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# Cuba Under Raúl Castro: Assessing the Reforms

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# 1

## Cuba's Economic and Social Development, 1959–2012

**As necessary background to understand the reforms that are being implemented by Raúl Castro, this chapter summarizes the history of Cuban economic and social policies during the revolution (1959 to 2012), following a typology of “idealist” and “pragmatist” cycles.<sup>1</sup> In the chapter we identify eight such cycles and for each of them we analyze internal and external causes, describe policies that were implemented, and evaluate outcomes.**

### **Idealist and Pragmatist Cycles in Cuba's Economic and Social Policies**

The socialist central-planning or “command economy” model, introduced in Cuba in 1961, remains today as the basic form of economic organization, although substantially transformed and without some of its original elements. Economic and social policies have swung eight times since 1959, giving rise to cycles of different intensity and length that have alternated from movement toward or away from the market. For the sake of simplicity, herein “idealist” cycles are those dominated by policies that move away from the market, while “pragmatist” cycles are market-oriented.

During idealist cycles, the political leadership generally set ambitious goals—for instance reaching the highest level of industrial production per capita in Latin America within four years, producing 10 million tons of sugar annually and subsequently reaching annual production of 20 million tons, creating an unselfish “new man,” and reaching food self-sufficiency within a five-year period. These goals were not achieved and their pursuit contributed to adverse economic and social performance and even crises.

Such failures raised the threat (real or perceived) of regime instability and prompted the political leadership to adopt market-oriented policies in order to boost economic performance and preserve or strengthen the regime and maintain control. Pragmatist cycles have resulted in moderate improvements in economic performance<sup>2</sup> and living standards, but have also brought about some adverse social effects, such as rises in unemployment or inequality. Typically, once the political leadership felt that the regime had been sufficiently strengthened under pragmatist policies, it launched a new idealist cycle, thus perpetuating a policy seesaw.

Economic logic dictates that Cuban authorities would maintain and strengthen pragmatist cycles that bring about positive economic results. But such rationality has not been followed by the Cuban political leadership because, in our opinion, it has perceived that market-oriented policies entail a certain loss of economic influence, decentralization of decisionmaking, and emergence of economic actors independent from the state and hence a loss of the latter's economic power and, potentially, political control. Thus, we argue that political logic (preservation of the regime and control) has surmounted economic logic, giving rise to recurring idealist cycles. Moreover, increases in unemployment and inequality and other negative effects associated with the market seemed unacceptable to the political leadership, at least through the decade of the 1990s.

Most of the cycles have lasted between five and six years, creating instability and uncertainty and hampering long-term economic growth. During the first pragmatist cycle, market-oriented policies were introduced slowly and timidly, while they were implemented more boldly in the second and third such cycles. In contrast, idealist cycles tended over time to become weaker.

### *The Eight Cycles: Characteristics and Effects*

Since 1959, there have been eight policy cycles under Cuba's revolutionary government, with the first one divided into three subcycles. Four of the cycles have been idealist, three have been pragmatist, and one has been characterized by policy stagnation:

- 1959–1966: Although difficult to classify, this was mostly an idealist cycle, with some facets of pragmatism particularly in 1964–1966; this period is divided into three subcycles: market erosion, introduction of orthodox Soviet central planning, and debate over socialist models.
- 1966–1970: Fidel's adoption and radicalization of the Guevarist model, a strong idealist cycle.
- 1971–1985: The Soviet timid (pre-Gorbachev) economic reform model, the first well-identified pragmatist cycle.
- 1986–1990: The so-called Rectification Process, the third idealist cycle.

1991–1996: Crisis and market-oriented reforms, the second and strongest pragmatist cycle up to this point, under the “Special Period in Time of Peace.”

1997–2003: Slowdown and halt of the reform, a cycle of policy stagnation.

2003–2006: Reversal of reforms, the fourth idealist cycle, although weaker than previous idealist cycles.

2007–present: Raúl Castro’s structural reforms, the third and strongest pragmatist cycle of the revolution.

During each of the cycles there were changes—often contradictory—with respect to eleven policy areas: collectivization of the means of production; centralization of economic decisionmaking; role of the state budget; foreign investment; allocation of goods through rationing (rather than through markets and prices); agricultural free markets; self-employment; voluntary (unpaid) work and labor mobilization; egalitarianism; moral versus material incentives; and expansion of free social services.

Idealist cycles are characterized by an increase in the degree of collectivization and centralization in decisionmaking, decline in the role of the state budget as an instrument of macroeconomic management, de-emphasis or phasing-out of foreign investment, rise in the importance of administratively set ration prices rather than market-determined prices, increased restrictions or disappearance of free agricultural markets and self-employment, upsurge in labor mobilization and use of voluntary work, escalation in egalitarianism and predominance of moral incentives over material incentives, and expansion of free social services.

Policies during pragmatist cycles are diametrically opposite, albeit with divergent degrees of intensity according to the cycle: de-collectivization, decentralization of decisionmaking, greater role of the state budget in macroeconomic management, increased receptivity to foreign investment and steps to promote it, wider use of market prices versus rationing and controlled prices, introduction or expansion of free agricultural markets and self-employment, reduction or elimination of labor mobilization and voluntary work, decline in egalitarianism, predominance of material incentives, and cutback of free social services.

We assess the effects of idealist and pragmatist cycles through the performance of seven economic and social indicators: economic growth, monetary liquidity (excess money in circulation or monetary overhang), fiscal deficit, deficit in the goods trade balance, open unemployment, income distribution, and poverty incidence. Unfortunately, the latter two indicators cannot be evaluated quantitatively because of the lack of official statistics, but they will be assessed qualitatively and through estimates from foreign and Cuban analysts.

*Internal and External Factors That Influence the Cycles*

The ideology and decisions of Fidel Castro were the principal internal factors shaping the policy cycles on the island for nearly fifty years, until illness forced him to turn over his leadership role to his brother Raúl. As unchallenged leader of the revolution and founder of the regime, Fidel wielded immense power, holding concurrently the key political posts in the country: chief of state, president of the Council of State and of its Executive Committee, first secretary of the Cuban Communist Party (PCC) and head of its Political Bureau, and commander in chief of the armed forces. As president of the Council of State, he nominated the president of the Supreme Court, an institution subordinated to the Council of State. The only significant political institution that Fidel Castro did not head was the National Assembly of People's Power (ANPP), the top legislative body in the country. In practice, the ANPP has limited power; it meets twice a year for two to three legislative days at a time, with the Council of State governing during the rest of the year through decrees. Finally, as chief of state, Fidel was constitutionally granted the power to declare a state of emergency and under such conditions to modify the exercise of constitutionally enshrined rights and duties.

Fidel's proclivity for centralization, collectivization of the means of production, egalitarianism, and labor mobilization strongly predisposed him toward antimarket policies. And yet he was willing to adopt ostensibly pragmatist policies and economic reforms—although reluctantly—when a major crisis made it necessary to preserve the regime and his power. The “maximum leader” resisted changes to the political system, and hence it has been more stable than the economic system, notwithstanding the political institutionalization that occurred in the 1970s. In our opinion, Fidel's charismatic leadership and ideological bend prevented the logic of pragmatism from institutionalizing state socialism and implementing comprehensive and stable market reforms.

There are notable similarities between Cuba under Fidel and China under Mao Tse-tung; in both instances, a powerful and charismatic leader shaped the economic policy cycles. It was only after the death of Mao that China's economic reforms were consolidated, expanded, and deepened to create the “market socialism” model. Fidel has consistently rejected Chinese and Vietnamese economic reforms; the limited and timid market reforms implemented by Cuba in 1993–1996 did not come even close to the Chinese reforms and were virtually stopped by Fidel in 1996. Even Raúl, after replacing Fidel, was not able to put in place and accelerate pragmatic structural reforms until illness made it impossible for Fidel to interfere and stop them, although through the publication of his “Reflections” and statements during public appearances he tried to obstruct the reforms, at least

through 2011, when he began to concentrate on foreign affairs and withdrew from the domestic policy arena (see Chapter 5).

Numerous exogenous factors, positive or negative, contributed to the launching, continuation, or end of a policy cycle. The two most important international actors, who played antagonistic roles, are the former Soviet Union and the United States. The former played a positive role from 1960 to 1990 through its economic aid, trade, and price subsidies, but its support declined beginning in about 1985 with the rise to power of Mikhail Gorbachev. The end of the vital Soviet assistance and the ensuing deep economic crisis at the start of the 1990s forced a change toward the implementation of market-oriented policies. The United States meanwhile has been a negative factor as a result of the economic embargo in place since 1961, subject to periods of hardening (presidencies of Richard Nixon, Ronald Reagan, and George W. Bush) and flexibility (presidencies of Jimmy Carter, Bill Clinton, and Barack Obama). The threat—whether real or imaginary—perceived by the Cuban leadership that political instability on the island would open the door to intervention by the United States was an important factor in the persistence of idealist cycles. Other historical actors have been the Organization of American States (OAS), the European Union, Cuba's international creditors, and foreign investors. Since 2002 the economic support of Venezuela has been essential for the survival of the Cuban regime.

### **Policies During the Cycles, Contributing Factors, and Effects, 1959–2012**

This section describes eight policy cycles from 1959 to 2012. For each cycle, we describe policies implemented, identify internal and external factors that influenced the start and end of the cycle, and assess economic and social effects with respect to the seven indicators identified above.

#### *Market Erosion, Soviet Orthodox Model, and Socialist Debate, 1959–1966*

This mostly idealist cycle is divided into three subcycles. The first, which involved the elimination of capitalism and erosion of the market (1959–1960), resulted by the end of 1960 in the virtual elimination of the market through the rapid collectivization of the means of production. The vacuum created was filled with a Stalinist-type “command” economy during the second subcycle, which involved adoption of an orthodox Soviet central planning model (1961–1963), supported by foreign aid and trade with the Soviet Union. The establishment by the United States of a commercial

embargo on Cuba in 1961, and its extension to most of the hemisphere in 1964 by the OAS, combined with the statements by Fidel in 1961 about the socialist character of the revolution, isolated Cuba from other countries in the Western Hemisphere and facilitated the adoption of the Soviet model.

There were important policy continuities during these two subcycles: expansion of collectivization of the means of production, elimination of foreign investment (through the nationalization of foreign assets on the island), centralization of economic decisionmaking, introduction and expansion of rationing, reduction in the role of the market and of market prices in resource allocation, growth of egalitarianism, and rapid expansion of free social services, particularly in rural areas. The economic development strategy centered on import substitution industrialization (Ernesto “Che” Guevara predicted that by 1965, Cuba would be the leader in Latin America on industrial production per capita), reduction of dependence on sugar, and increased agricultural diversification.

The Soviet central-planning model was ill-suited to Cuba, given that its economy was heavily dependent on a single agricultural commodity (sugar), and given its shortage of managers (who had left the country fleeing the revolution) and lack of experience with and weak statistical base in support of central planning. To compound the problem, collectivization proceeded at a fast pace and cut across all areas of the economy, while planning was introduced haphazardly. The industrialization plan set ambitious short-term targets that required imported capital goods and raw materials, which did not arrive as timely as needed. Agricultural diversification did not meet the anticipated targets and resulted in a significant decline in sugarcane cultivation, which led to declines in sugar production and exports and to a worsening of the merchandise trade deficit.

The failure of central planning and industrialization brought about the third subcycle, which involved debate and experimentation with alternative socialist models (1964–1966). During this cycle, two factions within the leadership, espousing differing ideologies regarding socialist development, engaged in an intellectual debate. Ernesto Guevara and his followers, partly influenced by the ideas of Mao embodied in the “Great Leap Forward,” proposed an idealist, antimarket approach: an even higher degree of collectivization; reliance on the central plan and use of centralized budgeting; creation of a “new man” free from selfishness, moral incentives, voluntary work, and labor mobilization; egalitarianism; and universal and free social services. In opposition to Guevara and his followers, a pragmatist, pro-Soviet faction, led by economist Carlos Rafael Rodríguez (one of the founders of the pre-revolutionary Cuban Communist Party), who had been influenced in part by the Libermanism in vogue in the Soviet Union at the time, argued for a socialist reform model: some decentralization of decisionmaking, use of selected market-oriented mechanisms, preference for the use of material



incentives, and halt to collectivization, egalitarianism, and expansion of free social services. In a Solomonic decision, Fidel divided management of the economy between the two groups, with the Guevarists controlling roughly two-thirds of economic ministries and the pro-Soviet group controlling the remaining one-third. Although this split in control makes it difficult to characterize this subcycle, economic policy tended to veer away from the market.

Overall, this cycle lasted seven and a half years, divided into subcycles that lasted two, three, and two and a half years, time spans that were too short for policies to take hold. Performance is difficult to assess because few statistics are available for 1959–1961 and because the introduction of the Soviet model in 1962 brought about a radical change in the methodology for calculating macroeconomic national statistics that was not compatible with the previous methodology. Economic results were mixed: economic growth initially rose, then declined, and later experienced a slight recovery; monetary liquidity and the commercial trade deficit increased throughout; the fiscal deficit apparently remained stable (although reliable statistics are not available); open unemployment initially rose but later declined; and poverty and inequality decreased (although there are no supporting statistics).

#### *Fidel's Adoption and Radicalization of the Guevarist Model, 1966–1970*

Although Fidel did not intervene directly in the policy debate, by the end of 1965 the leaders of the two contending factions were no longer at their posts: Guevara had left Cuba to promote guerrilla movements first in Africa and then in South America, and Rodríguez had resigned as director of the National Institute of Agrarian Reform. With the two faction leaders out of the picture, in mid-1966 Fidel publicly endorsed several elements of the Guevarist model and ordered their implementation, although he took the model to a higher level of idealism and distorted it with his own views. For example, he virtually eliminated the central plan and the state budget (essential in the Guevarist model), strengthened centralized decisionmaking (since the central plan had been eliminated, decisionmaking increasingly fell under Fidel's control), and gave even higher emphasis to moral incentives, labor mobilization, and the use of voluntary work.

Not only did Fidel diverge from the orthodox Soviet model, but he also affirmed that Cuba, with its idealist approach, had surpassed the Soviet Union in building socialism and communism. Moreover, through sponsorship of the guerrilla "foco" doctrine as a way to overthrow sitting Latin American governments, Cuba undermined traditional, pro-Soviet communist parties in the region. Despite this confrontation, the Soviet Union continued to support

Cuba economically until 1967, when Soviet leaders ran out of patience and reduced oil shipments to the island. Fidel responded by holding public trials of several prominent pro-Soviet government leaders and PCC officials (the so-called micro faction), who were found guilty of treason and “sectarianism,” adding to the already tense relationship with the Soviet Union. In 1968, however, Fidel publicly defended the Soviet Union’s invasion of Czechoslovakia (he argued that the Prague Spring was a counterrevolutionary and pro-capitalist movement, against worldwide criticism of the invasion), and such defense paid handsome dividends: resumption of oil shipments, better relations with the Soviet Union, and an overall increase in economic aid.

Cuba’s development strategy shifted after 1964 from “inward” (import substitution industrialization) to “outward” orientation (export promotion). The previous policy of reducing sugar’s role in the economy was reversed; a 1965–1970 sugar plan was adopted with the gigantic goal of producing 10 million tons of sugar in 1970. Perhaps the zenith of Cuba’s distancing from the market occurred in 1968, when Fidel launched a “revolutionary offensive” consisting of the following policies: increased collectivization through the elimination of free agricultural markets and individual family plots within agricultural cooperatives; nationalization of some 58,000 small businesses (including barber shops, shoe repair shops, and street food stands); expanded centralization of economic decisionmaking through the creation of sectorial plans (e.g., for sugar, cattle) directly controlled by Fidel; setting aside financial controls (the state budget disappeared for nearly a decade); restricting and sanctioning self-employment; boosting voluntary work and labor mobilizations in agriculture; and emphasis on egalitarianism through reductions in salary differentials, promotion of moral incentives, and expansion of free social services (e.g., public telephones, burials, admission to sports and cultural events), all aimed at forging a socialist “new man.”

This idealist cycle lasted four and a half years. Performance during this cycle is also challenging to assess, because of a government decision to cut back on collection and publication of statistics. Available information shows that most results were negative: the economic growth rate declined and was zero or negative in 1970, and sugar production fell short of the 10-million-ton target for that year by 15 percent and was accomplished at the cost of severe disruptions in other sectors of the economy. Monetary liquidity reached a record high and the excess currency in circulation brought about a significant decline in the purchasing power of the peso and a 25 percent rate of labor absenteeism (dealing a heavy blow to moral incentives and ending the myth of the creation of a “new man”). There are no statistics on the fiscal deficit because the national budget vanished, but the trade deficit increased considerably. Open unemployment fell to a record low (at the expense of increases in hidden unemployment and a sharp fall in labor

productivity) and income distribution was the most egalitarian under the revolution, as indicated by estimates by foreign academics.

### *The Soviet Timid Economic Reform Model, 1971–1985*

The failure in 1970 of both the sugar plan and the efforts to create a “new man,” combined with overall economic deterioration, provoked a dangerous crisis and led to a timid oscillation of the pendulum toward the market beginning in 1971. The failure of Cuban-supported guerrillas in South America and the death of Che Guevara in 1967, combined with Fidel’s public support of the Soviet invasion of Czechoslovakia in 1968, had facilitated reconciliation with the Soviet Union. Soviet soft loans, technical assistance, supplies of goods needed by Cuba, and price subsidies reached record-high levels during this period. For instance, the Soviet Union paid prices for Cuban sugar and nickel imports far above world market prices and sold oil to Cuba at below world market prices. Moreover, in 1972, Cuba was admitted into the Council for Mutual Economic Assistance (CMEA), an economic association composed of the Soviet Union and the socialist countries of Eastern Europe, which also opened up additional trade and financing opportunities. These positive factors were decisive at the start of the cycle and contributed to its continuation over a long period of time.

The United States, under the presidency of Gerald Ford (1974–1977), engaged in secret negotiations with Cuba and in 1975 the OAS lifted its multilateral sanctions, leaving it up to each member state to establish commercial and diplomatic relations with the island. But in giving military support to the socialist government of Angola, Cuba aborted its brief attempt at reconciliation with the United States. During the first years of the presidency of Jimmy Carter (1977–1981), tensions between the two countries were relaxed somewhat and an agreement was reached to establish political “interest sections” (at a level below that of embassies) in both countries. However, Cuba’s military intervention in the war between Somalia and Ethiopia, as well as the arrival in the United States in 1980 of 125,000 Cubans in small boats from the port of Mariel, launched with Fidel’s backing, gave rise to new tensions and paralyzed the process of improvement of diplomatic relations. During the presidency of Ronald Reagan (1981–1989), tensions between the two countries rose and Cuba organized “territorial militias” to defend itself from a presumed invasion by the United States. An offsetting positive external factor during this period was the availability of hard-currency credits to Cuba from international creditors.

During this period, the Cuban leadership essentially reversed its earlier idealist policies and initiated a timid journey toward the market. While there was an expansion of state-controlled cooperatives and a gradual absorption of private farms into cooperatives, a number of measures contrary

to collectivization were implemented: the reintroduction of free agricultural markets and of family plots within state farms; reinstatement of self-employment and authorization of private farmers to contract workers, of citizens to build their own homes, and of individuals to swap homes (*permuta*); and enactment of a law to permit foreign direct investment (although the law imposed so many conditions that it was unsuccessful in attracting foreign investment). At the same time, central planning and the state budget were reinstated as macroeconomic management tools. Fidel criticized as “idealist errors” the previous calls for egalitarianism, moral incentives, voluntary work, and labor mobilization. The pendulum swung to the other side, with Cuba now adopting policies justifying salary differentials, re-establishment and expansion of the use of material incentives, reduction and near elimination of voluntary work (because of its inefficiency), creation of “parallel markets” where goods were sold to the population at prices set by the law of supply and demand, and charging users for certain public services that were formerly offered free of charge. During this period, an economic and political institutionalization process also took place: a new socialist constitution was promulgated, the National Assembly of People’s Power was established, and the Cuban Communist Party was restructured. The new planning technocracy faced resistance; for instance, some of the measures were publicly criticized by Fidel (e.g., the free farmers’ markets and self-employment), while others were not fully implemented (e.g., enterprise self-financing, profit-sharing with workers).

The development strategy was more rational and balanced than in previous cycles. An export-led orientation was maintained, with the sugar industry tapped to generate the bulk of export earnings; policies to spur sugar production—without adversely affecting the rest of the economy—included the construction of new mills and the mechanization of sugarcane cultivation and harvesting. With support from the Soviet Union and other socialist countries, Cuba also expanded nickel production and exports. Finally, the Soviet Union allowed Cuba to reexport (for hard currency) Soviet oil that had been committed to the island but not consumed. Tourism was reestablished as a generator of export revenues and production, and exports of citrus fruits and fish and shellfish were expanded.

This cycle is the longest (fifteen years) of the cycles identified here. Available statistics (during this period, Cuba also increased the quantity and quality of statistics) show stronger economic performance than in previous cycles. Economic growth recorded the highest average annual rate, particularly in 1971–1975, spurred by historically high world market prices for sugar, large sugar crops that averaged over 7 million tons per annum (in 1976–1985), and good performance in nonsugar sectors. Monetary liquidity declined through 1980 and the fiscal deficit was brought under control from 1978 (when the national budget was reinstated) through 1985. The deficit

in the trade balance remained essentially unchanged for a number of years and actually declined slightly in the 1970s (as a result of generous Soviet price subsidies for Cuban exports) but began to rise again in the first half of the 1980s (when some of such subsidies were cut back). For the first time since the start of the 1960s, pockets of unemployment appeared (because of the efforts to increase labor productivity, the decline in the demand for labor, and the entry into the labor force of the baby boomers conceived between 1959 and 1965) and inequality probably rose, although there are no statistics to support the latter inference.

### *Process of Rectification of Errors, 1986–1990*

The economic recovery experienced in 1971–1985 resulted in economic growth and some improvements in population living conditions. However, internal and external forces conspired against the continuation and expansion of the timid market-oriented reforms that had been implemented. Fidel and the orthodox leaders resented the growing economic power of the technocrats who were leading the planning agencies, the elimination of some revolutionary institutions that were dear to them (such as voluntary work), the growth of inequality, and the emergence of a “new class” of individuals who were profiting from the reforms: private farmers, intermediaries who participated in the free agricultural markets, self-employed workers, and those engaged in the construction and swapping of homes. Although the magnitude of these activities was small, Fidel criticized them as early as 1982 and subsequently the government imposed heavy taxes on them. Fidel stepped up his attacks on private activities, accusing participants of being greedy and corrupt, a harbinger of policy changes to come. Externally, the rise to power of Mikhail Gorbachev in the Soviet Union in 1985 and the launch of his perestroika and glasnost policies, drove pressure within the Soviet Union to reduce trade and subsidies to Cuba and to demand more efficient use of the assistance given to the island. To make matters worse, in 1986 Cuba suspended servicing of its foreign debt with Paris Club members, resulting in a freeze of new credit to the island that continues to this day. In the United States, Presidents Ronald Reagan and George H. W. Bush maintained the economic embargo, providing Cuban authorities with justification to tighten internal controls as an alleged imperative to defend the country against an invading power.

The improving social and economic situation, coupled with important policy changes in the Soviet Union and pressures on the island to use Soviet assistance more judiciously, should have resulted in changes in Cuba along the line of those occurring in the Soviet Union and Eastern Europe. However, Fidel and the old guard feared that perestroika and glasnost in Cuba would weaken the revolutionary spirit, lead to social tensions, destabilize

the regime, and erode their power and control. A new idealist cycle, involving rectification of errors and negative tendencies, was launched by Fidel in mid-1986 and lasted until 1990. In theory, the new policies sought middle ground between the “idealist errors” of 1966–1970 and the “economic (pragmatist) errors” of 1971–1985. In practice, most of the policies of the rectification process shared the same antimarket tenor of those of the previous idealist cycle, although not as extremely: acceleration of the process of elimination of private farms; halt of decentralization and return of economic policymaking to the political leadership (replacement of the Central Planning Board—JUCEPLAN—by a new agency led by a politician from the PCC’s Political Bureau);<sup>3</sup> expansion of rationing and elimination of parallel markets; termination of free agricultural markets and of self-employment (the rationale for their elimination was that they were unnecessary and the state would assume their functions); severe restrictions on housing construction and swaps of private homes; reintroduction of voluntary work through the creation of military-style construction brigades; massive use of labor mobilization in agriculture; drastic reduction in the use of material incentives and reinstatement of moral incentives; and renewed emphasis on egalitarianism and free social services.

A new development strategy, centered on a food production program, set unrealistic targets, predicting that within five years the island would be self-sufficient in food production and would generate surpluses of food for export. A second, more pragmatic strand of the strategy was the development of the biotechnology industry, heavily promoted as a source of export revenue with the expectation that Cuba would become a world power in this industry. A third element of the strategy—and the most sensible—was the promotion of foreign tourism with foreign investment.

This idealist cycle lasted four and a half years, the same as for the 1966–1970 idealist cycle. Although publication of the Cuban official statistical yearbook, *Anuario Estadístico de Cuba*, was suspended after the 1989 issue, information from other sources shows that policies implemented during this cycle caused a recession, and Cuban society deteriorated according to virtually all socioeconomic indicators: the rate of economic growth was negative, monetary liquidity expanded significantly, fiscal deficits returned and expanded, the merchandise trade deficit reached historical highs, and open unemployment continued to rise. There is no information regarding inequality, but it probably declined in view of the measures taken. The urban population “at risk of poverty”—a euphemism for the internationally used term “poverty incidence”—was estimated in 1988, for the first time, at 6.3 percent.

### *Crisis and Market-Oriented Reforms, 1991–1996*

At the start of the 1990s, Cuba suffered its most severe economic crisis under the revolution and probably since the Great Depression. External and

internal factors were behind the crisis and the launch of a new pragmatist cycle. The first and most significant external factor was the disappearance of socialism in the Soviet Union and in Eastern Europe as well as of the CMEA, which resulted in the immediate loss of price subsidies and soft loans that had amounted to US\$65 billion from the Soviet Union alone between 1960 and 1990; the halt of hundreds of Soviet investment projects and the return home of Soviet technicians; and the virtual end to all trade and economic aid from Eastern Europe. Cuba's foreign trade contracted by 75 percent, because about 70 percent of it was with the Soviet Union and that nation stopped importing Cuban nickel, citrus fruits, cigars, and other products; stopped exporting consumer, intermediate, and capital goods; and severely cut back on oil shipments. In a matter of a few years, trade between the two former allies was pared back so drastically that it basically turned into bartering sugar for oil at reduced volumes and at world market prices.

A second external factor that contributed to the crisis was the hardening of the US economic embargo, through the Torricelli (1992) and Helms-Burton (1996) legislation. The Torricelli Act banned subsidiaries of US corporations from trading or investing in Cuba and banned foreign ships used in Cuban trade from entering US ports. The Helms-Burton Act resulted in tougher provisions: for example, it banned imports of Cuban products from third countries and allowed US citizens to sue in US courts persons or corporations that "trafficked" in property confiscated by the Cuban government, and restricted the issuing of US visas to persons convicted of "trafficking."<sup>4</sup> The European Union, Canada, and Mexico protested the extraterritorial reach of the Helms-Burton Act, enacted countermeasures against the United States, and threatened to challenge the law before the World Trade Organization. Based on a provision of the law, Bill Clinton suspended every six months during 1996–2000 both the suing of "traffickers" and the imposition of sanctions, a practice that subsequently has been continued by all US presidents through the end of 2012.

The internal factor was the recession of 1986–1990, which had its roots in the Rectification Process. Contrary to trends in the rest of the world, the Rectification Process reversed the timid but positive economic reforms of 1975–1985, returned to moral incentives, and embarked in a failed food self-sufficiency plan. The recession left Cuba in a vulnerable economic position to confront the collapse of the Soviet Union and the socialist camp. In our opinion, had Cuba maintained the market-oriented reforms of the pragmatist cycle, it may have been better equipped to face the economic challenges of the 1990s and perhaps mitigate to some extent the effects of the crisis.

The economic crisis reached bottom in 1993; comparing 1993 and 1989 levels, real gross domestic product (GDP), adjusted for inflation, fell by 35 percent, per capita GDP by 41 percent, and physical production of sugar by 48 percent, of nickel by 36 percent, of citrus fruits by 32 percent,



and of fish and shellfish by 63 percent. Monetary liquidity rose by 22 percent, to 73 percent of GDP; the value of exports declined by 80 percent and of imports by 75 percent, provoking a sharp shortage of foodstuffs, fuels, manufactured products, and raw materials and parts. The only positive developments were increases in the production of crude oil and of hard-currency revenue generated by the international tourism industry and a decline in the trade deficit resulting from a sharp fall in imports.

The crisis had other adverse effects as well. The rationing system was expanded to encompass nearly all consumer goods and rations were cut such that they covered barely half of monthly food needs of the average consumer. The black market grew rapidly and so did prices. The loss in the value of the Cuban peso resulted in a drop to one-tenth of the real average salary, which, combined with generalized shortages, spurred illegal activities and theft from state enterprises. This also had a negative impact on worker effort, bringing about an increase in absenteeism and a drop in productivity. The quality of all social services deteriorated severely. These developments offset many of the gains of earlier years and fed feelings of frustration and alienation among the population, eroding the regime's political base. In August 1994, hundreds of residents of Havana rioted in the streets to protest against the government, the first popular action of such nature and magnitude under the revolution.

At the beginning of the 1990s, a debate about economic policies and strategies resumed after a long hiatus since the 1964–1966 debate over the appropriate model of socialism to pursue. The debate this time was not over whether or not market instruments should be used, but rather the degree of their usage and how to do so within the context of a socialist system in order to avoid or mitigate potential negative effects. At the risk of oversimplifying a rather complex situation, there were essentially two positions. The most advanced reformers supported deep structural changes (but not neoliberal) that would reach to the roots of the economic problems and guarantee sustained economic growth in the long term, although they were concerned about the negative social effects of such policies. Meanwhile, orthodox thinkers (minimalists) supported only selected market-oriented measures to stop the economic freefall, reduce inflation and the fiscal deficit, strengthen the value of the peso, promote economic growth, and reduce social adverse effects, while keeping to a minimum the risk of destabilizing the regime.

The reformists were principally academics (economists and other social scientists) and technicians, who saw market reforms as the lesser of two evils. Some of them argued that repressing markets was futile, as they would emerge under any circumstances, as had been demonstrated by the black market. Besides, to the extent that the state was unable to meet the urgent basic needs of the population, the reformists argued that the state



should permit regulated markets or private enterprise to fill the gaps. Others supported the privatization of personal services that they were convinced the state was incapable of delivering to the population, and reestablishment of free agricultural markets, self-employment, and other mechanisms that had been de-emphasized or abolished during the Rectification Process. The reformists believed that the private sector could make positive contributions; for example, it could check the state monopoly in certain areas, promote competition and increase efficiency, create productive employment opportunities, and spur economic growth. The minimalists feared a snowballing effect, as a growing private sector would put additional demands on the state sector for inputs, create and accumulate wealth, and present a challenge to the government. A common apprehension was the adverse consequences that market reforms had caused in the Soviet Union and Eastern Europe, particularly the potential sharp reduction or disappearance of the social safety net: high open unemployment that would create serious political and social problems, income inequalities that would weaken population unity, increases in prices that would reduce significantly the purchasing power of low-income groups, and deterioration of social services.

Fidel initially opposed market-oriented reforms. In 1992–1993 he rejected commercial relations between state enterprises, including farms, and the private sector, as well as free agricultural markets and self-employed public vendors. In fact, he warned that the revolution would continue to expand state ownership of the means of production, nationalizing even the remaining small farms, and that any existing economic ills would be resolved through state action. He criticized supporters of reform within Cuba, calling them disaffected, defeatists, pseudo-revolutionaries, and traitors.

To confront the crisis, the government enacted an emergency plan (called the “Special Period in Time of Peace”) that allocated scarce resources to the country’s most vital needs. This was in fact a structural adjustment program, although it tried to protect social services as much as feasible. To halt the economic freefall and promote economic growth, several measures to stimulate the external sector were taken: promotion of international tourism, efforts to attract foreign investment, and redirection of foreign trade to Western nations. The new development strategy sought to keep the changes within enclaves in order to prevent “contamination” of the domestic economy and the socialist system. The results of these policy measures were modest at best and the economy continued to deteriorate. As the crisis deepened, in 1993 the government reluctantly introduced market-oriented reforms geared to the domestic economy; these measures were of limited scope, were taken in a piecemeal fashion, and were implemented cautiously to prevent the reforms from getting out of control.

This second pragmatist cycle embodied the most significant market-oriented reforms implemented up to that time under the revolution, through

the following measures: (a) reduction in collectivization through the transformation of state farms into a new type of cooperative—the Basic Unit of Cooperative Production (UBPC)—with some degree of autonomy from the state and the granting of small plots of lands within the UBPCs to farmers for production for family consumption; (b) decentralization of economic decisionmaking, initially regarding foreign trade and later also extending to the national economy through the creation of quasi-private and mixed enterprises; (c) reinstatement of the central budget as a key fiscal policy tool and implementation of measures to diminish public expenditures (e.g., cut subsidies) and increase revenue (e.g., impose new taxes), and reduce the monetary overhang; (d) enactment in 1995 of a more flexible foreign-investment law, creation of free trade zones, authorization for foreigners to buy real estate to be used for offices, homes, and tourism development, as well as authorization for Cuban citizens to rent a portion of their homes to tourists, legalization of the holding and use of foreign currencies (principally dollars), as well as of the receipt of hard-currency remittances sent from relatives and friends abroad, and increased flexibility of family visits to the island; (e) reduction in the scope of the rationing system, ability to purchase some goods in free agricultural and artisan markets at prices set by demand and supply, creation of the “convertible peso” (CUC), and opening of state-run hard-currency exchange houses (CADECAs) to buy and sell foreign currencies as well as of foreign-currency stores (TRDs) to sell goods to the population who are able to pay in hard currencies; (f) reopening of free agricultural markets and opening of artisan markets; (g) self-employment authorization in 157 specific occupations, among them small restaurants (*paladares*) and private taxis; (h) virtual elimination of voluntary work and substantial rollback of labor mobilization; (i) reduction of egalitarianism, broader acceptance of income differentials, and preference for economic incentives over moral incentives; and (j) increase in the price of certain public services and charge for others that were formerly free, although public health and education continued to be free.

This cycle lasted approximately six years, although the most significant and most market-oriented reform measures were implemented between 1993 and 1995. Beginning in 1994, the market-oriented policies began to generate an economic recovery, although precrisis economic levels were not recovered. Compared to 1993, the trough of the economic crisis, economic indicators in 1996 showed considerable improvement: GDP growth swung from negative (−14.9 percent) to positive (7.8 percent), the strongest growth rate since 1985; monetary liquidity fell from 73 percent to 42 percent of GDP; the inflation rate fell from 26 percent to negative (deflation); the fiscal deficit declined from 34 percent to 2.5 percent of the budget; exports and imports rose by 72 percent and 80 percent respectively (the merchandise trade deficit grew by 89 percent, but was still about half of its absolute

value in 1989); the value of the peso (CUP) with respect to the US dollar in CADECA exchange houses appreciated from 95-to-1 to 19-to-1. Negative effects included increases in open unemployment, from 6.2 percent to 7.6 percent, and in inequality, although there were no statistics on the latter.

### *Slowdown and Halt of Reform, 1997–2003*

The aforementioned pragmatist policies stopped the sharp drop in GDP and started a partial recovery. However, in our opinion, they generated distrust from Fidel and the minimalists due to their concern that the processes of de-collectivization, decentralization, delegation of governmental economic power, and growing economic independence of farmers, self-employed workers, and others would weaken the state and the power wielded by the leadership. Additional angst was caused by the growth of open unemployment and inequality; the latter particularly ran counter to the ideological preferences of the orthodox.

Pragmatist policies were subjected to strict government controls that prevented them from reaching their full potential and often led to their demise. For example, foreign investments exceeding US\$10 million had to be approved by the Executive Committee of the Council of Ministers; foreign investors were normally limited to 49 percent participation in joint ventures; moreover, joint ventures were not permitted to contract or pay workers directly, as there was a state agency charged with the duties of collecting the salaries from the employers in convertible currency and paying the workers in pesos. The agricultural cooperatives (UBPCs), unlike their Chinese and Vietnamese counterparts, lacked independence to decide which crop to plant, to whom to sell their output, and at what price; the state essentially made those decisions and purchased nearly all of the output produced by the cooperatives at government-fixed prices that were well below market prices. Substantial licensing fees and taxes were levied on the self-employed, at the same time that their businesses were subjected to frequent inspections and heavy fines for alleged violations. Small private restaurants (*paladares*) were first authorized, then banned, and finally authorized again, but subject to heavy regulations: a limit of twelve seats, employment of family members only, restrictions on which meats and seafood could be sold, and high taxes. Private taxi drivers suffered initially the same uncertainty as did the *paladares*, and later were prohibited from serving tourists. The exchange rate of the so-called convertible peso (CUC) is fixed unilaterally by the government—that is, it is not determined by international currency markets and is exchanged on the black market at lower rates.

In March 1996, Raúl publicly discussed the negative effects of the market-oriented reforms, many of which he had supported, as well as the political challenges they posed. Several reformers were censured and

removed from their posts, among them three internationally known economists who had published an important book about the need to move faster and deeper with the reform process within socialist parameters.<sup>5</sup> This purge put an end to the public debate on economic policy. While some additional reform measures were implemented after 1996 (for example, one reforming the banking sector and another creating free trade zones), from that point forward and through 2003 the process stagnated. Some measures that were discussed in 1995–1996 were never implemented: the elimination of redundant workers in the state sector, achieving the convertibility of the peso, authorizing individuals to operate their own businesses, a general reform of prices, and the requirement that all workers contribute to their social security pensions (only 11 percent of the labor force made contributions in 2012).

With production costs higher than prices in the international market, Fidel launched a major restructuring (dismantling) of the sugar industry: 45 percent of the sugar mills were shut down, 60 percent of sugarcane lands were shifted to other purposes, and 100,000 workers were laid off. The logic of the plan was that the downsizing of the industry would free up resources that could be used more productively in other economic endeavors.

The government judged—erroneously—that the problems associated with the economic downturn, the fiscal deficit, and inflation had been overcome, and so had the risks of political instability. The leadership probably judged that additional moves toward the market would enhance the risk of loss of economic and political power as well as adverse social effects. As in 1986, the political logic of Fidel and of the minimalists prevailed over the economic logic of the reformists, with the anticipated adverse impact on the economy and living standards. To address popular discontent and confront the looming peaceful dissident movement, in 1999 Cuba enacted Law no. 88, on the Protection of Cuban National Independence and Economy, which provided for jail sentences of between eight and twenty years and seizure of assets from citizens convicted of political crimes such as collaborating with foreign journalists, accepting payment for such collaboration, possessing or distributing “subversive materials” (independent publications not authorized by the government), disrupting the public order by participating in demonstrations, and so on. Based on a right enshrined in the Cuban Constitution, the Varela Project, spearheaded by Oswaldo Payá, a human rights activist and winner of the Sakharov Prize for Freedom of Thought (awarded by the European Parliament), collected over 11,000 signatures from Cuban citizens calling for a referendum to permit freedom of expression, hold free elections, grant amnesty to political prisoners, and permit the creation of small businesses. During a visit to Cuba in 2002, former US president Jimmy Carter made a speech (in Spanish) on national television, in which he described the elements of the Varela Project. A pastoral letter issued by Roman Catholic cardinal Jaime Ortega in 2003 called on the government to allow a political and economic opening and echoed some of the same proposals as in

the Varela Project. In the aftermath of government-organized public demonstrations against the Varela Project, not only was the latter soundly rejected by the National Assembly of People's Power in July 2002, but the Constitution was amended as well with the addition of a new article proclaiming the "irrevocability" of Cuba's socialist system. In the spring of 2003, the government arrested seventy-five dissidents (economists, journalists, writers, librarians, supporters of the Varela Project, human rights activists), who were charged with violating Law no. 88 and condemned to long jail sentences. These actions provoked criticism from the international community, including from world personalities who up to that time had supported the revolution. At about the same time, several Cuban officials who had supported the reforms were dismissed from their posts.

The stagnation of the reforms had negative economic consequences. Comparing 1996 and 2003: the GDP growth rate slowed in 1997–1998 and in 2000–2002; monetary liquidity increased in absolute terms beginning in 1998 and reached a peak in 2002 (43 percent higher than in 1996); the rate of price change, which was a negative 4.9 percent (deflation) in 1996, turned to positive 7 percent (inflation) in 2002; the fiscal deficit rose to 3 percent of the budget in 2002–2003; the merchandise trade deficit almost doubled over the period, reaching a historical high of US\$3 billion in 2003; and the aftermath of the September 11, 2001, terrorist attack on the United States led to a brief decline in Cuban tourism in 2002. The restructuring of the sugar industry provoked a 47 percent fall in production in 2004–2005, although the plan expected that the sugar plantations and mills that remained in operation—adduced to be the most productive—would partly compensate for those that were shut down. There are no statistical indicators that would permit a comparison of the social situation between 1996 and 2003, but those that are available suggest that there was a deterioration. Inequality increased markedly, with the Gini coefficient jumping from 0.250 to 0.407 between 1989 and 1999, while the ratio of revenue between the richest quintile and the poorest quintile grew from 3.8-to-1 to 13.5-to-1. The average monthly salary fell by 45 percent between 1989 and 2002. The urban population "at risk of poverty" rose from 6.3 percent in 1988 to 20 percent in 1999, while the share of the population who had a "perception of being poor" in a survey conducted in the city of Havana in 2002 was 31 percent. The only positive performance was with respect to open unemployment, which fell from 9 percent in 1996 to 3.3 percent in 2002, but at the cost of expanding labor surplus in the state sector.

### *Reversal of Reform, 2003–2006*

Active reversal of the reforms began in 2003 under the aegis of the "Battle of Ideas," an ideological construct that returned conscience and voluntarism to the center of policymaking, consistent with previous idealist cycles. In

2004, José Ramón Machado Ventura, member of the PCC's Political Bureau (and in 2012 its first vice president), strongly criticized government officials who had been copying capitalist management techniques so well that they had become capitalists themselves, and warned that liberalism, tolerance, and lack of control were harming the nation. The reversal of the reforms was centered on three policy strands (some of them also were geared to control hard-currency expenditure due to the severe scarcity, as well as to fight corruption).

First was the re-centralization of economic policymaking, attained through ten measures: (a) central control of imports and exports, which had been delegated to state enterprises and were brought back under the Ministry of Foreign Trade; (b) ban on state enterprises conducting their activities in convertible currencies; (c) sale (transfer) of all hard-currency holdings and future hard-currency earnings generated by enterprises from exports to the Central Bank of Cuba (BCC); (d) requirement that all enterprises purchase hard currencies from the BCC (with a surcharge) to finance imports; (e) ban on state enterprises with respect to providing eighty-seven services formerly billed in hard currencies, and transfer of such activities to the state; (f) creation of a single account at the BCC, where state enterprises were required to deposit all earnings in hard currencies and convertible pesos, irrespective of their source; (g) requirement that all state enterprises obtain BCC permission to make payments exceeding 5,000 convertible pesos; (h) prohibition on state enterprises and banks from accepting payments or deposits unless approved by the BCC; (i) re-centralization of state tourism enterprises under the Ministry of Tourism and strong controls on tourism personnel; and (j) weekly review and approval of the budgets of state agencies by the BCC. The second policy strand consisted of curbs on the already small private sector: a ban on state employees, managers, and military officers engaging in self-employment; removal of some forty self-employment categories that had been previously authorized; cutback of licenses for about 28 percent of the self-employed who had received authorization to operate (including the virtual ban of private taxis); and closure of nearly all *paladares*, besieged by heavy fees and taxes and frequent inspections. The third policy strand consisted of implementing a de-dollarization policy: disallowing the use of the dollar as a means of exchange throughout the nation, imposing a 10 percent surcharge to exchanges of dollars for convertible pesos, and "appreciating" the CUC by 20 percent; moreover, to soak up more dollars being held by households, prices of consumer goods offered at TRDs were increased between 10 and 30 percent in 2004.

With sugar output falling by two-thirds of its average output between 2002 and 2007, the development strategy shifted from goods exports (except for nickel, which experienced record-high prices in international mar-

kets), toward export of professional services, such as those provided by physicians, nurses, teachers, sports trainers, and security personnel.

The three previous idealist cycles not only were incapable of addressing the country's socioeconomic problems, but also actually worsened them, provoking a succession of crises and requiring subsequent policy corrections. Why, then, a fourth attempt at centralization of policymaking and reduction of the role of the private sector? According to the official discourse, the new ideological thrust had the following objectives: combat corruption and lack of discipline, correct neoliberal and capitalist errors, reduce inequalities, curb hard-currency self-financing by enterprises and stop hard-currency "leakages," restore revolutionary morality, and confront US threats. But another probable cause for the shift was that the decentralization of economic decisionmaking to hundreds of enterprises, in the hands of thousands of managers, and involving hundreds of thousands of persons in the small but dynamic private sector, was distrusted by the leadership because of the potential risk of autonomy. Finally, the ideological elements of the Battle of Ideas also aimed to distract the population from daily challenges in an environment of shortage.

The most significant external factor that contributed to the reform reversal was the economic support to Cuba from Venezuela under Hugo Chávez. During this period, Venezuela replaced the Soviet Union as the great subsidizer of the Cuban economy: US\$4 billion in credits, investment, and economic assistance in 2001–2007; an unpaid oil import bill of some US\$2.5 billion; payments for over 20,000 Cuban medical doctors and other professionals providing services in Venezuela estimated at about US\$5 billion in 2006; and two-way goods trade between Cuba and Venezuela amounting to US\$2.6 billion, which made the latter Cuba's most important trading partner. China also increased trade with Cuba, becoming the island's second most important trading partner, and also granted credits and entered into investment agreements, although not as significant compared to Venezuela's investments. Finally, although the number of foreign-invested projects declined, key investors such as Canadian firm Sherritt International and Spanish hospitality chain Meliá expanded their holdings in the areas of mining and tourism, respectively, and other multinational corporations entered into arrangements for oil exploration.<sup>6</sup> The combination of these three positive foreign sector developments gave Fidel confidence to dismantle elements of the reforms that ran counter to his ideology.

The return of centralization, coupled with shortages of foreign exchange, brought about a reduction in the operational flexibility of state enterprises, delays in the purchase of imported raw materials, and forfeiture of commitment to pay CUC incentives to the sugar industry, basic industry, and transportation workers. Hotel managers complained that required weekly



budgets forced them to estimate even how many rolls of toilet paper, light bulbs, or pounds of tomatoes would be needed for the following week, creating red tape and taking them away from their duty of providing quality service to customers. The de-dollarization policy generated a significant flow of dollars into the government's coffers in the short term, but had adverse results in the medium term: the restrictions on the use of the dollar, the 10 percent surtax on its exchange, the "appreciation" in the value of the CUC by 8 percent, and the general increase in prices in TRD-incentivized black markets for goods and currencies. Prices of goods on the black market, fed by theft from the state, were lower than those at the TRDs. The revaluation of the CUC made black market currency exchanges more lucrative and Cuban tourism offerings less competitive internationally, contributing to the stagnation in the number of tourists in 2006–2007 and in gross revenue until 2010.

To summarize, the economic results of the fourth idealist cycle were overwhelmingly negative: sharp decline in fixed capital formation, from 12.8 percent to 9 percent of GDP between 2001 and 2005; increase in the inflation rate from –1.4 percent to 5.7 percent between 2001 and 2006; record rise in monetary liquidity to over 20 billion pesos in 2006, 49 percent higher than the level in 2003; growth of the fiscal deficit from 2.8 percent of the budget to 4.6 percent; jump of 70 percent in the goods trade deficit between 2003 and 2006, reaching a new historical high of US\$6.6 billion; increase in the external debt over the same period of 36 percent, setting a new record of US\$15.4 billion in 2006; and decline by 31 percent in the number of foreign-invested enterprises (joint ventures or other arrangements) in Cuba.

Two indicators showed positive performance: a further decline in open unemployment, from 2.3 percent to 1.9 percent of the labor force between 2003 and 2006, and a miraculous jump in GDP growth, from 5.4 percent in 2004 to 11.8 percent in 2005 and 12.5 percent in 2006. The GDP growth rates in 2005–2006 were among the highest in the world—which would suggest that the reversal of the reforms had been wildly successful—but in fact resulted from two statistical manipulations: first, beginning in 2001, the base year for national accounts calculations "at constant prices" was shifted from 1981 to 1997, which resulted in an average increase of 56 percent in the growth rate for each year from 1989 to 2000 (the period for which the two series at constant prices, for 1981 and 1997, are available); and second, beginning in 2003, Cuban statisticians added to the conventional calculation of GDP the value of free social services consumed by the population plus the value of price subsidies to products sold through the rationing system, thereby overvaluing GDP. In contrast to the rosy picture painted by the official GDP statistics, production levels of thirteen out of nineteen key products in mining, manufacturing, and agriculture (sugar, steel, fertilizers, cement, shoes, soap, citrus fruits, rice, milk, eggs, fish and shellfish, raw tobacco, and cattle) were from 19 to 94 percent lower in 2006 than in 1989;



electricity production was unchanged in 2006 from 1989, but lower on a per capita basis, since population had grown over the period by 7 percent; and production was higher in 2006 than in 1989 for only five key products (oil, natural gas, nickel, root crops, and cigars). The previous analysis of underestimation of unemployment is also applicable to this cycle and will be elaborated in Chapter 4.

#### *Raúl's Structural Reforms, 2007–present*

The dreadful economic results accumulated over the several idealist cycles, worsened by the global financial crisis, brought about a slowdown of Cuban GDP growth in 2007–2009 and a contraction in mining production, segments of manufacturing, and most of agriculture; a significant rise in the budget deficit; and new historical heights in monetary liquidity, deficit in the goods trade balance, and external debt. To confront these challenges, in 2007 Raúl promised structural reforms that gave rise to the third pragmatist cycle, the strongest under the revolution. Following his call for a national economic policy debate, reforms started slowly and modestly. Since 2010, however, there has been an acceleration of reforms, many of which were approved by the Sixth Congress of the PCC in April 2011, and were still in the process of being implemented at the time we completed writing this book.

Raúl has dismantled to a large extent the Battle of Ideas programs, which previously were assigned a larger budget than some ministries. While Raúl has maintained the economic socialist model (central planning and predominance of state enterprises), he has proclaimed that such model must be “updated” to account for the market and private enterprise. The principal measures taken to date confirm the robustness of the current pragmatist cycle: (a) de-collectivization (for example, transformation of some ministries into state enterprises, dismissal of redundant workers from the state sector, expansion of the private sector, distribution to individuals of idle state lands in usufruct, greater flexibility for enterprises in setting prices, authorization for sale of homes and automobiles); (b) decentralization of decisionmaking (for example, allowing self-financing of state enterprises and cooperatives, allowing cooperatives to set the sale price of their output, and allowing agricultural producers to sell directly to state and to tourism enterprises); (c) larger role for the budget and its relation with fiscal and monetary policies, with tax reform aimed at increasing government revenues; (d) eradication of voluntary work and of construction brigades because of their inefficiency; (e) gradual elimination of the rationing system and increased role of market prices in resource allocation; (f) expansion of self-employment to cover 181 occupations, permission for private transportation service providers—including taxis—to operate, and creation of cooperatives in production and services; (g) permission for producers to sell their output directly at free agricultural markets; (h) criticism of egalitarianism,

virtual elimination of moral incentives, and predominance of material incentives; and (i) reduction in social expenditures, which must be based on economic criteria and availability of fiscal resources. Meanwhile, the open unemployment rate has increased and so has income inequality. These measures and their effects will be analyzed in Chapters 4 and 5.

### **Conclusion: Failure of Idealist Cycles and Structural Reform**

For more than five decades, socialist Cuba's policies followed a recurring pattern of idealist and pragmatist cycles, successively moving away from or toward the market. These cycles have lasted, on average, four to five years each. The frequent swings in the economic-ideological pendulum brought about contrasting policy prescriptions that created instability and uncertainty and had adverse effects on economic performance (it is worth noting that the longest cycle, the first pragmatist cycle, 1971–1985, which lasted fifteen years, is the one that achieved the most favorable and stable results). Fidel was the key internal factor in the generation of the cycles until his illness and transfer of power to Raúl in 2006.

The evolution of the sugar sector can be used to illustrate the effects of the policy zigzags: out of favor and perceived as an instrument of underdevelopment in 1959–1966; favored greatly and showered with resources diverted from other sectors of the economy in 1967–1970; provided with investment resources and subsidized by Soviet prices in 1971–1989, which resulted in high and stable levels of production; left to its own devices and shrinking when price subsidies ended in 1990–2003; and restructured through sharp reductions in capacity and production in 2004–2011 (at the time of this writing, Raúl may be attempting to revive it). The restructuring of the sugar industry (sharp agricultural and industrial capacity cuts) was carried out with a short-term perspective, at a time when world sugar prices were low; more recently, world sugar prices have risen substantially, putting into question earlier decisions. Moreover, a portion of the sugarcane fields that were demolished could have been used to produce cane for bio-fuels, as has been done in Brazil.

The first two clearly delineated idealist cycles (the Fidel-Guevarista cycle and the Rectification Process) brought about crises in the economic organization model and the development strategy, leading to economic and social deterioration and threatening the stability of the regime. On both occasions, Fidel shifted gears and reluctantly accepted the introduction of market-oriented reforms. The first two pragmatist cycles improved economic and living conditions, but accentuated inequalities and, in the first case, also increased open unemployment. The exaggerated egalitarianism associated with the idealist cycles was one of the factors responsible for

weak economic performance through its adverse impact on incentives. It should be noted that the sharp decline in open unemployment was accompanied by large increases in underemployment or disguised unemployment with a reduction in labor productivity and real salaries; moreover, from the end of the 1990s to 2010, open unemployment was understated by ignoring the growing hidden unemployment. The fourth idealist cycle also had negative economic impacts masked by statistical manipulation of GDP.

Fidel played a key role in launching and ending each of the cycles, although other contributing factors were also at play. Beyond Fidel's ideological preferences, the decisions to slow, halt, or reverse pragmatist cycles and return to idealist cycles that were destined to fail were driven, in our opinion, by fear on the part of Fidel and the political leadership of losing political control. Political logic, therefore, prevailed over economic logic, even if it resulted in deterioration of economic and living standards. The political leadership has not been harmed by the negative effects of its actions, since it is protected against such through the perks of power; the political leadership is also not subject to public transparency and accountability processes, as currently there is no possibility that these leaders would be removed from their posts through true democratic elections.

Idealist cycles prevailed over pragmatist cycles, compounding and deepening economic challenges, and making them more difficult to solve, including a massive bureaucracy, at all levels of government, plagued by corruption. In November 2005, Fidel warned that while enemies from abroad had plotted unsuccessfully to destroy the revolution, the revolution itself could self-destruct. At the time Raúl assumed power in 2006, the economic and social situation was unsustainable. Thus in 2007 he publicly announced that structural reforms (pragmatic policies) were the only way to tackle the nation's problems. While by the end of 2012 the Cuban government had implemented numerous positive measures, the road ahead was long and winding. Broadening and deepening of reforms was essential for achieving a high and sustained rate of economic growth, higher labor productivity, reduction in excess monetary liquidity, elimination of monetary duality, decrease in the goods trade deficit, creation of private sector productive employment to absorb excess workers dismissed from the state sector, increases in real salaries and pensions, and improvement in the quality of social services. At the time of this writing, the possibility that Cuba will return to an idealist policy cycle does not seem feasible.

## Notes

1. This typology was originally presented in Mesa-Lago, 1994, and expanded, systematized, and updated in Mesa-Lago, 2000, 2003, and 2009b. This chapter updates

it through 2012. The statistics used herein originate from Cuban official sources or from the above-cited works by Mesa-Lago, or are presented in other chapters of this book. For other interpretations of cycles or stages of Cuban economic history, see Pérez Villanueva, 2010c; Santamaría, 2011. For a comparison of Cuba's socioeconomic situation in 1958 and 2008, see Mesa-Lago, 2009a.

2. An econometric analysis for the period 1980–2005 conducted by a Cuban economist supports Mesa-Lago's hypothesis (although the author does not cite his work): during cycles associated with centralization policies (idealist), Cuban productivity and GDP declined, while both rose during cycles associated with decentralization policies (pragmatist) (Doimeadios, 2007).

3. The director of JUCEPLAN, Humberto Pérez, who also led the economic reforms, was dismissed and tried on charges that he had mechanically reproduced in Cuba a reform model not suitable for the island. Years earlier, Raúl had sent Pérez to Moscow to study economics and planning and later supported him as director of JUCEPLAN. Fidel assigned Raúl to preside over the tribunal that tried and dismissed Pérez.

4. Just as he had derailed détente efforts by Presidents Gerald Ford and Jimmy Carter, in 1996 Fidel ordered his air force to shoot down, over international waters, two small unarmed aircraft piloted by Cuban Americans. This action reversed the congressional support that President Bill Clinton had generated to defeat the Helms-Burton Act, thereby clearing the way for its passage.

5. Julio Carranza, Luis Gutiérrez, and Pedro Monreal, *Cuba, la restructuración de la economía: una propuesta para el debate* (Havana: Editorial Ciencias Sociales, 1995). The first and third authors were residing outside the island as of 2012.

6. Since 2001, a change in the US embargo has permitted the exportation of food and medicines to Cuba.