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BabunGroup Consulting, Inc.

## CUBA CHANGE NEWS ALERT

*EXCLUSIVE NEWS OF POTENTIAL INTEREST TO OUR CLIENTS & FRIENDS*

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### **Superstition, Denial...and Fidel Castro**

Last month U.S. officials said that the image of an increasingly revitalized Castro is impeding or holding back the island's day-to-day leadership from making major changes or embarking on any reforms. We would add that it is also making the current leaders make terrible and often embarrassing decisions.

#### **The damage that is occurring**

A revitalized Castro (or even the "appearance" of a revitalized Castro) is hurting progress. For example:

- **In January**, Cuba announced the formation of an academic commission to study problems with Cuba's system of socialist property. But in early April, following an announcement of a recovering Castro, the Cuban media announced that the much lauded academic commission would issue their report within the next three years.
- **In January**, the Cuban media reported that the number of tourists visiting Cuba dropped 3.6 percent in 2006. Cuba's tourism industry, the island's main economic engine for the past 15 years, is in a steep decline because of a range of factors including: increasing airfare rates, devaluation of the dollar, and crumbling tourist facilities. And we may add, the uncertainty created by the Cuban government having mobilized more than 200,000 militias and soldiers following the announcement of Castro's first operation, **showing the likelihood of civil unrest if Castro dies**.
- **In late February**, Cuba and Venezuela signed agreements for installation of 11 ethanol plants **in Venezuela, by far the largest Cuban foreign construction contract ever**. But in April, an article credited to Fidel Castro, which was published in the official Cuban media criticizes a U.S.-Brazil ethanol agreement. He called the deal a "cartel which would monopolize arable lands and starve the poor". The article was later followed by an announcement that the Cuba-Venezuela ethanol agreement had been terminated.

There is no basis for politically motivated scare tactics that ethanol would take away food from mouths of the world's poor. On April 18<sup>th</sup> in a rebuff against a similar statement on Ethanol production by Venezuela's president Hugo Chavez, President Lula da Silva of Brazil told reporters that "The truth is that biofuel is a way out for the poor countries of the world, the problem of food in the world now is not lack of production of food. It's a

lack of income for people to buy food." These types of differences aired in public by "friends of the regime", are proving to be quite embarrassing to Cuba (**but not to Castro**).

### **Latest regarding Fidel Castro's Illness**

On March 16<sup>th</sup> Ricardo Alarcon said Mr. Castro was focusing on recovery from surgery and would be fit to do his job. "To hear National Assembly President Ricardo Alarcón tell it, Castro is in fact preparing for a comeback" wrote Frances Roble of The Miami Herald.

Fidel's closest aides Felipe Perez Roque and Vice President Carlos Lage, stated that during the past few months, Fidel Castro has remained informed concerning the "principal problems of the country", and he has been "consulted on those issues".

More recently, on April 22<sup>nd</sup>, new photos published of Fidel Castro show him looking fit and meeting with senior Chinese Officials. However, Fidel failed to make an expected appearance at the important May 1<sup>st</sup> celebrations.



### **Our Perspective**

We are not medical experts. But the "positive" prognostics regarding the health of Fidel Castro seem to lack logic.

In any other political universe, if an 80 year old head of state had a major surgical operation and remained convalescing nine months later in a hospital, this would demand great attention in regards to the orderly transition of the government. After all, logical thinking suggests that the patient's health remains precarious.

So what is so different about Cuba or Fidel? Are we dealing here with an extraordinary human being, who somehow doesn't follow the same rules that affect all other humans?

This is the same individual who prior to July of last year was showing signs of: multiple ailments, including loss of memory, fainting spells, and uncontrollable shaking of the hands. Last week a senior American intelligence official confirmed in a meeting with reporters that Castro indeed suffers from Parkinson's disease, diverticulitis, and perhaps

Crohn's disease, a debilitating inflammation of the digestive tract. And reports are that he was fitted with an artificial anus during the first operation in July.

Every month that goes by demands a greater sense of urgency for preparation of the inevitable permanent absence of the convalescing patient.

**And...let's not forget the Cuban idiosyncrasies regarding superstition and denial of issues regarding death**

In any culture, death is a difficult and sad subject to deal with, particularly within a family. For Cubans, death of their 48-year leader will be especially hard. But in the Cuban culture the issue of death has very bizarre cultural idiosyncrasies and is often treated with superstition.

For example, for centuries Cubans have believed that "talking about death (when referring to a sick person) is in itself calling or wishing death". Those closest to the sick or convalescing person are often in "the lookout" for those who are making plans after the person's death. Even such things as estate planning or writing a will are suspect unless it is instigated by the principal. Therefore talking in "positive" terms about Castro's prospects for recovery may not only be political but also culturally correct.

To most of us, this way of acting defies logic. But in reality, it is not much different from the recent news that thousands of people in Kashmir saw the image of Saddam Hussein on the moon, or that in India many saw the name of a political leader in the veins of a Himalayan tree.

**US-Cuba Issues**

As anticipated by our company (see our 1/26/07 News Alert), Cuba has recently returned to the U.S. a convicted criminal who fled to avoid prison for crimes committed in the mid 60's, and released seven dissidents from jail.

Bills on travel restrictions and the embargo are soon to be debated in the US Congress. US lawmakers want to stop Cuba from drilling for oil in waters close to Florida, while Cuba indicates openness to American companies that want to join the communist country's new oil-drilling ventures.

**In Other News**

We are attaching a copy of a related story published in USA Today on May 3<sup>rd</sup>.

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*BabunGroup Consulting, Inc. is regarded as one of America's largest providers of strategic services related to Cuba. Since 1991, BGC has been engaged by a number of companies who are planning to expand or who for competitive or strategic reasons need to know more about future opportunities in a post-transition Cuba.*

## Fund's value rises when Castro ails

By John Waggoner, USA TODAY

Some stocks — and the mutual funds that own them — rise and fall in response to earnings or new-product announcements. Then there's the Herzfeld Caribbean Basin fund (ticker: [CUBA](#)). It tends to gain and drop according to the health of Cuban leader Fidel Castro.

On Tuesday, when Castro failed to make an appearance at May Day celebrations in Havana, the Herzfeld fund soared 11.8%. This closed-end fund, which trades on the Nasdaq exchange just as stocks do, invests in stocks that stand to gain once the USA lifts its trade embargo against Cuba.

The fund's share price has been tightly correlated with Castro's health for the past year, rising when news reports have indicated that the Cuban leader is gravely ill and falling when there are signs of his recovery. Castro temporarily stepped down as president on July 31 after emergency surgery, naming his brother, Raul, as acting president. The fund's share price leaped 12.8% the next day.

Castro met with President Hugo Chávez of Venezuela on Jan. 30. From that point until early this week, the fund plunged 21% on speculation that Castro had recovered.

Thomas Herzfeld, the fund's manager, started the fund in 1994, figuring that the U.S. trade embargo, which began in February 1962, would eventually end. "The vast majority of stocks we invest in should do well when trade resumes with Cuba," he says.

One example: Trailer Bridge ([TRBR](#)), which puts trucks on ships and delivers them from Florida to Puerto Rico. The company has shallow-draft vessels, which would work well in Cuba. Cuba has only three deep-water ports, Herzfeld says.

Another example: Florida East Coast Industries ([FLA](#)), a railroad company whose rail lines could enjoy substantially improved business if the Cuban trade embargo ended.

Of course, there are no guarantees that the U.S. trade embargo will end with Castro's death. His brother, Raul, the effective leader of the country, has made few changes. But some Cuba experts think Raul Castro would encourage a more open trade policy once Fidel Castro dies. Despite his illness, Fidel Castro's presence is still being felt, says Brian Latell, former Latin America analyst for the CIA and author of *After Fidel*.

"Raul is anxious to make substantial changes to the management of the Cuban economy but feels constrained to do that as long as Fidel is alive and aware," Latell says.

The USA will be looking for progress in several areas before it ends the embargo, Herzfeld says, including a restoration of human rights and, possibly, compensation to U.S. citizens for property seized by the Cuban government. "No one single event could more lead to the end of the embargo than the passing of Fidel Castro," Herzfeld says.

The Herzfeld Caribbean Basin fund has gained a sizzling 158% in the past three years, vs. 34% for the Standard & Poor's 500-stock index. But before you place any bets on Castro's death, be aware: This fund isn't cheap.

Closed-end funds issue a set number of shares. And their market price often doesn't reflect the current value of their portfolio. For example, the Herzfeld Caribbean fund's share price is now 26.2% higher than the value of the stocks it owns. In other words, it sells at a premium to its holdings. If the fund were to sell all its holdings and distribute them to shareholders, the shareholders would receive far less money per share than the current share price would indicate.

Most experts, including Herzfeld himself, advocate buying closed-end funds when their market value is less than the value of the securities they own, a situation that's called a discount. For example, the Mexico fund ([MXF](#)), which Herzfeld's fund owns, sells for a 13.6% discount to the value of its holdings. If that fund were to liquidate today, shareholders would receive an immediate profit.

The Herzfeld Caribbean Basin fund, with the ticker symbol CUBA, soared on news that Fidel Castro could not make it to May Day ceremonies.

### A CASTRO PLAY?

How the Herzfeld Caribbean Fund ([CUBA](#)) has reacted to news of Fidel Castro's health during the past 12 months:



#### Key dates and events:

- July 31, 2006:** Castro delegates duties to his brother Raul Castro.
- Dec. 2:** Misses 50th anniversary of Granma boat landing and events marking beginning of the Cuban revolution.
- Dec. 17:** Cuba says Castro will return to duties.
- Dec. 26:** Surgeon says Castro doesn't have cancer.
- Jan. 16, 2007:** Spanish newspapers say Castro is in "very grave" condition.
- Jan. 30:** Photos show Castro meeting with Venezuelan President Hugo Chávez.
- Feb. 27:** Castro reported improving.
- May 1:** Misses May Day parade.

Source: Yahoo Finance