QUESTIONS FOR RACHID SEKAK

ECONOMIST

Question 1

The decline in oil prices for almost three years has resulted in a weakening of Algeria's financial position, both internally and externally: a significant fall in foreign exchange reserves, a sharp drop in savings Internal, rising deficits .... Faced with this dashboard full of alarms, what room for manoeuvre is there for the new government?

The new executive will not have an easy task. There are at least two reasons for this. First, likely low prices for hydrocarbons over the medium term. Second, since the beginning of the crisis in the second half of 2014, there has been minimal reform.

Without any real effort of structural reforms apart from certain virtuous changes introduced by the Finance Law for 2017 our country has largely continued to live above its means. As a result, several worrying developments have been observed:

- A level of foreign exchange reserves which fell from $ 194 billion at the end of 2013 to $ 114 billion at the end of 2016
- A budget that moved from a balance in 2013 to a deficit estimated at 14-16% of GDP in both 2015 and 2016
- A current account balance that has gone from a positive balance of $ 1 billion in 2013 to a negative balance of about $ 26 billion in 2016
- Budgetary savings, measured by the availability in the Revenue Regulatory Fund (RIF), which fell from DZD 5563 billion at the end of 2013 to total depletion at the beginning of 2017.

The potential negative effects of the 2014 shock on economic growth and the banking sector, in particular banking liquidity, were temporarily offset partly through the use of foreign exchange reserves and an increase in domestic public debt, which rose from 8% of GDP in 2013 to 21% Of GDP in 2016.

But such an approach, quite understandable, because political and social priorities remained a priority in relation to the economic agenda, could only be temporary and transitory. They were based on an implicitly short-term vision and an anticipation of an upturn in the price of hydrocarbons and a belief that our foreign exchange reserves were large.

The situation is now more complicated because, after using up its savings, the country is in resource deficit and will probably remain so for many years to come. The new Executive therefore inherits a very difficult situation.

Admittedly more but limited margins of manoeuvre continue to exist, notably thanks to a still substantial level of foreign exchange reserves, a low level of external debt and a low level of domestic public debt.

But this room for manoeuvre cannot justify a status quo and do nothing.

The challenge remains the same for many years, that of the real desire to implement an ambitious programme of reforms to build a true production economy.

The country still has the opportunity to implement this reform program in a gradual way to mitigate the social impact. Not to do anything about structural reforms during the window of opportunity that opens up (2018- 2021) would be suicidal for future generations.

So let's stop talking about "new economic model" As the Anglo-Saxons say "action is the name of the game". It is now urgent to accelerate the pace of reforms in which everyone, apart from the rentiers, share the objectives.

Question 2

Future decisions will be painful! What do you think are the urgent measures most likely to contribute to the improvement?

I do not think we need to concentrate on "measures with immediate effect" because miracles in economics do not exist and decisions, particularly of an administrative nature, taken in haste are not the best and certainly not the most effective. There can be no single, unilateral measure but only measures that are consistent and coherent.

Therefore, it seems to me rather desirable to concentrate on two objectives over the next 3-5 years: the involves consolidating our public finances and the reviving production and exports in the hydrocarbon sector.

On the first part, it is clear that our current public finances are not sustainable. This calls for tightening of the fiscal trajectory, in the right direction, using the services of the Ministry of Finance.

Thisinvovles:

- A better control of the current State expenditure. This doubled between 2009 and 2015, rising from 2300 billion DZD to 4591 billion DZD. Is not this a sign of waste? It should also be noted that the public sector staffing costs account for more than 10% of GDP.
- A gradual but complete overhaul of the system of subsidies. Currently public social subsidies represent an important part of our GDP. They are however costly and often wrongly targeted and certainly unfair. In addition, they induce import demand due to insufficient local supply, excessive energy consumption and generate "superprofits" for importers who do not always reflect the price cuts seen in the international market.
- Seen against the "black decade", it can be understood that the economic agenda does not always fit with the political and social agenda aimed at ensuring cohesion and social stability. But there is an urgent need to replace commodity subsidies with a more targeted mechanism of direct monetary transfers to better protect the poor and to improve equity.
- There will also have to be a review of the currency exchange rate policies which currently subsidise imports and importers. Similarly, a review of the cumbersome direct and indirect subsidies to the housing sector is desirable.
- Making better use of our public investments. Many studies have shown that our public investment generates little growth and that the economic multiplier dear to Maynard Keynes did not apply in Algeria. Strengthening the CNED's real powers and expertise would facilitate such an objective.
- Better tax collection. Many experts believe that it is possible to widen tax revenues by improving the return on taxes and partially rebalancing the tax burden that is currently largely borne by employees. A new Minister of Finance who is familiar with the subject could assist such a development.

On the second part, it is clear that boosting production and exports in the hydrocarbons sector is paramount as this sector will remain our only source of income for many years to come.

Such a revival requires a significant increase in exploration effort. This requires changes in the institutional framework that is too restrictive in terms of both the current Hydrocarbons Act and taxation.

This recovery also depends on respecting the timetable for the new production capacities after their discoveries. This raises the question of the current position of Sonatrach in relation to the world's major energy companies.

Increasing hydrocarbon exports requires a substantial reduction in local consumption. Our country consumes about 50% of its produced oil and about one third of the 130 billion m3 of gas produced. This arises from generous subsidies on energy products, estimated by some analysts to more than 8% of GDP, that undoubtedly leads to enormous wastage.

In the same way, the development of renewable energies, in particular solar energy, is essential in order to obtain additional exportable quantities of gas.

All this is all the more critical as 2019 will see the expiry of a large part of current long-term gas sales contracts.

What will happen with these contracts in the context of increased competition in the gas market?

Hence we are reminded by the new Chairman of Sonatrach, with much timeliness, of the need to significantly reduce costs and improve the efficiency of our national airline.

Question 3

In terms of spending cuts, it is expected that the current trade-offs will lead to new austerity in the state budget: targeted subsidy allocation, lower capital and operating budgets, import restrictions etc. What do you think? I do not know if these choices are those of the new government but do you know of other alternatives in the current context?

It is desirable that these adjustments are coordinated and rational. They will not, however, be sufficient. Lastly, we need a programme of structural reforms, including the banking and financial sector, the labour market and education, economic governance and business climate, private sector development .... and many other topics.

The challenges are significant. The path will be long. Our country will need government stability and a broad political and social consensus.

I could develop, if you wish, more on this subject of structural reforms in an upcoming interview.

Question 4

What solutions do you advocate for financing the economy in a context where internal savings and liquidity are melting away like "snow in the sun"? The

previous initiatives on the bond market have been a bitter failure, as has the call to bank the money circualting in informal parts of the economy?

At the risk of repeating myself, our country, after having consumed its savings, is and will remain in resource deficit for many years.

This requires either reducing spending or seeking new resources. We have already talked about the consolidation of public finances. The new resources can only come from two sources: the local resources and the resources of the rest of the world.

The local resource could come artificially, from a generous refinancing of banks with monetary creation with the associated inflationary risks.

This resource could also come from an exchange rate adjustment that would favour the expansion of the oil tax base.

This local resource could come from off-shore banking savings, particularly in the informal sector. The local resource could finally result from the sale of public assets to local investors.

The resource of the rest of the world can only come from the use of external indebtedness, an increase in the flow of foreign investment or a transfer of public assets;

I will speak further in this interview on the external debt component. The use of FDI for its part raises the nagging question of 51/49, which, in my opinion, makes a lot of sense not only on the financial side but also on the technology side. The sale of assets to foreign investors remains an avenue to explore.

The financial management of the country will be complex because there are no "miracle" solutions. It will be necessary to optimize several variables, often contradictory, and make painful choices.

Question 5

What about external debt? Under what conditions will the budget deficits be at problematic levels?

The issue of external debt is a sensitive issue such as that of post-2009 credit. Politics has taken precedence over the economy and unfortunately our policies are often poorly advised. It seems to me therefore important to "de-dramatize" the subject.

Several points are important to note.

First, in the current context of our public finances and the country's resource gap ... ..External debt is no longer an option but is inevitable.

In particular, it would reduce the crowding-out effect of private investment by the Treasury's financial needs.

Secondly, it seems to me desirable not to "demonize" the external debt. Certainly there are painful memories of the late 80s and early 90s, but as I used to say: "Debt is like cholesterol .... There is good and bad. "

The good debt is that which repays itself by means of the projects it serves to finance, either by an increase in exports or by the generation of an import substitution effect. The good debt is the one that generates growth and employment.

Bad debt is the debt used to finance the balance of payments deficits of a country that consumes more than it produces. The bad debt is the debt that some use in hope of avoiding necessary macroeconomic adjustments.

We must rebuild, as soon as possible, a technical capacity at the level of our public banks and our large companies. The financial opulence of the last fifteen years and the age pyramid have undermined the available skills.

We will also need to define a clear strategy for external debt, backed up by a coherent discourse that can only be based on a multi-annual economic program to reduce public deficits and implement structural reforms.

Financial markets and banks are sensitive to speech but react to action.

The search for a sovereign rating with one of the three main international rating agencies would certainly be considered, in the case of our country, as a demonstration of a desire for transparency, a firm commitment on the paths to be taken for the restoration of the currently compromised macro-economic balances and the will to implement ambitious structural reforms.