4 August 2014

Transcript Q2 2014 results
Analysts' call 4 August 2014

Richard Piekaar
Ladies and gentlemen, good afternoon and welcome to the second quarter 2014 results of PostNL. My name is Richard Piekaar and with me today are Herna Verhagen, our CEO, and Jan Bos, our CFO. Herna Verhagen will start today's presentation with an update on the operational developments and an update on our outlook for 2014. This will be followed by a more detailed look at our financials by Jan. After that we will take your questions. For your information, the presentation will also be webcast live and a recording will be available shortly afterwards today's event. With that Herna would like to start and I hand over to you.

Herna Verhagen
Welcome today for the Q2 results 2014. I would like to start with the second quarter. What we did see in the second quarter is a very strong performance. The revenue was up 3% to a little bit above €1 billion and also the underlying cash operating income for PostNL was up €37 million from €23 million last year to €60 million this year. The strong performance of the second quarter, together with the good performance in Q1, did support our outlook increase which we have given to the market on July 7. On July 7 we issued a press release in which we said the outlook for the end of this year is expected to be within the bandwidth of €260 million to €290 million and I am talking underlying cash operating income. It is increased from the high end of €180 million to €220 million which was the outlook given when we had our meeting in May this year. So very strong performance in the second quarter together with a good Q1support us in the increased outlook. I would like to first of all give you more details on the Q2 numbers and give you a business update where we are at this moment in time. Secondly dive in a little bit deeper into our outlook update. After that I will hand over to Jan and Jan will give you a financial update on the second quarter, but also a more detailed financial update on the outlook for the end of the year.

Let's look into Q2, an update on sustainable delivery of our results and I start as usual with Mail in the Netherlands. In Mail in the Netherlands we see an increase in the underlying cash operating income from €3 million in Q2 last year to €48 million in Q2 of this year. That with a decrease of the addressed mail volume of 11.2%. That is within the bandwidth given earlier to you of 9% to 12%. Of course all cost savings are also planned on a volume decline within that bandwidth. The addressed mail volume and the decrease in the addressed mail volume is still based on substitution, which is 7% to 9%, and competition which is 2% to 3%, so in that sense nothing changed. We see the same division between substitution and competition. So main reason behind the decrease in addressed volume still is substitution. The underlying cash operating income and the good results on the underlying cash operating income are partly caused by cost savings. Cost savings are up if you compare to Q2 of last year from €17 million to €29 million. That is because we do see smooth execution of the reorganisation plans and we are ahead of schedule, which means that cost savings are coming in earlier. In my next slide I will give you an update on where we are on those restructuring plans.

Secondly what we do see, we do see a positive impact of the price increases and the mix effect. We also will give you a little bit more detail on that point. A third reason for the increase in the underlying cash operating income is a one off gain from cross border mail. And we had lower pension cash out in the second quarter of 2014. These four reasons are underpinning the good results of Mail in the Netherlands in the second quarter of this year.

Also important elements in the second quarter were a new CLA. It was a balanced CLA. Of course in that CLA we saw an increase of income, a salary increase, but on the other hand it also was very balanced for us, because it gives us much more flexibility for working on Saturday and that is important when it comes to our mail company, because we do work from Tuesday to Saturday. Secondly, the extra amount we have to pay for working on Saturday is decreased and thirdly, what was also important to us, is that the pension payment done by our employees is increased from 2 to 4%. So a balance between a salary increase and on the other hand much more flexibility and also cost reduction for our organisation. What we are also proud of is that if you look into all those changes and reorganisations they of course impact the people working for PostNL. But those people are taking pride in delivering mail every day to the right address against a very high quality. That is what we did see in Q2 again. A quality in mail delivery of above 97%, which is well above the mandatory level of 95% together with an increased customer satisfaction. So very strong results for Mail in the Netherlands.

As said, first of all a little bit more detail on the strong performance in our restructuring plans. Cost savings are coming in early and that is because of a smooth execution of our restructuring plans. First of all, last year February we communicated that part of that restructuring was the decrease of the depots in the Netherlands from 260 to 125. At that moment in time we are at a 148 and in Q2 we closed 22 depots. So the 125 depots is quite nearby. And that is also the reason why we do think that we will migrate another 25 which means that we will bring down 260 depots to 100 depots before the end of our reorganisation period. What we secondly do after a migration is that we start making our processes in that new depot more efficient. Also those efficiency and optimization processes are ahead of schedule.

The second important part of the reorganisation this year was the reduction from six day to five days a week delivery. And of course we took into account some extra cushion when it comes to bringing it back from six to five days, but the organisation prepared it very well, which means that also here cost savings were coming in more early than expected. We see more efficiency in our car unit. So every day we drive to every letter box in the Netherlands, every post office in the Netherlands, a lot of our customers in the Netherlands where we pick up mail and where we bring mail. What we do see is we can plan those routes more efficient. That means less cars, less kilometres and in the end also less fuel. An important step taken in the second quarter is also the fact that we think we can make the car unit even more efficient to partly combine it with our parcel unit. That redesign is approved by the works council and can be implemented in 2014 and further into 2015.

A third important part of the restructuring plans is the reduction of overhead. Reduction of overhead within our production unit, but also within marketing & sales of Mail Netherlands and at the head office. Also there we are on track and cost savings are coming in as planned. We increased our cost savings target last February to €365 million till the end of 2017. That is still the cost savings target we do think we can reach by the end of 2017. So cost savings are coming in early because of smooth execution of the restructuring plans. The second important reason behind the improvement of our underlying cash operating income is a positive price and a positive mix effect. Let's first take price. As communicated we do follow a pricing policy where we increase bulk mail and domestic single mail items well above inflation. That is what we did in 2013, that is also what we did in 2014 and that is what we are planning to do for the years 2015, 2016 and 2017 as well. The results of 2014 are of course part of the numbers you see when it comes to the results in Q2 and that is combined with a positive product mix and a positive product mix means that we see a relatively slower decline of single mail items versus bulk mail items. Single mail items do have a higher average price and secondly, within the bulk mail we see a positive shift, so there are coming in more bulk mail items with a relatively higher price than a lower price. So those two do bring a positive impact on revenue and therefore also on the underlying cash operating income.

For Mail in the Netherlands also regulatory is important. The regulatory environment in the Netherlands has three dossiers which are important for PostNL. It is a status update I can give you, because none of these dossiers did come to a conclusion yet, but that is what we expect to happen by the end of Q3 or in Q4. First of all of course the Postal Act. In the Postal Act or the amended Postal Act we expect that it will be sent to Parliament in September. That Postal Act is important for PostNL, because in that act they propose to diminish or to bring down the amount of post offices to 1,100, from 2,100 to 1,100, and the amount of letter boxes from 19,000 at this moment in time to around 9,000. In our view if you look into PostNL and if you look into a postal system which is sustainable for the long term, with a volume decline of around 11% at this moment in time, it is not only necessary to do reorganisations in our own organisation, but also to bring back some of the service levels we have to maintain. Therefore this Postal Act is important for PostNL. Secondly, significant market power. The Dutch regulator received of course some powers as of January this year, in which they can look into postal markets and try to find out if there is a case of significant market power. The ACM, the Dutch regulator, issued a press release in which they said we will focus on the unsorted 24 hour bulk mail. They did a market consultation after that, they also started questioning PostNL and that is the phase we are in at this moment in time. So we are answering questions of course for the regulator to make it possible for them to decide if there is a case of significant market power and what they want to do afterwards. I think the most important reasoning which is still followed by PostNL, is that if you look into postal market, we do not see a case for significant market power and that has to do with the fact that the main reason for the volume decline still is substitution. So you have to take into account e-mail and other mobile devices as well. Secondly, when it comes to significant market power, we still do think there are a lot of alternatives available in the market, even in the physical market. When you have 24 hour mail in a lot of the occasions you can also make it 48 hour mail. And next to that with Sandd and of course with some of the regional competitors in the Netherlands, there is an alternative available. We expect a view of the Dutch regulator after summer. Last important part are tariffs. We expect the Dutch regulator to decide on cost allocation and therefore the tariff headroom based on the new tariff mechanism in Q3 2014, so Q3 this year. The new tariff mechanism, to bring it back to memory, is of course that we can increase prices with inflation together with a part of the volume decline of the year before. We are in the middle of that process and expect ACM to decide as said by the end of Q3 2014. So for Mail in the Netherlands a very strong second quarter, strong results, based on cost savings, based on price increases, product mix and also based on a one off we had in cross border mail.

Then to Parcels. If we look into Parcels, we do see that we perform in line with our expectations with a strong volume growth. Volume growth in the second quarter was 8.2% versus 6.9% last year. As you probably remember, the number of volume growth for PostNL is always a mix of to Business (2B) and to Consumer (2C). 2B is growing relating to GDP and that means that our consumer volumes are growing around 10.5%, which is in line with the e-commerce market. This of course translates into revenue. So revenue within Parcels is up 5% from €194 million last year to €204 million this year in the second quarter. The extra volumes together with a good operational efficiency of our new logistical infrastructure is translated in the increase in underlying cash operating income from €20 million to €21 million. What we also do see when it comes to underlying cash operating income that Parcels is impacted by higher subcontractor cost and that is in line with what we mentioned during our presentation in February, where we said we do expect to have higher subcontractor cost in the next coming year, year and a half and part of that is what you see in Q2. Secondly what we do see is there is an ongoing change in customer mix resulting in a limited decline of the average price. This is not price competition, this means that the big web shops in the Netherlands are growing much faster than the smaller ones. That is of course big ones have better prices than the smaller ones and that is the reason behind the slight decline in the average price per parcel.

What we also said during the second quarter is that we are trying to develop the e-commerce market in the Netherlands further by an extension of our services and new products and by innovations. Because we do believe that if you further develop your logistical system, this is not only offering more opportunities and possibilities for you as a consumer, that you as a consumer can decide when, where and at what time you would like to have your parcel, but it also opens new markets and therefore new volumes can come in into our logistical system. I will give you a few examples.

When it comes to the extension of services and new products I think good examples of that is that in Q2 we started with six days a week delivery, so we do deliver Monday to Saturday. We also started with evening delivery on Tuesday and Thursday. We communicated to the market that we have started two pilots. The first pilot is distribute parcels on Sunday. That is what we will do for one customer as of the end of this month. We will add a few more in September and when it is successful, we will open it to all our customers as of January 1 next year. Sunday delivery is not standard delivery, so it does not fit into our Monday to Saturday delivery. It is only when you as consumer wants that parcel specifically on Sunday. That is for us a reason to come to your home and bring the parcel. The second pilot is on fresh food and that is a pilot we are doing in Limburg and Brabant, two provinces in the Netherlands. Fresh food is a huge market and if you look into the fresh food market, 84% of the Dutch consumers would like to have their fresh food delivered at home. But there are not that many opportunities. So what we did in this area, we developed a special package which enables to keep temperature at a low grade and that means that it fits through our normal logistical system. It is a special box, so fresh food can be delivered by our normal physical system to households. That is what we are piloting at this moment in time. It is a new market and that means that if the pilot is successful, it does create new volume within our system. We are rolling out additional parcel points in the Netherlands. We are opening 3,000 parcel points where you can pick up or deliver your parcel. That is what we do in Belgium as well. We see volumes from the Netherlands to Belgium grow by around 25%. We do have our own delivery network in Belgium and with a delivery network you also need drop off points and pick up points and that is what we are opening in Belgium at this moment in time as well.

Important to underpin these business initiatives but also to bring more efficiency is the new logistical infrastructure. 18 depots will be opened, 18 depots and sorting and distribution centres will be opened for parcels in the Netherlands. We already closed 28 old distribution centres and 3 old sorting centres. 16 of those depots are operational at this moment in time, which means that more than 80% of our parcel volume is running through the new infrastructure. That brings in more efficiency and on the other hand creates new opportunities for our customers. New opportunities for example that they can bring their parcel still late in the evening, till 0.00 or 01.00 am in the evening and it is still delivered next day. Secondly we do have new sorting machines in these centres which are able to handle fragile stuff. A new business for example when we did not have almost any wine bottle a few years in the past, we do have a lot of them now, because the sorting machines are able to handle those bottles and we can deliver them via our normal distribution system. So also here innovation and the renewal does bring in new business and new volumes. So for Parcels results in line with expectation, underpinned by good volume growth, especially when you look into e-commerce or the 2C market.

International. In International everything is focussed on enhancing our cash profitability. In International we see revenue growth. 4% revenue growth from €394 million last year to €409 million this year in the second quarter. What we also do see is that the underlying cash operating income is €2 million lower than last year. The results are impacted by the roll out of our end-to-end network in the UK and are impacted by a revenue decline in Germany.

In the UK as you all do remember, we do have our downstream access business, our business in which we sort and collect and bring to Royal Mail for last mile delivery. That business is doing well and we see revenue growth and new volumes within our downstream access business. Next to that we are rolling out our end-to-end network, our last mile delivery network. In the second quarter we did further investments in the roll out of that network. We are still awaiting the outcome of a complaint which was taken in by Ofcom. Royal Mail announced end of last year that they would decrease their prices in the areas where we want to do a roll out of end-to-end and increase prices in the other areas. That of course hinders the roll out of our end-to-end network. For that we put in a complaint to Ofcom which they accepted and we are waiting for the outcome which is expected by the end of September 2014.

In Germany we see two things. We see a lot of new volume coming in into our national and regional business and we do see that we are impacted by competition in our consolidation business, the Postcon business. We are impacted by for example Compador and they impact in two ways. We see less volume, that is one, and secondly, because of competition, prices decreased. So positive developments together with fierce competition leading to a revenue decline in Germany in the second quarter. Then Italy. In Italy we see further growth in Formula Certa. Next to that, we are on track for a nationwide coverage of 80% of all households which we want to reach in 2015. In Italy we did our rebranding, so the company is not called anymore TNT Post Italy, it is now called Nexive. That rebranding was done this year in May.

So if I would summarize the second quarter for PostNL, it is a strong second quarter. It is a strong second quarter when it comes to revenue and especially when it comes to underlying cash operating income. It is mainly underpinned by better results of Mail in the Netherlands, results for Parcels were in line and results for International were slightly behind last year. The good results of Q2 and of course the results of Q1 are reflected in our increased outlook. If you look into the main drivers behind that increased outlook, they are more or less the same as the reasons behind the good performance in the second quarter. It is first of all the smooth execution of the restructuring plans, which resulted in cost savings coming in more earlier at a lower restructuring cash out. It is secondly also for us important, cost consciousness with all our managers and employees which leads to better cost control and that is beyond restructuring. Thirdly, within letters we have a higher average price due to of course price increases and a positive mix effect. And fourth, we have a positive effect because of an incidental mainly in cross border mail. This has led to updated year end targets. The underlying cash operating income to €260 million to €290 million coming from the higher end of €180 million to €220 million, but also of course an increase in cost savings. We forecasted previously €95 million to €115 million and we are expecting now €115 million to €135 million. Thirdly restructuring cash out. We can do these restructurings against a little bit less cash out than expected. We expected a cash out of €50 million to €70 million and it will now be within the bandwidth of €40 million to €60 million. The half year results fuel our confidence in of course the given outlook for the end of the year to €260 million to €290 million, but it also fuels our confidence that we can deliver our targets 2015. So 2014 for us is a year in which we further solidified the foundation of our organisation. We are adjusting our Mail organisation to maintain profitable with motivated people working hard every day to deliver against a high quality. We are building and expanding in parcels and we do think that with an extension of our services we can underpin volume growth in the e-commerce market which in the end brings also extra volumes in within PostNL. We are working for a company towards a sustainable delivery of cash and lower financial risks. That means that in 2015 we have created and will create a company which runs efficiently a mail and parcel network, which is further in restoring its credit rating and we do expect that under current conditions we will pay dividend in 2016. I would like to hand over to Jan to give you more financial details on the second quarter and the outlook.

Jan Bos
Okay, thank you, Herna. I will start with financial highlights of the quarter. Reported revenue was up 3% this quarter and reported operating income increased by €50 million to €85 million. To get a better understanding of the actual underlying performance the reported operating income is adjusted for one offs. The one offs this quarter, totalling €3 million, were rebranding and a small net release of provisions. Then we come to our main KPI, which is underlying cash operating income and this is underlying operating income adjusted for the cash effect of pensions and restructuring of €28 million. Underlying cash operating income increased by €37 million to €60 million, which is mainly driven by strong savings, positive price mix effects and some incidentals more than offsetting the volume decline of Mail the Netherlands and autonomous cost increases. Looking at net cash from operating and investing activities that was minus €5 million this quarter, an improvement of €31 million, mainly explained by the higher operating results.

Let’s now look at the results per segment, first at revenue. Revenue from Mail in the Netherlands in the quarter was almost flat, compared to the second quarter 2013, at €479 million. The volume decline of 11.2% was compensated by a positive price effect on addressed mail and a change in revenue mix. Revenue of parcels increased 5% to €204 million with 8.2% volume growth. We saw the change in customer and product mix continue from the previous quarter which had a limited negative impact on the average price per parcel. In International revenue increased by €15 million to €409 million, all countries contributed to the growth except Germany, where we feel the impact from competitive situation in the consolidation business. Adjusted for the currency effect, revenue in International was up 2%. Then onto our underlying cash operating income. Underlying cash operating income in Mail the Netherlands increased by €45 million to €48 million. I like to highlight that the underlying cash operating income margin of Mail the Netherlands came out at 10%. Main contributors to that increase were the cost savings and some incidentals. I will show a complete picture of the main drivers on my next slide. In Parcels underlying cash operating income increased by €1 million which is explained by a better business performance. I like to highlight that Parcels was influenced by €2 million additional subcontractor cost compensated by €2 million one offs, mainly caused by the CLA last year in Parcels. The underlying cash operating income in International was down €2 million compared to last year. This is explained by the roll out of end-to-end and the continued competitive pressure in Germany. Then looking at PostNL Other, where the underlying cash operating income was down €7 million. The difference is mainly explained by higher IT implementation cost and other project costs.

Now into more detail on Mail the Netherlands. As said underlying cash operating income in Mail the Netherlands increased by €45 million to €48 million. The drivers that helped this improvement were a positive volume price and mix effect of €6 million, cost savings of €20 million excluding €9 million for pensions visible in pension cash, the incidental gain in cross border mail of €9 million and finally lower cash out for restructuring and pensions. These more than offset autonomous cost increases of €9 million.

Then the statement of income. Since the sale of half of our stake in Q4 last year, the results from TNT Express are accounted for as financial assets available for sale and changes in fair value are recognised in other comprehensive income. Excluding TNT Express our profit for the period increased by €37 million to €42 million, mainly the result of the improvement of our operating income offset by some higher income taxes. Then turning to cash flow. If you look at the cash generated from operations you see an improvement of €31 million, from €2 million to €33 million. This is mainly explained by an improved operational performance. We also had slightly lower capex this quarter, mainly as a result of lower investment in the restructuring of Mail the Netherlands and continued tight capex control. Overall net cash from operating and investing activities was minus €5 million, an improvement of €31 million compared to last year.

Our focus on cash remains visible in the performance of our cost savings and also in our capex performance. The total cost savings came in at €29 million. In the related restructuring cash out we continue to see some phasing effects, mainly into next year and also the implementation cost show some phasing effects mainly to the second half this year. As Herna already showed you, we have increased our cost savings target to between €115 million and €135 million and we have also adjusted our expectations for restructuring cash out for the full year downwards to between €40 million and €60 million.

Then to pensions. This slide gives the usual overview of the coverage ratio. The coverage ratio of the main pension fund was 113.4% at the end of the second quarter. The increase of 1% is mainly explained by the asset performance of the pension fund, partly offset by the effect from decreased interest rates. The pension expense in operating income in the second quarter amounts to €29 million, slightly lower than last year. The cash contributions were €46 million which is significantly lower than the €62 million last year. The decline in cash is attributable to the reduction of workforce, but also to the new pension arrangements we closed last year with the unions.

Then we have a look at the balance sheet. Consolidated equity is minus €618 million, a small improvement of €7 million compared to last quarter and on the next slide I will elaborate more on this development. For your information, we restated the opening balance 2013 for an adjustment of €17 million on current liabilities with a similar effect on equity. Corporate equity level levels around €1.9 billion and remained at around the same level compared to the end of Q1. At the end of Q2 net debt was almost €800 million which is also in line with last quarter. Now let's talk about the equity development. Total equity attributable to equity holders of the parent increased to minus €618 million from minus €625 million. The increase is the net result of the profit for the period of €44 million. The decrease of the book value of the stake in TNT Express of €49 million and an actuarial gain of €14 million relating to pensions and some other impact of €2 million. The decrease of the value of TNT Express is related to the share price decline from €7.12 to €6.51 at the end of Q2. The positive effect from pensions on equity was plus €14 million this quarter and this is explained by the fact that the discount rate was unchanged compared to the end of Q1 and this is the result of PostNL further improving the discount rate setting methodology. This is done by excluding bonds from government agencies and changing the basis for extrapolation of the longest term bond from a single bond to an average of bonds. The result in discount rate is around 0.3% higher than based on the previous method. Please note that our financial and equity position will continue to be vulnerable to changes in interest rates which will impact the pension position. Of course an environment of higher interest rates will be positive for equity.

To conclude a final look at our outlook for the full year. We have updated underlying cash operating income margin for Mail the Netherlands from 6% to 8% towards 9% to 11%. We expect our full year underlying cash operating income to come in between €260 million and €290 million. As Herna already explained, the main drivers behind this update are the smooth execution of the restructuring, including lower restructuring cash out, the cost conscious mindset in the company, a higher average price on Mail the Netherlands on the addressed volumes and a positive impact from incidentals mainly in Q2. To summarize this quarter, all in all a good quarter and also better than we expected. With that I would like to hand back to Richard for the Q&A. Thank you.

Richard Piekaar
Okay, thank you Jan. Indeed we will now turn to the Q&A session. Before we start I would like to ask everybody who is asking a question, to state his or her name before asking the question and also the company you work for. For the people on the call you can register you question by pressing star 1 on your phone. We first take the questions here in the room, but after a number of questions we will turn to the call. Okay, first question from here. Philip, you get the second one.

Maarten Bakker, ABN AMRO
I have a question about the cost, ABN AMRO by the way, cost savings target that you communicated for 2017. You stick to the €365 million for 2017. On the one hand you say there is a more cost conscious environment within PostNL that delivers additional savings and you also say that the, you are scaling down to 100 depots, so 25 more than initially planned. So, I mean, it seems like you are taking more measures and you are having a good performance, yet you are keeping the savings target unchanged. That is my first question. And then a very short question to Jan. The cash out is merely, for 2014 the guidance is merely a phasing effect, right? I mean, the cash will be out in 2015.

Herna Verhagen
Your first question on the cost savings targets. Cost savings targets till the end of 2017 is €365 million. The cost conscious environment is of course, that is what we see happening. The €365 million are based on restructuring plans and restructuring plans, part of them, I did mention in my presentation like the migration of depots, like the efficiency of car units. There we will go to a 100 depots instead of 125 depots is part of the €365 million. As you probably remember, we did increase that target by €75 million last February. Two third of that €75 million was based on current plans where we do better than expected. This is one of the plans where we do better than expected. So that is the reasoning behind the unchanged 2017 cost savings target. On cash out you were already knocking head, so the answer is yes, it is merely phasing.

Maarten Bakker, ABN AMRO
Then the last question. I mean, you have almost completed the roll out of the new logistics infrastructure in Parcels. Have the benefits of a more efficient infrastructure been cancelled out by a let's say competitive pressures or something? Because I mean, the result has been largely unchanged. I mean, has there been or have there been other effects?

Herna Verhagen
The more efficient infrastructure is indeed more efficient. It means that the results out of that better efficiency are not levelled out by competitive pressure. What you do see in the results of Parcels is partly what we did see over the last few quarters and that is a slightly lower average price per parcel. That is impacting the underlying cash operating income. Secondly higher subcontractor cost. When we talked to each other last February we did decrease the margins on parcels from 13% to 15% to 11% to 13%. That is still what we expect to reach this year for example the 11% to 13%, but part of that decrease were higher subcontractor cost and those you see in the numbers of the Q2.

Maarten Bakker, ABN AMRO
But the higher subcontractor costs were, amounted to €2 million and those were offset by some one offs, Jan mentioned. What are those one offs?

Jan Bos
It is mainly the CLA last year which had a negative cost impact that time, incidental.

Richard Piekaar
Okay, then the microphone will go to one in front.

Philip Scholte, Rabobank
Yes, thank you, it is Philip Scholte from the Rabobank. First of all, Jan probably. You again say you expect to pay a dividend in 2016, but taking this as a starting point the more than €600 million negative equity would imply that you expect to make a more than €300 million net profit per year in the next two years. That still sounds a bit optimistic to me or my modelling is completely incorrect. How do you plan to get there? My second question is on the cost reallocation. Is there still an impact of a reallocation from other two business segments or the other way around and can you quantify that? And the third question if I may is, your plans with the TNT stake. Why on earth did you not sell the remaining stake at the time that the lock up expired?

Jan Bos
Okay, first of all on the dividend expectation. We expect to pay dividend in 2016, so an interim dividend. That is one and secondly, in the expectation of the equity improvement is included also improvement on pensions. So in the other comprehensive income. That is the first answer. The second answer is on cost allocation. There is no cost allocation impact this quarter between the segments. The third answer, like we said in December last year, we expect to sell our stake in the medium term and that means two to four years.

Richard Piekaar
Okay, who has the next question? First row here in the middle please.

Henk Slotboom, the IDEA!
About the subcontractors in parcels. You recently signed a deal with SubcoPartners which basically if I do my maths correctly, it means that they earn the equivalents on the basis of normalized volumes and those kinds of things of close to €21 per hour. If I deduct the cost that they have to take for themselves, then you arrive at an hourly compensation which is more or less the same as what you are paying your mail deliverers. Do you think that that will make it more easy for the Social Affairs Minister to digest the deal with the Subcos? Because if there is no difference anymore between CLA based wages and the compensation you pay to your subcontractors, for you that must be an enormous advantage, because you still have the flexibility in place which you don't have in the case of your own staff. That is one question. Secondly and that is purely for my understanding, if I look at the volume in parcels, does that, is that one way traffic or does that include returned logistics as well? Thank you.

Herna Verhagen
When it comes to subcontractors we do expect of course to have more cost when it comes to subcontractors that is also what we already said, presented last February. I think the discussion which is done by the Ministry of Social Affairs, is a broad market discussion. So the, what he is discussing is of course is the position of independent workers in Dutch society. We have more than a million independent workers already in the Dutch labour market. So he is thinking about how can we make such a big independent working community, how can we make that sustainable for the long term? Therefore he wants to take actions which are part of a new law which he brought to Parliament for example. It is not a specific discussion on PostNL. And that is also not the way we are discussing with the Minister of Social Affairs. It much more has to do with how do you build a sustainable labour market in the Netherlands and what is then the position of the independent workers. Secondly, when it comes to volume in Parcels, is it one way traffic? Yes, it is.

Marc Zwartsenburg, ING
A couple of questions from my side. First of all on the Parcels division. You reiterate your target of 11% to 13% margin. In the first half you are just above the 11%, but in the second quarter for example not. May be seasonality, but how do you expect to achieve say a mid-range of that target also in the years beyond 2014? Can you perhaps give a little bit more colour in terms of efficiency, et cetera. That is my first question. The second question. The €9 million one off in Mail the Netherlands in the second quarter, I think from the raised guidance around €20 million is sort of incidental. How does that phase through the quarters to come, so Q3 and Q4? Then my third question. I want to come back on Philip's question on the equity and the dividend. Of course Jan, you mentioned that it is for a big part also dependent on the discount rate. Is there anything else from an accounting perspective that you can do to accounting wise raise the equity position? Is there something you can do there that might help the negative equity? Then a final question on International. Excluding UK the result is zero. It still requires investments. Tough market conditions in Germany. What is the reason to keep it within PostNL? What is the strategic reason to still stick with international mail? That was my last question, thank you.

Herna Verhagen
So first of all the 11% to 13% of parcels. We did give guidance for 2014 and 2015. Of course when it comes to the 11% to 13%, for this year we do think that we can reach that target like also for next year and that is based on operational efficiency. It is based of course on further growth of the amount of parcels which we do see continue. It is based on new services we bring to the

market, so that is where it is based upon. When it comes to the €9 million one off and the phasing through the quarters, I would like to hand over to Jan.

Jan Bos
Okay. So I think the phasing, the €9 million is just a one off in Q2.

Marc Zwartsenburg, ING
What is more to come in the second half over the quarters?

Jan Bos
I think there is not a lot more to come.

Marc Zwartsenburg, ING
So incidentals that were in the raised outlook are not.

Jan Bos
It is at around €15 million in total.

Marc Zwartsenburg, ING
€15 million, so the rest was already in Q1 you mean.

Jan Bos
Yeah, may be a small part in Q3 or Q4, but in total €15 million around. The third question on equity dividend. So, yes we have looked of course and always looking at improvement of our methods for accounting. So we looked this quarter especially at the discount rate setting methods. There we saw some improvements, also in line with our present method, which had a positive impact of 0.3%, but we also are aware of the fact that especially in corporate bonds interest rates are declining.

Marc Zwartsenburg, ING
So the improvement in the discount rate you mentioned on the slide, that is new, that is not the improvement that we already have seen last year? It is additional.

Jan Bos
No, it is an improvement in the second quarter. Yes.

Marc Zwartsenburg, ING
Okay.

Jan Bos
Otherwise the interest rate decline would have had a negative impact on our equity.

Herna Verhagen
Your last question on International. The international business is steered for cash profitability. That means for example for Germany we are further looking into restructuring and cost reductions but also volume growth. When it comes to Italy and when it comes to the UK, their business is good business, is cash profitable business. So why stick to International? I think that answer is already given a few times by us, we are acting rational when it comes to International. So we are not in International to be in International, we do act rational when necessary.

Marc Zwartsenburg, ING
May be to come back on the first one, on Parcels. What did you take into account in the 11% to 13% margin target also for beyond 2014 in terms of price pressure? That is based on the price pressure you have seen in the beginning of the year when you changed the outlook?

Herna Verhagen
What we did take into account when we gave the outlook 11% to 13% in February, was of course the extra cost we see in subcontracting and the extra cost we see in services and innovation. That was the reasoning behind the decrease to 11% to 13%. We do expect indeed that the price decrease or the slight price decrease as you see, that they will slightly continue and that has to do with the fact that your and my behaviour is merely that we go to the big web shops where we buy parcels and to a lesser extent to the smaller ones. That is what is behind that trend.

Marc Zwartsenburg, ING
Thank you very much.

Richard Piekaar
Next one for a question. On the other side of the room.

Wijnand Heineken, Independent Minds
A few questions if I may. First I am a bit puzzled with a few of your slides. First as far as cost savings are concerned. On slide 5 you mention within Mail in the Netherlands €29 million and in the bridge I believe on slide 20, it is €20 million. So I was wondering what the difference has caused. The other thing you mentioned about price volume effects within Mail in the Netherlands. Is there any main difference in trends for individual mail and bulk mail as far as volume is concerned? Is there any significant change in the contribution single mail is having in the Dutch mail business? Thank you.

Jan Bos
To answer your first question, Wijnand. The difference as already explained, it is €9 million in the line pension cash out. So part of the savings are also savings on pensions, but it is on cash pensions so that is the difference. On the trends this quarter, we have seen positive mix effects especially by a change in mix in the bulk mail, but also in that the volume decline on single mail was a little bit less and on bulk mail a little bit higher. In total it also had a positive price mix effect on our total volume.

Wijnand Heineken, Independent Minds
As far as contribution is concerned, because I believe some time ago individual or single item mail or something like was 7% of the mail business. Is that now materially different?

Jan Bos
Not materially different, but if the volume decline on single mail, so individual mail is lower, then the share will be a little bit bigger.

Wijnand Heineken, Independent Minds
But not beyond 10% for instance?

Jan Bos
No.

Richard Piekaar
Okay, André Mulder, on that side please.

André Mulder, Kepler
Two questions. Firstly, can you remind us where we are in terms of capacity utilization in Parcels? If you look at the new infrastructure what level of extra cost are you still incurring there running double networks? Third one, looking at the cost savings made for the first half and the €365 million target, how much of that €365 million has left now?

Herna Verhagen
Your first question on the utilization of our new logistical infrastructure. When we have those 18 centres up and running, we do think we can handle in those centres around 170 to 180 million parcels and by the end of last year we were at a 130 million parcels. I think the reasoning behind the fact that we built 18 sorting and distribution centres and not 2 or 3 is that it is quite easy to copy them without a big investment. So that is the reasoning behind having 18 instead of in the old infrastructure having 3 very big sorting centres. But still some volume to go before we are at max utilization. Then secondly the extra cost for double network. Almost gone, which means that is also what was in my slide, we closed 28 of the old distribution centres and we closed 3 of the old sorting centres, so almost all old infrastructure is closed at this moment in time and almost up and running in the new one except of Amsterdam, where we still have to open a new logistical infrastructure building. Then your third question on cost savings. €365 million of cost savings till the end of 2017, that was the number. Last year we did around 95, so that means we are now around €270 million. This year we expect somewhere to be €115 million to €135 million, so to do in 2015, 2016 and 2017 is somewhere between €135 million to €155 million of cost savings.

Richard Piekaar
Okay, one final question from here in the room.

Sander van Oort, Kempen
Two questions if I may. First of all on Parcels. I was wondering to what extent the new business initiatives like Sunday delivery, had a negative impact on the second quarter performance and to what extent that might also result in a temporary lower profitability in the first quarter after the new services will be offered. Secondly on the capex. You lower your guidance for this year. Does that mean a shift into next year or is it a more efficient capex programme and we will not see a step up next year?

Jan Bos
First question, it is about the impact of new growth initiatives. It is about €1 million this quarter. We already elaborated that also in the adjustment of the guidance last year, that of the €20 million change in parcels €15 million came from subcontractors and about €5 million on investments in new innovations. On capex I would say both shift and also tight capex control.

Herna Verhagen
And it is not because of Sunday delivery, because that was the example you were given, but that will be started by the end of August, so it is not Q2.

Richard Piekaar
Okay, I would now like to give the people on the conference call the opportunity to ask some questions. Could you please open the line?

Operator
Thank you. Your first question is from the line of Joel Spungin from the Bank of America Merrill Lynch, London. Please go ahead.

Joel Spungin, Bank of America Merrill Lynch
Good afternoon. Actually a couple I just want to follow up on. The first impression, I am just wondering if you could just clarify with the mail volume numbers you quoted, the difference between the 11.2% and 12.1%, what is that underlying number? My second question was just, you mentioned obviously the one off from cross border. I was wondering if you could just specify exactly what that is, just to help clarify for us. And then finally just coming back on this point about price mix in addressed mail. Is it possible for you to break it out between both the price inflation and the mix change?

Herna Verhagen
All right then, the first question, clarify mail volume, 11.2% and 12.1%. It is partly because of a working day effect and it is partly because of elections. Then the one off cross border. When we talk about cross border mail it is the distribution of mail from the Netherlands to other countries and from other countries to the Netherlands. There is of course always some discussion around the tariffs which we have to pay for the volume bringing into other countries and the other way around. Once every few years there is a calculation done and that calculation is in most of the occasions around zero, slightly negative or slightly positive. In this quarter it was much bigger and that was the reason for a positive incidental of €9 million. Thirdly, on your price mix in addressed mail and the price inflation on postal items. To be honest I do not exactly understand what sort of answer you would like to have.

Joel Spungin, Bank of America Merrill Lynch
I just want to get a feel, because obviously if the positive pricing is coming from the mix change, then obviously that will have no impact on the sort of volumes, but I just want to get a feel of how much it actually is from increase in prices versus the benefit in mix change.

Herna Verhagen
Okay. I think if you look into the positive effect we did see in Q2, it is partly because we did increase prices in bulk mail as well as in single mail items and that is on average an increase which is well above inflation. In the 11.2% of volume decline is of course taking into account the effect of price elasticity and it is also partly because product mix is changing and that is because of that we have, that the decline in single mail items which have a higher average price is a little bit less than the decline we see in bulk mail. Secondly, in bulk mail we do have more mailings coming in with a slightly higher average price than the lower average price. It is a mix effect. It is partly because of price increases and partly because the mix of volume coming in is slightly changing.

Joel Spungin, Bank of America Merrill Lynch
Okay, thank you.

Richard Piekaar
Okay, next question in the call please.

Operator
The next question is from the line of Andy Jones, RBC Capital Markets. Please go ahead.

Andy Jones, RBC Capital Markets
Hi there, good morning everyone. Sorry, good afternoon rather. I had three questions, please if I could. The first one just on the significant market power. I was wondering if you could help clarify the amount of revenue which you generate in the 24 hour unsorted bulk mail sector and what the prices have done there in the last few years. My second question is on pensions and going back to the equity position. I think you kind of eluded that you have done quite a lot, things are under control regarding the equity position. What could you remind me of the sensitivity? Where would interest rates need to go to in order to get you to a position where you can pay dividend? My final question is on the restructuring. What is the physical process of depot migration and what has gone right in the roll out so far? I would just be interested to hear what has been the cash out cost of coming in slightly lower than planned there. I guess usually when you progress faster than you expect cash out can come quicker rather than slower. Thank you.

Jan Bos
On SMP, on the 24 hour bulk mail volume unsorted it is about say 20%, 25% of our volume, so on average price it is higher, so it is above 30% of our revenue base and then only on the addressed mail revenue, so it is only part of the revenue of Mail the Netherlands. On pension equity, so if you look at the interest rates belonging for let's say pension improvement, you also have to look at the return on assets, so it is a little bit difficult to answer. But you need a little bit higher interest rates.

Herna Verhagen
Then on restructuring and the reasoning behind or what is the physical process we are running to do the migration of those depots and the cash out, I will answer that question as well. But first of all around the process, how do we optimize the amount of depots we have in the Netherlands. We look of course into regions or regional areas and try to find out what is the most optimal way of doing our mail business in that area. We try to make use of buildings we already have. So the buildings which we can leave, because we can sell them or we can rent them to someone else, we will leave as soon as possible, making sure that cost savings coming out of leaving those locations are coming in. What we do secondly is bringing those processes together on a new location which in most of the occasions is already an existing location within PostNL. Reason why we are doing quicker and also why we are doing it better when it comes to efficiency, is because of the fact that optimization is done together with local management and local people. So what we try to do together with local management is to find out what is the most optimal way of working at this moment in time for your region. That makes that there is a buy in from the people who have to do the change and there is a buy in from the people who are part of that change. It is never easy, because in the end of course it also means that there will be a reduction of the amount of jobs we have in that area, but by doing it together with the people who do have regional knowledge, what you do see is that we are able to do it quicker and bring in savings earlier. So why is it not all then restructuring cash out, in other words why is the cash out this year lower and will there be a phasing effect. That has to do with that not all cost savings which are coming in in Q1 and also in Q2 are cost savings related directly to people. When you remember the examples I gave, I also for example gave an example around the optimization of

car routes. And the optimization of car routes is also about less cars, less kilometres, less fuel. That does not have a direct impact on people. When I talked about the optimization of locations, what we try to do is to leave locations which we can rent to someone else or which we can sell. That also brings in cost savings which are not directly related to people. We still do think that with reaching the €365 million of cost savings it will impact 2,700 people to around 3,500 people, so that is still the reasoning or that is still the thinking behind reaching the €365 million. Therefore we need restructuring cash out. So it will mean that there is a little bit less people this year and a little bit more people probably next year and that is the reason why we say there is a phasing effect in the cash out.

Andy Jones, RBC Capital Markets
Okay, thank you very much. Could I just have one very quick follow up? Could you clarify whether the €365 million costs includes reductions in pension cash out?

Jan Bos
About €40 million.

Andy Jones, RBC Capital Markets
It is included in the target?

Jan Bos
Yes.

Andy Jones, RBC Capital Market
Okay, thank you.

Richard Piekaar
Okay, next question please.

Operator
The next question comes from the line of Hugo Turner from Credit Suisse, London. Please go ahead.

Hugo Turner, Credit Suisse
Hi, two questions from me please. The first, could you just give me a bit of detail around the ruling you are waiting for in Germany. That is the first one. The second one, looking at the international business focussed on the UK, I assume that you have been paying for the capex for the roll out of that deal. Was that through your joint venture partner was supposed to be paying the capex. I know the deal has not gone through, but is there going to be a change of the structure of the deal if you do win the actual pricing appeal?

Herna Verhagen
First of all on Germany. On Germany the cases running with the regulator in Germany are the normal cases around predatory pricing, which means that competitors are following us very closely in their pricing. So it is not a specific case like we have in the UK, these are the normal cases around using pricing instruments by competitors. What we do say about Germany and that is what we also said in May and last February, is that the support of the German regulator is important for the success of our business in Germany. When it comes to the international business in the UK we are awaiting the outcome of the complaint there with Ofcom. We did

investments in Q2 in a further roll out of end-to-end with the reasoning that we are of course positive around the outcome of the complaint with Ofcom. We do not foresee a change in the structure of the joint venture at this moment in time.

Hugo Turner, Credit Suisse
Okay.

Richard Piekaar
Okay, thank you. Next question please.

Operator
The next question is from the line of Marc McVicar from Nomura London. Please go ahead.

Marc McVicar, Nomura
Good afternoon. A couple of questions. The first question. Can you just remind us of what the space is within Parcels of B2B and B2C?

Herna Verhagen
More or less 40% is 2B and 60% is 2C.

Marc McVicar, Nomura
So 40% B2B and 60% B2C, okay. Thank you. Then can I just again to clarify on the joint venture in the UK, the formation of that is being stopped or has not happened because of the investigation or because of something else?

Herna Verhagen
It has been the formation has been stopped because of the investigation which is done by Ofcom and we are awaiting the outcome of our complaint which is accepted by Ofcom.

Marc McVicar, Nomura
Okay, and so if your complaint is not accepted, does that mean that the joint venture can still be formed or that would stop it forming?

Herna Verhagen
PostNL as well as LDC are positive about the outcome of the complaint with Ofcom, so I would not like to speculate on a negative outcome at this moment in time.

Marc McVicar, Nomura
Okay, thank you very much.

Richard Piekaar
Okay, thank you. Next question please.

Operator
The next question is from the line of Matthew O'Keeffe from Berenberg London. Please go ahead.

Matthew O'Keeffe, Berenberg
Thank you. Two of my questions were just answered. I do have one other. Just staying with the international business. Of the 3% growth that you have seen in the UK, how much can we attribute to the old access business and how much to the new end-to-end business? That's it for me.

Herna Verhagen
Okay, the 3% growth is in total downstream access. The reasoning behind that is, when we fill the end-to-end network it is done by volumes which are already in our downstream access network and are no longer delivered by Royal Mail, but are delivered by the postman of TNT Post UK. So when we are talking about 3% revenue growth it is all downstream access.

Richard Piekaar
Okay, thank you. The next question please.

Operator
The next question is from the line of Wenchang Ma JP Morgan London 1.16.08

Wenchang Ma, JP Morgan
Thank you very much. Good afternoon everyone. Most of my questions have already been answered, just one quick follow up please. So when you talk about the positive product mix in Mail the Netherlands, I am just trying to figure out what is again the main driver there. Do you see actually change among the customer groups or do you see actually customers opting for some more expensive products? How sustainable do you think that trend last? Thank you.

Jan Bos
It is just change in product lines, so we see lower declines for example in the higher expensive products, but not customers choosing for more expensive products.

Wenchang Ma, JP Morgan
Okay, thank you very much.

Richard Piekaar
Okay, thank you. Then I think we have time for one more and last question from the call please.

Operator
The last question is from the line of Damian Brewer from RBC London. Please go ahead.

Damian Brewer, RBC
Yes, good afternoon. Thanks. Three questions I just want a clarification on please. First of all, on your UK position. Is it the complaint and investigation or completion of the Ofcom review that is running separately that the key triggers there for getting LDC on board? Secondly, on the Parcel business. The numbers you gave us earlier, if you are saying a 10% growth for this year, you be doing about 140 million on capacity of 170 million to 180 million when all full 18 centres are up and running. Now it is an average over the year. Do you have enough capacity to meet the peak or will you need more capex and in time to expand that sorting centre network? And then very finally one for Jan. Given the confidence you have in being able to pay an interim dividend in 2016, what net has to happen with the pension position to provide enough equity in the business you be able to pay that?

Herna Verhagen
So what Ofcom did when we brought in the complaint around the new tariff system which Royal Mail would like to introduce, is that they started of course reviewing the complaint, but they also started reviewing the regulatory and postal system in the UK, so they are both important when it comes to the outcome of our joint venture with LDC, because they are both impacting of course roll out of end-to-end. Now when it comes to the 130 million parcels which we have done by the end of 2013, yes, the network is built on also delivering on peaks, because we do have peaks of course around Christmas and some other moments in the year, so that is how the network is designed. The reasoning why we have in the end 18 depots in the Netherlands, 18 new logistical infrastructure depots is because of the fact that it is much easier if we have to expand because volume is further growing than if we have to expand we can much more easily expand at a much lower investment. So we do not see that as an issue to be honest. I do see it as an opportunity, because then there will be even more growth in the e-commerce market than expected.

Damian Brewer, RBC
Okay, but that is more to learn if you try it on when you need them.

Herna Verhagen
Yes.

Jan Bos
For your last question. The confidence is built on the say interest rate at the end of last year. That was 3.5% and on normal return on assets. And of course we always say that our equity position remains vulnerable for interest rate movements.

Damian Brewer, RBC
Okay. So just to be absolutely clear, if you had to put a probability on your ability to pay the dividend in 2016. Where is that today versus where it was last year?

Jan Bos
Same confidence I would say.

Richard Piekaar
Okay, thank you very much. Thank you all for joining us today here in Amsterdam and for everybody on the call to dial in. If there are any follow up questions, please don't hesitate to give Inge or me a call. Hope to see you in the next quarter. Thank you.