Cuba’s Entrepreneurs: Foundation of a New Private Sector by Philip Peters
In November 2010, the labor ministry set up a temporary office in an electoral commission facility to license new entrepreneurs in the Centro Habana municipality.
Introduction

After years of stagnation, Cuban entrepreneurship has changed and grown dramatically.

Regulations governing entrepreneurship were liberalized significantly in October 2010, notably allowing the hiring of employees. Official attitudes about it changed from indifference to encouragement. The number of Cubans employed in this sector increased 145 percent, from 157,371 in October 2010 to 385,775 today, representing about one in 13 workers.

Most important, the purpose has changed. In the past, when no thought was being given to changing the socialist model, entrepreneurship seemed to be viewed as a necessary evil, of marginal importance to the economy. It is now viewed as a strategic necessity for a government that is determined to cut costs and boost economic output by reducing government payrolls and expanding the private sector. For every new person employed as an entrepreneur, the government counts one more job created, one more stream of tax revenue, one more household with higher income, and one less household in need of the universal food subsidies that it aims to eliminate.

Entrepreneurship, in Cuba called trabajo por cuenta propia, or self-employment, is the most visible manifestation of economic reforms undertaken by President Raul Castro since he took office in 2008. The entrepreneurs, called cuentapropistas, are operating their new businesses on the streets of every city and town. State media are covering this sector amply and, in a new twist, favorably.

But the new entrepreneurs are only part of the reform plan, which is being developed and implemented according to a blueprint approved by the Communist Party in 2011. To reach major economic objectives involving job growth, productivity increases, improved government finances, and reduced incentives for young Cubans to emigrate, a larger “non-state” sector of the economy has to develop, one that will need to include larger and more complex businesses than those that today’s entrepreneurs are creating.

This paper examines the history of Cuba’s entrepreneurial sector, its current state, and the possible new forms of business that will build a larger private sector within Cuba’s socialist economy.

The evolution of Cuba’s private sector

When Cuba’s socialist government came to power in 1959, it did not set out immediately to eliminate small private enterprise. The first years of the socialist revolution saw the nationalization of large and foreign enterprises, the agrarian reform that redistributed agricultural lands, and the urban reform that did the same for residential property.

It was in 1968, the year of the “Revolutionary Offensive,” that the small business sector came to be targeted. In a speech in March of that year, then-President Fidel Castro stated:

A note on currency

Two currencies circulate in Cuba. In this paper, “pesos” refers to the Cuban peso, which trades at about $0.04. This is the currency in which state salaries are paid, and it is used for transactions in farmers markets, some state retail stores, and among most entrepreneurs.

The convertible peso was introduced in 1994 and trades at par with the U.S. dollar, except that a ten percent surcharge is applied when dollar cash is used to buy convertible pesos. (There is no surcharge if dollars are sent by wire transfer, as in the case of some remittances.) The convertible peso is the currency of the hard currency economy – the tourism industry, foreign businesses, some state retail establishments, and entrepreneurs such as restauranteurs, bed-and-breakfast operators, and artists, whose customers are foreign visitors.
“If this Revolution can be reproached for anything it is not in the least for being extremist, but rather for having been insufficiently radical. And we should not miss the opportunity or let the hour or moment pass to radicalize this Revolution even more. And we have to finish making a revolutionary people.

“There still subsist a true set of privileged ones who prosper from the work of others and live considerably better than the others as they watch others work. Idlers in perfect physical shape who put up a stand, a little business of any kind to earn 50 pesos per day, violating the law, violating health regulations, violating everything while they watch trucks go by carrying women to work in the outskirts of Havana or to pick tomatoes in Guines or wherever.

“If many are asking what kind of Revolution this is, that still permits such a class of parasites after nine years, they would be perfectly right to ask.”

With words like that, the small and medium-sized business sector that predated the socialist revolution was put on the chopping block. Restaurants, bars (Fidel noted in his speech that Havana had 955), and service operations of all kinds were “intervened,” or taken over by the state. This action was part of a broader intensification of ideology in a revolution that, as a University of Havana newspaper put it at the time, “sweeps away all vestiges of the past...that violently breaks the capitalist umbilical ties in order to embrace the luminous future with faith and hope.”

Luminous or not, Cuba’s future soon became one with only slight vestiges of private entrepreneurship, mainly barbers and beauticians, numbering 10,000 to 15,000. The economy, from farm to factory to retail services, came to be dominated by state enterprises. It all ran under a Soviet-style model where the state attempted to plan nearly all economic activity including production levels, employment, allocation of resources, pricing, and trade and investment with Soviet bloc partners.

The aversion to private entrepreneurship continued until the early 1990’s when the dissolution of the entire Soviet bloc provoked a sharp economic crisis in Cuba. Responding to that crisis, Cuba legalized the circulation of hard currency, built up its tourism sector, opened to foreign investment, promoted incentive-based agriculture, and undertook a limited opening to small-scale entrepreneurship.

The entrepreneurial sector, like the other reforms, was carefully circumscribed. Private entrepreneurship was permitted only by license, it was limited to 158 specific lines of work, and employees were not permitted except in the case of family “assistants” in cafeterias, lunch stands, and small restaurants.

The sector peaked in 1996 at 209,000 cuentapropistas operating restaurants and lunch stands, bed and breakfasts for tourists, and home repair and service operations of all kinds all across the island.

The government’s attitude toward entrepreneurship ranged from neutral to wary and never expressed a policy goal of encouraging its growth. A June 1998
document from the Cuban labor federation expressed concern about increasing corruption, including theft of state supplies, and partially blamed the economic reforms that the government had been “obliged” to make. It lamented inequality arising from the parallel hard-currency economy, which allegedly produces “egotism, the cult of capitalist fetishes, and the mentality of the small property owner.”

A typical official view was stated by economy minister Jose Luis Rodriguez in February 2001: “We don’t see that our country’s development rests on self-employment or small private property holders.” In March 2001 he said, “We believe there is no reason for the self-employed sector not to exist if it follows certain regulations, but we don’t stimulate it because we don’t think it is the solution to our economic problems.”

Come 2004, Cuba’s economy had improved from its condition a decade earlier but had by no means fully recovered. With a new and beneficial economic relationship with Venezuela maturing, the government decided to pull back from some of the previous decade’s reforms.

On October 1, 2004, as part of the general retrenchment in economic policy, the Ministry of Labor and Social Security issued new regulations governing self-employment, noting in a statement that “self-employment, in the current economic revival that our country is experiencing, acts as a complement to some state activity in the production of goods and the supply of services of value to the public, and is an alternative source of employment...” However, it continued, some private economic activities might “be assimilated...by the central state administration.”

The regulations provided that no new licenses would be granted in 40 categories of self-employment, but those working in the remaining 118 lines of work could continue to work and have their licenses renewed. In those, an “annual analysis” by municipal authorities would determine whether any licenses at all were necessary.

No new licenses were to be granted for private family restaurants, cafeterias, and lunch stands, and the numbers of these businesses dropped noticeably while the government expanded its own retail food services.
The result was that the number of entrepreneurs declined beginning in 1997 and stabilized at about 150,000 during the decade 2000-2010. The causes were many. An income tax was introduced in 1996. Some businesses fell victim to competition from the state or from other entrepreneurs down the street. Others were affected by regulatory enforcement that was in many instances normal, such as health inspections of food establishments, and in many other instances seemed punitive. A Havana man tells of his one run-in with the law for operating his bicicati (a pedicab) outside the municipality where he was licensed – an infraction that drew a sentence of two years community service in a day care center. “The only problem I ever had in life was for working,” he says.

Given all this, many thousands of Cubans risked working without a license, engaging in occasional, part-time, or full-time business activity.

This is the situation that would remain until 2010 when a new political leadership produced a new economic diagnosis and a new plan to revamp Cuba’s socialist economic model.

Entrepreneurship in a changing socialist economic model

In the 1990’s, an expansion of trabajo por cuenta propia was undertaken to make a modest contribution to economic recovery in a context in which Cuba’s economic model was being adjusted but not changed in fundamental ways.

By contrast, today’s expansion of entrepreneurship is part of a major overhaul of the economic model, and its role in that change is of central importance.

When Raul Castro assumed Cuba’s presidency on an interim basis in 2006 and fully in 2008, he led a process of analysis, debate, and reform in economic policy that, while not yet complete, is more consequential than any economic policy change in Cuba since the early 1990’s. His actions are based on assessments made by him – and earlier by his brother Fidel in his last major policy speech as President in 2005 – that economic failings constitute a threat to the survival of Cuba’s socialist system itself. (For a full discussion of this process, see the author’s May 2012 paper, A Viewer’s Guide to Cuba’s Economic Reform.) Among its main features:

• Blunt assessments, in official statements and in state media, of the shortcomings of Cuba’s economic performance.

• A critique of “paternalism” in the form of excessive social benefits, an oversized government role in economic activity, and a need “to erase forever the notion that Cuba is the only country in the world where one can live without working,” in Raul Castro’s words.

• A recognition that strategic goals for the economy – preserving essential social benefits, ending the dual currency system and creating a unified currency, improving government finances and Cuba’s external balances, addressing income inequality by raising state sector wages for doctors and others – can only be met if the economy as a whole becomes more productive.

Cuban entrepreneurs, by the numbers

385,775…the number of Cubans in the entrepreneurial sector May 1, 2012, including employees

7.5…the entrepreneurial sector’s percentage of the Cuban workforce

228,404…the number who joined this sector since October 2010

600,000…the number expected to be working in this sector by 2013 according to government economic plans

66…the percentage of entrepreneurs who had no formal job prior to joining the sector

18…the percentage of those who had been working for the state

19…the percentage of entrepreneurs age 18-35

110,000…the planned 2012 reduction in state sector employees

500,000…the planned reduction in state sector employees by 2015 (a reduction of 140,000 was achieved in 2011 and a reduction of 110,000 is planned for 2012)

25…the percentage of new entrepreneurs who failed and turned in their licenses, as of September 2011

16…the percentage of newly licensed entrepreneurs working in transportation as of September 2011; other top categories are food service (15), hired employees (10), housing rental (5), producers and sellers of home articles (4), and messengers (3)
A recognition that greater output will not be achieved through the state sector; rather, the state must shed unprofitable enterprises and unnecessary activities, substantially reduce its payroll, and allow a larger private sector to operate within the socialist economy.

Any doubts about government intentions to reduce its own payrolls were set aside in September 2010 when this headline appeared on the front page of the Communist Party daily *Granma*: “Announcement of the Central de Trabajadores de Cuba.” The announcement, by Cuba’s labor union federation, was that 500,000 state sector jobs would be eliminated by the following May, with a “parallel increase in the non-state sector.”

For laid-off workers, the announcement explained, there would be a “broadened and diversified” set of job opportunities, including “renting, usufruct, cooperatives, and self-employment, toward which hundreds of thousands of workers will move in the coming years.” Those are all private sector options: “renting” refers to the leasing of state installations such as barber shops, beauty shops, and taxis where the workers now operate as small entrepreneurs; “usufruct” refers to long-term leasing of land or other facilities as in farm cooperatives; “cooperatives” suggests non-agricultural uses of that formula; and “self-employment” means entrepreneurship.

The announcement stated that “it is known” that the state sector has more than one million excess workers. It noted that opportunities for re-employment in the government and its enterprises would be limited to agriculture, construction, teachers, police, and industrial workers.
Also in September 2010, a briefing document that explains these layoffs was made public. It quotes Raul Castro saying that if Cuba continues to maintain “inflated payrolls in almost all areas” and to “pay salaries with no link to results,” prices will continue to rise, purchasing power will continue to erode, and pay increases for productive workers will remain impossible.

The document anticipated that 64,546 new private jobs would be created in Havana, 85 percent in small entrepreneurship. It lists dozens of ideas for businesses that can be performed by private cooperatives outside the farm sector, although policies to establish such cooperatives have not yet been issued.

In practice, the layoffs proceeded more slowly than planned, but they have proceeded. State payrolls were reduced by 140,000 in 2011; reductions of 110,000 are expected this year, and a 500,000 reduction is expected by 2015, according to a Cuban labor federation official and published economic plans. In other contexts the stated estimates have been higher; for example, the finance minister projected that 1.8 million workers will join the “non-state” sector by 2015. Vice President Esteban Lazo predicted in April 2012 that the private sector’s share of gross domestic product would grow from five to 45-50 percent within five years.

To reduce government spending, in February 2010 the government ended the practice of paying 60 percent of the salary of workers laid off from their jobs. Instead, it declared that such workers could find work in the private sector, they could receive pay if they continue to engage in productive tasks of a temporary nature, or they could accept relocation to other state jobs if offered. “This is not about the state taking charge of placing everyone through several job offers,” Raul Castro said. “The first ones interested in finding a socially useful job should be the citizens themselves.”

In this context, job generation in the private sector – combining the cuentapropistas, private sector agriculture, future private cooperatives, and other private entities – is an essential enabler of various elements of the reform process. Stronger private sector job creation allows the government to proceed faster with layoffs and to reap their budget savings. As more entrepreneurs pay taxes, they boost government revenues, hastening the day when the government can afford to attack the pernicious disparities in Cubans’ purchasing power by, for example, raising the pay of doctors and others in the health sector. And each time a household income improves because of a private sector job, the easier it becomes for the government to end universal benefits such as food rations and to direct them to the needy only.

October 2010: the policy liberalization

Shortly after the announcements about state sector layoffs, the government followed with announcements about new regulations that would permit an expansion in Cuba’s entrepreneurial sector.

A September 2010 Granma article previewed the new policies and stated,

The logo of Pizza Habana, a new private pizza place with delivery service that operates from a townhouse in Havana’s Vedado neighborhood. The delivery territory spans from Belascoain Street alongside Havana’s largest hospital all the way west to 84th Street in Miramar.

Attitude adjustment

“Continuing about the need for a change in thinking, I’ll mention an example: If we have reached the conclusion that entrepreneurship constitutes one more employment option for citizens of working age, having the purpose of increasing the supply of goods and services to the public and freeing the state of those activities so as to concentrate on what is truly decisive, then what the party and government must do in the first place is to facilitate this form of work and not to generate stigmas or prejudices against them, much less demonize them – and for this it is fundamental to change the negative views that more than a few of us hold toward this form of private work.”

– Raul Castro, addressing Cuba’s legislature on December 18, 2010
The problem of supplies

In the author’s past surveys of Cuban entrepreneurs, a top complaint has been the inability to obtain supplies at reasonable prices or at wholesale prices.

This issue is being addressed slowly through developments in the state retail sector. If entrepreneurs’ supplies are made available and affordable, there will be more growth, and incentives for theft from state supplies will be diminished.

One example is a hardware store on 28th Street in Havana’s Miramar neighborhood. Opened in March 2011, it offers a variety of tools and materials for carpentry, general home repair, plumbing, tile work, electrical work, painting and caulking. Most of the store’s products are Chinese imports and some are from Spain, Taiwan, and even the United States. The store serves two of the government’s goals: development of the entrepreneurial sector and encouraging do-it-yourself improvement of the housing stock.

For the most part, its prices are accessible. Converted to U.S. dollars, they are $3 for a putty knife, $6 for a three-inch paint brush, $20 for a gallon of white interior latex paint, $5.50 for a hammer, $5.50 for a pair of pliers, $20 for a box of floor tiles that covers 1.10 square meters, $17 for pruning shears. Other items are more expensive; a welding machine costs $306, a five-step indoor ladder $100. And others are outlandish; a three-foot tall plastic garbage can costs $85, and a one-gallon Rubbermaid beverage cooler costs $51.

Another example is a small store outside Havana’s Carlos III shopping center that sells flour, grains, and spices in bulk. Pizza makers buy their flour there at a 27 percent discount, and if they buy an entire 20-kilogram bag the discount is 42 percent off retail prices.

This is one of many establishments that is selling lower-priced goods pursuant to a May 2011 resolution issued by the finance ministry that aims, according to a story in Trabajadores newspaper, to “facilitate sales to entrepreneurs.” The new pricing policy covers both imported and domestic goods, including barber and hairdresser supplies, canned goods, soft drinks, fabric and accessories, shoe repair supplies, and more.
Applicants needed to show a letter from a bank certifying that they are debt-free, and in a few cases such as food service and child care they need to obtain some health-related certifications.

The situation was similar at labor ministry offices in the provincial capital of Sancti Spiritus, where an official said that 720 licenses had been issued in the first two weeks of the new policy.

Public response to the new policies was strong because of the government’s new disposition to issue new licenses again, and because they in fact expanded opportunities for entrepreneurship:

• Licenses are now available in 181 lines of work.

• To bring entrepreneurs in from the black market, licenses may be granted to those without a vinculo laboral, i.e. those with no current workplace.

• Previously, only restaurants and small food-service operations such as sandwich stands were permitted to employ assistants. The new regulations permitted employees to be hired in 83 lines of work, and later they were changed to allow employees to be hired in any line of work.

• In private restaurants, the seating limit was increased from 12 to 20 and later to 50. Prohibitions on serving beef and shellfish were ended.

• “Housing, rooms, and spaces” may be rented to entrepreneurs for use as places of business.

• Entrepreneurs may now have licenses for more than one line of work.

• Unlike before, entrepreneurs may work anywhere, not just in the municipality in which they were licensed.

• Instead of being restricted to selling to individuals, they may now sell goods and services to state entities, foreign companies, and cooperatives.

• A June 2012 article in Granma discussed the ways in which government entities in Artemisa are contracting “brigades” of carpenters, painters, bricklayers, and other construction workers to fix a stadium, cafeterias, and other public buildings. A local official praised the “speed and quality” of their work.

• Entrepreneurs must pay income tax. The first 10,000 pesos of income, an amount that equals approximately twice the average salary paid in the state sector, is tax-exempt. The top marginal rate is 50 percent. Expenses totaling up to 40 percent of gross income may be deducted from taxable income (the previous limit on deductions was 10 percent). In addition, there is a sales tax, a public service tax, and a tax per employee hired, all deductible from income tax. The tax on hired labor is explained as necessary “to avoid concentrations of wealth.”
• Finally, there is a contribution to social security, which entitles entrepreneurs to disability and maternity benefits and monthly payments upon retirement. Taxpayers can vary the amount they contribute, and benefits will depend on the amount contributed.

• In May 2011, these policies were eased to favor job creation over tax collection. The tax per employee was suspended for businesses with fewer than six employees, taxes were reduced and deductions increased in some occupations, and businesses were allowed to close for repairs more easily and for longer periods, suspending their licenses and their tax obligations.

Beyond the new regulatory treatment, other government actions evidence a change in attitude toward entrepreneurs and a desire to see the sector grow rather than simply subsist.

**News coverage.** The Cuban media’s treatment of the sector has changed dramatically. In the past, coverage of entrepreneurs was sparse and mainly fell into three categories: stories about pilferage of state resources to supply private businesses, stories about food service establishments that violate health codes, and stories about entrepreneurs profiting from deeply subsidized public services such as electricity.

Since late 2011, there is much more coverage of entrepreneurs, and much of it is positive. A one-minute June 2011 story on the news station Radio Reloj told about the increased numbers of entrepreneurs in Ciego de Avila, especially in food service. It told of a couple that runs a cafeteria across the street from a medical clinic and said that their fare has “earned the appreciation of the people.” Simple, positive coverage like that did not exist two years ago.

Cuban media encouraged people to apply for licenses and explained how to do so. In November 2011, an article in *Granma* detailed the new regulations governing home rental and the ways in which they “considerably broaden” the possibilities for this line of work. It explained that entire houses may now be rented in the Cuban peso or convertible currency; space can be rented for lodging or for use by other entrepreneurs (e.g. a room for a hairdresser, a front porch for a sandwich stand); those who rent out their homes can now get licenses for additional lines of work; and they may hire employees. The article noted that the time to process a license application is now 15 days instead of 30.

This same information, along with details about the application process, was carried repeatedly by Radio Reloj.

In January 2011, Radio Rebelde had labor ministry officials spend several days answering callers’ questions on the air to clarify the new regulations governing small entrepreneurship.

In December 2010, with new licensing processes in effect barely one month, *Granma* ran a 1,300-word article on the necessity “to untie the bureaucratic knots that slow down the expeditious issuing of licenses to small entrepreneurs.”
The article described the visits of officials to nine municipal licensing offices. These troubleshooters discovered “knots” in the process – such as an office that required applicants to supply four documents that are not required by law, or a case where health officials’ certifications for food vendors were coming too slowly – and fixed the problems.

The officials’ intent, the article reported, was to ensure that the same bureaucratic headaches “that have characterized other processes” do not affect the licensing of new entrepreneurs.

At one office, a surly worker tried to turn the group away because they had not received prior permission. That was a “‘welcome’ that should already belong to our ancient history,” the article said. One of the officials retorted: “Didn’t you listen to compañero Raul? The locomotive is already starting to roll.”

In February 2012, entrepreneurship was the subject of a long segment on Al Derecho, a television program that examines real-life situations and legal issues related to them. In this case, the subject was a lunch stand in Havana’s 10 de octubre neighborhood called “The Good News of Christ.” Located near several workplaces, the business was prospering but straining to keep up with demand. The reporter speculated that slow service could cause customers to drift away, and the business was deemed a good candidate for a loan to buy a new, higher-capacity oven. Would such a loan be possible? Back in the studio, the anchor then interviewed a bank lawyer whose answer was a clear “yes,” and she proceeded to explain all the details of applying for and paying back a small business loan.

Tourism. The April 2011 economic policy blueprint adopted by the Communist Party Congress singled out the private sector as a contributor to the tourism industry. A June 2012 international tourism fair in Havana was opened to participation by Cuba’s private restaurants and home-based bed-and-breakfasts. A May 2012 article in Juventud Rebelde noted the contribution of the entrepreneurial sector to the tourism industry, with 1,618 private restaurants and 5,207 homes in which Cubans rent rooms to foreign visitors.

Advertising. Cuba’s telephone company Etecsa announced in May 2012 that its 2012 telephone directory was opened for the first time to private business listings. In 13 days, 223 cuentapropistas listed their businesses and an additional 286 placed display advertisements.

<table>
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<th>Year</th>
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<th>Workforce</th>
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<td>1995</td>
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From official data cited in Cuban media, academic analyses, and official statements. 2011 and 2012 figures include entrepreneurs and their employees, following policy changes in 2010 that allowed hiring of employees.
Credits. On December 20, 2011 a new policy went into effect to permit entrepreneurs, private farmers, and homeowners carrying out renovations and repairs to obtain bank loans. Entrepreneurs may borrow to finance purchases of capital equipment or supplies. If approved after a bank performs a risk assessment, loans are granted with a minimum principal of 3,000 pesos (about $120) with amortization periods from three to 60 months and interest rates from one to 8.5 percent. In July 2011, the Central Bank president told a legislative committee that interest rates should yield a profit for the banks but be set “in accordance with the need to stimulate economic activity.”

Day care. An April 2012 article in Trabajadores reminded private sector workers that they have equal rights to use state day care centers for their children and gave examples of entrepreneurs who use them, with one paying one sixth the cost of her previous private day care arrangement.

Snapshots of the new entrepreneurs

With the new policies governing entrepreneurship, a retiree in rural Pinar del Rio province said, “The only people not working are those that don’t want to.” That’s an exaggeration, but an easy one to make given the appearance of so many new businesses across Cuba.

The block of Havana’s Neptuno Street between Aguiar and Amistad Streets is a good example. It is near areas frequented by tourists, but it is not a tourist spot and its businesses cater to Cubans. Many new businesses were in operation during a June 2011 visit.

A retired house painter sold herbs for medicinal, religious, and culinary uses from his front step, paying 150 pesos per month tax and earning, he said, a modest supplement to his pension. He was fixing up a bedroom upstairs to rent to foreigners, but he was waiting for the “right moment” to start that business. The room rental, he believed, would be “the only way to get my head above water. When I marry again it has to be to a foreigner too.”

Nearby, a babalawo (Santeria priest) ran the Ile Ogdara religious articles shop, with a cafeteria alongside. He pays 2,000 pesos per month to rent the space, and one month into the business he expected to do well. Next door to him, a shop sold religious clothing.

A few doors away, a woman took advantage of the new regulations to take out two licenses so she could sell party supplies and music CDs in the same premises. With a combined monthly tax bill of 450 pesos, she was clearing between 1,000 and 1,500 pesos per month.

Across the street, the Gran Via store is a place where the government rents space to 15 individual entrepreneurs for 30 pesos daily. Businesses included jewelry and watch repair, sales and repair of shoes and sandals, sale of wicker-like patio furniture made by the vendor’s husband, and more. “Much of this was hidden before,” one repairman said, “and now people are coming out in the open.”
In the small town of Santa María del Rosario, a barber works in a shop facing the town’s main square and 18th century church, and his work actually has national significance. He and others like him are in the vanguard of two movements crucial to the success of economic reform: the reduction of state payrolls and the movement of productive activities from the state to the private sector.

In 2011, 1,500 small barber and beauty shops were converted into private entities on an experimental basis. Despite this measure’s limited reach, a state radio station in Ciego de Ávila called it “an important step in the current economic adjustment that has as one of its main goals relieving [the state] of the heavy load brought about by the excessive paternalism in which it has engaged for more than half a century.”

The experiment was declared a success and a new law formalized the arrangement and provided for it to be extended to all barber and beauty shops with three or fewer chairs.

It’s a small start toward a declared goal of adding 1.8 million workers to private payrolls by 2015, but it’s a start.

The law provides that:

- the workers will work as private entrepreneurs and will enter contracts with the state to pay rent for their place of business;
- monthly rent is charged per square meter with a minimum payment that ranges, in the case of barbers, from 220 pesos in Havana to 15 pesos in the most rural areas of eastern Cuba;
- workers also pay income tax and social security contributions;
- prices are not regulated, the workers are responsible for their own supplies, and they may not sublet the space to other tenants;
- when leaving state employment, workers are owed a cash payment for any unused vacation time.

A similar change is taking place in state taxi companies. A Cubataxi driver explained that in 2010 his company stopped paying his salary and started renting him his taxi for a flat $42 per day. He keeps the taxi at his home, pays for gas and repairs, charges in convertible pesos, and keeps his profit. Interviewed in June 2011, he was not yet sold on the new system because his earnings vary so much between high and low tourism seasons.

What does the experience of converting the smallest barber and beauty shops into private entities tell about the government’s task ahead? First, the pilot projects and limited scope indicate the slow, cautious pace of the reform process. Second, these are examples of reductions in state sector payrolls that do not involve layoffs, but rather the conversion of state jobs to private jobs on the spot. The move to create private non-farm cooperatives will likely repeat these traits.

Snip, snip, snip

In the course of 2011, 1,500 small barber and beauty shops were converted into private entities on an experimental basis. Despite this measure’s limited reach, a state radio station in Ciego de Ávila called it “an important step in the current economic adjustment that has as one of its main goals relieving [the state] of the heavy load brought about by the excessive paternalism in which it has engaged for more than half a century.”

In November 2011, the experiment was declared a success and a new law formalized the arrangement and provided for it to be extended to all barber and beauty shops with three or fewer chairs.

For the barber in Santa Maria del Rosario, the change came in May 2011; he lost his state salary and his life became both more complicated and more lucrative. He pays 993 pesos per month to the state to cover rent, utilities, and taxes. That works out to about 40 pesos per workday, so he has developed the habit of setting aside that amount each day – and on a typical day, he says, that leaves about 80 pesos for himself. He acquires supplies completely on his own without difficulty, he says, including the electric clippers that friends bring him from the United States. His prices: ten pesos for a regular haircut, 20 for a “styled” cut, ten for a shave, all to the sound of Reggaeton played through an I-pod blaring through two small computer speakers on the windowsill.
At the corner, a window that opened to the sidewalk was occupied by a plumbing supply vendor. The vendor, one month into the business, was optimistic.

On J street between 25th and 29th streets, a two-block stretch leading to the University of Havana, new entrepreneurs have taken advantage of two factors – heavy daily pedestrian traffic and the closure of some of the cafeterias that the university used to run to provide employee lunches – to open five new lunch stands that offer pizza, pasta, sandwiches, salads, hamburgers, and more.

On Havana’s Infanta Street near the Carlos III shopping mall, there is a sign for an “Esoteric Digital Library.” Inside there are three businesses on the premises, run by a couple.

They have been entrepreneurs since 1994, when they got their first license for a home-based cafeteria. Tired of that work, they took advantage of the new opening to entrepreneurship to take out three licenses in November 2010: for a library, a manicure salon, and a posada, a place where couples can rent a room and get some privacy (three hours for 125 pesos).

And what is an Esoteric Digital Library? It is a place where customers come with a blank compact disc or flash drive to download books and articles about subjects such as *feng shui*, Tarot, the occult, and “thinking positive, how to overcome problems,” the proprietor explains. The first download costs 20 pesos, and each one after that costs 10.

190 kilometers west of Havana, the rural town of Vinales in Pinar del Rio province attracts tourists because of its natural beauty and because it is the heart of Cuba’s prime tobacco growing region. Locals have long operated businesses that take advantage of the tourist traffic and in a June 2011 visit, there were more businesses than before.

A local official said the number of entrepreneurs renting rooms in their homes had jumped from 200 to more than 400. The local tourist hotel on a hillside just out of town has only 78 rooms.

A recent economics graduate had just opened a gallery on the main street to sell art and photography. She does business in a sheltered porch and interior room that she rents from a retiree.

On the main street: room rentals, several cafeterias, ice cream stands, vendors of imported trinkets and housewares, pizza makers, and new private restaurants. Several taxi drivers had started business in recent months; one also rents a room in his home and is fortunate enough to be listed in *Lonely Planet*.

New restauranteurs worried about competition and many employ promoters who approach visitors to drive business their way. The owner of one new restaurant on the main street, *El Colonial*, said about 15 new private restaurants had opened in the past six months. Subsequent visits showed that some restaurants off the main street had closed.
Assessments

The growth of small enterprise has been strong and positive in several respects.

After hovering around the 150,000 level for more than a decade, the addition of 228,000 to this sector, counting both entrepreneurs and their employees, represents very substantial growth of 145 percent in legal employment.

It has demonstrated the amount of grass-roots economic initiative that previous regulations had driven into the underground economy or suppressed altogether.

The expansion of entrepreneurship has improved family welfare, boosted government revenues, and begun to provide a destination for workers laid off from the government’s “inflated payrolls.”

Current regulations do not amount to an open grant of economic freedom to all who wish to start the business of their choice, but the 2010 liberalization greatly expanded space for private economic initiative and is a positive human rights step.

Government statements that the new policies are here to stay are credible.

While Cubans remember the retreats from the economic openings of the 1990’s, many are watching the policies in action and the change in official discourse and are believing that there will be no turning back this time.

With the reform process steadily reducing state sector employment, further expansion of private employment is essential. A reduction would disrupt other parts of the reform program and be politically problematic.

Regulations continue to limit the growth of entrepreneurship and the benefits it provides the public.

The new regulatory regime is a significant pro-growth improvement: it allows entrepreneurs to hire employees, to hold multiple licenses, and to sell to government entities, state enterprises, and joint ventures. Development of markets for entrepreneurs’ basic supplies, especially at wholesale, will mark a further improvement.

Yet the need to choose among a list of 181 licensed lines of work is a limiting factor, preventing would-be entrepreneurs from choosing the activities that appeal to them and in which they believe they can succeed.

More than small-scale entrepreneurship in its current form is needed to meet the government’s goals for generating new private sector employment.

An expansion of Cuba’s entrepreneurial sector by more than 200,000 was unimaginable a few years ago. So was a government decision that a key to improving productivity is to expand the private sector by more than one million workers.
Cuba’s government gives Vanguardia Nacional awards for great socialist achievement. If such an award is ever given for small entrepreneurship, a candidate may be found across from Havana’s biggest farmers market.

The business is a small shop that sells religious objects and herbs that are used for both health and ceremonial purposes.

Taking advantage of the new regulations, the owner has hired ten employees, including one on the sidewalk outside hawking business with a megaphone. Business is steady and his location is a big advantage, with lots of foot traffic generated by the farmers market and many other nearby businesses. He has opened a small clothing store next door with two employees, where mainly religious clothing is sold, and a cafeteria around the corner with four employees. He and his father jointly run a small farm east of Havana with 10 employees.

“The taxes are high but this business is so fruitful that I don’t feel it,” he says, voicing a view that few other entrepreneurs would share. “I pay taxes with pleasure because I don’t have to hide anything. If an inspector comes I show him everything and all my employees are paid for.” He pays his employees 600 pesos monthly, more if business is good.

Other comments from the 48-year-old owner:

“I always wanted to be able to have employees to make the business bigger, and now it’s all legal. We need more stock all the time. I sell at low prices so people keep coming back.”

“The attitude of the state has changed for the better. There have been no inspectors for a year, and they used to be here all the time.”

“The government is watching very closely because many people got licenses and were scared by the taxes and they turned them back in.”

“I was born in this system, but I learned a lot from my father. Cubans don’t know entrepreneurship but we are just starting to learn how to have private businesses. It will take time, it’s like telling a baby all of the sudden to get up and walk.”
But entrepreneurs alone are not likely to generate one million new private sector jobs under current rules. Those jobs, combined with further reductions in the public sector workforce, can potentially eliminate a fiscal deficit that has already declined from 6.9 percent of gross domestic product in 2008 to 3.8 percent last year.

In Cuban discussions of economic policy – in academic journals, public debates, Catholic church magazines, and state media – there is no shortage of ideas for policies to spur the expansion of the private sector.

When it comes to entrepreneurship, the most common suggestion is to treat the sector as an “infant industry” by reducing taxes to promote growth until the sector matures. Other suggestions are to do away with the list of 181 permitted lines of work and instead to allow entrepreneurial ventures in any line of work except those that the state may reserve to itself, and to allow professionals to work as entrepreneurs in the field for which they were trained.

However, the potential for far more substantial job growth lies in the creation of private non-farm cooperatives. In this area, policies have yet to be defined except in general terms.

The economic policy blueprint adopted in 2011 by the Communist Party stated that private cooperatives will be formed “as a socialist form of collective property in different sectors...integrated by persons who join together contributing goods or labor....and assume all their expenses with their income.” A briefing document circulated as layoffs were beginning in 2010 noted dozens of potential business lines for cooperatives, including services to municipal governments, and singled out five general areas: agriculture, construction, construction materials, transportation, and food production.

Equal results vs. equal opportunity

“Raul and Fidel are two different men. Raul is a man of few words but one word that he said was very important: igualitarismo [egalitarianism]. Before, that’s what we had. If I work and you don’t and we still have to be equal, the result is that I won’t work. Now, if you are enterprising and honest and you do well, there is no problem.”

– a Havana entrepreneur who runs two businesses
A policy for pilot projects for non-agricultural cooperatives in three provinces was approved in March 2012, but details were not released. Among the issues to be defined will be policies governing cooperatives that are converted from state enterprises (such as cafeterias, repair shops, and manufacturing operations that are handed over to workers), and start-up cooperatives formed by persons who affiliate for that purpose. Also to be defined are levels of taxation, the sectors in which cooperatives may do business, and whether professionals will be permitted to participate. A likely limiting factor in the policies governing cooperatives is the government’s concern about “concentration of wealth,” which will presumably be addressed through taxation.

The new tax system is a key variable.

A primary consideration in tax policy has been fairness: charging entrepreneurs for the government services and benefits they receive.

The choice of tax rates is a matter of conflicting objectives. Higher rates can potentially increase near-term government revenues, enabling expenditures on other priorities such as attacking income inequality by raising some state sector salaries. Lower rates can encourage job creation and increase disposable income which, in turn, can fuel further private sector growth.

The government has shown that it is weighing these considerations, and its 2011 tax reductions were a mid-course correction to encourage job creation over immediate revenue generation.

To date, the impact of taxes on the entrepreneurial sector has varied. Surely, taxes are among the factors that have caused some entrepreneurs to return their licenses.

It is also possible to find entrepreneurs who are not held back by the current tax burden.

An entrepreneur who runs a pizza and sandwich stand in a good Havana location said he pays 400 pesos per month in tax – a burden that is “not very strong.” He has operated since May 2011 and his gross revenues average about 2,000 pesos daily, although he says that with each passing month he is feeling the effects of greater competition from additional private establishments. With his savings, he is starting a new cafeteria ten blocks away.

Many entrepreneurs are working below their professional potential and outside the fields of their education and training.

The lack of entrepreneurial opportunities for Cubans with advanced professional and technical skills means that Cuba is failing to take full advantage of the investment made in their education and foregoing their potential contribution to economic development: innovation, competitiveness, export growth, job growth, and reduced incentives for young Cubans to emigrate.

Many of the new entrepreneurs, such as those re-selling housewares brought to them from relatives abroad or selling copied music and movies on disc, have created jobs and pay taxes but otherwise contribute little to development.
The expansion of private sector food service, including attractive, high-quality private restaurants, is posing strong competition to the state sector.

The competition is so strong that one now sees state restaurants stationing employees on sidewalks to drum up business from passers-by. In spite of positive official statements about the private sector, government tour operators are refusing to arrange meals at private restaurants and refusing to transport passengers to them.

Cuba’s entrepreneurs are benefiting from investment from abroad.

An Inter-American Dialogue survey of Cubans who receive remittances from abroad showed that among recipients, 23 percent work as entrepreneurs and 34 percent are interested in doing so. Of that latter group, 95 percent believe that their initial capital requirement would be between $1,000 and $5,000, and 62 percent said they would seek their seed capital from relatives abroad.

Examples abound: a photographer in rural Bahia Honda whose Nikon digital camera, HP photo printer with Kodak paper, and props for children’s photos were all supplied by his family in Miami; a retiree in Sancti Spiritus setting up a private bakery aided by $300 per month from his Miami relatives; and a tire repairman in rural Guayos whose supplies come from Florida relatives. And there are private restaurants whose seed capital came in whole or in part from relatives and partners abroad.
Source material and further reading

The author’s May 2012 paper, *A Viewer’s Guide to Cuba’s Economic Reform*, explains the reasoning behind the reform process, its goals, commitments and progress made to date in each sector, the public debate about it, its political implications, and more. Available at lexingtoninstitute.org.

*The Cuban Triangle* blog, written by the author, has monitored economic policy developments since 2007 and is searchable by word and by tag. For all posts on entrepreneurship: http://cubantriangle.blogspot.com/search/label/cuenta%20propia

The *Gaceta Oficial* is published by Cuba’s Ministry of Justice and available on-line; the new regulations that liberalized the treatment of *trabajo por cuenta propia* (entrepreneurship) are in its October 8, 2010 issue; regulations governing severance pay for laid-off employees, the hiring of temporary agriculture workers, the rental of housing, and other topics are in that same issue; regulations governing the conversion of barbers and beauticians from state employees into entrepreneurs are in the November 11, 2011 issue; regulations governing taxation of entrepreneurs are in the September 7, 2011 issue; regulations governing bank loans for entrepreneurs, farmers, and home improvement projects are in the November 21, 2011 issue.

Data on Cuban population, demographics, health trends, and many other social and economic indicators are published by Cuba’s National Statistics Office and are available on-line with many data series in Excel format. See the annual statistical yearbooks and single-topic publications at www.one.cu.

*Espacio Laical* and *Palabra Nueva*, two magazines of the Archdiocese of Havana that contribute consistently to the economic debate, are available on the web.

The Guidelines for Economic and Social Policy adopted by the 2011 Communist Party Congress that constitute the blueprint for the economic reform process, are available in Spanish and English at the Cuban foreign ministry’s website, cubaminrex.cu.


*Photos by the author.*

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