

Political Economy of the Cuban Society before the post-Castro Transition

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ABSTRACT

The objective of this paper is to analyse the links between politics and economics in present Cuba and assess their external repercussions into the rest of the world. Cuban society has been challenged for 18 years by a unique experiment in its economy and politics: a combination of isolation and attempts at changing the strands of globalisation. Both had its endogenous and exogenous factors. E.g. by refusing to yield to external pressures of isolation and to get "globalised" with the incumbent capitalist world (as other communist countries did), the Castro regime had to "internalise" these pressures into turning the country to a police state that brought the nation an unparalleled misery. Paradoxically, such a shock strengthened the regime, so that Castros could even respond by re-arranging the world order at quite a significant margin.

What went wrong? Politics of the democratic world towards communist Cuba somehow abandoned the well-proven soft-peddalling approach that led to a "velvet" downfall of totalitarian regimes all over the world. In contrast, all strategic stakeholders opted for a confrontational stance that, after 18 years of practicing, has brought anything but negative results:

- totalitarian Castro's regime survived;
- 12 million Cubans suffered enormously;
- Cuban emigration of 2 million turned the US policies to an irrational fundamentalism;
- Eastern and Western Europe lost its foothold in Cuba;
- the democratic world as a whole found its position in Latin America eroding, while Latin America set adrift and began to follow populist politics;
- geopolitics of the world offered communist China a grand niche to be filled.

As we show, in the case of Cuba there are too many external stakeholders in waiting for future gains. Unfortunately, their motivation is predominantly redistributive, disregarding somehow the natural claims of the main stakeholders – the 11.5 million silenced Cubans trapped in a regime that for long has lost its popular support.

In the paper we analyse the Cuban society from the point of view of four segments of power: rulers represented by Castro brothers, entrepreneurially-minded nomenklatura, expats in Florida and the suppressed Cuban nation. The external world had also four players: the White House, the European Union, Venezuela and China. The outcome of the game reveals

all signs of prisoners' dilemma: the majority of them suffered long-run losses (compared to foregone alternatives) and small short-run gains were generally overwhelmed by deep short-run losses elsewhere. Thus the global political strategies undertaken led to overall suboptimal positions in both the Cuban economy and its social organisation, which polluted the world with its negative externalities. Until now the world lacks mechanism for controlling that the outcome of competing redistributive coalitions does not turn into a bloody clash with the US military power.

Potentially, Europe and the EU-27 could take up one of the crucial positions in the ongoing political battle, provided it could agree on a coherent common policy to Cuba, concentrated on economic co-acting with Cuban people, including its nomenklatura. The united free world has a responsibility to help Cubans mastermind a "sugar revolution" of their own and refrain from touting them by threats. The world should not forget that there was not a single case in the human history where a communist dictatorship would be defeated by a direct external power. On the other hand, there were 33 downfalls of communism induced without external aggression and based on co-acting between internal vested interests. Under the scenarios of external non-intervention the dismantling of communism was always peaceful, ending in democracy and leading after some 5-10 years to an intensive economic recovery.

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Primum non nocere !

INTRODUCTION

Even though Cuban economy does not offer an attractive market and, as will be explained, the depth of its economic crisis is often underestimated – its political spillovers are strong enough to shake any economic superpower or even cause a conflict between superpowers. Cuban politics have wide externalities to the outside world and especially within Latin America. Taken from the point of view of liberal economics or traditional democracy, such externalities have been negative. The alliance of Havana with Caracas, Beijing, Moscow or Madrid in the environment of world's uncertainty about energy, terrorism and viability of traditional welfare-state capitalism, and the strains about emerging new geopolitics of the globalised world, raises high opportunity costs among these players, which pose a threat of destabilising otherwise natural and advantageous economic relationships between both subcontinents of America and their coexistence with Europe or Asia.

There are several countries that claim the legacy of historical ties with Cuba, which are expected to yield preferential economic treatment: Spain as an old colonial power, United States as the centre of local gravity shielded by Monroe doctrine, Russia as the past mastermind and China as the potential dominant partner of the region. The rising democratisation in Latin America, shifting the orientation of governments further to the left and giving anti-American Cuba an image of vindication to be followed, thus concerns all of them. The unresolved conflict between the Central Europe and Spain about how to set the strategic EU policies to Castro's regime has shunted the EU role further closer to a second-class.

Nevertheless, Cuba still remains an important catalyst of the Latin American politics because of its ideological staunchness, so permanent vis-à-vis the fads of other regimes in the region. Also the mystery about the Cuban future after the brothers Castro will depart raises many vested interests. For some, Cuba offers an inspiration how to deal with the US big brother, how to gain local admiration or how to get rid of poverty and injustice. For some others, Cuba is one of the last countries in the world where the shift of property rights (from the far-out state ownership to the private one) could be a source of enormous speculative

gains. It is also expected that the recovery of its devastated economy would attract vast foreign investments and trade (Fortado, 2006). Last, but probably the most important, some imagine that the collapse of the communist regime in Cuba could be replaced by its free market opposite, becoming so a leader in the backlash to present Latin American socialist/populist drive.

As we will show, Cuban economy is in shatters and all its leaders agree that another round of "fine-tuning" (i.e. reforms) is necessary. However, the Cuban reformers are not united and the final say rested always in the hands of Fidel Castro, whose ideologically-based decisions have been rife with inconsistencies and economic (though not political) inefficiency. Once it became clear to Castro brothers that Europe was not able to offer Cuba a conflictless alignment, they turned at Venezuela and China. This move became surprisingly fruitful to them, turning upside down previous geopolitical expectations of economically advanced countries after the fall of communism.

The high-strung free world, distracted by the conflict with Islamism, is not so much aware that an alternative economic and political setup has begun to settle in Latin America – one that may end up in a serious diversion from traditional alignments. As the politics of “peaceful rising”, China is “selling” itself to Africa and Latin America as the model for ending poverty. The ever more confident China has been locating almost a half of its foreign direct investments into Latin America ¹ and it has pledged to bring there \$ 100 billion in the next five years (Hawksley, 2006), promising employment, prosperity and justice to poor, which is an attraction that neither Soviet Union nor United States were able to match so convincingly in the past.

Brothers Castro are still the key players in the Cuban political game. Fidel Castro became one the most intriguing political personalities of the last 50 years. He master-minded a most improbable revolution from 1953-59, outfoxed 10 US presidents and 15 CIA directors, withstood the communist collapse after 1989, survived a series of economic catastrophes in the last 15 years and currently sneers at the world’s high-power politics – all making him a magus of the impossible.

Since 2005 Czech diplomacy stood in the centre of the EU controversy over the common politics on Cuba, concentrated on renewing sanctions against Havana. Czechs became the staunchest of moralists by proposing a boycott of the dictatorial regime and together with the Polish became the closest US allies in tightening the embargo against Cuba. It seemed for long that such an initiative could not succeeded in rescinding the more pragmatic Spanish and French approach. Surprisingly, the Czech approach received a wide support in June 2006 and a part of its stringent proposals were incorporated into the EU’s Cuban policy. Europe made a short step towards the US but weakened further its potential for interfering directly with the Cuban real affairs. Castro has fought back in the meantime and his external policies are again on the ascent, though his internal policies remain a disaster. The expected rise of Raúl Castro, when his older brother's health further worsened after returning from the summit in Argentina, could lead to changes with unexpected outcomes.

Throughout this paper I will try to separate descriptive statements and facts from normative judgments about them, the interpretation of which depends on the ordering of believed values. Such values must be declared explicitly so that the reader can subject them to his/her own proofs of credibility. The politics about Cuba are deeply immersed in ideology (i.e. in pre-selected normative ballast, the validity of which is not opened to questioning) that descriptive papers of political economy should avoid. Since also the facts and statistics about Cuba could not escape the ideological bias, this paper could not escape relying on first-hand anecdotal experience. It is an aim of this study to provide a vehicle for shedding new light

¹ Maybe at the end of 2006 China has changed its strategy and turned investments into natural resources in Africa and participation in African development the priority of their foreign capital expansion.

about the present economic and political situation in Cuba and help in posing new questions about its future evolution.

The author will gladly change his views and adjust to criticism, especially if it is based on new empirical evidence and its interpretation free of ideology in making this paper more relevant for the thoughts about the future of the Cuban society.

CUBAN ECONOMIC STANCE

Cuban past prosperity, when its GDP per capita in late 1950s was considered to be one of the highest in Latin America, subsided after the revolution. Nevertheless, due to the mobilisation of labour and the support by an annual Soviet block's subsidy of \$5 billion until 1989, Cuba used to be a country that served as a case worth admiration by the majority of developing countries, including often those without a socialist inclination. The viability of Cuba's own economy after losing external support was one of the lowest and its collapse in 1990-91 was inevitable. The Cuban GDP sunk officially by 36%, though unofficial estimates ascribe it a more realistic initial collapse by as much as 50% (Mora, 2002). That was higher than in any other country of the Soviet empire². The breakdown was reflected by an unprecedented decline in the caloric contents of alimentation in 1991-93 (Vogeler, 2004). In 1991 F. Castro declared an emergency situation called "período especial" (Banco Central, 2004), which practically survived until now, even though the government hinted in late 2004 that it was going to be dismantled. But dismantling means introducing serious reforms³. But Fidel Castro stopped them to happen.

The official figure for the GDP of \$ 3000 per capita in 2004 (see the data provided by the IMF (2005), where the total Cuban GDP is \$ 33920 at PPS⁴) is in line with the Cuban government's proclamation that Cuba has weathered the "externally imposed" crisis. This figure was received by converting the GDP in national currency to dollars at purchasing parity standards by adjusting the Cuban price level to the US price level by the coefficient of purchasing power parity of 5.0⁵. For a change, the estimate for 2005 is \$ 3500 at PPS, another nicely rounded figure offering an enticing (but otherwise hardly visible) annual growth of 16.7%.

Estimating both the nominal GDP and the purchasing power of domestic currency are demanding statistical tasks with a large margin of error, especially in the case of Cuba – in a

² That was a similar economic crash like in the war-stricken Bosnia, but still sharper than it was in the cases of Tajikistan, Georgia or Moldova (data of UN ECE, 2005).

³ We might think of the Soviet Union and its replacement of war communism (the closest analogy to "período especial") by NEP (a free market liberalisation directed mainly to agriculture). Similarly it was the Brezhnev – Andropov switchover.

⁴ PPS is an acronym for "purchasing power standard" – an estimation of the GDP in international dollars, which is adjusted to differences in purchasing power parity (PPP) between the United States and the compared national economy. Thus the differences in price levels of two countries can be approximated by an index of ERDI (exchange rate deviation index) that quantifies how the GDP at commercial exchange rate (CER) is related to the GDP at PPS. The latter is estimated in accordance with the hypothesis of absolute purchasing power parity.

⁵ Such could be the theoretical ("shadow") exchange rate between peso-moneda nacional and dollar, provided the absolute purchasing power parity would be valid. In contrast, the actual commercial exchange rate in 2004 was around 25 pesos-moneda nacional per US \$, i.e. five times higher. Similar exchange rate differentials could be found in India or Vietnam. This coefficient hypothetically reflects high purchasing power of peso-moneda nacional relative to dollar, especially if the extremely cheap rationed goods were included. However, the official indigenous "markets" are notoriously undersupplied and Cubans must enter either the black market or the dollar commodity market where prices are much higher. Under such assumption the ERDI should be therefore decreased (e.g. to 4 or even 3), implying also the need for a depreciated commercial exchange rate and a depreciated "shadow" exchange rate at absolute PPP.

society where official producer prices have hardly any economic meaning and where existing consumer prices are earmarked on commodities, which effectively do not exist. So we have to take caution for such international comparisons. In the Cuban case both the commercial exchange rate (CER) and the exchange rate deviation indexes (ERDI) are unreliable braces for the GDP conversion into dollars and its international comparison⁶.

When comparing the GDP per capita in 2004, Cuba after 46 years of strenuous build-up of socialism remained with its \$ 3000 still close to the level of Honduras (\$ 2700), beat the socially devastated Haiti (\$ 1630), but trailed behind Guatemala (\$ 4009). It should be remembered that Cuba was for centuries, until 1959, one of the economic leaders in Latin America. Another criterion could be the standards of social safety network, which protect the inhabitants against the destitute poverty. Here the Cuban social setup (as it is in all totalitarian regimes) stands at high profile: due to direct government intervention (i.e. via compulsory labour commitment and rationing), the citizens are saved now from an exposure to biological subsistence (i.e. contrary to the situation in 1990s), including explicit unemployment, open beggary, homelessness or even criminality, which are a daily threat for nearly a half of inhabitants in the majority of Latin American countries.

However, even though Cuban totalitarian regime can hide by its edicts of taboos and orders many signs of weaknesses, their presence remains. A large part of employment is just a hidden unemployment with negligible or negative productivity and the household disposable income formed by official domestic resources (in contrast to foreign remittances and moonlighting) would rank Cubans among the poorest citizens in the world. The unparalleled deficit is in the lack of all kinds of freedoms, which paralyse the domestic economy: freedoms of employment, contract, sales, transport, housing, etc., which are necessary conditions for making the management efficient. We may call it an economic subsistence (instead of biological subsistence), notwithstanding the fact of having a full-time job, a TV set and that children receive a good schooling. The omnipresent interference of the State into the life of everyone, the rule based on external manipulation, lie, hypocrisy, fear and low expectations, has hardly a parallel in the world. Practically any private economic initiative is prohibited or subject to a bureaucracy turning it to absurdity.

The estimate of the Cuban GDP is a maze⁷. According to the purchasing parity standards, the GDP was \$ 33.9 billion in 2004 (IMF data of 2005). The purchasing parity in poor functionally closed economies without market-based prices of commodities and factors, and with a slanted primary distribution of income are subject to a large bias when estimating the quality and the international values of indigenous products. The estimates at PPS are generally overvalued, as the experience from the assessment of former communist economies in Europe has shown (Benacek, 2005, and 2004).

What concerns the estimates of the nominal GDP in domestic currency, the data are even less transparent. For example, the Cuban Statistical Office reported the GDP for 2003 in constant prices of 1997 at 28.4 billion pesos. That compares approximately with the estimates of \$30.8 billion at PPS by the IMF adjusted to Cuban inflation and saying that 1 peso-divisa = 1 \$. Values quoted in artificial peso-divisa of 1997 offer no clues about the GDP or its price

⁶ The GDP valued in dollars at CER depends on many local institutional and (often random) financial arrangements about the right to enter (or intervene at) the foreign exchange market. Its international comparison is therefore inconsistent. On the other hand, the estimation of the GDP valued at PPS depends on the quality of estimation of domestic price level relative to the US prices in the compared basket of products. Since the basket of products in Cuba and the USA is virtually incompatible and Cuban weights of quantities are also difficult to estimate, also the GDP at PPS in Cuba is a figure with a large standard deviation of its error term.

⁷ Mesa-Lago (2005) analyses the problems of growth and statistical “miracles” in computing the GDP in Cuba. The time series look highly inconsistent, leading to a bias by inflating the results of período especial.

level of 2003 in "moneda nacional" and thus no useful information about the current situation in the standards of living related to wages in nominal terms. We need a heuristic approximation for getting more insights (see Table 1).

If we accept the commercial exchange rate of peso 25 per US\$ in 2004 and estimate the ERDI at the level of 5.0, which should be equal to the "shadow" exchange rate computed under the assumption of absolute PPP, the GDP at commercial exchange rate would be then around 6.8 billion dollars and approximately \$ 600 per capita (i.e. somewhere between that of Vietnam and India). The GDP at current prices in domestic currency would be then at approximately 170 billion pesos. From that amount approximately 25.2 billion pesos can be estimated for the total of household wages in 2004.

The bottom-line of using the GDP per capita for comparing the standards of living in non-market economies is that its meaning at both parities (i.e. as an average quantity at PPS or nominal at CER) is not only fuzzy, but that it also overshoots the real situation of households. In the Cuban case it is particularly so. The alleged economic stability gained in the last 7 years concerns the income of the totalitarian regime only, meanwhile the gain of 11 million of ordinary Cubans is much less satisfactory. The state budget has recovered its hey-day's financial capture, but at the cost of the misery of households.

Table 1: Indicators of domestic product and incomes of households in Cuba, 2004

Indicator	Total billion	Per capita	Remarks
GDP at PPS in US\$	33920	3000	Data of IMF for 2004
GDP at CER in US\$	6784	600	ERDI 5.00
GDP in nominal pesos	169600	15000	CER 25 Pesos/US\$;
Annual wages in nominal pesos	25220	2231	Annual wages implying the share of 15% on the nominal GDP only
Annual wages at CER in US\$	1009	89	This annual wage represents an income of \$ 0.24 per day per capita
Annual disp. income in nominal pesos (incl. subsidies)	51664	4569	Annual disposable income as 30% of the nominal GDP (or less)
Annual disp. income at CER in US\$ (including subsidies)	2067	183	This disposable income represents \$ 0.50 per day per capita

Sources: IMF (2005) and own estimations.

The priority of non-productive state services (such as police, security, defence and bureaucracy) over the productive ones, which requires a very high tax wedge or some similar instrument for „residual claims“, is reflected in a depressive level of Cuban wages. The average monthly wage of 300 pesos (\$ 12), meanwhile it is some 90-170 pesos for farmers (according to the quantity and the quality of harvest prescribed and purchased by the State), doctors 400 pesos and police approximately 600 pesos. 300 pesos buys hardly 30 kilograms of food and the usual choice is between rice and bread. The ration card (libreta) adds some additional 8-10 kilograms per person for a symbolic price, if one is lucky and gets the irregular supplies. That raises the real income by additional 100 pesos. Nevertheless, there are even quantified claims of the Cubans that all these official sources are able to provide subsistence for only about 10-14 days a month. In each case it is clear that Cuban official economy is extremely inefficient, lacking basic incentives for a higher performance. Thus a significant part of the income must be made with funds from other resources – from foreign remittances, endless do-it-yourself, hustling as *jineteros* (touts) to tourists, moonlighting,

pilfering in factories, accepting bribes and committing crime. The roots of Cuban wide-spread underground economy are in its corrupt economic system banning systematically any market mechanisms (Ritter, 2006). In addition, its severe prosecution is going against the last residuals of innovation, which makes the whole economy even more incapacitated. The call for a substantial reform is therefore an objective one.

It may be argued that annual 3600 pesos per wage earner, plus 1200 pesos of rationing per capita, representing together mere 23 % of GDP, is still an incomplete indicator of the living standard because the welfare of households in centrally planned economies depends also on the free provision some goods, which are difficult to enter into the concepts of PPS or ERDI: free living during military exercises, pensions, infant supplements, subsidies to housing and electricity, or food and clothing supplements provided in schools. Nevertheless, even if we assumed that such public provisions and subsidies could bring additional 95 pesos per capita per month, they would not raise the indigenous income at CER over \$ 0.50 per day. That implies, nevertheless, an extremely low standard of living even at PPS, which is confirmed by daily observations of visitors ⁸.

The Cuban standard of living in 1984, as estimated by anecdotal recollections of Cubans, seemed to be nearly a double of that what it was during 1990s and also in conflict with official figures for the situation now. They claim that the real GDP in 2004 lagged behind that of 1989 by -7% only, what Mesa-Lago (2005) takes for overly optimistic. The problem even deepens if we compared the situation of households as the final users of the GDP. Many other figures support the hypothesis of a wide lagging of the present economy relative to 1980s. For example, the gross capital investments per GDP plummeted from 25% in 1989 to 9% in 2003, or the fall in physical output in beef, fish, tobacco, sugar, steel, cement or textiles was within the brackets of 40 through 80 % (Mesa-Lago, 2005). The problem is not in the blockade, as the local politicians claim, but in their management and dis-incentives to work.

Such facts reflect the paradoxes of the Cuban economic performance, which turn up much clearly if we distinguish between that part of the gross domestic income created in domestic production for domestic (indigenous) usage and the incomes received from external resources ⁹. Therefore the latter will include the income from visible exports (\$ 2.4 billion in 2005), the highly positive balance of services (tourism bringing \$ 2.7 billion), remittances from foreign residents and international aid, and net revenues from foreign direct investments. As we will prove later, more than a half of the gross domestic absorption in Cuba at CER is created by foreign transfers.

It is a paradox that the Cuban personal disposable income in real terms net of foreign remittances is one of the lowest in the world. So it would be if 400 pesos from monthly average wages and rationing scheme were converted into 40 kilograms of rice or bread per wage earner (not per capita!). A similar picture is revealed if we consider the per capita household disposable income, which makes 13 pesos per day. In addition, even such a small

⁸ As a fluke of chance, the exchange rate of peso to dollar in 2004 was nearly identical to that of Czech koruna to dollar (25-26 pesos and korunas per dollar, respectively). The comparison of the living standards is also facilitated because Czech controlled consumer prices around 1984 were very similar to those of Cuba in 2004 and the Czech government followed similar priorities at that time, which made also the Czech relative prices similar to those in Cuba. Thus the Czechoslovak net income of 2360 KCS per month in 1984 can be directly compared with present 400 Cuban pesos. I.e. the real personal income in Cuba is now approximately at one sixth of that in Czechoslovakia in 1984. On top of it, the consumer choice in Cuba is still much lower than one sixth of that what was offered in former communist countries.

⁹ The parallel between the GDP and the GNP is not of much use here since the income of foreign entities is distorted. E.g. FDI cannot enter in forms of acquisitions, mergers or green-field investments, but solely as temporary joint ventures. Incomes of tourist joint ventures are controlled by Cuban majority stakes and the extent of transfer pricing is difficult to estimate.

amount is difficult to convert into commodities other than basic food (i.e. rice or bread). The reason is an extraordinary low share of disposable income on GDP. As we have seen, the GDP per capita (\$ 3000 at PPS) is not so depressingly low, if compared with many Latin American countries. Contrary to the fact that both the employment rate (due to high female participation) and the working hours in enterprises are very high (provided there are not stoppages due to the lack of electricity or supplies), the resultant share of disposable income (net of remittances) on GDP is maximally 30%. Cuban workers are therefore some of the most exploited in the world ¹⁰ – and they are well aware of it.

The viability in living standards and the consumer sovereignty are achieved, however, by shifting them to external economic links coming mainly from capitalist countries. Thus by keeping the ordinary citizens as hostages at a margin of economic subsistence, the officially hated Cuban emigration was indirectly attracted to financing the citizens' welfare by legalising its remittances to relatives and transfers from various charities. The household remittances are estimated at \$ 800 million, which increase the annual wages per capita of \$ 89 by additional \$ 70, i.e. by 79%. The domestic disposable income of \$ 183 per capita is raised by 38% ¹¹. In addition, there is a shadow and black economy appended to tourism.

Dollars in cash (but not euros) are taxed by 10%, reflecting the fact that nearly all such transfers come from the United States. Although ordinary Cubans ceased to starve, procuring housing equipment, clothing, transport or medicaments is simply unavailable without pesos-divisa that is for vast majority difficult and humiliating. Cubans were historically accustomed to be a Latin American elite led by national esteem and a local intellectual elite. The present economic and political situation raises too many questions, notwithstanding the official proclamations to the opposite, whether there was any progress done since 1960 at all.

The GDP growth in 2006 was estimated to be over 7%. Although measuring growth in non-market economies with totalitarian regime is highly subjective, the notion that Cuban economy received a strong push recently is credible. As we have noted, the main source of Cuban income is derived from external economic activities, while the domestic production for domestic usage has been notoriously highly inefficient – being paralysed by bureaucracy, lack of inputs and stalled by disincentives to work. Raising it by 5-8% is not a striking change. At the same time rising prices of exported raw material (especially nickel), growing tourism organised by foreign joint-ventures, improved participation in trade with Latin America and massive implicit subsidies on imports of crude oil from Venezuela (estimated at \$ 1 billion per year) are in the core of present growth.

Thus the people crave for a change. They want what they have not known for so long: better food, a choice in the shops and more freedom in their work. Unfortunately, exactly that makes them extortionable, as commented the dissident Raúl Rivero (Rivero, 2005). The people, frustrated so much and for so long, are able to trade-off their rights for democracy by getting material concessions. The communist regime is now fully aware of it. The transition after Fidel can be safely in its hands if they were able to provide funds for better consumption.

¹⁰ For a comparison, the share of the communist government on Czechoslovak GDP in 1988 was 66%. In early 1950s it was approximately 70%. Since the capital depreciation and profits of enterprises were nearly completely "taxed" by the government until the reforms in early 60s., the residual to 100% in 1950 was closely related to the disposable income of households. The share of total disposable income on GDP in stabilised capitalist economies is over 50%. The share of government revenues on GDP is 35-50%. Cuban state capture in the last 15 years was therefore even higher than in the post-Stalinist economies. It was akin to the periods of communist war economies.

¹¹ Since official Cuban statistics about the standards of living are not very credible, the foreign observers prefer to rely on anecdotal evidence of their own. Unfortunately, many fall a victim to their unrepresentative sample of observations. Foreign visitors meet a narrow elite, which has an access to dollar remittances and income from tourism; they also use paved roads and forget about peasants living in isolated villages and settlements of forced labour. Their fictitious averages thus overshoot the reality.

With the recent large arrangements with Chávez and China, the money is close, though not from the domestic resources or from what the people would identify as their own achievement.

The economic deadlock to be broken is three-pronged:

a/ How will the government resign from its cupidity and need for more income under its control and propose incentive schemes for more income sharing with the households?

b/ How will the country attract more foreign inflows of finance to kick-start the Cuban economy?

c/ How to resurrect the domestic production for domestic usage and make the indigenous enterprises more efficient?

As it is easy to see, each of these measures poses a threat to the bureaucratic power of the uncompromising partisan apparatchiks symbolised by Fidel Castro. However, not to all bureaucrats, as the experience from post-communist countries reveals.

THE POLICIES AND THE POLITICS IN PERÍODO ESPECIAL

The 16 years of Cuban economic transition is a series of paradoxes in a completely unique social experiment, which combines the tradition of collectivism and feudal labour with an aggressive capitalist globalisation. Present Cuba is definitely not a mysterious closed state like that of North Korea, but the fruits of high economic and cultural openness are hardly accessible to an ordinary citizen. It is ever more surprising how easily brothers Castro withstood not only the enormous US political pressure but also the unending continuation of economic catastrophes (Hernández-Catá, 2001). Many even believe that, at the end, also their succession might be as smooth as it happened in North Korea.

The exclusive state central command over the economy, as it existed prior to 1990, was significantly decentralised. Nevertheless, it still remained incompatible with an efficient usage of market mechanisms of management, such as the dependence on free prices, profits or wages according to productivity. In agriculture 75% of former state enterprises were transformed into cooperatives and it is quite common to use land leases to individual farmers. However, at the same time the decision-making about crops, acreage sown and prices remained with the State and its communist hierarchies. The land can be neither relinquished nor sold, the access to municipal markets with unregulated (i.e. freely produced) crops is allowed to a small number of privileged farmers and the number of licences to private (family constrained) entrepreneurship is less than 200 thousand and falling. The role of the real free private sector (which should exclude cooperatives or forced private farming) in the Cuban national economy is similarly marginal as it was in the post-Stalinist Soviet Union or Czechoslovakia before 1989, when its share on GDP in the latter was mere 1.6%. In the last two years the government has been withholding the licences for private businesses and prosecuted the attempts at independent (shadow) business activities.

After the collapse of COMECON treaty in 1990, the Cuban government sought for its chances in exporting sugar. The revival of this traditional production failed in spite of the engagement of army. Exports of nearly 4 million tonnes at the price of 150 EUR per tonne made Cuba still an important producer in 2003 (Oxfam, 2004). Nevertheless, the pressure of more efficient Brazil (11 million tonnes) drove Cuba out of markets. The world prices of sugar, artificially low due to the tariff and intervention policies of the European Commission, hardly cover the costs of Cuban production¹². Therefore the output of sugar is sharply falling. The production in 2004 was mere 2.5 million tonnes and agriculture is switching to tobacco.

¹² According to Oxfam (2004), and RBU (2004), the world price of sugar was influenced by the EU tariff of 419 EUR per tonne and export subsidies of 525 EUR per tonne in 2003-04. The EU exports of its high-

The unexpected change occurred after the 9-11 terrorist attacks on the US when the prices of all kinds of non-agricultural natural resources began to soar. The Cuban chances in visible exports are envisaged now to be in nickel and in the extraction of oil at the shelf of Mexico Bay. Both are strategic products dependent on international business networks, requiring new investors, loans of foreign capital, imports of technologies and an oligopolistic alignment. Castros decided to rely on China in the case of nickel and on China, Venezuela and Canada in oil. The EU investments were generally cut short in the deals for strategic stakes. EU's past dominance in the Cuban external economic contacts, when the EU-15 was holding 80% of foreign investments and 45% of international trade at the end of millennium, is now difficult to sustain.

Notwithstanding the new economic ventures in natural resources, the most perspective economic industry in Cuba is tourism. Working for the tourists is considered the brightest prospect for employment. Unfortunately being selected by authorities to such a privilege is not easy, thus for the vast majority of ordinary Cubans the only alternative for an economic improvement is to work at his/her own. Moonlighting and side-lining are unavoidable, even though they are heavily punished. Here the ideas of Western politicians and ordinary Cubans often sharply diverge about what is the crucial Cuban problem. It is not so much the release of all 75 dissidents jailed in 2003 or the political terror that concerns tens of thousands of other politically persecuted, but it is mainly that of a monstrous bureaucracy, prosecution of the independent initiative in employment, punitive labour like in the times of *encomiendas* some 400 years ago (Landes, 1999) and in the shortage of everything good for living. It is the widest infringement of human rights in the participation of individuals in civil society, economy and social governance.

The economic reforms of „período especial“, if considered from the point of view of labouring citizens, look more akin the methods of Soviet war communism (1919-21) than to the experiments of „goulash socialism“ in Central Europe in 1968-89. The new Cuban economy, though concentrated for 15 years on reforms in farming, has not solved the problem of supplies with basic foodstuffs and still depends on imports. The provisions of non-agricultural products are virtually unavailable for the demand with domestic currency. As we discussed it above, all is arranged in a way that the government captures 85% of the primary distribution of the GDP. Thus the people lose their economic independence and depend on the mercy of the government. The state revenues are used primarily for financing army, police, food rationing and international aid. The second round of priorities concerns the sectors of public (communist) administration, schools, sports and culture. The financing of new investments, transport, housing or healthcare¹³ is a residual. These sectors have been hit by a long-lasting neglect. The regulation of society is all-embracing, coming from the State and communist hierarchies, assisted by taskforces in enterprises and the civic sector, where each street has its watch-dog of CDR (Comité de Defensa de la Revolución).

Thus the domestic agriculture and manufacturing are in shatters and the only sound management comes from abroad. The majority of reforms failed completely and many promising ones were suppressed, as the external resources brought suddenly the required

cost sugar were 5,5 million tonnes, the supply of which pressed the world price under the production costs of the majority of producers.

¹³ It is a paradox how the main propagandistic argument about the aid of 30 thousand Cuban doctors engaged in developing countries (see Pérez Roque, 2006) compares poorly with a penurious chaos in the domestic healthcare, once a pride of revolutionary achievements. The statement claiming that although Cuban communist regime failed in providing private goods, it was successful in providing public goods, is not true for long: the provision of both the private goods and the public goods (perhaps with an exception of basic education) is in the bottom of their potential given by natural and human endowments.

revenues. Only **three reforms** can be assessed as those which achieved success. All of them deal with Cuba's external relations.

The first successful economic reform was the introduction of the US dollar as a parallel currency. The ensuing influx of remittances from 2.6 million Cuban émigrés became an essential injection to the standard of living of ordinary Cubans. Their total domestic earnings of \$ 1.6 billion at CER (including rationing) were thus supplemented by additional \$ 0.8 billion. The agreement between the US and the Cuban governments about an annual quota of 20,000 Cuban emigrants to be accepted by United States, if they come legally, has an unexpected effect, which actually stabilises the Castro's regime (Klepak, 2000). In exchange for getting rid of the radical dissidents, the regime gains new remittance payers who relieve the dissatisfaction of those of their family who remained at home.

Assessing whether the present exchange rate (20-24 pesos per dollar) is compatible with the notion of equilibrium exchange rate is also difficult to figure out. Since 2004 there is a visible trend to de-dollarize the economy for both the households and enterprises (Granma, 2005). In 2005 the revaluation of peso-moneda nacional brought its bid price down to effective 20 pesos per dollar (including the 10% tax). Such measures have adverse effect on the transactions of households, even though not so much on enterprises, which operate with taxes, subsidies and exchange rate rationing.

Peso is technically undervalued if compared with the low domestic consumer prices – of those generally non-existent commodities sold in domestic currency. At the same time the exchange rate is overvalued from the point of view of enterprises and effective consumers. What matters to enterprises are their export revenues vis-à-vis the real domestic production costs. Being competitive internationally in manufacturing and agriculture, when extremely high taxes (paybacks) must be refunded to the Treasury, requires squeezing the wages to 2 pesos per hour (200 grams of bread), which eliminate both the link between income and productivity and the incentives for improvements. Concerning effective consumers, as we explained in footnote 4, the amalgamated ERDI, comprising both the domestic and the "divisa" prices, should be effectively decreased below 5. Then they would reflect higher effective domestic average prices, which would depreciate the exchange rate. Also the preferences of Cubans to exchange their dollars for national currency at that rate is low. Local foreign exchange „market“ is a market subject to too many constraints, which say little about equilibrium pricing of the dollar. Nevertheless, its mere legalisation to households was the most revolutionary measure changing the world outlook of all Cubans.

The second successful reform was the opening up of the country to foreign tourism. In 2005, 2.3 million visitors brought the regime revenue of \$ 2.7 billion. It helped re-vitalise the Cuban sinking economy to such a degree that it actually allowed to postpone other vital reforms. The impact of tourism on the rest of the economy is negative in another aspect: it acts as a sort of “Dutch disease”. Taking part in tourism is so lucrative that any other activity in remaining industries looks like a failure not worth investment.

The opportunities for the EU engagement in tourism were undisputed because neither China nor Venezuela could provide sufficient influx of holidaymakers, once the US locked itself out. Unfortunately, the EU businesses failed to take advantage of their monopolistic position and succumbed to accepting the participation in joint-ventures for building holiday ghettos owned by Cuban enterprises, which were controlled by police and army (e.g. Gaviota, the biggest one of them). Organised mass tourism is therefore a direct financial support of the political repression. That makes the EU contribution to shunting the communist totalitarian system towards the ways of velvet revolutions in Eastern Europe less credible.

The third major reform concerns the lifting of the ban on foreign capital. With the US stepping aside by sticking to embargo, this lucrative investment of nearly \$10 billion (for 1993-2005) used to fall mainly into the hands of Spanish, Canadians, Italians and French.

However, the foreign capital movement has its barriers. The authorities allow for a temporary entry only, limited maximally to 10 years. The property rights can be claimed on the capital invested and not on the real assets. Foreign investor is allowed to enter into a joint-venture, i.e. he/she must have a local partner that owns at least 51% of the deal. Very often the Cuban stake looks to be fictitious because its contribution in kind is assessed in administrative (or ad hoc) prices. It depends on the bargaining skills of the investor what kind of a deal is going to be agreed – what amount of land, labour and building works will have the Cuban partner to provide. Even though the property in Cuba cannot be owned by foreign agents, the returns on invested capital could be very high, especially if the corruption was a part of the game.

Foreign investments are advantageous for both sides:

- Foreign capital has access to local economic and political networks that promise preferential treatment for next contracts, while the US competition has sidelined itself.
- The communists have means for survival and for maintaining the loyalty of army and police that would not be so easy by financing them from the proceeds of sugar, rum, tobacco, coffee and nickel exports.
- The apparatchiks have access to bribes and other incomes, which grant them economic superiority and make them real domestic elite.
- Ordinary Cubans have a chance for random premium to their subsistence wages.

If we sum up the revenues from the mentioned three successful reforms in 2004, we should allow for the receipts from private transfers and remittances (\$ 0.8 billion), various international aid programmes (\$ 0.2), receivables from tourism (\$ 2.7 billion), FDI inflows (around \$ 1 billion) and implicit subsidies on oil imports from Venezuela (\$ 1 billion), which should be compared with the Cuban GDP of approximately \$ 6.8 billion at CER. We can again see that the economic dependence of Cuba on external relationships (even with excluded visible exports) is nearly as important as the whole domestic production for domestic usage.

There is also another aspect present: the originally highly egalitarian society turned suddenly into similar inequalities and class contradictions, which were the cause of revolution in 1958. Such environment is easily hurt by social instability and it is opened to conflicts. F. Castro declared 10 years ago (see Granma, 14 August 1996) that the gap between official and unofficial income had risen for some people more than 100-fold. He has raised the issue again in 2004 and the reforms had to be reversed. Since February 2005 enterprises have to ask authorities for an approval of their expenditure every week and transfers in foreign exchange require the consent of the Central Bank. Since the peak inflow of foreign firms (343 in 2003), the number of foreign entries was falling.

The ensuing Cuban schizophrenia is crucial for understanding what is going on there. The economic and social duality means that on one hand there are achievements of revolution offering a minimal of welfare, while on the other hand there are capitalist ideological enemies, who have the largest capacity for offering development and riches, but who seem to be in a retreat. As a windfall rescue of last resort, there are new allies emerging among former outsiders: the rising stars of Venezuela and China.

THE POSITION OF PARTY NOMENKLATURA AND POLITICS

Every Cuban is able to observe daily via television, radio, films or contacts with tourists what capitalism offers with its 150-times higher personal incomes. The regime lost the popular support that it had before 1990. So how does Cuban communism survive? First, the execution of general Ochoa in 1989, most probably on trumped-up charges, helped Fidel and Raúl to recover the control over army and police. Ochoa was a hero of the Cuban army intervening in Angola and his rising popularity was interpreted as a threat to revolutionary

stalwarts. (We can only speculate how the fall of communism would look like in Cuba, would the pragmatic general be alive.) The executive power of Raúl Castro, the least-charismatic leader imaginable, was thus strengthened before the transition commenced – a chance he did not let to lose.

The position of Cuban army is exceptional. There are not many achievements where Cuba is competitive. It is a superpower in sports; it offers one of the best education among poor developing countries; its performing culture (arts) still retained a high standard; last but not least – Cuban army is supposed to be the most functional organisation in the country. Maybe it is because its staff had to be restructured and decreased from 181 thousand to 105 thousand (Klepak, 2000).

The most ingenious achievement of Raúl Castro was that he – as a chief commander over all armed forces – could also become the chief new reformer and succeed in integrating army and police into the economy. It is this most characteristic feature of the present Cuban economy – the so-called „raúlismo“ (Mora, 2000) – which lifted the army above the communist party. The army is thus able to own or control a large part of agriculture, construction, industries, research, facilities of the tourist business and FDI inflows. The last two mentioned are of crucial importance because they are the main resource of foreign exchange for the government and industrial imports. It is then irrelevant what is the share of the army on state budget (officially 2-3%), when it is its own income which matters. Army is the single most important owner of the Cuban economy (Mora, 2002) and the succession after Fidel is under its control.

The connection between the army (and police) and the tourism can, however, seriously backfire. Even though the majority of visitors move exclusively in the dollarised tourist Potemkin ghettos, to where a non-screened Cuban is banned to enter, still many take advantage of free travels and contacts with ordinary Cubans. The belief in the omnipresent communist ideology is then seriously undermined and the people dream about a change. It is another paradox that the best position in case of a „Cuban sugar revolution“ would be taken by the managerial elite of the army and by that part of the state sector, which is engaged in internationally competitive businesses (e.g. FDI dealings, tourism, art and construction). This message should be stressed and passed to them.

Political power has now an access to foreign exchange from foreign investments, tourism, aid transfers and external implicit subsidies, in addition to the mentioned 85% of the GDP revenues. CIA estimates that Raúl Castro can call to arms 1.9 million men and the same number of female soldiers. Although only a fraction of them could be effective in the combat, the army is one of the rare Cuban resorts where economic transition was not ruinous. If indoctrinated by nationalistic sentiments and/or by the fear of alleged US terror, the Cuban army can be one of the biggest obstacles to democracy.

Since 1959 Cuban present regime has depended crucially on foreign aid and external economic relations, the importance of which still dominates. It has accumulated high debts, even though the relationship with creditors was more political than economic. External debt in 2004 was \$ 13 billion in convertible currency – a very high level relative to the effective GDP, plus there are estimated \$ 15-20 billion outstanding to be paid to former COMECON countries, especially to Russia. Although the reimbursement of those debts is only hypothetical, it gives the Putin Russia a better bargaining position in recovering a part of its former political dominance in the island, once the property rights become a rule of the game.

Paradoxically, the main underpinning of the totalitarian regime comes from making the danger from outside credible. This is a crucial point of departure for understanding the knife-edge situation in the Cuban potential for a change. The EU, Russia or China are not considered threats. But Fidel remains most efficiently helped by the US policies. The decades-prolonged and mounting embargo sealed off the presence of both US capital and US

visitors who cannot present themselves in a more constructive cooperative or humanitarian role. Taken from the point of economics of embargo (see Hufbauer and Schott, 2002, or Seiglie, 1997), the US embargo was nearly irrelevant in practically all Cuban imports, which could be purchased at the price increased by transportation costs in more distant non-embargoing countries. It was very inefficient in the majority of Cuban exports, which had to be diverted from the US market to other markets where they caused a mild price decline. The total loss in terms of trade and transportation costs was present but could not cause a major setback. The only great loss concerned Cuban sugar revenues, where the markets in both the US and the EU were highly regulated and subsidized – but that was not a direct effect of embargo. The US embargo had mainly political and ideological impacts, strengthening the internal political deadlock in both Cuba and the US.

The threat that the United States would seek to restitute property nationalized after 1958 is another politically explosive issue. In 2001 the US refused to negotiate the Cuban bid for indemnifying the nationalised US property. Hypothetically the restitutions can be raised for the majority of sugar industry, 1,2 million acres of land and hypothetically for assets producing 2/3 of GDP in 1958. There is also the property of 2.4 million emigrants, settled mainly in Florida (Grenier and Perez, 2003, p. 12). In the US there are registered restitution claims of 5000 US nationals and 898 companies. The estimates of their value are wide: from \$ 6 to \$ 100 billion. Cuba, precautionally, raised a claim for \$ 60 billion as a compensation for the damages caused by embargo (Eaton, 2005). Keeping this battlefield oriented to past reminiscences open – is a policy that boosts the calls for resisting America on grounds of both economic instability, political sovereignty and national pride. So it serves also as a deterrent undermining the momentum for a domestically-driven change in Cuba. At the same time the US political support of Cuban immigrants makes them look like a Trojan horse that frightens the majority of misinformed ordinary Cubans. “*Cuba sí, yanquis no*” – this hackneyed slogan has not gone surprisingly out of fashion among people.

ECONOMIC AND POLITICAL ALTERNATIVES

In spite of the slow pace and the superficiality of reforms, the position of nomenklatura and party elites is so deeply entangled in the dual (internal and external) economic system that substantial reforms must come sooner or later. Cuban society cannot avoid the convergence to the mainstream of development of civilisation, which is based on private initiative (i.e. capitalism) and democracy. We may suppose that partial reforms could start already under the present communist system, similarly like those in Central and Eastern European countries before and during perestroika. Such logical reforms could include:

- a) Currency: the repeal of the absurd three-level system of prices (i.e. the rationing system, prices in shops for domestic currency and dollar retail prices).
- b) Firms: raising the independence of enterprises in decisions about employment, product structure and the access to profits, foreign exchange and loans.
- c) Small privatisation: widening the access to licences for private ventures from the present strictly regulated minimum to micro-firms outside the family businesses and allowing an easier access to the supply-side on local markets.
- d) Wages: liberalising partially the wage regulation in the private and the cooperative firms.
- e) Ownership: allowing the ownership and the re-sale of land and real estates to domestic and foreign legal persons.

The last mentioned move is actually the first step of every real reform. The liberal laws on ownership would imply a complete U-turn in the expectations of nearly all stakeholders in future political changes. It would be tantamount to the power transfers to the US protégés in Florida. But that would also mean that incumbent Cuban nomenklatura would

lose not only its political power but also its share on earning assets – the greatest incentive for orchestrating the changes from inside. The latter is in sharp conflict with the arrangements in all previous smooth post-communist transitions¹⁴. That would also weaken the position in property transfers of all non-privileged Cuban residents. That makes the US dominated transition domestically unacceptable. The Chinese type of reforms would require much less radical demands on ownership transfers. Even more gradual than it was in the majority of Eastern European countries. No wonder why its attraction to Raúl Castro was long recognized. Fidel was silent for quite long (Lawrence, 2005), until he declared in February 2005 at an international economic conference that “the new engine of Cuban economy is going to be China” (Eaton, 2005). Indeed, the Cuban communist party would not risk so much in losing on its dominance, while it could gain over the economic returns. The Chinese type of reforms could start in the above points a) through d). There are only two problems to overcome: the opposition of old communist stalwarts at home and the fundamentalist opposition of the United States. For both the Chinese arrangement sounds like a threat.

It is highly disappointing that Raúl has not made any significant move even in the most gradual among reforms, except for allowing some philosophical non-conformist gestures in the public media. The long-lasting disastrous performance of domestic food supplies, transport, energy and construction cannot be changed by philosophical speculations. The only visible change in the last year is a drop by mere 20% in the number of detained dissidents! There are 69 of them now – a shameful figure but also a red herring for avoiding the debate in other serious issues, such as the economy. The only rational explanation of the stalling reforms is that Raúl Castro, as a heir apparent, did not get free hands in his decision-making and the spirit of Fidel was still dominant. Neither the external constraints were alleviated after Fidel’s retirement.

It is generally accepted that the solitary US embargo has had only a marginal impact on the Cuban economy. However, it was argued that it retained more importance for the outside of Cuba. It was supposed to represent a message of high ideological value to the rest of the world by clearly (and rightly) identifying the regime of brothers Castro as evil and worth punishing. No other government had such a moral integrity in proclaiming it so explicitly. Unfortunately this also backfired: it made the communist propaganda of an “external threat” a credible story locally in Cuba. Some pundits call it a proof by martyrdom (Macek, 2006).

People have always had a weakness for the suffering heroes. If someone (not necessarily a hero, quite probably a crook) has been subjected to years of attacks, distress and grieve, and finally vaults up with a call for a justice to be done – such a person acquires an aura of a saint showing an expiatory sacrifice, which is interpreted as a proof of his/her “truth”. That is why Cuban politics remain until now so unimpeachable in the minds of so many Latin Americans. The “proof” in question is neither logical, nor subject to empirical evidence – its validity is underpinned by endurance and by the weight of hated external pressures. Its contents can be nothing better than some endlessly repeated dogma, completely dissociated from reality. The higher is the external pressure and the longer is the endurance, the better for the argument. The emergence of the recent second US Plan for the Cuban Assistance backed by \$ 80 million serves that ideally.

Since the early 19th century, Cubans have embraced the tradition of patriotism. José Martí and his “*patria o muerte*” remained a symbol until now. Castro discovered that heating the awareness of sacrifice and martyrdom would bring the plummeting rotten regime popular support of the last resort. Therefore any over-reacting in the US (or EU) politics by showing an iron fist can turn to an ideological asset in the eyes of the US (or EU) opponents. But this

¹⁴ The only exception was the transition of Eastern Germany (see the next footnote).

brings a message to the world politics: **the struggle for the abolition of communism should bear no association with an external aggression**. Was it not noticed, or was it already forgotten, that it was exactly this non-violent clash of ideas and seemingly free choice given to the communists that powered the unique success of the “velvet revolutions” across Europe?

This message is often deeply misunderstood. The fall of communism in Europe is often explained as a combination of four factors:

- a) a complete economic collapse in these countries;
- b) their unconditional surrender to the thrust of the US (R. Reagan's) military and economic superiority (see e.g. O'Sullivan (2006));
- c) internal pressure of dissidents as recognized leaders of the dissatisfied public;
- d) desire of the public for free markets and a transformation by “shock therapy”.

Even though each of the 33 post-communist countries in Europe and Asia had a different mixture of their internal and external factors leading to transition, it was conceded recently by Kornai (2005) (and many others) that none of the mentioned four factors was of crucial importance. For the majority they were even insignificant, even though their presence acted definitely as a positive catalyst of transformation. The decisive factors for entering actively into a Great Transformation of the socio-economic system are always internal and forward-looking, not external and backward-looking (Csaba, 2005)).

The crucial factor is seen in resigning of the communist elite to communist fundamentalism and in their expectations for transforming their informal access (quasi-ownership) to capital into a formally legal ownership by using their advantages in human capital and social (relational, networking) capital. The daily contacts with the surrounding western culture and business and the lack of external aggression were the other most important factors. The whole problem was reduced in the initial stage of transition to the access of communist nomenklatura to privatization, entrepreneurship and political processes (Benacek (2001), Winiecki et al. (2004)). The paramount role of indigenous elites in domestic political shake-outs is difficult to dispute. Externally enforced takeovers of countries hardly succeed. All such attempts that avoid the participation of local elites cause an internal pressure for a revision or turn the productive initiatives into redistributive or even destructive.

Elites of all origins (including the communist ones) are more efficient in organising a collective action than any loosely organised public. Their ownership of human capital and social capital in particular cannot be disregarded. Any transition going against them is burdened with economic and political costs and wasted productive potential. The inversed U-shaped relationship between moral purity and its pragmatic expediency seems to end up again in a trade-off, once the initial optimum of "acceptable morality" is reached – like so many times in human history. The whole process of economic and political "tâtonnement" among millions of domestic agents who exploded into disequilibria of reallocations is too complicated to be mastered by external intervention or by relying on naive ethical rules where no one cheats and no one uses destructive strategies. It must be left at local micro-negotiations to settle the inter-human relationships that were fettered and neglected for ages.

According to Kornai (2005), transitions in post-communist Europe were unprecedented in human history and a true success, in spite of many flaws and "disappointments" ¹⁵. They were exceptionally fast in the implementation of reform programmes and led to an accelerating economic efficiency in all EU accession countries (and not only there). Surprisingly, in a sharp contrast to history of Great Transitions, the post-

¹⁵ According to Soros (2006), recent transitions were a result of new conciliatory approaches to world politics among adversaries that commenced with the French-German reconciliation after the World War II, followed by US-Chinese soft politics and the US-Soviet rapprochement. Instead of suppressing infidels by power that harms in the long-run all, the nominally stronger power should offer the weaker one a feeling of security. Then also the weaker party behaves less aggressively.

communist transitions in the majority of 33 countries of Europe and Asia were without any bloodshed. Its societies could adjust to new economic and political rules gradually in a peaceful process. However, even after 17 years it is still visible in all of them that the legacy of former communist bureaucracy was not eliminated, though it was radically modified. Definitely it was not the first best. The large corruption caused by this factor was counter-effective. Nevertheless, we cannot deny that betting on such second best was also the cause behind an exceptionally non-violent inception and (at the end, when the property acquired by insider trading was finally re-sold in a Coasian bargaining) a relatively low-cost implementation ¹⁶. Among the most controversial changes was the rise of new grand entrepreneurs in post-communist countries, who form the core of capitalism (Benacek, 2006 and 2007). Its evolution was full of ups and downs, bringing at the end quite efficient new economies – in many aspects the most dynamic and highly competitive ones in Europe.

Why Cuban transition should be so different and avoid the well-tested path of non-confrontational falls of regimes followed by politics of national reconciliation? Why should it be subject to the four misconceived factors mentioned above and turned into being violent? Why should there repeat the tragic aftermath of the political take-over in Chile by Pinochet? Is it for the vanity of their conceptualists? It would be good to repeat Adam Smith's path breaking idea that butcher is not selling meat for his altruism, but by following his selfish interests. Cuban political elite after the demise of Fidel Castro is as ready for the opportunistic capitalist transition as were other rotten communist regimes in Central or Eastern Europe. The process should be internal and peaceful, i.e. it should offer a chance for the nomenklatura to take part in transition. However, it cannot proceed without an external cooperation and cultural contact, acting as catalysts.

The fall of communism was an unparalleled break in the human history, bearing all signs of Polányi's (1962) "great transformation" (see also Kornai (2005), ch. 1.3). Now we cannot avoid mentioning and ranking of our values, on which this paper is based. The detour to communism was a blind alley in the history – an attempt to go back to pre-capitalist (feudal) social organisation. Capitalism is a human value in itself because it is the only way how to reconcile the rising importance of the division of labour, exchange and its underlying strand of individual initiative and entrepreneurship. The required economic freedom is vitally correlated with property rights, private ownership and intermediation via markets. Its political necessary reflection was found in democracy, i.e. in the markets for political visions. There is no democracy without capitalism. In the past discrimination of the unprivileged ones is alleviated by enforcing human rights. The provision of public goods by means of public administration is linked to electoral selection that allows retaining the hierarchical organisation of the State. The advancement of modern capitalism cannot be separated from the build-up of human capital. The "proof" of these values is possible only by looking at the flow of history. There are many aberrations how the market system, the State and the civil society could be combined, while still retaining the principles of capitalism.

The social system in communist countries has been a challenge to capitalism by offering an alternative vision, which was abandoned by its own masters. Cuba has so far disregarded that strategic lesson and its re-consideration is imminent. The free world should help Cubans mastermind their "velvet" dismantling of communism by themselves. This is the

¹⁶ There were examples of less successful transitions, which did not follow the path of the 8 new EU members. In Eastern Germany the factor of external dominance, the disregard of local pricing of labour and an attempt to eliminate nomenklatura from the social governance administratively, caused an unprecedented wastage of resources (approximately 1200 billion euros of transfers, of which 700 billion went into investments) and the slowest growth among Central European transition countries (see Sinn and Westermann, 2001). The cases of recent transition in Iraq and Afghanistan are other stories to learn from for avoiding their repetition in the Cuban case.

idea of the dissident project Varela. The shakeout should come from the civil society, where even the present apparatchik Cuban elites should feel a chance for survival. Unfortunately Cuba missed its moment in early 1990s. At present the external threat sounds too strong and the military-backed network of restructured party nomenklatura thinks it might lose too much of their growing fortune once the starved Cubans will lose their fear. There is a growing concern among Cubans at home and in emigration that the demise of the Castro brotherhood will result in a civil war. The conflicting policies of the free world, offering too many whips and too little carrots, may even press Cubans into such panicky reaction, once they would feel driven to a tight corner.

When the EU suspended its Cuban sanctions in January 2005, a new debate ignited about their reinstatement because of Cuba's treatment of dissidents. In response, Castro brothers intensified their alignment with China and Venezuela. Such a strong move off the traditional European alignment required a new "proof": so in June 2005 a controversy over the "spying" erupted, ending in expelling the EU activists from Cuba. The EU has kept losing the ground.

Concerning the geopolitical setup in Americas, China seems the best suited global power to build a new strategic alliance with Cuba and fill the vacancy left by Europe. Even though Beijing had first hardly any thoughts about a geopolitical entrenchment in the Latin America, it has been offered a windfall chance recently. China is investing \$ 1 billion (though promised 2 billion) into Cuban nickel and oil extraction and offering trading loans (\$ 400 million in 2005). Tourism, agriculture and local businesses would be even better ventures, once the regime would yield to the younger nomenklatura and liberate the economy by following the Chinese experience. As a long-term strategy, a bridgehead in Cuba represents an excellent bargaining position for China in striking a new arrangement with the US over the rule in Taiwan.

However, Cuba is an ideal bridgehead for another strategic move offered to all trade-intensive countries – to the penetration into the Latin American market of 600 million consumers, which can be easily extended to an economic and political alliance. The chance is offered by the continuing advancement of left-wing populism in the region and the ideological role that Castro's Cuba was able to play there. The miracle of endured economic crisis in Cuba after the fall of communism in early 90s and the political skill of Castro in turning his own failure to being a victim of "an American tyranny" opened wide window of opportunities for renewed export of Cuban ideology to Latin America. Cuba serves as a bandwagon of anti-Americanism and as a final "proof" that traditional Latin American populism is the only appropriate politics for independence, economic self-sustainability and ... (sic!) prosperity. The Cuban misinterpreted example helps support backlash to globalisation and deepening of capitalism, instead of its own fine-tuning within Latin America.

If the leadership in reformed China moulds its image by helping the developing countries in building their prosperity by trade, present Latin America is an ideal place for China to establish its quest for becoming a leader in world politics by commencing with its economic presence just there. As the United States and the EU could not follow the high speed of changes in this huge dynamic region and both have been losing political ground, their trade linkages have also weakened. The survival of "revolutionaries" in Cuba or elsewhere in this subcontinent will be much easier with the backing of China or under the revived centralised Russia. That would be again a flawed choice.

Hugo Chávez of Venezuela became another key vehicle for the survival of Fidel's heirs. With oil at \$ 60 a barrel, Venezuela's daily exports of 2.1 million barrels (out of the output of 2,9 million) brings \$ 45 billion a year. There is another ace of a paramount strategic importance at hand: Venezuela's potential deposits mapped only recently seem to be the second largest in the world – a discovery for which Venezuela should claim more powers in

the board of OPEC. The alignment of anti-American new populist riches with the leftist governments in Mercosur can be, indeed, interpreted in line with Chávez's words at the signing of the treaty as "a victory over the American imperialist politics".

Nevertheless, there were two recent events of major importance, which have revealed that Latin American downslide to populism had its limits. The electoral results in Perú and Mexico confirmed that the opposition to populism is able to mobilise and Latin America is not going to be a single left-wing arena. The democratic sentiments and the belief in free enterprise have not been eliminated. They have been only sharply polarised recently.

Strangely enough, the essential ideological service, which Cuba and Castro's mentoring has provided to populism for long, can turn under some circumstances into its opposite. The Cuban spiritual and personal opposition to communism, i.e. to its disastrous economic and totalitarian policies, is most probably the highest in Latin America. Hardly anywhere in the world the communist governments caused so many damages to human dignity and to the spirit of human rights, like in Cuba. If the Cubans were relieved of their totalitarian burdens and allowed to pursue their entrepreneurial spirit, their sudden sharp development could become a new showcase for an alternative way to the present populism. The containment of the Communist build-up in Latin America is therefore of world-wide strategic importance and Cuba can become again a key and respected leader.

The role of the EU, as the world's leading trading power, is also of strategic importance there. The political clash between the Spanish wing and the Central European wing of alternative policies to Cuba should be reconciled and restructured. Stress should be given to trade and investment opportunities, though still coordinated at the EU level with the politics of human rights and democracy. The inability to divert the Spanish tendency to contain the politics with Cuba and Latin America within the opportunism of its linguistic comparative advantage is a weakness of the EU foreign and trade policies that should be changed.

Spain alone is too weak to bring a strategic advantage in influencing politics in Cuba and in persuading the younger generation of local human and economic elites that Europe offers those more opportunities than China, Russia or Venezuela, including a message that Europe is a natural historical partner that is able to countervail the American dominance. The latter also implies that the EU should be able to coordinate its policies with the US and persuade them that politics of external threat are counter-productive and that the introduction of capitalism by fiat (i.e. not by internal pressure of the social upheaval) can never work. Bringing democracy to Cuba depends crucially on changed attitudes of the United States and their ability to share its dividend with Europe.

An inspiration can be drawn from various Bush-Putin talks. A constructive dialogue about concessions in some parts of the political issues is compatible with a tough sticking to principles. There are more examples to follow. Contrary to the strained relations between the Czechia and Cuba, Czech export figures confirm an accelerated growth in mutual trade that started in 2002. \$ 16.5 million of exports in 2005 was the highest figure in the last 15 years, promising at least a partial return to the days when Czechoslovakia was the second most important exporter and investor in Cuba before 1990. Dilapidating Czechoslovak power stations still provide the majority of Cuban electricity but they need heavy repairs or a delivery of new ones.

Surprisingly, a similar acceleration in trade can be seen in the US exports of food to Cuba – the embargo on which was lifted in 2001. The year 2005 brought the USA record export proceeds of \$ 370 million (contrasted with zero imports). Though this sounds a paradox, it may be a policy rational for the US long-run perspectives both economically and politically. Cuba has been under the US embargo since 1961 and there were several cases of tightening of its grip under the presidency of G. W. Bush. It included an establishment of the

Commission on Assistance to a Free Cuba headed by C. Rice and rising C. McCarry to the post of Cuba Transition Coordinator with a task of „accelerating the demise of Castro's tyranny“ via an annual spending of over \$ 90 million. Though US policies to Cuba are primarily hard-line, there were also passed several concessions vindicated by political rationale. However, the steps of disengagement were always followed paradoxically by measures outweighing their influence. Contrary to them, the world is even more surmising with uncertainty where Cuba will end up politically after the demise of Fidel Castro's rule.

The issue of too many large restitutions (e.g. the restitutions of land) and especially the restitutions favouring foreign outsiders, can virtually freeze the chances for a communist surrender. Nowhere in Central and Eastern Europe the privatization was driven by complete restitutions¹⁷. Also the large sales to foreign owners in the beginning of transition in Hungary or Eastern Germany was considered hostile by the population. The case of US restitution claims on property privatised prior to 1962 should be re-opened and treated as a dividend transferred to Cubans in exchange for their drive to democracy.

The politics of realism and the experience from the former communist countries in Europe call for a different approach. The revoking of embargo and the renewal of the presence of US volunteers, pensioners and businessmen in Cuba will subdue the present paranoia of the Castro brothers, support the expectations of more entrepreneurial Cubans and offer new hope and courage to ordinary citizens, who might otherwise suffer of poverty, humiliation and civil war. The future of 13 million Cubans, and even hundreds of millions of people in the whole of Latin America, depends on the concerted co-acting between Europe and the United States. It was that coordinated mix of sticking to liberal values and practicing economic openness that brought communism to an internally-induced soft crash in Europe. The voices proposing that Cuban communism should be brought to its knees by unyielding orthodoxy and external pressure disregard the causes of the fall of communism in Europe 17 years ago. They underestimate Cuban national sentiments as well.

In choosing among the types of models to be followed by Cuba we could consider:

- Puerto Rico/Batista – obedience under the US trusteeship;
- Haiti – with a weak State governance and social chaos as a result of internal strife;
- Venezuela – with an unhinged populism extending the present totalitarian rule;
- China – with a retained political power of communist party but with economic freedom;
- EU new members – with a minimal intervention of Western powers in politics but very intensive economic cooperation.

Let us leave the judgment on the readers, which model could suit Cuba best.

Open and concerted EU and US trade, investment and aid policies to Cuba are more likely to subvert the local communist system than an embargo. The presence of American, Dutch, Czech or any other businessmen from the free world at the Havana Trade Fair is not a sign of entrepreneurial greed committed to ideological sell-out, but a message to the Cuban nation that there is a better world and that they could become a part of it.

Castro's regime is corrupt, economically super-inefficient at home and generally hated. The people feel desperate and abandoned. They should be made aware, similarly like it happened in Central Europe 20 years ago, that capitalism could bring prosperity and dignity to all. The propaganda of bullying them by the threat of American power and restitutions is counter-productive. The economic incentives are high enough to bring both sides to wide cooperation. Economists at the National Summit on Cuba predicted that trade between the United States and Cuba could generate more than \$50 billion of trade and 900,000 jobs during a two-year period if the embargo was lifted and more reforms undertaken (Fortado, 2006).

¹⁷ Perhaps that exception was the case of Eastern Germany where government-operated Treuhandanstalt transferred a large part of enterprises to owners from West Germany, resulting in a feeling of estrangement and undue external dominance in Eastern Germans.

Such success would be instrumental to many Latin American countries for abandoning the lure of populism and engaging more in trade exchanges with other countries.

The politics of the free world should be therefore more supportive to raising the positive expectations of ordinary Cubans. That could be done, as the first step, if thousands of US and European tourists appeared in the towns and villages – but definitely not in the tourist ghettos, the revenues of which flow to police and army¹⁸. More European and US businessmen should be present there and deal more with the Cuban middle classes. That was the beginning of the communist end in Central Europe. Growing economic external relations, targeted at the ventures that could have impacts on the whole Cuban society, are not a paradox, but a part of the diplomatic game – one that should be more coordinated, not discontinued.

CONCLUDING REMARKS

The search for new strategic orientation towards Cuba, in both the EU and the USA, is of crucial importance because Latin America has entered into its new stage in the clash between populism and capitalist democracy. Politically it seems certain that the US Monroe doctrine is at its weakest standing since inception in 1823. It is not only challenged by sharp political swing to populism, socialism, Marxism, nationalism and the rule of strong presidents, but also by the weakening of an exclusive economic dependence on trade with advanced post-industrial countries.

The weak position of the US in Latin America and in developing countries in general, is an outcome of globalisation and the rise of new centres of economic gravity. The role of other leading developing countries (China, India or Brazil) in the trade and investment flows with the region has dramatically increased, replacing thus the former unwieldy network of the Soviets. By learning from the experience of European (or any other) communist countries, it can be expected that Marxist therapies will fail again in improving the economic stance of countries under its command, while the political grip over them will cause extensive domestic tensions. A backlash turn, calling for the re-establishment of private property rights, entrepreneurship and free markets, is most probable and Cuba may be a potential and highly influential leader of that move.

The role of Europe in bringing Cuba and Latin America back to socio-economic balance is quite unique since the USA has acquired an aura of being culturally a difficult model to adopt by the Latin Americans. In the case of Cuba, USA has also sidelined itself by introducing embargo and sanctions on cultural contacts with Cuban population. The European opportunistic approach to Cuba, symbolised by Spain, which competes with the participation of other countries from the EU-27, is also questionable because it avoids addressing strategic common policies. The cultural and economic foothold that some post-communist countries used to have in Cuba (like that of Czechia) is not used.

The lessons from the post-communist countries about the peaceful dismantling of totalitarian rule together with its communist economics, seem to be most inspiring approach how to deal with the future orientation of Cuba and some other countries in Latin America. The argument about that most unique transition – unique in its systemic depth of reforms, geographical width, speed of implementation and the complexity of internal bargaining – is explained by Kornai (2005) and Benacek (2006). Some implications for Cuba, especially in the policy-orientation, can be found at Mesa-Lago and Perez-Lopez, 2005. The awareness of free trade economics (as a contrast to embargo) and the presence of Europeans as partners at

¹⁸ It should be the duty of Western civil society (e.g. its NGOs) to explain the holidaymakers how immoral it is to support police state and gulags in Cuba by enjoying the vacation in a "different country".

the level of individual citizens of the Cuban society should be in the core of the EU strategic policies.

Perhaps the most important lesson that the recent post-communist transitions gave the world of history as a science was the learning that even the revolutions can be gradual and phased-out into several qualitatively different stages (Kornai, 2005; Benacek, 2007) where the societies, which for long did not have chances for democratic adjustments of their socio-political evolution, could do it in accelerated fashion without sinking into violence or without being threatened from outside. Routes out of socialism are a path-dependent process, as Zukowski, 2005, has so clearly described by attempting to use the Central Europe's experiences as lessons for Cuba. An idea that Cuban society can throw away its legacy of the last 50 (or even more) years and accept a model imported from outside without a process of internal clearing and harmonisation, is dubious and very dangerous.

Last but not least, there is a question of timing. When should there be conceived a coordinated move for refashioning the ineffective rigid policies of Cuban containment, orchestrated by the US and supported implicitly by the impotency of the European Commission, in formulating a common policy of democratic countries aimed at well-trying velvet type of transition in Cuba? The politics of external power produce in the Cuban society counterproductive incentives of retrenchment. When the time for such policies is to come, if not in the present time when the dogmatic grip of charismatic Fidel Castro is evidently bound for phasing out? The time when the Cuban society will have to switch the gear and react to its long-neglected economic, internal inter-generational and other socio-political disequilibria is long mature. It should be the Cuban nation and not the external powers who is supposed to decide about Cuban transition and its natural cultural orientation.

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