

Coronavirus and its impact on our portfolio

by Mirae Asset Global Investments (Hong Kong) Limited

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Coronavirus Update

The total number of confirmed cases increased exponentially to 17,388 on 3rd February, spreading more widely than SARS.

Debates are also ongoing around whether the virus can spread without symptoms, given several infected but asymptomatic cases; the virus is known to have a 14 day incubation period.

On 31st January, the World Health Organization (WHO) declared a global public health emergency over the spread of the coronavirus, citing the declaration was made to consider the potential for the virus to spread to countries that are not prepared or have insufficient resources to deal with the contagion. So far, it has spread to multiple countries in Asia, North America and Europe.

R0 - The contagious level is measured by R0 (# of secondary infected cases per infected case without intervention). WHO estimates R0 to be 1.4-2.5, while according to China The Centers for Disease Control and Prevention (CDC) the estimated R0 is ~2-3. In comparison, SARS had an R0 of 2-5.

CFR - The overall case fatality rate (CFR) for 2019-nCoV is ~2-3%. This is much lower than the mortality rate of SARS (~9%). As of 1st February, the fatality rate of overall case was 2.1% (Hubei Province: 294/9,074 = 3.24%).

Comparisons of the 2019 nCoV with other major pathogens

Disease	R0	CFR
Diphtheria	6-7	5-10%
Ebola	1.5-2.5	25-90%
Seasonal flu	1-2	<0.1%
Measles	12-18	0.1-0.2%
Mumps	4-7	0.01%
Pertussis (whooping cough)	12-17	4%
Polio	5-7	5-10%(paralytic polio)
Rubella	5-7	3-6(developing countries)
Smallpox	5-7	30% (variola major)
SARS-CoV	3	9-16%
MERS-CoV	<1	30-40%
2019-nCoV	1.4-2.5	2-3%

Source: Vaccinologist, China Merchants Securities (HK) Research, Jan 2020.

There have been differing opinions around how long the 2019 nCoV pneumonia will last, with the bull case being a peak in mid-February according to Chinese professor, Dr. Nanshan Zhong, considering the national containment efforts taken extensively. The bear case of a peak in April/May comes from Professor Gabriel Leung from Hong Kong University. However, Leung's estimates have only factored in the lockdown of Wuhan alone whilst neglecting the fact that restricted access has been implemented in all major provinces and municipalities. This can effectively curb the spread of the disease.

According to WHO, to date, there is no effective antiviral drug or vaccine for 2019-nCoV infection. Symptomatic relief and supportive care (many requiring hospital care) are the current treatment methods. Although the DNA sequence for 2019-nCoV was quickly identified, companies / researchers still need to go through a full evaluation for safety and efficacy of the potential vaccine (typically takes years) before it is ready for market.

Since mid-January, the China's National Health Commission (NHC) has published four editions of diagnosis and treatment guidelines for 2019-nCoV.

Timeline of 2019-nCoV Outbreaks

Date	Incidents
2 nd February 2020	First death outside China reported in Philippines
31 st January 2020	WHO declared the coronavirus outbreak a Public Health Emergency of International Concern (PHEIC)
29 th January 2020	Researchers from the Academy of Military Medical Sciences and the Wuhan Institute of Virology (WIV) under the Chinese Academy of Sciences (CAS) found three existing drugs – remdesivir, chloroquine and ritonavir – with fairly good inhibitory effects on the novel coronavirus (2019-nCoV) at the cellular level
27 th January 2020	China's State Council said the seven-day Lunar New Year holiday will be extended to 2 February (instead of 31 January). Shanghai and Shenzhen stock markets will be open on 3 February (instead of 31 January)
25 th January 2020	A joint research team of scientists from the Shanghai Institute of Materia Medica (SIMM) under the CAS and ShanghaiTech University selected 30 drug candidates to be considered for clinical treatment of patients with 2019-nCoV
23 rd January 2020	China suspended travel to and from Wuhan City
21 st January 2020	US confirmed its first coronavirus case
13 th January 2020	First case in Thailand reported
12 th January 2020	China shared the genetic sequence of the novel coronavirus for countries to develop specific diagnostic kits
11 th and 12 th January 2020	WHO received further detailed information from the National Health Commission of China that the outbreak is associated with exposures in one seafood market in Wuhan City
11 th January 2020	First coronavirus death reported
7 th January 2020	The Chinese authorities confirmed that they had identified a new virus, a coronavirus temporarily named "2019-nCoV"
31 st December 2019	WHO was alerted to several cases of pneumonia in Wuhan City, Hubei Province of China. The virus did not match any other known virus
30 th December 2019	Cluster of cases of pneumonia of unknown origin reported to China's National Health Commission (NHC)

Source: NHC, China CDC, WHO, BOCI Research, Jan 2020.

Stock Level Impact

Alibaba:

E-commerce should gain market share from offline retailers as people are unwilling to go out and choose to buy online instead. From 24th to 29th January, the national postal service collection increased by 77% yoy to 81.3million parcels and deliveries increased by 110.3% yoy to 78.2million parcels. That said, e-commerce players are also negatively impacted by the overall consumption slowdown in China and disruptions on supply side as many e-commerce merchants are still not in operation in the short term (More for BABA than JD with more 3P exposure). From a mid to long term perspective, the epidemic should accelerate the shift from offline to online and provide opportunity to expand user base for e-commerce players including Alibaba.

CITS:

Tourism is one of the industries that is most impacted by the coronavirus. Various governments have stepped up measures to discourage travel activities into and out of China and the Chinese government has also suspended Individual Visitor Scheme (IVS) to Hong Kong and Macau. At the same time, domestic travel within China also slowed down, with China hotel RevPAR declining 43% yoy in the week of 19th to 25th January according to STR. We expect to see further declines in the final week of January and in the month of February. CITS is a dominant Duty free retailer in China with most of its revenue and profit derived from Hainan DFS and China airport DFS.

TAL and New Oriental:

TAL and EDU suspended most of their offline classes nationwide and encouraged students to use the online platform. These companies are negatively impacted in the short term because online courses are not available in all the cities that offline classes have penetrated and TAL will refund the price difference between online and offline classes for students moving to online platforms. Peiyou online and Xueersi.com ASP is around 50% and 40% of Peiyou offline, respectively. That said, similar to e-commerce players, this will accelerate students to shift from offline to online education classes and gain further market share from smaller offline players, particularly for TAL.

Kweichow Moutai and Wuliangye Yibin:

On average, Chinese New Year-driven high-end baijiu sales represents 30% - 40% of annual revenue. Adverse impact by nature of demand-

- Business gifting is least, if at all, affected by the coronavirus outbreak thanks to the timing of procurement and gift giving. Business gifting is done before the commencement of CNY holiday, and the prevalence of Feitian for this consumption occasion means that procurement must be done 4 – 6 weeks in advance to avoid shortage.
- Impact on family festive consumption is also moderate.
- Friends & family gifting is most severely affected, as this typically happens during the CNY holiday and most people have stayed in their own home this year.

Adverse impact by segments of the premium spectrum-

- The most premium end of the spectrum is least affected for consumers and businesses alike would complete CNY-related procurements in advance to avoid being hit by either supply shortage or festive ASP surge.
- Brands closer to the midpoint of the premium spectrum are expected to be the hardest hit.
- Mass-market baijiu is not used for gifting and banqueting, and should also fare relatively well.

Therefore, Kweichow Moutai should suffer the least from foregone sales due to the coronavirus, whereas the impact is likely more severe for Wuliangye Yibin.

Yihai International:

All plants in mainland China had previously planned to resume normal production on 2nd February, this has now been pushed back to 6th February at the earliest - subject to further postponements. Yihai will soon commence production in Malaysia (1 new plant in Senai) and in US (2 new plants in California) to meet the demand from overseas Haidilao restaurants which are still in operation. Haidilao would increase the volume share of 3P OEMs temporarily in cases of supply shortages in overseas restaurants. Yihai's 3P off-trade: current production capacity and inventory is only sufficient for supplying a few KAs (7-11, JD's 7Fresh, and HeMa were explicitly mentioned) until normal production and operation resumes for both Yihai and Shuhai. Shuhai is expected to resume normal operation by 5th February.

Universal Robina:

Sales attributable to China have never exceeded 1% of URC annual sales, and the company only operates 2 minor facilities in China for the GCF businesses. Given URC only sources resins from China, the coronavirus outbreak in China is unlikely to have any material impact on CoGS either. As far as URC is concerned, the coronavirus is yet to affect Philippines domestic consumption.

Shanghai Airport and Guangzhou Airport:

Our base case is for air traffic to decline by 30-50% over the next three months. Based on assumed traffic loss in 1Q20 of between 30-50% and max quarterly duty free rent loss, we expect 16-20% downside to consensus 2020 NP for SHIA and 36-54% downside for GBIA. However, our long term thesis on both companies remain unchanged as we expect both airports to structurally benefit from the rising mix of international travel, growing proportion of non-aeronautical revenue and increasing duty free spending per traveler. Chinese airports are attractive in terms of valuation (15-50% discount on EV/EBITDA) vs regional airports while also having higher growth rates.

Sydney Airport:

Flights to/from China accounted for 7% of international passengers in CY19. Bear case scenario is for Chinese (including HK) passenger numbers to decline by more than 50% in Feb and Mar which will negatively impact EBITDA by 7-10%. During SARS, SYD reported monthly decline of international PAX of around 18-20% though full year international PAX growth was positive. SYD continues to be one of the best airport assets in the region with a dividend yield of 5%. Earnings impact is relatively minor for CY20 while upside remains on negotiation with airlines for increased aeronautical charges.

Portfolio Strategy

We continue to evaluate our existing positions in terms of business competitiveness and risk reward on medium term outlook. Should we see a peak in affected cases, we may increase exposure in secular themes of China focused travel, tourism and discretionary consumption post a sharp selloff in recent weeks.

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