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Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

29 January 1985

The Rt. Hon. Norman Tebbit MP
Secretary of State for Trade and Industry

Handwritten signature: Norman

POST OFFICE: 1984 CORPORATE PLAN AND OBJECTIVES

You wrote to me on 23 July with some draft objectives for the PO and Geoffrey Pattie subsequently wrote to me on 10 January about the PO's 1984 Corporate Plan. There is a strong connection between these two matters and this letter therefore addresses both.

I share Geoffrey's disquiet about the quality of the 1984 Corporate Plan and the time it has taken to circulate it to colleagues. I agree that Ron Dearing should be told of our concern and, more positively, should be given a clear indication of the kind of analysis we expect in a Corporate Plan and the options and policies which should be appraised. By setting challenging and unambiguous objectives we can convey clearly the direction and policies we wish the postal business to follow and also establish a framework in which the PO can construct their Corporate Plan. Setting appropriate objectives is an essential step if the PO are to be in a position to make good some of the deficiencies in the 1984 Plan.

My main reservation about both the draft objectives attached to your July letter and the summary of the Corporate Plan attached to Geoffrey Pattie's letter is that neither gives enough prominence to some of the important policies which we are expecting the PO to pursue. There is, for example, no reference in either document to the goals of privatisation and the introduction of private capital into the PO. I accept that the PO is not an obvious candidate for early and wholesale privatisation. However, the industry's objectives and the Corporate Plan should both look beyond the short term. If the PO are ever to benefit from more direct exposure to the market, we should surely be encouraging their management to focus now on the possibilities for introducing private capital into their business activities. But if their objectives make no mention of this, the PO will certainly not feel obliged to consider it.

The draft objectives also make no reference to the PO progressively separating their principal constituent businesses as a move towards identifying candidates for privatisation or for joint ventures for the private sector, yet I believe we both considered they should do just this. Publishing separate, audited accounts for Counters and the Royal Mail would be a positive step in this direction. If you agree, I suggest we should set the PO the specific objective of publishing separate accounts for the Counters and Mails businesses to fully audited standards from 1986-87. The 1985 Corporate Plan could then review progress. Separate Corporate Plans for Counters and Mails might also now be appropriate.



Finally, I think it wrong that the objectives and the Corporate Plan should tacitly assume that the postal monopoly is a permanent feature of the communications industry. I would prefer explicitly to leave open the possibility of some relaxation of this monopoly if circumstances in the future were to suggest that this would encourage new and competing services and technologies to be developed. I suggest that the PO should be asked to justify the continuation of the postal monopoly in their next Corporate Plan and to consider the alternatives.

... I enclose a revised set of objectives for the PO. You will see that it builds on your original draft but also incorporates the important aims which I have identified above. Most of the changes (all underlined) are to Section 5 of your draft but I have also proposed some smaller changes elsewhere. I hope you will agree that this draft accurately reflects our objectives for the PO and is consistent with the form and style of the objectives which have been settled with the Chairmen of other nationalised industries. I believe these objectives set a more challenging framework for the 1985 Corporate Plan and should lead to less complacency in its analysis of policy options.

May I also make some further comments on the proposed strategies which have emerged from the 1984 Plan? The plan for the Royal Mail which Geoffrey Pattie is proposing to approve appears essentially to aim for volume growth through vigorous marketing. But I have some reservations.

The 1984 Plan does not appear to have reviewed thoroughly some of the other options - in particular, whether a more efficient service could be offered by relaxing the postal monopoly to allow greater competition with private sector operators. I am concerned that without this analysis we do not have a proper basis on which to take strategic decisions.

I am also not yet satisfied that this strategy of growth can be justified in robust financial terms. You will recall that the MMC Report on the Letter Post Service published last September suggested that the PO's appreciation of the marginal costs and marginal revenues of their operations was inadequate and while this situation remains, I do not see how we can sensibly approve a strategy of volume growth. (Incidentally, if you agree with the proposals for following up MMC reports in my letter to you of 11 January, we might make a start by applying my suggestions to this report on the Letter Post Service. As an immediate step, we might tell the PO that we expect them to report on the progress made towards implementing the MMC recommendations in the 1985 Plan.)

As a result, I believe it would be premature to endorse the proposed strategy for the Royal Mail. We must surely wait until the PO have presented a more rigorously constructed Corporate Plan and can justify their recommended strategy in concrete financial terms. I imagine you will want to give the PO a clear message to this effect.

I am generally content with Geoffrey's proposal to accept the strategy for Counters on an interim and short term basis. I understand that the Counters' automation proposals have been expected for some time and we shall need to ask the PO to explain the delay in the 1985 Plan if there is any further slippage beyond this Spring. I think we should also ask the PO to consider in the 1985



Plan the alternatives to automation for achieving reductions in costs. These might include a review of the scale of the rural and urban networks and the cost savings which might reasonably be achieved through some intensification of the closure programme.

I agree that it would not be particularly useful for E(NI) to discuss the 1984 Plan now. However, I am sure we should aim for an E(NI) discussion of the 1985 Plan based on an appropriate set of objectives, requiring the PO to appraise a more thorough range of policy options. I suggest that arrangements are made now for an E(NI) meeting on the PO before the Summer Recess.

The summary of the performance review attached to Geoffrey's letter seems thorough and comprehensive and I hope this year's Review will maintain the same standards.

Finally, I recall from your IFR discussions with Peter Rees in September that you were shortly to make proposals for profit and efficiency targets for the PO which would take effect once the present targets expire at the end of March. It would be helpful if you could give us an early indication of your proposals as time is short and we do not want the PO to enter a new financial year without agreed targets in place.

I am copying this letter to the other members of E(NI) and to Sir Robert Armstrong.

NIGEL LAWSON

A handwritten signature in dark ink, appearing to read "Nigel Lawson", with a long horizontal flourish extending to the right.

POST OFFICE OBJECTIVES

For each of the Post Office's main business activities the objectives are as follows:-

1. INLAND LETTER BUSINESS OBJECTIVES

- 1.1 To make a profit each year.
- 1.2 To give good value for money by providing the quality and standards of service at the levels for which customers may reasonably expect to pay.
- 1.3 To increase the efficiency and cost effectiveness of the service and adapt it to maintain the business's competitive price position in the communications industry.

2. OTHER MAILS SERVICE OBJECTIVES

- 2.1 To provide a range of complementary communications and distribution services, consisting of Royal Mail International, Royal Mail Parcels, and Premium service activities.
- 2.2 To make a profit from each of these three business activities.
- 2.3 To provide service standards that meet customer demand within a competitive market.

3. COUNTER SERVICE BUSINESS OBJECTIVES

- 3.1 To make a profit each year.
- 3.2 To provide efficiently and economically, financial transactions, information and other related services to meet the needs of all Agency customers, National Girobank and the Mails business.
- 3.3 To adapt service and operations to changing market demands, taking appropriate advantage of opportunities offered by technology.
- 3.4 To provide efficient services in an attractive customer environment.

4. BANKING OBJECTIVES

4.1 To make a profit each year sufficient at least to comply with financial targets agreed with the Government.

4.2 To provide a competitive, nationwide banking service to both personal and business customers using post offices as branch outlets, and to **pursue a policy of profitable growth** within the framework of prudential ratios determined by the Bank of England.

5. In pursuing these business objectives, the Post Office will act within the framework of a Corporate Plan reviewed annually by Government and with recognition of its statutory and public service obligations, mindful of its special responsibilities where it provides a monopoly service, and will meet its financial and other targets and act within borrowing limits agreed from time to time with the Government.

In support of the business objectives, the Post Office will:

5.1 seek to realise the full potential of its workforce within a framework of good staffing practices;

5.2 improve the efficiency with which the resources are used and in support of that pursue a well conceived investment programme to take appropriate advantage of technological advances;

5.3 reduce the cost of services, measured in constant prices, by improved efficiency;

5.4 develop its business in accordance with changing customer needs, seeking opportunities for profitable growth at fair prices;

5.5 within the framework of its statutory powers, seek profitable new business opportunities through vigorous marketing, either on its own account or in association with other enterprises.

5.6 The Post Office should continue the functional separation of its constituent businesses of Royal Mails, Counter Services and National Girobank. The necessary management and organisational changes should be reflected in the Post Office's published accounts and in the financial and performance targets set by the Government. The Post Office should

publish separate accounts for the three constituent businesses to fully audited standards in 1986-87 and thereafter.

5.7 The Post Office should consider the possibilities for further introduction of private capital into any of its business activities and should make recommendations to Government from time to time. The Post Office should also consider the possibilities for establishing wherever appropriate separate subsidiaries as candidates for privatisation or joint ventures with the private sector and make recommendations to Government.

5.8 The Post Office should continue to appraise the scale and nature of its network and postal monopoly against the background of technological and other developments to ensure a proper and balanced evolution of its ability to offer efficient and cost effective services.

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From the Minister of State
for Industry and Information Technology

GEOFFREY PATTIE MP

Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

10th January 1985

Dear Chancellor,

POST OFFICE POSTAL BUSINESS: CORPORATE PLAN

I attach summaries of the Post Office Postal Business Corporate Plan, Environmental Review and Performance Review.

The Plan for Mails envisages a strong marketing effort in order to secure the growth that is necessary for a largely fixed cost business; the continuing development and application of new technology; and a serious attack upon the labour costs which account for approximately three-quarters of total current expenditure. The Post Office is hopeful of a major breakthrough on this front at the UCW Special Conference called for 4 and 5 March with a view to overturning previous Conference decisions which are preventing progress in negotiations of new working arrangements. I propose to tell Sir Ronald Dearing that I approve the strategies set out in the Plan as being appropriate for the Mails business in the medium-term.

The plan identifies the automation of the network as the key strategy for the Counters business and describes a holding operation in terms of containing and reducing costs through efficiency improvements and network closures in advance of a full automation appraisal. In a sense therefore it is an interim Plan pending the major decision on automation. I understand that the Post Office hopes to bring forward proposals in the spring. It would be my intention to tell Sir Ronald that I approve this plan for Counters as a short-term strategy but that I would expect to see a fully-worked up appraisal for automation in the spring and that this should be set in the context of an overall medium-term strategy.

I also intend to tell Sir Ronald that the form and timing of this year's Plan left something to be desired. I expect to see future

JA2/JA2AAD



plans submitted on time. I also regard the lack of a visible link to the Environmental Review and the complete absence of strategic alternatives in key areas as weaknesses. I would also intend to draw his attention to the inadequacy of the supporting data which led to considerable delays in considering this year's Plan.

I do not believe that it is necessary for E(NI) to meet to discuss this Plan unless you or other members of E(NI) wish to do so. I should therefore be grateful for your views and those of E(NI) colleagues to whom I am copying this letter and, in particular, for an indication that you are content for me to proceed on the basis that I have outlined.

Yours sincerely,

Timothy Abraham

PP. GEOFFREY PATTIE

(Approved by the Minister
and signed in his absence)

M12/M12AES

POST OFFICE CORPORATE PLAN 1984: SUMMARY OF KEY BUSINESS STRATEGIES

ROYAL MAIL

The essential strategy is to market for growth while seeking to contain costs and improve quality of service.

The Royal Mail is aiming for volume growth of 10% in inland letters, 25% in inland parcels, and substantial Datapost growth. Royal Mail International will seek real revenue growth.

As well as growing in traditional markets, the Royal Mail will develop its range of services to meet customer needs; Premium Services will be developed further; the Argonaut freighting service will be extended; and Royal Mail Parcels will continue to adapt to meet the demands of businesses.

The Royal Mail recognises the essential importance of high quality, reliable service in its drive to expand business. Service has improved in the last year, but targets have not yet been achieved. Major revisions to network and scheduling arrangements along with other improvements will be introduced to ensure that high quality service can be given. Attention will be paid to reducing damage levels for parcels.

The strong growth in Royal Mail volume, together with the target of providing consistently high quality of service will require some additional expenditure on staff^{and} conveyance. However, fixed costs - such as collections and to some extent, deliveries-absorb volume growth and this leads to increased productivity. Improved management information systems, national productivity schemes, new Organisation and Methods initiatives and the completed arrangements for mechanised letter sorting will also contribute to improved efficiency and service. The Plan looks forward to a major programme of work and effort to achieve an overall improvement in Royal Mail productivity of 10%, whilst recognising that such an increase has yet to be validated by detailed evaluation of opportunities.

COUNTER SERVICES

The essential strategy is the automation of the counters network which will offer opportunities for both a wider range of services and efficiency gains. The interim strategy is to seek to hold or increase overall volume while looking to cut back on costs through a reduction in the size of the network and continued gains from the counters productivity scheme.

Counter Services' traditional products - the supply of Government department business (55%) and Royal Mail services (22%) - cannot offer on their own significant growth opportunities. However, growth will come from National Girobank and from providing a widely available cash-issue service on behalf of financial institutions, through the Counter Automation programme, and conceivably through the provision of information services for which counter automation could qualify Counter Services eg the provision of up-to-date information on jobs.

The standards of service provided by Counter Services must be balanced with the need for efficiency. The Plan gives an indication of possible reductions in the numbers of town sub-offices over a three year period consistent with the public statements made on the counters network. Such reductions would be to protect the unique national coverage of the Counter Services network, preserving service in rural areas and retaining the level of urban provision above public standards. The customer environment in offices will be improved to bring the image of Counters up to modern standards to attract customers.

Counter Services plan to reduce costs through the basic grades (PO/PA) productivity scheme and O&M techniques. Economies will also be achieved from the application of published standards to the network of urban offices.

THE POST OFFICE: POSTAL BUSINESS: ENVIRONMENTAL REVIEW 1983

Three main themes emerged from the Review:

- That the Post Office's markets are coming under apparently increasing threat, both from rivals for conventional services as well as those based on new technology; the Counters in particular feel the need for unprecedented and quick change;
- that information technology and its effects on the communications market have the potential to increase the synergy between the three main businesses - Mails, Counters and Girobank;
- that to meet this situation, the Post Office must seek more than ever to "control its destiny in the market place; and welcome change under strong leadership".

The Review therefore proposes that, while there must be distinct action plans for each business, there should be a clear long-term strategy for the Corporation as a whole.

Economic assumptions included in the plan are unemployment in the range of 2 million to 4 million with the result that the Post Office will not suffer shortages of labour; an average annual rise of from 1 to 3% in output of the service sector with communications likely to continue to be a growth area of the economy; with a full supply of labour and slow growth in GDP, real wages to rise only perhaps in the range of $\frac{1}{2}\%$ to $1\frac{1}{2}\%$ a year.

The Review foresees the prospect of dynamic and possibly exponential growth in communications but suggests caution in forecasting rapid growth. The Review forecasts a mid-point view that the letter service in its conventional form has the prospect of a modest increase in volume for 3-5 years but thereafter volume could begin to decline.

The Review sees the Counters business as being under particular threat from the advance of information technology and from a decline in its traditional markets particularly for Government agency work. It sees the Counters as having certain unique advantages but to capitalise on these, the business needs to reduce its unit costs; to automate its transactions; to widen the range of its activities and consolidate its Government business; and to review the appropriate size of the network.

SPF2/DTI

December 1984

POST OFFICE

POSTAL BUSINESS PERFORMANCE REVIEW - 1984

Background

1 This review covers the period 1978/79 to 1983/84.

2 The Post Office currently comprises three main businesses - the Royal Mail, Counters and National Girobank. Telecommunications was formed into a separate corporation as a result of the 1981 Act. The Post Office was a Government Department until 1969 but has been in state control since the sixteenth century. The postal business has been run on the basis of one corporation until recently when board and management changes were introduced designed to create more distinct identities for the mails and counters business. The changes have been supported and encouraged by the DTI who will be pressing the Post Office to move quickly to the stage of separate formal accounting for the three businesses and Companies Act company subsidiary status for Counters and Girobank.

3 Draft objectives for the Post Office Corporation were sent by the Secretary of State to the Chancellor for comment on 23 July 1984.

4 The Post Office is set an EFL, a financial target and a real unit cost objective by Government. Quality of service aims are set by the Post Office and have been accepted by Government. The financial target and RUC objective run only to the end of 1984/85. Officials will be putting proposals to Ministers on new targets shortly. Annexed to this note are tables setting out the Post Office's financial and efficiency targets during the review period and performance against these.

5 The Post Office was the subject of an MMC investigation into the Inner London Letter Post in 1980 which led to recommendations for improved productivity which were accepted and successfully acted upon. A further report on the letter post was published on 12 September 1984 and the Post Office is due to submit its response to the Department before the end of the year. The report was very critical of the Post Office's performance chiefly on quality of service. The Counters side of the Post Office is to be referred to the MMC in 1985.

Performance - EFL (Summary at Annex 1)

6 EFLs have only been set separately for the postal business since 1982/83. For the previous two years, the EFL included Girobank and, prior to 1980/81, the telecommunications business of the old Post Office Corporation. Reliable Post Office figures are available only for 1980/81 onwards. In that year, the Corporation failed a negative £20m EFL by £12.3m, but more than recovered this by an excess of £23.9m the following year. 1982/83 showed a £3.9m surplus over the negative EFL of £55.8m. In 1983/84 there was a surplus of £10.6m against the negative EFL of £50.9m.

7 Despite shortfalls in some years and overspends in others, postal business capital spending over the review period at £542.2 was very close to the allocation of £555.2m. Outturn in 1983/84 was £123.1m compared to the allocation of £130.0m. A note giving details of Post Office capital expenditure over the review period is at Annex 2.

8 The impact of technology on both the mails and counters business over the next few years could be significant and, although the Post Office has been slow to move, it is now facing up to the implications. A new IT Division has been established with a Director brought in from outside. The major IT project is counters automation. While appreciating the scale and complexity of the project, officials have stressed to the Post Office the need for decisive action. A recently established project team within the Post Office is looking to put further proposals to the board later this year and officials will continue to keep abreast of developments. Progress in building up the electronic mail and Intelpost facsimile services has been satisfactory.

Performance against financial objective (Summary at Annex 3)

9 The Post Office comfortably exceeded its profit target in each year of the review period apart from 1980/81 when a target of 2% on turnover was failed substantially with outturn of 1.1%. This owes much to a rise in real wages of 7% in that year. In 1982/83 a target equivalent to 2.8% on turnover (after allowing for the effect of NIS reductions) was well exceeded with outturn profits of 4.9% (£129m against £74m target). However, this was almost entirely due to a tariff increase in February 1982 of 9½% when an increase of perhaps 3½-4% would appear to have been the maximum necessary. Departmental scrutiny of tariff proposals has been tightened up since then. Performance in 1983/84 was 4.2% against a target of 3%. A one year profit target of 4% on turnover has been set for 1984/85 while discussions continue on new financial and efficiency targets for the years from 1985/86.

Mails

10 Inland letters has consistently provided 57-59% of Post Office income over the review period; counters 20-22% and both parcels and overseas mails around 10%.

11 Inland letters has been consistently profitable with a return of 3.1% on turnover in 1983/84 (5.1% in 1982/83). Although a statutory monopoly, there is competition from other forms of message communication particularly telephone, computers (for financial and other mail) and television (direct mail advertising). Volume is therefore sensitive to price changes and has suffered from large price rises in the past - particularly following the national strike in 1971 and the ending of price restraint in 1975/76. Nevertheless prices have fallen by 20% in real terms over the last seven years. Main growth areas have been financial mail and direct mail advertising. Social mail is declining despite strong growth in greetings cards. Officials take the view that inland letters can continue to grow steadily for some time yet with the aid of marketing.

12 The Post Office is in the process of changing to a product-based approach to the mails market. Organisational changes are expected to be substantially completed this year which will include the appointment of product managers for specific segments of the market such as financial mail, direct mail and social mail. The Post Office has strengthened its marketing effort recently (not just on mail but on counters as well) and marketing is seen as being an increasingly important tool which within the new approach product managers will target towards exploiting the potential of their particular market segments.

13 Following substantial losses in 1976/77 and 1977/78, the parcels business recorded a small profit in 1978/79 and 1979/80. In 1980/81 volume fell by 4% and a loss of £5.9m was recorded. Although the Post Office blames the recession, it is more likely attributable to a rise in real prices of 10% and a rise in real unit costs of perhaps 13% again reflecting the large increase in real wages that year. Since 1980/81, profits have been restored and have grown steadily to 6.4% of turnover in 1983/84. Little market share information is available but the Post Office is looking to increased marketing and increased efficiency to secure sustained profitable growth. Recent performance suggests that this is attainable.

14 The overseas business barely broke even in 1979/80 and 1980/81 but profitability has increased strongly since. But this has been in the face of falling traffic (30% down over the review period) and there is evidence to suggest that the Post Office is able to increase real prices (up 42% over the review period) to maintain income and profits. There is also evidence to suggest that there may be some cross-subsidy within the overseas mail sector and officials are discussing this with the Post Office.

Counters

15 Counters business was consistently profitable until 1981/82 but this was largely inevitable given the cost-plus basis of the pricing agreement with Government Departments. The present three year agreement assumes a 5% reduction in RUC (in line with the whole business target) and, although profitability has held up, the business faces major problems. DHSS is by far the largest customer representing about a third of total income. DHSS volume is threatened by changes in benefit payment methods. A conscious effort has been made to replace this business with other Government work and, although there have been some successes, it is proving an extremely difficult task. This is largely because the counters service is seen as being expensive by user departments. Increased volume for a largely fixed cost business will reduce unit costs, allow keener pricing and make it easier to retain existing business and attract new work. But volume cannot increase while prices are at current levels. The need for the counters business therefore is for a step reduction in fixed costs.

16 Following consultations with Government, the Post Office announced plans earlier this year to reduce the size of the network by 80 Crown Offices and 1,000 town sub-offices. Additional savings were to come from downgrading 50 Head Post Offices and from economies in the rural service. Initial costs of £43m were to produce savings of £15m a year - 3% of total counters costs. This is probably too little and there will need to be a continuing review of network size. Consideration also needs to be given to ways of financing what will always be an uneconomic rural network. There is evidence that present pricing arrangements could disguise an element of cross-subsidy from users of the town network to users of the rural network. Counters automation should help reduce costs and bring in new business; the 1982 Counters productivity scheme is forecast to produce a 10% reduction in hours by the end of 1984/85 and a marketing drive including uplifting antiquated Crown Offices has been started. The prospects for Counters depend upon its ability to break into the price/volume spiral. In discussions on the Corporate Plan, officials have examined various strategies for Counters but pending detailed discussions which remain to be held on the vital question of pricing strategy these were inconclusive.

Forecasting

17 Post Office performance on forecasting GDP and RPI has not been particularly good. Forecasts for traffic growth have been consistently conservative - although consistently optimistic for overseas mail.

Pay and Associated Costs

18 The Post Office has four main negotiating groups. The UCW, representing 156,000 employees is by far the largest and sets the pace for the others. These are the POEU (8,000); Communications Managers Association (15,000) and the National Federation of Subpostmasters (20,000). In June, a ballot of UCW members accepted a settlement for 1984 of 4.9%. The UCW claim was for at least 5.2% and a package of other improvements including an hour off the working week. Extensive unofficial action was taken and there was a very real prospect of a programme of official action before the Post Office secured the deal which consists of 4% on basic rates plus a range of monetary additions and changes in overtime arrangements producing an overall average increase of 5.2% on basic rates but a pay bill increase of 4.9% this year and slightly more, but less than 5% in full year. There was no movement on the claim on hours and other conditions. The 1983 UCW settlement was 5% from 1 April and an additional 1% from August plus one day's extra holiday; in 1982 it was 7% and in 1981 8%. The 1984 CMA settlement was secured in July and consisted of 4% on basic rates plus a range of additions producing an increase to pay bill of 4.56% this year and 4.76% in a full year.

19 Paybill increases have roughly matched RPI movements apart from 1980/81 when paybill rose in real terms by 7%. It is no coincidence that the Post Office failed RUC and profit targets and EFL that year. Although NES (New Earning Survey) figures are on a different basis, they indicate that Post Office earnings have been rising in real terms over the review period, and that postal employees have been doing significantly better than average. Despite this evidence, the Post Office maintains that postmen's earnings have fallen in real terms and in comparison to national average earnings. Officials have raised this with the Post Office to try to establish a common data base. There is little prospect for an acceptable strategy on pay while this difference of perception remains.

20 Although the Post Office argues that it faces union pressure for a shorter working week, average basic hours are almost identical to NES average figures. Postmen work 39.5 hours basic compared to the national average 39.2. It is Post Office strategy to reduce overtime hours but this has stuck at around 15½% of total hours over the last three years. Postal workers work significantly more overtime than average. There may be some justification for the Post Office view that it is vulnerable on holidays, however.

21 Mails productivity has increased by 11.0% in the last three years with a 2.2% improvement in 1983/84 (4.8% in 1982/83) and is at its highest level since the 1971 strike. In London, productivity has improved by 26% in the four years from the MMC report in 1980 to March 1984. However, the Improved Working Methods Scheme (IWMS) which underpinned this improvement, provides for an effective 70% workforce share of the savings so that the benefit to the business was much reduced. There are other weaknesses in the scheme - which covers less than 60% of eligible employees and the Post Office has included the introduction of a replacement scheme in its Plan strategies this year. It is the intention to negotiate a new package covering productivity, hours and holidays. Officials are being kept in touch with developments.

A counters productivity scheme is expected to produce a 10% reduction in hours in the two years to 1984/85 which, with fairly static volume, represents good productivity gains and, because of 100% coverage and a lower workforce share (50%), good savings to the business.

22 Sub-postmasters average remuneration has risen by 20% in real terms over the review period - significantly more than the increases for direct employees which we have already suggested were generous. We do not know whether this reflects heavier workloads but it is very unlikely. Touche Ross looked at the question of the method of sub-postmaster remuneration as part of the Post Office response to a Select Committee on Industry and Trade recommendation. They expressed concern that the system may not be considered commercially sound and recommended that the objectives of the remuneration system be re-appraised together with the nature of the basic arrangements between the Post Office and the NFSP. The Post Office undertook to consider this and officials discussed the question in discussions on the Corporate Plan. The Post Office intend to undertake a fundamental review of the remuneration system but this will not be started pending completion of current work on the arrangement for measuring and allocating counters' costs and workload. Officials will continue to press the Post Office on the remuneration question.

Non - Wage Costs

23 Non - wage Costs relate chiefly to mails operations expenditure with accommodation charges and motor transport quite significant. Officials discussed the question of motor transport policy with the Post Office at length in Corporate Plan discussions. Motor transport is one of the areas which the Post Office has been subjecting to close Rayner-type scrutiny and involving outside consultants. These studies have revealed scope for increased efficiency and cost savings and action plans are being devised to secure the improvement which the studies have suggested. Officials will keep in touch with developments and seek to ensure momentum is maintained on follow up to the studies.

Real Unit Costs (Summary at Annex 4)

24 The postal business was first set an RUC objective of holding real unit costs constant over the five years to 1982/83. A 3.3% improvement was achieved in 1978/79 and costs were held steady the following year. But in 1980/81, the 7% real pay increase, lower volume and lower productivity led to an increase in RUC of 8.2% to take the Post Office 4.3% over target. This had increased to 4.8% by the end of 1981/82. The current target was then introduced with the aim of reducing real unit costs by 5% over the three years to 1984/85. The Post Office is on course to meet this target. Officials are currently discussing new targets for 1985/86 and beyond.

Quality of Service (QOS)

25 Current inland letter quality of service targets require the Post Office to deliver 90% of first class mail on the first working day after collection and 96% of second class mail by the third working day after collection. In no single month during the review period has the Post Office met quality of service targets for either first or second class mail. While performance edged up to within striking distance of the targets in late 1982 and early 1983 it fell back significantly towards the end of 1983 and has continued to be poor in 1984. The major reason for the deterioration has been industrial

relations problems within the Post Office both in connection with this year's UCW pay claim and more generally and more extensively, in connection with Post Office management's efforts to improve efficiency.

26 Officials have discussed with the Post Office the performance on QOS and action to secure improvements. The Post Office plans to meet the target by March 1985. Officials are continuing to monitor performance.

27 Although there is a Post Office quality target for parcels (70% delivered by the second working day after collection) and although it is seldom achieved, officials take the view that as parcels operates in a competitive environment, the market - not Government - should determine parcels quality of service and the price/quality relationship. There is no quality target for overseas mail but international postal organisations are currently studying this question. However, any targets would in any case be outside the control of the UK Post Office. The UK inland part of the journey is covered by the inland QOS. Officials are discussing the question of a QOS target for outward overseas mail from collection to delivery to the foreign administration. There is a quality of service target for counters - that average waiting time should be in the range 15-75 seconds. Officials are discussing the usefulness of this target with the Post Office and will be looking to the Post Office to establish a more meaningful target.

SPF2/DTI
November 1984

Performance against EFL

	(£ million)					
	1978/79	1979/80	1980/81	1981/82	1982/83	1983/84
EFL	(1)	(1)	(20.0) ⁽²⁾	10.5 ⁽²⁾	(55.8) ⁽³⁾	(50.9) ⁽³⁾
Achievement	(16.7)	(34.0)	(7.7)	(13.4)	(59.7)	(61.5)
Difference			12.3	(23.9) ⁽⁴⁾	(3.9)	(10.6)

Notes:-

1. EFLs were for GPO including Telecoms. Internally apportioned figures had no formal status and are highly unreliable.
2. For 1980/81 and 1981/82 the formal EFL was for Posts and Girobank.
3. Final EFL in year after adjustments for NIS reductions.
4. Agreement was reached towards the end of 1981/82 that the first claims on the then anticipated surplus profits would be repayment of the previous year's EFL shortfall resulting in a retrospective EFL of zero.

Post Office Capital Fixed Asset Expenditure

	1978/79	1979/80	1980/81	1981/82	1982/83	1983/84
New Construction £m	N/A	N/A	N/A	44.0	48.6	67.7
Land and Buildings £m	N/A	N/A	N/A	4.0	16.6	11.7
Vehicles £m	N/A	N/A	N/A	29.0	23.5	19.0
Plant and Machinery £m	N/A	N/A	N/A	34.8	36.0	24.7
<hr/>						
Total (outturn prices) £m	42.5	64.1	76.0	111.8	124.7	123.1
Allocation (outturn prices) £M	56.5	54.7	64.5	134.5	115.0	130.0
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Overspend/(Underspend) £m	(14.0)	9.4	11.5	(22.7)	9.7	(69)
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Overspend/(Underspend) %	(32.9)	17.2)	17.8	(20.3)	8.4)	(5.3)
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Performance against financial objective

	Turnover £m	Target*		Performance*	
		%	£m equivalent	%	£ million
1978/79	1,447.4	2.0	28.9	2.3	33.1
1979/80	1,708.0	2.0	34.2	2.0	34.1
1980/81	2,125.2	2.0	42.5	1.1	23.3
1981/82	2,438.2	2.0	48.8	3.6	87.5
1982/83	2,649.0	2.8	74.0	4.9	129.1
1983/84	2,770.4	3.0	83.1	4.2	116.9

*On a modified historic cost basis for all years other than 1983/84 which is on a current cost basis.

REAL UNIT COST OBJECTIVE AND PERFORMANCE

	<u>Target</u>	<u>Performance</u>	
		1977/78 = 100	1981/82 = 100
1977/78	100	100	
1978/79	100	96.7	
1979/80	100	96.6	
1980/81	100	104.3	
1981/82	<u>100</u>	<u>104.8</u>	<u>100</u>
1982/83	98	(102.5)	97.8
1983/84	..	(101.3)	96.6
1984/85	95		

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Secretary of State for Trade and Industry

8 February 1985

Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1

R Nigel,

POST OFFICE: OBJECTIVES AND CORPORATE PLAN

Thank you for your letter of 29 January. I fully accept that there is a need for both the objectives and the Corporate Plan of the Post Office to be consistent and to reflect the aims which we have for the Post Office both in the shorter and the longer term. But I fear that we have a difficulty in timing, and are in something of a "chicken and egg" situation. The 1985 Plan ought to be set in the context of agreed long-term objectives; but the 1985 Plan is an essential input into our consideration of those same long-term objectives. The 1985 Plan is scheduled to be presented to the Post Office Board later this month, in order to meet the timetable of submitting it to me by the end of March. As Geoffrey Pattie said in his letter of 10 January, we attach considerable importance to holding the Post Office to that timetable for this year. This means that I should like to make our views clear to Sir Ronald Dearing during the next week.

2 I believe, therefore, that it is necessary for us to establish some points in relation to the 1985 Plan, before progressing to the formulation of objectives. For example, it is too early to say whether we want Girobank to continue its present policy of growth within constraints (both financial and regulatory) imposed by Government; or whether it should be cut back to a simple money transmission service; or whether it should plan for more rapid growth with the injection of public funds, a private sector partner, or, indeed, whether it should be privatised. Also, the Counters business faces major decisions in the next few months that will affect its long term future. And, even on the Mails business, you have expressed doubt about the central strategy of marketing for growth given the absence of data on long-run marginal cost. And there is nothing at present in the draft objectives about pricing policy.

3 I would therefore propose to tell Sir Ronald that we will return to the question of objectives later in the year once we have

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considered the major areas of uncertainty, and that the Corporate Plan will be a major input for that consideration. But I will also propose to tell him that he should anticipate the re-formulation of the Objectives on the basis of our general aim to introduce private sector capital into the business. I will also raise the points on form and timing mentioned in Geoffrey Pattie's letter of 10 January to you and say that the strategies outlined in the 1984 Plan are acceptable on an interim basis. However, I would expect the 1985 Plan to justify the chosen strategy for Mails in the absence of long-run marginal cost data and I would expect to see the range of alternative strategies for Counters fully explored, including critical appraisal of the scale and nature of the network. I suspect that separate Plans for Mails and Counters would be appropriate but, at this stage, I would not wish to insist on it.

4 There are three further points in your letter on which I wish to comment: separation of the accounts, the letter monopoly, and private capital.

5 First, we are pursuing the question of separation of the accounts and Sir Ronald has been told that we expect to see, by the end of February, a monthly action plan for the introduction of fully-audited separate accounts for Mails, Counters and Girobank for 1986/87 and that we expect monthly progress reports.

6 Second, the letter monopoly was last reviewed by Keith Joseph in 1979/80. He concluded that the basic letter monopoly should not be disturbed. Your letter offers no reasons for re-examining the letter monopoly. Also, on the question of the introduction of private capital into the Post Office, Kenneth Baker and John Moore agreed only a year ago that we would look to see whether Girobank was a candidate but that the rest of the Corporation would not be a possibility in this Parliament. Nevertheless, it was agreed that we should move the Post Office to speedy action on corporate structure and creation of subsidiaries. On the scope for privatisation of Girobank, I would hope to put a note to you at about Easter. And we have made it clear to Sir Ronald that we see the creation of formal subsidiary status for Counters and Girobank as the next logical step once separate accounts have been established.

7 On these questions of the letter monopoly or privatisation, I should be happy for us to consider whether the results of earlier reviews should now be reopened. But, in the light of the priority which I attach to making progress now with the 1985 Plan, I hope you will agree that we should pursue these points separately. In view of the difficulty over timing, I shall assume that you are content that we should proceed with Sir Ronald on the basis of the



points set out in this letter, unless I hear from you to the contrary by Wednesday 13 February.

8 I am copying this letter to the other members of E(NI) and to Sir Robert Armstrong.

A handwritten signature in black ink, appearing to read 'Norman Tebbit', written in a cursive style.

NORMAN TEBBIT

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From the Minister of State
for Industry and Information Technology

GEOFFREY PATTIE MP

Rt Hon Peter Rees QC MP
Chief Secretary to the
Treasury
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

25 January 1985

Dear Peter

NATIONAL GIROBANK: FINANCIAL TARGET

The current financial target for National Girobank expires at the end of March 1985 and we have been giving consideration to a new target to run from 1985/86 onwards. I have concluded that it would be right to set a target for the next three years of an annual average return on mean net assets of 22% calculated on the historic cost basis before tax and before interest on long-term loans from the Secretary of State. This figure is consistent with the profit levels implied in the EFL/EFRs to which you recently agreed in the IFR bilaterals. I should be grateful if you would confirm that you are content for me to proceed on this basis.

I am copying this letter to the Prime Minister, other members of E(NI), the Financial Secretary to the Treasury and Sir Robert Armstrong.

Jea

GEOFFREY PATTIE

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~~with A-1. 31-7~~

Siobhán

28 JAN 1985

