

# Equity Strategy

## Risks Rise with Return of Community Transmission

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The return of community transmission of COVID-19 in New Zealand will likely dent business and consumer confidence across New Zealand. Four new cases in a single family in South Auckland from an unknown source has motivated the government to quickly lift restrictions. Auckland (~33% of New Zealand's population) moves to Alert Level 3 at midday today, while the rest of the country moves to Alert Level 2. The current duration of the heightened Alert Levels is until midnight on Friday 14 August. This buys the government time to pursue the source of the current known infections and trace all potential contacts. In light of the number of potential other infections in the community, we suspect New Zealand will remain at higher Alert Levels for longer, but recognise the increased level of uncertainty that now surrounds the near term outlook. Companies most exposed include SKYCITY (SKC), Fletcher Building (FBU), Steel & Tube (STU), retailers and Abano Healthcare (ABA).

### Government remains firm on eradication path

The government's decision to impose a three day lock-down of Auckland is primarily to buy time for the results to come in from the case tracing, in our opinion. This highlights some of the economic risks with New Zealand's chosen path of zero tolerance to COVID-19 cases. We caution against assuming that this will be over on Friday, and estimate that the time lag between infection and achieved test result could have been up to two weeks, implying that in a worst case scenario we could have up to 50-100 positive cases already. If no clear link to imported cases is established over the next three days we expect at least a further two week's of Alert Level 3 in Auckland, maybe more.

### Companies most impacted

We expect most New Zealand businesses will be impacted by the Alert Level changes to varying degrees. Given the heightened uncertainty, business and consumer confidence will take a hit. Those NZX listed companies that will be hit the hardest include:

- **SKYCITY (SKC)** – its Auckland casino will be closed during Alert Level 3, and see material restriction for Hamilton/Queenstown under Alert Level 2.,
- Building sector companies (**Fletcher Building [FBU]** and **Steel & Tube [STU]**) – additional social distancing measures at Alert Level 2 will likely have a material productivity impact.
- Retailers – those with NZ only footprints will be more impacted (**Warehouse Group [WHS]** and **Briscoe Group [BGP]**).
- **Abano Healthcare (ABA)** – dental practises will be largely closed (emergency procedures only) under Alert Level 3.

Stocks that may not have a direct impact but are driven to some extent by GDP include Freightways (FRE), Z Energy (ZEL), Kiwi Property (KPG), and the Aged Care players. While travel and tourism related companies will be severely impacted by heightened restrictions their businesses are already suffering significantly from border closures, therefore, the impact of the Alert Level changes is less than those listed above, in our opinion.

**Figure 1. Companies impacted most by Alert Level changes in New Zealand**

Alert Level 1 to 2		Alert Level 1 to 3		Alert Level 1 to 4	
SKYCITY	4	Abano Healthcare Group	10	Abano Healthcare Group	10
Fletcher Building	4	Michael Hill Intl	9	Michael Hill Intl	9
Metro Performance Glass	4	SKYCITY	8	SKYCITY	8
Steel & Tube Holdings	4	Kathmandu Holdings	8	Kathmandu Holdings	8
NZ King Salmon	3	The Warehouse Group	8	The Warehouse Group	8
		Briscoe Group	8	Briscoe Group	8

Source: Forsyth Barr analysis

## What is going on?

With four confirmed cases and no direct link to imported cases we have now what can be defined as community transmission. We believe the initial three day lock-down is primarily a reflection of turn-around time for tracing and testing; when the results from the tests of close contacts and casual contacts are in we believe the government will opt for one of three solutions;

1. If they find the direct link, and that link is sufficiently short and clear, we may go back to Alert Level 2 for Auckland and Level 1 in the rest of NZ. We believe the criteria here needs to be only a few positive cases and that none of those cases could be categorised as super spreaders (having extensive close contacts).
2. If they find several cases, which we view as quite possible, we believe we will potentially see a two week/one cycle shut-down of Auckland, potentially for the whole country depending on what cases are found. Case growth per day of COVID-19 is estimated to be c. 30–40% per day. Onset of symptoms can be anything from 5–14 days and many symptoms are very mild. Four people showing symptoms, theoretically, indicates that they would have been infected about five days earlier. To that we have to add the time it has taken for them to decide to get a test, we understand that the father of the family had shown symptoms for five days, and then for the test results to come back and the time it has taken the government to communicate the results with the country: 14 days with unrestricted spread can be anything from 20–50x, suggesting at the upper extremities we could be up towards 50–100 cases already.
3. If no link is established we believe the outcome will be path dependant; (1) If no link is established and no positive cases are returned, assuming that no other positive cases are found in the community, we believe we could go back to Alert Level 1 on Friday. The assumption here would be that there will be a link to overseas travellers but for some reason this has not been possible to establish; (2) If no link is established but one or more positive cases come back from increased testing and/or several of the contacts return positive but still with no clear chain back to overseas travel, we believe the assumption would be general (but local) community transmission and we would expect Auckland, and potentially the country, to stay in Alert Level 3 for at least one two week cycle, but potentially two.

### The downside risk of low tolerance to COVID-19

All in all we believe the latest development highlights some of the risks with New Zealand's chosen path of extremely low tolerance towards COVID-19 cases, the risk is expressed in two ways.

First, and directly, as the director general of health has stated numerous times; sooner or later we would end up with a domestically transmitted case. The Alert Level 3 response to just one family having been infected is what can be best described as an (extremely) high cost strategy of fighting COVID-19, and is different from some of the low cost strategies applied in countries such as South Korea and Taiwan, focussed on case tracing, testing and quarantine rather than wholesale lockdowns. The assumption here is that they will succeed; i.e. that case tracing will be successful, but what if it is not? What if there continues to be a small trickle of cases as lockdown fatigue reduces compliance with the various restrictions. The risk here is that we will find ourselves in multiple successive and ever more restrictive lockdowns.

The Second and interlinked effect is that one of the main economic impacts from COVID-19 is sentiment and behavioural changes. Sweden has applied a low touch approach, similar to Alert Level 1, despite having one of the world's highest fatalities per capita and has seen a similar economic impact as its neighbours with severe lockdowns. People have changed their behaviour, started to worry about their future and reduced their spending. NZ is potentially susceptible to these behavioural changes. The government's strong and very successful attempt to eradicate community spread in NZ has likely resulted in NZ yet to normalise COVID-19 in society. NZ is one of very few countries in the world where, until yesterday, most people were unlikely to be worried about getting COVID-19. If/when that changes, we could see significant negative impacts on spending and economic activity.

With regards to capital markets we believe the COVID-19 lock-down of Auckland could chase some of the animal spirits out of the market. The very strong, relative and absolute, performance of the NZ market over the last few months are, we believe, in no small part due to the sense of relief and optimism driven by the eradication of community spread of COVID-19 and better than expected data post re-opening. This could present an opportunity for some investors as a good excuse to sell.

## Company exposures

Figure 2. Companies most exposed by Alert Level and Alert Level changes

	Company exposure (10 - massive/little revenue/loss making, 0 no impact or benefit). Excludes cyclical economic impact on each company.					Most exposed (numerical difference between each alert level)		
	Level 4	Level 3	Level 2	Level 1	No alert	Level 1 to 4	Level 1 to 3	Level 1 to 2
Abano Healthcare Group	10	10	2	0	0	10	10	2
Michael Hill Intl	10	9	2	0	0	10	9	2
SKYCITY	10	10	6	2	0	8	8	4
Kathmandu Holdings	10	8	2	0	0	10	8	2
The Warehouse Group	10	8	2	0	0	10	8	2
Briscoe Group	10	8	2	0	0	10	8	2
NZ King Salmon	5	5	3	0	0	5	5	3
Fletcher Building	10	4	4	0	0	10	4	4
Steel & Tube Holdings	10	4	4	0	0	10	4	4
Sky TV	6	6	4	2	0	4	4	2
Asset Plus	5	4	2	0	0	5	4	2
Kiwi Property Group	5	4	2	0	0	5	4	2
Stride Property	5	4	2	0	0	5	4	2
Sanford	4	4	2	0	0	4	4	2
Air New Zealand	10	10	7	6	0	4	4	1
Tourism Holdings	10	10	7	6	0	4	4	1
Z Energy	8	6	3	2	0	6	4	1
Freightways	7	4	1	0	0	7	4	1
Metlifecare	4	3	2	0	0	4	3	2
Summerset Group	4	3	2	0	0	4	3	2
Infratil	4	4	2	1	0	3	3	1
Mainfreight	6	3	1	0	0	6	3	1
Comvita	3	3	1	0	0	3	3	1
PGG Wrightson	3	3	1	0	0	3	3	1
Auckland Airport	9	9	8	7	0	2	2	1
Refining NZ	7	7	6	5	0	2	2	1
Restaurant Brands NZ	10	2	1	0	0	10	2	1
Argosy Property	3	2	1	0	0	3	2	1
Precinct Properties NZ	3	2	1	0	0	3	2	1
Arvida Group Limited	2	2	1	0	0	2	2	1
Augusta Capital	2	2	1	0	0	2	2	1
Delegat Group	2	2	1	0	0	2	2	1
Goodman Property Trust	2	2	1	0	0	2	2	1
Oceania Healthcare	2	2	1	0	0	2	2	1
Ryman Healthcare	2	2	1	0	0	2	2	1
Skellerup Holdings	2	2	1	0	0	2	2	1
Napier Port	5	2	0	0	0	5	2	0
Port of Tauranga	5	2	0	0	0	5	2	0
Vital Healthcare	2	2	0	0	0	2	2	0
Contact Energy	2	1	1	0	0	2	1	1
Genesis Energy	2	1	1	0	0	2	1	1
Mercury	2	1	1	0	0	2	1	1
Meridian Energy	2	1	1	0	0	2	1	1
Property For Industry	2	1	1	0	0	2	1	1
Trustpower	2	1	1	0	0	2	1	1
Fonterra	1	1	1	0	0	1	1	1
Scales	1	1	1	0	0	1	1	1
Spark NZ	2	2	1	1	0	1	1	0
Gentrack	2	1	0	0	0	2	1	0
Vector	2	1	0	0	0	2	1	0
EBOS Group	1	1	0	0	0	1	1	0
Synlait Milk	1	1	0	0	0	1	1	0
Investore	1	0	0	0	0	1	0	0
Tilt Renewables	1	0	0	0	0	1	0	0
Chorus	0	0	0	0	0	0	0	0
Pushpay	0	0	0	0	0	0	0	0
F&P Healthcare	0	0	0	0	0	0	0	0
NZX	0	0	0	0	0	0	0	0
Pacific Edge	0	0	0	0	0	0	0	0
The a2 Milk Company	0	0	0	0	0	0	0	0

Source: Forsyth Barr analysis

## Alert Levels reminder

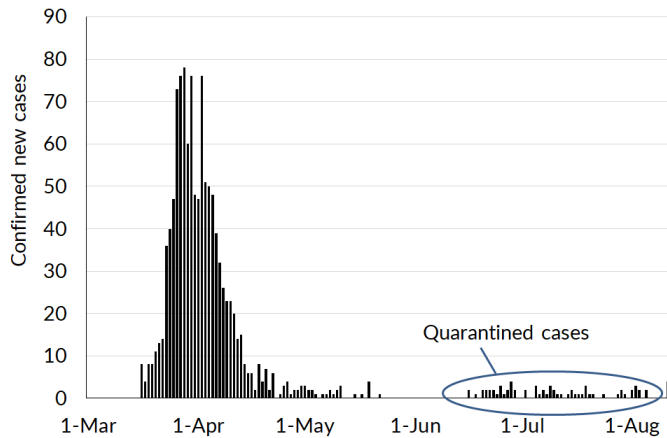
Figure 3. Alert Levels reminder

Alert Level	4 - Lockdown	3 - Restrict	2 - Reduce	1 - Prepare
	Likely the disease is not contained.	High risk the disease is not contained.	The disease is contained, but the risk of community transmission remains.	The disease is contained in New Zealand.
<b>Risk assessment</b>	<ul style="list-style-type: none"> <li>Community transmission is occurring.</li> <li>Widespread outbreaks and new clusters.</li> </ul>	<ul style="list-style-type: none"> <li>Community transmission might be happening.</li> <li>New clusters may emerge but can be controlled through testing and contact tracing.</li> </ul>	<ul style="list-style-type: none"> <li>Household transmission could be occurring.</li> <li>Single or isolated cluster outbreaks.</li> </ul>	<ul style="list-style-type: none"> <li>COVID-19 is uncontrolled overseas.</li> <li>Isolated household transmission could be occurring in New Zealand.</li> </ul>
<b>Range of measures</b>	<ul style="list-style-type: none"> <li>People instructed to stay at home (in their bubble) other than for essential personal movement.</li> <li>Safe recreational activity is allowed in local area.</li> <li>Travel is severely limited.</li> <li>All gatherings cancelled and all public venues closed.</li> <li>Businesses closed except for essential services (eg supermarkets, pharmacies, clinics, petrol stations) and lifeline utilities.</li> <li>Educational facilities closed.</li> <li>Rationing of supplies and requisitioning of facilities possible.</li> <li>Reprioritisation of healthcare services.</li> </ul>	<ul style="list-style-type: none"> <li>Bubbles must stay within their immediate household bubble, but can expand this to reconnect with close family/whānau, or bring in caregivers, or support isolated people. This extended bubble should remain exclusive.</li> <li>Schools (years 1 to 10) and Early Childhood Education centres can safely open, but will have limited capacity. Children should learn at home if possible.</li> <li>People must work from home unless that is not possible.</li> <li>Businesses can open premises, but cannot physically interact with customers.</li> <li>Low risk local recreation activities are allowed.</li> <li>Public venues are closed, eg libraries, museums, cinemas, foodcourts, gyms, pools, playgrounds, markets.</li> <li>Gatherings of up to 10 people are allowed but only for wedding services, funerals and tangihanga. Physical distancing and public health measures must be maintained.</li> <li>Healthcare services use virtual, non-contact consultations where possible.</li> <li>Inter-regional travel is highly limited, eg for essential workers, with limited exemptions for others.</li> <li>People at high risk of severe illness are encouraged to stay at home where possible, and take additional precautions when leaving home. They may choose to work.</li> </ul>	<ul style="list-style-type: none"> <li>Physical distancing of 1 metre outside home (including on public transport).</li> <li>Gatherings of up to 100 people indoors and 500 outdoors allowed while maintaining physical distancing and contact tracing requirements.</li> <li>Sport and recreation activities are allowed if conditions on gatherings are met, physical distancing is followed and travel is local.</li> <li>Public venues can open but must comply with conditions on gatherings, and undertake public health measures.</li> <li>Health services operate as normally as possible.</li> <li>Most businesses open, and business premises can be open for staff and customers with appropriate measures in place. Alternative ways of working encouraged, eg remote working, shift-based working, physical distancing, staggering meal breaks, flexible leave.</li> <li>Schools and Early Childhood Education centres open, with distance learning available for those unable to attend school eg self-isolating.</li> <li>People advised to avoid non-essential inter-regional travel.</li> <li>People at high risk of severe illness are encouraged to stay at home where possible, and take additional precautions when leaving home. They may choose to work.</li> </ul>	<ul style="list-style-type: none"> <li>Border entry measures to minimise risk of importing COVID-19 cases.</li> <li>Intensive testing for COVID-19.</li> <li>Rapid contact tracing of any positive case.</li> <li>Self-isolation and quarantine required.</li> <li>Schools and workplaces open, and must operate safely.</li> <li>Physical distancing encouraged.</li> <li>No restrictions on gatherings.</li> <li>Stay home if you're sick, report flu-like symptoms.</li> <li>Wash and dry your hands, cough into your elbow, don't touch your face.</li> <li>No restrictions on domestic transport, avoid public transport or travel if you're sick.</li> </ul>

Source: <https://covid19.govt.nz/alert-system/covid-19-alert-system/>, Forsyth Barr analysis

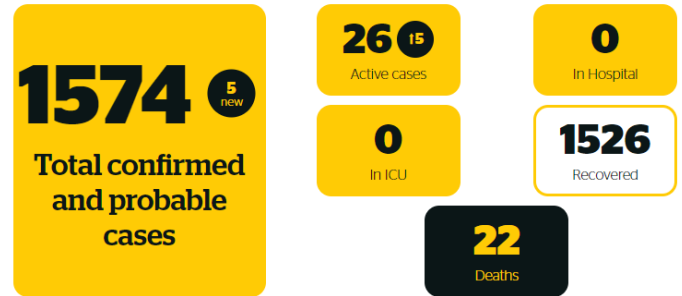
## COVID-19 history in New Zealand

Figure 4. New confirmed cases in New Zealand



Source: WHO, Ministry of Health, Forsyth Barr analysis

Figure 5. Current status of COVID-19 in NZ



Source: MoH, Forsyth Barr analysis

Figure 6. New Zealand's COVID-19 Alert Level experience

Alert Level	Snapshot	Entered	Duration (days)
Level 4 - Lockdown	Likely disease is not contained	26/03/2020	33
Level 3 - Restrict	High risk disease is not contained	28/04/2020	15
Level 2 - Reduce	Disease contained, but risk of community transmission remains	13/05/2020	26
Level 1 - Prepare	Disease is contained in NZ	08/06/2020	65
Level 3 - Restrict (Auckland)	High risk disease is not contained	12/08/2020	3?
Level 2 - Reduce (Rest of NZ)	Disease contained, but risk of community transmission remains	12/08/2020	3?

Source: Forsyth Barr analysis, COVID19.govt.nz

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