

EUROPEAN POLICY ANALYSIS

CBAM: Bending the carbon curve or breaking international trade?

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Summary

The world is not on track to fulfil the goals in the Paris Agreement. While multilateral climate cooperation plays an important role in climate action, states increasingly engage in unilateral and bilateral deals in the race to net zero. This could result in a more fragmented approach to climate governance, which may risk undermining wider cooperation.

Against this backdrop, we analyse the EU's carbon border adjustment mechanism (CBAM), which will apply a levy on certain carbon-intensive imports into the EU. Once it comes into full effect, it will be the world's first international carbon border levy with potentially significant impacts. Understanding the CBAM and its potential effects is important for discerning future trends in climate governance and the EU's role in the global landscape of climate action. The aim of the analysis is thus to cast light on the CBAM and in particular to examine its possible consequences in terms of third country responses.

The analysis concludes with policy recommendations on how EU policymakers can leverage trade-related conversations to push forward on climate policy, recognizing that the two areas are interrelated. In addition, we highlight that the EU needs to support developing countries in acquiring green technologies and services to build a broader coalition in support of climate action.

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The opinions expressed in the publication are those of the authors.

1. Introduction

Over 30 years of efforts to address climate change have so far failed to bend the global emissions curve (Stoddard et al. 2021). Multilateral approaches, such as those under the auspices of the United Nations Framework Convention on Climate Change (UNFCCC), seek to address climate change in the face of a large-scale collective action problem, necessitating coordination among multiple parties to prevent free riding. At the UNFCCC, nearly 200 countries negotiate and seek to enhance international cooperation on climate change at annual meetings. Since decisions at the UNFCCC negotiations take place through consensus, outcomes typically reflect the least common denominator and ambition is thus hampered.

This leaves room for more ambitious countries to take unilateral action to drive climate action forward faster than the international consensus. The EU's carbon border adjustment mechanism (CBAM) represents such an approach. Once it comes into full effect, it will be the world's first carbon border levy with potentially significant impacts.

The CBAM is a competitive mechanism, but it also aims to promote cooperation. Other such initiatives include the recently launched [Climate Club](#), which aims at driving industrial decarbonization, and the proposed [Global Arrangement on Sustainable Steel and Aluminium](#), which seeks to achieve an agreement between the US and the EU on increasing trade in green steel and aluminium. These initiatives represent a growing number of cases of new forms of cooperation and competition in climate governance around the world.

While cooperation and competition have been part of climate governance from the start, recent developments point to a certain shift in climate governance, characterized by seemingly more protectionist¹ and competitive approaches. There are different reasons for this shift. While the world has seen incremental progress on addressing climate change since the signing

of the Paris Agreement, emission reductions are not in line with the science (Hoppe et al. 2023). This means that deep transformations are required across economies to fulfil the goals of the Paris Agreement. For this to happen, countries must also address greenhouse gas (GHG) emissions from hard-to-abate sectors such as steel, aviation, shipping, agriculture, and cement, among others. This, in turn, puts pressure on maintaining national industries' competitiveness while addressing the risk of carbon leakage—i.e. production is moved to a location with more lenient climate policies (e.g. lower carbon price or tax), thereby increasing emissions elsewhere.

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The CBAM, we argue, exemplifies this shift in climate governance and provides an interesting case study with relevance for wider climate governance. This analysis examines the CBAM and assesses its implications from the perspective of conflict and cooperation in climate governance. We point to three trends in climate governance that form the backdrop to understanding the CBAM.

1. As more sectors of the economy need to decarbonize, climate policy increasingly gets tangled up with industrial and trade policies.
2. As climate policy broadens in scope, its interconnectedness with other policy areas will open up opportunities for reforms of governance arrangements in other policy areas such as global trade rules.
3. These shifts will have wider geopolitical implications—for example, through altered trade patterns and political alliances.

¹ Protectionism (whether real or perceived) can lead to higher prices and undermine a collaborative approach if it encourages tit-for-tat, potentially slowing the adoption of green technologies. Some protectionism may be warranted, but it needs to be properly managed to avoid negative side-effects. For example, see <https://www.csis.org/analysis/analyzing-european-unions-carbon-border-adjustment-mechanism>

There are different opportunities and pitfalls with these developments which will be explored in this analysis. How the EU manages to promote CBAM, and how other countries react to it, will influence whether the balance tips towards more competition or cooperation. This analysis therefore examines possible consequences of the CBAM in terms of third country responses. Understanding these responses provides insights into different scenarios for international climate action in the future. Firstly, we will describe the CBAM and carbon pricing as policy instruments. Then we will delve deeper into the perceived purposes of the CBAM and its current and potential impacts on countries outside the EU. Finally, we will discuss the role of the CBAM in the broader landscape of climate governance and provide policy recommendations.

2. What are the CBAM and carbon pricing?

The carbon border adjustment mechanism introduces the world's first international carbon border levy,² applying a tax on imports into the EU on industries that are carbon intensive and at risk of carbon leakage. This policy comes as a result of the EU aiming to raise its climate ambitions via the [European Green Deal](#), which is a package of policy initiatives with the overarching aim of making the EU climate neutral by 2050. Since 2005, the EU has set a limit on carbon emissions through a cap-and-trade system known as the EU Emissions Trading System (ETS), which is a carbon pricing instrument.³ With the EU climate law that sets a target to reach climate neutrality by 2050, the EU ETS has been reformed to drive emissions down faster. Moreover, since industrial decarbonization must be accelerated, the free emissions allowances that were previously allocated to carbon-intensive industries are set to be phased out. These reforms

imply that the price of carbon is set to go up. Thus, the EU wants to prevent its carbon-intensive production moving to other jurisdictions with lower or no carbon price at all, a phenomenon known as carbon leakage, as this would undermine the purpose of a higher domestic carbon price and simply shift carbon emissions geographically. This means that a higher carbon price necessitates the introduction of a trade regulation such as the CBAM. Although evidence of the effects of border adjustment instruments on carbon leakage varies, there are studies that show potential benefits of this type of policy instrument in reducing emissions from high carbon intensive sectors and minimizing carbon leakage (Clora et al. 2023; Eicke et al. 2021).

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The CBAM's transitional period began on 1 October 2023. During this period, foreign companies and exporters to the EU in six carbon-intensive industrial sectors (cement, iron and steel, aluminium, fertilizers, electricity, and hydrogen) are only required to meet reporting obligations—i.e. to report their emissions data to the EU registry. From 1 January 2026, however, they will be required to purchase CBAM certificates to cover the carbon price difference between non-EU and EU products.⁴

² The only jurisdiction that has implemented a carbon border levy in the past is at a subnational level, being the state of California ([Clora et al. 2023](#)).

³ According to the World Bank tracking system, in 2023 there were 72 carbon pricing initiatives around the world (39 national, 33 subnational) implemented, scheduled or under consideration.

⁴ The final set-up of the CBAM is yet to be decided pending a review after the transitional phase: “A review of the CBAM's functioning during its transitional phase will be concluded before the entry into force of the definitive system. At the same time, the product scope will be reviewed to assess the feasibility of including other goods produced in sectors covered by the EU ETS in the scope of the CBAM mechanism, such as certain downstream products and those identified as suitable candidates during negotiations.” https://taxation-customs.ec.europa.eu/carbon-border-adjustment-mechanism_en

While the EU's CBAM has been long in the making, its impacts on international relations and climate policy have only recently started to be discerned and they have the potential to be significant going forward. For instance, besides the EU, other countries are currently considering implementing their version of the CBAM, including the UK,⁵ Canada and the US. Such moves have already been criticized by other countries as being counter to World Trade Organization (WTO) rules, as well as against the principle of common but differentiated responsibilities enshrined in the UNFCCC. The risk of trade conflicts is thus one potential impact. According to Overland and Sabyrbekov (2022), it is likely that several trade partners (such as China, India, Russia and USA) will fight the EU's CBAM.

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The design of the EU CBAM will matter in terms of how it will affect its trading partners. Important design elements include, for instance, which sectors are covered by the CBAM, how carbon accounting is done, and whether any countries or sectors are exempt and/or compensated (Buylova et al. 2022; Marcu et al. 2021). According to Eicke et al. (2021, p. 2), “If designed poorly, a CBAM could increase administrative costs, raise prices for basic products, spur international trade conflicts and undermine the multilateral rules-based system.” The CBAM test period has begun and we need to examine how it performs in its trial period, what reactions it gets from its partners, and if and how its design is adjusted as a result. Already the CBAM is making an impact and generating responses. Below, we turn to the discussion of how the CBAM is perceived depending on its different purposes and present its potential impacts on different countries.

3. The EU CBAM's different purposes

In this section we examine what purposes the CBAM serves for the EU, how it may be perceived from outside the EU, and what role it could play from the perspective of international collaboration and competition on climate action.

According to the European Commission (2024), the CBAM is a “tool to put a fair price on the carbon emitted during the production of carbon intensive goods that are entering the EU, and to encourage cleaner industrial production in non-EU countries”. Scholars have noted tensions in the way different actors perceive the objectives of the CBAM, however. Table 1 summarizes the three main perspectives on the objectives of the CBAM and its implications for international collaboration on climate and trade as described in the literature. This is based on conceptual discussions of the CBAM's partially overlapping objectives and its possible effects (Buylova et al. 2022; Colgan et al. 2021; Pirlot 2022). We distinguish between possible effects in terms of whether it sets off more cooperative dynamics (productive competition) or more conflictual dynamics (counterproductive competition). Productive competition has the potential to set off a virtuous spiral of greater synergies between the climate and trade agendas. Counterproductive competition, on the other hand, risks leading to trade wars and undermining climate governance. The CBAM could set off both forms of competition, as described below.

The CBAM has been promoted by the EU as a climate instrument that prevents carbon leakage and encourages other countries to accelerate their domestic climate action (e.g. via creating a domestic carbon price). However, it has also been viewed by some observers as an economic instrument that protects domestic industry in the face of global economic competition as the EU imposes more regulation on its domestic production via increases in carbon prices (Buylova et al. 2022). The CBAM could also be seen as an

⁵ The UK is taking clear steps to implement the CBAM in 2027. See <https://www.gov.uk/government/consultations/addressing-carbon-leakage-risk-to-support-decarbonisation/outcome/factsheet-uk-carbon-border-adjustment-mechanism>

Table 1. Summary of the CBAM's objectives and its possible effects

| Objectives and perceptions of the CBAM | Productive competition | Counterproductive competition |
|--|--|---|
| <p>Climate instrument Preventing carbon leakage and achieving EU and global emission goals.</p> <p>Internalizing GHG emissions embedded in consumption.</p> | Climate instrument that fosters countries' responses by advancing domestic climate action (e.g. implementing a domestic carbon price instead of paying the EU border tax). | Can foster retaliation if seen as protectionist and no exemptions are provided. Retaliation measures can be negative for climate action and cause international conflicts. Potential administrative burden for reporting GHG emissions embedded in products by foreign countries may be too high, creating new conflicts and making the CBAM ineffective. |
| <p>Economic instrument Creating a level playing field for domestic industry and protecting it from external competition as the EU ETS carbon price increases.</p> | Countries' responses to CBAM measures can advance climate action by fostering changes to international (trade) rules that strengthen climate action. | Countries are unable to be part of the EU market and compete in the new trade order, potentially leading to lack of development, retaliation or the rise of new trade patterns. |
| <p>Diplomatic instrument Fostering uptake of climate instruments in terms of carbon pricing and green technologies around the world to avoid the border penalty. Encouraging countries to join collaborative initiatives such as the Climate Club to cooperate on industrial decarbonization.</p> | Competitive approach that aims to encourage other countries to join collaborative initiatives such as the Climate Club to harmonize standards and create new markets for green products. | Costs of the CBAM may be too high for many countries, potentially leading them to turn to other coalitions and trade partners, leading to climate and trade fragmentation and conflict. |

embryonic climate club⁶—a club of front runners that, via a more competitive approach, aims to encourage other countries to join and benefit from access to new technologies and trade markets. As a diplomatic tool, it could encourage more countries to join the recently established Climate Club, which aims at fostering cooperation on industrial decarbonization, though it does not yet include binding commitments on carbon pricing. If it manages to secure such commitments, especially among high emitters, it can accelerate the reduction of GHG emissions globally. However, if the barriers to entry are too high for countries that need access to information, technologies and services to act on climate change, then the club might be counterproductive for climate action and create more international conflict. One of the main debates around the CBAM's policy design has centred on its compliance with WTO rules, specifically the General Agreement on Tariffs and Trade (GATT 1947) Article 3, the National Treatment Principle, which prohibits less

favourable treatment of imported goods compared to domestic products. The EU has argued its intention to comply with the WTO principles of non-discrimination and said that ensuring fair competition for its industries via the border carbon adjustment was necessary to prevent the risk of carbon leakage (Espa and Holzer 2023). The WTO allows countries to adopt trade-related measures aimed at protecting the environment, but subject to specific conditions. Thus, the CBAM could in principle be aligned with WTO rules, but the details are still debated (see, for example, Espa et al. 2022; Hillman 2013). However, perceptions of compliance matter as much as actual compliance when it comes to diplomatic relations. As such, whether as a reaction to the CBAM or as a reflection of a shift in climate governance, some developments in other parts of the world also show an increase in attention to industrial decarbonization, such as in the provisions of the [US Inflation Reduction Act \(IRA\)](#) and [China's green industrial strategy](#).

⁶ The idea of climate clubs has been proposed as an alternative, or a complement, to multilateral efforts to address climate change (Hovi et al. 2019; Nordhaus 2015). While there are different definitions and types of climate club, the idea is for “a smaller group of actors to take action outside the UN climate regime, with clearly defined targets and conditions for members, possibly involving sanctions against non-members” (Falkner et al. 2022, p. 480).

Trade competition is necessary to spur green innovation, but too much competition can lead to protectionism that can undermine climate policies by restricting learning and the uptake of green technologies around the world. For example, green tariffs, fossil fuel subsidies, carbon taxes and other methods to regulate differences in production methods across countries can be seen as positive competition that can accelerate climate action but can also grow into unilateral action that leads to conflict, undermining global economic integration. As an example, the World Economic Forum (2023, p. 5) reports that “export restrictions on critical raw materials have increased fivefold since data collection began in 2019, according to the Organization for Economic Cooperation and Development (OECD), with 10% of global exports of these materials facing at least one restrictive measure. Many countries are now talking about critical mineral clubs and shoring up essential supply chains, with for example the US actively negotiating critical minerals agreements with key partners”, including the EU (European Parliament 2023). As such, protectionism can force countries to join other coalitions and cooperative partnerships that could reverse decarbonization (e.g. the expansion of BRICS,⁷ although not necessarily as a result of the CBAM). In this context, we will discuss how the CBAM is interpreted by third and specifically developing countries for whom trade with Europe, as well as growth and green technological development, are important to fulfil their climate targets.

4. How CBAM impacts countries outside the EU

In what follows, we present a summary of third countries’ responses and anticipated responses to the CBAM as described in the academic literature and policy reports. We discuss which countries are more likely to be impacted by the CBAM, in what ways, and what responses we can expect from them.

According to Smith et al. (2023), we can understand the impacts of the CBAM on non-EU countries from three perspectives: economic, trade and justice. These perspectives describe

expectations based on presumed effects and different groups of countries’ capacities to respond to the CBAM.

“Managing the geoeconomic and geopolitical effects of the CBAM will therefore be an important task for the EU.”

From the economic perspective, Smith et al. (2023) argue that the CBAM could be interpreted as a signal to major economies and GHG emitters that the EU plans to keep climate on the global agenda and to protect its domestic interests. Here, the focus is on the reaction of major economies as they have the greatest opportunities to push back due to their ability to control rules of global governance (e.g. in the WTO). For example, this perspective may be relevant in relation to countries like the US, China, Japan, Australia and Brazil. Even though these economies might not be directly affected by the CBAM, from this perspective the “power dynamics and coalition building in international governance” (Smith et al. 2023: 4, p. 4) is key as these countries are likely to try to preserve their dominant position and control. According to this perspective, we can also expect unilateral response measures. For instance, the slow and difficult negotiations between the EU and US on the Global Arrangement on Sustainable Steel and Aluminium (GASSA) risk leading to trade conflicts if negotiations break down. Moreover, the growing BRICS coalition may become a counterweight to the EU’s attempt at coalition building via the CBAM and may be a competitor in defining the global economic and trade order in the future. Managing the geoeconomic and geopolitical effects of the CBAM will therefore be an important task for the EU.

The trade perspective considers countries that are the largest exporters to the EU in absolute terms in the sectors covered by the CBAM (cement, iron and steel, aluminium, fertilizers, electricity, and hydrogen). Such economies include EU neighbouring countries like Russia, Turkey, Ukraine, Norway, Iceland, Switzerland, Egypt

⁷ BRICS is an informal group of states, originally comprising Brazil, Russia, India, China and South Africa. On 1 January 2024, Egypt, Ethiopia, Iran, Saudi Arabia and the United Arab Emirates joined BRICS.

and Morocco. However, unlike in the economic perspective, not all of these countries have financial and geopolitical power to wage trade wars with the EU, so their reaction (or retaliation) is mostly likely to take place via WTO legal disputes. However, it is uncertain which cases the WTO would be willing to take on.

On the other hand, countries in this category may also respond by adopting domestic carbon prices. If more of them do so, it can create a chain reaction around the world. For instance, the CBAM has already contributed to Turkey's decision to introduce a climate law and domestic carbon pricing (Weise 2021). This perspective also moves attention to sector-specific decarbonization and positions industries and companies as important players. Thus, cooperation within sectors and among industries may lead to coalitions that drive decarbonization even in the absence of broader state collaboration. Finally, while these countries are the top exporters to the EU in the respective sectors, not all of them are significantly dependent on trade with the EU. It would thus be easier for some of them to negotiate around the CBAM, which is not the case for countries in the next perspective.

The justice perspective takes into account the countries that would be most directly affected in relative terms. In other words, these are the countries for which the EU is the most important trading partner (in terms of their economies' dependence on exports to the EU) and for which the CBAM regulation may mean a significant pressure on their economies. This perspective could include countries that are part of the trade perspective, but also a number of developing countries such as Mauritania, Sierra Leone, Mozambique, Bhutan and Jamaica. Thus, if the EU does not implement the CBAM with consideration of the principle of common but differentiated responsibilities embedded in the Paris Agreement, that could cause the North-South divide to deteriorate further.

In addition to the three perspectives of CBAM impacts developed by Smith et al. (2023), which are largely built around characteristics of countries' economic power and trade exposure, it is important to consider other factors that may lead to positive or negative impacts of the

CBAM. Since the instrument is complex in its design and implementation, certain national level characteristics may alleviate or worsen the CBAM's impact. Eicke et al. (2021) argue that most countries that are at a relatively high risk of impact from the CBAM are in Africa and non-EU Eastern Europe. Factors that could contribute to this vulnerability include the carbon intensity of the economy and energy systems, energy and climate policies, institutional capacities—e.g. to measure and report emissions, level of emissions, carbon intensity of energy consumption, emission reduction targets, national statistical system and data quality. Looking at these factors, many developing countries would arguably face higher risks in these respects. Specifically, many developing countries are facing higher energy demand, thus locking them into high energy intensity development pathways, which are harder to escape and “the complexities and administrative costs of reporting carbon content pose additional difficulties for countries of the Global South” (Eicke et al. 2021; Ellis et al. 2011).

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Therefore, it is important to pay attention not only to risks for existing EU trade partners but to the CBAM's possible impacts on potential future partners in terms of both direct impacts and as a result of new international trade patterns and regulations. It is important to note that the CBAM can also be expanded to more product groups in the future, affecting third countries in different ways than are currently anticipated. Some of these countries may also be important to the EU for geostrategic reasons, particularly in times of global power struggles in strategically important geographic locations. Therefore, while several studies argue that the CBAM will not directly impact many countries in the short term, indirect and future risks should be considered. If vulnerable countries do not have affordable pathways to pursue a low carbon track, they are at significant risk of being stranded in the future. In addition, if more countries start adopting CBAM-like measures

without addressing justice concerns, the fragility of the least developed countries could be exacerbated (Magacho et al. 2023). Thus, we need to consider how the CBAM influences the EU's potential partners in the future, particularly for countries with lower abilities to adapt to a lower carbon pathway.

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Several reports show that a number of African countries, as some of the more vulnerable in terms of capacity to respond and to pursue low carbon development pathways, are concerned about possible impacts of the CBAM. Yet the Research Institute for Sustainability's (2023) report on stakeholder discussions in South Africa showed the presence of both negative and positive outlooks on the CBAM. Concerns included negative impacts of the CBAM on countries that are yet to make progress in transitioning to a low-carbon economy: in other words, those countries that are only starting to change their economies would be more constrained in being able to benefit from trade with the EU, and their access to new technologies could be more restrained due to a growing gap between the front runners and those left behind. The report also concludes that due to rising costs that domestic exporting companies will incur as a result of the CBAM, low and unskilled employment opportunities could be at risk. However, some stakeholders held positive views about the opportunities that the CBAM could bring. For example, possibilities to push climate issues to the top of the political agenda and to strengthen regional cooperation to deal jointly with the CBAM by sharing knowledge and capacity building were mentioned.

Similarly, a report by the African Climate Foundation and London School of Economics (2023) concluded that more meaningful reflections on the wider implications of the CBAM are needed, warning that potential trade wars between the EU and its trading partners require

multilateral solutions to decarbonizing trade, as the EU may further grow its power in controlling the global trading system, disadvantaging developing economies in Africa. The report also emphasized that implementation of the CBAM could incentivize African countries to divert their export to other markets—for example, China and India—with impacts on the global trade order. Finally, the justice perspective is emphasized in terms of the CBAM's potential to exacerbate inequalities not only between the EU and African countries, but also between countries in Africa, with a greater negative impact on the less developed countries on the continent. Recently, Rebeca Grynspan, Secretary General of the United Nations Conference on Trade and Development, expressed concern about the EU's CBAM for marginalizing the principle of common but differentiated responsibilities. More generally, she argued that rich countries are using subsidies and trade measures in a way that risks causing damage to poorer countries (Financial Times 2023). There is thus a risk that trade tensions regionally may spill over into UNFCCC negotiations and exacerbate the North-South divide.

5. Implications for international climate and trade governance

One thing is clear: the CBAM will and is already making impacts on international trade and climate governance. As the EU and other large economies implement climate instruments, they have the power to influence and change existing arrangements governing trade relations and the international economic order (Colgan et al. 2021). In some ways, adopting a measure like the CBAM represents an opportunity to reform the international economic order and incorporate sustainability values into its objectives. However, the great challenge is how to balance building domestic support and incentives for climate action and green technologies without sliding into the protectionist path and slowing the global diffusion of climate action (Colgan et al. 2021).

The World Economic Forum (2023) report argues for two scenarios to international climate action in the future: climate-on-track, characterized by climate-trade cooperation, strong green growth and investment, and net zero value chain development assistance, and fractured effort,

characterized by non-inclusive climate clubs, protectionism, and trade-distorting measures. The latter also envisions that countries have banded together in climate clubs to secure resources and align on climate measures with adverse impacts on trade competitiveness. These accelerate the divide between large markets in the Global North and the Global South and create a complex landscape for business to navigate and curb the spread of innovation. Thus, there is a need for critical discussions on principles to be used in the construction of climate-trade cooperation in the future.

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How things develop will depend a lot on how the CBAM is interpreted by the WTO, as well as if and how countries impacted by the CBAM take on legal disputes in the WTO. It also depends on whether the CBAM could lead to broader changes in the WTO and more attention being paid to climate and environmental sustainability in its rules (Szulecki et al. 2022). To allow measures such as the CBAM to be more widely accepted, together with other national industrial policies and trade measures that aim to support the growth of green technologies, it can be argued that the WTO’s national treatment principle needs to be renegotiated (Colgan et al. 2021; Colgan and Hinthorn 2023). And while countries can be reluctant to negotiate, if more try to pursue such a track, there may be enough momentum for change. In any case, there is a need for critical discussions on how outdated trade rules could be reformed to facilitate rapid decarbonization and promote sustainable development. The formation of the [Coalition of Trade Ministers on Climate](#) in 2022 shows that the nexus between trade and climate is being recognized by a range of governments.

The inter-linked nature of the climate and trade agendas has also been a topic of discussion at the UNFCCC. At recent UNFCCC conferences of parties (COP), the idea of the CBAM has received

pushback from various countries. In this regard, the outcome decision on the first global stocktake from COP28 notes the following:

Parties should cooperate on promoting a supportive and open international economic system aimed at achieving sustainable economic growth and development in all countries and thus enabling them to better to address the problems of climate change, noting that measures taken to combat climate change, including unilateral ones, should not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade. (UNFCCC 2023).

At the same time, moving forward we might find different conversations taking place regarding instruments like the CBAM at the UNFCCC. The longer the world fails to address the climate crisis, the greater the harm to the legitimacy of the UNFCCC and other multilateral institutions. As Allan (2019) has noted, “progress” in the climate regime has focused on diplomatic successes rather than environmental outcomes. As we are in the midst of a critical decade for climate change, it is likely that conversations at the UNFCCC will be affected by the wider trends identified above.

6. Conclusion

Climate action is increasingly interrelated with other policy areas and does not take place in a vacuum. While the world looks very different from the time when the UNFCCC classified states as developed or developing countries, inequalities between and within countries remain wide. This has implications for how climate governance is legitimately and effectively conducted. In particular, a collective answer to climate change requires international cooperation and support to enable decarbonization around the world. While competition will be necessary to drive ambition, it should not undermine international cooperation on climate change.

As such, the climate policy agenda seems set to be increasingly preoccupied with the question of what fair competition entails, how trade policies can help the climate cause further, and how to introduce reforms to this end. As climate action spreads in scope to hard-to-abate sectors such as

steel, cement, and agriculture, frontrunners will be keen to maintain a level playing field. This will put the existing rules-based system to the test, as the current rules stem from a different era. The multilateral rules-based order has served the EU well and therefore attention should be paid to reforming it rather than pursuing action that may risk undermining it.

The analysis presented above has shown that the EU is taking ambitious steps in climate governance by moving forward with implementing the CBAM. In doing so, the EU is pushing the boundaries of existing international trade rules, which is already creating ripple effects around the world by eliciting reactions from other countries. Some of these reactions include partner countries taking steps towards climate action; others, however, are taking a cautious position or challenging the CBAM through diplomatic channels. There are different potential effects for the multilateral rules-based system in the future, depending on how actors react. By distinguishing between productive and unproductive competition, this analysis has highlighted opportunities and pitfalls in the new landscape of climate governance.

Based on the analysis presented in this report, we conclude with the following policy recommendations:

- The CBAM should not be overloaded with different objectives such that it leads to unproductive competition. Rather, its value for decarbonization should be emphasized, building confidence through diplomacy and thus strengthening climate action. As such, the CBAM should not be used to further domestic competitiveness at the expense of global climate-policy effectiveness. If third countries come to view the CBAM as an economic instrument rather than a climate instrument, the risk of unproductive competition increases.
- The impact of the CBAM on climate and trade governance will depend on the reactions of EU and foreign companies, as well as the EU's partner countries. The three perspectives outlined in this analysis—economic, trade and justice—provide insights into possible reactions by third countries. While the reactions of major emitters will be important in terms

of determining the success or failure of the CBAM, the justice perspective highlights that the concerns of developing countries must also be factored in and addressed. The EU should pay attention to countries' exposure and vulnerability in the report evaluating the transitional phase of the CBAM in order to ensure its smooth entry into full force.

- The CBAM will be more effective in reducing carbon leakage in case of no retaliation from third countries (Clora et al. 2023). The EU should make significant efforts to support trading partners that are likely to be disadvantaged by the CBAM, especially developing countries that are vulnerable to changing trade patterns. This could take place through EU efforts to secure technology transfers, capacity building and aid in order to facilitate green industrialization in other parts of the world. Efforts should also be targeted at helping third countries transform carbon-intensive sectors and encourage the diversification of high-carbon economies.
- While the EU has promised technical assistance to developing countries for complying with the CBAM, it should also provide support measures to make sure that countries do not fall behind in their decarbonization efforts as an effect of the CBAM. To this end, working with the Climate Club to facilitate policy development and learning as well as market creation and improving finance could be beneficial if heterogeneity of transition pathways is acknowledged.
- EU countries could also add renewed impetus to, for example, the [Carbon Pricing Leadership Coalition](#) to support countries that wish to introduce carbon pricing mechanisms in a collaborative manner. Given the EU's considerable experience of employing carbon pricing, cooperation through international learning processes will be key to share best practices on design and implementation issues.
- The EU could also strengthen its diplomatic efforts to drive reform of trade rules both through different networks, such as the Coalition of Trade Ministers on Climate, and through bilateral discussions. Better alignment

of trade and climate policies is needed to drive decarbonization and avoid trade tensions. Dialogues with trade partners based on respect for different national circumstances is thus a key condition for reducing tensions and fostering collaboration. Such efforts could also help the EU manage the geopolitical effects of the CBAM.

In sum, in a turbulent world where geopolitical conflicts are heightened, high-level political attention will be needed to facilitate the harmonization of policies to drive decarbonization. The EU could use its frontrunner status to encourage more ambitious climate policies if the

concerns of key country groups are considered and support is offered. Through building alliances, the trade and climate agendas could be brought closer together and reformed. If more protectionist tendencies develop, however, the multilateral rules-based trading system could be at risk and both climate and trade could suffer as a result. The case of the CBAM thus illustrates what is at stake for climate governance in a new era of rapid decarbonization. Policymakers need to consider a more holistic approach where different agendas can come together in a productive way. The CBAM offers valuable lessons in this regard and can serve to highlight opportunities and risks going forward.

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