ESG Update

Catching up on the EU's CBAM as it moves into its pricing phase

What we know at this stage of the rollout and its potential impact

The EU's Carbon Border Adjustment Mechanism, a cornerstone of the bloc's climate policy, has entered its pricing phase, shifting carbon from a disclosure requirement to a direct cost for importers. While charges will be introduced gradually, allowing companies time to adapt, CBAM is set to become an increasingly relevant reference point for global carbon pricing frameworks. In this note, we outline how CBAM operates, its linkages with the EU Emissions Trading System (ETS), and the sectors and geographies most exposed.

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CBAM and the EU ETS: Two sides of the same coin. The EU's Carbon Border Adjustment Mechanism (CBAM) and Emissions Trading System (ETS) are designed to achieve a common goal: ensuring that goods consumed in the EU face an equivalent carbon cost, regardless of origin. Under the ETS, carbon-intensive EU producers have historically received a share of emissions allowances free of charge to mitigate carbon leakage risk (the reallocation of production to jurisdictions with weaker or no carbon pricing). CBAM complements this framework by applying an ETS-linked carbon cost to imports, thereby offsetting the competitive advantage associated with unpriced foreign emissions.

Gradual and synchronized implementation. CBAM is being phased in alongside the phase-out of free allocation under the EU ETS, maintaining a level playing field over time. CBAM rollout follows three stages (Figure 01): **(i)** transitional phase (2023-2025): importers are required to report embedded emissions for in-scope products, with no financial obligation; **(ii)** progressive financial phase (2026-2034): importers begin paying the EU ETS carbon price on an increasing share of embedded emissions, starting at 2.5% in 2026 and rising annually to 100% by 2034 (Figure 02); and **(iii)** full implementation (from 2034): the EU ETS carbon price applies to 100% of embedded emissions in covered imports.

Narrow sectoral coverage and uneven geographic exposure. To date, CBAM covers six carbon-intensive, trade-exposed sectors: iron ore & steel (~70% of total exposure), aluminum, fertilizers, cement, hydrogen and electricity, with the mechanism expected to reach ~20,000 non-EU producers exporting to the bloc. Exposure is uneven across regions: North Africa and Eastern Europe are among the most impacted, with ~5-10% of exports falling within CBAM scope. Brazil, by contrast, sits at the lower end of the exposure spectrum, with BNEF estimating that <1% of its trade is currently exposed. Overall, we see this limited exposure reflecting two main structural factors: **(i)** the EU is not a primary destination for Brazil's most CBAM-sensitive exports; and **(ii)** Brazil's relatively low-carbon, renewables-heavy energy mix reduces the emissions intensity of its industrial output, lowering the implied CBAM cost vs. more fossil-fuel-dependent regions.

Cost allocation and key drivers. CBAM liabilities are determined through a 3-step process: **(i)** calculation of the embedded emissions of imported goods; **(ii)** adjustment for the share of free allowances granted to EU producers under the ETS; and **(iii)** application of the EU ETS carbon price - currently in the €60–80/t range (Figure 03) - to residual emissions, determining the number of CBAM certificates importers must purchase (Figure 04).

What to monitor next. Looking ahead, we highlight two key areas to watch: **(i)** how the EU will recognize foreign carbon pricing[1]; and **(ii)** whether CBAM will expand beyond basic materials to include downstream and finished products, thereby broadening its scope.

Source: XP Research and BloombergNEF.[1]According to the European Commission, any explicit carbon price already paid in the country of production - via a carbon tax or a domestic ETS - can be deducted from the CBAM charge to avoid double taxation. However, the specific criteria and documentation required for this recognition have not yet been defined.

Catching up on the EU's CBAM

Key charts

Figure 01: CBAM progressive implementation timeline

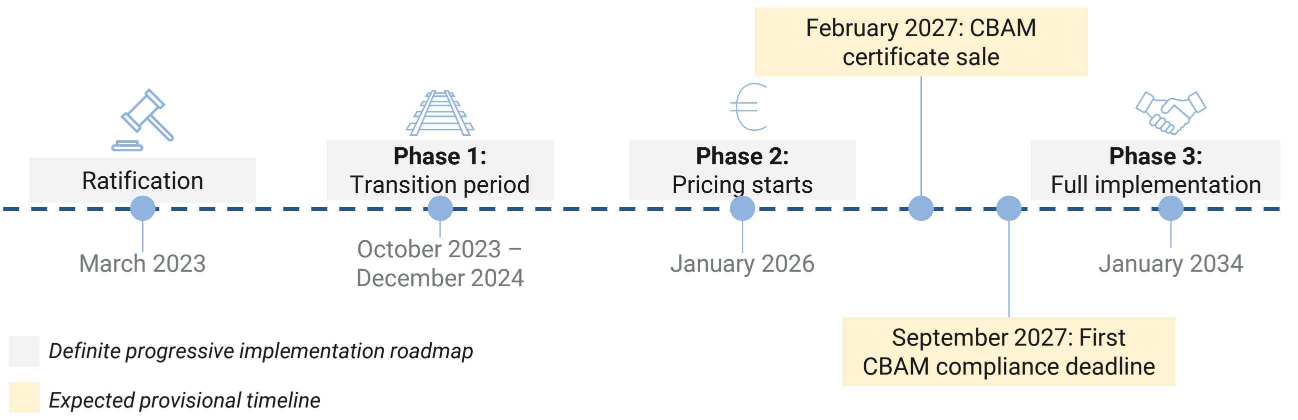


Figure 02: Synchronized timeline of EU free allowances and CBAM rates

Year	EU free allowances remaining	CBAM rate on imports	Phase
2024	100%	0%	Transitional — reporting only
2026	97.5%	2.5%	Financial phase-in begins
2028	90%	10%	Financial phase-in
2030	51.5%	48.5%	Financial phase-in
2032	26.5%	73.5%	Financial phase-in
2034	0%	100%	Full implementation

Figure 03: Average spot prices of the EU ETS *[€/tCO2e]*

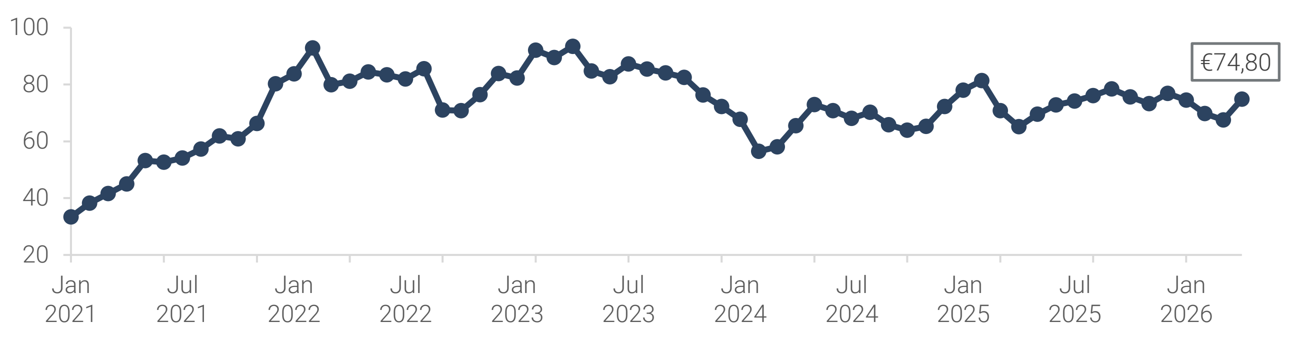
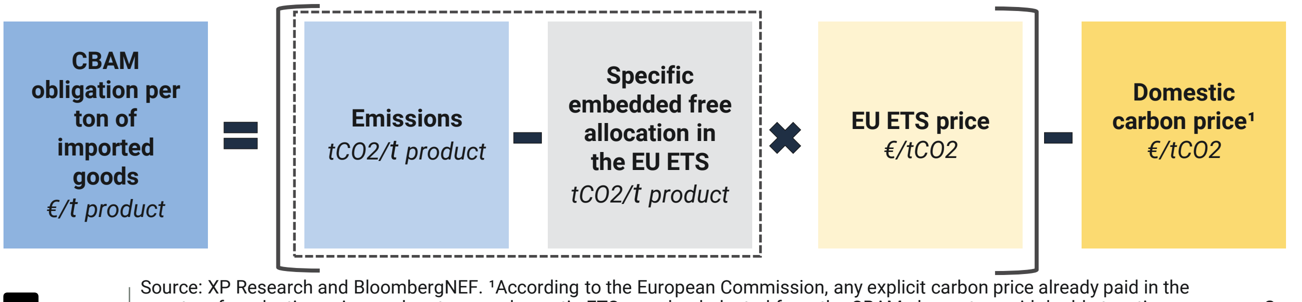


Figure 04: EU CBAM costs depend on carbon prices and embedded emissions of products



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