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How to respond to declining volumes in Postal Price Cap ?

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Discussion by Bernard ROY



- Very Clear paper, well written, and interesting to read
- Very relevant subject
- 1 st part is a survey of price caps systems in Europe since 2008 → declining volumes lead to adjustments of the « pure » formula
- 2nd part is a attempt to give practical guidance to apply « Brennan and Crew » formula



A quite simple task ... in theory !

- A price cap is a contract between the company and the regulator
- $P = RPI - X$ *X is the productivity factor*
- Problem : volume are declining and des-economies of scale offset productivity gains
- X becomes negative
- Increases of price create loss of traffic and again des-economies of scale (vicious spiral)
- X becomes « a mixture »,
 - With many parameters difficult to calculate
 - With great uncertainty over time
- Postal Regulators must be top-gun mathematicians AND possess a reliable crystal ball at the same time !



Separate the problems : use Brennan and Crew

- $P = RPI - X + Z$
 - X stays the “pure” productivity effect
 - Z is the “volume declining effects” factor
- Z encapsulates a double adjustment :
 - Increase of unit costs due to structural declining trends
 - Increase of unit costs due to price elasticity effects upon traffic
- Bender et al. propose a very elegant way to approximate Z using a « universal » cost function (Cohen et al.) and public studies on price elasticities
 - They recommend nevertheless to use more *ad-hoc* data as regulators have more refined information



three (controversial) recommendations from the authors ...

Demand elasticity of a basket is difficult to apprehend,

- the authors recommend to offset the demand effect on the Z factor

Uncertainty of traffic trends

- the authors recommend to use the passed two years instead of traffic forecasts, to give more visibility on long term

A part of the decline may be endogenous and costs savings could be made at the expense of a lower quality)

- the authors recommend to consider the mail market as a whole for the traffic volumes (USO provider + competitors).



Further remarks

- After 10 years of declining volumes, PO's are facing **the H factor**
- Human adaptation becomes more and more difficult, and creates management issues
- Innovation becomes crucial to share fixed costs, and to give hope to the employees
- La Poste launched 2 innovations last year to share fixed costs of USO infrastructure
 - « **Veiller sur mes parents** » concerns the postmen
 - “**Epreuves théoriques du Permis de Conduite**”, using the Post Offices
- In this very preoccupying period, Price cap should give a maximum of flexibility to help the USO provider to face new difficulties : the doubt on parameters should benefit the USO provider.
- Regulation is a long term relationship : Intelligent dialogue lead to intelligent decisions .



Thank you for your attention

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