Intelligence MEMOS

From: Glen Hodgson

To: Canada Post Clients

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Re: **What To Do with Canada Post?**

Canada Post announced in May that it generated a very large financial loss of nearly $748 million in its 2023 fiscal year, following a 2022 loss of $548 million. The corporation began recording annual losses in 2018 and has since lost $3 billion before taxes. Larger losses are projected in future years without a fundamental change in Canada Post's business model.

What should be done?

It's obvious the market for mail delivery has structurally changed. Mail delivery used to have characteristics of a natural monopoly, but there are now many possible substitutes, although not necessarily for every user. Digital technology has enabled easy mass communication like e-mail and messaging, slashing the number of letters being sent. Business mail is also down as many businesses and consumers opt for digital billing and payment. The result is much less mail delivered to households – down by around two-thirds compared to two decades ago.

In the parcel delivery market, online shopping has produced a boom in volumes shipped. Canada Post owns Purolator, which means it can generate revenue in this space, but it is a highly competitive market segment with many delivery options, from global brands to more local delivery services. The rise of online shopping has boosted parcel revenue, but Canada Post reports it costs significantly more to process and deliver parcels than mail. Growth in its parcels business is not offsetting losses from mail.

Doing the same thing is unsustainable. Canada Post and its shareholder, the government of Canada, will need to consider some key questions to keep its mandate relevant and operations affordable. Is daily mail delivery to households and businesses still an essential service that the market can't provide on its own? What services ought to be reduced? And how much are we prepared to pay?

Most consumers in urban and suburban areas have mail and parcel delivery options. However, delivery market gaps still exist in remote rural areas and for some individuals, such as those with disabilities. This context creates the risk of a very expensive business model, where Canada Post would be expected to provide essential service to remote regions and customers that would also be costly to serve. Given this reality, it makes more policy and financial sense for Canada Post to continue to provide service across the entire economy, but to do so in the most efficient way possible.

Some basic business decisions will be required to help close the financial gap. Business operating efficiency can be boosted, and Canada Post is investing significantly in improved processing automation. Other efficiency measures could be examined such as the potential for contracting out and modernization of its workplace practices.

Next, operating costs could be cut through less frequent mail delivery and by eliminating home delivery where it still exists. However, these decisions will inevitably mean difficult negotiations with the Canadian Union of Postal Workers, since reduced service would inevitably mean eliminating jobs.

What about other options for raising revenue from existing services? For example, the price of stamps could be increased significantly. However, sharply higher user prices would further encourage the shift to digital communication and bill payment, eroding baseline demand for mail services. There would also be pushback from consumers (who are also voters). Purolator cannot arbitrarily raise its parcel delivery rates as it operates in a competitive marketplace.

New lines of business could also be examined. Postal banking has been provided in other countries as a way to serve under-banked portions of the national financial services retail market. Canada generally has a well-developed financial services system and strong resistance to a postal banking option should be expected from existing banks and credit unions.

Other home-based services have been suggested, such as health checks by postal carriers on the aged and disabled. However, the ability to provide a service like health checks would depend on widespread daily home mail delivery. Training would be required for the Canada Post delivery workforce. And most importantly, who would actually pay for home health checks?

The other obvious policy option would be for the federal government to provide an explicit operating subsidy to Canada Post and expect management to limit losses to the subsidy, like the annual operating subsidy provided to other Crowns like Via Rail and the CBC.

My expectation is that the federal government and Canada Post will behave in a very Canadian manner. They will discuss and implement a mix of actions to minimize annual losses by boosting operating efficiency, reducing service costs, and enhancing revenue streams. After all the options are reviewed, I would not be surprised to see an end to the mandate for daily mail delivery, and home delivery largely eliminated. An operating subsidy may still be required from the feds to close the gap between revenues and costs, and Canada Post management would then be held to account for operating within this annual subsidy.

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