

# **The role of the universal service obligation in postal competition**

**Christian Jaag, Ph.D.**

Swiss Economics and University of St. Gallen

September 28, 2011

**POST-EXPO2011**

# Agenda

- **Competition in the postal sector**
  - Direct competition
  - Intermodal competition
  
- **Universal service obligation**
  - Economic rationale
  - Effect on competition
  
- **Towards a future-oriented regulatory framework**

## Competition in the Postal Sector It's All About the Cherries



Observed market entry strategies after liberalization (e.g. Netherlands, Sweden) are highly selective with respect to

- area coverage;
- product range;
- customer focus.

**Postal competition is likely to remain asymmetric in the near future.**

**Why?**

# Competition in the Postal Sector

## Barriers to Entry vs. Invitations to Compete

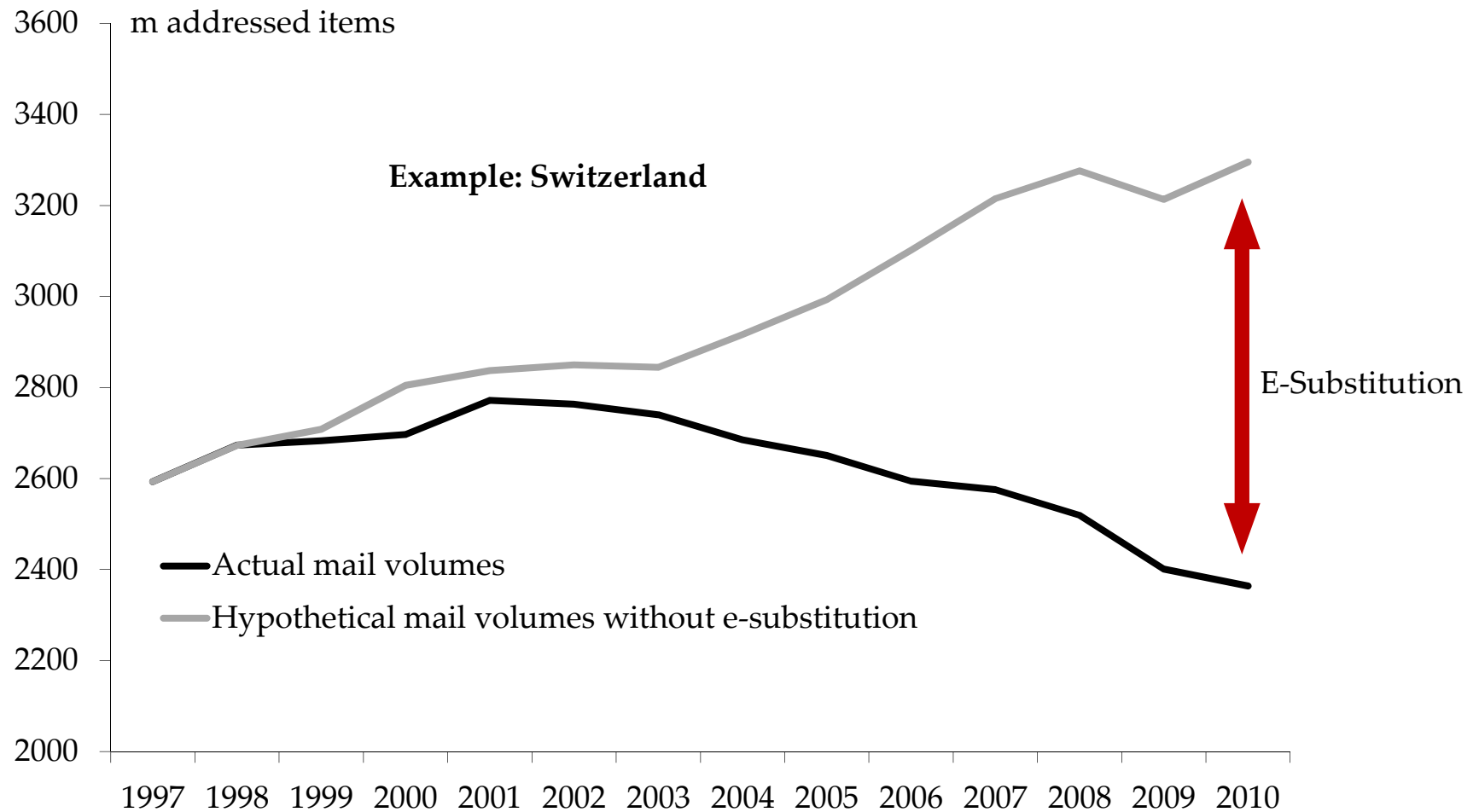
- **Legal aspects**
  - Reserved area
- **Regulatory aspects**
  - VAT exemptions
  - **USO and their financing**
  - Minimum wages
  - Network access
  - Pricing flexibility
- **Economic aspects**
  - Cost structure (proportion of fixed costs, geography)
  - Market development (e-substitution)



**Uncertainty**

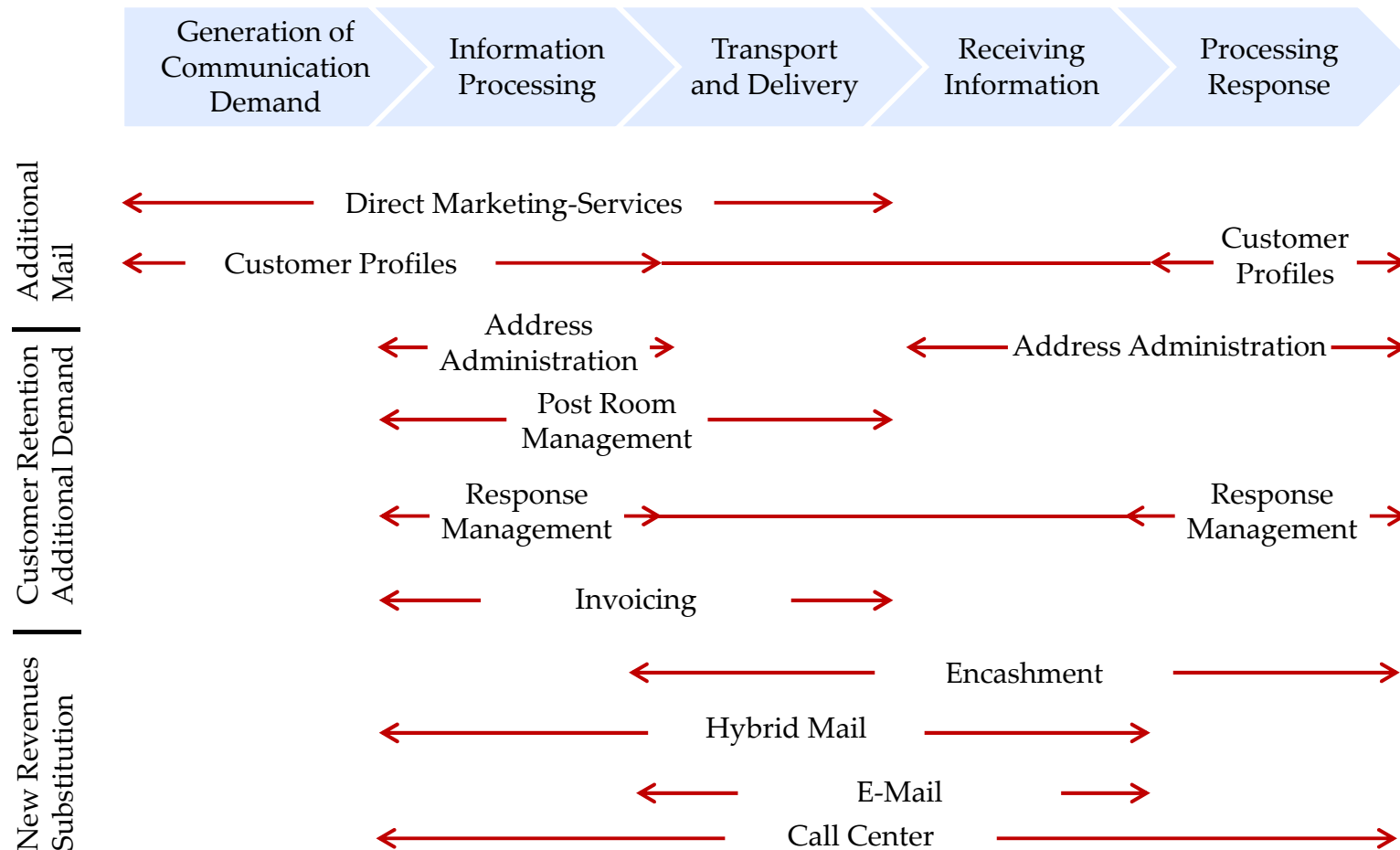
# Competition in the Postal Sector

## Intermodal Competition

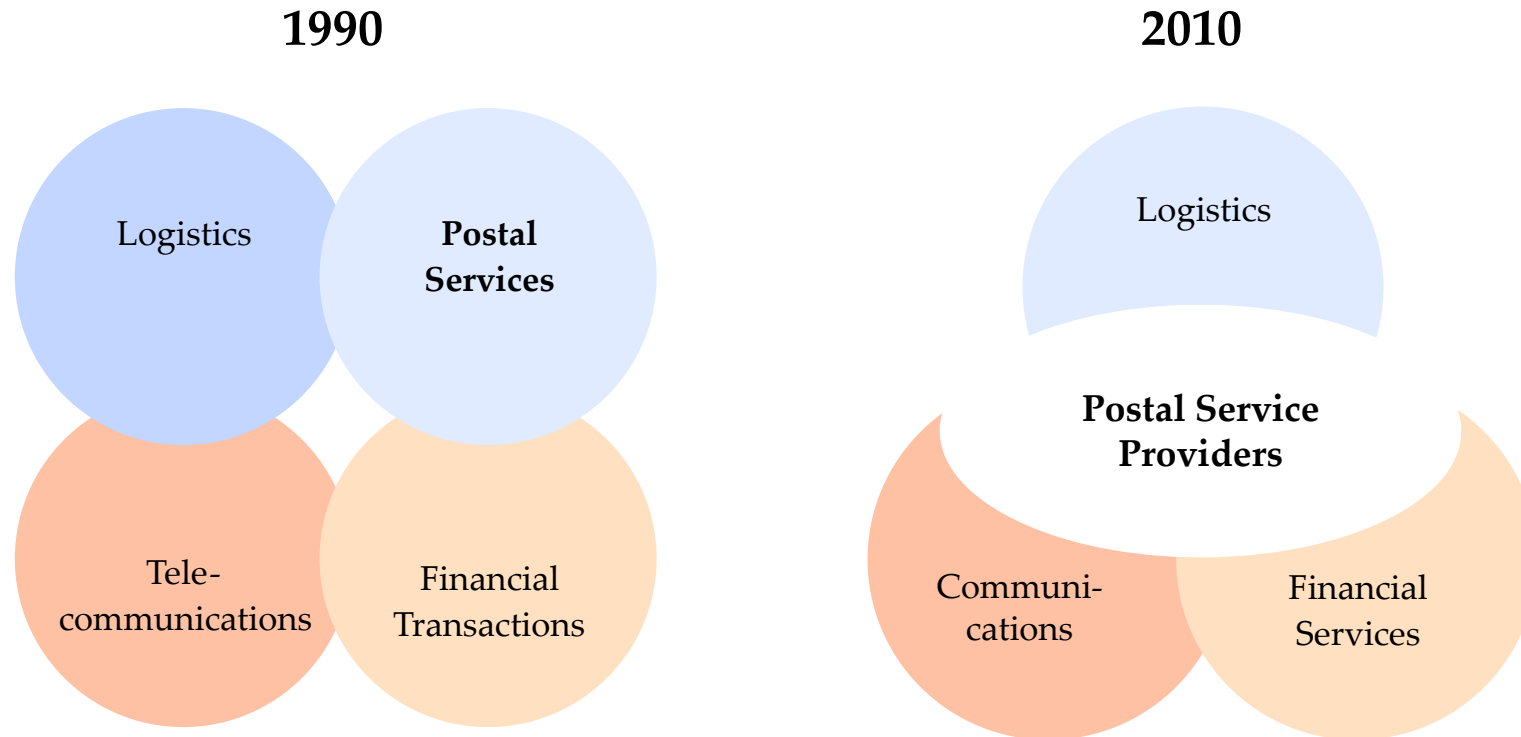


# Postal Business Model Transformation in Competition

## Examples of Value Added Services



# Convergence in the Postal Sector



**What is the current role of universal services?**

**How to adapt them?**

# Current Postal Universal Service Obligation

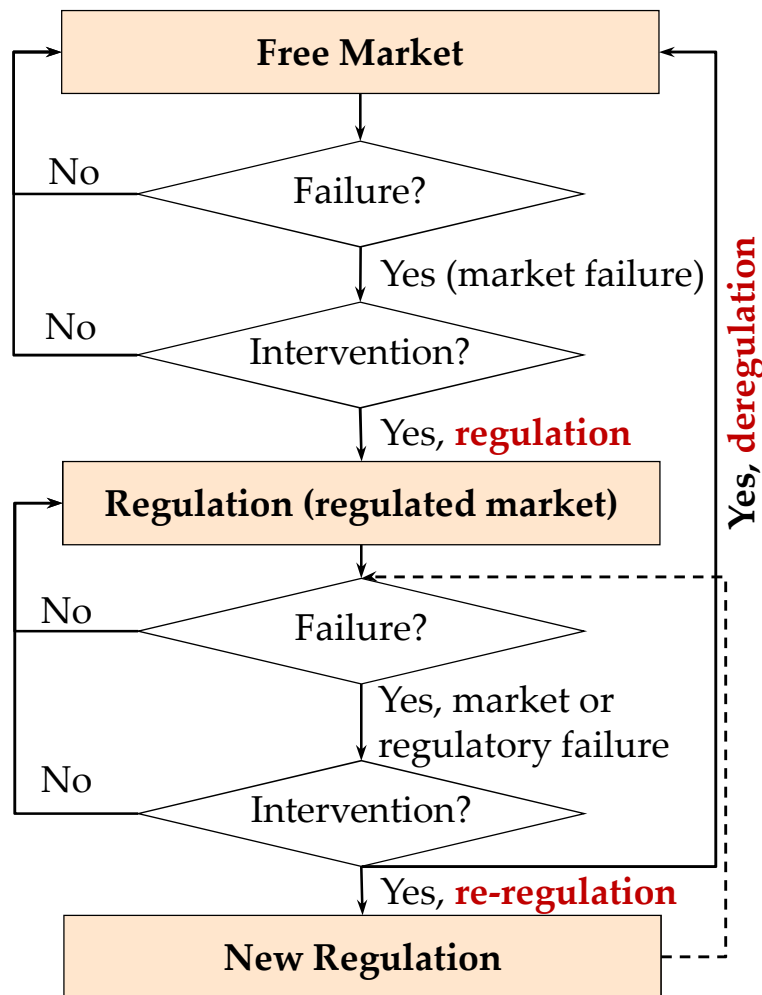
## USO Dimensions:

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

## What is the rationale for USO?



# Economic Rationale for USO



1) **USO regulations for redistribution in perfect markets**

→ Uniform pricing

2) **USO regulations based on general market imperfections**

– Asymmetric information /  
Enforcement of property rights

→ Availability of registered mail

3) **USO regulations based on sector-specific market imperfections**

– Externalities

→ Ubiquity, accessibility, product range, quality, pricing

– Asymmetric information

→ Quality

– Transaction cost

→ Uniform pricing

# How USO Affect Postal Competition

## Effect on USP

- + VAT exemption
- + Commitment device in strategic interaction to defend market
- + Economies of scale and scope
- Excessive cost due to inefficient processes; compliance
- Distorted innovation incentives (e.g. reverse hybrid mail)
- Distorted choice of product range and quality

## Effect on Competitors

- + Comparatively high flexibility
  - Contributions to the financing of the USO
- 
- USO move away prices from the competitive (efficient) equilibrium
  - USO affect market structure

# The Competitive Effect of Postal USO

## Example: Reverse Hybrid Mail (RHM)

RHM allows receivers to choose between various forms of delivery:

- open and scan letter mail,
- forward-ship it to any location,
- deposit a check,
- recycle or shred the letter,
- securely archive the original and/or the scanned electronic version.

Major benefits of RHM:

- ✓ Convenience for receiving customers
- ✓ Cost savings for postal operator

With USO, existing processes and infrastructures cannot be abandoned

→ RHM cannot realize its full potential

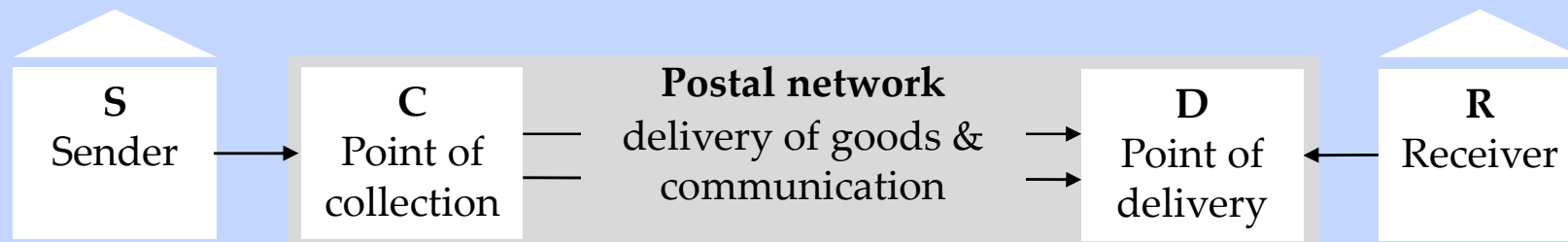
# Outline of Future-oriented USO

Traditional

- Accessibility of post offices
- Frequency of collection

- Letters, parcels, registered mail
- Speed (e.g. E+1, E+3)
- Prices must be affordable and uniform

- Home delivery for x% of population
- Frequency of delivery



Future-oriented

- Adequate accessibility of **basic services**
- Accessible at least every working day

- **Basic service** for letters, parcels
  - Option of proof of reception
  - Minimal end-to-end speed
  - Prices: Affordable, uniform
- Integrity requirements for electronic services

- Home delivery standards for **all letters and parcels** depending on complementary electronic alternatives provided

## Conclusion

- Direct and intermodal competition increasingly challenge traditional postal business models.
- Postal operators have various options for business model transformation. (Do they?)
- Universal services strongly interact with market forces and affect postal competition.
- Universal service obligations can and should be adjusted to the new competitive environment and technologies.

**Thank you!**

**Christian Jaag, Ph.D.,** Managing Partner

christian.jaag@swiss-economics.ch  
www.swiss-economics.ch

**Swiss Economics**  
Stampfenbachstrasse 142  
8006 Zürich  
Switzerland