



The Effects and Implications of Applying the Carbon Border Adjustment Mechanism (CBAM) on Egyptian Exports

March 2024

Introduction:

The phenomenon of climate change is one of the most important environmental problems resulting from increasing in human activities and consumption of non-renewable energy, which poses numerous threats to the global economy, international security, and the development of societies. As world is experiencing unprecedented rates of global warming and rising temperatures, 197 countries adopted the Paris Agreement during the 21st Conference of Parties (COP21) in 2015; To address climate change and its negative impacts. The agreement aims to limit global warming by ensuring that the increase in the global average temperature remains well below 2°C and striving to limit it to 1.5°C.¹ Fifty countries have also adopted carbon pricing² mechanisms, yet the average global carbon price currently stands at approximately two dollars per metric ton of CO₂, which is largely insufficient to restrict emissions and achieve the zero emissions target by 2050.³

The EU has launched the world's first system of border taxation on carbon dioxide emissions from imported high-carbon products, such as iron, steel, cement, aluminum, and fertilizers, as one of the mechanisms to meet the Paris climate agreement commitments. This is to prevent more polluting foreign products from hindering the EU's attempt to mitigate climate change, and to guide exporting countries, especially the developing countries, to adopt a less polluting production process. This requires procedures on all levels and financial instruments to curb climate change, with "carbon taxes" being one of those new tools to achieve these goals and help reduce greenhouse gas emissions from coal and other polluting fossil fuels.

Although this tax is scheduled to come into effect in 2026⁴, the announcement marks the start of the initial phase of the CBAM, which will require EU importers to report greenhouse gas emissions resulted from the manufacturing and production of the above-mentioned goods.

Essentially, this mechanism aims to place both European and foreign manufacturers on an equal footing in terms of environmental impact.

Objectives of applying the CBAM

CBAM aims to counter carbon leakage, which occurs when European manufacturers move production to countries with less stringent environmental standards, leading to an increase in total global carbon emissions, a loss of European market share to foreign competitors, and a threat to the effectiveness of global carbon reduction policies.

¹ United Nations. "The Paris Agreement". Available at: <https://www.un.org/ar/climatechange/paris-agreement>

² **Carbon pricing is** a rational fiscal and economic policy, and an efficient way to mobilize revenue – whether through an increased carbon tax or through a low-cap carbon market that is easier to manage and harder to evade than other taxes.

³ Ashour. Sally. "Global trends in carbon taxes." Egyptian Center for Strategic Studies. 5 July 2023. Available at: <https://ecss.com.eg/35001/>

⁴ European Commission. Carbon Border Adjustment Mechanism. Available at: https://taxation-customs.ec.europa.eu/carbon-border-adjustment-mechanism_en

Additionally, the mechanism plays a crucial role in promoting the transition to renewable energy, as the European countries aim to boost the clean energy transition, reduce greenhouse gas emissions by 55% this decade compared to 1990, and achieve climate neutrality by 2050.

Concisely, CBAM is one of the leading steps in the fight against climate change and it is a crucial policy aimed at reducing the negative effects of global warming. Alongside, the objectives of CBAM implementation include enhancing the ability of local industries in European countries to compete with relatively cheap products imported from countries that do not charge carbon taxes.⁵

Application of CBAM

The application system of the CBAM is based on the implementation of 4 steps:

1. Assess and calculate carbon content by identifying gases emitted during different stages of the manufacturing process.
2. The carbon price for the emission of these gases will be determined according to the local carbon price of the importing country or region.
3. Obtaining CBAM certificates; Importers must purchase certificates equivalent to the carbon content⁶ of their imports.
4. The customs authorities will be responsible for verifying the carbon price of the imported goods, and then start imposing the appropriate carbon limit tax based on the emissions certificates provided by the importer.

It is worth noting that the implementation of the CBAM may vary according to the laws of each country and the legislation of each region.⁷

Industries that will be affected by CBAM

CBAM is expected to affect many industries and products, especially high-carbon industries such as iron and steel, cement, fertilizers, aluminum, electricity, and hydrogen. In addition, CBAM is expected to extend its scope to all products covered by the EU emissions trading system, and therefore proposed to include chemicals and polymers in the mechanism by 2026.⁸

The Implications of the European Union's decision to impose CBAM

Developing countries and exporting companies have expressed concerns about the European Union's Carbon Border Adjustment Mechanism (CBAM). as the mechanism does not take into account the priorities and conditions of climate and development actions in these countries. Additionally, this tax will

⁵ Gamal. Bassant. "European efforts: Carbon Border Adjustment Mechanism in the face of climate change." Egyptian Center for Strategic Studies. 22 October 2023. Available at: <https://ecss.com.eg/37428/>

⁶ **Carbon content equivalency certificates** are certificates that serve as evidence that the carbon emissions associated with imported goods have been calculated and offset at the carbon price set by the importing country or region.

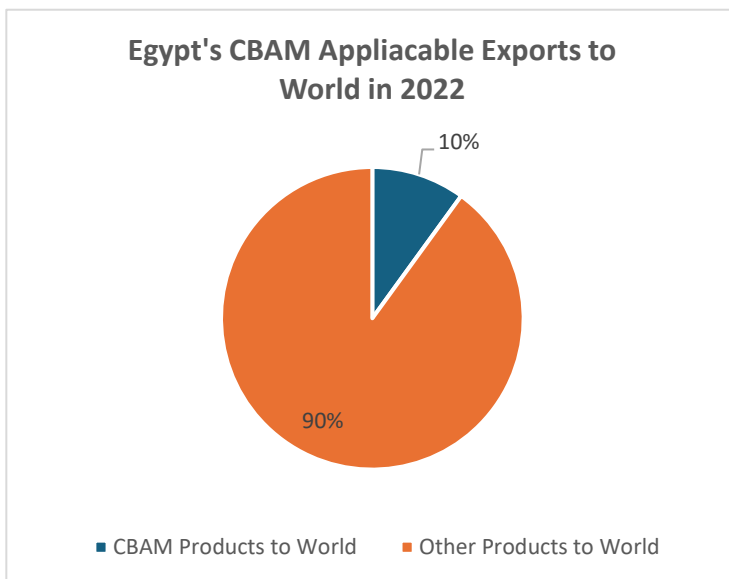
⁷ Oropeza. Jesus. "The Implications of the EU Carbon Border Adjustment Mechanism on the Environment and Global Trade". 4 August 2023. Available at: <https://earth.org/the-implications-of-the-eu-carbon-border-adjustment-mechanism-and-for-the-environment-and-global-trade/>

⁸ Durantez, Mariam, and Obern, Calli." The EU's Carbon Border Tax Could Hurt Developing Countries". 24 June 2022. Available on: <https://www.project-syndicate.org/commentary/eu-carbon-border-tax-could-hurt-developing-countries-by-miriam-gonzalez-durantez-and-calli-obern-2022-06/arabic>

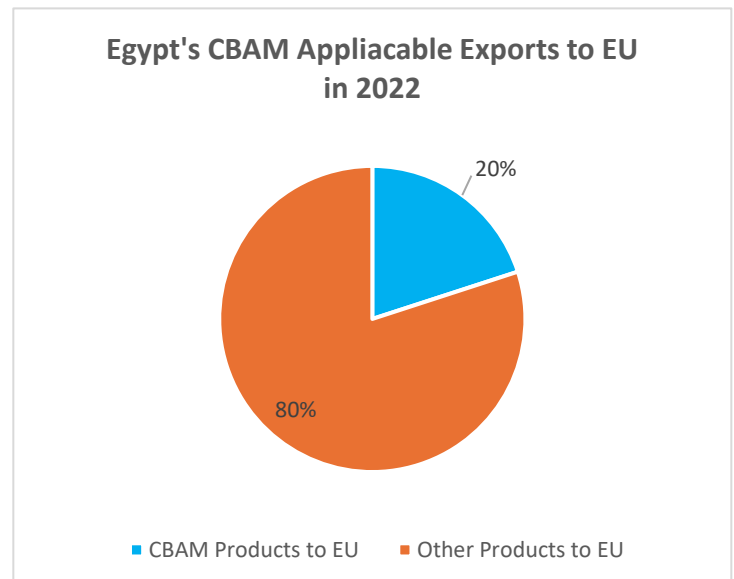
affect the activities of companies in some of the targeted industries by CBAM, which will negatively affect the exports of these countries and thus their economic growth⁹. Moreover, the 2023 Development and Trade Report notes that it is unfair for poor developing countries to bear the same cost as rich developed countries when imposing a tax on this new mechanism.¹⁰

Egypt is one of the countries that expected to be adversely affected by the implementation of this mechanism, as exports falling under CBAM make up 10% of Egypt's total exports to the world.¹¹ In addition, exports impacted by CBAM account for 0.3% of Egypt's GDP.¹²

At the EU level, these exports account for nearly 20% of Egypt's total exports to the EU¹³, which reached \$12.313 billion in fiscal year 2022/2023.¹⁴



Source: International Trade Centre



Source: European Service for Foreign Affairs

Challenges facing Egypt when Applying CBAM

Egypt's exports to the EU depend heavily on CBAM products, so the volume of Egypt's exports to the EU market as well as the carbon intensity of the Egyptian economy, increases the risks and potential negative impact on Egypt. **The main challenges that Egypt is expected to face can be summarized as follows:**

⁹ LYNX Strategic Business Advisors. "Policy Brief on The Implications of CBAM on Egypt". 11 September 2023. Available on: <https://www.lynxegypt.com/assets/pdfs/LYNX-Policy-Brief-CBAM.pdf>

¹⁰ UNCTAD. Trade and development report 2023. Available at: https://unctad.org/system/files/official-document/tdr2023_en.pdf

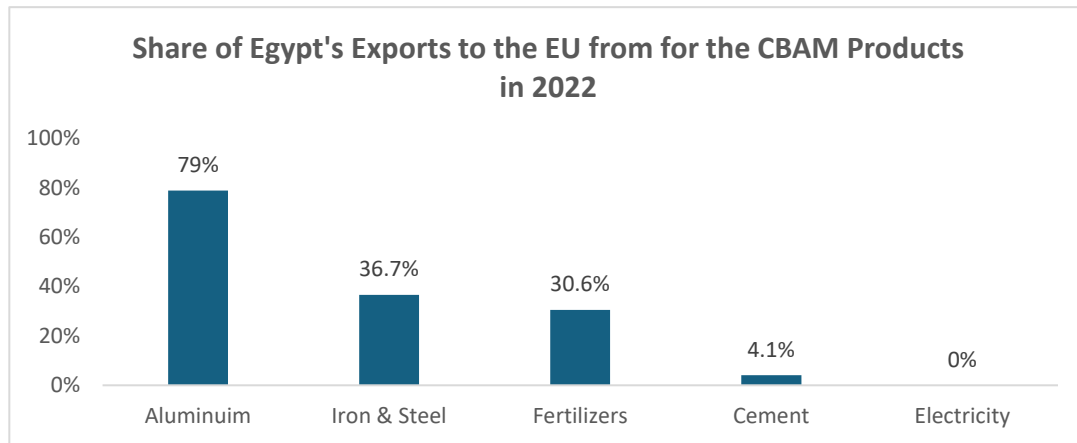
¹¹ ITC. Accessed on: 18 March 2024

¹² World Bank. Relative CBAM Exposure Index. 15 June 2023. Available at: <https://www.worldbank.org/en/data/interactive/2023/06/15/relative-cbam-exposure-index>

¹³ EEAS. "EU-Egypt climate cooperation can help boost both decarbonization and growth". 11 February 2024. Available at: [OP-ed: EU-Egypt climate cooperation can help boost both decarbonisation and growth | EEAS \(europa.eu\)](https://eeas.europa.eu/op-ed/eu-egypt-climate-cooperation-can-help-boost-both-decarbonisation-and-growth_en)

¹⁴ Central Bank of Egypt.

- Egypt relies on natural gas as its primary source of energy, which is used in various industrial processes and emits carbon gases, increasing the risks associated with the negative impact of CBAM.
- CBAM is expected to negatively impact the competitiveness of Egyptian companies and products in the European market due to the carbon intensity of Egyptian exports.
- The new policy mechanism increases risks related to Egypt's Sustainable Development Goals, including efforts to increase climate sustainability.
- CBM represents a major challenge for Egypt's six target sectors, particularly the fertilizer, cement and aluminum industries; For example, about 79% of Egypt's aluminum exports are directed to the EU market.

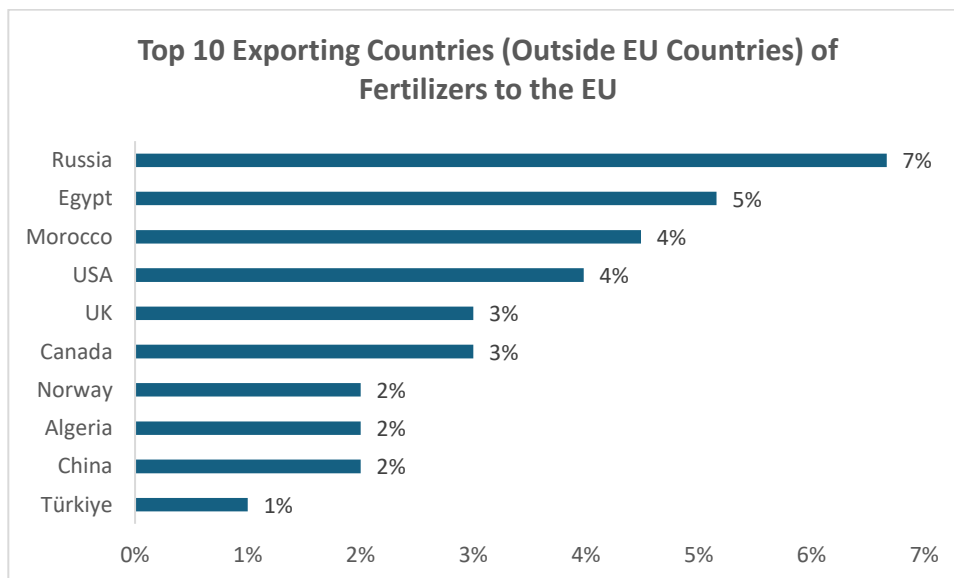


Source: World Bank. ¹⁵

- Egypt is the second largest fertilizer exporter to the EU in 2023 , accounting for 5% of total fertilizer exports to the EU, illustrating the challenge posed by the CBAM to the industry in Egypt once fully implemented ¹⁶.

¹⁵ World Bank. CO2 Emissions Intensity, by Product. <https://www.worldbank.org/en/data/interactive/2023/06/15/relative-cbam-exposure-index>

¹⁶ ITC. Accessed on: 18 March 2024



Source: International Trade Centre

- Egypt's exports will be affected by the implementation of CBAM; The World Bank released a report indicating that declines in exports of electricity, oil, and chemicals (especially fertilizers) are expected by 8.3%, 4.3% and 3.9%, respectively.¹⁷

Opportunities for Egypt to confront CBAM.

Despite the challenges that Egyptian exports could face, the CBAM could be seen as an opportunity for Egypt to capture the European market. The opportunity is as follows:

- Egypt has lower carbon emissions than its counterparts from other countries; Carbon emissions in Egypt account for about 0.6% of total emissions, compared to carbon emissions in China and India of 18.8% and 4.9%, respectively.¹⁸ As part of its drive to decarbonize value chains, Egypt scored a total of 79 points in the Sustainable Energy policies and Systems Index, which is higher than the Middle East and North Africa.¹⁹
- Egyptian ports are close to the European Union.
- The multiplicity of renewable energy sources in Egypt and the expansion of national projects to produce clean energy. For example:
 - ✓ The Benban Solar Park in Aswan aims to improve access to clean energy, promote local economic development, and reduce fossil fuel consumption.²⁰

¹⁷ World Bank. "Country Climate and Development Report". 8 November 2022. Available on: <https://documents1.worldbank.org/curated/en/099510011012235419/pdf/p17729200725ff0170ba05031a8d4ac26d7.pdf>

¹⁸ Regulatory Indicators for Sustainable Energy. Egypt. Available on: <https://rise.esmap.org/country/egypt-arab-rep>

¹⁹ Regulatory Indicators for Sustainable Energy. Egypt. Available on: <https://rise.esmap.org/country/egypt-arab-rep>

²⁰ United Nations. "A huge project to generate electricity from solar energy in Aswan in cooperation between Egypt and the United Nations." 25 January 2024. Available at: <https://shorturl.at/eABL3>

- ✓ A decision was issued to partially replace the mandatory replacement of alternative fuel in the cement sector to replace a proportion of imported coal in 2021 as the state seeks to reduce the clinker content in cement by up to 80%. ²¹
- ✓ Construction of a wind power project at the Suez Gulf complex on the Red Sea coast, in early 2023. ²²
- ✓ The establishment of the Industrial pollution Control Project - Phase III (EPAP III) in partnership with the European Union, the French Development Agency (AFD), the European Investment Bank and the German Construction Bank (KfW), to support Egyptian industries to achieve compliance with environmental laws by granting soft loans to companies to adjust their environmental conditions, with a grant of up to 10-20% funded of about 145 million euros. ²³
- ✓ Signing 7 agreements with global developers (Bash Global, Smart Energy, El Tokkel Geela, AMM Power, United Energy Group, Gamma Construction and Meridiam, SK E&C Plant-C&C North Africa) in green hydrogen and renewable energy worth \$40 billion. ²⁴

The most important recommendations and proposed policies

All the above factors contribute to giving Egypt a competitive advantage to move faster toward the implementation of the carbon limit adjustment mechanism and gain a greater market share in exports to the EU.

In this regard, Egypt should establish its own policies and standards for implementing climate and development action in line with the country's priorities, enhancing its potential, and increasing its competitiveness. **These procedures are as follows:**

- Immediate commencement of emissions mitigation in the industries targeted by the CBAM in the context of equitable transition. Therefore, the industrial sectors in Egypt will have to increase their technical capacity regarding CBAM monitoring, reporting and verification procedures, especially in the 6 target sectors.
- Recognize the importance of cooperation between the EU and Egypt on the establishment of voluntary carbon markets that²⁵ enable Egypt to exploit carbon credits to reduce emissions and thus increase the competitiveness of its products.

²¹ Farag. Wael. "Egypt's efforts to reduce carbon emissions." Al-Ahram Center for political and Strategic Studies. 25 October 2022. Available at: <https://acpss.ahram.org.eg/News/17652.aspx>

²² Map of Egypt projects. Available at: <https://shorturl.at/knq10>

²³ Ministry of Environment. Available at: <https://www.eeaa.gov.eg/Project/102/Details>

²⁴ Public Information Authority. February 28, 2024. Available at: <https://shorturl.at/rxB25>

²⁵ **Voluntary carbon markets:** A market in which companies, governments and individuals can buy and sell credits that represent reductions in carbon dioxide emissions, which can be used to offset emissions that cannot be reduced by other means, through the implementation of emission reduction projects in other parts of the world. such as installing renewable energy sources, implementing energy efficiency measures, or planting a forest. - Arab Center for the sustainability of Civil work.

- EU participation in capacity building in developing countries such as Egypt and providing financing and technical assistance for clean energy projects to help reduce carbon emissions from high-emission industrial sectors. ²⁶
- Documenting the carbon footprint of Egyptian exported goods, which increases the competitiveness of Egyptian exports in the EU markets. ²⁷

²⁶ LYNX Strategic Business Advisors. "Policy Brief on The Implications of CBAM on Egypt". 11 September 2023. Available on: <https://www.lynxegypt.com/assets/pdfs/LYNX-Policy-Brief-CBAM.pdf>

²⁷ Verofax "Automated export documentation for rapid compliance with updated EU carbon tax laws".