

Transport and Tourism Sectors

When Will Our Borders Reopen?

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"When it is safe to do so" has been the standard response to these types of questions by the New Zealand Government through COVID-19. We don't expect this approach to change materially regardless of the upcoming election. However, the nature of border restrictions could change as better track, trace and testing regimes are deployed. In the likely absence of a high efficacy vaccine, NZ's re-entry into the global travel market will be reliant on (1) its acceptance of a containment strategy, as opposed to elimination, and (2) superior technology based solutions for tracking, contact tracing and testing. NZ is not yet ready on many fronts, and it will take time for the government and the public to have confidence in the systems employed. The likelihood of NZ's borders reopening in the next six months is now very low, in our view. We're optimistic that it could be within the next 6–12 months, but recognise this will be reliant on a high efficacy vaccine, and/or superior transmission mitigation mechanisms. In the meantime, the risk to NZ's tourism industry is that as other destinations open up and we stay closed, the global flow of tourism may establish new routines and NZ could see damage to its share of wallet. This would be exacerbated if Australia opens its borders fully. Moreover, international business can only survive on zoom for so long, NZ may fall into the too hard basket if our border restrictions deviate too far from that of our trading partners.

The elimination fallacy

New Zealand closed its borders on 20 March 2020, and went into its first lockdown on 23 March 2020, when there were less than 350,000 known cases of COVID-19 globally. Today there are more than 7m known active cases. The US Food and Drug Administration has suggested that it would approve a COVID-19 vaccine that is shown to be safe and at least 50% effective.

To put this into context. The measles vaccine is readily available internationally, has been around for over 50 years, and has relatively high compliance and efficacy of 95%–99%. Yet in 2018 there were ~10m cases of measles globally, including some in New Zealand. The Case Fatality Rate (CFR) of measles is similar to that of COVID-19 (estimated to be 1%–2%). However, the CFR for measles is higher for younger people, in particular infants who can't be vaccinated. Compared to measles, a COVID-19 vaccine will have substantially lower efficacy, likely much lower uptake in young people, children in particular, will not have the same incentive as older to vaccinate, and for the first few years will be less readily available in all corners of the world.

New Zealand's strategy of elimination may have worked if the same strategy was adopted globally and the virus hadn't spread as widely as we now know it has. However, as a long term solution it is looking increasingly difficult to pull off.

Implications for companies

We make no changes to our earnings estimates in this report but acknowledge near term downside risk for companies with exposure to international travel including Auckland Airport (AIA), Air New Zealand (AIR), Tourism Holdings (THL), and Skycity (SKC).

- **AIR (UNDERPERFORM):** The timing of borders reopening has the most impact on AIR, given its material cash burn situation in the absence of commercial international passenger services. At Alert Level 1, with borders closed, the company's cash burn is NZ\$65m–NZ\$85m per month. The company will likely require an equity recapitalisation in order to de-leverage its balance sheet.
- **AIA (NEUTRAL):** While the impact of border closures is partly mitigated by its investment property business, we estimate AIA is NPAT loss-making in the absence of commercial international passenger services.
- **THL (NEUTRAL):** A strong vehicle sales market is significantly boosting THL's New Zealand cashflows and reducing its exposure to border closures, as its fleet is wound down. Vehicle rental demand from higher yielding international visitors will ultimately be required to generate a return on capital recovery.
- **SKC (OUTPERFORM):** SKC has a modest exposure to border re-opening (international customers ~15% of earnings pre COVID-19), particularly China/Asia and Australia. We understand demand is there from its premium customers, and expect a quick return (and potentially even initial surge) when permitted.

Four questions that help us understand when borders reopen

Nobody we ask can really answer the question "*when will borders reopen?*". We accept it's a difficult question with an infinite number of scenarios possible. Just a few months ago our base case expectations was that New Zealand would reopen its borders on a restricted basis, by October 2020. We are less certain now than we were then. The re-emergence of COVID-19 community transmission in New Zealand and the Victorian wave in Australia has created more uncertainty.

Instead of trying to directly answer this question we try and answer a number of other related questions, which help frame our thoughts:

(1) Does the government's COVID-19 strategy shift to containment from elimination? Probably not over the next few months. Politically the Labour Party has done very well out of COVID-19. Its polling remains high and appears increasingly likely that it will govern after the next election.

(2) Do other countries eliminate COVID-19 without a vaccine? New Zealand shouldn't be counting on this. History shows elimination requires economically damaging government restrictions and/or a compliant population.

(3) What is the status of New Zealand's technology to track, trace and test? Improving but still have a lot of work to do. If the virus is here to stay it is vital that New Zealand improves its track, trace and test regime to a point where the speed of identifying and managing outbreaks is far quicker than the recent Auckland outbreak. But more importantly, improve enough for the government to be confident enough to not introduce various broad lockdown restrictions following minor outbreaks/single family cases.

(4) When will a vaccine solution be readily available? Possibly by mid-2021 but this is unlikely to be a silver bullet given efficacy and uptake issues.

Having answered these questions we now believe that **the New Zealand border is unlikely to open, even on a restricted basis, for at least six months**. Given the increased seasonal risk from COVID-19 transmission in the winter months, a cautious government may not wish to experiment with the border, until clear of winter 2021. Therefore, a plausible scenario is that our borders remain heavily restricted for a further 12 months, even with the prospect of successful vaccine trials and mass inoculations during 2021.

(1) Does the government's COVID-19 strategy shift to containment from elimination?

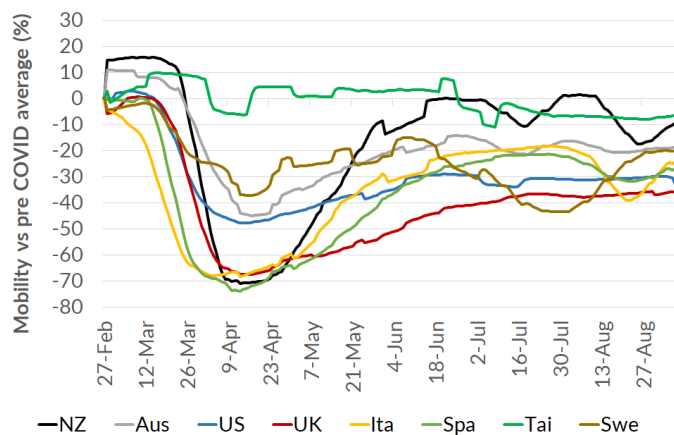
Eventually we think it is likely that it has to, the question is when?

Prime Minister Jacinda Ardern has made it clear that New Zealand's risk tolerance is very low to accepting COVID-19 in the community. There is a delicate balance the government needs to maintain between health, business and political outcomes. As New Zealand heads towards a general election on 17 October, it is the last of these three, which will take greater prominence.

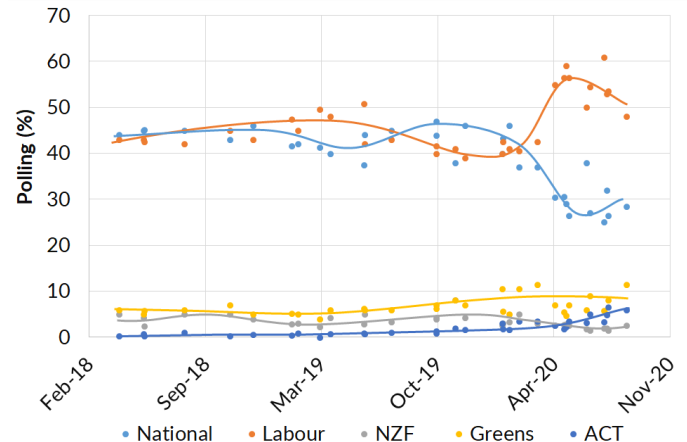
Our hypothesis is that majority of New Zealanders would rather the border remain closed for health and personal freedom reasons. The country wants to go back to Alert Level 1. The government knows this and therefore, while parts of the business community is suffering (the international travel and tourism sector in particular), the rest of the economy can operate at broadly usual capacity. When there's an election at stake why bother changing a winning formula. The Prime Minister has built considerable political capital through COVID-19 as Figure 2 illustrates.

Strategy status quo for now

Consequently, we don't foresee a strategy shift to containment pre or immediately post-election, regardless of its outcome, as New Zealanders en masse enjoy their relative freedom (and feel they've earned it). However, we believe it can't continue indefinitely. We expect personal freedom 'wants and desires' will change over time and New Zealand's relative isolation from a more connected world beyond its borders will play on the public psyche. This will ultimately have an impact on the political outcomes, and likely in time result in a readjustment of the government's strategy to managing COVID-19 and recovering from it.

Figure 1. Google 'workplace' mobility data for selected countries


Source: Google Mobility, Forsyth Barr analysis

Figure 2. Political polling in New Zealand


Source: Roy Morgan Research, 1 News Colmar Brunton, Newshub Reid Research, Forsyth Barr analysis

(2) Do other countries eliminate COVID-19?

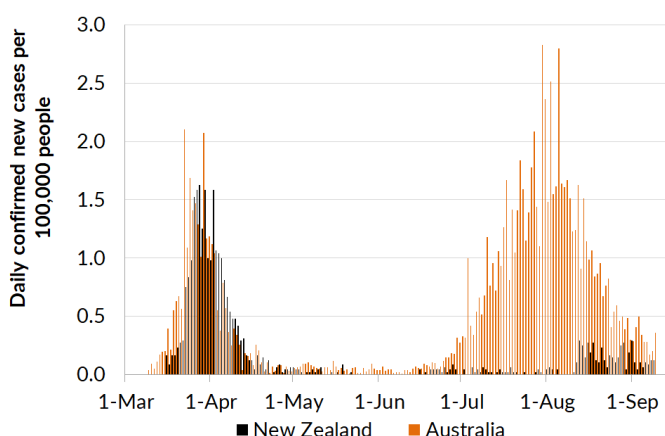
Few countries are running elimination strategies. While some Asian countries (including China, Taiwan, Thailand, Vietnam) have very low levels of new cases currently these are the exceptions rather than the norm. Some countries that reopened borders (for example Spain, France and the UK) are now experiencing second waves of rising infections. We expect the New Zealand Government to tread carefully.

Australia's suppression

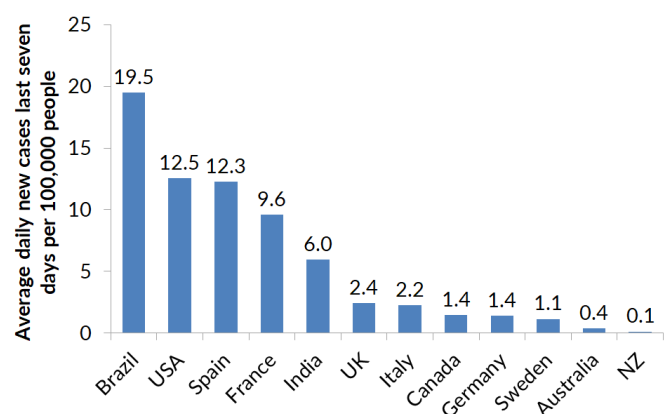
Our neighbour Australia is pursuing a "suppression strategy with the goal of no community transmission". This strategy may ultimately be successful in eliminating community transmission, but as history to date suggests, it may take time and any weaknesses in the strategy application can be quickly exploited by COVID-19. A state based approach to border re-openings in Australia is now more likely given recent comments from Prime Minister Scott Morrison. He outlined on 1 September 2020 that "when we're in a position to do so, and when the Acting Chief Medical Officer has come to a set of arrangements with New Zealand, then we would be able to have New Zealanders come to Australia.... That doesn't mean Australians can go to New Zealand. That's a matter for Prime Minister Ardern.... But if there's no COVID in Christchurch, and there's no COVID in Queensland, then there's no reason both of them can't come to Sydney".

Bubbles will initially be reliant on low transmission and trust

We expect the New Zealand Government to open up travel bubbles with countries, at least initially, where (1) infections rates are very low with limited or zero community transmission, and (2) higher levels of trust exist to ensure the bubble could operate safely for both countries. Australia appears to be the logical option, but even with current rates of infection, which appear low relative to other countries globally, the risk would be deemed too high.

Figure 3. Infection rates timeseries in NZ and Australia


Source: WHO, UN, Forsyth Barr analysis

Figure 4. Infection rates in selected countries (as at 7 Sept)


Source: WHO, UN, Forsyth Barr analysis

(3) What is the status of New Zealand's technology to track, trace and test?

The government's COVID tracer app now has been downloaded 2.2m times. Our observations and personal experience from travelling on public transport and visiting retail outlets is that contact tracing compliance is somewhere between ok (well below good), and poor. Unfortunately human behaviour quickly regresses to historic norms, and takes calculated risks, consciously or unconsciously, on a continuous basis. As long as people (probably correctly) are taking the view that the risks for them personally are very low, compliance is likely to deteriorate over time. We envisage that the number of recorded scans by registered users tapers off after the initial enthusiasm. This appears to be the case in data provided by the Ministry of Health in Figure 6.

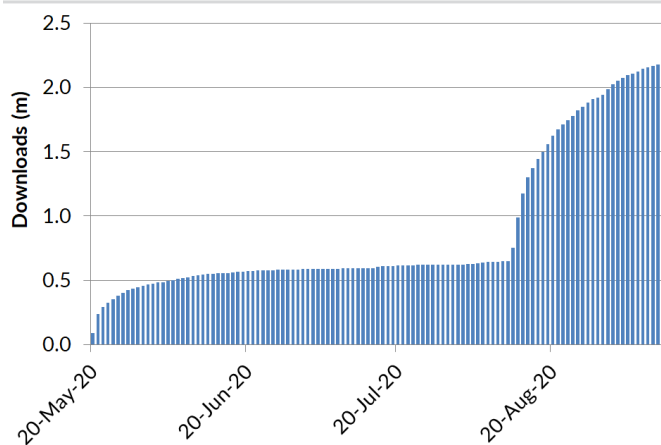
Technology will be critical to containment

The Sam Morgan led 'COVID Card' solution has struggled to gain Ministry of Health (MoH) engagement. This is unfortunate as a technology solution that relies far less on human behaviour, has greater chance of success, in our opinion. The broader testing regime could be enhanced for earlier detection of new cases. The inability of New Zealand to reopen the Cook Islands border suggests (with the benefit of hindsight) that the government was not confident in its own protection mechanisms (border controls, contact tracing and other measures) to mitigate the virus re-entry threat.

However, technology provides scope for best in class testing and contact tracing capability, and means a containment strategy (with open borders) could be undertaken in a relatively safe manner, without risk of widespread community transmission.

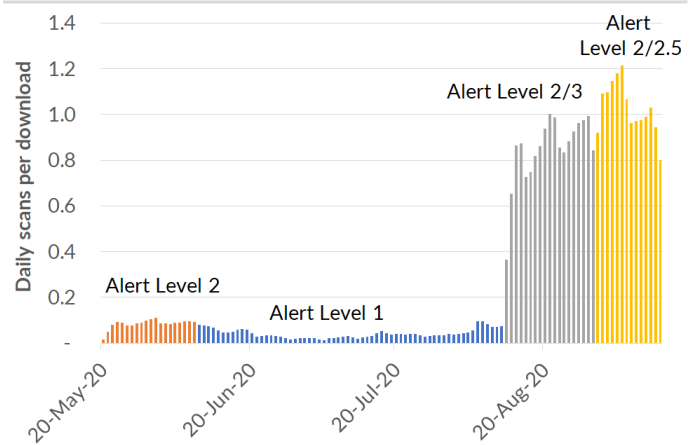
Rapid and reliable testing has the potential to result in a compromise solution with open borders to low risk countries, with rapid testing at the border and "one hour" quarantine.

Figure 5. Cumulative no. of NZ COVID Tracer app downloads



Source: MoH, Forsyth Barr analysis

Figure 6. Human behaviour regresses over time



Source: MoH, Forsyth Barr analysis

(4) When will a vaccine solution be readily available?

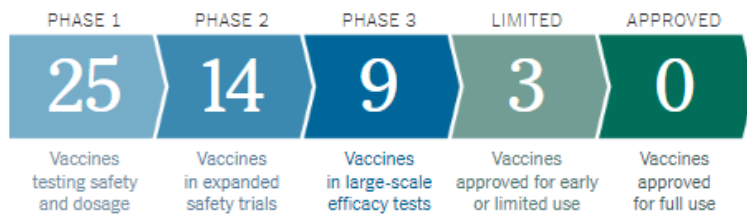
We have no specialist knowledge in vaccine development but we have read a whole heap of literature on the matter. This tells us that:

- **Only one virus has ever been eradicated by vaccination** – smallpox, therefore, it's likely that some ongoing level of COVID-19 infection will continue regardless of the success of a vaccine
- The best case vaccine development timelines suggest regulatory **approvals in late 2020, and mass distribution by mid-2021**, but this doesn't mean everyone globally has access to a vaccine or will want to use one
- The efficacy threshold of new vaccines will likely be lower than has been the case historically given political pressures; **the effectiveness and durability of a vaccine solution may limit its overall success**

The current level of investment in a COVID-19 vaccine, the number under trials and the regulatory desire to approve suggests a vaccine in some form will be available in 2021. There are currently 39 vaccines in clinical trials on humans, and at least 92 preclinical vaccines are under active investigation in animals.

However, we are wary that the anticipated silver bullet may be a long shot. Approved vaccines won't necessarily mean a return to pre COVID-19 normality given less than optimal efficacy. We foresee COVID-19 remaining in the global community for years to come, possibly decades, which means borders will need to incorporate a health security layer to its existing bio-security, aviation security and customs layers.

Figure 7. COVID-19 vaccines in trials globally

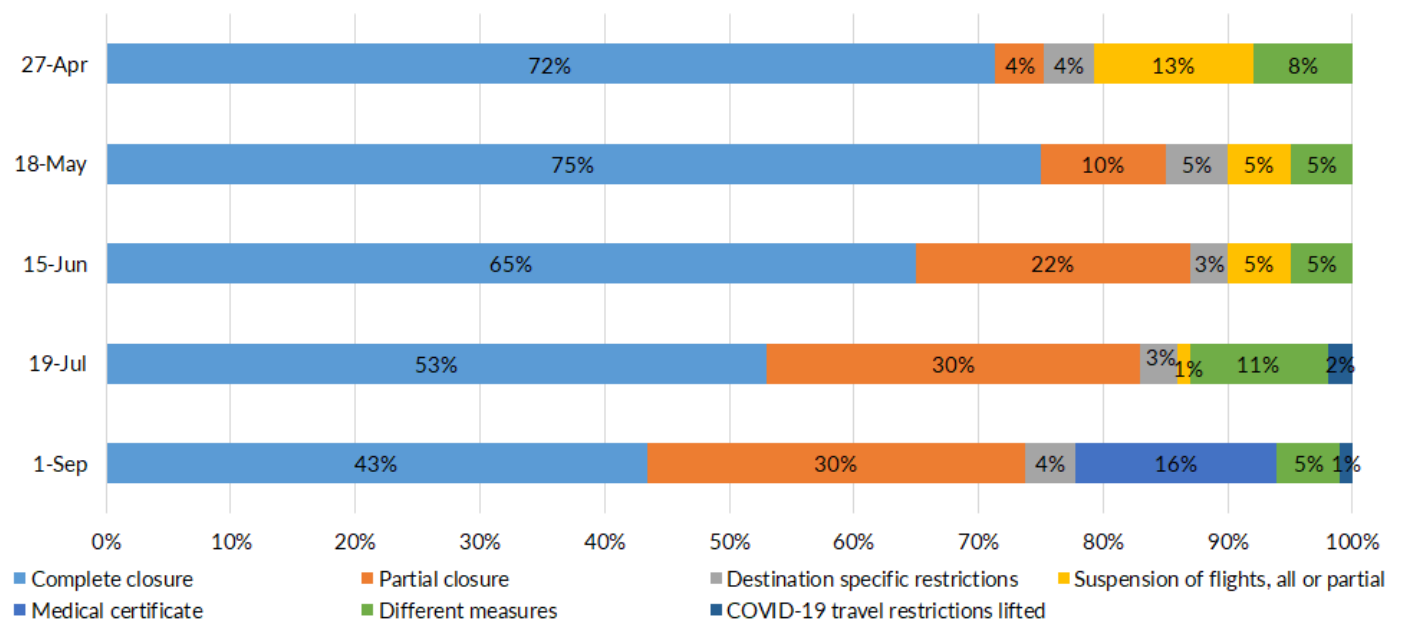


Source: Forsyth Barr analysis, <https://www.nytimes.com/interactive/2020/science/coronavirus-vaccine-tracker.html>.

Borders are reopening elsewhere

A majority of countries globally have started easing travel restrictions introduced in response to COVID-19. The UNWTO (UN World Tourism Organisation) reported last week that 53% of countries had eased border restrictions. However, 43% of countries retain complete border closures as measured for tourism purposes (including New Zealand and Australia). Virtually all countries have some form of border restriction in place.

Figure 8. Global travel restrictions have eased since April 2020



Source: UNWTO, Forsyth Barr analysis

Medical certificate measures

There is an emerging trend for medical certificates upon or after arrival; 35 countries (largely within the Caribbean and Africa) now apply this approach. Out of these 35 countries, three are asking for medical certificates as health declarations and 32 are now requesting the submission of a negative Polymerase Chain Reaction (PCR) test result. Quarantine from 7 to 14 days would apply for those cases where the test results are not presented within the requested timeframe.

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