Cuba: World Bank Exchange Rate Unification Recommendations

Our Talk Today

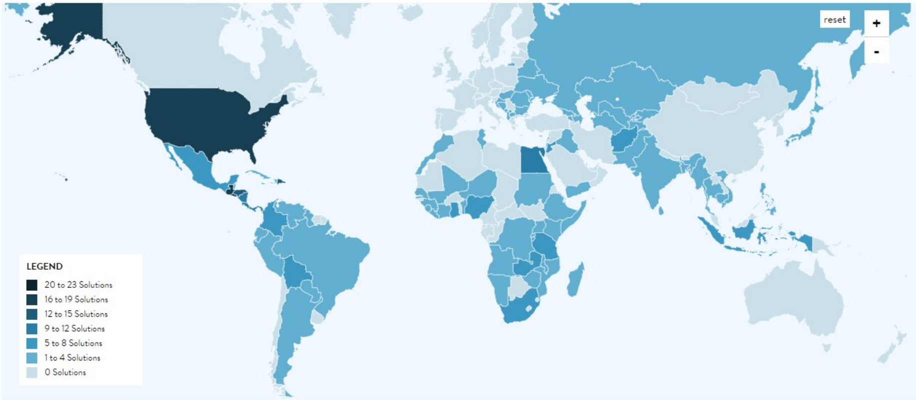
Background on World Bank proposal

World Bank Recommendations

Legal/ administrative Difficulties

Economic Difficulties

Difficulties due to the Outlook



Background on World Bank Role

- The World Bank assigned/ allowed Augusto de la Torre to develop and publish a proposal for exchange rate unification during the years 2010-15
- At the time, Dr. de la Torre was the Chief Economist for Latin America and the Caribbean for the World Bank
- The proposal was presented in numerous venues, including Brookings, Petersen, Bildner, etc.
- The proposal was among the highest profile public opinions issued informally by the IFIs in Cuba.
  - IMF staff had individually published for years on Cuba and in Cuba, including important papers on exchange rate unification, tourism, etc.,
  - There was no public official IMF position beyond tolerating this research
- There were internal presentations at the time to IMF
  - While the World Bank has not presented his work at ASCE, the comm presented here on their proposal were given to them at the time

https://brook.gs/30YaLtf

Legal/ administrative Difficulties

Administrative Difficulties:

- The proposal calls for a firm-specific tax based on prior years' purchases of foreign currency
- This proposal in essence appears to attempt to replace a distortionary system based on two prices with one based on N prices
  - N = the number of firms in Cuba that accessed Central Bank dollars in the prior year
- The proposal is silent on current workers earning in dollars or CUC, focuses on firms
  - If This would increase N to firms plus population
- This is an unwieldy system – Venezuela has a similar quota-based system for accessing multiple exchange rates,
  - Has led to widespread corruption, black markets, etc.

Economic Difficulties

Firm-level Rational Expectations

- This proposal appears to assume firms will pay this tax
- How do we treat a new hotel that did not buy CUCs last year?
  - The straight-forward implementation would tax them at zero
  - The incumbent hotel would be taxed at 96% i.e. 24/25
- The proposal suggests turning to international legal instruments to ensure payment, even in the case of firms exiting the market

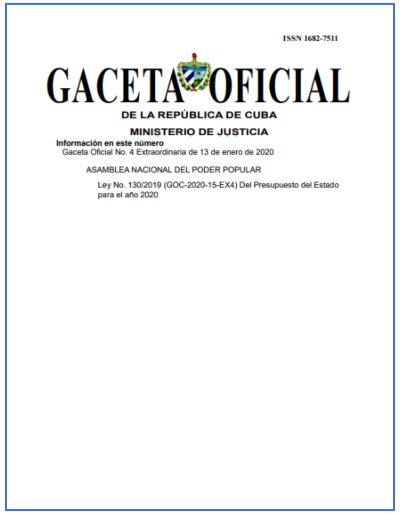
  La manera más sencilla de evitar que el operador incumpla con el pago del impuesto lump-sum sería recurrir a contratos sujetos a jurisdicciones internacionales, lo cual permitiría al gobierno cubano exigir legalmente que los operadores cumplan con sus compromisos ya sea que abandonen Cuba o no

- This appears to insert N firm-level international arbitration processes in motion.
  - DevTech Systems has significant experience in on economic advisory
  - On the basis of this expereince, this is not an advisable path

Difficulties due to the Outlook

The Current Outlook makes it hard to do half-measures

- Deficit is in the range of 8% of GDP
  - This deficit is monetized – that's why they don't unify
- Venezuela has become a major liability
  - Cuba's macroeconomic vulnerabilities to Venezuelan Shocks by Rodolfo Méndez, BBVA Research; José Pineda, UBC Sauder and DevTech Systems, Inc; and Rafael Romeu, DevTech Systems, Inc
  - Venezuela has pulled Cuba growth down since 2015
  - The volatility of "services" is also a drag
- The current global lock-down further aggravates



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GACETA OFICIAL

DE LA REPÚBLICA DE CUBA

MINISTERIO DE JUSTICIA

Información en este número

Gaceta Oficial No. 4 Extraordinaria de 13 de enero de 2020

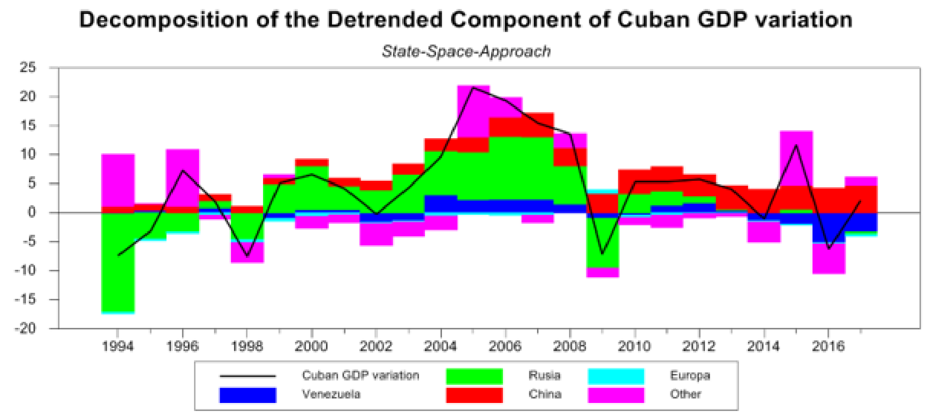
ASAMBLEA NACIONAL DEL PODER POPULAR

Ley No. 130/2019 (GOC-2020-15-EX4) Del Presupuesto del Estado para el año 2020

Artículo 5.1. El Presupuesto del Estado para el año 2020, se planifica con los siguientes resultados que muestra el Estado de Ahorro, Inversión y Financiamiento:

No.	CONCEPTOS	Millones de pesos
1	INGRESOS CORRIENTES NETOS (2+3)	65 390,8
2	Ingresos tributarios netos	49 148,1
3	Ingresos no tributarios netos	16 242,7
4	GASTOS CORRIENTES	67 499,0
5	Gastos de la actividad presupuestada	46 328,1
6	De ellos: Gastos Financieros de la Deuda	1 303,8
7	Gastos de la actividad no presupuestada	21 020,9
8	RESULTADO ECONÓMICO CUENTA CORRIENTE-Desahorro (-) (1-4)	-2 108,2
9	RECURSOS DE CAPITAL	700,0
10	Ingresos de Capital	700,0
11	GASTOS DE CAPITAL	5 686,8
12	Gastos y Transferencias de Capital	5 686,8
13	RESULTADO CUENTA DE CAPITAL (9-11)	-4 986,8
14	TOTAL DE RECURSOS FINANCIEROS NETOS (1+9)	66 090,8
15	TOTAL DE GASTOS (4+11)	73 185,8
16	RESULTADO FINANCIERO DÉFICIT (-) (14-15)	-7 095,0
17	RESULTADO FINANCIERO PRIMARIO (-) (14-15-6)	-5 791,2
	DEMANDA DE FINANCIAMIENTO	
18	FUENTES	11 395,6
19	Incremento de Pasivos (16+24)	11 395,6
20	Incremento de Patrimonio Neto	
21	Disminución de Activos	
22	APLICACIONES	4 300,6
23	Incremento Activos	

Figure 5. Decomposition of Cuba's cyclical GDP variation. State-Space Approach (1994-2017)



Thank you

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