UK Steel – Spending Review Submission 2025

About UK Steel

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

Introduction

- **Steel is a key driver of economic growth and supply chain resilience**
- **Steel is central to the UK's decarbonisation journey**
- **The UK is in a prime position to lead green steelmaking as one of the biggest generators of steel scrap in the world**
- **The sector employs 33,700 people directly in the UK and supports a further 42,000 in supply chains, with a median steel sector salary of £37,315, which is 26% higher than the UK national median and 35% higher than the regional median in Wales, and Yorkshire & Humberside, where its jobs are concentrated**
- **The steel industry directly contributes £1.8 billion to UK GVA and supports a further £2.4 billion, while directly contributing £3.4 billion to the UK's balance of trade.**

Steel is a foundation industry, literally the building block of our society, feeding into everything from construction to transport, critical national infrastructure, defence, energy pipelines, wind turbines, household goods, food packaging, and medical, industrial, and agricultural equipment. Steel is the bedrock of the UK's supply chains and is fundamental to the future of the UK economy, our economic resilience and national security. The industry supports thousands of jobs and communities both directly and indirectly along the supply chain, particularly in Wales, South Yorkshire and the Northeast of England.

Steel is not only a driver for growth and a major employer in the regions where it is located, but it is also at the heart of a low-carbon economy. Steel is infinitely recyclable and also critical to all low-emission energy generation and every single technology required for a Net Zero future.

Despite the clear advantages of a strong steel sector, the UK steel sector has faced an uncompetitive business environment, driven by persistently high electricity prices. Combined with the unprecedented growth in steel produced in developing economies, fuelled by state subsidies, it has become increasingly difficult to compete in a global market for steel riddled with distortions and excess steelmaking capacity. The landscape remains challenging for the UK steel sector amid a weak economic climate and lack of a clear operating framework that will ensure a competitive business landscape and a level playing field with our competitors.

The UK is an outlier in terms of its steel production relative to the size of its economy and relative to the size of its manufacturing base, which creates significant risks for its economic resilience. France, which is comparable to the UK in terms of GDP, population, and size of its manufacturing sector, produces around double the amount of steel. The UK's steel production has contracted at one of the fastest rates in the world over the last 50 years, second only to Venezuela. If the steel industry in the UK were to continue to contract, the UK would be unique in being by far the largest economy and steel consumer to be almost completely reliant on imports.

We welcome the National Wealth Fund and the Government's £2.5bn commitment to the steel industry. It is clear that this Government wishes to revitalise the steel industry and increase investment, but for this to bear fruit, it must be contingent with improving the business environment for steel. In this submission, we call for the Spending Review to include policies which support the UK steel industry to thrive in an increasingly challenging international competitive environment. These policies will enable the UK steel sector to continue supporting economic prosperity and well-paid, highly skilled jobs across the country, providing security of supply for a strategically important product and decarbonising in line with our domestic and international responsibilities.

UK Steel Spending Review Priorities

Summary of Priorities:

1. **Strategic investment of the £2.5bn committed to the steel sector via the Steel Strategy and National Wealth Fund to decarbonise and rebuild the UK steel industry**
2. **Establish truly competitive electricity prices for the steel sector through uplift to network charge compensation and addressing wholesale electricity prices**
3. **Mitigate late implementation and ensure robustness of the UK Carbon Border Adjustment Mechanism**
4. **Ensure continuation of indirect compensation**
5. **Abolish the Carbon Price Support Mechanism**

Priority 1: Strategic investment of the £2.5bn committed to the steel sector via the Steel Strategy and National Wealth Fund to decarbonise and rebuild the UK steel industry

The Government has demonstrated its commitment to the steel sector through its upcoming Steel Strategy, backed by up to £2.5bn of investment. This investment is essential to revitalise, decarbonise and modernise the UK steel industry and reverse the gradual erosion of competitiveness and market share which we have witnessed in recent years. This will also drive growth and create jobs outside the Southeast of the UK. There are several key investment priorities which the Steel Strategy and National Wealth Fund should consider, including:

i) **Decarbonisation:**
Decarbonisation is a necessity for the steel sector's viability, and governments around the world are partnering with industry to achieve this. UK Steel has published a roadmap[1] for how to decarbonise and the steel sector is committed to investing in reducing 80% of its emissions by 2035 and achieving Net Zero steel production by 2050. Significant progress is being made to invest in electric arc furnaces, and Government-Industry partnership is key to continue to decarbonise UK operations. In addition to the transition for the UK's blast furnaces, there are also other areas that need attention in order to complete the transition from low-emission to Net Zero steelmaking. For example, energy efficiency, decarbonising heat processes and enabling the sector to replace natural gas with hydrogen, which would be contingent on both availability and competitive pricing of hydrogen.

ii) **Strategic capability:**
Our industry needs to invest in broadening its manufacturing capabilities to be able to supply into a broader range of strategic energy and defence infrastructure, bolstering the UK's supply chain resilience. Furthermore, there is an opportunity to develop the UK steel sector's production capabilities in areas where there are strategic dependencies on foreign supply chains and where there are significant future demand opportunities, for example, certain types of plate for wind turbines and naval vessels, galvanised steel for solar farms, the steels needed for heat pumps and Small Modular Reactors (SMRs). If the government is committed to a programme of renewables/ or SMRs, then it must think strategically about how to maximise value for the UK economy and UK jobs from this investment, thinking about steelmaking and wider supply chain capabilities.

iii) **Research and innovation:**
The UK boasts some of the best research and innovation expertise, which we must capitalise upon and grasp the opportunity to become global leaders in low-emission steelmaking. The funding currently available to the steel sector for energy efficiency and R&D is limited and spread very thinly across a number of sectors, while the application process is too onerous. Meanwhile, the UK's £225m share of the European Research Fund for Coal and Steel, which was a key R&D resource, ceased to be available but was never replaced. According to the terms of the EU Withdrawal Agreement (Article 145), the approximately £180m UK share of

[1] UK Steel (2022), Net Zero Steel: A Vision for the Future of UK Steel Production, https://www.makeuk.org/about/uk-steel/net-zero-steel---a-vision-for-the-future-of-uk-steel-production

this fund was to be returned in five annual instalments from June 2021 but this never materialised.

UK steelmakers support over £214m in active UKRI research programs, tangibly demonstrating their strong and ongoing commitment to R&D. A more ambitious and targeted funding programme would drive results at the required pace and ensure that technologies are commercially available for the Government's mission-led economic priorities and the Net Zero transition. This should also be combined with developing and investing in the skills needed for the future in areas such as automation, digitalisation and the hydrogen economy.

A dedicated Green Steel Innovation Fund should cover investments in: a) Energy efficiency (including heat recovery), b) CO_2 emissions reduction (from steelmaking and adjacent processes), c) Circularity and resource intensity (such as water reduction and scrap recovery), d) Hydrogen deployment.

Recommendation: Allocate steel funding to continued decarbonisation and rebuilding of strategic capability in the UK, alongside a ringfenced Green Steel Innovation Fund to support R&D in green steelmaking.

Priority 2: Establish truly competitive electricity prices for the steel sector through uplift to network charge compensation and addressing wholesale electricity prices

The UK has long had Europe's highest industrial electricity prices and well above other key industrial competitors. The UK Government has taken a number of actions to reduce industrial electricity prices, but a significant price disparity still persists. For an electro- and trade-intensive sector like steel, this is hugely damaging to both short-term competitiveness as well as long-term viability and ability to attract inward investment. Higher electricity costs naturally increase production costs (electricity costs can represent around 20% of conversion costs[2]), making UK producers less competitive in home and export markets. This lowers the profitability of the UK steel industry while also reducing investment and making decarbonisation more expensive.

An ongoing electricity price disparity will continue to negatively impact the steel industry in numerous ways:

- The steel sector operates on relatively thin margins. Whilst there are increasingly specialised and high-value steels being produced, market requirements and economies of scale mean that the vast majority of steel made even in developed economies is commoditised and available from a broad range of sources. There is, therefore, intense competition, which keeps steel prices and margins low.
- Negatively impacting the decarbonisation process, as it would cost over £90m more to operate an electrified steel sector in the UK than a comparably sized sector in Germany.
- The direct impact of the UK's high electricity prices is on the steel manufacturers' international competitiveness. Raw materials such as iron ore and coal are sold in global markets, and there will, therefore, be little difference in the price of iron ore used in, for example, France and the UK. It is where there are national and regional variations in costs that competitiveness issues arise. As steelmakers are competing in an international market, they are unable to pass on any additional costs over and above those faced by their competitors. A consistently higher energy price, therefore, impacts their ability to compete and diminishes their profitability. A price disparity of £16.5/MWh translates into a total additional cost to UK steel producers compared to those in Germany of around £37m per year.

As a result, the previous Government announced the British Industrial Supercharger package to reduce the disparity between UK and European industrial electricity prices. However, it failed to align network compensation levels with those in France and Germany, offering only 60% compensation. The French and German governments exempt their steel industries from 85%-90% of network charges, resulting in network charges at around £0.85-2.55/MWh, compared to the UK network charges of 8.58/MWh after the 60%

[2] Conversion costs - the costs of converting the basic raw materials into steel.

compensation. UK steelmakers will, therefore, face network costs of ten times higher than their nearest competitors, resulting in an ongoing competitive disadvantage. The Government should, thus, increase Network Charges Compensation to similar levels as Germany and France, i.e. 90%, and provide truly competitive electricity prices for the steel industry.

Finally, additional actions must be taken to reduce wholesale prices for EIIs and steelmakers. While the previous Government considered a number of options through the Review of Electricity Market Arrangements (REMA), it has taken forward locational marginal pricing (LMP) as a proposal. From the Government's own analysis, it is clear that LMP will increase wholesale prices for steelmakers due to the existing locations, with wholesale prices varying by as much as £13/MWh across the UK in 2050 under LMP. This postcode lottery would hugely damage the steel industry's competitive position, create uncertainty around future investments, and increase the cost of decarbonisation. UK Steel is therefore urging the Government to drop LMP within the REMA process. Instead, a number of different options should be considered to reduce wholesale prices for EIIs, for example, such as a UK ARENH tariff as implemented in France or the introduction of CfDs for EIIs.

Recommendation: Increase network charging compensation to 90% in line with France and Germany.

Recommendation: Discount LMP within the REMA process, and instead consider other policy options to reduce wholesale electricity prices.

Priority 3: Mitigate late implementation and ensure robustness of the UK Carbon Border Adjustment Mechanism

The Government is introducing a UK Carbon Border Adjustment Mechanism (CBAM) in 2027, which will seek to level the cost of carbon for imported steel to that of domestically produced steel. This is vital to prevent carbon leakage for a highly carbon and energy-intensive, as well as trade-intensive product like steel.

However, the European Union is implementing a CBAM policy in 2026 and has already started initially phasing in reporting requirements. When the EU applies its CBAM to imported steel, this could divert steel away from the EU markets to other open, unprotected markets like the UK. As such, the one-year gap between the EU and UK CBAM policies could lead to high-emission steel flooding the UK in 2026. UK Steel has made strong representations to HM Treasury to recommend moving the UK CBAM forward to 2026 or introduce mitigation measures to limit the risk of damage to the domestic steel industry.

It is UK Steel's estimation that of the c28m tonnes of steel exported to the EU from around the world, up to 22m tonnes could be at risk of being diverted to other open markets. To put this into context, if just 10% of this were to be diverted to the UK, this would result in a 45% increase in UK imports, corresponding to around 80% of the UK market. The existing implementation timeline for the UK CBAM does, therefore, endanger this Government's overall strategy for growth and its strategy for the steel industry. Based on current carbon prices and reforms to the EU ETS benchmarks, it is estimated that blast furnace steel exported to the EU would face around €35-40/tonne of steel. As the steel market is very trade intensive, operates on thin margins, and with a background of global oversupply, a price difference of even £5/tonne of steel would be able to make or break a commercial contract. An additional charge of €35-40/tonne of steel would, therefore, be more than sufficient to divert some steel away from the EU steel market to more open markets, like the UK, unless equivalent carbon leakage protection is also implemented simultaneously in the UK.

Steel is highly price elastic, so even a year or six months can be sufficient to impact trade flows, as markets are quick to adapt to new price signals. While there are some specialised products and some particular end-use sectors that will look for specific product characteristics, the vast majority of steel trade is for commodity products like rebar and hot-rolled coil. These are fairly standardised products that are not differentiated on quality but compete primarily on price. These trade flows are, therefore, very responsive to price signals, and experience has shown that surges in imports can happen very quickly. Since HMT/HMRC will not move the UK CBAM forward to 2026 to match the EU timeline and avoid the negative trade diversion impacts, mitigating options should be considered. This could, for example, be introducing mandatory reporting from 2026 or additional trade measures.

Separately, HMT also confirmed in its consultation outcome that it would further weaken the UK CBAM on imports, creating significant fears within the steel industry that the UK CBAM will be inferior to the EU CBAM and enable circumvention and fraud. This could lead to more imports of high-emission steel, even post-2027, which will undermine UK steel production and its efforts to decarbonise. Below, we list seven areas where the current HMT proposals will hinder the establishment of an effective UK CBAM:

i) **Default values:** If importers cannot provide emission data for the products they wish to import, the Government will provide default values based on a global average value. As emissions from steel varies substantially (0.3 - 3.7 tonnes of CO2 per tonne of crude steel (tCO2/tCS)), basing the default values on the average of 1.85tCO2/tCS will provide a substantial discount to the highest emitting steel producers, which will only pay CBAM carbon costs for c. 1.85tCO2/tCS instead of 3.7tCO2/tCS. This will favour the most carbon-intensive global steel producers by allowing them to under-declare their emissions and carbon costs at the border. In contrast, the EU is only proposing to allow importers to use default values for 20% of their imports.

ii) **Threshold:** HMT has increased the minimum registration threshold fivefold, meaning the CBAM will only apply if companies import more than £50,000 within 12 months, resulting in 80% of businesses avoiding facing any CBAM costs. In comparison, the EU CBAM threshold is €150.

iii) **Robustness tests:** CBAM policies are untested and have not been implemented anywhere yet, so it is unclear how they will work, how easy they will be to circumvent, or how widespread fraud will be. Robustness tests should be built into the UK CBAM to ensure the CBAM works as intended. This would include regular evaluations of the policy and backup policy if proven ineffective, such as increasing free UK ETS allowances. HMT/HMRC has declined to build in robustness tests. In contrast, the EU Commission is required to report on the application and functioning of the CBAM every two years.

iv) **Auditing:** The Government intends to limit the requirements to providing high level emissions data and leave the auditing and verification to the independent verifier contracted by the installation. The steel industry has expressed deep concerns about the risk of circumvention and fraud.

v) **Linking:** The UK and EU both have similarly designed emission trading schemes that place carbon costs on industry, which both the UK and EU CBAM costs are based upon. If these two carbon schemes are linked, meaning that a UK ETS carbon allowance can be used in the EU ETS and vice versa, then carbon prices would converge. It would ensure industries in both jurisdictions faced similar carbon pricing and remove any barriers to trade. In particular, this would help smaller businesses which are less acquainted with carbon reporting.

vi) **Scope:** The UK has only committed to applying its CBAM to the aluminium, cement, fertilisers, hydrogen, and iron and steel sectors. In contrast, the EU is already considering expanding the EU CBAM to downstream products to prevent value-chain circumvention, for example where steel-containing cars and white goods avoid CBAM costs.

vii) **Exports:** Finally, the UK CBAM does not address export competitiveness. When carbon pricing is applied to UK steelmakers, it reduces the industry's competitiveness in export markets. In contrast, the EU Commission will publish a report this year on exports and likely introduce an export mechanism for goods produced in the EU for export to third countries which do not apply the comparable carbon pricing.

While the Government must balance the needs of importers and domestic producers to ensure that the UK CBAM does not impede trade unnecessarily or place too many burdens on importers, it should also not prioritise importers of non-UK steel over UK steel producers. The UK CBAM design must also account for the properties and timeline of EU CBAM policy and its implications for the UK.

Recommendation: Take action to mitigate the late introduction of a UK CBAM and prevent high-emission steel from being diverted away from the EU into the UK market in 2026. This could, for example, be by introducing a CBAM reporting period in 2026 and new trade measures.

Recommendation: Define default value methodology in an upcoming working group that includes the application of a markup to any default values to avoid rewarding the highest-emission steel.

Recommendation: Negotiate with the EU as a matter of priority the linking of the UK and EU ETS schemes to enable a mutual recognition of UK and EU CBAMs as equivalent and reduce trade friction with our largest trading partner.

Recommendation: Outline plan for expansion of CBAM scope to downstream sectors.

Recommendation: Review export mechanism options through DESNZ and HMT working group.

Priority 4: Ensure continuation of indirect compensation

The Government provides compensation to some steelmakers for the indirect impact on electricity prices caused by the UK ETS and carbon price support mechanism (CPS). UK Steel analysis finds that the CPS increases wholesale prices by £7.56/MWh, while the UK ETS increases prices by £17.43/MWh. The Government also recognises this, stating that "*carbon pricing through the UK ETS and CPS will have a knock-on effect on the wholesale electricity price and increase retail electricity prices in the short to medium term*"[3]. The Government has, therefore, compensated electro-intensive industries for this impact on electricity prices since 2013/14. The Departmental budget for these schemes will run out at the end of this fiscal year and will need to be extended to prevent carbon leakage and deindustrialisation.

Recommendation: Extend the compensation for the indirect costs of the UK ETS and the CPS mechanism for a further five years.

Priority 5: Abolish the Carbon Price Support Mechanism

The UK's Carbon Price Support mechanism is currently increasing the UK's carbon price unnecessarily compared to the EU. Most UK steel companies today receive near-full compensation for pass-through costs from power generators in industrial electricity prices. However, not all benefit from this, and many Energy-Intensive Industries (EIIs) are not eligible for the ETS/CPS compensation, resulting in higher electricity prices and a price differential with many European countries. This will remain a problem until either the UK removes the CPS or expands the compensation for the indirect cost of carbon in electricity prices to more EIIs.

The original purpose of the Carbon Price Floor mechanism was to provide a stable minimum carbon price in the UK, to drive investment within the power sector and later to drive out coal. With the EU ETS price remaining well below projections in 2013 and 2014, the UK total carbon price quickly became 4-5 times higher than the EU's and contributed significantly to the electricity price disparity between the UK and the continent. In order to minimise this impact on industrial competitiveness, HMT froze the CPS rate at £18/tCO_2 in the 2014 Budget, assuming the EU price would remain low for the remainder of the decade. The previous Government had aimed to phase out the CPS to keep the total carbon price above £25/tonne of CO_2 to ensure that coal generation was phased out. UK ETS prices have not been below £30/UKA at any time since it was created, with current levels around £40/UKA. Furthermore, the last coal generation is expected to close this September.

Additionally, the UK has now introduced its own ETS with a cap consistent with Net Zero and minimum auction price, making a separate top-up tax unnecessary, and the UK ETS prices have remained much higher than the intended total carbon price. The new Government can use this opportunity to remove a tax aimed at topping up an EU scheme and, thereby, reducing the impact on energy-intensive industries.

Recommendation: Remove the CPS completely.

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[3] UK Government (2024), Compensation for the indirect costs of the UK ETS and the CPS mechanism: guidance for applicants, https://www.gov.uk/government/publications/uk-emissions-trading-scheme-and-carbon-price-support-apply-for-compensation/compensation-for-the-indirect-costs-of-the-uk-ets-and-the-cps-mechanism-guidance-for-applicants