

UPDATE ON FOREIGN INVESTMENT IN CUBA: 1996-97

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Last year's paper presented at this conference¹ concluded that the argument for commercial engagement is fundamentally insupportable as a justification for foreign investment in Cuba under the current circumstances. Two primary factors were found to inhibit the feasibility of foreign investment as a vehicle of reform in Cuba. First, the island's distressed investment climate limits opportunities to attract a level of foreign investment that could have a meaningful impact on the economy and society as a whole. Second, because Cuba's peculiar *mode* of foreign investment has been designed to secure regime survival, its most significant reform-generating attributes remain, for all practical purposes, effectively suppressed. Perversely, its detrimental side-effects appear to mostly hinder, instead of bolster, the eventual establishment of a stable free-market democracy. In order to substantiate these points, last year's paper was divided into three parts. The first part established that Cuba's campaign to attract foreign investment had generated very disappointing overall results by mid-1996. The second part attributed this failure

to Cuba's highly risky investment climate, which was described in certain detail. The third part illustrated how Cuba's mode of foreign investment—essentially joint venture enclaves subject to singular regulations—has limited multiplier and dispersion benefits which are incapable of fostering meaningful economic or socio-political reform. On this occasion, we will provide a brief update on the same fundamental aspects, which have again been found to substantiate our previous conclusion.

CUBA'S DRIVE TO ATTRACT FOREIGN INVESTMENT

The Campaign to Lure Investors: 1996-97

The Cuban government continues to court foreign investors. During the last year investment protection and economic cooperation agreements were signed with France, Grenada and Laos, bringing the total number of bilateral agreements to 21.² A number of business fairs and conferences were held in Havana covering a wide range of sectors from health products and tourism to investment opportunities in sugar.³ Cuban officials continued to tour the world seeking to drum up business and covered a diversity of countries from the United States, Germany, France, and

1. See María C. Werlau, "Foreign investment in Cuba: The limits of commercial engagement," *Cuba in Transition—Volume 6* (Washington: Association for the Study of the Cuban Economy, 1996), pp. 456-495.

2. Agreements had been signed with: Italy, Russia, Spain, Colombia, U.K., China, Ukraine, Bolivia, Vietnam, Argentina, Lebanon, South Africa, Romania, Chile, Barbados, Germany, Greece, Sweden and Switzerland. Cuba reports thirty more bilateral agreements being negotiated. See *Economic Eye on Cuba* (17-23 February 1997, 3-9 March 1997 and 21-27 April 1997.) *Economic Eye on Cuba* is a weekly publication of the *U.S.-Cuba Trade and Economic Council, Inc.* (U.S.C.T.E.C.) For details on the *U.S.-Cuba Trade and Economic Council*, see Werlau, "Foreign investment in Cuba," p. 458.

3. *Economic Eye on Cuba* (21-27 April 1997, 25 November-1 December 1996, 26 May-1 June 1997, 3-9 March 1997); Joaquín Oramas, "Avance en el producto cubano," *Granma Internacional* (1997), edición digital.

Hungary to Belarus and Vietnam.⁴ Likewise, a number of commercial delegations, such as from China, Sweden, Laos and Jamaica, visited the island and groups of businessmen from Greece, Britain, France and others countries paid enthusiastic visits.⁵ In the public relations' arena, Cuba's most visible successes appear to have been the January 1997 visit of Canada's Foreign Minister, Lloyd Axworthy, and the festivities for the 30th anniversary of the Cohiba cigar the following month. This first visit of a Canadian foreign minister since 1959 received wide media coverage and produced a joint declaration, which was regarded as a snub to the United States and a legitimizing boost to the Castro regime.⁶ The Cohiba celebrations lasted over a week and culminated with a gala at Havana's Tropicana nightclub allegedly attended by 700 guests from 40 countries who paid US\$500 each. The dinner featured an auction of especially-rolled Cohiba cigars and hand-crafted humidors—one signed by Castro. 200 journalists from 20 countries requested accreditation to cover the event, which received widespread international media coverage.⁷

Historic experience and the absence of tangible results, however, make it highly unlikely that a significant level of actual (direct) foreign investment will result from the apparent enthusiasm with Capitalism "à la cubaine." The primary focus of most business delegations to Cuba appears to be the development

of trade opportunities and the exploration of *possible* investments. It seems that foreigners are more eager to tap into the island's dire need of a wide range of imports, despite the modesty of overall opportunities as a result of Cuba's lack of credit facilities and its depressed economy. Upon attempting to track down actual investment initiatives from the described contacts, one finds few concrete results. In turn, even optimistic coverage of the visits of French and British business delegations contain references to investors' concerns regarding such problems as Havana's water shortages, the need to totally renovate Cuba's citrus processing,⁸ and the country's lack of import financing facilities.⁹ While the President of the *U.S.-Cuba Trade and Economic Council* reported to the media that the past months have been very fruitful—with an increase in the Council's membership as well as in the number of companies involved in business—his personal comments are much less encouraging.¹⁰

Adding to Cuba's problems, a new trend seems to be emerging in the international media coverage on Cuba. Notwithstanding Cuba's publicity coups, the stream of enthusiastic stories on this "hot emerging market" seems to have dried out. Moreover, reports of a different twist are starting to gain ground. In March 1997 *Business Week* reported that Castro is counting on foreign companies to prop up Cuba through limited economic reforms, with the goal of keeping himself in power.¹¹ In July 1997 *The Economist* ran an article on free enterprise in Cuba, which

4. *U.S.-Cuba Trade and Economic Council*, electronic web page (11 July 1997); *Economic Eye on Cuba* (21-27 April 1997 and 9-15 June 1997).

5. *Economic Eye on Cuba*, several issues; Eloy Rodríguez, "Tercera visita del Consejo Nacional del Patronato Francés," *Granma Internacional* (30 abril 1997), ed. digital; Eloy Rodríguez, "Firma contratos misión empresarial británica," *Granma Internacional* (27 julio 1997), ed. digital; "Los griegos enfilan hacia el Caribe," *Granma Internacional* (2 junio 1997), ed. digital.

6. Axworthy was accompanied by the Secretary of State for American and African Affairs. Their visit took place on January 21-22, 1997. The Joint Declaration of the Ministers of Foreign Affairs of Canada and Cuba emphasized the mutual commitment and right to conduct international relations on the basis of the defense of international law and agreed to advance towards new bilateral initiatives and increased cooperation. *U.S.-Cuba Policy Report*, 4:1 (January 31, 1997), pp. 7-8.)

7. Orlando Gómez Balado, "Festejos por el mejor habano del mundo," *Granma Internacional* (13 febrero 1997), ed. digital; *Economic Eye on Cuba* (17-23 February 1997).

8. Gabriel Molina, "Franceses dispuestos a llenar espacio en la economía cubana," *Granma Internacional*, ed. digital.

9. E. Rodríguez, "Firma contratos."

10. Rodolfo Casals, "Empresarios norteamericanos interesados en comerciar con Cuba," *Granma Internacional* (8 julio 1997), ed. digital; John Kavulich in telephone conversations with the author of April 12, 1997 and July 11, 1997.

11. "Castro's Capitalist," *Business Week* (March 17, 1997), p. 48 and "A touch of capitalism," *Business Week* (March 17, 1997), p. 50.

specifically cites the new free trade zones and states that Castro hates the result of “yielding to market forces.” It declares the Cuban leader’s regard for foreign investment as a “temporary” and “necessary evil,” quoting a Castro supporter: “Our government hates people who make money.”¹²

Yet, some foreign businessmen persist in making bullish predictions on Cuba. Ian Delaney, the chairman of Canadian company Sherritt International, told *Business Week* last March that Cuba is “the best investment opportunity in the world.”¹³ Peter Scott, Chairman of Beta Funds Limited, has called Cuba “the last embryo market ...in the process of recovery and undergoing a gradual transition to a market-based economy.”¹⁴ The President of the German Association of Travel Agents declared Cuba “the safest travel destination in Latin America.”¹⁵ And a Frenchman with a business in Cuba extols: “This is the seventh time I have encountered President Fidel Castro. He is an extraordinary person. ...the country is recovering extraordinarily. ...Every day I discover new clients and new things to do here.”¹⁶

In the United States, a corporate campaign against unilateral economic sanctions has emerged involving General Electric, IBM, Exxon, Mobil, Citicorp, Allied Signal, Ingersoll Rand and Westinghouse. In alliance with the U.S. Chamber of Commerce the National Association of Manufacturers and the National Council for International Trade,¹⁷ the Helms-Burton

legislation has become one of its targets.¹⁸ In addition, a lobby to lift restrictions on the sale of food and medicine to Cuba was recently undertaken in Washington.¹⁹ Nonetheless, the general mood of the U.S. business community appears to be one of continued caution. For example, in July of 1996 CBS aired a documentary in which the aforementioned president of the U.S.-Cuba Trade and Economic Council named several U.S. companies and declared: “There isn’t a single CEO who doesn’t want to return to Cuba as soon as possible.” Yet, all but one of the companies responded to a letter of the Cuban American National Foundation disallowing any connections to the Council (Chrysler, General Motors, Ford, McDonalds, and ITT).²⁰ Most added strong statements denying business interest in Cuba and/or efforts to lobby against the embargo.²¹

To illustrate Cuba’s seeming quandary, perhaps an anecdotal account might provide some lucid insight. In February 1997, an elite group of powerful Latin American businessmen (the “Group of 50”) went on a visit to Cuba which featured a gala attended by Castro. Fidel was received as a star, posed for pictures and signed autographs. Notwithstanding the obvious enthusiasm, one of the attendees—the head of an industrial/banking conglomerate—admitted that most members of the delegation were not interested in doing any business in present-day Cuba, and were rather satisfying an alluring curiosity.²² In sum, Cuba,

12. “Cuba: enterprise?: tax it,” *The Economist* (July 5, 1997).

13. “Castro’s Capitalist.”

14. *Economic Eye on Cuba* (3-9 March 1997).

15. Rodolfo Casals, “Para los vacacionistas, Cuba es el país más seguro de Latinoamérica,” *Granma Internacional* (7 mayo 1997), ed. digital.

16. This French businessman produces metallic parts for the construction industry in Cuba. See G. Molina, “Franceses dispuestos.”

17. Newsletter of *The American Chamber of Commerce of Cuba in the United States* (April 23, 1997), p. 2.

18. “Empresas de EEUU lanzan campaña contra la ley Helms-Burton y las sanciones económicas,” *Granma Internacional* (9 abril 1997), ed. digital.

19. Sherritt International was reported to have retained Malcolm Wallop, a former Republican Senator from Wyoming, to lobby on this behalf. *The U.S.-Cuba Policy Report*, 4:4 (April 30, 1997).

20. The exception is Archer Daniels Midland, whose former Chairman, Dwayne Andreas, has been a very vocal spokesman for lifting the embargo on Cuba.

21. “Credibility challenged: Cuba trade booster’s comments on CBS rejected by companies,” Press Release, *The Cuban American National Foundation* (September 26, 1996), with copies of letters from the cited companies.

22. Related in person to the author.

continues to be the focus of much curiosity, but actual commitments to invest foreign capital appear direfully lacking.

Results

Verifiable results, as in the past, are unavailable. Yet, despite the ambiguous and contradicting data emanating from Cuban government sources,²³ it becomes apparent that results are disappointing. By the end of 1996 fairly consistent statistics emerge from official sources of the *total* number of joint ventures and economic associations.²⁴ Although the Deputy Minister for Foreign Investment reported a total of only 236 in June 1997²⁵ most reports cite 260, said to be established in the following sectors: 30 in oil extraction, 38 in mining (5 of these in nickel), 45 in tourism,²⁶ 41 in hotel administration, 4 in real estate, 85 in industry, and 12 in transportation and communications. Only a few joint ventures are said to be more than 50% foreign owned, in no case more than 70% foreign owned.²⁷ This claim of 260 joint ventures up

to the end of 1996 is puzzling because in late 1995 both Minister Carlos Lage, Cuba's "economic czar," and the *Comisión de Estudios de la Economía Cubana* had claimed the existence of 270 joint ventures from 50 countries.²⁸

Data on the number of joint ventures established in 1996 is more inconsistent. The Minister for Foreign Investment claimed that 80 were established after the enactment of the new foreign investment law in September 1995, 56 of these in 1996.²⁹ Notwithstanding, a later report from this same Minister cites 48 established in 1996³⁰ and the United Nations Economic Commission for Latin America (ECLA) report on Cuba of September 1997 refers to 46 joint ventures established in 1996.³¹

As in the past, reports from Cuba all fail to provide figures on foreign direct investment or to distinguish traditional joint venture investments from economic cooperation agreements, which typically don't entail direct capital infusions. A University of Havana pro-

23. Data is obtained from reports of Ministries, interviews and statements by different Ministers, the newspaper *Granma*, and other official and semi-official sources, such as academic centers. Cuba's reporting does not meet the standards of most countries; contrary to standard practice for the calculation of foreign direct investment, in addition to capital inflows, the data provided by Cuba appears to include diverse financial transactions, management contracts, production partnership arrangements, foreign contribution of assets, debt-equity swaps, exploitation contracts to service or expand deposits already mined, canceled deals and "announced" investments contingent on events that may never materialize. Discrepancies in figures provided by the government are exacerbated by conflicting information obtained from other national and international reports. See Werlau, "Foreign investment," pp. 462-463.

24. For purposes of simplification, we will use the term joint venture to refer to joint ventures and economic associations indistinctly.

25. "Cuba says few firms using old U.S. property," *Canadian Press*, Havana (June 18, 1997) and *Economic Eye on Cuba* (17-23 June 1997), p.1. (Minister Octavio Castilla is quoted.)

26. There is discrepancy with other reports provided by the same Minister for Foreign Investment which cite 20 joint ventures in tourism, including 17 hotels. See *Economic Eye on Cuba* (21-27 April 1997). The Minister of Tourism, in turn, reported 36 joint ventures in tourism—20 with joint capital, 16 management contracts. Orlando Gómez Balado, "Llegó el millón de visitantes," *Granma Internacional* (14 enero 1997), ed. digital.

27. *Economic Eye on Cuba* (25 November-1 December 1996), as reported by the Minister for Foreign Investment.

28. Magdalys Rodríguez, "Trabas al empresario interesado," *El Nuevo Día* (23 de noviembre de 1995); *Negocios en Cuba*, Suplemento del Mundo en Síntesis (semana del 19 al 25 de agosto de 1996), p.1. Adding to the confusion, the Ministry of Economy and Planning, however, reported 240 association agreements with foreign capital from 43 nations for the first semester of 1996. *Cuba: Economic Report*, First Semester 1996, Ministry of Economy and Planning.

29. *Economic Eye on Cuba* (25 November-1 December 1996).

30. Minister Ibrahim Ferradaz cited 48 joint ventures established in 1996 by December 1, 1996 for a total of 260. *Economic Eye on Cuba* (25 November-1 December 1996). In addition he reported the 1996 agreements as more complex and involving larger amounts of capital than those completed the year before and informed of an additional 100 joint venture agreements in the process of negotiation. *Economic Eye on Cuba* (3-9 March 1997). In another report, the Minister cited 42 association agreements with foreign investors from March to December 1996. Joaquín Oramas, "Turismo, zafra y níquel: ejes para el desarrollo," *Granma Internacional*, ed. digital.

31. United Nations Economic Commission for Latin America and the Caribbean (ECLA), "La evolución reciente de la economía cubana" (September 1997), p.139.

fessor acknowledged at an international conference: “It’s difficult to quantify the flow of international capital into Cuba (...) committed disbursements have amounted to more than US\$2.5 billion, of which what has actually been completed is unknown.”³²

One interesting and seemingly new development in the area of foreign investment is Cuba’s participation in joint ventures abroad. One already began operating in Mexico and is said to have contributed capital to form BIOTEK, to produce soy milk substitute using technology developed by the Research Institute of the Food Industry of Cuba.³³ Another joint venture was announced in March 1997 between the government-operated Cuban Agriculture Equipment Research Institute and Mexico’s Agroingeniería S.A., to produce in Mexico plowing equipment designed in Cuba to be sold in Mexico and other Latin American countries.³⁴ Cuba has also developed several joint investments with Vietnam. An agreement was signed by Cuba’s government-operated Tecnoazur, Spain’s Bilbao Vizcaya bank and “Vietnamese companies,” to construct a sugar mill in Vietnam. Government operated companies of Cuba and Vietnam agreed to establish Bio Viet Nam Limited to produce and distribute the organic pesticide BIORAT in Vietnam and other Asian countries.³⁵ In May 1997 a US\$8.5 million joint venture livestock and meat processing plant was inaugurated in Vietnam.

During the past year, it appears that indeed a few new joint ventures were established in Cuba, but

none of those for which numbers are cited involve a large amount of capital and most announcements don’t cite an amount at all.³⁶ Moreover, it’s impossible to say if these represent capital infusions and/or if they have been included in figures previously “announced” or “committed/delivered” investments, as per data provided by the U.S.-Cuba Trade and Economic Council. For example, mining “investments” sound large, but it looks like capital expenditures are limited in scope in many of the announced deals, at least for now and particularly in relation to the required capital for project development in the exploitation phase. While firms from Canada, France, Great Britain, and Sweden are said to have invested more than US\$200 million for seismic exploration in 19 of the 32 blocks in which the country has been divided, only a few wells are said to have been drilled and even fewer are producing.³⁷ Details on these investments are mostly unavailable and it is uncertain whether they will lead to continued investment. Some additional problems with announced foreign “investments” include:

- Valuation formulas are suspect; the terminology “valued at” chosen to cite some investment makes the amount of direct capital dubious;
- It is unclear whether foreign capital has actually been disbursed for many “deals”;
- Reportedly, the proceeds of certain foreign investments (sale of Cuban assets) are diverted to special accounts subject to Castro’s personal and

32. Omar Pérez Villanueva, Universidad de la Habana, Centro de Estudios de la Economía Cubana, *La inversión extranjera en Cuba: Peculiaridades*, paper presented at the LASA 97, XX International Congress, Guadalajara, Mexico, March 1997, p. 22.

33. *Cuba Monthly Economic Report* (July 1997), p. 3.

34. *Economic Eye on Cuba*, 1997 Monthly Chronology of Selected Commercial Activity (March 1997).

35. *Economic Eye on Cuba*, 1997 Monthly Chronology of Selected Commercial Activity (March and May 1997).

36. The author has compiled a partial list of 1996-97 joint venture deals in the form of an Addendum to this paper. This addendum is not included in this volume because of space restrictions. The addendum is available from the author. Ed.

37. A well in the Bay of Cardenas (Cupex IX) is said to be producing 3,750 barrels of oil a day, one at Puerto Escondido, 550 barrels a day. *Cuba Monthly Economic Report*, 1:3 (July 1997), p. 4.

arbitrary management (“the *Comandante’s* reserve”);³⁸

- Given the apparent nature of those investment agreements which grant joint ventures the rights to commercialize products of Cuban entities, capital infusions by the foreign partner for the development of these products seems improbable; and
- Foreign participation described as contributing technology and know-how³⁹ might indicate the sale of specialized equipment instead of a direct foreign investment.

Cuba has reported that 75% of the existing joint ventures and economic associations have initial capital of *less than* US\$5 million.⁴⁰ In a hypothetical calculation, if the cited 260 joint ventures and economic associations each represented an average capital investment of US\$2.5 million, the total foreign investment in Cuba could not exceed US\$650 million. If the average investment were raised to the maximum US\$5 million cited for 75% of the total, the amount would increase to only US\$1.3 billion. Yet, by 1995, when the reported number of joint ventures was lower, Cuba was announcing foreign investment of US\$2.1

billion. Moreover, government reports of US\$2.2 billion in foreign investment through 1996⁴¹ would represent an increase of a mere US\$100 million from the figures it reported more than a year ago.⁴² If 56 joint ventures had actually been established in 1996, the average investment would have been of a mere US\$1.8 million.

To get an idea of the questionable and confusing nature of the available data, the following might be taken into account:

- The increase of US\$50 million reported in Table 1 for Canadian investments includes investments made by Sherritt International and the purchase by KWG Resources, Inc. of a nickel option previously held by the South African company Gencor. Nonetheless, Sherritt’s annual report cites only US\$22.5 million in investments in Cuba in the fiscal year ending 12/31/96 and KWG’s purchase was reportedly for US\$10 million. Both total only US\$32.5 million; the US\$17.5 million shortfall is unaccounted for. Moreover, it is unlikely that KWG’s option entailed a capital investment, which would mean that the shortfall in direct capital invested would actually increase

38. Related to the author in August 1997 by Jesús M. Fernández, who left Cuba in May 1996 after occupying very high level government positions, including dealing with Castro’s “special reserve.” *Cuba Monthly Economic Report*, a publication of DevTech Systems, Inc. published a Special Edition (August 1997) recounting Mr. Fernández’s first-hand knowledge of the accounts. Mr. Fernández specifically cites a US\$50 million payment for the “sale” of Havana Club rum distilleries to the French firm Pernod Ricard going directly to the *Comandante’s* reserve as well as estimated net earnings of US\$10-15 million derived from several foreign investments involved in citrus, specifically citing joint ventures with Chilean investors. In 1993, Pernod Ricard obtained the rights to commercialize Havana Club rum internationally. Details of the financial arrangement involved have not been obtained as of the time of this writing.

39. As per at least one announced deal in which the Cuban part was said to be responsible for “assembling the equipment and implementing the investment.” See “Modernizarán empresas francesas generación de la termoeléctrica Antonio Maceo,” *Granma Internacional* (23 abril 1997), ed. digital.

40. Figures provided by the Minister for Foreign Investment. See *Economic Eye on Cuba* (3-9 March 1997); *Reuters* (November 5, 1996.)

41. *Economic Eye on Cuba* (21-27 April 1997).

42. The September 1995 issue of *Business Tips on Cuba* cites a Minister of Foreign Investment and Economic Collaboration, Ernesto Melendez, May 1995 report of 212 *economic associations* with firms from 53 countries with a “capital contribution of 2,100 million dollars, representing a 78% growth in relation to the same period of 1994.” *Business Tips on Cuba*, 2:9 (September 1995), p. 6. One year later, this publication cites the Minister of Economy and Planning, José Luis Rodríguez, informing of 230 economic associations and *the same* amount of investment, US\$2,100 million dollars. *Business Tips on Cuba*, 3:9 (September 1996).

by up to US\$10 million even lower in direct investment.⁴³

- We might extrapolate numbers cited for French joint venture investments to total investments. If the 39 French companies reported to be established in Cuba⁴⁴ (15% of 260 joint ventures) have US\$10 million in committed/delivered investment, as per the above table, their average investment would be only around US\$256 thousand. By applying this average investment to the 75% of joint ventures the government has cited as having investments below US\$5 million, we end up with around US\$49.9 million in total investment from 75% of all investors. This means that the remaining 25%, 65 foreign firms, would have invested around US\$33.8 million each. In light of the reports the government has put out, this seems implausible.
- **Table 1** shows committed/delivered Spanish investments of US\$80 million, yet the total for direct Spanish investment in Cuba reported by Spain's Ministry of the Economy in late 1996 was equivalent to around US\$11.2 million.⁴⁵ Yet, Cuba's Minister of Tourism reported that in

1996 alone Spain invested US\$100million in just one industry—tourism.⁴⁶

In fact, the total “committed/delivered foreign investment” in Cuba—*accumulated over time* from *all* investors from *all* countries—is estimated at no higher than US\$869.9 million, as per data provided by the *U.S.-Cuba Trade and Economic Council*.⁴⁷ This data, it must be noted, includes “committed” investments, such as options for mining rights, rather than just direct invested capital. If, indeed, Cuba has US\$869.9 million in direct investment, reported as “delivered” in Table 1, and we assumed a high return of capital of 33.3% per annum, a hypothetical 50/50 partnership would generate net earnings of US\$289 million per annum—around US\$145 million for each partner (the Cuban government and the foreign investor).⁴⁸ (Since the level of investment is presumably overstated and this assumed rate of return is very high, actual results would be lower unless a higher capital return ratio were factored in. It should be, for example, noted that Sherritt, Cuba's most notorious investor, reported a rate of return of 27% for its 1996 operations in Cuba.) Assuming our estimated revenue is for income derived from operations, the Cuban government will have additionally obtained approximately US\$123.9 million in tax revenues for

43. KWG announced plans to invest US\$300 million. (More details on this transaction are included in the Addendum referenced in footnote 36.) *CubaNews*, 5:7 (July 1997), p. 3. A media report cites 20 Canadian joint ventures by mid-1996 with investments totaling more than US\$300 million. Juliet O'Neill, “Firms forced out won't have a headstart when communism falls,” *Southam Newspapers* (July 13, 1996), distributed by *CubaNet*.) Yet, if we hypothetically, took the ratio Cuba has cited of 75% of the joint ventures totaling less than US\$5 million and pushed it to the very maximum of US\$5 million for 15 joint ventures (75% of the total), we end up with US\$75 million. This theoretically requires the five remaining Canadian companies to have invested US\$45 million each. Yet, other than Sherritt's, no such large investments have been reported. Interestingly, a 1996 Canadian media report cites Canadian investments in Cuba as “hundreds of millions of dollars more” than the reportedly \$390 million in two-way trade. Colin Nickerson, “Canada doesn't buy U.S. stance on Cuba,” *The Boston Globe* (February 29, 1996.)

44. *Economic Eye on Cuba* (21-27 April 1997).

45. Spain's direct investment in Cuba was reported to have risen sharply in the first nine months of 1996, from 527 million pesetas (US\$4.1 million) in relation to the same period in 1995. “Spain's investment rose sharply in 1996,” *Reuters*, Madrid (November 26, 1996). The dollar equivalence was calculated at 128 pesetas to the dollar.

46. Armando Correa, “España nombraría embajador en Cuba por visita del Papa,” *El Nuevo Herald* (12 agosto 1997), distributed by *CubaNet*.

47. Curiously, the *Council* reported US\$705 million in committed/delivered foreign investment as of 4/1/97, 5% less than in 8/1/96. *Economic Eye on Cuba* (21-27 April 1997). The *Council* receives the official cooperation of the Cuban government and sends copies of its reports to Cuban officials, who have not advised of any discrepancies in the calculations of foreign investment. (As per John Kavulich, President of the *Council*, in telephone conversation with the author, 7/11/97).

48. A 3-year rate of return of capital is an assumed average minimum return for highly risky cross-border investments. This capital recovery ratio is reported for some foreign joint ventures in Cuba.

Table 1. Foreign Investment in Cuba (in million US\$)

Country	As of 8/1/96		Reflecting Changes as of 6/30/97	
	Announced	Committed/Delivered	Announced	Committed/Delivered
Australia		500		
Austria	0.5	0.1		
Brazil	150	20		
Canada	941	100	1191	150
Chile		69	30	
China	10	5		
Dominican Republic	5	1		
France	15	10		
Germany	10	2		
Greece	2	0.5		
Honduras	7	1		
Israel	22	7		
Italy	97	87	397 ^a	
Jamaica		2	1	
Japan	2	0.5		
Mexico	2256	250	1806 ^b	400 ^c
Netherlands	300	40		
Panama	2	0.5		
Russia	25	2		
South Africa	400	15		5
Spain	350	125		80
Sweden	10	1		
United Kingdom	70	50		
Uruguay	0.5	0.3		
Venezuela	50	3		
Total	5301	751.9	5401	896.9
Net Change			+100	+145

Source: Conversations with John Kavulich, President, U.S.-Cuba Trade and Economic Council and adapted tables of August 1, 1966, January 27, 1997, and July 25, 1997 provided by the Council with the following statement: "Figures represent the amounts of announced, committed and delivered investments since 1990 by private sector companies and government companies from various countries to enterprises within the Republic of Cuba. ... Information compiled through the media and other public sources, individual discussions with company representatives, non-Republic of Cuba government officials, and Republic of Cuba-based enterprise managers and government officials."

a. \$300 million increase attributed to STET's purchase of Domos' share in ETECSA.

b. \$450 million decrease attributed to Domos' cancellation of \$450 million expected investment in ETECSA.

c. \$150 million increase attributed to Domos' alleged capital expenditures in ETECSA.

total revenues of US\$268.9 million.⁴⁹ This amount, presumed as already overstated, cannot come close to compensating for the huge gap left by the loss of Soviet aid (estimated at around US\$6 billion per annum).⁵⁰ In fact, even a University of Havana study has stated in circumspect language that "it has been reiterated that the development resulting from the absorption of foreign capital is inferior to what might be the actual needs of the country."⁵¹

Despite the obvious problems with Cuba's data, many media reports continue to pass on obscure data at face value. *The New York Times* reported in February of 1997 that, despite Helms-Burton, Canadian companies alone had "poured over half a billion dollars into nickel mines, luxury hotels and other businesses..."⁵²

Performance and Notes on a Few Foreign Investments

A striking aspect of the stream of reports on Cuba's joint ventures is their almost complete absence of data on earnings performance. (Please see Addendum available from the author for a partial list of recent investments.) The only notable example of a foreign joint venture partner readily reporting earnings to the media is Sherritt, which, by its corporate nature, is compelled to make its audited statements available.⁵³ Almost all public references to joint ventures lack revenue/earnings data that would allow an assessment of results. Yet, it would seem that if joint ventures were generating attractive earnings, this information would be forthcoming.

Investment funds for Cuba might provide a more graphic appreciation of actual business opportunities

49. Assuming Cuba had a 50% share of every joint venture, earnings before taxes would total US\$412.85 million and a 30% tax would net the state around US\$123.9 million. This amount plus Cuba's estimated share of operating revenues (\$145 million) equals \$268.9 million.

50. Minister Lage indicated that Cuba's 1995 net income from foreign joint ventures was just US\$114 million, representing 3% of the country's net income. Given the data we have, no significant improvement is likely to have occurred.

51. O. Pérez Villanueva, *La inversión extranjera en Cuba*, p. 22.

52. "Cuba's bridge to the U.S.," *The New York Times* (February 16, 1997).

53. This, of course, does not mean that reports do not exist; if a diligent search in the country of origin of these investors were conducted, at least publicly traded company reports should be available. Many investments in Cuba, however, seem to come from privately-held businesses. For our purposes, a time-consuming investigation of this sort has not been possible.

in the island, but it looks like this activity is also very limited:

Beta Gran Caribe (B.G.C.), registered in the Dublin/Irish Stock Exchange and managed by *Havana Asset Management*, was the first investment company with an exclusive focus on the Cuban market.⁵⁴ In September 1996, more than six months after beginning operations, out of the 24 investment opportunities identified, only one investment was reportedly completed in the financial sector, two proposals were listed as approved and awaiting investment and six projects were being negotiated. By March 1997 it was reported that only around US\$12.6 million, or 47% of the initial Swiss francs (CHF) 40 million (roughly US\$27 million) raised for the fund had been invested.⁵⁵ In sum, the number and amount of investments—undertaken and under consideration—are modest.

The Herzfeld Fund, registered in the U.S., started operations in December of 1993 and began trading in May 1994. It seeks to invest in companies which could benefit from a free Cuba. The fund (of around US\$8 million) is 63.3% invested mostly in U.S., Mexican and Panamanian securities (mostly stock) and placed 52 in a ranking of 85.⁵⁶ For the fiscal year ended June 1996 it posted a net investment income loss of .03% while its share price declined 7.26%.

Net asset value, however, gained 13.30%. Given the events of the past year and the unlikely lifting of the U.S. embargo, it is understandable why this fund—in size and performance—is, at least for the moment, of marginal importance.

The Cuba Growth Fund, Ltd., a Bahamas-based investment fund, issued a prospectus in January 1997 to raise C\$370 million to invest in Canadian listed companies with substantial business interest in Cuba. (One source reported the Fund sought to raise US\$365 million.⁵⁷) In February 1997, Fund executives reported that approximately US\$36 million in commitments from Canadian pension funds and other institutional investors had been obtained in one week.⁵⁸ Updated information on the closing and/or performance of the fund has not been found.⁵⁹

The Tourism Industry

In April 1997 the Minister for Foreign Investment reported 20 joint ventures in tourism with a capital of US\$605 million, including 17 hotels.⁶⁰ In June 1997, Cuba's Deputy Minister of Tourism reported that 36 hotels (30% of the 160 in operation) were under foreign management and that the tourism sector had 13 joint ventures valued at US\$728 million covering 8,905 hotel rooms.⁶¹ In September 1997 the Deputy Minister reported the tourism industry had 21 joint ventures with foreigners with foreign

54. The fund is registered in Guernsey, where costs and listing requirements are minimal. In February 1996 it placed around 1,000 units with investors, consisting of five ordinary shares and one warrant, the latter typically granting rights to purchase a share at a pre-established price. *The Cuba Report*, 6:1 (May 1997), p.4 and *Economic Eye on Cuba* (3-9 March 1997). The author's direct request to the company for information went unanswered.

55. 16% in finance (CHF6.4 million), 10% in real estate (CHF4 million), 11% in biotechnology (CHF4.4 million), 6% in mining (CHF2.4 million), and 4% in debt (CHF1.6 million). The reported investment in the financial sector is a 70% stake in Caribbean Finance Corporation (CFC) for CHF6 million (approx. US\$4million), which started operating in July 1996, looking to develop financial services in Cuba, presumably in property development. It has deployed some CHF3.5 million -around US\$2.4 million—in three short term loans. Investment figures for real estate are divergent; while *The Cuba Report* reports only two investments, *Economic Eye on Cuba* reports investments in several sectors. See *The Cuba Report* (May 1997), p.4 and *Economic Eye on Cuba* (3-9 March 1997).

56. Summary of *The Herzfeld Caribbean Basin Fund*, provided by Thomas J. Herzfeld Advisors, Inc.

57. *Economic Eye on Cuba*, 1997 Monthly Chronology.

58. *Economic Eye on Cuba*, 1997 Monthly Chronology.

59. The author's request to the company for information went unanswered.

60. *Economic Eye on Cuba* (21-27 April 1997). According to the President of FINTUR, the Republic of Cuba's company which finances production for the tourism industry, the 17 joint venture hotels had 8,336 rooms, of which 2,500 were operational, the remaining 5,836 in project or construction phase.

61. *Economic Eye on Cuba* (24-30 June 1997), p. 3.

capital invested of US\$667 million and that 33 hotels out of 174 in operation under foreign management.⁶² No explanation has been offered for the puzzling discrepancies.⁶³ In fact, reports on tourism joint ventures coming from different government sources are so contradictory and confusing that the actual number of joint ventures and the amount of capital invested in this sector is unclear. It is impossible to guess how much has been actually invested and what value Cuba may be assigning to management contracts or “economic association agreements,” which typically imply that the foreign partner contributes management and know-how but no direct capital. Moreover, 15 “investments” in tourism have been said to not have the Cuban government as a partner.⁶⁴

Officially, tourism was the country’s largest U.S. dollar earner in 1995 and 1996⁶⁵ (see Table 2) and constitutes its fastest growing area. There are 211 non-hotel establishments catering to tourists, 360 retail stores selling products for U.S. dollars, 624 government-operated restaurants and cafeterias and 435 stores offering U.S. dollar-priced prepared foods, thousands of privately-owned restaurants and cafeterias since they were legalized in 1994, and hundreds

Table 2. Tourism in Cuba, 1990-1996

Year	Tourists		Earnings	
	Number	% change	Amount (Million US\$)	% change
1990	340,300	N/A	242.3	N/A
1991	424,400	19.8	387.4	37.4
1992	460,600	7.8	567.0	31.6
1993	546,000	15.6	720.0	21.2
1994	617,000	11.5	850.0	15.3
1995	745,000	17.2	1,000.0	15.0
1996	1,040,000	28.0	1,300.0	23.0

Source: Derived from data from Cuba’s Ministry of Tourism, as reported in *The Cuba Report* 5:9 (February 1997).

Note: Country of origin of tourists in 1996: Italy, 185,000; Canada, 156,000; Spain, 113,000; Germany, 75,000; France, 61,000; Mexico, 36,000; England, 28,000; Colombia, 24,000; others, 362,000. See *The Cuba Report*, 5:9 (February 1997).

of bicycle-driven food carts and food kiosks established since 1996.⁶⁶

The growth in tourism, however, is not without its problems. Official revenue reports are highly questionable, a problem compounded by Cuba’s historic reporting of higher net revenues than more developed and presumably more efficient markets of the Caribbean.⁶⁷ Ministry of Tourism officials have uncovered problems such as corruption, poor marketing, inflexible pricing, and inelastic spending in respect of lower demand.⁶⁸ An occupancy level of

62. “Reconocen impacto de las explosiones en el turismo,” *El Nuevo Herald* (24 de septiembre de 1997).

63. In another report of an earlier date, the same Minister for Foreign Investment cited different numbers: 45 joint ventures in the tourist sector by the end of 1996. *Economic Eye on Cuba* (25 November-1 December 1996). A *Granma* report cites 20 joint ventures plus 16 management contracts. Orlando Gómez Balado, “Llegó el millón de visitantes,” *Granma Internacional*, via internet. For its part, the University of Havana’s *Centro de Estudios de la Economía Cubana*, reports 20 joint ventures with foreigners plus 37 hotels under foreign management and 15 joint firms dedicated to tourism, mainly in nautical activities, and US\$162 million in credits granted for the development of the nautical tourist sector. O. Pérez Villanueva, *La inversión extranjera*, pp. 13-14. Meanwhile, attendees of *The Economist’s* “Fourth Roundtable on Cuba” were told by the government that 41 hotel management contracts are in effect with foreigners, for 11,000 rooms, of which one third is dedicated to international tourism. Susana Lee, “Hemos puesto en marcha una reforma económica dentro del socialismo,” *Granma Internacional* (19 marzo 1997), ed. digital. ECLA, “La evolución reciente,” p. 131, cites 20 tourism joint ventures and 39 hotels under foreign management.

64. Cuba’s Ministry of Tourism, *Cuba Monthly Economic Report* (July 1997).

65. *Economic Eye on Cuba* (26 May-1 June 1997).

66. *Economic Eye on Cuba* (25 November-1 December 1996).

67. See Werlau, “Foreign investment,” pp.471-472.

68. The government carried out a week-long inspection of 2,353 tourism industry facilities and 13 audits of the most important government-operated tourism corporations. Minister Carlos Lage reported that 20 government operated tourism employment agencies would be reorganized due to the discovery of corruption in Varadero. *Economic Eye on Cuba* (30 June-6 July 1997). Evidence of corruption reportedly included bribes (selling of jobs), falsification of documents and unauthorized payments. Michele Hergas, “En Cuba se paga por trabajar,” *Habana Press* (Septiembre 15, 1997).

55.9% leaves many resources under-utilized⁶⁹ and only 10% of tourist visits is considered “repeat tourism,” professedly due to the low quality of services.⁷⁰ In addition, the average daily expenditure per tourist has reportedly declined to a low of US\$220, apparently due to the large number of underground services available for tourists.⁷¹ As a result, the government has taken measures to combat these practices. Also, the risk factor in the tourist industry has risen significantly as of late and could dampen projection of continued growth. Several tourist facilities have been the target of terrorist attacks⁷² and eight foreigners were killed in a July 1997 *Cubana de Aviación* accident which took 44 lives.⁷³ During a visit to Spain, Cuba’s Vice Minister of Tourism acknowledged that tourism has suffered a decline due to recent bombings. In August 1997 tourism increased 2% despite projections of a 19.2% rise, and the first 15 days of September sustained a decline of 18.1%.⁷⁴

In sum, given the puzzling statistics provided by the government, the only consistent conclusions about the tourism industry is that Cuba continues to attract increasing number of tourists and net revenues are not at desirable levels.

Free Trade Zones

Possibly, the most singular development in the area of foreign investment during the past year was the establishment of Free Trade Zones (FTZs). The Foreign Investment Law of September 1995 contained very general language authorizing the establishment of free trade zones and industrial parks. In June 1996, Decree Law 165 was signed, which authorized all forms of economic activity—assembly, manufacture, banking, financial services and warehousing, with incentives not available to ordinary joint venture investors.⁷⁵ The zones are to be regulated and overseen by the Ministry of Foreign Investment and Economic Development. Concessionaires, responsible for the development and operation of the zones, handle applications and negotiate for the provision of warehouses, factories, housing and commercial and other facilities.⁷⁶ The two companies awarded 50-year management concessions for the four existing zones are Republic of Cuba-controlled companies, mostly divisions of Cimex S.A. and the military.⁷⁷

The Minister for Foreign Investment has declared that FTZs represent a significant relaxation in the requirements for foreign investment, particularly be-

69. ECLA, “La evolución reciente,” p. 129.

70. *Cuba Monthly Economic Report* (July 1997), p. 2. According to official estimates, 68,000 visitors seek accommodations in private homes. *Cuba Monthly Economic Report*, 1:2 (June 1997), p.2.

71. *Cuba Monthly Economic Report*, 1:2 (June 1997), p.2.

72. In 1991, an exile group had taken credit for a mortar attack on a Varadero resort. Since April 1997 several bombs have exploded in Varadero and Havana hotels, one killing an Italian resident of Canada. Paul Simao, “Canadian tourists not put off by Cuban bombings,” *Reuters* (September 18, 1997), distributed by *CubaNet*; “Reconocen impacto de las explosiones en el turismo,” *El Nuevo Herald* (24 de septiembre de 1997); and Frances Kerry, “Explosions rock Havana hotels, bombs suspected,” *Reuters* (July 12, 1997); Larry Rohter, “Cuba sees American link to hotel bombs,” *The New York Times* (July 14, 1997); Larry Rohter, “On bombings at resorts, Cuba betrays its jitter,” *The New York Times* (July 27, 1997).

73. The *Cubana* flight was en route from Santiago de Cuba to Havana; two Brazilians and six Spaniards died in the crash. “Cuban plane crashes with 44 aboard,” *Associated Press* (July 12, 1997), distributed by *CubaNet*.

74. “Reconocen impacto de las explosiones en el turismo.”

75. The Deputy Minister for Foreign Investment Octavio Castilla heads the Ministry’s FTZ office. The Ministry has set up a commission on FTZs comprised of representatives from 10 ministries: Economy and Planning, Finance and Price, Foreign Trade, Labor and Social Security, Armed Forces, Interior, Transportation, National Bank, Customs and Science, Technology and Environment. Ley sobre zonas francas y parques industriales (FTZ law), Chapter IV, Article 2, *Prensa Latina* (junio 1996), via internet; *The Cuba Report*, 5:5 (September 1996), p. 7.

76. “Cuba: born free,” *The Economist Intelligence Unit* (September 22, 1997).

77. “Cuba: born free,” *The Economist Intelligence Unit*; *Economic Eye on Cuba* (28 April-4 May 1997). CIMEX corporation established in 1979, was the first private company in Cuba. O. Pérez Villanueva, *La inversión extranjera*, p.2. The Wajay concessionaire, Almacenes Universales, is a Cuban company reported to have the informal rights for the Mariel and Cienfuegos FTZs. See Eloy Rodríguez, “Zonas francas: Comienzan las operaciones,” *Granma Internacional* (20 mayo 1997) ed. digital.

cause 100% foreign ownership will be authorized there.⁷⁸ Nonetheless, 100% foreign ownership and speedy approvals are customary in FTZs worldwide. Cuba's FTZs also offer:

- exemption from profit and payroll taxes for up to 12 years, 50% exception for 5 years thereafter; the exemption for service oriented companies is 5 years, with 50% thereafter for 3 years. These exemptions are renewable. More favorable tax incentives may be granted on a case- by-case basis.
- tax free repatriation of profits in hard currency.
- 25% of FTZ-produced goods may be sold in the internal market free of duty; incremental amounts shall be decided by the Ministries of Foreign Investment and Foreign Trade.⁷⁹
- all products with 50% or more value added in the FTZs can be sold in the domestic (hard currency) market free of duty.

The first two FTZs opened in May 1997 near Havana (Berroa and Wajay)⁸⁰ and two more zones are set to open in the port of Mariel and in Cienfuegos⁸¹ (see Table 3). Despite announcements of numerous approvals for FTZ operators in the Havana FTZs, in mid-1997 only seven foreign companies, which will provide combined employment for 150 workers, were reported to have been licensed.⁸² The President of the U.S.-Cuba Trade and Economic Council, toured Cuba's FTZs in May 1997 and found seven

operators (producing building materials, lamps, soft drinks, and housewares) with initial investments of less than US\$1.5 million. These operators, he reported, are looking to eventually export to the Caribbean market, but all their current output had been previously contracted for the domestic Cuban market. Allegedly, they are being lured by an atmosphere of "everything is negotiable"—i.e. the terms of tax holidays, port status, regulations, etc.⁸³ For its part, *The Economist Intelligence Unit* reported that by September 1997 a dozen companies had established operations and around one hundred applications were being processed (30 involving industrial production); it called interest in the FTZs "hardly a mad rush."

Table 3. Specifications of Approved Free Trade Zones

Location	Size (hectares)	Warehousing (square meters)	Offices (square meters)
Berroa	244	41,616	4,200
Wajay	21	13,000	1,100
Cienfuegos	432	11,800	9,800
Mariel	533	7,000	9,800

Source: "Cuba: born free," *The Economist Intelligence Unit* (September 22, 1997).

Officially, the primary goals of the FTZs are to increase Cuban exports, generate employment and hard currency revenues, and acquire technology,

78. *Economic Eye on Cuba*, 28 April - 4 May 1997.

79. Cuban officials have stated that this is attractive to operators because many competing FTZs require the export of 100% of their production. E. Rodriguez, "Zonas francas."

80. *Almacenes Universales*, the concessionaire for the Wajay FTZ, announced the approval of 18 operators, four of them industrial—a soft drink plant financed with British capital, an Italian pasta company and two Spanish firms making plastics and furniture. The Berroa Valley concessionaire, *Havana in Bond*, was reported to have invested US\$30 million in infrastructure to open the 600 acre warehouse complex, which is still partly under construction. It allegedly began operations with licenses to 55 commercial business and two industrial firms, with additional applications under study for 36 to 45 companies from countries such as Brazil, Italy, Mexico, Spain and Panama. Isabel Morales, "Mas de doscientas hectareas abiertas al mundo del comercio," *Granma Internacional* (8 mayo 1997), ed. digital and E. Rodríguez, "Zonas francas."

81. Wajay is near Havana's International Airport and at Valle de Berroa is east of Havana's port. Mariel is 43 km. from Havana and Cienfuegos is 250 km. southeast of Havana, adjacent to the Panama Canal.

82. Operators are: three from Spain, one each from Canada, Jamaica, Italy and Holland. Pascal Fletcher, "First Cuban free trade zone could open next week," *Reuters* (April 29, 1997); *Economic Eye on Cuba* (28 April-4 May 1997).

83. John Kavulich, in telephone conversation with the author, 5/12/97.

knowledge, and know-how.⁸⁴ Although a government source has said that the *primary* objective of the FTZs is to export,⁸⁵ it looks as though existing operators are essentially producing for the domestic market. The cost of labor in Cuba is too high compared to other FTZs in similar locations in the Caribbean,⁸⁶ even though FTZ operators are free of the 11% payroll tax (labor utilization tax) typically paid by foreign investors.⁸⁷ Cuban workers in FTZs are reported to be earning 300 to 500 Cuban pesos monthly (equivalent to US\$13.6 to US\$22.7), but the Cuban employment agency is receiving an average of around US\$450.00 per worker from the FTZ operators.⁸⁸ The high salaries payable to the state makes Cuba's FTZs improbable competitors in the export sector. Even Cuban officials have recognized strong competition from over 100 geographical neighbors and the handicap of inaccessibility to the U.S. market.⁸⁹ Competition is particularly strong from neighbors such as Mexico, Panama, Jamaica and the Dominican Republic, all experienced in the free-zone business and with access to the U.S. market; Puerto Rico

will also soon be offering new incentives to attract industry.⁹⁰

It is likely that FTZ operators in Cuba are primarily looking, at least in the short term, to fill a very hungry domestic demand for goods mostly unavailable in the island.⁹¹ Although the purchasing power of the population is very limited,⁹² remittances from abroad, said to be higher than the total wages of Cuba's entire labor force at current exchange rates,⁹³ account for increasing sales in dollar-only stores. (1996 revenues from all government-controlled hard-currency retail operations was estimated at US\$750 million.⁹⁴) Estimated between US\$627 million⁹⁵ and US\$800 million⁹⁶ for 1996, surpassing sugar and tourism, remittances have become the country's first source of hard currency revenues.

Cuba, meanwhile, is probably hoping to put its idle space to use in addition to adding assembly and/or production capacity that can create employment and bring in technology. Access to highly-skilled labor, prime geographic location, low capital requirements, the potential of quick returns, the ability to operate

84. FTZ law, Chapter I, Article 1.3; *The Cuba Report*, 5:5 (September 1996).

85. P. Fletcher, "First Cuban free trade zone."

86. Most FTZs in the Caribbean have been established for several years, if not decades, with similar incentives (zero or special customs, import and export duties, land and building taxes, fees for work permits, corporate or capital gains taxes, etc.) There are 33 FTZ industrial parks in the Dominican Republic—14 owned by the state, 17 managed by the private sector and 2 under mixed administration. In 1995 the average salary paid for workers employed three months or less was equivalent to around US\$131 (RD\$1,678.69), or US\$0.57 an hour. Esther Hernández Medina, Employment Policies Coordinator, CIPAF, "A brief profile of free trade zones in the Dominican Republic," via Internet.

87. The FTZ Office Director has stated that labor costs will be only "a little over" the competition's, as the investor will be able to save in personnel training. E. Rodríguez, "Zonas francas."

88. John Kavulich, in telephone conversation with the author, 5/12/97.

89. Ibid.

90. "Cuba: born free," *The Economist Intelligence Unit*.

91. FTZs are normally attractive to companies looking to penetrate a market for which their goods, if produced in the country of origin, subject to conventional duties and taxes, would not be competitive.

92. Cuba's income per capita is currently the lowest in the Hemisphere, as per ECLA, "La evolución reciente." Pablo Alfonso, "Exertos: isla ocupa el último lugar en nivel de vida," *El Nuevo Herald* (28 de septiembre de 1997), distributed by *CubaNet*.

93. Pablo Alfonso, "\$800 millones del exilio son la 1ra. fuente de divisas en Cuba," *El Nuevo Herald* (10 de septiembre de 1997), distributed by *CubaNet*.

94. *Economic Eye on Cuba* (5-11 May 1997).

95. As per the Cuban government, in *Cuba Monthly Economic Report* (July 1997), p. 1. This report alleges that substantial regional inequality in food consumption is closely related to the availability of remittances from the U.S. Citing government studies, 30 to 60% of the population of 9 provinces has access to dollars while less than 30% do in the remaining 5 provinces.)

96. P. Alfonso, "\$800 millones del exilio," quoting ECLA.

without Cuban partners, and the absence of U.S. competitors can be assumed to be the main lures for investors. But Cuba's FTZs seem ambitiously large, spanning 1,250 hectares compared to 49 hectares in Panama's bustling Colón zone.⁹⁷ And it appears that capital for FTZ development has dried up. The FTZ director has acknowledged that the Cuban concessionaires of the Havana FTZs in operation are not planning to invest more capital; rather, they are looking for financing to continue developing to the planned levels. The Mariel and Cienfuegos FTZs, he reports, will need substantial foreign investment, as capital is unavailable in Cuba.⁹⁸ Moreover, the FTZ Director has given indications that FTZs are in experimental stage, stating: "We'll have to see if it's necessary to grant certain additional incentives or to decree complementary regulations to create a more adequate legal environment. This time frame will not be less than two or three years."⁹⁹ Unless dramatic changes are implemented, however, it is hard to imagine that Cuba's FTZs will turn into a success story. In the meantime, it seems that small enterprises eager to jump at opportunities in Cuba will be the ones taking the most advantage of this mode of investing.

THE INVESTMENT CLIMATE

Although in recent years there's been an upward trend in private investment in developing countries,¹⁰⁰ the competition to capture these funds is fierce. In Latin America, Chile—with a similar size population to Cuba's—received direct investment of US\$5.02 billion just in 1996.¹⁰¹ Poland, a transition

economy of the former Soviet bloc, received over US\$6 billion from 1990 to 1995.¹⁰² Conversely, Cuba has failed to attract meaningful levels of foreign investment, ostensibly due to its very high country risk.¹⁰³ Furthermore, those who do invest in the island typically commit low amounts and require high capital return/recovery ratios. To compensate for its shortcomings, Cuba's investment authorizations are thought to include enticing inducements with the government promising potential investors returns of up to 80% a year.¹⁰⁴ A Vice President of Altamira Management Ltd., which holds 11% of Sherritt, has illustrated the simple logic behind investor interest in Cuba: "Cuba's assets are incredibly cheap, and the potential return is huge."¹⁰⁵ Investors willing to take the risk may well reap high short term payoff.

There are no noticeable positive developments in the island's investment climate. The condition of the Cuban economy remains critically distressed and its prospects for recovery almost nil. Sugar prices have declined worldwide, as Cuba's output remains seriously impaired. In fact, it has been reported that if the value of the sugar industry were correctly calculated, it would be negative.¹⁰⁶ The Minister of Economy and Planning recently provided a grim outlook of the Cuban economy: "The state of economic emergency continues. (...) the Republic of Cuba has been surviving on short term credits (...) building up a short term debt with excessively high interest rates. (...) The foreign investment process is going reasonably well, though not as well as the government

97. "Cuba: born free," *The Economist Intelligence Unit*.

98. FTZ Director, Octavio Castilla, quoted in E. Rodríguez, "Zonas francas."

99. E. Rodríguez, "Zonas francas."

100. Foreign direct investment reached a new height in 1995, increasing by 38% from the previous year to US\$315 billion. *World Investment Report 1996*, UNCTAD, electronic overview. In 1996 private capital flows to developing countries alone totaled US\$244 billion and made up more than 80% of long term financial flows to poor countries. *The Economist* (March 29 1997), p. 116, citing the World Bank's report *Global Development Finance*.

101. Philip Sanders, "Foreign Investment in Chile leaped 42% last year," *Bloomberg News* (January 28, 1997). Authorized investments totaled US\$6.9 billion.

102. Values as of September 1995. U.S. companies have invested 30.5% of this total. "American vs. other foreign investors in Poland," Polish consulate in Chicago web page, updated 12/17/95.

103. See a more detailed explanation of country risk in Werlau, "Foreign investment," pp. 465-466.

104. "Castro's Capitalist," *Business Week*.

105. "Castro's Capitalist," *Business Week*.

106. "Castro's Capitalist," *Business Week*, p. 2.

would like.”¹⁰⁷ Cuba’s energy problems are particularly grave. Despite the increase in domestic oil prospecting and extraction (22 risk contracts for oil prospecting concessions have been completed with foreign companies) only 15% of the demand for oil fuel is being met locally.¹⁰⁸ In 1996 commercial energy usage rose 24% without a corresponding output increase (only 7%).¹⁰⁹ And, because Cuba’s hard currency debt is in default since 1986, it remains fundamentally shut off international credit markets.¹¹⁰

The legal environment and foreign investment regime remain highly risky, although some modest advances occurred in the regulatory arena targeting the external sector as a means of rescuing the ailing economy. On May 28, 1997 two laws were issued that seek “to effectively contribute to the economic/financial transformations taking place in the country” (i.e. to encourage foreign business).¹¹¹ The banking sector was reorganized by splitting in two the function of the National Bank: (1) Decree Law 172 established a Central Bank to oversee and regulate financial institutions and carry out the traditional roles of regulating monetary policy; and (2) Decree Law 173 relegated the National Bank to financial intermediation and commercial activity and codified bank regula-

tions in order to facilitate investment and trade. But the reforms are limited; the financial sector is far from reaching a modest or significant level of reform, both on the domestic and external sectors.¹¹² Foreign banks continue to be precluded from activities other than representative offices—of which there are 13—for the purpose of providing investments and serving foreign clients.¹¹³

In the FTZ law, the most significant element of reform is the establishment of 100% foreign-owned businesses, yet these remain of the traditional enclave type. The law disappointed those who had expected a relaxation in the labor regime characteristic of foreign joint ventures.¹¹⁴ Only non-Cuban and non-residents of Cuba may be hired directly by the FTZ operators. Generally, although exceptions *may* be permitted, Cuban employees will be hired from the Cuban concessionaire-controlled employment agency.

Serious deficiencies in the normal conduct of business persist.¹¹⁵ A business newsletter on Cuba recently acknowledged that “foreigners consider Cuba to be a very expensive place to develop and produce business.” Adding to the already high costs, it cites Cuba announcement of mid-1997 that foreigners who re-

107. *Economic Eye on Cuba* (21-27 April 1997), citing highlights of interview given by Minister José Luis Rodríguez to Cuba’s official business weekly *Negocios en Cuba*.

108. Joaquín Oramas, “Seguirán crecimientos en la industria del petróleo,” *Granma Internacional* (28 julio 1997), ed. digital

109. *Cuba Monthly Economic Report* (July 1997), p.1.

110. Cuba owes approximately US\$10 billion to Western creditors—European and Japanese banks—and has a huge debt with the former Soviet Union. A conversion of this debt must be worked out, but Moscow claims it amounts to 17 billion “transferable rubles.” It was reported in the summer 1997 that once a conversion of the ruble debt is worked out, Russian companies would likely obtain equity in certain Cuban enterprises in lieu of the debt. Cuba still depends on an economic relationship with the former USSR; it conducted in 1996 trade of US\$1.1 billion with Russia, of which 85% was barter, mostly sugar for oil. See “Cuban ambassador offers sweeteners,” *Central European* (July/August 1997), p.9.

111. Francisco Soberón, the former National Bank President, assumed the Presidency of the new Central Bank. “Creado el Banco Central de Cuba,” *Granma Internacional*; E. Rodríguez, “Firma contratos.”

112. See Yosem Companys, “Institution building: A regulatory and supervisory framework for Cuba’s financial sector reform,” Yale University (March 29, 1997). A version of this paper is included in this volume. Ed.

113. *Economic Eye on Cuba* (9-15 June 1997).

114. The law established that Cuban FTZ concessionaires (companies of the Republic of Cuba or joint ventures between foreigners and these companies) may establish their own employment offices—apart from Cubase—and may provide contracted Cuban nationals with U.S. dollar or U.S. dollar-based bonuses. *Economic Eye on Cuba* (28 April-4 May 1997). Although the Executive Committee of the Council of Ministries has the authority to provide special labor regulations for operators, it appears that only Cuban or joint ventures companies, not 100% foreign owned concessions, will be allowed to do this. *The Cuba Report* 5:5 (September 1996), p. 7.

115. See Werlau, “Foreign investment,” pp. 465-480.

side in Cuba for more than 180 days must file income tax returns.¹¹⁶ A University of Havana study, a telling source due to its origin, has detailed some of the problems business partners and potential investors confront:¹¹⁷ 1) bureaucratic delays and slow completion of investment agreements; 2) highly cumbersome bureaucratic procedures for renting commercial space or obtaining transportation, telecommunications and personal services; 3) unfamiliarity with market techniques and a lack of historic entrepreneurial experience; 4) unavailability of qualified personnel for certain areas; 5) absence of economically sound reference points for the application of exchange rates and prices in the valuation of the assets of the Cuban partners; 6) problems with the employment regime, particularly doubts concerning the loyalty of the workers to the foreign partners; and 7) absence of local financing.

The climate for doing business does not seem to have improved much. Canada's Wilton Properties, which announced a US\$400 million investment project in tourism in 1996, has allegedly pulled out of at least one of its projects (*El Viejo y el Mar*) for a number of reasons including problems with the Cuban partner.¹¹⁸ Although Sherritt's Chairman, Ian Delaney, stated that large multinational companies have an advantage in obtaining access to the highest levels of government, allowing for the completion of agreements quickly, he acknowledged that Cuba "needed to do more to provide clear rules and regulations that would apply to small and medium-sized firms."¹¹⁹ Sherritt is a prime example of the foreign investors who might benefit, at least in the short term, from the highly centralized and "flexible" nature of the

terms for investing, considered by Cuba as a lure to investors.¹²⁰

But investors stay happy as long as arbitrary decisions of the Cuban state do not affect their best interests, as has been seen in several cases in the past years.¹²¹ The recent falling out of the notorious joint venture investment by Mexico's Grupo Domos in Cuba's telecommunications company, ETECSA, is the most recent example. Apparently, Domos ran into problems obtaining financing for a portion of its share of ETECSA and was forced by the Cuban government to divest of its stock at a lower than market value. Allegedly, the stock was then sold by the government to the Italian company STET at a much higher price. Domos was said to be "studying its options to reclaim the \$450 million it paid for the original investment" and has sued STET, claiming compensation for a minimum of \$900 million. The Domos case is particularly poignant because from beginning to end it demonstrates the pitfalls of investors' "accessibility" to extremely centralized decision-making and the negotiation of agreements lacking in transparency and accountability. It might be noted that many foreign mining companies with operations in Cuba are not major industry players and at least one—Northern Orion—has been cited by market analysts as involved in investments in Cuba considered "speculative" and "highly risky."¹²² Domos, for example, was less than an ideal partner; even the President of the U.S.-Cuba Trade and Economic Council admitted that its "problems stem in large part from the fact that they weren't a company with substantial assets going into the deal."¹²³ A little known company with limited experience in the telecommunications sector,

116. *The Cuba Report*, 6:1 (May 1997), p. 8.

117. O. Pérez Villanueva, *La inversión extranjera*, pp. 20-21.

118. The Cuban partner was allegedly playing games with cash flow and overbooking space by selling rooms to Europeans for more money than the Canadian hotel management firm, Delta, had sold to Canadian travel agents. (Anecdotal information from a confidential source.)

119. *Economic Eye on Cuba* (3-9 March 1997).

120. O. Pérez Villanueva, *La inversión extranjera*, p. 12.

121. See Werlau, "Foreign investment," p. 69 and footnote 78.

122. *The Cuba Report*, 5:9 (February 1997).

123. Larry Rohter, "Mexican conglomerate abandons Cuban phone venture," *The New York Times* (June 30, 1997).

was apparently chosen over European and Canadian competitors due to the close political relationship between Cuba and Mexico. Reportedly, the Domos deal, which granted Domos a 55-year monopoly on telephone services in Cuba, was put together with the intervention of former Mexican President Carlos Salinas de Gortari.¹²⁴

Socio-political risks in Cuba remain high. Aside from recent bombings linked to the tourism industry, the media reported that in September 1997, several foreigners, including Spanish director Pedro Almodóvar and Swedish actress Bibi Anderson, were caught in a violent raid by Cuban security forces at a Havana discotheque. Those not carrying their identity documents were detained with many Cuban patrons. Social resentment against what foreigners represent apparently has not abated.¹²⁵ While Havana University's MBA program graduated its first class in February, one of the graduates gripes: "I am studying about investing capital when Cubans cannot invest in Cuba. If you are a foreigner, you can invest. But if you are a Cuban, no."¹²⁶

The condition of human rights in the island has not improved. Again, claims have been made against the

government for utilizing telephone services to harass dissidents. (ETECSA, Cuba's telephone company, is a joint venture with foreign capital.¹²⁷) The crack-down on dissidents initiated in late 1995 has been followed by successive waves of repression specifically targeted at independent journalists and dissidents who attain international media coverage.¹²⁸ In mid-July, for example, four dissident leaders who had distributed a joint paper to foreign media representatives were detained. All four remain in custody, accused of releasing false and inexact data about the Cuban economy with the intention of "negatively influencing internal and international public opinion and especially existing and potential partners and investors."¹²⁹

As for the environmental impact of foreign investment, international awareness was raised during the United Nations June 1997 Earth Summit+5 meeting in New York, which Castro did not attend as expected. Exile environmentalists, in conjunction with Castro's daughter Alina Fernández, held a press conference which received international media coverage.¹³⁰ The damage caused by foreign investments in tourism and mining, specifically by Sherritt's joint ven-

124. For sources/details on the Domos investment, see Addendum referenced in footnote 36 available from the author and Werlau, "Foreign investment," p. 463, footnote 45.

125. A recent independent journalist's report from Cuba reads: "There are many tourism projects not lacking in cement, sand, gravel or any other construction material, all of which are nationally produced. ...while entire families from Camagüey languish in homes without maintenance, built more than 300 years ago. Meanwhile, tourists are provided with modern and comfortable buildings, in which they can vacation happily. We don't know how long we can continue putting up with the situation to which the government subjects us." Carlos Manuel Guerra González (Patria Agency), "From Cuba: the other side of the coin," Camagüey (December 1996), distributed by *CubaNet*; slight translation modifications by the author.

126. "A touch of capitalism," *Business Week*.

127. For example, the Independent Press Agency for Oriente denounced government threats to one of its journalists to cut off telephone services and insinuated the monitoring of private conversations. "From Cuba: the government threatens independent journalists with canceling their telephone line" (October 21, 1996), distributed by *CubaNet*.

128. See for example, Press release from Havana from the Cuban Independent Press Bureau (June 27, 1996), distributed by *CubaNet* and *Amnesty International Urgent Action Appeal* (July 18, 1997).

129. Those held form part of the *Internal Dissidents' Working Group for the Analysis of the Cuban Socio-Economic Situation* and are members of unofficial organizations: Marta Beatriz Roque Cabello, of the *Cuban Institute of Independent Economists*, René Gómez Manzano, of the lawyers' group *Corriente Agrarionista*, Felix Bonne Carcassés of the *Corriente Cívica Cubana*, and Luis López Prendes of *Buró de Prensa Independiente*. The detainees were also accused of producing a letter to foreign businessmen warning them of the consequences of investing in Cuba under the one-party Communist government, of calling for the boycott of upcoming one-party elections and of involvement with leaders of terrorist groups based in the United States. See *Amnesty International Urgent Action Appeal* (July 18, 1997) and Pascal Fletcher, "Cuba explains arrests of four dissidents," *Reuters* (July 24, 1997).

130. Press conference held at Hyatt U.N. Plaza, New York, June 24, 1997 by the *Coalition for a Green and Free Cuba*, with the participation of Alina Fernández with Néstor Penedo and Andrés Solares of the A.M.A.C. (Asociación Medio-Ambiental Cubana).

ture plant at Moa Bay, was cited.¹³¹ The Juraguá Nuclear Plant, which Cuba is actively seeking to complete with foreign financing, was also named as a potentially serious hazard.¹³² On the other hand, foreign investment may bring some improvements to the environment. Sherritt reported the continued refurbishment and rehabilitation of two sulfuric acid plants at Moa Bay, with “considerable improvements in air quality,” although still not meeting international standards.¹³³ Although the Moa joint venture has been criticized for its environmental impact, if foreign capital were not available, it is unlikely that the Cuban government, particularly at this time of crisis, would earmark important financial resources to protect the environment, which it recognizes is severely deteriorated.¹³⁴ Allegedly these mining facilities have historically been heavy polluters. Cuba, meanwhile, passed a new law on the environment,¹³⁵ but its potential consequences for foreign investors are unknown at this time. Nonetheless, reportedly it would regulate the environmental impact of foreign investments “which could become a potential source of income for the state.”¹³⁶

In the international arena, public sensitivity over ethical issues seems to be growing at the governmental and corporate levels, as witnessed recently by Nike in Indonesia and Unocal in Myanmar.¹³⁷ *The New York Times* recently reported on oil industry experts agreeing that “the threat of unilateral economic sanctions... has become a shadow over investment decisions stretching for Southeast Asia to West Africa to the Caspian Sea.”¹³⁸ Meanwhile, the international outcry over Holocaust funds secretly kept by Swiss banks has bolstered the arguments of Helms-Burton proponents.¹³⁹

The United States’ Helms-Burton Law¹⁴⁰

The international outcry and defiance against the Helms-Burton (HB) Law has not abated. The European Union (EU) and several individual countries took steps to block the enforcement of U.S. judgments respective of HB measures range in intensity from mere discouraging language to “claw-back” provisions (allowing the recovery of legal awards) and the penalization of compliance.¹⁴¹ For its part, Cuba passed a counter-measure—*Law of Re-affirmation of Cuban Dignity and Sovereignty*—declaring HB “null

131. Investments in the tourist industry were described as neglecting environmental considerations to reduce costs. Causeways to small keys have been constructed taking the cheapest routes which block water flows, exacerbate contamination, and destroy coastal and marine habitats. As a result, species such as the Cuban shrimp are reported to be disappearing. In Varadero beach too many and poorly constructed hotels are being built too close to the beach and with inadequate space between buildings. See *The State of the Cuban Environment* (June 1997), press kit distributed at 6/24/97 press conference in New York city by the *Coalition for a Free and Green Cuba*.

132. The Soviet-designed reactors are deficient even by Soviet standards and Juraguá is just 180 miles off the coast of Florida. *U.S.-Cuba Policy Report*, 4:3 (March 31, 1997).

133. Sherritt International Corporation, Annual Report 1996 (fiscal year ending 12/31/96).

134. *National Environmental Strategy*, presented by Cuba at the United Nations’ Earth Summit+5, New York, 7/97.

135. Rodolfo Casals, “Tres nuevas leyes aprobó el parlamento,” *Granma Internacional* (28 julio 1997), ed. digital.

136. “Cuba assesses damage, finds it extensive,” *CubaNews* (July 1997), p. 11

137. The story covered Unocal’s problems in Myanmar—where it has already invested US\$1.2 billion to develop a natural gas field. Agis Salpukas, “Foreign energy, domestic politics: Burmese project tests Unocal resolve,” *The New York Times* (May 22, 1997).

138. Referring to Unocal’s problems in Myanmar, where it has invested US\$1.2 billion to develop a natural gas field.

139. A piece authored by a legal expert states: “The Holocaust principle demanding restoration of stolen property from traffickers or custodians is high-minded: it loses none of its moral strength when the plundered are gentiles, not Jews. Indeed, the principle fits the controversial Helms-Burton law like a glove, and should become a bedrock of international law.” “Applying Holocaust Principles to Cuba,” TWT (2/4/97). Cited in *U.S.-Cuba Policy Report* 4:2 (February 28, 1997), p. 10.

140. For details on this issue, please refer to Werlau, “Foreign investment,” pp. 472-473.

141. In October 1996 Mexico passed the “Act for the Protection of Commerce and Investment of Foreign Rules Contravening International Law,” which does not penalize companies from withdrawing from Cuba nor revoke visas to American executives whose companies file HB suits against Mexican companies. *U.S.-Cuba Policy Report*, 3:10 (October 31, 1996). The EU took action in November 1996. Amendments to Canada’s Foreign Extra-territorial Measures Act (FEMA) countering HB became effective in January 1997. France passed legislation in April 1997 to impose financial penalties on companies which ignore the EU’s agreement to defy HB. “Amplía Francia legislación anti Helms Burton,” *Granma Internacional* (16 abril 1997), ed. digital.

and void” and setting up commissions for Cubans to file claims against the U.S. for damages and injuries resulting from the embargo.¹⁴² The Cuban government is warning embassies whose businesses are potentially endangered by HB that Cuban laws declare illegal any form of collaboration, direct or indirect, to assist in the application of the HB law.¹⁴³

The U.S. State Department has issued letters warning of potential claims under the Helms-Burton law to several companies suspected of trafficking in confiscated U.S. properties. These include Canada’s Sherritt,¹⁴⁴ the Israeli Group BM and a Panamanian company selling automobiles in Cuba, in addition to Mexico’s Grupo Domos and CEMEX, both of which have reportedly ceased operations in Cuba.¹⁴⁵ More companies are vulnerable to Helms-Burton sanctions, including Title IV visa denials.¹⁴⁶

Cuba’s Minister for Foreign Investment has announced that the Helms-Burton law has not provoked the flight of any foreign investor and, instead, foreign investment has risen.¹⁴⁷ From the passage of the law in March 1996 to December of that year, 42 economic associations with foreigners were professedly established.¹⁴⁸ Meanwhile, the Deputy Minister for Foreign Investment Octavio Castilla report-

ed that only four joint ventures are linked to property formerly owned by U.S. firms.¹⁴⁹ But there are obvious signs that the law has indeed had a significant impact on foreign investment climate. A high official of Cuba’s Foreign Ministry, Carlos Fernández de Cosío, acknowledged in January 1997 that as a result of the law, many people were afraid of investing in Cuba.¹⁵⁰ Minister Carlos Lage acknowledged the Act had “complicated” Cuba’s relationships with some foreign enterprises and even Castro has admitted it has had “serious negative consequences” and has endangered foreign credits needed to reactivate main sectors of the economy, particularly sugar production.¹⁵¹ Netherlands’ ING-Barings Bank stopped financing Cuba’s sugar harvest because of the HB law and one of its executives declared it would remain active in Cuba “in activities in line with the Helms-Burton law.”¹⁵² Spain denied the extension of US\$15 million in pre-negotiated loans for Cuba’s sugar harvest after uncovering “technical problems” in loan insurance risk analysis; one might assume that HB weighed in the decision.¹⁵³ Allegedly HB also contributed to Domos’ problems by making alternative financing for its investment in ETECSA more difficult.¹⁵⁴ The law has also been cited as an impediment for Cuba to raise the financing to complete construc-

142. *U.S.-Cuba Policy Report*, 3:12 (December 31, 1996), p. 4.

143. Pascal Fletcher, *The Washington Post* (April 7, 1997), cited in the *Newsletter of the American Chamber of Commerce of Cuba in the United States* (April 23, 1997), p. 2.

144. Eleven persons affiliated with Sherritt are said to be barred from the United States. *The Cuba Report*, 5:11 (April 1997), p. 8.

145. Christopher Marquis, “Two firms face Helms-Burton sanctions,” *The Miami Herald* (January 22, 1997) and *U.S.-Cuba Policy Report*, 3:5 (May 31, 1996). Before it sold its stake in ETECSA, executives of Grupo Domos had also received warning letters for denial of entry into the U.S.

146. These include Italy’s Benetton, Spain’s Sol Meliá, France’s Pernod Ricard, Britain’s ED&F Man and Tate & Lyle and Bancomext, Mexico’s foreign trade bank. The latter has provided US\$400 million in soft credits to Cuba since 1992, and has a cement plant joint venture with Cuba’s Cement Producers. *Economic Eye on Cuba* (26 May-1 June, 1997); *U.S.-Cuba Policy Report*, 3:9 (September 27, 1996).

147. Eloy Rodríguez, “Califican de exitosa gira de ministro a Alemania y Francia,” *Granma Internacional* (13 mayo 1997), ed. digital.

148. J. Oramas, “Turismo,” and S. Lee, “Hemos.”

149. “Cuba says few firms using old U.S. property,” Canadian Press, Havana (June 18, 1997).

150. *U.S.-Cuba Policy Report*, 4:1 (January 31, 1997), p. 10, as per *The Washington Post* (January 25, 1997).

151. “Castro admits that Helms-Burton has hurt the Cuban economy,” *El País* (September 18, 1996). Distributed by *CubaNet*.

152. *U.S.-Cuba Policy Report*, 3:9 (September 27, 1996), p. 8.

153. Javier Rodríguez, “Niega Cabrisas que haya razones técnicas en la cancelación de crédito español,” *Granma Internacional*, 2:6 (20 febrero 1997), ed. digital.

154. Larry Rohter, “Mexican conglomerate abandons Cuban phone venture,” *The New York Times* (June 30, 1997).

tion of the Juraguá nuclear plant in Cienfuegos.¹⁵⁵ Canadian banks remain nervous about lending to Canadian investors in Cuba and a drop in Canadian exports to the island¹⁵⁶ might also be attributed to limited financing alternatives. (The Canadian government is said to be offering seed funds to investors.¹⁵⁷)

Potential investors and other businesses are showing concern. Canada's then Ambassador to Cuba, Mark Entwistle, confirmed in January 1997 that investments from larger Canadian companies had leveled off since the passage of the law due to their asset exposure in the U.S. Although he reported that investments from medium-sized companies with no exposure in the U.S. were on the rise, their ability to invest can be assumed to be much more limited.¹⁵⁸ Beta Gran Caribe Fund has announced a policy to not "knowingly and intentionally" invest in property in respect of which there is significant risk of significant liability as a result of an outstanding claim certified by the U.S.¹⁵⁹ Several foreign companies, including the U.K.'s largest tour operator, Thomson Travel Group, have reportedly communicated with the

State Department to make certain that their business activities do not violate the HB Act.¹⁶⁰

In August of 1996 President Clinton named Ambassador Stuart Eizenstat special representative to negotiate with allies on the issue of HB, to seek multilateral Cuba policies, specifically "concrete and specific measures to promote democracy in Cuba." Eizenstat initiated several rounds of foreign tours, visiting 12 countries. These efforts yielded several important successes despite a bleak start in Mexico City, where the envoy was pelted by eggs.¹⁶¹ In November 1996 the EU issued a common position on Cuba focused on encouraging a process of transition to a pluralist democracy in Cuba and conditioning full cooperation with Cuba upon improvements in human rights and political freedom in the island.¹⁶² In April 1997, shortly before initial papers were to be filed before a WTO dispute panel requested by the EU in February 1997, the U.S. and the EU announced their agreement to suspend the panel for six months,¹⁶³ with the EU reserving the right to reactivate the panel at any time if negotiations are unsuccessful. Terms

155. Cuba, which spends over US\$1 billion annually to import oil, has renewed efforts to complete the plant, in which the former USSR had invested most of the US\$1.1 billion to construct two 440 megawatt nuclear reactors. Construction which began in 1983, was suspended in September 1992 with the reactors 75% and 30% complete respectively. The Soviets are said to have demanded a \$200 million payment to continue the project. Cuba has used an annual US\$30 million Russian Federation grant to mothball the existing facility and is actively seeking foreign investors to complete the first reactor at a cost of US\$750 million. Russia's Deputy Minister of Atomic Energy claimed the U.S. had rejected an offer made to Westinghouse Electric Corp—probably its Canadian subsidiary—to participate in the completion of the power plant and referred to the HB law as the legal impediment. The Minister of Nuclear Energy of the Russian Federation has announced that construction will resume in 1998 through a consortium. Companies from the U.K, Germany, and Brazil have allegedly expressed interest, although it appears financing is still being sought. See *Economic Eye on Cuba* (2-8 June 1997); Frank J. Gaffney and Roger Robinson, "Stop the Cuban Chernobyl," *The Wall Street Journal* (January 21, 1997); and *U.S.-Cuba Policy Report* 4:2 (February 28, 1997).

156. Professor John Kirk, Dalhousie University, Canada, in e-mail to the author of 7/28/97.

157. Ibid.

158. *U.S.-Cuba Policy Report*, 4:2 (February 28, 1997), p.8.

159. *The Cuba Report* 6:1 (May 1997), p. 8.

160. Michael Rannenberger, Director of the Cuba Office at the U.S. State Department, reported having received word from 12 companies of ceasing business in Cuba to comply with the H.B. law. (April 1997, in conversation with the author).

161. Steven Lee Meyers, "Cuba policy a big headache for top commerce official," *New York Times News Service*, Washington, 1996.

162. The Council of the European Union, Common position, Brussels, November 29, 1996. See *U.S.-Cuba Policy Report*, 3:12 (December 31, 1996).

163. On April 21, 1997, the EU approved the April 11 accord, which was cited as an "acceptable compromise." *U.S.-Cuba Policy Report*, 4:2 (February 28, 1997). The EU claims the extraterritoriality of the HB law whereas the U.S. categorically declares it would not recognize WTO jurisdiction over an issue of national security, hinting that bringing non-trade matters to the WTO jeopardized the legitimacy of the recently-created international body.

of the accord include:¹⁶⁴ (1) continued negotiations (sought to be completed by October 15, 1997) to develop agreed disciplines and principles for the strengthening of investment protection; (2) continued U.S. suspensions of Title III claims provision;¹⁶⁵ and (3) once an accord is reached, the Clinton Administration would seek a Congressional amendment to the HB law to provide the President with authority to waive Title IV (denial of visa) provisions.

In addition to the accord, the most threatening counter-sanctions, such as EU visa denials for U.S. executives, the freezing of U.S. assets and counter-suits,¹⁶⁶ have not materialized. Moreover, STET, the Italian company in a telecommunications joint venture with Cuba, recently completed a 10 year agreement with ITT to pay the latter US\$30 million to use ITT's properties in Cuba. The accord relieves STET from penalties under the HB law and allows ITT to retain its US\$130 million claim against the government of Cuba.¹⁶⁷ The U.S. government and HB supporters have claimed this as legitimizing of HB, a proof that the law is effective and acts as a disincentive to investment in Cuba. In turn, HB detractors, including the EU, claim it demonstrates that the law is toothless.¹⁶⁸

Canada has taken the most active stance against HB. Its Ambassador to Washington declared that this was

the most visible issue between the two countries and that Canada would not let go of its position on HB.¹⁶⁹ But, it appears that a coalition of 20 church, labor and relief groups from Canada which called for a tourist boycott of Florida—to punish its population of Cuban origin—was unable to attain any success. (Around 2 million Canadian tourists visit Florida, almost 13 times the 156,000 which visit Cuba.¹⁷⁰) And, if push comes to shove, it would seem that Canadians will prioritize investments and trade with the U.S. Canada's annual trade with Cuba reportedly equals one day of its trade with the United States.¹⁷¹ At this time no Canadian investors have been reported to have retreated from Cuba due to the law, but it seems that Canadian Foreign Extraterritorial Measures Act regulations which penalize these actions would be hard to enforce, as investors could cite other causes for leaving Cuba.

In sum, it looks like the international clamor against HB has not toned down in volume, but actual results to strike down the law are less forthcoming. All told, HB appears here to stay.

FOREIGN INVESTMENT'S IMPACT ON REFORM

Creation of Employment

As an element of empowerment, the overall impact of foreign investment on employment is relatively

164. *U.S.-Cuba Policy Report*, 4:4 (April 30, 1997) and *The Cuba Report*, 6:1 (May 1997), pp. 2-3.

165. On July 16, 1997, President Clinton suspend Title III claims for the third time. See Alison Mitchell, "Clinton again waives penalty on foreign companies in Cuba," *The New York Times* (July 17, 1997).

166. Mark Lawrence, "EU threatens retaliation unless U.S. waives Cuba sanctions," *Associated Press*, Brussels (July 12, 1996).

167. "ITT in deal for properties seized in Cuba in '61," *The New York Times* (July 24, 1997), p. A8; "ITT makes deal with Italian company," July 23, 1997, *Associated Press*, distributed by *CubaNet*.

168. State Department Spokesman Nicholas Burns, in David Fox, "EU, US both claim victory in Helms-Burton twist," *Reuters*, Brussels (July 24, 1997), distributed by *CubaNet*. Also see Sue Fleming, "U.S. official asks Latin America to support Cuba moves," *Reuters*, Washington (July 28, 1997), distributed by *CubaNet*.

169. *U.S.-Cuba Policy Report*, 3 (October 31, 1996), p. 10.

170. See David Crary, "Groups urge boycott of Florida unless U.S. eases anti-Cuba bill," *Associated Press*, Toronto, (July 10, 1996). About 1.7 million Canadians spent US\$1.8 billion in 1996 in Florida.

171. *U.S.-Cuba Policy Report*, 4:2 (February 28, 1997), p. 8. In 1995 Cuba's imports from Canada totaled US\$200 million; exports from Cuba to Canada totaled US\$234 million. As per official Canadian trade data, in *Cuba: Handbook of Trade Statistics, 1996* (Washington: CIA, Directorate of Intelligence, November 1996). Prof. Julia Sagebien, of Canada's Dalhousie University, claims that Canada's trade with Cuba equals half a day of Canada's trade with the United States. "Canadians in Cuba: Getting to Know Each Other Better," presentation at the VII Annual Meeting of the Association for the Study of the Cuban Economy, Miami, August 1997. A version of this presentation is included in this volume. Ed.

meaningless and, in some respects, even detrimental. Despite anticipation that Free Trade Zones would feature direct employment of workers, the actual terms of the legislation thwarted these hopes.¹⁷² Moreover, FTZs have added very little employment—around 150 workers at present¹⁷³—and a continued focus on the guaranteed pre-selling of their output to Cuban enterprises for domestic consumption leaves no expectation of large-scale production¹⁷⁴ or important levels of employment.

By 1996 it had been reported that all foreign joint ventures “officially” employed 60,000 workers.¹⁷⁵ Given that estimated foreign investment has not risen significantly, we might assume no material change in the number of workers employed by joint ventures. This represents a mere 1% of the workforce of 4.5 million.¹⁷⁶ (Direct employment in tourism is only 65,000 to 70,000 and indirectly 200,000 to 250,000,¹⁷⁷ but the number of workers employed in the foreign sector is unknown.)

This scenario reinforces our conclusion in last year’s analysis: (1) with the unemployed said to be over a million (some estimate unemployment at around 50%, or 2.25 million), the number of workers employed in the foreign investment sector cannot significantly alleviate Cuba’s grave unemployment crisis;

(2) given the conditions of the domestic and international labor markets, competitive market forces would likely make the cost of labor for foreign capital firms in Cuba much lower. Due to Cuba’s singular labor arrangement, by arbitrarily fixing an artificially high price for labor, the state actually discourages and limits optimal employment by foreign capital firms; and (3) the limited number of jobs sought by a huge pool of workers in the foreign sector—the most desirable sector of the economy—instead of empowering the workers, actually reinforces the need to play by the government’s rules.¹⁷⁸

Generation of Hard Currency Earnings

Earnings derived from operations of foreign joint ventures had been estimated by June 1996 at roughly US\$211 million.¹⁷⁹ Given the presumption that foreign investment has not risen significantly in the past year, it can be assumed that this scenario has not changed materially.

The tourism industry was officially reported as Cuba’s largest dollar earner in 1996. Because revenues derived from foreign investment in tourism are not available, our conclusions must be based on overall data available for the industry. 1996 net revenues are noted inconsistently by different sources—reports range from 26% to 30-35%.¹⁸⁰ Yet, if tourism gener-

172. Only non-Cubans and non-residents of Cuba may be hired directly. The Executive Committee of the Council of Ministers has authority to provide special labor regulations for operators, but it appears that only Cuban or joint ventures operators will be allowed to hire workers from concession-managed employment agencies. See FTZ law, Chapter VIII, Section V and *The Cuba Report*, 5:5 (September 1996), p. 7.

173. The largest FTZ investor was a Canadian company producing building materials, reportedly employing 80 workers.

174. J. Kavulich, telephone conversations with the author, 5/12/97 and 7/11/97.

175. The number employed in joint ventures in the tourist sector is unknown. For the whole industry, in May 1997 the National Assembly of Cuba reported 130,000 employed (*Economic Eye on Cuba*, 26 May-1 June 1997) while the President of INTUR, reported 150,000 employed directly or indirectly at around the same date. *Economic Eye on Cuba*, 21-27 April 1997.

176. Employment as of 4/30/97, as reported by Cuba’s National Tax Office (*Economic Eye on Cuba*, 2-8 June 1997).

177. The E.C.L.A. report (op.cit., p. 129) cites 65,000 employed directly and 200,000 indirectly, while Cuba’s Deputy Minister of Tourism cited in September 1997 70,000 and 250,000 respectively. “Reconocen...” *El Nuevo Herald* (24 September 1997).

178. Despite very low wages, the material conditions of workers in the foreign enclaves is better than the rest. Workers are compensated with bonuses, gifts, transportation to work, meals, and in some cases dress. In the tourist sector, they receive tips and food served at the restaurants. These make jobs in this sector the most prized. Werlau, “Foreign Investment,” p. 484.

179. Based on \$751.9 million invested: \$114 million from operations (Minister Lage’s report for 1995) plus our calculation of \$97.5 million in taxes of 30%. (Tips are not included, as it is very difficult to estimate a reliable number.) Telecommunications’ payments made by U.S. companies constitute additional hard-currency earnings for Cuba.

180. Cuba had reported that costs per dollar of income dropped in the first half of 1996 to US\$0.68 from US\$0.73 (*The Cuba Report*, August 1996, p. 4), but these reports show costs ranging from US\$0.65 to US\$0.74. Data as per Cuba’s Ministry of Tourism. *The Cuba Report*, Volume 5, No. 9, February 1997, p. 3; O. Pérez Villanueva *La inversión extranjera*, p. 14.

ated net revenues of 26% this would represent a mere US\$338 million, which is low given the size of the population and the needs of the economy. Nevertheless, reported expenditures from these revenues totaled only US\$84 million; these financed imports of US\$66 million of food and agricultural and light industrial goods for the population while US\$18 million was spent in the development of tourism.¹⁸¹ (The latter is a strangely low sum in relation to the importance of this sector in the overall economy and Cuba's continued investment in new hotel rooms.) Even the government has recognized that 1996 revenue projections for tourism were not met.¹⁸² While the number of tourists visiting the island in 1996 increased by 28%, earnings rose only 23%. From January to April 1997 the number of tourists increased 19% while gross earnings rose only 7%, officially due to a 6.7% decline in the average number of days of tourists' visits.¹⁸³ In fact, the Minister of the Economy reported a loss of US\$3 million in the tourist industry for the first four months of 1997 (costs increased 1%), indicating that plans to improve efficiency/profitability have not materialized.¹⁸⁴ Analysts have traditionally estimated net revenues for tourism to be low due to a high dependence on imports, reportedly 70-80%,¹⁸⁵ hefty promotional discounts and mismanagement by the Cuban partners.

Plus, a low ratio of repeat tourism indicates that Cuba needs to dedicate expenditures to upgrade its services and facilities in order to remain competitive. In essence, without underestimating the importance to Cuba's deprived economy of tourism revenues tied to foreign capital, this does not appear to be a short-term answer to its predicament.

The disappointingly low level of revenues estimated from foreign investment, even from tourism, continues to make the wage retention arrangement of foreign capital firms the most lucrative source of hard currency earnings for Cuba from foreign capital enterprises.¹⁸⁶ (The new Free Trade Zones are also subject to this system.¹⁸⁷) Wage retention generates the government a guaranteed income irrespective of whether these enterprises—joint ventures or economic associations—operate profitably or not, as state employment agencies continue to appropriate around 98% of the total value added of labor in the production process. In the case of specialized and highly-skilled workers, the confiscation rate is even higher.¹⁸⁸ Sherritt International Corporation, for example, is reported to be turning over to the Cuban government US\$22 million per year for workers' salaries.¹⁸⁹ Just at its joint venture Moa Bay nickel-cobalt plant the wage retention scheme alone is estimat-

181. O. Gómez Balado, "Llegó ..." *Granma*, op.cit. (The inventory of hotel rooms has grown to 28,878 by 1996, at an annual average rate of 22.2% since 1990. According to official projection, the number will reach 50,000 by the year 2,000. N. Crespo and S. Negrón Díaz, "Cuban Tourism in 2007: Economic Impact," in this volume.)

182. O. Pérez Villanueva, *La inversión extranjera*, and *The Cuba Report*, February 1997, p. 3.

183. As per Republic of Cuba reports, *Economic Eye on Cuba*, 30 June-6 July 1997.

184. *Economic Eye on Cuba*, 30 June-6 July 1997.

185. *Cuba Monthly Report*, DevTech Systems, Vol. 1, No. 3, July 1997, p. 2. (The development of tourism requires substantial expenditures to remain competitive—promotional costs, personnel training, construction of new facilities, maintenance of existing facilities, and infrastructure development.)

186. A state-controlled employment agency hires the workers and charges the foreign capital firm salaries of an average of around US\$450 per worker. The workers are paid average peso wages of around US\$9. (Also see Werlau, op.cit., p.471.)

187. While the worker is earning 300-500 Cuban pesos, *Cubalse*—the state employment agency—is receiving approximately US\$450 per worker from the FTZ operator. (J. Kavulich, telephone conversation, 5/12/97.)

188. The Cuban-Brazilian joint venture producing cigarettes is reported to pay the state employment agency US\$3,000 per month for its manager, who in turn receives 380 pesos (US\$17.3), at a confiscation rate of 99%, leaving the government US\$35,792 in annual revenues. A mechanic at the plant receives 350 pesos while the employment agency gets US\$916. Likewise, the employment agency is reported to receive US\$2,700 for a geologist employed in Sherritt, while the geologist receives the equivalent of US\$10—at a wage confiscation rate of 99.6%—providing the state a return of US\$32,280 per year. (Charles Lane, "Canada Sly," *The New Republic*, August 6, 1996.)

189. *Cuba Monthly Economic Report*, July 1997, p. 3.

ed to leave the state at least around US\$740.5 thousand per month, or US\$8.9 annually (this without adding labor taxes and social security retention).¹⁹⁰ In 1995, before the existence of FTZs, earnings from wage confiscation in joint ventures are calculated to have totaled around three times the net earnings from operations. (With 60,000 workers in the foreign sector, wage conversion alone can bring around US\$26.5 million per month, or US\$317.5 million per annum. In addition, labor utilization taxes and social security contributions provide an estimated US\$33 million per month, US\$396.8 million per annum.¹⁹¹) Ostensibly, this situation hasn't changed much, with the exception of the FTZs, which will add to the state's appropriation of workers' salaries and benefits.

Meanwhile, the purchasing power of the workers is pitiful. The average monthly salary of 202.5 pesos (US\$9.20) translates into US\$2.19 per week, equal to US\$0.44 a day or 5.5 cents an hour, which could well be the lowest in the world.¹⁹² Economists in Cuba have estimated that, in order to buy goods at free market rates, workers on the average 202.5 peso per month salary have to labor 116 hours to purchase 1 kg. of powdered milk, 70 hours for 1 kg. of chicken, 13 hours for one lightbulb, and between 500-1,700 hours for a pair of shoes.¹⁹³ Some workers of joint ventures or under management contracts of foreign companies, subject to the same average peso salaries, are being reported as having access to hard-currency bonuses of a small percentage of their salaries. The sums involved are very low, but represent a sig-

nificant amount in Cuba.¹⁹⁴ Non-monetary benefits for workers of foreign joint ventures have endured: rewards such as meals, transportation, and uniforms. Moreover, material incentives for non-joint venture workers have been expanded; these can partly be attributed to the government's attempt to compensate for the special benefits of workers of the foreign sector. Last year, approximately one million workers, 25% of the labor force, had been estimated to be receiving some form of payment in dollars or convertible pesos as reward for meeting or exceeding work quotas. Presently, some 1.3 million workers—according to the government, one third of the workforce—are reportedly receiving bonuses for greater output. The problem is that these workers remain dependent on the state. Therefore, any material improvement in their situation—both the employed at joint ventures or exclusively by the state—is at the expense of even greater political compliance and economic dependence on the state. At the same time, the government continues to refuse allowing average Cubans, outside of the *nomenklatura*, to invest in joint ventures or even set up small or medium-sized businesses to supply even the tourist sector. Thus, by restricting the flow of revenues that foreign investment could generate workers and citizens, the government continues to prevent the emergence of independent economic agents potentially capable of diluting the formal power structure. While the most empowering hard currency earnings are those obtained directly by the population, through tips (in

190. The plant is reported to have 1,680 workers. "Castro's Capitalist," *Business Week*. The government employment agency is paid an average of US\$450 per worker, while the worker earns the average salary of 202.5 pesos.

191. These are rough estimates based on the average salary of US\$450, paid to workers as 202.5 Cuban pesos multiplied by 60,000 workers said to be employed in joint ventures. A 11% labor utilization tax on gross salaries and social security contributions of 14% of wages paid by the joint venture in hard currency but registered on behalf of workers in pesos at a one-to-one exchange rate, leaves the government, an estimated US\$35.6 million and US \$43.3 million per annum respectively.

192. A reported peso-dollar rate of 22 was used for this calculation. (Estimated US dollar hourly wages for garment workers in the spring of 1996 were: Pakistan .26, China .28, Bangladesh .31, Indonesia .34, India .36, Haiti .49, Egypt .63, Mexico 1.08, Honduras 1.31, El Salvador 1.38, Peru 1.39, Brazil 1.92, Taiwan 5.10, Britain 9.37, U.S. 9.56, Canada 9.88, Italy 14.32, Germany 18.43. Source: *The New York Times*, February 1, 1997.)

193. Study conducted by *Instituto Cubano de Estudios Sindicales Independientes* for year-end 1996, distributed by *CubaNet*, March 10, 1997.

194. At Suchel, the joint venture with British *Unilever PLC*, salespeople can earn one-third more than its Cuban executives. "A touch of capitalism," *Business Week* p. 50.

the tourist sector¹⁹⁵) and informal services, the unavailability of reliable data, makes their difficult to assess.

In sum, hard currency earnings derived from foreign investment are not enabling a significant improvement in the economy with meaningful trickle down effects empowering of empower workers or citizens. In fact, due to the nature of the foreign investment regime, the conditions and terms for the generation of earnings appear to reinforce the vested interest both of the state and of foreign investors to preserve existing joint venture arrangements. These have been designed to maximize short-term benefits for the partners in the context of a command economy and a closed political system. Therefore, despite the peculiar deficiencies of Cuba's investment climate, foreign investors are rationally interested in the survival of the current Cuban government and its investment agreements for the minimum period required to secure capital recovery and indefinitely to generate a stream of profits. For the Cuban government any revenue generation, whatever it might be, fosters self-preservation at this time of profound crisis.

Multiplier Effects

More than three-quarters of joint ventures with foreigners involve investments no larger than US\$5 million; these are concentrated in the export-oriented sector, in support businesses to foreign tourism or in extractive industries such as mining and oil exploration. Their relative size in the economy and their impact on overall domestic production are, consequently, insignificant. The highly risky investment environment appears to explain the limited initial capitalization (exposure) and the nature of the investments and the focus of investors on recovery instead

of reinvestment. All these factors restrict multiplier benefits to the local economy.

The multiplier effects emanating from worker remuneration remain very limited in scope due to wage confiscation, the low level of employment in joint ventures. The average size of the Cuban family is four. With 60,000 employed in joint ventures, roughly 240,000 people are calculated to depend on those jobs—around 2% of the population. For workers in tourism, with access to tips, a rough calculation which assumes that 40,000 are employed in tourism joint ventures shows around US\$7.5 million per month in tips (US\$187.5 per worker), a level which cannot have a significant impact on the economy. In terms of empowerment, advances are most perceived by the population in the informal and self-employed sectors, some of which service the foreign-generated economy. But the government has imposed steep taxes and fees to “redistribute” individual gains, canceling out most of their effect. And, with self-employment licenses totaling a scant 180,916 as of April 1997¹⁹⁶—a 13% decline since January 1996¹⁹⁷—multiplier impact is very limited. In fact, analysts have shown that the segregation of tourism from the rest of the economy limits the expansionary effect of the income multiplier. One elaborate study calculates that, due to Cuba's economic model, the country is losing several million dollars per day of economic impact from tourism.¹⁹⁸

From the Cuban state's standpoint, the rationale for foreign investment continues to be the prioritization of political necessities over structural economic reform together with the extraction of immediate economic gains to alleviate the monumental economic crisis. From the standpoint of the investor, the high risk scenario continues to impose an essentially spec-

195. Although workers are required to turn over up to 75% of tips, receiving an equivalent sum in pesos calculated at the official one-to-one rate, non-compliance with this rule is reportedly high (although it may lead to termination of employment).

196. *Economic Eye on Cuba*, 2-8 June, 1997.

197. In September 1996, licenses numbered 184,922, down from a peak of 209,606 in 1996. Philip Peters, *Islands of enterprise: Cuba's emerging small business sector*, The Alexis de Tocqueville Institution, January 27, 1997.

198. N. Crespo and S. Negrón Díaz, “Cuba Tourism in 2007: Economic Impact,” in this volume, elaborating on María Dolores Espino, “International tourism in Cuba: an economic development strategy.” The study compares a simulation of Puerto Rico's and Cuba's tourism activity indicators for the year 2007. Data for Cuba is derived from official figures.

ulative and short-term rationale bent on fast capital recovery and the maximization of profits. This scenario is contrary to the economy's need for capitalization—that which enables the creation of domestic savings and spurs internal growth.

Dispersion of Development

Notwithstanding the FTZs' potential contribution to the development of a small industrial base, as designed, they merely provide another variant of selective capitalist "reform" in the context of the model of enclave economies favored up to now. While it had been reported that a non-Republic of Cuba company was discussing the possibility of managing one of the FTZs, a development which would be unique,¹⁹⁹ finally only government-controlled companies were authorized to run the four existing FTZs,²⁰⁰ disappointing hopes for a small opening. In respect of empowerment, it will be interesting to observe if and how any potentially progressive elements are implemented, and, if they are, how the experience will be absorbed.

As for the dispersion impact of foreign investment discussed in our previous paper, a recent University of Havana study attributes to foreign investment a contribution in the promotion of efficient and competitive behavior and the creation of a new entrepreneurial culture.²⁰¹ These advances, however, are limited to a select group. The "demonstration effect on consumption"²⁰² or "*technocratic metamorphosis*"²⁰³ (both discussed in more detail in last year's paper), do not appear to show any significant advances in respect of actual empowerment. Both state technocrats and the population at large have been kept firmly subjugated to state control while the operation of the

new FTZs and the progression of activities related to foreign capital continue to indicate an extremely high concentration of resources in the state sector and the "privatization" of financial resources and capital among the ruling elite—especially the Armed Forces and the security police.²⁰⁴ The dispersion effects of tourism are perhaps the most significant within the sector tied to foreign capital. But joint ventures and Cuban enterprises in the sector of tourism and leisure tend to be run by arms of the Armed Forces (FAR), CIMEX—a subsidiary of the secret security police—and Habaguanex, the city of Havana's joint-venture corporation.²⁰⁵ Plus, its benefits are mitigated by its undesirable social costs—the most salient being prostitution, economic dualism and environmental damage—and the existing limitations of the traditional linkage between the tourist industry and the rest of the economy.

All in all, Cuba's enclave system of foreign joint ventures—captive to the *nomenklatura*, concessionary to foreigners, and lacking transparency and competitiveness—remains firmly in place. In fact, Cuba's brand of capitalism, designed to access foreign capital thru leadership-contained mechanisms (which we coined "coopted or distorted dispersion of development") harvests destructive societal aberrations which sabotage the eventual establishment of an appropriate framework to achieve social order and a rule of law. This scenario bolsters our original conclusion that, in a repressive regime, as long as individuals or groups remain suppressed, lacking the capacity to effectively implement change, empowerment seems independent of how foreign influence might alter their psychological disposition.

199. J. Kavulich, telephone conversation, 7/11/97.

200. *The Economist Intelligence Unit*, op.cit.

201. O. Perez Villanueva, *La inversión extranjera*, p. 18.

202. Michael Peters, *International Tourism*, Hutchinson Publisher, 1969; cited in G. Gunn, op.cit.

203. Term borrowed from James Shinn, "Engaging China: exploiting the fissures in the facade," *Current History*, Vol. 95, No. 602, September 1996.

204. A Canadian journalist has recently observed: "The new Cuban capitalist is more than likely an intelligence officer or army staffer," Brendan Howley, "Economic surge missing Cubans," *The Globe and Mail*, April 22, 1997, distributed by *CubaBrief*; Freedom House, March 1997.

205. Howley, "Economic Surge."

The dispersion effects of capitalist elements which might potentially challenge the prevailing economic and political order remain confined to this framework.

The Debate on Economic Determinism and Political Reform

A World Bank study has recently demonstrated that a state founded on effective institutions is essential for a prosperous economy; market friendly policies or reforms do not seem to work in their absence. In addition, it reveals that credibility in government weighs heavily in determining the level of foreign investment and economic growth a country effectively attains.²⁰⁶ Even if a deterministic relationship between economic and political reform could be demonstrated, a relationship analyzed in last year's paper, Cuba's is far from attaining a level of economic reform that *could* eventually lead to political reform. This is poignantly illustrated in The Heritage Foundation's 1997 Index of Economic Freedoms, which evaluates key areas, such as trade, monetary and banking policies, taxation, government intervention, property rights, and regulatory environment. Cuba is ranked 148 out of 150 countries surveyed, just ahead of Laos and North Korea.²⁰⁷

Because in Cuba economic freedoms are perceived as subversive to the prevailing order, the imperative of

regime survival overrides economic rationality and bars the establishment of a proper and enabling model, conceived on effective and credible institutions. As a result, the nature of foreign investment inherently limits and remains incompatible with stable and long-term economic growth and political stability.

CONCLUSION

The events of this past year buttress our previous conclusions. The October 1997 Party Congress is expected to reaffirm that the political necessities of the regime will continue to dictate the character of Cuba's economy, and, thus, of commercial engagement and foreign investment. As long as the ruling elite retains the means to impose power by force, this rationale will preclude meaningful economic and political development.

For the international community to promote a transition to a pluralistic democracy in Cuba, more realistic policy initiatives founded on the premise of "conditional engagement" ought to be pursued. These would condition economic ties to the dismantling by Cuba of reform-disabling mechanisms which assist in the containment of those forces which might bring about the eventual empowerment of the Cuban people.

206. "It's the government, stupid," *The Economist*, June 28, 1997, pp. 71-73.

207. Cited in *U.S.-Cuba Policy Report*, 3:12 (December 1996), p. 9.