Responding to green trade barriers

Unpacking Border Carbon Adjustments (BCAs) & their implications for South Africa

BUSA ENVIRONMENT SUBCOMMITTEE MEETING

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Context

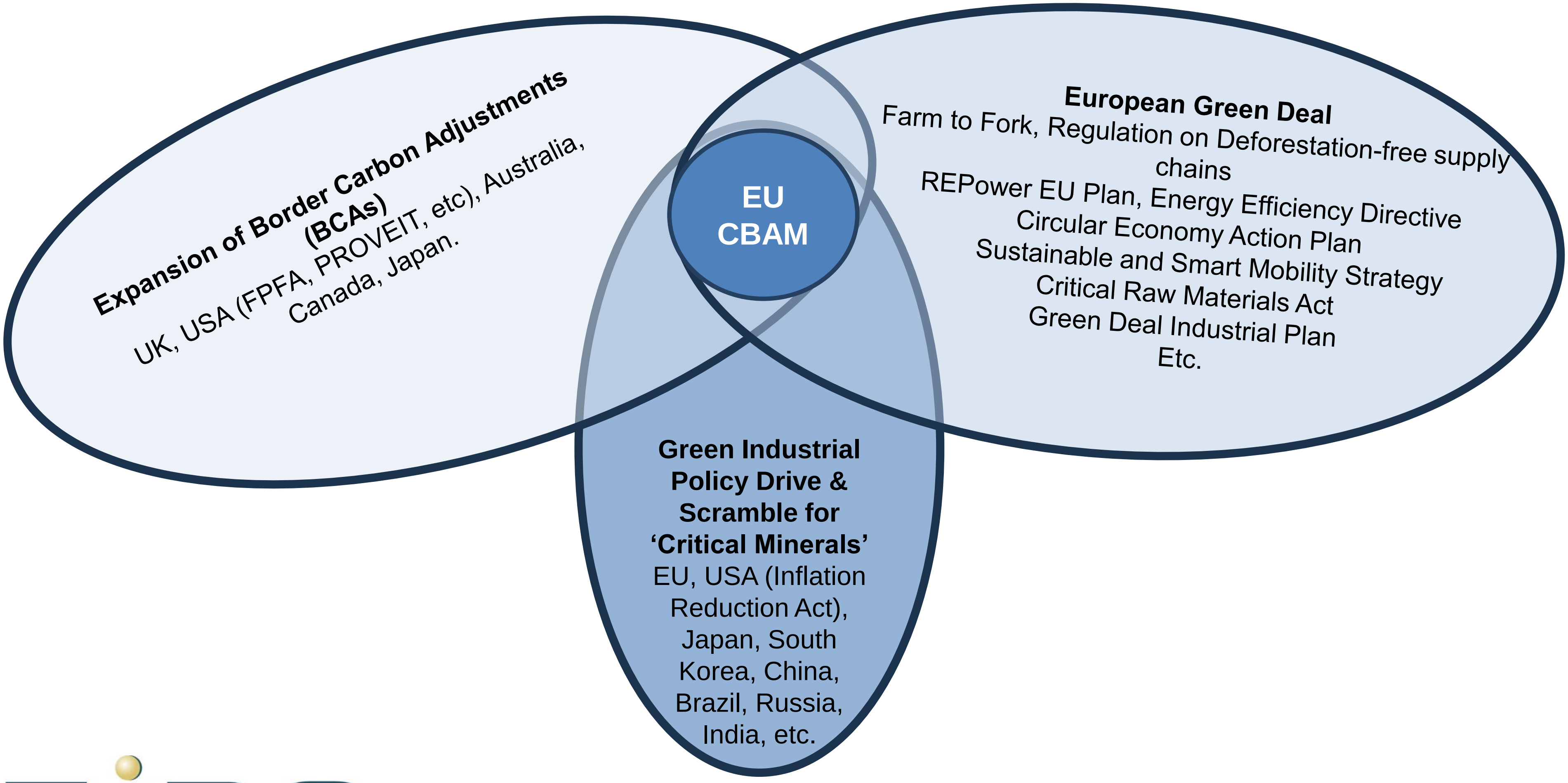
A global transition to sustainable development is under way and strengthening

- The transition to a sustainable development pathway is an all-encompassing endeavour, cutting across all spheres of government and policy.
- It is not only an environmental issue but also a socio-economic challenge which has ramifications at all levels of economic development, notably trade and industrial development
- From a trade and industrial perspective, it has implications on the composition and dynamics of entire value chains
  - Competitiveness, trade performance and industrial and economic development
  - Brings risks and opportunities

Key channels

- Climate change regulation, such as carbon pricing
- Shifts in trade patterns away from carbon-intensive products and/or jurisdictions
- Green protectionism, through trade-related climate change response measures, such as border carbon adjustments (BCAs) or other non-tariff barriers, is becoming more prevalent internationally (EU, USA, UK, Australia, Canada, Japan, etc.).
- Green industrial policy push (USA, EU, China, Brazil, etc.)
- Scramble for critical minerals

Context - CBAM: The tree that hides the forest



Overview of BCAs (Border Carbon Adjustments)

European Union (EU)

In 2019, the EU introduced the European Green Deal (EGD) - a multifaceted green policy instrument that affects every sector/industry and has global reach.
Key objective of this policy aims to reduce GHG emissions by 55% by 2030 compared to 1990 levels, and achieve carbon neutrality by 2050.

Included in the EGD is the CBAM as a policy tool with objectives to:

1. Raise revenue – Through a carbon border tax.
2. Promote climate action abroad – Amid increasing GHG emissions in the world.
3. Prevent carbon leakage – The avoidance of decarbonisation of high emitting entities (from jurisdictions that have stringent climate policies), by moving to jurisdiction with less jurisdiction that have less/or no stringent climate policies.

United Kingdom (UK)

In 2023 March, the UK conducted initial consultation on the design of the UK CBAM, and in December announced that it will introduce a Carbon Border Adjustment Mechanism (UK CBAM), to come into effect in January 2027.

A year later (March 2024), the UK announced consultations for the introduction of the UK CBAM – consultations ending 13 June. The UK CBAM mirrors the EU CBAM – with addition of new sector coverage (i.e., glass and ceramic).

Overview of BCAs (Border Carbon Adjustments)

<u>Other BCAs in policy discussions</u>

United States (US)

The US senate is introducing various bills to congress mirroring the objectives of BCAs, including:

- Foreign Pollution Fee Act (FPFA) – *Tax on Imports based carbon intensity*,
- PROVEIT Act - *The Act calls for a study on the carbon intensity of specific products in the US and select other countries*,
- Clean Competition Act – this *act aims to expand the scope of carbon taxes to include 25 sectors in addition to the sectors covered under the EU CBAM*.

Japan

Japan has been observing the EU CBAM with keen interest, and considering their own BCA (not been introduced in policy discussion yet)

Australia

In August 2023, the Australian government began assessing the viability of carbon taxation domestically

Canada

In 2020, the Canadian government outlined its intention to explore carbon border taxes to phase out the use of carbon-intensive products. Canadian carbon taxation broadly addresses and mirrors the EU CBAM in some respects with notable debates around certification.

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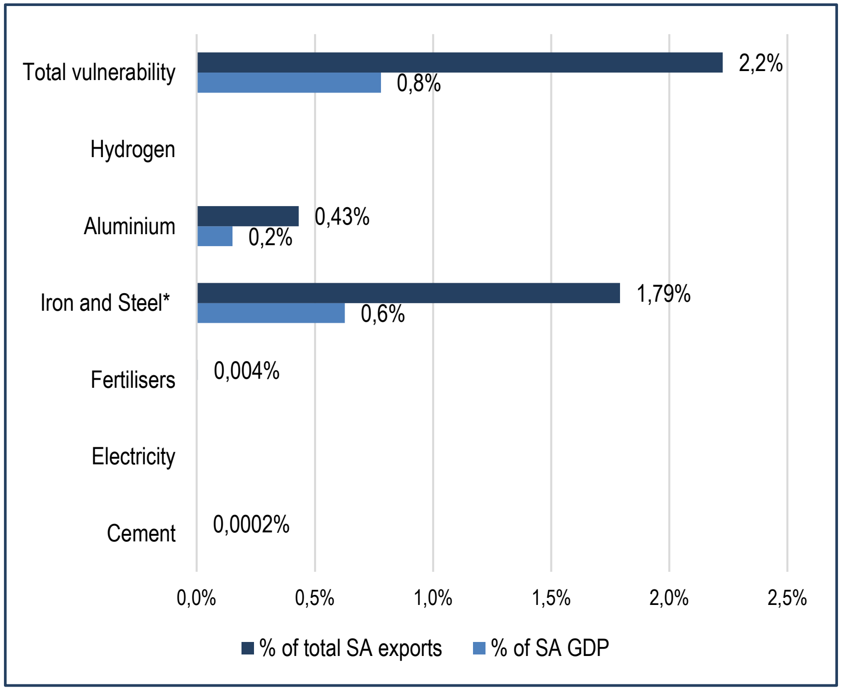
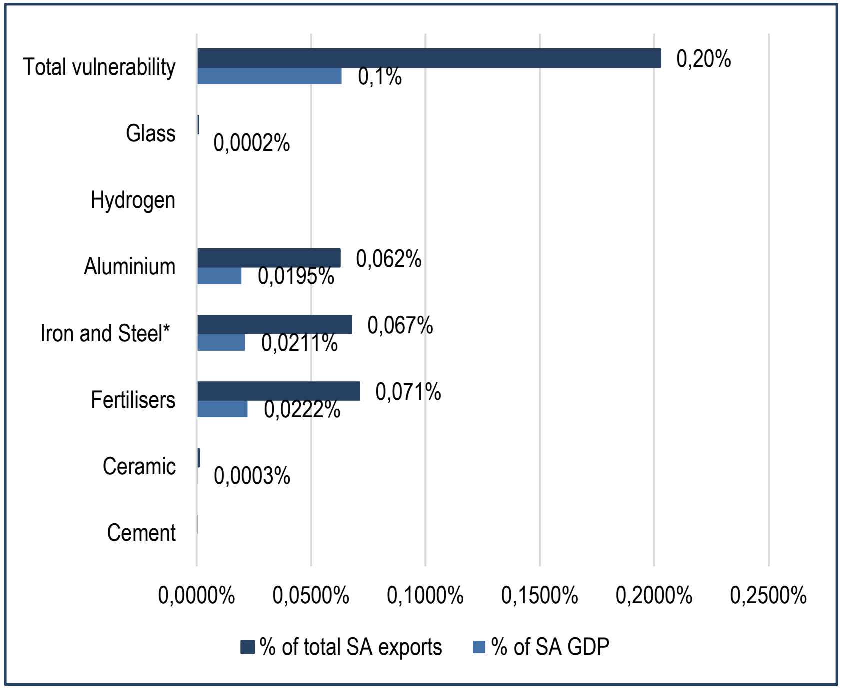
Impact of the EU & UK CBAM

South Africa's vulnerability to the EU CBAM



South Africa's vulnerability to the UK CBAM



Source: TIPS, 2023, 2024

*Iron and steel include input materials (also known as precursors) and articles of iron and steel

1. Based on the list of goods covered under the UK & EU CBAM, a total of **US$2,623 billion** (this is about **US$223 million** for UK and about **US$2,4 billion** for the EU CBAM) of South African exports (based on 2023 data) is at risk in the short term.

2. This is about 12% of all South African exports to the UK and EU, and about 2,4% of total South Africa exports to the world, and just 0.8% of total South African gross domestic product (GDP).

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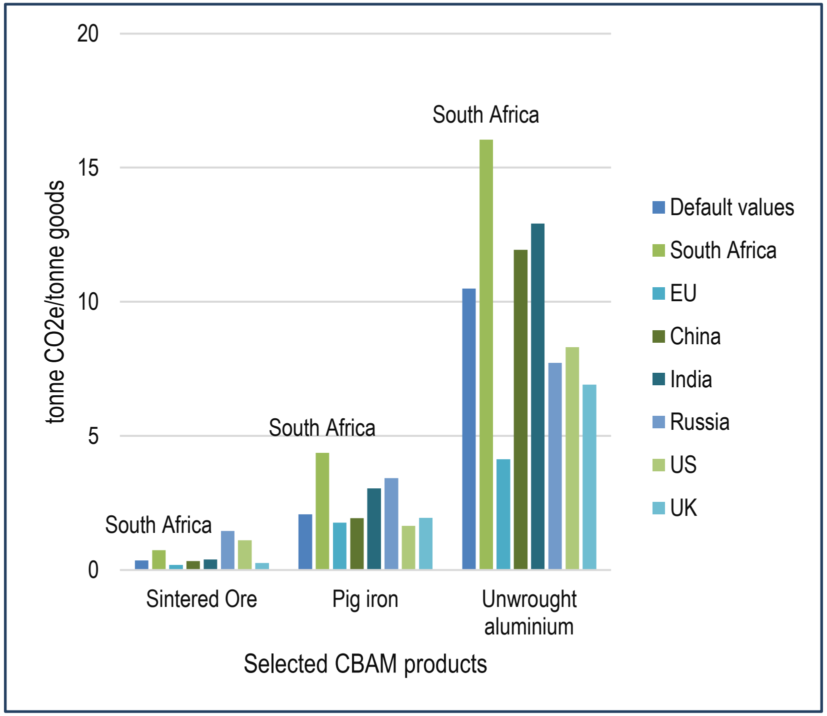
Fertilizers, Iron & steel, and aluminium sectors are in Jeopardy in SA

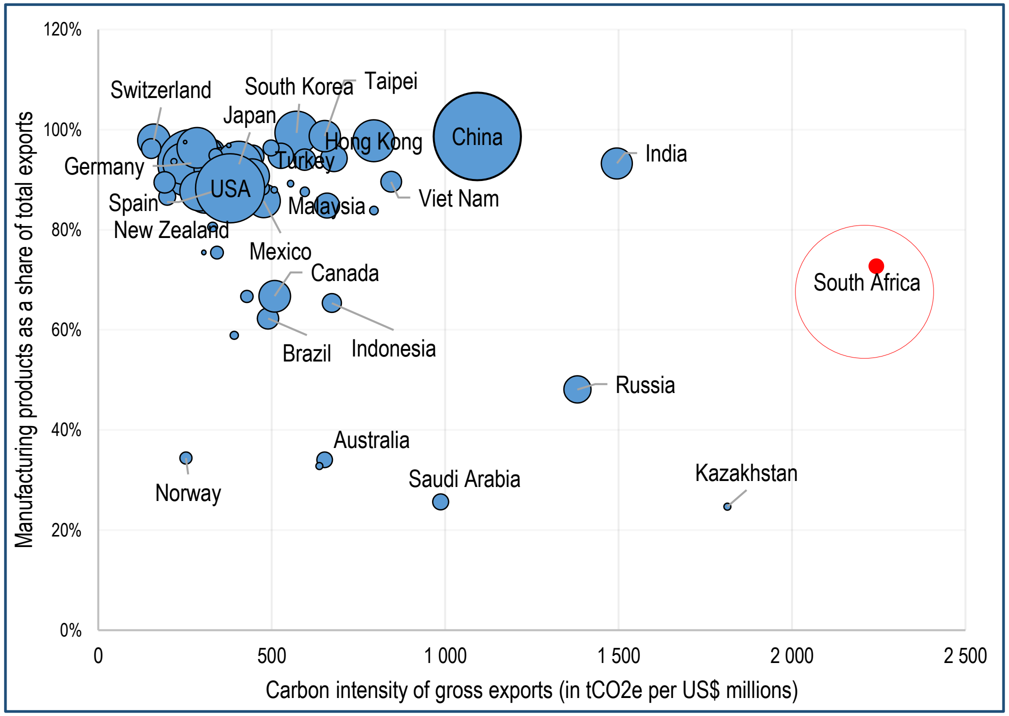
Impact of CBAM on Competitiveness

Total emissions embedded in selected iron and steel and aluminium products for selected SA competitors.



Source: TIPS forthcoming based on (European Commission)

Manufacturing export per country per carbon intensity



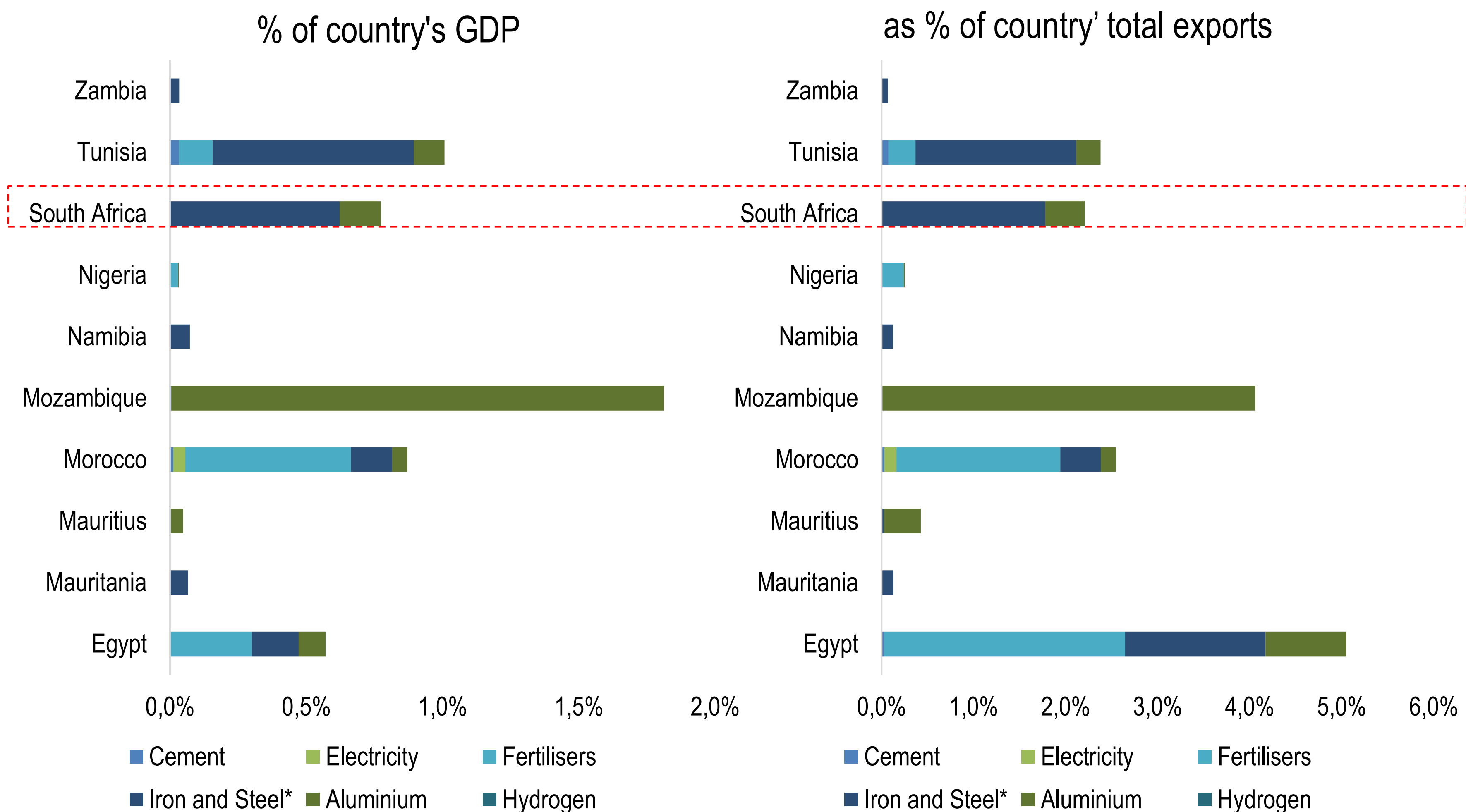
Source: TIPS, 2020

Goods will be expensive and less competitive to enter the EU & other market (s)

The general trend in the South African case is that the South African emissions embedded in CBAM products (especially iron and steel, and aluminium products) are higher than the EU's, higher than the default values, and higher than most competitors.

SA CBAM covered goods will be expensive to enter the EU & UK market as compared to other competitors

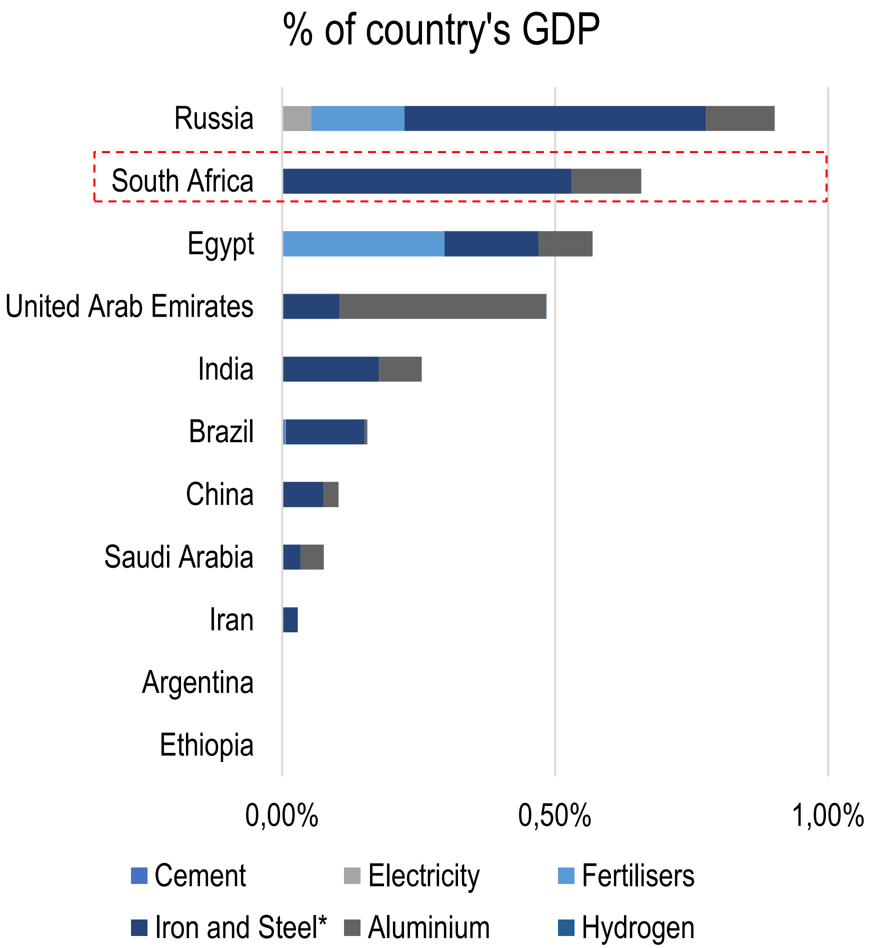
Impact of EU CBAM - South Africa in Africa (selected)

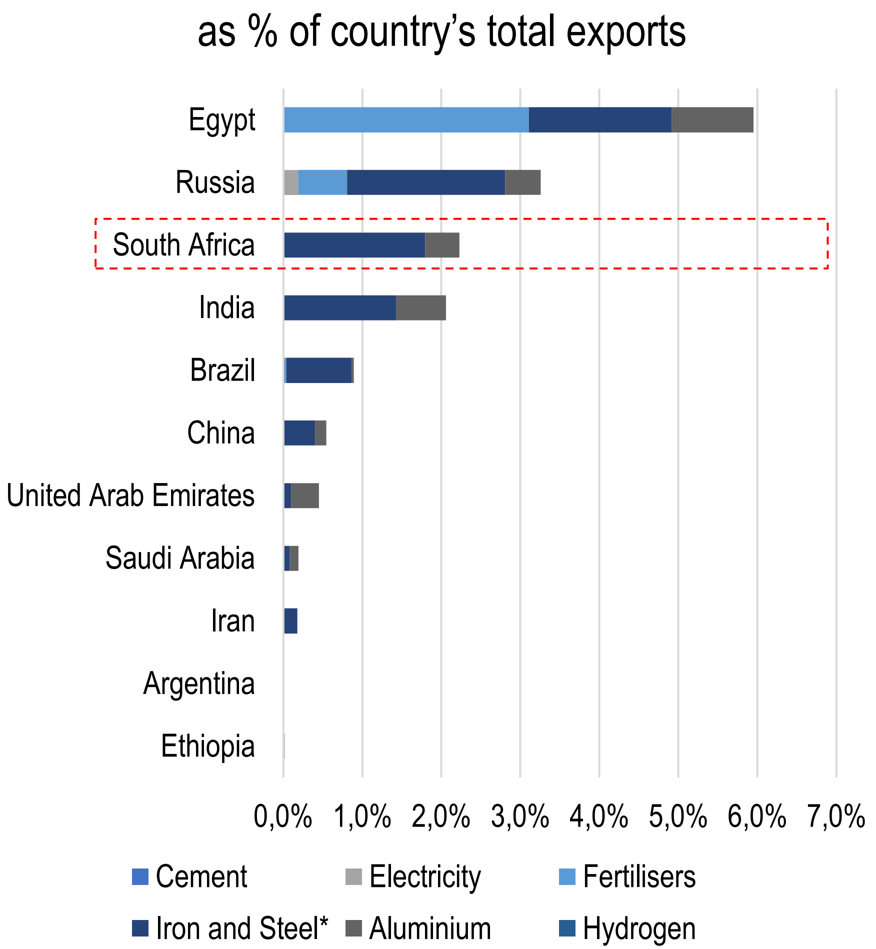


Source: TIPS, 2023

*Iron and steel include input materials (also known as precursors) and articles of iron and steel

Impact of EU CBAM - South Africa in BRICS+





Source: TIPS, *Forthcoming*

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Issues at hand – South Africa's readiness to the EU CBAM in transition

Lack of CBAM awareness in industry and government

i. Rushed implementation of CBAM
ii. Mechanism is unilateral – Creating an imposing to the climate change actions locally
iii. CBAM is still in legalese – Difficult to understand what is required from firms

This is aligned to the issues faced by EU declarants and firms in the EU

Domestic industrial challenges - Logistical, energy and coordination issues

i. Transnet issues
ii. Eskom issues – Loadshedding
iii. Lack of a coordinated response to CBAM both from government and industry

Misaligned GHG accounting infrastructure - CBAM & SAGERS not compatible

i. CBAM reports GHG emissions at a product level, while SAGERS report at an industrial level
ii. CBAM reports on a quarterly basis, while SAGERS report on an annual basis

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Issues at hand – Longer term issues

1. Slow decarbonisation of high emitting value chains (CBAM covered sectors)

2. Unambitious climate change policies (SA's commitment to climate change is not ambitious)

3. Low domestic carbon pricing by global standards (US$10 per tonne of emitted emissions, compared to US$50/t (Global corridor) and around US$90-100/t of the EU)

4. High dependence on coal of the South African electricity system (Around 80% of the electricity in SA is produced from Coal) – Causing the grid to be carbon intensive – creating issues in terms of indirect emissions

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How South Africa can respond to BCAs – Short-longer-term interventions

For starters, we need to start acting on the BCAs – Increasing awareness of these policies

Short-term interventions – Adapt and Engage

Adapt to BCAs
(No regret option)

Create **GHG accounting system** aligned to BCAs

Green industrialization – Through Retrofitting of industrial business models with green strategies (locally) including financing

Diplomatic engagements
(Ongoing strategy, low risk & uncertain chance of success)

Bilateral/plurilateral engagements

Engage the EU & UK on CBAM issues and open door for concessions
i.e., longer implementation/transition period, capacity building and technical assistance programs – To be funded by the EU & UK

Multilateral engagements

Raise CBAM issues at multilateral bodies, such the WTO, UNFCCC, G20, etc.

Medium-long-term interventions – Decarbonisation

Green Industrial policy
(Short term risk, long term benefits)
Greening high-emitting value chains

Energy policy
(No regret option)
Low carbon energy systems – Decarbonising Eskom

Fiscal policy –
(High risk but longer-term benefits)
Reforming South Africa's carbon tax to reflect global carbon pricing corridor of between US$50-100 /tCO2e

Trade Policy - Alternative Markets–
(High risk & expensive, longer-term benefits)
Increasing intra-African trade through trade in BCA covered goods

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Thank You.

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