

Audit on international business opportunities in cuba



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Cuba, with its beaches, colonial architecture, favorable climate and a rich cultural history is located at a point Gulf of Mexico, Atlantic Ocean and the Caribbean Sea. It was discovered by Christopher Columbus in the 15th century and was under the Spanish control until the late 19th century and became independent in 1902. Cuba has been continuously in the media' attention, be it for the strained relationship with the United States, the Guantanamo Bay detention center holding prisoners of war or the Fidel Castro's regime. Cuba is one of the major players in sugar and nickel based industries and there would be very less people who are ignorant of the Cuban Cigars! The word CUBA by itself means " the land of fertile soil". The official language is Spanish while the main religion is Christianity.

POLITICAL BACKGROUND:

Cuba is a totalitarian Communist state and Raul Castro is the head of the state. The principal organ of the state security and control is the Ministry of Interiors. This regime with its bureaucracy and state security control most aspects of the Cuban life. The US has imposed various bans on the Cuban government due to its political policies, which Cuba endured for almost 40 years time. The United Nations keeps trying to soften the embargoed relationships.

Castro led his rebel army in 1959 proving to topple the US-led dictator Batista. The Castro brothers along with Che Guevera, an argentine revolutionary led the infamous Cuban Revolution and succeeded to power in 1959. In 1976, Cuba published the socialist constitution, which proclaimed the adhesion of the country to the Marxist-Leninist ideology and international proletarian's power movement.

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Cuban Communist party is the fundamental source of political power and not ironically it is the only recognized political party in Cuba though there have been other political parties that have legally existed from 1992 but without the right to gather or publicize or field any candidates in the election. There was no legislative branch from 1959 to 1992. Fidel Castro was the first Prime Minister or the President of the Council of Ministers. Fidel Castro wielded the power for almost 5 decades before Raul bore his yoke, in 2008. The government has been struggling for long to stabilize the country, which has been deeply infested with illegal-black market, curtailed private ownership, lack of basic human rights and absolutely very little democracy and not to mention the highly strained relationship with Uncle Sam!

ECONOMIC STRUCTURE:

The Cuban economy has been significantly swaying with lots of ups and downs over the past few decades. The major cause was due to on and off trade embargo imposed by the US. Cuba follows a similar economy pattern of the Soviet Union just as North Korea does. In the period after the revolution, U. S. citizens owned approximately two-thirds of the businesses in Cuba, and almost the entire trading was done with the US. When Castro regime took over the government after the revolution it confiscated the private holdings. Towards the middle of 1962, US imposed the trade embargo and snapped all its trade ties with Cuba. The embargo prevails and is not lifted till date. It is a good sign for Cuban economy that the Obama administration has softened some of the bans. It doesn't mean Cuba is totally dependent on the trade with US, but can have a better market owing to the geographical proximity.

Cuba turned to the Soviet Union for business after the 1962 embargo.

Postponing debt payment schedules, creating new credit lines, paying high prices for Cuban exports, and offering military assistance subsidized the Cuban economy. Due to this attitude of the Soviet, Cuban economy did not suffer much until after the lapse of the Soviet Economy in 1989.

Consequently, Cuba lost almost 85% of its trade. Cuba was forced to recuperate from its failing economy. The 1990s was a period of economic hardship. There was a 35% decrease in the business in the period between 1990-93, causing the nation to fall into what Castro called " The Special Period in a Time of Peace."

The Cuban economy ran into a bleak period with no ration, transportation, electricity, or even food. Then came, the much-awaited respite to this struggle in the form of the tourism, which was the only booming sector in the 1990s, even though it was highly discouraged when Castro first took reins in 1959. Other major contributors to the Cuban economy are agriculture- sugar, coffee, tobacco (the Cuban cigars) and nickel. The Cuban economy suffers every time the sugar prices go down on the global market as it depends mainly on the export of sugar.

Cuba had a huge debt of almost US\$10 billion by the end of the millennium. Though Cuba has tried to refinance this, it failed due to the adverse economic conditions in the late 1990s. Many international loans claimed against plans to import the essentials of the people have been denied due to its poor credit record. But the economy showed some signs of recovery, when Cuba received some foreign aids. Cuba was not approved to claim

money from either the IMF or the World Bank. The money got from the UN pales in comparison to the borrowings of other Latin American countries.

The major changes to economy is by Raul Castro who focused on the decentralization of agriculture, leasing of idle state land, losing the hold in retail sector in order to stabilize the economy and to reduce robbery.

CULTURAL BACKGROUND:

Cuban culture is a blend of Spanish and African cultures. The richness, diversity and the significance of the Cuban culture is due to the fact that it has passed through historic generations.

Cuban culture enjoys a rich heritage in the field of art, music and literature. Music styles of France, Spain and the Americas have a major influence on the Cuban Music. Jazz, Argentinean Tango, Ghanaian high-life, West African afrobeat, Spanish ' Nuevo flamenco' are based on Cuban Music. Cuban music is a symphony of all these forms. Cubans' dancing is also a major cultural advantage - with Ballet and the Salsa having its roots in Cuba. The Cubans are pious with the main sects being Catholics and Santeria. Also, Cuba is a prestigious nation with four of the UNESCO's World Heritage Sites.

BUSINESS CULTURE AND GOVERNMENT ATTITUDE:

Business culture in Cuba is widely rated as one of the worst cultures, owing to the hostile business environment and unfriendly attitude of the Castro regime. This along with

Unskilled employees without motivation,

Shortages in supply,

Having to pay very high utility bills,

Poor customer services,

High degree of theft and pilferage

make Cuba one of the bad areas for international business. The London based Economist Intelligent Unit ranks Cuba at 80, amongst 82 countries in terms of top business environments. Moreover, socialist nations like China, which does business with almost 46 other countries, find it hard to do business in Cuba. The US trade embargo restricts the US businessmen from triggering business in Cuba, and even those who are permitted to do so, like the Food exporters, find it highly unfavorable.

Only 50 Cuban companies were allowed to participate in free trade until 1987. The lack of potential development in business discourages the companies from participating, as the Cuban government is the only customer. The foreign business is more tolerated than embraced even when the country is suffering a financial black hole. The foreign partnerships fell from 400 in 2000 to 236 last year according to the recent statistics in 2008. The government at present is trying to invite foreign business in terms of oil exploration and mining, large and costly projects and the inclination is more towards China, Venezuela and other fellow communist nations.

Cuba's government is expanding its own restaurants and store network thereby rejecting the small European companies willing to invest in retail.

Even if the companies get approval, the control soon transfers to the <https://assignbuster.com/audit-on-international-business-opportunities-in-cuba/>

centralized government and the company holds only a minor control, in spite of a 100% ownership. Staffing at foreign embassies is also through the government-staffing agency and nepotism is very common. Even the staff salary at foreign establishments should be made through the government agencies, leaving the employees with a meager amount while the government pockets the rest in the name of education, health care and welfare programs.

The import supplies are delayed and due to Cuba's credit and foreign exchange shortage there is a long queue. Also, the bureaucracy is slowly forcing some businesses to close down. There is almost a constant need to renew the visas and work permit by foreign workers and the judicial system is not as effective as the stringent policies.

On the other hand such tight government regulations and attitude has a bright side too. The Cuban Tourism Ministry has fixed a minimum room rate to the hotels, which ensures that there is no monopoly and squeezing of one operator by a competitor. Also Cuba is the highly literate and low crime-rate country of the Latin America.

Above all this there is an external pressure due to the embargo imposed by the US. This has forced even some banks to close down their financing operations in Cuba. Cuba is not having excessive storage with itself that it suffers lack of customers. Despite, Cuba spends more on transportation of exports and imports that raises the cost and feasibility of product access. All the drawbacks mentioned above pose a challenge to Cuba in creating a potential market for international business.

(Source: Association for the Study of the Cuban Economy; Sun-Sentinel research, Havana Journal, Feb 2007)

Major Exports:

Export Facts:

53% of Cuba's commodity export market is taken up by sugar and honey, which forms 5.7% of the world's export sales.

Nickel forms the second most export of Cuba, almost 23%

Fish and tobacco are the other major exports accounting for around 6-7% each.

Medicinal and pharmaceutical products are also exported (3%)

Export Figures:

The countries that buy export commodities from Cuba:

Russia 27%

Canada 18%

Spain 8%

Major Imports:

Import Facts:

Imports include petroleum, food, machinery, chemicals and electrical goods.

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Import Figures: The countries that Cuba imports from:

Spain 17%

France 9%

Canada 9%

Cuba and have a trade protocol agreement that in exchange for Cuba's sugar, Russia provides petroleum, while Venezuela supplies oil to get professional medical help from Cuba since the late 2000s. 40% of Cuba's trade is with Americas while 50% is with European countries.

Franchising, licensing and management contracts are the other forms of international business, which is yet to be adopted in Cuba. Being a communist nation, the government holds the centralized power. With tight control and slow bureaucracy, these business models are yet to gain popularity. There is only one Mc Donald's in the whole of Cuba.

THEORIES OF INTERNATIONAL TRADE: CUBA'S CURRENT STATUS:

There are various theories that explain the current position of international trade in a country. The basic reason of why countries need to trade has been explained by the ABSOLUTE ADVANTAGE theory. Adam Smith in 1776 proposed in this theory that countries should shift their available resources to those industries that can produce efficient and specialized products, which in turn can be used to buy other imports. This type of advantage can be either NATURAL or ACQUIRED. Natural advantage means that the resources are available naturally in the form of climate, skilled labor force. This

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determines the type of agricultural products produced. The country enjoys an advantage due to naturally available resources.

NATURE OF ADVANTAGE in the international trade theory is classified in to the following categories and defined by Daniels, Radebaugh and Sullivan as:

Natural advantage by means of climate, soil.

Acquired advantage through the processing of one of the basic factors of land, labour.

Comparative advantage against another nation's endowment of assets.

Country size as a proxy for the range of natural factors such as climate, soil, minerals and etc, size of population that provides opportunities to process materials and create markets – Country Similarity theory

Factor proportions that suggest their optimum utilisation in production.

I. NATURAL ADVANTAGE THEORY

Sugar, Nickel and Tourism

Cuba has a natural advantage in the production of Sugar and its products.

The climate and the soil are best suited to sugarcane production from which sugar is obtained. The available labor force is skilled to produce sugarcane, which is why almost 6% of the entire world's sugar comes from Cuba.

Another natural advantage that Cuba boasts of is the production of Nickel and its mattes as Nickel ore is naturally available in the island. This ore is

mined and processed and exported. Almost 23% export of Cuba consists of Nickel products.

One of the major sources of income to the economy is the tourism sector. Cuba with its beautiful beaches, tropical climate and colonial architecture attracts a lot of tourists, which has invited a number of foreign investors in the tourism industry. Due to its naturally strategic location in the Caribbean, tourism flourishes round the year, so this too can be considered as a natural advantage. A huge contribution is made to the economy from the tourism industry and its growing steadily because of the slight relaxation in government rules in this industry.

II. COMPARATIVE ADVANTAGE THEORY:

Sugar with petroleum and Medical Services with Oil

David Ricardo in 1817 proposed this theory. This theory proposes that a country can gain more by producing a highly efficient product rather than a low efficient product, even though the country enjoys an absolute advantage in both. A country can benefit more if it concentrates its resources on a product that can be produced more efficiently.

The following two cases form a classical example to the above theory:

Cuba has a trade protocol agreement with Russia to supply sugar in exchange for petroleum. So instead of trying to focus the resources on petroleum, Cuba concentrates the resources on the production of Sugar.

Also Cuba has a trade agreement with Venezuela to supply them with Medical help in the form of medicine as well as professional help in exchange

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for Oil from Venezuela. In exchange for 100, 000 barrels per day of petroleum products from Venezuela; services of some 30, 000 Cuban medical professionals are provided. Cuba also imports food and machinery in exchange for sugar and nickel.

III. COUNTRY SIMILARITY THEORY:

Country similarity theory states that countries with similar characteristics will trade among themselves, especially in the industrial and manufactured products. A direct application of this theory can be observed in the trade between Cuba and Russia, Venezuela, China and Vietnam (Refer to the table) especially after 2005.

This is attributed to the fact that all of these countries have a communist framework of governance with the government holding most power and control. And all these countries trade with manufactured goods.

PORTER'S DIAMOND OF NATIONAL COMPETITIVENESS:

Michael Porter proposed a model for a nation's competitive advantage. There are 4 main attributes to superior competitive advantage of a country that includes advanced factors apart from the natural resources, land, labor and climate of the country. Combined effects of these attributes form the diamond of national advantage. They are:

Demand Conditions:

A country should produce a product that has a local demand which in turn will eventually create a foreign market. Local sugar industries produce sugar

so that it can be exported out of Cuba, which means a national advantage. So is tourism. Cuba attracts a lot of tourists for its serene beauty and rich heritage.

Factor Conditions:

Highly skilled labor, technology, capital and equipments that support a particular product are factor conditions. Sugarcane is processed into sugar through a series of steps, which is able to meet the global standards, making it remain a national advantage.

The beaches, music, dance, architecture and rich cultural heritage are the factors that promote tourism and in turn contribute to national advantage.

Related and supporting industries:

Those industries that support the existing industry and are directly related to it can also contribute to national advantage. In the case of Cuba, Nickel exports can generate the required revenue for the flourishing of Sugar industry. Also this revenue can help achieve more innovative and effective methods of producing Sugar. The revenue from Sugar and Nickel export can be used to further promote a thriving industry to self-stain the economy, under the veils of the communistic policies.

Firm's Strategy, Structure and Rivalry:

The demand for produce, various factors like climate, land, labor along with the various industries that are related to company, enables it to develop a sustainable competitive advantage, which can provide favorable

circumstances for firm strategy, structure and rivalry. Rivalry can also lead to innovative methods of production and advancements in technology.

Thus all these 4 factors combined together can provide a superior competitive national advantage, in the case of Cuba, Sugar and Tourism being the major players in the national advantage category.

RECOMMENDATIONS:

As we have analyzed the international business scenario in Cuba in detail, there are some factors, which the country can improve to prove itself in the international arena of business. Some of the recommendations are:

Foreign Trade Policy of the State:

With respect to the foreign trade policy, the Cubans are conservative in monetary circulations. They are very narrow in spending with other nations and retain a large sum, discouraging foreign investors from investing in Cuba, as expressed earlier. The government has to refine its policy extending fraternity to foreign investments regardless of capitalistic nations or communistic nations.

Doing away with delays:

There have been lots of complaints from foreign firms with respect to queuing in claiming import supplies as well as shortage of supplies and utilities. Also the state agencies are responsible for importing supplies. To get a competitive advantage in the international business, these delays should be avoided by sharing the import orders with other agencies

Prevention of robbery and improved customer service:

Cuba suffers a high degree of loot, low productivity and a weak customer service. This can be avoided by imparting the essence of customer focus from the laborers to the top level managers for an improved customer service and also set international standards for the same.

Subsidies to transportation and utility costs:

The government can encourage international business by providing subsidies in transportation and utility costs, as these are the major costs incurred by the companies.

Reformation of Judicial System:

Most foreign traders find the judicial system to be incompetent as it is an extended arm of the communist government and this discourages the companies from doing business, as they fear unfair judgment. The judicial system has to be made independent, providing confidence to the companies.

Provide subsidies to local companies and encourage innovation so that processes and technology can be improved which will further enhance the Sugar production levels so that more exports can be done.

Encourage joint ventures between local and foreign firms, but make sure that sharing of power and control is justified. The local firms might prefer to have an upper hand, but do not lose the foreign investment to a rival by being too parsimonious.

Tourism industry in Cuba has been a major contributor to economy, so further investment and innovation in that area can boost international attraction.

Private property ownership is not being encouraged unlike the appeasement in recent times than before. so relax such unwanted and control-minded policies.

Skilled laborers are an asset, so make sure that those involved in Sugar and Tourism industries are competent enough so that national advantage can be maintained.

Trade embargo with the US is a major hindrance; try to reach an amiable solution to the problem. There is no use in being iron fisted when the economy is bleak

CONCLUSION:

Self-sustained economy cannot rule out International trade with globalization acclamations of the day. This is high time for Cuba to realize the need for its apparent socialistic rule to be a really sociable one with respect to the International scenario. As discussed earlier, Sugar and Tourism are the major promising and resourceful industries of Cuba, which when properly guided and carried out, can prove to be the stepping-stone to a strong economy in the coming decade.