



Investment and resource allocation

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Outline

- Theoretical aspects
- The Cuban case
- Final remarks



Investment and economic growth

- Increases capital stock
- Improves returns to other factors of production
- Assimilation of new technologies and knowledge, embodied technical change, Fisher (1965)
- Changing the investment composition delivers structural change
- May help tackling infrastructure bottlenecks



Investment efficiency

- Most studies assume full efficiency of investment
- Full efficiency: actual accounting cost of investment passes into the value of capital
- Result: literature is skewed to studies related to increasing investment levels



The basic (and wrong) assumption

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$$K_{t+1} = \gamma I_t + (1 - \delta)K_t$$

full efficiency means that

$$\gamma = 1$$

Evidence for developing countries

(Agenor, 2010) shows that it goes from 0,4-0,6



Determinants of investment efficiency

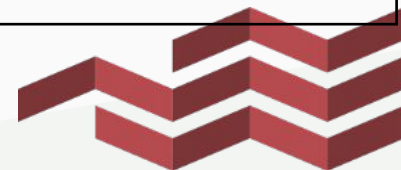
- Requirements in the four phases of investment management: strategic guidance, project selection, implementation and evaluation
- Systemic failures:
 1. Resource allocation mechanism
 2. Performance of the construction sector



Indicators related to investment efficiency, Cuba (2000-2013)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Returns on investment	0.80	0.71	0.73	-	-	-	-	-	-	0.58	0.48	0.46	0.73	0.55
Investment plan fulfillment ratio (%)	70.2	70.8	74.4	77.6	70	53.5	50	75.4	75.2	78	-	-	-	-

Source: Own calculations based on reports from the addresses of the Ministry of Economy and Planning at the National Assembly (several years).



Cuba: investment management

- Several studies have found different problems (Villar y Rodríguez, 2012):
 - Inadequate methods
 - Low quality of necessary information
 - Low availability of relevant data
 - Lack of appropriate skills by the personnel



Cuba: resource allocation mechanism

- Main institutions
 - Annual plan
 - Government budget
 - Paralell budget for foreign cash
 - Dual monetary and exchange scheme
- Other
 - Financial system
 - Informal sector



Performance of the construction sector

- Technological gap
 - Labor saving equipment
 - Esquemas ahorradores de trabajo
- Scarcity of labor force
- Insufficient experience for frontier projects:
Large infrastructure projects, ICT, etc.



Recent changes

- Rebalancing of the investment priorities towards productive projects
- Renegotiation of foreign debt
- New FDI Law
 - Mariel initiative



Recent changes

- More decision making power to the firm
- New regulations for the investment process
- New credit policy



Two emerging dynamics

- Accumulation in the private and cooperative sectors
 - Market based decisions
 - Informal and foreign originated funding
- US policy
 - Lessening of financial sanctions
 - Scenario of normal ties now likelier than ever
 - **Cuba as a less risky country**



Policy alternatives

- Macroeconomic conditions
 - Monetary system and price setting
 - Agents with real decision making power
- New resource allocation mechanism
 - More active role from the financial system
 - New logic behind planning:
 - strategic character
 - inclusive of all agents
 - policies and incentives rather than administrative tools



Last remarks...

1. It's not only about resources, but also how they are used is important
2. Lower than expected returns on investment imply:
 - a) Balance of payments crisis
 - b) Less resources available for the next period
3. Central plan: ¿stricter enforcement or new plan?
4. A more challenging new scenario

