

Coronavirus Outbreak

Implications for Businesses

 **Risk Consulting**

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Executive Summary

Since its initial identification in Hubei Province, China in November-December 2019, the novel coronavirus (2019-nCoV) outbreak has spread outside the region, affecting more than 20 countries and impacting health, trade, travel and the global economy. The following provides an analysis of its impact on global businesses.

- At the regional level, the outbreak will translate into a decrease in regional exports and medium-term revision of forecasted growth.
- Supply chain disruptions have already prompted factory closures, particularly affecting the manufacturing, oil and gas, and retail sectors; more are likely to follow.
- While businesses relying on Chinese exports are most exposed to potential supply chain disruptions, global demand for goods mass-produced in China will also likely affect global prices, increasing business costs and eroding profit margins.
- Many multinationals have triggered contingency plans as a result of travel restrictions and supply chain disruptions. Remote-working practices have increased, placing pressure on IT infrastructure and internet networks. Among these, industries reliant on staff presence have seen a drop in production, notably impacting the oil and gas sector.
- Drastic travel restrictions imposed by the US have prompted China to denounce Washington's decision as an attempt to undermine its soft power, potentially compromising recent progress towards a resolution of the rivals' trade dispute.
- Businesses operating in Hong Kong will plausibly face further unrest when the outbreak subsides amid accusations of government mismanagement of the outbreak.

Coronavirus Overview

The 2019 Novel coronavirus (2019-nCoV or COVID-19) is a variant of influenza that causes a respiratory illness previously not recorded in humans.

- As of 13 February 2020, there have been 60,374 confirmed cases of 2019-nCoV and 1,355 deaths attributed to the outbreak, including two outside mainland China (one in the Philippines the other in Hong Kong).
- On 30 January, the World Health Organisation (WHO) characterised the outbreak as a 'public health emergency of international concern' (PHEIC),
- On 10 February, the death toll surpassed the SARS outbreak in 2003, which stood at 774.

Origins: The first case was reported on 31 December and the source of the outbreak has been linked to the inland Chinese city of Wuhan, Hubei province. Various strains of the coronavirus are highly prevalent among animals; however, the outbreak constitutes the seventh instance of a coronavirus strain making the 'leap' and infecting humans, alongside the Severe Acute Respiratory Syndrome (SARS) and the Middle East Respiratory Syndrome Coronavirus (MERS-CoV) among the others. As of 11 February, the mortality rate for 2019-nCoV is approximately 2 percent.

Symptoms of coronavirus are similar to those of a common cold, such as fever, cough, irritable throat, difficulty breathing, headache and fatigue. Many of the associated fatalities have been due to pneumonia caused by the virus.

Transmission is thought to primarily occur upon contact with respiratory droplets from an infectious individual coughing or sneezing.

At-Risk Individuals: Initial evidence suggests that individuals at higher risk of contracting coronavirus include people with underlying medical conditions, the elderly and those with compromised immune systems. Some people have had a mild illness and recovered, while others have had more severe infections, and some have died.

Treatment: There is no specific treatment and no vaccine for coronavirus. Infected individuals receive supportive care to relieve symptoms. Avoiding direct contact with people exhibiting respiratory symptoms remains the primary preventative measure, along with maintaining good personal hygiene.

Outlook: The WHO, among other health authorities including those of China, estimates that coronavirus infection rates are likely to continue to increase in the immediate term or until the advent of a vaccine for the virus, which is unlikely to be readily available until the summer (June-July). However, the WHO cautions that reliable predictions about the trajectory and spread of the virus will not be possible until key details about its nature – including its pathology and contagiousness – are confirmed.

Analysis

Despite further spread of the virus in the region and globally over the past two weeks, the vast majority of cases continue to be overwhelmingly concentrated in mainland China. The actual number of such cases is also likely to be considerably higher than officially reported, as some individuals presenting symptoms do not seek medical attention. There is also precedent for Chinese authorities to underreport during public health emergencies.

While a reduction of airline services leaving China and increased health screening measures and travel restrictions implemented at regional airports may lead to a decline in the number of exported cases globally, continued spread of the illness is likely over the near-term. The public health risks from further spread of the virus outside China and the immediate region are considerably higher in countries with underdeveloped public health systems than in those of more advanced economies, though the latter remain at risk.

Despite the uncertainty surrounding the nature and trajectory of the virus, the auxiliary effects of the outbreak will continue to impact businesses operating in or via China, including travel, supply chain management, and contingency and business continuity planning.

TRAVEL RISKS

While health screenings and related restrictions at airports can lead to immigration delays and possible quarantine of at least 14 days, these measures apply primarily to travellers arriving via air either directly or indirectly from China, meaning it is currently unlikely that individuals travelling to destinations outside of mainland China would be significantly or repeatedly impacted by such restrictions.

REGIONAL ECONOMIC IMPACT

Although emanating primarily out of China, the coronavirus outbreak is likely to adversely affect the majority of Asian economies in 2020. As millions of Chinese limit their movement – and, consequently, their spending – Chinese demand for imports will weaken, negatively impacting regional suppliers. A reduction in visitor arrivals, disruption to supply chains and forced factory closures will cause additional economic damage for other Asian countries and companies.

WORLD HEALTH ORGANISATION ADVICE

The basic principles to reduce the general risk of transmission of acute respiratory infections, according to the WHO, include the following:

- Avoiding close contact with people suffering from acute respiratory infections.
- Frequent hand-washing, especially after direct contact with ill people or their environment.
- Avoiding unprotected contact with farm or wild animals.
- People with symptoms of acute respiratory infection should practice cough etiquette (maintain distance, cover coughs and sneezes with disposable tissues or clothing, and wash hands).
- Within healthcare facilities, enhance standard infection prevention and control practices in hospitals, especially in emergency departments.
- WHO does not recommend any specific health measures for travellers. In case of symptoms suggestive of respiratory illness either during or after travel, travellers are encouraged to seek medical attention and share their travel history with their healthcare provider.
- Regarding the wearing of facemasks, WHO and the US Centers for Disease Control and Prevention (CDC) both say that it is not medically advised for people without symptoms to wear masks, unless dictated by the local authorities.

Countries and companies involved in China's 'belt and road' (BRI) infrastructure initiative, particularly those heavily dependent on Chinese investment, are also among those most likely to be impacted by the outbreak. As Chinese financial resources – both public and private – become increasingly redirected towards preventing the virus from spreading and managing reputational impacts of the outbreak, future planned foreign investments in China will remain at risk of postponement if not outright cancellation.

SUPPLY CHAIN DISRUPTION

As the Chinese government continues with its efforts to control the spread of the disease by closing factories and limiting movements, regional supply-chain mobility is likely to become further restricted in the near-term. Such disruptions have already triggered force majeure claims by major Chinese companies. Most notably, China's largest LNG importer CNOOC on 6 February declared force majeure on LNG contracts, citing fuel delivery delays and obstruction as a result of the outbreak. CNOOC's counterparties, Shell and Total, have rejected the claims, making it likely that the issue will develop into a legal dispute, with others potentially to follow suit.

In the near to medium term, foreign companies that rely on Chinese manufacturing and exports will face continued exposure to the adverse impacts of the outbreak on global supply chains. Japanese car manufacturer Nissan has announced plans to suspend operations at its factory in Kyushu from 14 February due to a shortage of parts from suppliers in China. On 7 February, South Korean automaker Hyundai halted production at its plant in Ulsan owing to similar supply chain disruptions in China, while another Korean auto manufacturer, Kia, suspended work for a day earlier in February, citing similar shortages.

If the outbreak persists and spreads over the medium term, some foreign companies that are heavily dependent on goods manufactured in China could be forced to either absorb mounting logistical expenses or shift their supply chains to more stable markets. The shift in supply and demand will likely inflate global costs of items that are mass produced in China; which will erode margins. This will translate into a decline of year on year profit for many manufacturing companies and hence hinder growth. Share prices for major Chinese suppliers, as well as those businesses dependent on Chinese exports who fail to diversify their supply chains, will likely be affected.

Although northeast Asian economies, particularly sectors that depend on China as a link in global supply chains, will remain at greatest risk of adverse economic impacts stemming from the outbreak, should such disruptions continue or worsen, the impact is unlikely to remain confined to the region. Other manufacturing centres in Southeast Asia and India would likely face mounting difficulties in the event of a protracted period of reduced production in China, while leaked emails published by a US news outlet show Amazon has begun stockpiling products made in China due to coronavirus risk on its supply chain. Multinationals with adequate or surplus supplies of component parts otherwise affected by logistical disruptions could stand to gain from the situation, by inflating prices and maintaining production at a time when the market is squeezed due to the shortages and their smaller competitors are forced to wind-down operations or run losses.

BUSINESS CONTINUITY

Beyond China's borders, international responses to the outbreak, including the imposition of travel restrictions by many foreign governments, have prompted businesses to trigger contingency plans. Supply disruption of goods and services by Chinese companies with operations outside of China will likely occur in the medium term.

An illustrative example includes oil and gas supply by Chinese majors. Following the departure of Chinese officials from Iraq and other oil-producing countries for the Chinese New Year holiday, many have been unable to return to Iraq on rotation as Iraqi officials have blocked entry into Iraq to all non-Iraqi nationals having recently travelled to China. This has resulted in a shortage of Chinese expatriate staff in Iraq and disrupted rotations, with a likely impact on supply in the medium term.

The impact on crude oil prices will be offset by concerns over the plausible reduced demand for oil imports by China, the largest oil importer globally. This has already caused a sharp fall in oil prices, prompting the Organization of the Petroleum Exporting Countries (OPEC) to discuss potential cuts to crude output.

Numerous Southeast Asian countries have closed offices and promoted remote working practices, adding pressure onto IT infrastructure as online collaboration tools are increasingly used. This will benefit cloud services and will strain scalability capabilities for companies' networks and IT structures. Regulatory requirements and employee rights to remuneration and leave time, as well as medical support and personal protection equipment, has seen companies revise their business continuity plans.

GEOPOLITICAL IMPACT

As well as the health implications of the outbreak itself and various governmental responses, the declaration from the WHO that the situation constitutes a public health emergency of international concern (PHEIC) has had significant geopolitical ramifications. This is the first time a PHEIC has been declared for an outbreak primarily involving a leading economy since the WHO introduced its threshold guidelines for such declarations in 2005. Previous instances included outbreaks that took place in middle-to-low income countries such as the DR Congo, Guinea, Uganda, Brazil, Mexico, Syria and Afghanistan.

Two days after the PHEIC declaration, the US government advised its citizens not to travel to China due to the outbreak. The drastic US measures were poorly received by Chinese officials, who intimated that they were seen as politically motivated and aimed at exaggerating the extent of the outbreak to embarrass and discredit China internationally. Over the medium-term, perceptions that the Chinese authorities have poorly managed the outbreak, combined with a potentially prolonged disruption in trade linking China to other countries, will risk diminishing Beijing's geopolitical influence and international standing. More immediately, tensions between the US and China over the coronavirus outbreak could jeopardise recent progress made between the two sides in resolving their trade dispute, although there is currently no indication of such a trend.

The cancellation of major public events in China as a result of the coronavirus outbreak is likely to further compromise China's international standing. On 11 February, China's General Administration of Sport (GAS) instructed the country's sports associations to consider postponing or cancelling events as far as April. The 2020 Chinese Grand Prix, originally scheduled to take place in Shanghai on 19 April, was postponed due to the coronavirus outbreak. Multiple other events due to be held in the country over the coming months, such as the 18th World Athletics Indoor Championships and the 14th edition of the Chinese National Winter Games, have similarly been either cancelled or rescheduled. Elsewhere, organisers of the 2020 Tokyo Olympics, which are due to commence on 24 July, have repeatedly stated that the Games will not be cancelled or postponed. However, concerns have been raised over the viability of continuing with the mass-spectator event given the potential for the virus to proliferate in such an environment, as well as the logistical and practical challenges associated with current travel restrictions and the impact that could have on athletes' preparations.

IMPACT ON HONG KONG UNREST

The situation in restive Hong Kong, which has reported the most confirmed cases outside of mainland China, remains complex. At this stage, the incompatibility of organising public gatherings amid the outbreak and associated public health efforts is such that the protest movement has effectively been forced into a hiatus. Although the lull in mass anti-government protests is likely to continue for as long as the coronavirus outbreak persists and deters activists from attending large gatherings, there is minimal evidence to suggest that the anti-government sentiment underlying the protest movement has subsided. Widespread anger at the local authorities for allegedly mishandling managing the situation, including by not closing its border with the mainland, have continued to fuel anti-government sentiment. Once the threat to public health subsides, the anti-government protest campaign and associated mass-demonstrations are highly likely to resume. The potential for social upheaval will be particularly pronounced if the outbreak is contained by 9 June, which will mark one year since more than 1 million Hong Kongers marched through the streets to denounce the controversial extradition bill that catalysed the pro-democracy movement.

MITIGATION MEASURES

G4S Risk Consulting provides tailored security risk assessments, mitigation measures and business continuity planning advisory. For further information, please contact us at: riskconsulting@rm.g4s.com

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