# Sustainable Finance Outlook

## September 2026

Europe's carbon-policy balancing act

Research reports

SEB

# In this issue

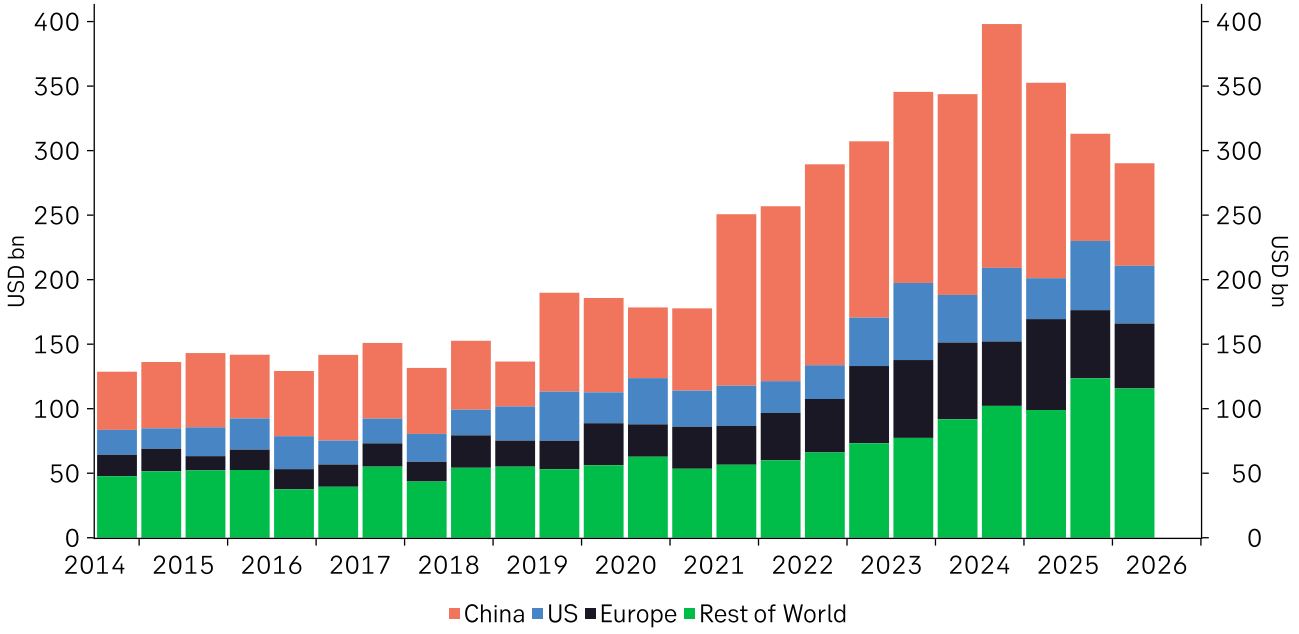
Europe's carbon-policy balancing act

# Energy transition update

Disruptions will hasten the end of the fossil energy era

Geopolitical disruption and extreme weather will accelerate the transition to a clean energy system. We see two drivers: a larger part of energy consumed will be electricity, and a larger share of the electricity will come from non-fossil sources. Over the coming 5-10 years, we expect a sharper decline in fossil energy's share of the world's primary energy supply.

**Figure 1 Renewables investment per region**




Source: BloombergNEF, SEB

## Renewable energy investment levels off

New data from BNEF show that the decline in global investment in solar and wind energy levelled off in the first half of 2026. After peaking in H2 2024 at an annualized level of USD 800bn, they were down to just below USD 600bn in H1 2026.

The decline in spending in 2025 and the first part of 2026 was primarily driven by a slowdown in investment in China, where subsidies were changed to a more market-based contract-for-difference model in 2025. This led to a temporary surge in investment as projects were front-loaded before the change took effect.

Furthermore, like we have seen in other parts of the world, it appears that the supply of electricity from renewables was outpacing the grid's ability to deliver it to users, so we are also witnessing a shift in the balance of investment from primary energy supply to transmission.

Renewable energy investment has been more stable in Europe and the US. Europe is thus still not seeing the shift to higher investment levels that we had expected for geopolitical reasons: European investment jumped in H1 last year, but the past 12 months have seen them fall back to a level close to the average for the past three years.

This still means that European investment over the past three years has been almost twice as high as before the Russian invasion of Ukraine in 2022, but we are not yet seeing investment in energy impendence picking up to match the increased spending on military independence, which we still think would be the logical strategy.

On the other hand, renewable energy investment increased 17% from last year in the rest of the world, suggesting that emerging and developing economies in Africa, Asia and Latin America are focusing on renewables as they build out their energy systems.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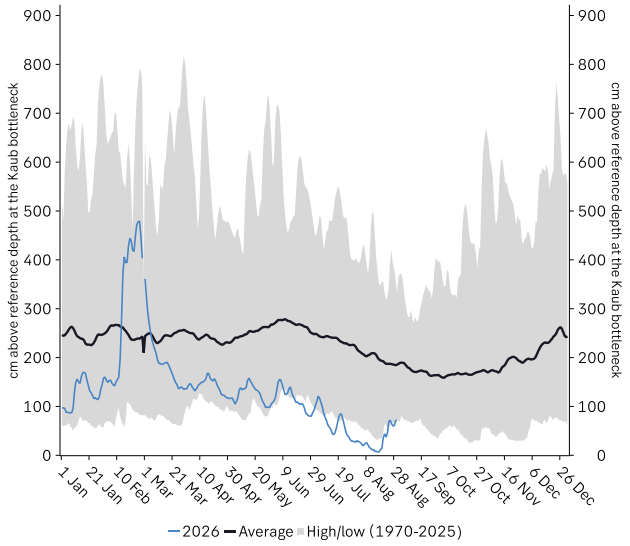
We believe that the recent dip in renewable energy investment is temporary and see three powerful drivers for renewed growth in transition investment increase, driven by Europe, developing economies and the US.

## Capex catalyst #1: physical climate risks

The first driver is that the widely anticipated economic and physical cost of global warming from extreme weather, melting ice and rising sea levels is starting to show up in the numbers sooner than expected.

Amid a strengthening El Niño expected to be strongest in living memory, 2026 has thus seen the most extreme levels on record for both air and ocean temperatures. Rising temperatures are a direct driver of extreme weather events, and the economic effects are starting to emerge.

**Figure 2 Water levels in the Rhine River**




Source: German General Administration of Waterways & Navigation, Macrobond, SEB

This summer, extreme drought on the European continent led to a decline in water levels on key waterways like the Rhine and the Danube to levels not seen in more than 50 years, disrupting important transportation routes and forcing Hungarian authorities to shut down a nuclear power plant due to lack of cooling water. In France, nuclear power production had to be reduced because the temperature of the cooling water was too high.

This is a broader problem for thermal power generation (nuclear and fossil power plants). A recent study by Coffel and Mankin found that "climate change to date has increased average thermal power plant curtailment in nuclear, coal, oil, and natural gas fired plants by 0.75–1 percentage points" due to higher temperatures of air and water used for cooling.

Meanwhile, repeated heatwaves with temperatures exceeding 40 degrees Celsius have hit the continent. Such high temperatures have now been recorded over several years, and the result is an increase in the demand for air conditioning, which will increase the demand for electricity in the same warm periods when e.g. nuclear plants will struggle to produce it.

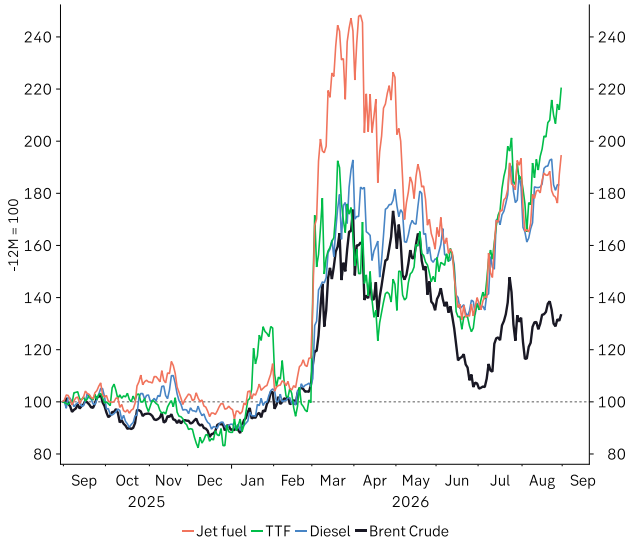
This should in itself provide strong arguments for expanding electricity production using less heat-sensitive technologies. What remains to be seen is whether feeling the effect of global warming moves decarbonization back up on the political agenda. At least, we got some circumstantial evidence from Mærsk, the Danish shipping company, that upgraded earnings guidance in August this year due to increased traffic from China and noted that batteries, solar panels, wind turbines and turbines, cooling systems for data centres and EVs drove the progress.

## Capex catalyst #2: energy supply security

The second driver emerging in 2026 is that the geopolitical case for increasing energy supply security has continued to strengthen, even if the conflict in the Middle East has been de-escalated from full-scale war to blockades.

Since the latest issue of *Transition Update* published in May, crude oil prices have come down despite the continued conflict in the Middle East. The Strait of Hormuz (SoH) is still officially closed, but the current oil price around USD 90/bbl and the fact that oil inventories have started rising again suggests that there are more ships travelling through the strait than the official data suggest.

**Figure 3 Different energy price contracts**




Source: Bloomberg, Macrobond, SEB

However, even though crude oil has moved lower, consumers do not feel that at the pump, and a range of energy products for final consumption like diesel, jet fuel and natural gas are around twice as high as they were a year ago.

Thus, while there is still some disruption from the war in Iran, the energy shock has entered into a new phase, which also highlights the vulnerability of the current fossil-based energy system.

The problem now is the lack of global refining capacity, in part due to disruption of Middle East refining operations, but also by Ukraine's successful campaign targeting Russian refineries, and the lack of strategic reserves for LNG, where the supply from the Persian Gulf has not been normalized to the same degree.

These problems are difficult to mitigate, not least since the reason why refineries are found in Russia and the Middle East is that Western economies tend to avoid the dirty parts of the energy system's plumbing. It also takes 5-10 years to build a new large-scale refinery. LNG is simply more difficult to transport and store than oil, and this means LNG supplies likely to be even more prone to disruption in e.g. geopolitical crises than oil.

The shock to distilled oil product prices has already had a strong impact on the automobile market in Europe after the start of the war. According to BNEF, EV sales in Germany for the period from March to July are up 54% from 2025 and 72% in France. This is perhaps the positive aside of disruption, accelerating the electrification of the transportation system.

However, another result of the disruption is that Europe is heading into the autumn with the lowest inventories ever seen at this point in the year. If the weather behaves, this may not lead to any major problems. However, the situation highlights the powerful geopolitical case for accelerating the build-out of an energy system that does not depend on importing physical products from other geopolitical areas.

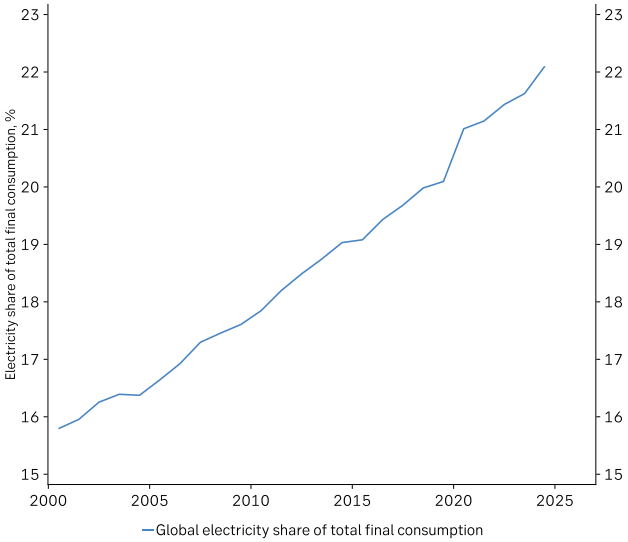
## Capex catalyst #3: second electrification wave

The third driver is technology as the diffusion of a new AI-enabled economic paradigm driven by the digitalisation and automation of basic production models as well as the electrification of the transportation system will increase the share of electricity in the global energy mix.

It is important to distinguish between primary energy consumption and final energy consumption. Electricity is a secondary energy source, which may be generated both with renewable energy and fossil energy as primary input.

Large parts of the economy were electrified already more than a century again when factories shifted from steam power to electric power and household chores were automated using electrical appliances, but large parts of the economy could not be electrified, and here distilled fossil energy products are still deployed directly.

**Figure 4 Global electricity of total energy consumption**

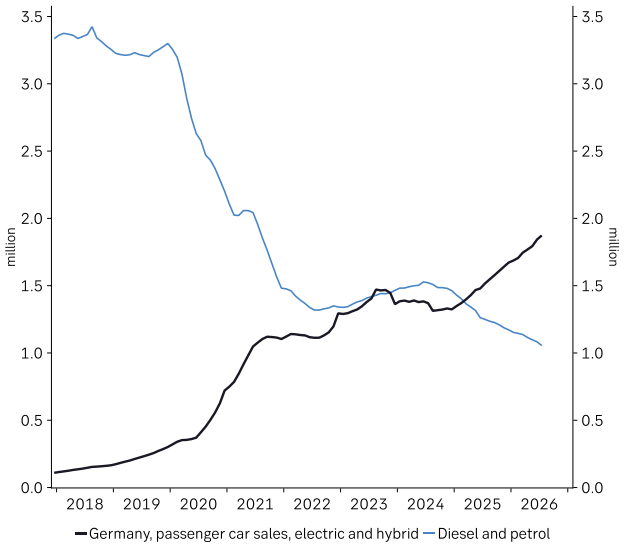



Source: IEA, Macrobond, SEB

Transportation is the most notable, as the combustion engine required liquid flammable fuels and until recently, there were no commercially viable alternatives. Electricity could in principle be used to generate liquid alternative fuels, but the price was not competitive.

However, rapid development of electric vehicles and battery technology over the past few decades have opened the door for electricity to be used directly as input. There are also several 'hard-to-abate' production sectors where fossil energy is consumed directly because electrification either is less efficient or too expensive.

**Figure 5 Germany car sales EV/PHEV vs Diesel/petrol**



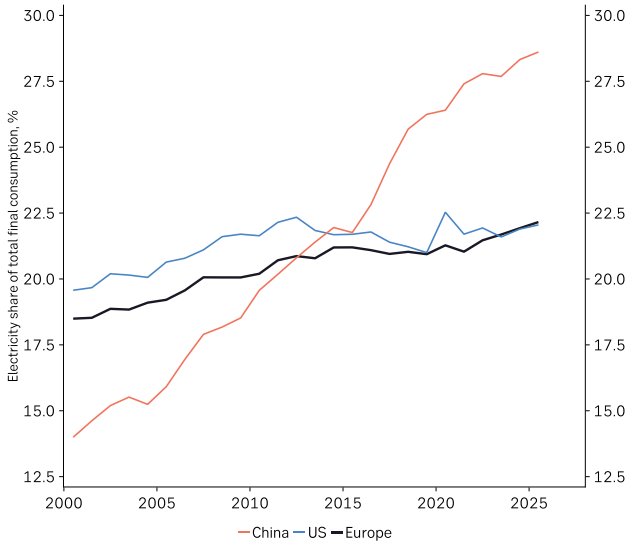

Source: Macrobond, SEB

The advance of EVs is one reason why the share of electricity in final energy consumption has increased from 17% in 2010 to 22% in 2025, but this transition is only in the early stages.

## Electricity share will continue to increase

As described above, electricity has already become a larger share of the total energy mix over the past 10-20 years, but this trend has mainly been driven by China and has yet to take off in the big, developed Western economies. Over the past decade China's electricity generation has thus grown 5-10% per annum, while there has been close to no growth in Europe and the US, and this is not just due to the faster growth in China's economy.

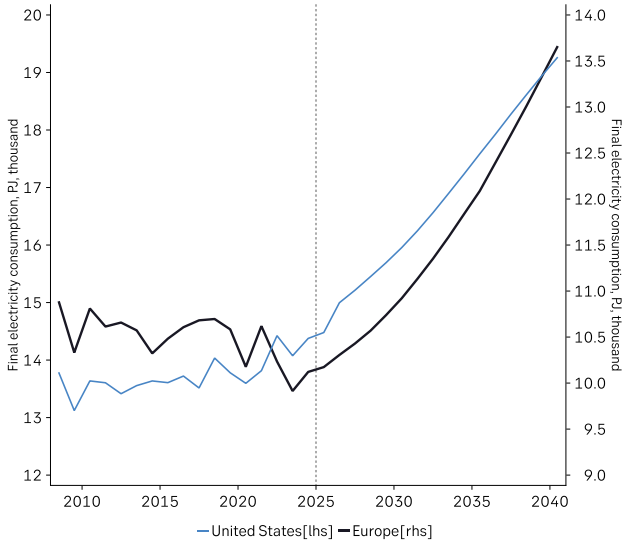
**Figure 6 Regional electricity of final energy consumption**




Source: EnerData, Macrobond, SEB

As seen in Figure 6, the fast growth of China's electricity generation is also a reflection of a deeper change in the energy system. In China, electricity's share of total final energy consumption has doubled since the start of the century and is now close to 30%. In Europe and the US, the share has only increased marginally from just below 20% to just above 20% in the same period, but we think that is about to change.

**Figure 7 US and Europe final electricity consumption**

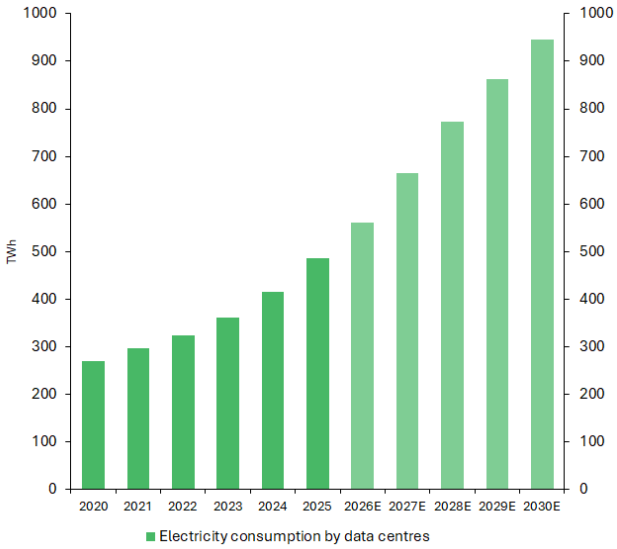



Source: BloombergNEF, Macrobond, SEB

There are several drivers behind the expected surge, mostly to do with technology. In the US, the surge in datacentre construction related to new AI tools has highlighted how these new technologies require very large amounts of electricity. The electrification of personal and commercial transportation systems and the emergence of autonomous capital equipment like humanoid robots will also shift final energy consumption towards electrification.

Over the coming decades, we expect global land transportation to become fully electrified and fossil-free production to become commercially competitive in areas like steel production.

**Figure 8 Global electricity consumption by data centres**




Source: IEA, SEB

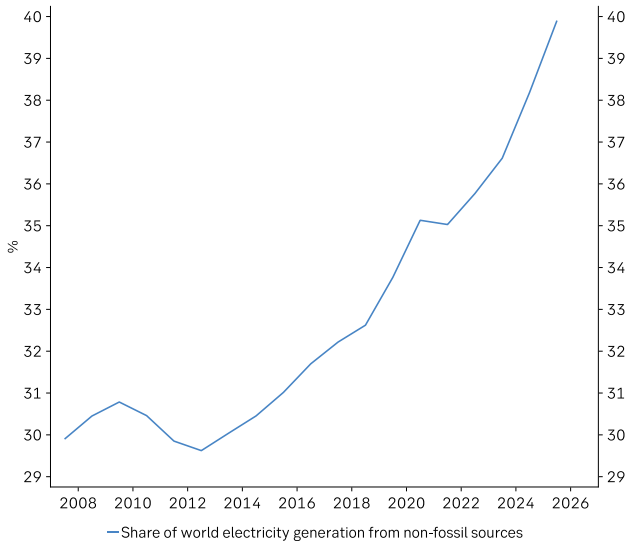
Perhaps more importantly, AI will create new demand for electricity that is not visible right now. Global data centres alone will, per IEA estimates, almost double their electricity consumption over the next 5 years from 485 TWh in 2025 to 945 TWh by 2030. Data centres are only the start of the story: autonomous vehicles, drones, robots etc. are all examples of new products that are barely starting to scale, and all will require electric power as their energy source.

## More electricity will be from non-fossil energy

As noted above, electricity does not necessarily come from renewable energy. However, while electricity may be produced with fossil energy as primary input, renewable energy is far more effective at transforming primary energy into useful energy output, and the technological advances has followed a Moore's law trajectory, where prices fall as volumes rise.

As a result, the past decade has seen a sharp increase in the share of electricity that came from non-fossil primary input from around 30% to around 40%, and we see no reason why this trend, driven by technological superiority as well as geopolitical security, should not continue.

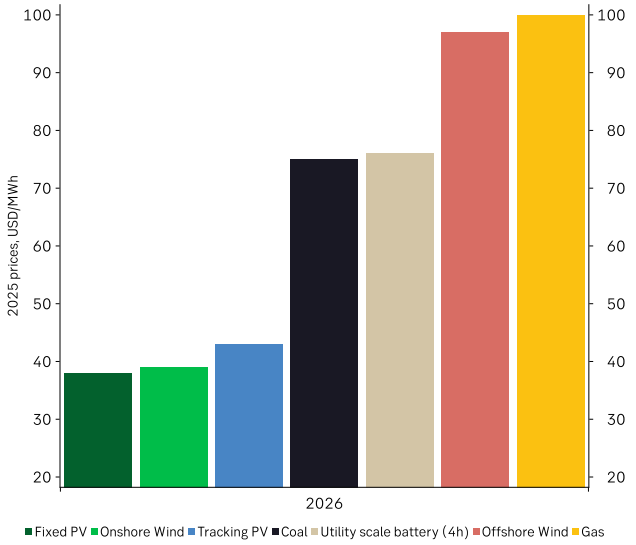
**Figure 9 Global electricity generation, share of non-fossil**




Source: BloombergNEF, Macrobond, SEB

According to BNEF, the levelized cost of solar and onshore wind is 30-50% lower than for coal and gas, so the economic case is clear. Intermittency is still a problem, but improved storage technology is also making that more manageable. However, China owns the supply chain behind these technologies and has far lower LCOEs than the rest of the world. BNEF estimates that China can produce electricity with solar + storage at a combined LCOE of less than USD 50/MWh, half the level in Germany and the US. Replicating China's low cost requires either that you are willing to integrate with the Chinese technology platform or subsidize your own supply chain.

**Figure 10 Levelized cost of energy by technology**




Source: BloombergNEF, Macrobond, SEB

Most developing economies are likely to integrate and move from a US-controlled oil and gas system to a China-controlled renewable energy system. Europe may want to strike a balance where domestic suppliers are protected in strategic areas, even if it is more expensive at first.

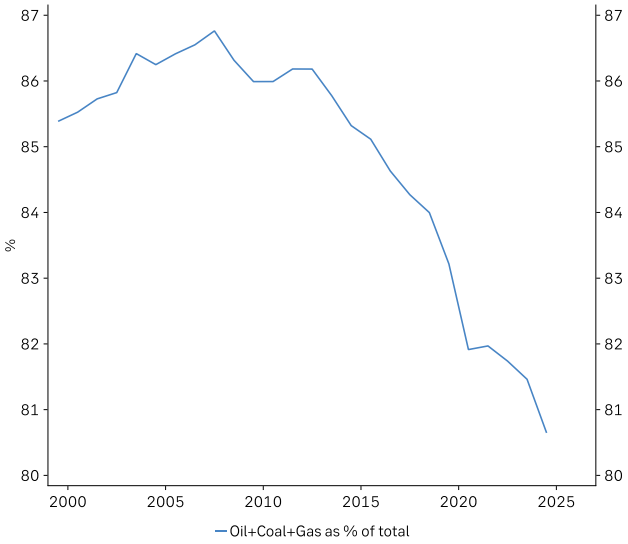
## Bottom line: peak fossil energy is behind us

Our analysis suggests that a) electricity will replace other energy types in final consumption for technological reasons and b) renewable energy will become the dominant source of electricity for economic and geopolitical reasons.

This means we are now entering a phase where fossil energy's share of the global primary energy mix collapses at a faster pace. On a technical note, in order to get the same amount of secondary energy actually used, you need to use twice as much primary fossil energy as if you had used renewable energy due to the efficiency loss. So, when you replace final fossil energy one-for-one with renewable energy, total primary energy consumption goes down.

In other words, if fossil energy provides 80% of total primary energy consumption, that probably means that it provides less than 50% of final energy consumed. And if you add one unit of primary renewable energy, you can remove two units of primary fossil energy.

**Figure 11 Oil, coal and gas share of total primary energy**




Source: Macrobond, SEB

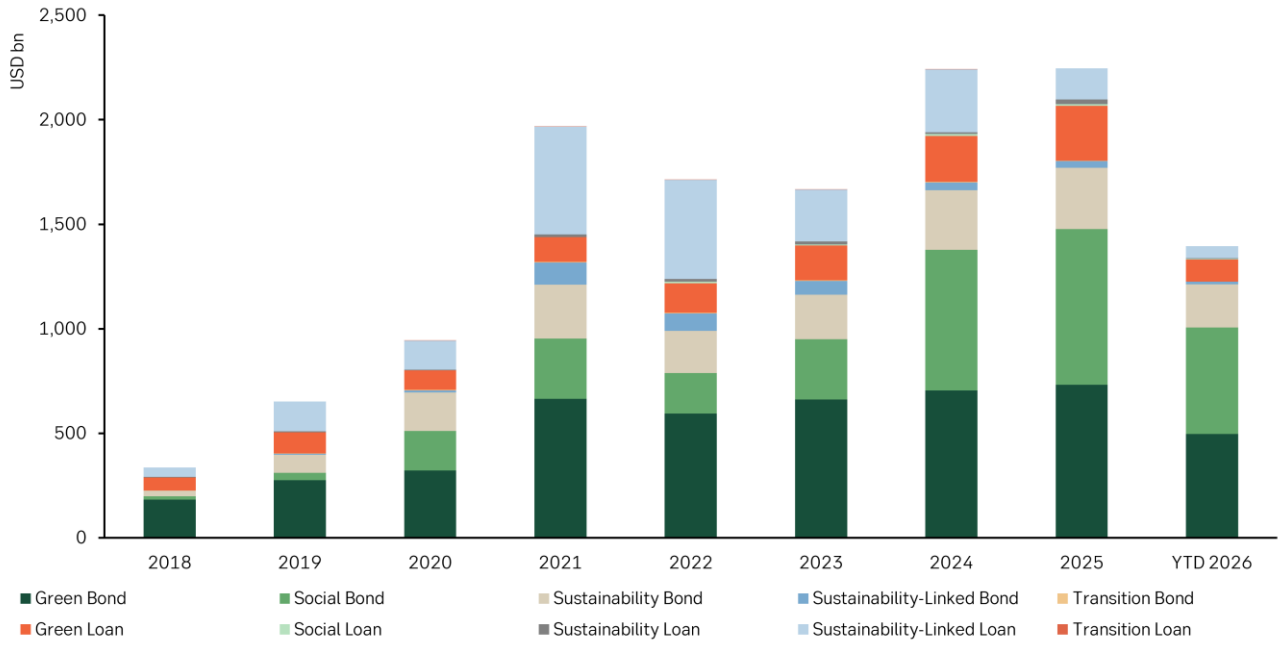
Fossil energy's share of global primary energy consumption has edged lower from 86% to 80% over the past 15 years. Over the next 15 years, we think that share will decline to less than 50%. During this period, the price of fossil energy will also decline towards the lowest regional production cost levels, but this will not be enough to halt the decline in market share. Oil will most likely not go quietly. We expect the endgame to involve destructive price wars between oil producers and potentially also geopolitical disruption in oil-rich regions. All of this is good news over the longer term, however, both from a climate risk and energy affordability perspective.

# Sustainable finance market update

The shifting incentives of EU ETS reform

Sustainable bonds reached USD 1226bn resulting in a 15% YOY growth despite geopolitical headwinds. Electricity dominates CBAM sector sustainable bond issuance pointing out a lack of incentives for heavy industry to invest in decarbonization. Upstream built environment sectors lead sustainable bond issuance, while the downstream, most affected by EU ETS, sees low issuance volumes.

**Figure 12 Sustainable debt transactions by product**



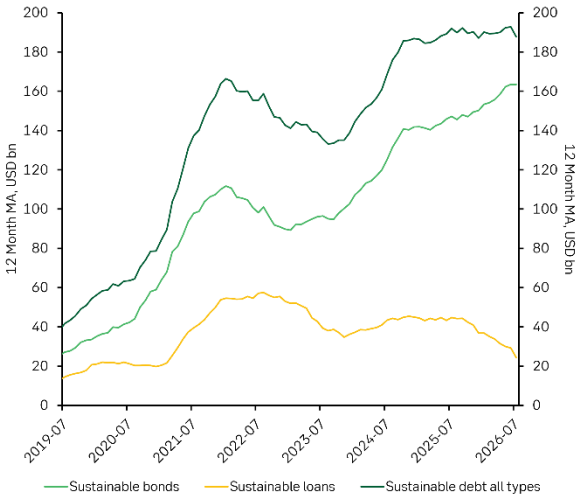

Source: BloombergNEF, SEB as of July 31, 2026

## Sustainable bond market grows

The global market for sustainable bonds continued to expand through July 2026, with issuance reaching USD 1,226bn, 15% YOY growth. Including labelled loans, total sustainable debt issuance reached approximately USD 1,400bn, illustrating stagnant YOY growth, suggesting that market momentum remains concentrated in bonds rather than loans. The composition of issuance also points to a narrower growth story led by traditional use-of-proceeds bonds, while sustainability-linked formats continue to decline.

Sustainable debt issuance continues to gain momentum, with the 12-month moving average reaching record highs by mid-2026. Growth has been overwhelmingly driven by sustainable bond issuance, while sustainable loan activity remains well below the levels seen during the 2021-2022 market peak.

**Figure 13 Sustainable debt transactions moving average**




Source: BloombergNEF, SEB as of July 31, 2026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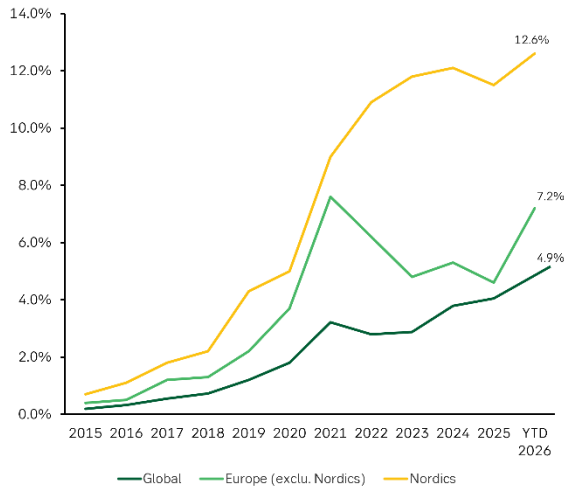
Sustainable bonds account for a rising share of overall bond market activity, with the rising global share reaching 4.9% YTD 2026, up from 4.0% in 2025. The Nordics remain the clear outlier, with sustainable bonds representing 12.6% of total bond issuance, while Europe excluding the Nordics has rebounded strongly to 7.2%, above recent full-year levels. We note that, in comparison to previous reports, there has been a change in methodology. Preliminary securities have been removed from the screening, and only active bonds are now included. This results in a higher reported share of sustainable bonds compared with earlier reports.

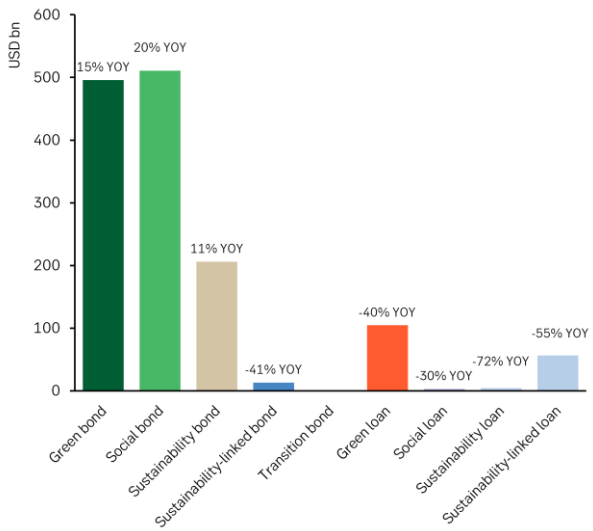
**Figure 14 Sustainable bond market share**




Source: BloombergNEF, SEB as of July 31, 2026

Use-of-proceeds bonds continue to dominate issuance, with green and social bonds broadly neck-and-neck globally. Through July 2026, social bond issuance reached USD 511bn, marginally ahead of green bonds at USD 496bn.

**Figure 15 Sustainable debt transaction by type**

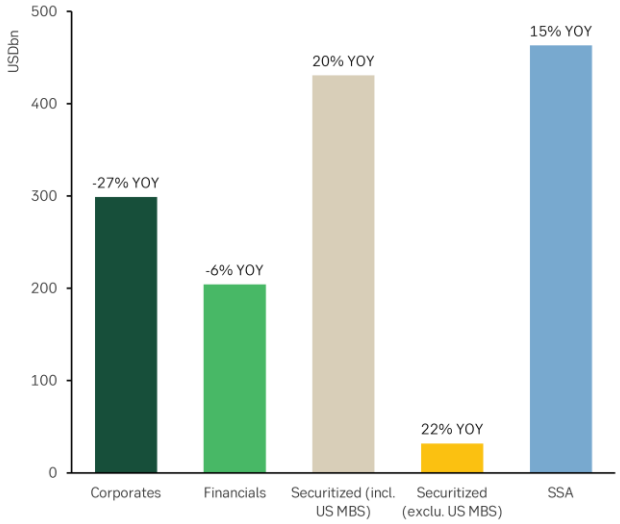



Source: BloombergNEF, SEB as of July 31, 2026

The more notable development has been the surge of sustainability bonds, particularly in Europe, where issuance reached USD 199bn and increased by more than 200% YOY. By contrast, only USD 11bn in sustainability-linked bonds have been issued globally through July 2026.

Year-on-year growth in sustainable bond issuance has differed by sector trends. SSA issuance continued to expand year-on-year and remain the primary driver of market growth, while securitized issuance also increased from 2025 levels. In contrast, issuance from both corporates and financials declined year-on-year, reducing their overall contribution to sustainable bond volumes. The strength of SSA issuance was particularly relevant in Europe ex-Nordics, where public-sector and development finance institutions provided a significant share of the market activity.

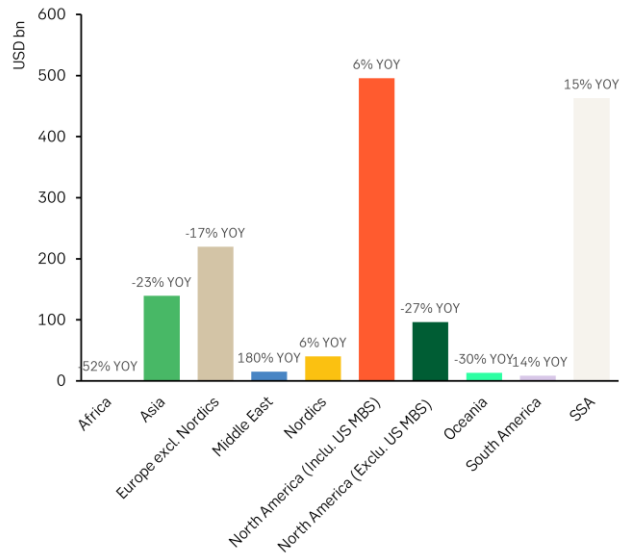
**Figure 16 Sustainable debt transactions by sector**




Source: BloombergNEF, SEB as of July 31, 2026

North America remains the largest regional contributor, with approximately USD 485.9bn of sustainable debt issued through July 2026, followed by Europe excluding the Nordics at US 387bn, Asia at USD 162 bn, and the Nordics at USD 41bn. However, regional ranking continues to be materially influenced by the inclusion of securitized issuance. North America's position is closely linked to the sizeable US mortgage-backed securities market, which continues to represent an outsized share of regional volumes. Excluding mortgage-backed securities, however, North American issuance is down 27% YTD, underscoring how heavily volume depends on MBS.

**Figure 17 Sustainable debt transactions by region**




Source: BloombergNEF, SEB as of July 31, 2026

The Nordics remain overwhelmingly a green bond market. Nordic sustainable bond issuance reached 41 bn USD through July 2026, of which USD 39.1bn came from green bonds. As a result, green bonds accounted for approximately 96% of Nordic sustainable bond issuance, making the region structurally distinct from the broader global market, which is more diversified. While global issuance is increasingly balanced between green and social formats, the Nordics story remains firmly centered on green bonds.

## EU ETS proposal redefines free allocations to drive investments

The European Commission's proposal to reform the European Emissions Trading System (EU ETS) seeks to balance strengthening Europe's competitiveness with promoting the investment needed to meet its climate ambitions. To support European competitiveness, the EU ETS uses free allocation to reduce the risk of carbon leakage—that is, companies relocating production outside the EU because of the bloc's carbon costs. Free allocation is intended to protect leakage-exposed sectors, including power and heavy industry, from losing out to producers abroad that face no comparable carbon price.

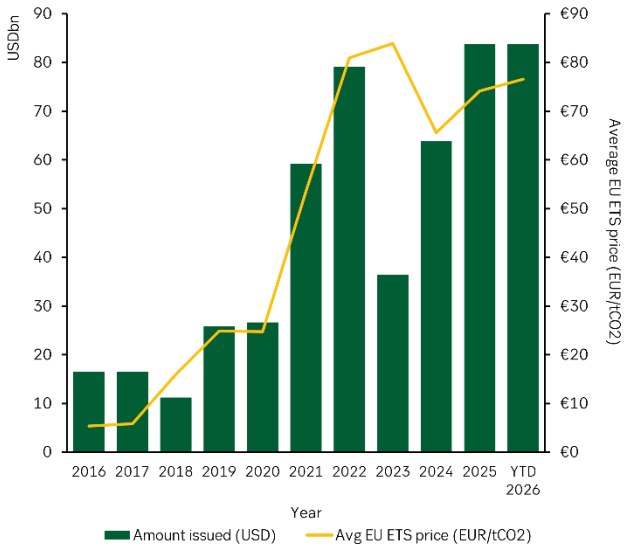
With its proposal, the Commission aims to expand the purpose of free allocation beyond preventing carbon leakage to also support investment in decarbonisation. The Commission concluded that free allocation had "not been conducive to driving transformational change" and "should be more clearly linked to needed investments". To that end, it proposes linking future free allocation to decarbonisation investment plans, with 80% of allowances issued upfront and the remaining 20% withheld until the investments are implemented.

To test whether the Commission is correct in its conclusions about the limited investment incentives created by free allocation, this analysis examines how sustainable bond issuance has developed across sectors covered by the EU's Carbon Border Adjustment Mechanism (CBAM): aluminium, cement, fertilisers, electricity, iron and steel.

Although these sectors have been eligible for up to 100% free allocation of emission allowances until 2026, they have not been unaffected by the rising EU ETS price. This is because the allowance price represents an opportunity cost for emitters. A company holding a free allowance faces the same choice as one that bought it at auction: use the allowance and forgo its market value, or cut emissions and sell it. Allowance prices therefore set the marginal cost of emitting, regardless of how many free allowances a company receives.

Since 2016, sustainable bond issuance from CBAM sectors has broadly tracked the EU ETS price, rising ~5x as the price climbed from ~EUR 5 to ~EUR 84/tCO2 between 2016 and 2022. The rising price aligns with the ETS's intended mechanism: a scarcity-driven carbon price that makes abatement increasingly attractive compared with paying for allowances.

**Figure 18 Sustainable bond issuance from CBAM sectors in EU vs. Avg EU ETS price**




Source: BloombergNEF, SEB as of July 31, 2026

That said, the relationship is not strong enough to suggest a perfect correlation, rather both series moved together during a period complemented by various policy pushes. The EU ETS was itself reformed under Fit for 55, raising the linear reduction factor from 2.2% (2021) to 4.3% (since 2024). In addition, Russia's invasion triggered a temporary gas-to-coal switch, whose higher carbon content pushed ETS prices up sharply in 2022 — a supply shock distinct from the compliance-driven path Fit for 55 set. And post-

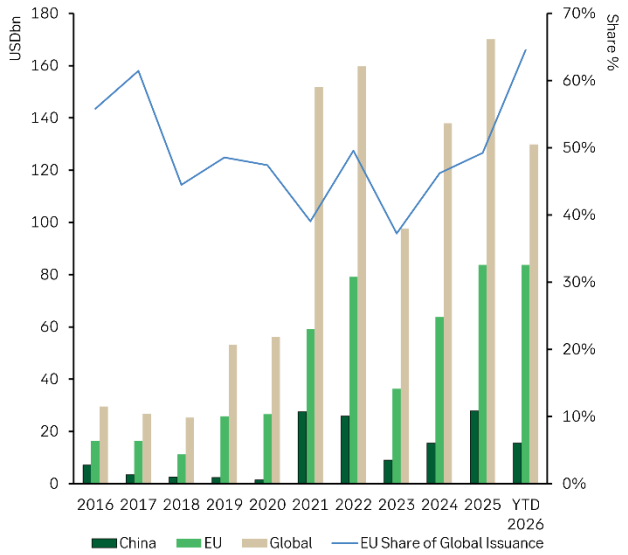
Covid's NextGenerationEU's Recovery and Resilience Facility, which allocated 37% of its €577bn[1] to climate objectives, gave issuers the fiscal capacity to respond to the EU ETS price signal.

Except for 2023, where there were elevated borrowing costs following global rate hikes[2] and in 2024, where falling ETS price fails to curb issuance, ETS price and CBAM-sector sustainable bond issuance have moved together over most of the observed period, consistent with price acting as one input into investment decisions.

## Europe's CBAM sector's total issuance lead

Since 2022, EU issuance of sustainable bonds from CBAM-exposed industries has run significantly ahead of China's, a gap that has widened as the two carbon markets have diverged in design. EU issuance has grown from ~USD 16bn in 2016 to ~USD 84bn in 2025, though the path included a steep decline in 2023, before recovering. China's issuance has been more episodic, consistent with phased sector entry into its national ETS, where at launch in 2021 the ETS only covered power generation and has since begun to expand to steel, cement, and aluminium.[3,4] Furthermore, Europe now accounts for the majority of global sustainable bond issuance from CBAM sectors, with its share growing significantly since 2023 and reaching ~65% YTD 2026.

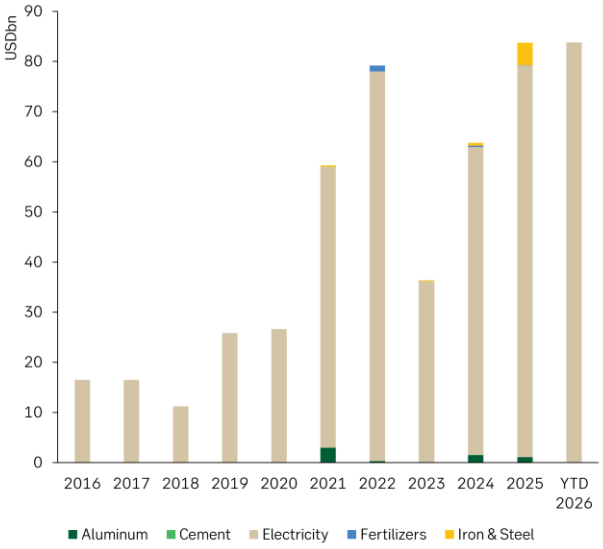
**Figure 19 Sustainable bond issuance from CBAM sectors China vs. EU vs. Global**




Source: BloombergNEF, SEB as of July 31, 2026

Electricity accounts for nearly all EU sustainable bond issuance across the CBAM-covered heavy-emitting sectors in Figure 20. Iron & steel, fertilizers, aluminium, and cement have very little issuance; combined, they never exceed a few billion dollars in any year. This concentration of issuance in electricity lines up with where the ETS has delivered abatement: roughly 75% of the scheme's historic emissions reductions have come from the power sector. Note that although electricity is covered by CBAM, it has experienced the largest reduction in free allowances of any EU ETS sector, with total allocations falling by 87% between 2013 and 2024. Electricity issuers decarbonized under a benchmark-based system designed to reward early movers with a widening cost advantage, as getting below benchmark sooner meant generating sellable surplus allowances while laggards remained net buyers.

**Figure 20 Sustainable bond issuance by CBAM sectors in EU by sector**




Source: BloombergNEF, SEB as of July 31, 2026

Green bonds dominate EU issuance throughout, but the composition shift tells a more interesting story. SLBs emerge in 2019, peak alongside the 2021–2022 issuance surge, then collapse to near-zero by 2025–2026 even as total issuance hits its highest levels. This is consistent with the broader market pullback from linked instruments illustrated in Figure 12 and Figure 15.

After Enel missed its 2023 emissions-intensity target, coupon step-ups were triggered on 10 sustainability-linked bonds and the utility scaled back its 2024–2026 ambitions. In 2025, Enel said the targets had served their purpose and its transition-aligned business model no longer required SLBs, framing the shift as more efficient market access rather than retreat.

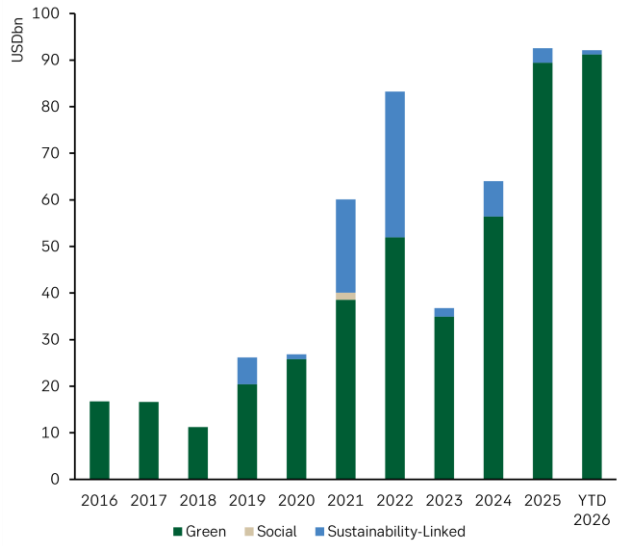
[1] Recovery and Resilience Facility

[2] Credit Trends: Global Financing Conditions: Bond

[3] Carbon Brief

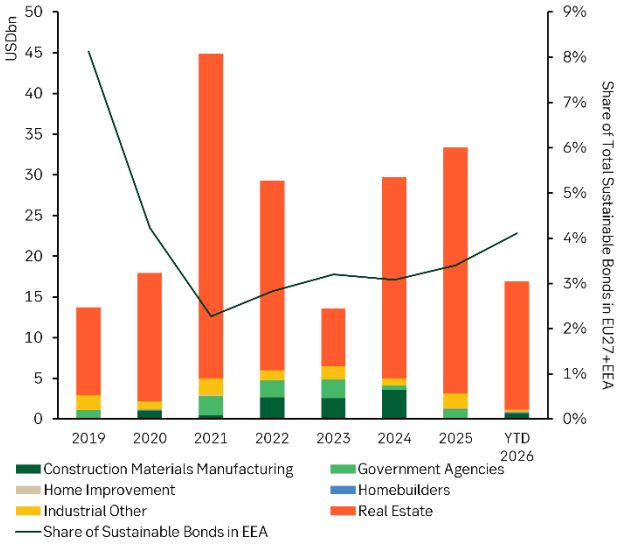
[4] China National ETS | International Carbon Action Partnership

**Figure 21 Sustainable bond issuance by CBAM sectors in EU by instrument**




Source: BloombergNEF, SEB as of July 31, 2026

**Figure 22 EU sustainable bond issuance by built environment sub-sectors**




Source: BloombergNEF, SEB as of July 31, 2026

## Majority of issuance in the built environment sector originates downstream the value chain

The EU ETS is becoming increasingly material across the built environment value chain. Carbon pricing directly affects producers of building materials such as steel and cement, while higher input costs can pass through to construction companies, real estate developers and owners.

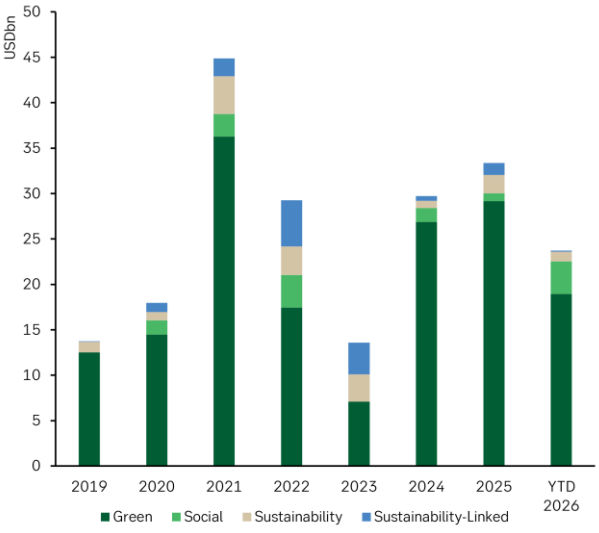
To complement the thematic research on how EU ETS price scenarios are impacting the levelized cost of production of steel and cement, we analysed sustainable bond issuance across the sub-sectors within the built environment whose value chains may be affected — to understand which have raised enough financing to be well-positioned against rising carbon costs, and which remain exposed.

Real Estate dominates issuance in every year, never falling below ~75–80% of the total, while construction materials manufacturing — the closest proxy to EU ETs-exposed cement and steel producers — remains consistently marginal, peaking at ~USD 3.5bn in 2024 before falling to near-zero by 2026. Government Agencies, Home Improvement, Industrial Other, and Homebuilders are negligible throughout.

Total issuance and the sustainable finance share diverge notably: 2021 posted the highest dollar issuance in the series ~USD 45bn but the lowest share of sustainable finance ~2%, as the broader sustainable finance market grew even faster that year and diluted this sector's relative share despite its own absolute peak. Despite this, the built environment sectors share of total sustainable bonds in the EU have been on a steady share growth since 2024, landing at ~4% YTD 2026.

Green bonds have been present every year between 2019-YTD 2026 and account for the majority of issuance throughout. While issuance through other instruments has declined in recent years, 2021–2023 saw more diversified activity, with Social, Sustainability, and Sustainability-Linked bonds each contributing meaningfully — a diversification that has since reversed, with issuance concentrating almost entirely in green by 2024-2026.

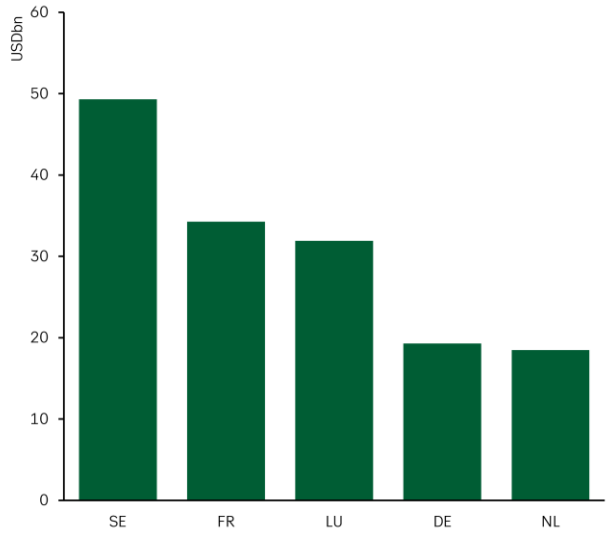
**Figure 23 Built environment issuance in EU by instrument**




Source: BloombergNEF, SEB as of July 31, 2026

Sweden leads built environment sustainable bond issuance in the EU at USD 49bn, roughly 45% ahead of France with the second highest issuance volumes, followed by Luxembourg, Germany, and the Netherlands rounding out the top five at roughly a third of Sweden's total.

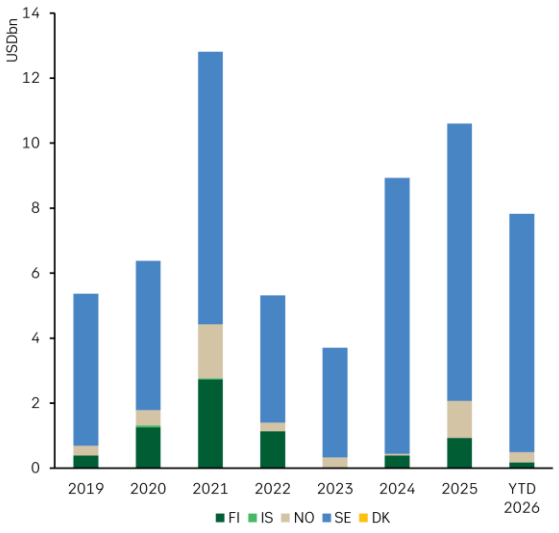
**Figure 24 Built environment issuance in EU by country (top 5) 2019-YTD 2026**




Source: BloombergNEF, SEB as of July 31, 2026

Within the Nordics, Sweden dominates issuance throughout the period, while Finland and Norway show modest but recurring activity — Finland's issuance is most visible in 2020–2022 and 2024–2026, while Norway contributes small, intermittent amounts, notably in 2021. Iceland and Denmark register almost no activity across the period. Swedish issuance is driven in large part by Vasakronan AB, which has issued ~USD 8.25bn in green bonds since 2019, accounting for 17% of all Swedish issuance.

**Figure 25 Built environment issuance in the Nordics**




Source: BloombergNEF, SEB as of July 31, 2026

## Real estate's inability to absorb costs may strengthen the case for abatement

Built environment issuance shows a parallel exposure to the value chain, not just the financing gap itself. Construction Materials Manufacturing, the sub-sector directly exposed to CBAM cement and steel compliance costs, has raised almost no labelled financing to offset that exposure. Real Estate, which is the sector with the overwhelming majority of built environment issuance, sits downstream: it doesn't face ETS costs directly but ultimately bears them as input costs passed through from cement and steel producers into construction and refurbishment spend.

The result is a mismatch along the value chain: the sub-sector causing rising compliance costs upstream (materials manufacturing) is the least financed to invest in abatement, while the capital that we have seen issued (Real Estate) sits at the end of the value chain, once cost pass-through has already occurred. If the proposal is adopted, we anticipate that rising carbon costs on steel and cement will eventually exceed real estate's capacity to absorb them, encouraging investment into less carbon-intensive buildings. These implications are further discussed in 'EU ETS reform and rising carbon costs in the built environment'.

## Delay of free allocation phaseout may weaken case for early-mover investments

Our data supports the Commission's conclusion that free allocation hasn't incentivized decarbonization in heavy industry: CBAM-sector sustainable bond issuance has risen, but mostly from electricity, which has faced steeper free allocation declines than other sectors. Under current rules, free allocation for all CBAM sectors phases out fully by 2034. Early movers stood to benefit, as shrinking allocation and rising prices would let them sell surplus allowances to slower-moving peers.

The Commission's new proposal weakens that incentive: it reinstates 15% free allocation and pushes full phase-out to 2038. This delays the reduced allowance supply early movers were counting on, cutting into the resale revenue they expected from decarbonizing ahead of peers.

That said, the Commission has proposed subsidies to back early movers: replenishing the Innovation Fund post-2030 and setting up an Industrial Decarbonisation Bank targeting EUR 100bn. Its first phase, *the Investment Booster*, would auction 400 million ETS allowances between 2028 and 2030, potentially doubling annual subsidies to ~EUR 26bn from current levels. First-come-first-served allocation, tied to project completion and verified emissions cuts, structurally favours early movers over laggards.

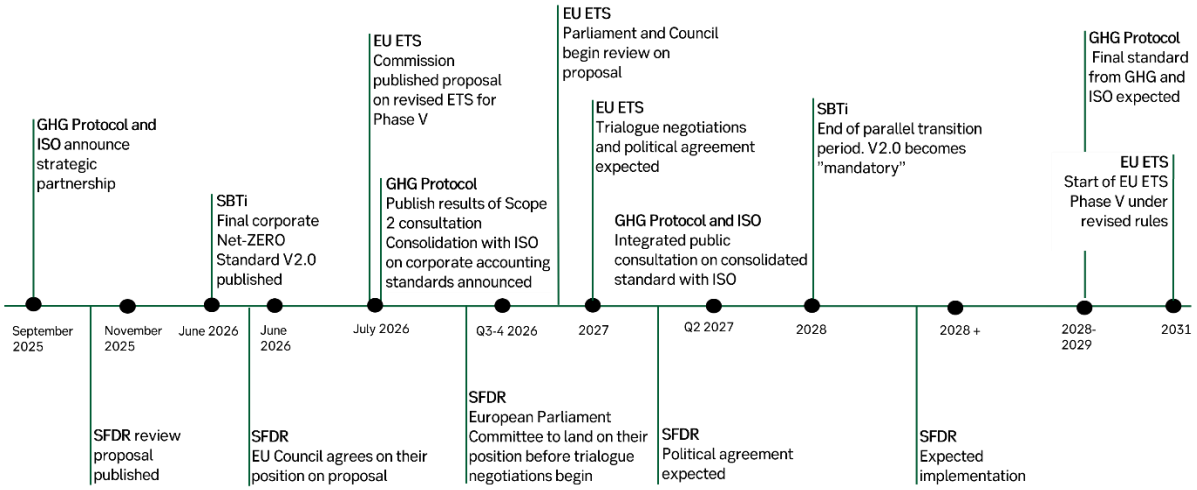
Despite the delay to free allocation phase-out, the Investment Booster raises an open question: will CBAM-sector sustainable bond issuance increase? Our initial read is that it likely will — and could go further, unlocking investment in alternative building materials that displace carbon-intensive steel and cement, such as timber construction.

# Regulatory update

Converging standards raise the bar for corporate transition

Consensus is emerging on what makes a transition strategy credible — moving beyond ambitious targets to an organisation's capacity to deliver them. This article examines recent regulatory and voluntary standard developments reshaping industrial decarbonisation and sustainable investment, for both investors and corporates.

**Figure 26 Timeline of framework revisions**




Source: European Commission

## Different frameworks, different definitions

Transition has become one of the defining concepts in sustainable finance. It appears in EU industrial policy, climate regulation, corporate reporting standards, and voluntary frameworks. Despite the growing importance of transition plans, there remains no universally accepted definition of transition.

## Corporate transition remains poorly defined

There is a lack of clarity in existing regulation on how to define what transition means at the corporate level. Under CSRD and ESRS E1, transition is primarily treated as a business strategy and governance concept. Existing regulation does not prescribe how companies should decarbonize but instead requires them to explain how their business model, strategy, actions, investments and governance structures align with climate objectives.

Transition plans therefore become tools for demonstrating strategic preparedness and accountability. The emphasis is on transparency, implementation planning, resource allocation and financial impacts rather than on any particular technology or emissions pathway.

## Investment rules overlook transition finance

The absence of a shared definition of transition also makes it harder to channel capital toward investments that support real-economy decarbonisation. In guidance for policymakers and investors developing net-zero-focused products under frameworks such as the SFDR and the UK SDR, the IIGCC argues that current rules and proposed reforms remain too focused on classifying investments as already "green", rather than recognising financing that enables credible transition. It identifies unclear criteria for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corporate transition alignment as one of the key factors holding back investments.[5]

## Standards converge on credible transition

In this article we review recent developments, including the EU ETS review, the European Commission's Electrification Action Plan, SBTi's Corporate Net-Zero Standard V2.0, ISO's Net Zero Guidelines, GHG Protocol Scope 2. While these frameworks differ in approach, ranging from industrial policy to climate science and corporate disclosure, they increasingly appear to be moving toward a common understanding of what constitutes a credible transition strategy.

## EU ETS links incentives to transition

The Commission's proposal to revise the EU ETS, published on 17 July, frames transition primarily as a matter of economic incentives and capital reallocation. While the reform is formally designed to align with the EU's newly adopted 2040 climate target, the Commission's objective is to maintain climate ambitions while improving industrial competitiveness. Importantly, the measures are only directly applicable to sectors and installations covered by the EU Emissions Trading System, although their effects may extend through value chains. Carbon pricing remains the central mechanism, but the July 2026 review also proposed an unprecedented EUR 100 billion expansion in subsidies through the Industrial Decarbonisation Bank, while making free allocation conditional on credible decarbonisation plans and related investments. The underlying theory is that transition occurs when market signals and investment frameworks make low-carbon technologies more attractive than high-emitting alternatives. The ETS is relatively technology-neutral; it is concerned with creating the economic conditions that drive industrial decarbonisation rather than prescribing a specific pathway.[6]

## Electrification reframes industrial transition

Released on the same day as the EU ETS proposal, the Electrification Action Plan frames transition as a physical transformation of Europe's industrial and energy systems. The plan's central objective is to make Europe the world's first "electro-powered continent", increasing electricity's share of final energy consumption from approximately 23% today to an indicative 46% by 2040, while reducing dependence on imported fossil fuels, strengthening energy security and improving industrial competitiveness. The implicit view is that decarbonisation will occur through the modernisation of industrial production processes and energy systems, making transition fundamentally an industrial competitiveness and economic resilience agenda rather than solely a climate agenda.[7]

## SBTi V2 links targets to execution

The second version of the SBTi Corporate Net-Zero Standard Version 2.0 (SBTi NZS V2), released in June, approaches transition primarily through the lens of climate science and emissions trajectories. Its central concern is whether emissions reductions are consistent with pathways that limit warming to 1.5°C. While the first SBTI NZS focused heavily on target setting, Version 2.0 places greater emphasis on implementation, governance, progress tracking and real-world delivery. To that effect, companies now need to publish detailed transition plans after target validation. Key technical elements of the proposed revision also include changes regarding Scope 1 emissions. For Scope 1 emissions SBTi NZS V2 moves beyond a sole focus on emissions reductions and places greater emphasis on the transition of underlying assets and technologies. The proposed revisions separate Scope 1 from Scope 2 target-setting and introduce more flexible approaches that can reflect asset replacement cycles and sector-specific decarbonization pathways. In practice, the changes strengthen the link between climate targets, transition plans and capital expenditure, reinforcing the view that credible transition is demonstrated through operational transformation and technology deployment rather than targets alone.[8]

## ISO formalises transition governance

ISO's original Net Zero Guidelines (IWA 42:2022) framed transition as an organisation-wide transformation process centred on governance, accountability, implementation, monitoring and continuous improvement. The recently released draft ISO 14060 Net Zero Aligned Organizations Standard builds on this foundation but represents a significant step towards a more formal and verifiable framework for net-zero alignment. Rather than focusing solely on emissions outcomes, the draft standard emphasises how organisations develop, implement and govern credible transition plans, embedding them within strategy, decision-making and business transformation processes. Key themes include transition planning, interim target-setting, validation and verification, transparent claims, and the management of residual emissions. In doing so, the draft standard reflects a broader shift across climate frameworks from defining ambition towards demonstrating implementation, positioning transition as both an emissions reduction challenge and an

[5] A summary for policymakers.pdf

[6] European Commission, EU ETS Review Q&A, 2026; ICAP, 2026

[7] European Commission, Electrification Action Plan, 2026

[8] SBTi Corporate Net-Zero Standard V2.0, 2026

organisational capability that must be evidenced through governance, execution and measurable progress.[9]

## Scope 2 revisions raise integrity

The GHG Protocol's proposed revision of Scope 2 reporting, released for public consultation in October 2025 after being approved by the Independent Standards Board in July 2025, retains dual reporting through both location-based and market-based methods but introduces stricter requirements for the latter. Proposed concepts such as hourly matching and deliverability would require companies to better align renewable electricity procurement with when and where electricity is actually consumed, strengthening the link between market-based claims and real-world decarbonization outcomes. Overall, the revision signals a shift toward greater environmental integrity and a closer connection between emissions accounting and transition outcomes.[10]

## SFDR Update

The ongoing review of SFDR aims to simplify disclosures and replace the current Article 8 and 9 classifications with three clearer product categories: Sustainable, Transition and ESG Basics. The objective is to make sustainability information easier for investors to understand, improve the comparability and credibility of sustainable investment products, reduce reporting burdens and limit greenwashing risks. Ahead of a European Parliament vote expected in September, the Council has broadly endorsed the Commission's proposed categorisation while suggesting several refinements before trialogue negotiations begin later in September.[11]

To strengthen comparability, the Council proposes that Sustainable and Transition products disclose at least three standardised sustainability indicators. It also clarifies that investments in fossil-fuel-related companies may qualify for the Transition category, provided that at least 20% of capital expenditure is Taxonomy-aligned and supported by a credible, time-bound emissions reduction plan covering Scope 1 and 2 emissions. These investments would additionally be subject to enhanced adverse impact disclosure requirements. Finally, recognising the practical challenges of portfolio implementation, the Council proposes a three-year phase-in period for funds to meet the required 70% investment threshold across all categories.

## Convergence on transition credibility

While the CSRD, EU ETS, Electrification Action Plan, SBTi, ISO and GHG Protocol originate from different policies and serve different purposes, they appear to be converging around a common understanding of what constitutes a credible transition strategy. Historically, credibility was often associated with the ambition of climate targets or net-zero commitments. Increasingly, all frameworks place greater emphasis on implementation, execution and evidence of real-world transformation in the latest revisions.

The revised EU ETS increasingly links subsidies and free allocations to decarbonization investments, while the European Commission's Electrification Action Plan focuses on whether companies and industries are investing in the technologies and infrastructure needed for decarbonization. Similarly, CSRD requires companies to explain how their transition plans are embedded in strategy, governance and resource allocation, while SBTi Version 2.0 places greater emphasis on implementation, progress and accountability in addition to target setting. ISO's Net Zero Guidelines reinforce this direction by emphasizing governance, monitoring and organizational capability as prerequisites for delivering net-zero commitments.[12]

Together, these frameworks suggest that transition credibility is increasingly assessed through a combination of factors: a clearly articulated transformation pathway, alignment of capital expenditure with transition objectives, measurable and science-aligned emissions reductions, robust governance and accountability structures, with reporting requirements on transition progress.

## Residual emissions follow feasible abatement

The EU ETS, SBTi V2 and the ISO Net Zero Guidelines reflect an evolving understanding of residual emissions and their role in the transition to net zero. While SBTi V2 continues to emphasize deep emissions reductions as the primary objective, it also recognizes the need for companies to address emissions that cannot yet be eliminated. ISO takes a similar position, defining residual emissions as those remaining after all feasible abatement actions have been implemented and recommending that they be neutralized through high-quality removals. At the same time, European climate policy is increasingly recognizing the role of carbon removals, carbon capture and other solutions for hard-to-abate sectors. Together,

[9] ISO - ISO launches public consultation on the world's first International Standard for net zero alignment today)

[10] GHG Protocol Announces Key Standard Development Updates | GHG Protocol

[11] Council agrees position on simpler transparency rules for sustainable financial products - Consilium

[12] ISO - ISO launches public consultation on the world's first International Standard for net zero alignment today

these developments suggest a growing consensus that residual emissions must be managed, but only after ambitious decarbonization efforts have been pursued.

## ISO and GHG Protocol converge

In July 2026 the consolidation of GHG Protocol and ISO corporate greenhouse ga accounting standards was announced.[13] For companies and investors, the move signals a shift towards greater interoperability between reporting, target-setting and assurance frameworks, reducing fragmentation while strengthening the credibility and comparability of emissions disclosures. The partnership also reflects a broader trend across sustainability regulation and standards towards convergence, with the stated objective of establishing a common global language for emissions accounting that can support corporate transition planning, regulatory reporting and sustainable finance decision-making.The announcement of the consolidation with ISO corporate accounting standards likely means that the proposed revisions on GHG Protocol Scope 2 reporting will not be released prior to the planned public consultation on the consolidated standard in Q2 2027. The consolidated standard will likely be leaning toward the same direction as the proposed revision of Scope 2 reporting as well as incorporating the feedback received in the consultation.

## Convergence raises the evidence bar

Frameworks that rely on GHG Protocol, including SBTi, CSRD/ESRS and ISO Net Zero Standard, would likely need to adapt harmonised emission reporting guidance. The changes could reinforce current efforts to move beyond target ambition towards implementation credibility, increasing scrutiny of how companies source low-carbon electricity and demonstrating whether reported emissions reductions are aligned with genuine power-sector decarbonization. The highest probability outcome being a broader convergence around the principle that transition claims should increasingly be supported by evidence that corporate actions contribute to real-economy decarbonization, not only lower reported emissions.

## Potential implications for corporates

Companies may face growing scrutiny of how transition commitments will be financed, governed, implemented and ultimately delivered. This shifts the challenge from defining ambition to demonstrating execution. As investors, lenders and regulators gain access to more comparable transition-related information, credible transition strategies are increasingly characterised by clear operational roadmaps, technology deployment plans, capital allocation decisions, governance structures and transparent performance monitoring. In this evolving landscape, transition capability is increasingly becoming a source of strategic competitiveness, potentially influencing access to capital, stakeholder trust and long-term corporate resilience.

## Investors must assess execution, not just ambition

For investors, the challenge shifts from assessing ambition to assessing capability. The most credible transition strategies appear to be those that combine a science-aligned pathway, clear technological choices, committed capital expenditure, robust governance and demonstrable implementation. Importantly, this direction is increasingly reflected in the ongoing evolution of the Sustainable Finance Disclosure Regulation (SFDR), where proposed reforms place greater emphasis on sustainability outcomes, transition characteristics and the management of adverse impacts rather than relying solely on broad ESG classifications. In this emerging landscape, investors may need to demonstrate not only that portfolio companies have credible transition plans, but also how investment strategies support and monitor real-world transition progress. As a result, transition capability may become as important an investment consideration as emissions performance itself.

## Conclusion

Taken together, these developments are likely sufficient to establish more of a market consensus on the core content of credible transition: science-aligned emissions pathways, financed implementation plans, accountable governance, comparable reporting and evidence of real-economy delivery. They are likely not yet sufficient to produce an immediate or uniform reallocation of capital. Key rules remain under negotiation, methodologies still diverge and implementation timelines extend from 2027 into 2029, while many investment decisions depend on sector economics, policy stability, data quality and investable project pipelines. The more plausible outcome is therefore phased convergence: transition criteria may begin influencing engagement, product design and risk assessment before they materially affect pricing and portfolio allocation, with stronger capital-flow effects emerging only once standards are final, disclosures become comparable and regulatory incentives operate consistently. In short, the direction of travel is increasingly clear, but market consensus on definition is likely to precede consensus on valuation- and measurable capital reallocation-by several years.

[13] GHG Protocol Announces Key Standard Development Updates | GHG Protocol

| Framework / Policy | What constitutes a credible transition? | Evidence |
|---|---|---|
| **EU ETS** | Demonstrable reduction of real-world emissions through deployment of low-carbon technologies and replacement of carbon-intensive production processes. | Verified emissions reductions, fuel switching, electrification, industrial transformation, ETS compliance and declining allowance exposure. |
| **EU Electrification Action Plan** | Substitution of fossil fuel use with clean electricity across industry, buildings and transport, supported by enabling infrastructure. | Rising electrification rates, deployment of electric technologies, grid investments, flexibility solutions, storage capacity and renewable power integration. |
| **GHG Protocol** | Reliable measurement of emissions and consistent accounting of progress over time. The framework does not define transition itself but provides the measurement foundation for assessing it. | Robust Scope 1, 2 and 3 inventories, transparent methodologies, comparable reporting and consistent emissions data. |
| **SBTi V2** | Delivery of emissions reductions consistent with a science-based pathway to net zero, supported by implementation measures and credible transition planning. | Science-based targets, progress against interim milestones, transition plans, procurement decisions, operational decarbonisation, value-chain engagement and management of residual emissions. |
| **ISO Net Zero Guidelines** | Organisation-wide transformation embedded in governance, strategy, planning and continuous improvement processes. | Documented governance structures, transition plans, management systems, implementation evidence, monitoring processes and continual improvement mechanisms. |
| **CSRD / ESRS E1** | Integration of climate objectives into business strategy, governance, investments and operational decision-making, supported by transparent disclosure of how targets will be achieved. | Transition plans, climate targets, allocated capital expenditure, implementation actions, governance arrangements, financial impacts, risks, opportunities and progress reporting. |
| **SFDR (proposed categorisation framework)** | Investments are supported by companies that can demonstrate a credible and measurable transition toward sustainability objectives and management of adverse impacts. | Transition plans, principal adverse impact (PAI) disclosures, decarbonisation targets, capex alignment, sustainability indicators, progress reporting and evidence of implementation. |

**Table 1 Overview of transition terminology across frameworks[14]**

[14] Commission boosts Europe's competitiveness, decarbonisation and independence, GHG-Protocol-Scope2-Public-Consultation.pdf, ISO - ISO launches public consultation on the world's first International Standard for net zero alignment today, Directive - 2022/2464 - EN - CSRD Directive - EUR-Lex, Commission simplifies transparency rules for sustainable financial products - Finance

# EU ETS reform and rising carbon costs in the built environment

Building costs and balance sheet effects of future carbon pricing in the EU

Under the Commission's proposal, EU ETS prices could reach EUR 180–270/t by 2040, increasing steel prices by 50–100% and cement by 80–135%. Building costs may rise by up to 3%, yet developer margins could fall by 15–40%, depending on portfolio mix, incentivising value chain efforts to cut building material emissions and low-carbon alternatives.

## Rising carbon price exposure in the built environment

The EU Emissions Trading System (EU ETS) is becoming increasingly material across the built environment value chain. Carbon pricing directly affects producers of carbon-intensive materials such as steel and cement, while higher input costs can pass through to construction companies, real estate owners, developers and investors. Following the European Commission's latest proposal to reform the EU ETS, companies and investors in the European building sector will need to assess how future carbon prices could affect costs, margins and returns in the 2030s.

## Centerpiece EU climate policy at a crossroad

Covering around 40% of the EU's total emissions, the EU ETS forms the cornerstone of EU climate policy, together with the Union's binding 2040 and 2050 emission reduction targets. Its core purpose is to incentivise cost-efficient emissions reductions in sectors with large point-source emissions. The ETS sets a declining cap on total emissions and requires covered companies to surrender allowances corresponding to their emissions and allows allowances to be traded, so that emission reductions take place where they are cheapest. While the system has been successful in driving down emission covered by the EU ETS more than 50 % since 2005, it is now approaching structural barriers to further emissions reductions. To meet future ETS targets, energy-intensive industry including steel and cement will need to account for a significantly larger share of future emission reductions than the roughly 21 % it has delivered historically.

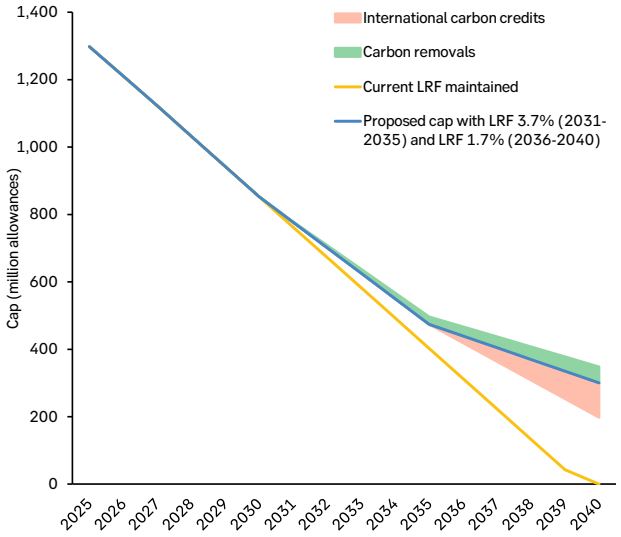
## Mounting pressure to reform the system

EU ETS allowance prices have risen sharply over the past decade, from below EUR 10/t on average in 2012–2018 to EUR 60–100/t since 2021. The increase reflects EU policymakers' growing reliance on carbon pricing to deliver more ambitious long-term climate and energy sufficiency targets. By early 2026, pressure to reform the EU ETS had intensified as allowance prices neared EUR 100/t, while European industry faced rising competition from Chinese imports. The European Commission's long-anticipated proposal therefore had to balance climate ambition with industrial competitiveness.

## Proposed policy realignment

On 17 July, the European Commission put forward a proposal for a comprehensive reform of the EU ETS. The Commission proposed lowering the linear reduction factor (LRF) from 4.3 % annually today to 3.7 % in 2031–2035 and 1.7 % in 2036–2040. This would largely align the EU ETS with the EU's target of reducing its emissions by 85 % by 2040. The Commission's proposal partly relies on emission reductions outside the ETS to soften the cap. To lower the LRF in 2036–2040 to 1.7 %, the Commission proposed the purchase of 260 million tonnes of international carbon credits. Furthermore, the proposal also envisions the auction of an additional 250 million allowances linked to permanent removals in 2031–2040, adding to the gross cap of the EU ETS and potentially lowering the effective LRF by up to 0.2% annually.

**Figure 27 Proposed EU ETS cap trajectory**




Source: SEB, European Commission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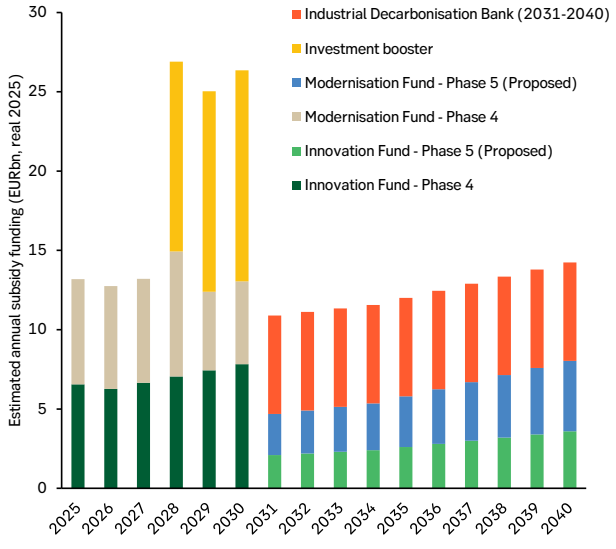
## Changes to free allocations

In the EU ETS, free allocation of emission allowances is used to limit carbon leakage by reducing the incentive for companies to relocate production outside the EU because of carbon costs. Under current rules, free allocation for sectors covered by the EU's Carbon Border Adjustment Mechanism (CBAM), including steel and cement, was due to be fully phased out by 2034. The Commission now proposes to restore 15% of free allocation for CBAM sectors and postpone the full phase-out to 2038. At the same time, the Commission plans to make free allocations conditional on plans to invest in decarbonisation in the EU and verified implementation, with 80 % granted upfront and 20 % released only once implemented.

## Subsidies increase to benefit early-movers

Concerns that EU ETS reforms would penalise companies already committed to major decarbonisation investments, especially in steel and cement, are partly addressed through expanded ETS-funded support. The Commission proposes to replenish the Innovation Fund after 2030, continue the Modernisation Fund and establish an Industrial Decarbonisation Bank aiming to raise EUR 100bn. Its first phase, the Investment Booster, would auction 400 million ETS allowances in 2028–2030, potentially lifting annual subsidies to about EUR 26bn — roughly twice today's level. On a "first in, first served" basis, and linked to completion and verified emissions reductions, the reforms would favour first movers.

**Figure 28 Proposed EU ETS funding by instrument**




Source: SEB, European Commission, based on Central EU ETS scenario

## EU ETS price scenarios

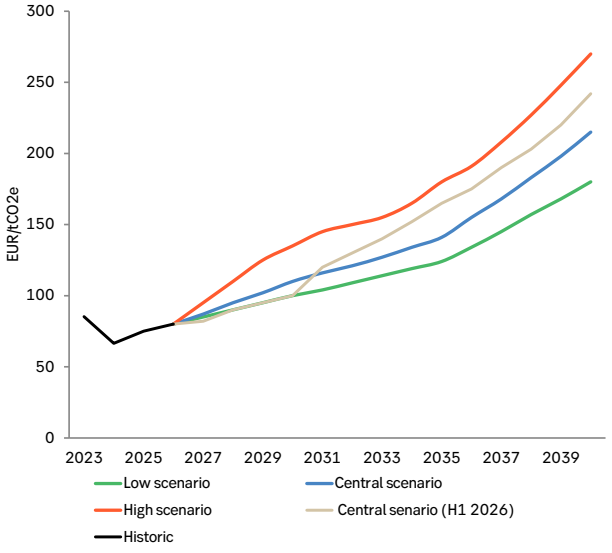
Following the Commission's proposal, future EU carbon prices will depend not only on the speed of cap reduction, but also on how much flexibility the system can deliver in practice: the lower proposed LRF would ease scarcity, but this depends on the availability of high-integrity international credits and permanent removals. The effect of subsidies on lowering demand for allowances will also depend on whether these resources are deployed at scale and quickly enough to reduce industrial emissions. Free allocation changes also matter: a slower CBAM phase-out reduces near-term compliance costs for some industrial producers, while tighter conditionality could squeeze allowance supply or bring forward decarbonisation investments. We therefore use three scenarios to capture different combinations of policy delivery, market confidence and decarbonisation speed.

Notably, our low and central scenarios suggest that European allowance prices will remain below previous expectations, particularly after 2030.

**1. Low price / Policy success scenario**

This scenario assumes the Commission succeeds in sourcing high-integrity removals and international carbon credits from 2031, lowering the effective LRF to 3.5% from 2031 and 1.5% from 2036. Auctioning 400 million allowances for the Investment Booster increases liquidity and limits near-term price pressure. Subsidies are deployed quickly, with limited permitting delays, enabling substantial heavy industry emission reductions from 2028 and lowering demand for allowances. The free allocation phase-out proceeds as proposed, while the delay to 2038 helps offset stricter conditionality and the withholding of 20% of free allowances until emissions reductions are verified. Any unclaimed free allocations are returned to the system after 2040, easing forward prices in the late 2030s. Under this combination, allowance prices remain broadly within the EUR 80–100/t range until 2030, before rising gradually to around EUR 180/t by 2040.

**Figure 29 EU ETS price scenarios, real 2025 prices**




Source: SEB, European Commission, Enerdata

**2. Central scenario**

In the central case, the Commission is only partly successful in sourcing high-integrity removals and international carbon credits from 2031. The LRF therefore remains at 3.7% until 2036 and above 1.7% thereafter, keeping scarcity higher than in the policy success scenario. Subsidies are fully deployed, but permitting delays mean material reductions in heavy industry emissions do not begin before 2030, limiting the near-term fall in allowance demand. Assumptions on the free allocation phase-out and conditionality are unchanged from the low-price scenario Under these conditions, allowance prices rise to EUR 110/t in 2030 and around EUR 215/t by 2040.

**3. High price / Policy under-delivery scenario**

This scenario assumes the Commission secures less than one-third of the planned international credits and permanent removals, keeping the effective LRF and compliance demand higher than in the other scenarios. Subsidy deployment is slower and less effective than in the central case, with limited impact on industrial emissions before the mid-2030s and therefore a weaker reduction in allowance demand. Free allocation phase-out and conditionality are unchanged from the low-price scenario, but more restrictive recycling of unclaimed free allocations after 2040 tightens expectations already from 2036. Under these conditions, allowance prices rise to EUR 135/t in 2030 and around EUR 270/t by 2040.

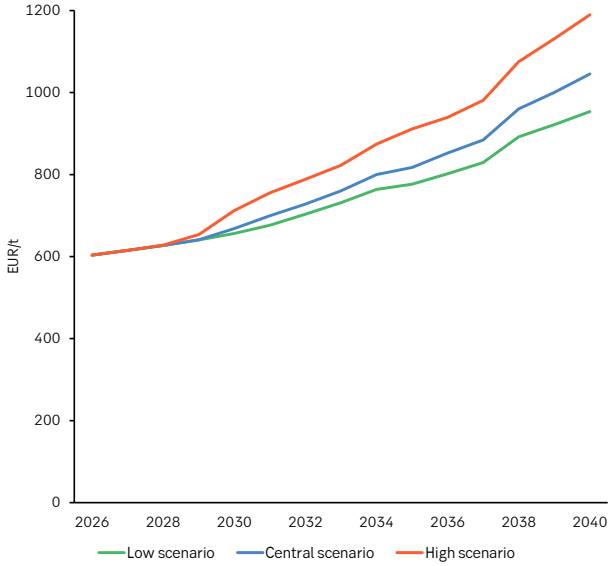
## Impact on building material costs

Producers of steel, cement, and other construction materials at risk of carbon leakage could, until 2026, offset up to 100% of their emission allowance obligations through free allocations. Even though free allocations come at no direct cost to emitters, they still carry an opportunity cost: a firm receiving them for free can still sell them on the market instead of using them. This means that the EU ETS sets the marginal cost of emitting regardless of how many free allocations were received. As free allocation phases out — even when postponed to 2038 under the Commission's proposal for CBAM sectors — the cash cost a firm actually pays converges with the marginal carbon cost already embedded in its pricing, closing the gap between the two that free allocation has maintained until now.

## Future market price of steel and cement

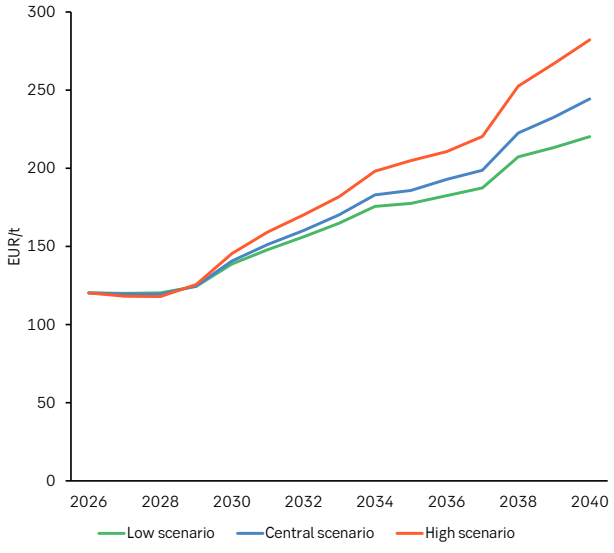
SEB has developed a proprietary tool to assess the cost of producing carbon-intensive commodities, including steel and cement in Europe. The tool estimates how changes in input costs, technology assumptions and carbon prices affect production costs across different production routes. Market prices are typically set by the marginal producer: the highest-cost established production option still needed to meet demand. The impact of future EU ETS prices on market prices therefore differs materially by commodity, scenario and year, reflecting differences in emissions intensity, free allocation exposure and available decarbonisation options. The estimates below show future market prices for steel and cement under different EU ETS price paths, holding other cost drivers such as power, weighted cost of capital or labour costs constant.

**Figure 30 Estimate future crude steel market prices in Europe, by EU ETS scenario, real 2025**




Source: SEB

**Figure 31 Estimated future cement price in Europe, by EU ETS scenario, real 2025**




Source: SEB

Future crude steel market prices rise differ sharply between EU ETS price scenarios. From a common 2026 level of around EUR 600/t, prices increase by roughly 50% in the low-price scenario, 70% in the central scenario and almost 100% in the high-price scenario by 2040. The divergence becomes pronounced after 2028, as sustained higher

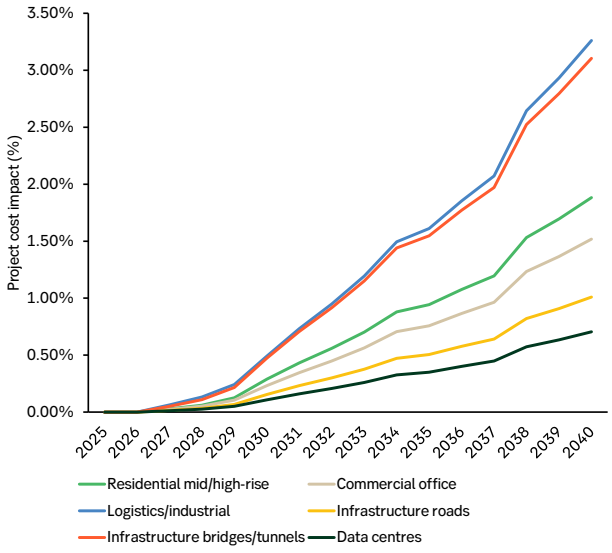
carbon prices raise the cost of carbon-intensive steel production and, in turn, the market price for steel.

Future EU ETS price have an even stronger impact on future cement market prices. From around EUR 120/t today, prices rise by roughly 80% in the low-price scenario and up to 135% in the high-price scenario by 2040. As with steel, the widening gap between scenarios after 2028 highlights growing exposure to carbon costs as more emissions-intensive production becomes increasingly expensive and lifts the market price.

## Total building costs set to increase

The effect of future carbon pricing on total building costs differs by scenario and building type. We assume that steel and cement producers pass through 80% of incremental production-cost increases to construction companies, and that construction companies pass through a similar share of higher material costs to real estate developers. Because steel and cement represent only part of total project costs, the impact on final building costs is smaller than the increase in material market prices. Total project costs also include labour, permitting and other building materials such as glass, which are not assessed in this analysis.

**Figure 32 Impact of EU ETS central scenario on total building costs, by project type**



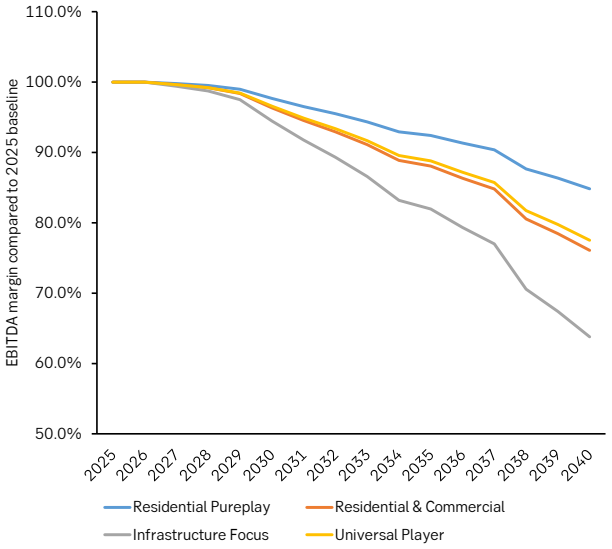

Source: SEB

Material-intensive infrastructure and logistics projects face the largest impact from rising EU ETS prices, with total building costs rising by more than 3% by 2040. Residential and office costs increase by a more modest 1.9% and 1.5%, respectively, reflecting lower steel and cement use per square metre of gross floor area. Data centres and roads are least affected: data centres because high project values dilute the impact of rising material costs, and roads because they use relatively little concrete and steel per square metre.

## Carbon pricing hit developers' bottom-line

The balance-sheet impact of higher EU carbon prices varies materially with portfolio mix. By 2040, developers concentrated in material-intensive infrastructure projects could see margins contract by almost 40%. For residential-focused developers or companies with a diversified portfolios or, margins could decline by 15% and 25%, respectively by end of the next decade.

**Figure 33 Impact of EU ETS central scenario on EBITDA margin, by developer type**




Source: SEB

## Conclusion

Our analysis suggests that the European Commission's proposed EU ETS reform could moderate carbon prices relative to earlier expectations, yet still drive substantial increases in steel and cement costs. Because material intensity varies significantly across building types, construction companies and developers may need to reassess project pipelines and portfolio exposure.

Even modest EU ETS-driven increases in total building costs could materially affect developers' margins, with potential knock-on effects across the value chain. To mitigate increasing cost pressures, developers may seek to pass a growing share of carbon costs downstream to investors, future owners or tenants, while also pressuring upstream suppliers to absorb more. Over time, landowners may also bear part of the burden through lower residual land values as higher construction costs reduce what developers can pay for land. Lower land value could even have fiscal impacts through lower future municipal land sale and land-lease revenues.

Taken together, the transmission of higher carbon costs through the building value chain could strengthen incentives to decarbonise steel and cement production and accelerate the substitution of carbon-intensive materials with timber and other lower-carbon alternatives.

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