Whither the Cuban economy after recovery? The reform process, upgrading strategies and the question of transition

CLAES BRUNDENIUS

Abstract. Where is the Cuban economy heading? The economy has been recovering at an average rate of four per cent per year since 1994 (after GDP declined by 35 per cent between 1989 and 1993). Many reforms have been undertaken in the direction of a market economy, but it is far from clear what kind of economy the Cuban ruling party has in mind after recovery. This article discusses the successes and shortcomings of the reform process in Cuba since the downfall of communism in Europe and the Soviet Union. It also addresses the salient issues in what appears to be a new development strategy in Cuba, and what could be said about the reforms and the strategy in the light of the debate on transition 'ten years after'.

Introduction

Not so long ago there was a lively debate on 'transition' in East and West, and North and South. Ironically, as it may seem today, that debate was about the transition from capitalism to socialism. The transition debate today is about transition from a centrally planned (socialist) economy (CPE) to a market economy (generally meaning the restoration of capitalism). This article addresses the current trends of the Cuban economy, the reform process, economic upgrading strategies, and how all this relates to the debate on transition. Most former CPEs are referred to in the debate as transition economies, and few of them have problems with accepting this characterisation. Even China and Vietnam, although not characterising themselves as transition economies, do not object to this designation in the international debate. In Cuba on the other hand there

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is strong resentment in official circles when Cuba is referred to as an ‘economy in transition’, since that would suggest that Cuba might consider abandoning ‘socialism’, and be on the road to the restoration of capitalism.

The article addresses this Cuban dilemma. If Cuba is not a transition economy, what is it and where is it heading? In Cuba the government and the ruling communist party have no problems with concepts such as ‘economic transformation and restructuring’ as a description of the Cuban process of change. Nor are issues such as hard budget constraints, enterprise reform, and financial and institutional reforms, taboo, as long as they do not question what are considered to be fundamental pillars of the socialist state (primarily meaning state ownership of the means of production).

The Cuban reform process

Between 1972 and 1985 the Cuban economy had experienced a sustained and robust rate of growth (around 6 per cent per year). However, by the mid-1980s there were clear signs of a saturation of the extensive growth model, which to a large extent was copied from the Soviet Union. Thus there were already a series of structural imbalances to deal with by the end of the decade. With the external shocks that subsequently accompanied the political and economic demise of the ‘socialist camp’ and the final dissolution of CMEA (Comecon) at the beginning of the 1990s matters did not look brighter.

For quite some time there was a ‘wait and see’ policy in Havana, apparently with some expectation that the winds would change again, and that the course of events in Eastern Europe, and especially in Russia, could reverse. Cuba had depended up to that point to a large extent on preferential terms of trade (especially sugar exchanged for oil at fixed and favourable prices) and long term credits at low interest. Practically overnight all this changed and the negative impact on all economic variables was severe. Between 1989 and 1993 GDP fell by 33 per cent, private consumption by 30 per cent, and gross investment by 80 per cent. Exports of goods and services fell from almost US$ 6 billion in 1990 to less than US$ 2 billion in 1993. By end of that same year the fiscal deficit amounted to almost one third of GDP, and it became obvious to everyone that a fundamental restructuring of the economy was necessary. This would require not only a series of urgent measures to reverse the macro imbalances, but also structural and institutional reforms to make long term growth sustainable.

Three challenges were facing the Cuban government, all requiring fundamental reforms:

(i) macro stabilisation of the economy, by reducing inflationary pressures (caused by shortages of goods and leading to a soaring black market dollar rate), reducing excess liquidity in the monetary system, addressing the growing external imbalances and shortages of basic goods, and tackling rising disguised unemployment;

(ii) structural reforms not only to make recovery feasible, but also to make high level growth sustainable in the longer run;

(iii) last but not least, the distribution of the social costs as fairly as possible among the population, social equity being one of the fundamental characteristics of the revolution and its raison d'etre.

Central planning based on five year plans was abandoned (making a virtue of necessity since they had been synchronised and conditioned by Cuba's integration into the CMEA trading system) and instead policy decisions were formulated in annual plans in relation to the preparation of the government budget. During the first years of the crisis the annual plans resembled crisis management and ad hoc decision making more than formal plans, and a 'Special Period in Peacetime' ('Período Especial en Tiempo de Paz') was declared, suggesting that the island was now virtually at war. As a matter of fact, during the early 1990s Cuba was preparing for a full scale invasion by the United States, now that protection from the Soviet Union was gone, and considerable effort went into strengthening the defence systems around Havana and other places.

By 1993 two matters were clear: an invasion was not very likely, but the economy was steadily deteriorating and something had to be done about it – at last. During the first three years of crisis, the trade gap diminished dramatically. In 1993 the trade deficit showed a record low of US$ 847 million, but this was achieved as a result of drastic reductions of imports that on the other hand further contracted the economy in a vicious circle. Public expenditures were reduced after 1993 as a result of drastic cuts in subsidies to unprofitable state enterprises (in 1993 amounting to 33 per cent of the budget), curtailing investment and freezing wages. There was a drastic reduction of the state bureaucracy by the elimination of 15 ministries. At the same time state-owned enterprises (SOEs) were to be decentralised and separated from the state budget, and enterprise contributions to the budget would accordingly be made as corporate taxes, rather than as appropriations by the central government. Special taxes were imposed on a number of non-essential goods (primarily liquor and tobacco), a special surcharge on excess consumption of electricity was applied, and bus fares and fees on many other services were raised. In
addition a new income tax was imposed on self-employed, private farmers and co-operatives.³

One of the more controversial measures was the legalisation of possession of foreign exchange holdings in the autumn of 1993. Up to that point many people were hoarding dollars and saving them to trade on the black market. The parallel exchange rate for the peso was soaring, reaching a maximum of 130 pesos to the dollar in mid-1994 (compared to the official exchange rate of 1:1). The main objective behind the legalisation was thus to eliminate the black currency market, as well as to stimulate dollar remittances to relatives in Cuba. These remittances today amount to an annual inflow of between US$ 800–900 million, and the government was, of course, keen to get this money into circulation, rather than have it hoarded. Special dollar shops were opened where Cubans could buy goods (both imported goods and Cuban goods in short supply) with a high sales tax imposed (around 140 per cent). It was made possible for Cubans to open interest-bearing savings accounts in foreign currency. It also became legal to pay in dollars for services offered by other Cubans.

There were immediate positive results from the reforms. The budget deficit disappeared within one year (from a deficit of 33.5 per cent in 1993 to a surplus of 7.4 per cent in 1994) and stabilised at around two to three per cent during the second half of the decade. The parallel exchange rate went down from 78 pesos to the dollar in 1993 to 32 pesos to the dollar in 1995, after having reached a peak of 130 in August 1994. The exchange rate continued to drop in subsequent years to reach a level of 20–22 pesos to the dollar, a level that has been maintained since. As a result inflationary pressures started to disappear after 1995.⁴ The reopening of the mercados agropecuarios in 1994 (originally opened in 1980 but forced to close again in 1984) also contributed to the absorption of the excess liquidity.

Structural changes in the Cuban economy

According to official data⁵ the Cuban economy has been recovering since 1993 at a relatively stable rate of around four per cent per year (Table 1). This is not an especially high rate for an economy in a recovery phase, but compares reasonably well with transition economies in Europe, and

³ In September 1993 a Decree Law was adopted, legalising and regulating 'work on one's own account' in 117 activities. At the same time, about 75 per cent of the land was transferred by decree from the state to a new kind of producer cooperative – Unidades Básicas de Producción Cooperativa (UBPC).

⁴ It should, however, be underlined that inflation in Cuba is to a great extent repressed inflation, since many goods (and until recently no doubt most goods) are not traded on markets determined by supply and demand. Many products are still rationed with fixed prices.

⁵ GDP variables (such as GDP sectors, capital formation and consumption) are recorded in current and constant prices. The latter are 1981 prices, which is problematic since
Table 1. Structural changes in the Cuban economy after 1989 (million pesos; 1981 prices)

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<td>85</td>
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* plus hunting, forestry and fishing,
** plus gas and water,
*** plus communications.
especially with the republics of the Former Soviet Union (FSU). It seems that manufacturing output had almost reached its pre-crisis level by 2000 (with a rate of growth of 6.4 per cent per year since 1993), but it was above all the mining sector (including petroleum, that has been booming) that was successful, with a growth rate of 8.2 per cent in the same period. On the other hand, agriculture lingered behind with a moderate rate of growth of 4.4 per cent per year. The slow growth of the agricultural sector is, of course, to a great extent due to the decline of sugar-cane production.

At first glance there seem to be no major structural changes in the Cuban economy after 1989, in the sense of a break with the pre-crisis trend of reinforcing the 'productive activities'6 sectors at the expense of the 'non-productive' sectors (commerce, transport and communications, and other services). The 'productive sectors' have maintained, and after 1993 even increased their share of GDP, from 45 per cent in 1989 (after a dive to 38 per cent in 1993) to 54 per cent in 2000. The 'non-productive' services have hence seen their share decrease from 55 per cent in 1989 to 46 per cent in 2000. However, this is not the whole picture. Two of the 'productive sectors', agriculture and especially the construction industry, are critically stumbling behind. There are also differences within the 'non-productive' sectors. Commerce has continuously declined as share of GDP since 1989, and so have transport and, to a lesser extent, communications, while services – particularly those related to tourism – have increased.

Coping with the external accounts

Even before the collapse of the trading relations with CMEA Cuba’s current account balance was in very bad shape, amounting in 1989 to some three billion dollars (that is, dollar equivalents, since most of the trade was recorded in convertible Soviet roubles). However, the consecutive current account deficits were covered at that time by accumulating a debt to the socialist allies (primarily the Soviet Union) on generous terms.7 It

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6 In the old accounting system (material balances system) 'productive sectors' were considered to consist of: agriculture, mining, manufacturing, the sugar industry and electricity generation. These series are discussed below.

7 The outstanding debt to the former Soviet Union is now negotiated with Russia. It is still not clear how it will be repaid and on what terms. There are signs that part of the debt will be used for a debt-for-equity deal in nickel mining (Cuba. Country Report. May 2001, Economic Intelligence Unit, London).
Table 2. The Cuban current account and major components, 1989, 1993–2001

<table>
<thead>
<tr>
<th>Year</th>
<th>Trade gap</th>
<th>Factor income gap</th>
<th>Services (net)</th>
<th>Transfer payments (net)</th>
<th>Current account</th>
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<td>−48</td>
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<td>−700</td>
<td>+2,500</td>
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Source: Author's calculations based on the following sources: 1989 data from La economía cubana. Reformas estructurales y desempeño en los noventa (Cepal, Mexico, 2000); 1993–1999 data from various issues of Informe económico (Banco Central de Cuba); data for 2000 from Cuba. Country Report August 2001 (Economic Intelligence Unit, London, 2001).

* Author's estimate based on trends during first semester of 2001.

is thus understandable that the sudden rupture of the trading relations had disastrous effects. The immediate impact was the curbing of imports (especially oil), with a contracting effect on the economy. In the meantime the government looked for alternative export markets and possibilities to substitute imports.

The current account deficit had shrunk considerably by 1993, primarily as a result of the drastic curbing of imports (Table 2). Since 1996, however, the current deficit has grown continuously, although so far not alarmingly. In 2000 it was US$ 687 million, or just about three per cent
of GDP. The deficit has been manageable, so far at least, thanks to a
growing services account (mainly tourism) and the influx of family
remittances (although they seem to have stabilised at around US$ 800
million). The factor income deficit (mainly onerous interests on short-
term credits and to some degree profit remittances) is growing although
not alarming so far.

The continuous increase in the trade gap remains a major cause of
concern. The gap is partially due to a decline of exports since 1996, mainly
as a result of a gloomy sugar industry (with low production and falling
prices). It is, however, also due to rapidly increasing imports that have
more than doubled since 1993. There is historically a strong correlation
between economic growth and imports in Cuba, and with the present
trend it will be increasingly difficult to finance growing imports, unless the
export sector starts to grow. There are limits to how much the tourism
industry and other services can grow, and it is also likely that family
remittances will taper off as a source of hard currency in the future.

The way forward is to rely on the consolidation and expansion of
traditional exports where Cuba enjoys a competitive advantage, like nickel
and tobacco. An additional possibility is to develop new export
products, as Cuba is already doing, for instance in the case of
pharmaceutical and other bio-tech products, although exports so far have
been rather limited.

A conclusion is thus that a sustained high level of economic growth in
Cuba is in the long run dependent on the implementation of a successful
export strategy (although it is recognised that the US government does
whatever it can to put obstacles in its way). In order to develop such a
strategy, many areas of the Cuban economy have to be modernised and

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8 It should be recalled that GDP estimates in US$ are somewhat uncertain in Cuba due
to the unrealistic official exchange rate (parity with the dollar). I have used estimates
made by the Economic Intelligence Unit of London (Cuba. Country Report. August
2001).

9 This dilemma is discussed at length in Claes Brundenius and Pedro Monreal, 'The
Future of the Cuban Model: A Longer View', in Claes Brundenius and John Weeks

10 The situation would no doubt change if family remittances could be used for
investment purposes, such as setting up small businesses on the island.

11 To expand sugar exports is, in my view, not such a good idea. It is rather an example
of so-called immiserised growth. In other words, it is an industry that may yield high
(quantity) growth rates but at prohibitive opportunity costs, since the costs of
production tend to exceed the export price. This does not deny the argument that it
might have been a good idea as long as the preferential trade agreements with the
Soviet Union were in effect.

12 In 1996 exports of pharmaceutical products amounted to a mere 14 million dollars (2.8
per cent of total exports). In 1999 these exports had declined to 52 million dollars
adapted to the requirements of an efficient market economy. Much of the machinery and equipment is obsolete and needs to be upgraded. It is difficult to conceive how this can be done without technology transfer from abroad and/or foreign direct investment (FDI) flows.

The potential role of foreign direct investment and technology transfer

One of the problem areas of the Cuban economy is the low investment rate. It fell from 28 per cent in 1989 of GDP to five per cent in 1993. It has since gradually increased but as of 2000 was only 10 per cent of GDP, which is a very low rate for an economy in a recovery phase. The low level of investment is epitomised by the faltering construction industry (cf. Table 1). One way of increasing the level of investment is to attract foreign direct investment (FDI), and Cuba is seeking to do that.

As a matter of fact, the Cuban government has had a Foreign Investment Law (Decree Law 50) in place since 1982. However, this has not been very successful in attracting investment, and it was only in the 1990s, when Cuba’s desperate need for foreign earnings made it open up on a great scale to international tourism, that foreign investors (especially Spanish tourist chains) started coming to the island. As early as 1992, the Cuban National Assembly amended the Constitution in order to give assurances to potential foreign investors that it was safe to invest in the island. A new article was added to the Constitution recognising ‘the ownership of property by joint ventures, corporations, and associations established in accordance with domestic law’, and another article was modified, clarifying that ‘socialist ownership of production was limited to “fundamental” means of production’. Furthermore, another article was modified to provide for the creation of property rights for the private sector.

These changes were later codified in the Foreign Investment Law (Law 77), enacted by the National Assembly in September 1995. Foreign investors participate in industrial and tourism joint ventures along with the Cuban state as partner, with up to 49 per cent of the firm’s assets being foreign owned. The new law has also opened up the possibility of establishing fully foreign-owned subsidiaries in certain industries, but so far there are very few such fully foreign-owned subsidiaries in Cuba. The

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13 Gross capital formation amounted as late as 2000 only to about 30 per cent of the pre-crisis level. This is a much lower level than in the recovery phases of most transition countries in Europe (with the exception of Russia and the republics of the Former Soviet Union); see Jacek Rostowski, ‘Comparing two great Depressions: 1929–33 to 1989–93’, in Salvatore Zecchini (ed.), Lessons from the Economic Transition. Central and Eastern Europe in the 1990s (OECD, Paris, 1997).

law is quite liberal in the sense that it offers a series of benefits to the foreign investor, although there are also many aspects that might be difficult for foreign investors to accept. Thus, for instance, a foreign company may not, as a rule, buy land (which is leased by the state) for the property in question, and all hiring of personnel has to be undertaken by the state (or the Cuban partner in a joint venture).

Cuba has, nevertheless, managed to attract a considerable amount of FDI to the island, though how much is a controversial issue. Officially it is claimed that more than US$ 2.5 billion have been invested in the island since 1990. Many claim that this is a greatly exaggerated figure but official figures (from balance of payments data) show that net FDI flows between 1993 and 2000 amounted to US$ 1,930 million, which would suggest that the 2.5 billion figure might well be correct. Another question is to what extent the official FDI flows actually reflect ‘greenfield’ investment. As Jorge Pérez-López argues, FDI is a rather ambiguous concept in Cuban accounts. ‘Inversión directa’ usually refers to ‘asociaciones económicas’, but it is not clear to what extent these contracts actually involve capital investment by the foreign partner. For instance, it is not known to what extent ‘management contracts’ and ‘debt for equity swaps’ are included.

By the end of 2000 there were 400 ‘active foreign agreements’ (supposedly involving both joint ventures and management contracts). This was an increase from one in 1988, to 31 in 1993 and 261 in 1997. The most important contracts have so far been in mining, oil exploration, telecommunications and tourism. The investors come primarily from Spain (23 per cent of contracts), Canada (19 per cent), Italy (9 per cent), France (4 per cent), UK (3.5 per cent), and Mexico (3.5 per cent).

After a heated debate in the National Assembly, ‘foreigners’ now also include Cubans living abroad (primarily in the United States). These are, on the other hand, prevented by the US Congress from investing in Cuba, but that is another story.

Workers have to be contracted through a government agency. The company pays the workers’ wages in foreign currency, while the agency pays the workers in pesos. It has been argued that this is a way for the government to confiscate the hard currency (to be set aside for other priorities such as health and education).

With commitments included, the total amount is reported to have reached US$ 5 billion (Cuba. Country Report. May 2001, EIU, London).


However, it is clear that at least debt for equity swaps are considered to be capital in accordance with standard definitions, see World Investment Report 2000, p. 267 (Definitions and Sources), United Nations (New York and Geneva, 2000). There is reportedly only one debt for equity agreement in Cuba. Furthermore, the government has been said to confiscate the hard currency (to be set aside for other priorities such as health and education).

Cuba. Inversiones y negocios. 1998–2000, pp. 42–43 (Havana, 2000). Detailed data (for instance invested amounts cross-classified by country and sector) are not published in Cuba, reportedly as a way to safe-guard company secrets (in order to avoid retaliation
FDI flows increased substantially after 1996, paradoxically after Clinton signed the Helms-Burton Law in March 1996, intended to make it more difficult for foreigners to invest in Cuba. In accordance with the Law, foreign companies can now be sued in US courts if they are found guilty of 'trafficking in US property in Cuba'. This refers to former US properties in Cuba nationalised by the Cuban government in the wake of the revolution. But these threats seem to have had only modest effects on FDI flows, which increased from US$ 82 million in 1996 to US$ 442 million in 1997, although declining to US$ 207 million in 1998, and US$ 178 million in 1999. In 2000, however, FDI flows again increased, to US$ 400 million.

Although it is clear that there have been substantial FDI flows to Cuba during the last decade, it is also clear that they are far from sufficient to compensate for the lack of state investment. An estimate of accumulated FDI flows in the period 1993–2000 gives an amount of US$ of 1.9 billion. Total gross investments in the same period amounted to 13.7 billion pesos (in current prices). Assuming a parity rate of 1:1 (that is the official exchange rate), the FDI share of gross capital formation in the period would thus be around 14 per cent. This is a reasonably high share in comparison to other Latin American countries, but then it should be recalled that the Cuban investment rate is still low, having increased from a mere 6.4 per cent in 1993 to 10.8 per cent in 2000.

The potential role of SMEs

There is a large potential for the growth of small scale and medium sized enterprises (SMEs) in Cuba. The sector could be an important complement for capital formation and innovation and thus contribute to the feasibility of sustained long term growth. Such a sector could also be an important source of employment creation, and an outlet for absorbing surplus labour, laid off from the downsized state sector. The problem is that by the United States). According to estimates by Pérez-López, the total amount of committed/delivered FDI was (as of 2 May 1998) US$ 1,757 million (with an announced total amount of US$ 5,636 million). 34 per cent of the committed amount came according to this estimate from Canada, 28 per cent from Mexico, and 34 per cent from Italy. Surprisingly, Spain had only 6 per cent of the FDI stock according to the source: Pérez-López, Foreign Direct Investment in the Cuban Economy: A Critical Look (manuscript, July 1998).

The problem is that
there is a very small, almost non-existent, base with which to start this process. In Cuba practically all private industry and commerce was nationalised in ‘the revolutionary offensive’ in 1968, making the island one of the most state sector-dominated countries in the world, including the Soviet Union and China (but possibly second to North Korea). As late as 1989, state employment accounted for 94 per cent of total employment. The only (legal) private sector at that time was a small sector of private farmers.

Even in the present reform process there are no plans to encourage private sector development. It is true, however, that there is today an embryonic legal private small-scale sector in Cuba that is growing slowly, especially after 1994, when it was made legal to exercise many professions on an individual self-employed basis \((a\ cuenta\ propia)\). Thus, it is not legal to hire workers, except family members, to assist in some ventures, such as private restaurants \((paladares)\).

However, there is still no significant private sector, in the narrow sense, in Cuba. \(Non\text{-}state\) activities have increased since 1994, but primarily as a result of the transformation of state farms into cooperatives. One measure of the role of the private sector is its share of total employment. Between 1989 and 1999 the private sector grew from 165,000 to 496,000, or from 4.3 per cent to 13 per cent of the labour force.\(^2\) In 1999 most of the private sector consisted of private farmers, while the share of the ‘self-employed’ accounted for a mere 4.1 per cent of total employment. Even the new ‘emerging sector’ encouraged by the government (consisting of new, more independent, state-owned ‘mercantile organisations’ and joint ventures) only made up 4.7 per cent of the labour force in that same year.

The main reason for the slow growth of registered self-employment has no doubt to do with barriers of entry and disincentives to do private business in Cuba. The taxes imposed are prohibitive, discouraging many from continuing with their business.\(^2\) It is clear that the government — at least for the time being — has no plans to encourage private sector development (apart from de facto privatisation of parts of the state-owned industry through joint ventures). There was an opening up of the issue during the discussions in the National Assembly, prior to the adoption of Law 77 in 1995. Several deputies considered it an anomaly that Cubans

\(^2\) La economía cubana. Reformas y desempeño en los noventa, Table A.48 (Cepal, Mexico, 2000); and Anuario Estadístico de Cuba 1999, Table V.1 (Havana, 2000).

\(^2\) For a discussion of this problem and how a new tax system could make the ‘micro-entreprise’ sector contribute more in terms of employment and income generation, increase production at lower costs and prices (and increase tax collection), see Archibald Ritter, ‘The tax regime for micro-enterprises in Cuba’, Cepal Review, (no. 71), August 2000 (Cepal, Santiago de Chile, 2000).
living abroad were welcome as ‘foreign’ investors, while Cubans at home could not invest even in SMEs. For a while the question of the possibility of opening up private SME sector development (on a limited scale) was debated openly, but soon the lid was put on, and the debate was (at least temporarily) closed with the publication of the Resolución Económica adopted at the Fifth Congress of the Communist Party in 1997, which ruled out such a possibility, mainly on ideological grounds.

One could, of course, argue (as is also argued by the government and the party) that recognising the potential dynamism of an SME sector does not necessarily mean that these enterprises have to be private. There have also been attempts to slim down some state enterprises, creating what is presumably intended to be networks, or clusters, of state-owned SMEs as suppliers and back-ups to the larger firms in a new development strategy, using the tourism industry as ‘an engine of growth’ (see further below). At the beginning of the last decade the great majority of workers were employed in SOEs with more than 500 workers. In 1991, out of a total of 818 SOEs, 530 (65 per cent) had a work force exceeding 500, and only ten employed fewer than 100. By 2000, there were 1,157 SOEs, of which 396 (34 per cent) employed more than 500 people, 180 (16 per cent) employed between 25 and 100 people, and 21 (under two per cent) employed fewer than 25 people. The SMEs (defined as those employing fewer than 100 people) are concentrated in the electrical machinery, construction materials and food industries.

Although state owned SMEs thus seem to be growing in number, it is too early to talk about the development of a dynamic SME sector in Cuba. First of all, the number of SMEs is still quite small, and the number employed could be estimated to be less than 20,000 (equivalent to less than three per cent of the manufacturing work force). In addition, it remains to be seen how innovative and dynamic the state-owned SMEs will be.

Social development in the Special Period

Cuba has coped remarkably well with social development during the Special Period. In contrast to most transition economies in Europe (and especially the FSU), many important social indicators have continued to

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25 It is interesting that Fidel Castro, intervening in that debate, proclaimed that there was nothing in the Constitution that prohibited Cubans from investing, but he asked himself ‘how it would be possible for an individual to accumulate so much money’ (Granma Internacional, 25 September, 1995). Castro was thus insinuating that such ‘wealth’ could only have been accumulated in an illicit way, and it was thus a moral question.

26 Based on official data.

improve, and more resemble those of developed market economies than those of developing and transition economies. Thus, in 1999 life expectancy was 75 (73 for men and 77 for women), infant mortality went down from 11.1 per thousand in 1989 to 6.4 per thousand in 1999. Cuba now also has the highest density of medical personnel in the world, with 172 inhabitants per physician (down from 303 in 1989). Social expenditures per capita (in constant prices) fell by over 40 per cent between 1989 and 1993, but have since recovered and in 2000 were at the same level as before the crisis started.  

The social security system is in principle intact, but some services have declined in value. This goes in particular for pensions, whose real value has eroded with the dollarisation of the economy. Retired people, living on pensions alone, have been among the losers during the Special Period. Other losers are the unemployed (although officially registered unemployment is relatively small, at around five per cent), those on sick leave, people working in the ‘peso sector’, and, surprisingly, also many medical personnel and teachers. The winners have so far been people receiving family remittances, people working in (or close to) the tourism industry, private farmers, some (but far from all) self-employed, people working in the new ‘emerging’ sectors, such as joint ventures, and ‘prioritised’ sectors (where workers are paid partly in pesos convertibles) such as energy, telecommunications and biotechnology.

The result of all this is a more unequal society after 1989, as is reflected in income distribution data; but it should be recalled that Cuba was previously an exceptionally equal society, not least by Latin American standards. It has been estimated that while the ‘richer’ segment of the Cuban population (the upper quintile) received 33.8 per cent of income in 1986, the ‘poor’ (the lower quintile) received 11.3 per cent. By 1999 the share of the ‘rich’ had increased to 58.1 per cent, while the share of the ‘poor’ decreased to 4.3 per cent. The Gini coefficient in the same period increased from 0.22 to 0.41.  

If the trend continues, income distribution in Cuba will increasingly resemble that of the rest of Latin America. This is no doubt one of the most complicated issues to tackle: how to reduce inequalities, maintaining social safety nets (and thus preserve the legitimacy of the revolution, and hence the government), while at the same time facing the daunting task of getting the macroeconomic balances in order, and formulating policies and strategies that might lead to a sustainable, high level growth trajectory in the long run.

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29 Ibid.
One of the systemic problems with the Cuban growth model before 1989 was that, like other socialist models of accumulation, it had been based on so-called extensive growth. This means that growth was mainly determined by the proportional growth of factor inputs. There was little room in the model for endogenous innovation and technological change, that would allow a more efficient use of the factors of production. Extensive growth has thus been coupled with slow productivity growth. During the second half of the 1980s labour productivity was even negative (−3.9 per cent), which illustrates the saturation of the extensive model.\(^{30}\)

Switching to an intensive growth model\(^{31}\) thus became a necessity for Cuba even before the real crisis set in at the beginning of the last decade. The crisis might provide an excellent opportunity to switch gear in the search for a more dynamic, intensive growth mode, and ‘sustained productivity growth requires that an economy continually upgrade itself’.\(^{32}\)

The industrial park in Cuba is old and obsolete and accelerated growth is dependent on increasing investment in new plant, machinery and equipment, and increased productivity. Increased productivity can only be achieved through technological upgrading, innovation and the efficient use of a highly skilled labour force. In Cuba, the inflow of FDI is considered to be an important means in this endeavour, although not as an alternative but rather as a complement to domestic capital accumulation.

In the Cuban context industrial upgrading primarily means technological upgrading, including the accommodation of new organisational learning. For Gary Gereffi ‘industrial upgrading involves organisational learning to improve positions of firms or nations in international trade and production networks’.\(^{33}\) Furthermore, ‘participation in global commodity networks is a necessary step for industrial upgrading because it puts firms and


\(^{33}\) Gary Gereffi, ‘Industrial Upgrading in the Apparel Commodity Chain: What can Mexico Learn from East Asia?’, paper presented at the international conference on Business Transformation and Social Change in East Asia (Taichung, Taiwan, 1999). Industrial upgrading can also be viewed as a government strategy to support technological upgrading of hi-tech industries, see, \(\mapsto\) Chiung-Wen Hsu and Hsueh-Chiao Chiang, ‘The government strategy for the upgrading of industrial technology in Taiwan’, Technovation, 21 (2001).
economies on potentially dynamic learning curves’. This is no doubt also part of the Cuban upgrading strategy (and the case of nickel discussed below is a case in point), but the Cuban strategy is much more complex than that. It also consists of technological upgrading of local industries that are primarily producing goods for the local market, a kind of ‘import substitution policy revisited’. The strategy consists, inter alia, of using the dollar sectors of economy (special shops and the tourism sector) as incentives for upgrading local supplier industries, since the latter have to compete with imports. To some extent this policy has been successful: sales by local suppliers in the dollar economy have steadily increased since the legalisation of hard currency holding, increasing from 25 per cent of total sales in 1996 to 61 per cent in 2000. The question remains whether these gains are the result of successful upgrading, or rather (or at least to some extent) the result of explicit import substitution policies (tariff and non-tariff barriers).

Industrial upgrading in Cuba as a rule takes place in association with a foreign partner, either in joint ventures, management contracts, risk contracts or other arrangements. Mining, oil exploration and telecommunications are examples, but upgrading in association with foreign partners is also the rule in many of the industries supplying goods to the tourism industry, as mentioned above.

**Mining**

Linking up to global commodity networks is also part of the Cuban strategy, and nickel mining is a case in point, and an apparent success story. Cuba possesses important reserves of non-ferrous minerals, nickel plus cobalt reserves being the largest in the world. The potential for developing an important export industry based on minerals is thus great. The United States is, of course, the largest potential importer but this market has been closed because of the US embargo. A large part of the nickel deposits are located at Moa in the north eastern part of Cuba. The near-by processing plant was built by the US-based Freeport Sulphur Company in 1958 but was nationalised just after the revolution. The Moa plant was run until the beginning of the 1990s by the Cuban state with technical support from the Soviet Union, which was also the destination of practically all its output.

After the Soviet collapse, the future of the Cuban nickel industry was uncertain to say the least. By 1991 the old plant was running at just 54 per cent capacity, and Cuba was desperately looking for a new market for its nickel production, and above all for a partner willing to assist with

technological upgrading of the facilities. Luckily there was a company in Canada looking for nickel feed for its processing plant, and possessing substantial financial and technical resources. In 1992 a cooperation started with Sherritt International of Canada, leading in 1994 to the formation of a 50-50 joint venture that could serve as a model for other developing countries.

The joint venture agreement was signed between Sherritt and the Cuban SOE Compañía General de Níquel S.A., resulting in three jointly owned subsidiaries: (1) a mine with a processing plant in Moa; (2) a refinery plant in Alberta, Canada; and (3) a sales and marketing company in the Bahamas. This has meant not only technological (and environmental) upgrading of the facilities in Cuba, but also a Cuban share in refining capacity, and not least access to nickel markets outside the United States. Since 1994 the Moa plant has doubled its output thanks to modernisation carried out jointly with Sherritt. Most of the plant managers are Cuban (trained in modern management techniques), and 30 other Cuban professionals are based at the Alberta plant in Canada. One of the problems for Sherritt is that the deal falls under so-called ‘trafficking with US-owned property’ under the Helms-Burton Law. The company is under constant threat of being sued in US courts, and the executives of the company (and their families) are not allowed into the United States. But, instead of giving in to US pressures, Sherritt is expanding its activities in Cuba, moving into new areas, such as petroleum and gas, telecommunications and tourism, and making the company by far the largest investor in Cuba.

**Petroleum and gas**

Cuba was until the 1990s almost entirely dependent on oil deliveries from the Soviet Union, receiving some 13 million tons annually at preferential prices. The cut in oil supplies from the old allies was the most important reason for the virtual collapse of the economy between 1991 and 1993. However, Cuba shares the Mexican Gulf with Mexico and the United States, and the Gulf is recognised as having the world’s largest oil reserves. So Cuba has great hopes of getting a share of this wealth. Since the beginning of the 1990s companies from Brazil, Canada, France, Great Britain and Sweden have signed exploration and production agreements with the Cuban government. The operations are based on risk contracts running for 30 years with an initial prospecting period of no less than six years. In 2000 the foreign assets in the oil processing were estimated at

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more than US$ 600 million, or about 25 per cent of the estimated FDI stock in the island.37

The results so far have exceeded expectations. In 2000 Cuba produced 2.8 million tons of crude oil from its off-shore deposits (compared to 527 thousand tons in 1991) and production is expected to reach 6 million tons by 2005. The association with foreign partners has led to the introduction of modern methods of production with the latest available technologies, implying higher efficiency in a series of areas. Most important in this context are technologies that have made it possible to use the associated gas in heavy oil extraction for the generation of electricity and for domestic consumption. The use of associated gas has increased from practically zero until 1997 to 550 million cubic meters in 2000, and is expected to reach 1,385 million cubic meters by 2005. Even more important than the actual use itself for domestic purposes, is the salutary effect it has on the environment (Pérez 2002). Before the introduction of the new technology (through the company Energas, a joint venture between Sherritt and the Cuban state), the gas went straight up into the atmosphere, polluting the coastal areas north of Havana and Matanzas, where the beach resort Varadero is located.

*Telecommunications*

The Cuban telecom network was until recently in very bad shape and much still remains to be done (such as the installation of many more new lines). In 1994 a new company was born, ETECSA, a joint venture between the Cuban telephone company (51 per cent) and CITEL of Mexico (49 per cent). The agreement involved an investment of more than US$ 1.5 billion with a 55-year concession, and with a commitment of US$ 740 million in the first seven years for the modernisation of the telecom network.38 This has been a very profitable investment. But even so, CITEL opted to withdraw gradually from the deal by selling its shares to the Italian telephone company STET (first selling 25 per cent of its shares in 1995, and then the rest in 1997). This came as a surprise to many, but no doubt had to do with the Helms-Burton bill becoming a law in 1996, scaring away many investors from ‘trafficking in US-owned property’ (the Cuban telephone company was owned by ITT before the revolution). The ETECSA joint venture has without any doubt been very beneficial for the Cubans, although tariffs have increased considerably. It has resulted in modern digital switching boards, microwave installations, the use of fibre optics and also the introduction of up to date customer services.39

38 Everleny Pérez, ‘La inversión extranjera directa en Cuba’.
39 Ibid.
Table 3. Indicators for the Cuban tourism industry, 1990–2000

<table>
<thead>
<tr>
<th>Year</th>
<th>Tourists (thousands)</th>
<th>Rooms (thousands)</th>
<th>Gross Income (US$ million)</th>
<th>Income/tourist (US$)</th>
<th>Local sales*** (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>1,774</td>
<td>34.7</td>
<td>1,948</td>
<td>1,098</td>
<td>61</td>
</tr>
<tr>
<td>1999</td>
<td>1,603</td>
<td>32.3</td>
<td>1,901</td>
<td>1,186</td>
<td>53</td>
</tr>
<tr>
<td>1998</td>
<td>1,416</td>
<td>30.9</td>
<td>1,759</td>
<td>1,242</td>
<td>49</td>
</tr>
<tr>
<td>1997</td>
<td>1,170</td>
<td>27.4</td>
<td>1,515</td>
<td>1,295</td>
<td>*</td>
</tr>
<tr>
<td>1996</td>
<td>1,004</td>
<td>26.9</td>
<td>1,333</td>
<td>1,328</td>
<td>*</td>
</tr>
<tr>
<td>1995</td>
<td>746</td>
<td>24.2</td>
<td>1,100</td>
<td>1,475</td>
<td>*</td>
</tr>
<tr>
<td>1994</td>
<td>619</td>
<td>23.3</td>
<td>850</td>
<td>1,373</td>
<td>*</td>
</tr>
<tr>
<td>1993</td>
<td>546</td>
<td>22.1</td>
<td>720</td>
<td>1,319</td>
<td>*</td>
</tr>
<tr>
<td>1992</td>
<td>461</td>
<td>18.7</td>
<td>550</td>
<td>1,193</td>
<td>*</td>
</tr>
<tr>
<td>1991</td>
<td>424</td>
<td>16.6</td>
<td>402</td>
<td>948</td>
<td>*</td>
</tr>
<tr>
<td>1990</td>
<td>370</td>
<td>12.9</td>
<td>243</td>
<td>715</td>
<td>12**</td>
</tr>
</tbody>
</table>

Sources: Anuario Estadístico de Cuba 2000; Figueras 2001; García and Pérez 2001 and data supplied by the Ministry of Economy and Planning.

* no available data,
** estimate based on Figueras (2001),
*** share of local industry in sales to tourism sector.

Tourism as an engine of growth in a new development strategy

From the examples so far it is clear that, through technology transfer in association with foreign partners, there has been an important economic and technological upgrading in crucial sectors of the Cuban economy. However, it is not clear to what extent this has been part of an overall strategy of economic upgrading as a means of connecting to the global economy.

The Cuban development strategy, although not explicit, seems to focus on using the buoyant tourism industry as an engine of growth (‘una locomotora de desarrollo’). Such a strategy is aimed at both upgrading local industry and at substituting imports. Why tourism? First of all tourism is an industry that, if unregulated, tends to require huge amounts of imports, and where there hence should be many import substitution possibilities, enabling the restructuring and upgrading of the local industry. Secondly, tourism is considered to be an area where Cuba should have clear comparative advantages (‘sun, sand and salsa’).

The tourism industry has no doubt been a success so far in Cuba. The number of foreign visitors to the island increased from 370,000 in 1990 to 1.8 million in 2000 (Table 3). In terms of income tourism is today by far the biggest money-maker in the Cuban economy, and its contribution to the balance of payments increased from 4 per cent in 1990 to 43 per cent in 2000. Gross income from tourism was estimated in 1999 to be about

40 See Miguel Figueras, ‘El turismo internacional y la formación de clusters productivos en la economía cubana’, paper presented to XXIII LASA Congress, 6–8 September, 2001 (Washington, DC).
2 billion dollars, compared to a total of 1.5 billion dollars from exports of goods (primarily sugar and nickel) in that same year.

Gross investments in the tourism industry accounted for almost 20 per cent of all gross investments in Cuba during the 1990s. The number employed in the sector is estimated to be between 100,000 and 150,000 (depending on accounting methods) and some additional 200,000 are estimated to work indirectly for the tourism industry. Another study, based on input-output analysis (especially adapted for analysis of the linkage effects from tourism) indicates that 100 new jobs in the tourism sector create 138 additional jobs in firms that deliver goods and services to hotels, catering and entertainment.

At the beginning of the crisis the development of international tourism was seen as no more than a temporary solution to the growing hard currency gap in the external accounts, which together with a series of other alarming macroeconomic imbalances led to the declaration of the Special Period. However, it is now clear that tourism is more and more seen as having a key role in a long-term development strategy. The tourism industry has linkage effects to many sectors in the Cuban economy, and by substituting imports many plants have been upgraded and modernised. New and more efficient production and management systems have been put in place, often in collaboration with foreign partners, as a rule as joint ventures. The upgraded companies supply goods not only to the tourism sector as such but also to the so-called dollar shops (TRDs), where most of the customers are Cubans with access to dollars.

It appears that this strategy succeeded. According to official data, the domestic share of deliveries to the tourism industry increased from 12 per cent in 1990 to 61 per cent in 2000, and national participation in the sales of the TRDs increased from 29 per cent in 1996 to 51 per cent in 2000 (Table 3). These shares look impressive, especially as they have increased over such a short period, but it is not clear how they are calculated. For instance, it is unclear whether imports of raw materials to the local industries are deducted.

The most important manufacturing sector being upgraded in this way is the food and beverages industry, in which there were sixteen joint ventures by 2000. In 1996 a company, Coralsa, was created to be a partner in joint ventures and other types of technology transfer with foreign

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41 Ibid.
42 A. García and M. Pérez Mok, ‘La importancia del turismo en el desarrollo futuro del la economía cubana’, paper presented to XXIII LASA Congress, 6–8 September, 2001, Washington DC.
43 Figueras, ‘El turismo internacional y la formación de clusters productivos en la economía cubana’.
companies, in order to find markets, technology and financing for the upgrading of the food and beverages industry.\textsuperscript{44} Most of the upgraded local industries are primarily oriented towards the domestic market (the tourism sector and the TRDs), but they are also looking towards new export markets (especially in the Caribbean and Mercosur).

In some fields Cuban products are, of course, already highly rated on the international market. This goes for instance for rum and tobacco. Havana Club International is a joint venture with the French company Pernod Ricard. Production of Havana Club has increased five-fold since the creation of the joint venture in 1994 – before the crisis Cuban rum was mainly exported to the socialist countries. Havana cigars are another example of successful export promotion in association with a foreign partner.

Using tourism as an ‘engine of growth’, as a springboard for upgrading local industries, by substituting imports to begin with but with the longer view of making some products competitive on the international market, could turn to be a clever strategy in the Cuban context. However, there are many pitfalls. Focusing on tourism as a key in a new development strategy is not just a question of capturing larger shares of deliveries of goods and services to the tourism industry in a narrow sense. Most of the segments in a typical tourist package to Cuba (or any other tourist package for that matter) are appropriated by other ‘players’, outside Cuba. It has been estimated\textsuperscript{45} that out of the total spending by a typical tourist on a package tour to Cuba, the tour operators get 20 per cent, and the airlines 40 per cent, and the remaining 40 per cent is spent in Cuba (equivalent to ‘gross income’ in Table 3). The big winners seem to be the tour operators, and the problem is that they can decide to shift destinations at short notice. They very seldom make long term commitments. The decisions are probably rational from their own point of view, although they seem irrational and sometimes turn out to be disastrous for the destinations abandoned. Even so, it is possible to capture new segments of the business. The national airline (in this case Cubana de Aviación) can try to compete with the international airlines, and the national tourist agency can try to compete with the big tour operators. But that is an uphill, costly and risky competition.

The big risk involved in relying so much on tourism in a development strategy is thus the tourists themselves, that is, that their numbers might stagnate, or even decrease. The number of tourists might, of course, dramatically increase if (when) the US embargo is lifted, but could also

\textsuperscript{44} Everleny Pérez, ‘La inversión extranjera directa en Cuba’.

\textsuperscript{45} Estimates provided by Miguel Figueras, adviser to the Cuban Ministry of Tourism (Mintur).
Table 4. Cuban industrial indices in 1981 and 1995 prices (1989 = 100)

<table>
<thead>
<tr>
<th></th>
<th>1981 prices</th>
<th>1995 prices</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>All industry</td>
<td>Manufacturing</td>
</tr>
<tr>
<td>1989</td>
<td>100.0</td>
<td>100.0</td>
</tr>
<tr>
<td>1990</td>
<td>95.0</td>
<td>95.0</td>
</tr>
<tr>
<td>1991</td>
<td>86.2</td>
<td>85.9</td>
</tr>
<tr>
<td>1992</td>
<td>73.2</td>
<td>71.8</td>
</tr>
<tr>
<td>1993</td>
<td>64.7</td>
<td>63.5</td>
</tr>
<tr>
<td>1994</td>
<td>69.4</td>
<td>68.4</td>
</tr>
<tr>
<td>1995</td>
<td>74.9</td>
<td>72.8</td>
</tr>
<tr>
<td>1996</td>
<td>80.8</td>
<td>78.1</td>
</tr>
<tr>
<td>1997</td>
<td>87.1</td>
<td>83.0</td>
</tr>
<tr>
<td>1998</td>
<td>89.7</td>
<td>87.8</td>
</tr>
<tr>
<td>1999</td>
<td>91.4</td>
<td>94.0</td>
</tr>
<tr>
<td>2000</td>
<td>100.2</td>
<td>98.1</td>
</tr>
</tbody>
</table>

Source: Elaborated on the basis of data in Anuario Estadistico de Cuba 1996 & 1999; plus updates based on official data.

Fig. 2. Cuban Industrial Indices, 1989–2000, in 1981 and 1995 prices (1989 = 100).

stagnate or decline as a result of unexpected international events, such as the terrorist attacks in the United States on 11 September 2001.

The puzzling industrial sector – how fast is it actually recovering?

The Cuban manufacturing industry is in great need of economic and technological upgrading as discussed above, and it also seems that industrial activities are recovering. The question is, however, how fast? As mentioned before (note 4), one problem with Cuban macroeconomic statistics is that many variables are accounted for in constant 1981 prices, in addition to current prices, which might give a distorted picture of reality. This is, for instance, the case with industrial growth figures. The series commonly used suggest that manufacturing and industrial activities (including mining, electricity and the sugar industry) had recovered their pre-crisis levels by 2000 (Table 4 and Figure 2).
However, if a new series, using 1995 prices, is applied, manufacturing and industrial activities are far from recovery. By 2000 industrial activities had only recovered 54 per cent of the 1989 level, and industrial activities 47 per cent of that same level. The main reason for this stark contrast between the two series is that the trough is much deeper when measured in 1995 prices, with manufacturing falling to a low of 32 per cent (1993), compared to 64 per cent if measured in 1981 prices – a difference of more than 30 percentage points. The differences are also remarkable, although not so great, in the recovery phase, with a manufacturing sector growth rate of 5.2 per cent per year between 1993 and 2000 at 1995 prices, compared to 6.4 per cent at 1981 prices.

Now, one could argue that these differences do not mean very much, since recovery is not just a question of quantitative growth rates but rather of quality and contents. Even if Cuba in fact had recovered its pre-crisis industrial level in 2000, this does not mean that situation is the same as in 1989. The structure of the industry is quite different. Many obsolete industries are gone, while others have been economically and technologically upgraded. For this reason it is not a good idea to use 1981 prices that tend to overvalue old and obsolete industries and technologies.

Based on 1995 prices it is now possible to estimate structural changes in the Cuban industry after 1998 (Table 5 and Figure 3). The data show that the sugar industry is maintaining its relative strength in spite of a fall of almost half in real terms. Consumer goods are also maintaining their relative share, while the share of intermediate goods is increasing. The most dramatic change is seen in the capital goods industry which has practically disappeared, falling to a level of only 15 per cent in 2000 in relation to 1989. This followed an important development of the capital goods industry in the 1980s, especially focused on supplying machinery and equipment to agriculture (especially the sugar industry).46

Cuba and the transition debate ten years after

Cuba has gone through a difficult ‘special period’ since the demise of communism in Europe and the Soviet Union. It started with a deep depression, followed by moderate reforms with moderate recovery growth. The island is confronted with the daunting task of adapting to a new international context, with opportunities and challenges, but also with many obstacles on the road. Although one could argue that Cuba has managed the crisis surprisingly well, it is not clear (so far), where the

Table 5. Structural changes in the Cuban industry after 1989 (1995 prices)

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td></td>
<td>Pesos (m)</td>
<td>per cent</td>
<td>Pesos (m)</td>
<td>per cent</td>
<td>Pesos (m)</td>
</tr>
<tr>
<td>Sugar Industry</td>
<td>1,932</td>
<td>16.5</td>
<td>1,078</td>
<td>23.5</td>
<td>1,092</td>
</tr>
<tr>
<td>Consumer Goods</td>
<td>4,189</td>
<td>35.8</td>
<td>1,655</td>
<td>36.1</td>
<td>1,954</td>
</tr>
<tr>
<td>Intermediate Goods</td>
<td>4,349</td>
<td>37.1</td>
<td>1,720</td>
<td>37.6</td>
<td>2,402</td>
</tr>
<tr>
<td>Capital Goods</td>
<td>1,244</td>
<td>10.6</td>
<td>127</td>
<td>2.8</td>
<td>198</td>
</tr>
<tr>
<td>TOTAL</td>
<td>11,714</td>
<td>100.0</td>
<td>4,580</td>
<td>100.0</td>
<td>5,646</td>
</tr>
</tbody>
</table>

**Source:** Derived from data in *Anuario Estadistico de Cuba 1999* (Table VIII.4) and updates based on official data. The benchmark for the series is the sector breakdown in 1989 in 1993 prices.
Whither the Cuban Economy after Recovery

Fig. 3. Structural changes in the Cuban industry after 1989 (million 1995 pesos).

Table 6. Recession/depression and recovery in Cuba and in transition economies: GDP levels in 1993 (or latest trough) and 2000 and annual rates of change

<table>
<thead>
<tr>
<th>Country</th>
<th>Level in 1993 or at trough (year)</th>
<th>Level in 2000 (1989 = 100)</th>
<th>Annual rate of GDP change during recession</th>
<th>Annual rate of GDP growth during recovery</th>
</tr>
</thead>
<tbody>
<tr>
<td>Poland</td>
<td>82 (1991)</td>
<td>128</td>
<td>-9.5</td>
<td>5.1</td>
</tr>
<tr>
<td>Slovenia</td>
<td>82 (1992)</td>
<td>114</td>
<td>-6.4</td>
<td>4.2</td>
</tr>
<tr>
<td>Hungary</td>
<td>82</td>
<td>105</td>
<td>-4.8</td>
<td>3.6</td>
</tr>
<tr>
<td>Slovakia</td>
<td>73</td>
<td>104</td>
<td>-6.9</td>
<td>4.8</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>85 (1992)</td>
<td>97</td>
<td>-5.3</td>
<td>1.7</td>
</tr>
<tr>
<td>Cuba</td>
<td>63</td>
<td>85</td>
<td>-10.2</td>
<td>3.9</td>
</tr>
<tr>
<td>Belarus</td>
<td>61 (1995)</td>
<td>83</td>
<td>-7.5</td>
<td>5.7</td>
</tr>
<tr>
<td>Estonia</td>
<td>61 (1994)</td>
<td>80</td>
<td>-9.4</td>
<td>4.6</td>
</tr>
<tr>
<td>Romania</td>
<td>75 (1992)</td>
<td>75</td>
<td>-9.1</td>
<td>0.0</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>73</td>
<td>71</td>
<td>-7.6</td>
<td>-0.4</td>
</tr>
<tr>
<td>Lithuania</td>
<td>53 (1994)</td>
<td>64</td>
<td>-11.9</td>
<td>3.1</td>
</tr>
<tr>
<td>Latvia</td>
<td>51</td>
<td>61</td>
<td>-15.5</td>
<td>2.6</td>
</tr>
<tr>
<td>Russia</td>
<td>53 (1996)</td>
<td>60</td>
<td>-8.9</td>
<td>3.1</td>
</tr>
<tr>
<td>Ukraine</td>
<td>36 (1999)</td>
<td>38</td>
<td>-9.7</td>
<td>4.0</td>
</tr>
</tbody>
</table>


A first look at some macroeconomic data indicates that Cuba has fared relatively well in comparison with transition economies in Europe and the

economic system is heading, and to what extent one can talk of a systemic change. But how has Cuba fared in comparison with transition economies in Europe and the FSU, and what can be said about the Cuban reforms in the context of the transition debate ten years after?

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FSU, at least as far as economic recovery is concerned (Table 6). The Cuban GDP recovery level stood in 2000 at 85 per cent (in relation to 1989). This is far below Poland and also the more successful transition economies in Eastern Europe, but ahead of countries like Bulgaria and Rumania, and much ahead of all the republics of the former Soviet Union, including the Baltic republics (with the exception of Estonia).

The country experiences are quite different, however. Some had a rather short, but deep recession, with subsequent slow recovery growth, and others had a protracted recession (even depression), with rapid recovery growth, while yet others had protracted depression with slow recovery (most FSU republics, and with Ukraine as one of the worst examples).

However, there are no clear patterns, suggesting, for instance, that countries with deep but short recessions have higher growth rates in the recovery period, or that countries with a protracted, but not so deep, recession are compensated by higher growth rates in the recovery stage. One could argue, however, that Poland stands out as a successful case of shock therapy with a deep but short lived recession, followed by a quick recovery with reasonably high and sustained growth. János Kornai argues that ‘shock therapy’ is a necessary means in order to prevent the prolonged recession to be expected after price liberalisation and drastic budget cuts. Thus, a deep and short recession is much to be preferred to a modest but prolonged recession. The problem is that if there is no institutional system to back up the macro reforms, then the result might be the worst of scenarios, a deep and protracted depression like in Russia (with the Gaidar 1992 reform package as a case in point). On the other hand, Hungary has managed better with a gradual approach than the Czech Republic has with shock therapy and voucher privatisation, so there are no clear-cut conclusions. What does seem to be the case,

47 The comparison here relates to macroeconomic data. A comparison of social indicators in the 1990s places Cuba as a top performer, especially compared to the republics of the Former Soviet Union (see, for example, Brundenius and Weeks (eds.), Globalization and Third World Socialism, and Milanovic, Income, Inequality and Poverty.

48 But there are former Soviet Republics that have fared even worse than Ukraine. Thus, GDP in Armenia fell by 69 per cent between 1989 and 1993; in Azerbaijan by 63 per cent (between 1989 and 1995); Georgia by 74 per cent (between 1989 and 1991); Kazakhstan by 51 per cent (between 1989 and 1995); Moldavia by 65 per cent (between 1989 and 1996); Tajikistan by 38 per cent (between 1989 and 1991).

49 In Poland GDP fell by 11.6 per cent in 1990, and by 7.0 per cent in 1991, but the growth rate turned positive (2.6 per cent) in 1992.

however, is that countries that were less dependent on trade with the Soviet Union (like Poland) have come out of the recession faster than the others. Another conclusion is that it is much easier to carry out radical reforms during an economic upswing than during a recession/depression phase, when certain type of reforms might actually contribute to the further contraction of the economy, and thus deepen the crisis.

The question of property rights

Quite a few scholars are having second thoughts about the transition, and the roadmap to follow from a centrally planned economy to a market economy. The criticism concerns primarily the sequencing and timing of the reforms in the Eastern Europe and the FSU (and it is primarily Russia that is discussed). As a contrast, China is heralded as a both prudent and wise reformer, both in terms of sequencing and timing (what has been termed 'gradualism' in contrast to 'shock therapy', or 'big bang'). There are, of course, also dissident opinions in the debate, primarily from those who advocated 'big bang' reforms in Russia, claiming that the reforms were half-hearted.

Janos Kornai's overall concern is with ownership reform and property rights. He says it is understandable that many reformers in Eastern Europe and Russia wanted to introduce a private sector as quickly as possible, in order 'to seize the opportunity to make a communist return impossible'. The argument in Russia was therefore that 'if the window of opportunity opens for privatization, the opportunity has to be seized and privatization carried out rapidly' and it has to be done 'while the state bureaucracy is still in a confused, weak state and unable to resist'. Accordingly, it was thought that the quickest way to get a systemic change with predominance of private ownership in Russia was to privatise the whole of state-owned industry, especially the most lucrative raw materials branches, through a 'mass privatisation' scheme.

But the Russian strategy turned out proved to be disaster for the country:

A voucher system (was) imposed on the country, coupled with mass manipulated transfers of property in the hands of management and privileged bureaucrats


Kornai, Ten Years After, p. 18.
(and) in this environment a historically unprecedented ‘ownership reform’ occurred, one in which the ownership of natural resources, especially oil and gas, was expropriated by the oligarchs.54

Reddaway describes this attempt to implant a market economy from above as ‘market bolshevism’, resulting in ‘a rather small number of bankers and businessmen acquiring valuable state assets at little or no cost and then being allowed to plunder the state treasury at little or no cost in partnership with ministers and bureaucrats’.55

The Chinese and Vietnamese roads

It is understandable that Cuban leaders see the Russian case as a negative example (one which they often refer to) and instead look further east, to China and Vietnam. They could get support in this view from Joseph Stiglitz, the former chief economist at the World Bank, who brings the contrasts between the Russian and the Chinese experience into full relief. While Chinese GDP nearly doubled during the last decade, Russia’s GDP almost halved. At the same time ‘Russia had succeeded in “privatising” much of its industry and natural resources, but the level of gross fixed investment – a far more important sign of a burgeoning market economy – has fallen dramatically over the last five years ... Russia was fast becoming an extractive economy, rather than a modern industrial economy’.56

In contrast the gradualist Chinese reform process has undoubtedly been a success. It has been a process in two stages. During the period 1979–93 the emphasis was on decentralisation of much decision-making to the regional level, the expansion of non-state enterprises, the creation of financial stability through financial dualism, and the dual-track approach to price liberalisation. It was only during the second stage, which started about 14 years after the initial reform process, that the emphasis was switched to establishing ‘a rule-based market system’:

In the five years between 1994 and 1998, China unified the foreign exchange system and made its current account, overhauled the tax system and fiscal systems, centralized the central bank, downsized the government bureaucracy and forced the military to give up its commercial operations, and started privatizing state-owned enterprises and laying off their workers.57

54 Ibid., p. 12. 55 Reddaway, Market Bolshevism Harmed Russia.
Could Cuba learn from the Chinese experience? Cuban leaders have occasionally lauded the Chinese and Vietnamese strategies, but officially Cuba rejects following new ‘models’. Nevertheless there are interesting coincidences: China’s initially cautious attitude to price reform and devaluation, resistance to privatisation of SOEs, the slow restructuring of SOEs, and the lagging behind of financial and banking reform, are to some extent reminiscent of the hesitant Cuban reforms in the 1990s. In addition, Cuba like China wants a regulated market economy that is compatible with equity and social development. Chinese leaders refer to their system as ‘a market economy with Chinese characteristics’. Perhaps there could be a case for a Cuban market economy with ‘Cuban characteristics’?

Pérez-López wrote in 1995 that ‘Cuba is coveting Beijing, but imitating Moscow’. This might sound surprising in consideration of what we know about Cuban resentment towards the reform process in Russia. However, Pérez-López refers to the reforms under the Perestroika era during Gorbachev. He mentions the similarities, for example, between Cuba’s law on the exercise of own-account work (‘a cuenta propia’) and the Soviet law on Individual Labour Activity of 1987. There are also similarities with respect to SOE reform, the laws on cooperatives, and decentralisation of foreign trade.

The most sensitive issue in the Cuban context is privatisation and private sector development. But as Joseph Stiglitz argues, ‘China has shown that a successful market reform can proceed without privatization, without even clearly defining property rights’. On the other hand the Chinese have put a lot of emphasis on competition. In China the existing SOEs have declined in importance, not as result of privatisation but as a result of the expansion of new private enterprises.

Cuba could learn a great deal from private sector experiences in both China and Vietnam. Vietnam has also followed step by step reforms towards market economy, although more cautiously than China. This is especially the case with government policies in dealing with the embryonic private sector. Although many small SOEs have been ‘equitised’, there is still much to be done about ‘levelling the playing field’ for the small but

58 Thus, José-Luis Rodríguez, Minister of Economy and Planning, told the World Economic Forum in Davos (February 1996), that ‘taking into account the positive experiences from other countries like China and Vietnam, we avoided a sudden devaluation. This would have added terrible social consequences to the already difficult economic crisis faced by the country’.


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growing private sector, for instance to make it easier for them to get access to credits and bank loans.

However, the larger part of the Vietnamese private sector consists of household micro-enterprises, operating at very small scale and with simple technologies. The ‘modern’ private sector, consisting of domestic liability and joint stock companies, contributes just over two per cent to manufacturing value added, and less than one per cent to GDP. This could be compared with the ‘foreign invested’ sector, which accounts for one third of manufacturing output. There are thus many similarities between Cuba and Vietnam in this respect. Both countries rely to an increasing extent on FDI flows for capital formation and technological upgrading, while private sector development is lagging behind. However, in contrast to Cuba there is today a commitment to the development of a mixed economy (with a sizeable private sector) in Vietnam, reconfirmed at the Ninth Party Congress in the spring of 2001. This is a process that Cuba no doubt could learn from.

Concluding remarks

It could be claimed that Cuba has fared surprisingly well in dealing with its macroeconomic balances, especially in view of the disastrous situation of the economy in the aftermath of the collapse of its former allies, on which 80 per cent of the external accounts depended. Emily Morris of the Economist Intelligence Unit goes so far as to talk about a ‘Cuban economic miracle’ (although admitting that this might sound like a bad joke to many Cubans). She justifies this claim, saying that ‘the description [of Cuba as an economic miracle] is valid, if a miracle is something positive that happens that we cannot explain using our standard tools of analysis’. Morris says, and this is no doubt correct, that few analysts (irrespective of ideological preferences) who were closely watching the Cuban economy at the beginning of the 1990s expected an economic recovery at all in Cuba, especially, in view of the unprecedented external shock waves that were sent to the island as a result of the overnight disappearance of former trading partners. Thus, Morris argues that the outcome of unorthodox Cuban policies ‘has been very much better than we expected’.

But if Cuba has managed the crisis comparatively well, the question of

62 Ibid.
what kind of system is lying ahead still remains. Some in Cuba talk about a system that would also accommodate the development of a small private sector 'on the side',⁶⁴ that would not only be tolerated but also encouraged (as in China today), and that would be part of a 'socialist market economy', as currently discussed in China.⁶⁵ So perhaps one may after all hope for a 'market economy with Cuban characteristics', or 'a market economy with a human face', although there are many sceptics.⁶⁶


⁶⁶ Kornai, for instance, is sceptical about the development of a 'socialist market economy', claiming that there is no 'third way'. He bases his judgement on the experiences of the reforms in Hungary in the 1980s exactly in that direction, claiming that it simply did not work. Capitalism was the mode of production that emerged and expanded in the 19th and 20th centuries, and socialism was just a brief parenthesis. Even Nordic welfare systems are just a branch of capitalism, according to Kornai. If this is so, there seems to be no way out for Cuba but to embrace capitalism in some form or other. See János Kornai, Highways and Byways. Studies on Reform and Postcommunist Transition (Cambridge and London, 1991).