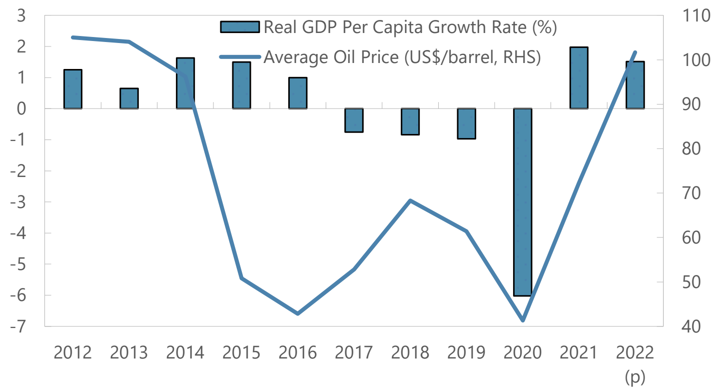
CONTEXT

1. **Boosted by high hydrocarbon prices, the Algerian economy continues to recover from the pandemic shock, but faces headwinds from rising inflation, and the prospects of a global slowdown.** Inflation has risen to its highest level in 25 years amid an upswing in international commodity prices and a confluence of global and domestic factors, including drought in 2021, loose monetary policy stance, wage increases in 2022 and tightening import regulation. Expectations of a global slowdown raise policy trade-offs in the short run, as curbing inflation and protecting fiscal sustainability will need to be balanced against supporting growth and purchasing power. Vulnerability to fluctuations in hydrocarbon prices remains high.

Text Figure 1. Algeria: Real GDP Per Capita: 2012-22



Source: Algerian Authorities and IMF staff calculations.

2. **The current conjuncture underscores once more the importance of building a resilient and diversified economy.** Successive adverse shocks since 2014 had dampened activity and reduced external and fiscal buffers. Relatively high hydrocarbon prices through the medium term, together with the emergence of new export markets, offer an opportunity to reconstitute buffers. Policy rebalancing and strengthening policy framework together with structural reforms to diversify the economy, improve and foster private sector development are critical to build resilience to commodity cycles and support inclusive growth.

3. **The consultation focused on policies to tame inflation, preserve fiscal sustainability, and foster resilient and inclusive growth.** Discussions focused on a policy-mix to stave off risks of a prolonged period of high inflation and low fiscal space, while protecting low-income groups and supporting growth. Staff also engaged with the authorities on implementation of their structural reform agenda.

RECENT DEVELOPMENTS

4. **The economic recovery continued in 2022, helped by significant terms of trade improvement.** GDP grew by 3.4 percent in 2021, supported by a rebound in hydrocarbon production, industrial activity, and construction. However, non-hydrocarbon GDP (NHGDP) growth was tepid, at 2.1 percent, following a 4.1 percent decline in 2020, due to a drought-related contraction in agricultural output and lackluster activity in services. The non-hydrocarbon sector gathered momentum in 2022Q1: NHGDP grew by 2.9 percent year-on-year compared with 2 percent in the previous quarter, driven by government consumption and recovery in agriculture.

5. The current account (CA) balance swung to surplus during the first nine months of 2022 for the first time since 2013. The CA deficit narrowed from 12.8 percent of GDP in 2020 to 2.8 percent of GDP in 2021 on a surge in exports of hydrocarbons and hydrocarbon-derived petrochemical goods together with contained increase in imports amid tight import regulation measures. This trend accentuated in 2022, with further increases in hydrocarbon prices. As a result, the CA recorded a surplus of USD 10.9 billion dollars during the first nine months of 2022 and official FX reserves increased from USD 46.7 billion at end-December 2021 to USD 58.7 billion dollars at end-November (12.7 months of imports of goods and services).

6. Rising inflation has become a major policy challenge. Average annual headline inflation picked up in 2021, reaching 7.2 percent—a level not seen since 2012. Volatile fresh food products contributed around 60 percent of this acceleration. Core inflation—which excludes fresh food products and regulated prices— accelerated to a three-year high of 6.1 percent. This trend accentuated in 2022, leading inflation to rise to 9.5 percent in August, a twenty-five-year high, before inching down to 9.2 percent in November mostly due to a slowdown in the prices of a small number of food products. The acceleration in inflation has been broad-based, affecting almost all the components of the consumer price index (CPI). It has been particularly pronounced for food prices, most of which have consistently recorded double-digit increases since December 2021.

7. Despite a slate of announced spending measures to support purchasing power and growth, an overall fiscal surplus was recorded through August. Hydrocarbon revenue doubled during the first eight months of 2022 relative to the same period in 2021. Current primary spending remained contained, rising by 2.3 percent year-on-year, and capital spending fell by 5.2 percent. The growth in spending appears low considering the measures included in the 2022 budget ("*loi de finances pour 2022*", LF2022) and supplementary budget ("*loi de finances complémentaire pour 2022*", LFC2022) to boost food supply, purchasing power and growth (Text Table 1), including a civil-service wage increase (12 percent of 2021's personnel expenses on a full-year basis) and the introduction of an allowance for first-time jobseekers. Accordingly, a fiscal surplus of 0.70 percent of the forecast 2022 GDP was recorded through August and the nonhydrocarbon primary deficit excluding Bank of Algeria's (BA) dividends (NHPD) narrowed to 17.6 percent of NHGDP, from 20.9 percent of NHGDP during the first eight months of 2021.

8. The BA strengthened the value of the dinar in 2022 to tame imported inflation. After trending lower against the dollar over the first half of 2022, the dinar appreciated against the U.S currency by 4 percent between end-July and end-August. This intensified the dinar's upward drift relative to the euro since the start of the year, as the euro slid against the U.S dollar. As a result, the nominal and real effective exchange rates (NEER and REER) appreciated by 10.7 and 8.8 percent respectively in the eleven months to end-November. Meanwhile, on the parallel FX market, the exchange-rate premium vis-à-vis the dollar and euro, which averaged at around 25 percent in 2020-21, widened to 35 percent in September-November.

Text Table 1. Algeria: Measures to Support Food Supply, Purchasing Power and Growth

Revenue
Suspension of tax and import duty increase on some food products included in the 2022 budget law
Reform of the tax regime of bakeries
Tax relief on edible oil to enhance domestic production and supply
Ten-year tax holiday on agricultural activities in new farms
Revision of the income tax schedule to reduce the taxation of lower brackets
Spending
Reinstatement of subsidies of wheat sold to agribusinesses
New monthly allowance for first-time job seekers aged below 40
Increases in salaries and pensions in the public sector
Increased transfers to state-owned entreprises involved in the supply of subsidized goods
Settlement of intra-public sector claims
Increase in capital spending equivalent to around 5 percent of GDP
Other Measures to Boost Food Supply
Ban on exports of subsidized food products
Constitution of domestic strategic reserves of cereals
Requirement to sell all domestic production of wheat and barley to the Cereal Agency (OAIC) and increase in the regulated purchase price
Monopoly of the Cereal Agency (OAIC) on the imports of pulses

Sources: IMF staff based on 2022 budget and supplementary budget laws

9. **The BA has also taken steps towards more active liquidity management, but its monetary policy stance has remained accommodative.** The key policy rate and the reserve requirement coefficient remained unchanged at historically low levels: the former had been lowered to 3 percent in May 2020 and the latter to 2 percent in February 2021. One liquidity injection operation under the special refinancing program ("*Programme Spécial de Refinancement*", PSR) was conducted in 2022 before the program expired, as scheduled, in June.[1] Boosted by the rise in hydrocarbon exports, excess bank liquidity increased to DZD 1,881 billion at end-October. However, its distribution in the banking system was highly asymmetrical due to the concentration of the

[1] The PSR was a one-year program in the amount of DZD 2100 billion (9.5 percent of GDP) launched in June 2021 to enable public banks to refinance themselves with the BA, using government debt securities received in exchange for long-term syndicated loans to SOEs which were purchased by the Treasury. See the 2021 Article IV Consultation Staff Report (CR No. 21/253) for further discussion.

deposits of the hydrocarbon sector with one bank. High excess liquidity persisted despite a small bilateral absorption operation by the BA and the early repayment of DZD 460 billion of PSR refinancing by some banks, equivalent to around 22 percent of the total stock borrowed under the program.

10. Aggregate liquidity and solvency ratios are significantly higher than minimum regulatory levels, but asset quality has deteriorated (Table 5). The expiry at the end of 2021 of pandemic-related regulatory easing measures did not generate any liquidity tensions at the aggregate level. Average solvency ratios have improved, partly due to the SOE debt buyback operations related to the PSR.[2] However, the liquidity of the Treasury notes issued well below market conditions under this operation is uncertain. NPLs have also risen substantially—to 19.3 percent at end-2021 from 14.8 percent at end-2019—and are higher in state-owned banks (SOBs). This deterioration partly reflects a denominator effect due to the PSR-related repurchase of SOE debt by the Treasury which reduced the total outstanding stock of bank lending to the economy. Profitability indicators have improved in 2021 relative to their 2020 levels.

OUTLOOK AND RISKS

11. The near-term outlook has significantly improved, mostly due to the upswing in hydrocarbon prices. Under staff's baseline scenario, the recovery is projected to have strengthened in 2022. NHGDP growth is expected to have accelerated to 3.2 percent from 2.1 percent in 2021, driven by the recovery in agriculture, stronger activity in services and steady growth in construction and industry. Hydrocarbon GDP growth is expected to have slowed to 1.7 percent, after rebounding by 10.5 percent in 2021. The external position was assessed to be stronger than the level implied by economic fundamentals and desirable policies in 2022 (Annex I). The CA is expected to have posted a surplus of 7.6 percent of GDP, reflecting a sharp rise in hydrocarbon exports, increased exports of other energy-intensive goods and only moderate increase in imports. This would drive an increase in FX reserves by USD 15.3 billion to USD 62 billion in 2022 (13.4 months of imports). Inflation is forecast to average 9.3 percent in 2022.

12. The prospects for 2023 are favorable but growth is projected to decelerate and inflation to remain high in the medium term. Under staff's baseline scenario, substantial fiscal easing (see ¶16-17) will likely raise NHGDP growth to 3.4 percent in 2023. Growth is forecast to taper off in the medium term to around 2 percent on average, as increasingly binding financing constraints would force cuts to budget spending and continued rise in bank lending to the public sector would weigh on credit to the private sector. The CA is projected to remain in surplus in 2023 and record a widening deficit from 2024 onwards, under the baseline assumption of gradual decline in hydrocarbon prices, continued growth in domestic hydrocarbon consumption and moderate rise in imports. FX reserves are projected to follow a gradual declining path to a still comfortable level of USD 45.4 billion in 2027, (8.4 months of imports, equivalent to 110.8 percent of the ARA metric).

[2] The SOE debt buyback in exchange for government debt securities reduced the asset risk weights for participating banks, and thus improved their capital adequacy ratios.

Inflation is projected to decline slightly to 8.1 percent in 2023, on base effects, easing in global cost-push factors and recent exchange-rate appreciation. Inflation is forecast to remain well above its historical average over the medium term on price inertia, sectoral price spillovers, public wage increases in 2022-2023 and persistent wide fiscal deficits.

13. **A range of risks surround the outlook.** Volatile hydrocarbon prices would significantly impact the external position and may generate destabilizing spending cycles. Signs of global slowdown and sharp swings in nonhydrocarbon commodity prices also constitute important downside risks (Annex II). Algeria is vulnerable to a range of climate risks, such as droughts, which could disrupt economic activity and raise fiscal costs. The emergence of new variants of COVID-19 could dampen growth, amid comparatively low domestic vaccination rates. On the upside, Algeria could benefit from increased investments in its hydrocarbon sector, which could boost capacity in the longer term, as more countries seek to diversify supply sources. Investment plans in the mining sector are under preparation and could also increase capacity in extractive industries and support growth and exports in the medium term.

Authorities' Views

14. **The authorities expressed strong confidence in sustained growth in the medium term**. They emphasized that structural reforms initiated in recent years, including the new investment law, will generate significant growth dividends and spur private sector activity. They concurred with staff that hydrocarbon price volatility is a key risk but considered that staff's emphasis on its importance in driving the outlook is excessive. In their view, the resilience of the Algerian economy to external shocks has materially improved and the recent sharp rise in nonhydrocarbon exports is indicative of strong progress on economic diversification. They viewed staff's projection for inflation in the medium term as pessimistic.

POLICY DISCUSSIONS

Despite a positive near-term outlook, Algeria's medium-term growth outlook faces multiple challenges, while external and fiscal vulnerabilities are high, particularly considering high dependence on hydrocarbon prices. Gradual policy rebalancing and structural reforms are needed to build resilience to commodity cycles, advance diversification, support inclusive growth and enhance governance, while protecting low-income households. The immediate priority is to contain inflation. Monetary and fiscal tightening may dampen growth in the short term, but delayed policy action risks an entrenchment of high inflation, which may require more abrupt and costly adjustments later. Fiscal consolidation is also needed to strengthen buffers and reduce its vulnerability to hydrocarbon price movements and ensuing risks to macroeconomic stability.

A. Fiscal Policy

15. **While a budget surplus is expected in 2022, the durability of spending restraint is uncertain.** The bulk of the budget spending increase introduced by the LFC2022 is unlikely to be executed within the calendar year, based on most recent budget outturn data shared by the

authorities. It could still be partly disbursed during the extended budget execution period for 2022, in early 2023.[3] As a result, the execution rate of current spending is projected to be low by historical standards in 2022 (Text Table 2). Under the assumption that spending of around 2.5 percent of GDP appropriated in the LFC2022 will be disbursed only in 2023, staff projects a 2.1 percent of GDP budget surplus in 2022, and a narrowing in the NHPD to 25.5 percent of NHGDP, the best outturn in at least two decades. The 2022 overall budget surplus should result in an increase in the Revenue Regulation Fund (“*Fonds de Régulation des Recettes*”, FRR) balance to (7.2 percent of GDP) at end-2022, up from 3.1 percent of GDP at end-2021 and, alongside a strong nominal GDP growth, drive a decline in total government debt to 52.4 percent of GDP in 2022 from 62.8 percent in 2021.

16. Announced spending increases for 2023 could reverse the narrowing trend of NHPD since 2019, even under the assumption of continued low budget spending execution rates. The 2023 budget has increased current and capital spending by 26.9 percent and 2.7 respectively relative to the appropriations under the LFC2022. A 26.6 percent increase in payroll spending, upward adjustments to pensions and the allowance for first-time jobseekers will contribute to the rise in current spending.[4] In staff’s view, spending plans for 2023 are unlikely to be fully executed given limits on available domestic financing and reluctance to foreign borrowing, as well as considering past trends of budget execution rates. Thus, staff’s baseline scenario assumes continued low execution of both current and capital spending. Still, spending would rise by 7 percent of GDP in 2023 leading to an overall budget deficit of 6.6 percent of GDP and resulting in the depletion of most accumulated fiscal savings. The NHPD would deteriorate by 6 percent of NHGDP relative to 2022, reversing most of its improvement since 2018.

Text Table 2. Algeria: Budget Appropriations and Forecast Outturns

(In percent of GDP unless otherwise indicated)

	2021	2022				2023			2003-2021
	Spending Outturns	2022 Budget	2022 Supplementary Budget	Staff Forecast *	Forecast Execution Rate of Budgeted Spending *(in percent)*	2023 Budget	Staff Forecast**	Forecast Execution Rate of Budgeted Spending *(in percent)*	Average Execution Rate of Budgeted Spending *(in percent)*
Current Spending	24.7	22.7	27.6	21.2	76.7	32.5	27.0	83.1	95.9
Capital Spending	9.0	12.7	14.0	6.8	48.4	13.4	8.0	59.8	69.6

*Excluding spending appropriated under the 2022 budget and assumed by staff to be executed in 2023

**Including spending appropriated under the 2022 budget and assumed by staff to be executed in 2023

Source: IMF staff based on budget laws and budget execution data

17. The announced fiscal easing in 2023 would further raise fiscal vulnerability and pressure on inflation. The significant rise in spending on wages, pensions and allowances will aggravate expenditure rigidity and reduce the room for adjustments to fluctuations in hydrocarbon prices amid limited fiscal buffers. Public sector salary increases could also catalyze higher unit labor

[3] In this case, these disbursements would be recorded as part of budget spending in 2023 as Algeria’s budget outturn data is elaborated on a cash basis.

[4] Spending reclassification following the closure of a number of earmarked treasury accounts will also contribute to the rise in current spending but will not affect total budget spending and the overall deficit. Spending related to these accounts was already included in overall spending under a distinct category (*“net lending and special Treasury accounts net operation”, see Tables 3.a and 3.b).*

costs in the broader economy and compound ongoing inflationary pressures. The projected rapid drawdown of accumulated fiscal savings would fuel sizeable rise in banking liquidity, further complicating the conduct of monetary policy.

18. In the medium term, projected large fiscal deficits and limited financing sources could pose significant risks to the execution of priority spending and macroeconomic stability. Under staff's baseline scenario, overall deficits are projected to remain elevated, averaging close to 7 percent of GDP through 2027. This is much lower than the projected average annual budget deficit of 22 percent of GDP in 2023-25 that features in the authorities' medium-term budget framework (MTBF).[5] Still, high fiscal deficits and principal repayments coming due on past borrowing from the BA will heap significant pressures on the domestic banking system, as fiscal savings would be almost depleted in 2023 and the authorities have ruled out foreign borrowing. Increasingly binding financing constraints could then lead to difficult trade-offs, including precipitous spending cuts in priority areas. These risks could materialize much earlier than expected should oil prices fall below staff assumptions. Although debt is projected to remain moderate through 2027, it is forecast to increase significantly between 2023 and 2027, and important risks to its trajectory stem from abundant contingent liabilities from SOEs which tend to be overindebted and unprofitable and other public sector entities (Annex III).[6]

19. Fiscal rebalancing guided by a rules-based framework is needed to curb inflation, rebuild fiscal savings, enhance resilience, and preserve macroeconomic stability by reducing fiscal financing requirements in the medium term. This would require an improvement in the NHPD by 10.2 percent of NHGDP relative to its 2022 level and through 2027, which represents an additional improvement of 6 percent of NHGDP relative to the trajectory assumed under the baseline scenario. Gradual phasing out of universal subsidies, in line with plans announced in the 2022 budget, could generate substantial savings, part of which could finance targeted support to low-income households.[7] Staff encouraged the authorities to accelerate ongoing preparatory work and launch the reform at the earliest opportunity with a clear implementation calendar. Parametric pension reform, reduction in capital spending and continuing ongoing tax reform would also contribute to the needed consolidation. Enhancing the spending efficiency should also remain a key priority (Annex V). Consolidation should be guided by a rules-based framework to reduce policy procyclicality, protect priority spending, including health and social spending, and ensure steady progress towards medium-term consolidation targets (Box 1).

20. Ongoing domestic tax revenue mobilization efforts should be continued, as they can support fiscal consolidation and inclusion. Recent efforts to improve the recovery of tax arrears

[5] Windfall hydrocarbon revenue beyond budgeted levels, as projected by staff, is added to the MTBF's revenue forecasts for comparability. Excluding this windfall revenue, the MTBF projects annual average budget deficits of 25 percent of GDP.

[6] See the 2022 Annual report of the Algerian Court of Audit.

[7] Based on new official estimates, the cost of on-budget subsidies of basic food products and water was 2.2 percent of GDP in 2021, in addition to off-budget fuel subsidies of 12.2 percent of GDP.

and leverage digital technologies are steps in the right direction. The reform of the tax on professional activities initiated in 2022 is welcome and should be continued in line with past IMF recommendations to tackle the distortions this tax generates while accelerating the reform of the property tax to guarantee sufficient funding of local governments. Measures introduced in 2022 to broaden the tax base should be complemented with reforms to lower barriers to formalization. Eliminating inefficient VAT exemptions would support both compliance and revenue mobilization.

21. In parallel, diversifying sources of financing can help limit macroeconomic and financial stability risks. Monetary financing should be strictly avoided to protect the independence of the BA and its ability to control inflation. Principal repayments coming due on past BA lending to the government should continue to be paid as scheduled. Staff welcomed the authorities' plans to improve the functioning of the secondary debt market and deepen the domestic debt market, with technical assistance from the IMF. The authorities also plan to use Public-Private Partnerships (PPPs) to finance basic infrastructure projects. This can help leverage international expertise and private sector innovation, but PPPs should be underpinned by a strong governance framework with sound risk sharing and management (Annex V).

22. A stronger fiscal framework and improved budget credibility can help support consolidation efforts and efficient implementation of public policies. In general, weaknesses in the credibility of the budget risk undermining its key role in the allocation of public resources in support of policy priorities. The authorities have made strides in public financial management (PFM) reforms in recent years, drawing on IMF technical assistance, towards the planned full implementation of the Organic Budget Law (OBL) in 2023.[8] A recurrence of the exceptionally low spending execution rate in 2022 should be avoided to protect these efforts and forestall emerging challenges to cash management and budget control and monitoring.[9] In this regard, staff recommended to (i) include detailed financing plans in published annual budgets, (ii) premise budget laws on updated projections for full-year outturns based on most recent execution data rather than on budget appropriations from previous years, (iii) strengthen cash management in line with the conclusions of recent IMF technical assistance, and (iv) produce and publish timely, comprehensive and disaggregated intra-year budget-execution data. It is also important to enhance budget integrity and comprehensiveness by regularly publishing information on budget outturns, off-budget operations, and fiscal risks, especially from PPPs and SOEs. The full implementation of the OBL in 2023 should contribute to better transparency given enhanced disclosures requirements under the law.

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[8] Several new tables have been included in the 2023 budget law, in line with the requirements of the OBL, enhancing budget transparency. The authorities intend to execute the 2023 budget in program mode—though delays in the rollout of the new integrated financial management information system may hamper efforts.

[9] The fiscal rebalancing strategy recommended by staff would require a reconsideration under a supplementary budget of the large spending increase announced in the 2023 budget, rather than repeated spending under-execution which would weaken the budget's credibility.

Authorities' Views

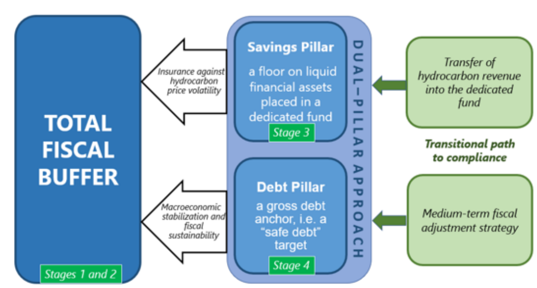
23. **The authorities expressed strong commitment to public finance sustainability and highlighted that their fiscal strategy is prudent and forward-looking**. They were confident that progress on fiscal and growth-enhancing reforms would pay off in the medium term, support tax revenue mobilization and allow scaling back budget spending. They emphasized their efforts to bring the informal sector under the tax net and the considerable progress achieved in reforms of PFM, digitalization, cash management and the administration of State assets. The authorities also reiterated that protecting purchasing power is critical and increases to budget spending are necessary to counteract the social fallout of high inflation and recent shocks. They ruled out difficulties in financing the budget deficit in the coming years.

Box 1. Designing a Rules-Based Fiscal Framework for Algeria[1]

A rules-based fiscal framework could help the government rebuild buffers and preserve the sustainability of public finances in the medium term. Well-designed fiscal rules— adequately balancing simplicity, flexibility and enforceability—help promote fiscal discipline and prevent deficit bias, while still allowing for countercyclical policies when needed. They can act as commitment devices, produce signaling effects and help rally political support around fiscal goals. Based on stochastic simulations of medium-term macro-fiscal trajectories, staff estimates that in Algeria, a total fiscal buffer of 38 percent of GDP (in the form of savings and/or lower debt) would help accommodate most macro-fiscal shocks into the medium-term while preserving fiscal sustainability.

Staff analysis suggests the adoption of a dual-pillar system, comprising a savings floor and a gross debt anchor. The savings floor could be accumulated into the oil stabilization fund ("*Fonds de Régulation des Recettes*", FRR), for the purpose of smoothing hydrocarbon revenue. It is calibrated using a value-at-risk approach, to insure public finances for a set number of years against hydrocarbon price shocks. The medium-term gross debt target is set to cover the rest of the required buffer computed above. While the relevant gross debt anchor depends on the authorities' preference for savings, setting the savings floor at 16 percent of GDP and the gross debt anchor at 48 percent of GDP is feasible, based on past FRR balances and on adjustment capacity.

A Dual-Pillar Approach for a Rules-Based Fiscal Framework in Algeria



A transition period of 8 years would be needed at first to comply with both objectives, after which a "net" debt anchor could be considered. Compliance would necessitate an improvement in the NHPD by close to 10 percent of NHGDP relative to its projected 2022 level and through 2027. This deficit trajectory would allow transferring an annual 1.4 percent of GDP in hydrocarbon revenue to the FRR.

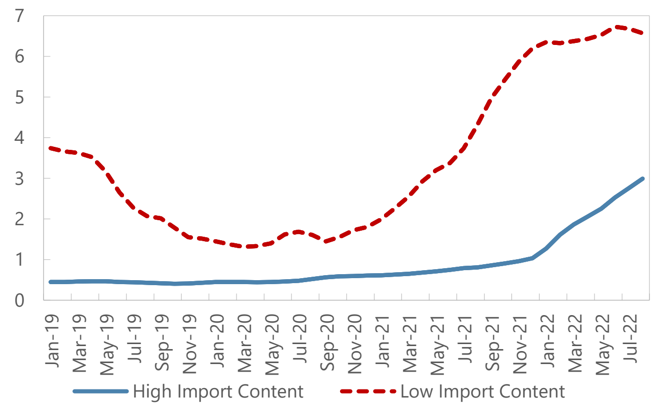
The success of the rules-based framework would require a range of adequate institutional arrangements. Mechanisms to ensure flexibility (escape clause) and compliance (correction mechanism, reporting) would be particularly useful features. Continued efforts to strengthen FRR governance and enhance medium-term planning and forecasting, monitoring, and reporting capacities at the Ministry of Finance are needed so that the rules truly inform strategic planning, budget preparation and execution.

1/ For more detail on the calibration of the framework, please refer to the SIP "A Rules-Based Fiscal Framework for Algeria"

B. Monetary and Exchange Rate Policies

24. If not addressed, risks of entrenchment of high inflation are high.[10] Staff analysis points to broad-based acceleration in trend inflation prior to the 2022 commodity price shock, underscoring risks of persistent inflationary pressures and de-anchoring of expectations. Import prices have significantly contributed to the acceleration in inflation, but the impact of domestic factors appears to be larger (Text Figure 2). Domestic factors include temporary exogenous developments (e.g. a drought in 2021) as well as more permanent ones, such as disruptions to retail markets and wage increases. The expansionary fiscal policy stance expected in 2023 could add to demand and price pressures.

Text Figure 2. Algeria: Contribution to Inflation
(percentage, 12-m average, YoY)



Source: IMF staff calculations.

25. Staff urged the BA to immediately tighten monetary policy to safeguard price stability. While the recent dinar appreciation can temporarily help mitigate imported inflation, it cannot durably substitute for needed monetary policy tightening, amid deeply negative real interest rates. Staff recommended a gradual increase in the policy rate alongside a resumption of a more active liquidity management (Annex VI). These combined actions would give an operational existence to the key policy rate, strengthen the BA's ability to conduct contracyclical policy, and help anchor inflation expectations.

26. Strengthening the BA's governance framework would help improve the effectiveness of monetary policy. Staff recommended adding an explicit ban on any form of monetary financing (beyond the well-circumscribed mechanism of temporary advances to the Treasury) in the forthcoming revision of the Law on Money and Credit (LMC). This would enhance the BA's independence and its ability to safeguard price stability and complement other proposals currently under discussion to modernize its governance and organizational framework.

27. Well-managed exchange rate flexibility can help the economy adjust to volatile terms of trade.[11] The REER has markedly appreciated in 2022 amid a sharp improvement in terms of trade, reversing most of its depreciation since early 2020. Going forward, inflation is projected to remain high and significant fiscal policy easing has been announced for 2023, while the terms of trade are projected to decline gradually as hydrocarbon prices edge lower. A consistent policy mix, combining tighter fiscal and monetary policies is needed to avoid steep exchange rate adjustment risks. In

[10] For more details, see the SIP *"A reexamination of inflation dynamics and drivers in Algeria"*.

[11] The de jure exchange rate arrangement is managed floating, while the de facto exchange rate arrangement is a crawling-like arrangement.

parallel, reforms to the FX and trade regulatory frameworks, including measures to deepen the interbank FX market and allowing for greater exchange rate flexibility in the medium term would enhance the effectiveness of the nominal exchange rate as shock absorber, support economic diversification, reduce the parallel FX market premium, and improve monetary policy transmission.

Authorities' Views

28. The BA reiterated its commitment to price stability but did not see the need for immediate action. The authorities concurred with staff that entrenchment of high inflation is a risk and that the exchange rate has limited effectiveness in taming durable price pressures. They expressed readiness to deploy all policy tools as needed to safeguard price stability but considered that recent inflation dynamics have not necessitated further policy actions yet given lackluster private sector credit growth, limited monetary policy transmission and signs of slowdown in inflation in September. The BA also indicated that its objective is to maintain the REER close to its equilibrium level, which it assesses on a regular basis and timely actions are taken to avoid the emergence of any significant misalignment of the dinar. They expressed appreciation of continued IMF technical assistance on priority areas to further enhance its monetary policy and supervisory frameworks.

C. Financial Sector Policies

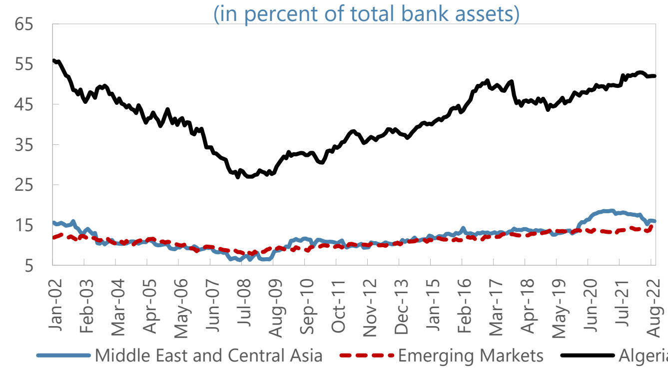
29. The BA is making steady progress on reforms to modernize the financial system and implement some key recommendations of the 2020 FSAP. This includes: (i) the implementation of new accounting standards; (ii) the preparation of a new bank risk rating system which would enable a transition to risk-based supervision; (iii) gradual progress towards the institution of supervisory review and evaluation processes. Regulatory initiatives are also underway to strengthen bank governance. The BA has also contributed to the preparation of an important revision of the LMC to spur innovation in the financial sector, including in the fields of electronic payment systems, digital banks, and Islamic finance.

30. Nevertheless, the financial health of banks deserves closer attention amid an aggravating sovereign-bank nexus. Bank claims on the government and SOEs are on the rise, and at 52 percent of total bank assets at end-August, are high both by historical standards and relative to peer economies (Text Figure 3). Tightening interlinkages between the balance sheets of the government, non-financial SOEs and SOBs can amplify sovereign or banking-sector stress, magnifying risks to financial stability and debt sustainability. These risks are exacerbated by the deterioration in bank asset quality. NPLs and bank balance sheets remain burdened by sometimes unprofitable loans to SOEs and illiquid government debt securities issued in the context of the PSR.[12] The supply of loans on criteria other than profitability could divert credit from viable projects, lead to the mispricing of risks and distort factor allocation, weighing on growth and financial

[12] These securities were issued well below market yields and are likely illiquid. See Algeria: 2021 Article IV consultation Staff Report

stability. It could also further undermine monetary policy efficiency and generate important contingent liability risks for the budget.

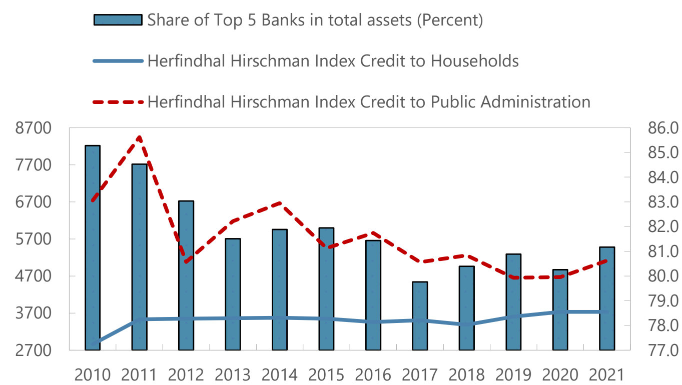
Text Figure 3. Algeria: Bank Claims on the Public Sector
(in percent of total bank assets)



Notes: Claims on the public sector include lending to the central and local governments as well as to state-owned enterprises.
Regional aggregates are calculated as medians.
Source: IMF staff calculations.

31. To address these risks, fiscal funding sources should be diversified, and the business model of SOBs improved to focus on commercially viable projects. SOBs should strive to implement an effective business strategy. Compliance with prudential rules, notably on NPLs and risk exposure limits, should be ensured. Furthermore, a detailed assessment of the quality of public bank loan portfolios should be conducted through an examination of the assets, guarantees, and provisions, as well as a review of the NPL write-off process.

Text Figure 4. Algeria: Banking Sector Concentration



Notes: Herfindahl-Hirschman Indices (HHI) measure concentration and are computed by aggregating the squared-value of market shares of all banks. Higher values indicate greater concentration.
Source: IMF staff calculations using data from the Algerian Authorities.

32. In parallel, it is important to lift constraints to private sector financing. Credit to the private sector has been slow in recent years due to both conjunctural and structural factors—including the focus of SOBs on lending to SOEs and weak competition, as reflected by a high degree of concentration in deposits and credits (Text Figure 6). Reform priorities to level the playing field and enable the financial system to better support growth include: (i) strengthening SOB governance; (ii) reforming loan subsidy programs; (iii) developing prudential policies to boost credit to small and medium-sized enterprises and households; (iv) introducing an effective public credit registry and a personal bankruptcy framework; and (v) deepening the government debt market and encouraging private debt issuance.

Authorities' Views

33. The authorities were confident of the good financial health of the banking system. They highlighted that SOBs are profitable and have been taking their credit-related decisions independently over the last two years. They also indicated that around half of NPLs in SOBs are legacy issues and have not been written-off due to cumbersome administrative processes. They noted that a large share of NPLs is provisioned or backed by guarantees or collateral, posing limited risk to financial stability. The authorities stressed their continued efforts to promote financial

modernization and inclusion, including through digitalization, and modernize the existing central risk registry.

D. Structural Reforms

34. The authorities have continued to implement the 2021 Government Action Plan ("*Plan d'action du government"*, PAG).[13] Several measures have been taken in pursuit of the PAG's key objectives, some of which are in line with previous IMF recommendations (Text Table 3, Annex IV). A new investment law and its attendant decrees have helped streamline the regulatory framework for private investment. The new law follows the elimination of the 51/49 rule on FDI in non-strategic sectors in 2020. In addition, the authorities are working to accelerate the digitalization of the economy—a key element for streamlining procedures and improving the ease of setting-up a business. A new law on micro-entrepreneurship could help promote formalization. The forthcoming law on renewable energies will help set up a legal framework to spur investment in sustainable energy sources and promote decarbonization. A new public procurement law and dedicated electronic portal are currently under preparation.

35. Efforts to improve governance, reduce corruption risks and reinforce the legal AML/CFT framework are welcome and should be strengthened further, in line with past IMF recommendations.[14] Recent reforms include the formal installation of the new High Authority in charge of fighting corruption, the application of enhanced mechanisms for asset recovery and an ongoing revision to the legislation on AML/CFT. Ensuring that this legislation includes a strong risk-based approach to supervision will be important. Staff also encourages further efforts to strengthen institutional safeguards against conflicts of interest and the operational autonomy of anti-corruption and judicial institutions.

36. Pursuing greater trade openness can also support economic diversification by lowering the cost of inputs, facilitating technology transfer, and fostering competition. The authorities' efforts to ratify several free trade agreements, including the African Continental Free Trade Agreement could support trade integration. However, regulation measures taken since 2015 to contain imports cannot substitute needed reforms to support domestic production.[15] They induce regulatory uncertainty, create rent-seeking opportunities, may generate inflationary pressures, and encourage informality. Product and labor market reforms would help reduce distortions, create an economic environment conducive for the private sector, enhance competitiveness and stimulate economic diversification.

37. Staff urged the authorities to prioritize actions to improve the quality and availability of macroeconomic data, which suffer from considerable weaknesses. The authorities have

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[13] The PAG aims at consolidating the rule of law and reforming governance, supporting economic recovery and renewal, and reinforcing human capital and social cohesion.

[14] See the 2021 Article IV Consultation Staff Report (CR No. 21/253) for further discussion.

[15] See the 2021 Article IV Consultation Staff Report (CR No. 21/253) for further discussion.

publicly announced plans to enhance data production. However, deep macroeconomic data gaps persist and complicate surveillance, although data remains broadly adequate for this purpose. For instance, CPI weights are based on a 2000 household survey and are severely outdated, which could

Text Table 3. Algeria: Implementation of the Government Action Plan: Selected Measures

Strategic Pillar	Main Areas of Focus	Selected Key Measures (Implemented or Planned)
Consolidating Rule of Law and Reforming Governance	Independence of the judiciary, good governance, efficient and transparent management of public finances, modernization of public administration including through digitalization	-Revisions to the organic law on the State Council (Law 22-11), creation of new specialized commercial tribunals -Preparation of a Chart of Account for the State and operational guides for multiyear budget frameworks. -Adoption of a new investment code and preparation of a new competition law to improve the business environment -Forthcoming reform of the law on Money and Credit -Acceleration of efforts to promote digitalization and facilitate business creation, for example by revamping the one-stop shop, increasing digiral taxpayer services through the *Jibaya'tic and Moussahama'tic* portals, creation of a portal for public procurement, and digitization of many government services -Ongoing efforts to improve governance and reduce potential for corruption including the formal installation of the new High Authority in charge of fighting corruption, the application of enhanced mechanisms for asset recovery, the insertion of good governance in draft regulations against corruption and on penal procedures, and the
Supporting Economic Recovery and Renewal	Supporting the recovery through the following: modernization of the banking and financial sector, reforms to the commercial public sector and state-owned enterprises, business climate, incentives for formalization, research and development, and emergence of start-ups, digitalization Spurring new growth drivers through the following: development strategy for the energy and mining sectors including transition to renewable energy sources, agriculture and fishing, pharmaceuticals, and tourism Export diversification and facilitation, including through updated or new free trade agreements Support to small and medium entreprises	-Expansion of the bank and insurance networks, including for Islamic financial products -Completion of a national strategy for exports and various measures to boost non-hydrocarbon exports including fiscal incentives -Preparation of a new law on free zones -Evaluation of several bilateral and multilateral trade agreements and of the process for accession to the WTO -Adhesion to the African Continental Free Trade Area in 2021 -Provision of tax relief and other transfers in the 2022 budget law to support household purchasing power -Preparation of a legal framework for PPPs to sustain investment in infrastructure -Preparation for the launch of large investment projects in infrastructure and mining, in partnership with foreign investors
Reinforcing Human Development and Social Cohesion	Creating jobs and reducing unemployment, promoting human capital, improving living conditions and enhancing efficiency and equity of social policies	-Planned reforms to improve the targeting of subsidies -Instauration of a new monthly allowance for first time jobseekers aged up to 40 years. -Salary increases in the civil service -Hiring of youth in the civil service under the "Dipositif d'Aide à l'Insertion Professionnelle"(DAIP) -Conversion of the National Housing Fund (CNL) into a financial institution, under the BA's oversight, specializing in the financing of housing -Reinforced controls on the prices of foodstuff and fighting against speculation

Note: The fiull list of measures (implemented and planned) for the 5 strategic pillars of the PAG are described in the October 2022 Policy Statement available here:
https://www.aps.dz/algerie/145921-conseil-de-la-nation-presentation-de-la-declaration-de-politique-generale-du-gouvernement
Source: Government of Algeria "Plan d'Action du Gouvernement", September 2021 (Chapters 1-3) and Policy Statement ("Déclaration de Politique Générale"), October 2022

lead to significant errors in the measurement of inflation. No employment data has been published since 2019. Quarterly national account data and semi-annual industry surveys are published with great delay. No data on intra-annual budget execution is published. Addressing data deficiencies is crucial to better inform economic policies and private sector decisions. Staff recommended efforts

to improve the timely provision of data to the IMF, including data on budget outturns. Staff stands ready to provide all needed support to the authorities in their efforts to address data gaps through dedicated technical assistance.

Authorities' Views

38. **The authorities concurred with staff on the need to pursue structural reforms to promote diversification and job creation.** They stressed the considerable progress achieved on legislative reforms since 2020 and reiterated an unwavering commitment to the implementation of the PAG policy agenda. They viewed import regulation measures as necessary to combat fraud and promote domestic production and reiterated their commitment to full compliance with outstanding agreements with external trade partners. The authorities agreed with staff on the need to address data deficiencies and attributed some of them to pandemic-related disruptions.

STAFF APPRAISAL

39. **The near-term outlook for the Algerian economy has materially improved, buoyed by the upswing in hydrocarbon prices.** The CA swung to surplus in 2022 and international reserves rose for the first time since 2013. This trend is projected to continue in 2023. A fiscal surplus is estimated in 2022 for the first time since 2008, on higher hydrocarbon revenue and large under-execution of spending. Nonhydrocarbon growth has likely picked up pace in 2022 and will strengthen further in 2023 helped by significant fiscal easing (Annex I). The outlook remains highly contingent on hydrocarbon prices and faces risks from a weaker global backdrop and commodity price volatility. Algeria's external position in 2022 was stronger than the level implied by fundamentals and desirable policy settings.

40. **The rise in inflation is a major challenge, amid a loose monetary policy stance.** Inflation has been accelerating and reached its highest level in 25 years. This acceleration has been broad-based, albeit more pronounced for food products. Despite steps towards more active liquidity management, monetary policy remains accommodative as the BA kept the reserve requirement ratio and policy rate near historical lows and excess bank liquidity built up.

41. **Staff urges the BA to tighten monetary policy immediately to forestall possible de-anchoring of expectations and persistent high inflation.** Recent dinar appreciation cannot substitute for needed monetary policy tightening. Staff recommends that the BA increase its policy rate and resume well-calibrated liquidity management to enhance monetary policy transmission. The forthcoming revision of the LMC is a welcome opportunity to strengthen the governance framework of the BA. Staff recommends a formal ban on monetary financing in the new law to enhance the BA's independence and its ability to act in defense of price stability.

42. **The announced sizeable rise in spending under the 2023 budget could reverse the progress achieved on narrowing the deficit since 2018, weaken the resilience of public finances and add to inflation pressures.** Financing constraints are likely to forestall full execution

of announced spending. However, even continued low execution of budgeted spending could lead to a substantial deterioration of the fiscal deficit. Higher spending rigidity and a rapid drawdown of fiscal savings would exacerbate the vulnerability of public finances to gyrations in hydrocarbon prices—with the risk of abrupt adjustment should oil prices decline— and add to excess liquidity, complicating the conduct of monetary policy.

43. **The medium-term deficit trajectory also carries risks for macroeconomic stability.** Continued wide fiscal deficits and increasing principal repayments coming due on past monetary financing would result in large fiscal financing needs through the medium term. As the authorities have ruled out foreign borrowing, meeting these financing needs would heap significant pressure on the domestic banking system and pose risks to financial and macroeconomic stability.

44. **Gradual fiscal rebalancing guided by a rules-based framework is needed to enhance the resilience of public finances and safeguard macroeconomic stability in the medium term.** Staff recommends an adjustment to improve the NHPD by 10 percent of NHGDP relative to its 2022 level and through 2027. Subsidy reform together with enhanced targeted social protection would help achieve the required fiscal rebalancing, alongside parametric pension reform, lower capital spending and continuation of tax reforms. Staff also proposes the adoption of a medium-term fiscal framework based on well-calibrated rules comprising a saving floor and a gross debt anchor, to guide fiscal rebalancing, reduce policy procyclicality and protect priority spending. More diversified financing sources would afford space to stage fiscal adjustment over several years while limiting pressures on the banking system.

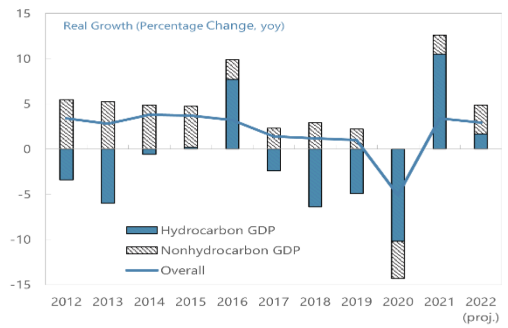
45. **Staff welcomes the progress achieved on PFM reform and calls for further efforts to strengthen the fiscal framework.** The projected full implementation of the OBL in 2023 would mark a major milestone for modernization efforts. To protect this progress, budget projections should be in line with execution capacity and available fiscal space. Budgets should also incorporate comprehensive and transparent financing plans and efforts should be deployed to strengthen cash management and improve transparency on budget execution.

46. **Acceleration of structural reforms is needed to advance the transition to a more diversified, resilient and job-intensive growth model and further strengthen the governance framework** Legislative reforms recently adopted or underway, including the new investment law and the forthcoming laws on micro-entrepreneurship and renewable energies, could help create a more conducive environment to private sector activity. Staff cautions against the risks from tight import regulation measures—e.g., fueling inflation and incentivizing informality— and recommends further reforms to improve trade openness and competitiveness, including product and labor market reforms. It also urges the authorities to prioritize actions to address weaknesses in macroeconomic data quality and availability. Ongoing efforts to strengthen governance and reduce corruption risks are welcome and should be intensified.

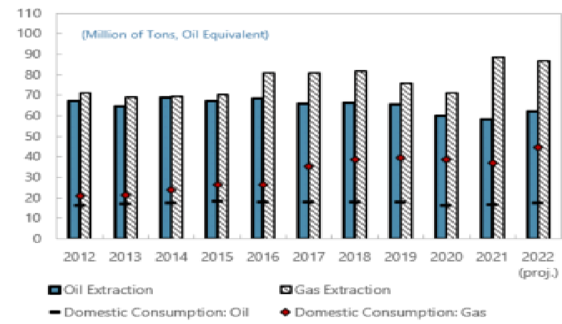
47. **Staff recommends that the next Article IV consultation take place on the standard 12-month cycle.**

Figure 1. Algeria: Selected Macroeconomic Indicators

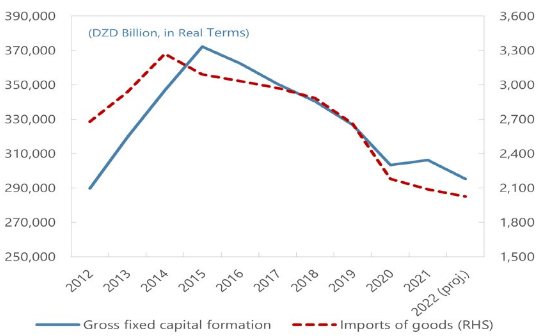
The recovery from the pandemic was uneven in 2021 given weaknesses in services and the labor market.



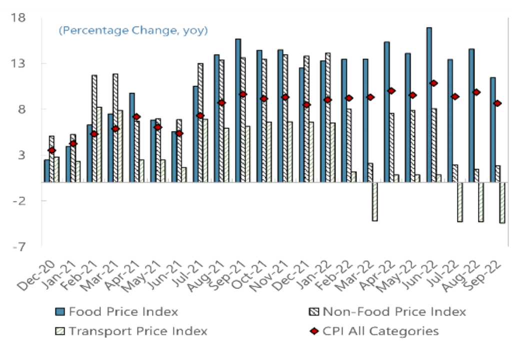
Gas production rebounded sharply in 2021 amid higher domestic and external demand.



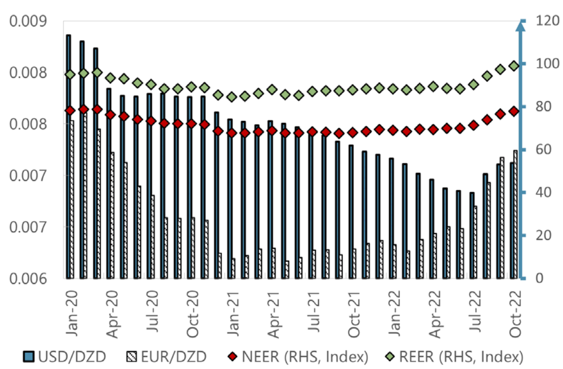
Gross aggregate investment continued its downward trend and imports of goods declined in lockstep.



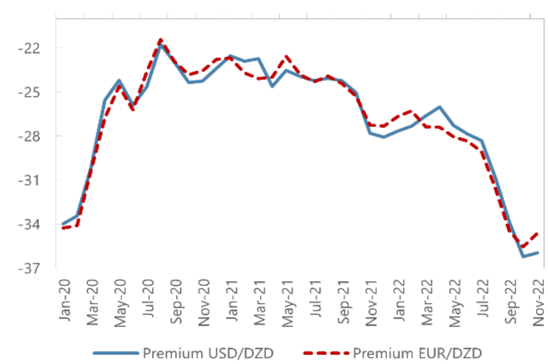
Amid a global commodity shock, inflation continued to rise to levels not seen in decades.



The central bank implemented an appreciation in the dinar against the dollar in August to tame inflationary pressures.



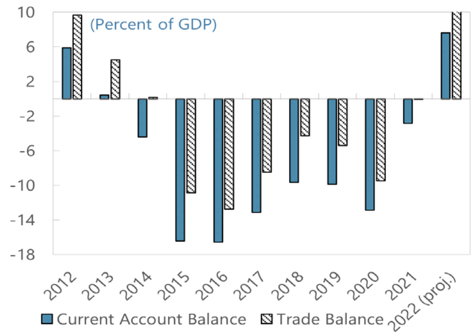
The parallel exchange rate premium, which had been stable during 2020-21, has widened in 2022Q3.



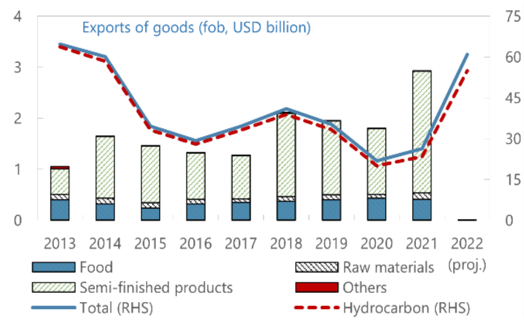
Source: Algerian Authorities and IMF staff projections.

Figure 2. Algeria: External Sector Developments

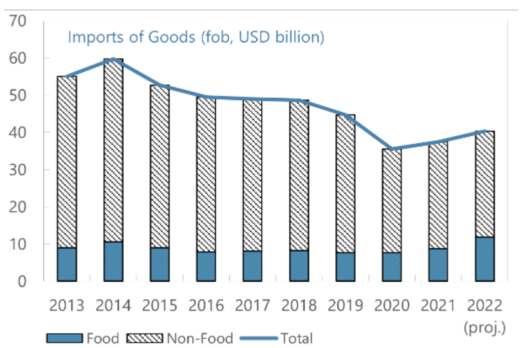
Algeria's external position improved markedly.



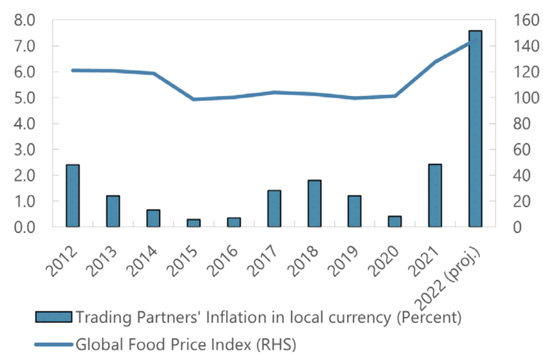
Hydrocarbon exports rose sharply. Other exports are small but doubled in two years driven by energy-intensive goods. .



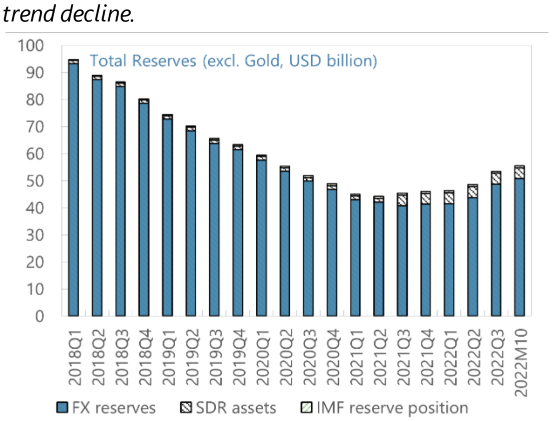
Imports of goods increased moderately, remaining below pre-pandemic levels amid tight regulation …



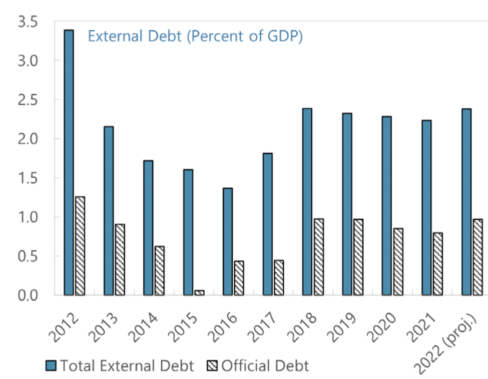
… and global price pressures



FX reserves increased in 2022, halting their multiyear trend decline.



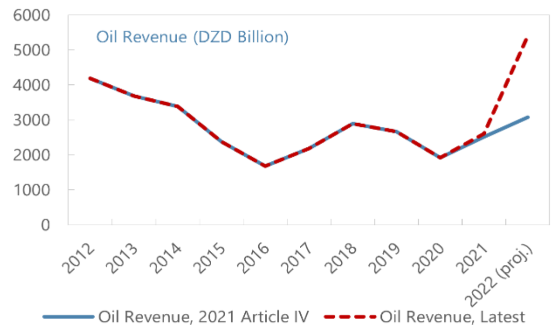
External debt remains low.



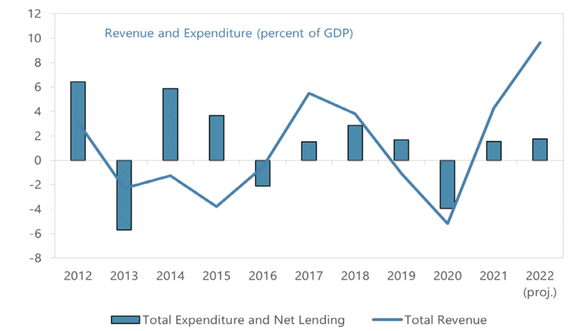
Source: Algerian Authorities and IMF staff projections.

Figure 3. Algeria: Fiscal Indicators

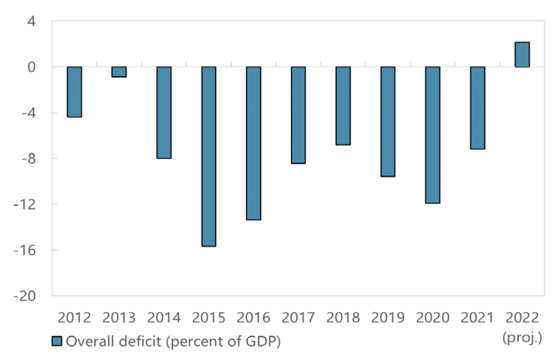
Rising hydrocarbon prices shored up budget revenues.



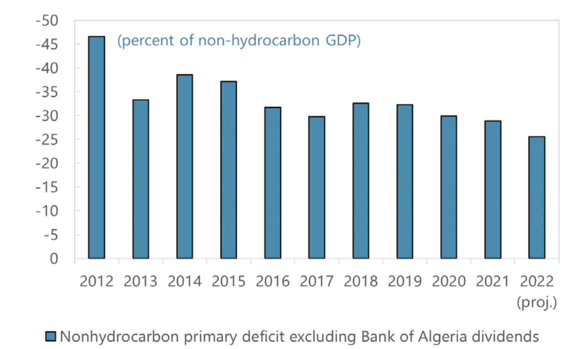
Despite the announcement of large spending increase in 2022, spending growth has been moderate.



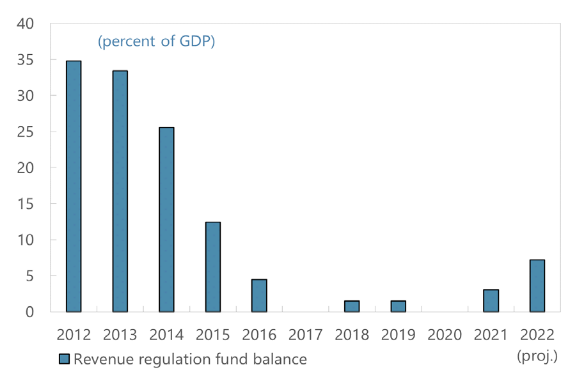
An overall surplus is projected in 2022.



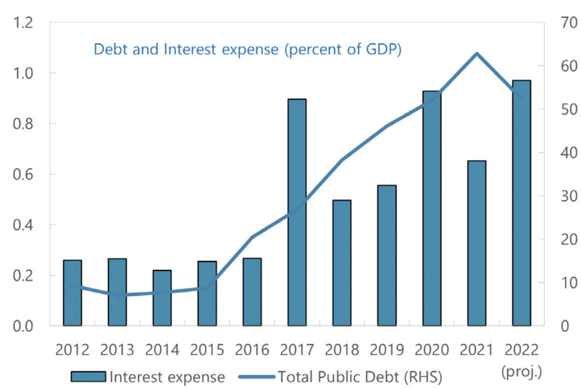
The non-hydrocarbon primary deficit is projected to narrow to its lowest level in decades.



Reflecting the budget surplus, the balance of fiscal savings deposited on the Revenue Regulation Fund will increase.



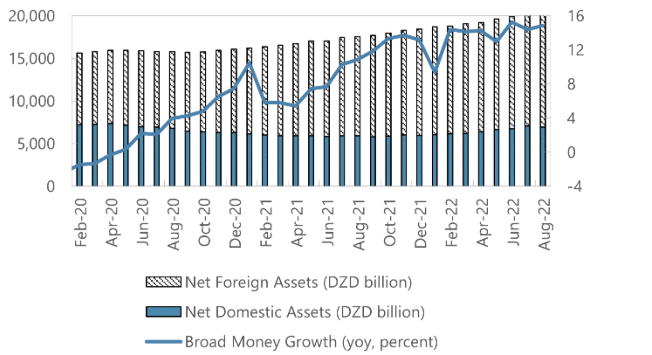
Public debt/GDP will temporarily decline due to the achievement of a fiscal surplus and strong nominal growth.



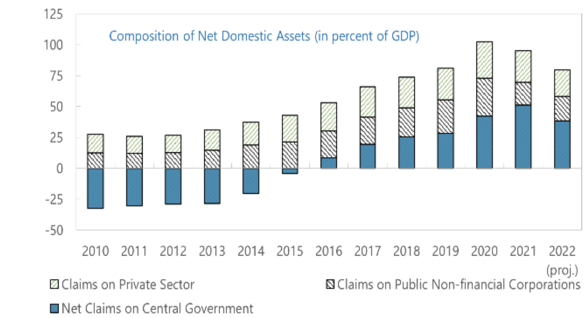
Source: Algerian Authorities and IMF staff estimates.

Figure 4. Algeria: Monetary and Financial Sector Indicators

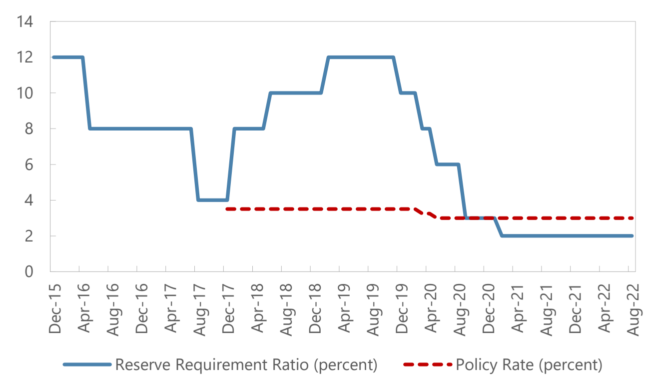
Broad money growth has been mostly driven by the accumulation of net foreign assets in recent months.



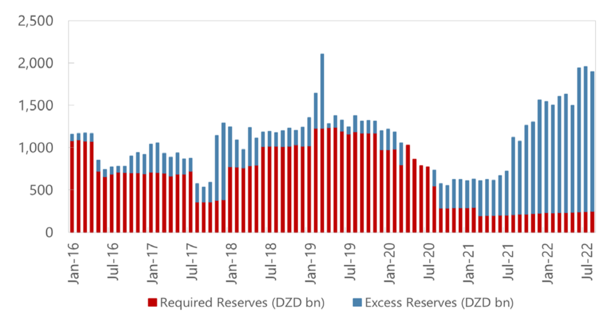
Net domestic assets have been driven by credit to the public sector, while credit to the private sector is tepid.



Monetary policy has been on hold after a slate of easing measures in 2020-21…

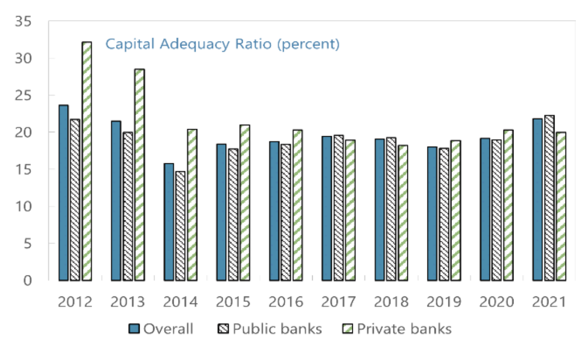


…and banks have high levels of excess reserves.

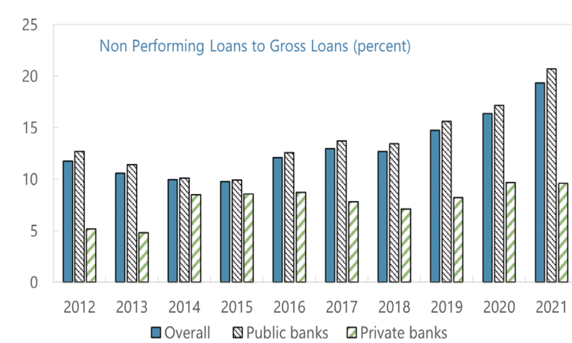


Note: Data on excess reserves is not available for the period April-July 2020.

Bank capitalization ratios are above regulatory thresholds…



…but non-performing loans have increased.



Source: Algerian Authorities.

Table 1. Algeria: Selected Economic and Financial Indicators, 2017–27

						Projections					
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
Output and prices				(Annual percentage change)							
Real GDP	1.4	1.2	1.0	-5.1	3.4	2.9	3.0	2.6	2.2	2.1	1.6
Hydrocarbon sector	-2.4	-6.4	-4.9	-10.2	10.5	1.7	0.7	1.7	0.8	1.8	0.0
Nonhydrocarbon sector	2.3	2.9	2.2	-4.1	2.1	3.2	3.4	2.8	2.4	2.1	1.9
Per capita	-0.8	-0.8	-1.0	-6.0	2.0	1.5	1.6	1.2	0.8	0.7	0.3
Consumer price index (period average)	5.6	4.3	2.0	2.4	7.2	9.3	8.1	7.6	6.6	6.0	5.6
Investment and savings				(In percent of GDP)							
Savings-investment balance	-13.1	-9.6	-9.9	-12.8	-2.8	7.6	2.7	-1.4	-3.1	-4.4	-4.9
National savings	30.3	31.7	29.5	27.0	35.1	39.6	39.2	36.6	34.7	33.4	32.6
Central government	5.4	5.0	4.3	-1.7	1.8	8.9	1.4	0.6	-0.1	-0.3	-0.7
Nongovernment 1/	25.0	26.7	25.2	28.7	33.3	30.7	37.8	35.9	34.8	33.7	33.4
Investment	43.5	41.3	39.3	39.9	37.9	32.0	36.5	38.0	37.8	37.8	37.6
Central government	13.8	11.8	13.9	10.2	9.0	6.8	8.0	7.3	6.6	6.7	6.5
Nongovernment 1/	29.7	29.5	25.5	29.6	28.9	25.2	28.5	30.7	31.1	31.2	31.1
o/w Nongovernment nonhydrocarbon	25.6	23.6	18.9	25.8	26.0	22.7	26.2	27.9	29.2	29.3	29.5
Central government finances				(In percent of GDP)							
Revenue	32.0	33.4	32.2	30.5	29.8	33.2	31.4	29.5	28.5	27.5	26.9
Expenditure (incl. net lending)	40.5	40.2	41.8	42.4	37.0	31.1	38.1	36.1	35.2	34.4	34.1
Overall budget balance	-8.4	-6.8	-9.6	-11.9	-7.2	2.1	-6.6	-6.7	-6.7	-7.0	-7.2
Central bank financing (flow)	11.6	16.5	4.9	0.0	2.3	0.0	0.0	0.0	0.0	0.0	0.0
Gross government debt (excluding guarantees)	26.8	38.3	46.0	52.0	62.8	52.4	49.4	51.9	54.6	57.5	60.8
				(In percent of nonhydrocarbon GDP)							
Nonhydrocarbon primary balance excluding central bank dividends	-29.8	-32.6	-32.2	-29.9	-28.9	-25.5	-31.4	-26.4	-24.4	-22.6	-21.6
Nonhydrocarbon balance	-24.8	-26.9	-28.1	-25.9	-24.5	-24.4	-31.0	-26.4	-24.4	-23.1	-22.3
Revenue	39.9	42.9	40.0	35.5	38.4	47.0	42.3	37.8	35.9	34.2	33.1
Hydrocarbon	14.3	18.2	16.2	12.1	15.2	27.4	22.1	17.8	16.0	14.4	13.4
Nonhydrocarbon	25.5	24.8	23.8	23.4	23.1	19.6	20.1	20.0	19.9	19.7	19.6
Expenditure (including net lending)	50.3	51.7	51.9	49.3	47.6	44.0	51.2	46.4	44.4	42.8	41.9
Current expenditure	30.8	33.4	29.7	31.5	31.7	30.0	36.3	33.2	32.4	31.3	30.9
Capital expenditure	17.2	15.2	17.2	11.9	11.6	9.6	10.8	9.4	8.4	8.3	8.0
Net lending	2.3	3.1	5.0	5.9	4.4	4.3	4.1	3.8	3.6	3.3	3.0
External sector 2/											
Current account balance (percent of GDP)	-13.1	-9.6	-9.9	-12.8	-2.8	7.6	2.7	-1.4	-3.1	-4.4	-4.9
Exports, f.o.b. (percent change)	19.0	19.1	-14.2	-37.9	75.9	58.0	-5.2	-11.3	-3.0	-3.1	-0.7
Hydrocarbons	20.0	17.2	-14.5	-39.8	70.2	61.4	-7.6	-14.3	-5.6	-6.1	-3.7
Nonhydrocarbons	-1.9	62.3	-6.7	-7.7	135.7	32.4	16.6	10.7	11.8	11.6	11.3
Imports, f.o.b. (percent change)	-0.9	-0.8	-8.1	-20.4	5.4	7.6	15.2	5.8	2.1	2.1	1.6
Crude oil export unit value (US$/bbl)	54.1	71.2	64.5	41.9	72.3	101.7	87.0	80.9	77.4	75.0	73.2
Gross official reserves											
In US$ billions	97.3	79.9	62.8	48.2	46.7	62.0	69.5	68.1	63.1	54.9	45.4
In months of next year's imports of goods and services	19.4	17.7	17.6	13.0	11.6	13.4	14.1	13.3	12.0	10.4	8.4
Gross external debt (percent of GDP)	2.3	2.3	2.2	2.4	1.9	1.6	1.6	1.6	1.6	1.6	1.5
Money and credit				(Annual percentage change unless otherwise indicated)							
Net foreign assets	-11.1	-15.8	-20.3	-14.9	-5.2	36.2	18.8	3.1	-3.1	-9.4	-14.4
Credit to the economy	11.9	12.3	9.0	3.0	-12.1	13.2	2.3	2.5	4.9	6.7	7.6
Money and quasi-money	8.4	11.1	-0.8	7.4	13.2	11.9	13.4	8.6	7.5	6.9	6.9
Memorandum items:											
GDP (in billions of dinars at current prices)	18,876	20,452	20,500	18,477	22,079	27,863	30,062	32,097	34,753	37,461	40,126
Nominal GDP Growth	7.8	8.3	0.2	-9.9	19.5	26.2	7.9	6.8	8.3	7.8	7.1
NHGDP (in billions of dinars at current prices)	15,177	15,904	16,509	15,902	17,167	19,709	22,367	24,998	27,608	30,109	32,610
GDP capita per (in US$)	4,080	4,119	3,953	3,322	3,669	...	...	...	...	...	...
Exchange rate (DA per US$)	110.9	116.6	119.4	126.9	135.3	...	...	...	...	...	...
REER (percent change)	2.4	-4.7	2.3	-4.6	-4.9	...	...	...	...	...	...

Sources: Algerian authorities; and IMF staff estimates and projections.
1/ Including public enterprises.
2/ In U.S. dollars unless otherwise indicated.

Table 2. Algeria: Balance of Payments, 2017–27

(in percent of GDP)

	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
						Projections					
					(In percent of GDP; unless otherwise indicated)						
Current account	-13.1	-9.6	-9.9	-12.8	-2.8	7.6	2.7	-1.4	-3.1	-4.4	-4.9
Balance on goods	-8.5	-4.3	-5.4	-9.4	0.7	10.5	5.5	1.0	-0.2	-1.4	-1.8
Exports, f.o.b.	20.3	23.5	20.6	15.1	23.6	31.2	27.8	24.3	22.8	21.6	21.0
Hydrocarbons	19.5	22.2	19.4	13.7	20.9	28.1	24.5	20.6	18.9	17.3	16.3
Other	1.4	2.2	2.1	1.9	4.5	6.0	6.9	7.7	8.6	9.6	10.7
Imports, f.o.b.	28.8	27.7	26.0	24.4	23.0	20.6	22.4	23.3	23.0	22.9	22.8
Balance on services Services (net)	-4.7	-4.7	-3.7	-3.0	-2.2	-2.4	-2.8	-3.2	-3.6	-3.9	-4.1
Exports	1.8	1.9	1.9	2.1	2.0	1.6	1.5	1.5	1.5	1.4	1.4
Imports	6.5	6.6	5.6	5.0	4.2	4.0	4.4	4.7	5.1	5.3	5.5
Primary Income (net)	-1.7	-2.6	-2.5	-2.0	-2.5	-1.7	-1.2	-0.7	-0.8	-0.9	-0.9
Inflows	1.2	0.7	0.6	0.6	0.4	0.7	0.9	1.1	0.9	0.7	0.6
Outflows	-2.9	-3.3	-3.1	-2.6	-2.9	-2.4	-2.1	-1.8	-1.7	-1.6	-1.6
Interest payments	0.0	0.0	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
Secondary income (net)	1.7	1.9	1.8	1.5	1.2	1.2	1.3	1.4	1.6	1.7	1.9
Capital and financial account	13.0	9.6	9.9	12.9	2.9	-7.6	-2.7	1.4	3.1	4.5	4.9
Capital account	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign Direct Investment	0.7	0.4	0.8	0.8	0.6	0.2	0.8	0.8	0.8	0.8	0.8
Portfolio Investment	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Investment	-0.5	0.2	-0.7	0.9	1.4	0.0	0.1	0.0	0.0	0.0	0.0
Net errors and omissions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Official reserves (increases (-))	12.8	9.0	9.8	11.2	0.9	-7.8	-3.6	0.6	2.3	3.7	4.2
Memorandum items:											
Current account balance (in percent of GDP)	-13.1	-9.6	-9.9	-12.8	-2.8	7.6	2.7	-1.4	-3.1	-4.4	-4.9
Algerian crude oil price (US$/barrel) 1/	54.1	71.2	64.5	41.9	72.3	101.7	87.0	80.9	77.4	75.0	73.2
Gross official reserves (in billions of US$) 2/	97.3	79.9	62.8	48.2	46.7	62.0	69.5	68.1	63.1	54.9	45.4
Idem, in months of next year's imports	19.4	17.7	17.6	13.0	11.6	13.4	14.1	13.3	12.0	10.4	8.4
Reserves (in percent of ARA EM metric) 3/	881.5	647.0	538.0	476.7	378.3	134.4	144.7	148.2	143.9	131.1	110.8
Net international investment position (in percent of GDP)	50.7	38.4	27.8	23.7	18.3	22.9	24.2	22.4	18.6	13.6	8.4
Gross external debt (in percent of GDP)	2.3	2.3	2.2	2.4	1.9	1.6	1.6	1.6	1.6	1.6	1.5

Sources: Algerian authorities; and IMF staff estimates and projections.
1/ Weighted average of quarterly data.
2/ Gross official reserves includes holdings of SDR assets and, for 2021, Algeria's share of the general SDR allocation by the IMF in August 2021.
3/ ARA EM metric includes additional buffer for commodity intensive countries (projection period only).

Table 3a. Algeria: Summary of Central Government Operations, 2017–27 1/

(in billions of dinars)

						Projections					
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
Budget revenue and grants	6,048	6,827	6,602	5,641	6,587	9,262	9,451	9,461	9,910	10,283	10,779
Hydrocarbon revenue 2/	2,177	2,887	2,668	1,922	2,609	5,400	4,950	4,460	4,404	4,341	4,386
Nonhydrocarbon revenue	3,871	3,940	3,933	3,719	3,971	3,863	4,501	5,002	5,506	5,943	6,394
Tax revenue	2,630	2,712	2,843	2,625	2,762	2,982	3,577	4,035	4,498	4,916	5,313
Nontax revenues	1,241	1,228	1,090	1,094	1,209	881	923	966	1,008	1,027	1,081
o/w Fees	271	189	204	178	198	261	285	310	333	356	378
Bank of Algeria dividends and interests	920	1,000	800	800	900	500	500	500	500	478	492
Other	50	39	86	116	111	120	138	156	175	193	210
Grants	0	0	0	0	6	0	0	0	0	0	0
Total expenditure (incl. net lending and special Treasury accounts)	7,638	8,223	8,566	7,839	8,176	8,665	11,444	11,596	12,249	12,896	13,676
Current expenditure	4,677	5,314	4,895	5,009	5,444	5,919	8,113	8,299	8,953	9,411	10,085
Current non-interest	4,508	5,212	4,781	4,838	5,300	5,649	7,690	7,813	8,449	8,789	9,347
Personnel expenditure	2,218	2,169	2,283	2,283	2,363	2,414	3,241	3,250	3,534	3,682	3,919
Mudjahidins' pensions	228	242	253	267	206	260	281	332	354	405	428
Material and supplies	189	216	216	109	171	131	228	255	282	308	333
Current transfers 3/	1,874	2,584	2,029	2,178	2,560	2,844	3,940	3,976	4,279	4,394	4,667
Interest payments	169	102	114	172	144	270	422	486	505	623	738
Capital expenditure	2,605	2,418	2,846	1,894	1,985	1,889	2,412	2,338	2,305	2,494	2,601
Net lending and special Treasury accounts net operations	356	491	825	937	748	857	920	960	990	990	990
Budget balance	-1,235	-905	-1,140	-1,262	-842	1,454	-1,073	-1,175	-1,349	-1,623	-1,907
Overall balance	-1,590	-1,396	-1,965	-2,199	-1,590	597	-1,993	-2,135	-2,339	-2,613	-2,897
Nonhydrocarbon balance	-3,767	-4,283	-4,633	-4,120	-4,199	-4,802	-6,944	-6,595	-6,743	-6,953	-7,282
Nonhydrocarbon primary balance (excluding Bank of Algeria dividends)	-4,518	-5,181	-5,319	-4,748	-4,962	-5,032	-7,022	-6,609	-6,738	-6,809	-7,036
Net financing	1,590	1,396	1,965	2,199	3,669	-77	1,993	2,135	2,339	2,613	2,897
Domestic	1,593	1,399	1,966	2,200	3,676	-63	2,006	2,148	2,354	2,627	2,912
Bank 4/	1,510	932	1,842	1,302	3,267	-583	1,966	2,108	2,314	2,587	2,872
o/w gross central bank financing	2,185	3,371	1,001	1	517	0	0	0	0	0	0
Nonbank 5/	83	467	125	898	409	520	40	40	40	40	40
Foreign	-3	-3	-2	-2	-7	-14	-13	-13	-15	-14	-15
Memorandum items											
Gross financing requirements	3,356	2,323	2,525	2,720	2,438	287	3,201	3,612	3,544	3,389	4,849
Financing need to be filled with new domestic debt issuance	2,922	3,343	2,172	628	4,995	1,605	1,460	3,272	3,504	3,349	4,809
Principal payments on public debt	1,766	927	561	522	849	884	1,207	1,477	1,205	777	1,952
Oil stabilization fund											
in billions of Algerian dinars	0	306	306	0	682	2,000	300	0	0	0	0.0
in percent of GDP	0.0	1.5	1.5	0.0	3.1	7.2	1.0	0.0	0.0	0.0	0.0
Gross government debt, including guarantees (percent of GDP)	44.4	54.6	62.7	71.0	78.7	56.1	52.9	55.1	57.6	60.3	63.4
Gross government debt, excluding guarantees (percent of GDP)	26.8	38.3	46.0	52.0	62.8	52.4	49.4	51.9	54.6	57.5	60.8
o/w owed to central bank ..	11.6	27.2	32.0	35.5	29.7	23.4	20.3	17.2	14.2	12.7	11.0

Sources: Algerian authorities; and IMF staff estimates and projections.
1/ On cash basis.
2/ Including Sonatrach dividends.
3/ Includes 500 billion dinars of transfers to the pension fund in 2018
4/ Bank financing includes domestic debt issuance and a drawdown of the oil stabilization fund and other government deposits at the central bank. It includes the repurchase of syndicated loans owed by SOEs for a total amount of DZD 2,080 billion in 2021 and DZD 520 billion in 2022, under the financial scheme including the PSR.
5/ Includes proceeds from sales of state-owned assets.

Table 3b. Algeria: Summary of Central Government Operations, 2017–27 1/

(percent of GDP, unless otherwise stated)

						Projections					
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
						(In percent of GDP)					
Budget revenue and grants	32.0	33.4	32.2	30.5	29.8	33.2	31.4	29.5	28.5	27.5	26.9
Hydrocarbon revenue 2/	11.5	14.1	13.0	10.4	11.8	19.4	16.5	13.9	12.7	11.6	10.9
Nonhydrocarbon revenue	20.5	19.3	19.2	20.1	18.0	13.9	15.0	15.6	15.8	15.9	15.9
Tax revenue	13.9	13.3	13.9	14.2	12.5	10.7	11.9	12.6	12.9	13.1	13.2
Nontax revenues	6.6	6.0	5.3	5.9	5.5	3.2	3.1	3.0	2.9	2.7	2.7
o/w Fees	1.4	0.9	1.0	1.0	0.9	0.9	0.9	1.0	1.0	0.9	0.9
Bank of Algeria dividends and interests	4.9	4.9	3.9	4.3	4.1	1.8	1.7	1.6	1.4	1.3	1.2
Other	0.3	0.2	0.4	0.6	0.5	0.4	0.5	0.5	0.5	0.5	0.5
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total expenditure (including net lending and special accounts)	40.5	40.2	41.8	42.4	37.0	31.1	38.1	36.1	35.2	34.4	34.1
Current expenditure	24.8	26.0	23.9	27.1	24.7	21.2	27.0	25.9	25.8	25.1	25.1
Current non-interest	23.9	25.5	23.3	26.2	24.0	20.3	25.6	24.3	24.3	23.5	23.3
Personnel expenditure	11.7	10.6	11.1	12.4	10.7	8.7	10.8	10.1	10.2	9.8	9.8
Mudjahidins' pensions	1.2	1.2	1.2	1.4	0.9	0.9	0.9	1.0	1.0	1.1	1.1
Material and supplies	1.0	1.1	1.1	0.6	0.8	0.5	0.8	0.8	0.8	0.8	0.8
Current transfers 3/	9.9	12.6	9.9	11.8	11.6	10.2	13.1	12.4	12.3	11.7	11.6
Interest payments	0.9	0.5	0.6	0.9	0.7	1.0	1.4	1.5	1.5	1.7	1.8
Capital expenditure	13.8	11.8	13.9	10.2	9.0	6.8	8.0	7.3	6.6	6.7	6.5
Net lending and special Treasury accounts net operations	1.9	2.4	4.0	5.1	3.4	3.1	3.1	3.0	2.8	2.6	2.5
Budget balance	-6.5	-4.4	-5.6	-6.8	-3.8	5.2	-3.6	-3.7	-3.9	-4.3	-4.8
Overall balance	-8.4	-6.8	-9.6	-11.9	-7.2	2.1	-6.6	-6.7	-6.7	-7.0	-7.2
Primary overall balance	-7.5	-6.3	-9.0	-11.0	-6.5	3.1	-5.2	-5.1	-5.3	-5.3	-5.4
Nonhydrocarbon balance	-20.0	-20.9	-22.6	-22.3	-19.0	-17.2	-23.1	-20.5	-19.4	-18.6	-18.1
Nonhydrocarbon primary balance (excluding Bank of Algeria dividends)	-23.9	-25.3	-25.9	-25.7	-22.4	-18.1	-23.4	-20.6	-19.4	-18.2	-17.5
Net financing	8.4	6.8	9.6	11.9	16.6	-0.3	6.6	6.7	6.7	7.0	7.2
Domestic	8.4	6.8	9.6	11.9	16.6	-0.2	6.7	6.7	6.8	7.0	7.3
Bank 4/	8.0	4.6	9.0	7.0	14.8	-2.1	6.5	6.6	6.7	6.9	7.2
o/w gross central bank financing	11.6	16.5	4.9	0.0	2.3	0.0	0.0	0.0	0.0	0.0	0.0
Nonbank 5/	0.4	2.3	0.6	4.9	1.9	1.9	0.1	0.1	0.1	0.1	0.1
Foreign	0.0	0.0	0.0	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0
						(In percent of non-oil GDP)					
Budget revenue and grants	39.9	42.9	40.0	35.5	38.4	47.0	42.3	37.8	35.9	34.2	33.1
Hydrocarbon revenue 2/	14.3	18.2	16.2	12.1	15.2	27.4	22.1	17.8	16.0	14.4	13.4
Nonhydrocarbon revenue	25.5	24.8	23.8	23.4	23.1	19.6	20.1	20.0	19.9	19.7	19.6
Tax revenue	17.3	17.1	17.2	16.5	16.1	15.1	16.0	16.1	16.3	16.3	16.3
Nontax revenues	8.2	7.7	6.6	6.9	7.0	4.5	4.1	3.9	3.7	3.4	3.3
Fees	1.8	1.2	1.2	1.1	1.2	1.3	1.3	1.2	1.2	1.2	1.2
Bank of Algeria dividends and interests	6.1	6.3	4.8	5.0	5.2	2.5	2.2	2.0	1.8	1.6	1.5
Other	0.3	0.2	0.5	0.7	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total expenditure (including net lending and special accounts)	50.3	51.7	51.9	49.3	47.6	44.0	51.2	46.4	44.4	42.8	41.9
Current expenditure	30.8	33.4	29.7	31.5	31.7	30.0	36.3	33.2	32.4	31.3	30.9
Current non-interest	29.7	32.8	29.0	30.4	30.9	28.7	34.4	31.3	30.6	29.2	28.7
Personnel expenditure	14.6	13.6	13.8	14.4	13.8	12.2	14.5	13.0	12.8	12.2	12.0
Mudjahidins' pensions	1.5	1.5	1.5	1.7	1.2	1.3	1.3	1.3	1.3	1.3	1.3
Material and supplies	1.2	1.4	1.3	0.7	1.0	0.7	1.0	1.0	1.0	1.0	1.0
Current transfers 3/	12.3	16.3	12.3	13.7	14.9	14.4	17.6	15.9	15.5	14.6	14.3
Interest payments	1.1	0.6	0.7	1.1	0.8	1.4	1.9	1.9	1.8	2.1	2.3
Capital expenditure	17.2	15.2	17.2	11.9	11.6	9.6	10.8	9.4	8.4	8.3	8.0
Net lending and special Treasury accounts net operations	2.3	3.1	5.0	5.9	4.4	4.3	4.1	3.8	3.6	3.3	3.0
Budget balance	-8.1	-5.7	-6.9	-7.9	-4.9	7.4	-4.8	-4.7	-4.9	-5.4	-5.8
Overall balance	-10.5	-8.8	-11.9	-13.8	-9.3	3.0	-8.9	-8.5	-8.5	-8.7	-8.9
Primary overall balance	-9.4	-8.1	-11.2	-12.7	-8.4	4.4	-7.0	-6.6	-6.6	-6.6	-6.6
Nonhydrocarbon balance	-24.8	-26.9	-28.1	-25.9	-24.5	-24.4	-31.0	-26.4	-24.4	-23.1	-22.3
Nonhydrocarbon primary balance (excluding Bank of Algeria dividends)	-29.8	-32.6	-32.2	-29.9	-28.9	-25.5	-31.4	-26.4	-24.4	-22.6	-21.6
Net financing	10.5	8.8	11.9	13.8	21.4	-0.4	8.9	8.5	8.5	8.7	8.9
Domestic	10.5	8.8	11.9	13.8	21.4	-0.3	9.0	8.6	8.5	8.7	8.9
Bank 4/	9.9	5.9	11.2	8.2	19.0	-3.0	8.8	8.4	8.4	8.6	8.8
o/w central bank	14.4	21.2	6.1	0.0	3.0	0.0	0.0	0.0	0.0	0.0	0.0
Nonbank 5/	0.5	2.9	0.8	5.6	2.4	2.6	0.2	0.2	0.1	0.1	0.1
Foreign	0.0	0.0	0.0	0.0	0.0	-0.1	-0.1	-0.1	-0.1	0.0	0.0

Sources: Algerian authorities; and IMF staff estimates and projections.

1/ On cash basis.
2/ Including Sonatrach dividends.
3/ Includes 500 billion dinars of transfers to pension fund in 2018

4/ Bank financing includes domestic debt issuance and a drawdown of the oil stabilization fund and other government deposits at the central bank. It includes the repurchase of syndicated loans owed by SOEs for a tot
amount of DZD 2,080 billion in 2021 and DZD 520 billion in 2022, under the financial scheme including the PSR.

5/ Includes proceeds from sales of state-owned assets.

Table 4. Algeria: Monetary Survey, 2017–27

(in billions of dinars, unless otherwise stated)

						Projections					
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027
					(In billions of Algerian dinars; at end of period)						
Net foreign assets	11,058	9,316	7,429	6,321	5,994	8,165	9,704	10,001	9,693	8,786	7,525
o/w Bank of Algeria	11,155	9,406	7,472	6,384	6,036	8,173	9,684	9,959	9,632	8,709	7,433
Foreign assets (BA)	11,354	9,606	7,672	6,615	6,636	8,783	10,325	10,631	10,338	9,450	8,211
Foreign liabilities (BA)	199	200	200	231	600	610	640	672	706	741	778
Foreign assets (comm. banks)	65	92	90	82	95	96	101	106	112	117	123
Foreign liabilities (comm. banks)	163	182	134	144	137	104	82	64	51	40	31
Net domestic assets	3,916	7,321	9,082	11,419	14,085	14,305	15,772	17,669	20,061	23,015	26,481
o/w Bank of Algeria	-4,978	-2,749	-839	495	1,519	1,025	680	1,428	2,574	4,502	6,659
Domestic credit	12,629	15,298	16,828	19,126	21,259	21,988	24,211	26,602	29,491	32,912	36,794
Credit to government (net) 1/	3,641	5,200	5,820	7,788	11,296	10,712	12,678	14,786	17,100	19,687	22,559
Credit to the economy	8,989	10,097	11,008	11,338	9,964	11,276	11,532	11,816	12,391	13,225	14,235
o/w Private sector	4,606	5,078	5,291	5,459	5,700	5,954	6,031	6,121	6,295	6,494	6,733
Other items net	-8,713	-7,977	-7,746	-7,707	-7,174	-7,683	-8,438	-8,933	-9,430	-9,898	-10,313
Money and quasi-money (M2)	14,974	16,637	16,511	17,740	20,079	22,470	25,476	27,670	29,754	31,801	34,005
Excluding Sonatrach deposits	13,983	15,573	16,073	17,496	19,143	20,122	23,282	25,751	27,807	29,837	32,002
o/w Money	10,266	11,404	10,979	11,931	12,206	12,830	14,845	16,419	17,730	19,024	20,405
Reserve money	6,177	6,658	6,633	6,879	8,143	9,787	10,953	11,976	12,794	13,799	14,681
					(In percent change over 12-month period)						
Money and quasi-money (M2)	8.4	11.1	-0.8	7.4	13.2	11.9	13.4	8.6	7.5	6.9	6.9
Credit to the economy 2/	11.9	12.3	9.0	3.0	-12.1	13.2	2.3	2.5	4.9	6.7	7.6
o/w Private sector	15.0	10.2	4.2	3.2	4.4	4.5	1.3	1.5	2.8	3.2	3.7
Memorandum items:											
Credit to the economy/GDP	47.6	49.4	53.7	61.4	45.1	40.5	38.4	36.8	35.7	35.3	35.5
Credit to the economy/NHGDP	59.2	63.5	66.7	71.3	58.0	57.2	51.6	47.3	44.9	43.9	43.7
Credit to private sector/NHGDP	30.4	31.9	32.0	34.3	33.2	30.2	27.0	24.5	22.8	21.6	20.6

Sources: Bank of Algeria; and IMF staff estimates and projections.

1/ Net credit to government excludes Treasury postal account("dépôts CCP") deposited at the BA.

2/ The decline in credit to the economy in 2021 and 2022 reflects the effect of a debt buyback operation by the Treasury which reduced banks' claims on state-owned enterprises (the public sector).

Table 5. Algeria: Financial Soundness Indicators, 2010–21

(in percent)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021 (Prelim.)
Capital adequacy ratio	23.6	23.7	23.4	21.5	15.8	18.4	18.8	19.5	19.0	18.0	19.2	21.8
- Public banks	21.7	21.9	21.6	19.9	14.7	17.8	18.4	19.6	19.2	17.8	19.0	22.3
- Private banks	31.6	31.2	31.9	28.5	20.4	21.0	20.3	18.9	18.2	18.9	20.3	20.0
Tier I capital adequacy ratio	17.7	16.9	17.5	15.5	13.2	15.8	16.2	15.0	15.0	14.3	15.4	17.9
- Public banks	14.8	14.1	14.8	13.1	11.6	14.6	15.4	14.3	14.4	13.5	14.6	17.6
- Private banks	29.3	28.8	29.7	26.3	19.7	20.3	19.6	18.1	17.4	18.2	19.5	19.2
NPLs net of provisions/Regulatory capital	21.1	19.4	16.1	17.1	24.8	26.5	35.0	36.4	39.3	52.6	59.6	58.5
- Public banks	27.5	25.1	20.3	21.7	28.1	29.6	40.0	40.8	44.9	60.7	69.2	68.4
- Private banks	3.0	2.3	3.2	2.6	14.5	15.8	16.7	16.2	13.4	14.6	14.0	12.6
NPLs/total loans	18.3	14.5	11.5	10.6	9.9	9.8	12.1	13.0	12.7	14.8	16.4	19.3
- Public banks	20.5	16.1	12.4	11.4	10.1	9.9	12.6	13.7	13.4	15.6	17.2	20.7
- Private banks	4.1	4.0	5.2	4.8	8.5	8.6	8.7	7.8	7.1	8.2	9.7	9.6
NPLs net of provisions/total loans	4.9	4.4	3.5	3.4	3.8	3.9	5.5	6.2	6.3	7.9	8.8	10.1
- Public banks	5.4	4.9	3.9	3.7	3.7	3.8	5.6	6.5	6.8	8.4	9.5	11.1
- Private banks	1.4	1.0	1.3	0.9	4.7	4.7	4.6	3.9	3.0	3.4	3.4	3.1
Provisions/classified loans	76.5	69.8	69.5	68.2	61.8	59.9	54.6	52.3	50.1	46.7	46.1	47.5
- Public banks	73.7	69.6	69.4	67.4	63.6	61.5	55.4	52.4	49.4	45.9	44.8	46.2
- Private banks	66.7	75.9	71.7	80.3	45.0	45.3	46.1	50.6	57.3	58.7	65.2	67.4
Return on equity	16.7	24.7	23.3	19.0	23.7	21.3	17.8	18.8	22.4	13.7	8.3	11.2
- Public banks	29.8	26.1	22.7	18.0	25.1	23.1	18.9	20.0	22.7	11.9	7.3	10.4
- Private banks	20.3	21.4	24.8	21.5	20.0	16.1	15.3	14.7	21.2	22.4	13.6	15.4
Return on assets	2.2	2.1	1.9	1.7	2.0	1.9	1.8	2.0	2.4	1.5	1.4	1.9
- Public banks	1.8	1.8	1.5	1.3	1.8	1.7	1.7	2.0	2.3	1.2	1.2	1.8
- Private banks	4.6	4.5	4.5	3.7	3.4	3.1	2.8	2.6	3.4	3.2	2.7	3.0
Interest margin/gross revenues	63.8	64.9	64.2	69.5	67.2	66.8	72.5	73.0	78.8	78.9	73.4	78.7
- Public banks	71.6	73.6	72.1	73.3	66.7	65.8	72.3	72.7	80.8	81.7	73.0	78.5
- Private banks	44.2	44.4	45.2	59.1	69.1	71.5	73.4	74.2	71.1	69.7	75.3	79.3
Non-interest expenses/earnings before tax	31.4	33.6	35.6	33.5	40.7	40.0	34.1	36.0	29.3	30.8	35.8	34.9
- Public banks	31.6	34.8	38.1	34.0	40.6	39.2	31.4	33.7	26.4	28.1	34.3	32.1
- Private banks	31.0	30.8	29.8	32.3	41.3	43.4	46.3	46.2	40.5	39.5	41.5	43.6
Liquid assets/total assets	53.0	50.2	45.9	40.5	38.0	27.1	23.5	23.5	19.8	16.0	13.1	35.7
- Public banks	54.2	51.1	45.1	39.4	37.0	25.8	22.7	21.9	18.4	14.2	10.3	35.7
- Private banks	43.7	43.2	50.9	46.5	44.0	35.9	29.1	33.1	28.5	27.3	30.3	36.3
Liquid assets/short-term debt	114.3	103.7	107.5	93.5	82.1	61.6	58.4	53.7	47.4	44.2	37.1	101.7
- Public banks	118.1	106.6	110.5	95.7	83.4	60.2	58.8	52.2	46.3	42.2	31.5	109.6
- Private banks	88.5	84.6	93.5	84.1	75.4	69.8	56.2	60.6	52.6	52.5	59.5	68.9

Source: Banque d'Algérie

Annex I. External Sector Assessment

Overall Assessment: *Algeria's external position in 2022 was stronger than the level implied by fundamentals and desirable policy settings, taking into account the heightened risks to the external outlook. The current account gap, based on the results of the IMF's EBA-lite current account model, is estimated at 4.7 percent of GDP in 2022, reflecting a substantial improvement of Algeria's external position compared to the current account gap of -2.8 percent in 2021.*[1] *But, this external improvement, mainly driven by the rally in hydrocarbon prices coupled with continued import regulation measures that resulted in a current account surplus—the first since 2013, is subject to hydrocarbon prices' volatility and could be quickly reversed given existing vulnerabilities and announced policies. Foreign exchange reserves have risen, halting the downtrend in recent years, and are projected toto decline over the medium-term while remaining above adequacy metrics. External debt is low but could increase rapidly in the event of adverse shocks or if large fiscal deficits cannot be entirely financed domestically.*

Potential Policy Responses: *Continued fiscal consolidation anchored in a credible medium-term framework, combined with structural reforms—to foster economic diversification and enhance non-price competitiveness— and greater flexibility of the nominal exchange rate would help ensure external sustainability over the medium-term. Regulation measures taken since 2015 to contain imports cannot substitute needed reforms to support domestic production.*

Foreign Assets and Liabilities: Position and Trajectory

Background. Algeria's external assets consist mostly of international reserves, whose size dwarfs Foreign Direct Investment (FDI) liabilities and external debt. International reserves, excluding monetary gold but including SDRs, increased to US$62 billion in 2022, representing 13.4 months of imports, after a steady decline to a hollow of US$46.7 billion at end-2021. The NIIP increased from 18.3 percent of GDP in 2021 to 22.9 percent of GDP in 2022, mirroring the sharp increase in reserves assets.

Assessment. The dynamics of Algeria's NIIP mainly reflects its dependance on hydrocarbon exports, pointing to its vulnerabilities to price volatility over the medium term. Under the baseline scenario, the NIIP is projected to decline to 8.4 percent of GDP by 2027 as lower hydrocarbon prices result in current account deficit and reserves deaccumulation. Reserve coverage is projected to decline to around 8.4 months of imports by 2027.

2022 (% GDP)	NIIP:	Gross Assets:	Debt Assets:	Gross Liab.:	Debt Liab.:
	22.9	40.6	2.2	17.7	6.9

[1]The external sector assessment is based on staff's estimates.

Current Account

Background. Algeria's external current account balance is largely determined by the balance of trade in goods. Hydrocarbons make up the bulk of goods exports, despite a continuous increase in non-hydrocarbons exports since 2021. The share of hydrocarbons in total exports, while declining, is significant and averaged 85 percent between 2017 and 2022. The current account balance has substantially improved in 2022 to a surplus of 7.6 percent of GDP, due to the increase in hydrocarbon exports and the containment of imports. Goods imports have declined in tandem with government capital spending. Various import compression policies introduced since 2015, to protect FX reserves and reduce over invoicing and fraud, coupled with conjectural factors also contributed to reducing imports, especially in the non-food consumer goods and industrial equipment categories. Goods imports declined from 31.7 percent of GDP in 2015 to 20.6 percent in 2022. The improvement in the current account balance in 2022 largely reflects an increase in saving and a decline in investment for the government.

Assessment. The EBA-lite current account (CA) model approach of the Fund's external balance assessment methodologies (updated in 2022) suggests that the current account balance climbed above its norm in 2022, a substantial improvement compared to 2021, translating into a REER undervaluation. High hydrocarbon prices have also led to fiscal surplus in 2022, further highlighting the strong correlation between fiscal and external balances and the structure of the exports. Going forward, a continued fiscal consolidation coupled with greater nominal exchange rate flexibility would help contain policy gaps and maintain the current account balance closer to its norm over the medium term as hydrocarbon prices come down.

- The EBA-lite current account model suggests that the actual current account, adjusted for the temporary effect of the pandemic on oil prices and export volumes was substantially stronger than warranted by medium-term fundamentals and desirable policies in 2022. The current account gap estimated using this approach was 4.7 percent of GDP, of which 4.3 percent of GDP reflects the contribution from the increase in reserves in 2022 and 3.3 percent reflects the domestic fiscal policy gap related to the one-off fiscal surplus in 2022. Given an assumed elasticity of the current account with respect to the REER of -2.1, this translates into a REER undervaluation of 2.3 percent. However, this external improvement is driven by a combination of exceptional factors in 2022—high hydrocarbon prices and import compression measures, as well as unexpected fiscal consolidation. This assessment is subject to considerable uncertainty related to underlying assumptions about long-term hydrocarbon prices. Going forward, the external position risks a quick reversal given the volatility of hydrocarbon prices, the projected declined in reserves, as well as announced expansionary policies. As noted in previous assessments, the existence of a parallel exchange market also complicates the interpretation of model results. Taking all these factors into account, staff assesses the external position in 2022 to be stronger than warranted by medium-term fundamentals and desirable policies in 2022.
- The current account norm estimated using consumption allocation rules for exporters of exhaustible resources is 11.5 percent of GDP in the medium term against a projected cyclically adjusted CA of -7.1 percent of GDP, implying that Algeria's current account trajectory is not consistent with intergenerational equity. A consumption-based model, which accounts for the exhaustibility of

resources to determine the sustainability of the current account trajectory, suggests that the projected medium-term current account path is inconsistent with intergenerational equity despite the near-term surplus. Notably, the current account path is considered sustainable if the Net Present Value (NPV) of future wealth (in this case hydrocarbon revenues plus income on financial assets or investment) are bigger or equal to the NPV of imports of goods and services net of non-oil exports.[1] This intertemporal constraint generates a path for imports ('annuities' or 'allocation rules') and thus a current account norm consistent with intergenerational equity.[2] Import trajectories calculated under a constant real per capita annuity allocation rule, to account for population growth, yield a current account norm of 11.5 percent of GDP in the medium term. Given the projected path for the current account deficits over 2022-27, a significant current account gap of -18.6 percent of GDP would remain over the medium term in the absence of further savings.

Algeria: EBA-lite Model Results, 2022

	CA model 1/	**REER model** 1/
	(in percent of GDP)	
CA-Actual	**7.6**	
Cyclical contributions (from model) (-)	1.9	
COVID-19 adjustors (-) 2/	0.1	
Natural disasters and conflicts (-)	0.1	
Adjusted CA	**5.5**	
CA Norm (from model) 3/	**0.8**	
Adjusted CA Norm	**0.8**	
CA Gap	**4.7**	**31.5**
o/w Relative policy gap	8.3	
Elasticity	-2.1	
REER Gap (in percent)	**-2.3**	**-15.2**

1/ Based on the EBA-lite 3.0 methodology
2/ Additional cyclical adjustment to account for the temporary impact of the tourism (0.1 percent of GDP).
3/ Cyclically adjusted, including multilateral consistency adjustments.

Real Exchange Rate

Background. The REER has appreciated by around 8.8 percent between December 2021 and end-November 2022, owing to high hydrocarbon prices and a nominal appreciation of the dinar, and marked a pause in the continuous depreciation of the REER since 2015. For instance, the REER depreciated by 10.6 percent between January 2015 and December 2021, albeit with periods of relative stability during 2018-19. But the gradual pace of depreciation combined with the small size of the nonhydrocarbon tradeable sector and supply-side constraints dampened the effect on the overall competitiveness. Expansionary fiscal policy also offset the impact of REER depreciation on the current account given the high import content of public spending, notably investment.

Assessment. The EBA-REER model estimates suggest an undervaluation of 15.2 percent but are unreliable. Staff assessment gives more weight to the EBA-lite CA model, which has often proven to be more informative and reliable than the REER model. The latter tends to be a poor fit for many countries as it does not adequately capture country-specific characteristics (IMF, 2019).

Capital and Financial Accounts: Flows and Policy Measures

Background. Algeria's economy remains mostly closed to external capital flows. Inward FDI declined from 0.9 percent of GDP in 2018 to 0.6 percent in 2021. It is projected to increase slightly to 0.75 of GDP in 2022, considering the impact of reforms and change in regulations. Portfolio flows were nil.

Assessment. The elimination of the 49 percent limit on foreign ownership in Algerian investment projects (the '51/49' rule), except for strategic sectors, removed an important constraint on inward FDI. Ongoing reforms (new investment law, digitalization initiatives), if accompanied by efforts to improve the business climate and policy predictability could improve attract FDI in the medium-term. The abolition in 2021 of the surrender requirements, except for hydrocarbon and mineral exports, could help ease supply bottlenecks by facilitating imports of raw materials and inputs.

FX Intervention and Reserves Level

Background. Algeria's official reserves are projected to increase in the near-term, driven by the improved outlook for hydrocarbon prices and exports, before falling over the medium-term. The country has been financing its current account deficits since 2014 by running down foreign exchange reserves. The de jure exchange rate arrangement is managed floating, while the de facto exchange rate arrangement is a crawling-like arrangement The BA intervenes in the foreign exchange market directly by proposing its own rates and by making foreign exchange available to banks at their request. The BA sets the buying and selling rates of the dinar against the US dollar in this market within a margin of 0.015 dinar.

Assessment. FX reserves have increased in 2022, but the downward trajectory in FX reserves is expected to resume from 2024 with their level dropping below 10 months of imports by 2027(to around 111 percent of the ARA metric).

[1] Proven hydrocarbon reserves at end-2022 were estimated at 12,200 million barrels for crude oil and 4,504 cubic meters for natural gas (OPEC, 2020). Staff projections assume that hydrocarbons production grows at a constant rate of 1 percent, peaking in 2040. From 2041 onwards, both production and consumption decline by 1 percent annually. Hydrocarbon prices are assumed to increase in line with the US GDP deflator by 1.9 percent. Future hydrocarbons revenues are discounted at a rate of 5 percent, which is the assumed rate of return on foreign assets, while population growth is 1.4 percent.

[2] Bems, R. and I. de Carvalho Filho. 2009. "Exchange Rate Assessments: Methodologies for Oil-Exporting Countries", IMF Working Paper 09/281.

Annex II. Risk Assessment Matrix[1]

Risks	Likelihood	Impact	Policy Response
Conjunctural risks			
Commodity price shocks. A combination of continuing supply disruptions (e.g., due to conflicts and export restrictions) and negative demand shocks causes recurrent commodity price volatility and social and economic instability.	High	**High.** Algeria's economy is highly dependent on hydrocarbon exports and food imports. Recurrent commodity price volatility, reflecting continuing supply disruptions (e.g., due to global conflicts and export restrictions) and negative demand shocks would significantly worsen the external position and may generate destabilizing spending cycles.	Implement broad-based fiscal consolidation to help curb inflationary pressures, rebuild buffers, and prepare for downside risks. Allow the nominal exchange rate to act as shock absorber, in the context of tighter policies. Continue the implementation of reforms to diversify the economy. Strengthen the fiscal framework to reduce fiscal policy procyclicality.
Systemic social unrest. Rising inflation, declining incomes, and worsening inequality amplify social unrest and political instability, causing capital outflows from EMDEs, slowing economic growth, and giving rise to economically-damaging populist policies (e.g., preserving fossil fuel subsidies).	High	**Low.** Social unrest spreading globally is not likely to significantly impact Algeria but rising living costs could stoke social tensions domestically.	Tighten monetary and fiscal policies to curb inflationary pressures. Reprioritize spending and improve its efficiency to help finance targeted and temporary measures to low-income households.
De-anchoring of inflation expectations and stagflation. Supply shocks to food and energy prices sharply increase headline inflation and pass through to core inflation, de-anchoring inflation expectations and triggering a wage-price spiral in tight labor markets. Central banks tighten monetary policy more than envisaged leading to weaker global demand, currency depreciations in EMDEs, and sovereign defaults. Together, this could lead to the onset of stagflation.	Medium	**High.** Higher than expected inflation from global prices or domestic sources could de-anchor inflation expectations and generate a self-reinforcing inflation spiral.	Tighten monetary policy without delay and strengthen the transmission of policy. Implement broad-based fiscal consolidation and target transfers and subsidies to curb inflationary pressures while supporting low-income households Implement structural reforms and improve the policy framework to limit the effect of policy tightening on growth.

[1]The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path. The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Risks	Likelihood	Impact	Policy Response
Abrupt global slowdown or recession: Europe. The fallout from the war in Ukraine is exacerbated by a gas shutoff by Russia, resulting in acute gas shortages and further supply disruptions, which triggers an EU recession.	**High**	**High.** An abrupt global slowdown would depress oil prices and demand. However, Algeria could still benefit from higher natural gas prices as countries in Europe seek to diversify supply in the context of Russia's war in Ukraine.	Tighten monetary policy Implement broad-based fiscal consolidation to help curb inflationary pressures, rebuild buffers, and prepare for downside risks. Allow the nominal exchange rate to act as shock absorber, in the context of tighter monetary and fiscal policies. Continue the implementation of reforms to diversify the economy. Strengthen the fiscal framework to reduce fiscal policy procyclicality.
Local COVID-19 outbreaks. Outbreaks in slow-to-vaccinate countries or emergence of more contagious vaccine-resistant variants force new lockdowns or inhibit commerce. This results in extended supply chain disruptions, slower growth, capital outflows, and debt distress in some EMDEs.	**Medium**	**Medium.** The emergence of more transmissible and/or deadly variants in Algeria or elsewhere could disrupt lives and livelihoods. The reintroduction of lockdowns or border closures could exacerbate supply constraints.	Accelerate the vaccination campaign, possibly with vaccines adapted to new variants. Prepare fiscal contingency plan to reallocate spending and deploy targeted and temporary measures if needed
Structural risks			
Deepening geo-economic fragmentation and geopolitical tensions.	**High**	**Medium.** Deepening geo-economic fragmentation and geopolitical tensions could disrupt trade flows and hamper economic diversification attempts. Algeria could nevertheless benefit in the short-term if there is, an increase in hydrocarbon prices.	Accelerate diversification and economic resilience through well-timed and sequenced implementation of the reforms outlined in the Government Action Plan, and measures to strengthen the fiscal and monetary policy frameworks
More frequent natural disasters causing water and food shortages and reducing medium-term growth.	**Medium**	**High.** Algeria is vulnerable, like other countries in North Africa, to climate shocks. In addition to the impact on lives and livelihoods, these shocks could entail large fiscal costs and add to inflationary pressures.	Invest in climate-resilient infrastructure and agriculture Accelerate economic diversification, including by harnessing the potential of renewable energies

Risks	Likelihood	Impact	Policy Response
Idiosyncratic risks			
Calls on government-guaranteed debt or capital injections needs for public banks or SOEs	**High**	**High.** Calls on government guarantees, or capital injections would worsen the trajectory of public debt. A deterioration in the balance sheet of public banks and SOEs would dampen bank lending, investment and growth.	Improve monitoring and management of fiscal risks Streamline governance of SOEs and condition state support on improved transparency, restructuring and reforms Develop a government shareholder policy focused on enhancing profitability and efficiency Divest from non-core assets and open the capital of selected SOEs to the private sector
Deepening sovereign-bank nexus	**High**	**High.** Fiscal financing needs are projected to remain significant in the absence of consolidation and/or diversification of funding sources. The strengthening of feedback loops weakens the monetary policy transmission mechanism and raises concern for financial stability.	Prohibit any form of direct or indirect financing of the budget deficit by the Central Bank and strengthen its independence Expand available fiscal space by mobilizing nonhydrocarbon revenue and reducing spending Adopt a medium-term fiscal adjustment plan. Explore alternative non-inflationary financing for the deficit, including foreign borrowing Reform the governance of public banks, focus their lending on profitable projects and implement a detailed assessment of their loan portfolio and other assets
Partial or delayed implementation of macroeconomic adjustment and necessary structural reforms	**Medium**	**High.** Partial or delayed reform implementation could entail significant costs to the budget, while yielding limited growth dividends and increasing risk of policy inconsistency and reform reversals.	Increase transparency about the state of the economy, including through timely publication of economic data and communication. Adopt a medium-term fiscal adjustment plan supported by coherent monetary and exchange rate policies. Provide additional temporary and targeted fiscal support to low-income households to mitigate the social impact of reforms

Annex III. Public and External Debt Sustainability Analysis

A significant fall in Algeria's government debt in 2022 will bring down its medium-term trajectory and support its sustainability. Government debt is projected to remain at moderate levels through the medium term, despite forecast wide fiscal deficits. However, debt sustainability is constrained by a narrow range of available funding sources given reluctance to foreign borrowing and limits to the domestic financial system's absorption capacity. Large contingent liabilities from SOEs and an aggravating sovereign-bank nexus pose significant risks to the debt path. Support from the central bank has put a lid on borrowing costs so far but an increase in interest rates is needed amidst high inflation and could worsen debt dynamics. The outlook for public finances is highly contingent on hydrocarbon prices.

1. Algeria's government debt is projected to fall in 2022 after rising rapidly in recent years. Central government debt, excluding guarantees on loans to SOEs, had risen by nine folds between 2013 and 2021, but is projected to fall to 52.4 percent of GDP at end-2022 from 62.8 percent of GDP at-end 2021, driven down by a primary fiscal surplus and strong nominal GDP growth given the upswing in hydrocarbon prices. Past debt built-up was driven by the deterioration in the budget balance which shifted from continuing surpluses to recurrent deficits starting in 2009, as hydrocarbon revenue gradually declined while spending on wages, social transfers and investment increased. Transfers to off-budget entities also contributed to the rise in debt. Between 2018 and 2021, annual average budget transfers of 2.9 percent of GDP were channeled to the pension system to cover its financing shortfall. In 2016-17, the government recognized and settled liabilities of around 5 percent of GDP to SONATRACH—the national oil company—on subsidy-related losses. In 2017, the Treasury acquired loans owed by the national electricity and gas company Sonelgaz for an amount equivalent to 3 percent of GDP. The government purchased public bank loans to SOEs worth DZD 2,080 billion (9.4 percent of GDP) in 2021 and DZD 520 billion (1.9 percent of GDP) in 2022 as part of the financing operation built around the central bank's special refinancing operation (*"Plan Spécial de Refinancement", PSR)*.

2. A number of intra-public sector claims might yet add to the debt stock. The government has accumulated additional subsidy-related liabilities to SONATRACH of around DZD 900-1000 billion (4.1.-4.5 percent of the 2021 GDP) according to preliminary estimates. These liabilities are not reflected in government debt, as the Treasury and SONATRACH are yet to conclude an arrangement on their recognition and settlement, but the 2023 budget draft included provisions for the settlement of DZD 100 billion (0.3 percent of the forecast GDP) to SONATRACH. The Treasury has also tapped the deposits of public entities to finance the fiscal deficit for an average of around 2 percent of GDP per year over the last five years. Possible claims on the government arising from these financing operations are not included in government debt as defined by the authorities. Claims on the government by social security and the SOE in charge of the supply of pharmaceutical products are also being gradually settled and could add to the debt stock as payments are made.

3. A large share of government debt is owed to the central bank, and the debt stock is almost entirely denominated in dinar. Around 45 percent of government debt or 23 percent of GDP were directly owed to the BA in 2022, reflecting the monetization of the budget deficit between 2017 and 2019. Around 99 percent of debt was held domestically and denominated in dinars. Government external foreign-currency debt represented 0.6 percent of GDP and mostly comprised a €900 million loan obtained from the African Development Bank in 2019.

4. Debt is projected to resume its ascension after temporary fall in 2022-23 but remain at moderate levels through the medium term. Under staff's baseline scenario, debt-to-GDP is projected to fall further in 2023 as the large deficit forecast for that year is assumed to be financed through FRR drawdowns. Debt is projected to resume its rise from 2024 onwards, reaching 60.8 percent of GDP in 2027. This is despite significant projected improvement in the NHPD by 4 percent of NHGDP between 2021 and 2027 with progress on tax reforms and cuts to capital spending amid increasingly binding financing constraints. The forecast fiscal adjustment will not suffice to halt the rise in debt, as rise in the rigid current spending announced under the 2023 budget, a projected fall in the BA's dividend payments and a gradual decline in hydrocarbon prices mean that the overall deficit will remain elevated over the projection horizon. The financial imbalances of the pension system are also yet to be tackled, and large annual budget transfers to cover the system's financing shortfall will continue apace. Projected fiscal adjustment under staff's baseline is somewhat large by historical standards, tilting risks around the debt trajectory to the upside (see Realism of assumptions tool).

5. Meeting persistently high fiscal funding requirements only on domestic markets will be challenging. Gross financing requirements are projected to average 10.6 percent of GDP per year in 2023-2027, on wide fiscal deficits and increasing principal repayments coming due on government debt, including on liabilities owed to the BA. Algeria's external and FX debt are at negligible levels, leaving space for external borrowing, but the government's stated policy is to limit foreign financing only to strategic investment projects. However, the absorption capacity of the domestic debt market is modest. Claims on the government accounted for one third of bank assets in August 2022, posing risks of feedback loops between the banking sector, which is mostly dominated by state-owned banks, and the sovereign, particularly in light of high lending to SOEs and deterioration in bank asset quality. Furthermore, meeting fiscal financing needs arising from stated fiscal plans on the domestic market is likely to strain the banking sector's balance sheet, crowd out credit to the private sector and weigh on growth and macroeconomic stability.

6. Debt dynamics are particularly sensitive to a rise in interest rates. Past direct monetary financing and the financing operation built around the PSR have kept a lid on debt interest cost, with the budget interest expense remaining stable around its five-years average of 0.7 percent of GDP per year despite the sizeable rise in debt. Staff's baseline is premised on the continuation of low real rates on fiscal debt. However, the government's commitment not to resort to further central bank financing will likely translate into higher interest costs, while the needed monetary policy tightening to tame currently high inflation as well as the government's strategy of promoting

financial deepening would also require a welcome rise in market rates. Higher rates could lead to significant deterioration in debt dynamics, in the absence of sufficient consolidation to stabilize and ultimately bring down debt. As illustrated in the stress tests (see heatmap) a shock to real interest rates would push government debt to 70 percent of GDP in 2027 and average annual financing needs to 13 percent of GDP.

7. The debt trajectory is also vulnerable to a broad range of other shocks as illustrated by the results of stress tests summarized in the heatmap. A fall in hydrocarbon prices is a major risk. A combined macro-fiscal shock, illustrating for example a fall in oil prices, would cause debt to rise close to 80 percent of GDP by 2027. However, its exposure to fluctuations in oil prices is aggravated by the projected depletion of fiscal savings in the Revenue Regulation Fund (*Fonds de Régulation des recettes*, FRR) in the near term. A one-standard deviation shock to real growth, or a modest fiscal slippage would lead debt to rise well above 60 percent of GDP in 2027. The very low level of FX liabilities and natural hedge from the large share of FX-denominated hydrocarbon revenue in budget intakes limit the vulnerability of the debt trajectory to exchange rate movements. The predictive density of debt under the asymmetric distribution—which is more relevant than the symmetric distribution in this instance given the somewhat large fiscal adjustment already assumed under staff's baseline—points to material upside risks to the debt trajectory.

8. Sizeable contingent liabilities from the pension system and SOEs pose additional risks to the debt path. SOEs require recurrent government support, reflecting their quasi-fiscal role. Non-financial SOE debt to the domestic banking system was 15 percent of the forecast 2022 GDP in September 2022, around one fourth of which were explicitly guaranteed by the government. The exposure of public banks to public enterprises, SOE reliance on government support, and an aggravating sovereign-bank nexus sets a mechanism for a negative feedback loop that would amplify macroeconomic shocks and weaken debt sustainability and macroeconomic stability. The reform of the tax on professional activities *("taxe sur les activités professionnelles", TAP)* will address a major weakness in the business climate but could reduce the resources of provincial and local governments in the short run and require government support to fill the gap. Government plans to expand the portfolio of PPPs could give rise to additional contingent liabilities in the medium term.

9. The downward trend in total external debt, from already low levels, is projected to continue over the medium-term. Staff projections show that total external debt would decline from 1.9 percent in 2021 to 1.6 percent of GDP in 2022, due to the substantial current account surplus recorded in 2022. Total external debt is forecast to be broadly stable through 2027, as FX reserves are used to finance the widening current account deficit projected over the medium term under the baseline scenario. Bound stress tests show that the trajectory of external debt is nevertheless subject to several risks, notably an adverse current account shock (Table 1, Figure 6).

Figure 1. Algeria: Public Debt Sustainability Assessment - Baseline Scenario

(in percent GDP unless otherwise indicated)

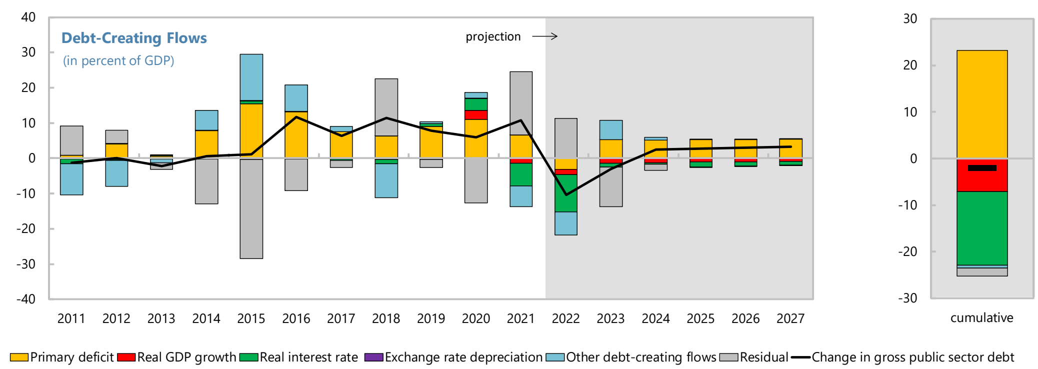
Debt, Economic and Market Indicators [1/]

	Actual 2011-2019 [2/]	2020	2021	Projections 2022	2023	2024	2025	2026	2027
Nominal gross public debt	19.3	52.0	62.8	52.4	49.4	51.9	54.6	57.5	60.8
Public gross financing needs	10.7	14.4	10.9	1.0	10.6	11.3	10.2	9.0	12.1
Real GDP growth (in percent)	2.6	-5.1	3.4	2.9	3.0	2.6	2.2	2.1	1.6
Inflation (GDP deflator, in percent)	3.7	-5.0	15.6	22.6	4.8	4.0	6.0	5.6	5.4
Nominal GDP growth (in percent)	6.3	-9.9	19.5	26.2	7.9	6.8	8.3	7.8	7.1
Effective interest rate (in percent) [4/]	3.0	1.8	1.5	1.9	2.9	3.3	3.0	3.3	3.4

As of September 23, 2022		
Sovereign Spreads		
EMBIG (bp) 3/		n.a.
5Y CDS (bp)		n.a
Ratings	Foreign	Local
Moody's	n.a.	n.a.
S&Ps	n.a.	n.a.
Fitch	n.a.	n.a.

Contribution to Changes in Public Debt

	Actual 2011-2019	2020	2021	Projections 2022	2023	2024	2025	2026	2027	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	4.0	6.0	10.8	-10.4	-3.0	2.5	2.7	2.9	3.3	-2.0	
Identified debt-creating flows	7.0	18.6	-7.1	-21.8	8.3	4.3	2.6	2.9	3.3	-0.3	
Primary deficit	7.2	11.0	6.5	-3.1	5.2	5.1	5.3	5.3	5.4	23.2	-2.1
Primary (noninterest) revenue and grants	33.9	30.5	29.8	33.2	31.4	29.5	28.5	27.5	26.9	177.0	
Primary (noninterest) expenditure	41.1	41.5	36.4	30.1	36.7	34.6	33.8	32.8	32.2	200.2	
Automatic debt dynamics [5/]	-0.4	6.1	-7.8	-12.1	-2.4	-1.6	-2.5	-2.3	-2.0	-22.9	
Interest rate/growth differential [6/]	-0.4	6.0	-7.8	-12.1	-2.4	-1.6	-2.5	-2.3	-2.0	-22.9	
Of which: real interest rate	-0.1	3.4	-6.4	-10.6	-1.0	-0.4	-1.5	-1.2	-1.1	-15.8	
Of which: real GDP growth	-0.3	2.6	-1.5	-1.5	-1.5	-1.2	-1.0	-1.0	-0.9	-7.1	
Exchange rate depreciation [7/]	0.0	0.1	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.2	1.6	-5.9	-6.6	5.5	0.8	-0.1	-0.1	-0.1	-0.6	
FRR withdrawal (+) or accumulation (-) (negative)	2.2	6.5	-4.0	-4.7	5.7	0.9	0.0	0.0	0.0	1.9	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Deposits of public entities (- reduces financing need)	-2.0	-4.9	-1.9	-1.9	-0.1	-0.1	-0.1	-0.1	-0.1	-2.4	
Residual, including asset changes [8/]	-3.0	-12.7	17.9	11.3	-11.3	-1.8	0.0	0.0	0.0	-1.7	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

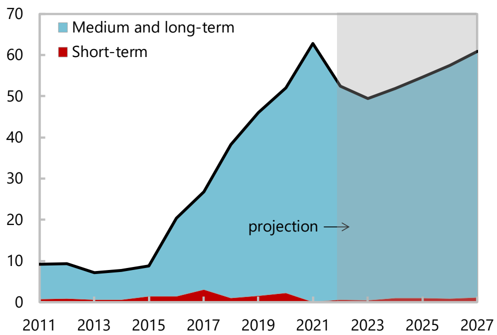
8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

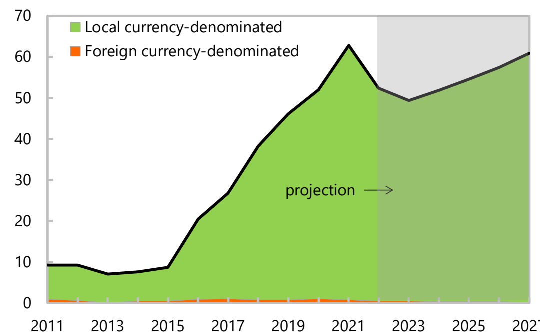
Figure 2. Algeria: Public Debt Sustainability Assessment - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

By Maturity
(in percent of GDP)



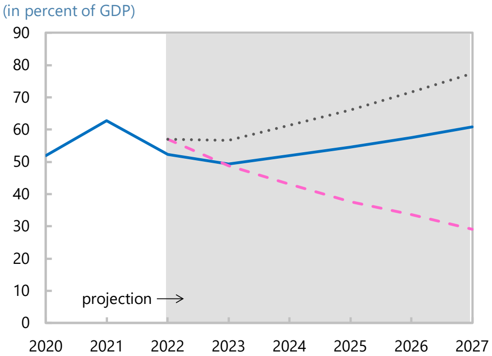
By Currency
(in percent of GDP)



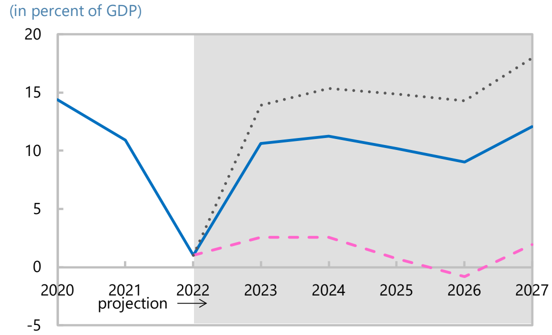
Alternative Scenarios

Baseline   Historical   Constant Primary Balance

Gross Nominal Public Debt
(in percent of GDP)



Public Gross Financing Needs
(in percent of GDP)



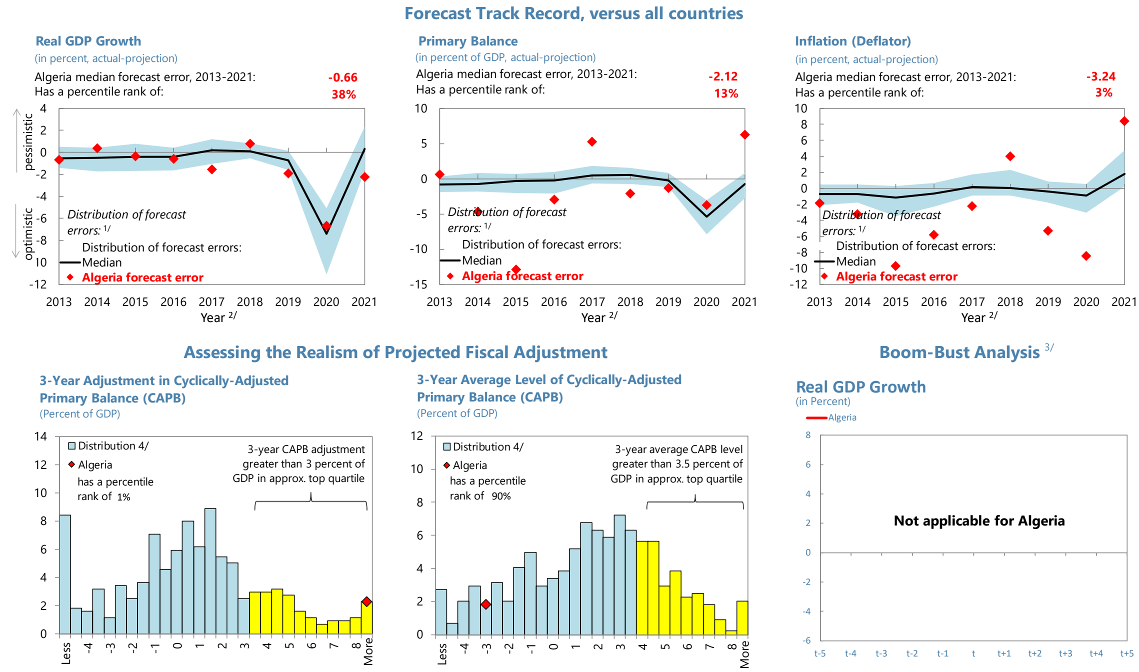
Underlying Assumptions
(in percent)

Baseline Scenario	2022	2023	2024	2025	2026	2027
Real GDP growth	2.9	3.0	2.6	2.2	2.1	1.6
Inflation	22.6	4.8	4.0	6.0	5.6	5.4
Primary Balance	3.1	-5.2	-5.1	-5.3	-5.3	-5.4
Effective interest rate	1.9	2.9	3.3	3.0	3.3	3.4
Constant Primary Balance Scenario						
Real GDP growth	2.9	3.0	2.6	2.2	2.1	1.6
Inflation	22.6	4.8	4.0	6.0	5.6	5.4
Primary Balance	3.1	3.1	3.1	3.1	3.1	3.1
Effective interest rate	1.9	3.2	3.4	2.9	3.1	3.2

Historical Scenario	2022	2023	2024	2025	2026	2027
Real GDP growth	2.9	1.9	1.9	1.9	1.9	1.9
Inflation	22.6	4.8	4.0	6.0	5.6	5.4
Primary Balance	3.1	-8.1	-8.1	-8.1	-8.1	-8.1
Effective interest rate	1.9	3.2	4.2	5.0	5.9	6.5

Source: IMF staff.

Figure 3. Algeria: Public Debt Sustainability Assessment - Realism of Baseline Assumptions



Source : IMF Staff.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

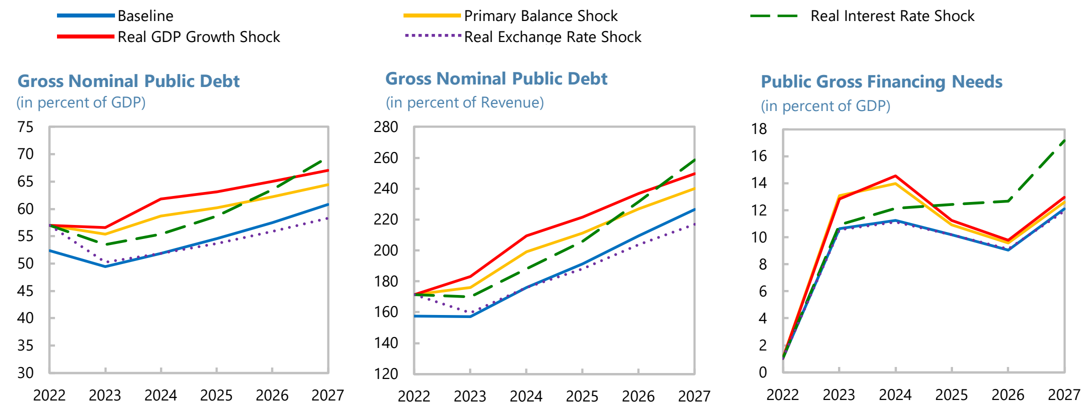
2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Algeria, as it meets neither the positive output gap criterion nor the private credit growth criterion.

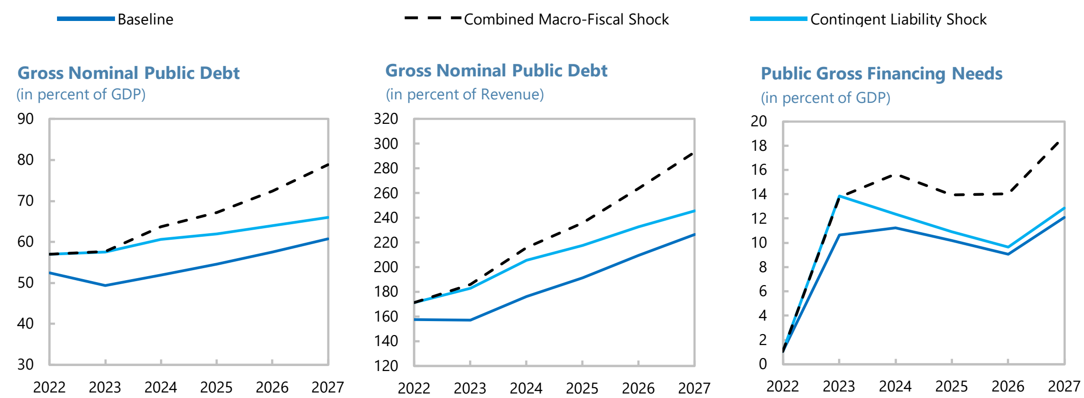
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 4. Algeria: Public Debt Sustainability Assessment – Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

Primary Balance Shock	2022	2023	2024	2025	2026	2027
Real GDP growth	2.9	3.0	2.6	2.2	2.1	1.6
Inflation	22.6	4.8	4.0	6.0	5.6	5.4
Primary balance	3.1	-7.4	-7.3	-5.3	-5.3	-5.4
Effective interest rate	1.9	3.2	3.6	3.6	3.8	3.9
Real Interest Rate Shock						
Real GDP growth	2.9	3.0	2.6	2.2	2.1	1.6
Inflation	22.6	4.8	4.0	6.0	5.6	5.4
Primary balance	3.1	-5.2	-5.1	-5.3	-5.3	-5.4
Effective interest rate	1.9	3.2	4.8	7.0	9.3	11.1
Combined Shock						
Real GDP growth	2.9	0.3	0.0	2.2	2.1	1.6
Inflation	22.6	4.1	3.4	6.0	5.6	5.4
Primary balance	3.1	-7.9	-7.5	-5.3	-5.3	-5.4
Effective interest rate	1.9	3.2	5.3	7.8	10.0	11.6

Real GDP Growth Shock	2022	2023	2024	2025	2026	2027
Real GDP growth	2.9	0.3	0.0	2.2	2.1	1.6
Inflation	22.6	4.1	3.4	6.0	5.6	5.4
Primary balance	3.1	-6.9	-7.5	-5.3	-5.3	-5.4
Effective interest rate	1.9	3.2	3.6	3.5	3.8	3.9
Real Exchange Rate Shock						
Real GDP growth	2.9	3.0	2.6	2.2	2.1	1.6
Inflation	22.6	12.5	4.0	6.0	5.6	5.4
Primary balance	3.1	-5.2	-5.1	-5.3	-5.3	-5.4
Effective interest rate	1.9	3.2	3.5	3.3	3.6	3.8
Contingent Liability Shock						
Real GDP growth	2.9	0.3	0.0	2.2	2.1	1.6
Inflation	22.6	4.1	3.4	6.0	5.6	5.4
Primary balance	3.1	-7.8	-5.1	-5.3	-5.3	-5.4
Effective interest rate	1.9	3.4	3.6	3.4	3.7	3.8

Source: IMF staff.

Figure 5. Algeria: Public Debt Sustainability Assessment

Heat Map

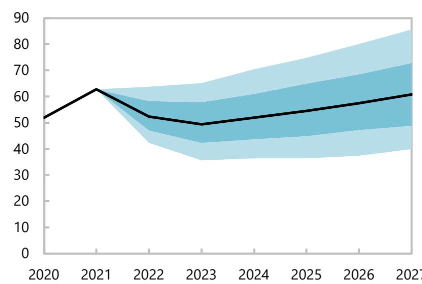
Debt level 1/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs 2/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile 3/	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

Evolution of Predictive Densities of Gross Nominal Public Debt

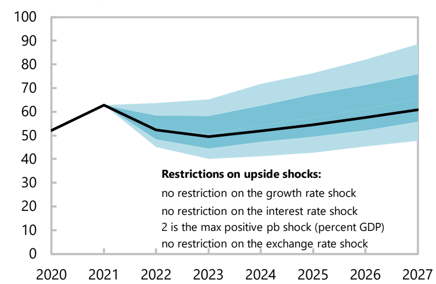
(in percent of GDP)

Baseline Percentiles: 10th-25th 25th-75th 75th-90th

Symmetric Distribution



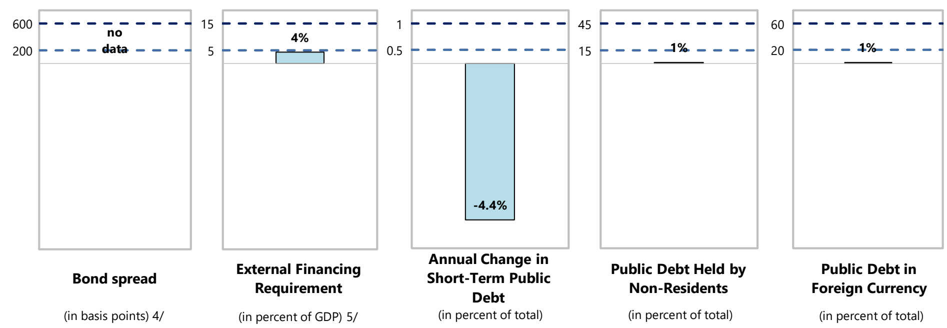
Restricted (Asymmetric) Distribution



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2021)

Algeria Lower early warning Upper early warning



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ Long-term bond spread over German bonds, an average over the last 3 months, 25-Jun-22 through 23-Sep-22.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Figure 6. Algeria: External Debt Sustainability Framework, 2017-27

(In percent of GDP, unless otherwise indicated)

	Actual								Projections						
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	**Debt-stabilizing non-interest current account 6/**
Baseline: External debt	1.4	1.8	2.4	2.3	2.3	2.2	2.4	1.9	**1.6**	**1.6**	**1.6**	**1.6**	**1.6**	**1.5**	**-0.8**
Change in external debt	-0.2	0.4	0.6	-0.1	0.0	0.0	0.1	-0.5	-0.3	0.0	0.0	0.0	0.0	0.0	
Identified external debt-creating flows (4+8+9)	3.7	17.2	15.6	12.2	9.2	9.1	12.5	2.0	-7.9	-3.5	0.6	2.3	3.6	4.1	
Current account deficit, excluding interest payments	4.4	16.4	16.5	13.1	9.6	9.8	12.8	2.8	-7.6	-2.7	1.4	3.1	4.4	4.9	
Deficit in balance of goods and services	3.7	15.4	17.3	13.2	9.0	9.2	12.3	1.6	-8.1	-2.6	2.2	3.9	5.2	5.9	
Exports	29.7	22.9	20.3	22.1	25.3	22.5	17.1	25.6	32.8	29.3	25.8	24.3	23.0	22.4	
Imports	33.4	38.4	37.6	35.3	34.3	31.6	29.5	27.2	24.6	26.7	27.9	28.1	28.2	28.3	
Net non-debt creating capital inflows (negative)	-0.7	0.4	-1.0	-0.7	-0.4	-0.8	-0.8	-0.6	-0.2	-0.8	-0.8	-0.8	-0.8	-0.8	
Automatic debt dynamics 1/	0.0	0.5	0.1	-0.1	0.0	0.1	0.4	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	
Contribution from nominal interest rate	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contribution from real GDP growth	-0.1	-0.1	-0.1	0.0	0.0	0.0	0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	
Contribution from price and exchange rate changes 2/	0.0	0.5	0.1	-0.1	0.0	0.1	0.3	-0.2	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	-3.9	-16.8	-15.0	-12.3	-9.3	-9.2	-12.3	-2.5	7.6	3.5	-0.6	-2.3	-3.7	-4.2	
External debt-to-exports ratio (in percent)	4.6	7.9	11.8	10.5	9.0	10.0	13.9	7.4	4.8	5.5	6.3	6.5	6.8	6.8	
Gross external financing need (in billions of US dollars) 4/	11.0	29.6	28.5	24.5	19.1	19.4	21.1	6.9	-12.7	-3.2	5.8	9.7	13.0	14.5	
in percent of GDP	5.1	17.9	17.8	14.4	10.9	11.3	14.5	4.2	-6.5	-1.5	2.8	4.5	5.8	6.3	
Scenario with key variables at their historical averages 5/									**1.6**	**12.8**	**19.8**	**25.0**	**28.6**	**31.6**	**0.4**
Key Macroeconomic Assumptions Underlying Baseline															
Real GDP growth (in percent)	3.8	3.7	3.2	1.4	1.2	1.0	-5.1	3.4	2.9	3.0	2.6	2.2	2.1	1.6	
GDP deflator in US dollars (change in percent)	-1.8	-25.1	-6.6	4.9	1.8	-3.1	-10.6	8.3	16.4	3.1	-0.9	0.9	0.6	0.4	
Nominal external interest rate (in percent)	1.3	4.3	0.9	1.2	1.1	1.7	0.6	0.8	0.9	1.0	0.8	0.7	0.6	0.6	
Growth of exports (US dollar terms, in percent)	-7.0	-40.1	-14.6	16.0	17.8	-13.1	-35.4	67.7	53.4	-4.9	-10.7	-2.8	-2.9	-0.7	
Growth of imports (US dollar terms, in percent)	8.6	-10.8	-5.4	-0.2	-0.1	-9.7	-20.9	3.3	8.7	15.2	6.4	3.8	2.9	2.3	
Current account balance, excluding interest payments	-4.4	-16.4	-16.5	-13.1	-9.6	-9.8	-12.8	-2.8	7.6	2.7	-1.4	-3.1	-4.4	-4.9	
Net non-debt creating capital inflows	0.7	-0.4	1.0	0.7	0.4	0.8	0.8	0.6	0.2	0.8	0.8	0.8	0.8	0.8	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

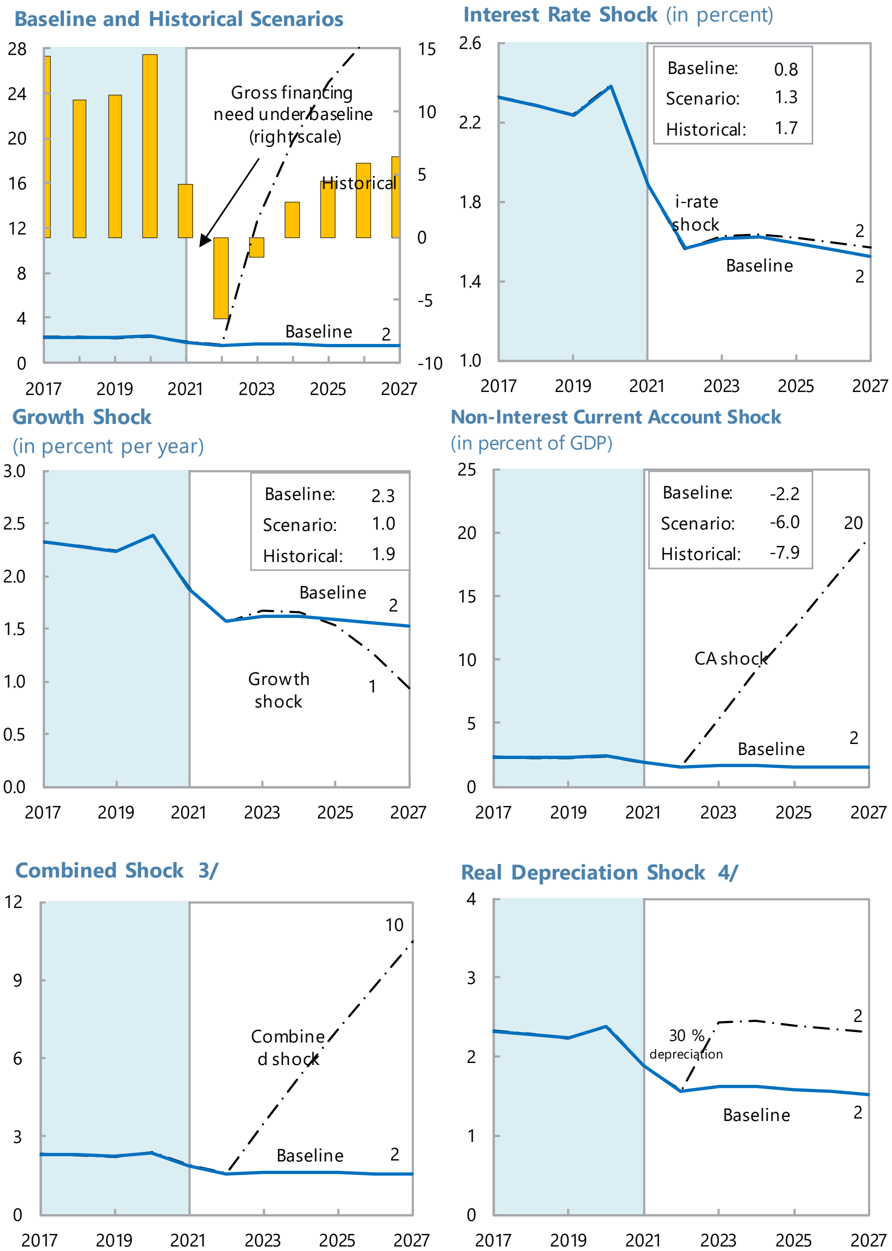
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 7. Algeria: External Debt Sustainability: Bound Tests 1/ 2/

(External Debt in Percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2022.

Annex IV. Implementation of Previous IMF Recommendations

Recommendation	Implementation Status
Macroeconomic Policy	
Adopt a medium-term fiscal consolidation strategy over 2022-26 to narrow the nonhydrocarbon primary deficit, adapting the pace of consolidation to the evolution of the pandemic and to domestic economic conditions to protect the most vulnerable.	Significant increase in spending was announced under the 2022 budget and supplementary budget. However, spending was largely under-executed, contributing, alongside a sharp rise in hydrocarbon revenue, to the achievement of a fiscal surplus. The subsidy reform was announced in the 2022 budget law and remains under preparation Progress is also being achieved on tax reforms.
Diversify budget financing sources, but exclude direct borrowing from BA	Direct monetary financing, authorized by the revision of the Central Bank law in 2017, ceased in early 2019. The special refinancing program (PSR), a one-year program instated by the BA in June 2021 to provide refinancing to public banks which had benefited from the buyback of syndicated loans to SOEs, ended in June 2022. The Algerian authorities are working on a legislative framework for public-private partnership and are receving technical assistance from the IMF's Monetary and Capital Markets (MCM) department on the development of domestic debt market.
Tighten monetary policy to consolidate gains from fiscal adjustment and contain inflationary pressures	Monetary policy has remained on hold since February 2021 and the reserve requirement ratio and policy interest rate are at their lowest level in years. Excess liquidity is sizeable.
Allow for greater flexibility of the exchange rate in the context of tighter fiscal and monetary policies to faciliate adjustment to shocks	The dinar depreciated by 10.7 percent in nominal effective terms in 2021. It subsequently appreciated by a cumulative 5.9 percent during the first nine months of 2022 amid an improvement in the terms-of-trade
Carefully monitor financial stability risks and take timely corrective action as needed	With technical assistance from the IMF's Monetary and Capital Markets Department and the Middle East Technical Assistance Center (METAC), the BA is working to strengthen its liquidity management framework (notably, short-term liquidity forecasting and Emergency Liquidity Assistance) and its regulatory and supervisory functions (review and evaluation process, developing a risk assessment methodology and risk scoring model for supervisors). The BA is also working on developing a collateral framework and has signed a technical assistance protocol with the Islamic Development Bank to enhance the regulatory and supervisory framework for Islamic Banking activities.
Reforms for Sustainable and Inclusive Growth	
Modernizing the business climate, scaling back barriers to entry and reducing red tape; opening the economy to more foreign investment and trade	The authorities are accelerating the digitalization of the economy, including to enhance taxpayer services. A new one-stop shop for investors is under preparation. The distortionary tax on professional activities is being reformed. A new investment law and attendant decrees have been published. This follows the elimination of the 51/49 rule requiring majority Algerian ownership for new businesses, except for strategic sectors (hydrocarbons, mining, defense, and pharmaceuticals manufacturing). Import regulation measures have been tightened.
Improving access to finance	A Sharia-compliant governance framework and regulations are in place and Islamic Banking services have been available in 2020.
Strengthening the Policy Framework to Increase Policy Effectiveness	
Pursue ongoing efforts to modernize budget management and improve the monitoring of fiscal risks	The authorities are working towards the implementation of the Organic Budget Law in 2023. A draft program budget and several new budget documents have been prepared.
Strengthen liquidity management to improve the effectiveness of monetary policy	The BA has worked on improving its short-term liqudity forecasting, with assistance from the IMF's Monetary and Capital Markets Department.
Reinforce the independence of the BA to protect its operations and price stability mandate	The central bank law ("Loi sur la Monnaie et le Crédit) is being revised.
Improving Governance and Reducing Vulnerabilities to Corruption	
Improve governance and reduce potential for corruption, including by increasing transparency across the public sector, strengthening oversight and control capacities and reinforcing digitalization, and enhancing the legal framework for AML/CFT	Regular reporting on fiscal operations is still very limited. Draft regulations have been prepared in the context of improving the regulatory framework for the prevention and fight against corruption. Amendments to law 06-01 on the prevention and fight against corruption are also envisaged. A new High Authority in charge of fighting corruption has been installed and an enhanced mechanisms for asset recovery was announced. A code of ethics for public agents is under preparation. The new investment law has established the principle of evenhandedness in the treatment of private investors and reinforced appeal processes. A new public procurement law and dedicated electronic portal are currently under preparation. There are ongoing efforts to accelerate digitalization. External stakeholders have been consulted in some recent legislative reforms.

Annex V. Managing Public Investment and PPPs for Growth

1. **Ensuring a growth-friendly consolidation will require continuous efforts to improve the efficiency, governance, and financing of public investment.** There is room to enhance the efficiency of capital spending. Algeria's capital spending has been continuously high, averaging 11.7 percent of GDP over the last five years, much higher than the North Africa and MENA averages of 5.7 percent and 4.3 percent respectively. Nonetheless, while Algeria displays a relatively high public capital stock, physical access and quality of infrastructure tend to be below those of the average emerging market economy (Text Figure 5).

2. **Enhancing the management of public investment projects is a key policy priority to improve efficiency.** This will help ensure that only the most productive infrastructure projects are selected for implementation, and that sufficient budget is available for their maintenance and effective operation. Public investment management reforms could help enhance efficiency, especially efforts to strengthen the appraisal and selection of investment projects, enhance the soundness of public procurement practices and develop monitoring and reporting on projects. In particular, the authorities should proceed with the adoption of their draft decree on project preparation and ensure that due attention is given by both the Ministry of Finance and line ministries to the technical and financial viability of projects. A Public Investment Management Assessment (PIMA) evaluation by the IMF's Fiscal Affairs department could help the authorities identify important reforms to improve public investment efficiency and governance.

3. **Algeria is also looking to increase its recourse to public-private partnerships (PPPs) to develop infrastructure.** PPPs are long-term service contracts where the private sector provides upfront financing, builds, operates, and maintains an asset in exchange for user fees or periodic payments by the government. They have three key characteristics: (i) private execution and financing of public investment; (ii) an emphasis on both investment and service provision by the private sector; and (iii) risk-sharing between the government and the private sector. As of 2021, according to the World Bank's Private Participation in Infrastructure (PPI) database, there are 30 active PPP projects in Algeria, for a total investment of US$ 9.2 billion. PPPs are explicitly mentioned in the 2021 Government Action Plan ("*Plan d'action du government*", PAG) as a way to develop infrastructure.

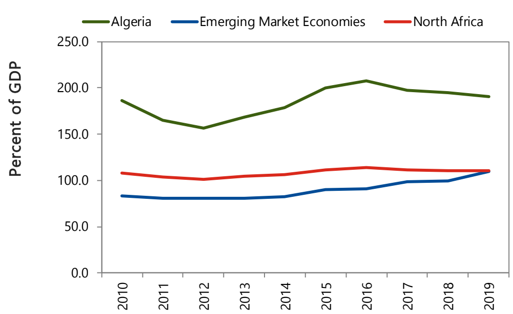
4. **Without proper governance, the risks associated with PPPs may outweigh their benefits.** Because the cost of PPPs for governments usually materializes over a long period of time, they may favor them over traditional government procurement to develop infrastructure when fiscal space is lacking in the short run. Yet, intertemporal fiscal costs of PPPs might prove higher, including in the short run. The prospect of quickly delivered infrastructure has led some governments to carry out low-priority and poorly appraised projects, which would otherwise have been excluded from their public investment plans. Without the proper skills to analyze projects and negotiate contracts, governments might have to compensate the private partners pursuant to unfavorable risk-sharing clauses. PPPs also create risks of collusion between the government and the private sector, when unsolicited bids are submitted, or when mechanisms to select the private partner and procure contracts are not transparent or competitive.

5. Strong management and oversight functions are key to avoid the materialization of fiscal risks and the creation of additional vulnerabilities to corrupt practices. The Algerian government is working on a draft law on the management of PPPs. The law should both provide a clear, fair, and predictable legal environment for the private sector, set disclosure requirements on future fiscal costs and risks, and clarify roles and responsibilities of all relevant counterparts in PPP transactions. At any point in the PPP development process, the Ministry of Finance should be able to analyze costs and fiscal risks and have the power to stop projects that are fiscally unaffordable (gateway process). [1] The authorities could also envisage ceilings on both stocks and flows of PPPs to help control fiscal risks.

Text Figure 1. Algeria: Public investment efficiency

Algeria displays relatively high levels of public capital stock relative to peers…

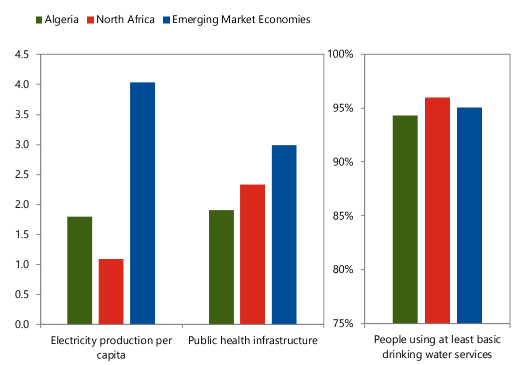
Public Capital Stock
(Percent of GDP)



Source: FAD Investment and Capital Stock Dataset.

…but physical access to infrastructure lags behind peers on average in key sectors.

Selected Indicators of Physical Access to Infrastructure



Source: World Bank Development Indicators. Left hand axis: Electricity production per capita as thousands of kWh per person; Public health infrastructure as hospital beds per 1,000 persons. Right hand axis: percentage of people using at least basic water services. This indicator encompasses both people using basic water services as well as those using safely managed water services. Basic drinking water services is defined as drinking water from an improved source, provided collection time is not more than 30 minutes for a round trip. Improved water sources include piped water, boreholes or tubewells, protected dug wells, protected springs, and packaged or delivered water.

[1] The IMF-World Bank PPP Fiscal Risk Assessment model (PFRAM) is a useful Excel-based tool to analyze government costs and risks in individual PPP projects. The Excel template and user manual can be downloaded from http://infrastructuregovern.imf.org/

Annex VI. Strengthening Monetary Policy Transmission

1. **Limited liquidity management and weak policy rate transmission are challenges to the conduct of monetary policy in Algeria.** Past recourse to monetary financing of the budget has also complicated the Bank of Algeria's (BA) role as monetary policy agent. Current excess liquidity has not been managed actively through regular liquidity-absorbing operations, thereby depriving the BA's key policy rate of an operational existence, and limiting its influence on bank funding costs. Consequently, money market rates are closer to the marginal cost of excess reserves than to the BA's key policy rate. Excess reserves at the end of August 2022 amounted to DZD 1,881 billion (more than 8 percent of banking system assets). The yield on the shortest interbank market tenors has hovered around 0.5 percent through the first nine months of 2022, well below the policy rate of 3 percent.

2. **A three-pronged strategy could improve the conduct of monetary policy:**

- **The BA's statutes should strengthen its independence and its price stability mandate**. The ongoing revision of the Law on Money and Credit is a timely opportunity in this regard. It should include a strict prohibition of monetary financing while preserving the BA's capacity to provide temporary advances to the treasury under strict conditions and limits. The Law should also strengthen the BA's governance and accountability to the Parliament. The BA's performance should be assessed based on its capacity to deliver on its price stability and financial stability mandates.

- **The BA should actively manage the banking system's liquidity to transmit its policy rate and influence bank funding and lending conditions.** To give its policy rate relevance and impact on the banking system, the BA should immediately raise its policy rate and:
    - *Increase the reserve requirement ratio and conduct regular liquidity-absorbing operations for the residual liquidity surplus.*[1] Regular liquidity-absorbing operations should be conducted at the policy rate. The calibration of the different liquidity-absorbing instruments should consider the heterogeneous distribution of excess reserves in the banking system, as well as the impact of ongoing and future PSR repayments on aggregate excess liquidity; or
    - *Maintain a symmetrical standing facilities corridor around its policy rate to effectively tighten monetary policy***.** Should the heterogeneous distribution of excess reserves across banks complicate the proposed increase in reserve requirements, the BA could increase the three policy rates, with the two standing facilities rates forming a symmetrical corridor at +/- 2 percentage points around the key policy rate. The higher remuneration of excess reserves through the deposit facility (currently at 0 percent) would be transmitted to bank deposit and lending rates, and subsequently to the economy.

[1] The BA could also consider bilateral liquidity operations with banks with significant excess reserves as a result of significant hydrocarbon export proceeds.

- **The BA should strengthen its communication on the policy rate as the instrument expressing its monetary policy stance.** Once the BA's key policy rate has regained operational and financial relevance, the BA should focus its public communication on changes to its policy rate as its main countercyclical tool to maintain price stability.