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Updating Cuba's Economic Model

DR. OMAR EVERLENY PÉREZ VILLANUEVA, *Centro de Estudios de la Economía Cubana*
UNIVERSIDAD DE LA HABANA

Cuban authorities have repeatedly claimed, as early as 2007, that structural problems should be solved as soon as possible, since they prevent any possibility of growth. It is precisely this argument, in combination with objective and subjective factors in the direction of the economy that have promoted "the updating of the Cuban economic model." At the same time, we should not ignore that as early as the 90´s there was a prolific academic body of work that supported the need to make deeper changes in the Cuban economy.

The structural problems of the economy have been strongly debated, at least in the financial area for the last 15 years, including the lack of hard currency, distortions of the price system resulting from the over-valued official exchange rate, lack of convertibility, monetary duality, segmented markets, poor performance of the "real" economy, and in particular the sugar industry and agriculture, and the efficiency issues affecting public entities.

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Which are some of these structural problems that have lead to the deterioration of the majority of the economic indicators in the country?

- The structure of the Gross Domestic Product, with an elevated expansion of the services, especially professional services, while agriculture and industry remain lagging or are given little relevance.
- Excessive economic centralization.
- Limited diversity in foreign trade where the balance of payments depends on the export of professional services, specially from health personnel, whose dragging effect on the rest of the economy that remains low.
- Low productivity in a large percentage of the state-owned business sector, which causes low economic efficiency in general, with high consumption of energy and other materials.

- A high distortion in the relation of consumption-accumulation and income-consumption. In other words, an inadequate relationship between workers´ income and the high prices of goods and services, both in free markets as well as in state run markets, in local currency and in free currency.
- High level of prohibitions in society with regards to the possibility of the acquisition of certain good and services.
- Complicated demographic situation with a low birthrate, high percentage of the population over 60, and emigration that exceeds 35,000 persons per year.

These problems are interrelated and affect an economy with a small internal market, extremely dependent on imports, that has to face the economic blockage by the United States.

But the time spent in the socialist project, plus the analysis of the experiences of other Asian socialist countries, places on the Cuban government the urgent imperative of updating its own economic model, where the market must have an ever-growing role in the economy, even while the model of economic management that will prevail is central planning, but taking the market into account.

There is a pressing need then to implement changes in the economic structure of Cuba, but not just any changes, at least for the short term, but rather those that allow a move towards higher productivity or higher value-added sectors.

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It has been accepted that the government may assign nonstrategic activities capable of absorbing the large number of workers that will be available in the next few years, as a result of the new reorganization underway in state enterprises and budgeted units, where the numbers of workers to be relocated will be between 1 and 1.3 million for the first period. The first period began in 2011 and will make 500,000 government workers available.

The call to update Cuba's economic model, which was already submitted, required a meeting of the Party Congress (sixth Congress), which had been postponed for the last 13 years due to different reasons and for which the document "Draft guidelines of the economic and social policy" was prepared. This document was discussed throughout the country; taking into account its recommendations, amendments and new proposals.

An analysis of the main economic indicators makes obvious the sagacity and the necessity of the Cuban government when it began updating its economic model, although authorities insisted in their resistance to the changes that have begun, both from current leaders, as well as from the general population, accustomed to a more paternalistic type of state, more interested in spending that in increasing income for the state.

It is evident that a diagnostic of the current economic situation demonstrates still unfavorable results, for example:

a) Evolution of the Gross Domestic Product (GDP).

The Cuban economy stopped in 2010 the slowing rate of economic growth of the last few years, which grew at 2.1 %, and similar results are expected for 2011, although the growth rate between 2000 and 2006 was significant, reaching an annual average of 6.2 % of the Gross Domestic Product (GDP) at constant 1997 prices. However, are still slow paces according to the insufficient utilization of the potential of the so-called "real economy" such as industry and agriculture and the accumulated needs, by both the population and by the government.

b) Structure of the GDP.

The structure of the GDP shows a tendency toward a reduction in the relative weight in the composition of the GDP in the goods sector (agriculture, industry) and basic services as construction and transportation. There is also an important growth in other "basic services" such as health and commercial services, among others, where services contributed 80% of GDP in 2010.

Then we should reflect if it is possible to begin the development project on the basis of the growth of service sectors with low productivity, such as health, commerce, and education among others.

Although the areas for economic growth have been prioritized, it is not clear yet which sectors would recover in this future economic growth. The country is working on its economic stabilization, but the paths for the economic development of Cuba are not fully defined, and the products that will be used to insert the country in the global economy have not yet been identified.

The so-called real sector of the economy, such as industry and agriculture, has a very week contribution to GDP growth, since for the last three years their performance has been stagnant.

c) Low return on investments.

For the past decade and even in prior years, there has been a strong paralysis of financial resources in Cuba, with less new investments than those in process.

...how much longer would it be possible to continue an extensive growth model already 50 years old?

From 2000 to 2009 the approved investment plan was never implemented, demonstrating either an incorrect preparation of the plan, and low interest from the executors of the works, or the lack of construction materials and required equipment. This was the result of the lack of foreign financing required by investors, which in turn resulted in a paralysis of material and financial resources for the country. Therefore, the state lost financial resources and opportunities due to this situation.

This comment requires that we ask how much longer would it be possible to continue an extensive growth model already 50 years old? We must also remember that until 1990 the extensive growth was not reflected so dramatically, although the economic indicators did so, due to the generous support offered to Cuba from the old socialist field, specially the URSS.

d) Aging and low growth rate of the population.

As the result of Cuba's low birth rate, the percentage of the population between the ages of 0 to 14 is decreasing and the group 60 years old and older continues to grow. In 2010, 1.9 million Cubans were 0 to 14 years old, but also 1.9 million were 60 years old and older.

The aging of the population is one of the most important causes of the demographic transition in the country, in particular because of the preparation that it demands from all the institutions and members of society to face it. The first stage of aging in Cuba was at the start of the 70´s, and by the end of that decade the population shows a dip in the birth rate, which fell under replacement levels and the population of 60 years old an older exceeded 10 per cent. For 2010 the aging of the population is placed at 17.4 per cent.

e) Unfavorable relationship between the growth of productivity and average wages.

If we analyze the relationship of the growth of productivity and average wages until 2009, we can summarize that there was a complete distortion evidenced by the fact that salaries grew faster than productivity.

Evidentially in a country where there are "Inflated Payrolls" or more than 1,000,000 underemployed workers, it is possible to conclude that such relationship was never favorable. This issue must be resolved by the government in the next 2 years, or at least this is what the Cuban authorities have indicated.

An analysis of employment by sector clearly evidences that the sector that would leave more workers unemployed would be in the "other services," which is where the number of jobs had grown in the last few years, while decreasing the numbers of those occupied in the goods sectors.

Since 2010, the government has been accelerating the analysis of the jobs that could become available and that were generated in the health, education, public administration, among others, from the programs associated to the "Battle of Ideas."

f) Number of completed houses per year.

A special construction program was undertaken in Cuba in 2006, for the rehabilitation and preservation of houses, where it was decided that one hundred thousand homes per year starting would be build beginning in 2006. This program was only met in 2006, since there were already many homes pending small actions for completion from the Special Period and given the priority assigned for the task for the year.

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Current policy has been directed to favor the construction of homes by participant effort, where Resolution No 40/2010 from the Housing Institute published in the Official Publication of the Republic of Cuba, on February 17, 2010, allows incentives to be offered for the construction of homes by owners, through the issuance of construction licenses.

This resolution includes the "Special Third Provision" authorizing the municipal housing investment units to approve, without a prior selection process, the requests for construction licenses from private individuals for new projects, extensions, remolding, rehabilitation, divisions and unifications, with the only requirement of the property of the land or the right to use the roof.

This resolution opens the issuance of other licenses to individuals who through their own effort may request:[1]

- Construction activities to repair houses in poor condition or to completely replace them.
- Extensions within the property limits.
- Build in unfinished construction, legalized or approved.
- Construction actions to allow itemizations, changes in concepts to convert leased spaces into appropriate homes.
- Building of new homes by owners of land or roofs.

g) Foreign trade.

The unbalance in the commercial exchange of goods continues to be typical of the Cuban foreign trade over the last decade. Exports fail to grow with the needed dynamism due to the fall in the production of sugar, the stagnant mining production such as nickel, the fall of exports of seafood, citric production, among others, and where imports remain at a high level in spite of the official policy of contraction.

1 Instituto de la Vivienda. Indicación metodológica No 10, Vicepresidencia Primera. April 6, 2010. Habana, Cuba.

The increase of imports for 2008, added to their prior commitments, has resulted in growing tension in the Cuban balance of payments, to the point that all foreign payments were withheld, particularly in 2009. This caused the burden of the foreign debt to increase significantly, both in relation to export of goods and as well as with relation to both goods and services together.

h) Foreign exchange of goods and services.

The service sector remains as the main generator of income since 2004, with important qualitative changes, since services requiring intense knowledge have displaced the tourist sector as the first generator of income.

Estimates show that more than 50 percent of the services exported correspond to medical services, which contributed to a surplus in the commercial balance of goods and services for 2009 and 2010.

After analyzing these economic indicators we will identify the main proposals of the "Guidelines for the economic and social policy of the party and of the Revolution" approved on April 18, 2011, and confirmed by the National Assembly of the People's Power on August 1, 2011.

The following are the main proposals and adjustments approved by the Congress of the Party:

- Adjustment of expenditures in the budget (education, health, sports, culture).
- Adjustment of employment in the state sector by the elimination of inflated payrolls.
- Assignment of idle land under the figure of "usufruct".
- Reorganization of the government, ministries and large state-run companies.
- Incentives for private employment, such as the reauthorization of independent work.
- Proposal to create non agricultural cooperatives.
- Possibility to hire personnel.
- Proposal to eliminate prohibitions such as the purchase/sale of homes, automobiles and other goods and services, etc.
- More business autonomy.
- Development of local projects and more autonomy to local governments.
- Equality of opportunity for all but not "equalitarianism".
- Search for self-sufficiency in food production and the gradual elimination of rationing.
- Possibility to lease government-owned facilities, for activities such as gastronomy.
- Separation of government and business activities.
- Updating of tax policies.
- Strategies to redirect payment of foreign debt.
- Promote the creation of Special Development Zones.

In the interest of updating the Cuban economic model it is be important to include the re-analysis of the so-called Small and Medium Enterprises ("SMEs"), whose implementation was planned for the middle of the 90´s, a process that was interrupted due to many factors.

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These companies fall under the proposal to expand independent work made by the National Assembly of the Peoples Power in August 2010, and approved in later documents and published in the Official publication of the Republic of Cuba in Special Issues No 11 and 12, from 1 and 8 of October 2010.

The advantage of the SMEs is that they represent an employment alternative, so much needed these days, which results in an increase in living standards and income for participants, allows the decentralization of certain productions and services, and an increase in the offer of goods and services.

It is interesting to remember that this term is not created by the current difficult situation of the Cuban economy, but it is a worldwide tendency that is prevailing by structuring production on the basis of small and medium size enterprises, which very flexibility, high level of qualification in the labor force (one of the largest assets that Cuba has at this time) and are very competitive.

It is also true that currently the Cuban government is analyzing the need to implement some variations of SMEs, specially the so-called cooperatives for the socialization of production and the benefits that they may contribute.

But there are also other forms that should be analyzed such as independent workers and the government, or independent work and cooperatives.

It is well known that these activities and associations exist, but the intention is to legitimize and bring into the open this labor relationship, establishing the applicable social responsibilities and government control over these activities.

There is a group of activities that were proposed initially but failed to be included in the current regulation of independent activities issued in the 90's, and there are others that worked but later disappeared, and which could be rescued in this updating of the model.

In addition to the high quality of the labor force, and the fact that there is a high percentage of unemployed young people, studies should be made about the type of companies that could make better use of this knowledge to prevent the exclusion of this labor force that otherwise would tend to emigrate to other jobs with better pay, but with lower qualification requirements and in some cases they could emigrate aboard. These jobs should be structured as Consulting, Audits, Architecture, Design and others that could even be proposed by the citizens themselves.

This new process must overcome the difficulties suffered by independent workers in the past, among them the difficulty to purchase supplies, the strict tax policies, inexistent financial support (microloans), lack of government controls, regulations for the subcontracting of labor force, among others.

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The experiences of China and Vietnam could be used in this process, since there has been a lot of reflecting in Cuba with regards to the economy, society, politics and ideology and in this case it is part of the more general discussions about modern socialism, given the fact that socialism has been the framework of reference for the transformations in Cuba since the fall of the "real socialism" in Europe, and obviously in China and Vietnam which are socialist countries.[2]

One of the most important focuses of attention from Cuban economists toward the experience of China and Vietnam, probably the best framework, would be the interest for a more ample and radical market

2 Mercado Interno y Desarrollo. Collection of various authors. Havana, 2004.

reform started by a Communist party in charge, which has been quite successful with relative extended and beneficial effects in the economic area, although polemical and contradictory in the social area and legitimized in the political area. It could be argued that Vietnam is a similar case.

China always offers an economic perspective limited to few dimensions: very high economic growth, magnet for foreign investment and a formidable export capacity. But when analyzing in detail the reality in China and Vietnam these dimensions could be lowered to second place, highlighting instead the importance of the internal market. What predominates today is the vision of a huge internal market with an accelerated growth.

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The priority given to the internal market in the general context of the reform in China goes back to its beginnings, based on agricultural reforms, and has been reinforced by the passage of time, reflected in the preference for diversification policies in the form of properties with a high inclination towards the creation of income supported by expanding private economic activity.

In particular, this leads one to reflect on the fact that although Cuba has an "open economy" (based on exports) very different to China´s, the expansion of the internal market would be key for the development of any economy and therefore must occupy a prominent place in any development strategy. This has obviously been a component that was absent in the Cuban economic policies of the last years, and which must be identified as "the" absolute priority in the development plans for the Cuban economic model.

The updating of the Cuban model is an essential step for the design of Cuba's development model for the medium term, which would solve some of the structural deformations described above, and where the development of the internal market is one of the especial variables of the Project.

This transformation of the model according to the plan prepared taking into account the new variables introduced, would allow for a growth of 5 % per year starting in 2012. It has been predicted that by 2015 35% of jobs in Cuba would be non related to the government and by 2012 there should be a surplus in the balance of payment of more than 1,500 million US and total exports should grow at 12 % per year between 2011 and 2015.

The stimulus of the productive forces intended, the promotion of industrial growth added to the infrastructure megaprojects and the current industrial projects such as the development of the port of Mariel, the petrochemical Project of Cienfuegos, the development of the production of nickel, among others, plus the incentive for the development of the non government forms of production, both in agriculture as well as in services, may contribute to the growth of the main economic indicators in Cuba.

For this purpose it is necessary to open the minds of the policymakers and to use efficiently the word "autonomy," break myths of the past, and understand that current and future generations should not be tied to the recent past.

OMAR EVERLENY PEREZ VILLANUEVA

Director of the *Centro de Estudios de la Economia Cubana* at the University of Havana. Doctorate in Economic Sciences of the University of Havana in 1998. Masters in Economic and International Relations from CIDE, AC Mexico City, Mexico in 1990. Bachelors in Economics from the University of Havana in 1984. Professor at the University of Havana.

Mr. Perez Villanueva has presented at conferences in various Cuban institutes as well as internationally, including in the United States, Japan, France, Canada, Spain, Brazil, Puerto Rico, Mexico, Dominican Republic, Venezuela, China, Malaysia, Argentina, Peru, Jamaica, Barbados, Trinidad and Tobago and Norway. He has served as a visiting professor at Universities in the United States, Japan and France and has published over 70 research papers in a variety of areas of the Cuban and global economy.

Mr. Perez Villanueva has also published over 75 articles in publications and has co-authored several books in Cuba and abroad, including "Cuban Economy at the Start of the Twenty-First Century," with Jorge Dominguez and Lorena Barberia (Harvard University. ISBN 0-674-01798-6, 2004), the second edition of "Reflections on the Cuban Economy" (Editorial Ciencias, Havana. ISBN 959-06-0839-6, 2006) and "Outlook fo the Cuban Economy I and II" (ISBN 978-959-303-004-5). His last book is "Fifty Years of the Cuban Economy" (Editorial Ciencias Sociales. Havana. ISBN 978-959-06-1239-8).