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The EU Carbon Border Adjustment Mechanism

Implications for Morocco and Necessary Policy Adjustments

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The EU's planned Carbon Border Adjustment Mechanism (CBAM), which was agreed upon by the EU in December 2022 and adopted by the European Parliament in April 2023, presents one of the components of a complex framework of policies and measures aimed at achieving the European goal of carbon-neutrality by 2050. The proposed EU policy is an attempt to mitigate carbon leakage by imposing a carbon tax on imports of goods from countries with less stringent climate policies than the EU. By taxing imported goods based on their embedded carbon emissions, the measure is thus supposed to level the playing field for EU firms and discourage non-EU producers from exporting, at a "competitive" advantage, carbon-intensive goods to the EU.

While many details concerning CBAM are still being discussed, the implementation is envisaged in two phases, starting in October 2023 with a pilot phase in which a simplified CBAM would require only reporting obligations, followed by a full implementation from 2026 onwards, when the requirement to purchase certificates for carbon emissions will kick in. Initially, CBAM will apply to imports of iron and steel, aluminium, electricity, certain fertilisers, cement, and hydrogen. Decisions on a possible extension of the mechanism to other products, such as organic chemicals and polymers, are outstanding and expected to be taken before full implementation kicks in in 2026.

This paper is based on discussions during a workshop jointly organized by the Regional Programme Energy Security and Climate Change Middle East and North Africa of the Konrad-Adenauer-Stiftung (KAS-REMENA) and the Istiqlal Group in the Second Chamber of the Moroccan Parliament on 7 February 2023.

Expected impacts of the CBAM on Morocco

Experts agree that the implementation of CBAM will have wide-ranging implications for Morocco's economy. The EU is Morocco's largest trading partner, accounting for over half of its total trade and 65 per cent of its exports.¹ Morocco exports mainly agricultural products, cars, textiles, aeronautics parts, fisheries, and phosphates to the EU. Expected effects of CBAM include potentially negative impacts on the competitiveness and volume of Moroccan exports to the EU, particularly in the sectors directly covered by CBAM (especially fertilizers at an initial stage). At the same time, CBAM could also offer an incentive for Morocco to accelerate its

¹ European Commission, EU Trade Relations with Morocco. Facts, figures and latest developments. Available online at: <https://bit.ly/EU-Mor-Trade>. Last accessed on 13/04/2023.

energy and environmental transition by encouraging investment in renewable energy, supporting the transition to use renewables-based energy in industry, and reducing greenhouse gas emissions.

Among the challenges posed to the Moroccan economy by the implementation of CBAM is the increase in costs of exporting goods to the EU. Shifting to renewables in phosphates and industry will require investments that will make production cost soar and therefore reduce Moroccan exports' competitiveness. The government could deflect some of those costs through direct support for exported goods.

CBAM is likely to affect several key sectors in Morocco. The phosphate industry, especially the fertilizer and the chemicals subsidiary industries – a major source of exports for Morocco – is expected to be one of the most impacted due to its current high carbon emissions. The current ambitious plan by OCP ("Office chérifien des phosphates", the Moroccan public company that oversees phosphates production, transformation and exports) to invest 13 billion USD to achieve 100 per cent carbon neutrality by 2040 will certainly make phosphate derivative products more competitive in the long run, but in the meantime, Morocco's exports to the EU are likely to be negatively impacted, leading to a negative impact on its balance of payments and overall economic output.

While direct effects will be felt by sectors that are heavily reliant on carbon-intensive exports, such as phosphates and cement, indirect effects are to be expected for industries that are linked to these sectors, such as transportation and logistics, due to changes in prices and demand. The extent of the impact will depend on a range of factors, including the carbon intensity of the products being exported, the level of competition in the market, the ability of companies to adapt and innovate in response to the new regulatory environment and the willingness of the Government of Morocco to issue policies to support industry investments in efforts to transition to low carbon energy sources.

Besides the challenges it poses, CBAM also presents opportunities for Morocco. Experts hail CBAM as an opportunity to use as an incentive to accelerate the transition towards a low-carbon economy. Given that the policy would make high-carbon products relatively costlier, it is set to induce an increase in demand for low-carbon products. The policy could therefore create opportunities for Morocco to develop its own low-carbon industries and reduce emissions in hard-to-abate sectors, by scaling up the use of renewable energies and energy-efficient technologies. Plans to transition to a zero-carbon production model, such as the OCP 2023-2027 Investment Program and its 2040 Zero Carbon Vision, could allow the industry to maintain its competitive edge in the wake of applying CBAM. Energy transition plans require, however, significant investment and innovation, as well as the development of new certification and monitoring systems to ensure compliance with EU regulations.

Morocco has already invested heavily in the development of its renewable energy capacities and the development of the necessary political, legislative and economic frameworks. It thus boasts a solid base and an ambitious framework to build upon for an effective transition to a low-carbon economy; it is also well-positioned to become an exporter of renewable energy and green hydrogen to the EU and other markets, which will give the North African country an advantage over other exporters to the EU.

Path dependencies in the current economic structures and relatively limited resources pose, however, a challenge in pushing this transition forward in the necessary timeframe. To succeed and capitalize on its advantages, Moroccan policy-makers and businesses need to set up bold investments in energy transition infrastructure and technologies, as well as develop new partnerships and collaborations with EU companies and governments.

Overall, the impacts of CBAM on the Moroccan economy are likely to be complex and multifaceted, with both challenges and opportunities arising as a result.

Response options for Morocco

In light of the potential impacts of CBAM on Morocco's economy, several options for responding to the new mechanism have been suggested by the experts and speakers.

One possible response is to adopt more stringent climate policies to minimize the effects of CBAM on Moroccan exporters. The idea consists of increasing investments in renewable energy and energy-efficient technologies to reduce embedded carbon emissions in export products. Additionally, it is worth looking at the option of implementing one's proper carbon pricing mechanisms, using rigorous monitoring and objective tracking, easily recognized by EU partners as equivalent, which could help in preventing additional taxes through CBAM.

Morocco could also communicate concerns over specific aspects of CBAM to the EU and suggest adaptations that take into consideration the challenges for countries of the Global South. Experts emphasize the concept of Common But Differentiated Responsibility (CBDR), an important aspect in this context which should open the possibility of providing financial support for developing countries to invest in adapting to CBAM. Countries like Morocco could also negotiate an exemption or a reduced rate for Moroccan exports to the EU or at least a gradual adaptation that would allow for more time than what is envisaged in the CBAM – as long as such adaptations do not threaten the WTO compatibility of CBAM.² Diplomatic efforts should be deployed to convince the EU to recognize Morocco's advanced efforts to reduce its carbon emissions and to support the country's transition towards a low-carbon economy. Moreover, Morocco could also negotiate bilateral agreements with the EU to promote trade in low-carbon products and services.

On the other hand, Morocco could advance in diversifying its export markets beyond the EU through increasing exports to other regions, such as Africa, the Americas, the Middle East, and Asia. A diversification policy would reduce Morocco's dependence on the EU market and would also provide opportunities for the country to promote its low-carbon products and services to new markets. Such a response should however not come at the cost of concerted efforts towards reducing the carbon intensity of Moroccan industries.

Concrete recommendations for the adaptation to CBAM

Beyond general guidelines on how to respond to CBAM – and given the reality of CBAM coming into initial effect in October 2023 – this paper also aims to provide concrete policy recommendations for Morocco on how to prepare for and adapt to CBAM. Given that CBAM needs to be viewed as an element of a larger package aiming at decarbonisation, Moroccan policymakers should re-evaluate existing decarbonisation strategies, particularly in sectors affected by CBAM, but also beyond. Existing strategies should be updated and recalibrated with a view towards new challenges posed by CBAM and towards an overall acceleration of decarbonisation efforts.

Develop and implement targeted policies to support sectors that are likely to be affected by CBAM: Policymakers in Morocco should consider the potential impact of CBAM on industries such as cement, steel, and fertilizer production, which will be impacted directly. While the phosphates-related industries will go through a “greening” process, policymakers should use the same model to develop and implement targeted policies to support the other sectors,

² Some provisions within the CBAM may be in contradiction with the WTO principles, especially the “Most Favored Nation” (MFN) principle which is based on the idea that „countries should treat all their trade partners equally—that no one country should be “more favored.” It means no country should give special treatment to goods or services coming from one particular trading partner” (Bank for Canadian Entrepreneurs, “Most Favored Nation”).

including measures to improve energy efficiency and reduce greenhouse gas emissions through the use of renewable sources of energy. Necessary certification and monitoring systems should be put in place and supported as well.

Draft a roadmap for the decarbonisation of crucial sectors: Policymakers should develop a comprehensive roadmap for the decarbonisation of critical sectors, even if not impacted directly by CBAM, such as energy, agriculture, transport, extractive and other industries. The roadmap should include clear targets, timelines, and specific policy measures to achieve these goals.

Strengthen the regulatory framework to support the decarbonisation of key sectors: In order to enable an accelerated decarbonisation process, policymakers should revise and strengthen the regulatory framework, in order to set incentives and provide legal certainty and visibility for companies. Aspects such as promoting the development of renewable energy, improving energy efficiency, and implementing sustainable land use practices should be considered.

Promote capacity-building efforts to support the transition to a low-carbon economy: Policymakers should promote capacity-building efforts to support the transition to a low-carbon economy. Training and education for workers in key sectors, promoting research and development of new technologies and their adaptation to industries as well as enhancing certification, monitoring, and reporting systems to track progress are some of the initiatives that could be taken.

Foster innovative approaches to decarbonisation: Besides more traditional measures, Moroccan policymakers should also explore innovative ideas for decarbonisation, such as cooperation between industries and farmers to sequester CO₂ and sell carbon credits, as well as create the necessary regulatory frameworks for such innovative collaborations.

Leverage the renewable energy sector: Morocco has a strong position in the renewable energy sector, which can be leveraged to boost the country's exports by reducing the carbon footprint of industrial production. Policymakers should thus continue to incentivize the development of renewable energy – both with a view towards domestic use and the aim of transforming Morocco from an importer of fossil fuels to an exporter of renewable energy. They should also take the necessary steps (legislative, regulatory and technical) to allow all businesses to use renewable energy.

Invest in energy efficiency: The Moroccan government should enhance its efforts to help businesses improve their energy efficiency. Reducing carbon footprints while remaining competitive (the business case for sustainability), and at the same time contributing to Morocco's broader ambitions in energy efficiency and sustainable energy supply is a promising approach in this sense.

Strengthen partnerships with the EU to accelerate decarbonisation efforts: Policymakers in Morocco should engage with their EU counterparts to strengthen and deepen partnerships supporting the decarbonisation of the economy. The engagement could include sharing knowledge and best practices, developing joint projects and initiatives, as well as financial support for energy efficiency measures. Another area, in which financial support from the EU could help Morocco, is the renovation of its energy infrastructure to minimize energy losses and to adapt the networks to renewable-energy-based electricity.

Utilise CBAM as opportunity for positive political communication around decarbonisation: A holistic decarbonisation effort in Morocco requires the buy-in of all necessary stakeholders. This is why policymakers in their communication around CBAM and decarbonisation should focus on stressing the business potential presented by CBAM and how this can help the Moroccan economy to accelerate its low-carbon transition. The business case for decarbonisation should be supported by solid economic arguments. From a broader point of

view, adapting to CBAM can thus be seen as supporting the country's own climate ambitions and international reputation as well as the competitiveness of its economy. Given these potential advantages, advances in decarbonisation should be portrayed as genuinely being in the interest of Morocco, for it to remain a strong economic and political actor on the global stage.

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