COVID-19 and the retail sector: The perspective of Estonia, Latvia and Lithuania

A comparative look at changes to the law and state aid in the Baltics since the COVID-19 pandemic

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Upon the arrival of the COVID-19 pandemic, in the Baltic states specific amendments were adopted to existing insolvency rules and specific packages of state aid measures were introduced.

Legal framework: overview

In **Estonia**, the main amendment to the Bankruptcy Act was a stay on the obligation of directors to file for bankruptcy for the duration of the pandemic as well as a stay on the running of recovery terms during the pandemic. These amendments were in force until mid-July.

In **Lithuania**, the Law on the Impact of Consequences Caused by a New Coronavirus (COVID-19) on the Application of the Law of the Republic of Lithuania on the Insolvency of Legal Entities (the "Law") was adopted. Similar to Estonia, the Law suspended the obligation of directors to apply to a court for the opening of insolvency proceedings during the quarantine period and also for three months after the end of the quarantine. The Law also restricted creditors' right to initiate insolvency proceedings against a debtor until the end of the quarantine (provided the debtor's financial difficulties were due to the pandemic).

A broader moratorium was adopted in **Latvia**, where creditors were prohibited from applying for insolvency proceedings against a debtor until 1 September 2020 irrespective of whether the financial difficulties arose due to the outbreak of the COVID-19 virus. However, it is interesting to note that in Latvia, companies' directors' duty to file for bankruptcy was not postponed. Latvian law also provided for extended terms in restructuring proceedings. In cases where the spread of COVID-19 prevented the implementation of a restructuring plan, the deadline for implementing legal protection proceedings could be further extended by another year.

Lithuania's legal environment did not go that far, establishing a rule that non-fulfilment of the plan did not automatically constitute a reason for termination of the restructuring process. However, this had little benefit, as Lithuanian companies are now forced to apply for adjustments to restructuring plans because implementation of the plans was not frozen during the quarantine. This means that even though restructuring was not terminated due to non-compliance with the plan, companies still had to comply with the plan which had been calculated as feasible before the pandemic.

In **Latvia**, on the contrary, the time allowed for implementation of legal protection proceedings was subject to extension by one year if consequences of the crisis caused by COVID-19 were what prevented the debtor from implementing such proceedings. Latvian law also established additional support regarding the term of restructuring proceedings: for legal protection proceedings (restructuring) declared up until 31 December 2020, the maximum length of the plan was set at four years (previously it was two years).

Impact of the COVID-19 crisis on retail trade

With the start of the pandemic, the retail sector in the Baltics was hit hard, as were many other sectors. The main reason was uncertainty on the part of consumers and the visitation restrictions imposed on large malls. Retail companies faced a series of difficulties: from reduced demand and financial difficulties to health safety at work and long-term supply challenges, to the challenge of moving trade to the Internet. Lithuanian statistics show that insufficient demand was crucial among the factors which restricted activities in the retail sector during the quarantine period.

Latvia's retail sector faced the steepest decline of any industry in the country. Due to the COVID-19 crisis, the decline in retail sales in Latvia in April this year was the biggest in the last ten years, with turnover at constant prices down by 9% year-on-year. Sales decreased in both food and non-food trade.

Lithuania saw similar numbers. In April retail sales fell by an annual 15%, though already in May and June year-on-year growth of 3.6% and 5.9% was recorded. It is evident that April was the most difficult month of lockdown for the retail sector, as after that restrictions were gradually lifted.

While Latvian retail sales in grocery stores rose sharply in March this year (up 7.1% from a year before) as people built up food reserves amid concerns that all grocery stores might close soon, those fears soon subsided and in April grocery stores' sales decreased by 3.5% year-on-year. But after declines in April and May, relatively strong growth was registered again in June. According to the Central Statistical Bureau of Latvia, trade volumes at constant prices increased by an annual 4.6% in June.

Statistics Estonia also suggests the situation does not look so bad, reporting that overall sales in the retail sector in that country in June were 671 million euros, which is 7% more than in June 2019. The office also notes that although the industrial commodities sector was down in April and May this year, it recovered in June, even seeing a 12% increase in sales versus the same month last year.

Increased online shopping was a key factor helping some parts of the retail sector recover after April's drop. In Estonia, for example, some companies selling essential commodities saw their online sales triple during the COVID-19 crisis. In Lithuania, Internet retail sales increased by 58% in the period.

Decreasing number of insolvency proceedings in Latvia and Lithuania

The statistics show a general decrease in bankruptcy cases. In **Latvia**, where in April-July 2019 there were 197 bankruptcy cases, in the same period of 2020 there were only 81, for a 59% decrease. Among the 81 cases, 13 companies were retail sector companies, though their total combined turnover was less than 3 million euros. So, from the perspective of insolvency, the Latvian retail sector was not significantly affected by the COVID-19 crisis.

Lithuanian statistics show that in the first quarter of 2020, the total number of bankruptcies fell by 25.6% compared to the same period of 2019. Such a decreasing trend, however, has been observed in Lithuania for several years. During the quarantine period, from 1 March to 1 July 2020, 205 companies in Lithuania went bankrupt, i.e. only about half the number in the same period of 2019. In the first quarter of 2020, most bankruptcy proceedings opened were for wholesale and retail businesses (23.7%). Also, the new Lithuanian Insolvency Law that took effect as of 1 January 2020 fundamentally changed the regulation of insolvency. Hence the decline in the number of bankruptcies in Lithuania could also be a result of the change in the legal environment. However, economists emphasise that while companies operating in the retail sector, i.e. 81%, are considered to be of average or low bankruptcy risk, up to 51% of them, or one of every two companies, are seen to be at risk of being particularly strongly impacted by the quarantine. This signals a possible increase in the number of bankruptcies in the retail sector.

Increasing number of bankruptcy cases expected

The state aid measures mentioned above were adopted with the aim of coping with disruptions to the economic activity of companies due to the COVID-19 crisis. It is too early to say, however, whether the state aid with respect to insolvency laws was indeed effective for managing the crisis.

As the retail sector involves a wide range of company activities, it is difficult at this stage to pinpoint the full impact of the COVID-19 crisis on the sector as a whole. Still, it can be said that there are signs the retail sector is coping with the crisis and making a good recovery. Much of course depends on the further development of the COVID-19 pandemic and the threat of a possible "second wave" this autumn. Since the amendments to the insolvency laws postponed filing for bankruptcy, it is widely noted that the effect of the amendments was temporary and the Baltics could see a wave of bankruptcy and reorganisation applications this autumn. This would surely affect the retail market also, especially those companies which have not been able to cope with the changes in consumer behaviour and the rise of online commerce. ■

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