



BabunGroup Consulting, Inc

# CUBA CHANGE NEWS ALERT

## Economy in Shambles Forces Cuba to Tweak Socialism

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

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### Our Analysis

Cuba's economy has been spiraling downward since last year when three damaging hurricanes raked the country, followed by the onset of the global financial crisis. Earlier this year, the Cuban government announced that 2009 economic growth projections had dropped from 2.5 percent to 1.7 percent. This year the Cuban government has faced the impact of the global crisis by introducing foreign exchange restrictions, accumulating debt service arrears, lowering government subsidies by reducing its commodity distribution program, and by rationing energy. Last year, when the rest of the world reeled from the global financial meltdown, Cuba was hit with three hurricanes that cost them over \$10 billion. While the price of Nickel prices (which accounts for 57 % of total exports) dropped substantially.

Business between Cuba and four of its top five trading partners has declined sharply this year in a reflection of a deep economic crisis facing the Island. Other trade reports show that China's imports from Cuba are down 48 percent, Spain, and Canada report double-digit trade decline, and U.S. food sales to the island is also down. Even telephone calls to Cuba from the U.S. are down, and as of November 2009, the energy situation they face is so critical, that if they don't adopt extreme measures they will have to revert to planned blackouts affecting the population.

Exports are about US\$3.6 billion, which is slightly less than the previous year, while imports last year reached US\$14.2

billion due in large part to the increase in oil and food prices, according to the National Statistics Office. As a result of the combination of rising prices for its imports and declining value of its exports, cash reserves have been depleted to the point that the government froze the local accounts of hundreds of foreign businesses and stopped or slowed payments to many foreign creditors. In short, the Cuban Economy is an absolute mess.

Now the government announced the probable elimination of rationing and the subsidized lunches in work centers to save hard currency and resources. The reduction of rationing is likely to disproportionately affect lower income households, particularly those that do not have (or have limited) access to supplemental sources of income such as remittances, hard currency earnings or private sector activities. And subsidized meals provide a supplementary source for food for the majority of Cuban workers.

The Challenge for Castro is to implement the changes without causing problems in a population where complaints about economic circumstances are common. Raul is playing a risky game by cutting back on long-standing social safety nets without offering new economic alternatives.

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BabunGroup Consulting, Inc.**



## Business Climate

Investors in Cuba represent about 40 countries operating in 32 sectors of the economy, mostly from Spain, Canada, and Italy. European capital, mostly from Spain and France sustains foreign direct investment. Of 185 foreign-financed joint ventures with the Cuban government, two-thirds originate in Europe, but the number of mixed enterprises has declined from a peak of 400 in 2002 to less than 250 in 2007, and many foreign suppliers and investors are unable to repatriate hundreds of millions of dollars from local accounts almost a year after Cuban authorities blocked them because of the financial crisis.

Tourism, Oil and Gas, Mining, Energy and Telecoms are the main sectors of investment. The largest players are Sherritt International from Canada (nickel, oil, gas and power), Imperial Tobacco from England (cigarettes and cigars), and Telecom Italia in (telecommunications). Cuba is now interested in partnering only with well-known companies in strategic sectors of the economy, and thus has walked away from contracts and agreements that they had with a number of smaller companies who were adventuring in the Cuban market.

China and Venezuela represent two of Cuba's largest trading partners and an important source of foreign investment.

Bilateral trade with China is about \$2.5 Billion; China is sending a growing amount of durable goods to Cuba. Chinese goods have become the primary tools both in the planned revitalization of Cuban transport infrastructure and in the "Energy Revolution" of 2006 to provide electricity to the Cuban population. Additionally, China is providing loans and grants to help improve Cubas Telecom-network and ports. Some large-scale transactions include:

**Locomotives** (Cuba has purchased 100 locomotives from China for US\$130 million)

**Buses** (Cuba has agreed to buy 1,000 Chinese buses)

**Nickel** (China invested US\$500 million in the completion of an unfinished Nickel processing facility)

**Oil** (Contract for joint production in one of Cuba's offshore areas off the northern coast)

**Biotechnology** (Signed agreement to develop two manufacturing plants)

Venezuela is not left far behind. It sends 98,000 barrels of oil every day under preferential conditions, and provide considerable multilateral assistance.

Some of the better known Venezuelan injections include:

**Construction** (Construction of 150 homes in hurricane damaged areas)

**Refinery** (Investment of US \$500 million to restore refinery in Cienfuegos)

**Power** (\$20 US million for various electricity projects)

**Lubricants Plant** (\$47 million for a lubricants and oil plant)

**Liquid Gas Plant** (Construction and joint operation of a liquid gas plant)

And other less known collaborations such as the creation of a commercial shipping venture, assistance to dredge three major ports, and financing of a Venezuela-Cuba optical communications cable, amongst others.

***“Bilateral trade with China is about \$2.5 Billion; China is sending a growing amount of durable goods to Cuba.”***



## U.S.-CUBA TIES

The following article by Domingo Amuchastegui is reprinted from *CubaNews*.

As long-dormant talks resume between the United States and Cuba, keep one thing in mind: these meetings mean little unless other parties are brought into the picture. If not, there will be no tango to dance. Many matters of substance are not in the hands of the executive branch or the U.S. Postal Service. Congress and the judicial branch play a big role in these talks, while judges in South Florida — strongly linked to Cuban- American voters and lawmakers — have the power to jeopardize these talks in many different ways. And this is already happening.

So if the White House really wants serious and comprehensive negotiations, it must streamline the federal government's political and institutional framework as a whole. That means not beating around the bushes with minor issues at the top of its agenda, while the real beef — matters of substance — remain off the agenda, seriously jeopardizing even the minor issues.

It took almost nine months to legally clarify President Obama's simple announcement relaxing rules on Cuban-American travel and remittances to Cuba. Now the administration is negotiating direct mail service, but how long will it take? Will it be viable?

Will Cuban authorities and planes have the same guarantees when landing on U.S. territory with their share of the mail? A long chain of questions remains unanswered — and those answers are not exclusively in the hands of U.S. negotiators.

### TERRORIST LIST PRECLUDES EVERYTHING ELSE

The official rhetoric from the White House is that mail, telecommunications and other initiatives mentioned in early 2009 by several key Obama advisers are aimed at helping the "Cuban people." Officials keep on talking about the "Cuban people" but not the Cuban authorities — as if the people would be their interlocutor. But they know perfectly well that their interlocutor is the Cuban government. Any initiative requires negotiations and agreements with Cuban officials, yet according to Washington these authorities represent a regime that supports terrorism.

In accordance with such classification, the United States cannot have normal relations — meaning tourism, direct mail and telecom arrangements — with such a state.

So first things first: remove Cuba from the State Department list of terrorist states (*see article in this issue, page 1*). A host of prestigious retired U.S. generals and admirals and several lawmakers have suggested this repeatedly, but no one is actually listening.

Will the State Department make its policies more constructive path anytime soon? That doesn't seem very likely. It's the same story with Congress and the embargo. Executive orders can bypass some aspects of the embargo — for example regarding allowing U.S. oil companies to drill in Cuban waters — but Obama has implicitly and repeatedly refused to take such an initiative.

The crux of the embargo lies now within the halls of Congress. But after the



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**“...37 votes are still needed to reach the magic number of 218.”**

summits at Port of Spain and San Pedro Sula, various bills aimed at undermining or bypassing different aspects of the embargo remain frozen. There appears to be no initiative in sight — from either the White House or congressional leaders — to bring these bills to a final vote.

Is it because there just aren't enough votes, or because the White House has sent a clear message that it's not interested in the issue? Steve Clemons commented Sept. 14 in his blog, *The Washington Note*, that “by stating that he will not lift the embargo until Cuba undertakes democratic and economic reforms, Obama is perpetuating a fallacy that conditionality produces results in Cuba's domestic internal affairs. That approach has failed for decades — and needs to be dropped.”

Recently, Rep. Sam Farr (D-CA) predicted that by year's end, a Cuba travel bill allowing all U.S. citizens to visit the island may pass a final vote in the House of Representatives.

According to his math, 37 votes are still needed to reach the magic number of 218. Imagine that it's finally approved. The bill then needs to be hammered out with the Senate, and then comes the huge obstacle: U.S. citizens cannot travel to a terrorist state.

#### **TALKS MUST TAKE ON A NEW APPROACH**

Furthermore, the court system could create and multiply obstacles of every sort. It might, for example, validate the confiscation of Cuban assets (planes, boats, etc) to be used against compensation claims or any type of charges against top Cuban leaders.

Negotiations with Cuba must take on a different approach. They must clear away discrepancies between branches and institutions of government by establishing a strong federal “eminent domain” policy to avoid obstacles and tensions. Above all, however, this requires a consistent political will on the part of the Obama administration.

Unfortunately, recent White House actions indicate an opposite approach to the “new beginning” policy espoused during the Port or Spain summit in April.

Earlier this year, the administration ratified Cuba as one of the world's four state sponsors of terrorism. Singer Silvio Rodríguez was denied a U.S. visa to attend Pete Seeger's 90<sup>th</sup> birthday. Obama ratified the embargo, and only a few weeks ago, the State Department denied a visa to Ricardo Alarcón, president of Cuba's National Assembly.



Alarcón, Cuba's top U.S. expert and troubleshooter — with whom informal and Exploratory talks could have been held discreetly — had been invited to Washington by the Congressional Black Caucus.

Noted the Associated Press: “Obama bypassed an opportunity to suggest a willingness for easing U.S.-Cuba animosity.” So true.

## Latest Business Headlines

- **China to Give Cuba \$600 Million in Aid**

China provided its ideological ally Cuba \$600 million in loans and grants Sept. 3 during a three-day visit to strengthen ties by the Asian giant's parliamentary head Wu Bangguo, diplomatic sources said. Wu, the No. 2 man in China's ruling Communist Party, and Cuban parliamentary chief Ricardo Alarcón oversaw the signing of a series of agreements, including for a loan worth \$260 million for the purchase of 10 grain shipments, as well as a \$300 million loan to help improve Cuba's telecom network. A Chinese credit also will be invested in Cuban television; a spokesman of China's diplomatic mission told the news agency AFP, without specifying the amount. In addition, Beijing donated \$9 million, offered an official credit in the same amount, and provided a \$1 million preferential line of credit, all for investment in projects to be determined by Cuba's government.

- **PetroVietnam to Search For Deepwater Oil**

Vietnamese and Russian state oil companies have signed a memorandum of understanding on offshore oil and gas exploration in Cuba, said a PetroVietnam official in Hanoi. PetroVietnam Exploration and Production Corp. and Zarubezhneft agreed to prepare for oil and gas exploration production in a deepwater area offshore Cuba, said the source, who wanted to remain anonymous. Both companies had previously agreed with Cubapetroleo (Cupet) to participate in the exploration of deepwater oil reserves in the Cuban Exclusive Economic Zone in the Gulf of Mexico, off the island's northwest coast.

- **Alimport's Food Bill: \$4.4 Billion Since 2001**

Despite the embargo, Cuba has imported more than \$4.4 billion worth of food and agricultural products from the United States over the past eight years, say government officials. "Since operations were begun in December 2001 to date, Cuba has paid to its U.S. counterpart more than \$4.4 billion," said the online edition of *Opciones*, quoting Pedro Alvarez, the former president of state-run Alimport. Cuba imports 80% of the food its 11.2 million citizens consume, despite the fact that the state has kept more than half of the island's cultivable land idle for decades.

- **Sherritt: Boca Power Plant Ready by 2011**

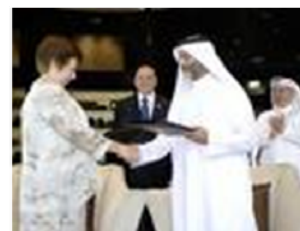
Toronto-based Sherritt International continues to carry out engineering work for a 150-MW expansion at the Boca de Jaruco thermo plant in Cuba, a company executive said in a webcast carried by BusinessNews Americas. Previously, the company said the \$247 million project was due to come online by early 2011. The expansion will increase Sherritt's capacity in Cuba to 526 MW.

- **Repsol Plans Offshore Drilling Next Year**

Spanish oil major Repsol-YPF SA says drilling in Cuba could begin by the end of next year, according to Miguel Martínez, the company's chief operating officer. In Cuba, the company holds rights to an offshore exploration block which covers six areas, plus area 35, which are in Cuba's exclusive economic zone in the Gulf of Mexico. Repsol has a 40% stake in the exploration consortium, while Norway's Norsk Hydro and India's ONGC-Videsh each hold 30%.

- **Thomson to Offer a Havana Port of Call**

British line Thomson Cruises is shaking things up in winter 2010-11 with a series of new 14-night Caribbean itineraries — including Thomson's first-ever calls in Havana, reports *Cruise Critic* website. The cruises will be operated by the new 1,506 passenger, 54,000-ton Thomson Dream, which will join the fleet in April 2010.



*“...Cuba has important more than \$4.4 Billion worth of food and agricultural products from the US...”*





**“Fuel oil rose 10.5% to 1.4 million tons, while diesel jumped 25.3% to 646,000 tons...”**

- **Fuel Oil Production Up, Gas Down In 1st Quarter 2009**

Cuba increased its output of diesel and fuel oil in the first half of 2009, but gasoline production fell dramatically, according to statistics issued in late August by the government. Fuel oil rose 10.5% to 1.4 million tons, while diesel jumped 25.3% to 646,000 tons, the National Statistics Office reported. Gasoline dropped 36.1% to 232,000 tons. Kerosene, liquid gas and lubricant oils also fell significantly, while there was no information provided for jet fuel and other products. There was no official explanation for the mixed performance. Cuban oil refining nearly doubled to 5.46 million tons in 2008 as a new joint refining venture with Venezuela in Cienfuegos completed its first year of operations, producing mainly for export. The 2008 production included 977,000 tons of gasoline, just over 1 million tons of diesel and 2.7 million tons of fuel oil. Jet fuel production totaled 278,000 tons for the year.

- **Miami Firm Says It Will Lay First US-Cuba Fiber (AP)**

A small Miami-based company said the U.S. government has given it permission to lay the first optical communications fiber from the U.S. to Cuba. That could drastically cut the cost of calling the island nation and make the Internet more accessible to Cubans. Treasury Department officials were unavailable to confirm that TeleCuba Communications Inc. has received approval, which is necessary even though the Obama administration eased long-standing restrictions on telecom links to Cuba in April.

- **Venezuela, Cuba to Start Laying Fiver Cable**

Installation of 1,630 kilometers (1,013 miles) of fiber optic cable between Cuba and Venezuela was scheduled to start on October 14, 2009, Venezuela's Science and Technology Minister Jesse Chacon said. "This is something that we hope will be ready in two years' time," Chacon said in a statement. The hookup will have a 640-gigabyte capacity and multiply Cuba's ability to connect by 3,000, experts from both countries say. The project, set to lay cable from near La Guaira in Venezuela's Vargas state to Siboney, outside the Cuban city of Santiago de Cuba, is expected to cost 63.4 million dollars.

- **Philips to Cuba: We Did Nothing Wrong**

Dutch electronics giant Philips dismissed claims by Fidel Castro of "betrayal" and blamed bureaucratic red tape for a delay in delivering medical equipment to Cuba. "Because of the complexity of the application of the rules to the transactions, the company did not obtain all the licenses required" for the delivery of spare parts for medical equipment, Philips said in a statement. "We have disclosed the matter, cooperated fully, accepted the penalties and improved our procedures to prevent similar recurrences."

- **Foreign Suppliers in Cuba Fret Over Payments Crisis**

Many foreign suppliers and investors in Cuba are still unable to repatriate hundreds of millions of dollars from local accounts almost a year after Cuban authorities blocked them because of the financial crisis, foreign diplomats and businessmen said. Delegations from foreign banks and investor funds holding commercial paper from Cuban state banks have repeatedly traveled to Cuba this year seeking answers from the central bank or other authorities -- without success -- sources said. Representatives of some companies with investments or joint ventures on the island said they were bracing for the possibility of not being able to repatriate year-end dividends paid to their accounts in Cuba.



- **Top UAE Official Cuba to Discuss Mariel Port**

Abdullah bin Zayed al-Nahyan, foreign minister of the United Arab Emirates, held talks with Cuban Vice-President Ricardo Cabrisas about possible joint ventures — chief among them a project by Dubai Ports World to build and operate a container terminal at the Port of Mariel, in order to relieve the bottleneck in Havana, 30 miles east. In June, Brazil announced it would grant a \$300 million loan for construction at Mariel. But it wasn't clear whether that would cover Brazilian participation in the project, or be restricted to building and operating an offshore oil logistics center at the port.



- **Cuba Modernizes Ports to Admit Larger Ships**

Cuba is working on the dredging and technological modernization of its three major ports in collaboration with China and Venezuela to meet the challenge that the enlargement of the Panama Canal will bring, official media said. The works seek to increase depth to allow the operation of larger vessels in the ports of Havana, Cienfuegos and Santiago de Cuba, through which more than 80 percent of the island's imports enter the country, the director of the Havana port authority, Miguel Izquierdo, told the weekly *Opciones*. The official said that financing will be provided by an accord approved recently between China and Cuba, and from another with the mixed company Puertos del ALBA (Bolivarian Alliance for the Peoples of Our America), founded to promote the development and modernization of Venezuelan and Cuban port terminals.

- **Cuba Reports 45% Drop in Citrus Output**

A decade-long decline in Cuban citrus and juice production continued through July with the government reporting a steep decline over the same period in 2008, said Reuters. "Citrus, with a production of 234,000 tons, declined 45.3% due to low production of oranges and mainly grapefruit," the National Statistics Office reported on its web page. The grapefruit harvest begins in August and peaks before year's end, with oranges harvested mainly from January through June. Citrus production was 391,800 tons in 2008, down from 469,000 in 2007 and 792,700 in 2003. Local officials blame aging groves, hurricanes and disease and say they're working to replant and thin and spread out orchards.

- **Chinese J-V to Build Hotel at Havana Marina**

China's Suntime International Techno-Economic Cooperation (Group) Co. Ltd., together with Grupo Cubanacán, will build a 600-room hotel at Marina Hemingway in the western suburbs of Havana, reports Reuters. Suntime, with a 49% stake in the venture, will provide \$150 million in financing. Chinese state entity CITIC Construction will build the hotel beginning next month. In 2003, Cubanacán partnered with Suntime to build a 700-room property in Shanghai. That hotel, in the upscale Pudong district, is managed by Spanish hotel operator Sol Meliá.

- **Cuba Reemplaza Locomotoras de EEUU Por Chinas**

Cuba substituirá por maquinaria china unas locomotoras norteamericanas de la época de la II Guerra Mundial que nunca pudo reparar debido a que el embargo estadounidense le impidió comprar los repuestos necesarios. "Próximamente llegarán 60 locomotoras chinas para dar de baja a las americanas" -de las cuales 32 ya no sirven-, dijo a periodistas el viceministro Antonio Puente durante un recorrido por los Talleres José Ramírez Casamayor.

**"China's  
Suntime  
International...  
will build a 600-  
room hotel at  
Marina  
Hemingway..."**



## ***Cuba Geopolitical Outlook*** BabunGroup Consulting, Inc.



On November 4, 2009 Babun Group Consulting, Inc.'s President and CEO, Dr. Teo A. Babun, spoke at the DEC conference on the subject of Western Hemisphere Trade Restrictions and Risk (Focus on Bolivia, Cuba, Haiti, Nicaragua and Venezuela). Other panelists that attended were: Clara David, Chief, TWEA Licensing Section, Office of Foreign Assets Control; Walter Bastian, DAS Western Hemisphere, MAC ; Mathew S. Borman, Deputy Assistant Secretary of Commerce for Export Administration; Jarahn D. Hillsman, Economic Officer, Office of the Coordinator for Cuban Affairs, U.S. Department of State.

The event was held at the U.S. Department of Commerce building in Washington, DC. Over 300 traders, international businesses, and members of the U.S. Congress attended. This event was accentuated by a speech on the importance of International Trade which was given by President Barack Obama.

- **Access to professional Staff:** BGC is known as a business-driven watch group that informs/updates/advises multinationals throughout the world to understand the goings on in Cuba. Our company has substantial expertise in Cuba issues; we often provide independent feasibility analysis and other business consulting and research assignments to multinational corporations. Our company has under contract to two former ministers and over 40 experts on different industries/expertise related to Cuba. **-Contact us for a full brochure.**
- **Customized executive briefings:** BGC conducts informal discussions/briefings on Cuba issues with client's staff. The briefing sessions are general and informal business focused (not academic) presentations and discussions regarding current Cuba and US-Cuba subjects. The number and timing of the sessions is at the discretion of the client. **-Contact us for rates.**
- **Business reports:** BGC is experienced in preparing reports to help provide a preliminary strategic plan and overview of issues related to a possible economic opening of Cuba to allow the client to conduct business operations in the emerging (future) new market. This "Analysis for Strategic Direction" could be drafted as a "Quick-Response Business Plan" in the event that things suddenly change in Cuba and it becomes permissible to do business in the Island. Our first step is to conduct a confidential meeting to help develop a scope of work at no cost to the potential client; following the scope of work we would determine the cost of such assignment. **-Contact us for an appointment.**



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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.*