F, The issues surrounding the secret review of Australia Post by the Boston Consulting Group leading to the introduction of changes to Australia Post's service model

Note:

This note has been prepared to the best of my ability with limited access and resources to files. Every effort has been made to give accurate reporting and I apologise in advance, if in some instances dates or figures are incorrect.

I understand the sensitivity of the BCG report. I have agreed to assist the Committee and provide details as requested, to enable the Committee to have a better understanding regarding this important work and to be able to make a more balanced assessment of this question. I am providing this evidence, as I have been assured in writing, that I am protected under parliamentary privilege rules. I ask the Committee to assess whether they believe this information should be made public or not, as they are better equipped to understand the implications.

Summary of Findings:

In November 2019 following the appointment of a new Chair, the Government announced BCG would conduct a strategic review of Australia Post to inform the Chair, the Board and I.

The review was comprehensive and both the Executive and the Chair was extensively involved in it.

The BCG Review did not support Management's view of having a strategy to grow the business or remaining sustainable by leveraging our infrastructure to carry parcels and letters whilst building new services, including extending financial services. We believed this strategy would protect community services, maintain jobs and build a new legacy for Australia Post to serve all Australians for decades to come, whilst remaining viable. BCG essentially argued it was too optimistic and risky, even though the business was ahead of its targets for the year when the review commenced and the organization had only lost money once in its history.

BCG put forward 4 reform paths for consideration, which focused on cutting costs and driving efficiencies. Initially these reform paths started from driving efficiencies in the corporate center, to significantly reducing letter services nationally, increasing prices, closing Post Offices, divesting of the parcels business and restricting financial and other services. The implications of these would be significant, including cutting thousands of jobs, reducing services and risking customer loyalty.

As an Executive Team, we committed to be more efficient in the corporate center, but we pushed back on the need and the ability to cut back the services and jobs as they proposed and the significant disruption a parcels divesture would cause. Disappointingly the BCG review did not significantly explore opportunities to grow, such as extending financial services as many other profitable post offices around the world had, including Swiss Post, La Poste (France), China Post, and Japan Post. After extensive feedback with BCG and the Departments, BCG did adapt their review. However, their final review still did recommend significant reforms and cuts in the letters service, which they argued would be important if we were to avoid losses, which they believed could be as soon as 2021.

The final draft of the review, which was to be sent to the Shareholder Ministers, was forwarded to the Chair of Australia Post on February 21st, the day after the Board had met to discuss the report with BCG and the Departments.

In March 2020 Australia Post, the impacts of COVID-19 accelerated; Qantas had significantly reduced their air network and new safe working requirements were introduced, as a consequence we faced a period of simply not being able to meet the delivery times regulated. The CFO had prepared scenarios of how our business could look, based on significant feedback from other Postal Operators. We realized we only had enough cash to pay our people and partners for approximately 6 weeks and the outlook for profits were dire. We immediately took action, cutting non-essential costs so we could divert investment to the front line and be able to acquire PPE for our people and partners. We knew that this action alone would not be enough, to avoid losses or to meet accelerating customer demands, so I requested Temporary Regulatory Relief until December 2020, to enable us to better manage through this period of great uncertainty and volatility.

It is worth noting that at this stage Qantas, Virgin and many major employers in the country had stood down their staff. Many employees across the country faced periods of no income. We did not want that for our employees and we knew if we stopped working the impact on the millions of businesses we support, would be devastating too. We sought ways to be considered as an essential service and gain relief so we could meet the needs of our customers. We embarked on a simple strategy, **Protect, Serve & Safeguard**. Protect our People – their health and their roles, Serve the country through the Pandemic and Safeguard the business.

On March 21st 2020, Australia Post secured an agreement with the Pharmacy Guild of Australia and the Health Department to deliver medicines to the elderly and vulnerable through the COVID-19 crisis. This agreement secured the right for Australia Post to be considered as an essential service and remain operational.

On April 21st 2020, the Government committed to temporary regulatory relief until June 30th 2021, it primarily included enabling longer times to deliver, suspending priority mail and introducing alternative delivery days in metro areas only.

The relief given by the Government, has some similarities to BCG's 'reform path 2'. Although the intent of BCG's review was to drive cost efficiencies, the reality was at the peak of COVID, Australia Post simply could not deliver to the regulated speeds and the relief was critically important. BCG's 'reform path 2' was very similar to the recommendations from many of the different reviews, which had taken place over the years prior. One difference to the BCG reform path 2, was that Australia Post, supported by the Departments, wanted to leverage our own Posties to help ndeliver the Parcels, as opposed to cutting jobs and outsourcing all the work to contractors. The organization was told clearly from the Government that the regulatory relief was temporary and that the services for rural and regional Australia, were to be protected as much as possible.

As the weeks and months progressed the financial and operational reality was very different than first predicted by the CFO. Although letters significantly fell and international parcels fell, domestic parcels grew, as almost 10 million households shopped online and over 250 thousand businesses engaged in ecommerce to keep their businesses viable through the crisis. Instead of losing money, even in the face of significantly increased costs, the business remained profitable.

Victoria is disproportionally the home of ecommerce, with approximately 65% of all ecommerce generating from there. When the further Victorian lock downs and restrictions were introduced, parcels rose by up to 175%. If it was not for the relief granted to Australia Post, we would not have been able to serve Victoria adequately through their lock down.

The recently announced first half 2021 financial results, highlighted that Australia Post had achieved the highest ever revenue growth for the organization in its history, delivering a first half profit of over 100% growth to $166m, which was an incredible $68m over budget performance, demonstrating that the relief had worked. Jobs have been protected. the organization has served the country and the business has been safeguarded.

I strongly believe in the growth prospects for Australia Post, although I recognize it is not without its challenges. It is important Australia Post is able to pursue a competitive agenda, individual political agendas are avoided and it is supported with a strong skilled Board to provide necessary governance and support, just as any other significant organization would have.

During my 3 years at Australia Post, I went through 4 reviews with external companies, the first initiated by myself the following three by the Government. The three government reviews all suggested our plans were too ambitious and that there should be more focus on cutting costs. Each year we overachieved our targets, avoided losses, secured our jobs and protected our Community Post Offices, whilst still remaining viable, delivering modest dividends and covering a cost of approximately $400m to meet our Community Service Obligations (CSO). Australia Post received no funding towards our CSO costs, unlike other organisations; we paid taxes, collected GST and gave dividends.

The period of the temporary regulatory relief is coming to an end. The Government and Parliament must decide whether to extend the relief or not, or to make it permanent.

I believe that question is not so simple. I would recommend considering:

- Listening to the voice of the customer and seek a thorough understanding of the impacts of stopping priority mail and longer delivery times. Priority Mail was a very important service for many small businesses and without the service many printing houses and magazine companies suffer. This could impact jobs further.

- The projected future growth of parcels. I believe this will continue to be strong as the trends of ecommerce have now become a reality for shoppers and retailers. 16% of Australian retail sales are now online, although Australia still trails many western markets and there is still significant opportunity to grow this. Many major retailers have recently announced this will be an ongoing strategic focus for them and parcel growth has remained strong post COVID-19 as shopping habits have changed.

- The opportunity to develop financial and other trusted services to ensure communities are served and post offices remain viable, similar to many other international postal operators, such as Swiss Post, La Poste, China Post and Japan Post. Many postal operators around the world have extended into financial services to ensure both the Government’s ambitions to protect and build social economic inclusion complemented with the fact that the profits from financial services have subsidized the declining letter business, consequently avoiding losses. Whilst there are risks in becoming a fully licensed bank, there is a significant opportunity to play a larger role without risking the balance sheet or breaching compliance rules etc. Over 50% of the communities in Australia do not have a bank, yet there is a Post Office. An extended role in Financial Services would help keep Community Post Offices sustainable whilst providing a very important community service.

- The resourcing required to ensure Australia Post meets its original delivery standards. I do not believe Alternative Delivery Days in metro or not, is the real issue, but how much resources do Australia Post need, to deliver on time and efficiently. The growth of ecommerce has heightened the need for speed. Slowing letter services is likely to accelerate the volume declines, which in turn this will disproportionately disadvantage rural and regional Australia and small businesses. Although letters are declining, the declines are better than budgeted and this remains a business with revenues of over $1.6bn and as such, it should be nurtured.

- As Qantas opens its air network and PPE and safe distancing requirements are relaxed, costs should be saved. How much are they.

- If the temporary regulatory relief is extended, is it all of the relief, how long for and how long will it take Australia Post to adapt to a different model again. Changing models is highly disruptive.

- The trade off from delivering significantly higher dividends compared to protecting services and jobs, whilst still remaining viable and delivering to the purpose of Australia Post for the benefit of all Australians.

Chronology of Evidence regarding BCG:

Prior to joining Australia Post in October 2017 there had been several reviews assessing future sustainability options. There were two reviews of note:

- **In 2014,** BCG conducted a review of strategic options for Australia Post in a review called The Australian and International Postal Services Overview. These options included slowing letter services reducing delivery frequencies and increasing pricing.
- **28th September 2017, the ANAO** produced a report called: Australia Post's Efficiency of Delivering Reserved Letter Services. This report was apparently prepared by the Department of Finance in conjunction with Australia Post and includes a number of commitments to cut the costs of delivering reserved letters. These included rolling out alternative day deliveries nationally and reducing labor rates by restricting penalty rate shifts. There were a number of options to improve efficiencies which are summarized in the extract from this report which can be found **in Appendix F1.**

1st November 2019, on the announcement by the two shareholder Ministers of the appointment of Lucio De Bartolomeo as new Chair of Australia Post the statement said "To inform the incoming Chair and further inform the Board and Chief Executive Officer, in addition to Australia Post's existing Corporate Plan 2023, the Australian Government has appointed management consulting firm BCG to conduct a review of Australia Post's strategy to operate as a sustainable and fit-for-purpose service provider for the longer term. This review will consider broader market conditions such as growth in e-commerce, the regulatory environment, and changes in business and consumer needs. The review is expected to report back to Government in early 2020. This report is referred to as the BCG report or BCG review.

21st November 2019, the first Steering Committee meeting is held between BCG, members of the Finance & Communications Department and senior Management at Australia Post, including Rodney Boys CFO Australia Post, (currently Acting CEO) and I.

29th November 2019, a comprehensive analysis by BCG on Australia Post's Financial Sustainability is prepared.

3rd December 2019, the second steering committee meeting is held. Attended by BCG, senior Managers from both departments and Australia Post, including Rodney Boys CFO Australia Post, (currently Acting CEO) and I.

3rd December 2019, a briefing note to the Australia Post Board is updated on Diligent.

5th December 2019, an update on the BCG review is given at the Australia Post Board meeting. The Chair, the CFO and I were all present.

8th December 2019, BCG Share an updated Overview on their financial modelling.

10th December 2019, Members of the Australia Post Executive Team and I meet with Minister Paul Fletcher. At this meeting we share Parcels & Express revenues are up 11% Year on Year and are significantly ahead of budget. Letter volumes were down 11.8%. Financial Services and International were both performing very strong 30% and 35% up year on year respectively. Profit Before Tax YTD (5 months) at $68m was up $22m to budget.

10th December 2019, Australia Post receives a briefing pack ahead of the Steer-Co process Check-in the following day. This is shared with Rodney Boys, CFO and I.

11th December 2019, Steer-Co Process Check-in meets and focuses on page 5. **Appendix F2**

12th December 2020, we receive notice that BCG would like to discuss Letter Reform Options and Parcel Divestiture Options further with Bob Black (Chief Operation Officer Australia Post), the next day (13th December).

16th December 2019 dated, (although received 16th January 2020) the reference terms for the BCG review are shared with Australia Post and these terms reference the request for a special dividend from Australia Post to cover the cost. This is sent to the Chair.

17th December 2020, Australia Post receives a BCG briefing pack ahead of the scheduled Steering Committee the next day.

19th December 2019, BCG Steering Committee Meeting. This was an extensive meeting for 2. 5hours. The Executive Summary of this meeting is attached in **Appendix F3**

1st January 2020, a 10c increase to the Basic Postal Rate becomes effective. This was the first increase in 4 years and partially offset letter losses.

16th January 2020, Rodney Boys advises we will soon see a draft report for BCG Steering Committee Review to be held on the 30th of January. This draft report was received and outlines their strategic options. This is an extensive report.

22nd January 2020, BCG held a process check-in teleconference.

24th January 2020, Australia Post shares with BCG their considerable concerns for their proposed 4 strategic options and for the implications of these for our employees and services. These concerns included:

- Product cross dependencies for customers
- Australia Post's purpose
- Growth from Additional Services – the BCG review had minimal support for extensions to Financial & Identity Services.
- Employee Relations Context
- Redundancies
- Benchmarking Analysis
- Letter Reform Savings
- Reform Complexities

29th January 2020, the Chair receives from the CEO a copy of the interim BCG report and a copy of Australia Post's feedback.

30th January 2020, BCG Steering Committee Meeting.

31st January 2020, Stacie Hall, the First Assistant Secretary in Finance, sent the Chair a draft final BCG report, copying the CEO and others.

31st January 2020, the CEO and the Chair, Lucio Di Bartolomeo meets to discuss the BCG review and prepare for the upcoming Board meeting.

2nd February 2020, the CEO sends the Chair a briefing pack on the BCG review ahead of their meeting on the 4th February in Canberra with BCG and senior members of the departments.

4th February 2020, the Chair and the CEO travel to Canberra to meet with BCG at the Department of Finance, with members of the Finance and Communications Departments to discuss the report. At this meeting the CEO presents to the Group her considerable concerns with the 4 reform paths suggested by BCG and the lack of probable success in executing them. She also shared her disappointment that BCG did not support the Growth prospects of the business, including future parcel growth and the potential to develop further the role the Community Post Offices could play in financial services.

6th February 2020, BCG host a process check in teleconference.

11th February 2020, Australia Post receive another draft of the BCG Review.

13th February 2020, Steering Committee Meeting. At this meeting Australia Post again push back on many of the BCG recommendations and the impacts it would have.

17th February 2020, BCG are provided with further feedback.

19th February 2020, the Chair received a Board presentation prepared by the Finance Department and BCG, which summarised the report, from the CEO.

20th February 2020, the Australia Post Board Portal was updated with a copy of the BCG presentation on the findings of the review.

20th February 2020, BCG with members of the Department of Finance (and members of the Department of Communications present), presented for several hours at a 5hour Australia Post Board meeting on their findings. McKinseys also attended part of this meeting. The CFO, Rodney Boys (Acting CEO) was present throughout the meeting.

21st February 2020, Stacey Hall, the First Assistant Secretary in Finance emails the Chair "a Final Draft of the BCG's report, which departments will present to Shareholder Ministers.", copying the CEO. Appendix F4 highlights the executive summary.

24th February 2020, Quarterly report sent from the Chair to both Shareholder Ministers highlighting at $83m the PBT was $30m above budget at the end of Half one 19/20.

14th March 2020, I write to the Shareholder Ministers offering Australia Post to carry medicines and essential items through the pandemic. I seek approval that our people can be classified as an essential service and that we can be exempt from strict Quarantine restrictions. This was essential to enable our people to operate through the crisis, which in turn enabled many businesses to still operate and it saved our people's jobs.

20th March 2020, Qantas announce a 60% reduction with their ground fleet. This seriously impacts Australia Posts' options to carry letters and parcels around the country.

21st March 2020, Australia Post secures an agreement with the Pharmacy Guild of Australia and the Department of Health to deliver medicines to the home for elderly and vulnerable patients. This agreement secured our ability to be an essential service and remain operational throughout COVID-19 restrictions.

From approximately **March 22nd** new working practices were operational, including safe distancing in the workplace etc. These changes had a significant impact on our ability to operate efficiently.

March 23rd 2020, Australia Post Board meeting discusses potential scenarios prepared by the CFO depending how COVID evolves. The consequences of these scenarios were stark. See **Appendix F5.**

March 26th 2020, There was a second Board meeting, further scenarios were developed, but the results looked potentially starker. A draft letter to the Ministers was discussed with the Board. In the course of days, we had experienced significant increased volatility. Letter volumes were down 30%, B2B road parcel volumes fell 12%, international volumes were down 29% and Post Office traffic and services were plummeting.

March 27th 2020, Royal Mail UK announce that they expect to make a material loss and suspend any guidance. We were in regular contact with the major postal partners to Australia Post and none of these were expecting to remain profitable.

March 30th 2020, There was a Board call to discuss and review the draft letter to the Ministers. Parcel volumes started to shift and we started to see an increase in extra large parcels, these are items which could not be carried by Posties on motorbikes.

30th March 2020, Australia Post receives a letter from both Shareholder Ministers. It acknowledges the Chair's letter on the 24th February. It encourages further cost savings consistent with those on

the BCG review. It requests clarity on whether Australia Post is going to pay a special dividend of $1.32m to cover the cost of the BCG review. It states:
"We thank you for your assistance during the Review and look forward to continuing to work closely with the Board and Australia Post as you manage the effects of COVID-19 on your workforce, your customers and the business, and through the upcoming Corporate Plan process. An initial step, we envisage that BCG's findings should be taken into account as the Corporate Plan Process is developed as we work together to support Australia Post's ambition for transformation"

March 31st 2020, I write to shareholder ministers seeking assistance to be able to manage through the crisis. This included regulatory relief for delivery times and stopping priority mail as we could not meet the times stipulated with a significantly reduced air network.

- At the time of sending the letter on the 31st March 2020, Qantas had significantly reduced its air network and Australia Post was already obliged to work differently to ensure compliance to new safety standards. Australia Post carried letters and parcels around the country and world in the belly of Qantas planes. A combination of a significantly reduced air freight network and new operating standards was impacting Australia Post's ability to deliver on time. **The outlook was very uncertain**.
- The CFO had forecast we could face significant financial challenges including needing a cash injection.
- The letter outlined the many initiatives and actions Australia Post had taken to protect our people, serve the country and safeguard the business. It requested consideration for help until 31st December 2020, to enable Australia Post to have time to adjust to the considerable obstacles facing us.

April 4th 2020, (dated 3rd April 2020) the Chair receives a letter from the Shareholder Ministers acknowledging our request on the 31 March and confirming that the Departments will urgently prepare advice.

April 9th 2020, Qantas announce they will be reducing their network to effectively Zero, ultimately it maintained approximately 15%. Australia Post worked to build the chartered air network to up to 17 planes to enable letters and parcels to continue to be carried across the country. This was at a significant extra cost to Australia Post.

21st April 2020, The Shareholder Ministers announce Australia Post will be provided with Regulatory relief as a temporary measure until 30th June 2021. Specifically, this included:

- Suspension of our Priority Letter Service.
- Delivery time for regular interstate mail would be extended to five days after the days of posting.
- Delivery frequency in metropolitan areas would be adjusted to every other day. Regional & Rural frequencies would remain unchanged.
- Allowing for greater flexibility of Post Offices being open through the Pandemic.

24th April 2020, The Executive Team and I meet with Minister Fletcher. We share with the minister that the scenarios prepared in March had not materialized and losses had been avoided. March YTD Profit (PBT) was at $91m up $74m to budget. The losses had been avoided as we had taken prompt action on costs and we had seen an unprecedented growth in parcels, but we were struggling to manage the volumes. Qantas had now significantly reduced their network and we were chartering up to 17 planes at an extra cost per week of over $1m. The cost of providing PPE was growing and our customers were uncertain regarding the immediate future.

13th May 2020, A progress report is sent to the Shareholder Ministers and Australia Post has a Board meeting.

16th May 2020, the temporary regulatory changes were formally passed through parliament.

8th July 2020, there was a Senate Inquiry "Future of Australia Post Service Delivery" specifically reviewing the need and implications for the temporary regulatory relief. The outcome of the inquiry was to support the temporary relief.

14th August 2020, the Chair writes to the CEO and says:

Hi Christine
Had my regular teleconference with Andrew Jaggers and Stacy this afternoon re Aust Post. Andrew asked if we were dealing with request for the special dividend to cover the cost of BCG Review. I just had a quick look at the papers currently downloaded and could see our standard 65% of Profit After tax but saw nothing yet re the special dividend. The request for this dividend is very unusual but only $1.5 mil. We were going to pay in March but we were given relief after our early concern of financial position. Given the very different result achieved we should now pay the special dividend. There is an important parallel that won't go unnoticed.
Lucio.

1st September 2020, the final Australia Post F21 Corporate Plan is approved.

February 20th 2021.

The F21 financial results for the first half were announced. They evidenced a significant uplift in both revenue and profits. Profits (PBT) was up 100% to $166m year on year, this was $68m above budget.

Appendix F1

ANAO Report 28th September 2017: Australia Post's Efficiency of Delivering Reserved Letter Services.

Table 2.2: Reform our Letters Service—network and labour force optimisation strategies

Process	Description	Projected savings 2018–19($m)
Automation impacts in delivery	New machines at major mail centres will automate sorting of mail and reduce sorting times and associated labour costs.	128
Implementing the National Delivery Model (NDM)	Under the NDM, regular mail will be delivered every second weekday (as opposed to every weekday), reducing the time and cost of outdoor delivery rounds.	53
Increasing automation in Mail Centres	Investment in new machines will reduce manual work effort, reduce number of required operators per machine and improve throughput rates.	52
Shift alignment in delivery	This will drive savings by increasing the number of non-penalty shifts worked.	45
Renegotiating contract terms	Renegotiation of terms for delivery contractors is expected on more favourable terms for Australia Post.	33
Shift alignment in processing	This will drive savings by increasing the number of non-penalty shifts worked, with all regular mail to be processed during the day. [A]	18

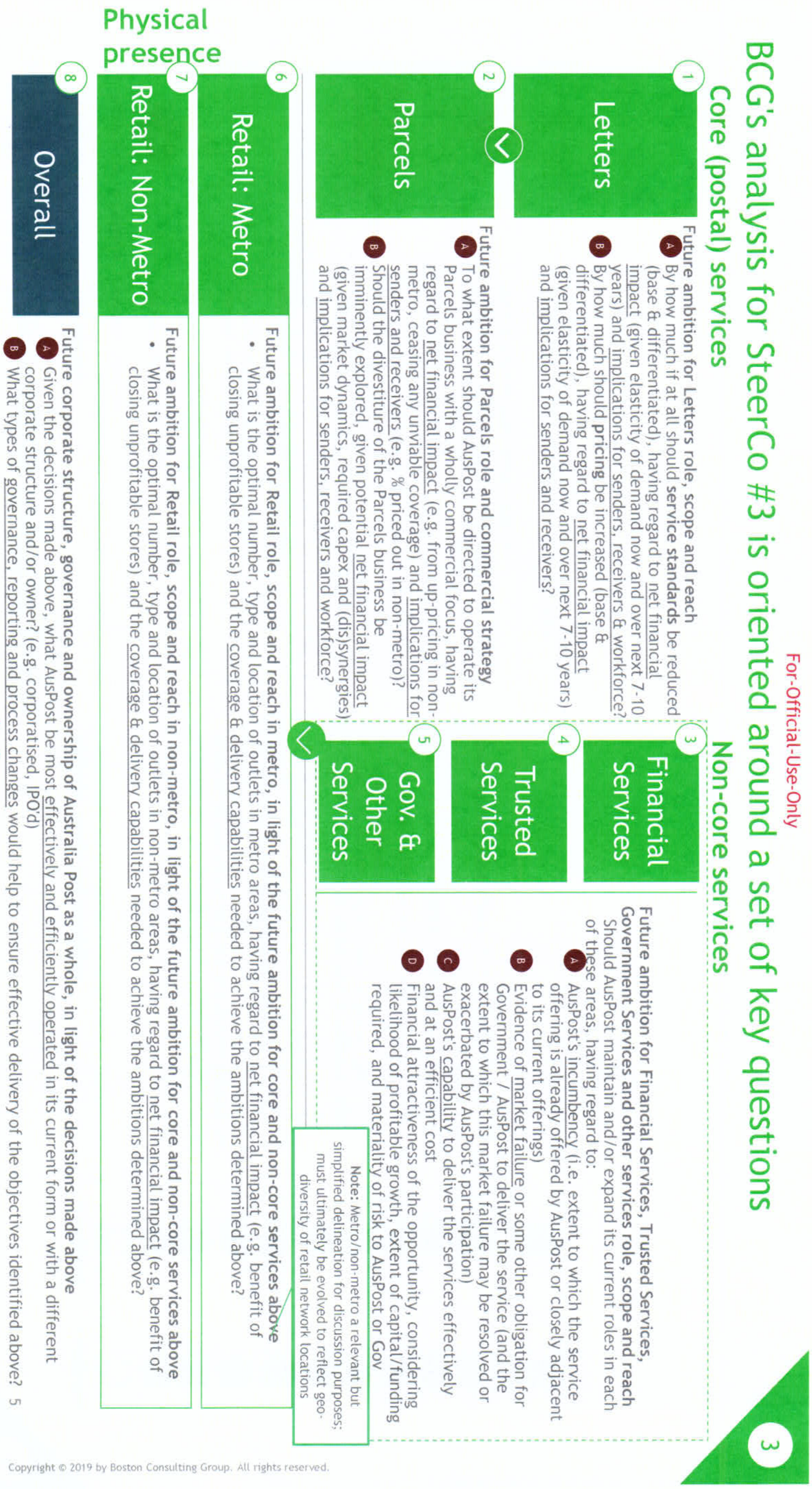
Process	Description	Projected savings 2018–19($m)
Consolidating processing of regular mail	Consolidation of mail processing activities will reduce the number of Mail Centres from 15 to 4.	4
Consolidating Delivery Centres	Consolidation of Delivery Centres into existing sites to allow disposal of surplus centres.	2
Vehicle optimisation	Optimisation of vehicle selection for delivery rounds based on conditions, terrain and density (for example, using electric bicycles).	3
Street Posting Box optimisation:	Aligning the Street Posting Box clearance time (that is, cut-off times) with mail centre processing windows.	0.6
TOTAL		339

Note a: The projected saving from shift alignment in processing is targeted to have been achieved by the end of the 2016–17 financial year. The remaining figures in the ROLS blueprint document are cumulative savings over the four years, targeted to be achieved by the end of the 2018–19 financial year.

Source: Australia Post, 2014, Reform our Letters Service - Detailed Design Blueprint, p. 73, 111.

2.22 The total costs of the network reforms from the RoLS program, including transition, implementation and capital costs, as well as anticipated redundancy incentives, is estimated at $278 million.[22]

Appendix F2


For-Official-Use-Only
BCG's analysis for SteerCo #3 is oriented around a set of key questions
3
Core (postal) services
1 Letters
Future ambition for Letters role, scope and reach
A By how much if at all should service standards be reduced (base & differentiated), having regard to net financial impact (given elasticity of demand now and over next 7-10 years) and implications for senders, receivers & workforce?
B By how much should pricing be increased (base & differentiated), having regard to net financial impact (given elasticity of demand now and over next 7-10 years) and implications for senders and receivers?
2 Parcels
Future ambition for Parcels role and commercial strategy
A To what extent should AusPost be directed to operate its Parcels business with a wholly commercial focus, having regard to net financial impact (e.g. from up-pricing in non-metro, ceasing any unviable coverage) and implications for senders and receivers (e.g. % priced out in non-metro)?
B Should the divestiture of the Parcels business be imminently explored, given potential net financial impact (given market dynamics, required capex and (dis)synergies) and implications for senders, receivers and workforce?
Non-core services
3 Financial Services
4 Trusted Services
5 Gov. & Other Services
Future ambition for Financial Services, Trusted Services, Government Services and other services role, scope and reach
Should AusPost maintain and/or expand its current roles in each of these areas, having regard to:
A AusPost's incumbency (i.e. extent to which the service offering is already offered by AusPost or closely adjacent to its current offerings)
B Evidence of market failure or some other obligation for Government / AusPost to deliver the service (and the extent to which this market failure may be resolved or exacerbated by AusPost's participation)
C AusPost's capability to deliver the services effectively and at an efficient cost
D Financial attractiveness of the opportunity, considering likelihood of profitable growth, extent of capital/funding required, and materiality of risk to AusPost or Gov
Note: Metro/non-metro a relevant but simplified delineation for discussion purposes; must ultimately be evolved to reflect geo-diversity of retail network locations
Physical presence
6 Retail: Metro
Future ambition for Retail role, scope and reach in metro, in light of the future ambition for core and non-core services above
• What is the optimal number, type and location of outlets in metro areas, having regard to net financial impact (e.g. benefit of closing unprofitable stores) and the coverage & delivery capabilities needed to achieve the ambitions determined above?
7 Retail: Non-Metro
Future ambition for Retail role, scope and reach in non-metro, in light of the future ambition for core and non-core services above
• What is the optimal number, type and location of outlets in non-metro areas, having regard to net financial impact (e.g. benefit of closing unprofitable stores) and the coverage & delivery capabilities needed to achieve the ambitions determined above?
8 Overall
Future corporate structure, governance and ownership of Australia Post as a whole, in light of the decisions made above
A Given the decisions made above, what AusPost be most effectively and efficiently operated in its current form or with a different corporate structure and/or owner? (e.g. corporatised, IPO'd)
B What types of governance, reporting and process changes would help to ensure effective delivery of the objectives identified above? 5
Draft
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2

Appendix F3

Executive summary (I/II)

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II

AusPost expects to maintain thin profit margins over at least the next four years, with NPAT forecast to range from $11m-41m during the Corporate Plan period. There is meaningful risk of a loss-making trajectory, and operational improvements within current constraints appear necessary but insufficient to avert it

- There appear to be a number of material risks across AusPost's business lines, which together render a loss-making trajectory as soon as FY21 a possibility without further action or change (to cost efficiency, growth opportunities or regulatory obligations)
- AusPost's financial sustainability can and should be improved with a range of operational efficiency levers that are practicable within current constraints (*identified in SteerCo #2 materials*). It could also benefit from several upside scenarios
- However, such improvements and upsides are likely insufficient to meaningfully improve AusPost's financial sustainability, and it is therefore prudent to consider the broader reform options outlined in these materials

There is potential to meaningfully improve AusPost's financial sustainability through broader reforms to its business lines. These include adjusting Letters obligations to reflect changing community behaviours and ongoing Government investment in digital infrastructure, and reorienting the post office network to focus more on trusted services in non-metro locations. Such changes involve significant trade-offs for Government and AusPost, and require a clear view of AusPost's future role in 10 years

Letters:

- There is potential to drive sustainable reductions of 20-40%+ in AusPost's cost base over the next ten years, in line with changing customer behaviour, while also increasing prices[1] to deliver a further $30-170m p.a. in run-rate EBITDA uplift
- Achieving such benefits would require a major reduction in AusPost's workforce (analysis to date indicates approximately 80% of savings are labour-related). It would also require reducing service standards and affordability for senders and receivers of mail

Parcels:

- There appears to be merit in further exploring a partial divestiture of this business to release cash and avoid significant capital investment over time (approx. 1.5x the amount currently planned). A decision to pursue this path will hinge on whether or not a sufficiently attractive transaction premium can be achieved, which for the parcels business as a standalone is questionable given divestment dis-synergies for both a prospective acquirer and AusPost
- There appears to be limited merit in increasing the commerciality of the non-metro parcels business. While there may be potential to improve margins by approx. 1.5-2% p.a. (approx. $45m p.a.), achieving this benefit would require a reduction in affordability for as many as 2 million citizens in non-metro areas, and may have problematic commercial flow-on effects

1. Price increases applied to products other than Regular mail, which is subject to ACCC regulation having regard to AusPost's cost base

Source: AusPost Corporate Plan; industry research and publications; interviews with 60+ stakeholders from Government and AusPost; BCG analysis

Draft

11

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Executive summary (II/II)

II

additional services (trusted, financial, government):

- In face-to-face services, AusPost increasingly operates in geographies and segments where a degree of market failure exists or is emerging (e.g. in-person identity verification; regional and remote banking services for individuals and small businesses). Before taking on further services of this type, Government must consider whether it wants AusPost to have an abiding presence in such markets as a **'provider of last resort'**, as its continued participation appears likely to lead to such an outcome
- In financial services, Government and AusPost must consider how best to participate going forward. A more systematic continuation of the current intermediary model, particularly in non-metro areas, appears significantly less risky and less capital intensive than becoming a prudentially regulated "Postbank"
- In trusted services, AusPost's in-person offering shows continued promise. Digital identity services and opportunities in large-scale digital identity solutions or systems integration (beyond those already embarked upon, like the Visa tender) present challenges, appearing to be generally risky, binary, winner-takes-all/winner-takes-most opportunities requiring significant capital investment, considerable management attention to win and deliver, and with questionable probability of success
- In other Government services, there is scope for AusPost to deliver more Government services (particularly in-person transactional services), leveraging its non-metro footprint, provided this is of value and cost effective for the relevant agencies

Post office network (retail footprint):

- AusPost's metro footprint has a high degree of unprofitability and geographical overlap, and significantly exceeds regulated numbers. There appears to be a clear rationale for **streamlining** it (e.g. closing the 114 metro CPOs that are unprofitable and have 100% catchment overlap with more viable outlets) and using smaller formats to reduce cost (e.g. lockers, counters)
- AusPost's non-metro footprint is generally profitable and close to regulated levels, with less overlap between outlets. It can be leveraged to deliver prioritised core and additional services, consistent with any decisions made for the other business lines

The types of changes described above involve **meaningful reforms to AusPost's regulatory instruments and operating environment** - potentially encompassing changes to its enabling legislation, regulations, EBAs and Statement of Expectations. These changes have considerable lead-time, and will need to be set in motion as early as feasible to deliver the desired future state for AusPost

Further, and regardless of the approach taken, there is a need to implement clearer **corporate governance mechanisms,** ensuring greater two-way transparency as to strategic direction between AusPost and the Shareholder Departments

Source: AusPost Corporate Plan; industry research and publications; interviews with 60+ stakeholders from Government and AusPost; BCG analysis

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Appendix 4

As at 21 February 2020

1 Executive summary

Australia Post (AusPost) is a Government Business Enterprise (GBE) operating under the *Australian Postal Corporation Act 1989* (the Act) and related regulations. Its statutory obligations are to provide a universal letter service that is reasonably accessible by all Australians, and to operate in a manner consistent with sound commercial practice to provide a financial return to its shareholders.

AusPost has played an important role in the lives of Australian communities, individuals and businesses over the last 200 years, and it continues to do so. It provides a trusted and effective postal service within Australia and between Australia and the rest of the world. It has also progressively taken on a broader role in Australian society – facilitating the rapidly growing eCommerce market as the largest parcel delivery operator in the country, and providing a range of products and services (including financial, identity and government services) to Australians through its uniquely broad, nationwide network of post offices.

The scale and reach of AusPost's operations are significant. Last year it delivered more than 3 billion items, including more than 1.3 million parcels each day, to a growing network of over 12 million delivery points around Australia. Its assets include 4,338 post offices, 15,085 street posting boxes, 7,000 motorbikes, 6,500 delivery vans, 2,600 trucks, seven airline freighters (leased from Qantas), 500 facilities and 325 parcel lockers. AusPost is one of Australia's largest employers, with 35,000 direct employees in delivery, logistics, retail and eCommerce, and a further 35,000 contractors, sub-contractors, licensees and delivery partners.

In terms of financial performance, AusPost has remained profitable in all but one of the last 15 years, despite a steep decline in letter volumes and operating in a challenging geography with very low population density. It has achieved this outcome by strategically diversifying its revenue base, regularly delivering cost efficiencies across the business, and periodically increasing the Basic Postage Rate (BPR). However, AusPost's profits and dividends have been low and volatile over the last 15 years, delivering a dividend of $42m in 2019 and profit margins in the third quartile of its global postal peers.[1] AusPost also faces the prospect of further credit rating downgrades following Standard & Poor's (S&P) one-notch downgrade in December 2019.[2]

AusPost's operating environment and customer needs are evolving rapidly. Looking ahead to 2030, BCG expects that a lower but still significant volume of letters will need to be delivered – between 0.8 billion and 1.2 billion in 2030, compared to 2.6 billion today. The public's expectations of letters service standards are also likely to decline further over the decade, as broadband penetration continues to grow and communication preferences become increasingly digitised. Conversely, twice as many parcels are expected to be delivered in 2030 compared with today, even as eCommerce markets mature over the decade. A much higher proportion of shopping transactions, and financial and identity services, will be delivered online in 2030, but a high volume of residual in-person transactions will remain – particularly in non-metro areas,[3] where incumbent banks are expected to reduce the number of branches by 35% and ATMs by 50% between FY2020–FY2030.

In this changing context, the Australian Government (represented by the Shareholder Departments of the Department of Finance and the Department of Infrastructure, Transport, Regional Development and Communications) engaged Boston Consulting Group (BCG) to undertake an independent review of AusPost from November 2019 to February 2020. **The overarching goal of the review was to identify a path to deliver a meaningful improvement in AusPost's financial sustainability now and for the next decade (2020–2030), while maintaining an appropriate level of community service.**

The Shareholder Departments and AusPost have expressed an aligned commitment to ensuring the business' ongoing, self-funding delivery of relevant services to the Australian community and to its financial sustainability over the long term. BCG's assessment of the options available to meet this aligned commitment takes into consideration the implications of AusPost's current Corporate Plan for the period FY2020–FY2023, its financial and operating sustainability out to 2030, and the challenges that are being faced by peer postal organisations globally.

AusPost's Corporate Plan forecasts thin profit margins over the next four years, with net profit after tax (NPAT) ranging from $11m–$39m. **However, BCG sees a number of material risks to this plan, which could see AusPost delivering a loss as soon as FY2021 without further action or change beyond that currently envisaged in the Corporate Plan.** In particular, there is potential for letter volumes to decline faster than currently forecast (8% per year rather than 7% per year) as digital substitution trends continue and large senders reduce their use of letters. There is also potential for more intense price-based competition from existing players and new entrants (e.g. Amazon) in the Business-to-Consumer (B2C) parcels market, which poses a material risk to AusPost's forecast market share and price realisation.

While there are some scenarios that could see higher profitability delivered over the next four years, the number and materiality of risks, and the financial position of the business, lead BCG to believe that planning for a more conservative performance trajectory is prudent. It is also BCG's view that, for AusPost to be financially sustainable, its focus on revenue growth must be complemented by a particular focus on significant and sustained cost efficiencies. This is because: (i) revenue growth objectives built into AusPost's Corporate Plan are exposed to the market risks identified in this report; (ii) revenue growth is typically more difficult to control and predict than cost efficiency in markets that are highly competitive or exposed to secular trends; (iii) revenue growth opportunities available to AusPost typically require material upfront capital investment and have longer pay-off periods than cost efficiencies, placing additional financial pressure on the business given the capital intensity of its core delivery operations; and (iv) there may be potential public policy risks associated with a GBE such as AusPost adopting an expansive growth strategy in competitive markets.

Ensuring AusPost's financial sustainability will require effective delivery of the ambitious agenda in the Corporate Plan, including continued investment in its leading Parcels business, strategic turnaround of its Consumer business, and delivery of its planned multi-year efficiency program. **Financial sustainability will also require a set of actions beyond those in the Corporate Plan.** Some of these actions can be undertaken without regulatory change or broader reform. These include cost efficiencies that would flow directly to the bottom line, such as: further efficiencies in the Letters and Parcels businesses (building on AusPost's consistent historical delivery of efficiencies in these areas); closure of loss-making metro Corporate Post Offices (CPOs) or transformation to lower-cost store formats; cost reductions in central support functions in line with benchmarks; capital structure improvements using Government debt rather than market debt; and exploration of targeted divestitures. It is BCG's view that these actions are needed to help mitigate the risk of losses, and that they be urgently validated, planned and implemented as they do not rely on changes to regulatory or other instruments. However, it is also BCG's view that these actions will require a step-change in the efficiency of AusPost's operations, and that they **are likely to delay, but may not entirely avoid, a loss-making trajectory for AusPost within the next four years.**

Given this, BCG believes the Government and AusPost should consider more fundamental, sequenced reforms to AusPost's regulatory environment and operations. These reforms would have the potential to deliver more significant and lasting improvements in financial sustainability in the decade to 2030, further reduce the risk of losses in the first half of the decade, and drive commercial returns in the latter half of the decade.

BCG's starting point for considering reform options is that AusPost's overarching purpose, as enshrined in the Act, remains to "supply a letter service" while physical letters are a relevant form of communication for the Australian community and one that cannot be viably delivered by the private sector. AusPost also holds responsibilities for letter delivery between Australia and the Rest of World as part of its membership of the Universal Postal Union. Even under the most rapid declines in letter volumes modelled for this work, Australians will continue to send and receive billions of letters to 2030. This declining but ongoing demand, along with the financial challenges of letter delivery as a business, continues to support AusPost's core purpose and the need for both a letter service and a post office network in some form. Further, since AusPost has a financial imperative to deliver a commercial return given its GBE status, BCG believes that AusPost's purpose should continue to extend to the provision of an appropriate set of additional, related products and services that would deliver a benefit to the Australian community, cross-subsidise its community service obligations, and leverage the organisation's existing capabilities and presence. This will help AusPost to achieve ongoing financial sustainability without undue risk or market distortion, with options that include continuing to operate in the parcels market, and selectively providing other products and services discussed in this report.

The detailed research and analysis undertaken during this review has uncovered a wide range of potential reform options for AusPost to achieve its purpose in a financially sustainable way. While these options can be combined in different ways, BCG has developed a set of **integrated reform paths** for AusPost for 2020–2030. Each path has the potential to reshape AusPost's role over the next decade, including expectations for letter delivery standards, improved financial sustainability and higher commercial returns to the Government, and greater strategic clarity for the business.

The paths are distinct, with each representing a progressively greater level of change for the organisation and, consequently, a path to commercial returns. Each reform path has different financial and non-financial implications for AusPost's stakeholders, including the Shareholder Departments. These implications have been analysed in detail and are included within this report. The three main reform paths that BCG has developed are summarised below.

- **Reform Path 1: A more resilient and efficient AusPost, with a refreshed post office network.** AusPost would maintain its current role and position in the community, continue to invest in parcels and additional services, and drive operational efficiencies. The size of the metro CPO network would be reduced by 106 outlets over the next two years to increase overall profitability, providing some benefit to Licenced Post Office (LPO) licensees' small businesses in those areas, and preserving the current high level of service to customers within the 2.5km regulated radius in metro. The regional and remote (non-metro) footprint would be maintained. [4] AusPost would continue to deliver a range of valued additional products and services, focused in particular on in-person transactional service delivery, and continue to invest in delivering a strong parcels service. AusPost and Services Australia would explore opportunities for partnership, including the potential for AusPost staff to deliver in-person transactional services and the potential for facility sharing.

  This path would likely reduce but not avoid the risk of AusPost incurring losses, and profits would remain modest. BCG expects this path could be delivered without regulatory change, and it has been included in the consideration set in large part for this reason; it would likely require a refreshed Statement of Expectations and explicit support from Government for closures of unprofitable metro CPOs.

- **Reform Path 2: A more resilient and efficient AusPost, with a refreshed post office network and a streamlined letter delivery service.**
  AusPost would maintain its current role and position in the community, continue to invest in parcels and additional services, and drive cost efficiencies. AusPost would streamline its letter

offering to reflect changing customer and communication preferences: reducing letter delivery frequency to three days per week in suburban metro areas, with accompanying delivery speed reductions (D+5).[5] Current delivery frequency would be preserved for the highest-volume customers in central business districts, and for Post Office (PO) Box customers and receivers in non-metro areas.[6] Parcels would continue to be delivered daily. Priority Mail would be removed to enable more streamlined sorting operations. AusPost would reduce the size of its metro CPO network by 106 unprofitable outlets over the next two years to increase overall profitability while ensuring metro residents retain their current level of access to at least one post office within 2.5km of their residence;[7] this would provide benefit to LPO licensees' small businesses in those areas and preserving a high level of service to customers within the 2.5km regulated radius in metro. The regional and remote (non-metro) footprint would be maintained. AusPost would continue to deliver a range of valued additional products and services, focused in particular on in-person transactional service delivery, and continue to invest in delivering a strong parcels service. AusPost and Services Australia would explore opportunities for partnership, including the potential for AusPost staff to deliver in-person transactional services and the potential for facility sharing.

This path would likely contain the risk of losses to a four-year period, and deliver more meaningful dividends later in the decade. BCG expects this path would require changes to letters service standards in the Regulations, potentially greater flexibility in the Enterprise Bargaining Agreement (EBA), a refreshed Statement of Expectations, and explicit support from Government for closures of unprofitable metro CPOs.

- **Reform Path 3: A more resilient and efficient AusPost, with a refreshed post office network, and a further streamlined letter delivery service.**
  AusPost would maintain its current role and position in the community, continue to invest in parcels and additional services, and drive operational efficiencies. AusPost would streamline its letter service and metro CPO footprint more meaningfully: within two years, regulatory change would allow for letters service standards to nationwide alternate-day delivery, with delivery speed reductions (D+5), reflecting changing customer expectations. Parcels would continue to be delivered daily. Priority Mail would be removed to enable more streamlined sorting operations. Street and community letterboxes would also be introduced for greenfield residential developments to help contain the growth in delivery points. The metro CPO footprint would be reduced by 190 unprofitable CPOs over the next two years, with almost all metro residents retaining their current level of access to a post office within 2.5km of their residence;[8] this would provide benefits to LPO licensees, while modestly increasing travel times for some customers in metro areas. The regional and remote (non-metro) footprint would be maintained. AusPost would continue to deliver a range of valued additional products and services, focused in particular on in-person transactional service delivery, and continue to invest in delivering a strong parcels service. AusPost and Services Australia would explore opportunities for partnership, including the potential for AusPost staff to deliver in-person transactional services and the potential for facility sharing.

  This path would likely contain the risk of losses to a three-year period, and deliver increasingly large dividends later in the decade. BCG expects this path would require changes to letters service standards, potentially greater flexibility in the EBA, a refreshed Statement of Expectations, and explicit support from Government for closures of unprofitable metro CPOs.

A fourth reform path that delivers a basic postal service to all Australians has also been explored as part of BCG's analysis, and is discussed later in this report. Pursuit of this path is not recommended by BCG.

BCG recommends that, at a minimum, a strategy along the lines of Reform Path 1 should be adopted to help reduce the risk of losses in the first half of this decade and beyond. If the Shareholder Departments seek material improvements in financial sustainability, BCG believes that this is offered by Reform Paths 2 and 3, while noting their greater impacts on stakeholders (including the workforce). It is BCG's view that the preferred path should be set in motion as soon as possible, given the risk of imminent losses and the long lead times for changes of this nature.

More specifically, from across the broad range of possible reform options for AusPost, BCG recommends that the following actions be undertaken:

1. **Implement a set of near-term efficiencies**, in addition to those in the Corporate Plan, across AusPost's business lines and corporate functions, all of which can be achieved within current regulatory constraints. These efficiencies are likely to involve meaningful change to AusPost's internal structures and processes, and are important to provide greater financial stability, but are unlikely to fully avoid the risk of losses;
2. **Streamline the post office network**, either closing 106 unprofitable metro post offices to give metro residents access to at least one post office within 2.5km,[9] or closing unprofitable metro 190 post offices to give metro residents access to at least one post office within 3.5km.[10] These changes can be effected without changes to the Regulations, and will help to bolster financial sustainability; however, they will involve risk and challenges, and are likely to require explicit Government support and customer engagement. The non-metro footprint should be preserved in its current form, given the ongoing relevance of AusPost's offering in regional and remote communities. Coupled with the efficiencies above, this change can deliver a degree of financial sustainability, but not a commercial return;
3. **Set out a path to reform the Letters business**, including changes to service standards to ensure the Letters community service obligation (CSO) is fit-for-purpose and AusPost has greater flexibility to manage its cost base, and ongoing increases in the BPR. Together, these types of changes will be important for driving a more material uplift in AusPost's financial performance. Reductions in delivery frequency (e.g. to three days per week, as in New Zealand, or alternate-day delivery), which have the potential to realise significant and lasting cost efficiencies, will involve regulatory change and significant disruption for a range of stakeholders (e.g. workforce, senders and receivers) as well as requiring multi-year consultation and implementation;
4. **Establish a clear process to guide AusPost's strategic direction** in additional products and services, helping to strike an appropriate balance between generating additional revenue to cross-subsidise Letters losses (e.g. pursuing in-person transactional service delivery, potentially in partnership with Services Australia) while avoiding excessive capital outlay or risk; and
5. **Take a range of steps to optimise AusPost's capital structure**, including exploring potential divestitures of specific subsidiaries (e.g. StarTrack Road Express, SecurePay).

In addition, if Government decides to further investigate a potential full or partial divestiture of the Parcels business, it should undertake a detailed scoping study to understand the economic trade-offs between retaining Parcels profits and synergies, and releasing cash through a divestiture. BCG notes that divestiture of the Parcels business would remove approximately $150m–$250m in annual NPAT from AusPost's bottom-line, leaving an operating loss from the residual business without meaningful reforms to the Letters business, but could yield a large upfront cash release with potential to fund the ongoing delivery of the CSO if appropriately sequestered.

As at 21 February 2020

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Exhibit 68: Summary of key settings and financial impacts by Reform Path, compared to current state

	Today	Reform Path 1	Reform Path 2	Reform Path 3	Reform Path 4
Letters reforms to be implemented in phase 2 (2022-2026)					
Delivery frequency	5 days per week	5 days per week	3 days per week for suburban metro; PO Boxes daily **($78m)**	Alternate weekdays; PO Boxes daily **($177m)**	2 days per week for all delivery points **($237m)**
Priority Mail	Available	Available	Discontinued **($19m)**	Discontinued **($19m)**	Discontinued **($19m)**
Delivery speed	D+3	D+3	Shift to D+5 **($43m)**	Shift to D+5 **($54m)**	Shift to D+5 **($54m)**
Household delivery point	Residence	Residence	Residence	Residence for most; introduce street/ community for greenfield	Introduce street letterboxes in metro; residence for others
Average price rise 2024–2030	To be determined Standard nationwide price	3% p.a. **($78m)** Standard nationwide price	3% p.a. **($78m)** Standard nationwide price	3% p.a. **($78m)** Standard nationwide price	5% p.a. **($108m)** Standard nationwide price
Parcels reforms to be implemented in phase 1 (2020–2022)					
Delivery frequency	5 days per week	5 days per week	5 days per week	5 days per week	As determined by regulator / operator
Ownership	Wholly owned	Potential for targeted divestitures	Potential for targeted divestitures	Potential for targeted divestitures	Potential divestiture with SLAs
Additional Services reforms to be implemented in phase 1 (2020–2022)					
Product and service offering	SoE allows AusPost "flexibility and discretion" in keeping with the Act	SoE or other instrument (e.g. CFF) sets specific criteria for the pursuit of additional product and service offerings, potentially including partnership with Services Australia			Divestiture of some financial and identity services, esp. digital; retention of streamlined consumer and in-person services offering
Product & Innovation team	Grow in line with business	Grow in line with business	Maintained at current size ($23m)	Maintained at current size ($23m)	Reduced by 6% overall ($31m)
Post office network reforms to be implemented in phase 1 (2020-2022)					
Metro catchment	2.5km	2.5km	2.5km	3.5km	7.5km
Metro CPO closures	Nil	106 **($35m)**	106 ($35m)	190 ($58m)	213 (**$65m**)
Non-metro closures	Nil	Nil	Nil	Nil	Nil
Workforce					
Retail FTE reduction	N/A	Up to 590	Up to 590	Up to 1,045	Up to 1,171
PDO FTE reduction	N/A	N/A	Up to 3,029	Up to 5,066	Up to 6,636
Corp Functions FTE reduction	N/A	TBC (~300 – 500)	TBC (~300 – 500)	TBC (~300 – 500)	TBC (~300 – 500)

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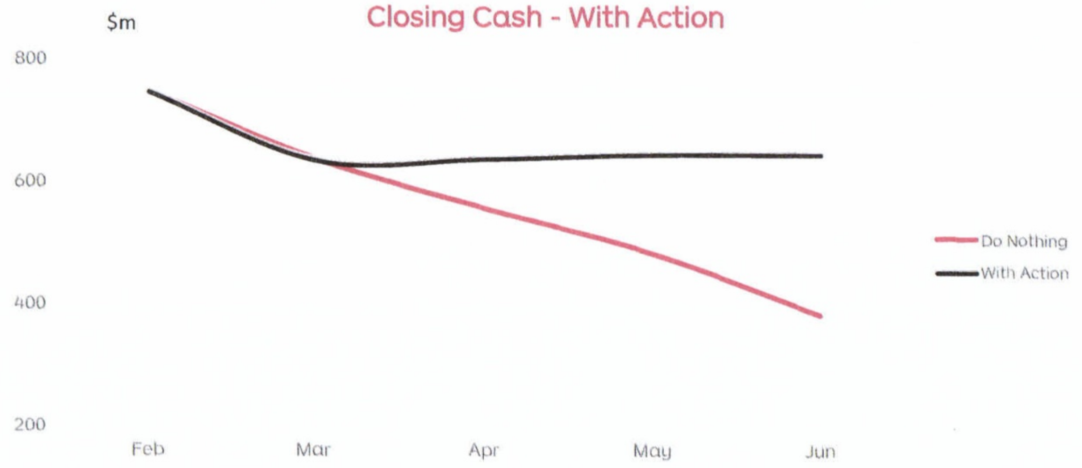
Summary financial impacts					
Reform run-rate (ex. Pricing)	N/A	$35m	$221m	$394m	$501m
Incremental efficiencies	N/A	$143m	$143m	$143m	$143m
Cost of reform (redundancies)	N/A	($56m) one-off cost	($363m) one-off cost	($586m) one-off cost	($680m) one-off cost
Cost of efficiencies	N/A	($104m) one-off cost	($104m) one-off cost	($104m) one-off cost	($104m) one-off cost

Note:

- Price benefits refer to incremental benefit as compared to 2.5% per year price rise over the period
- SoE = Statement of Expectations; CFF = Commercial Freedoms Framework
- Actual PDO FTE reduction may be lower, as higher benefits may be achieved on certain routes / in certain areas by leveraging additional PDO time to deliver parcels (i.e. where PDO can achieve same or lower effective unit cost than parcel delivery contractor by achieving sufficiently high delivery productivity, given fixed salary)

Appendix 5

Closing Cash With Action



		YTDFeb	Mar	Apr	May	Jun	Full Year
No Action	PBT	**35**	41	(103)	(89)	(118)	**(234)**
	Cash	**747**	635	554	480	380	**380**

		YTDFeb	Mar	Apr	May	Jun	Full Year
Action	PBT	**35**	41	(49)	(35)	(52)	**(59)**
	Cash	**747**	635	637	644	645	**645**