Postal Regulation and Business Model Transformation

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Agenda

Direct Competition

Intermodal Competition

Business Model Transformation

Regulatory Transformation
Addressed Mail
Modes of Competition

Competitive Bypass

Electronic Bypass: e.g. online-banking, e-invoicing

Banks
Utilities
Government
Addressed Mail
Economics of the Traditional Value Chain

**High cost elasticity**
Relatively low economics of scale / density

- High efficiency gains through competition
- Major innovations:
  - Optimization software
  - Digital Stamp
  - Sorting automation with OCR

**Low cost elasticity**
Large economics of scale / density

- Low efficiency gains through competition (natural monopoly)
- Delivery is labor-intensive
- Alternative delivery channels?
Addressed Mail
Cost / Price Structure

- loss
- profit

Unit costs vs. density (Items/skm)

Uniform tariff

Rural areas vs. cities
Addressed Mail
Specific Characteristics

- Labor-intensive instead of capital-intensive
- Fixed instead of flexible routes
- USO
  - Geographical scope
  - Frequency
  - Uniform tariff
- Increasing platform competition – E-substitution
Addressed Mail
Volumes in Switzerland

Graph showing the addressed mail volumes in Switzerland from 1997 to 2008. The line graph includes two lines:
- Actual Mail Volumes
- Hypothetical Mail Volumes without E-Substitution (in parallel with GDP)

Sources: Swiss Post Annual Reports; SECO

Effect of E-Substitution
How Can Postal Operators React?

- Downsizing?
- Defense of core business?
  - Product and price differentiation
  - Value-added services
- Modification/transformation of business model?
  - Vertical integration – extend the value chain
  - Geographical expansion
  - Horizontal expansion – new products and services

Which way to go?
Internal View
What Posts are Especially Good at

Resources and Capabilities

- Delivery know how
- Post office network
- Access to every household
- Brand reputation
- Trust

How can these resources be leveraged?
Internal View
What Mail is Especially Good at

The Value of Direct Mail

Personalization: Targeted at specific market segments.
Low cost per response: Compared to less targeted approaches, e.g. telephone direct marketing.
Measurability: Tracking of response rates and the return on investment on each campaign.
Confidentiality: Communication of messages to specific customers without letting other customers and competitors know.

Mail only

The personal touch
Tactile experience
Less intrusion

How can these values be leveraged?
Business Transformation
Step 1: Add Value to Services

- Generation of Communication Demand
- Information Processing
- Transportation and Delivery
- Receiving Information
- Processing Response

- Direct Marketing-Services
- Customer Profiles
- Address Administration
- Post Room Management
- Response Management
- Invoicing
- Encashment
- Hybrid Mail
- E-Mail, EDI Clearing
- Call Center

New Revenues Substitution
Additional Demand
Additional Mail
Customer Retention
Business Transformation
Step 2: Redefine the Role of Postal Services

- **Traditional role: Economic enabler**
  Universal postal services enable other parts of the economy by reducing transaction costs and overcoming distances between buyers and sellers.

- **New role: „Transformer of last resort“**
  Posts are “bridges” between the physical and the digital worlds and take the role of a “transformer of last resort”.
External View
Postal Services as Economic Enabler

Basic steps in commercial activities and the role of postal services

<table>
<thead>
<tr>
<th>Process</th>
<th>Role of Postal Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Advertisement</td>
<td>Addressed an unaddressed mail</td>
</tr>
<tr>
<td>(2) Closing a deal</td>
<td>Letters, registered mail</td>
</tr>
<tr>
<td>(3) Delivering</td>
<td>Parcels, periodicals &amp; newspapers</td>
</tr>
<tr>
<td>(4) Billing</td>
<td>Invoices, reminders, registered mail, writs</td>
</tr>
<tr>
<td>(5) Payment</td>
<td>Checks, postal counters, online solutions</td>
</tr>
<tr>
<td>(6) Cancellation (of subscriptions)</td>
<td>Letters, registered mail</td>
</tr>
</tbody>
</table>

Economic view: Posts...

- play an important role in enforcing contracts
- reduce transaction costs
- provide positive externalities

But: This role is increasingly contested by other communication platforms
Posts offer a “physical insurance” for the digital world and thereby complement digital alternatives. Cf. national banks as “lender of last resort”.

Postal Services as Transformer of Last Resort

- Direct Mail, Bills
- Letter
- Express
- In- and outpayments
- parcel
- document management
- Security & Identity Management
- mailroom services, scanning, etc.
- physical digital
- E-Finance, transactions
- E-health
- Electronic post office desk
- B2C e-gov
- B2C e-health

Sender

Receiver

Sender

Receiver
Direct Competition  
Intermodal Competition  
Business Model Transformation  
Regulatory Transformation
Two aspects of regulation strongly affect competition in the postal sector:

- **Access regime**
  Do competitors have access to the incumbent’s infrastructures and processes at regulated rates?

- **Universal service obligation**
  What are the minimum requirements for the service offer of at least one postal operator?
Regulatory Transformation
End-to-end Competition vs. Worksharing with Bypass

- **End-to-End Competition**
  Free market entry
  Duplication of delivery fixed costs; possibly destructive competition
  Prohibitively high delivery fixed costs may prevent entry
  → Either too much or too little competitive pressure

- **Worksharing with Bypass**
  Free market entry
  (Downstream) cherry picking option
  → Cross-subsidization between rural and urban areas is impossible
  → What about the USO?
Regulatory Transformation
Universal Service Obligations

USO Dimensions:
- Area Coverage (Access Points, Delivery)
- Uniform Prices
- Delivery Frequency
- Product Range

Rationale: Underprovision? Distributional concerns?
Adapting the USO: Towards Electronic Delivery?

Printing The NYT Costs Twice As Much As Sending Every Subscriber A Free Kindle

Nicholas Carlson | Jan. 30, 2009, 4:35 PM | 121
Tags: Media, Media, New York Times, Newspapers

Not that it’s anything we think the New York Times Company should do, but we thought it was worth pointing out that it costs the Times about twice as much money to print and deliver the newspaper over a year as it would cost to send each of its subscribers a brand new Amazon Kindle instead.

Here’s how we did the math:

According to the Times’s Q308 10-Q, the company spends $63 million per quarter on raw materials and $140 million on wages and benefits. We’ve heard the wages and benefits for just the newsroom are about $200 million per year.

After multiplying the quarterly costs by four and subtracting that $200 million out, a rough estimate for the Times’s delivery costs would be $644 million per year.

Source: businessinsider.com
Adapting the USO
E.g. Electronic Delivery?
Conclusions

- Direct and intermodal competition increasingly challenge traditional postal business models.
- The role of postal services must be reconsidered.
- Postal operators have various options for business transformation. (Do they?)
- Regulated access may accelerate direct competition in the postal sector. (Is this still an issue?)
- Universal service obligations can and should be adjusted to the new competitive environment and technologies.
Thank you very much!

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