



THE IMPACT OF THE INFORMAL ECONOMY ON ECONOMIC DIVERSIFICATION IN ALGERIA

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Abstract:

This study explores the impact of the informal economy on economic diversification efforts in Algeria. Despite various government initiatives, the informal sector to grow, posing significant challenges to formalization, fiscal policy, and sustainable development. The research aims to diagnose the structure and dynamics of the informal economy, identify the factors driving its expansion, and assess its effects on diversification strategies. Using a qualitative analytical approach, the study draws on national and international data, official statistics, and previous literature. Findings reveal that the informal economy distorts market competition, undermines tax revenue, deters foreign investment, and perpetuates structural inefficiencies. Key drivers include excessive bureaucracy, high tax burdens, low regulatory quality, limited financial inclusion, and persistent unemployment. The study concludes that the informal economy acts both as a socio-economic buffer and a barrier to long-term reform. To mitigate its negative impact, the paper recommends a comprehensive strategy focusing on institutional reform, improved governance, targeted incentives, digitalization, and expanded social protection. These measures are essential to create an inclusive, competitive, and diversified Algerian economy.

Keywords: Informal economy, Economic diversification, Algeria, Taxation, Bureaucracy.

JEL Classification Codes : E26; Q32; O55; H20; D73.



تأثير الاقتصاد غير الرسمي على التنويع الاقتصادي في الجزائر

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ملخص:

تستكشف هذه الدراسة تأثير الاقتصاد غير الرسمي على جهود التنويع الاقتصادي في الجزائر، فعلى الرغم من المبادرات الحكومية المختلفة، يواجه القطاع غير الرسمي نمو، مما يشكل تحديات كبيرة أمام إضفاء الطابع الرسمي على الاقتصاد، والسياسة المالية، والتنمية المستدامة. ويهدف البحث إلى تشخيص هيكل وديناميكيات الاقتصاد غير الرسمي، وتحديد العوامل المحفزة لتوسعه، وتقييم آثاره على استراتيجيات التنويع. وباستخدام نهج تحليلي نوعي، تستند الدراسة إلى البيانات الوطنية والدولية، والإحصاءات الرسمية، والدراسات السابقة. وتكشف النتائج أن الاقتصاد غير الرسمي يشوه المنافسة في السوق، ويقوض الإيرادات الضريبية، ويثني الاستثمار الأجنبي، ويديم أوجه القصور الهيكلية. وتشمل العوامل الرئيسية السببة لذلك البيروقراطية المفرطة، والأعباء الضريبية المرتفعة، وتدني جودة اللوائح التنظيمية، ومحدودية الشمول المالي، واستمرار البطالة. وتوصلت الدراسة إلى أن الاقتصاد غير الرسمي يمثل حاجزاً اجتماعياً واقتصادياً، وعائقاً أمام الإصلاح طويل الأمد. وللتخفيف من آثاره السلبية، توصي الورقة باستراتيجية شاملة تركز على الإصلاح المؤسسي، وتحسين الحوكمة، والحوافز المستهدفة، والرقمنة، وتوسيع نطاق الحماية الاجتماعية. تعد هذه التدابير أساسية لبناء اقتصاد جزائري شامل وتنافسي ومتنوع.

الكلمات المفتاحية: اقتصاد غير رسمي؛ تنويع اقتصادي؛ الجزائر؛ ضرائب؛ بيروقراطية؛

تصنيف JEL : E26؛ Q32؛ O55؛ H20؛ D73 .

1. INTRODUCTION

The hydrocarbon sector remains the backbone of Algeria's economy, contributing 19% of the GDP, 93% of product exports, and 38% of budget revenues from 2016 to 2021 (The World Bank, 2023). In 2022, Algeria was the fourth-largest economy in Africa, with a GDP of US\$225 billion as an official figure, while in reality, it may range between US\$240 and US\$245 billion. (Houadef, 2023)

The country aims to diversify its economy to expand its sources of income and enhance employment opportunities. In 2021, the unemployment rate stood at 12.7% of the total labour force, with youth unemployment at 31.9%. (The World Bank, 2023)

In 2014, Algeria faced a severe crisis due to a 40% drop in fuel revenues due to the decline in oil prices. This decline led to a decline in all economic indicators. The COVID-19 pandemic further exacerbated the economic situation. As a result, the growth rate, according to IMF estimates, declined by 6% in 2020. (Cilliers & Kwasi, 2023)

In addition to these two 'circumstantial' crises, Algeria is also facing a deep structural crisis in terms of economic and social development, as well as a crisis related to the economic model that has been adopted for over 40 years. It has also been unable to produce an elite group of creative public and private contractors to lead the process of economic and social development. Some contractors have exploited weaknesses in the administration of public property, allowing them to capture the majority of hydrocarbon revenues. This was accomplished through subsidies, tax exemptions, and generous public bank loans. This has generated an informal economy that now competes with the organized economy in almost every sector of activity. This poses a threat to the economy due to its size, whether it be the monetary mass it deals with or the volume of operations. All statistics indicate that this is a fragile and inappropriate situation. The main danger of this type of economy is that it is focused on trade rather than production and is dominated by the 'predatory, plundering' side rather than the unregulated 'subsistence' economy. (Shafir, 2021, p. 5)

This is considered one of the biggest obstacles to transforming the economy from rent-seeking to production and diversification.

Study problem:

Main problem :

- In what ways does the informal economy in Algeria impede efforts toward economic diversification?

Sub questions:

- What are the reasons for the growth of the informal economy in Algeria?
- How does the informal economy impede economic diversification in Algeria?
- What measures have been implemented by the Algerian government to mitigate the impact of the informal economy on the country's economy?

Methodology:

The methodology used in this study relies on examining available data from a range of specialized national, regional, and international bodies, as well as various

studies conducted on the informal economy, and analyzing a variety of indicators. The goal is to diagnose the status of the informal economy in Algeria and identify the challenges it poses to achieving economic diversification in the country.

Objectif of the Study:

This study aims at:

- Understanding the size and nature of the informal economy,
- Identify the reasons that contributed to the intensification of the informal economy phenomenon.
- Understanding the barriers that prevent informal businesses from transitioning to the formal economy and contributing fully to the economy.
- Assessing the impact of the informal sector on economic diversification efforts.
- Formulating recommendations for integrating informal businesses into the formal economy, with the aim of supporting economic diversification.

Importance of the Study:

The importance of this study lies in clarifying the prevailing economic reality in Algeria, of which the informal sector constitutes a large part, and its implications for the Algerian government's efforts to diversify the economy.

Literature Review:

A plethora of studies and research has emerged, on issues of the informal economy. In this section, we will provide a concise overview of the relevant studies that form the foundation of our own research.

- Souag, Adair, and Hammouda (2018) critically assess Algerian statistical data on the informal sector, estimating that it accounted for over one-third of total employment between 1997 and 2013. revealing that the contraction of public sector employment led to a marked expansion of informal employment, particularly among young, less-educated individuals in precarious jobs within very small enterprises. And they highlight the predominance of small production units operating without formal premises, mainly in retail trade, hospitality, construction, manufacturing, and transport sectors. (SOUAG, ADAIR, & HAMMOUDA, 2018)
- Bouriche and Bennihi (2020) estimate the size of Algeria's informal economy from 1980 to 2019 using the Currency Demand Approach, finding an average size of approximately 21% of official GDP. They identify the tax burden as a significant determinant, suggesting that tax policies have not effectively curbed the growth of the informal economy. (Bouriche & Bennihi, 2020)
- Zerrouki, Dahmani, and Chebbah (2022) examine the relationship between government expenditure on education and the size of the informal economy from 1970 to 2019. Their study concludes that increased educational spending negatively impacts the informal economy's size, emphasizing the role of quality education in raising awareness about the risks of informal activities. (Zerrouki, Dahmani, & Chebbah, 2022)

The reviewed studies highlight the multifaceted nature of the informal economy in Algeria, influenced by economic policies, institutional frameworks, and educational

factors. The extant literature on this subject has predominantly focused on the economic contribution of the informal sector, as measured by such indicators as GDP, employment, and the amount of money it generates. The present study will focus on analysing its impact on the government's plans to diversify its economy, with a view to providing insights into the effectiveness of its policies in achieving this goal.

2. Definition of The Informal Economy

The term "informal economy" refers to the operation of an economic sector that is not accounted for or authorised and finances its operations through activities that generate illicit income. The term encompasses all activities that are not officially registered or recognised by the government, including those that take place within the black market. The phenomenon has a detrimental effect on the economic system, facilitating the flow of funds, trade, and labour exchange between individuals and businesses outside of legal channels and government oversight. (Patel, 2020)

The informal economy is defined by governments as the part of the economy that does not have annual accounts, is not subject to taxation, is not subject to any form of government oversight, does not belong to the Chamber of Commerce, and is not included in the gross national product. Its workers are outside the formal economy, not on anyone's payroll, and earn their living in the informal sector. These enterprises are engaged, at least partly, in producing goods and services for the market. The informal sector comprises small, unincorporated private enterprises that are not registered under national laws. (UNESCO, 2015)

3. The reality of the Informal Economy in Algeria

The informal economy in Algeria has undergone successive phases of expansion, significantly altering the structure of the national economy, social dynamics, and institutional integrity. It is evident that, over time, this entity has evolved into a predominant force, which has infiltrated pivotal sectors such as wholesale trade, finance, real estate, and public procurement. This pervasive influence operates predominantly beyond the confines of formal legal and regulatory frameworks. This pervasive informality has had a deleterious effect on economic indicators, reduced the accuracy of national accounts, and impeded effective policymaking. The state's fiscal capacity is further undermined by the substantial loss of tax revenues due to unregulated informal activities. The informal economy has been demonstrated to function as a socio-economic safety net during periods of crisis, by virtue of the precarious employment and income it engenders. However, it simultaneously obstructs economic diversification, sustainable development, and the implementation of coherent public policies. The intricate networks that have been established by the powerful actors involved have resulted in the development of a parallel economic system. Despite some government efforts to integrate informal financial resources into the formal economy, these initiatives have largely lacked consistency and transparency, reflecting broader shortcomings in economic governance and policy coherence. (Temlali, 2019)

For several years, experts and observers have estimated the size of the informal economy in Algeria at between US\$40 billion and US\$60 billion. On 29 September 2021, Algerian President **Abdelmadjid Tebboune** estimated the size of the informal economy in the country at approximately 10 trillion DZ, equivalent to US\$75 billion. (Al-Estiklal Newspaper, 2021)

4. The Reasons for The Growth of The Informal Economy in Algeria

Algeria's informal economy has undergone successive phases of expansion, becoming a prominent structural feature of the national economic landscape. This growth has been fuelled by the exacerbation of existing labour market pressures resulting from demographic expansion and the cumulative effects of recurrent global crises, particularly the sharp drop in oil prices in 2014 and the subsequent emergence of the Coronavirus pandemic.

Nevertheless, the present study will concentrate on the internal factors that resulted in the propagation of this phenomenon, as outlined below:

4.1 Structural Reforms Implemented in A Hasty and Ill-Considered Manner:

The liberalisation policies implemented in the early 1980s, characterised by lax and unequal implementation, contributed to the emergence of a substantial informal economy in Algeria. This economy was interconnected with the formal economy but evaded state accountability. The distribution of income was skewed towards those with close ties to the state, who leveraged subsidised inputs and engaged in high-profit sectors. This led to the emergence of a parasitic private sector characterised by a low investment rate but a high profit rate. The paucity of declared profits signifies that a substantial proportion of wealth is outside government control, and they have a strong interest in reducing the state's dense network of administrative regulation. (Harrold, 1995)

4.2 The spread of corruption and bureaucracy:

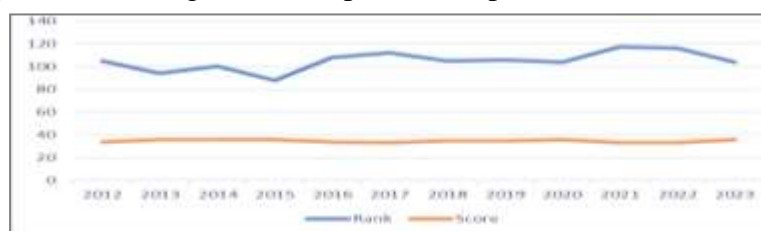
The 2023 Transparency International report indicates that Algeria ranked 104th with a score of 36 points on the Corruption Perceptions Index, which is calculated out of 100 points. This represents a three-point increase from the previous year, which places it among the most corrupt countries. (Transparency International, 2024)

Table 1. Corruption Perceptions Index (2012 – 2023)

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Rank	105	94	100	88	108	112	105	106	104	117	116	104
Score	34	36	36	36	34	33	35	35	36	33	33	36

Source : (Transparency International, 2024)

Fig.1. Score changes in Corruption Perceptions Index (2012 – 2023)



Source: Established by the authors from the data in Table 1

The figure above indicates that Algeria's index has not improved significantly over the past ten years. This has resulted in a loss of confidence among citizens in the government's ability to provide fair opportunities. Consequently, many have chosen to leave the formal sector and turn to the informal sector, despite the negative aspects.

4.3 Tax Burden:

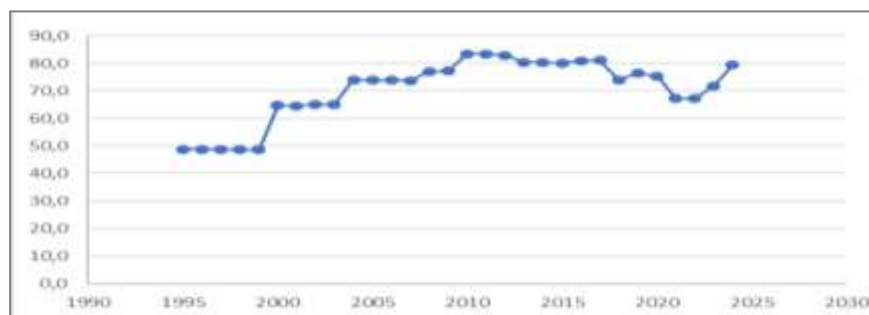
Algeria is among the highest-taxed countries, as indicated by the Index of Economic Freedom. In response to financial pressures stemming from declining oil revenues, public authorities have increasingly relied on raising taxes and fees as short-term solutions. Algerians are subject to over 35 distinct taxes, with the value-added tax (VAT) being the most significant, applied universally at a rate of 19% on most goods and services, irrespective of income level. Beyond the VAT, citizens face a wide array of taxes, including income, property, environmental, consumption, and administrative fees. This extensive taxation system contributes to a heavy fiscal burden on individuals and households. (echoroukonline, 2016)

Table 2. Tax Burden Index (1995-2024)

Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Index	48.7	48.6	48.8	48.8	48.7	64.7	64.6	65.0	65.2	74.1
Year	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Index	73.9	73.9	73.8	77.0	77.2	83.5	83.5	82.9	80.4	80.5
Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Index	80.0	81.0	81.1	74.0	76.4	75.4	67.2	67.2	71.9	79.4

Source: (Index of Economic Freedom, 2024)

Fig.2. Evolution of the tax burden index (1995-2023)



Source: Established by the authors from the data in Table 2

The above figure illustrates the instability of the tax burden and its increase from year to year. This represents the extent of the heavy tax burden in Algeria, which is due to the multiplicity of taxes, their high rates, complexity and unfairness. The high taxes have led to evasion, which has contributed to the growth and development of the informal economy.

4.4 The Widening Gap Between the Official and The Unofficial Exchange Rate:

The existence of a black market for foreign currency is an indication of the economic difficulties currently being experienced by Algeria.

Table 3. The official and the unofficial exchange rate (1994-2023)

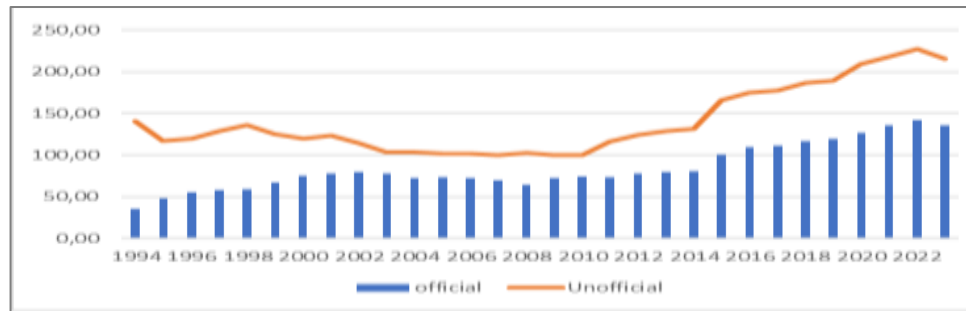
Year	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Official	35.09	47.69	54.75	57.72	58.74	66.64	75.28	77.27	79.68	77.37

Unofficial	140.08	117.43	119.65	129.17	135.55	125.31	119.41	123.20	114.23	103.08
Year	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Official	72.06	73.36	72.64	69.36	64.56	72.64	74.40	72.85	77.55	79.38
Unofficial	103.51	101.74	101.31	99.92	102.24	100.28	100.00	116.15	124.07	128.85
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Official	80.56	100.46	109.46	110.96	116.61	119.36	126.83	135.11	142.00	135.85
Unofficial	131.62	166.00	174.41	177.40	186.75	189.43	209.04	218.31	227.13	215.51

Source Official : (Bank of Algeria, 2024)

Source Un official : (Change DA, 2023)

Fig.3. The gap between the official and the unofficial exchange rate (1994-2023)



Source:

Established by the authors from the data in Table 3

The figure highlights a significant gap between the official and unofficial exchange rates in Algeria, driven by strict foreign exchange controls and the state's reluctance to let the exchange rate adjust freely. This has weakened the purchasing power of citizens, diminished trust in the national currency, and contributed to the expansion of the informal economy.

4.5 Inflation and The Low Level of Income:

Official data indicates that the average monthly wage in Algeria remains the lowest among Arab countries, ranging from 30,000 to 40,000 DZ. However, more than 55% of employees in the public and private sectors earn less than this rate (Africa News, 2022), which is insufficient to achieve sufficient purchasing power in light of inflation, which rose to 8.86% in 2022 and 9.37% in 2023. (Bank of Algeria, 2024)

The minimum wage in Algeria is 20,000 DZ per month, equivalent to US\$147.22 at the official exchange rate and US\$92.80 at the unofficial exchange rate, while the cost of living in Algeria is estimated at US\$467.7 (Numbeo, 2024), so the minimum basic wage for an Algerian employee covers only 21.12% of the cost of living.

The aforementioned factors collectively diminish the intrinsic value of individual income in Algeria, thereby engendering a considerable discrepancy between the per capita GDP and the per capita GDP according to purchasing power parity (PPP), as evidenced by the World Bank figures presented in the table below.

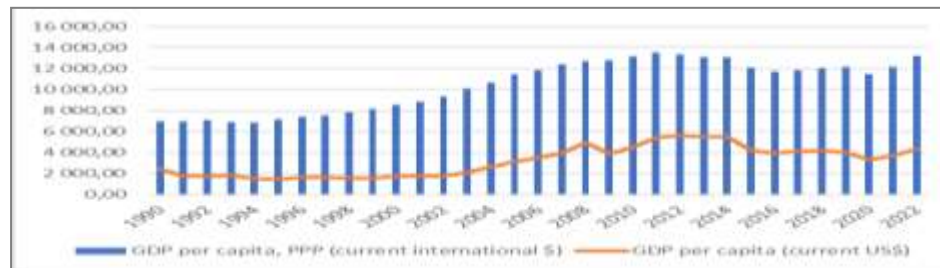
Table 4. GDP per capita PPP and GDP per capita (1990-2022)

Year	GDP per capita, PPP (current international \$)	GDP per capita (current US\$)	Year	GDP per capita, PPP (current international \$)	GDP per capita (current US\$)	Year	GDP per capita, PPP (current international \$)	GDP per capita (current US\$)
1990	6 974.08	2 431.55	2001	8 840.67	1 754.58	2012	13 347.36	5 610.73
1991	6 955.54	1 749.29	2002	9 354.22	1 794.81	2013	13 104.74	5 519.78

1992	7 075.76	1 794.62	2003	10 088.09	2 117.05	2014	13 058.12	5 516.23
1993	6 934.26	1 825.88	2004	10 653.34	2 624.80	2015	12 071.81	4 197.42
1994	6 872.21	1 522.83	2005	11 478.03	3 131.33	2016	11 685.45	3 967.20
1995	7 144.57	1 466.54	2006	11 861.17	3 500.13	2017	11 809.48	4 134.94
1996	7 441.30	1 619.53	2007	12 392.51	3 971.80	2018	12 007.77	4 171.79
1997	7 525.31	1 634.47	2008	12 714.16	4 946.56	2019	12 120.41	4 021.98
1998	7 878.21	1 610.30	2009	12 768.99	3 898.48	2020	11 452.23	3 354.15
1999	8 130.39	1 602.86	2010	13 141.12	4 495.92	2021	12 170.19	3 700.31
2000	8 510.36	1 780.38	2011	13 543.60	5 473.28	2022	13 226.79	4 342.64

Source: (The World Bank, 2024)

Fig.4. The gap between GDP per capita PPP and GDP per capita (1990-2022)



Source: Established by the authors from the data in Table 4

The figure above illustrates a substantial gap between average income and the cost of living in Algeria, especially for public sector workers. As a result, many individuals seek additional income through informal work, such as offering private lessons or operating informal taxis, thereby contributing to the expansion of the informal economy.

4.6 Unemployment and The Government's Inability to Provide Jobs:

In the aftermath of the 1986 oil crisis and the attendant economic reforms, unemployment rates began to rise in Algeria. This transition was precipitated by the adoption of a market economy and the implementation of a structural reform programme in 1994, leading to an unemployment rate of approximately 31.8% of the total labour force in 1995. (The World Bank, 2024)

According to data from the National Office of Statistics, as of the second half of 2009, 50.4% of Algeria's professionally active population - approximately 9.47 million individuals - were not registered with the Social Security Fund. An analysis of labour force data from 2001 to 2010 indicates that, in 2010, informal employment was widespread across various economic sectors. The agricultural sector had the highest share, with 84.4% of its workforce employed informally. Informality was also prevalent in the construction sector (77.8%), followed by trade, hotels, and restaurants (71.3%). In the industrial sector, 63.6% of workers were informally employed, while 49.9% of the labour force in the transportation and communication sector operated outside the formal system. (Temlali, 2019)

According to other figures that were circulated in the media in September 2014, the number of unlicensed markets that are operational on a weekly basis is approximately 1500, and approximately 100000 people are employed in these markets. According to the National Union of Trades and Artisans, 80% of officially registered

merchants fail to declare their non-permanent workers to the National Social Security Fund. (Temlali, 2019)

Not to mention the large numbers of new entrants to the labour market, which exacerbated the crisis, and according to official figures, the unemployment rate reached 11.38% in 2019, as shown in the following table.

Table 5. Employment and Unemployment Rates (2015-2019)

Year	2015	2016	2017	2018	2019
Working population	11 932 000	12 117 000	12 299 000	12 463 000	12 729 000
Actual working population	10 594 000	10 845 000	10 859 000	11 001 000	11 280 000
Rate of Actual working population	88.79%	89.50%	88.29%	88.27%	88.62%
Unemployed people	1 338 000	1 272 000	1 440 000	1 462 000	1 449 000
Rate of Unemployed people	11.21%	10.50%	11.71%	11.73%	11.38%

Source : (Bank of Algeria, 2023)

The figures in the table above, which include individuals registered with employment agencies and those not covered by the social security system, do not accurately represent the true state of the Algerian labour market. Reliable data on informal employment remains limited due to the sector's unregulated nature and the inadequacy of the national statistical system, resulting in inconsistent and incomplete datasets. This data gap complicates efforts to monitor the informal economy's evolution over time.

The persistence of high unemployment and the state's limited capacity to absorb the active labour force, particularly new entrants, have significantly contributed to the expansion of informal employment. This sector serves as a coping mechanism for individuals excluded from formal employment, as it operates without government oversight or regulatory constraints. Informal workers are typically excluded from social protection schemes and lack collective bargaining rights, placing them in vulnerable positions. Additionally, informal employment often involves longer working hours compared to the formal sector. Employers in the informal economy benefit from this arrangement by minimizing labour costs, evading taxes, bypassing legal obligations, and leveraging competitive advantages through reduced production costs and increased profit margins.

4.7 Administrative regulations and legal procedures:

The regulatory quality index reflects perceptions of the government's ability to formulate and implement sound policies and regulations that allow and promote private sector development, and the following table shows Algeria's ranking in this index.

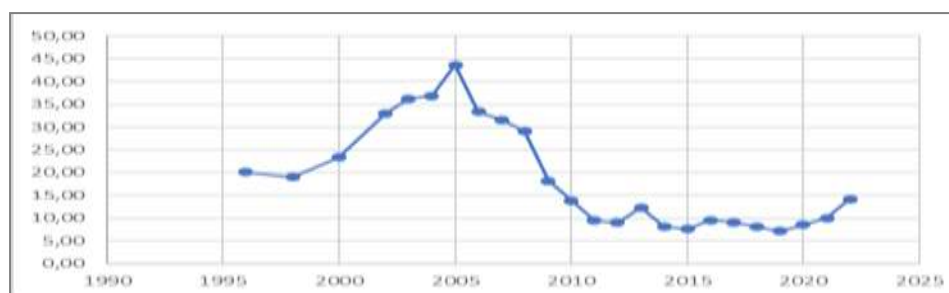
Table 6. Regulatory Quality index (1996-2022)

Year	Rank	Year	Rank	Year	Rank	Year	Rank
1996	20.11	2005	43.63	2011	9.48	2017	9.05
1998	19.02	2006	33.33	2012	9.00	2018	8.10
2000	23.37	2007	31.55	2013	12.32	2019	7.14
2002	32.97	2008	29.13	2014	8.17	2020	8.57
2003	36.22	2009	18.18	2015	7.62	2021	10.00

2004 36.82 **2010** 13.88 **2016** 9.52 **2022** 14.15

Source : (The World Bank, 2024)

Fig.5. The evolution of the Regulatory Quality Index (1996-2022)



Source: Established by the authors from the data in Table 6

The figure shows a sharp decline in Algeria's regulatory quality index, falling from 43.36 in 2005 to 14.15 in 2022. This indicates that regulatory policies during this period failed to support private sector development and instead imposed greater restrictions. As a result, many individuals turned to the informal economy to bypass these constraints.

5. The Impact of The Informal Economy on Economic Diversification

The informal economy has both positive and negative effects on the formal economy. Positively, it can support economic growth by creating jobs, generating income, and serving as a potential entry point for future formalization. However, it also undermines government tax collection, regulatory control, and the provision of public services. Additionally, it fosters unfair competition, corruption, and illicit activities, while reinforcing poverty, inequality, and social exclusion, ultimately worsening challenges within the formal economy. (Jaiswal, 2022)

The informal economy can impact the formal economy and hinder economic diversification in various ways, including:

5.1 Revenue Loss:

In response to inquiries from members of the Finance and Budget Committee of the National People's Assembly concerning the Accounting Council's report and the 2019 budget settlement, the Director General of Taxes disclosed that the General Directorate of Taxes had recorded over 4,800 billion DZ in outstanding tax revenues accumulated over several decades. This total is classified into two categories: recoverable amounts -tax revenues that can still be collected from taxpayers- amounting to 2,051 billion DZ, and non-recoverable amounts, which total 2,749 billion DZ. (fastercapital, 2024)

The informal economy can result in a significant loss of revenue for the government. It can also contribute to the generation of black money and contributing to illegal activities.

Table 7. statistics on seizures within the framework of some of the predicate offences (2017-2021) in US\$

Type of offence	Number of cases	Seized			Total amount seized
		Funds	Assets	Instrumentalities	
Drug Trafficking	49671	1 915 420,834	2 069 025	10 455 522	1 927 945 381

Corruption/Bribery	5173	274 827 790	1 485 880	238 460	276 552 130
Smuggling of goods and commodities	50265	29 657 090	-	181 465 087	211 122 177
Migrant Smuggling	1607	36 339 417	-	55 817 605	92 157 022
Fraud	3423	57 677 356	-	-	57 677 356
Tax crimes	616	5 496 445 558	-	-	5 496 445 558

Source : (MENAFATF, 2023, p. 73)

The above table illustrates the value of seized funds, assets and instrumentalities of crime, which is estimated to be approximately US\$8 billion. This inflated value is attributed to funds seized in the context of tax crimes, which are estimated to be approximately US\$5.4 billion.

5.2 Undermining Rule of Law:

The spread of informal economic activities can undermine the rule of law and weaken institutions, this leads to the erosion of trust in the government and the institutions responsible for enforcing regulations. The following table shows Algeria's ranking on the rule of law index during the period 2019-2023.

Table 8. Rule of Law Index (2019-2023)

Year	2019	2020	2021	2022	2023
Rank	81/126	83/128	88/139	94/140	96/142
Rank Change		0	+3	-6	0
Score	0.48	0.48	0.48	0.47	0.47
Score Change		0	-0,01	-0,01	0

Source : (worldjusticeproject, 2024)

The data in the table above indicates that Algeria has maintained a low ranking on the rule of law index over the past five years, reflecting weak institutional capacity to enforce laws. This has led to diminished government credibility, erosion of public trust, and the persistence of informal and illegal economic practices. Such conditions pose significant obstacles to implementing effective policies for economic diversification, as they may face resistance from those who benefit from the informal sector.

5.3 Impact on The Formal Economy and Distort Market Dynamics:

The informal economy can have a negative impact on the formal economy by distorting market prices and creating unfair competition for formal firms. Informal firms operate with lower overhead costs, avoiding tax and regulatory compliance, which can undermine the viability of formal firms and the rule of law.

Table 9. Growth rate of legitimate business activities registered in the commercial registry (2013-2022)

Year	Registered (inscriptions)	New registration (new creations)	Rate New registration	Deregistration (cessation of activities)	Rate Deregistration	Growth rate
2013	1 678 791	181 751	10.83%	106 052	6.32%	4.51%
2014	1 764 000	166 816	9.46%	96 921	5.49%	3.96%
2015	1 830 999	169 091	9.23%	107 322	5.86%	3.37%
2016	1 890 257	160 478	8.49%	106 298	5.62%	2.87%
2017	1 952 606	156 738	8.03%	97 526	4.99%	3.03%
2018	2 013 374	154 635	7.68%	96 825	4.81%	2.87%
2019	2 059 810	130 577	6.34%	86 481	4.20%	2.14%

2020	2 125 472	149 123	7.02%	83 645	3.94%	3.08%
2021	2 183 389	168 786	7.73%	110 230	5.05%	2.68%
2022	2 227 814	171 228	7.69%	128 239	5.76%	1.93%

Source : (National Center for Commercial Registration, 2024)

Fig.6. The Evolution of The Growth Rate of Legitimate Business Activities (2013-2022)



Source: Established by the authors from the data in Table 9

The figure above shows a steady decline in the growth of legally registered businesses in Algeria, largely due to the widespread informal economy, which creates unfair market conditions and discourages formal sector investment and entrepreneurship. This environment favors a concentration of economic power among a few dominant actors, limiting competition and weakening the impact of economic reforms aimed at fostering diversification.

5.4 Limited Foreign Investment Confidence:

The prevalence of an extensive informal economy can act as a deterrent to both domestic and foreign investment. Investors may be reluctant to commit resources to an economy where informal activities are prevalent, as this raises concerns about regulatory instability, property rights protection, and overall economic governance.

Table 10. The growth rate of foreign investors registered in the commercial register (2013-2022)

Year	Moral Persons		Natural Persons		TOTAL	
	Number	Growth Rate	Number	Growth Rate	Number	Growth Rate
2013	8 459	-	2 207	-	10 666	-
2014	9 224	9.0%	2 275	3.10%	11 499	7.80%
2015	9 715	5.3%	2 324	2.20%	12 039	4.70%
2016	10 321	6.2%	2 348	1.00%	12 669	5.20%
2017	10 983	6.4%	2 424	3.20%	13 407	5.80%
2018	11 537	5.0%	2 515	3.80%	14 052	4.80%
2019	12 067	4.6%	2 590	3.00%	14 657	4.30%
2020	12 390	2.7%	2 648	2.20%	15 038	2.60%
2021	9 849	-20.5%	2 802	5.80%	12 651	-15.90%
2022	10 050	2.0%	2 965	5.80%	13 015	2.90%

Source : (National Center for Commercial Registration, 2024)

Fig.7. The Growth Rate of Foreign Investors Registered in The Commercial Register (2013-2022)



Source: Established by the authors from the data in Table 10

The figure above highlights a continued decline in foreign investor growth in Algeria, reflected in fewer commercial registry registrations. This trend is largely due to the informal economy offering higher returns and lower risks, making it more appealing than the formal sector. As a result, reduced formal investment has hindered progress toward economic diversification.

5.5 Reduced Access to Finance:

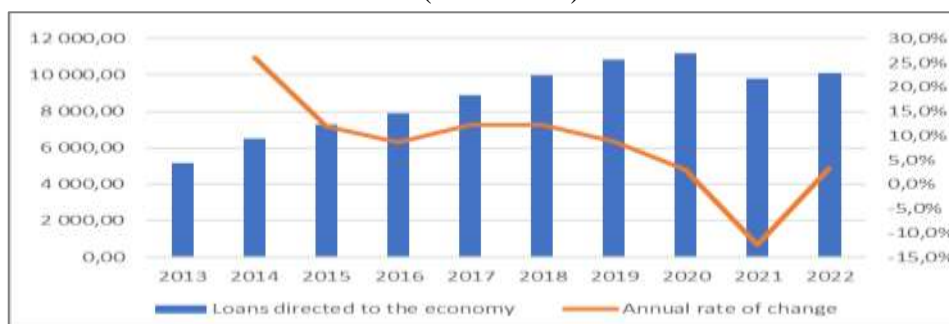
Informal businesses typically lack access to formal financial services such as loans and credit. This lack of access constrains their ability to invest in innovation, technology, and expansion, which are essential for economic diversification.

Table 11. Distribution of loans directed to the economy according to the maturity period (2013-2022)

		2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Loans directed to the economy	Short term	1 423.40	1 608.70	1 710.60	1 914.20	2 298.00	2 687.10	3 011.10	3 203.70	3 563.80	3 903.10
	Medium term	1 227.90	1 413.40	1 641.80	1 810.90	1 844.40	1 683.30	1 665.90	1 654.50	1 484.30	1 470.50
	Long term	2 505.00	3 482.50	3 924.80	4 184.80	4 737.60	5 605.90	6 180.90	6 324.10	4 746.60	4 741.60
TOTAL LOANS		5 156.30	6 504.60	7 277.20	7 909.90	8 880.00	9 976.30	10 857.90	11 182.30	9 794.70	10 115.20
Annual rate of change	Short term	-	13.0%	6.3%	11.9%	20.1%	16.9%	12.1%	6.4%	11.2%	9.5%
	Medium term	-	15.1%	16.2%	10.3%	1.8%	-8.7%	-1%	-0.7%	-10.3%	-0.9%
	Long term	-	39.0%	12.7%	6.6%	13.2%	18.3%	10.3%	2.3%	-24.9%	-0.1%
TOTAL RATE		-	26.1%	11.9%	8.7%	12.3%	12.3%	8.8%	3%	-12.4%	3.3%

Source : (Bank of Algeria, 2023)

Fig.8. The Change in the growth rate of loans directed to the economy by maturity period (2013-2022)



Source: Established by the authors from the data in Table 11

The persistent decline in loan growth in Algeria is predominantly attributable to the banking system's constrained flexibility and its predilection towards medium and large enterprises, thereby impeding access to credit for small businesses. This

exclusion has driven many economic actors towards informal financing channels, resulting in unregulated money transfers and further expansion of the informal economy. Consequently, this phenomenon has the effect of diminishing the government's capacity to mobilise the financial resources that are necessary for economic diversification and sustainable development.

5.6 Lack of Innovation and Productivity:

The innovation process is a key driver of economic development. However, informal businesses often operate with traditional methods and limited technological adoption, which can hinder innovation and productivity growth. The following table presents the rankings of Algeria over the past four years in GII compared to its GDP.

Table 12. The Global Innovation Index (GII) 2023 of Algeria 2020-2023

Year	Ranking	Innovation inputs	Innovation outputs
2020	121	111	126
2021	120	109	128
2022	115	110	118
2023	119	118	116

Source: WIPO (2023) The Global Innovation Index 2023 algeria, page 1.

From Table 12, It is evident that Algeria produces less innovation outputs relative to its level of innovation investments. This is due to the prevalence of the informal economy, which is characterized by economic activities led by individuals with limited education and skills. This results in a vicious circle of underutilization of the labour force and its inability to contribute effectively to the various economic sectors that require specialized knowledge and skills.

6. Measures Has Government Taken to Address the Informal Economy

Algeria has taken several measures and actions to try to limit the informal economy and integrate it into the formal economy. Among these measures are:

6.1 Attracting the Cash Mass in The Informal Economy into The Banking System:

This is done through several initiatives whose success or failure difficult to determine, including the following: (Temlali, 2019)

In 2011, a policy was introduced requiring mandatory check payments for transactions exceeding 500,000 DZ, along with obligations for dealers to issue invoices and register with tax authorities. However, this measure was quickly suspended following the “sugar and oil events,” during which widespread non-compliance by wholesalers led to market shortages and sharp price increases, forcing the government to reverse the policy.

In 2015, a new initiative sought to encourage informal economic actors to deposit their funds into the banking system in exchange for a lump-sum tax payment. The initiative lacked clarity regarding the definition of “illegal” activity, raising concerns about its effectiveness. Official statements provided inconsistent or vague information on its outcomes; for instance, a government bank reported deposits of only 3 billion DZ - insignificant compared to the estimated 3,700 billion DZ circulating informally.

A third initiative in 2016 involved the issuance of public bonds with attractive interest rates (5%–5.75%) to finance state expenditure and investment. Although the banking sector subscribed to nearly 158.9 billion DZ in bonds, it remained unclear whether any of this amount originated from informal sources.

Finally, in 2018, the Central Bank issued a directive to separate banks' core function of resource mobilization from financial investigations, intending to ease concerns about excessive anti-money laundering scrutiny. However, this directive was never implemented.

6.2 Tax Reforms and Registration Incentives:

- **Simplification of Administrative Procedures:** The Algerian government has streamlined the procedures required to register new businesses, thereby enabling individuals to commence economic activities with reduced requirements. This initiative is designed to facilitate the transition from the informal to the formal economy, and to simplify the laws regulating businesses to encourage informal businesses to transition to the formal economy. (Cilliers & Kwasi, 2023)
- **Tax Exemptions and Incentives:** Temporary tax incentives have been provided to small and medium-sized enterprises transitioning to the formal sector, such as partial or full tax exemptions for a specific period to encourage registration and compliance with the laws. Furthermore, the government has undertaken a comprehensive tax system reform, including a reduction in certain taxes, and the introduction of temporary tax exemptions and incentives for first-time registrations. (BIT Atlas, 2024)

6.3 Financial support programs for Small and Medium-Sized Enterprises:

with a view to encouraging investment and promoting the growth of small businesses. It has introduced financing programs through agencies such as the National Agency for the Support of Youth Employment (ANSEJ). These agencies provide soft or interest-free loans to finance small and medium-sized enterprises, which are the group that most often operates in the informal sector. The overarching objective of these initiatives is to motivate young entrepreneurs to engage with the formal economy by offering financing programmes, tax benefits, and advisory services. (Musette, 2019)

6.4 The Facilitation of Access to Bank Financing:

The government has implemented measures to enhance access to bank financing for informal business owners, thereby enabling them to formalise their activities and integrate into the formal economy. Furthermore, the government has encouraged the utilisation of the banking system by establishing bank accounts for institutions and individuals operating within the informal economy. Furthermore, it has facilitated access to loans and formal financial resources, thereby contributing to the economic empowerment of individuals and businesses operating within the informal economy. (BIT Atlas, 2024)

6.5 Strengthening Oversight and Tightening Penalties:

The Algerian government has increased inspection and monitoring measures for informal markets and economic activities, especially in major cities. Economic

inspectories have been assigned the responsibility of enhancing oversight of enterprises that fail to register their activities or function beyond the confines of the established legal framework. Furthermore, the government has reinforced penalties for businesses that fail to comply with the law. Businesses that continue to operate outside the formal economy are subject to strict penalties, including fines and legal prosecution. (Ministry of Internal Trade and National Market Control, 2023)

6.6 Promoting the Use of Digitization and Technology:

The Algerian government has initiated the development of a digital system for the registration of companies and economic transactions, with the objective of enhancing online registration and administrative procedures. This initiative is designed to facilitate the transformation of informal activities into formal ones, with the overarching objective being to enhance transparency and reduce informal operations. The administration of taxes has also been improved through the use of digital technology to track economic activities and reduce tax evasion, and the encouragement of electronic payments and the reduction of cash transactions is part of the government's efforts to reduce the prevalence of cash transactions in the informal economy. This objective is pursued by encouraging businesses and commercial entities to adopt digital payment methods. (International Trade Administration, 2024)

6.7 Reforming the Labour Market and Social Protection Through:

- **Expanding the Scope of Social Protection:** Social security programs have been expanded to include a wider range of informal workers, encouraging these workers to register for health insurance and retirement benefits. (Merouani, Messekher, Hamaizia, & Ait Belkacem, 2023, p. 39)
- **Vocational Training Programs:** The government has launched programs to train workers in the informal economy through vocational training to enhance their skills and guide them toward the formal labour market. (Musette, 2019)

6.8 Citizen Awareness and Sensitization:

The government-initiated campaigns to show informal business owners the advantages of engaging in the formal economy, like legal protection and social security, stable jobs, and getting bank loans, to help people understand why it's important to register their businesses legally and be part of the formal economy. (Ministry of Internal Trade and National Market Control, 2019)

6.9 Combating Corruption and Bureaucracy:

To address the bureaucracy and corruption that hinder business registration, the government has simplified procedures, adopted digital transparency tools, established institutions to combat corruption and bureaucracy, and prosecuted related crimes. (OMSAC, 2023)

7. RESULTS AND DISCUSSION

- The informal economy represents one of the biggest obstacles facing Algeria in achieving economic diversification.
- Despite some government attempts to reduce the informal economy -including efforts to integrate it and improve trade openness- tangible progress remains elusive.

- Government initiatives aimed at formalizing the informal sector have so far been ineffective due to ambiguity in economic policies and low public trust.
- Structural issues such as poor governance, administrative barriers, corruption, and a lack of competitiveness continue to feed the growth of the informal sector.
- The persistence of an informal foreign exchange market and demand for foreign currencies further illustrate the weaknesses of the formal economic system.

8. CONCLUSION

The Algerian economy is characterised by a significant reliance on hydrocarbons, with oil and gas exports constituting approximately 97% of total exports. The Algerian government is pursuing a policy of economic diversification. Nevertheless, this objective is confronted by substantial impediments, most notably the predominance of the informal economy. The informal sector has been demonstrated to engender market distortions, cultivate a milieu of illegality and opacity, and concentrate wealth in the hands of a select few, thereby discouraging formal investment. Moreover, the informal economy has been demonstrated to impede the government's capacity to collect taxes and regulate economic activity, thereby reducing the efficacy of public policies, particularly in the domains of monetary control, worker protection, and crisis response.

Recommendations

In order to address the challenges posed by the informal economy, it is recommended that Algeria adopt a comprehensive, long-term strategy involving all stakeholders, including government institutions, the private sector, civil society, and social partners. This strategy should integrate the informal economy into national economic planning and Sustainable Development Goals, supported by a strengthened statistical system and detailed field studies to better understand its scope and dynamics. Key reforms include the simplification of bureaucratic procedures, the expansion of the tax base, and the easing of tax burdens on formal businesses to enhance competitiveness. It is imperative that efforts are concentrated on enhancing governance, combating corruption, increasing transparency, and establishing a business-friendly environment. Furthermore, enhancing access to finance, education, and markets for informal actors is likely to facilitate their transition to the formal sector. It is imperative that all measures are adapted to Algeria's specific socio-economic and cultural context, in line with successful international experiences. The implementation of these reforms is expected to contribute to a reduction in the negative impact of the informal sector, while concomitantly strengthening the effectiveness of economic policy and promoting an economy that is more inclusive, diversified and sustainable.

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