



EUROPEAN COMMISSION
EXTERNAL RELATIONS DIRECTORATE-GENERAL
Latin America Directorate
Mercosur and Chile Unit

**EASTERN REPUBLIC OF URUGUAY –
EUROPEAN COMMUNITY**

**COUNTRY STRATEGY PAPER 2001-2006
AND NATIONAL INDICATIVE PROGRAMME 2002-2006**

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EXECUTIVE SUMMARY

Uruguay is a middle-income country, where traditional development co-operation assistance plays a relatively limited role. Official development assistance amounted to only US\$ 30.7 million in 1999. The EU is the largest donor by far in Uruguay with a total share of over 63% of all aid (US\$ 143.7 million) during the period 1995-1999. It should be noted that Uruguay also benefits from significant amounts of multilateral assistance in the form of loans, primarily by the IDB, and the WB.

Uruguay finds itself currently in a serious economic recession, which is partly linked to the regional Mercosur context on which the Uruguayan economy is very dependent. Recent events, such as the recessions in the USA and the EU, or the economic and financial collapse of Argentina, have not helped the plight of the Uruguayan economy. The country has suffered negative economic growth since 1999, with the situation in 2001 resulting in -2% growth and 15.5% open unemployment. In the short term unemployment, growing poverty and social marginalisation are threatening the achievements of Uruguay as a middle-income country. In the longer term the Uruguayan government is confronted with a number of serious economic and social challenges, which depend for their solutions on internal structural reforms and on a more favourable external environment. Only then can the economic and social sustainable development of Uruguay be ensured in the future. The agenda of the present government in Uruguay focuses on four main priorities which seeks to address the challenges faced by the country: 1) Implementation of structural reforms in order to increase competitiveness, stimulate private sector development, attract investment and boost exports based on comparative advantage; 2) Modernisation and reform of the State; 3) Development of the social sectors including especially human resource development; 4) Institutional, economic, physical and social integration within Mercosur.

Taking into account the relatively high level of economic and social development in Uruguay, the size of EC economic and financial-technical assistance provided to the country is relatively limited. Given the present needs of Uruguay, which are not those of typical developing country, it is proposed that EC assistance focuses on the following priority sectors in order to help the country in its efforts to address structural problems and to create the conditions for sustained development: 1) Economic reform; 2) Modernizing the State; 3) Social development. At the same time, this assistance should be seen within the framework of the EU's overall policy aimed at strengthening the political, co-operation and trade relations with Uruguay through the negotiation of an EU-Mercosur Inter-regional Association Agreement. The response strategy that follows in this paper should be read in the light of these on-going negotiations, which are expected to be concluded well before the end of 2006 when a new country strategy paper will have to be prepared.

URUGUAY AT A GLANCE

POLITICAL :

Official Name : Eastern Republic of Uruguay

Population: 3.4 million

Urban population: 93% (2000)

Area: 176,215 sq km

Main cities: Montevideo

President of the Republic: Jorge Batlle

Minister of Foreign Affairs: Didier Operti

Next elections (Presidential, parliamentary): October 2004

ECONOMIC :

GDP: US\$ 20.8 billion, GDP at PPP US\$ 31 billion (2000)
GDP per capita: US\$ 6,180, GDP per capita at PPP: US\$ 9,480
Annual growth: -2% (estimate 2001), -1.5% (2000), -3.2% (1999), 4.6% (1998)
Unemployment : 15.5% (Nov. 2001), 14.5% (2000), 11.3% (1999)
Inflation : 3.5% (2001), 5% (2000)
Currency : US\$ 13 = US\$ 1 (July 2001), US\$ 17 = US\$ 1 (Jan. 2002)
FDI Flows : US\$ 180 million (2000)
Total stock FDI : US\$ 5.6 billion (1999)

TRADE :

Exports of goods & services form roughly 20% of total GDP.
Total Exports: US\$ 2.3 billion (2000)
Total Imports: US\$ 3.2 billion (2000)
Exports 2001 : exports to Mercosur -9.5%, exports to world -15.7% (IDB estimate 2001)
Exports to EU : 421 million Euro (2000)
Imports from EU : 859 million Euro (2000)
Main exports to EU: meat, rice, wool, dairy products, and leather.
Main imports from EU: machinery, appliances and electrical equipment (19.3%), mineral products including petroleum (15.8%), chemical and related products (13.3%), and transport equipment (8.3%).

1. EUROPEAN COMMUNITY CO-OPERATION OBJECTIVES

General Objectives

According to article 177 of the EC Treaty, Community policy in the sphere of development co-operation, shall foster:

- The sustainable economic and social development of the developing countries, and more particularly the most disadvantaged among them;
- The smooth and gradual integration of the developing countries into the world economy;
- The campaign against poverty in the developing countries.

In addition, in their “Declaration on the Development Policy of the European Community” of 10 November 2000 ⁽¹⁾, the Council of the European Union and the European Commission decided to concentrate the activities of the Community in a limited number of areas, six in total, chosen in function of their contribution to the fight against poverty, and in which the activities of the Community may offer an added value. These areas are: 1) trade & development; 2) regional integration & co-operation; 3) macro-economic policies & equitable access to social services; 4) transport; 5) food security & sustainable rural development; 6) institutional capacity building ⁽²⁾.

At the WTO ministerial Conference launching the Doha Development Agenda, it was agreed to provide trade related technical assistance to the developing country Members of the WTO as a central component of the negotiations under that agenda. Following the launching of the Doha Development Agenda, the Commission has noted that “at the level of the EU, we must now ensure that trade related technical assistance and capacity building is well integrated into the EU’s current and future technical assistance/development co-operation programming.

¹ Council doc. 12929/00 (Presse 421).

² Following the WTO ministerial conference in Doha during Nov. 2001, the areas of trade & development and institutional capacity building have taken on a renewed priority, noted by the European Commission in SEC(2001)1903 of 20 Nov. 2001.

Objectives concerning Latin America

With regard to the countries of Latin America said objectives have been confirmed and reinforced through various general and specific documents⁽³⁾, in which in particular the human dimension of development has been underlined and where the European Community has stressed the great importance it attaches to:

- human rights;
- processes of democratisation;
- good management of public resources;
- protection of the environment;
- trade liberalisation;
- and a strengthening of the cultural dimension.

In addition to this, for the countries of Latin America, an important guideline was the first Summit meeting of June 1999 between the Heads of State and Government of the Latin American and Caribbean region and of the European Union, which focused on the strengthening of the strategic bi-regional partnership in its political, economic, social, environmental, educational, cultural, technical and scientific dimensions. The declaration issued by the Heads of State and Government and the follow-up given to the summit conclusions since then are also to be taken into account when focusing on the EC's particular objectives as regards co-operation with Uruguay. Following this, the results of the second Summit meeting of May 2002 in Madrid will also be taken into account.

Objectives concerning Mercosur

At the sub-regional level, the EU and Mercosur, of which Uruguay is a member, signed an Interregional Framework Co-operation Agreement in December 1995, which fully entered into force in July 1999 (provisional application already 1996). This Framework Agreement consists of three main elements: political dialogue, co-operation and trade issues. This agreement is expected to be replaced by a more comprehensive bi-regional association agreement in the future, for which negotiations have been on-going since November 1999. In parallel to the current Country Strategy Paper for Uruguay, a Regional Strategy Paper on Mercosur co-operation until 2006 has also been prepared.

Objectives concerning Uruguay

At the bilateral level, the main objectives of EC co-operation are set out in the Framework Agreement for co-operation between the European Economic Community and the Eastern Republic of Uruguay of 16 March 1992. This agreement provides for the development of various lines of co-operation, particularly economic affairs, industry, the environment, science and technology, the administration and regional integration. A previous Country Strategy Paper on Uruguay in 1998 identified the key areas for EC intervention until 2000. In March 2001 the authorities of Uruguay and the European Commission signed a Memorandum of Understanding (MoU) which spells out the priority sectors for the bilateral co-operation between Uruguay and the European Community for the period 2000-2006.

³ See COM (95) 495 final "The EU and Latin America. The present situation and prospects for closer partnership 1996-2000", COM (1999) 105 final "A new EU-Latin America partnership on the eve of the 21st century", COM (2000) 670 "Following up to the Rio Summit of 1999", and Regulation (EC) 443/92 concerning financial and technical aid and economic co-operation with the developing countries of Latin America and Asia.

2. URUGUAY'S POLICY AGENDA

The current government's policy agenda, as described in President Batlle's inaugural speech addressed to the Uruguayan Parliament on 1 March 2000, identifies a list of government priorities. In broad terms, the current government's policy focuses on four main priority areas:

- Implementation of structural reforms in order to increase competitiveness, stimulate private sector development, attract investment and boost exports based on comparative advantage.
- Modernisation and reform of the State.
- Development of the social sectors including especially human resource development.
- Institutional, economic, physical and social integration within Mercosur.

Uruguay's longer-term development strategy follows a similar line and is mainly focused on:

- The opening of the country to the world, both in a regional context of Mercosur integration as well as in an international context in order to improve market access.
- The development of a competitive agricultural export model, given the limited size of the internal consumer market.
- The reallocation of investments to make the country more competitive so as to attract private investments in: the national road network, ports and airports, telecommunications.
- Social investments in: housing, education, health, investment in knowledge.
- Decentralisation: to promote local development by encouraging municipalities to coordinate investments with national investments through appropriate mechanisms.

Looking at President Batlle's policy agenda, the four main priority areas can be explained in more detail.

Firstly, in order to modernise the economy and improve competitiveness, the government seeks to create an attractive investment climate by improving the legal framework as well as pursuing key structural reforms. Apart from privatisations in selected sectors of the economy, this includes implementation of social security reforms, tax reforms and financial sector reforms. Furthermore, the government aims at stimulating exports, and in particular to diversify its export base and penetrate new world markets for the country's key products, in particular in agriculture. The government is also committed to make Uruguay a regional centre for business and investment by improving the country's infrastructure and ensure closer regional integration. Finally, the government seeks to further develop the services sector, which accounts for the major share of the economy, especially in the areas of finance, business and tourism.

Secondly, as far as the reform and modernisation of the State is concerned, the government will continue with the process initiated by previous governments. This process will involve three key elements:

- Review the public spending in order to identify where expenditure cuts can be made or reallocated in order to ensure sound public finances.

- Reducing the role of the State in the economy through deregulation of particular sectors in order to open up to competition and private participation.
- Creating an efficient and modern public sector by ensuring better governance and transparency as well as improving the quality of public services.

These reforms are to be complemented by cutting red-tape and instituting key laws aimed at promoting competition and investment.

Thirdly, in the social sectors, the government is committed to make adequate investments in education and health and institute necessary reforms in order to improve efficiency in these sectors. In particular, it is committed to effectively reach out to marginal sections of society in order to ensure improved access to basic services. The government has expressed its desire to attack problems of poverty and social exclusion, especially in the marginal urban settlements and rural areas, and the co-ordination of this policy has been assigned to the Budget and Planning Office (OPP). Special emphasis has been put on human resource development, especially retraining of labour, developing higher education, and improving IT skills throughout the country in order to make Uruguay into a centre of excellence and develop the country's scientific and technological base.

The fourth priority of the Government consists of consolidating and broadening regional co-operation in the context of Mercosur. This aims at:

- Ensuring effective free circulation of goods in Mercosur by removing existing non-tariff barriers so as to obtain concrete "enlargement" of its present small internal market.
- Deepening the institutionalisation of Mercosur by creating a Permanent Secretariat and common courts to ensure an effective dispute settlement mechanism.
- Promoting Uruguay as the regional centre of Mercosur.
- Advancing trade negotiations and ensuring that Mercosur acts as a block in this process with its partners as well as in international fora.
- Promoting macroeconomic co-ordination between Mercosur countries so as to ensure regional convergence and stability.

President Batlle was elected in October 1999 and came into office in March 2004. The next presidential and parliamentary elections are scheduled for October 2004.

3. ANALYSIS OF THE CURRENT SITUATION

3.1. Political situation

Uruguay is a constitutional democracy with an elected president and parliament. The constitution from 1967 provides for a strong central executive branch, subject to legislative and judicial checks. The executive branch comprises a president, a vice-president and a cabinet of twelve ministers. The president and vice-president are chosen by direct popular vote (consecutive re-election is not permitted). The ministers are appointed by the president. National elections are held every five years with the next general elections scheduled for October 2004. Voting is compulsory. The country is divided into nineteen departments including Montevideo, the capital with limited local government. The election of department governors takes place in May the year following a national election year. All elected offices are for a five-year term.

The Legislative branch consists of a bicameral General Assembly. The two chambers are the Senate and the Chamber of Representatives. The Senate is made up of 30 senators selected by popular vote for a five-year term. The Chamber of Representatives is made up of 99 deputies, also chosen by direct popular vote for a five-year term. The Judiciary, one of the most independent in Latin America, is headed by a five-member Supreme Court. Judges are nominated by the executive branch and elected for ten-year terms by the General Assembly. Additionally, there are electoral and administrative courts, an accounts court, and a military judicial system.

There are three major political forces in Uruguay: the Colorado Party, the Blanco Party, the Frente Amplio–Encuentro Progresista. Uruguay's two traditional political groupings are the Colorado Party and the Blanco Party. Although both espouse similar ideals, the former's core electorate is urban while the latter is rural-based. Although internal factions exist within the parties, both parties broadly favour economic reform and free enterprise as well as further efforts at international and regional integration. The Encuentro Progresista-Frente Amplio, a leftist coalition of various parties and movements, was founded in 1971 and brings together nine different leftist parties including Christian Democrats and Communists. It supports a strong role by the State in the management of the economy and it advocates a redistribution of wealth through major tax reforms. The party has a substantial following in the main urban centres and among younger voters seeking to break away from the traditional parties.

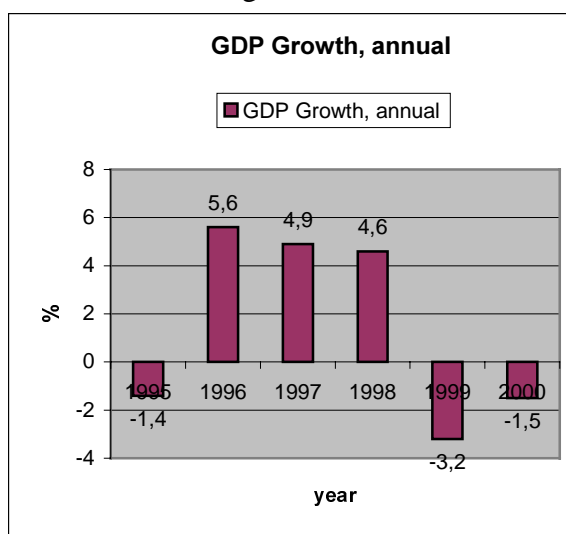
Except for the period of military rule between 1973-1984, Uruguay's human rights record has been free from violations against its citizens. The law and judiciary generally provide effective means of dealing with individual instances of abuse. In a regional context, the country enjoys the reputation of being one of the most open society's with respect to political and social freedoms. However, there are still problems in some areas, principally: instances of police abuse and mistreatment of detainees and poor prison conditions; delays in the justice system; domestic violence exercised against women; marginalisation of the black minority. In August 2000, President Batlle created a Peace Commission to clarify the fate of about 160 persons who are believed to have disappeared for political reasons during the 1973-84 military dictatorship. Uruguay has strong laws to prevent bribery and other corrupt practices and the government has taken the initiative to further strengthen these laws. As far as labour market relations are concerned, Uruguay has ratified a large number of ILO conventions protecting worker rights and generally adheres to their provisions. The Uruguayan constitution guarantees workers the right to organise and strike, and union leaders are protected by law against dismissal for union activities. Labour unions are independent of government.

3.2. Economic and trade situation

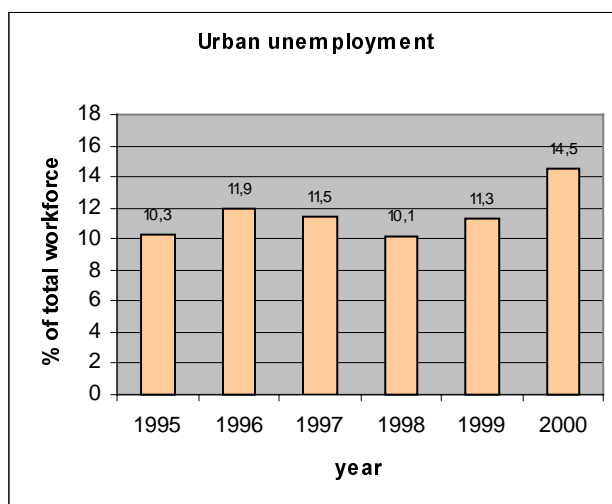
The Economy

Uruguay enjoys a relatively high level of economic and social development placing it among a group of upper middle-income countries. Its GDP ranks among the third highest in the Latin American region, after Chile and Argentina. In terms of income distribution, Uruguay enjoys one of the most equitable distributions in Latin America. Uruguay is a small and open economy with a limited natural resource base. Its principal natural assets are its agricultural land which is abundant and fertile, and the coast line which attracts tourism. As a result of the small domestic market, the country is relatively dependent on trade in goods and services and hence on developments on its key exports markets.

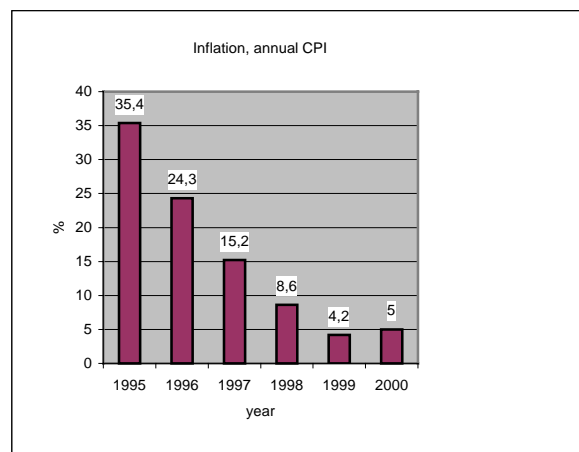
During most of the 1990s, the economy of Uruguay grew steadily recording an average GDP growth rate of 3.5% to be compared with a population growth of 0.5%. This growth was mainly achieved thanks to prudent macroeconomic policies, some structural reforms and a rebound in regional activity, most notably thanks to growing intra-regional trade in the context of Mercosur. In 1999 the economy entered into a period of deep recession when real GDP growth fell as a result of a number of adverse shocks, including the devaluation of the Brazilian real, the beginning of a deep recession in Argentina, as well as terms of trade losses due to weakening international commodity prices. This weak performance continued throughout 2000, mainly as a result of the economic developments in its two neighbouring countries, Brazil and Argentina, a severe drought and the sharp rise in international oil prices. Furthermore, an outbreak of the foot and mouth disease in the late 2000 had a serious impact on the important beef sector. Growth during 2001 was estimated to have been -2%.



In parallel to this deteriorating situation, unemployment has been rising steadily. During the last decade, efforts to curb hyperinflation in Uruguay have been extremely successful mainly thanks to the commitment by successive governments to ensure price stability as a fundamental pillar of the macroeconomic framework. The Uruguayan economy is highly dollarised with almost 90% of deposits denominated in foreign currency, of which one third are held by non-residents.



Within the framework of the current economic downturn the government reached an agreement on a 22-month Stand-By Arrangement with the IMF in April 2000 (letter of intent), providing a framework for improving the immediate fiscal problem and guiding a gradual path out of the present recession. Under the auspices of this programme, the government committed itself to cutting the fiscal deficit in half to about 1.8% of GDP. On the expenditure side, the adjustment plan takes a balanced approach. Nominal public sector wages will grow by only 1.5%, in the context of inflation in the 4-6% range, and a broad range of other primary expenditures will suffer moderate adjustments. In addition the government has agreed to certain structural reform benchmarks. Given the difficult economic situation of Uruguay's regional partners, Argentina and Brazil, the Government has not been able to achieve its short term macroeconomic targets under its economic programme for 2000–2001 in the context of the IMF programme, mainly a recovery in GDP growth and a reduction of the fiscal deficit to a sustainable level. Moreover, a global slowdown in the world economy is contributing to a reduction of economic activity. In this economic context, the government may have to lower its growth targets for the next years and hence reassess projections of various indicators, in particular the fiscal.



Foreign Direct Investment in Uruguay is relatively small, at less than 1% of GDP, and is mainly directed towards forestry, specialised manufacturing and services (tourism, restaurants, and shopping malls). In 2000, it amounted to some US \$180 million. During the period 1995-1999 the USA was the largest single investor in Uruguay (with 32 % of overall FDI), followed by MERCOSUR (28%) and the EU as the third most important source (26%). FDI in the non-financial sector amounted to US\$ 2.4 billion in the 1995-1999 period. The overall stock of FDI amounted to US\$ 5.6 billion as of 1999.

Uruguay enjoys good relations with its external creditors, and is one of few countries in the Latin American region to have received an investment grade rating on its sovereign debt from international credit rating agencies (besides Chile and Mexico) and the only one in Mercosur. Thanks to its reputation of a financial safe heaven and given its stable political institutions, Uruguay is a net receiver of capital inflows, especially in times of uncertainty in the region. Uruguay has maintained a long-lasting tradition of imposing no restrictions on the purchase of foreign currency, or remittance of profits abroad. As a result, the country has traditionally enjoyed a comfortable foreign reserves position.

In Uruguay, key economic sectors, in particular public utilities, are dominated by State run enterprises (SREs). The main SREs are: the electricity company (UTE), the alcohol, cement and petroleum company (ANCAP), the telecommunications company (ANTEL), the water and sanitation company (OSE), the railways (AFE), and the port authority (ANP). The State run enterprises generate about 18% of the gross domestic product. By and large, performance of these enterprises has not been weak. The SREs remit their surpluses to the central government in the form of taxes and transfers, and during 1995-99, these contributions averaged 4.2% of GDP. However, the financial performance may mask inefficiencies, obscured by the lack of competition and relatively high tariff levels. In addition, such hidden inefficiencies as a result of lack of competition may also contribute to reducing overall competitiveness of the economy, especially vis-à-vis its neighbouring countries, Argentina and Brazil. Uruguay may risk to fall behind its regional partners in the reform process of key sectors, hereby losing out on its objective to turn Uruguay into a regional center.

The agricultural sector has constituted the backbone of the Uruguayan economy and in particular the livestock sector has played a major role in economic development. The agricultural sector today, continues to play a key role through its contribution to output, exports and employment since it: accounts for 10% of the country's GDP, comprises more than 50% of exports (especially meat, wool, hides and skins, and rice) and directly employs around 13%. Agricultural sector contribution to output, exports and employment is far more important than suggested by sheer numbers thanks to its indirect and strong linkages to other sectors of the economy, such as the agro-industry. Trade liberalisation in Uruguay has stimulated specialisation in agricultural sectors where the country has a substantial potential. Resources have been shifted towards cereals that Uruguay produces efficiently, including rice, sunflower seeds, and barley, and the production of meat and dairy products. The beef sector has grown fast and displayed a good potential in exports. Given the favourable climate and fertile soil enjoyed by Uruguay, combined with the fact that a large part of its land is not cultivated, the country has strong comparative advantages, and a growth potential in the agricultural sector. The present government has recognised the importance and growth potential of the agricultural sector, and has committed itself to further support the development of this sector.

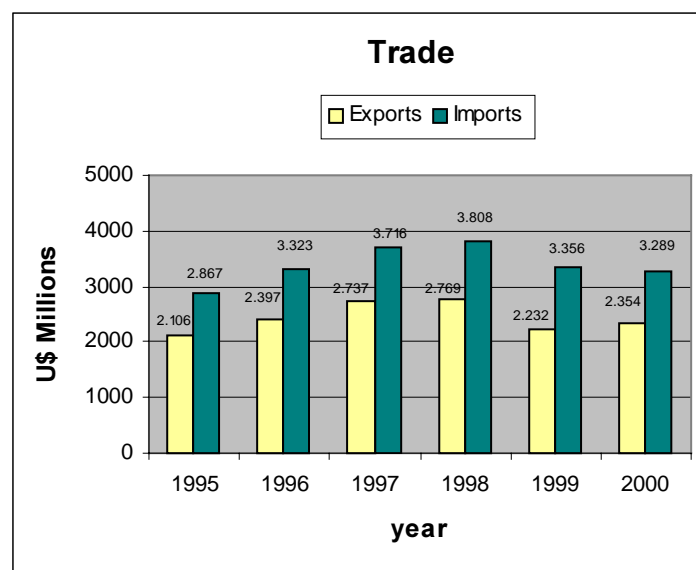
For the immediate future the economic policy agenda of the current coalition government of President Batlle is based on a two-pronged approach. Firstly, in the short term to ensure a stabilisation and recovery of the economy in order to achieve growth and reduce unemployment. Second, a development plan for the medium-term as set out in the five year budget for 2000-2004. In the short-term, the budget aims to control the fiscal situation by reviewing public spending in order to make necessary adjustments on the expenditure side while limiting the use of tax increases at a time of recession. In the medium term the budget aims to reduce the public sector borrowing requirement in order to control and decrease the public debt-GDP ratio, stimulate an increase in savings and investments, and to encourage a reduction in wage costs in order to promote employment generation and improve competitiveness. On the structural side, the government plans to move ahead with deregulation and the opening of state monopolies to private capital and competition. The 2000-2004 budget seeks to enhance the competitiveness of national production in the framework of stable fiscal and price policies in order to restore sustainable growth and be able to meet the challenges of globalisation and integration.

In the area of structural reforms, some tangible progress has arguably been made, such as the reform of the social security system and steps to restructure the public sector and open it up

to private participation in certain sectors such as telecommunications, operation of ports, air services, roads and energy. However, the remaining reform agenda remains wide and important in view of the government's proclaimed goal of transforming Uruguay into a modern and dynamic economy which can effectively compete on world markets and attract foreign investment, and in particular turn Uruguay into a regional centre in Mercosur. Notwithstanding the fact that the external economic climate remains unfavourable for Uruguay, the country must accelerate the pace of needed reforms so as to improve competitiveness and not lag behind its regional and international partners.

Trade

For a small and open economy like Uruguay's, trade plays a relatively important role, with exports of goods and services accounting for roughly 20% of GDP. Since the early 1990s, the country has embarked on a path of steady trade liberalisation in good and services as well as deeper regional integration. Although this trend may have been somewhat reversed in the wake of the economic crisis which has affected the region since early 1999 and as a result of unilateral changes announced in the context of the Mercosur tariff regime, Uruguay's trade regime remains liberal with some few exceptions. The Mercosur integration process is of great immediate importance for Uruguay's trade relations (approx. 45% of all imports/exports), while the EU-Mercosur association negotiations and the WTO Doha round are also of great relevance for a small and open economy like Uruguay.



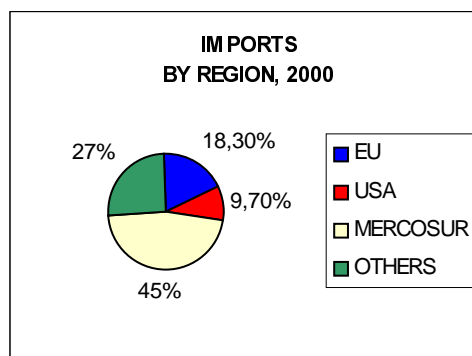
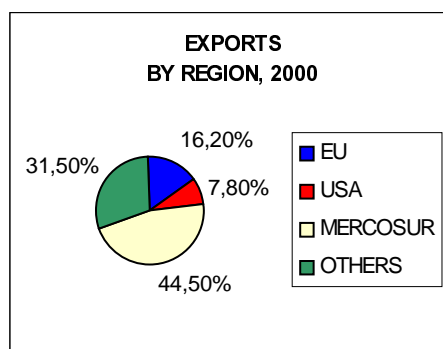
In the past few years export earnings on two of Uruguay's principal markets, Brazil and Europe, have been depressed due to unfavourable exchange rate developments. In 2000, the trade deficit was around US\$ 935 million, with exports remaining fairly stable at US\$ 2.3 billion while imports increased to US\$ 3.2 billion due to a higher oil import bill. In particular, agricultural exports in 2000 were hit by the severe drought experienced by the country as well as the outbreak of the foot and mouth disease in late 2000 with a direct impact on meat exports which account for around 21% of total merchandise exports. However, net income from services and transfers mainly tourist receipts was positive, at around US\$359 million, resulting in a manageable current account deficit of US\$ 576 million, or -2.9% of GDP. Uruguay's exports are highly concentrated in a few products,

especially agricultural related products. Meat, rice, wool, dairy products, and leather, account for roughly half of overall exports.

Exports to EU: 421 million Euro (2000) = 16.2% total exports
Imports from EU: 859 Million Euro (2000) = 18.3% total imports
Trade balance with EU: -438 million Euro (2000)

Exports to EU (2000) by product:		Imports from EU (2000) by product:	
Agricultural products	339 million Euro	Agricultural products	87 million Euro
Energy	0 Euro	Energy	1 million Euro
Machinery	6 million Euro	Machinery	227 million Euro
Transport material	0 Euro	Transport material	99 million Euro
Chemical products	8 million Euro	Chemical products	197 million Euro
Textiles and clothing	20 million Euro	Textiles and clothing	30 million Euro

On the import side, Uruguay's trade is concentrated on machinery, appliances and electrical equipment (19.3%), mineral products including petroleum (15.8%), chemical and related products (13.3%), and transport equipment (8.3%). The main destination for its exports have been in 2000: Mercosur (44.5%), the EU (16.2%), the USA (7.8%). Lately, the government has sought to diversify its exports and new markets such as the Middle East and Asia are being penetrated.



Uruguay's exports to the EU are highly concentrated in agricultural and agro-industrial products, which together account for nearly 92% of the total, and include: foodstuff products (46%), textiles, wearing apparel and leather products (29%), forestry and logging (8%), agriculture and hunting (8%), and wood manufacture (1%). Notably, meat exports accounted for a third of total exports in 2000. Imports from the EU mainly consist of industrial products such as capital inputs and machinery and transport equipment. As an active member of the Cairns group and given the importance of the agricultural sector in its economy, Uruguay strongly supports the intensification of efforts to fully liberalise agricultural trade.

As indicated in the previous chapter, the agricultural sector and especially the livestock sector play a very important role in Uruguay's economy and trade relations, based on the country's comparative advantages in this area. This may appear to be a strong competitive edge for the country, however, it also exposes Uruguay to an important degree of risk and potential instability by creating a strong dependence on one sector/subsection for its GDP and exports. The risks and dangers of monoculture come to mind and, as such, a greater diversification of the economy's sectors would be more advisable. This appraisal is reinforced, in particular, by the recent dramatic experiences in Uruguay that showed what the combined effect can be of weakened international commodity prices, a serious veterinary crisis (FMD), negative economic developments in neighbouring countries (Argentina) and depressed export markets (Brazil and EU). By depending on external trade for 20% of its

GDP, on the agricultural dominance in 50% of its exports (which is 10% of GDP), and on the particular agricultural focus in specific export markets (exports to EU nearly 92% agricultural products), Uruguay itself has aggravated the current crisis that it is facing. Diversification of production and exports, and a strengthening of the competitiveness and the productivity of companies, products and services, should help Uruguay to overcome the risk-prone dependence it has on one sector of the economy.

3.3. Social situation and the environment

Social situation

Uruguay enjoys one of the highest economic and social standards in Latin America, and some of its key social indicators matches well those in the industrialised world. Uruguay has the most equitable income distribution in the whole Latin American region. This achievement is attributable to a variety of factors, including relatively high and broad-based educational achievements, a generous social security system which protects the elderly, and a number of social programs targeted to the poor. The literacy level is almost universal at 97.6% and life expectancy of 74 years matches industrialised countries, while infant mortality rates of 16 per thousand are among the lowest in the region. According to the Human Development Index, established by the UNDP, in 2000 Uruguay ranked at no. 39, the third highest ranking in the Latin American region, only preceded by Argentina and Chile.

Educational levels are high in Uruguay, by regional standards. Urban data show that, overall, the proportion of school attendance between ages 6-15 is 93%. As could be expected, education levels among poor heads of household are lower than the non-poor. Education has been given priority by the new administration, with a particular emphasis on improving computer literacy among the population.

Access to health care is high in Uruguay, with 95% of the total population covered in some way, and two-thirds of the population with health care insurance. For the poor, about 8% of individuals have no health coverage. In general, while there are problems of inefficiency in the health care system, spending is, on the whole, relatively well-targeted to those in the middle and lower income groups.** Health expenditures have been on the rise, due to factors affecting the demand for health care such as demographic changes resulting from an ageing population, changing lifestyles associated with urbanisation, rising living standards, and increased demand for highly complex procedures. There is a public and a private health system in Uruguay. The public system receives insufficient resources from the State and its capacity is overloaded (the number of patients increased by 43% in 2000 compared to 1999, from 105.787 to 151.531), affecting the efficiency and the quality of the service. Nevertheless, the quality of the treatment provided is good; there is no problem of availability of medicines and vaccines and some public establishments are equipped with high technology materials. Despite the current subsidies, medicines remain relatively expensive for the population, except medicines for HIV+ patients which are free (their cost is approximately USD 900 per month). As a consequence of the economic crisis which affects the country since 1998, the number of affiliates to the private system is decreasing, especially in less than 15 years old population (-3% in 2000 compared to 1999).

Social protection is provided to the population through an extensive pension system, an unemployment insurance scheme, and a number of social welfare programs targeted to the poor. Examples of the latter are feeding programs, family assistance, cash transfers, youth training, and a social-fund type project. Uruguay has by far the highest expenditure levels as far as social security and welfare are concerned, at 20.5% on average during the period 1993-

98, compared to an average of 7.4% for the Latin American and Caribbean region, and 7.9% for middle-income countries. During the 1990s, one of the most important structural reforms undertaken regards the social security system in an attempt to deal with growing financing deficits due to the generous system. To this end, the authorities have established a complementary private capitalised pension system alongside the public pay-as-you-go system. As this has led to a shift of some contributions from the public to the private, the reforms have implied a transitional cost which requires additional government resource transfers to cover the deficit. Over the medium term, however, the introduction of private pension plans to the public system and other reforms is expected to eventually reduce social security expenditure.

In terms of equality between females and men, Uruguay belongs to the most progressive states in Latin America. Females have equal access to education and health, and their basic rights are on equal footing with those of men. However, women may face certain types of discrimination such as on the labour markets. Women, who make up almost one-half the work force, tend to be concentrated in lower paying jobs and their salaries average two-thirds those of men. Unemployment among females tends to be higher than among men.

Despite a high income level and relatively equitable distribution of income, pockets of poverty continue to exist in Uruguay. According to the World Bank's Poverty Assessment, carried out in 2000, the rate of poor was 22% in urban areas while in the urban interior the rates were 1 to 4 percentage points higher. An improvement took place in the early 1990s, up to 1995, after which a rise in poverty had been recorded, and it is plausible to believe that especially since the country entered into a deep recession in 1999 there may have been a further deterioration as unemployment has risen. According to the WB study, the profile of the poor in Uruguay is quite similar to other countries in the region: Poverty is heavily concentrated among the young. Poverty is also high among female headed households with children. The high percentage of young people among the poor is particularly worrying. In addition, with 40% of Uruguay's children now born into poor families, there are significant implications for future social and economic programs resulting from a shift in the structure of the population needing attention. Without significant investments in education for this group, there will be a progressive deterioration in the human capital of the population and overall increase in poverty levels given its intergenerational nature.

A major problem that the government is faced with currently, and which has been growing in the past years, is the high rate of unemployment. In August 2001, unemployment had peaked to 16%. In a regional context, Uruguay has, together with Argentina, one of the highest urban unemployment rates. Particularly worrying, is the high rate of unemployment among young people, according to some estimates, reaching as high as 25%. Although the present recession has played a large part in explaining the rising unemployment, structural factors are also likely to have contributed to such a high underlying unemployment as a result of public sector restructuring in the economy and opening up to foreign competition.

In Uruguay, social exclusion is relatively new as generous welfare policies over the past decades have ensured that most Uruguayans receive access to basic health, education and other services. However, as unemployment, poverty and social exclusion tend to go hand in hand, recent developments point to a rise in the risks of certain groups in society being marginalised and socially excluded. In some cases, excluded groups may include those who have migrated from rural and smaller urban centres to search for new opportunities. In other cases, it may simply involve people who have become unemployed and may not have the

skills adapted to a changing labour market. Data on the rural population are scarce but the general hypothesis is that Uruguay's rural population, albeit very small in total (less than 10%), tends to be even more excluded from higher wage occupations and income generation opportunities than their urban counterparts. Finally, it is also noteworthy that Uruguay's minority black population - about 5% of the total population is concentrated in the major urban areas, and tends to be overly represented among the poor.

Also closely linked to unemployment is the issue of migration. As a migrant society, Uruguay has a long experience in in-migration as well as out-migration. Internal migration is driven by the search for better opportunities in larger cities, mainly Montevideo. Migration puts pressure on urban development such as housing needs and the provision of basic services such as water and sanitation which may not expand rapidly enough to meet growing demand. This leads to unsatisfactory solutions, with migrants settling into marginal settlements or shanty towns. These settlements often develop their own life, being excluded from formal networks and the provision of basic services. Ensuring universal and adequate access to education and health becomes more difficult.

However, at a different level, unemployment and lack of economic opportunity, especially among the young, induces people to search for better opportunities abroad. Polls confirm that Uruguayans, especially in the younger age brackets, are willing to leave the country if given the right opportunity. It is estimated that some 500,000 Uruguayans live abroad, representing around 13% of the population. In recent years, this process has accelerated, with notably young people ready to leave the country. This development has been driven by search of opportunities abroad, in times of economic decline, but also as a result of closer relations with neighbouring markets and the opportunities offered in relatively large countries, such as Argentina and Brazil, especially for professionals.

The social and economic impact of the present out-migration should not be underestimated. In particular, the fact that there is a tendency for younger and skilled people to leave the country has a serious impact on the country and important implications for the future. First of all, the change in the demographic structure as a result of such out-migration, combined with an already low population growth, gives rise to a smaller group of active population which has to support the inactive population, and contribute to the extensive social security system. Second, the fact that there is an outflow of young and capable people, leads to 'brain-drain', hereby eroding the country's human capital base and hence its competitiveness.

The Environment

Adequate environmental policies are essential to ensure the long-term sustainable development of any country. The pressure put on urban development and natural resources by migration and degradation of basic public services necessitates a well formulated policy in order to ensure sustainable urban development. In particular, the marginal urban settlements are a cause of concern as they often have poor environmental standards. However, environmental issues are of a cross-cutting nature through their various links to key sectors of the economy. Uruguay's traditional livestock and agricultural sectors depend on the country's fertile soil, while important foreign exchange earnings from tourism depend on the natural beauty of the coastline (net income from services and transfers mainly tourist receipts was positive, at around US\$ 359 million).

In other words, Uruguay is a country where the link between environmental-natural resource conservation and the economy are direct and obvious. A good example of this is the forest situation in Uruguay. As a predominantly grassplains (pampas) country (75%), natural and artificial forests in Uruguay account only for respectively 3.6% and 4% of the total agricultural area (2000). An official policy of “forestry incentives” for industrial uses has been implemented for almost ten years and as a result the forestry industry has grown in this period. However, no governmental policy of “forestry sustenance” has been even discussed.

Because of its proximity to Argentina and Brazil, Uruguay's environmental situation is closely tied to that of its larger neighbours. The country faces substantial pollution from Brazilian industry along its borders especially as one-fifth of the country is affected by acid rain generated by Brazil. However, the country has been relatively successful in avoiding serious environmental degradation. As a signatory to the United Nations Framework Convention on Climate Change, Uruguay has identified areas of opportunity to implement low-cost greenhouse gas mitigation measures. These include abatement of carbon dioxide emissions through energy conservation and of methane emissions from solid waste landfills. Concerns in the environmental area in recent years relate mainly to:

- (i) inadequate natural resource management which could jeopardise the otherwise promising performance of the livestock and agricultural sectors during the last decade.
- (ii) poor water resource management is still widespread, leading to inefficient water use and increased pressure on water resources
- (iii) the marine and coastal biota along the Uruguayan coastline are increasingly impacted by human activities (a.o. tourism). Marine biodiversity may be threatened by future oil spills and other forms of hydrocarbon pollution, ship generated wastes, as well as wastes from coastal municipalities (tourism) and the main port
- (iv) managing environmental issues related to urban development (such as tourism).
- (v) On the tourism sector, strong pressure has been created by private investors through real estate agencies (until 2001 when Argentina’s economic recession reduced summer tourism by almost 80%). Parliament has already approved a general law on coastal areas management, which should regulate the impact of the lack of planning. However, despite the existence of a ministry dealing with the environment, there is no environmental strategy at the national level.
- (vi) Despite water being an abundant resource, there is no diagnosis of subterranean water resources, or a strategy on water resource development and management, or an agenda on effective water governance (water & poverty, water & climate, water & sustainable development, etc.).

3.4. External relations

As a founding member of the UN and WTO, Uruguay is strongly committed to the multilateral rules based system in order to promote peace and prosperity. Uruguay supports constitutional democracy, political pluralism, and individual liberties. The country’s international relations have been guided by the principles of non-intervention, respect for national sovereignty and reliance on the rule of law to resolve international disputes. Uruguay is also a member of the OAS, Rio Group and ALADI.

Uruguay is an important partner in the Mercosur integration project, alongside Argentina, Brazil and Paraguay, with Bolivia and Chile as associated partners. The further strengthening of Mercosur is one of Uruguay's top foreign policy priority, as well as a stepping stone for a gradual wider international integration. Over the last two years the advance of the Mercosur integration process has slowed down. However, notwithstanding conjunctural difficulties, Uruguay continues to expose a strong policy priority in support of further Mercosur integration and the completion of the Mercosur common market. Moreover, Mercosur forms Uruguay's no. 1 external trade partner, accounting for 44.5% of its exports (Argentina 17.9% and Brazil 23.1%) and 45% of its imports. This strong exposure to Mercosur creates an important Uruguayan interest in the further progress of the Mercosur process and its external relations.

Since the conclusion in 1992 of the Framework Co-operation Agreement between the European Community and Uruguay the bilateral relationship has strengthened and the improvement of relations with the EU has become one of the priorities of the Uruguayan foreign policy. The mutual relationship is very strong in economic, but also in political and cultural terms. The relations took on a new dimension with the signature, in December 1995, of the EU-Mercosur Framework Co-operation Agreement, which has as its objective the preparation of an Inter-regional Association. To this end, specific negotiations were launched and Uruguay is an active partner in these EU-Mercosur negotiations, which aim at the intensification of political and co-operation ties, as well as the establishment of a free-trade area. One of the main stakes for the EU in these negotiations is to ensure that Mercosur realizes and completes its intention to become a fully-fledged common market. This is an important prerequisite for the EU in creating an Association with Mercosur, one in which Uruguay also has an important interest. It is the EU's objective to conclude an association agreement/free trade area between two common markets, thus obliging Mercosur to continue and to complete its programme. As such, it is clear that both Uruguay as well as Mercosur will still need to do much before the Mercosur common market is completed and an EU-Mercosur free trade area can come into being. However, at present the EU accounts for 16.2% of Uruguay's exports and 18.3% of its imports, making the EU for Uruguay the no. 2 external trade partner after Mercosur, while on a regional basis the EU is the no. 1 external trade partner for Mercosur as a whole. The EU also provided 63.9% of Uruguay's development co-operation during this period 1995-1999. For Uruguay, Mercosur is an important conduit for maintaining its essential relations with the EU.

Uruguay also has an important interest in the greater regional and hemispherical affairs. Uruguay is a participant as part of Mercosur in the process of negotiations for a Free Trade Area of the Americas (FTAA). Uruguay has been negotiating a bilateral trade agreement with Mexico, is also participating as part of Mercosur in the "4 + 1" discussions on trade and investment with the United States, based on the 1991 Rose Garden Agreement. Following a recent bilateral US-Uruguayan meeting in February 2002, a bilateral trade and investment joint committee has been established to strengthen trade co-operation between the two parties. The USA forms for Uruguay the no. 3 external trade partner, accounting for 7.8% of its exports and 9.7% of its imports. The USA also provided 2.7% of Uruguay's development co-operation during this period 1995-1999.

3.5. Sustainability of current policies

The government of President Batlle has to get out of the present economic recession and solve a number of longer term social issues confronting Uruguay. In order to do so it has to

tackle a wide range of reform issues, both in the economy as well as in public policies, on which limited progress was made in the past years. To be able to achieve this progress, the government depends on a positive outcome of two crucial processes: 1) it will be required to forge a broad consensus in the Uruguayan Parliament for its policies; 2) the external economic climate plays an important role in the success of the government's economic policy.

As regards the first element, given the fact that the 1999 election results produced a parliament divided among the three main political forces, President Batlle's capacity to implement any major reform initiatives is constrained by the need to negotiate legislative approval with both the opposition party Encuentro Progresista–Frente Amplio as well as with his coalition partner, the Blanco Party. The last elections in Uruguay were held in October 1999 and required two rounds of voting for the election of a President as no candidate received the required majority of votes in the first round. Thanks to the alliance with the Blanco Party Jorge Batlle, leader of the Colorado Party, managed to muster enough support to emerge as a victor with 51.6%. The elections produced a fragile coalition between the Colorado and Blanco Party in both Chambers. However, the opposition is in a strong position to block any legislative proposals requiring two-thirds majority, making it difficult for the present government to pursue key economic and social reforms without the political support from the left. In this context, President Batlle has promised to work closely with all parties on key issues. The Government's success in implementing its policy agenda will thus depend on the extent of support the leftist opposition is willing to provide and also to what extent the present coalition itself can maintain the working partnership. The risk in this situation lies not so much in a change of government, but rather in a paralysis of the economic and social reform process by a lack of consensus/agreement between the three main political forces, leading to a stalemate reinforcing to the current economic crisis and causing harm to Uruguay's longer term prospects.

With respect to the second element, it is clear that the external economic climate will play an important role in the success of the current government's policy. A small country like Uruguay with a limited internal market, partner in the wider Mercosur integration process, dependent on agricultural exports and suffering from low commodity prices in world markets, Uruguay is closely linked to the economic fate of its two neighbours. It was particularly affected by devaluation in Brazil since 1999 and the economic recession in Argentina. This situation worsened during 2001 and has by now also started to affect progress in the Mercosur integration process. Uruguay is very dependent on its access to the Argentinean and Brazilian (Mercosur) markets for exports and whatever happens in these two countries in the medium term future, economically, financially and politically speaking, will have a major impact on the Uruguayan economic and financial situation. President Batlle will only be able to fight the economic recession and realise the necessary reforms if the external environment for Uruguay, both regionally and well as internationally, becomes more stable and returns to a situation of sustained growth.

The need to reform for the current government can be placed in the framework of the previous Uruguayan government's efforts since 1995 to implement a medium-term reform programme, which included three basic components: 1) State reform and modernisation; 2) social security reform; 3) reforms in the educational sector. The government of President Batlle has declared its intention to continue with these reforms and build on the economic progress achieved in the 1990s. In this context the 2000-2004 national budget was presented to the Congress in October 2000, and came into effect on February 26, 2001. This comprehensive national budget covers the whole term of government of President Batlle.

However, ultimately, the political prerogative will be the main element to ensure the sustainability of the present government's policies.

3.6. Medium term challenges

Over the last couple of years, since Uruguay entered into one of its deepest and longest lasting recessions in recent time, the country has revealed a series of structural weaknesses in its economy, and which need to be addressed in order to ensure a stable economic recovery and in order to create the right conditions for sustained medium- and long term GDP growth and development. Such growth is necessary in order to tackle the growing number of social problems that are currently affecting Uruguayan society and that pose a threat to its long term stability and development.

Some of these social issues may seem to be embedded in the short term situation, such as unemployment, poverty and social exclusion, but the more important social matters bear long term implications for Uruguayan society and the economy. On the one hand the generous social security system (relatively-speaking by Latin American standards), which has created a heavy financial burden on the political-economic system, while on the other hand the lack of opportunities for younger and skilled people, which has led to an out-migration or brain drain of the population. This not only threatens to erode Uruguay's human capital base and thus its economic competitiveness, but is also having a serious impact on the demographic structure of Uruguay, where a smaller group of active population has to support a growing inactive population and carry the financial burden of the extensive social security system.

Since 1999, Uruguay has faced a less favourable external environment, and given its dependence on exports of trade and services, the country faces some serious challenges in the medium and longer term. In recent years, economic growth has been negative and unemployment steadily on the rise. Latest estimates by the IDB indicate a negative growth of -2% during 2001. Although external shocks and regional developments have played an important role in this process, there remain underlying problems of a structural nature in the economy such as:

- the excessive role of the State in the economy;
- limited diversification in economic and trade structures;
- poor performance of the public sector;
- lacking competitiveness of the private sector;
- high costs of the social welfare system.

These are the challenges that President Batlle is trying to tackle, not just to get out of the current economic recession, but also to create basis for a longer term sustainable growth and development in Uruguay that can contribute to finding solutions for its growing social problems. Improving competitiveness, diversifying trade structures, reducing the role of the State in the economy, improving public sector efficiency and modernisation of State institutions, and promoting private sector development and improving the investment climate should all contribute to an improvement of the medium term economic situation. However, these reforms will both generate longer term effects that are beneficial for the Uruguayan economy as a whole, as well as create the necessary opportunities for younger people to stay in Uruguay and use their capacities to the benefit of their own country. This could alleviate the situation as regards the social welfare system, as well as provide solutions for addressing development issues such as poverty and internal migration flows.

4. ASSESSMENT OF PAST AND ON-GOING EUROPEAN COMMUNITY CO-OPERATION

4.1 Overview of past and ongoing EC co-operation

Co-operation between the European Commission and Uruguay started in 1986, before the opening of the EC Delegation in Montevideo in 1991. In its early phase it was carried out through decentralized co-operation, focusing on repatriate scientists, professionals and technicians, as well as in social programs executed jointly by European and Uruguayan NGOs with a total amount of almost 4 million Euro. Since the establishment of the Commission Delegation and the signature of the first Co-operation Agreement (1992) which provides for bilateral co-operation with the national authorities, especially economic co-operation and financial and technical co-operation, European amounts of aid have increased and co-operation sectors have become more diversified, including government structures, health, human rights, environment, rural development and civil society. During the period 1986 to 1999 almost 50 million Euros have been provided to Uruguay. During this period, EC contributions were focused on the following sectors:

- NGO's 12.7 million Euro (25.8%);
- Health (prevention on Hiv/Aids and drugs abuse) 1.6 million Euro (3.3%);
- Human rights (rehabilitation of torture's victims) 330,675 Euro (0.6%);
- Local development 1.4 million Euro (2.8%);
- Environment 858,800 Euro (1.7%);
- Economic co-operation and financial and technical assistance reached 29.9 million Euro (63%).

Under the economic, financial and technical assistance co-operation budget lines, a wide range of sectors have been supported by the EC. For instance, since the early 1990s, the improvement of competitiveness and the modernization of the State emerged as new development challenges faced by Uruguay, notably in the context of Mercosur integration. The development of new productive and industrial activities, forestry planning as well as an expansion of the wood sector, the modernizing of the Ministry of Foreign Affairs, support for de-centralization of municipalities and support for the development of the tourism sector, were some of the projects executed during this period.

Recently, in March 2001, the European Commission and Uruguay signed a Memorandum of Understanding, which spells out the priority sectors for the bilateral co-operation between Uruguay and the European Community for the period 2000-2006 and which also provides for an indicative amount of 18.6 million Euro for the period 2000-2006, within budget headings B7-310-financial and technical co-operation (6.5 million Euro) and B7-311-economic co-operation (12.1 million Euro). Some of the programmes identified in this Memorandum are already being prepared or entering into the implementation phase, such as:

- Support to the Uruguayan Parliament 970,000 Euro
- Support to the Sectoral Commission for Mercosur (Regional Integration) 350,000 Euro
- Environmental project in the western districts of Montevideo 900,000 Euro

4.2 Information on programmes of other donors

Given Uruguay status as a middle-income country, traditional development co-operation assistance plays a relatively limited role. In fact, official development assistance amounted to only US\$ 30.7 million in 1999. During the period 1994 to 1999 Uruguay benefited from a total amount of international co-operation assistance (loans and grants, OECD-DAC figures) of around US\$ 225 million dollars. Of this amount a major share was contributed by the European Commission and the EU Member States, totaling to an amount of US\$ 143.7 million (63.9% of the total), making the EU the largest donor by far in Uruguay. EC funds were mostly directed towards to support structural reforms (5.6%), productive reconversion (5.2%), rural and social development (80%) as well as support for health programmes related to drugs and HIV/Aids prevention, human rights and the environment. Other important donors are to be found in the UN family (UNDP, UNFPA, UNHCR, UNICEF) or in the multilateral organizations (IDB, IFAD, Montreal Protocol). The USA provided US\$ 6 million in co-operation to Uruguay during this period (2.7% of the total). US aid is focused in sectors where the EU and its Member States do not intervene (like military support, police equipment, etc.), with the exception of the drugs sector where a regular co-ordination is structured through the Dublin Summit meetings.

EU Member States' funds have been concentrated on improving competitiveness – Germany in particular has recently allocated around 12 million Euro to this sector- as well as for the modernisation of the State, training, social development, human rights, education and science and technology. IDB funds, from 1994 to 2001 were mostly destined for strengthening competitiveness and supporting the development of private enterprises (43%), support to structural reforms (22%), modernisation of the State (27%) and, finally, social development (7%). During the period 1995 to 2000, UNDP funds covered the following areas: 17% for the modernisation of the State, 3% for support to prevention programmes against drugs and HIV/Aids through UN-AIDS funds, 17% to social development activities, in particular for supporting child and family attention centres, and 63% for environment, through the Global Environment Fund (Montreal Protocol).

4.3. Recommendations

Based on the Commission's experience of formulating external policies and conducting international relations it has become clear that the past forty years of EC development co-operation has proven that key factors for sustainable development are: 1) a stable democracy and the rule of law; 2) well-functioning institutions; 3) the implementation of healthy internal policies based on good governance, fair distribution of incomes, maintenance of macroeconomic equilibrium, economic and commercial openness, respect for the environment and social dialogue. Many of these key factors are today recognised by the international donor community as being essential for achieving sustainable development. In the case of Uruguay many of these key factors are present, though certain ones could use some improvement. These are often the ones where Uruguay is facing important challenges.

Based on the experience of the Commission's Delegation in Montevideo as regards co-operation with Uruguay in the past, the following principles should be respected in order to ensure greater effectiveness and coherence of EC donor activity. 1) EC contributions should ideally concentrate in key sectors of priority avoiding a proliferation of projects over a large number of areas. This should also contribute to enhance complementarity and avoid overlapping of donor activities in the country. 2) Although the institutional capacity of the country is strong, sustainability of donor interventions in some areas may be an issue, and efforts should therefore be made to ensure continuity and close evaluation of the

implementation of projects. 3) While co-operation with the authorities has generally worked well, there may still be a need to better articulate the relationship between the OPP (the Budget and Planning Office) and concerned line ministries in order to improve co-ordination internally.

However, following the experience of the DG RELEX Geographical Desk in Brussels, it has also to be noted that in previous years a Mercosur perspective has been lacking to a certain extent in the bilateral co-operation policies of the EC with the individual member states of Mercosur. A full co-ordination or linkage needs to take place between the co-operation policies at the regional level and the co-operation policies at the bilateral level with these countries. Whereas Mercosur as a regional process still needs to complete its common market and prepare itself for an association and a free trade area with the EU, it is clear that the Mercosur member states will also need to go a long way at the national/domestic level to prepare themselves for these two major events. The specific challenges for Uruguay of competitiveness/productivity/trade issues and of institutional/State modernisation issues are very relevant in creating a stronger link between the bilateral co-operation relationship with Uruguay and the regional co-operation relationship with Mercosur.

Following evaluations carried out on past co-operation it has become clear that from 1995 onwards a growing emphasis on horizontal and decentralised programmes has taken place in the context of economic co-operation with Latin America (i.a. ALURE, ALFA, URB-AL). This has led to a diversification of partners through the establishment of networks drawn from civil society (incl. business community)⁴ Though weaknesses in design and implementation occurred in general, it is important to note that this type of activities also yielded positive lessons, in particular for 1) enhancing the role of EU enterprises in the development process of Latin American countries, and 2) developing structures that may in the long term help strengthen the position of the private sector in this region. For the future it is recommended that decentralised programmes should be sustained by gradually shifting to a more market-driven approach, while emphasis should be placed on encouraging the emergence of European-linked business associations or chambers of commerce with the support of modest amounts of “seed” money from the EC. In this respect a pro-active identification and funding of initiatives by the private sector and civil society is recommended. Taking the specific case of Uruguay this means that the use of the horizontal programmes should be stimulated and encouraged, especially in view of Uruguay’s priorities in the field of productivity and competitiveness.

5. EUROPEAN COMMUNITY RESPONSE STRATEGY

5.1 Priority areas for future co-operation

The EC response strategy should be in line with the EC general co-operation objectives, specifically the ones that are most relevant for Uruguay such as sustainable economic and social development, integration into the world economy and poverty reduction. However, co-operation with an upper middle-income country like Uruguay, having a relatively well-developed level of economic and social development, cannot be based on the same criteria as co-operation with poorer countries, where development policy takes on a much more priority role.

⁴ Analysis and recommendation derived from the most recent evaluation of economic co-operation with Latin America completed in August 2001 by Eva-EU Association (Nordic Consulting Group a/s).

Secondly, the response strategy should be fully coherent with the Memorandum of Understanding, which was signed with Uruguay in March 2001 and which foresees an indicative budget of 18.6 million Euro for the period 2000-2006. The priorities identified in the Memorandum of Understanding remain valid.

Thirdly, future EC co-operation must take account of the experience of past EC co-operation in Uruguay and ensure a degree of continuity and coherence in its actions, while also looking for ways to ensure complementarity with other donors' co-operation in Uruguay and a degree of coherence between EC co-operation in Uruguay and other EC policies with regard to Uruguay. Therefore EC co-operation should be selective and focus on a limited number of areas where the EC has a comparative advantage. EC co-operation should make a difference, as compared to other donors' co-operation, due to the specific characteristics of the EC as a successful common market/economic and monetary union, using the experiences gained in the EC integration process and in various EU member. The specific EC regional perspective should be considered as an added value to all fields of co-operation.

Based on the assessment of the current development challenges faced by Uruguay, the response strategy aims to focus on areas where EC co-operation can effectively play an important role in contributing to on-going government efforts. The objective of EC co-operation with Uruguay during the next five years should be to assist the country in implementing reforms in the economic area and public administration so as to overcome the current economic recession and realise its medium-term development plan that should lay the basis for a more competitive and diversified economy, one able of producing sustained economic growth. In realising this, solutions will also be created for tackling the longer term social problems that face the Uruguay of tomorrow, although in the shorter term, during the next five years, EC co-operation should also address some of the most pressing social problems that confront Uruguay today.

In view of the preceding analysis, the EC response strategy should focus on the following three focal areas as priority sectors for EC co-operation:

- Economic reform
- Modernising the State
- Social development

Co-operation in these three focal areas should provide a boost the Uruguayan government's efforts to tackle the main challenges that it is facing, as well as provide some support to the current social problems. These three areas should be supported by the financial resources available under the budget lines B7-311 for economic co-operation (12.1 million Euro) and B7-310 financial-technical co-operation (6.5 million Euro).

Economic reform

Co-operation in this sector has a special relevance for Uruguay in respect of its Mercosur and international policies and the dependence of its economic future on progress and growth in these areas. The main objective in this area should consist of actions that assist the productive and services sectors by supporting the efforts of the government to diversify economic structures and improve quality of production, by promoting the development of services, and by bringing European and Uruguayan businesses closer together. The actions should be

conceived avoiding any overlap with AL-INVEST actions and/or European funds managed by the IDB for the SME sector in Latin America.

However, as secondary objectives in this area of co-operation, actions should also be undertaken that aim at improving competitiveness and productivity by contributing to the Uruguay's technological innovation capacity, as well as actions that aim at enhancing Uruguay's capacity to participate in regional and multilateral negotiations and to fully implement their results. This would on the one hand imply co-operation activities in the field of science and technology with Uruguay, while on the other hand it would imply trade-related technical assistance allowing Uruguay to strengthen its institutional and regulatory capacities, notably in the areas of trade facilitation and standards.

Modernising the State

Co-operation should concentrate mainly on institutional support, including reform, decentralisation and modernisation of State institutions, which has both a national as well as a Mercosur relevance for Uruguay. Co-operation should back Uruguay's efforts to improve the operation and increase the transparency of the various state institutions, and to rationalise and improve the efficiency of the administration. A public administration which is transparent, of an appropriate size, that can manage public funds efficiently and that can make decisions at the appropriate level, is among the preconditions for a sustainable economic and social development. A more efficient public administration will make a big difference in helping Uruguay to create greater competitiveness and productivity. As far as the reform and modernisation of the State is concerned, the EU should support the government to continue with the process initiated by previous governments. This process will involve three key elements:

- 1) Reducing the role of the State in the economy through deregulation of particular sectors in order to open up to competition and private participation.
- 2) Support to relevant institutions (for instance, the "Unidades Reguladoras").
- 3) Creating an efficient and modern public sector by ensuring better governance and transparency as well as improving the quality of public services.

Social development

The social sector, being a government priority in its national development strategy, will also form part of EC co-operation during the next five years in order to alleviate hardships during the reform process and to contribute to the longer term solution of Uruguay's social problems. Two key areas of intervention should be foreseen: the integration of young people into the labour market and support to efforts to reduce unemployment, especially among women.

EC co-operation with Uruguay in other non-focal areas and through other financial instruments or programmes should be continued during the next five years and as such could either provide additional resources to the priority areas described in the above response strategy, or provide supplementary assistance to important areas for Uruguay's development, where it was not possible to provide priority resources from the economic co-operation and financial-technical co-operation budget lines.

Budget lines that could provide additional resources for established priority areas, such as economic reform, could be:

- horizontal programmes for co-operation in Latin America (AL-INVEST, URB-AL, ALFA, @LIS).
- horizontal framework programmes in the field of science and technology;
- the Synergy programme (energy efficiency).

Budget lines that could provide supplementary assistance to important non-focal areas for Uruguay's development, such as regional integration or the environment, or more cross-cutting issues such as human rights or drugs, could be:

- environmental co-operation;
- decentralised co-operation (NGOs);
- horizontal programmes on human rights;
- horizontal programmes on drugs.

Finance from these other instruments and programmes will, however, be decided in accordance with the Commission's procedures for the budget lines concerned and will depend on the availability of funds.

5.2. Coherence with EC policies

The main strategic objective of Uruguay and the other countries of the Mercosur is to fully integrate themselves into the global system and to participate in international organisations in order to ensure their sustainable development and, ultimately, to become part of the group of developed countries. Respect for democratic principles, the rule of law and good governance constitute the cornerstone of the relations between the EU and the countries of the Mercosur to be implemented through the political dialogue at the various levels (Heads of State and Government, Ministers, ad hoc group of high officials etc.).

As far as **trade aspects** are concerned, the long-term objective in relation to the Uruguay and the other Mercosur countries is the full liberalisation of trade and investment. This will imply pursuing the conclusion of the EU/Mercosur negotiations for an Interregional Association Agreement, a key element for the future EU-Latin American relations and European presence in Latin America. In the short and medium term this implies pursuing the EU/Mercosur negotiations, while at the same time at the national level trying to solve the main trade irritants and prevent the introduction of new barriers. The priority is thus to come to amicable agreement with Uruguay on priority market access cases, which contravene WTO rules, via bilateral consultations and to establish lists and analyse other cases of market access barriers. In the area of co-operation, trade concerns should be taken into account, especially in the EU-Mercosur framework. This wish to liberalise trade has a number of important side effects : being that the EU is trying to promote its way of functioning at the level of other community policies in order to facilitate exchanges and strengthen the commercial opportunities available, in particular in the fields of single market policy, tax and customs policies, competition policy and statistics.

The EU is by far the most important importer of **agricultural produce** from Uruguay and the other Mercosur countries, absorbing 39% of the agricultural exports of Mercosur. More than 60% of the agricultural imports from Mercosur enter the EU at a 0% customs rate. In addition, certain products benefit from a preferential access in the framework of tariff contingents. However, the Mercosur countries, which are major producers in the agricultural field, reject the EU's Common Agricultural Policy (CAP) and are striving for a total

liberalisation of trade in this area, in particular through the Cairns Group. However, it has to be mentioned that the CAP has significantly changed during the past years, with social and environmental measures being strengthened, while institutional prices have been lowered, leading to gradual approximation of community agricultural prices to the level of world prices.

As far as agreements on *wines and spirits* are concerned, the EU and Mercosul have agreed to pursue negotiations on wines and spirits between the EC and the Mercosul countries, it being understood that an agreement on wines and spirits resulting from these bilateral negotiations will be part of the single undertaking of the future bi-regional association agreement.

In the area of the **single market policy** the EU's strategy of is to conclude a public procurement agreement, which it is currently negotiating with Mercosur, thus aiming at an opening up of the sector to European companies and, more in general, the EU is seeking to promote its practices in this area. The EU is also interested in concluding an agreement on concessions and other types of public-private partnerships. The current negotiations with Mercosur should ensure that the countries provide an effective and appropriate protection of intellectual and industrial property rights in accordance with the highest international standards, including effective means of enforcing such rights provided for in international treaties. Measures taken by the EU in the framework of some of its policies, such as its **health and consumer protection policy**, might be referred to by some as being "protectionist", however, they relate to an established level of quality required by European consumers. If Uruguay and the other Mercosur countries wish to maintain their strong presence in the European market, they will have to adapt to the established requirements for food safety of European consumers, thus the importance for these countries of concluding a veterinary and phythosanitary agreement with the EU. As far as **veterinary and phythosanitary** agreements are concerned, the EU and Mercosul have agreed to pursue negotiations on veterinary and phythosanitary issues between the EC and the Mercosur countries, it being understood that a veterinary and phythosanitary agreement resulting from these bilateral negotiations will be part of the single undertaking of the future bi-regional association agreement.

In the field of **fisheries**, the Mercosur countries are also important partners of the EU. A co-operation agreement was signed with Argentina in this field, which included a science and technology co-operation section and support to the creation of joint ventures and temporary partnerships for the exploitation of fishery resources. This agreement was not renewed in 1999, but the EU is in discussion with the Argentinean government and wishes to conclude a similar agreement with Chile and Brazil. Such an agreement would probably be of lesser interest to Uruguay.

In the area of **science**, the community policy also has a significant impact on the Mercosur countries. The EU is seeking co-operation with these countries, in particular to allow high-level researchers from these countries to participate in community research. The EC has already signed a science and technology co-operation agreement with Argentina, in order to open up reciprocal possibilities to participate in the programmes and activities managed by each party in the field of R&D, while discussions are underway with Brazil. It is the EU's strategy to favour the concrete implementation of these agreements, obliging the Mercosur authorities to finance the participation by their researchers in the projects of the 6th Framework Programme and supporting the participation of European researchers in the

research programmes of these countries. Moreover, there is a community programme called INCO, which offers possibilities of scientific co-operation in the areas of health, agriculture, environment and development policy. Finally, other community policies deserve to be mentioned to the extent where they may influence the EU's co-operation strategy. In the field of the **environment** the EU has identified four main areas of action and among them climate change and biodiversity loss form the key fields of action. The EU is more specifically involved in stopping deforestation and the degradation of forests. The development of the **information society** is also an important horizontal objective for the EU, having a positive impact on essential development issues. In the field of **transport** priorities are market integration and improvement of security/safety in air and maritime transport, while in the field of **energy** the EU seeks to ensure security of supply including an appropriate energy infrastructure network and to develop alternative sources of energy. In this field the Synergy programme allows for the financing of co-operation projects with the Mercosur countries, to assist them in defining, formulation and implementing their energy policies in areas of mutual interest and to promote industrial co-operation in the energy sector. In the area of **competition** the EU is stimulating the Mercosur countries to adopt legislation on competition which basically follows the EU model for competition policy.

With regard to the question of coherence with EC policies one can **conclude** that our policies towards Uruguay form part of the framework and context of EC policies towards Mercosur as a whole and are linked to the EC policies towards the other Member States of Mercosur. Thus, EC policy on Uruguay is not isolated from the political and economic environment in which Uruguay is obliged to shape its future and as such provides a realistic perspective for further developing the EC relationship with a country such as Uruguay. In terms of coherence between EC co-operation in Uruguay and other EC policies in Uruguay one can conclude that they all form part of the same framework of ideas, priorities and objectives. As such they form a coherent policy mix.

5.3. Complementarity with programmes by other donors

In Uruguay traditional development co-operation assistance has played a relatively limited role. During the period 1994 to 1999 Uruguay benefited from a total amount of international co-operation assistance (loans and grants, OECD-DAC figures) of around US\$ 225 million dollars. Of this amount a major share was contributed by the European Commission and the EU Member States, totalling to an amount of US\$ 143.7 million (63.9% of the total), making the EU the largest donor by far in Uruguay. Other important donors are to be found in the UN family (UNDP, UNFPA, UNHCR, UNICEF) or in the multilateral organisations (IDB, IFAD, Montreal Protocol). The USA provided US\$ 6 million in co-operation to Uruguay during this period (2.7% of the total).

Priority areas in the EC co-operation complemented other donor's activities by either strengthening co-operation in certain areas of great priority (i.a. competitiveness, social development) or by focussing on issues that did not receive great attention in the international donor community or that were only supported by a few donors (science & technology). In all cases, the specific EC regional perspective must be considered as an added value to any field of co-operation, because of the EC's comparative advantage as representing a successful regional integration process and the way this can contribute to Uruguay's efforts at regional integration. Activities by international donors can mainly be grouped together in three areas:

1) Modernisation of the State (incl. structural reforms), an area mainly dealt with by multilateral organisations such as the IDB and the UNDP, but one on which the EC and the EU Member States put much emphasis and which serves very prominently in Uruguay's development strategy. During the next five years the EC's co-operation should be complementary to that of other donors in this area, while also taking in to account Uruguay's regional considerations (Mercosur).

2) Social Development and Sustainable Development (social and rural development, health issues, education, human rights, environment), an area covered by various donors such as the IDB and the UNDP, as well as the EC and EU Member States, and an area where much work still has to be done in Uruguay. EC co-operation during the next five years should be both complementary to that of other donors, as well as specific with regard our experiences at the EU and international levels in terms of social issues.

3) Competitiveness and trade (competitiveness, productivity, conversion), an area of great priority for the Uruguayan government, both from a national point of view, as well as in the more international context. An area where both the EC and EU Member States are active, as well as the multilateral organisations such as the IDB and the UNDP. Complementarity of actions is important here, but the EC has a very particular added value to contribute in this sector, due to our experience of creating a single market, strengthening competition and enhancing competitiveness, and assisting the productive and services sectors to adapt to a more liberalised economic environment.

There are some areas supported by other donors that remain outside of the EC's scope of activities for specific reasons of competence or specialism. The search for complementarity between EC, EU and international co-operation should take place in particular in the day-to-day practice of co-operation activities, which will be facilitated by the current deconcentration exercise of the management of co-operation activities to the Commission's Delegation in Montevideo. It should bear upon the sharing of information, the exchanging of ideas, the co-ordination of activities and the timing of activities, and the identification of a division of activities, or a convergence of activities. However, these activities are a two-way street, the search for complementarity and a full co-ordination of activities also needs to have the support and input of EU Member States' representatives. This type of complementarity should have a greater impact and effect during the various phases of the project cycle.

6. NATIONAL INDICATIVE PROGRAMME 2002-2006

6.1. Introduction

The National Indicative Programme is the operational translation of the above-mentioned response strategy and covers the budgetary period 2000-2006 with an indicative financial envelope that amounts to 18.6 million Euro and which only concerns budget lines B7-310 financial and technical co-operation (6.5 million Euro) and B7-311 economic co-operation (12.1 million Euro). The focal areas identified as priority sectors for the co-operation strategy with Uruguay are the following:

1. Economic reform (8.4 million Euro/or 45% of the indicative budget; dividing key for various actions 29%/16%) (B7-311)
2. Modernising the State (5.5 million Euro/or 30% of the indicative budget) (B7-310)
3. Social development (2.45 million Euro/or 13% of the indicative budget) (B7-311)

The National Indicative Programme as presented in the following can be revised on a yearly basis in function of developments, events and special needs that may arise during the course the period of implementation of the country strategy for Uruguay until 2006.

The National Indicative Programme is based on the condition of full coherence with the Memorandum of Understanding signed with Uruguay in March 2001, but takes into account those “measures” in the Memorandum of Understanding that are already being prepared, identified or being implemented. This implies that a certain part of the total indicative financial resources of 18.6 million Euro (2.25 million Euro/12% thereof) is already being used at present.

The final selection of the projects and the corresponding amounts will be done in function of the results of the identification and detailed preparation activities undertaken by the European Commission. The indicative work programme is subject to the annual budgetary resources available to the European Commission.

The modalities and principles for the monitoring, evaluation and revision of programmes and projects will be determined by the general rules applicable to these issues.

6.2. National Indicative Programme.

6.2.1. *Economic reform*

Background

Uruguay is undergoing a process of structural reforms aimed at increasing competitiveness, stimulating private sector development, diversifying the productive structure of the economy, attracting investments and boosting exports. This process is placed both in a national, a Mercosur and an international context. This is a priority area of the current government and the EC has also recognised it as a priority area for Uruguay’s development. In the current negative economic situation in which Uruguay finds itself, this sector should not only aim at short term improvements, but also at a more medium to longer term effect that aims at improving the Uruguayan economy’s competitiveness, diversification and integration into the world economy.

Co-operation in this sector has a special relevance for Uruguay in respect of its strong political support for the Mercosur process and the dependence of Uruguay’s economic future on progress and growth both in the regional and international economic areas. Supplementary actions in this area of co-operation, which should also be undertaken to improve the competitiveness and productivity of the economy and productive sector, would be on the one hand actions contributing to Uruguay’s technological innovation capacity, while on the other hand actions aiming at enhancing Uruguay’s capacity to participate in regional and multilateral negotiations and to fully implement their results. This would on the one hand imply co-operation activities in the field of science and technology with Uruguay, while on the other hand it would imply trade-related technical assistance allowing Uruguay to strengthen its institutional and regulatory capacities, notably in the areas of trade facilitation and standards.

a) Competitiveness & diversification programme

Objective : The main objective in this action would be to assist the productive and services sectors by supporting the efforts of the government to diversify economic structures and improve quality of production, by promoting the development of services and by bringing European and Uruguayan businesses closer together. The actions should be conceived in such a way as to avoid any overlap with AL-INVEST actions and/or European funds managed by the IDB for the SME sector in Latin America. However, as a secondary objective in this action, also in order to increase competitiveness, this action should include elements aimed at better managing the regional and international environment on which Uruguay's economic future so much depends, allowing Uruguay to participate more effectively in and benefit from international negotiations. To this end it must enhance its capacity to negotiate and to implement the results of negotiations. In order to benefit from the link between these two objectives, using the synergies and efficiencies for the benefit of both, these objectives are joined together in the same programme, in which both separate types of actions can be foreseen, as well as joint or overlapping types of actions.

Using codification of Trade Related Technical Assistance and Capacity Building (TRTA/CB) activities, as defined by the WTO in co-operation with the OECD and bilateral donors, based on the Doha Ministerial Declaration of November 2001, probably most of the "Competitiveness and diversification programme" under a) could be identified as TRTA/CB, amounting to 5.4 million Euro, or 29% of the indicative budget.

Expected results :

- greater economic diversification ;
- higher rates of productivity ;
- improvement of economic growth ;
- better competitive position for Uruguayan products and companies ;
- growth of employment ;
- better participation in and management of international (multilateral, inter-regional and regional) negotiations ;
- full implementation of results of international (multilateral, inter-regional and regional) negotiations ;
- strengthening of institutional capacities to allow for a better participation in negotiations in the future and a better implement of new obligations assumed in the future.
- strengthening of regulatory capacities, notably in the areas of trade facilitation and standards.

Key indicators of achievement :

- more diverse package of exports to regional and international partners ;
- more output/production per unit of labour/capital/technology applied ;
- positive rates of economic growth ;
- growth of volume and value of exports ;
- lower unemployment rate ;
- performance of Uruguayan negotiators in international negotiations ;
- proven implementation of negotiating results in Uruguay ;
- improvements in government ministries and other public institutions, as well as in relevant private-sector organisations ;
- improved market access, as well as greater compatibility of standards.

Cross-cutting issues :

- sustainable economic and social development ;
- integration into the world economy ;
- trade and development ;
- gender equality ;
- good governance ;
- fight against poverty.

Programme components :

- technical assistance and training to the government, to the productive sector and to the services sector to develop and adopt innovative measures enhancing productivity and creating a greater diversity in the production of goods and the offer of services;
- technical assistance aiming in particular at the promotion of the development of services ;
- transfer of know-how, and possibly technology, to strengthen competitiveness and productivity of companies, possibly including collaboration with EU companies ;
- technical assistance to better implement the results of international negotiations ;
- capacity building to better participate in international negotiations ;
- technical assistance in the fields of customs administration and valuation, import-export-transit procedures, trade statistics, SPS, TBT, IPR, market access issues, trade and investment, trade and competition policy, transparency in government procurement, trade and the environment.

Financing : 5.4 million Euro/or 29% of the indicative budget (B7-311)

b) Science & technology programme

Objective : The main objective in this action is aimed at the Science & Technology community (research) and should contribute to the country's technological innovation capacity and through this help the improvement of production systems, productivity and competitiveness of the Uruguayan business community.

Expected results :

- closer co-operation and collaboration between EU and Uruguayan scientific and research institutions ;
- generation, exploitation and application of technology innovations that enhance the productivity of the productive and services sectors ;
- greater preparedness, and possibly also participation, of Uruguay's scientific sector for the EU's framework programmes in the field of research and development.

Key indicators of achievement :

- joint research projects completed aimed at specific S&T areas relevant for the Uruguayan economy ;
- achievement of a number of specific technology innovations, which have been implemented in practice with success by the Uruguayan business sector ;
- larger number of Uruguayan participation in the EU framework programmes on R&D.

Cross-cutting issues :

- sustainable economic and social development ;
- integration into the world economy ;

- trade and development.

Programme components :

- technical assistance and training, which builds upon the close links between the EU and Uruguayan scientific communities, aiming at fostering research into technological innovation that is directly relevant and applicable in Uruguay's business community ;
- technical assistance to improve the management of the linkage between Uruguay's scientific community and business community, aiming at facilitating the transfer of innovations to the sectors where they should be applied ;
- exchanges between scientists and institutions from both sides, focussed in particular on areas that are directly linked to greater productivity and/or diversity.

Financing : 3 million Euro/or 16% of the indicative budget (B7-311)

6.2.2. *Modernising the State*

Background

A State apparatus that is transparent and of an appropriate size, and an administration which can manage public funds efficiently and make decisions at the appropriate level, are among the preconditions for sustainable economic and social development. Therefore, Uruguay needs improve the operation and increase the transparency of the various State institutions, and to rationalise the efficiency of the administration, by means of modernising, decentralising and reforming the State and its public administration. State modernisation is in particular important in order to properly implement structural and economic reforms that are needed in the economy and that are needed to improve Uruguay's regional and international integration.

- Modernisation and decentralisation of the public function

Objectives : As a part of the process of domestic reform and modernisation, Uruguayan public institutions and public administrations need to prepare and adapt their organisations and activities to the changing domestic, regional and international context. A well-organised and efficient civil service is an essential pillar for a modern state and for sustainable economic growth. The action should focus on specific key public institutions that are directly involved in the national processes of change, reform and modernisation, while at the same time aim at decentralising public functions to more appropriate levels of government.

Expected results :

- modernisation and improvement of the performance of Uruguayan public institutions and public administration ;
- decentralisation of public functions more a more appropriate level ;
- facilitation of implementation of structural and economic reforms in the economy ;
- facilitation of introduction and implementation of Mercosur and international regulations and standards in the Uruguayan context.

Key indicators of achievement :

- provision of efficient and well-organised public services in the areas covered by the action ;
- process of decentralisation started and local authorities (municipal or sub-municipal level) increasing their abilities/authority to handle issues at their level ;
- efficient application of structural and economic reforms within reasonable timeframe;

- efficient application of international regulations and standards with reasonable timeframe.

Cross-cutting issues :

- sustainable economic and social development ;
- institutional development ;
- good governance ;
- gender equality ;
- democratisation and human rights.

Programme components :

- technical assistance to contribute to the analysis of the current operation of Uruguay's administration, the preparation of a strategy and plan of action to modernise and re-organise the public administration and public services, by using methods including training and information technology ;
- technical assistance to support actions aimed at the decentralisation of the public administration ;
- technical assistance to support actions aimed at the optimisation of performance and provision of public services.

Financing : 5.5 million Euro/or 25% of the indicative budget (B7-310)

6.2.3. Social development

Background

Uruguay is a middle-income country, which can independently shoulder the solution to fundamental social issues. However, during the current economic down-turn in Uruguay the economy is not generating sufficient means for the government in order to tackle either the short term social problems related to the current economic recession, or to address the longer term social problems that are linked to Uruguay's continuing development. This leads to a very vulnerable social situation in Uruguay. The country is faced with a number of long-term social challenges that could undermine its social and economic sustainability. The analysis presented in the country strategy provided a good idea of these problems and it is clear that much work can be done in this area to address issues and situations in the country. Especially the intergenerational aspects will bear large consequences for Uruguay in the longer term, while specific sections of the population, such as youths or women, though currently much affected in the shorter term, might be the sectors that could bear solutions for the longer term situation.

- Support to social vulnerable groups (young people & women).

Objective : This programme should aim at two key areas of intervention in the field of social vulnerable groups in Uruguay: 1) the integration of young people into the labour market; 2) support to efforts to reduce unemployment, especially among women. These two key areas are interlinked and clearly have been identified as part of the social groups at risk in Uruguay. Moreover, the employment/unemployment perspective creates a link to the other actions under this National Indicative Programming that aim at enhancing productivity and creating greater economic diversification.

Expected results :

- more employment of younger people in the economy ;

- less unemployment, in particular less unemployment among women ;
- less out-migration of young and skilled Uruguayans.

Key indicators of achievement :

- improvement of official rate of employment for young people ;
- lowering of the official unemployment rate, with a disproportionate lowering of the unemployment rate for women ;
- slowing down, halting or reversal of emigration rate of Uruguayans.

Cross-cutting issues :

- sustainable economic and social development ;
- gender equality ;
- fight against poverty.

Programme components :

- technical assistance to support the formulation of innovative methodologies that aim at better integrating young people in the labour market ;
- technical assistance to support the formulation of innovative methodologies that aim at reducing unemployment, especially among women ;
- training activities for both young people and women ;
- technical assistance to support the establishment of local production operations and family businesses.

Financing : 2.45 million Euro/or 13% of the indicative budget (B7-311)

6.3. Calendar of actions.

2002 : Modernisation and decentralisation of the public function, 5.5 million Euro.

2003 : Science & technology programme, 3 million Euro.

2005 : Competitiveness & diversification programme, 5.4 million Euro.

2006 : Support to social vulnerable groups, 2.45 million Euro.

Uruguay									
		2000	2001	2002	2003	2004	2005	2006	
1 Economic reform :									
Competitiveness & diversification programme							5,4		
Science & technology programme					3				
2 Modernising the state :									
Modernisation and decentralisation of the public function				5,5					
3 Social development :									
Support to social vulnerable groups								2,45	
4 Commitments 2000-2001:									
Total	18,6	1,3	0,9	5,5	3	0	5,4	2,45	

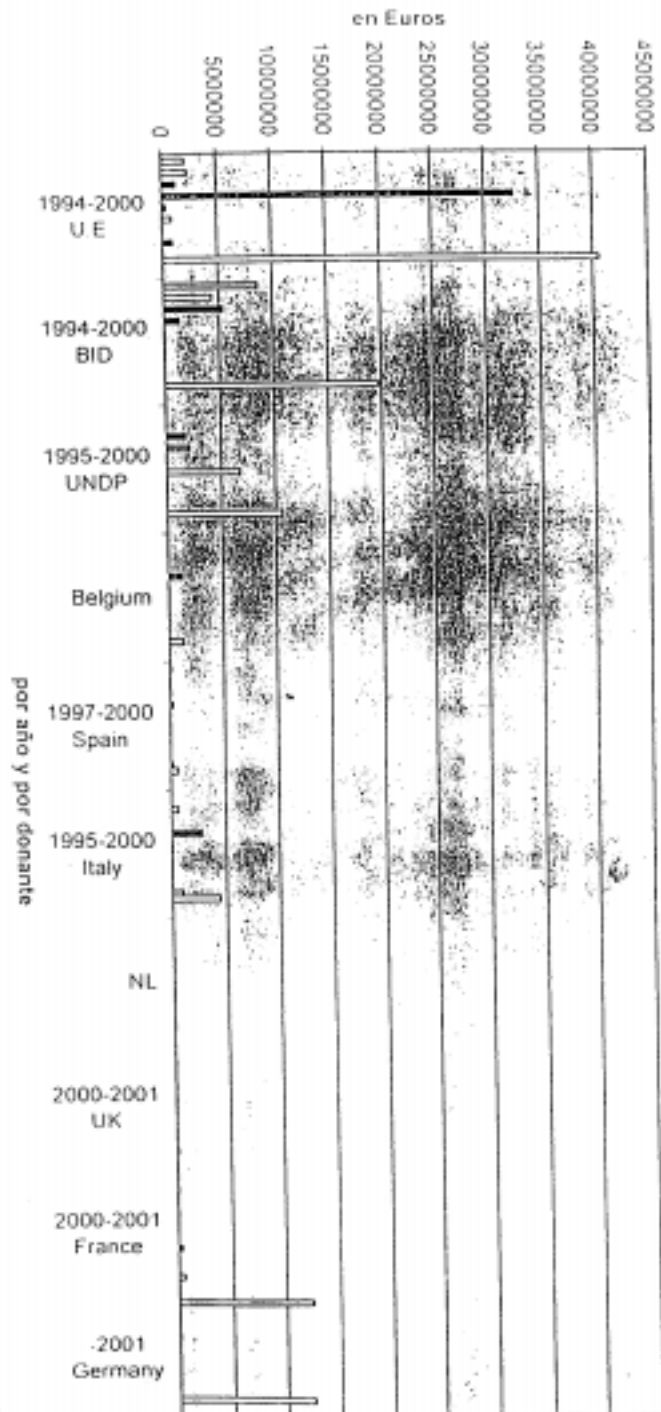
7.1. ANNEX: Donor matrix of co-operation with Uruguay

recipient name	Uruguay				
APD Brute, (Dons + prêts), millions de \$ US					
Sum of dac2a amount	year				
donor name	1995	1996	1997	1998	1999
ALL Donors, Total	75,61	42,12	43,54	33,55	30,73
Australia	0,01				
Austria	0,04	0,06	0,03	0,02	0,03
Belgium	1,21	0,8	0,97	0,95	0,63
Canada	1,21	1,2	1,64	0,79	1,33
DAC Countries, Total	62,03	33,57	36,24	25,1	24,99
EC	7,2	3,47	2,91	3,81	3,51
EU Members, Total	46,47	24,54	18,45	17,96	15,38
Finland	0,02	0,04	0,03	0,02	
France	4,66	4,25	3,18	2,05	2,33
G7, Total	35,27	24,95	31,05	20,38	20,93
Germany	11,99	9,19	8,76	10,98	8,3
IDB Sp. Fund	0,7	1,5	0,93	0,41	0,07
IFAD	1,72				
Ireland	0,01				
Italy	2,7	2,43	1,13	0,22	0,55
Japan	10,94	6,55	14,83	5,41	7,64
Korea (not in Total)	0,01	0,16	0,16	0,22	0,07
Luxembourg	0,03	0,02	0,01		
MONTREAL PROTOCOL				0,64	0,06
Multilateral , Total	13,58	8,55	7,3	8,45	5,74
Netherlands	1,77	1,76	0,78	0,3	
New Zealand	0,18	0,15	0,21	0,14	0,07
Norway	0,17	0,05	0,02	0,04	0,05
Other UN	2,09	0,71	0,12	1,35	0,3
Spain	20,38	4,06	2,13	2,6	3,14
Sweden	2,89	1,6	0,92	0,43	0,11
Switzerland	0,05	0,08	0,09	0,22	0,03
UNDP	-0,27	1,08	1,51	0,44	0,37
UNFPA	0,1	0,27	0,28	0,26	0,23
UNHCR	0,11	0,12	0,12	0,1	
UNICEF	1,03	0,71	0,73	0,88	0,66
United Kingdom	0,77	0,33	0,51	0,39	0,29
United States	3	1	1	0,54	0,49
UNTA	0,9	0,69	0,7	0,56	0,54

	U.E.	BID	UNDP	Belgium	Spain	Italy	NL	UK	France	Germany
	1994-2000	1994-2000	1995-2000		1997-2000	1995-2000		2000-2001	2000-2001	-2001
competitiveness	2 095 590	8.592.500			99.109				20 043	12 400 000
structural reforms	2 298.950	4.381.100				595.940		48.109	77 971	
modernization of state	1 274.000	5.345.000	1 813.382		49.225					
social development	32 692 048	1 400.000	2 134.545	1 292 601	274.470	2 791 652	39.000	38.106	43 329	66 000
human rights	330 675							37 635	19 763	
environment	858 800		6 663 156		10 800			15 250		
science & technology									353 511	
regional integration (*)	932 590				187					
culture / education	34 098				205 035	1 013 000	11 620	12 540		
	40.516.751	19.718.600	10.611.083	1.292.601	638.826	4.400.592	50.620	151.640	514.617	12.466.000

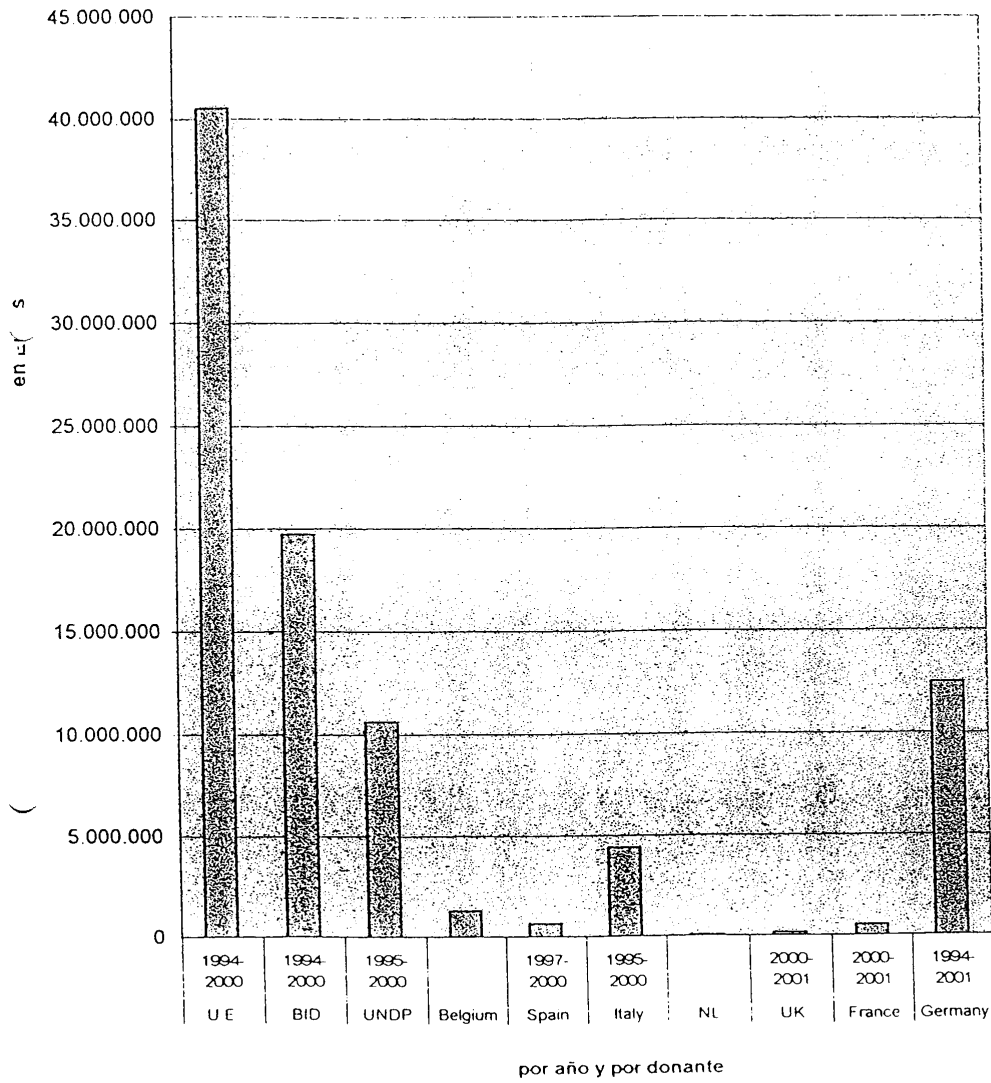
(*) excluding specific projects for MERCOSUR

Cooperación Internacional (donantes)



- competitiveness
- social development
- science & technology
- modernization of state
- environment
- culture / education
- structural reforms
- human rights
- regional integration (*)
- (*) excluding specific projects for MERCOSUR

Total Cooperación Internacional (Donantes)



7.2. ANNEX: Memorandum of Understanding 2000-2006

MEMORANDUM OF UNDERSTANDING
between
THE EUROPEAN COMMUNITY
and
THE EASTERN REPUBLIC OF URUGUAY

Concerning the Multiannual Guidelines for the implementation
of Community Co-operation

**MEMORANDUM OF UNDERSTANDING BETWEEN THE EUROPEAN
COMMUNITY AND THE EASTERN REPUBLIC OF URUGUAY
CONCERNING THE MULTIANNUAL GUIDELINES FOR THE
IMPLEMENTATION OF COMMUNITY COOPERATION**

The European Community, hereinafter referred to as "the Community", represented by the Commission of the European Communities, hereinafter referred to as "the Commission", and the Government of the Eastern Republic of Uruguay, represented by its Ministry of Foreign Affairs;

WHEREAS the Framework Agreement for co-operation between the European Economic Community and the Eastern Republic of Uruguay of 16 March 1992 provides for the development of various lines of co-operation, particularly economic affairs, industry, the environment, science and technology, the administration and regional integration;

WHEREAS Council Regulation (EC) No 443/92 of 25 de February de 1992 lays down the basic principles for financial and technical assistance and economic co-operation with developing countries in Latin America, and Article 9 thereof recommends that multiannual indicative programming should be established by country, wherever possible;

WHEREAS both parties attach great importance to co-operation as a means of promoting economic and social development and reinforcing reciprocal links,

HAVE AGREED AS FOLLOWS:

ARTICLE 1

Objective and Context

1. Objective

The objective of this Memorandum of Understanding is to define multiannual guidelines for implementing co-operation between the Eastern Republic of Uruguay and the European Community for the period 2000-2006.

2. Context

The range of activities covered by this Memorandum for the period indicated covers financial and technical co-operation and economic co-operation, for which management rules and allocation methods are laid down in Council Regulation (EC) No 443/92 of 25 February 1992.

In addition to the co-operation activities included in this Memorandum, other Community-financed co-operation activities of a regional or national nature (e.g. projects carried out by NGOs) or decentralised nature (AL-INVEST, ALURE, URB-AL, ALFA, SYNERGY programmes etc.) may be carried out.

The co-operation priorities for the period 2000-2006 have been set in accordance with the policy orientations of the Uruguayan government and are based on the priorities set out in the indicative multiannual guidelines (IMG/OPIN) for Uruguay drawn up by the Commission in agreement with the Uruguayan authorities and approved by it in September 1998.

ARTICLE 2

Basic Principles

In order to determine the sectors and subsectors on which the Community will focus its co-operation activities for the period 2000-2006, the following principles will apply:

- All the sectors and subsectors selected will be in line with the priorities laid down by the Uruguayan government, and they must fall within the framework of government sectoral policies which can rely on suitable national funding. Community action will support Uruguay's efforts to draw up and implement these policies.
- The Uruguayan government undertakes to provide the necessary counterpart resources, including financial resources, needed to implement the operations covered by this Memorandum.
- Special attention will be devoted to ensuring that Community co-operation activities in Uruguay are co-ordinated with those of the European Union Member States and other donors.

- The Uruguayan government will also undertake to use intersectoral arrangements to bring about proper co-ordination with the various ministries and bodies involved.

The Uruguayan government is making the Planning and Budget Office responsible for the operations covered by this Memorandum.

This Memorandum has been drawn up in agreement with the Member States' embassies in Montevideo.

ARTICLE 3

Sectors of Co-operation

In accordance with the Framework Agreement for co-operation between the European Economic Community and the Eastern Republic of Uruguay of 16 March 1992 and with the priorities set out in the indicative multiannual guidelines (IMG/OPIN) for Uruguay, co-operation between the European Community and Uruguay over the period 2000-2006 will focus on the sectors and subsectors listed below:

I. Production and Services

Indicative Community contribution: 5.400.000 Euro (economic co-operation).

The aim of the Community contribution is to back the efforts to adapt Uruguay's economy to an increasingly globalised environment. In some cases, traditional production structures which are part of the social and production fabric, especially in SMEs, will have to be reworked. If there is to be improvement, quality output with added value and special attention to environmental issues will need to be promoted. Output will need to focus on well-defined market niches, and efforts will have to be made to diversify products and markets.

Objectives:

- Exploiting the Uruguayan economy's strengths, making use of existing resources and promoting a policy of quality and diversification.
- Promoting the development of services.
- Bringing European and Uruguayan businesses, particularly SMEs, closer together.

1.1. Measures

2002 - 2005

- 1.1.1 Supporting diversification of the Uruguayan economy and the development of policy for non-traditional sectors of agro-industry and services

This area of activity, which is based on a diagnostic assessment of the Uruguayan economy, will seek to find possible problems and identify sectors and products with a comparative advantage and the potential to be competitive. At a later stage, a training programme (in areas such as quality, European standards and marketing) and a promotion strategy for accurately identified competitive sectors and goods will have to be drawn up and implemented.

When it comes to producing an agro-industry policy covering non-traditional sectors, a detailed analysis of realities in Uruguayan agro-industry, its potential and its weaknesses will make it possible to find subsectors and products for which Uruguay has a comparative advantage, so that policy and strategy can be plotted for them.

With regard to formulating policy for the service sector, Uruguay's geostrategic position is an important point of departure for developing services, with a focus on tourism and the backdrop of Mercosur. Provision also needs to be made for developing sectors such as financial services, transport and insurance.

2003 - 2005

1.1.2. Programme backing the development of links between Uruguayan and European businesses.

As a corollary of the activity described in 1.1.1., this programme will seek to develop strategies to help Uruguayan businesses and the related structure of associations to forge links with European businesses. This support will concentrate on the sectors which are most competitive and have a comparative advantage. The programme needs to complement cross-cutting programmes like AL-INVEST.

2. Modernising the State

Indicative Community contribution: 6.500.000 Euro (financial and technical co-operation)

The aim of the Community contribution will be to back Uruguay's efforts to improve the operation and increase the transparency of the various state institutions, and to rationalise and improve the efficiency of the administration. A state apparatus which is transparent and of appropriate size, and an administration which can manage public funds efficiently and make decisions at the appropriate level are among the preconditions for harmonious and sustainable economic and social development.

Objectives:

- Organising the administration and public services.
- Decentralising administration.
- Modernising and optimising the social security system

2.1. Measures:

2000 - 2001

2.1.1. Support for the Uruguayan Parliament.

The overall aim of the programme is to back Uruguay's efforts to improve the operation of its parliament. The programme will seek to contribute to such areas as refining the drafting of legislative texts and the way they are circulated and debated, improve the information systems of the two chambers of parliament and establish a plan for communication between the parliament and the citizen.

2001 - 2003

2.1.2. Backing for the modernisation of the civil service and public services.

The Uruguayan government has made modernising the state one of its priorities. This is because a well-organised and efficient civil service is an essential pillar of a modern state. As a result, the programme intends to back the government's efforts to reform the country's civil service and public services, to make them more efficient. This will be achieved by analysing the operation of Uruguay's administration, locating any shortcomings and preparing a strategy and plan of action to modernise the civil service and public services using methods including training. The analysis should also cover the use of information technology to improve the administration's quality and efficiency in the field of culture (the Biblioteca Nacional - national library).

2001-2002

2.1.3. Backing for the social security system.

The aim of this programme is to help to optimise the operation of the Banco de Previsión Social (welfare bank), the organisation which is responsible for running social security in Uruguay.

2002 - 2006

2.1.4. Backing for administrative decentralisation.

Uruguay's population (almost half its inhabitants) is concentrated in the capital, Montevideo. This has resulted in heavy administrative centralisation. The aim of this programme is to help define an administrative decentralisation policy which is suited to the reality of the country and can contribute to improving the management of public funds and local affairs. It needs to ensure that there is continuity with programmes previously implemented in the sector, and to draw on their findings.

3. Regional Integration

Indicative Community contribution: 350.000 Euro (economic co-operation).

By providing direct institutional support for international consultation processes, Community co-operation helped to set off regional integration in Latin America. In the case of Mercosur, the Community implemented programmes to transfer know-how in customs management, technical standards and agricultural markets. There are now plans to extend this co-operation to other matters. The establishment of Mercosur has considerably boosted regional trade. In 1999, 45% of Uruguay's exports went to Mercosur, and 44% of its imports came from Mercosur.

Objectives:

- Consolidating and furthering Uruguay's integration into Mercosur.
- Helping Uruguay to make the most of the benefits and advantages it draws from Mercosur membership.

3.1 Measures:

2000-2001

3.1.1. Backing for the Sectoral Commission for Mercosur (COMISEC).

The aim of the programme is to back the process of integration by means of institutional support for COMISEC. More specifically, the programme will help to develop instruments for analysing, monitoring and providing information on Mercosur's process of integration, to facilitate decision-making by the various sectors involved (public, private and academic).

4. The Social Sector

Indicative Community contribution: 2.450.000 Euro (economic co-operation).

As Uruguay is a middle-income country which can independently shoulder social measures which need fundamental solutions, existing and future co-operation activities in social sectors should be interpreted as pilot and demonstration projects and should be designed with that in mind. Among the forms that such activities can take are training and the establishment of local production operations and family microbusinesses, in rural, semi-urban and urban areas.

Objectives:

- Integration of young people into the labour market
- Reducing unemployment, with special emphasis on the situation of women

4.1. Measures:

2005 - 2006

4.1.1. Programme to integrate young people into the labour market and combat social marginalisation.

The programme will not be restricted to Montevideo, and will cover the whole country. The European Union has considerable experience of policies to combat unemployment and integrate the unemployed and young people who are first-time jobseekers into the labour market. These policies to combat unemployment are translated into action through vocational training, work experience in businesses, promoting the creation of businesses, and other instruments. This experience could be of use in inspiring similar policies in Uruguay which were suited to local circumstances.

5. Protection of the Environment

Indicative Community contribution: 900.000 Euro (economic co-operation).

A multi-sector policy to protect the environment and make rational use of natural resources is among the basic preconditions for sustainable development. The Uruguayan government attaches great importance to environmental issues. Urban development in cities like Montevideo creates pressure on natural resources which requires urban management policies which preserve an environmental balance. Exchanges of European experience and know-how in this field could be of great use to Uruguay.

Objectives:

- Incorporating environmental considerations into action and decisions in the fields of urban planning and restructuring of production systems.

5.1 Measures:

2000

5.1.1. Improving the environment in the western districts of Montevideo, and converting the related economic fabric.

The aim of this programme is to back the production of a sustainable urban development policy for the western districts of Montevideo, and a package of economic, social and environmental measures.

5.1.2. Environmental and noise pollution.

6. Co-operation in Science and Technology

Indicative Community contribution: 3.000.000 Euro (economic co-operation).

Uruguay has a first-rate scientific community which maintains relations with the European scientific community, providing a fertile ground for developing co-operation in science and technology in fields of mutual interest. Community science and technology programmes implemented with Uruguay in recent years have helped to create closer links between the two scientific communities. This sector thus deserves special attention in the light of the positive results of collaboration in the past.

Objectives:

- Exploiting the results of co-operation in science and technology to produce technological innovation, particularly where it could improve the production system.

6.1. Measures:

2003 - 2005

6.1.1. Programme to back the development of science and technology.

The central aim of this programme is to determine which sectors could use technological innovation to help improve the production system. At a later stage, arrangements could be developed for exchanges between European scientists from centres of excellence in the fields chosen and Uruguayan scientists. The programme would complement the Commission's programmes in the fields of research, technological development and demonstration activities.

ARTICLE 4

Indicative financial allocation

The Community financing provided for all the activities covered by this Memorandum amounts to a total of EUR 18 600 000 for the period 2000-2006, within budget headings B7-310-financial and technical co-operation (EUR 6 500 000) and B7-311-economic co-operation (EUR 12 100 000). These amounts are purely indicative, as they may vary in the light of the Community's actual budget availability and the recipient's level of implementation of expenditure.

ARTICLE 5

Consultation procedures

The parties will hold an ongoing dialogue, through their respective representatives, on the follow-up to the provisions of this Memorandum.

ARTICLE 6

Mid-term review

Within the framework of the dialogue provided for in Article 5, this Memorandum will undergo a joint mid-term review in order to determine any measures and changes required for it to be properly implemented.

ARTICLE 7

Final provisions (future developments clause)

It is agreed that the Memorandum's provisions may be amended, altered or supplemented at the request of either of the Parties, by agreement between the latter.

7.3. ANNEX: Map of Uruguay

