COMMENTS ON

"Financing the Economic Reconstruction of Cuba While Rebuilding the Financial Sector: Perspectives on Development Banking" by Manuel Lasaga

Ricardo C. Martínez 1/

This paper looks into one of the thorniest, and most crucial, subjects in the study of economic development, namely the role of financial intermediation, or of how the financial system transforms a country's savings into the flow of investment that the economy needs in order to grow and develop. Mr. Lasaga adds complexity to this issue by looking at it in the context of a future Cuban economy in transition from Marxism to a free-market system. In my view, three issues raised by this paper merit further exploration.

The *first issue* can be viewed as a version of that old riddle of folk wisdom: "who came first, the chicken or the egg?" This is because the author's proposal for rebuilding Cuba's banking system features a first phase in which a new, mixed, state/private entity—the proposed development bank named BANFOR—would provide most financial intermediation services in the economy, thus allowing a privately owned banking system to develop, strengthen, and ultimately, in phase II, take over the main intermediation role in the economy. On the other hand, the description of the BANFOR entity itself often refers to functioning private financial institutions, and even to a capital market, as essential in the organization and early functioning of BANFOR. So which came first, the chicken or the egg?

Actually, the riddle in this case may be more apparent than real. This is because Mr. Lasaga's paper makes very little reference to the financial system which exists under Castro's dictatorship. Whatever the constitution and functioning of that system are now, it will necessarily have to provide one of the few building blocks available for the transition. For example, existing branches of the Cuban central bank, suitably reorganized, and possibly privatized, could be the origin of a commercial banking system, even during "Phase I" in Mr. Lasaga's definition. In any case, this topic is worth exploring in greater depth, prefaced by a brief explanation of the organization and functioning of the country's existing financial system.

The *second issue* is that Mr. Lasaga's paper has very little to say about the role that foreign banks and financial intermediaries could play in the Cuban transition. These entities could make critical contributions of capital and technology in phase I of the transition, when the new Cuban commercial banks would still be in embryonic form. This is particularly true of the multinational banks, which have experience operating in a wide variety of countries and conditions. However, two problems come to mind with respect to these institutions:

1/ The views expressed in this comment are entirely and solely the author's, and should in no way be construed to represent the views of the Inter-American Development Bank, its Governors, Management, or staff.

1. Can they be persuaded to come in, given the high level of risk involved in an early entry into the Cuban market, and, if so, how?
2. If they in fact do come in, how can the country avoid their using their vast resources and advanced technology to prevent domestic competitors from growing? (It is assumed here that the national objective would be to develop Cuban-owned financial institutions to the point where they have the lions's share of the country's financial market).

The *third issue* refers to government policy. After a critique of various approaches to structural reform of the economy of the paper discusses the economic policy guidelines which the author deems advisable for the development of the financial sector. It is remarkable that the list omits both fiscal policy, particularly taxation and deficit financing, and monetary policy, with the exception of interest and exchange rates. Both of these sets of policies would very directly affect the development and role of the financial sector. The core issue in this regard boils down to two related questions: (a) what is the best macroeconomic policy framework for the development of the financial system?; and (b) what role will the financial system itself play in that same framework? This paper is not quite definite about answers to either question.

In *summary*: these comments have dealt mostly with issues which were not, in my opinion, sufficiently discussed in Mr. Lasaga's paper, but which would have enhanced that work if they had been so taken up. As it stands the paper makes a very useful contribution to understanding the difficulties a future Cuban economy in transition would face in building up a new financial system, suitable for its growth and development. One final *caveat*: in a paper that deals with a subject as complex as this one is, a "summary and conclusions" section would have been very useful.