

Cuban Integrated Financing Framework (CIFFRA)



POLICY NOTE No. 6 FINANCING GAP COSTING



Financing gap costing

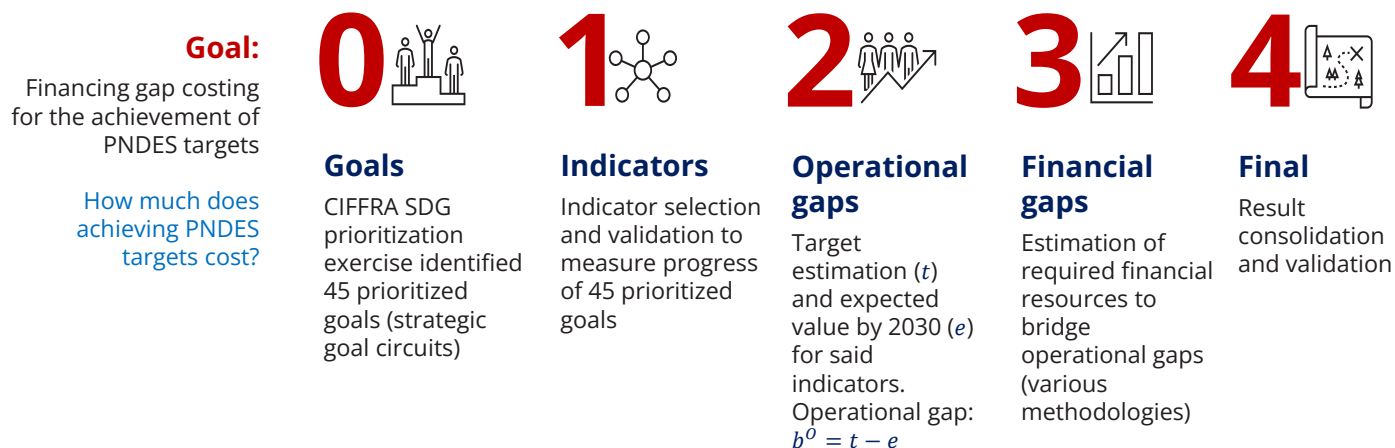
One of the activities carried out as part of the Joint Program “Support for the development of an Integrated National Financing Framework for SDGs in Cuba” (CIFFRA), was an exercise to estimate financing gaps for the achievement of the targets of the 2030 National Economic and Social Development Plan (PNDES 2030), which is aligned with the 2030 Agenda. Said estimation allows for a better understanding of development financing challenges, facilitates the dialogue on PNDES targets, while providing inputs, in combination with other financing source availability assessments (see *Policy Note No. 2*), for the design of an integrated financing strategy.

To that end, the Economic Commission for Latin America and the Caribbean (ECLAC) created a team led by Abelardo Medina, international expert on tax issues and financing gap costing. With the support of the Foundation for Innovation and Development of the University of Havana, six national experts joined the team for each of the PNDES axes: José Luis Rodríguez, Luis del Castillo, Anicia García, Wenceslao Carrera Doral, Silvia Odriozola Guitart, and Joel Ernesto Marill.

With this work, guided by the methodology proposed by Abelardo Medina (see diagram 1), they set out to answer the question: how much does achieving PNDES targets cost? The 45 prioritized goals identified during the SDG Prioritization exercise carried out under CIFFRA (see *Policy Note No. 3*) were used as starting point.

Diagram 1

Cuba: proposed methodology for the financing gap costing exercise



Source: Authors.

On that basis, four essential steps were followed: (i) selection and validation of indicators to measure the progress in those 45 goals; (ii) definition of targets for indicators, estimation of their expected values by 2030 and estimation of operational gaps (difference between targets and expected values); (iii) estimation of financing gaps (financing required to bridge operational gaps); and (iv) consolidation and validation of results. As a result of the process, 189 indicators were established to monitor the 45 PNDES prioritized goals. Out of which, 102 (54.0%) are directly linked to the 2030 Agenda, although the rest are indirectly linked, given the high convergence that goals and implementation terms of both planning tools have. Likewise, said indicators were assessed to determine whether they met the SMART¹ criteria, and 152 (80.4%) of them, did.

Once SMART indicators were identified, national consultants held various meetings with the Technical Secretariats of Macroprograms. During said meetings, indicators and their targets were narrowed down, consolidated and validated. Similarly, productive discussions were held on the importance of the creation of a system of metrics for PNDES design, implementation, monitoring and evaluation. Once the final list of 152 indicators was ready, consultants estimated operational gaps: the difference between calculated trend values and estimated 2030 targets (efforts the country shall make to achieve PNDES planned goals). Finally, and as a result of financing gap estimation exercises, it was estimated that the preliminary amount of resources required to bridge operational gaps during the 2022–2030 period was 55.1 billion dollars (see table 1).

Table 1
Cuba: financing gaps, 2022-2030

Axis	Gap (millions of dollars)	Gap (millions of Cuban pesos)	Percentage
1. Government, institutionality and macroeconomy	114.1	2 740.0	0.2
2. Productive transformation and international integration	19 434.6	442 431.3	33.4
3. Infrastructure	16 276.6	390 639.3	29.5
4. Science, technology and innovation	6 943.4	166 641.2	12.6
5. Natural resources and environment	11 797.5	281 700.7	21.3
6. Human development, equity and social justice	1 620.4	38 888.5	2.9
Total	55 126.7	1 323 041.1	

Source: Authors.

The preliminary assessment of financing gaps showed that key investments are concentrated in the strengthening of the general and sectoral productivity of the economy (competitiveness), the development of infrastructure, and in research, development and innovation (R+D+I). The 75.6% of the overall investment demand is concentrated in these three areas alone (see table 1), which is consistent with evidence of other developing countries.

¹ Methodology that makes it possible to assess the efficacy of a goal on the basis of five parameters: Specific, Measurable, Achievable, Relevant and Time-bound.

The expressed environmental interest in the PNDES design and the alignment of its goals with the 2030 Agenda, account for the high investment in this area (21.3%).² On the other hand, the limited increase suggested for social expenditure (2.9%), may be driven by three factors: (i) the crosscutting impact that investments in other areas (infrastructure, sectoral, R+D+I) may have in the living standards of people, through their impact on productivity and national revenues; (ii) high initial levels in the country (existing infrastructure and human capital); and (iii) reliance on less resource-intensive policies (institutional design, training, consensus building).

The exercise faced barriers that should be corrected in future updates. Firstly, the combined impact of the pandemic, the stepping up of the US blockade and accumulated internal imbalances seriously distorts the trajectory of key variables. Secondly, the implementation of the Monetary Overhaul brought about disruptions in the series of national accounts, which limit their relevance for the estimation of future values. Lastly, the lack of a general balance model makes it difficult to identify synergies between incorporated resources and processes and achieved results, as well as possible duplications.

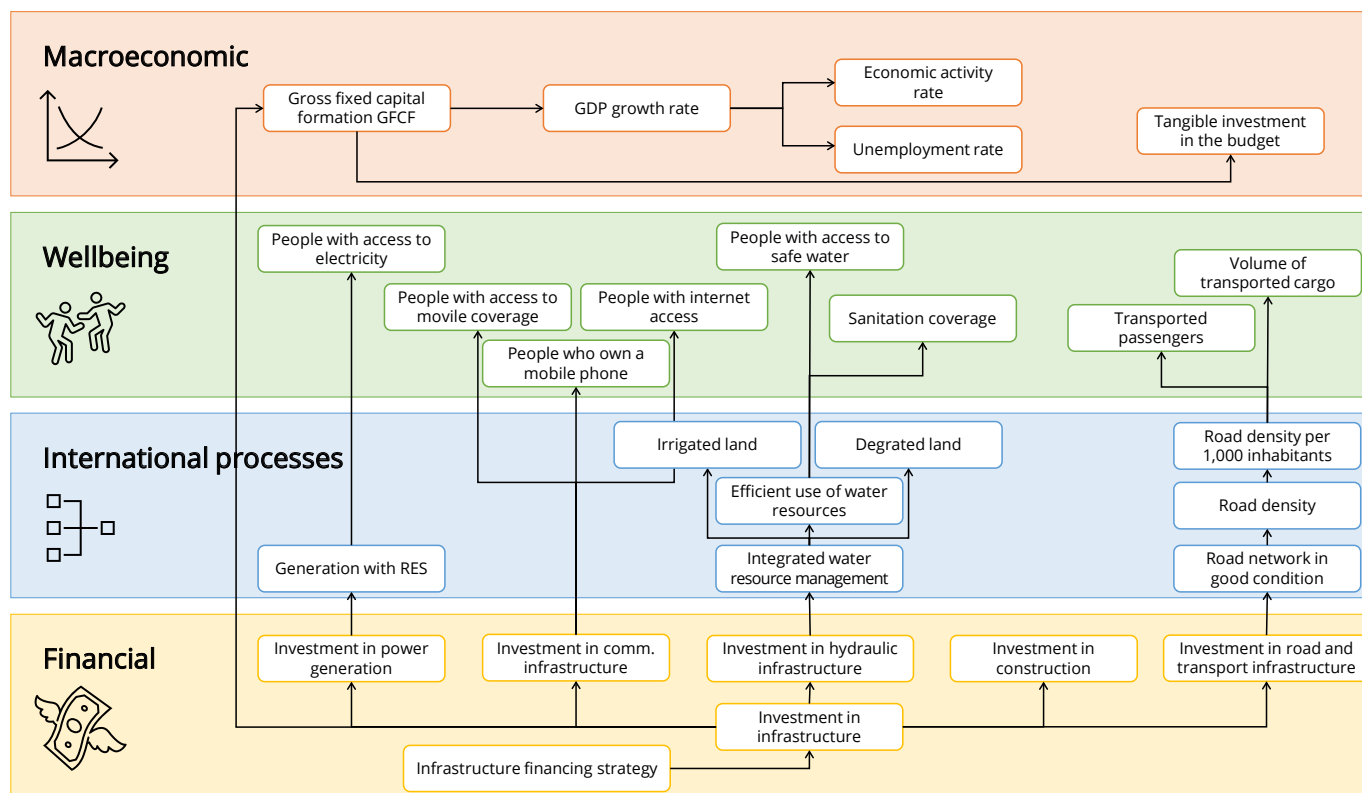
On the basis of these limitations, the following assumptions were made: (i) no consideration was given to the specific GDP increase dynamics and the multiplier effect of new investment on production; (ii) production processes are carried out with optimal efficiency (efficiency reserves derived from possible process reengineering were not taken into account); (iii) in most cases, maintenance expenses are not included, due to lack of available statistics; and (iv) the economy will first transition to the post Covid-19 crisis recovery period, therefore, although annual increases are projected up to 2030, the greatest advance is seen in the last five-year period (2026–2030).

Despite assumptions made could lead to possible under- or overestimations, the exercise is a relevant opportunity for Cuban authorities. It provides a baseline methodology and exercise that could be updated regularly. Likewise, key challenges for the improvement thereof were identified: (i) review of statistic tools and databases; (ii) adjustment and validation of targets and indicators; (iii) incorporation of maintenance cost estimations; (iv) process reengineering study, when appropriate; and (v) design of a general equilibrium model and sectoral equilibrium models, to verify identified cause-effect relations and optimize the information resulting from the set of indicators.

Additionally, with the exercise, the implementation of three tools for the use of metrics and indicators in PNDES frameworks and financing strategy is proposed: (i) set of diagrams of goal connections, establishing connections among indicator families (direct investment, immediate results, impact on people and macroeconomic results); (ii) grouping indicators per financing family, as a means to identify available financing sources; and (iii) bases for the creation of a Balanced Scorecard to monitor the fulfillment of the PNDES (diagram 2 shows an example for infrastructure investment).

² The estimation does not include the expected values of potential material losses as a consequence of the impact of extreme weather events, as their occurrence is uncertain. However, they are an element to be considered by authorities.

Diagram 2
Balanced scorecard - infrastructure investment



Source: Authors.

The exercise concludes with the presentation of a series of recommendations, including: (i) estimating financing sources required to bridge financial gaps; (ii) creating a specialized technical team to follow up and monitor PNDES and 2030 Agenda indicators; (iii) training public employees on the development and use of targets and indicators; (iv) deepening the dialogue for the update of targets and indicators with various stakeholders and the support of national consultants; (v) assess the impact of PNDES implementation on economic growth, employment, income and wellbeing; and (vi) carry on with the PNDES - 2030 Agenda strategic alignment process.

The report allows for additional interpretations of development financing challenges in Cuba. Firstly, estimated financing requirements to achieve development goals nearly double the country's growth and investment capabilities.³ Hence, not all PNDES goals can be advanced, particularly in the current scenario. It is imperative to prioritize targets, while reducing financing needs increasing the productivity and efficiency of the economic mechanism.

³ For the exercise the following macroeconomic initial assumptions were used: 5% real GDP increase and an average 22% accumulation rate between 2025 and 2030. Up to 2024, a post Covid-19 crisis recovery period is assumed, on the basis of EIU (2021). Under this scenario, total investments from 2022 to 2030 would reach 31.775 MMUSD.

Secondly, Foreign Direct Investment (FDI) emerges as the main financing source as it does not create new imbalances, taking into account existing public and foreign debt levels, as well as the limited availability of other financing sources (both in terms of volume and timeliness). Assuming FDI will cover 60% of investments required to achieve PNDES targets, it would still be necessary to attract capital five to nine times higher than the average levels secured in the last five-year period. Therefore, it is essential to continue working on institutional transformations to attract foreign capital and make an objective assessment of the potential FDI flow in the current international context.

CIFFRA Technical Committee
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