Enlargement of the EU Postal Market

Market performance, liberalization and competition in the postal sector: a comparative analysis of the ten new member states

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The Information Revolution is placing severe strains on the traditional national post office. As the pace of commerce has quickened, private express services have arisen to provide more rapid and reliable delivery services than available from the post office. Telecommunications coupled with improved printing technologies allow large mailers to bypass the first stages of postal distribution. Email has become an increasingly viable substitute for all types of letters and invoices. Corporate websites routinely handle transactions that once required several postal exchanges.

In the postal world, however, change is welcomed by few. The postal monopoly and government status have substantially insulated the post office from the larger world of commerce. Isolation has impeded the incremental changes that allow orderly transformation in most industries. Politically important groups oppose radical change. Armies of postal managers and employees fear (probably correctly) that postal modernization will mean fewer jobs and lower wages for them (although not necessarily for the sector as a whole). Citizens in rural districts believe (probably incorrectly) that adapting the post office to changing times will lead to relatively higher prices or poorer service in the countryside.

Nonetheless, in the last decade a cautious European Union has pressed a reluctant postal sector to introduce significant reform. The Postal Directive of 1997, adopted after 10 years of study and debate, placed a ceiling on the scope of postal monopolies and required tighter and more objective regulation of "universal service providers", i.e., national post offices. In 2002, the maximum scope of services that could be reserved for the national post office was lowered again, and regulatory requirements were strengthened in

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small but significant respects. Further liberalization is planned for 2006, and complete liberalization in 2009 is being contemplated, but has not yet been agreed [1].

In the long process of postal modernization, the ten "accession" countries (ACs) that joined the European Union in May 2004 present an especially interesting case. They are being required to put in place in short order reforms that western European countries have taken almost 15 to agree upon and implement. Moreover, the accession countries must introduce reforms far earlier in the natural life cycle of their post offices, for in most accession countries, the internet remains are relatively distant threat, the rivers of direct mail that help sustain the post offices in more advanced countries are unknown and use of the postal system is still increasing. If postal reforms devised in the advanced economies of Western Europe can be rapidly and successfully introduced in the relatively less advanced economies of Eastern Europe, then the lessons of postal reform developed in Europe will have earned still more general acceptance around the world.

By way of establishing a baseline for judging extension of postal reform to Eastern Europe, this article summarizes the current state of the postal systems in the ten accession countries and reviews the status of regulatory reform and competition in the region to date [2].

■ Postal markets in the ten new member states

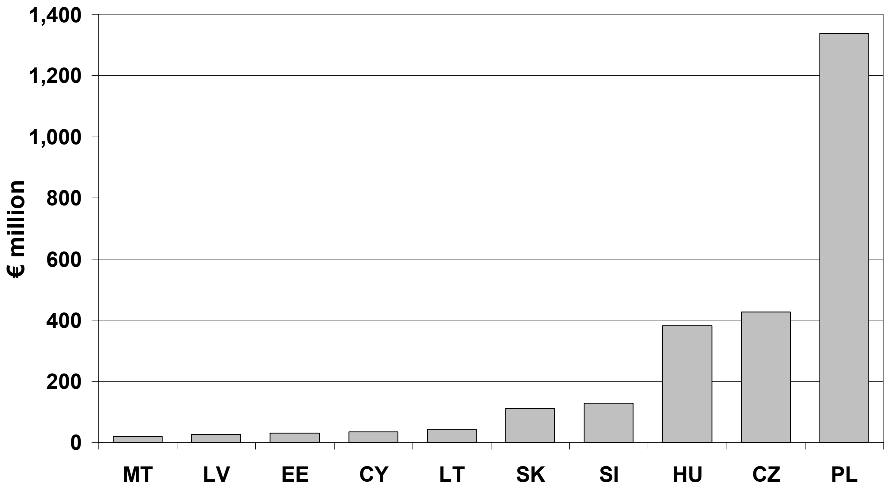
The European continent experienced a unique political and economic change when 10 central European and Mediterranean countries joined the single market of the European Union. While the EU's population increased by approximately 20 percent, total GDP increased by only 5 percent because most of the new economies are relatively less developed than those of the original EU-15 member states. This imbalance is even more

[1] Directive 97/67/EC amended by Directive 2002/39/EC. The Postal Directive suggests full liberalization for 2009, but requires the Commission to study the impact of full liberalization on universal service until the end of 2006 and then propose a (possibly revised) schedule for market opening accordingly.

[2] The analysis presented in this article is largely based on data gathered by the authors in the course of two surveys carried out for the European Commission: WIK-Consult (2003) and WIK-Consult (2004). All views and opinions expressed in this analysis are those of the authors and do not necessarily reflect the position of the Commission.

obvious in the postal sector: the addition of the ten new countries increased the Community's postal market by a mere 3 percent in terms of revenue. However, the letter post market (the most important subsegment) appears relatively more developed in terms of market volume rather than market size in terms of revenue.

Figure 1: Postal services market [(1)] by country (2002)



[(1)] Market for letter post, parcels, express services and delivery of unaddressed items.

Source: WIK-Consult, 2003

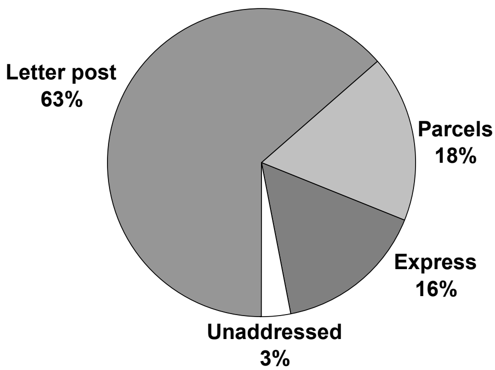
Market size by revenue

In the ten accession countries, postal services generated approximately EUR 2.5 billion revenues in 2002, about three percent of the size of the EU-15 postal market in 2000 [3]. Furthermore, the postal industry is a less significant component of total value added in the new member states than in entire Community: In the ten new members, the postal market represents about 0.57 percent of total gross domestic product (GDP) in 2002 while, in the EU-15, it contributed roughly to one percent to the Community's total GDP

3 Total revenues from postal services in the EU-15 amounted to EUR 85 billion in 2000; see Commission of the European Communities (2002).

Figure 1 illustrates the relative sizes of postal markets by revenues in the ten accession countries in 2002. The three largest countries (CZ, HU, and PL) [4] account for approximately 85 percent of the total AC market – slightly more than these three countries' share in total AC population. On the lower end, the five small Baltic (EE, LT, and LV) and Mediterranean (CY and MT) countries each generate than EUR 50 million in annual postal revenues.

Figure 2: Postal services market by submarket (2002)



Source: WIK-Consult, 2003

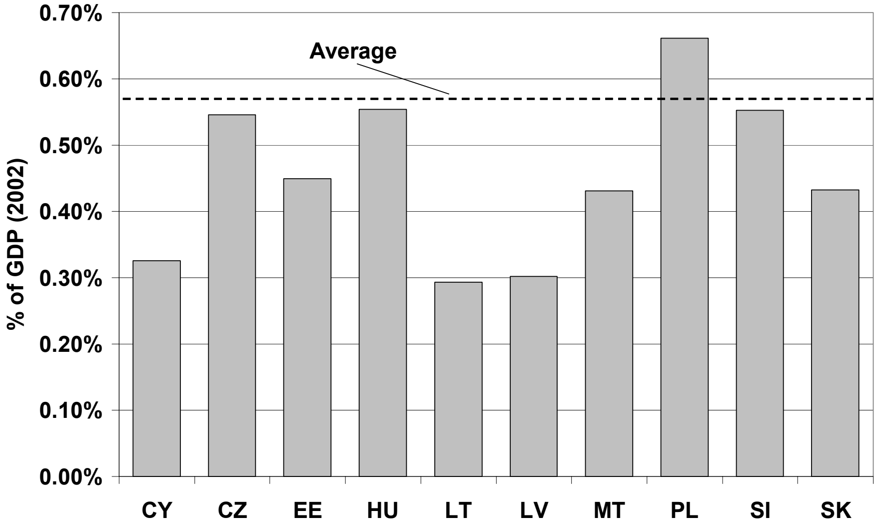
The relative importance of different postal market segments in the new member states is presented in figure 2. Letter post is the most significant postal market segment and accounts for slightly less than two-thirds of total postal revenues in the new member states. The parcel and express segments together account for roughly one-third of the postal market, while the delivery of unaddressed mail is relatively negligible.

Compared to the relative size of the submarkets for letter post, parcels and express in the entire EU-25, the letter post market appears more important in the new member states [5]. Conversely, given the high growth in the express market over the last decade, this suggests there is particular potential for further growth in the eastern European parcels and express markets.

[4] Figures in this article use the following two-digit country codes (ISO 3166-1 alpha-2): CY - Cyprus, CZ - Czech Republic, EE - Estonia, HU – Hungary, LT - Lithuania, LV - Latvia, MT - Malta, PL - Poland, SI - Slovenia, SK – Slovakia.

[5] For 2002, the EU-25 letter post market is estimated to be worth approximately EUR 52 billion (see WIK-Consult 2004) while the parcels and express market was valued at around EUR 36 billion for 2001 (see MRU 2002), yielding a ratio of 59 : 41 (letter post : parcels and express). For new member states this ratio is 66 : 34 as follows from figure 2.

Figure 3: Postal services market as percent of total GDP (2002)



Sources: WIK-Consult (2003) (for market size); Eurostat NewCronos (for GDP data)

In the EU-15, postal services were estimated to contribute slightly less than one percent to the Community's GDP in 2000. While generally below this level, the importance of the postal market to the national economy varies substantially among the new member states. As figure 3 illustrates, the postal markets in the three largest countries (CZ, HU and PL) and in Slovenia accounted for more than 0.55 percent of total GDP in 2002 while postal markets in other new member states did well to reach 0.45 percent of GDP. For example, Lithuania's postal market constituted only about 0.29 percent of total economic activity.

It should be noted that the relationship between postal revenues and GDP is significantly influenced by the price of postal services. The price level for postal services in new member states is somewhat below prices in EU-15 countries. Lower prices partly explain the apparently lower significance of the postal market in AC countries. By the same token, the apparent significance of the postal market in Poland is due in part to high postage rates. By contrast, in Slovenia, where the postal market accounts for 0.55 percent of GDP, high postal volume is somewhat masked by low postage rates [6].

[6] For detailed data on postal tariffs see WIK-Consult, 2004.

Moreover, the development of domestic express markets, a high-value segment of the postal market, may explain some of the differences between the new member states. In the large central European countries, domestic express services are more advanced due to the activities of international express companies (e.g. DHL/Deutsche Post World Net, TNT/TPG, UPS). In relative terms, the express postal markets in smaller countries are less significant even in the economically more advanced (higher GDP per capita) new member states Cyprus and Malta.

Letter post volumes

Average letter post volume in the EU-15 was 224 items per capita in 2002, while in three countries (Sweden, the Netherlands and the U. K.) per capita volume exceeded 300 items. For several decades, postal markets in Europe have experienced continuous but modest growth. However, the volume of letter post items in the most advanced postal markets declined after 2000. Although this decline may be partly due to a difficult economic environment in this period, some operators (like Sweden Post and Dutch TPG) have identified a long term trend towards the substitution of electronic communications for letter post as the major cause, and they predict further losses due to this "e-substitution".

In the ten new member states, postal volumes are well below those in the EU-15. As shown by table 1, per capita volume in 2002 exceeded 100 items in only two countries, namely Malta and Slovenia. Although mail volume per capita is often used as an index of postal development, it is generally recognised that mail volume is generated by economic activity more than by population. Postal service is primarily a business service. In the EU (old and new members combined), over three-quarters of all letter post items are posted by business senders and the "business to consumer" segment alone is estimated to account for over 60 percent of total letter post volume (WIK-Consult, 2004). It is therefore unsurprising to see lower volume levels in less developed countries (in particular the Baltic States) and higher volumes in Slovenia, the most economically advanced new member state.

Figure 4 illustrates the relationship between GDP and letter post volume. As countries become richer (moving from left to right), they typically achieve higher volumes of mail per capita (moving from bottom to top). At any given level of GDP per capita, it is plausible to suggest that a postal system with more mail per capita is more highly developed in some senses, because of better quality service or lower prices or other factors. On the other hand, it would be unreasonable to compare volumes of countries with quite different levels of GDP per capita. Figure 4 thus allows for a rough comparison of volume levels in the new member states and comparable EU-15 countries.

Table 1: Domestic letter post volumes [(1)] by country (2002)

Country		*Letter post volume (million)*	*LP volume per capita*
CY	Cyprus	52	74.1
CZ	Czech Rebublic	716 [(2)]	70.1
EE	Estonia	68	50.1
HU	Hungary	888	75.6
LT	Lithuania	40	11.5
LV	Latvia	85	32.4
MT	Malta	52	131.5
PL	Poland	1,659	42.9
SI	Slovenia	373	187.0
SK	Slovakia	236	52.4
AC-10		4,087	54.7
EU-15		84,713	223.6
EU-25		88,800	195.8

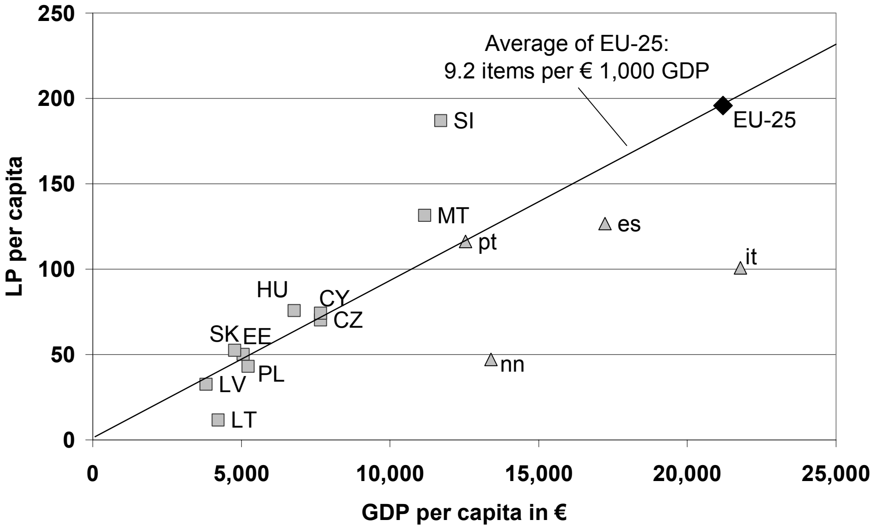
(1) Volumes carried by incumbent operators only.
(2) Volume data from UPU, 2004.

Source: WIK-Consult, 2004

The line drawn in Figure 4 from the origin through the average values for the enlarged Community represents the average relationship between GDP per capita and letter post per capita in the EU-25 (9.2 domestic letter post items per EUR 1,000 of GDP). In rough terms, any location above the line suggests a level of postal development above average taking into account differences in GDP per capita.

Overall, volume data suggest that letter post markets in most of the new member states are reasonably well developed by EU standards and indeed perform better than in some southern European countries. In particular, the figure underlines the outstanding performance of the incumbent postal operator in Slovenia and reveals successful postal operations in Malta and Hungary. At the other end of the scale, postal volumes in Lithuania appear underdeveloped in both absolute and relative terms.

Figure 4: Letter post per capita versus GDP per capita (2002)



Country codes for EU-15 (lower case): es = Spain, it = Italy, nn = confidential, pt = Portugal.

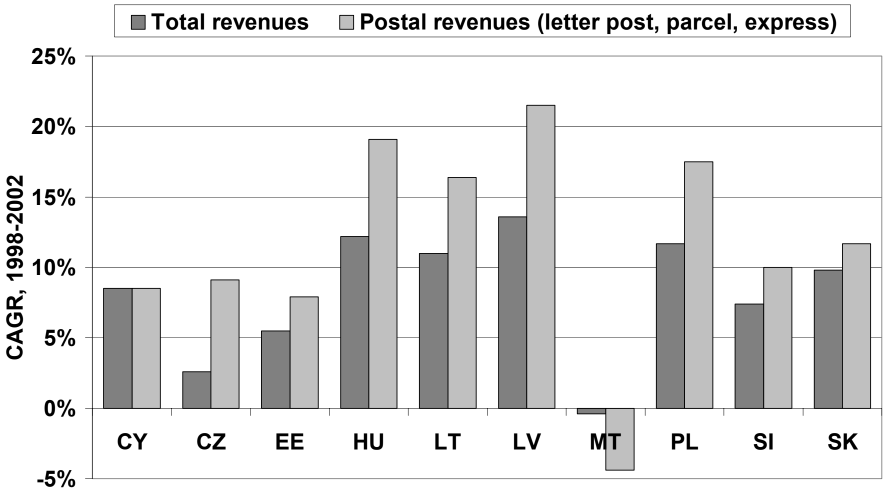
Source: WIK-Consult, 2004

Market growth

Unlike the more mature postal markets in Western Europe and North America, postal markets in the new member states have experienced impressive growth rates since 1998. While there is little information on private operators' revenues in the region; the growing revenues of national post offices imply overall market development. Since postal markets in the new member states (as in most other countries) continue to be dominated by public operators, revenue data from the post office can be assumed to reflect total market development reasonably well. Indeed, growth rates based solely on data from the incumbent public operator may understate higher growth in the market as a whole due to emerging competitive operations in the sector.

As shown by the right columns (shaded light grey) in figure 5, revenues from postal services of the ten AC post offices annually increased by an average of 14.5 percent and for most operators, increases in postal revenues exceeded total revenue growth.

Figure 5: Revenue growth of incumbent postal operators (1998-2002)



Source: WIK-Consult, 2003

Although some public postal operators in the EU-15 have sought diversification to offset stagnating postal revenues, in AC countries the core business has been the key driver of revenue growth for postal operators. However, it may be noted that some incumbent operators achieved their impressive revenue growth in part by increasing rates rather than volume [7].

In many of the new member states, the incumbent postal operator is much more than a provider of postal services, so that growth in total corporate revenues does not necessarily follow the development of the postal market. For all ten operators on average, only 53 percent of total revenues stemmed from postal services in 2002 (WIK-Consult, 2003).

The remaining revenues are primarily related to financial services offered by post offices, but incumbent operators are also engaged in various other services including the sale of retail goods and the provision of government services (e.g., distribution of licenses).

[7] For example, standard rates (for non priority) in Poland doubled from 0.55 Zloty in 1998 to 1.10 Zloty in 2003 roughly representing a 30% increase over inflation in the five-year-period. Moreover, some operators – again including Poczta Polska – recently introduced priority mail products in addition to former standard mail (subsequently called non priority) thus again increasing average revenue per mail item.

From 1998 to 2002, total revenues of incumbent operators in the region grew by over 9 percent per year on average. In this period, only Maltapost (MT) lost ground financially. At the other end of the spectrum, Latvijas Pasts (LV) grew at an annual rate of 14 percent.

■ Transformation of public operators

One after another, public postal operators in Europe have been transformed from governmental departments or semi-independent state enterprises into ordinary commercial corporations. Among the EU-15 countries, corporatization was well underway by the early 1990s. More recently, public operators in the new member states have been, or will likely soon be, transformed into commercial corporations as well.

Table 2 provides an overview of the current status of privatisation in the new member states. Most public operators have been privatised, i.e., organized as a public liability company (PLC) under normal company law. In three countries (CZ, LT and PL), the public operator has been established as a "state enterprise", a special status that gives the company operational separation from the government, but exempts the USP from some of the rules applicable to private companies. Cyprus has preserved its public operator as a government department to-date. While in some European countries, privatisation was followed by a sale of shares to the public (Deutsche Post and Dutch TPG), no such moves have been made in the new member states. However, Maltapost in February 2002 retained Transend Worldwide, a subsidiary of New Zealand Post, to a management contract which will expire in March 2005 (MITI, 2004). As part of this arrangement, Transend purchased 35 percent of Maltapost.

Many governments of the new member states are still in the process of reconsidering the institutional form of their public operators. On July 1st, 2004, Slovenská Pošta was re-established as a joint-stock company and similar steps are being discussed in the Czech Republic (Interfax Information Services, 2004; SITA Slovenska Tlacova Agentura, 2004). In addition, government discussions over postal reform are reported from Cyprus and Lithuania, but no decisions have yet been taken in these countries.

Table 2: Transformation of public postal operators

Country	*Incumbent operator*	*Legal status*
CY	Dept. of Postal Services (Ministry)	Government department
CZ	Česká Pošta	State enterprise
EE	Eesti Post	PLC (state owned)
HU	Magyar Posta	PLC (state owned)
LT	Lietuvos Paštas	State enterprise
LV	Latvijas Pasts	PLC (state owned)
MT	Maltapost	PLC (state controlled, 35% held by strategic investor)
PL	Poczta Polska	State enterprise
SI	Pošta Slovenije	PLC (state owned)
SK	Slovenská Pošta	PLC (state owned)

Source: WIK

Many AC post offices are also transforming their transportation and mail processing networks. Sorting centres have been consolidated to create sufficient volume per centre to enable the introduction of sorting machines, and transportation systems have been reorganized to reduce the number of links. In 2003, Poczta Polska operated 65 sorting centres, mostly in crowed downtown facilities without sufficient space for sorting machines; in the medium term, however, Poczta Polska plans to build 10 fully automated sorting centres in suburban locations. Similar strategies are being pursued by all of the larger central European posts. Czech Ceská Pošta and Slovenian Pošta Slovenije, in particular, have been at the forefront of network restructuring and are consequently achieving better routing times than many posts in western and southern Europe.

■ Liberalization and competition

In the EU-15, partial liberalization of postal markets was achieved only after lengthy debate. Respecting the legal principle of subsidiarity, the Postal Directive (Directive 97/67/EC), amended in 2002, required limited harmonization of Community postal services. The Directive established a gradual liberalization process by placing a ceiling on the scope of services that may be reserved for universal service providers. At present, during the second phase of liberalization, the maximum reservable area is defined by a weight limit of 100 grams and a price limit of three times the basic stamp price [8]. In 2006, both limits will be further reduced before the postal market, and postal services may be completely liberalized in 2009, following a decision by Council and Parliament. In parallel with the liberalization process, postal services in the EU have become more commercial due to the changing business attitude of public operators that have been transformed into commercial corporations, as well as to the expanding presence of private operators in the market.

By joining the EU and implementing the *acquis communautaire* in the postal sector, the ten new member states have introduced postal liberalization at a significantly faster pace. Competition has been introduced to postal markets that were both less developed than those of the EU-15 member states and less well prepared by transition periods.

Reduction of legal monopolies

As of July 2004, eight out of ten new member states had reduced their postal monopolies at least to the limits set out by the Directive. As table 3 shows, two countries have preserved a reserved area exceeding these limits: Malta and Poland, the latter having negotiated a derogation which allows to maintain a reserved area of letters up to 350 grams for a two-year transition period [9].

While most new member states have recently established reserved areas based on the maximum allowable limits, two have pushed liberalization further: Estonia entirely abolished the postal monopoly in 2001. Slovenia reduced its postal monopoly to the currently applicable weight and price limits in 2002, two years before it was obliged to do so, and has introduced a major exception to the reserved area by opening bulk mail to competition, the most attractive business segment for competitive operators.

Withdrawal of legal monopolies, however, does not necessarily open the postal market up to entrants in practice. Under the terms of the Postal Directive, a major loophole permits governments to prevent entry into the letter post market by establishing excessive conditions for licences to

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8 That is, postal services for an item of correspondence cannot be reserved for the post office if either (1) the item weighs 100 grams or more or (2) the item weighs less than 100 grams, but the price charged for the postal service is at least three times the public tariff for an item of correspondence in the first weight category of the fastest category of postal service.

9 See *Act of accession* (2003), OJ L236, 23.09.2003, p. 890.

provide universal service. Whether a specific licence condition imposes an undue burden on private operators may be a murky issue, but for purposes of summary analysis it appears sufficient to ask whether any licenses to provide non-reserved letter post service have in effect been issued.

Table 3: Legal monopolies for postal services

Country		*Weight limit*	*Price limit*	*Sole licence for universal services* [(1)]
CY	Cyprus	100 gram	3 times stamp	Yes
CZ	Czech Rebublic	100 gram	3 times stamp	Yes
EE	Estonia	No reserved area		Yes
HU	Hungary	100 gram	3 times stamp	Yes
LT	Lithuania	100 gram	3 times stamp	Yes
LV	Latvia	100 gram	3 times stamp	Yes
MT	Malta	350 gram	5 times stamp	Yes
PL	Poland	350 gram	3 times stamp	No
SI	Slovenia	100 gram	3 times stamp	No
SK	Slovakia	100 gram	3 times stamp	No

[(1)] "Yes": only one licence to provide universal services was issued (to the incumbent).

Source: based on data from WIK-Consult, 2004

The right column in table 3 therefore shows whether a country has established a licensing regime and failed to grant a licence to anybody, but the incumbent operator ("sole licence") [10]. This table reveals that in seven new member states the formal monopoly has been withdrawn for an important share of the letter post market, but at the same time, private operators are required to obtain a licence, which none of them received in practice.

Emerging competition from private operators

The obvious objective of any serious liberalization policy is to stimulate private operators to enter the market and thus to create effective competition. In the EU-15, the success of liberalization generally varies by segment: While there is substantial competition in the parcel and express segments, all incumbent operators continue to enjoy dominant positions in

10 The right column in table 3 is not intended to form any legal position on the adequacy of specific licence conditions. It merely indicates whether or not licenses were issued to private postal operators.

the domestic letter market. As in the EU-15, competition in the new member states' postal markets varies by country and by postal market segment. For each country and for the three basic submarkets, table 4 presents the estimated market shares of incumbent operators.

Table 4: Estimated market shares of incumbent postal operators by submarket

Country	*Incumbent operator*	*Letter post*	*Parcels*	*Express*
CY	Dept. of Postal Services (Ministry)	> 95%	40%	15%
CZ	Česká Pošta	> 95%	50%	10%
EE	Eesti Post	90%	65%	25%
HU	Magyar Posta	> 95%	40%	15%
LT	Lietuvos Paštas	80%	30%	5%
LV	Latvijas Pasts	90%	65%	20%
MT	Maltapost	> 95%	90%	15%
PL	Poczta Polska	> 95%	20%	5%
SI	Pošta Slovenije	> 95%	40%	30%
SK	Slovenská Pošta	> 95%	70%	15%

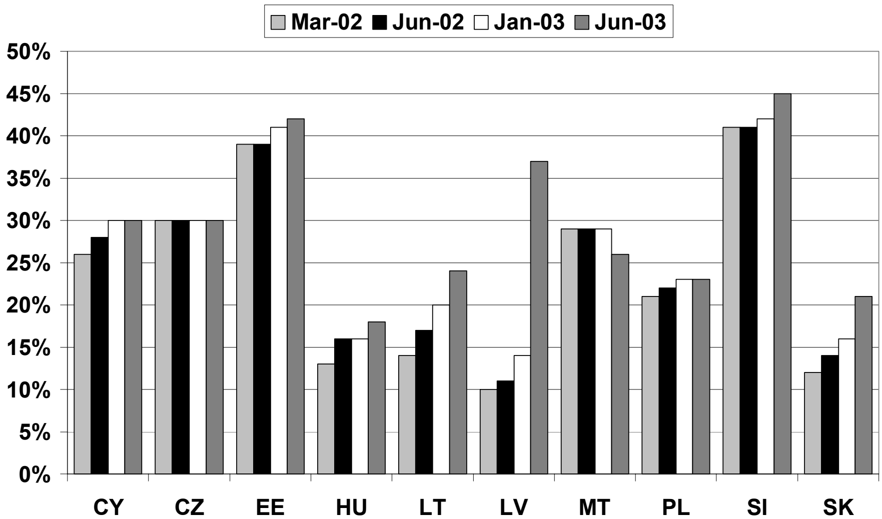
Source: WIK-Consult, 2003

The level of competition in the new member states' letter post markets is noteworthy when compared with the almost complete absence of competition in most countries. Emerging competition is reported in a number of new member states and incumbent operators in some countries appear to have lost small parts of this market, in particular in the Baltic countries. In most cases, private operators appear to be illegally intruding into the reserved area or perhaps operating in disregard of licensing requirements. In some cases, authorities seem not to enforce the monopoly effectively. This appears to be the case in Lithuania where more substantial competition in the letter market was reported that in any new member state, and there is a substantial uncertainty about the legal definition of reserved services as well as the enforcement powers of the regulatory authorities. In Estonia, many operators are reportedly providing direct mail delivery by relying on an unclear legal definition of express services.

In the parcel and express market segments there is significant competition in all new member states except Malta, where a domestic market for parcel and express services hardly exists at all because the island is so small that a potential sender can himself reach any domestic destination by car in less than an hour. The most successful public postal operators in the parcel and express markets appear to be those from Estonia and Slovenia. At the other end of the spectrum, Poczta Polska has a comparably low share of the parcels market. One reason seems to be that central Europe has become a region of special interest and extensive activities for all major European and global private operators. In addition, Poczta Polska has faced stiff competition since the late 1980s from a local parcel operator, Servisco (recently acquired by Deutsche Post World Net).

Competition from electronic media

Figure 6: Internet users' penetration (2002-2003)



Source: PWC, 2002; IBM, 2002; IBM, 2003a, 2003b

In contrast to some of the most developed postal markets, electronic substitution has not yet proven to have a negative impact on mail volumes in the growing postal markets of the new EU member states. Over the last years, different segments of the communication market have developed equally healthily. The growth of telecommunication markets, and particularly increases in mobile and internet penetration rates, appear not to have slowed postal market growth. On the positive side, some postal operators have promoted use of electronic communication by offering internet access to the public in postal outlets. In early 2003, internet usage was still relatively low in many accession countries and exceeded 40 percent only in Estonia and Slovenia. While the public postal operators in those countries may be vulnerable to substitution effects, they are also under a stronger incentive to improve their performance.

Postal operators and the digital divide

Some governments have urged that universal postal service providers should promote internet access. In particular, internet access offered in public post offices has been espoused as a means to combat the "digital divide" that (some claim) is opening between "e-literate" societies and societies relying more heavily on traditional means of communication. Should postal operators be engaged as a bridge to the broadband world or regarded as merely the "communications network of last resort"?

At first glance, the relatively dense and ubiquitous network of public post offices may seem a good way to provide free or subsidized internet access. However, it appears questionable whether postal operators have comparative advantages over the private sector in providing this public service. Anecdotal evidence suggests caution. In Germany, Deutsche Post launched a web portal combined with internet service offerings to individual customers in the late 1990s only to discontinue the service in 2002. In developing and transition countries, a World Bank publication notes that "several post offices have already tried to develop an internet access service, with few reports of success" (GUISLAIN & LEE, 2004, p. 14). To explain their lack of success, the World Bank cited limited customer demand and lack of trained staff, as well as inadequate market analysis and business plans.

Indeed, the rise of ever cheaper and more mobile means of telecommunications is also undermining the role of the post office as the communications network of last resort. The post office is increasingly being used as means of distributing mass communications, i.e., as broadcast medium rather than a medium of exchange for individualized communications. As a result, the use of mail (both sending and receiving) appears to be closely linked to income (KOLIN & DAVIS, 1999; BERTHÉLÉMY & TOLEDANO, 2000) thus contrasting its alleged importance as a "communication of last resort".

■ Conclusions

By virtue of recent accession to the European Union, the ten new member states in central Europe and the Mediterranean are facing postal modernization at a much faster pace, and at an earlier stage in postal development, than experienced in the more developed economies of Western Europe and other regions.

So far, these countries have moved quickly to adapt to the formal requirements of the European Postal Directive, most importantly by introducing more competition into postal markets. In parallel, former national post offices are undergoing substantial institutional and operational transformation to increase customer orientation and improve efficiency. While postal markets in the ten new member states remain well below European averages in terms of volumes and revenues, they are growing more quickly than their western European counterparts. Indeed, postal volumes per capita in the new member states are generally comparable to – or above – volume levels in other European countries if differences in GDP per capita are taken into account.

It remains to be seen, however, how thoroughly these new regulatory concepts will take root in the new member states and what effects reform will have on actual postal operations.

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