

Course on Climate-Smart Trade and Investment for Sustainable Development

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# Climate policies and international trade: Implications of the EU's Carbon Border Adjustment Mechanism

Dr Salamat Ali  
Trade Economist  
International Trade Policy Section



# Trade Hot Topics

A Special Focus on Trade, Environment and Climate Change

## Outline

Overview of the EU's Carbon Border Adjustment Mechanism (CBAM)

CBAM's implications for international trade

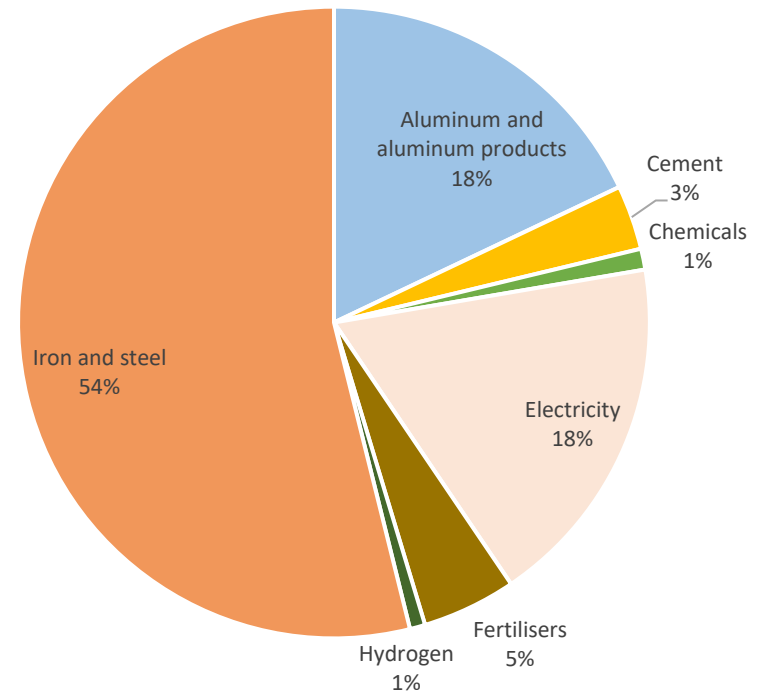
Key issues and challenges around the CBAM

Conclusion

## Overview: Salient features of the EU's CBAM

- Pricing embedded carbon (direct and indirect) at the border for specified imports according to the emission intensity of goods' production processes
- Transitional period from 1 October 2023 to 1 January 2026, and phase-in period for 8 years from January 2026
- Resolution entered into force on 16 May 2023 and the first report to be generated on 31 Jan 2024.
- In phase 1, the CBAM will apply to more than 500 products in six energy intensive sectors ([EU deal reached on the CBAM: what you need to know](#))
- Imports originating from countries having their own carbon pricing or ETS could seek abatement in CBAM charges.

**Industrial sectors with strong forward and backward linkages are exposed to the CBAM**



**Iron and steel**

Canada, the UK; India, South Africa, Malaysia



**Aluminium**

Canada and the UK; Mozambique, India, South Africa, Papua New Guinea



**Fertilisers and chemicals**

The UK, Canada; India, Singapore, South Africa, Jamaica



**Cement**

The UK, South Africa

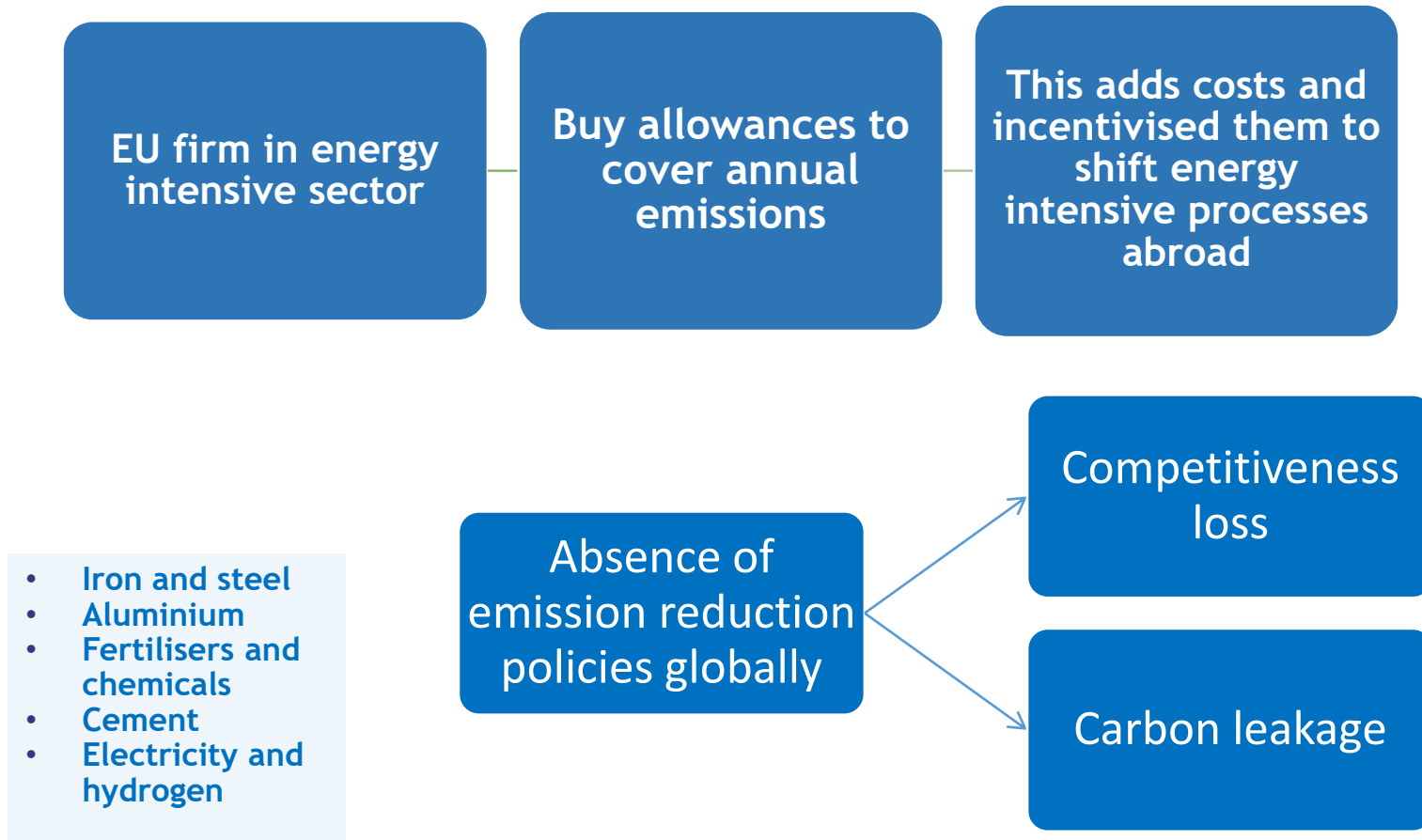


**Electricity**

The UK

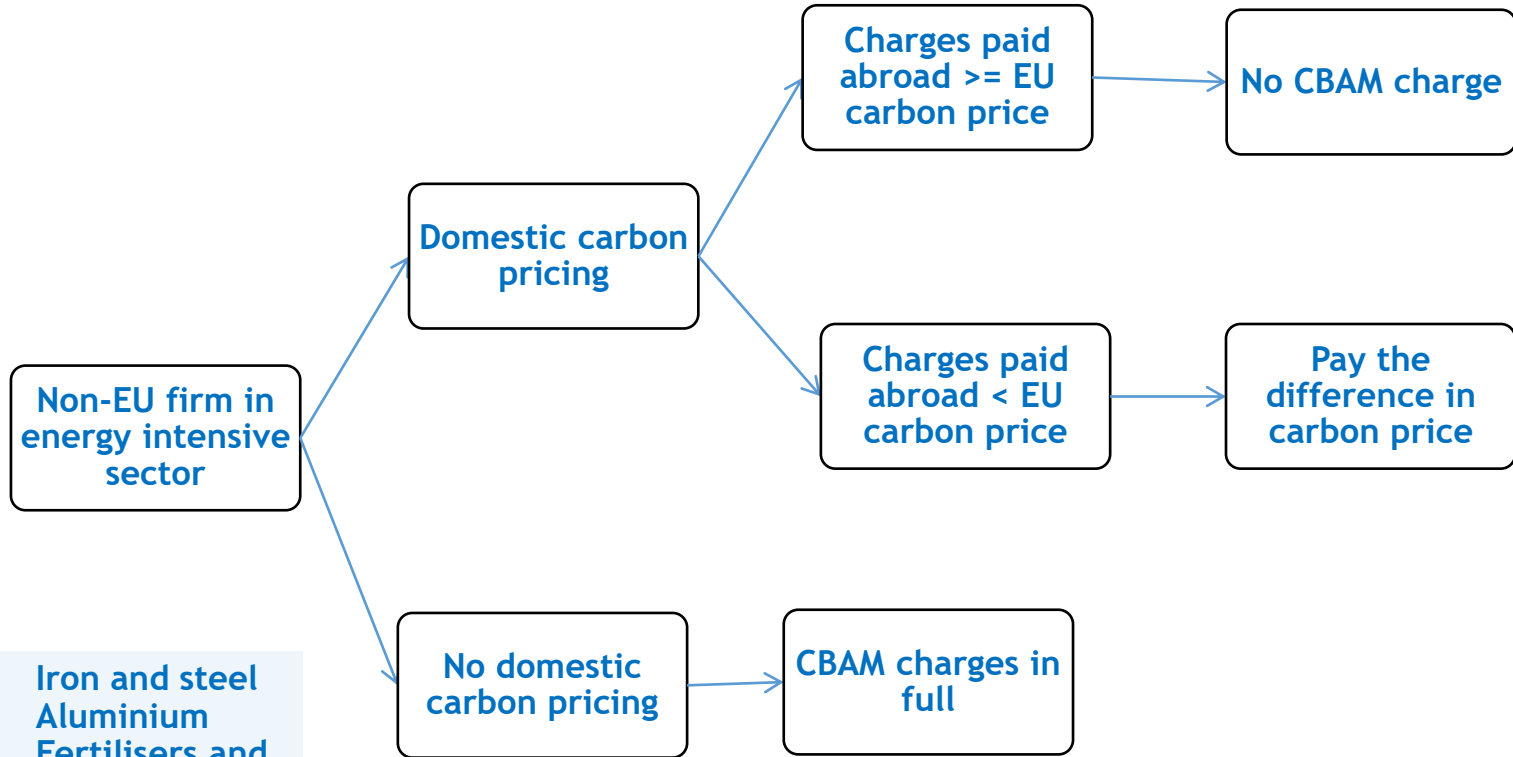


## Rational of the CBAM



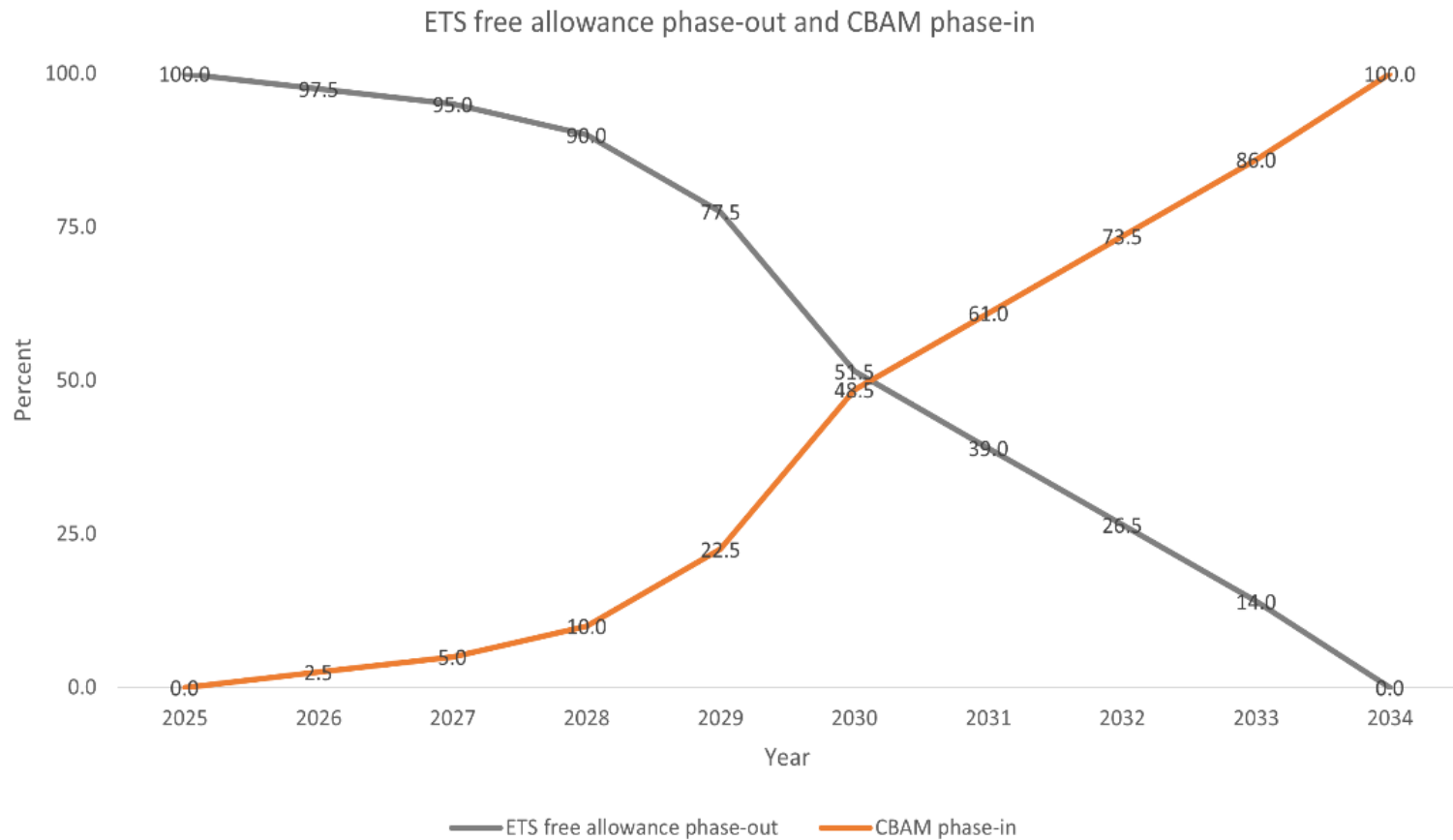
Carbon leakage occurs when companies based in the EU move carbon-intensive production abroad to countries where less stringent climate policies are in place than in the EU, or when EU products get replaced by more carbon-intensive imports: [Source: Carbon Border Adjustment Mechanism \(europa.eu\)](https://europa.eu)

# Mechanics of the CBAM



- Iron and steel
- Aluminium
- Fertilisers and chemicals
- Cement
- Electricity and hydrogen

# CBAM timeline: Transition to full implementation





# Implications for international trade

- EU-bound exports in CBAM exposed sectors
- Regional break up



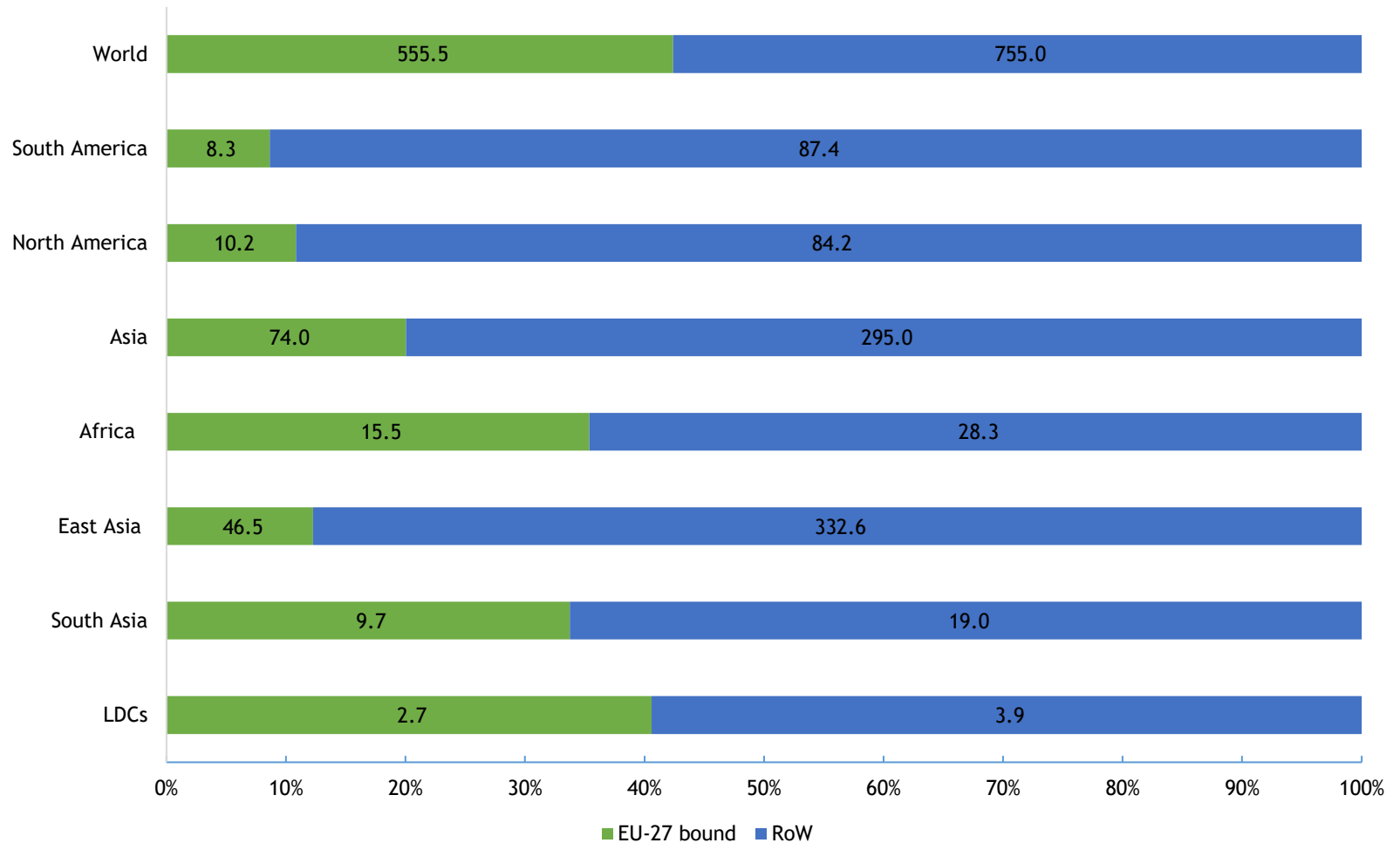
The Commonwealth



## Exports from energy intensive sectors at risk

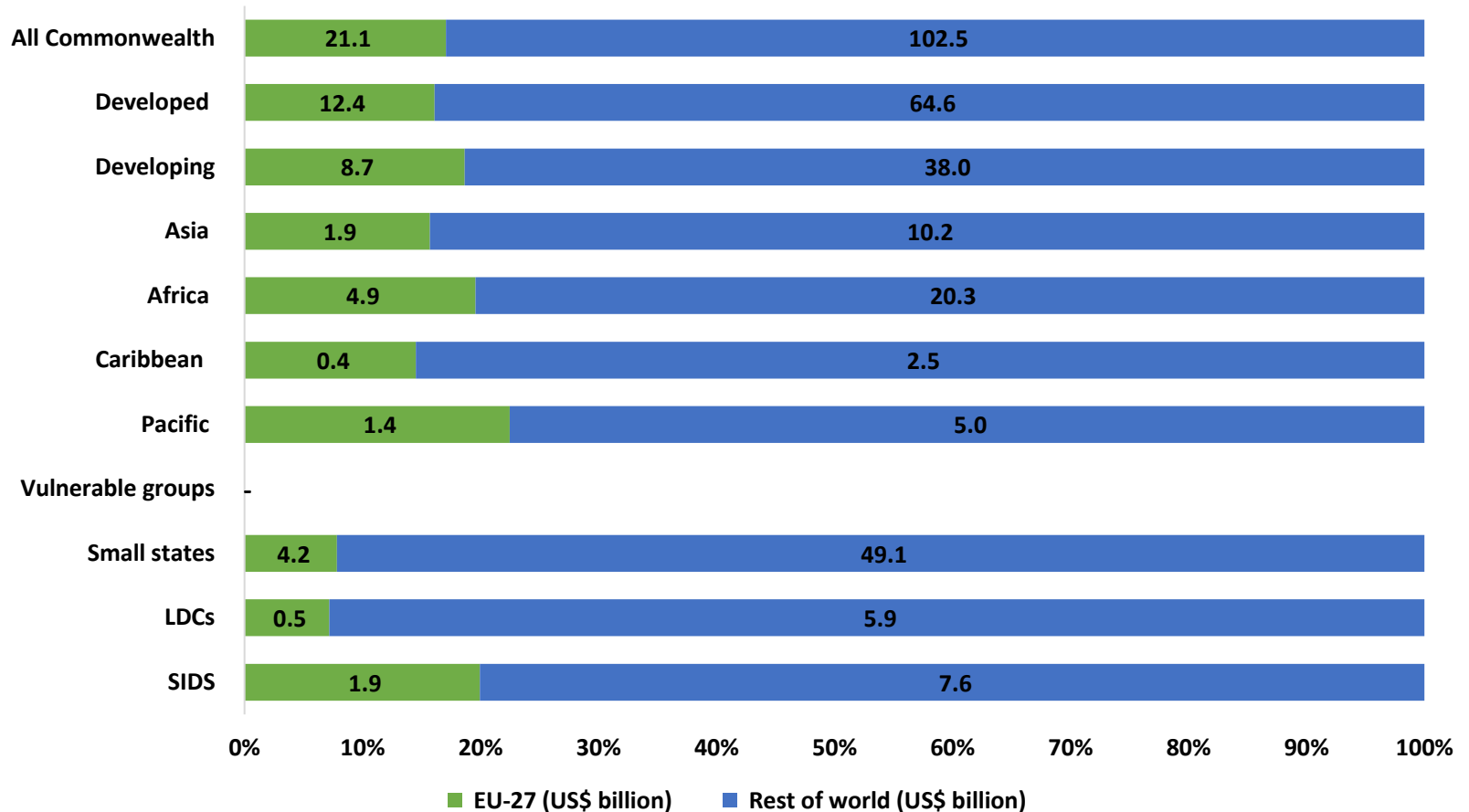
- EU-27's total imports in 2022: US\$7.4 trillion (29%)
  - Exports at risk of the EU CBAM:
    - \$556 billion (of \$1,310 global total)
    - 42% of exports from these selected sectors
    - 7% of all EU-bound exports
- Recent BCA announcements (for instance, United States; Canada; Japan; UK and others) could place large exports from these energy intensive sectors at risk (\$1.3 trillion).

## Distribution of global trade exposed to the CBAM across regions (US\$ billion, %)\*



\*Data for 2022

# Commonwealth members' trade exposed to the CBAM





# Issues and concerns regarding the CBAM

WTO compatibility

Administration and compliance

Revenue generation and usage

Treatment of developing countries and LDCs



## WTO consistency?

Most-Favoured  
Nation



Non-discriminatory treatment  
between products of WTO  
Members

National Treatment



Non-discriminatory treatment  
between imported and domestic  
products

Under certain conditions, Members can adopt trade-related measures aimed at protecting the environment provided they do not constitute a disguised barrier to trade or discriminate between countries.

## Administrative challenges around implementation (1)

Absence of universal measurement standards for assessing product-specific emissions (MRV)

Capacity constraints in developing countries to measure emissions and complete procedural formalities

Complications around abatement (production place vs. default emission averages)

Effectiveness to reduce global emissions

## Developing countries perspectives on the CBAM

- Undermines the spirit of multilateralism
- Potential conflict with Paris Accord and United Nations Framework Convention on Climate Change (UNFCCC) principles:
  - Nationally Determined Contributions (NDCs)
  - Common but Differentiated Responsibilities and Respective Capabilities (CBDR-RC)
- Potential conflict with the WTO rules (MFN, and NT)
  - Green protectionism; shifting climate mitigation burden on others
  - Forcing countries to align their trade policies with the EU



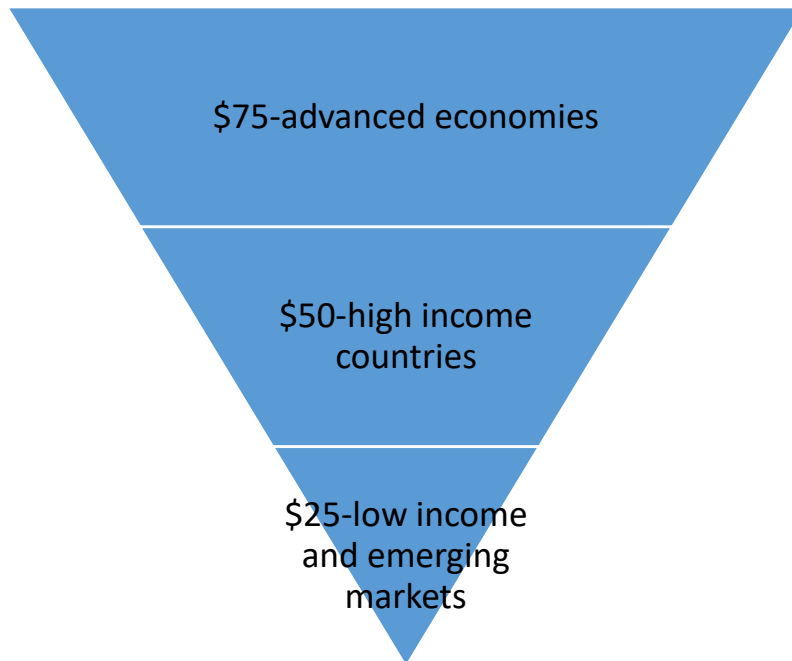
## Some thoughts from African members

- African continent could lose \$26 billion per annum due to the EU's border taxes.
- South Africa's exports at risk of the EU CBAM:
  - \$1.5 billion
  - 4% potential decline in the EU-bound exports
- Fragile economies (LDCs, for example Mozambique) not exempt
- Knock on effects on upstream sectors, leading to increase in poverty, inequality and unemployment
- Potentially violates WTO's provisions on non-discrimination
- Inclusion of indirect emissions (scope 2 and scope 3) could have significant negative effects.

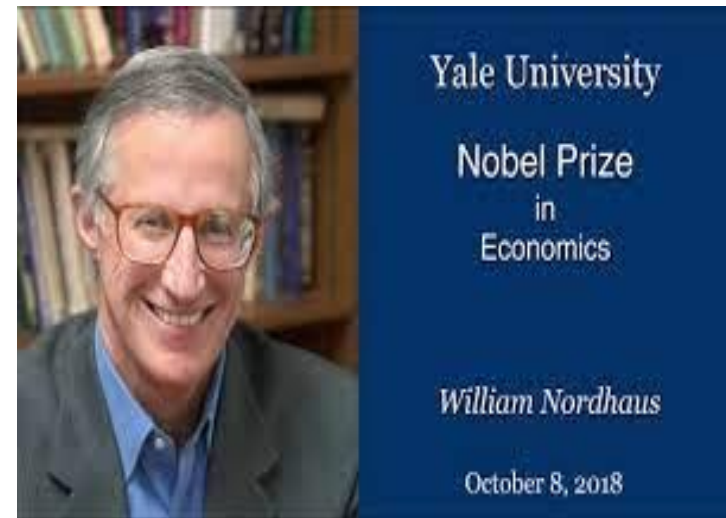


# Alternative carbon pricing proposals

## A: Universal carbon floor price



## B: Climate clubs (G7)



Inclusive vs. exclusive clubs

CBAM + Climate Club=Carbon Customs Union

## 4. Conclusion and way forward



Need for more global cooperation and coordination.



Multilateral agreement similar to the Paris Accord or Glasgow Climate Pact



Dissemination of environmental technologies

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Thank you!

