

# **Current and Future USO in the Postal Sector**

**Christian Jaag, Ph.D.**

November 10, 2011

Swiss Economics and University of St. Gallen

# Agenda

- **Universal postal services today**
  - Scope
  - Rationale
- **Universal postal services tomorrow**
  - Challenges in the marketplace
  - Outline of a new postal USO

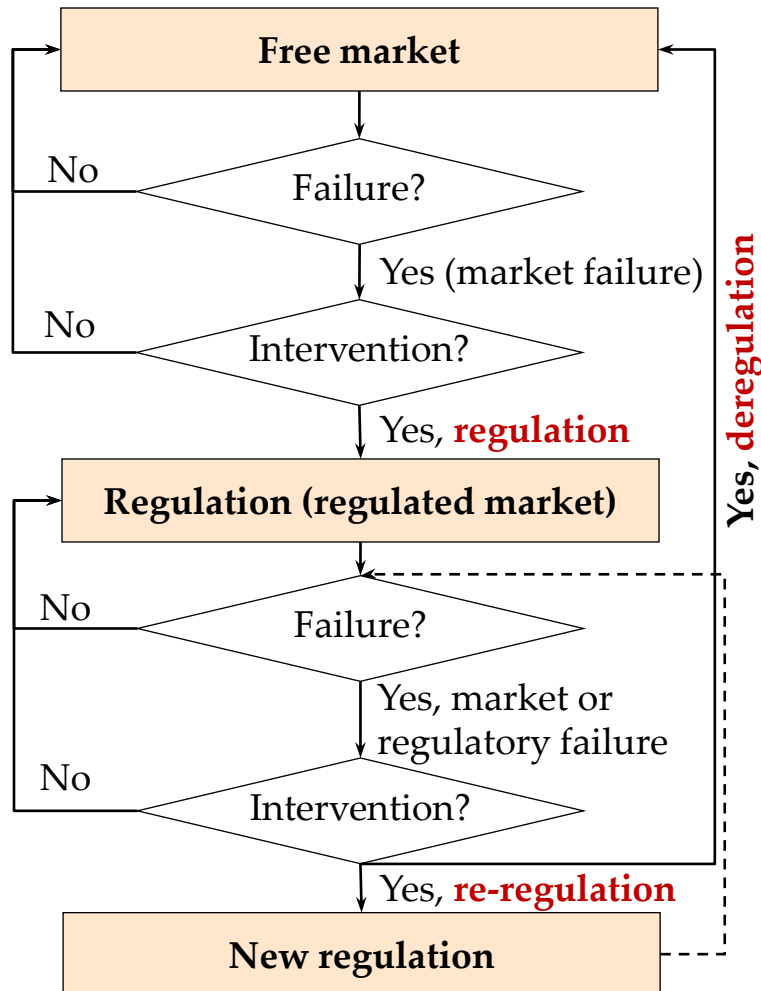
# Current Postal Universal Service Obligation

## USO dimensions

- Area coverage (access points, delivery)
- Uniform prices
- Delivery frequency
- Product range

**What is the rationale for USO today and in the future?**

# Economic Rationale for USO

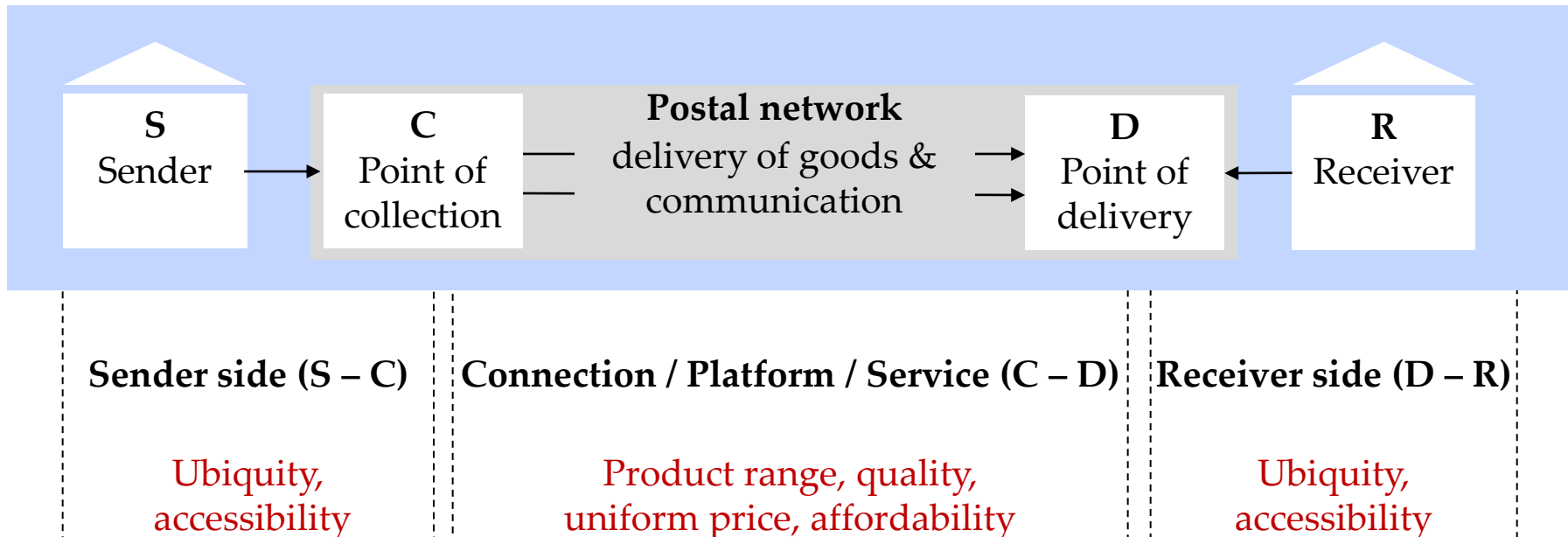


- 1) **USO regulations for redistribution in perfect markets**  
 → Uniform pricing
  
- 2) **USO regulations based on general market imperfections**
  - Asymmetric information / Enforcement of property rights
  - Availability of registered mail
  
- 3) **USO regulations based on sector-specific market imperfections**
  - Asymmetric information
  - Quality monitoring
  - Transaction cost
  - Uniform pricing
  - Externalities
  - Ubiquity, accessibility, product range, quality, uniform price

**Are these points still valid?**

# The Postal Market is Two-sided

## What does this Imply for the USO?



- Obligations w/r to **ubiquity, accessibility and quality** (Cremer et al., 2008)
- Importance of **free home delivery** and potential positive effect of **uniform pricing** (Jaag and Trinkner, 2008)
- **Affordability** to ensure access of every sender

# Universal Service Obligations

## Nature, Cost and Benefit

### Two possible natures of USO:

„**General Allocation Rule**“: Substitutes market as allocation mechanism

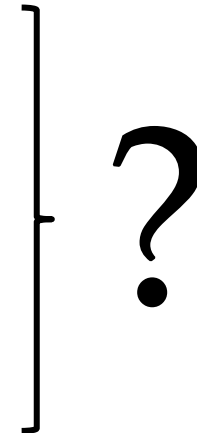
„**Safety Net**“: Makes sure people who might be at a disadvantage can have a certain service. → Complements market as allocation mechanism

### Cost of USO

- Inefficient allocation due to distorted price signals
- Forced over-/underprovision with certain goods

### Benefit of USO

- Fairness
- Efficiency



# 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**

# Cost of USO

## 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



# Cost of 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

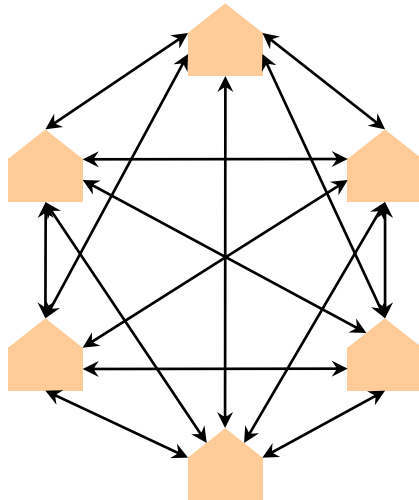
With USO, existing processes and infrastructures cannot be abandoned

→ RHM cannot realize its full potential

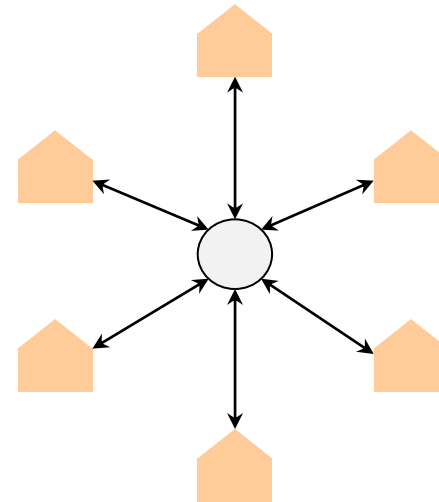
# Benefit of USO

## Traditional Role: “Enabler”

**Delivery without intermediary**  
Number of Links:  $(n, 2) = 15$



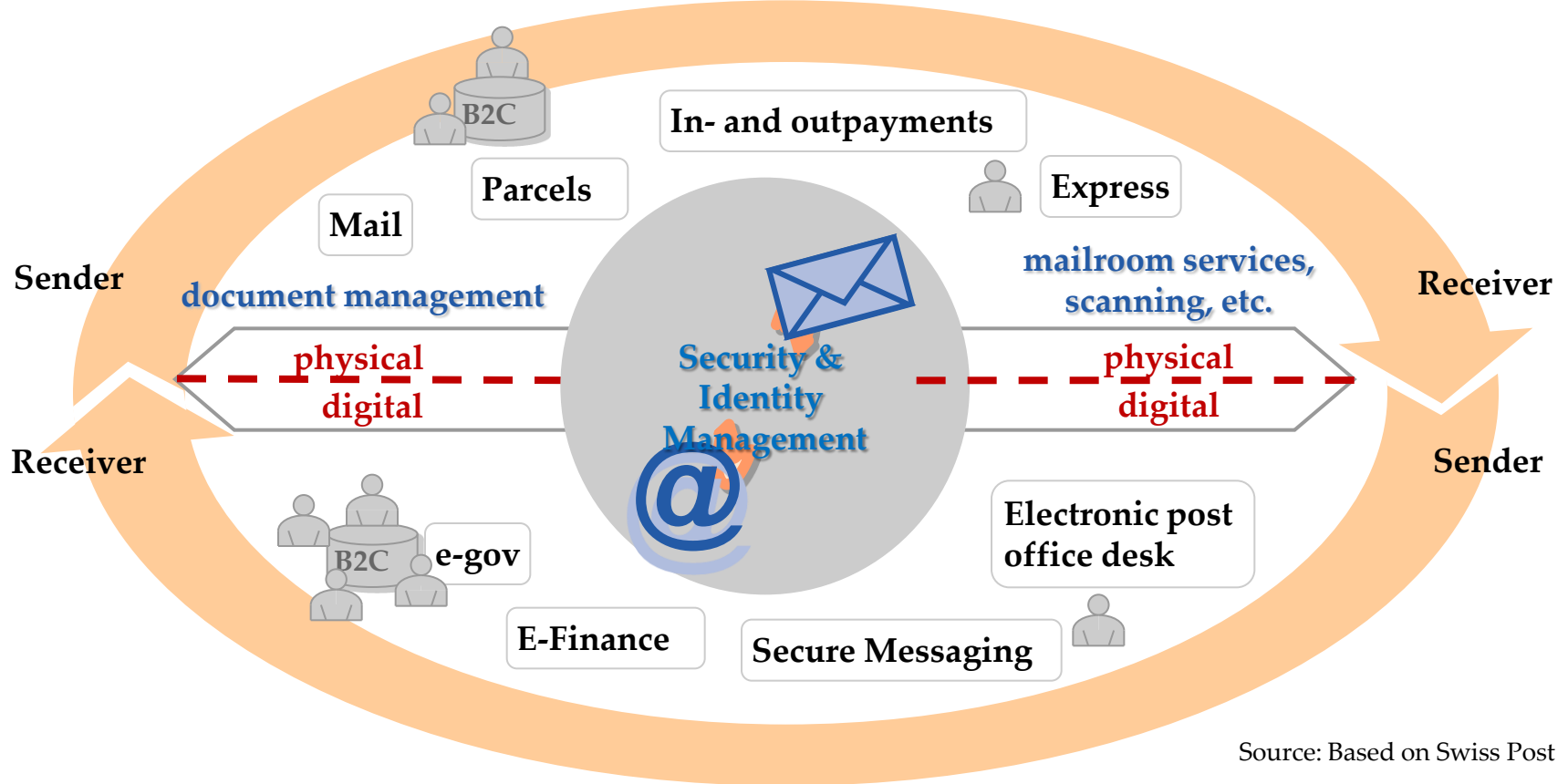
**Delivery with intermediary**  
Number of Links:  $(n, 1) = n = 6$



**→ Reduction of Transaction Costs**

# Benefit of USO

## More Recent Role: "Transformer"

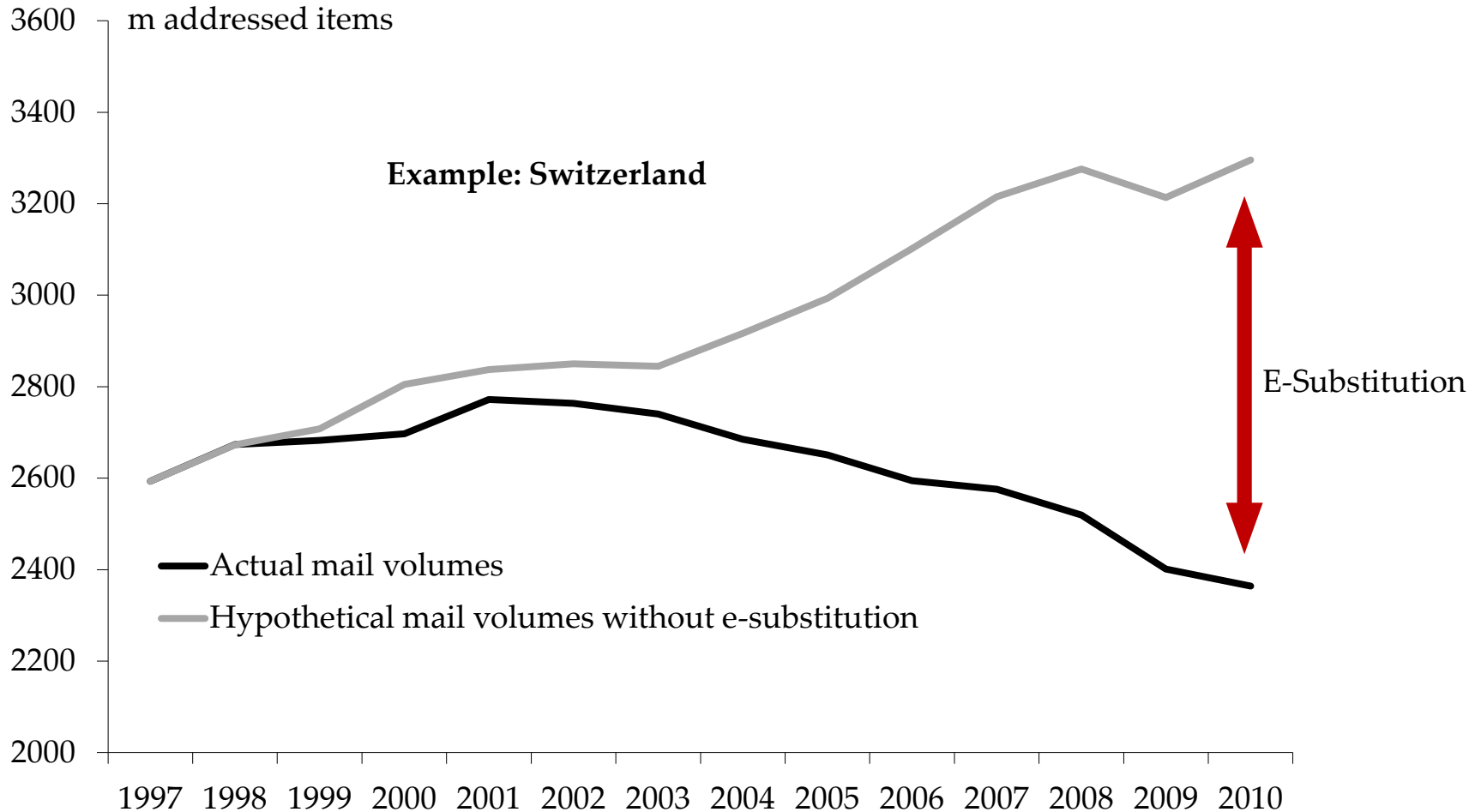


Source: Based on Swiss Post

Posts increasingly ensure the link between the physical and the digital world. They provide a physical insurance of digital means.

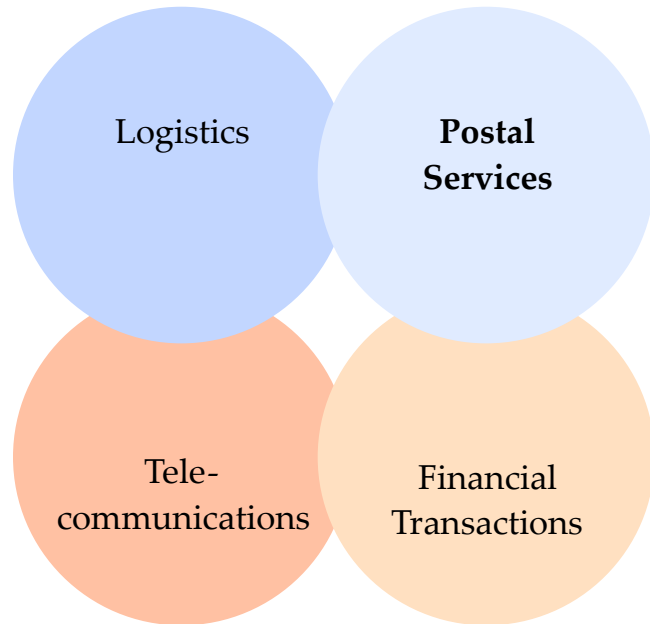
# Competition in the Postal Sector

## Intermodal Competition

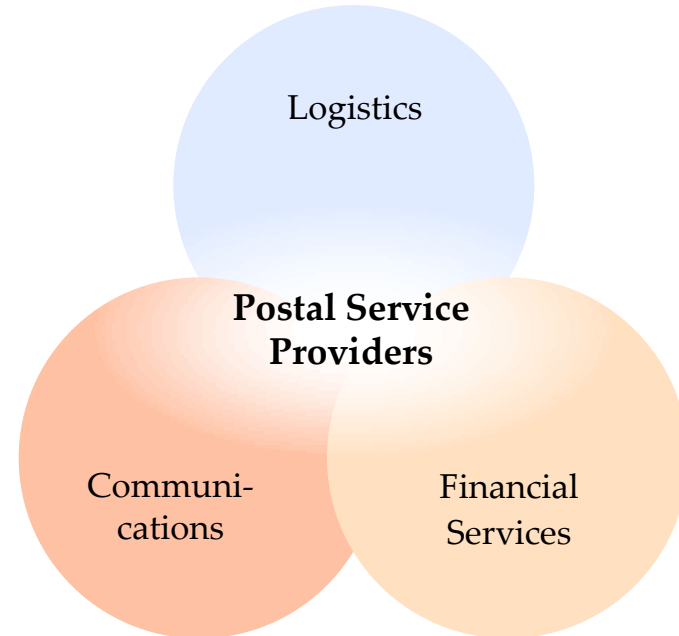


# Competition in the Postal Sector Convergence

1990



2010



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

# 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

- The optimal scope of USO results from a trade-off between its social costs and benefits
  
- Universal services strongly interact with market forces and affect postal competition.
  
- Universal service obligations can and should be adjusted to reflect
  - the economic rationale of USO regulations,
  - consumer preferences and
  - the current and future role of electronic complements and substitutes.

**Thank you!**

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

[christian.jaag@swiss-economics.ch](mailto:christian.jaag@swiss-economics.ch)

[www.swiss-economics.ch](http://www.swiss-economics.ch)

**Swiss Economics**

Stampfenbachstrasse 142

8006 Zürich

Switzerland