

**Environmental Policy and Investment Location Decisions:
The Risk of Carbon Leakage in the EU-ETS**

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Abstract

I estimate the effects of the European carbon market (EU ETS) on investments, using novel data on cross-country investments from firms that are subject to it. I show that firms with higher emission intensities have increased their investments outside of the EU ETS area, but only when these investments are sizeable. I use this insight to estimate a structural model that links production to emissions and investment location decisions. The model can be used to simulate counterfactual emissions in different locations, to quantify the displacement of carbon emissions induced by the policy.