

Asia Illicit Tobacco Indicator 2016: Australia

Prepared by Oxford Economics
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Australia: Legal Domestic Sales

- Australia Legal Domestic Sales of cigarettes and loose tobacco are estimated at 18.5 billion cigarettes (or cigarette equivalents) in 2016, falling by 3.1% from 2015.¹
- Manufactured cigarettes account for the majority of the legal market for tobacco, with a share of 85% of Legal Domestic Sales in Australia. The legal market for cigarettes is composed almost exclusively of 3 international manufacturers (BAT, Imperial Tobacco, and PM).
- Australian cigarette prices are among the highest in the world, costing AUD 20.4 per pack of 20 cigarettes based on the Most Sold Brand. This is substantially higher than most markets covered by the Asia Illicit Tobacco Indicator Report, with the exception of New Zealand, where a pack of the Most Sold Brand of cigarettes is AUD 0.5 higher at AUD 20.9 per pack.²
- In particular, Australian cigarette prices are much higher than in China (AUD 1.98 per pack) and South Korea (AUD 5.33), both of which have consistently been key source markets for non-domestic Inflows since the beginning of the Asia Illicit Tobacco Indicator research.
- Cigarette prices have evolved in line with Excise Taxes in recent years, which have been progressively increased by the Australian government. It was announced in the 2016-17 budget that Excise Taxes will continue to increase by 12.5% per year to 2020.

Australia

Legal Domestic Sales:

18.5 bn
cigarettes

Including RYO equivalent.

Price:

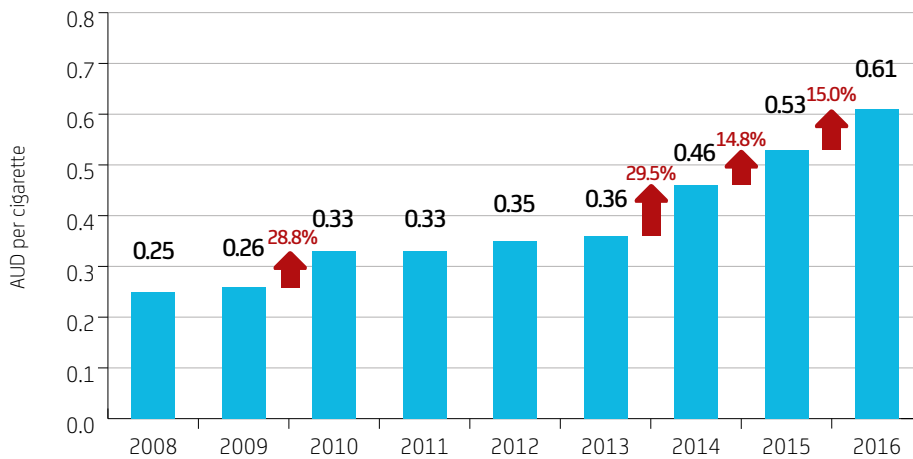
AUD **20.4**

USD **15.4**

¹Based on official statistics on the volume of tobacco clearances sourced from the Australian Treasury Department. A conversion rate of 0.8 grams per cigarette was applied to turn loose tobacco weight into cigarette equivalent, based on rates applied by the Australian Taxation Office.

²Price per pack of 20 of the Most Sold Brand in October 2016, based on PM data. The Most Sold Brand in Australia consists of a pack of 40 cigarettes. The Australian pack price of 20 is therefore derived from a pack of 40 cigarettes.

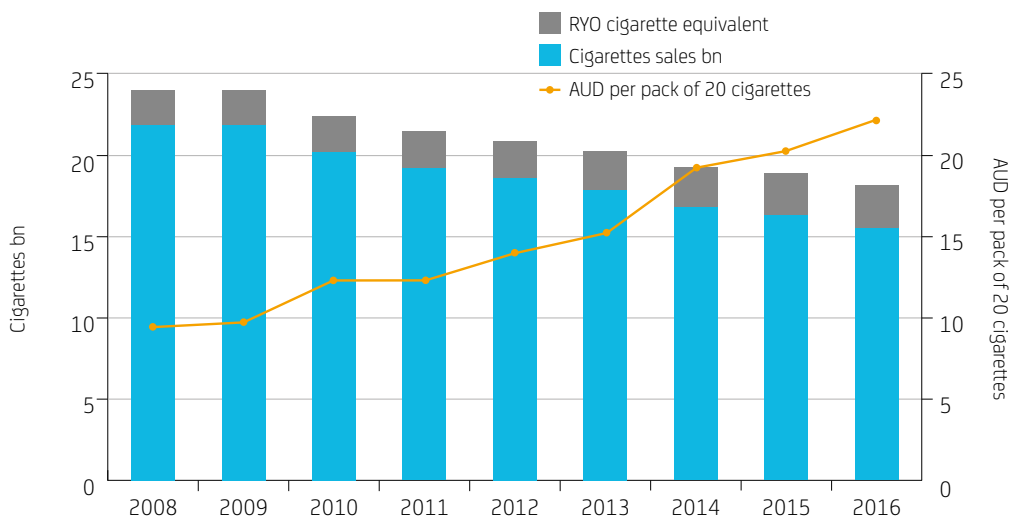
Australia: Excise duty applied to cigarettes³



Source: Australian Taxation Office

³Rate applied in October of each year. Includes individual Excise Tax increases as well as biannual index-linked rises.

Australia: Legal Domestic Sales and prices⁴



Source: Euromonitor, KPMG, and Oxford Economics based on PM data

⁴Price per pack of Winfield 25's (the Most Sold Brand until 2015) in October of each year. The pack price of 20 is derived from a pack of 25 cigarettes.

Australia: Tobacco Consumption

- The results from two Empty Pack Surveys,¹ combined with official statistics on the volume of tobacco clearances sourced from the Australian Treasury Department,² and KPMG data on Chop-chop volumes,³ were used to estimate Total Consumption of cigarettes and loose tobacco in Australia.
- Total Consumption (legal and illicit) is estimated at 21.4 billion cigarettes in 2016, representing a decline of 3.9% in comparison with 2015. Of this, an estimated 86.5% or 18.5 billion cigarettes is Legal Domestic Consumption, 0.5% is Non-Domestic Legal Consumption, and 13.0% or 2.8 billion cigarettes is Illicit Consumption.⁴
- Total Non-Domestic Inflows also fell in 2016, by 8.5%. This was underpinned by a 20% fall in Non-Domestic Illicit consumption. Non-Domestic Illicit was 1.1 bn cigarettes, close to 50% lower than in 2013. However, Chop-chop volumes rose by 1.3% in 2016, following a modest fall the previous year.
- With Illicit Consumption registering a larger decline than Legal Domestic Consumption, Illicit Incidence fell by 0.6pp to 13.0% in 2016. This is the second consecutive decline in Illicit Incidence, but the proportion of Total Consumption accounted for by illicit cigarettes remains 2pp higher than in 2012.
- The findings of this Report are in line with similar analysis conducted by KPMG, which indicates that Illicit Incidence was 13.9% in 2016, 0.1pp lower than in 2015.⁵ The higher level of Illicit Incidence in the KPMG research is partially explained by a supplementary analysis of Illicit Whites to include brands that have been packaged for the domestic market, which are otherwise designated as of domestic market origin in the Empty Pack Survey, and are therefore excluded in this Report. This would suggest that our figures probably underestimate the true value of Illicit Incidence in Australia. Moreover, the presence of non-domestic Illicit Whites suggest our estimates are lower-bound estimates of the size of the entire (legal and illegal) market.
- The recent decline in Illicit Consumption has coincided with a pick-up in anti-illicit tobacco efforts in Australia, part of a wider move to integrate agencies working on border and customs enforcement. In October 2015, the Australian Border Force (ABF) declared that illegal tobacco was a top priority, launching a dedicated unit called the “Tobacco Strike Team” (TST).
- In June 2016, the TST received additional funding to expand their activities in the fight against illicit tobacco. In turn, there has been a significant increase in seizures in the fiscal year 2016/17. According to the ABF, around 318 tonnes of illegal tobacco, with a duty rate equivalent to AUD 240 million, was seized in 2016/17, nearly four times the level of seizures in the previous fiscal year. Over the same period, officers from the Australian Tax Office made 13 seizures related to home-grown tobacco, destroying 76 tonnes of tobacco with a duty rate equivalent to AUD 59.4 million in the process.⁶

Australia: Composition of cigarette consumption⁷

	2012		2013		2014		2015		2016		% change 2015-16
	Cigarettes bn	%	Cigarettes bn	%	Cigarettes bn	%	Cigarettes bn	%	Cigarettes bn	%	
Legal Domestic Consumption (LDC)	21.9	88.7	21.5	86.5	19.8	85.6	19.1	85.8	18.5	86.5	-3.1
Legal Domestic Sales (LDS)	21.9	—	21.5	—	19.8	—	19.1	—	18.5	—	-3.1
Outflows of domestic duty-paid cigarettes	0.0	—	0.0	—	0.0	—	-0.1	—	-0.1	—	-7.3
Total Non-Domestic Inflows (ND)	2.8	11.3	3.3	13.5	3.3	14.4	3.2	14.2	2.9	13.5	-8.5
Non-Domestic Legal (NDL)	0.1	0.4	0.1	0.4	0.1	0.5	0.1	0.6	0.1	0.5	-10.1
Non-Domestic Illicit	0.8	3.1	1.9	7.8	1.5	6.4	1.4	6.2	1.1	5.2	-20.0
Chop-chop	1.9	7.8	1.3	5.2	1.7	7.4	1.6	7.4	1.7	7.8	1.3
Domestic Illicit	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	n/a
Total Consumption	24.7	100.0	24.8	100.0	23.1	100.0	22.2	100.0	21.4	100.0	-3.9
Total Illicit Consumption	2.7	10.9	3.2	13.0	3.2	13.9	3.0	13.6	2.8	13.0	-8.4

Source: Oxford Economics

¹Empty Pack Surveys were undertaken in 2016 Q2 and 2016 Q4 (see Report methodology for more details).

²Tobacco clearances for 2012–2016 retrieved via FOI requests from the Australian Treasury Department. 2012 data were adjusted to account for tobacco products destroyed following the introduction of plain packaging legislation.

³KPMG, *Illicit tobacco in Australia*, 2016 Full Year Report, March 2017.

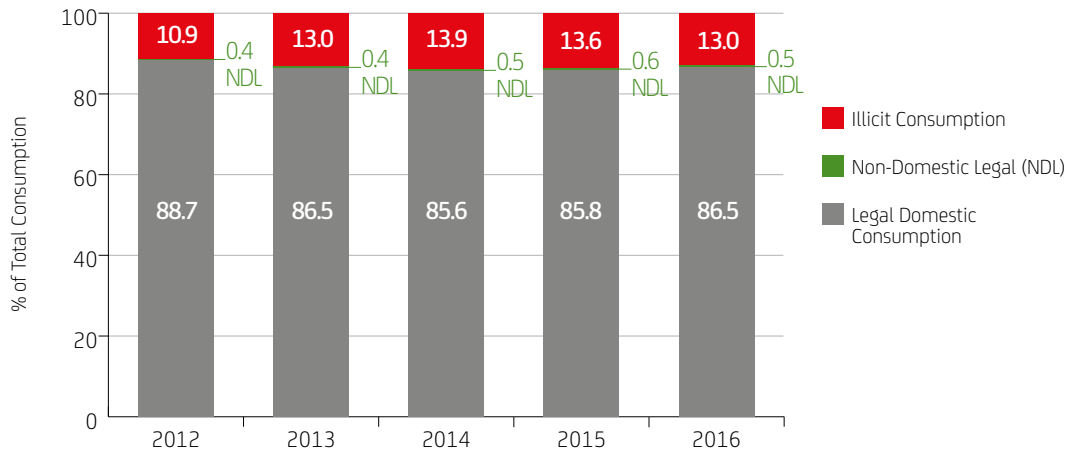
⁴This illicit total includes cigarette equivalents of Chop-chop. A conversion rate of 0.8 grams per cigarette was applied to turn weight into cigarette equivalent, based on rates applied by the Australian Taxation Office.

⁵KPMG, *Illicit tobacco in Australia*, 2016 Full Year Report, March 2017.

⁶Department of Immigration and Border Protection Newsroom, see <http://newsroom.border.gov.au/releases>, and ATO media centre, see <https://www.ato.gov.au/Media-centre>

⁷All references to cigarette consumption includes RYO equivalent.

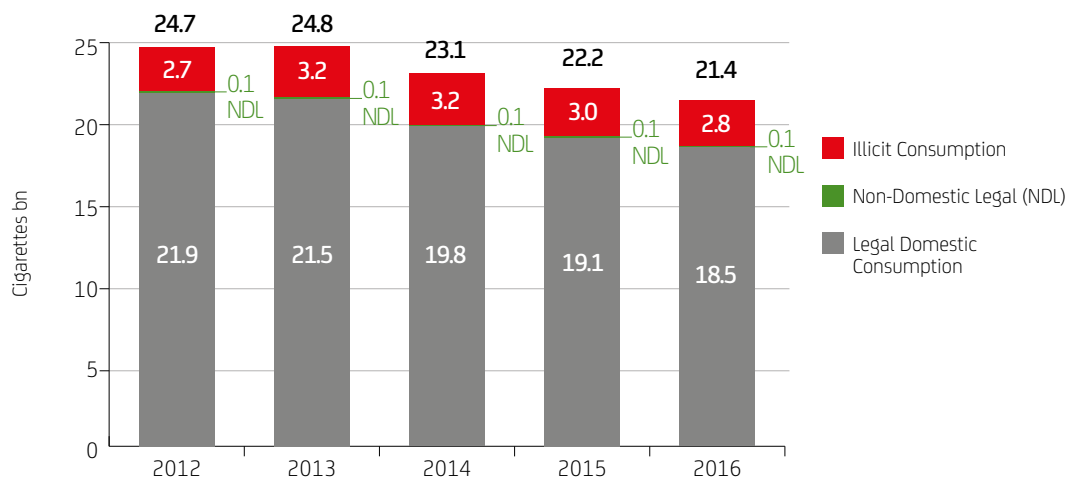
Australia: Composition of cigarette consumption (% of Total Consumption)¹



Source: Oxford Economics

¹Cigarettes and RYO equivalent

Australia: Composition of cigarette consumption (number of cigarettes)²



Source: Oxford Economics

²Cigarettes and RYO equivalent

Australia: Government Finances

- Australia operates a single-tier unit-specific Excise Tax structure with additional biannual increases linked to average earnings (the average weekly ordinary time earnings, or AWOTE index).
- In November 2013, the federal government announced that it would proceed with a series of four annual 12.5% increases in excise duty on tobacco products. The last of the scheduled increases was implemented in September 2016.
- In September 2016, the Excise Tariff Amendment (Tobacco) Act 2016 was approved, which will lead to four more annual increases at the same rate, covering the period to 2020.
- In May 2017, the Excise Tariff Amendment (Tobacco Duty Harmonisation) Bill 2017 was introduced, which aims at better aligning the tax treatment of manufactured cigarettes and RYO products by adjusting the assumptions behind the tobacco content per stick for the purposes of applying the “excise-equivalent customs duty rate” from 0.8g to 0.7g. The changes will be phased in over the four-year period to 2020.
- Australia also levies a GST of 10% on the retail price for tobacco products.
- Actual revenues from excise on tobacco amounted to AUD 9.9 billion (USD 7.2 billion) in the fiscal year 2015/16, rising by 12.5% in comparison with fiscal year 2014/15. This is despite a 3.1% decline in Legal Domestic Sales realised over the same period, with the higher Excise Tax rate more than offsetting the decline in legal sales.
- Actual revenues from excise duties on tobacco have increased every year since the first Asia Illicit Tobacco Indicator Report.
- The impact of rising Excise Tax on tobacco is also reflected in the estimated Tax Loss over the same period, which increased by 17.9% in 2015/16. Higher Excise Taxes are offsetting the impact on estimated Tax Loss from the estimated decline in the volume of Illicit Consumption over the same period.
- The estimated Excise Tax Loss as a share of total potential Excise Tax revenues rose to 14.3% in fiscal year 2015/16, an increase of 0.8pp from 2014/15. However, since the volume of Illicit Consumption has continued to fall, this is driven by a more pronounced rise in estimated lost excise revenues compared with the rise in actual excise revenues in 2015/16 (+20.6% vs +12.5% respectively).

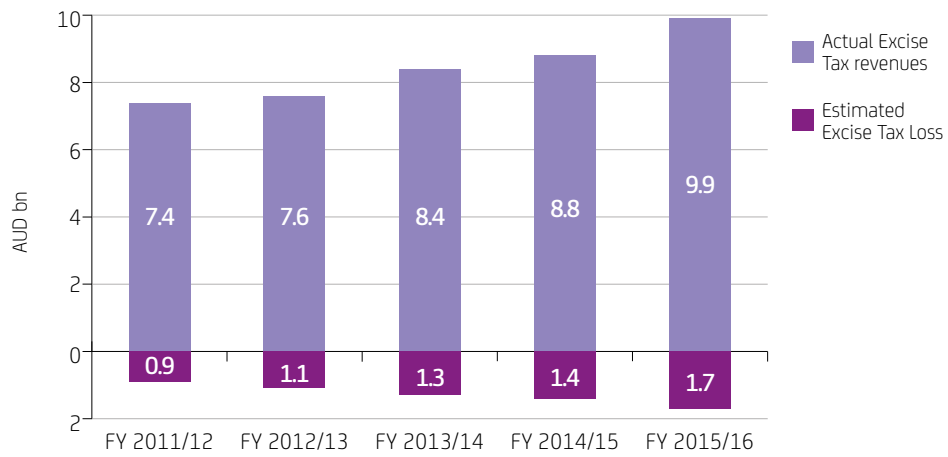
Australia: Actual government revenues and estimated Tax Loss¹

	2011-12 fiscal year		2012-13 fiscal year		2013-14 fiscal year		2014-15 fiscal year		2015-16 fiscal year		% change in local currency 2014/15-2015/16
	AUD bn	USD bn	AUD bn	USD bn	AUD bn	USD bn	AUD bn	USD bn	AUD bn	USD bn	
Actual revenue from excise duties on tobacco	7.4	7.6	7.6	7.0	8.4	7.7	8.8	7.4	9.9	7.2	12.5%
Estimated number of illicit cigarettes purchased (cigarettes bn)	0.8		2.0		1.7		1.4		1.1		-18.4%
Estimated volume of illicit loose tobacco (Chop-chop) purchased (cigarettes equivalent bn)	1.8		1.3		1.8		1.6		1.6		0.7%
Estimated Tax Loss from Illicit Consumption	1.1	1.1	1.3	1.2	1.5	1.4	1.6	1.4	1.9	1.4	17.9%
Lost excise revenue	0.9	0.9	1.1	1.1	1.3	1.2	1.4	1.2	1.7	1.2	20.6%
Lost GST revenue	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	2.6%
Excise Tax Loss as % of potential total Excise Tax revenues	10.8%		13.1%		13.7%		13.5%		14.3%		

Source: Australian Treasury Department, Australian Tax Office, and Oxford Economics based on PM data

¹Estimated number of illicit cigarettes purchased adjusted for fiscal year, which runs from July to June. Includes loose tobacco. A conversion rate of 0.8 grams per cigarette was applied to turn weight into cigarette equivalent, based on rates applied by the Australian Taxation Office.

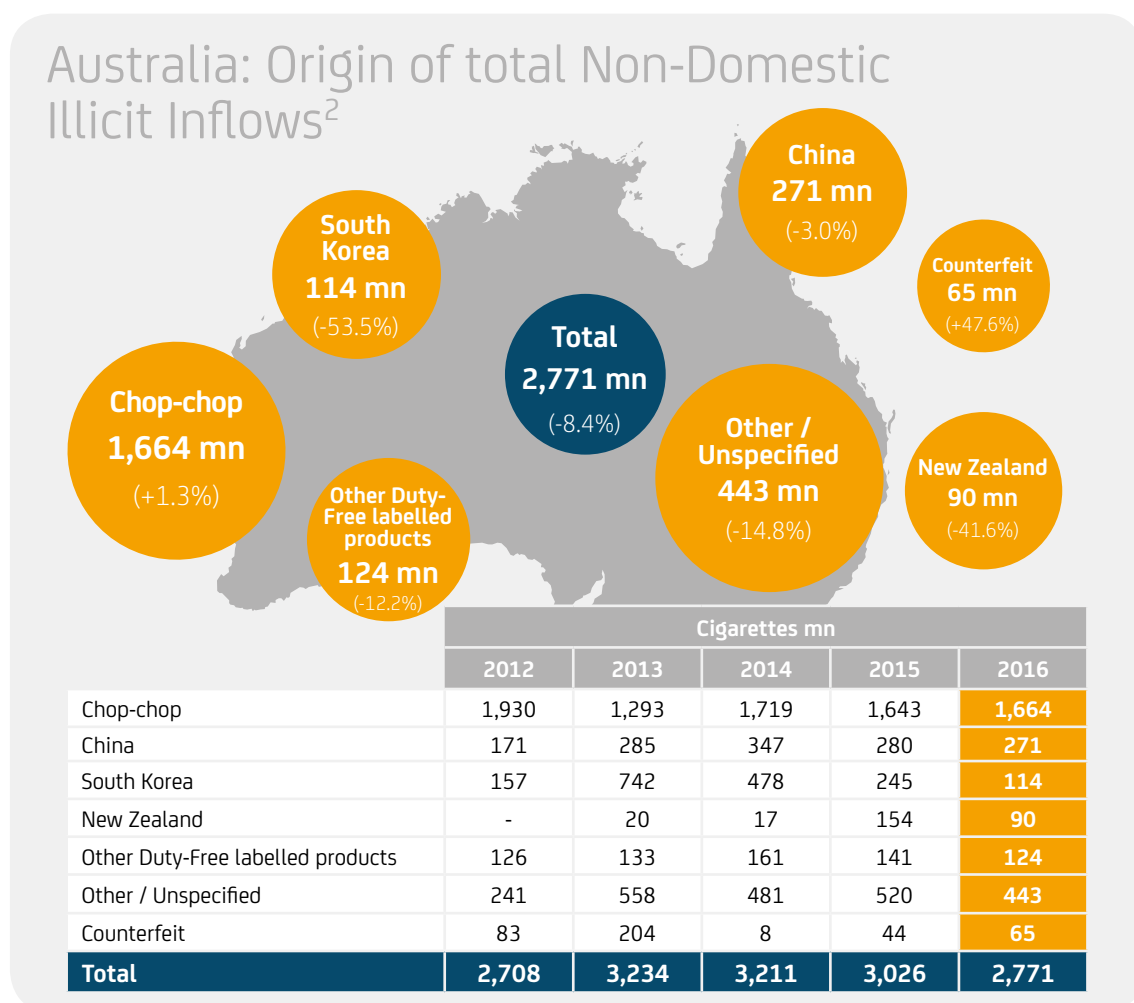
Australia: Actual government revenues and estimated Excise Tax Loss



Source: Australian Treasury Department, Australian Taxation Office, and Oxford Economics based on PM data

Australia: Trade Flows

- Non-Domestic Illicit Inflows, including Chop-chop, fell by 8.4% in 2016. This fall was primarily driven by lower Inflows from South Korea and New Zealand, which fell by 53.5% and 41.6% respectively. However, Inflows from China and other markets also fell, albeit by much more modest amounts, equivalent to 3.0% and 12.2% respectively. By contrast, the volume of Chop-chop consumed in 2016 edged up by 1.3%.¹
- At 2.8 billion cigarettes (including Chop-chop cigarette equivalents), Non-Domestic Illicit Consumption has now fallen for three consecutive years. Chop-chop accounted for 60% of total Non-Domestic Illicit Consumption in 2016, up from 54.3% in 2015. This reflects the relatively stable level of Chop-chop volumes and falling Inflows of illicit cigarettes.
- The sharp fall in Inflows from South Korea means that this market now accounts for 4.1% of total Non-Domestic Illicit Consumption in Australia, down from 8.1% the previous year. By comparison, most other categories of Non-Domestic Illicit Consumption were relatively stable in terms of the share in Total Consumption. Counterfeit cigarettes have increased from a negligible share to 2.4% in the past couple of years.
- Outflows of duty-paid cigarettes to other markets covered by this Report are estimated to be very low given the higher prices in Australia than most other markets. The exception is New Zealand, where 64 million cigarettes from Australia were identified in 2016.

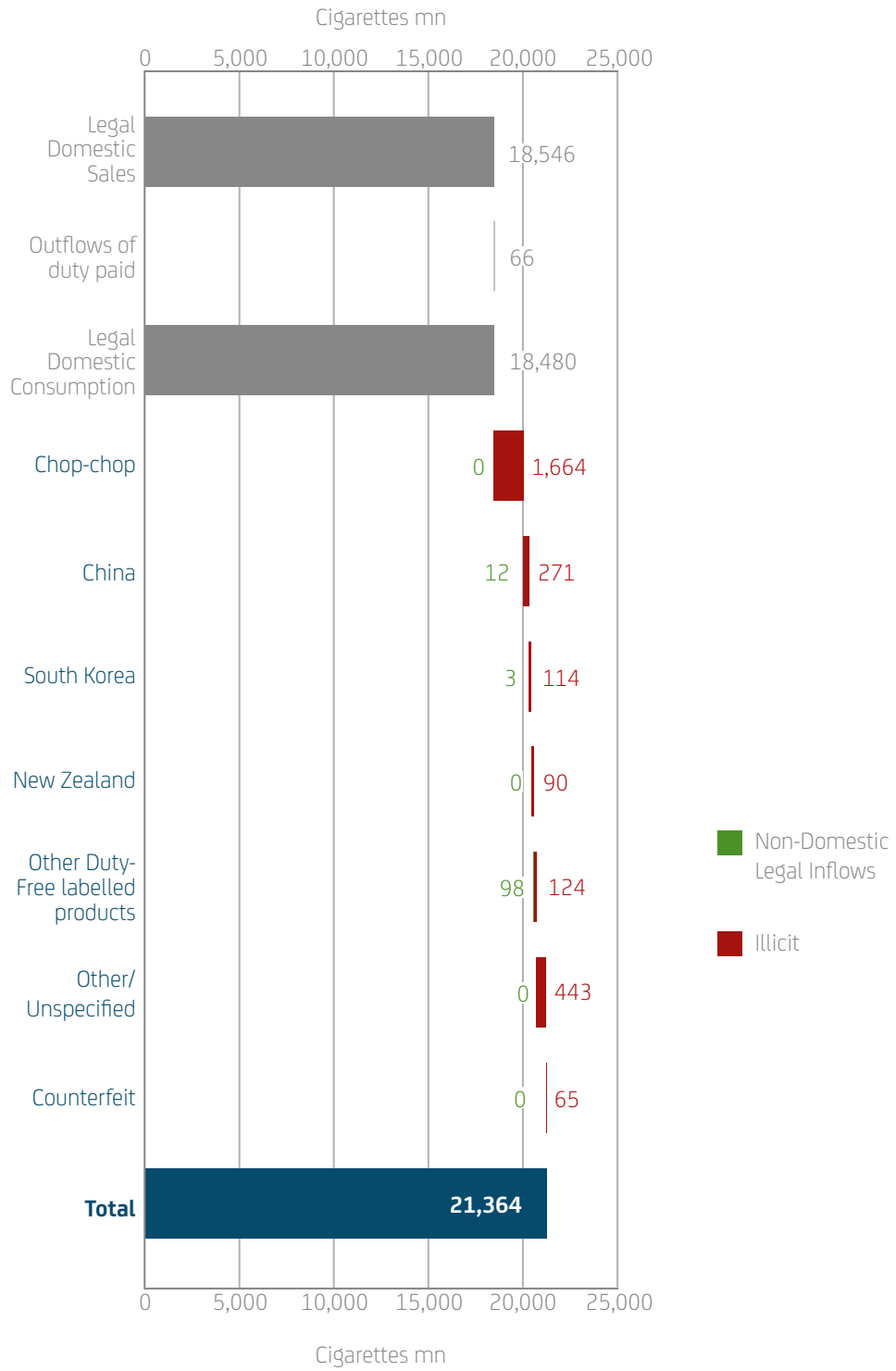


Source: IT Flows Model and Oxford Economics.

¹It is recognised that Chop-chop originates from both Non-Domestic and Domestic home-grown sources; however it is not possible to separate the two, and therefore for the purposes of this Report we consider all Chop-chop volumes to be of Non-Domestic origin.

²Including Chop-chop. Figures in brackets reflect % changes from 2014.

Australia: Consumption breakdown 2016

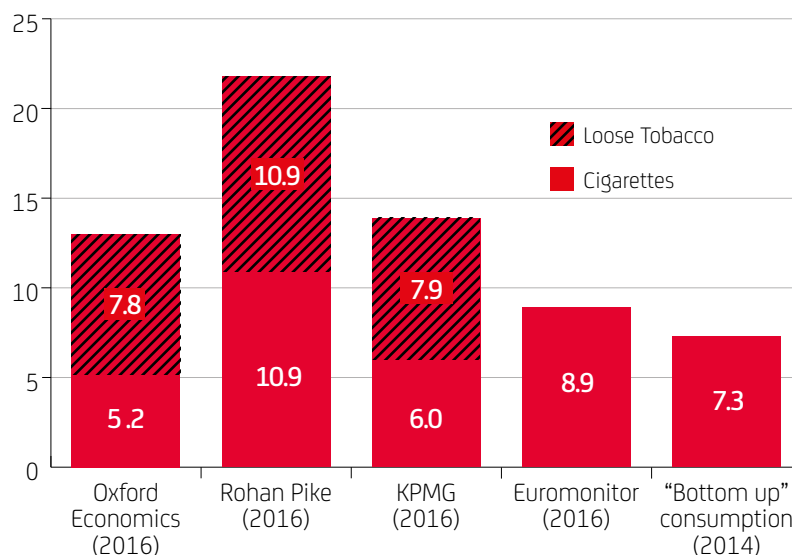


Source: IT Flows Model and Oxford Economics

Australia: Other estimates

Source	Comment
Comparing consumption estimates with LDC ("bottom up" approach)	Using data on average annual cigarette consumption per adult, plus UN population data, a "bottom up" estimate of cigarette consumption can be made which can then be compared with LDC. This approach yields an estimate for the Illicit Incidence of 7.3%, or around 1.3 billion cigarettes (based on 2014 LDC). The source for annual cigarette consumption per adult (age 15 and above) is Euromonitor (available via www.tobaccoatlas.org).
KPMG, Illicit tobacco in Australia, 2016 Full Year Report, March 2017. Retrieved via https://home.kpmg.com/uk/en/home/insights/2017/04/illicit-tobacco-in-australia-2016.html	Analysis by KPMG of a survey of consumers suggests an Illicit Incidence of 13.9% of Total Consumption in 2016.
Euromonitor Passport, 2017	Euromonitor estimates an Illicit Incidence of 8.9% in 2016. The methodology, sampling, and coverage are unknown, so it is difficult to assess the robustness of this estimate.
Parliamentary Joint Committee Inquiry into Illicit Tobacco, submission by Rohan Pike, former Superintendent of the Fraud and Anti-Corruption Division of the Australian Federal Police and head of the ABF Tobacco Strike Team. Retrieved via http://www.aph.gov.au/DocumentStore.ashx?id=0c1314f4-1cbf-4e69-ac6b-4b86fdeedf35&subId=462367	Drawing conclusions from a variety of sources, Rohan Pike estimates the size of the illicit market to be the equivalent of 21.8% of Total Consumption in 2016 (cigarettes and loose leaf tobacco only). ¹ This is equivalent to around 5 billion cigarette equivalents, resulting in a Tax Loss of nearly AUD 3.1 billion. Note that this excludes an additional AUD 763 million of revenue losses resulting from Illicit Consumption of molasses tobacco (which is excluded from the analysis in this Report). When including this, the total estimated Tax Loss is AUD 3.8 billion, which represents 28.2% of the total market based on revenues.
Illicit trade of tobacco in Australia. A report prepared by Deloitte for British American Tobacco Australia Limited, Philip Morris Limited, and Imperial Tobacco Australia Limited. A critique prepared by Quit Victoria, Cancer Council Victoria, March 2011 (updated 18 November 2011). Retrieved via http://www.cancervic.org.au/downloads/plainfacts/CommtsDeloitte18_11_11_2_.pdf	An estimate by Quit Victoria based on the 2010 National Drug Strategy Household Survey suggests an Illicit Incidence of around 2–3%. However, possible weaknesses of this survey include the generation of its results from a "drop and collect" self-completed questionnaire (risking unrepresentativeness) and the fact that its definition of illicit loose tobacco may be insufficiently broad.

Australia: Alternative estimates of Illicit Consumption



¹A conversion rate of 0.8 grams per cigarette was applied to turn loose tobacco weight into cigarette equivalent, based on rates applied by the Australian Taxation Office.

Australia: Data Sources

	Primary source	Calculation	Comments
Legal Domestic Sales (LDS)	Actual volume of tobacco clearances recorded by the Australian Taxation Office and Border Protection Service (Customs), sourced from the Australian Treasury Department.	—	Includes legal Other Tobacco Products sales.
Outflows of domestic duty-paid cigarettes	Empty Pack Survey data in other markets included in this Report.	Empty Pack Survey data in other markets used to identify the presence of packs bearing Australian market-specific labelling (e.g. health warnings, tax stamps etc.).	Outflows of domestic duty-paid cigarettes to other markets are estimated at around 66 million cigarettes, with the majority going to New Zealand.
Legal Domestic Consumption (LDC)	—	Legal Domestic Sales minus Outflows of legal sales.	Outflows of duty-paid cigarettes refer only to Outflows to other markets included in this Report.
Total Non-Domestic Inflows (ND)	—	Sum of Non-Domestic Legal and Non-Domestic Illicit.	—
Non-Domestic Legal (NDL)	—	Estimated using passenger data, smoking rates, and passenger duty-free personal import allowance.	Maximum theoretical amount an individual can carry across a border. Passenger data from the Australian Bureau of Statistics.
Non-Domestic Illicit	Empty Pack Surveys and KPMG.	Based on Empty Pack Surveys, KPMG data, and OE estimates.	Estimates derived from the average of Empty Pack Surveys conducted in 2016 Q2 and 2016 Q4. An estimate for loose tobacco (Chop-chop) has been added based on the study by KPMG (2017). See Report methodology for more details.
Domestic Illicit	—	Zero under-declaration of domestically produced cigarettes.	There is assumed to be no under-declaration of domestically produced cigarettes.
Total Illicit Consumption	—	Sum of Non-Domestic Illicit and Domestic Illicit.	—
Total Consumption	—	Legal Domestic Sales minus Outflows of domestic duty-paid cigarettes, plus estimated Non-Domestic Legal consumption, plus estimated Illicit Consumption.	The IT Flows Model estimate of consumption is 21.4 billion cigarettes for 2016.
Total Tax Loss	—	Total Illicit Consumption multiplied by the weighted average tax rates (Excise Tax and GST).	See Report methodology for more details.

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