more and Welsh users slightly less than English and Scottish users. In addition, deep rural users valued it more than rural and urban users. Disabled users also valued the connection more than non-disabled users. Finally, those users that sent/received higher volumes of letters valued the connection more than those who sent/received fewer letters. The importance was particularly pronounced for users that sent a medium and high volume of letters.

Figure 12: Agreement with statements about feeling cut off from society broken down by demographic (residential letters)



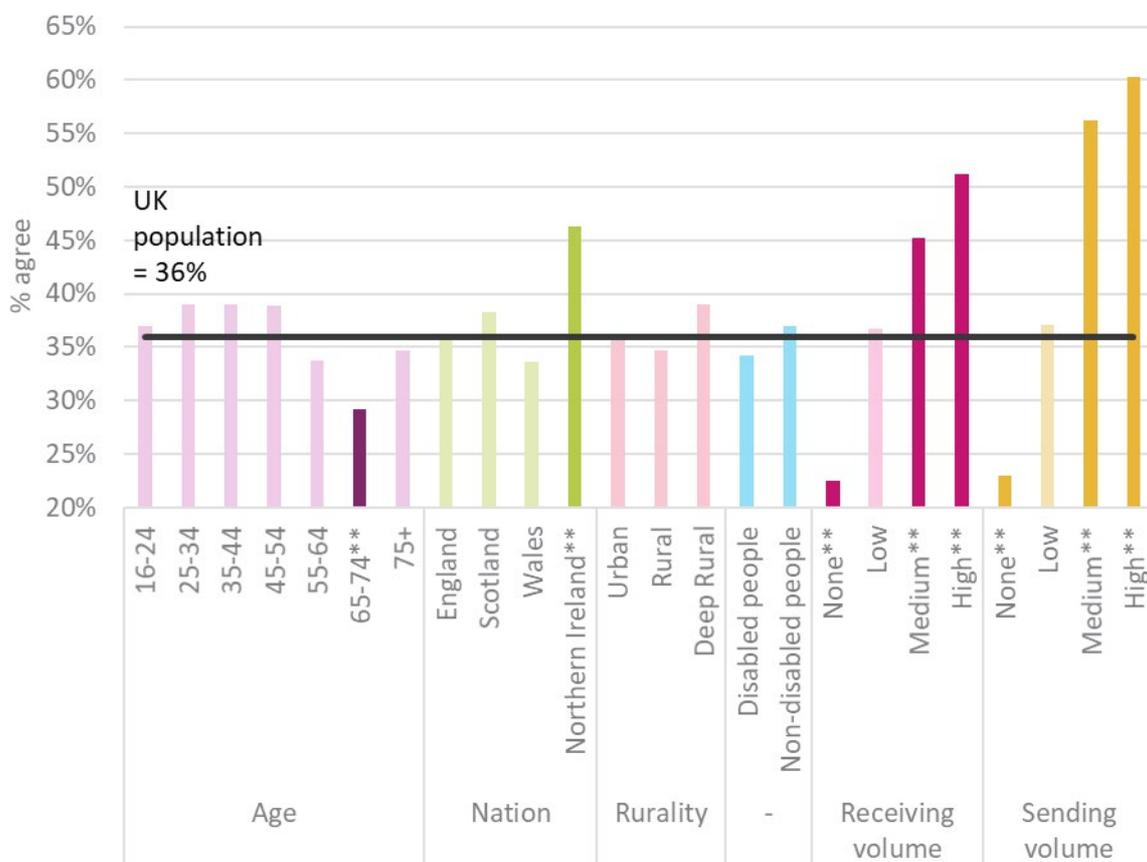
Source: Ofcom analysis from Jigsaw Market Research.

Question: Feel cut off from society if I were not able to send or receive letters almost every day of the week (how far do you agree or disagree with the statement?).

Note: darker tones denote statistically significant differences from the UK population (*=95% confidence level; **=99% confidence level).

4.39 For parcels, the younger to middle aged subgroups (i.e. 16-54) most valued the connection with society provided by regular almost daily deliveries of parcels and the 65-74 demographic valued it the least. We note that Northern Irish users valued it more than the other three nations. There were not marked differences between urban and rural or deep rural users. Finally, as was the case for letters, those users that sent/received higher volumes of parcels valued the connection more than those who sent/received fewer parcels. The importance was particularly pronounced for users that sent a medium and high volume of parcels.

Figure 13: Agreement with statements about feeling cut off from society broken down by demographic (residential parcels)



Source: Ofcom analysis from Jigsaw Market Research.

Question: Feel cut off from society if I were not able to send or receive parcels almost every day of the week (how far do you agree or disagree with the statement?).

Note: darker tones denote statistically significant differences from the UK population (*=95% confidence level; **=99% confidence level).

User views on core features of the current universal postal service

- 4.40 ‘Core features’ are elements within the provision of the current universal postal service that users value highly, have a strong desire to maintain and a low willingness to compromise on.
- 4.41 Our research suggested that the principle of “universality” in terms of both price and service was a core feature and very important to users. Users wanted a “simple” service that was easy to understand to the average user and for which everyone pays the same regardless of location. “Affordability and value for money” and “certainty and reliability” were also very important to users. “Delivery to the door” was strongly endorsed, one supporting rationale being concerns around how some vulnerable users would be affected if this was to change. Finally, it was widely accepted that users needed a broad range of services, to reflect their diverse needs.

4.42 Below, we outline the research findings in detail and explain our interpretation.

Universality

- 4.43 Universality of service and price, no matter where the user is in the UK, is one of the main principles of a universal postal service. The research showed, both in terms of price and service, that there was strong support for the concept of “universality”. It was highly valued by users and contributed to the simplicity of the service.
- 4.44 The results of our qualitative research showed that participants highly valued the fact that there was no variation of service or pricing based on geography. Indeed, many participants considered that having the same price and service, regardless of where you lived, was needed in order for the service to feel “fair”.¹⁰¹
- 4.45 Having a universal price was strongly supported in our quantitative research. 67% of residential participants agreed that Royal Mail should provide its services at the same price to all, regardless of where a letter or parcel was sent within the UK, and a slightly higher proportion of SMEs (69%) also agreed.^{102 103 104}
- 4.46 Universality also helps to ensure simplicity of the service, which was highly valued by participants in our qualitative research. Users stated that they need clarity, convenience¹⁰⁵ and when sending letters, ease of getting them into the system.¹⁰⁶ Participants considered that having different delivery and collection days in different parts of the country added far too much complexity, as postal users would need to understand how the postal service operated in their area and the areas that they were sending to.¹⁰⁷ Some of the issues associated with moving away from a universal service were clearly articulated by a heavy residential user in Leeds, *“It would be way too complicated if you had different prices for different locations, I really don’t want to have to think about that. We all send and receive things from closer and further away sometimes and you can’t always control how far you have to send stuff – it just seems fairer and easier this way.”*

¹⁰¹ 2019 qualitative research, p.26.

¹⁰² We note that Minimum Requirement 3 in Section 31 of the Act requires, “a service at affordable prices in accordance with a public tariff which is uniform throughout the UK”. Moreover, Requirement 1 in Section 31 of the Act specifies that the delivery of letters and parcels must be made “to the home or premises of every individual or other person in the UK”

¹⁰³ 2019 quantitative research, p.1.

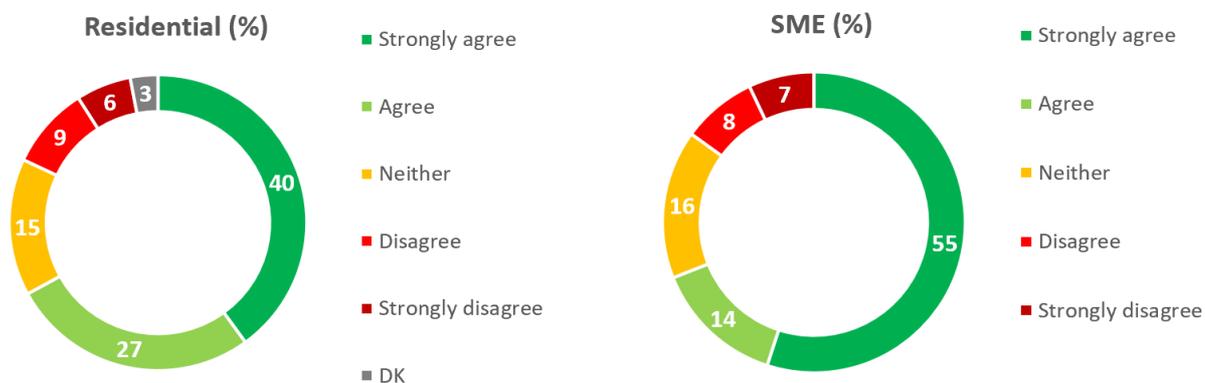
¹⁰⁴ Our Covid-19 bespoke research produced similar results with 68% of participants agreeing that the same price should be charged to all users. See slide 23.

¹⁰⁵ 2019 qualitative research, p.8.

¹⁰⁶ 2019 qualitative research, p.6.

¹⁰⁷ 2019 qualitative research, p.26.

Figure 14: Whether Royal Mail should provide its services at the same price to all, regardless of where a letter or parcel is sent within the UK

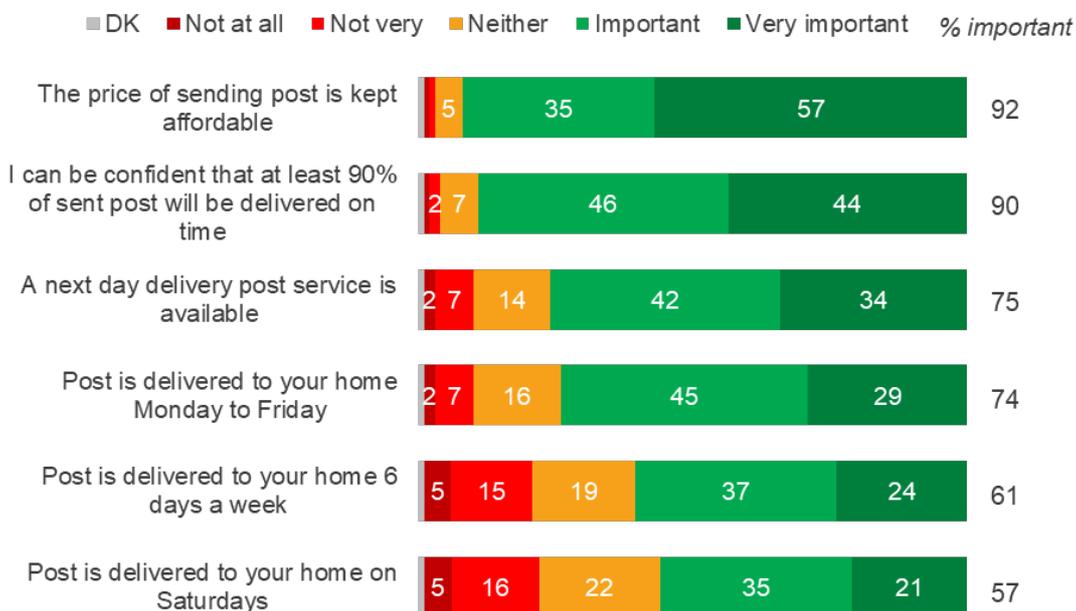


Source: Jigsaw Market Research.

Affordability, certainty and other features of the service

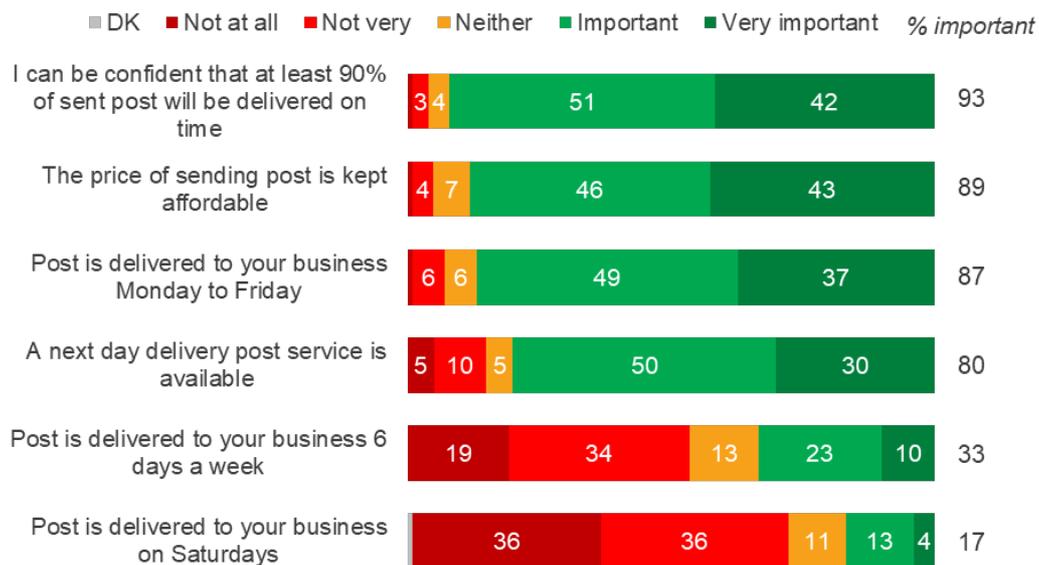
4.47 As part of our quantitative market research, we asked participants about how important different aspects of the postal service were to them. Responses are set out in Figure 15 and Figure 16 below.

Figure 15: Residential users, “How important is it to you that...”



Source: Jigsaw Market Research.

Figure 16: SME users, “How important is it to your business that...”



Source: Jigsaw Market Research.

- 4.48 The vast majority (around nine in ten) of both residential and SME users considered affordability and high certainty/reliability to be important aspects of the postal service.
- 4.49 We further note that having post delivered Monday to Friday, and the availability of next day delivery also seemed to be fairly important to both SME and residential users. Both Monday to Friday delivery (87% vs 74%) and availability of next day delivery (80% vs 75%) were more important to SME users than residential users.
- 4.50 A materially smaller proportion of users considered that delivery six days a week or on Saturdays was important. 57% of residential users and 17% of SME users considered Saturday delivery to be important. We note that this question asked participants to consider post (i.e. letters and parcels), and so this is not a perfect indicator of the importance of Saturday letter delivery alone.¹⁰⁸

Affordability and value for money

- 4.51 As noted above, our quantitative research showed that delivering an affordable service that offers value for money was very important for users.¹⁰⁹
- 4.52 The research suggested that users think Royal Mail provides a postal service that was offering value for money. According to the post tracker, at least seven in ten participants

¹⁰⁸ Our Covid-19 bespoke research provided results that were broadly comparable and largely consistent in terms of ranking of important elements of the USO. It separates out letters and parcels and shows that, while there are few differences in expectations for parcels and letters, Saturday delivery was marginally more important for parcels. See slides 17 and 18.

¹⁰⁹ See Figures 16 and 17 above, which note the importance of affordability to both residential and SME users.

are satisfied with the value for money of sending mail.¹¹⁰ This appears to be corroborated in our qualitative research, where a few exceptions aside¹¹¹ participants thought the USO offered good value for money.¹¹²

- 4.53 We also found that a large portion of participants were unclear about the cost of sending letters¹¹³ and parcels¹¹⁴, a finding that was broadly supported by data from our postal tracker.¹¹⁵ There were a number of reasons identified in our research as to why participants might not know the price of post, one of which was that some used postal services intermittently, if at all.^{116, 117}

Certainty and reliability

- 4.54 Our research found that both certainty and reliability were important for postal users. This is consistent with high standards for quality of service, which gives users a high degree of certainty as to when an item will arrive.
- 4.55 The qualitative research strongly supported a need for certainty and reliability of service. When it came to sending letters and parcels and receiving parcels, users valued having certainty as to when an item would arrive and confidence it would arrive in good condition. Some other users, such as senders of parcels and recipients of letters, also valued an option that ensured items arrived on a particular date.¹¹⁸ Moreover, in the case of letters in particular, certainty appeared to be valued more highly than speed.
- 4.56 This finding was strongly endorsed in our quantitative research, which found a high degree of certainty to be one of the two most important aspects of the service for residential and SME users.¹¹⁹
- 4.57 Our qualitative research also suggested that both certainty and reliability play a role in Royal Mail's strong reputation as a post provider.¹²⁰

¹¹⁰ We note that satisfaction is higher in high income households (79%) than low income households (68%). Ofcom, Residential Postal tracker Q3 2019-Q2 2020.

¹¹¹ For example, special delivery was seen as fairly expensive, as was a redirection service for some users (e.g. low income, large household, those that moved more regularly). 2019 qualitative research, p.29.

¹¹² 2019 qualitative research, p.27.

¹¹³ For example, estimates of the cost of a stamp varied from 20p to £3. 2019 qualitative research, p.26.

¹¹⁴ Our qualitative research suggested that awareness of parcel prices was even lower than for letters. 2019 qualitative research, p.27.

¹¹⁵ For letters, the range for a First Class stamp was 0p to £9.70 and for a Second Class stamp it was 0p to £9. 14% of participants gave a value over £1 for First Class and 8% for Second Class. The postal tracker did not collect the same data for parcels.

¹¹⁶ There were three other reasons mentioned. Specifically, stamps were typically bought in books, as opposed to individually (making the individual price less obvious). They were often bought alongside other items and so the price was not always obvious. Third and finally, the monetary value was not written on a stamp as a reminder. 2019 qualitative research, p.27.

¹¹⁷ We further note that actual household expenditure on post is very low. According to the ONS, it constitutes just over 0.1% of household expenditure. See Ofcom, 2019. Review of the Second Class Safeguard Caps 2019. p.53, Figures 3 and 4

¹¹⁸ 2019 qualitative research, pp.6-7.

¹¹⁹ Also see Figures 15 and 16 above, which note the importance of certainty to both residential and SME users.

¹²⁰ 2019 qualitative research, p.17.

Delivery to the door

- 4.58 In the research, there was strong support overall for continued delivery to the door.
- 4.59 In our qualitative research, most participants were unwilling to compromise on having their post (particularly letters) delivered to their door. They saw delivery to the door as a fundamental part of the service and therefore tended to be strongly opposed to delivery to a central point.¹²¹ There was a further consideration among some participants that delivery to a central point could have a particularly negative impact on vulnerable consumers (e.g. the elderly, disabled or housebound) and those who lived in remote areas.
- 4.60 This finding was strongly endorsed in the quantitative research too. There was significant opposition to the idea of a secure central locker being provided instead of delivery to the door. Among residential users, 76% were against dropping delivery to the door in relation to letters and 64% in relation to parcels. For SMEs, the numbers were even more pronounced with 82% against in relation to letters and 77% in relation to parcels.^{122 123}

Figure 17: Popularity of the secure locker concept for letters and parcels



Source: Jigsaw Market Research.

User needs extend beyond standard services

- 4.61 Our qualitative research showed that, when sending an item, in most instances participants did not need add-ons such as a guaranteed next day delivery or insurance. A standard service (e.g. First Class or Second Class service) would often meet their needs. This could suggest that postal users' needs could often be met by a narrow range of postal services.
- 4.62 However, there were cases where the standard services did not meet user needs. For example, there were instances where users needed a guaranteed next day delivery (e.g. for a late birthday card), proof of delivery when selling an item via an e-commerce platform or

¹²¹ 2019 qualitative research, p.8.

¹²² 2019 quantitative research, p.4.

¹²³ Our Covid-19 bespoke research produced broadly consistent results, with 63% (letters) and 54% (parcels) either against or strongly against delivery to a central point. These results were a bit lower than our main research but do continue to show strong opposition to delivery to a central point, in particular for letters.

greater certainty when an item would be delivered (e.g. for certain legal documents).¹²⁴

There were also some cases when users needed insurance, such as when sending a passport or other valued item. We further note that our quantitative research showed that there was a clear on-going use of these additional services.^{125 126}

- 4.63 Therefore, we consider that users' need for a broad range of postal services was supported by the research.

Conclusions

- 4.64 In our last review of user needs, we found areas where needs appeared to be changing. We noted that there appeared changing needs in relation to delivery speed¹²⁷ and there was some support, rationale and evidence to suggest that five days letters delivery met user needs.¹²⁸
- 4.65 Since our last review, there has been a significant growth in the use of mobile phones and the internet to communicate. There has also been the emergence and increased take up of new communication services and market growth in online shopping. As noted here and elsewhere in this document, this has been accompanied by a further reduction in letter volumes. There has been a decline in reliance on letters as a means to communicate and transmit urgent messages, which is changing how letters are used. Needs are continuing to evolve in line with the trends identified in our last review and as described above.
- 4.66 As our research has highlighted, there was strong user support for certain core features of the USO, such as universality, affordability and delivery to the door. We have therefore not considered changes to these requirements of the current universal service in more detail. We have instead focused our more detailed assessment on other features of the universal service specification, in particular, but not limited to, the required number of letters delivery days a week. The following section sets out our analysis on delivery days.

¹²⁴ 2019 qualitative research, p.16.

¹²⁵ For instance, 67% of SME participants had used Signed For in the last year and more than half had used Special Delivery Next Day (53% (letters), 56% (parcels)). 2019 quantitative research, p.18.

¹²⁶ 2019 quantitative research, p.3.

¹²⁷ Ofcom, 2013. Review of postal users' needs, p.19.

https://www.ofcom.org.uk/data/assets/pdf_file/0022/58432/statement1.pdf

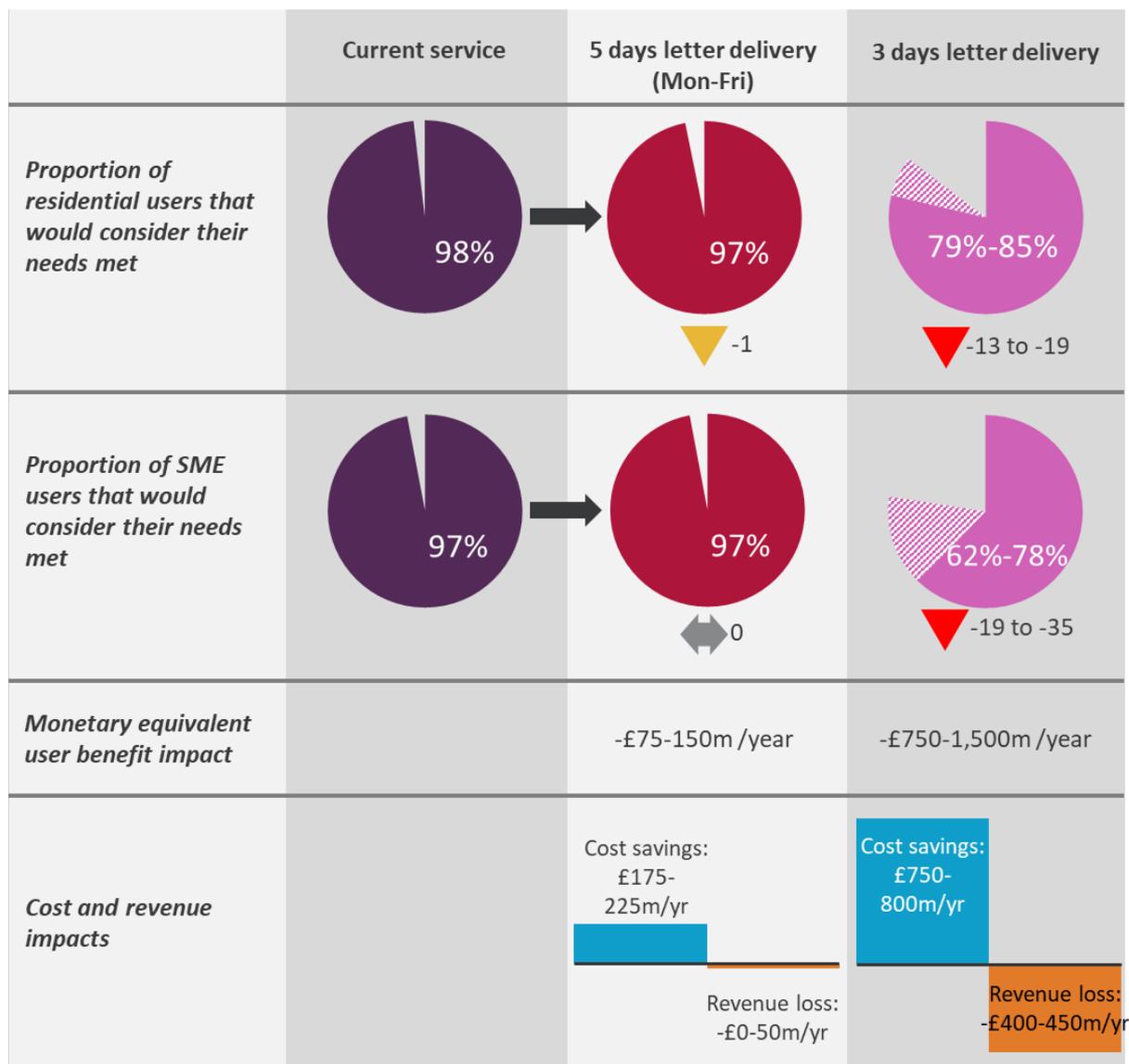
¹²⁸ Ofcom, 2013. Review of postal users' needs, p.51 and p.54.

5. Delivery frequency

Key findings

- The **current service**, delivering letters and parcels six days a week, meets the needs of virtually all users, and this suggests it reflects users' reasonable needs.
- **Five days a week letter delivery frequency** would have a very small impact on residential and SME users, and our research suggested it would continue to meet the needs of virtually all users. This evidence suggests that reducing the frequency of letter deliveries requirement to five days a week would reflect users' reasonable needs.
- **Weekday letter delivery is preferred to Saturday**. Whilst findings are similar for residential users whether the five days are specifically Monday-Friday or include Saturday plus four weekdays, SMEs have a preference for weekday deliveries.
- **Three days a week letter delivery frequency** would have a substantially larger negative impact on users than five days, even though it could also facilitate potentially significantly greater cost reductions.
- In relation to **parcel delivery frequency**, Royal Mail currently exceeds the minimum requirements of the USO by delivering parcels six days a week in response to customer demand and market pressures. We expect the service provided to continue in future. Our findings also suggest users are largely indifferent between Royal Mail delivering parcels five or six days a week.
- There are operational and user benefits of maintaining **frequent collections**. Collections account for a relatively low proportion of Royal Mail's network costs, and so it is likely that the benefits of maintaining the current minimum standards for collection frequency are likely to outweigh any potential costs savings that could be made by collecting items less frequently.

Figure 18: Key findings in relation to letter delivery frequency



Source: Jigsaw Market Research and Ofcom modelling.

Note: Cost savings estimates in the above figure are based on our assumption that Royal Mail is able to implement all operational changes available to it to optimize its network for a re-scoped USO. To the extent that Royal Mail faces contractual or other barriers to making these changes, it may not be possible for it to quickly achieve the full extent of these cost savings in practice.

Introduction

5.1 The minimum requirements set out in the Act require collection and delivery of letters six days a week (Monday to Saturday), and delivery of parcels five days a week (Monday-Friday). Royal Mail’s commercial practice is to exceed these minimum requirements by collecting and delivering parcels six days a week, including Saturday.

- 5.2 This section discusses our findings on whether potential changes to letter delivery frequency would reflect user needs. In particular, we consider the impact on users and Royal Mail of changing letter delivery frequency from six days a week to five days a week. We also look at the impact of changing letter delivery to three days a week.
- 5.3 This section also considers parcel delivery frequency and letter and parcel collection frequency.

Conjoint analysis

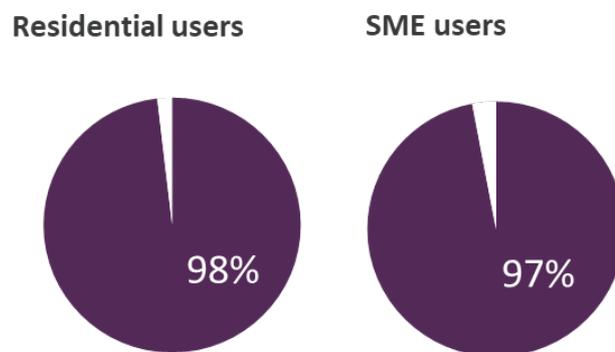
- 5.4 Our 2019 survey asked consumers and SMEs about their views on different aspects of, and hypothetical variations to the USO and whether these “met their needs”, including the number of delivery days. Using the survey results we can understand the extent to which the current USO reflects the needs of users. We used conjoint analysis for this evaluation, a form of discrete choice modelling. This is a standard technique used widely in market research to evaluate consumer preferences for different configurations of a product or service. It is commonly used for designing and pricing a wide range of products and services, to estimate the market share, revenue and profitability of new propositions, and how changes to aspects of the product or service could affect these. The technical details are set out in Annex 4.
- 5.5 Conjoint analysis has advantages over direct questions about which individual aspects of a service are important or valued, which participants often find difficult to answer. This mainly occurs because such direct questions ask them to think about their preferences in a way that is unfamiliar to them, and partly because other factors, such as their desire to appear logical or socially responsible, constrain their responses.
- 5.6 In simple terms, a conjoint exercise asks participants to consider alternative designs of a product (and often the price that would be charged for that design), and state which of the alternatives they prefer. This means that participants evaluate the different designs of products as a whole, which is more reflective of the way people make choices in the real world. It does not ask participants to artificially focus on elements of the service (that may not be particularly relevant to their overall valuation of the service) in isolation from the overall package being offered. By asking enough participants about the choices that they would make between various alternatives, and applying statistical analysis to this data, we can estimate consumers’ implied valuations for different elements of the product, and how these would change if the product specification was changed. This method gives a more reliable picture of what features of a product are really important to participants. For this reason, when considering indications about the relative importance of different aspects of the service, we place more weight on indications from our conjoint exercise than individual answers to direct questions on the importance of certain features.

Current postal service, six days a week letter and parcel delivery

5.7 As shown in Figure 19, our conjoint analysis shows that almost all residential and SME postal users consider that their needs are met by the current service. This was broadly consistent across the range of subgroups of users, as shown in Figure 20.

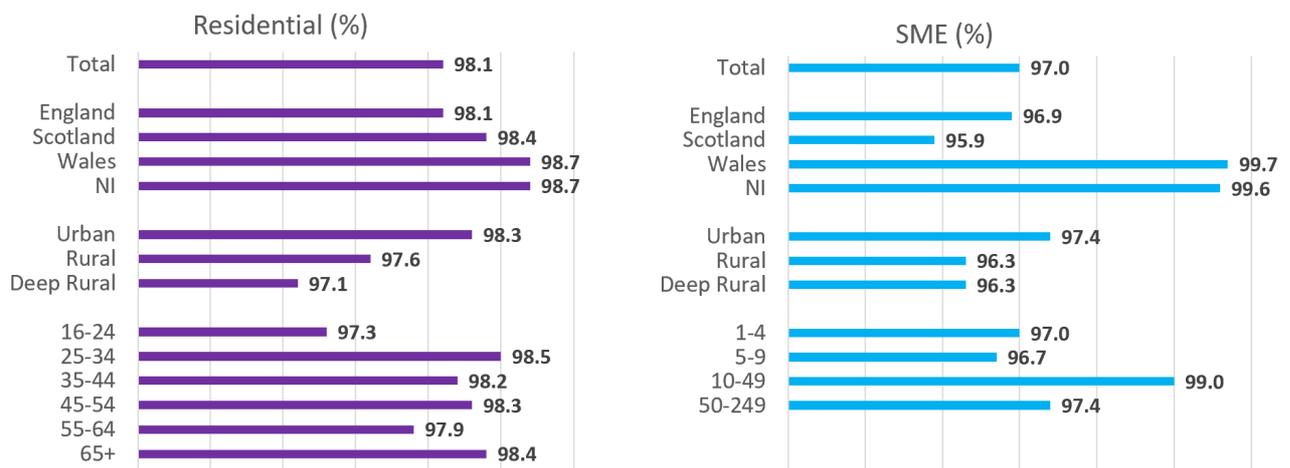
5.8 We further note that the majority of users are satisfied with the postal services they receive from Royal Mail. For residential users, overall satisfaction has remained over 80% in the last few years¹²⁹ and SME users' overall satisfaction with the quality of services they receive from Royal Mail has also increased markedly since 2012.¹³⁰

Figure 19: Proportion of Residential and SME users that consider their needs met by the current service



Source: Jigsaw Market Research.

Figure 20: Predicted proportion for whom current postal service meets needs



Source: Jigsaw Market Research.

¹²⁹ Residential postal tracker survey (2016-18), QG5 – How would you rate your overall satisfaction with Royal Mail?

¹³⁰ In 2012-13, 66% of SMEs that used Royal Mail said they were "satisfied" with the overall quality of services they received from Royal Mail. This has increased to 85% in 2018. SME postal tracker survey (2012-18), QRM2. Thinking generally about the service your organisation receives as a whole, how satisfied are you with the overall quality of the services you receive from Royal Mail as a recipient and sender?

Five days a week letter delivery service, Monday to Friday

- 5.9 As the universal service provider, Royal Mail is required to collect and deliver letters six days a week from Monday to Saturday, and parcels five days a week from Monday to Friday. Royal Mail's commercial practice is to exceed these minimum requirements by also collecting and delivering parcels on Saturdays.
- 5.10 In this section, we consider the evidence on the impact of the minimum requirements for letter delivery being reduced to five days a week (Monday to Friday). We expect that this would end standard letter deliveries on Saturdays.¹³¹ For clarity, we have assumed the requirement to make collections of letters would remain at six days a week from Monday to Saturday and the requirement to collect and deliver parcels would remain unchanged at five days a week from Monday to Friday. However, we have assumed that Royal Mail would continue to deliver and collect all parcels on Saturdays as it does now due to strong commercial incentives. Whilst it is possible that Royal Mail could reduce the delivery frequency of certain parcels, we do not assume this in our analysis.¹³²
- 5.11 In practice, this would mean later deliveries for some items. For example, a First Class letter posted on Friday would typically be delivered on Saturday under the current service, but would instead be delivered on Monday in this scenario. We assume that Special Delivery Next Day items would continue to be delivered on Saturdays, likely sharing the parcel delivery network. We assume other USO services that are processed as standard letters, such as Signed For, would not be delivered on Saturdays. We also assume non-USO letter services, such as bulk mail sent by large businesses, would be treated in the same way.

Reflecting reasonable needs of users

A move to a five day a week letter delivery service (Monday-Friday) would meet the needs of virtually all residential users

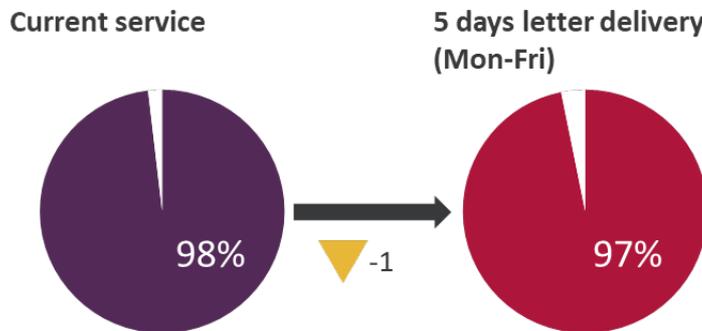
- 5.12 Our 2019 survey allows us to understand how users would react to a potential reduction in delivery days, and the extent to which such a reduction would reflect reasonable needs. We can compare this to the current service to estimate the change in the proportion of the population that would consider their needs met in different scenarios.
- 5.13 A reduction in letter delivery frequency to five days a week would meet the stated needs of virtually all residential users, as shown in Figure 21. Only a very small minority (around

¹³¹ If the requirement to deliver letters on Saturdays were to be removed from the Postal Services Act 2011, it is our expectation that Royal Mail would not continue to deliver letters on Saturdays. However, it would still be open to Royal Mail to exceed USO requirements for letters as it currently does for parcels.

¹³² This scenario is broadly consistent with the period from 2 May – 6 June 2020 when, due to the impact of Covid-19, Royal Mail temporarily suspended deliveries of letters on Saturdays in most areas. During this time, Royal Mail maintained the collection of letters on Saturdays. It also continued to deliver parcels and Signed For and Special Delivery Next Day letters and parcels on Saturdays.

1%) would consider that the service no longer met their needs due to the loss of Saturday letter deliveries.

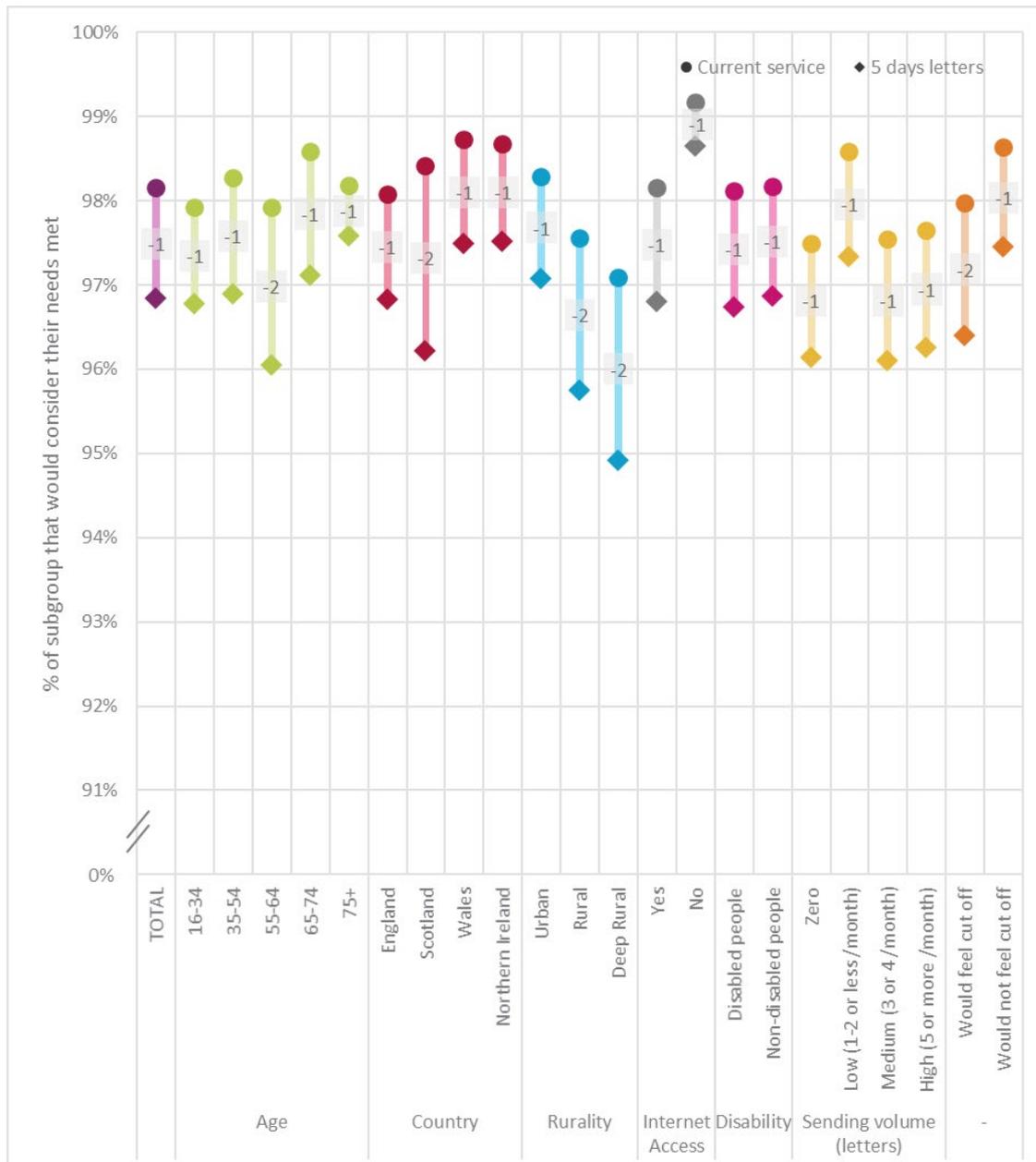
Figure 21: Proportion of residential users that would consider their needs met by a five day a week letter delivery service (Monday-Friday)



Source: Jigsaw Market Research.

5.14 This impact is similar across a range of subgroups of residential users. There are no major subgroups where our estimate of the proportion that would consider their needs met by five day a week letter delivery falls below 94%, and none where the reduction is larger than two percentage points. Based on this, we consider that the impact on any subgroups of residential users is likely to be modest, and unlikely to differ materially from the impact on the general population. We summarise our estimates for a range of subgroups in Figure 22 below. This shows the percentage of different subgroups that would consider their needs met by the current service, and by a five day a week (Monday-Friday) letter delivery scenario, and the percentage point difference between the two.

Figure 22: Estimates of proportion of residential subgroups that would have their needs met in a five days a week (Monday-Friday) letter delivery scenario, showing reduction from current service

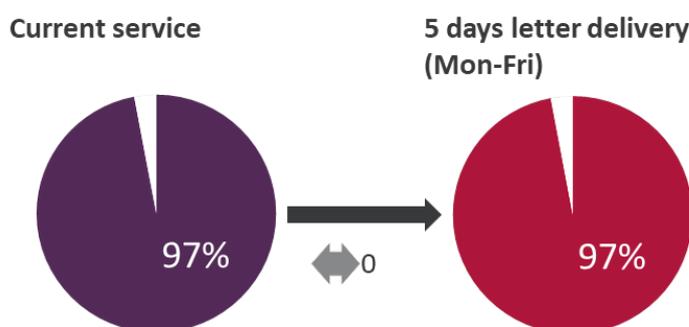


Source: Jigsaw Market Research.

A move to a five day a week letter delivery service (Monday-Friday) would meet the needs of virtually all SME users

5.15 A reduction in letter delivery frequency to five days, Monday-Friday, would have no impact at all on the proportion of SME users that would consider their needs met, as shown in Figure 23. This is likely because many SMEs do not operate on weekends, so Saturday deliveries are not important to them.

Figure 23: Proportion of SME users that would consider their needs met by a five day a week letter delivery service (Monday-Friday)



Source: Jigsaw Market Research.

- 5.16 As with residential users, there is limited variation in the impact on subgroups of SMEs. For subgroups of SMEs, there is negligible difference between the proportion that would consider their needs met by the current service and by a Monday-Friday letter delivery service.

Other indications from the market research

Our quantitative research suggests Saturday deliveries are less important than other features

- 5.17 As set out in Section 4, our quantitative research investigated the relative importance of various features of the service. While we put less weight on this part of our research than the conjoint analysis (for the reasons set out above in paragraphs 5.4-5.6), we consider that that this set of questions still provides useful insight on the relative (rather than absolute) importance of service features. In particular, a clear indication from this was that other aspects of the service are, for the large majority of users, more important than delivery of post (letters and parcels) six days a week. This is supportive of the evidence from the conjoint analysis.
- 5.18 61% of residential participants and 33% of SME participants considered deliveries of post six days a week to be important, whilst around 90% considered affordability and certainty to be important. SMEs in particular place little value on Saturday delivery, with only 17% considering that to be important.¹³³
- 5.19 Our Covid-19 bespoke research similarly showed that other aspects of the service are more important than delivery of letters six days a week. 68% of participants considered letter deliveries six days a week to be important, whilst around 90% considered affordability and certainty to be important.¹³⁴
- 5.20 There was some variation between different subgroups of residential participants. A greater proportion of residential participants considered Saturday deliveries of post

¹³³ 2019 quantitative market research, QE6.

¹³⁴ Covid-19 bespoke research, Slide 17.

important if they were aged under 55, lived in urban areas or sent a high volume of letters. However, these groups still considered affordability and certainty to be the most important features. One possible explanation for some of these differences is that some participants may have focused on parcel services when answering this question. As some people are more likely to be out on weekdays, they may place more importance on the Saturday delivery of parcels. There are few significant differences on this set of questions amongst different subgroups of SME users.

In our qualitative market research, the majority were of the view that Saturday deliveries were not essential to meet their needs

5.21 Overall, the majority of residential and SME participants in our qualitative research accepted that retaining a Saturday delivery of letters was not essential to meet their needs. When considering the need for deliveries of letters and parcels on Saturdays, some residential participants felt that they needed a Saturday service as they were more likely to be at home on Saturdays to receive and open post, but this was more important for parcels than letters. Most SMEs indicated they would be satisfied without a Saturday service, if this fitted with their working patterns.¹³⁵

Quantified impacts on USO user benefits

We have quantified the impact on private user benefits from conjoint analysis outputs

- 5.22 The research outlined above tested whether a potential change to the USO would be unacceptable to users, such that the service would no longer meet their needs. To supplement this, we have also estimated the monetary value that users place on retaining the current service compared to a move to five day a week letter delivery.
- 5.23 We quantify this impact as a price increase for the current service that would have the same impact on users as a change to five day a week letter delivery. We estimate this using outputs from our 2019 survey. In other words, we estimate what, on average, users would be willing to pay to avoid a reduction in service. We can interpret this as the loss of benefits from a change in service, even if overall - despite that loss in benefits - users would still consider that their needs are being met by the service.
- 5.24 We interpret the conjoint analysis with care and advise caution about the precision of these estimates. We focus more on the relative magnitude of different scenarios as a result, for example whether a change is broadly equivalent to a small price increase (say 10%) or to a substantially larger price increase (30-40% or more). We calculate an overall impact using users' current spending on USO services.¹³⁶ Because SMEs spend more overall on post than residential users, the impact on SMEs has greater weight in this calculation of the overall impact. These impacts are calculated on the basis of 2018/19 spending to align with our estimates of cost impacts. They provide a snapshot of how users valued the

¹³⁵ 2019 qualitative research, p.35.

¹³⁶ For example, if users currently spend £2bn per year on USO services, and the impact of a change is equivalent to a 5% price increase, then the overall annual impact is £100m.

service in 2019. We note that as usage of post changes in future, spending patterns and consumer preferences could change to some extent. The impact on users in subsequent years may differ, and could be smaller than these estimates if reduced usage is not offset by increasing importance of post to users. Annex 4 sets out the details of our methodology.

A move to five days a week letter delivery service (Monday-Friday) leads to a small reduction in user benefits

5.25 We have estimated the impact on users of moving to a service with five days a week letter delivery, Monday to Friday. Our results are summarised in Table 1 below, which shows the estimates of the amount users would be willing to pay to retain the current service rather than move to a five day a week letter delivery service. In general, we consider this impact on both residential and SME users to be small; we estimate that residential users would pay 6-10% more to retain the current service, and SME users would pay 2-4% more. In aggregate, this impact is in the region of £100m per year. The overall annual impact is modest compared to annual spending on USO services of around £2.8bn.¹³⁷

Table 1: Impact on user benefits of a five day a week letter delivery service (Monday-Friday)

	Equivalent price increase		Aggregate annual impact
	(%)	(First Class stamp)	
Residential users	6-10%	4-7p	£25-100m
SME users	2-4%	1-3p	£25-75m
TOTAL			£75-150m

Source: Ofcom calculations from Jigsaw Market Research.

5.26 This estimate only quantifies the impact on users of USO products. To the extent that moving to five day a week letter delivery leads to impacts on other non-USO services sent by large businesses (such as bulk and access products) there would be a further loss of benefits for users of those services. This impact is also likely to be small, as we discuss qualitatively at paragraphs 5.33-5.35.

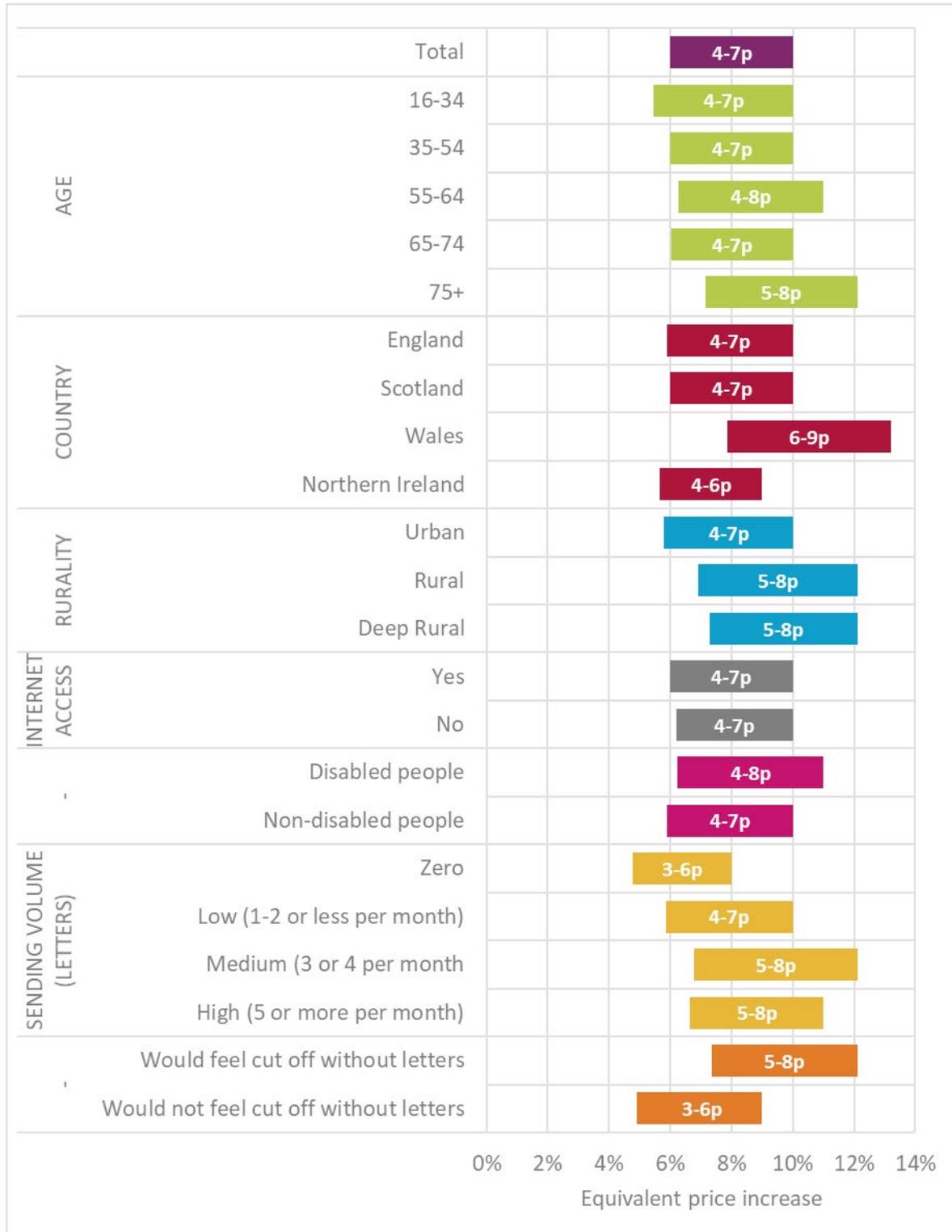
There is limited variation in the impact on private benefits between different subgroups

5.27 We have also considered the impacts on benefits for subgroups of users, to identify whether some user groups might experience a disproportionately larger impact. Figure 24 summarises these impacts for residential users in terms of equivalent percentage price increases (represented by the coloured bars – different colours show different sets of subgroups), and in terms of a representative increase in First Class stamp prices (displayed in the labels). A larger increase means that this group of users would consider themselves

¹³⁷ See Royal Mail regulatory financial statements 2018-19, including international USO services. We note that users derive benefits above their total spending on USO services (i.e. they gain consumer surplus), and so any estimate of the value of postal services will be higher than this. Royal Mail, 2019. Regulatory Financial Statements 2018-19. <https://www.royalmailgroup.com/media/10808/royal-mail-2018-19-regulatory-financial-statements.pdf>

worse off in this scenario. Generally, there is limited variation in the average impact amongst residential subgroups.

Figure 24: Impact of five days a week letter delivery on residential user willingness to pay by subgroup, % equivalent price increase and equivalent increase on a First Class stamp



Source: Ofcom analysis of Jigsaw Market Research.

- 5.28 There is also limited variation amongst different SME subgroups. The impact on sole traders is greater than the overall average, and closer to the impact on residential users, but impacts on other businesses appear negligible.

Knock-on effects of the change

Five days a week letter delivery could require users to switch to more expensive services for a fraction of urgent items

- 5.29 Our quantitative market research indicates that only a minority of letters need to arrive the next day. When thinking about letters they will always need to send by post, residential users suggested that a small proportion (20-30%, dependent on the type of item) would typically need to arrive the next day.¹³⁸ We note that only a subset of that minority would need to arrive on a Saturday. As discussed in Section 6, the impact of removing a First Class service is relatively small for residential users in particular, indicating a generally low need for this service.
- 5.30 Changing the USO such that First and Second Class letters are no longer required to be delivered on Saturday could have consequences for users sending items that need to arrive on a given Saturday. Senders of such items would broadly have two options: post the item earlier so that it arrives on or before the preceding Friday, or use a priority service when sending on Friday such as Special Delivery Next Day (on the basis that this would still be delivered on Saturday).
- 5.31 We expect that for many items ensuring delivery on (or before) Saturday is not likely to be essential. For example, many businesses do not operate on Saturdays, and so Saturday deliveries are likely to be less important for items received by businesses. For items that do need to arrive by a given Saturday, in many cases it is likely that users will be able to adapt by sending items earlier so that they arrive by Friday at the latest.
- 5.32 Therefore, we think that there are likely to be only a small number of items that both need to be received on a Saturday at the latest, and could not be sent earlier to assure this. For this minority of time-critical items, users can use an alternative priority service, though this is substantially more expensive than the current First Class service. Our revenue modelling estimates that only a very small fraction [X%] of stamped First Class volumes would switch to Special Delivery Next Day in a five days a week letter delivery scenario. Given that we expect that this would only apply to a small minority of items, we consider the overall impact of this will be small. If, instead, demand for a lower price express service including Saturday delivery were material, it would be open to Royal Mail to develop such a product.

Certain large users that value Saturday deliveries may have to make changes to adapt

- 5.33 Large users sending bulk mail do not use the USO services that Royal Mail is required to provide to residential and SME customers. Nevertheless, these bulk letters get delivered over the same network and alongside USO letters, so if Saturday delivery was not required

¹³⁸ 2019 quantitative research, Residential QD3b.

under the USO, we assume that Royal Mail would cease Saturday delivery of bulk mail due to cost synergies. Therefore, for completeness, we have sought to understand the views of bulk mailers on five days a week letters delivery, as the letters services they use could be affected as a consequence of changes to the USO.

- 5.34 In our interviews with large users, we found that in most cases there would not be a significant impact on them if there were no deliveries of letters on Saturdays, both as a sender and a receiver. This is because their workplaces are typically closed or less well-staffed. Some consciously avoid sending mail which would arrive on Saturdays, so that they do not prompt consumers to contact them when they have lower staffing levels.
- 5.35 However, there are certain sectors, for example publishing and advertising which place higher importance on a Saturday letters delivery. In publishing, some titles value the publication arriving on Saturdays when readers have more time to read and act upon advertising. Weekly news titles tend to go to print in the second half of the week, targeting arrival on Friday or Saturday when news is topical. There were also advertisers from particular sectors (e.g. financial services) that valued sending in-depth materials to arrive on Saturdays when people have more time to consider them. The removal of Saturday delivery could therefore require these users to adjust their business practices to send letters earlier in the week, or use an alternative premium service that guaranteed Saturday delivery.

Impacts on broader societal benefits

- 5.36 We do not consider that a change to a five day a week letter delivery service would have a significant impact on the broader societal benefits of the USO. The change would maintain a frequent uniform service at uniform prices, so would not significantly affect inclusion. In addition, our research does not suggest that the impact of this change would disproportionately affect some users more than others, including customer groups that may be more likely to be vulnerable.

Impacts on costs and revenues

- 5.37 We believe that a reduction of one letter delivery day per week could lead to a positive net impact on profits of £125-225m per year, both in 2018/19 terms and in 2022/23 terms (accounting for projected volumes and costs).¹³⁹ This is based on our modelling and the assumption that Royal Mail would be able to make all necessary operational changes that we have modelled. We discuss the cost and revenue impacts in this section, and our modelling approach in greater detail in Annexes 5 & 6.

¹³⁹ Our estimates of impacts in 2018/19 terms are based on Royal Mail's costs, revenues, volumes and operations in that year. See Annex 5 for more details on how we have modelled cost impacts and Annex 6 for how we have modelled revenue impacts. In projecting cost impacts to 2022/23 we account for anticipated changes in volumes and wages using Royal Mail's latest Business Plan. As this scenario primarily affects the letter delivery operation, and letter volumes have declined and are projected to continue to decline beyond 2018/19, the number of hours that can be removed is smaller in 2022/23 than it was in 2018/19. However, the cost reduction per hour removed is higher due to wage growth.

Removing Saturday letter deliveries could reduce delivery costs

- 5.38 Our modelling suggests that reducing letter deliveries from six to five days a week could reduce delivery costs. Our modelling assumes that, in response to this change, Royal Mail would stop delivering all letters on Saturday (except special delivery), and so reduce costs by no longer operating on-foot deliveries. We assume that Royal Mail would continue to deliver parcels on Saturday using its van delivery network, and any small parcels that would have been delivered on foot on Saturday would be delivered via this network. There may be some small offsetting cost increases due to diverting greater volumes through the van delivery network on Saturday, and delivering an increased volume of letters on Monday (which would have to absorb letters previously delivered on Saturday).
- 5.39 We have modelled these impacts on costs, and set out our approach in Annex 5. Our estimates are based on our own modelling and should be considered approximations of potential cost savings, should Royal Mail be able to make all necessary operational changes to implement this scenario. They include savings from not delivering non-USO products, such as bulk or access mail, on Saturdays.
- 5.40 In this scenario we estimate potential annual cost savings of £175m-225m, in both 2018/19 terms and in 2022/23, when accounting for anticipated changes in volumes and wages. There is a marginally downward trend in the cost savings achieved in this scenario over time, due to volume changes outweighing wage rate growth, but this is a gradual change and the potential cost savings in 2022/23 are similar to, though slightly smaller than, the potential cost savings in 2018/19.
- 5.41 Royal Mail would incur costs in making operational changes to deliveries on Saturdays. While these transition costs are likely to be material, we do not believe they would be disproportionate to the ongoing cost savings that could be achieved by making the change.

Reducing letter delivery frequency to five days a week could also lead to a small reduction in revenue

- 5.42 We have considered how reductions in letter delivery frequency would impact the volumes and revenues of all relevant products, including both USO and non-USO products. Reductions in letter delivery frequency could lead to changes in demand, switching to and from alternative Royal Mail products, as well as price changes. Annex 6 sets out our approach and our key assumptions to estimate these volume and revenue changes.
- 5.43 In general, we estimate that a move to a five days a week letter delivery service would result in a relatively modest adverse impact on mail volumes, due to some users choosing to no longer send some First Class letters if they cannot be delivered on a Saturday (we assume a proportion of those users would use Special Delivery while the majority would stop using mail). We also assume Royal Mail's First Class bulk letter services would be similarly affected. Given that parcel services and the speed of most letter deliveries would remain unchanged, we expect that most current users of the service would continue to send the same volume of post via Royal Mail as they would have under the current service, noting the general declining trend in letter volumes.

- 5.44 Our modelling also assumes that Royal Mail does not alter its level or structure of prices in response to a change to a five days letter service.
- 5.45 We estimate that the change could lead to a loss of revenues of £0-50m in 2018/19 terms. We estimate the projected revenue impact to be £0-50m in 2022/23 assuming the changes were implemented in time for the full impact to materialise in that year (see Annex 6).

Five days a week letter delivery service, including Saturday

- 5.46 The above discussion has focused on a Monday-Friday letter delivery service. We have also considered how the impact of a reduction in letter delivery frequency to five days a week would vary if the delivery day removed was a weekday, not Saturday.
- 5.47 The impacts on users are broadly similar, though there could be a greater impact on SME users. This is because many SME users place very low value on Saturday deliveries, so five day a week letter delivery that includes only four weekdays is in effect a four day letter delivery service for those users. Impacts on costs and revenues are also broadly the same, though revenue risks could be slightly greater given weekday deliveries are more important for businesses.

Our evidence suggests therefore that reducing the frequency of letter deliveries to five days a week would reflect users' reasonable needs

- 5.48 Five days a week letter delivery frequency would have a very small impact on residential and SME users, and our research suggested it would continue to meet the needs of virtually all users. Our monetary estimate of the loss of benefits to USO users is small, compared to total spending on USO services and smaller than our estimates of potential cost savings from reducing delivery frequency. As a result, we consider that the evidence suggests reducing the frequency of letter deliveries requirement to five days a week would reflect users' reasonable needs.
- 5.49 Whilst our findings are similar for residential users whether the five days are specifically Monday-Friday or include Saturday plus four weekdays, weekday letter delivery is overall likely to be preferred to Saturday, given SMEs' preference for the former.

Three days a week letter delivery service

- 5.50 We have also considered the impact of a more substantial reduction in delivery frequency to three days a week.¹⁴⁰ Our assumption is that a three days a week letter delivery service would be implemented as an "alternate" model, where half the addresses in an area receive letters on one day, and the other half the next day.¹⁴¹ This is operationally easier to implement and allows the continued provision of full-time postal delivery positions. We

¹⁴⁰ We have not given detailed consideration to the impact of a four days a week letter delivery service, as this would not enable the same degree of operational transformation, and therefore has less potential for material cost savings.

¹⁴¹ As opposed to an option where Royal Mail delivers to all addresses on 3 days, and makes no deliveries on the other days of the week.

assume collection and parcel delivery requirements would remain unchanged and that Royal Mail would continue delivering parcels and Special Delivery letters six days a week.

5.51 In practice, this change to delivery arrangements would mean Royal Mail would no longer be required to provide a standard next day delivery or First Class letters service. Though Royal Mail could respond to this change in different ways, for simplicity we have assumed Royal Mail would not offer a standard next day delivery service outside the universal service, but would continue to deliver special delivery items six days a week. We therefore assume Royal Mail would offer a single class (D+3) service, arriving within three days of collection. We assume that other USO services that are processed as standard letters, such as Signed For, would be delivered three days a week. We also assume non-USO letter services, such as bulk mail sent by large businesses, would be treated in the same way.

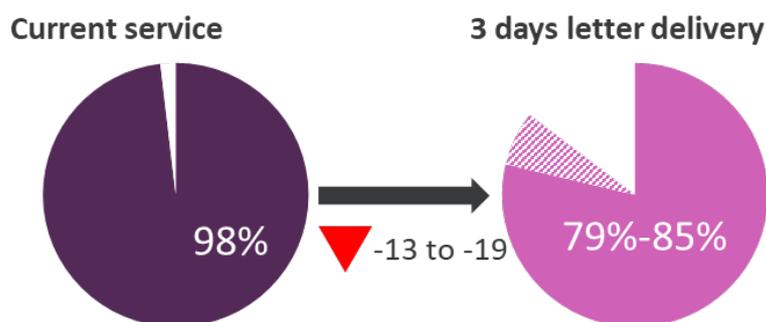
Reflecting reasonable needs of users

5.52 Our market research was not set up to directly assess the service described above with letters delivered three days a week (including Saturdays for half of the addresses) with a D+3 service, and parcels delivered six days a week with First and Second Class services.¹⁴² We therefore present results for a range of scenarios which best approximate the impact of this specific service.

At this point in time, a three days a week letter delivery service would not meet the needs of a substantial minority of residential users

5.53 Our research suggests that a move to a three days a week letter delivery service would lead to a substantial reduction in the proportion of residential users that say it met their needs, meaning only 79-85% would consider their needs met, as shown in Figure 25.

Figure 25: Proportion of residential users that would consider their needs met by a three days a week letter delivery service



Source: Jigsaw Market Research. Solid areas represent lower bound, shaded areas represent upper bound.

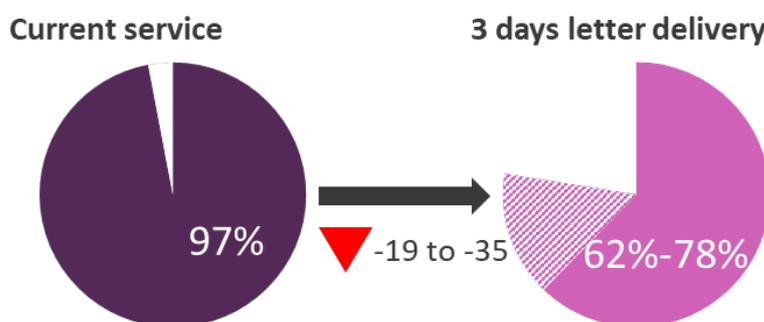
¹⁴² Our conjoint exercise included scenarios where post was delivered to all addresses on Saturday, or no addresses on Saturday. It also assumed that the same delivery service and speed applied to all items, i.e. either both letters and parcels had First and Second Class services or both had a single class service. More detail on our approach to the conjoint exercise is set out in Annex 4.

5.54 The analysis also suggests that this change of service may have a greater negative impact on certain subgroups. Some groups of residential users are less likely to say the service would meet their needs including: those living in Wales (73-83%), Northern Ireland (70-81%) and rural areas (76-84%); disabled people (76-84%); and medium (74-82%) and high senders of letters (74-82%). There are generally small differences between different age groups.

A three days a week letter delivery service would not meet the needs of a substantial minority of SME users

5.55 Our analysis suggests the impact on SME users could be greater than for residential users, with more SMEs (up to nearly 40%) likely to consider their needs no longer met by a reduction of letter delivery frequency to three days a week, as shown in Figure 26.¹⁴³

Figure 26: Proportion of SME users that would consider their needs met by a three days a week letter delivery service



Source: Jigsaw Market Research. Solid areas represent lower bound, shaded areas represent upper bound.

5.56 If delivery was reduced to three days per week, it would be even more important to SME users that those three days were weekdays and did not include Saturday (as discussed in relation to five days delivery above). This is particularly so for SMEs, which do not tend to value Saturday deliveries

Quantified impacts on USO user benefits

A move to a three days a week letter delivery service has a large impact on user benefits from the USO

5.57 To supplement the above assessment, we have also used our survey results to estimate the monetary value of impacts on users of a three day a week delivery service. This suggests that the average impact of a change to a three days a week letter delivery service is likely to be substantial for both residential and SME users, as summarised in Table 2. Residential users would prefer to pay at least 30% higher prices to retain the current service than

¹⁴³ The wider range for SMEs reflects their greater sensitivity to a move to a single class service, and the low value many SMEs place on Saturday deliveries.

make this change, and SME users would prefer a more than 40% price increase (the largest increase tested in our conjoint analysis).¹⁴⁴

Table 2: Impact on user benefits of a three days a week letter delivery service

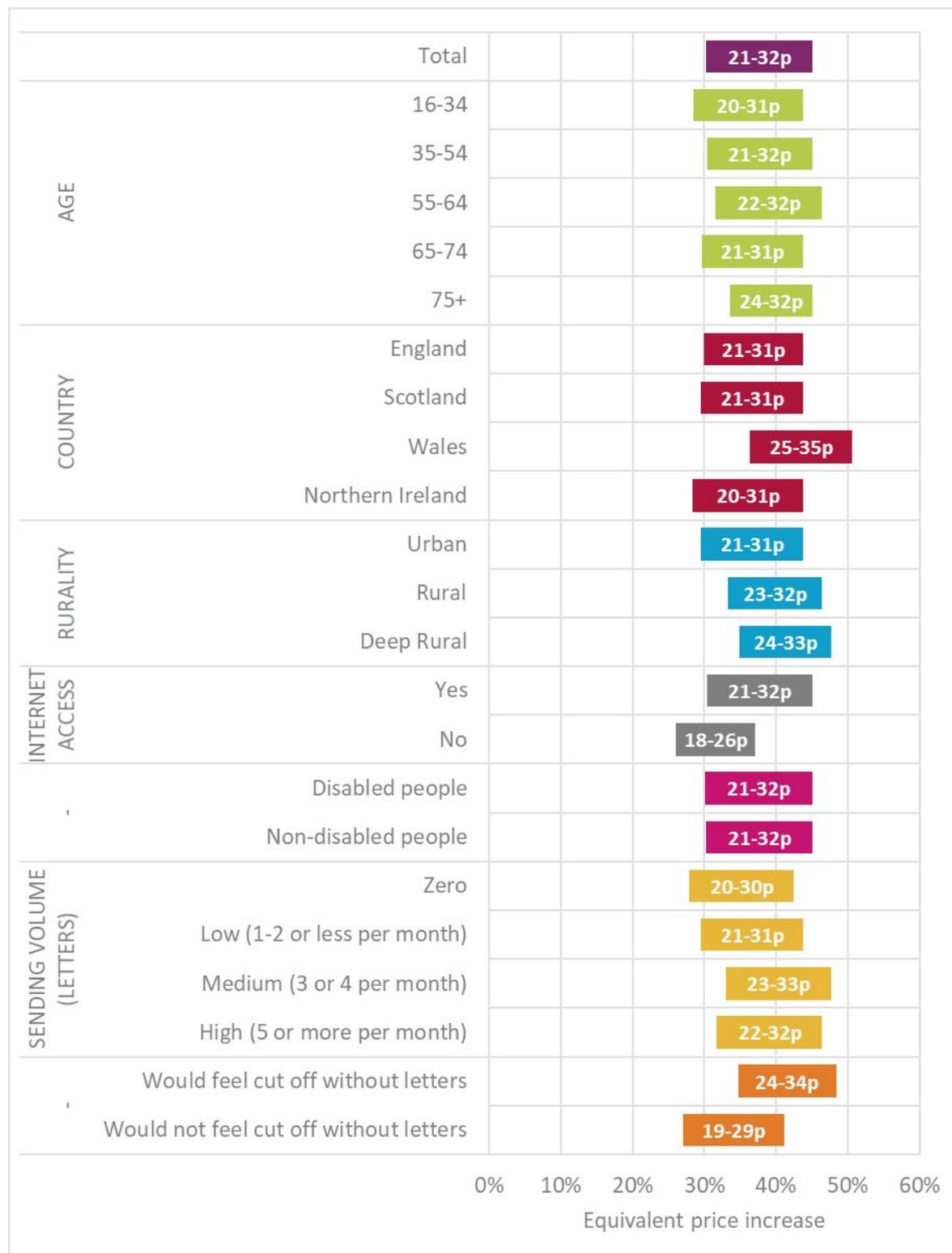
	Equivalent price increase		Aggregate annual impact
	(%)	(First Class stamp)	
Residential users	30-45%	21-32p	£200-500m
SME users	50-70%+	35-50p	£500-1250m
TOTAL			£750-1500m

Source: Ofcom calculations from Jigsaw Market Research.

5.58 We have also considered whether average impacts are greater for certain subgroups. Figure 27 below illustrates these impacts for residential users. This indicates impacts may be somewhat greater for some residential user groups, and potentially in excess of a 40% price increase, including for those living in Wales or rural areas. There is limited evidence of substantial variation amongst subgroups of SME users.

¹⁴⁴ Our conjoint exercise provides indications of the impact of four price steps above current prices – the highest of these steps is around 40% above current prices. Because the impact of a 3 day a week delivery service on SME users is greater than the impact of the highest price step tested (40% above current prices), estimating the level of impact requires extrapolation and so is more uncertain.

Figure 27: Impact of three days a week letter delivery on residential user willingness to pay by subgroup, % equivalent price increase and equivalent increase on a First Class stamp



Source: Ofcom calculations from Jigsaw Market Research.

Knock-on effects of the change

With a three day service a greater proportion of users may need to switch to more expensive services for more time-sensitive and urgent items

- 5.59 As in the case of a scenario resulting in a reduction in letter delivery frequency to five days a week, users of USO services that need an item to arrive on or by a given day, or those sending urgent items, may have to make adjustments. As discussed above, our research and consideration of other factors suggests that for many items delivery on or before a particular day is not likely to be essential.
- 5.60 For those that are time critical, consumers may be able to post many of these items earlier. There are likely to be a relatively small number of items where users would need to use a more expensive priority service. However, this impact is likely to be greater in the case of a reduction to three days per week of letter deliveries than for a reduction to five days a week letter delivery, as there would be more days without letter deliveries.

Certain larger users may have to make changes to adapt to less frequent deliveries

- 5.61 As discussed above, we assume that Royal Mail would also change the frequency of letter deliveries for non-USO bulk mail services, in line with USO services. A USO change would therefore have consequences for users of these products. These products are typically bills, statements and advertising sent by banks, financial services, utilities, public sector organisations and retailers. They also include publications (e.g. news titles and magazines).
- 5.62 As only half of addresses would receive letters on a given day, there could be knock-on effects for senders of these items if they are time sensitive or designed to arrive on a particular day (such as a weekly news publication that senders want to be delivered to users on a particular day). Senders of these items may therefore need to adjust their production process to reflect the fact that not all addresses will receive mail on the same day, or use a premium service (such as Special Delivery Next Day) to guarantee delivery by a given day. More senders may be affected by a greater reduction in delivery frequency to three days a week, and some of these senders may incur costs in making these adjustments.

Impacts on costs and revenues

- 5.63 We believe that a reduction of letter deliveries to every other day (excluding Sundays) could lead to a positive net impact on profits of £300-400m per year in 2018/19 terms. This is based on our modelling and the assumption that Royal Mail would be able to make all necessary operational changes that we have modelled. We discuss the cost and revenue impacts in this section, and our modelling approach in greater detail in Annexes 5 and 6.

Three days a week letter delivery could allow substantial reductions in delivery and processing and logistics costs

- 5.64 A change to a three day a week letter delivery service could provide scope for significant reductions in Royal Mail's costs, primarily through a reduction in delivery costs. It could also lead to savings in processing and logistics by increasing the time available for posted items to reach the delivery office. We estimate potential cost reductions could total around £750-800m per year in 2018/19 terms. These estimates are based on our own modelling and should be considered approximations of potential cost savings, should Royal Mail be able to make all necessary operational changes to implement this scenario.
- 5.65 However, these cost reductions are likely to only be achieved by incurring substantial transition and implementation costs. Given the scale of the change, there are also likely to be significant implementation risks in realising the potential future cost savings.

This substantial change to the nature of the service could lead to significant revenue risks

- 5.66 A reduction of letter delivery frequency to three days a week would represent a large change to the nature of letter deliveries, including for non-USO services, particularly Royal Mail's bulk letter and access services used by large businesses, which make up the majority of letter volumes. As such, it could carry a risk of substantial reductions in letter volumes and revenues for Royal Mail, particularly if it led users (and large users in particular) to re-assess their use of letters and substitute to electronic alternatives or cheaper services. Forecasting this response is difficult as we cannot base predictions on historical responses to price increases or moderate service changes, so the potential impact on revenues is more uncertain for this larger change in service. We estimate this impact could be a revenue reduction of around £400-450m in 2018/19 terms. However, as letter volumes continue to decline, we expect the revenue loss to be considerably lower in future years due to the volume decline in letters and any enduring impact of Covid-19.

Parcel delivery frequency

Current parcel service

- 5.67 The minimum requirements for the universal service include the delivery of parcels (up to 20kg) five days a week, Monday to Friday. Royal Mail currently exceeds these minimum requirements by delivering six days a week in response to customer demand and market pressures.¹⁴⁵ An important driver of this is the demand for Saturday delivery from large senders of parcels (such as online retailers), and Royal Mail's need to compete with other parcel operators to win these contracts.
- 5.68 Our assumption is that Royal Mail will continue to have commercial incentives to deliver parcels six days a week - even if letter delivery frequency were to be reduced - to meet

¹⁴⁵ In its 2020 AGM, Royal Mail noted that it wanted to consider whether there was customer demand for a seven-day commercial parcel service. Royal Mail, 2020. Virtual Shareholder Event September 2020 - AGM Statements Transcript. https://www.royalmailgroup.com/media/11264/royal_mail_agm_statements_transcript.pdf

demand from users, particularly online retailers. However, Saturday delivery of parcels is not secured by the current USO minimum requirements, and so it would still be open to Royal Mail to change this practice in future for some or all parcel deliveries.

5.69 Our research included scenarios to test user responses to a reduction in parcel frequency, which we set out below.

Five days a week parcel delivery service

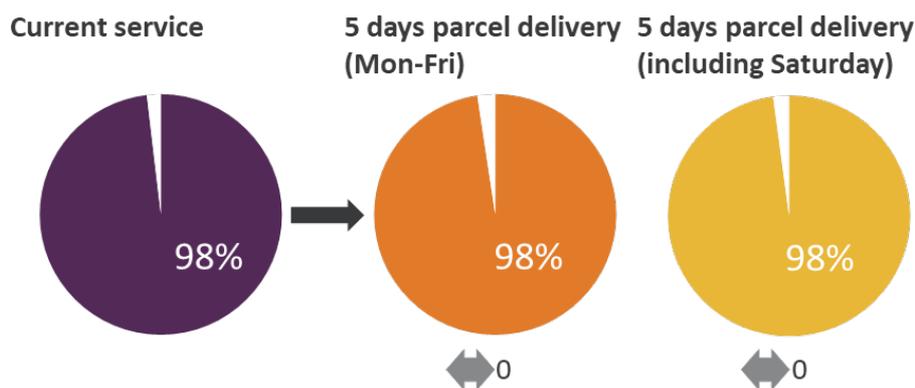
5.70 In this sub-section, we discuss the potential impacts on users if Royal Mail were to start delivering parcels in line with the minimum requirements – five days a week, Monday to Friday. We also consider a variation on this where parcel deliveries are made on four weekdays plus Saturday.

5.71 Our assumption is that other aspects of the current service remain unchanged, such that letters are delivered six days a week. Our assumptions about other services are equivalent to those for letter delivery frequency reductions – specifically that Special Delivery continues to be delivered six days a week, and other services that are processed as standard parcels would be delivered five days a week.

Impacts on users

5.72 Our market research suggests that a reduction in parcel delivery frequency to five days a week would not have a material impact and would continue to meet the needs of virtually all (98%) of residential users, as shown in Figure 28.¹⁴⁶ This impact is similarly small (less than a percentage point difference) across a range of subgroups of residential users.

Figure 28: Proportion of Residential users that would consider their needs met by five days a week parcel delivery service



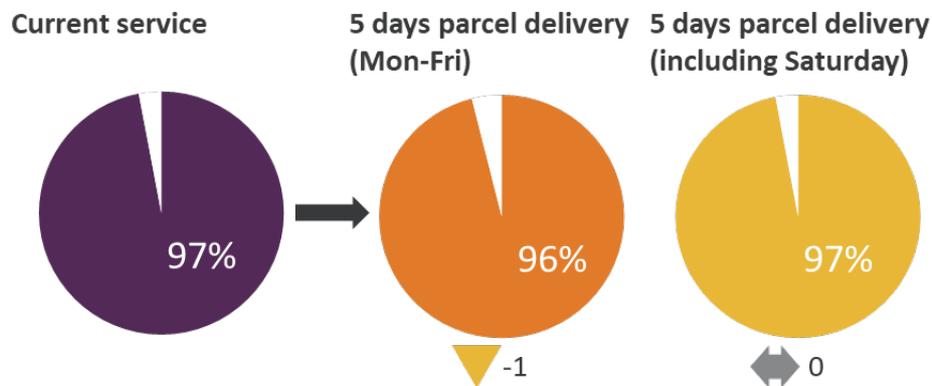
Source: Jigsaw Market Research.

5.73 Our research also suggests a very small reduction (around 1 percentage point) in acceptability for SME users for a Monday-Friday parcel delivery service, as shown in Figure

¹⁴⁶ This may reflect the relative infrequency of parcel deliveries to residential users, meaning that they may consider a five day delivery frequency sufficient. It may also reflect consumers that consider parcel deliveries by other operators separate from the “postal service”.

29.¹⁴⁷ As for residential users, there is no indication that particular subgroups of SMEs would be materially more affected than average.

Figure 29: Proportion of SME users that would consider their needs met by five days a week parcel delivery service



Source: Jigsaw Market Research.

5.74 Our research suggests that impacts on users would be more substantial if parcel delivery frequency were reduced further. A three day a week parcel delivery service would meet the needs of 87-93% of residential users and 78-91% of SME users.

Other indications from market research

5.75 Our qualitative market research suggested that Saturday parcel deliveries were important for some residential users, as they were less likely to be working that day.¹⁴⁸ Our quantitative findings on the importance of various aspects of the service (as discussed in Section 4) suggest that Saturday deliveries (important to 57% of residential users and 17% of SMEs) are less important than other features such as affordability and certainty (important to around 90% of residential and SME users).¹⁴⁹ Our Covid-19 bespoke research suggested that Saturday delivery of parcels was important to 66% of residential users, compared to affordability and certainty which were important to over 85% of residential users.¹⁵⁰

Collection frequency

5.76 Royal Mail is required to collect letters six days a week from Monday to Saturday, and parcels five days a week from Monday to Friday. Royal Mail's commercial practice is to exceed these minimum requirements by also collecting parcels on Saturdays.

¹⁴⁷ In general, many SMEs tend to operate Monday-Friday, so have no requirement to receive parcels on Saturdays. There may be some SMEs that value being able to send parcels that are delivered to consumers on Saturday, hence the slight preference for Saturday deliveries indicated here.

¹⁴⁸ 2019 qualitative research p33.

¹⁴⁹ 2019 quantitative research QE6.

¹⁵⁰ Covid-19 bespoke research, Slide 18.

5.77 In this sub-section, we consider the potential impact of a reduction in minimum requirements for letter or parcel collections.

Impacts on users

5.78 Most participants in our qualitative research were willing to have collection of post reduced to five days a week. When considering further reductions, participants' main concern was for post to be received within two or three days of being sent, and they wanted collection arrangements to achieve this. This provides an indication that a substantial reduction in collection frequency may be less likely to reflect user needs as it would likely result in greater delays between posting and delivery.

5.79 As discussed in Section 4, our 2019 quantitative research found that the availability of a next day service was important to 75% of residential and 80% of SME users. This indicates that speedy delivery is relatively important to users – more important than Saturday deliveries (57% residential, 17% SME) but less important than affordability (92% residential, 89% SME) and certainty (90% residential, 93% SME).¹⁵¹ This could be relevant for collections, as regular collections are required to ensure that items arrive quickly after posting.

Impacts on Royal Mail

5.80 Collections make up a relatively low proportion of Royal Mail's costs. Of a total cost of around £7bn, we estimate collection costs to be around £[X] (c.[X]% of total costs), compared with delivery costs of over £[X] (c.[X]% of total costs).¹⁵² Therefore, any cost savings from reduced collection frequency would likely be small.

5.81 Our understanding is that Royal Mail derives operational benefits from regular collections. Changes to the frequency of delivery do not necessarily require consequential changes to flow through to other parts of the network, which require a steady flow of mail to ensure it runs effectively. To meet required delivery speeds, it is important that mail is not left for multiple days at collection points (e.g. post boxes) before being collected. In addition, processing efficiency is improved if mail is collected regularly rather than large volumes of mail being collected all at once.

5.82 We consider it is likely that the operational and service benefits of maintaining the current minimum standards for collection frequency are likely to outweigh any potential costs savings that could be made by collecting items less frequently.

¹⁵¹ 2019 quantitative market research, QE6.

¹⁵² Royal Mail, 2020. Royal Mail Regulatory Financial Statements 2019/20.
<https://www.royalmailgroup.com/media/11242/rfs-2019-20-signed.pdf>

6. Speed of delivery, quality of service, tracking and additional services

Key findings

- This section sets out our research and thinking on these other aspects of the USO, to provide additional context alongside our assessment of the minimum delivery requirements.
- **Reducing the speed of delivery** by removing the requirement for a First Class service and introducing a single class service has a small impact on residential users, but a larger impact for SMEs. This change could result in a reduction in some Royal Mail costs, namely in processing, logistics and delivery, but is unlikely to allow for substantial savings.
- **Reducing the certainty of the service**, by lowering the percentage of mail required to arrive on time, has some impacts on residential users and greater impacts on SMEs, particularly more substantial reductions in certainty. This change could reduce some costs by allowing some items to be processed more slowly, but is unlikely to allow for substantial cost savings.
- The majority of residential consumers and SMEs consider that **end-to-end tracking** is an important feature of parcel services, but it was not identified as a key enhancement sought to Royal Mail's USO services.
- Users regarded **Special Delivery Next Day, Signed For and Certificate of Posting** as essential. Other services including metering (using franking machines), redirection, insured services and return to sender remain important for users that need to use these services, while others view them as relatively less important in most instances.

Introduction

- 6.1 The main focus of this report is the frequency of deliveries, as discussed above in Section 5. Delivery frequency is part of the minimum requirements, and changes to these are a matter for Government and Parliament. We are not proposing to make changes to other aspects of the USO at this time. However, this section sets out our research and thinking on these other aspects of the USO, to provide additional context alongside our assessment of the minimum delivery requirements.
- 6.2 Our market research included the speed of delivery, quality of service (the percentage of mail required to arrive on time), views on tracking, and some key additional services such as Special Delivery Next Day, Signed For and Redirection. In this section, we highlight our main findings in relation to these aspects of the service.
- 6.3 In contrast to the number of delivery days covered in the previous section, which would require Parliament to change the minimum requirements of the USO, some of the features in this section are set by Ofcom in the universal postal service order.¹⁵³ These features can

¹⁵³ The Postal Services (Universal Postal Service) Order 2012 (SI 2012/936).
http://www.legislation.gov.uk/uksi/2012/936/pdfs/uksi_20120936_en.pdf.

be modified by Ofcom after an assessment under section 30 of the Act has been carried out.¹⁵⁴ Other features described below are minimum requirements set by Parliament in s.31 of the Act and cannot be modified by Ofcom.¹⁵⁵

Speed of delivery

- 6.4 In our research, users were presented with a scenario where both First (D+1) and Second Class (D+3) are replaced by a single class service arriving two or three days after posting (which we term D+2 or D+3). Our research was designed such that users were asked to consider this change applied to all items. However, in practice it could be applied to letters or parcels only, or Royal Mail could choose to offer a faster service for some items outside the USO.
- 6.5 We assume that a premium next day delivery service would remain part of the USO, such that Special Delivery Next Day would be available for urgent items. Our assumption is that Royal Mail would adjust the speed of delivery for other non-USO products to match the speed of the single-class USO service.

Impacts on user benefits

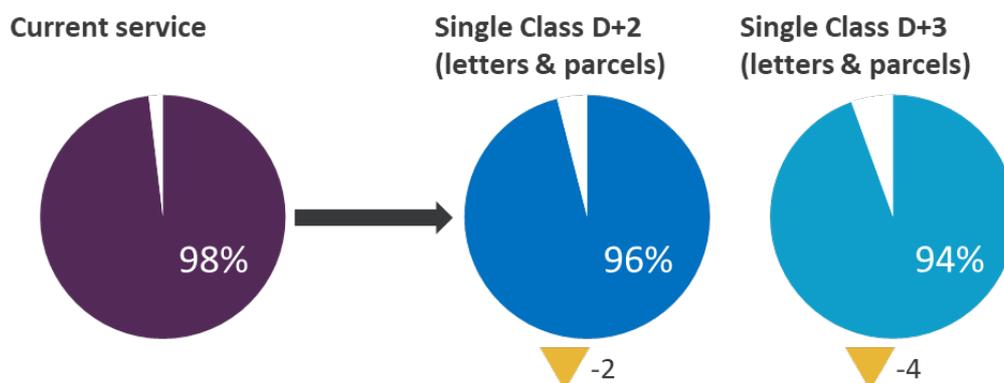
A single class service leads to moderate reductions in acceptability, particularly if delivered to D+3 timescales

- 6.6 Our market research presented scenarios where the same speed and reliability of service applied to both letters and parcels, and so results presented here are on this basis.
- 6.7 We estimate that a single class D+2 or D+3 service would meet the needs of around 95% of residential users, as shown in Figure 30. There is limited variation amongst residential subgroups, though the impact may be slightly greater for high volume senders of letters and parcels.

¹⁵⁴ Under Section 30 of the Act, Ofcom can amend the Order if we consider that necessary following an assessment of the extent to which the market for the provision of postal services in the UK is meeting the reasonable needs of the users of those services.

¹⁵⁵ This is the case for registered and insured services, services for the blind or partially sighted and for legislative petitions and addresses.

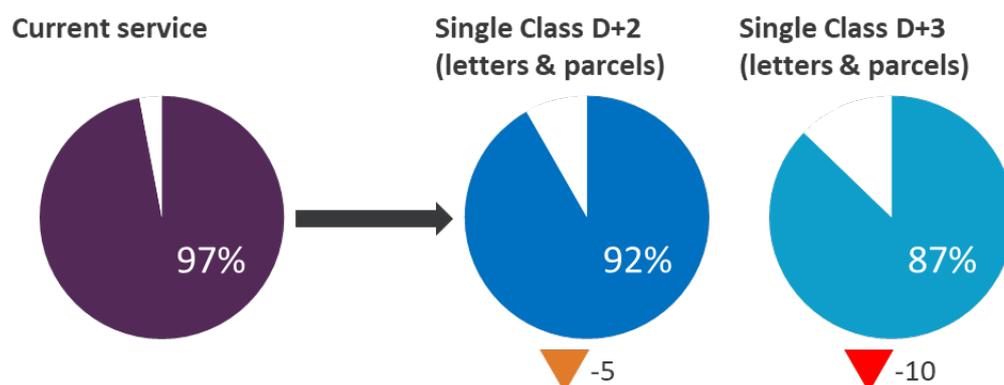
Figure 30: Proportion of Residential users that would consider their needs met by a single class D+2 or D+3 service



Source: Jigsaw Market Research.

6.8 It appears that this change would have a greater impact on SME users, and would meet the needs of 92% (for a D+2 service) and 87% (for a D+3 service), as shown in Figure 31.

Figure 31: Proportion of SME users that would consider their needs met by a single class D+2 or D+3 service



Source: Jigsaw Market Research.

Other indications from market research

6.9 Our quantitative research provides further indication of the relative importance of next day delivery services, as discussed in Section 4. This indicates that a substantial majority of residential (75%) and SME (80%) participants regard next day delivery as important. More participants were more likely to consider this important than delivery six days a week or on Saturdays.¹⁵⁶ Our additional Covid-19 bespoke research confirmed this, suggesting next day delivery was important to 72% of participants for letters and 71% for parcels.¹⁵⁷ “Normally

¹⁵⁶ 2019 quantitative research, Residential QE5, Base all weighted residential = 4596; SME QE5, Base all weighted SME = 971.

¹⁵⁷ Covid-19 bespoke research. Slides 17 and 18.

gets there the next day”, was the main stated reason for using First Class (although many of the other factors were also noted).

- 6.10 In our qualitative market research, many participants were supportive of the provision of a Single Class (D+2 or D+3) service, in particular for letters which in most cases were seen as less urgent. For those participants that used First Class services, when asked about their reasons for using the service, most of the responses had little to do with speed of the service. However, a minority of participants expressed concerns about implementing a single service and some saw inherent value associated with maintaining a First Class service.¹⁵⁸

A single class service would lead to small reductions in residential user benefits and greater impacts for SME users

- 6.11 Our analysis of survey results suggests a Single Class service would have a small impact on average willingness to pay for residential users, particularly if provided as a D+2 service. These impacts may be slightly greater for residential users living in Wales and rural areas and those that send a higher volume of letters. The average impact on SMEs appears greater, which may suggest SMEs place more importance on maintaining a next day First Class service. The aggregate annual impact is around £250-350m for a D+2 service and £500-750m for a D+3 service. Table 3 summarises these impacts.

Table 3: Impact on willingness to pay of Single Class D+2 or D+3 service

		Equivalent price increase		Aggregate annual impact
		(%)	(First Class stamp)	
D+2	Residential users	2-5%	1-4p	£25-50m
	SME users	14-18%	10-13p	£200-300m
	TOTAL			£250-350m
D+3	Residential users	9-13%	6-9p	£50-150m
	SME users	25-35%	17-25p	£400-700m
	TOTAL			£500-750m

Source: Ofcom calculations from Jigsaw Market Research.

Knock-on effects of the change

- 6.12 USO users sending urgent items may have to make adjustments to their use of postal services. As previously discussed, the evidence suggests that only a minority of items are likely to be time critical and not able to be sent earlier. We anticipate that Royal Mail would also alter the speed of delivery for non-USO services. Slower delivery could also affect users of these products that rely on faster deliveries, such as publishers of topical

¹⁵⁸ 2019 qualitative research, pp.33-34.

magazines. Senders of such items may need to use more expensive priority services such as Special Delivery Next Day.

Impacts on costs and revenues

- 6.13 Replacing First Class and Second Class letter services with a single class service could reduce Royal Mail's costs in processing and logistics, as items would not need to reach delivery offices as quickly. However, we expect these savings to be modest in comparison to changes in delivery frequency.
- 6.14 We have modelled these impacts on costs, and set out our approach in Annex 5. We estimate that the removal of first class could reduce costs by £100-175m per year in 2018/19 terms, if Royal Mail is able to implement all of our modelled operational changes in practice. These estimates include savings from reducing scope of service for non-USO products, such as bulk or access mail.
- 6.15 While Royal Mail would be likely to incur some costs in making these operational changes, we expect the transition costs of removing First Class services and changes to processing and logistics arrangements to be relatively modest.
- 6.16 Moving to a new single class product (D+2 or D+3) and therefore removing First Class next day services could risk substantial reductions in revenue. A number of assumptions are required to model the impacts including the price of the new single class services, but our modelling suggests a significant risk to revenues. Our modelling assumes that items currently sent by First Class would largely be sent using the lower priced Single Class service, but a significant proportion of the volumes will be lost as users would stop using mail (see Annex 6 for an explanation of our approach and our key assumptions). We estimate the revenue impact would be around £200-375m per year in 2018/19 terms.

Quality of service and certainty

- 6.17 Royal Mail is currently required to meet quality of service standards (mail delivery targets) set by Ofcom at 93% of First Class mail to arrive next working day, and 98.5% of Second Class mail to arrive within three days of collection.¹⁵⁹ Our research assessed the implications of reducing these standards to 90% or 80% for all First and Second Class items.
- 6.18 Reducing quality of services standards in this way would mean that users sending mail would be less certain that what they have sent will reach its destination on time. Reduced certainty through lower quality of service standards is likely to have some consequential effects on other elements of USO services, for example, mail sent using Signed For, which is an add-on to First and Second Class services, would also be less likely to arrive on time. However, Special Delivery Next Day would remain a guaranteed service, and would be

¹⁵⁹ Royal Mail is also subject to a range of other performance targets, as set out in DUSP 1, such as for Special Delivery Next Day items.

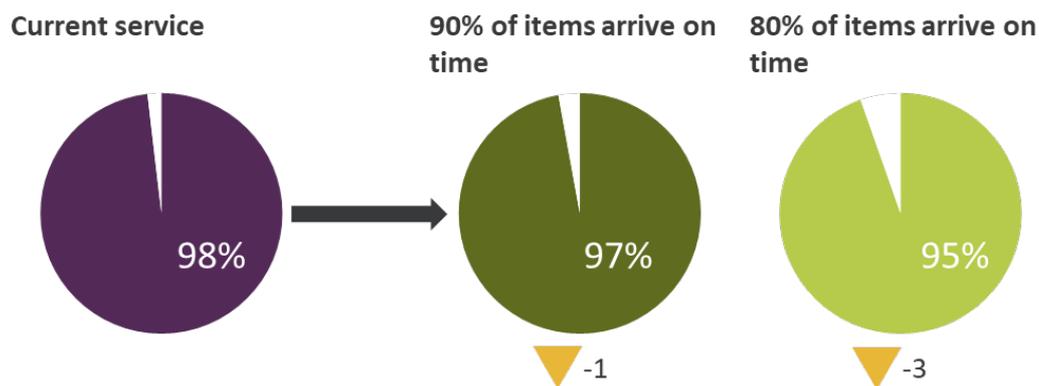
unaffected. For non-USO services, it is our expectation that large users' letters would also be affected by this change in quality of service standard.

Impacts on user benefits

A reduction in certainty has some impacts on acceptability for residential users and greater impacts from SME users

- 6.19 Our conjoint exercise assumes that the same quality of service standards apply to both letters and parcels. We therefore assess conjoint results for the impact of reducing quality of service for both letters and parcels.
- 6.20 We estimate that for the current service scope, a reduction in quality of service targets to 90% would meet the needs the vast majority of residential users (around 97%). Reducing targets to 80% would be unacceptable to more users, but still meet the needs of the vast majority (95%), as shown in Figure 32. We also found limited variation amongst residential subgroups.

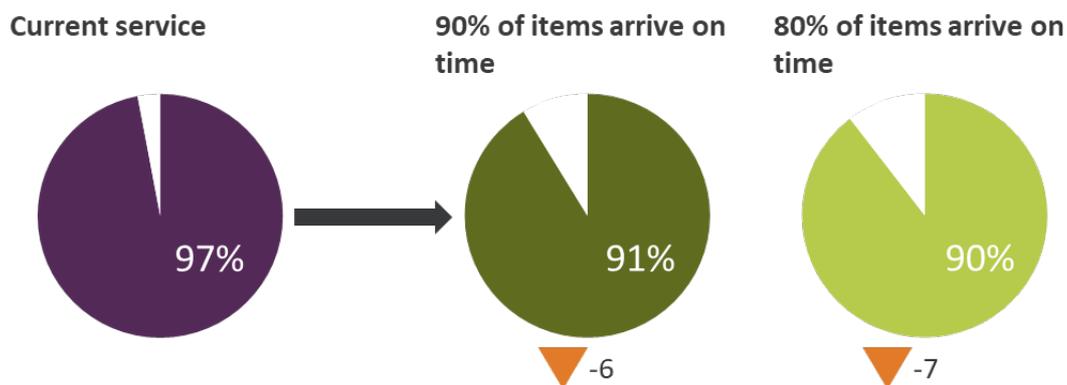
Figure 32: Proportion of Residential users that would consider their needs met by the current service where 90% or 80% of items arrive on time



Source: Jigsaw Market Research.

- 6.21 The impacts on SMEs appear to be larger, as we estimate a greater proportion would not consider their needs met by this reduction in certainty of service, which would meet the needs of around 90% of SME users, as shown in Figure 33. There is limited variation among subgroups.

Figure 33: Proportion of SME users that would consider their needs met by the current service where 90% or 80% of items arrive on time



Source: Jigsaw Market Research.

Other indications from market research

- 6.22 As discussed in Section 4, our quantitative research¹⁶⁰ provides further indication that certainty is important to users, with 90% of residential participants and 93% of SME participants considering it important that 90% of post is delivered on time. This indicates that a reduction in quality of service could have a significant impact. Our additional 2020 research also found that this was important to 87% of participants in relation to letters and 88% in relation to parcels.¹⁶¹
- 6.23 Our qualitative research found that participants were generally not prepared to accept lower quality of service requirements, especially if other aspects of the service were reduced. This aligns with the wider finding that certainty in terms of when mail would arrive was seen as key. However, it is worth noting that most people were unaware of the current quality of service requirements and often believed the requirement to be lower than 93% for First Class.¹⁶²

A reduction in certainty leads to a reduction in user benefits, particularly for SMEs

- 6.24 Our conjoint analysis suggests this change would have a relatively small impact on the benefits residential users derive from the service, and a potentially greater impact on SME users, and impacts are greater if targets were reduced to 80%, as shown in Table 4.

¹⁶⁰ 2019 quantitative market research, QE6.

¹⁶¹ Covid-19 bespoke research. Slides 17 and 18.

¹⁶² 2019 qualitative market research, p.35.

Table 4: Impact on willingness to pay of reduced quality of service

		Equivalent price increase		Aggregate annual impact
		(%)	(First Class stamp)	
90% of items arrive on time	Residential users	2-5%	1-4p	£25-50m
	SME users	5-7%	3-5p	£200-300m
	TOTAL			£250-350m
80% of items arrive on time	Residential users	9-14%	6-10p	£50-150m
	SME users	20-35%	14-25p	£300-700m
	TOTAL			£500-750m

Source: Ofcom calculations from Jigsaw Market Research.

Knock-on effects of the change

- 6.25 For some users and some items, the certainty of the service will be critical. We expect many such items would be sent by Special Delivery Next Day in any case, and so would be unaffected by this change to quality of service. There may be a small number of additional items that users need to switch to the more expensive Special Delivery Next Day service (or an electronic alternative) due to the reduction in certainty of standard services. This could affect both users of USO and non-USO services.
- 6.26 From our interviews with large users, we learned that many value knowing on which day mail will arrive with a high degree of certainty. These include banks, public sector organisations and advertisers. For example, when banks issue replacement bank cards they typically use different mail classes to ensure a gap between arrival of the card and the PIN code to minimise the risk of fraud. Public sector bodies issuing fines value knowing when mail will arrive so that the deadline set for payment is reasonable. Many, including public bodies and advertisers, also like to know when mail will arrive so that they can ensure that their contact centres have adequate staffing levels to respond to consumer inquiries.

Impacts on broader societal benefits

- 6.27 Changes in the certainty of delivery times could increase the geographic variation in quality of service.¹⁶³ This is because items delivered slower than the target may be likely to be more difficult or costly addresses to reach, such as in remote rural areas. Therefore, this change could carry the risk that users in these areas receive a materially poorer service than the rest of the country.

¹⁶³ The following postcode areas are already exempt from quality of service targets for First Class mail because of their remoteness: HS, the Outer Hebrides postcode area which covers the islands making up the Outer Hebrides Island archipelago; KW, the Kirkwall postcode area, which covers certain areas in the North of Scotland, including the Orkney Islands; and ZE, the Lerwick postcode area, which covers the Shetland Islands in Scotland.

Impacts on costs and revenues

- 6.28 Reducing quality of service standards could lead to reductions in costs, as Royal Mail would be able to process and distribute some items more slowly, allowing it to reduce the number of items sent on planes and the volume of overnight traffic. We have not modelled these impacts on costs in detail. However, we estimate these could be of the order £75-125m per year in 2018/19 terms, based on a scenario in which Royal Mail is only required to deliver 80% of its First Class mail within the D+1 specification.
- 6.29 Royal Mail may incur some costs in making these operational changes, but we anticipate these are likely to be small.
- 6.30 We also estimate that reductions in quality of service standards could lead to material reductions in revenue, primarily due to customers switching to electronic alternatives due to the reduction in certainty of postal services. We estimate this risk to revenues could be around £75-125m per year in 2018/19 terms.
- 6.31 These potential revenue losses could offset the cost savings, such that it may reduce profitability in practice.

Tracking on parcel services

- 6.32 Our quantitative research suggests that the majority of consumers and SMEs consider end-to-end tracking as an important feature of parcel services, when presented as a standalone feature, for looking up and tracking the journey of their parcel online.¹⁶⁴ There were also no substantial differences on the perceived importance of tracking from a sender and receiver perspective. For example, among residential consumers, 74% regarded tracking as important when sending parcels, compared to 78% when receiving parcels.
- 6.33 However, tracking was not identified as a key reason for why users sometimes use other providers than Royal Mail. For example, among both residential consumers and SMEs only 4% said that they use other providers when sending parcels so that they could track their deliveries.¹⁶⁵ In addition, improvements to the standard and level of tracking was not identified as a key improvement sought to Royal Mail's service, especially relative to other aspects such as competitive prices and delivery times.¹⁶⁶

Additional USO services

- 6.34 As well as frequent collections and deliveries and First and Second Class services, Royal Mail is required to offer certain additional services to users. These include well-known services such as Special Delivery Next Day (Guaranteed by 1pm); Signed For (an add on to

¹⁶⁴ 2019 quantitative research, p.76, p.82.

¹⁶⁵ 2019 quantitative research, p.14, p.25.

¹⁶⁶ 2019 quantitative research, pp.95-96.

First Class and Second Class services); Certificate of Posting; and Redirection. They also include several services which are used less frequently, and by specific groups of users.

- 6.35 We asked participants in our qualitative research for their views on many of these additional services. We asked participants whether they considered specific services to be “essential”, “nice to have” or “not required”. As part of our quantitative research, we asked further questions about Redirection services.
- 6.36 Most participants did not have a complete knowledge of the range of services available, or an understanding of all the features of these services. This meant that they generally decided that most services were “essential” or “nice to have”.¹⁶⁷ Except where highlighted below, there was a high degree of alignment in terms of the relative importance attached to each service by residential and business users.
- 6.37 We explain our findings in more detail below, first considering findings in relation to the services which derive from the minimum requirements, followed by those that derive from the Order.

Table 5: Universal Postal Service minimum requirement, Royal Mail brand name and explanation of key features

Minimum requirement	Royal Mail brand name and key features
Registered and insured items service(s)	<p>Special Delivery Next Day Guaranteed by 1pm: is a registered, tracked service which guarantees delivery of mail by 1pm the next working day, includes insurance and requires a signature on delivery. Senders have the option of buying additional levels of insurance cover.</p> <p>Signed For: is a registered service which requires signature on delivery for First Class or Second Class mail in the UK. Includes standard compensation for loss and damage.¹⁶⁸</p>
Services for the blind or partially sighted persons	Articles for the blind: enables blind and partially sighted people to send certain items First Class through the post free of charge.
Legislative petitions and addresses	Petitions to Parliament, Addresses & Petitions to the Queen: enables the sending free of charge of petitions and addresses to the Sovereign, and petitions to members of UK Parliaments and Assemblies.

Source: the description of these services is based on Royal Mail’s website (2020) and Ofcom analysis.

¹⁶⁷ Our qualitative research participants identified Special Delivery Next Day; Signed For; and Certificate of Posting as “essential”. They identified meter mail (franking); redirection; insured services; and return to sender as “nice to have”. They identified poste restante as “not required”.

¹⁶⁸ Signed For also meets the requirement to offer First Class and Second Class services with the addition of proof of delivery.

Special Delivery Next Day

- 6.38 When describing their current use of and main needs from postal services, participants in our qualitative research said that they used Special Delivery Next Day (Guaranteed by 1pm) when sending important and urgent items which needed to arrive the next day, sometimes by a certain time. They had also used Special Delivery Next Day services where they needed the reassurance of proof of delivery.¹⁶⁹
- 6.39 When considering the importance of USO services, most felt that Special Delivery Next Day was “essential”. However, many were unclear about all of its features, typically using it for the guarantee of next day delivery, rather than the 1pm delivery deadline, insurance or tracking components of the service.
- 6.40 Insured services, offered as part of Special Delivery Next Day, tended to be considered most useful when sending parcels as these often had a clear monetary value. Insurance was less frequently thought to be useful when sending letters, as they often did not have a clear monetary value. However, some participants valued insurance when sending letters which contained important items, for example passports.¹⁷⁰
- 6.41 Tracking, offered as part of Special Delivery Next Day, tended to be used by SMEs when sending parcels, and by those sending parcels who use online marketplaces to sell goods¹⁷¹. Tracking was felt to be useful to confirm delivery of an item, or to give customers up-to-date information about delivery times. It could also help to minimise the time spent by senders and receivers trying to find out where an item was, and when it would arrive.¹⁷²
- 6.42 In terms of pricing, participants typically used Special Delivery Next Day infrequently so did not know how much it cost. When told the price, they often felt that it was fairly expensive, and they often did not require all the features of the service. Guaranteed next day delivery was typically the most important feature, but some did not need delivery by 1pm the next day. Further, when sending letters, they often did not need insurance or tracking. Some said that because they used it so infrequently, they gave little thought to the price when they used it.
- 6.43 In a scenario where First Class services were no longer required by the USO, and there was only a slower, single class service offered, many noted that the next day guarantee service offered by Special Delivery Next Day would become more important. Some expressed concern about the pricing of Special Delivery Next Day, which is a premium service, if they had to use it more regularly for next day services. Some also expressed concern that, if Special Delivery Next Day were not within the USO, a next day guaranteed next day service may not be offered commercially by Royal Mail to remote parts of the UK.¹⁷³

¹⁶⁹ 2019 qualitative research, p.20.

¹⁷⁰ 2019 qualitative research, p.20.

¹⁷¹ Tracking enables a sender to monitor progress of an item through the postal system.

¹⁷² 2019 qualitative research, p.21.

¹⁷³ 2019 qualitative research, p. 29, p.32.

Signed For

- 6.44 As well as Special Delivery Next Day, participants in our qualitative research reported using Signed For services for important and urgent items which needed to arrive the next day. Both services were also used where they needed the reassurance of proof of delivery.¹⁷⁴
- 6.45 Signed For was seen as one of the most important USO services. Some felt this because it could be recommended when sending legal or government documents so that there was a record of an item having been received. Needing a signature on delivery was also felt by participants to raise the importance of a letter in the eyes of the recipient. Like Special Delivery Next Day, Signed For was not used often by participants, but when used it was seen as “essential”.
- 6.46 We found that many participants were unclear about the difference between Signed For and Special Delivery Next Day, and in particular whether Signed For guaranteed delivery next day (which it does not).¹⁷⁵

Articles for the blind and legislative petitions and addresses

- 6.47 We did not seek the views of participants on the two free services which are minimum requirements in the Act: (i) services for the blind; and (ii) petitions and addresses to the Sovereign, and petitions and addresses to parliaments and assemblies. This is because we consider that both services provide clear social benefits as well as benefits to their users. Services for the blind and partially sighted provides a free, First Class service to a specific group who may be more dependent on postal services¹⁷⁶. Legislative petitions and addresses support democratic engagement.

Table 5: USO services which derive from the Universal Postal Service Order, Royal Mail brand name and explanation of key features

Order requirement	Royal Mail brand name and key features
Certificate of Posting	Certificate of Posting: is a receipt which provides proof of posting. It is free of charge and available from post office counters. It can be used in connection with compensation claims for lost or damaged items.
Meter mail	Metered mail refers to a method of payment or payment channel for Royal Mail services where customers (typically SMEs) pre-pay for postage and apply an impression to the envelope, label or wrapper using a franking machine licensed by Royal Mail.

¹⁷⁴ 2019 qualitative research, p.20.

¹⁷⁵ 2019 qualitative research, p.32.

¹⁷⁶ Royal National Institute for the Blind told us that the Articles for the Blind service is valued by them, local support agencies and blind and partially sighted people, and that it was important that the scope of the service is not diminished.

Redirection services	Redirections: the service of redirection of all mail addressed to a particular recipient from one address to another for a specified period of time.
Return to Sender	Return to Sender: is the service whereby the customer receives a letter with the correct address but the wrong name, and can return it by writing “return to sender” or “not known at this address” on the envelope and putting it back in a post box or returning it to a post office. Where it can identify the sender, Royal Mail then delivers it back to the sender.
Poste restante	Poste restante: a service which allows users to have mail delivered to a post office. The address of the post office is used as the customer’s postal address. It is required to be free of charge.
Retention	Keepsafe: a service through which Royal Mail holds customers’ mail for up to 100 days at their local delivery office, and delivers it on their return.

Source: the description of these services is based on Royal Mail’s website (2020) and Ofcom analysis.

Certificate of Posting

- 6.48 Certificate of Posting was ranked in the middle of the table in terms of the importance of USO services that we tested in our qualitative research. Participants saw this service as equivalent to a receipt which offers proof of postage, which should be available free of charge on request.
- 6.49 Senders of parcels saw it as particularly important, as did those selling items using online marketplaces and SMEs. Both tended to see it as an essential service. However, senders of letters typically saw it as less important and more of a “nice to have”. Some participants felt that Certificate of Posting was less useful because it replicated what was offered as part of other services e.g. Signed For.¹⁷⁷

Meter mail (franking)

- 6.50 Our quantitative research found that, while most SMEs use stamps when sending letters, 14% of SMEs use metered/franked mail (and 9% use metering/franking for parcels). This compares to only 3% of SMEs that use the bulk mail services offered by Royal Mail, and 2% that use bulk mail services provided by other postal operators. Among those SMEs that use metered/franked mail when sending letters or parcels, 61% find it ‘very important’ to their business to be able to use this method, and a further 24% regard it as ‘important’.
- 6.51 Our qualitative research found that, although many SMEs do not use metered services (via franking machines), some do have a continuing need for metered services. For those SMEs that do use metering, this payment method gives them flexibility in applying postal

¹⁷⁷ 2019 qualitative research, p.32.

markings to variable volumes of letters and parcels at discounted rates. They do not need to commit to minimum volumes of mail. So, some SMEs appear to value the availability of an alternative way of accessing postal services if large bulk mail propositions do not meet their needs. We also estimate that the costs of leasing a franking machine are low.¹⁷⁸

Redirection

- 6.52 Redirection was felt to be of moderate importance when compared with other USO services we tested in our qualitative research. Those that had used the service said that they used it for convenience and peace of mind. However, those that had chosen not to use it had found work around options i.e. collecting post from the new occupiers, or they did not mind if they missed some post, so felt that it was more of a “nice to have”. Other participants were not aware of the existence of the service but could appreciate its benefits. SMEs tended to see it as a slightly less important service than residential participants.¹⁷⁹
- 6.53 There was widespread agreement that an affordable Redirection service was an important part of the USO. However, there were mixed views about the pricing of the service. Residential participants who had used the service, or who could imagine using it in the future, felt that it offered reasonable value for money. However, the pricing felt expensive for larger households, those on lower incomes and those who moved regularly.¹⁸⁰ Some participants commented that the level of the pricing should mean that Redirections should be both reliable and effective, however they reported experiencing problems.¹⁸¹
- 6.54 SMEs, particularly small businesses, were more likely to see Redirection pricing as prohibitive for them. Smaller SMEs pointed to the fact that the pricing structure did not take account of the size of a business, or the volume of mail it received, and they felt that this could be seen to be unfair.¹⁸²
- 6.55 We also tested views on redirection services and their affordability in our quantitative research. Of the residential participants who had moved in the last three years, 38% had used the Redirection service. Those that did not use the service were asked the reason

¹⁷⁸ The monthly cost of a low volume franking machine is likely to be around £20-£40 (excluding expenses associated with printing ink, labels, etc). See: <https://www.frankingmachineexperts.co.uk/how-much-franking-machine-cost/>. For a machine with a monthly lease cost of £40, a business would at a minimum need to send four letters per day using First Class rates (£0.63) in order to cover this cost (assuming on average there are 20 working days in a given month).

¹⁷⁹ 2019 qualitative research, p.33.

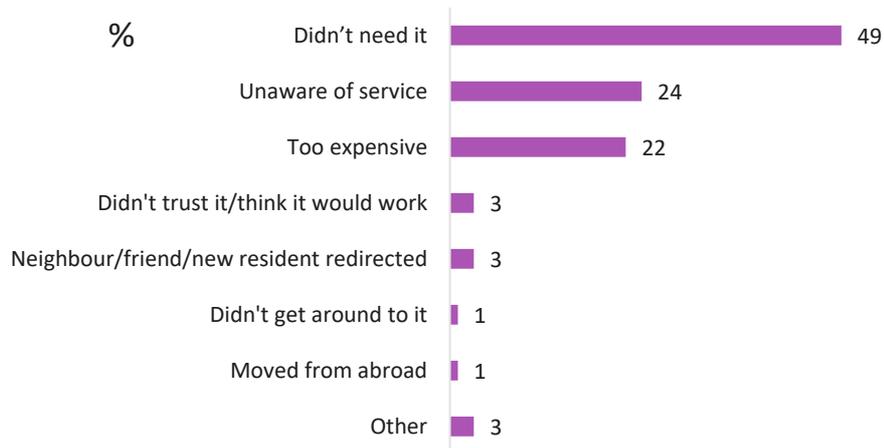
¹⁸⁰ Residential participants in our qualitative research were presented with residential redirection pricing which applied at the time the research was conducted. This reflected the lead applicant + extra person pricing structure Royal Mail introduced in March 2019. In March 2019, Royal Mail introduced a concessionary scheme offering a 20% discount on the price of a 3-month or 6-month UK residential redirection if you rent your home and receive Job Seeker’s Allowance or Pensions Credits. This was not highlighted to participants. See: <https://www.royalmail.com/personal/receiving-mail/redirection>

¹⁸¹ These problems included delays in receiving post, some post not being redirected or going missing, and difficulties resolving problems with Royal Mail’s customer services. In relation to delays, we note that the redirection process means mail goes first to the old address and is then forwarded First Class to the new address. This means at least an extra day being added to the mail’s journey. See 2019 qualitative research, p.29.

¹⁸² SME participants in our qualitative research were presented with business redirection pricing which applied at the time the research was conducted.

why. Nearly half (49%) said that they did not need it. Around a quarter (24%) were unaware that the service existed, and just over a fifth (22%) said it was too expensive.¹⁸³

Figure 34: Reason for not using Royal Mail redirection service – residential



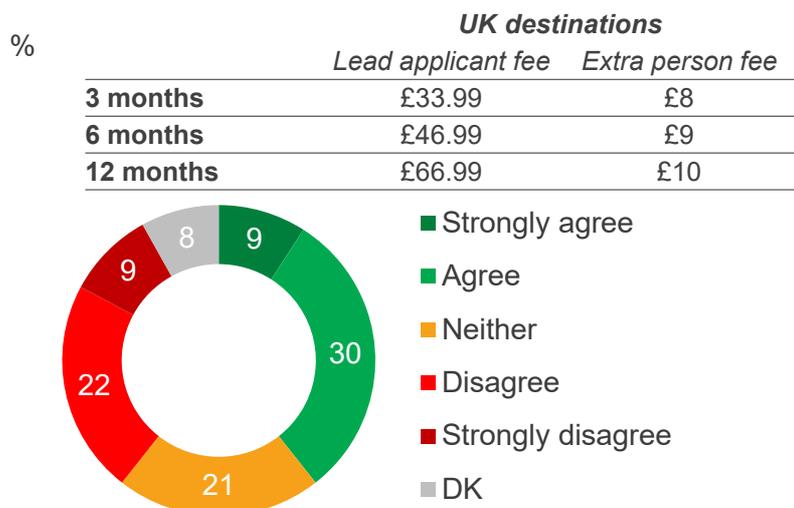
Source: Jigsaw Market Research.

6.56 In terms of value for money offered by the Redirection service, 39% of residential participants agreed that the service offered value for money (rising to 65% for those that had used the service). Those in deep rural areas had higher levels of agreement (45% compared to 39%). Those on lower incomes were less likely to agree: 29% of those with household incomes under £11,500 a year agreed that the service offered good value for money, compared with 47% of those with household incomes more than £50,000 a year.¹⁸⁴

¹⁸³ Residential participants in our quantitative research were presented with residential redirection pricing which applied at the time the research was conducted.

¹⁸⁴ Since March 2019, Royal Mail has offered concessionary pricing on UK residential redirections if you rent your home and receive certain benefits. See: <https://www.royalmail.com/personal/receiving-mail/redirection>

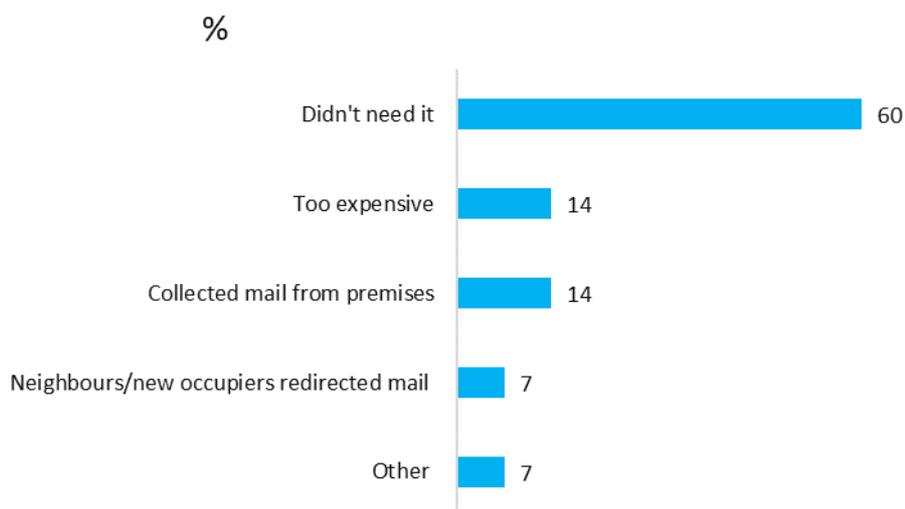
Figure 35: Does Royal Mail redirection offer value for money? - residential



Source: Jigsaw Market Research.

6.57 Among SMEs, of those that had moved premises in the last 3 years, 44% had used the Redirection service. Again, those that did not use the service were asked the reason why. 60% said that they did not need it. 14% said it was too expensive, 14% said that they collected mail from their old premises, 7% said that others redirected the mail for them, and 7% listed the reason as “other”.¹⁸⁵ Other typically included work around solutions e.g. putting a note in the window with their new address.

Figure 36: Reason for not using Royal Mail redirection service - SME

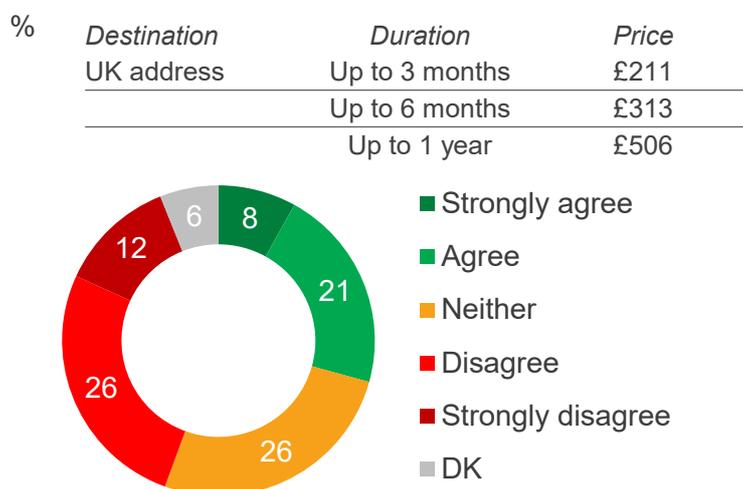


Source: Jigsaw Market Research.

¹⁸⁵SME participants in our quantitative research were presented with business redirection pricing which applied at the time the research was conducted. Due to the small base size (fewer than 50 participants), this finding should be treated with a degree of caution.

6.58 In terms of value for money offered by business redirection, 29% agreed that the service offered value for money (rising to 48% among those that had used the service, and 49% among larger SMEs (with 50-249 employees)). However, 38% disagreed that the service offered value for money.

Figure 37: Does Royal Mail redirection offer value for money? - SME



Source: Jigsaw Market Research.

Return to Sender

6.59 Participants in our qualitative research ranked Return to Sender as one of the less important USO services, more of a “nice to have”. Participants had a range of views on the service, largely depending on whether they had used it or felt that they had benefited from it.

6.60 Some users reported writing “return to sender” on items, but others said that they threw away post addressed to people not known at their address. A minority of participants said that they had benefited from the service.¹⁸⁶ Some SMEs said that receiving mail returned to them via Return to Sender helped them to manage their customer mailing lists, but other businesses had not used it.

6.61 In discussion, participants generally concluded that the product was unreliable as it was dependent on the recipient taking action. Some felt that it should not be “funded by” or be part of the USO, as it was the responsibility of businesses to ensure that their mailing lists were accurate. They felt that if they were not, those businesses should pay for incorrectly addressed mail that was returned to them.¹⁸⁷

Poste Restante

6.62 Poste Restante was ranked as the least important USO service by participants in our qualitative research, with the majority feeling that it was “not required”. People generally

¹⁸⁶ 2019 qualitative research, p.33.

¹⁸⁷ 2019 qualitative research, p.33.

had not heard of it or used it, and after explaining its features, the majority of participants saw it as 'old-fashioned'. Some suggested that the service felt as though it had been conceived when post was the main form of communication.

- 6.63 While some recognised the value of the service for certain groups of people, for example those living and working in different areas, foreign nationals working in the UK and tourists, it was seen as a niche service. Participants generally felt that it should be paid for by those that used it, and that it did not need to be required by the USO or be free of charge.
- 6.64 Because there is low awareness of this service, participants generally had little experience of it. To understand more about the benefits, we would need to carry out research with users of the service.

Keepsafe

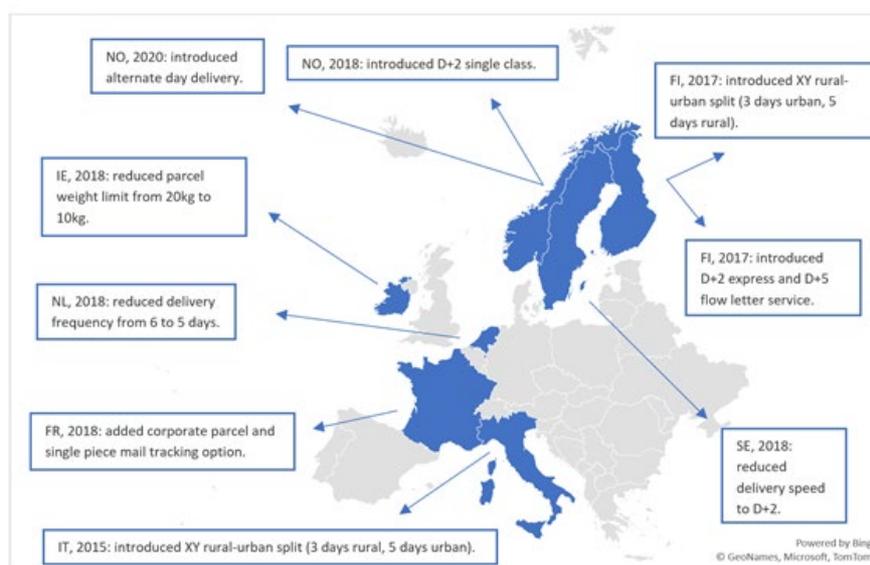
- 6.65 We did not seek the views of participants in our qualitative research on Keepsafe, which is a service where Royal Mail holds a customer's mail at their local delivery office for a period of time typically while the customer is away. This was because there were constraints on the number of additional services that we could include in our research, and we expected Keepsafe to have social benefits. For example, it may help to reduce crime in unoccupied properties by stopping mail from building up on doormats for a period of time. There may also be benefits of the service to organisations which have regular periods away from their workplaces (such as schools).

A1. International context and experiences

Introduction

- A1.1 The trends we have outlined in the UK’s postal market are not changes that the UK is experiencing alone. Internationally, many countries are experiencing similar trends in their own postal markets, with postal users relying less on sending and receiving letters and relying more on sending and receiving parcels. This change in user behaviour has led to a marked increase in parcel volumes and a marked decrease in letter volumes across most countries.
- A1.2 As a response to this, several countries have adjusted, or are considering adjusting, the specification of their USO, typically reducing the service requirements imposed on the designated USO provider. We understand that the decisions to introduce these changes have been taken for a range of reasons, including to try and achieve cost-savings, thereby potentially improving the financial sustainability of the USO.
- A1.3 The following figure demonstrates some of the different changes which have been introduced across parts of Europe.¹⁸⁸ Some of the changes displayed are explored in more detail as case studies, below.

Figure A1.1: Examples of different changes to USOs across Europe



Source: Ofcom analysis.

- A1.4 The trends in letter and parcel volumes noted in the paragraphs above should be considered within the context of the ongoing Covid-19 pandemic. Whilst Covid-19’s impacts on the international postal sector are still emerging, the pandemic appears to have

¹⁸⁸ Changes to the equivalent of the universal service obligation have also been explored in countries outside Europe, such as in Canada and New Zealand.

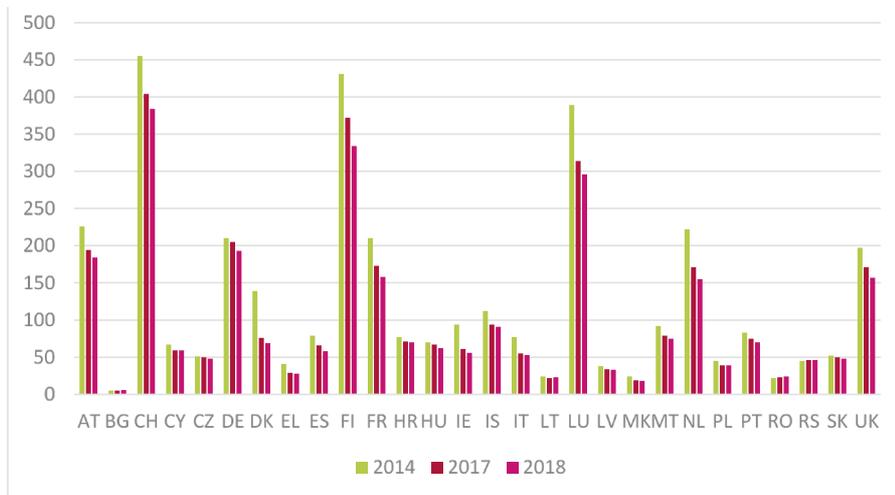
generally accelerated pre-existing trends (i.e. rising parcel volumes/falling letter volumes). Overall, between January and May 2020, cross-border mail volumes (i.e. mail sent between different countries) fell 21% for all mail classes (letter, parcel, express) when compared to the same period last year.^{189, 190} In addition to this, Covid-19’s impact on domestic mail volumes has varied, with a number of EU countries reporting a “marked increase” in domestic mail volumes, often due to a marked increase in online shopping. Other EU countries have found a “stabilising or dropping” of domestic mail volumes. This has happened because the fall in letter volumes has not been compensated by an equivalent or larger rise in parcels. In part, this could be explained by some countries having low household internet penetration, and therefore relatively underdeveloped e-commerce.^{191, 192} This suggests that while the general trends have accelerated, the individual impacts of Covid-19 have been felt differently throughout parts of Europe.

A1.5 This section sets out evidence on changing volumes in other countries and the changes, or potential changes under consideration, in the specification of specific countries’ universal postal services.

International trends

A1.6 The aforementioned changes in mail volumes (both letters and parcels), caused by changing user behaviour, are outlined in the following two tables:

Figure A1.2: Total Letter Volume per capita/per year (EU)



¹⁸⁹ Universal Postal Union, 2020. The COVID-19 crisis and the postal sector. p.8.

<https://www.upu.int/en/Publications/Factsheets-backgrounders/The-COVID-19-crisis-and-the-postal-sector>.

¹⁹⁰ For context, the growth trend (measured from January 2019 until the first few months of 2020) has been, for the most part, positive, with some slight variation due to seasonal changes. The UPU note in the same report that year-on-year growth rates in the first few months of 2020 have been permanently measured in the negative, in a way that cannot be explained by seasonal change.

¹⁹¹ Universal Postal Union, 2020. The COVID-19 crisis and the postal sector. pp.17-18.

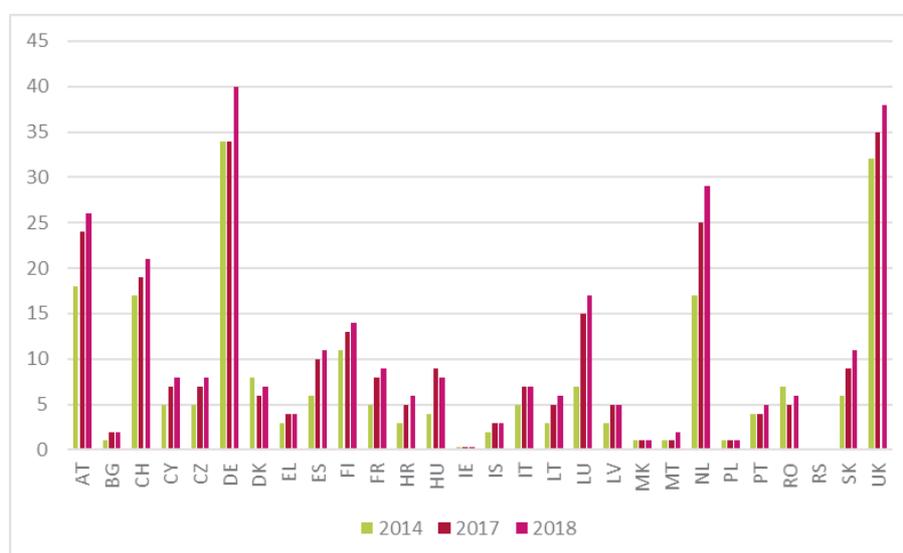
¹⁹² There are also several other drivers besides internet penetration which affect parcel volumes, such as trust in online e-commerce stores and the cost of technology needed to access e-commerce platforms.

Source: European Regulators Group for Postal Services (ERGP).

Notes: see full report for full list of notes.

A1.7 The above graph demonstrates a clear and consistent trend of falling letter volumes across nearly all countries. Among the above countries, the UK has experienced the eighth largest fall in letter volumes per capita between 2014-2018 (from 197 to 157 letters per capita, a decrease of -20%).¹⁹³ Of note is the fact that not only have several of the countries with larger letter volume per capita decreases than the UK made changes to their USO service specification (e.g. Finland, Netherlands)¹⁹⁴, but countries with smaller letter volume per capita decreases than the UK have also made changes (e.g. Italy, Republic of Ireland)¹⁹⁵, demonstrating that such changes are being made at different stages of letter volume decline.

Figure A1.3: Total parcel volume per capita/per year (EU)



Source: European Regulators Group for Postal Services (ERGP).

Notes: see full report for full list of notes.

A1.8 A similar, but inverse, comparison can be drawn from the above graph when compared to Figure A1.2. There has been a steady, consistent increase in parcel volumes across the listed countries. The UK has had the joint-fourth largest increase in parcel volumes (from 32 to 38 parcels per capita, an increase of 19%). This ties the UK with Germany, both increasing by 6 parcels per capita when compared to 2014.¹⁹⁶ From this, it is clear that the relative percentage increase and decrease in volumes for letters and parcels across the UK have been widespread and significant, demonstrating a shift in user behaviour.

¹⁹³ The European Regulators Group for Postal Services, 2019. ERGP PL II (19) 37 Report on Core Indicators. p.50. <https://ec.europa.eu/docsroom/documents/38864/attachments/1/translations/en/renditions/native>.

¹⁹⁴ See below for case studies on both countries.

¹⁹⁵ Similarly, see below for a case study on Italy.

¹⁹⁶ The European Regulators Group for Postal Services, 2019. ERGP PL II (19) 37 Report on Core Indicators. p.51.

International experience of changing USO specifications

- A1.9 This section summarises the experience of some countries that have already adjusted, or are in the process of adjusting, the Universal Service Obligations in their country. Changes to USO requirements that have been (or are currently being considered) by countries within the European Union should be considered in light of the ongoing review of the Postal Services Directive¹⁹⁷ by the European Commission, taking advice from the European Regulators Group for Postal Services (ERGP). The European Commission is currently reviewing the directive framework, including the potential to adjust its scope to reflect “the developments in technology and the fundamental changes in user demand in recent years”.¹⁹⁸
- A1.10 The sections below consider just a few of the many changes that countries from across the world have implemented. These changes have varied from adjusting delivery speeds (e.g. Sweden),¹⁹⁹ introducing a single class postal service (e.g. Norway)²⁰⁰, trial delivery away-from-the-door (e.g. Canada)²⁰¹ and the removal of a particular USO service where it is considered that the market is already meeting postal user needs (e.g. Republic of Ireland).²⁰² Three areas – change of delivery and collection frequency, the introduction of a single class and geographical differentiation – are outlined below, exploring the common trends in specific postal markets where changes have been made, what the impacts of these trends have been on the financial sustainability of the country’s USO and what changes have been, or are being made, in response by the country’s national regulatory authority (NRA) and/or government.

Delivery and collection frequency

- A1.11 A change in the ‘frequency’, or number of days a week the post is delivered or collected, is a change that has been adopted by several countries. Within the EU, legislation states that, while geographic exceptions are allowed, delivery and collection of universal service letters and parcels must be carried out at least five days per week.²⁰³ As a result, many EU countries have only ever provided for five days of delivery and collection per week.

¹⁹⁷ The Postal Services Directive (97/67/EC), amended by Directives 2002/39/EC and 2008/6/EC.

¹⁹⁸ The European Regulators Group for Postal Services, 2019. ERGP PL I (19) 18 Press Release Opinion on the review of the regulatory framework for postal services, p.51.

<https://ec.europa.eu/docsroom/documents/36201/attachments/1/translations/en/renditions/native>.

¹⁹⁹ Copenhagen Economics, 2018. Reports on USO Net Costs in Iceland, p.35.

https://www.copenhageneconomics.com/dyn/resources/Publication/publicationPDF/4/454/1535975317/report-on-uso-net-cost-in-iceland_public-version.pdf

²⁰⁰ Posten Norge, 2018. Financial Report 2018, p.13. [https://www.postennorge.no/en/report-archive/_/attachment/inline/f7f94dec-a73e-4d1a-91e1-](https://www.postennorge.no/en/report-archive/_/attachment/inline/f7f94dec-a73e-4d1a-91e1-0207e21ee7c9:cf67d07f81cf372a700e79466e580f0b21e7124e/Financial%20Report%202018.pdf)

[0207e21ee7c9:cf67d07f81cf372a700e79466e580f0b21e7124e/Financial%20Report%202018.pdf](https://www.postennorge.no/en/report-archive/_/attachment/inline/f7f94dec-a73e-4d1a-91e1-0207e21ee7c9:cf67d07f81cf372a700e79466e580f0b21e7124e/Financial%20Report%202018.pdf)

²⁰¹ Canada Post, 2014. Canada Post’s transition to community mailbox delivery will begin in fall 2014 in 11 communities across Canada. https://www.canadapost.ca/cpc/en/our-company/news-and-media/corporate-news/news-release-detail.page?article=2014/02/20/canada_posts_transit&cat=newsreleases&cattype=announcements

²⁰² Commission for Communications Regulation, 2018. Review of the Universal Postal Service Specification: Response to Consultation and Decision, pp.1-21 <https://www.comreg.ie/publication/review-of-the-universal-postal-service-specification-response-to-consultation-and-decision>

²⁰³ Article 3(3), The Postal Services Directive (97/67/EC), as amended by Directives 2002/39/EC and 2008/6/EC

- A1.12 Like the UK, some European countries, through their national law, exceed the EU’s minimum requirements and provide for six days of deliveries and collections within their USO (see tables A1.1/A1.2 below). However, in response to changing market conditions, several of these countries have adjusted the specification of their USO to reduce the delivery and/or collection frequency to the five day minimum, whilst others are considering doing so.
- A1.13 The two tables below detail countries where there is currently a five day minimum service, and those whose national requirements exceed the EU’s minimum and provide a six day service. Within this six day service, some countries provide six days of letter deliveries only, some provide six days of parcel deliveries only, and some provide for both. Following this, the section goes on to detail two case studies of countries that have recently reduced their delivery frequency from five to six days.

Table A1.1: Delivery frequency of priority letters specified under USO requirements:

As a general rule (i.e., excluding exceptional circumstances), how many days of the week does the NRA or government oblige the USP to deliver priority letter post items?	
5 days per week	AT, BE, BG, HR, CY, CZ, EE, FI, EL, HU, IS, IE, IT, LV, LT, LU, NL, NO, PL, PT, RO, SK, SI, ES, SE, CH
6 days per week	FR, DE, LI, MT, UK
No specific requirements	DK*

Source: Copenhagen Economics.

Note: “CZ, DE, LU, ES - have no differentiation between priority and non-priority. *DK – priority letter (D+1) is outside the USO... IT – the requirement is five days per week, except for the rural areas affected by the XY delivery model...”

Table A1.2: Delivery frequency of parcels specified under USO requirements:²⁰⁴

As a general rule (i.e., excluding exceptional circumstances), how many days of the week does the NRA or government ensure delivery of parcels in the universal service?	
5 days per week	AT, BE, BG, HR, CZ, DK, EE, EL, HU, IS, IE, IT, LV, LI, LT, LU, NO, PL, PT, RO, SK, SI, ES, SE, CH, UK
6 days per week	FR, DE, MT
No specific requirements	CY, FI, NL

Source: Copenhagen Economics.

²⁰⁴ We note here that, in this figure, the Netherlands are listed as having “No specific requirements”. Despite this, however, several sources of information strongly suggest that the Netherlands is required (bar exceptional circumstances) to deliver parcels/letters at least five days per week, in line with EU legislation. Sources demonstrating this include the Dutch Ministry of Economic Affairs ([here](#)) and PostNL’s own website ([here](#)).

Netherlands: In 2014, the Netherlands adjusted the specification of its USO by reducing the delivery frequency for letters from six to five days.²⁰⁵ The delivery frequency for parcels remained at six days. By way of context, the Netherlands has experienced similar changes in postal user behaviours to many other countries, with fewer users sending/receiving letters and more sending/receiving parcels. These postal market trends are similar to the UK, with a consistent decline in letter volumes (e.g. 221 sent letters per capita (2013) to 137 sent letters per capita (2018)) and a rise in parcel volumes (e.g. 11 parcels sent per capita (2014) to 20 parcels sent per capita (2018)).²⁰⁶ This decrease in letter volumes has also been prevalent in the Netherlands before the 2014 change: for example, in 2012, decreased letter volumes meant that PostNL, the designated USO provider, had to initially apply for compensation to cover the cost of the USO.^{207, 208} As a result of this change in user needs, and its possible impact on the financial sustainability of the USO, the Dutch Government commissioned a review which concluded that, among other options, a reduction in the delivery frequency from six to five days brought about the “biggest savings”.²⁰⁹ Whilst achieving cost-savings, it was also important to ensure that users’ needs would be met by this change. 85% of respondents highlighted that they would be willing to accept a reduction in delivery frequency, indicating that this change could both lead to cost-savings, and still meet user needs to a high degree. This change, overseen by the Dutch Authority for Consumers & Markets,²¹⁰ saw Mondays removed from the USO as a smaller percentage of mail (just 2%) was delivered on this day.²¹¹

Germany: A change to the delivery or collection frequency of the USO is a change which is actively being considered by some EU countries presently. As per tables A1.1/A1.2, Germany is one of the few remaining countries whose national requirements exceed the EU minimum and provide for six days of delivery and collection per week.²¹² The ongoing German ministry review, which is looking at reducing delivery and collection frequency from six days to five days, comes following research undertaken in March 2018, investigating German postal users’ needs.²¹³ The 2018 report highlighted

²⁰⁵ Netherlands Authority for Consumers and Markets, 2015. Dutch Postal company PostNL delivered letters on time in 2014. <https://www.acm.nl/en/publications/publication/14556/Dutch-postal-company-PostNL-delivered-letters-on-time-in-2014>

²⁰⁶ European Commission, (no date). Postal data from 2012. https://webgate.ec.europa.eu/grow/redisstat/databrowser/explore/all/GROW_TOP?lang=en&subtheme=GROW_CURRENT&display=card&sort=category

²⁰⁷ Post&Parcel, 2012. PostNL seeks 125m compensation to run universal postal services.

<https://postandparcel.info/48821/news/postnl-seeks-e125m-compensation-to-run-universal-postal-services/>

²⁰⁸ This compensation claim was eventually withdrawn following “extra tariff headroom [that] was created that led to the price increases...”. PostNL, 2013. Annual Report, p.11. https://www.postnl.nl/Images/20140224-postnl-annual-report-2013_tcm10-15599.pdf

²⁰⁹ Post&Parcel, 2011. Dutch Postal Reforms to Eliminate Monday Deliveries.

<https://postandparcel.info/44462/news/dutch-postal-reforms-to-eliminate-monday-deliveries/>

²¹⁰ Netherlands Authority for Consumers and Markets, 2015. Dutch Postal company PostNL delivered letters on time in 2014.

²¹¹ Post&Parcel, 2011. Dutch Postal Reforms to Eliminate Monday Deliveries.

²¹² Bundesnetzagentur, 1999. Postal Universal service Ordinance 1999. <https://www.gesetze-im-internet.de/pudlv/BJNR241800999.html>. For an English translation, see: <https://germanlawarchive.iuscomp.org/?p=720>

²¹³ Please see the following for the relevant research document. However, this version of the research is in German only. Bundesnetzagentur, 2018. Evaluationsstudie zum Post-Universaldienst – Ergebnisbericht.

https://www.bundesnetzagentur.de/SharedDocs/Downloads/DE/Sachgebiete/Post/Verbraucher/Universaldienst/Universaldienst_ergebnis.pdf?__blob=publicationFile&v=5.

the changing trends in the German postal market, with declining letter volumes and rising parcel volumes. The report concluded that, while respondents still valued speed of delivery, a reduction in the number of delivery days from six to five would be an acceptable change. Respondents were unwilling, however, to stretch this further to a reduction to three days per week. Following this, Germany's Ministry for Economic Affairs & Energy (BMWi) released a 2019 summary presenting an option to reduce delivery frequency to five days. This, the summary notes, may form part of a wider "reorientation" of the Postal Act regulations.²¹⁴ While this planned change has not yet been implemented, it was reaffirmed in the August 2019 summary that *Bundesnetzagentur* (BNetzA) (Germany's postal regulator), intended to continue this process and review reducing delivery frequency.²¹⁵

The introduction of a single class service

A1.14 The vast majority of European countries continue to offer two main services within their USO, with one of the two services offering a faster speed of delivery. However, merging two postal classes (with different delivery speeds) into a single class of one delivery speed has been looked at by a number of countries. Below, we discuss a case where this change was implemented.

Norway: in January 2018, Norway adjusted the scope of its USO by merging its A-priority mail (D+1) and B-Economy mail (D+4) letters into a single class of mail (D+2). Norway had experienced a consistent fall in the volume of letters (e.g. -9% 2014-2015;²¹⁶ -10%, 2017-2018)²¹⁷ and an increase in the volume of parcels (e.g. +8% 2014-2015;²¹⁸ +12%, 2017-2018).²¹⁹ These trends, brought about by changing user behaviour, led to a government-commissioned report on the "Effects of changing the USO in Norway".²²⁰ The research highlighted that the net-cost of sustaining the USO had increased significantly (by 400m NOK since 2014); the research highlighted that this trend is also set to continue, which "may result in large socioeconomic loss over time".²²¹ The research, instead of focusing on sustainability, looked at what changes would meet an "assessment of the right to a reasonable profit...".²²² The report concluded that Norway's postal users were not heavily reliant on a five day service. The report noted the most radical option, of reducing delivery service to one day, would achieve large cost savings (estimated between 440-930m NOK) but fail to meet postal user needs, highlighting the importance of the balance between postal user needs and financial

²¹⁴ Bundesnetzagentur, 2019. Key points for a revision of the Postal Act.

https://www.bmwi.de/Redaktion/DE/Downloads/J-L/key-points-for-revision-of-postal-act.pdf?__blob=publicationFile&v=4

²¹⁵ Bundesnetzagentur, 2019. Key points for a revision of the Postal Act.

²¹⁶ Post&Parcel, 2015. Online shopping delivers solid parcels growth for Norway post.

<https://postandparcel.info/67478/news/online-shopping-delivers-solid-parcels-growth-for-norway-post/>

²¹⁷ Posten Norge, 2017. Quarterly Report – 4th Quarter 2017, p.7. https://www.postennorge.no/en/report-archive/_/attachment/inline/a7bffb5-7b82-485c-9015-c397ae0f4e06:300cd7ce408a76a72f939d4cf757c7f0fd21c5d4/Q417%20presentasjon%20eng_16.02.18_eng%20final.pdf

²¹⁸ Post&Parcel, 2015. Online shopping delivers solid parcels growth for Norway post.

²¹⁹ Posten Norge, 2017. Quarterly Report – 4th Quarter 2017, p.12.

²²⁰ Copenhagen Economics, 2017. Effects of changing the USO in Norway, pp.1-136.

https://www.copenhageneconomics.com/dyn/resources/Publication/publicationPDF/0/420/1515667878/effects-of-changing-the-uso-in-norway_final-report_sladdet-versjon.pdf

²²¹ Copenhagen Economics, 2017. Effects of changing the USO in Norway, p.6.

²²² Copenhagen Economics, 2017. Effects of changing the USO in Norway, p.9.

sustainability. Following this, the report stated that “merging A-mail and B-mail into one stream with delivery within two days will allow Posten to realise cost savings”,²²³ noting that much of the c.20% of mail that is sent next-day will either be sent via Posten’s express service or posted under the new, slower service (with users, therefore, accepting that it will take longer to arrive).²²⁴ The change did not result in a change to the quality of service target, which remains at 85% (the former target for both services).²²⁵ *Posten Norge*, Norway’s designated USO provider, continues to offer a priority mail service outside of the USO to accommodate those users that require a faster service.²²⁶

Geographical Differentiation

A1.15 A change to the frequency of delivery and collection by geographical region has been implemented by several countries. This change typically involves setting a different delivery or collection frequency for rural and urban areas. This form of change allows a degree of variation, with some countries preferring a higher frequency of rural collections and deliveries and some preferring a higher frequency of urban collections and deliveries. This is often influenced by the country’s geography, population density and the level of competition in each geographical area. Two recent case studies are detailed below.

Italy: in October 2015, Italy moved from a nationally uniform five day delivery service to the phased introduction of an alternating delivery model, with different delivery frequency depending on geographical area. This model differentiates the collection or delivery frequency residents receive by geographical area (i.e. by large metropolitan areas, urban areas and rural areas).²²⁷ In practice, this means that those residents in rural areas (about 25% of Italy’s population) receive deliveries and collections on Mondays, Wednesdays and Fridays on one week, and Tuesdays and Thursdays on the next week.²²⁸ In remaining areas, residents continue to receive a five day delivery frequency. This change was introduced following research by *Poste Italiane*, Italy’s designated USO provider. The research found that few citizens were regularly relying upon the postal service (e.g. an average of 1.7 letters were received per person per week)²²⁹. Overall, this contributed to what *Poste Italiane* identified a “triple challenge” of problems, with below average “parcel exposure” (12% market share), “onerous” network and delivery requirements and declining letter volumes (-11% from 2011-2014).²³⁰ This research indicated that postal users’ needs had changed. Research undertaken following this indicated that 75% of respondents thought that an alternating delivery model would

²²³ Copenhagen Economics, 2017. Effects of changing the USO in Norway, Appendix A.

²²⁴ Copenhagen Economics, 2017. Effects of changing the USO in Norway. p.28.

²²⁵ London Economics, 2003. Study of the Consequences of Further Liberalisation of the Postal Market in Norway, p.8. <https://londoneconomics.co.uk/wp-content/uploads/2011/09/95-Study-of-the-Consequences-of-Further-Liberalisation-of-the-Postal-Market-in-Norway.pdf>

²²⁶ Posten, (no date). Express overnight. <https://www.posten.no/en/sending/packages/express-overnight>

²²⁷ Poste Italiane, 2018. Capital Markets Day Deliver 2022 presentation, February 2018.

<https://www.posteitaliane.it/files/1476478339877/CMD-2018-Presentation-27-Feb-2018-DEF.pdf>

²²⁸ Poste Italiane, (no date). Modalità di recapito a giorni alterni. Fase III. <https://www.poste.it/recapito-giorni-alterni.html>

²²⁹ Poste Italiane, WIK 16th Königswinter Postal Seminar, 2016. Universal Postal Service Reform in Italy, 2-4 November 2016. https://www.wik.org/fileadmin/Konferenzbeitraege/2016/16th_Koenigswinter_Seminar/S1_4_Scarfiglieri.pdf

²³⁰ Poste Italiane, WIK 16th Königswinter Postal Seminar, 2016. Universal Postal Service Reform in Italy.

be “very” acceptable or acceptable “enough”, a key factor leading to the change.²³¹ Supporting this, *Poste Italiane* stated that the change would achieve cost savings of between 30-50% compared to its previous delivery model.²³² The scheme’s third and final phase was successfully approved in April 2017 by the *Autorità per le Garanzie nelle Comunicazioni* (AGCOM), who provided *ex ante* approval before each of the change’s three phases.²³³

Finland: in July 2017, Finland adjusted the specification of its USO by reducing the frequency of the delivery of parcels and letters by geographical region.²³⁴ Unlike Italy, the delivery frequency in urban areas was reduced to three days per week, while the delivery frequency in rural areas was kept at five days per week.²³⁵ The change was introduced as a result of changing user behaviour in Finland, resulting in a decline in letter volumes (e.g. 265 letters sent per capita (2012) to 134 USO provider sent letters per capita (2014)²³⁶) and an increase in parcel volumes (e.g. 11 parcel sent per capita (2014) to 15 parcels sent per capita (2018)).²³⁷ As a result, the Finnish Government stated that the volume of USO consignments being sent no longer justified five days per week delivery; and that a change was needed to “secure the possibility of dividend” for the USO’s designated provider, Posti. One reason why the delivery frequency was reduced in urban areas was because there were other active postal service providers in urban areas,²³⁸ suggesting that the needs of urban postal users were being met by other operators in the market. This is consistent with the Postal Services Directive’s purpose, which is to provide a guaranteed minimum service.²³⁹ Posti decided voluntarily to avoid implementing the relaxed restrictions, instead continuing to provide a six day service. Posti has stated that this change will be “necessary from the point of view of the future”, suggesting that the voluntary service is likely to change in future.²⁴⁰

²³¹ Poste Italiane, WIK 16th Königswinter Postal Seminar, 2016. Universal Postal Service Reform in Italy.

²³¹ <https://www.poste.it/recapito-giorni-alterni.html>

²³² Poste Italiane, WIK 16th Königswinter Postal Seminar, 2016. Universal Postal Service Reform in Italy.

²³³ Poste Italiane, (no date). Modalità di recapito a giorni alterni. Fase III. <https://www.poste.it/recapito-giorni-alterni.html>

²³⁴ Finnish Government, 2017. Postal Act reform opens doors to new postal services. https://valtioneuvosto.fi/en/article/-/asset_publisher/postilain-uudistus-avaa-ovia-uusille-postipalveluille

²³⁵ Posti, 2017. Posti’s delivery day reform will proceed during the summer – the number of delivery days will not change. https://www.posti.fi/private-news/english/current/2017/20170531_postis-delivery-day-reform-will-proceed-during-the-summer.html

²³⁶ In this case, this number refers specifically to letter volume figures for Posti, the designated USO provider. The volume of combined USO/non-USO letters in Finland have increased very slightly (e.g. 265 letters per capita (2012) to 287 letters per capita (2016)).

²³⁷ European Commission, (no date). Postal data from 2012.

https://webgate.ec.europa.eu/grow/redisstat/databrowser/explore/all/GROW_TOP?lang=en&subtheme=GROW_CURREN T&display=card&sort=category

²³⁸ Eduskunta Riksdagen, 2017. Report KoUB 9/2017 rd – RP 2727.2016 rd.

https://www.eduskunta.fi/SV/vaski/Mietinto/Sidor/KoUB_9+2017.aspx

²³⁹ The Postal Services Directive (97/67/EC), amended by Directives 2002/39/EC and 2008/6/EC.

²⁴⁰ Posti, 2017. Posti’s delivery day reform will proceed during the summer – the number of delivery days will not change.

A2. Legal Framework

A2.1 This annex outlines:

- the legal framework applicable to our review, including our statutory duties;
- the scope of the universal postal service (based on the minimum requirements set by Parliament and the Secretary of State); and
- Ofcom’s role and powers to change the universal postal service.

Ofcom’s statutory duties

Duty to secure the provision of a universal postal service

A2.2 The Postal Services Act 2011 (the ‘Act’) sets the legal framework for the regulation of postal services. This framework is set out in Part 3 of the Act (which came into force on 1 October 2011).²⁴¹

A2.3 Section 29(1) of the Act provides that Ofcom must carry out its functions in relation to postal services in a way that it considers will secure the provision of a universal postal service. Section 29(2) of the Act provides that Ofcom’s power to impose regulatory conditions is subject to the duty imposed by section 29(1) of the Act.

A2.4 In performing its duty to secure the provision of a universal postal service, Ofcom must have regard to the need for the provision of a universal postal service to be:

- financially sustainable; and
- efficient before the end of a reasonable period and for its provision to continue to be efficient at all subsequent times.²⁴²

A2.5 The Act does not give a definition of ‘financially sustainable’. However, section 29(4) states that it includes the need for a reasonable commercial rate of return for any universal service provider on any expenditure incurred by it for the purpose of, or in connection with, the provision by it of a universal postal service.

General duties

A2.6 Section 3(1) of the Communications Act 2003 (the “2003 Act”) provides that it shall be Ofcom’s principal duty, in carrying out its functions, to further the interests of citizens in relation to communications matters and to further the interests of consumers in relevant markets, where appropriate by promoting competition.

A2.7 This principal duty applies also to functions carried out by Ofcom in relation to postal services. Section 3(6A) of the 2003 Act provides that the duty to secure the provision of a

²⁴¹ The provisions of the Act gave effect to Directive 2008/6/EC of the European Parliament and of the Council of 20 February 2008, which amended Directive 97/67/EC, with regard to the full accomplishment of the internal market of Community postal services (“the Postal Services Directive”).

²⁴² Section 29(3) of the Act.

universal postal service (in section 29(1) of the Act) takes priority over Ofcom’s general duties in the 2003 Act (in case of conflict between the two where Ofcom is carrying out functions in relation to postal services).

- A2.8 In performing its general duties, Ofcom must have regard to a range of other considerations which appear to be relevant, including, amongst other things:
- i) the desirability of promoting competition in relevant markets;
 - ii) the desirability of encouraging investment and innovation in relevant markets;
 - iii) the vulnerability of children and of others whose circumstances appear to Ofcom to put them in need of special protection;
 - iv) the needs of persons with disabilities, of the elderly and of those on low incomes;
 - v) the opinions of consumers in relevant markets and of the public generally; and
 - vi) the different interests of persons in the different parts of the United Kingdom, of the different ethnic communities within the United Kingdom and of persons living in rural and in urban areas;
 - vii) the extent to which, in the circumstances of the case, the furthering or securing of the matters mentioned in section 3(1) is reasonably practicable.
- A2.9 Section 3(5) of the 2003 Act provides that in performing its duty to further the interests of consumers,²⁴³ Ofcom must have regard in particular to the interests of those consumers in respect of choice, price, quality of service and value for money.
- A2.10 In performing its general duties, Ofcom must have regard, in all cases, to the principles under which regulatory activities should, amongst other things, be transparent, accountable, proportionate, consistent and targeted only at cases in which actions is needed, and any other principles appearing to us to represent the best regulatory practice.²⁴⁴

The universal postal service

The minimum requirements

- A2.11 Section 31 of the Act sets out the services that must, as a minimum, be included in a universal postal service.²⁴⁵ The ‘minimum requirements’ comprise, in summary:

²⁴³ Under section 405 of the 2003 Act as amended, references to consumers in a market for a service include, where the service is a postal service, addressees.

²⁴⁴ Section 3(3)(a) and (b) of the 2003 Act.

²⁴⁵ The Postal Services Directive obliged all EU Member States to ensure that a universal postal service encompassing a minimum range of specified services were provided. These minimum requirements are reflected in section 31 of the Act. In some aspects, the minimum requirements set in the Act went further than the requirements of the Postal Services Directive. For example, while the Postal Services Directive required the collection and delivery of postal items not less than five working days per week, the minimum requirements of the Act require the delivery and collection of letters six days per week in the United Kingdom, from Monday to Saturday; and while the Postal Services Directive requires tariffs to be “affordable”, the UK legislation requires them to be “uniform” as well as affordable.

- i) At least one delivery of letters²⁴⁶ every Monday to Saturday, and at least one delivery of other postal packets every Monday to Friday;
- ii) At least one collection of letters every Monday to Saturday, and at least one collection of other postal packets every Monday to Friday;
- iii) A service of conveying postal packets from one place to another by post at affordable, geographically uniform prices throughout the UK;
- iv) A registered items service at affordable, geographically uniform prices throughout the UK;
- v) An insured items service at affordable, geographically uniform prices throughout the UK;
- vi) The provision of certain free services to blind/partially sighted people; and
- vii) The free conveyance of certain legislative petitions and addresses.²⁴⁷

A2.12 Section 33 of the Act sets out exceptions to the minimum requirements. It specifies that the minimum requirements set in section 31 do not apply to letter (or other postal packets) whose weight exceed 20kg or whose dimensions fall outside the minimum and maximum dimensions laid down by the Universal Postal Union (UPU).²⁴⁸

A2.13 Section 33 further sets out that the minimum requirements in respect of delivery or collection of letters or other postal packets do not need to be met in such geographical conditions or other circumstances as Ofcom consider to be exceptional and that, nothing in the minimum requirements, is to be read as requiring a service to continue without interruption, suspension or restriction in an emergency.²⁴⁹

Review of the minimum requirements

A2.14 Under section 34 of the Act, Ofcom has the power to review (from time to time) the extent to which the minimum requirements reflect the reasonable needs of users of postal services in the UK.²⁵⁰ As part of such a review, Ofcom may, in particular, consider whether the minimum requirements imposed by the Act could be altered so as better to reflect those needs.

A2.15 Ofcom must send a copy of any review conducted under section 34 to the Secretary of State.²⁵¹ Following such a review by Ofcom, the Secretary of State may decide to amend the minimum requirements set out in section 31 of the Act.²⁵² Any amendment must be made by order that is subject to affirmative resolution procedure (instrument subject to

²⁴⁶ The term 'letter' is defined in section 65(1) of the Act.

²⁴⁷ Section 32 of the Act defines some of the terms used in section 31 to describe the minimum requirements (e.g. 'Legislative petitions and addresses').

²⁴⁸ As set out in the Convention and the Agreement concerning Postal Parcels adopted by the UPU.

²⁴⁹ Section 33(2)(b) and (3)(a) of the Act.

²⁵⁰ Section 34(1) of the Act.

²⁵¹ Section 34(3) of the Act.

²⁵² Section 34(5) of the Act.

that procedure cannot become law unless approved by both Houses of Parliament).²⁵³ As set out in section 34(6) of the Act, the power of the Secretary of State to amend the minimum requirements by order does not include the power to make ‘different provision in relation to different places in the UK’.

The universal postal service order

- A2.16 The Act further requires Ofcom to make an order (the ‘universal postal service order’) to set out:
- a description of the services that Ofcom considers should be provided in the UK as a universal postal service; and
 - the standards with which those services are to comply.²⁵⁴
- A2.17 The services and standards set out by Ofcom are subject to the minimum requirements. Section 30(2) of the Act requires Ofcom to ensure that the universal postal service order contains, as a minimum, each of the services set out in section 31 of the Act (the minimum requirements).
- A2.18 Section 30(3) of the Act further specifies that before making or modifying a universal postal service order, Ofcom must carry out an assessment of the extent to which the market for the provision of postal services in the UK is meeting the reasonable needs of the users of those services.
- A2.19 The first universal postal service order made under the provisions of the Act was made by Ofcom on 26 March 2012.²⁵⁵ In its Statement of 27 March 2012,²⁵⁶ Ofcom further designated Royal Mail as the universal service provider with effect from 1 April 2012. As the designated universal service provider, Royal Mail is required to comply with certain regulatory conditions to provide the universal postal service (the “DUSP conditions”).²⁵⁷ The universal postal service, as described in the order, and subject to the minimum requirements set in the Act, is reflected in DUSP Condition 1.

²⁵³ Section 34(7)(a) of the Act.

²⁵⁴ Section 30(1) of the Act.

²⁵⁵ The Postal Services (Universal Postal Service) Order 2012 (SI 2012/936). A copy of that order was annexed to Ofcom’s Statement of 27 March 2012. Ofcom, 2012. Securing the Universal Postal Service – Decision on the new regulatory framework. <http://stakeholders.ofcom.org.uk/consultations/review-of-regulatory-conditions/statement/>. The first universal postal service order is at Annex 6, <http://stakeholders.ofcom.org.uk/binaries/consultations/review-of-regulatory-conditions/statement/annex6.pdf> and http://www.legislation.gov.uk/uksi/2012/936/pdfs/uksi_20120936_en.pdf

²⁵⁶ Our 2012 Statement on Securing the Universal Postal Service contained our decision on the new regulatory framework and imposed certain regulatory conditions on Royal Mail with effect from 1 April 2012, including the DUSP conditions. Ofcom, 2012. Annex 7, Statutory Notification: designated USP conditions.

https://www.ofcom.org.uk/data/assets/pdf_file/0019/71812/annex7.pdf

²⁵⁷ Ofcom website, 2019, conditions imposed on postal operators. <https://www.ofcom.org.uk/postal-services/information-for-the-postal-industry/conditions>

A3. Market research methodology

2019 research methodology

- A3.1 In 2019, we commissioned Jigsaw Research to conduct qualitative and quantitative research amongst residential and small and medium-sized enterprise (SMEs) users of postal services across the UK.
- A3.2 The objective was to provide user evidence to feed into an overall assessment of reasonable postal needs.
- A3.3 In August and September 2019, we conducted qualitative research employing the following methodologies:
- a) 8 x three-and-a-half-hour workshop sessions conducted across the four nations. Each workshop consisted of between 17 and 21 participants and was made up of both residential users and SME users.
 - b) 2 x two-hour focus groups in with rural residents in Northern Ireland (held in Armagh). One group consisted of residential users (10 participants) and one group consisted of SMEs (9 participants).
 - c) 16 x one-hour in home depth interviews with residential users who felt reliant on postal services, some of whom also lacked mobility (self-reported). Further detail on the methodologies can be found in the research reports published alongside this document.
- A3.4 During the qualitative research sessions, participants were asked to describe their current usage of and attitudes towards postal services. Participants were also asked to review the services guaranteed within the Universal Service Obligation (USO) and to identify the services and standards which would adequately meet their needs. Throughout the research, participants were encouraged to think about their *needs*, rather than the services and standards they *wanted*.
- A3.5 A quantitative survey was also conducted. The fieldwork took place between October and December 2019 and comprised of the following;
- a) 4,596 x 30-minute interviews with UK adults (aged 16+ years); 2,355 of these were conducted face-to-face and 2,241 were conducted online, carried out from 15 October to 29 November 2019. The sample was representative of the UK adult population.
 - b) 971 x 30-minute interviews with UK SME representatives. All participants had responsibility for their organisation's post. Interviews were carried out from 15 October to 10 December 2019. The majority of each interview was completed over the telephone via a computer assisted telephone interview (CATI), with a trade-off exercise section completed online. The sample was representative of UK SMEs.

Conjoint analysis

- A3.6 A conjoint analysis was used to understand what drives participants' preferences and how different aspects of the service contribute to meeting their needs. In the conjoint exercise, participants were asked to choose between different descriptions of the postal service with different combinations of product features – and then asked whether their selected scenario met their needs for a postal service.
- A3.7 The exercise was used to help us understand the relative importance of the elements that make up the USO and what levels of service would meet postal users' stated needs.
- A3.8 The attributes of the USO tested by the conjoint exercise were:
- a) Number of days per week letters will be delivered;
 - b) Number of days per week parcels will be delivered;
 - c) A single class vs. dual-class service;
 - d) Quality of service; and
 - e) Price of postage.

2020 follow up survey

- A3.9 Covid-19 and the measures used to tackle it have impacted society and consequently the use of and, perhaps, expectations from the postal service.
- A3.10 We conducted a new survey to help us to understand how the impact of Covid-19 may have affected views and use of the postal service. Fieldwork ran from 24 July – 6 August 2020, which was after some, but not all, of the first lockdown restrictions had been lifted.

Methodology

- A3.11 We conducted an online survey with a nationally representative sample of 2,366 UK adults (16+). Participants in Scotland, Wales and Northern Ireland were over-represented during fieldwork, to produce robust sample sizes for analysis. The data was subsequently weighted to correct for this, with weights being applied by age, gender and socio-economic group to provide national representativeness.
- A3.12 The survey took approximately 15 minutes to complete. Further details on the methodologies can be found in the research report.

A4. Estimating impacts on user benefits

Approach to estimating impacts on user benefits

- A4.1 Our assessment of user benefits from the existing USO and possible alternative specifications relies primarily on market research carried out by Jigsaw Research, including a conjoint exercise – the approach to which is detailed in Annex 3 above and in the Jigsaw reports published alongside this document.
- A4.2 We have also supplemented this by using the outputs from Jigsaw’s analysis to estimate the monetary value of the impact on user benefits of potential changes to the USO.
- A4.3 This annex sets out how we have used Jigsaw’s conjoint analysis to model the scenarios we consider in this document, and the methodology we have used to estimate the monetary value of the impact on user benefits.

Conjoint analysis

- A4.4 Our quantitative market research included a conjoint exercise, a standard technique used widely in market research to evaluate consumer preferences for different configurations of a product or service. It is routinely used for designing and pricing a wide range of products and services, to estimate the market share, revenue and profitability of new designs, and how changes to aspects of the product or service could affect these.
- A4.5 Conjoint analysis has advantages over direct questions about which individual aspects of a service are important or valued, which participants often find difficult to answer. This mainly occurs because such direct questions ask them to think about their preferences in a way that is unfamiliar to them, and partly because other factors, such as their desire to appear logical or socially responsible, constrain their responses.
- A4.6 In simple terms, a conjoint exercise asks participants to consider alternative designs of a product (and often the price that would be charged for that design), and state which of the alternatives they prefer. This means that participants evaluate the different designs of products as a whole and have to select one (and by implication, reject the other(s)), which is more reflective of the way people make choices in the real world. It does not ask participants to artificially focus on individual elements of the product - that may not be particularly relevant to their overall valuation of the service - in isolation from the overall package being offered. By asking enough participants about the choices that they would make between various alternatives, and applying statistical analysis to this data, we can estimate consumers’ implied valuations²⁵⁸ for different elements of the product, and how

²⁵⁸ To illustrate this implicit valuation, suppose that we ask a consumer to choose between a blue car priced at £10,000 and an otherwise identical red car priced at £10,100. If the consumer prefers the red car, we can infer that the consumer values red over blue at more than £100. It is generally accepted that approaching the question of value of car colour indirectly in this way is more reliable than simply asking the consumer “would you pay £100 extra for a red car?”, which asks participants to think about their preferences in an unfamiliar way and may be constrained by a desire to appear logical.

these would change if the product specification was changed. This method gives a more reliable picture of what features of a product are really important to participants.

- A4.7 An additional benefit of using a conjoint approach is that we can use the method to estimate user preferences across a wide range of alternative specifications of the postal service, without having to show every participant every single possible scenario.

Our approach to this conjoint exercise

- A4.8 We have used a conjoint exercise to evaluate users' needs from the postal service in two ways. Firstly, Jigsaw have used this exercise to estimate the proportion of participants that would consider their needs met by different specifications of the postal service. They do this by estimating the minimum level of service that would be acceptable to (meet the needs of) a given participant, and assessing whether alternative specifications of the postal service would exceed this minimum level.
- A4.9 We have supplemented Jigsaw' estimates by using the outputs of this analysis to consider participants' relative preferences for price increases or reductions in the scope of the postal service. This allows us to infer an indicative monetary valuation of the reduced service. For example, we can assess whether, on average, consumers would prefer a 10% price increase or a reduction in letter delivery frequency to five days a week. We have used these preferences to place a monetary value on the reduction in user benefits that could arise due to reductions in the scope of the postal service.
- A4.10 We set out the technical detail of the approach to this analysis below.

Conjoint methodology

- A4.11 In this conjoint exercise, participants were asked to make a series of choices between two alternative specifications of the postal service. Each described a postal service with different levels of provision against four features of the service: letter delivery frequency, parcel delivery frequency, speed and certainty of delivery, and the price of the service. Each participant only saw a sub-set of the range of possible alternative specifications.²⁵⁹ An example of the choices presented to consumers is shown in Table A4.1 below.

²⁵⁹ This makes the process of the survey itself manageable (each interview takes less time) and runs less risk of confusing those being surveyed by putting before them very large numbers of alternative specifications.

Table A4.1: Example choice from conjoint exercise

	Option A	Option B
Days letters will be delivered	6 days a week	3 days a week – including Saturday
Days parcels will be delivered	6 days a week	3 days a week – including Saturday
Level of service	First Class (that arrives the next day 93% of the time) Second Class (that arrives within 3 days 98.5% of the time)	Single Class that arrives within 2 days 95% of the time
Example price of service	First Class standard letter 70p Second Class standard letter 61p First Class small parcel £3.55 Second Class small parcel £3.00	Single Class letter 65p Single Class small parcel £3.30

Source: Ofcom.

- A4.12 Conjoint analysis estimates individual utility scores for each participant, using a technique called Hierarchical Bayes. A utility score is a number representing the attractiveness of each feature – for example the attractiveness of letter deliveries six days a week versus five days a week. The choices of all participants in the study are used to estimate the average utilities for all the different levels of provision considered across the four features of the service. Each participant’s individual data is also used to determine how they differ from the sample averages. This produces individual utility scores for each level of service within each of the four features of the service,²⁶⁰ for each participant.²⁶¹
- A4.13 Utility scores for each of the four features can be combined to give an overall utility for a given specification of the postal service. If one specification has a higher overall utility score than another, then this indicates that specification is preferred by the participant in question.²⁶² We have used these utility scores to carry out further analysis to estimate the monetary value of changes in user benefits, detailed below.
- A4.14 The conjoint exercise also asked participants whether their selected preferred options would meet their needs from the postal service. From this, an estimate was produced of the minimum or threshold utility that a scenario would need to provide in order to meet each individual participant’s needs. A given scenario “meets participant’s needs” if the utility the participant would derive from a scenario exceeds this minimum threshold.²⁶³ We

²⁶⁰ For example, individual scores for each of the seven levels of the letter delivery frequency feature – six, five, four or three days a week; the latter three each with or without Saturday delivery.

²⁶¹ 2019 quantitative research, p.45.

²⁶² 2019 quantitative research, p.46.

²⁶³ 2019 quantitative research, p.55.

present these results as the proportion of participants (weighted to be nationally representative) that we estimate would have their needs met by a given scenario.

Conjoint features

- A4.15 Conjoint analysis necessarily involves a simplification of the features used to describe a service. As set out in Jigsaw's report, we described the service using four features:
- frequency of letter deliveries, including whether or not letters were delivered on Saturday;
 - frequency of parcel deliveries, including whether or not parcels were delivered on Saturday;
 - level of service for both letters and parcels, including whether the service has First and Second Class or a Single Class service, the time taken for those services to be delivered and the reliability of those services; and
 - price, presented using example prices for letters and small parcels.
- A4.16 We then need to represent the potential changes to the USO that we have considered in terms of these four features. For some potential changes, these directly map to a single set of features. For example, we can represent a five days a week letter delivery service using a single combination of features:
- Letter delivery frequency of 5 days a week, Monday-Friday;
 - parcel delivery frequency of 6 days a week;
 - current First and Second Class speeds of delivery, at current quality of service; and
 - current (2019) prices.
- A4.17 For other potential changes, a single set of features would not perfectly describe the way we expect the change would be implemented in practice. In these cases, we consider conjoint estimates from a range of scenarios that, taken together, provide the best reflection of how a change would work in practice.
- A4.18 For example, for a potential change to three day a week letter delivery, we assume that half of addresses would receive letters on Monday, Wednesday and Friday and the other half on Tuesday, Thursday and Saturday. However, our conjoint exercise assumed for simplicity that either no or all addresses would receive items on Saturday. As a result, we consider conjoint scenarios with and without Saturday letter delivery to provide a range of impacts. The impact of the specific change we are considering, with half of addresses receiving Saturday deliveries, is likely to lie within this range. Table A4.2 below summarises how we have mapped features from the conjoint analysis to the potential changes considered in this document.

Table A4.2: Conjoint representations of potential USO changes

Potential USO change	Letter delivery frequency	Parcel delivery frequency	Level of service	Price
Current service	6 days a week	6 days a week	First and Second Class, current quality of service	Current (2019) prices
Five days a week letter delivery, Monday-Friday	5 days a week, Monday-Friday	6 days a week	First and Second Class, current quality of service	Current (2019) prices
Three days a week letter delivery	3 days a week, Monday-Friday	6 days a week	First and Second Class, current quality of service	Current (2019) prices
	3 days a week, including Saturday	6 days a week	First and Second Class, current quality of service	Current (2019) prices
	3 days a week, Monday-Friday	6 days a week	Single Class D+3 (95% arrives on time)	Approximate mid-point of Current (2019) First and Second Class prices
	3 days a week, including Saturday	6 days a week	Single Class D+3 (95% arrives on time)	Approximate mid-point of Current (2019) First and Second Class prices

Potential USO change	Letter delivery frequency	Parcel delivery frequency	Level of service	Price
Five days a week parcel delivery, Monday-Friday	6 days a week	5 days a week, Monday-Friday	First and Second Class, current quality of service	Current (2019) prices
Five days a week parcel delivery, including Saturday	6 days a week	5 days a week, including Saturday	First and Second Class, current quality of service	Current (2019) prices
Single Class D+2	6 days a week	6 days a week	Single Class D+2 (95% arrives on time)	Approximate mid-point of Current (2019) First and Second Class prices
Single Class D+3	6 days a week	6 days a week	Single Class D+3 (95% arrives on time)	Approximate mid-point of Current (2019) First and Second Class prices
90% of items arrive on time	6 days a week	6 days a week	First and Second Class, 90% arrives on time	Current (2019) prices
80% of items arrive on time	6 days a week	6 days a week	First and Second Class, 80% arrives on time	Current (2019) prices

Source: Ofcom.

Estimating the monetary value of impacts on user benefits

- A4.19 As discussed above, the conjoint analysis provides estimates of average utility values for a postal service user for a range of scenarios. We can use the average utility scores to consider how the value of the service to users changes in response to changes in price and non-price features, and relative preferences between different features.
- A4.20 The conjoint exercise included five price steps, the prevailing prices when the research was carried out in 2019, and four incremental price steps, each of which represented a 10% increase on the previous price step. For scenarios with a single class service, prices presented were an average of First and Second Class prices. Participants were shown

example prices for a standard letter and small parcel. The specific price steps presented are show in Table A4.3 below.²⁶⁴

Table A4.3: Price steps tested in conjoint exercise

Price step	First and Second Class	Single Class
Current price	First Class standard letter 70p	Single Class letter 65p
	Second Class standard letter 61p	Single Class small parcel £3.30
	First Class small parcel £3.55	
	Second Class small parcel £3.00	
Current price +10%	First Class standard letter 77p	Single Class letter 72p
	Second Class standard letter 67p	Single Class small parcel £3.60
	First Class small parcel £3.91	
	Second Class small parcel £3.30	
Current price +20%*	First Class standard letter 85p	Single Class letter 79p
	Second Class standard letter 74p	Single Class small parcel £3.96
	First Class small parcel £4.30	
	Second Class small parcel £3.63	
Current price +30%*	First Class standard letter 93p	Single Class letter 87p
	Second Class standard letter 81p	Single Class small parcel £4.36
	First Class small parcel £4.73	
	Second Class small parcel £3.99	
Current price +40%*	First Class standard letter £1.02	Single Class letter 95p
	Second Class standard letter 89p	Single Class small parcel £4.79
	First Class small parcel £5.20	
	Second Class small parcel £4.39	

Source: Ofcom.

* Note that for ease we refer to the prices as +20%, + 30%, +40% however this is not strictly true. Prices were calculated by applying 10% increases on the previous price level.

Estimating the relationship between price changes and utility

A4.21 We have used the estimated average utility (as described in paragraph A4.12) for the current service at each price level to identify the impact of price changes on average utility for users, holding non-price features constant. We use these data points to estimate the

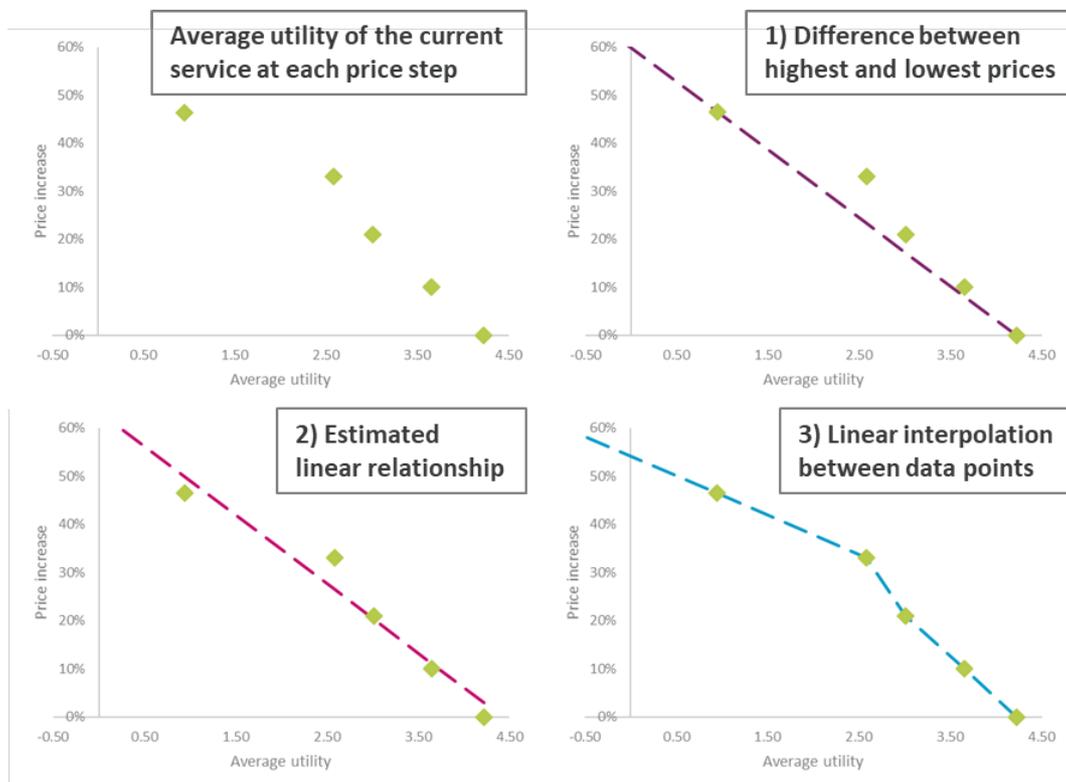
²⁶⁴ 2019 quantitative research, p.49.

relationship between price and average utility. That is, to estimate how much residential and SME users value different aspects of the service, in monetary terms. To reflect uncertainty about the exact nature of the relationship between price and utility, we do this in three ways, and reflect the results of the different approaches in the range we place around our estimates:

- Approach 1: Take the difference in utility between the current and highest price levels that Jigsaw asked consumers about in the survey, and divide this by the price difference between those steps to derive an estimate of the utility impact of a given increase in price.
- Approach 2: Fit a linear relationship between price and average utility, and use this coefficient to estimate the utility impact of a given increase in price.
- Approach 3: Interpolate linearly between data points and identify the price increase on the current service that is equivalent to a given change in the level of average utility.

A4.22 Figure A4.1 below illustrates these three approaches – using results from the residential part of the conjoint exercise. We present price impacts in terms of a range of percentage price increases to all prices across Royal Mail’s USO products (including letters and parcels, and First and Second Class services). This is most straightforward for presentational purposes because consumers buy a range of post products at different prices. For illustrative purposes, when summarising results below and in the main document we also show this as the equivalent price increase in pence for a First Class stamp for a standard letter, though the overall impact is calculated through assuming a proportionate increase for all products.

Figure A4.1: Approaches to estimating the relationship between price and utility



Source: Ofcom analysis of Jigsaw Market Research.

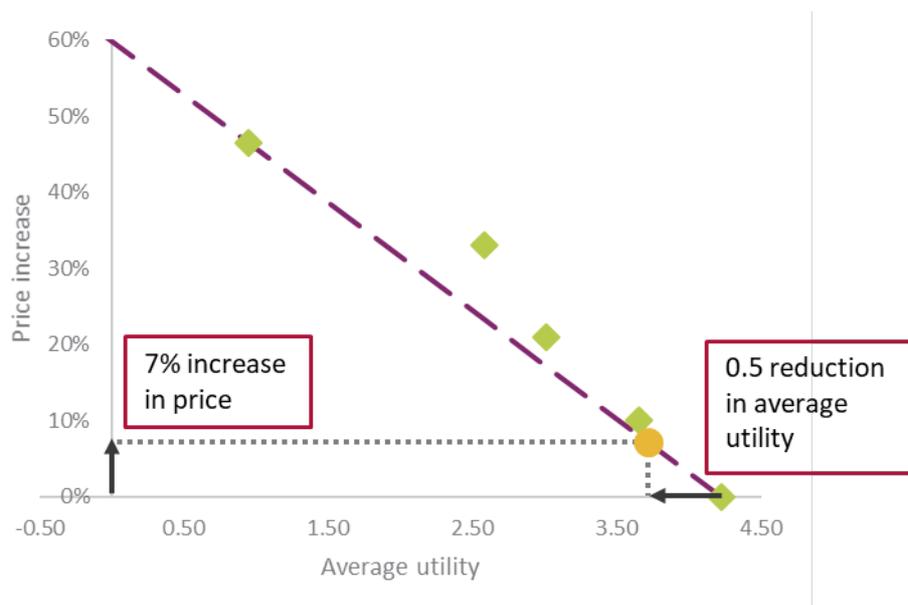
A4.23 This data suggests assuming a broadly linear relationship could be appropriate, particularly for smaller changes in utility. However, inspection suggests that at higher price increases of around 40%—equivalent to a standard letters price of around £1—users may become more price sensitive, such that a further price increase has a larger impact on utility. There is also uncertainty for changes to the service where the utility impact exceeds the impact of the most expensive price step tested, as this requires us to extrapolate the relationship between price and utility beyond the data points we have from the conjoint exercise. This is particularly the case for substantial reductions in service (such as a move to three day a week letter delivery) for SME users. For these reasons, our estimates have a greater range where there is a more substantial impact on utility, and in general we are more cautious about our estimate of the impact of larger changes to the postal service.

Estimating the monetary value of potential USO changes

A4.24 We can use the above estimates to approximate users' willingness to pay to avoid a reduction in service. We do this by identifying the reduction in average utility caused by the change in non-price elements of the service and estimating the price increase that would have the same impact on average utility. In other words, we identify the point at which users would be indifferent between a given change in service and a price increase to maintain the current level of service.

A4.25 Figure A4.2 below illustrates this for a reduction to five day a week (Monday-Friday) letter delivery frequency (in this example using 'Approach 1' to estimating the relationship between price and utility). The output of the conjoint research indicates that a reduction in letter delivery frequency to 5 days a week leads to a reduction of 0.5 in average utility for residential users. Figure A4.2 shows that, based on 'Approach 1' to estimation, a reduction of 0.5 in average utility is equivalent to around a 7% price increase.

Figure A4.2: Approach to estimating the monetary value of lost benefits from reduced delivery frequency to 5 days a week (Monday-Friday)



Source: Ofcom analysis of Jigsaw Market Research.

A4.26 We apply this methodology to the separate conjoint exercises carried out for residential and SME participants. Table A4.4 sets out these estimates across the main scenarios considered in this document. We also apply this approach to subgroups within those samples, to identify if there are impacts on some user groups that are materially different to the average impact on the population as a whole.

Table A4.4: Estimated monetary value of impacts on users for main scenarios

Scenario	Equivalent price increase – Residential users		Equivalent price increase – SME users	
	(%)	(First Class stamp)	(%)	(First Class stamp)
Five day a week letter delivery (Mon-Fri)	6-10%	4-7p	2-4%	1-3p
Three day a week letter delivery	30-45%	21-32p	50-70%+	35-50p+
Single Class D+2	2-5%	1-4p	14-18%	10-13p
Single Class D+3	9-13%	6-9p	25-35%	17-25p
90% of items arrive on time	2-5%	1-4p	5-7%	3-5p
80% of items arrive on time	9-14%	6-10p	20-35%	14-25p

Source: Ofcom analysis of Jigsaw Market Research.

A4.27 We also recognise that there is uncertainty in ascribing a precise monetary value to the results of the conjoint exercise, so we treat these estimates as indicative of the general

magnitude of impacts rather than placing significant weight on their precise values. We take a conservative approach to this approximation, presenting a range of impacts to reflect uncertainty and avoid spurious accuracy. We focus more on the relative magnitude of different scenarios, for example whether a change is broadly equivalent to a small price increase (say 10%) or to a substantially larger price increase (30-40% or more).

Calculating overall annual impact

A4.28 To derive an overall annual impact on user benefits, we assume that the percentage price increase is applied across all prices paid by USO users. We scale up these proportionate impacts using estimates of the amount of USO revenue spent by residential and SME users respectively. From its published regulatory financial statements, Royal Mail's USO revenue was around £2.8bn in 2018/19.²⁶⁵ We take assumptions about the broad split of USO between residential and business users from our revenue modelling. We apply the estimate of the average impact on residential users to our assumption of the range of Royal Mail's annual USO revenues attributable to residential users, and the average impact on SME users to the rest. This gives us a range for the total impact on users on an annual basis. As business users tend to send more mail, impacts on SMEs carry more weight in this calculation.

²⁶⁵ Royal Mail, June 2019. Royal Mail regulatory financial statements 2018-19.

A5. Cost methodology

Summary

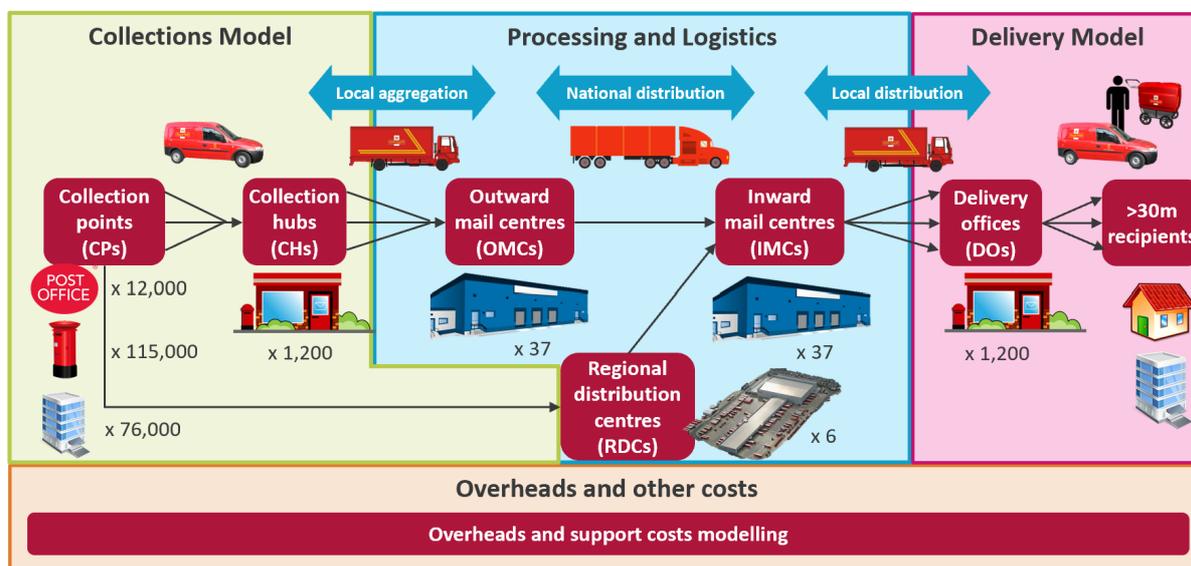
- A5.1 One aspect of our overall work programme on post²⁶⁶ has been to build a suite of three bottom-up cost models which seek to replicate Royal Mail's operational approach to each part of the postal pipeline. The models cover Collections, Processing & Logistics, and Delivery respectively. In addition to these we have built a fourth model which includes overheads and other costs not included in the three bottom-up models. Collectively, the models have helped us gain a better understanding of the cost elements of Royal Mail's operations and in turn have been useful in providing us with insights as to how costs may change in line with any potential changes to the future scope of the postal USO. We describe these models and present key outputs from them in this annex.
- A5.2 In October 2019, we held a workshop with stakeholders to update them on our approach to modelling Royal Mail's operations. The workshop covered the aims, structure, approach and data used in each of the Collections, Processing & Logistics, and Delivery models, and allowed stakeholders a first opportunity to ask questions or make points regarding the modelling approach. Since then, we have continued to develop the models and have engaged with Royal Mail on points of detail to ensure that our models accurately reflect Royal Mail's operations.
- A5.3 We have built these models using volume and operational data from Royal Mail. Together they aim to model the entirety of the postal pipeline:
- a) Collections: the Collections model calculates the costs involved in collecting mail from collection points (CPs) and aggregating it at collection hubs (CHs);
 - b) Local aggregation: the Processing & Logistics model calculates the costs involved in transporting mail from collection hubs to outward mail centres (OMCs) and regional distribution centres (RDCs);
 - c) National transport: the Processing & Logistics model calculates the costs involved in transporting mail from OMCs and RDCs to the inward mail centres (IMCs);
 - d) Processing: the Processing & Logistics model calculates the costs of processing mail at the OMCs, RDCs and IMCs for onward transit;
 - e) Delivery: the Delivery model calculates the costs involved in preparing mail at delivery offices (DOs) and delivering it to delivery points (DPs);
 - f) Overheads and support costs: the Overheads and other costs model calculates overheads and other costs, such as charges paid to the Post Office for handling mail, that are not captured elsewhere in the models.

²⁶⁶ Ofcom, April 2020. Ofcom Plan of Work 2020/21.

https://www.ofcom.org.uk/_data/assets/pdf_file/0029/194753/statement-ofcom-plan-of-work-2020-21.pdf

A5.4 The postal pipeline and the coverage of each model is illustrated in Figure A5.1 below.

Figure A5.1: Postal pipeline and structure of the models



Source: Ofcom.

A5.5 As discussed later in paragraph A6.29, we have decided not to publish our cost models. While we aim to publish modelling wherever possible, our cost models very closely mirror Royal Mail's operational structure. In order to publish the models, we would need not only to redact any confidential data, but also remove structure from the model where that structure itself reveals commercially-sensitive information regarding Royal Mail's operations. We consider that models redacted in this way would serve little purpose to other stakeholders, and so we have decided against publication in this case.

A5.6 In order to provide stakeholders with the opportunity to scrutinise and understand our approach, in this annex we describe the functioning of each of the bottom-up cost models and highlight key assumptions and elements based on our testing of the models.

Key assumptions across the models

We model in a bottom-up way

A5.7 A bottom-up model calculates the resources required for running the network from a series of network operation algorithms and then assigns costs to these resources. This allows us to test the effect of different scenarios such as different levels of volumes or different operational assumptions on the resources and costs needed for the network. Bottom-up models may not capture all relevant cost drivers or constraints on changes to resources, such as contracts that cannot be amended, and as such may understate costs or overstate the responsiveness of costs to changes in operations. For this reason, calibration is important to ensure that the modelled network aligns with reality – we discuss the calibration we have done at the end of this annex.

We have modelled Royal Mail's current network

- A5.8 Our models are based on Royal Mail's current network and operations and do not attempt to model any significant change to this network. In particular, we do not account for any change to the parcel delivery network. Royal Mail's plans are evolving, and we do not have sufficient granular visibility as to how these might be implemented in practice. It is therefore not possible for us to make the detailed assumptions required for bottom-up modelling.
- A5.9 There are many ways to design a postal network, each of which may be better suited for different volumes and product mixes. We have not set out to model a network which is set up optimally for current and future products and volumes. Instead, we aim to build a representation of Royal Mail's current operations and test how these costs may change under certain scenarios. To the extent that Royal Mail's operations may not be efficient, we do not attempt to account for any potential additional efficiency in these models.
- A5.10 Consistent with this approach, each of our models assumes that certain aspects of Royal Mail's current operation, such as the locations of its buildings, are fixed. This is referred to as a 'scorched node' approach, as opposed to a 'scorched earth' approach where all aspects of the model could be flexed to better optimise operations.

We do not model quality of service performance

- A5.11 Under current performance targets, Royal Mail is required to ensure that a certain percentage of its mail is delivered within the specified timeframe.²⁶⁷ In our model, we do not make any specific allowances for mail failing to meet the specified timeframes – all mail is assumed to need to be delivered 'on time'. This is a modelling simplification which, all else being equal, would tend to cause our model to overstate the costs. For reasons outlined later in this annex, we do not expect this over-specification to lead to significant overestimation of costs.

Consistency of volume impacts

- A5.12 In each of the cost models, we use outputs from the revenue modelling (described in Annex 6) to account for the anticipated changes in volumes under each scenario due to users changing which products they use to accommodate their needs, for example due to changes in product specifications.
- A5.13 Each of our models uses a different volume base specific to the part of the pipeline they model, as volumes are different at each stage in the process. For example, access mail is not collected by Royal Mail and does not enter the OMC, but arrives from access operators at the IMC and is passed on for delivery. As such, access mail does not appear in the Collections model but does in each of the Processing & Logistics and Delivery models. The revenue model allows us to calculate proportional volume changes for each volume base

²⁶⁷ At least 93% of First Class mail must be delivered the day after it was posted (excluding Sundays). At least 98.5% of Second Class mail must be delivered within three working days of it being posted (again excluding Sundays).

used in our cost modelling to ensure that we are treating volumes consistently across our cost models.

Potential reduction in delivery days

- A5.14 We have considered scenarios in which the number of days letters are delivered to any given delivery point are reduced from six days per week currently to five days, or to three days. We assume that this reduction, and any necessary changes in product specification such as a loss of next-day letter services, has an impact on volumes and revenues of letters. We assume that in these scenarios volumes and revenues of parcels would not be affected, because it would likely make commercial sense for Royal Mail to continue to deliver all parcels as frequently as it does now (i.e. 6 days a week).
- A5.15 It is possible that some further net cost savings could be achieved if Royal Mail reduced the delivery frequency of certain parcels, in particular some Second Class parcels (e.g. untracked and RM48). These parcels could be delivered by the joint network and alongside letters. However, reducing the frequency of parcels delivery is likely to have a significant impact on revenues too. We therefore expect that the bulk of the net cost savings would be achieved by reducing the frequency of letters as we have calculated.

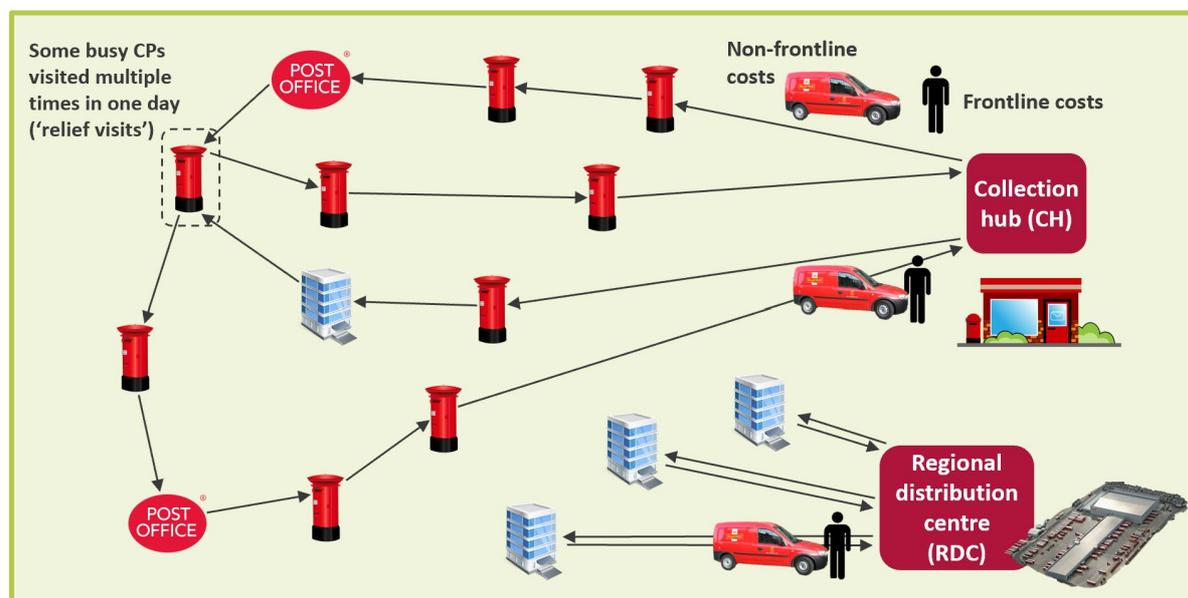
Transition costs

- A5.16 Changes to the scope of the USO could result in the need for changes in the network and operations. We refer to the costs of such changes as transition costs. Transition costs include costs of workforce reorganisation and hours reduction, equipment and IT, route and network re-design, and management time etc. The transition costs could be incurred in one financial year or over a number of years, depending on the extent of the operational changes needed.
- A5.17 As explained later in this annex, a key output of our cost models is the changes in hours needed. We consider the costs of reducing hours to be by far the most significant element of transition costs. These reductions in hours could be achieved through a variety of means including voluntary redundancy, reducing overtime, reducing recruitment, and natural attrition. Each of these methods bears a different cost, and therefore any estimates of the cost of this reduction are likely to cover wide ranges.
- A5.18 In considering the possible scale of these transition costs, we have taken into account Royal Mail's historical voluntary redundancy costs, its latest business plan, the scale of changes of output hours in our cost models and potential routes to achieving these changes in the 5 day delivery scenario. Overall, we do not consider that the potential transition costs would be disproportionate to the scale of potential ongoing cost savings we think are achievable in this scenario.

Model descriptions and base case outputs

Collections model

Figure A5.2: Overview of the Collections model



Source: Ofcom.

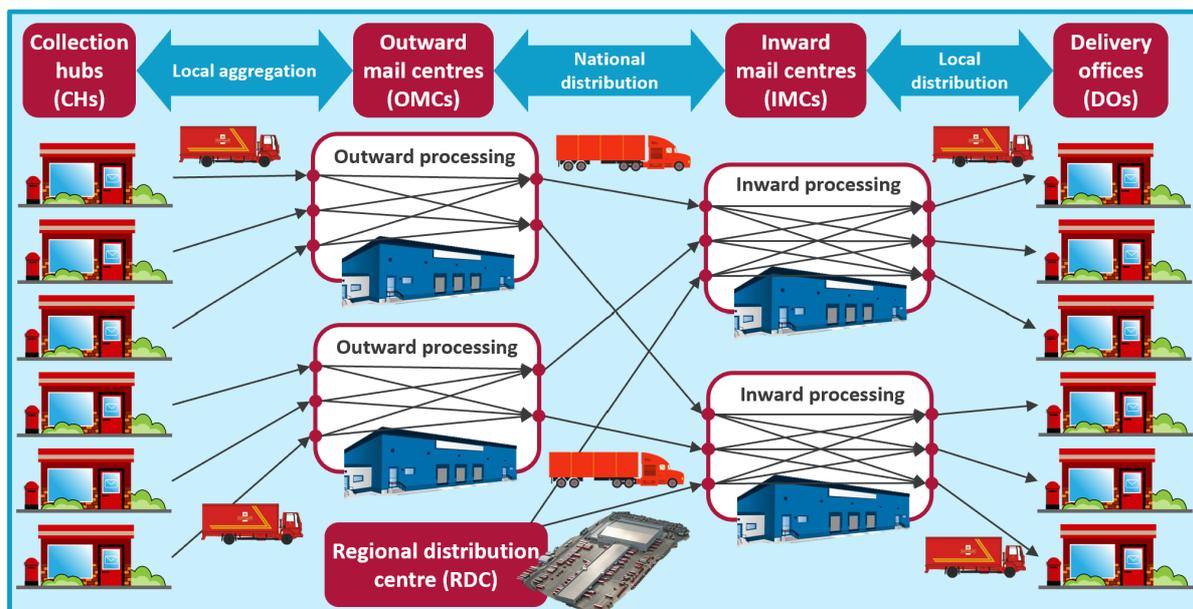
Description of the Collections model

- A5.19 The aim of the Collections model is to estimate the annual operating costs associated with Royal Mail collecting and conveying mail from CPs (postboxes, post offices, or businesses) to collection hubs. A collection hub is usually within a mail centre or delivery office, with some standalone satellite collection hubs.
- A5.20 To do this, the model dimensions the collections operations needed for a representative week (25 March – 31 March 2019) to collect a given volume of mail. We use this week as it should be representative of ordinary operations and not be distorted by any seasonal variation of volumes (e.g. due to Christmas). Because the Collections model calculates the costs for a representative week which is then scaled up to an entire year, it assumes annual costs rise linearly with volume.
- A5.21 The data we use to populate the Collections model is based on data extracted from Royal Mail's collections management database (CMD). It also uses volumes data from Royal Mail measured at the OMC. The Collections model is able to shift any percentage of any day's volumes of letters and/or parcels to any other days. The model has been completed in Excel, with an external Python script to model distances between CPs, which then forms an input into the Excel model.
- A5.22 We assume that on a collection day every CP is visited at least once. The volume of mail modelled at a CP determines whether additional visits are required to avoid the physical capacity of the CP being exceeded.

- A5.23 The number of routes required for each collection hub is determined by the number of visits each CP requires, the length and distribution of routes, the shift length, and the van capacity.
- A5.24 **Frontline Costs:** Frontline collections hours are determined by the number of routes a collection hub needs to send out to collect all the mail from its CPs, and the time required for each of these routes. Which collection hub a particular CP's mail goes to is determined from Royal Mail's current mapping in the CMD.
- A5.25 **Non-Frontline Costs:** Non-frontline costs in the Collections model are the vehicle costs for the number of routes determined to be required to collect all the mail from all CPs. This is calculated based on the total miles driven to serve all routes, with a cost-per-mile assumption from Royal Mail.

Processing & Logistics model

Figure A5.3: Overview of the Processing & Logistics model



Source: Ofcom.

Description of the Processing & Logistics model

- A5.26 The Processing & Logistics model was developed for us by consultants Analysys Mason, with the final version produced in March 2020. Its aim is to estimate the annual operating costs associated with Royal Mail transporting collected mail from CHs to DOs so that it can be delivered. This involves:
- transporting mail from CHs to OMCs and RDCs;
 - processing the mail to identify where in the country it will need to be delivered and which IMC is closest to the eventual DP;
 - transporting the mail to the appropriate IMC;

- d) processing the mail to identify the appropriate DO for final delivery; and
- e) transporting the mail from IMCs to DOs.

- A5.27 To do this, it dimensions a processing and logistics network, specified in terms of components such as staff and vehicles, that is sufficient to process and transport a given volume of mail through each of the above steps, accounting for the features of different kinds of mail such as speed of delivery and physical size ('volumetrics'). It calculates the resources needed for a representative week (25 March – 31 March 2019), which are then scaled up to an annual figure. It therefore assumes, like the Collections model, that annual costs are linear in volume.
- A5.28 All of the above steps need to take place within narrowly defined timing windows to ensure that Royal Mail is able to meet the quality standards for its different classes of mail. For example, all of the above steps must be able to be completed such that a First Class letter collected on a Monday afternoon in one part of the country reaches the appropriate DO by Tuesday morning so that it can be delivered that day.

Logistics costs

- A5.29 Our model calculates the various stages of transportation based on the volumes to be transported and the nodes between which they need to be transported. It calculates local transport (between CHs and OMCs, and between IMCs and DOs) separately from national transport (between OMCs/RDCs and IMCs). While the logistics modelling calculates the cost of transporting the mail, it assumes that mail will arrive at MCs and DOs as scheduled – that is, the time that mail arrives at buildings does not change based on the modelling, it is instead a constraint that the transportation network is dimensioned to achieve.

Local transport

- A5.30 We have based our modelling of local transport on data from Royal Mail's road service lists which identify driver shifts for medium and large goods vehicles, including the start times of, and locations visited on, each of these shifts. This provides a detailed breakdown of the trips and times required to deliver Royal Mail's actual volumes. Where these lists are incomplete (for example due to smaller vehicles not being included in Royal Mail's dataset), we have made assumptions based on the information available to create estimated routes to complete the plans.
- A5.31 The routes calculated remain fixed in the model, regardless of scenario. However, the number and size of vehicles on each route is driven by peak volume demand. Therefore, with larger volumes of mail, more or larger vehicles are used, at greater cost, in local transport. This allows us to flex the costs with volumes without redimensioning the transport plan; while redimensioning the transport plan may result in a more efficient output, the complexity of such a task (and expertise required to create a realistic plan) is outside the scope of this analysis.

National transport

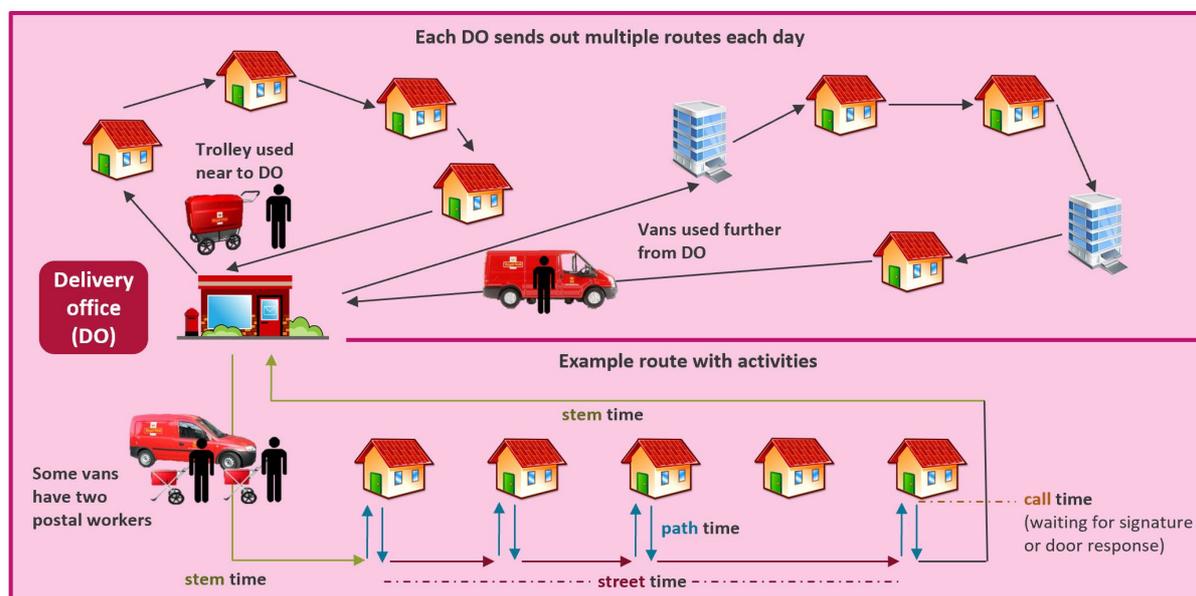
- A5.32 We have based our modelling of local transport on data from Royal Mail's national transport plans which, like its road service lists that we use for local transport, provide a detailed trip-by-trip breakdown of its actual operations. We have processed the data from Royal Mail to produce full routes, allowing us to track how many vehicles would be required to fulfil all trips in a representative week.
- A5.33 Unlike with local transport, we also undertake some further analysis to allow greater flexibility in this part of the network. For example, for scenarios which assume that a D+1 service is not required, we allow routes primarily used to service first-class traffic (air routes and some night-shifts) to be turned off, with these volumes being loaded onto other, less expensive modes of transport.
- A5.34 After flexing the plan for any scenario-specific requirements, routes are populated with vehicles of different sizes similarly to local transport. Routes carrying larger volumes of mail require more or larger vehicles at greater cost. These vehicles are also assumed to require a long-term space at a distribution centre, as well as short-term space (calculated hour-by-hour) between their arrival at and departure from a distribution centre. These space requirements form part of accommodation costs.

Processing costs

- A5.35 Our model calculates the costs of processing mail at each mail centre (and RDC) separately. Each mail centre operates as an OMC at some hours of the day and IMC at others. Mail is assumed to arrive at MCs based on data from Royal Mail, and must be processed quickly enough to be taken on the next logistics step. These time windows are narrower for First Class mail, with Second Class mail given longer to be processed.
- A5.36 Each mail centre can have a different set of processing machines available to it, which are used where available. Any mail that cannot be processed by the machines available either due to characteristics (e.g. non-Mailmark) or volume (i.e. mail in excess of the available machines' operating capacity) is processed manually. We first calculate the resources required to process First Class mail within the necessary time windows, and then any excess capacity (e.g. partial shifts of workers or running a machine full-time rather than part-time) is used to process any remaining mail. Further resources are then dimensioned if needed to process any mail in excess of this capacity.

Delivery model

Figure A5.4: Overview of the Delivery model



Source: Ofcom.

Description of the Delivery model

- A5.37 The aim of the Delivery model is to estimate the annual operating costs associated with Royal Mail delivering mail to delivery points after it has arrived at delivery offices from mail centres. To do this, it dimensions a delivery operation, specified in terms of components such as staff and vehicles, that is sufficient to deliver a given volume of mail.
- A5.38 The Delivery model, unlike the Collections and Processing & Logistics models, calculates costs on the basis of a representative day, rather than a representative week basis. That is, it calculates the costs for a single day, carrying the average daily volume of mail items, and then scales this up to an entire year. This simplifying approach assumes that changes in costs tend to move linearly with changes in volume, so that the higher costs on days where there are larger volumes of mail to deliver are offset by lower costs on days where there are smaller volumes of mail to deliver.
- A5.39 The Delivery model separates the delivery process into two stages:
- Indoor delivery:** these are activities performed inside the DOs prior to mail leaving the DO on a delivery route. This includes unloading mail from lorries on arrival, sorting/sequencing any unsorted mail for each route, aggregating mail into bundles for each route and gathering them into a trolley or van. It also includes staffing the secure Special Delivery locker and the customer service counter; and

- b) **Outdoor delivery:** these are the activities performed outside the DOs to deliver mail to DPs. This includes the time spent travelling to the first DP (stem time), the time spent walking or driving along streets between DPs (street time), the time spent walking up paths from the street to the DPs themselves (path time), time spent waiting for customers to open doors and sign for mail (call time), and the time spent travelling back to the DO from the last DP (also stem time).

A5.40 These stages comprise frontline costs, which are the paid hours for operational staff. In addition, our model calculates non-frontline costs which are all other costs and include management hours, vehicle costs, and accommodation costs.

Frontline costs

A5.41 Frontline indoor delivery hours are calculated using Royal Mail's planning values – detailed assumptions calculated by Royal Mail's industrial engineers who break down a high-level activity into its constituent tasks and time required to undertake each of these tasks. Many of these are variable and expressed in terms of minutes the task will take for a certain number of mail items. Others do not vary with the number of mail items and vary in other ways such as per-route or simply per-day at each DO. We use these planning values to calculate the expected time taken for each activity based on the volumes of mail at each DO.

A5.42 Frontline outdoor delivery hours are largely based around the calculation of the numbers of routes required to deliver all mail items, and the time required for each of those routes. These are built up on a postcode-sector (PCS)²⁶⁸ basis in our model, with each PCS mapping to one DO (and each DO serving multiple PCSs). Each PCS is assigned one delivery method²⁶⁹ which is then used in the model to serve all DPs in that PCS.

A5.43 Based on the delivery method chosen, the model then calculates the total time required to deliver all mail items in each PCS using Royal Mail's planning values and geographic data regarding the distances between PCSs and their respective DOs and the total lengths of streets in each PCS. This time is broken up into routes, ensuring that routes do not take longer than the maximum allowable shift duration.

Non-frontline costs

A5.44 Non-frontline costs are separated into accommodation costs, vehicle costs, and other non-frontline costs. Within accommodation costs, we use Royal Mail data for rent and facilities management costs and then calculate energy costs based on the size of each DO. Vehicle costs are calculated based on the total miles driven to serve all routes, with a cost-per-mile

²⁶⁸ A postcode sector comprises all characters of a postcode up to and including the first character in the second part of the code. For example, the postcode sector that contains 'SE1 9HA' would be 'SE1 9'.

²⁶⁹ The methods used in the Delivery model are either van-based delivery using one of three types of van, which are delivered by either one or two postal workers, or on-foot delivery using a trolley. In PCS where delivery is done on-foot, delivery is supplemented by van routes which deliver larger parcels which are not appropriate to be delivered using a trolley.

assumption from Royal Mail. Aggregate other non-frontline costs (also provided by Royal Mail) are allocated to each DO in proportion with all other calculated costs.

Overheads & other costs model

Description of the Overheads & other costs model

A5.45 The aim of the Overheads and other costs model is to estimate any overheads and other costs not modelled in the Collections, Processing & Logistics, or Delivery models. In general, these are costs which are not clearly driven by underlying cost drivers which we can identify and build into our other models. In some cases, these costs may in theory be able to be modelled on a bottom-up basis, but we lack the data required to do so in a robust way.

Overheads

A5.46 We use Royal Mail's Cost Allocation Model (CAM) to identify costs that have not been calculated in our other models. The CAM breaks down all costs by activity and pipeline incurred by Royal Mail, providing a single and complete overview of the costs of its network and operations.

A5.47 We split costs in this model into two broad categories on a case-by-case basis. Where we believe costs are likely to change significantly with volume, they are classified as Variable. Where this is not the case, they are classified as Fixed. Examples of Variable costs are commission to the Post Office and attributable VAT; examples of Fixed costs are central group costs and data services.

A5.48 Overheads in the CAM are separated into pipeline-specific overheads that only apply to one of the modelled pipelines (e.g. to Delivery, or to Collections), and general overheads. General overheads are categorised in the CAM as Business Sustaining costs, Support costs, Commercial costs, and Wholesale costs.

A5.49 Any costs that are allocated to a specific pipeline in the CAM and which we have identified as not being modelled in any of our other three cost models are included in the Overheads & Other Costs model and allocated to the relevant other cost model. We allocate Collections costs to the Collections model. Outward, RDC, Network, Inward and Local Distribution costs are allocated to the Processing & Logistics model. Delivery Indoor and Delivery Outdoor costs are allocated to the Delivery model.

A5.50 The CAM is used to determine how much each product type contributes to each variable cost. Processing & Logistics base case volumes are used to calculate a per-unit cost of each variable cost for each product type. For example, suppose a variable CAM activity costs £4m where £3m of that is attributed to First Class (1c) letters, and £1m is attributed to Second Class (2c) letters. If there are one billion 1c letters and one billion 2c letters in the base case, then there is a £0.003 and £0.001 per-unit cost on 1c letters and 2c letters respectively. This additional variable overhead cost sits within the overheads model.

Other Costs

A5.51 The Other Costs in this model include 'International and Other Operations', which are fixed in the model, and 'Collection Mail Prep' and 'Post Office Ltd Counter Handling', which are treated as variable. The variable costs are calculated in the same way as variable overheads as described above.

Scenarios modelled

A5.52 Earlier in this document we have described several key scenarios relating to possible changes to Royal Mail's operations. We have modelled these scenarios in our cost models to estimate how Royal Mail's costs may change in each, and describe the assumptions we have made and main effects we have identified through our modelling.

A5.53 These estimates presume that Royal Mail is not contractually or in other ways constrained in how it can adjust its operations to account for changes in the specification of the USO. It therefore represents an estimate of the potential cost savings that could be possible, without making a judgment on whether the full extent of these changes can be achieved in a reasonable timeframe.

A5.54 Royal Mail's 2018/19 financial year included 53 weeks. Typically, Royal Mail's financial years include only 52 weeks. We have therefore reduced the calculated cost impacts pro rata (i.e. -1.9%) to make them comparable with typical annual results.

A5.55 Table A5.5 below summarises the differences in key assumptions for each of the scenarios we have modelled. We present the overall cost impact from each scenario in each of our cost models at the end of this section in Table A5.6.

Table A5.1: Summary of key assumptions under each scenario

Scenario	Days per week of letters delivery	First Class letters?	Second Class letters?	Quality of service standards
Base case costs	6	Yes, at D+1	Yes, at D+3	Same as now
5 days letters	5	Yes, at D+1	Yes, at D+3	Same as now
3 days, D+3 letters	3	No	Yes, at D+3	Same as now
D+2 letters	6	Merged into a single D+2 class		Same as now
D+3 letters	6	No	Yes, at D+3	Same as now
D+2 letters, 5 days	5	Merged into a single D+2 class		Same as now
D+3 letters, 5 days	3	No	Yes, at D+3	Same as now
QoS to 80% (1st class)	6	Yes, at D+1	Yes, at D+3	First Class letters reduced to 80%

Source: Ofcom.

5 days letters

- A5.56 In the '5 days letters' scenario we assume that Royal Mail stops delivering letters on Saturdays. We assume that parcels are still delivered on Saturdays using dedicated van routes. There are no changes to the Collections and Processing & Logistics operations as a result – letters are still collected and processed as normal, and are assumed to be held at the DO if they arrive on a Saturday and are then delivered on Monday.
- A5.57 This may in practice lead to a larger delivery requirement on Mondays compared with other days. We have instead modelled this as a smaller uplift to volumes in each remaining delivery day, rather than a spike on a single day. We would expect that over time, user behaviour would adjust to account for the expected delivery days, particularly for business users. However, we would not expect this to completely negate the effect of mail building up over the weekend, creating a larger workload on Mondays than is currently the case. We note that this is a simplifying assumption which we believe is a proportional approach to take without overcomplicating the models.
- A5.58 The bulk of cost savings in this scenario come from the Delivery model. Costs saved in the Collections and Processing & Logistics models are solely a result of expected volume changes from this scenario, as users switch products to better suit their needs. For example, some users of First Class letters may want to ensure delivery specifically on Saturday, and without Saturday deliveries these users may switch to Second Class products or cease sending this mail at all. The Overheads & Other Costs model cost savings are predominantly related to changes in costs from the mark-up to Delivery costs, i.e. they move in proportion to reductions in Delivery costs, as this is the large majority of the change in costs in the three pipeline cost models.

3 days, D+3 letters

- A5.59 In the '3 days, D+3 letters' scenario, we assume that Royal Mail moves to an alternating delivery structure, where letter delivery to each delivery point is on either a Monday-Wednesday-Friday or a Tuesday-Thursday-Saturday schedule. As a result, a First Class service cannot be provided and so all letters are assumed to be subject to a D+3 delivery speed. Letters are assumed to be held at the DO if they arrive on a non-delivery day for their delivery point. Parcels are still delivered 6 days per week, using dedicated van routes on days where the area does not have a letter delivery service.
- A5.60 There are significant potential savings in delivery as a result, resulting from the reduction in letter delivery routes and from the improvement in efficiency of routes on delivery days. As mail can build up over two days before delivery, more mail can be delivered per-route as it is more likely that multiple items will be delivered to a single delivery point. In addition, more delivery points will have at least one item delivered on a given street which reduces the time spent walking past homes or businesses per delivery. There are also some cost savings in Delivery from volume changes.

- A5.61 There are further potential savings from processing and logistics, as the loss of a First Class service allows for more efficient operations. This largely arises from being able to spread mail processing over wider time windows and get more use out of processing machines as they do not need to prioritise First Class mail in short time windows to allow it to be delivered on time. There are also some potential savings from the reduction in need of fast logistics routes (such as using the air network) as these only need to service First Class parcels. However, these savings are quite small and would only be fully realised with the loss of all First Class mail including parcels – the cost of operating fast logistics routes is largely fixed, with limited variable costs from running fewer or smaller vehicles on these routes. There are also some cost savings in Processing & Logistics from volume changes.
- A5.62 Costs saved in the Collections model are solely a result of expected volume changes from this scenario, as users switch products to better suit their needs, notably from First Class to Second Class. We also assume that a material proportion of mail that moves from First Class to Second Class may actually be captured by access providers rather than by Royal Mail which in turn would lead to a more noticeable change in collections activity than under the '5 day letters' scenario, given that access operators undertake their own collections activity. The Overheads & Other Costs model cost savings are predominantly related to proportional changes in costs from the mark-up to Processing & Logistics and Delivery costs.

D+2 letters

- A5.63 In the 'D+2 letters' scenario we assume that Royal Mail stops providing separate D+1 First Class and D+3 Second Class letter products and replaces them with equivalent products with a D+2 delivery speed. We model six delivery days per week for all mail and make no change to the classes of parcel products provided.
- A5.64 As with the '3 days, D+3 letters' scenario above, there are potential savings from Processing & Logistics resulting from the change in class of service and consequent improvement in processing efficiency and reduction in fast logistics routes. We have greater uncertainty over the exact extent of these savings, however, as they have been based on a hypothetical set of processing time windows and route requirements as Royal Mail does not currently operate on a D+2 processing schedule.
- A5.65 Costs saved in the Delivery and Collections models are solely a result of expected volume changes from this scenario, as users switch products to better suit their needs. As we assume a significant movement from the loss of First Class letters to be towards access operators, there is a more noticeable change in collections activity than under the '5 day letters' scenario. The Overheads & Other Costs model cost savings are predominantly related to proportional changes in costs from the mark-up to Processing & Logistics and Delivery costs.

D+3 letters

- A5.66 In the 'D+3 letters' scenario we assume that Royal Mail stops providing D+1 First Class letter products. There is no change to the number of days of delivery for letters, nor is there any change to the classes of parcel products provided.
- A5.67 As with the '3 days, D+3 letters' scenario above, there are savings from Processing & Logistics resulting from the change in class and consequent improvement in processing efficiency and reduction in fast logistics routes.
- A5.68 Costs saved in the Delivery and Collections models are solely a result of expected volume changes from this scenario, as users switch products to better suit their needs. As we assume a significant movement from the loss of First Class letters to be towards access operators, there is a more noticeable change in collections activity than under the '5 day letters' scenario. The Overheads & Other Costs model cost savings are predominantly related to proportional changes in costs from the mark-up to Processing & Logistics and Delivery costs.

D+2 letters, 5 days

- A5.69 This scenario combines the effects of the 'D+2 letters' and '5 days letters' scenarios described above.

D+3 letters, 5 days

- A5.70 This scenario combines the effects of the 'D+3 letters' and '5 days letters' scenarios described above.

QoS to 80% (First Class)

- A5.71 In the 'QoS to 80% (First Class)' scenario, we assume that Royal Mail is able to have a greater proportion (20%) of First Class mail miss the D+1 delivery speed standard. This allows greater flexibility across the pipeline, with collections, processing and logistics activities all being able to avoid some situations where it is very costly to handle a small amount of First Class mail, and helps to smooth out some volatility in mail volumes to improve efficiency.
- A5.72 We have not modelled the cost impact of a change in QoS standards, as our models are not equipped to do so. As explained earlier in this section, our models assume 100% QoS and do not have any flexibility for changing QoS standards. Therefore, while we have estimated in our revenue modelling (see Annex 6) the volume changes that could come about as a result of a reduction in the quality of service, we have not estimated directly in our cost model any cost savings that this reduction in volumes this would allow.
- A5.73 We have instead estimated cost savings on the basis of work previously done by Royal Mail which included estimates of cost savings arising from changes in quality of service. In our analysis we have accounted for changes in the underlying cost base since the original work was done.

Summary of results

A5.74 Table A5.6 below shows the outputs from each model first for the base case, and then for each scenario the difference to the base case. Results are presented on a 52-week basis.

Table A5.2: Modelled outputs for each scenario on a 2018/19 52-week basis

Scenario	Total	Of which Collections	Of which Processing & Logistics	Of which Delivery	Of which Overheads & other costs
Base case costs	c. £7.1bn	c. £[x]m	c. £[x]m	c. £[x]m	c. £[x]m
5 days letters	-£[x]m -£175-£225m	-£[x]m c. 0-10%	-£[x]m c. 0-10%	-£[x]m c. 90-100%	-£[x]m c. 0-10%
3 days, D+3 letters	-£[x]m -£750-800m	-£[x]m c. 0-10%	-£[x]m c. 0-10%	-£[x]m c. 80-90%	-£[x]m c. 0-10%
D+2 letters	-£[x]m -£125-175m	-£[x]m c. 0-10%	-£[x]m c. 30-40%	-£[x]m c. 30-40%	-£[x]m c. 30-40%
D+3 letters	-£[x]m -£100-150m	-£[x]m c. 0-10%	-£[x]m c. 40-50%	-£[x]m c. 10-20%	-£[x]m c. 30-40%
D+2 letters, 5 days	-£[x]m -£325-£375m	-£[x]m c. 0-10%	-£[x]m c. 10-20%	-£[x]m c. 70-80%	-£[x]m c. 10-20%
D+3 letters, 5 days	-£[x]m -£300-350m	-£[x]m c. 0-10%	-£[x]m c. 10-20%	-£[x]m c. 60-70%	-£[x]m c. 10-20%
QoS to 80% (1st class)	Not modelled, but estimated at -£[x]m -£75-125m, largely expected to arise in the Processing and Logistics segment of the postal pipeline				

Source: Ofcom Post Cost Models.

Note: All cost savings estimates in the above table are based on our assumption that Royal Mail is able to implement all operational changes available to it to optimize its network for a re-scoped USO. To the extent that Royal Mail faces contractual or other barriers to making these changes, it may not be possible for it to quickly achieve the full extent of these cost savings in practice.

A5.75 As explained above, our cost impact results are based on 2018/19 costs. In reality, if any changes to the scope of the USO were to happen, they would happen in future years and their impact would therefore materialise from that point onwards. Therefore, we also project the cost to the financial year 2022/23 for the five days a week letter delivery service, Monday to Friday. We expect the cost savings to be slightly smaller in the future due to the competing impacts of changes in letter volumes, which tend to reduce the potential cost savings of changes in number of delivery days, and growth in wage rates which increases potential cost savings.

- A5.76 We assume the changes to the scope occur at such a point which results in the full cost savings being materialised in 2022/23. This is somewhat hypothetical. In reality, the changes could happen at such a time that results in the full impact in a later year, both due to the timing of any future decision on delivery frequency (which is for Government and Parliament) as well as the time it takes to implement all the necessary operational changes in practice. However, forecasting assumptions become less reliable as we go further into the future. The 2022/23 financial year appears to strike the right balance between broadly realistic whole year cost savings estimates and forecast reliability.
- A5.77 We use our forecast model to estimate the projected revenue impact in 2022/23. Our model is informed by Royal Mail's latest business plan, submitted to us in the 2020/21 financial year under the regulatory reporting requirements, and reflects our view on how volumes and costs are likely to evolve in the future. It takes account of the significant events since 2018/19, including the impact of Covid-19.
- A5.78 Using our forecast models, we estimate the cost savings in the five days a week letter service scenario to be in the range of £175-225m in 2022/23, should Royal Mail be able to make all necessary operational changes to implement this scenario.

Calibration and checks

- A5.79 The purpose of calibration is to ensure that the model produces a reasonably realistic network. Any bottom-up model has a risk of missing key dimensioning relationships and producing a network which, while internally consistent based on the assumptions made, does not adequately match the reality it is designed to model.
- A5.80 Our models build a theoretical uncalibrated cost base. To ensure that the postal cost models are generating a realistic network, we have then calibrated our base case to Royal Mail's actual costs, hours worked, and routes using data gathered under our formal information-gathering powers. For costs, this is done as a mark-up. For hours and routes, we have changed input assumptions to ensure that our outputs are reasonably closely aligned with Royal Mail's actuals. This ensures that we do not underestimate costs unrealistically, but also means that we build in any inefficiencies from Royal Mail's operations into our modelling.
- A5.81 When running scenarios in our models, we apply the same mark-ups and use the same calibrated assumptions as with our calibrated base case. This gives us a reasonable level of confidence that the hypothetical operations created in our scenarios are realistic representations of how Royal Mail would operate under those circumstances.

A6. Revenue methodology

A6.1 In this annex we set out our approach to modelling the potential impact of changes to the scope of the universal service on Royal Mail's volumes and revenue.

Overall approach

- A6.2 Changes to the scope of the USO could impact the volumes and revenues of Royal Mail's products, whether these changes involve the addition or removal of certain services, or they involve changes to the frequency and/or speed of delivery.
- A6.3 We have built a model to assess the impact on the Reported Business volumes and revenues of each scenario of changes to the scope of the USO. The Reported Business is the business unit within Royal Mail Group which encompasses the network that delivers the universal service. The Reported Business excludes other networks that Royal Mail operates. It does not include Parcelforce Worldwide and GLS networks.
- A6.4 The model uses granular data on volumes, revenues and average unit revenues ('AURs') of Royal Mail's products as inputs (see below for further details).
- A6.5 The calculations follow these main steps:
- a) Estimate the impact of changes in the services provided on volumes, applying assumptions about switching routes and switching factors which define what proportion of volumes of impacted products would switch to other products or be lost;
 - b) Assume new prices for new products (for example the D+2 letter product and a commercial next day letter product);
 - c) Calculate the new revenues using the new volumes and prices; and
 - d) Calculate the volume and revenue impact by comparing the new volume and revenues with the volumes and revenues of the base case.

Volume and revenue data

- A6.6 We use Royal Mail's 2018/19 actual volumes and revenues submitted to us as part of the regulatory reporting requirements. This is to ensure our analysis is comparable with our cost modelling which is also based on 2018/19 data. This consistent approach allows all the scenarios to be compared on a like for like basis. However, as we explain below, we also estimate the projected revenue impact for the five days a week letter service scenario in the 2022/23 financial year. This would give a more realistic estimate of the impact as it would account for the letter volume and price changes caused by other factors after 2018/19 such as letter volume decline.
- A6.7 The granularity of our volume and revenue data is based on the data Royal Mail uses for its business plan and revenue modelling. However, we further disaggregate the product

categories or add new product categories where needed (for example a new D+2 single class product).

- A6.8 We also segment the data between types of postal users where necessary, for example, in relation to parcels we segment between C2X, small/large business and Amazon. We consider each user segment has a different demand response (for example, a business user sending 1000 items a month may be more concerned about a price increase than a residential user who only sends 1 item a month).

Switching routes and factors

- A6.9 The switching routes represent the possible outcomes for the impacted volumes. We assume there are four possible switching routes:
- a) Leave the postal market, for example, due to acceleration in e-substitution;
 - b) Move to other competitors or downstream access operators;
 - c) Upgrade to another Royal Mail product with higher specifications and/or price, for example, customers may upgrade to Special Delivery Next Day if the First Class service is not provided; and
 - d) Downgrade to another Royal Mail product with lower specifications and/or price, for example, customers may downgrade to a Second Class service, if the First Class service is not provided.
- A6.10 The switching factors represent the proportions of volumes which could go down each switching route. The switching factors we have used are based on the information we have gathered from our user needs research and international precedents, our knowledge and experience of Royal Mail's products and its markets, and Royal Mail's submissions.

Pricing

- A6.11 We assume most prices to remain unchanged. If a scenario involves a new service, for example a single class at D+2 speed of delivery or a new commercial next day letter service, we make assumptions about the level it is likely to be priced at (considering the price of other similar or comparable services). We explain below our key assumptions regarding pricing in the relevant scenarios in Table A6.1.
- A6.12 There may be further pricing strategies that Royal Mail could adopt to minimise revenue loss. However, we do not have sufficient information to model all such potential strategies and price changes with confidence.
- A6.13 As explained above, we use granular data for product volumes and AURs. This enables us to have a better and more targeted assessment of the impact on the users and their volumes. This also enables us to assess more precisely the impact of volume changes and new prices on revenues. Using aggregated categories of products would entail using total volumes and average AURs which could lead to inaccuracies in some cases. For example,

the volumes across weight steps of some products, in particular of large letters or parcels, often vary significantly by class.

Key assumptions

A6.14 We first explain our key assumptions about how the two potential key changes in the scope, the reduction in delivery frequency and the exclusion of the current First Class speed, are likely to impact the volumes and revenues. We then summarise our key assumptions by scenario and product type in Table A6.1 below.

Reduction in letter delivery frequency (5 days or 3 days)

A6.15 We assume that in these scenarios only the volumes and revenues of letters would be affected and not parcels, because we expect Royal Mail to have strong commercial incentives to continue to deliver all parcels as frequently as it does now (i.e. 6 days a week). It is possible that some further net cost savings could be achieved if Royal Mail reduced the delivery frequency of certain parcels, in particular some Second Class parcels (e.g. untracked and RM48). These parcels could be delivered by the joint network and alongside letters. However, reducing the frequency of parcels delivery is likely to have a significant impact on revenues too. We therefore expect that the bulk of the net cost savings would be achieved by reducing the frequency of letters as we have calculated, and so have not considered the potential for Royal Mail to reduce the delivery frequency of some parcel types any further.

A6.16 We assume that Royal Mail would also change the frequency of delivery for Royal Mail bulk and access letters to match the USO letters delivery frequency in each scenario. Therefore, the volumes and revenues of Royal Mail's both USO letters and bulk and access letters would be affected in these scenarios.

A6.17 In scenarios where the frequency of delivery of letters is reduced to 3 days, there may be a need to delay the current 1pm delivery deadline for Special Delivery. This would lead to some Special Delivery volumes being lost. As explained above, we assume that Royal Mail would continue to deliver parcels at the current frequency and speeds (both First and Second Class). This is likely to increase the volumes delivered by parcel delivery methods. The delay in delivery deadline may be necessary to enable the parcels network to service the increased workload.

Current first class letter service discontinued

A6.18 We assume where First Class letters are discontinued (whether due to de-scoping First Class or reducing delivery frequency to 3 days, which would not permit continuation of the First Class service), some USO First Class volumes would be lost and the remainder would switch to cheaper products (Second Class or new D+2 service).

A6.19 We assume in these scenarios that Royal Mail would also stop its First Class bulk and access letter services to realise further cost savings. We assume that as a result, some First Class bulk mail volumes would downtrade to Second Class bulk mail. We also assume that a

considerable proportion of the volumes would switch to standard access. This is because we expect the access operators' offering to be competitive compared with Royal Mail's Second Class bulk service and in the absence of Royal Mail's First Class bulk service.

A6.20 We assume that in all these scenarios, Royal Mail would retain a significantly more expensive next day delivery letter service, which would be delivered alongside parcels. Although we expect the take-up would be low due to the high price, this could help Royal Mail mitigate the revenue impact to some extent.

A6.21 In scenarios with a single class D+2 service, we assume that Royal Mail would discontinue the current First Class and Second Class for both USO and retail bulk services, and instead offer single class D+2 USO and bulk mail services. We assume the price for these services would be set at the current Second Class level plus a modest increase. We assume the impact of the modestly higher price would be compensated for by the increase in speed (from D+3 to D+2) and would therefore have no impact on Second Class letter volumes.

A6.22 The table below summarises our key assumptions by scenarios:

Table A6.1: Summary of key assumptions by scenario and product type

Assumptions / Scenario	5 days letters	3 days letters	Single class D+2 letters, 5 or 6 days	Single class D+3 letters, 5 or 6 days
USO First Class	Continue at same price / Some volumes are lost and small volumes upgrade to Special Delivery	Discontinue except for a commercial next day letter service at a high price with small volumes / Some volumes are lost and the rest switch to Second Class	Discontinue except for a commercial next day letter service at a high price with small volumes / Some volumes are lost and the rest switch to D+2 priced modestly higher than current Second Class	Discontinue except for a commercial next day letter service at a high price with small volumes / Some volumes are lost and the rest switch to Second Class (D+3)
USO Second Class	Continue at same price / No impact on volumes	Continue at same price / Some volumes are lost	Discontinue, volumes switch to new D+2 priced modestly higher than current Second Class / Some volumes are lost in 5 days scenario	Continue at same price / Some volumes are lost in 5 days scenario
Bulk letters First Class	Some volumes are lost	Discontinue except for a commercial next day letter service at a high price with small volumes / Some volumes are lost and the rest	Discontinue except for a commercial next day letter service at a high price with small volumes / Some volumes are lost and the rest switch to D+2 (priced modestly higher than current Second Class) or standard access	Discontinue except for a commercial next day letter service at a high price with small volumes / Some volumes are lost and the rest

		switch to Second Class or standard access		switch to Second Class or standard access
Bulk letters Second Class	No impact on volumes	Some volumes are lost, and some volumes switch to standard access	Some volumes are lost and the rest switch to D+2 (priced modestly higher than current Second Class) or standard access	Some volumes are lost, and some volumes switch to standard access
Access	No impact on volumes	Some volumes are lost	Some volumes are lost in 5 days scenario	Some volumes are lost in 5 days scenario
Special Delivery	Uptrading volumes from USO First Class	Some volumes lost due to potential change in 1pm delivery deadline	No impact	No impact
Parcels	No impact	No impact (except for Special Delivery above)	No impact (except for Special Delivery above)	No impact (except for Special Delivery above)

Source: Ofcom.

Calculation of revenue impact

- A6.23 As explained above, our modelling is based on 2018/19 volumes and revenues. In reality, if changes to the USO were to happen, they would happen in future years and have their impact felt from that point onwards. Therefore, we also project the revenue impact to the financial year 2022/23 for the five days a week letter delivery service, Monday to Friday (see below). We expect the revenue impact to decrease in the future mainly due to the decline in letter volumes.
- A6.24 We assume the changes to the scope occur at such a point which results in the full revenue impacts materialising in 2022/23. In reality, the changes could happen at such a time that results in the full impact in a later year. However, forecasting assumptions become less reliable as we go further into the future. The 2022/23 financial year appears to strike the right balance between broadly realistic whole year figures and forecast reliability.
- A6.25 We use our forecast model to estimate the projected revenue impact in 2022/23. Our model is informed by Royal Mail's latest business plan and reflects our view on how volumes and prices are likely to evolve in the future. It takes account of the significant events since 2018/19 including the impact of Covid-19.
- A6.26 Royal Mail's 2018/19 financial year included 53 weeks. Typically, Royal Mail's financial years include 52 weeks. We have therefore reduced the calculated revenue impacts pro rata to make them comparable with typical annual results. The total revenues for 2018/19 was around £7,065 million on a 52-week basis.

A6.27 The following table sets out our key results for each scenario:

Table A6.2: Revenue impact results for each scenario on a 2018/19 52-week basis

Scenario	Revenue impact range
5 days letters	-£0-50m
3 days letters	-£400-450m
D+2 letters, 6 days	-£200-250m
D+3 letters, 6 days	-£325-375m
D+2 letters, 5 days	-£225-275m
D+3 letters, 5 days	-£350-400m
QoS to 80% (1st class)	-£75-125m

Source: Ofcom analysis.

A6.28 Using our forecast models, we also estimate the revenue impact in the five days a week letter service scenario to be revenue reductions in the range of £0-50m in 2022/23.

We are not publishing the models

A6.29 We have used financial models to calculate the revenue and cost impact of hypothetical scenarios for the specification of the USO. In this Annex and Annex 5 to this document, we describe the methodologies and structures of our models. We also explain their key inputs and assumptions and their key outputs, and how the various models inter-link. We consider this information will be necessary for stakeholders to gain a sufficient understanding of how we arrive at our results and conclusions.

A6.30 We do not consider it would be appropriate to publish the models. To publish the models, we would have to replace a significant proportion of the data of most of our models with dummy information, and also remove some calculations and structure entirely. This would be necessary to avoid disclosing commercially sensitive information about Royal Mail's operations and its financial position and performance. We have in the past published models with entirely dummy or randomised data. In this case, given the necessary structural changes to avoid disclosing confidential information regarding Royal Mail's operations, this benefit would be lost, and the published models would not provide significantly more information than the descriptions of the models we have provided.

A7. Glossary

This glossary sets out a non-exhaustive list of defined terms and acronyms used throughout the document. It is intended to help the reader to understand the document and our research in a clearer, more transparent way.

Term	Definition
Access operator(s)	The name given to postal operators (other than Royal Mail) who collect volumes of mail from larger business, distribute it across the UK and insert it into Royal Mail's local network for delivery.
Articles for the blind	A USO service which enables blind and partially sighted people to send certain items First Class through the post free of charge.
B2B	Letters or parcels sent from a business to another business.
B2C	Letters or parcels sent from a business to a consumer.
Business access mail services	Where competing access operators collect bulk volumes of mail from larger businesses (such as banks or insurance companies), public sector organisations and charities, transport it across the UK and insert it into Royal Mail's local network for delivery.
Business retail end-to-end services	Where Royal Mail collects bulk volumes of mail directly from larger businesses (or other organisations) and adds it to its network for sortation, distribution and delivery.
C2X	Letters or parcels sent from a consumer to another entity, which could for example, be a business or another consumer.
Certificate of Posting	A USO service which offers a receipt providing proof of posting. It is free of charge and available from post office counters. It can be used in connection with compensation claims for lost or damaged items.
Collections model	One of our four cost models. The collections model is used to estimate the annual operating costs associated with Royal Mail collecting and conveying mail from collection points (e.g. post boxes, post offices, businesses) to collection hubs (e.g. mail centres, delivery offices)
Conjoint analysis	A market research exercise where participants were asked to make a series of choices between two alternative specifications of the postal service, and state whether their selected preferred option would meet their needs from the postal service. Each specification had a different level of provision against four service features: letter delivery frequency, parcel delivery frequency, speed and certainty of delivery, and the price of the service.
Covid-19 bespoke research	Our online follow-up quantitative survey research, undertaken between July-August 2020, which looked at understanding how the impact of Covid-19 may have affected views on and use of the postal service.

D+1	A postal service which aims to deliver one working day after collection. The number can be substituted to represent any number of days (e.g. “D+3” means delivery three working days after collection).
Delivery frequency	The number of days letters and/or parcels are delivered per week.
Delivery model	One of our four cost models. The delivery model aims to estimate the annual operating costs associated with Royal Mail delivering mail to delivery points, after it has arrived at delivery offices from mail centres.
Designated Universal Service Provider (DUSP) Condition	Ofcom may impose a “DUSP condition” on a universal service provider which may, in summary, require it do one or more of the following: <ul style="list-style-type: none"> • Provide a universal service or part of a universal service in the UK to specified standards; • Provide access points for the universal postal service to a certain specification; • Provide information to postal operators and users about universal services; and • Anything else that Ofcom considers appropriate in relation to any of these obligations.
European Postal Service Directive	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 2008/6/EC of the European Parliament and of the Council of 20 February 2008).
First Class (1st Class)	The USO priority service for letters and parcels, provided by Royal Mail, which has a delivery frequency speed of D+1 and a QoS target of 93%.
Geographical differentiation	A postal service which typically splits up an area into different geographical regions (e.g. rural, urban) and provides differing levels of service to each (e.g. a higher delivery frequency in one area and a lower delivery frequency in another area).
Inward Mail Centre	The part of a Royal Mail mail centre where the activities related to the final sorting of mail for delivery (in that mail centre’s catchment area) received from the upstream part of Royal Mail’s network (or from other postal operators, etc.) take place.
Journey 2024 Strategy	Royal Mail Group’s five-year business plan.
Keepsafe	A USO service through which Royal Mail holds customers’ mail for up to 100 days at their local delivery office and delivers it to them on their return.
Large letter	A Large Letter is any postal item larger than a Letter (see definition below) and up to 353mm in length, 250mm in width and 25mm in thickness, with a maximum weight of 750g.

Large letter/parcel user	Organisations such as banks, insurers, utilities and public sector organisations that primarily use bulk mail letter or bulk parcel services (i.e. non-USO products) to interact with their customers.
Large Parcel	A Large Parcel is any parcel larger than a Medium Parcel (see definition below) up to 1.5m in length and up to 3m length and depth combined, weighting no more than 30kg.
Letter	A Letter is any postal item up to 240mm in length, 165mm in width and 5mm in thickness, weighing no more than 100g.
Mail	Refers to both letters and parcels and packets.
Medium Parcel	A Medium Parcel is any parcel larger than a Small Parcel (see definition below) up to 61cm in length, 46cm in width and 46cm in thickness, weighting no more than 20kg.
Metered mail	A USO service which refers to a method of payment or payment channel for Royal Mail services where customers (typically SMEs) pre-pay for postage and apply an impression to the envelope, label or wrapper using a franking machine licensed by Royal Mail.
Minimum requirements	Set out in S.31 of the Postal Services Act 2011, minimum requirements refer to those requirements which must be included within a USO.
Non-minimum requirements	As under S.31 of the Postal Services Act 2011, non-minimum requirements include those requirements which Ofcom considered should be provided in the UK as part of the USO in addition to the minimum requirements.
Overheads & other costs model	One of our four cost models. This model aims at estimating any overheads and other costs not modelled in the Collections, Processing & logistics or Delivery models.
Parcel	Typically refers to small, medium and/or large parcels.
Petitions to Parliament, Addresses & Petitions to the Queen	A USO service which enables the sending free of charge of petitions and addresses to the Sovereign, and petitions to members of UK Parliaments and Assemblies.
Post	Refers to both letters and parcels and packets.
Post Office	Post Office Limited, whose registered company number in England and Wales is 2154540.
Postal operator	Defined in section 27(3) of the Postal Services Act 2011 as meaning a person who provides the service of conveying postal packets from one place to another by post, or any of the incidental services of receiving, collecting, sorting and delivering postal packets.
Postal packet	Defined under section 27(2) of the Postal Services Act 2011, “postal packet” means a letter, parcel, packet or other article transmissible by post.

Postal service	Defined in section 27(1) of the Postal Services Act 2011 as the service of conveying postal packets from one place to another by post, the incidental services of receiving, collecting, sorting and delivering postal packets, and any other service which relates to, and is provided in conjunction with, any of those services.
Poste Restante	A USO service which allows users to have mail delivered and held at a post office for a time period of 14 days for items posted in the UK and one month for items posted overseas. The address of the post office is used as the customer's postal address. It is required to be free of charge.
Processing & logistics model	One of our four cost models. The processing and logistics model aims to estimate the annual operating costs associated with Royal Mail transporting collected mail from collection hubs to delivery offices.
Qualitative research	Defined by the Market Research Society as an unstructured research approach with a small number of carefully selected individuals to produce non-quantifiable insights into behaviour, motivations and attitudes. Our qualitative research, undertaken in September and October 2019, consisted of workshops, focus groups and face to face, individual interviews with vulnerable users.
Quality of Service (QoS)	A requirement (defined under DUSP condition 1.9.1) requiring Royal Mail to meet certain quality of service performance standards, including at least 93% of First Class mail to be delivered within one working day of collection and at least 98.5% of Second Class mail to be delivered within three working days of collection.
Quantitative research	A form of research which is designed to provide numerical data to quantify insights into behaviour, motivation and attitudes. Our quantitative survey research, undertaken between October-December 2019, consisted of face to face, telephone, and online interviews with representative samples of UK adult residential users and SME decision-makers.
Redirection	The USO service of redirection of all mail addressed to a particular recipient from one address to another for a specified period of time.
Return to Sender	A USO service whereby the customer receives a letter with the correct address but the wrong name, and can return it by writing "return to sender" or "not known at this address" on the envelope and putting it back in a post box or returning it to a post office. Where it can identify the sender, Royal Mail then delivers it back to the sender.
Revenue model	Our model, which looks to assess the impact on the Reported Business volumes and revenues of each scenario of changes to the scope of the USO.
Royal Mail	Royal Mail Group Limited, whose registered company number in England and Wales is 04138203. Royal Mail has been designated by Ofcom as the designated universal service provider in the UK.

Second Class (2nd Class)	The USO standard service for letters and parcels, provided by Royal Mail, which has a delivery frequency of D+3 and a QoS target of 98.5%.
Secure central locker	A receptacle used by postal operators to deliver (typically) parcels away from the recipient's door. These are often found in 'central' locations, like town or city centres.
Signed For	A USO, registered service which is an add-on to First Class and Second Class and requires signature on delivery. It includes standard compensation for loss and damage.
Single class	A postal service which typically merges and replaces the use of separate priority (e.g. First Class) and economy service (e.g. Second Class) services, instead creating one single standard of postal service.
Single piece end-to-end services	Single letters (e.g. birthday cards) sent by individuals or other entities using a post box or a Post Office, which are collected and delivered by Royal Mail.
Small Parcel	A Small Parcel is any parcel up to 45cm in length, 35cm in width and 16cm in thickness, weighing no more than 2kg.
Special Delivery Next Day (Guaranteed by 1pm)	A USO service which offers registered, tracked service which guarantees delivery of mail by 1pm the next working day, includes insurance and requires a signature on delivery. Senders have the option of buying additional levels of insurance cover.
Speed of delivery	The number of working days from the point of collection that it takes to deliver the letter(s) and/or parcel(s) in question.
Universal Service Obligation (USO)	The obligations imposed on the universal service provider by any designated universal service provider (DUSP) condition.
Universal service provider (USP)	Any postal operator currently designated by Ofcom as a universal service provider under the Postal Services Act 2011.
Universality	Refers to both the price and service provided for under the USO being uniform across all parts of the UK.
Utility score	A number used to represent the attractiveness of each feature considered under the conjoint analysis. Utility scores for each of the features can be combined for a given specification of the postal service to give an overall utility. If one specification has a higher utility score than another, then this indicates that that specification is preferred by the participant in question.
Volume	Refers to the number of letters and/or parcels which are sent with the given operator(s).
Working day	Defined under 1.1.2 of the DUSP conditions, a "working day" means any day which is not a) a Sunday; or b) a public holiday in the place of collection or the place of delivery of the postal packet.