

5th October 2022

Royal Mail change of holding company name to International Distributions Services plc

Introduction

Royal Mail confirmed on 4th October 2022 that it has changed its holding company name from Royal Mail plc to International Distributions Services plc.¹

From Wednesday 5th October, Royal Mail's stock market code will change from RMG to IDS, though its other codes will remain unchanged. Royal Mail said that the change will not impact on any of the company's brands which will remain the same.

The following document sets out the background and implications of this development, along with some commentary from analysts and a brief comparison with other European postal operators.

Background

Royal Mail's 1st quarter results published in July 2022 stated that the business would be changing its holding company name to reflect the group structure of two separate companies (Royal Mail and GLS).²

Explaining the reasons for the name change, Royal Mail's 1st quarter results stated:

*"Our intention is to have **clearer financial separation with no cross subsidy**, reflecting the **increased importance of GLS to the group** and our position in the wider logistics and distribution markets.*

*"In the event that significant operational change within Royal Mail in the UK is not achieved, the **Board will consider all options** to protect the value and prospects of the Group, **including separation of the two companies.**"*

Implications

Royal Mail's change of name and the rationale for this raises serious concerns for the CWU that Royal Mail Group may move to break up and sell off the most profitable parts of the business. This would prevent Royal Mail from accessing capital from GLS and may increase the risk to the future financial sustainability of the six day postal Universal Service Obligation (USO).

¹ Royal Mail confirms name change to International Distributions Services, Proactive Investors, accessed at: <https://www.proactiveinvestors.co.uk/companies/news/994411/royal-mail-confirms-name-change-to-international-distributions-services-994411.html>

² Royal Mail trading update for first quarter April to June 2022, accessed at: <https://www.royalmailgroup.com/media/11810/royal-mail-group-q1-trading-update-20-7-22.pdf>

Commentary from analysts and reporters

When Royal Mail Group announced plans for its name change in July, analysts were sceptical that a separation of GLS and Royal Mail would happen, arguing this could present problems for both businesses. For example, asset managers Hargreaves Lansdowne said:

“While the road ahead looks bumpy to say the least, if GLS and Royal Mail part ways, neither will have an easy ride. Royal Mail’s bloated cost structure will continue to be a ball and chain and GLS, while profitable, will struggle against deeper-pocketed competitors. At present the split’s just a hypothetical, and it could be a tactic management’s using to inch forward in union negotiations.”³

The reference to ‘deeper-pocketed competitors’ here is likely to be in relation to DHL and DPD which are owned by Deutsche Post and La Poste respectively. They are both state owned operators with significant market share, revenue, network infrastructure and access to state funding. Without Royal Mail, GLS would no longer benefit from the Group’s network infrastructure, economies of scale and other commercial advantages that come with being part of an integrated business.

On 19th September, investment bank JP Morgan said that a demerger was “doubtful” in the present circumstances and that the division “can likely only be separated once the UK business is in a more sustainable position”.⁴

However, on 5th October 2022, The Times published an article titled ‘Postal chief delivers threat to unions’, which argues that Royal Mail ‘has a fiduciary duty to prepare for a split’. The article quotes Keith Williams, Royal Mail Chair, as saying “Royal Mail needs GLS. GLS probably doesn’t need Royal Mail.” Williams also reportedly said of a potential break-up: “Many people thought we would not pull the labour agreements but we did. We’ve reached a crucial stage here.”⁵

Impact on the Royal Mail share price

Royal Mail’s share price has fallen by more than 60 per cent this year from a high of 526p in January to 200p today (5th October). Analysts have put this down partly to the fall in parcel volumes following the pandemic boom, and partly to deteriorating industrial relations.

Royal Mail has reportedly argued that spinning off GLS could unlock value for shareholders,⁶ and after yesterday’s announcement Royal Mail’s shares closed up 10½p, or 5.4 per cent, at 207p.⁷ There is also speculation that the potential break-up of the business is one reason why Luxembourg based private equity firm Vesa Equity has stated its intention to increase its stake in Royal Mail Group from 22% to 25%. The CWU has raised concerns directly with the Business Secretary about this issue, which is now being reviewed by the UK Government under the National Security and Investment Act.

³ Royal Mail – stalled savings mean losses mount, Hargreaves Lansdown, 20th July 2022, accessed at: <https://www.hl.co.uk/shares/share-research/202207/royal-mail-stalled-savings-mean-losses-mount>

⁴ Rival’s alert and broker warning unnerve Royal Mail investors, The Times, 17th September 2022

⁵ Postal chief delivers threat to unions, The Times, 5th October 2022

⁶ Rival’s alert and broker warning unnerve Royal Mail investors, The Times, 17th September 2022

⁷ Royal Mail makeover hints at break-up, The Times, 5th October 2022

The importance of cross subsidisation in the postal sector

The universal postal service relies on cross-subsidisation from profitable to non-profitable areas to be financially sustainable. It is also worth noting that Royal Mail has made clear in past public statements and regulatory submissions that the continued financial sustainability of the Universal Service relies on the revenue pools generated from both USO and non-USO activities.⁸ Royal Mail reported in 2017 that it commissioned a substantive piece of research on the optimum scope of the Universal Service which concludes that the business relies on revenues from non-USO commercial activities, particularly parcels, to help fund the Universal Service.⁹

Postal regulators distinguish between harmful cross-subsidisation which may undermine competition, and desirable cross-subsidisation which may be necessary to fund the postal USO and ensure social inclusion.¹⁰

The use of cross-subsidisation by other European postal operators

Other universal service providers including for example La Poste, Deutsche Post and Poste Italiane rely to an extent on cross-subsidies to fund their universal postal service. Their potential for cross-subsidisation is assisted by having maintained an integrated postal network and retaining ownership of their international logistics operations.

For example, La Poste owns DPD Group, and Deutsche Post owns DHL. Unlike Royal Mail, there has been no suggestion from La Poste or Deutsche Post that they would separate or divest their international parcel delivery operations. DPD and DHL are highly successful international parcel delivery services that generate enormous revenues each year which strengthen the overall balance sheet of La Poste and Deutsche Post.

It is also worth noting that unlike Royal Mail, many USPs (including in France, Germany and Italy) remain either wholly or part state owned. This means they benefit from public funding to help maintain the universal service. For example, La Poste provides four 'Services of General Economic Interest' for which it receives hundreds of millions of Euros in tax relief and state funding each year from the French State.

⁸ Submission from Royal Mail to ERGP (European Regulators Group for Postal Services), Letter from Royal Mail HQ 100 Victoria Embankment to Mr Cardani and Mr Hamande, 9th October 2017 (available in the public domain, accessed via Google on 5th October 2022)

⁹ Submission from Royal Mail to ERGP October 2017, *ibid*

¹⁰ ERGP report on cross subsidisation practices, 2019, accessed at:

<https://www.coursehero.com/file/105272670/ERGP-PL-II-19-40-Report-on-cross-subsidization-practices-FINpdf/>