CUBA'S DUAL CURRENCY DILEMMA

By Matthew Rinaldi

Two Different Cuban Pesos

In 2017, visitors to Cuba from the United States, including first time delegates from the National Lawyers Guild, often found themselves perplexed by the use of two different peso currencies inside Cuba. Like most economic distortions in Cuba, the problem of dual currencies can be traced to the impact of the United States blockade of the island. The use of two currencies has created unintended and unanticipated problems for the Cuban economy.

Upon entering Cuba, foreigners must change their currency into Cuban Convertible Pesos, known by the acronym CUCs. All currency exchanges, or cadecas, charge a 3% fee for any transaction, but U.S. dollars are charged an additional 10% penalty before being exchanged for CUCs. Once within Cuban society, visitors learn to pay for hotels, tips, tourist cabs and most tourist attractions in CUCs. Cubans working in the tourist industry acquire CUCs, while Cubans working in non-tourist industries are paid in regular Cuban pesos, the national currency or "moneda nacional", known by the acronym CUPs. At any Cuban currency exchange, each CUC is worth 24 CUPs. How did this contradiction develop?

The revolution in 1959 inherited a Cuban peso tied to the dollar economy. With the rupture between the Cuban revolution and the United States, including U.S economic sanctions and the Bay of Pigs invasion, Cuba demonetized the pre-revolutionary peso and introduced a redesigned peso. All of these pesos were CUPs. Cubans on the island had a relatively brief opportunity to exchange the old currency for the new. Many emigres in Florida who were still holding old pesos in cash saw their value extinguished.

The redesigned pesos carried images of Cuba's wars of revolution and independence, retaining Jose Marti on the one peso note, with an image of the 1959 rebel column entering Havana on the reverse, Antonio Maceo and Maximo Gomez on the 5 and 10 peso notes and adding Camilo Cienfuegos to the 20 peso note. Early peso bills were signed by Che Guevara, who was President of the National Bank of Cuba for slightly over a year.

Some Cubans who chose to remain in Cuba after the revolution were skeptical of the new currency. A few held on to the old pesos, but soon found they were unable to spend them. A larger number held on to U.S. dollars, certain they would retain their value. Some of these dollars continued to circulate in the unofficial economy.

Cuba ultimately confronted the U.S. blockade by joining the Soviet economic trading bloc, and the new CUP pesos became Cuba's currency within the Soviet Council for Mutual Economic Assistance, or COMECON. Much of this trade was barter for goods like sugar or consisted of direct aid, requiring limited use of international currency transactions. This period of relative currency stability stretched for decades, but ended with the collapse of the Soviet Union. Financial assistance from the Soviet Union and trade with the Soviet bloc declined precipitously between 1989 and 1991, cutting off critical financial transactions and sending Cuba into a spiraling economic decline known as the Special Period.

The Cuban CUP peso was not accepted in world currency exchanges and was worthless in the now dominant U.S. world economic bloc. Cuba faced a shortage of hard currency and a desperate need for international trade after the collapse of the Soviet Union.

Anti-revolutionary forces with the United States, seeing this crisis, were quick to act. Their goal was to wreck what remained of the Cuban economy. The Torricelli Bill of 1992, also known as the Cuban Democracy Act, openly called for regime change in Havana and imposed severe sanctions on companies and countries throughout the world conducting trade with the Republic of Cuba. It is this imposition of sanctions on other sovereign nations which transforms the U.S. "embargo" into a true "blockade" (or "el bloqueo" as it is known in Cuba.)

The Cuban government initiated dramatic changes to overcome the economic crisis. In one major policy change the island was thrown open to tourism, with the hotels and rental homes at the fabled beaches of Veradero converted to use by foreigners. Though U.S. tourists were still prohibited from visiting socialist Cuba by U.S. law, Canadians came to the beaches in the hundreds of thousands during the winter months and Europeans started to fill the hotels of Havana and other major cities.

In 1994 the unofficial dollar economy functioning in Cuba was legalized and tourists freely used the dollar currency for purchases. At the same time, Cuba issued an early version of the CUC, with statues of revolutionary heroes on the obverse and the colorful national emblem of Cuba on the reverse. The CUCs were generally not well received at first, but the boom in tourism and the use of the dollar allowed Cuba to increase its supply of hard currency for use on the world markets.

The U.S. goal remained the destruction of the Cuban socialist economy. What better way to "prove" that socialism cannot work than by destroying that economy's ability to trade? In addition, U.S.-based Cuban counterrevolutionaries initiated armed attacks on hotels in Havana to discourage tourism. (One bomb killed an Italian visitor, Fabio di Celmo.} To further tighten the blockade in 1996, the United States passed the Helms-Burton Act. It authorized legal action against any non-U.S. companies doing business with Cuba, opposed Cuba's membership in any international financial organization and authorized legal action against any financial institution exchanging dollars with Cuba. The Clinton-era goal was to strangle the Cuban economy.

Cuban socialism survived this period of attack. As Cuba began to climb out of the Special Period, the Bush administration intensified its financial war attacks. Starting in 2004, the limits on fines which the U.S. could impose on foreign banks doing business with Cuba was raised dramatically, with a fine of $100 million assessed against the Swiss Bank USB for transferring U.S. dollar notes to Cuba. USB terminated its transactions with Cuba and paid the fine rather than risk its business operations in the United States.

Cuba responded immediately in 2004 by suspending all use of the U.S. dollar in the internal economy. A newly designed series of CUC notes was introduced, with newly added anti-counterfeiting features. New CUPs were also issued with anti-counterfeiting features, including an image of Celia Sanchez only visible if the bill is held up to the light. Possession of dollars or other hard currency by Cubans was not prohibited, but exchanging CUCs or CUPs for dollars without a penalty had to be done by November 8, 2004. After that time an additional 10% fee was imposed on all exchanges of U.S. dollars, a fee which remains in place in 2017.

Impacts of the Dual Currency

The number of visitors to Cuba from the United States has risen sharply since 2014, when President Obama announced the first steps toward an anticipated normalization of relations between the two countries. This step was taken by executive order, with no supportive legislation from Congress. Further executive orders eased travel restrictions on U.S. citizens visiting Cuba, particularly for Cuban Americans, increased the amount of money U.S. citizens could bring to and spend in Cuba and removed the limits on the amount of remittances Cuban-Americans could send to their relatives on the island.

Visitors quickly see the impact of the CUC. The increased arrival of U.S. dollars, transformed into CUCs, comes at a time when the economic reforms initiated within Cuba encourage the establishment of small businesses, particularly restaurants and home rentals, catering to tourists. It is impossible to ignore the changes in Havana. New restaurants are constructed on empty lots, financed by money sent as remittances. Some argue that estaurants with CUCs crowd out the food market for the best products. Cubans within the tourist industry or on its edges benefit from personal access to CUCs.

Income inequality is growing within a society which took pride in providing for all its citizens. The demographics of those visiting Cuba and those sending remittances are not the same as the demographic of Cuban citizens, with remittances in particular flowing disproportionately to white-skinned Cubans. Afro-Cubans feel the most pain from the growing systemic inequality.

When CUCs were first introduced, efforts were made to utilize them to harvest hard currency from tourists while maintaining social equality in civil society. A ticket for a baseball game, for example, might be 3 pesos. A Cuban citizen would be charged 3 CUPs while a tourist would be charged 3 CUCs, thus using a fixed price to charge an appropriate additional amount for visitors. This benefits the budget of the public sector. But an additional long-term impact of the CUC has been to reward those Cubans who can obtain them.

Other impacts are not as visible. One might assume that Cuba's increased ability to harvest U.S. dollars when they enter the island would increase the purchasing power of Cuba in the international markets. But neither Congress nor the Obama administration took any steps to allow Cuba to freely use dollars in transactions with other countries. Congressional mandates established by the Torricelli Act and the Helms-Burton Act continue to empower the U.S. Office of Foreign Assets Control (OFAC) to impose fines on foreign banks handling dollar transactions with Cuba.

OFAC regulations are set forth and implemented through Cuban Asset Control Regulations, 31 CFR part 515. Many U.S. citizens assume that the blockade of Cuba was lifted by President Obama. Not so. As late in his term as January 13, 2017 OFAC announced a settlement with the Canadian Toronto-Dominion Bank for payment by the bank of $516,505 for 167 alleged violations of 31 CFR section 515, engaging in dollar transactions with Cuba.

Judith Lee of the Washington, D.C. law firm Gibson, Dunn and Crutcher commented on an earlier settlement by one of Gibson's clients, the French bank BNP Paribas, that "the U.S. Treasury Department has been relying on these banking-related sanctions more frequently. In particular, the sanctions influence the decision-making of foreign financial institutions by forcing them to make a choice: Either do business with the targeted country or do business in the United States. It's no surprise then that - given their success – OFAC has employed these measures against Cuba, hoping to further increase the pressure on that country."

These policies have continued under the Trump administration. On June 8, 2017 OFAC imposed a fine of $87,225 on American Honda Finance Corporation for violations of 31 CFR 515, including the act of providing financing for a car for the Cuban embassy in Ottawa, Canada. On June 16, 2017 Trump declared that he was "canceling" the Obama Administration's opening to Cuba, primarily cutting back on the ability of U.S. citizens to visit the island on their own, while leaving all other aspects of the blockade intact. Further restrictions may be imposed.

The net effect of current U.S. financial regulations is to foster inequality within Cuba while using international financial sanctions to impede the efforts of the Cuban government to use U.S. dollars to acquire goods and products in the international market.

A third impact of the dual currency dilemma is virtually invisible to foreign visitors. The exchange rate of CUCs to CUPs utilized within the system of socialist state enterprises distorts the statistics generated within the Cuban economy. According to Juan Triana Cordovi of Havana University, "The entire state sector operates with the rate of 1 CUC equal to one CUP. Here the Cuban peso is overpriced and it is a harmful exchange rate for the efficiency of the state sector." Yet the exchange rate between other sectors is not the same. Hotels and food suppliers use an exchange rate of 1 CUC to 11 CUPs, and the exchange rate at the port of Muriel has varied from I CUC equals 10 CUPs to 1 CUC equals 2 CUPs.

Professor Triana goes on to note, "In my opinion, the most strategic measure would be to unify these exchange rates and conversion factors within the socialist state business sector. This is the dominant sector that employs over 3 million workers and produces 85% or more of the national economy. Today, because of the distortion in the rate of exchange, it is impossible to know who operates efficiently and who does not."(see On Cuba magazine, May 13, 2016.)

This distortion becomes more complex when Cuba engages in foreign trade. If it sells Cuban-made products overseas, those products sell for hard currency, the domestic equivalent of CUCs. But if the raw materials necessary to manufacture that product are provided to the enterprise with a CUP valuation, how then are the proceeds distributed? Typically the enterprise receives a share of the hard currency proceeds in CUPs, with the excess value utilized to provide for the social services of the state economy. This helps alleviate income inequality, but it makes it almost impossible to determine the efficiency of the state sector.

Plans for a Unified Currency

Discussion about unifying the Cuban peso currencies began in earnest at the Party Congress in 2011. In October of 2013 the government announced that the council of ministers had approved a timetable for implementing measures "that will lead to monetary and exchange unification." The announcement anticipated a gradual process, but there was mention of an 18 month transition. That timetable has been considerably delayed.

There are many Cuban economists who argue that the key issue is the rates of exchange between the CUC and the CUP more than the dual currency impact on foreign visitors, but clearly, if there were no dual currency there would be no discussion of the rate of exchange. Identified as a major distortion of the economy and described by Raul Castro as “one of the most important obstacles to the progress of the nation,” the problem remains unsolved.