

Cuban Integrated Financing Framework (CIFFRA)



POLICY NOTE N° 18 MEDIUM TERM BUDGETARY FRAMEWORK

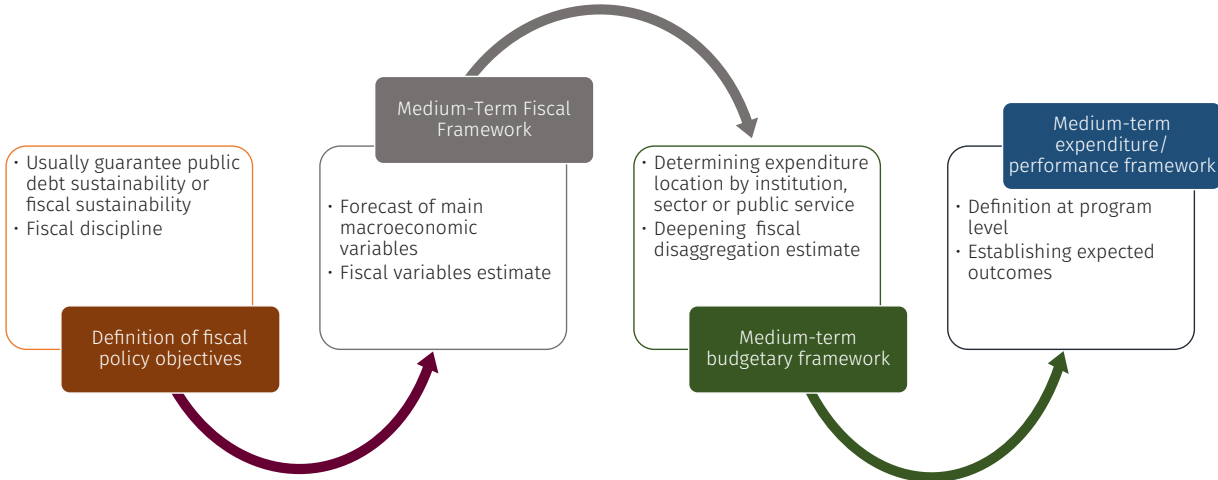




Several of the exercises of the Joint Program “Support for the development of an Integrated National Financing Framework for the SDGs in Cuba” (CIFFRA) recommended moving towards the modernization of public finance management. Given the restrictive access to international financing faced by the country, this process is key to promoting better use of domestic financing sources.

Accordingly, a Medium-Term Budgetary Framework for the period 2023 - 2026 was developed as part of the broader objective of developing a medium-term fiscal planning framework (see diagram 1.) The tool –implemented for the first time in the country– not only allows an evaluation of medium-term fiscal scenarios and their interrelation with the national development strategy, but also the training of public officials in its use and adaptation to Cuba’s specificities.

Diagram 1
Cuba: medium-term fiscal planning framework

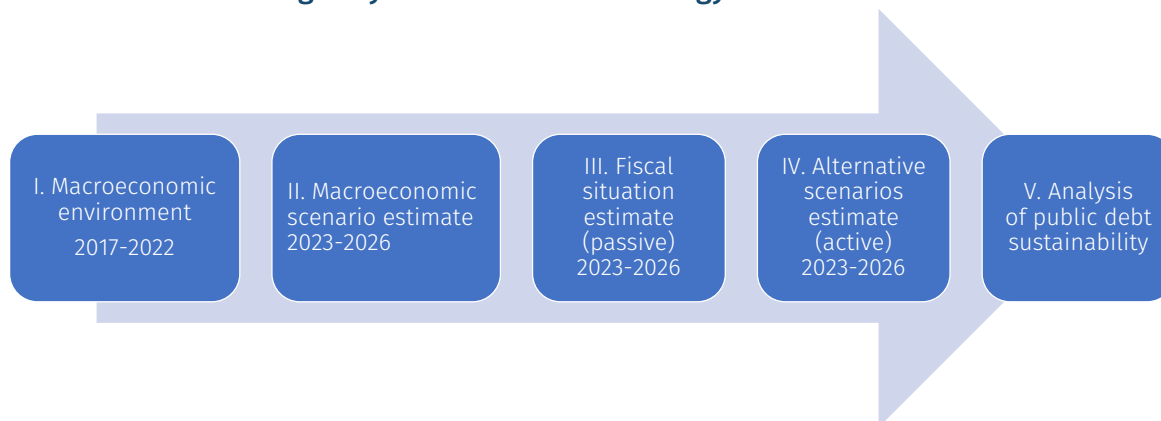


Source: Author’s own elaboration.

This first exercise includes an evaluation of the Cuban public finances trajectory, assuming that the current fiscal policy and accommodating conditions stay in place after the implementation of the monetary

overhaul,¹ as well as a review of the potential fiscal effects of incorporating some of the programs and projects of the 2030 National Economic and Social Development Plan (PNDES, its Spanish acronym.) The exercise was carried out using the methodology proposed by Dr. Abelardo Medina Bermejo, ECLAC consultant (see diagram 2).

Diagram 2
2023-2026 Medium-Term Budgetary Framework: Methodology



Source: Author's own elaboration.

The purpose of the exercise is to provide a scheme of sustainability to Cuban public finances, while catering to the needs of the population and strengthening the country's productive capacity. To this end, the exercise included a thorough analysis of the macroeconomic and fiscal context by: (i) describing Cuba's economic and fiscal situation for the 2017-2022 fiscal period; (ii) estimating the behavior of Cuba's macroeconomic variables for the 2023-2026 period; (iii) estimating fiscal variables for the 2023-2026 period in a passive scenario; and (iv) assessing the sustainability of Cuba's public debt in the medium term.

As with other quantitative exercises carried out as part of CIFFRA, the main challenge was data management. On the one hand, the Monetary Overhaul implied structural changes in many of the series used, which limited the ability to estimate future behavior. On the other hand, the deep external shocks that impacted the economy between 2019 and 2021 (increased U.S. sanctions, the crisis caused by the Covid-19 pandemic and the conflict in Eastern Europe), made the use of these years as a reference even more complex. Accordingly, inputs from public institutions were used and analyses were carried out with national and ECLAC experts who helped validate the assumptions made.

In addition, by eliminating the dual exchange rate distortions on the main macroeconomic and fiscal aggregates, the Monetary Overhaul enabled the transparency of many of the macroeconomic and fiscal aggregates and ensured better analysis and international comparability. This is particularly noticeable in the relative reduction of public spending and the tax burden, which is not essentially due to the impact of external shocks, but rather to the calculation of GDP² under the new conditions.

¹ Monetary unification process carried out in 2021 which, among other measures, eliminated the circulation of one of the national currencies (CUC), devalued the exchange rate of the state sector thus unifying the different existing exchange rates, and carried out profound transformations in pricing mechanisms and wages.

² In the first year of the implementation of the Monetary Overhaul, the current GDP in dollars was adjusted by almost 5 times.

Likewise, the impact of the official exchange rate devaluation by 2,300% reduced the domestic debt, which went from accounting for 76.1% of GDP in 2020 to 26.7% in 2021. This makes it easier for authorities to manage the public debt, although the following two circumstances should be noted: (i) the high fiscal deficit levels reached since 2015 (if this trend continues, the domestic debt could reach unsustainable levels); and (ii) the high foreign debt.

After estimating the passive scenario, two active scenarios were estimated: (i) recomposition of public spending to modify the subsidy scheme (from subsidizing products to subsidizing people); and (ii) inclusion of resources needed to finance the infrastructure investment foreseen in the PNDES in the spending plan up to 2026 (previously estimated through the financing gap costing exercise)³.

As a complement to the exercise, an analysis of the sustainability and vulnerability of the domestic public debt⁴ was carried out based on 7 indicators, both for the passive and active scenarios. At the same time, the different scenarios were compared and the main fiscal risks (specific internal risks, specific external risks, macroeconomic risks) for the period were defined.

The main conclusion of the exercise is the need to find solutions for public debt sustainability. It is not possible to maintain the country's spending on social policies and programs linked to the national development strategy (PNDES), without increasing revenues, improving efficiency in the use of public resources, and recomposing spending (but it should be said that there is not much room for maneuver.) Without mobilizing new funds, it is not possible to incorporate PNDES programs or apply wide-ranging social compensators, since it will entail the loss of fiscal sustainability and the exponential increase of the debt.

Accordingly, the exercise concludes with the following recommendations:

- ▶ consider the use of other active estimation alternatives for the 2023-2026 period;
- ▶ incorporate information related to foreign debt service;
- ▶ implement a wide-ranging tax reform to adjust the tax system to the new context, especially the diversification of economic actors (SMEs, cooperatives, individual farmers, self-employed workers, etc.);
- ▶ enhance the use of electronic and control mechanisms for cash transactions,
- ▶ clearly establish who will be in charge of managing fiscal resources and define their responsibilities,
- ▶ estimate the budget ceilings for each reporting entity and the expected results of the use of such funds (introduction of a results-based budgetary system and measurement of the impact of using those public resources); and
- ▶ allocate resources to each administrative unit using a project-based and program-based approach, in order to improve accountability mechanisms.

CIFRA Technical Committee – November 17, 2022

³ See policy note 6: Financing Gap Costing [on-line] <https://www.cepal.org/es/marco-integrado-financiamiento-cuba-cifra>.

⁴ Public foreign debt was not taken into consideration since there was not sufficient information available to estimate these indicators



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