CASE STUDY

The Economy of Cuba*

Geographic, Social, and Economic Indicators

Area:	114,524 km^2
Population:	11.2 million (2000)
Population (annual growth rate):	0.6% (1998)
GDP per capita (PPP):	$3,967 (1998)
GNP per capita (average annual growth rate):	−8.1% (1989–1993)
Agriculture as share of GDP:	11% (1993)
Exports as share of GDP:	11% (1993)
Under-5 mortality rate (per 1,000 live births):	8 (1999)
Child malnutrition (underweight):	8% (1992–1997)
Females as share of labor force:	39% (1997)
Illiteracy rate (age 15+):	3% (1999)
Human Development Index:	0.783 (medium) (1998)
Life Expectancy	76 (1999)

Cuba, larger than the other Caribbean islands combined (about the size of England), separates the Gulf of Mexico from the Caribbean Sea. From its discovery by Columbus in 1492 until gaining nominal political independence in 1902, Cuba was the center of the Spanish colonial system in the Western Hemisphere. The Spanish eradicated the aboriginal population and imported slaves from Africa to work in the burgeoning sugar industry. The contemporary Cuban ethnic mixture is a complex and seamless continuum from Spanish to African with recognizable additional components including descendants of Chinese laborers imported in

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the nineteenth century. In the two Cuban wars for independence from Spain (1868–1878, 1895–1898), both the leadership and the ranks of the insurgent forces included former slaves as well as Creoles (Cuban-born Spaniards).

In the long decline of Spanish power in Latin America, ownership and control of much of the Cuban economy was acquired by U.S. firms in the nineteenth century. As Cuban independence forces neared victory over colonial rule in 1898, the United States invaded Cuba, and the peace treaty between Spain and the United States later that year transferred sovereignty to the latter. Annexation was considered, but instead Cuban formal independence was declared in 1902 after an elected Cuban government reluctantly accepted an amendment to the first Cuban constitution granting the U.S. sweeping powers of intervention. (The remaining U.S. military installation in Cuba, at Guantánamo Bay, dates from 1902.)

U.S.-based firms remained dominant in most major sectors of the Cuban economy until the revolution of 1959. The largest industries were sugar and its derivatives (e.g., rum), tourism, and tobacco, but other significant sectors included utilities (the AT&T-owned Cuban Telephone Company had only an English name), transportation, and mining. Regulations modeled on southern U.S. Jim Crow laws were imposed, and Havana, the Cuban capital, became infamous for providing U.S. vacationers pleasures forbidden at home. Cuban governments in this period, notoriously corrupt and compliant to U.S. interests, culminated in the brutal dictatorship of Fulgencio Batista.

On New Year's Day 1959, after an improbable struggle, a revolutionary movement with middle-class leadership but initially based in the destitute peasantry of eastern Cuba, overthrew the Batista regime. Its most prominent leader was Fidel Castro, a 1951 Havana University law graduate. The new government immediately instituted dramatic economic changes, including nationalization of agricultural holdings in excess of 400 hectares (largely foreign-owned sugar plantations). In a quick succession of tit-for-tat measures, the United States cut Cuba's sugar import quota, Cuba nationalized other U.S.-owned assets (including petroleum and telephones), and the United States imposed a punitive embargo. In February 1960, Cuba negotiated a sugar-for-oil exchange with the Soviet Union that began the extraordinary transformation of Cuba from a *de facto* component of the U.S. economy to, 2-years later, an anomalous Western Hemisphere nation conducting 85% of its foreign trade with the Soviet bloc.

The extent of Cuba's political subservience to Soviet policy demands over the ensuing three decades is disputed, but that Cuba became quite dependant economically on the Soviet bloc is clear. Cuba exported agricultural products, primarily sugar, in exchange largely for oil and manufactured goods, with an implicit subsidy (estimated relative to world market prices) for Cuba in the range of $5 billion per year. Except for a residual and economically significant sector of private farms, the Cuban economy became almost entirely state-owned and state-managed.

After the U.S.-sponsored invasion by Cuban counterrevolutionaries was defeated at the Bay of Pigs in 1961 and the diffusal of the Cuba Missile Crisis of 1962, in which Soviet missiles were withdrawn and the United States pledged not to invade the island, Cuba then proceeded on a unique path of economic development.

The major consequences of this process of development were sustained and substantial growth in national income per capita and, even more strikingly, a momentous egalitarian shift in the distribution of income. By 1986 Cuba's income inequality index (Gini coefficient) was among the lowest in the world. Especially notable were the transformations in health and education. Despite emigration in the early 1960s of most professionals, largely to the United States, the health and education systems were dramatically expanded until, by the early 1980s, life expectancy, infant mortality, literacy, and scientific and technical education statistics for Cuba approached those of highly developed countries, even though per capita income, though substantially increased since the revolution, remained in the range of less developed countries.

In the early 1960s, Cuba had suffered an enormous economic shock. Abruptly severed from its traditional markets by the U.S. embargo, the country, with great difficulty, reoriented its production and trade to the possibilities and demands of the Soviet bloc. The resulting system differed importantly from Soviet models but was not significantly more efficient. Nevertheless, substantial economic development did take place.

With the collapse of Eastern European communism in the early 1990s, however, Cuba suffered an even more traumatic economic shock than it did when the U.S. embargo was imposed three decades earlier. The advantageous Cuban sugar-for-Soviet oil arrangement evaporated. Essential inputs and spare parts for the whole of Cuban industry and agriculture became unobtainable. Aggregate output (and consumption) plummeted by over one-third.

After sometimes chaotic emergency measures as the crisis worsened in the early 1990s, a succession of fundamental changes in economic institutions and policies have since ensued. Some elements of this restructuring have significantly diminished the control of economic activity by central authorities. Thus a large portion of state-owned land has been turned over to newly organized agricultural cooperatives, which are to some degree worker-managed. A substantial portion of consumption, especially of food, is now allocated through relatively competitive retail markets (although a very meager state ration system remains in place). A sector of self-employed service providers has been established, allowing regulation and taxation of some of what had previously been illicit economic activities.

In a no less dramatic change of policy, certain sectors have been opened to foreign private investment, with Cuba seeking to project itself as "open for business" with competitive advantages in unexploited opportunities and an unusually healthy and well-educated workforce. And, in spite of intense U.S. opposition, billions of dollars of investment have since flowed into Cuba, primarily from Mexican, Canadian, and European multinational corporations. U.S. firms remain on the sidelines, excluded by U.S. (not Cuban) law.

Almost all foreign investment in Cuba takes place in joint ventures with state-owned entities and in most such joint ventures the Cuban partner holds a controlling share. The most noticeable investments have occurred in tourism, which had been almost entirely dormant for three decades. But quite substantial sums have also been committed to petroleum and mineral (especially nickel) extraction and to refining, telecommunications, and the production and marketing of high-value-added agricultural derivatives (e.g., alcoholic beverages, tobacco, and citrus).

Yet even with the growth of foreign investment and cooperative and self-employment, the vast majority of the Cuban labor force remains employed in the state sector, which is still for the most part astonishingly inefficient despite continual, well-advertised campaigns for improvements. The transformation of the economy in the last decade has been wrenching for Cuban society. The dramatic fall in per capita income has recouped only slowly since 1993 and has been accompanied by visible unemployment (thought banished since the early 1960s) and what many see as an "inversion of the social pyramid"—not only has income inequality obviously increased, the few beneficiaries seem to be almost entirely those involved, licitly or illicitly, in the small part of the economy affected by foreign investment, mainly tourism. The U.S. dollar denominates a portion of the Cuban economy from which most Cubans, especially those who have most supported and benefited from the revolution of 1959, feel marginalized. But popular discontent remains tempered by persisting egalitarian access to the health and education systems.

The future of the Cuban political economy is not predictable with any confidence. As has been true for two centuries, much depends on U.S. policies. For example, the immigration policy under which Cubans are granted a uniquely privileged status (starkly denied other economic refugees) has dramatically shaped Cuban domestic and foreign policy, as has an array of U.S. economic sanctions, which became even more stringent in the 1990s. An end to this embargo would let loose a wave of catch-up U.S. investment that could conceivably return Cuba once again to the status of a *de facto* U.S. economic subsidiary, although U.S. investors would suffer some disadvantage given their late start. Even more important here is the potent Cuban perception that genuine national independence must be maintained. Nationalist sentiment is the bedrock of popular support for the regime still headed by Fidel Castro, which, though by no means the most authoritarian or repressive in the world, remains unwilling to risk domestic political competition.

For over four decades, Cuba has offered an example of economic development in which comparatively high levels of resources for building and maintaining human capital have been provided in an exceptionally egalitarian way. Given the generally low development of the rest of the Cuban political economy, maintaining this development strategy through the process of recovery from the economic traumas suffered a decade ago remains problematic.