MODELS OF ECONOMIC REFORM AND CUBA’S “UPDATING” OF ITS MODEL

Over the past five decades, Cuba has achieved significant advances in the areas of health and education, but has lagged with respect to economic growth. Perhaps the most significant challenge facing Raúl Castro’s administration in the short and medium terms is how to promote vigorous and sustained economic growth. The consensus within and outside the island is that economic policy reforms are essential to kindle economic performance.

This paper begins with a discussion of broad economic reform strategies that have been adopted by developed and developing countries over the past three decades, with special emphasis on the set policy reforms that has come to be called the “Washington Consensus,” which dominated thinking in the economic development discipline for most of the 1980s and 1990s. The market-oriented reforms embodied in the Washington Consensus were deemed to bring broad benefits to society and thus had the characteristics of public goods. This package of market-oriented reforms was supported by many academicians and economic development practitioners and embraced by the World Bank and other key institutions in the development field, rais-
ing their profile and acceptability. As Morrison (2011) describes in his review of world trends in economic reforms, by now some of the glitter of the Washington Consensus has worn off, giving rise to a healthy reconsideration of development strategies and rejecting facile, one-size-fits-all approaches to economic reform.

How does that analysis translate to Cuba? The second part of the paper focuses on the Cuban leadership’s analysis of economic reform priorities and economic policy choices. The emphasis here is that context and culture matter in choosing a model and Cuba’s cautious moves reflect a pervasive lack of a reform mentality, which Raúl Castro is trying to change. Cuba’s long and strong tradition of demonization and elimination of the market—emphasizing, for example, moral vs. economic incentives and egalitarianism vs. efficiency—circumscribes reform options for the Cuban leadership. They are clearly not ready to adopt Washington Consensus–type reforms, but the global market and internal pressures for economic growth are forcing dramatic experiments. Our expectation, then, is that there will be pockets of reform; in some areas Cuban policy makers will open the economy, but in others they will seek to preserve their heritage. Over time these parts may merge together, but for a time a dual strategy, which seems consistent with the slow steps they have been taking, could provide them with an opportunity to learn from other development models as well as build on their own economic successes and cultural legacies.

ECONOMIC POLICY REFORMS, THE WASHINGTON CONSENSUS

In 1989, as the economics profession was grappling with a global debt crisis that afflicted many developing countries and was seeking ways to invigorate economic growth, U.S. economist John Williamson wrote a paper for the Washington-based Institute for International Economics (IIE) in which he identified and discussed ten policy instruments “about whose proper deployment [to address overwhelming debt burdens] Washington can muster a reasonable degree of consensus.” By “Washington” Williamson meant the United States government (and its agencies, such as the Treasury Department and the U.S. Agency for International Development) as well as international financial institutions (IFIs), that is, the International Monetary Fund (IMF), the World Bank (WB), and multilateral regional development banks. The ten policy instruments identified by Williamson (1990, 2–3) were:

1. Fiscal discipline: Reducing large fiscal deficits to avoid balance of payments crises and high inflation that hit mainly the poor.
2. Reordering public expenditure priorities: Switching expenditure in a pro-
growth and pro-poor way, from subsidies from areas that did not merit
them to basic health, education, and infrastructure.

3. Tax reform: Aim was a tax system that would combine a broad tax base with
moderate marginal tax rates.

4. Liberalizing interest rates: Removing controls on interest rates.

5. A competitive exchange rate: Avoiding overvalued or undervalued exchange
rates.

6. Trade liberalization: Removal or reduction of tariff and nontariff barriers to
trade.

7. Liberalization of inward foreign direct investment: Removal or reduction of
barriers to foreign direct investment.

8. Privatization: Sale or transfer of state-owned resources to the private sector.

9. Deregulation: Easing barriers to entry and exit into markets.

10. Property rights: Providing the informal sector with the ability to gain prop-
erty rights at acceptable cost.

In an important survey of economic policy reform, Rodrik (1996, 9) stressed
the concurrence of views on economic reforms implicit in the Washington
Consensus: “What is remarkable about current fashions on economic develop-
ment policy (as applied to both developing and transitional economies),
however, is the extent of convergence that has developed on the broad out-
lines of what constitutes an appropriate economic strategy. This strategy em-
phasizes fiscal rectitude, competitive exchange rates, free trade, privatization,
undistorted market prices, and limited intervention (save for encouraging
exports, education, and infrastructure).” The common assumption of propo-
nents was that the set of market-oriented reforms would ultimately make all,
or nearly all, of the citizenry better off.

Twenty-five years after Williamson’s seminal paper, it is fair to say the
intellectual attraction of the Washington Consensus has ebbed. William-
son has defended his construct, clarifying that he only attempted to identify
economic policy areas and did not prescribe specific implementation steps.
Moreover, he has stated that it was not his intention to set forth a one-size-
fits-all approach to economic policy reform, and it was well understood in
his presentation that national circumstances would govern the potential ap-
plication of each of the policy prescriptions.
Despite these pronouncements, many in Latin America would argue that the international economic community did see the Washington Consensus as a prescription. Through the 1980s and 1990s, loans and restructuring packages from the international financial institutions required privatization, reduction of state payrolls, increased interest rates, and elimination of trade barriers. Clearly these policies had some positive impacts: some inefficient state enterprises were sold, bloated government budgets were trimmed, and governments introduced more accountability in their economic models. The neoliberal reforms, however, did not result in anticipated growth and in many instances sharpened distributional disparities. In a continent of poor people, more belt-tightening had its limits. Further, privatization was handled badly, resulting in state property going to political cronies and limiting revenue to the state from the sales. The implementation of neoliberal schemes and austerity policies also led to severe protests and riots, as seen in Venezuela, Bolivia, and Argentina. The dissatisfaction with policy reforms by certain groups who felt that the reform imposed costs on them rallied them to use the political process to block their implementation.

POLICY REFORM AFTER THE WASHINGTON CONSENSUS

The disappointing results of the implementation of the Washington Consensus brought about a reconsideration of economic reforms in promoting growth and addressing the challenges of poverty and wide differences in living standards across countries. In April 2006, the World Bank established a Commission on Growth and Development that brought together 21 leading practitioners from government, business, and the policy-making arenas, mostly from the developing world, “to take stock of the state of theoretical and empirical knowledge on economic growth with a view to drawing implications for policy for the current and next generation of policy-makers.” The rationale for the establishment of the Commission was:

1. The sense that poverty cannot be reduced in isolation of economic growth, and that that link has been missing in the minds and strategies of many;

2. Growing evidence that the economic and social forces underlying rapid and sustained growth are much less well understood than generally thought—economic advice to developing countries has been given with more confidence than justified by the state of knowledge;

3. Realization that the accumulation of highly relevant (both successful and unsuccessful) growth experiences over the past 20 years provides a unique source of learning; and
4. Growing awareness that, except for China, India, and other rapidly growing economies in East Asia, developing countries need to accelerate their rates of growth significantly for their incomes to catch up with income levels in industrialized countries, and for the world to achieve a better balance in the distribution of wealth and opportunity.

The final report of the Commission (2008) represents a milestone in thinking about pro-growth policy reforms. The Commission identified some of the distinctive characteristics of high-growth economies that could be emulated by other countries but does not provide a formula for policy makers to apply, as no generic formula exits. Each country’s specific characteristics and historical experiences, the Commission concluded, must be reflected in its growth strategy.

Drawing on the report of the Commission, Morrison (2011) notes that countries should take an “experimental” direction in devising a reform strategy because there is no “generic” direction for growth. What special conditions are there for Cuba, assuming we accept the proposition that there is no “generic” agreed-upon best direction for reform?

CUBA’S “UPDATING” OF THE ECONOMIC MODEL

Cuba has, of course, much company in working to reform its economic policies. Most in Latin America have done this within the context of leftist politics, though as popularized by Castañeda (2006), some Latin American leaders have emphasized “populist” solutions, while others have leaned more toward solutions emphasized by the Washington Consensus. As mentioned by John Beverley—a participant in the conference that was the basis of this current volume—Castañeda (2006) and Reid (2008) harshly criticize the populists. Needless to say, those on the other side—especially Venezuela and Bolivia—have ended up with much more antagonistic relations with the United States. Cuba has fallen even further afield in terms of both opposition to neoliberal economic policy reforms and political relations with the United States. There was an odd parallel, however, in that Cuba implemented austerity measures during its Special Period in Time of Peace of the 1990s that were quite similar to those demanded by the IMF and the World Bank as part of their structural adjustment programs. Still, as the ideological vanguard of anti-Americanism, Cuban leaders would have a strong political and cultural reason to resist reforms that had a taint of bending to American-led policy prescription.

This cultural taint of the term “reform” has yielded several neologisms. Since the international lending institutions and the Washington Consensus appropriated the term “reform” to connote market-oriented changes, the for-
mer Soviet Union referred to its economic policy changes as “perestroika” (restructuring), the Chinese as “modernization,” and the Vietnamese as “renovation.” Thus, instead of “reforming” their economy, Cubans are “updating their economic model.”

After five decades of implementing and promoting the virtues of a socialist economic model, it is difficult for the Cuban leadership and the Cuban people to change course and abandon the socialist ways. Adding to the policy immobilism, Cubans live by the proverb “better the devil you know than the saint you don’t.” Perhaps for these reasons, “updating” of the Cuban model has proceeded very slowly, but there are some notable changes as outlined in other chapters in this volume. This slow pace, which includes areas of experimentation overlaid within a continuation of socialism and economic centralism, fits at least three logics.

First, the resistance to change represents a recognition that change based on neoliberalism has not brought the promised results to the countries that have adopted it. In addition to examples of lackluster growth in earlier decades throughout Latin America, the region is continually plagued by income inequality and poverty. If this were not enough to bring caution to Cuban reformers, they must add the legacy that their economy has been conditioned by the longstanding U.S. embargo. Rightly or wrongly, the Castro regime instilled the idea in the Cuban population that the U.S. embargo was the primary reason for the island’s poor economic performance. Cuba’s political and economic allies have reinforced this view. Venezuela’s support, which has been vital, has reinforced an anti-American stand.

Second, socialism has been shown to maintain power in the hands of the leadership, and thus the unwillingness to reform represents a political maneuver by the leadership to maintain power. This is one of the attractions for the Cuban leadership of the Vietnamese or Chinese models, which have reformed their economy but preserved political order. This dovetails with what Alzugaray believes is a sincere movement to save the legacy of the “historic” generation. The historic generation knows that its members are passing away and they want to leave behind to their children and grandchildren something better than what is happening in Cuba today. Therefore, Cuba is following the Vietnamese or Chinese general path, namely to reform the economy in order to preserve political order.

Cuba has in common with these socialist countries that its reforms have been “top down.” They have not come from below, but actually imposed from the top. It is within the party and government structure that reforms happen. However, in the longer term it is impossible to pretend that reforming the economy can be accomplished without affecting the political order.
Thus, future Cuban leaders must consider the effect of changes not only on their powers but also on the likelihood of economic success.

While there is recognition in Cuba of Chinese and Vietnamese successes in policy reform and some academics and think tanks feel that Cuba should do something similar, Alzugaray argues that at the same time there is a cultural tendency—which is actually quite old and entrenched—that Cuba is exceptional. While politicians and many others think that the United States is exceptional, so do their counterparts in Cuba. The thinking that “Cuba has to do this differently” has been in place for a long time and continues to be so today.

Thinking about Cuban reforms requires considering a biological variable—in the next few years, there will be a political succession in Cuba whether political actors want it or not. If we accept that Fidel and Raúl Castro have had unique concerns with centralizing power and maintaining the centralized socialist system, then reform will naturally occur once those octogenarians pass the leadership torch. The experience of multiple past and current leaders in Latin America and other parts of the world suggests that future Cuban leaders may also see political advantages in the current centralized model. A key question may be whether future leaders will have the ability to mobilize the citizenry in their support. Cuban citizens have begun to criticize policies and make demands on their government. This has led to notable policy changes and reversals, such as opening possibilities for private employment, new opportunities for obtaining loans to set up small businesses and construct a high-tech port and free trade zone in Mariel. An open question is whether future leaders will marshal support in favor of what they have accomplished or face threatening pressure for further changes.

Third, the Cubans have a particular concern with nationalism and preserving the legacy of the historic generation that was involved in the revolution. While it would be cynical to assume that the Cuban leadership is unconcerned with growth, it also seems reasonable to argue that the generation that fought in the revolution and built an anti-American political and economic system would be particularly focused on the successes of the revolution, whether mythical or actual. The “historic” generation is passing away, but it is unclear whether the next generation of leaders will still privilege this legacy as they devise the economic future.

The legitimacy of the Cuban political system, and thus its economic model, is based on five premises. First, Cuba has a strong nationalistic sentiment, based on more than a half century of conflict with the United States. Second, the Castros based their leadership on charisma. It is not clear that representative democracy is a strong value in the island. Third, at the same time,
the Cubans have built some semblance of popular representation, because the government has consulted with people through different referenda. This third factor is reinforced by the fourth, the peculiarities of Cuban historical evolution: its Spanish heritage and revolution against Spain in the nineteenth century, American domination in the early 1900s, the socialist revolution ending in 1959, and so forth. Fifth, the revolution delivered public goods in its initial phase and it has maintained at least two: public health and education.

THE HISTORICAL LEGACY AND THE PACE OF REFORMS

These cultural and political factors explain the slow and irregular pace of reforms. While there are also many examples of experimenting with reforms under Fidel, there have been clear and dramatic changes under Raúl, in spite of his statement that he did “not want to improvise because in the past there was a lot of improvisation.”

The reforms under Raúl through the end of 2012 are outlined in detail by Mesa-Lago and Pérez-López (2013); more recent changes are included in other chapters of this book. In what follows we illustrate the reforms focusing on three broad policies: the special development zone and shipping port at Mariel, employment policies, and rules to promote private agriculture. In addition to describing these policies briefly, we also bring out their incomplete nature and some inconsistencies in application that are hindering results.

Mariel Special Development Zone

The Economic and Social Development Guidelines approved by the Sixth Congress of the Cuban Communist Party in 2011 foresaw the establishment of special development zones (zonas especiales de desarrollo, ZED) with the objective of increasing exports, promoting import substitution, attracting high-technology investment, and promoting employment. The first ZED was established at Mariel, west of Havana, in 2013. Concurrently, the port of Mariel was also the location of a major infrastructure development project in the form of a shipping container megaport whose construction, estimated at a cost of $1 billion, was financed by Brazilian export promotion agencies. Illustrating the multinational nature of the project, the bulk of the Mariel port loading equipment originates from China and a Singaporean company will manage the facilities.

This is a clear example of Cuba’s reforms implemented without full confidence, since it combines a dramatic change with severe restrictions. On the dramatic side, Cuban economist Omar Everleny Pérez Villanueva has stated that businesses that locate in the ZED will be able to operate for 50 years,
own 100 percent of assets, operate tax-free for a decade, and be exempt from paying tariffs on imported equipment and raw materials (Johnson 2015). Businesses located in the ZED are expected to generate some 8,000 direct and indirect jobs for Cuban citizens, who will earn good salaries and be better able to support their families. If successful, it seems that the model would put great pressure on the government to open up other areas of the economy.

These important reforms with their potentially game-changing impacts are hamstrung in terms of their reach and impact by some national polices and others directed specifically at the free trade zone. At the national level, a limiting factor is the dual currency system, which distorts economic signals. Also at the national level, businessmen and workers in the zone will see the inconsistencies between economic freedoms in that area compared to severe limitations elsewhere. Activities in the zone will be affected by policies with respect to at least two areas. First, the free trade zone is limited by the employment system. Foreign firms will be allowed to set up manufacturing facilities and other businesses, but they must hire workers though an agency of the Cuban government. Thus workers will continue to earn the paltry government wages, while working alongside foreigners earning many times what they are earning. Second, the free trade zone has high hurdles that companies will have to jump in order to build businesses in the zone, including a complex, time-consuming, and uncertain application process.

**Employment Policies**

For most of the revolutionary period, the Cuban state was the overwhelming employer in the country, with the private sector limited to some agricultural and transportation activities. In 1993, in the depth of the economic crisis brought about by the end of the economic relationship between Cuba and the former Soviet Union, the Cuban government authorized self-employment by Cuban citizens in 157 specific occupations, among them production of food items (which led to the creation of small private restaurants, *paladares*), operation of private taxis, as well as a host of menial occupations (such as party clown, cigarette lighter refiller, etc.). Workers seeking to become self-employed had to register with the authorities, seek a license, and pay taxes in accordance with a special schedule for self-employed workers. Self-employed workers were allowed to hire family members in their activities, but not workers without a familial tie.

Shortly after ascending to Cuba’s top leadership position in 2006, Raúl Castro announced the intention to reduce the size of the state payroll, indicating that up to 20 percent of state employees (around 1 million workers) were redundant and would be removed from their positions. The intention
was that the retrenched workers would be absorbed by the private sector. After the Sixth Party Congress in 2011, the scope of self-employment was slightly expanded, with an additional 21 occupations authorized, bringing the total of authorized occupations to 178. Self-employed workers were also authorized to hire up to five nonfamily workers in about half the occupations. However, professionals are still not allowed to practice the trade for which they were trained, which means that accountants, physicians, architects, engineers, teachers, and other professionals must continue as employees of the state sector. (Many professionals, unable to practice their profession as self-employed, leave white-collar state jobs and join the tourism sector in menial jobs as they are able to increase their income through tips. It has been observed that Cuba has the most highly educated taxi drivers and tourism labor force in the world.) Rather than designating the occupations that are allowable under self-employment, a stronger and more positive action by the Cuban government would be to allow all occupations to be suitable for self-employment and strategically create a short list of occupations not allowed for self-employment at this time.

A very significant constraint on the expansion of the private sector is the lack of markets for intermediary goods, i.e., outlets where self-employed workers could legally purchase the inputs to ply their trade, for example, beef, rice, chicken, eggs for paladares; spare parts and tools for automobile mechanics; fabric, leather, buttons, and other sewing notions for dressmakers and tailors. Recently, the Cuban government has facilitated the sale to individuals of construction materials as a way to improve housing maintenance, but for most private sector workers, the black market and other illegal transactions provide a significant portion of their inputs and raw materials.

Promoting Private Agriculture

One of the most significant Cuban reforms to date is Decree Law no. 259 of 2008, which provided for the distribution of idle state lands in usufruct to private farmers not possessing land and to cooperatives. The logic of this reform measure was impeccable: on the one hand, it removed from the state inventory lands that were not being productively used and often had deteriorated (e.g., they had been infested by the invasive shrub marabú, which renders the land unusable) and on the other provided an incentive for private farmers and cooperatives to produce higher volumes and variety of agricultural products that would contribute to reducing the huge food import bill.

Despite the strong logic of the agricultural reform measure, the legislation that was approved by the Cuban government placed significant restrictions on the distribution of land that limited the measure’s beneficial impact.
Thus, as originally proclaimed, the maximum amount of land that could be
distributed to individuals pursuant to the reform measure was too small to
permit crop rotation and other good agricultural practices; disallowed the
construction of houses or other structures on the land (which meant that
farmers who worked the land could not build even a tool shed and had to
live elsewhere and possibly travel daily a long distance from and to their
homes); limited the possession in usufruct to 10 years, although it could be
renewed for a similar length of time (the criteria for renewal were not set out,
however); and did not make any financial or credit provision to assist work-
ners in clearing the land from marabú and otherwise preparing the land for
cultivation. Subsequently, some of the above restrictions have been relaxed,
but nevertheless the full impact of the distribution of land is being hampered.

LOOKING TO THE FUTURE

Raúl has rejected expediting economic reforms, which Cuban officials asso-
ciated with the despised “shock treatment” they claim devastated the econ-
omies of the former Soviet Union and Eastern Europe, and stated that the
pace of Cuba’s reforms will be “sin prisa, pero sin pausa” (Castro 2013). This
suggests a lack of urgency, which was summed up by a former Spanish Am-
bassador to Cuba who expressed to one of the authors, “Cuban leaders seem
to think that time doesn’t exist.” International observers express a sense that
Cuba faces enormous challenges and that time is running out on the “updat-
ing of the model.”

There is no clear model for Cuba to follow, however. Given the negative
consequences of neoliberal policies in much of Latin America and the result-
ing breakdown (or at least softening) of the Washington “consensus,” plus
the ideological hesitation that they would surely feel about adopting U.S.-led
neoliberal policies, Cuba must find a new model. Several countries, includ-
ing Cuba’s ideological brethren Bolivia and Venezuela as well as the domi-
nant player in the region, Brazil have developed a model centered on more
state-centered capitalism. The model is not without its problems, but it has
allowed the state to maintain control of important sectors and earn signif-
ican income with which it can support its highly valued social programs.
Market oriented critics, of course, question the viability of this approach, as
they argue that state enterprises are inefficient, wasteful, and have been un-
able to attract needed foreign capital to expand productive capacity. The sim-
ple response is that private enterprise has not always supported positive and
equitable growth in Latin America, either.

Beyond the broad categories of economic plans, Cuba must deal with spe-
cific challenges. It faces pressures to simultaneously reform government en-
terprises, generate alternative employment, and unify the currency. Further, reforming the state would imply devolving decision-making power to the managers, which would be a new responsibility for a group of cadres who are used to following directives. The basic premise of the reform process—that economic change will bring benefits to all citizens that will ensure the stability of the system—is not happening. There is an increasing consciousness that political reform should accompany economic reform but there is no consensus yet on this point. The definition of what the new economic model will look like, on which it will be difficult to reach consensus, will carry with it the acceptance of the new mentality. There is increasing pressure from citizens to improve their standard of living, which has been demonstrated each time that a reform is reversed or modified or that the necessities of citizens are ignored by bureaucrats.

The Seventh Party Congress, held in April, 2016, was an opportunity for the country to revise its path, given the new opening to the United States. The Congress, however, largely reaffirmed the past, and offered few important changes. It confirmed, for example, that Raúl would step down from his government posts in 2018, but he will remain party secretary until 2021. This continuity is somewhat surprising, given the results of the efforts to “update the model,” which has and will continue to lead to an inevitable assessment by the population of in terms of tangible improvements in their standard of living. The announced retirement of Raúl Castro does provide another opportunity for reform, since for the first time in six decades the new top leader will not likely to be part of the “historicals” cohort and may not have the Castro surname. And, of course, there are the international issues, which are critical to the Cuban economy. Looming large is the future of economic support from Venezuela whose economy has been in free-fall and its political situation highly unstable.

Management of the new relationship with the United States announced by President Obama but now controlled by the Trump administration is, of course, critical. The economic and political opening at first brought both the prospect of an erosion or even elimination of the U.S. trade embargo, but also political challenges for the leadership. So far the Trump administration has been boisterous about clamping down on trade and political openings to Cuba, but while President Trump decreed some new restrictions on travel and the ability of U.S. companies to do business in Cuba, there have not been many material changes. U.S. public opinion and many from the business sector generally favor openness to the island, but pressure has not risen to a level to raise Cuba on Trump’s priority list. The most important forces that could bring reform, then, are likely the passing of the Castro regime with the
historicals, the continuing crisis in Venezuela, and the domestic pressures that have arisen from those hoping for improved living conditions. For six decades the regime has withstood the latter two types of pressures, but it remains to be seen whether a change in leadership will continue to avoid serious “updating.”

NOTES

This chapter has been prepared by Scott Morgenstern and Jorge Pérez-López relying heavily on transcripts of presentations made at the conference by Kevin Morrison, “The Washington Consensus and the New Political Economy of Economic Reform,” and Carlos Alzuguray, titled respectively: “The ’Updating of the Economic Model’ in Cuba: An Initial Comparative Perspective of Its Domestic and Foreign Political Contexts and Implications.” Morrison’s presentation at the conference drew from Morrison (2011). The paper has been reviewed by Alzugaray and Morrison and their comments incorporated into the final draft.

1. For a discussion of the economic situation in Cuba through 2012 that underlies the current economic reforms see Mesa-Lago and Pérez-López (2013).
4. Roughly translated as “without haste, but steadily.”
5. In a conversation with Carlos Alzugaray.

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