

# COMMISSION OF THE EUROPEAN COMMUNITIES

COM(82) 257 final

Brussels, 21 June 1982

## SPECIAL ACTION IN FAVOUR OF THE ECONOMIC AND SOCIAL DEVELOPMENT OF CENTRAL AMERICA

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(Communication from the Commission to the Council)

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I. INTRODUCTION

Concerned at the unstable situation in Central America, the Commission forwarded to the Council on 4 December 1981 a communication containing guidelines for increasing Community aid to Central America.

On 29 and 30 March 1982 the European Council expressed serious concern at the ever-increasing tension in Central America, particularly as a result of serious economic problems and social inequalities. It recognized the international community's responsibility for restoring just and democratic peace in the region. In this context the European Council hoped that the Nassau Group initiative would help to attain these ends.

The European Council noted that the Community and its Member States had already provided substantial aid to the region in the past but had also agreed that this aid for Central America and the Caribbean should be coordinated and increased within the limits of available resources.

Increased Community aid to Central America, which is the subject of this communication, is justified by the assessment made by the Member States and the Commission, in the political cooperation framework, of the current situation in the region and its possible repercussions at regional and world level.

This communication proposes practical measures likely to make a contribution, through development aid, to increasing the economic independence and improving the social welfare of the countries in the region. The proposed measures represent a temporary increase in the Community's development efforts in the region and do not anticipate the Community's longer-term policies in the region or in other developing countries.

The Commission feels that the Community should make a greater effort to:

- (i) help solve the problems in the socio-economic structures of these countries, which are the cause of the current instability;
- (ii) ensure that the impact is quick and substantial enough to produce tangible results, not only from the political point of view, but also in terms of economic efficiency.

To this end, the economic and social situation of the region should be discussed before the details and scale of this initiative are worked out.

## II. THE ECONOMIC AND SOCIAL SITUATION OF THE COUNTRIES OF CENTRAL AMERICA

The economic structure of the Caribbean basin is far from sound. It is dominated by the production and export of almost exclusively tropical products, a lack of other raw materials and an almost total lack of oil resources. It is faced with a difficult world economic situation and caught between rising prices for imported products, including energy, and the drop in the prices of the products which it can export.

All the countries are affected by inflation, ranging from 11% to 65%, and increasingly large deficits and foreign debts are being incurred.

All branches of the economy are affected by this appalling state of affairs, and are showing visible signs of flagging. Two sectors, however, namely industry and the predominant sector, agriculture, deserve special attention, since their importance and structure are characteristic features in the social and economic context of Central America.

### A flagging industrial sector

Although the various governments have accorded priority to industry, it is prey to a number of structural and cyclical difficulties, which have a cumulative effect and cannot be solved quickly.

In all the Central American and Caribbean countries, production costs have risen enormously owing to the rise in the cost of imported oil, a rise with which these small countries, suffering from a severe shortage of cash cannot cope. In addition to these high production costs, steep interest rates and the widespread shortage of cash there is in many instances a decline in domestic demand, which is restricting production even further.

Although the countries of Central America had sought to concentrate on import substitution, their industry still depends on imports of raw materials which are, for them, prohibitively costly. Their industry is therefore stagnating, and, except in Costa Rica, is less productive than agriculture - and yet the industrial sector also depends on farming, for although the main industries turn out intermediate products (paper, paper products, chemicals and rubber, oil-refining, minerals other than metals, furniture and timber), the more traditional industrial activities include the food industry, beverages, tobacco, meat and cotton (textiles and clothing). Agriculture itself is plagued by serious difficulties, however.

#### An essentially agricultural economy

The economic structure of these countries is still essentially agricultural and this is the main cause of the present lack of economic and social stability in the region.

The predominantly agricultural export (65% of total exports) - reflected in a highly capital-intensive "plantation economy" using seasonal labour - are fully integrated into the world's economic channels; the marketing of the products (mainly sugar, bananas, coffee, cotton, meat) depends entirely on the international markets and their prices, and determines in turn the financial equilibrium of the countries concerned.

The drop in world prices for exports and in particular the rise in the prices of imports (energy products, but also fertilizers, pesticides, machinery, etc.) have had a direct adverse effect on this sector and on all economic activity, with serious balance of payments deficits as a result.

The structure of agriculture - which provides employment for, on average, over 60% of the labour force - and the distribution of land are very strictly governed by the rigid integration of the sector into the world market.

Most of the peasant farmers either earn mainly seasonal wages harvesting export crops or are engaged in small-scale village production supplying the domestic market with foodstuffs, and this category subsists at a very low level, without equipment or capital or economic incentive. It is the fundamental imbalance in the structure of agriculture which has prompted decisions to introduce agrarian reform, although the decisions have rarely been acted upon, and which is at the root (directly or indirectly) of the social unrest.

As well as the rigid agrarian structure there is an additional problem that is common to the entire region, with the exception of Haiti, namely arable land left uncultivated, on the latifundios and elsewhere.

### III. SPHERES WHERE COMMUNITY ACTION COULD PROVE EFFECTIVE

From the preceding paragraph it is evident that, although the Central American countries' most immediate problems stem from their balance of payments deficits (and the resulting level of debt), their stability is being undermined largely by the structure of the rural sector. Any additional cooperation must therefore be channelled in these two directions, although only a restructuring operation - even a partial one - could have a real impact in helping the countries to overcome the crisis.

#### A Community initiative to help improve the rural structure

Most of the countries, in particular Nicaragua, Costa Rica, Honduras, the Dominican Republic, Guatemala and El Salvador, are currently implementing major agrarian reform programmes. These generally comprise the expropriation of large plantations and/or the settling of virgin land by peasant groupings or cooperatives. These programmes are making slow headway, since they come up against not only inadequate technical know-how on the part of the peasant farmers, a serious shortage of agricultural credit and a lack of rural extension services and basic infrastructure, but also a lack of a framework for public assistance for the farming community.

Although it is unlikely that isolated foreign support would bring about any rapid change in the overall situation, there is no doubt that an operation in this sector, even limited in scope, could act as a catalyst and demonstrate that genuine agrarian reform can result in an improvement in the farmers' living conditions, an increase in production and a lessening of social unrest.

Since the peasant farmers concentrate on food crops, this would be of direct help in improving the food security of the entire Caribbean-Central American region, which has a serious shortfall.

In this sector, while there will be a uniform regional approach, the initiative can be given individual form only on a country by country basis. The specific nature of the aid and optimum implementing procedures will be defined country by country, depending on the progress made in the reform programmes and on the agricultural structures.

Without directly constituting an example of its implementation, this type of initiative falls within the scope of the plan of action to combat hunger in the world adopted by the Council on 3 November 1981 and now being carried out. In view of the particular features of the agricultural sector in the countries concerned, and in particular the crucial importance attaching to effective implementation of the existing agrarian reform programmes, what is involved in this case is support for their implementation.

In specific terms the Community initiative could involve:

- (i) strengthening training facilities and extension services for the peasant farmers, and possibly the national technical services concerned;
- (ii) improving agricultural credit, inputs and basic rural infrastructure;
- (iii) intensifying food production.

Measures aimed at mitigating the effects of insufficient import capacities

While the measures described above may contribute to a long-term solution of the problems of Central America, it is equally necessary to help these countries overcome the immediate conjunctural difficulties arising at the level of import capacities.

It is appropriate therefore that the Community should also foresee the provision of quick-working assistance permitting these countries to purchase those factors of production which are indispensable to the maintenance of agricultural and industrial production.

The goods to be taken into account must be goods originating in the EEC or goods involved in regional trade, in particular goods from the Central American Common Market, given the present and prospective importance of this trade, which is the most seriously hit by the present crisis, and which is not aided by other donors.

Since aid for restructuring the rural sector, as referred to above, necessitates mainly expenditure in local currency, the two forms of aid may be combined by using counterpart funds from import aid, supplemented by direct financial aid for only that expenditure in local currency required for implementing the programmes.

Recipient countries

The countries to be included in the scope of increased aid for Central America are the Isthmus countries and Haiti and the Dominican Republic. The other countries of the Caribbean basin are already receiving relatively large sums from the Community under the Lomé Convention (ACP) or are part of separate economic systems (French departments, Cuba and Puerto Rico). All the countries belonging to the abovementioned region are to be considered eligible. The actual granting of the aid should however be based on the principles and criteria governing the Community's development cooperation policy and the likelihood of effective implementation of the operations.

#### IV. COORDINATION

The special initiative considered in this paper would not take place in a vacuum. The Community and its Member States are already helping these countries in various ways, and international efforts involving other countries as well are in hand to define the content and terms of increased aid in response to the seriousness of the present situation.

##### Integrating different types of aid

The Community has gradually built up a range of budget instruments which can be used for cooperation with non-associated developing countries.

Taking account of the relatively limited amounts available under other instruments, it is mainly financial and technical cooperation and food aid which must be used, in a coordinated manner, to meet the present objective.

Such coordination will be all the more easy given that food aid can not only help meet balance-of-payments needs, but also create (where this is possible) counterpart funds which can be used in structural activities.

As regards the rural-sector aid, this is already in part directed, in Central America, towards structural improvements in the sector of peasant agriculture.

In this way, all the Community resources available in 1982 and 1983 may be mobilised jointly with the additional effort here proposed.

##### Coordination and harmonization of Community aid and Member States' bilateral aid

The Commission already frequently confers with the Member States on the programming and actual administration of aid in the region. Though there has been little in the way of cofinancing with bilateral aid donors, projects which have been identified are increasingly discussed beforehand with the main bilateral donors involved in the country or sector concerned.

A more systematic form of coordination will undoubtedly be needed for the implementation of the special initiative.

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Once the initiative has been approved the Commission will set to work to identify the types of action best suited to each country. It will discuss its findings with the Member States and their development officials so that the Community projects can be dovetailed as closely as possible with existing or planned bilateral ones.

#### Coordination with other aid donors

It is important to coordinate activities with existing or planned aid to the region to avoid overlap and increase overall effectiveness.

The Commission is already in regular touch with the other major aid donors and will be taking part in the work of the Central America Consultative Group, as it already does with the Consultative Group for the Caribbean. Obviously bilateral contact with other aid donors should be stepped up, once the outcome of internal Community coordination is known. It will also be a good idea to coordinate at Community level the position to be adopted within the various aid donors' groups.

#### V. PROVIDING THE ADDITIONAL FUNDS

##### Amount

Total direct aid from the Community and its Member States for the Central American region represents approximately 30% of the total public aid received by this region.

In exploring the scope for an increase in the financial contribution the Commission cannot afford to underestimate the severe constraints on the Community budget, which of course are to a considerable extent due to the same international recession that is so exacerbating the ominously unstable situation in Central America.

Given the US and Canadian plans for large-scale financial assistance as from this year, and of course the oil agreements with Venezuela and Mexico, the proportion of aid from the Community will be reduced, however, if it remains at the present level, and will thus fail to convey the desired degree of European solidarity in the international Central American rescue operation.

In establishing the amount of the special effort proposed here (on a "one-time" basis), one must take account both of current annual aid levels (Community plus Member States, approximately 150 M ECU per year), and of the amounts which would be necessary to carry out any significant actions.

In the light of the objectives suggested in paragraph III, we can estimate the cost of each of the rural restructuring pilot programmes by analogy with other similar operations at about 20 M ECU.

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Taking account of the contributions expected under existing budget allocations, and of the likely benefits of an intensified coordination of Member State bilateral aid, the additional financing required will be of the order of 10 M ECU per country. Accordingly, the Commission proposes to set the supplementary allocation at the level of 65 M ECU.

#### Source

Since Central America's share of Title 9 appropriations cannot be increased without cutting provision for other countries, additional resources must be made available. Given the aims and type of operations envisaged, it would be best to concentrate the extra money on financial and technical cooperation (Article 930), since the basic regulation allows for such use, providing ad hoc guidelines are drawn up in accordance with the specified procedure for the allocation and implementation of the aid.

The Commission will therefore be presenting a proposal to the budget authority for a 65 m ECU increase in Article 930 in the next amending budget. Even at the lowest, such a sum should be enough since it is topping up other contributions from the Community itself or the Member States. Naturally, it would be a good thing if the Member States could step up their own bilateral aid too, over and above the coordination measures mentioned in paragraph IV.

#### Implementation

The Commission intends to define for each country the ways in which the aid can be used most effectively and the conditions of implementation on the basis of a brief but thorough survey of that country's economic and social circumstances, and more specifically of agrarian reform programmes. Regard will be had to the preferences and priorities of the different governments and the need to remain consistent with the broader policy framework which can affect the results.

The level of balance of payments support will be geared to the local currency component of each programme estimate and particular attention will be paid to means of securing the availability of counterpart funds in line with the requirements of the main programme.

Once the Article 930 Committee has returned an opinion in accordance with the specific guidelines laid down by the Council on the basis of these Commission proposals, the Commission will approve the final programmes.

The plan is for all resources to be committed this year, and subsequently disbursed as required, with payments heavily concentrated in the early part of 1983.