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Briefing Note 2: Carbon Border Adjustment Mechanism (CBAM) – A challenge and an opportunity for developing countries

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The European Union's Carbon Border Adjustment Mechanism (CBAM), a border tax on embedded green-house gas emissions, was finalised in May 2023 and will begin implementation in October. The CBAM aims to equalise the price of carbon between EU products and imports by ensuring importers face similar carbon costs as EU manufacturers. Ultimately, it should help Europe achieve its climate objectives.

CBAM will enter gradually into force. In the first year, importers will only have to report on the direct emissions from production of the goods purchased, but no tax will be levied. Thereafter, CBAM will gradually ramp up, reaching full force in 2034. Importers will have to purchase digital CBAM certificates for each tonne of carbon generated by the goods they import. The price of the certificates will be derived from the weekly average auction price of the EU Emission Trading System.

The African Climate Foundation estimates that full implementation of CBAM will cost the continent about US$25 billion annually. It will have a particularly significant impact on South Africa, as one of the most carbon-intensive economies in the world for which the EU is a key trading partner. Europe purchases around a fifth of all South African exports. Based on 2022 data, about R53 billion worth of South African exports are at risk in the short term, and the number will rise as CBAM coverage extends to more products.

CBAM will likely have a major impact on the steel and aluminium industries. Likewise, the organic chemicals and plastics industries are also exposed (although their inclusion in the CBAM is still to be confirmed after the transitional period). South Africa exports to the EU around 80% of iron and steel products, and 20% of its aluminium products that fall under CBAM. The affected exports equalled 2.2% of total South African exports in 2022.

Japan, the UK, the US and Canada, among others, are considering measures like CBAM. Except for Canada, these countries are major export destinations for South African exports.

The BRICS countries (Brazil, Russia, India, China and South Africa) have opposed CBAM and other carbon taxes on trade. They are concerned that the costs will disproportionately impact the Global South. In effect, countries that have not contributed significantly to the climate emergency, including most of Africa, will still end up with substantially narrowed export markets. Some authors also argue that the measures are inherently protectionist, despite the proclaimed aim of responding to the climate emergency.

Minimising the negative effects of CBAM while continuing to disincentivise high-emissions exports could take several pathways. They include the following:

1. Reforming the World Trade Organization (WTO), to prioritise the climate emergency more fairly. In its current form, the WTO is not climate compatible, providing little policy space for countries, especially in the Global South, to shift to low carbon and climate resilient economies.
2. Helping South African companies to comply with the CBAM. In the short term, exporting firms are expected to have a Monitoring, Reporting and Verification system in place. This system will be piloted to report GHG emissions to the EU at the product level.
3. Analyse the possible pathways to decarbonise South Africa's (and Africa's) industrial value chains without disproportionately burdening working-class communities and national economies. The aim would be to ensure a just transition at both local and international level.
4. Explore the potential and opportunities of a regional carbon market for Africa. Such a market would enable African countries to retain revenues collected from the carbon market, rather than paying into the EU budget through the CBAM. These funds could then be leveraged for continental decarbonisation purposes. Also, the use of carbon credits can open a window to trade off the carbon credits in international carbon markets for Africa's debt.