THE HILL

The Folly of Investing in Cuba

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The Cuban government's recent announcement that it intends to permit foreign private investment in the nation is fueling the hopes and dreams of those in the business community whose naivete, avarice or moral agnosticism actually believe that their financial investment in the island economy will turn out to be manageable, profitable and sustainable.

While the embargo on Cuba has prevented Americans from doing business with Cuban nationals and entities for more than 60 years, the Biden administration has recently rolled back Trump-era restrictions and authorized a U.S. license to *finance* and *invest* directly in private small businesses on the island.

Admittedly, there are sectors of the Cuban economy that present attractive possibilities such as tourism, energy, agribusiness and biotechnology. However, American firms must bear in mind that foreign companies from Canada, Europe and Asia enjoy "first mover advantage"—they know the turf, the power brokers, the fixers, the suppliers and networks, the culture, and the invisible rules of the game. They can also count on their governments to step in protect their interests due to the loans provided to Cuba—especially loans from Spain, Britain, Canada, France and Japan.

Before a company decides to invest in a foreign locale, be it a "greenfield investment" (building a factory from scratch), a joint venture, or an acquisition, the firm must meticulously consider a variety of major factors. With *trading* (import-export)—a buyer-seller relationship is relatively easy to terminate, and each party subsequently seeks a new partner. With *investing*, the cost of putting up a brick-and-mortar facility and dissolving the partnership can be lengthy, complicated and costly. (Trading is like dating. Investing is like marriage.)

In the case of Cuba, the economic environment, infrastructure, operations, markets (internal and external), and opportunity cost will determine whether a company should proceed.

The first thing companies look for is the overall *macroeconomic* situation and the environment for doing business. In terms of GDP per capita, over 100 countries in the world fare *better* than Cuba. However, in terms of economic freedom—a more important ranking for investors—the country ranks an abominable 172 out of 184 nations. The categories that comprise the ranking consist of indicators such as property rights, financial freedom, rule of law, labor freedom, and fiscal health.[1]

Prospective investors in Cuba should be aware of the extremely poor state of Cuba's *infrastructure*. This includes transport links, housing, Internet and facilities for expatriate staff. Only 17% of Cuban households have a computer, and Cuba has the lowest mobile phone penetration of any country in Latin America. [2] Water resources and sanitation are also illustrative with 80% of the infrastructure more than 40 years old. Additionally, power outages are not confidence-builders for manufacturing companies eyeing investment in Cuba.[3]

In terms of *business operations,* there are problems galore. Foreign firms present in Cuba can attest to the fact that their operations are challenged by a slew of factors. These include government bureaucracy, the slow pace of decision making, and the inability to hire workers and pay them directly. Cuban law generally requires that foreign investors hire workers via public agencies known as "hiring entities" (*entidades empleadoras*).[4] Low levels of worker productivity and high levels of absenteeism also characterize the Cuban workforce.[5]

As for *markets*, last year Cuba exported $1.15 billion (versus imports of $3.4 billion), the bulk consisting of commodities: tobacco, sugar, and nickel. China, Spain, India, Singapore and Germany were the leading export destinations.[6] In terms of consumer markets, private income (mainly remittances from relatives abroad) is essential to supplement government salaries, as the minimum weekly wage in Cuba is equivalent to a large thin crust pizza from Domino's. Half of Cuban spending goes for food, clothing, shoes and hygiene products. With a lack of brand awareness, restrictions on pricing, promotions, and advertising, consumer goods companies are severely challenged. [7]

Finally, any consideration regarding foreign direct investment in Cuba must consider *opportunity cost*—investing in an authoritarian nation where capitalism is absent versus investing in a democratic nation where a free-market system exists, albeit imperfectly. There are far better choices in the Caribbean Basin region, both Spanish- and English-speaking for tourism; business process outsourcing and IT; light manufacturing; agribusiness; and logistics and transportation services. The Dominican Republic, Costa Rica, Panama, Trinidad and Tobago, and Mexico are the most notable.

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[1] https://www.heritage.org/index/country/cuba
[2] https://freedomhouse.org/country/cuba/freedom-world/2022
[3] https://ejmallen04.medium.com/why-cuba-is-ready-for-an-infrastructure-revolution-3b33fde77aec
[4] https://lupicinio.com/en/hiring-staff-in-cuba-a-guide-for-the-foreign-investor/
[5] https://blogs.bu.edu/espiegel/cuba-a-macroeconomic-analysis/productivity/
[6] https://oec.world/en/profile/country/cub
[7] https://www.bcg.com/publications/2016/globalization-consumer-products-understanding-evolving-cuban-consumer

The 16th century French writer and humanist François Rabelais observed that: “We always long for the forbidden things and desire what is denied us.” The Cuban government’s recent gesture authorizing direct equity investment to entice foreigners is an act of desperation given the island nation’s dire economic situation. Financially astute and socially responsible American corporations will take a pass on this “opportunity” and invest their money elsewhere.

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