Carbon Border Adjustments Mechanisms – Position of Eurometaux

ERCST Roundtable

Cillian O'Donoghue, Director of Climate & Energy, Eurometaux

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Our key messages for today

1

The non-ferrous metals (NFM) = the most electro-intensive industry in Europe

More impacted by indirect than direct CO2 Costs

2

But…having analysed the measure, NFM don't wish to be included in the CBAM pilot phase

We believe the current measures (indirect costs compensation & free allowances) are a more optimal approach for NFM

for 4 main reasons:

1. Inability to have a border charge on indirect costs (Not emissions) in a WTO compatible manner
2. Complex value chain
3. Likelihood of circumvention
4. No possibility for rebates for exports

3

We thus see increased carbon leakage risk exposure as a result of the 55% GHG emissions target but no increased carbon leakage protection

55% target will inevitably lead to high carbon prices

- ✓ Given that CBAM is not a viable alternative for our sector, the result of the higher 2030 target will be further closures
- ✓ **Instead of CBAM, the Commission should look at the regulatory framework 'toolbox' needed for energy intensives**

3 key facts about non-ferrous metals production in Europe

Electro-intensive

One of Europe's most electro-intensive industries

Al Aluminium — Electricity = ***38-45%*** of production costs

Zn Zinc — Electricity = ***31%*** of production costs

Si Silicon — Electricity = ***30%*** of production costs

For the NFM, electricity is a key localisation factor. However, European producers face higher power prices than the rest of the world.

Price-taker

As price-takers, we cannot pass on any regulatory costs to the customer

$ + EU

Metals priced globally by London Metals Exchange

Electricity costs vary from country to country

=

Automatic competitive disadvantage on global market

Rising demand being replaced by imports with higher carbon footprint*

Metals demand increase by 2050*

+300% **+200%** **+1000%**

Vs.

Tonnes of CO_2

Al 1 tonne

China	**20**
Europe	**7**

X 2.5 more CO2

11/35

European aluminium smelters closed since 2007

Non-Ferrous Metals are likely the most exposed sector to Carbon Leakage

* *IES-VUB, 2019: Metals in a climate-neutral Europe*

** Source: World Bank 2017

Why we believe a CBAM cannot be efficiently designed to cover non-ferrous metals?

Current indirect costs compensation and free allowances are more effective than CBAM at addressing any carbon leakage risk due to:

1 Inability to calculate indirect carbon costs

i. Indirect costs are decoupled from indirect physical emissions (due to the power market dynamics). The public consultation only refers to indirect emisslons not indirect costs

ii. Indirect costs in Europe vary between regions and Member States, making it impossible to be set at the EU level

iii. Major questions on whether it can be designed in a WTO compatible manner

2 NFM value chain complexities

NFM value chains are characterised by:

(1) Many production steps;
(2) Intertwined material flows
(3) Strategic links with other energy intensives in downstream applications

This complexity makes very difficult to capture the CO2 embedded content in metals products.

But, applying CBAM only upstream would lead to higher costs for downstream producers and move production outside Europe

3 Possibility to circumvent

1. Avoidance based on slight change in the product

2. Transshipment strategies

3. Resource shuffling

Eg: 90% of Chinese primary aluminum production based on coal-fired power, whereas the remaining 10% is hydropower.

So it would be easy to allocate this 10% for exports to Europe and maintain the major carbon intensive production.

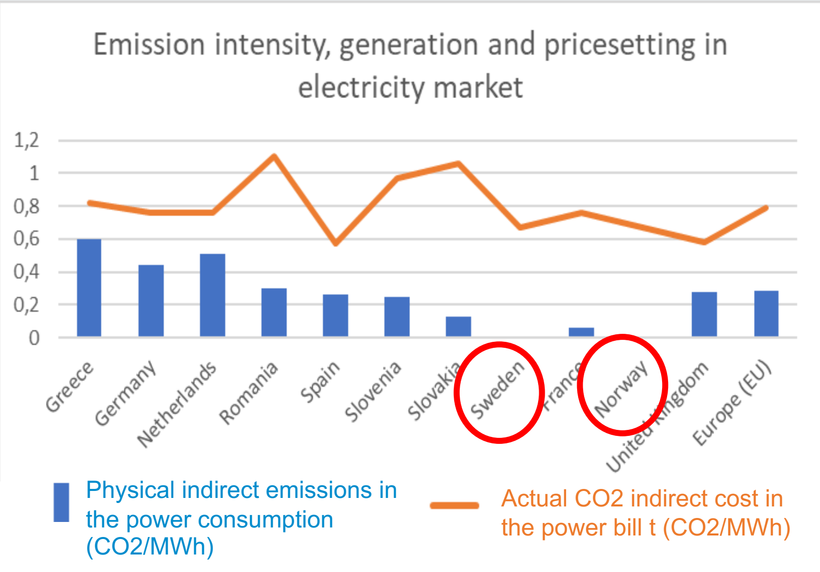
4 Lack of Export Rebates

One underlying problem with all of the options mooted in the Commission's consultation is:

How to handle the exports out of the EU?

The EU's specific CO2 costs will have to be reimbursed somehow in order to make exports competitive. Most likely this will be regarded as an export subsidy by the WTO and hence be challenged by our global competitors

Indirect CO2 physical Emissions are not correlated with Indirect CO2 Emissions Costs



Indirect costs vs. indirect emissions

There's a huge difference between actual power GHG intensity (indirect emissions) vs intensity of the price setting technology in power market (indirect cost)

The indirect CO2-costs in EU are a result of the marginal price-setting mechanisms in the power market, not an expression of the indirect emission levels in products.

→ **Hence indirect costs are not the same as tax on the CO2 content of indirect emissions**

How to calculate indirect emissions costs?

- ✓ Indirect costs vary within the European regions while the CBAM will be set at EU level.
- ✓ EU's own Guidelines (21.09.2020) describe 2 different methodologies: 1) Market based CO2 emission factor based on margin setting technology in power market or 2) Average of CO2 intensity of electricity produced from fossil fuels in different geographic areas

- ✓ **European smelters extra climate costs on power prices (indirect costs) have no relation to the physical generation emission footprint.**
- ✓ **It seems not possible for a CBAM to address indirect costs. Thus indirect costs compensation would need to be maintained.**
- ✓ **A CBAM on top of indirect carbon costs to address indirect emissions is feasible.**

A Combination of Policies are Needed to Protect Industry from Carbon Leakage Today and Facilitate Industrial Transformation to Climate Neutrality

Today: Phase IV – 2021 - 2030

Tomorrow: Post 2030 up to 2050

- ✓ **Free allowances**
  (Including changes to avoid CSCF)
- ✓ **Indirect CO_2compensation**
  (Targeted approach to proiect the most exposed)

Other measures needed:

- ✓ **Support for new tech & investments**
- ✓ **Create market for low-CO2 products**

1. **Indirect CO2 costs**: Carbon leakage protection measures focusing on electricity/indirect CO2 costs *until power is fully decarbonised (means pass through factor is zero) or until other regions face similar indirect carbon costs.*
2. **Direct CO2 costs:**Carbon leakage measures to address direct CO2 costs *(*until we see similar carbon pricing arrangements outside the EU)*
3. **Technological breakthroughs**: Support on low-CO2 breakthrough technologies (innovation funding, contracts for difference, etc)
4. **Low carbon products**: Create markets and demand for low carbon products (Public procurement, standardisation, product labelling, etc)
5. **Charges to the consumer:** Creates incentives for choosing & using climate friendly materials

2020 2030 2040 2050

THANK YOU

Cillian O'Donoghue

Energy and Climate Change Director

odonoghue@eurometaux.be

@Eurometaux

www.eurometaux.eu

Avenue de Tervueren, 168 | B-1150 Brussels | Tel: +32 (2) 775 63 11 | eurometaux@eurometaux.be