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**COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN
PARLIAMENT AND THE COUNCIL**

on the Commission's objectives, in the framework of the relations between the European Union and Latin America, in view of the 3rd Summit of Heads of State and Government of the European Union and Latin America and the Caribbean to be held in Guadalajara (Mexico) on 28 May 2004.

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1. THE RELATIONS BETWEEN THE EUROPEAN UNION AND LATIN AMERICA

This Communication defines the objectives of the Commission in the framework of the relations between the European Union and Latin America in view of the 3rd Summit of Heads of State and Government of the European Union and Latin America, to be held in Guadalajara (Mexico) on 28 May 2004. Nonetheless this Communication includes some specific references to the Caribbean countries whose participation at the Summit is of utmost importance for the strengthening of the bi-regional partnership.

The Guadalajara Summit will be the first Summit of Heads of State and Government in which the enlarged European Union and Latin American countries will have the opportunity to assess the current state of their bi-regional relations.

These relations, which aim at contributing to peace, political stability and economic development in the region, are of utmost importance for the European Union.

Social and political stability in Latin America is vital for global peace and security. The European Union is contributing to the creation and consolidation of structural stability in Latin America through political dialogue, cooperation and economic relations.

The European Union is interested in developing a political partnership with Latin America which promotes global governance and strengthening multilateralism. It is also interested in intensifying the dialogue with the region on the key issues discussed at major UN events and meetings. Latin America's deep commitment to multilateralism was reaffirmed at the last Presidential summit of the Rio Group in Cusco (Peru) which underlined "the need to reactivate initiatives related to the reform and update of the United Nations system, especially in collective security matters".

The European Union is Latin America's second most important trading partner. The European Union has gradually strengthened its economic and trade links with Latin America, resulting in trade figures that more than doubled between 1990 and 2002. European Union imports from Latin America increased from € 26.7 to € 53.7 billion, and exports to the region rose from € 17.1 to € 57.5 billion¹. This positive trend is bound to be reinforced thanks to the enlargement of the European Union which will become, as from 1st May 2004, an integrated market of 455 million inhabitants. The European Union will thus become the biggest market

¹ These figures include the Andean Community, the Caribbean region, Central America, Chile, Cuba, Dominican Republic, Haiti, Mercosur and Mexico

in the world, offering enormous possibilities for Latin American countries to sell their products to a wider range of consumers.

The European Union is also the most important source of foreign direct investment (FDI) for Latin America. Flows of European FDI to Latin America peaked in 2000 and have since diminished. However, the total stock of European investment in Latin America grew from € 176.5 billion in 2000 to € 206.1 in 2002².

Last, the European Union is the leading donor of development assistance for Latin America. In addition to the contributions from the Member States, since 1996 the European Community budget for Latin America has totalled more than € 500 million³ per year. Furthermore, between 2000 and 2003 the European Investment Bank invested € 1,104 million in the form of loans for projects of mutual interest to the countries of the European Union and Latin America.

2. THE RIO DE JANEIRO AND THE MADRID SUMMITS

Rio de Janeiro

The first Summit between the Heads of State and Government of Latin America, the Caribbean and the European Union was held in the city of Rio de Janeiro on 28 and 29 June 1999.

The Summit was convened as a result of the political will to enhance bi-regional relations and its objective was to strengthen political, economic and cultural understanding between the two regions in order to develop a strategic partnership.

The three strategic dimensions of this partnership are: a fruitful political dialogue respectful of international law and based on the strong attachment of both regions to multilateralism; solid economic and financial relations based on a comprehensive and balanced liberalisation of trade and capital flows; and more dynamic and creative co-operation in the educational, scientific, technological, cultural, human and social fields.

This partnership is built on shared values and aims to contribute to the furthering of common objectives such as strengthening representative and participatory democracy and individual freedom, the rule of law, good governance, pluralism, international peace and security, political stability and building confidence among nations.

Madrid

On 17 May 2002, three years after the Rio de Janeiro Summit, the second Summit of Heads of State and Government of the European Union, Latin America and the Caribbean took place in Madrid. This Summit consolidated the process which begun in Rio de Janeiro and confirmed both regions' commitment to the development of the bi-regional strategic partnership.

² These figures include the Andean Community, the Caribbean region, Central America, Chile, Cuba, Dominican Republic, Haiti, Mercosur and Mexico

³ These figures include the Andean Community, the Caribbean region, Central America, Chile, Cuba, Mercosur and Mexico

The decision to develop a more efficient political dialogue with the aim of bringing the positions of both regions closer together on international issues highlights the strategic dimension of this partnership. The Madrid Summit established new modalities of dialogue and consultation such as regular meetings of Heads of Mission in New York, Geneva and Vienna.

The conclusions adopted during the Summit reflect the convergence between the two regions on themes such as security, disarmament, terrorism, the fight against drugs and organised crime, and the eradication of small arms.

The Summit marked the conclusion of the Association Agreement with Chile, a particularly important result of the Madrid gathering.

The Heads of State and Government also noted the progress achieved in the negotiations with Mercosur and decided to call a Ministerial meeting in order to give the negotiations new impetus.

One of the most important themes addressed during the Summit was the future of relations between the European Union and the countries of the Andean Community and Central America. The Madrid Summit declaration gave a political mandate for the negotiation of political dialogue and cooperation agreements with these two regions. The Madrid meeting also opened the prospect of the negotiation of Association Agreements, including free trade areas. Two pre-conditions were established in this respect: the completion of the multilateral Doha development round, and the achievement of a sufficient degree of regional integration. The political and co-operation agreements were conceived to strengthen EU support for attaining higher levels of regional integration, which would contribute towards the fulfilment of the regional integration pre-condition.

The Summit also confirmed both parties' significant interest in strengthening bi-regional cooperation. In this context the Heads of State and Government underlined the importance of the @LIS and ALBAN programmes. These programmes aim at strengthening the links between the European Union and Latin America in the fields of information society and higher education respectively.

Follow up to the Madrid Summit

In Guadalajara both regions will report on progress made and actions undertaken since the Madrid Summit in the framework of EU-Latin American relations. Substantial progress has been made towards fulfilling the Madrid commitments.

The European Union and Chile signed an Association Agreement in November 2002.

The European Union also concluded negotiations of Political Dialogue and Cooperation Agreements with Central America and the Andean Community, signed by both sides in Rome in December 2003.

With regard to the EU-Mercosur negotiations, two ministerial meetings as well as several negotiating rounds have been held. The ministerial meetings agreed on a work programme that should now allow negotiations to be possibly concluded by the end of this year if circumstances at the Summit allow for it.

Turning to cooperation, it is worth highlighting that since the launch of the ALBAN scholarships programme at the Madrid Summit, a total of 251 grants have been awarded to

Latin American post-graduate students. Under the programme for the promotion of information technology, 19 demonstration projects began in October 2003 with the participation of 103 organisations from the European Union and 109 from Latin America.

New initiatives have been launched both at regional and sub- regional level:

At sub-regional level EU cooperation has focused on providing support for regional integration. This includes a project for "Harmonisation of Technical Standards, Technical Regulations and Conformity Assessment Procedures", aimed at facilitating the free circulation of goods between Mercosur member countries, and between Mercosur and the European Union; a trade- related technical assistance programme to support the process of the creation the Common Andean Market; and a programme supporting the Central American integration whose specific objective is to increase the capacity of the Central American Integration System (SICA) and of civil society to strengthen and deepen the process of integration and co-operation.

At regional level the Commission decided to contribute to the Programme for Democratic Government in Latin America (PRODDAL) led by the UNDP. Also, the Commission has approved a programme aimed at the creation of the Observatory of European Union-Latin America relations: a network of European and Latin American institutes to achieve a better understanding of regional and sectoral challenges in the framework of our relations. The Commission set up a web-mechanism for the presentation and dissemination of EU-Latin American and Caribbean bi-regional projects.

Furthermore, and in accordance with the decision taken by the Heads of State at the Madrid Summit, a bi-regional seminar to carry out an integrated analysis of the different issues of migration between the two regions was organised in Quito.

Also civil society has played an important role in contributing to strengthening the bi-regional partnership by reinforcing the links between both regions' civil society organisations and by conveying to the Summit its views on the most relevant aspects of our partnership.

3. COMMISSION'S PRIORITIES FOR THE GUADALAJARA SUMMIT

The Guadalajara Summit will be held in a more favourable economic climate than that of the Madrid Summit in 2002, a year in which Latin American recorded negative economic growth (-0.4%). According to the UN's Economic Commission for Latin America and the Caribbean (ECLAC), in 2003 Latin American growth reached 1.5%, exports grew by 8%, inflation was down to 8.5% from 12.2% in 2002, and for the first time in 50 years the current account of Latin America as a whole showed a surplus (0.4% of GDP).

In 2004, the regional economy is expected to grow by 3.5%, leaving behind the preceding "lost" six-year period, and gradually entering into an expansionary cycle. For the first time since 1997, there is no Latin American economy for which negative growth is projected.

However, these figures do not leave much room for complacency. Growth in 2003 was modest if compared with the growth of other regions such as East Asia, which that grew by 6.1% in the same period. And the picture of recovery is still uneven: the robust growth of Argentina and Costa Rica, for example, contrasted with the slower growth of Brazil and Mexico.

The resurgence of social tensions in several countries of the Latin American region, and the rise of the number of people living in poverty, cast some shadows on the prospects of consolidating the trend of economic recovery over the coming years.

In addition, there are other reasons for concern such as, the increasing political instability in the Andean region. After the crisis of October 2003 and the resignation of former president Sanchez de Lozada, Bolivia is in a critical situation; Venezuelan society continues to be bitterly divided between the fervent supporters of President Chavez and those who want him out of power; in Ecuador, President Gutierrez lost the support of the country's powerful indigenous movement; and Colombia remains embattled, fighting a war against guerrilla forces, paramilitary groups funded by extortion, kidnapping and drug money and sometimes indistinguishable from drug gangs.

The economies of Central America have on average been performing better than those of the rest of the Latin America. However democratic policies are jeopardized by criminal violence and corruption.

The Madrid Summit stressed that the top common priority of both regions is to strengthen the multilateral system on the basis of the purposes and principles of the United Nations Charter and international law. In particular, we underline the importance of the WTO as the main forum for promotion of trade liberalisation and the establishment of the basic rules and disciplines for the necessary regulation of the international trade system. The removal of trade barriers, based on stronger more transparent multilateral rules, allows everyone to benefit from the comparative advantages of their respective economies and fosters competitive integration in world trade and reduces the scope for protectionism. . The Doha Development Agenda launched in 2001 should bring benefits to all WTO members by increasing international trade and economic growth. This new round of negotiations should contribute to integrating developing countries into the world economy, including through special and differential treatment provisions, fully taking into account the priorities and concerns of our citizens and, promoting sustainable development. Both regions therefore supported the relaunch of the DDA negotiations decided in December 2003 after the setback of the Cancun Ministerial (September 2003). In view of its communication endorsed in December 2003 on "reviving the DDA - an EU perspective" and of recent declarations made by Latin American governments, the Commission expects the Guadalajara Summit to give renewed strong political support to the on-going negotiations, which should bring about significant progress by the Summer.

Social cohesion

According to the ECLAC, the number of people living in poverty Latin America reached 227 million in 2003, accounting for 44.4% of the population⁴ This percentage is higher than for Eastern Europe, the Middle East and North Africa, even though Latin America has a higher GDP per capita than those regions.

Political instability and social tensions are inextricably linked and are partially the result of the high levels of inequality, poverty and exclusion that prevail in Latin America. Inequality, poverty and exclusion weaken democracy and threaten peace and stability. Economic exclusion engenders political exclusion and vice-versa. By endangering social justice, inequality provokes social unrest and discontent.

⁴ "2003 Preliminary overview of the economies of Latin America and the Caribbean"

Social tensions and economic performance are also closely linked, since uncertainty of any kind negatively affects the behaviour of financial markets and investors.

Addressing these problems with the objective of increasing the levels of social cohesion is an overriding priority for Latin America. Latin America can no longer postpone taking bold measures in social and fiscal policies to respond to the signals of distress coming from a significant part of the population.

The Commission expects that concrete decisions will be taken in the field of social cohesion in Guadalajara. This is explored in more detail in section 4 of this communication.

Regional integration

In order to take full advantage of the favourable perspectives identified by ECLAC, it is also necessary to achieve a greater degree of economic integration between the countries of the region.

The insufficient degree of economic integration in Latin America can be appreciated by looking at the importance of intra-regional trade as a proportion of all trade; for Latin America the proportion is 15.4%, while for North America it is 40.3%, Asia 48.9% and Western Europe 67.3%.

This shortfall of effective regional integration constitutes a serious obstacle to the development of the region. Specifically, further integration is required if Latin America is to attract more foreign direct investment (in 2003 FDI was US\$29 billion, 25% less than in 2002 and substantially below the US\$38 billion that was the average for the period 1990-2002) and have a greater capacity to withstand and respond to external shocks.

The shortfall of effective regional integration is also an obstacle for deeper EU-Latin America relations. The EU has supported and continues to support the regional integration processes in Mercosur, Central America and the Andean Community. As far as Central America and the Andean Community are concerned, the Madrid declaration implies that further progress with regard to regional integration **is one** of the key conditions for the launch of negotiations on possible Associations Agreements. This progress is also needed for the satisfactory conclusion of the current negotiations with Mercosur.

The Guadalajara Summit should send a clear message with regard to the progress that is necessary in the field of regional integration and should give a new impetus to sub-regional integration processes in Latin America. These themes are examined in greater detail in section 5.

4. SOCIAL COHESION

During the 1990's Latin American countries began a process of economic restructuring and policy reforms and took substantial steps towards further democratisation. However, the benefits of democracy and development have not yet been felt by large sections of the population. Inequality, poverty and exclusion are a common pattern in all Latin American countries; they constitute a hindrance to economic development and they generate instability and discontent across the region.

It is urgent to deal with these problems in depth and move towards more political and social stability in the region.

Inequalities and exclusion in Latin America

According to the Inter American Development Bank⁵, Latin America consistently records the highest average level of inequality of any region in the world. The unbalanced income distribution patterns are evident when compared to other regions. The Gini Coefficient which measures inequality in terms of income distribution is higher in Latin America (0.51) than in South Asia (0.37) and Eastern Europe (0.29). In the late 1990s, the wealthiest 20% of the population received some 60% of the income, while the poorest 20 percent only received about 3 %.

Compounding the problem of inequality is social exclusion. Socially excluded populations in the region, by gender, age, race, ethnicity, disability and HIV/AIDS, migration status or other excluding features, share poverty, suffer multiple and cumulative disadvantages, stigma and discrimination. Socially excluded groups lack a voice and influence over the policy processes that shape structural reforms.

Their cost for the region

Inequality and exclusion have a high cost for the region. They not only slow the pace of poverty reduction and hamper sustainable development, but also fuel political and social instability.

Again according to the Inter American Development Bank, high income inequality may result in higher poverty levels since the poor obtain a smaller share of total income. If LAC's income distribution corresponded to the expected distribution for a region of its level of development, the number of poor people would be reduced by half. Reductions in equality can improve the contribution of economic growth to poverty reduction.

Social inequalities and exclusion prevent wide sectors of society from contributing to growth through consumption, savings and investment. This limits the expansion of internal markets. Inequality and exclusion reduce growth by reducing the opportunities of poor people and poor regions to improve their productivity and earnings, as well as by reducing competition, international competitiveness and efficiency in resource allocation.

Improving the low productivity of poor and excluded workers, which in many countries comprise more than half of the labour force, should be key to enhancing prospects for growth in Latin America. For example, rough estimates of the growth impact from expanding the educational and labour market opportunities of excluded groups show that Bolivia's GDP could increase by 36 percent, that of Brazil by 13 percent and Guatemala's by 14 percent.

Inequality and social exclusion have been linked, in LAC as well as in other regions, with social upheaval and threats to public safety, especially in countries with high ethnic or racial diversity. A lack of direct attention to problems of inequality and social exclusion may translate into social and political instability and low growth. Inequality and exclusion are closely associated in vicious circles with each other and with increased poverty, reduced growth and social and political crises.

⁵ American Development Bank, prepared a background document for the EC/IADB Seminar on social cohesion in Latin America and the Caribbean: "Inequality, exclusion and Poverty in Latin America and the Caribbean: Implications for Development"

The Commission's initiative

At the last ministerial meeting between the EU and the Rio Group (Vouliagmeni, March 2003), the Commission proposed to place social cohesion at the centre of bi-regional relations between the EU and Latin America and suggested that social cohesion should be one of the main topics at the Guadalajara Summit. The Commission announced the organisation of a joint European Union/Inter American Development Bank seminar on social cohesion. And it also announced that it would adopt a regional programme to promote the exchange of experiences and best practice between the both regions.

In the context of the Guadalajara Summit, and in a framework of close cooperation with the Inter American Development Bank, the Commission proposes that the Heads of State and Government take concrete decisions aimed at:

A. Encouraging Latin American countries to adopt sound and efficient policies to increase social cohesion by reducing poverty, inequalities and exclusion.

In this context three main sectors are concerned:

Democratic governance

According to the last Latinobarometro survey only one in five Latin Americans trusts their judicial system, only 17% trust their parliament or congress and only 11% trust political parties. Democracy is perceived as having failed to widen access to public goods such as equality before the law. It is not possible to develop inclusive societies if large parts of the population feel excluded from the political system. Measures that ought to be taken by LAC governments in this field include improving the functioning of electoral systems, guaranteeing the independence of the judiciary, improving the functioning and representative nature of political parties.

Social policies

According to the Inter-American Development Bank, the last decade witnessed substantial gains in social programs. However, social sector reforms did not overcome implementation problems nor did they succeed in significantly expanding access to quality health, including safe drinking water and nutritional health, education and housing services for the poor, thereby leaving many effectively excluded.

Therefore, sound and effective policies should urgently be implemented to increase access to quality health education and housing, to improve social protection systems, and to implement employment policies aimed at reducing segregation and discrimination across labour markets.

It is necessary that social policies and programmes go beyond achieving universal access to services to include the goals of equity and quality in education, health and housing, especially for the poor and excluded. Inequality not only appears between those who have access to services and those who do not, but also between those who have access to good services and those that only benefit from poor quality services.

The management of social policies should be improved, as should the effectiveness and efficiency of public spending.

Public finance and fiscal policy

High levels of inequality are closely linked to unfair and inefficient fiscal policies. Taxation policy has a special significance in LAC because of its potential to contribute towards the development of effective systems of democratic rule that effectively include the poor and disadvantaged. While weak states are deplored as one of the most serious shortcomings of the region, LAC government spending is low, partly because of limited institutional capacity for tax enforcement and inefficient tax collection. In comparison to industrial economies, government revenue in LAC countries relies more heavily on value added taxes than income taxes and property taxes. This hampers the redistributive role that the tax system should play.

LAC governments should consider fiscal reforms in order to increase their tax base, and in particular to promote equity and to allow for adequate levels of social spending.

B. Encouraging the international community, including international financial institutions, to support the measures referred to above.

International co-operation must support these efforts, while respecting the principle of ownership that implies that the countries concerned – their governments, businesses and civil societies – must lead the quest to build greater social cohesion. LAC countries should include all measures relevant to the reduction of poverty, inequality and social exclusion in their national plans. And international support and cooperation should be based on these plans. Reform programs supported by the international community and in particular by the international financial institutions should be carefully screened for their impact on social cohesion and social stability. And there must be more and better coordination between all donors including EU Member States.

International financial institutions and donors should support more counter-cyclical fiscal and monetary policies to deal with the negative impact of recessions as well as support social investments from a long term inequality reduction perspective. If growing economies are to improve social cohesion through the fight against poverty, exclusion and inequality, thus laying the foundations of sustained and stable growth, international financial institutions should pay attention to these aspects in the negotiation of macro-economic stability objectives for each country.

C. Intensifying cooperation between the European Union and Latin America in the field of social cohesion.

The principle of social cohesion lies at the core of the European Union's values. And that is also why the European Councils in Lisbon and Feira made the promotion of social cohesion an essential element in the Union's strategy to achieve its objective of becoming the most competitive and dynamic knowledge-based economy in the world by 2010.

The enlargement of the EU to include 10 new Member States on 1 May 2004 will require renewed efforts to promote social cohesion within the Union. The European Union has developed social policies and working methods that have proved successful. The experience gained by the European Commission and Member States in this field could be very useful for Latin America.

Cooperation between the European Union and Latin America should focus on the sharing of this experience and the transfer of European know-how. Attention should be given to experiences of the development, implementation and evaluation of social and fiscal policies in favour of social cohesion.

Before the Summit a programme of € 30 million aimed at facilitating the transfer of experience and know-how between public administrations of both regions in the fields of health, education, taxation and justice will be submitted to the Commission for approval. The programme will favour the development of networks of public administrations dealing with these policy sectors.

In deciding how to develop a European perspective on issues of poverty and social exclusion, the Lisbon European Council chose to draw on the experience of the European strategy for employment which has been in place since 1997. It thus adopted what is known as an Open Method of Coordination. This method allows for dialogue, exchange of experience, establishment of common objectives and evaluation of policies in areas relevant for fighting exclusion. The Commission encourages the countries of Latin America to launch a regional process which will create a new dynamic for dialogue and exchanges between countries of the region, allowing them to learn from each other's successes and failures. If the countries of Latin America were to decide to establish such a mechanism, the Commission would be willing to provide and finance technical support. In this context it is also worth noting the importance of social dialogue.

The Working Group

These objectives have been discussed in the working group on social cohesion set up by the Commission together with the Inter-American Development Bank after the seminar on social cohesion that took place in June 2003 in Brussels. Other institutions also participated in the group, such as UNDP and ECLAC, and various Latin American, Caribbean and European experts.

The group met twice (Mexico, October 2003 and Brussels, February 2004) and adopted a set of recommendations which inspire those proposed by the Commission and detailed above. These proposals have been addressed to the Senior Officials tasked with the preparation of the Summit. If approved, these recommendations will be submitted to the Heads of State and Government at the Guadalajara Summit.

The Commission encourages the Heads of State and Government to adopt these proposals at the Summit. They will provide a social cohesion agenda based on clear guidelines as well as fresh political support to shape policies oriented towards greater social cohesion.

5. REGIONAL INTEGRATION

Importance of regional integration in LA

The other key subject the Commission would like the Guadalajara Summit to focus on is the importance of deepening regional integration throughout Latin America. From the Commission's perspective, deepening the process of regional integration throughout Latin America is not an end in itself. In economic terms it will help the region fulfil its potential and facilitate the insertion of the individual countries into the international markets. Politically, it will allow Latin America to become a more influential player on the global scene.

The EU cannot be indifferent to achievements in the field of regional integration: we stand to gain from having a strong partner on the other side of the Atlantic with whom we can continue to expand our strategic alliance.

EU experience has taught us that the economic benefits of regional integration are substantial: bigger markets are more attractive to foreign investment; economic integration improves competitiveness; and it strengthens the region's capacity to withstand external economic shocks.

Regional integration is also important for stability and conflict prevention. Closer co-operation can be a catalyst for democracy and improved human rights. Regional integration provides opportunities for countries to become more active and influential partners in, rather than dependant spectators of, global, political, economic and social developments.

The absence of a regional integration system that effectively covers the whole Latin American region has led to the development of sub-regional initiatives. Beyond Mercosur, this is also true for sub-regions that have been characterised by political instability, internal and external conflict, and extremes of poverty and social exclusion, as is the case of Central America and the Andean Community.

The EU has always supported these regional integration initiatives and is convinced that they can make an important contribution to political stability, economic and social development and social cohesion within each sub-region. It considers that further progress towards deepening integration is a sign of political and economic maturity and their capacity to undertake reforms, and will continue to work with and provide support to these processes.

The EU's support to the process of sub-regional integration has taken the form of human resources development, institution building, support for the formation of customs unions and the development of common policies. In addition to the key role played by the Commission, exchanges have also involved other European institutions such as the Parliament, the Court of Justice and the Economic and Social Committee. Macroeconomic convergence is an aspect of economic integration that remains a challenge for Latin American's sub-regions. The Community is ready to continue supporting macroeconomic convergence efforts in Latin America through the provision of technical assistance.

The aim has not been and will be not to recommend a European model, but rather, where relevant, to share European experience with interested parties in Latin America.

As regards Central America and the Andean Community, the importance of making substantive progress in their respective integration processes was confirmed by the Heads of State and Government at the Madrid Summit. In defining the roadmap for future relations with both regions, the Madrid Declaration made any move towards an Association Agreement (including an FTA) conditional upon the completion of the DDA and the achievement of satisfactory degree of integration in both regions.

In doing so, the Madrid Summit made clear that the deepening of our relations with Central America and the Andean Community should proceed on a bi-regional basis. It remains the Commission's view that given the differences in economic weight and development, only bi-regional (as opposed to bilateral) agreements are sustainable in the long term and can offer benefits to both regions. In this context, the recently concluded Political Dialogue and Cooperation Agreements with Central America and the Andean Community mark an important step forward and underline the commitment of the Latin American partner regions and the EU to work together in support of current integration processes.

Governments participating in the Central American and the Andean Community integration processes expressed commitment to advancing towards deeper integration models.

Nonetheless, the integration measures actually put in place has not always corresponded to the commitment at political level. Bilateral avenues with third countries such as FTAs are sometimes pursued to the detriment of the integration process. The recent policy debate in the Andean Community shows that perceptions of the usefulness of such enhanced integration vary. In Central America the debate concerns the type of model of integration to be pursued.

Central America

Central America has made significant progress in conflict resolution, democracy and economic development over the past decade. Furthermore, since 2002 the re-launch of the regional integration process has become a priority for Central American governments. The EU enjoys additional credibility in the sub-region thanks to its political support for the pacification process and the return to democracy in the context of the San Jose Dialogue (initiated in 1984) and also thanks to the significant volume of development cooperation provided over the past two decades. There is a need to capitalise on this by playing a facilitating role in the field of Central American regional integration.

Although the process of Central American integration dates back to 1950, its first four decades were characterised by significant lapses and setbacks. However, since the establishment of a new integration framework in 1993, the Central American Integration System (SICA), the process of regional integration has moved ahead steadily, building on the stability provided by the resolution of the internal conflicts that existed in a number of countries. The necessity to take further steps towards economic integration was acknowledged by the Heads of State of the CA countries, who committed in March 2002 to adopting an action plan to complete the CA customs union by December 2003. The accomplishment of this objective has not been possible due in part to the proliferation of trade negotiations with numerous third parties, in particular the recently agreed Free Trade Agreement with the USA (CAFTA). Nevertheless, progress has been achieved in other respects, namely the harmonisation of 92% of tariff lines, the signature of a treaty on investment and services and the implementation of a dispute settlement mechanism. At the Belize Presidential Summit of 19 December 2003 a renewed commitment was taken to forge ahead with the customs union before the end of 2004. Progress will also need to be made on the removal of non tariff barriers, establishment of a common customs administration, implementation of common standards policies, etc. Furthermore, experience shows that real progress in regional integration will only be achieved if special attention is paid to the effective application and enforcement of approved measures. The shortfall of effective regional integration is also borne out by macroeconomic data, and indicators such as the current levels of intra-regional trade will need to be improved.

The Central American sub-region appears to have turned the page on the era of internal conflict and political instability. There is a high level of commitment to regional integration, which is seen as a necessity both to improve competitiveness and to prevent conflict. However in two countries there exist some doubts regarding the model of economic integration that should be followed (Costa Rica) and whether economic integration should be pursued at all (Panama, which has not yet confirmed its interest in joining the customs union, due to its highly service-oriented economy). At the institutional level, not all countries are members of the Parlacen and the Central American Court of Justice (CCJ).

Andean Community

As regards the Andean Community, the EU has supported the process of regional integration since its inception. In fact, with the establishment of the Andean Pact in 1969, regional

integration in this area was the first of its kind in Latin America. The Andean region was also the first in Latin America with which the EU concluded a Cooperation Agreement (1983).

During the 35 years of its existence, there have been various ups and downs in the process. A major step forward was taken with the Trujillo Protocol of 1996, which transformed the Andean Pact into the Andean Community, set up a wide range of regional institutions, and broadened the mainly economic and commercial agenda of the past to include co-operation on political and social matters. It is important to note that in addition to the objective of building a common external policy and launching the Andean Peace Zone, the Trujillo Protocol also set out the objective of creating a common market by 2005.

With political agendas often dominated by important domestic challenges, the Andean countries have not always been able to focus on the longer term benefits to be gained from regional integration and, as a consequence, the integration process continues to progress only slowly. Nonetheless, recent years have seen important new initiatives in the political field in areas such as conflict prevention, border cooperation, the fight against drugs and arms trafficking. Significant efforts have also been made to make the Andean Community a reality for its citizens, such as the introduction of an Andean passport, the establishment of working groups on consumer or indigenous matters, and direct elections to the Andean Parliament (not yet implemented in all CAN member countries).

It is in the area of economic integration, often hampered by structural differences between the different countries and a lack of political will, that the Andean Community has encountered particular difficulties. With internal trade liberalised since the mid-1990s between four of the five CAN countries (excluding Peru), the Quirama summit in June 2003 confirmed that the achievement of the common market remains the goal of all five Andean countries. Thus, notable progress was made in 2003 by the adoption of a decision to harmonise the Common External Tariff up to 62% for all five countries (up to 95% when excluding Peru). However, recently the entry into force of the latter decision was postponed. The five countries have adopted a Common Customs Classification which should enter into force at the beginning of 2005 but there is not yet a common customs administration. Intra-regional trade has increased a little but remains at a low level of 10-12%, indicating that important trade obstacles still remain. In addition, various initiatives taken by individual CAN member countries towards the conclusion of bilateral Free Trade Agreements outside the CAN framework risk undermining the integration process.

Moving towards Association Agreements with Central America and the Andean Community

The Madrid Declaration opened the avenue for the launching of Association Agreement negotiations with the Andean Community and Central America provided that two preconditions would be met, notable the completion of the Doha development programme and the achievement of a sufficient degree of regional integration. In view of the progress outlined before, and reconfirming the positive signal given in principle by the Madrid Declaration, the Commission believes that the Guadalajara Summit should help pave the way towards the opening of negotiations on Association Agreements, including FTAs. To that extent, all efforts have to be made by both sides to ensure that the Doha round advances as much as possible in 2004 towards its rapid conclusion, since any possible future FTA's shall be built upon the outcome of the Doha Development Agenda. The realisation of a sufficient level of regional integration would then become the trigger for launching negotiations.

In order to advance the process and make the most efficient use of scarce resources and time, the Commission proposes to start preparing the ground already at this stage for the opening of negotiations through a joint monitoring of progress in regional integration. By doing so, the Commission hopes that the perspective of negotiating Association Agreements including FTAs region-to-region becomes a meaningful incentive to these regions to continue their own processes of regional integration.

The Commission considers that it is important to define a clear set of criteria against which both regions' progress is to be measured and the attainment of which would be considered as satisfactory.

The Commission considers that a satisfactory degree of regional integration to launch FTA negotiations would include:

1. A fully operational **institutional framework**. This would entail assessing, among other things, effective mechanisms for furthering the regional integration project and for ensuring the implementation and enforcement of decisions, including a dispute settlement mechanism, the participation of all countries in all institutions and the design and implementation of sustainable financing mechanisms to support the institutional set-up;
2. The **creation of a customs union** compatible with Art. XXIV of GATT and notified to the WTO (including common external tariff, common customs administration and common external trade policy). Furthermore it would be necessary to assess the effectiveness of the customs union of which an indicator could be the progress of intra-regional trade.
3. The reduction of non-tariff obstacles to intra-regional trade. An increasing share of obstacles to trade is of a non-tariff nature. Therefore, special attention should be paid to the existence of effective rules that aim at removing these obstacles (either through harmonisation or mutual recognition), in particular in the area of technical regulations and standards and as regards sanitary and phyto-sanitary matters. It would also be necessary to encourage the concerned countries to adopt regional regulatory regimes on services and investment that facilitate future negotiations of FTAs with the European Union. And to assess whether legislation to protect intellectual property rights and rules on government procurement exist, and whether there is progress in the establishment of a regional competition policy.

In order to accelerate the process, and with a view to preparing the ground for the opening of the negotiating process, the Commission proposes, to make use of the existing institutional set-up and launch a monitoring process on progress in regional integration along the lines described above. Officials from both sides would meet on a regular basis to review the state of integration and assess whether the progress achieved permits the start of negotiations. This exercise would be done in parallel but independently with the Andean Community and with Central America.

In line with the Madrid conclusions, the future FTAs should build on the outcome of the Doha Development Agenda. The EU and Central America and the Andean Community have a shared interest to spare no energies in order to advance in the DDA negotiations. The scope of any FTA must provide added value to the multilateral regime.

Finally, as regards the immediate future of our trade relations with Central America and the Andean Community, the Commission would like to recall that trade relations with both

regions are currently based on the GSP-drugs regime, which offers extremely advantageous access to the EU market. The system has gained further in attractiveness as a result of the recently adopted amendment to the GSP regime, which limits the application of the graduation mechanism to principal GSP beneficiaries. The decision to extend the current GSP regime for an extra year implies predictability of the preferential regime for Andean and Central American countries until the end of 2005. The Commission is currently re-shaping the EC GSP and it is exploring ways to continue to provide preferential market access for import products from Central American and Andean countries after 2005.

Mercosur

The European Union has favoured and supported a strengthening of the process of regional integration in Mercosur and has therefore supported the Mercosur initiative from its very conception in 1991. The EU continues to work towards a stronger relationship with Mercosur and a deepening of the Mercosur process internally with a view to help Mercosur to establish an effective common market. Part of the current work between the EU and Mercosur, but also part of the negotiations of an EU-Mercosur Association Agreement, aims at reinforcing the internal Mercosur programme to complete its common market by 1 January 2006.

The EU-Mercosur negotiations would result in an association between two integrated regions. In fact it was shortly after the creation of Mercosur and the definition of solid objectives for deep integration towards a Mercosur common market, that the formation of an interregional association was first being considered.

The 'region-to-region' dimension of this agreement is thus creating new challenges to both partners as rules need to be defined between two players who internally are still developing their own set of intra-regional rules. Again, Mercosur integration is entirely interlinked with the on-going negotiations, and progress in deepening integration is needed both to successfully conclude the negotiations and to make the agreement work. This progress mainly relates to the institutional aspects and to the trade aspects of the Association Agreement which is currently being negotiated.

Political/Institutional aspects

The first objective of an enhanced political dialogue between the EU and Mercosur would be ensured through the creation of new institutional mechanisms already foreseen in the draft chapter of the agreement on political dialogue. Further, The EC welcomes Mercosur's initiative to appoint a well known political figure as the President of the Mercosur Coreper in the person of President Duhalde. This appointment contributes to the overall objective of further strengthening the institutions of Mercosur. In the same spirit, the further upgrading of the Mercosur Secretariat, the establishment of a Permanent Court for Dispute Resolution and efforts towards streamlining the Mercosur decision making process are important steps. The Commission hopes that this institutional strengthening will improve the implementation of decisions and ensure that political commitments are translated into effective regional integration.

Trade aspects

The EU believes that the completion of the Mercosur customs union is an essential basis to make this agreement possible. In addition, Mercosur integration should be pursued towards the establishment of a single market concept conducive to free circulation of goods, services and capital. To successfully conclude the negotiations it will therefore be essential that the

intra-regional rules are in place in the areas subject to interregional negotiations. In this respect, the EU will continue to negotiate with Mercosur in each of these areas in order to make this agreement truly ambitious and comprehensive, going beyond the respective WTO commitments.

To this end, the work programme agreed on 12 November 2003 during the last EU-Mercosur Trade Negotiators meeting at Ministerial Level established several comprehensive rounds of negotiation and two ministerial meetings. According to this programme, the future comprehensive trade chapter will include a free trade agreement in goods and services. Further it will also cover inter alia market access/rules on government procurement, investment, intellectual property rights, competition policies, SPS (sanitary and phyto-sanitary issues), TBT (technical barrier to trade), agreements on trade in wine and spirits, business facilitation, trade defence instruments, a dispute settlement mechanism etc. The political impetus given by the ministerial meeting should, under appropriate conditions, enable the groups to achieve the required progress in each area so that negotiations could possibly be concluded by October this year.

The Commission expects that Heads of State and Government will encourage further progress on the work programme on EU-Mercosur negotiations for an Association agreement, as agreed on 12 November 2003 during the last EU-Mercosur Trade Negotiators meeting at Ministerial Level. This should, under appropriate conditions, enable the negotiations be concluded by October this year.

The Caribbean

As in Latin America, the European Union has systematically supported regional integration in the Caribbean. The Caribbean Community and Common Market (CARICOM), established in 1973, decided in 1989 to advance towards a CARICOM Single Market and Economy (CSME). When completed, the CSME will provide for the free movement of goods, services, capital, labour and right of establishment within CARICOM and harmonised laws and regulations affecting commerce. The agreed CSME deadline is 31 December 2005. At the same time, CARICOM is pursuing further integration with the Dominican Republic, and implementation of a Free Trade Area between the two started in 2001.

The EU is building on and reinforcing regional integration in the Caribbean by focussing its regional financial support under the 9th EDF regional indicative programme (2003-2007) on intra and inter regional integration processes including an Economic Partnership Agreement (EPA) with the region. EPA negotiations will be opened in April 2004. EPAs are new WTO-compatible trading arrangements, removing progressively barriers to trade within the region and enhancing cooperation in all areas relevant to trade. The EPA process is vital for consolidating and boosting Caribbean integration, thus laying the basis for enhanced economic relations between the EU on one side, and a stronger, more competitive Caribbean region on the other side."

6. CONCLUSION

The Commission attaches great importance to the success of the Guadalajara Summit, which will be the first in which the enlarged European Union participates. The Commission has

taken initiatives, negotiated agreements, adopted programmes, and organised and co-financed seminars and meetings to ensure this success.

However the success of the summit will largely depend on the ability of the Heads of State and Government to take concrete and far reaching decisions that give new impetus to our relations and map out their future course.

In this Communication, the Commission argues that these decisions should focus above all on social cohesion and regional integration, two issues that are vital both for the development and the stability of our regions and for the strengthening of our relations.

The Commission proposes that the Heads of State and Government take concrete decisions aimed at:

Social cohesion:

- **Encouraging Latin American countries to adopt sound and efficient policies -on democratic governance, social aspects and public finance and fiscal policies- to increase social cohesion by reducing poverty, inequalities and exclusion;**
- **Encouraging the international community, including international financial institutions, to support such social cohesion measures;**
- **Intensifying cooperation between the European Union and Latin America in the field of social cohesion;**
- **Adopting the proposals suggested by the working group on social cohesion set up by the Commission together with the Inter-American Development Bank after the seminar on social cohesion that took place in June 2003 in Brussels, so that they will provide a social cohesion agenda on the basis of clear guidelines.**

Regional integration

- **Reconfirming the positive signal given in principle by the Madrid declaration to Central America and the Andean Community and paving the way towards the opening of negotiations on Association agreements, including FTA's which shall be built upon the outcome of the Doha Development Agenda. The realisation of a sufficient level of regional integration would then become the trigger for launching negotiations.**
- **Encouraging further progress on the work programme on EU-Mercosur negotiations for an Association agreement, as agreed on 12 November 2003 during the last EU-Mercosur Trade Negotiators meeting at Ministerial Level. This should, under appropriate conditions, enable the negotiations be concluded by October this year.**

The Commission hopes that its proposals regarding these two issues will be considered positively by the Heads of State and Government and will be reflected in the conclusions of the Summit.