

# Betting On Start-Ups as an Alternative to Smes for Algeria's Economic Take-Off

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**Abstract:** This paper addresses the issue of the trade-off between SMEs or start-ups to achieve the desired economic take-off in Algeria by assessing the performance of SMEs in Algeria and what they have achieved so far, and whether they have been able to achieve the set goals. The state has also bet on the promotion of start-ups as a powerful enabler of economic take-off.

The research concluded that the SME sector has not been able to achieve the desired goal despite the resources allocated by the state to promote and develop this sector, yet the state is still counting on it along with the startup sector, because this fabric has proven its ability to achieve economic take-off.

**Keyword:** Small and Medium Enterprises; Startups; Economic take-off; Algeria.

## I. Introduction:

In order to achieve economic take-off and break out of the tunnel of dependence on hydrocarbons, Algeria has spared no effort to promote the SME sector, given its proven ability to create jobs, reduce unemployment rates, especially among youth and females, increase economic diversification, integrate production chains of goods and services, create added value, and improve the competitiveness of the national economy. In spite of all the state's endeavours, this fabric has not lived up to the expectations expected of it, and its performance has achieved very modest results.

The state has recently added to its interest in nurturing young people with new ideas and seeking to transform them into productive projects or what has become known as start-ups. This interest stems from the significant role that this type of organization has proven to be a locomotive for economic development in several countries.

**II. Problematic:** Based on the above, we pose the following question: Can startups fill the gap that SMEs have failed to bridge and achieve the desired economic take-off in Algeria?

Sub-questions: In light of the main question, we will formulate the following sub-questions:

- Have SMEs been able to fulfil the role assigned to them in supporting the Algerian economy?
- What is the importance of startups in achieving economic take-off? Will they be a substitute for SMEs?

## III. The importance of the research:

The importance of this research is that it sheds light on the reasons for the failure of SMEs to achieve the economic take-off that was hoped for after two decades of state care for this fabric, in order to correct the shortcomings and overcome the difficulties in front of them. The importance of this research also includes highlighting the importance of start-ups in achieving economic take-off and the role of the state in supporting and accompanying these companies.

**IV. Objectives of the study:** This study aims to:

- Evaluate the extent to which SMEs fulfil their role in supporting and developing the national economy.
- Highlight the importance and role of startups in achieving economic take-off as an alternative option.

**V. Methodology:** We followed the descriptive approach in order to familiarise ourselves with the theoretical aspects of the subject, and we also used some statistics and data that serve the subject of the study.

**VI. The structure of the study:** The study is structured according to the following steps:

- 1- Evaluating the performance of SMEs in Algeria.
- 2- Betting on startups in achieving economic take-off .

## Section one: Assessing the performance of SMEs in Algeria

### 1. Assessing the performance of SMEs:

The State's endeavours to improve the investment climate and facilitate doing business have resulted in the emergence of SMEs in a remarkable manner over the following years. At the end of 2022, 1,359,803 SMEs were registered, an increase of 5,71% compared to 2021 (1,267,365 SMEs). This represents a net increase of 92,438 SMEs, while the number of SMEs in 2021 increased by 2,86% compared to the previous year (1,231,073 SMEs in 2020)

#### 1.1 Contribution of SMEs to employment:

The emergence and development of SMEs has contributed to creating jobs and reducing the unemployment rate, as shown in the following table:

**Table n° 01: Evolution of the number of declared jobs during the period 2017-2022**

**U: Milliard DA**

The nature of SMEs	2017	2018	2019	2020	2021	2022
Public Enterprises	2632018	2702067	2 864 566	2968618	3114860	3288213
Private Enterprises	23452	22 197	21 085	20898	20108	19608
<b>Total</b>	<b>2655470</b>	<b>2 724 264</b>	<b>2 885 651</b>	<b>2989516</b>	<b>3134968</b>	<b>3307821</b>

Source: Ministry of Industry, SME Statistical Information Bulletins 2018-2023.

SMEs create jobs every year with an annual increase of 4,78%, 3,62%, 5,57%, 4,87% and 5,46% during the period 2017-2022 respectively. SMEs are characterised by the low cost of job creation, as studies have proven that the cost of job creation in a small or micro enterprise is three times lower than the average cost in large enterprises, and these enterprises gain this advantage through:

- ✓ The productive source is labour-intensive, unlike large enterprises, which require large investments, capital-intensive technological patterns and advanced technical skills that are not available in developing countries.
- ✓ Provides opportunities for all segments of society as it does not require technical skills, provides opportunities for inexperienced employees and workers, and is present in all regions due to its flexibility to relocate from different regions.
- ✓ Promote individual and collective entrepreneurship by creating new economic and productive activities.

#### 1.2 The contribution of SMEs to value-added creation:

The contribution of SMEs to value-added creation in the Algerian economy is increasing at an increasing rate every year, and the table below shows that the private sector accounts for the lion's share of value-added creation at more than 85%.

**Table n° 02: The Contribution of SMEs to Value Added**

**U: Milliard DA**

The nature of the sector	2017		2018		2019		2020		2021	
	%	Value	%	Value	%	Value	%	Value	%	Value
The contribution of the public sector	12,775	1291,14	12,51	1362,21	12,66	1449,22	12,233	1299,91	12,13	1426,61
The contribution of the private sector	87,225	8815,62	87,49	95,2441	87,34	10001,3	87,767	9326,55	87,49	10334,13
<b>Total</b>	<b>100</b>	<b>10106,76</b>	<b>100</b>	<b>10886,62</b>	<b>100</b>	<b>11450,6</b>	<b>100</b>	<b>10626,4</b>	<b>100</b>	<b>11760,7</b>

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Source: Ministry of Industry, Statistical Information Bulletins on SMEs N°42, 2023

### 1.3 Contribution of SMEs to economic diversification

Public sector SMEs are active in all economic sectors, mainly in the agricultural sector (36.77% of total SMEs), industry (31.84%) and services (24.22%), while private sector SMEs are concentrated in the services sector (51.74%) where they are mainly active in transport and communications, trade, hospitality and catering, services for enterprises, services for families. Crafts (23.84%) construction and public works (15.04%), industry (8.53%) and agriculture (0.61%), (Ministry of Industry, 2023)

## 2. Identifying the reasons for the failure of SMEs to achieve economic take-off in Algeria:

Although the state provided all the means to facilitate the establishment of SMEs based on its bet on the ability of SMEs to achieve economic take-off, they failed to do so, and we summarise the reasons for this in the following:

- **SMEs are not included in the financial inclusion umbrella:** SMEs suffer from the financial inclusion gap, which deprives them of the benefits of growth and increased employment and productivity opportunities, and the reason for their lack of access to credit is due to a number of determinants, namely: Public sector crowding out of the private sector, financial instability and high inflation rates resulting in increased perceptions of credit risk, rigidity of the banking sector and lack of competition between banks, weak transparency and governance of banks.
- **Sectoral imbalance in terms of investor preferences:** The dominance of private sector enterprises over the public sector (1,359,580 enterprises in the private sector compared to 223 enterprises in the public sector in 31/12/2022) is not an issue in the affiliation of these enterprises, but in the fact that the private sector enterprises that lead this fabric are mainly and largely focused on the services sector, mainly transport and communications due to their ease of materialisation on the ground and the speed of starting the activity as well as the quick profitability. Despite the importance of this sector, which cannot be overlooked as the backbone of economic life, the need for the Algerian economy to take off is to direct investments towards promising sectors such as renewable energies, agriculture, industry and tourism, which are strategic alternatives to the hydrocarbon sector and are considered reliable in achieving economic take-off.
- **Deviation of the tax expenditure policy from its objectives:** The tax expenditure policy is a strategic variable taken by the state as a way to achieve its economic development and create a stimulating and encouraging climate for investment, so that the tax expenditure policy increases capital accumulation by reducing the tax burden on the enterprise and thus increasing the self-financing capacity of the enterprise. However, the expansion of tax privileges and excessive waiver of the state's tax dues makes investors believe that the key to success is the extent of the benefits they receive and makes them reduce the importance of competition, creativity and perseverance, so the use of the tax expenditure policy should be rationalised and not focus on it alone to improve the investment climate, but to take into account other elements that constitute the investment climate for these institutions such as sources of financing, simplifying administrative procedures, facilitating procedures for obtaining industrial and agricultural property (Nacer, 2003, p. 119).
- **Lack of protection of local products from imported products:** SMEs' local products cannot withstand imported foreign products in the absence of adequate state protection for local products, and some foreign companies flood the local market at prices lower than the prices of local goods, which leads to a weakening of the competitive position of SMEs. This is exacerbated by the absence of basic concepts of quality, which reduces the ability of SMEs to open markets and is a barrier to competing with both local and foreign products.

## Section two: Betting on startups to achieve economic take-off

Startups are characterised by creativity, innovation and the ability to bring about change regardless of the circumstances, and have become a real benchmark that measures economic progress.

### 1 Start-ups and their role in achieving economic take-off:

**1.1 Concept of Start-ups:** A start-up is defined by the French dictionary Larousse as “a young, innovative company, active in the technology sector” (Larguier), and by the English dictionary as: “a business or project that has recently started” (dictionary.cambridge). a startup is defined as a new business venture that aims to develop a viable business model to meet a market need or customer issue. (Startups)

While Paul Graham defined it in his famous article on Growth as ‘a company designed to grow quickly’, and the fact that it is newly founded does not make it a startup per se. Startups don’t have to be in the tech industry, or funded by a venture capitalist or funding venture. The only thing that matters is growth, and everything else associated with startups follows growth. Good growth should be between 5-7 per cent per week, and in exceptional cases 10 per cent. (Bouchaour, page 420)

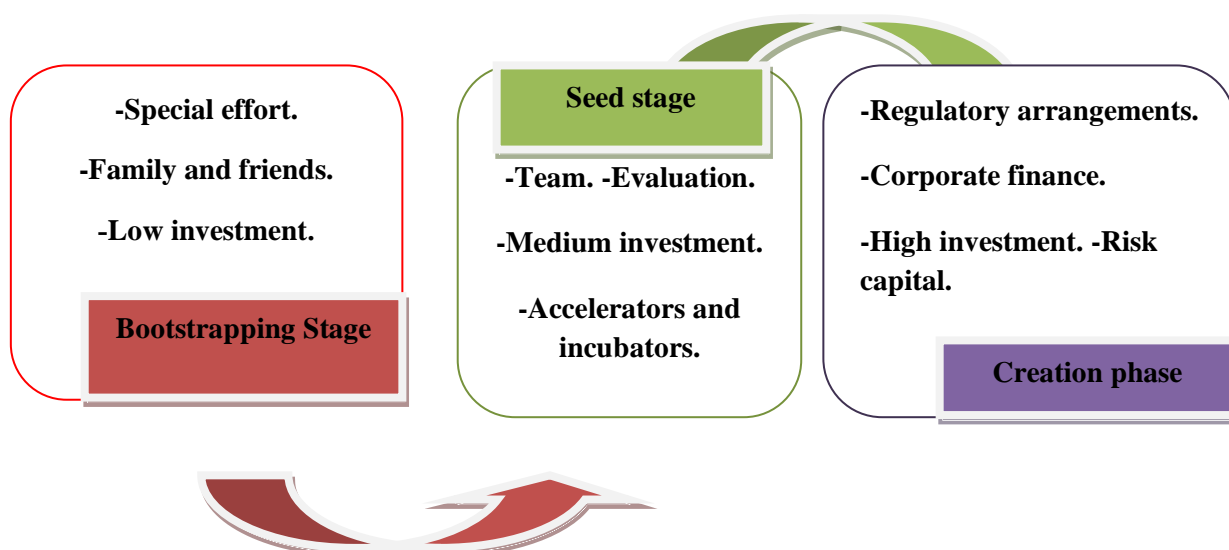
A startup is a young company founded by an entrepreneur or a group, with the aim of developing a unique product or service to launch in the market. By their very nature, traditional startups tend to have a limited business at inception and start with an initial investment amount put in by the founders or one of their relatives. A Startup is based on a scalable business and grows very quickly and efficiently compared to a traditional small or medium-sized business. SMEs need to invest a certain amount of money to enter the market, and it takes some time for them to show their returns. Startups, on the other hand, enter the market looking for capital and use technology to grow and find funding. (investopedia)

From the previous definitions, we can conclude the following about the concept of a startup:

- ✓ A young, young and unconventional organisation that seeks to achieve rapid and strong growth.
- ✓ Looking to introduce new and innovative products or services.
- ✓ Relies on modern technology services.
- ✓ Operating in a high-risk and uncertain environment.
- ✓ Seeks to make significant profits.

**1.2 Startup life cycle:** Startups, like other businesses, have a life cycle, although Startups are diverse and somewhat complex in nature, due to the different activities from one startup to another. Many studies have been developed in the field of this type of companies, in order to better understand them and their life cycle. The following figure illustrates the life cycle of a startup.

**Figure 01: The Startup Life Cycle**



**Source:** Aidin Slamzadah; Hiroko Kawamorita, Startup Companies, “Life Cycle and Challenges”, Conference Paper, January 2015, on website: <http://www.researchgate.net/>

The lifecycle of a startup varies depending on the company itself, but its lifecycle can be summarised in the following stages: (Slamzadah & Kawamorita, 2015)

- **Bootstrapping Stage:** In this very early stage, the entrepreneur or creative idea owner begins to turn his idea into a profitable project, and this stage is characterised by a high level of risk and uncertainty. But he forms a team, consisting of close people (family and friends) using personal funds at this stage.
- **Seed Stage:** After the bootstrapping stage, the founder enters a new stage, the Seed Stage. This stage is characterised by teamwork, prototype development, market entry, project evaluation, and the search for support mechanisms such as accelerators and incubators. Frankly speaking, a large number of startups fail at this stage, as they are unable to find support mechanisms and at best they will turn into a low-profit company with a low success rate. On the other

hand, those who succeed in receiving support have a higher chance of becoming successful and profitable companies.

- Creation Stage: This stage begins when the company sells its products, enters the market, and hires its first employees. Some scholars believe that entrepreneurship stops at the end of the Creation Stage. At the end of this stage, the company is formed, and corporate finance is the primary option for funding a startup, and it can also be done through venture capital.

### **1.3 The importance of startups and their role in achieving economic take-off:**

Given the pioneering role that startups play in the economic fabric, and given the experiences of others, most of the large companies that are now worth billions of dollars started as small companies from the entrepreneurial environment, which today has become an important and indispensable engine for job creation and inclusive growth, and the countries around the world are competing with each other to attract entrepreneurs and support them financially, to transform their creative ideas into productive projects that are beneficial to society and their surroundings. Countries around the world are competing with each other to attract entrepreneurs and support them financially, to turn their creative ideas into productive projects that benefit society and the environment in which they live, and to create job opportunities for young people.

The role of startups in achieving economic take-off is highlighted by the following points: (Bakhiti and Bouaouina, 2020, pp. 537-538)

- ✓ Balancing the structure of productive activity: Since most developing countries suffer from an imbalance in the structure of the economy, due to the absence of a strong base of new and innovative industries based on it, it is necessary to reduce the gap and develop strategies to fix this imbalance and expand the base of these institutions capable of development and production.
- ✓ Supporting large companies: By providing the various intermediate products they need and offering various advanced services.
- ✓ Providing real job opportunities and eliminating unemployment: Start-ups are characterised by their high capacity to create jobs.
- ✓ Investing local savings: By utilising personal savings due to small capital, and redistributing income.
- ✓ Contributing to the realisation of import substitution policy.
- ✓ Spreading positive industrial values such as quality management, creativity and innovation management.
- ✓ Contribute to achieving local development.
- ✓ The ability to innovate and develop new products and achieve high profitability.

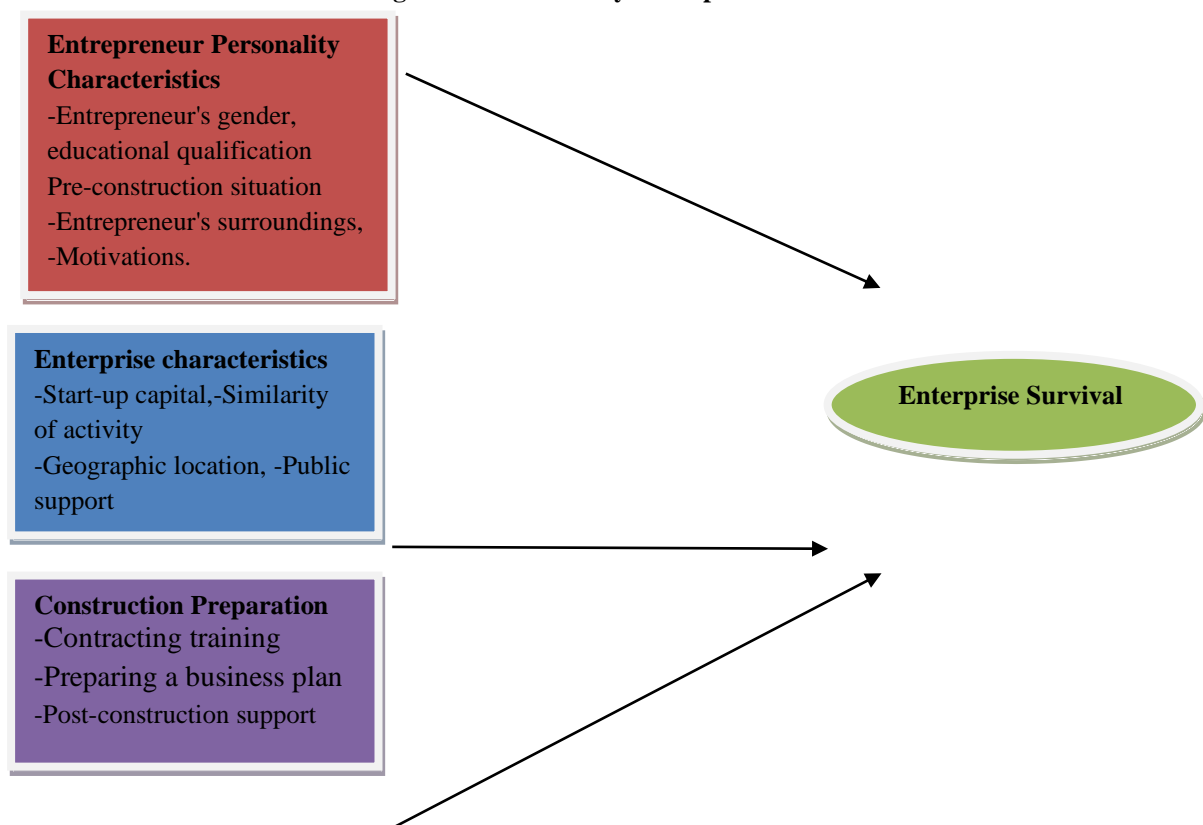
According to Wamda, a regional entrepreneurship platform, more than a dozen startups - including Bayt, Careem and Wadi.com - are valued at more than \$100 million. Souq.com, founded in 2005 and employing some 3,000 people, is set to become the first startup in the region to exceed \$1bn in estimated value. Venture capitalists are growing in capacity and numbers, for example in the UAE, which remains a hub for them, but also in Lebanon, Egypt and Jordan. This year, three lists were released to rank the brightest startups across the Arab world. The 100 Most Powerful Startups in the Arab World is made up of companies implementing the most innovative ideas and backed by the best investors across the globe, while the 100 Most Powerful Startups in the Arab World is made up of companies implementing the most innovative ideas and backed by the best investors across the globe.

## **2- The causes of startup failure and the challenges they face:**

### **2.1 Reasons why startups fail:**

The first years of an organisation's life are considered the most vulnerable to failure, only 50% of them are able to survive and continue during the first three years of their launch, and therefore many studies use the indicator of survival and continuity as an indication of the success of the organisation, and on the contrary, the early cessation of activity puts us in front of the concept of failure, where survival is the challenge that the organisation must overcome at the beginning of its life. (Tlili and Siagh, 2020, p. 779) The following figure illustrates the factors and reasons that lead to the failure of startups.

**Figure 2: Reasons why startups fail**



**Source:** Tlili Yacin, Ahmed Ramzi Siagh,2020, p.

**2.2 Startups' Challenges:** Below we will list a set of challenges facing startups, the impact of which varies from one startup to another: (Slamzadah & Kawamorita, 2015)

-Financial challenges: Finance is an integral part of the startup process and any startup will face financial issues for several reasons and at different stages. For example, while the founder is negotiating with family members and friends to convince them to invest in his idea, since the idea is still in its early stages, he may need more money to expand it. Then, in the seed stage, the founder must look for ANGEL INVESTORS and convince them with reasonable valuation schemes. Then, in the creation phase, the founder must prepare a plan along with documents and paperwork to utilise the venture capital.

-Human Resources: Startups usually start with one founder and a few co-founders. Over time, the founder needs more experts to develop the prototype, then they have to negotiate with people, build a team, and finally hire employees. This process is critical to success, and if the founder lacks sufficient domain knowledge, the startup may fail due to human resource management issues.

-Support mechanisms: There are a number of support mechanisms that play an important role in the startup lifecycle: Angel Investors, Incubators, Science and Technology Parks, Accelerators, Small Business Development Centres, Venture Capital, etc. Lack of access to support mechanisms increases the risk of failure.

-Environmental factors: Environmental factors affect many startups. Failure to take into account and study these factors, such as current market trends, limited markets, legal issues ...., etc. will affect startups and may lead them to failure. While a favourable and supportive environment facilitates the success of startups, a startup's environment is more challenging and complex than that of an established company.

### **3-Measures taken by the state to promote and support startups:**

Algerian President Abdelmadjid Tebboune, in a speech at the opening of the national symposium for startups ‘Algeria Disrupt 2020’, said that the organisation of this event ‘confirms our absolute belief in a new economic model for our country, based on knowledge, in which startups are a real locomotive for it.’ The organisation of this symposium comes about a month after the organisation of the National Symposium on Economic Revival, which brought together representatives of economic operators and paves the way for measures aimed at achieving the ultimate goal of investing in the energy and projects of young people and mobilising them in the service of the national economy.

Among the measures and procedures adopted during this seminar, and in order to encourage this type of company, the following measures were taken: (Al Shorouk Online)

-Establishing a national investment fund to finance and support startups: This funding mechanism will allow for the financing of young people with entrepreneurial and creative ideas, while avoiding the need to deal with banks and bureaucratic procedures. The fund will be financed by the state, as well as by private investors and foreign companies.

-Establishing a Higher Council for Innovation: This will be the cornerstone of the strategic direction in the field of valorising innovative ideas and initiatives and the national potential for scientific research in the service of the development of the knowledge economy.

-Establish a legal framework that defines the concepts of start-ups and incubators: as well as the terminology of the knowledge economy ecosystem, in order to facilitate the procedures for establishing these entities. In addition to the preparation of relevant regulatory texts which, will lead to the revision of existing texts. In order to adapt funding mechanisms, to the growth cycle of start-ups,

-Transforming the National Agency for the Promotion and Development of Technological Parks (ANPT) into the Ministry of Small and Emerging Enterprises and Knowledge Economy.

- Transforming the HUB for startups, which is being built by Sonatrach at the Dunia Park, to the Ministry of Small and Medium Enterprises and the Knowledge Economy.

- Enabling innovative entrepreneurs and start-ups to benefit from the spaces available within the institutions of the youth and vocational training sectors at the national level.

-The creation by local communities of spaces dedicated to start-ups, with priority given to regions with high potential for innovative entrepreneurs, especially the states of Bechar, Ouargla, Constantine, Oran, Tlemcen, Sétif and Batna, before expanding this endeavour to the entire national territory.

-The need for an in-depth reform of the tax system and all related regulations and tax incentives in favour of enterprises, especially start-ups and small and medium-sized enterprises. It is noteworthy that the 2020 Finance Law introduced new tax measures and incentives in favour of emerging enterprises, especially those active in the fields of innovation and new technologies, by exempting them from profit tax and value-added tax, with the aim of ensuring the development of their performance, allowing for the sustainable economic development of our country in the medium term. The law also includes exemptions from taxes and customs duties at the stage of exploitation, while facilitating the access of these organisations to real estate for the expansion of their investment projects. (Algerian News Agency)

### **Conclusion:**

Despite the modest results achieved by the SME sector, Algeria still attaches great importance to this sector and relies on it to advance the national economy and break the link with oil, as an economic pattern to achieve development and enhance the role of the private sector in the economic fabric. In addition, start-ups have emerged as a promising sector that must be promoted as the first building block to build a strong SME sector, which has become the main engine of the economy of many countries. From the above, we reached the following conclusions:

- It is necessary to identify and correct all the shortcomings that have hindered the role of SMEs in achieving economic take-off by working to integrate enterprises under the umbrella of financial inclusion, rationalising the tax expenditure policy, and taking into account all aspects of the investment climate.

- The startup sector is a promising sector and may be the key to achieving economic take-off, given the experiences of the leading countries, so the orientation towards this sector is imperative.

-The Algerian state plays a role of support and accompaniment for start-ups, which is reflected in the many measures taken to encourage and promote this type of companies.

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