05 Mar

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# R27 billion in exports under threat

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**BUSINESS**

About $1.5 billion (R27 billion) a year of South African steel, aluminium and iron exports to the eurozone are at risk after the EU introduced the Carbon Border Adjustment Mechanism (CBAM), a strategy for reaching the EU's 2050 carbon emissions goal.

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The CBAM, which was introduced to help EU industries decarbonise and prevent carbon leakages – a situation in which a company decides to move its production from a country with stringent policies to a country that is more lenient, leading to an increase in greenhouse gas emissions – will have far-reaching consequences on global trade and the wider energy transition.

It is a border tax on embedded greenhouse gas emissions of carbon-intensive products imported into the EU, and will mean that South African exporters will pay tariffs equal to carbon prices paid by EU manufacturers.



A policy brief by think-tank Trade & Industrial Policy Strategies, penned by economists Valentia Lerato Monaisa and Seutame Maimele, suggests that the country's steel, aluminium, iron, cement, fertiliser, electricity and hydrogen exports to the EU – one of its major trade partners – are in jeopardy.

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The initial CBAM proposal only covered direct emissions from electricity and 29 product categories from the cement, fertiliser, iron, steel and aluminium sectors.

However, in the new, provisionally agreed to CBAM proposal, the scope has been extended to include hydrogen as well as indirect emissions (to be included in a well-circumscribed manner by 2026), certain precursors (input materials) for production of the covered products, and some downstream products such as screws, bolts and similar articles.

"Iron and steel exports face significant risk. About 26% [in value] of products included in the CBAM are exported to the EU. Iron and steel exports covered by the CBAM accounted for 4% of total South African exports in 2021," the brief reads.

> **South African iron and steel production is highly carbon-intensive. Iron and steel production is the largest source of industrial processes and product use [IPPU] sector emissions, producing 7 725 [gigagrams of carbon dioxide equivalent] (about 24% of IPPU sector emissions in 2017) in South Africa.**

At a recent webinar hosted by the Presidential Climate Commission, John Ward, who authored a working paper on the impact of the CBAM proposal, found that the CBAM would lead to a 30% to 35% decline in exports from Africa, while South Africa's exports to the EU would fall by 4%.

Ward said the inclusion of green hydrogen would aid the country's ambitions in line with the Just Energy Transition Investment Plan.

"This could be a stimulus when it comes to [hydrogen] exports because South Africa's green energy exports will be attracting a much lower charge from the CBAM, compared with grey hydrogen exports."

Ward said South Africa had two proposals to respond to the CBAM.

"It's either an aggressive stance of seeking to undermine the entire CBAM construct through a legal challenge at the World Trade Organisation [WTO], or negotiating with European policymakers to mould some of the design features of the CBAM in favour of South African producers."

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Speaking at the same webinar, University of Cape Town adjunct Professor Faizel Ismael pointed out that "this measure provides protectionism and support for EU companies in a bid to remain competitive and to compete with other countries around the world".

"So, it's really a competitiveness rather than an environmental instrument. It is unilateral and there is no doubt that its legality under the WTO is very questionable and, in my view, illegal.

"It also violates a number of principles of the WTO, including article 1, as it doesn't take into account special and differential treatment."

South Africa's heavy reliance on coal-based power generation makes it one of the most highly carbon-intensive exporters of metals to European markets and other regions. It is therefore likely to face added tariffs, reducing its competitiveness and the value of its future exports.

The country's carbon intensity in metals exports stands at about 5 000 tons of carbon dioxide equivalent (tCO2e) per $1 million, far exceeding other metal-exporting countries.

"The CBAM will impose significant compliance costs. Exporting firms will have to account for, report and verify the embedded emissions in their products," said the policy brief.

The CBAM requires third-party verifiable carbon audits, which can be costly even for large firms.

"A domestic carbon reporting system, which could be led by the department of forestry, fisheries and the environment, could ease the administrative burden of South African firms," the brief suggested.

Also at risk are organic chemicals and plastics exports, which will now be included, although their inclusion in the CBAM is still to be confirmed after the transition period from October this year until 2026.

During this period, the burden will be administrative rather than financial, as importers will only report direct greenhouse gas emissions embedded in their export to the EU.

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"The organic chemicals sector's exposure to the CBAM was around 30% [in value] of the products covered by the CBAM exported to the EU in 2021. Organic chemicals exports covered by the CBAM accounted for 1% of total South African exports in 2021," the report found.

The largest contributors to greenhouse gas emissions are the production of ammonia and nitric acid.

South Africa's chemicals and pharmaceutical product exports are more carbon-intensive than most other countries, with a carbon intensity of exports at an estimated 1 200 $tCO_2e$ per $1 million.

The carbon footprint of the South African plastics value chain was estimated at 17.9 million $tCO_2e$ in 2018, with 52% of these due to the local coal-based monomer production process, making the country's exports an outlier.

Plastics exports covered by the CBAM accounted for 1% of South Africa's total exports in 2021, as coal is also a feedstock for plastics production, while the risk for chemical fertilisers and cement was marginal, as the EU accounts for less than 1% of South African exports for both sectors.



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