Top Risks to Australian Business 2024–25

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Executive summary

This report sets out some of the key geopolitical risk scenarios for Australian businesses. It provides guidance for business leaders to prepare both strategically and operationally for an increasingly volatile future. Resilience doesn't mean predicting the future, it means knowing how to adapt.

Geopolitical volatility

Australian businesses are navigating a more complex geopolitical environment than at any time in living memory. Structural changes to the international system, rising global mistrust, rapid technological advances, and the dramatic impacts of the climate crisis are driving fundamental changes to the risk landscape.[1] These changes represent a complex range of interconnected challenges and opportunities for global and Australian organisations alike.

In 2022, when we released the previous edition of Australia's Top Risks, we reported that the geopolitical risk environment was becoming increasingly fluid.[2] Two years on, fluidity has morphed into volatility, and we are now witnessing clear examples of geopolitical fracturing and fragmentation. National security concerns and geopolitical logic are driving major policy decisions about foreign investment, international alliances and advanced technology. Economic cycles and trade flows are no longer following familiar patterns. Conflict has broken out in multiple regions, and experts predict there is more to come. Companies can no longer wait out disruptions and expect things to go back to 'normal'. Disruption is the new normal.

Until recently, many companies felt that geopolitics was not particularly relevant to them.[3] However, the events of the past few years are now shaking this sense of comfort. According to a major recent survey of business leaders worldwide, 93 percent of international firms suffered losses linked to political instability in 2023, compared to just 35 percent in 2020.[4] In the 2023 Global KPMG CEO Outlook, business leaders around the world rated geopolitical risk as their number one concern.[5] Given the interconnectivity of geopolitical risk, these geopolitical concerns matter just as much to Australian business leaders as their global counterparts.

Three risk scenarios present major challenges to Australian businesses

Geopolitical risks tend to be highly interconnected and contagious. As such, they should not be considered in isolation. This report identifies and analyses three risk scenarios of particular importance to the Australian business community, each of which is made up of three interconnected and mutually reinforcing risks.

Scenario 1. Crisis hits, we're not prepared.

This scenario shows interconnections between the risks of climate change and biodiversity loss, energy and food security, and the imbalance between long-term and short-term strategy.[6] The scenario suggests that we are unlikely to be sufficiently prepared to cope with the broad-ranging volatility that lies ahead.

Scenario 2. The death of truth and trust.

The risks of AI governance, a decline in trust of public institutions, and misinformation and disinformation create a scenario where trust becomes a scarce commodity.[7] It's almost impossible for us to know what the truth really is, but at the same time, there are higher expectations on businesses to be trustworthy actors.

Scenario 3. Walls, moats, and stranger danger.

This scenario shows the contagion effects between the risks of deglobalisation, Australian national security, and US politics and policy. When these risk factors come together, it results in a world of increased competition, where countries turn inwards and away from cooperation, and instead, build connections with those they feel they can trust.

The common thread – connected challenges, fragmented solutions

There is a clear thread running through the three scenarios. Responding to these interlinked and inherently global challenges will require an unprecedented degree of international collaboration. However, the geopolitical environment of competition and mistrust is making countries less inclined to cooperate, and more inclined to band together into like-minded blocs. The result is likely to be a patchwork of fragmented policy solutions and business responses that vary widely between countries. Companies will face different operating environments across the globe, including regulations, supply chains, and incentives. This will deliver further complexity and risk.

Implications and key questions for Australian businesses

Sectoral differences

The risk environment explored in this report will affect all Australian industries, but impacts will be uneven. Some sectors are particularly exposed to certain risk scenarios, and the scenarios may also create opportunities if geopolitical risk management strategies are put in place. This report spotlights key Australian industries and analyses the geopolitical risk exposure outlook for each.

- Energy and resources
- Defence industries
- Agribusiness
- Financial services
- Consumer and retail
- Advanced manufacturing

Diversification and strategic self-sufficiency

Geopolitical volatility means that global trade and investment flows are being disrupted by countries' efforts to become more self-sufficient and reduce their dependence on others. Businesses may no longer be able to rely on their traditional sources of goods and/or capital. They will need to adapt, including by diversifying their supply chains or by onshoring/friendshoring operations, which can be costly and complex.

Changing domestic regulations and compliance

As geopolitical competition prompts the Australian Government to strategically regulate businesses that operate in critical parts of the economy – and as the definition of 'critical' becomes broader – changing regulations will be an increasing challenge for more and more Australian companies. This will be a pattern that also plays out in other countries around the world, so Australian businesses will need to be able to navigate regulatory changes both at home and abroad.

Trust and reputation

Declining trust in public institutions and leaders is translating into increased expectations of businesses. Because growth requires trust, companies will need to work harder to build and maintain the public's trust by ensuring transparency, demonstrating ethical conduct, and taking responsibility for the conduct of suppliers further up the supply chain than ever before. The challenge will be in ensuring that building trust with one section of the community does not undermine trust elsewhere.

Contents

This report is an Australia-focused version of *Top Risks 2024: The Bottom Line for Business*, authored by KPMG Global, based on our global alliance partner Eurasia Group's annual Top Risks report.

To create a dynamic risk analysis specific to the Australian business context, KPMG Australia surveyed experts both from within and external to the firm to develop the top Australia-specific business risks. These risks were then used as the basis for a Dynamic Risk Assessment (DRA) survey. DRA is a risk assessment tool that helps organisations make better-informed decisions by understanding what can happen when individual risks combine and interact.

Dynamic Risk Assessment

Understanding risk in a geopolitically fragmented world

We have had tension and conflict for as long as we have had humans. The necessity to manage the risks arising from tension and conflict is, in itself, nothing new. However, something is changing.

Risks are becoming increasingly interconnected – when one risk eventuates it can trigger multiple others, which in turn connect to further risks.

Over the past decade, the global risk environment has become synergistic. When geopolitical risks occur together, they create a whole that is greater than the sum of its parts, with impacts that are more severe and long-lasting. To reflect this synergistic risk context, in 2023 the World Economic Forum coined the term 'polycrisis'.[8]

The complex relationships among risks matter. Multiple and shifting points of stress on every element of business, from supply chains to workforces to digital security, and everything in between, mean that a new approach for navigating rapidly growing volatility is required.

KPMG's Dynamic Risk Assessment (DRA) investigates the structure of an entire risk system to understand the connections between risks and the speed at which risks materialise, as well as their likelihood and potential severity. This view looks beyond conventional depictions of risk – typically based on the two dimensions of likelihood and severity – by taking into consideration risk interconnectedness and the velocity with which risks create impacts. DRA modelling allows us to identify where risks could trigger contagion with other risks, or form critical clusters, understood as 'scenarios'.

Risk scenarios

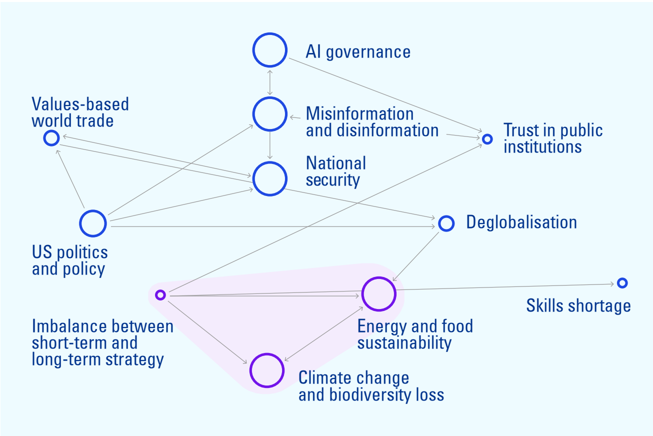
Clusters of strongly interconnected reciprocal risks mean that if any one risk eventuated, it would likely create a domino effect, setting off the other risks in the cluster. The cumulative impact of these compounding risk events creates a risk scenario. It is essential that Australian businesses understand and are prepared for these synergistic 'polycrisis' risk events.[9]

This paper explores three key risk scenarios facing Australian businesses that were identified by a diverse group of experts through a Dynamic Risk Assessment undertaken in April 2024.

Risk cluster scenarios

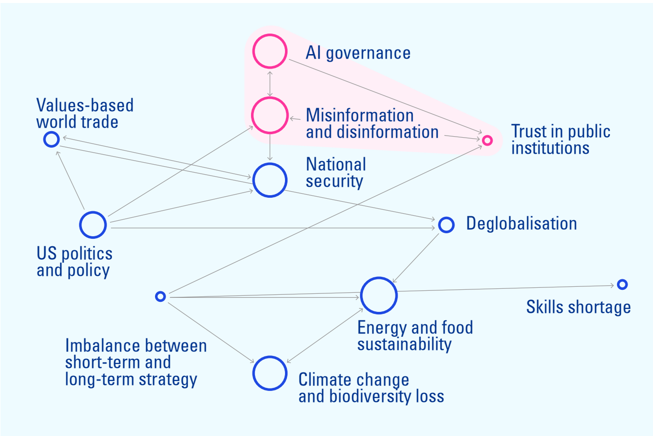
Three major risk cluster scenarios with implications for Australian businesses

Scenario 1: Crisis hits, we're not prepared



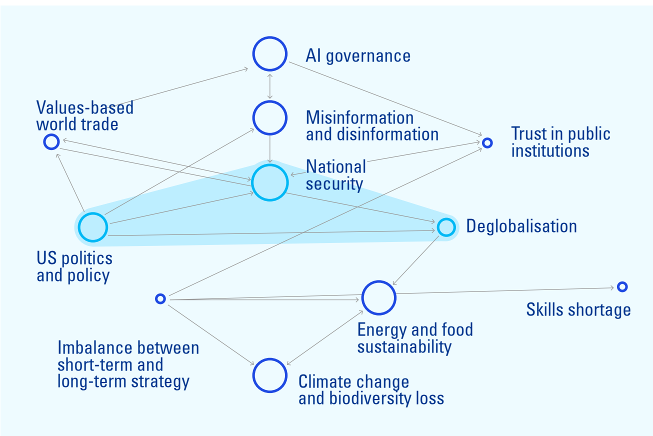
This scenario shows reciprocity among the risks of climate change and biodiversity loss, energy and food security, and the imbalance between long-term and short-term strategy. When these three risks are combined, it means that we are unlikely to be sufficiently prepared to cope with the broad-ranging volatility that lies ahead.

Scenario 2: The death of truth and trust



This scenario reflects that at the same time that trust in public institutions is eroding, keeping up with advances in artificial intelligence (AI) and the proliferation of disinformation is creating novel challenges. The combination of these risks means it is increasingly difficult for anyone to know what is true, but at the same time, there are increasing expectations on businesses to be trustworthy.

Scenario 3: Walls, moats, and stranger danger



This scenario shows how increasing concerns about national security, developments in US politics and policy, and deglobalisation add up to a world in which countries are turning inwards and away from cooperating with each other. Instead, to protect themselves from what they see as an increasingly hostile world, they try to reduce interdependencies by onshoring and friendshoring.

Please refer to page 37 for a list of definitions of the risks included in the risk diagram.

SCENARIO 1: Crisis hits, we're not prepared

This scenario shows interconnections among the risks of climate change and biodiversity loss, energy and food security, and the imbalance between long-term and short-term strategy.

Within Australia and around the world, policymakers and business leaders are struggling with balancing short-term challenges, like inflation, against looming threats that require long-term strategies and investments, like climate change. However, this scenario shows that short-term planning cannot be at the expense of long-term horizons – and long-term needs to be 10 years plus. Geopolitical volatility means that all kinds of disruptions and crises are going to hit more often and harder, including those driven by climate change and biodiversity loss – but are we ready?

Currently, in some sectors, some Australian businesses set strategies based on relatively short time horizons, looking at three to five years as 'long-term'. As such, they tend to focus on concerns like workforce availability, supply disruptions, or inflation rates. Valid as these challenges are, in this volatile geopolitical climate, these issues can be understood as symptoms, rather than the disease itself. These time horizons are also inadequate for managing longer term risks, like the two environmental challenges in this risk scenario.

Scenario 1, Risk 1: Climate change and biodiversity loss

Neither the impacts of climate change nor the ability to adapt to them are uniform across the globe. Certain regions are particularly vulnerable to climate change, which will exacerbate existing inequalities and tensions. The Asia-Pacific region is a key example. The United Nations (UN) describes climate change as posing an 'existential threat' to the region because of its geography, population distribution, and socio-economic conditions.[10] As nations scramble to adapt to shifting growing conditions for their agriculture sectors and more frequent extreme weather events, migration patterns change, inducing stress on social systems and potentially creating tension and conflict. For the Asia-Pacific region, the implications of climate change could be disastrous.[11]

According to the UN, the strongest natural defence against climate change is biodiversity. It is also a critical factor for food and water security. In addition, the World Bank observes that over half of global economic value is generated in industries that rely on biodiversity.[12] However, despite all these positive benefits, the planet's biodiversity is being rapidly eroded. Ironically, the main cause of the loss of the biodiversity that underpins our food security is humans' use of land for food production.[13] According to a report by the United Nations Environment Program (UNEP) and Chatham House, global agriculture accounts for 86 percent of species risk.[14]

The long-term challenges of climate change and biodiversity loss and energy and food security are enormous on their own, but they also act to trigger and accelerate each other. The geopolitical implications of this scenario – the struggle for power, the competition for increasingly scarce resources, the mass movement of people seeking sanctuary from uninhabitable climates – are profound and will lead to increased tensions and conflicts around the world. This is certainly the case in our own region, where research from the Australian Strategic Policy Institute (ASPI) finds that the geopolitics of climate change is set to create extremely destabilising security challenges in the Indo-Pacific region within the next decade.[15]

Scenario 1, Risk 2: Energy and food security

Energy and food security should be seen as critical concerns for Australian businesses in an era marked by shifting power balances and a warming planet. As the impacts of climate change intensify, experts predict that tensions and conflict over energy and food security will dramatically increase, including in Australia's near region.[16]

Energy security is a fundamental aspect of national and global stability. However, global energy is undergoing a transformation as nations seek to transition from fossil fuels to renewable energy sources. Countries rich in hydrocarbons face the challenge of diversifying their economies, while those leading in green technologies aim to maximise their assets for their own national security as well as to increase their global weight and influence. In a geopolitically volatile world where national security matters more than ever and energy security underpins national security, energy policy can be weaponised and used as a tool for competition.[17] Where countries cannot develop their own onshore energy supplies, they will increasingly look to secure and reliable providers, and will be more likely to pay a premium for that certainty. The same is true for the components necessary for green energy, like critical minerals. Australian businesses must navigate this complex terrain where energy is profoundly political.

According to the World Bank, at the end of 2023, 45 percent of the world's population was food insecure. Domestic food inflation remains high in many low- and middle-income countries. In real terms, food price inflation has exceeded overall inflation in almost half the countries of the world.[18] Global rates of hunger and malnutrition are on the rise, and look set to continue to increase.[19] Like energy security, food security is a critical element of stability, at multiple levels – individual, community, national and global. Food insecurity can lead to nutritionally inadequate diets, causing health concerns across populations. Competition for scarce resources undermines social cohesion and drives political fragmentation and instability. Food insecurity also contributes to economic volatility. Ultimately, extended periods of food insecurity can lead to humanitarian crises, conflict and violence, and mass migration, both within and across borders, as people move in search of better food availability. The Asia-Pacific region accounts for half of the world's severe food insecurity, with around 370 million undernourished people.[20] Climate change exacerbates food security issues, threatening agricultural yields and leading to potential conflicts over arable land and freshwater resources. Research projecting a 1.5°C increase in global temperatures argues that by 2035, the impacts of climate change on food production in the Indo-Pacific region will be severe, with widespread food insecurity, mass migration, and instability.[21]

In an era of increasing geopolitical volatility, and with the climate crisis deepening, the risk of simultaneous shocks to both energy and food supplies could severely test the resilience of Australian businesses. As such, strategies that enhance sustainability, diversification of supply sources, and investments in innovation become not only environmentally and ethically imperative but also a fundamental business necessity for long-term viability and risk management.

Scenario 1, Risk 3: Imbalance between long-term and short-term strategy

Maintaining a balance between long-term and short-term strategy is essential for the sustainable success of any organisation. An overemphasis on short-term strategy and a neglect of future, long-term goals can hinder growth, lead to missed opportunities, and drive unsustainable practices. An insufficient focus on the short term can negatively impact operational efficiencies and hinder an organisation's ability to adapt to immediate challenges and crises.

At the global level, different lengths of political cycles can create real challenges in achieving collaboration on global issues. Politicians in Western democracies with three, four, or five-year electoral cycles need to be highly conscious of public accountability and their own political survival. This can lead to a focus on immediate economic impacts and a range of re-election pressures. This focus can lead to a tendency to prioritise reactive agendas over long-term objectives. Countries with longer electoral cycles, a dominant incumbent party, or a non-democratic political system are arguably more able to set and stick to long-term strategies – although this is not to say they are immune from short-term challenges and pressure from their own domestic vested interests.

We can see this tension between long-term and short-term approaches playing out when it comes to climate change policy. Domestic electoral imperatives can cause climate policy to shift, sometimes dramatically, from one leadership cycle to the next. This is particularly the case in times of economic downturn where immediate cost-of-living pressures become a real issue for large parts of the population, pushing longer-term climate policy to the sidelines. Likewise, increasing social and political polarisation can erode the 'social licence' for elected politicians to drive ambitious climate policies. While countries without this electoral cycle pressure certainly still have their own domestic imperatives to meet, the political calculations behind public policymaking are quite different.

In the business realm, prioritising short-term gains can lead to a focus on immediate financial performance, potentially at the expense of innovation, brand equity, and investment in human capital. Such an approach might appeal to some stakeholders in the short term, but can erode an organisation's competitive edge and adaptive capacity over a longer time frame. Firms that over-prioritise short-term strategies may find themselves ill-prepared for responding to symptoms of geopolitical competition and mistrust. For example, rapid and substantive policy changes and ongoing trade wars would require long-term strategic planning and diversified risk management to navigate. By the same token, companies that are too focused on the long-term may lack the agility to swiftly respond to immediate geopolitical crises, such as political unrest, trade restrictions, or a sudden deterioration in diplomatic relations. This misalignment can jeopardise supply chain integrity, create financial instabilities, and can even tarnish a company's reputation, making it less attractive to investors who are increasingly aware of geopolitical sensitivities.

CASE STUDY

A question of just-in-time or just-in-case?

COVID-19 shocked the entire global system. It was the most widespread viral outbreak the world had seen in more than a century.[22] Many businesses that had focused on maximising efficiencies with a 'just-in-time' approach, assuming global supply chains would meet their needs, were caught short.[23] Global shortages and disruptions to supply chains clearly exposed the limitations of the just-in-time model.

The just-in-time model, developed by Toyota after World War II with the aim of catching up to the American auto industry, was an approach that suited the times.[24] It works very well to create high-quality products at low costs when conditions are stable and when supply chains are reliable. By the early 2000s, almost every production facility around the world had moved towards a just-in-time model to cut costs. As another cost-saving move, companies also developed long and elaborate supply chains, sourcing parts from wherever in the world made them most efficiently and at the best prices.[25] This complicated and thinly stretched approach was very fragile, but worked effectively when global circumstances were dependable and predictable.

Times have, of course, changed. Disruptions to supply chains during the COVID pandemic jolted many businesses to seriously reconsider the high-efficiency just-in-time model and pivot 'back' instead towards 'just-in-case' to rebalance efficiency and resilience.[26] In some sectors and for some companies, building resilience to weather uncertainty and instability and the disruptions they cause to supply chains became seen as the preferred way to maintain business continuity.[27]

However, five years after the COVID-19 virus was first identified, how much has the business community changed its approach? Commentary suggests that many businesses feel that it's 'time to return to just-in-time'.[28]

The reinvigoration of lean inventories and complex supply chains leads to the obvious question – does this approach suit the times we are in now? Will it suit the future?

Australian businesses should ensure they are not approaching their inventory management based on circumstances that no longer hold true. There are many other potential supply chain disruptions likely to become more common in the future, including natural disasters, conflicts, climate change impacts on infrastructure, and geopolitical trade restrictions.

All Australian businesses need to ensure they are taking a proactive and clear-sighted approach to business strategy and operations. Are you ready for the next pandemic? Are your supply chains prepared for increasing and rapidly shifting geopolitical tensions, or will the next upset expose weaknesses in vulnerable logistics chains?

Australia, like many other countries, faces the challenge of having to balance short-term economic growth and employment concerns with longer-term issues of global competitiveness and future prosperity.[29] For example, previous thought leadership from KPMG shows that as Australia decarbonises, how the country manages its energy transition will have serious consequences for its medium- and long-term prosperity and wellbeing.[30] These decisions will impact national power and wealth, connections and alliances with other nation-states, and how successfully Australia is able to navigate future tensions and conflicts.

Different approaches to time horizons at the national level can lead to a fragmented international policy landscape, where businesses are compelled to straddle increasingly uneven regulatory and policy environments. Companies operating across these varied regimes must exhibit exceptional strategic agility, ready to capitalise on the short-term advantages provided by some governments while aligning with the stability and future orientation of others. The capability to adapt will allow businesses to better maintain competitive advantage, manage risk, and drive business growth in a politically diverse world.

The conundrum is that overdoing either side of the short-term/long-term equation will run a high risk of causing major problems in the other.[31] As this scenario underlines, when it comes to risks like climate change and biodiversity loss, and energy and food security, we cannot afford to focus on the short-term at the expense of the long-term.

Are we preparing now for when the next crisis hits, whether in two years, five years, or ten years (or all three)?

Key questions for Australian business leaders

1. Are you considering how to balance immediate financial pressures and operational demands with the need to invest in long-term enterprise value?
2. Can you readily adapt to regulatory changes? Shifting global norms and regulations surrounding climate change mitigation efforts and sustainability practices may introduce regulatory uncertainty for Australian businesses. Companies must consider both short-term and long-term political developments in their strategies.
3. Are you assessing how your business can build and maintain resilient supply chains that can withstand energy and food security challenges as well as geopolitical disruptions?
4. Are you thinking about how to integrate sustainable practices into your business model to mitigate the risks associated with climate change and biodiversity loss while ensuring long-term profitability?

SCENARIO 2: The death of truth and trust

The risks of AI governance, a decline in trust of public institutions, and misinformation and disinformation create a scenario where trust becomes a scarce commodity and it's almost impossible for us to know what the truth really is. At the same time, businesses are expected to take on more responsibility for trustworthiness.

Is that really the Prime Minister speaking? Is that really your mother on the phone asking you to transfer funds? Is the local pizza shop actually a front for an international crime ring?[32] How do we know? The less truth and trust, the more instability. This scenario makes it clear that we must be extremely vigilant – not only in ensuring we actually know what we think we know, but also about navigating the instability and disruption that comes from a world where trust and truth are scarce.

It also raises the question of whether the business community can or should take on a greater role in rebuilding the trust that is being so rapidly eroded.

It is hard to imagine stability in a world experiencing almost inconceivably life-changing technological advances but without agreed governance to manage them. Add in growing mistrust of those very regulators and the proliferation of misinformation and disinformation, and the outlook seems like chaos.

Scenario 2, Risk 1: AI governance

The impact of emerging technology like artificial intelligence (AI) on human life and the planet has been compared to the Industrial Revolution, but perhaps even that is an understatement. There is considerable optimism about the positive potential of new technologies, but that optimism depends on a very big 'if' – *'if'* we manage it well. It's a big *'if'* because while emerging technologies could solve many of our pressing problems, doing so requires global collaboration on norms and governance. However, geopolitical competition means many aspects of emerging tech are also key tools in nation-states' struggles to gain and maintain power and influence. For an exploration of the challenges of building trust in AI governance, see this recent KPMG-University of QLD report.[33]

'Gaps in AI governance will become evident as regulatory efforts falter, tech companies remain largely unconstrained, and far more powerful AI models and tools spread beyond the control of governments.'[34]

AI is one example of an emerging technology that can be a powerful tool for the benefit of humanity, but also has the potential to do real harm if not effectively governed. Breakthroughs in AI are moving far more rapidly than our ability to govern them, and this gap will continue to grow.[35]

Getting the balance of AI governance right is difficult. On the one hand, to fulfil its potential, regulation should not stifle innovation and creative potential. On the other, a robust governance framework is necessary to ensure that AI tools and systems remain ethical, and controllable. Otherwise, there is risk of system failure and/or abuse, including from the misuse of data, algorithmic discrimination, and miscalculations in automated decision-making.

There have been national and international debates around how best to govern AI since at least 2016.[36] Data sovereignty is a key issue in cross-border contexts where differing norms and legal standards about data usage and protection come into conflict. This challenge becomes particularly fraught given the global nature of data flows, and the borderless operation of many tech entities. Accountability is another major issue – who is held responsible for AI decisions? Existing legal frameworks are ill-equipped to address how complex, autonomous systems can and should be held to account. While there are many existing initiatives, arguably, none of them is currently able to address the challenge of maximising the opportunities of AI, while identifying and minimising the risks.[37]

Another key challenge in AI governance, given its potential to influence the global power map, is who gets to set the rules and standards. Because AI is an expensive and complex technology, only a handful of technologically advanced nations have the capability to invest in it. At the same time, the potential for AI to be a tool of power means that the countries with the greatest will to pursue its rapid development are those competing with each other for pre-eminence. These two factors together create a real risk that governance models will be shaped to favour their interests, rather than the interests of the broader global community. A truly inclusive and globally beneficial AI governance framework will need to mitigate, not replicate and strengthen, power imbalances. This will be a profoundly challenging task given geopolitical competition and mistrust.

AI and geopolitical competition

Two decades ago, the United States was a (if not the) world leader in AI research. Since then, other major global actors have invested heavily in AI and made significant progress.[38] In 2017, China declared its ambitious goal of making the country 'the world's primary AI innovation centre' by 2030.[39] Australia also recognises the critical importance of artificial intelligence to national security (understood to include economic security), including AI as one of the technology priorities of the AUKUS agreement.

Scenario 2, Risk 2: Misinformation and disinformation

The increasing spread of misinformation and disinformation is exacerbating mistrust and discontent. Technological developments are enabling the proliferation of 'alternative facts' and creating the echo chambers in which increasingly extreme, hostile and paranoid views can become normalised as mainstream.[40] Algorithms designed to capture our attention and optimise engagement amplify the effect by serving us more news content that fits – rather than challenges – our existing preconceptions. Research shows that when an individual is exposed to social media echo chambers, they then tend to regard any expression of opposing viewpoints not as a discussion, but as an attack on their very identity.[41] The way social media can shape people's views is no accident – known as 'persuasive technology', social media algorithms are designed to modify behaviour by deliberately exploiting users' emotional and psychological responses.[42]

Don't believe everything you read

In May 2024, a poll found that 49 percent of Americans believed the S&P 500 stock market index was down for the year – although in fact it was up 9 percent, and, while unemployment was not far above its lowest point in 50 years, the same percentage believed the unemployment rate was at a 50-year high.[43] Believing in things that are so far removed from the truth suggests a society in which many individuals have constructed their own realities and don't – or won't or can't – see facts that don't fit.[44]

With disinformation driven by algorithms, media can become a tool of social and political polarisation. The echo chamber phenomenon further entrenches social polarisation.[45] Fake news – the proliferation of misinformation and disinformation – is not only a threat to social cohesion, but also to the legitimacy of institutions such as free and fair journalism and a transparent legal system.[46] People's mistrust of public institutions can and does drive support away from the centre, and towards populist political actors who trade on anger and disenfranchisement. With a rise in populism comes further disruption to domestic institutions like the rule of law, as well as international norms like openness, cooperation, and support for a multilateral rules-based order.

What is disinformation and misinformation?[47]

Misinformation is false information that is spread due to ignorance, or by error or mistake, without the intent to deceive.

Disinformation is false information knowingly designed to deliberately mislead and influence public opinion or obscure the truth for malicious or deceptive purposes.

How social media creates and promulgates information has profound consequences for our societies, our politics, our economies, and our environment. As with the governance of AI, questions around who should be responsible for the truthfulness of content on social media are complex. Should providers of digital spaces be held accountable for fact-checking and moderating content? Do such interventions impinge on the right to free speech and the open exchange of ideas, such that regulations could be co-opted by governments to suppress dissent or privilege certain narratives over others? The issue of how to ensure existing legal and regulatory frameworks are best able to address these issues is fraught.

Scenario 2, Risk 3: Plummeting trust in public institutions

Growing mistrust among citizens around the world in their political and public institutions creates its own instability, but also provides the basis for increasingly nationalist and inward-focused policymaking. Around the world, including in Australia,[48] citizen trust in public institutions like the bureaucracy, the rule of law, and the political system, is diminishing.[49] Trust in traditional news media is also declining. Younger generations increasingly trust social media sites as their preferred news source, rather than local or national news organisations.[50] At its simplest, this growing distrust makes resolving problems harder. Declining political trust undermines public confidence in public institutions like government to perform their core roles, including effective policymaking, policy implementation, and service delivery.[51]

The lack of trust arises because growing numbers of people around the world see their public institutions and public figures as corrupt, inefficient, promoting inequality, inadequately responsive to crises, and, critically, not accountable to the public they purport to serve – either deliberately or through mismanagement.[52] Rather, these individuals and institutions are understood as representing the interests of the status quo elite. Whether or not these criticisms are valid is beside the point. Perceptions drive beliefs, which in turn drive actions.

The 2024 French and UK elections show how lack of trust causes political fragmentation, drives people from the centre of politics towards 'anyone but the incumbent', and creates instability and unpredictability. The 2024 Edelman Trust Barometer notes that the UK is now among the least trusting countries in the world. France is also in the 'red zone' of extremely low trust.[53]

What is the difference between mistrust and distrust?

The words mistrust and distrust can technically be used interchangeably. As verbs, they both basically mean 'to be suspicious of' or 'to lack trust in', and their noun forms similarly mean 'suspicion' or 'a lack of trust'.

However, they do have different connotations. *Distrust* implies a lack of trust based on previous experience or knowledge. *Mistrust* implies a broader absence of confidence that doesn't necessarily stem from anything specific.

Australia is not immune to what has been described as the 'pandemic of mistrust'. In Australia in 2024, 52 percent of respondents reported that they trust political institutions, not high by any means, but up from 48 percent in 2023. This uninspiring figure reflects the broader trend of a 'hollowing out' at the centre of politics across democracies around the world.[54] Interestingly, Australia's trust in political institutions ranks well below China, in first place when it comes to the general population's trust in government. But trust in China has dropped from 83 percent in 2023 to 79 percent in 2024.[55] The 2024 Edelman Trust Barometer shows that more than half of Australian respondents are concerned that politicians are deliberately misleading them. In a twist, in Australia, government is seen as 'far less competent and ethical than business', but at the same time, exactly the same percentage (59 percent) of respondents who think government leaders are trying to purposely mislead people believe business leaders are trying to do the same – an increase of 5 percentage points from 2023.[56]

Key questions for Australian business leaders

1. **How can you ensure the responsible use of AI and data management within your organisation to maintain trust with customers and stakeholders?**
2. **What role can your business play in combating misinformation and disinformation, and how can you improve information accuracy and reliability for your stakeholders?**
3. **If lack of trust in public institutions means a more volatile operating environment, and more expectations being put onto business, how can you contribute to building public trust, not just in your own company or industry, but in societal institutions more broadly?**

SCENARIO 3: Walls, moats, and stranger danger

This scenario shows the contagion effects among the risks of deglobalisation, US politics and policy, and Australian national security. These risk factors together result in a global context of increasing mistrust and competition.

Rising concerns about protecting the national interest from an increasingly hostile world mean countries are turning inwards and away from cooperation, looking to minimise dependence on others. When they have to go beyond their own borders, countries build connections with those they feel they can trust. This values-based networking further reshapes global connections.

We are entering a time when trust among nation-states is diminishing, and rather than reaching out to cooperate, countries are shrinking back behind national lines. US President Joe Biden declared in 2022 that the country's future depends on 'made in America'.[57] Chinese leader Xi Jinping has likewise been advocating 'self-reliance'.[58] India's Prime Minister Narendra Modi has adopted a slogan of 'self-reliant India'.[59] Similar language can also be heard in Europe, and elsewhere around the world.[60] Australian government officials talk about the importance of 'sovereign capability', arguing that 'the more we make and do in Australia, the less vulnerable we are to unexpected global surprises'.[61] National leaders are building metaphorical and actual walls to 'protect the national interest'. Around the world, geopolitical competition and mistrust are driving leaders to shift their rhetoric and behaviour away from a generally shared understanding that connection and interactions based on the notion of comparative advantage are beneficial. Instead, leaders are increasingly seeing openness and interdependencies as vulnerabilities and risks, and building yards and fences to protect their strategic assets and national security.

This scenario shows that as these three interconnected risks intensify over time and more and more walls to open trade are erected, Australian businesses will need to examine where they fit in Australia's national security discourse, and how exposed and prepared they are for potentially dramatic shifts in the global trading system.

Scenario 3, Risk 1: Deglobalisation

Many analysts argue that the world has hit peak globalisation, at least for trade in goods. The current system is now starting to 'deglobalise' and transition to something different.[62] That is not to say that overall trade volumes and values have shrunk, rather that the direction of flows and selectiveness of trading partners are operating on different terms.

Globalisation has never been completely global. There have always been exclusions, usually based on political factors. For example, when the second wave of globalisation began after the end of the Second World War, trade liberalisation in advanced economies drove intensive economic integration around the world – except in countries like China, the then-Soviet Union, and even India, economies that were more state-led.[63] After the Cold War ended, technological advances in communications and transportation and political decisions to 'open up' economies, created a period of 'hyperglobalisation'.[64] These factors meant that manufacturing firms based in advanced economies could source labour-intensive products from lower-cost locations. The modern, complex supply chain was born, connecting advanced and developing or emerging economies according to who could make or supply what most efficiently.

Around the world, there is a growing perception that globalisation isn't meeting human needs, and this perception is driving mistrust in economic openness and integration.[65] Globalisation generates winners and losers, and for some, it has been highly disruptive.[66] Acknowledging this tension, the World Bank argued in 2020 that global value chains (GVCs) *could* be good for boosting growth, creating better jobs and reducing poverty in developing countries. However, this would only be the case *if* those countries introduced deep reforms, industrialised countries pursued open, predictable policies, and all countries revived multilateral cooperation.[67] At the time that report was published, the current period of geopolitical disruption was well underway. COVID-19 had already up-ended 'business-as-usual'. In a global context of increasing competition and mistrust, the likelihood of those 'ifs' being met are slim at best. As such, it is likely that the existing public dissatisfaction for globalisation will continue to grow, creating demand for change.[68] There is a growing perception around the world that the uncertain environment means it is now time to pull back from the global, and rather place tighter controls on borders, ensure supply chains are resilient (and preferably mostly domestic, or at least networked with trusted partners), and use trade restrictions for political leverage – both domestic and international.[69]

'On average globally, only 48 percent agree that globalization is a good thing for their country.

Positive views of globalization are down in every country (most of all in Latin America) by an average of 10 points since 2019, pre-COVID and vary widely across countries (from 72 percent in Malaysia to 27 percent in France).

About as many agree as disagree that globalization prevents their country's government from implementing effective economic policies and democracy in their country from functioning properly, but more are neutral or unsure.'[70]

At the same time that public support for globalisation is waning, geopolitical uncertainty is driving political leaders to look to protect their national interests by strengthening networks – including trade connections – with 'friends', rather than through unrestricted international connectivity.[71] 'Friendshoring' as a political term can be traced back to a speech made by US Treasury Secretary Janet Yellen in April 2022 when talking about 'the way forward for the US economy'.[72] Yellen argues that because some countries use their strong market position in various areas to disrupt the US economy or 'exercise unwanted geopolitical leverage', the US must respond. The key element is to 'do it with the countries we know we can count on'.[73] While this trend begins with strategic and critical raw materials and technologies, as national insecurity grows, so too does the definition of strategic and critical. And so, the scope of what needs to be sourced only from 'friends' expands. These shifts are not to say that the movement of goods, capital and information is ceasing, but rather that these things increasingly flow along lines that follow geopolitical rather than economic logic.

'Peak globalisation' and reshaped globalisation

In 2010, Bruce Nussbaum wrote an article in the Harvard Business Review which coined the term 'peak globalisation'. The idea at its simplest is that ever-increasing economic openness is a thing of the past.

'We, in fact, are living in an era of Peak Globalization as the costs and benefits of globalization begin to diverge according to country, class, and constituency. The international political consensus of the universal economic benefits of globalization that defined much of the 20th and early 21st centuries is breaking down. The centrifugal forces drawing nations toward globalization are giving way to centripetal forces pulling them away from it.[74]

While some argue that the narrative is oversimplified, there tends to be general agreement that the answer to the question of whether globalisation has peaked or not, is 'probably yes' for trade in goods, but for trade in services, the answer is 'no'.

Whether you agree that globalisation has peaked or not, it is important to look at the changing shapes and patterns of international connectivity. Prior to 2000, most trade liberalisation was multilateral (at the World Trade Organization (WTO) level) and therefore effectively global. Since then, however, there has not been a successful WTO round concluded, and we have seen an explosion of bilateral, mini-lateral and regional trade agreements, benefitting the countries involved, but not the whole world. Economic complementarity and geopolitical alignment have driven free trade agreement (FTA) growth, but in recent years geopolitical concerns have had increasing influence over the economic case for new preferential agreements.

In this geopolitically volatile world, we may still find ourselves moving as many goods and services around as ever, but we need to focus on where they go and where they come from. Rather than the whole world being our oyster, and goods and services coming from wherever makes the most economic sense – the logic of comparative advantage – networks will be increasingly based on values and trust. This will be particularly true for 'strategic' and 'critical' goods – and as geopolitical volatility grows, the definition of those is changing and expanding all the time.

Scenario 3, Risk 2: US politics and policy

Given the US' weight in the world, changes in US domestic and international politics and policy have significant influence on everyone. The US political system is facing major challenges, and these challenges are affecting how the country's leaders approach policymaking, both domestic and international. Because of Australia's historically close ties with the US, based largely on shared values and views on how the world should work, challenges to US politics and policy matter for Australia and Australian businesses.

Eurasia Group argues in its Top Risks for 2024 report that the US political system is 'more dysfunctional than that of any other advanced industrial democracy'.[75] Research shows that the country is suffering historic lows in trust for political institutions like the legal system, the Congress, and the traditional media as a legitimate 'Fourth Estate' representing the interests of 'the people' rather than political or business elites.[76] The capacity of social media to create and amplify disinformation is exacerbating the problem. Political dysfunction is pushing people away from the centre of politics, towards the outer fringes, creating deep and dangerous divides in US society.[77] As the two major parties and their supporters move further apart from each other, there are fewer centrists who can bridge the divide and broker compromises to enact legislation.[78] Scholars note that deep political divides in Washington 'have crippled efforts at legislative compromise, eroded institutional and behavioural norms, and incentivized politicians to pursue their aims outside of gridlocked institutions, including through the courts'.[79]

Far more than a disagreement or a different opinion about a matter, social or political polarisation refers to clustering ourselves into competing groups, where differences are seen as zero-sum win or lose, and where negotiation or compromise are seen as nothing less than betrayal.[80] Some research even argues that Americans are so polarised the country is on the brink of civil war.[81] Social polarisation is, at its simplest, the opposite of social cohesion.

Concerningly, researchers argue that the trend for US social and political cohesion is towards further weakening.[82] In the US, the ruptures are particularly difficult to reverse, because they have deep roots in a profound struggle between conservative and progressive visions of the country.[83] These divisions can be traced back to at least the 1960s and have been intensifying over the past five decades.[84] More recently, those existing fissures are being deliberately exploited by politicians, with the unsurprising result that US society and politics continue to become more fragmented.

Social polarisation can drive political leaders to adopt increasingly inward-focused policies as a means of demonstrating their powerful commitment to rebuilding domestic jobs and economic growth, and protecting them from foreign competition.[85] In the US, growing social polarisation is combined with deep concerns about geopolitical competition threatening the national interest. Together, these two factors are moving US foreign and trade policy away from the openness we have come to expect of it over the past several decades. Numerous analysts note that the US in recent years has moved away from being an important actor driving free trade, towards a more locally focused industrial policy, designed to revive American manufacturing.[86] Former Treasury Secretary Larry Summers described the approach as 'manufacturing-centred economic nationalism that is increasingly being put forth as a general principle to guide policy'.[87] Tariffs and other trade restrictions are being used to reshape US trade policy in ways that at least rhetorically serve domestic workers and their wage concerns and protect national security. Trade is becoming a tool of power, both domestic and international.[88] Current Treasury Secretary Janet Yellen's second visit to China in 2024 is a powerful example of this shift. In the past, Yellen has welcomed the lower prices for American consumers that came from China's ability to make inexpensive products at a great rate. However, in 2024, Yellen's concerns about Chinese industrial overcapacity and trade practices led her to note that 'cheap Chinese products' threaten the viability of American firms.[89] What was once an opportunity is now a threat.

As a powerful global actor, what would be minor policy shifts for any other country have global consequences when it's the US.

When it comes to the international sphere, the Lowy Institute's 2023 Asia Power Index shows that the United States still ranks as the world's number one overall power.[90] This includes measures of its current resources, like economic and military capability, its resilience, and its future resources, including defence, demographic, and economic. The Power Index also measures power in terms of influence – that is, what actual impact on the world a country's weight has.

The US again ranks number one.

There is no denying that the US matters. However, despite this strong performance, US influence in the system is weakening. According to the Lowy Institute's Asia Power Index,[91] while still strong, the US' overall power score is slowly declining. Indeed, it retains its top position not because of its own strategic performance, but largely due to China's setbacks during COVID. What this means is that if US global power continues to decline, its ability to influence norms and institutions in the global system in ways that suit Australian interests may also wane. This leaves Australian businesses in a highly uncertain and vulnerable position.

Scenario 3, Risk 3: Australian national security

Australia, like many nations, is bringing the issue of its national security and interests to the forefront of its public policy and political conversations. As a nation whose prosperity is built on reliable and predictable international trade, Australia depends on global openness and stability, and to a considerable extent, US policy and political predictability.

It is broadly accepted among analysts and researchers that external factors are making Australia's national security environment more complex and competitive.[92] Like America and other nations, Australia is responding to that global uncertainty by trying to shore up its trade and commercial connections with those it feels it can trust, and minimise its exposure to potential vulnerabilities that could come from being too reliant on those it feels it can't trust. This is particularly the case for 'strategic' and 'critical' goods. Like much of the world, national security for Australia means shifting its global outlook to one that is much more cautious and circumspect. Like other countries, this is reflected in a new approach to industrial policy: where possible, make it at home; if not, ensure we're trading with trustworthy friends.[93] The challenging question here of course is, when everything is so uncertain, how do we know whom we can trust?

A good real-life example of how security and criticality expand from the strategic security centre outwards to affect the mainstream is procurement. Governments in Australia and its close allies have long been acutely aware of the risks of procuring essential defence items from potentially unreliable actors, and recognise that cheaper is not always better.[94] Examples that demonstrate this awareness include the Australian Department of Defence's Force Structure Plan, released in 2020, which noted how shifting geopolitical dynamics threaten access to defence technologies, and the US Defence Department's strategy for Securing Defense-Critical Supply Chains (released in 2022).[95]

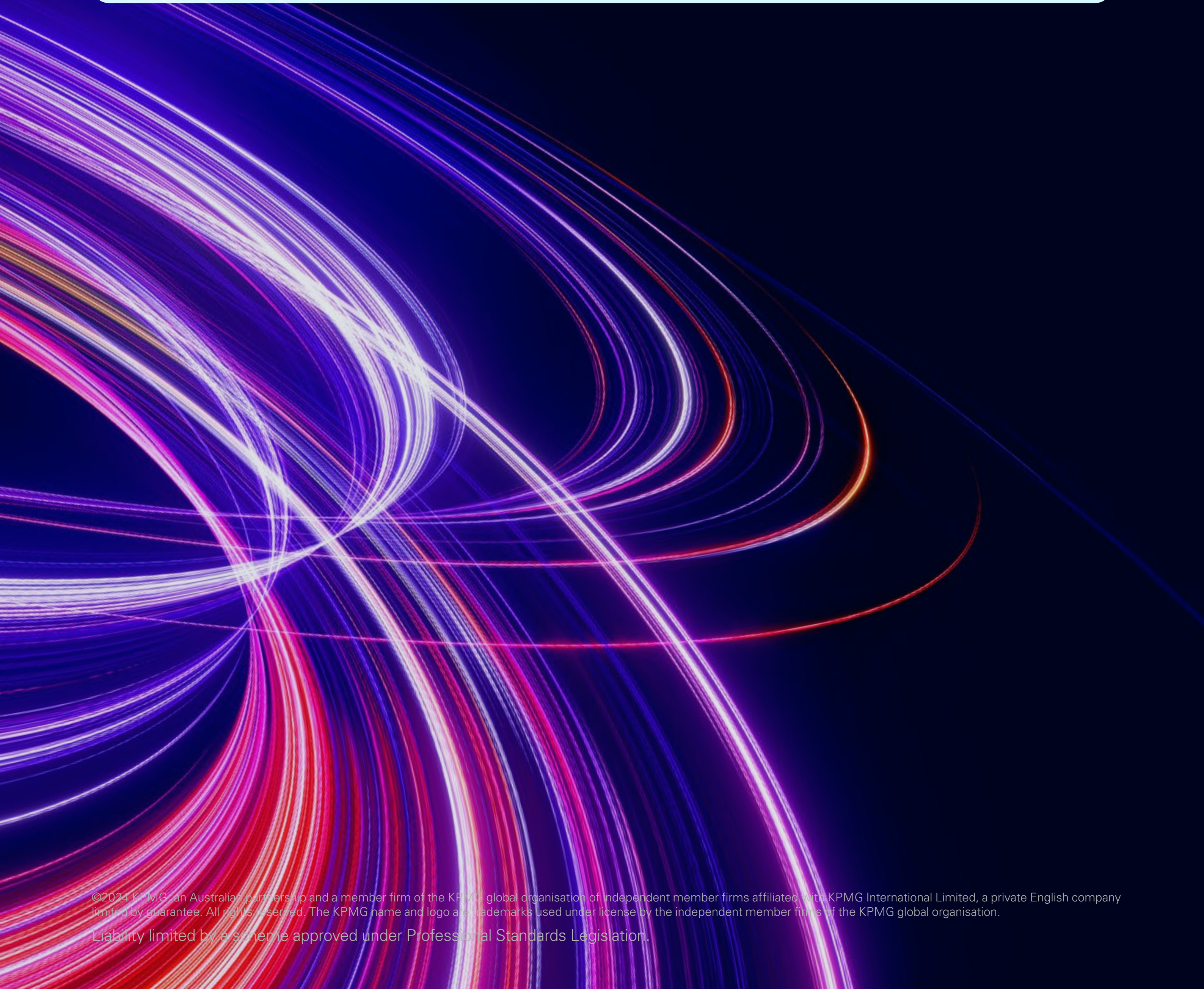
Australia's Security of Critical Infrastructure Act 2018 (SOCI) included four sectors seen as critically strategic to Australia's national security: electricity, gas, water and ports. In 2020, the Act was amended so that coverage was expanded to include 11 sectors: communications, financial services and markets, data storage and processing, defence industry, higher education and research, energy, food and grocery, health care and medical, space technology, transport, and water and sewerage.[96] In parallel, in 2021, the Treasury Department significantly expanded the definition of what constitutes a 'national security business', such that it now includes any business responsible for an asset in any of the industries covered by the amended SOCI Act.[97] Just as the understanding of which sectors are critical is expanding, so is the understanding of which actors are responsible for Australia's security (see breakout box on the following page). As in the US, with the expansion of what is to be kept safe in the 'small yard', this growing definition of what cannot be compromised in the interests of national security and who is responsible for protecting national security means that more aspects of our economy will become shaped by national security interests – and that cost is understood and accepted by governments.

There is a growing understanding in Australian government that everyone across society, including all aspects of government, as well as the business sector, now holds a part of the shared responsibility for national security.[98] While Australian companies understand the importance of security of supply, business is still largely driven by commercial considerations, namely cost. Given the government's growing concern around national security, and noting this perspective is bipartisan, there are likely to be policy shifts that will aim to incentivise business to align more closely with the government's strategic concerns. We would not expect anything as ambitious as America's Inflation Reduction Act (IRA) – a fundamentally geopolitical policy – in Australia, but business can anticipate policy shifts that 'nudge' towards simplifying and facilitating private financing of projects and investments that 'de-risk' Australia's economy.[99]

The Future Made in Australia Act (FMIA Act) is a good example of how Australia, like the US and others, is turning to a new and more interventionist approach to industrial policy to protect its national security.[100] The FMIA Act reflects the Australian Government's concern about being overly reliant on potentially unreliable suppliers for strategic and critical technology – like that required for energy security in Australia's decarbonising economy. For example, the 2024 Australian Budget earmarked A$1 billion to support the Australian production of solar panels. Economists argue that this policy is 'innocent of any convincing rationale' because even with production subsidies of A$8 billion over the next 10 years, the final product would still be more expensive than what could be imported from China, and potentially of lower quality.[101] The FMIA Act explicitly identifies a more active role for government to play in industrial investment in cases where the market has failed to align with broader national interest objectives, including security.[102] From an economic logic perspective, many have argued that the FMIA Act represents a return to protectionism, including current and former heads of the Australian Productivity Commission.[103] The counterargument is that independence in critical industries like energy is quite simply a matter of national security, and therefore, while perhaps more costly, nevertheless non-negotiable.[104] The FMIA Act is a clear signal of the shifting balance in Australia's thinking, where geopolitical logic is becoming increasingly influential in government decision-making.

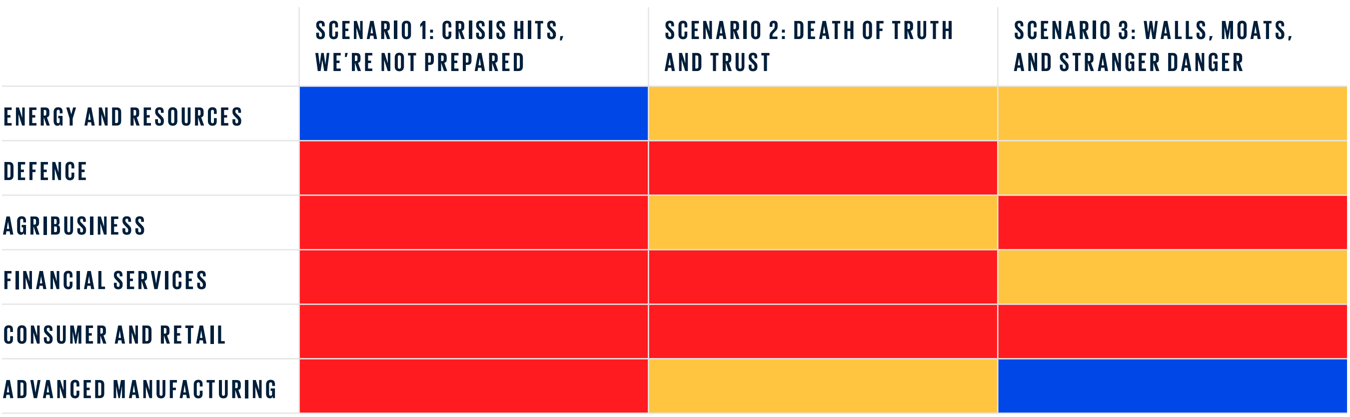
Key questions for Australian business leaders

1. How can your business adapt to the changing landscape of international trade and potential shifts towards more inward-looking, nationalistic policies globally?
2. What implications do changes in US politics and policies have for your business operations, and how can you mitigate associated risks?
3. In what ways can your business align with Australia's evolving national security priorities without compromising competitiveness and growth?
4. Who do you trade with internationally, and do they align to the government's perceptions of who we can trust?



Industry spotlight

Top geopolitical risks – heat map for Australian industries



Indicates the scenario represents a less material source of risk for this industry

Indicates the scenario warrants active management for this industry

Indicates the scenario represents critical risks for this industry

Energy and resources

Scenario 1: Crisis hits, we're not prepared

(Risks: climate change and biodiversity loss, energy and food security, and the imbalance between long-term and short-term strategy)

Australia's energy and resources industries are arguably better prepared than many sectors to navigate some (but not all) aspects of Risk Scenario 1.

> 'Energy and resources projects often span multiple decades, so companies in the sector are used to planning many years ahead. This long-term strategic outlook can help companies manage some of the challenges that come with climate change and protecting biodiversity.'
>
> – NICK HARRIDGE, ENR LEAD, KPMG AUSTRALIA

Energy generators, on the other hand, may enjoy greater demand as global energy supply becomes more constrained. As this risk scenario plays out, energy and resources companies need to consider how the mutually reinforcing risks will impact each project, and set strategy accordingly.

Scenario 2: The death of truth and trust

(Risks: AI governance, a decline in trust of public institutions, and misinformation and disinformation)

The energy and resources sector is significantly exposed to this risk scenario, with declining trust, artificial intelligence and rising expectations from stakeholders all creating challenges. While AI advances offer the sector productivity gains, they also open new categories of cyberthreat – especially for energy companies, and those that operate as part of defence industry supply chains. Meanwhile, as people lose faith in public institutions, they expect more from companies. These expectations can span issues from ESG performance to taking a stand on divisive social issues. Responding to these challenges will be made harder by the growing threat of misinformation and disinformation. This is because companies may need to commit significant time and energy to actively countering false narratives in the public domain, or risk reputational damage.

Scenario 3: Walls, moats, and stranger danger

(Risks: Australian national security, deglobalisation, and US politics and policy)

The increasing fragmentation of global trade and investment markets means that companies need to consider which countries they rely on for export sales, supply of inputs and investment. As countries build walls and raise drawbridges, even the most economically complementary relationships can become dysfunctional. We have already seen an example of this dynamic in 2020, when China halted imports of Australian coal, copper, and other commodities. By the same token, Australia and many other countries are now seriously limiting the ability of foreign investors from some countries to acquire assets and enter into partnerships in strategic resources and energy sectors – examples include decisions from Australia's Foreign Investment Review Board, and Canada's restrictions on foreign ownership of lithium projects.[105] However, this process of de-risking also creates opportunities. For example, the US Inflation Reduction Act[106] – a US$370 billion set of industrial and climate policies – includes rules that favour exports of critical minerals and defence goods from close US allies, including Australia.[107]

Defence industries

Scenario 1: Crisis hits, we're not prepared

(Risks: climate change and biodiversity loss, energy and food security, and the imbalance between long-term and short-term strategy)

Defence industries face a wide range of short-, medium- and longer-term risks and opportunities. In the near-term, geopolitical disruptions driven by conflict in Ukraine, the Middle East, and North Africa are contributing to high demand for defence products, and an array of restrictions and sanctions impacting with whom companies can do business. Longer term, the geopolitical impacts of climate change – including competition for renewable energy, mass migration and food insecurity – are likely to increase Australian demand for sovereign defence products and capabilities. Other long-term government policies – notably Pillar 1 of the AUKUS agreement – also create opportunities and challenges for defence industries. Opportunities include increasing funding for sovereign defence manufacturing, including nuclear-powered submarines and their value chains. Challenges include the way that such policies could attract scarce expert labour and regulatory support, crowding out companies that are working on other aspects of the defence sector.

Scenario 2: The death of truth and trust

(Risks: AI governance, a decline in trust of public institutions, and misinformation and disinformation)

Defence industries are especially exposed to Scenario 2. One reason for this is the strategic value to foreign interests of the data that the sector manages.

> 'Defence industry firms may be privy to classified government strategy, technical specifications, and other information, making them a tempting target for cybercriminals and foreign intelligence services. The international collaboration envisaged under Pillar 2 of the AUKUS agreement is a key example of the need for incredibly robust data governance.'
>
> – PETER ROBINSON, LEAD PARTNER DEFENCE INDUSTRIES, KPMG AUSTRALIA

As AI advances rapidly and governance structures struggle to keep up, these cyberthreats are multiplying. Another, more fundamental, challenge posed by this scenario flows from the general decline in truth and trust. It will become harder and harder for defence industry firms to identify trustworthy intelligence and partners, and to prove their own trustworthiness to stakeholders.

Scenario 3: Walls, moats, and stranger danger

(Risks: Australian national security, deglobalisation, and US politics and policy)

The increasing process of deglobalisation that is playing out as part of Scenario 3 means that defence industry firms do business in a global market that is splitting into rival geopolitical groupings. As a result, it may become increasingly difficult to work with counterparts in less 'like-minded' nation-states, but local companies may enjoy some advantages in Australia and closely allied countries. International commercial partnerships with firms based in a country that is not closely allied with Australia are already becoming harder to maintain. Proposed regulations include prison penalties for researchers that collaborate with some international partners.[108] On the other hand, opportunities that flow from Scenario 3 include the already-announced industry policies that aim to increase Australia's sovereign capabilities in strategic industries, including defence.[109] Either way, supply chain resilience could become increasingly challenging, as companies are obliged to source the inputs and expertise they require from 'like-minded' countries only. All of this looks like the early stages of a growing trend: as the global environment becomes more competitive and mistrustful, support for domestic defence industries is likely to continue to increase.

Agribusiness

Scenario 1: Crisis hits, we're not prepared

(Risks: climate change and biodiversity loss, energy and food security, and the imbalance between long-term and short-term strategy)

Food and agribusiness industries in Australia are intrinsically linked to climate and biodiversity risks, as well as energy and food security. As a highly productive agricultural nation, Australia's diversity of commodities relies on fertile soils, water availability, and stable climatic conditions, all of which face significant risk under this scenario. Implementing technology and adaptation strategies at the farmer and supply chain level will be crucial for industry management of these risks, which are exacerbated by the long-term planning timescales required in agriculture for planting, rearing and/or cultivation. Australian agricultural competitiveness domestically and in export markets is also impacted by the higher input costs associated with Australian farming when compared to competing nations. Fluctuating energy costs and availability of inputs (including labour) has already proven to be a significant risk to industry – and has the potential to spiral. This risk scenario overall will impact agriculture unevenly, across commodities and regions within Australia, making long-term planning at scale an acute challenge.

Scenario 2: The death of truth and trust

(Risks: AI governance, a decline in trust of public institutions, and misinformation and disinformation)

The fundamental principles at the core of risk Scenario 2 (technology, data, and regulation) all intersect with the Australian agricultural sector. Agriculture is a global industry that has traditionally been highly regulated. Governments both support and constrain the sector using a combination of quotas, subsidies, licences and tariffs. As such, a changing relationship with the public sector and regulators could generate significant uncertainty for agricultural firms, who would have to respond to politically driven changes in regulation. The agricultural sector in Australia has typically been viewed as a leader in innovation. Australian operators employ sophisticated technological approaches to improve yields and productivity. AI offers new possibilities in this area. However, future regulatory efforts to govern AI may impact the ability of agricultural operators to harness these technologies. Agricultural firms will rely on these same regulatory efforts to safeguard them from cyberattacks, especially from malicious actors that understand the importance of the industry to Australian national food security and prosperity.

Scenario 3: Walls, moats, and stranger danger

(Risks: Australian national security, deglobalisation, and US politics and policy)

As a major sector in the Australian economy, the success of Australian agriculture is ultimately an issue of national security. What occurs on the international stage, and risk trends in global trade, will influence outcomes for the industry, which produces much more food than is required to serve the Australian domestic population alone. A free trade environment, with market access and commercial opportunities in multiple markets, has historically suited Australian agriculture. The Free Trade Agreements (FTAs) that Australia signed with North Asian and other economies in the 2010s have contributed to record export sales from sectors including red meat, horticulture and dairy.

> 'In a world where globalisation is being reshaped and where trade restrictions are frequently levied based upon geopolitical rather than economic rationales, Australian agriculture will have to work hard to diversify its markets. It will also need to accept that the scale and margins achieved in some destinations in the past may not be possible in the new trade environment.'
>
> – GEORGIE ALEY, CONSULTING SECTOR LEAD – CONSUMER PRODUCTS & INDUSTRIAL MARKETS

Agricultural operators will need to rethink cost structures all along the supply chain to improve Australian competitiveness and meet customer demand.

Financial services

Scenario 1: Crisis hits, we're not prepared

(Risks: climate change and biodiversity loss, energy and food security, and the imbalance between long-term and short-term strategy)

Australia's financial services sector faces a wide range of interconnected issues driven by climate change, energy and food security and the long- and short-term strategies that these challenges are prompting. For example, the climate crisis is increasing pressure on financial services firms to declare and manage the associated financial risks. This is a particularly challenging issue for insurers, with more and more properties at risk of being uninsurable.[110] Banks and institutional investors will need to consider how this risk scenario could impact them, but also their borrowers. Borrowers include companies in industries that are highly exposed to the physical effects of climate change and to the policy changes that climate change will make necessary. Successfully navigating Scenario 1 could require revising the way that macro risks are identified and managed by Australia's financial services firms.

Scenario 2: The death of truth and trust

(Risks: AI governance, a decline in trust of public institutions, and misinformation and disinformation)

The growing mistrust that is a key element of Scenario 2 represents both general and specific risks for the financial services sector. General risks include the increasing challenge of demonstrating to customers and regulators that financial services firms are trustworthy and are acting in the best interests of their clients and the broader financial system. Stakeholders – from government officials to customers to employees – expect more and more from financial services firms,[111] and the task of rebuilding trust following the 2019 Royal Commission is arguably still underway.[112] Specific risks include the increasing threat of AI-enabled fraud.[113] Banks and other financial services firms now need to invest significantly in helping protect customers from fraud, but debate remains about whether banks or customers should bear responsibility for losses.[114] As is the case with other sectors, financial services firms need to invest in trust capital. However, the events that prompted the Royal Commission in Australia mean that the industry faces an uphill battle in doing so. Many of these risks require a collaborative response, but competition laws can make it difficult for banks and other financial firms to work together.

Scenario 3: Walls, moats, and stranger danger

(Risks: Australian national security, deglobalisation, and US politics and policy)

The increasing fragmentation of global markets that is a key element of Scenario 3 is of high importance to Australia's financial services businesses. As countries try to insulate themselves against foreign influence, truly global markets for capital, insurance and currencies could become a thing of the past. A growing policy focus on national security is driving this trend. Strategic efforts to exclude Russia from key parts of the global financial system following the invasion of Ukraine provide one example.[115] Another is the desire of members of the Shanghai Cooperation Organisation (SCO) to reduce the global role of the US dollar.[116] These examples represent a broader trend away from international financial integration, which will represent complex challenges for the financial services sector in the years ahead.

> 'Australian financial firms have historically been able to access global funding sources during difficult moments in the national economic cycle. As these overseas sources become less accessible, due to the fragmentation outlined above, Australian banks may be less able to help shield the economy from shocks.'
>
> – DANIEL KNOLL, FINANCIAL SERVICES LEAD, KPMG AUSTRALIA

Consumer and retail

Scenario 1: Crisis hits, we're not prepared

(Risks: climate change and biodiversity loss, energy and food security, and the imbalance between long-term and short-term strategy)

Australia's consumer and retail firms are already facing risks that flow from Scenario 1, and the challenges are set to intensify.[117] Impacts on the sector range from the immediate and physical to more complex longer-term issues. The immediate physical effects of climate change impact supply chains, making it harder and more expensive for retailers to source the products they need.[118] This contributes to an inflationary environment, that in turn hurts consumer confidence. Energy supply challenges and price rises associated with the uneven transition to renewables threaten to raise costs for retailers, and impact customers' discretionary spending. If consumer and retail firms do not anticipate and prepare for these looming challenges, they will be subject to a steadily deteriorating business environment.

Scenario 2: The death of truth and trust

(Risks: AI governance, a decline in trust of public institutions, and misinformation and disinformation)

The death of truth and trust is a serious matter for consumer and retail companies. These firms rely on the trust of all their stakeholders, including customers, employees, regulators and suppliers. The risks that make up Scenario 2 are a threat to this trust. AI-enabled fraud is a growing challenge that companies in the sector face, on behalf of themselves and their customers. Cyber security – protecting the huge volumes of customer and employee data – is another threat that is only growing. As well as these specific risks, the general decline of trust in public institutions is prompting citizens to look to high-profile companies to fill the trust void. Research indicates[119] that many citizens now have more faith in companies than in governments. This can be a positive for major consumer brands, but by the same token, as people increase their trust, they expect companies to engage on contentious social and political issues.[120] Doing so can be fraught, as taking a stand can alienate as many stakeholders as it pleases. Ongoing investment in trust capital will be an increasingly important objective for public-facing brands in the years ahead.

Scenario 3: Walls, moats, and stranger danger

(Risks: Australian national security, deglobalisation, and US politics and policy)

The general pulling back from global interdependence that forms a key aspect of Scenario 3 carries important implications for consumer and retail companies. As Australia and other countries become more and more focused on national security and reducing dependence on potentially unreliable countries, conflict and trade wars are becoming more likely. This can disrupt supply chains for energy and other goods, and the associated supply shortages and price increases hurt consumer confidence.[121] Another aspect that can contribute to consumers closing their wallets is the general anxiety that people feel as a result of national security worries: the US Federal Reserve has identified a direct link between geopolitical uncertainty and falling consumer confidence.[122]

> 'All of these challenges – disrupted supply chains, rising prices for energy and other imported goods, and low consumer confidence – must be carefully managed by consumer and retail businesses.'
>
> – JAMES STEWART, NATIONAL LEADER, CONSUMER AND RETAIL, KPMG AUSTRALIA

Advanced manufacturing

Scenario 1: Crisis hits, we're not prepared

(Risks: climate change and biodiversity loss, energy and food security, and the imbalance between long-term and short-term strategy)

Climate change, energy and food security challenges, and the trade-offs governments make between short- and long-term objectives are all highly relevant for the Australian advanced manufacturing sector. Specific challenges include energy cost and availability risks, and climate change disruptions to supply chains. These two factors could make it more difficult and expensive for advanced manufacturers to access the energy and raw materials that they need, and to ship their finished goods to export customers, and could contribute to inflation in prices for manufactured goods. Another challenge results from the imbalance between short- and long-term thinking identified in this risk scenario. Investing in advanced manufacturing industries requires long time horizons and is aided by policy certainty. When governments prioritise shorter-term economic outcomes, they are less likely to make the long-term policy commitments that help convince advanced manufacturers to invest.

Scenario 2: The death of truth and trust

(Risks: AI governance, a decline in trust of public institutions, and misinformation and disinformation)

The death of truth and trust presents some major challenges and opportunities for the advanced manufacturing sector. Governments around the world (including in Australia) are grappling with how to effectively regulate new technologies such as AI and quantum computing. This task is made harder due to the increasing mistrust citizens feel for governments, which is amplified by social media echo chambers.[123] As a result, companies in advanced industries face an uncertain regulatory environment. However, many companies will also benefit from increasing customer demand for their products, and supportive industry policies.

> **'To harness the opportunities while managing the risks inherent in the environment of growing cyber risk and declining trust, advanced manufacturers will need to invest in their own trust capital, their government relations capabilities, and their cyber security systems.'**
>
> – SOPHIE RITCHIE, HEAD OF PORTFOLIO MANAGEMENT, KPMG HIGH GROWTH VENTURES

Scenario 3: Walls, moats, and stranger danger

(Risks: Australian national security, deglobalisation, and US politics and policy)

Scenario 3 paints a picture of a retreat from global integration and increasing government concern about national security. International cooperation on advanced manufacturing is becoming less open and more strategic – much more likely between close geopolitical allies. This is not all bad news for Australia's advanced manufacturing sector. These moves towards domestic self-sufficiency in strategic sectors stand to benefit companies in renewable energy and other advanced technology industries. This is because there is increasing policy support for domestic investment in these industries, for example the various funding mechanisms announced as part of the Future Made in Australia Act.[124] Another source of potential opportunity for advanced manufacturers is the growing preference in other countries – notably the US, EU, Japan, and South Korea – for strategic goods sourced from geopolitically aligned countries. Australian firms may find that customers and investors in these geopolitically like-minded countries are willing to pay a premium for some strategic or critical products, including renewable energy goods.

Common thread

Connected challenges, fragmented solutions

The risk scenarios identified in this report all call for coordinated and collaborative responses between countries, companies, and people. However, the geopolitical volatility and mistrust that is driving these risks is also driving growing isolation and competition, which makes working together less likely.

There is a real risk that more and more countries will conclude that there is little point taking costly actions to address shared risks or push for public goods if others can't be relied on to do the same.

Scenario 1 describes a world unprepared for complex crises, including climate change and associated threats to food and energy security. Responding to the crises will require an unprecedented degree of collaboration between countries.[125] However, the more competitive and mistrustful the geopolitical environment becomes, the less inclined countries will be to agree on a shared way forward. Similarly, Scenario 2 unpacks how advances in AI and other tech are raising misinformation and disinformation risks, and outpacing governments' ability to effectively regulate them – which contributes to declining trust in public institutions. Like climate change, these issues cross borders, and require global collaboration to manage.[126] The challenge is that the competitive geopolitical environment is prompting countries to pursue their own AI advantages, rather than working together, compounding the risks associated with the loss of trust, misinformation and disinformation. Adding further pressure to collaboration, Scenario 3 describes the risks Australia faces in a world where globalisation is being reshaped along values lines. An interdependent, collaborative and stable region would best support Australia's national security objectives, as would economic and security partnerships with a wide range of countries. However, in the increasingly volatile geopolitical environment, exacerbated by the impacts of climate change, countries in the region are more likely to pull back from collaboration – retreating behind walls and moats – than they are to increase cooperation.

Global collaboration on these global challenges will continue to prove difficult, and companies will need to consider what this means for their strategic and operational decisions.

Implications for Australian businesses

Global market dynamics

Political instability in many countries is making international investors nervous and affecting global flows of capital. The International Monetary Fund (IMF) highlighted these impacts this year, finding that investment flows are being redirected along geopolitical lines.[127] As a large country with a relatively small population, Australia has always depended on inward foreign investment.[128] For Australian businesses, disruptions in global investment flows could make it harder to get the capital they need.

The same instability and competition have resulted in disruptions to supply chains for energy, food and other goods, and analysts believe that these disruptions could intensify.

Businesses will need to adapt by diversifying their supply chains or reshoring some operations, which can be costly and complex.

Domestic regulations and compliance

The rapidly shifting geopolitical environment is prompting the Australian Government to set new regulations that affect businesses. At the same time, the definition of 'critical' is growing. Australia's Security of Critical Infrastructure Act provides an example of these evolving regulations.[129] The Act requires businesses that operate parts of Australia's critical infrastructure to maintain and demonstrate stringent security settings. As noted earlier in this report, the Act originally applied to just four sectors (electricity, gas, water, and ports) but was amended in 2020 to cover eleven industries, including communications, higher education, food and groceries, and financial services and markets.

These regulations can change rapidly, especially when they are considered necessary for safeguarding critical national interests.

As geopolitical competition and mistrust prompts the Australian Government to increase regulatory requirements for businesses that operate in critical and strategic parts of the economy, compliance will be an ongoing challenge for more and more firms.

Trust and reputation

The climate crisis demands that businesses adopt sustainable practices, not only to comply with regulations but also to fulfil customer expectations. In addition, as AI technologies evolve, misinformation and disinformation can threaten a business's reputation. Companies must be proactive in ensuring the information they disseminate is accurate, and in combating false narratives about their products or services.

As citizens lose trust in public institutions, research indicates that their faith in companies is actually increasing.[130] But with this growing faith comes far greater expectations to do the right thing, and the risk of punishment in the form of boycotts and the like if companies are not seen to meet these standards.

Companies will need to work harder to build and maintain public trust by ensuring transparency and demonstrating ethical conduct. They will also have to tread carefully along the shifting line between what is considered 'the right thing' by some groups, but not others.

Another implication for businesses is that there is a growing risk of overall systemic breakdown because of the way that declining trust erodes the system itself. Often businesses believe that the political environment is outside of their ability to influence. However, given that many of the challenges we face arise from a lack of trust, the urgent need for trust and connectivity is something the business community can be part of building. In addition to trust and reputation for our own benefit, we can and should be investing in rebuilding citizen confidence in a world not of extremes, but of predictability, equity, and fairness.

Individual risks

Definitions

RISK	DESCRIPTION
AI governance	Technology outstripping AI governance, regulatory efforts fail to keep up, leading to an unconstrained spread of far more powerful AI models beyond the control of governments.
Climate change and biodiversity loss	Failure to achieve climate goals leads to various circumstances (e.g. extreme weather events, biodiversity loss, crop failures, etc.) that drive profound social, political and economic instability in the ASPAC region.
Deglobalisation	A shift away from globalisation as countries build protectionist measures and self-sufficiency to mitigate risks of external shocks from geopolitical events.
Energy and food security	Inability to sustainably and cost effectively secure energy, food and water supply.
Imbalance between short-term and long-term strategy	Australia's public and private sector not managing to find a balance that optimises short-term goals vs having a proactive stance on long-term investments and priorities (e.g. ESG investment and critical minerals).
Misinformation and disinformation	Rise of deepfakes and deliberate misinformation from international governments presenting a large risk for political and social unrest and economic uncertainty.
National security	Failure to invest in national security resulting in exposures to the nation's resilience with regard to foreign interests and influence.
Skills shortage	Lack of skilled talent to match demand for resource capabilities tied to migration policy.
Trust in public institutions	Corporations and the private sector don't meet community expectations at the same time as decreasing trust in politics and public institutions.
US politics and policy	The United States' political challenges and election outcomes affect global economic and political dynamics, foreign and industrial policies, and expectations of Australia.
Values-based world trade	Mistrust at a global level means Australia's trading partners become limited to those who can be 'trusted', negatively impacting import and export markets.

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