

Future scenario developments in the Dutch postal market

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Executive Summary

In this project commissioned by the Dutch Ministry of Economic Affairs, WIK has reviewed the current situation and outlined expected trends and developments in the Dutch postal market for the next ten years. The study assesses the impact of market trends on the future sustainability of postal networks and universal postal service. Interviews with postal companies and customer representatives and a stakeholder workshop held in The Hague in September 2016 form the basis of this study, adding to WIK's standing expertise in postal regulation.

Digitisation puts pressure on letter volume

The Dutch market for domestic letter services has been continuously declining year on year. Since 2010, domestic letter volume has declined by nearly one third to 3.1 billion items and revenues by more than one fifth to 1.3 billion Euros. Between 2010 and 2015 domestic letter volume declined by 7.6% per annum. Business letters account for 93% and consumer letters for 7% of total volume. Time-critical letters ("24 hours") have declined more than non-time-critical letters ("48+ hours"). The relation between time-critical and non-time-critical delivery of domestic business letters has been shifting from around 40/60 in 2010 to one third/two thirds in 2015.

The future demand for postal services is mainly driven by the "megatrend" digitisation. Digitisation and digital readiness are extraordinarily high in the Netherlands compared to many other European countries. Today's total domestic letter volume is expected to decline by around 30-35% until 2020 and by around 45-55% until 2025. The basic development to digital communication is irreversible, but the speed of decline depends on the dynamics in the Dutch postal market. While letter volume will further decline, there are clear prospects for growth in packages and parcels (including universal service parcels) as a result of dynamic growth in e-commerce.

Digitisation puts pressure on all letter products, including universal service letters. In the Netherlands, domestic letters appear to decline more than international (import and export) letter items.

Domestic universal letter services are particularly affected by volume decline

Unlike in other EU Member States, only domestic single-piece letters and parcels ("Losse post") are defined as universal postal services in the Netherlands, while domestic bulk mail services ("Partijenpost") are outside the universal services. For international mail both single-piece and bulk mail are the part of the universal postal services. PostNL is the designated universal service provider.

While the provision of universal parcel services will benefit from the growing parcel business of PostNL, the leading delivery partner of Dutch online sellers, the decline in

letters will negatively affect the financial sustainability of the provision of universal letter services.

Domestic universal service letters account for less than 15% of total domestic letter volume. They are more affected than international universal service letters because digitisation is less advanced in most other countries than in the Netherlands. Switching from universal to non-universal postal services (e.g. to bulk mail products of PostNL or to competitors of PostNL) by small business customers additionally reduces universal service volume.

There is a high risk that universal service tariffs will further increase because volume declines. Postage for universal services is regulated by a complex formula that relates the headroom for tariff increases to the development of average fixed costs (among other things). Volume decline of time-critical letters would raise average fixed costs and therefore facilitates additional tariff increases.

Volume decline mainly threatens the sustainability of competitors' networks

Competition in the Dutch letter market has successfully emerged in time-critical and non-time-critical delivery of letters despite of the shrinking letter market.

- In the non-time-critical segment competition is characterised by slowly declining volume and fierce price competition between two remaining major players, PostNL and Sandd.
- Local and regional competitors have gradually increased their market share in time-critical delivery of letters mainly targeting small and medium-sized business customers. For “rest mail” (mail directed to addresses they do not delivery to), this group of competitors relies on PostNL’s network to organise nationwide delivery.

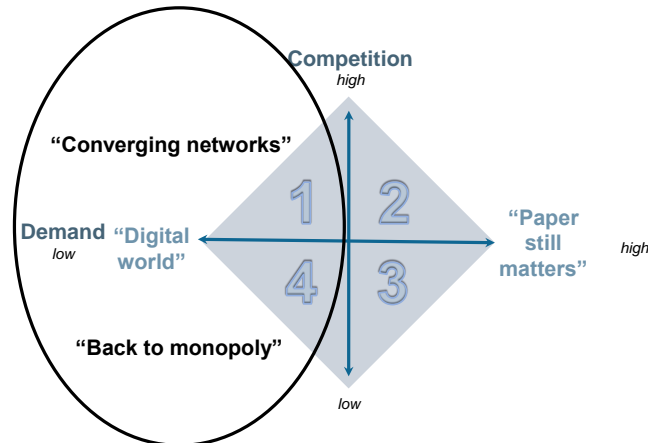
WIK has analysed the sustainability of postal networks in light of volume decline, and found that all postal networks will be challenged by letter volume decline. However, the risks for competitors will be higher than for PostNL that is more diversified. According to WIK’s assessment the sustainability of the competitors’ postal networks is additionally threatened by possible strategic pricing of the market-leader PostNL and, in the short term, by regulatory uncertainty around competitors’ access to PostNL’s network.

Competition in the Dutch letter market is at a crossroad

The decline in market volume challenges all suppliers of letter services in the Netherlands. To which extent the different postal networks are affected depends on many factors including demand trends, operators strategies, cost trends, and future regulation. To capture the uncertainty on future developments in competition, this study

has introduced two future scenarios: “Converging networks” and “Back to monopoly” (see Figure 1).

Figure 1 Future development scenarios of the Dutch letter market



The scenario “**Converging networks**” is characterised by a more competitive landscape for letter delivery services, based on commercially minded players:

- There will be two postal operators delivering non-time-critical letters nationwide and regional competitors specialised on time-critical delivery of documents and goods (in addition to PostNL).
- Business mailers have an incentive to support future competition in the market for strategic reasons.
- Regional competitors will further develop the cooperation with other competitors, parcel operators, and PostNL to offer best value to postal customers.
- Inter-carrier business will become a major business for all postal operators, including PostNL, and carriers will regard each other as important customers (in addition to competing in other market segments).

“**Back to monopoly**” describes a development path where volume decline could result in a situation with the incumbent as the only surviving company to provide letter services in the Netherlands.

- PostNL has significant economies of scale and scope and is well-prepared for future challenges due to improved customer service, new and improved products, sophisticated IT solutions, highly efficient letter and parcel operations and its ability to rescale letter operations in line with volume decline.

- In contrast to the “multi-product” company PostNL, most competitors are “stand-alone” suppliers of specific postal products, like Sandd, and have less opportunities to compensate losses in letter delivery by other businesses. Sandd will face increasing average costs due to volume decline and increasing input costs. If their letter business becomes loss-making, the flexible, relatively small regional competitors will exit the postal delivery segment.
- In “Back to monopoly”, the combination of increasing average costs and intense price competition with the incumbent would result, in practice, in a fall back to the postal monopoly of the last millennium.

Scenarios for future postal policy

Dutch postal legislation is guided by two main objectives: (1) To ensure an affordable and sustainable universal postal service and (2) to ensure a sustainable competitive postal market.

This study assessed a variety of detailed policy options and their appropriateness in the scenarios “Back to monopoly” and “Converging networks”. Based on the impact analysis of potential policy options, for each scenario, the study recommends appropriate responses from Dutch postal policy.

“Converging networks”: Protect infrastructure competition for the benefit of postal users

The scenario “Converging networks” requires a balanced approach to ensuring universal postal service by relying on market powers. This approach puts emphasis on competition and trust in commercial solutions to meet the challenges of a shrinking postal market.

Rely on market forces to ensure the universal postal service. In this situation, WIK recommends relying on market forces first before designating a universal service provider for some or all universal postal services. Designating the market dominant postal operator to provide universal service, or parts of it, should only be considered if the market did not satisfactorily provide all universal services. If no postal company was designated, the regulation of universal service tariffs, if considered necessary, could be linked to the market dominant position of a postal operator.

More flexible universal service requirements. Universal service requirements are regulated by Ministry decision and can be adapted based on an evaluation of the USO every three years. The number of options for further reducing universal service requirements consistent with the Postal Directive appears limited. However, there will still be room of manoeuvre by, for example, further relaxing the accessibility requirements and by considering exemptions from five-day collection and delivery.

Impose basic access products for rest mail. As long as local and regional competitors do not have nationwide coverage, they need access to an existing postal network for their “rest mail”, i.e. for the mail which they collect from their customers but that is directed to areas/addresses that they do not deliver to. Imposing access products in time-critical delivery should be the measure of last resort, i.e. such obligations should be imposed only after negotiations between the market dominant operator and competitors have failed. For this purpose, the existing legal instrument of access regulation (Article 13a-k) of the Postal Law (Postwet) should be kept as a possibility, but should be implemented by ACM with great care in practice.

Enforced action against possible predatory pricing, fidelity rebates and tying. To support the transition to “Converging networks”, strict enforcement of competition law standards appears necessary as long as PostNL continues to be dominant. To prevent anticompetitive pricing strategies, ACM should be informed about individual contracts and the pricing behaviour of the market dominant postal operator on a regular base.

“Back to monopoly”: *Ensure universal postal services in the Digital World*

Even in the “Digital World” universal postal service will still play a role for secure and reliable communication between all households, individuals, businesses, and government offices. This scenario for future postal policy gives emphasis to ensuring these services for the general public in light of changing postal users’ needs and technological progress.

Keep PostNL as designated USP in the Dutch letter market. In the scenario “Back to monopoly”, PostNL will be the only surviving postal operator in the Dutch letter market. Keeping PostNL as the designated universal service provider will be the most appropriate instrument to replace missing market incentives, particularly for most vulnerable postal users, notably consumers. For the increasingly competitive Dutch parcel market, however, WIK recommends not designating PostNL (or anybody) for the provision of parcel services but to rely on market forces.

Allow for more flexible universal service requirements. Due to declining demand for USO services considering more flexible universal service requirements will also be appropriate in “Back to monopoly”.

Require segment reporting on USO services. If policy makers decided to stick to designation of one postal operator (i.e. PostNL) as WIK recommends for “Back to monopoly” it should be considered to require a more detailed reporting on universal services to improve transparency in costs, revenues and volume in order to facilitate policy decisions on future USO requirements.

1 Introduction

1.1 Study focus and central research questions

The Netherlands is one of the European countries that are mostly affected by declining letter volume. Since 2010 the Dutch letter market has gone down by nearly one fifth in revenue and one third in volume.¹ For the last two years PostNL reported positive margins in the provision of universal postal services.² Letter prices for consumers and small business mailers have been substantially increased while medium-sized and large business mailers were less affected by price increases in time-critical delivery.³ The market developments challenge the sustainability of universal service provision and the future of the Dutch letter market. Despite of these demand trends local and regional competition in time-critical delivery of letters has been emerging. With Sandd and PostNL, there are two nationwide players for delivering non-time-critical letters. Growing competition in a strongly declining letter market is unique in Europe and impressively reflects that the Dutch postal policy is guided by two major objectives:

- Ensuring an affordable and sustainable provision of universal postal services
- Ensuring a sustainable competitive postal market (and thus choice for Dutch consumers and businesses)

Infrastructure competition in time-critical delivery of letters is emerging at local and regional level. So far, no nationwide network for five day delivery has been developed so that local competitors still need access to PostNL's postal network to ensure that the letters they collect from their customers are delivered nationwide. The discussion of how to regulate access to PostNL's network is controversially discussed among stakeholders. The Ministry therefore asked WIK-Consult to put some emphasis on this important topic in postal regulation.

The Ministry commissioned WIK-Consult in July 2016 to conduct a study on future scenario developments in the Dutch postal market. The study was carried out from July to November 2016. It shall provide solid input for policy options needed to facilitate the long term sustainability of the postal networks in light of the objectives of the Dutch postal policy.

¹ Based on ACM (2015), The current state of the Dutch postal market, press notice of 22 December 2015 and information provided by ACM.

² See PostNL, Financiële Verantwoording universele postdienst 2014 and 2015.

³ See PostNL, Postal rates (2010-2017).

WIK was specifically requested to address the following central research questions:

- What are the expected trends and developments in the Dutch domestic postal market in the 10 coming years (2025) and what effect will these developments have on the sustainable exploitation of the postal networks in the Netherlands, especially on the sustainability of a postal network (or a combination of postal networks) that has (have) to fulfil USO obligations?
- Given possible future market developments and business models, what aspects need specific attention in order to safeguard that the postal legislation and regulation adequately enable a sustainable postal service and which components of that policy framework might require adjustment to ensure financially sustainable provision thereof?
- What are the main prerequisites for a viable USO provision in the middle- and long term and how should the designation of the USO be organised?

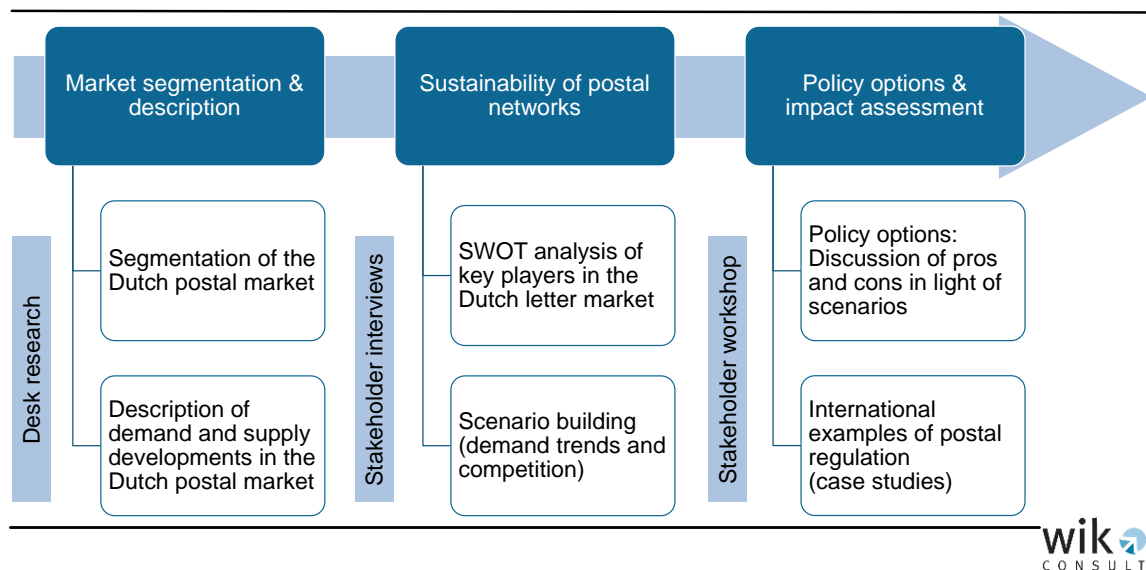
Policymakers need a solid understanding of current and, more importantly, future postal market developments and how these developments affect the supply of postal services in order to optimally adapt postal legislation in light of the objectives of postal policy. This study shall support policymakers to come to well-informed decisions.

The research on current and future trends of demand and competition in the Dutch postal market is based on extensive desk research and on interviews with many stakeholders, including ACM, PostNL, Sandd, VSP and local competitors in letter delivery, parcel operators as well as representatives from the mailer side including Thuiswinkel, VGP and DDMA. We discussed the draft scenarios in a well-visited stakeholder workshop taken place in Den Haag on 15 September 2016. Last but not least, WIK has been working closely with the Ministry. We are most grateful for the time, information and expertise received from the organisations and individuals that have contributed to our study. While gladly acknowledging this assistance, WIK-Consult remains, of course, responsible for the report, including any errors it may contain.

1.2 Methodology of the study

The study was prepared for the Dutch Ministry of Economics (“Ministerie van Economische Zaken”), by Alex Dieke (project director), Antonia Niederprüm (project manager), Annette Hillebrand and Christian Bender (all WIK-Consult). The project team was supported by a Dutch colleague, Stefano Lucidi (WIK-Consult). The project was carried out from July to November 2016.

Figure 1 WIK's methodology



Source: WIK

In Section 2 the study starts with a description of recent developments in the Dutch postal market for the demand and the supply side of letter and parcel services as well as in the provision of universal postal services. Section 3 shed light on future letter volume development and discusses the strengths, weaknesses, opportunities and threats of the key market players in the Dutch letter market. Based on these results the future development scenarios are presented and the long-term sustainability of universal postal services is discussed given the current regulatory framework. In Section 4 the study outlines scenarios for future postal policy for each of the scenarios consisting of selected policy options. The detailed discussion of all policy options is presented in the Appendix of this study.

This study relies on three methodological approaches: desk research, stakeholder interviews and one stakeholder workshop.

Desk research formed the starting point and was the major source of information on the postal legislation in the Netherlands and recent trends in demand and supply. In close cooperation with the Ministry and ACM, WIK had access to all relevant market reports, and decisions prepared by ACM (formerly Opta) since 2010. Additionally, stakeholders provided useful studies and surveys on demand trends.

In July and August WIK conducted in total eleven interviews, most face-to-face. Minutes of the interviews were exchanged with each partner. The interviews improved our understanding on the Dutch letter and parcel market and provided input for the scenario building and the SWOT analysis of the major players in the Dutch letter market.

Table 1 List of interview partners

Stakeholder group	Organisations interviewed
Postal service providers	PostNL Mail
	Sandd
	Van Straaten Post
	Cycloon / Businesspost
Parcel service providers	PostNL Parcel
	DPD
National regulatory authority	ACM
Mailers	Vereniging Grootgebruikers Postdiensten (VGP)
	Data Driven Marketing Association (DDMA)
	Thuiswinkel Waarborg

WIK organised a stakeholder workshop that took place in Den Haag on 15 September 2016. Around 20 stakeholders participated in the workshop. Participants included most of the interview partners and additionally, representatives of DHL Parcel and the Vereniging van Postal en Bancaire Retailers (VVP).

Table 2 Programme of the stakeholder workshop

Time	Programme
09.30-10.00	Arrival
10.00-10.10	Welcome address and overall introduction of project (MinEZ)
10.10-10.30	Round of introductions
10.30-11.00	The Dutch postal market – today and tomorrow WIK presentation
11.00-12.00	Discussion in working groups: Group A “Evolution of mailer needs” Group B “Challenges for postal operators”
12.00-12.10	Break
12.10-12.40	Groups report findings & Discussion
12.40-12.50	Closing remarks (WIK)
12.50-13.00	Next steps of the project and the overall process (MinEZ)
13.00	Lunch

The stakeholder workshop was used for an in-depth validation of scenarios and the discussion of their impact on the stakeholders. The results of the workshop contributed greatly to the outcome of this study.

1.3 Market segmentation

As outlined the study mainly focusses on postal services as legally defined in the Dutch postal regulatory framework. Postal services include addressed letter items including publications sent by post and USO⁴ parcels (i.e. “fully paid” single-piece parcels franked and sent by consumers and very small business mailers via post offices). According to the terms of reference WIK puts the emphasis on domestic postal services i.e. items collected and sent within the Netherlands. However, market developments and their impact do not fully coincide with legal definitions. For the better understanding of market developments and in light of “converging” networks we also shed some light on developments in the Dutch parcel market.

Depending on the point of view we apply three different segmentations of the Dutch postal market.

- The “demand-side view” is necessary to discuss the impact of digitisation on letter and parcel volume. We differentiate five major segments.



Social mail consists of letters and cards mainly sent between individuals / consumers.

Business communication consists of daily business communication between companies and suppliers/customers respectively between public authorities and citizens/private and public institutions. Businesses include private and public institutions, i.e. companies, public authorities, non-profit organisations and similar institutions. Additional to transaction letters, like invoices this also includes day-to-day communication (office mail). Advertising mail refers to direct mail, i.e. addressed advertising letters while publications include regularly published periodicals and magazines (e.g. TV magazines) and customer/member magazines for example issued by associations (for example Algemene Nederlandsche Wielrijders-Bond, ANWB).

Merchandise or goods delivered by postal or by parcel companies is an increasingly important segment particularly in the parcel market. In case of small, light-weight and low value goods this growing segment also offer opportunities not only for parcel, express and courier companies but also in letter delivery.⁵

⁴ USO is the abbreviation for Universal Service Obligation. USO parcels are parcel services that are subject to the universal service obligation.

⁵ See Section 2.2 for more detail.

- The “supply-side view” includes the presentation of the key players in the Dutch letter market and recent developments in competition.



For the discussion of current and potentially future developments in competition we compare the Dutch letter market into two major segments: Time-critical and non-time-critical postal services.

Time-critical postal services are usually delivered the next working day (“24uurspost”) and require the collection and delivery of postal items on at least five days per week. Time-critical postal services mainly include the collection and delivery of consumer and business letters (business communication). A small proportion of advertising mail and publications are also delivered the next working day. Business and consumer parcels can also be considered as time-critical as these items are mostly delivered the next working day.

Non-time-critical letters are not delivered on five days per week but depending on the supplier on three or two days per week. Today, business mailers have the choice between “48 hours” and “72+ hours” delivery. The combined offer of PostNL and Sandd allows business mailers to get their letters delivered on Tuesdays, Thursdays, Fridays or Saturdays. The difference between the non-time-critical offers is that mailers have the opportunity to either hand over their consignments three or two working days before the planned delivery day. Additionally, there are offers in the market to deliver letters within one week time after consignment (72+).

- The “regulatory view” allows putting the emphasis on a specific sub-segment of the Dutch postal market, the universal postal services.



One major task in this study is to discuss the impact on the provision of universal postal services (“USO postal services”).

In the Netherlands, the universal postal services mainly include

- Domestic addressed letters weighing up to 2,000 grams and domestic parcels (“counter parcels”) weighing up to 10 kilograms, priced at the single-piece tariff.
- International inbound and outbound mail items, i.e. letters and parcels (weighing up to 20kg) collected or delivered by the designated universal service provider (single-piece and bulk).

- Registered and insured letter and parcel services

International USO postal services are also considered as time-critical because the transport from collection points to the Dutch international exchange offices as well as the transport and delivery from the Dutch international exchange office to recipients usually have to be done within one working day.

Non-universal postal services include domestic bulk mail services (letters and parcels). Other delivery services, including non-USO parcel, express and courier services are legally not considered as postal services.

2 The Dutch postal market today

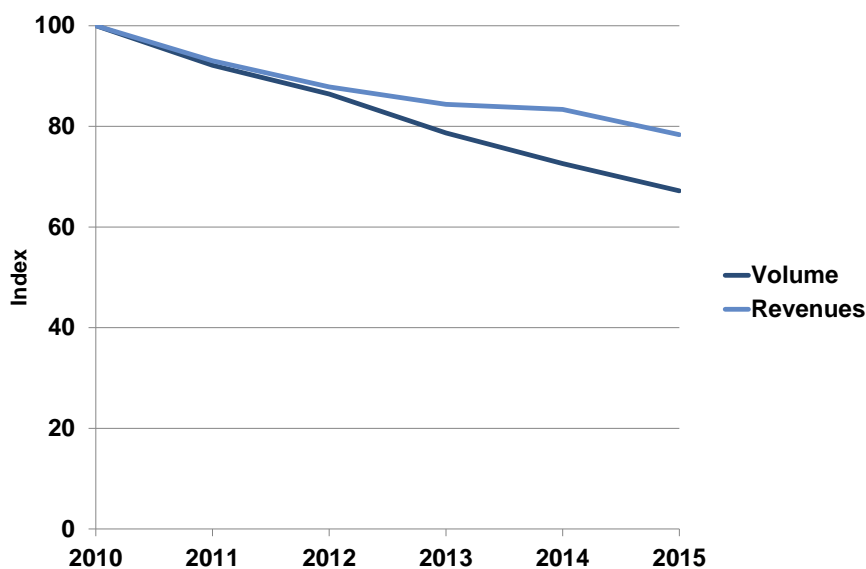
In this Section the current situation of the Dutch postal market is described. It summarizes our understanding of the developments in the Dutch postal market since 2010 we have got in several in-depth interviews with market participants and reflected by discussions with Dutch postal stakeholders. Section 2.3 takes a closer look at universal services provided in the Dutch postal market.

2.1 Letter services

2.1.1 Demand for letter services

The Dutch market for domestic letter services has been continuously declining year on year. Since 2010, domestic letter volume has declined by nearly one third to 3.12 billion items and revenues by more than one fifth to 1.29 billion Euros.⁶ Between 2010 and 2015 domestic letter volume declined by 7.6% per anno.

Figure 2 Development of domestic letter volume and revenues between 2010 and 2015



Source: Based on ACM (2016), Ontwikkelingen en feiten bij de Nederlandse postmarkt in 2015, 21 November 2016, and information provided by ACM

⁶ See ACM (2016), Ontwikkelingen en feiten bij de Nederlandse postmarkt in 2015, 21 November 2016.

Major drivers of this development were general economic developments and, more importantly, the “megatrend” digitisation and its impact on the use of paper-based communication and advertising channels.

Digitisation and digital readiness, i.e. the ability and the infrastructure to use online communication is very high in the Netherlands. A turnaround of the megatrend digitisation is most unlikely. The number of households with internet access is approaching 100% and there are more than 90% of households using broadband access.⁷ There is almost no gap between urban and rural coverage. The Digital Agenda for Europe (DAE) target for coverage with 100 Mbps for 50% of the European households until 2020 was already exceeded in the Netherlands in 2013. Coverage exceeds 95% of households.⁸ The Netherlands, together with Norway, Sweden and Denmark are the leaders in terms of LTE⁹ coverage in the EU (99% of households).¹⁰

According to Eurostat, 90% of all Dutch internet users browse the web daily and 88% send e-mails and 58% SMS regularly (2015).¹¹ Recent figures of Statistics Netherlands show that the number of non-users is less than 8% of the whole population (older than 12 years, i.e. around 1.2 million people) consisting mostly of people at retirement age. Even in the age group of the over 75 year olds adoption rates are still growing. In 2012 66% of people aged 75+ did not use the Internet. Today this group has declined to 50%.¹²

Dutch people are also frequent users of social media. More than 11 million onliners claim to use it daily, 6.6 million use Facebook every day thus substituting e-mails and text messages in their electronic communication.¹³

Mobile internet use is also on the uptake. More than eight out of ten Dutch consumers have a smartphone (81%, 2015), a plus of 11 percentage points compared to 2014. The increase is mainly caused by growth among the age group 50+. Half of the people 65+ own a smartphone. Among the age group of 12 to 30 year olds penetration is approaching 100%.¹⁴

⁷ 95% of households had internet access in 2013. See CBS (2016): ICT gebruik van huishoudens naar huishoudkenmerken, 2005 – 2013.

⁸ See European Commission, Digital Single Market, Country information – Netherlands, <https://ec.europa.eu/digital-single-market/country-information-netherlands>

⁹ LTE means “Long Term Evolution” and describes the mobile communication standard of the fourth generation (4G).

¹⁰ See European Commission (2016): Broadband Coverage in Europe 2015, p. 8.

¹¹ See Eurobarometer October 2015, CBS 2015, ICT, kennis en economie.

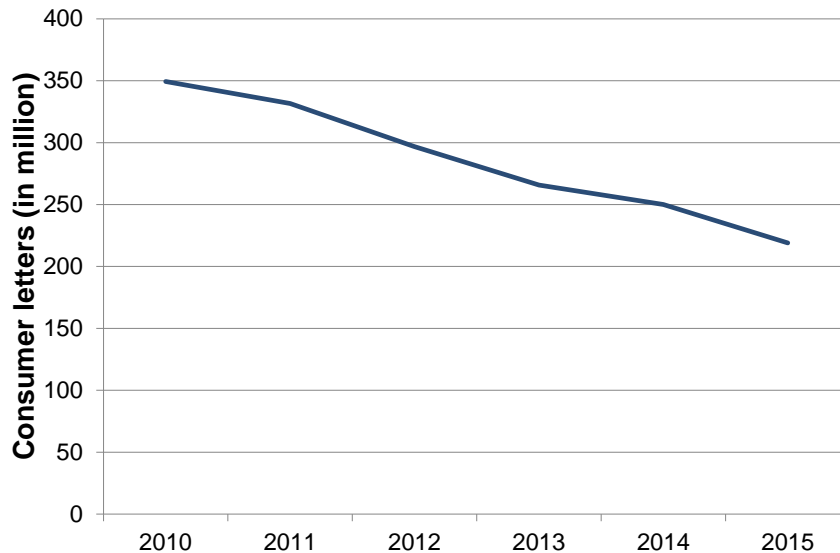
¹² See CBS (2016): Acht procent van de Nederlanders nooit op internet, press release 3 June 2016.

¹³ See eCommerce Europe, Country Report Netherlands 2016.

¹⁴ See ‘Dutch Smartphone User’ of Q1 2015 report by Telecompaper, quoted in: <http://www.dutchdailynews.com/majority-of-the-elderly-in-the-netherlands-has-a-smartphone/>

Social mail is substantially affected by digitisation

Figure 3 Development of domestic letters sent by consumers



Source: Based on ACM (2016), *Ontwikkelingen en feiten bij de Nederlandse postmarkt in 2015*, 21 November 2016, and information provided by ACM.

“Social mail” is undeniably put under the most pressure from substitution: Since 2010 consumer letters have declined from 350¹⁵ to 220¹⁶ million items or by 8.9% per anno and account for about 7% of domestic letter volume.¹⁷ Standard letters from consumer to consumer have almost vanished and anniversary cards, Christmas cards and holiday postcards are also much less popular than several years ago. Texting or sending Facebook messages for birthdays has become commonly accepted in certain age groups as Dutch market experts point out. Christmas and New Year cards account for about half of total social mail and results in peak in delivery in December and early January.

Business communication mail

Business communication mail consists of Government-to-all (i.e. consumers, businesses and other government authorities) and Business-to-all (i.e. to consumers, other businesses and public authorities) letters. That way, substitution in this segment comprises the implementation of online solutions for businesses as well as e-government trends.¹⁸

¹⁵ See WIK-Consult (2011), *Developments in the Dutch Postal Market*, p. 35.

¹⁶ See ACM (2016), *Ontwikkelingen en feiten bij de Nederlandse postmarkt in 2015*, 21 November 2016.

¹⁷ Ibid.

¹⁸ For an overview see CBS (2015): *ICT kennis an economie 2015*, Den Haag.

G2X letters decrease due to successful e-government implementation

E-government as a form of government-to-citizens communication meets with broad acceptance of internet usage and vast diffusion of devices and infrastructure. The Netherlands are one of the forerunners in e-government implementation in Europe. Future prospects are driven by the Dutch digital agenda “Digitaal 2017” and in particular the implementation of the “Berichtenbox”. Both foster the substitution of government letter post by electronic communications.

The Dutch government introduced MijnOverheid.nl, a website for all public authorities and citizens. Today, there are more than 200 institutions participating, e.g. the tax authority, pension funds, local authorities (communities), etc. From the beginning, MijnOverheid.nl was frequently used for a variety of services. In April 2016 the platform had five million users, one year ago there were only 1.8 million. Statistically, 38% of the population older than 20 years, or 50% of the population aged between 20 and 65 years are using this e-government service.¹⁹

The rapid increase is mainly due to a law coming into effect on 1st November 2015 that will abolish letter mail in the financial and tax sector.²⁰ Tax letters (“blauwe brieven”) shall be abolished completely by the end of 2018. The initial deadline of 2017 had proved to be too ambitious.²¹ From 1 January 2019 all mail in finance and tax will be digital by default. There is an opt-out system in place for any citizen who prefers letters.

This development in e-government will severely reduce the letter volume of 300 million national government letters per year. Till the end of 2022, a maximum of 150 million letters could for example be substituted in the tax area.²² Given that an estimated 5% of population might refuse the new solution there will be less than one million Dutch people receiving letters from the public authorities on a regular basis. Some experts claim that these people will receive about 15 letters per year which then sums up to less than 15 million letters per year.²³

¹⁹ See Rijksoverheid, Nieuwsbericht 29-04-2016: 5 miljoen Nederlanders gebruiken digitale Berichtenbox MijnOverheid (<https://www.rijksoverheid.nl/actueel/nieuws/2016/04/29/5-miljoen-nederlanders-gebruiken-digitale-berichtenbox-mijnoverheid>)

²⁰ See Wet elektronisch berichtenverkeer belastingdienst (Law from 14 October 2015 that came into effect on November 1st 2015), <https://zoek.officielebekendmakingen.nl/stb-2015-378.html>.

²¹ Information in this section is based on expert interviews and workshop results. In many respects, the Dutch e-government initiatives follows the Danish example. Denmark has established mandatory digital self-service since 1. November 2014, for details see European Commission (2015), eGovernment in Denmark.

²² “De Belastingdienst stuurt momenteel circa 150 miljoen blauwe brieven per jaar. Dit zijn uitnodigingen voor het doen van aangiften, beschikkingen, informatieverzoeken, afhandeling van bezwaarschriften, aanslagen, enz. In het jaar 2015 deed de belastingdienst dat voor het 100e jaar. Dit vormt een grote kostenpost en in het kader van de bezuinigingen en digitaliseringsdrift, is besloten de blauwe envelop in een periode van 7 jaren af te schaffen.”, see <http://www.baa.nl/berichtenbox-mijnoverheid-vaarwel-blauwe-envelop/>.

²³ Estimations from interview partners.

Step-by-step government mail on all levels, local and national, will be substituted. Following the law for financial and tax communication there will be regulations to provide a digital infrastructure for each sector. Digital signing and electronic identification schemes for identification will be developed for each sector and its special requirements.

B2X letters decrease because of e-invoicing and seamless working solutions

In B2B communication substitution rates are lower and adoption of digital solutions is slower compared to e-government solutions. For example, exchange via electronic data interchange (EDI) standards, enterprise resource planning (ERP), customer relationship management (CRM) or e-invoicing is used to a lower extent in small and medium-sized enterprises while at large companies seamless working has already been going on for some time.

In the field of e-invoicing, substitutional effects may still significantly increase in future as recent surveys suggest. In 2013, 28% of companies did not receive and 59% did not send e-invoices.²⁴

From all invoices companies send to their business partners and customers paper-based billing still accounts for a large amount (56% of all invoices in 2013²⁵) but this number decreases. The largest share of paper invoices is to be found in the financial sector (72% in 2013). Experts emphasise that letters are often used when security and safety issues are essential (authentication, integrity, confidentiality).

Successful digitisation in business communication involves the need for ICT knowledge. In the Netherlands, the Digital Agenda.nl activities foster these qualifications. Today, already 65% of all employees work with Internet PCs and 69% of all companies use teleworking.²⁶ The ICT strategy may also be part of „green politics“ in more and more companies and avoiding paper-based communications is considered a sign of environmental awareness. All these developments contribute to increasing substitution of letters.

In the future, not only the substitution of letters could influence volume decline but also a “leapfrogging” trend in innovations. More and more companies will not choose in-between solutions that need mailings for security reasons (i.e. sending of ID confirmations per letter) but move to a pure digital solution from the start. This might be true for payment and transactions based on mobile communication. In contrast to traditional telecommunications, mobile devices offer a high degree of personalised and secured communication and in this way paper-based identification schemes may become redundant.

²⁴ See Centraal Bureau voor de Statistiek (CBS), ICT, kennis en economie 2015.

²⁵ Ibid.

²⁶ Ibid.

Direct mail can be still a relevant option in an advertisement mix of the future.

Direct mail (addressed advertising letters) competes with other forms of advertising. In general, overall advertising expenditure is related to economic development. The allocation of the advertisers' budgets will probably be determined by online and on-screen options, as marketing trends for the last two years suggest. Online media account for the largest share of advertisement spending (45%), followed by TV (28%), newspapers (11%), radio (7%), out of home (5%) and magazines (4%). Budgets for advertisement in the internet are expected to rise by 7,8% in 2016 while magazines and newspapers will go down (-12.5% / 5.1%).²⁷

There are no statistics for direct mail volume available but the above mentioned indicators suggest how factors like real time information exchange and potential cost reductions contribute to volume loss in this segment. Apparently advertisers are willing to raise their investment budgets for digital campaigns but not so much for paper-based marketing.

Direct mail compared to mail based on online media becomes less important to advertisers.²⁸ In a non-representative survey by DDMA in 2015 only 20% of participants expect direct mail to increase in the forthcoming year but 27% expect a decrease and 42% see its volume unchanged (11%: do not know).

In addition, environmental issues influence the acceptance of advertisements. Some local authorities like e.g. Amsterdam have already put a regulation in place where citizens do not receive unaddressed advertising (leaflets) unless a sticker on their letter box gives an opt-in sign. By this, the city wants to reduce litter in the streets. It seems likely that more regulation to prevent paper waste might be put in place and will also have effects on direct mail.

Furthermore, people are reluctant to receive personalised advertisements whether by addressed advertising or online. Data protection and privacy concerns can influence digital advertisement channels as well as direct mail. People more and more opt for do-not-write-me registers or use ad block options. A recent study points out that "there is evidence that 35% of Dutch shoppers in the 18 – 24 age group use website ad-blocking software" but direct mail "combined with digital marketing has a role in consumer communications for some brands. This will be particularly true where DM can support a brand message that arrives amongst the almost 100 marketing emails a week that Dutch online consumers receive."²⁹ In conclusion, trends in the advertising segment have to be seen as ambivalent and can have contradictory effects on demand for letter products for advertising.

²⁷ See Deloitte (2016), IAB report on Online Advertising Spend The Netherlands 2015, March 2016.

²⁸ See survey of DDMA (2015): DM barometer. De marketeer in 2015, January 2015.

²⁹ See E-Commerce worldwide (2016): Belgium & Netherlands Cross-Border Trading Passport 2016. p. 39.

On the other hand, response rates, interaction and “look & feel”, as well as digital illiteracy may be in favour of using direct mail.³⁰ Data compiled by Post NL and Spring Global Delivery Solutions suggests that 87% of direct mail is opened and read.³¹

It cannot be denied that direct mail can be still a relevant option in an advertisement mix. Innovations emerge, like e.g. 2D codes on letters which enable tracking and personalised offers. Cross-advertisement (e.g. certain consumer clusters are targeted via different channels) can become more important in future. Big data analysis will help to combine campaigns. Direct mail can have a part in this. Its future role, however, also depends on the competitiveness of paper-based advertising and the innovative power of the postal sector to promote its attractiveness.

Publishers jeopardise their business for several years now without gaining compensation for revenue losses in the paper-based segment

An overall substitution of traditional daily newspapers, general and special interest magazines or blogs are a very common phenomenon today. Publishers offer their products not only on paper but also as online magazines or apps and thereby jeopardise their traditional businesses. At first, many offered their online editions for free, nowadays “freemium” is a popular pricing strategy by which some information is provided free of charge but readers are charged for additional features and exclusive content. If micropayment would become more widely accepted, these service offers could prove to be more profitable in future.

For more than 15 years these so-called jeopardising tendencies do not remain without consequences for revenues. Readers willingly accept stripped down online news which are free of charge and advertisers responded accordingly. Advertising budgets are shifted to online media and budgets for print media shrink. In the end, a vicious circle of substitutional effects and decreasing advertising budgets can be observed (see Figure 4).

30 Even (pure) e-retailers use direct mail for advertising because of better targeting and higher response rates as experts in the interviews pointed out.

31 See E-Commerce worldwide (2016): Belgium & Netherlands Cross-Border Trading Passport 2016. p. 39. The study cites surveys that suggest: “67% of online searches are triggered by the mail piece. Online advertising, in conjunction with physical DM, leads to a 25% increase in response rates.”

Figure 4 Vicious circle of online substitution in the periodicals segment



Source: WIK

As observed in the advertising segment trade-offs between digital and print trends can also occur in the periodicals segment. On the one hand, the general economic development might stabilise demand for print and some new periodicals in the field of special interest magazines surprisingly became a market success against the overall trend. Print customer magazines have apparently also developed into a popular form of marketing. On the other hand, traditional periodicals like TV guides are particularly affected by substitutional effects and new (customer) magazines surely cannot be expected to compensate overall volume loss in the periodicals segment.

Ease of use and convenience as well as cost savings (and partly, environmental issues) lead people to prefer digital media like tablet computers instead of reading paper-based newspapers. This is especially the case in the age group 50+.³² Tablet users will unsubscribe to their magazines if digital alternatives offer sufficient content. Digital natives will probably not become accustomed to the look & feel of print magazines but prefer interactive products altogether.

Preconditions are in favour for substitutions as figures about the popularity of tablet computers show:³³

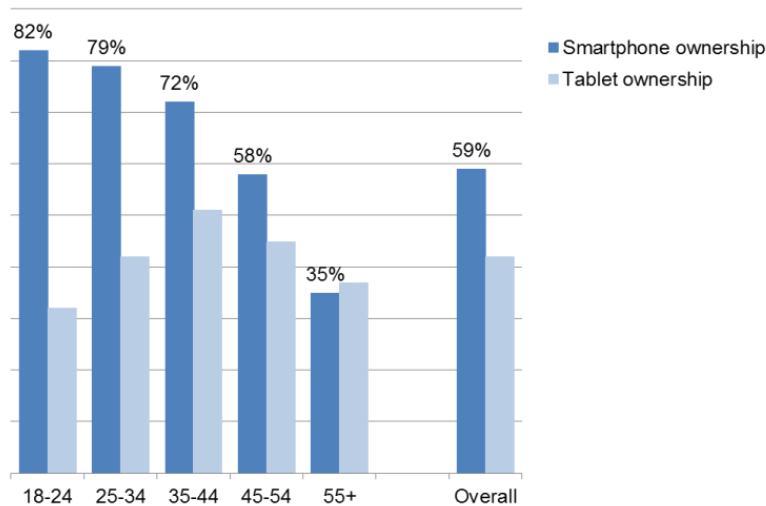
- In 61% of households (Q4 2014) in the Netherlands people use a tablet
- Use at home (for example „dual screen“ in front of the TV) predominates, only 25% of tablets used out and about
- 17% of Dutch consumers without a tablet plan to buy one

³² See Deloitte (2013), Global Mobile Consumer Survey – Addicted to Connectivity.

³³ See Telecompaper Consumer Panel 2014 (Q4), “Telecompaper Press Release: Dutch tablet market still growing, fifth of households have at least 2 tablets” (based on a survey of 6,200 Dutch consumers aged 12-80).

37% of users are older than 55 years and experts suggest that elderly people form an interesting target group for tablet computers in future.

Figure 5 People that own or have access to mobile devices (per age group in %)



Source: Deloitte 2013 (base: Total respondents 2,009)

Time-critical delivery has become less important to business mailers

Time-critical delivery comprises most single-piece letters of consumer and businesses (including public authorities and non-profit organisation) and some bulk mail consisting mainly of business letters or business communication, some publications (periodicals) and a low share of advertising. Business mailers increasingly use non-time-critical letters for daily communication and transaction letters. While speed of delivery plays a less important role in the delivery of advertising and periodicals reliable delivery on specific delivery days (day-definite) delivery is more important. Most advertising letters and periodicals (including sponsored magazines) use non-time-critical delivery services.

Both segments are declining, time-critical delivery more than non-time-critical. The relation between time-critical and non-time-critical delivery of domestic business letters has been shifting from around 40/60 in 2010³⁴ to one third/two thirds in 2014³⁵. This demand trend has also been driven by significantly increasing prices for time-critical delivery between 2010 and 2014 while average prices for non-time-critical delivery have remained fairly stable during the same period.³⁶ Based on a representative business customer survey SEO analysed, among others, the switching behaviour of business

³⁴ WIK estimation based on Opta (2011), De Nederlandse Postmarkt in 2010, p. 29.

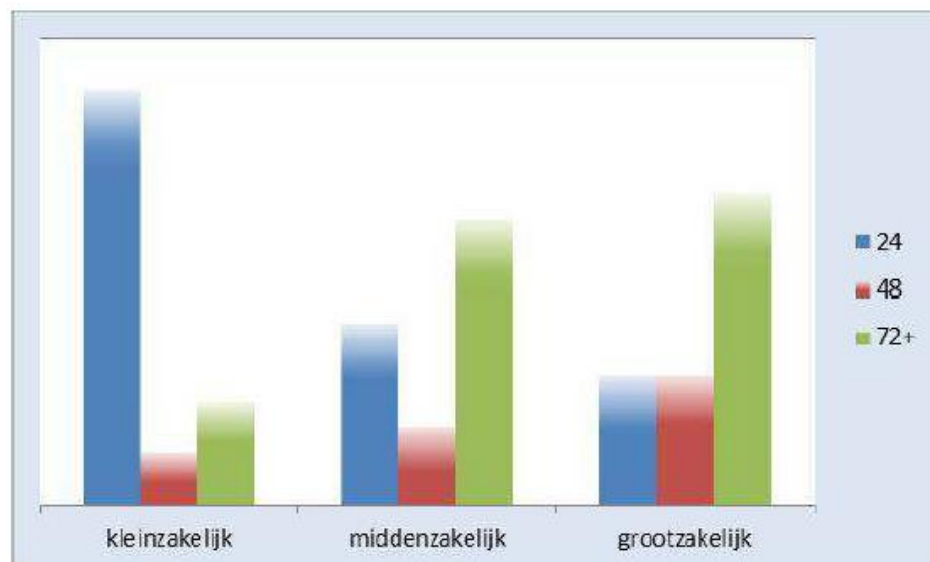
³⁵ See ACM (2016), Marktanalysebesluit 24-uurs zakelijke post, Ontwerpbesluit, openbare versie, Figuur 4, p. 39.

³⁶ Ibid., Figuur 3, p. 38.

mailers following a 10% price increase for next-day delivery services. The conjoint analysis provided indications that business mailers switch to the relatively cheaper, slower delivery services first before switching to electronic alternatives.³⁷

ACM's collected data on the demand behaviour of business mailers depending on their size in terms of total letters sent per annum.³⁸ ACM defined three categories of business mailers: small business mailers sent up to 100,000 items per year, medium-sized business mailers between 100,000 and 2.5 million items and large business mailers more than 2.5 million items per annum. ACM's research shows that small business mailers still prefer using time-critical delivery services while medium-sized and particularly large business mailers already switched a substantial proportion of time-critical letters to non-time-critical delivery services.³⁹

Figure 6 Demand for time-critical and non-time-critical delivery (2014)



Source: ACM (2016), Marktanalysebesluit 24-uurs zakelijke post, Ontwerpbesluit, openbare versie, Figuur 6, p. 45.

The larger the mailer the more important the postal budget and the cost-driving effect of price increases on the budget. The incentive to switch to cheaper delivery solutions is therefore higher for medium-sized and large business mailers than for small ones.

³⁷ See SEO (2014), Keuzemogelijkheden en overstapedrag zakelijk postvervoer, Study commissioned by ACM. ACM discussed some caveats of the SEO analysis in its market analysis. Among others, SEO had not distinguished between the structure of time-critical and non-time-critical mail flows, see ACM (2016), Marktanalysebesluit 24-uurs zakelijke post, Ontwerpbesluit, openbare versie, p. 132 sseq.

³⁸ See ACM (2016), Marktanalysebesluit 24-uurs zakelijke post, Ontwerpbesluit, openbare versie.

³⁹ Ibid., Figuur 6, p. 45.

Small business mailers switched less to slower delivery services. One reason can be that very small business mailers do not reach the volume thresholds per consignment to benefit from PostNL's lower bulk mail rates in order to get access to non-time-critical delivery services than next-day delivery. Additionally, emerging competition in time-critical delivery improved small business mailers' choice among postal companies providing next-day delivery services. Local postal companies offered cheaper time-critical delivery services and become therefore more interesting to small business mailers who mainly send letters within locally (not nationwide). This switch from PostNL's to competitors' time-critical delivery services is reflected in a growing market share of this group of competitors and may have additionally limit the switching from next-day to slower delivery services.

2.1.2 Supply of letter services

PostNL is the biggest postal company in the Dutch letter market and provides letter delivery services in the time-critical and the non-time-critical segment.

Non-time-critical delivery

The Dutch letter market was fully opened to competition in April 2009. "Printed matter" (advertising and publications) has long been fully liberalized before the implementation of the Postal Directive⁴⁰ in the Netherlands. The most competitive letter segments was the delivery of non-time-critical letter items, i.e. advertising letters and periodicals, while competition in the delivery of time-critical letters (i.e. consumer letters and most business communication) was very limited at that time.⁴¹ In 2010, the major competitors in the Dutch mail market were Sandd, a privately owned mail company, and Selektmail owned by Deutsche Post with a combined market share of around 14% (in volume, 2010). Both companies delivered mainly advertising mail and magazines twice a week.

To compete with these lower cost networks, PostNL also offered a budget mail service via its subsidiary Netwerk VSP. The general volume trend, combined with fierce price competition, prompted a consolidation process in the letter market. In the first half of 2011, Deutsche Post sold its loss-making Dutch mail business, Selektmail, to Sandd and closed down its activities in the unaddressed mail business (via its subsidiary Interlanden). Later in 2011, PostNL also decided to shut down the low-budget

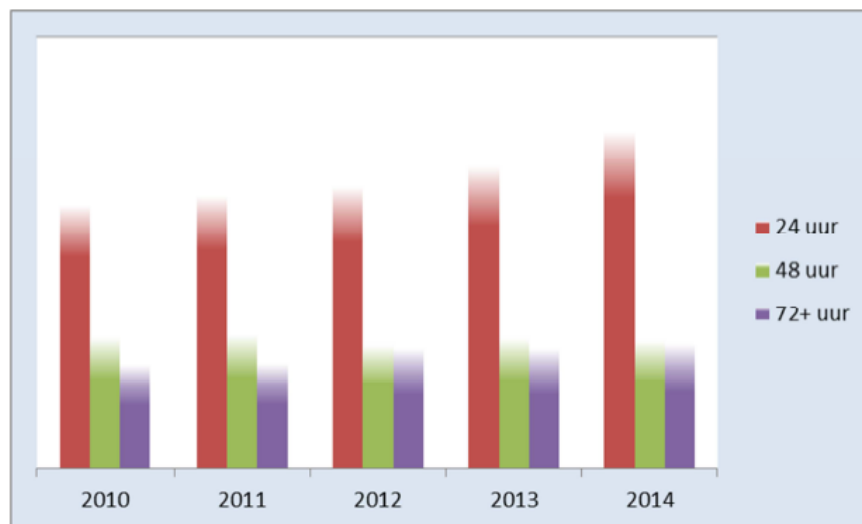
⁴⁰ Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service (OJ L 15/14, 21.2.1998) amended by Directive 2002/39/EC of the European Parliament and of the Council of 10 June 2002 amending Directive 97/67/EC with regard to further opening to competition of Community postal services (OJ L 176/21, 5.7.2002) and by Directive 2008/6/EC of the European Parliament and of the Council of 20 February 2008 amending Directive 97/67/EC with regard to the full accomplishment of the internal market of Community postal services (OJ L 52/3, 27.2.2008).

⁴¹ See WIK-Consult (2011), Developments in the Dutch Postal Market, p. 26 sub., see also OPTA (2012), De Nederlandse postmarkt in 2011.

addressed mail delivery activities of its subsidiary Network VSP and to refocus this network on the unaddressed mail distribution (where Network VSP improved its market position after the exit of Interlanden). Network VSP's exit from the addressed mail market additionally increased Sandd's market share.

The consolidation process in the Dutch mail market has thus created a quasi-duopoly in the market segment for non-time-critical delivery. With Sandd and PostNL, there are today two well-established players with nationwide delivery networks in the Dutch letter market. Since 2011 PostNL delivers non-time-critical items on three days per week (Tuesdays, Thursdays and Saturdays)⁴² while Sandd delivers on two days per week (Tuesdays and Fridays). In 2014, PostNL's market share was between 70 and 80% (in revenues) in this segment.⁴³

Figure 7 Development of average revenues for domestic time-critical and non-time-critical business letters



Source: ACM (2016), Marktanalysebesluit 24-uurs zakelijke post, Ontwerpbesluit, openbare versie, Figuur 3, p. 38; see also Table 2, p. 46.

Despite market consolidation, price competition was and appears to be intense in non-time-critical delivery. Average revenues of the “48 uur” and the “72+ uur” letter service

⁴² In 2011 PostNL introduced its “peak / off-peak” tariff model to become more competitive in the segment of non-time-critical delivery. In this model, time-critical letters are delivered on six, since 2014 on five days per week while non-time-critical letters are delivered on three days per week. See TNT Post, Tariffs January 2011 Business products and services.

⁴³ See ACM (2016), Marktanalysebesluit 24-uurs zakelijke post, Ontwerpbesluit, openbare versie.

have apparently converged which indicates that both services are interchangeable to some extent.⁴⁴

Time-critical delivery

The situation is very different in the market segment for time-critical letters. Despite of substantially declining volume, particularly in time-critical letters, competition has been emerging more dynamically since around three years. PostNL is by far the largest provider for next-day delivery services with a market share of more than 90%. Competition is highly fragmented: Around 90 local postal companies are active in the Dutch postal market. Most of them are very small. Only 16 local competitors achieve revenues of at least one million Euros. Only Van Straaten Post, Intrapost, Skynet (owner of Falkcourier, a specialist for delivery of time-critical juridical documents) and the members of the “Coöperatieve Zakelijke Post Nederland” under the brand Businesspost gained more than five million Euros. Their revenues are by far lower than those of Sandd (between 100 and 200 million Euros) and PostNL (in total between 900 and 1,000 million Euros). Most local postal companies are active in semi-urban and rural areas and not in the high-density areas in Zuid- and Noord-Holland.⁴⁵

So far, there is no competitor with a nationwide network for time-critical letter delivery services. Even though local competitors cooperate with each other in final delivery they are still not able to provide nationwide delivery services for time-critical letters without access to PostNL’s network. Local competitors target mainly small and increasingly medium-sized business mailers. There is factually no competition for consumer letters which would require a dense collection network (sales points for stamps, postal outlets and street letter boxes).⁴⁶

Regional and local delivery companies mainly compete in the “high-price” time-critical segment. They provide daily delivery services from Tuesday to Saturday (like PostNL). Competition in the “48uur” service which would be operationally possible (and much easier to organise than next day delivery) is minimal. It appears that this group cannot compete with the low price level in this segment.

Table 3 summarises the level of competition in time-critical and non-time-critical delivery in the Dutch letter market and PostNL’s market share (in revenues) in each of the segments.

⁴⁴ However, only PostNL is able to provide the 48 uur service for the three “peak” delivery days. Sandd can provide the 48 uur service only for one delivery day per week (Friday).

⁴⁵ See ACM (2016), Marktanalysebesluit 24-uurs zakelijke post, Ontwerpbesluit, openbare versie, p. 59 sseq.

⁴⁶ There is only one postal operator POST.FRL post that offers a non-time-critical postal service for consumers in the province of Friesland. They do not have a very dense collection network. See <http://www.post.frl/postpunten-op-kaart/>.

Table 3 Level of competition and PostNL's market share per segment (2014)

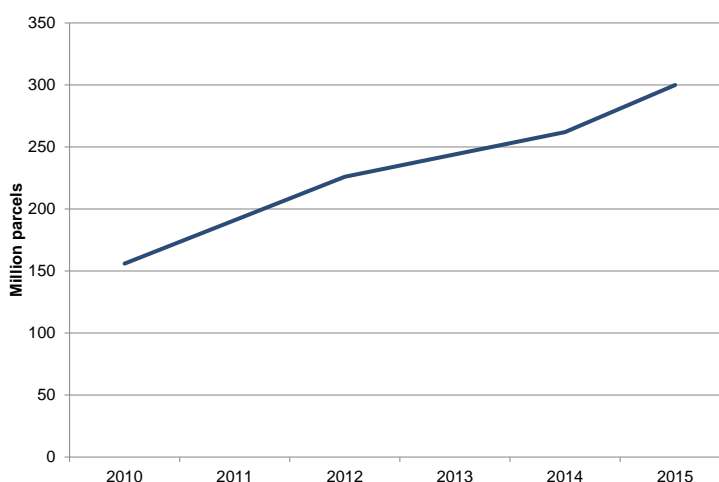
Level of competition	Time-critical letters	Non time-critical letters	PostNL's market share
Consumer letters	None		100%
Small business mailers	Emerging	Emerging	80-90%
Medium-sized business mailers	Emerging	Stagnating	70-80%
Large business mailers	None	Stagnating	80-90%
PostNL's market share	>90%	70-80%	80-90%

Source: Based on ACM (2016), Marktanalysebesluit 24-uurs zakelijke post, Ontwerpbesluit, openbare versie and WIK assessment.

2.2 Parcel services

In contrast to domestic letter services, parcel & express services have increased substantially in the last years. The major driver for parcel growth, domestically and internationally, is e-commerce.⁴⁷ Dutch consumers increasingly buy goods in online shops in and outside the Netherlands and drive the growth in parcels, domestically and internationally.

Figure 8 Development of domestic and international parcels in the Netherlands



Source: Based on ACM (2016), Marktscan Pakketten and Opta (2010), De Nederlandse Postmarkt in 2010 and information provided by ACM.

⁴⁷ A more detailed discussion of the impact of digitisation on the different segments (demand-view) is provided in Section 3.3 of this report.

The total volume of parcels (domestic and international) is still substantially lower than domestic letter post volume. In 2015 nearly 300 million parcels have been collected and/or delivered in the Dutch parcel market, two thirds were domestic parcels. Between 2010 and 2015, the total number of parcels increased by more than 10% p.a. on average. Since 2012, domestic parcels have increased by more than 7% p.a. on average. Revenues increased less so that average revenues per parcel declined overtime. Consumer parcels account for around 2% on total parcel volume.⁴⁸

These figures do not include the delivery of goods by letter service (oversized letters “special” or letterbox packets). Letterbox packets are small-sized packets that fit through the aperture of recipient’s letter boxes and are therefore easy to deliver jointly with letters. Market experts expect a growing number of these letterbox packets because they represent a low-cost alternative for the delivery of small sized goods, e.g. books, CDs, small electronic articles and gadgets of low value. There are estimations that around 70 million of these items have been delivered in 2014.⁴⁹

The major driver of this impressive growth in parcel volume is the dynamically growing e-commerce. In the Netherlands, e-commerce volume increased by 16.1% to 16.1 billion Euro from 2014 to 2015.⁵⁰ Mobile e-commerce (by smartphones and tablets) accounts for nearly 15% of total online sales. In total, 12.9 million internet users shop online. This means that three-quarter of Dutch people already buy merchandise and services via the internet (2016). The current growth in e-commerce is triggered by more online purchases per online shopper and not so much by attracting new groups of buyers. Most popular product groups are clothing, telecom and IT equipment. The travel segment is the most popular service group, followed by insurances and event tickets. These service groups partly depend on secure and reliable delivery services send by mail.

The Dutch e-commerce market has three major Dutch players: bol.com (by far the biggest), wehkamp.nl and coolblue.nl. About 35.000 smaller e-retailers (including “garage shops”/private persons) offer their products and services. Amazon is currently not active in the Dutch e-commerce market but an entry within the next years is likely along with substantial changes in market structure and strategies of major players.⁵¹ Although the company faces high entry-barriers as the Dutch e-commerce market is well developed and already features a high delivery quality, it appears likely that the

⁴⁸ See ACM (2016), Marktscan Pakketten, p. 21.

⁴⁹ See VVP (2015), VVP Marktverkenning 2015, p. 2. According to PostNL estimations only a small proportion of letterbox packets are sent by e-retailers to date. PostNL explained that around half of these 70 million items actually contained goods and less than 10 million items were sent by e-retailers using the new service “Brievenbuspakje Extra” introduced in 2014 (see PostNL (2016), Response PostNL to additional WIK questions, 19 August 2016).

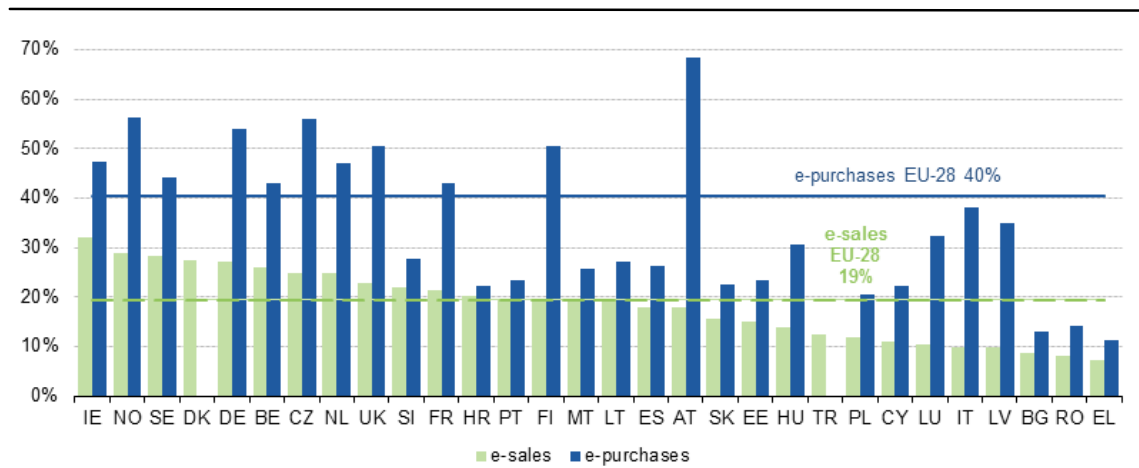
⁵⁰ For the following section see E-Commerce Europe (2016): The Netherlands B2C E-commerce Report 2016. Among others, the report is based on statistics provided by Thuiswinkel, GfK and PostNL.

⁵¹ For example, Amazon has already started with the roll-out of pick-up points/ parcel lockers (in cooperation with DPD).

entry may change the market as Amazon would probably be determined to undercut prices significantly.

In the B2B segment the Netherlands are also positioned above EU average e-sales and e-purchases but the overall low volume indicates that this segment has still a significant potential for growth (see Figure 9).

Figure 9 E-sales or e-purchases of businesses in the EU (% of businesses)



Source: European Commission 2015 (Community survey on ICT usage and e-commerce in enterprises)

In the Netherlands, consumers are considered to be price-sensitive but tend to favour products of good quality.⁵² Dutch online shoppers value home delivery (~80% of all deliveries) as well as free delivery and free return options. Pick-up points are less important for delivery but around 80% of returns are collected via pick up points. Nearly 18% of all orders are sent back.⁵³ The Netherlands are 2nd in Logistics Performance Index (EU-28) and customers and receivers of parcels are used to choices based on price and quality comparisons. The average total cost for shipping are 5.28 Euro, according to a survey by Thuiswinkel.⁵⁴

According to our research and interviews, online shoppers expect to have

- Fast and reliable delivery (next day almost expected as a standard)
- Free delivery
- Time slot for delivery (predictable delivery)

An increasing demand for same-day delivery (at least for some goods, e.g. clothes) can be perceived. Same-day delivery is still more expensive than next-day delivery. Except

⁵² See E-Commerce Europe (2016): The Netherlands B2C E-commerce Report 2016, p. 29.

⁵³ See Thuiswinkel (2015): E-commerce benchmark 2015.

⁵⁴ Ibid.

for some products, same-day delivery is not expected to become standard in the medium term.

To date, delivery by letter post (“letterbox packet”) plays a minor role for Dutch e-retailers because the service does not meet the requirements of e-retailers in terms of visibility and flexibility,⁵⁵ for example there is a high demand for quality which could not necessarily be met by the highly standardised letter products (e.g. real-time tracking, evening delivery and 7-days-a-week delivery).

E-retailers rather expect lower parcel delivery prices for the future delivery via the parcel network to remain their first choice because of tracking options and choice of different delivery options. Cross-border delivery from Asia (China) may rely more on letter post because of low terminal dues.⁵⁶

In future, a more fragmented delivery service landscape (“service matters not operator”) can be foreseen with even more demanding requirements on quality and personalized delivery (“sender in control”). Delivery of goods that are either urgently needed or bulkier in format like most parcels will be more affected by this development than small-sized and lightweight goods which can be easily delivered in the letter box. However, visibility and delivery the next working following the order are basic standards required by Dutch online shoppers that should be met by each type of delivery service.

There are indications that PostNL is upgrading the service characteristics of letterbox packets by improving the visibility of the service. PostNL will introduce track & trace for letterbox packets per January 2017 (instead of “tracking information on shipment”). Moreover, since January 2016 PostNL offers only time-critical delivery of letterbox packets i.e. the items are delivered on five days per week.⁵⁷ These improvements combined with high convenience for Dutch online buyers (home delivery in the letterbox) may promote the demand of this low cost delivery solution for small-sized goods in the next future.

Driven by the strong growth in e-commerce and the trend of a more “recipient-centric” approach in delivery, parcel & express operators including local couriers have been highly innovative in developing new and more flexible delivery solutions. Customers have today more choice among different parcel services in terms of delivery day, delivery speed and delivery location. Tracking & tracing of parcels has become a general standard.

The Dutch parcel & express market is more competitive than the Dutch letter market. There are at least six parcel & express operators with nationwide delivery networks for

⁵⁵ Interview Thuiswinkel, 28. July 2016.

⁵⁶ See Dieke, Niederprüm, Thiele (2016), UPU-Terminal Dues and International E-commerce, WIK Discussion paper No. 412.

⁵⁷ See PostNL, Postal rates per 1 January 2016 and per 1 January 2017.

parcels in the Netherlands, including PostNL, DHL, DPD, GLS, TNT Express/FedEx, UPS/Kiala. Additional to these operators there is a large number of local couriers, e.g. Cycloon and Verstraaten Express.⁵⁸

PostNL has a market share of around 60% in domestic parcel services (in revenue and in volume) followed by DHL Parcel with a market share of approximately 30%. DPD and GLS are still relatively small players with market shares around 5%.⁵⁹ For e-commerce the delivery of parcels to consumers (B2C) is most relevant. In this sub-segment PostNL is the market leader followed by DHL Parcel.⁶⁰ Average revenues in parcel delivery declined between 2012 and 2015 partly driven by lower average costs (scale economies), by competition and demand power of large online sellers.

The growing emphasis on e-commerce driven delivery to consumers is reflected in the set-up of nationwide retail networks for parcel collection and, partly, delivery. ACM reports that in the Netherlands there are in total 6,300 service points for parcel services. More than 45% (2,900) are managed by PostNL, followed by DHL Parcel (1,350), DPD (750), GLS (600) and UPS/Kiala (700).⁶¹

2.3 Provision of universal postal services

USO items comprise domestic stamped and franked letters and international mail up to 2 kilogram, domestic single-piece (up to 10kg) and international parcels (up to 20kg). USO letters have to be delivered on five days per week (since 2014) and are subject to quality of service requirements. Mourning cards and medical post have to be delivered on six days per week. From January to November, at least 95% of these items have to be delivered the next working day.⁶² USO letters form a substantial share of the time-critical letters.

In 2009 the Ministry of Economics ordered PostNL to provide the universal postal services in the Netherlands.⁶³ This includes the operation of a nationwide dense collection network (post offices and street letter boxes) and the delivery of stamped and franked single-piece items the next working day on five days per week. On average, 95 per cent of these letters have to be delivered the next working on average.

⁵⁸ See ACM (2016), Marktscan Pakketten, p. 19.

⁵⁹ Domestic parcel services do not include volumes and revenues of express operators like UPS and TNT Express who both deliver parcels in the Netherlands.

⁶⁰ See ACM (2016), Marktscan Pakketten, p. 22.

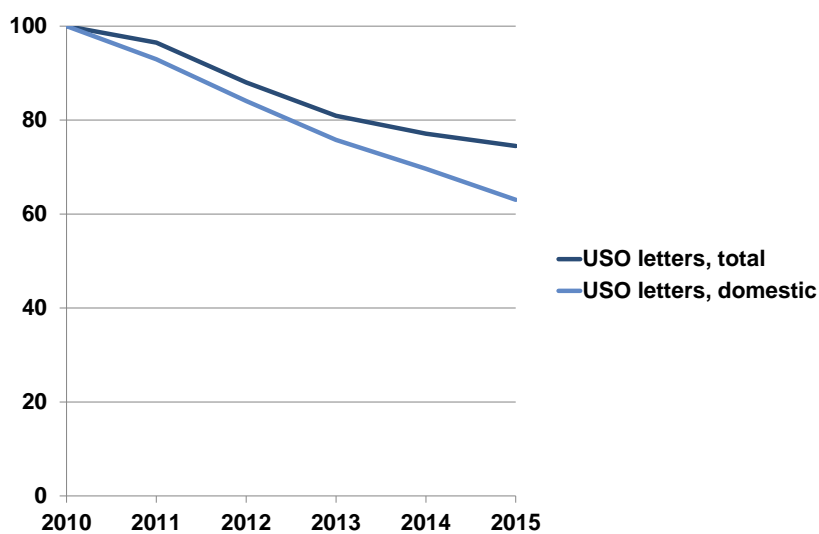
⁶¹ Ibid., p. 26.

⁶² This requirement is not applied for December post (mainly Christmas and New Year cards). In this period senders can use the cheaper “decemberzegel”. The price for the “decemberzegel” is subject to approval by ACM. In 2016 the “decemberzegel” costs 65 cents (compared to 73 cents for a regular letter), see ACM, Verhoging tarief decemberzegel past binnen wettelijke grenzen, Besluit 12 September 2016.

⁶³ See Regeling van de Staatssecretaris van Economische Zaken van 15 april 2009, nr. WJZ/9067599, tot aanwijzing van Koninklijke TNT Post BV als verlener van de universele postdienst (Aanwijzing verlener universele postdienst 2009).

Since 2014, collection and delivery have been reduced to 5 times per week (Tuesday to Saturday). USO postal services are exempt from VAT. Dutch postal legislation does not foresee any external funding of the USO but expects that the USO is fully funded by USO revenues. For this reason universal service tariffs are subject to a pricing rule that shall ensure that the costs of USO services are fully covered by USO revenues (including a reasonable rate of return) which was firstly applied in 2015. Domestic and international (inbound) USO postal services are part of time-critical delivery services because they require delivery on five working days per week.

Figure 10 Development of USO volume between 2010 and 2015



Source: Based on PostNL (2016), Response PostNL to WIK questions, 19 August 2016.

Note: USO letters, total include domestic, international inbound and international outbound letters.

Between 2010 and 2015 domestic USO letters declined by nearly 9% per annum (similar rate as consumer letters). Since 2010, the share of domestic USO letters in total USO volume has declined from more than 60% to around 50%. Domestic USO letters consists of consumer letters (around 220 million in 2015) and franked letters mainly sent by small businesses (ca. 200 million items).⁶⁴ International import and export letters and USO parcels account for the other half of total USO volume. Particularly, export letters have grown while import letters declined (but at a lower rate than domestic USO letters). In 2015, the share of inbound international in total USO letter volume delivered by PostNL was approximately 20%, up from 16% in 2010. By contrast,

⁶⁴ WIK estimation based on non-confidential data provided by ACM and PostNL.

the share of inbound in PostNL's total delivered volumes was approximately 4% in 2015, up from 3% in 2010.⁶⁵

In contrast to letters, the number of domestic and international USO parcels has grown from 11 to 15 million.⁶⁶ USO parcels therefore account for around 5% of total parcel volume.

As outlined in Section 2.1.2 there is currently close to no competition in consumer post and very little competition in the segment of small business senders that partly use USO letter services and partly non-USO bulk mail services either offered by PostNL or by local and regional competitors. Serving consumers and very small business mailers requires a dense collection network. As designated universal service provider PostNL operates a dense network of postal outlets and street letter boxes to meet the universal service requirements. This network allows consumers and other small senders to feed in their letters into PostNL's postal network. None of PostNL's competitors in the Dutch letter market have established a comparable collection network, neither on national nor on local level. Local postal companies usually pick up letters at the premises of the mailer or the mailer transports the letters to the office of the local postal company. Competitors' daily letter volume is usually too low to make it economically viable to operate dense retail networks for collecting letters. In contrast, business mailers have different options to consign letters depending on volume/value per consignment: at postal outlets, at specific outlets for business mailers (sometimes located at the sorting facility), at postal outlets that also offer printing facilities or their letters are collected at their premises by postal operators.

PostNL's dense collection network is partly borne by its universal service obligation. Without the USO, it is conceivable that PostNL would operate a smaller network of street letter boxes and postal outlets. The costs of the "excess" services ("Overservice") are fixed costs and fully allocated to the universal services.⁶⁷ To reduce USO costs the Ministry decided in late 2015 to relax the requirements on the collection network. The changed requirements allow PostNL to reduce the number of postal outlets from around 2,000 to 1,000 and the minimum number of street letter boxes from around 19,000 to less than 10,000.⁶⁸

USO tariffs are subject to price regulation. The headroom for tariff increases is determined by a price formula that takes into account, among others, the decline in USO volume and changes in the cost structure (proportion of fixed costs on total costs).

⁶⁵ WIK estimation based on PostNL (2016), Response PostNL to WIK questions, 19 August 2016 and PostNL, Annual Reports.

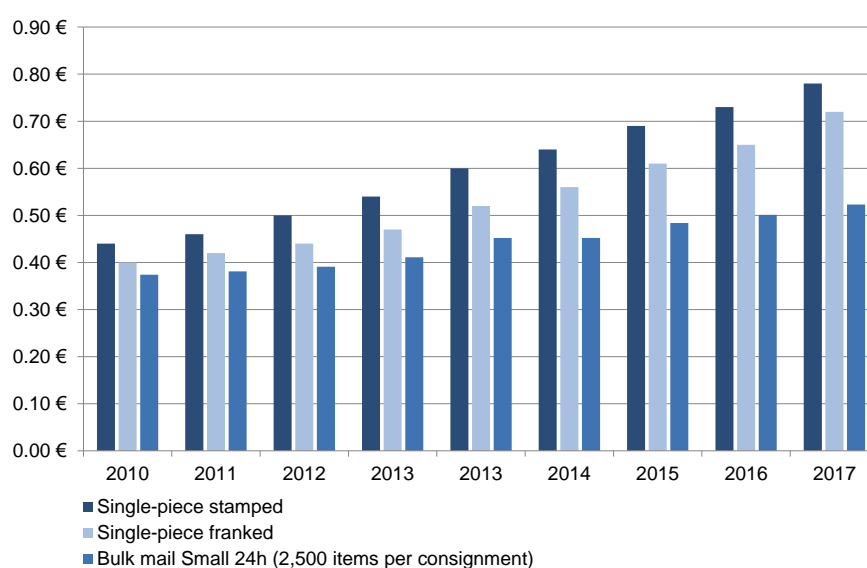
⁶⁶ See PostNL (2016), Response PostNL to WIK questions, 19 August 2016.

⁶⁷ See PostNL (2016), Financiële Verantwoording universele postdienst 2015, p. 9.

⁶⁸ See Besluit van 29 oktober 2015 tot wijziging van het Postbesluit 2009 in verband met de modernisering en flexibilisering van de universele postdienstverlening in combination with Wet van 4 juni 2015 tot wijziging van de Postwet 2009 tot modernisering en flexibilisering van de universele postdienstverlening (modernisering UPD).

The formula was defined by Ministry regulation.⁶⁹ ACM implemented the price formula in 2015 and defined the first headroom for the 2016 USO tariffs.⁷⁰ The cost base refers to the financial year 2014 i.e. after the reduction of the number of weekly delivery days from six to five. This cost base is inflated annually by the consumer price index, changes in letter volume decline and fixed costs. In 2016, PostNL has not fully used the approved headroom for tariff increases. The remaining headroom has been transferred to the next period. For 2017 PostNL is allowed to increase USO tariffs up to 8% on average.⁷¹

Figure 11 Price developments of a domestic 20g letter (PostNL list prices)



Source: Based on PostNL price lists 2010-2017.

Note: In 2013 PostNL increased the postal tariffs in January 2013 and August 2013.
Bulk mail Small 24h: In 2010 and 2011 the volume threshold was 2,000 items per order.

Figure 11 illustrates the development of public tariffs for 20g letters delivered the next working day of two USO products (stamped and franked letters) and a comparable bulk mail product (“Small”, 20 grams, 2,500 items per order). The most visible development is that the gap between single-piece and bulk mail tariffs for small 20g letters has been grown (from 7 Eurocents to nearly 26 Eurocents, respectively from 15% to 33% of the stamp price between 2010 and 2017).

Tariff increases are mainly driven by ongoing volume decline. Volume decline means that average cost per item increases given that a substantial share of total cost is fixed.

⁶⁹ See Postregeling 2009, Bijlage 3.

⁷⁰ See ACM, Besluit kostentoerekening PostNL en tariefreimte 2016, 28 September 2015.

⁷¹ See ACM (2016), Brief aan PostNL over Vaststelling tariefreimte Universele Postdienst 2017, 20 September 2016.

A second driver is the total cost allocated to USO services which depend on the structure of time-critical letters. Time-critical letter services need five day delivery per week. This delivery network is used for both, time-critical USO and time-critical non-USO (bulk) letters. The fixed costs of the five-day delivery network are therefore allocated to both services, USO and non-USO services depending on demand. PostNL reported that the share of non-USO business letters on total time-critical letters declined in 2015. Consequently, USO services had to cover a higher share of the fixed costs of the five-day delivery network.⁷²

⁷² See PostNL (2016), Financiële Verantwoording universele postdienst 2015, p. 8.

3 Future sustainability of postal networks

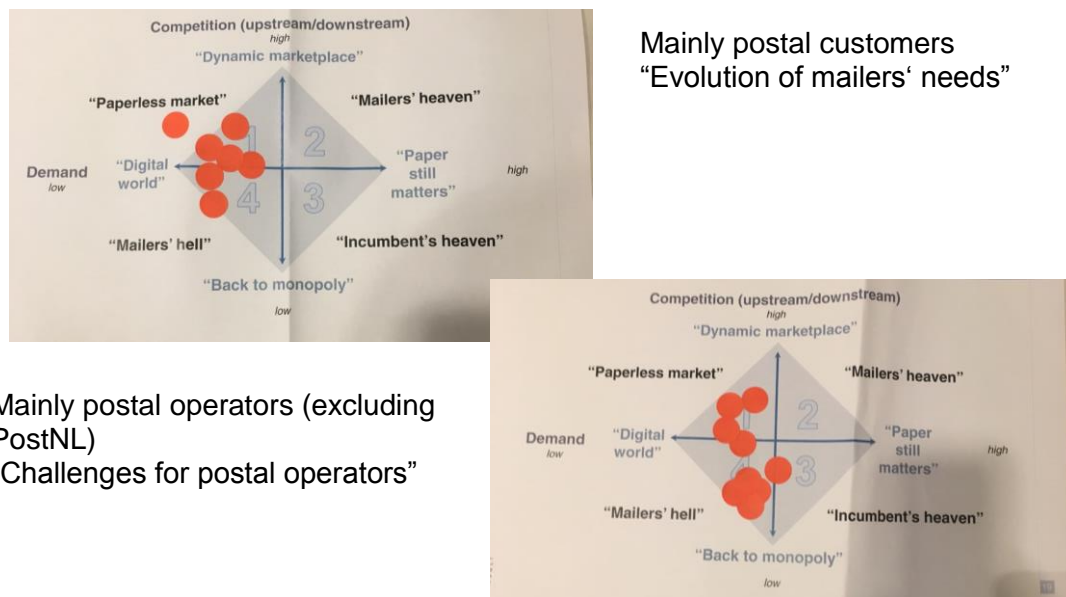
3.1 Introduction

The future economic sustainability of postal networks depends on two major drivers: demand (and future needs of Dutch mailers and recipients) and competition.

When discussing sustainability, this report puts the emphasis on economic sustainability of postal networks. It does neither discuss environmental nor social sustainability in the provision of postal services which also play an important role in the political discussion. The provision of postal services is characterised by economies of scale and scope particularly in collection and delivery. This implies that declining letter volume drives average costs which may result either in price increases of postal services and/or declining profitability (or increasing losses) of postal operators in a static environment. In a dynamic environment, however, postal companies have the opportunity to save cost and/or develop new, innovative services that attract more volume and revenues which may facilitate the economically viable provision of delivery services in future.

Regarding future demand trends the common view of interviewees and stakeholders is that the decline in letter volume will continue in the next 10 years mainly driven by the “megatrend” digitisation. This development is considered to be irreversible but it does not affect each mail segment to the same extent. Additionally, there are also positive effects of digitisation particularly on the delivery of items ordered online. The expected impact of digitisation on demand is discussed in Section 3.2.

Figure 12 Expectations of participants in the stakeholder workshop



Source: Stakeholder workshop, 15 September 2015

The future of competition in the Dutch postal market is considered highly uncertain in light of volume decline. In Section 3.3 we discuss the strengths, weaknesses, opportunities and threats of the key players in the Dutch letter market and analyse what would happen if the current regulatory framework remains unchanged. This analysis prepares the ground for developing the scenarios in Section 3.4.

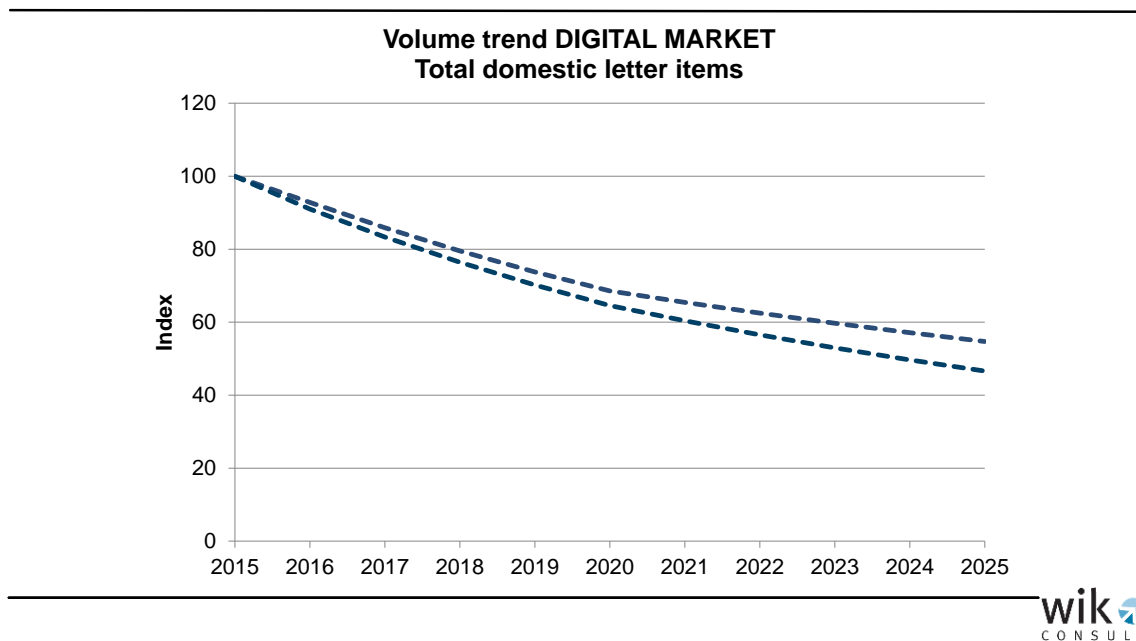
In our analysis, we consider the future developments in demand and competition separately. Actually, developments in demand and competition are interrelated but as outlined in the previous paragraph, digitisation as "megatrend" will progress and negatively impact letter volume independently from competition. However, competition helps promoting innovation in delivery, drives efficiency in postal operations and ensures that (average) prices develop in line with average costs. While competition is, in our view, not able to stop digitisation of physical communication it is able to postpone the process and to promote the competitiveness of letter services compared to its digital counterparts (e.g. in the advertising business).

In Section 3.4 we analyse the impact of the market developments on the sustainability of the universal postal services under the assumption that the universal service requirements would be unchanged and that PostNL would be the designated universal service provider.

3.2 Future demand for letter services

Overall, we estimate that in the “Digital World” the domestic letter volume will decline by around 30-35% until 2020 and by 45-55% in total until 2025 compared to 2015.

Figure 13 Volume trend 2015-2025: Total domestic letter items



Source: WIK estimation.

The demand segments are differently affected by digitisation but stakeholders agreed that paper-based communication (social mail and business communication) and advertising as well as the delivery of paper-based magazines and periodicals will continue declining at significant rates in the next 10 years.⁷³ The stakeholders also expect that the decline rates will fall over time so that total volume decline will slow down during the next 10 years.

From the demand side we see a declining need for time-critical delivery in all letter segments. Reliable and, increasingly, day-definite delivery becomes more important in the view of business mailers. It is expected that there will be still a need for time-critical delivery for specific purposes and, more importantly, for delivery of items ordered online (and sent by letter or letterbox packet).

Moreover, the speed of substitution of time-critical by non-time-critical letters depends not only on the trends in digitisation but also on the supply of and access to non-time-critical services as well as price developments. These developments also depend on future competition trends.

⁷³ See Section 2.1.1 for a discussion of the impact of digitisation on the demand for letter services.

3.3 SWOT analysis of key players in the Dutch letter market

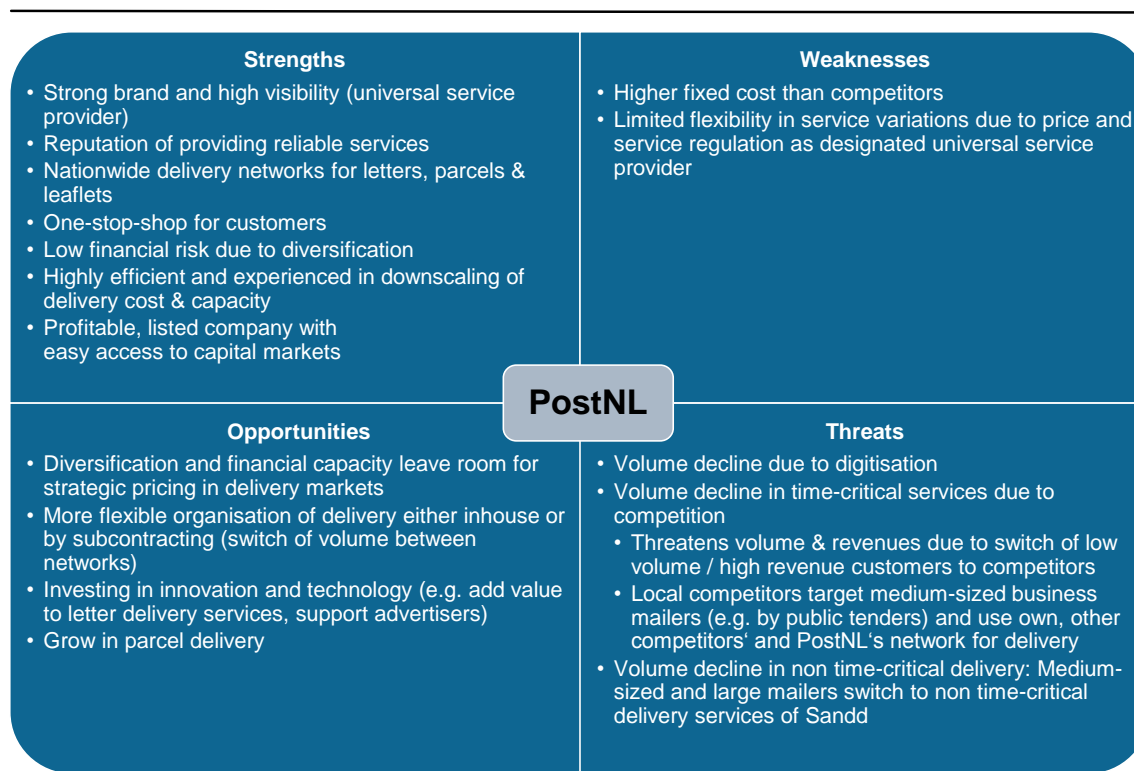
While the demand trends appear relatively clear it is still uncertain how competition will develop. Future competition prospects mainly depend on three factors: (1) the impact of letter volume decline on the existing business models, (2) the market position of postal companies and their behaviour, and (3) their operational flexibility and innovative power to deal with expected challenges. In this section we discuss the strengths, weaknesses, opportunities and threats of PostNL, Sandd and the more heterogeneous group of local and regional competitors in the Dutch letter market and how the current regulatory framework would affect competition in the shrinking letter market.

3.3.1 PostNL

PostNL is the only postal company in the Netherlands that provides nationwide delivery services in all market segments: in time- and non-time-critical delivery of letters, in door-to-door distribution of leaflets (via its subsidiary Spotta, formerly Netwerk VSP)⁷⁴, in the delivery of parcels and, in the provision of international postal services. Historically, the company had benefitted from a legal monopoly for the delivery of letter services. It has been responsible for the provision of universal postal services since decades and remained the designated universal service provider after full market opening in 2009. For this reason PostNL benefits from a strong brand and high visibility (ubiquity of PostNL's services) linked with a high reputation in providing reliable postal services. As designated universal service provider PostNL is subject to USO requirements that may limit PostNL's flexibility in varying its service provision.

⁷⁴ See <http://zakelijk.spotta.nl/over-ons/overspotta>.

Figure 14 SWOT analysis for PostNL

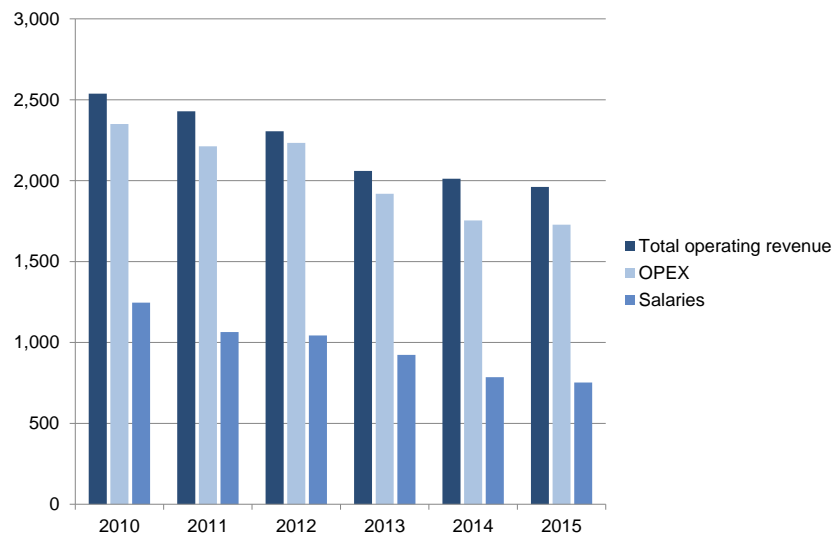


Source: WIK assessment

PostNL is a fully privatised company listed at the stock exchange in Amsterdam. As listed company, PostNL has easier access to capital markets to finance investments than its smaller competitors in the Dutch letter market. In an international perspective, PostNL is a regional player with a high dependence on the Dutch market. Nearly three quarters of total revenues are achieved in the business segments “Mail in NL” and “Parcels”.⁷⁵ Nearly 100% of PostNL’s operating income came from these segments while PostNL’s international activities have not been very profitable since years.

⁷⁵ See PostNL, Annual Report 2015. Revenues from parcel services offered in Belgium included.

Figure 15 PostNL “Mail in NL”: Developments of revenues and costs



Source: Based on PostNL, Annual Reports 2010-2015, Segment reporting

Between 2010 and 2015 the group was not making any losses.⁷⁶ The business segments “Mail in NL” and “Parcels” are both very profitable with EBIT margins well above 10% in 2015.⁷⁷

Over a period of more than one decade, PostNL has managed to reorganise its mail operations to increase flexibility in reacting on changes in the market conditions. This is also reflected in the financial data for PostNL’s business segment “Mail in NL”. Between 2010 and 2015 PostNL’s letter volume has declined by 10% per annum, and total operating revenues by 6% which indicates that price increases partially limited revenue decline. During the same period PostNL has reduced the number of employees (in full-time equivalents) by nearly 8% and labour cost by more than 9% per year.⁷⁸ This development shows that PostNL has successfully managed keeping the mail business profitable despite of a substantial decline in letter volume by a mix of price increases and cost savings. Moreover, the change from full-time postmen to more flexible part-time deliverers combined with the implementation of low- and high-volume delivery days indicate PostNL’s ability to make their operations more flexible to better adapt delivery capacities with varying, overall, declining letter volume.

As multi-product company PostNL benefits from synergies (i.e. economies of scale and scope) and is able to diversify its risks. PostNL has successfully benefited from the past growth in e-commerce driven delivery in its mail and parcel business and is able to offer

⁷⁶ See PostNL (formerly TNT), Annual Reports 2010-2015.

⁷⁷ See PostNL, Annual Report 2015, p. 98. The EBIT (Earnings Before Interest and Tax or Operating Income) margin refers to total operating revenue (including intercompany sales).

⁷⁸ Based on PostNL, Annual Reports 2010-2015, Segment information.

a broader product portfolio to its customers than any of its competitors (one-stop-shop) in the letter and the parcel market.

More than one decade ago, PostNL decided to strictly separate letter and parcel operations. This is mostly visible in sortation and delivery. PostNL operates 18 parcel facilities with a combined function for sorting and delivery preparation (starting point for parcel deliverers). Letters are sorted and prepared for final delivery in six letter sorting centres and around 100 delivery offices.⁷⁹ Only in very rural areas letters and parcels are delivered jointly, when delivery is organised by car because of long distances between stops. While letter delivery is mainly organised with part-time deliverers substantial parts of parcel delivery are sub-contracted either to companies or to self-employed drivers. The separation of the delivery networks has the advantage that PostNL has been more flexible to introduce innovative delivery solutions in parcel delivery and to better meet changing customers' and particularly recipients' needs regarding convenient ways of delivery (e.g. delivery of parcels on six days per week, optional delivery on Sundays, and evening delivery).

Separated delivery networks for letters and parcels do not necessarily mean that the parcel network only delivers parcels and the letter network only letters. For example, registered letters are processed and delivered in PostNL's parcel network. These letters have similar service characteristics like parcels. They are fully tracked and need a signature on delivery (like registered parcels). This is also reflected in the single-piece price for a registered letter that is higher than for a parcel (8.15 Euros compared to 6.95 Euros).

In contrast, letterbox packets are processed and delivered in the letter network. Although being a highly standardized product in terms of format (not thicker than 32mm) this service has the potential to become more and more attractive for small and medium-sized online sellers. Major reasons for improving attractiveness are the relatively low price compared to parcel products, speed (delivery within one working day which is the preferred delivery option of Dutch online buyers) and high convenience in delivery. As the items fit into the letter box it is not necessary for online buyers to be at home or to pick these items up in the next postal outlet. PostNL has been promoting this product by improving the tracking of letterbox parcels to improve visibility for online sellers and buyers. From the viewpoint of PostNL, average delivery costs are relatively low because these items are delivered together with other letter items in the letter box. PostNL reported that they delivered around 70 million large letters and letterbox packets in 2015. According to PostNL, only a small proportion of these items are sent by e-retailers, so far.⁸⁰ WIK expects that the upgrade of the service will promote online sellers' demand for this low-cost alternative to parcel services.

⁷⁹ WIK-Consult (2016), Review of the Projected Costs within Royal Mail's Business Plan, Section 3.2.

⁸⁰ See PostNL (2016), Response PostNL to WIK questions, 19 August 2016.

Declining letter volume due to digitisation and the growing number of letterbox packets and parcels due to e-commerce lead to the question whether it is economically reasonable to partly or even fully merge the delivery of letters and parcels in one network. Compared to its competitors PostNL would be well positioned for such a strategy if this is economically reasonable.

Table 4 Illustrative example: PostNL's average handling costs for letters and parcels in 2015 and 2025

Year	2015		2025 (estimated)			
			% fixed costs: 100%		% fixed costs: 50%	
	Letters	Parcels / registered letters	Letters	Parcels / registered letters	Letters	Parcels / registered letters
Volume (million)	2,401	166	1,200	400	1,200	400
Operating expenditure (million EUR)	1,728	816	1,728	816	1,296	1,046
Average operating expenditure per item (EUR)	0.72	4.92	1.44	2.04	1.08	2.62

Source: WIK estimation based on PostNL, Annual Report 2015 (Segment reporting on "Mail in NL" (Letters) and "Parcels").

Notes: Operating expenditures include non-operational items.
Simplifying assumptions for the calculation:
Operating expenditures in 2015 input prices (no change in input prices).
Stable volume structure.

Table 4 provides an illustrative example on the development of PostNL's average handling costs depending on volume. It shows the development of (highly aggregated) average handling costs of letters and parcels as of today compared to estimated volume levels in 2025 given total cost are either fully fixed (100% fixed costs) or half fixed (50%).⁸¹ In 2015, PostNL reported that it delivered in total 2.4 billion items in its letter network and 156 million parcels (including the Belgian parcel business)⁸² plus an estimated number of around 10 million registered letters⁸³ in its parcel network. Based on PostNL's published segment reporting ("Mail in NL" and "Parcels") the average total operating costs of handling one letter were 0.72 EUR in 2015 compared to the average operating costs per parcel of 4.92 EUR. Assuming that in 2025 PostNL only delivers half of letter volume and more than double of parcels and registered items the average handling costs of letters would still be lower than those of parcels independently whether we assume that operating costs are completely fixed (100%) or fifty-fifty fixed

⁸¹ Actually, the share of 50% on total cost is more realistic than 100% (see WIK-Consult (2013), Main Developments in the Postal Sector (2010-2013), p. 194 sseq.). This example shall illustrates the maximum span of average costs.

⁸² See PostNL, Annual report 2015.

⁸³ See the.idea (2015), (2C) Pakketten in Nederland.

(50%). This simple calculation indicates that full convergence of PostNL's letter and parcel delivery is not a likely outcome in light of estimated volume decline.

Reasons for higher handling costs in parcel operations than in letter operations are manifold: Sorting facilities need more space and higher investments in sorting technology. Parcels need more transport capacity. Parcels are usually delivered by van. Rounds are longer and the number of delivered items per round is usually substantially lower than in letter delivery (less economies of scale). Each stop needs more time because parcels usually have to be handed over at the door, they have to be scanned (tracking is a standard service in parcel delivery) and in some cases delivery has to be confirmed by signature (registered letters and parcels). E-commerce mainly drives the number of parcels delivered to consumers which is more costly than delivery to businesses because of the lower "stop factor" (usually one parcel per stop is delivered) and the difficulties to successfully deliver a parcel. Additionally, the organisation of parcel delivery has become more challenging in terms of delivery options, delivery time, frequency and predictability (driven by online sellers' and buyers' needs).

Some convergence of letter and parcel operations could be economically reasonable in some geographical areas or on specific delivery days. In that case the question would remain whether parcels are then delivered by letter deliverers or letters by parcel deliverers. Today's practice in many countries and also in very rural Dutch areas is that parcels are delivered by letter deliverers (if letter delivery is organised by van) and not the other way round.⁸⁴

The illustration in Table 4 shows additionally that PostNL's average costs would increase surprisingly moderately if volume halved within ten years' time. It should be noted that this calculation depends on a number of simplifying assumptions like stable input prices (e.g. wages), stable volume structure (in terms of delivery quality and size of items), and abstracts from technical progress or potential cost savings due to efficiency gains. Moreover, the long-term financial viability of PostNL not only depends on volume and costs but also on the development of revenues (i.e. prices). This development depends on PostNL's pricing strategy which is partly affected by competition and partly by the demand power of single mailers.

⁸⁴ See WIK-Consult (2016), Review of the Projected Costs within Royal Mail's Business Plan, Section 3.2.

3.3.2 Local and regional competitors

There are basically three groups of competitors in the market segment for time-critical delivery of letters.

- Some bigger players including Van Straaten Post, Intrapost and Skynet (Falkcourier). In contrast to Van Straaten Post and Skynet, Intrapost has mainly provided upstream services including collection, franking and sorting of letter items to business mailers as well as to local competitors. Intrapost hands over collected and sorted letters to PostNL as well as to local and regional competitors for final delivery.
- Local delivery organisations affiliated to the label “Businesspost”: These delivery organisations employ handicapped people for organising letter delivery. Handicapped people usually have a lower productivity and their wages are partly subsidized by the state. During the last 3-4 years these organisations have been increasingly becoming more commercial and more professional by cooperating with local courier companies as the example of Cycloon Post & Fietskoeriers illustrates (see below).
- Many very small local and less professional competitors without ambitions to grow in delivery.

Figure 16 SWOT analysis for local competitors



The majority of local competitors target small and medium-sized business mailers within their delivery area. There are some regional competitors (e.g. Van Straaten Post) who increasingly target medium-sized business mailers outside their own delivery area by participating in public tenders. They use, similar to Cycloon, a combination of different postal networks (PostNL, local postal companies and, in case of Van Straaten Post, their own delivery network) to manage the delivery. ACM reports that the share of letters handed over to PostNL for final delivery declined from around half of collected letters to 40% in 2015.⁸⁵

Case study 1 Businesspost: Transformation from social entities to commercially driven postal companies – Example Cycloon Post & Fietskoeriers⁸⁶

Cycloon was founded in 2002 as bike messenger company (which is still an important business of Cycloon). Part of its business used to be the collection from P.O. Boxes in the morning and collection from customers in the evening. In 2012, Cycloon started its cooperation with Business Post by overtaken the delivery operations in Zwolle. Cycloon is a member of the Businesspost network (Coöperatieve Zakelijke Post Nederland U.A.) that was originally the cooperation between “Sociale werkbedrijven” distributed all over the Netherlands. In these “social companies” handicapped people are employed and one important task has been and still is postal delivery. These workers are paid for their activities (e.g. postal delivery) and receive additional income from the state. While in the past Business Post members were exclusively “Sociale werkbedrijven”, today commercial companies, like Cycloon, increasingly overtake parts of the operations by applying a more commercial, professional approach to develop this business while keeping the social aspects of this work in mind.

Cycloon started its expansion to other cities by overtaking further seven of these “social companies” so that Cycloon is now active in 17 cities with around 500 deliverers. Additionally, the company employs around 100 bike messengers and 60 persons in administration and sales. Cycloon delivers letters on five days per week (from Tuesday to Saturday) and offer a service range similar to the one of PostNL. They offer time-critical and some non-time-critical (“48 uurspost”) delivery services. Non-time-critical letters are used to levelling the daily letter volume for its deliverers. Cycloon delivers more than two thirds of the collected letters either itself or via Business Post partners and less than one third via PostNL:

Local and regional competitors are also threatened by the general decline in letter volume. They mainly compete in the segment for time-critical delivery because, similar to PostNL, they offer delivery services on five days per week. They also provide some non-time-critical services but these appear to play a minor role for small business mailers.⁸⁷

Digitisation has substantially reduced the total size of the market but this has not resulted in declining volume for local and regional competitors. In contrast, competitors have grown by offering lower priced letter services at a comparable service quality as PostNL to small and medium-sized business mailers (i.e. delivery at the next working day). There are several potential drivers for the competitors’ growing market share:

⁸⁵ See ACM (2016), Ontwikkelingen en feiten bij de Nederlandse postmarkt in 2015, 21 November 2016.

⁸⁶ Interview Cycloon, 2 August 2016.

⁸⁷ See Section 2.1.1.

- Competitors have successfully improved their delivery services and became more visible and more professional in the acquisition of new customers. They offer better and more individualised service to small business senders compared to PostNL and usually offer collection, franking and delivery services (including of delivered items from P.O. Boxes of PostNL).
- Some competitors have synergies with other services they provide (e.g. courier services like Cycloon, or document exchange services like Skynet);
- PostNL has substantially increased single-piece and bulk mail tariffs for time-critical letter services⁸⁸; additionally in 2012 PostNL stopped offering regional tariffs for non-USO bulk mail products which were much lower than nationwide tariffs⁸⁹;
- Access to PostNL's delivery services has become easier and less costly (based on the strict application of non-discrimination as required by Article 9 of the Postal Act supported by ACM's decision practice).

There is no clear evidence which of these drivers was the most important one but combined, they have promoted competition in this high revenue segment of time-critical delivery during the last three to four years.

Additionally, local and regional competitors have a lower cost base than PostNL. They usually have a lean management and a low cost, regional delivery organisation. Their small size allows them to be more flexible compared to PostNL. Most of them have not invested in sorting machines but sort the letters manually so that the proportion of fixed costs in competitors' operations is lower than in PostNL's operations. Labour cost is the major cost element of these companies. As they deliver considerably less items than PostNL their economies of scale are much smaller. For this reason low or subsidised wages (as for handicapped people) and / or more flexible working arrangements (so-called OVO or zero hour contracts) are crucial for their business. Due to their small size local and regional competitors are still more flexible in the way how to employ people compared to PostNL and Sandd. If they reach the critical size the "80% clause" could become a threat for their business, too (similar to Sandd). Business Post partners do not appear to be challenged because they employ handicapped persons in delivery (as full time employees) with subsidised wages (to compensate for their lower productivity). However, eroding wage subsidies could also challenge their current business model.

Of course, there are opportunities for local and regional competitors to grow in the delivery of goods ordered online like PostNL does. For local retailers this could be an

⁸⁸ See Figure 11 in Section 2.3.

⁸⁹ See TNT Post, Rates January 2011 and PostNL, Postal Rates 2012. In 2011, the lowest average tariff for a 20g letter ("Mixed") cost 0.377 Euros if delivered regionally and 0.493 Euros if delivered nationwide.

attractive alternative to PostNL's services that mainly target e-retailers with higher volume. Local competitors could benefit from synergies in the delivery of small goods and letters at local level as PostNL does at national level. Moreover, the usually higher priced delivery of small goods could positively contribute to local competitors' revenues and margins.

Overall, declining letter volume will challenge local competitors in the next ten years. This will result in a consolidation of the market that is still characterised by market entry⁹⁰. Consolidation means that with declining market volume the probability of market exit increases at local level particularly in those areas where more than one local competitor is active.

The most promising strategy for local and regional competitors to stabilize their business is to deepen and to improve the cooperation among them (like Business Post). The exchange of collected items means that each local or regional postal company would add volume to the delivery network of their cooperation partners which would reduce average costs in delivery and improve their competitiveness. At the same time, this strategy would also reduce the dependency on PostNL's delivery services.

As long as competitors need access to PostNL's network for final delivery the development of new, innovative letter services for nationwide delivery is more difficult. Additionally, business mailers are well educated on the product portfolio of PostNL which makes it more difficult to introduce letter products that are completely different from those of PostNL. Consequently, regional and local competitors offer comparable letter services. Moreover, as outlined by competitors, the final decision of customers mainly depend on the price that has to be lower than PostNL's price while the willingness to pay a mark-up for better quality is actually very low.

Moreover, access conditions to PostNL's network have been the most controversial topic between PostNL and their competitors since more than three years. When using access to PostNL's delivery network many competitors rely on the bulk mail product "Gemengd" (Mixed)⁹¹ that is available for time-critical as well as for non-time-critical delivery. PostNL gives a 1% discount if the letters are "machine-ready" and the consignment includes more than 2,500 items. Discounts for pre-sorting are only available for periodicals and letters with special format (for consignments >5,000 items), but not for products "Mixed", "Small letters" and "Large letters".⁹² That said, operational rebates are relatively small.

⁹⁰ See ACM (2016), Ontwikkelingen en feiten bij de Nederlandse postmarkt in 2015, 21 November 2016.

⁹¹ PostNL's letter product "Mixed" allows for handing over letters of different size, packaging, contents and appearance with a maximum thickness of 32 mm (see for example PostNL, Postal Rates as of 1 January 2016).

⁹² See PostNL, Postal rates as of 1 January 2016, p. 9 sseq.

Much more important are the multi-year volume discounts PostNL offers business mailers with a volume above 50,000 items per year.⁹³ The discount is at least 2.5% of the standard rate. In determining the annual letter volume, the following products are taken into account: Domestic Bulk mail, Domestic Business Reply items and Domestic Letterbox Mail franked with a NetSet™. Domestic bulk mail includes letters, direct mail and periodicals. Article 9 requires that competitors shall have access to an existing nationwide five day delivery network (i.e. PostNL) based on the principles of transparency and non-discrimination compared to services offered (by PostNL) to other postal operators and mailers at special terms and tariffs.⁹⁴

In 2014, first complaints related to this topic have been filed at ACM mainly by the two biggest competitors, Van Straaten Post and Intrapost. Basically, PostNL refused Van Straaten Post access to the “Gemengd” bulk mail product at the same conditions as business mailers⁹⁵ and access to the annual volume discounts.⁹⁶ ACM decided in favour of the complainants on the basis of Article 9 in most cases. PostNL appealed all these decisions and after losing at the court in first instance it went to the highest court. On 8 November 2016 the highest court repealed the ACM decision on PostNL’s discriminatory behaviour because ACM had not sufficiently assessed whether higher tariffs for competitors’ batches consisting letters from different senders were actually discriminatory compared to tariffs bulk mailers have to pay for “per-sender” batches.⁹⁷ In the view of PostNL the highest court decision supports its argumentation that access to bulk mail products and volume discounts can only be given for “per-sender” batches.⁹⁸ In the current situation, there is substantial legal uncertainty for local/regional competitors because postage paid to PostNL for ‘rest mail’ is a major cost to them, but it is not clear how high this cost is under current and future contracts with PostNL.

⁹³ Ibid. p. 14. This is the only year when PostNL titles the volume discounts in this way. In the 2015 and in the 2017 price lists the same discounts were titled “Annual volume discount on letterbox mail”.

⁹⁴ Article 9 Postwet determines in its first paragraph: “Indien een postvervoerbedrijf, dat beschikt over een netwerk waarmee poststukken op ten minste vijf dagen per week kunnen worden bezorgd op alle adressen in Nederland, met gebruikmaking van dat netwerk postvervoer verricht tegen special voorwaarden en tarieven, verricht hij dit postvervoer voor andere postvervoerbedrijven tegen non-discriminatoire en transparante voorwaarden en tarieven ten opzichte van andere afzenders en andere postvervoerbedrijven. [...]”

⁹⁵ PostNL required a mark-up from competitors when handing over letters, see ACM (2015), Besluit van de Autoriteit Consument en Markt als bedoeld in artikel 7:11 van de Algemene wet bestuursrecht naar aanleiding van het bezwaar van Koninklijke PostNL B.V. tegen het besluit van 1 mei 2015 tot oplegging van een last onder dwangsom wegens overtreding van artikel 9 van de Postwet 2009 (de non-discriminatieverplichting).

⁹⁶ See ACM (2015), Besluit van de Autoriteit Consument en Markt op grond van artikel 48, eerste lid, van de Postwet 2009 in samenhang gelezen met artikel 5:32, eerste lid, van de Algemene wet bestuursrecht tot het opleggen van een last onder dwangsom aan Koninklijke PostNL B.V. wegens overtreding van artikel 9 van de Postwet 2009 (de non-discriminatie- en transparantieplichting, alsmede het kenbaarheidsvereiste), 10 april 2015.

⁹⁷ See College van beroep voor het Bedrijfsleven (CbB), zaaknummer 16/173, Uitspraak uitspraak van de meervoudige kamer van 8 november 2016. In this procedure the bpost court ruling has been filed as a relevant case.

⁹⁸ See PostNL (2016), CBb annulled incremental penalty PostNL, press release of 8 November 2016.

The application of Article 9 shall be replaced by Article 13a-k of the current Dutch Postal Act. In case of significant market power in a specific market segment ACM can impose remedies on PostNL, for example to require that PostNL has to provide competing postal operators access to its network at specific conditions (including the way how the access tariffs should be determined). In December 2014, ACM published the first draft decision that PostNL should provide access in the market for time-critical letters (five day delivery). So far, ACM has not yet finally decided how to regulate access to PostNL's delivery network based on Article 13a-k. The most recent draft of the decision was published in July 2016.⁹⁹

Currently, the Ministry of Economics is deciding on a clarification how Articles 13a-k should be applied by ACM, particularly with regard to the long-term impact of ex ante remedies on market players.¹⁰⁰ The decision is still pending.

This discussion shows that the future business opportunities in the delivery of time-critical letters partly depend on pending regulatory decisions on mandatory access to PostNL's postal network. According to ACM and based on interviews with competitors, local postal companies have extended their delivery networks but they have not yet reached nationwide coverage, so far, and therefore still heavily depend on access to PostNL's network to offer their customers nationwide delivery services. The share of letters handed over to PostNL for final delivery declined from 50 to 40% in 2015.¹⁰¹

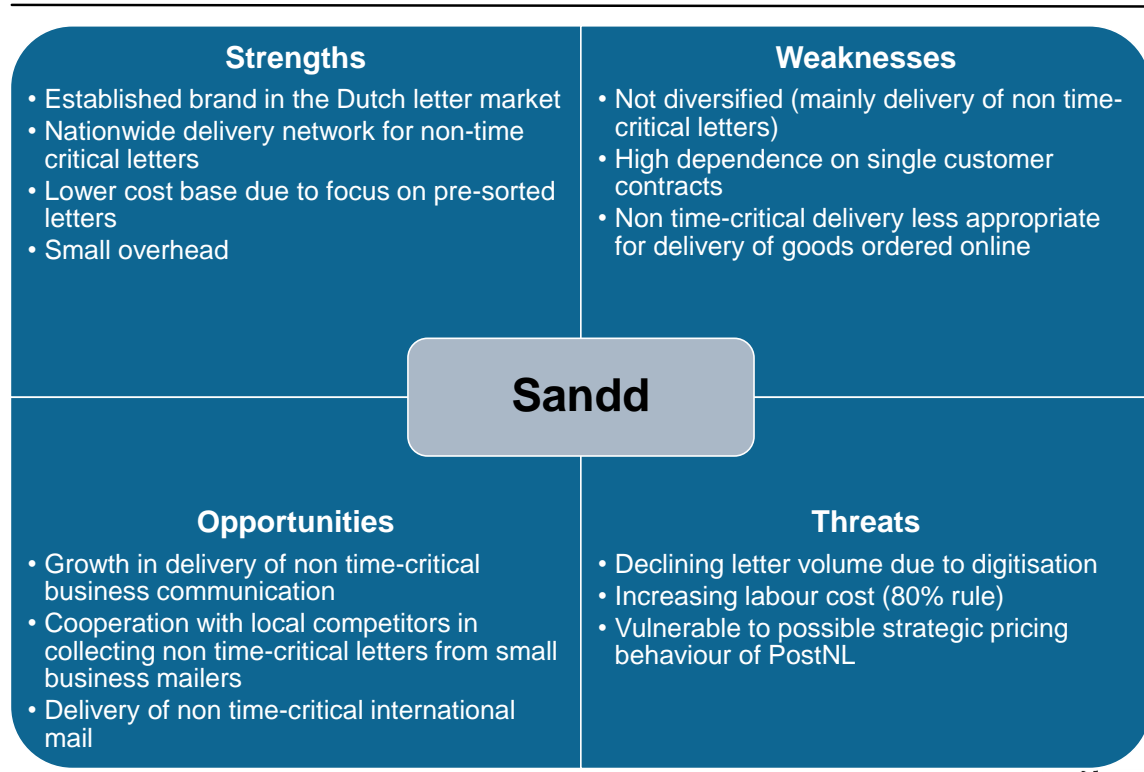
⁹⁹ See ACM (2016), Marktanalysebesluit 24-uurs zakelijke post.

¹⁰⁰ See Minister van Economische Zaken (2016), Concept "Besluit van de Minister van Economische Zaken van houdende beleidsregel inzake de toepassing door de Autoriteit Consument en Markt van de artikelen 13a tot en met 13k van de Postwet 2009", 7 June 2016.

¹⁰¹ See ACM (2016), Ontwikkelingen en feiten bij de Nederlandse postmarkt in 2015, 21 November 2016.

3.3.3 Sandd

Figure 17 SWOT analysis for Sandd



Source: WIK assessment

PostNL’s major competitor in non-time-critical delivery is Sandd. The company addresses the segment of non-time critical letter post including the delivery of direct mail, magazines (including published magazines (e.g. TV guides) and free customer/member magazines that serve more advertising purposes) and, increasingly transaction mail. It mainly targets medium-sized and large business mailers and also participates regularly and successfully in public tenders. Sandd experiences a growing number of small packages (mailing of merchandise in letter format that fits through the aperture of private letter boxes) sent from domestic as well as from foreign e-retailers (Sandd notes that in December 2015 they delivered around 12 million packages in the Netherlands). In relation to international inbound letters Sandd cooperates with foreign postal companies.¹⁰²

Sandd delivers letter post items at two fixed days per week (“delivery days”) nationwide. It does neither cooperate with local or regional competitors nor with PostNL for final delivery of letters. Letter post items are either collected by Sandd at the premises of the

¹⁰² Interview Sandd, 2 August 2016.

sender / mailing house or transported to one of the depots. Sorting is done “digitally” during letter production (i.e. printing). Sandd mainly deals with pre-sorted bundles of letter items that can easily be distributed to deliverers so that no specific sorting technology and space is needed. The deliverers manually sort the items to delivery sequence before they start their rounds. Delivery is mainly organized by part-time workers, partly employed by Sandd (“contract employees”) and partly self-employed. Sandd initially left it up to its deliverers to decide whether they wish a contract or whether to remain flexible. Driven by the legal obligation to have at least 80% contract employees, the company is now forced to replace deliverers. Sandd reports that the switch to contract employees will increase labour cost.¹⁰³

Sandd argues that the application of “80%-clause” increases labour cost driven by more administrative costs, higher social security payments including employee leave benefits while the wage levels remain the same. Sandd is clearly challenged by the legal requirement to employ at least 80% of their personnel on a contractual basis (instead of cheaper and more flexible OVO). This requirement becomes obligatory by the end of 2016.¹⁰⁴

After the acquisition of Selektmail by Sandd and PostNL’s decision to stop low cost letter delivery services via its subsidiary Netwerk VSP Sandd expected that price competition would become more relaxed and thus facilitate the switch from self-employed deliverers to contract employees. Despite of the consolidation process, price competition remained intense in the segment of non-time critical delivery services reflected in fairly stable average revenues per item as outline in Section 2.1.2 of this report. Moreover, Sandd could be threatened by “targeted discounts” as announced by PostNL in its Strategy Update.¹⁰⁵ As Sandd’s customer base mainly consists of medium-sized and large business mailers it can be substantially harmed when losing single customers. Recently, ACM published an information request on the functioning of the market for non-time-critical delivery due to competition problems in this segment.¹⁰⁶

Overall, Sandd’s future business opportunities depend on PostNL’s pricing strategy in non-time-critical delivery additional to its own strategic decisions and ACM’s behaviour (as competition authority). Sandd has a lower cost base than PostNL due to a lower number of delivery days, a smaller collection network and the focus on pre-sorted letters. In addition, Sandd has benefited from economies of scale because of growing volume since 2010. In contrast, PostNL has synergies in the combined delivery of time-critical and non-time-critical letters and thus more volume to be delivered. Moreover, Sandd’s current business model limits its opportunities to approach small and very small business mailers because of a lack of sorting capacities and a dense collection

¹⁰³ Interview Sandd, 2 August 2016.

¹⁰⁴ See Postwet 2009, Article 8 as amended in 2015.

¹⁰⁵ See PostNL (2015), PostNL 2020 Strategy update, 3 November 2016, p. 19.

¹⁰⁶ See ACM, Consultatie zakelijke post, 16 September 2016.

network. To close this gap Sandd could cooperate with other market participants that provide sorting capacities (e.g. Intrapost) and have access to very small and small business mailers.

Generally, Sandd's opportunity to diversify its business to new services or to attract additional volume from the growing e-commerce business appears limited. Dutch online buyers are very demanding with regard to speed of delivery. Next day delivery is the standard for domestic e-commerce deliveries, a standard that is not achievable for Sandd given its current business model (two-day delivery service) and would require a fundamental strategic change. The growing cross-border e-commerce business could be an opportunity to attract additional volume.

3.4 Future developments scenarios in the Dutch postal market

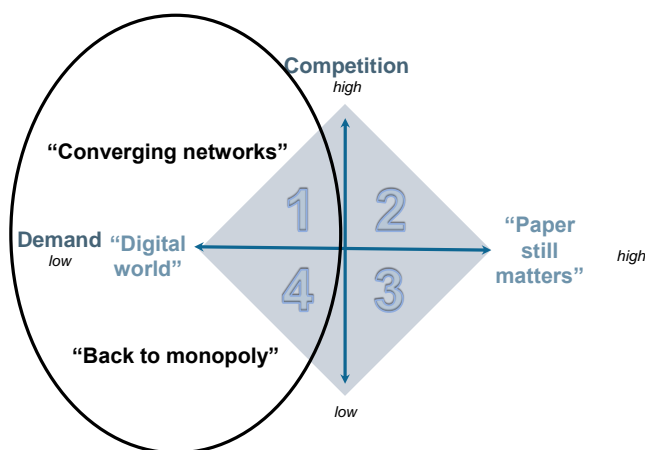
In ten years' time there would still be demand for time-critical and non-time-critical letter services, however, at much lower level than today. Domestic and cross-border e-commerce may drive delivery volume of items that can easily be delivered in the letter box. In the Digital World time-critical delivery would therefore increasingly consist of goods either sent by letter or parcel service (depending on size, weight and value) and urgent documents mainly sent from/to government institutions, businesses and consumers that would still need paper-based communication for different reasons (e.g. security, refusal or disability to use digital communication). Other, less important business communication, advertising and remaining publications would be only use non-time-critical delivery services.

The previous sections presented the current situation of market players in the Dutch letter market under the existing regulatory framework. Competition in the Dutch letter market has successfully emerged in time-critical and non-time-critical delivery of letters despite of the shrinking letter market. In the non-time-critical segment competition is characterised by slowly declining volume and fierce price competition between two remaining major players, PostNL and Sandd. Local and regional competitors managed to develop some business in time-critical delivery of letters targeting small and medium-sized business customers. This group of competitors still depends on PostNL's network to organise delivery of their 'rest mail', and thus be able to offer nationwide coverage to their customers. Simultaneously, total demand for time-critical delivery of letters has been declining more than for non-time-critical letters. The group of small business mailers appears to be more reluctant to switch to slower services than medium-sized and large business mailers.

The SWOT analysis also highlighted that competitors' success in the Dutch letter market in both segments, time-critical and non-time-critical delivery, significantly depends on the pricing strategy of PostNL as leading postal operator in the Dutch letter market with a market share of 80-90%. In light of its declining letter volume PostNL has

decided to defend market shares in the Dutch letter market more actively than in the past five years, to protect volume. In non-time-critical delivery, the major competitor Sandd reports to be challenged by PostNL's current pricing strategy. In time-critical delivery of letters, local and regional competitors are facing regulatory uncertainty about future access conditions to PostNL's postal network, and thus a major input cost to their business.

Figure 18 Future development scenarios of the Dutch letter market



Source: WIK

In the following we present two different scenarios, “Converging networks” and “Back to monopoly”, that describe potential market outcomes for the next ten years given the current regulatory framework. Which of the two scenarios may emerge depends on many factors including demand trends, operators’ strategies, cost trends, and future regulation.

3.4.1 “Converging networks”

The scenario “Converging networks” will result in a competitive landscape with two postal operators delivering non-time-critical letters nationwide, many regional competitors specialised on time-critical delivery of documents and goods, and cooperation with national parcel networks for some products or regions. In the scenario “Converging networks” nationwide delivery of letters will be organised flexibly considering cost efficiency of specific suppliers, and needs of specific customers.

Local and regional competitors will maintain good relations to local companies and public authorities and will be successful in customer care and service. They will benefit from the demand trend to more environmentally-friendly delivery solutions and emerging city logistics solutions. They will further develop the cooperation with other local and regional competitors, parcel operators, and PostNL to offer best value to

postal customers. In this scenario, different operators will cooperate professionally on operational issues (interconnection, exchange of letters, quality control) and contracting (agreed service levels and pricing).

For local competitors, the main goal will be to deliver as much volume as possible within their own delivery networks regardless of where the items come from, as long as the price they get covers their costs. Inter-carrier business will become a major business for all postal operators, including PostNL, and carriers will regard each other as important customers (in addition to competing in other market segments). Technological progress could promote this process (e.g. emerging IT platforms for logistics solutions that would facilitate the coordination of collection and delivery processes between several parties¹⁰⁷). Due to general volume decline we expect that the number of local competitors will decline either by market exit or by acquisition particularly in areas where more than one local postal operator is active. The remaining regional delivery companies will benefit from economies of scale due to higher delivery volume.

In non-time-critical delivery, Sandd will remain the major competitor of PostNL. Our research has shown very clearly that there is no appetite by investors to create a third network to compete with PostNL and Sandd in this segment. Therefore, in this market segment, maintaining the two operators is the most competitive outcome that appears realistic. We expect that non-time-critical letters will be less affected by volume decline than time-critical letters. First, time-critical business communication partly switches to non-time-critical delivery services and Sandd will be successful in attracting new customers in this segment. Second, direct mail will be less affected by volume decline than communication and transactional letters. The attention and the response rates of direct mail increases the lower the number of total delivered items which supports the competitiveness of paper-based advertising with digital advertising channels.

In light of volume decline it is not likely that Sandd would increase the number of delivery days from two to three per week. Sandd benefits from higher economies of scale with two day delivery. Additionally, Sandd's operational costs would remain lower and more flexible in volume than those of PostNL's.¹⁰⁸ Particularly the second element supports Sandd's financial viability in the shrinking letter market.

Medium-sized and large business mailers that need nationwide delivery benefit from current competition in non-time-critical delivery because they have the choice between two alternative networks. This improves their bargaining position with both postal operators resulting in more cost-oriented prices for reliable delivery services. For this reason, medium-sized and large business mailers have an incentive to promote

¹⁰⁷ See for example Tiramizoo, that provides to senders customised solutions in same-day delivery in cooperation with many local courier companies.

¹⁰⁸ The proportion of fixed costs in delivery will increase if the company becomes less flexible with regard to labour conditions by law.

competition in nationwide delivery of non-time-critical letters and may therefore support future competition in the market for strategic reasons.

In the scenario “Converging networks”, PostNL will remain the only postal company with a nationwide network for time-critical and non-time-critical letters. PostNL has already achieved a high level of cost efficiency and is able to flexibly organise letter delivery by switching between its delivery networks for letters, parcels and leaflets (unaddressed advertising) where economically reasonable (as they already do today, e.g. when jointly delivering registered letters and parcels).

Local and regional competitors will still need access to PostNL’s network for letters to be delivered to the rest of the Netherlands at the next working day, but at declining scale over time. In this scenario, PostNL will provide access to competitors at attractive conditions for both sides, and will increasingly regard local competitors as important customers in some market segments. In the short run, some regulatory action by ACM may be necessary to overcome current uncertainty around access. In the future, we imagine that local and regional competitors may as well cooperate with Sandd in the collection and delivery of non-time-critical letters. Similarly, PostNL may see benefits in cooperating with the most successful regional competitors in final delivery of its time-critical letters in some areas of the Netherlands.

3.4.2 “Back to monopoly”

The scenario “Back to monopoly” describes the opposed development where letter volume decline combined with other factors will result in a situation with PostNL as the only surviving company providing time-critical and non-time-critical postal services.

PostNL benefits from economies of scale and scope that will remain more significant than those of its competitors. Additionally, PostNL has reacted on competition by improved customer service and a pricing schedule that has been particularly attractive for medium-sized and large business mailers in all segments. Finally, despite volume decline PostNL has been very active to improve its services and to develop new products often in combination with sophisticated IT solutions. It is very likely, that PostNL will put similar efforts in its future postal strategy. Finally, PostNL has proven since 2010 (and earlier) that it is able to keep its profitability despite significant volume decline. In this scenario “Back to the monopoly” PostNL will continue its efforts to successfully rescale letter operations in line with volume decline. Likely growth in more “valuable” letterbox packets (in terms of average revenues) in letter delivery will additionally support the financial viability of PostNL’s network in future.

In contrast to the “multi-product” company PostNL, competitors are often “stand-alone” suppliers of specific postal products and have less opportunities to compensate losses in letter delivery by other businesses. Sandd will be particularly challenged because of

its focus on non-time-critical delivery services that are less appropriate for growing e-commerce delivery. The focus on medium-sized and large business mailers with long contract periods will additionally threaten Sandd's business model in this scenario. If PostNL was successful in winning back important contracts from business mailers Sandd's profitability would be threatened by general volume decline plus a loss in market share. This development combined with potentially increasing labour cost would end up with the market exit of Sandd in this scenario, and thus lead to a monopolistic situation in the segment of non-time-critical delivery of letters.

Local and regional competitors will also be challenged by general decline in letter volume. At short term, regulatory uncertainty on access conditions will limit their opportunities to acquire new customers. Local and regional competitors that also offer local courier services (like Cycloon) or are specialised on specific segments, e.g. the collection and delivery of legal documents (like Falk) will be less challenged. In this scenario, local operators will not find ways to maintain their current cost advantages as their business declines. As flexible, relatively small companies they would decide to exit the postal delivery segment if the business became loss-making. Instead, they could for example put all their efforts on high-revenue and high-quality delivery services that will become increasingly attractive for e-commerce deliveries (same-day delivery, delivery within two, three or four hours). In total, this will result in a fall back to the pre-2010 situation with negligible competition in letter delivery, or even to the postal monopoly of the last millennium.

3.5 Sustainability of USO provision

The negative demand trend in written communication will affect the future development of USO items. Universal postal services comprise domestic and international letter and parcel services, including the possibility to send registered and insured items. Unlike to other EU Member States. The scope of domestic universal services is very narrowly defined in the Netherlands and includes only single-piece items (stamped and franked letters and parcels). Between 2010 and 2015, domestic USO letters declined more rapidly than international import and export letters with the consequence that the proportion of international letters on total USO letters has increased. Domestic USO letters have declined by 37%, cross-border inbound letters by less than 20% while cross-border outbound items remained fairly stable. USO parcels have grown by 36% (more than 6% per year) from 11 to 15 million parcels in the same period.¹⁰⁹

USO letters and parcels have to be delivered on five days per week (Tuesday to Saturday) and are therefore part of the time-critical items. Letters with medical contents and funeral announcements have to be delivered on six days per week, including Monday. Moreover, senders shall have the possibility to consign letters and parcels in

¹⁰⁹ WIK calculation based on PostNL (2016), Response PostNL to WIK questions.

postal outlets (at least 1,000) and letters additionally in street letter boxes (around 10,000). Letters and parcels should be collected from postal outlets and street letter boxes five days per week.

Table 5 Illustrative example: PostNL's average costs for USO items in 2015 and 2025

Year	2014	2015	2025 (estimated)	
			% fixed costs: 100%	% fixed costs: 50%
USO volume (million)	807	780	390	390
Operating expenditure (million EUR)	777	827	827	620
Average operating expenditure per item (EUR)	0.96	1.06	2.12	1.59

Source: WIK estimation based on PostNL (2016), Response PostNL to WIK questions, 19 August 2016 and PostNL, Financiële Verantwoording universele postdienst 2014 and 2015.

Notes: USO volume include domestic single-piece letters and parcels, cross-border inbound and outbound letters and parcels.

Simplifying assumptions for the calculation:

Operating expenditures in 2015 input prices (no change in input prices).

Unchanged volume structure and stable operating costs.

PostNL reported positive margins in the provision of universal services of 9% in 2014 and 5.5% in 2015.¹¹⁰ Despite of substantial decline in USO letter volume USO revenues have increased by 3.7% driven by increases in letter tariffs and growth in USO parcels. Total costs allocated to universal services increased more than double by 7.8% (see Table 5). This substantial increase in universal services cost is explained by the increased number of parcels, higher pension costs and increased fixed costs allocated to universal services. The cost of time-critical delivery of letters and parcels is shared between USO and time-critical non-USO products that need five day delivery per week. PostNL reported that the share of non-USO business letters on total time-critical letters declined in 2015. Consequently, USO services had to cover a higher share of the fixed costs of the five-day delivery network.¹¹¹

Table 5 also illustrates the development of average costs per USO item based on the regulatory financial reports of PostNL. The reports do not allow identifying costs allocated to different universal services (domestic USO letters, domestic parcels, cross-border inbound & outbound USO items) so that the impact of changes in the volume structure cannot be identified. Assuming stable costs and unchanged volume structure average costs per USO item would double if costs were fully fixed and they would remain constant if the share of fixed costs was 50%. This illustrative example indicates

¹¹⁰ See PostNL, Financiële Verantwoording universele postdienst 2014 and 2015.

¹¹¹ See PostNL (2016), Financiële Verantwoording universele postdienst 2015, p. 8.

that the pressure to substantial increases in single-piece tariffs to cover USO costs grows in the next years if the regulatory framework remains unchanged.

A reliable forecast of future USO costs is not feasible. There are indications for declining USO costs. Firstly, PostNL is reducing the number of collection boxes and full-service postal outlets in 2016 and 2017. This would reduce total cost and particularly fixed cost in providing USO services. Secondly, driven by competition PostNL is continuously improving efficiency in administration and postal as well as parcel operations to save costs. It is always looking for the most cost-effective way to organise the collection, sorting and delivery of different letter and parcel products. As USO and non-USO services are provided in the same networks, USO service provision will also benefit from these efforts. Increasing costs for labour (wages and pension costs), outsourced activities (e.g. transport services and sub-contractors in parcel delivery) and other operating costs could reduce or even outweigh net cost savings. However, PostNL is a highly commercial, profit-oriented company and therefore highly professional in making good deals in order to minimize increases in input costs.

Volume per USO segment (domestic letters, parcels and international items) is developing differently. In WIK's view, the provision of collection and delivery services for USO parcels at affordable prices will not be threatened in the next 10 years for the following reasons. Firstly, the number of USO parcels as well as the total number of parcels (at PostNL and in the market) has been growing. This reduces average costs in delivering parcels. Secondly, PostNL delivers parcels on six days per week and not on five days as required by the USO. The USO requirement of five day delivery is therefore not binding for parcels. Delivery quality is high: tracked delivery and delivery the next working day is standard for PostNL's parcel services, including USO parcels. The needs of online sellers and online buyers drive PostNL and other suppliers in the parcel market to keep the quality level high (and prices low). Thirdly, affordability of USO parcel services is reflected by stable tariffs for sending single-piece parcels at a level of below 7 Euros during the last five years.¹¹² Fourthly, competitors in the Dutch parcel market, like DPD or DHL, both offer parcel services to consumers at competitive tariffs. Moreover, competition in the Dutch parcel market (which is more substantial than in the Dutch letter market) has not threatened the provision of USO parcel services in any way. That said, it is also unlikely that PostNL would reduce the number of postal outlets/parcel shops because this very dense network is one of its unique selling points compared to its competitors.

The situation is different in the USO letter segment. The Dutch letter market is shrinking and so do domestic and, to less extent, cross-border USO letters. In the past, the collection (from street letter boxes) and the delivery of USO letters on five days per week was more challenged by digitisation than by competition. The share of single-

¹¹² See PostNL, Price lists 2010-2016.

piece USO letters delivered in the Netherlands (domestic and international import) on total delivered letters of PostNL is around 16%.¹¹³ The domestic USO letters include consumer letters (around 7% of total domestic letters) and letters sent by small businesses, both account for about half of domestic USO volume.

Today, competition in the USO letter segment still appears to be negligible. PostNL is the only postal operator that has, for historical reasons, a dense network of street letter boxes. It is not likely that competitors in the letter market would build up a similar dense network nationwide because it is very costly and time-consuming (finding and renting locations, buying secure boxes). Additionally, volume collected would be very low so that collection costs (which are mostly fixed) would be very high per item. Moreover, it is not likely that PostNL would completely give up their street letter boxes in order not to harm their brand and reputation.

The narrow definition of domestic USO letters to single piece items implies that the future development of USO costs depends on four factors: (1) impact of digitisation, (2) switch of USO letters to PostNL's non-USO time-critical and non-time-critical bulk mail products and (3) switch of small and medium-sized business customers to local and regional competitors for sending time-critical letters and (4) switch of business customers from time-critical to non-time-critical services offered by PostNL and Sandd.

- (1) Digitisation is in our view by far most important challenge for USO letters. Particularly consumer letters which account for around half of total domestic USO letters have declined substantially. Business letters are also heavily affected by digitisation but still less than consumer letters.
- (2) PostNL also offers non-USO bulk mail products for small business customers. The most attractive non-USO bulk mail product for very small business mailers is the bulk mail product "Mixed". If PostNL reduces the tariffs of non-USO products below the tariff of comparable USO services very small business mailers have an incentive to switch from USO to non-USO services. This switch will additionally reduce USO letter volume. PostNL announced to reduce the tariffs of non-USO products below the level of franked single-piece letters from January 2017.¹¹⁴
- (3) If business customers switch time-critical letters to local and regional competitors this may increase the share of USO letters on total time-critical letters. In this case,

¹¹³ See PostNL (2016), Response PostNL to WIK questions, 19 August 2016.

¹¹⁴ The lowest threshold of the bulk mail product "Mixed" is 22 Euros minimum revenue per consignment. Between 2010 and 2016 the single-piece tariff for franked letters (20g) was always lower than the lowest available 24h and 48h tariff for the "Mixed" 20g letter (excl. VAT). In the same period the minimum revenue per consignment has grown from 15 Euros to 22 Euros. This will change in 2017. PostNL reduces the revenue threshold to 17.50 Euros as well as the 24h and 48h tariffs below the single-piece tariff of a franked 20g USO letter. The franked 20g USO letter will cost 0.72 Euros per item while the "Mixed" 20g letter will cost 0.71 (24h delivery) respectively 0.63 Euros (48h delivery).

the cost base for USO letters will increase which will further drive average costs of USO letters (and thus tariffs).

- (4) In light of the stakeholders' expectation that time-critical delivery becomes less important for senders due to secure and quick electronic alternatives and cheaper, non-time-critical, day-definite delivery services¹¹⁵ it is possible that the share of USO letters on total time-critical letters will increase. Then again, USO letters have to cover a higher share of fixed costs which may result in additional price increases.

Experience with competition in non-time-critical delivery in the Netherlands has shown that it has not harmed universal service provision in the past. First, switching costs between time-critical and non-time-critical delivery services offered by PostNL are low (particularly if business customers additionally benefit from multi-annual volume discounts that not differentiate between time-critical and non-time-critical letter products). Second, Sandd has been more successful in targeting medium-sized and large business customers for mainly delivering direct mail and periodicals than in targeting small business customers.

Competition generally challenges revenues and volume of incumbent postal operators but it also promotes efficiency and flexibility in postal operations in combination with cost savings at incumbents, including PostNL. Moreover, competition means more choice and (relatively) lower prices for business mailers which again reduces the incentives to move from physical to digital communication channels and improves the competitiveness of postal services in the digital world, generally.

Given these trends we expect that the tariffs for single-piece letters will continue to increase. USO tariffs are regulated by a complex price formula that ensures that the headroom for price increases depends on the development of average fixed costs (among other things). The cost base in the price formula refers to the financial year 2014 (after the reduction of the number of delivery days from six to five) and will be inflated by the consumer price index year-on-year. ACM yearly checks the level of fixed costs allocated to universal services and its share on total cost. Assuming constant fixed costs for USO letters the average fixed cost increases with volume decline. This again increases the leeway for higher USO tariffs.

¹¹⁵ Stakeholder workshop, 15 September 2016.

4 Scenarios for future postal policy

4.1 Introduction

Dutch postal legislation is guided by two main objectives: (1) To ensure an affordable and sustainable universal postal services and (2) to ensure a sustainable competitive postal market. In this study, we examine how these policy objectives can be achieved in each of the scenarios for future development of the Dutch postal market, and in line with the requirements of the EU Postal Directive.

Basically, we argue that the regulatory framework should introduce the least deviation from the rules of the normal commercial market necessary and proportionate to achievement of the policy objectives agreed for the sector. Particularly, the regulatory framework and its application should not predetermine specific business models in postal operations beforehand but this should be left for the market. This is important because market dynamics have increased and uncertainty about developments and the future role of postal services in the “Digital World” is uncertain.

Based on our research on the current state of the Dutch postal market, and interviews with many stakeholders in the market, this study discussed a bundle of detailed policy options (see Appendix). Against the objective of safeguarding affordability, availability, choice and quality in the postal market, the Appendix addresses a bundle of policy options concerning five important policy areas (tools): designation of the universal service provider, USO requirements, USO reporting, access for competitors and ex post control. The appropriateness of each policy option is discussed separately for the scenarios “Back to monopoly” and “Converging networks”. In both scenarios we expect that letter volume will continue to decline substantially.

Table 6 compiles our analysis of the detailed policy options. The conclusions are summarised using coloured balls (borrowed from common traffic lights): A red ball indicates that the policy option would not be appropriate in the sense that it harms the market outcome in the considered scenario. A green ball means that the option would be appropriate in the sense that it supports the better functioning of the postal market in that situation. A yellow ball indicates that the option is “neutral” which means that it neither harms nor supports the considered scenario.

Table 6 Policy options: Summary assessment

Policy tools	Policy options	Scenario for future development	
		Back to monopoly	Converging networks
Designation of universal service provider	No change: Keep PostNL as designated USP	●	●
	Designate more than one postal operator as universal service provider	●	●
	Rely on market forces to ensure the universal postal service	●	●
USO requirements	No change: Keep current USO requirements	●	●
	Allow for more flexible universal service requirements	●	●
USO reporting	No change: Keep reporting on consolidated USO results	●	●
	Require segment reporting on USO services	●	●
Access for competitors	Remove access regulation for rest mail	●	●
	Impose basic access products for rest mail	●	●
Ex post price control	No change: Cautious approach in controlling predatory pricing	●	●
	Enforced action against possible predatory pricing, fidelity rebates and tying	●	●

Source: WIK assessment.

Notes: Red ball: Policy option is not appropriate for the scenario.
Green ball: Policy option is appropriate for the scenario.
Yellow ball: Policy option is neutral.

The detailed options are not independent of each other. The next two sections present recommended bundles of policies that, based on our expert assessment, are best suited for the two scenarios of future market development:

- (1) “Converging networks”: In this scenario, the key policy objective will be to protect infrastructure competition for the benefit of postal users.
- (2) “Back to the monopoly”: In this scenario, the key policy objective will be to ensure universal postal services in the Digital World.

4.2 “Converging networks”: Protect infrastructure competition for the benefit of postal users

The scenario “**Converging networks**” is characterised by a more competitive landscape regarding how letter delivery services could be organised in the future, based on commercially oriented players in letter and parcel delivery.

- There will be two postal operators delivering non-time-critical letters nationwide and regional competitors specialised on time-critical delivery of documents and goods (in addition to PostNL).
- Business mailers have an incentive to support future competition in the market for strategic reasons.
- Regional competitors will further develop the cooperation with other competitors, parcel operators, and PostNL to offer best value to postal customers.
- Inter-carrier business will become a major business for all postal operators, including PostNL, and carriers will regard each other as important customers (in addition to competing in other market segments).

This scenario requires a balanced approach to ensuring universal postal service by relying on market powers. This approach puts the emphasis on competition and trust in commercial solutions to meet the challenges of a shrinking letter market. Under conditions of uncertainty it is a good strategy to rely more on the market forces of demand and supply. Compared to regulation, market forces are better able to develop, test and implement innovations, or to adapt their business to the rapidly changing technologies and customers’ needs. This approach would support the competitiveness of the postal sector in the wider communication and advertising markets and ensures that postal services would meet the needs of all postal users, including consumers, small, medium-sized and large business customers as senders and recipients.

Table 7 “Converging networks”: Recommended policy options

Recommended policy options	Converging networks
Rely on market forces to ensure the universal postal service	●
Allow for more flexible universal service requirements	●
Impose basic access products for rest mail	●
Enforced action against possible predatory pricing, fidelity rebates and tying	●

Source: WIK assessment.

Notes: Red ball: Policy option is not appropriate for the scenario.
 Green ball: Policy option is appropriate for the scenario.
 Yellow ball: Policy option is “neutral”.

Rely on market forces to ensure the universal postal service

Today, the Dutch letter market is one of the most competitive markets in the European Union despite of being highly challenged by volume decline. In the scenario “Converging networks”, competition in the Dutch letter market will still exist. For this reason it is conceivable that most parts of the universal service will be satisfactorily provided by “market forces” without a designated universal service provider:

- In this scenario business mailers will have the choice between different postal companies delivering their letters: small, medium-sized and large business mailers. Competition ensures that prices will be more cost-oriented and postal companies will seek for opportunities to improve customer services.
- The provision of nationwide letter services to all customer groups forms an essential element of PostNL’s reputation and represents a unique selling point. For this reason, it is unlikely that PostNL would stop providing this service if not being the designated universal service provider.
- Consumers and small business mailers (including online sellers) already have the choice between domestic and international parcel services provided by different parcel operators. Driven by e-commerce (demand) trends and competition, accessibility and affordability of consumer parcel services will further improve.

If the market does not satisfactorily provide all universal services or parts of it then it can be considered to designate the market dominant postal operator. If no postal company is designated to provide specific universal postal services the regulation of universal service tariffs, if considered necessary, could be linked to the market dominant position.

Allow for more flexible universal service requirements

In both future developments scenarios declining letter volume is the major threat for the affordability of USO letter services in the future. USO letter volume is additionally threatened by competition with non-USO letter services. The USO requirements affect cost flexibility in the provision of postal services by determining minimum criteria for the accessibility and the collection and delivery frequency per week. Declining USO letter volume results in increasing average costs because some costs are still fixed in collection and in delivery on five days per week.

Since 2014, the decision procedure for adapting USO requirements has been facilitated. They are regulated by Ministry decision and can be adapted, if considered necessary, based an evaluation of the USO every three years. The number of options for further reducing universal service requirements in compliance with the Postal Directive appear limited. However there is still some room of manoeuvre by further

relaxing the accessibility requirements and by considering exemptions from five-day collection and delivery.

Impose basic access products for rest mail

As long as local and regional competitors do not have nationwide coverage, they need access to an existing postal network for their “rest mail”, i.e. for the mail that they collect from their customers but that is directed to areas/addresses that they do not deliver to. If market players cannot agree on terms of access, ensuring such access for competitors may require regulatory decisions that enforce non-discriminatory terms of access. The objective of such regulation should be to ensure that local/regional competitors can offer similar terms to their customers for rest mail that the customers would get from PostNL in their own right, and ensure simple procedures for exchanging mail between operators seeking and granting access for rest mail. That way competitors can focus on being competitive in the part of the country where they deliver.

Downstream access vs. Access for rest mail

Since postal liberalisation started in the 1990s, there have been controversial discussions about the need to impose access obligations on incumbent postal operators. In part, those discussions were transferred to the postal sector from telecommunications and other sectors with strong physical infrastructure. Where access has been imposed in the postal sector (e.g. in Germany, the UK), access has created business opportunities for consolidators, i.e. companies that collect and pre-sort mail but do not have own delivery operations. In other countries, incumbent operators have voluntarily offered discounts for consolidators to incite additional demand, and save operational cost in collection (e.g. France). In the UK, access discounts are so high that no alternative carriers found it economical to roll out delivery networks. This shows that there can be a tension between access and consolidation on the one hand, and infrastructure competition on the other hand. While there are no definite conclusions from discussions in economic literature for the postal sector, it seems fair to say that practical experience with such downstream access is not entirely good.

In the postal sector, the Netherlands have traditionally relied on infrastructure competition rather than downstream access. The discussions at a stakeholder workshop as well as all persons interviewed for this study highlighted the importance of infrastructure competition in the Dutch postal market. For this study, therefore, we have not specifically examined, and do not recommend introducing low access rates that would offer high margins to competitors, and would allow consolidation to emerge as a stand-alone business model.

By contrast, local and regional competitors rely on the incumbent operator (and possibly other regional operators) to deliver their rest mail. For this mail, this report argues that regional competitors should have access to similar retail prices as other senders with similar mail, but should not get wholesale prices with special discounts (“margins”). That way competitors can focus on being competitive in the part of the country where they deliver.

In the scenario “Converging networks” infrastructure competition will successfully emerge in letter delivery where local and regional competitors cooperates with each other. In this scenario the importance of basic access products will therefore decline with increasing coverage of the Netherlands by competitors’ own delivery infrastructure and will therefore simultaneously reduce the competitors’ dependence on the product

portfolio of the market dominant operator. In the transition period to this scenario, enforcing non-discriminatory access for rest mail could be necessary to protect infrastructure competition.

Imposing access products means that a market-dominant company would be obliged to provide access to certain network components determined by the regulator for a fee also determined by the regulator. Regulated access should be the measure of last resort, i.e. such obligations should be imposed only after negotiations between the market dominant operator and competitors have failed. In that case each party has the right to go to ACM to call for imposing access products. For this purpose, the existing legal instrument of access regulation (Article 13a-k) of the Postal Law (Postwet) should be kept as a possibility in postal law, but should be implemented by ACM with great care in practice.

Enforced action against possible predatory pricing, fidelity rebates and tying

Today, PostNL has a market share between 80 and 90 percent in the Dutch letter market (only domestic letters). It has strong economic advantages because it benefits from substantial economies of scale and scope in best combining the available delivery networks (for letters, parcels and unaddressed items). However, noticeable infrastructure competition has successfully emerged in time-critical and non-time-critical delivery despite declining letter volume.

To support the transition to “Converging networks”, strict enforcement of competition law standards appears necessary as long as PostNL continues to be dominant. This option means that ACM would scrutinise potentially abusive pricing practices vigorously, applying its powers under competition law. To prevent anticompetitive pricing strategies, it is necessary that ACM is informed about individual contracts and the pricing behaviour of the market dominant postal operator on a regular base. In case of individual contracts, no side (neither the market dominant postal operator nor the customer) has an incentive to provide this information voluntarily.

4.3 “Back to monopoly”: Ensure universal postal services in the Digital World

“Back to monopoly” describes a development path where volume decline could result in a situation with the incumbent as the only surviving company to provide letter services in the Netherlands.

- PostNL has significant economies of scale and scope and is well-prepared for future challenges due to improved customer service, new and improved products often in combination with sophisticated IT solutions, highly efficient letter and parcel operations and its ability to rescale letter operations in line with volume decline.
- In contrast to the “multi-product” company PostNL, competitors are often “stand-alone” suppliers of specific postal products, like Sandd, and have less opportunities to compensate losses in letter delivery by other businesses.
 - Sandd will face increasing average costs due to volume decline and increasing input costs.
 - As flexible, relatively small companies regional competitors will exit the postal delivery segment if the letter business becomes loss-making.
- In “Back to monopoly”, the combination of increasing average costs and intense price competition with the incumbent would result in a fall back to the postal monopoly of the last millennium.

Even in the “Digital World”, universal postal services will still play a role to secure reliable communication between all households, individuals, businesses, and government offices. As competition cannot ensure strong incentives on the postal market in this scenario, regulatory authorities will need to put emphasis on ensuring universal postal services.

Table 8 “Back to monopoly”: Recommended policy options

Recommended policy options	Back to monopoly
Keep PostNL as designated USP	●
Allow for more flexible universal service requirements	●
Require segment reporting on USO services	●

Source: WIK assessment.

Notes: Red ball: Policy option is not appropriate for the scenario.
 Green ball: Policy option is appropriate for the scenario.
 Yellow ball: Policy option is “neutral”.

Keep PostNL as designated USP in the Dutch letter market

In this scenario, PostNL would be the only surviving postal operator in the Dutch letter market. “Keep PostNL as designated universal service provider” would be the most appropriate instrument to replace the missing market incentives, particularly for most vulnerable postal users, notably consumers.

Economic theory suggests that, without designation, PostNL, as monopolist would focus more on saving operational costs and maximising revenues than on the basic needs of postal users in the provision of universal services. The option to designate PostNL as universal service provider would allow a closer regulation of quality of service and tariffs of universal services.

The situation will be completely different in the Dutch parcel market where competition will continue emerging. For this reason policy makers should consider having a designation only for universal service letters, but to rely on market forces for parcels.

Allow for more flexible universal service requirements

In both future developments scenarios declining letter volume will be the major threat for the affordability of USO letter services in the future. USO letter volume could be additionally threatened by competition with non-USO letter services (that would only be provided by PostNL and would therefore depend on PostNL’s pricing policy). Due to declining demand for USO services policy makers should allow for more flexible universal service requirements also in this scenario.

Require segment reporting on USO services

Developments in volume, revenues and costs vary among letters and parcels, domestic and international. Letters are declining, domestic more than international. USO parcels are growing. More transparency on volume, cost and revenue developments in universal service provision will improve transparency on detailed demand developments and potential sources of losses. This would facilitate policy decisions on future USO requirements. Additionally, segment reporting would meet complaints from competitors in letter and parcel delivery on missing transparency in USO costs.

If the policy makers decided to stick to designation of one postal operator (i.e. PostNL) as we recommend for this competition scenario it should be considered to require a more detailed reporting on universal services. The designated universal service provider could for example report on (1) Domestic letter services, (2) Domestic parcel services (if element of the designation), (3) International inbound postal services and (4) International outbound postal services, separately.

Appendix: Discussion of detailed policy options

A1 Introduction

The “megatrend” digitisation challenges the business models of all relevant players in the Dutch letter market and the provision of the universal postal service as it is defined today. There is substantial uncertainty about the future of competition in the Dutch postal market, and future levels of competition will depend on the demand trends, the behaviour of the market players, particularly of the incumbent PostNL, as well as the regulatory framework established by postal legislation and its implementation in practice (e.g. by regulatory decisions of ACM).

Table A1 Overview of policy tools and addressed policy options

Policy tools	Policy options
Designation of universals service provider	No change: Keep PostNL as designated USP
	Designate more than one postal operator as universal service provider
	Rely on market forces first to ensure the universal postal service
USO requirements	No change: Keep current USO requirements
	Allow for more flexible universal service requirements
USO reporting	No change: Keep reporting on consolidated USO results
	Require segment reporting on USO services
Access for competitors ¹¹⁶	Remove access regulation for rest mail
	Impose basic access products for rest mail
Ex post price control	No change: Cautious approach in controlling predatory pricing
	Enforced action against possible predatory pricing, fidelity rebates and tying

This section addresses those tools of the current regulatory framework that need in our view specific attention in order to safeguard affordability, availability, choice and quality of the postal service. Table A1 summarises these policy tools and the related options under consideration. For each tool the discussion starts with a description of the current regulatory framework. Then we present alternative policy options per tool. One option is always not to change the regulatory framework (“no change”).

¹¹⁶ Of course, one could consider the additional option to ensure non-discriminatory access to all PostNL tariffs and discounts for competitors. However, we understand that this is not compliant with the Dutch postal policy objectives (which is reflected in the decision to delete Article 9 in the Dutch Postal Act in favour of the application of Article 13a-k).

The appropriateness of each policy option is discussed in light of the scenarios “Back to monopoly” and “Converging networks”. In both scenarios we assume that letter volume will decline substantially (“Digital World”). At the end of each sub-section the discussion is summarised by using coloured balls (borrowed from common traffic lights). A red ball indicates that the policy option would not be appropriate in the sense that it harms the market outcome in the considered scenario. A green ball means that the option would be appropriate in the sense that it supports the better functioning of the postal market in that situation. A yellow ball indicates that the option is “neutral” which means that it neither harms nor supports the considered scenario. Section 4.7 presents the compiled table of the tools and policy options together with results of discussion for each scenario.

A2 Designation of a universal service provider

Figure A1 Designation of a universal service provider: Current postal legislation

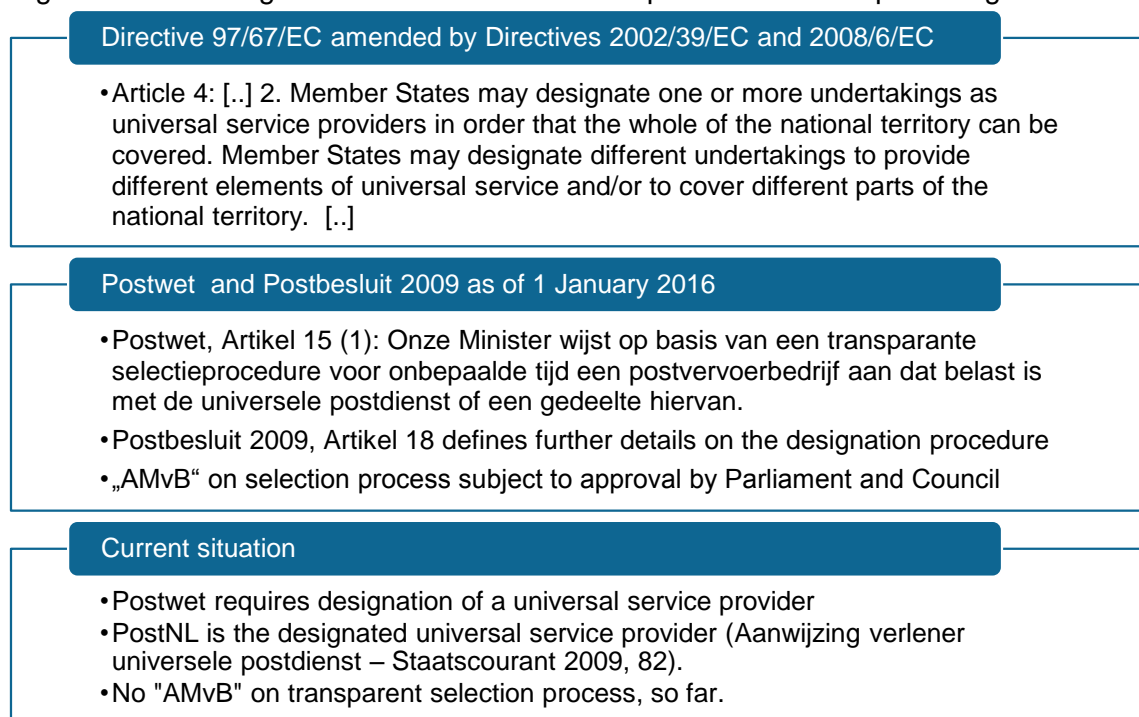


Figure A1 presents the current postal legislation, starting with the requirements as defined in the Postal Directive and how the specific aspect has been implemented in the Dutch regulatory framework.

The Postal Directive requires Member States to ensure that users enjoy the right to a universal postal service, i.e., a continuous, affordable, nationwide, postal service of specified quality. The Member State has the choice to ensure universal service by relying upon one or a combination of three regulatory mechanisms: reliance on market forces, designation of one or more universal service providers (USPs), and public

procurement of postal services. The Directive leaves it to the Member States how to ensure this right, with or without (“may”) designation of “one or more undertakings as universal service providers” (Article 4, paragraph 2 Postal Directive). Not designating a universal service provider per se does not exclude the possibility to designate one for specific universal services, or subsets of universal services.

In the Dutch regulatory model the designation of one or more postal companies to ensure the universal postal service is possible. Designating several providers would require the development of a procedure how to select the appropriate postal operator(s).



A2.1 No change: Keep PostNL as designated USP

Within the current regulatory framework only one postal operator, PostNL, is designated to provide all universal postal services (for an indefinite period).

Today, PostNL is the only organisation in the Dutch postal market that currently provides all postal services (letter and parcel services, national and international postal services). Moreover, it is the only company with a nationwide, dense collection network of collection boxes and postal outlets. Finally, the regulation of universal postal services (to ensure affordability, accessibility and an appropriate level of quality of service) would be facilitated because only one company would be subject of regulatory control.

Moreover, PostNL is the only supplier that offers letter services to consumers which requires a dense network of collection points. While competition in this segment appears unlikely it is emerging in the segment for consumer parcels by other parcel and express operators with nationwide collection and delivery networks. As designated universal service provider PostNL benefits from the VAT exemption because consumers as end-customers are not able to deduct VAT. This could distort competition in the consumer parcel segment.

The policy option would be possible to ensure the provision of universal postal services in both scenarios, “Converging networks” and “Back to monopoly”. While it is not urgently needed in the scenario “Converging networks” because the market solution would be more appropriate (see Section A2.3) it would be the most appropriate instrument in the scenario “Back to monopoly”. In this scenario regulation has to replace the missing market incentives particularly for small postal users, notably consumers, that are most vulnerable.

Appropriateness of the policy option	Back to monopoly	Converging networks
“No change: Keep PostNL as designated USP“		

A2.2 Designate more than one postal operator as universal service provider

This option complies with the current regulatory approach in the Netherlands. The Ministry could assign one or more postal operators to fulfil the universal service obligation. This means that independently on the market situation there would be always at least one company responsible to provide universal service. The question is whether it would be economically reasonable to designate more than one postal operator.

As already highlighted, PostNL is the only postal operator that currently provides all postal services and manages a dense collection network. As “multi-product” company PostNL benefits from economies of scale and scope in the provision of letter and parcel services. Moreover, PostNL has already proven that it is able to flexibly organise collection and delivery of letters and parcels by using the available networks which facilitates the combined provision of all universal postal service in a more cost-efficient way than “stand-alone” competitors in the letter and parcel market.

In contrast, PostNL’s competitors are much smaller (particularly in the letter market) and only active in specific market segments. They are therefore at this moment not able to fully meet the universal service requirements without support of PostNL:

- None of the competitors has a dense network of street letter boxes;
- None of the competitors in the letter market has a network of postal outlets;
- Although competitors in the parcel market have parcel shops which may facilitate collection of letters, letter delivery would not be economically feasible at the current conditions.
- Sandd currently delivers letters only on two days per week.
- Local competitors do not have nationwide coverage and would still need access to PostNL’s network to organise nationwide collection and delivery.

The next question would be which parts of the universal service could be reasonably designated to different postal operators:

- Specific universal services, e.g. the collection and delivery of parcels or registered letters on five days per week and/or
- Specific activities, e.g. the collection and delivery in specific geographic areas (e.g. islands) and/or the collection and delivery of time-critical letters on specific days (e.g. on Wednesdays).

Assigning specific services, e.g. parcel services, would be a conceivable option because of emerging competition in the consumer parcel market. This would require a transparent, non-discriminatory and proportionate designation procedure. However, it is unlikely that PostNL would stop providing letter and parcel services to consumers if not being obliged to do so. What should be PostNL’s incentive to stop providing parcel services to consumers, for example. This would harm its reputation and brand, PostNL would lose substantial revenues (consumer parcels are high-price parcels) and it would reduce economies of scale (in parcel sorting and delivery) and scope (in collection). In that case it remains unclear what would be the benefit for the competitors of being designated to provide specific postal services.

Assigning specific activities (e.g. delivery in specific areas) to more than one postal operator results in additional implementation and transaction costs (compared to the situation that all services are provided by one postal operator) for the Ministry, the postal operators and the postal customers. Again, the Ministry would have to develop a transparent, non-discriminatory and proportionate designation procedure. Secondly, it may affect operations of designated postal operators because they have to cooperate with each other in order to ensure nationwide postal services (in case that specific activities are assigned to different postal operators). Thirdly, senders and recipients would have to deal with different postal operators depending which activities would be assigned to which postal operator.

Finally, the current regulatory approach of universal service regulation is best applicable in case that only one postal operator is the designated universal service provider that is subject to tariff regulation and regulation of quality of service (including accessibility). However, tariff regulation in a more competitive market segment, which is increasingly the case for consumer parcels, could be questioned anyway.

In the scenario “Converging networks” the designation of more than one postal operator by a transparent procedure could be conceivable. In the scenario “Back to monopoly” it would be still possible to designate different universal service providers for consumer parcel services.

Appropriateness of the policy option	Back to monopoly	Converging networks
“Designate more than one postal operator as universal service provider”	●	●

A2.3 Rely on market forces to ensure the universal postal service

This option complies with the Postal Services Directive but does not comply with the current regulatory framework for the Dutch postal sector.

In the EU there is only one Member State that has not designated a postal operator to fulfil the universal service obligation per se: Germany. In case the market does not fulfil the USO satisfactorily, the German regulatory authority (Bundesnetzagentur) can either oblige the market dominant postal operator or, if the provision would result in a financial loss, procure this specific service in a public procedure. In a public tender, the most efficient and reliable bidder that requests the least financial compensation should be selected (see case study). Since the full market opening (1 January 2008) the Bundesnetzagentur has not found it necessary to designate a universal service provider for any services. The instrument “public procurement” has therefore not been applied in practice so far because universal service was provided at sufficient quality by market forces.

Case study A1 Safeguarding universal postal service in fully liberalized postal markets¹¹⁷

At present, Germany is the only Member State in the European Union where postal legislation relies on market forces to provide universal service and introduces public procurement as a mechanism to ensure universal service where the market fails to deliver. This case history outlines how the German Postal Act ensures universal service. Until 1998 German NRA (Bundesnetzagentur) was authorised by the German Postal Act to take measures to ensure the universal service, if not provided voluntarily by postal service operators. Between 2002 and 2008, following a change in government, the universal service obligation was solely imposed on Deutsche Post by the German Postal Act. Since full opening of the postal market on 1 January 2008, there is no obligation on any postal service operator. At present, the incumbent Deutsche Post provides the postal universal service voluntarily. Any dominant operators (at present: Deutsche Post) that intends to discontinue provision of universal service or to provide such services on less favourable terms than specified in the Postal Act, must notify Bundesnetzagentur six month prior to cutting down universal service.

If the universal service is not being adequately provided or if there is reason to believe that such will be the case, Bundesnetzagentur, as a first step, has to publish a statement in its Official Gazette,. As a second step, dominant postal service operators can be obliged by Bundesnetzagentur within one month to provide the specified universal service gap, provided that no postal operator volunteers to provide the gap without compensation. Then, Bundesnetzagentur could oblige the market dominant operator (i.e. Deutsche Post) to provide the service. If the postal operator that is to be obliged to provide the universal service gap provides sufficient evidence that it would suffer financially losses as a result of this obligation, this operator could require compensation. In this case, Bundesnetzagentur shall call for tenders to provide the universal service gap as a third step. Bundesnetzagentur may abstain from public procurement if it does not appear appropriate. In a public procurement, the most efficient and reliable bidder that requests the least financial compensation should be selected. This mechanism to ensure universal service appears consistent with the requirements of the Postal Directive. The procurement procedure must be based on the principles of transparency, non-discrimination and proportionality, thereby guaranteeing the continuity of the universal service provision.

¹¹⁷ WIK-Consult (2009), The Role of Regulators in a More Competitive Postal Market, p. 230.

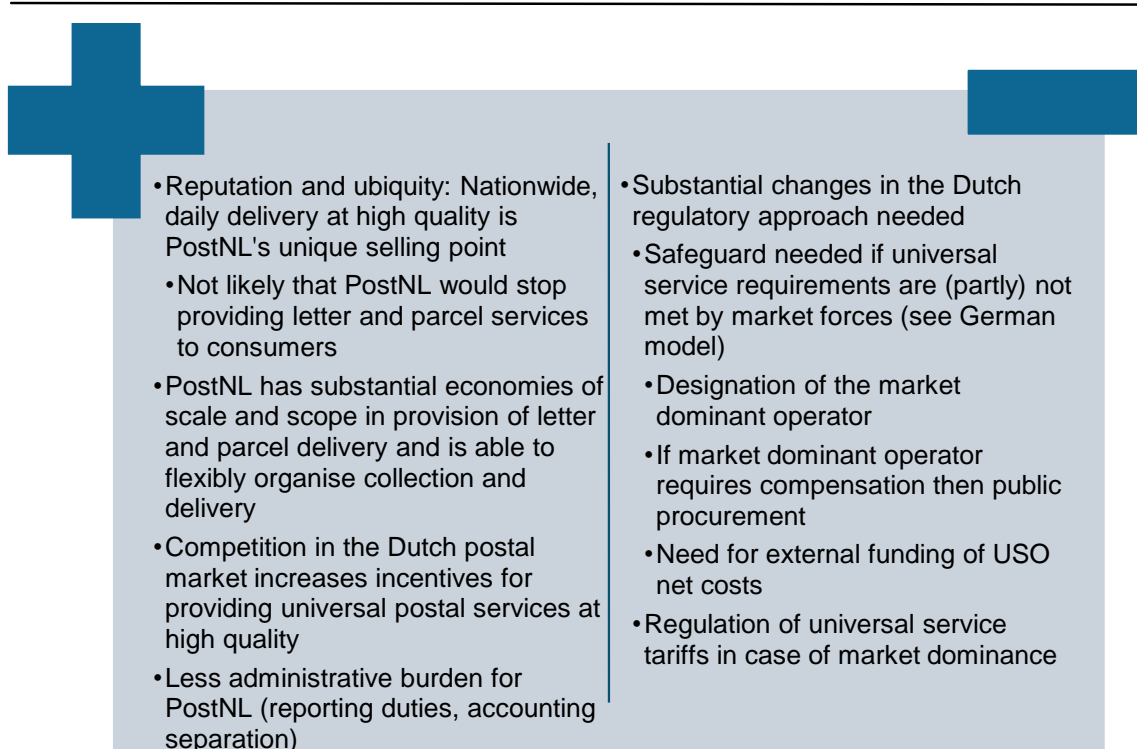
Today, the Dutch letter market is one of the most competitive markets in the European Union despite of being highly challenged by volume decline. For this reason it is conceivable that (parts of) the universal service would be satisfactorily provided by “market forces” without a designated universal service provider. However, market forces require that there is sustainable competition in the postal market to ensure that the incumbent meets customers’ needs. Therefore, “relying on market forces” could be an appropriate approach for single-piece services already subject to competition, e.g. the collection and delivery of consumer parcel services.

In WIK’s view, the provision of collection and delivery services for USO parcels at affordable prices will not be threatened in the next years for the following reasons.

- First, the number of USO parcels as well as the total number of parcels (at PostNL and in the market) has been growing. This reduces average costs in delivering parcels.
- Second, PostNL delivers parcels on six days per week and not on five days as required by the USO. The USO requirement of five day delivery is therefore not binding for parcels. Delivery quality is high: tracked delivery and delivery the next working day is standard for PostNL’s parcel services, including USO parcels. The needs of online sellers and online buyers drive PostNL and other suppliers in the parcel market to keep the quality level high (and prices low).
- Third, affordability of USO parcel services is reflected by stable tariffs for sending single-piece parcels at a level of below 7 Euros during the last five years.¹¹⁸
- Fourth, competitors in the Dutch parcel market, like DPD or DHL, both offer parcel services to consumers at competitive tariffs. Moreover, competition in the Dutch parcel market (which is more substantial than in the Dutch letter market) has not threatened the provision of USO parcel services in any way. That said, it is also unlikely that PostNL would reduce the number of postal outlets/parcel shops because this very dense network is one of its unique selling points compared to its competitors.

¹¹⁸ See PostNL, Price lists 2010-2017.

Figure A2 Reliance on market forces: Pros and Cons





Source: WIK assessment.

Figure A2 summarises the pros and cons of this approach. Implementing this approach could have substantial implications for the future design of universal service regulation. For example, in the current Dutch model, the regulation of USO tariffs is linked to the designation. If no postal company was designated to provide the USO the regulation of universal service tariffs could be linked to the market dominant position (e.g. by applying the approach of significant market power). In that case, regulation of consumer parcel tariffs, for example, could be excluded (if PostNL was not market dominant). Moreover, there could be a need to implement additional safeguards if in some areas or for some customer groups or services the universal service was not provided satisfactorily. These safeguards could be the public procurement of the service in question to find an operator that provides this service at the lowest cost (i.e. lowest compensation needed). Consequently, external funding of (parts of) the universal service obligation could become an issue.

The policy option “Rely on market forces” instead of designating one or more postal operators is the more appropriate the more competitively substantial parts of the letter market are structured. In the future scenario “Converging networks” this would be the case. Moreover, in the parcel market this would be the case in both scenarios. Policy makers could therefore consider not designating a specific postal company for providing

universal parcel services. In the scenario “Back to monopoly” the policy option “Rely on market forces” would still be not appropriate particularly for universal letter services because in that case there would be a substantial risk that PostNL would focus more on operational costs and revenues than on the basic needs of postal users in the provision of universal services.

Appropriateness of the policy option “Rely on market forces”	Back to monopoly	Converging networks
		

A3 Requirements of the universal service obligation

Figure A3 Universal service requirements: Current postal legislation

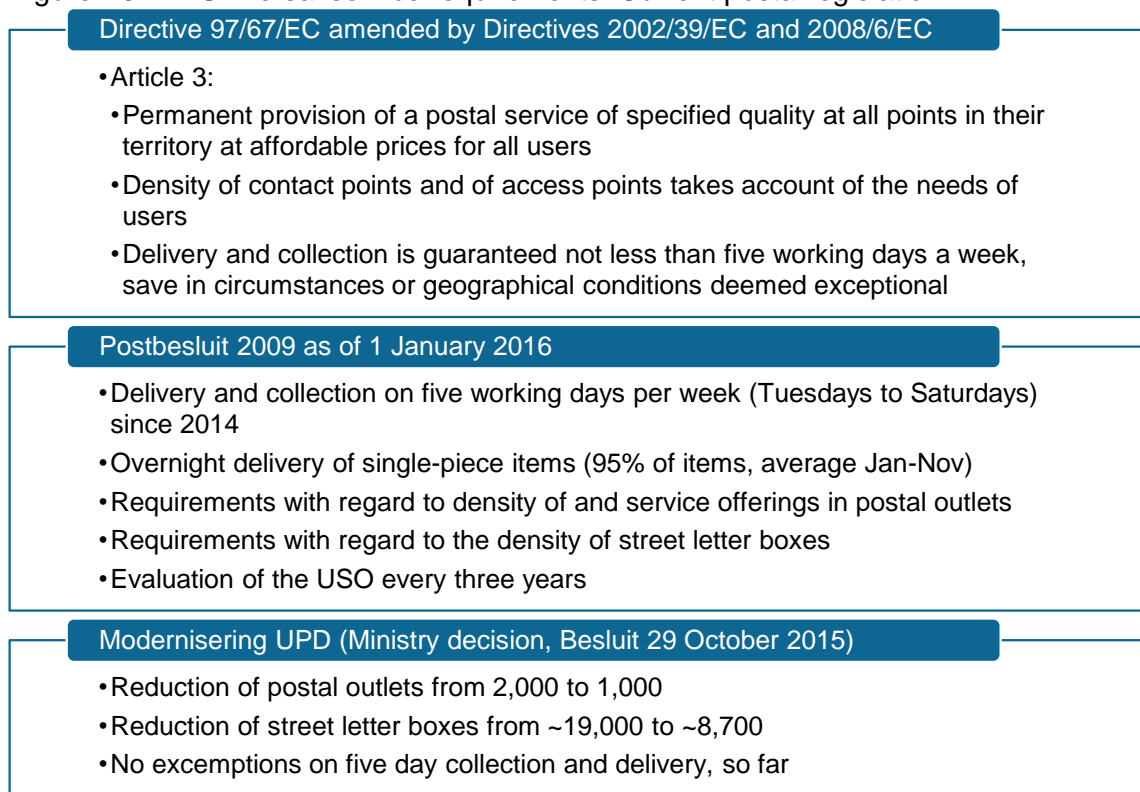


Figure A3 summarises the universal service requirements with regard to accessibility, collection and delivery frequency as well as quality of service.

Basically, the Postal Directive applies the principle of subsidiarity regarding the national universal service requirements. Article 3 only provides the general guidelines for the accessibility of universal services. In contrast to flexible access requirements, collection and delivery requirements in the Postal Directive are more restrictive. It requires the Member States to “ensure that the universal service is guaranteed not less than five working days a week, save in circumstances or geographical conditions deemed

exceptional". With regard to the detailed universal service requirements the Member State shall take steps to ensure that the universal service "shall evolve in response to the technical, economic and social environment and to the needs of users." (Postal Directive, Article 5, paragraph 1).

A3.1 No change: Keep current USO requirements

In Section 3.5 in this report we discussed in detail the sustainability of USO provision in light of volume decline and emerging competition in the Dutch letter market given the current USO requirements. We highlighted that declining letter volume is the major threat for the future affordability of letter services given the USO requirements remain unchanged. Parcel services for consumers and very small business senders are not affected because they are provided in a more competitive environment than letter services. Less demand in single-piece letters and in letter services more generally indicates that the Dutch society's needs for universal letter services have been changing. Keeping the current USO requirements unchanged would therefore mean not to recognize these trends.

As outlined in previous sections, the universal service consists of domestic single-piece letters and USO parcels plus total international import and export mail (letters and parcels). Developments in volume, revenues and costs vary among domestic letters and parcels, domestic and international. Letters are declining, domestic more than international. USO parcels are growing and are increasingly provided in a more competitive environment. In the last two years (2014 and 2015) PostNL reported that USO services were profitable. The cost savings due to the recently, reduced accessibility requirements (less postal outlets and street letterboxes) have not yet materialized (they should do so in 2016 and 2017).

PostNL is pushed by competition and by shareholders to keep costs in line with revenues which have resulted in continuous cost savings and improvements in cost efficiency and flexibility in letter and parcel operations since years. As the same networks are used to provide USO and non-USO services USO services have also benefitted from these cost savings.

Declining USO letter volume results in increasing average costs because some costs are still fixed in collection and in delivery on five days per week. Additionally, the demand for time-critical letter delivery services from business customers has been and will continue declining which may additionally burden USO letter services. Increasing costs to provide the universal services result in higher prices if USO requirements remain unchanged and thus would challenge the affordability of these services. For this reason this policy option would not be appropriate for both future scenarios “Back to monopoly” and “Converging networks” that are both characterized by substantial decline in total letter volume.

Appropriateness of the policy option “No change: Keep current USO requirements”	Back to monopoly	Converging networks
	●	●

A3.2 Allow for more flexible universal service requirements

In 2015, the Dutch Ministry of Economic Affairs relaxed the universal requirements by reducing the collection and delivery frequency from six to five days per week and by softening the density requirements of street letter boxes and postal outlets. Moreover, the decision procedure for adapting USO requirements has been facilitated. They are regulated by Ministry decision and are no longer defined in the Postal Act. This additionally improves the flexibility in adapting universal service requirements based on the obligatory evaluation of the USO every three years.

Case study A2 Examples for flexible universal service requirements

Before 2008, universal service providers had put substantial effort in achieving a high quality level in terms of next-day delivery. A high percentage of domestic and international import letters should be delivered the next working day.¹¹⁹ This has fundamentally changed after 2008, the year of the financial crisis, and for many postal operators the starting year of accelerated letter volume decline. So far, we are not aware that the European Commission has initiated any infringement proceedings in response to emerging practices for having more flexible interpretations of the five-day requirement.

Example Denmark:

In 2016, the individual authorisation granted to Post Danmark A/S as designated universal service provider was adapted.¹²⁰ Letters and parcels have to be collected and delivered on five days per week (Monday to Friday). Ordinary letters (that are subject to ex ante price regulation) have to be delivered within five working days (D+5). Post Danmark introduced in 2016 the “Quickbreve” that is delivered the next working day (on six days per week) and costs 27 DKK (3.63 Euro) for letter with a maximum weight of 100g. The ordinary letter (D+5) costs 8 DKK (1.08 Euro) for a letter weighing up to 50g and 16 DKK for a letter weighing up to 100g.

¹¹⁹ See for example WIK-Consult (2006), Main Developments in the Postal Market (2004-2006).

¹²⁰ See Individual authorisation granted to Post Danmark A/S, Inofficial translation (

Some years ago, the accessibility requirements have been reduced. Instead of applying density criteria (like in the Netherlands) the licence now requires: “The location of the access points [postal outlets] must be determined by the needs of customers, i.e. based on an assessment of places typically frequented by customers, e.g. supermarkets, grocery stores and other retail shops. Similarly, access points offering a full range of services will be located where there is a demand for all the postal services encompassed by the universal service obligation. An additional number of access points offering a full range of services will be located in such a way as to ensure geographical coverage.”¹²¹

Example Italy:

The Italian regulatory authority AGCOM has adapted the universal service requirements for Poste Italiane in 2015.¹²² This change allowed Poste Italiane to introduce a new “ordinary” letter service for consumers and business mailers. The items have to be delivered four weekdays after consignment (D+4). For up to 25% of the Italian population Poste Italiane is implementing an “alternate delivery model”. In selected areas letters are delivered in the first week on Mondays, Wednesdays and Fridays and in the second week on Tuesdays and Thursdays. The new delivery model is being rolled out in three phases: the first started in October 2015 and comprised 256 municipalities in the Lombardy, Piedmont, Friuli Venezia Giulia and Veneto regions, whilst the second phase has been launched in April 2016 and the third in February 2017.¹²³

The number of options that could be considered for further reducing universal service requirements without breaching the Postal Directive appears limited. However, there is still some room of manoeuvre (see Case study A2). Basically, we identified three options that policy makers could consider: (1) Adapting the (physical) accessibility to universal services; (2) Exemptions from five-day collection and delivery and (3) Reducing the transit time requirements for single-piece items (in combination with exemptions from five-day collection and delivery).

(1) After the 2015 decision of the Ministry, PostNL, as designated universal service provider, has already the possibility to reduce the total number of street letter boxes and full-service outlets. The implementation takes one to two years because local authorities and population have to be informed. With regard to postal outlets it is not likely that PostNL will reduce the total number of access points. PostNL has the densest network of outlets which improves PostNL’s competitive position in the Dutch parcel market. More than halving the number of street letter boxes in 2016 and 2017 reduces the fixed costs in collection compared to the 2015 situation. For the future a further reduction and / or a relocation of street letter boxes in high traffic areas (e.g. near or in supermarkets) could be possible. This would require that the density requirements should be reconsidered. Finally, PostNL as well as competing parcel operators have additionally introduced and are going to expand alternative ways to access postal and parcel services. For example, all parcel operators including PostNL of online franking of parcels (at lower cost). PostNL is testing

¹²¹ Ibid., Section 6.

¹²² See AGCOM (2015), Delibera N.395/15/CONS, 25 June 2015.

¹²³ See Poste Italiane, Annual Report 2015.

combined parcel lockers and letterboxes in Almere¹²⁴ and will introduce the “Digitale Postzegel” for consumers that is cheaper than traditional stamps.¹²⁵ The emergence of hybrid solutions (e.g. for sending individualised greeting cards) is another example for circumventing physical access points. In the “Digital World” there are more opportunities to access postal services as only using physical access points.

- (2) Currently, exemptions from five-day collection and delivery have not been allowed to PostNL. PostNL provides parcel delivery services on six days, for some service even on all days per week to meet online sellers’ and, particularly, online buyers’ needs and improve its competitiveness. It is more conceivable that the collection and delivery of time-critical letters may create “circumstances [...] deemed exceptional”. PostNL delivers time-critical and non-time-critical letters jointly on three days per week. The combined delivery results in more items delivered per household on peak days while on off-peak days volume delivered is much lower. The most costly delivery areas are low-density rural areas with long distances between the stops. If time-critical letters decline substantially due to digitisation this also reflects a technology-driven change in customers’ needs (possibly promoted by increasing tariffs). It could be therefore considered to allow exemptions in five-day collection and delivery either in specific regions with very low letter volume or in specific low volume periods (e.g. during summer time). Of course, the exemptions should be closely monitored by the regulatory authority and should not be in contradiction to postal policy objectives.
- (3) Finally, there would be the opportunity to reduce the transit time target for next-day delivery. Currently, 95% of collected single-piece letters have to be delivered the next working day (on average during January to November). There are two arguments to require a less ambitious target.
- Exemptions from five day collection and delivery negatively affect the transit time of single-piece letters and may increase the average transit time.
 - Today, it is common practice that local competitors exchange letters between each other to organise final delivery without using PostNL’s network. Interconnection of postal networks need additional time and less ambitious targets would facilitate potential interconnection and exchange between postal operators.

¹²⁴ See PostNL, PostNL start met innovatieve pakket- en briefautomaat in Almere, press release of 14 October 2016.

¹²⁵ The “Digitale Postzegel” for a 20g letter cost 0.75 Euro compared to 0.78 Euro for a stamped letter. See PostNL, Posttarieven Per januari 2017.

Overall, Dutch policy makers should consider more flexible universal service requirements by taking the technological trends and the changing needs and preferences of the Dutch society into account¹²⁶. The general demand trend in letter communication is not reversible and will emerge independently of the scenarios “Converging networks” and “Back to monopoly”.

Appropriateness of the policy option “Allow for more flexible universal service requirements”	Back to monopoly	Converging networks
	●	●

A4 USO reporting

A4.1 No change: Keep reporting on consolidated USO costs and revenues

Currently, PostNL as the designated universal service provider only reports on total universal service.¹²⁷ ACM has the possibility to receive more information on request which would not be published. The current situation does not allow to regularly inform the interested public more specifically about USO revenues, costs and profits. This could result in a lack of transparency for policy makers when deciding on how to address potential sources for loss-making services.

This is the more important because developments in volume, revenues and costs vary among letters and parcels, domestic and international. Letters are declining, but domestic letters decline more than international letters. USO parcels are growing and are provided in an increasingly competitive environment.

Appropriateness of the policy option “No change: Keep reporting on consolidated USO costs and revenues”	Back to monopoly	Converging networks
	●	●

¹²⁶ This could be subject of the obligatory evaluation of the USO each three years, for example based on a representative postal user survey that also takes the willingness to pay for specific services into account (see for example Rand Europe (2011), Study on Appropriate Methodologies to Better Measure Consumer Preferences for Postal Services, prepared for DG GROWTH (formerly DG MARKT)).

¹²⁷ See PostNL, Financiële Verantwoording universele postdienst 2014 and 2015.

A4.2 Require segment reporting on USO services

More transparency on volume, cost and revenue developments in universal service provision would help to improve transparency on developments and potential sources of losses. This would facilitate policy decisions on future USO requirements. Additionally, more transparency would meet complaints from competitors in letter and parcel delivery on more transparency in USO costs and revenues.

Compared to other Member States, the Dutch definition of universal service for domestic mail is unique because it is much narrower than the definition in the Directive, and in all other EU Member States. For international mail, the Dutch definition is the same as in all other EU Member States. As a result, international mail represents a much higher share in total universal service volume than in other Member States. In 2015, the share of international import letters in total universal service volume delivered by PostNL was approximately 20%, up from 16% in 2010.¹²⁸ Universal service accounts presented by PostNL could therefore be increasingly influenced by the profitability of international import mail. PostNL may incur losses from the delivery of international import mail (including bulk parcels) under UPU terminal dues that are below the cost of delivery, and this may lead to a loss in universal service.

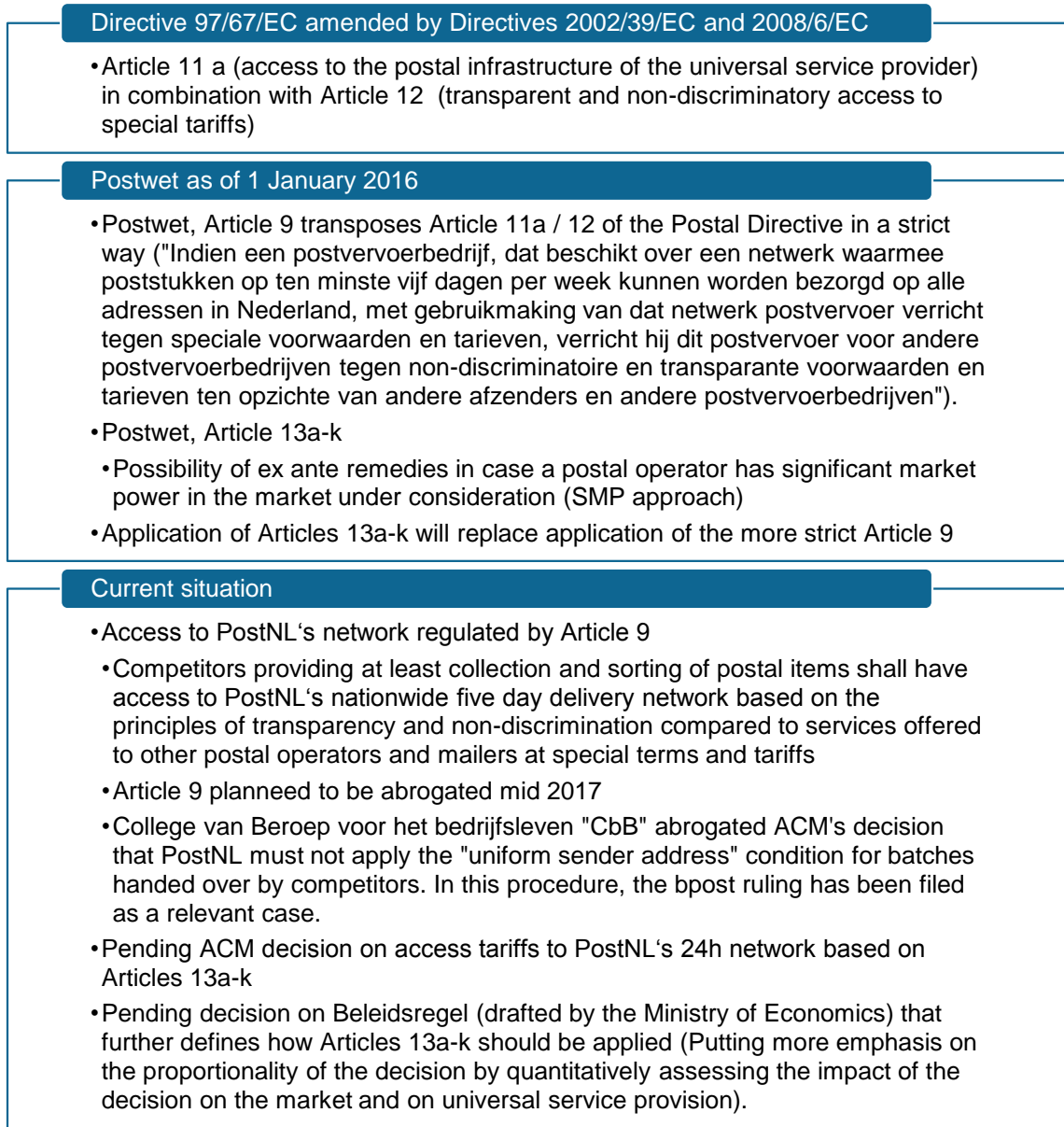
We therefore recommend being transparent about cost, revenues and volume of specific USO segments. For example, the designated universal service provider could separately report on (1) domestic letter services, (2) domestic parcel services, (3) international inbound postal services and (4) international outbound postal services, separately. This would be applicable independently from the scenarios “Converging networks” (in combination with the designation of a universal service provider) and “Back to monopoly”.

Appropriateness of the policy option “Require segment reporting on USO services”	Back to monopoly	Converging networks
	●	●

¹²⁸ WIK calculation based on PostNL (2016), Response PostNL to WIK questions, 19 August 2016.

A5 Access for competitors

Figure A4 Access regulation: Current postal legislation



This section refers to access for competitors for rest mail only. If local and regional competitors and the incumbent postal operator do not agree on access conditions acceptable for both sides this may require regulatory decisions that have to strike a balance among competing considerations including competition in the upstream market (collection and sorting) versus competition in the end-to-end market and entry by similar services versus more innovative entry. The discussions at a stakeholder workshop as well as all persons interviewed for this study also highlighted the importance of infrastructure competition in the Dutch postal market. In its draft decision, ACM also stressed the importance of infrastructure competition as guideline for regulatory

decisions in its draft decision on access to the postal network of PostNL for time-critical letters:

“Effectieve en duurzame concurrentie wordt naar het oordeel van ACM het beste bereikt door voorrang te geven aan verplichtingen die infrastructuurconcurrentie bevorderen. Effectieve en duurzame concurrentie is het beste verzekerd in de situatie waarin postvervoerbedrijven met hun eigen postinfrastructuur met elkaar concurreren. Hierdoor zijn zij minder afhankelijk van het postvervoernetwerk van PostNL, en daardoor beter in staat om een eigen commercieel aanbod aan postvervoer te ontwikkelen en zich te onderscheiden van PostNL. ACM heeft dan ook de doelstelling geformuleerd om met de regulering van de postmarkt infrastructuurconcurrentie zoveel mogelijk te bevorderen.”¹²⁹

A5.1 Remove access regulation for rest mail

This option would imply that Article 13a-k would be removed. Removing access regulation means that PostNL’s current pricing policy for bulk mail would not be affected by any regulatory measure. Of course, it would still be possible that regional competitors and PostNL could agree on access conditions acceptable for both sides by means of negotiations.

“Removing access regulation for rest mail” would mean to solely rely on negotiated access products for competitors. The final business opportunities for regional competitors then depend on the conditions¹³⁰ and prices agreed with PostNL. Less preferential access conditions may increase competitors’ incentives to invest in own delivery infrastructure. Such investment decisions, however, depend on competitors’ opportunities to acquire additional customers and volume.

Generally, less preferential access conditions and prices could limit the potential customer base for competitors to those business mailers that mainly send letters to local / regional destinations. The competitiveness of local and regional players would then be the lower the higher the share of letters delivered to destinations outside their area. Regional postal operators, for example, could hardly compete with PostNL for medium-sized business mailers if there was a significant share of “rest mail”, i.e. for the mail that they collect from their customers but that is directed to areas/addresses that they do not deliver to. This again could reduce the volume that could be handed over to other regional and local operators for final delivery. Overall, this could result in declining market shares of local and regional competitors so that competitors’ letter volume would

¹²⁹ ACM (2016), Marktanalysebesluit 24-uurs zakelijke post, Ontwerpbesluit, p. 15.

¹³⁰ Access conditions include for example latest acceptance time and rules for mail presentation (presentation in bags or trays, pre-sorting, machine-readiness and so on) to ensure next day delivery nationwide.

decline more than the market volume possibly resulting in potential market exits of some or many of these competitors.

In the scenario “Converging networks”, access to PostNL’s network could still be relevant. As long as local and regional competitors do not have nationwide coverage, they need access to an existing postal network for their “rest mail”. In this scenario infrastructure competition would successfully emerge in letter delivery where local and regional competitors would cooperate with each other. In this scenario the importance of access to PostNL’s network would therefore decline with increasing coverage of the Netherlands by competitors’ own delivery infrastructure and would therefore simultaneously reduce the competitors’ dependence on the product portfolio of the incumbent. In the transition period to this scenario, however, regulated access for rest mail could be necessary to protect infrastructure competition.

In non-time critical delivery access would not be an issue in the scenario “Converging networks” because there would be two competing networks. If local and regional competitors decided to enter the non-time-critical delivery segment they would have the choice between two postal companies offering nationwide delivery services in this segment. In that case bilateral negotiations would be more useful (and most likely successful).

In the scenario “Back to monopoly” competition would have vanished for time-critical delivery and there would be no need for access regulation for rest mail in this segment.

Appropriateness of the policy option “Remove access regulation for rest mail”	Back to monopoly	Converging networks
	●	●

A5.2 Impose basic access products for rest mail

Imposing access products means that a company would be obliged to provide access to certain network components determined by the regulator for a fee also determined by the regulator.

Inn general downstream network access can be useful to competitors for two reasons:

- First, a company can focus on merely performing pre-sorting and transportation services thus leaving final delivery to other postal operators including the incumbent (consolidators).
- Second, postal operators that start their operations in one region or choose to provide local services only, will reasonably want to handle all the mail received from their customers. Since they are not in a position to deliver all of this mail, they need access to the incumbent’s postal network for delivery of the “rest

mail". Rest mail consists of those items consigned to PostNL for final delivery i.e. outside the competitor's (or its cooperation partners') delivery network(s).

Basic access products should be as simple as possible. Access conditions should be transparent and simple and should be applied in a non-discriminatory way to all postal operators. Imposing basic access products by the regulator should be the measure of last resort, i.e. such obligations should be imposed only after negotiations between the market dominant operator and competitors have failed. In that case each party has the right to go to ACM to decide on imposing access products.

Depending on the access conditions and tariffs, local and regional competitors would retain the potential to win more market share supported either by intermediaries that collect mail from business customers nationwide and organise delivery via competitors' and incumbents' network and/or by own acquisition of customers. It would enlarge the potential customer base and reduce handling costs compared to the policy option "Remove access regulation".

There would also be some risks that depend on the level of access tariffs and their relation to the incumbent's retail tariffs. Local competitors need access at conditions that do not hamper their core business and leave enough opportunities for growth. Of course, they seek for opportunities to get access as cheap as possible because this helps to offer the service at a more competitive price to its local business customers and/or to earn some additional income. However, this type of income should not be the major source for the financial viability of local and regional competitors (and this is not what competitors in the Netherlands are aiming at presently). If access tariffs were lower than competitors' average delivery costs, it would be economically reasonable to consign the total volume to the incumbent instead of delivering themselves.

The often cited argument of "cherry picking" is not applicable to the Netherlands. In that case competitors would choose those areas with low delivery costs to start delivery services (usually areas with high population density). In contrast, Dutch local and regional competitors mainly cover semi-urban and more rural areas in the Netherlands. Moreover, the population density in the Netherlands is relatively high in many areas of the country. This also explains why the Netherlands is the only country in Europe where, with Sandd, a competitor has successfully established a nationwide letter delivery network.¹³¹

Imposing basic access products for rest mail by the regulator could affect PostNL's pricing policy for domestic bulk mail. International experience shows that it is very difficult to effectively exclude business mailers from using "wholesale" access products

¹³¹ By contrast, for example, the major competitor in Sweden, Bring Citymail, mainly targets the densely populated Southern cities. Both, Sandd and Bring Citymail have a similar business model with delivering pre-sorted letters on two days per week.

if they are more preferential than comparable retail products. In Germany and the UK, business mailers as well as consolidators use the same “access” products.¹³² In Slovenia, some business mailers registered as postal operators to benefit from low access tariffs (see case study A3). Introducing new access products by regulatory decision could consequently have a similar effect as directly regulating retail prices for business mailers. This could call for rebalancing of its pricing model. Price increases for some customers could result from such tariff re-balancing and could promote the switch to slower letter services or to digital communication channels. However, the final impact on PostNL’s pricing policy depends on the conditions and the tariff level of the basic access products.

Case study A3 Access for competitors in Slovenia¹³³

Under the Postal Services Act (Article 32) in Slovenia, providers of ‘interchangeable postal services’ must be given access to the universal postal service provider’s network. The universal postal service provider (Pošta Slovenije d.o.o.) must conclude an agreement on access with providers of interchangeable postal services at their request, regulating the manner and conditions of accessing the postal network, cost-oriented price of the access, charging and invoicing, and other issues related to access.

Following complaints from alternative postal operator that wanted to offer mail consolidation, the national regulatory authority APEK had ordered prices for these access service at discounts from 16.8% up to 48.4% compared to the public single-piece tariff in 2010. These discounts were available only to providers of ‘interchangeable postal services’ but not to senders of bulk mail directly. These access prices thus represent preferential tariffs for other postal operators. According to Pošta Slovenije, some business mailers have registered as postal operators (providers of interchangeable services) following APEK’s access decision in order to have benefit from those preferential rates.

In the scenario “Converging networks” infrastructure competition would have successfully emerged in letter delivery where local and regional competitors cooperates with each other. This requires that they have to further develop the cooperation to become more professional in terms of operations (interconnection, exchange of letters, quality control) and contracting (agreed service levels and pricing) to successfully compete with the incumbent. Their main goal should be to deliver as much volume as possible within their own delivery networks disregarding where the items come from (as long as the price they get is covering their costs). Mail collected and sorted by intermediaries (e.g. Intrapost) or produced and prepared by mailing houses facilitates acquiring letter volume from business mailers nationwide. The importance of these basic access products would decline with increasing coverage of the Netherlands by

¹³² See Dieke, Alex; Petra Junk and Martin Zauner (2010), Netzzugang und Zustellwettbewerb im Briefmarkt, WIK Discussion Paper No. 336 and Martin Zauner (2010), Upstream Competition and Retail Price Regulation: Lessons from Downstream Access Models, Presentation held at 12th Königswinter Seminar, 22-24 February 2010 „Regulation and Business in a Changing Postal Market”.

¹³³ This case study was published in WIK-Consult (2013), Main Developments in the Postal Sector (2010-2013).

competitors' own delivery infrastructure and would simultaneously reduce the competitors' dependence on PostNL's product portfolio.

Additionally, in a competitive environment, PostNL may have a strategic interest to offer access products voluntarily. In Germany for example, Deutsche Post was first obliged to introduce new access products (in 2001). After full market opening in January 2008, Deutsche Post voluntarily increased the discounts for upstream services and increased discounts further after the loss of the VAT exemption on bulk mail (in 2010), and yet again after each increase of the single-piece tariffs (see case study A4). Assuming PostNL behaves like Deutsche Post, a balanced procedure to implement basic access products should be implemented that should first be based on negotiations between PostNL and competitors. Imposing access products by ACM decision should only be the instance of last resort if both parties did not agree on access conditions and prices.

Case study A4 Access for competitors in Germany

In Germany, market dominant postal licensees are obliged to grant competitors access to portions of its network at rates considered reasonable and competitive by the NRA. In its first access case in 2000, Bundesnetzagentur (formerly RegTP) determined lawful rates for downstream access to the network of Deutsche Post AG (DPAG), the German universal service provider. Bundesnetzagentur adopted the principle that the price for access to DPAG's network should be set at the retail price for the postal service at issue less avoided costs. The interpretation of German postal law did not allow for competitors' access within the reserved area. This limitation effectively barred consolidators from access to discount tariffs that DPAG offered to large customers. In February 2005, the German competition authority—taking on a case initiated by the European Commission (DG Competition)—obliged DPAG to provide downstream equal access to both mailers and consolidators. Following a provisional approval of the decision by administrative courts in April 2005, many consolidators have reached access agreements with DPAG under the terms determined by the NRA.

In 2003, Bundesnetzagentur adopted a price cap regime for many of DPAG's services; this regime incorporated the principles of the earlier access case. Compared to retail tariffs, the highest discounts amounted to 21% in 2007, the year before full market opening. After full market opening bulk mail tariffs (including the access products) have been subject to ex post control. Since then Deutsche Post has substantially increased the discounts for access products to maximal 45% (in relation to the single-piece tariff).¹³⁴ In absolute figures the access tariffs remained fairly stable between 2007 and 2016 (including VAT of 19% for the bulk mail products; the VAT exemption ended in 2010) while the consumer tariffs for the 20g letter has increased from 0.55 to 0.70 Euro during the same period.

Limiting infrastructure competition was one important incentive for Deutsche Post's strategy to voluntarily offer basic access products for competitors and customers in order to keep volume and at least some revenues in the network but with reduced margins. In Germany, the market share of competitors (in volume) have increased very slowly between 2010 and 2015 from 10.2% to 13.2% although the German letter market is much less challenged by digitisation than the Dutch letter market.

¹³⁴ See Deutsche Post AG (2015), Preismaßnahmen zum 1. Januar 2016, 21 October 2015.

In the scenario “Back to monopoly” the situation would be different: PostNL would be the only postal company providing letter services and would not be necessary anymore to impose access products to provide competitors an opportunity to consign their rest mail to PostNL.

Appropriateness of the policy option “Impose basic access products for rest mail”	Back to monopoly	Converging networks
	●	●

A6 Ex post price control

In the European Union, there is an increased activity of national competition authorities that react to abuse of market power, primarily with respect to rebates seeking to impede entry of competitors or exclude new entrants.¹³⁵ The increase in abusive rebate practices by incumbents is the result of emerging competition following sector liberalisation. It reflects intensified competition in many countries (as in the Netherlands). Competitors in end-to-end delivery challenge the incumbents’ volumes and revenues, and in some countries, consolidators put pressure on the incumbents’ margins. Reacting to those pressures, incumbents seek to protect revenues by price-discrimination between different groups of customers and competitors, and competition authorities have to deal increasingly with complaints from competitors.

In the Netherlands, end-to-end competition has developed for more than ten years, and despite continuing dominance by PostNL, the market is one of the most competitive postal markets in Europe. Overall, Dutch authorities have taken a fairly liberal approach by European standards: there has been effective market opening, and the regulatory and competition authorities have broadly taken a hand-off approach that is more passive than in other EU Member States, relying more on free market forces.¹³⁶

Our research for this study has revealed an increased interest by ACM, the regulatory and competition authority in allegedly anti-competitive practices, and increased complaints from competitors in both segments for time-critical and non-time-critical delivery since 2012.

¹³⁵ See WIK-Consult (2013), Main Developments in the Postal Sector (2010-2013) and WIK-Consult (2009), The Role of Regulators in a More Competitive Postal Market; both studies commissioned by the European Commission.

¹³⁶ See WIK-Consult (2013), Main Developments in the Postal Sector (2010-2013), p.67-74.

A6.1 No change: Cautious approach to controlling predatory pricing

This option would mean to continue the current hands-off approach to postal market regulation under competition law. This approach would rely primarily on unregulated market forces, and less on active or retro-active regulation by ACM.

Assessment

Arguments in favour of continuing a cautious approach to applying competition law ('pros'):



- Legal certainty. Market players have taken decisions based on past practice. Changing accustomed practices would only be justified in this respect if market conduct has changed significantly.
- In liberalised industries, cautious approaches to applying competition law generally benefit incumbents, and thus have a positive effect on incumbents' profitability, and their ability to provide universal service in the short run.

Arguments against continuing a cautious approach to applying competition law ('cons')

- There is a risk that critical pricing strategies by PostNL lead to reduced choice and higher prices for mailers.
- Selective rebates in public tenders by PostNL, and possible tying strategies may have an adverse effect on existing competition in the market, and stop potential competitors from entering the market.

At present, there is a risk that existing levels of competition in the postal market may get weaker in the future due to falling volumes and intense price competition. The current situation may lead to market consolidation and less competition, and thus to the scenario "Back to monopoly". This would reduce choice to mailers and lead to (additional) price increases over the medium and long term.

Given these risks, maintaining current hands-off approaches would only seem appropriate if there is no realistic hope to competition to persist in the Dutch postal market (scenario "Back to monopoly"). By contrast, the approach seems inappropriate in the more competitive scenario "Converging networks", see table below.

Appropriateness of the policy option	Back to monopoly	Converging networks
"No change: Cautious approach to controlling predatory pricing"		

A6.2 Enforced action against possible predatory pricing, tying and fidelity rebates

This option means that ACM would scrutinise potential abusive pricing practices more vigorously, applying its powers under competition law (in line with the European case law exemplified below). To prevent anticompetitive pricing strategies ACM should be informed about individual contracts and the pricing behaviour of the incumbent postal operator on a regular base. In case of individual contracts, no side (neither the incumbent nor the customer) has an incentive to provide this information voluntarily.

Sections 3.3.2 and 3.3.3 conclude that the business models of local competitors as well as the business model of Sandd in part depend on the strategic behaviour of PostNL. PostNL has a market share between 80 and 90% in the Dutch letter market (only domestic letters). Due to its size PostNL has strong economic advantages because it benefits from substantial economies of scale and scope in best combining the available delivery networks (for letters, parcels and unaddressed items). As a result of PostNL's persistent market dominance, competitors in the Dutch letter market are vulnerable to abusive behaviour of PostNL, for example

- There is a risk of predatory pricing in single contracts, including offers submitted in public procurements by public mailers.
- Long-term contracts that offer discounts related to pre-specified volumes can have tying effects. By consequence, mailers would be dis-incentivised to switch some volume to competitors in order to keep the volume rebate. Outside the Netherlands, rebates based on annual volumes have been considered as tying rebates by some authorities (see below). Tying effects would be even stronger for multi-annual rebates (if there was evidence for such rebates).¹³⁷
- There is a risk of anti-competitive bundling if volume discounts refer to total volume and not to volume of specific products. Critical rebates in this respect include rebates for combined sales of letters and parcels, or combined sales of different letter products, e.g. time-critical and non-time-critical letters. Such rebates can be used to leverage market power from one product market to another, and have been considered as fidelity rebates by some authorities outside the Netherlands.

¹³⁷ Research for this report indicated that PostNL currently applies rebates based on multi-annual volume discounts, see for example PostNL, Postal rates January 2016, p. 14.

The following examples of cases by European competition authorities or postal regulators illustrate the diverse issues presented in acting against abusive pricing:

- *Impulspost (2016)*¹³⁸: Deutsche Post introduced a new, inexpensive product for direct mail used to acquire new customers solely, called “Impulspost”. This service was offered at prices much lower than the standard direct mail product. The regulator Bundesnetzagentur requested Deutsche Post to stop offering “Impulspost” at this low price because it is below the relevant cost standard.
- *Forbruger Kontakt/ Post Danmark I*: The competition authority condemned Post Danmark in 2004, having found selective and discriminatory rebates for unaddressed mail to large customers (supermarkets). The price was above average incremental and below average total costs. The Danish high court confirmed the decision in 2007. On 27 March 2012, the CJEU replied to the Danish Supreme Court (Case C-209/10) that selective below-cost pricing was not prohibited per se, but the actual or likely exclusionary effects should be proved. In 2013 the Danish Supreme Court overturned the High Court decision because of no sufficient evidence of exclusionary effects.
- *ASEMPRE/Correos (VATC/2458/03)*: An association of competitors in letter delivery has complained about incumbent Correos allegedly violating commitments from an earlier decision related to predatory prices (discounts to large customers). The competition authority CNC condemned Correos with a fine of 4.8 million Euros in 2011
- *TNT/Poste Italiane A413*: In 2011, acting on a complaint by TNT Post Italia, incumbent Poste Italiane was found to apply predatory prices by the competition authority, and was fined a penalty of 39.4 million Euros.
- *Post Danmark A/S v Konkurrencerådet (Post Danmark II)*: Following a complaint lodged by Bring Citymail, the competition authority Konkurrencerådet found, in 2009, that Post Danmark had abused a dominant position on the market for the distribution of bulk mail by applying, in 2007 and 2008, retroactive rebates in respect of direct advertising mail which had the effect of tying customers and ‘foreclosing’ the market, without being able to substantiate the efficiency gains that might have benefited consumers and neutralised those rebates’ restrictive effects on competition (target/fidelity rebates).
- *Sandd/ PostNL (ex TNT) 6207*: In 2012, NMa (now ACM) rejected Sandd’s complaint (lodged in 2009) that PostNL had abused its position on the Dutch postal service market. Sandd had claimed that competition was being distorted

¹³⁸ See Bundesnetzagentur, Beschlusskammer 5 (2016), BK5-16/012, Verwaltungsverfahren wegen nachträglicher Überprüfung nicht genehmigungsbedürftiger Entgelte für das Produkt „Impulspost“.

because of, among other reasons, PostNL's subsidiary Network VSP's alleged 'free' use of its parent's network. The NMa found no evidence that PostNL's network was used at prices below cost. In addition, the market situation in 2012 was different from the one in 2009, since Network VSP no longer delivers addressed mail.¹³⁹ The appeal of ACM's decision by Sandd failed in September 2013.¹⁴⁰

- *Market Court Bring CityMail/Posten, 2011/14*: In a decision by Swedish Market Court of 2011, Sweden Post was ordered to discontinue a retroactive rebate for addressed direct mails and non-priority (economy) letters and non-priority (economy) periodicals. Sweden Post was fined SEK 100 million (approximately 10.8 million Euros) to cease applying these loyalty discounts.

Competition law would be appropriate to deal with potentially emerging complaints for two reasons: First, the standards for identifying predatory pricing, tying and fidelity rebates are not unique to the postal market, and should indeed be consistent with ACM's practice in other industries. Second, powers relating to access to information (from both suppliers and buyers) are generally more extensive under competition law, and so are enforcement powers.¹⁴¹

Arguments in favour of enforcing action against anti-competitive pricing ('pros'):

- It would foster undistorted competition in the postal sector,
- It is established practice in competition law (including outside the postal sector) to conduct reviews of critical pricing elements.
- While pricing standards in postal legislation appear clearer and more ready to be applied to price caps (or other review of maximum prices), competition law standards and procedure appear more appropriate to ex-post review of discounts (or minimum prices).
- ACM is well placed to review rebate policies since it is both, postal and competition regulator.

¹³⁹ In 2011, PostNL decided to shut down the low-budget addressed mail delivery activities of its subsidiary Network VSP (see Section 2.1.2). See NMa (2012), NMa rejects Sandd's complaint: no abuse by PostNL, 22 May 2012.

¹⁴⁰ See Rechtbank Rotterdam d.d. 26 September 2013, ECLI:NL:RBROT:2013:7337.

¹⁴¹ This general assessment relates to analysis of postal legislation in the Netherlands, and WIK's research and experience with application of Art. 101 TFEU, and national competition law in many European countries. We have not performed any legal analysis of competition law in the Netherlands.

Arguments against enforcing action against anti-competitive pricing ('cons'):

- Regulatory uncertainty from parallel application of postal and competition law by ACM.
- Effect of retroactive action under competition law is slower than effect of standards under postal legislation.

Strict enforcement of competition law standards appears necessary as long as there will be notable competition on the postal market, and PostNL continues to be dominant (i.e. in scenario "Converging networks"). In the scenario "Back to monopoly" with PostNL as the only postal operators competition complaints would not play any role (no competition – no complaints). Therefore, this option would not have any impact in this scenario.

Appropriateness of the policy option	Back to monopoly	Converging networks
"Enforced action against possible predatory pricing, tying and fidelity rebates"	