

Transport & Tourism Sectors

Breathing Life into the Trans-Tasman Bubble

ANDY BOWLEYandy.bowley@forsythbarr.co.nz
+64 4 495 8246**SCOTT ANDERSON**scott.anderson@forsythbarr.co.nz
+64 4 914 2219

The New Zealand Government has announced the commencement of two-way quarantine-free travel across the Tasman from 19 April 2021. This marks a key recovery milestone for New Zealand's global connectivity and inbound tourism industry. We anticipate a strong demand response to the inflating of the bubble, particularly from the visiting friends and relatives (VFR) cohort. Pent up demand will also be a driver of the leisure segment, albeit with the New Zealand Government actively highlighting the risks for outbound travellers (which historically account for around half of Tasman travellers) with a strong "flyer beware" message, international connections beyond the Tasman restricted (representing ~20% of pre COVID-19 passengers), and the likelihood of higher-risk groups less willing to travel, we expect overall demand to be at a modestly lower level than pre COVID-19. Nonetheless, the commencement of quarantine-free travel will provide a major financial boost to the beleaguered transport and tourism sectors and will result in near-term positive earnings risk to each of Air New Zealand (AIR), Auckland Airport (AIA) and Tourism Holdings (THL).

Sentiment trumps fundamentals for the time being

We're NEUTRAL on each of AIA, AIR and THL, recognising that sentiment and uncertainty (each country reserves the right to close their borders at short notice in the event of further outbreaks) will remain key drivers for the foreseeable future. Reopening sentiment remains a short-term positive catalyst but we expect reopening reality will dampen the prospect of prolonged enthusiasm, as investor focus ultimately reverts back to fundamentals.

Auckland Airport (AIA; NEUTRAL) – green zone to re-energise concession income

The Tasman represented ~41% of total international pax (including transit) at AIA in FY19, but excluding international connections pure-Tasman pax represented ~30%. The high incremental margin of aeronautical and commercial activities at airports means a meaningful uplift in pax will drive a significant improvement in profitability. We estimate that AIA is currently losing ~NZ\$4m per month at the NPAT line. We estimate this could swing by up to ~+NZ\$20m per month into profit generation under a full pre COVID-19 demand Tasman scenario, driven by retail and aeronautical income. Assuming the bubble evolves into a broader aviation recovery there should no longer be any concerns over AIA's next covenant test at 30 June 2022.

Air New Zealand (AIR; NEUTRAL) – welcome boost ahead of capital raise

Early capacity indications suggest AIR will initially apply 70%-110% of pre COVID-19 Tasman capacity subject to route. We estimate that AIR's cash burn could reduce by up to ~NZ\$30m per month excluding any ongoing benefit from working capital (forward bookings) and potentially halve P&L losses, assuming pre COVID-19 Tasman demand and yields. We expect cash burn will continue but down from 2H21 guidance of NZ\$45m-NZ\$55m per month to perhaps NZ\$15m-NZ\$25m per month. However, the rate of cash burn would deteriorate in 1H22 given the end of government's PAYE deferral scheme from October 2021. P&L losses would continue but the rate of net asset value (NAV) dilution would halve (to ~1.5c per month). The opening of the bubble is a timely boost ahead of AIR's upcoming capital raise, which the company has said will be undertaken before 30 June 2021.

Tourism Holdings (THL; NEUTRAL) – losses to be partly mitigated

The seasonal nature and historic reliance on long haul demand for RV rentals means THL has less to gain from a trans-Tasman bubble, when compared with AIA and AIR. Nonetheless, we expect a demand boost, which will partially offset material 2H21 losses and further NAV dilution. We'd expect THL to increase its Tasman demand profile compared to pre COVID-19 given available capacity, more attractive pricing and its dynamic, commercially minded, sales approach.

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