

FUTURE SOCIAL POLICIES IN CUBA: SEARCHING FOR AN OPTIMAL BALANCE

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**Governance and Social Justice in Cuba:
Opportunities and Constrains**

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- **Three Scenarios for the Transition**
- **Future Social Policies on:**

Health Care

Social Security Pensions

Education

Income Distribution

THREE SCENARIOS FOR THE TRANSITION

- 1) The current political regime continues but resumes the reforms halted in 1996 and partly reversed since 2003, reinstates policies reversed and implements others previously planned but not executed. This approach won't generate the needed dynamism in the economy
 - 2) Gradual implementation of a socialist market economy following China-Vietnam style policies, dismissed by Fidel arguing major differences between Cuba and China on size, distance from the USA, and Cuba's burden by the embargo, arguments not as applicable to Vietnam. Unlikely to materialize while Fidel is alive, after his death it might be the best road map for the succession. We will focus future policies on this scenario, intermediate between 1 and 3.
 - 3) A full-fledged transition to a market economy and democracy similar to that in Central-Eastern Europe, the Baltic region and the CIS. An unlikely scenario, at least in the short term and probably in the mid term
- Whatever the scenario, Cuba won't be able to cope with social problems, without macroeconomic reforms that increase GDP, output, productive jobs, real wages and fiscal revenue.
 - An optimal balance should be searched between the desire for equality and equity on the one hand, and the need for incentives, efficiency, growth and financially sustainable social policies.

HEALTH CARE

Health services that are free for all and not means-tested increase cost, subsidize high-income groups, reduce the quality of services and are financially unsustainable in the long run, particularly in aging societies as in Cuba.

- **Maintain the public health care system but infusing competition in the state monopoly, raising its efficiency, reducing costs and improving the quality of its services, by reallocating resources, eliminating or reducing costly programs of low domestic value, generating new sources of revenue, and striving for an optimal balance.**

Reallocating resources:

- **Give absolute priority to improving the badly deteriorated infrastructure of potable water and sanitation.**
- **Halt investing in new physical plant and give precedence to maintaining buildings and equipment.**
- **Convert unneeded hospitals (particularly gynecology and pediatrics, the most underutilized) into old-age homes for the needy.**
- **Reallocate scarce resources to areas in urgent need, such as basic infrastructure, prevention of contagious diseases and import of essential medicines and prophylactics (funds invested in reducing the already low infant mortality are a prime target for reallocation).**
- **Partly shift resources assigned to training of physicians towards expanded training of nurses and paramedic personal.**

Reducing costs:

- **Terminate the free overseas medical aid program as well as the fellowships for foreign students in Cuba.**
- **Integrate the costly, privileged scheme for the armed forces and internal security personnel, and top leaders of the party and government into the general health system.**
- **Make the pharmaceutical and biotechnological industries efficient, competitive, and profitable with regulated foreign investment.**

Increasing sources of revenue:

- **Charge the full cost of private rooms to high income groups who want better quality of service (e.g., better food and air conditioning) and can afford to pay.**
- **Attract retired Cubans living abroad to move back and receive health care, negotiating the transfer of insurance costs with foreign governments.**
- **Offer large enterprises tax incentives to provide primary health care to their employees.**

Optimizing the balance:

- **Subordinate the number of health professionals working abroad to meeting internal needs, and invest part of the external revenue generated by those abroad in improving domestic health care and the supply of medicine and other badly needed inputs.**
- **Authorize self-employment of physicians and creation of medical cooperatives, (eventually providing services for foreigners in competition with the state), charging taxes on their profits.**
- **Allow religious orders to expand their free asylum facilities by increased immigration of their members, and subsidize their services.**

SOCIAL SECURITY PENSIONS

- **The current pension system is unsustainable (the 2006 deficit was 39% of expenditure and 3% of GDP, fully financed by the state) because of the lowest retirement ages (55 women, 60 men) and highest life expectancies in the region, insufficient revenue, and accelerated aging of the population (which declined for the first time in 2006). On the other hand pensions are grossly insufficient to meet basic needs.**

Cutting expenditures:

- **Gradually increase the current retirement ages by five years for men and women, in a 20-year period.**
- **Integrate the costly privileged schemes of the armed forces and state security personnel into the general pension system.**

Increasing revenue:

- **Expand the worker salary contribution for pensions stipulated in the 1994 tax law from the current 20% of the labor force (in *perfeccionamiento empresarial*) to all salaried workers.**
- **Establish salary contributions in all non-state firms having a minimum number of employees.**

Optimizing the balance:

- **Cover on pensions all private sector employees—formal and informal, some under special conditions and benefits.**
- **Incorporate self-employed workers by charging them the same percentage contribution of salaried workers, plus a state subsidy in lieu of the employer contribution (that they lack) on behalf of low-income self-employed.**
- **Raise the minimum pension in tandem with economic improvement and expansion of contributions and fiscal resources.**
- **Introduce a voluntary supplementary pension program for high and upper-middle income groups.**
- **Consider as alternative to close the current pension system, making the state responsible for ongoing pensions, and creating a mandatory public system for younger workers, at lower costs and financed by employer and worker contributions, with voluntary individual accounts for supplementary pensions and a fund invested to generate capital returns.**

EDUCATION

A public educational system should be maintained but adapting it to the nation needs, improving its efficiency, reallocating resources and generating new sources of revenue.

Reallocating resources:

- **Develop education programs that respond to economic needs and demand.**
- **Rationalize resources at the primary school level. Low student-teacher ratios and declining birth rates justify shifting resources to other areas in need. For example, establish an adequate wage structure for teachers in secondary and higher education.**
- **Make vocational education a priority.**
- **Improve educational efficiency, reduce desertion rates and establish rigorous quality standards.**
- **Introduce proper incentives to train technicians, agronomists, managers, bankers and other professionals. Create schools of business administration and modernize faculties of economics.**

Generating new sources of revenue:

- **Establish tuition in public higher education, exempting capable poor and low income applicants who have been submitted to a means test.**

Optimizing the balance:

- **Authorize self-employment of teachers. Allow participation of private schools particularly at the university level under strict state rules.**

INCOME DISTRIBUTION

The tax structure is increasingly regressive: 65% of tax revenue in 2006 came from indirect taxes (60% on sales, and 5% on public utilities), and 35% from direct taxes but only 1% from “personal” income; 8% from profits, 17% from labor and social security. There are progressive taxes on inheritance, real estate and Income earned abroad, but none generate significant revenue, and the 1994 law didn't establish a general income tax.

Changing tax policies:

- Reduce sales and public utility taxes to the minimum necessary and replace them by a combination of a progressive personal income tax and a corporate tax.
- Make all residents and those earning income abroad pay income tax, with few rates and exemptions, and withheld on salaries, interest and dividends.
- Reduce the sales tax rate as more consumer goods become available and private shops established; the increase in sales volume should offset that cut.
- Taxing remittances is difficult due to the informal channels used, although part of that revenue is currently taxed in the state hard-currency shops at a very high rate.
- Soften tough taxes currently imposed on self-employment, *paladares* and house rentals for tourists in order to promote rather than discourage these activities.
- Keep taxes on alcohol and tobacco because of their positive health effects.

Optimizing the balance:

- **Balancing growth and equity is crucial in the transition: economic incentives are indispensable to promote savings, growth and employment, but the reform will accentuate inequalities. Policies suggested above would help to reach equilibrium between the unavoidable inequalities and equity.**
- **Establish a wide social safety net to protect vulnerable groups during the transition**
- **Make workers owners of part of the national productive capacity, so that the partial privatization process achieves a degree of distributive equity. Other alternatives are to use part of privatization revenue to finance the cost of ongoing pensions or fund a new pension scheme for younger workers.**