

For Information

Legislative Council Panel on Economic Services

Post Office Trading Fund Postage Revision

Introduction

This paper briefs Members on the plan of the Post Office (PO), a trading fund, to revise some postage rates in October this year. The revisions include both increases and reductions. With these revisions, the PO will anticipate an operating deficit of \$44 million in 2001-02.

The Postage Revision Plan

2. Briefly, for **local mail**, the Postmaster General (PMG) plans to **increase** postage for letters up to 50g in weight by 10 cents per letter, and for letters between 51g and 250g in weight by 20 cents per letter. In addition, local printed papers rates will be abolished, i.e. printed papers will be subject to the same rates as letters. For international mail, the plan is that for **surface mail**, postage for bulk posted bags be increased by \$4/kg. For all other types of surface mail, the plan is for an average increase of about 10%. For **airmail**, a **reduction** of 10 cents for all non-bulk items is planned. The weighted average net increase amounts to 6.5%. Details of the postage revision plans for the various categories are set out in Annexes I to IV.

3. The revision will increase the revenue of the PO by about \$59 million in 2001/02. Notwithstanding this, the PO is still projected to operate at a loss of \$44 million in 2001/02. The PMG aims to achieve full cost recovery for the loss-making mail services in phases.

Factors Taken into Account in Postage Revision

4. In determining the level of adjustment in postage rates referred to in paragraph 2 above, the PMG has taken into account the following factors.

Increase in Operating Costs

5. Postage rates were last increased in September 1996. The operating costs have since increased by about 8.6%, from \$3,341 million in 1996/97 to \$3,627 million in 2000/01. Overall increase in mail traffic of 14% over the last five years has led to increase in operating costs but corresponding revenue does not match operating cost because some of the mail services do not achieve full cost recovery.

Decrease in Revenue

6. While operating costs have increased, revenue for PO has decreased by about 19.6% from \$4,470 million in 1996/97 to \$3,596 million in 2000/01. In particular, revenue from airmail and philatelic services, which have been the two major sources of revenue subsidizing losses incurred by other mail services, has been drastically reduced in recent years.

7. In respect of airmail, due mainly to widespread e-substitution and diversion of international mail from the normal international mail exchange, revenue has dropped by over 35.9% from \$905 million in 1996/97 to \$580 million in 2000/01.

8. As regards philatelic services, although there were exceptional windfall profits in 1996/97 and 1997/98 which amounted to about \$913 million and \$1,454 million respectively, revenue has returned to a much lower level since then: \$303 million in 1998/99, \$287 million in 1999/2000 and \$127 million in 2000/01.

9. To better utilise its asset and manpower, the PO has since April 2000 introduced the PayThruPost service to accept counter bill payment for utility companies. The service will be extended to accept payment for government bills by the end of the year, and revenue is estimated to be around \$30 million per year depending on patronage.

Cross-Subsidization among Postal Services

10. Cross-subsidization has become increasingly untenable and need to be phased out for the reasons set out below.

11. At present, local mail, surface mail and miscellaneous postal services are subsidized by revenue generated by airmail, Speedpost and philatelic services. For example, the existing rates for surface mail bulk posted bags at \$26 and \$27 per kilogram for the two different postal zones are insufficient to cover the delivery payment rates charged by destination administrations at \$35 per kilogram, not to mention the conveyancing and local handling costs for these items. As revenue from the profitable services decreases, continuation of cross-subsidization has become untenable.

12. Recent changes in the payment system for the delivery of international mail by the postal administration at destination have also accentuated the need to remove cross-subsidization. It was agreed among postal administrations at the Universal Postal Union Congress held in 1999 that with effect from 1 January 2001, the despatching postal administration may request the postal administration at destination to link the rate of payment for mail delivery to the latter's domestic tariff. In the case of Hong Kong, implementation of such an arrangement would mean subsidizing overseas mailers. Although at present Hong Kong has not yet acceded to such requests, the PO expects that it will be under increasing pressure to do so.

13. It has also emerged that some overseas mail is already being diverted from the normal international mail exchange the PO has with other postal administrations to take advantage of the lower domestic tariff through bringing in international mail for direct posting at local post offices.

14. In the light of decreasing revenue from airmail and philatelic services, the prospect of the need to implement new payment system for international mail, and emerging diversion practice, there is a need to reduce cross-subsidization so as to maintain the overall viability of postal services.

The PMG aims to gradually remove cross-subsidization and achieve full cost recovery for the loss-making mail services in phases.

Operating Deficit since 1998/99

15. Post Office Trading Fund (POTF) has recorded operating deficits since 1998/99. Total operating loss for 1998/99 and 1999/2000 amounted to \$150 million and \$77 million respectively. For 2000/01, the amount of operating deficit was reduced to a projected amount of about \$32 million as a result of increase in productivity, additional profit from election postings (\$42 million) and the Hong Kong 2001 Stamp Exhibition (\$33 million). However, the PO expects that the trend of operating deficit will continue and deteriorate if the present postage rates remain unchanged. With the existing postage rates, POTF is projected to incur an overall operating loss of \$103 million for 2001/02.

Inflation

16. The weighted average increase under PO's postage revision plan, as compared with existing postage levels, is 6.5%. Compared with the postage levels after the last weighted average increase of 8.7% in September 1996, the weighted average increase would be around 3%. This is because PMG has restructured postage rates of local letters and bulk air mail in 1997 and 1998 respectively resulting in a weighted average reduction of 4% for the former and 17% for the latter.

17. The Government Economist has projected that the cumulative change in the Composite Consumer Price Index from September 1996 to September 2001 would be about -1%. However, during the same period, the Government Consumption Expenditure Deflator (GCED), which reflects the change in the costs of providing government services, is projected to increase cumulatively by about 8.2%. The weighted average increase of 6.5% is not out of line with inflation applicable to Government spending.

Abolition of local printed papers service

18. Historically, printed papers, such as advertisements, newspapers

and periodicals etc, enjoy a discount off the letter postage rates, on the assumption that they are to be posted in bulk and processed at a lower cost with longer delivery time. However, a review by the Post Office has revealed that more than 45% of the local printed papers are not posted in bulk and no operational savings could be achieved. In fact, the Director of Audit had, in 1993, queried the price differential between letters and printed papers both of which enjoy the same service standard. The Public Account Committee had also recommended a review of the price structure and service standard of the printed papers service. PO has decided that it would be more equitable to give discounts only where operational savings are achievable because of mail standardisation, mail pre-sorting, posting in bulk, lower delivery standards etc. and that the printed papers rates be abolished. In June 1997, in briefing the Legislative Council on the plan to restructure local postage rates, PMG had already indicated that the printed papers category would be phased out in due course.

19. Currently, there are printed papers rates for standard and non-standard services. Following the abolition of printed papers rates the same rates for first class and bulk economy would apply to printed papers. For items using the bulk economy service, there will only be very small increases or even reductions, depending on the weight of the individual items. There will be increase for items using the non bulk first class service. Therefore, business which rely heavily on postal service such as publishing, advertising and mail ordering could choose the service quality optimal to their requirement. The PO will also continue to provide the same discount levels currently available for pre-sorted mail and bulk postings of first class and “economy” items.

Economic Implications

20. Given that postage constitutes only a small proportion of overall household expenditure, the planned increase in postage is estimated to increase the Composite Consumer Price Index by about 0.002%. Also, postage constitutes only a small proportion of business costs in general. Thus the impact on inflation will not be significant. For businesses which rely heavily on the postal service, such as publishing, advertising and mail ordering, the impact of the planned increase in postage on them could be larger.. However, the choice of services available to these businesses as detailed in paragraph 19 above would help minimise such impact.

Background

21. On 19 July 1995 the Legislative Council passed a Resolution under the Trading Funds Ordinance (Cap. 430) to establish the POTF. The PMG is the general manager of the trading fund and the management will retain the trading fund revenue to finance the cost of service provision on a financially autonomous basis.

22. Section 6 of the Trading Fund Ordinance requires the general manager to manage a trading fund with the objectives of -

- (a) providing an efficient and effective operation that meets an appropriate standard of service;
- (b) within a reasonable time, meeting expenses incurred in the provision of the government service and financing liabilities of the trading fund out of the income of the trading fund, taking one year with another; and
- (c) achieving a reasonable return, as determined by the Financial Secretary, on the fixed assets employed.

In moving the resolution for establishing the POTF in July 1995, the Administration undertook that future postage rate increases would be broadly in line with inflation.

23. For the past four years, the PO has been able to deliver over 98% of locally posted letters to addressees by the following working day. It has also taken a number of productivity measures. Productivity index in terms of “handling rate per man-hour” increased by 7.4% over the last five years. According to the public perception survey conducted by an independent consultant in March 2000, PO now ranks second amongst all the best service organizations in Hong Kong, up from third place in 1999.

Economic Services Bureau/
Hong Kong Post
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**Local Mail - First Class and Bulk Economy Letters and Cards
(October 2001)**

Annex I

Non Bulk First Class

Weight Step	Postage Rate		
	First Class		
	Existing	New	Increase
gm	\$	\$	\$
Standard			
30	1.30	1.40	0.10
50	2.10	2.20	0.10
Non-Std			
30	1.30	1.40	0.10
50	2.10	2.20	0.10
100	2.80	3.00	0.20
150	3.50	3.70	0.20
200	3.80	4.00	0.20
250	4.20	4.40	0.20
500	8.20	8.20	-
1,000	16.40	16.40	-
2,000	28.00	28.00	-

Bulk First Class

Weight Step	Postage Rate								
	Non Presort			Presort to Delivery Office			Presort to Postman's Route Beat		
	Existing	New	Increase	Existing	New	Increase	Existing	New	Increase
gm	\$	\$	\$	\$	\$	\$	\$	\$	\$
Standard									
30	1.20	1.30	0.10	1.20	1.30	0.10	1.00	1.08	0.08
50	1.90	2.00	0.10	1.90	2.00	0.10	1.53	1.61	0.08
Non-Std									
30	1.30	1.40	0.10	1.20	1.30	0.10	1.00	1.08	0.08
50	2.10	2.20	0.10	1.90	2.00	0.10	1.53	1.61	0.08
100	2.80	3.00	0.20	2.52	2.70	0.18	2.24	2.40	0.16
150	3.50	3.70	0.20	3.15	3.33	0.18	2.80	2.96	0.16
200	3.80	4.00	0.20	3.42	3.60	0.18	3.04	3.20	0.16
250	4.20	4.40	0.20	3.78	3.96	0.18	3.36	3.52	0.16
500	8.20	8.20	-	7.38	7.38	-	6.56	6.56	-
1,000	16.40	16.40	-	14.76	14.76	-	13.12	13.12	-
2,000	28.00	28.00	-	25.20	25.20	-	22.40	22.40	-

Bulk Economy

Weight Step	Postage Rate								
	Non Presort			Presort to Delivery Office			Presort to Postman's Route Beat		
	Existing	New	Increase	Existing	New	Increase	Existing	New	Increase
gm	\$	\$	\$	\$	\$	\$	\$	\$	\$
Standard									
30	1.15	1.25	0.10	1.15	1.25	0.10	0.92	1.00	0.08
50	1.75	1.84	0.09	1.75	1.84	0.09	1.42	1.49	0.07
Non-Std									
30	1.20	1.29	0.09	1.15	1.25	0.10	0.92	1.00	0.08
50	1.85	1.94	0.09	1.75	1.84	0.09	1.42	1.49	0.07
100	2.35	2.52	0.17	2.12	2.27	0.15	1.88	2.02	0.14
150	2.90	3.07	0.17	2.61	2.76	0.15	2.32	2.46	0.14
200	3.15	3.32	0.17	2.84	2.99	0.15	2.52	2.66	0.14
250	3.45	3.61	0.16	3.11	3.25	0.14	2.76	2.89	0.13
500	6.90	6.90	-	6.21	6.21	-	5.52	5.52	-
1,000	11.00	11.00	-	9.90	9.90	-	8.80	8.80	-
2,000	22.00	22.00	-	19.80	19.80	-	17.60	17.60	-

**Local Mail - Options available to users
after abolition of Printed Papers rates
(October 2001)**

Annex II

Option 1 Printed Papers posted as non bulk first class Letters

Weight Step	Postage Rate		
	Existing	After Abolition	Increase
gm	\$	\$	\$
Standard			
30	1.20	1.40	0.20
50	1.80	2.20	0.40
Non-Std			
30	1.30	1.40	0.10
50	2.10	2.20	0.10
100	2.40	3.00	0.60
150	3.00	3.70	0.70
200	3.20	4.00	0.80
250	3.50	4.40	0.90
500	7.20	8.20	1.00
1,000	11.50	16.40	4.90
2,000	-	28.00	-

Option 2 Printed Papers posted in Bulk Economy Class

Weight Step	Postage Rate								
	Non Presort			Presort to Delivery Office			Presort to Postman's Route Beat		
	Existing	After Abolition	Increase (decrease)	Existing	After Abolition	Increase (decrease)	Existing	After Abolition	Increase (decrease)
gm	\$	\$	\$	\$	\$	\$	\$	\$	\$
Standard									
30	1.20	1.25	0.05	1.08	1.25	0.17	0.96	1.00	0.04
50	1.80	1.84	0.04	1.62	1.84	0.22	1.44	1.49	0.05
Non-Std									
30	1.30	1.29	(0.01)	1.17	1.25	0.08	0.96	1.00	0.04
50	2.10	1.94	(0.16)	1.89	1.84	(0.05)	1.44	1.49	0.05
100	2.40	2.52	0.12	2.16	2.27	0.11	1.92	2.02	0.10
150	3.00	3.07	0.07	2.70	2.76	0.06	2.40	2.46	0.06
200	3.20	3.32	0.12	2.88	2.99	0.11	2.56	2.66	0.10
250	3.50	3.61	0.11	3.15	3.25	0.10	2.80	2.89	0.09
500	7.20	6.90	(0.30)	6.48	6.21	(0.27)	5.76	5.52	(0.24)
1,000	11.50	11.00	(0.50)	10.35	9.90	(0.45)	9.20	8.80	(0.40)
2,000	-	22.00	-	-	19.80	-	-	17.60	17.60

International Mail - Bulk Bag and Surface Mail
(October 2001)

Annex III

Bulk Bag

	Postage Rate					
	Zone 1			Zone 2		
	Existing	New	Increase	Existing	New	Increase
per kg	\$ 26.00	30.00	4.00	\$ 27.00	31.00	4.00
per item	0.60	0.60	-	0.60	0.60	-
min-charge	1.20	1.20	-	1.30	1.30	-

Surface Mail (except China, Macau & Taiwan)

Letters and Cards

Wt Step (gm)	Postage Rate					
	Zone 1			Zone 2		
	Existing	New	Increase	Existing	New	Increase
	\$	\$	\$	\$	\$	\$
20	2.30	2.50	0.20	2.60	2.90	0.30
50	4.00	4.40	0.40	4.50	5.00	0.50
100	5.30	5.80	0.50	6.00	6.60	0.60
250	10.50	11.60	1.10	11.90	13.10	1.20
500	20.50	22.60	2.10	22.50	24.80	2.30
1000	36.00	39.60	3.60	39.00	42.90	3.90
2000	60.00	66.00	6.00	62.00	68.20	6.20

Printed Papers

Wt Step (gm)	Postage Rate					
	Zone 1			Zone 2		
	Existing	New	Increase	Existing	New	Increase
	\$	\$	\$	\$	\$	\$
20	1.90	2.10	0.20	2.30	2.50	0.20
50	3.70	4.10	0.40	4.00	4.40	0.40
100	4.70	5.20	0.50	5.10	5.60	0.50
250	9.60	10.60	1.00	10.40	11.40	1.00
500	18.00	19.80	1.80	19.00	20.90	1.90
1000	32.00	35.20	3.20	34.00	37.40	3.40
2000	47.00	51.70	4.70	50.00	55.00	5.00
extra 1 kg	23.50	25.90	2.40	25.00	27.50	2.50

Surface Mail to China, Macau & Taiwan

Wt Step (gm)	Postage Rate					
	Letters and Cards			Printed Papers		
	Existing	New	Increase	Existing	New	Increase
	\$	\$	\$	\$	\$	\$
20	1.60	1.80	0.20	1.40	1.50	0.10
50	2.70	3.00	0.30	2.20	2.40	0.20
100	5.20	5.70	0.50	3.00	3.30	0.30
250	10.40	11.40	1.00	6.30	6.90	0.60
500	20.10	22.10	2.00	11.70	12.90	1.20
1000	35.00	38.50	3.50	20.00	22.00	2.00
2000	54.00	59.40	5.40	30.00	33.00	3.00
extra 1 kg				15.00	16.50	1.50

Small Packets

Wt Step (gm)	Postage Rate		
	Existing	New	Increase
	\$	\$	\$
100	5.10	5.60	0.50
250	10.40	11.40	1.00
500	19.00	20.90	1.90
1000	34.00	37.40	3.40
2000	50.00	55.00	5.00

International Mail -Air Mail
(October 2001)

Annex IV

Air Mail Letters & Cards

Weight Step (gm)	Postage Rate					
	Zone 1			Zone 2		
	Existing	New	Decrease	Existing	New	Decrease
	\$	\$	\$	\$	\$	\$
Aerogramme	2.30	2.30	-	2.30	2.30	-
Not over 20g	2.50	2.40	(0.10)	3.10	3.00	(0.10)
Not over 30g	4.60	4.50	(0.10)	5.40	5.30	(0.10)
Each additional 10g	1.20	1.20	-	1.30	1.30	-

Air Mail Printed Papers and Small Packets

Weight Step (gm)	Postage Rate					
	Zone 1			Zone 2		
	Existing	New	Decrease	Existing	New	Decrease
	\$	\$	\$	\$	\$	\$
Not over 20g	2.00	1.90	(0.10)	2.60	2.50	(0.10)
Not over 30g	3.20	3.10	(0.10)	4.20	4.10	(0.10)
Each additional 10g	0.80	0.80	-	1.00	1.00	-