THE IMPACT OF COVID-19
ON THE UK HAULAGE SECTOR

SECTION 3: What is the Future for the UK Haulage Sector after COVID-19?

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WHAT IS THE FUTURE FOR THE UK HAULAGE SECTOR AFTER COVID-19?

In the ***first*** instalment of our three-part analysis on the impact of COVID-19 on the UK Haulage Sector, we explored the current coronavirus Pandemic, possible recovery scenarios and the evolution of the Pandemic's social and economic impact.

In our ***second*** instalment, we looked at lessons from the 2008 Great Recession — interpreting how this affected the UK haulage industry and, in particular, employment numbers within the Transport and Storage Sector and the UK LGV driver workforce.

This ***final*** instalment combines the key conclusions from the previous two sections to predict how the UK Haulage Sector and the LGV driver market will be affected by the COVID-19 Pandemic crisis, the subsequent recession and recovery. It's our hope that this report provides a useful basis for understanding our current circumstances and will help hauliers decide what they can do now to maximise their chances of survival to eventually come out with increased competitive advantage.

Our Report **COVID-19 & Its Impact on the UK Haulage Sector** is structured into 3 sections:

SECTION 1: Economic Crisis, Recession & Recovery Scenarios

We explore the current COVID-19 Pandemic and the consequent social and economic crisis. We look at how this is likely to evolve over time and we develop a number of possible recovery scenarios.

SECTION 2: The Effects of Recession on the UK Haulage Sector

We look at lessons from the 2008 Great Recession. We interpret how this affected the UK haulage industry and in particular employment numbers within the Transport and Storage Sector then, more granularly, the UK LGV driver workforce.

SECTION 3: What is the Future for the UK Haulage Sector after COVID-19?

We combine the key conclusions from the previous two sections to predict how the UK Haulage Sector and the LGV driver market will be affected by the COVID-19 Pandemic crisis, the subsequent recession and recovery.

We are in an extremely volatile period, with significant developments occurring daily and a prolific amount of new data regularly being disseminated. This means that this report will need continuous maintenance to keep it current. We nevertheless hope that it will provide a useful basis for understanding our current circumstances, how these are likely to evolve and help hauliers decide what to do now to maximise their chances of survival to eventually come out with increased competitive advantage.

Section 3:
WHAT IS THE FUTURE FOR THE UK HAULAGE SECTOR AFTER COVID-19?

The COVID-19 Pandemic has been developing for nearly half a year and its effect on the UK economy should not really have been a surprise, nevertheless we have been shocked by the extreme nature of the changes it has forced upon us and the massive challenges we now face to return to some degree of normality. Unfortunately we humans are myopic; we are very good at downplaying the seriousness of potential threats to ourselves and also other people's suffering until it is staring us in the face, at which time it is often too late to take the most appropriate preventative action and we are forced into remedial measures.

We are right in the middle of it now, with the government taking extreme measures in an attempt to diminish the longer-term human and economic impact of this microbial attack on our population. The lock-down has been traumatic to say the least, the closest living memory being the rationing after the Second World War. The effect on our economy is disastrous, with the entire recreational and high street retail sectors decimated, manufacturing and construction activity stalled for all but critical sectors, leaving healthcare, social care, emergency services, grocery distribution and home delivery as the primary functioning sectors.

The Haulage Sector has now been recognised as a critical service, promoting logistics workers and delivery drivers to the esteemed status of "Key Worker". Finally, some recognition of the importance of the service the Haulage Sector provides, which before was grudgingly accepted as a "necessary evil" by the retailers and other haulage customers, who forced hauliers down to razor-thin margins, through to the general public who resented lorries clogging up "their roads".

So how is the lock-down affecting the UK Haulage Sector? Many people have approached me over the past few weeks and declared that we must be extremely busy; after all, the supermarket companies and grocery suppliers are having a field day, home delivery is in overdrive, surely there is more work than we can shake a stick at. This is partly true, but omits the other half of hauliers, whose customers are caterers, restaurants, events companies, businesses, manufacturers and construction companies. All these have shut down, hopefully only temporarily, with their workers furloughed or working from home. This has led to an extreme polarisation of the Haulage Sector, with one half standing down workers and drivers, and the other half screaming out for more workers. Agencies have played a critical role in transferring some of these redundant workers from idle sectors to busy sectors, but there are only so many extra workers these busy sectors can absorb.

The result is that, according to surveys conducted by the FTA and RHA, there are around a quarter of a million delivery vehicles parked up with no work, this being just under half of the UK's truck fleet. An ONS survey of UK businesses in March found that 55% of Transportation and Storage businesses were laying off (furloughing) staff in the short term and 37% were decreasing working hours, and that was only at the beginning of the lock-down. Our direct experience has been that haulage companies only started to wind down at the end of March, and it was in early April that many took drastic action. This means that we can expect the April numbers to be worse.

Clearly the government is going to unprecedented lengths to prevent these companies going into administration, which is enormously appreciated. The problem is that many hauliers, large and small, have been operating on tiny margins, have extended their debts to the limits and have poor cash reserves. Aside from the coronavirus Job Retention Scheme (furloughing), the government's approach is to make loans available to distressed companies, which presents a problem to haulage companies who have little capacity to take on extra debt. The process will take weeks, and even then, the banks are extremely reluctant to provide more credit because they consider these low profitability, highly indebted hauliers to be "toxic" customers. Meanwhile these hauliers still have vehicle lease payments, fuel, vehicle maintenance, property rates and utility bills to pay, mortgages to service, all eating away at what little cash they have remaining. We are yet to see the consequences, but, if the lock-down continues, don't be surprised if we start to see more haulage companies filing for administration, with the knock-on effect on their workers, fleet providers and creditors.

A further impact on those hauliers who are busy servicing the remaining active sectors, is the massive reduction in backhaul. When a lorry delivers a load, it is inefficient to return empty with no income being derived from the return journey. As the haulage industry has come under increasing pressure to reduce margins and increase efficiency, backhaul, the practice of planning a return load to pay for the return journey, is fundamental. The problem we now face is that much of the backhaul traffic was from sectors that have closed down, so hauliers are often having to run empty on their return journeys, causing them to run at a loss. We must hope that the supermarkets, despite the pressure on their profits caused by the crisis, will be prepared to negotiate temporarily increased haulage rates to account for the loss of backhaul income.

We have addressed the here and now, and our attention must turn to the future. What is in store for the Haulage Sector as we move out of lock-down and through the ensuing recession? What lessons did we learn from the 2008 Great Recession and do these apply to our current circumstances? What can hauliers and their suppliers do to maximise their chances of survival and perhaps even prosper through this extraordinary period?

In Section 1 we forecast a V-Shaped dip in UK GDP followed by a quick partial resurgence and then a slow return over several years to pre-crisis GDP levels. We acknowledged the high likelihood of a global recession through to the end of 2020, and that this would potentially have an impact greater than that of the 2008 Great Recession.

Let's go through this one step at a time, considering the implications for UK hauliers, their workers and temporary worker suppliers.

We have talked about the immediate drop in haulage activity caused by the lock-down and the possibility of multiple haulage businesses collapsing if it continues. We expect the government to end the lock-down at the earliest opportunity and to restart trade as quickly as safe and practicable.

Consequently, the Haulage Sector and its agency worker suppliers, need to be ready to respond to a rapid increase in demand for their services. There will be large stockpiles that have built up through the lock-down that need to be distributed and we therefore expect a substantial initial spike in activity along with an associated spike in demand for fleet and workers. This should then fall off to “business as usual”, which will be when we start to discover the real structural impact of the crisis.

It is worth noting that the release of the lock-down will very likely be staged, and, if we are to follow what other countries have done, it is likely that the government will start with production & manufacturing facilities and important services, then proceed through other sectors, such as construction and retail, concluding with the entertainment (catering, restaurants and events) sector. This will have a disproportionate effect on those hauliers focused on particular sectors, for example builder’s merchants who are waiting for housing construction to be reactivated, or catering suppliers who service the restaurant sector.

Agencies will be instrumental in diverting resources from those still dormant sectors to those that are experiencing a spike in demand as they clear backlogs. Hopefully the sequencing and timing will work to everyone’s advantage and exploit the surplus resources to maximum effect as we revert to normal operations. If, however, it is not properly thought through and managed carefully, we may end up with periodic and/or regional shortages of fleet and labour to meet demand.

There is also anecdotal evidence of an “exodus of foreign LGV drivers” to be with their families during the crisis, though we expect this has been overstated as it is not something we at Driver Require have experienced. It will be interesting to find out if it has really been the case; if so, we could see a potential shortfall in LGV drivers to cope with short-term peaks in demand.

- In Section 2 we observed that a -6.3% drop in GDP produced a drop in “Transport and Storage” employment of **2 times** the GDP % drop, and a fall in LGV driver employment of approximately **2½ times** the GDP % drop.
- The time for the Transport and Storage sector, including LGV drivers, to recover was around **1½ times** the time it took for the overall economy to recover.
- We have applied these assumptions to the Average Case scenario from Section 1 which assumed that GDP drops by -14% in Q2 then rises to a total 2020 GDP of -7%. Subsequently it rises at 0.5% per quarter, which equates to 2.0% per annum.

Using these assumptions we have modelled a possible scenario in the graph below:

This would lead to GDP returning to pre-crisis levels by mid-2024, i.e. it takes 4 years to recover. Remember that this is our “Average” case scenario and should be considered against the backdrop of much more drastic forecasts including the OBR’s “reference” scenario of a -35% drop in Q2 GDP and a -13% fall in 2020 annual GDP.

We have then taken the key findings from Section 2 (see above) and applied these to the GDP forecast to predict how Transport & Storage, and more granularly the LGV driver employment numbers will evolve as we come out of recession.

All in Employment:
We assume a -25% drop in total employment during the lock-down, recovering to about a -5% drop by the end of 2020, then rising slowly to regain its pre-crisis level by the end of 2023. Essentially 3 and half years to recover from the crisis. We believe this is consistent with the ONS UK survey of businesses in March, which indicated that 30% of businesses reported laying off staff or reducing working hours. We expect this measure to be significantly worse from April onwards, when businesses really appreciated the impact of the lock-down, and then we allowed for the fact that many businesses would furlough or lay off only a proportion of their staff.

Transport & Storage:
We assume a -35% drop in employment in the Transport and Storage sector during the lock-down. This also correlates with the ONS UK survey of businesses in March, which indicated that 55% of Transport and Storage businesses were laying off (furloughing) staff and 37% reducing working hours. We assume this rises quickly, as the government relaxes the lock-down restrictions, to a net drop of -15% by the end of 2020. Employment in this sector rises to 5% below pre-crisis levels at the end of 2021, It then recovers slowly over the following 5 years. This compares with a protracted (5+ years) drop of -14% during the 2008 Great Recession caused by an overall GDP fall of -6.3%; we therefore believe our assumption is conservative.

Specifically, looking at the current circumstances, we think it is consistent with a potentially significant drop in business volumes due to delayed manufacturing recovery, as well as numerous business closures and continued restrictions on trading in the recreational and catering sectors. Thereafter employment numbers are assumed to rise gradually, though held back by the global recession, to eventually achieve pre-crisis levels in mid-2026.

LGV Driver Employment:
We assume a -50% drop in LGV driver employment numbers based upon the claim that -49% of the UK fleet is standing idle during the lock-down. These then rebound to a -23% drop by the end of the year as haulage companies reactivate. As happened during the 2008 Great Recession, we expect recovery of LGV employment numbers to lag 3 to 6 months behind the overall Transport and Storage sector. LGV employment will continue to rise to around 10% below pre-crisis levels by mid-2021 as manufacturing and construction activity ramps up, then it levels off to rise gradually to achieve pre-crisis levels by the end of 2026.

Our conclusion is that we may be looking at a 10% drop in LGV driver employment, equating to around 30,000 driver positions, for several years following the crisis, as the global economy recovers. This is expected to partially offset the perceived current UK shortage of around 50,000 LGV drivers.

Note that the recovery period of 6 years from the start of the crisis for both LGV Driver and Transport & Storage employment numbers correlates with the observation that during the 2008 Great Recession it took 50% longer for this sector to recover than for GDP.

It is hard to be more optimistic about post-2020 growth rates for all the reasons explained in Section 1 of this document. To summarise, these are:

- Long term slow down of the global economy.
- High business debt levels slow investment plans or cause them to be cancelled.
- Government increases progressive taxation on individuals, while also increasing Corporation Tax in order to pay down its enormous debt burden, which in turn reduces consumer demand and business capability to invest and expand.
- Dislocated supply chains need repairing, slowing down recovery.
- Money that would have been invested in growth initiatives is instead diverted towards restructuring supply contracts to accommodate multiple-sourcing strategies in order to mitigate sole-supplier risk.
- UK productivity remains flat or maybe even deteriorates further.

Our key conclusion is that it is unlikely there will be a chronic shortage of LGV drivers once we are beyond the steep recovery “bounce” that follows the relaxation of lock-down. In fact, we expect there to be a surplus of LGV drivers in the UK that will naturally achieve equilibrium levels during 2021. Only once business activity returns to pre-COVID-19 levels can we expect LGV driver numbers to become a constraint and we can re-start our discussions about how to tackle the underlying driver shortage.

In April 2021, we will finally see the introduction of the IR35 reforms in the Private Sector, which will bring agency pay and charge rates into line with permanent employee costs. We still expect that this will increase agency rates to the hauliers by up to 20%, regardless of there no longer being a chronic shortage of LGV drivers. This is because the cost increase is essentially a tax by the government that increases the cost of the driver to the agency. Neither the agency nor the driver will benefit from this rate hike. For more information please refer to our IR35 White Paper, which can be found at:
www.driverrequire.co.uk/ir35
It is also worth countering any speculation that the government may further defer or even cancel the roll out of the IR35 reforms, by reinforcing that the government will be looking for every possible opportunity to recoup its massive COVID-19 financial stimulus and is therefore extremely unlikely to forego the extra tax income it would achieve from the IR35 reform roll-out to the Private Sector.

In the longer term we will be living in “a new world” with some potentially fundamental changes to our strategic priorities and the way we work and live. Here are a few thoughts along these lines.

Relevant to the Haulage Sector we hope that there will be continued recognition and appreciation of the essential services provided by delivery drivers and logistics workers, alongside healthcare, social care and supermarket workers, not forgetting of course our emergency services and armed forces. Perhaps the concept of Key Worker status will be formalised, and the government will be persuaded to protect and nurture these worker categories, regardless of the economic pressures it may be under.

As a nation we can expect to endeavour to build greater resilience to international health crises and consequent economic and political instability:

- JIT (Just in Time) will become JIC (Just in Case): strategic reserves will be built up and stored locally to protect against supply chain disruption caused by international crises.
- No more sole sourcing of key components, especially to foreign suppliers. We expect businesses to establish dual or multiple sourcing networks to make their supply chains more resilient.
- Related to the previous point, businesses will have to better understand each link in their entire supply chain, so that vulnerabilities can be detected and reinforced. This will help avoid the threat of "supply chain dislocation" in the event of another international crisis.

We can expect greater government intervention:

- More protection of businesses in key sectors from acquisition or falling into administration.
- "Nationalisation" of key "strategic" assets, which so far has extended to writing off NHS debts, temporary "nationalisation" of the railways (government has taken over the franchises), could the airlines be next... would road haulage ever be considered?
- It is a very grey area as to what exactly is Key or Strategic and there will be much contention as to which businesses and sectors fall within this definition.
- Austerity and recession will bring about higher and more progressive taxation. The government will continue to seek to maximise its tax revenues while at the same time trying to stimulate economic growth. Not so different from the past 10 years...

Furthermore, we expect more home working and maybe fewer cars on the roads, while increased online purchasing will lead to larger demand for home delivery services, both van multi-drop and LGV trunking. We have felt the positive impact of quieter roads and reduced carbon emissions. This, together with a Government keen to launch large infrastructure projects to revitalise the economy, may lead to an acceleration of the decarbonisation of the UK Road Haulage Sector. We could soon be looking at electrification of the inside lane of motorways and key arterial routes, powered by new gas fired power stations with super-efficient carbon capture systems.

So, what does this mean for temporary staffing agencies?

V

There will be spikes in demand as we come out of the V-Shaped phase and agency workers will be at a premium as different sectors accelerate at different rates. Agencies will perform a critical role in providing a flexible workforce to respond dynamically to varying demand for temporary staff as it evolves across the sectors.

U

As we move into the U-shaped recession, we expect temporary blue collar agency requirements to drop off significantly, except in those sectors that remain robust through the recession, such as supermarket deliveries, grocery supply chain operations, healthcare, pharmaceuticals, home delivery and other essential services. We expect to see businesses downsize their permanent workforce over time in the negatively impacted sectors until they reach steady-state employment levels. During this time agency requirements will be reduced, returning to normal activity levels once steady-state levels are achieved. This will result in a short to medium-term reduction in agency requirements and a recovery once the market stabilises at its new lower level and starts to grow again.

W

If we are unlucky enough to have a W-shaped recession it will essentially be an extended turbulent time for us all, with agency support being essential to moving resources between sectors as they are variously affected by the swings and turns of the economy. Flexibility and agility will be key.

In the medium term we expect the government to proceed with the implementation of the IR35 reforms in the Private Sector. The House of Lords recently announced its wish for the IR35 reforms to be reviewed, but it is our belief that this review will focus mainly on the white collar contractors rather than our professional blue collar workers, who clearly fall within IR35. The government has already stated that, despite the possible review, it is determined to proceed with the IR35 reforms in order to increase its tax income to help offset its massive debt burden. We can therefore expect this to raise agency costs to hauliers and encourage them to transfer agency workers who are covering "normal operations" back "in-house" to permanent positions.

We also expect stricter regulatory enforcement and compliance, which will force out disreputable players and level the playing field for agencies and umbrella payroll companies. This should lead to greater transparency of agency charge rates, leading to open-book commercial relationships, and a greater appreciation of the value added by agencies.

Further down the line we expect large manufacturing and assembly clients to de-risk their supply chains by increasing buffer stocks and establishing local 2nd source suppliers. The consequence will be less variability in their supply chains, a reduction in agency usage and outsourcing or consolidation of storage to third party sub-contractors.

While we envisage these large volume contracts diminishing, there should eventually be an increase in smaller contracts driven by the establishment of local supply arrangements. Ultimately agencies should move towards their true purpose, this being to a primary focus of covering their clients' variable requirements. It is also worth noting that, in these turbulent and uncertain times, most companies would be expected to hold off on hiring new permanent staff and instead engage more temporary workers until they are sure that their requirements are likely to persist for the longer term.

We can therefore expect temporary professional blue collar staffing agencies to continue providing a valuable service to the Haulage Sector in the longer term.

Conclusion:

We don't yet know where this will take us. Every week brings new data and understanding. There are so many diverging views and it is anyone's guess which is right.

We have put together a forecast based on everything we have gleaned from the current analyses, press articles and our own experience. We believe this forecast is not unreasonable, but we consider it to be just a starting point, from which we will gradually refine a better prediction of what is to come as more information becomes available. We will constantly strive to provide our latest interpretation of the potential impact on the Haulage Sector, the LGV driver market and more specifically how we as a temporary driver supplier can add value.

Right now, the most important thing for every business is to maintain gross income while conserving cash so as to remain as robust as possible in the face of the ups and downs you will encounter over the coming months and possibly years. Beware of being lured into trading with high risk clients who offer extended payment terms. Remember that while on paper you may believe you are making a profit, if your clients go under you will be saddled with a debt and a consequent cash flow shortfall of 5 to 10 times the profit you thought you had made. There are many decent companies that have gone into administration for this reason.

There will always be a need for haulage companies and temporary staffing agencies in the long term; the greater the uncertainty and variability in demand, the greater the need for a temporary workforce. For this reason, we want to live to fight another day. If that means hunkering down for the next three months and furloughing staff, then that is a wise option; we must remain agile and ready to spring into action as soon as the lock-down is relaxed.

Flexibility and agility will be paramount for hauliers and agencies alike to exploit opportunities as they arise.