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Targeted cash assistance as a reformative alternative to the universal in-kind subsidy in Algeria

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Abstract---This paper highlights the importance of replacing the Universal In-Kind Subsidy with Targeted Cash Assistance. It is structured into four sections: first, an overview of government subsidy concepts; second, a comparison of Targeted Cash Assistance and Universal In-Kind Subsidies based on various opinions and experiences; third, steps for designing a cash assistance program; and fourth, the reform of the Universal In-Kind Subsidy in Algeria. The findings indicate that Targeted Cash Assistance is more effective, though its successful implementation requires mechanisms to ensure proper targeting, a gradual reduction of in-kind subsidies, and protection for vulnerable groups.

Keywords---In-Kind Subsidy, Targeted Cash, Subsidy Reform in Algeria.

Jel Classification Codes---H23, H24, H25.

1. Introduction

To alleviate pressure on the public budget and ensure subsidies reach those who truly need them, promoting both social justice and economic efficiency, the current government has opted to reassess the social subsidy policy. This is outlined in a provision within the 2022 Finance Law, which introduces a national compensation system for eligible households. This system will establish the mechanisms and procedures for managing the list of subsidized products subject

to price adjustments, as well as define the target households for direct cash transfers and the criteria for eligibility. This measure aims to reduce the negative consequences of the Universal In-Kind Subsidy by shifting to a more focused model of targeted cash assistance. This approach involves identifying actual income to separate those who require support from those who do not. However, its success depends on implementing a set of necessary mechanisms and requirements.

Statement of the problem

What are the options available to Algeria for reforming the Universal In-Kind Subsidy?

To address this issue, this work has been divided into four sections, as follows:

- Concepts of Government Subsidies.
- Opinions and Experiences on the Comparison Between Targeted Cash Assistance and Universal In-Kind Subsidy.
- Steps for Designing a Cash Assistance Program.
- Reforming the Universal In-Kind Subsidy in Algeria.

2. Concepts of Government Subsidies

2.1. Definition of Government Subsidies

Government subsidy policies are part of the economic strategy aimed at achieving overall stability and ensuring a decent standard of living for all members of society (Mahoudar, 2012). Subsidy is also defined as any intervention in prices that lowers the price of a service for the consumer below the market price, or reduces costs for both producers and consumers, through direct or indirect support (Ismail, 2016).

The United Nations Development Programme defines subsidy as a government financial contribution that provides an advantage, either directly or through an intermediary. Subsidy can be described as the financial burden that the state budget assumes to cover the price differences of goods and services relative to their economic prices, as part of its social, economic, and political responsibilities (Ghazal & Hamed, 2009). In this context, it represents a financial contribution made by the government or a public entity, which provides a benefit to the recipients in order to achieve various goals (Mahoudar, 2012).

2.2. Objectives of Government Subsidies

- **Promoting Economic Stability:** Subsidy policies can contribute to achieving economic stability by reducing economic fluctuations and promoting sustainable growth.
- **Improving Income Distribution:** Subsidy policies can target specific segments of society to improve income distribution and reduce the gap between social classes.
- **Supporting the Poor and Vulnerable Classes:** Some subsidy policies target the poor and needy to improve their living conditions and provide them with essential services.
- **Reducing the Effects of Inflation:** By supporting the prices of certain

essential goods, subsidy policies can help control inflation.

- **Achieving Social Justice:** Subsidy policies can achieve social justice goals by directing support to the most needy groups (Ali, 2024).

2.3. Types of Government Subsidies

Government subsidy forms vary between countries depending on the economic conditions each country is experiencing. Generally, government subsidies include (Nasr, 2021) :

- First, in-kind or commodity subsidies through supporting foodstuffs, petroleum products, electricity, medicine, or water.
- Second, subsidies for certain services, such as reducing the prices of public transportation.
- Third, government subsidies directed towards development purposes, such as providing concessional loans and supporting social housing.
- Fourth, subsidies for certain economic activities, such as supporting industrial zones, aiding farmers, and subsidies aimed at promoting exports.

As Schwartz has defined the forms of government subsidies as follows:

- First: Credit subsidies through providing loans with reduced interest rates.
- Second: Tax subsidies through reducing tax obligations.
- Third: Equity support in the form of government contribution to capital.
- Fourth: Government in-kind subsidies for goods and services by providing them to citizens at prices lower than market rates.
- Fifth: Cash subsidies for producers or consumers.
- Sixth: Subsidy for targeted purchases by producers through the government's purchase of goods and services from producers at higher prices.
- Seventh: Implicit payments aimed at regulating market prices.

Based on its nature, government subsidies are divided into two types:

- ❖ **Cash Subsidy:** This refers to providing monetary assistance to groups unable to work, such as the elderly, disabled individuals, widows, orphans, etc. It is also defined as granting a financial increase to the recipient's income in order to achieve specific economic or social objectives.
- ❖ **In-Kind Support:** This type of assistance involves providing goods and services to low-income and impoverished groups at reduced prices (Mourad, 2021).

3. Opinions and Experiences on the Trade-off Between Targeted Cash Transfers and Universal In-Kind Support

3.1. The Dilemma of Choosing Between Targeted Cash Transfers and Universal In-Kind Support

Economists unanimously agree that mitigating the long-term negative effects of subsidies requires boosting production and implementing an integrated economic

policy. In the short term, some suggest transitioning from in-kind support to cash transfers over a five-year period. Others argue for maintaining subsidies on essential goods and services while gradually optimizing them to promote social equity. They emphasize that eliminating subsidies altogether could have significant economic, social, and political consequences. Therefore, a more balanced approach would involve refining subsidy policies to ensure they reach those in need while enforcing strict measures to address the inefficiencies of in-kind support. The shift from in-kind support to cash transfers has significant implications, such as overcoming issues of excessive consumption and misuse. Furthermore, a consumer who receives cash support will only buy the goods and services they require, leaving the rest of the cash subsidy unused. In contrast, with in-kind support, the consumer may purchase subsidized goods and services even if they have no need for them.

For the successful implementation of a policy shifting from in-kind to cash support, it is crucial to determine the eligible individuals and exclude those who are not entitled. This can be achieved by establishing a maximum income threshold for households to qualify for cash assistance. Households with an income above this threshold will be excluded from receiving the support.

Cash support is delivered to eligible individuals by incorporating it into the salaries of government employees and the pensions of retirees. For private sector workers, the support is paid alongside their salaries, with the employer responsible for distributing the funds from the state's treasury. Additionally, It is important to differentiate between the poor and low-income groups by mapping out each category clearly. This allows for the design of tailored support programs for each group. Society might believe that expanding financial assistance benefits certain low-income segments, while providing in-kind support and free services may be more beneficial to the poorest groups (Rushdi, 2022).

The differing views on whether to eliminate, maintain, or rationalize subsidies all have valid justifications. However, some believe that replacing in-kind support with cash assistance through financial grants is a more effective solution. This would result in budgetary savings, as cash support would be focused exclusively on the targeted groups, while excluding those who are ineligible. Others oppose this view, basing their argument on the following points:

- The challenge of determining the appropriate cash allowance for various eligible groups. However, the amount can be estimated based on specialized studies of consumer incomes and overall price levels. Even if it's not set with complete precision, adjustments or increases can be made if needed.
- The absence of guarantees that essential goods will be available at prices affordable to the poor and low-income groups, potentially resulting in a decline in their nutritional standards following the removal of in-kind support. In reply, it is argued that ensuring affordable prices for essential goods is the responsibility of the state and its regulatory bodies, which should be actively enforced. Strict penalties should also be applied to those who manipulate prices.
- The possibility of inadequate compensation due to rising prices after the elimination of in-kind support, which may lead to a decline in the living standards of the poor. In reply, it is argued that if full compensation is not

achieved due to price increases, this would not be an issue, as the cash support can be adjusted to match the current market prices.

The following table outlines the advantages and disadvantages of both in-kind support and cash support.

Table 01. Pros and Cons of both In-kind and Cash Subsidy

	Pros	Cons
In-Kind Subsidy	- Alleviating poverty by providing basic goods and services to the targeted support classes at low prices. - Raising the health level of the targeted groups by improving the level of nutrition. - In-kind support is accepted by political decision-makers in the country.	- Leakage of some subsidized goods into the parallel market. - In-kind support requires greater administrative expenses compared to cash support. - All segments of society benefit from most subsidized goods such as fuel.
Cash Subsidy	- It achieves the principle of consumer sovereignty, as through monetary support the individual can choose the goods and services he needs and direct his spending towards them. - Low transportation and distribution costs, and the presence of alternatives for goods and services that the individual can compare between and choose the least expensive one. - There is no more than one price for a good or service in the markets, which avoids negative effects of production. - Cash support reduces the burden on the state budget, as only the targeted groups will benefit from it.	- There is no accurate database of the targeted support layers, and there are no programs to update them. - Cash support may be directed towards spending on goods that are religiously forbidden and inconsistent with societal customs, such as spending on alcohol and drugs. - Cash support may help raise the general price level, leading to a decrease in the purchasing power of the poor. - Policymakers in developing countries do not prefer cash support over in-kind support.

Source: Prepared by the researchers, based on: Rushdi Ibrahim Al-Sayed Abu Karima, The Economic and Social Effects of Subsidies in Egypt, Legal Journal, 2022.

3.2. International Experiences in Comparing Targeted Cash Subsidy with Comprehensive In-kind Subsidy

Reviewing support programs in developing and developed countries, it becomes clear that each country chooses a combination of support programs that it uses to achieve its own economic and social goals, as follows (Kiki, 2024):

- In Mexico, support programs include both in-kind and cash assistance. The in-kind program provides subsidies for bread and cooking oil, as well as food vouchers for discounted milk. Meanwhile, the cash assistance program benefits around 6 million households (those in the lowest 10% income

bracket). Eligibility for this program requires families to ensure their children remain in school and consistently visit health centers.

- India also combines both in-kind and cash assistance programs. Cash transfers are provided to households in the poorest rural areas to ensure a minimum standard of living, while food vouchers are distributed to low-income communities in urban areas. To be eligible for support in either case, households must participate in public employment programs (the MGNREGS), which guarantees 100 days of work per year on local community projects, with wages below the prevailing market rate.
- In Iran, after 20 years of using in-kind support, the government transitioned to cash assistance in 2008 because the previous system was seen as unfair due to its broad, blanket nature. The in-kind support was not abolished immediately but was phased out over a five-year period, with a minimum cash allowance of \$25 per person. The government also allocated higher amounts to the poorest populations in informal settlements. This transition helped reduce consumption of petroleum products by 30% in the early years of the program. Furthermore, the cash transfers played a significant role in gaining public acceptance of the shift to cash support, particularly after the government conducted an extensive media campaign to emphasize the importance of reforming the subsidy system.
- In 2005, Indonesia launched its energy subsidy reform program, adopting a gradual reduction of subsidies and implementing compensatory measures for the poor. By 2012, the government had replaced natural gas with kerosene and diesel, and reduced electricity consumption in government buildings and street lighting. Simultaneously, the savings from the subsidy reform were redirected into four main areas: cash transfers, subsidies for public transportation, increased spending on productive activities, and enhanced funding for education. Additionally, social programs were introduced to shield the poor and low-income groups from the inflationary impacts of the subsidy reform.
- The Brazilian government primarily implemented a cash transfer program called **Bolsa Família** to enhance the income of the poor, aiming to achieve two key objectives:
 - The first objective: A short-term goal focused on raising the income of the poor through cash transfers to selected households. The program used indicators to assess individuals' income levels and targeted families with incomes below \$28.
 - The second objective: A long-term goal focused on enhancing the quality of human capital as a crucial factor for economic development. Cash transfers were conditioned on strict requirements for beneficiary families, such as ensuring their children attend school and receive regular vaccinations. In return, families received \$30 per month for each child, up to a maximum of three children per family. These payments were directed to the mother, based on the assumption that she is most capable of improving the well-being of her children and family. The program was funded by allocating 0.5% of the GDP (Abu Zaid, 2019).

4. Steps to Design a Cash Subsidy Program

The First Step: The focus is on targeting the poorest groups, including those with no income or very low income, whose earnings fall below the minimum required for a decent standard of living. This includes poor households led by mothers, widows, and divorced women without support, as well as individuals with disabilities, the elderly, orphans, and those facing extreme poverty, along with unemployed children and youth.

The Second Step: Targeting Mechanism

Studies indicate that there are several targeting methods available that can be chosen to enhance the efficiency and fairness of the support program, including:

- **Household Income Indicator:** A household is eligible for support when its income falls below a pre-determined threshold.
- **Proxy Indicators of Household Living Standards:** These include factors like household size, the education level of the head of the household, the dependency ratio, the quality and location of the residence, electricity consumption, and vehicle ownership. This approach is used when it is challenging to directly assess the household's income.
- **Involving Civil Society:** This refers to working with non-governmental organizations to gather information about the living conditions of the targeted households and leveraging data from local community officials.
- **Self-targeting for Subsidized Goods and Services:** This approach is applied to subsidize goods or services for which demand is expected to decrease as income increases (lower demand elasticity / inferior goods).
- **Geographic Targeting:** This approach uses indicators that highlight low living standards in certain areas, such as the absence of public amenities, child labor, illiteracy rates among those under 15, and other relevant factors.
- **Demographic Targeting:** This approach uses indicators like the age of the head of the household and the number of children, especially daughters, to assess a household's eligibility for support.

The Third Step: Methods for Determining the Cash Support Amount

To meet the basic needs of the poor, especially for essential food items, the amount of cash support can be determined either as a percentage of the average household spending on basic food items before they enter the subsidy system, or as a percentage of the cost of a basket of essential goods and services used by the poor (with some countries estimating this to range from 5% to 25%). Pioneering countries in cash support systems, like Brazil and Mexico, have set the support amount to 25% to 50% of the income of the poorest households (Abu Zaid, 2019).

5. Reform of the Universal In-Kind Subsidy System in Algeria

5.1. Justifications for the Reform of the Universal In-Kind Subsidy System in Algeria

They can be summarized as follow (Al-Humaidi, 2022):

- The justifications and motivations for support reforms are as follows:
The current subsidy system in Algeria is universal, applying to all segments

of society without distinction between households. Ideally, a subsidy policy aimed at achieving social justice should be progressive, benefiting the poorest populations the most, ensuring that 40% of the poorest receive between 50% and 80% of the total subsidy amount. However, in Algeria, subsidies are distributed to all individuals regardless of their income levels or living conditions. As a result, the groups that benefit most are those with higher incomes, capital-intensive industries, and electricity generation plants, which consume large amounts of energy products. This is in stark contrast to low-income households, which consume far less, thereby contributing to growing income inequality.

- The challenge of multiple stakeholders and the difficulty of monitoring them with regard to the prices applied and the availability of products.
- There is a significant issue of overconsumption and waste among consumers. For example, the average Algerian consumes 247 kg of grains annually, in contrast to 140 kg in Tunisia and Morocco. This has resulted in the wastage of approximately 3 million out of the 40 million loaves of bread produced daily. Moreover, the per capita milk consumption in Algeria is 147 liters, compared to just 100 liters in the neighboring countries
- The burden of subsidy costs on the state budget is significant, with subsidies nearly equaling the budget deficit in some years. In 2018 and 2019, the ratio of subsidies to the deficit reached 92% and 86%, respectively. In certain years, subsidies even exceeded the deficit, with the ratio rising to 130% in 2017 and 117% in 2020
- The widespread issue of smuggling and the growth of informal markets stem from price distortions. It is estimated that 660,000 vehicles in Morocco and Tunisia operate year-round using fuel smuggled from Algeria. In 2013, the total amount of fuel smuggled was around 1.5 billion liters, leading to annual losses of approximately two billion dollars. Despite the closed border with Morocco, most of this smuggled fuel was routed from Tlemcen to the Berkan and Oujda regions.

The following table shows the mechanisms for implementing support policies in Algeria.

Table 02. Mechanisms for Implementing Subsidy Policies in Algeria

Subsidized goods	Describe the mechanism or the implementation of subsidy policy
First: Energy	
Petroleum products (diesel, gasoline)	- For locally manufactured products: Support for used petroleum as a raw material for converting petroleum products. - For imported products: support the selling price to the consumer.
- Electricity	- Support for natural gas used as a raw material for electricity production. - Electricity price support with a consumption tax reduction on the first social segment. - Electricity price support for the other three months.

- Cooking gas (methane gas)	- Support the price of natural gas used to produce cooking gas. - Support the price of kitchen gas with a consumption tax reduction for the lowest 20 percent of the population. - Kitchen gas price support for other income groups.
- Butane gas	- Natural gas support used to produce butane gas.
Second: Basic food commodities	
- Cereals and their derivatives	- Supporting the prices of locally produced and imported grains. - Tax reduction on the import of locally produced and imported grains.
- White sugar - Cooking oil (regular refined cooking oil)	- Determine the maximum price at consumption and the maximum profit margins at production, import, wholesale and retail distribution of ordinary refined edible oil and white sugar. - Tax reduction on import of raw materials intended for the production of sugar and cooking oil - Tax reduction on the sale of raw materials intended for the production of sugar and cooking oil.
- Milk in bags	- Support the selling price of milk powder intended for the production of packaged milk in bags. - Tax reduction on the import of milk powder intended for the production of packaged milk in bags. - Tax reduction on the sale of milk powder intended for the production of packaged milk in bags.

Source: Prepared by researchers, based on: Tariq Ismail, Government Subsidy Policies in Arab Countries, Arab Monetary Fund, Abu Dhabi, UAE, 2018.

The following table shows the development of the Subsidy structure for goods and services.

Table 04. Development of the Subsidy Structure for Goods and Services 2010-2020

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Subsidy for basic consumer goods prices	96	279	216	197	214	247	224	182	198	208	198	197
Electricity, gas and water price Subsidy	90	82	76	66	63	82	63	65	82	89	82	96

Unit: billion dinars

Source : www.dgpp-mf.gov.dz

As shown in the table above, there has been an increase in subsidies for essential food items like grains, sugar, and oil, driven by rising international market prices. This notable rise can be attributed to several factors, primarily the population growth and the increased consumption of subsidized products.

5.2. Measures Taken to Reform Comprehensive In-kind Subsidy in Algeria

The Algerian government is moving towards implementing reforms to the commodity subsidy system, with the aim of determining which households will benefit from the direct cash transfer program once it is put into effect. The National Committee has decided that eligibility for this program will be based on a precise targeting system to ensure access to public services. Subsequently, applications will be assessed according to criteria that will be defined at a later stage. To implement these reforms, the government has introduced several measures since 2016, focused on restructuring the subsidy system to direct benefits to those who need them most. These measures include a comprehensive review of government subsidies for food and energy products, the establishment of a National Committee to design subsidy reform policies, comprising relevant ministries, experts, and professional organizations. The principle of targeted support was also incorporated into the 2022 Finance Law, which mandates direct cash transfers to qualifying households. Additionally, a work plan was developed for the reform of government subsidies, along with a strategy for its implementation, including the design of an institutional and administrative framework. Furthermore, digital tools (both technical and statistical) are being developed to evaluate the impact of the reforms on the national economy, household purchasing power, and to build a comprehensive database of individual information, starting with households' regular income.

In 2016, Algeria took a significant step toward subsidy reform by gradually adjusting fuel prices for the first time since 2005. Among the measures implemented was an increase in the value-added tax (VAT) on petroleum products, which rose from 0.01 dinar per liter to 5 dinars per liter for premium gasoline, 4 dinars per liter for regular gasoline, and 2 dinars per liter for diesel. Additionally, VAT was applied to diesel, electricity consumption exceeding 205 kWh per season, and gas consumption exceeding 2,500 thermal units per season, raising the rate from 7% to 17%. These actions led to the following outcomes (Ismail, 2018):

- The price of diesel has risen from 13.7 dinars per liter to 18.76 dinars per liter, premium gasoline from 23 dinars per liter to 31.42 dinars per liter, and unleaded gasoline from 22.6 dinars per liter to 31.02 dinars per liter. These changes reflect an increase in fuel prices ranging from 34% to 38%.
- The electricity tariff has been increased by 15% to 31% for the residential and business sectors whose consumption exceeds 250 kWh per billing cycle.
- The price of natural gas has been increased by 15% to 42% for the residential and business sectors whose consumption exceeds 2,500 thermal units per billing cycle.

In line with this, at the start of 2018, the fuel price structure was revised, with an increase of 5 dinars per liter for gasoline and 2 dinars per liter for diesel. Consequently, the prices of premium and unleaded gasoline rose by 14 dinars

per liter, regular gasoline by 13 dinars per liter, and diesel by 4 dinars per liter. Despite these substantial price hikes in energy products since 2005, they remain among the lowest worldwide, highlighting the need for further efforts to expand subsidy reforms to include additional products.

5.3. Steps to Reform Subsidy in Algeria

- ❖ Subsidy removal should be gradual to minimize the impact of price shocks. The Algerian government needs to shift gradually from a universal subsidy system to a targeted cash transfer system that benefits only the poor and disadvantaged. Accordingly, prices should rise over time, reflecting current circumstances, the nature of subsidized goods and services, and their significance for different social classes in Algeria. Furthermore, priority should be given to addressing the most costly subsidies for the national budget.
- ❖ To ensure subsidies are directed only to those in need and to move away from a universal subsidy system, the Algerian government should implement a cash transfer program targeting the poor and low-income populations as part of its reform plan. This program should establish clear criteria and selection mechanisms, each with its own benefits and drawbacks. Potential criteria include household income or related indicators reflecting the standard of living, housing conditions, number of school-age children, family size, gender composition, educational level and age of the household head, residence location and distance to public services, electricity bills, child labor, demand for low-quality goods, number of disabled individuals, illiteracy rates among children under 15, and number of people living in a single room. These criteria can vary according to the specific circumstances of each country. Additionally, it is important to regularly update and digitize the information of subsidy recipients, linking it to a centralized system. The government should also verify undeclared income and wealth within the informal sector, including agricultural and livestock production.
- ❖ Reforming energy subsidies should be a key focus of Algeria's reform agenda, given their high cost, broad scope, and both domestic and international consequences. However, price increases should mainly target products that are widely consumed by high-income households and industrial sectors. For products crucial to low-income families, price hikes must be gradual and linked to consumption levels. Pricing should rise with higher consumption, particularly during peak periods such as for electricity, butane gas, and city gas. Additionally, there should be a review of gasoline and diesel prices, which remain among the lowest globally, with gradual adjustments. It is also important to encourage citizens to shift towards using liquefied gas in vehicles currently powered by gasoline or diesel.
- ❖ Establishing a more efficient and effective social protection system: The Algerian government must evaluate and revise the current social protection frameworks, determining the key areas for reform. These systems, which were designed over three decades ago during the Black Decade, are no longer aligned with today's needs. The networks that support social protection are managed by various agencies facing challenges related to budget deficits and financial sustainability. Moreover, the government should integrate these systems with targeted programs, such as poverty assessment cards for

households, and regularly assess and track the impact of subsidies across different income groups over time.

- ❖ Choosing the right economic and political conditions: Given the economic impact of the COVID-19 pandemic on the global economy, and particularly on Algeria's economy, it is challenging to implement a subsidy reform agenda, especially with the decline in oil prices and budgetary pressures. Therefore, it is essential to select the appropriate economic conditions for the gradual subsidy reform process in Algeria (Ben Khedda & Bouzkri, 2021).

6. Conclusion

The subject of social subsidies in Algeria is complex. Experts frequently urge for a thorough evaluation of the subsidy system; yet, it is evident that the existing subsidy policy in Algeria, while beneficial to citizens, possesses inherent shortcomings. The primary concern is the substantial financial strain on the public treasury, while the secondary issue is to the misallocation of subsidies to individuals who do not genuinely require them. Consequently, amending the existing subsidy policy has become imperative, transitioning from a generalized, in-kind subsidy framework to targeted cash transfers aimed at individuals who genuinely require assistance. This strategy would enhance social justice and economic efficiency, while alleviating the burden on the state's budget.

Recommendations of the Study:

It can be summarized as follows:

- The need to adopt pre-emptive measures to protect vulnerable and weak groups and mitigate the impact of lifting support.
- Establishing criteria for eligibility for targeted cash transfer measures, identifying the beneficiary groups, and developing and implementing mechanisms to ensure that support reaches the designated groups.
- Adopting an effective communication strategy that connects stakeholders involved in implementing the transition to targeted cash support, and addressing resistance to change by providing up-to-date, accurate, and reliable information through a dedicated communication platform established for this purpose.
- Gradually phasing out universal in-kind subsidies, with initial focus on products that impose a significant financial burden on the budget.
- Reviewing the wage and reward system, and moving towards establishing an economic wage that balances the effort exerted with the financial compensation, ensuring it meets the worker's or employee's needs without the need for social support

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