

Swine flu - pandemic or just another flu pandemonium?

Oliver's insights



Key points

- Swine flu deaths in Mexico and the spread of cases around the world have led to fears of a global flu pandemic.
- Coming at a time when the global economy is already weakened, pandemic fears have already caused nervousness in share markets and more weakness is possible.
- While there is reason for concern, the experience with SARS and bird flu highlight that worst case pandemic fears don't usually come to pass. The world is also better prepared for a viral pandemic now. The key for investors is to be alert, but not alarmed.

Introduction

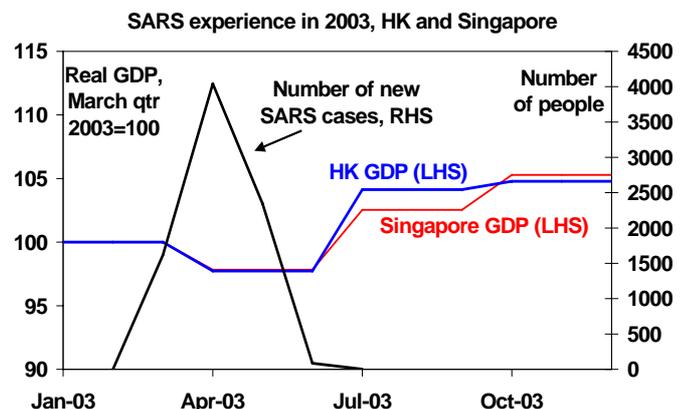
As if investors didn't have enough to worry about, concerns about another flu pandemic – swine flu in this case – are now causing concerns globally following deaths in Mexico and its spreading to various parts of the world. The World Health Organisation has declared the outbreak a “public health emergency” and raised its pandemic alert rating to 4 (on a scale that runs to 6). Global share markets have been rattled by concerns about its economic impact with travel related stocks being hard hit so far. While a flu pandemic - were it to eventuate - would first and foremost be a human tragedy, the economic and financial market impact would also be significant. The swine flu outbreak has come at a time when the world is already weakened by the global financial crisis. That said, there is a real danger of over-reacting to the outbreak of swine flu; it could just turn out to be a nasty version of the flu. Recent experiences with SARS and bird flu highlight that worst case pandemic fears don't always eventuate. This note looks at the risks.

Past experience – Spanish flu, SARS and bird flu

Before looking at the swine flu outbreak causing concern it is worth reviewing past pandemics – both real and feared. There were three influenza pandemics in the last century: 1918-19, 1957 and 1968. The 1957 and 1968 pandemics are estimated to have killed up to 4 million people. However, the 1918 Spanish flu pandemic was the most severe. While the mortality rate was low, up to 50 million people died worldwide. In the US the first case was reported in March 1918 and deaths peaked sometime

between September 1918 and March 1919 (with possibly a double peak), but cases were still reported as late as 1920. In Australia, the disease hit in January 1919, infected over 30% of Sydney's population and killed over 11,000 by the end of 1919. With a big proportion of the population staying at home, economic activity was severely disrupted, although this was compounded by the ending of World War I. US industrial production slumped 18% between March 1918 and March 1919. Australian real GDP slumped 5.5% in 1919-20 (but then rebounded 13.6% in 2020-21). The share market impact is hard to discern given the volatility associated with the ending of WWI, however US and Australian share markets rose through much of the pandemic period.

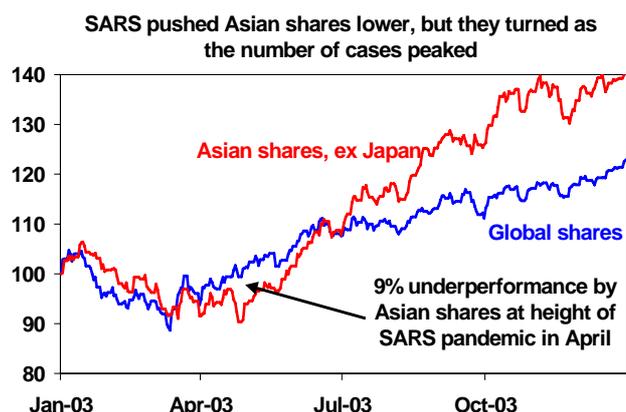
The SARS outbreak of 2003 is perhaps a more useful guide to predicting the economic and financial market damage a pandemic might cause. After emerging in China around February 2003, SARS infected about 8000 people (mostly in Asia) in 30 countries over a five month period and had a mortality rate of about 10%. While the number infected was not that great, SARS had a big negative impact on the countries most affected as people stayed home for fear of catching it. While the number of new cases peaked in April 2003, GDP in Hong Kong and Singapore (two of the countries most affected) slumped by over 2% in the June quarter of 2003 as retail sales fell, workers stayed home and travel dried up. Growth then subsequently rebounded.



Source: Thomson Financial, AMP Capital Investors

Reflecting SARS, Asian shares fell in April 2003, even though global shares started to move out of a three year

bear market from March. The April 2003 low in Asian shares coincided with signs the number of new cases was peaking, and this was well ahead of the economic recovery.



Source: Thomson Financial, AMP Capital Investors

Most pandemics have taken six to 18 months to run their course and usually peter out as measures are taken to slow their spread (eg, hygiene, quarantining, banning gatherings, preventing travel). SARS ended quicker due to the nature of the virus and rapid action by authorities.

In 2005 and early 2006, there was significant concern that a severe strain of bird flu (caused by a virus called H5N1), which was resulting in human casualties mainly in parts of Asia where people had contact with chickens, would mutate into a form that was readily transmissible between humans. However, this didn't really eventuate and as such the economic impact was modest although it did cause bouts of volatility in share markets in 2005 and early 2006.

What do we know about swine flu outbreak

As it's early days there isn't a lot of information on the swine flu virus now causing concern. However, here is a summary of what we do know:

- The swine flu virus causing concern (influenza type A, H1N1) appears to contain genetic material from human viruses, North American bird viruses and pig viruses. It may be completely new or it may have been around for a while having become only recently detectible due to new testing and surveillance procedures.
- As a number of cases have had no direct exposure to pigs, the concern with this virus is that it has the ability to transmit between humans. This is something that the H5N1 bird flu virus never really attained (at least not so far).
- In Mexico it also seems to be hitting young adults (20 to 35 year olds) the hardest.
- While it has apparently killed 150 or so people in Mexico, the death rate is unknown as thousands may have been infected and simply recovered. So far there have been no reported deaths outside Mexico. For example, some New Zealand students who are thought likely to have contracted the swine flu after a trip to Mexico don't have severe symptoms and some reports indicate they appear to be recovering. As such the deaths in Mexico may have something to do with its

less able health care system. It is also worth noting that hundreds of people die from flu every year anyway.

- More significantly, while there is no vaccine that protects against swine flu, two anti-viral drugs, Tamiflu and Relenza, have been effective against the new strains according to the US Centers for Disease Control.
- Australia is well prepared with a stockpile of nearly 9 million doses of anti-viral drugs, including Relenza. Australia also has a well developed plan to deal with a pandemic. Today many countries are also far better prepared given all the concerns about bird flu over the last few years. Less developed countries are of course more vulnerable.
- It is also worth noting that the world is mobilising against the threat so this may slow its spread.

The economic and financial impact

Coming at a time when the world is in its worst recession since the great depression and investors are still very nervous, concern about the swine flu outbreak turning into a global pandemic could drive a setback in share markets. Travel related stocks are most vulnerable followed by consumer related shares whereas health care stocks (particularly manufacturers of anti-virals) could continue to do well.

A full blown swine flu pandemic with millions of deaths could also deepen and extend the global recession already underway - global travel would virtually cease, workers would stay at home and the supply of goods and services would be seriously interrupted. If this were to occur the bear market in shares would likely resume and cash would be the place to be.

However, while there is reason for concern and it is easy to dream up nightmare scenarios, the experience with the SARS outbreak of 2003 and the pandemonium over bird flu with "predictions" it could kill as many as 150 million people tell us that the worst case fears of pandemics usually don't come to pass. Hopefully the same will apply to the swine flu outbreak and any setback in shares driven by pandemic fears will just provide a buying opportunity. Certainly the lack of deaths outside of Mexico so far, signs that anti-virals appear to be effective and the better preparedness of the world for a pandemic after the scares of recent years are positive signs in this regard. These considerations suggest that while there might be a bit of short term volatility there is unlikely to be a major impact on share markets. That said, given the risks and with many flu pandemic experts agreeing that a new pandemic could occur any time, it will be necessary for investors to keep a close eye on how swine flu develops. The key for investors at this stage is to be alert, but not alarmed.

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