COVID-19 Marine: Cruise industry impact from Coronavirus

The cruise industry has been significantly affected by the current Coronavirus (COVID-19) outbreak. Here we discuss the impact to the cruise industry so far and the impact it may have in the future.

The cruise industry is the fastest growing sector of the travel industry, with an increase in demand of 20.5% in the past five years. Around 26.7 million people took a cruise in 2017, whereas around 28.5 million passengers chose to go on a cruise in 2018.

The recent and on-going global outbreak of the Coronavirus (COVID-19) has created a high degree of disquiet amongst the public as to the maintenance of health and safety on board cruise ships. Fears within the industry are that the impact of COVID-19 will affect sales for a long-time, particularly in the Asian market, which has become a very important market for cruise companies in recent years.

Whilst other incidents have created negative publicity for the cruise industry, such as the outbreak of Norovirus ("the cruise ship virus"), the sinking of the "COSTA CONCORDIA" in 2012 and the stranding of passengers and crew on the "CARNIVAL TRIUMPH" for nearly a week, the cruise industry has rebounded and in recent years has consistently operated at 100% capacity. COVID-19 appears to be creating a longer-term negative impact: keeping the "DIAMOND PRINCESS" quarantined at berth in Yokohama for two weeks was constantly in the headlines,
followed by the news outlets reporting of the "MS WESTERDAM" with 2,000 passengers onboard, as it was prevented from docking by various countries over Coronavirus fears. News that the "MSC MERAVIGLIA", was turned away from Jamaica, the Cayman Islands and Mexico after a crew member tested positive for the flu and cruise ships "AZAMARA QUEST" and "SUN PRINCESS" were greeted by demonstrators in the French overseas territory of Reunion who were worried about the transmission risk of COVID-19, even though neither vessel reported any coronavirus cases onboard, has only added to the disquiet. Add to this that the United Arab Emirates has suspended all cruise operations at the country's ports, as part of preventative measures to stop the spread of coronavirus and the "GRAND PRINCESS" was forced to remain in international waters for five days as at least 19 crew members and 2 passengers have tested positive for COVID-19, the cruise market looks as if the negative impact is only set to worsen and will continue for quite some time. The "GRAND PRINCESS" is due to dock in California on Monday 9 March and passengers will disembark, most of whom will be quarantined.

At the time of writing, the Asian cruise market has been abruptly suspended. Norwegian Cruise Lines has announced that it has cancelled Asian voyages, across three brands, until the end of September; other cruises have been cancelled until as late as mid-October. The cruise ships which were designated for these specific cruises have been "re-routed" with changed schedules (for example not calling at or departing from certain ports such as Hong Kong or Singapore). Whilst changed schedules may be better than an outright cancellation of the cruises, changing a cruise ship's itinerary is complicated and is largely dependent upon port and berth availability. In addition, it is not straightforward, as few ports have the infrastructure to accommodate the big cruise ships. In some cases, it may not be an option as passengers from the Far East and Europe may resist changing their holiday plans. The impact on the small cruise players may be even more severe; some may be forced to exit the market.

All of these factors are already having and will continue to have a significant financial impact on the income projections of the big cruise operators. The three big players in the industry, Royal Caribbean, Carnival and Norwegian Cruise Lines have all issued share warnings, although none of them can predict how much and for how long, given the many variables. Royal Caribbean has provided an update on their health protocols which includes, amongst others, denial to board and a full refund for guests who have travelled from, to or through or have come in contact with anyone from mainland China, Hong Kong, Macau, Iran, South Korea, and Italy in the 15 days prior to boarding. A similar announcement was made by Carnival on 3 March with the company stating that they "continue to work closely with the relevant health and port authorities at our destinations. Certain restrictions are in place for guests and crew who have travelled to affected areas in the past 14 days". Carnival warned in mid-February that while it was too early to assess the full impact, a suspension of all Asia operations until the end of April would shave $0.55-to-$0.65 from its 2020 earnings per share.

The unpredicted increase in capacity of cruise ships due to the disruption or suspension of the Asian market is expected to force operators to offer lower prices in order to increase demand. In their most recent announcement, Norwegian Cruise Lines have stated that "At this time, we have modified, cancelled or redeployed a number of sailings and none of our vessels are calling to ports in mainland China. In addition, we do not have any vessels deployed in East Asia through the end of the third quarter. We also have the flexibility to alter our itineraries as needed to avoid areas of concern". This impact would be much more serious if it affects the Mediterranean and, given the current lockdown in Italy, it would not be unsurprising if the Mediterranean market also suffers severe disruption or even suspension. This could have even more of an impact than the disruption of the Asian cruise market, as for 2020, 10% of cruise ships worldwide were to be deployed in Asia, compared to 32% in the Caribbean and 28% in Europe.

Cruise lines are expected to be paying out substantial sums to passengers in refunds, compensation and cancellation fees, subject to the relevant ticket terms and conditions. Cruise lines will also have to bear the cost of docking at ports where ships are quarantined and the cost for maintaining and operating ships, with passengers on board, that are being turned away from ports and being forced to remain in international waters.
Based on the average cabin price for next year, cancelling a full-capacity 12-day cruise on Norwegian Cruise Line from Hong Kong would cost the company around £2.3m in refunds⁷. Commenting on the ongoing Coronavirus outbreak and the group's financial performance, Royal Caribbean Cruises reported on 13 February 2020 that "There are still too many variables and uncertainties to make a reasonable forecast for 2020"⁸. At the time of writing, some cruise companies have suspended their usual penalties for cancellations: Royal Caribbean have announced that if a passenger is booked or books a cruise which is due to set sail at any time between 6 March 2020 and 31 July 2020 the cruise can be cancelled at least 48 hours in advance. Passengers will not receive a refund, but a "Future Cruise Credit" which can be used towards any cruise that sets sail until 31 December 2021.

From a newbuild perspective, even though ship building projects in China and the Republic of Korea are suffering delays as yards in China struggle to fully resume work and there are delays to supply chains due to the virus outbreak, the impact on newbuild cruise ships on order may not be so severe, as such yards are mainly based in Europe. Nonetheless, delays within the supply chain, with many suppliers based in Asia, might be inevitable. Builders may find it difficult to pass this delay on to the owner and whether this can be done will depend on the drafting of each build contact. Under English law, the builder would have a duty to mitigate any delay and will have to use reasonable endeavours to make good any such delay.

As the virus spreads, the effects on the cruise industry will become more quantifiable, although it is unlikely to be a positive outlook for 2020. In the long-term – and perhaps even the short-term - this may affect repayments under financing arrangements and create general cash flow problems for the cruise companies. Cruise operators may find themselves in a position whereby they are unable to service loan repayments: failing to make a financing repayment when due may lead to a default under their financing structure which would typically result in an acceleration of the payment of any amounts due. Whilst lenders may show a degree of tolerance in respect of existing financings, for any new financings this will be more difficult in terms of interest margin and percentage. Cruise companies may opt to enter into discussions with their financiers which might lead to restructuring of their financing arrangements. We may also see cruise operators considering laying-up their cruise ships if demand decreases over a prolonged period of time. Typically, the financier’s consent would be required for this, or it could result in a breach of covenant under the financing documents. Financiers will be concerned because of the negative effect this has on cash flow and therefore the ability of the borrower to meet the payments required under the financing arrangements.

If the cruise industry follows the aviation industry, it could find itself in a deep crisis which will be hard to recover from and which could cause smaller and medium sized companies (if not even the larger companies) to collapse.

As this is an evolving situation with daily reports of cruise ships being turned away at various ports and being held in international waters, we will monitor the situation and issue an update on the impact of COVID-19 on the cruise industry when more is known.

Written by Marie-Anne Moussalli & Ioanna Tsekoura

¹ Data provided by Cruise Lines International Association (CLIA) 2018
