Economic Bulletin.

8 April 2020

Through the looking Glass – What Covid-19 means for New Zealand's tourism sector.

- The impact of Covid-19 on New Zealand's tourism sector will dwarf anything that has gone before.
- We are forecasting 2.3m international visitor arrivals in 2021, compared to 3.9 in 2019.
- The initial post-Covid-19 recovery will be led by domestic tourism and young international visitors.
- One possibility is that travel will be allowed for those certified as immune from Covid-19.
- Although near-term activity is unlikely to return to pre-Covid-19 levels, new opportunities, cheap money and low barriers to entry should encourage new start-ups.
- Long-term, visitor arrivals are expected to get back to pre-Covid-19 levels, and the tourism sector is likely to look much like it used to prior to the pandemic.

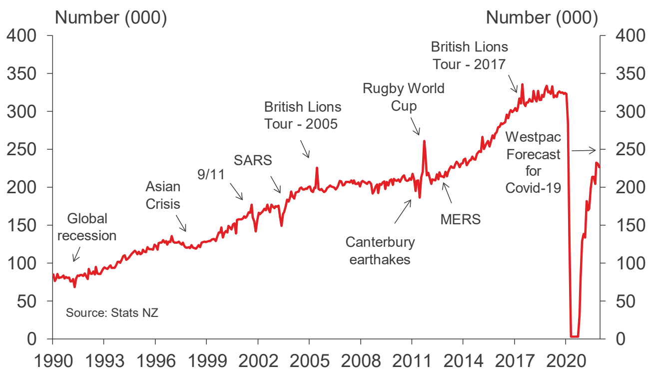
Dominick Stephens, Chief Economist
+64 21 262 5569

Paul Clark, Industry Economist
+64 21 713 704

An unprecedented event.

The Covid-19 bans on international and domestic travel are obviously a serious blow to New Zealand's tourism sector. This bulletin summarises the immediate impact on the sector, while also tracing out the path to recovery once Covid-19 has passed.

Figure 1: Monthly visitor arrivals to New Zealand, seasonally adjusted



The sector is facing disruption of a completely different order of magnitude to anything seen in recent decades. The travel restrictions used to combat SARS were largely limited to countries neighbouring China, the epicentre of the disease, and then only for a short time. The impact on visitor arrivals to New Zealand was short and sharp. The 9/11 terrorist attacks also had a short, sharp impact. The drop in visitor arrivals following the Canterbury earthquakes was of a similar size but lasted a little longer. Visitor arrivals fell slightly after the recessions of 1991, 1998 and 2008, and each time it took a couple of years for growth to re-emerge. Finally, for MERS no travel restrictions were introduced and there was little impact on visitor numbers to this country. None of these past events provides a good guide to how tourist arrivals will fare over the next couple of years, or how the industry will cope. Figure 1 illustrates how much more severe Covid-19 will be compared to anything that has gone before.

Path to recovery.

Given the pace at which Covid-19 infection rates are rising across the world, it is reasonable to assume that current travel restrictions into New Zealand will be here for some time. Indeed, we think that they will only be relaxed once it becomes clear that other countries are able to contain the spread of Covid-19 within their own borders. Even then, this is likely to be on a case-by-case basis given the potential for re-infection. On that basis, we are picking that New Zealand will remain virtually off limits to visitors from abroad for the next 6 months, with a partial relaxation of the travel ban introduced gradually thereafter as countries get control over the virus.

In a similar vein, restrictions on domestic travel are only likely to be relaxed once it is confirmed that the rate of infection in New Zealand is not only tracking lower but is at levels where it can easily be contained. It is not clear when that might be, but for the purposes of our forecasts we have assumed that domestic travel will remain restricted until July. Whatever the timing, it is likely that restrictions on local travel will be lifted well before those on visitor arrivals from abroad.

Once Covid-19 passes and travel restrictions are eased, activity levels are likely to lift very rapidly. However, we doubt they will return to previous levels any time soon. Even when travel restrictions are lifted, people will remain less likely to travel due to fear of Covid-19 and because their economies are going into reverse and incomes are under pressure.

However, as time progresses, and Covid-19 is finally relegated to the past, confidence should slowly return, and this will boost domestic travel and the visitor arrivals from abroad. We suspect that the first active travellers will be those who are immune to the virus, either because they have caught it and recovered, or because they are vaccinated. One possibility is that a global certification scheme to verify immunity will be developed, with borders opening only for "certified immune" people (much as yellow fever vaccination certificates are a condition of entry to many countries today). The rich countries of North America and Europe are the more likely to develop a vaccination and/or certification scheme early, meaning that early growth in visitors to New Zealand could come from these countries.

We also suspect that young travellers are likely to return sooner than older travellers, because young people are less susceptible to Covid-19 and are therefore less fearful.

Tourism forecasts.

Based on these assumptions, we expect close to zero visitor arrivals from abroad until September. After that, it's likely that there will be a partial recovery, extending well into 2021 and beyond. As such, we are picking visitor arrivals to fall from what was an expected 3.9m tourists in 2020 to just under 1m in 2020 – a 75% decline. Given an average spend of $3,300 per visitor, this suggests that the industry stands to lose about $12bn in revenue from offshore visitor arrivals in 2020.

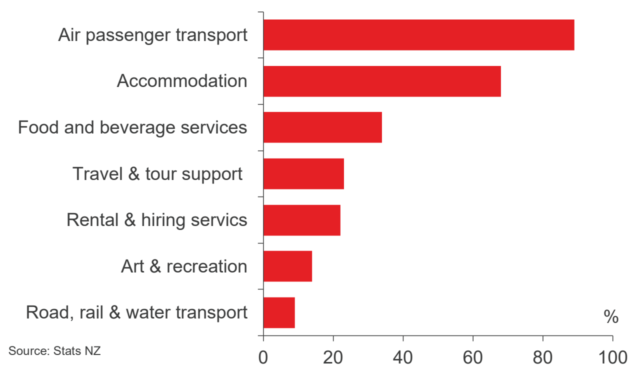
As the recovery gathers pace, losses in 2021 are likely to be smaller but still significant. One off-events such as the America's Cup, the Women's Cricket World Cup and APEC towards the end of the year should help. So too, an expected charm offensive from Tourism New Zealand, tasked with attracting visitors to these shores. Still, our forecasts suggest that visitor arrivals in 2021 will be around 1.6m below the 2019 level, equating to about $5.5bn lower revenue.

The outlook for domestic tourism is better. With the lockdown now firmly in place, there is little chance of domestic travel at present. However, as New Zealand gradually moves back to alert Level 1, we would expect domestic tourism to recover quite strongly. New Zealanders will probably be deterred from travelling overseas either out of fear of Covid-19 or by other countries' travel restrictions. Consequently, Kiwis will holiday at home. The extent of domestic tourism, however, is likely to be tempered by the slow economy. All things considered, we expect that revenues generated from domestic tourism will be down by about $8bn in 2020 compared to 2019.

Sector impacts.

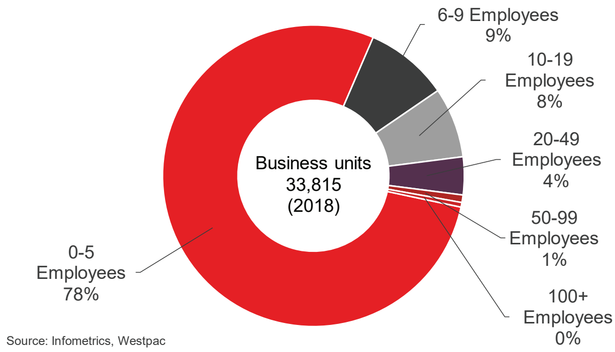
For the thousands of firms that rely on tourism, this period of low or no international and domestic tourism will be very challenging. Among the most vulnerable will be the big names in the airline industry, which are in the process of restructuring their operations. Also vulnerable are the 30,000 or so small firms that employ less than 20 people, ranging from accommodation, travel, rental and tour service providers to restaurant operators and bar owners. Some retailers in tourism heavy regions might also be included in this mix, although the retail sector as a whole in New Zealand places little reliance on tourism.

Figure 2: Tourism demand for sector outputs



The situation would have been a lot worse had it not been for the Government's wage subsidy, now amounting to $9.3bn, and the Business Finance Guarantee Scheme, which will advance relatively cheap credit to help firms get through the disrupted period where possible. Thousands of firms in the tourism sector are already tapping into these subsidies and other programmes to stave off possible closures and job layoffs.

Figure 3: Tourism sector structure - 2018



However, the wage subsidy is time limited to 12 weeks at present. Even if the Government's support packages are extended, it is likely that visitor arrivals will remain impaired for longer than the wage subsidies are available. Unfortunately, it is likely that many firms will go out of business, although not as many as would have been the case had it not been for the subsidy. Most vulnerable will be those small firms that depend heavily on cash flowing through their books and lack the reserves to get through the disrupted period. Tourist guides, bars, restaurants and some accommodation providers will be among them. Larger firms are more able to tap into debt to keep their heads above water.

Once the crisis has passed, we think it will be these small firms that will lead the recovery. As visitor arrivals start to pick up, new entrepreneurially driven firms, bolstered by cheap money and low barriers to entry, will spring up. Large firms, less dynamic than their smaller counterparts, will focus on reducing debt and are less likely to expand.

That said, the sector is likely to be a shadow of its former self over the next couple of years, with fewer firms servicing a smaller number of tourists than before the pandemic. Those that spring up are likely to target specific high growth areas. These might include adventure and eco-tourism for younger people arriving from abroad as well as family vacation packages for Kiwis looking to travel domestically. Small, agile accommodation providers, as well as food and beverage outlets, are likely to tailor their service offerings accordingly. Other areas won't do as well. Cruise liner visits, for example, are likely to fall sharply in the aftermath of the pandemic, and so there are likely to be few firms servicing this segment of the market.

With fewer tourists coming into the country, many existing firms will find themselves having to make some big changes to how they operate to keep their heads above water. One example we have already seen is that houses previously listed on Air BnB targeting tourists are migrating back to the long-term rental market targeting locals. Large hotels are simply closing floors or wings to minimise operating costs.

Longer-term, we do think that visitor arrivals will eventually get back to roughly the same levels as those last seen prior to Covid-19. After all, international trade and travel recovered from the Spanish Flu pandemic of 1918 to 1920, and the 1920s were a strong decade for the world economy. Key to the eventual recovery will be the efforts of Tourism New Zealand, which is expected to go into marketing overdrive. But this time it won't be just the youngsters that will be coming to New Zealand. Tourists of all ages will eventually return in greater numbers, encouraging more firms to set up shop. Most of these will be small, and many will be niched, much like they were prior to the pandemic. After much introspection, cruise ships should also return while hotel occupancy rates are expected to rise. Indeed, long-term, we are picking the industry to look very much like it did prior to the pandemic.

Contact the Westpac economics team.

Dominick Stephens, Chief Economist
+64 9 336 5671

Michael Gordon, Senior Economist
+64 9 336 5670

Satish Ranchhod, Senior Economist
+64 9 336 5668

Paul Clark, Industry Economist
+64 9 336 5656

Any questions email:
economics@westpac.co.nz

Past performance is not a reliable indicator of future performance. The forecasts given in this document are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Disclaimer.