

**Which structural reforms and which
industrial policy in Algeria?
*10 actions for a diversified and
dynamized economy***

El-Mouhoub MOUHOUD (Université Paris
Dauphine - PSL)

**Webinar on "State-Business Relations, Cronyism and
the Role of the Private Sector in Algeria, Ethiopia and Sudan"
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Outline

1. Introduction : what can Algeria do with this new rise in hydrocarbon prices ?
2. Recall the fundamentals of the Algerian economy
3. Is the new macroeconomic context conducive to a change in the growth regime?
4. Ten actions for a new industrial dynamic of emergence in the industry and the knowledge based services

1.Introduction : what can Algeria do with this new rise in hydrocarbon prices ? (1)

- The Algerian economy has entered since the changes in the political direction of the country imposed by the Hirak in 2019 in a “air hole”.
- If the authorities thought to put an end to the relations of privileges between the state and some companies, the economy does not seem to have found the necessary relays in the private sector.
- The economy of the Bouteflika era was based on the close relationship and vassalage between companies and the state in the context of a game of collusion and privileges (legal, tax ...) granted to these companies.
- Gas and oil resources (a good third of GDP) allowed to finance a large sector of imports of intermediate goods and final consumption representing another third of GDP.
- Just before the Hirak uprising, the economy having suffered a collapse of its foreign exchange reserves of 200 billion dollars were almost divided by ten in 2021
- After the fall of Bouteflika vast majority of private business leaders associated with political power in a relationship of "structural cronyism, have almost all been arrested and imprisoned and their tangible and intangible assets confiscated by the State, which has become the direct owner of several conglomerates of Algerian personalities in the building and public works sector, as well as in the agri-food industry and entire sectors of the manufacturing industry.

1.Introduction : what can Algeria do with this new rise in hydrocarbon prices ? (2)

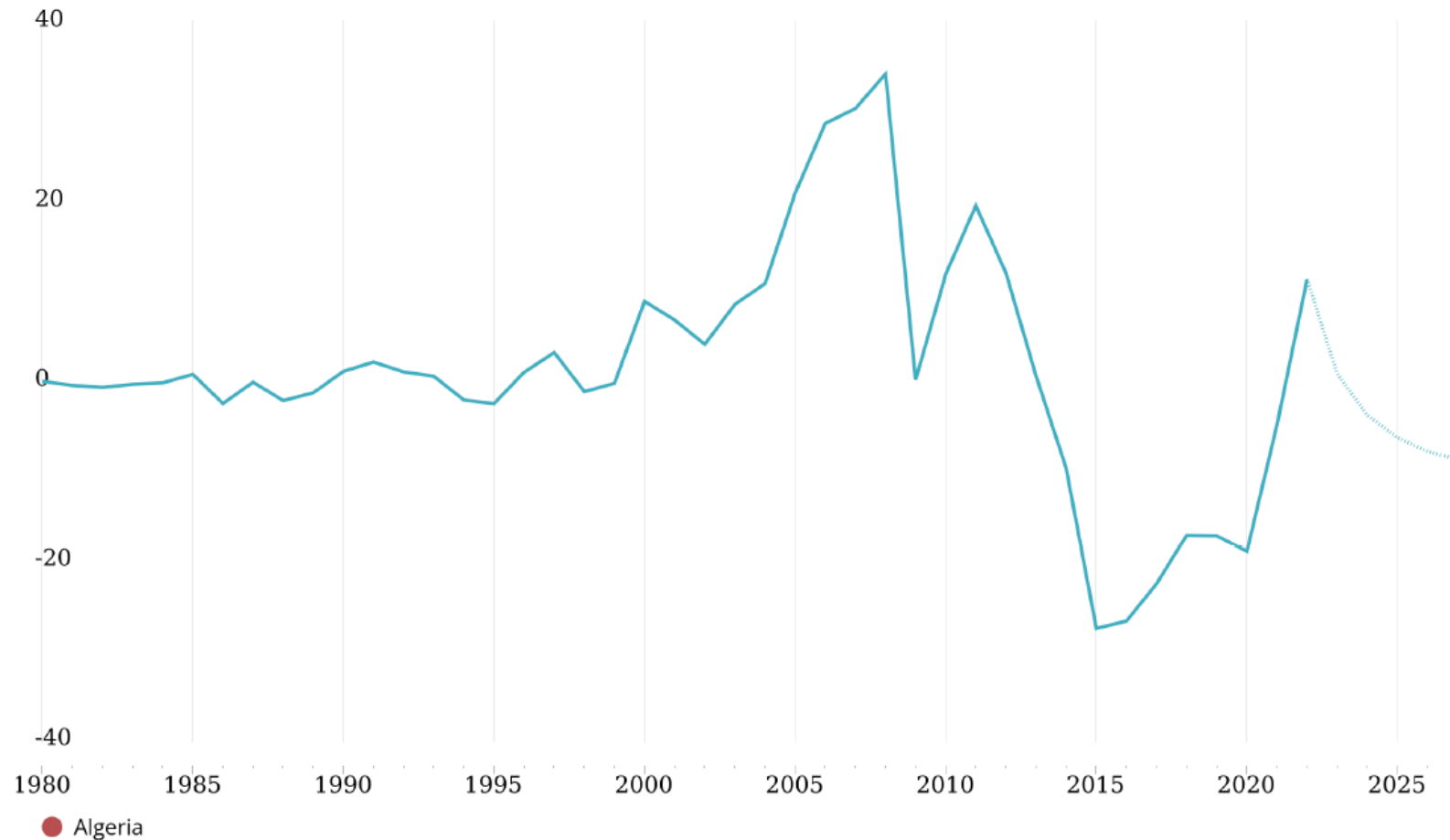
- “air gap” :
 - With no companies having taken over from the dominant companies now neutralized in the post-Hirak political game, hydrocarbons remain the only resource whose revenues have been eroded until after the global containment of 2020-2021.
 - Unemployment and inflation + the twin internal and external deficits (international debt still excluded)
- “breath of fresh air”
 - the sudden rise in the price of hydrocarbons (following the great deconfinement + Russian War in Ukraine)
 - => relax macroeconomic constraints and continue to subsidize consumption and housing households
- Are the fundamentals of the Algerian economy, recalled in section 2, changing?
- What does the new situation bring with its (section 3)?
- How can Algeria take advantage of this windfall for its macroeconomic balances?
- We believe that it is urgent to use these new unexpected and exogenous margins of maneuver in the Algerian economy to implement real structural reforms and establish an industrial and commercial policy adapted to the new configurations of globalization.
- This is marked by a strong trend towards the relocation of global value chains on a regional basis for the manufacturing industry but also the advent of a hyper-globalization of services and digital activities which Algeria could benefit more than ever.
- This is why section 4 proposes for public debate 10 major actions to diversify and boost the Algerian economy. .



Current account balance

IMF DataMapper

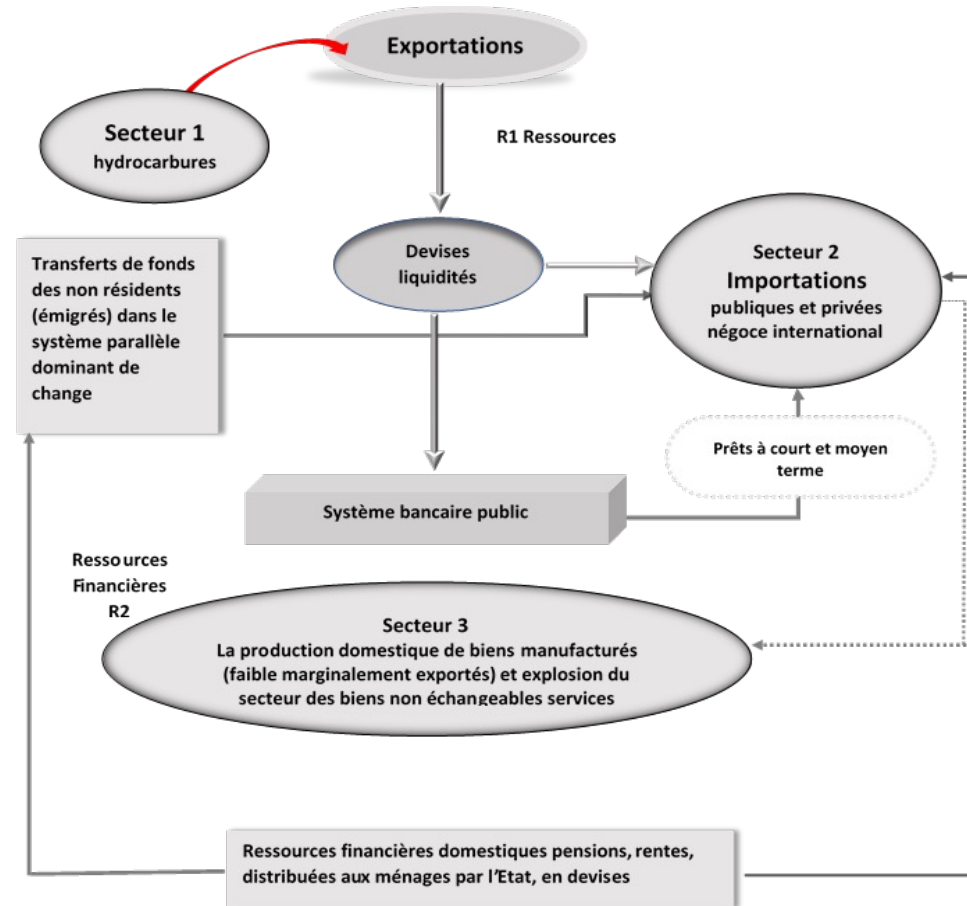
Current account balance U.S. dollars (Billions of U.S. dollars)



2. Recall the fundamentals of the Algerian economy

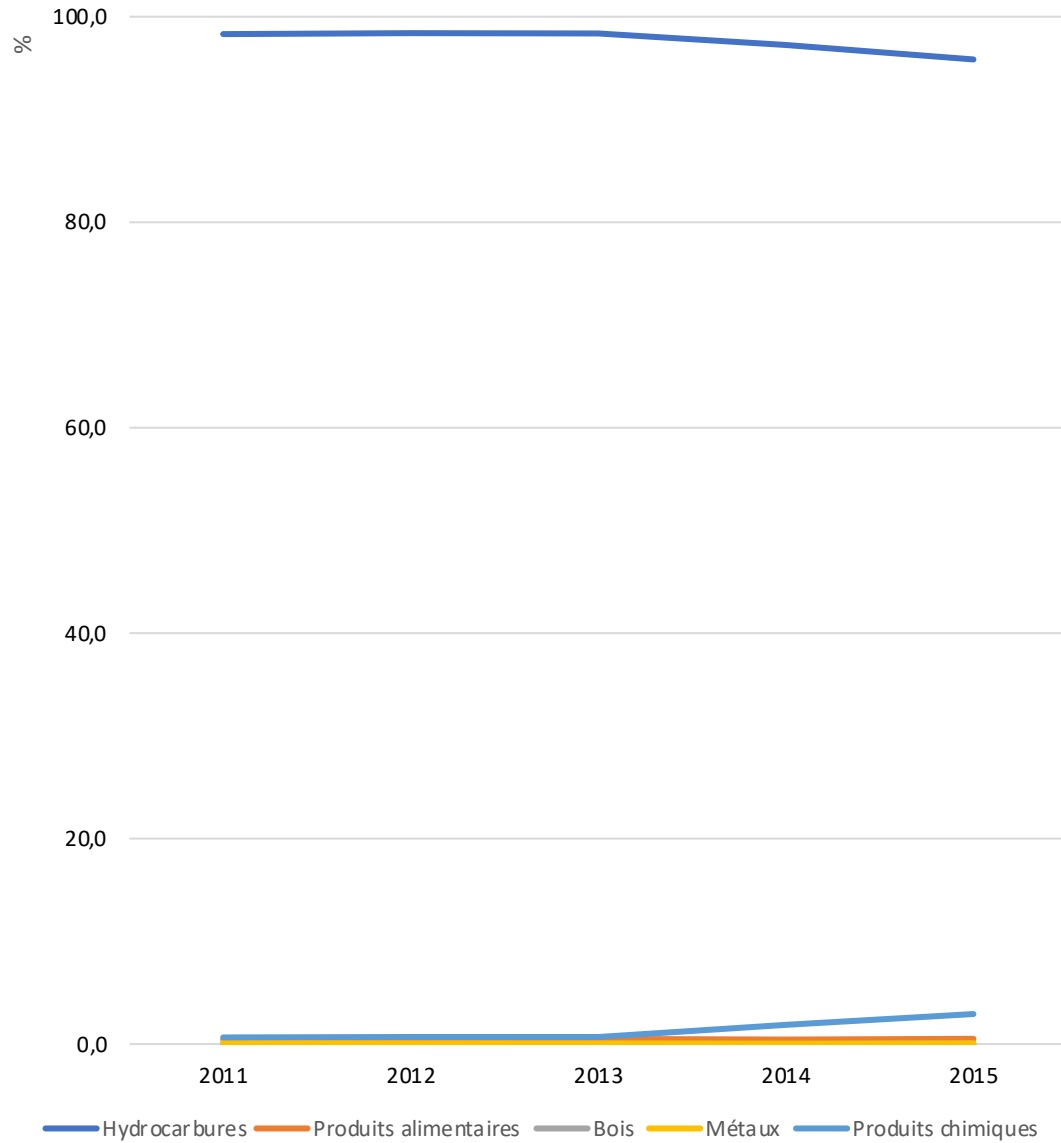
- A hyper concentrated and deindustrialized economy
- The hydrocarbon rent favors the inertia of the economy but also social redistribution
- The lowest participation rate of the labor force (worse for female)
- Unemployment and non-formal employment increases with the level of education
- Abnormally expatriation rate of skilled (brain drain)

Une concentration sur peu de secteurs une désindustrialisation profonde



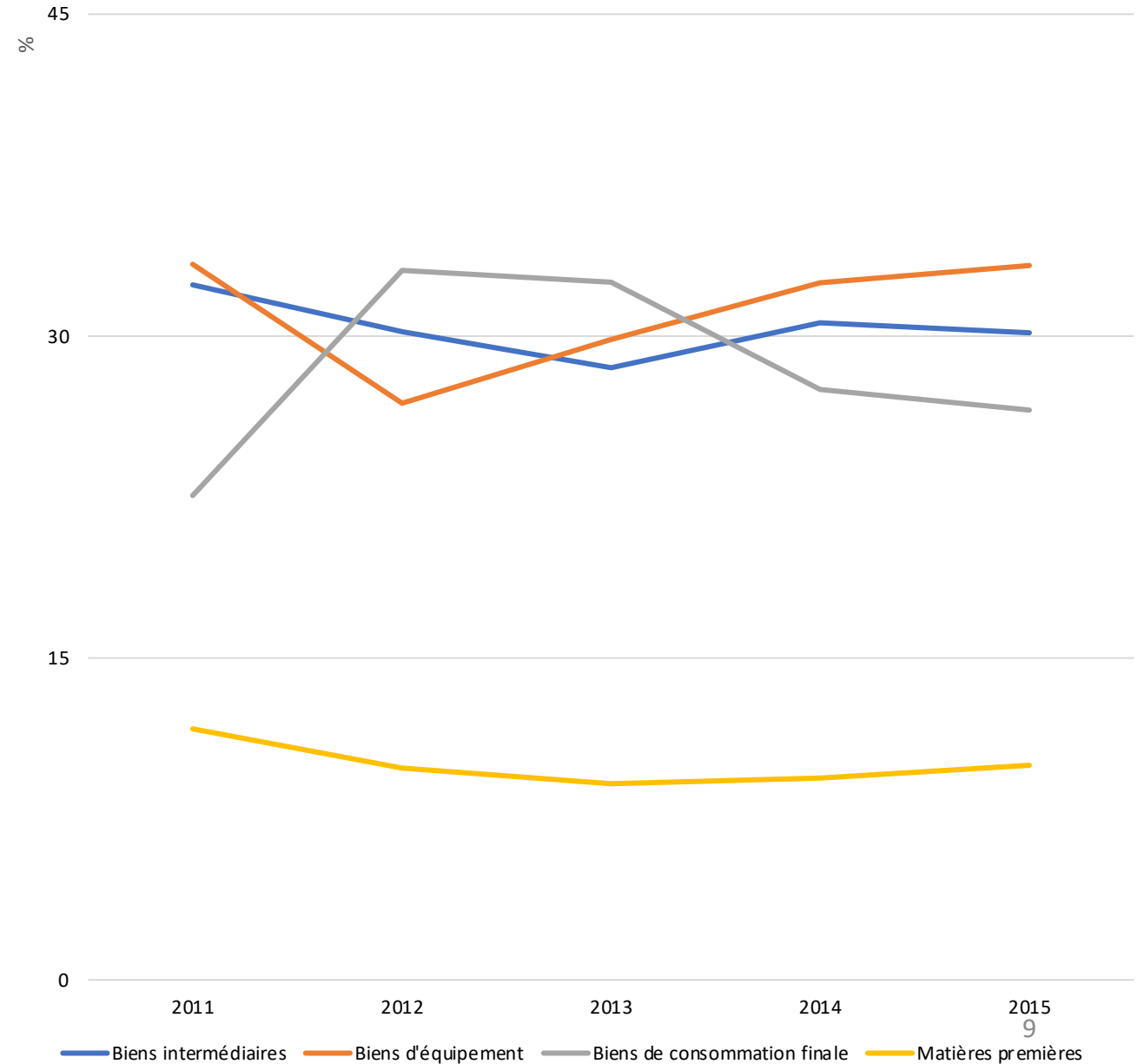
Secteur 2. Importations
67,5 % **of GDP** (1961)=>
18,4 % en 1987 et **30 %**
en moyenne (1960-2014)

Graph. 1-a. Export structure
In % of total exports

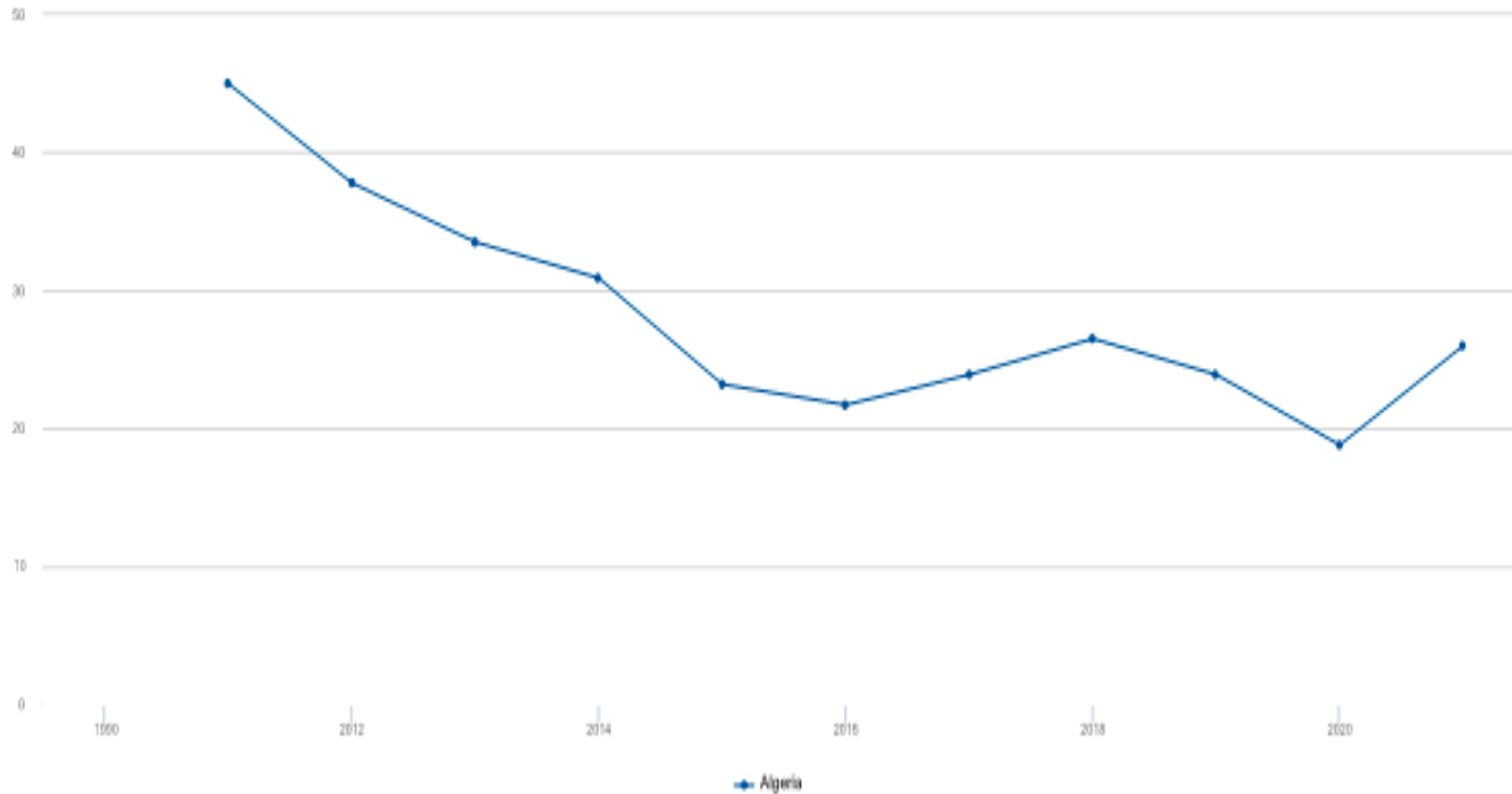


Source : Mouhoud 2017

Graphique 1-b. Import structure
By stages of production (% of total imports)



DEINDUSTRIALISATION

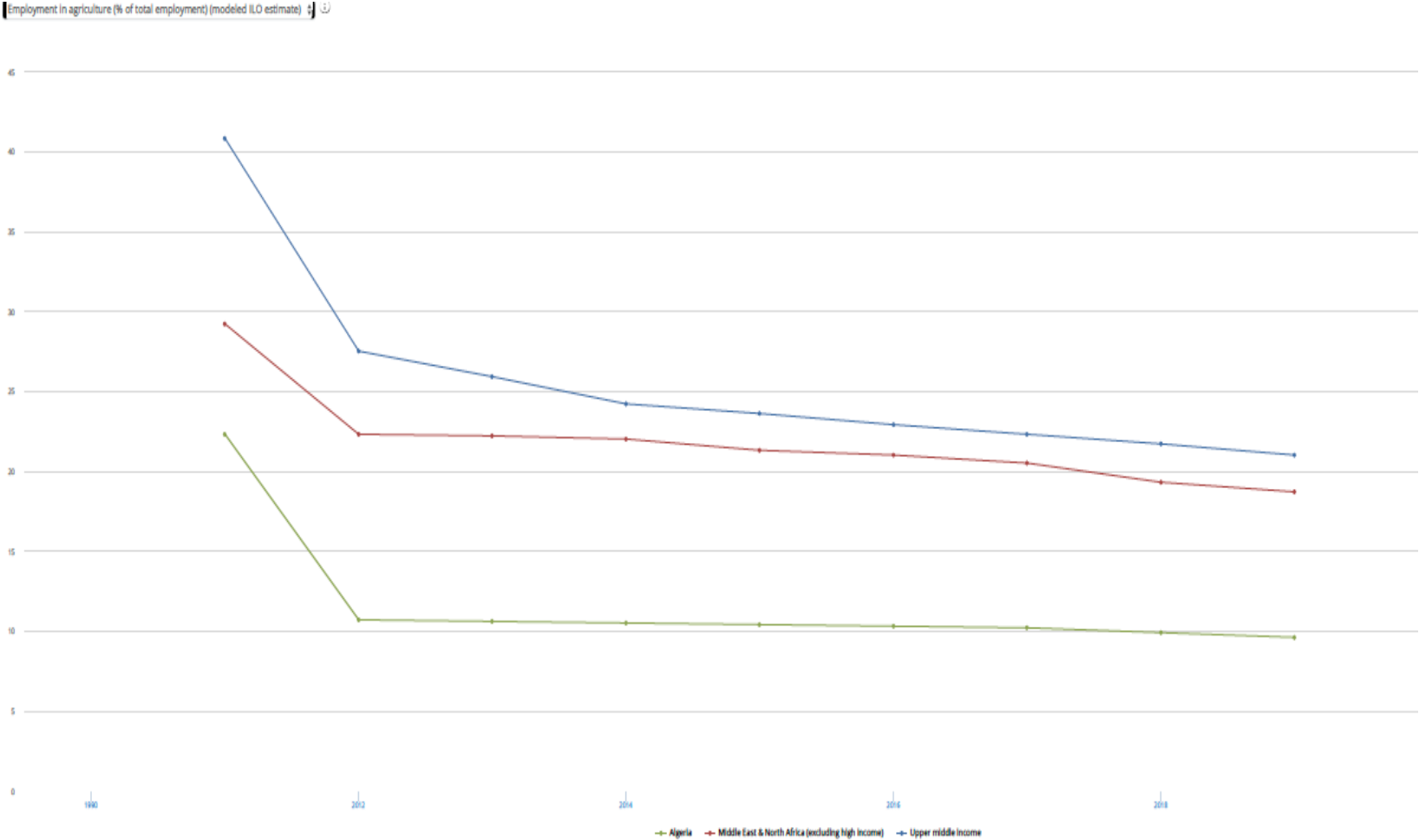


Series : Manufacturing, value added (% of GDP)

Source: World Development Indicators

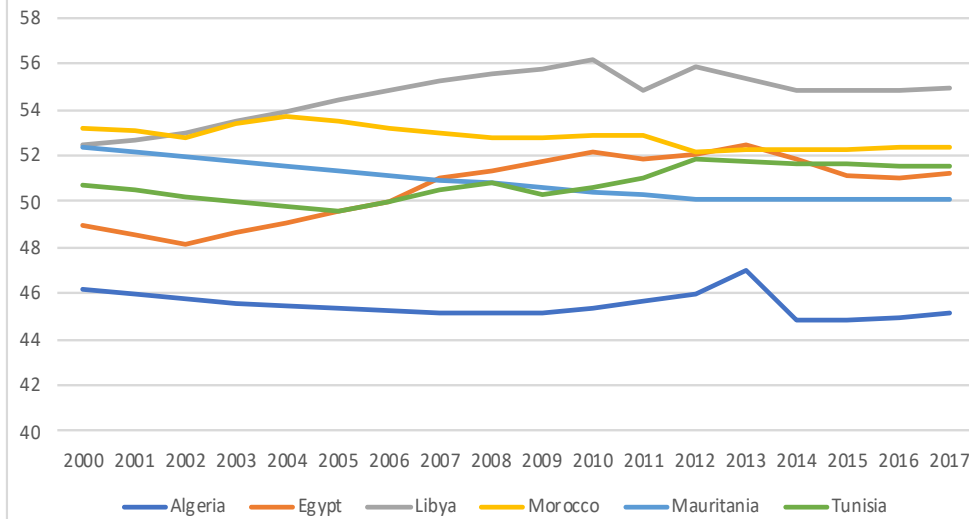
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Employment in agriculture % total employment

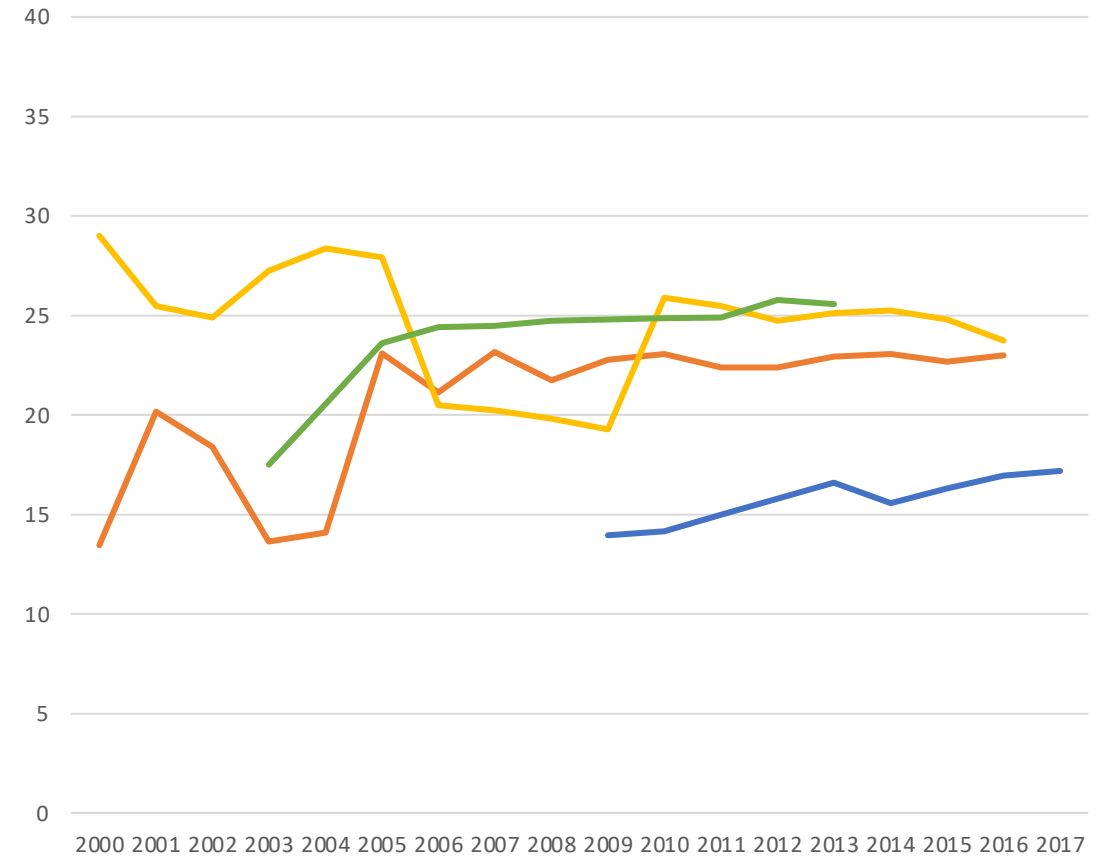


Source: World Development Indicators

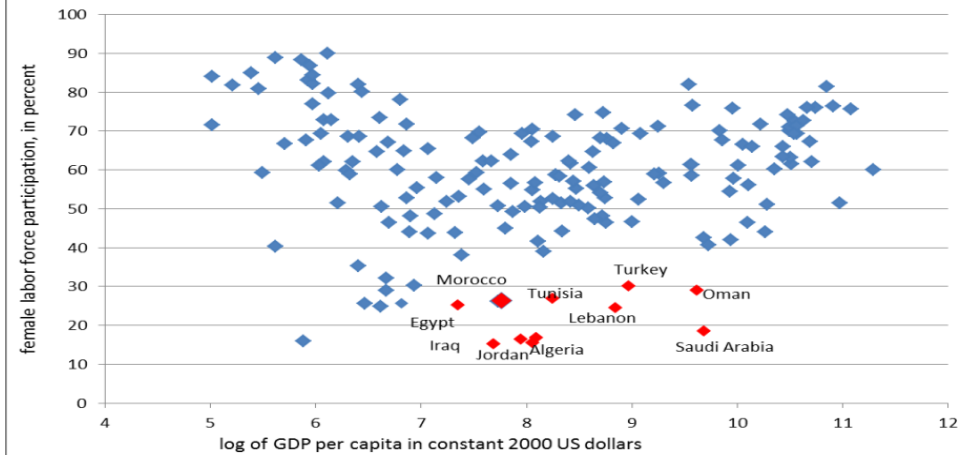
Labor force participation rate (%)



Female Labor Force participation (%)

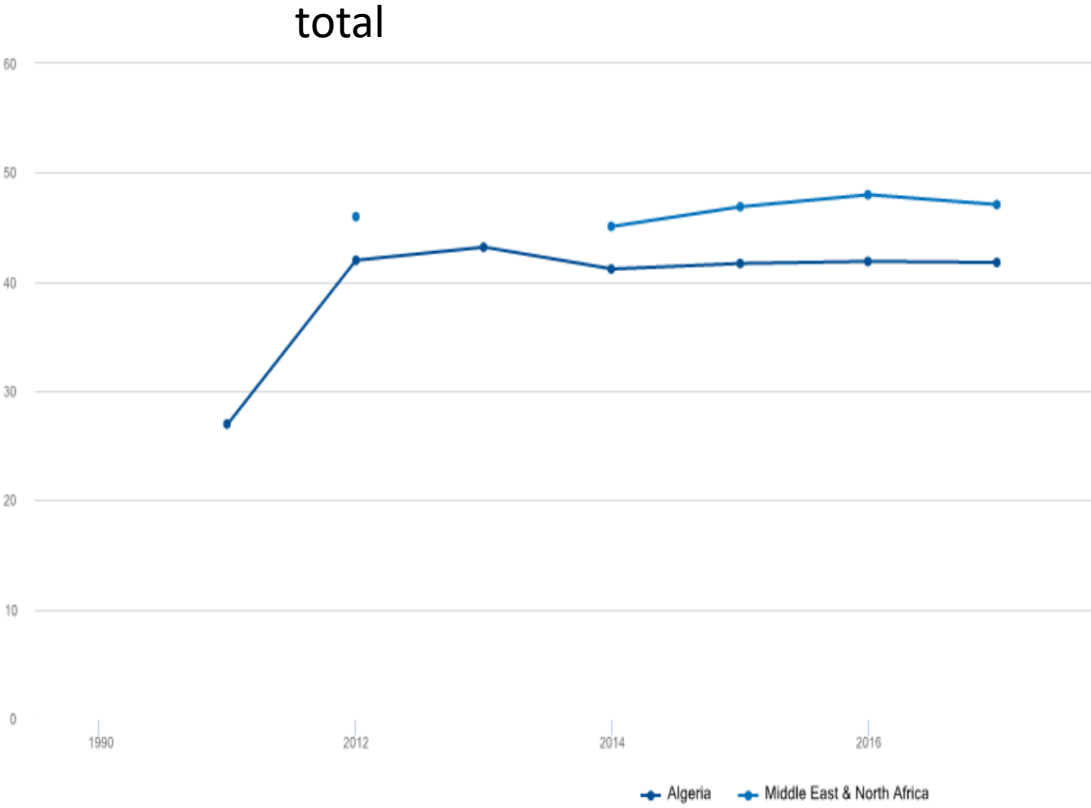


Female labor force participation across country, 2010



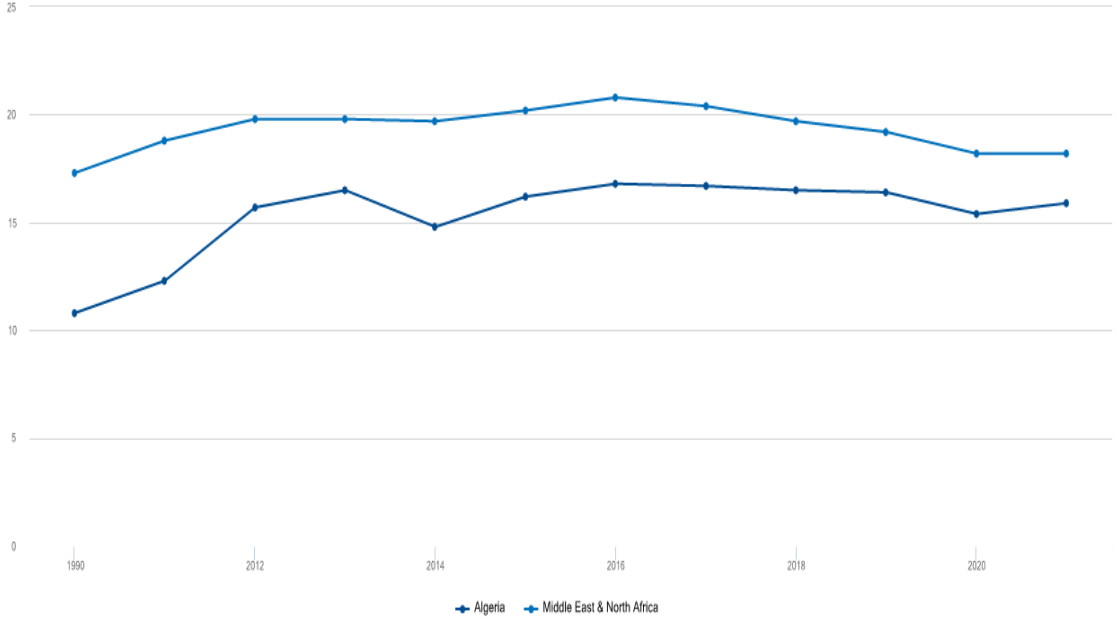
The lowest female labor force participation rate

Labor participation rate %



Series : Labor force participation rate, total (% of total population ages 15+) (national estimate)
Source: World Development Indicators
Created on: 03/11/2023

female



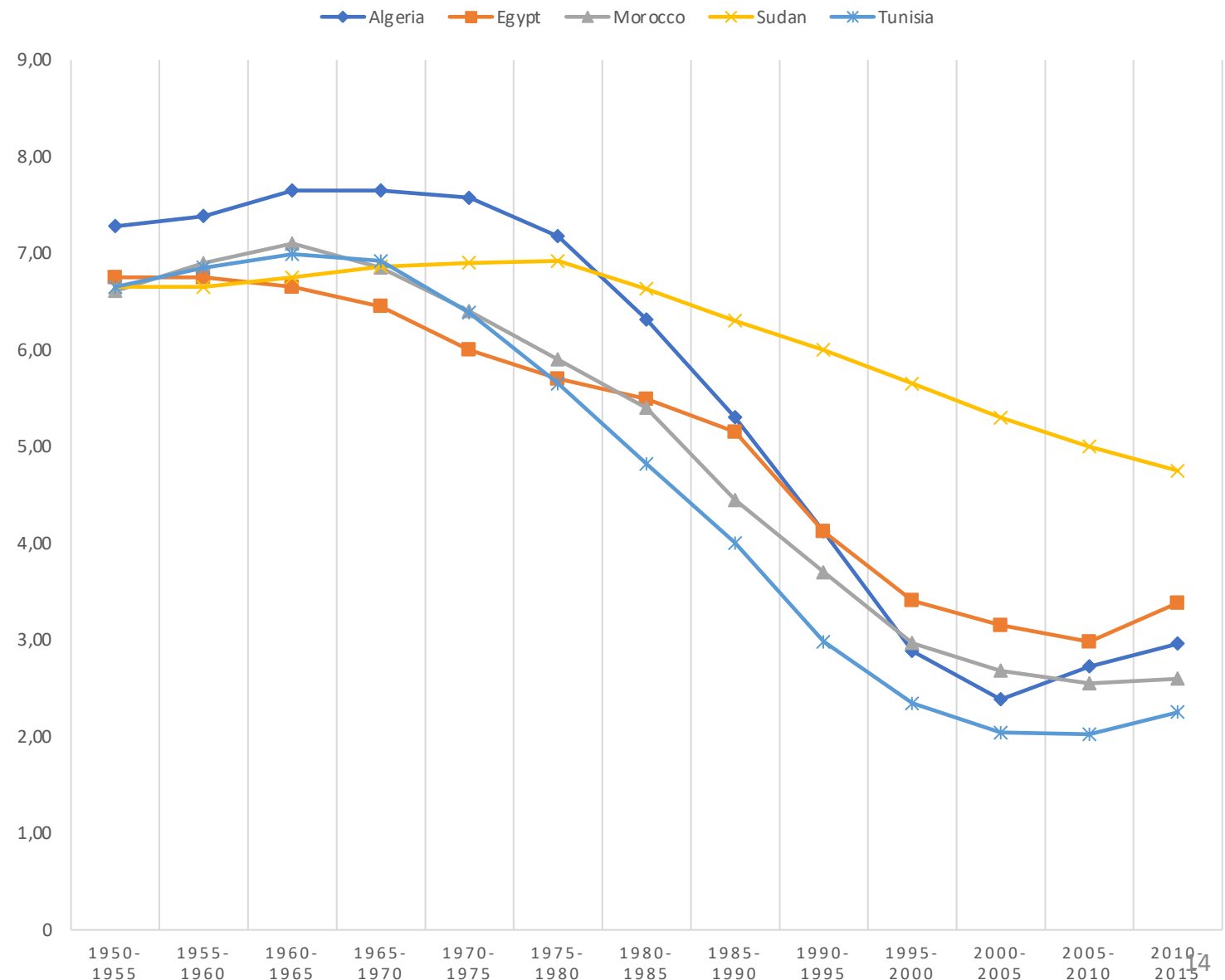
Series : Labor force participation rate, female (% of female population ages 15+) (modeled ILO estimate)
Source: World Development Indicators
Created on: 03/11/2023

A counter demographic transition in Algeria, Egypt and Tunisia ?

- 3 main explanations for Algeria
- Mini baby-boom after the violent decade (1990's)
- Very low female labor force participation rate
- Diffusion of conservatism and religious values

FERTILITY RATES IN SELECTED MENA COUNTRIES (1950-2015)

SOURCE: UNFPA, WORLD POPULATION PROSPECTS, 2017



- ### 3. Is the new macroeconomic context conducive to a change in the growth regime?
- The rise in gas prices, could be exploited to make more reforms and actually implement them but in the short to medium term, the demand for gas remains fragile:
 - The replenishment of foreign exchange reserves eroded during the oil crisis of 2014 is reducing the external constraint
 - But an increase in national gas supply requires surplus volumes once domestic demand has been met and contractual commitments to foreign partners honored.
 - Must take into account the ageing and rarefaction of oil reserves, making the short-term supply of Algerian gas low.
 - The option of exploiting shale gas resources, whose reserves would be the third largest in the world, has become seriously considered despite the resistance and protests.
 - The windfall from the rise in gas prices seems to be strengthening the fundamentals of the Algerian growth model and leaving procrastination in reforms as a permanent zero value option.

4. Ten actions for a new industrial dynamic of emergence in the industry and the knowledge based services (1)

- **Action 1: To equip Algeria with a true "State-strategist" entrepreneur and coordinator**
- **Action 2. Engage in a complete renovation of higher education and vocational training.**
 - target technological and management knowledge in the key areas of manufacturing and high value-added services.
 - The main principles of a diversification policy must in fact be based on the development of human capital formation.
- **Action 3. Target a few key industrial sectors by promoting private sector companies of intermediate size (ETI) by targeting**
 - the agriculture-biotechnology sector, the chemical-pharmaceutical sector, and the knowledge services sector.
 - The sustainable development and renewable energy sectors (wind, solar, etc.) should be targeted.
 - The digital sector and the new digital economy.
 - Training young people in artificial intelligence in order to master its skills must be an absolute national priority.
 - The renovation of the training and qualification system and of the higher education sectors must aim to develop both research (in universities and in companies) and professional training in the form of technological bachelor's degrees through apprenticeships.

4. Ten actions for a new industrial dynamic of emergence in the industry and the knowledge based services (2)

Action 4. Dynamic integration into global value chains

- Seize the opportunity of the reorganization of global value chains (GVC) on a regional basis to develop active insertion strategies in high value-added segments using skilled labor
- The factors (lower transport costs and lower wage costs) that have driven the hyper-globalization of value chains are experiencing opposite
- But at the same time the GVC in the services activities is increasing dramatically => Hyperglobalization of services and digital activities
- The share of services in world trade has become more important when expressed in value added (45%) than in gross or nominal value (23%). This difference is precisely the result of the implementation of GVC strategies by multinational firms on a larger scale. At the same time, the weight of the manufacturing sector, expressed in terms of value added, is almost twice as low (37%) as in terms of gross value (65%).
- A strategy of Algerian companies => privileging the activities of knowledge services and intangible investment (research and development, consulting, marketing, etc..) whose evolution would be favorable to the development of the knowledge economy and employment of graduates.
- Define an FDI attractiveness policy: sectoral priorities, objectives and conditionality in terms of economic benefits, modernization of their international investment promotion agencies by equipping them with a corporate social responsibility (CSR) framework, etc.
- Free trade zones or "technology parks" like the Moroccan experience in Casablanca, could accompany the system

4. Ten actions for a new industrial dynamic of emergence in the industry and the knowledge based services (3)

- **Action 5: Build comparative advantages in knowledge services**
- The diversification of the economy and the employment of young graduates must be the top priorities.
- Past choices in some countries to promote subcontracting and assembly activities in labor-intensive sectors (textiles, leather, clothing, electrical equipment, toys, etc.) have proven to be clear failures: in addition to the lack of upward movement of sectors towards higher value-added segments, incentives to increase the level of training and qualification have remained weak.
- For high-tech products, barriers to entry have become extremely high
 - Imitating the latest products (reverse engineering) stopped by the generalization of intellectual property rights since the TRIPS agreements signed by the WTO (1994).
 - Insertion into global value chains must target medium and high technology sectors of manufacturing activities such as the automobile and aerospace industries, and a focus on high value-added business services (knowledge-based services).
- Give priority to activities that are very geographically based and favorable to the development of the knowledge economy and to the massive use of graduates.
- The very fragile and volatile activities are the information services associated with support functions (computer maintenance, tertiary functions of execution, call centers, etc.)
- **Action 6. Encourage long-term technological co-contracting agreements with foreign**
 - Algerian companies must move from subcontracting agreements in industry and services to co-contracting or even OEM (Original Equipment Services) agreements stipulating the use of local executives in co-contracting subsidiaries.

4. Ten actions for a new industrial dynamic of emergence in the industry and the knowledge based services (4)

Action 7. Develop a co-production strategy that involves governments, firms and civil society

- To set up a strategy of vocational co-training: to establish a public policy declined in sectoral fields by including the new fields of activity (energy transition).
- This policy must be designed taking into account policies to improve the business climate for SMEs (taxation, accounting and land registry standards, banking and financial mechanisms).
- Developing regional infrastructures, without which the comparative advantage of proximity is not exploited. Ex. => development of a Euro-Mediterranean network of logistics platforms to accelerate the convergence of standards, particularly customs, and a professional training plan for ministries and technicians on the platforms.
- Ensuring normative convergence and legal security for long-term investments
- Ensure the efficiency of public services & promote a deconcentrated administrative model that favors the responsibilities of territorial actors
- **Action 8. Associate with industrial policy a strategy towards the diaspora**

4. Ten actions for a new industrial dynamic of emergence in the industry and the knowledge based services (5)

- **Action 9. Direct public investment differently and more effectively**
- Rentier state regime : revenues flow to the state, eroding the private sector, favoring public subsidies, public investment, and public sector hiring.
- The Algerian banking system has important assets, but also handicaps that are linked to its history and its economic and political structures.
- The hydrocarbon boom (2000s), despite the creation of the hydrocarbon regulation fund (FRR) in the early 2000s, has not been accompanied by a successful continuation of the structural reform program necessary for the diversification of the economy.
- Price volatility and perverse effects of commodity dependence (volatility is the fundamental characteristic of the natural resource curse Van der Ploeg and Poelhekke (2011)).
- The economy is necessarily often subject to negative terms-of-trade shocks, in periods of price reversals leading to a decline in real income.
- +> building the capacities that allow long-term investments to succeed, "investing in investment" (Collier's formulation (2012)). Price volatility requires anticipating the effects of volatility rather than trying to predict the evolution of revenue prices.
- 2 instruments
 - => creation of a sovereign wealth fund whose objective is to distribute revenues in an intergenerational manner in order to ensure the sustainability and consolidation of revenues during the boom.
 - => creation of a smoothing fund to smooth expenditure by setting upper and lower limits to the evolution of expenditure.

4. Ten actions for a new industrial dynamic of emergence in the industry and the knowledge based services (6)

- **Action 10. Reform the hydrocarbon revenue regulation fund and establish long-term financing mechanisms for the Algerian economy**
- April 2000, the government decided to create a hydrocarbon revenue regulation fund (FRR) => Treasury's single account at the Central Bank - the government can thus pay all public debt maturities from this fund and use the resources release
- These resources can be used to
 - (i) compensate for the loss of oil tax revenues resulting from a level of hydrocarbon revenues that is lower than forecast in the budget laws
 - or (ii) to reduce the external debt
- the use of this fund as part of the general government budget does not allow for an effective counter-cyclical macroeconomic fiscal policy.
- The tendency towards a preference for the present and maximum extraction of hydrocarbon rents has been well theorized by Robinson, Torvik and Verdier (2006).
- The question of institutions and their transformation in the Algerian case must be asked simultaneously, and closely linked, to the question of how the authorities should manage revenue volatility and long-term investment.

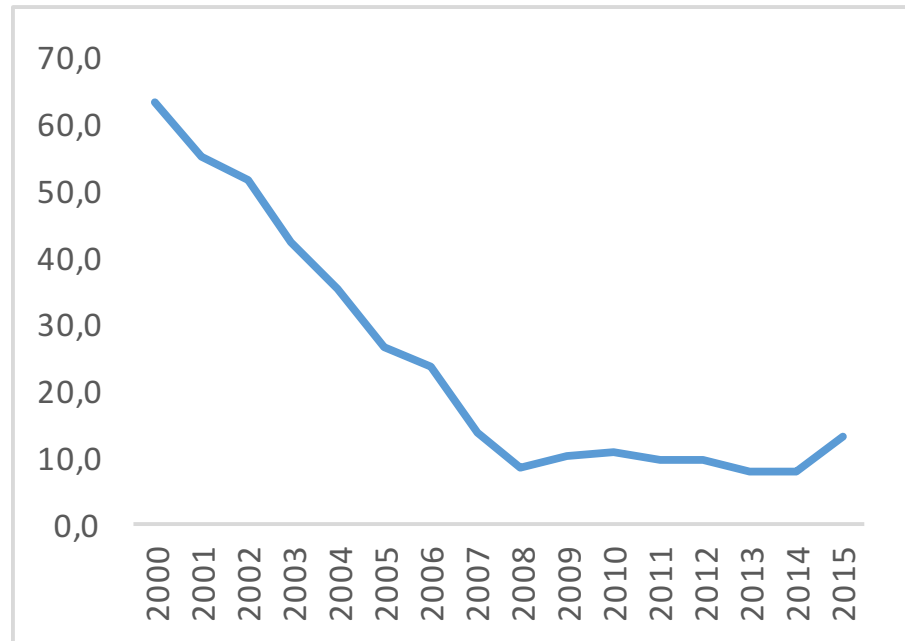
4. Ten actions for a new industrial dynamic of emergence in the industry and the knowledge based services (7)

- **Action 10. Reform the hydrocarbon revenue regulation fund and establish long-term financing mechanisms for the Algerian economy**
 - reform the FRR by making it more dynamic and using part of its resources to feed a development and consolidation fund to promote the long-term financing of the Algerian economy.
 - remodel this instrument by drawing inspiration from sovereign wealth funds that have proven their effectiveness in some oil-producing countries.
 - As Collier (2012) recommends, more than a sovereign fund, it is a "sovereign development fund" that should be established following the example of the implementation of an Algerian Caisse de dépôts et consignations whose architecture, objectives and governance principles were outlined in the Mouhoud-Plihon-Thieu report in 2016.
 - This report recommended the sustainable replenishment of the funds of this long-term financing tool by part of the resources of the FRR.

Algérie

Figure 1. Indicateurs Macroéconomiques [2000-2015]

(a) Public Debt (% GDP)



(b) Fonds de Régulation des Recettes (FRR) (US\$ billions)

