



COVID-19's Impact on the Transportation Industry in Europe



Q&A: COVID-19's Impact on the Transportation Industry in Europe

The COVID-19 pandemic may be waning in some parts of the world, but its economic impact continues to linger across the European transportation sector. In this Q&A, Brattle's International Arbitration Practice Leader **Richard Caldwell** poses some questions about the ongoing economic issues raised by COVID-19 in the transportation sector to Infrastructure Practice Leader **Francesco Lo Passo**.

WHAT ARE SOME OF THE IMPACTS OF THE GLOBAL PANDEMIC ON THOSE OPERATING IN THE TRANSPORTATION SPACE IN EUROPE?

COVID-19 has put a good deal of strain on many sectors, including transportation. In this space, passenger volumes have decreased and remain uncertain; contracts are up in the air; and people may be dissatisfied with the compensation and settlements provided. We are seeing firms renegotiate concession contracts, attempt to rebalance clauses, and invoke *force majeure* clauses – just to name a few issues

central to related disputes. We have actively addressed the economic impacts of COVID-19 recently, and have routinely dealt with the impact of contractual issues in the past, both in our regulatory and arbitration work. There is certainly an increase in activity in the marketplace and within the firm.

HOW ARE YOU SEEING TRANSPORTATION CLIENTS ATTEMPT TO RECOVER AND QUANTIFY LOST REVENUE, AND WHAT ARE THE EFFECTS OF THESE EFFORTS?

Publicly and privately held transportation companies in Europe, such as airlines, bus companies, rail companies, and others, are contending with major losses and advocating for support. For example, Air France, Lufthansa, and Alitalia are receiving government subsidies. When calculating the feasibility and rates of these subsidies, we have to look at the proper timeframes of lost revenues, the extent of the lockdowns in various places, and even the increase in costs due to new safety measures. We also need to account for differences between transportation companies that deal with passengers versus those that deal in the shipment of goods.

In addition, some European governments are renegotiating concession contracts in good faith, while other governments appear to be more opportunistic: attempting to resist the provision of sufficient monetary support or adjusted contract terms. It is not yet clear how passenger demand will evolve over the long run. It is also not clear if altered passenger expectations have to result in significantly altered pricing outcomes for either party. Sometimes parties can achieve an equitable solution by increasing the term of a concession for a limited number of years to compensate for lost demand and value during the pandemic. The economic upside of this option is that it is relatively cheaper for taxpayers and consumers in the near term. The downside is that it might delay or obstruct competition.

WHAT ABOUT TRANSPORTATION COMPANIES THAT HAVE A LOT OF DEBT AND ARE HIGHLY LEVERAGED? DOES THEIR FINANCIAL LEVERAGE RAISE PARTICULAR ISSUES?

High levels of financial leverage add urgency and a further layer of complexity to the contractual situation. In some cases, our transportation clients have been able to negotiate waivers on their debt, giving time and space to address the uncertainty about passenger demand and the contractual situation. In other cases, we have seen interesting and consequential moves by major investors seeking to take advantage of the crisis.

For example, we have seen hedge funds take significant positions in the outstanding senior debt of some transportation clients at temporarily distressed prices and then use the crisis and their rights as creditors to seek substantial debt restructurings, with the end goal of giving senior creditors more control over the company. One strategy is to buy up tranches of the senior secured debt and then attempt to wipe out subordinate and unsecured creditors.

Such strategies are contentious and highly important for the potential payoffs of different debt tranches, given the prevailing uncertainty about the lingering impact of COVID on passenger demand. They are likely to prompt disputes over the terms of proposed restructurings themselves and potentially further litigation after the dust settles and particular investors find that they miss out on any post-COVID recovery.

THE LEGAL ISSUES AT PLAY IN THIS SECTOR ARE COMPLEX, BUT WHAT TYPES OF ECONOMIC ISSUES ARE CENTRAL TO THE RESULTING DAMAGES CLAIMS?

When calculating lost revenues and cash flows, our teams look carefully at demand and pricing, operating expenses, possible debt, and financial interests. In more formal terms, we conduct coherent counter-factual analyses based on detailed and accurate financial modeling to help our clients obtain full and fair compensation. This is true for governments and infrastructure companies in the regulatory world and in the context of computing financial impact and damages in arbitration.

Since these types of economic analyses are routinely subject to close scrutiny and critique from interested parties, it is critical for every expert to

hold their work to stringent standards related to accuracy, transparency, and intellectual coherence.

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