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CUBA...FUTURE TRADE AND INVESTMENT PERSPECTIVE



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When President Bush took the oath for the US Presidency this past January, he became the ninth person to do so under the watch of Fidel Castro. Amazing as it all seems-through the Bay of Pigs, a decades long embargo and the dissolution of the Soviet Empire, indeed, from Ike to George W-Castro has prevailed. Few could have imagined such a long tenure.

Since 1992-93, the Cuban regime has made some reforms to deal with the loss of Soviet subsidies. Use of the dollar has been legalized; several categories of work have been authorized for self-employment, (this sector is now 150,000 strong) cooperative farms have been granted more autonomy, including some latitude to sell products outside central-planning dictates, (over 300 farmers, markets have been authorized through December 2000).

The regime has aggressively attempted to woo foreign investors for joint ventures with the Cuban government. All of these changes represent tactical responses to the Cuban regime's need for hard currency; none of these changes represent a fundamental shift in Castro's system. The essence and everyday fact of a repressive, controlling system remain unchanged.

TRENDS IN U.S.-CUBA RELATIONS

As the new president takes office, that relationship is at a crossroad, with U.S. policy open to debate more than at any time since the advent of the Castro regime, due primarily to the ascendancy of opponents of the embargo. The mobilization of the U.S. business and agricultural communities, the emergence of active Vatican interests in the island and new opportunities for the Cuban church to participate in Cuban civil society.

The Rise and Decline of the Embargo

The Cuban Democracy Act of 1992 (CDA) was approved over Bush's initial objections. The CDA established a two-track policy to reach out to the Cuban people while strengthening the economic embargo against the regime. It permits humanitarian donations, including food and medicines, while attempting to increase

economic pressure on the Cuban government by prohibiting U.S. subsidiaries from trading with Cuba and prohibiting any vessel from entering a U.S. port for a period of 180 days if that vessel had handled freight to or from a Cuban port.

As part of its new effort to overturn sanctions policy, elements of the U.S. corporate community established USA*Engage in 1997, largely in response to Helms-Burton and ILSA. USA*Engage, followed by the active emergence of the U.S. Chamber of Commerce in lobbying against sanctions.

Although removing U.S. sanctions against Iran, Libya, and Iraq remained the ultimate goal-as these nations have oil revenues-that goal also meant taking on the domestic lobby interested in strong U.S. support for Israel. Cuba was an easier first target. Third, corporate America learned that Cuba gave them greater resonance with the U.S. media. Initiatives on Cuba brought wider media coverage than did the general cry of "sanctions reform" or an effort to reverse existing sanctions on a Middle Eastern state.

NEW DYNAMICS

The pope's call for change hit a nerve in the Cuban exile community. This has contributed to increased numbers of Cuban Americans willing to voice opposition to the U.S. embargo. Although a majority of Cuban Americans remain strongly anti-Castro and pro-embargo, there is a growing segment of that community that wants to reconnect with the island.

For years, Cuban Americans celebrated exile, refusing to return except on the heels of an invasion or Castro's death. A change is occurring, however, among a younger generation of Cuban exile activists. Many younger Cubans in exile are returning to Cuba to visit and find their family roots, if not actually renew family ties broken by the revolution.

The sustenance comes with the remittances regularly sent to relatives on the island. Some estimates place the amount as high as \$800 million annually, making them one of the island's largest-if not the largest-sources of foreign currency. Although remittances give the recipient some autonomy from state-rationed goods as part of its search for hard currency, the Cuban government has opened "dollar stores", once reserved only to non-Cubans, to anyone with dollars.

CubaCaribbean Development Co.
INVESTMENT OPPORTUNITIES DATA CENTER



Whereas surveys between 1992 and 1996 showed the public opposed to the normalization of U.S.-Cuban relations and in favor of the embargo, by May 1999, Gallup found support for normalization had risen to 71 percent, with 25 percent opposed. The May poll also recorded a shift in attitudes on the embargo: 51 percent now expressed support for ending the embargo, while 42 percent expressed opposition to such a move. Respondents continued to express strong negative feelings toward Cuba, however.

FUTURE U.S. TRADE WITH CUBA

No one really knows what the consequences the end of the US embargo would have on trade between the United States and Cuba. Certainly, US exporters would have a significant advantage over most other suppliers in competing for Cuba's \$500 million to \$1 billion in food imports, particularly rice, corn and other agricultural commodities as well as specialty foods. This is simply because of the fact most other suppliers are much farther away, with the exception of Mexico, and transportation costs from the United States are lower.

The success of other US products in the Cuban market over time would depend on the circumstances leading up to the end of the embargo. If economic sanctions are lifted while Castro is still in power, it is far from clear that Cuban state companies, which import the vast majority of all goods, would be anxious to give all of their business to US suppliers and risk angering their European and Canadian trading partners.

However, if the embargo is lifted during or after a major transition in Cuba, Cuban officials and companies may have more freedom in making purely economic decisions about where they make purchases. If this is the case, US suppliers would be competing on a level playing field and would succeed or fail based on their ability deliver products at competitive costs. Here again, the short distances between the two countries would lend US companies and advantage.

There have been a number of studies about expected trade between the United States and Cuba. In general, they found that trade would likely start slowly and focus initially on exports of US food, primarily rice, corn and soybeans. Initial sales are usually judged to be about \$150 million to \$300 million per year for the first year or two. These studies assume that the end of the embargo and an influx of US investment would increase demand for consumer goods, as well as in the relatively short term.

Later, US investments in industry, privatization and programs to rebuild the island's infrastructure would create demand for construction equipment, building materials and other bigger ticket items. Cuba's infrastructure is crumbling and new roads, water and sewage systems and housing will have to be built on a large scale. US suppliers of the necessary equipment will be well positioned to take advantage of these opportunities. The speed with which these investments can be made will depend on financing and this is a complicated problem.

The US government and private investors have billions of dollars in outstanding claims against the Cuban government. These claims will not disappear just because Fidel Castro and the communists have left the scene. Until these claims are resolved, Cuba's ability to tap US bank loans will be limited, as

ECONOMY & FUTURE BUSINESS OPPORTUNITIES

Cuba is experiencing accelerated change. Some say that relations with the USA are eminent. This prediction of a soon-to-be opening of a new Caribbean market has created excitement among U.S. and European entrepreneurs who consider the country ripe for trade and investment.

The country's existing inventory of industrial plants along with its sea, air and transportation infrastructure could attract significant foreign interest and become a focal point that enables it to fulfill its economic potential.

Cuba, with about 11 million inhabitants, is larger than Belgium, Holland and Ireland combined, and it is longer than the State of Florida. Its strategic location at the crossroads of the Atlantic Ocean, the Gulf of Mexico and the Caribbean Sea, together with its proximity to the USA, makes it a potential target as a regional transshipment center. It is also a huge potential consumer of everything from ammonia to X-ray equipment.

But any foreign firm must consider both, the condition of Cuba's infrastructure and the best way to enter this pre-emerging market before planning a future investment.

Florida & Cuban-American Partners

It is projected that trade between Florida and Cuba, following normalization of trade relations between the United States and Cuba will surpass \$3.5 billion after the first few years. This rate of trade will make Cuba the second largest trade partner, after Brazil, with Florida. American companies with properties or operations in pre-Castro Cuba or which previously did significant business with Cuba will be poised to take advantage of the re-opening of that market. Numerous businesses have contingency plans for trade with and investment in Cuba utilizing Cuban-Americans as their managers or partners for such ventures.

INFRASTRUCTURE

- **Road and highways.** One of the island's strong points is its transportation system, which is in acceptable conditions. There are more than 21,100 miles of highways. Of these 6,290 miles are paved and 7,391 miles having gravel surface. The road network will require less investment to upgrade than other parts of the infrastructure. There is a relatively new intra-island expressway, but there are only 800 gas stations in the country of which 120 are located in Havana.
- **Railways.** With 9,270 miles of track, Cuba's main railway system presents unique opportunities for cargo transportation. The country maintains one of the Caribbean's two remaining passenger railroads (the other is in Jamaica). The sugar industry, Cuba's largest, uses

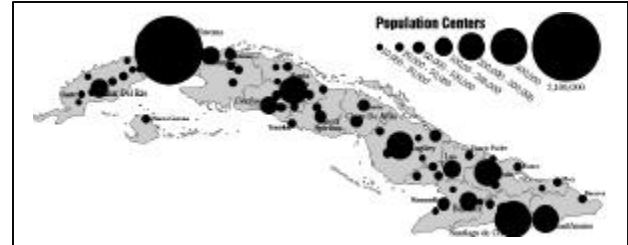


approximately 5,900 miles of track to transport cane from the fields to the mills. The railway equipment needs to be upgraded and modernized.

- **Airports.** There are six international airports. The largest commercial facility, located in Havana, handles more than 700,000 passengers each year and has the capacity to process 1,800 per hour. Perhaps, Cuba's biggest air "wild card" is its nine strategically located military airports, all of which have substantial runways. These could easily be converted to civilian international airports.
- **Ports.** Cuba's coastline sports a total of 70 ports, 31 with cargo operations. Ten of these can be categorized as major ports. The island's seaports are deep, protected harbors with narrow entrances but spacious anchorage. The port system can handle 150,000-ton oil tankers, accept modern roll-on, roll-off vessels, discharge all types of grain and fertilizers in bulk, handle modern 40-foot containers in experimental gantry cranes, and even dock up to six nuclear submarines in state-of-the-art facilities.
- **Telecommunications.** The telephone infrastructure cannot support adequate services by developed-country standards. A penetration rate of 5.3 phones per 100 persons is among the lowest in Latin America. Telecommunications facilities are made up of a mix of obsolete US and former soviet-bloc equipment and modern European systems. Much of the domestic equipment outside of Havana is more than 25 years old and in need of repairs and modernization.
- **Energy.** There are 14 electrical-power plants with a total generating capacity of 3,192 mega-watts. The system consists of pre-1959 US-built plants as well as newer Japanese, French and Soviet-bloc facilities. One-third of its plants are more than 35 years old and in need of constant repair. Spare parts are difficult to obtain at best. There is a partially constructed nuclear-power plant located near the city of Cienfuegos. Once completed it will add another 834 mw to the system. The petroleum and petrochemical industry is one of Cuba's lesser known. There are oil refineries in Havana (two), Santiago de Cuba, Cienfuegos and Cabaiguan with a combined capacity of 13 million tons/year. The country extracts about 1.4 million tons/year and there are at least two major international oil companies drilling on the island.
- **Mining.** The history of mining in Cuba dates back to 1512 when the first mine in the western hemisphere was established by colonists there. Cuba has identified over 200 mining deposits, many of which have not been exploited due to the lack of capital and know how, but include: Copper, Lead, Zinc, Manganese and a number of other minerals, including 27% of the world's reserve of Nickel and Cobalt. There are 53 active mining operations in the country extracting and processing such diverse products as nickel oxides, nickel sulfur, cobalt concentrates, diverse copper concentrates, gold chromite, and others.
- **Construction.** Perhaps one of the most obvious future investment opportunities in Cuba will be in the area of construction of new homes, apartments and office buildings. Other new developments can be expected in hotels, tourist resorts and commercial construction. The island is well poised to deal with this issue. There are six cement plants with a combined capacity of 5.3 million Mt/year, as well as, 22 facilities to produce prefabricated homes and 11 brick plants scattered throughout the country.
- **Industrial Facilities.** Cuba's industrial plants are surprisingly diverse in capabilities, quality and products produced. There are more than 290 large factories with more than 500 employees manufacturing products as varied as cranes, engines, steel containers, elevators, railway cars and complete sugar mills. Recent economic problems and the loss of the former –Soviet-bloc markets have kept most of them from operating at full capacity.

- **Agriculture.** Of course, Cuba is best known for its agricultural industry. There are 156 sugar mills and eight white-sugar refineries with installed capacity of 8.5 million tons/year of raw sugar. The country also produces citrus products, tobacco, coffee, bananas, potatoes, rice, winter vegetables, tropical fruits and other crops.

Population Centers



Financing Considerations

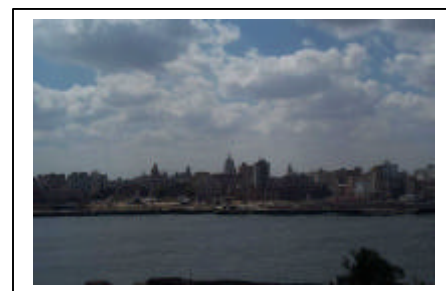
Cuba is a bankrupt country with defaulted foreign loans and no positive trading position to justify credit. The extent to which the needs of the Cuban infrastructure and the pent-up demands of its citizens will be met within a reasonable time after Cuba becomes free will be a function of the availability of financing. In some measure donations and gifts from the exile community located mainly in Miami will satisfy the demand existing within Cuba for consumer products, in part. Cuba's banking infrastructure will also need to be reestablished.

United States firms can be expected to replace a significant part of the trade previously handled by their offshore subsidiaries, which totaled over \$2.7 billion during the past decade. Prior to the enactment of the Cuban Democracy Act of 1992, this trade was estimated at something under \$1 billion on an annual basis.

PERMITTED COMMERCIAL ACTIVITIES & LAWS

American businesses need special licenses for commercial activity in Cuba. By and large, purely American-owned business activity in Cuba doesn't go beyond trade shows, exhibitions, and a range of allowable projects to identify and explore investment opportunities in agriculture, medical supplies, telecommunications, and other fields defined by the U.S. Treasury Department. The department has a Web site, www.treas.gov/ofac, which provides a detailed overview of the regulations under the embargo.

Port of Havana & City



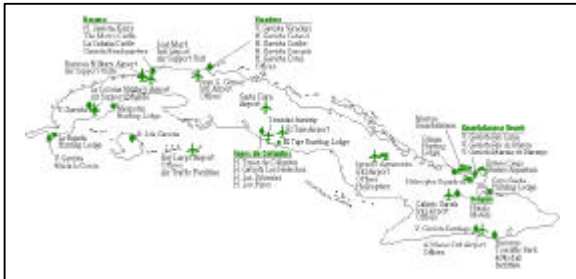


WARNING SIGNALS FOR 2001

Warning signals that the embargo's days are numbered can be found in recent congressional votes to permit food and agricultural sales and to limit the enforcement of the travel restrictions.

The House voted to lift sanctions on food and medicine sales by a 301-116 vote. This was followed by a 232-186 vote to restrict the enforcement of the travel ban. The Senate has been as active in turning against the embargo. A year earlier, the Senate accepted language ending the use of food and agriculture sanctions except in the case of nations deemed by the State Department to be "terrorist" states. The confirmation of the Senate's shift against the Cuba embargo can be found in late July 2000 with a 79-13 vote to lift the embargo on food and medicine.

Tourism & Airports



POLITICAL REALITY OF 2001

The political reality of the year 2001 is that any mayor shift in U.S.-Cuba relations must wait until the following realities run their course.

- The re-election of Florida's U.S. Senator, Bob Graham.
- The re-election of the President's brother, Florida's Governor, Jeb Bush.
- U.S. Senator Jesse Helms remains Chairman of the Senate Foreign Relations Committee for two more years.
- The President may be obligated to "pay back" votes by the Cuban-American community from Miami.
- The Republican House and Senate majority wants to show loyalty to the new President.

POSSIBLE U.S. GOVERNMENT ACTION

The new administration could implement a series of steps to establish a basis for future progressive change and a new policy toward Cuba. These could include:

- Clear Pro-Active statements to indicate its support of strengthening Cuba's civil society.
- Articulate a clear and strong policy to foreign governments.
- Strategical offers of changes in our policy for initiatives by the Cubans.
- Aggressive funding of NGOs, universities and other programs to promote people-to-people contact and the strengthening of civil society.

Havana's Relative New Taxi



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