

## **The Algerian economy facing the Covid-19 pandemic: Current situation, analysis and perspectives**

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### **Abstract:**

The health crisis in Algeria and in the most countries of the world risks compromising the progress made in achieving development purposes. Indeed, the consequences of the COVID-19 pandemic go far beyond the strict health dimension. In such a context, this paper reaches to provide an analysis and an impact study of covid-19 on the Algerian economy, with the objective of proposing recommendations to face this crisis.

**Key words:** Covid-19 pandemic, Algerian economy, Perspectives.

**Jel Classification Codes:** I150, E6, O1.

## **1. INTRODUCTION**

The global economy is going through a strong recession at the beginning of 2020 caused by the spread of the Covid-19 pandemic. This slowdown has had a negative impact on the growth of economies around the world.

Following the world economic outlook reports of the international monetary fund (IMF), the contraction of the world economy in 2020 was estimated to the tune of -4.9 %. This collapse in global economic activity in 2020 is estimated to have been slightly less severe than previously projected, mainly due to shallower contractions in advanced economies and a more robust recovery in China during the second half of 2020. Hence the IMF forecasts were revised in April 2021, in particular, for the Chinese economy (+2.3%, against + 2.1% forecast in January 2021 and + 2.2 % in October 2020) and for that of the Euro Zone (-6.6%, against -6.8% in January 2021).

Following this update, the world economy is expected to record, according to the latest IMF forecasts a decline of 3.3% in 2020(International Monetary Fund 2021).

For 2021, additional stimulus measures in the United States and an accelerated recovery of the Asian economies should allow the forecast for global economic growth to be revised upwards to + 6.0%. These forecasts remain, however, surrounded by uncertainties, as to the spread of the new variants of Covid-19, the effectiveness of vaccines, the levels of sovereign debts for many countries, inflationary pressures and the responses of central banks.

After a contraction of 3.5% in 2020, economic growth in the United States of America in 2021 is expected to grow by + 6.4%. Forecasts for the Euro Zone in 2021 are estimated at + 4.4%, after a contraction of 6.6% last year. Japan's GDP in 2020 closed with a contraction of 4.8%, while it is expected to rebound to + 3.3% in 2021. In contrast, Only China remains on a positive trend in its economic growth (+ 2.3% in 2020, and + 8.4% in 2021, against + 5.8% in 2019).

For the other emerging countries, the data indicates, for 2021, that the economy of India is expected to reach 12.5% of growth, against -8.0% recorded in 2020. The growth of the Brazilian economy is estimated at +3.7% in 2021, after the contraction of -4.1% recorded in 2020. The Russian economy is expected to grow by +3.8% in 2021, compared to -3.1% in 2020.

Algeria, in turn, is facing twins shock, the Covid-19 pandemic and the simultaneous collapse of oil prices that have negatively impacted the country's vulnerable macroeconomic environment, putting the authorities in the grip of a multifaceted crisis. The rapid adoption of containment measures has helped slow the spread of the pandemic, but these have severely hampered activity in several economic sectors. The sharp fall in prices and demand for hydrocarbons on a global scale weighs heavily on external and fiscal revenues, despite the depreciation of the Algerian dinar. As a result, rapid action to reduce the dual deficit and the adoption of internal good governance rules combined with structural reforms conducive to private sector led growth is more necessary than ever.

In such a context, this contribution comes to provide an analysis and an impact study of Covid\_19 on the Algerian economy, with the objective of proposing recommendations to face this crisis.

The paper is structured as follows: After the introduction and an analysis of the recent macroeconomic and financial situation in Algeria, a model to estimate the macroeconomic impact is presented with a discussion of the results. Finally, following the previous analysis, recommendations are suggested with a conclusion.

## **2. Recent macroeconomic and financial developments**

In The following section; we analyze the dynamics of Algeria's main economic accounts: economic growth, external trade, public finances and monetary situation.

### **• Economic growth**

GDP growth had already slowed to 0.8% in 2019, compared to 1.4% in 2018, while growth excluding hydrocarbons was 2.4% in 2019 compared to 3.3% in 2018.

Growth was driven by the agriculture, construction, industry and services sectors, with increases of 2.7%, 3.8%, 3.8% and 3.0% respectively in their values added.

Conversely, the growth rate of Gross Domestic Product (GDP) excluding hydrocarbons is higher than that of GDP but slightly down compared to 2018 since it goes from 3.0% in 2018 to 2.4% in 2019, which in the context of the year 2019 constitutes a significant performance(Office national des statistiques 2020).

With the continued disruption of production since mid-January 2020, the global economy is set to enter in a recession, which will have a long-

term impact. This is not the usual business cycle in which monetary and fiscal policies can work. Fiscal policies can only slow down the decline but not prevent it, while monetary policies need to be accommodative (Kumar 2020).

In Algeria, following the collapse of oil prices and the various containment measures taken to deal with the spread of the Covid-19 pandemic, the Algerian business cycle has returned to recession. Real GDP fell by 3.6 in the first quarter and by nearly 10% in the second quarter of 2020 (Office national des statistiques 2020) and it is expected to decline by 4.7% per year according to the 2021 Finance law forecasts. The containment measures put in place have had a negative impact on all sectors of production and more important on services and construction, and caused the loss of many jobs.

Agriculture, which represents 12% of GDP, employs 10% of the working population, and covers national needs up to 73%, is the only sector that continues to record positive growth rates with 2.7% in 2019 and 2.8% in the first quarter of 2020.

On the domestic demand side, final household consumption in 2019 slowed slightly to 2.1% from 2.8% in 2018, but remains below the 3.3% growth rate of 2016. Households have effectively reduced their consumption in 2019 and are increasingly faced with trade-offs between savings and consumption.

In 2019, despite the slowdown in the consumption deflator, households are anticipating price increases and are therefore reducing their consumption in order to save for future periods. In 2020, the fall in the volume of private consumption is more significant with a rate of -1% recorded in the first quarter of 2020.

- **External trade**

Hydrocarbons are traditionally the corner stone of the Algerian economy, accounting for 93% to 95% of exports. However, since 2014, lower oil prices have gradually reduced the budget and melted foreign exchange reserves. In 2020, restrictions on the movement of people and social distancing measures taken to mitigate the spread of Covid-19 combined to the oil shock, had subsequently aggravated the situation, which

was already precarious after the significant decline in 2019. hence, Algeria experienced, during the year 2020, a significant decrease in exports with - 51% in crude oil and - 33% in natural gas compared to the previous year.

Imports of goods stood at 34.4 billion US\$ at the end of december 2020, down by 18%. This negative evolution is essentially explained by the decline in purchases of almost product groups, namely energy products, intermediate consumer goods, capital goods and semi-finished goods.

The trade deficit (-15.1 billion US\$) is expected to lead to a fall in foreign exchange reserves to 44 billion USD at the end of 2020 against 195 billion USD at the end of 2013 (Ministry of finances 2020).

- **Public finances**

The decline in oil and gas export revenues has contributed to a further widening of the public and external deficits. The budget deficit more than doubled in 2020 to 11.1% of GDP, up from 5.6% in 2019 (ministry of finances 2021), under the combined pressure of lower hydrocarbon revenues, which constitute a large share of government revenue, and a high government spending to mitigate the economic effects of the health crisis.

- **Monetary situation**

The monetary situation, at the end of 2020 (Bank of Algeria 2021) indicates a resumption of the expansion of the broad money supply M2. Indeed, after having recorded a decline of 0.78% at the end of 2019, the M2 money supply increased significantly to reach 7.12% at the end of 2020, peaking at 17 682.7 billion dinars against 16 506.6 billion DZD at the end of 2019. Excluding hydrocarbon deposits, it increased by 9.05% against 6.03% at the end of December 2019. Thus, the fiduciary circulation excluding banks increased by 12.93%, from 5 437.6 billion DZD at the end of 2019 to 6 140.7 billion DZD at the end of 2020. It represented 34.73% of the M2 money supply at the end of 2020, compared with 32.94% at the end of 2019.

### **3. Macro-econometric impact model**

The study was based on a model of the financial programming type, this type of models is used to make forecasts of the short and medium-term national accounts and allows the coherence of the four major accounts (national accounts, public finances, balance of payments and monetary situation) (International Monetary Fund 2014). It provides:

- Forecasting expenditure and revenue for the macroeconomic framework with a view to drawing up the public budget and preparing the finance law;
- Analyzing economic policies (monitoring of exchange rate, interest rate and money supply indicators and their counterparts);
- Monitoring and evaluating fiscal policies (tax revenues, budgetary expenditure, level of public debt...).

These models are sometimes used for simulating policies and the impact of macroeconomic shocks.

The model adopted is based on the assumption that the main factors impacting the growth rate in Algeria are public capital expenditure, private consumption, world demand and the price of oil (Brent). The other assumption concerns the exchange rate, which is expected to be fixed during the year.

For the year 2021, our study takes into consideration the recovery of the world economy according to the first quarter 2021 forecasts published by the World Bank and the International Monetary Fund. Indeed, the assumptions made are:

- An increase of 55 % (65 US\$) in the price of a barrel of oil compared to 2020;
- An increase in public investment expenditure of 25 % compared to 2020;
- An estimated exchange rate of 134 DZD/USD in 2021 which represent a depreciation of 5.4% compared to 2020.

#### **4. RESULTS AND DISCUSSION**

##### **• Impact on macro-economic variables**

The model simulates the reaction of the Algerian economy based on assumptions reflecting an improvement in economic activity after the gradual lifting of the containment measures. The two variables chosen are the price of oil and public investment, as these are the ones that stimulate growth in Algeria. The results are presented on the table below:

**Table 1: Main macroeconomic indicators**

	<b>Unit</b>	<b>2020</b>	<b>2021 Forecasts</b>
<b>Assumptions</b>			
Oil price	\$/barrel	41.8	65.0
Exchange rate	DA/\$	126.8	134.0
Capital expenditure	%	-	25.0
<b>Real growth rates</b>			
GDP	%	-4.8	4.2
GDP Excluding Oil	%	-3.5	3.4
Agriculture	%	1.5	6.6
Hydrocarbons	%	-9.9	10.2
Industry	%	-4.7	5.9
Construction	%	-3.9	3.9
Merchant services	%	-3.8	3.6
Non merchant services	%	-1.5	3.0
private consumption	%	-2.2	2.3
investment	%	-3.4	3.8
Inflation	%	2.4	4.2
<b>External balances</b>			
Trade balance / GDP	%	-10.0	5.6
Current account balance / GDP	%	-13.7	2.0
Balance of payments / GDP	%	-12.1	2.2
Foreign exchange reserves in months of imports	Month	12.1	16.4
<b>Fiscal balances</b>			
Budgetary revenues	Billion DZD	5 186.2	5 288.3
Budgeted oil taxation	Billion DZD	1 394.7	1 927.1
Budgetary expenditure	Billion DZD	7 162.4	8500.0
Current expenditure	Billion DZD	4 752.4	5525.0
Capital expenditure	Billion DZD	2 410.0	3017.5
Budget balance/GDP	%	-11.3	-15.5
Public debt/GDP	%	54.6	65.0

**Source:** Estimated by BOUGUERROUMI and BOUDJANA, 2021.

The economic growth in Algeria should record in 2021 a rebound of 4.2%; this performance will result of an improvement in various sectors of activity.

The hydrocarbons sector will increase by 10% according to the recovery in oil prices and the increase in the global demand, the agriculture sector come in the second position recording +6.6% in 2021 that is an increase of 5 points of percentage from its growth rate in 2020. The construction sector is estimated to be increased by 3.9% after a decrease of 3.9% in 2020. Also merchant and non-merchant services sectors will record positive growth rates of 3.6% and 3% respectively. Excluding the hydrocarbons the growth of GDP would be +3.4%.

For the demand side, both household consumption and public investment will contribute positively to the economic growth; they are estimated to increase by 2.3% and 3.8% respectively.

Concerning the external trade, our model forecasts an improvement of the trade balance which should represent +5.6% of the GDP, as a result of the increase in exports due to the increase in oil prices on one hand, and the decrease in imports under the effect of the restrictive measures taken in the complementary finance law of 2020 on the other hand. The balance of payment over GDP would be +2.2% and the foreign exchange reserves would cover 16.4 months of imports.

Finally for the public finance, the budget deficit relative to GDP is expected to be -15.7% in 2021 compared to -11.3% in 2020, due to the combined effect of a slight increase in budgetary revenues (+2%) and an increase of 25% in capital expenditures. The deterioration of the overall budget balance compared to 2020 should increase the public debt which will represent 65% of GDP after recording a rate of 54.6 % of GDP the previous year.

### • **Proposals for economic recovery**

The coronavirus pandemic has brought a new reality to all levels and sectors, especially to the economy of countries (KUMA 2020). As a result, the authorities were obliged to draw up a post-pandemic strategic plan that would allow it to be integrated into the process of designing the recovery plan and a new vision for the coming decades.



So, Algeria should prepare a post-covid strategy, which takes into consideration the adverse effects of the pandemic on all sectors, to which the economy would be the cornerstone of the strategy's return sheet, in order to remedy its repercussions on businesses, people's incomes, etc.

In this context, and with the aim of creating a relationship of confidence and trust between the authorities and the population, emergency measures of solidarity, aid and mitigation of the impact of the crisis on the population and on economic operators have been taken, but many others remain to be deployed for an effective economic recovery.

The main emergency measures taken by the Algerian government to respond to the economic challenges related to the Covid-19 health crisis include the following:

- Encourage investment by limiting the investment rule relating to partnership (rule of 51% for the Algerian part and 49% for the foreign one) to certain strategic sectors only;
- Exemption from value added tax and customs duties for inputs in certain sectors such as the pharmaceutical industry;
- Cancellation of tax penalties for the year 2020 and deferral of bank and tax schedules;
- Encourage local manufacturing of protective masks to meet national demand;
- Assistance to companies, especially small and medium-sized ones, by providing them with an emergency envelope of direct financial support, distributed in a differentiated manner according to the size of the company, the sector of activity and the region.

Below are some proposals aimed primarily at reviving the Algerian economy, social stability and building resilience to cope with future shocks and crises due to the Covid-19 pandemic:

- Establishment of governmental action coordination units, between the various stakeholders, namely the central administration and the regional and local authorities, to ensure greater efficiency of governmental action through the monitoring of the implementation of measures taken.
- Encouragement of the use of new technologies being a haven for economic operators resorting to teleworking, during this crisis;

- Encouragement of transfers from Algerians abroad by incentive mechanisms allowing them to be directed towards the financing of regional development projects in various sectors of activity;
- Monitoring, evaluation and impact assessment of the measures implemented through digital platforms developed for this purpose and coupled with mobile applications would allow for the collection of information from both the administrations and the final beneficiaries;
- Strengthening and improving regional connectivity in order to unlock the economic potential of the different regions through the improvement of road infrastructure and road networking, as well as the development of telecommunications infrastructure (connectivity of rural areas), with the aim of facilitating the development of markets and better access of populations to economic opportunities, public services, etc;
- Reducing the digital divide between the governorates, the different sections of society, small and little enterprises and large companies and improving the coverage of inland regions with fixed broadband internet, given the important role that digital technology and digital platforms can play in accessing markets and ensuring business continuity, as revealed by the current health crisis;
- Encouraging the generalization of training centers for digital technologies in all the interior regions, which would allow young graduates to be trained in technologies and innovation and which can exhibit digital solutions such as mobile applications, websites, etc.;
- Revision of the form of the social and solidarity economy, being a lever for development and for opening up the most disadvantaged, through the potential for employment that it can offer and the opportunities for wealth creation and territorial inclusion, by limiting the beneficiaries to a target population;
- Formalization of the informal sector by prioritizing it and drawing on international experiences;
- Financing of the response to Covid-19, through the enlargement of the budgetary space by the fiscal instrument and the rationalization of expenditure; the dematerialization of means of payment allowing the integration of money currently circulating outside the formal financial circuit and the establishment of innovative financing instruments focused on strengthening access to financing by

vulnerable populations, with a view to strengthening resilience to shocks.

In addition to the above-mentioned proposals, and in order to maintain a sustainable level of public spending to overcome the consequences of the Covid-19 crisis, a tax reform is essential. It should provide for a significant increase in ordinary revenue equivalent to at least 8% of non-hydrocarbon GDP by reducing the dependence of the state budget on oil taxation and returning to covering the operating budget through ordinary taxation.

In this respect, tax reform should be structured, in line with international best practice, around:

- Broadening the tax base through incentives by lowering the rates of certain taxes;
- Strengthening collection capacities by increasing human resources in a decentralized manner, generalizing deductions at source and digitalizing collection (digitalization requires the introduction of a unique identifier for the digitalization of the tax circuit allowing deductions at source, online declarations and centralization of data);
- the introduction of new taxes that affect the wealthiest strata such as wealth taxes, more realistic pricing of market services and the ecological tax;
- Another important cross-cutting reform would, on the one hand, help cushion the impact of the pandemic and the fall in oil prices on the Algerian economy and, on the other, contribute to financing economic diversification. This concerns the reform of the banking system and payment methods, which remain underdeveloped, even by MENA standards.

In order to increase the contribution of this sector to development financing, public banks should improve their governance while private banks should commit to finance the economy in the long term in a negotiable proportion of their activities.

Finally, supporting the Start up through the deployment of adequate legal and regulatory instruments, especially in the sector of digitalization, artificial intelligence and new technologies, is the driving force of the digital economy, the potential of the Algerian economy in its post-covid era.

From all the above, a macroeconomic policy of counter-cyclical recovery, through the implementation of an intelligent financing

strategy targeting the most productive sectors with positive externalities, is essential to overcome the current health crisis and avoid future crisis.

## **5. CONCLUSION**

The current health crisis in Algeria and most of the world's countries risks undermining progress towards development goals. In fact, the Covid-19 pandemic is certainly a health crisis, but its aftermath has gone far beyond the strict health dimension, reversing decades of progress in economic development and the fight against poverty.

In order to mitigate the socio-economic challenges inherent to the Covid-19 pandemic on the one hand, and to relaunch the economy on the other hand, emergency measures by the Algerian government have been taken by supporting the most vulnerable groups and by activating the levers accelerators of recovery economic. However, it would be important to apply other measures based on in-depth studies to better assess the impact of the crisis on the various sectors and subsequently the impact of these measures that they must have a more sustainable and deeper character.

Therefore, Algeria must work towards a transition towards a diversified economic model driven by the private sector, which accounts 40% of informal sector, by encouraging it, facilitating its access to credit, skills, economic land and public services and programs, thus improving its profitability and its ability to compete with the public sector and foreign companies.

Hence, it was noted that the Covid-19 crisis has led to a rethinking of behaviors, particularly with regard to the need to move towards new communication and information technologies, digitalization and artificial intelligence. The acceleration of digital transformation is therefore a pillar of an economic recovery strategy post covid-19.

Finally, the multidisciplinary response calls for greater coherence in the design and implementation of public policies during this period of profound disruption of lifestyles, with greater emphasis on sustainable development objectives.

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