THE DAILY CHECK-IN WITH GOLDMAN SACHS

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Liz Bowyer: Hi, Greg.

Greg Lee: Hey, Liz. How are you?

Liz Bowyer: Good, thanks. So, Greg, cruise lines have been among the hardest hit industries during the pandemic. And from your seat in Investment Banking at Goldman Sachs, you've advised some of the cruise lines on how to navigate the financial challenges of the pandemic. Just give us a sense of the scale of the crisis that this industry has faced.

Greg Lee: I don't think that there has been a sector hit as hard as the global cruise line sector. The cruise line industry saw revenue fall just for the first nine months, which doesn't include the, you know, Q4, just for the first nine months of 2020 our clients were seeing revenue fall as much as 65-75% from the year before. And those numbers will be worse when you include Q4 where revenue was essentially zero for most of our clients. The CDC earlier in the year put out a "no sail" order for cruise line companies. That was extremely challenging. Needless to say, the industry has been working extremely hard, working with the CDC, working with health experts to come up with new protocols not just with the advent of vaccine distribution but also with testing protocols. And they have to navigate different jurisdictions. It's not just about what does the US think, but it's about the ports to which they sail.

Liz Bowyer: So just given the scale of the crisis, how have the cruise lines managed the financial challenges that are specific to this industry?

Greg Lee: The first thing is there's a tremendous cash burn. These are huge operations, a lot of expenditures, so they had to cut cash costs. They had to preserve capital. And the way they did that was thinking through whether or not they would put their vessels into a warm or a cold layup to preserve capital. They also had to cut costs by deferring capital expenditures, by going to customers and offering them, instead of cash refunds for canceled trips, vouchers. And they got a very, very successful take-up from their customer base showing the resiliency demand. So passengers were willing to take vouchers at some discount in order to cruise later on. So that was a very positive sign for the sector. But preserving cash, Liz, was really important given how much cash burn otherwise they would have had to sustain.

Liz Bowyer: And what about the capital markets, which had been so important to so many companies in weathering the pandemic?

Greg Lee: So in the beginning, in March and April, it was very scary. Cash burn was quite high. We needed to raise a lot of money very quickly. This was really before we saw the significant stimulative impact of global monetary policy pumping liquidity into the system. Carnival started with a large $6 billion rescue financing, multi tranche transaction. That means common equity, convertible bonds, and high-yield debt all done in the same time. It was a very important transaction, and if they hadn't successfully completed that financing the consequences could have been quite dire. It bought them very much needed time.

Now Carnival can access the senior unsecured markets. So the markets have healed quite dramatically because of monetary policy, I believe, but also because the markets realized that there is still significant demand for these businesses and that the vaccine and testing protocols will allow them to come back to market and service their passenger base in 2021.

Liz Bowyer: And how did they deal with their existing financial obligations?

Greg Lee: That's a good question. I mean, this was fundamentally an investment-grade industry coming into this crisis. So in addition to preserving cash, raising a lot of capital as quickly as possible and as efficiently as possible, they also had to deal with existing liability structures, which meant that they had to go to existing lenders, to banks, to creditors, to the export credit agencies who supported a lot of their ship-building initiatives and capital expenditures. They had to go to them and negotiate and restructure existing covenant obligations, which makes sense. This is an unprecedented situation where they had no top-line revenue coming in, no IBIDA coming in of meaningful size. And so a lot of the covenant structures that protect lenders are designed to protect lenders against things like significant drops in cash flow. So they had to go and negotiate, just a huge effort with many, many different counterparties and convince them that, hey, this is an industry that does have legs beyond this COVID pandemic, and we'll be able to sail again and generate revenue and ultimately take care of, you know, existing debt obligations.

Liz Bowyer: Well, with things hopefully looking up in 2021, what's your outlook for the cruise industry for the rest of this year?

Greg Lee: Well, I'm encouraged when we talk to our clients by how much pent-up demand there is. Our clients share with us that if they could wave a magic wand and have a safety protocol in place that CDC and the European equivalent agree with they could fill their vessels up, you know, next month. So there's a huge pent-up demand. Again, this is an industry that had 30 million passengers, 99% load factors. Compare that to, say, the hotel industry or the airline industry where, you know, you might have 70-75, 80% load factors in any given day. These are companies that really had restrictions on growth more by the availability of vessels than the amount of demand.

So we think that in 2021, as soon as they can get their agreement in place with the regulators and hopefully that's Q2 but it might be Q3 -- the summer is very important for the industry -- they can fill their vessels to maximum capacity.

Liz Bowyer: And what do you think cruising will look like post pandemic? What kind of changes do you think there might be?

Greg Lee: We do think that the safety protocols will be very different. They've hired a panel of experts who have worked with them on creating new ways to, for example, feed passengers. There's new protocols in place for rapid testing, both on board and pre board. And of course the vaccine distribution and requiring vaccine inoculations is going to be I think part of whatever solution they end up agreeing with the CDC.

So I think 2021 we'll see a resumption of sailing. I think it's more likely to be heavier in the second half of the year than the first half of the year. And I think you'll see a difference in some of the on-boarding protocols for testing, for vaccination, and I think we'll see a little difference as well in some of the on-board activities. For example, you know, restaurants and, say, buffet dining, for example,

Liz Bowyer: So given the encouraging signs for the cruise lines, how are you investors thinking about this industry?

Greg Lee: It's interesting. So even before the vaccine news, which was extremely positive in Q3, into Q4 as well, investors were taking the view that this is an industry that has such significant built-in institutionalized consumer demand. So not a cyclical sort of fees around consumer sentiment and behavior but really kind of a secular growth in fundamental consumer demand. So investors were playing that this was an industry that was hit really hard. It was doing extremely well for many years going into COVID. And that it would resume once there was a new safety protocol in place. I think the vaccine news accelerated that. So we're seeing investors not just hedge funds and fast money but long-term institutional capital coming in saying this is a smart way to play the recovery, and it's a smart way to play what is a pent-up demand on the consumer side for travel experience. We're seeing this in everything from the equity, common equity, as well as investors who play in both the high-yield and secured investment-grade debt markets.

Liz Bowyer: So finally, Greg, our economists in Goldman Sachs Research have a pretty bullish view for economic growth in 2021. How do you think the cruise lines fit into that story?

Greg Lee: So I think hopefully we're right, that there is a V-shaped recovery and that we're seeing pretty significant growth in GDP. I do think a lot of that is going to be consumer-driven demand, which, again, wasn't hit as hard during 2020. And I think the cruise line sector is a really great example of both the importance that consumer-driven consumption and demand for global GDP. And, two, the sort of secular trend line around the importance or prevalence or the relative importance of prioritization of experiences versus goods.

Liz Bowyer: Thanks, Greg.

Greg Lee: Thank you very much, Liz. Appreciate the time.