



THE CUBA-VENEZUELA ALLIANCE: The Beginning of the End?

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The turmoil of the last several months in Venezuela has raised again the prospect of a post-Chavista regime in Caracas and what that may entail for its closest ally in the region, Cuba. This policy brief takes an updated view of the relationship in light of recent developments and concludes that both countries have much to gain from reducing their mutual dependence, which is based on a highly subsidized economic and political relationship. A reduced Cuban presence in Venezuela would give Venezuelans more control of their own democratic destiny. Likewise, a gradual reduction in Venezuelan assistance to Cuba would bolster the case for further economic restructuring and diversification of its international partners. Washington should use its advantageous position as a growing energy producer to help loosen the ties that bind Cuba and other neighbors to Venezuela's oil largesse.

BACKGROUND

In the past decade, Venezuela and Cuba have become close allies both economically and politically. Venezuela provides deeply subsidized oil supplies to Cuba in return for doctors, teachers, sports trainers

and military advisors. In addition, Venezuela's former president Hugo Chávez professed deep admiration for Fidel Castro and the Cuban revolution, stating that Cuba was 'the sea of happiness' toward which Venezuela should navigate. The two leaders' bond was highlighted by Hugo Chávez's decision to spend the final months of his life under Cuban medical supervision, conducting Venezuelan government business and holding cabinet meetings in Havana until his death in March 2013.

While Cuba and Venezuela have become increasingly interdependent since Hugo Chávez took office in 1999, the relationship is asymmetrical. Economically, Cuba is more dependent on Venezuela as their bilateral trade in goods and services amounted to 20.8 percent of Cuba's GDP in 2012 yet only 4 percent of Venezuela's GDP.² Politically, Venezuela is more dependent on Cuba, not only for the doctors, teachers and other professionals who staff social missions that sustain the government's popularity, but also for the intelligence and military advisors that train the Venezuelan security services and monitor dissent and conspiracies against President Nicolás Maduro's administration.³

¹ We would like to thank Ashley Miller and Emily Miller for outstanding research support and editorial advice during the preparation of this policy brief. We would also like to thank Richard Feinberg for his comments on an earlier draft of this brief. Any errors and omissions are the responsibilities of the authors alone. All statistics are drawn from official sources where possible, including Oficina Nacional de Estadística e Información de Cuba, Banco Central de Venezuela, Ministerio del Poder Popular para la Energía y Petróleo, Instituto Nacional de Estadística de Venezuela, International Energy Agency, U.S. Energy Information Administration, and the World Bank.

² Calculations for the bilateral trade in goods and services follows the methodology used in Pavel Vidal Alejandro, *Proyecciones macroeconómicas de una Cuba sin Venezuela*, Desde La Isla (Cuba Study Group, 2014), www.desdelaisla.org, using 2012 data measured in current prices. In this calculation, Cuban services sent to Venezuela are estimated at 73 percent of total services exported, excluding international tourism revenues, as per Carmelo Mesa Lago, *Cuba en la era de Raúl Castro. Reformas económico-sociales y sus efectos*, (Madrid: Editorial Colibrí, 2012), 135.

³ Carlos A. Romero, *South-South Cooperation between Venezuela and Cuba*, Special Report on South-South Cooperation, South-South Cooperation: A Challenge to the Aid System? (Reality of Aid Network, 2010), <http://www.realityofaid.org/wp-content/uploads/2013/02/ROA-SSDC-Special-ReportEnglish.pdf>; Kevin Ginter, "Truth and Mirage: The Cuba-Venezuela Security and Intelligence Alliance," *International Journal of Intelligence and CounterIntelligence* 26, no. 2 (2013): 215-40.

Until 2013, the negative aspects of Cuban-Venezuelan interdependence were not as salient in their bilateral relationship. Venezuela could afford the economic cost of support to Cuba during a decade of rising oil prices, and the Cuban and Venezuelan governments were ideologically aligned under the leadership of Hugo Chávez and Fidel Castro. The personal and political solidarity between the two leaders mitigated the vulnerabilities created by interdependence.

The economic and political crisis in Venezuela in 2014, however, highlights the downsides of their close relationship for both countries. Venezuela experienced inflation greater than 50 percent, shortages of nearly 30 percent of essential consumer goods in retail outlets, and a fiscal deficit of 15 percent at the end of 2013.⁴ Inflation and scarcity have worsened during the first six months of 2014. Under these circumstances, the economic cost of Venezuela's support for Cuba becomes an increasingly important constraint on the Maduro administration. On the other hand, instability in Venezuela serves as a reminder to the Cuban government of the risks associated with interdependence.

The Cuba-Venezuela alliance has also had important implications for inter-American relations. Together, the two countries have formed a coalition of states in the Western Hemisphere, the Alianza Bolivariana para los Pueblos de Nuestra América (ALBA), which has consistently supported a regional agenda that excludes and demonizes North America. ALBA is highly influential in the Caribbean and Central America largely due to Petrocaribe, a program by which Venezuela has extended the privileged oil relationship it started with Cuba to 16 other states.⁵ Cuba and Venezuela have also been able to convince other states in the Americas to deemphasize the hemispheric agenda in favor of new multilateral forums focused exclusively on

Latin America, such as the Community of Latin American and Caribbean States (CELAC), and (even though it does not include Cuba) the Union of South American Nations (UNASUR). Together, this strategy has neutralized the Organization of American States and other inter-American institutions that once sustained a hemispheric agenda, particularly in the area of human rights and democracy. In the most dramatic example of this tension, most Latin American states are threatening to skip the next Summit of the Americas in 2015 if Cuba is not invited, despite its failure to meet the democracy-related criteria for participation in the group.

This policy brief will first establish the degree of Cuba and Venezuela's mutual interdependence. It will then analyze the implications of close political and economic relations for each country and for the United States. It will conclude with recommendations for U.S. policy toward Cuba and Venezuela.

CUBA AND VENEZUELA: A RECENT HISTORY OF GROWING INTERDEPENDENCE

In a historical context, Cuba and Venezuela's partnership is a recent phenomenon. Relations between the two countries were poor for decades after the Cuban revolution due to Venezuela's refusal to provide economic support to Fidel Castro after 1959 and Cuba's support for Venezuelan left-wing insurgents in the 1960s.⁶ Relations normalized in 1974, but this was not followed by close political and economic ties until after Hugo Chávez was elected president of Venezuela in 1998.

It was the personal relationship between Hugo Chávez and Fidel Castro that drove Cuban-Venezuelan interdependence, rather than any economic or trade-based affinity between the countries.

⁴ Harold Trinkunas, "Venezuela Breaks Down in Violence," in *Big Bets & Black Swans: A Presidential Briefing Book* (Washington DC: Brookings Institution, 2014), 38–40, http://www.brookings.edu/~media/programs/foreign%20policy/bbbs/bigbets_blackswans_2014.pdf.

⁵ Rachel Glickhouse, "Explainer: What is Petrocaribe?" Americas Society/Council of the Americas, May 20, 2013, <http://www.as-coa.org/articles/explainer-what-petrocaribe>.

⁶ Harold A. Trinkunas, *Crafting Civilian Control of the Military in Venezuela: A Comparative Perspective* (Chapel Hill: University of North Carolina Press, 2005).

Hugo Chávez had been an admirer of the Cuban revolution since he was a teenager. He developed a deep friendship with Fidel Castro after spending time in Cuba after his release from a Venezuelan prison following a failed coup attempt in 1992. The Cuban-Venezuelan relationship was buttressed by civilians from Venezuela's left that Chávez brought into his political movement and his government, a number of whom had been part of the pro-Cuban insurgency of the 1960s.⁷

Cuba and Venezuela's interdependence has grown rapidly during the past 15 years, and it extends from trade and investment ties, to military and security assistance, to international diplomacy.

Trade and Investment

The centerpiece of Venezuelan-Cuban economic cooperation is the oil-for-services trade. Venezuelan oil sold to Cuba is heavily subsidized as only 60 percent is paid for in the first 90 days while the other 40 percent is financed at a one percent interest rate over 25 years.⁸ Venezuelan crude oil shipments to Cuba reached 38,000 barrels per day (bpd) by 2003, increasing to 97,000 bpd in 2008 under the terms of

Petrocaribe.⁹ Combined crude and refined oil product exports climbed to 104,000 bpd in 2012.¹⁰ By 2011 imports of crude oil from Venezuela made up 61 percent of Cuba's total oil supply.¹¹ For Venezuela, shipments to Cuba represented only 5.1 percent of total crude oil exports in 2011,¹² although this proportion has been slowly increasing across time due to the steady decline in Venezuela's production capacity resulting from a lack of investment in and maintenance of its oil industry.¹³

From Cuba, Venezuela receives professional services. By most accounts, there are 40,000 Cuban professionals in Venezuela, 75 percent of whom are health-care workers.¹⁴ Civilian personnel, such as doctors and teachers, are deployed as part of a network of social assistance programs in Venezuela known as *misiones*, focused on basic community health, sports, and literacy programs, which form the backbone of the Bolivarian movement.¹⁵ Venezuela reportedly pays the Cuban government approximately \$5.4 billion per year for the Cuban assistance.¹⁶ Since 2003, Cuba also provides advanced medical care for tens of thousands of Venezuelans in Cuba itself and hosts thousands of Venezuelan university students, particularly for the study of medicine.¹⁷

⁷ Alberto Barrera Tyszka and Cristina Marcano, *Hugo Chávez sin uniforme: Una historia personal* (Mondadori, Spain: Debate, 2005).

⁸ Rolando H. Castañeda, "La ayuda económica de Venezuela a Cuba: Situación y perspectivas ¿Es sostenible?," in *Cuba in Transition*, 19 (presented at the Nineteenth Annual Meeting of the Association for the Study of the Cuban Economy, Miami, FL, 2009), <http://www.ascecuba.org/publications/proceedings/volume19/pdfs/castanedavenezuela.pdf>.

⁹ Ministerio del Poder Popular de Petróleo y Minería (MENPET), *Petróleo y otros datos estadísticos 2009-2010*, 51st ed. (Caracas, Venezuela: Gobierno Bolivariano de Venezuela, 2012), 105.

¹⁰ *Informe de Gestión Anual 2012 de Petróleos de Venezuela* (Caracas, Venezuela: Petróleos de Venezuela, 2012), 90.

¹¹ Authors' calculations. Data on Venezuela's oil exports to Cuba were drawn from MENPET, *Petróleo y otros datos estadísticos 2009-2010*, 105 and Ministerio del Poder Popular de Petróleo y Minería (MENPET), *Memoria 2012*, (Caracas, Venezuela: Gobierno Bolivariano de Venezuela, 2013), 328. Data on Cuba's domestic oil production and total oil imports were drawn from the Anuarios Estadísticos published by Cuba's Oficina Nacional de Estadística e Información (ONEI). The International Energy Agency cites a greater level of Cuban oil imports beginning in 2009; this results in a lower estimate for the share of Venezuela's oil in Cuba's total oil supply (55% in 2011).

¹² Authors' calculations using data from *Informe de Gestión Anual 2012 de Petróleos de Venezuela*, 90.

¹³ Francisco Monaldi, *Oil and Politics in Venezuela*, Perspectives on the Americas (Miami, FL: Center for Hemispheric Policy, University of Miami, 2014), https://umshare.miami.edu/web/wda/hemisphericpolicy/Perspectives_on_the_Americas/Monaldi%20-%20Perspectives%202014.pdf.

¹⁴ Romero, *South-South Cooperation between Venezuela and Cuba*.

¹⁵ Total Venezuelan aid to Cuba is difficult to piece together as it consists of oil provided for joint ventures, concessional financing for oil purchased, and overpayment for professional services. The level of the subsidy has been estimated at \$9.97 billion in 2008 and \$7 billion in 2010, 16 percent and 11 percent of Cuba's GDP, respectively. Because of the uncertainties involved with these estimates, we prefer to focus on trade data and oil export data for which statistics are publicly available on a consistent basis. For estimates of Venezuelan aid to Cuba, see Romero, *South-South Cooperation between Venezuela and Cuba*; Ernesto Hernández-Catá, "Cuba, the Soviet Union, and Venezuela. A Tale of Dependence and Shock," in *Cuba in Transition*, vol. 23 (presented at the Twenty-Third Annual Meeting of the Association for the Study of the Cuban Economy, Miami, FL, 2013), <http://www.ascecuba.org/publications/proceedings/volume23/pdfs/hernandezcata.pdf>.

¹⁶ Carmelo Mesa-Lago, "El posible impacto de la muerte de Chávez en la economía cubana," *Cubaencuentro*, December 3, 2013, <http://www.cubaencuentro.com/cuba/articulos/el-posible-impacto-de-la-muerte-de-chavez-en-la-economia-cubana-283444>.

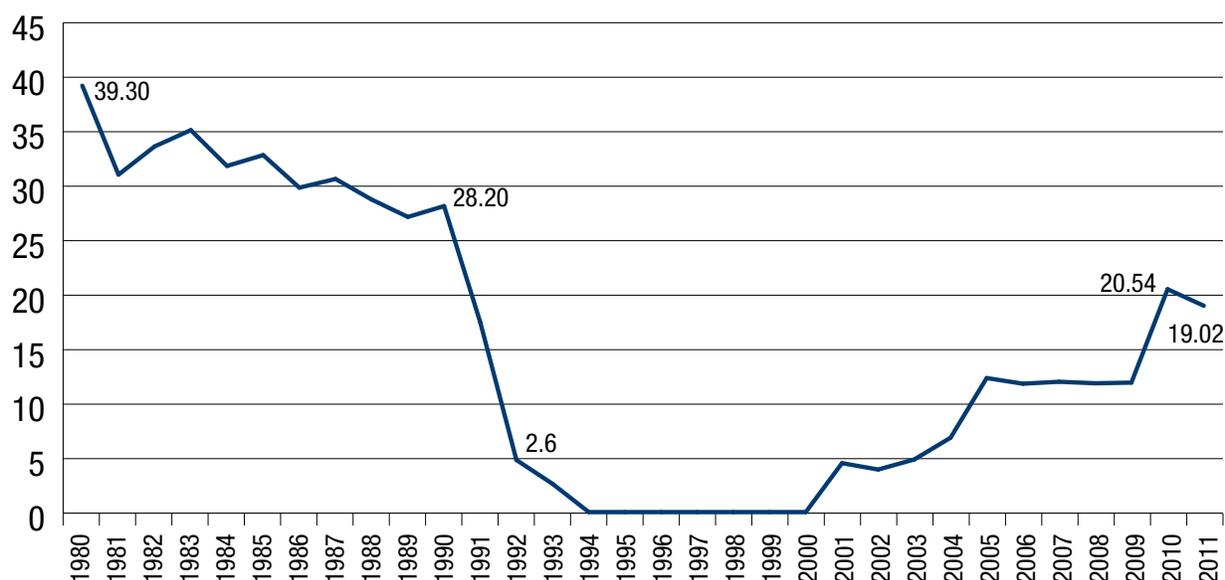
¹⁷ Michael J. Bustamante and Julia E. Sweig, "Buena Vista Solidarity and the Axis of Aid: Cuban and Venezuelan Public Diplomacy," *Annals of the American Academy of Political and Social Science* 616 (March 2008): 223–56.

It is important to keep in mind that Cuban professionals are paid much less than their government receives from Venezuela in payment for their services. As of 2010, Venezuela paid Cuba approximately \$11,317 per month on average for each professional it provided.¹⁸ By contrast, Cuban doctors reportedly receive \$425 per month, although this is more than double what they received six years ago and similar to what they earn on medical missions to Brazil.¹⁹ Cuban doctors would be earning only up to \$64 a month back home.²⁰ It is clear that these services are both a major item in the Cuban-Venezuelan trade balance, as well as a significant source

of revenue for the Cuban government and for Cuban workers abroad.

In addition to oil, Venezuela exports chemicals, plastics, and textiles to Cuba and has imported construction materials and medicine. Bilateral goods trade between Cuba and Venezuela accounted for 44 percent of Cuba's total goods trade in 2012, but only 5 percent of Venezuela's total goods trade.²¹ Venezuela's dominance in the trade in goods is partly compensated by Cuba's exports of professional services to Venezuela, as previously described.²² Graph 1 charts Cuba's commercial

Graph 1. Cuba's Trade with Allied Country as a Percentage of GDP
(USSR-Cuba trade from 1989-1993; Venezuela-Cuba trade from 2001-2011)



Trade in goods and services with allied country in constant 1997 prices is divided by GDP in constant 1997 prices.

Source: Based on the methodology of Vidal Alejandro, *Proyecciones Macroeconómicas de una Cuba Sin Venezuela* with updated 2011 data.

¹⁸ This is based on a \$5.432 billion payment from Venezuela to Cuba. Carmelo Mesa Lago, *Cuba en la era de Raúl Castro. Reformas económico-sociales y sus efectos* (Madrid: Editorial Colibrí, 2012), 136.

¹⁹ The Venezuelan government also provides a modest stipend for Cuban doctors for food and housing, approximately \$50-60 at the black market exchange rate of BsF 65:\$1 in April 2014. Andrea Rodriguez, "Cuban Doctors in Eye of Venezuelan Hurricane," *Associated Press*, April 16, 2014, <http://bigstory.ap.org/article/cuban-doctors-eye-venezuelan-hurricane>; Julia M. Feinsilver, "Médicos Por Petróleo," *Nueva Sociedad*, no. 2016 (2008): 107-22.

²⁰ In March 2014, the Cuban government more than doubled wages for doctors. "Cuba duplica salarios de médicos, que ganarán hasta 64 dólares al mes," *El Universo*, March 21, 2014, <http://www.eluniverso.com/noticias/2014/03/21/nota/2421001/cuba-duplica-salarios-medicos-que-ganan-hasta-64-dolares-mes>; "Aprobó Consejo de Ministros incremento salarial para el sector de Salud," *Granma*, March 21, 2014, <http://www.granma.cu/cuba/2014-04-25/aprobo-consejo-de-ministros-incremento-salarial-para-el-sector-de-la-salud>.

²¹ Total bilateral goods trade between Cuba and Venezuela as a share of Venezuela's total goods trade with the world. Authors' calculations using export and import data from Banco Central de Venezuela and Oficina Nacional de Estadística e Información, "Cuentas Nacionales," in *Anuario Estadístico de Cuba 2012, 2013 ed.* (Havana, Cuba: República de Cuba).

²² Carlos A. Romero, "Cuba y Venezuela: 'La génesis y el desarrollo de una utopía bilateral,'" in *Cuba, Estados Unidos y América Latina frente a los desafíos hemisféricos*, ed. Luis Fernando Ayerbe (Barcelona: Icaria Editorial, 2011), 159-202.

relationship with allied countries, first indicating heavy reliance on Soviet trade until 1993 and then substantial commercial relations with Venezuela from 2001 forward.

Venezuela has invested extensively in the Cuban economy. There were at least 370 joint investment projects signed between 2000 and 2011, although there is little information available regarding the number fully implemented.²³ Among the most important of these was an investment of \$2 billion in the Cuban Cienfuegos and Hermanos Díaz refineries as part of a deal signed between PDVSA (Petróleos de Venezuela S.A., Venezuela's state-owned gas and oil company) and CUPET (Cuba Petróleo, Cuba's state-owned oil and gas company) at the end of 2008.²⁴ Venezuela also increased the amount of oil it shipped to Cuba from 87,000 bpd in 2007 to 111,700 bpd in 2008, of which 21,700 bpd was destined for the joint venture refinery at Cienfuegos. This deal allows Cuba to export more profitable refined petroleum products, including jet fuel, diesel and gasoline.²⁵ One estimate suggests that Cuba sold refined petroleum products for \$880 million in 2008.²⁶ However, it is difficult to estimate Cuba's earnings from these exports precisely because some are used to satisfy Petrocaribe quotas. Beyond the oil relationship, the Venezuelan Economic and Social Development Bank (BANDES) is reported to have invested 70 percent of its funds in Cuba, in excess of \$1.1 billion, as of 2011.²⁷

Security

Although difficult to observe and quantify, Venezuela and Cuba also experience a close, if asymmetrical, security relationship. Various sources report the numbers of Cuban intelligence operatives and military advisors as ranging from hundreds to thousands. Around 400 military advisors provide direct support to the Presidential Guard.²⁸ Intelligence and military advisors are reportedly deployed in military units, the Ministry of Interior and Justice, the Directorate of Military Intelligence, and the Servicio Bolivariano de Inteligencia Nacional. This service is coordinated by Cuba's military attaché in Caracas.²⁹ A coordination and liaison group of the Cuban armed forces in Venezuela was also established in 2009.³⁰ The Venezuelan armed forces have revised their doctrine, previously based on a U.S. model, to adapt a Cuban military doctrine. This is based on prolonged popular war, designed to incorporate the civilian population into resistance forces in the event of an invasion. Cubans also man the 'sala situacional' (war room) for the Venezuelan president, which largely focuses on domestic security and politics. Cuban advisors serve in the Venezuelan Interior Ministry, immigration service, and national telecommunications company.³¹ By contrast, the Venezuelan military and intelligence presence in Cuba is limited to a military attaché group, established in 2007, and officers receiving training at Cuban military schools.³²

²³ Carmelo Mesa-Lago, "El posible impacto de la muerte de Chávez en la economía cubana."

²⁴ Castañeda, "La ayuda económica de Venezuela a Cuba: Situación y perspectivas ¿Es sostenible?"

²⁵ MENPET, *Petróleo y otros datos estadísticos 2009-2010*, 105; Castañeda, "La Ayuda Económica de Venezuela a Cuba: Situación Y Perspectivas ¿Es Sostenible?"

²⁶ Castañeda, "La ayuda económica de Venezuela a Cuba: Situación y perspectivas ¿Es sostenible?"

²⁷ Gerardo Cárdenas, trans, "Cuba consumes more than 70% of Bandes' aid funds," *El Universal*, October 24, 2011, <http://www.eluniversal.com/economia/111024/cuba-consumes-more-than-70-of-bandes-aid-funds>.

²⁸ Lara Mantiñán Búa, "La injerencia cubana inquieta al mando militar de Venezuela," *ABC.es*, September 26, 2013, <http://www.abc.es/internacional/20130926/abci-injerencia-cubana-ejercito-venezuela-201309251956.html>.

²⁹ Ginter, "Truth and Mirage"; Cristina Marcano, "Las relaciones desmedidas," *El País*, March 31, 2014, http://internacional.elpais.com/internacional/2014/03/28/actualidad/1396026665_272257.html.

³⁰ Romero, "Cuba y Venezuela: 'La génesis y el desarrollo de una utopía bilateral.'"

³¹ Ginter, "Truth and Mirage."

³² Romero, "Cuba Y Venezuela: 'La génesis y el desarrollo de una utopía bilateral.'"

Diplomacy

As president, Hugo Chávez adopted some of the same strategies pursued by the Cuban government in the 1960s and 1970s to build a network of support among political parties, civil society organizations, and international organizations, both across Latin America and globally. Chávez's diplomacy was successful in no small part because of the resources at his disposal from Venezuela's booming oil income during this period.³³ Still, there was important institutional collaboration between Cuba and Venezuela through the Alianza Bolivariana para los Pueblos de Nuestra América—Tratado de Comercio de los Pueblos (ALBA-TCP), originally offered as a counterproposal to the Free Trade Area of the Americas. This economic and political treaty brings together Cuba, Venezuela, Bolivia, Ecuador, Nicaragua and four Caribbean states within a common trade framework; it also includes a number of solidarity programs in education and food security. In addition to ALBA, Venezuela and Cuba participate in Petrocaribe,³⁴ and they cooperate in the context of CELAC, whose summit Cuba hosted in January 2014.³⁵ Finally, Venezuela and Cuba are also co-owners with Argentina of Telesur, a broadcast service designed to provide alternative media across Latin America. It generally follows a pro-Cuban and pro-Venezuelan editorial line.³⁶

IMPLICATIONS OF INTERDEPENDENCE IN CUBAN AND VENEZUELAN RELATIONS

Both the Fidel Castro and Hugo Chávez governments benefited from interdependence. Each

provided the other with capabilities not possessed on their own: Castro received important levels of economic assistance and collaboration with the reinsertion of Cuba into Latin American regional relations, and Chávez received the support of professionals he could trust to execute his domestic programs. While the asymmetry of the relationship favored Cuba, which was reeling from the collapse of Soviet-era subsidies and in desperate need of assistance to sustain its socialist system, it created vulnerabilities for each state. The implications of this asymmetry are now becoming increasingly apparent.

The 2014 crisis in Venezuela highlights the vulnerability created by unsustainable subsidized oil assistance. Venezuela is dependent upon the sale of petroleum for over 95 percent of foreign earnings, and it uses this to pay for the imports of over two-thirds of basic consumer products.³⁷ Foreign exchange is increasingly scarce because PDVSA's oil production has been on a downward trend for the past 15 years, declining in earnest since 2009, and oil prices have fallen back from their peak in 2008. This is compounded by the increasing proportion of Venezuela's oil exports that are sold at below market rates to Petrocaribe members, to other South American nations, and to its own citizens, as shown in Table 1. Domestic consumption is highly subsidized and accounts for one-fifth of total domestic oil production. In addition, starting in 2007, Venezuela has sent up to 415,000 bpd annually to China in repayment for an accumulated \$49.5 billion in loans to the Venezuelan government.³⁸ This means that these exports provide no new revenue for the Venezuelan government. Venezuela exports

³³ Harold Trinkunas, "International Bolivarianism and Its Influence" (Western Hemisphere Security Analysis Center, Florida International University, June 2011); Javier Corrales, "Using Social Power to Balance Soft Power: Venezuela's Foreign Policy," *The Washington Quarterly* 32, no. 4 (October 2009): 97–114.

³⁴ For additional details, see Norman Girvan, "ALBA, Petrocaribe, and Caricom: Issues in a New Dynamic," in *Venezuela's Petro-Diplomacy: Hugo Chávez's Foreign Policy*, ed. Ralph S. Clem and Anthony P. Maingot (Gainesville: University Press of Florida, 2011), 116–34.

³⁵ Tim Anderson, "Chávez and American Integration," in *Democracy, Revolution and Geopolitics in Latin America: Venezuela and the International Politics of Discontent*, ed. Luis Fernando Angosto-Ferrández (New York, NY: Routledge, 2014), 13–46.

³⁶ James Painter, "The Boom in Counter-Hegemonic News Channels: A Case Study of Telesur" (Reuters Institute for the Study of Journalism, Oxford University, 2007), https://reutersinstitute.politics.ox.ac.uk/fileadmin/documents/James_Painter.pdf.

³⁷ Trinkunas, "Venezuela Breaks Down in Violence."

³⁸ Mayela Armas H., "Chinese loans to Venezuela total USD 49.5 billion in seven years," *El Universal*, January 6, 2014, <http://www.eluniversal.com/economia/140106/chinese-loans-to-venezuela-total-usd-495-billion-in-seven-years>. For yearly amounts, see *Informe de Gestión Anual 2012 de Petróleos de Venezuela*, 93.

Table 1. Recipients of Venezuela's Oil at Non-Market Rates (2011)³⁹

Recipients	crude, products and natural gas liquids in BOE per day
Total crude oil production	3,129,000
Domestic consumption	646,000
China	415,000
Cuba	102,000
Petrocaribe	94,600
Argentina	24,600
Bolivia	10,800
Uruguay	9,700
Paraguay	7,500
Percentage of crude oil allocated at non-market rates	42%

over 100,000 bpd of crude and oil products to Cuba alone in addition to another shipment of approximately 95,000 bpd to Petrocaribe members under subsidized financing arrangements that defer payment to Venezuela. The aggregate effect is that at least 42% of Venezuela's oil production is allocated via non-market arrangements. As domestic production continues to stagnate while external commitments increase, these commitments are unsustainable in the long-run. They also fuel an immediate shortage of dollars which translates directly into a scarcity of consumer products and a sustained rise in inflation in Venezuela.

Venezuelan opponents of Maduro have been highly critical of the relationship with Havana. They see economic benefits mostly accruing to Cuba, and

they view the level of Cuban support for the Maduro administration as an infringement on Venezuela's sovereignty and autonomy. The relationship has even been a focal point for opposition demonstrations calling—among other things—for an end to the Cuban role in the Venezuelan armed forces.⁴⁰

The relationship has become a concern for the Cubans as well. Not only is the crisis in Venezuela a reminder of their economic vulnerability, but it also highlights the growing tension between the Cuban economic restructuring effort—aimed at pushing state workers toward the *cuentapropista* (self-employed) and cooperatives sector—and the increasingly statist Venezuelan economic model. Cuba's current restructuring policy aims to shrink the size of the state sector in the economy, diversify international trade, and increase the role of foreign direct investment. The Cuban government under Raúl Castro recently adopted a new foreign investment law and opened, with much fanfare, a new special development zone at the port of Mariel with major support from Brazil. In addition, Cuba is engaged in a rapprochement with the European Union, which in 2008 began to lift some of its sanctions against the island.⁴¹ This approach differs from the state-centric model pursued previously under which investment in Cuba was drawn mainly from China and joint ventures with Venezuelan state-owned enterprises. It also differs from the trends in Venezuela, which are increasing the size of the state sector, narrowing Venezuela's export sector to the petroleum industry, and driving away foreign investment. The Cuban economy is clearly still much more statist than Venezuela's, but the economic policies presently pursued by each government are advancing toward different

³⁹ All data is drawn from *Informe de Gestión Anual 2012 de Petróleos de Venezuela*, 43, 93, 128., 43, 93, 128. Exports to China include Fondo Pesado II and Fondo Gran Volumen, which are the amounts provided as repayments for government-to-government loans. For more on the terms of Venezuela's agreements with Bolivia, Uruguay and Paraguay, see *Acuerdo de Cooperación Energética Petrocaribe* (Caracas, Venezuela: Sistema Económico Latinoamericano y del Caribe, 2013). Table assumes barrels of oil equivalents for product totals. Other sources, such as the U.S. Energy Information Administration and the British Petroleum Statistical Review of World Energy provide lower numbers for annual production (2,300,000 and 2,766,000, respectively) and higher numbers for domestic consumption in 2011 (750,881 and 764,000, respectively), but they do not report the amounts sent to recipients of Venezuela's oil under non-market arrangements.

⁴⁰ Victoria Burnett and William Neuman, "Protesting in Venezuela, With Antipathy Toward Cuba's Government," *New York Times*, March 25, 2014, http://www.nytimes.com/2014/03/26/world/americas/protesting-in-venezuela-with-antipathy-toward-cuba.html?_r=0.

⁴¹ Andrea Rodriguez, "Cuba. EU Talks Aim to Reset Stalled Relations." *Associated Press*, April 30, 2014, <http://bigstory.ap.org/article/cuba-eu-talks-aim-reset-stalled-relations>.

goals, rather than converging on a coherent hybrid model. This suggests that the two governments may not be as closely aligned as they were during the Fidel Castro-Hugo Chávez period.

SCENARIOS FOR CUBAN-VENEZUELAN RELATIONS GOING FORWARD

The level of assistance that Venezuela provides is a key variable in determining the degree of its mutual dependence with Cuba. Despite the cost of its largesse, the Venezuelan government under Maduro is unlikely to abandon its privileged relationship with Cuba without compelling reasons. The Venezuelan government sees the benefits of intelligence, security, military and health support as too valuable. However, economic and political crises may force Venezuela to limit assistance to Cuba.

The likely future scenarios for the relationship are either: i) a status quo level of support from Venezuela, allowing the relationship with Cuba to continue on its current path, ii) a slow decline in Venezuela's support for Cuba, driven either by political or economic considerations, or iii) a rapid decline in support due to an economic collapse in Venezuela or a change in government. Expanded Venezuelan assistance to Cuba is unlikely. It is doubtful that Venezuela will re-experience the economic boom that financed the initial expansion of the Cuban-Venezuelan relationship under Hugo Chávez; oil prices grew dramatically from \$11.20 per barrel on the week he was elected president to a peak of \$142 per barrel in 2008.⁴² Of the remaining scenarios, the present Cuban and Venezuelan administrations are likely to prefer the status quo. However, a slow decline in Venezuelan support for Cuba, the most probable future scenario, would benefit both populations by reducing the unsustainable depen-

dence on subsidized economic relations, improving the prospects for Venezuela's democracy, and strengthening the case for economic restructuring and diversification in Cuba.

Scenario 1: Status Quo Assistance to Cuba

A modicum of economic and political liberalization in Venezuela would have a stabilizing effect and allow assistance to Cuba to continue. Politically, the dialogue between the government and the opposition in Venezuela, which began in March 2014, may reduce political tensions and provide sufficient cover for the Maduro administration to take economic adjustment measures. Maduro would be able to close the fiscal gap and reduce scarcity through a liberalized currency exchange and import regime. Better conditions for domestic businesses and a rise in the price of gasoline would begin to provide economic relief, rationalize domestic energy use, and improve government finances. This would allow Maduro to maintain the present relationship with Cuba, and it would continue to be in his interest to do so because of the services the Cubans provide as a trusted workforce, particularly in the security dimension. Given the role of the Venezuelan armed forces in supporting the Maduro administration, Cuban intelligence support to monitor discontent in the security services is essential to regime survival.⁴³

Under this scenario, Cuba would most likely continue present levels of dependence on Venezuela. However, even if Cuba felt secure in the level of Venezuelan assistance in the short to medium term, Cuban economic reform efforts would continue. Although there are a number of factors driving the reforms, they have an important benefit of providing a hedge against a possible decline of Venezuelan assistance in the future.

⁴² Venezuelan crude oil earns approximately \$96.92 per barrel as of May 16 2014. "Precios del Petróleo," Ministerio del Poder Popular de Petróleo y Minería, República Bolivariana de Venezuela, accessed May 20, 2014, <http://www.menpet.gob.ve/secciones.php?option=view&ids=45>. For historical oil data, see "Petroleum & Other Liquids: Cushing, OK WTI Spot Price FOB," U.S. Energy Information Administration, last modified April 30, 2014, <http://www.eia.gov/dnav/pet/hist/LeafHandler.ashx?n=PET&s=RWTC&f=D>.

⁴³ During the present crisis, 30 military officers have reportedly been detained, including three Air Force generals that are alleged to have conspired against President Maduro. "Imputados los tres generales acusados de golpismo en Venezuela," *ABC.es*, April 16, 2014, <http://www.abc.es/internacional/20140415/abci-maduro-confirma-identidad-tres-201404152134.html>.

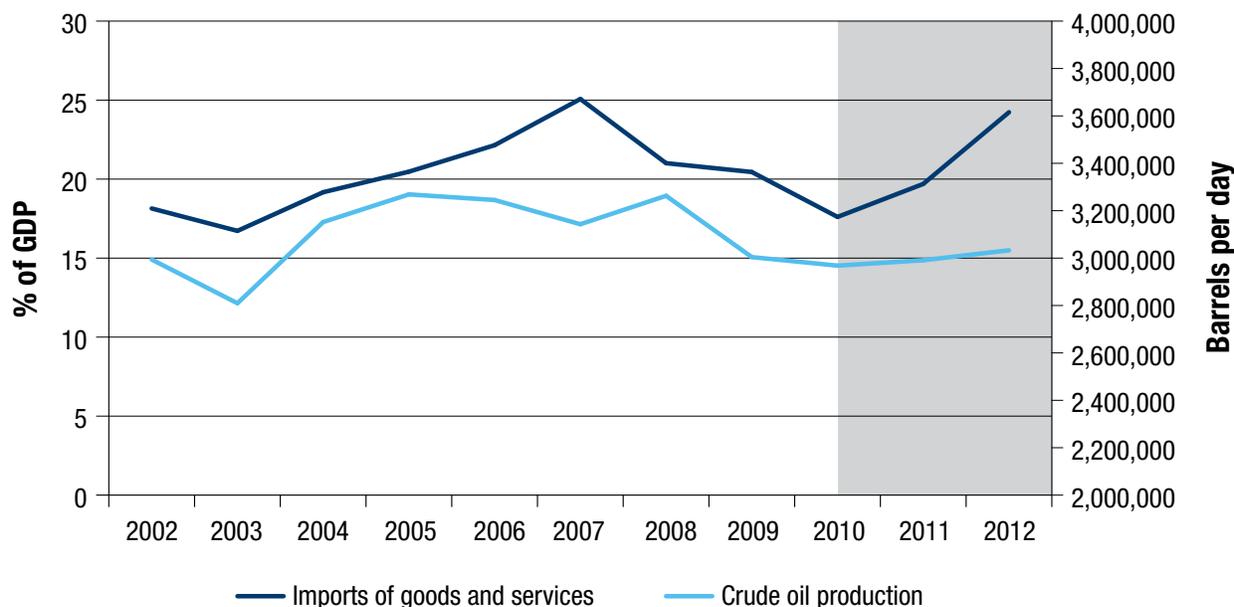
Scenario 2: Gradual Decline in Assistance to Cuba

There is also the prospect of a slow decline in Venezuelan support for Cuba. This might happen as a consequence of continuing economic deterioration in Venezuela. Recent economic data on Venezuelan imports and oil production highlight a critical problem: demand for imports is growing while oil production is stagnating, as is illustrated by Graph 2. Since Venezuela's oil exports are the source of over 95 percent of foreign exchange used to pay for imports, this gap contributes to the economic crisis in Venezuela. The Venezuelan government has already taken measures to reduce consumption, but the present trends may also force the Venezuelan government to adopt a more pragmatic attitude toward oil exports, including shifting oil shipments toward buyers that can pay market prices. Given the current structure of Venezuela's oil sales, this would

realistically mean reducing oil sold to Petrocaribe. A recent statement by Venezuelan Oil and Mines Minister Rafael Ramirez in Havana in February 2014 indicates that the volume of oil provided by Venezuela to Cuba may have already dropped by between 23 and 32 percent.⁴⁴ It remains to be seen how Cuba will adjust to this reduction in supply.

It is also possible that Venezuelan oil in the U.S. market will be increasingly displaced by the growing supply of Canadian heavy crude transported by rail to the Gulf Coast refineries (or possibly by the Keystone XL pipeline should it be approved), coupled with additional oil exports from Mexico, should energy reforms succeed. Venezuela exported an average of 797,348 bpd in 2013 to the United States, as compared to an average of 1.56 million bpd in 2004.⁴⁵ Increased U.S. imports from Canada have already made up the difference.⁴⁶ If its exports continue to be displaced by North

Graph 2. Venezuela: Rising Imports and Stagnant Oil Production



Source: Authors' compilation using data from the World Bank DataBank and Venezuela's Ministerio del Poder Popular de Petróleo y Minería.

⁴⁴ Andrés Rojas Jiménez, "PDVSA recortó exportaciones hacia Cuba y Petrocaribe," *El Nacional*, February 27, 2014, http://www.el-nacional.com/economia/Pdvsarecortó-exportaciones-Cuba-Petrocaribe_0_363563835.html; Ernesto J. Tovar, "Envíos petroleros a Cuba llegan a 80 mil barriles al día," *El Universal*, February 21, 2014, <http://www.eluniversal.com/economia/140221/envios-petroleros-a-cuba-llegan-a-80-mil-barriles-al-dia>.

⁴⁵ U.S. Energy Information Administration, "U.S. Imports from Venezuela of Crude Oil and Petroleum Products," accessed May 29, 2014, <http://www.eia.gov/dnav/pet/hist/LeafHandler.ashx?n=PET&s=MTTIMUSVE1&f=M>.

⁴⁶ Pietro D. Pitts and Nathan Crooks, "Venezuela Oil Sales to U.S. at 1985-Low Shows China Cost," *Bloomberg*, January 31, 2014, <http://www.bloomberg.com/news/2014-01-30/venezuela-oil-sales-to-u-s-at-1985-low-shows-china-cost.html>.

American oil production, Venezuela would likely switch to markets in Asia, particularly China and India. However, the added transportation costs would have a significant impact on earnings.⁴⁷

Any of these possibilities could mean a reduction in Venezuelan assistance to Cuba. Under this scenario, Cuba's economic restructuring effort would gain an added urgency. An anticipated withdrawal of economic aid from Venezuela would help reformers in Cuba further justify and accelerate plans to shift the workforce off the government payroll and attract international investment. It would also provide the Cuban government with the opportunity to either renegotiate the terms under which professional services are deployed in Venezuela, or transfer the number of *cooperantes* to other countries such as Bolivia, Brazil and Nicaragua. Already Cuba has increased its deployment of doctors to Brazil's poor neighborhoods and rural areas to 11,400 under President Rousseff's *Mais Médicos* program.⁴⁸

Scenario 3: Sudden, Rapid Decline in Assistance to Cuba

There is a small, but nevertheless concrete, possibility that Venezuela's economic and political crisis will precipitate a rapid change in the level of assistance to Cuba. Recent Venezuelan government efforts to devalue the currency may simply produce more inflation without ameliorating the growing scarcity of consumer goods. Economic conditions in Venezuela have continued to deteriorate in the first half of 2014, with a worrisome one-third drop in the level of international reserves to \$20.6

billion (\$16-17 billion of which are held in gold) for a country that is highly import dependent.⁴⁹ In addition, political dialogue between the government and the opposition may fail, which in the context of the ongoing crisis would sharpen social protest. If a deeper crisis were to trigger either a sudden revision in economic policy or a new government altogether, Cuba might be faced with the prospects of sudden adjustment.

Still, the threat to the survival of the Cuban political regime is questionable. According to one estimate, the loss of support from Venezuela would imply an economic contraction of between 4 percent and 7.7 percent of GDP spread out over four years.⁵⁰ Although this would be a severe recession, it would not approach the scale of the crisis suffered by Cuba after the withdrawal of Soviet support in 1991. Moreover, the Cuban economy today is more diversified and has a broader range of trading partners than it did in the 1990s.⁵¹ Nevertheless, the sudden shock might prompt hardliners in the Cuban regime to seek to rollback recent economic restructuring efforts on the grounds of improving regime security and tightening social control.

IMPLICATIONS FOR THE UNITED STATES AND POLICY RECOMMENDATIONS

In the long run, reduced reliance on the unsustainable and subsidized oil-for-services relationship would be desirable for both Venezuela and Cuba as well as for the United States. Cuba's economic dependence on Venezuela is a major vulnerability due to the damage a withdrawal of assistance would

⁴⁷ "PDVSA no utiliza el canal de Panamá para ningún destino petrolero," *El Mundo*, March 7, 2014, <http://www.elmundo.com.ve/noticias/petroleo/pdvsa/pdvsa-no-utiliza-el-canal-de-panama-para-ningun-de.aspx>.

⁴⁸ "Más médicos para Brasil, menos para Venezuela," *El País*, March 19, 2014, <http://www.bloomberg.com/news/2014-01-30/venezuela-oil-sales-to-u-s-at-1985-low-shows-china-cost.html>.

⁴⁹ Armando Armenta and Hongtao Jiang, *Venezuela: The Value of Opportunistic Adjustment* (Deutsche Bank, 2014); Emili J. Blasco, "Venezuela se queda sin suficientes divisas para pagar las importaciones," *Abc.es*, April 23, 2014, <http://www.abc.es/internacional/20140423/abci-venezuela-divisas-importaciones-201404222046.html>.

⁵⁰ Even though Venezuela has provided support in the amount of 12-20 percent of GDP (depending on the year), the withdrawal of the assistance does not imply that the Cuban economy would suffer a fall of a similar magnitude. Cuba would be able to mitigate some of the effect through trade with other partners. See Vidal Alejandro, *Proyecciones macroeconómicas de una Cuba sin Venezuela* for econometric modeling of this effect.

⁵¹ Domingo Amuchastegui, "Cuba: The Impact of Venezuela," in *Cuba in Transition*, vol. 23 (presented at the Twenty-Third Annual Meeting of the Association for the Study of the Cuban Economy, Miami, FL, 2013), <http://www.ascecuba.org/publications/proceedings/volume23/pdfs/amuchastegui.pdf>.

cause to Cuba's struggling economy and the lack of a readily available and willing substitute. For Venezuela as a country, political dependence on Cuba is harmful to its sovereignty and aid to Cuba does not produce economic benefits commensurate with the level of expenditure. Cuba's dependence is also harmful to Venezuela's prospects for greater democracy, as it creates a strong temptation for the Cuban regime to use its influence in the government and the armed forces to protect the Maduro status quo.

For the United States, Cuban and Venezuelan mutual dependence on the present terms is also undesirable. It strengthens the hand of political hardliners in each government. Their preferred policies undermine the prospects for democracy, human rights, and economic development in both Cuba and Venezuela. These are also the factions most interested in undermining both U.S. leadership in the region and the operation of inter-American institutions such as the Democratic Charter and the Inter-American Human Rights Court.

Of all the scenarios presented here, the gradual decline of Venezuelan assistance to Cuba is most likely to produce a positive outcome for all countries. It would most probably strengthen the hand of reformers in Cuba, which would lead to further liberalization of the economy and growth of the middle class. It would increase Venezuela's prospects for democratic stability and rationalize its government expenditures in ways that provide greater benefit to its citizens.

However, direct U.S. efforts to produce such an outcome would lead to a counterproductive confrontation that would only benefit hardline factions in both Cuba and Venezuela. Hardline actors in both countries desire such a conflict to strengthen their own political fortunes, as illustrated by the Maduro administration's efforts to blame the United States for Venezuela's current political crisis. As it would not be seen as legitimate by other states in Latin America, a confrontational approach would also risk damaging U.S. relations with the hemisphere more broadly.

Fortunately for the United States, market forces are already producing the kind of economic pressures on Venezuela that should lead its government to reconsider its spending on overseas assistance in Cuba. Venezuela's oil sold in the United States is the most profitable segment of its exports. To the extent that Venezuelan oil exports to the United States decrease and are replaced by Canadian and Mexican production, so its government revenues will decrease. Venezuelan oil exports to North America have already dropped by half in the past decade. Venezuela will still be able to replace U.S. markets with those in India and China, both of which have the capacity to refine some of the heavy crude Venezuela exports and are further investing in this area. But the increase in transportation costs, together with the steady erosion of oil production capacity in Venezuela due to mismanagement and underinvestment, will constrain Venezuela's ability to aid Cuba. Although Venezuela may continue to provide oil to Cuba on a preferential basis, it will increasingly need to charge market prices for its exports so as to maximize income. Finally, decreasing revenue will mean it will have to rethink its generous rates of reimbursement for Cuban *cooperantes*.

To facilitate such an outcome, the United States should focus on improving North American energy integration and supporting Mexico's efforts to reform its energy sector. This means accelerating the approval process for the infrastructure that will facilitate the flow of oil and other energy sources among North American countries, where production is rapidly increasing. For example, new cross-border pipelines could be physically built in two to three years. Such efforts will reinforce the market forces that are already pushing Venezuelan crude out of the North American market.

Additionally, regional institutions and governments should prepare for the consequences of reduced Venezuelan oil assistance to the Caribbean and Central America currently provided by Petrocaribe. Before Venezuela decreases aid to Cuba, it is likely to reduce subsidized oil shipments to Caribbean and

Central American countries participating in Petrocaribe. As recommended in an earlier Brookings policy brief, the United States should lead multilateral efforts to create mechanisms by which Petrocaribe countries can assure themselves of their energy security at reasonable costs in the short term. It should also support a transition to sustainable alternative energy sources in the long term.⁵² This will mean helping countries hedge against the loss of Petrocaribe support, and develop the regulatory frameworks to attract private investment in energy production with the goal of using renewables and natural gas. Such a multilateral mechanism should be open to Cuba as part of an incentive structure to deepen economic reform and diversify its energy production matrix.

The Obama Administration should also adopt a new round of executive measures to ease the long-standing embargo on U.S. investment and trade with Cuba.⁵³ This would support further diversification of the Cuban economy and the emergence of middle classes, as well as facilitate Cuba's search

for new energy resources. It would also improve U.S. relations with the rest of the hemisphere as it approaches the 2015 Summit of the Americas in Panama.

Ultimately, it is up to Cuba and Venezuela to address the consequences of an unsustainable subsidized economic and political relationship. While beneficial to Fidel Castro and Hugo Chávez during Venezuela's oil boom, the effects of close political and economic relations between the two countries become more doubtful as Venezuela's crisis continues. In particular for Cuba, replacing dependence on the Soviet Union with dependence on Venezuela simply creates a new vulnerability and a new threat to its autonomy. For Venezuela, Cuba's significant role in its politics and economy is an obstacle to resolving its current crisis via democratic and constitutional means. Although the leadership in neither country is likely to agree, it would be best for the Cuban and Venezuelan people if the unsustainable level of mutual dependency were reduced.

⁵² Harold Trinkunas, *Changing Energy Dynamics in the Western Hemisphere: Impacts on Central America and the Caribbean*, Latin America Initiative Policy Brief (Washington DC: Brookings Institution, 2014), <http://www.brookings.edu/~media/research/files/papers/2014/04/04-energy-central-america-trinkunas/changing-energy-dynamics.pdf>.

⁵³ For example, the administration can allow U.S. NGOs and other organizations to lend directly to *cuentalpropistas* and other small enterprises in Cuba. For additional recommendations, see Ted Piccone, "Reach out to Cuba," in *Big Bets & Black Swans: A Presidential Briefing Book*, 26-28, and "Open Letter to President Obama: Support Civil Society in Cuba," signed by 44 high-level former policy makers and academics, <http://supportcubancivilsociety.org/>.