COFACE ECONOMIC PUBLICATIONS

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Global Transport: What does the future hold beyond COVID-19?

The COVID-19 pandemic has triggered a mobility crisis, mainly because of physical distancing requirements and the necessity to avoid confined spaces, to limit the virus' propagation. This has had a disastrous impact on the global transport sector[1], with air passenger transport being the most affected segment. According to IATA (International Air Transport Association), air traffic decreased by 94% year-on-year (YoY) in April 2020, and is not expected to return to its pre-COVID level before several years. Moreover, other segments of the transport sector (maritime, rail) are also experiencing a strong deterioration in activity at the global level, even though some markets (such as rail freight between China and Europe) are benefiting from the situation. The crisis is also affecting planemakers and their suppliers, whose financial health heavily relies on aircraft activity.

COVID-19's impact on global transport is all the more important as economic activity was already decelerating before the crisis. Additionally, the sector already had to deal with several issues and challenges, like the Boeing 737 MAX crisis for air transport.

Overall, Coface does not expect the sector to recover to fourth quarter (Q4) 2019 level before 2022 and will be strongly impacted in 2020. In Coface's central scenario, the turnover of listed companies of the global transport sector will be 32% lower in Q4 2020 than in Q4 2019. By contrast, in a "risk scenario", in which a second wave of the pandemic materializes in Q3 2020, the turnover would be 57% lower in Q4 2020.

1 In Coface's sector assessment methodology, the transport sector is divided into several segments: air, maritime, road and rail transport, which all take into account both individual and freight transport. In this study, we are focusing on air and rail transport, as well as maritime transport.

Erwan Madelénat,
Sector Economist
and data-scientist,
Paris, France

1 COVID-19 CRISIS: A CATALYST OF GLOBAL TRANSPORT VULNERABILITIES

Activity in the sector was decelerating before the COVID-19 pandemic

Economic activity in the transport sector was already slowing down before the COVID-19 crisis, mainly because of the global economic slowdown. The YoY growth rate of the world trade monitor[2] was negative in Q4 2019, for the first time since 2009. Consequently, global airfreight (measured in freight ton kilometers, FTKs) decreased by 3.3% in 2019, the worst figure since 2009. The container throughput index, a measure of container volume carried by container ships, increased by 2.0% in 2019, the lowest reading since 2015. Air passenger demand was on the decline as well: Revenue Passenger Kilometers (RPKs) increased by 4.2% in 2019, and for the first time since the Global Financial Crisis, RPK growth was below its long-term trend of 5.5%, according to IATA.

Air passenger transport is very sensitive to economic conjuncture, particularly in Europe, where the market has to deal with strong overcapacity issues that dampen companies' margins. Furthermore, the growing importance of low-cost carriers, whose business is based upon small margins and large volumes, led to numerous bankruptcies in the air transport market in the past years. Emblematic examples of this are Flybe, a British low-cost carrier, which ceased operations on 4 March 2020, or WOW Air, which ceased activity on 28 March 2019 and was the second largest Icelandic airlines, carrying more than a third of passengers travelling to Iceland.

Maritime freight had also decelerated: the Container Throughput Index, a proxy for the volume of containers carried by sea each month[5] decreased by 2.2% YoY in December 2019, and increased by only 2.0% in 2019 after 4.3% in 2018.

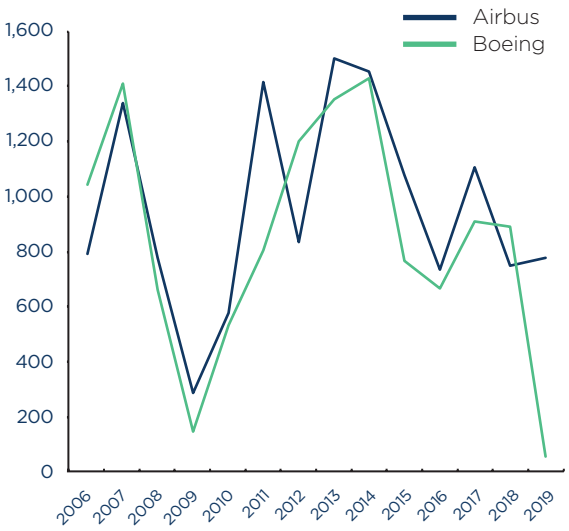
An emblematic pre-COVID shock in air transport: the Boeing 737 MAX case

Two deadly crashes of the Boeing 737 MAX – Lion Air Flight 610 (October 2018) and Ethiopian Airlines Flight 302 (March 2019) – due to technical issues led to the grounding of the plane in a large number of countries. This has had an important impact on air transport companies, as many of them (mainly North American carriers) were using the Boeing 737 Max. In February 2019, the three companies that owned the most 737 MAX were Southwest Airlines (US), American Airlines (US) and Air Canada with 34 planes

INSERT 1:
COVID-19 shock impact on supply chain - the example of the aerospace industry

In addition to the impact on airlines, the COVID-19 crisis has also negatively affected the entire aircraft industry, which already had to manage the Boeing 737 MAX crisis. Following the drop in activity, airlines had to delay airplane deliveries, leading to a decrease in plane manufacturing in Q1 2020. Therefore, leading actors of the sector like Airbus, as well as companies in the ecosystem/value chain, experienced financial difficulties. To face reduced demand from airlines, Airbus and Boeing cut production by a third and a half, respectively[3]. This decrease in production was echoed to aircraft component manufacturers like Rolls Royce (aero-engines producer), who announced the suppression of 9,000 jobs. There is a high proportion of small companies among aerospace suppliers: in France and Germany, nearly 60% of them generated less than EUR 50 million of revenue in 2018[4]. These small suppliers mostly produce for planemakers, so their financial health strongly depends on planemakers' demand, hence on airlines activity.

Chart 1:
Net orders of aircrafts



Source: Airbus, Boeing, Coface

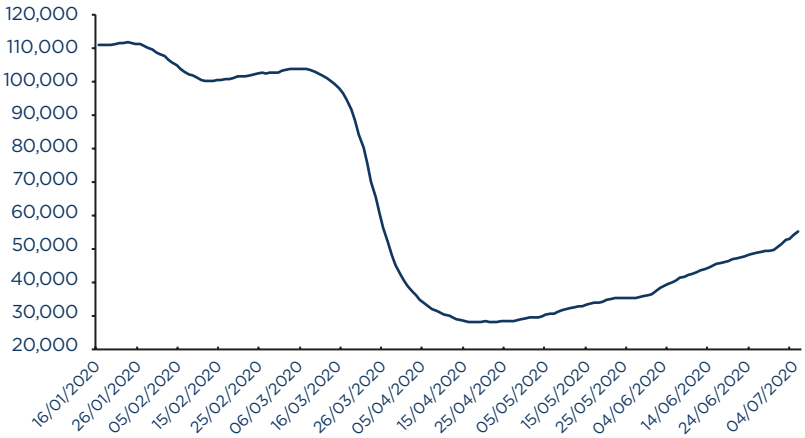
2 The world trade monitor is an indicator of world trade developped the Netherlands Bureau for Economic Policy Analysis
3 Hollinger, P., Keohane, D. (4 June 2020), Airbus veterans called up to rescue aviation supply chain, *Financial Times*, https://www.ft.com/content/3bec9f5b-086f-4757-8022-642b738dd0b7
4 *Ibid.*
5 In value, container shipping represents 52% of world sea trade. See World Shipping Council, http://www.worldshipping.org/

for Southwest and 24 for American Airlines and Air Canada. Excluding Norwegian Airlines, which owned 18 Boeing 737 MAX before the grounding, European carriers were less affected, as they have less of these planes than their American competitors. With part of their fleet removed by the grounding, carriers often have had to cancel flights, leading to lower turnover. For instance, Southwest Airlines has cancelled more than a hundred flights daily since the grounding and estimates that it caused a USD 828 million reduction in operating income[6].

However, airlines are not expected to support the cost of the 737 MAX grounding on their own, as many of them requested a compensation from Boeing. For example, Southwest Airlines received a USD 428 million compensation from the American planemaker.

These compensations reduce the weight of the grounding for airlines, but add more pressure on Boeing's finances, which saw a strong deterioration in 2019. Net orders[7] of Boeing's commercial airplanes decreased by 94% to 54 aircrafts in 2019 (see **Chart 1**).

Chart 2:
Number of commercial flights (7-days moving average)



Source: Flightradar 24, Coface
Latest point: 6 July 2020

Mobility Crisis: COVID-19 is disrupting all segments of the transport sector

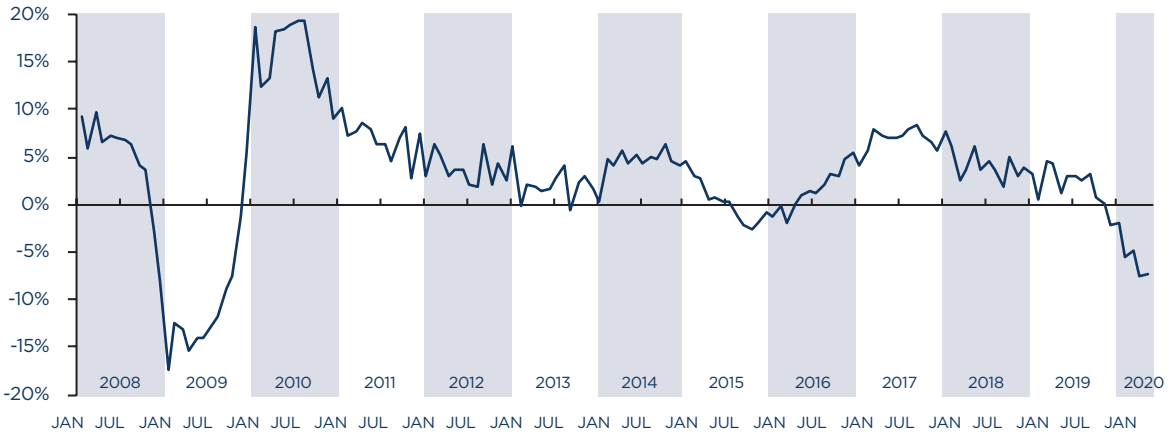
Since the beginning of the COVID-19 pandemic, the transport sector has been one of the sectors at the heart of the crisis[8]: countries have imposed travel restrictions, closed their borders and implemented lockdowns, leading to a strong decrease in freight activity and passenger demand.

Air and maritime segments have been severely hit

The air market is the segment most impacted by COVID-19. To face the drop in passenger demand caused by lockdowns and travel restrictions, airlines reduced capacity and workforce (American Airlines cut 5,100 jobs, Lufthansa said it has a surplus of 26,000 employees) or imposed unpaid vacations to their employees (for instance, Cathay Pacific forced its 27,000 employees to take three weeks of unpaid vacation between 1 March and 30 June).

The number of daily commercial flights decreased by 75% between 16 January and 12 April - the lowest point (see **Chart 2**). According to IATA (International Air Transport Association), air passenger capacity (measured in Available Seat Kilometers, ASK) decreased by 87% YoY in April 2020, while air traffic (measured in Revenue Passenger Kilometers, RPKs) fell by 94% YoY in April. The fall in air passenger activity led to a strong decrease in air cargo capacity, as most of air cargo is carried by passenger aircrafts in the "belly" of the plane. In this regard, according to IATA[9], air cargo volume declined by 27.7% YoY in April 2020 while capacity fell by 42%, leading to an all-time high load factor of 58% (+11.5 pp compared to April 2019) and higher freight rates.

Chart 3:
Container throughput index (YoY growth)



Source: RWI/ISL, Coface
Latest point: May 2020

6 2019 Annual report to shareholders (2020), Southwest Airlines.
7 Defined as the difference between gross orders and cancellations during a year.
8 Coface Country and Sector Risks Barometer (Q2 2020): From a massive shock to a differentiated recovery.
9 IATA (June 2020), Air cargo market analysis: April 2020, available at: https://www.iata.org/en/iata-repository/publications/economic-reports/Air-Freight-Monthly-Analysis-Apr-2020/