



# A perfect storm in the logistics and distribution industry

How the global pandemic, Brexit, and other significant events have affected SMEs in the logistics and distribution industry.





## An introductory note from Dale Trenam

**A**lmost every industry has been challenged by recent global events, with the Covid-19 pandemic at the heart of many business struggles, resulting in a significant shift in the SME landscape.

The logistics and distribution industry has been uniquely affected by a perfect storm of complex and entirely unforeseen circumstances layered on top of the pandemic. As I write this, the challenging geopolitical situation is creating further pressure on the sector through soaring fuel costs. Whilst business boomed in home delivery - with home delivery up 49% on the previous year at the start of the pandemic - the infamous 2021 Suez Canal blockage compounded an already flailing supply chain.

It's estimated that US\$9.6 billion worth of trade between Europe, Asia and the Middle East was prevented, with at least 369 ships queuing to pass through the canal.

Whilst the Government announced new measures to support business investment - with schemes such as the super-deduction, announced in March 2021, allowing companies to cut their tax bill by up to 25p for every £1 they invest - the HGV driver shortage and crisis in late 2021 required SMEs in the logistics and distribution industry to take a more balanced approach to investment to protect working capital and help deliver efficient operations.

Immediately before the pandemic, Brexit had already caused significant disruption to companies trading within the EU, with the driver crisis coming to a head in August 2021.

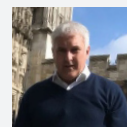
All this against a backdrop of rising inflation, increased cost of living and soaring energy prices, which will be an ongoing challenge for all SMEs well into 2022.

The immediate impact on the logistics and distribution industry - and in particular SME lending - was a shift in the volume and types of investment companies were able to make. Commercial vehicle production was brought almost to a complete halt at the start of the Covid-19 pandemic and, despite recovering within 12 months, production levels remain lower now than before the pandemic.

This shift in buying behaviour has continued throughout the pandemic - impacted by volatile supply and demand - and the industry's performance will be heavily dependent on UK road freight volumes and on the state of the overall economy. There are also long-term factors to consider, with the Government's commitment to cutting transport pollution to help the UK reach net zero carbon emissions by 2050 likely to impact the logistics and distribution industry more than any other.

As electric vehicles continue to proliferate the roads - with electric car sales in the UK jumping by 186% to 108,000 in 2020 and still rising - it is unclear if logistics firms, for example, can catch up and counter progressive bans for diesel HGVs from 2035.

This report explores trends in the logistics and distribution industry, with a focus on the impact of these issues and how they might influence SMEs in the short, medium and long-term.



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# How UK commercial vehicle production has reignited

Commercial vehicle production was brought almost to a complete halt at the start of the Covid-19 pandemic – but quickly recovered. Data from the Society of Motor Manufacturers and Traders (SMMT) showed output in May 2021 was up by more than 2% on pre-pandemic levels, despite continuing Covid restrictions. That also represented a 661% increase on May 2020, which coincided with the first coronavirus lockdown. In total during that period, just 820 new commercial vehicles were built in the UK.

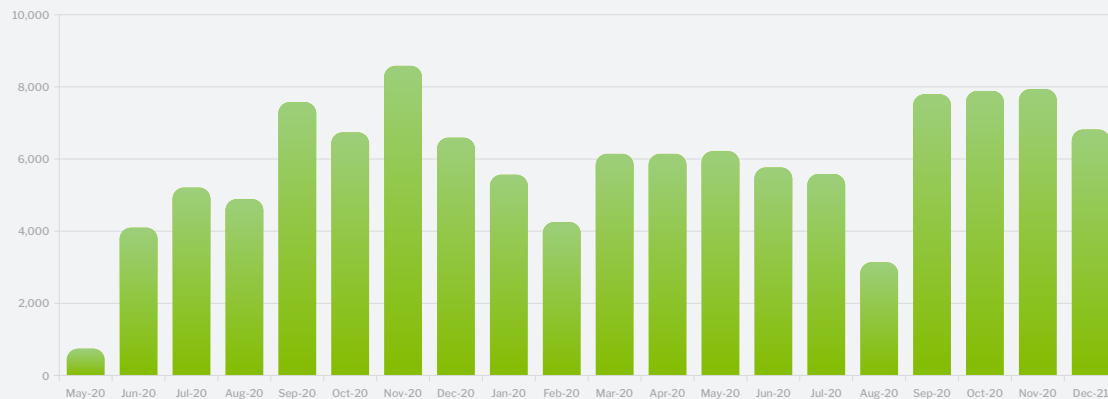
By mid-2021, new commercial vehicle production had grown slightly above pre-pandemic levels, compared with the five-year average output between 2015-2019. The SMMT believe this growth was largely down to the domestic market, which was up by 48.4% in the 12 months to May 2021. As a result, by May 2021, exports made up 49.5% of all commercial vehicles built in the UK – down from 56.3% in 2020 – partly due to new trading agreements and ongoing lockdown measures abroad.

However, the number of commercial vehicles produced in the UK fell by almost 8% in November as the global semiconductor computer chip shortage bit. According to SMMT figures, just under 8,000 commercial vehicles, including vans, were built in the UK in November. That 7.8% drop in output compared with the same month in 2020 made it the worst November performance for the sector since 2017.

Despite this, the UK new van market enjoyed its best November ever in 2021, with more than 31,000 new light commercial vehicles registered. With 31,320 new light commercial vehicles (LCVs) hitting the road, the market was up by almost 10% compared with November 2020, and 11.4% up on the pre-pandemic average for the month, in spite of the global chip shortage.

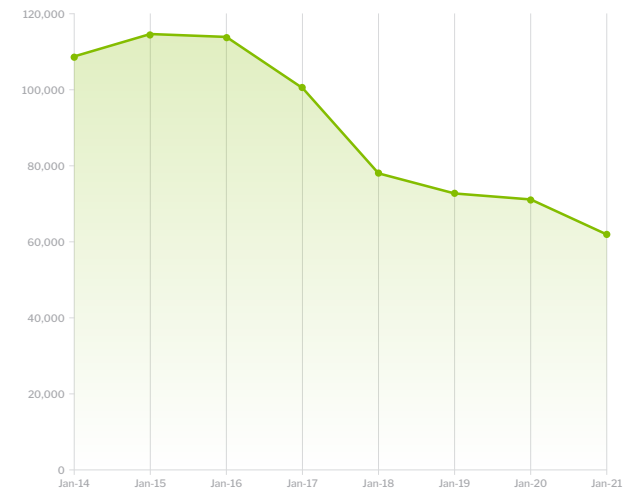
We expect new registrations to continue as the shift towards online retail continues to hold above pre-pandemic levels, with production following as quickly as possible within the constraints of the global chip shortage and ongoing supply chain issues.

Commercial vehicle production in the UK



Source: SMMT

Total UK car output



Source: SMMT

## Effects of the semiconductor computer chip shortage on vehicle production

British car industry output has been in decline for consecutive months since July 2021 as the months-long shortage of computer chips hampered the sector's recovery effort. The total number of cars built in UK factories fell by 27% year-on-year to 37,200 in August, according to the SMMT. That was down from 51,000 in the same month in 2020, when carmakers were racing to make up for time lost to lockdowns.

Demand in the UK and beyond recovered rapidly as economies opened up again, but carmakers around the world have struggled to raise their output because of the disruption caused by the pandemic – most notably the global shortage of computer chips used in everything from entertainment systems to controlling windscreen wipers and electric car batteries.

The SMMT predicted the chip crisis would wipe 100,000 off the UK's total car production for 2021. Production to August 2021 was only 14% higher than 2020, when factories were closed for months. Output was down by 32% compared with the same period in 2019.



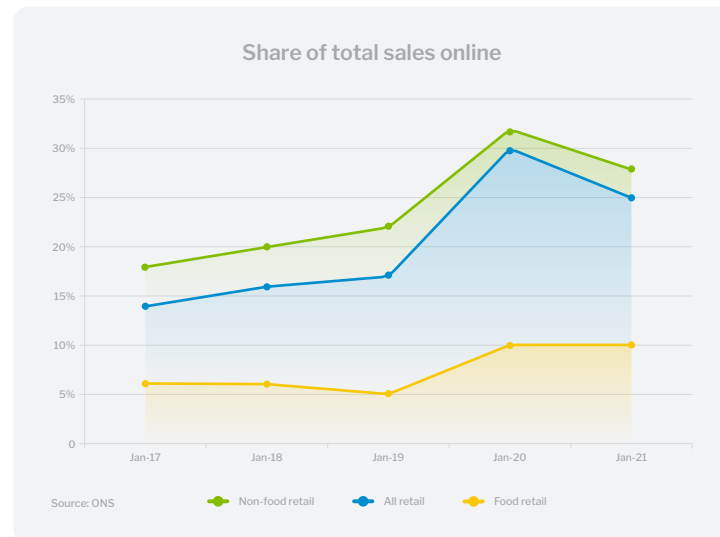
# Consumer buying behaviour has propelled home delivery sector

## The surge in online spend has buoyed logistics and warehousing

Since the onset of the Covid-19 pandemic in 2020, online shopping has seen a huge increase in a trend widely predicted to continue beyond the lifting of restrictions. During the pandemic's initial peak in April 2020, ONS figures show that internet sales formed over 30% of total retail sales, which was up 49% on the same month in 2019.

Online retail sales are still booming in the wake of the most recent lockdown, and this continues to put huge demand on delivery firms. Carriers such as Hermes have been overwhelmed with demand from retailers and growing numbers of independent courier businesses have been established as online retail continues to surge.

Despite a slight decline in the 12 months between December 2019-2020, online retail remains well above pre-pandemic levels. Retail volume and sales results to December 2021 released by the ONS demonstrate that the growth in online retail channels for both food and non-food products looks to be permanent.



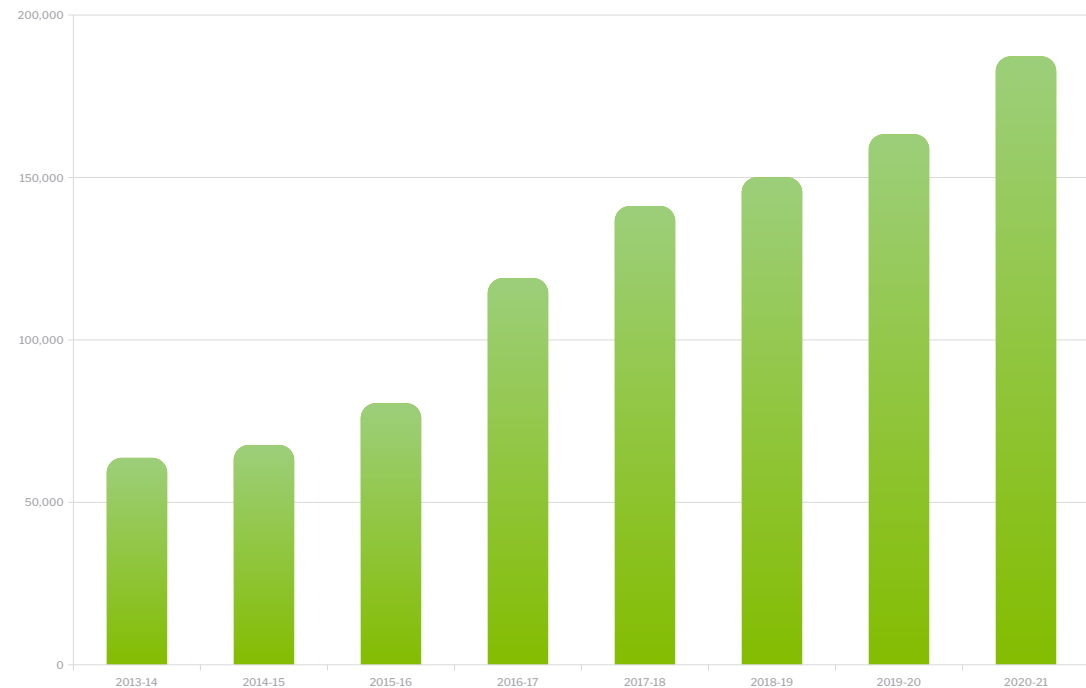
## Logistics boom

Driving demand for commercial vehicles and in response to higher demand for deliveries, Companies House data shows a significant increase in new transportation and storage businesses – making it one of the biggest growth industries in the past few years.

In 2013-14, there were 64,277 transportation and storage businesses. By 2020-21, that had almost tripled to 187,651, with year-on-year growth of 15%, up from 163,783 in 2019-20. This is likely a result of smaller logistics and distribution companies delivering for the likes of Amazon, at a time when distribution centres are also increasing in both volume and size.



Transportation and storage companies in the UK



Source: Companies House



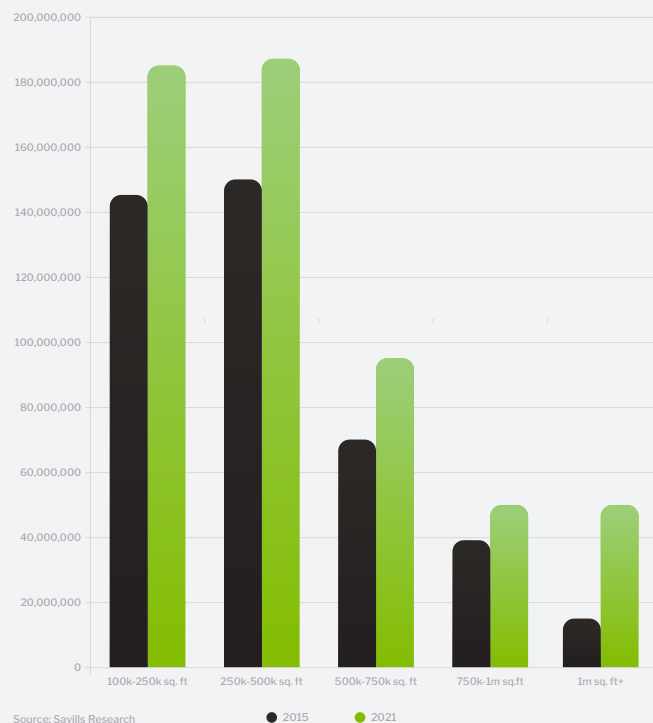
## A growing warehousing sector

Contributing to the logistics boom, a June 2021 report by Savills, commissioned by the UK Warehousing Association (UKWA), found online retailers have increased their warehouse footprint in the UK from 8 million to 60 million sq. ft in the past six years, a jump of 614%. This is largely be attributed to the structural shift away from the high street, which has been further accelerated by the Covid-19 pandemic.

Savills notes that in 2021 warehouse space has risen by as much as 32% to 566 million sq. ft in the past six years, however vacancy rates remain at just 5.4%, compared with 7.5% in 2015.

Research from Forrester states that by 2025 online retail will account for 35% of all retail, which means that at least 64m sq. ft of additional warehouse space will be needed for that sector alone. A 2020 paper from Savills also suggests that for every additional £1bn invested in manufacturing processes, an additional 175,000 sq. ft of warehouse space is needed in the wider supply chain.

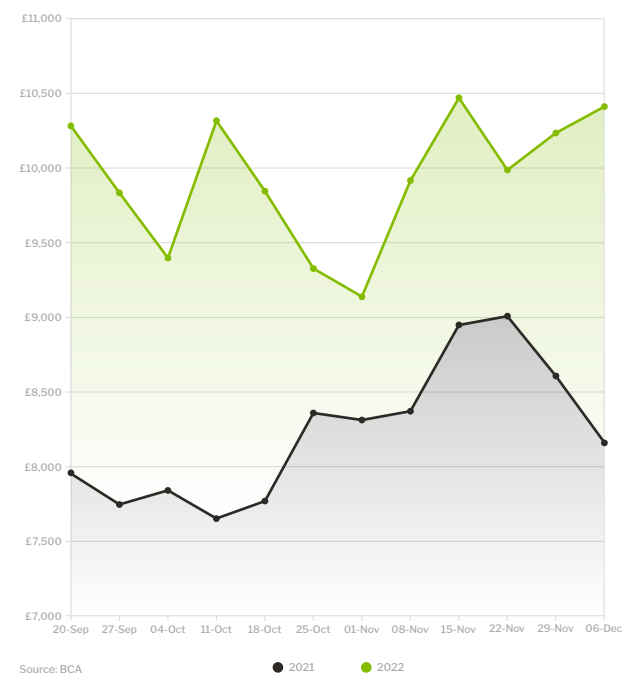
Warehouse size in the UK



Warehouse  
space has risen  
by as much as

32%

LCV value by average sale price, Sep - Dec 2021



## Residual value of LCVs

Sustained demand to service online shopping, home delivery and trade sectors saw values of LCVs achieve near record numbers at BCA in December 2021. According to data from used vehicle specialist BCA, the average value of £10,001 was the second highest average monthly value on record and a continuation of the strong values seen throughout 2021.

It maintained a seventh-month run where average LCV prices have hovered around the £10,000 mark. November 2021 values were up £1,394 (equivalent to a 16.4% increase) compared to the same month last year. This data in what has traditionally been one of the quieter trading months of the year suggests the boom in values in the used LCV sector following the onset of the pandemic, driven by with the huge shift towards more consumer-driven online activity, could remain in the medium to long-term.

# Road freight activity on the rise

## The levels of road freight on UK roads increased after the first lockdown, but growth is hampered by a driver shortage

The latest annual Government statistics for road freight transported by Great Britain and UK registered HGVs in the UK from July 2020 to June 2021 shows the amount of goods lifted increased by 7% from 1.30 to 1.39 billion tonnes, and the amount of goods moved increased by 8% from 140 to 152 billion tonne kilometres.




This growth is to be expected as the UK had just been released from its first national lockdown. However, levels remained 2% lower than the 5-year average of 1.42 billion tonnes from July 2014 to June 2019.

Conversely, international road freight activity in the same period decreased by 9% from 6.8 million to 6.1 million tonnes, and the amount of goods moved decreased by 11% from 4.1 billion to 3.7 billion tonne kilometres. This activity, as well as imports and exports, were also significantly down by up to 35% compared to the 5-year average of from July 2014 to June 2019.

These figures were largely due to the impact of Covid-19 restrictions – however, Brexit had already caused severe disruption to international freight, with the end of the EU exit transition period coinciding with the early stages of the pandemic and the effects felt throughout consecutive national lockdowns.





### Domestic road freight activity in the 12-month period to June 2021

	 1.39 billion tonnes of goods lifted	 152 billion tonne kilometres of goods moved	 17.8 billion vehicle kilometres vehicle distance
Compared to the 12-month period ending June 2020	<b>+7%</b>	<b>+8%</b>	<b>+5%</b>
Compared to the 5-year average beginning July 2014 until June 2019	<b>+2%</b>	<b>+3%</b>	<b>-5%</b>

Source: ONS

### International road freight activity in the 12-month period to June 2021

		Compared to the 12-month period ending June 2020	Compared to the 5-year average beginning July 2014 until June 2019
	6.1 million tonnes of goods lifted	<b>+7%</b>	<b>-26%</b>
	3.2 million tonnes of goods imported	<b>+8%</b>	<b>-26%</b>
	2.9 million tonnes of goods exports	<b>+5%</b>	<b>-27%</b>
	3.7 billion tonne kilometres of goods moved	<b>-11%</b>	<b>-33%</b>
	1.9 billion tonne kilometres of goods imported	<b>-9%</b>	<b>-30%</b>
	1.8 billion tonne kilometres of goods exports	<b>-14%</b>	<b>-35%</b>

Source: ONS

## HGV driver shortage

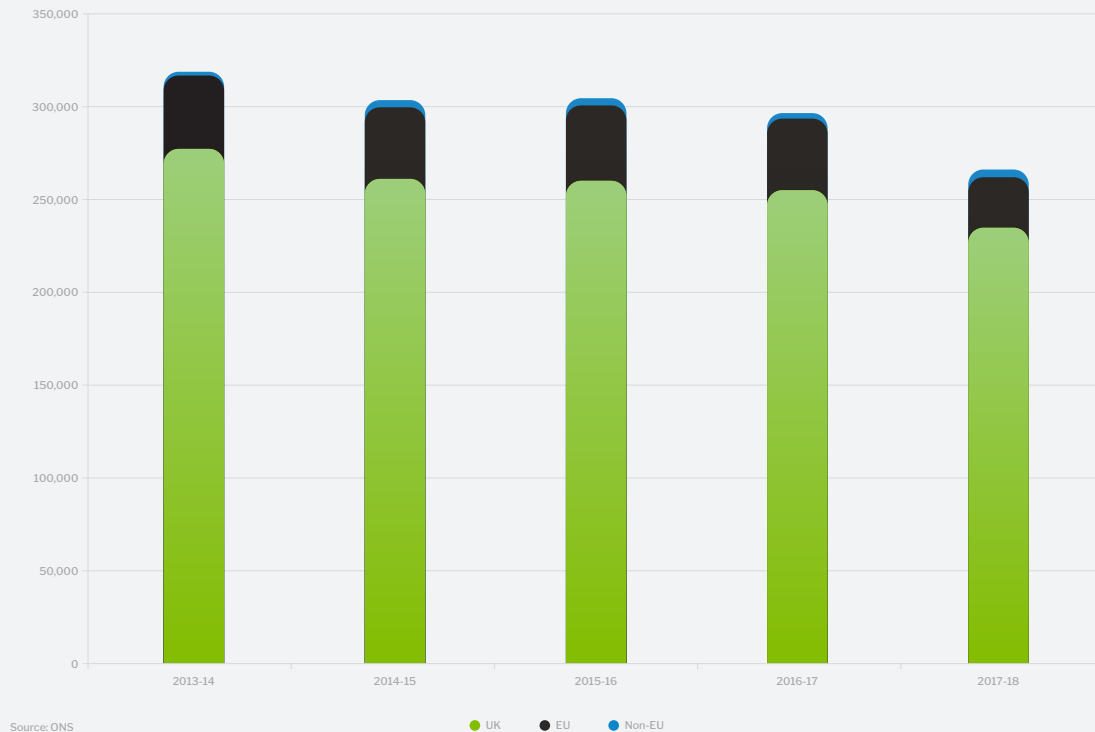
A shortage of hauliers and associated issues with logistics has led to some businesses reporting difficulties importing and exporting goods and some consumers reporting not being able to find certain items in shops. There has been a general decline in the number of HGV drivers in the UK for the past four years. Most of that decline has been in the previous two years, particularly during the coronavirus pandemic.

According to ONS data, an estimated 268,000 people were employed as HGV drivers between July 2020 and June 2021. This is 39,000 fewer than the year ending June 2019 and 53,000 fewer than the peak for HGV driver employment, during the year ending June 2017 (321,000).

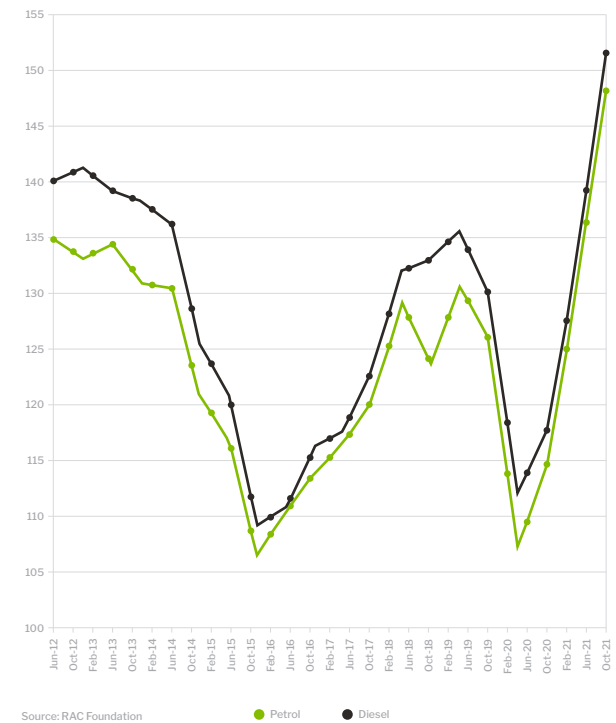
There has been a fall in the number of UK nationals employed as HGV drivers since the year ending June 2017. The number of EU nationals employed as HGV drivers increased between 2017 and 2020, but then decreased during the coronavirus pandemic. The number of HGV drivers has generally declined since July 2016 to June 2017. The largest decline over the four years was among those aged 46 to 55 years.

There were 52,000 vacancies for posts in transport and storage in the three months ending September 2021, which is the highest since records began in 2001. HGV drivers make up around 10% of the transport and storage industry, which also includes rail and sea transport as well as road transport occupations such as taxi drivers and bus drivers.

Number of HGV drivers in employment by nationality



Pump prices over time, pence per litre



## The impact of rising fuel prices

At 147.64p per litre for petrol and 150.85p per litre for diesel, fuel prices in the UK reached their highest levels in a decade at the end of November 2021 and remain historically high. The cost of fuel has hit fresh highs in more recent weeks as a result of the sanctions issued against Russia and challenging geopolitical conditions.

This is not only impacting logistics companies but has a significant knock-on impact to the cost of living for everyone. Increased costs to cargo freight leads to product inflation, product shortages, and slower economic growth. There is growing pressure on the logistics and distribution industry to operate more efficiently, to counter rising costs and ongoing shortages, but also to ensure a long-term future as greener practices become mandated.



# The move to net zero

## The logistics and distribution sector faces a challenge to meet net zero targets

Government policy will introduce progressive bans for diesel HGVs from 2035-2040 but banks have commitments through the Science Based Targets initiative (SBTi) and other initiatives to cut the content of carbon emitters within their portfolios by 50% by 2030.

The SBTi defines and promotes best practices in emissions reductions and net-zero targets in line with climate science.

As such, lenders may find it more challenging to fund such assets. It's also likely that supermarkets and other businesses that have also signed up to the SBTi will be applying pressure on suppliers who continue to use diesel fuelled HGVs.

The sale of all diesel lorries will be banned from 2040 as part of the major Government plan to cut carbon emissions from the transport sector. The sale of smaller diesel heavy goods vehicles (HGVs) will be banned from 2035, with ones weighing more than 26 tonnes prohibited five years later. In November last year, the Prime Minister brought forward the ban on the sale of new petrol and diesel cars and vans from 2040 to 2030. The ban will apply to new hybrid cars and vans from 2035.

As a result, SMEs in the logistics and distribution industry are required to deliver significant, costly innovation in a short space of time. Engine manufacturer Cummins has begun testing a hydrogen-fuelled internal combustion engine as an alternative to fossil fuels to decarbonise vehicles and construction machinery.

The real quandary surrounds the Government's likely ignorance of how firms acquire HGVs. If finance appetite dries up for HGVs because of the SBTi or other drivers, the Government timeline on bans becomes irrelevant. We believe many lenders will reshape their portfolios by being more selective about assets and their emissions from 2027 at the latest, to hit 50% reduction by 2030.

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*Lenders will reshape their portfolios and  
reduce their emissions from 2027 to hit*

**50% by 2030**

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# What's next?

## We highlight some of the trends that will define the logistics and distribution sector going forward.

### The green agenda

The increasing demand for more eco-friendly travel and green initiatives within the logistics and distribution industry will continue to have a significant impact. A huge proportion of HGVs on UK roads are running on empty as they return to depots following deliveries, resulting in wasted fuel, money, and time. More and more haulage companies and couriers are beginning to network with each other to collaborate and find back loads to reduce this empty travel.

Green couriers are beginning to emerge, operating fleets of battery-powered and ultra-low emission vehicles. Larger companies are also following suit, including the likes of Amazon, which has unveiled an all-electric fleet of delivery vehicles. The company plans to have over 20,000 of these vehicles operating by 2022 and it is highly likely that other couriers will follow suit.

### Covid recovery

During national lockdowns and Covid-19 restrictions, travel within the UK was halted for much of the past two years, with coach firms serving the leisure industry and other commercial vehicle operators hugely impacted. However, due to the lifting of restrictions and efficient social distancing measures now in place within schools and wherever else necessary, demand for coaches for school travel has increased sharply, with passengers able to travel safely and within Covid-19 guidelines.

This increase in commercial vehicle demand will continue across the hospitality and leisure industry, further increasing the demand for production and registration of new commercial vehicles. The challenge is for the logistics and distribution industry to meet this demand, despite ongoing shortages and rising costs.

### Road network improvements

Covid-19 aside, the Department for Transport is making large scale investments in transport infrastructure, which includes the UK road network. A major project is the A14 road upgrade, which provides a vital link between the Midlands and East Anglia and will be of huge significance to hauliers.

### Semiconductor computer chip shortage

Demand is clearly robust, but market volatility is likely to remain a feature as supply chain shortages throttle the logistics and distribution industry's ability to fulfil orders. Manufacturers are working hard to try and overcome these shortages. Whilst the outlook remains challenging, customers can be reassured of the industry commitment to the commercial vehicle sector, given its importance to the operation of society and business growth.



# Speak to Paragon

Whether you're looking to Hire Purchase, Lease or Operating Lease a commercial vehicle, keeping control of your rental payment, or if you need to fund a fleet of HGVs, vans, trailers, buses, coaches, or recovery vehicles, we'll help you get the wheels moving.

From hire fleet to operator funding, our specialist team have the experience and expertise to support you with your commercial vehicle investment and help find the right finance solution for you.

As a specialist commercial vehicle finance provider, our experienced team can offer bespoke funding solutions. For used and new HGV dealers looking for a complimentary alternative leasing option for your customers, we can help. So, whatever your requirements, we will help you find a finance deal that works for you and your business.

## We provide a variety of financing options tailored specifically to the commercial vehicle industry, including:

- HGV and truck finance
- Bus and coach finance
- Trailer finance
- Leasing solutions for B2B van and HGV rental companies
- Waste and recycling vehicle finance
- Haulage and road recovery vehicle finance

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