



Border Carbon Adjustments and Industrial Competitiveness in a European Green Deal

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Abstract As part of the European Green Deal, the EU is considering the introduction of a Border Carbon Adjustment (BCA) to ensure that the price of imports into the EU more accurately reflects the environmental costs of their carbon content. BCAs could be an alternative to free allocation to trade-exposed sectors as a measure to address the risk of carbon leakage in the EU's Emissions Trading System. While a BCA for exports is not categorically excluded, it is less likely to be consistent with WTO rules and therefore less likely to be proposed than an import-only BCA. A key point is that replacing free allocation by an import-only BCA would weaken the competitiveness of EU producers in foreign markets. The reason is that free allocation also helps support the cost competitiveness of domestic products that are exported to markets outside the EU. Therefore, a move to import-only BCAs does not necessarily make redundant the continued use of free allocation to help safeguard overall industrial competitiveness. While combining an import BCA with free allocation can increase the risk of legal challenges, such risks may be reduced with an appropriate design. More broadly, policymakers need to navigate a complex trade-off between competitiveness support, a stronger carbon price signal, and extra fiscal revenue.

Keywords Border carbon adjustment, carbon pricing, competitiveness, international trade

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