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Future Development of the Postal USO Team
Ofcom
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Dear Sir

Whistl response to Call for Input on The Future of the Universal Postal Service

Whistl thanks Ofcom for the opportunity to contribute to this important debate with its Call for Inputs on The Future of the Universal Postal Service. This response has been prepared by Andrew Goddard, Managing Director Mail on behalf of Whistl. It is non confidential and may be published in full at Ofcom's discretion.

Introduction

The discussion of the USO is of fundamental importance to us, our customers and all other Access Operators because the network used to deliver USO products is the same network used to deliver Access products and is also largely the same network that is used to deliver Royal Mail parcel services.

Any changes to the network that delivers Royal Mail traffic is very likely to have significant and lasting implications for both Access and parcel traffic and these need careful consideration as they will have far reaching effects on the market as a whole.

The reason we say that is because c86% of all items that are delivered by Royal Mail's delivery network are non-USO items and c70% of all letter volumes are sent using Access. The revenues from Access and non-USO products underpin the delivery network that is used to provide the USO. Any changes which are detrimental to the Access market and the market in other non-USO products will not just affect those markets, but will rebound to be similarly detrimental to USO services.

In our response to this Call for Input, we have included the results from our own customer survey, the conclusions that we have drawn from it, our proposals for next steps and the accompanying Annex sets out the background for our views. Whistl and its posting customers make little use of USO products and so we leave it to other stakeholders to comment on the detail of the USO specification itself.

Customer Survey

Whistl is the largest Access Operator, delivering c58% of the Access volumes to Royal Mail from a varied and diverse bulk mail and SME client base.

One of our concerns in relation to the Call for Input is that, whilst Ofcom has conducted extensive user needs research for consumers and SMEs on USO products, it has not done the same for bulk mail posters.

As we stated in the Introduction, Access helps to underpin the entire USO delivery network and by way of comparison in 2022/23 USO volumes were just 1.488 billion items whilst Access volumes amounted to 5.126 billion items. We have set out below, as one of the next steps, that Ofcom carry out the necessary work to survey the requirements of bulk mail posters.

In the absence of any survey by Ofcom, we have conducted an inhouse, online survey with a sample of clients from across our customer base to gauge their reaction to the discussion topics in the Call for Input.

Customers were chosen for the survey from 12 business categories in order to represent as wide a cross section of organisations as possible. The customers included a mixture of those who regularly send business mail, advertising mail and ecommerce items. After the online survey, there were follow-up discussions with all participants.

Responses were provided by 56 customers, representing 44% of our annual postal volume which equates to around 1 in 4 of all Access letters. Whilst this does not represent the majority of mail items sent in a year, we believe the results are indicative of customer sentiment in the market.

The key findings of the survey are as follows:

- When asked about support for the options set out in the Call for Input:
 - 46% of customers said that they were not supportive of any of the options put forward
 - 39% of customers said they would broadly support the removal of Saturday deliveries
 - 11% of customers said they would be supportive of reduced frequency to 3 days a week
 - 2% of customers said they would be supportive of a move to 2.5 days a week
 - Only 4% of customers were supportive of the removal of D+2 as a delivery speed
- 93% of customers reported delivery frequency per week as very important (64%) or important (29%).
- 96% of customers reported delivery speed as very important (57%) or important (39%).
- When asked about the factors that are most important / important and are most likely to influence future postal volumes
 - 85% rated price
 - 52% said service reliability

The research and follow up conversations show that customers are generally not supportive of the changes put forward for discussion in the Call for Input; they are content with the D+2 and D+5 options currently available to them, although they are deeply concerned with Royal Mail's current quality of service and continuous price increases.

The survey also shows that there is a significant base of customers for whom the proposed changes would be entirely unacceptable and that they would find alternatives to post if the reductions in the USO were introduced.

Next steps: Whistl requests of Ofcom before proposals are finally issued

It is imperative that Ofcom understand the objections and requirements of those organisations which find unacceptable the proposals for change to the USO. This can only come through proper structured research and analysis and the findings built into any further proposals for change that may be put forward in due course.

The key message from all other customers is that they would prefer not to have any change to the current service offerings, but if there must be change, then they would expect to share in the benefits of change through certainty on Royal Mail pricing and through greater reliability of the service from Royal Mail.

Therefore, before any changes to the USO are finalised, we propose that Ofcom carry out the following:

1. A comprehensive, representative and quantitative market research piece on the user needs of bulk mail posting customers to match the existing levels of research in the consumer and SME markets.

Ofcom's primary duty relates to the financial stability and affordability of the USO. As we have stated above, Whistl's bulk mail customers do not use USO services but the revenues that are generated by Access underpin a significant portion of the USO network costs.

The needs of bulk mailers are many and varied as will be their views on the proposals set out in the Call for Input. It is vital that Ofcom understand the consequences of any potential changes to ongoing volumes and Ofcom will only be able to assess this properly if they conduct appropriate research to quantify the impacts.

The key question for Ofcom to answer will be to determine the proportion of letter mail volume that is time-sensitive and which may be lost to other media as a consequence of the proposed changes and what impact this would have on the finances of Royal Mail.

Following the Call for Input should Ofcom, Royal Mail or Government conclude that a change in delivery days is needed then customers will want to understand the quid pro quo; what benefits they could expect to receive from the changes.

2. A full refresh of the Quality of Service regime with the introduction of a timely, relevant enforcement regime and the inclusion of Access in the measures

The existing Quality of Service (QoS) regime was not tested when Royal Mail were broadly hitting their QoS targets in the years prior to 2020. Since the Covid-19 pandemic this position has changed and QoS is now consistently well below the target levels set by Ofcom. Despite Ofcom's ongoing efforts and enforcement actions, the market has seen little improvement in QoS over the last two years.

Ofcom has acknowledged that reliability is a key factor for users of USO services and the residential trackers show that trust in post is falling as a consequence of a lack of QoS reliability. We believe that the same will be true for business posters when Ofcom research the needs and attitudes of this group. Posters need to have confidence in the reliability of drop date of their items and this is currently lacking due to poor QoS.

Many important items, such as NHS letters, communications from Local and National Government, and utility and financial services providers, are not USO items but are delivered by Access. It seems odd that these items are not included in Ofcom's monitoring regime, given their importance and the scale of the volume of items. With large volumes and high levels of barcoding on bulk mail it may well be that ongoing monitoring could be made more cost efficient, made available with an improved level of granularity and provided faster than the existing method.

Sadly, there is also a need to review the enforcement aspect of QoS. The current deterrent is simply inadequate and is not encouraging or driving the proper behaviour. Ofcom need to find a more proportionate and relevant deterrent that will ensure that Royal Mail meets its QoS obligations for the delivery products that are proposed as a result of this review. Ofcom could usefully explore the effect of imposing regulation that requires the payment of meaningful levels of compensation and linking price increases to achieving realistic but challenging QoS targets.

Frankly customers would say a major overhaul in this area is needed with or without a change in delivery, but if change is going to come, it is imperative that these areas are considered as part of the change.

3. A mechanism to ensure the benefits of the change are realised by Royal Mail and that customers are provided with appropriate pricing at start and enhanced pricing confidence.

If customers are to be asked to accept a degraded service in order to allow Royal Mail to realise some operational cost saving benefit, then customers will naturally expect to be charged a lower price for the new degraded service based on (a fair share of) the efficiencies that Royal Mail expect to obtain.

However, trust in Royal Mail's ability to deliver these cost savings is low amongst posting customers based on previous experience. The overarching concern is that Royal Mail would - yet again - fail to deliver the savings envisioned and then use their commercial freedom to increase the prices once again to compensate for their lack of success. Customers would then be left with a demonstrably poorer service but at a higher cost: hardly an attractive position for them.

The London forum heard that customers would welcome some form of price control to provide greater confidence in the cost of using the medium going forward. Ideas were put forward of the possibility of using an RPI price cap to drive real term efficiencies (for both USO and Access services) and implementing a mechanism linking QoS attainment to the ability to increase prices for both services. We would encourage Ofcom to explore these and other meaningful compensation options.

This is an important debate with significant implications, and we look forward to working with Ofcom and other industry stakeholders to assess the best way forward. As a first step we urge that the needs of business users that account for 70% of postal volume in the UK are fully understood before proposals are made on the future design of the USO.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Andrew Goddard', written over a light blue horizontal line.

Andrew Goddard
Managing Director Mail
Whistl UK Limited

Annex: Background

We have provided this background section to give some context of our views, and those of our customers, and so that we have a proper discussion of change which deals with the failures of the past.

Royal Mail

Much has been made of the mail volume reductions during Ofcom's tenure as regulator, and the decrease in volumes is cited as one of the principal reasons for the need for reform of the USO. Further, we are told by Royal Mail that volume reductions and delivery point increases have combined to make the efficient delivery of the USO untenable.

However, these changes are not a sudden revelation to the market. Royal Mail has been quite accurately forecasting the volume decline for the last 10 years. Indeed, all postal operators have known about this trend and looked to take steps to improve costs and efficiency to ensure that they have sustainable businesses going forward.

Unfortunately, that is not the path that Royal Mail have taken. Royal Mail has adopted a twin strategy in letters first, to rely on its monopoly position to impose vast increase prices on customers, and second to deliberately under-resource the delivery network to reduce daily delivery costs.

In the absence of positive change coming from Royal Mail, Access Operators have tried to propose changes to benefit posting customers. However, any such customer-led opportunities for change and innovation have been delayed, and then blocked by Royal Mail's charging strategy, which imposes gold-plated compliance costs and render any proposals unsustainable. Alternatives to this gold-plating have been proposed but Royal Mail have chosen to reject them, because it suits their price-increase strategy to do so.

The price increase strategy has been implemented for short term revenue gain and in the full and certain knowledge that this strategy would negatively impact future volumes. The combination of this, the lack of innovation and the under-resourcing of the network means that letter-posting customers are forced to pay an ever-increasing price but for a service whose only consistency seems to be in missing its targets.

In addition, while volume decline has been highlighted, less seems to have been made of the increase in labour costs and the lack of a significant reduction in overall operations costs in Royal Mail over the same period - despite the considerable reduction in workload caused by the volume decline.

Further there is little mention of the significant returns that Royal Mail has made to shareholders consisting of billions of pounds in dividends and share buy backs that will have impacted Royal Mail's ability to invest in its network.

It is certainly true that Royal Mail is in a financial hole but it is a hole largely of their own making with past and present management failing to tackle the issues around its cost base in line with the volumes it has to process.

It is also true that Royal Mail has been judged and found guilty in using its pricing freedoms in an anti-competitive manner to cause Whistl to cease its own End to End delivery business, for which Royal Mail has been heavily fined. Had this form of delivery competition been allowed to continue and grow Royal Mail would not have been able to rely on these destructive strategies to enhance their position

and would have instead had to look at innovation, their own cost base and to moderate their pricing increase activities to respond to lost volumes. Posting customers have undoubtedly lost out on the benefits of a competitive market both in terms of price and service development.

It is therefore understandable why customers find themselves somewhat aggrieved that they are now being required to shoulder the burden of USO reform to help Royal Mail, when Royal Mail has done so little to help itself. While we cannot change the past, Ofcom must ensure that any proposed reform of the USO also addresses these issues as otherwise that reform will just be another short-term gain which is quickly swallowed up by the long term structural weaknesses in Royal Mail.

Ofcom

With its twin statutory duties to preserve the financial sustainability of the USO and deliver benefit to consumers where necessary by promoting competition, Ofcom made sweeping changes to regulation when it took over as the postal market regulator in 2012, and has largely maintained the same regulatory structure following the 2017 and 2022 reviews.

The principal changes in 2012 were to grant Royal Mail wide commercial freedom by removing much of the price control regulation, and deregulating parcel traffic. Ofcom implemented a light touch regulatory regime with emphasis on:

- monitoring aspects of Royal Mail's performance, particularly Quality of Service on USO products and ongoing efficiency measures. Aspects of the efficiency measures were changed in the 2022 review to make Royal Mail's targets and performance against these more transparent and it remains to be seen what impact this will actually have on Royal Mail efficiency improvements.
- Pricing controls largely limited to a price cap on 2nd class letters and large letters and margin squeeze protection on Access volumes against the equivalent retail products.

Ofcom's regulatory regime has not fully delivered the results intended by its duties:

- Royal Mail's finances are in a perilous state prompting the debate around the possibility of relaxing aspects of the USO and necessitating this Call for Input.
- Despite the monitoring regime around Royal Mail's planned efficiency gains, Royal Mail has failed to drive sufficient efficiency improvements. This is by no means a new thing. Ofcom had previously commented that Royal Mail efficiency targets were set at the bottom end of what could reasonably be expected but, despite that, Royal Mail still went on to miss those lowest of targets.
- Despite the monitoring regime around Royal Mail's QoS, Royal Mail has failed to make any significant improvements to restore the QoS to anything like an acceptable level. Ofcom has launched several investigations and taken enforcement action by fining Royal Mail for its performance, but since the savings from understaffing delivery outweigh the fines Ofcom impose by several orders of magnitude, there is no incentive for improvement.

It seems as if shareholder pressure and management incentives are not sufficient alone to deliver the improvements necessary. Any reform of the USO must find solutions to deal with the issues of Royal Mail pricing, Royal Mail efficiency and Royal Mail QoS in Access as these are inseparable from the debate on the stability of the USO network. USO reform must not act simply as the acceptance and codification of past market failures.

We also note that Ofcom's approach appears to be to consider the merits of USO change and, should change be required, to alter the Access regime to fit the new model. However, in our view and given the importance of Access both in terms of the volume of items sent through it, and the fact that its revenues underpin much of the USO network, it would be more sensible to consider the combined workload of Royal Mail's operation across USO, bulk mail and parcels and then define the ideal network. Services that fit the network and meet the needs of consumers could then be developed and bought to market in each area.

Whistl

Whistl is the largest Access Operator delivering some 58% of the Access volumes to Royal Mail across a varied and diverse customer base. Our customers have a broad range of needs which are met with a range of services for both pre-sorted and unsorted mail.

Whistl customers have largely used the D+2 Access service happily since Access started but with increasing concern about the escalation in the downstream prices and decrease in QoS. Access charges have broadly tripled since the market was opened (from c13p an item to c45p currently) with the largest increases coming when Ofcom took over as regulator and in recent years.

The advent of the Economy D+5 service (at c4p per item less than D+2) was a welcome alternative for a portion of our customers who are less delivery-time-sensitive. The QoS of next working day Access D+2 has in the last two years fallen well short of the 95% target and this has prompted migration to the D+5 service since posting customers have realised that the performance of the D+5 mail at day 3 is not too dissimilar to the actual performance of their D+2 streams. Ofcom should not make the mistake of assuming that all of the volume that has migrated to D+5 is because customers are content with a longer delivery window: it is a cost and QoS issue for many customers, and is more a reflection of customer resignation with the QoS for D+2 than customer requirement for slower delivery.

Whistl also uniquely has had practical experience of alternate day End to End delivery at scale. Between 2012 and 2015 Whistl offered an alternative to Royal Mail's standard D+2 service. The service had a slower delivery speed with half the mail delivered at D+2 and half the mail delivered at D+3 in Whistl's area of operation. However, the service benefited from individual item tracking and was made available at a discounted price to the Access D+2 services. Conversion levels from our customer base were excellent to this service because customers had good reliable data on the QoS they were receiving, mail drop dates were reliable and of course all of this innovation came at a lower price.

Customers that, for whatever reason, could not live with the elongated delivery window still had the option to use the D+2 DSA service so mail volumes were not impacted negatively. With the possibility of network reform to move to longer delivery spans these customers would no longer have this D+2 option and would have a choice of accepting the degraded service, moving their volumes to a premium service at potentially significant extra cost or seeking alternative channels, all to their detriment and to the detriment of the mail market and volume that currently supports the USO.