

Written evidence from UK Steel – Mr0002

About UK Steel

UK Steel, a division of Make UK, is the trade association for the UK steel industry. It represents all the country's steelmakers and a large number of downstream steel processors.

Submission to the Energy and Environment Sub-Committee's evidence session on Carbon Border Adjustment Mechanism

1. Should the UK welcome or be worried that the EU is considering introducing a carbon border adjustment mechanism?

As the UK is highly aligned to the EU's current climate change policies and share similar (if not more ambitious) climate change mitigation aims, it is unlikely that such a mechanism will be used against the UK. Depending on how it will be designed and applied to the UK, the UK should cautiously welcome such a mechanism.

Considering the wider challenges of imported and consumption emissions, it is likely that the UK will need to consider and assess a similar policy to avoid carbon leakage and closure of emission-intensive industries. As such, it would be helpful to learn from the EU's experience of implementing such a policy. However, the UK should ensure that it does not become a dumping ground for high-emission products that can no longer be sold to an EU market with a carbon border mechanism. This will depend on how the EU policy will be designed and how strictly it will be applied to the relevant markets. From a steel perspective, the UK could be flooded with high-emission, lower-cost steel, which cannot be sold to the EU market and would have a detrimental impact on the domestic steel production.

2. How do you expect the EU to implement a carbon border adjustment mechanism and what will be the key challenges for the EU?

a. Which sectors do you expect to be targeted initially and subsequently?

It is highly likely that the EU would target the steel sector as it is highly trade-exposed and a very carbon-intensive industry. It is our understanding that the steel industry amongst other energy intensive industries will be the primary targets of a border mechanism in a sectoral approach.

b. Will it be possible for the EU to design a WTO-compliant mechanism?

c. How do you expect the EU's major trading partners to react?

3. If the UK and EU agree to link emissions trading systems, how might the EU's carbon border adjustment mechanism apply to the UK?

a. Would an adjustment be applied to goods from the rest of the world that enter the UK?

4. What are likely to be the advantages and disadvantages of the UK being within the EU's carbon border adjustment mechanism?

Being within the EU carbon border mechanism would reduce administrative burdens to prove compliance for UK companies, depending on the design of the policy. It would also ensure that the UK would not be more liable to receive imported steel from producers facing high costs from the EU carbon border mechanism. Furthermore, depending on the policy design, it could further assist the UK in decarbonising its industry while avoiding carbon leakage and even open the options of re-industrialising certain sectors. This would also be an advantage if the UK itself implementing a carbon border mechanism.

In terms of disadvantages, then the mechanism could be designed from an EU perspective and not take account of UK specific market characteristics nor accept evidence from UK companies. This could ultimately harm UK companies and create perverse market outcomes.

a. How might the UK mitigate any negative impacts?

b. Is this likely to require the UK to align with EU rules?

5. If the Government implements a domestic carbon tax, would you expect the EU to apply the mechanism to the UK?

The UK already has a domestic carbon price through the EU ETS and the Carbon Price Support, the latter which is UK-only policy. It the Government's stated aim to continue to apply a carbon price after leaving the transition period in December 2020.

Depending on policy design, we would not expect the EU to apply their carbon border mechanism to the UK, given that the UK continues its current policy of taxing carbon after the end of the transition period.

6. If the UK is outside the EU's mechanism, what are the advantages and disadvantages of the UK developing its own carbon border adjustment mechanism or choosing not to do so?

Steel is an intensively traded product, with 30-40% of the 1.9 billion tonnes of steel produced globally each year travelling across national borders. The UK imports some 6.6 million tonnes of steel each year, around 61% of requirements, and exports 3.5 million tonnes, around 48% of its production. Being a highly trade-exposed industry, the steelmakers are unable to pass on any additional costs over and above those faced by their competitors. However, all decarbonisation options for steel require large capital investment and currently increase operational costs, and consequently lead to higher cost steel, which means the sector will be outcompeted in domestic and export markets by higher-emission products.

There is, therefore, a need to either 1) finance the additional ongoing cost the steel sector and other heavy industry face in decarbonising, which raises questions about who and how the UK pays for the environmental subsidies required; or 2) create a market for low-carbon steel, where UK steelmakers are not outcompeted by imported high-carbon, low-cost steel. The latter could require carbon border adjustments, product standards, and the like, to create a market for low carbon steel.

There are currently no policies in place that sufficiently protect UK steelmakers against being outcompeted by such high-carbon imported steel, and therefore no incentive to invest in decarbonisation technologies if they increase operational costs.

Without policies to finance higher ongoing costs, carbon border mechanisms, or other policies with the same effect, steel manufacturing will be moved outside of the UK, while ceding control of UK emissions to overseas producers. The UK must take responsibility for all of its emissions – including consumption emissions from imports. It cannot just export its steel manufacturing, jobs, and emissions, to meet its Net Zero target.

a. What proportion of the relevant carbon-intensive products does the UK trade with the EU and what proportion is traded with the rest of the world?

Around 4.5 million tonnes, or 69% of total UK imports last year, came from the EU, and the UK sent 2.6 million tonnes, 77% of its exports, across the Channel. This has increased compared to last year, largely due to the rise in global trade restrictions. An EU carbon border mechanism is thus very likely to impact steel trade if applied to the UK.

7. How big a factor should the EU's proposed carbon border adjustment mechanism be in the UK's consideration of domestic carbon pricing policy?

If the EU applies a carbon border mechanism, then the UK should follow suit. In decarbonising its economy, there are very good reasons to consider a carbon border mechanism, regardless of whether the EU will adopt one, to avoid carbon leakage and an increase in overall industrial emissions. Should the EU apply such a policy, the UK would benefit by applying a similar, although independent, policy to ensure that imported products are in line with its own climate change policies.

8. Does the Government's ambition for the future relationship – including for trade in goods or energy – make one way of interacting with the carbon border adjustment mechanism more likely?

9. What should Government be doing in the short and medium-term given the announcement of this policy?

The Government should start the process of assessing which markets a carbon border mechanism would be most suitable for, how it would be implemented in the UK, and how it will fit with wider Government trade negotiations. As a minimum, it should start preparing market evidence and engage with the EU Commission on how such a policy would be applied to the UK.

In the medium term (i.e. within the next 2-4 years), the Government should have decided how it intends to respond to trade-intensive, high-emission markets such as steel in terms of decarbonisation. It should have a clear policy as to whether it intends to 1) finance the additional ongoing cost the steel sector and other heavy industry face in decarbonising; or 2) create a market for low-carbon steel, where UK steelmakers are not outcompeted by imported high-

carbon, low-cost steel. Otherwise, industry will face significant uncertainty, increased carbon costs, but with no viable route to decarbonisation.

Given the amendment to the Climate Change Act to adopt a Net Zero target, it is clear that the Government cannot continue as it has so far. If it continues to increase costs for the steel industry through carbon pricing and funding of renewables through energy bills, while not protecting steelmakers from imported high-carbon, low-cost steel, we will see a continued increase in imported steel. This will cede control of UK emissions to overseas producers, leaving the UK Government with no power over how the steel is produced. Ultimately, this will lead to import of high-carbon products, and overall more global emissions – the very opposite of the Government’s policy aim.

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