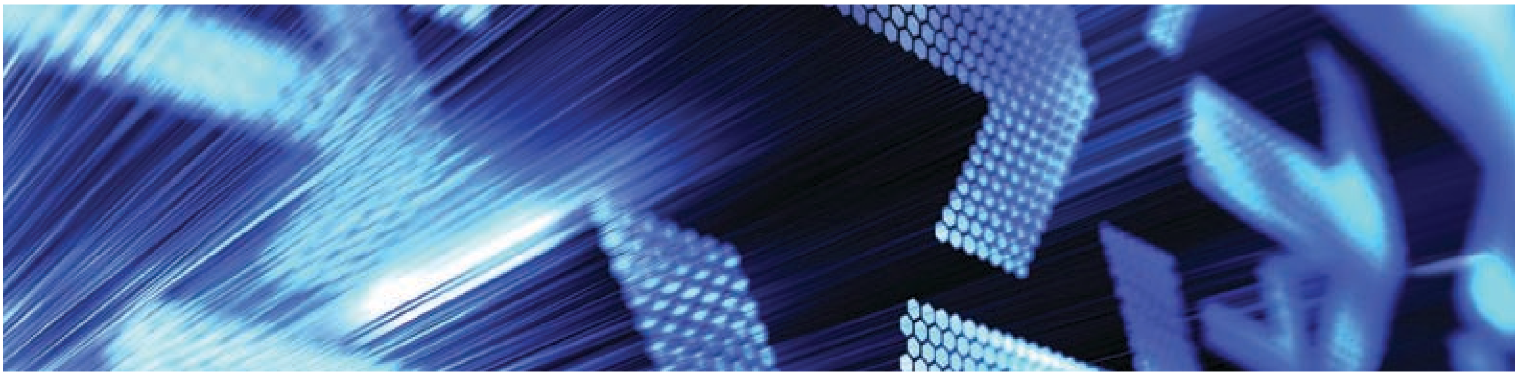
Australian Government
Australian Customs Service

Customs Strategic Outlook 2015 Update 2008



An update to the *Customs Strategic Outlook 2015* to assist in identifying future trends and implications for border management to 2015

January 2009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Context

The *Customs Strategic Outlook 2015* considers the global context in which border management activities occur and looks in detail at the impact on border management developments.

The *Customs Strategic Outlook – Update 2008* (the Update) is a supplement to the *Customs Strategic Outlook 2015* (the Outlook) to reflect events occurring in the preceding year that may influence future trends, potential implications on border management out to 2015 and provides possible responses in the medium term. The Update deals only with new trends observed in 2008 and does not supplant unchanged trends covered by the Outlook.

It is noted that the Update considers issues current as at the time of publication. Should events overtake the discussions in this paper prior to the release of Update 2009, separate strategic product will be published.

The Update is intended to encourage discussion and debate about how Customs may position itself to respond to the challenges of the future. It is an unclassified product based on open source information. It does not assess or rate risk, nor seek to generate an operational response, but rather to identify issues for further consideration.


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Executive summary

Overall, while global drivers of change continued to evolve over the preceding 12 months, the trends identified in the Update 2008 broadly reflect and continue to build upon those articulated in the Customs Strategic Outlook 2015 (the Outlook). The information in the Update has been written to give guidance on future trends identified in 2008 that have potential implications for border management to 2015. The Update should be read as a companion document to the drivers and implications of trends identified in the Outlook.

The instability of global financial markets was a key economic development in 2008. This may impact on Australia's international trade and travel volumes in the short-term; however the long-term prognosis is for the nation to experience sustained economic growth, albeit at a slower rate than in 2007. The recession in the United States, Japan and the European Union is likely to delay the growth of predicted trade figures.

Developments in 2008 highlighted the increasing trend towards regionalisation of trade and travel, driven by increases in the cost of transportation and a renewed focus on regional and bilateral trade agreements. Continued economic growth in the Asia Pacific region and the rising cost of conducting long distance international trade are likely to drive a relative increase in trade volumes between Australia and regional neighbours.

Trade security issues are likely to shape long-term expectations of the border management role. Concerns regarding product safety and counterfeit goods may lead to expectations of increased intervention at the border for community protection purposes. Growing interest in nuclear power in Southeast Asia may cause Australia to reshape its controls around counter-proliferation and trade in strategic goods. A continued focus on import and export security by the US may also impact on Customs operations in containerised cargo.

Over the long-term, the combined impact of fluctuating world oil prices and the proposed implementation of an Australian Carbon Pollution Reduction Scheme in 2010 may result in border management having increased operating costs. International trade and travel trends may also vary in response to the generally increased cost of fuel.


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The border

A number of developments or events have occurred in 2008 with the potential to shape and influence future trends. The following discussion identifies these key drivers, the likelihood of border implications arising from these drivers and explores possible responses.

There are notable linkages between many of the key drivers in 2008 that may have a cumulative impact on border management. Issues such as the global economy, volatile oil prices, trade negotiations and the continuing focus on consumer safety will all contribute towards a likely increase in regionalised trade. Therefore, these key drivers should not be considered in isolation.

The economy

Key drivers

The instability of the United States (US) economy is a key uncertainty to come out of 2008. The economic slowing in the US as well as parts of the European Union (EU) is likely to impact Australia in the short-term via changes in the volume of some international trade and travel. If, as many analysts are predicting, the US experiences a lengthy downturn this may serve to facilitate the increasing dominance of China as a driver of the global economy.

The instability in the global financial markets has flowed through to other sectors of the global economy. Due to the stock exchange volatility in Australia, there has been widespread reporting in the media of the potential for the Australian economy to fall into recession. However, major economic opinion is that Australia's economy is relatively resilient. While the current economic slowing will see a deceleration, at this time it appears unlikely to cause a negative downturn and therefore a recession.

It is likely that there will continue to be positive growth in the Australian Gross Domestic Product, though probably at a slower rate than in 2007. This is due to Australian unemployment rates being very low and a continued demand for commodities from relatively resilient economies in Asia, despite inflation being relatively high compared to the last 10 years and the slowing economies in US and the EU.

Border implications

Analysis of the impact of economic instability for events such as the 1990-91 recession, 1997-99 Asian financial crisis and the 2001 US recession indicate that these all impacted on year to year trends. However, an overall trend towards greater volumes of both passengers and trade has continued since the late 1980s.

Economic drivers are likely to exaggerate existing variation in Australia's import and export trends. But short term uncertainty in international trade is unlikely to change long term trends.

Travel is likely to continue within our region, continuing the longer term trend of migration. Short term variability in people's travel patterns will occur, but the long-term growth in passenger numbers trend is likely to continue.

Border response

A watching brief and critical ongoing assessments will be necessary to ensure that Customs is able to respond to any emerging challenges.

The forecast growth for trade is likely to be delayed in the event of a relatively prolonged period of slow growth, following a recession in the US, Japan and the EU.

Developing economies

Key drivers

The slowing of the US economy will present growth opportunities for developing economies such as Brazil, with the ongoing discoveries over the past year of reportedly significant oil and gas reserves. Over the next decade Brazil is likely to become an increasingly significant competitor with Australia in some sectors, especially if infrastructure in Brazil improves sufficiently to overcome the cost differential in shipping Brazilian slab steel to China. While political stability remains an uncertainty, the Australia-Chile bilateral trade agreement, to come into force January 2009, is likely to increase the importance of the Brazilian economy regardless.

Countries such as Vietnam are growing as manufacturing centres in the Asian region as well as increasing their share of foreign direct investment. As the Association of South East Asian Nations (ASEAN) aims to become a borderless unified trading bloc by 2015, the importance of these countries as trading partners with Australia is likely to increase. However, Australia's influence in the region may be affected as affluence and energy demands increase in Asia. Emerging economies in Asia may be more comfortable negotiating trade in resource materials and manufactured goods with higher paying, less politically demanding countries such as China.

Border implications

Implications for border management may arise from trade within the Asia-Pacific region. Trade in this region has increased in 2008 and is likely to continue as the region maintains economic growth, albeit at reduced levels from 2007. Increased transport costs are likely to cause industry to review distant sourcing strategies. Looking forward over the next ten years, outsourcing to geographically distant countries may not be as attractive. Suppliers may look to re-align manufacturing in developing economies closer to points of consumption.

Increased transportation costs following the volatility of fuel prices will first impact the business of air carriers, but international shipping costs will also rise and domestic transport costs will become higher, impacting the entire supply chain. As a nation that depends heavily on trade, Australia is likely to be significantly impacted as the cost of conducting long distance international trade becomes increasingly more expensive. It is likely that regional trade will be a strong influence on cargo growth as manufacturers are likely to be compelled to look to neighbouring markets for opportunities as the cost of long-haul markets are impacted by transport costs.

Border response

Anticipate regionalised trade and travel patterns and develop strategies to incorporate border management and law enforcement agencies in our region into information sharing activities on both legitimate trade and illicit activities.

Trade negotiations

Key drivers

Multilateral trade negotiations stumbled in 2008. The collapse of the Doha talks in July 2008 and current trade developments again suggest there is likely to be a returned focus on regional and bilateral trade agreements. During the Doha round of talks Australia, the EU, India and the US have all signed trade agreements; but the US Congress over the same period has blocked the passage of a number of agreements. There is some speculation by analysts that this reflects current suspicion in the US of the benefits of free trade agreements, although it is as yet unclear how the new administration will impact this.

Border implications

The renewed focus on regional and bilateral trade agreements may result in an increase in the scope and complexity of the work performed by border management agencies. While tariffs will be reduced under new trade agreements, there will be continued complexity of the Customs Tariff as a classification tool for community protection and trade safeguards. The increasing complexity of rules of origin may complicate intervention and post-transactional compliance activity. This situation could be compounded by multiple overlapping agreements making it more difficult to determine the true origin of goods and may drive a change in risk assessment procedures to consider what countries could be used as transiting ports for high risk goods.

Border response
Strategies will be needed to ease the effect of more complex trade and tariff rules on border management.

Nuclear capability – Supply chain security

Key drivers
Australia's trade security is likely to increase in significance with the growing interest in nuclear power in Southeast Asia and the Australian Government's stated commitment to proliferation controls. Indonesia is expected to commission its first nuclear power plant by 2016/17 and Vietnam in 2020. This is likely to focus the public debate in Australia about proliferation on uranium and its enrichment. Recent suggestions of a potential Indonesian partnership with Iran to develop a nuclear power generation capability will give added urgency to this debate. As some countries tighten their counter proliferation controls, shippers of these types of goods, even legitimate, are likely to shift their logistics routes to avoid potential scrutiny to either deliberately evade controls or simply as a matter of expedience to avoid delays to shipments.

Further complexity may be introduced into the debate on proliferation as unexpected countries develop nuclear capability, illustrated by Brazil's recently announced plans to commission a nuclear submarine by 2020. Similarly, the development of novel technologies and weapons systems may lead to hitherto disregarded items being controlled under counter-proliferation arrangements.

Border implications
Due to the interest of new countries in nuclear activity, implications for border management are likely to stem from potentially greater sensitivity about uranium exports. Tighter counter proliferation controls from other countries may result in different trade routes for these types of goods, meaning that border management agencies may need to change some assumptions in order to target such goods. Advances in novel technologies may further complicate border management in the control and identification of non-traditional materials, source trading partners and trade routes.

The continued focus on import and export security may also have the potential to impact on Customs operations in containerised cargo. This may take similar form to the US push for 100 per cent inspection of sea containers at the export port of loading to take effect from mid-2012. Assuming this law comes into effect, it will re-orientate ports into greater regulation of export cargo. There is likely to be an increasing pressure on export operations to have capabilities in several different types of technology for non intrusive inspection of a large number of export containers in a time critical environment.

The flow on effect of tough security regulations of export cargo could lead to possible reduction in ports not only in Australia, but globally, that are capable of supplying export containers to the US. This will result in more complex logistics systems to channel exports from their place of origin to a compliant port as the "port of export". This has the potential to create international hub ports making the supply chain more opaque to border management agencies.

Border response
Possible methods to increase our knowledge and accountability of goods being exported from Australia may include:

- Continuing to actively promote risk-based approaches

to supply-chain security in contrast to mass screening.
- Expanding investment to enhance Customs border targeting and risk assessment of exports.
- Anticipating more complex relationships between suppliers and end-users for counter-proliferation intelligence and targeting activities.
- Accepting the development of more complex export structures in the supply chain to accommodate enhanced security regimes, possibly in the format of the US 100 per cent inspection of sea cargo containers.

Consumer safety and community protection

Key drivers

Trade and import security will continue to be the focus of community expectations as emerging economies in Asia continue to develop their manufacturing, amongst other industries. They are likely to become more influential at the same time as trade becomes increasingly regionalised. The growth in this regionalised trade may lead to an increase in incidents of goods of questionable safety being imported into Australia. There are increasing community protection issues regarding product safety and counterfeit goods as public scrutiny of this issue increased in 2008. Counterfeit pharmaceuticals are a growing area of concern and this is likely to increase with emerging and expanding supply methods such as internet commerce facilitating the trade in illicit and counterfeit pharmaceuticals via online pharmacies.

Organised crime groups are also continuing to become more sophisticated in their operations. In the past year, law enforcement agencies have reported an increase in the number of domestic organised crime groups which are developing and strengthening regional and global partnerships with transnational organised crime groups. These partnerships are formed to facilitate the movement of illicit goods and commodities across the Australian border.

Border implications

The community is likely to expect greater intervention at the border to protect consumers from goods not meeting health and safety standards, such as pharmaceuticals and automotive spare parts. Meeting this expectation will involve increased resource allocation to enable a stricter inspection regime and legislative changes to enhance Customs ability to interdict goods prior to release.

It is likely that regulatory and permitting agencies will utilise Customs' presence at the border to control and monitor an increasing range of internationally regulated goods and prohibited items of environmental and safety concern.

Border response

Customs may need to explore new border controls, regulations, inspection and intervention methods in the interests of consumer safety, and the protection of Intellectual Property Rights and interdiction of illicit goods.

Should greater inspection/intervention rates at the border be required to ensure product safety, this will require an increased resource allocation to enable a stricter inspection regime. However, allocation of resources for stricter inspection regimes would have to be tempered by a clear-sighted assessment of the actual risk posed to the community.

Effective control of goods for consumer safety at the border may require a fundamental rethink of existing business including closer operational and informational links between Customs and the regulators, between Customs and industry and, finally, enhanced powers for the immediate disposal of low value goods, and expansion of infringement notice type schemes.

Food shortages

Key drivers

Over the next decade the cost of subsistence may become an important driver of global changes. Gains made on reducing global rates of poverty in 2008, driven largely by increased affluence in China, were undone in many places by the dramatic impact of markedly increased food prices. The Food and Agriculture Organisation of the United Nations has recorded an overall rise in food price indices by 44 per cent in the twelve months to June 2008. This has increased the number of people going hungry by about 50 million globally. The economic pressure from higher food prices has exacerbated conditions in unstable states and, in the developed world, has invigorated debate about the merits of growing crops for the purpose of bio-fuels manufacture rather than food. South America and India have further encouraged rising prices by imposing export restrictions and taxes enforced on some food products such as corn, grain and rice in order to secure domestic supply.

Border implications

Increases in the cost of living, including the price of food and fluctuating costs of fuel, could foster an increase in regional population displacement. The implications for border management may include the need for greater monitoring of the economic exclusion zone to combat illegal fishing, and increased emphasis on pre departure interdiction of illegal arrivals in both the air and sea environment.

Increased price controls, tariffs and export restrictions by grain producing countries further complicate trading systems and may impact on longer term trends in trade.

Border response

Structural changes to the Government's approach to maritime people smuggling, which now gives Customs primary carriage of this activity, have initiated an enhanced response to this pressure.

Container ship capacity

Key drivers

Other changes to the global supply chain are likely to stem from increases in the carrying capacity of container ships past 2012. This means ship congestion at certain ports may become of increasing concern, impacting on the global supply chain. Lower carrier profitability in the trade routes such as Asia/Australian trade may be caused by overcapacity, and shipping lines will inevitably pass increases in running costs through higher freight rates. This is likely to have a number of implications including greater demand on port infrastructure to efficiently deal with throughput; demand peaks as cargo arrives in 'waves'; increased consolidation of cargo; and a growth in the amount of cargo transhipping through Australia.

Border implications

The growth in the volume of containerised cargo in Australia is still projected at this time to follow the international average of five to six per cent. This will lead to a predicted 70 per cent increase in the number of twenty foot equivalent units (TEU) imported and exported to and from Australia by 2015.

Border response

Customs may need to continue initiatives supporting a whole of government approach to improve the quality and connectedness of information between border management agencies and industry to support legitimate trade in goods, such as the International Single Trade Window Initiative.

Continued initiatives in workforce planning to provide flexible solutions to peaks of cargo as it arrives in 'waves', amongst other demands on resources due to the volume of containerised cargo.

Airlines

Key drivers

Global economic instability will continue to impact low cost air carriers. However, they are likely to continue to increase their market share for the time being in response to growing relative affluence in Asia, albeit mostly on intra-Asian routes. Some will operate internationally on the relatively short flight to Australia and will continue to make forays into the Australian domestic market, assuming maintenance of a good safety record.

It is noted that these carriers are likely to be the worst affected by a post catastrophic event travel downturn and will only remain viable while efficiency offsets (low costs) can mitigate high oil prices. It remains possible that these airlines might be a comparatively short term phenomenon.

Border implications

In the airline industry consolidation is likely to continue globally in response to continued volatility of fuel prices and international travel becomes more costly, seasonal peaks in passenger numbers and air cargo consolidations will increase. With the international airline industry reducing in size through mergers and/or code sharing arrangements, international carriers are likely to become influential lobbyists of government, both state and federal. Low cost carriers will increasingly utilise regional airports because of lower costs and their proximity to Asia. A concomitant model of low cost airports has emerged, in which the emphasis is on quick turnaround times for aircraft rather than services to passengers; border agencies can by default end up providing passengers services they would not otherwise at large airports, which may not be considered a useful allocation of resources.

Border response

Customs is identifying regional airports best placed for short-term use by low cost carriers and to be ready to respond to likely peaks and troughs in passenger numbers as carriers change their operating patterns in response to the costs associated with fluctuating oil prices. A clear statement may need to be developed on the nature and extent of services that Customs provides at such airports.

Energy — cost and supply constraints

Key drivers

In 2008, issues of global resource availability have come to the forefront of global concern. The economic and political drivers affecting the cost of oil have developed as a significant domestic and international cause of concern. The increasing supply pressures, the inherent cost of alternatives to oil extraction, and the continuing demand for oil for purposes other than energy, make it unlikely the price of oil will return to pre-2000 levels. While oil prices have reduced from the record high prices earlier in 2008, they remain vulnerable to external drivers that can drive up prices and increase demand.

Further impacting future energy resource costs, in 2008 the Australian Government responded to international concerns about climate change with the proposal to introduce a Carbon Pollution Reduction Scheme. This has the objective of reducing carbon emission via a cap and trade scheme to commence in 2010. The scheme will entail a cap on the total amount of carbon pollution which may be emitted within Australia each year, which has the potential to increase fuel and other running costs over the long-term.

Border implications

Continuing variability of oil prices is likely to contribute to increased regional trade as it becomes less viable to trade across greater distances, greater pressure on the global food shortage as crops are grown for bio-fuels rather than food and increased pressures on low cost airline carriers.

A review of current commentary on the Carbon Pollution Reduction Scheme reveals some concern of financial pressure on Australian industry and energy consumers. The scheme's trading permits may also have an impact on Customs operating expenses, particularly in relation to aerial and coastal surveillance.

Further implications for border management may arise if analogues of the Carbon Pollution Reduction Scheme trading permits were to become commodities on the international market. This may have the potential for organised crime groups to attempt exploitation of vulnerabilities in cross border transactions. Characteristically, organised crime groups readily seek out and adapt to emerging business opportunities. Carbon emissions trading permits will represent a high value commodity which criminal syndicates may attempt to exploit, for example, to launder the profits of criminal enterprise.

Border response

The continued external pressures affecting the cost of fuel world wide will require an operational readiness by border management to respond to the likely peaks and troughs in passenger and cargo volumes as carriers change their operating patterns in response to the costs associated with fluctuating oil prices. Additionally, the costs associated with operating Customs maritime surveillance, and more generally, will be impacted by high fuel prices.

The potential for organised crime groups to attempt to exploit carbon emissions trading permits may have border management implications.

Political outcomes

Key drivers

Political commentary arising from the US presidential election indicates that the change in administration may have little immediate impact on the international security environment, although it is likely to cause some initial finetuning of US commitments abroad. That said, the election win by relative hardliners in Iran this year, and the likely similar outcome for the Iranian presidential election in 2009, means that Iran's relationship with the West will remain adversarial and will be key in keeping the US focussed on the Middle East.

Other geopolitical events for 2008 include the Taiwanese election of a government more moderately disposed towards China that has reduced the danger of open conflict for now. Tensions will however remain between China and the US and may shift in emphasis to other arenas, such as space, as the US continues to view China as a competitor.

Border implications

Statements made by various members of the international community reveal that the current approach towards Iran on the subject of enrichment of uranium is likely to remain unchanged. The US will continue to push for harder sanctions from United Nations Security Councils beyond travel and financial institutions. Any expanded sanction regime will impact on border management operations and risk assessment, complicating import and export systems in identification of origin and destination and passenger movements.

Border response

In the event that expanded sanctions should occur, border management agencies will look to concurrently expand initiatives for whole-of-government approach to improve the quality and sharing of information between border management agencies, including overseas counterparts. These initiatives will be used especially in response to circumstances where shipment through third countries as a means to disguise the origin or destination of goods is suspected.


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Border response summary

Broad capability development needs

The *Customs Strategic Outlook 2015* identified a number of broad capability development areas that will allow Australia's border management agency to face the challenges out to 2015. Many components of these capabilities are already being developed and are likely to be implemented prior to 2015.

The border response options discussed in this Update supplement and reiterate the importance of the operating responses detailed in the *Customs Strategic Outlook 2015*.

1. Operational readiness

This broad capability concerns the positioning of border management resources to respond to challenges in a timely and considered manner. Challenges likely to be faced include increased pressure on cargo handling facilities, sea ports tonnage capacity, the use of regional airports by low cost carriers and expectations for border management to control an increasing number of prohibited items of a security, environmental or safety concern. The areas of focus for this capability could include:

- Continuing identification of regional airports best placed for short term use by low cost carriers.
- Managing the likely peaks and troughs in passenger and cargo numbers as carriers change their operating patterns in response to the costs associated with fluctuating oil prices.
- Prevention and response capabilities against illegal foreign fishing and people trafficking that can be deployed quickly and effectively in a highly changeable environment.
- Recognising the growing costs associated with the Carbon Pollution Reduction Scheme and considering investment into carbon efficient technology research.
- Continuing current initiatives such as tracking of cross border shipments and use of technology to identify consignments of abnormal movements.
- Monitoring and responding to the increasing amount of internationally regulated goods and prohibited items of a security, environmental or safety concern.
- Anticipating more complex relationships between suppliers and end-users for counter-proliferation intelligence and targeting activities.
- Preparing for the development of more complex export structures in the supply chain to accommodate enhanced security regimes, possibly similar to the United States 100 per cent inspection of sea cargo.

2. Information sharing

This existing capability will become increasingly important as trade becomes increasingly regionalised, the country of origin becomes more difficult to determine and expectations on border management expand to control an increasing number of prohibited items of a security, environmental or safety concern. The focus of this capability could include:

- Developing strategies to achieve increased information sharing between regional border management and law enforcement agencies for both legitimate trade and illicit activities.
- Working with regional border management and consumer safety standards authorities to develop comprehensive information sharing techniques.
- Continuing initiatives for a whole-of-government approach to improve the quality and sharing of information between border management agencies and industry to support legitimate trade in goods, such as single trade window.
- Continuing to work with other law enforcement agencies, health authorities, the private sector and the pharmaceutical industry to coordinate action and obtaining advanced data in combating counterfeit goods not meeting standard ahead of the border.
- Continuing investment in initiatives that enhance

Customs border targeting and risk assessment of exports.

Additionally, there are international events such as continuing economic uncertainty, implications arising from the change of government in the US, and the impact of fluctuating world food and oil prices that impact Australia's border management agencies. These events will continue to be monitored, and critical ongoing assessments made to ensure that Australia's border management agency is prepared and able to respond to emerging challenges.