Postal Sector Reform

Kumar Ranganathan
with Rohini Dey

Private Sector Development Department
The World Bank
In Collaboration with Universal Postal Union
Contents

Abbreviations .............................................................. vii

Acknowledgments ............................................................. ix

Foreword ............................................................................ xi

Introductory Statement ........................................................ xiii

Chapter 1
Agenda for Reform .............................................................. 1
  Objective of the Study ............................................................ 2
  Key Messages on Reform Policy .................................................. 3
  New Directions ........................................................................ 23
  Conclusion .............................................................................. 26
  Annex 1: Concerns about Postal Reform ........................................ 27

Chapter 2
Regulatory Policy Reform ............................................................. 31
  Competition Policy and Public Service Obligations ......................... 34
  Cost Disaggregation .................................................................. 37
  Universal Service ...................................................................... 38
  Monopoly Scope ..................................................................... 40
  Interconnection ....................................................................... 44
  Aspects of Pricing Policy .......................................................... 47
  Tariff Regulation ..................................................................... 49
  Regulatory Framework ................................................................ 50
  New Directions ....................................................................... 53
  Conclusion .............................................................................. 55
  Annex 1: Country Examples: Postal Service Regulatory Reform ........ 57

Chapter 3
Enterprise Reform: Structural and Corporate Transformation ....................... 61
  Corporatization ....................................................................... 63
  Post and Telecommunications .................................................... 65
  The Legal Transformation ......................................................... 67
  Legal Status of the Postal Service ................................................. 69
  Ownership of the Postal Service ................................................ 73
  Functions, Powers, and Obligations .............................................. 75
  Financial Performance ............................................................... 76
  Conclusion .............................................................................. 80
  Annex 1: Structure of the Postal Service: Some Examples ............... 83
  Annex 2: Country Examples: Postal Service Structural and Corporate Transformation .................................................. 85

Chapter 4
Enterprise Reform: Commercialization of the Postal Service ................... ............ 93
  Improving Operational Efficiency ............................................... 95
  Corporate Planning Strategy .................................................... 100
  Organizational Structure .......................................................... 101
  Staffing and Human Resources ................................................ 104
  Affiliates, Acquisitions, and Alliances ......................................... 105
## Contents, concluded

### Case Study 5
**British Post Office: The Need for Further Reform**
- Background: 243
- Royal Mail and Parcelforce: 245
- Post Office Counters: 246
- The Need for Change: 247
- Conclusion: 250

### Case Study 6
**Canada Post: Reinventing the System**
- The Reasons for Reform: 252
- Reform through Legislation: The Birth of Canada Post Corporation: 257
- Relationship with the Government: 262
- Reform through Commercialization: The Four Phases: 265
- The Results of Reform: 269
- Continued Problems at the Post: 277
- Conclusion: 280
Abbreviations

AR Acknowledgment of Receipt
ATM Asynchronous Transfer Mode
BT British Telecom
CAGR Compound Annual Growth Rate
CBD Central Business District
CEO Chief Executive Officer
CNCT Comisión Nacional de Correos y Telégrafos
CPC Canada Post Corporation
CPI Consumer Price Index
CSI Customer Satisfaction Index
CSO Community Service Obligation
CTC Compañía de Teléfonos de Chile
DTI Department of Transport and Industry
EDI Electronic Data Interchange
EFL External Financing Limit (U.K.)
EFT Electronic Funds Transfer
EFTPOS Electronic Funds Transfer at the Point of Sale
EMS Express Mail Service
ENTEL Empresa Nacional de Telecomunicaciones
EPOS Electronic Point of Sale
EU European Union
GBE Government Business Enterprise
GDEW GD Express Worldwide
IAS Telecommunications Authority of Singapore
IATA International Air Transport Association
KPN Royal PTT Netherlands NV
MLOCR Multi-Line Optical Character Reader
MPT Myanmar Post and Telecommunications
NCPR National Competition Policy Review
OCR Optical Character Recognition
P&T Post and Telecommunications
PAM Postal Automated Machine
PLFC Philpost Leasing and Financing Corporation
POUNC Post Office Users' National Council (U.K.)
PPI PTT Post International
PPIC PTT Post International Company
PSBR Public Sector Borrowing Requirement (U.K.)
PSTN (or PBX) Public Switch Telephone Network
PTC Post and Telikom Corporation
PTT Post, Telephone, and Telegraph
R&D Research and Development
SDR Special Drawing Right
SOE State-Owned Enterprise
SWIFT Society for Worldwide Inter-bank Funds Transfer
TAS Telecommunication Authority of Singapore
UPS United Parcel Service
UPU Universal Postal Union
VAT Value Added Tax
VES Video Encoding System
Acknowledgments

This report has been prepared by the Advisory and Implementation Group of the Private Sector Development Department of the World Bank, in collaboration with the Universal Postal Union (UPU) of Berne, Switzerland.

The World Bank wishes to extend particular thanks to the UPU and the Director-General of its International Bureau, Thomas E. Leavey, for their contributions to and support for this work.

We wish to express our gratitude as well to the Government of Canada for providing resources that funded fieldwork research for several of the case studies, and also to Australia Postal Corporation, the British Postal Consultancy Service (BPCS), Canada Post Systems Management Limited (CPSML), Empresa de Correos de Chile, John Mulligan (UPU consultant), PT Finland Ltd. Singapore Post Private Limited, Sweden Post Ltd, and the Telecommunication Authority of Singapore (TAS), as well as several other postal administrations and governments, for their technical input and kind support. In addition, our thanks are due to the review panel—namely, to John Dowson (Partner, Coopers & Lybrand), Ronald Kopicki (Privatization Specialist, PSDPS), Thomas E. Leavey (Director-General of the International Bureau, UPU), and Kevin Young (Manager, PSDPS), all of whom provided valuable comments to the first draft of the report. Additional thanks are due to others who provided valuable comments throughout the study, in particular, Juan Ianni (United States Postal Service), who was also the study coordinator for UPU, John Mulligan, M. Richard Porras (United States Postal Service), and Christer Blomquist (Postal Development Action Group). We are grateful as well to Partho Sanyal, Dhruva Sahai, and Alicia Kuno of the World Bank, who laid the groundwork and provided timely contributions to the study.

Not least, we would like to thank those who labored with us in structuring, designing, refining, and finalizing this report. Special thanks are due to Emily Evershed who, through her excellence in editing and in managing the report production process, has kept this project on track, and to Roxolana Kassaraba who, regardless of the bottlenecks, provided the continuity to the production process and the technical input on data analysis. We would also like to thank Thomas Termini of Enigma Concepts Inc. for the design, layout, and typesetting of the report, Craig Ballard, Marcy Rye, and Kanitha Saleetid of the World Bank for document input work, and Brenna Hearty for other administrative assistance connected with this report.

We are grateful to the United States Postal Service for kindly supplying us with the photographs used with this text.

We are especially grateful for the ongoing support of Kevin Young, Manager, Privatization Services Group, Private Sector Development Department, World Bank, who encouraged us to undertake this study and whose valuable direction was instrumental in bringing this paper to completion, and for the initial encouragement on the part of Inder Sud, Director, MN2, World Bank, to undertake this sizable piece of work.

Kumar Ranganathan
This study, *Redirecting Mail: Postal Sector Reform*, a collaborative effort between the World Bank and the Universal Postal Union (UPU), is a pioneer work in the area of postal services. It has raised key policy-related messages for countries that are considering postal sector reform by reviewing the experiences—positive and negative—of the reform efforts of several countries around the world and extracting lessons on reform from other network-based industries. Past experience in comprehensive postal sector reform is very limited indeed, even among high income economies. The postal sector has remained virtually unchanged for many decades all over the world. However, given the advances in competition from alternative media, such as the private courier industry and telecommunications-based services, and given that postal services in many developing countries are operating with heavy financial losses, governments are being forced to reform the sector. In this regard, we are faced with a rapidly growing volume of inquiries from governments to provide assistance to their postal sector. This report is intended to disseminate policy and implementation options to reformers, and to provide a set of “new” alternatives to the old issues—such as regulation, monopoly protection, technology integration, and private sector participation.

The report discusses in detail the current outlook for reform, the reform of regulatory policy, structural and legal reform, enterprise reform, and the effect on postal services of the current technological revolution. The case studies presented here cover the reform efforts of Australia, Canada, Chile, Singapore, Sweden, and the United Kingdom, and provide instructive lessons.

We are pleased to present this review of international postal sector reform as part of the World Bank’s Private Sector Development (PSD) Department’s program to disseminate country experiences of postal service reform. This report is one of the early efforts to promote postal reform concepts in developing countries. Through our alliance with the Universal Postal Union for project preparation assistance and through the Postal Reform Trust Fund that we are organizing, the PSD Department is uniquely resourced to assist developing countries in their postal reform.

Magdi Iskander
Director
Private Sector Development Department

Kevin Young
Manager
Privatization services Group
Many qualitative changes in the environment, both external and internal, have triggered the transformation of today's postal services. Over the last few years the globalization of exchanges in goods and services has shown dramatic acceleration. This includes the service industry of which postal services are a part. As trade barriers have fallen, large and sophisticated multinational companies, which until now specialized in the express market, are looking more and more to take larger shares of other international physical mail procedures. This has added an international dimension to the postal business, not only with competitors for physical mail, but also with the providers of new electronic communications products that have no national borders.

The separation of Posts and Telecommunications in a growing number of countries was greeted at first with apprehension. Concerns were raised about the division of resources and management expertise. The economic viability of postal services was also called into question. This has now given way to a sense of cautious optimism that postal services can indeed be self-sufficient and even profitable.

The rapid evolution of the transportation market, also part of the trend toward globalization, certainly represents a challenge for postal services. But we should also see it as an opportunity. The transportation market is being liberalized and is destined to reorganize itself on the strength of worldwide links. Wherever it is seen as more economical or more efficient, road networks are being developed as alternatives to rail transportation. Air transportation is more flexible and less costly than in the past, mostly through deregulation but also as a result of the larger presence of freight forwarders, multinational integrators, and customized shipping firms.

A new industrial and commercial logic is emerging, based on the need to react quickly in order to supply market demand. In addition, a market liberalization process is under way which, as it pulls down trade barriers, will leave postal services more vulnerable to competition. But at the same time it will open up opportunities to exploit new markets by taking advantage of the development of international trade.

A postal market with a diminishing monopoly is the result of multiple factors which have exerted a strong influence on policymakers. Important among these factors are:

1. The emergence of the private sector as a dominant force in the transportation and communications sectors.

2. Lobbying groups established by the private couriers which, through claims that a level playing field is needed, are actively pushing to reduce the postal monopoly to a bare minimum.

3. The more recent orientation of financial and development agencies such as the World Bank and International Monetary Fund, which, under the structural adjustment programs, are advocating less government and more private initiative.
4. In Europe especially, through regulatory influence exercised by the European Union (EU), the telecommunications market and the postal market are gradually being liberalized. In its proposed directive on liberalization of the postal market the EU wants to set limits on the postal monopoly and to harmonize the common universal service obligations of its members. The issues raised, although particular to the EU member countries, will certainly have an influence far beyond the European sphere.

The classic postal administrations are giving way to postal corporations of different colors. Some countries have taken bold steps toward achieving true regulatory reform. We have also seen a few examples of the complete privatization of postal services. However, in the majority of cases, corporatization has taken place. In these situations, the national postal service provider has adopted commercial principles and gained greater management autonomy. Many governments have started to implement the strict separation of operator and regulator.

One of the most important results of this transformation is the change in the mentality of postal management. Accountability, often incidental in a classic postal administration, has taken on a high profile in the new organization. Greater accountability exists before the government or the regulator, before customers, before external auditors, and before the staff. We are beginning to speak today of stakeholders in the postal business, just as we would describe the shareholders in a private company.

However, there are still many unresolved questions that only time will answer. At present we can state little more than that postal services are caught in an ambiguous position between the pressures of a largely unregulated market economy and the notion of a public service obligation. This brings us to a fundamental question: regardless of the legal status and the internal organization of postal services, what is the basic mission of a postal service provider?

For a private postal entity, the mission will be easy to define. It will be to maximize profits. But as a public service provider, it may be difficult to judge its performance solely on commercial grounds. As a service to society, the national postal service provider will have to negotiate a compromise with its government. It will be up to the national authority to fix the role of the national postal service provider vis-à-vis the customers it serves. In this respect, it must not be forgotten that postal banking is part of the financial strength of many postal services and plays a vital role in the sustainable development of numerous developing countries.

Postal managers will have an important role to play, for example, in helping the national government make informed decisions on postal matters. These decisions, of course, must be both politically convincing and economically viable.

The new environment has caused postal services to be more aware of their level of contribution to the gross domestic product. This awareness can strengthen the position of the national postal service providers in the eyes of national policymakers. For governmental recognition and support, the national postal service provider must better explain its role as a major transporter of goods for the business sector. Without this recognition, a fair assessment of the contribution of the postal service provider to the national economy is impossible.

In today's postal environment, customer satisfaction is determined not only by how well the product is designed to meet needs, but also by the quality of service provided in the delivery. The world's postal services are making every effort to improve their quality of service. The International Bureau of the UPU is certainly conscious of the important role that it can play in this area.
New postal products and services are making their appearance. Hybrid electronic mail (although present volumes are still rather modest) has enormous potential to replace anticipated losses of traditional mail volumes in future years. Direct mail provides another unique opportunity to build mail volumes within the developing as well as the developed countries. Both advertising mail and mail order fulfillment services are experiencing significant growth. Appropriate encouragement and cooperation between postal services and the direct mail industry will produce greater development of these eminently postal services.

From the point of view of management, the new trends are encouraging. The management style of the past was often bound to rules and regulations. There was a bureaucratic indifference to the needs of the customer. But now we are beginning to see greater management autonomy, flexibility, and decision-making at the appropriate levels. With the decline of monopoly protection and the establishment of corporate structures, a more business-like focus on financial performance and quality of services will increase. The stakeholders in the world’s postal services will certainly place more demands on management than in the past.

This will result in the emergence of a new management culture. The emphasis on human resource development will be on developing people who can conceive and implement change. What will matter to the new postal managers will be results rather than the rigid application of rules. They will have to exhibit a greater sense of responsibility, as well as foresight gained through better knowledge of the multiple factors affecting the postal market.

Finally, the area of technology may well be where the most far-reaching changes will take place. We are experiencing today an incredible explosion of information. The telephone, fax, electronic mail, and other new forms of electronic communication are showing tremendous growth and their growth is proceeding at a much faster pace than that of physical mail. With electronic mail, new multimedia messages, and the great interest shown in the Internet, this trend toward greater use of other forms of communication will accelerate during the coming years. Postal services must understand that even as the volume of physical mail items may continue to increase, their share of the overall communications market is likely to show a steady decline.

For postal services in a number of countries, technology has been a generator of growth for physical mail. Countries have used transportation technology to deliver mail to customers more rapidly and have used technology for improvements to their infrastructure, from postal counters to the automation of the postal processing chain. But these technological advances need to be extended to the postal services of all the UPU member countries. Unless this happens, we run the risk of increasing even further the gap between the information rich and the information poor.

The explosive growth of the communications market will also force more postal services to move beyond the core, physical mail business. They will have to diversify in order to broaden the range of choices they offer their customers. New hybrid postal products which combine electronics with hard-copy delivery are being used successfully today by the more innovative postal services.

These are just a few preliminary thoughts on some of the trends that will determine the future growth of postal services. Change and reform will be crucial to ensuring this growth. A growing number of postal services have shown us that reform works. Now we, within the UPU, will have to convince all postal services that their future depends on their willingness to begin
the postal reform process themselves. Those postal services that take a passive approach to the future will be unwittingly helping to lead the postal business toward obsolescence. Accepting the status quo will mean that the market share now held by postal services will continue to erode in favor of competitors and the newer forms of communications media.

On the other hand taking a proactive approach gives us the means to anticipate future changes. The World Bank study on Postal Sector Reform has produced a number of key messages and strategies for postal services and governments alike to consider when embarking on their own reform movements. The UPU had the opportunity to contribute to this study and must congratulate the World Bank on the excellent work done. I hope that this study will produce a lively and constructive debate within the postal community and that it will become a valuable tool in the future development of postal services.

Thomas E. Leavey  
Director-General  
of the International Bureau of the Universal Postal Union
For an overwhelming majority of countries, the postal service is the most basic and most common means of communication. In these countries the postal service is, in some areas, the only link serving the entire populace; it also serves as the most important medium of communication for business and commerce. In a world where reliable and speedy communication is essential to the success of rapidly globalizing trade, industry, and services, the development of this sector is vital. The sheer size and impact of the sector are also significant in terms of the employment that the sector supports and the proportion of GDP that the sector generates. In spite of this, the key role of this sector and its significance for economic progress and social development were not acknowledged by governments in the past. As a result, while significant progress in terms of reform has been made in other public service sectors, the postal service is one of the last bastions of the old order.

In many developing countries, the postal service operates with huge inefficiencies and offers a poor quality of services to the public—services that, in addition, have not responded to the needs of the changing market. Consequently, the post has become a significant financial burden on the government. Until recently, postal services could operate with cost and service inefficiencies because they faced virtually no challengers. As state-owned companies they had no fear of going bankrupt. Many had tidy non-mail income earners such as a postal savings bank or a contract to distribute government benefits. As for the mail segment—the core product—monopolies on collection, transport, and delivery kept rivals out; in addition, there were few alternative means of communication. The telephone service, which was the main “competitor,” was also run by the post office. All these factors
which protected the postal service provided no incentives to improve performance.

However, this situation is changing significantly and rapidly. Governments are no longer prepared to continue covering the losses of the postal sector as public revenues are becoming more scarce. Indeed, many countries are dismantling the integrated PTT (Post, Telephone, and Telegraph) structure, and thus the post office is more exposed financially without the support of telecommunications and postal banks. There is growing competition from the private courier industry and the electronic communications industry. Even with continued monopoly protection in some areas of business, postal volumes face a significant threat of erosion if the postal service remains intransigent regarding change. Unless national postal services adapt to the changes in government priorities, in customer needs, and in the communications industry, they face a bleak future. If they reform early, however, postal services could benefit significantly from the explosive growth in overall communications worldwide. Some postal services, at least, have taken heed.

Recently some countries have awakened to the need to reform. While only a few countries to date have implemented full-scale postal reforms, some of these reforms show quite workable and interesting results that have relevance for other countries that are attempting to modernize their postal service. This study analyzes some of these reforms and highlights their successes as well as the difficulties encountered. Despite the success of some of the reform programs discussed here, it should be borne in mind that such sectoral reform takes time to implement fully, and that even those countries that have implemented reforms have not yet completed their journey.

Objective of the Study

The main objective of this study is to review some of the major postal sector reforms around the world and extract key policy-related messages for those countries that are considering postal sector reform. In its discussion of this subject, this report does not look at the payments systems and financial services typically undertaken by postal services. These systems and services are a topic for future studies.

To date, very few countries have implemented reform programs in the postal sector. Those that have done so are generally high income countries. Owing to time constraints, the study examined only six countries: Australia, Canada, Chile, Singapore, Sweden, and the United Kingdom. This does not in any way imply that the selected six countries represent only the best cases of reform. The selection of the case study countries was based on a number of factors including: serious need for reform, lessons to be learned (positive or negative), access to information, availability of data, willingness to participate in the case study, and geographical spread. In addition to
the six case study countries, the study team gathered information on reform steps taken by postal administrations in many other countries. Thus, the key policy messages that have emerged from the study are based on the experiences of about 35 countries. These policy messages were further validated through a cross-country analysis of key data and information relating to the postal sectors of more than 125 countries.

Following this chapter's discussion of the outlook for reform in the postal sector, Chapter 2 covers reform of the regulatory policy, while Chapters 3 and 4, respectively, discuss corporatization and commercialization of the postal service. Chapter 5 provides a picture of current technology reform in relation to the postal service and its overall importance to the service's development. Six case studies provide a detailed look at differing experiences with postal reform around the world.

This review of the postal sector and the experiences of postal reform in countries across the world have led to the following conclusions:

1. **There is a Need for Reform** in the postal sector. This need is particularly evident and urgent in low income and middle income countries.

2. **Enterprise Reform** is being adopted increasingly for the postal sector in many countries, and the process is accelerating and is following a broadening range of approaches. There are some good examples to support the fact that enterprise reform can bring about efficiency and enhanced service. However, most of these experiences are in high income countries. Unfortunately, several postal administrations have used corporatization as the only reform approach and have hoped that the legal transformation would lead to sustainable improvement in performance.

3. Very few countries have undertaken **Regulatory Reform**. Some countries have taken bold steps in this area. Examples include Argentina, Finland, Sweden, and the Philippines. A few other countries have made marginal attempts at regulatory reform. Most countries have either ignored regulatory reform, and thereby continue to keep the entire postal sector under monopoly protection, or have deferred any policy actions in this regard.

4. State ownership is overwhelmingly the predominant **Institutional Approach** found in the postal sector. There are only a few privatized postal services (an example is seen in the postal services of the Netherlands through public ownership of a share of the PTT company). Apart from these few cases, the private sector has not been involved in the man-
5. Postal services must undertake Technological Reform. Although the overall communications market is experiencing an explosive growth, and although the postal sector is also benefiting from this growth, maintaining the status quo would ultimately lead the postal sector into obsolescence. Technological reform would help the postal sector fortify its business and financial position in the near term and would help reduce the risk to the sector of complete replacement by other communications media in the long run. Only a few countries have recognized the immediate need for technological reform.

1. Need for Reform

In most low income countries, and in several rural areas in middle income countries, paper mail is the only medium, or the predominant medium, of communication. Not only personal communication but also business to private and private to business transactions are dependent on the postal service. Thus, a viable postal service is a basic commercial need for an economy. In countries where the postal service is unreliable, people are forced to use other modes of communication which are usually expensive and could carry a substantial cost to the economy as a whole.

There is an urgent need for postal service reform in low income and middle income countries. Evidence from the study underscores this message. The major reasons for introducing reforms in the postal sector are the following.

• The sector is usually of considerable importance to governments. It typically represents a significant portion of GDP and is also a large employer. For example, in the EU the postal sector represents 1.8 percent of GDP and employs over 1.6 million people. In many countries it is a socially sensitive sector primarily because of its heavy unionization.

• The sector is inefficient in most developing countries. The service is often unreliable and has not been responsive to market needs and trends. In addition, the cost to consumers of covering the system’s inefficiencies, either through high tariffs or Treasury transfers to cover deficits, is very high in many developing countries (see, for example, Box 1.1).
Box 1.1 An Example of Operating Deficit Coverage

The operating deficit of the Post Office of one country from the Latin American and Caribbean region in 1994 was about 84 percent of that in 1992. The apparent reduction in operating deficit was due to a tariff increase. In fact, mail volume actually declined over this period. Indeed, if these two years are compared, the implied tariff increase over and above the retail price inflation is about 24 percent. With this in mind, it can be concluded that the cost to the customers, through tariff and deficit covered by the Treasury, increased significantly (see figure on right).

- The sector represents a consistent large financial drain on the budget. In most developing countries the service is unable to generate sufficient income to cover its operating expenses. As a result, the sector suffers from chronic underinvestment.
- An efficient, universal postal service could generate substantial welfare gains. Owing to the poor service quality, the public will often resort to alternative modes of communication, which are always more expensive than the postal service.
- In addition, since considerable commercial and financial transactions are carried out by mail, any excessive delay in mail delivery leads to a higher transaction cost.
- One of the "infrastructural facilitators" of economic growth is, in fact, the postal service. As economic activity grows, so does the number of commercial and financial transactions by mail. An efficient postal operation is important to the success of this growth cycle.

Financial Performance

In terms of return on sales, the postal sector throughout the world is operating at a loss (about -3 percent return on sales). Given that the postal service in most countries is still operating as a government department, the return on sales shown by these postal administrations does not take into account many cost or expenditure items that are normally considered in generally accepted accounting principles (e.g., the cost of financing investments). This accounting deviation is particularly significant in the case of middle income and low income countries, since in high income economies there is a higher proportion of corporatized postal services using commercial accounting principles. Thus, the true losses would be higher than 3 percent of revenue.
Even with this accounting aberration, it is nevertheless clearly evident that there is substantial disparity in profitability across the different economic categories of countries (see Figure 1.1). While the postal operations of high income countries almost break even (-1.5 percent return on sales), middle income countries are running at a huge loss of about -15 percent return on sales—a performance 10 times worse than that of high income countries. The profitability of low income countries (about -30 percent return on sales) is twice as low as that of middle income countries, or 20 times worse than that of high income countries.

Figure 1.1
Sector Profitability, 1993

<table>
<thead>
<tr>
<th>Return on Sales (percent)</th>
<th>High Income</th>
<th>Middle Income</th>
<th>Low Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>-10</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>-20</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>-30</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Universal Postal Union (UPU).

In the case of the postal sector, particularly that of developing countries (see Box 1.1), poor profitability is due not only to cost inefficiencies but also to lack of growth. The service offered by the postal organization in many countries has not changed in decades, and is not in line with market needs and industry dynamics.

Resource and Asset Utilization

Although only 16 percent of the world's mail volume is handled by the postal services in developing economies, well over 40 percent of the postal infrastructure is located within these countries (see Table 1.1). To collect, process, transport, and deliver this 16 percent of the world's mail, developing countries employ 43 percent of the world's postal workers and carry 57 percent of all of the permanent post offices of the world. The necessity for fixed network assets is dictated by a multitude of other factors besides mail volume, including the geo-
graphic and demographic characteristics of a country. Developing economies have approximately five times the population and one-and-a-half times the surface area to service as do industrialized economies, and developing countries thus have more than double the population density as well. Although there are limits to what can be deduced from aggregative analysis, the above would seem to imply, given the network characteristics and economies of scale associated with this sector, that developing economies possess a far more favorable population density for the postal sector to service. Therefore, if anything, they are in a superior position to benefit from cost economies through increased utilization of their networks. Nevertheless, increased utilization of their networks applies only in a case by case basis to countries with dense population.

Table 1.1
Distribution of Postal Infrastructure, Area, and Density, 1992

<table>
<thead>
<tr>
<th></th>
<th>Staff (%)</th>
<th>Permanent Post Offices (%)</th>
<th>Letter Boxes (%)</th>
<th>Population per km²</th>
</tr>
</thead>
<tbody>
<tr>
<td>Developing Economies</td>
<td>44</td>
<td>59</td>
<td>42</td>
<td>55</td>
</tr>
<tr>
<td>Industrialized Economies</td>
<td>56</td>
<td>41</td>
<td>58</td>
<td>21</td>
</tr>
</tbody>
</table>


The excess of postal infrastructure located in developing economies relative to the mail volumes they service, even after taking into account the population and size of these economies, would appear to imply either or both of the following:

1. The postal network is not being optimized and considerable inefficiencies exist in the operation and administration of the service

2. The postal service has considerable excess capacity which it has not been able to utilize.

Moreover, resource and asset utilization in developing countries is worsening, primarily because growth is hampered by the poor quality of service. Whereas industrialized countries are experiencing a modest positive growth in mail per capita, developing countries are actually experiencing a decline in mail per capita (see Figure 1.2).
Figure 1.2
Average Annual Growth of Mail per Capita, 1987-92


Investments

One of the immediate and profound casualties of poor financial performance and asset utilization is the level of investment. Therefore, it is no surprise that the postal sector suffers from chronic low investment levels. Since most of the network resources and facilities are in a poor or unusable state in developing countries, significant investments are needed if a quality service is to be offered at low cost. The postal sectors of developing countries typically require investments in the following areas.

1. Network Rebalance: The postal network of many developing countries has been preserved intact for many years, although the mail flow patterns have changed significantly (mainly because of urbanization and economic development). Thus, there is an urgent need to rebalance the network to correspond with the logistics of mail operations. This typically calls for the construction of new post offices, sorting centers, and collection centers in optimal locations. The objective of rebalancing is to develop the optimal network to provide good service at the lowest possible cost.

2. Network Rehabilitation: A significant proportion of postal facilities in low and middle income countries is dilapidated. This applies not only to buildings and equipment but also to transportation assets. Thus, not only is service performance affected because of frequent vehicle breakdowns, but the public is reluctant to use the postal service because of the apparent lack of security.

3. Service Expansion: Investments are needed to extend the postal service to cover all residents of the country and to
provide products and services that are responsive to specific market requirements.

4. **Systemization**: Basic systems such as financial and management control systems and track-and-trace systems for EMS are typically not found in developing countries. These are essential instruments for providing a reliable service and for enabling management to take appropriate tactical and strategic actions. Unfortunately, some developing countries, prior to investing even in basic management control systems, have spent large sums of money in automating their sorting functions (for example, using optical character recognition sorters, or automatic sorting machines). Automation will not provide any net benefits if there are not sufficient mail volumes to process through a sorting center, since the acquisition and operating costs of automated sorting are very high. Automation should be looked at very carefully as an integral part of a comprehensive reform program.

5. **New Products**: To maintain their position, and indeed to fortify their competitiveness, postal organizations have to develop hybrid products using the traditional mail operations and electronic communications technology. This would involve investments in research, technology acquisition, and joint ventures. The payback for such investments could have a moderately long gestation.

One good indicator of postal sector development (although this is not always the case) is growth in investments. Given the need for improvement, one would expect a steady growth in investments in developing countries. As is shown in Figure 1.3, over the 10-year period up to 1993, there has been no real improvement in the level of investment in the world postal sector. In low income countries not only is the level of investment much lower than the world average, but there is a rapidly diminishing trend (except for 1993).

**Figure 1.3**

**Level of Investment in the Postal Sector**

![Bar chart showing investment per 1,000 mail items in SDRs for the World Postal Sector and Low Income Countries from 1983 to 1993.](image)
It is evident that the postal service sector is caught in a vicious circle of poor financial performance which causes a lack of investment, thereby preventing either improvements in the quality of service or expansion, which generates even lower usage of the sector and mail volumes, which further perpetuates the cycle (see Figure 1.4). To disengage this sector from this downward spiral, urgent reform measures are called for.

**Figure 1.4**
The Vicious Circle

2. Enterprise Reform

The term *enterprise reform* refers to programs implemented primarily by the enterprise itself to provide it with a more commercial orientation. In *commercialization*, market principles are introduced into the entity, while *corporatization* provides a legal transformation that subjects the entity to the legal requirements of a private firm. Such a transformation can be an effective enabler of change.

**Commercialization**

An increasing number of countries have recognized the importance of commercializing their postal service. Commercialization is the process of introducing market principles into postal administrations. Therefore, core areas such as finance, accounting, strategic planning, marketing, and so on are either introduced or strengthened in postal administrations. Training may be provided for core functions, experienced personnel may be brought in from the private sector, or the management function may be contracted out for specific periods in order to hasten the learning process and ensure its effectiveness. While some restructuring measures are within the realm of any postal administration’s autonomy, the authority to take many commercialization steps may have to be specifically included in legislation or
explicitly sanctioned for a government department or a statutory corporation. However, a limited liability company, which holds all the powers of a legal entity, normally has the freedom to undertake most reform measures.

Commercialization need not necessarily follow or precede corporatization. Postal administrations can do much to improve the quality of services and to develop financial self-sufficiency and a market-oriented outlook even without the legislative changes that accompany corporatization. In a few postal administrations, such as those of Chile, Singapore, and Sweden, these changes have been introduced sequentially, and corporatization is regarded as the next major step in the process of postal reform. However, complete commercialization cannot be achieved without the appropriate autonomy, accountability, and incentives that corporatization grants the postal service, nor can corporatization by itself lead to successful reform. Therefore, it is vital that both processes be implemented for reform to achieve its goals. Some postal administrations have chosen to first initiate the corporatization process, accompanied and followed by commercialization, in the interests of clarifying the institutional environment (the roles and responsibilities of all parties) and thereby accelerating reform.

Changes at the policy level, such as market deregulation, the establishment of an autonomous regulator, or the corporatization of the post, affect the parameters within which the post operates. However, commercialization focuses on what it is that the post itself can do to improve its performance within these parameters. Therefore, the steps taken to corporatize and commercialize the post may be termed enterprise reform.

Corporatization

Corporatization is the process of giving postal administrations an independent legal status and subjecting them to the same legal requirements as private firms. Thus, the entity is subject to standard commercial and tax laws, accounting criteria, labor laws, etc. What is more important, by explicitly separating the ownership and management responsibilities, the postal service renders itself less susceptible to government influence. This process enhances managerial autonomy by to some degree insulating the postal service from non-commercial pressures and constraints. It also clearly demarcates the role of the government as owner of the enterprise, which is distinct from the operation of the enterprise. Corporatization is an important step in the ongoing process of commercialization. Most postal administrations which have reformed for the sake of operational efficiency and market alignment have placed great importance on corporatization.
By conferring a distinct legal structure on the postal service, corporatization converts the problem of official governance to the still difficult task of corporate governance—the creation of an optimal system of accountability and incentives within the postal administration. Therefore, it is necessary to introduce explicit contracts between governments and postal enterprise managements in order to run the postal service according to market principles. Without these disciplines, management and resource allocation decisions will not reflect commercial realities.

The present study looked at a number of cases of recent postal enterprise reform experiences throughout the world. The following conclusions can be drawn from these reform experiences.

- Most of the successful postal enterprise reform experiences are found among high income countries such as New Zealand, Canada, and Singapore. This is primarily because the threat of substitution by other communication media is greater and is overtly transparent in high income countries. Additionally, in many such countries there has been an overall emphasis on the self-sufficiency of state-owned enterprises, imposed by the government.

- There are only a few cases of successful enterprise reform in developing countries. Two primary drivers exist for developing countries to initiate enterprise reform. First, serious postal reform has taken place in countries in which the government has initiated an overall public sector reform to improve the efficiency of government agencies. Agencies that were considered significant “cash drains” on the treasury, or those that consistently offered poor value to the public, were prioritized for reform under the overall public sector reform program. The postal service usually meets the criteria for prioritization as one of the government agencies in need of urgent reform (as, for example, in Trinidad and Tobago). The other primary driver of serious reform in developing countries is the emergence and steady growth of a private postal sector. Although the provision of most of the services offered by the competing companies may be illegal, enforcement of the exclusive privileges of the incumbent is more or less impractical and is too costly. The threat of competition has forced the postal organizations themselves to recognize the need to improve efficiency and to introduce quality service (see Case Study 2, on Correos de Chile, in this report).

- A significant number of postal organizations which have undergone corporatization have unfortunately considered the corporate transformation as the only required reform. As a result, their post-corporatization operational and fi-
nancial performances have not improved because reform did not include commercialization.

- Those postal organizations that have successfully implemented enterprise reform have brought about significant benefits for the public (in terms of better service, new products, and value for money), for the government (in terms of tax revenue), and for the enterprise or its parent (in terms of retained earnings, higher salaries, etc.). However, even these postal organizations consider enterprise reform to be an intermediary step in the entire reform.

- Successful postal enterprise reforms have been led by a common postal policy and strategy adopted by the government (the owner), the postal organization (the operator), and the regulator. This approach has maintained explicit and corresponding objectives, and the government, the postal organization, and the regulator have worked together toward the development of the sector as a whole. A good example of this is found in Singapore. TAS, the regulator, and the government have consistently aimed to ensure that tariffs stay within acceptable limits, that consumers benefit from a wide range of high quality services, and that Singapore Post continues to make productivity and efficiency gains. As long as these conditions are met, Singapore Post is free to maximize profits provided that part of these profits is reinvested in the business or directed toward sector development.

- Even in cases of successful enterprise reform in which dramatic improvements in efficiency, product offerings, and quality of service have been achieved, government ownership and control has restricted the competitiveness of the postal service. The United Kingdom, where the British Post Office was perhaps one of the earliest post offices in the world to go through a systematic corporatization and commercialization program, is a case in point. Today, the Post Office has not only achieved substantial efficiency gains, but it also provides outstanding service levels. However, the government-imposed External Financing Limit (EFL)1 and the traditional Treasury restraint on postal activities are hindering the Post Office’s ability to act as a commercial organization and to meet the challenges and opportunities of international competition. Indeed, the Post Office would like to be free to raise

---

1 The External Financing Limit (EFL) is one of the three targets set by the government. While the other two targets are considered appropriate, the EFL is seen as a constraint on the postal business and its development. Details of the EFL are provided in the United Kingdom case study.
money without being subject to the Public Sector Borrowing Requirement and free to make investments without having to consult the Treasury frequently.

3. Regulatory Reform

Enterprise reform can and does benefit postal service up to a point. Beyond that, further improvements are achieved only through policy changes relating to regulatory and institutional reform. Regulatory reform, in the context of the postal sector, focuses mainly on (1) the extent of monopoly powers and exclusive privileges granted to the post office; (2) the competitive structure within the sector; and (3) the appropriate mechanisms to ensure the proper functioning of a public service (for example, tariffs, quality, and coverage for the regulated services). Many decisions to be made stem from the issue of competition, such as how the sector should be organized and what institutional approaches should be adopted to foster efficiency and innovation while maintaining contestability or competition.

The study has drawn the following conclusions.

- There are very few cases of regulatory reform in the postal sector. Most developing countries have indeed preserved the original monopolistic structure with no changes at all in the scope of exclusive privileges since the creation of their postal services. It is therefore not uncommon to find that monopoly protection applies to all products of the post office, with the exception of express mail service (EMS), which in most developing countries is a new addition. However, owing to the problems of enforcement, the number of private sector postal operators is on the increase although the operations of these service providers are considered illegal.

- Many countries that have recognized the overall benefits that result from liberalizing markets have in fact not liberalized. Governments are reluctant, often without justification, to open postal markets. Even the EU, which has been liberalizing many markets within it, has recently decided that it will reduce but retain the exclusive privileges for letter mail for the time being.

- There is implicit evidence that such exclusive privileges have not served the postal service well. This “market guarantee” is perhaps the main reason (although not the only reason) why postal services in many developing countries have remained inefficient in terms of both cost and service. It is clearly evident that in EMS, owing to competitive pressure, the cost and the service of the post office are usually better than those of other product categories. Even so, it is not
uncommon to see that the dominant players in EMS are always the private operators.

- It is possible for the post office to operate in a completely liberalized market. Sweden, Finland, and Argentina stand as proof. However, for demographic reasons and for the resulting cost differences between a rural letter and an urban letter, some other countries consider it safer to remove the monopoly gradually through a progressive but systematic relaxation of exclusive privileges (see, for example, the Australia Post case). Explicit and transparent subsidization of non-commercial social activities by the government allows the post office to conduct a commercially oriented business and levels the playing field for the post office (see, for example, the Sweden case).

- In principle, many approaches developed in infrastructure sectors could be brought into the postal sector in order to introduce competition or contestability efficiently. For example, interconnection (as is found in other network industries such as telecommunications and gas supply) could feasibly be introduced into the postal network. This study evidenced no such approaches in the postal sector in developing countries. However, in high income countries there is growing interest in, as well as partial adoption of, such approaches.

- Many countries, even those in which the postal service is corporatized, do not have a proper regulatory process or institution for the postal service. In many developing countries, fundamental regulatory issues such as tariff levels, structure, and increases are effectively determined by the postmaster general alone. This gives the postal service a further disincentive to improve efficiency and quality of service.

It is natural that a close link exists between the extent of regulatory reform and the institutional setup (particularly the ownership issue). If the postal service remains under government ownership, it is likely that the controls imposed by government will have to remain in order to ensure that the post office does not abuse its privilege of being "underwritten" by the taxpayer. These controls usually prevent the post office from entering joint ventures or from having the same access to financial markets and the same degree of commercial freedom as its competitors. For this reason, the British Post Office has seen competitors attack its core markets but has been unable to fight back because as a public sector body it faces government restrictions on its activities. Therefore, countries which plan to embark on postal reform should consider regulatory reform in conjunction with institutional reform.
4. Institutional Approaches

The institutional framework for the sector is key to its success in providing high quality service at competitive costs. Several institutional approaches are available to governments for the management and development of their postal sector. However, it is evident from the experiences of other sectors that enterprise reform is both more feasible and more effective when the private sector is involved as manager, investor, financier, and, increasingly, part owner.

While it is possible to make a public enterprise work well without changing its ownership, World Bank and other experiences clearly show that under these circumstances success in commercialization has been elusive. The record of reforming public enterprises without involving the private sector is largely unsatisfactory.

Some of the reasons cited for not involving the private sector—or for not giving up government control of the postal service—are listed below.

- The provision of universal service will not be respected
- Other public service obligations will be abandoned
- Profit orientation will result in higher prices
- Workers will be made redundant.

While improving efficiency is at the heart of such reforms, public sector goals can also be accommodated under an institutional arrangement involving the private sector. For example, it is feasible to cost the postal service’s non-commercial activities separately, and to allow revenues from these non-commercial activities to be augmented by the government as part of its social services program. In this way, the costs associated with the social elements of the postal service are isolated and the subsidization is made explicit and transparent. Sweden has recently implemented such an explicit subsidization (see the Sweden Post case study for details). It is indeed possible to continue to realize non-profit objectives while increasing private participation in the supply of services. Thus, both universal service and public service obligations can be preserved (as in Sweden) even under a competitive environment involving the private sector.

A sound regulatory framework and a properly prepared contract will ensure that a private operator does not abuse its power on issues such as market power, tariffs, operational practices, and human resources management. For example, it is a common practice to bring in the private sector for management on a predetermined, explicit tariff evolution formula. The factors that make up the tariff formula are closely regulated.

The study evidenced a strong move toward involving the private sector in the operations and financing of the postal service, regardless of whether a country is high income, middle income, or low in-
come. Typically, the rationale for privatizing or implementing some form of private sector involvement includes the following:

- Governments increasingly feel that there is no longer a need for them to own or operate the postal service. Social service obligations could easily be built into the privatization framework. Many countries have done this in other socially sensitive sectors.

- Governments of developing countries would, and should, prefer to direct public funds toward poverty alleviation and investing in social sectors. Underwriting the losses of the postal service and investing in postal development are not priorities. Consequently, governments feel that if postal infrastructure needs to be developed to support economic growth, the most prudent approach would be to involve the private sector in the operations and financing of postal services.

- Implementing a comprehensive reform requires a strong institutional capacity that is typically not found in the current organization of the postal service. Any form of private sector participation is an effective way of immediately strengthening the capability to implement and effect change in almost all areas of the business.

A variety of options are available in which the private sector is involved in all or some of the postal operations and postal development. Private sector involvement has worked well in other infrastructure sectors such as telecommunications, power, transportation, and water supply and distribution. It is possible to involve the private sector efficiently in postal services despite the fact that natural monopoly elements may exist in the sector and that the postal service contains certain public service obligations which are considered "non-commercial" (see Chapter 2 for details). Three types of private sector participation models are briefly described below—management contracting, concession, and joint ownership.

In management contracting, a public authority contracts with a private company to provide specific services for the operation and maintenance of the postal service. These services could include the provision of key staff for technical assistance, operations, maintenance, marketing, new product development, finance, and project management. Compensation to the private company would be of the type made under contracts for consulting services (time-based, lump sum, percentage of revenue, cost-plus, etc.). The responsibility of the private company would be limited to that part of the system operated on behalf of the public authority. Where the complete operation is contracted out, customers legally remain clients of the public authority and the private company is compensated in accordance with the terms of the contract. There are several types of management
contracts, including those which include a productivity bonus to the contractor or a share of the profits. Such incentivized management contracts provide the operator with the stimulus to be entrepreneurial, as well as to exceed the contractual targets.

In a concession system, the public authority contracts out development and operation to a single private operator, or to a consortium of companies. The concessionaire finances, invests in the appropriate technology, constructs, and operates, at its own risk, all facilities and networks for the provision of postal services. On the termination of the concession, the concessionaire must return the postal system to the public authority in perfect condition. This means that during the life of the concession the concessionaire must replace dilapidated or non-functional equipment and facilities, make the necessary additional investments for better operation and sales enhancement, and also recover its invested capital.

The major difference between a management contract and a concession is that in a concession contract the concessionaire assumes full commercial risk—that is, if the postal operations make a loss, the concessionaire realizes the loss. Equally, if the concession makes a profit, the concessionaire will keep it after paying the necessary taxes and dividends. In a management contract the commercial risk assumed by the operator is considerably smaller. In a fixed fee contract, for example, no operation risk is assumed. In incentivized management contracts, part of the operator fee is linked to the operator's performance. Although it is possible to have a management contract that involves investments, in general, if a primary motive for involving the private sector is to bring in private capital to accelerate the development of the sector, then a concession may be the most appropriate approach. And a concession gives the operator greater autonomy, since the operator assumes the full commercial risk.

Joint ownership involves a new partnership under which the employees, the sub-postmasters, and the government could each hold significant shareholdings in the business, together with a strategic partner that has a strong interest in the business and that could provide not only financial capital but also technical and management expertise. The retention of government shareholding is an indication of the government's continued commitment to the vital public services that the post office provides. It also allows the government and the employees to share in the company's future success through its shareholding.

However, if this option is to add value to the development of the postal service, it is essential that the retained government shareholding should not leave the government in control of the business. If the government were to retain a majority shareholding, it would still be in control, the post office's borrowings would continue to count against
the government's public sector borrowing requirements, and the taxpayer would effectively be underwriting the business.

For the post office to operate as a private sector company, the government must sell a majority of the shares and must also involve the strategic partner's ownership in a significant way. As long as the government is only a minority shareholder, the business would be classified to the private sector and would be free from public sector controls. This option provides the post office with the commercial freedoms that are most necessary if it is to respond to increasing competition and market dynamics, and could also benefit the consumer by allowing the new company to develop new services.

Figure 1.5 presents a comparison of relative attributes of various institutional models for the postal sector.

**Figure 1.5**
Relative Attributes of Different Institutional Models for the Postal Sector

<table>
<thead>
<tr>
<th>Attribute</th>
<th>Government Owned</th>
<th>Autonomous Board</th>
<th>Private or Mixed (Government-Private) Company</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Institutional Alternatives</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Legal autonomy</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Responsibility for setting tariffs</td>
<td>Public</td>
<td>Public</td>
<td>Public</td>
</tr>
<tr>
<td>Financing of fixed assets</td>
<td>Public</td>
<td>Public</td>
<td>Public</td>
</tr>
<tr>
<td>Ownership of fixed assets</td>
<td>Public</td>
<td>Public</td>
<td>Private until expiration of contract, Public and private</td>
</tr>
<tr>
<td>Operation and maintenance of system</td>
<td>Public</td>
<td>Public</td>
<td>Private without commercial risk, Private with full commercial risk</td>
</tr>
<tr>
<td>Beneficiary of revenues from tariffs</td>
<td>Public</td>
<td>Public</td>
<td>Public</td>
</tr>
<tr>
<td>Compensation to private company</td>
<td>—</td>
<td>—</td>
<td>Proportional to physical parameters (mail volume, number of outlets)</td>
</tr>
<tr>
<td>Contract validity period</td>
<td>—</td>
<td>—</td>
<td>About 5 years, About 10-20 years, Variable</td>
</tr>
</tbody>
</table>
In order to implement postal reform in the most effective way, and also to realize rapid benefits such as enhanced efficiency and improved service, the optimal institutional approach is to involve the private sector in the management and financing activities while retaining full, or partial, government ownership. While in some countries it might be difficult to transfer operations fully to a private operator, an attempt should nevertheless be made to gradually increase the private sector's role.

5. Technological Reform

The postal service as operated today is very much based on physical distribution. The mail is collected, transmitted, and distributed physically. Indeed, in the postal services of almost all countries, the labor component of the total cost is in the range of 60 to 85 percent. This high labor content contributes to the physical limitations in service provision—particularly as regards cost and service levels. In the most efficient postal service, a first class letter, if posted by close of business, can only be delivered the next day. While this is remarkably quick for a largely manual-based system, even this delivery rate can be challenged today by the rapid innovation and growth in electronic communications. With this in view, this discussion of technological reform addresses the postal sector's urgent need to respond to the ongoing communications revolution.

Today, in many countries, even in developing countries where the telecommunications industry has been reformed, the use of electronic communication for business transactions has rapidly become affordable. In developing countries, because of the high hardware and link-up costs, electronic communication systems are usually owned by larger business companies. However, "intermediary" service providers (for example, small bureaus that provide fax, E-mail, and other electronic communications services) are also emerging rapidly in developing countries, albeit only in the urban centers. Close examination of the market for traditional postal services clearly indicates that the problem is more urgent than is realized. For example, as is seen in Table 1.2, most mail demand is generated by the business community (about 85 percent of mail). This pattern is similar for all countries, including developing countries. Additionally, it is the business market segment that attaches greater importance to high service standards and reliability, and the competitive threat from alternative communications media is greatest in this area (see Figure 1.6).
Table 1.2
Typical Composition of Mail, by Origin and Destination, in Developing Countries

<table>
<thead>
<tr>
<th>Percent</th>
<th>To:</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Household</td>
</tr>
<tr>
<td>Household</td>
<td>10</td>
</tr>
<tr>
<td>Business</td>
<td>60</td>
</tr>
<tr>
<td>Total</td>
<td>70</td>
</tr>
</tbody>
</table>

Figure 1.6
Competitive Threat from Electronic Media

It is ironic that the postal sector has expended so much energy arguing for legal protection from direct competition via monopoly protection and exclusive privileges, when the immediate and most significant threat is from the rapidly evolving electronic communications industry. Even if post offices remain partly protected by a monopoly, the most severe competitive attack is from electronic communications service providers, which are not, and are unlikely to be, subject to any restrictions in competing in the overall communications market. Postal operators need to realize that they are part of an overall communications market and that they do not have a privileged or special position in this respect; in other words, they must adapt to the new and evolving situation.

The key messages, then, concerning adaptation to the changing market characteristics, are:

- The postal sector must clearly recognize its position as part of the overall communications market, with changing customer requirements, and must initiate, with the greatest urgency, a comprehensive technological reform.
Any postal authority that is planning to reform or improve its postal service should include technological reform high on its agenda.

Often the prime constraint to introducing technological advances into the postal service is the legislative framework itself, and also government-imposed financial controls. Technological reform starts with a review of, and appropriate amendments to, the legislative and regulatory frameworks.

The investment requirements needed for technological reform can be substantial and the required skills are new to the postal sector. In this regard, postal services may need to form alliances with other private communications companies in order to rapidly implement technological reform.

Perhaps the most important policy message is that unless the postal service integrates communications technology into its service provision, the economics and the changing market preferences may prevent the post from providing a truly universal service.

Although it is not the intent of this study to recommend a specific course of action for postal services, this report offers certain policy options in Chapter 5. At a primary level, postal services could take either a passive option or a proactive option. The passive option is an evolutionary one: in other words, the postal sector could continue to provide the traditional services with some changes at the margin (such as opening a fax bureau service). The proactive option, on the other hand, acknowledges the need to take immediate action and adopt electronic communications technology through the development of hybrid messaging services. In this regard, there are four strategic options open to the postal sector: Minimal, Intermediate, Expansionist, and Exclusive (see Figure 1.7). These strategies are outlined in detail in Chapter 5.

The postal sector should bear in mind that it already has a significant competitive edge. As has been noted, typically about 75 percent of the mail is destined to households. For the mail to reach individual households, there must be a strong delivery network. The postal service is perhaps the leader among the few organizations that have this delivery capability. Thus, the postal sector has a choice: it can build on this strength and become one of the important players in the overall communications market, or it can maintain the status quo and allow its wide network to become increasingly underutilized, thereby allowing the postal service to become a victim of the ongoing communications revolution.
In recognition of the magnitude of the changes urgently needed in the postal sector, governments of low and middle income countries (and, indeed, of some of high income countries as well) should give greater priority to immediate, comprehensive reform. It is clear from the worldwide review of reforms discussed here that the following four broad principles should be adopted for the postal sector:

**Principle 1.** A reform program should be initiated immediately if the country is faced with a poor quality postal service or if the postal service is unable to generate or raise sufficient funds for its development, or, again, if the sustainability of a low cost universal service is being threatened by growing competition (owing to volume erosion).

**Principle 2.** A comprehensive reform program should be undertaken. Many countries examined for this study have implemented independent programs in several functions of the post office or have undertaken partial reforms. Although these efforts lead to some improvement in those particular functions, very little global benefit in the overall postal service is realized. This is one of the primary reasons why several countries have spent a significant amount of resources on improving the postal service and yet have failed to improve the service at the customer end.

**Principle 3.** Traditional beliefs should not be allowed to limit the nature and scope of the reform effort. This is particularly true in dealing with sensitive aspects such as universal service, monopoly, competition, market definition, social obligations, and private sector participation. The communications industry, the market preferences, and the supply economics have all changed dramatically since Rowland Hill’s postal re-
form in 1840. It is time for the postal sector to respond to these changes.

**Principle 4.** Governments should take charge of the reform program. Since a comprehensive program includes legal, regulatory, and institutional reform components, the management of change has to come from the government, not from the post office.

The way to move forward is to rethink the basic design of the postal sector and to prepare and implement a comprehensive reform program quickly. The following chapters provide new dimensions for the old issues of, for example, monopoly, competition, universal service, tariffs, regulation, commercialization, institutional arrangement, private sector participation, and technological integration. The specific reform design largely depends on the objectives for the sector as a whole. However, in general terms, for many developing countries significant benefits could be achieved by fostering some level of competition in the sector through relaxing the scope of the monopoly given to the national postal service operator. Competition is the best force for introducing rapid commercial orientation and business realignment. However, since in most developing countries the national operator can easily be won over by the private sector, a level playing field should be created for competition before any changes are made to the competitive regime. Creating a level playing field includes not only providing appropriate amendments to the existing legislation and regulatory framework, but also upgrading the business capability of the national operator so that the incumbent can compete “equally” with the competitors. The most prudent, and most rapid, way of upgrading the management capability of the postal organization in low income and middle income countries is to bring in the private sector for the management, and possibly the financing, of the postal service. Such an institutional approach, which could be in the form of a management contract, a leasing contract, or a joint venture, provides immediate access to proven modern management techniques, business marketing approaches, project management capability, and technological know-how that otherwise would take the postal organization a very long time to develop by itself.

In general terms, as a way of suggesting appropriate reform paths, the following points should be taken into consideration. The postal sectors of low income and middle income countries could be classified into two broad groups: **Group A:** in this group the postal service’s basic network infrastructure has to be extended or rebuilt in order to
provide a minimum level of universal service; and Group B: this group comprises those postal sectors that have the basic infrastructure but need to rehabilitate and modernize the network for cost and service optimization. Group A can approach its reform in two broad ways:

1. The postal service enters into a concession type of arrangement with the private sector, where the private operator will take on the full responsibility of operating the postal service and expanding or rebuilding the network as specified by the government's sector objectives. The contract period would vary depending on the investment requirements for the expansion, but typically a concession is for a longer period (about 10 to 20 years). The concessionaire will have the responsibility for implementing most of the commercialization and technological reform programs.

2. The government takes on the responsibility of expanding or rebuilding the postal network infrastructure and only then passes the entire operation on a management contract basis or other form of private sector participation approach to the private sector for a fixed period of time, during which most of the commercialization and technological reform programs will be implemented.

Option 2 may be more suitable in countries where the network is so poor that no regulatory reform can be undertaken prior to building a sufficient supply capacity (e.g., where there is a true reason for keeping a wide monopoly for some time), or where the private sector is unwilling to take on the operation.

For reasons stated earlier in this section, Group B postal sectors should involve the private sector early in the reform program. Private sector participation should be for the full management and possibly the financing of the postal service, as in a management contract with investments, or in a joint venture.

The reform could be implemented fully at once, or a phased approach could be used. In either case it is important to implement a full reform program to achieve the maximum benefits. Figure 1.8 provides a selection of postal reform actions.
Figure 1.8
Possible Actions for Postal Reforms

<table>
<thead>
<tr>
<th>Policy Aspect</th>
<th>Degree of Reform</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Low</td>
</tr>
<tr>
<td>Regulation</td>
<td>Separation of post from telecom</td>
</tr>
<tr>
<td></td>
<td>Relaxation of monopoly</td>
</tr>
<tr>
<td></td>
<td>Further relaxation of monopoly</td>
</tr>
<tr>
<td></td>
<td>Relaxation of control regime</td>
</tr>
<tr>
<td></td>
<td>No monopoly</td>
</tr>
<tr>
<td></td>
<td>Monitoring of social obligations</td>
</tr>
<tr>
<td>Investments</td>
<td>Primary network for universal service</td>
</tr>
<tr>
<td></td>
<td>Advanced processing and transport infrastructure</td>
</tr>
<tr>
<td></td>
<td>Hybrid technology</td>
</tr>
<tr>
<td>Institutional</td>
<td>Separation of regulator, owner, and operator</td>
</tr>
<tr>
<td></td>
<td>Implementation of enterprise reform</td>
</tr>
<tr>
<td></td>
<td>Management contract</td>
</tr>
<tr>
<td></td>
<td>Lease contract, joint venture, or privatization</td>
</tr>
<tr>
<td>Arrangement</td>
<td>Separation of regulator, owner, and operator</td>
</tr>
<tr>
<td></td>
<td>Implementation of enterprise reform</td>
</tr>
<tr>
<td></td>
<td>Management contract</td>
</tr>
<tr>
<td></td>
<td>Lease contract, joint venture, or privatization</td>
</tr>
<tr>
<td>Financing of</td>
<td>Government guaranteed loans or bonds</td>
</tr>
<tr>
<td>Development</td>
<td>Government guaranteed loans</td>
</tr>
<tr>
<td></td>
<td>Private capital</td>
</tr>
<tr>
<td>Tariff Policy</td>
<td>Explicit subsidies</td>
</tr>
<tr>
<td></td>
<td>Regulated tariff increases</td>
</tr>
<tr>
<td></td>
<td>Relaxed subsidies</td>
</tr>
<tr>
<td></td>
<td>Uniform or zonal tariff, but rebalanced service levels</td>
</tr>
<tr>
<td></td>
<td>No subsidies</td>
</tr>
<tr>
<td></td>
<td>Unbundled pricing for non-discriminatory network access</td>
</tr>
</tbody>
</table>

Conclusion

In several countries the postal sector is at a trigger point. If nothing is done and the status quo is maintained, then it is likely that the sector will continue to erode as competitors and other communications media take over the market. Under such a situation, it may not be possible to provide a postal service at a reasonable cost or to ensure universal service. Given the importance of this sector, particularly in developing countries, such a situation would lead to adversity in the net welfare.

However, countries that commit themselves to postal reform could turn their postal service around so that it becomes an important player in the communications market. The benefits of a carefully planned and well executed reform program can be significant. Argentina, for example, embarked on a comprehensive postal reform in 1993. This reform involved full commercialization, complete liberalization of the market, and private sector participation in the management and financing of the postal service. Within two years of reform, even before the reform process was completed, the sector and the consumers were reaping considerable benefits. During this period, mail volume grew by about 40 percent, and 96 percent of the letter mail was delivered on time (an improvement from 78 percent in 1993). The consumers also benefited—the average price of delivery fell by over 65 percent. An interesting point from Argentina’s experience is that, after removing the monopoly and introducing competition, not only did the overall mail volumes grow, but the volume of the national postal service increased substantially.
1. The postal service is a dying form of communication which will inevitably be replaced by electronic forms of communication. Therefore it is pointless to restructure/reform the postal sector.

- First, there is a considerable technology gap between countries. As a result, for an overwhelming majority of countries the postal service is the predominant communication mechanism.
- In absolute terms, mail volumes have been increasing despite the evolution of technological communications substitutes. Even in countries which are the most technologically advanced, the growth in mail volumes seems to indicate an overall increase in the potential for communication.
- Traditional mail also services a niche that electronic communications does not in terms of the features associated with hard copy mail, as well as economies associated with it for large volume, less urgent segments.
- The postal service can play a crucial role in making technology accessible to every consumer through its pervasive retail and delivery network.

2. The postal service is the communications lifeline of a nation. Therefore, it should not be tampered with.

- A reliable and efficient postal service is a vital asset to any country. However, if the postal service is plagued by financial and service inefficiency, these shortcomings need to be explicitly addressed in a systematic manner, all the more so because of the vital role the postal service plays in communications. If this is not done, the service will continue to diminish in its value and contribution and will eventually wither away.
- More capital-intensive and sensitive sectors, such as water, are being actively restructured in order to improve them. The postal service has the potential to learn a lot from the experience of these other sectors.
- Although they may not be perfect substitutes, there are other communication mechanisms available, such as the telephone, facsimile, electronic mail, etc.
Redirecting Mail: Postal Sector Reform

<table>
<thead>
<tr>
<th>Perceived Concern</th>
<th>Response</th>
</tr>
</thead>
<tbody>
<tr>
<td>3. Service to the public will suffer. A large number of post offices (especially rural) will be closed or replaced with agency outlets that offer limited services.</td>
<td>• The operator is legally compelled to provide a nationwide counter service or postal access. In areas where usage does not justify the establishment of a full post office, provision of these services at existing banks, shops, etc., makes perfect commercial sense. These postal outlets/agencies can be mandated to maintain a certain external appearance and certain service standards (as in franchises) so that the public does not feel it is lacking a postal establishment.</td>
</tr>
<tr>
<td></td>
<td>• The government can choose to explicitly subsidize the retention of unprofitable post offices where it feels this is vital in the interests of the community. This was the approach adopted in Sweden to maintain counter services for financial transactions in remote areas.</td>
</tr>
<tr>
<td>4. Postal rates will rise by too much if the service is to be financially self-sufficient. This is socially unacceptable.</td>
<td>• Postal rates to most users should reflect the true cost of the service. Therefore, the focus should be on improving efficiencies in order to keep rates at an acceptable level. Rates should not be increased to compensate for operational inefficiency. At the same time, there is no reason why the service should be underpriced if there is no clear social reason.</td>
</tr>
<tr>
<td></td>
<td>• Generally 60 to 80 percent of the mail is generated for the purpose of business/institutional communication. There is no reason why, as in any other input, this clientele should not pay the full price of the service. If the service is subsidized by the government, the obvious beneficiaries of the subsidies are the commercial mailers.</td>
</tr>
<tr>
<td></td>
<td>• It has to be acknowledged that an underpriced postal service will probably compromise on service. There is no social value to fostering an inefficient postal service. In addition, the public is willing to pay for a reliable, speedy service, the proof of which lies in the excessive use of expensive courier services in countries where the postal service is inadequate.</td>
</tr>
<tr>
<td></td>
<td>• For the segment that relies on the postal service for personal communication: (1) postage is a most insignificant component of expenditure. (2) this segment will also benefit from a reliable, if more expensive, service.</td>
</tr>
<tr>
<td>5. The quality of service will deteriorate if the postal administration is driven by profit motives.</td>
<td>• Explicit contracts will mandate compliance with quality of service standards, and service performance will be specifically monitored. This can only bring about an improvement as opposed to the current system, where performance goals may not even exist.</td>
</tr>
<tr>
<td></td>
<td>• In postal services that have reformed (Singapore, Sweden, the Netherlands, Finland, Canada, and the United Kingdom, to name a few), the quality of service has improved.</td>
</tr>
<tr>
<td>Perceived Concern</td>
<td>Response</td>
</tr>
<tr>
<td>-------------------------------------------------------</td>
<td>----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>6. The social objectives will not be fulfilled by a</td>
<td>• Legislation and an explicit contract with the postal operator will mandate compliance with social obligations. However, the costs of these obligations should be calculated and either explicit compensation should be provided for them, or a judgment should be formed as to whether the enterprise is financially capable of servicing these obligations without additional compensation, as in Sweden. This approach confines subsidies, if necessary, to the social obligations and also makes the process transparent. In the past, by shouldering their fiscal losses, governments have implicitly subsidized the entire operations of the postal sector.</td>
</tr>
<tr>
<td>corporatized, privatized, or liberalized postal</td>
<td></td>
</tr>
</tbody>
</table>
### Perceived Concern | Response

9. The government will lose foreign exchange (terminal dues) if the postal service has control of its own revenues. Net terminal dues are generally positive in developing countries.

- The government no longer has to subsidize the entire enterprise (if it was making losses).
- The government will financially benefit from the introduction of corporate tax, VAT, and dividends/financial return. This should more than suffice to compensate for the loss of terminal dues as a source of foreign exchange.

10. National post offices can never compete with their rivals in the private sector because of the expensive obligation to maintain universal services at fixed prices.

- Given the appropriate contracts, and explicit compensation for the social aspect of the service that it has to shoulder, these obligations should not be a bar to commercial success. Generally, no other organization can rival the delivery and counter network of the national post office. It should be able to draw on these assets to compete with its rivals, provided it is given the freedom to do so.

11. The post is incapable of being financially self-sufficient.

- The existence of profitable postal services such as those in Australia, New Zealand, Sweden, Finland, the Netherlands, the United Kingdom, Singapore, Malaysia, and the United Arab Emirates would seem to indicate that this is not true. The Chilean and New Zealand posts have transformed themselves from loss-making to profitable services. The postal business, while maintaining the basic social obligations, can be a profitable business.
Regulatory Policy Reform

The postal sector in almost all countries is protected. Even in countries where free market forces are prevalent in most sectors, the postal service is allowed to continue to operate under the monopoly protection. The justification for this situation is centered around universal service provision. It is a long-held view that to provide postal service to all residents, even in the remotest parts of the country, it would be necessary to protect the service from competitive providers that might service only the lucrative market segments and leave the unprofitable segments to the national operator. Yet these monopolies in some developing countries still leave a significant proportion of the rural residents unserviced.

There are, of course, significant benefits in preserving the universal service concept, although the specific definition of universal service is debatable and may—and should—vary depending on the specific circumstances. It is clearly evident from the experiences of the once-protected markets that services improve when their providers must compete. Thus, the important question that governments face is how to bring about a reform in the postal sector that will benefit the public through both universal service and competition at the same time.

At present the public providers of most postal services claim that this is not possible. They argue that, because it is expensive to service remote areas, they need to be compensated by having a monopoly in lucrative areas and using the profits from it to subsidize their loss-making services. Certainly this policy, which has been used by many governments for a long time, is one of the options, but not the only one. It is questionable whether the cost of preserving universal service is as high as many postal organizations claim it to be. To
take an example from another area, the true cost of providing telephone services to uneconomic British customers is about 2 percent of turnover (see Box 2.1). Moreover, a U.S. study concludes that it is likely that sparsely populated rural areas would still have service if the universal service requirement was removed (see Box 2.5 later in this chapter). One of the main forces behind Sweden's abandonment of the postal monopoly was that the cost of the obligation to deliver mail to all areas, including the country's barren north, was roughly offset by the benefits of scale and the advantage of being able to have a nationwide service.

**Box 2.1 Private Delivery of Public Service Obligations in the United Kingdom**

Recent experiences in the infrastructure sectors have shown that regulatory systems can ensure that services that have an element of public service obligation are delivered by private sector firms. The case of British Telecom (BT) in the United Kingdom is a good example. When BT was privatized, it was obliged to provide telephone lines and call boxes throughout the country, including the remotest parts. There are now 122,000 BT call boxes in the country, compared with 86,000 in 1987 (when BT was privatized), an increase of more than 40 percent. There has been a significant improvement in the reliability of phone boxes so that 95.7 percent are now working compared with only 75 percent in 1987. Many phone boxes are not profitable for BT to operate, but BT is legally required to keep them going. At the same time, BT's prices overall have fallen by around 35 percent in real terms since privatization.

Up to the present, governments that have wanted to improve their postal service have concentrated on chipping away at the margins of the state monopolies. It is important to realize that several options are open to governments in terms of setting an effective regulatory policy for the postal sector. It is possible that the cost of preserving the monopoly outweighs the cost of other policies. For example, given that the volume (the main cost driver) of mail collected or delivered in sparsely populated areas is relatively insignificant in comparison with total mail volume, it may be cheaper for the government to subsidize remote users of postal services directly than to bear the cost of preserving the monopoly.

The study team made the following observations.

- Very few postal services have introduced regulatory reform.
- The few countries that have studied the costs of service provision have found that the additional cost of adding the public service obligations to the postal service is between 2 and 30 percent of the total cost (under a regime of optimized operations). This points to the feasibility of continuing the public service obligations even under a fully liberalized market regime. (This issue is discussed further in the next section of this chapter.)
• Gaining some knowledge of the cost of service is a prerequisite to designing a regulatory policy. Governments should disaggregate the cost of postal service and analyze the cost components to determine the true cost of providing universal service. In light of the cost analysis, governments should re-examine the costs and benefits of preserving the monopoly. This type of analysis would make it easier for a government to assess the most suitable regulatory policy for its postal service. Only a very few postal organizations or governments have carried out such an analysis.

• There is an increasing trend, particularly among high-income countries, to reduce the scope of monopoly protection in order to widen the non-reserved areas to foster competition. On the other hand, in many countries, particularly in developing countries, no changes have been made to the scope of monopoly protection.

• In most countries the definition of universal service (that is, that all residents of a country should have reasonable access to core postal services at affordable prices) does not relate to optimal service economics. Many countries are attempting to provide the same level of service to all residents, including those in remote areas. In fact, there is no need to provide this level of equality when the cost of truly providing such service is very high. Customers attach greater value to reliability than to frequency of service. Even with a uniform tariff, a rebalanced universal service that is in line with user needs could be provided economically.

• Regulatory reform has the maximum benefit when it is considered as a component of an overall postal service reform. This is particularly true in countries in which the postal service requires considerable upgrading in order to deliver service to acceptable standards. Isolated regulatory reform in such situations could lead to net welfare losses (see Box 2.2).

• There is very little evidence of private sector participation with the view of introducing contestability into the postal sector, although private sector involvement has been used successfully in other infrastructure sectors such as gas supply, power, transport, and water. Even where infrastructure service is provided economically by a single supplier, competition from alternative suppliers for the right to supply the market can improve efficiency. In this regard, it is fair to say that the postal sector has ignored the potential benefits that could be brought in through private sector participation in all or most of the postal operations.
Box 2.2 Deregulation without a Strategy

One country in East Asia completely removed the monopoly protection during corporatization through the enactment of a new postal services act. Prior to the new act, the service quality of the national postal service had been poor: delivery within the metropolitan capital area averaged six days and interurban delivery averaged eight days. Corporatization and deregulation exerted pressure on the post to improve its service levels. Indeed, soon after the new postal act became effective, delivery in the metropolitan capital area was down to four days and interurban delivery averaged six days. Nevertheless, these new service levels are not satisfactory from the viewpoint of the market, particularly the business market segment. Therefore competitors (private firms) are gearing up to provide a more rapid postal service at a low uniform price in the main urban centers. Volume losses are expected to be high, and the national postal service is expected to have the burden of mainly servicing the rural segments. Should this be the case, the postal service would find it difficult to provide a truly universal service at low cost.

The government’s mistake was to hope that the new postal act and the removal of monopoly alone would be sufficient to improve the quality of service of the post. Although the new act provided the correct incentives, the postal service was unable to introduce the needed changes rapidly because of insufficient investment capital and lack of the institutional capacity necessary for implementing the transformation.

The government is now undertaking a comprehensive postal service reform in order to strengthen the capacity and capability of the postal service. This reform includes the mobilization of private capital, so that universal service at low cost is ensured in a completely deregulated environment.

Competition Policy and Public Service Obligations

The public service obligation (which includes the provision of service to residents in remote areas) is perhaps the overwhelming “policy bottleneck” in keeping competition out of the sector.

However, the experiences of other infrastructure subsectors indicate that it is possible to inject competition while continuing to provide those activities that are considered public service obligations. To address this issue, it is useful to divide the overall postal service business into two segments—commercial service and public service.

1. **Commercial Service Segment:** This is the commercially viable business segment of the postal service which is capable of generating adequate revenues to cover the service’s operating and investment costs. This business segment should be run primarily on market-based pricing principles (even with uniform tariff constraints). There is no need to subsidize any of this portion of the postal service. If the postal operator is making a loss in this segment, it is because of bad management practices or restrictions on economic tariff increases by the government for political reasons, or both. The commercial service segment includes most letter mail, almost all parcels, Express Mail Service (EMS), most counters, and most giro services. This segment represents about 70 to 98 percent of the postal service in value terms.
In high income countries, where the postal volume is relatively high even in sparsely populated areas, commercial service represents a high proportion of the total business (about 85 to over 98 percent), whereas in developing countries the figure is much lower (typically about 70 to 75 percent of the total business) (see Figure 2.1).

**Figure 2.1**
**Broad Segments of the Postal Service Business**

<table>
<thead>
<tr>
<th>70-98%</th>
<th>2-30%</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Commercial Service</strong></td>
<td><strong>Public Service</strong></td>
</tr>
<tr>
<td>- Most letter mail</td>
<td>- Letter service to remote areas</td>
</tr>
<tr>
<td>- Parcels</td>
<td>- Some regional post office counters</td>
</tr>
<tr>
<td>- EMS</td>
<td>- Frequency of service</td>
</tr>
<tr>
<td>- Most counters</td>
<td>- Newspaper distribution</td>
</tr>
<tr>
<td>- Most giro services, etc.</td>
<td>- Literature for the blind, etc.</td>
</tr>
</tbody>
</table>

2. **Public Service Segment:** This segment of the postal service business is legally required from the postal operator as services to be carried out for the benefit of the less privileged portion of the residents. Thus, typical business activities that fall under this segment include letter mail service to sparsely populated areas, maintenance of regional post office counters in such areas, newspaper distribution to all rural parts of the country, and distribution of literature to the blind. These are unprofitable activities; they bring either no revenues or revenues that fall far below the fully allocated cost of service. The public service segment represents about 2 percent (in high income countries) to 30 percent (in low income countries) of the total business.

A key factor in determining policy regarding the scope of monopoly and the degree of competition to be allowed in the sector is the percent of total postal business that belongs to the social service segment. In high income countries, the percent of total business represented by the social service segment is very low. Thus, it is economically feasible and politically palatable to remove the postal monopoly completely and still continue to provide the public service obligation at the same level (see the Sweden Post case study and...
Box 2.4). There is a belief, however, that in developing countries this social service segment represents a very high percentage of the total business (because of lower mail volumes and a greater proportion of rural population). It should be noted, however, that most of the mail-generating customers in developing countries are in the urban areas that there is relatively little mail flow to or from sparsely populated areas, and, in fact, the social service sector’s percentage of total postal service business ranges from about 10 to 30 percent.

The activities and costs relating to the social service segment, once isolated, would provide a sound basis for determining the explicit subsidies to the postal operator for these non-commercial functions. The subsidies could be channeled from the appropriate government ministries. For example, subsidies for the distribution of newspapers to rural areas and literature to the blind could be provided by the Ministry of Education, while subsidies relating to universal service could be provided by the Ministry of Communications, Transportation, or Public Utilities. To negotiate the terms of such subsidies efficiently, it is necessary to understand the cost of providing the entire postal service, and, in particular, the cost of providing the public service obligations (see Box 2.3).

Box 2.3 Transforming the Retail Network in New Zealand

New Zealand Post has implemented a significant reconfiguration in composing its retail network away from company retail outlets to private sector agencies. With restructuring, although the number of official post offices has decreased (see figure, below), contact points for basic postal services have increased dramatically. Although the postal service is corporatized, the Deed of Understanding with the government mandates the maintenance of the retail network at specific levels. For example, in 1990 the Deed required a network of at least 880 outlets excluding stamp retailers. An amendment of the Postal Act also mandates that the Post furnish information about its retail network. An amendment to the Postal Act also mandates that the Post furnish information about its retail network. This reconfiguration of the retail network (1987 and 1991) is shown below in the figure.

Therefore, although the level of service cannot be compromised, the postal service is allowed to be the best judge of this kind of retail network that can best service the population, given the demands for its services and the costs of providing them. If the case arises in which economically unviable outlets are required to be maintained on social grounds, the government has the option of explicitly compensating the Post for these outlets, thereby reconciling the retention of financial accountability with social accountability.
A thorough cost analysis is one of the prerequisites for any policy decision, particularly in the postal sector. Since most government departments do not follow commercial accounting principles, a special effort (through, for example, an Activity Based Costing Method) should be made to isolate cost by product or service category. Such a cost analysis could provide the policymaker with most of the necessary information on the postal service with regard to which regulatory policy is best suited to that country's postal operation.

Sweden was one of the few countries that undertook a cost analysis (in 1991) to evaluate the cost of its regional and social responsibilities within the Sweden Post letter mail and the Post Giro business units. The intent of this analysis was to have a better understanding of this business and also to collect the information that would bring about a more businesslike relationship between the Post and the government on some of the critical issues such as social responsibilities. The government encouraged this analysis in order to better determine the most appropriate regulatory policy for the country (see the Sweden case study and Box 2.4 for further details).

**Box 2.4 Deregulation in Sweden**

In the early 1990s the Swedish Government authorized a systematic analysis of the postal market by an independent consulting firm. This analysis divided Sweden Post's obligations into three categories and recommended the following responsibilities:

- **Social responsibilities in the letter service:** This encompasses delivery of newspapers, and of literature for the blind, elderly, and disabled, emergency situations; letters to other Nordic countries; letters sent by non-profit associations, etc. The study recommended that (1) for newspaper and stamp delivery, temporary subsidies should be paid by the relevant ministries and rates should be gradually raised to market prices; and (2) for the remaining social obligations, Sweden Post should receive full cost compensation from the relevant agency or ministry.

- **Regional responsibilities in the letter service:** This covers Sweden Post's obligation to provide nationwide service at a single unitary tariff with a 95 percent delivery reliability for overnight mail. It was concluded that the economic costs associated with these regional obligations approximately equaled the benefits of economies of scale and scope that Sweden Post enjoys. Since Sweden Post's profitability could cover the provision of these services in sparsely populated areas, no compensation was recommended.

- **Regional responsibilities for cash payments:** This assesses the costs incurred by Sweden Post in providing a cash payment service for the state on a daily basis in areas where no bank is available. The study recommended that the Postal Giro be compensated for the extra cost of maintaining this service.

On the basis of this analysis and for reasons provided earlier, it was decided that the monopoly protection was no longer necessary even though the universal service would be maintained. By 1995, apart from Sweden Post there were two companies operating letter or combined letter and parcel services, one delivering computer-produced letters in the Stockholm metropolitan area and the other with a large share of unaddressed bulk mail. A few international integrators and postal administrations have also evinced interest in entering the Swedish postal market. As far as Sweden Post is concerned, it is not competition from alternative operators that it fears but competition from alternative forms of communication.
The social responsibilities that Sweden Post felt should be directly subsidized by the government represented only 2.7 percent of its turnover. This was the cost of providing the public with all the social obligations set by the government. In addition, Sweden Post felt that no further compensation was required from the government to provide a regional universal service. Sweden Post concluded that the letter business unit’s profitability was sufficiently high to cover the costs of servicing sparsely populated areas, even after a price structure adjusted to market conditions was introduced. Consequently, Sweden abandoned its monopoly in 1993.

Sweden Post offers a good example of the importance of developing a robust understanding of the costs of the various activities of the postal service and the various costs of the social responsibilities that it must continue providing as a national operator. Such an understanding provides a good basis for enabling both the government and the operator to take the most appropriate and commercially logical decisions that are beneficial to the operator as well as to the customers.

Universal Service

One of the first steps in regulatory reform is to clarify the definition of universal service in view of its social and economic justifications. Cost is directly related to the level of service. It is no surprise that, under universal service as defined earlier in this chapter, many postal operators have a relatively high cost of service and a considerable overcapacity of network resources, including labor. Market surveys of customer preferences indicate that users in developing countries attach greater importance to the reliability of the service than to the frequency of service. This preference is greatest in countries where there is a poor level of service. When reliability is no longer an issue, user preference is focused on frequency, and users are willing to pay a premium for more frequent service. Therefore, it is important to understand the minimum customer requirements and the delivery economics of providing a certain level of service. This could mean that every resident in a country has easy access to the core postal services but that the frequency of service varies (within predetermined limits) depending on the distribution cost structure. Such a system can receive public acceptance as long as assurance is given with regard to reliability of service. Box 2.5 gives the results of a U.S. study on rural delivery service.

1 From a 1993 market survey in 25 countries, by respective postal administrations.
Box 2.5 Rural Delivery in the United States

The need to offer an economical postal service that is universal has been the principal argument used by postal administrators and governments to justify the continuation of the service under government control and supervision. In a recent quantitative study, the U.S. Postal Rate Commission analyzed rural delivery costs in the United States and compared them with urban delivery costs. The study concludes that it is likely that if the universal service requirement were eliminated in the country, even sparsely populated rural areas would still receive service. This is primarily because, in the U.S. postal system, there is no real difference between city and rural addresses in carrier time required, and the revenue from mail delivered to rural areas as a whole exceeds the cost of handling and delivering that mail.

The average time per day per delivery is 1.04 minutes for city delivery and 1.07 minutes for rural delivery, primarily because businesses require more time per delivery than do residences (the average delivery time on business routes is five times the carrier time of that on residential routes); in addition, city routes have a high proportion of business deliveries. This business delivery time is high because: (1) businesses receive almost three times as many pieces per delivery as do residences; (2) in business areas carriers travel by foot; and (3) there are no "curb delivery" routes in business areas. As a result, rural carrier time per delivery is only 10 percent higher than city residential route delivery time. Other factors come into play as well; the labor cost on city routes is slightly higher because of wage differences and higher overtime work and delivery vehicle costs for rural routes are lower because carriers use their own vehicles for delivery and are paid an allowance, whereas for city routes the postal service has to maintain a delivery fleet.

Although these results may apply only to the United States (where the per capita annual mail volume is very high—over 600 pieces), and although it is difficult to extend the analysis to assess the impact on the cost equilibrium if the universal service requirement or the monopoly were to be removed, the study raises some useful points for policymakers. The results of the study lead to the following conclusions:

- Traditional beliefs, particularly about universal service and monopoly requirements, may be questioned in the future by governments which are hard pressed for resources and looking to redefine public service obligations.
- Appropriate policy actions should only be taken after careful analysis of cost structures and cost dynamics of service provision.
- Even when there is a significant cost difference between urban and rural deliveries, the difference could be closed by altering the service level for the rural residents.
- There may be no need for the government to run the postal service in order to ensure universal service provision—it is a matter of cost-service optimization. The government's role is more valuable in providing the most appropriate legal and regulatory framework.


In sparsely populated areas, where the cost of delivery is relatively very high, one way to determine user preferences is for the users themselves to define the service level. Rural communities could thus determine the minimum level of service acceptable to them. If the cost of service is above what is dictated by the economics of providing an optimal universal service, the postal operator could either negotiate a service level within the delivery economics with the rural community, or the rural community could pay the excess of the cost of providing an optimal universal service (for example, via semian-
nual explicit appropriations through local or property taxes). In fact, the rural community could demand any array of services at any frequency and pay the difference in cost (see Figure 2.2). Such community-based "market-driven" service provision has been effective in other infrastructure subsectors, particularly in rural water supply and sanitation.2

Thus, if a good quality postal service is to be provided at low cost, governments should focus on the elements of universal service, such as universality, affordability, and confidentiality of core services, and should give less importance to providing an equal level of service to all residents.

Figure 2.2
Market-Driven Mapping of Universal Service

Relative cost of providing different levels of service

Optimal cost of providing a universal service to a rural community

Efficient cost of providing postal service to a rural community

Cost of serving community preference

Option 1: Renegotiated service level (lower service level than preferred)

Option 2: Excess cost of service met by community (higher service level)

Direct cover of excess cost by the community

Monopoly Scope

As Chapters 3 and 4 demonstrate, enterprise reform can bring about cost and service improvements only up to a point. Beyond that, it is necessary to address the issue of the most appropriate regulatory policy for the postal service. The central theme in this regard is competition.

Postal services are usually given some form of exclusive privilege or protection regarding certain aspects of the postal market. The rationale is to allow them to capture the monopoly benefits associated with being the sole provider of the service in order to compensate for the universal service requirements imposed on postal services. Thus, service requirements are funded by a cross-subsidy within the letter service which spreads the cost of providing the service across all

2Perhaps one of the most famous cases is the Orangi project in Pakistan for the provision of sewerage services. There are numerous other examples.
postal users. It is argued that it is impossible to provide a nationwide postal service at reasonable rates without this monopoly protection. This is a much studied, much debated, and controversial issue in the postal sector.

If some extent of protection for postal services is to be retained, the scope of these exclusive privileges should be based on a careful consideration of the cost of the primary obligations and community service obligations of the postal service and the availability of alternative services. This decision will also be heavily influenced by the government's philosophy regarding the extent to which free market forces are beneficial to the development of the postal sector as a whole. The scope of the exclusive privilege may be narrower than the scope of the obligations, since the rationales for the two differ. A typical example is the case of parcels, which might be part of the universal service obligations and at the same time a competitive area as well.

To define the scope of the exclusive privilege given to postal administrations, a combination of various criteria is used. The basic classification is that of content or type of product: for example, parcels, which are goods-bearing items, are usually excluded from the monopoly, and international mail is also increasingly exempt from the reserved areas. The next criterion is weight. For example, in the EU the limit applied ranges from 0 g (no protection) to 2 kg. Some administrations apply a price criterion; this is the case in the United Kingdom where the upper limit for the exclusive privilege of the postal area is set at a value of £1. Still other countries protect their postal services by applying a price threshold above which competitors must price their products. Several combinations of weight and price protection are also used in defining the scope of the monopoly area (see Table 2.1 in this chapter and Annex 1 in Chapter 3 for examples).

For a postal service that is part of a government department, a broad approach is usually used which reserves a wide range of services and specifies exceptions. However, when a monopoly is being granted to a postal service operator through enabling legislation and a licensing/concession process, the normal approach is to specify the minimum essential extent of exclusive privileges. The geographical extent of the monopoly protection also needs to be specified. The definition of exclusive privileges must recognize reality, such as the existence of couriers and document exchanges and the need for their continued existence given the commercial demand for their services. It is important that legislation clearly specify the extent of the monopoly protection. More important, it should be borne in mind that monopoly protection does not serve its purpose unless it is enforced. Lack of enforcement undermines the government's credibility, creates an uncertain regulatory environment, and works to the detriment of postal development (see Box 2.6).
Redirecting Mail: Postal Sector Reform

Box 2.6 The (Chaotic) Legal and Regulatory Framework in Chile

The regulatory situation is unique in Chile in that the legislation applying to the exclusive privileges of the postal service (Correos de Chile) is contradictory and is not enforced. In addition, the interpretation of activities or businesses that the post may engage in is subject to interpretation of the Postal Law, which is very broadly worded.

The Postal Law (as written in 1960) provides for a monopoly over “pieces of mail,” fairly ambiguously defined as encompassing items such as letters, newspapers, packets, and documents. Thus the Postal Law spells out the obligation of the post and the exclusive privileges it enjoys over the provision of postal services. However, in 1980, during the era of military rule, a “Supreme Decree” was issued by the government allowing for the private carriage of mail. This decree still has the full force of law and is thus in direct contradiction to the Postal Law. Correos de Chile serves as the regulator in terms of the 1960 Law and is responsible for enforcing its own monopoly. However, it has chosen not to do so, because there is strong support for private business in Chilean culture, and the Supreme Decree has created a situation in which the success of any attempt to enforce its monopoly seems doubtful.

Consequently, Correos de Chile is faced with intense competition from a host of small local private postal companies, local and national bus companies, and international courier companies. In fact, Chile Express, a subsidiary of the former government telecommunications corporation, which has been privatized, also competes with Correos de Chile in the provision of mail.

In addition, the business and commercial activities that Correos de Chile may engage in are subject to the approval of a government body known as the General Controllership. This body has defined Correos de Chile’s role very narrowly by limiting it to providing traditional postal services only, as specified by its 1982 legislative mission statement and further defined by the definition of “pieces of mail” in the 1960 Postal Law. Thus, Correos de Chile is prevented from expanding its range of agency services or from providing electronic and hybrid services.

Thus, severe structural and regulatory constraints limit the postal service’s operating autonomy and prevent it from enjoying the commercial freedom that its competitors enjoy. Correos de Chile has commercialized its operations to the maximum extent possible within the current structure. However, beyond a certain point, a level playing field is necessary in terms of the competitive and regulatory environment for Correos de Chile to remain viable.

While only a few countries (for example, Finland, Sweden, and Argentina) have completely removed monopoly protection for their postal services (see Boxes 2.4 and 2.7), there is an increasing trend toward reducing the extent of monopoly protection for postal administrations (see Table 2.1). It is argued that regulation of a monopoly is generally less efficient than are market forces in ensuring the acceptability of services. Free choice on the part of the customer will bring success to services that provide value for the price. This phenomenon can be seen with parcels and express mail service, which are generally competitive services. In a government department with monopoly protection, there may not be sufficient incentive to compete effectively in delivering services and in restraining costs. However, in a commercial structure with explicit profit and service targets, the threat of reduced monopoly protection provides strong incentives for ensuring a competitive postal service.
Table 2.1
Who's Liberalizing?

<table>
<thead>
<tr>
<th>Country</th>
<th>Letters</th>
<th>Parcels</th>
<th>International Mail</th>
<th>Express Mail</th>
<th>Electronic /Hybrid Services</th>
<th>Agency Services</th>
<th>Publications /Documents</th>
<th>Consolidated Rerouting /Interconnection</th>
<th>Direct Marketing /Bulk Mail</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Zealand</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
</tr>
<tr>
<td>Australia</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Singapore</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td></td>
<td>✔</td>
</tr>
<tr>
<td>Argentina</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sweden</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Finland</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td>✔</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Key:
☑ = Allowed
☒ = Not Allowed
❖ = Restricted

Notes:

New Zealand: In New Zealand, liberalization of the postal market was planned in three phases: (1) in 1985, weight protection was lowered from 500 g to 200 g and price protection was NZS1.25; (2) in 1990 price protection was reduced to NZS1.00; and (3) in 1991 price protection was further reduced to NZS0.80. This is the current protection level against a letter price of 45 cents charged by the Post in 1994. In 1991, 53 percent of revenue was generated from competitive product segments. At some future point, full deregulation and privatization of the Post are also to be considered.

Australia: In Australia, in 1994: (1) weight protection for letter mail was reduced from 500 g to 250 g and (2) price protection was reduced from ten times Australia Post’s standard letter rate (45 cents) to four times the rate. Other areas which have been completely deregulated include: outward international mail, interconnection by bulk mailers at specified mail centers (see Chapter 4), transfer of intra-company mail by third parties, movement of documents within an exchange network, and catalogues and leaflets. In 1996 a further review will assess whether the letter monopoly should continue. Forty-five percent of the revenue was generated from competitive areas in 1994.

Singapore: The exclusive 15 year license that Singapore Post has on the delivery of mail expires in the year 2007. Apart from letters and postcards, all items are open to competition in 1993-94. In 1991, 56 percent of the postal volume and 67 percent of the total revenue was generated by monopoly items. Singapore Post is sensitive to the expiration of its exclusive license in 2007. In order to prepare for this, as well as for the ongoing competition from technological advances, the Post is trying to wean itself from reliance on its monopoly product.

Argentina: See Box 2.6.

Sweden: See Box 2.4.

Finland: While the postal market has been completely deregulated in Finland since 1994, Finland Post was the only license holder for the provision of mail.

Often there is resistance to liberalization on the grounds that the bulk of the population lives in rural settings and the financial burden of providing a universal service merits the monopoly protection. This argument is questionable for two reasons:

1. Even in countries in which the majority of the population resides in rural areas, the bulk of the mail is generated and received by the commercial and government sectors which are easily accessible.

2. If the government explicitly compensates the postal service through a direct budget subsidy for the economically unviable services that it has to perform, there is no justification for the continuation of monopoly protection. The cost of such a
subsidy may be a lot less for the government than preserving existing monopolies intact. Terminating the monopoly protection would also promote transparency and clarity, and would provide incentives for efficiency. Certainly, it is worthwhile calculating the costs and benefits of either approach.

Additional country examples of the scope of monopoly protection are given in Annex 1 to this chapter.

---

**Box 2.7 Deregulation in Argentina**

In June 1994, after a careful analysis of the different options for the postal market, the Argentine government completely eliminated Encotesa’s monopoly on letter mail. In fact, since the 1970s a system of private permit-holders, “permissionaries,” had been servicing the postal market in Argentina. In spite of much higher prices, the private sector had captured 49 percent of the postal market by 1993. In 1994, approximately 250 private firms serviced the postal market, although four private competitors (allegedly with common ownership) serviced almost 90 percent of the private share.

The deregulation was undertaken for the following main reasons:

- Although Encotel had a statutory monopoly on letter mail, this had never been enforced.
- It is believed that the postal business does not differ widely from other business fields and is subjected to strong competition from other services. The free market model being adopted widely in the rest of Argentina is thus being extended to the postal sector.
- The government feels that the market should dictate whether the postal service should be a monopoly because of the network scale economies and synergies among the various postal products. If these economies are indeed valid, the industry is likely to evolve into a few major competitors with some niche players. The removal of the legal entry barriers to the market will introduce, in addition to direct competition, the element of contestability, which will prevent abusive price practices that adversely affect the society.

The government, through the deregulation of the postal market and its commercialization program, has realized the following significant benefits:

<table>
<thead>
<tr>
<th></th>
<th>1993</th>
<th>1995</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total volume of mail</td>
<td>449 million</td>
<td>645 million</td>
<td>+40%</td>
</tr>
<tr>
<td>Revenue</td>
<td>ArgS775 million</td>
<td>ArgS 968 million</td>
<td>+25%</td>
</tr>
<tr>
<td>On-time Delivery</td>
<td>72%</td>
<td>98%</td>
<td>+27%</td>
</tr>
<tr>
<td>Average price of delivery of mail</td>
<td>ArgS1.75</td>
<td>ArgS0.60</td>
<td>~65%</td>
</tr>
</tbody>
</table>

---

**Interconnection**

Interconnection is another means of introducing competition into the national postal network, particularly in the upstream activities of the postal service. Like the telecommunications, electric power, transportation, and gas supply sectors, the postal service is a network industry. This network structure has important implications for the analysis of efficient industry structure in the market for postal services. The provision of postal service requires few specialized facilities. As a result, the exit barriers are low since most of the postal service’s assets, such as land, buildings, and vehicles, could be dis-
posed of quite easily. Thus, there are low sunk costs involved in providing postal services. Box 2.8 discusses some advantages of interconnection as it applies in Australia.

**Box 2.8 Interconnection in Australia**

In 1994, the Australian Postal Corporation Amendment Bill was passed to liberalize the postal sector. Further mail services were opened to competition and protection was removed in several other areas. A key feature of the amendment of the Postal Act was the introduction of "interconnection."

Interconnection permits bulk mailers to bypass the Post's linehaul transport service and lodge their pre-sorted mail at designated mail centers for delivery by Australia Post. This gives businesses greater choice and incentive to interconnect with Australia Post's network rather than to lodge their mail at the nearest post office. Mail interconnected in this manner will receive discounts for the pre-sorting and drop-shipment services performed. Australia Post has developed pricing arrangements to offer interconnection discounts based on avoidable costs. The current pricing arrangement is based on three letter sizes for bulk mail (medium, large, and extra large), and each letter will also have "Same State" or "Other State" pricing.

While this limited access regime does not constitute complete deregulation of this activity, it does permit bulk mail customers of the Post to perform the sorting and certain aspects of the delivery operations by themselves. The provision of discounts increases the incentives for these customers to continue to use the Post for their mailing purposes. Complete interconnection, however, would also permit consolidators, integrators, and all mail carriers to access the postal service network.

The postal service in almost all countries is a vertically integrated industry. Rather than looking at the service as one integrated business, it is more meaningful to examine the postal network in terms of separable components. The postal network, in a stylized form, has five components: retail services, collection, sorting, transportation, and delivery.

It should be noted, however, that there is a basic asymmetry between the inward and outward movements of mail. Several studies have indicated that there are significant economies of scale in the delivery function. In addition, it is generally believed that there are substantial economies of scope between delivery and collection. The physical network associated with delivery could be utilized for the collection function as well, which would do away with the need to duplicate the fixed costs of delivery to carry out collection. However, the peak load nature of the postal service may give rise to a stronger form of economies of scope. The distribution of the arrival of mail for inward delivery (final delivery to destined addresses) has a peak pattern; mail arrives at set times, within a narrow window of time, in bulk, throughout the day. The distribution of the arrival of mail for collection, on the other hand, is even throughout the day. The staffing level and operations are usually planned to absorb the peaks of the inward delivery work load. This gives the post office extra capacity to pro-
cess outward activities during periods of little or no delivery activities. This shared, synergistic capacity relationship between inward and outward mail flows has a significant impact on the incremental costs of both. The economies of scope found in collection and delivery are stronger than those resulting from the mere sharing of resources and overhead.

Free entry, though a necessary condition for economic efficiency, is not always sufficient to stimulate the needed competition, and may not be possible to implement immediately. In particular, where there is a sustainable natural monopoly, there is a need to consider innovative means of extending competition. The most important innovation in telecommunications, electricity, and gas has been the realization that there is no compelling reason why the monopolist should have an exclusive right to use its distribution network.

Today many cases of such vertical "unbundling" exist in infrastructure sectors, particularly in telecommunications, gas, and electricity. The postal service is another sector in which vertical unbundling could help improve the efficiency of service delivery. In the postal service, this would mean that the pricing of postal service components is unbundled and access to each essential monopoly service component is priced on a nondiscriminatory basis.

The real issue at stake is to determine nondiscriminatory terms of access to each of the post office's postal network components. For example, let us assume that a new private entrant wishes to compete with the post office in undertaking all postal activities except the local delivery function and would like to access the post office's local delivery network for final delivery. For the sake of simplicity, if it is assumed that the financial objective of the post office is to break even, under a regime of nondiscriminatory access pricing the rate that should be applied to the private entrant is the average-cost bundled rate less the incremental unit cost of all nondelivery functions. This rate should be available to any competitor willing to deliver pre-sorted, route sequenced mail to the loading dock of a local post office.

The policy framework as described above is capable of ensuring that a competitor at least as efficient as the existing postal service has the appropriate incentive to enter the market. It could be argued that competitors might capture all of the gains of efficient entry under the regime of efficient access pricing. It should be noted that nondiscriminatory access pricing merely requires that there be equal terms of access to the delivery network for competitors and for the relevant portions of the post office's network. The level of the nondiscriminatory access charge is determined by the (regulated) profit requirements of the enterprise. In fact, under such circumstances, a local delivery monopolist (i.e., the post office) could earn the maximum possible monopoly return without providing nondelivery services except in cases where it is the low cost producer.
Certain issues may need to be addressed when equal network access to postal competitors is introduced. In almost all countries there is significant averaging of costs in postal services, owing to the requirement for universal service with a geographically uniform tariff structure. The costs of service could vary significantly across market segments, and there is a high degree of cross-subsidization among addresses of different geographical areas and among high volume mailers (i.e., businesses) and casual mailers (i.e., residential). In most countries there is a simple rate structure based on a geographically uniform tariff. A critical issue, therefore, would be the degree of cross-subsidization that governments would wish to see retained among the different market segments. The more governments wish to retain cross-subsidy, the more complex the access charging arrangements will have to be in order to fund cross-subsidy.

It is clearly evident from the study’s worldwide review of tariff structures and pricing principles that the pricing policies being adopted by most postal services are ineffective and are detrimental not only to the development of the sector as a whole but also to the survival of the national postal service itself. It is not the intent of this study to recommend pricing policies—it is a matter that should be left in the hands of the respective policymakers. However, the study has identified two primary policy issues in the field of pricing: (1) price rigidity, and (2) regulatory pricing.

- **Price Rigidity:** Most postal administrations, in accordance with the embracing legislation, have a fixed pricing structure that varies according to the class of service or to volumes. For example, for a large mailer prices are determined according to a pre-formulated table of discounts relating to volumes. The postal service does not have the flexibility to deviate from this pricing structure. As the monopoly scope is being reduced and more competition is being introduced into the traditional service areas, postal services are finding that they are crippled by this price rigidity. As a result, the competition, which often prices each customer individually according to operating profit contribution, can easily capture the large accounts. This practice is evident in many countries in which the monopoly scope is being reduced to allow competition into certain market segments. Thus, it becomes important to ensure a level playing field in the area of pricing. If competition is brought into previously protected market segments, then the legislative framework should be altered to ensure that the postal administration may make decisions, including pricing decisions (within a regulated framework), on a commercial basis. Achieving this objective may be difficult until the postal service retains a mo-
nopoly or exclusive privileges in any segment of the postal market, because the competition could (and does) allege that a monopolist can abuse its privileges by cross-subsidizing the "commercial" market segments with "protected" market segments.

- **Regulatory Pricing Regime:** As has been mentioned, nondiscriminatory access pricing is an important means of introducing competition into postal service provision. If all service providers were charged the same price for access to and usage of the postal network, any differences in their costs would be due to differences in their efficiency in providing the service. If the competition should force prices to costs, then by choosing the lowest cost carrier the final consumer could ensure that the costs of the postal network would be minimized. In this case, it would be necessary to determine unbundled rates for collection, outward sorting, transportation, inward sorting, and delivery. These rate elements would have to be established for each class and category of service. The competitive service providers could then choose any segments of the network (see Figure 2.3). If such a system of unbundled service component rates is to enhance the efficiency of the (public and private) postal network, the main issue is reduced to determining nondiscriminatory terms of access for the postal service's local delivery network. Under a regime of nondiscriminatory access pricing, the postal service would pay the same rate for access to the local delivery network as would any of its competitors.

![Figure 2.3](image.png)

**Figure 2.3**

Nondiscriminatory Access to the Postal Network
In the interests of social welfare, the revision of postal tariffs has traditionally been subject to government approval. The increasing separation of the postal service operator through the process of corporatization, combined with the retention of some monopoly services, gives the issue of regulating postal tariffs significant relevance. This regulation has been considered essential to prevent the potential abuse of monopoly powers by the postal operator, in terms of both overcharging customers for its monopoly services and cross-subsidizing competitive services, thereby deterring entry into other market segments through predatory pricing. Nevertheless, it is also recognized that regulation should give the postal service the highest possible degree of flexibility in business decisions, and should permit it to retain incentives to achieve efficiencies and provide high quality innovative services.

The usual mechanisms in place for price regulation are the requirements to achieve overall cost-recovery and an approval process for price changes proposed by the postal administration. In some cases there is a further requirement to be profitable in individual products, or across monopoly and competitive segments, in order to avoid the potential for cross-subsidization. At one end of the spectrum, full control for any revisions to the tariffs of reserved services may lie with the relevant ministry or with an independent authority. On the other hand, the postal service operator may be permitted to change prices within a certain limit, such as following a price-cap scheme (RPI-X formula).

Corporatization has brought a more commercial approach to postal management and therefore a less intrusive, bureaucratic, and politically driven rate-making process is required. Price caps have the benefit of containing built-in incentives to achieve cost reductions while giving the postal service entrepreneurial and commercial freedom within a clear regulatory framework. However, price caps will be effective only if: (1) the postal service is the residual claimant of profits (once all expenses, including financial returns to its owner, are covered); and (2) the postal service is given full autonomy to achieve efficiency improvements and cost reductions.

It is increasingly evident that only the prices of monopoly services require regulation, and that the pricing of services considered competitive (such as courier and parcel services in general) should be left to the commercial judgment of the postal service board or management. (This is also increasingly the practice.) Market forces should ensure that the prices for competitive services are not set too high. In addition to the pricing of monopoly services, the following may also require specification with respect to price regulation.

- The power to grant discounts for preparation of mail (for example, pre-sorting or drop shipment) or for various commercial reasons should rest with the management.
An overall requirement to operate in a commercial manner and not cross-subsidize between the reserved and unreserved services should be put into place.

Interconnection charges may also be regulated when it is decided that access to the delivery network of a postal service should be provided to competitors in the interests of developing the postal sector as a whole.

In addition to the regulation of tariff revisions, another critical issue in postal pricing is the ability to recover costs. The provision of postal services is often underpriced because of the social, and hence the political, sensitivity of the service, and because cost data are not developed by product segment and therefore cost levels are unknown. It is important that price increases not be utilized as a mechanism to conceal cost inefficiencies. However, it is equally important that, once costs are under control, well-established, commercial pricing principles are used to prevent distortions in resource allocations. For the segment of the population that is dependent on the postal service for personal communication, it is unlikely that the disadvantage of paying in full for the service will outweigh the benefits of improvements in service.

Country examples of tariff regulation are provided in Annex 1 to this chapter.

Regulatory Framework

The concept of regulation is relatively new to the postal field and its relevance has been increasing with the restructuring and growth of competition in the postal sector. The most prevalent form of regulation is where the postal department itself continues to play the role of regulator. In such a case, the department is authorized to delegate its monopoly operations through licensing, if it so chooses. The role of regulation is minimal under such an arrangement because of (1) the lack of explicit contracts with which the postal department has to comply, and (2) the minimal incentive to promote competition. However, once a postal service evolves beyond a government department, impartial and informed regulation will be necessary for the following purposes:

1. To ensure that the universal service is provided according to standards which meet the objectives of government (in terms of accessibility, affordability, and quality of service).
2. To justify the continuation of reserved services and advise the government on the scope of the universal services.
3. To ensure that both the postal service and the government are meeting their obligations.
4. To ensure that fair competition exists in non-reserved areas. Where network access is permitted in a multi-operator
postal sector, the terms of interconnection may also require regulation.

5. To ensure consumer representation, if a separate body does not exist for this purpose.

A major factor in deciding on the form of the regulatory body is that effective regulation requires both independence and integrity. Therefore, it is best if the regulator is seen as independent of both the owner (the government) and the operator (the postal service). The form of the regulator may also be dictated by its cost, the volume of work and expertise involved, and the swiftness required of decision making. Since these factors vary within countries, there is no single blueprint for a successful regulatory framework or body. As a result, there is a vast array of regulatory forms, which can be broadly categorized as follows:

- Within the postal department itself, where the monopoly operator continues to play the role of regulator.
- Where operation is separated from regulation but regulation is retained within a ministry of the government. This usually occurs when the postal service has been corporatized but ownership and regulation have not yet been separated.
- Where there is an “independent” regulatory body which either reports to a government ministry or acts as an independent commission, thereby separating ownership, operation, and regulation.

The division of powers among the owner, the operator, and the regulator is a potential source of conflict. In the interests of the postal service as a whole, it is preferable if the regulator is sufficiently strong and autonomous to be unaffected by direct government controls. The regulator should be concerned in a neutral fashion with all of the operators in the postal market, licensed or otherwise. Therefore, to ensure a level playing field as well as to ensure that all parties are meeting their obligations, the regulator should have access to information from all operators to satisfy itself that the terms of the license are being complied with. It is essential to strike a careful balance between the minimal information required for effective regulation and the cumbersome regulatory requirements that may negate the benefits of both corporatization and liberalization.

Licensing is another form of regulation. Licenses may be issued for a variety of reasons: to provide functions that may be more effectively supplied by a licensee; to enhance competition by opening up certain reserved service areas; to service areas in which the post is not performing adequately, etc. Licensing was regarded as a mechanism to raise revenue for the government, but it is realized increasingly that the treasury will be best served by taxes on a healthy
industry. To this effect, when Argentina deregulated its postal sector it also eliminated the A$0.38 postal fee that private postal operators paid to the government. As far as licensing is concerned, the main powers of the regulator will be to grant licenses, set terms for licenses and ensure that they are being met, collect license fees if they exist, and revoke licenses or impose penalties for noncompliance.

Some examples of licensing are given below.

- In Ecuador private carriers were used to provide services to localities not served, or insufficiently served, by the Post.
- Peru permitted mail delivery by private carriers on the basis of prior authorization and payment of a set fee per item. Chad permitted the same practice for domestic mail conveyance.
- Venezuela has contemplated a domestic licensing agreement with a guarantee of collecting a commission on each item entrusted to the licensee.

Under a deregulated or liberalized postal regime, the function of licensing will be more to register rather than to authorize operators to service the postal market. Under this scenario, active regulation can actually stimulate and promote competition in the interests of the sector far more than can the absence, or presence, of ineffective regulation. By establishing the rules of the game and ensuring that the game is played according to the rules, the regulator promotes transparency in the market, which renders the optimal amount of market entry feasible. It is natural that the incumbent postal service operator will possess considerable advantages owing to its sheer size, its experience, and its monopolistic access to the postal network. Potential market entrants will be hindered by a lack of information concerning cost and revenue information; consequently, it is vital that the regulator establish ground rules and methodological principles to be used in establishing interconnection. The regulator will also have to ensure that the postal operator is not abusing its monopoly position to cross-subsidize services that are competitive, thereby eliminating competition.

The central purpose of removing the postal service from direct government intervention and controls, thereby granting it greater autonomy and flexibility to operate, will be defeated if a stifling regulatory regime is imposed. Therefore, it is better if the regulation is output-based or result-based rather than applied through direct interference in the operations of the postal service. The functions of a regulator should be confined to ensuring that government policy is implemented in the entire postal sector and that the postal sector develops in the interests of the nation as a whole.

Country examples of regulatory frameworks will be found in Annex 1 to this chapter.
The postal sector, in its reform efforts, needs to rethink many of the traditional designs relating to the regulatory policy aspects of postal service and to craft a regulatory policy that is meaningful and is also responsive to the many changes that the sector has undergone and is undergoing in terms of industry and competitive structures. Policymakers in the postal field should consider the seven points detailed below.

- **Introducing Competition.** In many low income countries, where the postal market is still not well developed (i.e., where mail per capita is relatively low), *it may not be prudent to remove the monopoly completely.* However, in these countries competition can and should be introduced in segments of the postal market such as parcels, EMS, and parts of the letter mail. Thus, the scope of monopoly should be reexamined with a view to its reduction. As the postal market becomes more developed, the low and middle income countries will have greater flexibility regarding the monopoly scope. Argentina, which has completely removed monopoly across the postal service, has set a precedent for a feasible approach for those countries with high mail volume.

- **Licensing Exclusive Privileges.** Governments that prefer to maintain a monopoly for a portion of the postal market or other exclusive privileges should only do so on a *licensing arrangement with an operator.* The license grants the operator the privileges for a fixed period of time only. Such licensing arrangements do in fact limit the “market guarantee” for the operator. At the end of the licensing period the government should review the regulatory situation again to determine the way to proceed.

- **Redefining Universal Service.** *The definition of universal service should be redesigned* as one of the prerequisites for reform. In defining the level of service and service standards to be provided to rural residents of a country, the economics of delivery should also be considered. Otherwise, it would be difficult to sustain a low cost service for the entire postal operation.

- **Unbundling Costs.** Whether the postal service is planning on providing nondiscriminatory network access to competitors or not, *unbundling the total cost of the postal service across its value chain,* from collection to retail operations, is a worthwhile exercise. This not only provides a basis for determining the best means of introducing competition, but it also helps to quantify the social obligations that the postal service is required to carry out on a fully allocated (activity) cost basis.
- **Pricing the Social Obligations.** Delivering mail to and maintaining outlets in remote areas of the country, together with providing non-commercial services to certain groups of the population, should be costed in order to understand the impact of these obligatory services on sustaining a commercially oriented business. If necessary, direct payment for these services should be sourced from the government.

- **Introducing a Flexible Pricing Regime.** Although prices and price development should be regulated, it is important to give the postal operator the flexibility to respond to market preferences and competition. This means that the traditional approach of not being able to deviate from a predetermined, rigid table of tariffs should be abandoned. As long as monopoly is reduced or removed, the freedom to set commercial prices and to flexibly price the services also becomes increasingly feasible.

- **Establishing a Regulatory Regime.** The regulation of the postal service, or, indeed, the regulation of the postal sector, should not be left to the postmaster general, or to any agency that is directly linked to the post office. A clear, transparent regulatory regime should be established and the regulator should be located in as independent a place as possible. It is important to “privatize” as many as possible of the audit functions (for example, the audit of service quality) by using external auditors. Many of the regulatory “f Freedoms” (such as providing pricing flexibility to the post office, allowing the postal service to enter other businesses) are linked to the controls that governments typically impose on the postal service. These controls are in principle imposed because the risks assumed by state-controlled postal services are ultimately underwritten by the taxpayer. In particular, government controls over borrowing by the post office provide a discipline over all funds that are raised with the backing of the taxpayer and for which the government is ultimately accountable. Without such controls, a nationalized postal service would have a clear advantage over commercial rivals, both in competing for business and in raising new funds on capital markets. Public sector controls are designed to prevent public corporations from exploiting this privileged position. Given the nature of the commercial activities into which the postal services should plan to extend their business, governments would find it difficult to free the postal service from all controls as long as the service remains in the public sector.

For this reason, and for many others that have been cited in Chapter 1, it is important to institutionalize commercial freedom in a post office as early as possible. Many of the high income countries that have achieved commercial freedom have done so after 10 or 15 years.
of reform effort. The postal sectors of many developing countries do not have the luxury of spending 10 years on the reform of their service. The quickest and easiest way to achieve commercial freedom (as is noted in Chapter 1) is for the postal service to bring in the private sector to manage and finance its operation. Thus, the ability to incorporate many of the regulatory aspects discussed in this chapter is closely linked to the establishment of an appropriate institutional framework.

In most countries the postal sector has preserved a traditional regulatory regime. This stance has been justified by the view that to assure universal service, even to remote parts of the country, there must be a postal monopoly, as competitors might not service unprofitable areas. This position is one of the approaches that is open to governments, but it is not the only one.

Today this view is being challenged. In some developing countries the postal monopoly still leaves some rural residents without service, and experiences have shown that services in formerly protected markets can improve when providers compete. Meanwhile, there are regulatory innovations in other areas of infrastructure from which lessons can be extracted.

This chapter has highlighted the importance of using cost disaggregation in order to understand the economics of the sector. The chapter also offers the decision maker the possibility of other options for providing postal sector service. It also examines the importance of an impartial and informed regulatory framework for the operations of the postal sector.

This regulatory framework should ensure the postal service's ability to compete efficiently in the market. It should cover, among other areas: service provision, the scope of monopoly and exclusive privileges, fair competition, the financial control regime, tariff regulation, licensing, and consumer representation. The chapter also discusses the nature of the regulatory regime and points to the effectiveness of output-based or result-based regulation that fosters the development of the sector as a whole, rather than regulation that interferes in the sector's operations.

There is much to be learned in the area of postal regulatory reform from countries such as Sweden and Argentina that have taken steps in this area, and also from regulatory policy innovations in other infrastructure subsectors.

Conclusion
Monopoly Scope

*Papua New Guinea:* The legal framework within which the Post exists is relatively underdeveloped. The 1982 PTC Act does not explicitly address the issues of who the regulator is, what is regulated, or what the scope of the monopoly is. Although legislation provides a monopoly privilege to Post and Telikom Corporation (PTC) Post for the carriage of letters up to 500 g, this is not enforced. There is also open and active competition in international mail markets and in parcel and courier services. The existence of a below cost domestic letter rate and its interaction with the terminal dues has led to a large "remailing" practice from Australia and New Zealand, by a large private courier company, through PTC Post. TNT, DHL, and Federal Express are strong competitors within the postal market. For further commercialization of the postal service the government will have to develop a coherent legal and regulatory framework.

*Finland:* Finland officially deregulated its postal services in 1991—and was the first country in the world to do so. The Postal Services Act came into force at the beginning of 1994, and Finland Post’s new terms and conditions of delivery are based on this Act. As a license holder, Finland Post Ltd. is responsible for providing basic postal services throughout Finland. The Act also requires Finland Post to ensure that basic postal services are equally available at a standard price throughout the country. As of 1994, there were no other license holders. The Telecommunications Administration Center, which is the regulatory authority for the Post as well, has issued further guidelines to define the terms of the Act.

Tariff Regulation

*New Zealand:* The Deed of Understanding between New Zealand Post and the government specified that only the basic first-class letter rate was to be regulated through a price-cap mechanism. The Board of New Zealand Post has the authority to set postage rates without government involvement except for price surveillance by the Commerce Commission. The Post has complete discretion to set prices in products for which it does not have any protection. The provisions of the Commerce Act apply to New Zealand Post and can be invoked if prices are deemed to be anti-competitive.

*The Netherlands:* A tariff control system agreed upon with the government determines the company’s scope to amend postal rates. Under this system, average price changes may not exceed the movements in wage costs in the private sector. The Post amends postage rates for business customers each year within the scope allowed by
the statutory tariff control system. The rates for private users remain unchanged for as long as possible.

Singapore: The rate changes for the monopoly products of the Post (letters and postcards) are controlled by TAS, the regulatory authority. Pricing for the competitive products is within the discretion of the Post, however. Pricing for the monopoly products began to be formally regulated as of 1995 in order to ensure affordability and international rate competitiveness. The tariff mechanism aims to keep letter rates below the average tariffs of Hong Kong, Taiwan, and South Korea (before this, prices were benchmarked to the tariffs of 10 countries). In addition, the rate examination process includes examination of the cost components of letter mail in order to monitor input cost increases as well as efficiency increases achieved by the Post.

An interesting aspect of regulation in Singapore is that the regulator is primarily concerned with ensuring the provision of a good postal service at affordable rates throughout Singapore. Thus, prices of the monopoly service are capped to ensure affordability, but, unlike the situation in other postal administrations, the regulator is not concerned with the financial returns of the Post. Therefore, the Post has maximum incentives to achieve cost efficiencies. Permitting the Post to earn and retain robust financial returns may also be an implicit policy of the regulator in the interests of the postal sector as a whole, since Singapore Post is committed to reinvesting its retained earnings in the development and improvement of its service.

The Czech Republic: Until April 1995, the Post's prices on mail services were specifically and individually subject to Ministry of Finance approval. With the development of a cost model (on a consultancy basis from another postal administration) that allocates direct and indirect costs to each product, the Ministry has adopted a more liberal approach to postal price regulation. This approach permits the Post to set its own prices as long as it follows the principles embodied in the model. This involves assuring that no cross-subsidization takes place between monopoly and non-monopoly products, that price increases are reasonable in relation to inflation, and that network costs are shared by all activities. In addition, the Ministry has reserved for itself final approval of four mail categories thought to be politically sensitive: letters weighing up to 20 g, parcels weighing up to 10 kg, cash-to-cash money orders, and newspapers.

The pricing approach utilized in the Czech Post is designed to emphasize cost factors and to generally base prices on average costs.

\[1\] This is different from most countries where not only are pieces explicitly regulated but the Post has a mandate to break even or achieve a "normal" rate-of-return, implying an implicit rate of return regulation as well. For example, in the United Kingdom the British Post Office is subject to an explicit price cap and, through the EFL, an implicit rate-of-return scheme as well.
Demand and elasticity have not been factored into pricing as yet, nor have all services been priced to cover their costs. The sensitive categories that are priced by ministerial discretion are still priced below the model costs. These products were heavily subsidized under the planned economy and their prices are being phased upward to recover full costs.

**Regulatory Framework**

*Sweden:* The Postal Services Act laid the basis for a supervisory authority responsible for monitoring the application of the Act and intervening in the case of anomalies. This regulatory body, which is now functioning, is the National Swedish Post and Telecom Agency, a section of the Ministry of Transport and Communications. *Thus, the functions of ownership, operation, and regulation have been completely separated.* Operators that intend to service the postal market are obliged to register with the Agency but do not require any form of licensing or formal authorization. The Agency is charged with promoting competitive neutrality in the postal services market and has also undertaken certain tasks of a public nature from both the Post (such as the opening of undeliverable letters) and the government (to be the signatory of international intergovernmental treaties in the postal field).

*Argentina:* The Comisión Nacional de Correos y Telégrafos (CNCT), the postal and telegraphic regulatory agency in Argentina, was created in 1992 within a closed postal market, but with the deregulation of postal activity its role takes on a far more active dimension. Its self-stated functions are: the defense of the consumer; commercial loyalty; and the defense of competition. At present the regulatory regime is being crystallized. Recently, the Argentine Senate approved legislation imposing heavy regulation on the postal services market—only 18 months after the 1993 Decree that drastically cut back on red tape.

*The United Kingdom:* In the United Kingdom, where the current regulatory authority is the Postal Section of the Department of Trade and Industry, proposals are being considered for the establishment of an independent body, the Office of Postal Services (analogous to OfTEL and OfWAT), which would oversee the quality of universal service and would also advise the government on the scope of the postal monopoly. A quasi-governmental body, the Post Office Users National Council, also plays a supervisory role in terms of representing the public interest.
Until very recently, the structure of the postal sector varied little among countries. Although change is gradually taking place, even today in most countries the postal service is provided by a state-owned Post, Telephone, and Telegraph (PTT) Administration within a government department. The traditional justifications for this have been the following characteristics of the sector: its vital role in communications, the obligation to provide a universal service, and, consequently, the high infrastructure costs. There has been a general belief that, because of these characteristics, postal services are best provided under a government monopoly within the PTT structure.

Historically, the importance of the postal service to communication and development has been understated, if not ignored, which partly explains why the postal sector has been unaffected by the renaissance that is transforming all other areas of infrastructure. However, countries have been forced increasingly to look at the postal sector because (1) the legacy of negligence has led to a crisis in the sector, and (2) dramatic changes in the approach to other sectors, especially telecommunications, have forced the issue.

Today, the postal service stands at a crucial crossroads: if the status quo continues, the service's contribution to development will rapidly diminish. On the other hand, the adoption of a proactive stance toward reform could transform the postal service into a valuable national asset. With this in mind, this chapter and Chapter 4 explore options for reforming the postal sector and examine the ways in which a few countries have taken the initiative of reform. In these two chap-
enterprise reform is discussed in detail in terms of achieving such reform through commercialization (Chapter 4) and corporatization (this chapter).

The term enterprise reform refers to a group of performance improvement programs that could revitalize the postal service's efficiency and service quality. These programs focus on functions, resource deployment, and processes within the postal service organization. The design, implementation, and management of such programs is referred to as commercialization. To be successful, commercialization requires commercial freedom, flexibility in decision making, and independence in issues relating to resource deployment. Typically, such changes, as they would apply to the postal service, could be brought about through corporatization, which would involve a legal transformation of the postal service into a corporate entity. Thus, enterprise reform refers not only to commercialization but also to the facilitating processes required to implement the commercialization programs, including corporatization.

This chapter concentrates on the structural determinants and legislative processes that make it possible to provide a good postal service. The mechanics of the enterprise-focused programs that are required to improve the service will be dealt with in the next chapter under the banner of “commercialization.” It is important to keep in mind, however, that achieving effective results through structural transformation goes beyond legislative changes to a change in the basic organization outlook and business ethos (see Chapter 4).

The present study evidenced a broad range of corporatization experiences, some of which were effective and some of which were not. The following conclusions were drawn concerning success in structural and corporate transformation.

- Many countries that have gone through corporatization have ended the reform at that juncture and have hoped that the transformation itself would provide a sufficient basis for performance improvement. In some of these cases, however, the operating autonomy gained through the corporate transformation was effectively taken away, because the postal service continued to make substantial losses and therefore the government had to intervene in the running of the business. Thus, more than corporate transformation is needed.
- Separation of the postal service from the telecommunications business provides the needed structural clarity, and the incentives, for strategic performance improvement. The traditional integrated PTT structure has been a factor in constraining the development of the sector. Under a PTT structure, the postal service does not receive adequate political or managerial attention because it represents a minority proportion of the PTT’s business.
The embracing reform legislation should provide both the flexibility and the incentives for the reformed postal service. Even some high income countries that have undergone a comprehensive enterprise reform program have found themselves handicapped by restrictions on commercial behavior.

- The monopoly aspects of the postal act should be specified only for a fixed period of time (preferably a short period) and should be subject to policy review at the end of that period with a view to narrowing the scope of monopoly protection. The threat of the possible reduction of monopoly protection in itself provides an incentive for improving performance (see the Singapore case study).

The main objectives of postal reform (as discussed in previous chapters) are:

- To improve the quality of service
- To make the postal service financially self-supporting
- To run the postal service on commercial principles
- To continue to provide the social obligations.

Corporatization, as a means of achieving these objectives, is the process of giving postal administrations an independent legal status and subjecting them to the same legal requirements as private firms. Thus, the entity is subject to standard commercial and tax laws, accounting criteria, labor laws, etc. More important, the explicit separation of ownership and management responsibilities (e.g., through a board of directors or other body) renders the postal service less susceptible to government influence. This process enhances managerial autonomy by insulating the postal service from noncommercial pressures and constraints. It also clearly demarcates the role of government as owner of the enterprise, which is distinct from the operation of the enterprise. Managerial and organizational autonomy does not imply complete freedom, however. The government, as owner of the corporation, continues to set sectoral policies and goals while leaving detailed planning and implementation of the service to the administration. In addition, the enterprise is subject to regulatory oversight.

Corporatization, merely by providing the postal service with a distinct legal structure, converts the problem of official governance to that of corporate governance—the creation of an optimal system of accountability and incentives within the postal administration. Therefore, explicit contracts are needed between governments and the

---

1While the term "corporatization" is used rather widely, for our purposes the transition to a limited liability company (and all issues associated with it) is regarded as the process of corporatization.
management of the postal enterprise so that the postal service can operate on true market principles. Without such disciplines, management and resource allocation decisions will not correspond to realities.

At the outset, we would like to stress that legislative changes can only give the postal service the freedom to reform itself. From then on, the success of reform depends on the initiative taken within the postal service itself to operate on commercial, market-based principles. On occasion, varying degrees of commercialization have been introduced into postal services even before corporatization. However, whichever comes first, the implementation of both corporatization and commercialization is necessary for complete postal reform to take place.

This chapter captures the various structural, legal, ownership, and market options available to the post and the steps involved in the transition from one phase to another, with a view to maximizing the benefits of postal reform (see Figure 3.1). The decision on where to place the postal service along the spectrum of each of these four aspects will have a tremendous impact on the key parameters that need to be addressed for postal reform: accountability, autonomy, incentives, and competition.

**Figure 3.1**
Four Dimensions of Policy Options (with examples)
The traditional combined P&T (Post and Telecommunications) or PTT (which includes Telegraph as well) organizational form is still prevalent in many countries. Since both post and telecommunications belong to the larger communications sector, it has been customary to place the two within the same organization. It was felt that under this arrangement the sharing of common facilities and resources would maximize the economic and social benefits as well as the development of both sectors. As a result, unlike other areas in infrastructure which have been sheltered by the government, the postal sector has remained under the double mantle of both the government and telecommunications (see Annex 1 to this chapter for a listing of structural arrangements in selected countries).

There are three broad levels of structure for P&T:

- They belong to the same organization
- They are separate operational entities, but both are under the same supervisory authority and are governed by the same texts
- They are completely separate.

From the telecommunications sector’s perspective, the dynamism of the sector is constrained by its links to the postal service. Since the postal service sector is far more labor-intensive, and because its employees are usually under civil service statutes and are often heavily unionized, the capacity for organizational change and restructuring is reduced for the P&T as a whole. In addition, the telecommunications sector very often subsidizes the operations of the postal sector, thereby curtailing its own expansion.

In reality, this integrated organizational structure has severely handicapped the development of the postal sector as well. The postal service in developing countries typically constitutes 10 to 15 percent of a P&T in terms of revenue, and thus management, planning skills, and attention tend to be dedicated to the telecommunications sector. Therefore, the postal sector rarely receives the benefits of a clear-cut policy and development plan. Because of the integration of accounts in a P&T, especially as regards expenses, accountability and performance incentives are at a minimum in the postal sector. The postal sector not only has the government to subsidize it—it also has telecommunications to buffer its existence. This structure is not conducive to letting the postal sector come into its own.

From an operational perspective, it is not clear that telecommunications and the postal service enjoy their presumed level of synergies. First, the postal service is not only in the communications market, but in distribution as well. In fact, its pervasive retail network and delivery capacity are generally unparalleled by other organizations. In addition, the two sectors cannot be more dissimilar in terms of their capital-labor mix, and this has significant implications for the
Redirecting Mail: Postal Sector Reform

needs and targets of both sectors. The management and operational expertise required differs greatly for the sectors: both sectors target different product needs within their customer base, and both interact with entirely disparate entities on the supply side. At most, these sectors may have the potential to share retail space in providing their services and to utilize each other’s services as inputs. This is not a sufficiently valid rationale to justify the integration of the two sectors. It is preferable that they operate at arm’s length and with a well-defined system of market pricing for the utilization of each other’s facilities and services, thereby maintaining a commercial separation and maximizing accountability in both sectors.

Most countries that are contemplating reform in the postal sector, or that have implemented reform (the United Kingdom, Australia, New Zealand, Argentina, Canada, Chile, Tanzania, to name a few), are in the process of separating, or have separated, the postal service from telecommunications for the reasons specified above. In the case of Sweden the two services were never integrated.

An example is provided by New Zealand Post, where the government was encouraged to separate the postal service from the other businesses because of the post’s deteriorating performance.

Prior to 1987, the New Zealand Post Office, which was a department of the state, had been responsible for the provision of telecommunications services, postal service, and retail banking. Telecommunications constituted 60 percent of revenues, while postal services accounted for only 25 percent. Retail banking represented only 15 percent of revenues. Under this arrangement, the postal sector suffered from the following constraints:

- Decision making was centralized
- Telecommunications issues dominated
- Capital was scarce and, when available, was channeled into telecommunications
- Political and social issues took priority over commercial issues
- Marketing initiatives and customer support were weak
- The organization was slow to respond to market pressures.

Within this environment, the postal business was incurring trading losses and also suffered from a paucity of strategic capital investment. Very little finance was devoted to upgrading mail processing facilities and equipment. For all of the above reasons, service standards slipped and New Zealand Post’s market share decreased. In

---

2 Increasingly, the postal sector is providing a combination of electronic and hybrid services which draw heavily on communications technology (electronic mail, facsimile, etc.). While this may be regarded as a source of synergy for the two sectors, it may well be a source of friction (see Chapter 5).
view of this situation, the government separated the post from telecommunications and banking and corporatized all three. New Zealand Post is now a limited liability company, headed by a board of directors and owned by two ministries.

In a few countries postal services and telecommunications have been retained within the same organization, although attempts have been made to maximize operational and even financial separation. The reasons for retaining or adopting an integrated structure are:

- To maintain a continuity within change
- To be able to offer a broad range of communications services within one organization
- To harmonize the relative roles and activities of the two sectors (e.g., in the provision of electronic and hybrid communications services).

Further examples of the structure of post and telecommunications are given in Annex 2 to this chapter.

The primary functions of postal legislation are: (1) to provide a nationwide postal service that fulfills the social and economic objectives of the government; and (2) to regulate and facilitate the development of the postal sector in the interest of the nation as a whole.

While legislation is important to achieve these functions, it should be borne in mind that the advantages of corporatization are to grant the postal service the independence and flexibility to meet commercial challenges and develop the sector in a rapidly transforming and increasingly competitive market. Care should be taken to see that, while the postal service should meet its obligations, excessive legislation and regulation should not handicap the service to the point of negating all the benefits of corporatization. The operation of market forces should be allowed to dictate, to the maximum extent possible, the desired output of services and ensure that this output is achieved at the least possible cost.

A multitude of reform issues should be considered during the framing of postal legislation (whether primary, transitional, or subordinate) for the transformation of a postal service from one legal status to another. These issues vary with the legal customs and principles of each country (see Figure 3.2). The establishment of a postal service under any of the legal options, or change of legal status, requires different forms of legislation. The departmental model is created by an act which establishes the department and authorizes its operations. The establishment of a statutory corporation generally requires two acts.
1. **Core Postal Law:** At minimum, this enabling act establishes the legal status of the postal service and specifies the structure, powers, functions, reserved services, obligations, and privileges of the postal operator (and regulator if the regulatory function is put into a separate organization). This act will be the legal constitution of the postal operator as a corporate body and should contain everything necessary to enable the postal service to have an independent legal existence, to own its assets, and, to some extent, to manage its revenues and expenditures. In addition to the core law, subordinate legislation and adherence to international treaties and conventions may have to be factored in separately.
2. Transitional or Vesting Legislation: This legislation vests the assets and liabilities of the former entity in its successor, and also specifies the initial capitalization and the rights and obligations of employees affected by the restructuring. Since this legislation is pertinent only to the restructuring phase, it is preferable not to include it with the core act.

In the case of a limited liability company, which operates under private law, the legal constitution of the postal enterprise will be the Memorandum of Association. Therefore, the transition of a postal service to a limited liability company generally requires a brief specifying those aspects in which the postal service may differ from a company, or any special provisions that prevail over company law. Postal law also needs to nominate the company to be licensed for postal purposes. A separate act establishes and authorizes the regulator. Legislation may also specify measures to ensure the continuity of the organization (perpetual succession) irrespective of the continued existence of a government, minister, board, or chief executive.

In some countries the change of status of a postal administration is conducted by an instrument lower than a law, such as an ordinance, a decree, or a simple decision.

Examples of legal transformation can be found in Annex 2 to this chapter.

Postal services may be broadly classified into the following legal structures, in increasing order of enterprise autonomy:

1. A government department under the jurisdiction of a ministry or state secretariat, or an independent ministry

2. A statutory corporation (also referred to elsewhere as a public corporation or public enterprise), which is generally wholly government owned, and is controlled by the parliament, government, or a special committee

3. A limited liability company under companies' law, which may be:
   a. A wholly or partially government-owned company
   b. A privatized company, in which the controlling interest or full ownership lies with the private sector.

These three legal structures are described below.

*Government Department*: This is the most prevalent and traditional legal form for many postal services in developing countries. All functional responsibility for the postal service is assigned to a government department, which does not possess a separate financial or legal status. Because of the lack of financial separation from the rest
of the ministry and the ambiguity of accounting principles, the enterprise is often either highly subsidized when it makes losses, or utilized as a cash cow if it generates profits. As a result, the enterprise is starved for investment and maintenance funds and, consequently, the quality of service deteriorates. Lack of financial separation is also detrimental to the postal service because of low managerial accountability and incentives. Management is aware that it will be buffered by a soft budget constraint and therefore has no motivation to achieve increased productivity or cost efficiencies. Given the multitude of institutional options that have been tried for the provision of infrastructure, there is little justification for assigning all functional responsibilities for the postal sector to a government department. The government's role is more appropriate for providing overall policy guidance and sectoral planning.

Statutory Corporation: This is a limited reform step whereby a statutory company is established by an act of parliament. This institutional form allows the company to acquire a financially separate status and is therefore useful in making management accountable for the utilization of resources in response to competitive pressures. The postal administration is given autonomy in operation and maintenance, and is expected to operate the enterprise like a business.

The postal administration is generally supervised by the parliament, government, or an independent committee. Explicit cost-accounting is introduced which helps identify the revenue and expenditure streams and the viability of individual products. Postal administrations are generally obliged to balance revenue and expenditure and are occasionally required to make a specified financial return. Nonetheless, because ultimate responsibility for the provision of the service and all liabilities of the enterprise rest with the government, the establishment of a statutory company achieves limited results in reforming the postal service sector—although it could be a useful step in the continuing reform process.

Limited Liability Company: The establishment of a limited liability company involves the dissolution of a government department or statutory body and the transfer of its assets to a new corporate entity which operates under company law. The enterprise may still be fully or partially government owned, or it may be fully owned by the private sector. The government exercises limited supervisory authority over a limited liability company and also imposes certain obligations on such a company.

Under this legal form, postal administrations are obliged not only to balance revenue and expenditure, but also to make profits for the Treasury. The enterprise is responsible for meeting its service obligations and also for shouldering all of its liabilities and commercial
risks. In return, the enterprise is given a high level of managerial autonomy and flexibility. The monopoly privileges of the postal administration are usually transferred to a licensing system which is subject to periodic review. The introduction of rigorous financial accounting identifies activities which are non-remunerative. If these activities remain justified as essential public services, they should be financed by explicit government subsidies or justified on other economic grounds. This institutional form has the advantage of introducing the maximum market pressures and also increases the scope for market-based financing.

The choice of legal status should depend on the needs of the sector and the urgency of reform, as well as on the balance which the government may want to attain between management's autonomy to act in a fully commercial manner and the constraints necessary to ensure a satisfactory level of personal and public accountability.

While some postal administrations have evolved through these options by following a phased process, others have moved directly from a government department to a limited liability company. There are several variations of these three broad legal options as well. For example, in the United Kingdom the Royal Mail is a statutory corporation but two of its subsidiaries are limited liability companies. In several countries, although a postal service is a government department, it may have relatively greater autonomy in terms of the budget, the maintenance of separate accounts, etc. Therefore, the spectrum of legal options available to the postal service should be regarded as a continuum rather than as the three discrete states presented here. For a comparison of the different legal forms of postal administrations, see Table 3.1.

To date, no postal administration has been fully privatized, although this was under consideration in the United Kingdom and is in preparation in Argentina. However, the partial sale of shares of the postal service has been provided for in the Postal Act of the Philippines and has also been undertaken in the Netherlands and Germany.

Further examples of legal classifications of the postal service can be found in Annex 2 to this chapter.
### Table 3.1
Comparison of Legal Options

<table>
<thead>
<tr>
<th>Function</th>
<th>Government Department</th>
<th>Statutory Corporation</th>
<th>Limited Liability Company</th>
<th>Privatized Corporation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ownership</td>
<td>State</td>
<td>State</td>
<td>State/mixed</td>
<td>Private sector</td>
</tr>
<tr>
<td>Sectoral Planning &amp; Policy</td>
<td>State</td>
<td>State</td>
<td>State</td>
<td>State</td>
</tr>
<tr>
<td>Investment</td>
<td>State</td>
<td>State</td>
<td>State approval for large amounts</td>
<td>State (internal agency)</td>
</tr>
<tr>
<td>Regulation</td>
<td>State (internal to postal service)</td>
<td>State (internal or external agency)</td>
<td>State (internal agency)</td>
<td>State (internal agency)</td>
</tr>
<tr>
<td>Tariffs</td>
<td>State</td>
<td>State</td>
<td>Enterprise (within bounds)</td>
<td>Enterprise (within bounds)</td>
</tr>
<tr>
<td>Operation &amp; Maintenance</td>
<td>State</td>
<td>Enterprise</td>
<td>Enterprise</td>
<td>Enterprise</td>
</tr>
</tbody>
</table>

### Ownership Features

<table>
<thead>
<tr>
<th>Feature</th>
<th>Government Department</th>
<th>Statutory Corporation</th>
<th>Limited Liability Company</th>
<th>Privatized Corporation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legally Responsible for</td>
<td>Parliament</td>
<td>Parliament</td>
<td>Shareholding ministers/private shareholders</td>
<td>Private shareholders</td>
</tr>
<tr>
<td>Separate Legal Status</td>
<td>No</td>
<td>Yes</td>
<td>State/private</td>
<td>Yes</td>
</tr>
<tr>
<td>Shareholders</td>
<td>n/a</td>
<td>State</td>
<td>State/private</td>
<td>Private</td>
</tr>
<tr>
<td>Dividends</td>
<td>None</td>
<td>Not usual</td>
<td>To shareholder[s]</td>
<td>To shareholder[s]</td>
</tr>
<tr>
<td>Liability</td>
<td>Unlimited</td>
<td>Limited</td>
<td>Implicit</td>
<td>None</td>
</tr>
<tr>
<td>Government Guarantee</td>
<td>Essential</td>
<td>Explicit</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Tax Payment</td>
<td>None</td>
<td>Not usual</td>
<td>To shareholders</td>
<td>To shareholders</td>
</tr>
<tr>
<td>Pension Liability</td>
<td>State</td>
<td>State</td>
<td>Enterprise</td>
<td>Enterprise</td>
</tr>
</tbody>
</table>

### Discretionary Behavior

<table>
<thead>
<tr>
<th>Feature</th>
<th>Government Department</th>
<th>Statutory Corporation</th>
<th>Limited Liability Company</th>
<th>Privatized Corporation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Board Autonomy</td>
<td>None</td>
<td>Moderate</td>
<td>Considerable</td>
<td>Considerable</td>
</tr>
<tr>
<td>Managerial Autonomy</td>
<td>None</td>
<td>Moderate</td>
<td>Considerable</td>
<td>Considerable</td>
</tr>
<tr>
<td>Alliances/Diversification</td>
<td>Not permitted</td>
<td>Limited</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Dividends/Sell By</td>
<td>None</td>
<td>Not usual</td>
<td>Board/Minister</td>
<td>Board</td>
</tr>
<tr>
<td>Management/Accountability</td>
<td>Low</td>
<td>Medium</td>
<td>High</td>
<td>High</td>
</tr>
<tr>
<td>Financial Authority</td>
<td>None</td>
<td>Separate budget</td>
<td>Financially autonomous</td>
<td>Independent</td>
</tr>
</tbody>
</table>

### Operations

<table>
<thead>
<tr>
<th>Feature</th>
<th>Government Department</th>
<th>Statutory Corporation</th>
<th>Limited Liability Company</th>
<th>Privatized Corporation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Statutory Monopoly</td>
<td>Heavy, can usually delegate</td>
<td>Heavy</td>
<td>Relaxed or removed</td>
<td>Removed</td>
</tr>
<tr>
<td>Source of Financing</td>
<td>Consolidated funds</td>
<td>Specific fund allocation</td>
<td>Private capital markets</td>
<td>Private capital markets</td>
</tr>
<tr>
<td>Organizational Flexibility</td>
<td>None</td>
<td>Minor</td>
<td>Some</td>
<td>Complete</td>
</tr>
<tr>
<td>Accounting Principles</td>
<td>Absent</td>
<td>Commercial</td>
<td>Commercial</td>
<td>Commercial</td>
</tr>
<tr>
<td>Commercial Risk</td>
<td>State</td>
<td>State</td>
<td>Enterprise</td>
<td>Enterprise</td>
</tr>
<tr>
<td>Service Responsibility</td>
<td>State</td>
<td>State</td>
<td>Enterprise</td>
<td>Enterprise</td>
</tr>
</tbody>
</table>

### Control Mechanisms

<table>
<thead>
<tr>
<th>Feature</th>
<th>Government Department</th>
<th>Statutory Corporation</th>
<th>Limited Liability Company</th>
<th>Privatized Corporation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Management</td>
<td>Civil/public service statute</td>
<td>Civil/public service statute</td>
<td>Board</td>
<td>Board</td>
</tr>
<tr>
<td>Employees</td>
<td>Civil/public service statute</td>
<td>Civil/public service statute</td>
<td>Board</td>
<td>Board</td>
</tr>
<tr>
<td>Internal Monitoring</td>
<td>n/a</td>
<td>Minister/Treasury</td>
<td>Minister/Treasury</td>
<td>Private shareholders</td>
</tr>
<tr>
<td>Senior Director</td>
<td>Minister</td>
<td>Board</td>
<td>Board</td>
<td>Board</td>
</tr>
<tr>
<td>Senior Management</td>
<td>Secretary</td>
<td>General manager</td>
<td>Chief executive officer</td>
<td>Chief executive officer</td>
</tr>
</tbody>
</table>

### External Monitoring

<table>
<thead>
<tr>
<th>Feature</th>
<th>Government Department</th>
<th>Statutory Corporation</th>
<th>Limited Liability Company</th>
<th>Privatized Corporation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Spending Plans</td>
<td>Parliament</td>
<td>Parliament/minister</td>
<td>Minister/capital market</td>
<td>Capital market</td>
</tr>
<tr>
<td>Financial Accounts</td>
<td>Audit office</td>
<td>Audit office</td>
<td>Private auditor</td>
<td>Private auditor</td>
</tr>
<tr>
<td>Overall Performance</td>
<td>Treasury/select committees</td>
<td>Treasury/select committees</td>
<td>Minister/capital market</td>
<td>Capital and stock markets</td>
</tr>
</tbody>
</table>
The postal service is still a predominantly government-owned sector. However, the wave of privatization in the telecommunications sector is one of the forces that is leading countries to consider private ownership of the postal service as well. A few countries have implemented partial privatization schemes with the primary aims of:

1. Maximizing commercial pressures and disciplines with the infusion of private capital
2. Raising capital for expansion and improvement to increase competitiveness
3. Giving the postal service an opportunity to compete on equal terms with its competitors.

Nevertheless, private ownership of the postal service, whether by a strategic investor, by dispersed ownership through the stock exchange, or by the employees, is relatively uncharted territory. The examples provided below illustrate the privatization process in the few countries that have implemented it or are in the process of so doing. In addition to these examples, France and New Zealand have also contemplated the privatization of their postal services.

This organizational option represents the extreme option for the postal service in terms of maximum accountability, autonomy, and incentives (see Table 3.1). A detailed treatment of the potential mechanisms available to introduce private sector participation into the postal service has been given in Chapter 1.

In the Netherlands, shares in KPN, the Dutch state post and telecommunications company, were floated on the Amsterdam Stock Exchange in June 1994. The government sold 138 million shares in KPN, representing a 30 percent stake, to raise f. 6.9 billion. The sale of a second tranche in October 1995 raised more than f. 6.0 billion. A third tranche of KPN shares is expected to be sold by the end of 1997. About 188,500 private shareholders participated in the offer, 31,000 of which were KPN employees. Almost 60 percent of the shares on offer were taken up by foreign institutions, and the issue was oversubscribed almost threefold. The announcement of net profits of f. 2.04 billion (US$1.32 billion) in the 1994 fiscal year (an increase from f. 1.78 billion in 1993) has caused renewed demand for and international interest in the next offering of shares.

KPN expects to spend a substantial amount in the coming years on upgrading infrastructure. During 1994-98, PTT Post alone expects to spend f. 1 billion on land, buildings, and machines as part of the "Briefpost 2000" project—a special project for improving efficiency through infrastructure modernization and consolidation. Therefore, in the case of KPN, one of the primary aims of privatization is to raise capital. An infusion of private capital will provide increased freedom to expand national and international operations, and, at the same time, will exert continual commercial and market-based pressures.
The government intends to reduce its share to less than 33.3 percent before the year 2004. KPN's postal arm, PTT Post, might then become the world's first privatized postal service. The privatization of the postal service is not just a by-product of the selling off of state telecommunications companies. It reflects the fact that postal services must become more like private businesses—or must even be private businesses—if they are not to lose out to new competitors in a rapidly changing market.

Argentina is one of the few countries that is preparing its postal service for private sector participation. In the 1970s Encotel, the government postal service, began to lose market share to private operators in the postal market, and from then on suffered rapid commercial deterioration. In 1991 the volume serviced by Encotel was half of the 1981 volume and from 1984 to 1991 Encotel experienced a negative annual rate of 6.5 percent. In 1993 the private sector had captured a market share of 48.8 percent, although its average charges were more than double Encotel's rates. It was clear that the public preferred to pay a premium for the superior services offered by the private sector. In recognition of the fact that this trend could lead to the “disappearance” of the postal service, the government decided to move boldly toward liberalization and deregulation of the postal sector, skipping some of the interim stages used by postal administrations elsewhere.

In May 1993 Encotel was incorporated into Encotesa Inc., and in June the government passed a decree deregulating the entire postal market. Thus, with these few steps, a restructuring process was set in motion for the postal service that aimed at making the best use of available resources. This exercise was also conducted to pave the way for the privatization of the postal service. The issue of preventing Encotesa from being converted into a private monopoly after its privatization is of prime concern and has led to intense public controversy which has prolonged the privatization process. Limitations on the participation of foreign capital (to 30 percent) have also raised objections, since several foreign postal administrations have shown an interest in the privatization of the Argentine postal service.

In the interim period, the government is trying to clarify the regulatory framework in order to make the oversight of the entire postal market more precise. The government is also building controls into the legislation to prevent the emergence of a private monopoly and also to promote competition in the postal market. Encotesa will continue to be responsible for maintaining universal service even after privatization. Currently the privatization law is awaiting passage by the National Congress (Parliament).
Functions describe the role of the postal service in the community. While the core function of any postal service is to carry postal items, clear definition of the term “postal item” removes ambiguity as to the type or form of item included. Item definitions are useful for service description purposes such as charging and handling and for monopoly clauses. In some countries, apart from carrying postal items, the postal service may have to be specifically authorized to be able to offer financial and agency services, electronic mail and hybrid services, consultancy services, sale of postal products at retail outlets, or expansion of agency services (providing licenses, registration, etc.). The postal authority may have to be given a specific function to service these areas; otherwise its operation may be challenged by private or other operators. Clarification of the geographical territory in which functions are to be exercised is also necessary, and this may differ for different functions. The specification of explicit functions in legislation is considered preferable because it expresses the objectives of the government in a way that facilitates interpretation of the Postal Act.

Legislation should give the postal service operator the power to do everything necessary for the performance of its functions and obligations. Failure to grant this level of autonomy dilutes the responsibility and accountability of the postal service and degrades the service by lengthening the decision process. Granting of powers is central to the entire purpose of corporatization which aims to create a structure that is capable of responding flexibly and efficiently to the postal needs of the national market. In the case of a corporatized postal service which is subject to company law, the enterprise has all the powers of a natural person. The Act would therefore specify (1) anything that grants the service extra powers, such as the exclusive right to perform reserved services, or (2) anything that would limit company laws.

A postal service is held to certain obligations to fulfill the social and economic objectives of the government. Service obligations usually require the provision of a universal basic postal service which is accessible to the population and is provided at reasonable prices. Legislation specifies the extent of the obligation, which takes into consideration alternative provision available to the population. At minimum, the obligation generally covers the reserved services. The manner of service provision addresses issues such as accessibility, affordability, and acceptable quality. Special service provisions for the blind, disabled, elderly, etc., are also specified. Commercial obligations may generally require that the postal service operate in a manner consistent with sound business practices or specify certain profitability or financial targets. Government obligations may require the postal service to follow the directions of the minister in matters relating to general government policy, in specific postal matters such as...
as the appropriation of surpluses or fixing of prices, or in relation to
the country's obligation under an international treaty.

If a postal service is expected to comply with obligations that re-
quire it to provide certain services at less than cost for political or
social reasons, an economic analysis should be undertaken to gauge
the cost of these obligations. The government has to decide whether
the postal service is capable of servicing these obligations without
any compensation because of its current position (as is the case with
regional obligations in Sweden: see Box 2.4 in Chapter 2) or whether
it should be explicitly subsidized for the provision of these services
(as is the case with all other obligations for Sweden, Canada, Argen-
tina, and the Netherlands). With the appropriate contract between
the government and the postal service, there is no reason why the
postal service cannot be competitive and financially viable, even if
the government requires the maintenance of a nationwide postal ser-
vice at affordable rates.

Some examples of functions, powers, and obligations of postal
services are given in Annex 2 to this chapter.

Financial
Performance

A limited liability corporation obtains its legal status from company
law. Therefore, its financial structure and processes will be within the
limits authorized by that law and as set out in detail in the Memoran-
dum of Association. Specific legislation will deal only with matters of
ownership, with reporting to the owner, and with financial responsi-
bilities which legislation will have to specify as overriding company
law. Under normal circumstances, since the objective is to level the
playing field with its competitors, a corporatized postal service will be
expected not only to be financially self-sufficient, but also to provide
its owners with a reasonable financial return. If the corporatized postal
service is expected to provide services outside the realm of its com-
mercial activities, such as servicing universal obligations, any subsi-
dies or compensation for this should be based on explicit
cost-accounting and should be made transparent.

Purpose of Legislation

In the case of a statutory corporation, legislation should provide clear
financial objectives. The range of options is as follows:

- To cover expenditures with revenues
- To recover costs, and fund all or a part of capital outlays
- To cover costs, fund capital outlays, and pay a specified
  rate of return to the owners.

The choice depends on the state of development of the postal ser-
vice and its capacity to meet such objectives. Legislative provisions
concerning the payment of dividends and interest may also have to
be specified. These might include the authority empowered to declare the final and interim dividends (e.g., the Board); the authority empowered to approve the declaration (e.g., the Minister); and the time limit for payment of dividends.

Government departments are generally not taxable whereas limited liability companies generally are taxable. Statutory corporations lie in the middle, where the taxation status is defined by a choice made in the legislation. Legislative provisions should specify whether the postal service is subject to taxation. If it is taxable, the nature of the taxes should be specified, and if it is exempt, the extent and duration of exemption should be specified. Provisions concerning auditing should be specified, such as: (1) the authority that will carry out the audit; (2) the qualifications for appointment as an auditor; (3) the power to remunerate the auditor; (4) the nature and types of audits; and (5) the timetable for the audit. The auditor will also require access to all documentation, stores and property, and information necessary for the audit.

Legislation must also specify the ownership provisions and the power of the relevant minister to sell or authorize the sale of shares, as well as the circumstances for the exercise of this power. A corporation will need the power to borrow and to give security over the assets for this purpose. In some cases, approval from the relevant minister is required for raising debt above a certain amount; therefore provisions concerning external debt may also have to be included in the legislation. While the debt, and for that matter all liability, of statutory corporations is backed by a government guarantee, which confers statutory authorities with an additional advantage over competitors in terms of raising capital, this is not the case for limited liability companies (see Box 3.1 for the case in Sweden).

In the case of the United Kingdom, for example, the Post Office is given three financial targets by the government: ROCE for profitability, RUC for efficiency, and EFL for cash generation. The targets for 1992-93 are shown in Table 3.2.

While ROCE and RUC are the result of consultation between the Post and the government and are regarded as appropriate by the Post, EFL is seen as a constraint on the improvement and competitiveness of the Post. Any profit that the group makes above its capital requirement for the year, or above the target EFL, is paid to the Treasury and invested in the public sector. This often exceeds the EFL target, and the Group does not have the flexibility to retain its profits or channel them into capital investment. In 1993 the EFL requirements escalated dramatically; these increases are partly dictated by the condition of the Public Sector Borrowing Requirement (PSBR). As of 1993, the Post Office’s borrowing limit under section 74(2) of the British Telecommunications Act of 1981 was £1,200 million. Capital investment was capped by the government to £325 million in 1994.
While the Post Office pays a corporation tax, like its private competitors postal services are exempt from VAT.

The Post Office is also given service level targets for first class letter delivery (a 92 percent next day delivery target for 1993-94) which are monitored by the Post Office Users National Council (POUNC), the body that mediates between the Post Office and its customers. Both inland and international quality of service are measured independently by external agencies. Service at Post Office Counters is assessed by reference to average queuing times. External measurement was introduced for letter services in 1988, and from then on the drive to enhance quality has produced significant improvement each year.

Table 3.2
United Kingdom Post Office Financial Goals, 1992-93

<table>
<thead>
<tr>
<th>Royal Mail</th>
<th>Parcelforce</th>
<th>Counters</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Return on capital employed (ROCE)</td>
<td>Target</td>
<td>Actual</td>
<td>Target</td>
</tr>
<tr>
<td>15.0%</td>
<td>16.3%</td>
<td>0.0%</td>
<td>-5.7%</td>
</tr>
<tr>
<td>Real unit cost reduction (RUC)</td>
<td>Target</td>
<td>Actual</td>
<td>Target</td>
</tr>
<tr>
<td>0.5%</td>
<td>0.8%</td>
<td>none</td>
<td>0.5%</td>
</tr>
<tr>
<td>External financing limit (EFL) in £m</td>
<td>Target</td>
<td>Actual</td>
<td>Target</td>
</tr>
<tr>
<td>none</td>
<td>none</td>
<td>none</td>
<td>none</td>
</tr>
</tbody>
</table>

1 Reduction in RUC is based on previous year.

Box 3.1 Corporatizing Sweden Post: Financial Issues in the Transition

The incorporation of Sweden Post was accompanied by the formulation of specific contracts between Sweden Post and the state specifying the duties and obligations of each party. The first agreement was for less than three years, up to the end of 1996. The financial requirement imposed on Sweden Post by the government in its capacity as the owner is that the business must operate commercially and generate a return on equity comparable with that of major, well-managed Swedish companies in similar industries. The government has set the long-term return on capital requirement at 11-13 percent, after tax at a standard rate. Sweden Post has consistently exceeded this target for the six years preceding corporatization. Profit margins (after financial items) have also been consistently over 5 percent. As owner of Sweden Post, the government has also specified that the equity/assets ratio at the Group level shall be approximately 15 percent. Corporatization sharply increased Sweden Post’s debt/equity ratio because it undertook full liability for both historical and current pension commitments. Because of this large increase in pension liabilities, the government has agreed that it will not receive dividends until the equity/assets ratio is deemed satisfactory.

From 1994 to 1996, prices are to be capped at 80 percent of the road transport price index. Sweden Post is expected to achieve productivity improvements of at least 2 percent per year, and is expected to maintain 95 percent delivery of overnight mail as far as quality of service is concerned. It is also expected to maintain a nationwide counter service of at least 2,000 outlets. Sweden Post is not permitted to own securities and investment companies.
Transitional Legislative Provisions

To ensure that financial performance is monitored and controlled, transitional legislative provisions encompass financial issues in restructuring. These must provide for the effective transfer or vesting of assets and liabilities in the new postal organization. Provisions must be broad enough to include tangible and intangible assets and liabilities, work in progress, contingent liabilities, and similar items such as pension rights and obligations. Transitional financial legislation will include the specification of the method of valuation (book or market value) for the transfer of assets and liabilities to the name of the new postal entity. If the balance sheets or accounts relating to assets were not being prepared in the predecessor organization, which is likely in government departments, a market valuation may have to be undertaken—although it is a time-consuming and expensive process. In addition to making possible the capitalization of an enterprise, a market valuation is also necessary if financial targets will be utilized to measure the performance of the postal service. If the sale of shares at some future date is a possibility, the asset backing per share is a critical issue for prospective investors and therefore an up-to-date market valuation of assets will again be necessary.

For example, the Philippine Postal Service Act 1992, Section 9 - Capitalization, states the following under (b): the values of all the existing assets of the Bureau of Posts and its successor office, the Postal Services Office, and the various postal facilities throughout the country owned by it, [are] to be determined by an independent appraiser within a year [of the] effectivity of this Act.

Transitional provisions also specify the manner in which the rights of property and assets are to be transferred to the new organization. For transition from a government department to a 100 percent government owned corporation, the value of net assets will be recorded as equal to a capital account representing the initial capital investment by the government. The treatment of liabilities incurred to the government by a predecessor organization has to be determined, especially if these are to be written off. As far as liabilities are concerned, the handling of pension schemes is a crucial area. If the operations are being converted from a department, employees will be covered by a government pension scheme which should continue to be responsible for these former employees. The possibilities for employees that transfer to the new entity are:

- To remain with the government pension scheme, or
- To transfer to a new postal service scheme.

It is preferable for the postal service to formulate a new pension scheme in line with industry standards. By being more expensive, government pension schemes may hamper the postal service in the
competitive arena to the long-term detriment of both the staff and the organization. If a new scheme is introduced, all new employees would automatically be enrolled in it.

The method of determination of initial capital has to be specified. The initial book value of investment in the entity will be the value of net assets transferred to it and new capital injected by owners at the time of transition. This initial investment will be in the form of debt (loans) or equity (shares). The accounting principles of the new entity will also have to be determined. Most government departments use cash (non-accrual) accounting systems, but a corporation has to switch to accrual accounting in accordance with generally accepted accounting practices. Detailed procedures will need to be prepared and staff retrained if necessary in the new accounting regime. The design of a new accounting system may require professional accounting services.

An example can be seen in Title 39, United States Code: U.S. Postal Service, Section 2002 - Capital of the Postal Service, which states the following:

(a) (1) Assets shall be valued on the basis of original cost less depreciation, to the extent that such value be determined. The value recorded on the former Post Office Department's books of account shall be prima facie evidence of asset value.

(a) (2) All liabilities attributable to operations of the former Post Office Department shall remain liabilities of the Government of the United States, except that upon commencement of operations of the Postal Service, the unexpended balances of appropriations made to, held or used by, or available to the former Post Office Department and all liabilities chargeable thereto shall become assets and liabilities, respectively, of the Postal Service.

Conclusion

This chapter has discussed the structural and legal reform of the postal sector in the context of the corporatization of the postal service. The focus has been on the legislative processes that are needed to ensure an efficient postal service.

Corporatization is seen to be an essential early step in postal reform. By giving the postal administration an independent legal status and a distinct legal structure, and by separating ownership and management, corporatization supplies the conditions for optimal accountability and incentives within the postal administration.

Country examples in this chapter and in Annex 2 point to various options for structural reform and illustrate their advantages and dis-
advantages. The discussion of the legal transformation of a postal administration is also enhanced by a number of country examples and by a classification of the choice of legal forms for a postal service.

This chapter makes the point that legalization should give the operator of the postal service the power to properly perform its functions and obligations. Failure to grant such power weakens the postal service's accountability and its ability to respond efficiently to the postal needs of the national market.
### Annex 1: Structure of the Postal Service: Some Examples

<table>
<thead>
<tr>
<th>Country</th>
<th>Year (As of)</th>
<th>Post &amp; Telecom</th>
<th>Legal Status of Post</th>
<th>Protected Service</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argentina</td>
<td>1994</td>
<td>Post &amp; telegraph integrated, telecom separate and privatized, post to be privatized</td>
<td>Limited Liability Corporation</td>
<td>No protection</td>
</tr>
<tr>
<td>Australia</td>
<td>1994</td>
<td>Separate</td>
<td>Limited Liability Corporation</td>
<td>Domestic letters up to 250 g and price threshold four times basic letter rate</td>
</tr>
<tr>
<td>Belgium</td>
<td>1991</td>
<td>Separate</td>
<td>Statutory Corporation</td>
<td>Letters, postcards, and printed paper up to 2 kg</td>
</tr>
<tr>
<td>Canada</td>
<td>1995</td>
<td>Separate</td>
<td>Limited Liability (Crown) Corporation</td>
<td>Letters and postcards up to 50g</td>
</tr>
<tr>
<td>Chile</td>
<td>1995</td>
<td>Separate, telecom privatized</td>
<td>Statutory Corporation (Correos)</td>
<td>Mail broadly defined as letters, newspapers, packets, and documents. Not enforced.</td>
</tr>
<tr>
<td>Côte d'Ivoire (Rep)</td>
<td>1987</td>
<td>Separate</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Denmark</td>
<td>1991</td>
<td>-</td>
<td>Government Department</td>
<td>Letters and card mail up to 1 kg</td>
</tr>
<tr>
<td>Finland</td>
<td>1994</td>
<td>Post &amp; telecom in same organization, but separate within it</td>
<td>Limited Liability Corporation</td>
<td>No protection</td>
</tr>
<tr>
<td>France</td>
<td>1991</td>
<td>-</td>
<td>Government Department</td>
<td>Letters, postcards, and packets up to 2 kg</td>
</tr>
<tr>
<td>Germany</td>
<td>1991</td>
<td>Separated in 1989, but telecom continues to subsidize post (as of 1993)</td>
<td>Government Department</td>
<td>Letters, postcards, printed matter, parcels with a personal message up to 1 kg</td>
</tr>
<tr>
<td>Greece</td>
<td>1991</td>
<td>Operate separately, but telecom subsidizes post</td>
<td>Statutory corporation</td>
<td>Letters, postcards, and printed paper up to 2 kg</td>
</tr>
<tr>
<td>Honduras (Rep)</td>
<td>1987</td>
<td>Separate, telecom privatized</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Indonesia</td>
<td>1987</td>
<td>Separate</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>
## Redirecting Mail: Postal Sector Reform

<table>
<thead>
<tr>
<th>Country</th>
<th>Year (As of)</th>
<th>Post &amp; Telecom</th>
<th>Legal Status of Post</th>
<th>Protected Service</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ireland</td>
<td>1991</td>
<td></td>
<td>Limited Liability Corporation (100% government ownership)</td>
<td>Letters, postcards, packages, printed papers, and express items up to 2 kg, plus parcels containing a personal message</td>
</tr>
<tr>
<td>Italy</td>
<td>1991</td>
<td>Integrated</td>
<td>Government Department</td>
<td>Letters and postcards up to 2 kg</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Transporting (not delivery &amp; collection) parcels interurban</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>1991</td>
<td></td>
<td>Government Department</td>
<td>Letters and postcards up to 2 kg</td>
</tr>
<tr>
<td>Malaysia</td>
<td>1994</td>
<td>Separate</td>
<td></td>
<td>Letters and postcards up to 2 kg</td>
</tr>
<tr>
<td>Myanmar</td>
<td>1995</td>
<td>Integrated, telecom subsidizing post</td>
<td>Government Department</td>
<td>–</td>
</tr>
<tr>
<td>Netherlands</td>
<td>1993</td>
<td>Integrated</td>
<td>Limited Liability Corporation (partially privatized)</td>
<td>Letters and postcards up to 500 g</td>
</tr>
<tr>
<td>New Zealand</td>
<td>1994</td>
<td>Separate, telecom privatized</td>
<td>Limited Liability Corporation</td>
<td>Price threshold of 80 cents</td>
</tr>
<tr>
<td>Nigeria</td>
<td>1987</td>
<td>Separate, telecom privatized</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Norway</td>
<td>1987</td>
<td>Separate</td>
<td></td>
<td>–</td>
</tr>
<tr>
<td>Papua New Guinea</td>
<td>1993</td>
<td>Integrated</td>
<td>Government Department</td>
<td>Letters up to 500 g</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Not enforced</td>
</tr>
<tr>
<td>Portugal</td>
<td>1991</td>
<td></td>
<td>Statutory Corporation</td>
<td>Letters, postcards, and express items up to 2 kg</td>
</tr>
<tr>
<td>Senegal</td>
<td>1987</td>
<td>Separate, telecom privatized</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Singapore</td>
<td>1995</td>
<td>Subsidiary of telecom</td>
<td>Limited Liability Corporation (partially privatized)</td>
<td>All letters and postcards until 2007</td>
</tr>
<tr>
<td>Spain</td>
<td>1991</td>
<td></td>
<td>Government Department</td>
<td>Letters and postcards up to 2 kg for inter-urban items</td>
</tr>
<tr>
<td>Sweden</td>
<td>1995</td>
<td>Separate</td>
<td>Limited Liability Corporation</td>
<td>No protection</td>
</tr>
<tr>
<td>Switzerland</td>
<td>1993</td>
<td>Integrated, telecom subsidizes post heavily</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Tanzania</td>
<td>1994</td>
<td>Separate</td>
<td>Limited Liability Corporation</td>
<td>Letters and postcards up to 2 kg</td>
</tr>
<tr>
<td>Ukraine</td>
<td>1993</td>
<td>Integrated (to be separated)</td>
<td>Government Department</td>
<td>–</td>
</tr>
<tr>
<td>UAE</td>
<td>1994</td>
<td>Separate</td>
<td></td>
<td>–</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>1995</td>
<td>Separate, telecom privatized</td>
<td>Statutory Corporation with two Limited Liability operating divisions</td>
<td>Letter of tariff up to £1</td>
</tr>
<tr>
<td>United States</td>
<td>1987</td>
<td>Separate, telecom privatized</td>
<td>–</td>
<td>–</td>
</tr>
</tbody>
</table>
Post and Telecommunications Structure

*Papua New Guinea:* The postal services were established in 1955 as the responsibility of the Department of Post and Telegraph. In 1980, the department was converted into a statutory company, the Post and Telikom Corporation (PTC), which is government owned. The post and telecommunications services share common functional services (finance, human resources, etc.). Many of their assets are shared and they provide services to each other without charge. The post comprises some 8 to 10 percent of the entire organization’s revenues; therefore, a greater proportion of management attention and resources is devoted to telecommunications. In 1993, Papua New Guinea was on the verge of privatizing telecommunications—a major step. However, the issue of where the post stood in the reform process had not been clarified. Although PTC was semi-corporatized, measures to wean PTC Post from resource sharing with PTC had not been implemented. As a result, the board of PTC and the government did not have an accurate picture of PTC Post’s financial condition or of its ability to be self-sufficient as a commercial entity. In addition, there was lack of clarity in the government’s policy regarding the Post. In retrospect, then, the entire corporatization process seemed to have been driven by the telecommunications side and the post was more or less carried along.

*Myanmar:* The postal, telephone, and telegraph services in Myanmar are provided by Myanmar Post and Telecommunications (MPT) under a state-granted monopoly. MPT is a government department within the Ministry of Communications, Posts and Telegraphs. MPT is organized functionally with integrated management for post and telecommunications at the national headquarters level. There are 14 territories; operating responsibility between the post and telecommunications is supposedly distinct at the territorial level. However, sharing of facilities and resources takes place at lower levels as well. There are no direct or indirect financial transfers to either the post or the telecommunications side for the use of each other’s services. Accounting statements are issued for MPT as a whole (post and telecommunications combined), and, as is typical in P&T departments, postal revenues are reported separately, but expenses are reported jointly with telecommunications. As a result, it is impossible to determine, on a current basis, the financial status of the post. However, estimates show that the post is suffering severe losses (its costs are 27 percent of MPT’s costs, while revenue contribution to MPT is only 8 percent) and that the degree to which telecommunications is subsidizing postal
services is increasing dramatically each year. The lack of postal ac-
to accounting has resulted in a system in which no visible management
tracking, reporting, or accountability exists. This integrated P&T or-
ganizational structure, combined with the purely functional nature of
MPT's organization, has proved a severe drawback to the develop-
ment of postal policy and strategic direction, since the post accounts
for only 8 percent of MPT's total revenue and, therefore, receives
scant attention. MPT has acknowledged some of these shortcomings and has targeted areas for reform in its January 1994 Postal
Development Plan.

**Finland:** The postal service and telecommunications have always been integrated in Finland. For many years they operated under a government department, for four years as a state business enterprise, and finally, from 1994, as a limited liability company. While both services are limited liability companies within the PT Finland Group and are operationally distinct, certain core functions are centralized at the group level. One reason for retaining the two services within this group structure was to ensure the continuity of P&T Finland's operations.¹

**Singapore:** The evolution of relations between the postal service and telecommunications in Singapore is unique. The postal service was a government department and was separate from telecommunications until 1982, when the post was merged with telecommunications, a statutory corporation. In 1992, when telecommunications was corporatized, Singapore Post became a wholly owned subsidiary of Singapore Telecommunications Private Limited (Singapore Telecom). In 1993, 11 percent of Singapore Telecom's shares were sold on the Singapore Stock Exchange, raising US$2.5 billion.

While Singapore Post enjoys a high level of operational autonomy, its budgeting and business planning processes are overseen and authorized by Singapore Telecom. In addition, its board of directors, chairman, president, and chief executive officer are staffed by persons holding the same positions in Singapore Telecom. Although the Post is a subsidiary of Telecom, the two maintain an arm's length relationship in their commercial dealings. All services rendered to each other are priced at market rates and each is required to compete with other private sector companies for the other's business.

The perceived advantages of merging the two sectors were as follows:

- Singapore Post would benefit from Singapore Telecom's corporate image, especially since the latter sector was distinct from the government.
- Post and Telecom would share some of the same corporate resources (legal, financial overheads).

¹ Annual Report, PT Finland, 1994.
• Singapore Post could draw on Telecom’s resource pool to staff some of its management positions.
• Coordination of post and telecommunications would improve.

The perceived major disadvantages of this structure were the following:
• Potential conflict over the provision of electronic and hybrid services
• The fear that the Post might not have the opportunity to develop fully into an autonomous organization
• Uncertainty about the Post’s future.

Legal Transformation

New Zealand. The New Zealand postal service operates within the legislative framework of: (1) the State-Owned Enterprises Act; (2) the Postal Services Act; and (3) the Articles of Association of the New Zealand Post Limited. This legislation is described below.

The State-Owned Enterprises Act, which is the umbrella legislation for the establishment of several state-owned enterprises (SOEs), of which New Zealand Post Limited is one, spells out the nature of the government’s ownership of the company, the broad business objectives to be achieved, and the operating requirements. The act specifically requires that the Post: (1) be as profitable and efficient as comparable businesses in the private sector; (2) be a good employer; and (3) exhibit a sense of social responsibility to the extent possible.

The Act defines the roles of directors and specifies the responsibility of shareholding ministers. By also outlining the reporting requirements for SOEs, the Act deliberately distances commercial management of the Post from political control. The Act explicitly stipulates that where an SOE undertakes non-commercial activities at the request of the Crown, these services will be explicitly funded by the Crown.

The Postal Services Act is a brief legislation which identifies the extent of the letter post monopoly and the postal obligations and also the international obligations that New Zealand Post must meet. The act also specifies that the Post must establish and maintain transparent accounting arrangements and an audit trail to clearly separate letter services subject to statutory protection from other activities. This is intended to prevent cross-subsidization into other competitive areas.

2The case of New Zealand is unusual in that the structure of the commercial postal service is defined outside the Postal Services Act. This is because the government set up eight state-owned enterprises (SOEs) simultaneously and passed a single SOE Act in 1986 defining the structure of all of these organizations, including the New Zealand Post.
The Articles of Association of New Zealand Post Limited are similar to those of a private company, set up under the provisions of the Companies Act. The Articles cover such matters as the issue of shares, procedures for meetings, voting rights of directors, and other corporate governance issues.

Sweden: Sweden eliminated the monopoly protection on letter mail in 1993, thereby completely deregulating its postal market. In 1994 Sweden Post changed its status from a public service corporation to a limited liability company. Sweden had never had a comprehensive postal law. In fact, the previous monopoly provisions were enacted in legal statements of a lower status than an actual law. The last legal text concerning the monopoly dated from 1947 and was not subsequently updated. However, with the liberalization of the postal market, it was decided to regulate certain aspects of the market through a special law. Unlike such laws in other countries, the new Postal Services Act, which was promulgated in 1994, is applicable not only to the public operator but also to the entire postal sector including existing and potential private operators.

The Postal Services Act ensures the general public a right to a postal service according to law, placing the burden of ensuring a good postal service on the government. In turn, the Act gives the government complete freedom to contract with any company in the market that is able to provide a postal service (thereby introducing the possibility of contestability). At present, however, Sweden Post is the only operator qualified to serve the entire country. In 1996, when the first contract between Sweden Post and the government lapses, the government has the option to appoint another, or several other, operators. The Act also defines the limits of the universal service (letters up to 2 kg and parcels up to 20 kg). The Act also stipulates that the privilege of issuing stamps designed according to the UPU Convention would be reserved for the operator appointed by the government to fulfill its obligations according to the UPU Acts. However, this implies that all other operators are free to issue stamps with another design.

The Postal Services Act also lays the basis for a supervisory authority responsible for monitoring the application of the Act and intervening in the case of anomalies. This regulatory body, which is now functioning, is the National Swedish Post and Telecom Agency, a section of the Ministry of Transport and Communication. Thus, the functions of ownership, operation, and regulation have been completely separated.

Legal Classification

Sweden: From 1911 to 1994, Sweden Post was a public service corporation. Although it was an independent financial unit in relation to
the state budget and was financially self-sustaining. Sweden Post was an integral part of the state with respect to capitalization and investments, and financing had to be approved by Parliament. In Sweden, the postal service and telecommunications were never combined in the same administration; therefore, the postal service was never cross-subsidized by the telecommunications business and was compelled to balance its budget through its own efforts. Sweden Post was obligated to obey all directives issued by the government and Parliament, and was also subject to several restrictions with respect to the formation of companies and to the acquisition and divestment of real estate or other businesses. This organizational form considerably constrained the ability of Sweden Post to operate commercially.

Sweden Post became a limited liability company in 1994. The state retained complete ownership of Sweden Post. The Post's change of status was a gradual process. In the mid-1980s Sweden Post bought all of its assets from the state. At the same time, it was given complete autonomy to decide on and finance its investments. Then, in the few years prior to incorporation, Sweden Post was given complete autonomy to set prices, subject only to a limited price cap.

Sweden Post was incorporated mainly to create a level playing field in the postal market. The Post will now be subject to the same opportunities and restraints as its competitors (such as negotiating labor contracts with employees, forming alliances, and also paying corporate tax, VAT, and pensions, etc.). In addition, the major clientele of Sweden Post is other limited companies that prefer to deal with a limited company rather than a government enterprise whose decisions are more likely to be influenced by politics. Corporatization of Sweden Post has also clearly defined the role of the state as owner of and customer for Sweden Post's services.

Papua New Guinea: PTC, as a statutory authority, is headed by a Managing Director who reports to the Board of Directors, which in turn reports to the Minister of Information and Communications. PTC is supposed to have control over its own revenue use, and is required to realize a target return on assets and to pay taxes and dividends to the government. Numerous government controls placed on PTC, as a statutory authority, limit its autonomy severely. Rate setting must be approved by the Department of Finance and Planning. The Ministry of Finance must approve all capital expenditure above US$300,000. Limitations stipulated in the 1982 PTC Act restrict the postal service with regard to expanding its agency services. The postal service is subject to the Salaries and Conditions Monitoring Act, which specifies job grades, salary levels, and benefits for all government employees. This has resulted in salaries that are lower than the private sector for management positions and are relatively generous for lower level staff. Thus, prices, investment decisions, personnel practices, and, to some extent, commercial strategies are subject to gov-
government control. Papua New Guinea has been poised to take the major step of privatizing its telecommunications. However, the postal service's stance on this proposed reform of PTC has not been clarified.

**Finland:** The postal service in Finland, a limited liability company since 1994, is one of five subsidiaries within the PT Finland Group which is responsible for providing post and telecommunications services. PT Finland Ltd., a limited liability company wholly owned by the Finnish state, incorporated its operations at the beginning of 1994. Each subsidiary within PT Finland is also a limited company. This change in legal status and reorganization were undertaken to highlight profitability, improve marketing management, and prepare for increasing competition in the post and telecommunications business.

**Argentina:** In 1993 the Argentine postal service was incorporated into Encotesa Inc., which was headed by an Argentine professional team in cooperation with specialists from various countries to assist in the transition phase. In order to level the playing field, the following steps (among others) were taken:

- Encotesa would pay taxes on an equal footing with its competitors. Therefore the postal tax formerly paid by private couriers was eliminated and Encotesa began paying the VAT.
- An explicit subsidy would be provided to Encotesa, if necessary, to help it meet its service obligations.
- Although Encotesa had the exclusive delivery of mail items from the state administration and the City of Buenos Aires, in future the government would adopt competitive tendering based on price for this service.

**Australia:** From 1901 to 1975, the Australian national postal service operated as a government department (the Postmaster-General's Department). In 1975, two separate statutory authorities were established for telecommunications and the post. The Australian Postal Commission's main function was to operate the postal services with a pronounced social mission. The Commission did not have a commercial chapter, although it was required to recover costs and to fund at least half of its capital expenditure requirements. In 1989 the postal service was corporatized. The Australia Postal Corporation is still wholly owned by the government, but the 1989 reforms restricted the government's influence on strategic controls and ended the government's day-to-day bureaucratic controls. Through this corporatization, the postal enterprise was put on a positive commercial footing. Although social objectives were still explicitly included in the postal enterprise's charter, their scope, content, and cost impact were specified and quantified. Thus, corporatization separated ownership and regulation from the operations aspect of the postal ser-
vices, and, more important, allowed the social and commercial ob-
jectives of the post to be reconciled in an explicitly planned manner.

Functions, Powers, and Obligations

Sweden: A specific contract was drawn up in 1993 between the Post
and the government which, among other matters, specified the fol-
lowing:

- The Post would provide a nationwide mail service (including
delivery of newspapers) at uniform and reasonable cost
without compensation from the government. The universal
service is defined by the Postal Act (letters up to 2 kg and
parcels up to 20 kg).
- The Post would provide a nationwide counter service. Some
compensation would be paid for retaining counter services
in small localities where other mechanisms for payment
transactions are not available. In 1993, Sweden Post was
remunerated in the amount of SKr 300 million for maintain-
ing a nationwide counter service and it expected to receive
the same compensation in 1994.
- The state would compensate Sweden Post for its other so-
cial commitments, such as free delivery of literature to the
blind, services for the elderly and disabled in low-popula-
tion areas, etc. In 1993 these costs were estimated at
SKr 565 million.
- The contract also included further specifications about the
delivery, quality of service, and principles of pricing of vari-
ous categories of mail.

New Zealand: New Zealand Post and the government agreed on a
Deed of Understanding to formalize service obligations in exchange
for a continued level of protection. The main features of the Deed
are:

- The universal letter service will be continued.
- Existing delivery standards will be maintained.
- The Post will be obliged to maintain a basic network of New
Zealand Post agency outlets.
- A price ceiling of CPI - 2 percent would be imposed initially
on the basic first class letter rate; after this the ceiling would
be CPI - 1 percent.

The Netherlands: The provisions of the Postal Act specify that the
holder of the postal concession shall have the following obligations:

- It shall transport postal items (up to certain maximum weights
and sizes) for anyone throughout the Netherlands and to
and from other countries in return for payment (unless in violation of the law).

- It shall comply with the general directives laid down by the Minister of Transport, Public Works and Water Management.
- It shall have an exclusive concession, unless the Act specifies otherwise, for the conveyance of letters weighing up to 500 g. It shall also have the exclusive right to place posting boxes on public highways and to issue stamps depicting the monarch or bearing the word Nederland.

**Australia:** Through all of the Australian postal service’s successive waves of reform, the government has been committed to maintaining the nationwide basic letter service at uniform rates. The reform packages have continued to retain a level of reserved services protection to meet the principle of universal access (although these have been progressively reduced and are to be reviewed again in 1996: see Table 2.1 in Chapter 2). While corporatization in 1989 clearly separated the commercial from the social objectives of the post, community service obligations are still funded by a cross-subsidy within letter services from low to high cost mail paths. However, with corporatization, the scope, content, and cost impact of the social objectives have been clearly specified and quantified. The 1992 Industry Commission had recommended that the Australia postal service’s community service obligations be funded by a direct budget subsidy based on criteria of transparency, clarity, and incentives for efficient behavior. This proposal is likely to be considered again in the 1996 review of future arrangements for the Australia post.
The postal market can be divided broadly into “individual” and “business” segments. The individual segment is mainly concerned with securing safe and reliable services from the postal operation. Although this would appear relatively straightforward, many postal services fall short of these simple demands. In addition, in most countries the principal driving force behind postal activity is no longer merely the communication between individuals for personal reasons. While this is still an important market segment, large untapped avenues for growth exist in business generated communication, which, like any other transaction intrinsic to markets, is also based on competitiveness. Therefore, unlike the “individual” segment, which required merely a reliable postal service with a single rate structure that was economical, businesses require an array of services at varying prices to meet their various needs. Each of these services must be characterized by speed, security, and guaranteed delivery for domestic as well as international items. Today, to regain lost ground and competitiveness, the postal service must acknowledge and respond to both of the above segments.

The post, therefore, should be seen as a “service industry,” providing services that meet customer demand. Such a commercial orientation is currently absent in most postal administrations, which are characterized by their civil service outlook and by some weaknesses which are common to certain public enterprises (see Table 4.1). Under these circumstances, managers have little incentive or authority to satisfy customers or to achieve a reasonable financial return. Therefore, in addition to affording the postal service the protection of a commercial operation by corporatizing it, several business practices not common to the public sector will have to become part of the post’s routine operations.
Commercialization is the process of introducing these market principles into postal administrations. Therefore, core areas such as finance, accounting, strategic planning, marketing, and so on, will have to be either introduced or strengthened within postal administrations. Training can be provided for core functions, and often experienced personnel are brought in from the private sector or the management function is contracted out for specific periods. These measures can hasten the learning process and ensure its effectiveness. While some restructuring measures are within the realm of any postal administration's autonomy, the authority to introduce many reform steps may have to be specifically included in legislation, or explicitly sanctioned for a government department or a statutory corporation. However, a limited liability company, which has all the powers of a legal entity, normally has the freedom to undertake most reform measures.

Table 4.1
Common Management Problems in Public Sector Infrastructure Entities, 1980-92

<table>
<thead>
<tr>
<th>Sector</th>
<th>Number of Projects</th>
<th>Unclear Goals</th>
<th>Lack of Management Accountability and Autonomy</th>
<th>Financial Problems</th>
<th>Wage and Labor Problems</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electricity</td>
<td>48</td>
<td>27</td>
<td>33</td>
<td>73</td>
<td>31</td>
</tr>
<tr>
<td>Water</td>
<td>40</td>
<td>25</td>
<td>40</td>
<td>70</td>
<td>35</td>
</tr>
<tr>
<td>Telecom</td>
<td>34</td>
<td>15</td>
<td>35</td>
<td>53</td>
<td>32</td>
</tr>
<tr>
<td>Rail</td>
<td>39</td>
<td>15</td>
<td>21</td>
<td>54</td>
<td>33</td>
</tr>
<tr>
<td>Roads</td>
<td>35</td>
<td>9</td>
<td>23</td>
<td>40</td>
<td>40</td>
</tr>
<tr>
<td>Ports</td>
<td>28</td>
<td>21</td>
<td>36</td>
<td>32</td>
<td>43</td>
</tr>
</tbody>
</table>


As was mentioned in the preceding chapter, commercialization need not necessarily follow or precede corporatization. There are many actions that postal administrations can take to improve quality of services and develop financial self-sufficiency and a market-oriented outlook even without the legislative changes that accompany corporatization. In a few postal administrations these changes have been introduced sequentially and corporatization is regarded as the next major step in the process of postal reform (see the discussion of Chile later in this chapter, as well as the cases for Chile, Singapore, and Sweden). However, complete commercialization cannot be achieved without the appropriate autonomy, accountability, and incentives that corporatization grants, nor can corporatization by itself lead to successful reform. Therefore, for reform to achieve its goals, it is vital that both processes be implemented. Some postal administrations have chosen to first initiate the corporatization process, followed by commercialization, in the interest of clarifying the roles and responsibilities of all parties and thereby accelerating reform.
Changes at the policy level, such as market deregulation, establishment of an autonomous regulator, or corporatization of the postal service, affect the parameters within which the service operates. This chapter, however, concentrates on what it is that the post can do to improve itself within these parameters. Therefore, the steps taken to commercialize the post may be termed enterprise reform. The mandate of financial self-sufficiency, or a specified financial return, that accompanies corporatization forces the postal service to do the following:

1. Look inward to eliminate operational inefficiency, reduce costs, and improve the service
2. Look outward to gauge market needs and tailor services accordingly.

This chapter covers the principal steps involved in this process of enterprise reform. Therefore, it dwells on the main areas in which most postal administrations, by virtue of being government bureaucracies, need to develop expertise or on which they should focus. Many of these areas, such as corporate planning and strategy, marketing, new product development, management information systems, etc., are fundamental management concepts for which ample academic and other published literature exists. For such issues, this chapter does not provide a detailed description. It is the chapter's intent to bring out the relevance of these areas to the postal service, and to supplement this with examples from various postal administrations. The experiences and practices cited here merely represent some ways of approaching the commercialization of the postal service. Each country's "best practice" will ultimately have to be tailored to its own individual conditions and requirements.

Like many government bureaucracies, postal administrations are typically overstaffed, their assets are not aligned with their operational requirements, and their operating procedures are not up to standard and are outdated. There are several reasons for such inefficiencies. First, the commercial aspects of a postal administration are not accorded primacy. Therefore, the postal service is neither required to attain operational efficiency nor is it rewarded for such efficiency. In addition, the social obligations of a postal service often take precedence over, and are not reconciled with, the service's commercial goals. Thus, the postal service is required to provide unpaid services to the government, the costs of its universal obligations are neither quantified nor compensated for, and it cannot restructure the postal network or its own employment because of social and political concerns.
In many countries the postal service has "grown" in an unfocused way. Unfortunately, expansion has not always been targeted to the best use of resources. For example, a common tendency is for postal services to augment their staff and network of post offices in an attempt to reach more customers, whereas resources may have been better spent in consolidating, modernizing, or restructuring other aspects of the collection, mail processing, or distribution systems. At the very least, a feasibility analysis would be called for any investment or expansion, and this requires adequate financial information and expertise, which have traditionally been lacking. In postal administrations with inadequate funds, maintenance and rehabilitation of assets is another significant issue that needs to be addressed. Under the above circumstances, a considerable amount of restructuring would be necessary to bring about internal efficiencies.

With corporatization, or some form of imposed fiscal discipline, postal administrations are beginning to implement specific steps to reduce costs and improve productivity (see the discussion immediately below, on New Zealand Post). Emphasis on the commercial objectives of the postal service and on the explicit reconciliation of commercial objectives with social goals is an important move toward bringing about accountability (see examples from Australia, Sweden, and the Netherlands in the previous chapter). In addition, the increase in autonomy and incentives is leading to proactive reform in several operational, administrative, and managerial areas.

When New Zealand Post was corporatized in 1987, it faced a significant operational challenge. In its previous year the postal component alone had suffered a loss of NZ$40 million, which was likely to continue unless drastic steps to restructure the organization were taken. The Post suffered from a lack of management systems, misallocated assets (an excess of post office buildings instead of mail processing plants), and a very poor public image among its clientele and customers. Hours of operation were unrelated to business demands, shifts were misaligned, and not enough use was made of temporary staff. To address these severe problems, New Zealand Post took the following steps to cut down on costs and improve productivity.

1. **Cost Control**
   - A major shift took place, away from company retail outlets to private sector agencies. In 1988, 432 company owned postal outlets were closed and replaced with a network of private sector retail outlets. In 1991, more than 80 percent of the 1,400 outlets were privately owned, which significantly reduced fixed costs.
   - By 1994 the workforce was reduced by 40 percent. The need for change was widely communicated throughout the
organization and natural attrition and voluntary redundancy permitted a downsizing of the work force.

- Recurring non-personnel expenditure was reduced by 30 percent in the first year.
- Inventory levels were reduced by more than 40 percent in the first year.
- Conveyance expenditure was reduced by 30 to 35 percent with the introduction of commercial price negotiation through selective or open tendering.
- Credit controls were tightened to ensure that receivables were repaid on time.

2. Productivity Improvement

- Capital expenditure was redirected from providing retail outlets to modernizing the mail processing network, replacing vehicles, and developing computer systems to replace costly manual processes.
- Significant staffing changes were implemented, including the employment of part-time staff for peak traffic hours.
- A concerted effort was made to rapidly cultivate a marketing and customer-driven outlook through the recruitment of sales and marketing professionals from the private sector.
- Mail processing centers were required to operate a no inventory policy, and, coupled with more attention to networking, this has led to consistent on-time delivery standards of 96 to 97 percent for all mail.
- In the retail area, although a major rationalization of post offices was undertaken, growth opportunities were actively explored. Merchandising in Post shops has been developed as a significant source of revenues.
- Track and trace computer systems were purchased from another postal administration and modified for the specific needs of New Zealand Post. This investment was targeted toward enabling the Post to compete in courier and parcel services.
- A program of counter automation was introduced to improve the response time to customer inquiries about mail and to achieve more rapid and accurate data entry. It would also make possible the provision of an expanded range of agency services such as the motor vehicle registration service.
- Optical Character Readers were purchased to provide very high speed electronic sorting of machine addressed mail down to individual postal delivery rounds.
- A mail containerization program was implemented to maximize the volume of mail moved in protective containers ca-
pable of being handled by forklift. This was also meant to minimize damage in handling.

- Line haul services were extended across the country.
- Several innovative pricing schemes and new services were introduced to increase market share.
- An Information System Strategy Plan was developed to provide a platform for direction and growth in the counter automation, track and trace, and customer management programs, and in upgrading the telephone systems. The aim is to develop and enhance the management information, recording, access, switching, and distribution systems of the Post.

In spite of the severe rationalization schemes, by 1994 the Post had achieved a volume increase of 25 percent. Real unit costs, as measured by total real expenditure divided by total volumes, were reduced by 20 percent. The Post achieved a 30 percent return after tax on shareholders’ funds and a 16 percent return on sales before tax. Over the eight-year period, prices were raised once by 12.5 percent while inflation was 30 percent over the same period.

In certain cases, as has been mentioned, commercialization has been undertaken without corporatization, as, for example, in Chile. In Chile commercial mail accounts for 75 percent of the total mail volume. The principal sources of future expansion are believed to be in direct mail marketing, mail-order sales, and express mail, all of which are areas that face significant competition from private couriers as well as electronic communication mechanisms. Although these markets possess a considerable amount of untapped potential, the Chilean Postal Corporation (Correos de Chile) underwent significant internal reform so that it could effectively service its demands and could also compete.

In 1989 Correos de Chile faced a crisis in several key areas: (1) inadequate investment; (2) rates that were below operating costs; (3) a limited range of products; (4) lack of government interest in postal service development; (5) lack of strategic vision; (6) a poor public image; (7) poor staff morale; and (8) the lowest wages in the public sector.

The postal service’s management developed a strategy to address the above and also to instill a customer orientation into the corporation which would enable it to recover lost ground and win new markets. This strategy was aimed at three key areas:

- A **commercial** focus on the customer: specifically, to seek and develop a new position for the corporation in the market

- An **internal management** focus on tasks: specifically, to implement a technological and administrative program within the postal service
A human resources focus on people: specifically, to re-evaluate the human capital within the postal service as a function of changes undertaken.

To implement its goals, the management developed corporate projects that cut across functional compartmentalization and lines of hierarchy to overcome the tendency to inertia in public administrations. These corporate projects were supported by clear systems of evaluation and coordination. The principal corporate projects were:

1. Information systems development
2. A training plan
3. A quality plan
4. Commitment to a performance program
5. New products
6. An employee participation program
7. A corporate image and environmental working conditions program
8. A regionalization and decentralization program
9. A domestic delivery system

Three years after making a concerted effort at commercialization, Correos de Chile experienced a noticeable improvement in quality of services, in physical and human resources, in employee wages, and in its overall financial aspects. A substantial aspect of these financial improvements can be attributed to price increases, which outpaced inflation until 1993. The objective from 1993 onward was to achieve real increases in revenue through improved efficiency. Another key bottleneck being targeted is the delivery system, which is still a source of considerable inefficiency. As a result of these steps, Correos de Chile showed the following results from 1990 to 1993:

<table>
<thead>
<tr>
<th>Growth, 1990-93 (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mail Volume</td>
</tr>
<tr>
<td>Revenue</td>
</tr>
<tr>
<td>Investment</td>
</tr>
<tr>
<td>Training</td>
</tr>
<tr>
<td>Return on Capital</td>
</tr>
<tr>
<td>Transfers to Treasury</td>
</tr>
</tbody>
</table>

The case of Chile illustrates the point that postal administrations can do much to develop a commercial attitude and manage a postal service in a financially self-sufficient way. Changes in management focus and organizational attitude can achieve results independent of legislative transformation. However, in the words of the General Manager of Correos de Chile, these improvements have been achieved “despite the disadvantages of the Corporation’s current legal framework that result in limited business opportunities, penalizing taxes, and a disproportionate reliance on the national Treasury.”

Further examples of improved operational efficiency are given in Annex 1 to this chapter.

---

Postal reform is being accompanied increasingly by a clarification of the postal service's mission and goals, which are being stated explicitly. The postal service is being held accountable for achieving this mission and these goals. Therefore, it is essential (as in any other business) that the postal service develop a clear plan of what it aims to achieve and how it intends to meet its own internal goals. While this is mandatory for introducing a systematic approach toward operations, the formalization of this process will also furnish information that is relevant to the owners of the service. The primary purposes of a corporate plan are, therefore, as follows:

1. To reveal the direction of development for the business, as intended by top management and the board
2. To form a "contract," in the planning period, between the owners and management, regarding the results of the business. This may require that the production and presentation of the corporate plan be specified legislatively.

The planning functions include both a long-term strategic plan and an annual performance or business plan. Such plans are fundamentally different from those requested by government from government departments, which focus primarily on expenditures and budget reconciliation. The corporate plan is usually organized around a time frame of five years and its contents include:

- A mission statement covering the objectives, major functions, and operations of the postal service and its subsidiaries, if any
- Overall management and financial strategies and policies to achieve objectives and discharge obligations
- Performance and financial indicators and targets
- Key factors external to the postal service that may significantly affect the attainment of objectives
- The estimated cost of carrying out community services and other obligations.

The annual performance plan should be consistent with the corporate plan for the period. It will include the following:

- Financial targets, profitability forecasts, and forecasts of capital expenditure and borrowings
- Performance goals in objective, quantifiable, and measurable form to define the level of performance to be achieved by each operational activity
- Human, capital, technological, and other resources required to meet performance goals
- Performance indicators for assessing outputs, quality levels, and the outcome of each operational activity.
In the Netherlands, for example, the postal service has aggressively cultivated a strong international strategy for itself, and it is one of the most progressive postal administrations in terms of the extent of its commercialization. For the coming years, the objectives of the state post and telecommunications company (KPN), are:

- To retain its position as the market leader on the national markets for postal and telecommunications services
- To rank among the top ten international suppliers of postal and telecommunications services by the year 2000
- To increase sales in tandem with receiving a good return on investment
- To continue improving price/performance ratios.

To achieve these objectives, KPN's stated strategy is as follows:

- To introduce new services and to stimulate the use of existing ones
- To raise the quality of service while containing costs
- To expand internationally from a strong position in its home market, often in partnership with other companies
- To devote attention to the quality of staff through its human resources policy.

PTT Post, KPN’s postal arm, feels that the market for international mail offers the best growth opportunities. While this market will grow in response to the single European market, the Post also anticipates mounting competition from other postal companies known as “integrators.” It is therefore trying to develop better alternatives to traditional mail to increase its share of international conveyance.

Public enterprises in general are the rigid, vertically structured hierarchies that fit Weber’s classic description of a bureaucracy. Actions that attempt to achieve far-reaching transformation within such a setup have very limited chances of success because of their inherent inertia. For this reason, the transformation to a corporate status will call for the introduction of elements of flexibility and the reorientation of the organizational structure.

Commercialization brings with it a change in the goals and focus of the organization. The postal service will have to shift from merely meeting its service obligations to assuming a customer-oriented approach where the focus is on quality, cost, and profits (see Table 4.2). Lean, flat structures are often considered more efficient and responsive to these commercial needs. The optimal organization, whether it is structured by product, area, function, or a matrix of various attributes, will naturally depend on the specific circumstances of a postal
service and an assessment of how it can best achieve its goals. The control of administrative overheads is also a factor that may have to be reconciled with the need to maximize operational efficiency.

Table 4.2
Organizational Forms across Postal Enterprises

<table>
<thead>
<tr>
<th>Country</th>
<th>As of (Year)</th>
<th>Primary Organizational Form</th>
</tr>
</thead>
<tbody>
<tr>
<td>Netherlands</td>
<td>1993</td>
<td>Seven business units (1994): letters, direct marketing/printed papers, parcels, international, EMS, logistics, philately</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>1995</td>
<td>Strategic business unit segmented into: letters, parcels, counters, subscription</td>
</tr>
<tr>
<td>Sweden</td>
<td>1995</td>
<td>By product/business grouping Four divisions: letters, parcels, counters, giro</td>
</tr>
<tr>
<td>Myanmar</td>
<td>1995</td>
<td>By function</td>
</tr>
<tr>
<td>Finland</td>
<td>1994</td>
<td>Three business groups: letter mail and transport, publication and delivery, counters</td>
</tr>
<tr>
<td>Ukraine</td>
<td>1993</td>
<td>By region</td>
</tr>
<tr>
<td>New Zealand</td>
<td>1994</td>
<td>Three strategic business units: letter post, commercial, property</td>
</tr>
<tr>
<td>Canada</td>
<td>1995</td>
<td>Matrix structure by function and product</td>
</tr>
<tr>
<td>Chile</td>
<td>1995</td>
<td>Regional organization with 13 units</td>
</tr>
<tr>
<td>Singapore</td>
<td>1995</td>
<td>Functional and business organizational setup. Three divisions: letters and parcels, sales and marketing, engineering and computer services</td>
</tr>
<tr>
<td>Tanzania</td>
<td>1994</td>
<td>Organized around functional lines</td>
</tr>
</tbody>
</table>

In the Philippines, for example, the operations of the Philippine Postal Corporation (Philpost) had been adversely affected by the weaknesses and deficiencies inherent in its bureaucratic organizational form. Authority and responsibilities were excessively concentrated with the Postmaster General and the Regional Directors and the operating units were held to minimal accountability. After corporatization, a dynamic reorganization process was undertaken. This led to the adoption of a functional structure (administration, finance, operations, and marketing and business development) wherein operations was subdivided into 14 regional offices with increased levels of decentralization. In addition, to optimize the cost efficiency of delivering the core service, Philpost developed certain autonomous sub-units as profit centers. Participative planning mechanisms have also been implemented in order to broaden the contributory base of officers and employees in all aspects of corporate management.

In New Zealand, when the Post was corporatized, the traditional functional organization form was retained, since it was considered appropriate for the first year of operation. This form was chosen to
facilitate the acquisition of new skills and to build a management team. Prominence was given to strengthening three new areas: strategy and business planning, finance, and marketing. During the second year of operation a new management structure was introduced based on a "divisionalized" organizational form. The three divisions were: letter post, commercial services, and property. Each would operate as a profit center with its own set of audited accounts. The thrust of this reorganization was to build on the core product, enter new business fields, and assess acquisition opportunities. The Post did not want to rely solely on the basic letter post for its long-term survival but wanted to see value-added products and services grow and prosper. Thus, the organizational form evolved according to the requirements and goals of the Post.

The experience of the Czech Republic has been that the reorganization of the overall structure of the Czech Post has led to considerable decentralization. Management's organizational structure at the corporate level is rather flat and staffing is small (0.34 percent of the workforce). Operational responsibility is entrusted to five business units (transport and sorting, logistics, computer centers for Prague and Vitkov, and International) and eight regional directorates, all of which are highly autonomous. Headquarters is organized functionally and so are the regional offices. Most of the business units have been designated as full profit centers and charge the regions for their services. The concept of intra-company charges is to be expanded, in conformity with the philosophy of managing the organization through a collection of relatively autonomous, but accountable, profit centers.

In the case of Sweden, commercialization preceded corporatization. The evolution of Sweden Post from a product-led government agency to a modern, profit-led commercial business began in 1984, when a basic business orientation was introduced. In 1989, systematic business planning with a focus on profits, as well as on customer and personnel satisfaction, was introduced. Simultaneously, Sweden Post was reorganized into logical profit centers managed by objectives. The third step was the reorganization of Sweden Post into clearly defined business areas. Since the end of 1994, Sweden Post has been a group consisting of a parent company (Sweden Post) and four subsidiaries, namely, the Letter Division, the Parcel Division, the Post Office Counter Division, and the Postgiro Bank Division (which is a limited liability company). However, it is made up of five business areas: Postgiro, banking services, counter services, parcels, and international. Each business area has responsibility for products, sales, production, and profitability within its area. The division of Sweden Post into business areas was designed to introduce greater efficiency into the management of the organization. It does not imply that the business areas are independent of each other. Internal purchases among the areas amounted to more than SKr 6 billion in 1993.
Corporatization is regarded as the final step in the reform of the postal service, and now Sweden Post has the additional flexibility to establish new forms of service via consortia, alliances, and company acquisitions, both in Sweden and internationally.

Staffing is a critical area in postal reform. The postal service sector is extremely labor-intensive and a significant amount of postal reform is concerned with the following staffing issues:

- Rationalizing labor
- Designing a corporate governance structure
- Reconfiguring the skills mix to suit the needs of the transformed organization
- Implementing appropriate incentive and penalty systems
- Improving working conditions for employees.

A governing board will be required to: (1) represent the interests of its owners; and (2) provide overall strategic direction for the development of the company without intervening in routine operations. Thus, excessive government oversight is replaced by a board, which should be given clear mandates and duties. Legislation or applicable company law should contain provisions covering the following issues concerning the board:

- Procedures and basis for the selection and appointment of directors
- Termination of appointments
- Size parameters of the board
- Duration of appointments and remuneration of members
- Voting rules and the power to delegate
- Declarations of conflicts of interest
- Duties and liabilities of directors
- Any liabilities or penalties attached to the breach of the above duties.

In a corporation, the method of appointment of the chief executive officer (CEO) will be specified in legislation, and the duration of appointment, powers, and remuneration may need to be specified as well. Several reforming postal services have chosen to staff senior level management with qualified people from the private sector in order to benefit from their expertise. To attract successful professionals (1) remuneration levels must be commensurate with those in the private sector, and (2) management must be given considerable autonomy in developing the corporation.

In the case of employees, legislation may specify the following:

- The classes of employees
- The power to set terms and conditions of employment, and the limits (if any) within which this power may be exercised
4. Enterprise Reform: Commercialization of the Postal Service

- The right to strike, in the case of a limited liability corporation
- Transitional provisions.

In most countries, by virtue of the post being owned and operated by the government, postal employees come under the purview of civil service statutes. This implies that compensation and employment are often separated from performance levels. This has been a significant institutional constraint in reforming postal services, and the trend is increasingly to change the laws governing employment practices to commercial/private law.

In Sweden, for example, in the five years preceding incorporation (1994) and also during 1994, staff was rationalized by some 12,000 employees for the following reasons:

- To align staffing levels with decreasing volumes of transactions at postal counters
- To promote more efficient working procedures
- To increase the mechanization of mail processing.

This rationalization led to the belief among staff and within political circles that corporatization was responsible for the employment reduction and generated considerable controversy and opposition. As a result, when corporatization eventually passed parliamentary approval, it did so by a slim margin. Therefore, in the Swedish postal service sector, which is highly labor-intensive and where considerable overstaffing exists, this experience points to the importance of giving serious consideration to handling labor problems and publicizing the internal and external benefits of postal reform.

Other examples of the handling of staffing and human resources can be found in Annex 1 to this chapter.

A truly autonomous postal service should have the power to acquire other organizations, own subsidiaries, form joint ventures or strategic alliances with private organizations, divest, or contract out any aspect of its operations that it sees fit in the commercial interests of the postal service. An autonomous postal service should not be restricted to government supply channels, but should be free to use them. It should not be bound to use other government agencies for transport services, procurement of property, construction of buildings, etc. A corporatized postal service, which is subject to company law, will be able to perform any of these activities unless otherwise stipulated in legislation. However, in the case of a statutory corporation these powers may have to be specifically granted through legislation. The freedom to perform the above-mentioned activities has provided many postal services with a commercial advantage.

For example, Canada Post believes very strongly in employing alliances in order to develop its competitiveness. Canada Post acquired Purolator, a major express courier operator in North America, in or-
Redirecting Mail: Postal Sector Reform

der to develop its presence in the domestic and international express mail market. The Post is also a member of GD Express Worldwide (GDEW) (See Box 4.1) for its international courier segment. The Post has major alliances with Air Canada (for transportation), Systemhouse (for information technology), and DMR (for information technology architecture). Therefore, all of the Post's information technology component, most of its air and surface transportation, and a large amount of vehicle maintenance are outsourced. The corporation sees value in concentrating on its core business and vertically disintegrating activities that can be performed in a better and more cost effective way externally. The corporation is also considering entering into partnerships with some banks, thereby increasing the provision of financial agency services at their retail outlets on an agent basis.

Box 4.1 International Cooperation: GD Express Worldwide

In 1993, five postal administrations (Switzerland, France, Germany, Canada, and the Netherlands) formed a 50-50 joint venture with the Australian-based private parcel operator TNT Express Worldwide to cooperatively service the international express mail arena. Since then, this venture, GD Express Worldwide (GDEW), has steadily added operating posts around the world. In 1994 it had more than 40 shareholding or contractual service partners and operated in 180 countries.

GDEW aims to run itself as a commercial and operationally autonomous company. Therefore, business is conducted on an arm's length basis, even where shareholders are concerned, and interlocking directorships are avoided. If shareholders cannot comply with the expected service standards, they are not awarded contracts for business. Evaluation of partners is based on purely commercial performance.

An interesting dimension to this venture is that shareholders agree to withdraw from the principal market in which GDEW is active—the international, time-guaranteed delivery market. The only areas of potential overlap are in international mail and contract logistics.

In the 1993 financial year, the volume of goods carried by GDEW increased by 20 percent, but average income per consignment fell as a result of over-capacity on the market. While GDEW was loss making as of 1994, the company poses a significant threat to other postal administrations in this market segment, especially if it is extended into the letter mail and electronic mail sectors.

Sweden Post also acquired a private sector information technology company and two leading electronic mail companies in order to gain competitiveness in the electronic and hybrid product segments. The Post has also established a new overnight parcel/packet service, the distribution of which is contracted out. In 1993 Sweden Post established a joint venture company with City Mail, its competitor in Stockholm, to administer change of address and mail forwarding information. This alliance was aimed at simplifying customer services in the deregulated market.

In the Netherlands, in order to operate efficiently, the Post has been given the freedom to acquire and invest capital and enter into partnerships with other companies. In 1993, PTT Post made the post
4. Enterprise Reform: Commercialization of the Postal Service

offices part of a joint venture with Postbank NV, reducing its share in this activity by half. The new company, Postkantoren BV, is intended to improve profitability by lowering overhead costs for both owners, and by broadening its range of services, cutting costs, and improving quality. Express Mail Service (EMS) has also reinforced its position in the courier market through the takeover of City Courier and Wini Traffic Couriers BV.

The Dutch Post has entered several new markets abroad, notably through acquisitions in Eastern Europe, and has also established sales arms in a number of countries. In the United Kingdom, PPIC (UK) Ltd. is targeting international mailers to use the Netherlands as their posting point. PTT Post International (PPI) also has offices in other countries which acquire items from foreign companies for international distribution. PTT Post has a large stake in a joint venture with KLM (the Royal Dutch Airlines) called InterPost Group. This partnership acquires customers in North America and Southeast Asia for the full service worldwide distribution of magazines. Through controlling this company, PTT Post hopes to be in a better position to serve the American market.

PTT Research, a subsidiary of KPN, carries out research and development aimed at improving and expanding the services of KPN and its group companies—mainly PTT Post and PTT Telecom. The main areas relevant to PTT Post are the following:

- Logistics processes (optimization and application of information technology)
- Automatic reading of postcodes and sorting systems based on these codes
- Networks and network management
- Cryptography (to advance the automation of the coding and sorting processes).

PTT Research undertakes strategic research within PTT Post's corporate objectives, and maintains an ongoing dialogue with the Post to ensure an optimal link between research and market requirements.

The Czech Post also felt the need to form a joint venture to fortify its market position. The Post had a dominant position in financial services during the communist era because of the absence of a commercial banking system. With the development of the banking sector and the evolution from a cash-based system to a system employing other financial instruments, the Czech Post is faced with a decrease in the demand for its financial services. Therefore, it has formed a partnership with a commercial savings bank to maintain its markets as well as to make commercial banking accessible to everyone, including consumers in the non-urban areas. Revenue from the Czech Post's joint venture with the Investment and Postbank rose to 382 million Czech koruny, or 5.6 percent of total revenue, in the joint venture's second year of operations.
If management is to keep track of performance, the development of internal information and control systems within the organization is vital. The information component involves the development of standard financial and cost-accounting procedures, as well as detailed quantitative and qualitative indicators. Commercial accounting procedures will be of immediate benefit for the development of information systems in the postal service. Explicit cost-accounting identifies nonremunerative activities and reveals sources of inefficiencies, thereby making costs and benefits far more transparent than they were under government departments. However, the introduction and implementation of standard accounting procedures is a tedious and lengthy process and may require external accounting expertise at the outset for those postal administrations that may not be familiar with these financial techniques.

For a postal administration to function commercially, a key accounting practice is a product profitability system. Typically, postal administrations are able to allocate revenue streams across different products but have no concept of product costing. One reason for this is the considerable extent of joint inputs across different products. From a competitor's perspective this may be considered a deliberate attempt to conceal the cross-subsidization of products behind ambiguous accounts or the lack of accounts. A product costing system is essential to identify the areas most in need of productivity improvement actions, including the control of overhead costs. This information is also needed for price-setting and strategic product management. Estimation techniques beyond conventional accounting techniques will be needed where joint processing of different types of products occurs.

Other important management information systems include the following:

- Budget preparation and control systems
- Internal performance monitoring systems
- A system to determine the cost of the community service obligations.

In the United Kingdom several factors have contributed to the financial success of the British Post Office (which has been profitable for the past 18 years); some of the key contributing factors have been the following:

- The preparation of proper commercial accounts dating back to 1969
- Investment appraisal methods that are based on realistic costs and reliable savings
- Costing methods that are able to distinguish which services are broadly profitable and which are not.
To extend its own success to other postal administrations, the Post Office considers the establishment of a proper accounting regime, with both product costing and investment appraisal systems, to be a first priority. These features are also essential to a well-directed marketing effort.

When Canada Post evolved from a government department to a Crown Corporation in 1981, no financial procedures were in place. Initially, emphasis was placed on instituting generally accepted accounting principles and controls to meet certain statutory requirements. Subsequent development of the financial systems has enabled the Corporation to track and monitor costs that are considered critical and also allows monitoring of the variance between planned and actual costs down to the manager and officer level. When Canada Post acquired a major private company to strengthen its express mail segment, a product costing methodology was developed by independent consultants for the Post in order to verify that the Post was not cross-subsidizing the express mail segment from its monopoly areas. Since then, product costing and contribution reporting are conducted on an annual basis within the Post and are taken into account in the planning process on product positioning. At more micro levels, revenue verification units and inventory control systems have been implemented.

The development of performance monitoring systems has also been vital to the improvement of Canada Post's operations. External performance monitoring and public reporting of performance levels of letter mail were instituted in 1987. Internal performance monitoring for the other products began in the middle to late 1980s, and from 1990 all new products were given performance monitoring systems at the time of their introduction. Productivity, volume, time, and attendance systems have been put in place at the employee level; quality assurance programs have also been implemented at the micro level.

A key need in the postal sector is the development of a progressive marketing mentality. Historically, most postal administrations have operated in a "public sector" mode, based on the assumption that the consumer has no alternative choice. From this perspective, marketing is not a necessary activity and product development and growth strategies are dictated by government fiat rather than by systematic market research. The intensification of direct and indirect competition has given increasing importance to marketing. The significance of the role of marketing activities has only recently been acknowledged by postal administrations. The marketing concept needs to be cultivated not only in the marketing division, but within the whole organization.

In 1990, the Universal Postal Union (UPU) held a symposium on "Market Research - Methods and Applications," an account of which is presented in "Commercial Strategies in the Various Branches of the Post," Study 711, by the Consultative Council for Postal Studies.
organization—which includes every location that has customer contact, as well as areas that provide customer services behind the scenes. Increasing sensitivity to customer requirements is vital for regaining and expanding the postal service’s share in the communications market.

An initial step in developing a marketing outlook should be the introduction of a separate marketing unit staffed by professionals. This unit’s functions would include the following:

- Market analysis to identify and anticipate customer needs
- Monitoring of activities and strategies of competitors
- Preparation of marketing plans and customer-oriented strategies
- Identification of customer characteristics (market segmentation)
- Design of new services and products to meet changing customer needs
- Estimation of the marketplace’s acceptance of potential new products and services
- Advertising and public relations
- Development of quality standards and customer satisfaction indicators
- Reporting of the results of surveys and performance measurements within the organization and externally (measurement of performance indicators should be undertaken by independent agencies in order to validate the process)
- Preparation of an institutional framework for the interface between management and customers
- Evaluation and monitoring of the effectiveness of marketing communications and advertising.

Advertising and sales promotion are widely used in some countries to prevent the diversion of mail volumes to other communications mechanisms, especially in areas in which the postal service does not have a monopoly (e.g., in parcels, financial services, EMS, electronic mail, consultancy, and several agency services). Special departments and sales forces are being used to promote contracts with top corporate clients, to change the postal identity, and to promote specific services and products. Among the adopted mechanisms are the following:

- Improvement of post office interiors and of product displays
- Improvement of telephone response and decrease in queuing time
- Attractive postal service logos, new uniforms, and identity badges for staff
- Increased international visibility through membership in international postal unions and participation in conferences
- Use of surveys and analyses of quality improvement and customer satisfaction
- Easier reference to products, rates, and services
- Use of community sponsorship programs and activities
- Certification of postal establishments according to the ISO 9000 standard which is an internationally accepted quality assurance standard
- Use of innovative advertising media, such as video advertising, in post offices.
- Publishing of stamp albums and participation in exhibitions and commemorations.

The full-fledged use of marketing to enhance competitiveness should contain a note of caution. Marketing can provide only limited assistance to a postal administration whose basic level of service and performance is sub-standard, and it is necessary to raise this basic level before communicating with customers and attempting to develop new products and services. Marketing activities alone are not a universal panacea.

Since its corporate transformation New Zealand Post has significantly upgraded the marketing of postal services. Under the Customer Care Program, an analysis of the Post's customer base targeted the (1,200) core customers that generated approximately 70 percent of the postal demand. The needs of these customers are regularly tracked and a special data file is maintained on each customer. Market research programs now determine customer perceptions of service, product awareness, etc. Growth targets have been set for all retail managers, and specific corporate targets have been set in select product areas. Postal products have been repositioned, and comprehensive internal and external promotional programs have been undertaken. Delivery performance is tested extensively and the results are advertised on a monthly basis in key newspapers. A Customer Management Program to handle inquiries and complaints has been established through dedicated centers in several cities, in order to decrease customer inquiry response time and streamline billing procedures at all the Post facilities. Phantom shopper surveys are conducted to monitor staff attitudes to customers and staff knowledge of products and services. Quality assurance systems were being introduced throughout the company by a specialist unit assisted by consultants from IBM (NZ) Ltd. The emphasis is on identifying customer needs, setting standards to meet customer needs, and providing regular measurement and feedback of results to work groups.

Finland Post has also devoted considerable resources to the development of total quality with the ISO 90004-2 standard and the
Malcolm Baldrige Quality award criteria. It is also focusing on cus-
tomer satisfaction and customer retention, and has commissioned
frequent customer satisfaction surveys to analyze the total quality of
its operations and services. Figure 4.1 shows some of the weighting
assigned by customers to various aspects of postal operations. Since
these weights vary in accordance with customer service requirements,
continuous feedback and quality monitoring and management are
essential to the operation and management system.

Other examples of marketing and customer orientation strategies
can be found in Annex 1 to this chapter.

Many postal services, particularly in middle and low income coun-
tries, provide a “supply-driven” rather than a “market-driven” service.
For example, in these countries the absence of products or services
to cater to the specific needs of bulk mailers or large business mail-
ers has resulted in low volumes from these market segments. As a
result, these bulk mailers usually make their own arrangements for
the national distribution of their mail or parcels. Evolving customer
needs, intensifying competition, and the advent of new technology
pose a continuing threat to the economic viability of the postal ser-
vice. Under such circumstances no organization can afford to main-
tain the same product line indefinitely if it wants to protect and enhance
its revenue base. These competitive trends, seen in many industries,
result in shorter product life cycles. Therefore, the postal service must
continually modernize its products.

Two distinct weaknesses characterize the present product devel-
opment efforts of most postal services. The first is internal and re-
flects the absence of a systematic new product development process
in which market and competitive analyses play a significant role. The
second weakness is external and is a function of the postal service’s
restrictive institutional and regulatory environment, which discourages
innovation in developing the product portfolio.

A wide variety of corporate missions and objectives, plus a range
of legislative, institutional, political, and market environments, can
result in significant differences in product development strategies for
the domestic postal market segment in various administrations. It is
essential for product development that each administration under-
stand the restrictions that this situation places on its products and
prices. Postal legislation and its interpretation frequently dictate the
avenues open to the postal service in product development. For ex-
ample, in Chile and the United Kingdom (see the relevant cases) the
postal administrations are being restricted from expanding their
agency services and entering the hybrid product market.

A policy decision must be made beforehand regarding the mission
of the post. Is the postal service to be confined to the traditional mail
market, or should it service the broader communications market and
provide other value added services (see Figure 4.2)? This decision
Figure 4.1
Criteria Affecting Customer Satisfaction and Retention in Finland

![Diagram of Success Criteria]


Figure 4.2
The Postal Market

![Postal Market Diagram]

High Profit Margin
Low Profit Margin

High Revenue Contribution
Low Revenue Contribution

EMS
Direct Marketing Mail
Letter Mail
Postgiro
Medium Profit Margin
Consulting Services
Parcels
Counter Services
Hybrid Mail
Low Profit Margin

Redirecting Mail: Postal Sector Reform

should not be based on the historical mission of the postal service but should focus on the post's unique assets, such as its unparalleled delivery and retail network, and should select the best use of this competitive advantage. The choice of growth strategies requires an evaluation of available resources and opportunities in light of the organization's fundamental mission and objectives. While the post's broader mission will be defined by the government's social and economic goals, within this framework the post should have the autonomy to develop new products and services. Excessive regulation will stifle innovation, thereby preventing the Post from catering to consumer needs.

Products

A unique decision criterion or a combination of decision criteria with pre-specified weights is vital to the choice of products for the development process. In Australia, for example, the decision criterion is the objective of the postal service, and this decision criterion is unambiguously stated as profit expressed as a return on total assets. In some developed countries, the traditional letter mail segment is considered a mature industry which will grow at a steady but low rate. Therefore, postal administrations are focusing on other avenues to develop value added services which typically command higher profit margins. In addition, evolving customer needs offer postal administrations additional opportunities to develop markets. This, combined with the presence of strong competition in virtually every field, whether legal or de facto, is necessitating systematic and efficient market research in the development of new products (see Figure 4.3). It is thus imperative that postal services develop systematic processes for the generation, development, evaluation, and introduction of new products.

Services

As far as the provision of new services is concerned, consumers will have no faith in new services until the existing basic and value added services operate at a high level of service which is measured and published. Users now have a wide choice of methods of communication, supported by technology that is advancing rapidly. Users are not concerned with who provides the service but are concerned to secure the right service to meet their needs at the right price. To this end, postal administrations should employ accounting and invoicing systems that reflect normal commercial practice.

Pricing

All customers seek a good service and price combination. For the universal service (the individual segment) this involves a fair service,
accessibility, and simple pricing structures. On the other hand, large commercial customers require the service provider to have a flexible approach and to be able to tailor services to the needs of their individual organizations. To this effect, postal administrations may need to use innovative pricing schemes as a mechanism for differentiating their products and providing incentives to valued customers (see Box 2.8 in Chapter 2, on "interconnection" in Australia). The structure of discounts is likely to vary according to the administration and will usually depend on the product, the volumes posted, and, more important, the operational system of the postal service. It is important that discounts be linked to cost savings, however, since the rampant provision of discounts leads to underpricing of the service—which defeats the goal of financial self-sufficiency.3

Figure 4.3
The Product Development Process

---

3In the case of Chile, where 70 to 80 percent of mail volume is generated by businesses, excessive discounts were offered in the past which had adverse financial consequences for the postal service.
A good example of product, services, and pricing innovation is found in New Zealand. New Zealand Post is seen as operating in the larger communications and retail transactions services markets. Therefore, in addition to traditional letter mail and parcels, it is developing and marketing electronic mail services and a variety of agency services. New Zealand Post aims at being able to offer an array of services that will be able to meet all customer needs: the customer should have access to bulk-mailing facilities, expedited mail, high quality courier and parcel services, and value added services such as direct mail consultancy, direct mail lists, etc. New Zealand Post has introduced the following new services:

- **Facilities Management Contracts:** For a fee, New Zealand Post employees would undertake the complete mailroom management for a firm, thereby freeing up overheads within the firm. This covers both internal mail processing and receipt and dispatch of mail and courier items.

- **Financial Transaction Processing Service:** This process will service the entire billing needs of a company by utilizing the retail, delivery, and mail network of the Post. Through a joint venture, the Post will prepare financial statements directly downloaded from a data link to a laser printer, will envelope the mail, and will transport and deliver it. In addition, the Post will receive and process payments, either through its retail outlets or by business reply post at a central processing center.

- **Ad Post:** In order to be able to capture the unaddressed advertising mail segment, the Post acquired a small circular delivery company to service this area.

Upon corporatization, the Post also assumed the autonomous responsibility to set prices for its competitive areas. The following are some of the steps taken to improve the service and build market share through differentiated pricing techniques.

- In 1988 the Post stopped giving registered publications discounts, which were not commercially justifiable and which had been cross-subsidized.

- Differentiated pricing for enveloped mail based on weight criteria was eliminated and a three step price structure based on envelope sizes (medium, large, and extra large) and corresponding to paper size standards was implemented.

- A new service called BoxLink was introduced for commercial customers. BoxLink offers a complete mail service in which customers are charged an annual total fee based on estimated annual volume, size of articles, and distribution.
patterns. This service offers high performance (overnight mail service) and eliminates the need for stamping, franking, and other mail processing activities; in addition, the mail is picked up by a courier at pre-set times. This contract pricing offers the opportunity to price differentially for service, distance, and other factors, but removes the need to do this for each individual mail item.

Other examples of innovation in products, services, and pricing are provided in Annex 1 to this chapter.

Commercialization, as it applies to the post, is in the process of introducing market principles into postal administrations. Therefore, the post should be seen as a service industry that is oriented toward meeting customer demand.

Using a number of country examples, the chapter has discussed major steps in this reform process: operational efficiency; corporate planning and strategy; organizational structure; staffing; acquisitions and alliances; internal reporting and control; marketing and customer relations; and innovation in products, services, and pricing.

This chapter concentrates on the above areas from the point of view of what the postal service can do to improve itself. If the reformed postal sector is to respond competitively to servicing the business market, certain business practices not common in the public sector must become part of the post's operations.
Operational Efficiency Improvements

*Sweden:* In the years preceding incorporation, Sweden Post was in the throes of development, renewal, and restructuring to meet the conditions created by deregulation, new technology, and internalization. As part of the rationalization scheme, the number of employees continued to decline. Nonetheless, the Post's capacity to handle mail volumes increased, indicating improved internal operations (see Figure 4A.1). The post office network was also undergoing development and restructuring so as to provide a nationwide network of counter services at reasonable cost. The network is being coordinated with other services and is taking on new complementary tasks in collaboration with various partners, mainly shops and banks.

Figure 4A.1
Postal Operations and Outlets, Sweden, 1989-93

Total productivity, which describes the relationship between revenues and personnel costs calculated at fixed prices, shows an erratic pattern but a healthy recovery in the final year preceding corporatization. As of 1993, total productivity was required to increase by at least 2 percent annually. In terms of financial profitability, the Post is required by the owner to achieve a return on equity of at least 11 to 13 percent, which it consistently exceeded in the past. Profit after financial items has been relatively stable, except for 1990, which was a year of extreme conditions (in the form of a boom in the economy and a bank strike) (see Figure 4A.2).
As far as tariffs are concerned, in real terms the price of a letter has actually decreased considerably over the last decade in Sweden (see Figure 4A.3). This phenomenon, combined with Sweden Post's financial success, points to the achievement of business expansion as well as cost efficiencies. In terms of affordability as well, the consumers appear to be well off in Sweden compared with several other countries.

Sweden Post is also aiming to achieve 98 percent automation of letter sorting by 1996. Correspondingly, it is consolidating its sorting centers, which were reduced in number from 44 to 32 in 1993.

Finland: Finland Post became a limited liability company in 1994 after having been a government department for many years and then a business enterprise for four years. Employment relationships were changed from state to private sector contracts. Since Finland Post's incorporation, all Finnish domestic postal services became subject to VAT, which increased letter post rates by about 22 percent. As part of its reorganization, the Finnish postal service rationalized its work...
force, began to trim its post office network, and improved the cost efficiency of its sales network. It also implemented a mailbox delivery reform program that achieved considerable savings, and it is automating mail processing and concentrating it in large sorting centers. While these cutbacks were taking place, net sales increased by 6 percent over the previous year, and there was a return on sales (after financial items) of 7.6 percent. In addition to cost reduction, reorganization was focusing on a more flexible service company. According to Finland Post, being a limited company has made possible more rapid and more flexible decision-making processes and has improved customer-oriented operations.

The Netherlands: In 1993 the Dutch Post initiated the “Briefpost 2000” project, which aims to improve efficiency in sorting, reducing distribution costs, and strengthening the Post’s competitive position in the long term. The project involves a new structure for sorting centers as well as far-reaching automation of mail processes. The current star-shaped network of interchange centers is being replaced by a web-shaped network of six large sorting centers, thereby consolidating sorting considerably. Introduction of the latest automation equipment is aimed at making possible the automatic sorting of 98 percent of all letters. This project is expected to become operational in 1996-98 at a total cost of almost f. 1 billion and is expected to structurally reduce wage costs by a significant amount. The annual savings are expected to run to approximately f. 300 million. “Briefpost 2000” is also expected to facilitate quality control and create opportunities for developing new services.

PTT Post has also formed a joint venture with Postbank NV to provide post offices, and this has provided the basis for large-scale modernization of the post office network. A franchise formula has been developed for postal agencies and small post offices, and a “mini postal agency” concept has been introduced (this involves postal agencies that provide a small range of services to meet the everyday needs of customers).

Singapore: Singapore Post represents a successful financial and operational case (see Singapore case for details). However, although total postal volumes have been growing in Singapore, the growth rate of mail volumes has not kept pace with that of the economy, as measured by GDP growth, since 1989. Therefore the Post has taken the two-pronged approach of reducing its reliance on traditional mail and also attempting to curtail costs by increasing postal processing efficiency. Currently, the Post is reducing and reconfiguring the retail network. Full post offices are being replaced by smaller, retail-only outlets in business districts where the rents are high, but where business opportunities are greater. The delivery outlets for letter carriers are being relocated to less expensive real estate areas. Network
changes, however, have to conform to the obligations of the Post and be approved by the regulatory authority.

Since corporatization, Singapore Post has been consistently increasing the number of part-time employees, to more efficiently meet the service standards to which it is held. Increasing emphasis is being placed on the evening and night shifts to meet the new service standards. Sorting is consolidated in one location, and a large amount of investment is being directed into a new sorting center which will increase the automation of the sorting function on the basis of postal codes. Some five years previously, on the basis of cost and service criteria, the Post also contracted out the handling of airmail at the airport and the transportation and storage of mail at the seaport.

Czech Republic: The history of the Czech Post dates back to 1946 when the Czechoslovakian Department of Posts and Telecommunications was established. This structure remained relatively unchanged until 1989, when the department was transformed into a state enterprise, and 1993, when two separate state enterprises were established for the postal and telecommunications services. As part of the legacy of the communist system, which was dismantled in 1990, the Czech economy essentially lacks a commercial banking system. Therefore, the Czech Post is a major and critical force in the transfer of money throughout the economy. The Czech Post is a recovering postal system that has accomplished much since the communist system was abandoned and since its separation from telecommunications.

The postal network is excessively dense in relation to the geographic areas that it serves, as is manifest in the extensive "nodes" of the delivery, counter operations, and distribution networks (with almost 3,500 post offices, 18 regional hubs, and 67 district sorting centers to service an area of 300 by 160 miles). The proliferation of processing points dilutes any possible gains from automation or mechanization, multiplies the number of times mail is handled prior to delivery, and greatly increases overhead infrastructure expenses. Therefore, the Post sees its next steps as: undertaking the recovery and renovation of its extensive physical plant, streamlining its network of post offices, investing in automation, improving the cost effectiveness of delivery, and assuring a good quality of service levels. Future strategy also includes reducing manpower, while raising wage rates to competitive levels, through the automation of letter sorting down to delivery point sequencing and the conversion of some of the post office network to a contract or an agency basis. Delivery is also a major target for efficiency improvements, with emphasis on motorizing non-urban delivery.

The Philippines: The Philippine Postal Corporation (Philpost) has been undergoing reform in order to improve the postal sector, with the eventual aim of privatizing the postal service. Accordingly, in 1993 Philpost
was transformed from a government department into a government-owned corporation. Philpost’s agenda is currently focused on ensuring the rapid and safe delivery of postal services; therefore, its efforts are concentrated on its core processes, namely: receiving, collecting, handling, sorting, and delivery. Ancillary and complementary services are to be performed by its subsidiaries, by autonomous sub-units, and through alliances. With the assistance of another postal administration, Philpost is implementing a mechanization, computerization, and automation program. A comprehensive program for fleet upgrading is also under way to develop a highly motorized delivery network. In addition, concrete disciplinary steps have been taken to improve the security of mail.

Staffing and Human Resources

**New Zealand:** Since New Zealand Post’s corporatization (1987), the many reforms that have taken place have included the following measures affecting the board, management, and employees.

- **The Board:** The principal criterion for appointment to the board was a demonstrated competence in business in the private sector. Qualified, nonpolitical, professional business people were selected to import the commercial disciplines lacking in the public sector. In terms of autonomy, the board is responsible for appointing senior management, setting prices, approving capital expenditure, raising finance within limits of the authorized debt/equity ratio, and determining the policies and priorities for the Post. The board provides a strategic direction and purpose to the organization and monitors management performance. It is not involved in the routine management of the company.

- **Management:** Approximately half of the senior management team was appointed from outside the Post, to bring in the needed financial and marketing expertise. The heads of the Marketing, Finance, Human Resources, and Business Planning Departments came from the private sector. Management staff are contract employees and are paid on a performance basis. Management compensation is within a 20 percent margin above or below a base salary. The salary level and rate of progression are determined by the ability to achieve established objectives.

- **Employees:** All employees were removed from the public sector and are now contract employees. Their pay and employment conditions were aligned with private sector norms. Performance-based compensation schemes have been instituted, and tenure of appointment is not guaranteed. The Post, in negotiation with the union, is responsible for setting wages and conditions of employment directly.
The Human Resources Department emphasizes improving individual performance and accountability through training, development, and performance appraisal. The remuneration policy seeks to be competitive with the market, to reward individual contribution, and to provide career opportunities for those seeking advancement. Some of the Department's specific activities are:

- An occupational health and safety program
- Communications through team briefings, bulletin boards, and a monthly employee newsletter
- Various awards to recognize team efforts.

**The Philippines:** An ad hoc Merit System Committee was established within Philpost to draft a Human Resources Management System intended to instill professionalism and excellence at all levels of the corporation. This system governs the selection, hiring, appointment, transfer, promotion, and dismissal of personnel. In addition, Placement and Selection Boards for both central and regional offices assist the Postmaster General in these two activities. Consistent with the goal of mutually beneficial labor-management relations, the following programs have been initiated within Philpost:

- In 1993 the management and leaders of organized labor entered into a “Covenant for Industrial Peace and Corporate Growth” as an initial step toward giving employees a stake in corporate development.
- The Philippine Postal Institute Foundation, Inc. was established as an accredited, degree-granting institution to offer skills upgrading as well as values reorientation courses to both local and international postal workers.
- In order to improve employee working conditions and morale, postal facilities have been upgraded, stand-by power generation capacity has been provided, the primary health care service has been improved, water purifying fountains have been provided, and a day care center has been opened for pre-school children of employees.
- An Employee Welfare Division has been created to ensure the welfare and security of employees. Correspondingly, a provident fund was created, coverage of hospitalization benefits has been expanded, additional incentives have been provided to employees, and in-depth analyses of hazard pay and paternity pay provisions have been conducted and are under policy review by the Board of Philpost.
- Participative planning has been implemented with the establishment of Labor-Management Councils in all operating units.
Singapore: Since Singapore Post is a wholly owned subsidiary of Singapore Telecom, its Board of Directors is a subset of the Board of Telecom. Although neither board has a direct official relationship with the government, four of the seven members of the Post's Board currently hold government or government-related positions. The Chairman of the Singapore Telecom Board is also the Chairman of the Post Board. The President and Chief Executive Officer of Singapore Telecom also holds the same positions in the Post. As agents of the owner of the Post, the Board appoints the top position in the Post, as well as the Vice President and the upper layer of management.

Singapore Post has full autonomy in its staffing and makes an effort to consult and keep the labor union informed about changes in operations. The union itself owns and runs several businesses, in which every union member is a shareholder. This commercial orientation of the union has facilitated its relationship with the management of the Post. Employee wages are determined by the Post in negotiation with the union, although the government provides a general guideline for all companies. The Post has job descriptions for each job and uses the Hay points system for determining salary levels. Incentives have been instituted for employees whose output exceeds the expected norm, and overall compensations conform with private sector wages for equivalent work.

Marketing and Customer Orientation

Sweden: The Customer Satisfaction Index (CSI) is the most important measure of quality for Sweden Post. It is the survey mechanism utilized by Sweden Post to gauge what customers feel about the quality of service offered by Sweden Post. Attributes included in this index include reliability, speed of service at post offices, attitude and service mindedness, and handling of grievances and complaints.

Each business area measures the CSI. The overall index for Sweden Post in 1993 was 73, and the Post has set itself a goal of 77 to be achieved by 1997. The Post is seeking accreditation under ISO 9000 standards.

Other quality measures also monitored by Sweden Post include the quality of letter and parcel deliveries; waiting time at post offices; and quality of transaction and distribution in payment transmission.

Sweden Post also conducts annual surveys to measure personnel attitudes regarding their duties, management, and work environment. In 1993, 75 percent of the response was favorable, as opposed to a goal of 85 percent. The difference, and also a decline over the previous year, were attributed to the major rationalization measures under way and to uncertainty about the future.
Singapore: The Marketing and Sales Group was created in 1992 when Telecom and the Post were corporatized. Since then, Singapore Post has adopted a systematic approach to marketing and product development which has resulted in shorter product development and implementation schedules, partly because of the ease with which information is now communicated up the line through the Post's senior management.

The Post's current marketing strategy uses a three-pronged approach:

- Primary emphasis is placed on knowledge of the customer base and its needs and requirements
- Importance is given to the provision of a "one-stop shopping" service for the customer
- Strategic alliances are formed with the private sector where mutual benefits are possible.

In 1995, approximately 79 percent of the mail in Singapore was generated from businesses, 11 percent from the government, and 10 percent from individuals. The customer base is also broken down into "mail service" and "agency service" users. Accordingly, the sales strategy has two areas of concentration: (1) on corporate customers that have sales account managers to monitor and service them, in order to tailor the development of new products to their needs; (2) on the postal counters, where the public comes into contact with the Post. Counter employees receive specific training to make them customer-oriented.

Although Singapore Post has been measuring customer satisfaction annually for the last five years, there is no formal customer service group. Much customer care is product-specific and there is a customer care officer within each operational group. There is also a general inquiries line for the public.

Canada: In order to bring some structure into its sales strategy, Canada Post conducted a market segmentation analysis that grouped its customers into five categories and prioritized them according to their revenue contributions. The sales strategy was then revamped so that sales staff could spend more time penetrating the top priority accounts. Commercial centers were created to service lower priority customers.

The Post is also addressing its excessively broad product base (175 products and services including their options), with the objective of simplifying its product and pricing options. In addition, the Post has created a customer service functional unit which covers the spectrum of claims, general inquiries, provision of postal code information, community mailbox inquiries from customers, money order verifications, complaints, courier inquiries, telemarketing, general customer relations, service performance measurement, and
customer satisfaction measurement. Various performance indicators are monitored, such as number of incoming calls, type of calls, length of calls, dollar value of claims, turnaround time on complaints and claims, etc.

**Czech Republic:** In the Czech Post, marketing was established at the senior management level only in 1993. The marketing division consists of a market research unit, a promotion and public relations unit, and a product marketing section. The Post breaks its customers into two major groups—businesses and consumers—and the business group is further categorized by revenue levels. A new account management system accumulates information on business customers. An active market research effort is aimed at both the public and major business customers. The public survey (which covers satisfaction, utilization, expectations, knowledge/awareness of services, competition, and pricing) has resulted in actions to improve service and examine product features. Results of the business survey revealed that, in rating three features, reliability came first, then speed, and then price.

**The Philippines:** Together with the partial corporatization and restructuring steps undertaken by Philpost to improve the provision of postal services, a concerted effort was directed at improving the public perception of Philpost. These efforts included the following:

- Creation of a Public Complaints and Action Staff to receive and collect data and initiate action regarding complaints and suggestions from the public, and to establish “quick response desks” in all regional offices
- Use of the media to increase public awareness of the changing thrust of Philpost and of its plans to increase efficiency (daily radio information and a weekly television sitcom)
- Development of a customer satisfaction index (the goal is 100 percent service efficiency)
- Participation of the postal network in a nationwide campaign for presentable post offices and an impeccable corporate image
- Reorientation of employee values toward customer service through the Philippine Postal Institute Foundation, Inc.
- Continuous development of new products and services.

**Innovation in Products, Services, and Pricing**

**Singapore:** Singapore Post offers an array of 31 postal and agency services, the range and diversity of which are large (see Singapore Case for details). The current thrust of product diversification is based on use of the retail network for a variety of agency services.
Singapore Post has also introduced electronic and hybrid products. This concerted product diversification strategy has been adopted to prepare the Post for the loss of its monopoly in traditional postal services in the year 2007. Ever since corporatization in 1992, when the marketing and sales group came into being, the Post has been able to maintain much shorter product development and implementation schedules. As has been mentioned, this stems in part from the resultant ease with which information is now communicated up the line through senior management.

The pricing of non-monopoly products is more market driven than cost driven in Singapore. Although both direct and indirect costs of all products are systematically evaluated on an annual basis, a comparison with market rates allows the Post to determine its growth avenues. Prices are also reviewed annually for competitive products.

Sales representatives who are responsible for major clients are permitted to offer discounts or adjust the published rates for these large accounts. However, discounts offered must comply with guidelines issued by the Post and costs must be recovered. In areas where discounts are not permitted, added value is offered to targeted customers through the inclusion of additional services such as transportation, packaging, etc. To secure long-term agreements with customers, price incentives are also offered for advance mail preparation. Incentive pricing is generally offered in printed letters, promotional mail, and magazines. Approval for rate adjustments and discounts comes from the Marketing and Sales Group or, if necessary, from senior management within the Post.

Canada: Canada Post considers itself to be operating in the following three market areas:

- The communications market, where it competes with telecommunications and electronic communication mechanisms. Although all forms of communications have grown rapidly over time, since the volume of the Post's base product (letter mail) has increased only slightly, the Post's market share in communications has been steadily declining. In 1995 this market was estimated to be some Can$10 billion, of which CPC has about Can$2 billion.

- The distribution/shipping market, which involves transporting physical goods from point A to point B. This market is estimated to be worth Can$700-800 million, and is the most competitive because of the presence of 2,000 domestic and international courier and distribution companies. Canada Post estimates that it has about 5 percent of the short haul and local delivery markets and 18 to 19 percent of the long haul markets. Canada Post has the distinct advantage of being the only truly national distributor.
The advertising market, where the Post competes with the media (including broadcasting). This market is estimated to be worth Can$10 billion, of which the Post has Can$700 million.

In 1995, letter mail accounted for slightly more than 50 percent of Canada Post's revenue. Although this is a significant component, over the past 12 years the contribution of letter mail to revenue has been slowly but steadily declining. Approximately 80 percent of letter mail volume is due to business mail, and consumer letter mail has generally been declining in volume. The Post introduced "incentive mail," which is discounted mail offered to large volume mailers that have met various contractual obligations with respect to the preparation of mail. Incentive mail accounted for 31 percent of the letter mail revenue in 1995.

As was mentioned earlier, Canada Post is concentrating on reducing and simplifying its current product and pricing portfolio. In addition, in response to decreasing margins and changing markets, the Post is trying to position itself as the only company that can provide customers with coast-to-coast service that can meet all their shipping needs. To leverage the delivery component of its business, Canada Post is trying to become the lowest cost and best value provider.

Czech Republic: The Czech Post categorizes its offerings in the manner indicated in Table 4A.1.

Table 4A.1
Czech Post Product/Service Offerings

<table>
<thead>
<tr>
<th>Category</th>
<th>Product/Service</th>
</tr>
</thead>
<tbody>
<tr>
<td>Traditional</td>
<td>Letters, money orders, parcels</td>
</tr>
<tr>
<td>Electronic</td>
<td>POSTFAX</td>
</tr>
<tr>
<td>Agency Services</td>
<td>Savings/giro, pension payments, billing and bill collection, lottery sales</td>
</tr>
<tr>
<td>Commercial</td>
<td>Currency exchange, sale of paper products, customs declaration service, etc.</td>
</tr>
</tbody>
</table>

About 60 to 65 percent of the Czech Post's revenue is generated by traditional products and 25 to 35 percent by agency services. Although the Post believes letter mail—its monopoly product—has the potential for healthy growth, it expects strong competitive pressures in many other product lines. Therefore, substantial emphasis is being placed on developing non-traditional services and on improving traditional products. The Czech Post believes that its market will transform rapidly because of the changes in the way news is distributed.
and the development of the banking sector. Management foresees a
dwindling money order business, but is positioning the organization
to be a major player through partnership in the consumer banking
business. Automation of retail counters is aimed at assuring a place
in the financial transaction market. In addition, strong growth is ex-
pected in the direct mail and merchandise delivery segments.

*Finland:* Finland Post is focusing on the creation of value added ser-
vices, especially in its current freight and direct mail businesses. The
post now offers tailored, comprehensive communications, transpor-
tation, and delivery services (at least for its main customers) based
on modern information and materials management systems. The Post
has developed the Home Shopping Service, the Logistic Service, and
the Total Communications Sorting System, which are value added
services that combine, in an innovative way, all the core competen-
cies of the Post with technological communications devices (see
Chapter 5 for a full discussion of various technologies).
The Technological Revolution: Threat or Opportunity?

Within the postal service it has been acknowledged that, unless certain proactive managerial and technological changes are made, two fundamental forces characteristic of the ongoing era of competition will render the service obsolete. The first of these forces is the rapid development of increasingly sophisticated competition in all niches of the postal market, in conjunction with the trend toward relaxation of monopolies. The second factor, which is the focus of this chapter, is the technological revolution in electronic communications systems for text, data, and image transfers. This latter factor, which operates beyond the boundaries of postal monopolies, is regarded either with paranoia as representing the demise of the postal service, or is seen as an opportunity for the postal service to contribute substantially to communications infrastructure. Either way, it is recognized that adapting to this rapidly transforming technological environment is crucial to the long-term survival of the postal service all over the world.

The study's findings regarding the need for technological reform and the attitudes of postal services with regard to technology are given below.

- In the postal sector of many countries, there is no choice but to integrate technological reform in order to continue providing a low-cost universal mail service.
- Typically, postal administrations have been slow to embrace technological advances in the communications area, and the

---

1 This chapter focuses on the communications, or "carriage of mail," function of the postal service. It should be noted, however, that another fundamental function of the postal service is the distribution of goods, namely, parcels. While distribution does not face competition from technological alternatives, it is exposed to a barrage of direct competition from private courier and transportation services.
postal administrations of developing countries are more focused, in most cases quite wrongly, on expensive processing technology.

- In a number of cases the real bottleneck to technological advancement comes from the legislative framework or financial control regime imposed by the government rather than from poor management or lack of innovation.

- There is often, in addition, a degree of complacency arising from the belief that (1) the physical mail business is "immune to" technological advances, or (2) that a safety net will always exist for the mail business through government protection. Certain bureaucratic and monopolistic postal organizations have sought legislative protection from technological advances rather than accept the new opportunities to satisfy customers and revive the sector.

- There is overwhelming evidence that in post offices with a high degree of operating and financial autonomy (including autonomy for investment decisions) technological innovation and rapid technological adoption are high (see the Singapore and Sweden cases).

- It appears that, with developing countries in particular, the entry of postal administrations into hybrid mail products can overcome severe problems in mail distribution (truck ing) caused by poor transportation infrastructure.

- The gradual introduction of hybrid mail products and the take-off rate of these products have implications not only for the level of employment but also for the required skills mix of the postal service staff. Technological reform should pay particular attention to such labor issues as (1) the possible effects of the introduction of hybrid mail products and (2) how such effects could be handled to bring about the maximum staff buy-in.

To analyze the impact of the technological revolution on the postal sector, this chapter will first define the technological revolution. The chapter will then analyze its influence as both a threat and an opportunity for the postal service. Before concluding, the chapter will elaborate on the implications of the technological revolution for the postal sector and the strategic options that the postal service faces at this juncture.
Rapid technological change is increasingly favoring new electronic mechanisms for communicating the written word. Several methods exist for transmitting messages from one location to another without either physically sorting or transporting the original hard copy (see Annex 1 for a description of the most important technologies that affect the postal sector). Table 5.1 shows the characteristics of some of these electronic communications mechanisms. Any assessment of the true extent of competition from these technological communication mechanisms will vary depending on where the postal service is placed—within the spectrum of the narrower market of delivering only physical letters as opposed to the broader market of servicing communications needs. From the latter perspective, a wide range of competing technologies affects virtually every class of mail: transaction, person-to-person, and advertising.

As can be seen from Table 5.1, the various technological communication mechanisms affect different categories of mail because of their attributes. Thus, letter mail, especially business mail, competes directly with fax, E-mail, electronic data interchange (EDI) systems, electronic funds transfer (EFT), and telephone. The telephone and all media, both print and broadcasting, also compete with direct mail used for advertising purposes. While electronic messaging systems are often superior communication mechanisms because of their high speed, reliability, and security, their use is often restricted either because they are "systems-based" communication mechanisms or because their installation requires a large up-front investment. These features have, in particular, curtailed the use of sophisticated communication mechanisms in developing economies, which still predominantly rely on the postal service for their communication needs. In addition, letter mail has the advantages of universal access, hard copy is still the only legal form of documentation, and paper mail has not been supplanted in personal forms of communication such as cards.

---

2 The effectiveness of their use depends on the network of users linked to this particular communications device.
Table 5.1
Characteristics of Certain Electronic Communication Mechanisms

<table>
<thead>
<tr>
<th>Mechanism</th>
<th>Competes with</th>
<th>Cost</th>
<th>Equipment and Other Costs</th>
<th>Speed</th>
<th>Reliability</th>
<th>Other Features</th>
</tr>
</thead>
<tbody>
<tr>
<td>E-mail/Internet</td>
<td>- Letter mail (business and residential)</td>
<td>Low within network</td>
<td>PC terminal, modem, phone line, E-mail account</td>
<td>High</td>
<td>High</td>
<td>- Facilitates data exchange and management</td>
</tr>
<tr>
<td></td>
<td>- Carriage of publications, catalogues, etc.</td>
<td>Higher across networks</td>
<td>- Facsimile machine and phone line (not necessarily dedicated)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Express mail</td>
<td>Much lower than express mail</td>
<td>- PC with faxmodem, phone line</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Bulk mail</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Facilitates data exchange and management</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Document not legal</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Limited capacity of fax machine</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Document clarity lower than mail</td>
</tr>
</tbody>
</table>

Fax

<table>
<thead>
<tr>
<th>Mechanism</th>
<th>Competes with</th>
<th>Cost</th>
<th>Equipment and Other Costs</th>
<th>Speed</th>
<th>Reliability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fax</td>
<td>- Letter mail (business)</td>
<td>Cost of telephone calls (varies with scanning speed, size of document, area, time, day)</td>
<td>- Facsimile machine and phone line (not necessarily dedicated)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Express mail</td>
<td>Transmission can be delayed to economize</td>
<td>- PC with faxmodem, phone line</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Much lower than express mail</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

EDI

<table>
<thead>
<tr>
<th>Mechanism</th>
<th>Competes with</th>
<th>Cost</th>
<th>Equipment and Other Costs</th>
<th>Speed</th>
<th>Reliability</th>
</tr>
</thead>
<tbody>
<tr>
<td>EDI</td>
<td>- Letter mail (business and residential)</td>
<td>Low within network</td>
<td>PC terminal, modem, phone line, EDI software and subscription</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Express mail</td>
<td>Higher across networks</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Much lower than express mail</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

EFT

<table>
<thead>
<tr>
<th>Mechanism</th>
<th>Competes with</th>
<th>Cost</th>
<th>Equipment and Other Costs</th>
<th>Speed</th>
<th>Reliability</th>
</tr>
</thead>
<tbody>
<tr>
<td>EFT</td>
<td>- Letter mail (business and residential)</td>
<td>Often free for user</td>
<td>Telephone, account with both financial institutions, access to an ATM, etc.</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Express mail</td>
<td>Or flat fee, higher than letter mail</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Telephone

<table>
<thead>
<tr>
<th>Mechanism</th>
<th>Competes with</th>
<th>Cost</th>
<th>Equipment and Other Costs</th>
<th>Speed</th>
<th>Reliability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Telephone</td>
<td>- First class mail (business and residential)</td>
<td>Generally higher than letter mail</td>
<td>Telephone line/connection and instrument</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Express mail</td>
<td></td>
<td>High</td>
<td>High-medium</td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Bulk mail</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Radio/ Television

<table>
<thead>
<tr>
<th>Mechanism</th>
<th>Competes with</th>
<th>Cost</th>
<th>Equipment and Other Costs</th>
<th>Speed</th>
<th>Reliability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Radio/Television</td>
<td>- Unaddressed bulk mail</td>
<td>High cost for broadcasting time</td>
<td>Instrument</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>High</td>
<td>Medium</td>
<td></td>
</tr>
</tbody>
</table>

Interactive Television

<table>
<thead>
<tr>
<th>Interactive Television</th>
<th>Competes with</th>
<th>Cost</th>
<th>Equipment and Other Costs</th>
<th>Speed</th>
<th>Reliability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interactive Television</td>
<td>- Letter mail</td>
<td>Variable</td>
<td>Telephone line, terminal, modem, subscription</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Bulk mail</td>
<td></td>
<td>High</td>
<td>Selective</td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Transmission of publications, catalogues, etc.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Nevertheless, the diffusion of certain electronic communications mechanisms has been extremely rapid in the last decade (see Figure 5.1) and these rapid advances in telecommunications are virtually transforming the way that several sectors, especially in services, operate. For example, in the banking sector changes in telecommunications technology have fundamentally altered operations by facilitating and accelerating automation considerably. Developments that have altered the face of banking include: electronic funds transfer at the point of sale (EFTPOS) technology; credit card verification over a packet-switched network or through dial-up mode; automated teller machines (ATMs); the Society for World-wide Interbank Funds
Transfer (SWIFT) network; and the development of home banking through the telephone and computer. As a result of these technologies, the flow of paper mail that originates from banking transactions has been replaced to a considerable extent by electronic communication.

Figure 5.1
Worldwide Growth in Major Electronic Text Communication Devices

Severe disparities are evident across countries in terms of access to electronic communications; therefore, in most countries it may not be feasible currently to connect every household by electronic communication. However, such a possibility may not be too far in the future when the high-speed dissemination of information is augmented by a universal telecommunications network that enables users to communicate at any time and in any locality. In the interim, however, the use of many text communication services is limited by the global installed base of telephones. In the case of E-mail, growth is limited by the global population of personal computers, which in 1993 was about 100 million, or less than one-fifth of the global installed base of telephones. Increasingly, however, in both developed and developing economies, access to many text communication devices is being provided by both the public telecommunications operator and private intermediary services for a fee. And in a few countries, the postal administrations have begun to provide fax, E-mail, and other electronic communications mechanisms. Thus, access to electronic messaging systems is rapidly increasing.

Often, ease of communication increases the volume of communication, in which case the postal sector can maintain its optimism in spite of the growth of telecommunications traffic in all forms. And electronic transactions are often followed up or verified by hard copy
Redirecting Mail: Postal Sector Reform

notifications and receipts, thereby generating additional mail volume for the postal sector. It is argued that the development of such new office technology as word processors and copiers has actively resulted in an exponential increase in the ability to generate and send more mail. Today more and more reams of paper are feeding the fax machine, the high-speed copier, and the laser printer, which hardly suggests a paperless society in the future. Similarly, it is argued that technological innovation, coupled with broad changes in society, will lead to unforeseen and new uses of mail. In developed economies, for example, sophisticated data processing combined with vast telecommunications networks has led to an explosion of direct marketing and mail order business through the postal services.

Whether technological advances in communications are regarded as a threat or an opportunity, the needs of the postal service's clientele are bound to respond to these changes in technology. A demand for more flexible, lower-cost, speedy, and reliable services will undoubtedly increase. Thus, the postal service in most countries is at a crucial juncture, where the technological revolution is either under way or is rapidly unfolding and it is necessary to adapt to this phenomenon in order to survive and to prosper in the transforming environment.

Technology as a Threat

From this perspective, the growth of electronic communications mechanisms has severely reduced the domain of the postal sector in several countries, particularly in developed countries where access to substitutes is greater. The fear of the erosion of the postal sector by technological innovations is considerable. For example, a large European postal administration has estimated that the diversion of letter mail and express mail traffic to fax and electronic messages could cost it US$750 million annually by 1997. And Sweden Post, despite the deregulated postal sector, sees the telecommunications sector as its chief threat. An example from Finland of the threat to letter mail is given in Box 5.1.

Facsimile machines, electronic mail, EFT systems, EDI systems, store and forward systems, word processing systems, TWX/Telex systems, interactive cable television systems, and in-home computers are among the various telecommunications services/devices that allegedly pose a threat to the survival of the postal sector. In addition, traditional media and broadcasting services have always competed with certain types of mail. These telematic communications mechanisms that are outside of the postal monopoly are viewed by postal

3 Direct mail, advertising mail, and bulk mail.
services as powerful rivals and substitutes for the traditional letter posts that are affecting every class of mail. From this point of view, the future development of these electronic communication systems will be of such magnitude that they will become essential components of everyday life and will virtually crowd paper mail and the postal sector out of existence.

Box 5.1 Estimated Replacement of Letter Mail by Electronic Communications in Finland

Finland is a large country with a small population and is therefore heavily dependent on its communications infrastructure. Approximately 80 percent of the telecommunications network in Finland had been digitized by 1992, there were 54 telephone lines per 100 inhabitants (fifth highest rate in the world), and Finland was the sixth cheapest country for domestic calls and the second cheapest for international calls. Finland is also one of the pioneers in terms of fully opening the postal and telecommunications sectors to competition. This liberalization and the possession of a highly advanced and affordable telecommunications service creates a scenario favorable to the replacement of letter mail by electronic communications.

The study that was undertaken to estimate the mail volume that would be replaced in Finland by the year 2010 relative to 1993 focused on first-class and second-class domestic letter mail in 1993 and excluded bulk mail. The distribution of letters by content exceeded 100 percent as more than 30 percent of the letters could be recorded in more than one content category (e.g., bills accompanied by notices). The letter mail categories, their distribution, the electronic alternatives, and the estimated degree of replacement (of 1993 volumes) in percent by 2010 were as shown in the accompanying chart.

These results are naturally dependent on the specification of the models, the assumptions about the diffusion of technological communications alternatives, and the fact that no growth in overall communications has been accounted for. Nevertheless, these results would seem to indicate a replacement of approximately 43 percent of physical mail by electronic communications by the year 2010, which paints a bleak picture for the postal service. However, under an alternative scenario where GNP and, correspondingly, mail volumes, grow by 3 percent annually, it is estimated that mail volumes in the year 2010 will have declined by 5 percent relative to 1993 because of replacement by electronic means.

In conjunction with electronic mail and information retrieval systems, the use of electronic transaction systems is seen as part of the trend toward the "paperless" office and "checkless" society. In most developed economies, approximately 70 percent of letter mail (the postal service's core business) is made up of business transactions mail which includes items such as bills, notices, invoices, mortgage payments, and funds transfer payments. As far as postal administrations in most countries are concerned, direct competition from private mail delivery systems has not posed a significant threat to letter mail because of the postal sector's monopoly in letter mail. However, it is conjectured that the impact of telecommunications on transaction mail will be severe. This paranoia may be countered by the observation that mail volumes have consistently risen over the last decade, especially in economies in which electronic communication systems are most prevalent. Nevertheless (although reliable estimates are difficult to derive), it appears that to date growth in postal volumes has taken place because of the overall growth in the communications market.

Thus, if the postal sector is to protect its mail volumes, or even maintain its share of the communications market relative to its competitors, a fundamental rethinking of the entire role, strategy, and operations of the postal service is imperative.

Technology as an Opportunity

Given that changes are inevitable, albeit with a lag across countries, any reform and reorganization of the postal sector must adjust to this technological revolution in a proactive manner. Organizational restructuring is not enough. It is necessary to rethink the postal service's entire range of services as well as its core mission. It should be borne in mind that the restrictions that prevent the postal service from competing with the electronic communication mechanisms in price, quality, or service are bound to have severe repercussions.

In developing countries in particular, the postal sector has a much larger role to play in initiating and educating the public in the use of the new telecommunications services. For large segments of the population, lack of access to the equipment in question puts the onus on the postal service to improve the communication systems through its own initiative. The postal sector has unique access to the business and household sectors through its network of post offices and letter carriers. It should therefore be allowed to pursue opportunities to capitalize on this unique delivery service in partnership with existing electronic communications providers.

Certain postal administrations have responded to these forces of technological advances, more intense direct and indirect competition, and changing customer needs. In addition to providing tradi-
tional mail products, these postal administrations have begun to provide both hybrid and electronic services (see Box 5.2). Hybrid systems, with electronic and other inputs, can potentially provide much more rapid delivery of first class mail than can present mail, at a substantially lower cost than the present cost of first class mail, and with much higher levels of reliability. Thus, hybrid systems may prove to be one solution to the problems of service quality that typically plague postal operations.

**Box 5.2 Categories of Message Service Technology**

<table>
<thead>
<tr>
<th>Type</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Traditional</td>
<td>This refers to ordinary mail which is transmitted/delivered in hard copy (paper) form in all steps of postal operations.</td>
</tr>
<tr>
<td>Hybrid</td>
<td>This involves the electronic transmission of messages in combination with, at some point in the mail stream, the transmission of hard copy messages. Thus, hard copy is an input in the mail stream, which is to be distinguished from the creation of hard copy at the end of an electronic link. Hybrid systems typically accept electronic messages, produce presorted paper messages at a state or regional printing center, put them in envelopes, and then deliver them as part of the regular mail stream. Mail may also be physically inducted into the mail stream and then electronically delivered.</td>
</tr>
<tr>
<td>Electronic</td>
<td>In this case message transmission is purely electronic and may take place by wire, microwave, or satellite. Although hard copy may be generated at the end of the link, it is not transported in this form at any point.</td>
</tr>
</tbody>
</table>

Hybrid services can be vital in both transaction and person-to-person mail. Once high quality color printing on special paper becomes technologically feasible at low cost, the hybrid system will also be significant for the advertising market. For developing economies in particular, postal entry into hybrid products can provide a solution to severe problems in mail distribution (primarily trunking) that stem from poor transportation infrastructure (badly maintained roadways, vehicles, or rail and air transportation). Thus, with the development of hybrid products, postal reform could be undertaken independent of improvements in a country's transportation infrastructure.

The postal sector brings valuable assets to the hybrid message service. Through its universal distribution network, the postal service can make hybrid electronic services available to a much wider range of consumers than private or public telecommunications firms can efficiently reach. If the postal sector is prevented from entering the hybrid markets, it loses a challenging opportunity. Such a situation also sets the postal sector against electronic message service firms when the two should be cooperating as service suppliers, and may, in addition, deprive potential electronic message service users of access. The universal access and delivery capability of the mail sys-
term should therefore be combined with the beneficial features of other communication technologies so that a fast, reliable, inexpensive messaging system, universally available to all users, can be developed. In addition, incorporation of these technological advances can benefit the postal service by providing it with a base for developing a full range of higher value-added services.

The experiences of Sweden and Canada are noteworthy in terms of integrating electronic communication technology with the mail distribution network.

Sweden Post is committed to making use of all available media so that messages or mail may be transmitted by the method chosen by the sender. This method may be by mail, mainframe computer, personal computer, or telefax, or over the counter at the post office. The aim is to maximize quality, reliability, and universal access for the Post's service. For this purpose, the Post considers it necessary to be dynamic and actively attuned to change. In 1993 a new subsidiary of Sweden Post, PostNet, was formed through the merger of BASCET Infolink AB and Scandinavian Information Link AB. PostNet now markets computerized systems for inter-business communications as well as other products. This has enabled Sweden Post to provide the following hybrid and electronic messaging services:

- **E-post letters:** Information is "posted" directly from a computer and distributed in the form of letters.
- **E-post PC:** As above, but electronic input is from a personal computer.
- **E-mail:** This is the purely electronic transmission of PC to PC messages.
- **eDI:** This is an EDI system for sending electronic business documents between computers.
- **eDIREKT:** This is Sweden Post's electronic marketplace, where it is possible to obtain a wide spectrum of information and/or to order goods and services in databases via a PC or a terminal. This has replaced the discontinued Videotex system.
- **E-FAX:** This consists of various forms of value-enhancing fax services (e.g., Fax-broadcast, which distributes faxes to a large number of receivers).

This focus on electronic messaging services in conjunction with Sweden Post's traditional services has allowed the Post to offer a wide-ranging and up-to-date selection of messaging services. It has also enabled it to face the onslaught of technological competition and operate in a completely deregulated market as well (see Sweden Post case). However, Sweden Post is an unusual case because of the high level of autonomy that the postal administration enjoys in all aspects of its operations, financing, investments, and prices. Thus, Sweden Post has the capacity to take initiative and the ability to compete with others on equal terms.
Canada Post, in order to capitalize on its unique distribution and delivery advantage (i.e., its access to nearly 12 million businesses and home addresses across Canada) and on the opportunities opened up by new technologies, aims to continually innovate communications solutions that will enable it to deliver a customer's message physically, by fax, or electronically regardless of the originating medium. The following are a few examples of the hybrid and electronic products it currently offers.

**OmniPost:** This is a software application provided by Canada Post that transforms a PC into a personal mailbox and provides access to the Post’s coast-to-coast communications network. OmniPost allows customers to choose their format (electronic-to-electronic or electronic-to-paper). The customer composes the text, addresses the mail, and specifies one of three methods of forwarding:

- **Lasermail:** This is electronically sent to the Canada Post print facility nearest the recipient, where it is printed, enveloped with postage, and deposited for next day delivery in most major urban centers.

- **E-mail:** This can be forwarded to any other subscriber on the OmniPost network.

- **Faxmail:** This can be faxed to individuals with a fax machine or fax modem.

**Admail Plus:** This service is targeted to companies that routinely distribute large volumes of advertising material, solicitations, notices, newsletters, etc. Clients provide the contents of the mailing, plus the mailing disk on computer tape or disk. Canada Post produces the mailing pieces and provides a proof. Once the proof is approved, the information is electronically transmitted to local production sites across Canada where materials are printed, folded, inserted into envelopes, and sealed for local mail delivery by Canada Post. Clients can customize the mailing by supplying company stationery, having the Post prepare customized stock, or selecting print material from the stock. Admail Plus can produce inserts or reply envelopes for mailing.

**Lettermail Plus:** This service is for businesses with high volume, personalized mailings of invoices, statements, time-sensitive notices, and other financial correspondence. The mailing pieces are printed and inserted at regional production facilities and are delivered to customers in the region. This ensures a more rapid and cost-effective delivery of financial correspondence.

**Remote Desktop Publishing:** This is an “in-shop” printing facility of Canada Post. The client provides an electronic copy of a newspaper and the address list. The Post handles production and distribution with the aim of maximizing delivery speed.

**Address Accuracy:** Large and medium-size businesses with large
mailings can submit their mailing lists in any computer format to Canada Post and will receive (1) a valid address list that conforms to the Canadian Addressing Standard; (2) an invalid address list; and (3) a report giving reasons for the invalid addresses. This process is based on barcoding undeliverable mail and then electronically transmitting the information to subscribers.

**Certified Plus:** This service provides the date of delivery and the recipient's signature automatically to the sender and includes a sequentially numbered Acknowledgment of Receipt (AR) label on the envelope. A barcode provides an electronic link between the letter and the AR label. The AR is returned to the sender or, alternatively, is processed by Canada Post which provides the client with an electronic file of ARs.

**Registered Plus:** A proof of mailing manifest is produced in hard copy and electronic format by Canada Post. The tracing service can provide a copy of the proof of mailing manifest up to two years after delivery. Two 1-800 telephone numbers are provided to confirm the date of delivery.

Thus, it can be seen that the current developments in telecommunications represent a tremendous opportunity for the postal sector to capture a significant share of the growing communications market. In this context, the postal sector needs to develop systematic processes for generating, developing, evaluating, and introducing new products. These products should capitalize on the postal sector's core competencies in following nationwide networks:

- The collection network
- The retail network
- The transportation fleet
- The delivery system (national and international)
- The labor pool.

To bring in the needed expertise in electronic inputs to the products, the Post should be given the freedom to form strategic alliances with other entities. In addition, a comprehensive market and competitive analysis should play a significant role in new product development so that the postal service can reap the benefits of the technological revolution. Detailed information on mail flows and detailed analyses of these flows (by sender, recipient, purpose, needs) are necessary to enable the postal service to assess the potential impact of competitive threats and to prepare for them (see Chapter 4 for details of these commercialization aspects). The lessons offered by other national postal systems that are further along the learning curve can also prove useful, although any new system will need to be tailored to domestic requirements and capacities.
5. The Technological Revolution: Threat or Opportunity?

Under the present scenario, the consequences of restricting the flexibility of the postal sector in the provision of these new services will be severe. An excessive diversion of volume to electronic message service markets (see Box 5.3) will result, and there will be corresponding inefficiencies and increases in unit costs in the postal sector. The current situation of most postal administrations will worsen. In these circumstances, the postal service will be motivated to introduce new products only if it is given the commercial and financial autonomy, and the incentives, to do so.

Box 5.3 Bureaufax and Electronic Message Handling in the Postal World

The bureaufax service is fairly well established in the postal world and the number of participating postal administrations continues to increase. Although the volume of traffic and revenues generated by this service is relatively limited in most postal administrations, the profitability of the service is considered satisfactory because of the low investment required for introduction. Not only postal administrations, but also a number of telecommunications administrations and private operators operate a bureaufax service. A survey conducted by UPU in 1994 indicated that approximately 92 postal administrations had introduced this service as of 1993.

The number of postal administrations that provided electronic message handling was fairly low. Only 13 administrations (9 in industrialized countries and 4 in developing countries) reported their number of electronic messages (200 million messages in 1993). Nine postal administrations offered text-based services for bulk hybrid mail; 8 administrations offered text-based services for individual messages; and only 3 offered an end-to-end electronic mail service. However, 21 postal administrations intended to introduce electronic message handling services in 1994 or 1995.


To provide the new services discussed above, the postal sector must emerge from its normally sheltered atmosphere so that its viability, survival, and growth are subject to the market forces of competition. This most certainly requires today's postal services to undergo a fundamental transformation.

In summary, postal administrations the world over are confronted with the following challenges:

- The rapid growth in electronic communications (electronic text, data and image transfer mechanisms)
- A new generation of users/clientele
- Competition from sophisticated physical competitors
- The relaxation of monopolies

Options Open to the Postal Service
The Two Strategies

In view of the above challenges, two core strategies emerge that postal administrations can adopt at this juncture: one strategy is passive and the other is proactive (see Table 5.2). These two options are discussed immediately below.

Table 5.2
Available Options for the Postal Sector in Hybrid Messaging

<table>
<thead>
<tr>
<th>Service Component</th>
<th>Passive</th>
<th>Proactive</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electronic Input</td>
<td>Status Quo</td>
<td>Minimal</td>
</tr>
<tr>
<td></td>
<td>None</td>
<td>Private</td>
</tr>
<tr>
<td></td>
<td>Private</td>
<td>Private/Subcontracted by PO</td>
</tr>
<tr>
<td></td>
<td>Intermediate</td>
<td>Exclusive</td>
</tr>
<tr>
<td>Printing &amp; Sorting</td>
<td>PO</td>
<td>Either</td>
</tr>
<tr>
<td></td>
<td>Either</td>
<td>Either</td>
</tr>
<tr>
<td>Physical Delivery</td>
<td>PO</td>
<td>PO</td>
</tr>
<tr>
<td></td>
<td>PO</td>
<td>PO</td>
</tr>
</tbody>
</table>

1 Service component performed by private sector, public or private postal operator (PO), or either one.

Postal services can choose to remain unchanged and to continue to engage in the provision of purely traditional services (passive option). Indeed, in several countries in which the postal service's mission is narrowly interpreted as the carriage of mail, postal administrations have been forced to adopt this strategy (see the Chilean Post case study). The danger of adopting this strategy is that the postal service will be confined to a shrinking role and will be less able to meet the needs of its clientele. Decreasing mail volumes will further increase unit operating costs, which will exacerbate the problems of financial deficits faced by most postal administrations and will entrap the postal service in a cycle of perpetual subsidies and/or decreasing quality of service. In addition, as was mentioned earlier, a large section of the population may be deprived of access to certain electronic communication mechanisms that only the postal service could provide. Choosing this strategy would involve confronting another crucial issue: namely, will physical mail shrink too far and too rapidly to support national networks in the future?

In the second option the postal service could choose to capitalize on the opportunities provided by the various technological advances (proactive option). By providing an entire range of traditional, hybrid, and electronic services, the postal sector could not only revive itself and face the onslaught of competition, but it could also contribute substantially to the communications infrastructure of the country. However, this strategy would necessitate a complete restructuring of the postal operations and the parameters within which most postal administrations currently operate. The postal sector would need to be removed from government protection and provided with both the incentives and the autonomy to behave commercially and to operate on equal terms with its competitors (see Chapters 3 and 4). Several
5. The Technological Revolution: Threat or Opportunity?

Postal administrations that have reformed have already taken this proactive route.

Hybrid Messaging Systems

Hybrid messaging systems must rely on either the postal service or its potential competitors for the hard copy elements of the service, or they must receive these elements from integrated suppliers that provide both electronic and hard copy message services and link them up. Therefore, a rigid extension of the monopoly that currently applies to the transmission of hard copy in most postal administrations would expand the postal sector's monopoly to one of the crucial inputs in hybrid services. Private companies in the telecommunications sector are both for and against the encroachment of the postal service on their domain. On the one hand, the postal sector could be of substantial help in diffusing several telecommunications services by educating the general public and by investing in equipment to connect homes as well as businesses via the postal delivery system. On the other hand, the private sector would prefer to maintain its hold over the electronic communications business. Competitors of the postal service are especially concerned about the following two issues:

1. The national postal service will try to extend the reach of the letter mail monopoly to cover electronic communications or hybrid products, thereby excluding the private sector.

2. The national postal service will attempt to use its letter mail monopoly to cross-subsidize the hybrid products it offers, thereby "outcompeting" the private sector via predatory pricing.

Accordingly, a crucial issue is the specification of the entry and price regulations and the combinations thereof that would lead to the best intertemporal performance of the combined communications markets. A significant policy issue revolves around whether the postal service should provide the electronic communications portion of the service itself, and, if so, under what conditions it should do so. Typically the telecommunications industry, like the private courier industry, tends to favor exclusion of the postal service from electronic messaging services on the grounds that a government-subsidized multi-product firm that monopolizes some markets might engage in predatory behavior. The compromise that is emerging is that the postal service should be authorized to enter electronic telecommunications without its letter mail monopoly and with restraints that are intended to ensure that its presence does not lead to anticompetitive effects in the relevant telecommunications submarkets. In the case of Sweden Post, for example, this dilemma has been resolved because the entire postal sector is completely deregulated, and access prices to the Post's delivery system are explicitly specified.
If postal services are permitted to retain their letter mail monopoly and proceed with the provision of hybrid services, their development and competitiveness in these markets will nevertheless be hampered unless the hard copy services that form part of the mix are priced correctly, both internally (within the postal service) and externally (for clients or customers). Such a pricing arrangement would require a set of changes in the structure and regulatory environment of the postal system that would result in the unbundling of postal services. Not only should pricing be unbundled and transparent between the delivery service (the monopoly aspect of the service) and the electronic value-added activities (which are competitive), but prices should be based on a cost rationale that reflects the differentiating features of delivery (such as coverage, speed, and place of insertion in the mail stream) and should not consist of the application of a flat rate. This would require sophisticated estimates of the postal service's cost functions and could also involve the application of multi-product pricing principles to the services the postal sector has to offer (see Chapter 2). Pricing plays an important role in determining the relative rates of development of various kinds of message services—electronic, hybrid, or traditional. Proper pricing is essential to ensure that the pie is as large as possible, so that the greatest benefits are available to the society.

Even in the provision of hybrid messaging services, the postal service has the choice of adopting four strategic options: (1) a minimal role; (2) an intermediate role; (3) an expansionist role; or (4) an exclusive role (see Table 5.2). The postal sector's activities in each of these four scenarios are outlined below.

**Minimal Role:** The postal sector cooperates with the private sector in the provision of hybrid services that use the existing postal delivery network, but does not engage in the complete provision of any of the services themselves. Thus, the role of the postal sector is confined to the provision of regional printing and sorting (possibly) and physical delivery. The drawback to this option is that the postal sector may not choose to pass on all the savings that it realizes to either the user or the sender.

**Intermediate Role:** In addition to carrying out the above minimal role, the postal sector is engaged in providing complete hybrid services that make use of the existing postal delivery network by subcontracting with private firms that offer the relevant telecommunications input. The postal service would develop, operate, market, and deliver the complete service to the public and would also accept electronic messages from other firms that meet certain standards. Thus, the postal service and private firms would offer competing hybrid services, although only the postal sector would provide complete physical delivery. The pricing of delivery takes on considerable significance under this option. By excluding the postal
service from the electronic portion of the service, this option creates incentives for the postal service to cooperate with the industry and to do so on a nondiscriminatory basis.

**Expansionist Role:** The postal sector uses the existing postal delivery network as a base from which to transform the postal service into a modern information processing company. Thus, the postal sector is in direct competition with telecommunications sector firms in the provision of the electronic input (as in Sweden, for example). This arrangement would require the acquisition of substantial new technical and management capability by postal administrations. In addition, the postal service might have to re-evaluate its entire investment in automation, which is typically directed at processing hard copy mail. More attention would need to be directed at investment in information technology, which represents the products of the future.

**Exclusive Role:** The postal service offers the complete service (electronic component, regional printing, physical delivery) on an exclusive basis, and there is no provision for accepting messages in electronic form from the private sector. Private firms can insert messages in the mainstream only in physical form. A likely consequence of this option might be the development of a large subsidized electronic mail service with a monopoly, which might discourage the development of new services and incentives to cut costs. Therefore, the logic of adopting this option is questionable.

Any choice among future growth strategies would require a complete evaluation of the core competence of the postal service and a carefully thought out decision as to what features it should capitalize on in the light of future opportunities and changes. Most postal services possess an unparalleled distribution and retail network, which provides them with a major opportunity to substantially expand the range of services offered at the postal retail outlets. In terms of the technological onslaught, however, the core competence of the postal sector lies in its delivery network. The postal service has unique access to the household sector through its network of post offices and letter carriers. The service should therefore pursue opportunities to exploit its delivery service in combination with existing electronic communications. The postal service should have the choice of pooling its talents with those of other organizations that possess complementary expertise and resources. This would be done through strategic alliances.

Today competition affects every class of mail in the postal sector, either directly or indirectly. The telephone has done much to undercut the monopoly of the postal service, and now the telecommunications revolution threatens to completely replace several paper-based transactions. To successfully cope with this situation, as well as with
the changing needs of customers, postal sectors throughout the world will have to overcome the following two fundamental obstacles:

1. The internal lack of a market orientation (pricing, new products, planning, marketing)

2. The extant political and regulatory constraints that prohibit innovation and/or market access.
5. The Technological Revolution: Threat or Opportunity?

Annex 1: Description of Competing Technologies

Telex and Telegraph

One of the oldest mediums of electronic communication is the telex, which originated in the early 1930s and whose usage continued to grow until 1987 (see Figure 5.1 in the main part of the chapter), when the worldwide total of telex subscribers peaked at 1.6 million. Since then its use has been declining because of technical limitations relative to newer text communication mechanisms. Nevertheless, the telex and telegraph continue to be the main text communication services used by developing countries in communicating with each other. This is especially true of countries in which the public switched telephone network (PSTN) is too poor in quality to support fax traffic. However, with the progressive replacement of the telex by other text communication devices, the installed base of telex machines has declined substantially since the mid-1980s in the developed world, which indicates that these services cannot be sustained in the long term. In terms of competing with the postal service, these electronic messaging systems were used mainly for urgent written communications in the era preceding express mail and courier services.

Videotex

Videotex is a low speed and limited interactivity screen-based service used mainly for information retrieval. Although more than 50 countries have installed this technology, videotex is a predominantly European technology that enjoyed maximum success in France (Télétel) and Britain (Prestel). In 1993, France accounted for three-quarters of the global installed base of 8.4 million videotex terminals. Accordingly, although worldwide diffusion of videotex has been steady, it has also been much slower in relation to the growth of other electronic messaging systems (see Figure 5.1).

This communications device was used predominantly for the distribution of information, such as for telephone directories, and it competed mainly with the distribution of publications, etc., through the postal service. Recently videotex was seen in a range of new services such as home banking and electronic messaging (which also competes with letter mail). However, a major handicap to videotex use has been the need for dedicated videotex terminals—which have traditionally been distributed free of charge. There is now consider-

able uncertainty as to whether the videotex system will ever repay the large investment necessary to sustain this policy of distributing terminals free. However, with the rapid convergence of telecommunications, computer, and broadcasting terminals, the need for dedicated videotex terminals may disappear; this would eliminate a considerable obstacle to the diffusion of this technology.

**Facsimile Machines (Fax)**

The rapid growth of the fax machine has been one of the prime communications technology successes of the 1980s (see Figure 5.1). The development of the fax machine is linked to advances in semiconductor chips, data compression, and thermal printing technology. Although a fax is not legally an original document, the speed of its transmission gives it a substantial advantage over mail. In developing countries a constraint on the use of faxes is the poor quality of telephone lines. Nevertheless, the spread of facsimile use has fewer constraints than other network-based communications services which are dependent on the PTO network or standardization. This is because the fax is primarily a terminal-based service as opposed to a network-based service. In addition, the facsimile does not require major investment in new infrastructure and is not restricted to countries in which the switching systems are fully digital. Users are therefore able to choose, install, and apply the technology without assistance from PTOs.

The transmission of facsimile messages can be mixed (involving hard copy and electronic transmission) or purely electronic, depending on the equipment on which the fax is being received and stored. The translation of coded fax signals into the kinds of electronic signals that computers are capable of processing and storing facilitates effective management of information via the fax. Thus the computer interface facilitated by the fax is a function that goes beyond the mere transmission of written messages. Additional features that enhance the utility of fax machines are that these machines can use regular paper, they permit the use of color, and they can store messages to be transmitted at a later point, thereby economizing on telephone costs and reaching people conveniently in other time zones.

Compared to the mail, faxing may not prove cost-effective for all users. Users who send documents infrequently, or for whom the time factor is not urgent, will still find it cheaper to mail documents. Investing in a commercial fax machine and a dedicated phone line is worthwhile for businesses that communicate frequently, even with the equipment costs and other costs that accompany faxes. Depending on the type of machine, the time required to feed the fax machine can

---

2 This section draws on: Richard B. McKenzie, "Communications, Just the Fax Ma'am!" *American Enterprise*, March/April, 1993.
be significant. However, the mushrooming of intermediaries that provide fax services for a fee is removing obstacles to accessing this communication device.

The majority of fax machines in use are commercial machines. In the past, the expense of investing in a fax machine may have kept consumers from joining the "fax revolution." However, with the advent of personal computers and answering machines that have built-in fax machines at a nominal cost, and because a telephone line does not have to be dedicated to the fax machine any longer, the expenses associated with fax use are dropping sharply. Faxing is likely to become cheaper as long as machine prices and long-distance telephone rates continue to fall. Thus, fax use is spreading from businesses and institutions to the household level fairly rapidly and is thus affecting every class of letter mail. The fax has been rapidly adopted by many developing economies, particularly those that are export-oriented or that have a large tourism industry.

**E-mail/Internet Services**

This major computer-to-computer electronic messaging technology has flourished in the late 1980s and the 1990s (see Figure 5.1). E-mail is superior to other electronic messaging services because it preserves most of the features of the original text and permits file transfer and re-editing. E-mail users can conveniently and economically communicate with users within the same network. It is also possible to translate messages across networks at additional costs. Some hosts are connected on-line with commercial data sources that are accessible through E-mail. Thus, like faxing through a computer, this form of communication not only bypasses the mailing of hard copy, but also facilitates information management. Moreover, it is increasingly possible to conveniently interconnect across international systems.

In some countries private telecommunications companies provide electronic mail to individual subscribers. Some countries also have ongoing coordinated efforts among businesses, governments, and universities to transfer information from one computer to another, which permits access to a wealth of information. In 1994, 59 countries had direct E-mail connectivity through internet hosts, and an additional 68 countries had indirect connectivity through other networks. The internet operates predominantly over leased lines rather than over PSTNs and is therefore capable of providing better quality transmission links than those of other text communication services.

Within a single network, E-mail communication is much cheaper than faxing, although different addresses and interconnections among networks can cause significant cost differentials. Direct electronic mailing between personal computers is far more rapid than faxing and holds the promise of supplanting faxes in the future. Both E-mail
and the fax are usually less expensive than telex and are far cheaper than express mail. However, express mail has the advantage of carrying originals and can be cheaper than a fax or telex if a large document is involved. But express mail is slower than both the fax and E-mail and can seldom match the cost of E-mail within a single network. Because the internet does not have volume-based tariffs, and because it bypasses the problem of high rates for international calls by using flat-rate pricing, it is ideally suited to developing countries. However, because E-mail use requires (1) rudimentary computer literacy, (2) an up-front investment in computer equipment, and (3) for most users, the additional costs of linking up to the internet, a widespread diversion of letter mail to electronic mail has not taken place.

Electronic Transaction Systems

Electronic transaction systems are used for communication in cases where speed, accuracy, and authentication of amounts and identities take on paramount importance. Many transaction systems are financially oriented, and their formats are standardized and messages are brief. Hard copy or paper transaction systems are much slower than these electronic systems. In addition, these systems can confirm transactions instantaneously as the transaction is conducted. The two major electronic transaction systems are (1) funds transfer; and (2) electronic data interchange.

Electronic Funds Transfer (EFT): Mail from residential customers to businesses is threatened by EFT, which makes possible payment of bills or electronic transfer of funds among financial institutions without the posting of a check. This is made feasible by the use of automated bank transfers. Employers are also encouraging the direct deposit of payroll checks into bank accounts. In addition, several banks, savings and loans, and other financial institutions are offering a "pay by phone" bill-paying service, facilitated by the use of credit cards. The use of Automated Teller Machines and credit cards also substantially decreases the need for financial correspondence by mail. Thus, EFT represents a potential threat to the absolute volume of business mail in countries in which the postal service is heavily utilized for financial correspondence. However, it is ironic that, because of lack of speed, security, and reliability, the postal service in many developing countries is rarely used for financial correspondence and is, therefore, currently immune to the threat posed by EFT.

Electronic Data Interchange (EDI): EDI is a computer-based billing and accounting system used for sending standardized format electronic business documents. Since data transmission is between computers, the system also facilitates effective data exchange, storage, and management. EDI is used mainly for purchase orders, bills, receipts, notifications of financial transactions, and responses that in-
clude payment checks. Thus, the use of EDI also has the potential to divert a significant amount of business correspondence away from the postal sector. However, because EDI is a network-based service and its use requires a PC terminal, a modem, a telephone line, the EDI software, and a subscription, its use to date has been confined predominantly to developed countries.

**Broadband Communication**

The development of broadband communication will transform most technologies into multimedia networks capable of carrying video and other image-based services, high speed data communications and other computer-to-computer traffic, and voice and text communications. Growth in broadband communication is dependent on the advancement of data compression technology (or large-scale recabling with fiber) or the diffusion of software-defined intelligent switching standards, such as Asynchronous Transfer Mode (ATM).

The development of broadband communication is part of a more general trend toward the convergence within the information industry of its three formerly separate sectors: telecommunications, computing, and broadcasting. A technical convergence is occurring in the way information is communicated. When all three sectors are able to receive and transmit information digitally, there will truly be a single information industry. A functional convergence in the use of services is also taking place. In addition to interpersonal communication, telecommunications networks are being used for entertainment, advertising, videoconferencing, information retrieval, education, banking services, home shopping, etc. It is not difficult to imagine the potential for substantial replacement of each and every class of mail by the development of such systems.

**Media and Broadcasting**

Bulk mail or advertising mail in the postal sector also faces direct competition from the print and electronic media that carry advertisements to potential customers (telephone canvassing, print media, and broadcasting). On the other hand, while the print and electronic forms of advertising have grown rapidly, so has the volume of direct mail in developed countries. In comparison with media and broadcasting services, however, advertising through direct mail has the potential to target specific audiences. The advancement of information technology in formulating updated and current mailing lists of various consumer attributes has also benefited the postal service in this niche. However, in addition to indirect competition from the media and broadcasting in direct mail, postal administrations frequently face direct competition in this arena from alternative mail delivery services, especially when the postal monopoly does not encompass bulk mail.
Introduction to the Case Studies

This study has reviewed and analyzed in detail the reform experience of six countries: Australia, Canada, Chile, Singapore, Sweden, and the United Kingdom. The postal services of all these countries have gone through varying degrees of reform and are at various stages of their reform process. One point that must be stressed at the outset is that all of the six postal services consider that their reform program has not yet been completed. Some of these countries, such as Canada and the United Kingdom, embarked on their reform program many years ago and are still grappling with some serious issues.

The case studies are not intended to give the reader a view on how to reform. Instead, the purpose of this part of the report is to summarize the experience of six major reforms in the world's postal sector, and to bring to the fore some major issues and lessons regarding the specific case studies. Each case study offers different lessons, poses different issues with regard to reform, and, more important, explains the approaches that postal services have taken to improve performance even when they have been faced with widely differing legal, institutional, and regulatory environments and policy bottlenecks.

This part of the postal reform study begins with the case of Singapore Post, which is a good example of how a postal service, together with the government as the owner and the regulator, has developed a policy framework that is symbiotic and fosters continuous performance improvement. Singapore Post could not be called a typical postal service. In the first place, it services an island-country with its own special demographics; thus, the Post's delivery economics are quite different from those of most postal services. Second, Singapore Post is integrated with Singapore Telecom in its corporate structure, although the Post operates independent of the Telecom.

However, the case of Singapore Post provides interesting lessons for reformers. Of particular note is the relationship among the operator, the regulator, and the government. How these three parties have uniformly helped the development of the postal sector in their homogeneous approach to objectives and policies is explained in the case study. This relationship has been one of the primary enablers of performance improvement. Singapore Post has achieved ongoing performance improvements through enhanced commercialization programs and has also been focusing recently on technological reform. The postal service recognized early on the importance of technological integration in the mail market and is equipping itself to become a major player in the communications industry for the future paperless society. Singapore has not completed its reform journey. Some issues relating to regulation, competition, and institutional arrangements may be revisited in 2007 when the Post's exclusive license to operate letters and postcards expires.

The case of Correos de Chile, on the other hand, is a contrast to the case of Singapore Post. Correos de Chile is an example of how a postal enterprise is managing to improve performance despite an unclear legislative and regulatory regime. The Chilean postal service organization has focused on enterprise reform and has been able to improve its revenue and
productivity, having invested heavily in the system and having provided its employees with more training. However, the extent of Correos de Chile's reform can only proceed up to a point: the country must now implement a suitable enabling environment. In this regard, one of the first challenges will be to develop a sound postal legislative and regulatory framework. As in Singapore, in Chile the government, the operator, and the regulator should work together toward sector development.

Sweden Post is a bold example of reform, particularly from the viewpoint of regulatory reform. It is one of the very few countries, and the second in the world, to completely remove the postal monopoly. Although this might appear unpalatable for many developing countries, the process that Sweden went through in addressing issues of regulation and competition is relevant to all governments considering reform. For example, Sweden is one of the few countries in the world to have undertaken a systematic analysis to isolate the cost of providing postal service to remote areas and of providing the other public service obligations that are mandated by the government. The results of this analysis formed the basis for the government and the operator to decide on regulatory policy for the postal sector. Sweden is also a pioneering example of technological reform. Its adoption of hybrid mail is one of the highest in the world and is growing rapidly.

Australia Post has just completed the third phase in its reform. Through its phased approach, the Post has ensured its ability to fulfill its social obligations while focusing on improving commercial performance. Australia Post, unlike Sweden Post, has taken a cautious approach with regard to regulatory reform. Although Australia recognizes the importance of competition to increase market-driven, commercial discipline in the postal service, because of the country's demographic structure, the government has introduced regulatory reform slowly. In the third phase of the reform, Australia Post has introduced a limited form of interconnection, thereby increasing competition in the upstream functions of the postal service. The corporatization success of Australia Post is a good example for countries that are inclined toward a phased approach to reform.

The case of the British Post Office highlights the need to free the postal service of unnecessary regulatory and institutional constraints to ease the way for further development in the postal service. The British Post Office has achieved a great deal through its early enterprise reform. It is one of the leading postal administrations in terms of service performance. Nevertheless, for the Post Office to respond effectively to changing market needs and industry dynamics, controls placed by the government need to be eliminated. This is one of the problems that postal services face today — as the commercial segment of the postal business becomes overwhelmingly dominant, the usefulness of government ownership and control is questionable.

The last case, Canada Post, is an example of how commercialization has improved the financial and market performance of a postal service that had been mired in a dismal state of deficits and poor delivery performance. Canada Post is another postal service that has taken technological reform seriously.
With the growing worldwide trend for postal services to move away from functioning as public service administrations and to operate more as commercial businesses, postal services have had to become customer-oriented, rapidly responsive in crucial areas, and capable of financial viability. For such a transformation into a dynamic and progressive organization to take place, postal administrations must become less bureaucratic, must be able to implement actions and ideas rapidly, and must become more innovative and more personal. In these respects, Singapore Post, which is a good example of successful commercialization and which may prepare for eventual complete liberalization of the sector, is well able to share its experience.

Singapore Post is a highly unusual case because of ongoing progressive reform measures that have been taken despite the fact that Singapore is one of the few countries in which the postal service has provided the public with a good quality of service at affordable rates and has been financially successful as well. Nevertheless, in anticipation of a rapidly changing and increasingly competitive environment, Singapore's postal development policy has kept one step ahead of events by providing Singapore Post with both the guidance and the latitude to continually improve itself in order to compete. Thus, in contrast to most countries, in Singapore reform in the postal sector has not been targeted to redress a crisis situation. This is primarily evident in the fact that public policy has maintained an arm's length relationship regarding the Post's operations and regulation has been directed exclusively at developing the postal sector in the interests of society. Thus, the case of Singapore Post not only provides the ex-

---

1 This case study is based on research undertaken by John Mulligan, UPU consultant, and John Lee, Gary Halpin, and Donald Dickie, of Canada Post Systems Management Limited.
ample of a postal service that has taken the appropriate steps necessary at each stage to maintain its competitiveness but also highlights an enabling policy environment that has fostered postal development by both initiating and facilitating the reform process.

The Republic of Singapore is an independent city/state, located off the tip of the Malay Peninsula and connected to Malaysia by a causeway. Formerly a British Crown colony and then part of the Federation of Malaysia, Singapore became independent in 1965. Singapore is a parliamentary democracy and has enjoyed unusual political stability, as the same prime minister and political party ruled the state for over 30 years. Although a new prime minister took office in 1990, there was no change in the ruling party. This situation has no doubt fostered a single-mindedness and consistency with regard to public policy planning and direction.

Singapore is a compact, entirely urban, modern city/state. The nation is contained principally on the Island of Singapore and covers approximately 641 sq km. It is densely populated (2.873 million people, or approximately 4,482 people per sq km) and has a literacy rate of approximately 90 percent. The small size of the country, and its consequent lack of a rural/urban division, and also its high population density, make the national delivery of postal services comparable to city deliveries in most countries.

In the 1970s Singapore's GDP grew on average by 8.3 percent annually and in the 1980s it grew by 6.7 percent annually. Since a recession in 1985, Singapore has continued to experience a healthy, sustained economic growth. The economy was expected to grow by 6 to 7 percent in 1994, and was forecast to maintain a growth of 6 to 7 percent in the following five years. In 1992 Singapore enjoyed a GNP per capita of US$15,730, which put it in the category of a high-income economy.

A large part of the success of Singapore Post may thus be attributed to the country's unusual geographic and demographic features, the consistent public policy toward the postal sector, and the robust economic growth that the country has experienced. However, the dismal condition of the postal sector in most countries, developed and developing, indicates that the existence of favorable external factors is not sufficient for the establishment of a quality postal service. Accordingly, the story of Singapore Post highlights the significant role in the development and transformation of this sector that was played by the postal service's efforts to constantly improve its performance, and the government's foresight in its policies regarding postal development.
The evolution of Singapore Post, which deviated greatly from the pattern followed by most postal administrations, was marked by several distinct events. The distinct phases experienced by the Post show how its development intertwined with that of the telecommunications sector, and also illustrate its transforming organizational form over time (see Figure 1).

Singapore Post has a long and eventful history that dates back to the founding of Singapore in 1819, when a single mail office manned by just three people collected and delivered the small volume of letters. With the flourishing of trade and commerce and a corresponding growth in the letter volume, the postal service evolved into a separate government department in 1858. From 1949 to 1965 a colonial postal system was imposed during which time Singapore and the Federation of Malaysia formed a single postal area. Following its independence in 1965, Singapore took over its own postal function in stages and was admitted to the Universal Postal Union (UPU) in 1966. In 1967 the Singapore Postal Services became an autonomous body with its own Postmaster General. The postal service and the international and domestic telecommunications services operated as three distinct government departments within the Ministry of Communications. In 1972 the Post Office Savings Bank was separated from the Postal Services Department and commenced operations as an independent statutory corporation.

Figure 1
Phases in the Evolution of Post and Telecommunications

---

2 For examples, see Chapter 3 on Corporatization of the Postal Service.
While Singapore Post’s status continued relatively unchanged, in 1972 telecommunications was transformed from a government department into a statutory board called TAS (Telecommunications Authority of Singapore), and in 1974 international and domestic telecommunications services were consolidated into TAS (see Figure 1). The telecommunications service was incorporated in order to facilitate commercialization of the sector by granting it more autonomy and holding it to financial self-sufficiency. The next major event in Singapore Post’s evolution took place in 1982, when the Postal Services Department was merged with telecommunications. Thus, as part of TAS, the Post also became a statutory board. This merger signaled the government’s recognition that the postal service, like telecommunications, could be run as a business along commercial lines. This merging with telecommunications was also meant to provide a shelter for Singapore Post during a period crucial to its development. Thus, unlike most other countries, where the combined P&T form is traditional and is increasingly being dismantled, in Singapore there was a converse situation.

The next watershed in the evolution of postal services occurred in 1992 when the TAS Act was passed. This Act provided for the following three fundamental changes:

1. The establishment of an independent regulator retaining the name TAS
2. The corporatization of the telecommunications and postal services through the creation of Singapore Telecommunications (Telecom) Ltd. and Singapore Post (Pte) Ltd.
3. The establishment of Singapore Post as a subsidiary of Singapore Telecom.

These events marked the formal separation of the ownership, operation, and regulation of both the postal and the telecommunications services in Singapore. Consistent with Singapore’s prior history of pioneering the reform process, in October 1993 Singapore Telecom was partially privatized and became a public limited company. This event points to the government’s willingness to loosen the reins on ownership, although it is still the majority shareholder. Singapore Post remains a private limited company and its shares have not been offered in the market; therefore, the Post is still a subsidiary of Singapore Telecom, and whether it will follow the route of privatization taken by Telecom remains to be seen.

---

¹For a description of the broad legal classification of state-owned enterprises, see Chapter 3.
²Eleven percent of its shares were sold to the public.
Prior to 1992 the government directly regulated the postal and telecommunications sectors. In 1992 the passage of the TAS Act provided for the creation of an independent regulatory authority (TAS), which remained a statutory board responsible to the Minister of Communications and under the direction of a government-appointed Board of Directors. The Board consists of representatives from business, labor, customer groups, and industry. TAS, a small organization with a staff of 130 in 1992, is completely self-financed through its licensing and frequency fees and through investment income and therefore maintains complete financial autonomy from the government.

As an independent regulator, TAS carries far more credibility as an impartial body than does the government, both with the public and with the postal and telecommunications licensees. It is worth noting that while several countries have separated the function of ownership from ownership through corporatization of the postal services, very few have separated regulation from ownership by establishing an independent regulatory authority. In this respect, the establishment of TAS is a progressive move in the reform of the postal and telecommunications sectors and is meant to pave the way for gradual liberalization.

In its new role, as defined by the TAS Act of 1992, TAS serves two principal functions as both a regulator and a promoter of the postal sector. In its capacity as a regulator, TAS must ensure that Singapore continues to enjoy a high standard of postal service at reasonable prices, as it guides the transition to a more competitive environment in this service. TAS has granted Singapore Post an exclusive license to provide postal services for letters and postcards until the year 2007, and a non-exclusive license for these same services through the year 2017. It is anticipated that full competition could be permitted for letters and postcards in 2007. All other items, such as parcels, advertising material, and courier express items, are open to competition. Licensing conditions require Singapore Post to provide a nationwide postal service and to comply with the TAS price control arrangements and standards for quality of service and network performance. TAS is also empowered to

---

5 The description of TAS focuses on its role with respect to the postal sector. TAS is also responsible for regulating the telecommunications sector and managing the radio frequency spectrum of Singapore.

6 On April 1, 1995, TAS partially liberalized the letter mail market by granting courier companies licenses to provide express letter delivery services. With this liberalization, more than 100 new operators offered the service. This move signals the Authority's willingness to respond to market demand. Indeed, TAS is constantly reviewing the need to open the market to competition and has introduced appropriate measures which benefit the postal industry and the users and also improve service quality. However, any latitudinal changes on the monopoly can only be implemented after the 15 year exclusivity granted to Singapore Post expires in 2007.
charge an initial and recurring annual license fee from its licensees. It is understood that the license fee for Singapore Post is a percentage of the annual total sales, subject to review from time to time.

The TAS Act specifies a clear mandate for TAS, which encompasses the following requirements with respect to the postal service:

- Ensuring the provision of good and sufficient domestic and international postal services
- Issuing licenses to operators of postal services
- Regulating rates while ensuring efficient services and recognizing the necessity for independent financial viability on the part of the operators
- Promoting the development of postal services in accordance with recognized international standard practice and public demand
- Representing Singapore in international postal matters
- Advising the government on all postal matters
- Furthering the advance of technology relating to postal systems.

TAS follows an ongoing policy of progressive market liberalization in both the postal and the telecommunications sectors. The objectives of liberalization are to facilitate greater product choice, more competitive pricing, higher standards of service, and greater innovation in the range of services and products made available to the public through competition. Thus, the process of deregulation of the postal sector is regarded as eliminating the barriers to positive change. The self-stated goal of TAS is to support Singapore’s aim to become a global hub for business and commerce by making Singapore a global hub for communications.

Monitoring the Quality of Service

As the regulatory body for the postal sector, TAS sets standards to keep services and infrastructure in Singapore in line with the latest global advances. The standards set by TAS for all the products and services provided by Singapore Post are intended to provide superior service in terms of competitive pricing, availability, accessibility, quality, and variety. TAS works closely with international bodies committed to developing standards, and participates in meetings of international and regional postal bodies to ensure the coordinated development of standards between postal administrations.

Besides setting standards, TAS engages in the monitoring of domestic and international mail and counter services. Performance indicators measured by TAS include various aspects of service quality, such as mail delivery time, queuing time for counter services, etc. Independent consultancy firms are commissioned by TAS to conduct
customer surveys and other quantitative measurements to examine the performance of these services. Opinion surveys provide further insight into customer satisfaction and expectations. Results are then compared with those of major operators around the world, which enables TAS and Singapore Post to jointly improve the quality of the services provided to consumers and businesses in Singapore. In this way, TAS aims to stimulate greater efficiency in existing services as it promotes the introduction of new services.

TAS has interpreted its responsibility to guarantee the provision of "good and sufficient" postal services as stipulated in the TAS Act rather broadly. Thus, it considers anything that affects the national interests with regard to postal services to fall within its purview. Accordingly, any changes that might materially affect the delivery and retail networks or that might restructure service standards must be approved by TAS. In addition, Singapore Post must keep TAS informed of any new business developments, including the introduction of new products and the formation of alliances.

Thus far, TAS has not intervened in any of Singapore Post's major business decisions. For example, Singapore Post has been free to consolidate costly outlets in unprofitable areas outside of the central business district and to increase the smaller, retail-only outlets in business areas. Moreover, TAS has not restricted Singapore Post from diversifying into non-postal product areas or entering into alliances with other companies to provide value added products and services. Since the Post and TAS have been in agreement regarding the development of the Post, no conflict between them has arisen to date. Nevertheless, given the broad jurisdictional authority that TAS holds over the Post, it remains to be seen whether the Post's autonomy would be eroded should a difference of opinions arise.

Regulating Tariffs

An important component of TAS's responsibility is to monitor the prices of Singapore Post's monopoly products to ensure that they are affordable for the public. Prior to the establishment of TAS, an explicit mechanism for tariff increases was not followed. This is evidenced by the fact that in the 18 years prior to 1989 postal rates were kept constant (see Figure 2). Unlike the postal services in most countries, legally Singapore Post is not subject to a universal price requirement. However, Singapore's small size and lack of an urban/rural division minimizes cost differentials in the delivery of mail, thereby providing no basis for differentiated pricing within Singapore.

Postal rates were kept at 10¢ for 18 years despite inflation because the Post was able to sustain itself through productivity gains arising from the legislation in 1971 which mandated the provision of central letter boxes at ground level for any high rise establishment above four stories.
In 1992, TAS developed an explicit mechanism to raise Singapore Post's tariffs, which involved benchmarking its tariffs to ten countries to evaluate the reasonableness of the postal rates for regulated products. The proposed postal rates had to be lower than the average of the median four countries of the ten-country benchmark. In 1995, TAS switched to a quarterly comparison of Singapore Post's rates against a three-country benchmark to ensure that Singapore Post's tariffs are lower than the average tariff of Hong Kong, Taiwan, and South Korea. In spite of the benchmarking, the rate-setting process still includes an examination of whether the cost components of the Post are increasing, and whether the Post is taking steps to become more cost-effective. Thus, Singapore Post's tariffs are regulated on the basis of internal cost efficiencies and external tariff comparisons.

Although Singapore Post does not require approval from TAS for the pricing of its competitive products, any changes in the rates for these products have to be submitted to TAS one month prior to implementation for “information” purposes. Similar “advice” requirements exist for the introduction of new products.

Promoting the Development of the Sector

TAS considers automation the key to promoting efficiency in the Post and fully supports Singapore Post's plans to automate, where possible, in order to improve postal services provision and to keep up with world trends in modernizing postal equipment and networking. TAS helped launch a new postal code system to ease the mechani-

---

9 The countries in the ten-country benchmark were the United Kingdom, the United States, Australia, Malaysia, Indonesia, Japan, Hong Kong, New Zealand, Taiwan, and South Korea.
zation of the sorting process for individual addresses, with minimum inconvenience to the public, TAS also urged envelope manufacturers to produce standard sizes to aid the automation process. In addition, TAS has supported Singapore Post’s initiative to launch Postal Automated Machines (PAMs) in 1994; these self-service post office terminals offer customers the convenience of 24-hour service. TAS aims to spur the development of a modern and up-to-date network of post offices and is promoting the widespread use of technologies and systems so as to provide an integrated, modern universal postal service.

TAS is also aiding the development of Singapore Post and the postal sector by confining its regulation to ensuring that rates are affordable and service quality is high. Thus, TAS is unconcerned with capping Singapore Post’s returns, as is evident by the Authority’s approval of the 1995 rate increase despite Singapore Post’s consistent high profitability (see Figure 12). It is highly unusual for an independent regulator to allow financial returns of this magnitude, even when benchmarks or price ceilings are used as the formal mechanisms for regulation. An implicit justification for the lack of concern with returns may be that Singapore Post is very specific about utilizing retained profits for improving future service. The Post has declared that profits (after dividends) are transferred to its reserves and then are ploughed back for re-investment in the postal infrastructure to support future growth. TAS may implicitly permit Singapore Post to achieve high returns because these returns, in the form of investments in infrastructure, will serve the consumer better in the future. In addition, by allowing the Post to retain residual profits, TAS ensures the maintenance of incentives for further efficiency improvements. Thus, the unconventional regulatory philosophy followed by TAS appears to have helped the development of the sector as a whole.

Because Singapore Post has been able to fund all of its investment through retained earnings rather than resorting to external borrowing, it has economized considerably. Although the Post has forgone interest income because of this financing strategy, it has actually benefited from the differential in the interest rate on its earnings and the higher lending rates charged by commercial banks. For example, in 1995 when the Post invested S$71.2 million it avoided paying interest rates in the range of 6 to 6.5 percent to commercial banks on this amount, but incurred an opportunity cost by losing interest income in the range of 2.5 percent on this amount. Because of the difference in interest rates, the Post saved S$2.67 million through its investment financing strategy (see Figure 3).
crease over the next few years. The Post anticipates spending S$529.9 million in the next five years to (1) construct the new Singapore Post Centre with automated mail processing equipment; (2) redevelop its delivery bases; (3) purchase post offices and motor vehicles; and (4) invest in computerization at the post office counters. This will further enable Singapore Post to upgrade customer service, enhance productivity, and improve operating margins.

Figure 3
Gains from the Investment Financing Strategy, 1971-95

Singapore Post's investment financing strategy is accompanied by the regulation of tariffs to ensure that the tariff levels are below benchmark averages. This implies that high levels of returns are not to the detriment of the customers and that the adopted investment financing strategy is helping the postal service to keep its tariffs within acceptable limits at all times.

This unusual regulatory approach on the part of TAS represents a continuation of the government's policy toward Singapore Post when it was a statutory corporation. TAS and the government have consistently aimed to ensure that tariffs stay within acceptable limits, that consumers benefit from a wide range of high quality services, and that Singapore Post continues to make productivity and efficiency gains. As long as these conditions are being met, TAS and the government have given Singapore Post the freedom to pursue profit maximization objectives—especially if these profits are reinvested into the business for the betterment of the sector.

Thus, one of the major factors contributing to Singapore Post's success has been the regulatory philosophy, which seeks to protect the interests of the consumers while allowing the Post to operate autonomously. The creation of an independent regulator has helped

---

17 Singapore Post is expected to invest a total of S$500 million by 1998 to build a new sorting center.
to specify and separate the roles, responsibilities, and areas of control of both the operator and the regular, which has removed the potential for excessive intervention by the regulator and has helped to further clarify and stabilize the Post's policy environment. Although TAS does possess considerable authority over Singapore Post in its regulatory capacity, as long as the Post has met its obligations, TAS has followed the philosophy of not intervening in the Post's business decisions or eroding its operating autonomy. If complete deregulation were to be introduced after 2007, TAS would also have the responsibility of ensuring a level playing field for all competitors in the sector and ensuring that all parties abide by their duties and obligations.

As has been mentioned, Singapore is unique in that, whereas most governments around the world are currently dismantling the traditional structure of combined telecommunications and postal departments, in Singapore the two services were integrated in 1982. Singapore Post is presently a private limited company and is licensed by TAS to provide postal services. At the same time, the Post is a subsidiary of Singapore Telecom, which became a public limited company in 1993. Thus, Singapore Post's organizational structure and environment are unusual by world postal norms.

The integration of the postal service with telecommunications was undertaken so that Singapore Post could benefit from Singapore Telecom's commercial success during the latter's transition from a government department to a business-oriented corporation. Since Singapore Telecom was the first to become a statutory board, it has a longer history of applying commercial principles to the management of its enterprise. Singapore Telecom is currently the largest company on the Singapore Stock Exchange and enjoys worldwide recognition for its services, and this situation has enhanced the corporate image of Singapore Post. In fact, the association with Singapore Telecom has enabled Singapore Post to dissociate itself from the government and develop as a commercial entity in the public eye.

Singapore Telecom also served as a support while Singapore Post was building its corporate infrastructure. For example, Singapore Post shared corporate resources such as personnel, finances, and maintenance with Singapore Telecom throughout the 1980s, which allowed the Post to focus on core aspects of its operations. Immediately after the merger, Singapore Post made it a priority to improve working conditions, benefits, and services for its staff. In an effort to become more decentralized, the Post gave its staff greater freedom to make decisions. Singapore Post was also able to draw on Singapore

---

12 Singapore Post is one of the five subsidiaries of Singapore Telecom which is akin to a holding company.
Redirecting Mail: Postal Sector Reform

Telecom's human resources pool to staff some of its management positions. In 1992, with corporatization, Singapore Post was established as a fully independent subsidiary with its own management functions and corporate infrastructure.

Another motivation for the integration of Post with Telecom in 1982 was to harmonize the roles of the two in an environment in which electronic communications services were rapidly gaining in importance. Rather than allowing the two services to become involved in potentially destructive competitive battles over the provision of these services, the two were merged into one entity with the probable aim of synchronizing their relative roles in this arena. At present, however, both companies are providing various electronic communications services.

Although Singapore Post was initially able to develop rapidly because of the protection and support provided by Singapore Telecom, it is unclear whether any future benefits would accrue from keeping the two companies integrated. Today the Post has come into its own in terms of financial success, quality of services, and corporate image. Currently, the parent and the subsidiary do not share any corporate resources apart from a legal division. Both entities pay each other market rates for services and compete with other private companies to provide these services. Thus it appears that few, if any, synergies remain.

Under the current organizational arrangement, Singapore Post enjoys a high level of operating autonomy with respect to the government. In essence, Singapore Post is responsible for providing a return to its parent, Singapore Telecom, and Singapore Telecom is responsible for providing a return to its shareholders, the majority shareholder being the government. Thus, Singapore Post's implicit financial mandate is to meet its profit targets after paying taxes as any private corporation does, to have enough cash to reinvest in infrastructure, and to pay dividends to Singapore Telecom. However, the Post does not enjoy complete autonomy over its own budgeting and business planning with respect to Singapore Telecom. The Post's senior management works closely with the senior management of Singapore Telecom to establish detailed targets for revenues, operating costs, and profits, which are subject to Singapore Telecom's approval. In addition, Singapore Telecom's President, its CEO, and the Chairman of its Board hold the same positions within Singapore

\footnote{In 1993 Singapore Post paid a dividend of 5 percent of profits to Singapore Telecom. Dividends for 1994 were 7.65 percent.}
Post, and Singapore Post's Board of Directors is a subset of Singapore Telecom's Board.\(^4\)

The overlap of senior management between Singapore Telecom and Singapore Post provides a common management approach toward commercialization and a customer orientation, although it is recognized that the telecommunications and postal businesses are entirely different. Singapore Post contributed only 8 percent of Singapore Telecom's total revenue. Since, as has been mentioned, the integration was intended to help Singapore Post develop its corporate image and commercial infrastructure and become self-sufficient and profit-making, there remain no logical reasons to keep the two companies together. Currently, however, no steps are being taken to spin off Singapore Post and establish it as a stand-alone independent corporation.

In summary, with Telecom's authority over the Post as its owner, and with the authority exercised by TAS as the regulator, Singapore Post's jurisdiction is confined to its own internal operations (see Figure 4). Singapore Post's apparent autonomy has been due primarily to the fact that its goals have always been identical with those of the two controlling entities. While this degree of direct control over the Post may have been necessary in the early stages of the Post's corporate development, with the absence of explicit regulation, it may have outlived its usefulness.

**Figure 4**

Control over Singapore Post

---

\(^4\) The President and CEO of the Singapore Telecom Group ceased to be the CEO of Singapore Post on December 1, 1995, although he remains a member of the Board of Directors of Singapore Post. The Executive Vice President and General Manager of Singapore Post was re-designated as the CEO of Singapore Post on the same day.
Achieving Efficiency through Commercialization

One of the keys to Singapore Post's success has been its focused, well-planned, and gradual commercialization process. In the 1980s Singapore Post gradually implemented commercial practices under the guidance of Singapore Telecom. In 1989, when the government announced that TAS would be the first statutory board to be corporatized, Singapore Post adopted commercial accounting practices and created its own Finance and Personnel Departments in preparation for reform. Therefore, when the Post actually corporatized in 1992, the majority of its corporate infrastructure was in place and it had to create only the sales and marketing, engineering, and computer service divisions. In addition, sufficient rate increases had been implemented prior to corporatization to ensure that revenues would suffice to maintain service levels and provide for capital investments. Investment in infrastructure, especially technological infrastructure connected to automation and computerization, had already been undertaken to provide for further efficiency improvements. Thus, in 1992 Singapore Post was well prepared for corporatization.

Throughout its development process Singapore Post has undergone commercialization in order to compete in the marketplace. Currently, since only 65 percent of its revenues come from its monopoly services, the Post faces vigorous competition in other market segments such as courier and express services, admail, parcels, multiple agency services, financial services, and electronic communications. DHL, TNT, FedEx, and UPS are all active competitors in the courier and express delivery segments and there is intense competition from banks in the issuance of traveler's checks, money orders, and international bank drafts. The Post is also experiencing strong and growing indirect competition in its monopoly areas from electronic communications devices such as fax and email. Singapore Post expects the twenty-first century to be an era of information technology and a cashless society and is accordingly preparing a niche for itself. Thus, the Post has focused on improving its operational efficiency and capitalizing on its core competencies, which are its delivery capabilities and its extensive network of computerized retail outlets. Presently, with the prospect of full deregulation in view, its commercialization efforts have taken on renewed vigor.

Singapore Post's core commercialization efforts are broadly directed toward the following objectives: (1) enhancing efficiency via restructuring, consolidation, and automation; (2) developing a customer orientation; (3) diversifying its product base; and (4) forming alliances with other companies.

Improving Operational Efficiency

Even as a government department, Singapore Post was able to provide efficient services since the government itself was concerned with promoting economic development. In 1971, Singapore was one of
Case Study 1
Singapore Post: An Enabling Environment

the first countries to pass a law that made it mandatory for all high rise establishments of more than four stories to provide letter boxes at the ground level. This enabled the Post to improve its delivery costs considerably. In 1979 Singapore Post implemented a four-digit postal code system which facilitated mail processing and sorting. These increases in productivity helped Singapore Post continue operating to 1989 without rate increases.

Singapore Post, with the support of its owner and the regulator, has always considered that automation and the integration of technological advances were key to improving its efficiency. Therefore, it has invested in automation equipment such as Optical Character Recognition (OCR) sorters, mechanized culling, facing, and canceling machines, and mechanized parcel and sack sorters. Currently, 30 percent of letter mail and 90 percent of parcels are sorted mechanically. Automation generates considerable economies for the Post, especially since all of its sorting operations have been consolidated in a single facility. In 1990 Singapore Post was given approval to build the Singapore Post Centre at a cost of approximately S$500 million. When completed, the Centre will comprise office buildings and a modern fully automated mail and parcels sorting center. With the proposed new six-digit postal code, the new facility will be able to automatically sort mail to the delivery sequence of the letter carrier.

Singapore Post has also invested in increased computerization, new buildings, and increased motorization of its delivery force. The Post is currently the only company using track and trace for domestic courier services in Singapore, which gives it a considerable edge in this market segment.

Labor expenses comprise only 43 percent of Singapore Post's total expenses, whereas labor costs are typically in the 70 to 90 percent range in other countries (see Figure 5). This is partially because of Singapore's relatively low network infrastructure requirements, owing to the country's geographic and demographic features.

However, the low labor costs also reflect Singapore Post's concerted efforts to adjust its employment to maximize efficiencies in collection, sorting, and delivery. For example, the Post has increased the number of part-time workers in its sorting center in order to adjust for peak periods. The Post also maintains a lean corporate staff, of approximately 20 persons, which allows it to reduce overhead costs and to make decisions and implement new products or alliances quickly.15 In addition, the Post enjoys a very good relationship with its work force, since unions in Singapore are commercially oriented and understand the need for cost reductions and technological change. In September 1993, Singapore Post concluded its first collective

15 For example, E-Post, a new hybrid product, only took eight months to develop from conception to implementation.
agreement since corporatization with the Union of Telecom Employees of Singapore. Performance-based salary systems were implemented in this agreement. Thus, owing to all its efforts, Singapore Post has experienced a steady increase in labor productivity. This is manifest in an increase in mail items per employee, which grew by 6 percent annually\(^6\) from 1986 to 1995 (see Figure 6) and in the growing differential between revenue per employee and expenditure per employee (see Figure 7).

Figure 5
Breakdown of Expenses, 1994

- Property Related: 11%
- Depreciation: 5%
- Selling, Administration, etc.: 15%
- Transportation: 9%
- Terminal Dues: 17%
- Staff Costs: 43%

Figure 6
Trends in Employee Productivity, 1986-95

Mail Items per Employee (thousands)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Items</td>
<td>140</td>
<td>160</td>
<td>170</td>
<td>180</td>
<td>190</td>
<td>200</td>
<td>210</td>
<td>220</td>
<td>230</td>
<td>240</td>
</tr>
</tbody>
</table>

\(^6\) On a compounded average growth rate basis.
Recently, Singapore Post has been consolidating its retail network by closing down some of its full-service postal outlets in remote areas and increasing the number of secondary outlets in the business district as a means of keeping costs down. The Post is also reducing the number of delivery bases. All of the above measures have contributed to increased productivity which is visible in the decreasing expenses per mail item (see Figure 8).

**Customer-Oriented Approach**

Singapore Post's efforts to improve internal efficiency have not been made at the expense of quality of service. The Post has realized that it is necessary to focus on its customers in addition to its internal operations in order to remain competitive in the marketplace. The Post began promoting customer satisfaction by implementing new delivery standards and imposing strict standards on acceptable wait-
ing times for customers at its post offices. To better service its customers, Singapore Post also installed PAMs, which are 24-hour self-service machines. To ensure its commitment in this area, the Post has hired independent management consultants to determine the satisfaction level of its customers (see Figure 9).

Figure 9
Indicators of Customer Satisfaction, 1989-94

Another major component of Singapore Post’s customer-oriented approach is the targeting of customer needs accurately, for which the Post established a Sales and Marketing Division in 1992 after corporatization. Although Singapore Post had always taken market factors and the viability of each product into consideration, the Sales and Marketing Division provided the first official and systematic method of targeting customer needs and developing appropriate new products and services. As an example, when the Post realized that express mail service represented a high-growth lucrative segment, it concentrated its marketing efforts on these products (Local Urgent Mail and Speedpost) and in 1993 experienced an increase in the number of sales contracts of over 150 percent for each of these services.

New Products and Services

With the realization that its monopoly products may be open to full competition in 2007, and that these products do not represent a high-growth area for postal services, Singapore Post has initiated a concerted effort directed at diversifying into non-monopoly mail products as well as non-mail products (see Figure 10). Accordingly, Singapore Post has had next-day delivery service for a long time. Prior to 1991, however, letters in the central business district had to be posted by 2:00 p.m. rather than 7:00 p.m. for next-day service to apply.

17 Singapore Post has had next-day delivery service for a long time. Prior to 1991, however, letters in the central business district had to be posted by 2:00 p.m. rather than 7:00 p.m. for next-day service to apply.
Post is developing a diverse mix of postal, telecommunications, and agency products and services. Most of the Post’s product development has been carried out only in the last two years because of the rapid development and implementation schedules in place since corporatization. Therefore, since 1992 Singapore Post has introduced ten new products and services (of which only two are in the monopoly segment), which has widened its customer base and improved its image with the public and is strengthening its position in the future highly electronic market place.

Figure 10
Change in Revenue Composition by Market Segment, 1986-95

Singapore Post recognizes that its postal outlet network represents a unique access to consumers and has marketed this network to other companies. Many of Singapore Post’s new offerings are not related to traditional postal services (see Figure 11). For example, with Post-a-Gift, Singapore Post works with large commercial customers and mails out gifts on their behalf. Singapore Post stocks, picks out, and sends appropriate goods to recipients who are specified by the customer, and intends to offer one-stop shopping to its customers. It also considers the effect of advances in technology on changes in customer needs when developing new products and services. For example, with the recognition that Singapore is moving further toward a cashless society, Singapore Post has configured its PAMs to accept bank debit cards. E-Post, its first hybrid product, merges the electronic transfer of data with the Post’s physical distribution system. Since Singapore Post has existed in its present form for only two years, most of its ambitious expansion into the communications market is still in the planning stage. Currently, the front line counter service computer systems offer 17 postal services, 7 telecommunications services, and 28 agency services.
Figure 11
Select Products and Services Offered by Singapore Post

<table>
<thead>
<tr>
<th>Agency</th>
<th>Traditional Mail</th>
<th>Other Mail</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Collection of fines, taxes, etc.</td>
<td>• Letter mail</td>
<td>• International reply coupons</td>
</tr>
<tr>
<td>• Renewal of licenses</td>
<td>• Parcels</td>
<td>• Franking machine setting</td>
</tr>
<tr>
<td>• Pension payments</td>
<td>• Stamps</td>
<td>• Labeling machines</td>
</tr>
<tr>
<td>• International bank draft</td>
<td>• Registered articles</td>
<td>• Cartons/envelopes and security</td>
</tr>
<tr>
<td>• Greeting card sales</td>
<td>• Express mail</td>
<td>envelopes</td>
</tr>
<tr>
<td>• QTV - advertising medium</td>
<td>• Postal orders</td>
<td>• Stamped stationery</td>
</tr>
<tr>
<td>• Traveler’s checks</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Lamination service</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Area license</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Vehicle entry permit</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Vehicle quota form</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Photo booths</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Browse and buy centers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Money orders</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Benefiting from Alliances

Singapore Post considers the utilization of joint ventures and strategic alliances necessary to help it survive in an increasingly competitive business. Forming alliances with firms that have the expertise or technology in areas in which it lacks competencies has helped the Post to leverage its investment and shorten implementation time scales. The Post began contracting out services in the 1980s, on the basis of whether outsourcing was cost-effective and could provide a high level of service. In the transportation arena the Post has used competitive bids to select two companies to handle airmail at the airport and to transport and store mail at the seaport. Recently, Singapore Post has been working with other companies in information technology to create and provide new products and services. For example, Singapore Post worked with IBM to provide PAMs and formed an alliance with Datapost to create E-Post. It is likely that, as Singapore Post continues to diversify away from its traditional products, it will continue to depend on external partners for complementary technology and expertise.

The Performance of Singapore Post

Singapore Post serves as an interesting case study because its constant efforts directed at improving its operations have resulted in extraordinary success in terms of both financial performance and quality of service.
Financial Performance

In fiscal year 1995, Singapore Post earned revenues of S$264.6 million and an after-tax income of S$80.4 million, representing a return on sales of 30 percent and a return on assets of 17 percent. Since corporatization, Singapore Post has consistently achieved returns on sales in excess of 25 percent (see Figure 12). These are excellent returns even by private sector standards and they easily surpass the average for the postal sector, which is loss-making in an overwhelming number of countries.

Figure 12
Financial Performance, 1986-95

Superior Service

Singapore Post's financial returns have not been won at the expense of customer satisfaction and quality of service. Customers benefit from the following:

1. High delivery standards: Letters and postcards mailed before 7 p.m. from the central business district (CBD) and before 5 p.m. outside the CBD are delivered the next day. Singapore Post's target is to deliver at least 95 percent of mail within these standards. It has consistently attained this target (see Figure 13).

*Singapore Post's fiscal year ends March 31 of each year. All dates in this case refer to the fiscal year unless otherwise noted.*
2. **Low tariffs**: Singapore Post has raised its tariffs only three times over the last 20 years. In addition, Singapore Post's tariffs are benchmarked to ensure that they are lower than the average of selected countries (see Figure 2).

3. **Wide range of products**: Singapore Post offers a variety of innovative products and services at its post offices, providing convenience and one-stop shopping to its customers. Besides strengthening the quality of its basic mail services, the Post has also diversified its product base to reduce its dependence on traditional products (see Figure 14).

![Figure 13](image)

**Figure 13**

**Delivery Performance, 1986-95**

![Diagram](image)

Note: 1994 was the first year of external audits.

![Figure 14](image)

**Figure 14**

**Breakdown of Revenues, 1986-95**

![Diagram](image)
Singapore Post has achieved the above while experiencing increases in both mail volumes and mail per capita. From 1986 to 1995, the total mail volume increased by a 7.4 percent CAGR (see Figure 15). From 1987 to 1992, mail per capita in Singapore increased by a 4.6 percent CAGR, which is much higher than the average growth rates of other high-income countries (0.97 percent) during the same period.

Figure 15
Growth in Mail Volumes, 1986-95

Singapore Post has been successful, both financially and in terms of the quality of its service, because of the interaction of two fundamental factors:

1. Internal commitment within the Post that is directed toward attaining further efficiencies, maintaining a high quality of service, and adapting to a transforming environment
2. An enabling regulatory and institutional environment which has consistently fostered the Post’s development.

Initially, the government supported Singapore Post through legislation that contributed to improving sorting and delivery efficiencies. Then, with the realization that commercialization was necessary to further improve productivity, the government merged Singapore Post with the existing statutory board for telecommunications services. After ten years, the government corporatized the two bodies, thereby granting them further autonomy. It is because the government has allowed Singapore Post to develop as a business from the very early stages that Singapore Post has been able to adapt to a market environment so easily. Judicious regulation directed at ensuring a good and affordable service has also maximized incentives within Singapore Post to achieve financial success. In turn, the fact that Singapore Post is committed to reinvesting its profits in further improvement of the postal service ensures the welfare of the consumer as well.
The true test of Singapore Post's competitiveness, however, will come when it must prove itself under a completely deregulated regime. The Post has been given ample time and support to prepare for possible complete deregulation of the postal market. The only choices that exist now are in how competition will be introduced and what restraints will be placed on the Post in order to ensure the continued growth of competitors. In addition, when Singapore Post is perceived by either the government or its parent as having fully developed, the potential also exists for further changes such as gaining independent corporate status and being privatized. Thus, as Singapore Post looks to the future, certain significant transition issues still remain.
Correos de Chile: Reforming under Constraints

To view the case of Chile’s postal service in context it is necessary to understand the geographic, demographic, economic, and political environment within which it operates. Chile’s population of 13.6 million (as of mid-1992) is predominantly urban (85 percent) with over 40 percent concentrated in the capital, Santiago. Chile stretches like a ribbon along the west coast of South America, with a length of approximately 4,200 km and an average width of only 177 km, spanning an area of 757,000 sq km. The country is bordered on the east by the Andes and on the west by the Pacific Ocean.

Because of these geographic features, Santiago accounts for 80 percent of the country’s mail volume, at about 800,000 items per day. Outside of Santiago, the population and the mail volume densities are very low. Most of the mail centers are connected by a highway transportation network, and only in the far southern and northern reaches of the country is the mail transported by air. As of 1993, the Chilean Post serviced a mail volume of approximately 282 million pieces, equal to a per capita volume of about 20 pieces per year. Home delivery was supplied to 80 percent of the population by a delivery force of approximately 1,800 employees. The extensive network of 1,169 postal outlets (most of which are in rural areas) is staffed by postal employees, and the entire mail processing system is manual. The above features combine to make the Chilean postal service extremely labor-intensive.

Prior to the 1980s, Chile experienced a period of considerable social, political, and economic instability. The early 1970s were characterized by a strong wave of nationalization and expropriation of the

---

1 This case study is based on research undertaken by John Mulligan, UPU consultant, and by John Lee, Gary Halpin, and Donald Dickie, of Canada Post Systems Management Limited.

2 Letter carriers constituted approximately 30 percent of a work force of 6,009.
private sector, under the auspices of the Chilean Socialist Party during the Allende regime (1970-73). The repercussions of this period, together with other factors, culminated in a military coup in 1973 which was followed by several years of severe political repression. Under military rule, which lasted for 16 years, the government initiated a policy of drastic financial and trade liberalization, accompanied by a policy of public retrenchment, as part of an effort to reduce the large fiscal deficits and to halt runaway inflation. The adoption of widespread liberalization programs involving large-scale privatization of the state-owned enterprises and reduction of barriers to foreign investment and trade led to 11 years of uninterrupted growth in Chile. Accordingly, Chile has become a model for economic reform in Latin America. Since the reinstitution of democracy in 1990, the Chilean Government has consisted of an executive branch (the President), a legislative branch (a bicameral legislature), and a judicial branch.

In the 1970s Chile experienced an average annual rate of inflation of 187 percent. This hyperinflation slowed economic growth considerably, and the country's GDP grew by an average of only 1.8 percent per annum during this decade. High rates of inflation and economic uncertainty also led to a sharp fall in gross domestic investment, which was -2.1 percent per year in the 1970s. During the 1980s, with the relative stabilization of inflation, the economy experienced a turnaround. The period from 1980 to 1992 saw an average annual inflation of 21 percent, an annual growth in GDP of 4.8 percent, and a corresponding annual increase in gross domestic investment of 9.2 percent. As of 1992, the per capita GNP in Chile was US$2,730, which, according to World Bank classifications, placed the country in the category of a lower-middle-income economy. Currently, although inflation in Chile still exceeds 10 percent per annum, it is considerably reduced in relation to past levels. As a result of these macroeconomic improvements, Chile now possesses a well-developed transportation and communications system, its population enjoys a high literacy rate of 94 percent, and unemployment is a low 5.5 percent.

Chile has been a pioneer, with one of the most extensive privatization experiences in the developing world. The country's privatization scheme began in 1974, when the military government reprivatized some 250 companies nationalized under the Allende Administration. The final wave of privatizations, which commenced in the mid-1980s, focused on the sale of public utilities and large industrial corporations with the overriding goal of attaining enhanced efficiency and better services for the public. The majority of the former state-owned companies are now privately owned.

Despite Chile's progressive efforts directed at reforming the state sector, its experience with the privatization of large-scale public utilities, and its strong private sector orientation, its efforts to reform the
Case Study 2
Correos de Chile: Reforming under Constraints

Postal sector appears to be ineffectual. Lack of reform in the postal sector may also stem from government neglect of this sector—a situation prevalent in many countries. As a result, the postal service in Chile is operating under conflicting legislation, repressive regulation, and a mantle of strong government control, all of which prevents it from operating as a truly commercial enterprise. Despite these constraints, the Chilean postal service (Correos de Chile) has improved its performance admirably.

The Chilean postal service is strongly influenced by its external environment. Its institutional framework is determined by legislation, regulation, and its owner, the government. The postal service is also affected by its competitive environment.

The Legislative Framework

Current postal legislation in Chile, which was re-enacted in 1982, is essentially based on the first postal law, which was introduced in 1960. The postal service in Chile was originally viewed as an obligation of the state because of a constitutional guarantee of both access to and security of the post. The service was formerly part of the Ministry of the Interior and until 1982 was part of a combined government Post and Telegraph Department. In 1982 the two services were separated and incorporated into two distinct government corporations, Correos de Chile and Telex Chile, respectively.

The 1982 legislation, which defined the legal and company structure of Correos de Chile, carried over the 1960 postal laws intact and merely added language specifying the mission of Correos de Chile. During the 1980s, although there was an ongoing debate about the extent of reform to be undertaken in the postal sector, legislation concerning corporatization or privatization of Correos de Chile was never actually implemented. Thus, Correos de Chile still remains a government corporation. During the late 1980s, uncertainty regarding privatization prevented the Post from developing new products or making investments, which hampered development of the sector. In contrast, reform in the telecommunications sector was both sweeping and rapid, and appears to have benefited the development of the sector (see Box 1).

The postal legislation introduced in 1960 gave the postal service a monopoly over “correspondence,” which was broadly defined as the admission, transport, and delivery of pieces of mail that covered letters, postcards, business documents, newspapers, printed materi-

---

3 A government corporation is more or less analogous to a statutory corporation. Thus, incorporation brought about only partial corporatization. For the difference between the various legal forms, see Chapter 3.

4 Telex Chile was fully privatized in 1985.
als, registered mail, and small packages, all of which must weigh less than 1 kg. However, the same legislation defined another category called “encargo,” which was exempt from monopoly protection. According to Correos de Chile, the definitions of both correspondence and encargo are identical except that the latter is not covered by the monopoly. Since encargo is an unregulated product and there are no restrictions on competitors, reliable estimates of volume counts or other indicators of the size of the encargo market are unavailable. Thus, the 1960 postal legislation, which has been carried forward into the 1982 legislation, in effect enacted conflicting laws regarding the monopoly of mail.

In addition to the treatment of the encargo category, the postal sector was further opened to the private sector in 1980 by the military government’s passage of a Supreme Decree. This decree introduced the concept of “transport upon request” which, while it did not designate a specific product, allowed private companies to transport mail that would normally be under monopoly protection. Although the Supreme Decree does not have the ability to supersede law (i.e., the 1960 and 1982 postal legislations), it apparently carries the full force of law even today. This decree appears to have been motivated by pressure from the business sector to have the government officially permit competition in the postal sector. Thus, as a result of the encargo category and “transport upon request,” the legal environment with respect to the postal monopoly is extremely contradictory and unclear. This lack of clarity creates tremendous uncertainty for both Correos de Chile and its competitors.
Box 1 Reform in the Telecommunications Sector

In comparison with the slow evolution of the postal service in Chile, it is interesting to study the progressive development of the telecommunications sector during the same period. In keeping with the liberal economic reform policy, in 1978 the National Telecommunications Policies Act was passed, which allowed the government to grant concessions, licenses, and permits for the provision of telecommunications services. This law was followed by the 1982 General Law of Telecommunications, which provided the basis for competition in all telecommunications services.

Passage of this legislation led to the privatization in 1988 of all state-owned telecommunications companies, including Compañía de Teléfonos de Chile (CTC), which provides most of the domestic local services, and Empresa Nacional de Telecomunicaciones (ENTEL), which provides the majority of the country's domestic long-distance services and until recently was the sole concessionaire for international services. As of 1993, both CTC and ENTEL were fully privatized and there was substantial foreign equity participation in their ownership.

Since the privatization, turnover in the Chilean telecommunications market has been growing at an annual rate of 14 percent, about twice as fast as the overall economy. There is also clear evidence of an upturn in investment spending. Between 1989 and 1992, investment averaged more than 60 percent of revenues. This is reflected in the growth rate of main lines, which rose from 7.5 percent per year between 1982 and 1988 to more than 25 percent per year since 1989. As a result, in 1994 Chile had a level of telecommunications spending as a percentage of GDP which was higher than the regional average for the Americas. Thus, the liberalization and privatization of the telecommunications sector have proved beneficial to the sector's development.


The Regulatory Environment

As has been mentioned, the legislative environment in Chile is unique in that the legislation applying to the monopoly of Correos de Chile is contradictory and is also not enforced. According to postal legislation, Correos de Chile itself is responsible for enforcing its own monopoly. However, it has chosen not to do so for two fundamental reasons:

1. Strong support for private business exists in the Chilean culture
2. Both the contradictory postal legislation and the Supreme Decree have created a legal environment in which the success of any of Correos de Chile's efforts to enforce its own monopoly appears dubious.

In fact, currently Correos de Chile has challenged the interpretation of the 1982 postal legislation, and among its proposed changes is the complete deregulation of the postal sector.
The government regulates the pricing of monopoly products, which include letters, registered mail, printed matter, and small parcels. Other postal products, such as parcel post, giros, express mail service, and international mail, are not subject to rate approval by the state. Although only the maximum prices for services covered by the monopoly need approval, this category covers a significant proportion of the total revenue. The rate proposal (as well as the margin for each product) is developed within the Post by a cross-functional committee composed of the Planning Advisory Department and the Finances Department and coordinated by Commercial Management. After approval by the Post's Board of Directors, the rate proposal is submitted to the Ministry of Transportation and Communication. The Ministry and the Post then negotiate rate increases which are given final approval by the Executive Board or the President through a Presidential Decree.

The rate proposal developed by the Post is supposed to be based on market considerations, company policy, and national public policy. However, the philosophy followed by the government in regulating the postal service's basic tariffs appears rather unusual in that affordability does not appear to be a primary consideration. Despite the achievement of returns on sales of over 20 percent by Correos de Chile over the last decade (see Figure 1), postal rate increases during the same period consistently exceeded the rate of inflation (see Figure 2). This strategy has made the Post unusually profitable relative to other state-owned companies in the past. However, as of 1993 the Post believed that it had reached a stage at which rate increases based solely on inflation would suffice for it to attain its profit targets.

Figure 1
Profitability of the Post, 1986-94

Return on Sales before Taxes and Postal Levy (percent)

0 10 20 30 40


Gray bars indicate period after new management team was instituted
Figure 2
Rate Increases Relative to Inflation, 1986-93

Relationship with the Owner

The 1982 postal legislation defines the legal and corporate structure of the Post. Correos de Chile, which is fully owned by the government, reports to it through a Board of Directors composed of five individuals appointed by the President of the Republic. The Ministers of Transportation and Economics may each recommend two Board appointees. The Board elects its own Chairman and appoints a General Manager to run Correos de Chile. Although the Board is responsible to the President, its day-to-day communication with the government is through the Minister of Transportation and Communications. The Board also makes appointments to many senior level management positions, which may be subject to political influence or political approval.

In addition to being subject to substantial government control over senior staffing, the postal operating, investment, and borrowing budgets are individually subject to government approval. The overall objective of the budgeting process is to maximize the returns to the government as owner of the enterprise, principally through the setting of profit targets. Investment and operational budgets are developed internally by a cross-functional committee and after approval by the Board are presented to a government committee for review.\(^5\) This review committee comprises representatives of the Ministry of Planning, the Ministry of Finance, the Ministry of Transportation and Communications, and Correos de Chile. The Ministry of Finance, which focuses mainly on bottom line financial results, leads the process and undertakes economic evaluations of the budgets. The Ministry of Planning plays a major role in the approval of investment budgets, which are subject to its scrutiny although investments are

\(^5\) Since the Post has not borrowed externally recently, borrowing budgets have not as yet entered the picture.
funded out of the revenues of Correos de Chile. Funds are transferred from Correos de Chile to the Ministry of Planning to cover the approved investments. Postal investments are evaluated by the Ministry, using financial and social criteria, along with the other investments the government is planning to make for a given period. If the budgets are approved, a request is made to the Ministry of Finance for use of the Post's own resources. Each year when the Post's budgets are approved the government also approves the number of employees. Thus, the government also has substantial control over the size of the work force.

The financial mandate of Correos de Chile is to be financially self-sufficient and to provide a return to its owner. The Post is subject to the standard corporate tax of 15 percent of net profits and also to a 40 percent postal levy unique to Correos de Chile that was introduced in 1990. The Post is also expected to remit to its owner a dividend from its earnings after taxes, which is determined by the state. The dividend payout ratio is essentially negotiated annually with the government during the budget approval exercise. In recent years the dividend has consumed almost all of the earnings after taxes (see Figure 3). In 1992 the Post paid out dividends of 2.8 billion pesos (Ch$) on after-tax earnings of Ch$3.016 billion, and in 1991, although after-tax earnings were Ch$2.326 billion, the dividends paid out exceeded the earnings by Ch$0.156 billion. The Post also engages in profit sharing with all its employees in proportion to their salaries. Prior to 1992 the Post was able to achieve its profit targets because of price increases that were in excess of inflation. From 1994 onward, the Post has aimed at reaching profit targets by increasing internal efficiency and expanding business.

**Figure 3**

Excessive Taxation of Postal Income

---

[Diagram showing Net Income Breakdown in 1993 (pesos, millions):
- Earnings Remaining (4%)
- Profit Sharing (8.5%)
- Dividends (32.5%)
- Postal Levy (40%)
- Taxes (15%)]
The Competitive Environment

Correos de Chile faces intense competition from a host of small local private postal companies; local and national bus companies; newspaper companies; cargo, airline, and railway companies; and international and domestic courier companies. The strongest areas of competition are in parcels and express mail service, which are officially deregulated. The Post has a mere 5 percent of the parcels market (which it exited in 1985 and re-entered in 1989) and less than 1 percent of the courier market (which it re-entered in 1992). Of the 30 courier companies that operate in Chile, major international couriers have the dominant share of the market. Approximately 80 percent of the courier market consists of documents and small packages weighing less than 1 kg, and thereby falling within the purview of the postal monopoly. A relatively large proportion of the parcel market may also fall into the category of items weighing less than 1 kg. The Post currently uses DHL and TNT in certain cases, since their charges are often lower than those of airlines, which apply International Air Transport Association (IATA) rates to their products. The Post has held talks with TNT about creating a more basic courier product which could be sold within the Post, but currently Correos de Chile cannot establish strategic alliances because of a General Controllership regulation. In the meantime, Telex Chile, the privatized telegraph company, has formed an alliance with DHL to service the courier market.

Private postal operators have specialized in specific niches in order to compete with Correos de Chile’s extensive network of post offices. These private operators offer value added services not offered by the Post, such as: sorting, personalized printing, data base management, reliable and secure delivery, rapid delivery (measured in hours), and multiple deliveries during the day in certain suburbs. Chile Express, a subsidiary of Telex Chile, is the Post’s most serious competitor in this area. Chile Express is establishing an alternative delivery network in Santiago and currently has a delivery staff of 270 and approximately 150 to 200 agencies throughout Chile. Chile Express is also the strongest competitor in the parcels segment, is the only company capable of providing international giros in Chile, and, with the introduction of the multi-carrier system, is poised to enter the electronic hybrid mail segment, which Correos de Chile is prevented from entering. Although most private postal companies are currently fragmented, strategic alliances among them pose a serious threat to the Post. The Post also faces the threat of the adoption of electronic messaging systems. Correos de Chile expects the postal monopoly to come to an end within the next two years, after which fierce competition in the national postal arena will ensue.
Commercialization and the Operations of the Post

From 1986 to 1990 the Post's mail volumes grew at a CAGR of 10.1 percent (see Figure 4), despite the prediction of a negative trend in mail volumes from 1985 onward. Because of this pessimistic outlook, and because of uncertainty regarding the corporatization and privatization of the Post, the development of the service had been neglected during the 1980s. Unexpected growth, coupled with inadequate investments and interest in the Post, led to a crisis in 1989 in the following respects: (1) inadequate investments; (2) limited range of products; (3) poor staff morale; (4) lack of strategic vision; (5) poor public image; (6) lowest wage in the public sector; and (7) lack of government interest in postal service development.

Figure 4
Trend in Mail Volumes, 1986-93

In March 1990 a new management team, which was appointed from the business and academic communities as well as from within Correos de Chile, took over the Post and set out aggressively to "revitalize" the service. Management developed a strategy to address the above problems as well as to instill a customer orientation that would enable the Post to recover lost ground and win new markets. In Chile, mail for commercial purposes, which circulates within businesses or between businesses and individuals, accounts for 75 percent of the total mail volume. At this juncture the new management felt that the principal sources of future expansion would lie in developing corporate mail in the areas of direct marketing and mail-order sales, and in express mail—all areas that face significant competition from private couriers. Although the above markets held significant untapped potential (since the business community is extremely sensitive to price and quality), management felt that significant internal reform would be needed to service the demands of the business community. The thrust of the strategy developed for the Post was thus directed toward three key areas: (1) a commercial focus directed
at the customer; (2) an internal management focus on tasks; and (3) a human resources focus on employees.

To implement its goals, management developed corporate projects that cut across functional departments and lines of hierarchy to overcome the inherent tendency to inertia that exists in public administrations. These corporate projects were supported by clear systems of evaluation and coordination. The principal corporate projects were the following:

- An information system development plan
- A training plan
- A quality plan
- A performance program
- A new products program
- A delivery system program
- An employee participation program
- A corporate image and environmental working conditions program
- A regionalization and decentralization program.

Although the Chilean government approved of the new plans for the Post, it did not support these efforts by enhancing management autonomy or by lifting financial or strategic restrictions. However, it did permit the Post to invest increasing amounts in capital investment and in employee training (see Figures 5 and 6). Compared with the investments in the amount of Ch$420 million over the three years preceding the new management, the increase after 1990 is significant indeed. The peak investment in 1992 was due to investment in computerization and information systems. The Post estimates that future trends in investments will be around Ch$2 billion a year.

**Figure 5**
Marked Rise in Investments, 1986-93
Since the new management team has been appointed, the trend in mail volumes has not changed substantially (see Figure 4). The CAGR in mail volumes since 1990 has been 9.1 percent which is slightly below previous growth rates. However, growth in mail volumes has consistently outpaced the average annual growth rate in GDP over the 1980-92 period, which was 4.8 percent. In addition, even after the appointment of the new management team, financial targets have been met primarily through price increases, which outpaced inflation (see Figures 1 and 2).

In terms of operational efficiency, although revenue and expenditure per mail item have increased sharply, the differential between the two has increased favorably (see Figure 7a.). The Post still has fairly high operating costs, however, because it operates a network of 1,130 postal outlets, out of which 700 run at a deficit. While the Post is compelled to maintain this network to provide a nationwide service, it does not have the option of sub-contracting its retail outlets (into private sector facilities), since it is prevented from entering into alliances. As far as employee productivity is concerned, growth in labor cost per mail item has far outpaced mail item per employee (see Figure 7b.). A large part of this is attributable to the substantial wage increases that have been implemented as part of the strategy to make salaries in the Post at par with those in the rest of the public sector. Salaries increased by approximately 80 percent in excess of the CPI from 1989 to 1993.

In Chile, the state has experimented with direct subsidization of deficit services through a competitive bidding process. Thus, it is possible that either the state will directly subsidize Correos de Chile for the maintenance of these deficit outlets, or it will ask the private sector to compete with the Post in servicing these outlets. Whoever puts in a cheaper bid, ensuring a predetermined level of quality, will be paid by the state.
The majority of post offices are now connected with a computer system, which has resulted in improved working conditions, increased security, automation of manual processes, and access to many corporate forms. More important, this investment in technology has provided the capacity to streamline the processes. Special facilities have been introduced for the corporate sector such as monthly billing systems and commercial customer counters at retail facilities. However, as has been mentioned, because regulation restricts it to the provision of traditional mail services, the Post is heavily dependent on this market segment for its revenues (see Figure 8). Correos de Chile believes that the future market trend is one of increasing globalization, competition, and technological replacement, and that, to sustain a position of leadership and financial stability in the long term, the Post must be allowed to offer more diversified and competitive products in accordance with the requirements of the marketplace.
Another factor that severely hinders Correos de Chile’s efforts at improving its internal efficiency, its corporate image, and the quality of its service, is the prevailing inefficiency of its delivery system. The “delivery right” stipulated by law entitles the letter carrier to a fee of Ch$15 from the recipient for each item delivered. Currently, homes and businesses do not have mailboxes and the letter carrier hand delivers each item and collects the fee. This fee accounts for some 50 to 60 percent of the letter carrier’s compensation and therefore creates a strong incentive to hand deliver all mail; this practice slows down delivery operations considerably. The Post is therefore attempting to switch delivery from homes and businesses to postal boxes. In addition to detracting from the commercial image of the Post, the delivery right creates a problem for the introduction of new products (for example, through direct marketing), since recipients are unlikely to pay to receive advertising material. Because of this delivery system, labor costs are a significant component of total costs (see Figure 8). In 1993, labor expenses increased to 72 percent of total costs as opposed to 54 percent in 1985.

In addition, the collection system is bottlenecked: only 2 percent of mail traffic reached the Post through its 1,700 letter boxes. This is due to the public distrust of letter boxes, which historically have been poorly serviced. The Post has contracted out collection services to increase efficiency, has introduced uniforms and corporate logos to increase public confidence, and has introduced a national delivery plan aimed at motorizing delivery, although this goal is far from being achieved.

In addition, changes have been made to the appearance of postal retail counters to give them a commercial and professional look. As far as quality of service is concerned, since 1987 an average of 75 percent of the mail has been delivered on time within the specified delivery standard. This is a fairly low rate considering that current postal delivery performance levels are in the high 80 and 90 percent range. In Chile, the service standard is D+1 for local delivery within a city, and D+2 for cities in the rest of the country. Prior to 1987 no delivery standards existed. Thus, improvement of delivery speed and reliability is another aspect that remains to be addressed.

Correos de Chile has a relatively new, but active, marketing function which is part of a commercial department with responsibility for marketing, sales, and retail counters. The commercial department’s objectives of generating new income, developing a commercial attitude toward the customer, and developing a greater understanding of the company’s markets are well integrated into the company’s corporate objectives. There is a national sales force at headquarters which concentrates primarily on the Santiago region. Other regions have smaller sales forces. However, the public still has little knowl-
edge of the benefits of the various products offered by the Post, nor does the Post have a specific customer service group. In addition, the Post does not maintain statistics or information on customer satisfaction with service or with postal products. Thus, performance monitoring is another function that the Post has to reinforce.

Internal contracts called *Commitments of Results* have recently been introduced in the Post as a management technique to enhance accountability. Management has established a total of 24 Commitments of Results with different operating units, services, and supporting areas. Once a year, a contract is developed between the General Manager and each of his 24 direct reporters (14 regional entities, 5 advisers, and 5 functional managers) which is put into writing and is signed by the two parties. The contracts contain targets with respect to financial indicators, operational indicators, quality of service indicators, and working productivity indicators, all of which are evaluated twice a year. If a manager fails to meet his contracts for two consecutive years, he may be dismissed. Although this system has been in use for only a little over a year, the Post has indicated the following benefits from the Commitments of Results: an increase in investment return; improvement in the margin in sales; increased operational efficiency; and increased motivation of employees. This system has also elicited a higher degree of commitment from employees with regard to the goals of the company and a better attitude toward the introduction of new technologies that are intended to reduce costs. Although the Commitments of Results are a commendable technique for improving internal accountability, because of their relative newness they have yet to prove their effectiveness.

Despite severe legislative and regulatory constraints on its autonomy, Correos de Chile has attempted to streamline its management team, develop a disciplined internal strategic plan, and introduce a structured process for setting management objectives and for promoting goal commitment. Chile’s experience since 1990 shows that changes in management focus and organizational attitude can achieve progress in the direction of commercialization. Beyond a certain point, however, a level playing field can only be achieved through changes in the regulatory regime and the competitive policy. The Post is currently challenging the interpretation of the 1982 legislation by the General Controllership. The thrust of the Post’s proposed changes would officially negate the monopoly, thereby legally allowing competition; would change the tax structure so that it would be in line with other corporations; would allow more product development and joint ventures; and would maintain the Post’s status as a state-owned corporation.
Reform Issues
Confronting the Post

Chile has not yet developed a formal national policy supportive of a commercially autonomous or liberalized postal system. After legislative action was taken to liberalize and privatize telecommunications in the early 1980s, there was a period of debate on the direction of reform in the postal service. However, over a decade has passed and no formal public policy has been enunciated with respect to the postal service. In the meantime, Correos de Chile continues to operate in a highly contradictory legal environment which treats it as the legally designated monopoly provider of services and regulates it accordingly, while at the same time providing legal loopholes for competition. In the interests of the healthy development of the sector, a clear stance regarding either liberalization or enforcement of the monopoly needs to be adopted and enforced.7

Although the economic environment in Chile is strongly based on free competition, private postal companies service only 5 to 7 percent of the market with regard to mail. Because of the confusion about encargo mail and because the private sector is not required to report data, these statistics are highly unreliable and most probably underestimate the true share of the private sector. In areas such as parcels and express mail, which are legally open to competition, private competition is extremely fierce, as has been mentioned. Although the letter monopoly is not enforced, Correos de Chile suspects that entrepreneurs are deterred from committing large amounts of capital to the postal sector because of the Post's de jure monopoly and because of uncertainty about future legal developments in the sector. Current postal companies are relatively small, operate within confined local areas, and have access to capital of between Ch$50,000 and Ch$2 million. Thus, the contradictory legal environment and uncertainty about the sector's legislative evolution are hampering the development of Correos de Chile as well as that of its competitors.

The lack of an independent regulator for price increases has permitted the Post, in collaboration with the government, to implement unusually high tariff increases. Virtually ensured of a high rate of return, the Post is not compelled to reduce costs by improving internal efficiency. On the other hand, the government stands to benefit from the high profitability of the Post since it lays claim to virtually 90 percent of the Post's net income through taxes, levies, and dividends. This absence of an explicit rate-setting

7 In Argentina a similar situation existed in the postal sector. Private permit holders called "permisionarios" competed with Encotel (the national postal service), which had a statutory monopoly on mail. In recognition of the fact that the monopoly was not being enforced, the Argentinean Government issued a decree in 1994 which completely deregulated the postal service. The government felt that it would be preferable to promote competition in order to achieve lower prices, increased efficiency, and better services, and is designing a regulatory and legal framework to bring about these results.
mechanism, administered by an impartial regulator, can have severe negative consequences. An arbitrary pricing scheme has the potentially adverse effects of: (1) either overcharging customers for monopoly services, or (2) lapsing into a bureaucratic and intrusive rate-making process, thereby compromising the long-term development of the postal service for political interests.

The Post is also subject to unusually high levels of taxation of its profits. While the corporate tax is justifiable, the unusually high postal levy puts the Post at a substantial disadvantage relative to its competitors. Utilizing the Post as a cash cow by raising rates and taxing away profits has the potential to deprive the public not only of an affordable postal service but also of a quality postal service.

The development of Correos de Chile has also been curtailed by an unusually restrictive regulatory policy which has kept it from diversifying its product base. It is unfortunate that an organization with the Post's capacity and infrastructure (in terms of postal outlets and delivery capabilities) is prevented from using them in the best interests of society. Not only is the Post incapable of tailoring its product and service offerings to the evolving needs of society, but it also faces the onslaught of its competitors, which are rapidly consolidating and providing innovative new services. In addition, the commercial market, which currently accounts for 70 percent of the Post's revenue, is highly sensitive to advances in the electronic communication arena. Chile has the only digital telephone system in South America, thus facilitating the installation of electronic messaging systems. A multi-carrier system has also been implemented for all long-distance calls, and this is expected to bring about a savings of up to 50 percent. While the Post's competitors, such as Telex Chile, plan to incorporate these technological advances into their products and services, the Post does not have this option.

Contrary to the normal practice in other countries, in Chile regulation by both the government and the General Controllership does not focus on ensuring a high quality of service. Nor does it prevent the cross-subsidization of services within the Post. These are both areas that normally receive considerable attention in the regulation of a monopoly provider of services.

While the Post is expected to operate as a commercially oriented organization, it has not been granted the autonomy to do so. In combination with the restrictive regulatory policy that affects its operations, other factors, such as government control over the Post's operating and investment budgets, its senior staffing, its workforce size, its dividend payout levels, etc., erode a substantial amount of the Post's operating freedom. While the external
environment will play a critical role in the future reform of the Post, completion of the reform process strongly depends on internal initiatives as well. Thus, the Post still must improve core aspects of its operations to improve its basic quality of services. Management has already begun to focus on critical problems such as the inefficient delivery system, the high operating costs, and the poor public image. However, while the Post’s management appears to have made valiant efforts at simulating commercialization, the absence of a supportive institutional environment is ultimately bound to limit the benefits of this strategy.

**Conclusion**

Prior to the 1980s, political and commercial uncertainty prevented any postal reform from taking place. However, despite the country’s economic recovery and political stability, it is unfortunate that a country which pioneered bold economic reform steps in the rest of its public sector remains behind regarding postal reform.

Correos de Chile has itself initiated a request for the elimination of its monopoly in return for greater autonomy and a chance to compete on equal terms with its competitors. The Post should be supported in its reform efforts with an enabling legislative and regulatory framework that will allow the sector as a whole to develop and provide support to commerce and industry. The case of Correos de Chile shows that changes in management focus and attitude can achieve progress toward commercialization, independent of legislative changes. Beyond a certain point, however, structural restraints on the Post must be removed if it is to truly develop significantly. For this to take place, the goals of the postal operator, regulator, and owner must be reconciled and directed at the development of the sector in the interests of society and the country.
Following Finland, which was the first country to completely deregulate its postal service, Sweden abolished its postal administration's monopoly protection on letter mail, effective from January 1, 1993. Sweden Post's active support of the removal of its own monopoly provides an example to countries that maintain that a basic postal monopoly is mandatory if the public operator is to fulfill its universal service obligations. This was also a notable step on the part of Sweden Post because continuing the postal monopoly could be "justified" in Sweden, more than in other countries, for demographic reasons (i.e., the need to service the 15 percent of the population in the northern half of the country). The Swedish postal experience is also unique in that Sweden was one of the few countries to conduct a systematic cost analysis of the postal administration's regional and social responsibilities. This cost analysis has enabled the postal service to equitably isolate those noncommercial products and services that the government requires the postal service to offer as social obligations.

The year 1993 was a historic one for Sweden Post. In December the Riksdag (the Swedish Parliament) approved a decision to incorporate Sweden Post into a limited liability company. The new company, Posten AB, which became effective on March 1, 1994, has remained under state ownership. However, this change in status was not sudden; it was the final step of a gradual process, which began with a move toward commercialization in 1984. From its beginnings, Sweden Post had functioned as a profitable public service organization and government agency. Between 1911 and February 1994, Sweden Post had been a public enterprise responsible for its own budget. Until the mid-1980s, however, the organization was obliged to deliver

---

1 This case study is based on information provided by Torsten Zillén of Sweden Post International.
its profit to the Treasury. It was dependent on the state for its capital expenses and was obliged to obey all directives issued by the government and the Riksdag. Moreover, it was subject to several restrictions with respect to the formation of companies and the acquisition and divestment of real estate and other businesses. The existing organizational form, therefore, constrained Sweden Post’s ability to operate commercially, since public enterprises in Sweden are part of the state and function as administrators of state property.

At the same time, competition from other means of communication and other carriers was increasing. National and international deregulation, together with technological developments, allowed competitors to select the most attractive elements of postal volumes and to offer customized arrangements and products. A direct consequence of this was the drop in the use of post office counters for financial transactions. To counter these developments and to ensure its commercial viability, Sweden Post underwent a transformation from a product-led government agency to a modern, profit-led commercial business.

The new structure gives Sweden Post the opportunity to enter new, complementary areas of business and to provide new products via consortia, alliances, and company acquisitions, both in Sweden and internationally. It also clearly defines the role of the state as owner of, and as customer for, the organization’s services. As the owner of Posten AB, the state contracts for an acceptable rate of return on equity. As a customer, the state expects a basic postal and payment transmission service to exist in Sweden.

After providing a brief background to Sweden Post, this case study discusses the Post in the context of its competitive environment. Following this, the study describes the postal reform process in Sweden (in three steps). Regulation and labor restructuring issues are discussed, followed by brief discussions of the Post’s innovations and of the Post’s position today. A concluding section reviews the lessons that can be learned from Sweden Post’s corporatization process.

**Background: Sweden and Sweden Post**

The particular logistical challenges faced by Sweden Post in terms of postal collection, transportation, and delivery stem from Sweden’s geographical and demographic characteristics. With an area of 174,000 square miles, Sweden is similar in size to California, Spain, Thailand, or Iraq, and is a large country by European standards. Half of Sweden’s land surface is covered by forests. Less than 10 percent is farmland. Nearly 100,000 lakes dot the countryside, which is relatively flat. There are thousands of islands along the jagged coast. With a population of 8.8 million, 85 percent of which lives in the southern half of the country, Sweden has a polarized population density. Like other industrialized countries, Sweden has a low birth rate and a
high life expectancy (76 years for men and 81 years for women). About 4.3 million people (50 percent of the population) are in the labor force, and 75 percent of women in the 16 to 64 age group are gainfully employed. Unemployment stood at 7 to 8 percent in 1994. Roughly 25 percent of the labor force, mainly women, work part time. About 80 percent of all employees are members of a trade union.

Sweden Post is the largest service and communications organization in Sweden. On an average day, the organization handles 17 million mail items and sells services worth SKr 90 million. Approximately 580,000 customers call at the post offices and 40,000 mailboxes are emptied. Postgirot (the postal savings bank) books transactions worth SKr 24 billion, and rural letter carriers cover 220,000 km on their deliveries.

Posten AB is the limited company delegated by the government to provide universal postal service in Sweden. In 1993 its revenues were SKr 21.6 billion (US$2.9 billion), yielding a profit of SKr 1.4 billion net of taxes (US$183.1 million). The number of staff employed stood at approximately 50,000. The company's basic business concept is illustrated in Figure 1.

This basic business concept is to be able to transmit messages, deliver goods, and provide a payments transmission mechanism between people in Sweden and abroad. With an annual mail per capita of 500, which is among the highest in Europe, Sweden Post delivered approximately 4.3 billion postal items in 1993. Normal first class mail is delivered overnight all over Sweden, and 96 percent of all deliveries are able to reach this target. Prices charged for delivery of mail had been under the European average until VAT was imposed. Highlights of the Sweden Post group over the period 1991-93 are presented in Table 1.

---

2 Based on an exchange rate of US$0.1343.
Table 1
Sweden Post Group Highlights, 1991-93

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating revenues (Skr m)</td>
<td>21,032</td>
<td>22,096</td>
<td>21,644</td>
</tr>
<tr>
<td>Profit after financial items (Skr m)</td>
<td>1,168</td>
<td>1,413</td>
<td>1,363</td>
</tr>
<tr>
<td>Profit margin (percent)</td>
<td>5.6</td>
<td>6.4</td>
<td>6.3</td>
</tr>
<tr>
<td>Return on equity (percent)</td>
<td>15.4</td>
<td>15.9</td>
<td>13.4</td>
</tr>
<tr>
<td>Investments in fixed assets (Skr m)</td>
<td>1,700</td>
<td>1,693</td>
<td>917</td>
</tr>
<tr>
<td>Total assets (Skr m)</td>
<td>53,211</td>
<td>46,197</td>
<td>48,709</td>
</tr>
<tr>
<td>Average number of employees</td>
<td>56,415</td>
<td>53,345</td>
<td>50,213</td>
</tr>
</tbody>
</table>

Competition Faced by Sweden Post

The Postal Sector all over the world is being exposed to competition from other means of communication and from other and/or new carriers. Sweden is no exception to this rapidly evolving pattern. The changes in the business environment are reshaping the form of product development, marketing, and restructuring in Sweden Post. The most significant of these changes are the following:

- Rising competition and new patterns of customer behavior in the wake of technological developments
- National and international deregulation, which gives competitors the ability to select the most attractive elements of postal volumes and to offer customized arrangements
- An increasing volume of automated money transfers (giros) leading to a continued decline in the use of post office counters
- A demand for leveling the playing field which requires Sweden Post to be subject to the same laws and regulations that apply in comparable industries with respect to pension funds, commercial return on capital and dividend requirements, and equivalent wage and employment conditions.

To understand the emerging competitive environment and the threat of competition eroding Sweden Post’s market share, it would be useful to analyze the primary three markets in which Sweden Post operates, namely:

- Communications/Messages
- Goods Transport/Logistics
- Payment Handling/Financial Services.

Table 2 shows the services offered by Sweden Post, its share in these markets, and the proportion of Sweden Post’s revenues generated from these services.
Table 2
Services Offered by Sweden Post

<table>
<thead>
<tr>
<th>Market</th>
<th>Sweden Post market share (percent)</th>
<th>Proportion of Sweden Post revenues</th>
</tr>
</thead>
<tbody>
<tr>
<td>Communications/Messages</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Written business communications</td>
<td>90</td>
<td>32</td>
</tr>
<tr>
<td>Written market communications</td>
<td>55</td>
<td>12</td>
</tr>
<tr>
<td>Private written communications</td>
<td>95</td>
<td>6</td>
</tr>
<tr>
<td>Daily newspapers</td>
<td>35</td>
<td>2</td>
</tr>
<tr>
<td>Members' magazines</td>
<td>100</td>
<td>1</td>
</tr>
<tr>
<td>Other periodicals</td>
<td>75</td>
<td>1</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>54</td>
</tr>
<tr>
<td>Goods Transport/Logistics</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inland parcels, mailings</td>
<td>62</td>
<td>11</td>
</tr>
<tr>
<td>International parcels</td>
<td>10</td>
<td>1</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>12</td>
</tr>
<tr>
<td>Payment Handling/Financial Services</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Giro transfers</td>
<td>50</td>
<td>18</td>
</tr>
<tr>
<td>Banking services</td>
<td>11</td>
<td>7</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>25</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td></td>
<td>9</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>100</td>
</tr>
</tbody>
</table>

Communications/Messages

In the communications/messages market, Sweden Post letter mail faces competition from three main sectors: telecommunications and data communications; computer-based communications; and other carriers.

Telecommunications and Data Communications. Over the last few years competition from telephones and other forms of data communications, such as telefax, have resulted in a decrease in communication through letters in some customer segments. The decrease in the price of telephone rates combined with the ease and penetration of the telecommunications market has fueled this decline. Sweden Post estimates that one in three telefax messages replaces a letter.

Computer-based Communications. With the use of computers becoming pervasive, electronic mail has become the preferred means of communicating, especially because of its low cost and ease of use. Electronic mail is fast becoming a major competitor of traditional letters, and if the current growth rates continue the trend is expected to last.
Other Carriers. In addition to competition from domestic mail delivery services, competition from international couriers and the express mail/parcel businesses is strong in the market for international messages. The increase in remailing services poses a threat to profitable mail exports. Competitors have been cashing in on the poor international settlement system among postal administrations by posting bulk mail in countries with lower postal rates.

Goods Transport/Logistics

In the goods transport/logistics market, competition is both domestic and international.

Domestic Market. Severe competition persists in the market for distribution and transport of goods. Bilspedition (with 36.0 percent of market share) and ASG (with 30.0 percent of market share) are the main competitors of Sweden Post, which has 23.5 percent of market share based on turnover.

Sweden Post still enjoys a dominant position in the light cargo market (under 35 kg), although it has a smaller share of the heavy goods market. The transport industry has long been characterized by unsatisfactory profits, which were further aggravated by the recession of the early 1990s.

International Market. Profitability in the international transport market has also been low. Mergers, acquisitions, and rearranging alliances have resulted in sudden shifts in Sweden Post's competitive position. The excess supply that exists in this market means that further restructuring will continue in the haulage and international courier market which will oblige the Post to compete for existing business.

Payment Handling/Financial Services

In this market, the competition is from other banks and also from electronic systems.

Other Banks. With the abolition of Postgirot's exclusive right to government payments and their transmission, this market will be opened up further. Negotiations are taking place between Postgirot and the other banks regarding a proposed computer linking of the autogiro system to the salary-based accounts of banks.

Electronic Systems. Over the past ten years, transactions in the post office network have fallen by slightly more than one-third. This declining trend is expected to continue with the increased automation of payments transmissions and cash withdrawals. This increase in
electronic transfers will necessarily result in a continuing fall in the demand for traditional banking services.

In view of the constraints discussed earlier, which had hampered Sweden Post's ability to operate commercially, and in view of the increasing competition faced by the Post, the reform of Sweden Post was undertaken. Figure 2 traces this reform process and indicates the three key steps, which are discussed in detail below.

Figure 2
Sweden Post's Reform Process

**STEP 1. Business reorientation and systematic business planning**

**STEP 2. Reorganization of Sweden Post into strategic, logical, and clearly defined business areas**

**STEP 3. Transformation into a commercial corporation**
- Abolition of the postal monopoly
- Introduction of the Postal Services Act
- Incorporation into a limited liability company
- Agreements between the government and Sweden Post
  - Application of VAT
  - Competition in government payments
  - New legal structure
Step 1: Business Reorientation and Systematic Business Planning

Over the past 15-year period, Sweden Post has undergone a number of important changes as part of a logical and necessary evolution from a production-led government agency to a modern customer-led and profit-led business. In the past, all funds for investment had to be requested from the state. In the late 1970s, however, the Post Office was permitted to set up a Consolidation Fund for the purpose of equalizing results in good and bad years. Allocations to, and withdrawals from, the fund required government approval. The Consolidation Fund accumulated a large surplus over the years. Over time, a worsening of the government deficit and Sweden Post's desire to gain autonomy resulted in the Post Office's decision to buy all its assets from the state. Sweden Post was able to pay for the assets from its Consolidation Fund.

In 1985 further freedom of action was obtained. The Swedish Parliament approved Sweden Post's right to make practically all its own investment decisions. All investments were to be financed out of the organization's own funds. Moreover, profits were to be consolidated entirely through Sweden Post's account.

In 1984 Sweden Post's new business focus had resulted in a reorganization into two primary business areas: letters and parcels and giro and counter services. In 1989 the first real step toward business orientation was taken—namely, the organization of internal management around three long-term goals: customer satisfaction, financial performance, and satisfied personnel (see Figure 3). It was felt that such complementary goals were vital to the profitability of the organization. Sweden Post also restated its business concept: that is, it delivered messages, goods, and payments instead of letters, parcels, and brown giro envelopes. The above-mentioned long-term goals are discussed in detail below.

Figure 3
Sweden Post's Business Planning Concept

![Diagram of business planning concept]

Financial Performance

Customer Satisfaction

Satisfied Personnel
Customer Satisfaction. In order to take appropriate strategic action, Sweden Post implemented a Customer Satisfaction Index (CSI) mechanism. Sweden Post used the CSI to measure the extent to which the customer satisfaction goal is achieved. All Sweden Post business areas, regions, and sales areas measure customer satisfaction on the basis of the CSI. Results are reported as a weighted index figure that reflects customer satisfaction with Sweden Post's service and products. Included in the index are categories for reliability, speed of service at post offices, waiting times at post offices, and customer service, including handling of grievances. The survey is carried out among both private and business customers once every quarter. A CSI of 80 is considered satisfactory for a market-leading business. In 1993 the overall group's index was 73. The goal is to improve the index to at least 77 by 1997.

Financial Performance. The basic profitability goal is that Sweden Post must be able to finance essential investments and survive on its own resources. The long-term goal is to attain a profitability of at least 5 percent of operating revenues. The achieved productivity in 1993 was 3 percent, well above the minimum target of 2 percent. The profit margin for the same time period was 6.3 percent.

Satisfied Personnel. It goes without saying that profitability and customer satisfaction can only be sustained if employees are satisfied with their jobs, and Sweden Post has introduced surveys to gauge personnel attitudes toward their duties, management, and work environment. In 1993, 75 percent of those surveyed were content with their jobs, down from 82 percent for the previous year. This decline was attributed to the labor restructuring measures that were being undertaken.

With the reformulation of the organization's business concept, it was logical to broaden operations around the Post's core activities. But it was also logical to sell off unrelated operations, including the Sweden Post Bus Transport Service, Sweden Post Printing Service, and Sweden industries. In 1989-90 five strategic, logical, and clearly defined business areas were created and in 1992 they were set up as independent units, each with its own regions, production facilities, etc.

Step 2: Reorganization of Sweden Post into Five Business Areas

Structure

Sweden Post's reorganization into five main business areas (along with other units) is illustrated in Figure 4. Each business area is responsible for products, sales, production, and profitability within its
area of accountability. The reorganization was designed to introduce greater efficiency into the management of Sweden Post, with each business area operating as an independent profit center.

**Figure 4**

**Sweden Post’s Reorganized Structure**

![Diagram of Sweden Post's Reorganized Structure]

Table 3 summarizes revenues, profits, and average number of employees of each business area of the Sweden Post group in 1993.

### Table 3

**Revenues, Profits, and Employment of Sweden Post Business Areas**

<table>
<thead>
<tr>
<th>Business Area</th>
<th>Operating revenues (SEK millions)</th>
<th>Net profit (SEK millions)</th>
<th>Average number of employees</th>
<th>Net profit per employee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Postgirot</td>
<td>4,673</td>
<td>703</td>
<td>3,237</td>
<td>0.22</td>
</tr>
<tr>
<td>Sweden Post Banking and Counter Services</td>
<td>5,857</td>
<td>191</td>
<td>12,556</td>
<td>0.02</td>
</tr>
<tr>
<td>Sweden Post Letters</td>
<td>14,468</td>
<td>1,131</td>
<td>31,853</td>
<td>0.04</td>
</tr>
<tr>
<td>Sweden Post Parcels</td>
<td>2,489</td>
<td>-916</td>
<td>1,010</td>
<td>-0.91</td>
</tr>
<tr>
<td>Sweden Post International</td>
<td>1,606</td>
<td>28</td>
<td>706</td>
<td>0.04</td>
</tr>
<tr>
<td>Sweden Post Finance</td>
<td>312</td>
<td>14</td>
<td>15</td>
<td>18.73</td>
</tr>
<tr>
<td>Central Executive Functions and Subsidiaries</td>
<td>2,176</td>
<td>14</td>
<td>691</td>
<td>0.02</td>
</tr>
<tr>
<td>Other</td>
<td>673</td>
<td>-69</td>
<td>145</td>
<td>-</td>
</tr>
</tbody>
</table>

**Business Areas**

*Sweden Post Letters* delivers individual and mass-produced messages, newspapers, and periodicals throughout Sweden. Delivery is carried out via traditional mail services, electronic means (E-mail), or a combination of the two (E-post). The letters division also delivers light goods weighing up to 1 kg within the country. Sweden Post Letters is divided into 13 geographical regions, each with responsibility for sales, customer service, and production. The majority of the division's revenues (almost 90 percent) are derived from businesses and other organizations, with the remainder coming from private individuals.

*Sweden Post Parcels*, one of the country's three largest goods carriers, provides standardized, nationwide transport services for consignments up to 35 kg in weight. Letters and Parcels provide pickup and delivery services in Sweden from Sweden Post International.
Sweden Post International is responsible for the marketing of letters destined for delivery to a network of almost 200 countries outside Sweden's borders, as well as for customs, clearance, and distribution of all letters and parcels arriving in Sweden from abroad.

Postgirot provides efficient payment handling and information services supplemented by lending and investment services and enables its customers to earn a reasonable return on funds deposited in accounts. Postgirot also offers cash management services and in-payment and out-payment services through the network of post offices. In 1993, Postgirot booked 428 million payments totaling SKr 24 billion per day. The single most important factor affecting the division's financial performance is the interest rates that Postgirot receives on funds invested in the money market. Higher interest rates generate higher revenues. Revenues are also derived from transaction charges mainly to high volume customers.

Sweden Post Banking and Counter Services represents Sweden Post's retailing network and provides the organization's full range of services to individuals and small businesses through 2,000 service points. This division also conducts banking services on behalf of a state-owned bank, Nordbanken, with Sweden's households and small businesses as customers. During 1994 the post office network was to be organized into a system of about 1,200 owned full-service post offices including some 300 with expanded banking and business services, together with 800 contract post office facilities offering simple postal services in collaboration mainly with shops. In addition, Sweden Post has a number of subsidiaries (for example, a transport company, a real estate company, and consulting services).

Step 3: Transformation into a Commercial Corporation

Before discussing the reforms that led to the corporatization of Sweden Post, it would useful to review the basis for these reforms, namely, the reason why abolishing monopoly protection was important to the process.

Rationale for Removing Monopoly Protection

The majority of European countries still tend to argue that a basic postal monopoly is required for the public operator to fulfill its universal service obligations. This argument stems from the fact that since the postal company is obliged to deliver mail at a uniform tariff all over the country, delivery cannot be dictated by profitability alone. In other words, since the public company is obligated to deliver to areas where its operations might not be profitable, it can only make up these costs by being granted the entire market without competition from other companies. Given Sweden's large area and its thinly spread
population, the traditional arguments for retaining monopoly protection seem even more relevant.

However, Sweden Post, the state-owned postal operator, actively supported the removal of its own monopoly for several reasons:

- The legal text of the monopoly act had not been amended since 1947 and was out of date. New forms of communication and distribution of information through local and international courier services had in fact eroded the monopoly.

- The public's perception of Sweden Post as a state monopoly adversely influenced the Post's relations with its customers. This negative influence spilled over into other business areas, such as parcels and banking services, where the Post had no monopoly protection.

- In the early 1990s a private company began a letter delivery service in Stockholm. According to the letter of the Monopoly Law this firm was violating the law by entering the letter delivery market and should therefore be subject to public prosecution. However, the private company argued that its activity was legal because computer-generated letters, the company's main business, did not exist in 1947. The government therefore had to decide whether to retain a de facto monopoly or remove the monopoly altogether.

To facilitate a decision on the monopoly question the government hired an independent international consulting firm to conduct a systematic cost analysis of Sweden Post's regional and social responsibilities, primarily within Sweden Post's letters and postal giro business areas. The banking and counter service business area was not included in the analysis since it had no social responsibilities or monopoly protection. In the parcels business area competition for the market is intense and there is no monopoly protection. Table 4 outlines the social responsibilities of Sweden Post.

### Table 4

<table>
<thead>
<tr>
<th>Social responsibilities</th>
<th>Regional responsibilities in letter service</th>
<th>Regional responsibilities for payment services</th>
</tr>
</thead>
<tbody>
<tr>
<td>Newspapers</td>
<td>Daily service</td>
<td>Daily availability</td>
</tr>
<tr>
<td>Literature for the blind</td>
<td>Nationwide delivery</td>
<td>Nationwide service</td>
</tr>
<tr>
<td>Subsidies for delivery to disabled persons</td>
<td>Overnight service</td>
<td></td>
</tr>
<tr>
<td>National defense planning</td>
<td></td>
<td>95% delivery reliability</td>
</tr>
<tr>
<td>Letters sent to other Nordic countries</td>
<td>Uniform tariff</td>
<td></td>
</tr>
<tr>
<td>PFA (stamps division) move to Kiruna</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Letters sent by non-profit organizations</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Social Responsibilities in Letter Delivery. It was proposed that Sweden Post should cease to subsidize the letter service (that is, it should allow prices to increase so that they reflect full cost). Given the social necessity of providing these services, the alternative was that Sweden Post would receive full cost compensation, estimated at SKr 565 million for 1993. In the short run, it was recommended that a combination of temporary subsidies be paid by the relevant ministries and that rates be raised to market prices. In the long run, as a result of the repeal of the ordinance on the delivery of newspapers by the Post and the initiation of negotiations on market pricing, the price of newspaper delivery would eventually increase to a level that would cover Sweden Post's full costs. For the remaining social obligations, it was proposed that Sweden Post receive full cost compensation by the relevant agency or ministry and that this compensation be established under a purchasing agreement between the two parties for five-year periods. The subsidies proposed included an acceptable return on capital.

Regional Responsibilities for Letter Services. It was concluded that, on balance, the economic costs incurred as a result of these regional obligations (that is, having to deliver mail to far-flung, sparsely populated rural areas) were more than compensated by the high profit margin enjoyed by Sweden Post in other areas. Sweden Post enjoyed sufficient economies of scale and scope (as the only company able to deliver mail every weekday to every address in the country) to be able to recover its losses from loss-making regions. It was therefore recommended that Sweden Post receive no special compensation for its regional service responsibilities.

Regional Responsibilities for Payment Services. Since it is the state's responsibility to ensure that payment facilities exist throughout the country, it was recommended that the Post be compensated for the extra costs (calculated at SKr 300 million) of maintaining this service in localities with no banks. This compensation was further justified by the evolving trend in the postal and banking sector. It was anticipated that banks would continue to rationalize their network of branches, which would lead to an increase in post offices in rural areas. With declining volumes in postal transactions leading to a fall in revenues and with no apparent reduction in costs, this would imply increasing risks for the post office network.

Table 5 provides a breakdown of social responsibilities, as calculated by the independent consulting firm.³

In addition to the reasons cited above, the consultant's report substantiated the call to abolish monopoly protection for Sweden Post, although it argued for the continued universal service obligation, for

³ At the end of this process the government agreed to compensate Sweden Post for just Skr 53 million in 1994.
Redirecting Mail: Postal Sector Reform

which Sweden Post was to be adequately compensated for extraordinary costs through government transfers. It was decided that, in the longer term, if the market for postal services was characterized by increased competition, the government would consider amending the agreement on regional policy responsibilities and postal rates. All operators would also be obliged to finance the regional service obligations.

### Table 5
**Sweden Post Social Responsibilities**

<table>
<thead>
<tr>
<th>Category</th>
<th>Total compensation proposed for 1992 (Skm)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Newspapers and magazines (weekly)</td>
<td>113</td>
</tr>
<tr>
<td>Newspapers (Saturdays)</td>
<td>82</td>
</tr>
<tr>
<td>Trade press</td>
<td>188</td>
</tr>
<tr>
<td>Literature for the blind</td>
<td>27</td>
</tr>
<tr>
<td>Subsidies for delivery to disabled persons</td>
<td>19</td>
</tr>
<tr>
<td>National defense planning</td>
<td>23</td>
</tr>
<tr>
<td>Letters to other Nordic countries</td>
<td>97</td>
</tr>
<tr>
<td>PFA (stamps division) move to Kiruna</td>
<td>12</td>
</tr>
<tr>
<td>Letters sent by non-profit organizations</td>
<td>4</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>565</strong></td>
</tr>
</tbody>
</table>

The transformation of Sweden Post from a public service enterprise to a commercial corporation necessitated seven legislative changes. These legislative changes (postal reforms) are discussed below.

1. **Abolition of the Postal Monopoly**

Because of reasons cited earlier and the conclusions of the independent consultant’s report, the Government of Sweden recommended to the Riksdag that the postal letter monopoly be abolished effective January 1, 1993. The Riksdag accepted the recommendation.

2. **Introduction of the Postal Services Act**

Sweden never had a comprehensive postal law. The monopoly provisions were enacted in legal instruments of a lower status than an actual law and had not been amended since 1947. With the liberalization of the postal market, however, it became necessary to regulate some aspects of the market through a special law. In Sweden, as opposed to other countries, the new Postal Services Act, effective from March 1, 1994, is applicable not only to the public operator but also to the entire postal market including existing and potential private operators.

The Postal Act ensures the general public a right to a postal service according to law. The Act places the burden of ensuring a good postal service on the government. In turn, it gives the government complete freedom to contract with any company in the market that is
able to provide a postal service (thereby introducing some element of contestability). At present Sweden Post is the only operator qualified to serve the entire country. In 1996, when the first contract between Sweden Post and the government lapses, the government has the option to reassess the situation and appoint other operators as needed. The Act also defines the limits of the universal service (letters up to 2 kg and parcels up to 20 kg). The Act stipulates that the privilege of issuing stamps designed according to the UPU Convention would also be reserved for the operator appointed by the government. This, however, does not preclude other operators from issuing stamps with other designs, if they need to use this means of prepayment for the price of their services and for putting mailboxes in public places.

The Postal Services Act also provides for the formation of a supervisory body. Details of this regulatory body are discussed later in this case study.

3. Incorporation of Sweden Post into a Limited Liability Company

On March 1, 1994, Sweden Post was incorporated into a limited liability company under private law. First, the assets and liabilities of the business were transferred at book value to Postbolagen AB (formerly a subsidiary of the public service corporation), which was then renamed Posten AB. The assets and liabilities of Sweden Post's other divisions were also transferred to Posten AB. The depreciation schedule for all fixed assets was taken over by the new companies. Since conversion, all operations are conducted within a limited liability group whose parent company is Posten AB. At conversion, the pension liability of retirees and the earned pension entitlements of current employees over 65 were reported as a liability by the public service corporation. This liability of SKr 7,461 million was assumed by Posten AB. Consequently, the company's equity was reduced by this amount.

This transformation of Sweden Post from a commercial state enterprise to a limited liability company was a less radical step than the abolition of the monopoly and the change in legislation. The formal change in status was the culmination of a process initiated in the 1980s. During the process, Sweden Post was given more freedom with respect to setting prices and making investments. Eventually, Sweden Post was granted complete autonomy with regard to deciding and financing investments and was free to set prices subject to a limited price cap. As was mentioned earlier, Sweden Post bought off all of its assets from the state in the mid-1980s. It did this by making extra final depreciations, the amount of which was delivered to the state, thereby strengthening the state budget.

All these factors facilitated the final move to Sweden Post's current status. The decision of Sweden Post's owner (the Swedish Govern-
ment) to change the Post's organizational form recognized that all the markets in which Sweden Post had a presence were competitive in nature. All parties concerned felt that Sweden Post should operate under conditions that were equal in all respects to those of its competitors. Thus, the incorporation of Sweden Post was motivated mainly to create a level playing field in the postal market. The Post is now subject to the same opportunities and restraints as its competitors (such as negotiating labor contracts with employees, forming alliances, and paying corporate tax, VAT, pensions, etc.). In addition, Sweden Post's major customers are also limited liability companies that prefer to deal with another limited company as opposed to a government enterprise whose decisions might be influenced by politics.

A major point is that there has been no privatization in the strictest sense of the word. Sweden Post is incorporated according to the normal law on limited companies. The state has retained all the shares in the company. However, nothing prevents the government from selling shares at a later stage, if there is a political majority for such a move. As the sole owner, the government appoints the external Board of Sweden Post, and the Board in turn appoints the President/Chief Executive Officer.

Because of the incorporation, specific contracts were drawn up between Sweden Post and the government specifying the duties and obligations of each party. The first agreement was for less than three years (i.e., to the end of 1996). The financial requirement imposed on the Post by the government in its capacity as the owner is that the business must operate commercially and generate a return on equity comparable to other major, well-managed companies in similar industries. The government has set the long-term return on equity capital at a standard rate of 11 to 13 percent after tax. Sweden Post consistently exceeded this target for the six years preceding corporatization. Profit margins after adjusting for all financial items have consistently been over 5 percent. As owner of Sweden Post, the state has also specified that the equity/assets ratio be at about 15 percent.

As regards the issue of pension funds, a corporatized firm is expected to pay a pension to its retirees and to maintain a fund for this purpose. The issue of financing pension commitments proved to be a major problem. In the past, Sweden Post, like all other government agencies, had not set up a fund for future pension commitments but had only booked pensions paid to employees that were actually retired. With the incorporation of the Post, it was expected that the government would assume this responsibility, but the government was not willing, and Sweden Post had to undertake full liability for both historical and current pension commitments. Consequently, the Post's debt/equity ratio rose rapidly. However, in return for assuming this liability, Sweden Post will not
be required to pay any dividends on its shares (all of which are
government owned) until a sufficient capital base has been built
up. Dividends will not be paid until the equity/assets ratio is deemed
satisfactory.

4. Agreements between the Government and Sweden Post

A specific contract was drawn up between the Post and the govern-
ment, which, among other items, specified the following:

- The Post would provide universal (nationwide) mail service
  (including delivery of newspapers) at a uniform and reason-
able price without compensation from the government. The
  universal service is defined by the Postal Act as concerning
  letters up to 2 kg and parcels up to 20 kg.

- The Post would provide a nationwide counter service. Some
  compensation would be paid for retaining counter services
  in small localities where other mechanisms for payment
  transactions are not available. In 1993, Sweden Post was
  remunerated in the amount of SKr 300 million for maintain-
ing a nationwide counter service; it received the same com-
pensation in 1994.

- The government undertook to compensate Sweden Post
  for its other social commitments such as free delivery of
  literature to the blind, services for the elderly and disabled,
  and national defense planning. In 1993 these costs were
  estimated at Skr 580 million, but the actual amount paid in
  1994 was Skr 53 million. This meant mainly that the gov-
  ernment expected Sweden Post to be able to cover the deficit
  in the delivery of newspapers and periodicals from the sur-
 plus of other services.

- The contract also includes further specifications about the
  delivery, the quality of service, and the mechanism for pric-
ing of various categories of mail items. In particular, there is
  a price cap on the domestic letter rate for private individuals
  of up to 500 g (i.e., the price may be increased by a maxi-
mum of the average change in the net price index over a
three-year period).

5. Application of the Value Added Tax (VAT)

As per the Sixth European Community VAT Directive, “public postal
services” are exempt from VAT within the EU. Given the recent re-
forms in the Swedish postal sector whereby all private operators op-
erating in Sweden must pay VAT, it would be noncompetitive to exempt
the public operator from paying this tax. As a consequence, Sweden
Post has been subject to VAT since March 1, 1994.
Since the price increase was passed on to the customer, Swedish Post had expected a public outcry. However, since the majority of the population was accustomed to paying VAT on most goods and services, they found the policy acceptable. (And since most major customers were able to continue to deduct the VAT for postal services, as for other goods and services, they did not have to pay a higher price.) To mitigate the effects of the VAT on private individuals and non-profit-making organizations, the rate of VAT was initially limited to 12 percent, but was later increased to 25 percent.

From Sweden Post's perspective, an advantage of VAT on mail conveyance is that it gives Sweden Post the opportunity to contract out various tasks and to save money, rather than being forced to perform all tasks in-house because of the tax advantage. This trend has been noted in the post office network business area, where reliance on contract post office facilities in shops or banks is increasing, as a means of limiting to some extent costs in areas where post offices are not economically viable.

6. Competition in Payments to and from the Government

Postgirot was transformed into a bank as part of Sweden Post's corporatization process. On July 1, 1994, Postgirot's exclusive right to government payments was terminated. Parliament's intent was to safeguard continued competition in the payment transmission market to maintain Sweden's highly efficient payment handling system. In the past, Postgirot enjoyed a favored position with regard to these payments (taxes, VAT, pensions, etc.) and the interest income from this money had contributed to the maintenance of a dense Post Office network. These privileges have now been removed and all banks and other financial institutions are allowed to compete for this business.

In spite of these changes, Postgirot continues to be the primary channel through which government payments are handled. To enable Postgirot to survive in the payment transmission market, it has been granted extended powers. Postgirot can now operate almost as a commercial bank. It can provide loans and pay interest to attract these loans for 360 days to both private individuals and corporate bodies. In the past such loans could be extended only 30 days. The Postgirot Bank is also entitled to supply checks and credit cards and to undertake currency trading.

However, Postgirot has not been permitted to develop a banking business that also extends into savings. A ceiling has been imposed on the total volume of interest-bearing deposits and loans. Moreover, the business area may not own securities and investment companies.

---

4 VAT on most goods and Services in Sweden is 12 to 25 percent.
7. New Legal Structure

Corporatization has required the introduction of a new legal structure for Sweden Post. The parent company, which includes the Chief Executive Officer, the Executive Staffs, and Sweden Post Finance, has four subsidiary corporate groups: Posten Distribution AB, Postgirot Bank, Postbolagen AB, and Postfastigheter AB (see Figure 5).

Figure 5
Sweden Post's Legal Structure, from March 1, 1994

General Regulatory Structure

Any reform process requires legislative amendments. These amendments are implemented by an overseeing/regulatory body. To understand why the postal reform process has been successful in Sweden, it is necessary to look at the regulatory structure prevalent in the country. Sweden is ruled by a parliamentary government, which, in keeping with the principles of this form of government, is responsible to the Riksdag for its actions. The Constitution stipulates that the government act collectively on all matters of policy. The government is divided into various ministries, covering different spheres of activity. These ministries are responsible for preparing business to be submitted to the government for its consideration. Once a decision is taken, the relevant ministry is responsible for implementing the decision.

Ministries do not interfere with the government's day-to-day administrative work, which is carried out by legally autonomous bodies called Boards or Agencies. The heads of these administrative bodies have no political functions and their appointments and tenures are independent of changes in the government. Thus the de jure autonomy of the Boards appears in two ways:
First, they apply laws and make decisions on the rights and duties of the concerned bodies without being influenced by the government.

Second, they do not receive orders from individual ministers but from the government as a whole.

This regulatory structure is unique to Sweden and has much to do with the country's success with postal reforms.

**New Regulatory Agency**

The Postal Services Act lays the basis for a supervisory authority responsible for monitoring the application of the Act and for intervening in case of anomalies. This regulatory body, which is currently functional, is the National Swedish Post and Telecom Agency, a section of the Ministry of Transport and Communications. *It should be noted that the functions of ownership, operation, and regulation have been completely separated.* Operators that intend to service the postal market are obliged to register with the Agency, although they do not require any form of licensing or formal authorization. The Agency is charged with promoting competitive neutrality in the postal services market and also undertakes certain tasks of a public authority nature for both postal operators (such as the opening of undeliverable letters) and the government (acting as the signatory of international intergovernmental treaties in the postal field).

**Managerial Freedom and Pricing**

Sweden Post is free to enter joint ventures and form subsidiaries. Its international division participates in a joint venture called GDNet with four other postal administrations and TNT International. Sweden Post is not required to maintain a specific number of retail postal outlets and has the freedom to close outlets in remote areas. In turn, the Post has adopted a policy of franchising post offices within the framework of the agreement with the government. Posten AB has full autonomy in setting prices for all of its products. The standard domestic letter is subject to a price cap equal to the inflation rate. The parent company is also free to acquire and invest in other companies.

**Labor Restructuring**

In recent years, decreasing volumes of transactions at postal counters (due to a lower rate of increase in letter volumes as well as a steady decline in counter transactions), better working procedures in general, increased mechanization of mail processing, and a decline in personnel absences due to illness have all contributed to the pressure for staff reductions. Figure 6 shows the drop in number of employees during the period 1990-93.
Case Study 3
Sweden Post: Removal of Monopoly Protection

Figure 6
Sweden Post Employees, 1990-93

Over the previous five years, staff has been rationalized by 12,000 employees. In 1993 alone, the number of employees fell by some 7,000, of which 1,850 were declared redundant. The number of employees on December 31, 1993 was 55,385, of which 46 percent were men. The average number of full-year employees during 1993 was 50,123. Posten AB worked closely with the three labor unions during this retrenchment process. Table 6 shows the reduction in employees by personnel category.

Table 6
Number of Employees by Personnel Category

<table>
<thead>
<tr>
<th>Category</th>
<th>As of Jan. 1, 1994</th>
<th>Reduction since Jan. 1, 1994 (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mail handling</td>
<td>26,974</td>
<td>-11.6</td>
</tr>
<tr>
<td>Counter personnel</td>
<td>10,959</td>
<td>-15.3</td>
</tr>
<tr>
<td>Administration and office</td>
<td>7,801</td>
<td>-10.2</td>
</tr>
<tr>
<td>Rural letter carriers</td>
<td>3,589</td>
<td>-7.0</td>
</tr>
<tr>
<td>Cleaning staff</td>
<td>950</td>
<td>-22.4</td>
</tr>
<tr>
<td>Computer and other technology</td>
<td>1,045</td>
<td>-3.8</td>
</tr>
<tr>
<td>Miscellaneous (including</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Public Service Corp.)</td>
<td>95</td>
<td>-21.5</td>
</tr>
<tr>
<td>Postbolagen AB</td>
<td>3,710</td>
<td>-2.1</td>
</tr>
<tr>
<td>TOTAL</td>
<td>55,123</td>
<td>-11.3</td>
</tr>
</tbody>
</table>

In the wake of the decreased demand for labor, a freeze on external recruitment has been implemented. Together with the personnel reductions, this has led to a compressed age structure with a lower proportion of young employees. According to Swedish law, in case of layoffs the last to be employed have to leave first, unless it is otherwise agreed upon with the union. The average age of employees by 1993 was 41, up from 39 a year previously. Employees in
Posten AB can be laid off when there is a shortage of work. However, under the public corporation employment law, approximately 3,000 employees are guaranteed employment if their positions are made redundant. The wage structure of Posten AB is similar to that of comparable industries. Minimum pay for an 18-year-old is SKr 9,600 (US$1,289).

**Employee Morale**

Given that employee satisfaction is one of Sweden Post's long-term goals, the group conducts surveys to measure the proportion of employees who are satisfied with their job. In 1993, 75 percent of those surveyed expressed satisfaction (down from 84 percent in the previous year). This decline is attributable to the major rationalization measures currently under way in the organization as well as to uncertainty about the future.

Since the layoffs coincided with the corporatization process, the belief among staff and in political circles was that corporatization was responsible for the employment reduction. This belief generated considerable controversy and disfavor. As a result, corporatization eventually passed parliamentary approval with a very slim margin.

**Future Policy**

Sweden Post is geographically the country's most highly decentralized business. As a result, in many localities it is an important employer. To minimize backlash against layoffs, a policy on social responsibility during restructuring has been drawn up. A committee is to examine the necessity of layoffs before they are implemented. A common approach has been established with employee unions on how to deal with personnel reductions. In addition, guidelines for handling severance pay have been developed.

**Innovations**

It should be noted that, owing to the threat of competition, Sweden Post has diversified into new markets and has launched new products. While Sweden Post has a dominant position in the addressed letter market, there is a new focus on electronic mail messaging. PostNet, the division's integrated electronic messaging service, offers a variety of products: (1) E-mail (transmission of messages via computer networks); (2) E-post (a system which permits transfer of both physical and electronic mail by accessing information posted directly from a computer and distributing it in the form of letters); (3) EDI (electronic data interchange, a system for sending electronic business documents between computers); (4) E-direct (a service that provides access to a wide spectrum of information services from stock market quotes to computer-aided shopping; and (5) E-fax (various
forms of value-enhancing fax services, such as fax broadcast, which distributes faxes to a large number of receivers). This mix of traditional mail service together with state-of-the-art electronic messaging options represents one of the most up-to-date communication systems offered by any postal system in the world.

Sweden Post is in the process of development, renewal, and restructuring in order to meet the new conditions created by deregulation, new technology, and internationalization. In 1993 Sweden Post was able to exceed the return on capital requirement set by the state for the sixth year in a row and achieved a net profit of SKr 1,363 million. Much credit for achieving this level of profitability goes to improved productivity, which rose by 3 percent in 1993, corresponding to an improvement in profit of about SKr 600 million.

The company continues to direct its resources at developing new services and products and measures up well to other international postal administrations. In early 1994 one of the company's new products, E-post, received the "Innovator of the Year" award at an international industrial fair.

Several lessons emerge from Sweden Post's corporatization. The most important of these are discussed in this section.

Sweden is one of the few countries that has been successful in isolating the social obligations of its postal administration, identifying and attaching costs to these responsibilities, and aiming at making explicit transfer payments to support these activities. In most other countries, subsidies are granted to the postal sector as a whole, which results in the subsidization of business users. But in Sweden the compensation is more targeted.

Contrary to the prevailing arguments for maintaining monopoly protection for postal services, Sweden Post has explicitly stated that it does not require monopoly protection to perform the universal service obligation. That Sweden Post was willing to lobby the removal of its statutory monopoly power on letter mail suggests that the benefits of a competitive environment outweigh the minimal benefit that monopoly accords. In fact, the monopoly protection was harmful to Sweden Post's public image, and this negative perception spilled over into other sectors in which the Post did not have monopoly protection. The freedoms (such as the option to form joint ventures) that come with a competitive environment have been welcomed by Sweden Post.

Despite having to maintain universal service coverage, Sweden Post hoped to remain profitable without monopoly protection because profits from its core businesses would more than compensate for its
loss-making units. In general, Sweden Post operates in a number of business areas and regions including the following:

- Core business areas that are market driven and operate under commercial principles. In these business areas the Post is able to recover full costs plus a profit margin in all regions.
- Non-core business areas, where the Post has universal service obligations. In these areas and regions there is less than full cost recovery.
- Areas of social obligation where the Post has zero cost recovery.

However, Sweden Post has been able to support its profitability by receiving compensation for the cost of some of its social commitments. Sweden Post's loss-making business areas and regions are being cross-subsidized by the Post's profit-making core businesses.

Sweden Post has been quick to adopt technology in the form of innovative products. The Post is a leading producer of hybrid and fully electronic services with approximately 10 percent of its mail transactions transmitted in electronic form. Competition from other carriers will undoubtedly prompt postal administrations to innovate in order to survive. In this regard, Sweden Post is at the forefront.
Australia Post: A Corporatization Success

Australia Post is a government business enterprise (GBE) owned by the Commonwealth of Australia. Serving approximately 18 million Australians, Australia Post handled almost 4 billion mail items in 1994-95, delivering to some 7.7 million household and business addresses across the continent. The Post, which is headquartered in Melbourne, has five state profit centers: Sydney, Melbourne, Adelaide, Brisbane, and Perth. With a retail network of some 4,300 outlets, the Post provides the 800,000 customers who visit it daily with easy access to postal, financial, and other complementary services. Australia's population is highly dispersed. About 99 percent of the country's land area of 7.7 million sq km is considered rural or remote and these rural or remote areas are home to 29 percent of the population. Nevertheless, 98 percent of the population receives five letter deliveries a week.

With annual revenues of almost A$2.8 billion, an asset base valued at over A$2 billion, and profits of A$330 million in 1994-95, Australia Post is among the few profitable postal enterprises in the world. However, this was not always the case. Between 1960 and 1975, Australia Post consistently incurred losses. As a department of the state, in the past 20 years it was forced to charge low tariffs. However, Australia Post went through three distinct sets of reforms: in 1975, 1989, and 1994.

Since its corporatization in 1989, Australia Post has upgraded its performance and its image. The customer focus is stronger; industrial relations have improved; innovative products and services are priorities; and investment in the business is at a record level. Today Australia Post operates commercially, is subject to all taxes, and pays commercial dividends to its owner, the government. The many initia-

---

1 This case study is based on information provided by Ken McKeown of Australia Post.
Redirecting Mail: Postal Sector Reform

tives that the Post implemented over the past few years—workplace reform, customer service focus, standard letter price stability, and overhead reductions—are now paying dividends. Revenue in 1994-95 was up 8.3 percent from the previous year, the operating profit was up 15 percent, the return on assets was up 1.2 percent, and the dividend paid was 33 percent higher than that paid in the previous year.

By harnessing the cooperation of its 37,500 employees in 1995 (down from 38,600 in 1989), the management of Australia Post has turned the Post into one of the country's top performing businesses. Management, staff, and unions now share one goal: the provision of high quality customer service. To this end the Post has initiated innovative training, quality service, and best practices programs. Through internal benchmarking, the enterprise has pinpointed the areas where best practices exist and has brought such practices to all work centers. Indeed, international benchmarking confirms that Australia Post performs as well as, if not better than, most overseas postal organizations. In sum, the benefits have been twofold: the Post continues to meet its customers' changing expectations, and the business continues to prosper.

The obvious question for those postal administrations that have been plagued by problems similar to those faced by Australia Post is: “What has Australia Post done to turn around its performance so dramatically?” These postal administrations may well be interested in using Australia Post's experience as a blueprint for reforming their own postal sectors. The present case study describes the changes undergone by Australia Post, reviewing the reform process and highlighting the specific results.

The Reform Process

Three distinct and deliberate sets of reforms, introduced within Australia Post in 1975, 1989, and 1994, have contributed to the present success of this enterprise. A historical perspective of this reform process outlines the drivers of each of these stages of reform and the changes introduced by the reforms.

The First Stage: 1975

Drivers of Reform

The Australian postal service's performance in the 1960s and early 1970s was cause for concern. In the decade preceding the creation of a separate postal organization in 1975, postal operations had been making a loss every year, with losses ranging from 5 percent to 20 percent of revenue. Figure 1 shows operating profit levels from 1964 to 1974.
Over the same period, mail service performance (on-time delivery) on an average national basis had fluctuated around 93 percent. However, performance in New South Wales, the largest state, which accounts for 35 to 40 percent of total mail, had never exceeded 90 percent, and, for a number of years, service levels had fluctuated between 75 and 85 percent. The poor performance in New South Wales had been accompanied by considerable time lost through industrial disputes. The Vernon Report, a report of the Commission of Inquiry into the Australian Post Office, described the situation as follows:

The unsatisfactory industrial climate at this [Sydney mail] exchange, evidenced by the number of stoppages and black bans, the frequency of meetings between management and staff and the difficulties of making changes in procedures, is unique within the A.P.O. service. The Commission has no ready solutions to propose. Improvement in the industrial climate at the Sydney exchange will be one of the major tasks for the new management of the postal service as it has been for A.P.O. for many years.... The achievement of better industrial relations at the Sydney mail exchange appears as one of the problems which management and the staff organizations will have to pursue assiduously in the public interest of maintaining a reliable and efficient mail service.

Tariffs and productivity improvements did not increase as rapidly as expenses, which escalated under the pressure of increasing salary and wage rates. The losses, which averaged about $A20 million per year, severely limited the capital expenditure available for modernizing the service. This effectively meant that telecommunications was subsidizing the postal service. The Vernon Report went on to state the following:

Postal and telecommunications services, which are examined separately [in the report] show widely differing characteristics with respect to capital investments, growth rates, and profitability. In the profit and loss sense, postal services have been a problem area within the A.P.O. for a number of years. Consistent losses have largely offset profits derived from telecommunications services.
No government had the will to raise tariffs by the amount necessary to establish a profitable base. For such a move to occur, it would have to come from a non-governmental agency, since politicians were not willing to risk the public furor over such a price hike. This factor, together with the poor performance of the postal sector over a sustained period of time, was the primary reason for reform.

Reforms of 1975

The reforms of 1975 resulted in far-reaching structural changes. The main components of these reforms were as follows:

- The postal service was separated from the affairs of the general government by the placement of postal matters at arm's length from the day-to-day business of government. For this, the postal and telecommunications operations role of the Postmaster General's Department ceased and the functions were reallocated. Three separate commissions were set up: the Australian Postal Commission, the Australian Telecommunications Commission, and the Overseas Telecommunications Commission. Operations of the postal services thus passed from a department of the state to a statutory corporation.

- The mission of the newly created postal entity was clarified through legislative provisions. The newly formed Commission was given explicit postal functions; was required to recover all costs from postal charges; and was obligated to provide at least half of its annual capital expenditure requirement from its internally generated funds. As a result, revenue and cost were closely aligned and deficit financing or cross-subsidization from other sources (e.g., from telecommunications, as in the few years before reform) was no longer an available option. This was an important step forward in establishing an organization that could develop, albeit gradually, its own commercial culture and take charge of its own destiny.

- The tariff on a standard article was raised from 10 cents to 18 cents. This substantial raise in tariffs was instrumental in driving Australia Post toward profitability, although mail growth suffered for three years.

- Social obligations were explicitly, if only broadly, stated in legislation.

In brief, the 1975 reforms provided the postal service with a robust structure, a clearer mission, industrial separation from the public service work force, and proper and effective financial discipline, all of which prepared Australia Post for its transition to commercial operation.
The Second Stage: 1989

Drivers of Reform

In contrast to the previous reform initiatives, the driving force in 1989 was national economic policy. Since the mid-1980s the Government of Australia had embarked on a number of reform initiatives, including the reduction of tariffs and other forms of protection and the introduction of competition in aviation and telecommunications. These initiatives came to be referred to as the microeconomic reform program and they were aimed at restructuring key industries in the Australian economy and improving their efficiency. The focus of microeconomic reform was on the structural and institutional factors that inhibited efficient performance. The changes to be instituted included corporatization, the abolition or reduction of restrictions on competition, and privatization.

Microeconomic reform in its broadest sense was about making markets work better, improving incentives, and enhancing the effectiveness of government operations. The process was a comprehensive program that involved removing those market impediments that prevented resources from being used in the most efficient manner, including restrictions on competition (whether domestic or from imports), rigidities in work organization, or a tax system that distorted incentives.

Another driving force in this period was the flat performance and low profitability of the sector. The period from 1983 to 1986 was one of relatively unremarkable postal performance: on-time delivery fell significantly in 1984-85 and remained at a low level; the number of days lost as a consequence of industrial disputes rose significantly; and labor productivity remained subdued. Moreover, the government was increasingly concerned by the low returns on assets that the Postal Commission achieved from 1975 to 1989, since the government had made a commitment to increase the efficiency of GBEs.

The continuation of day-to-day controls by the government became an increasing source of frustration for the Commission's managers. For example, a number of government departments and agencies had to approve the disposal of property and contract conditions for building works. Frequent delays and conflicts with staff who did not have accountability for the business sapped management's energy and morale.

With these concerns (as well as others) in mind, the Australian Government in 1988 announced a program of reform for the major business organizations in the transport and communications sector under federal jurisdiction. The major thrusts of the reform were the following:
Redirecting Mail: Postal Sector Reform

- New emphasis would be placed on planning and accountability mechanisms
- The board and management of Australia Post would be left largely free of government day-to-day controls
- The playing field would be made level by the removal of concessions enjoyed by the Post, such as exemptions from all taxes and state laws
- Non-commercial costs including community service obligations would be made transparent.

Reforms of 1989

The reforms introduced in 1989 changed the nature of the Postal Commission and resulted in changes that would affect the enterprise for years to come. Clearly, these reforms built on the achievements, principles, and institutional changes introduced in 1975. The major changes introduced are listed below:

- The Australian Postal Corporation Act of 1989 legislated the corporatization of Australia Post. As a result, a Postal Corporation was created to replace the Postal Commission. The dominant intent of corporatization was to give Australia Post a commercial character. For this purpose, Australia Post was required to conduct its operations in accordance with sound commercial practices, to achieve a reasonable rate of return on assets, and to pay a reasonable dividend to the owner government. Consequently, a board of directors, selected for their commercial skills and experience, was appointed, executives drawn from the private sector were recruited to top management, and a commercial financial structure was put in place.

- A set of financial and other performance targets was agreed upon with the government over a three-year planning period. These targets were to reflect a gradual improvement in performance, thus allowing for the continuing impact of past decisions. Measurements of performance against these targets were to be published every year in Australia Post's Annual Report.

- Transparency in planning, the calculation of costs, and the delivery of both community service obligations (CSOs) and specific general government obligations was embedded in the system. Through the corporate planning process, agreement was to be reached between Australia Post and the minister responsible for the Post on the strategies and policies regarding the cost and delivery of CSOs. Plans for meeting or reducing these costs were agreed upon with the
government. In turn, the government's day-to-day controls were lifted.

- The organization was to be subject to the laws of the Australian states as well as federal laws, including payment of all taxes.
- Detailed statutory provisions governing employment conditions were replaced by provisions in various union awards. Senior staff positions were to be spilled, and then filled competitively under contracts that excluded tenure of public sector employment. Remuneration for these positions was to be set by reference to the market and not pegged to the salaries of similar positions in other public sector jobs.

In sum, the 1989 reforms gave the enterprise a positive commercial orientation and put further distance between the enterprise and the owner government. The reforms strengthened the enterprise's organizational and financial structure by giving it a board, as is the case with other commercial enterprises, and also restructured capital in its balance sheet. These reforms also opened the door to the appointment of executives from the private sector, and redefined the relationship between Australia Post and the government. Having completed the internal commercialization of Australia Post, the 1989 reforms cleared the way for future reforms to focus on market regulation and competition.

It must be pointed out, however, that the regulatory framework, the scope of the letter monopoly, and the barriers around the reserved services were left unaltered. Moreover, the corporation was still subject to the following three major strategic controls:

- It had to submit all proposed price raises on all monopoly letters to the Prices Surveillance Authority, a body set up to oversee pricing in key Australian industries
- It had to seek government approval to borrow
- It had to coordinate its industrial relations policies with those of the government.

Australia Post understood and accepted the need for pricing regulation of products under a statutory monopoly and the national policy requirements under a central wage fixation system.

**The Third Stage**

*Drivers of Reform*

The postal reforms introduced through the Australian Postal Corporation Amendment Act of 1994 were a consequence of a report of the *Industry Commission on Mail, Courier and Parcel Services*. The main recommendations of this inquiry were the following:
• The letter monopoly provided by legislation to Australia Post would be terminated as of January 1, 1995. The social objective of a universal service with a uniform price for standard letters within Australia would be replaced by a maximum affordable charge regime for domestic standard letters. Under the new regime Australia Post would be allowed to charge up to a certain maximum (initially, the current 45 cent rate would be the maximum charge), while competitors would be free to compete as they wished.

• If the above option was not acceptable to the government, then the minimum amount that other providers must charge to carry a letter would be reduced from ten times the standard rate to A$1.20. This amount would be reduced by ten cents each year thereafter for five years. A further review of the letter monopoly would be undertaken in 1997.

• The weight limit for exceptions to reserved services would be reduced from 500 g to 250 g.

• The operation of document exchanges, the transfer of mail within an organization, and advertising mail would be removed from monopoly protection.

• Australia Post's exclusive right to carry letters between Australia and locations outside of Australia would be withdrawn.

• Interconnection with Australia Post's network would be allowed, under fair terms and conditions, at any point between sender and receiver.

The recommendations of the Industry Commission were not adopted in full by the government, but most certainly had some influence on the outcome. The Minister for Communications at that time stated that the government had rejected the Industry Commission's radical proposals because they might have destroyed Australia Post's viability and might not have ensured continued delivery of the community service obligations. The Industry Commission's failure to estimate with confidence the amount of monopoly protection necessary to ensure the viability of Australia Post while community service obligations continue to be internally funded was considered a major reason for the government's decision to take a moderate first step in 1994 and to review competitive arrangements in 1996-97.

The National Competition Policy Review (NCPR) was established in 1993 to improve Australia's international competitiveness through a review of institutional impediments to competition at all levels of government. Microeconomic reform had until 1992 been championed by the Commonwealth Government, and had concentrated on areas within its responsibility under the Australian Constitution. Large sectors of the Australian economy, including roads, gas, water, power, and rail—all beyond the direct power of the Commonwealth—had
escaped reform. By 1993, national reform seemed to have come to a standstill.

To reinvigorate the reform program and to make it national in scope, the Commonwealth commissioned NCPR in 1992. NCPR's recommendations were debated for well over a year and initially met with opposition from the states and the territories. In 1995, after protracted negotiations and a report on the benefits of reform, a national reform program was finally agreed upon and launched. This program now provides for a timetable, for set processes, and for agreed principles to reform competition in Australia. The program also incorporates powerful incentives for the states and territories to comply and is expected to guide and stimulate reform in Australia in the next few years.

Reforms of 1994

The Australian Postal Corporation Act of 1994 put into place the following decisions of the government:

- The monopoly protection afforded to Australia Post reduced the weight barrier from 500 g to 250 g, and the price barrier from ten times the standard rate (i.e., A$4.50) to A$1.20.
- Carriage of letters within document exchanges and of mail internal to organizations was excepted from the letter monopoly.
- Outbound international letter traffic was excepted from the letter monopoly, but the delivery in Australia of inbound international letters continues to be reserved for Australia Post.
- A limited interconnection regime for bulk presorted mail was introduced for delivery within the same state.
- The remaining monopoly protection given to Australia Post would be reviewed in 1996-97.

A succinct summing up of the results of the reforms was given in Standard and Poor's Assessment Report, which in 1994 established an AAA domestic rating for Australia Post. The report states:

Australia Post's financial performance has improved markedly over the past few years, with its profitability increasing threefold over the four years to 1992-93... This improving performance has been underpinned by the steady natural growth of the core business, strengthened cost control, [and] the introduction of advanced network automation and favorable labor relations, as illustrated by the recent record of labor/management agreements and low incidence of industrial disputes.

A useful evaluation of Australia Post's performance since the 1989 reforms can be made under the following main categories: financial performance, labor performance, customer orientation, products, and service.
Financial Performance

Australia Post's financial performance since the 1989 reforms has been nothing short of spectacular. In all categories: revenues, profits, return on assets, mail volumes, revenue per employee, dividends paid, and investments, Australia Post has been achieving steady improvement. Annual profits have grown from A$46.2 million in 1989 to A$331.6 million in 1995. From paying no dividends in 1989 to its owner, the government, the Post paid out an annual dividend of A$120 million in 1995. Returns on assets have increased fivefold, from 3 percent to above 15 percent within the same period. In spite of increased competition, mail volumes have increased from about 3 billion articles in 1989 to some 4 billion articles in 1995. Figure 2 illustrates these trends.

Australia Post's active support for local industry has resulted in some 90 percent of the corporation's capital investment expenditure of A$884 million being invested in Australian industry since 1989. A further A$270 million is targeted for investment over the next year.

Labor Performance

The chief areas of labor performance that were affected by the reforms were labor productivity, industrial disputes, and the new emphasis on work force participation. Labor productivity gains rose to a record 6.4 percent in 1995, after sizable annual increases since 1991 (see Figure 3).

Where industrial disputes are concerned, the relationship between Australia Post and its unions in 1989 was strained and adversarial. As much as an hour per employee was lost to postal disputes in 1989, about average for Australia Post in the 1980s. In 1995 the time lost to postal disputes had dropped to an almost negligible level (see Figure 4).

These improved relations among Australia Post's management, employees, and unions, which have become open and constructive, are among the most important changes to the Post over the past six years.

The foundation for the new emphasis on work force participation came from the joint statement of understanding signed by Australia Post and its major unions in 1989. The statement emphasizes the importance of worker participation, commits management and unions to consultation, and encourages the development of a cohesive team. Thus, all staff now participate in the decisions that affect their workplace. In October 1992 Australia Post and its unions signed the first Enterprise Agreement with remunerations based on productivity improvements, now recognized as a leading example of enterprise bargaining and industrial relations.
Figure 2
Financial Performance of Australia Post, 1991-95
Customer Orientation

The principal areas to be significantly improved were: customer service; customer satisfaction; links with customers and customer interaction; and commitment to best practices.

As meeting or exceeding customers’ expectations of service has been the focus of Australia Post’s decisions and efforts since its conversion to GBE in 1989, customers today are benefiting from a range of improvements and innovations in the area of customer service. In customer satisfaction as well, consistent and sustained increases have
been indicated by both business customer and private customer feedback (see Figure 5).

**Figure 5**
**Customer Feedback on Australia Post, 1992 and 1995**

Another principal goal of Australia Post has been to establish closer links with customers and improve interaction with customers. In 1989 the Post was largely focused inward on its operations. The handling of complaints and customer feedback was sporadic, and there appeared to be no underlying commitment to speedy and effective resolution of problems. Linkage with customers was on an ad hoc basis.

To achieve its goal, Australia Post established the Postal Services Consultative Council. This body is made up of Australia Post’s customers, union members, and postal licensees and provides the enterprise with vital feedback on services and customer needs. Some 7,500 retail staff members have been further trained in improved cus-
customer contact skills and in techniques for handling complaints. In addition, when inquiries or other concerns come in to the Post, they are handled at the location at which they were received.

The Post’s fourth major goal in the area of customer orientation was to establish a widespread commitment to best practices. In 1989, “best practices” was an abstract concept understood by few employees of Australia Post.

A move in the direction of this goal was the Enterprise Agreement of 1992, which had as a fundamental objective the achievement of world-best practices. The agreement also included an important participative quality accreditation program known as Quality Service One (QS1). The program emphasized an improved internal focus on quality and provided a structured approach to assessing quality. By 1994 about 95 percent of Australia Post’s work centers had met or exceeded the standards of the QS1 program, and the need to provide quality service to customers is now high in the consciousness of all Australia Post staff. A follow-up program, QS2, has been launched.

Products

In this area Australia Post has concentrated on developing innovative and customer-focused products and services as well as on increasing financial transactions through a broader range of services. The Post has continued to introduce innovations to meet the changing needs of postal users. New products such as EDIPost, peel-and-stick stamps, extended financial and bill payment services, and FaxPost have been added and expanded. EDIPost is the Post’s hybrid mail service which enables customers to lodge data electronically for printing, enveloping, and delivery by the enterprise. It is an efficient and sophisticated means of handling bulk mail lodgments. Other products continue to be added.

Regarding a broader range of services for financial transactions, customers in 1989 could pay a limited number of accounts and conduct banking transactions with the Commonwealth Bank through the national retail network. Australia Post handled some 45 million of these “agency” transactions. After 1989, volume increased annually for the next five years. In 1995 the corporation handled some 100 million agency transactions, which reflects the customer preference for these easy-to-use services. Figure 6 shows revenues from these transactions.

Australia Post has established its single largest electronic counter network, Electronic Point of Sale (EPOS), which provides cash and stock control and improves the speed and efficiency of customer transactions. EPOS, which is widely regarded as one of the most advanced electronic counter technologies in the world, has opened new doors for Australia Post, and has made possible the rapid expansion of bill payment and payment services.
Service

The goals in this area have been: to improve letter delivery performance; to develop and implement a retail structure that better meets market segment needs; to provide universal letter service at uniform prices; and to modernize the mail handling system with minimal disruption.

*Letter delivery performance* urgently needed upgrading. In 1989, customers faced a confusing array of mail delivery times. The fact that 80 percent of the nation’s mail was lodged with Australia Post between 4 p.m. and 6 p.m. added to the delays. Indeed, a self-assessment by Australia Post led it to conclude that 88 percent of letters were delivered on time.

By 1994, however, there was a standard closing time of 6 p.m. for all major population centers. This closing time is, on an average, up to an hour later than that of many Western countries. In 1994 an external audit by KPMG Peat Marwick revealed that 93.3 percent of mail arrived early or on time, with the figure rising to 98.5 percent being delivered within one more day. This figure is all the more impressive given that mail volumes have been rising and that in Australia vast distances need to be covered.

A retail structure was needed that would *better meet market segment needs*. In 1989 Australia Post’s retail network of post offices and post office agencies was not meeting contemporary needs. Many offices were poorly located. In addition, retailing standards were outdated and did not suit customer needs or the direction in which the Post was moving. The post office network was also losing money.
By 1994, customers were increasingly able to choose from a range of outlets in convenient locations to suit their specific needs. Such outlets included: postshops, business centers, delivery centers, licensed post offices, and postpoints—along with traditional "over-the-counter" post offices. Since 1989, some A$145 million has been invested in the network, and 38 mail centers and 14 parcel centers are at the core of the network.

Another goal concerned Australia Post's community service obligation (CSO) to provide a universal standard letter service at good standards of performance at a uniform price throughout Australia. To enhance the accessibility of the postal service, the Post has located 35 percent of its outlets in rural and remote areas where 14 percent of Australia's population lives. Figure 7 shows senders' comparative access to the postal network.

**Figure 7**

*Letter Senders' Comparative Access to the Postal Network, by Area Type, 1995*

Urban postal outlets service two to three times as many residents as do rural and remote outlets. Delivery services across the country have been maintained. Ninety-eight percent of the 7.7 million addresses served in 1995 received at least five letter deliveries a week. In sum, access to rural and remote areas stands firm.

The problem of modernizing mail handling with minimal disruption was an urgent concern of Australia Post. In 1989 most letters had been sorted manually, at the rate of 1,300 letters an hour.

In a three-year A$50 million program, completed in 1994, Australia Post installed sophisticated letter processing machines to provide quicker and more reliable mail sorting. By 1994, 30 electronic ma-
chines were each sorting up to 35,000 standard size letters an hour or about 27 times the rate in 1989. In addition, 16 similar electronic
machines sorted larger letters rapidly. This innovative system has
ccontributed significantly to on-time delivery performance.

What is even more remarkable about this increased mechaniza-
tion is that it was achieved without a single day lost through labor
disputes. In 1989 the Post's adversarial industrial climate would have
stifled these changes. With Post's changed culture, these innova-
tions took place with the staff cooperating and participating fully in
the process.

There is no public government blueprint available that sets out the
intended future course of postal deregulation in Australia. However,
the public record provides firm indications on a process, a timetable,
a set of principles, and the publicly stated views of ministers. Further
reforms can be expected, in view of past developments in Australia
and of worldwide trends, since countries overseas that have oper-
ated, or are intending to operate, without a letter monopoly will also
have an influence on developments in Australia in the medium term.

Review in 1996-97

The review of the remaining monopoly protection available to Aus-
tralia Post is to be conducted in 1996-97. This review must be carried
out as provided in the National Competition Policy Reform legislation
and related agreements between the Commonwealth and the states
and territories, entered into in April 1995. The NCPR agreement states
that legislated restrictions on competition would be removed unless it
could be demonstrated (i) that the benefits of such restrictions to the
community as a whole outweigh the costs, and (2) that the objectives
of the legislation could only be achieved by restricting competition.
Moreover, such legislation would be systematically reviewed at least
once every ten years. The Australian Postal Corporation Amendment
Bill of 1994 made the following statement:

The Terms of Reference for the 1996-97 review will be consistent with
the Government's determinations on the findings of the National Com-
petition Policy Review. This approach reflects the Government's view
that a public monopoly must justify the continuation of its monopoly
position.

Stated Government Objectives for the Post

The government objectives for the Post, as set in 1993, were (1) to
safeguard the basic letter service and the uniform postage rate (both
of which are currently provided by Australia Post under a legislated
community service obligation); (2) to encourage price and service
competition in value added services; and (3) to encourage Australia
Post to continue to operate using world-best practices and as a 100 percent publicly owned corporation

The Social Objectives and the Monopoly

While Australia Post is required to perform commercially, it also has a CSO (estimated at A$65 million for 1994-95) to provide all Australians with a letter service that reasonably meets their needs on an equitable basis and that includes a uniform price for domestic standard letter service. This means that the Post delivers a standard letter anywhere in Australia for 45 cents, even though the cost of delivery may exceed the price charged (particularly to rural and remote areas).

Providing the letter service through Australia Post—a single, large enterprise—achieves economies of scale, which are essential for a universal low-cost service. This in turn results in affordable prices. Figure 8 shows the falling real cost of postage relative to the CPI between September 1975 and June 1995.

**Figure 8**

Falling Real Cost of Postage
Relative to the CPI, 1975-95

<table>
<thead>
<tr>
<th>1975</th>
<th>1985</th>
<th>1995</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic Postage Rate</td>
<td>0</td>
<td>20</td>
</tr>
<tr>
<td>Consumer Price Index</td>
<td>40</td>
<td>60</td>
</tr>
<tr>
<td>Price Freeze</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

To achieve the two objectives of service universality and price uniformity, competition is restricted in parts of the letter market, reserving some letter services for Australia Post. In addition, since uniform price is a separate social objective, it has been argued that exclusive rights of carriage for standard letters for Australia Post would be necessary to prevent "cream skimming" and subsequent erosion of the letter pool from which the uniform price can be cross-subsidized.

It should be noted that Australia's vast distances and sparse population make postal delivery a continual challenge. Delivery frequency
depends on delivery costs and community needs. In some remote and rural areas it can cost between A$7 and A$20 to deliver a 45 cent letter. It has been estimated that if the CSOs were delivered by an operator other than the Post, the cost to the federal government would be in the order of A$150 million.

It is still too early to establish accurately the long-term impact of the changes discussed above. However, certain conclusions can be drawn. It is evident that Australia Post has benefited tremendously from its reform efforts. It is now ranked among the world's better performing postal enterprises.

Through a careful phasing of reform, Australia Post has retained its capacity to fulfill its social obligations without detriment to its commercial performance. The challenge for future postal reform is to balance social benefits against the effects of the remaining restrictions on competition, and the risks and costs of short-term disruption to customers' communication patterns and service quality. The lessons of the Australian experience in postal reform indicate that measured, carefully designed reform provides a good path toward optimal consumer and social benefits.
CASE STUDY 5

British Post Office: The Need for Further Reform

The United Kingdom's Post Office is regarded as providing a superior service while being profitable at the same time, and is also considered an early and effective example of corporatization and commercialization. Nevertheless, the Post Office is of the opinion that, to respond effectively to the changing market requirements and the current competitive structure, the sector needs to be further liberalized. If such liberalization is not forthcoming, it is feared that the competitive and financial position of the postal service will be eroded. This highly focused case study looks at the constraints that the Post Office faces.

From its origins as a government department providing services based in local communities, the British Post Office has migrated, through a series of structural changes, to a changed customer base in the business community. The first driver for this migration was the government's decision in the early 1960s that the Post Office should introduce a form of profit and loss accounting. In 1969 the Post Office was established as a public corporation. The 1981 British Telecommunications Act led to the privatization of the telecommunications business and the creation of a Post Office Board solely concerned with the affairs of the Letters, Parcels, and Counters Services and the Girobank (opened in 1969). The Girobank was structured and managed separately until its sale in 1989.

Background

The Post Office is required by legislation to meet all reasonable demands for letter services. It carries out other tasks which are not required by statute but with which it is traditionally associated, such as the nationwide parcels service provided by Parcelforce and the payment of social security benefits at post offices. Today the Post Office consists of three main businesses: Royal Mail, Parcelforce, and Post Office Counters. Royal Mail and Parcelforce are separate operating divisions of the Post Office, while Post Office Counters is a wholly owned subsidiary. Key facts on each of the three main Post Office businesses are given below.

**Royal Mail** represents some 70 percent (over £4 billion) of total Post Office turnover. It employs 165,000 people, most of whom are front-line postmen and postwomen providing a daily delivery service to 23.4 million addresses. They deal with more than 60 million items of mail a day, collected from 100,000 street postboxes as well as from post offices and directly from many organizations. Royal mail has a statutory monopoly on letters delivered for less than £1 (although the government is committed to reducing this figure).

**Parcelforce** represents some 10 percent (around £500 million) of Post Office turnover. It employs 13,000 staff and deals with three-quarters of a million parcels a day. It offers an individual parcels service to customers at post offices, delivering throughout the country for a uniform tariff. Its main business activity, however, is to provide a collection and delivery service for larger customers on a contract basis for which it competes with many other businesses in the private sector. For reasons of efficiency it subcontracts some of its services to Royal Mail.

**Post Office Counters** represents 20 percent (around £1 billion) of Post Office turnover. It runs the network of nearly 20,000 post offices, of which nearly 19,000 are sub-post offices owned and managed by private individuals or companies on an agency basis. The remaining post offices are directly run by Post Office Counters, which employs about 15,000. Post Office Counters provides services to many clients in addition to Royal Mail and Parcelforce, including the Benefits Agency, the Girobank, the Driving and Vehicle Licence Agency, the Department for National Savings, and a number of utility companies. Of these, by far the most important is the Benefits Agency which accounts for about one-third of the income of Post Office Counters. About 25 percent of Counters’ income comes from Royal Mail and Parcelforce.

---

2 Post Office counters provides a retail outlet through which various government bodies and ex-government bodies provide services to the public. These bodies are generally called “clients” of Post Office Counters, to distinguish them from “customers,” namely, members of the public who receive or buy those services in post offices. It is generally the clients rather than the customers that provide the income of Post Office Counters Limited.
A fourth trading business, Subscription Services Ltd, provides licensing and subscription management services, principally for the BBC. It employs some 1,400 people and has a turnover of £50 million.

Royal Mail has been consistently profitable for many years. It makes the largest contribution by far to the Post Office's overall profits. Parcelforce, on the other hand, operates in a parcels market which has suffered from overcapacity in the recent recession and has been loss-making.

For Royal Mail, it is important to recognize that the letters market is not self-contained but is part of a wider communications market. Businesses and individuals now have an increasing number of ways of sending messages, such as by telephone, fax, and electronic mail. Businesses can now order and pay for goods electronically, home banking is a reality, and home shopping is a prospect. Direct mail is competing with television, radio, and press advertising.

These changes pose a growing threat to Royal Mail's traditional business. Royal Mail has a monopoly over all mail delivered for less than £1 per item. But even with this protection, commercial pressures are making themselves felt, for example, in the following ways.

- Royal Mail's market share in the wider communications market is estimated at only some 14 to 16 percent. Competition in that market is fierce. The electronic data interchange (EDI) market is growing by about 20 percent annually and the fax market is growing by 30 percent a year. Both businesses and individuals have a wide range of alternatives to written communication sent through the post.

- There is also increasing competition for letter traffic. Letters costing more than £1 can be delivered by a wide range of local, national, or international private sector courier companies. The real value of the £1 limit has been reduced significantly since its introduction in 1981. If mail for U.K. companies is printed overseas and posted to the United Kingdom, the revenue for Royal Mail is lower than the revenue for mail posted in the United Kingdom. In addition, the government is committed to lowering the monopoly further to allow other operators to develop new services, consistent with ensuring that Royal Mail can deliver its universal service at a uniform and affordable tariff.

Parcelforce is not protected by a monopoly. While it is the only parcels service available at post offices, this business represents only about 6 percent of its volume and, for the most part, Parcelforce is competing directly with the private sector. It faces growing competition from the following sources:
• A marked growth of competitors in the U.K. market, particularly from small, independent businesses.

• Increasing demands by its business customers for a faster and more reliable parcels service. Most of Parcelforce's competitors have invested heavily in this area of the market, notably in "track and trace" facilities which enable customers to be given much better information on whether and when their parcels are delivered.

• Growing international competition. In the absence of a monopoly, there are no constraints on other companies regarding the delivery of parcels and related services within the United Kingdom.

While both Royal Mail and Parcelforce have taken many steps to respond to the new business environment, there are limitations on their ability to respond because of the constraints of nationalized industry status. The Post Office Board has made it clear that the future of both businesses, and thus their ability to maintain their vital public services, requires that they be able to respond with a higher level of commercial flexibility and freedom than is permitted under the current public sector control regime.

The Trade and Industry Select Committee has also argued that traditional Treasury restraints on these postal activities have hampered the Post Office's ability "to meet the challenges and opportunities of international competition."

The government believes that increased competition benefits consumers and strengthens the country's economy and also accepts that Post Office Counters, Royal Mail, and Parcelforce need greater commercial freedom if they are to respond effectively to the challenges they face. The government takes the view that it is in the interests of consumers and the wider economy for these businesses to be allowed to change so that they can operate successfully in a more competitive environment.

Post Office Counters

The network of post offices represents a partnership between the public and private sectors. Post Office Counters, the public sector core of the business, is at the hub of this network, negotiating and coordinating the contracts with government bodies and other clients on which the network depends. Post Office Counters provides the infrastructure that supports the individual post offices and ensures that they provide services to a high standard, building on the reputation of the business for security and efficiency. Post Office Counters also directly runs some 800 of the larger offices (known as "Crown" offices), although the Post Office has been converting these to agency status in the interests of efficiency and customer service. The Counters
business is relatively small, employing 15,000 of the 200,000 staff of the Post Office.

The network of sub-post offices injects private sector involvement and capital into the business. This network provides direct employment for 19,000 sub-postmasters and their support staff. The combined investment of the sub-postmasters in the post office network has been estimated at more than £1 billion, which is well in excess of the public sector investment in the business. This combination of public and private interests is mirrored at the level of the individual office. The great majority of the 19,000 sub-post offices run an independent business parallel with the Post Office, and the two businesses are often mutually self-supporting, with the “private” side of the shop supporting the “public” services of the Post Office, and vice versa.

Royal Mail and Parcelforce recognize the need to respond effectively and flexibly to the changing marketplace and competitive structure. They are fully aware of the need for access to capital to invest in new technology and the freedom to compete with private sector operators in supplying new and better services to customers. Other countries are giving their post offices greater freedom to compete in the new market. The Dutch, for example, are selling a large shareholding in the company that runs their postal service.

As has been mentioned, studies conducted by special government committees have concluded that the government’s target impositions on the Post Office and the traditional Treasury restraints on Post Office activities are affecting the Post Office’s ability to act as a commercial organization and to take advantage of the opportunities offered by international competition. The current control regime and the proposed extension of powers are discussed below.

**Control Regime**

The Post Office works to three targets set by the government. Two of these targets—return on capital employed and reduction in real unit costs—are the result of consultation and are accepted by the Post Office as relevant and appropriate. The third target, the External Financing Limit (EFL), is seen as a constraint on business. The EFL target is determined on the basis of a bid submitted to the Department of Trade and Industry (DTI) by the Post Office and is calculated by taking the group’s operating profits, adding working capital and depreciation for the year and the proceeds of any asset sales, and then deducting capital requirements. The DTI negotiates the actual target with the Treasury in the course of the public expenditure round. As the Post Office can be expected to make a profit above its capital requirements, it has a negative EFL: the money to meet the target
plus any excess is paid to the Treasury and is invested in the public sector. In recent years the Post Office has regularly exceeded its EFL target (see Table 1).

Table 1
EFL Target and Post Office Achievement, 1988-95

<table>
<thead>
<tr>
<th></th>
<th>88-89</th>
<th>89-90</th>
<th>90-91</th>
<th>91-92</th>
<th>92-93</th>
<th>93-94</th>
<th>94-95</th>
</tr>
</thead>
<tbody>
<tr>
<td>Target</td>
<td>57</td>
<td>97</td>
<td>91</td>
<td>nil</td>
<td>65</td>
<td>66</td>
<td>181</td>
</tr>
<tr>
<td>Achiev</td>
<td>80</td>
<td>102</td>
<td>102</td>
<td>nil</td>
<td>74</td>
<td>80</td>
<td></td>
</tr>
</tbody>
</table>

The EFL target set for 1994-95 was higher than the Post Office's current post-tax profit. The 1993-94 target represents a rate of return on capital of about 20 percent. As the Post Office has said, it is impossible to find such an amount from cost savings, particularly in an organization with such high increases in efficiency. Increased EFLs have forced the Post Office to cut back its capital investment plans by between £80 million and £100 million. This has meant that the Post Office has not been able to proceed with worthwhile projects that would have reduced its costs considerably. The EFL was also the determining factor in the rise in postal charges in November 1993, and major users felt that the vast increases in the EFL were damaging to the Royal Mail and its customers.

The government’s financial controls in the form of the EFL, the capital expenditure limits, the profit and efficiency targets, and other limitations were intended to create the general incentives and pressures on management that management would face from private sector shareholders. But the government’s controls differ from a private sector approach in the following ways:

- For overall budgetary management reasons, the EFL is set a year in advance and is cash-related rather than profit-related. A private sector company would decide on the level of its dividend retrospectively. The EFL is set by the government, whereas private sector dividends are set by company directors.
- The Post Office is not permitted to borrow on capital markets but has to rely on the Treasury for external funding except in limited circumstances.
- Through the setting of the EFL and the capital expenditure limit, the Post Office effectively competes with other candidates for public expenditure in the annual public expenditure survey.
Extension of Powers

The Post Office argues that its separate but linked demands for extension of its powers are essential to its ability to compete. The activities that the Post Office can undertake are determined by the Post Office Act 1969 and the British Telecommunications Act 1981. Under this legislation the Post Office is granted specific powers that can be extended in certain areas by the Secretary of State. This means that some restrictions could be removed by ministerial approval alone, without primary legislation.

A particular example of an irksome restriction is seen in entry into joint ventures. The postal administrations of Sweden, France, Germany, Canada, and the Netherlands have formed a joint venture, GD Express Worldwide, with TNT, and New Zealand Post operates a document processing service through joint ventures. The Post Office in the United Kingdom has pointed out clear strategic advantages in joining forces with airlines or telecommunications companies, but despite the legality of such ventures, it was made clear to the Post Office that, as a matter of policy, some members of the government did not want the Post Office to enter into such arrangements. Therefore, certain steps that could be taken to ensure that the Post Office remains competitive cannot be considered, for example, ventures and partnerships with cable companies to offer multi-media distribution, and with printing or facilities companies to provide one-stop shop services. Other joint ventures, for example, those involving freight brokerage or security services, would require primary legislation.

Post Office Counters has its own difficulties in that it not only has no monopoly but it is constrained as to the services it can provide. The Counters have also been adversely affected by their declining role in activities funded by government agencies, such as pensions or child benefit payments. Since 90 percent of Counters are run as private enterprises, this restriction on their ability to develop their own businesses is hard to justify. In the Netherlands, post offices act as banks, travel agents, job centers, and ticket agencies. The British Post Office has considered introducing similar schemes in the United Kingdom, including financial services, the sale of pools coupons, and further involvement in the National Lottery (beyond the sale of tickets already proposed), but such activities are outside of its existing powers.
Conclusion

The case of the British Post Office is a good example of the limitations of corporatization and commercialization. Beyond such enterprise reform, it is almost imperative to introduce institutional and regulatory reform if further improvements are needed or if the competitive posture of the postal service is to be maintained. It should be borne in mind that the British Post Office has these restrictions and limitations because of its institutional arrangement: the Post Office is under state ownership, and the government ensures that a state-owned service does not abuse its exclusive privilege by imposing a tight financial and legislative control on such state-owned services. This in turn limits the Post Office’s ability to operate along commercial lines and to respond to market dynamics effectively. It is evident, then, from the U.K. example, that if a postal service is concerned with assuring greater commercial freedom, it must first design the appropriate institutional and regulatory approach.
Canada Post: Reinventing the System

In a number of countries, the postal sector faces the issue of transforming a poorly performing government department into a competitive business that provides a high quality of service and is financially self-sustaining. The experience of Canada Post Corporation can provide insights into this reform process, particularly as some of the problems faced by Canada Post when it commenced reform are common to the postal sectors of many countries.

Canada Post’s case is of particular interest in that the country’s demographic and geographic features add to the challenge of reforming its postal sector. Canada spans a distance of approximately 5,514 km, through six time zones. Its population exceeds 28 million, approximately 74 percent of whom are literate. The population is thinly spread over nearly 10 million km², with a population density of only 2.8 persons per km². The majority of the population is concentrated in the major urban centers situated close to the Canada-United States border, which increases the disparity of the rural-urban population density that the post has to service. These features have made it a formidable task to provide an efficient postal service while maintaining universal service at uniform prices.

Today Canada Post is a substantial enterprise. In 1995 it processed 11.6 billion pieces of mail and generated revenues of Can$4.7 billion from operations. In addition to the 28 million inhabitants, the Post serves over 900,000 businesses and public institutions through a network of approximately 18,500 retail points of purchase, as well as

---

1 This case study is based on research undertaken by John Mulligan, UPU consultant, and by John Lee, Gary Halpin, and Donald Dickie, of Canada Post Systems Management Limited.

2 Years refer to fiscal year, which ends March 31 unless otherwise indicated. Thus, 1995 refers to the 1994/95 fiscal year.
some 884,000 locations at which customers can deposit their mail. The Post combines its extensive physical distribution network with a broad spectrum of electronic messaging tools to access virtually every business and residential address across Canada. It also works in partnership with more than 200 foreign postal administrations to meet the global needs of its international customers. The Post employs 62,500 full-time and part-time staff, which makes it one of the largest employers in Canada. It is also one of the largest users of air, surface, and marine transportation in the country.

In spite of these impressive statistics, Canada Post still has considerable scope for improvement, and in that sense has still to complete its journey of reform. In addition, Canada Post, like many other reforming postal services, has kept away from significant regulatory reforms. Nevertheless, the case of Canada Post is an interesting experience of the commercializing of a formerly fully state-controlled postal service.

The Reasons for Reform

Prior to 1981, mail volume grew at a compound annual growth rate (CAGR) of 5.7 percent and revenue patterns displayed a healthy trend as well (see Figures 1 and 2). Nevertheless, Canada Post was plagued by several acute problems that provided a strong impetus to the reform program. This was in line with the prevalent view that internal inefficiencies were negating the benefits of growth.

The main problems confronting the Post as it embarked on its reform process are listed below.

Figure 1
Trend in Mail Volumes, 1976-81

![Graph showing trend in mail volumes from 1976 to 1981.]

3 The fourth largest employer in 1991.
• **Severe financial losses:** One of the most significant problems that the Post faced at this juncture was the magnitude of the financial losses that it had been experiencing (see Figure 3). In the mid-1970s the post had experienced deficits in excess of Can$500 million for three consecutive years. Because of this legacy of unprofitability, the Post not only represented a huge financial burden on the government and the public exchequer, but was incapable of securing the finances necessary to turn itself around. It had reached a stage where users paid only 57 percent of the costs and general taxation paid for the rest (because of subsidization of the Post). In addition, the overall trend was toward a larger deficit and, unless this process was stemmed, there was every expectation that the deficit would soon exceed Can$1 billion.

**Figure 2**

*Trend in Revenues, 1976-81*

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Revenue (Can$ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1976</td>
<td>0</td>
</tr>
<tr>
<td>1977</td>
<td>400</td>
</tr>
<tr>
<td>1978</td>
<td>800</td>
</tr>
<tr>
<td>1979</td>
<td>1,200</td>
</tr>
<tr>
<td>1980</td>
<td>1,600</td>
</tr>
<tr>
<td>1981</td>
<td>2,000</td>
</tr>
</tbody>
</table>

**Figure 3**

*Financial Losses Prior to Reform, 1969-81*

<table>
<thead>
<tr>
<th>Year</th>
<th>Deficits of Canada Post (Can$ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1969</td>
<td>50</td>
</tr>
<tr>
<td>1970</td>
<td>100</td>
</tr>
<tr>
<td>1971</td>
<td>150</td>
</tr>
<tr>
<td>1972</td>
<td>200</td>
</tr>
<tr>
<td>1973</td>
<td>250</td>
</tr>
<tr>
<td>1974</td>
<td>300</td>
</tr>
<tr>
<td>1975</td>
<td>350</td>
</tr>
<tr>
<td>1976</td>
<td>400</td>
</tr>
<tr>
<td>1977</td>
<td>450</td>
</tr>
<tr>
<td>1978</td>
<td>500</td>
</tr>
<tr>
<td>1979</td>
<td>550</td>
</tr>
<tr>
<td>1980</td>
<td>600</td>
</tr>
<tr>
<td>1981</td>
<td>650</td>
</tr>
</tbody>
</table>

• **Deteriorating asset base:** Because of the Post's worsening financial condition and a lack of access to resources for investments, the postal system's asset base was deteriorating rapidly (see Figure 4). For several years capital investment had not even equaled depreciation and certainly could not provide for the maintenance and expansion of a modern operating system. And the trend was toward further decreases in investment levels. Plants and other facilities were outdated and inefficient, and equipment was obsolete, which exacerbated the problem of poor operational performance and curtailed the Post's ability to improve its service.

**Figure 4**

**Lack of Investment, 1976-81**

<table>
<thead>
<tr>
<th>Year</th>
<th>Investments in Fixed Assets (Can$ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1976</td>
<td>60</td>
</tr>
<tr>
<td>1977</td>
<td>50</td>
</tr>
<tr>
<td>1978</td>
<td>40</td>
</tr>
<tr>
<td>1979</td>
<td>30</td>
</tr>
<tr>
<td>1980</td>
<td>20</td>
</tr>
<tr>
<td>1981</td>
<td>10</td>
</tr>
</tbody>
</table>

• **Ad hoc pricing policy:** The Post lacked an explicit pricing mechanism, and in the past postal rates had not increased to keep pace with rising costs, since rate increases were politically unpopular. Thus, while Canada Post flaunted the fact that its postage rates were the lowest among the industrialized nations, revenues were insufficient to cover payrolls. Combined with operational inefficiency, underpricing of postal services culminated in severe fiscal losses.

• **Reputation for unreliability:** As a result of a complete absence of the operating standards, systems, and procedures essential to harmonize a nationwide distribution system, delivery commitments were largely based on guesswork and performance was highly erratic. From 1973 to 1981, delivery performance ranged from 60 to 92 percent of the stan-

---

Case Study 6
Reinventing the System

dards that the Post had set for itself (see Figure 5). Because of its poor service performance, the Post Office Department acquired a reputation for unreliability. This loss of confidence in the Post also coincided with (or perhaps caused) the massive growth in the use of private sector services and technological alternatives. Undoubtedly, this contributed to a lower utilization of the Post, thereby perpetuating the cycle of financial losses and poor quality of service.

Figure 5
Poor Delivery Performance, 1976-81

<table>
<thead>
<tr>
<th>Year</th>
<th>Percent of Mail Delivered on Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>1976</td>
<td>90</td>
</tr>
<tr>
<td>1977</td>
<td>80</td>
</tr>
<tr>
<td>1978</td>
<td>70</td>
</tr>
<tr>
<td>1979</td>
<td>60</td>
</tr>
<tr>
<td>1980</td>
<td>50</td>
</tr>
<tr>
<td>1981</td>
<td>40</td>
</tr>
</tbody>
</table>

Note: National service performance of first class short and long distance delivery.

- Labor strife: The Post’s work force was militant and heavily unionized, and its relations with management were adversarial. Strikes and work stoppages had become the norm during the prolonged collective bargaining negotiations (see Figure 6), and this further eroded the public’s confidence in the system. By the end of 1979 the Post had incurred a backlog of 15,140 labor grievances. To compound matters, management’s flexibility to operate effectively had been given away in past settlements by the government, in an attempt to end postal strikes.

- Organizational chaos: The Post Office Department was divided into four regions, each of which had complete autonomy, thereby relegating the headquarters to a mere administrative role. The regions maintained their own prac-

---

* The postal unions have been among the most radical unions in Canadian history. The influence of war veterans in the management ranks, combined with a low turnover of union members, ensured that the “collective union memory” and distrust of management would remain a significant hurdle.

* For example, the right to decide the priority of mail for delivery had been given to the unions in one of the collective agreements.
Redirecting Mail: Postal Sector Reform

tics and priorities, and this extreme decentralization ag-
gravated the problem of attaining synchronized operations
on a nationwide scale. In addition, as is typical of govern-
ment departments, the Post had control only over its core
operations; all support services (payroll, data processing,
labor, property, etc.) were provided by other government
departments whose priorities may not have corresponded
with those of the Post.

Figure 6
Disruption of Postal Operations, 1979-82

- Poor corporate culture: Both the management and the em-
employees of the Post were unfamiliar with the norms and val-
ues of a customer-oriented, self-financing business,
operating in a highly competitive market, with critical ser-
vice and profit targets to meet. Transforming the corporate
culture of a public service environment was one of the Post's
greatest challenges during its reform process.

- Political interference: As was mentioned earlier, because
of political implications the government preferred to sub-
sidize the operation and shoulder the huge losses rather
than authorize a rate increase in postal services. Politi-
cal considerations often entered staffing decisions as well.
Local postmasters were appointed by local politicians, for
reasons other than ability, thereby depriving the sector of
critical expertise. In addition, as has been mentioned,
management’s control over mail delivery and other key
aspects of operations had been severely compromised
in government-imposed settlements made to end postal
strikes. It was now necessary for the Post to regain its ability to manage operations.

By 1978 the government had acknowledged that something had to be done to remedy the above problems, which were severely affecting the Post's performance. In addition, the government acknowledged the higher service expectations from customers, the increasingly aggressive competition, and the expected explosion of new communication technologies. In October 1981, Canada Post Corporation (CPC) was established as a Crown Corporation to operate a postal service on a self-sustaining financial basis while providing a standard of service that would meet the needs of the people of Canada.

Since the postal sector in many developing countries experiences some of the above problems, the reform experience of Canada Post can provide useful lessons regarding postal services.

As a government department, Canada Post suffered from the two classic shortcomings associated with this organizational form—lack of autonomy and lack of accountability. The Post Office Department could not control its own operations because it was dependent on other government departments to perform many of its crucial services. It did not have control over its own staff (which is critical in the labor-intensive postal sector) and it had no control over its investment and expansion programs (which were completely divorced from its own earnings). In addition, political intervention in the Department's operations was commonplace. Lack of accountability was the flip side of this situation. Since the Post consisted only of an operating unit with no support services, it was not capable of following (nor was it mandated to follow) the financial disciplines essential for accountability. The assurance of government support (a soft budget constraint) did not provide incentives to curtail expenses. It was also difficult to demand accountability because management responsibilities were so diffuse, both regionally and functionally.

After more than a decade of consideration and study, CPC was established by the Canada Post Corporation Act on October 16, 1981. Prior to this date, the 113-year-old Post Office Act was a reflection of experiences within the United Kingdom on which much of the common law of Canada has been based. The new legislation would also update and clarify many of the provisions of the Post Office Act, bringing them into line with prevailing practices and conditions. The CPC Act was therefore adopted to provide for a continuing national postal

---

Reform through Legislation: The Birth of Canada Post Corporation

---

As is commonplace in government departments, the Post's revenues went directly into a consolidated revenue fund and the Post had to justify its budget against that of every other federal department. As a result, the Post's capital program ran well below even the level of depreciation of the Post's buildings.
service able to respond to changing social and communication needs. In setting out the objectives of a new postal corporation, the new legislation recognized both the need for the continuity of a basic universal and accessible mail service and the commercial nature of modern postal operations and services.

CPC is a Crown Corporation included in Schedule C to the Financial Administration Act and is an agent of Her Majesty. This organizational structure was chosen because of the government's familiarity with it and (primarily) because "such a structure would allow for a single management focus on all aspects of the postal business, rather than having responsibility diffused among various government departments, each concerning itself with only one particular aspect of management."\(^9\) Day-to-day operations became the responsibility of the Board of Directors vested with the power to set corporate policy and make financial, staffing, managerial, and other decisions independent of government departments. This change in procedure and responsibility would greatly simplify operations and would enhance efficiency.

Proclamation of the Act initiated the monumental task of transforming Canada Post from a government department to a Crown Corporation. At that juncture, the Act was considered to be a model Crown Corporation act in that it reflected advanced thinking concerning the balance between providing management with the necessary freedom to control the affairs of the corporation and providing the shareholder (the government) with the basis for accountability to Parliament. The establishment of the Crown Corporation was intended to segregate a significant portion of the government's activities and establish the Post as a stand-alone entity. Thus, ownership was to be separated from operations, and the latter was to be subject to explicit regulations in the form of the mandates and objectives for which the Corporation would be held accountable.

The CPC Act provides the CPC with a basic mandate within which to conduct the affairs of the postal service. That mandate is as follows:

- To establish and operate a postal service for the collection, transmission and delivery of messages, information, funds and goods both within Canada and between Canada and places outside Canada;
- To manufacture and provide such products and to provide such services as are, in the opinion of the Corporation, necessary or incidental to the postal service provided by the Corporation; and
- To provide to or on behalf of departments and agencies of,

\(^9\)Canada Post Annual Report, 1982-83.
and corporations owned, controlled or operated by, the Government of Canada or any provincial, regional or municipal government in Canada or to any person services, that in the opinion of the Corporation, are capable of being conveniently provided in the course of carrying out the other objects of the Corporation.

The Act also specifies more tangible objectives for the Post by stating that, while maintaining basic customary postal service, the Corporation shall have regard to:

- The desirability of improving and extending its products and services in the light of developments in the field of communications;
- The need to conduct its operations on a self-sustaining financial basis while providing a standard of service that will meet the needs of the people of Canada and that is similar with respect to communities of the same size;
- The desirability of utilizing the human resources of the Corporation in a manner that will both attain the objects of the Corporation and ensure the commitment and dedication of its employees to the attainment of those objects.

Thus, the government explicitly addresses the three primary concerns of quality of service, financial self-sufficiency, and labor-related issues in legislation that guides the operation of the CPC. It is worth noting that both the mandates and the objectives of the CPC recognize that the corporation can enter into activities that are coincidental to traditional postal activities and that the mandates and objectives provide that the CPC should have due regard for developments in the telecommunications industry, thus allowing the CPC to move beyond hard copy material.10

To give the CPC sufficient control over its operations and to put it in a position to accomplish its mandate and objectives, the Act conferred certain rights and responsibilities on the corporation. These included the following:

- The corporation was granted the exclusive privilege11 for the collection, transmission, and delivery of letters to an addressee in Canada. Other competitors that wish to serve the letter mail market have to charge at least three times the 50 g letter rate charged by the corporation, thereby providing the corporation with considerable price protection.

---

10 It is interesting to note that while some countries consider diversification into value added activities and the provision of new communication modes vital to the survival and competitiveness of the postal sector, others regard this as detrimental to the provision of traditional postal services (for example, see the Chile case).

11 Although this "exclusive privilege" provides the corporation with weight and price protection for basic letter mail, it refuses to concede that it has a monopoly.
The corporation is also responsible for prescribing regulations for postal rates and other matters governing the movement and handling of mail, all of which are subject to the approval of the Governor in Council.

It also has the right to the setting of postal rates at fair and reasonable levels that are consistent, as far as possible, with providing a revenue— together with revenue from other sources—sufficient to defray the cost of operations.

A mechanism was established for government funding of the corporation during the transitional period toward financial self-sufficiency, and thereafter, should the need arise.

A provision was made whereby the corporation may be compensated for any loss that it incurs in carrying out directives from the minister responsible for the corporation or the Governor in Council. In addition, these directives must be laid before Parliament.

The CPC Act provided that all the property, assets, rights, obligations, and liabilities of the Post Office Department be transferred to the CPC from the Government of Canada. The major long-term liability carried on the CPC’s balance sheet at incorporation related to the severance pay entitlements of employees (approximately Can$245 million); however it is important to note that this is a joint liability with the government. The Act provided for the establishment of a share capital structure. CPC was established with contributed capital of Can$1.67 billion and is fully owned by the government. As a Crown Corporation, Canada Post enjoys certain privileges that ordinary business corporations do not. It has access to sovereign credit at lower interest rates than market rates, since it is co-guaranteed by the government. In addition, until 1994 Canada Post was exempt from paying income taxes.

While the corporation has been mandated in its statute and by the Government of Canada to conduct its affairs on a financially self-sufficient basis, at its inception CPC inherited a deficit from the Post Office Department of approximately Can$600 million a year, which was estimated to grow to Can$1 billion a year if left unchecked. So that the deficit reduction could be accomplished in an orderly manner, and without constraining improvements in human relations and service, the government and the corporation agreed that financial self-sufficiency would be targeted for 1987. In the intervening years, Parliament would provide the CPC with a series of deficit appropriations.

This may be regarded as “explicit subsidies.”
As regards labor relations, the Act established that the Canada Labor Code would replace the Public Service Staff Relations Act as the legal framework in which collective bargaining would take place. This move had long been sought by both the postal unions and management, since it would result in a bargaining forum in which those directly concerned with the operations of the postal system (the management and workers) would be participants in collective bargaining. To help ensure a smooth changeover during the transition period, the Act also included provisions providing for the continuation of benefits and contractual rights and obligations of employees and their bargaining units until such time as these would be modified by collective agreement or, for non-unionized employees, by management policy. For pension purposes, however, the corporation's employees continue to be covered by the Public Service Superannuation Plan, which is administered by the Government of Canada.

In addition to the CPC Act, the corporation operates within the purview of two other specific segments of legislation. The Financial Administration Act applies to all Crown Corporations and establishes parameters within which certain fiscal responsibilities are to be carried out. This Act also allows the government in its capacity as the owner of these corporations to issue directives, and to establish control mechanisms and reporting requirements. Canada Post is also subject to the Competition Act, like any other business corporation. This Act specifically prohibits the corporation from using its exclusive privilege to further initiatives in other business markets.  

However, legislation, while necessary, was not in itself sufficient to solve the problems of Canada Post. At this juncture, the corporation faced the daunting task of transforming a government department, with the problems discussed above, into a "customer-oriented, employee-caring and financially self-supporting organization." Although CPC inherited the formidable problems of its predecessor, from a positive perspective it also inherited a work force of some 62,000 trained employees, the operating knowledge of an experienced management, the established business of providing mail service to all Canadians, and, most important, an operating and policy environment of a more "facilitating" nature.

---

13 This Act was invoked once Canada Post acquired Purolator, a private courier company. The Post had to prove that its courier products were not being cross-subsidized by its letter mail products. For this purpose, the Post developed a detailed product costing system which it has since found indispensable to basic business decisions.

Relationship with the Government

In Its Capacity as the Owner

Although the establishment of Canada Post as a Crown Corporation sought to remove the operations of CPC from excessive government oversight, the Government of Canada still retains considerable control over the Post in its capacity as the sole shareholder of CPC. The government appoints the Board of Directors and the President of the corporation. However, while the President is appointed by the government, the corporation has considerable say in his selection through the Board of Directors.

As is specified by the Financial Administration Act, CPC must submit its five-year corporate plan to the government, the first 12 months of which are specified in detail. This plan gives the government insight into the strategic direction of the Post and clearly delineates where the Post may be departing from prior practices. The corporate plan also enables the government to observe the balance that the corporation is striking in achieving its objectives through operational efficiencies, business growth, or rate increases. In addition to the corporate plan, operational and investment budgets must also be approved by the government, sometimes after extensive negotiations. In addition, the government signs off on any borrowings that are needed by using sovereign credit, and gives specific approval for any acquisition in the form of equity in other corporations or for joint ventures.

Although the corporation is obliged to provide universal service at a uniform price, there are no non-commercial or social obligations that are carried out for reasons of government policy. However, there are certain activities for which the corporation is reimbursed by the government for the difference between the rate charged and the current market rate. These activities include delivering mail free to Members of Parliament, delivering mail at underpriced rates to the Northern areas, providing literature for the blind free of charge, and until recently, providing support to the publications industry.\(^5\) These discount rates are set in conjunction with the department whose policies are being promoted; the difference between the commercial rates and the actual rates is recovered by the corporation from the department in question.

The CPC Act vests the Minister and Cabinet of the Government with the capacity to issue specific instructions to the corporation to carry out certain activities relative to its mandate. This is referred to as directive power, and although it has not been invoked since incorporation in 1981, it does provide the government with a broad range of authority over the corporation should it choose to exercise this power.

\(^5\) Recently the corporation stopped providing the publications industry with subsidized rates, and it has been decided that any financial support from the government will be rendered directly to the sector.
In Its Capacity as the Regulator

Regulation of an autonomous postal service has been considered necessary to prevent the Post from abusing its exclusive privileges in certain market segments, by either overcharging its customers or compromising on the quality of service. Canada Post has an exclusive privilege over basic letter mail, which is considered the regulated product. It has no monopoly with respect to parcels, publications, flyers, advertising material, or counter services. Even with basic letter mail, the exclusive privilege is not enforced rigidly since utility companies exist that distribute their own bills despite the CPC Act.

CPC has decided that it is in its own interest to improve its own service offerings rather than enforce the exclusive privilege. In terms of regulation of service, the Committee on Government Operations reviews Canada Post's activities and performance. In addition, every five years an external auditor examines Canada Post's management efficiency, service quality, and compliance with laws and regulations. The rate paid for a service will largely dictate the value that a customer derives from a service. Accordingly, regulation of postal rates has been accorded primacy by regulators or governments. In the case of CPC, it is only the basic letter mail whose prices are regulated. The pricing structure of other products is entirely at the discretion of the corporation and is dictated by market considerations.

Canada Post does not possess an explicit pricing mechanism (such as a specified rate of return or an RPI-X mechanism) for rate changes of the regulated product, although the stated policy for basic letter rates is to keep the price increases within inflation, using 1982 postal rates as a basis. In assessing rate increases requested by the Post, the government takes into account the historical volume/demand responses of the product to price increases—that is, its own price elasticity. The government also considers information from other countries with respect to basic letter rates in order to benchmark affordability. Finally, the effect of competing alternatives, especially electronic communication mechanisms, is also kept in mind when the government authorizes rate increases. Thus, as long as rate increases are limited by inflation, the government has considerable discretion in deciding the exact amount of an increase.

As has been stated, prior to the incorporation of the Post, postal rates were severely underpriced since they had not been increased to keep pace with costs. To facilitate postal reform, the government authorized a substantial rate increase immediately before the corporation was set up. As is evident from Figure 7, since then postal letter rates have been kept consistently well below inflation.

In 1995, the corporation attributes a large amount of its unfavorable financial performance relative to its plan (namely, a loss of Can$26 million) to the impact of the delayed rate increases. While
this was the first time that the government actually held off the rate increase requested by the Post, in the past Canada Post has deliberately requested low rate increases as a precautionary measure against such an outcome. It has not been determined whether, in view of the Post’s continuing deficits, the government has opted for the pricing strategy of increasing the differential between the CPI and postal rate increases (1) to benefit the consumer; (2) to compel the Post to achieve further internal efficiencies and cost reductions; or (3) simply because rate increases are politically unpopular. While rates should not be increased to compensate for operational inefficiency, it is vital that regulated postal rates do not again tend toward underpricing, thereby compromising postal reform in the long term. This delicate balance of considerations underscores the importance of an explicit pricing mechanism which introduces certainty into the magnitude of rate increases and hence rewards the postal sector for efficiencies attained beyond its goals.

Figure 7
Trends in the Postal Rate, 1982-94

Before framing a formal proposal for rate increases, the corporation signals its intentions well in advance through its corporate plan. While approval is not necessary for non-regulated products, the corporate plan also spells out the general range of increases expected for these products. The process for the approval of rate increases of regulated products requires the corporation to frame a formal proposal (after publishing its intentions and taking into account public response) which is then presented to the Minister. The Minister indicates his support by signing the proposal and sponsoring it to the Cabinet where the rate proposal is assessed by the Governor in Council, the senior-most subcommittee of the Cabinet. The Governor in Council then has 60 days to either approve or reject the proposal.
This process has worked smoothly for the last 12 years, and the only exception has been the current rate action which has been deferred by the present government.

When CPC was created, it initially resorted to certain “quick fixes” to remedy or alleviate the problems it faced. This approach, when it proved ineffective, was abandoned in favor of a strategic approach. The strategy developed was first to lay the foundations of the required corporate structure and then to concentrate on operational improvements, in the belief that only when the corporation could deliver on its basic service commitments, and win back the public’s confidence, should it attempt more aggressive product restructuring and marketing strategies. In retrospect, distinct phases have been identified in the corporation’s reform process.

Laying the Foundations of a Corporate Structure (1981-85)

During the first four years of CPC’s existence, the priority was to put in place the infrastructure that would allow CPC to operate as a business. This proved to be time-consuming, not only because CPC lacked any support services (all of which had previously been performed by other government departments) but also because it lacked expertise in corporate operations and procedures (much of which expertise had to be acquired externally). A key element in establishing the corporation was the development of a senior management team capable of transforming a government department into a more competitive and business-oriented organization. To this end Canada Post began recruiting executives from the public and private sectors to join those already engaged in the management of the Post. Extensive management training programs were also implemented to upgrade the management skills and knowledge of the supervisors, and to emphasize the fundamental changes in attitudes needed to motivate employees in a dynamic and competitive corporation.

Some of the aspects of establishing the financial foundations of CPC involved: separating the corporation’s assets and liabilities from the government; establishing the corporation’s own balance sheet and other financial statements (based on generally accepted accounting principles, which differed from government accounting principles); opening a bank account; and building accounts payable, general ledger, receivables, payrolls, and other basic accounting systems. A new countrywide integrated computerized personnel records system was created to store and access employee information. Management information systems were implemented to measure and manage time and
Redirecting Mail: Postal Sector Reform

attendance, cost identification and reporting, operational performance, and other business systems required for more efficient operation.\(^6\)

The organizational structure was also consolidated and streamlined to give CPC a flatter, more responsive, structure. The old structure of four autonomous regions was replaced by a structure of nine regional divisions that would report directly to the head office. The layers of management were pared down from 11 to 6. The management of real estate, the portfolio of buildings, the fleet of vehicles, and basic purchasing and supply were consolidated to introduce a systematic, coherent approach to these functions. CPC developed its own labor negotiation capabilities and also implemented mechanisms to handle grievances.

**Achieving Operational Improvements (1986-88)**

This phase, which concentrated on the central task of improving operations, began by introducing the disciplines of industrial engineering and documenting the capabilities of the existing operations. Following this, uniform national standards, systems, and procedures were developed and implemented that would maintain delivery at clearly defined and publicized service standards. During the next four years CPC spent close to Can$1 billion on capital assets, including replacement and replenishment of physical operating networks, new buildings, new equipment, new processes, and standards and data collections systems. This was necessary to bring in the discipline and technology needed to monitor, measure, and control the network. The control of information and the integration of activities on a nationwide scale was brought into place by the establishment of the National Control Center, which linked all divisions and functional groups into a unified operation.

After completing the overhaul of its operations, and after implementing its reporting systems, the CPC felt it was ready to introduce public monitoring of its delivery performance by independent auditors, which would be published on a quarterly basis. CPC was the first postal administration to introduce this process, which it considered an essential step in rebuilding customer confidence in the reliability of its service.

CPC then confronted the problem of regaining the flexibility to manage mail delivery and other vital services that had been negotiated away in prior strike settlements. This culminated in additional postal strikes which led, in 1987-88, to a loss of 173,417 person days (see Figure 19). The difference this time, however, was that postal services were maintained despite the strikes. This provided management with hands-on experience of running postal services and also

\(^6\)For additional information, see Chapter 4 on the commercialization of the postal service.
reinforced the corporation's reliability as far as customers were concerned. The CPC developed the capability to rapidly reconfigure the network to maintain service when faced with labor disruptions. However, this approach to the resolution of labor problems came at the cost of deteriorating labor relations.

CPC also adopted a more businesslike approach with its suppliers and renegotiated contracts that required suppliers to adhere to agreed standards or accept a penalty.

Building Up Communication and Marketing (1988-90)

This phase of the reform involved employing both internal and external communication and marketing strategies, to motivate employees and involve them in the process of change, as well as to generate growth in business by demonstrating CPC's capability to the public. To communicate this new thrust to its employees, CPC adopted the following mechanisms, among others: a new corporate identity and logo; regular internal publications; videotapes, to be sent to every employee's home, to explain the fundamental changes; programs for rewarding employees for outstanding suggestions and exemplary performance; awards for employment service anniversaries; scholarship programs for employees' children, etc. Through these mechanisms, CPC aims to provide a more interesting, a safer, and a healthier working environment.

During this phase the corporation also redesigned its services and products to better meet the needs of its customers. With this restructuring in place, the corporation launched an intensive advertising and marketing program to expand its business. A separate customer service functional unit has also been created to manage claims, answer inquiries, provide information, handle complaints, verify money orders, conduct telemarketing, supervise general customer relations, and measure service performance and customer satisfaction.

Reshaping for the Future (1990 to the present)

Greater familiarity with its own products, markets, and business opportunities provided CPC with the capacity to create a large systems development team which played a major role in both the rethinking of mail processing operations and the review of the corporation's core business. The R & D Center was also established to conceive, to develop, to prototype, and to demonstrate new products, services, and equipment.

17 For further details, see Chapter 4.
In addition, CPC is facing the challenge of new electronic communications methods by integrating technology into its operations in several ways. It is meeting the changing needs of its customers by adapting to their new capabilities in the generation and reception of electronic information. It is also developing new hybrid services to bridge the gap between high technology and low technology and the different modes of information exchange (see Box 1), overcoming interconnection problems in the process as well. Canada Post has been involved in electronic mail for over two decades through services that combine the advantages of electronic transmission with the corporation’s hard copy delivery capability. The corporation is also using new technology in its internal operations to maintain an accurate and up-to-date addressing capability, and is improving internal efficiency by increasing the percentage of mail that can be electronically processed.

**Box 1 Experimenting in High Value Added Services**

CPC has gone into partnership with a consortium called UBI (Universality Bidirectionality Interactivity), thereby providing a vital link in the home electronic highway. UBI is intended to be the main network for the electronic distribution of goods and services. It will allow customers to order products, pay their bills, and receive personalized mail electronically using an interactive terminal installed in their home. Customers will pick up the goods they have ordered at a community mailbox, strategically located near their home.

Other partners in the UBI consortium are Le Groupe Vidéotron Ltée, Hydro-Québec, the National Bank of Canada, Loto-Québec, Vidéoway Communications Inc., and the Hearst Corporation. This service was being tested in 34,000 homes and implementation was expected to begin in June 1996. CPC’s participation in this initiative reflects its commitment to exploring innovative new services and to forming strategic partnerships where necessary.

CPC has also developed several domestic and international alliances to strengthen its competitiveness. It sees value in concentrating on its core activities and vertically disintegrating activities that can be better and more cost effectively performed externally. As a result, most of the corporation’s information technology, air and surface transportation, and vehicle maintenance have been outsourced. CPC has also aggressively pursued a strategy of acquisitions and alliances when it has considered this necessary to complement its own operations. Thus, CPC has recently acquired Purolator, a major express courier company in North America, and has joined GD Express Worldwide to develop an end-to-end presence in the international time certain and courier express market. The corporation has also entered into partnerships with the banking sector to increase the provision, on an agent basis, of financial

---

16 See Box 4.1 in Chapter 4.
agency services at their retail outlets. Since the postal business is international in scope, CPC is collaborating with other modern postal administrations to provide products and services that compete effectively worldwide. It has also launched a wholly owned subsidiary to market its expertise worldwide.

In 1995, the shift from an operations-driven to a customer-driven operation received renewed emphasis. To become the supplier of choice, Canada Post plans to continuously improve its distribution network; to streamline its service mix according to changes in customer needs; to continue developing new services; and to undertake a major retraining program to make its employees more responsive to customer expectations.

It should be noted that throughout this reform process the CPC had to ensure that the initiatives being adopted in all major areas of activity across the corporation were coordinated with each other and were directed toward the same corporate goals.

To evaluate the results of CPC's reform program, it is necessary to evaluate its success in eradicating the problems it inherited as well as in achieving its specific mandate.

Since 1983, the corporation has experienced a CAGR of 5.5 percent in mail volumes (see Figure 8). In 1995, letter mail accounted for almost half of CPC's revenue. Over the past 12 years the contribution of letter mail to revenue has been slowly and steadily declining, correspondent with the growth of other segments of the market. Currently, approximately 80 percent of letter mail volume is generated by businesses, and consumer letter mail has been gradually declining. To boost the use of letter mail the corporation introduced discounted mail, "incentive mail" for large volume mailers that meet contractual obligations with respect to the preparation of mail. This category has grown in importance, accounting for a significant percent of the revenue from letter mail in 1995.

Growth in mail items does not reflect the change in the composition of products and services the Post has offered over time. CPC aims to continue developing innovative services that meet the current and emerging needs of its customers. In the higher value added line of services, CPC is marketing its expertise and innovative technology to business corporations, government departments, institutions, and even to other postal administrations.

Today CPC considers itself to be in three market areas where it holds different competencies and faces different competitors. The first of these market areas is the communications market which is CPC's core service, where it competes with telecommunications and

---

19 In 1995, CPC formed an alliance with the Canadian Imperial Bank of Commerce.
20 For details see Chapter 4.
Redirecting Mail: Postal Sector Reform

electronic communications mechanisms. While the overall communications market has grown rapidly, the volume of the Post's base product (letter mail) has not increased correspondingly and its share in this market has steadily declined. Nevertheless, in terms of revenue this remains the core component. The distribution/shipping market involves transporting physical goods and is the most competitive of the markets, owing to the presence of a multitude of domestic and international couriers and distribution companies. The advertising market is where CPC competes with the media and broadcasting through direct mail and publications. CPC estimates that it has approximately one-fifth of the communications and long-haul distribution markets and 7 percent of the advertising market. Thus, CPC still has ample potential for growth. In all three markets, the Post has the advantage of being the only true national distributor that can access virtually any residence or business.

Figure 8
Trend in Mail Volumes, 1983-95

The corporation's revenues have displayed a healthy growth, driven primarily by growth in business, especially in higher value added areas, as opposed to price increases (see Figure 9).

Financial self-sufficiency has been one of the key objectives of CPC. When CPC's performance is compared with that of the Post Office Department prior to 1982 (see Figure 3), the deficits show a marked decrease since the operation became a Crown Corporation (see Figure 10). Until 1988, transitional government funding helped significantly to smooth the way financially for the corporation (see Figure 11). The year 1989 was significant for the corporation, which moved into a profitable position for the first time and did not require government appropriations to fund its operating losses. In addition, the corporation was able to borrow Can$80 million in long-term debt from the
government to assist it in financing an increased capital expenditure program. Since 1989 CPC has broken out of the red more than once. However, 1993 was the only time that the corporation earned a profit purely out of revenue from postal operations. Canada Post does not plan to rely on mail protected by exclusive privilege legislation to overcome its losses, since it is constrained by the requirement to provide universal access at uniform cost, as well as regulated postal rates. Instead, it is looking at a variety of initiatives in the business sector to attain growth and profitability. These initiatives include revamping and simplifying its core products to meet customers' requirements, strengthening its marketing and sales capability, focusing more attention on small- and medium-size customer business segments, and pursuing new products and value-added services.

Thus, although deficits have been reduced significantly, CPC has yet to attain its aim of financial self-sufficiency. Nevertheless, conversion to a Crown Corporation has made CPC accountable for its own performance. Owing to the establishment of commercial fiscal practices, and the corporation's separation and clear demarcation from all other government departments, CPC's financial scenario is explicitly visible and the corporation can be held accountable to it.

A marked increase in investments in fixed assets is visible after incorporation, especially after 1986 when attention to operational improvements began in a concerted manner (see Figure 12). The Post has financed its investments from its own earnings—from transitional funding until 1988 and from long-term debt since then. Recently, CPC has begun to take a strategic view of investments and has instituted a procedure that segments investments into maintenance, restructuring, product development, and system infrastructure categories. Each investment is then evaluated to determine whether it provides a good payback in terms of financial return and strategic importance. The corporation recently undertook a three-year restructuring program to offset the operating cost pressures of an increasing delivery network and growing mail volumes. Investment in operational equipment has recently been reduced in an effort to contain spending. The focus on capital investment in mail processing equipment and expansion of the delivery network continues.
Figure 9
Trend in Revenues, 1983-95

Revenue from Operations
(Can$ millions)

Figure 10
Financial Performance after Reform, 1982-95

Net Income or Loss
(Can$ millions)

Figure 11
Taxpayer Funding of the Post, 1982-90

(Can$ millions)
CPC has consistently directed efforts at consolidating and mechanizing certain aspects of mail processing in order to achieve increased efficiencies and cost reductions. In 1983, the Post had 32 mechanized plants which have now been consolidated into 22, and a further reduction is expected. Consolidation facilities for mail from different places of origin have also been reduced—from 130 facilities to 30 larger facilities. Canada Post has a long history of automation of mail processing and has invested in the latest technological equipment, such as MLOCR and VES systems. In 1995, CPC finished installing the latest mail processing technology in all of its major mail processing plants. Currently, a high proportion of all letters and a lesser proportion of parcels are sorted mechanically. This has had an important impact on labor, which has decreased by 10 percent in ten years.

The result of these efforts to improve operational efficiency can be seen in a distinct improvement in the processing, delivery, and collection operations (see Figure 13). In 1983, operating revenue per piece was markedly less than operating cost per piece, which was also reflected in the Post Office Department's enormous fiscal losses (see Figure 3). Although revenue and cost per piece are now at par, the corporation must maintain operational efficiencies in order to stay financially viable.

Efficiency and timeliness are important components of the quality of service. As far as delivery performance is concerned, CPC has achieved a consistent standard of 97 to 99 percent of on-time mail in recent years (see Figure 14). In itself, this is a fairly good record, but the improvement in service quality is impressive in comparison with...
Redirecting Mail: Postal Sector Reform

an on-time mail rate of less than 85 percent in 1987 and still worse standards prior to incorporation (see Figure 5). Now that delivery performance has reached a relatively high and consistent plateau, concern for speed has given way to concern for reliability. The corporation is also considering tightening its delivery standards for letter mail to one, two, and three days, respectively, as opposed to the current two, three, and four day performance.

Figure 13
Comparison of Operating Efficiency Indicators

<table>
<thead>
<tr>
<th>Index (1983=100)</th>
<th>1983</th>
<th>1994</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pieces of mail processed per hour</td>
<td>100</td>
<td>320.8</td>
</tr>
<tr>
<td>Points of call per hour</td>
<td>100</td>
<td>40.1</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(Can$)</th>
<th>1983</th>
<th>1995</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating revenue per piece</td>
<td>0.34</td>
<td>0.41</td>
</tr>
<tr>
<td>Operating cost per piece</td>
<td>0.34</td>
<td>0.41</td>
</tr>
</tbody>
</table>

Figure 14
Trends in Delivery Performance, 1988-95

Accessibility to the public is another important component of postal service quality. Over the years, the corporation has steadily expanded its network, thereby increasing convenience for its customers. The trend has been toward consistent growth in both the outreach of the post office in terms of delivery points, and the number of retail points through which the public can reach the postal service (see Figure 15). However, the composition of the retail network has changed over time with a decrease in the number of corporate offices and an increase in privately contracted outlets. This trend is consistent with
the corporation's philosophy of establishing alliances where they prove to be more cost effective. New access points have also become available, such as the commercial service center, which services small and medium-size businesses and displays information about the entire range of products and services offered by the corporation.

Figure 15
Network Expansion, 1983-95

Since incorporation, CPC has reduced its staff by some 10,000 employees (see Figure 16). In 1994, about 7 percent of the work force was managerial, 6 percent was administrative, and 87 percent was engaged in operational and delivery activities. An overwhelming 92 percent of the work force was unionized. The corporation is confined to using attrition and incentives for those seeking early retirement or voluntary termination because of its agreements with the labor unions. Therefore, although the corporation may wish to decrease labor costs, especially since mail processing operations have been progressively automated, this option is not available.

Figure 16
Employment Trends, 1982-95

Note: The rise in the last year encompassed CPC's acquisition of Purolator.
The third crucial objective for CPC was to involve its employees in its reform program, and to motivate them by improving working conditions and by using a process of dialogue and cooperation. In 1995 CPC's absenteeism rate averaged 9.9 days per employee (see Figure 17)—a major improvement. CPC has also worked closely with employees to review mail processing procedures in order to redistribute work hours from nights to days and to reduce weekend work without compromising efficiency or productivity. CPC has also developed a flexible Workplace Options Program aimed at adjusting work schedules to employees' particular family or health circumstances. The corporation launched the Canada Post Learning Institute in 1994 to give its employees extensive training in new skills and to give them a better understanding of the competitive and business challenges faced by the corporation. The results of these initiatives and of an improved dialogue with the unions can be seen in a drop in workplace grievances of 34 percent in 1995 over the previous year. In addition, the corporation has managed to reduce the number of unions from 29 to 4, which has greatly simplified labor negotiations.

In summary, CPC appears to have built up a modern, efficient, and reliable nationwide retail, processing, and delivery network. In addition, CPC's basic letter mail service is quite affordable. Much progress has also been made in the range of products and services offered by the corporation and in the basic quality of service. CPC has also improved its operating position through enhancing productivity and through diversifying revenue sources. To benefit from feedback, the corporation maintains its links with its customers and the community through the Postal Service Customer Councils and the Better Busi-
ness Bureaus. However, there still remain problems that CPC must resolve to fully attain its goals.

Canada was fortunate to have acknowledged the problems of its postal sector and taken action to remedy them over 15 years ago. Unlike the urgent situation that most postal sectors face today, Canada had the luxury of implementing a gradual reform process. However, while partial corporatization and commercialization have brought about distinct improvements in the Canadian postal sector, there are issues that CPC must still confront if it is to further its reform process and attain its objective of competitiveness.

Despite all of the commercial changes and the fact that Canada Post was given a financial shelter in the form of transitional government funding, tax exemption, and preferential rates for debt, and despite the fact that it was sheltered from competition through its exclusive privilege in almost half of its market, Canada Post has not been able to overcome its financial deficits on a consistent basis. As a result of these deficits, CPC’s equity holdings have been run down significantly and the corporation has become increasingly dependent on long-term debt to finance its operations and investments (particularly after government subsidization ended in 1988) (see Figure 18).

At its inception, CPC had anticipated that financial self-sufficiency would be achieved by 1987, but this is yet to happen. After achieving profitability in 1989, the corporation, with the approval of its shareholder, adopted financial performance and dividend payout ratio objectives that would enable it to be measured against established private sector companies of similar size and risk. Among the objec-

Figure 18
CPC’s Evolving Capital Structure, 1982-95
tives established was an expectation that the corporation would provide the Government of Canada with an annual dividend beginning in 1990, but this has not materialized either.\textsuperscript{22}

While CPC can claim to be the low price provider of services, it is not necessarily the low cost provider. If the two are to be reconciled, and CPC wishes to attain its financial mandate primarily through improved efficiency and market growth (as opposed to postal rate increases), there still remains considerable scope for improvement. However, CPC is caught by its commitment to the labor unions to the effect that any workforce reduction is to be achieved through attrition and not through layoffs. This prevents the corporation from cutting down on the largest component of its costs and capitalizing on its mechanization program. The corporation is also committed to (1) previously contracted cost-of-living wage adjustments, which often exceed inflation, (2) improved benefits for employees, and (3) adherence to the Public Service Superannuation Program. On the other hand, CPC is subject to the vagaries of government policy when it comes to implementing rate increases. Thus, within the current scenario it appears difficult for CPC to reduce a large component of its costs in order to attain financial self-sufficiency.

In addition, labor relations remain an ongoing problem area for CPC. Prior to incorporation, labor disruption had become the norm. While the situation has improved, CPC has nevertheless experienced four strikes since 1981. In 1988 and 1992, the corporation lost in excess of 150,000 person-days (see Figure 19).\textsuperscript{23} Given the history of Canada Post, labor relations will continue to come to the fore for two main reasons: (1) there is a large unionized workforce; and (2) the move from a government department to a competitive corporation which is market driven involves a corporate change that is far from complete. Although management recognizes the problem and is taking concrete steps to address the issue, there is still some management distrust, and the process of changing the public service mentality has been gradual. Therefore, a mixed attitude still exists in the workplace. Recently, a new era of labor-management relations has emerged as the corporation is becoming more employee-oriented. A partnership with the unions is beginning to develop though it is a long way from completion. Since the public does not differentiate between the unions and management, labor relations is regarded as a corporate problem.

Another area in which CPC has yet to reach a self-imposed goal, is in its determination to become the carrier of choice for all of Canada's information, communication, and parcel delivery needs. Under such market dynamics, it could be argued that no exclusive privileges will

\textsuperscript{22} Dividends have been paid to the government only in 1991 and 1992.

\textsuperscript{23} The corporation switched its unit on data on work stoppages from days to hours in the mid-1980s in its Annual Reports. A conversion rate of 8.04 hours per day was derived from the presentation of overlapping data for two years.
be required for any of CPC's operations. Only with complete liberalization of the postal service (which as yet has been implemented in very few countries) will CPC be truly confident of its ability to compete in the marketplace on equal terms with its competitors.

Figure 19
Work Stoppages since Incorporation, 1983-92

Person-days Lost through Work Stoppages (days in logarithmic scale)

<table>
<thead>
<tr>
<th>Year</th>
<th>Person-days</th>
</tr>
</thead>
<tbody>
<tr>
<td>1983</td>
<td>229</td>
</tr>
<tr>
<td>1984</td>
<td>199</td>
</tr>
<tr>
<td>1985</td>
<td>709</td>
</tr>
<tr>
<td>1986</td>
<td>6,485</td>
</tr>
<tr>
<td>1987</td>
<td>1,169</td>
</tr>
<tr>
<td>1988</td>
<td>173,417</td>
</tr>
<tr>
<td>1989</td>
<td>31,509</td>
</tr>
<tr>
<td>1990</td>
<td>348</td>
</tr>
<tr>
<td>1991</td>
<td>25</td>
</tr>
<tr>
<td>1992</td>
<td>168,740</td>
</tr>
</tbody>
</table>

Although external performance monitoring and public reporting of performance levels have been instituted since 1987, CPC appears to lack explicit regulation/monitoring of its quality of service.

Finally, there remain some aspects of CPC's policy environment that have handicapped the corporation's reform efforts. These aspects are reflected in CPC's complex relationship with the government, which plays the dual role of owner and regulator. Since the government is the sole shareholder, it is reasonable that CPC be held accountable to the government for its performance. This is especially true since the government has barely realized any financial returns on its contributed capital (in the form of dividends), but has experienced considerable erosion of its equity holdings because of the Post's deficits (see Figure 18). However, it should be kept in mind that one of the aims of the establishment of a Crown Corporation is to separate operations from ownership. Unless this separation is maintained, the corporation cannot truly be held accountable for its performance since it lacks the autonomy to run itself. Although in the past this has not been the case, the vesting of the government with the capacity to modify CPC's corporate plans, annual plans, operating budgets, investment plans, and the exercise of its directive pow-

24 See Chapter 4.
ers, leaves considerable potential for the erosion of CPC's autonomy in the future.

In addition to coping with the political intervention of the current power, CPC faces the additional uncertainty of changing governments and their corresponding changing philosophy toward the Post. For example, with the change to a Liberal Government in 1993, the corporation is still determining its relationship with the new government and with how this relationship will affect its mandate. To date, this government has altered CPC's philosophy on the closure of rural outlets, as a result of which CPC is exploring opportunities for marketing its retail network for other uses. In addition, CPC's most recent request for rate increases has been deferred. It is difficult for CPC to implement long-term strategies if it fears that each change in government will bring about a corresponding change in regulatory philosophies.

Conclusion

CPC has made considerable progress to date, although it is still far from fully meeting its own expectations of corporate excellence and fulfilling its stated mandate of financial self-sufficiency. Nevertheless, the drastic reduction in its deficits and the significant improvements in quality of services are substantial accomplishments. These results should not be understated, especially in light of the dismal condition that the postal sector was in when the reform program commenced.

As can be seen from this case, much can be learned from the reform program of the Canadian postal service in its transition from a government department to a competitive business. However, it should be borne in mind that there are critical differences in the reform situations of countries today. The condition of their postal sectors may be such that they do not have the luxury of the long and gradual reform process that Canada Post adopted. And the point could be taken that it is probably advisable that countries do not wait until the situation is as critical as it was in Canada when Canada initiated its reform.
The World Bank

Headquarters
1818 H Street, N.W.
Washington, D.C. 20433 U.S.A.
Telephone 202-477-1234
Facsimile 202-477-6391
Telex MCI 64145 WORLD BANK
MCI 248423 WORLD BANK
CABLE INTBAFRAD
WASHINGTON DC

European Office
66 Avenue d'Iéna
75116 Paris, France
Telephone 1-40-69-30-00
Facsimile 1-40-69-30-66
Telex 842-640651

Tokyo Office
Kokusai Building
1-1, Marunouchi 3-Chome
Chiyoda-ku, Tokyo 100, Japan
Telephone 3-3214-5001
Facsimile 3-3214-3657
Telex 781-26838