

THE IMPLICATIONS OF NEUTRALITY RULES:

APPLICATION TO OTHER SECTORS

**Courier, express and
parcel service**

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1. NEUTRALITY RULE IN COURIER, EXPRESS AND PARCEL SERVICE

Courier, express and parcel companies' business model is based on logistic process optimization. To this aim, they need to maximize the volume of shipments and reduce costs of classifying, collecting or delivery, which change depending on the shipment features.

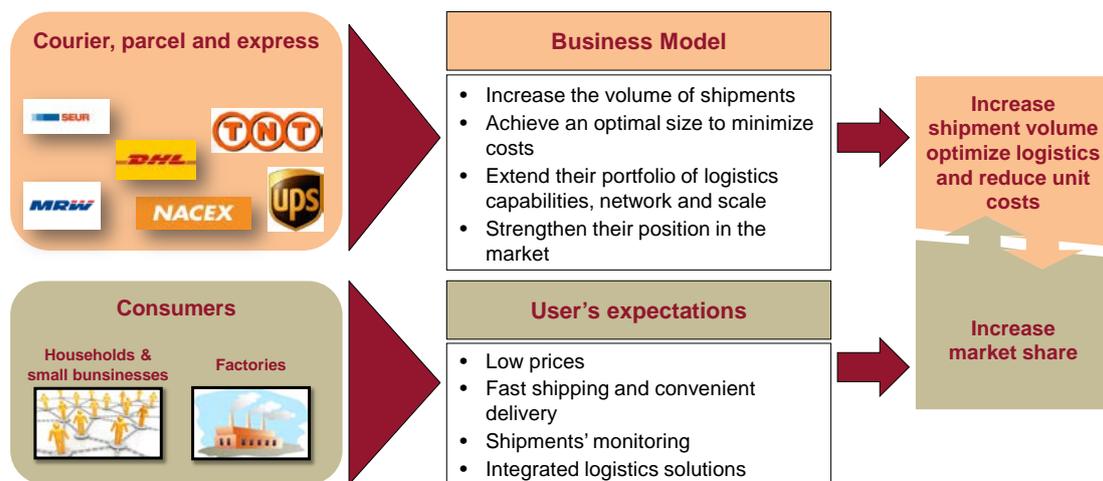
Companies seek to extend and strengthen their position in the market, by building broad coverage networks and offering integrated logistics solutions that can create value for customers.

The sector is highly competitive with a wide range of actors. Barriers of entry are small and the market is fragmented in lots of companies, resulting in a low bargaining power. To potentially overcome this situation and boost their market share, companies try to differentiate themselves from competitors by:

- Seeking competitive advantages in performance, delivery time and location.
- Extending their portfolio of logistics capabilities, network and scale.
- Adapting their business model to capture existing market opportunities or niches.

This sector also includes a broad range of commercial strategies that imply discriminatory practices towards customers. In Spain, Courier, express and parcel companies' have no significant bargaining power and cannot use commercial strategies on providers.

Figure 1: The courier, express and parcel business model diagram



Source: Created in-house.

Courier, express and parcel companies' commercial strategies for customers

Courier, express and parcel companies most common commercial strategies intend to attract customers and increase the volume of shipments. In a very competitive scenario, the aim is particularly focused on gaining market share and retaining customers.

Most strategies involve conditions suited to the cost of delivery, volume discounts, promotion initiatives within upselling or cross-selling practices and discounts to certain groups of subscribers and partners in order to attract them and increase their loyalty.

i. Different prices according to destinations: Regardless of the distance, companies offer different shipment conditions depending on the point of delivery. This strategy responds to different costs of delivery, accessibility and frequency of shipments.

ii. Volume discounts: Some companies offer their customers promotions based on the volume of shipments hired. For example 4x3 promotions in which the fourth shipment with the same conditions and features is free. These promotions are addressed to increase the shipment volume.



iii. Promotions for businesses: In exchange for an annual fee, companies may benefit from especial conditions in their shipments, such as discounts or even free shipments. These strategies ensure fixed costs recovery and reduce risk of demand.

iv. Discounts based on business customers' monthly turnover: Percentage discounts can be applied based on the business clients' turnover during a certain period of time. The higher the turnover, the larger the discount. It helps companies to improve customers' loyalty and retain market share.

Monthly turnover	Discount
< 50€	0%
50€ - 150€	15%
150€ - 250€	20%
250€ - 500€	25%
> 500€	30%

v. Discounts on optional services: Depending on the volume and frequency of shipments or in exchange for a recurrent fee, parcel companies offer optional services such as shipment insurances, proactive tracking, weekend pick up or delivery, etc. In some cases companies apply discounts on optional services under certain conditions. This strategy also helps customers' loyalty and reduces risks of demand.

vi. Promotions based on customers' features: special conditions or discounts are generally offered to customer groups such as: students, disabled people, large families, unemployed or the elderly. These promotions are commonly offered under certain conditions such as: number of shipments, volume threshold, packages' weight or shipments' distance. This allows companies



to increase their range of customers and optimize the shipments' capacity.

vii. **Special conditions applied to partners:** some courier, express and parcel companies commonly apply more appealing prices and/or better discounts in optional services to partners than to other costumers. The subscription generally consists of an annual fee. This is a loyalty strategy.

viii. **Discounts applied to online subscribers:** discounts applied to customers in exchange for their online registration on the companies' websites. This is a segmentation strategy.



ix. **Online coupons:** temporary discounts offered by companies commonly through an online intermediary in exchange for a fee. Thanks to those discounts, companies increase their market share, capturing customers from competitors. This is a segmentation strategy.

x. **Different price according to delivery-times (prioritization):** Companies charge different prices depending on the shipments' urgency and priority required by customers. The greater the customers' urgency and/or priority the higher the prices.

Application of neutrality rules in courier, express and parcel strategies

The imposition of neutrality criteria would limit business strategies of the courier, express and parcel industry. In our definition of neutrality rules we mentioned that *“when the neutrality rule is applied, all market participants must be treated equally in terms of pricing, preferences, quality, quantity and priority¹”*. **Hence, this rule would particularly mean that companies would not be allowed to distinguish among costumers’ profiles or the characteristic of each parcel (size, weigh, fragile delivery, urgent delivery, etc.).** Neutrality would interfere on industry performance and harm some users. No optimization of courier, express and parcel logistics process could be achieved and costs would increase. Final prices would also be higher.

Neutrality would specially affect other industries, such as retailing or e-commerce, that intensively use transport parcel services. As result, neutrality would have secondary effects on other good final prices and worsen other industries services.

a) Impact of neutrality rule on courier, express and parcel companies:

- It would disappears the locations with less frequent deliveries. The coverage of the distribution network would be reduced in those areas.
- Less tools to optimize logistics processes.
- Less variety of services and niche markets.
- Higher unit costs.

b) Impacts of neutrality rule on customers:

- Services in low profitable destinations could disappear.
- It would disappears promotions and discounts to some customers.
- Higher costs of the services as a result of higher unit costs.
- The quality of service for urgent and fragile packages would be worsened.
- The services in other sectors could be harmed. In particular in the commercial distribution.
- Harms on e-commerce.
- Indirect impact on other goods final prices which delivery depends on the courier, express and parcel services.

Specific effects on each commercial strategy on customers are shown in Table 1.

¹ Same shipment service regardless the characteristics or treatment of the delivery (normal, prioritised or urgent).

Table 1: Summary of marketing practices that would be prohibited if "neutrality rules" are applied and their impact on consumers

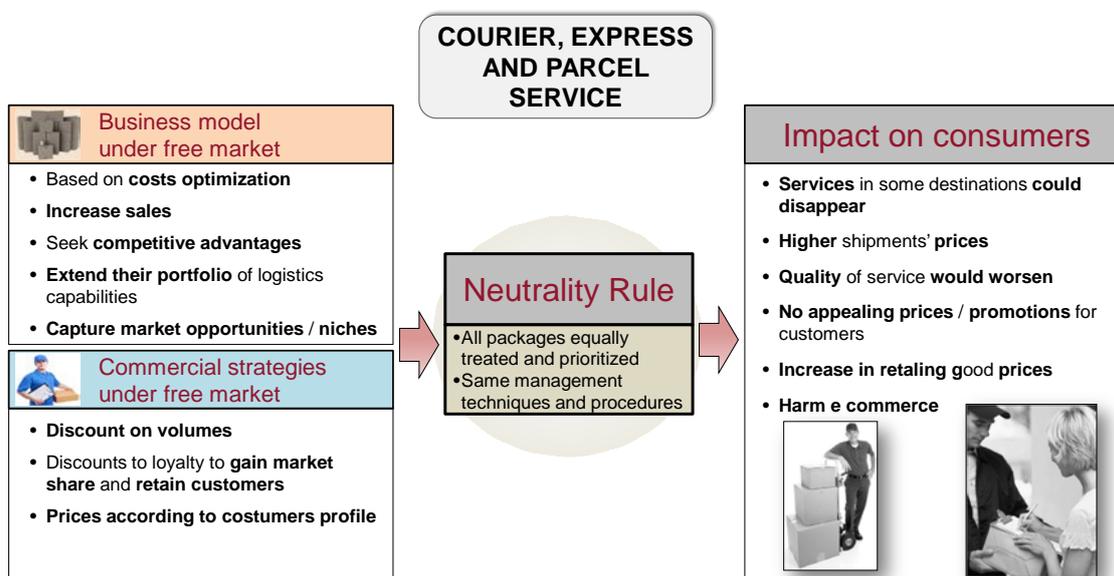
Commercial Strategy	Restrictions arising from neutrality rules	Impact on customers
<p>Different prices according to delivery-times</p> <p><i>Higher prices for the most urgent and prioritized shipments</i></p>	<p>Enforces uniform qualities for a range of similar distances</p> <p><i>No discriminatory practices among the different delivery-times / prioritization</i></p>	<ul style="list-style-type: none"> · The quality of service for the urgent and fragile packages would worsen
<p>Different prices according to destinations</p> <p><i>Prices and delivery deadlines according to location</i></p>	<p>Enforces uniform qualities for a range of similar distances</p> <p><i>No discriminatory practices among locations at the same distance</i></p>	<ul style="list-style-type: none"> · Disappearance of services provided to less profitable areas such as isolated towns · Increase in shipments' prices for low cost destination customers
<p>Discounts for businesses:</p> <p><i>Promotions for businesses in exchange for a fee</i></p> <p><i>Discounts based on business customers' monthly turnover</i></p>	<p>All market participants should be treated equally</p> <p><i>No discriminatory practices among business customers for the same shipment service</i></p>	<ul style="list-style-type: none"> · Less appealing prices for businesses · No special offers, promotions for business customers · Higher prices for the products manufactured by business customers · Higher prices for other consumer goods linked to courier, express and parcel distribution · Less e-commerce supply
<p>Promotions based on customers' features:</p> <p><i>Discounts applied to students, large families, unemployed and disabled people</i></p>	<p>All market participants should be treated equally</p> <p><i>No discriminatory practices for the same shipment service depending on customers' profile, willingness to pay or needs</i></p>	<ul style="list-style-type: none"> · No promotions for certain groups of customers
<p>Membership discounts:</p> <p><i>Special conditions applied to partners</i></p>	<p>All market participants should be treated equally</p> <p><i>No discriminatory practices depending on customers' loyalty</i></p>	<ul style="list-style-type: none"> · No promotions for loyal customers
<p>Online discounts:</p> <p><i>Discounts applied to online subscribers</i></p> <p><i>Online coupons</i></p>	<p>All market participants should be treated equally</p> <p><i>No discriminatory practices depending on customers' method to purchase services</i></p>	<ul style="list-style-type: none"> · No promotions or discounts for online customers

Main results and conclusions

If a “neutrality rule” was imposed, the equal prioritization of all packages would limit different shipment conditions. The quality of service would worsen, especially for those customers that need urgent shipments or those whose packages need a special treatment (fragile parcels).

Neutrality would limit to introduce new integrated services and options to improve logistics process. Costs would rise and quality would affect direct users and retailing industries that rely on efficient parcel services, such as e-commerce.

Figure 2: Summary of “neutrality rule” application on courier, express and parcel service industry



Source: *Created in-house.*

2. ANNEX I: DESCRIPTION OF THE BUSINESS MODEL USED BY COURIER, EXPRESS AND PARCEL SERVICE COMPANIES

In 2012, the 6.605 Spanish courier, express and parcel companies had about 58.000 people employed, 92% of firms had less than 10 employees and only 1% of the firms had more than 50 employees. Their market turnover was up to 6.230 M€ (around 0.6% of the Spanish GDP).

Courier, express and parcel industry use a wide variety of strategies to build up extensive coverage networks and offer integrated logistics solutions that can create value for customers.

i) Description of the business model, analysis of the relevant market and customer profiles

The courier, express and parcel industry refers to the activities of collection, transport and distribution of packages and documents. Depending on the product features and the customers' needs, we may find mail operators, couriers, parcel operators, freight integrators and truck companies.

According to the Antitrust Agency, their services include: collection, transport, distribution and express parcel services.

The Spanish courier, express and parcel industry is divided into the traditional services provided by the former National Post Office (Correos), and the rest of the market, attended by private firms, that together represent the 80% of the whole industry turnover.

From now onwards, we will focus in this second group, in which we distinguish two activities:

- Business parcel: is aimed at businesses and individuals. It usually consists of express services for delivering light parcels to different destinations in short periods of time using various means of transports and a wide branch network.
- Industrial parcel: is aimed at industrial companies. It includes less urgent scheduled services with variable frequency and higher weight.

The courier, express and parcel market has a national dimension. However, it has been observed an internationalization trend in the last years because of the normative harmonization process in the European Union and the evolution of the customers' needs.

The most important companies in Spain are Seur, MRW, MEX, DHL Iberia and Nacex for the business parcel, and DHL, Azkar, Integra2, Buytrago and TDN for the industrial parcel. In 2009 the 5 greatest companies represented the 38.9% of market share in

business parcel and the 44.9% of market share in industrial parcel. There are not high barriers of entry in the parcel industry; it is highly fragmented, so competition among companies is intense.

The business model consists in maximizing the volume of shipments. One of the main determinants of the size of the firms is the extension, in order to potentially exploit economies of scale, scope or density, associated to the activity (classifying, collecting or delivery) and the shipment features (letters, packages, etc.).

The demand of courier, express and parcel industry is formed by companies (large and small and medium-sized companies), self-employed and individuals. Customers can be classified into two types:

- Occasional customers: they hire this type of services occasionally. These customers are mainly individuals and small-sized companies.
- Regular customers: they have regular relationships and negotiated prices with the courier companies. These customers are mainly other firms.

The courier companies use different strategies to appeal customers, they usually provide value added to services such as package collection in convenient locations or track parcels/shipments.

ii) Revenue and cost function and profit maximization description

The revenues of the courier, express and parcel industry companies come from its normal business activities. The success of courier, express and parcel companies depend on their ability to optimize their costs by defining the best strategy for delivering the products and taking thus advantage of economies of scale, scope and density which mainly arise in the packages' delivery. Economies of scale in the delivery depend on:

- Type of product.
- Household density of the delivery area.
- Size of the delivery area.
- Delivery frequency.
- Number of delivered products at each delivery point.

Previous considerations lead us to distinguish between high-cost areas (bad connected and less densely populated areas) and low-cost areas (well-connected and high densely populated areas).

Basically, the key issue for competing in this market is to optimize their cost function, taking advantage of economies of scale, scope and density and to offer more

appealing services to customers in terms of prices and convenience, such as frequency, number of points of delivery, reliability and timing.

iii) **Description of discrimination mechanisms and effects on quantity, quality, efficiency, equity and incentives of the industry.**

Courier, express and parcel companies use commercial strategies to adjust to customers preferences and reach very competitive prices. Companies offer different prices according to the delivery costs, which depends on:

- Different prices according to destinations.
- Volume discounts
- Promotions for businesses
- Discounts based on business customers' monthly turnover
- Discounts on optional services
- Promotions based on customers' features
- Special conditions applied to partners
- Discounts applied to online subscribers
- Online coupons
- Different price according to delivery-times (prioritization)

These strategies contribute to reduce prices and diversity services to fulfill customer's needs. Considering the fact that this industry is very competitive, the discrimination of prices according to delivery costs promotes innovative services. The gain of new customers reduces unit costs, decreases prices and increases the market share.

3. ANNEX II: MAIN REFERENCES

References used for the courier, express and parcel industry

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