



# ALGERIA

## 2016 ARTICLE IV CONSULTATION—PRESS RELEASE AND STAFF REPORT

May 2016

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2016 Article IV consultation with Algeria, the following documents have been released and are included in this package:

- A **Press Release**.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse of time basis, following discussions that ended on March 14, 2016, with the officials of Algeria on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 29, 2016.
- An **Informational Annex** prepared by the IMF staff.

The document listed below has been or will be separately released.

Selected Issues

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## **IMF Executive Board Concludes 2016 Article IV Consultation with Algeria**

On May 16, 2016, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation<sup>1</sup> with Algeria, and considered and endorsed the staff appraisal without a meeting.<sup>2</sup>

The economic outlook has deteriorated since the 2014 Article IV consultation, with the fall in oil prices increasing the urgency to reshape Algeria's growth model. The impact of the oil price shock on growth has been limited thus far, but the fiscal and external balances have deteriorated significantly.

In 2015, real GDP grew by 3.9 percent and inflation increased to 4.8 percent. The fiscal deficit doubled to 16 percent of GDP as a result of the decrease in hydrocarbon revenues, and the fall in hydrocarbon exports by nearly half caused the current account deficit to widen sharply. Reserves, while still substantial, declined by US\$35 billion to US\$143 billion, down from a peak of US\$192 billion in 2013. External debt remains very low.

### **Executive Board Assessment**

In concluding the 2016 Article IV Consultation with Algeria, Executive Directors endorsed staff's appraisal as follows:

Algeria's economy is facing a severe and likely long-lasting external shock, calling for a vigorous policy response built on fiscal consolidation and structural reforms. The collapse in oil prices has exposed longstanding vulnerabilities in a state-led economy that is overly dependent on hydrocarbons. Thus far, the impact of the oil price shock on growth has been limited, but fiscal and external balances have deteriorated significantly. Thanks to buffers accumulated in the past, Algeria has a window of opportunity to smooth the adjustment to the

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<sup>1</sup> Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

<sup>2</sup> The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

shock and reshape its growth model. Restoring macroeconomic balances will require sustained fiscal consolidation over the medium term combined with a critical mass of structural reforms to diversify the economy, while exchange rate, monetary, and financial policies should play a supporting role. Communication to build a consensus around the needed reforms will be important to ensure their timely implementation.

Fiscal consolidation will need to be sustained over the medium term to restore fiscal sustainability, ensure intergenerational equity, and support external stability. It will require controlling current spending, pursuing further subsidy reform while protecting the poor, mobilizing more nonhydrocarbon revenues, increasing the efficiency of investment, and strengthening the budget framework. Rapidly declining fiscal savings mean that Algeria will need to borrow more to finance future deficits. In addition to increasing domestic debt issuance, the authorities should consider borrowing externally and opening the capital of some state-owned enterprises, in a transparent way, to private participation.

Wide-ranging structural reforms are needed to help support economic activity during the fiscal consolidation and to diversify the economy. Key reforms include improving the business climate, opening up the economy to more trade and investment, improving access to finance and developing capital markets, and strengthening governance, competition, and transparency. Increasing the flexibility of labor markets while better matching the skills produced by the educational system to those needed by the private sector is also needed. Import restrictions, while perhaps providing a temporary relief, introduce distortions and cannot substitute for reforms aimed at boosting exports. As structural reforms take time to bear fruit, they should be started without delay.

Together with fiscal consolidation and structural reforms, greater exchange rate flexibility would support the adjustment to the oil price shock. Despite some depreciation in 2015, the REER remains significantly overvalued. Fiscal consolidation and structural reforms, together with greater exchange rate flexibility, would help bring the REER in line with its equilibrium value and contribute to the rebalancing of the economy.

Monetary policy must adjust to a changing liquidity environment while guarding against potential inflationary pressures. The BA is appropriately adjusting to a changing liquidity environment by reactivating its lending instruments and strengthening its liquidity forecast and management capacity. Going forward, it should carefully calibrate monetary policy to guard against potential inflationary pressures.

Financial sector policies should be further strengthened to address growing financial stability risks. The banking sector as a whole is well capitalized and profitable, but protracted low oil prices increase financial stability risks. Moreover, the strong links between the financial, hydrocarbon, and public sectors increase the vulnerability of banks to systemic risks and call for preemptive actions. The authorities should continue their efforts to strengthen the

prudential framework, including by enhancing the role of macroprudential policy, and improving crisis preparedness and management.

## Algeria: Selected Macroeconomic Indicators, 2013–17

Population: 39.5 million; 2014  
 Quota (old): SDR 1,254.7 million  
 Key export markets: EU  
 Main exports: oil and gas

Per capita GDP: US\$ 4,318 (2015)  
 Gini coefficient: 0.31 (2011)

	2013	2014	2015 Est.	2016	2017
<b>Output</b>					
Real GDP growth (percent)	2.8	3.8	3.9	3.4	2.9
Nonhydrocarbon GDP growth (percent)	7.1	5.6	5.5	3.7	3.1
<b>Employment</b>					
Unemployment (percent, end of period)	9.8	10.6	11.2	...	...
<b>Prices</b>					
Inflation (percent, average)	3.3	2.9	4.8	4.3	4.0
<b>Central government finances (percent of GDP)</b>					
Total revenue	35.8	33.4	30.1	26.8	28.0
<i>Of which, hydrocarbon</i>	22.1	19.7	14.1	10.2	11.2
Total expenditure	36.7	41.3	46.5	42.4	40.2
Overall budget balance (deficit-)	-0.9	-8.0	-16.4	-15.6	-12.2
Gross government debt	7.7	8.0	9.0	15.4	25.4
<b>Money and credit</b>					
Broad money (percent change)	8.4	14.4	0.5	1.1	10.0
Credit to the economy (percent change)	19.9	25.7	16.1	9.0	10.0
<b>Balance of payments</b>					
Current account balance (percent of GDP)	0.4	-4.4	-16.2	-17.9	-17.0
FDI (percent of GDP)	0.9	0.7	-0.4	0.9	1.1
Gross reserves (months of imports) 1/	32.3	33.5	29.8	22.1	18.9
External debt (percent GDP)	1.6	1.7	1.8	2.8	4.9
<b>Exchange rate</b>					
REER (percent change)	-1.4	2.1	-4.3	-1.6	-3.2

Sources: Algerian authorities; and IMF staff estimates.

1/ In months of next year's imports of goods and services.



# ALGERIA

## STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION

April 29, 2016

### KEY ISSUES

**Context.** The oil price shock has hit Algeria's economy hard and exposed the longstanding vulnerabilities of a growth model dependent on hydrocarbon and public spending. The fiscal position—already weakened by a ramp-up in spending in the wake of the Arab Spring—has deteriorated further as oil revenues plummeted. Once-substantial fiscal savings have been nearly depleted to finance large budget deficits. Following several years of comfortable surpluses, the current account balance has swung sharply into deficit and official reserves, while still large, are diminishing. The banking system as a whole appears healthy, but financial stability risks are increasing. The policy response in 2015 was insufficient, but the 2016 budget calls for a sharp reduction in spending, and the authorities have initiated some reforms, including a much needed reform of the subsidy system.

**Outlook and risks.** The outlook will crucially depend on the appropriateness of the policy response to the oil price shock. The impact on economic activity has been limited thus far, with fiscal policy remaining expansionary through 2015, but growth is expected to slow because of the needed fiscal consolidation. Medium-term financing needs will remain large and require increased recourse to borrowing. External risks remain important, and concerns about social stability, in a volatile regional context, could slow the pace of reforms.

**Policy recommendations.** The magnitude and expected persistence of the oil price shock require a vigorous policy response to restore macroeconomic balances and foster sustainable growth and jobs creation. To ensure fiscal sustainability, address external imbalances, and promote intergenerational equity, the government needs to achieve a durable and ambitious fiscal consolidation over the medium term. Deep structural reforms are necessary to offset the impact of fiscal consolidation on growth, improve medium-term prospects, and facilitate a much-needed diversification to reduce the dependence on oil. These efforts would help bring the real effective exchange rate in line with fundamentals and should be accompanied by greater exchange rate flexibility, a carefully calibrated monetary policy that guards against inflation, and policies to mitigate risks in the banking system. Thanks to buffers accumulated in the past, Algeria has a window of opportunity to smooth the adjustment to the oil price shock and reshape its growth model. This opportunity needs to be seized swiftly to avoid a more drastic adjustment down the road.

Approved By  
**Daniela Gressani and  
 Catherine Pattillo**

The discussions took place in Algiers from March 1-14. The staff team comprised Mr. Dauphin (head), Mr. Jewell, Mr. Souissi, and Mr. Tabarraei (all MCD). Mr. Auclair and Ms. Kebet (all MCD) assisted in the preparation of this report.

The team met with the Governor of the Bank of Algeria, Mohammed Laksaci; Finance Minister Abderrahmane Benkhalfa; Industry and Mines Minister Abdessalem Bouchouareb; Trade Minister Bakhti Belaib; Agriculture and Rural Development Minister Sid Ahmed Ferroukhi; Labor, Employment, and Social Security Minister Mohamed El Ghazi; and Minister Delegate of the Budget Hadji Baba Ammi. The mission also held discussions with other senior government and central bank officials as well as with representatives of the economic and financial sectors and civil society. Mr. Badsı (OED) participated in most of the meetings.

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## INTRODUCTION

### 1. **The collapse in oil prices points to the urgent need to reshape Algeria's growth model.**

Following a devastating civil war in the 1990s, Algeria experienced over a decade of relatively steady growth and social stability. Thanks to rapidly increasing oil prices, it was able to accumulate large fiscal savings and international reserves while paying off most of its debt. However, Algeria did not take advantage of over a decade of high oil prices to overcome the structural shortcomings in its growth model, as the economy remained overly dependent on hydrocarbons and public spending. From 2002 (when oil prices started to rise) until 2014 (when they started to fall), hydrocarbons on average accounted for 98 percent of exports, 69 percent of fiscal revenues, and 36 percent of GDP. Government spending swelled as the authorities granted wage increases and provided employment, social housing, and subsidies—most recently in the wake of the Arab Spring. Furthermore, the public sector remains a dominant actor in the economy through many and often large public enterprises, including in the energy and banking sectors. Indeed, public banks account for 87 percent of total banking assets. With the fall in oil prices, Algeria needs to confront an old challenge with new urgency: how to diversify the economy away from hydrocarbons and find new sources of growth that will create jobs for a youthful and fast-growing population.

## RECENT DEVELOPMENTS, OUTLOOK, AND RISKS

### A. Recent Developments

2. **Growth was sustained in 2015 while inflation picked up.** After a decade of contraction, hydrocarbon production increased slightly last year (0.4 percent), while nonhydrocarbon growth was steady. Overall growth edged higher from 3.8 percent to 3.9 percent. Average inflation exceeded the central objective of the Bank of Algeria (BA), likely driven by supply effects and the depreciation of the dinar (Box 1). The unemployment rate increased from 10.6 percent in September 2014 to 11.2 percent in September 2015. It remains particularly high among the youth (29.9 percent) and women (16.6 percent).

3. **The budget deficit reached a record high in 2015 due to the collapse in hydrocarbon revenues and a significant fiscal expansion.** The overall budget deficit reached an all-time high of 16.4 percent of GDP. Lower oil prices translated into a 30 percent decline in hydrocarbon revenues, while spending grew by 10.2 percent, driven by a surge in capital spending. The deficit was mainly financed by drawings from the *Fonds de Régulation des Recettes* (FRR), Algeria's oil saving fund, which declined to 12.3 percent of GDP from 25.6 percent in 2014.

4. **The current account deficit also widened significantly, but foreign reserves remained at comfortable levels.** The current account deficit widened to 16.2 percent of GDP in 2015 from 4.4 percent in 2014, as hydrocarbon exports fell almost by half. Gross inflows of foreign direct investment remained weak at 1 percent of GDP. Foreign exchange reserves declined by nearly US\$35 billion but remain substantial, equal to 2½ years of imports or 833 percent of the Fund's

metric to assess reserve adequacy (ARA metric). External debt stood at 1.8 percent of GDP at end-2015.

**5. The real effective exchange rate depreciated but remains significantly overvalued.**

Despite a 25 percent depreciation of the dinar against the dollar, the nominal effective exchange rate depreciated by only 6.7 percent in 2015, owing to the depreciation of other trading partners' currencies. The real effective exchange rate (REER) depreciated by 4.3 percent, as the nominal depreciation was partly offset by an increase in Algeria's prices relative to those in its trading partners. The REER remains significantly overvalued, hurting Algeria's competitiveness (Annex III).

**6. Broad money growth slowed, driven by a decline in net foreign assets.** Credit to the economy expanded by 16.1 percent in 2015. However, broad money growth slowed sharply to 0.5 percent from 14.4 percent in 2014, largely due to the decline in net foreign assets, and despite liquidity injections resulting from the government's drawdown of the FRR to finance the fiscal deficit. Bank deposits declined, partly due to the government's purchase of a majority stake in a major telecom company.

**7. On aggregate, the banking sector remained well capitalized and profitable, but liquidity tightened.** According to preliminary figures, the overall capital-adequacy ratio was 17 percent at end-2015 compared to 16 percent in 2014. Bank profitability improved in 2015, with an aggregate return on assets of 2.2 percent. The ratio of gross non-performing loans (NPL) to total loans, which had been on a declining trend thanks in part to growth in credit, edged higher to around 9.5 percent at end-2015. However, the net NPL ratio was 3.6 percent owing to high provisioning levels (around 61 percent on aggregate). Liquidity in the banking system contracted sharply due to the impact of lower oil prices on bank deposits and to rapid growth in credit to the public sector (partly used to finance imports). On aggregate, 27 percent of bank assets were liquid at end-2015 (compared to 38 percent at end-2014), sufficient to cover almost two-thirds of their short-term liabilities.

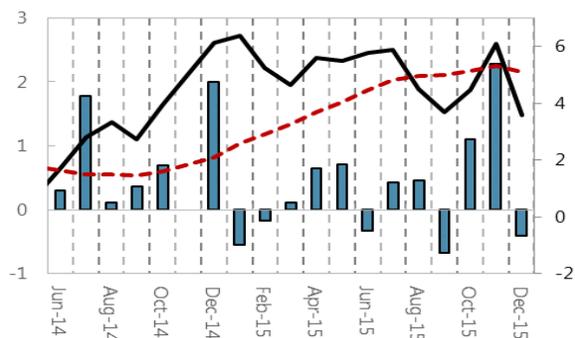
**8. A new constitution includes provisions to foster greater transparency, better governance, and a more market-based economy.** The new constitution, adopted in February 2016, makes a number of changes aimed at strengthening democracy and promoting a more market-based economy. Achieving a diversified economy and fighting corruption become explicit objectives. Freedom of trade and investment is recognized, and the government is to "strive to improve the business climate." Monopolies and unfair competition are prohibited. On the political side, the constitution re-introduces two-term limits on the presidency (lifted in 2008).

### Box 1. Algeria: Inflation Developments in 2015

Headline inflation stood at 4.8 percent on average at end-2015. Year-on-year inflation accelerated in the second quarter, largely driven by higher food prices (including regulated food prices) and products with high import content. However, during the second half of the year, year-on-year food inflation was more volatile and slowed sharply toward the end of the year, while year-on-year imported goods inflation accelerated. Overall, the effects of the depreciation of the dinar on imported prices, likely combined with some market failure effects (related to inadequate market infrastructure and the presence of oligopolies), kept average headline inflation above the central bank’s 4 percent central target.

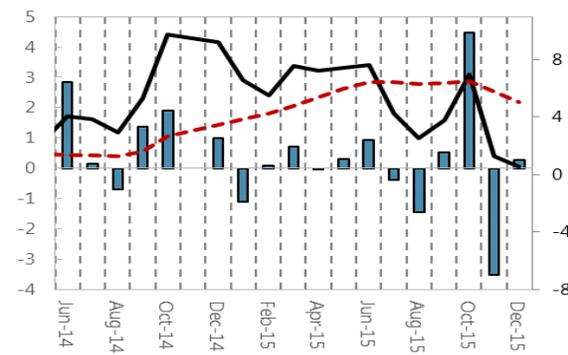
#### Headline Inflation

(Seasonally adjusted)



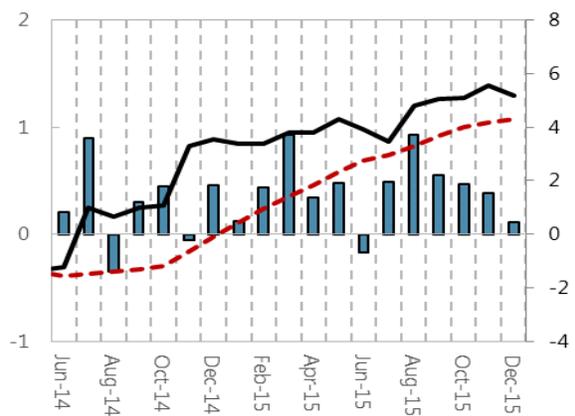
#### Food Price Index

(Seasonally adjusted, weight: 43.1 percent)



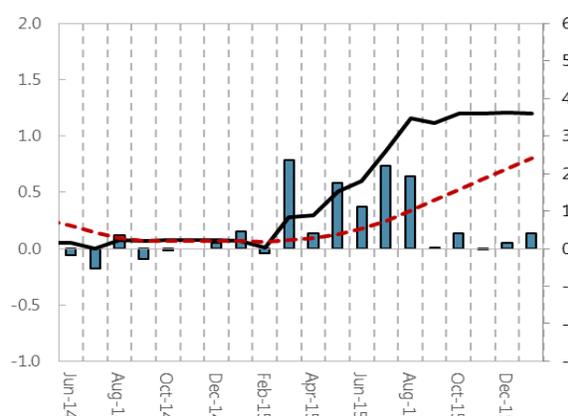
#### Import Price Index

(Seasonally adjusted, weight: 26.1 percent)



#### Administered Food Price Index

(Seasonally adjusted, weight: 12.5 percent)



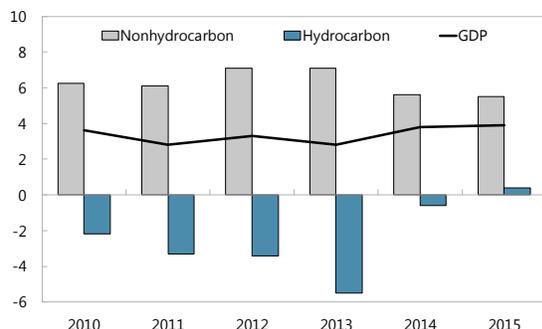
■ m-o-m (LHS)    — y-o-y (RHS)    - - - 12m moving average (RHS)

Sources: Algerian authorities; and IMF staff calculations.

**Figure 1. Algeria: Selected Macroeconomic Indicators**

The hydrocarbon sector rebounded as new fields came on stream, while nonhydrocarbon growth was steady.

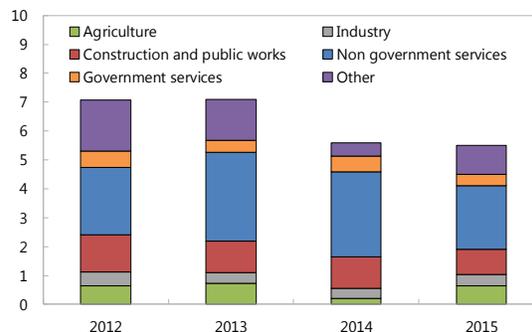
**Hydrocarbon and Nonhydrocarbon Growth**  
(Percent)



Sources: Algerian authorities; and IMF staff calculations.

Stronger growth in the agricultural sector helped offset weaker activity in the construction and services sectors.

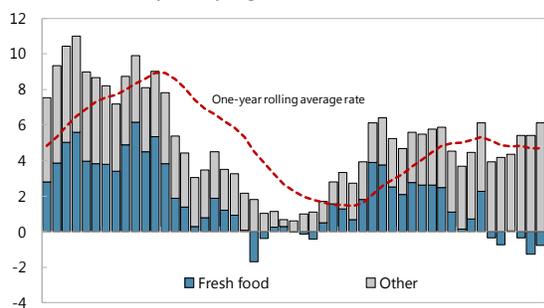
**Sources of Nonhydrocarbon Growth**  
(In percent)



Sources: Algerian authorities; and IMF staff calculations.

Inflation picked up in 2015, mainly driven by non-food items during the second half of the year.

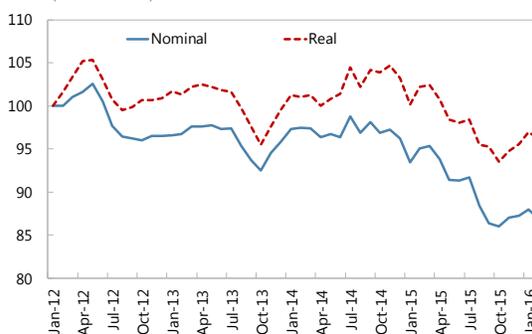
**CPI Inflation**  
(Contribution to year-on-year growth rate)



Sources: Algerian authorities; and IMF staff calculations.

Both the nominal and real effective exchange rates weakened for most of 2015.

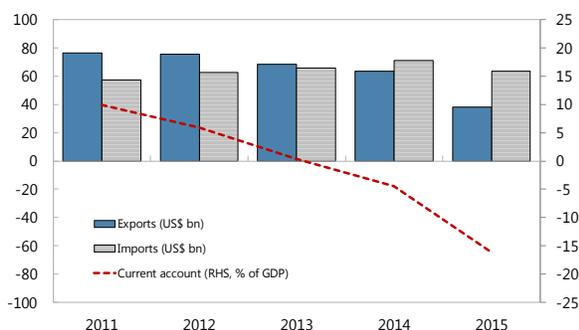
**Effective Exchange Rate**  
(Jan 2012=100)



Source: Algerian authorities; and IMF staff calculations.

The current account balance continued to deteriorate as hydrocarbon exports fell.

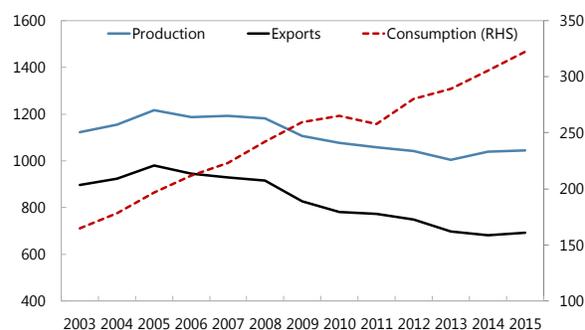
**Current Account**



Sources: Algerian authorities; and IMF staff calculations.

Domestic hydrocarbon consumption continued to grow rapidly, weighing on exports.

**Hydrocarbon Production, Consumption, and Exports**  
(Millions of barrels)



Source: Algerian authorities; and IMF staff calculations.

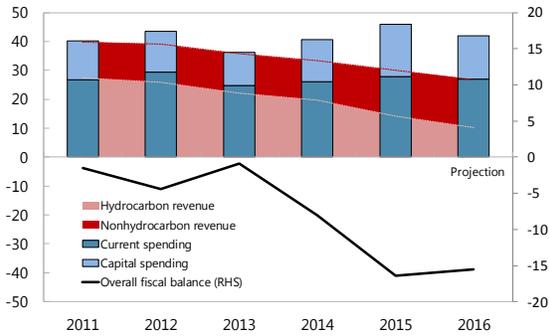
**Figure 2. Algeria: Fiscal Indicators**

Despite large spending cuts, the fiscal deficit is projected to improve only marginally in 2016 as hydrocarbon revenues fall.

The nonhydrocarbon deficit, however, is projected to narrow significantly in 2016.

**Overall Fiscal Balance**

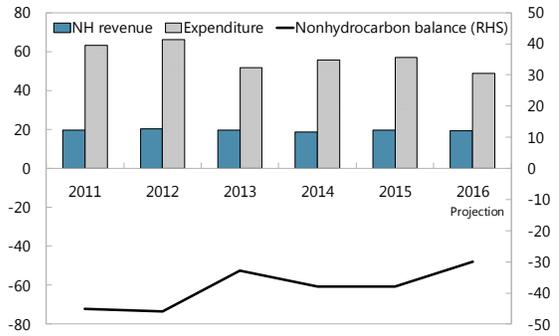
(In percent of GDP, 2011–16)



Sources: Algerian authorities; and IMF staff calculations.

**Nonhydrocarbon Fiscal Balance**

(In percent of NHGDP)



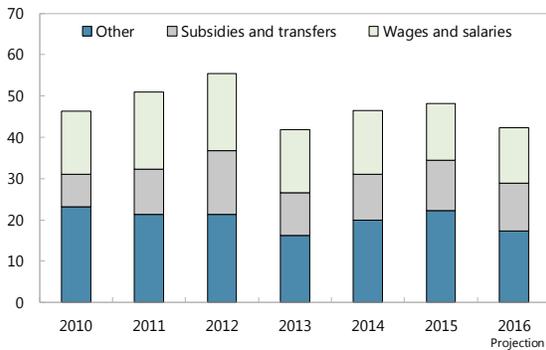
Sources: Algerian authorities; and IMF staff calculations.

Current spending as percent of GDP is expected to decline...

... financed increasingly by nonhydrocarbon revenues.

**Current Spending**

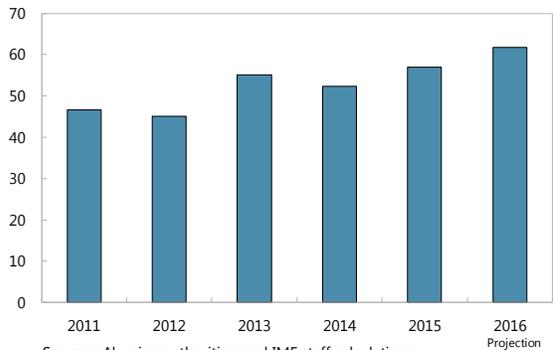
(Percent of nonhydrocarbon GDP)



Sources: Algerian authorities; and IMF staff calculations.

**Share of Nonhydrocarbon Revenue to Current Spending**

(Percent)



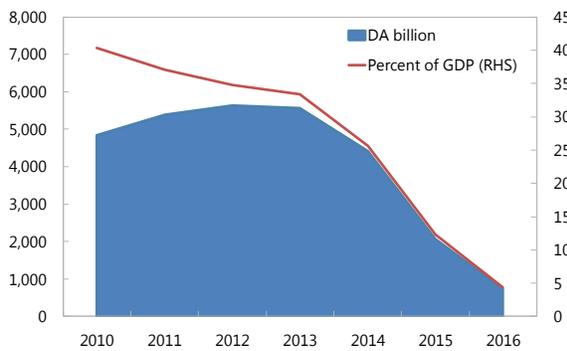
Sources: Algerian authorities; and IMF staff calculations.

The oil savings fund is expected to reach its statutory floor this year.

The breakeven oil price is expected to decline in 2016, driven by a narrowing of the nonhydrocarbon deficit.

**Oil Fund**

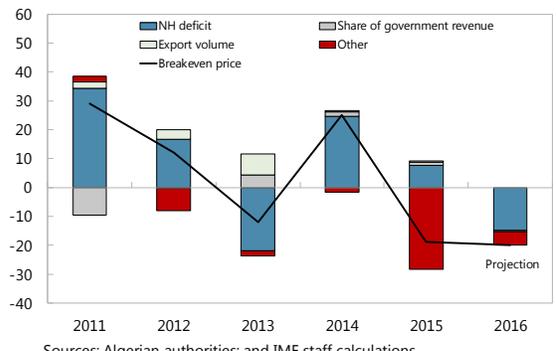
(Stock)



Sources: Algerian authorities; and IMF staff calculations.

**Change in the Fiscal Breakeven Price**

(Contribution in percent)



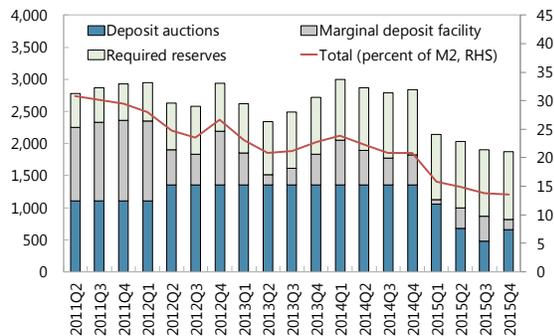
Sources: Algerian authorities; and IMF staff calculations.

**Figure 3. Algeria: Monetary Indicators**

The BA continued to mop up excess liquidity in 2015 but at a slower pace, reflecting tighter liquidity conditions.

**Liquidity Management**

(Liquidity management in DZD bn and in percent of M2)

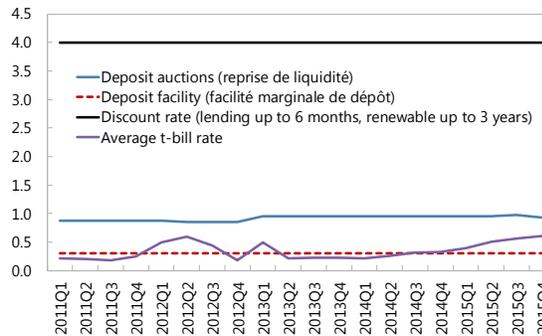


Sources: Algerian authorities; and IMF staff calculations.

Government bond yields entered into the BA's interest rate corridor amid tighter liquidity conditions.

**Interest Rates**

(In percent)

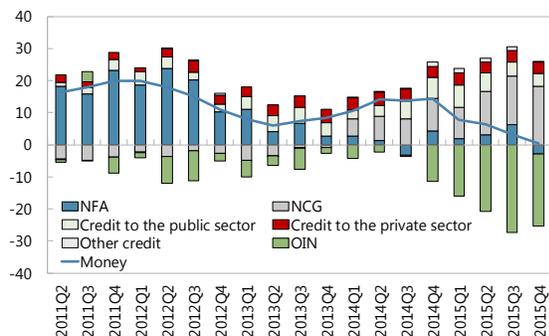


Sources: Algerian authorities; and IMF staff calculations.

A decline in net foreign assets contributed to a sharp deceleration in broad money growth.

**Contribution to M2 Growth**

(In percent)

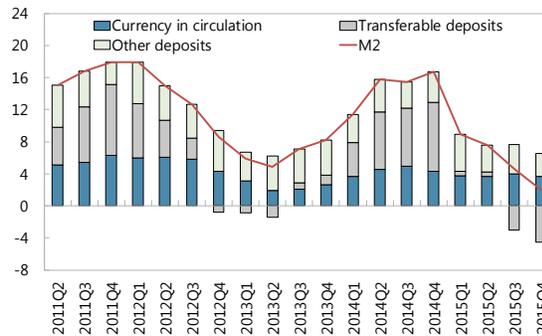


Sources: Algerian authorities; and IMF staff calculations.

Bank deposits declined, partly due to the government's purchase of a majority stake in a telecom company.

**M2 Growth and Determinants**

(In percent)

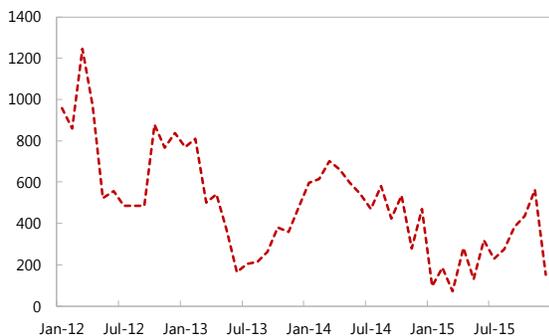


Sources: Algerian authorities; and IMF staff calculations.

The collapse in oil prices led to a decline in excess liquidity.

**Excess Liquidity**

(Billions of dinars)

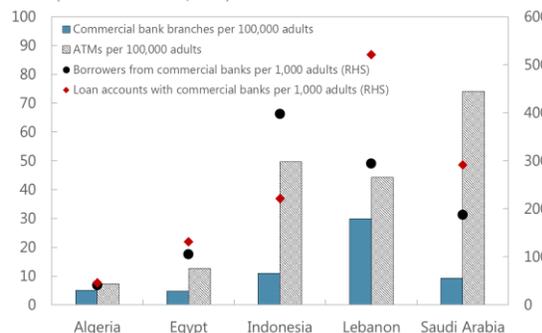


Sources: Algerian authorities.

Financial services remain underdeveloped.

**Financial Access Survey**

(Selected indicators, 2014)



Sources: 2015 IMF Financial Access Survey.

## B. Outlook and Risks

**9. Hydrocarbon growth is expected to increase in 2016, but fiscal consolidation will weigh on nonhydrocarbon growth.** Hydrocarbon growth is expected to accelerate to close to 2 percent as new fields come on stream and a key gas facility that closed after a terrorist attack in 2013 resumes full production. However, fiscal consolidation should weigh on nonhydrocarbon growth, which is expected to slow to 3.7 percent. Headline inflation will likely remain higher than 4 percent, driven by further dinar depreciation and increases in administered energy prices. The spending cut envisaged in the 2016 budget, combined with higher tax revenues, is projected to reduce the nonhydrocarbon deficit to 29.9 percent of nonhydrocarbon GDP from 37.8 percent in 2015. The current account deficit should widen further as oil prices continue to fall, and reserves are projected to fall to 712 percent of the ARA metric. Broad money growth should remain low due to a continued decline in net foreign assets compensated in part by increased domestic debt issuance by the government.

**10. Beyond 2016, the outlook hinges on the strength of the policy response to the oil price shock.** Over the medium term, Algeria's macroeconomic prospects will depend on the size and pace of fiscal consolidation, the extent of structural reforms, and the appropriateness of other policies. Staff developed three scenarios to illustrate the possible outcomes under different policy responses and highlight the policy trade-offs at play (Annex I). All scenarios factor the fiscal adjustment embedded in the 2016 budget.

- *The baseline scenario represents the minimum effort necessary to preserve macroeconomic stability over the medium term (Tables 1-4).* It assumes a gradual fiscal adjustment beyond 2016, some structural reforms, and some further real exchange rate depreciation. Under this scenario, the nonhydrocarbon deficit is projected to decline to 22.3 percent of nonhydrocarbon GDP in 2021. Nonhydrocarbon growth initially slows under the effects of fiscal consolidation but eventually accelerates as structural reforms start bearing fruit. Debt increases rapidly given large financing needs and limited remaining savings in the FRR. The current account deficit narrows as oil prices recover (as in all scenarios) and fiscal consolidation dampens import demand. Foreign exchange reserves continue to fall but remain at comfortable levels.
- *A more ambitious reform scenario would further reduce fiscal and external vulnerabilities and increase growth potential.* This scenario assumes greater fiscal consolidation through greater efforts to contain the wage bill, more efficient public investment and deeper subsidy reform, a more significant mass of structural reforms, and larger real exchange rate depreciation. This stronger policy package leads to lower debt accumulation, higher reserves, and, ultimately, faster growth.
- *By contrast, under an illustrative no-policy-change scenario, the fiscal and external positions would quickly deteriorate.* Significant government borrowing would lead to rapidly increasing debt levels and crowd out private investment, contributing to slower nonhydrocarbon growth and continued high unemployment.

**Text Table 1. Key Macroeconomic Indicators under Alternative Scenarios**

	2015	2021		
		Baseline	No policy change	Ambitious reforms
Overall growth	3.9	3.4	2.3	3.9
Nonhydrocarbon growth (percent)	5.5	3.6	2.2	4.1
International reserves (months of imports)	29.8	8.6	5.5	19.9
Net fiscal saving (percent of GDP)	3.3	-40.4	-62.1	-31.9

**11. Risks are tilted to the downside** (Box 2). A further prolonged decline in oil prices (which could result from lower-than-expected global growth) would worsen economic imbalances and increase financial strains. Algeria, however, is insulated from world financial market turbulence given existing capital account restrictions. Domestically, difficulties garnering a political and social consensus, particularly in a volatile regional context, could complicate the implementation of necessary reforms and ultimately lead to a more abrupt adjustment.

### Box 2. Algeria: Risk Assessment Matrix

Source of Risks	Relative Likelihood	Expected Impact	Source of impact	Policy response
<b>Persistently lower energy prices</b> , triggered by supply factors reversing only gradually.	High	High	Lower oil and gas prices would worsen the current account and fiscal deficits, given Algeria's strong dependence on hydrocarbon exports.	Wide-ranging structural reforms are needed to diversify the economy away from hydrocarbons. A fiscal rule, with a credible enforcement mechanism, would help shield the country from shocks arising from the hydrocarbon sector.
<b>Sharper-than-expected global growth slowdown</b>				
Significant slowdown in other large EMs/frontier economies.	Medium	High	A sharper-than-expected slowdown in global growth would negatively affect Algeria through lower oil prices. Slower growth in Europe in particular could negatively affect demand for Algeria's gas exports. Weaker demand for nonhydrocarbon exports would have little impact on the balance of payments, as nonhydrocarbon exports represent a small fraction of total exports. Financial market spillovers would be limited given Algeria's very limited financial integration with the rest of the world.	Wide-ranging structural reforms are needed to diversify the economy away from hydrocarbons. A fiscal rule, with a credible enforcement mechanism, would help shield the country from shocks arising from the hydrocarbon sector.
Structurally weak growth in key advanced and emerging economies.	High/ Medium	High		
<b>Dislocation in capital and labor flows</b>				
Heightened risk of fragmentation/security dislocation in part of the Middle East, Africa, and Europe, leading to a sharp rise in migrant flows, with negative global spillovers.	High	Medium/ High	Heightened security concerns may benefit Algeria to the extent that they lead to higher oil prices. However, regional instability would increase pressure on the government to maintain security and social spending, thus delaying fiscal consolidation. Low trade and financial flows with the region limit the potential for direct impacts.	The authorities should mount an effective communications campaign that raises awareness about the benefits of reforms and the cost of inaction. A targeted cash-transfer system would mitigate the impact of subsidy reform on the poor.
<b>Algeria-specific risks</b>				
Difficulties garnering a political and social consensus around necessary reforms, particularly in a volatile regional context	Medium	High	A slower pace of structural reforms and fiscal consolidation could jeopardize the needed fiscal and external rebalancing and could ultimately lead to a more abrupt adjustment.	The authorities should mount an effective communications campaign that raises awareness about the benefits of reforms and the cost of inaction. A targeted cash-transfer system would mitigate the impact of subsidy reform on the poor.

<sup>1</sup> The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). 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. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

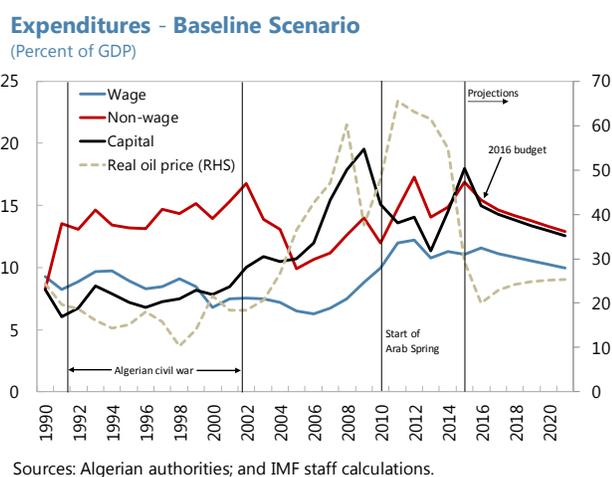
## POLICY DISCUSSIONS

**12. The discussion focused on the policy response to the oil price shock, given short and medium-term objectives.** Addressing the large external shock will involve difficult choices. On the one hand, the authorities must restore fiscal sustainability, reduce external vulnerabilities, contain inflation, and preserve financial stability. On the other hand, they need to reduce the economy's dependence on oil, boost medium-term growth potential and create jobs, and maintain social stability and cohesiveness. The consultation explored the policy choices that these multiple objectives involve, in a difficult external environment.<sup>1</sup>

**13. The mission argued that the magnitude and durability of the external shock call for a vigorous policy response built on fiscal consolidation and structural reforms.** Algeria, whose fiscal policy was already unsustainable when oil prices were high, needs to undertake ambitious and sustained consolidation combined with a critical mass of structural reforms to diversify its economy and promote private sector-led growth and job creation. Greater exchange rate flexibility should support these efforts, while monetary policy should guard against inflationary pressures and financial policies need to address rising risks in the financial sector. Existing buffers allow for an orderly adjustment, but action should start now on many fronts, as reforms will take time to bear fruit while buffers will continue to erode. The authorities agreed with the broad strategy laid out by the mission but occasionally differed on its specific translation into concrete actions. They are also concerned about how fast the adjustment can be implemented. Staff remains ready to support the authorities' efforts through close dialogue on policy options and technical assistance.

### A. Pursuing Fiscal Consolidation

**14. The 2016 budget is ambitious and should be followed by sustained consolidation efforts over the medium term.** The 2016 budget marks an important step toward fiscal consolidation. Staff stressed that additional consolidation efforts will be needed over many years to ensure medium-term debt sustainability and help support the external rebalancing (Annex II).<sup>2</sup> Since fiscal consolidation will unavoidably have a negative impact on growth, it should rely primarily on fiscal



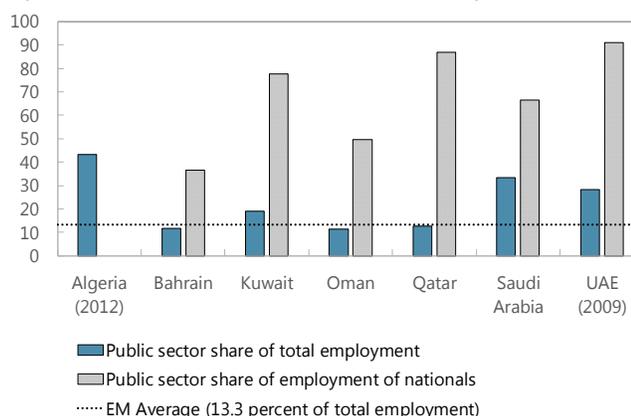
<sup>1</sup> See accompanying Selected Issues Paper: "A Structural Model for Algeria."

<sup>2</sup> While the consolidation assumed in the baseline scenario would ensure debt sustainability, it would not be enough to ensure intergenerational equity. The permanent income hypothesis (PIH) rule suggests that a nonhydrocarbon primary deficit equal to 5.6 percent on a permanent basis would ensure adequate savings for future generations.

levers that have the smallest multipliers and be accompanied by ambitious structural reforms. It should also be implemented as part of a clear medium-term strategy that establishes the appropriate pace of consolidation toward a well-defined medium-term objective taking into consideration the time necessary to implement various reforms. The more-wide ranging the structural reforms are, the more ambitious the fiscal objective can be (as illustrated in staff's ambitious scenario). At a minimum, to ensure medium-term stability, the authorities should consider a fiscal consolidation path in line with staff's baseline scenario. The authorities agreed that further fiscal consolidation was necessary beyond 2016 while stressing the importance of mitigating the impact on growth and employment.

**15. The wage bill needs to be contained.** Spending on wages and salaries has nearly doubled since 2006 (as a percent of GDP), as the government hired more workers, increased salaries, and granted back payments to maintain social stability. Staff supported the authorities' decision to maintain the freeze in public sector hiring announced last year (with some limited exceptions). Staff argued that fiscal consolidation should entail over the medium term a gradual reduction in the wage bill, as a percent of GDP, to levels that prevailed before 2011. This can be achieved by reducing the size of the civil service (a civil service review could help identify nonessential positions) and by anchoring wage growth to productivity improvements.<sup>3</sup> The latter would contribute not only to reducing the budget deficit but also to improving the quality of public services. The authorities agreed that current expenditure should be curtailed, including by containing growth in the wage bill.

**Public Sector Employment**  
(Share of total, 2014 or latest data available)



**16. Implicit and explicit subsidies should be gradually phased out and a well-targeted cash transfer system should be introduced to protect vulnerable consumers.**<sup>4</sup> Subsidies cost an estimated 13.6 percent of GDP in 2015, with energy subsidies accounting for over half this amount. In addition to their fiscal cost, subsidies are mostly regressive. For example, households in the richest quintile spend, on average, six times

**Subsidies, 2015**

	DA billions	Percent of GDP
Explicit	926	5.5
Housing	357	2.1
Education	109	0.7
Food	225	1.3
Electricity, natural gas, water	74	0.4
Interest rates	160	1.0
Implicit	1,367	8.1
Housing (2013 estimate)	67	0.4
Energy (fuel, natural gas, electricity)	1,300	7.7
<b>Total</b>	<b>2,293</b>	<b>13.6</b>

Sources: Algerian authorities; and IMF staff estimates.

<sup>3</sup> Algeria has the highest ratio of employees working in the public sector of any country in the region for which data is available. See 2014 Selected Issues Paper: "[Meeting Algeria's Fiscal Challenges](#)."

<sup>4</sup> See accompanying Selected Issues Paper: "Subsidy Reform in Algeria."

more on subsidized fuel products than households in the poorest quintile. Subsidies have also led to increased domestic energy consumption, squeezing exports. The increase in fuel and electricity taxes contained in the 2016 budget is an important first step toward subsidy reform, but much more needs to be done.<sup>5</sup> Staff urged the authorities to pursue comprehensive subsidy reform over time, starting with the most regressive and expensive subsidies. Subsidy reform should entail raising energy prices further, adopting a rule-based mechanism for setting energy prices, and gradually removing other subsidies. Concurrently, the government should put in place a well-targeted cash transfer program for the poor, building on existing infrastructure. The authorities agreed with the need to deepen subsidy reform and are considering options to both phase out subsidies and introduce a cash transfer system.

### Box 3. Algeria: Main Recommendations on Subsidy Reform

- **Carefully prepare the reform and implement it gradually.** Both explicit and implicit subsidies should be gradually phased out. Price increases should be spread over time. A well-prepared reform increases the chances of success.
- **Put in place a targeted cash transfer program.** The government should gradually move from the current system of subsidies on goods and services to a program of targeted cash transfers to low-income households.
- **Explain the reform.** Well-designed communication is essential to generate broad support for the reform. It should explain the cost of subsidies (including the distortions they create), who benefits from them, and how the public stands to gain from subsidy reform.
- **Start with the costliest and most regressive subsidies.** In light of their large fiscal cost, regressive nature, and negative externalities, energy subsidies should be first in line for reform (with the exception of butane, which is important in the consumption basket of poor households).
- **Adopt a depoliticized and rules-based mechanism for setting prices.** An automatic pricing mechanism, especially when communicated clearly to the public, can reduce the chances of reform reversal by distancing the government from pricing decisions, and would also help cap the cost of the subsidy.

**17. With hydrocarbon revenues significantly reduced, Algeria needs to mobilize more nonhydrocarbon revenues.** To raise more nonhydrocarbon revenues, tax exemptions (e.g., on VAT) should be significantly reduced, excise taxes increased, and property taxes overhauled. These measures would also help level the playing field among enterprises. It is also critical to improve tax administration, in particular tax enforcement. To bring the informal sector into the formal economy, the authorities should avoid offering tax amnesties and instead pursue other well-established measures in this area.<sup>6</sup> The authorities indicated that they are focused on improving tax enforcement, including with respect to arrears. They have also launched a welcome cost-benefit analysis of tax expenditures.

<sup>5</sup> The increase in fuel taxes has resulted in retail price increases in the range of 34 to 37 percent, but prices remain very low (e.g., unleaded gasoline went from US\$0.21 to US\$0.29 per liter).

<sup>6</sup> See "[Revenue Administration: Managing the Shadow Economy](#)" (IMF, 2014) and "[Current Challenges in Revenue Mobilization: Improving Tax Compliance](#)" (IMF, 2015).

**18. Public investment spending should be strategically curtailed and its efficiency substantially improved.** Capital spending averaged 15 percent of GDP over the last decade—higher than the averages in the region and in emerging market and developing countries. At the same time, Algeria’s investment efficiency is weak compared to other oil exporters in the region and well below the global average, implying that the adverse impact of investment cuts on growth could be modest initially if implemented strategically.<sup>7</sup> Given that the multiplier effect will increase over time as the least productive projects are eliminated, the government should strengthen investment efficiency by improving the selection, implementation, and ex-post assessment of investment projects. Better governance of state-owned enterprises (SOEs) would also improve investment efficiency while reducing the need for episodic fiscal bailouts. The authorities acknowledged that public investment spending had grown beyond Algeria’s absorptive capacity and needed to be rationalized.

**19. To meet large financing needs over the medium term, Algeria will need to borrow more.** Fiscal savings in the oil savings fund will likely be depleted this year, requiring more government borrowing to finance budget deficits over the medium term. An increase in government domestic debt issuance is also needed to help develop nascent monetary and capital markets. In a context of tightening liquidity conditions, interest rates on government debt will likely increase. Given very low external debt, the authorities could also consider borrowing externally (on international capital markets or from bilateral or multilateral creditors) to mitigate crowding out effects of domestic borrowing and reduce pressure on international reserves. Furthermore, the mission encouraged the authorities to open the capital of some SOEs to private participation, in a transparent way, not only to help meet financing needs but also to improve their governance. The authorities indicated a willingness to consider borrowing externally from bilateral or multilateral sources, but they are not considering borrowing on international capital markets at this time. In April 2016, they issued a domestic bond aimed at mobilizing savings in the informal sector. They consider partial or total privatization of some SOEs to be an option but not a short-term priority.

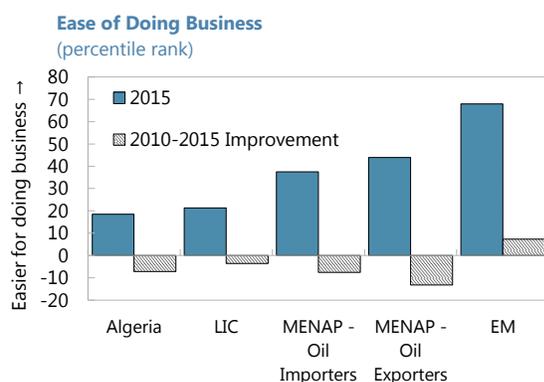
**20. Broad public financial management (PFM) reforms are needed to support fiscal consolidation and improve governance.** The mission supports the authorities’ efforts to adopt a medium-term budget framework and performance-based budgeting. The ongoing revision of the organic budget law could support these efforts, notably by including a fiscal rule that would help insulate fiscal policy from oil price volatility. The mission also recommended improving expenditure and revenue forecasting and the capacity to control spending, including by putting in place an integrated financial management information system. The authorities agreed with the need for PFM reforms and welcomed further technical assistance in this area. They are considering introducing a rule in the organic budget law that would tie current spending to nonhydrocarbon revenues.

<sup>7</sup> See the [staff report for the 2014 Article IV consultation](#), IMF Country Report No. 14/341.

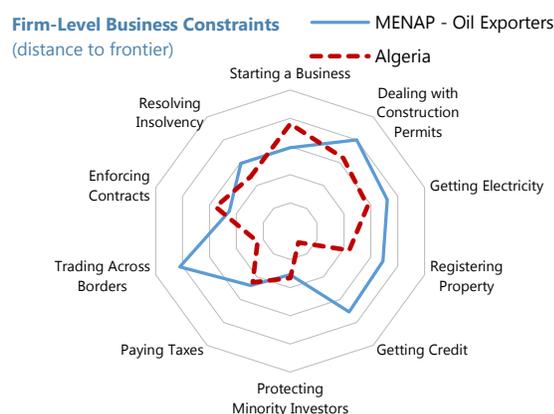
## B. Promoting Diversification and Private Sector-led Growth

**21. An ambitious structural reform agenda is needed to diversify the economy, increase potential growth, and create jobs.**<sup>8</sup> Algeria's state-led economic model is characterized by a large share of economic activity conducted by the public sector and based directly or indirectly on hydrocarbons. Pervasive bureaucracy and cumbersome administrative procedures hinder private sector activity. To adapt to a world of lower oil prices, the state will need to retrench and allow the private sector to take the lead. A critical mass of structural reforms is needed to unleash the potential of the private sector and should be implemented urgently, as reforms will take time to bear fruit. The authorities agreed with the need to change Algeria's economic model, but they continue to see a large role for the state in directing the economy.

**22. Algeria should continue its efforts to improve the business environment.** Recent efforts in this area—for instance to facilitate the creation of enterprises and the granting of building permits—go in the right direction. However, they have yet to translate into improved rankings in international surveys. Indeed, Algeria's 2016 Doing Business ranking slipped two places to 163<sup>rd</sup> out of 189 economies. Staff urged the authorities to continue streamlining administrative procedures related to starting a business, trading across borders, and registering property. The authorities stressed that improving the business environment required considerable coordination among agencies and therefore would take time. They nevertheless reiterated their commitment to pursue reforms, noting that a provision in the new constitution explicitly commits the government to improving the business environment.



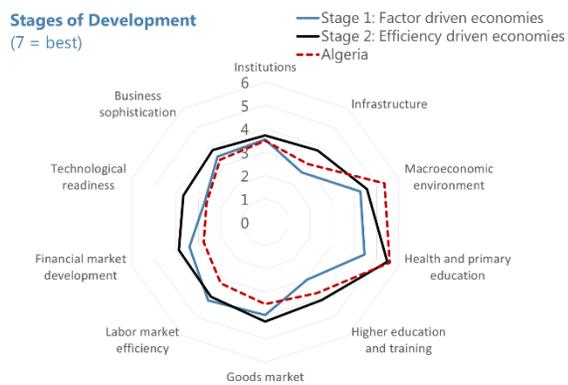
Sources: World Bank Doing Business (2016), and IMF staff calculations. EM = Emerging Market Countries. LIC = Low Income Countries.



<sup>8</sup> For more on diversification, see 2014 Selected Issues Paper: "[Fostering Export Diversification in Algeria.](#)"

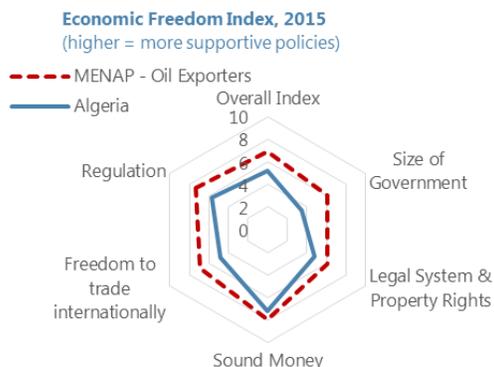
**Figure 4. Algeria: Structural Issues**

Algeria's labor and financial markets are particularly weak compared to other economies.



Sources: World Economic Forum 2015 Global Competitiveness Index; and IMF staff estimates.

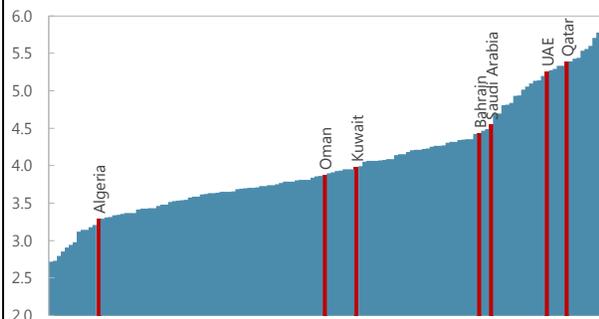
The economy is characterized by a dominant public sector, heavy regulations, and barriers to trade and investment.



Sources: Fraser Institute; and IMF staff estimates.

Businesses lack sophistication.

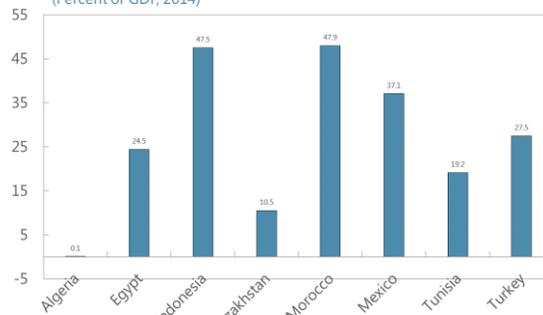
**Business Sophistication**  
(all countries, 7 = best)



Sources: World Economic Forum 2015 Global Competitiveness Index; and IMF staff estimates.

Capital markets are nascent.

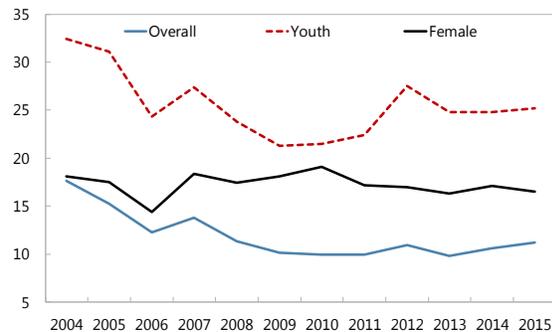
**Market Capitalization**  
(Percent of GDP, 2014)



Sources: World Bank; Bourse d'Alger; and IMF staff estimates.

The overall unemployment rate has started to edge higher...

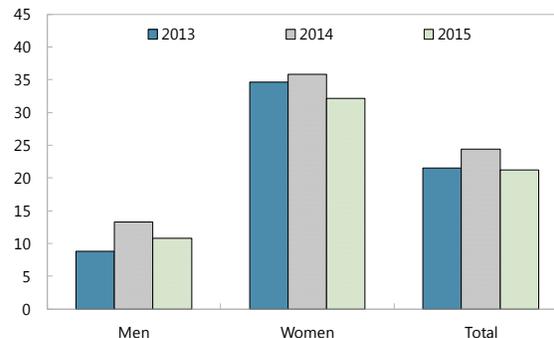
**Unemployment Rate**  
(Percent)



Source: Algerian authorities.

...and the share of youth that are neither employed, nor in school, nor in vocational training is high.

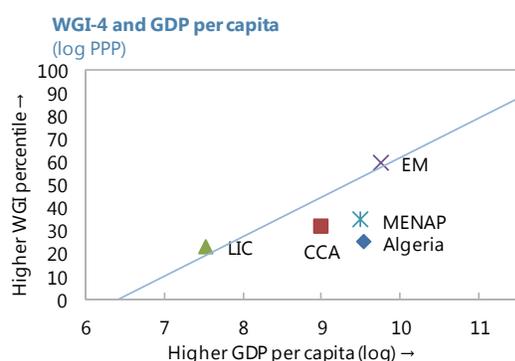
**Youth Not in Education, Employment or Training**  
(In percent of 15-24 year old population)



Source: Algerian authorities.

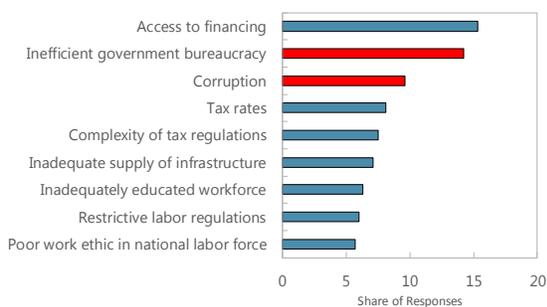
**23. To promote greater economic diversification, the government should open the economy to more trade and foreign investment.** Trade openness would support diversification through lower costs of inputs, technological transfers, and increased competition. Staff stressed that import restrictions, which the authorities have tightened in an effort to contain imports, should not be the response to the terms-of-trade shock, as they introduce distortions and rent-seeking opportunities, are likely to drive more activity underground, and may create inflationary pressures.<sup>9</sup> The authorities are currently overhauling the investment code. As a priority, staff urged them to seize the opportunity offered by this revision to eliminate or relax the requirement of a minimum 51 percent Algerian ownership in foreign investments (“51/49 rule”), which remains a major obstacle to foreign investment. Staff also reiterated its call for Algeria to pursue WTO accession, which has languished for decades.

**24. Improving governance, transparency, and competition are also needed.** According to the World Bank, Algeria ranks behind regional peers and emerging market countries in terms of governance. Other surveys find that poor governance and corruption are significant obstacles to doing business in Algeria, with negative implications for growth and job creation. Another feature of the economy is a lack of competition in certain sectors. More competition would lead to better functioning markets, where prices ensure the most efficient allocation of resources. Strengthening anti-corruption efforts, including by mobilizing the AML/CFT framework, would also assist in improving the business environment and social inclusion.



Sources: Worldwide Governance Indicators 2014 (government effectiveness, regulatory quality, rule of law, and control of corruption); the line is the trend for all countries.

**Algeria: Executive Opinion Survey, 2015**



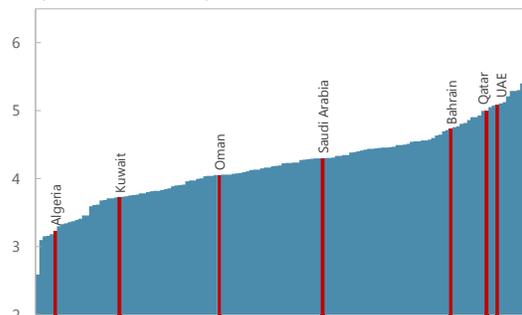
Source: World Economic Forum Executive Opinion Survey. From a list of 16 factors, respondents are asked to select the five most problematic and rank them from 1 (most problematic) to 5.

<sup>9</sup> In an effort to reduce imports, the authorities have begun requiring importers to apply for licenses to import certain products (e.g., vehicles and cement).

## 25. Further progress in reducing unemployment will require not only more labor-intensive economic growth, but also better functioning labor markets.

The unemployment rate has been edging higher, while the labor force participation rate—at 42 percent—is low by international standards. The labor market is marked by rigidities in hiring and firing, high payroll taxes, jobs-skills mismatches, and excessive growth in wages with respect to productivity. Staff supported the ongoing revision of the labor code—undertaken in consultation with representatives from trade unions and employers—as an opportunity to enhance labor market flexibility while ensuring adequate protection for workers. The mission also stressed the need to develop closer ties between the educational system and the private sector, and to thoroughly assess the effectiveness of active labor market policies.

**Labor Market Efficiency**  
(1-7 scale, 7 = best)

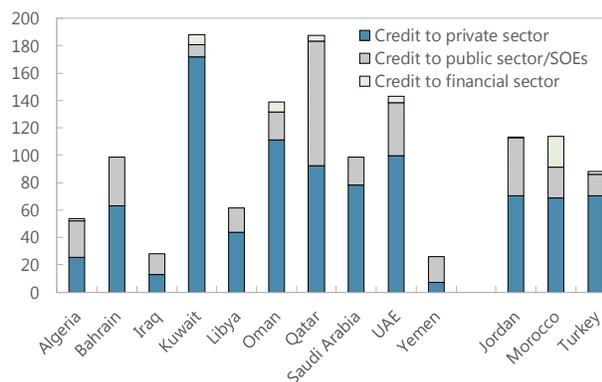


Source: World Economic Forum, Global Competitiveness Index (2015).

## 26. Reforms are needed to improve access to finance and develop capital markets.

Doing Business ranks Algeria 174<sup>th</sup> out of 189 countries on the ease of getting credit. The mission recommended strengthening competition in the banking sector, enhancing creditor rights, modernizing the bankruptcy framework, and improving debt enforcement procedures. Lending to small and medium-sized enterprises (SMEs) is impeded by high collateral requirements and difficulties dealing with NPLs. The guarantee system has so far failed to spur credit to SMEs and needs to be reformed. Opening the capital of large SOEs and state-owned banks to private participation would help increase competition and develop capital markets.

**Allocation of Domestic Credit to the Economy, 2014**  
(Percent of non-oil GDP)



Source: IMF staff estimates.

## C. Implementing Supportive Exchange Rate, Monetary, and Financial Policies

### Exchange rate policy

**27. Fiscal and external sector adjustment should be supported by a further real depreciation of the dinar.** Various methodologies point to a substantial current account gap, implying that the REER remains significantly overvalued (Annex III). Most of the adjustment should come from fiscal policy and structural reforms. Greater exchange rate flexibility would also help eliminate this overvaluation and rebalance the economy over the medium term, but cannot be the

primary lever, considering the insufficient diversification of the economy (and therefore the limited short-term potential for nonhydrocarbon exports) and the possible inflationary impact of further nominal exchange rate depreciation. The authorities agreed that the dinar remains overvalued and that fiscal policy should play a major role in reducing the overvaluation.

**28. Measures are needed to deepen and unify the foreign exchange market.** Staff called on the BA to take action to eliminate the premium in the illegal parallel foreign exchange market, which reportedly stands at around 50 percent. As a first step, the indicative foreign exchange ceiling for individuals should be raised to more realistic levels and related exchange procedures simplified. The relaxation of the 51/49 rule would also contribute to the supply of foreign exchange. In the longer term, it will be important to further diversify the supply of foreign exchange as part of a gradual and properly sequenced plan to develop foreign exchange markets. The plan would include lifting some capital account restrictions as well as relaxing repatriation and surrender obligations of nonhydrocarbon export receipts and the *de facto* high reserve requirement rate on foreign currency deposits. The authorities did not see an urgent need to relax foreign exchange controls, but they recently announced their intention to increase the indicative foreign exchange ceiling for individuals.

### Monetary policy

**29. Banque d'Algérie (BA) is adjusting to a changing liquidity environment.** As a result of the collapse in oil prices, Algeria is transitioning from a long period of structural excess liquidity to a situation of structural refinancing needs. This offers the BA an opportunity to reestablish control over domestic liquidity conditions and short-term interest rates, which would strengthen monetary policy transmission mechanisms. The BA is preparing to reintroduce its refinancing instruments and is working to strengthen its liquidity forecast and management capacity, in coordination with the Treasury. Staff recommended that the BA continue to absorb excess liquidity using its term deposits until neutral or quasi-neutral liquidity conditions are achieved (i.e., no excess reserves or close to banks' voluntary excess reserves). The BA should also reactivate the overnight lending facility in order to establish a ceiling on the (short-term) interest rate corridor. Thereafter, the BA should introduce open-market refinancing operations to signal its policy stance and take steps to encourage the development of the interbank repo market. The government can help by issuing more debt securities on a regular and predictable basis. The BA is continuing to absorb excess liquidity in the banking system, taking into account the government's debt issuance plans, and welcomed further technical assistance to help them manage the transition to the new liquidity environment.

**30. The BA should carefully calibrate monetary policy to guard against potential inflationary pressures.** Despite the anticipated fiscal consolidation, several factors could push inflation higher, including further dinar depreciation, the increase in subsidized prices, the impact of import restrictions, and the recent lifting of the ban on consumer credit. Because of these uncertainties, staff recommended that the BA maintain the existing interest rate corridor, rather than change existing rates, which may prematurely signal a shift in policy stance. In practice, as liquidity conditions normalize and banks turn to the BA or to other banks to meet their liquidity needs, funding costs will necessarily increase. The authorities agreed with the need to guard against

potential inflationary pressures and indicated that monetary policy would not be accommodative in the short term.

## Financial sector policy

**31. The impact of the oil price shock on banking system stability has been moderate so far.** At end-2015, the banking sector remained well capitalized, profitable, and with little maturity mismatch. Supported by robust growth in the nonhydrocarbon sector and a high level of public investment, the sector remained profitable while asset quality was broadly unchanged. Liquidity buffers have declined markedly, reflecting rapid credit growth and, since 2014, the decline in oil prices. Nonetheless, liquidity buffers at the system level remain high compared to other countries in the region.<sup>10</sup>

**Text Table 2. Prudential Indicators for the Algerian Banking System**

Ratio	2012	2013	2014	2015 <sup>1</sup>
Capital adequacy ratio (percent)	23.6	21.5	16.0	17.0
Return on assets (percent)	1.9	1.7	2.0	2.2
Gross NPL / total loans (percent)	11.7	10.6	9.2	9.5
Provisioning coverage ratio (percent)	69.8	68.2	65.2	61.4
Net NPL / total loans (percent)	3.5	3.4	3.2	3.6
Liquid assets / total assets (percent)	45.9	40.5	37.9	27.1
Liquid assets / short-term liabilities (percent)	107.5	93.5	82.1	64.0

Source: Banque d'Algérie.

<sup>1</sup>Preliminary.

**32. However, protracted lower oil prices can negatively affect the banking system through multiple channels.**<sup>11</sup> The banking system exhibits strong linkages with the hydrocarbon and public sectors. Public banks, which represent the bulk of the system, channel most of their lending to the public sector and rely heavily on oil-related public deposits. Private banks primarily focus on corporate banking business (both credit and funding), which remains highly sensitive to changes in hydrocarbon-driven fiscal spending. These linkages make the banking system vulnerable to oil price fluctuations, which can induce sharp reversals in liquidity and credit conditions due to the economy's insufficient diversification and fiscal policy procyclicality.

**33. The slump in oil prices is expected to increase liquidity, interest rate, and credit risks.** In the short term, excess liquidity will give way to structural refinancing needs, triggering higher funding costs in the banking system and reducing bank profitability. Over the medium term, liquidity risks could increase quickly if fiscal consolidation is not sustained, in part because of the high import content of capital expenditures and also because of increased debt issuance. By

<sup>10</sup> For example, liquid assets represent 26.5 percent of total bank assets on average in the Gulf Cooperation Council countries.

<sup>11</sup> See accompanying Selected Issues Paper: "The Financial Stability Implications of Low Oil Prices for Algeria."

contrast, the fiscal consolidation needed to restore macroeconomic balances could result in a slowdown of nonhydrocarbon activity and increase, possibly substantially, credit risks. The exchange rate channel is muted, as banks can only have small open foreign exchange positions and their foreign exchange funding source—nonhydrocarbon exports—is limited.

**34. Macro-financial linkages increase the vulnerability of the banking sector to systemic risks.** The large public banks, some of which are systemically important, are heavily reliant on public deposits and highly involved in financing public enterprises. A weaker fiscal position could lead public enterprises to increasingly draw down their deposits and take on long-term financing, putting liquidity pressures on both sides of public banks' balance sheets, increasing competition among banks for funding, and heightening systemic liquidity risks. In the event of a sharp slowdown of the economy, large exposures to the same set of public enterprises could lead to synchronized deterioration in bank asset quality. Furthermore, the expected return of banks to the interbank market will strengthen their interconnectedness, possibly opening up new channels through which potential problems in individual banks could spread to the system as a whole.

**35. The mission supported the recent improvements to regulatory and supervisory frameworks, which strengthen the resilience of the banking sector.** In 2014, the BA strengthened its regulatory and supervisory frameworks in response to the 2013 FSAP recommendations (Annex V). It introduced new regulations on capital adequacy related to pillar one of Basel II and elements of Basel III, and tightened existing large exposure requirements.<sup>12</sup> Although the new Basel III net stable funding ratio (NSFR) has not yet been implemented, the BA introduced a number of liquidity instruments to help reduce risk taking behaviors, including a minimum liquidity ratio that requires banks to hold highly liquid assets to meet short-term obligations, and a limit to the ratio of long-term liabilities to long-term assets. In addition, loan classification requirements were strengthened to cover the treatment of overdraft and restructured loans. The BA continues rolling out its CAMELS-based bank risk rating methodology to cover all banks, and new and improved offsite prudential indicators have been introduced. The mission also welcomed the ongoing bank stress tests and crisis simulation exercise conducted by the BA.

**36. The mission encouraged the BA to continue its efforts to strengthen the prudential framework.** Further efforts are needed to improve the surveillance of the build-up of risks in individual banks and in the system as a whole. Currently, important data gaps limit the BA's ability to monitor systemic risks, in particular with respect to common exposures and corporate and household leverage. The BA should also pursue its efforts to strengthen liquidity forecasting capabilities and conduct more frequent liquidity and solvency stress testing of the banking sector. Loan classification rules should be further tightened and existing regulations should be amended to

<sup>12</sup> The new regulations increased minimum capital adequacy requirements (from 8 percent to 9.5 percent, including a capital conservation buffer of 2.5 percent). They also tightened prudential limits on large exposures, reducing both the threshold of the aggregate large exposure limit to 8 (from 10) times the regulatory capital, and the threshold of individual exposures to be included in the aggregate limit to 10 (from 15) percent of regulatory capital.

include more detailed governance requirements for public banks.<sup>13</sup> The BA should strengthen its macroprudential framework, including by better defining the objectives of the financial stability committee, implementing a framework for systemic risk analysis, and improving data quality.<sup>14</sup> The BA should also implement a comprehensive macroprudential toolkit to address the buildup of systemic risks. Time-varying reserve requirements and dynamic provisioning could be envisaged. The authorities agreed with staff's recommendations and are seeking further technical assistance to implement them.

**37. The authorities should improve crisis preparedness and management.** A well-defined crisis resolution framework that provides a clear description of roles and responsibilities of the different agencies is lacking, and the range of available bank resolution options is limited to the liquidation of insolvent banks under the general insolvency regime. An explicit framework for bank resolution should be prepared while the insolvency framework should be strengthened. The authorities agreed with staff's recommendations but noted that implementation would take time given the need to coordinate with many stakeholders.

## STAFF APPRAISAL

**38. Algeria's economy is facing a severe and likely long-lasting external shock, calling for a vigorous policy response built on fiscal consolidation and structural reforms.** The collapse in oil prices has exposed longstanding vulnerabilities in a state-led economy that is overly dependent on hydrocarbons. Thus far, the impact of the oil price shock on growth has been limited, but fiscal and external balances have deteriorated significantly. Thanks to buffers accumulated in the past, Algeria has a window of opportunity to smooth the adjustment to the shock and reshape its growth model. Restoring macroeconomic balances will require sustained fiscal consolidation over the medium term combined with a critical mass of structural reforms to diversify the economy, while exchange rate, monetary, and financial policies should play a supporting role. Communication to build a consensus around the needed reforms will be important to ensure their timely implementation.

**39. Fiscal consolidation will need to be sustained over the medium term to restore fiscal sustainability, ensure intergenerational equity, and support external stability.** It will require controlling current spending, pursuing further subsidy reform while protecting the poor, mobilizing more nonhydrocarbon revenues, increasing the efficiency of investment, and strengthening the budget framework. Rapidly declining fiscal savings mean that Algeria will need to borrow more to finance future deficits. In addition to increasing domestic debt issuance, the authorities should

<sup>13</sup> Currently, banks are not required to classify as non-performing an impaired loan that carries a government guarantee.

<sup>14</sup> A Financial Stability Committee (FSC) was created in 2009 and is responsible for macroprudential monitoring and implementation. However, due to the lack of an effective operational structure and formalized objectives, the FSC has not monitored systemic risks on a regular basis and has not put in place a macroprudential policy framework.

consider borrowing externally and opening the capital of some state-owned enterprises, in a transparent way, to private participation.

**40. Wide-ranging structural reforms are needed to help support economic activity during the fiscal consolidation and to diversify the economy.** Key reforms include improving the business climate, opening up the economy to more trade and investment, improving access to finance and developing capital markets, and strengthening governance, competition, and transparency. Increasing the flexibility of labor markets while better matching the skills produced by the educational system to those needed by the private sector is also needed. Import restrictions, while perhaps providing a temporary relief, introduce distortions and cannot substitute for reforms aimed at boosting exports. As structural reforms take time to bear fruit, they should be started without delay.

**41. Together with fiscal consolidation and structural reforms, greater exchange rate flexibility would support the adjustment to the oil price shock.** Despite some depreciation in 2015, the REER remains significantly overvalued. Fiscal consolidation and structural reforms, together with greater exchange rate flexibility, would help bring the REER in line with its equilibrium value and contribute to the rebalancing of the economy.

**42. Monetary policy must adjust to a changing liquidity environment while guarding against potential inflationary pressures.** The BA is appropriately adjusting to a changing liquidity environment by reactivating its lending instruments and strengthening its liquidity forecast and management capacity. Going forward, it should carefully calibrate monetary policy to guard against potential inflationary pressures.

**43. Financial sector policies should be further strengthened to address growing financial stability risks.** The banking sector as a whole is well capitalized and profitable, but protracted low oil prices increase financial stability risks. Moreover, the strong links between the financial, hydrocarbon, and public sectors increase the vulnerability of banks to systemic risks and call for preemptive actions. The authorities should continue their efforts to strengthen the prudential framework, including by enhancing the role of macroprudential policy, and improving crisis preparedness and management.

Table 1. Algeria: Selected Economic and Financial Indicators, 2013–21

	Est.			Proj.					
	2013	2014	2015	2016	2017	2018	2019	2020	2021
Output and prices									
	(Annual percentage change)								
Real GDP	2.8	3.8	3.9	3.4	2.9	2.6	2.8	3.1	3.4
Hydrocarbon sector	-5.5	-0.6	0.4	1.9	2.0	2.4	2.4	2.6	2.5
Nonhydrocarbon sector	7.1	5.6	5.5	3.7	3.1	2.7	2.9	3.2	3.6
Consumer price index (period average)	3.3	2.9	4.8	4.3	4.0	4.0	4.0	4.0	4.0
Investment and savings									
	(In percent of GDP)								
Savings-investment balance	0.4	-4.4	-16.2	-17.9	-17.0	-13.1	-10.6	-9.1	-8.6
National savings	45.1	43.4	36.4	32.1	31.9	34.8	37.3	39.0	39.4
Government	10.5	6.5	1.5	-0.6	2.0	3.7	5.0	6.1	7.2
Nongovernment	34.6	36.9	34.8	32.7	29.8	31.2	32.4	32.9	32.2
Investment	44.7	47.8	52.6	50.0	48.9	47.9	47.9	48.1	48.0
Government	11.4	14.5	17.9	15.0	14.3	13.8	13.4	13.0	12.5
Nongovernment	33.3	33.3	34.6	35.0	34.6	34.1	34.5	35.1	35.4
Central government finances									
	(In percent of GDP)								
Overall budget balance	-0.9	-8.0	-16.4	-15.6	-12.2	-10.1	-8.4	-6.9	-5.3
Revenue	35.8	33.4	30.1	26.8	28.0	28.8	29.3	29.7	30.1
Expenditure (incl. net lending)	36.7	41.3	46.5	42.4	40.2	38.9	37.7	36.6	35.4
Gross government debt	7.7	8.0	9.0	15.4	25.4	32.8	38.1	41.6	43.3
	(In percent of nonhydrocarbon GDP)								
Nonhydrocarbon primary balance	-32.4	-37.7	-37.5	-29.4	-27.2	-25.6	-24.0	-22.4	-20.6
Nonhydrocarbon balance	-32.7	-38.0	-37.8	-29.9	-27.9	-26.5	-25.2	-23.9	-22.3
Revenue	51.0	45.7	37.2	31.2	33.3	34.7	35.6	36.4	37.0
Hydrocarbon	31.5	27.0	17.5	11.8	13.3	14.3	15.0	15.4	15.7
Nonhydrocarbon	19.5	18.7	19.7	19.4	20.0	20.3	20.7	21.0	21.3
Expenditure	51.6	55.8	56.9	48.8	47.6	46.8	45.8	44.8	43.6
Current expenditure	35.4	35.8	34.6	31.4	30.7	30.1	29.6	28.9	28.2
Capital expenditure	16.2	19.9	22.2	17.4	17.0	16.7	16.3	15.9	15.4
External sector 1/									
Current account balance (percent of GDP)	0.4	-4.4	-16.2	-17.9	-17.0	-13.1	-10.6	-9.1	-8.6
Exports, f.o.b. (percent change)	-10.2	-6.8	-42.3	-29.4	17.4	9.4	7.3	6.1	5.5
Hydrocarbons	-10.3	-7.8	-43.3	-31.0	17.8	9.2	6.9	5.6	5.0
Nonhydrocarbons	-8.9	55.4	-9.1	8.1	12.2	12.0	13.0	13.4	11.8
Imports, f.o.b. (percent change)	6.6	8.5	-11.8	-9.6	6.7	-5.4	-2.6	-0.5	2.5
Export volume (hydrocarbons, percent change)	-6.9	-0.6	-0.2	0.0	0.9	1.5	1.6	1.7	2.2
Import volume (percent change)	-0.7	-1.1	-5.7	-3.1	0.5	0.5	0.6	0.5	0.4
Terms of trade (percent change, "-" = deterioration)	-2.9	-6.2	-39.7	-28.8	16.2	7.1	4.6	3.3	2.4
Crude oil exports (in millions of barrels/day)	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.6
Nonhydrocarbon exports (percent of total exports)	1.6	2.7	4.3	6.6	6.3	6.4	6.8	7.2	7.7
Gross official reserves (US\$ billions)	192	177	143	113	91	76	62	52	41
In months of next year's imports of goods and services	32	33	30	22	19	16	13	11	9
Oil and gas sector									
Hydrocarbon production (in ton oil equivalent)	137	142	142	145	148	151	155	159	163
Hydrocarbon exports									
Of which: liquid petroleum exports (in millions of barrels/day)	1.2	1.2	1.2	1.2	1.2	1.3	1.3	1.3	1.3
Of which: natural gas exports (in billions of m3)	46.3	44.3	42.8	42.8	43.2	43.8	44.6	45.5	46.6
Crude oil export unit value (US\$/bbl)	109.5	99.4	53.1	36.6	42.8	46.0	48.5	50.3	51.7
Share of hydrocarbons in total exports (in percent)	98.4	97.3	95.7	93.4	93.7	93.6	93.2	92.8	92.3
Money and credit									
	(Annual percentage change unless otherwise indicated)								
Net foreign assets	1.9	3.3	-2.4	-18.8	-15.6	-13.5	-14.2	-14.1	-17.1
Credit to the economy	19.9	25.7	16.1	9.0	10.0	8.5	8.4	8.4	8.5
Money and quasi-money	8.4	14.4	0.5	1.1	10.0	8.5	8.4	8.4	8.5
Velocity of broad money (GDP/M2)	1.4	1.3	1.2	1.2	1.2	1.2	1.2	1.2	1.2
Memorandum items:									
GDP (in billions of dinars at current prices)	16,644	17,205	16,799	16,988	18,688	20,272	21,968	23,816	25,846
NHGD (in billions of dinars at current prices)	11,676	12,547	13,566	14,602	15,704	16,819	18,060	19,441	21,008
GDP (in billions of US\$ current prices)	210	214	167	161	168	174	179	185	192
GDP capita per (in US\$)	5,476	5,459	4,182	3,952	4,072	4,136	4,197	4,261	4,331
Exchange rate (DA per US\$)	79.4	80.6	100.7	...	...	...	...	...	...
REER (percent change)	-1.4	2.1	-4.3	...	...	...	...	...	...

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

1/ In U.S. dollars terms.

Table 2. Algeria: Balance of Payments, 2013–21

	Est.				Proj.				
	2013	2014	2015	2016	2017	2018	2019	2020	2021
	(In billions of U.S. dollars; unless otherwise indicated)								
Current account	0.8	-9.4	-27.0	-28.8	-28.7	-22.7	-19.0	-16.9	-16.5
Trade balance	9.4	0.3	-18.1	-23.1	-22.1	-16.6	-13.1	-10.8	-9.9
Exports, f.o.b.	64.4	60.0	34.6	24.4	28.7	31.4	33.7	35.7	37.7
Hydrocarbons	63.3	58.4	33.1	22.8	26.9	29.4	31.4	33.2	34.8
Volume change (in percent)	-6.9	-0.6	-0.2	0.0	0.9	1.5	1.6	1.7	2.2
Price change (in percent)	-3.6	-7.2	-43.1	-31.0	16.8	7.6	5.3	3.9	2.7
Other	1.1	1.6	1.5	1.6	1.8	2.0	2.3	2.6	2.9
Imports, f.o.b.	-55.0	-59.7	-52.6	-47.6	-50.7	-48.0	-46.7	-46.5	-47.6
Volume change (in percent)	7.4	9.7	-6.4	-6.7	6.1	-5.9	-3.3	-1.0	2.1
Price change (in percent)	-0.7	-1.1	-5.7	-3.1	0.5	0.5	0.6	0.5	0.4
Services and income (net)	-11.3	-13.0	-11.7	-8.4	-9.5	-9.1	-9.0	-9.3	-9.9
Services (net)	-6.8	-8.2	-7.2	-6.7	-7.0	-6.2	-5.7	-5.5	-5.5
Credit	3.9	3.5	3.8	3.3	3.6	3.9	4.1	4.3	4.4
Debit	-10.7	-11.7	-11.0	-9.9	-10.6	-10.0	-9.8	-9.7	-9.9
Income (net)	-4.5	-4.9	-4.5	-1.7	-2.5	-2.9	-3.3	-3.9	-4.4
Credit	3.5	3.2	2.1	1.5	1.5	1.6	1.7	1.5	1.3
Debit	-8.1	-8.1	-6.6	-3.2	-4.0	-4.5	-5.0	-5.4	-5.7
Interest payments	-0.1	0.0	-0.1	-0.1	-0.3	-0.5	-0.7	-0.8	-0.9
Other, including profit repatriation	-8.0	-8.0	-6.5	-3.1	-3.7	-4.0	-4.3	-4.6	-4.8
Transfers (net)	2.8	3.3	2.7	2.7	2.9	3.0	3.1	3.2	3.3
Capital account	-0.7	3.6	-0.5	2.8	6.9	7.1	5.6	5.9	6.3
Medium- and long-term capital	1.5	1.3	-1.1	3.1	6.9	7.2	5.6	5.9	6.3
Direct investment (net)	2.0	1.5	-0.7	1.4	1.8	2.2	2.6	3.1	3.6
Loans (net)	-0.4	-0.2	-0.4	1.7	5.1	5.0	2.9	2.8	2.7
Drawings	0.0	0.0	0.0	2.0	5.5	5.5	3.5	3.5	3.5
Amortization	-0.4	-0.2	-0.4	-0.3	-0.4	-0.5	-0.6	-0.7	-0.8
Short-term capital and errors and omissions	-2.3	2.3	0.7	-0.3	0.0	-0.1	0.0	0.0	0.0
Overall balance	0.1	-5.9	-27.5	-26.0	-21.8	-15.6	-13.4	-11.0	-10.2
Financing	-0.1	5.9	27.5	26.0	21.8	15.6	13.4	11.0	10.2
Official reserves (increases -)	-0.1	5.9	27.5	26.0	21.8	15.6	13.4	11.0	10.2
Memorandum items:									
Current account balance (in percent of GDP)	0.4	-4.4	-16.2	-17.9	-17.0	-13.1	-10.6	-9.1	-8.6
Algerian crude oil price (US\$/barrel) 1/	109.5	99.4	53.1	36.6	42.8	46.0	48.5	50.3	51.7
Gross official reserves (in billions of US\$) 2/	192.4	177.4	142.6	112.8	91.3	75.8	62.5	51.6	41.4
Idem, in months of next year's imports	32.3	33.5	29.8	22.1	18.9	16.1	13.3	10.8	8.6
Reserves (in percent of ARA EM Metric)	858.4	783.1	833.0	711.6	537.6	429.4	341.5	272.4	210.4
Net international investment position (in billions of US\$)	158.6	141.7	132.7	96.1	71.2	52.6	36.5	23.2	10.8
Net international investment position (in percent of GDP)	75.6	66.3	79.6	59.8	42.3	30.2	20.3	12.5	5.6
Gross external debt (in billions of US\$)	3.4	3.7	3.0	4.4	8.2	11.9	13.8	15.7	17.6

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

1/ Weighted average of quarterly data.

2/ Excluding SDR holdings.

Table 3a. Algeria: Summary of Central Government Operations, 2013–21 1/

	Est.			Proj.					
	2013	2014	2015	2016	2017	2018	2019	2020	2021
	(In billion of Algerian dinars)								
Budget revenue and grants	5,958	5,738	5,051	4,560	5,231	5,828	6,435	7,076	7,781
Hydrocarbon revenue 2/	3,678	3,388	2,375	1,728	2,096	2,407	2,705	3,000	3,308
Nonhydrocarbon revenue	2,279	2,350	2,676	2,832	3,135	3,421	3,730	4,076	4,474
Tax revenue	2,031	2,091	2,354	2,615	2,912	3,188	3,495	3,833	4,225
Taxes on income and profits	823	881	1,050	1,162	1,281	1,410	1,553	1,715	1,900
Taxes on goods and services	742	769	815	938	1,067	1,173	1,290	1,415	1,561
Customs duties	404	371	406	427	468	503	543	585	636
Registration and stamps	63	71	82	89	95	102	110	118	128
Nontax revenues	248	258	323	217	223	232	234	243	248
Fees	84	76	197	96	100	104	108	113	117
Bank of Algeria dividends and interests	112	123	89	80	79	81	76	76	73
Other	53	60	37	40	44	47	50	54	58
Grants	0	0	0	0	0	0	0	0	0
Total expenditure	6,024	6,996	7,712	7,131	7,482	7,867	8,279	8,710	9,159
Current expenditure	4,132	4,494	4,697	4,591	4,815	5,066	5,338	5,622	5,917
Personnel expenditure	1,792	1,941	1,861	1,971	2,080	2,196	2,318	2,447	2,583
Mudjahidins' pensions	226	218	267	279	290	302	314	326	339
Material and supplies	149	162	118	59	64	71	78	86	95
Current transfers	1,920	2,136	2,407	2,212	2,269	2,333	2,402	2,473	2,548
Interest payments	44	38	43	71	111	165	227	290	352
Capital expenditure	1,893	2,501	3,015	2,540	2,667	2,801	2,941	3,088	3,242
Budget balance	-67	-1,258	-2,661	-2,571	-2,251	-2,038	-1,844	-1,634	-1,377
Overall balance	-144	-1,376	-2,758	-2,642	-2,286	-2,056	-1,853	-1,638	-1,380
Primary overall balance	-100	-1,338	-2,716	-2,572	-2,175	-1,891	-1,626	-1,348	-1,028
Nonhydrocarbon balance	-3,822	-4,764	-5,133	-4,370	-4,382	-4,464	-4,558	-4,638	-4,687
Financing	144	1,376	2,758	2,642	2,286	2,056	1,853	1,638	1,380
Domestic	146	1,378	2,761	2,493	1,870	1,624	1,624	1,394	1,119
Bank 3/	-95	1,174	2,560	1,900	1,031	1,062	1,061	948	728
Nonbank	241	204	201	593	839	562	564	445	391
Foreign	-2	-2	-3	149	416	433	229	245	260
Memorandum items									
Oil stabilization fund									
in billions of Algerian dinars	5,564	4,408	2,074	740	740	740	740	740	740
in percent of GDP	33.4	25.6	12.3	4.4	4.0	3.7	3.4	3.1	2.9
Gross government debt (in percent of GDP)	7.7	8.0	9.0	15.4	25.4	32.8	38.1	41.6	43.3
Net savings (in percent of GDP)	25.7	17.7	3.3	-11.1	-21.4	-29.2	-34.8	-38.5	-40.4

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

1/ On cash basis.

2/ Including Sonatrach dividends.

3/ Bank financing includes domestic debt issuance and a drawdown of the oil stabilization fund and other government deposits at the central bank.

Table 3b. Algeria: Summary of Central Government Operations, 2013–21 1/

			Est.		Proj.				
	2013	2014	2015	2016	2017	2018	2019	2020	2021
	(In percent of GDP)								
Budget revenue and grants	35.8	33.4	30.1	26.8	28.0	28.8	29.3	29.7	30.1
Hydrocarbon revenue 2/	22.1	19.7	14.1	10.2	11.2	11.9	12.3	12.6	12.8
Nonhydrocarbon revenue	13.7	13.7	15.9	16.7	16.8	16.9	17.0	17.1	17.3
Tax revenue	12.2	12.2	14.0	15.4	15.6	15.7	15.9	16.1	16.3
Nontax revenues	1.5	1.5	1.9	1.3	1.2	1.1	1.1	1.0	1.0
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total expenditure	36.2	40.7	45.9	42.0	40.0	38.8	37.7	36.6	35.4
Current expenditure	24.8	26.1	28.0	27.0	25.8	25.0	24.3	23.6	22.9
Personnel expenditure	10.8	11.3	11.1	11.6	11.1	10.8	10.6	10.3	10.0
Current transfers	11.5	12.4	14.3	13.0	12.1	11.5	10.9	10.4	9.9
Capital expenditure	11.4	14.5	17.9	15.0	14.3	13.8	13.4	13.0	12.5
Budget balance	-0.4	-7.3	-15.8	-15.1	-12.0	-10.1	-8.4	-6.9	-5.3
Overall balance	-0.9	-8.0	-16.4	-15.6	-12.2	-10.1	-8.4	-6.9	-5.3
Primary overall balance	-0.6	-7.8	-16.2	-15.1	-11.6	-9.3	-7.4	-5.7	-4.0
Nonhydrocarbon balance	-23.0	-27.7	-30.6	-25.7	-23.5	-22.0	-20.7	-19.5	-18.1
Financing	0.9	8.0	16.4	15.6	12.2	10.1	8.4	6.9	5.3
Domestic	0.9	8.0	16.4	14.7	10.0	8.0	7.4	5.9	4.3
Bank 3/	-0.6	6.8	15.2	11.2	5.5	5.2	4.8	4.0	2.8
Nonbank	1.4	1.2	1.2	3.5	4.5	2.8	2.6	1.9	1.5
Foreign	0.0	0.0	0.0	0.9	2.2	2.1	1.0	1.0	1.0
	(In percent of non-oil GDP)								
Budget revenue and grants	51.0	45.7	37.2	31.2	33.3	34.7	35.6	36.4	37.0
Hydrocarbon revenue 2/	31.5	27.0	17.5	11.8	13.3	14.3	15.0	15.4	15.7
Nonhydrocarbon revenue	19.5	18.7	19.7	19.4	20.0	20.3	20.7	21.0	21.3
Tax revenue	17.4	16.7	17.3	17.9	18.5	19.0	19.4	19.7	20.1
Nontax revenues	2.1	2.1	2.4	1.5	1.4	1.4	1.3	1.2	1.2
Grants	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total expenditure	51.6	55.8	56.9	48.8	47.6	46.8	45.8	44.8	43.6
Current expenditure	35.4	35.8	34.6	31.4	30.7	30.1	29.6	28.9	28.2
Capital expenditure	16.2	19.9	22.2	17.4	17.0	16.7	16.3	15.9	15.4
Budget balance	-0.6	-10.0	-19.6	-17.6	-14.3	-12.1	-10.2	-8.4	-6.6
Overall balance	-1.2	-11.0	-20.3	-18.1	-14.6	-12.2	-10.3	-8.4	-6.6
Primary overall balance	-0.9	-10.7	-20.0	-17.6	-13.9	-11.2	-9.0	-6.9	-4.9
Nonhydrocarbon balance	-32.7	-38.0	-37.8	-29.9	-27.9	-26.5	-25.2	-23.9	-22.3
Financing	1.2	11.0	20.3	18.1	14.6	12.2	10.3	8.4	6.6
Domestic	1.2	11.0	20.4	17.1	11.9	9.7	9.0	7.2	5.3
Bank 3/	-0.8	9.4	18.9	13.0	6.6	6.3	5.9	4.9	3.5
Nonbank	2.1	1.6	1.5	4.1	5.3	3.3	3.1	2.3	1.9
Foreign	0.0	0.0	0.0	1.0	2.7	2.6	1.3	1.3	1.2

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

1/ On cash basis.

2/ Including Sonatrach dividends.

3/ Bank financing includes domestic debt issuance and a drawdown of the oil stabilization fund and other government deposits at the central bank.

Table 4. Algeria: Monetary Survey, 2013–21

	Est.				Proj.				
	2013	2014	2015	2016	2017	2018	2019	2020	2021
(In billions of Algerian dinars; at end of period)									
Net foreign assets	15,099	15,602	15,222	12,361	10,438	9,025	7,741	6,647	5,508
<i>Of which: Bank of Algeria</i>	15,145	15,695	15,373	12,520	10,604	9,199	7,924	6,839	5,710
Foreign assets (BA)	15,130	15,431	15,297	12,709	10,803	9,408	8,144	7,070	5,952
Foreign liabilities (BA)	146	155	181	190	199	209	219	230	242
Foreign assets (comm. banks)	48	45	57	60	63	67	70	73	77
Foreign liabilities (comm. banks)	94	138	208	219	230	241	253	266	279
Net domestic assets	-3,158	-1,938	-1,490	1,526	4,842	7,559	10,228	12,833	15,626
Domestic credit	500	3,079	6,699	9,289	11,155	12,994	14,888	16,743	18,468
Credit to government (net) 1/	-4,742	-3,512	-952	948	1,979	3,041	4,101	5,050	5,778
Credit to the economy	5,242	6,591	7,651	8,341	9,176	9,953	10,786	11,694	12,690
<i>Of which: Private sector</i>	2,747	3,151	3,633	3,839	4,223	4,581	4,965	5,382	5,841
Other items net	-3,658	-5,017	-8,190	-7,764	-6,313	-5,436	-4,659	-3,910	-2,842
Money and quasi-money (M2)	11,942	13,664	13,731	13,887	15,280	16,583	17,969	19,480	21,134
Excluding Sonatrach deposits	11,432	12,839	13,245	13,535	14,874	16,062	17,334	18,751	20,337
Money	8,250	9,580	9,558	9,767	10,734	11,591	12,509	13,532	14,676
Quasi-money	3,692	4,084	4,173	4,120	4,546	4,992	5,460	5,949	6,458
(In percent change over 12-month period)									
Money and quasi-money (M2)	8.4	14.4	0.5	1.1	10.0	8.5	8.4	8.4	8.5
<i>Of which: Money</i>	7.4	16.1	-0.2	2.2	9.9	8.0	7.9	8.2	8.5
Credit to the economy	19.9	25.7	16.1	9.0	10.0	8.5	8.4	8.4	8.5
<i>Of which: Private sector</i>	20.9	14.7	15.3	5.7	10.0	8.5	8.4	8.4	8.5
Memorandum items:									
Liquidity ratio (average M2/GDP)	71.7	79.4	81.7	81.7	81.8	81.8	81.8	81.8	81.8
Liquidity ratio (e.o.p. M2/NHGDP)	102.3	108.9	101.2	95.1	97.3	98.6	99.5	100.2	100.6
M2 velocity	1.394	1.259	1.223	1.223	1.223	1.222	1.223	1.223	1.223
Credit to the economy/GDP	31.5	38.3	45.5	49.1	49.1	49.1	49.1	49.1	49.1
Credit to the economy/NHGDP	44.9	52.5	56.4	57.1	58.4	59.2	59.7	60.1	60.4
Credit to private sector/NHGDP	23.5	25.1	26.8	26.3	26.9	27.2	27.5	27.7	27.8

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

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

**Table 5. Algeria: Financial Soundness Indicators, 2009–15**

(In percent)

	2009	2010	2011	2012	2013	2014	2015 Prel.
Capital adequacy ratio	26.2	23.6	23.7	23.4	21.5	16.0	17.0
- Public banks	23.9	21.7	21.9	21.6	19.9	14.9	16.2
- Private banks	35.2	31.6	31.2	31.9	28.5	20.9	20.6
Tier I capital adequacy ratio	19.1	17.7	16.9	17.3	15.5	13.3	14.5
- Public banks	15.6	14.8	14.1	14.7	13.1	11.7	13.3
- Private banks	32.9	29.3	28.8	29.5	26.3	20.2	19.9
NPLs net of provisions/Tier I capital	33.9	21.1	19.4	16.2	17.1	21.4	24.7
- Public banks	46.0	27.5	25.1	20.4	21.7	26.8	27.2
- Private banks	1.5	3.0	2.3	3.4	2.6	4.6	16.3
NPLs/total loans	21.1	18.3	14.5	11.5	10.6	9.2	9.4
- Public banks	23.6	20.5	16.1	12.4	11.4	9.7	9.5
- Private banks	3.8	4.1	4.0	5.2	4.8	5.1	8.7
NPLs net of provisions/total loans	7.3	4.9	4.4	3.5	3.4	3.2	3.6
- Public banks	8.3	5.4	4.9	3.8	3.7	3.4	3.5
- Private banks	0.7	1.4	1.0	1.5	0.9	1.4	4.8
Provisions/classified loans	65.4	76.5	69.8	69.5	68.2	65.2	61.4
- Public banks	65.0	73.7	69.6	69.4	67.4	64.8	63.4
- Private banks	82.0	66.7	75.9	71.7	80.3	71.9	44.9
Return on equity	26.0	16.7	24.7	23.3	19.0	23.6	24.6
- Public banks	27.9	29.8	26.1	22.7	17.9	25.1	27.7
- Private banks	20.9	20.3	21.4	24.8	21.6	19.6	15.7
Return on assets	1.8	2.2	2.1	2.0	1.7	2.0	2.2
- Public banks	1.5	1.8	1.8	1.6	1.3	1.8	2.1
- Private banks	3.7	4.6	4.5	4.6	3.8	3.3	3.1
Interest margin/gross revenues	58.4	63.8	64.9	67.2	68.2	68.5	69.1
- Public banks	60.4	71.6	73.6	78.1	71.5	68.4	68.7
- Private banks	52.5	44.2	44.4	41.6	59.1	69.1	70.6
Non-interest expenses/earnings before tax	32.2	31.4	33.6	33.2	33.5	28.5	26.9
- Public banks	33.7	31.6	34.8	34.7	33.9	26.9	24.4
- Private banks	31.0	31.0	30.8	29.5	32.3	34.4	36.6
Liquid assets/total assets	51.8	53.0	50.2	45.9	40.5	38.0	27.2
- Public banks	52.8	54.2	51.1	45.1	39.4	37.0	25.9
- Private banks	44.7	43.7	43.2	50.9	46.5	44.0	35.9
Liquid assets/short-term debt	114.5	114.3	103.7	107.5	93.5	82.1	63.9
- Public banks	118.4	118.1	106.6	110.5	95.7	83.4	62.8
- Private banks	89.0	88.5	84.6	93.5	84.1	75.4	69.8

Source: Bank of Algeria

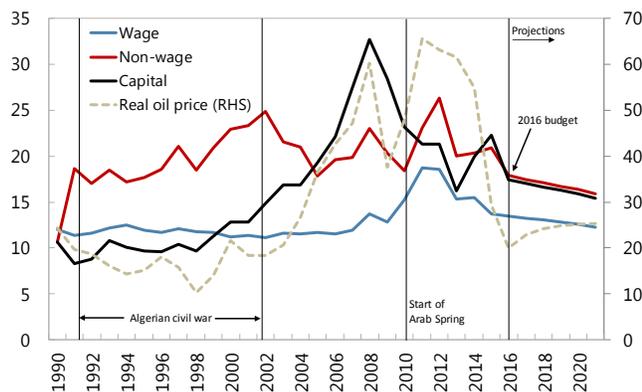
## Annex I. Alternative Scenarios

### Staff discussed the implications of three scenarios:

- A **baseline** scenario that assumes a gradual fiscal adjustment beyond 2016, some structural reforms, and some further real exchange rate depreciation. The wage bill returns to pre-Arab Spring levels (as a percent on nonhydrocarbon GDP) and capital spending falls back to 2002 levels. Nonhydrocarbon growth initially slows under the effects of fiscal consolidation (see fiscal multiplier assumptions below) but eventually accelerates as structural reforms start bearing fruit.

#### Expenditures - Baseline Scenario

(Percent of nonhydrocarbon GDP)



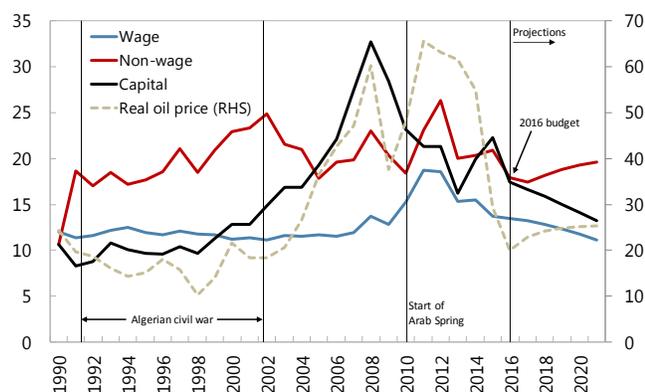
Sources: Algerian authorities; and IMF staff calculations.

- A **no-policy-change** scenario that assumes no further fiscal consolidation beyond 2016 (i.e., the nonhydrocarbon primary deficit is fixed at the projected 2016 level as a percent of nonhydrocarbon GDP). Wage growth exceeds productivity gains and inflation, and capital spending remains at the 2016 level as a percent of GDP. To meet growing financing needs, the government begins to borrow on international capital markets.

- An **ambitious** scenario that assumes additional fiscal consolidation beyond what is in the baseline. The wage bill gradually returns to levels that prevailed in the early 2000s (as a percent of nonhydrocarbon GDP), capital spending returns to pre-oil boom levels, targeted cash transfers are introduced, and revenues increase further. In addition, wide-ranging structural reforms are implemented, ultimately leading to an acceleration in private sector-led growth. Although financing needs are reduced compared to the other two scenarios, the government is nevertheless assumed to borrow externally (on international capital markets as well as from multilateral or bilateral creditors.)

#### Expenditures - Ambitious Scenario

(Percent of nonhydrocarbon GDP)



Sources: Algerian authorities; and IMF staff calculations.

**The no-policy-change scenario leads to a rapid deterioration of key economic indicators.** Real GDP growth is initially supported by continued expansive fiscal policy, but over the medium term large deficits crowd out private sector credit and lead to a loss of confidence. High and persistent fiscal deficits increase debt, which grows to 65 percent of GDP. Current account deficits widen over the medium term, leading to a further depletion of foreign reserves.

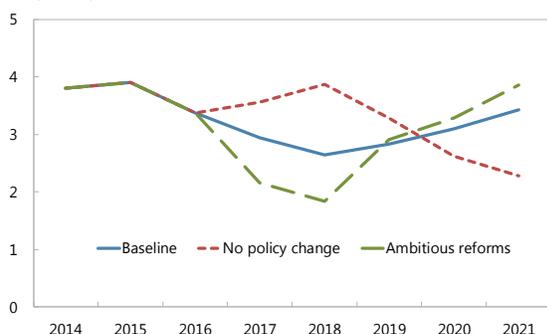
**In the ambitious scenario, sustained fiscal consolidation coupled with structural reforms helps restore macroeconomic balances.** Fiscal consolidation initially leads to slower growth compared to the baseline and ambitious reform scenarios, but growth begins to accelerate in the outer years, reflecting the impact of structural reforms. By 2021, the fiscal balance approaches equilibrium and current account surpluses return. Reserves start to accumulate again in 2020.

### Fiscal Multiplier Assumptions

Ratio	Year 1	Year 2	Year 3	Year 4	Year 5
Government consumption	0.5	0.7	0.3	0.0	0.0
Subsidies and transfers	0.3	0.4	0.2	0.0	0.0
Capital expenditure	0.8	1.0	0.6	0.3	0.0
Tax revenues	-0.3	-0.4	-0.2	0.0	0.0

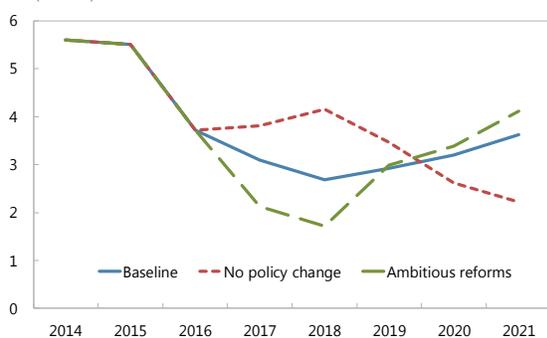
Source: IMF staff estimates of multipliers in oil-exporting countries in the region.

### Real GDP Growth (Percent)



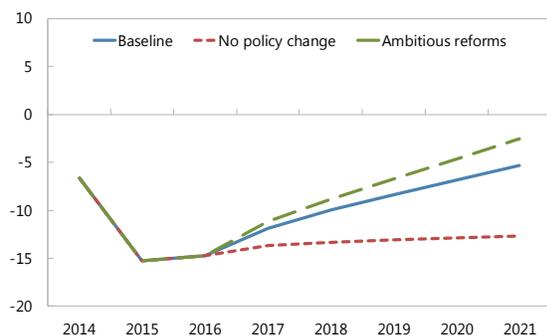
Sources: Algerian authorities; and IMF staff calculations.

### Nonhydrocarbon Growth (Percent)



Sources: Algerian authorities; and IMF staff calculations.

### Fiscal Balance (Percent of GDP)



Sources: Algerian authorities; and IMF staff calculations.

### Overall growth

**No-policy-change:** Growth returns to 3.9 percent in 2018, but declines toward 2.3 percent over the medium term, as large fiscal deficits crowd out private sector credit and lead to a loss in confidence.

**Baseline:** Growth slows gradually under the effects of fiscal consolidation but remains supported by private demand.

**Ambitious reforms:** Growth declines more sharply due to further fiscal consolidation, but then starts to accelerate as structural reforms take hold.

### Nonhydrocarbon growth

In all three scenarios, nonhydrocarbon growth roughly tracks overall growth.

**No-policy-change:** Nonhydrocarbon growth initially accelerates, fueled by expansionary fiscal policy, but later slows.

**Baseline:** Nonhydrocarbon growth slows gradually under the effects of fiscal consolidation before starting to accelerate as reforms take hold.

**Ambitious reforms:** Similar to the baseline, nonhydrocarbon growth initially slows but accelerates after 2018 as reforms take hold.

### Fiscal balance

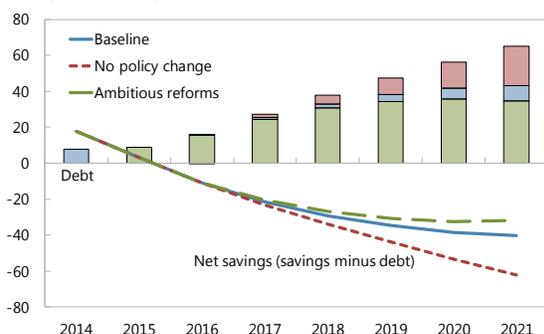
**No-policy-change:** The fiscal deficit remains large over the medium term as interest payments mount.

**Baseline:** Fiscal consolidation leads to a narrowing of the deficit over time.

**Ambitious reforms:** The fiscal deficit approaches equilibrium by 2021 thanks to slower wage growth, additional hydrocarbon and nonhydrocarbon revenues, comprehensive subsidy reform, and faster growth.

### Net Savings and Debt

(Percent of GDP)



Sources: Algerian authorities; and IMF staff calculations.

### Net savings and debt

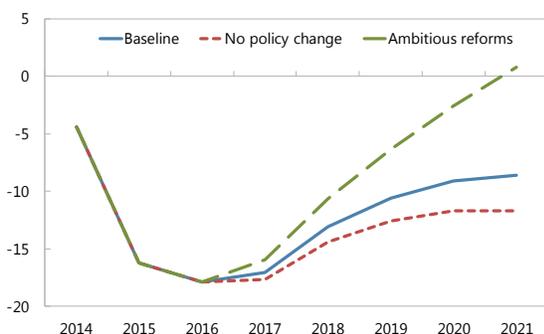
**No-policy-change:** Net savings (negative since 2016) continue to decline, while debt reaches 65 percent of GDP.

**Baseline:** Net savings decline more slowly; debt increases to 43 percent of GDP.

**Ambitious reforms:** Net savings remain negative but begin to increase, and debt begins to decrease by the end of the projection period.

### Current Account

(Percent of GDP)



Sources: Algerian authorities; and IMF staff calculations.

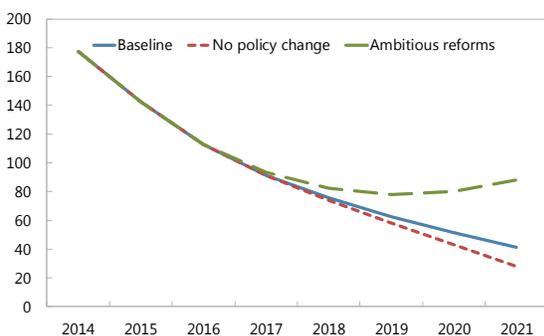
### Current account balance

Current account deficits continue over the medium term in the **no-policy-change** and **baseline** scenarios.

In the **ambitious reform** scenario, however, current account surpluses return by 2021, thanks to fiscal consolidation, subsidy reform (which decreases domestic consumption of hydrocarbons), growth in nonhydrocarbon exports, more FDI, more tourism receipts, and more remittances.

### International Reserves

(US\$ billion)



Sources: Algerian authorities; and IMF staff calculations.

### International reserves

**No-policy-change:** Reserves decline to US\$28 billion by 2021.

**Baseline:** Reserves decline to US\$41 billion (8.6 months of imports) by 2021.

**Ambitious reforms:** Reserves start to accumulate again in 2020 and reach US\$88.1 billion (19.9 months of imports) by 2021.

## Annex II. Public Debt Sustainability Analysis

*In the years leading up to the global financial crisis, Algeria repaid most of its debt and accumulated large fiscal savings, mainly thanks to rising oil prices. Since the crisis, debt levels have remained low, but fiscal savings have been nearly depleted to finance consecutive fiscal deficits. The increase in public spending in the wake of the Arab Spring and more recently the collapse in oil prices have exacerbated the country's fiscal position and prompted the government to begin undertaking fiscal consolidation in 2016. To meet large financing needs over the medium term, the government will need to increase domestic debt issuance and likely resort to external financing. Under the baseline scenario that assumes steady and sustained fiscal consolidation over the medium term, debt levels are projected to remain at manageable levels. Stress tests, however, suggest that financing needs pose risks.*

**Fiscal savings have been nearly depleted, but debt remains low.** In the decade leading up to the global financial crisis, rising oil prices led to surging hydrocarbon revenues. Part of this hydrocarbon windfall was used to pay down external debt, which fell from over 60 percent of GDP in the 1990s to less than 2 percent by 2007. Another part was saved in the *Fonds de Régulation des Recettes* (FRR), Algeria's oil savings fund. Since 2009, Algeria has recorded consecutive fiscal deficits due to increased spending and slumping hydrocarbon production. Since 2014, deficits have been financed essentially by drawing down savings, allowing debt levels to remain low. At end-2015, gross public debt was equal to 9.0 percent of GDP. Savings in the FRR, however, declined from a peak of 43.3 percent of GDP in 2009 to 12.3 percent.

**External debt has continued to decline while domestic debt has started to increase.** Algeria has not borrowed externally since it received its last disbursement from the IMF in 1999. Remaining external debt is mostly on concessional terms and owed to official bilateral creditors. At end-2015, public external debt represented less than 1 percent of GDP. Domestic debt increased from 7.2 percent of GDP in 2014 to 8.2 percent in 2015. Domestic debt consists of Treasury bills and bonds, as well as debt purchased from state-owned enterprises. About half of outstanding Treasury securities have maturities ranging from 5 to 15 years.

**Algeria will need to borrow more to meet large financing needs and preserve some fiscal savings.** Despite the significant fiscal adjustment assumed in the baseline scenario, gross financing needs are large. With savings in the FRR near the statutory floor of DA 740 billion, Algeria will need to increase domestic debt issuance to meet its financing needs. Tighter liquidity conditions imply that domestic borrowing costs will increase. The authorities have announced their intention to issue a domestic bond aimed at mobilizing savings in the informal sector. They have also publicly expressed a willingness to consider limited external borrowing to finance large infrastructure projects. The baseline scenario assumes US\$2-\$4 billion per year in bilateral external borrowing starting in 2016.

**Debt levels are projected to remain manageable in the baseline scenario.** The baseline scenario assumes steady fiscal consolidation over the projection period, with the nonhydrocarbon deficit declining from 37.8 percent of nonhydrocarbon GDP in 2015 to 22.3 percent in 2021. The largest single-year adjustment occurs in 2016, in line with the budget. Thereafter, current spending falls gradually (as a share of GDP), as the wage bill approaches pre-Arab Spring levels, capital spending falls back to 2006 levels, and nonhydrocarbon revenues increase modestly on the assumption of continued subsidy reform and improvements in tax administration. The government is also assumed to benefit from a small rebound in hydrocarbon revenues due to further depreciation of the dinar and a gradual recovery in oil prices. Nevertheless, gross financing needs are large, averaging 15.5 percent of GDP over the period. The government is assumed to draw from the FRR until savings fall to the statutory floor of 740 billion in 2016; thereafter, financing needs are met by domestic and external borrowing. In this scenario, the ratio of debt to GDP increases from 9.0 percent in 2015 to 43.3 percent in 2021.

**Alternative scenarios and stress tests indicate that projected debt levels are resilient to shocks, but gross financing needs pose risks.** Assuming no change in the primary balance (i.e., no fiscal adjustment) beginning in 2016, public debt would increase to 80 percent by 2021—much higher than in the baseline scenario, but only somewhat above the 70 percent benchmark for emerging market countries. However, gross financing needs, already projected to be large, are sensitive to shocks, particularly to real interest rates and the primary balance. The authorities are aware of the financing challenges ahead and are weighing their options. Two provisions in the 2016 budget suggest possible ways forward should the government have difficulty meeting its financing needs. One provision gives the finance minister the power to cut spending via decree in order to rectify budget imbalances; the other opens the door to selling shares in state-owned enterprises.

## Algeria Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

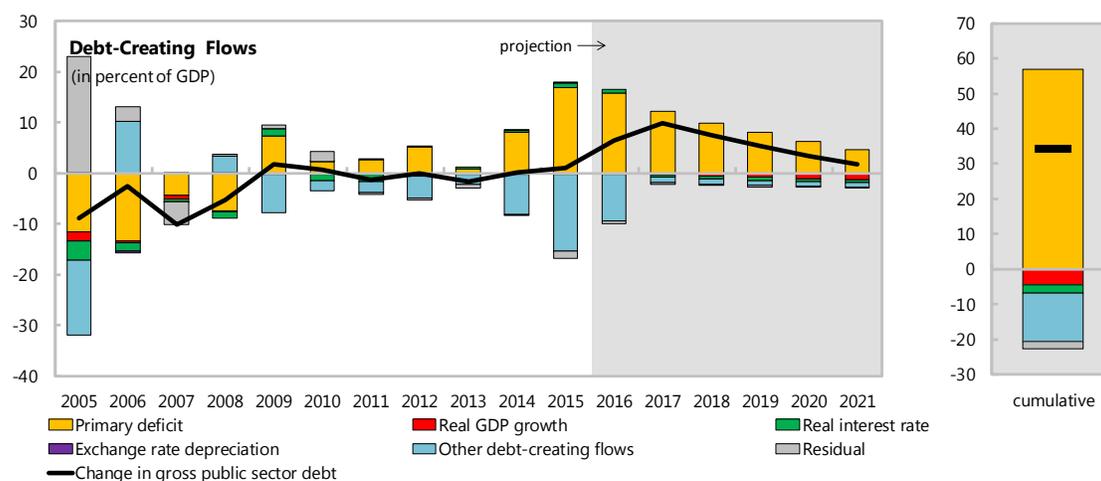
(in percent of GDP unless otherwise indicated)

### Debt, Economic and Market Indicators <sup>1/</sup>

	Actual			Projections						As of April 08, 2016		
	2005-2013 <sup>2/</sup>	2014	2015	2016	2017	2018	2019	2020	2021	Sovereign Spreads	Foreign	Local
Nominal gross public debt	13.3	8.0	9.0	15.4	25.4	32.8	38.1	41.6	43.3	EMBIG (bp) <sup>3/</sup>	n.a.	n.a.
Public gross financing needs	4.4	10.2	18.8	17.8	17.5	17.5	15.4	13.4	11.3	5Y CDS (bp)	n.a.	n.a.
Real GDP growth (in percent)	3.1	3.8	3.9	3.4	2.9	2.6	2.8	3.1	3.4	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	8.7	0.0	-6.0	-2.2	6.9	5.7	5.4	5.2	4.9	Moody's	n.a.	n.a.
Nominal GDP growth (in percent)	12.2	3.4	-2.4	1.1	10.0	8.5	8.4	8.4	8.5	S&Ps	n.a.	n.a.
Effective interest rate (in percent) <sup>4/</sup>	3.6	2.9	3.1	4.7	4.2	3.5	3.4	3.5	3.6	Fitch	n.a.	n.a.

### Contribution to Changes in Public Debt

	Actual			Projections						cumulative	debt-stabilizing primary balance <sup>9/</sup>
	2005-2013	2014	2015	2016	2017	2018	2019	2020	2021		
Change in gross public sector debt	-3.1	0.2	1.0	6.4	9.9	7.5	5.3	3.4	1.7	34.3	
Identified debt-creating flows	-5.6	0.2	2.5	7.0	10.3	7.7	5.5	3.7	1.9	36.1	
Primary deficit	-2.0	8.1	17.0	15.8	12.2	9.9	8.0	6.3	4.6	56.8	-2.7
Primary (noninterest) revenue and gra	38.9	33.0	29.3	26.1	27.4	28.2	28.7	29.1	29.5	169.0	
Primary (noninterest) expenditure	36.8	41.1	46.2	42.0	39.6	38.1	36.7	35.4	34.1	225.8	
Automatic debt dynamics <sup>5/</sup>	-1.4	0.0	0.6	0.3	-0.8	-1.2	-1.5	-1.7	-1.9	-6.8	
Interest rate/growth differential <sup>6/</sup>	-1.4	-0.1	0.4	0.3	-0.8	-1.2	-1.5	-1.7	-1.9	-6.8	
Of which: real interest rate	-1.0	0.2	0.8	0.6	-0.4	-0.5	-0.6	-0.6	-0.6	-2.2	
Of which: real GDP growth	-0.5	-0.3	-0.3	-0.3	-0.4	-0.6	-0.9	-1.1	-1.3	-4.6	
Exchange rate depreciation <sup>7/</sup>	0.0	0.1	0.2	...	...	...	...	...	...	...	
Other identified debt-creating flows	-2.1	-7.9	-15.1	-9.1	-1.1	-1.0	-1.0	-0.9	-0.8	-13.9	
FRR withdrawal (+) or accumulation	2.0	-6.7	-13.9	-7.9	0.0	0.0	0.0	0.0	0.0	-7.9	
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)	-4.2	-1.2	-1.2	-1.3	-1.1	-1.0	-1.0	-0.9	-0.8	-6.0	
Residual, including asset changes <sup>8/</sup>	2.5	0.0	-1.5	-0.6	-0.3	-0.3	-0.2	-0.2	-0.2	-1.8	



Source: IMF staff.

1/ Public sector is defined as central 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  $[(r - \pi(1+g) - g + ae(1+r)] / (1+g+\pi+g\pi)$  times previous period debt ratio, with  $r$  = interest rate;  $\pi$  = 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  $r - \pi(1+g)$  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.

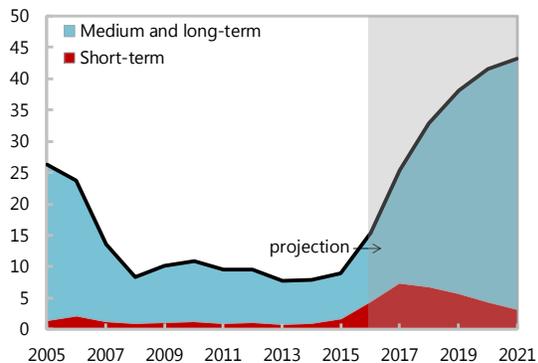
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

### Algeria Public DSA - Composition of Public Debt and Alternative Scenarios

#### Composition of Public Debt

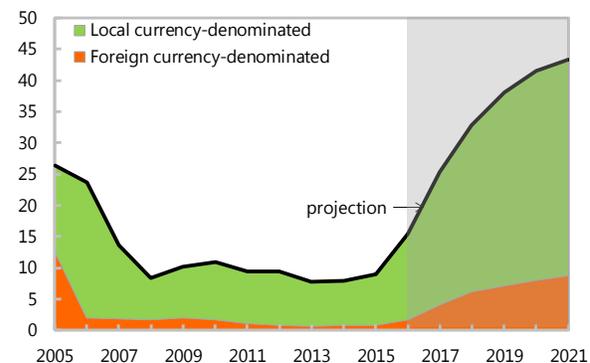
##### By Maturity

(in percent of GDP)



##### By Currency

(in percent of GDP)



#### Alternative Scenarios

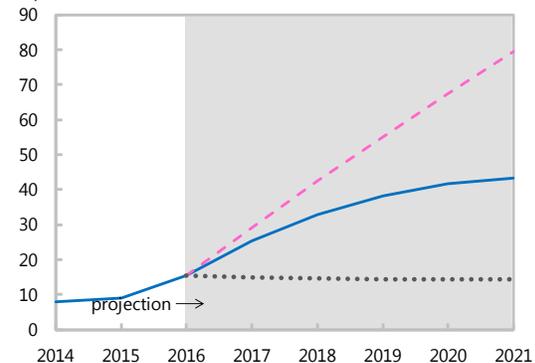
— Baseline

..... Historical

- - - Constant Primary Balance

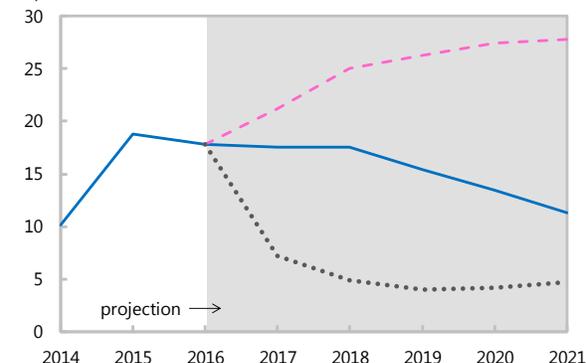
##### Gross Nominal Public Debt

(in percent of GDP)



##### Public Gross Financing Needs

(in percent of GDP)



#### Underlying Assumptions

(in percent)

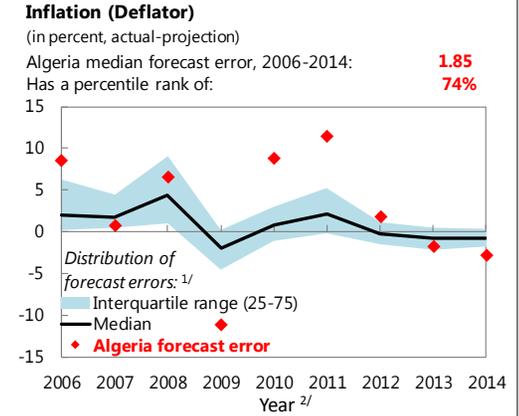
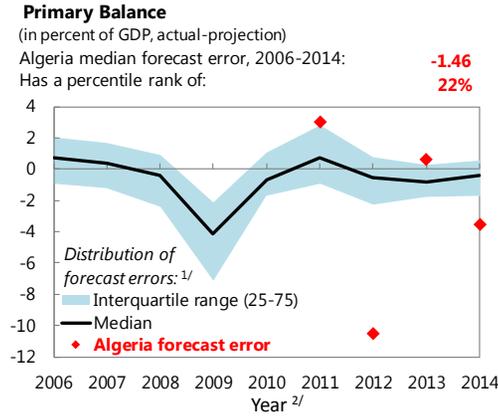
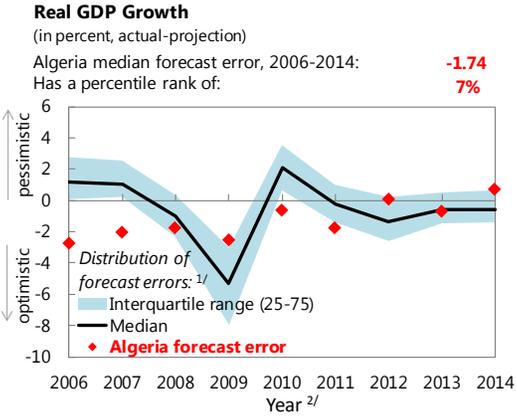
Baseline Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	3.4	2.9	2.6	2.8	3.1	3.4
Inflation (GDP deflator)	-2.2	6.9	5.7	5.4	5.2	4.9
Primary budget balance	-15.8	-12.2	-9.9	-8.0	-6.3	-4.6
Effective interest rate	4.7	4.2	3.5	3.4	3.5	3.6
Constant Primary Balance Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	3.4	2.9	2.6	2.8	3.1	3.4
Inflation (GDP deflator)	-2.2	6.9	5.7	5.4	5.2	4.9
Primary budget balance	-15.8	-15.8	-15.8	-15.8	-15.8	-15.8
Effective interest rate	4.7	4.2	3.3	3.2	3.3	3.4

Historical Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	3.4	2.9	2.9	2.9	2.9	2.9
Inflation (GDP deflator)	-2.2	6.9	5.7	5.4	5.2	4.9
Primary budget balance	-15.8	-1.8	-1.8	-1.8	-1.8	-1.8
Effective interest rate	4.7	4.2	4.0	3.9	3.9	3.9

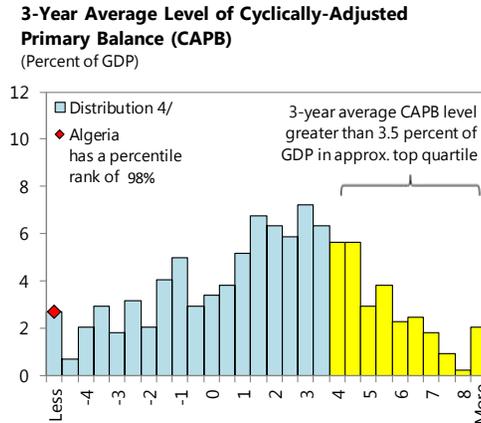
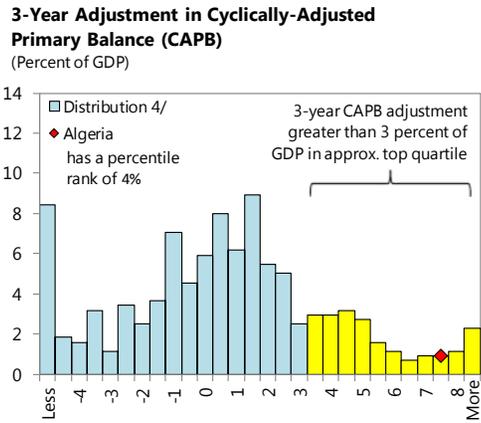
Source: IMF staff.

### Algeria Public DSA - Realism of Baseline Assumptions

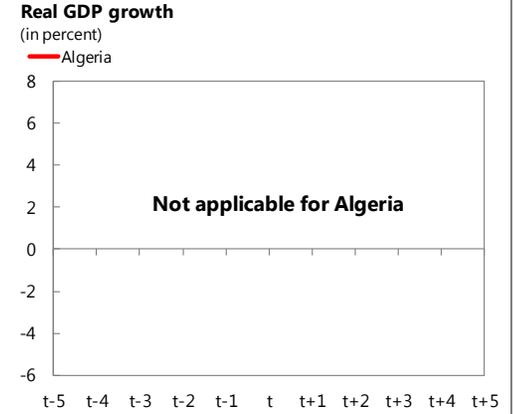
#### Forecast Track Record, versus all countries



#### Assessing the Realism of Projected Fiscal Adjustment



#### Boom-Bust Analysis<sup>3/</sup>



Source : IMF Staff.

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

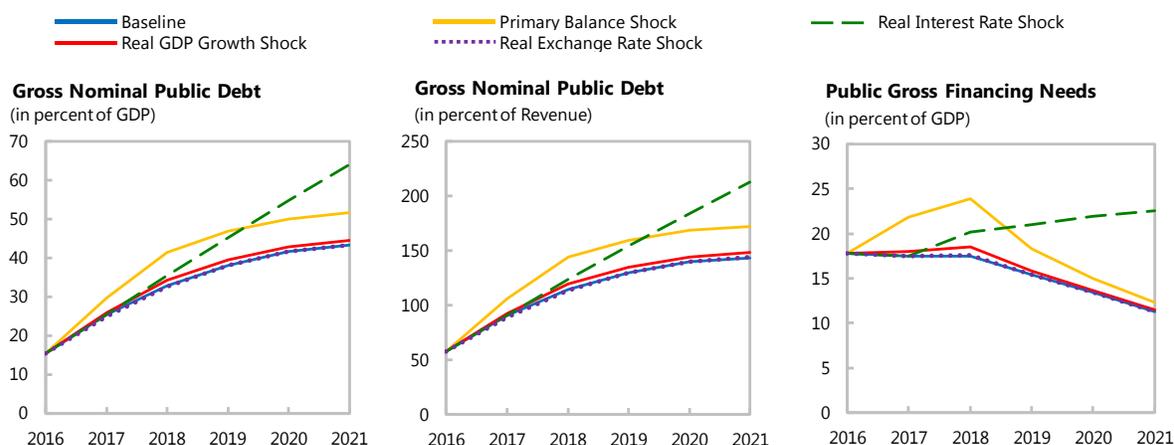
2/ Projections made in the spring WEO vintage of the preceding year.

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

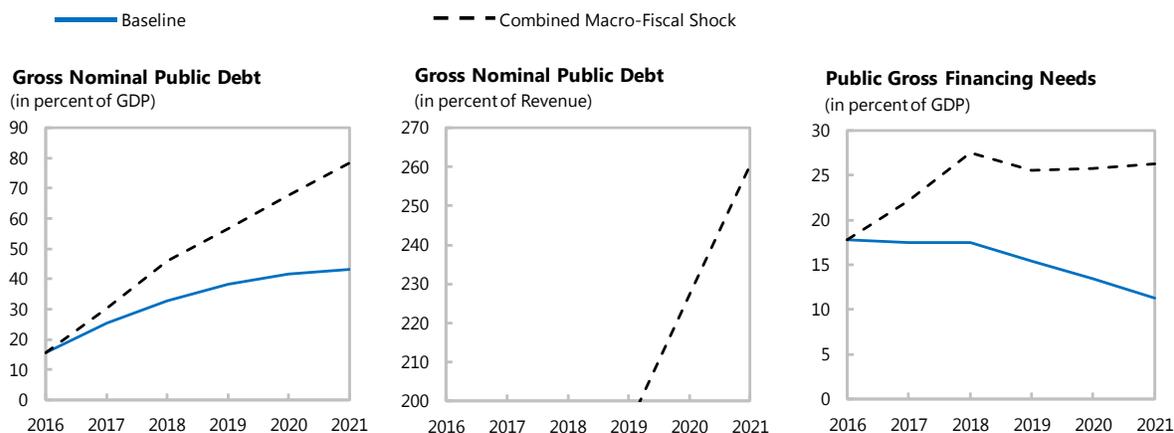
4/ Data cover annual observations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.□

## Algeria Public DSA - Stress Tests

## Macro-Fiscal Stress Tests



## Additional Stress Tests



## Underlying Assumptions

(in percent)

	2016	2017	2018	2019	2020	2021		2016	2017	2018	2019	2020	2021
<b>Primary Balance Shock</b>							<b>Real GDP Growth Shock</b>						
Real GDP growth	3.4	2.9	2.6	2.8	3.1	3.4	Real GDP growth	3.4	2.1	1.8	2.8	3.1	3.4
Inflation	-2.2	6.9	5.7	5.4	5.2	4.9	Inflation	-2.2	6.7	5.5	5.4	5.2	4.9
Primary balance	-15.8	-16.5	-14.2	-8.0	-6.3	-4.6	Primary balance	-15.8	-12.6	-10.7	-8.0	-6.3	-4.6
Effective interest rate	4.7	4.2	4.1	4.1	3.9	3.9	Effective interest rate	4.7	4.2	3.5	3.5	3.5	3.6
<b>Real Interest Rate Shock</b>							<b>Real Exchange Rate Shock</b>						
Real GDP growth	3.4	2.9	2.6	2.8	3.1	3.4	Real GDP growth	3.4	2.9	2.6	2.8	3.1	3.4
Inflation	-2.2	6.9	5.7	5.4	5.2	4.9	Inflation	-2.2	14.6	5.7	5.4	5.2	4.9
Primary balance	-15.8	-12.2	-9.9	-8.0	-6.3	-4.6	Primary balance	-15.8	-12.2	-9.9	-8.0	-6.3	-4.6
Effective interest rate	4.7	4.2	14.9	17.1	18.4	19.5	Effective interest rate	4.7	4.6	3.6	3.5	3.5	3.6
<b>Combined Shock</b>													
Real GDP growth	3.4	2.1	1.8	2.8	3.1	3.4							
Inflation	-2.2	6.7	5.5	5.4	5.2	4.9							
Primary balance	-15.8	-16.5	-14.2	-8.0	-6.3	-4.6							
Effective interest rate	4.7	4.6	15.7	17.7	18.8	19.7							

Source: IMF staff.

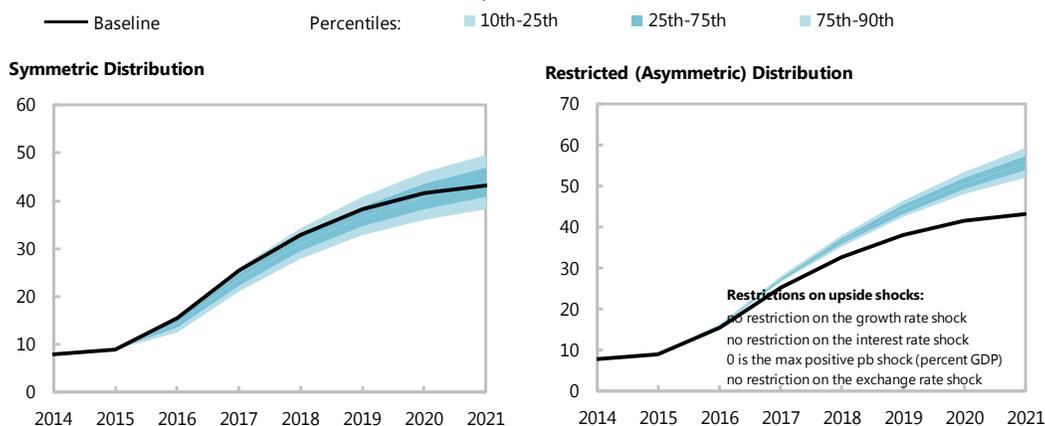
### Algeria Public DSA Risk Assessment

#### Heat Map

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

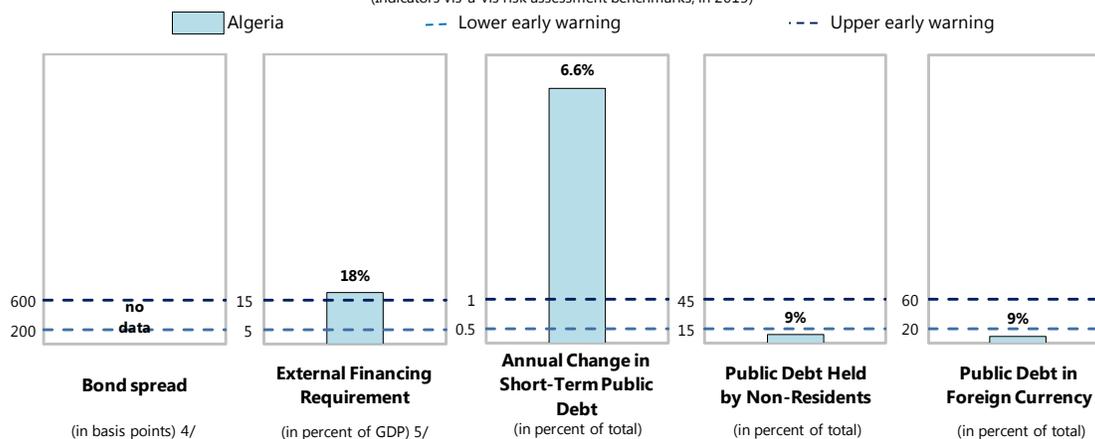
#### Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



#### Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2015)



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, 09-Jan-16 through 08-Apr-16.

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.

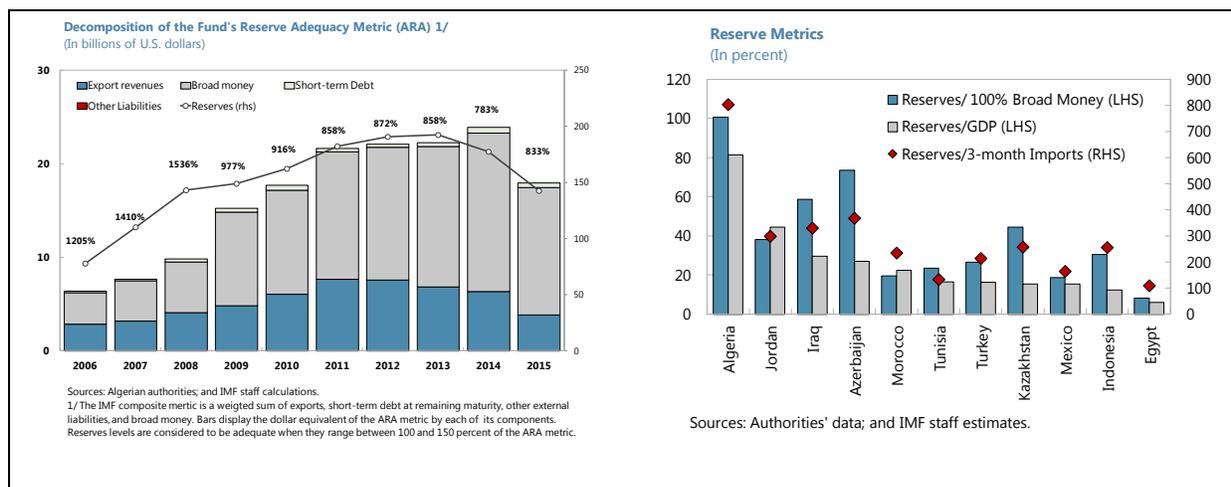
## Annex III. External Sector Assessment

The collapse in oil prices has substantially weakened Algeria's external position. The current account registered a deficit in 2014 for the first time since 1998, and large deficits are projected over the medium term. Reserves remain comfortably above adequacy ratios but are declining rapidly. External debt is low but is expected to increase as the government considers options for meeting its large fiscal financing needs. External assessment methods point to a substantial current account gap, consistent with the dinar remaining significantly overvalued despite some depreciation last year.

**Algeria's current account declined markedly in recent years with the plunge in international oil prices.** Hydrocarbon exports have halved since 2013, mostly reflecting a decline in oil prices. Although nonhydrocarbon exports have slightly increased, their share in total exports remains minimal. Over the medium term, imports are projected to decline somewhat, but nonhydrocarbon exports are expected to remain weak. As a result, the current account deficit is projected to widen from 4.4 percent of GDP in 2014 to 17.9 percent of GDP in 2016 before starting to narrow as hydrocarbon exports eventually recover and fiscal consolidation compresses imports.

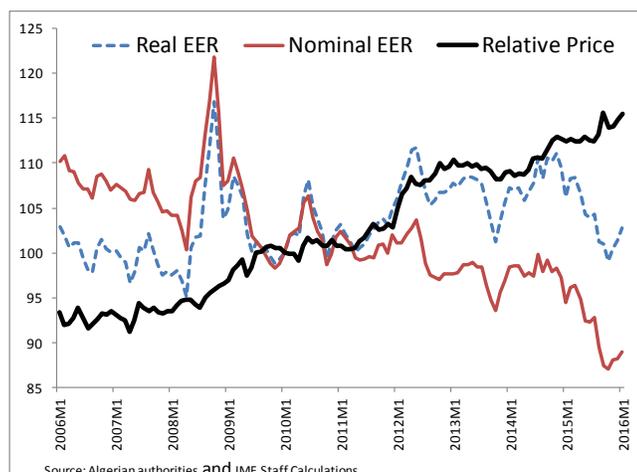
**Algeria's external buffers are still sizeable but are vulnerable to durably low oil prices.**

Although international reserves stood at US\$143 billion at end-2015, equivalent to 30 months of imports and 113 percent of broad money, they fell by US\$35 billion, or 19.6 percent, in 2015 alone. At-end 2015, reserves stood at 833 percent of the IMF composite metric. Staff projects that Algeria's international reserves will fall to US\$41 billion by 2021, or 210 percent of the ARA metric, on current assumptions of oil prices remaining low. External debt stood at 3 percent of GDP at end 2015 but the government is expected to increase its external borrowing to finance the deficit.



### The real effective exchange rate (REER) trended higher after 2011 but weakened in 2015.

Despite rising relative prices, the REER fell back to levels last seen in 2010-11 due to a significant depreciation of the nominal effective exchange rate (NEER). Although the dinar depreciated by 25 percent against the dollar, the REER and NEER depreciated by only 4.3 and 6.7 percent respectively due to the increase in Algeria's price levels relative to its trading partners. The foreign exchange premium on the parallel market reportedly stands at around 50 percent.



### The real exchange rate assessment is based on two methodologies:

- The EBA-lite's current account (CA) model estimates the country's current account norm based on non-policy fundamentals, cyclical factors, and policy variables. The current account gap is calculated as the difference between the calculated current account norm and the actual current account. Assuming that the exchange rate is the only instrument to bring the actual current account to its norm, the misalignment is derived using the current account elasticity.
- The EBA-lite's external sustainability (ES) model focuses on the relationship between the sustainability of a country's net external assets position, its current account, and the real exchange rate. In this approach, assuming a benchmark for the net international investment position (IIP), the model calculates the current account balance that would need to prevail over the medium term.

### Estimates based on the EBA-lite methodologies suggest that the current account balance remains well below the norm for 2015, pointing to a significant overvaluation of the REER.

- According to the CA approach, the current account is weaker than the value consistent with medium-term fundamentals and desirable policies. Depending on assumptions for desirable policies, the current account norm ranges between -4.2 percent and -6.3 percent of GDP, yielding respectively a current gap between -12.0 and -9.9 percent of GDP in 2015. The factors that contribute the most to the gap are domestic demand and fiscal policy. Closing the current account gap requires primarily pursuing fiscal consolidation and fostering export diversification through structural reforms, while greater exchange rate flexibility would support these efforts.
- The ES approach also suggests that the REER was significantly overvalued in 2015. Assuming the IIP remains stable at its 2015 level of 80 percent of GDP, the current account norm would be 2 percent of GDP, implying a gap of -10.6 percent over the medium term. When the IIP is

stabilized at its projected level in 2021, i.e., 5.6 percent of GDP, the current account norm would be -0.4 percent of GDP, yielding a smaller gap of -8.2 percent of GDP.

- Under the assumptions underpinning staff's baseline scenario, the above current account gaps would correspond to a degree of REER overvaluation in the 60-80 percent range. However, these estimates are subject to significant uncertainty as the magnitude and persistence of the terms-of-trade shock make the results of standard methodologies unstable: minor changes in underlying assumptions (e.g., regarding trade elasticities, desirable policies, or target IIP) lead to significant variations in the degree of estimated overvaluation. Furthermore, the results should not be interpreted as the needed nominal exchange rate adjustment to restore current account balance. As noted above, the primary levers to bring the REER closer to fundamentals should be fiscal consolidation and structural reforms while greater exchange rate flexibility can help support these efforts.

<b>EBA-Lite Estimates of CA Gap</b> (Percent of GDP)			
	Current Account Norm	Underlying Current Account in 2015	Current Account Gap
EBA-lite CA			
Scenario 1: Baseline scenario 1/	-6.3	-16.2	-9.9
Scenario 2: Ambitious scenario 2/	-4.2	-16.2	-12.0
EBA-lite ES			
		Underlying Current Account in 2021	
Scenario 1: Stabilizing net IIP at current level	2.0	-8.6	-10.6
Scenario 2: Stabilizing net IIP at 2021 projected level	-0.4	-8.6	-8.2
1/ The cyclically-adjusted fiscal balance is set to its average value over the baseline scenario horizon.			
2/ The cyclically-adjusted fiscal balance is calibrated such that debt/GDP is stabilized by 2021.			

**Table 1. External Sustainability Assessment**

<p><b>Current account</b></p>	<p><b>Background:</b> Hydrocarbon exports fell by nearly half in 2015, resulting in a widening of the current account deficit to US\$27.0 billion (16.2 percent of GDP) from US\$9.4 billion in 2014 (4.4 percent of GDP). The deficit is expected to narrow over the medium term as a result of policy action and some recovery in the oil prices.</p> <p><b>Assessment:</b> The EBA-lite CA model yields a current account gap of around 10-12 percent of GDP at end-2015, while the ES approach suggests a current account gap between 4-6 percent of GDP. Fiscal consolidation combined with structural reforms and further exchange rate depreciation would help to close the gap.</p>	<p><b>Overall assessment:</b> Algeria's external position has weakened significantly since the onset of the oil price shock. A large current account gap implies that the REER is significantly overvalued. Reserves remain adequate but could be depleted in the absence of adjustment.</p> <p><b>Potential policy responses:</b> Fiscal consolidation would help to mitigate the impact of the oil price shock on the external position. Structural reforms are needed to foster export diversification in the medium and long-term. Further exchange rate flexibility would help to reduce the current account gap and bring the REER in line with its equilibrium value.</p>
<p><b>Real effective exchange rate (REER)</b></p>	<p><b>Background:</b> Banque d'Algérie targets the equilibrium value of the REER. The REER depreciated for most of 2015 before strengthening somewhat at the end of the year.</p> <p><b>Assessment:</b> Despite the depreciation of the REER in 2015, the EBA CA and ES approaches suggest that the REER remains significantly overvalued.</p>	
<p><b>Capital and financial accounts</b></p>	<p>Capital flows are minimal due to multiple restrictions, including restrictions on external financing. FDI is small and is concentrated in the hydrocarbon sector.</p>	
<p><b>Reserve Position</b></p>	<p><b>Background:</b> Reserves peaked at US\$192 billion in 2013. Since then, reserves have declined by 26 percent and stood at US\$142.6 billion at end-2015, equal to 2½ years of imports.</p> <p><b>Assessment:</b> Despite their rapid decline, reserves remain more than adequate, equal to 833 percent of the IMF composite metric.</p>	
<p><b>Foreign assets and liabilities position and trajectory</b></p>	<p><b>Background:</b> Algeria's NIIP at end-2015 was 79.6 percent of GDP. Liabilities are negligible compared to assets, which are dominated by foreign reserves. Portfolio investments do not exist as either assets or liabilities.</p> <p><b>Assessment:</b> Since the stock of debt and FDI is small, the NIIP trajectory is similar to the path of foreign reserves. Under the baseline scenario that assumes some adjustment, the NIIP is sustainable over the medium term.</p>	

**Table 2. Algeria: External Debt Sustainability Framework, 2011–21**  
(Percent of GDP, unless otherwise indicated)

	Actual					Projections							Debt-stabilizing non-interest current account 6/ -1.9
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021		
<b>1 Baseline: External debt</b>	2.2	1.7	1.6	1.7	1.8	<b>2.8</b>	<b>4.9</b>	<b>6.8</b>	<b>7.7</b>	<b>8.5</b>	<b>9.2</b>		
2 Change in external debt	-1.3	-0.5	-0.1	0.1	0.1	0.9	2.1	2.0	0.8	0.8	0.7		
3 Identified external debt-creating flows (4+8+9)	-11.6	-6.7	-1.3	3.7	17.1	16.7	15.5	11.3	8.5	6.8	6.1		
4 Current account deficit, excluding interest payments	-10.0	-6.0	-0.4	4.4	16.2	17.6	16.6	12.5	10.0	8.5	8.0		
5 Deficit in balance of goods and services	-9.6	-6.2	-1.2	3.7	15.1	18.6	17.3	13.1	10.4	8.8	8.1		
6 Exports	38.4	36.2	32.6	29.8	23.0	17.2	19.2	20.3	21.0	21.6	22.0		
7 Imports	28.8	30.0	31.4	33.4	38.2	35.8	36.4	33.4	31.5	30.4	30.1		
8 Net non-debt creating capital inflows (negative)	-1.0	-0.7	-0.9	-0.7	0.4	-0.9	-1.1	-1.3	-1.5	-1.7	-2.0		
9 Automatic debt dynamics 1/	-0.6	0.0	0.0	0.0	0.5	0.0	0.1	0.1	0.1	0.1	0.0		
10 Contribution from nominal interest rate	0.1	0.1	0.0	0.0	0.0	0.1	0.2	0.2	0.3	0.3	0.3		
11 Contribution from real GDP growth	-0.1	-0.1	0.0	-0.1	-0.1	-0.1	-0.1	-0.1	-0.2	-0.2	-0.3		
12 Contribution from price and exchange rate changes 2/	-0.6	0.0	0.0	0.0	0.6	...	...	...	...	...	...		
13 Residual, incl. change in gross foreign assets (2-3) 3/	10.3	6.2	1.2	-3.5	-17.1	-15.8	-13.4	-9.3	-7.7	-6.0	-5.3		
External debt-to-exports ratio (in percent)	5.7	4.8	5.0	5.9	7.9	16.0	25.3	33.7	36.4	39.2	41.7		
<b>Gross external financing need (in billions of US dollars) 4</b>	-16.9	-10.3	0.8	11.0	29.4	30.3	30.9	25.1	21.0	18.8	18.4		
in percent of GDP	-8.5	-4.9	0.4	5.1	17.6	10-Year 18.8	10-Year 18.4	14.4	11.7	10.1	9.6		
<b>Scenario with key variables at their historical averages 5/</b>						<b>2.8</b>	<b>-18.8</b>	<b>-35.2</b>	<b>-49.4</b>	<b>-61.3</b>	<b>-72.1</b>	<b>1.4</b>	
<b>Key Macroeconomic Assumptions Underlying Baseline</b>						Historical Average	Standard Deviation						
Real GDP growth (in percent)	2.8	3.3	2.8	3.8	3.9	2.9	0.8	3.4	2.9	2.6	2.8	3.1	3.4
GDP deflator in US dollars (change in percent)	20.3	0.9	-2.3	-1.5	-24.8	3.2	16.3	-6.8	1.8	0.7	0.4	0.1	-0.1
Nominal external interest rate (in percent)	3.5	5.9	1.5	0.8	2.0	2.9	1.5	3.5	6.0	4.6	4.1	4.0	3.8
Growth of exports (US dollar terms, in percent)	26.3	-1.2	-9.8	-7.0	-39.6	1.1	25.9	-27.8	16.6	9.1	7.1	6.0	5.4
Growth of imports (US dollar terms, in percent)	13.0	9.1	4.9	8.6	-10.8	11.0	16.7	-9.6	6.7	-5.4	-2.6	-0.4	2.5
Current account balance, excluding interest payments	10.0	6.0	0.4	-4.4	-16.2	7.2	13.0	-17.6	-16.6	-12.5	-10.0	-8.5	-8.0
Net non-debt creating capital inflows	1.0	0.7	0.9	0.7	-0.4	1.0	0.6	0.9	1.1	1.3	1.5	1.7	2.0

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 d

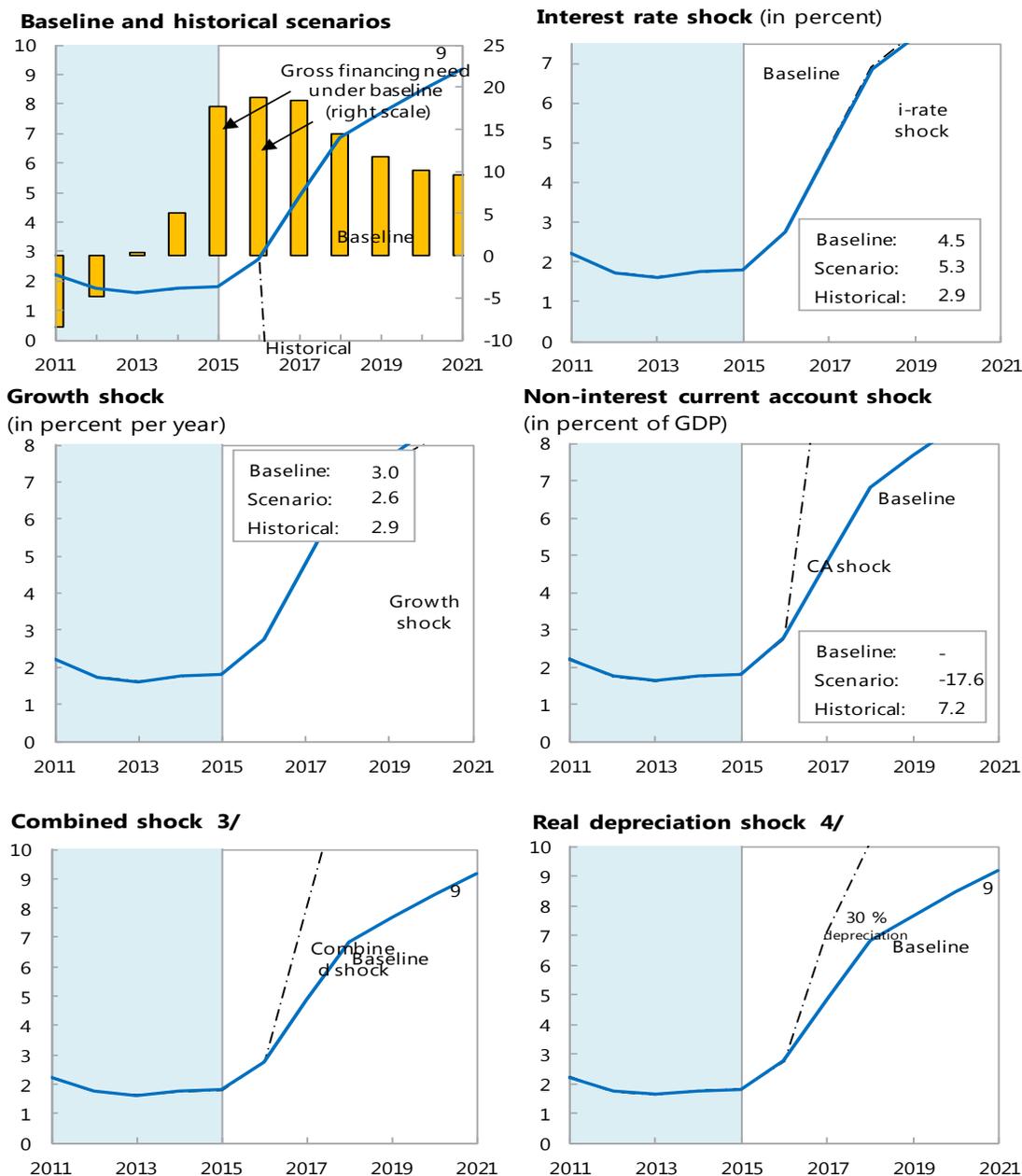
3/ For projection, line includes the impact of price and exchange rate changes.

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 1. 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 2010.

## Annex IV. Authorities' Response to Past IMF Recommendations

The authorities generally agree with staff's broad recommendations, but their views about implementation have differed. Insufficient action was taken in 2015 in response to the oil price shock, but the 2016 budget calls for significant fiscal consolidation, and the authorities have initiated subsidy reform. The Banque d'Algérie has allowed the dinar to depreciate against the dollar, but the real exchange rate remains overvalued. With technical assistance from the IMF, the authorities have taken steps to improve tax administration, enhance the banking regulatory framework, and strengthen liquidity management and forecasting. However, little progress was seen on structural reforms that would increase economic openness and reduce the state's control over the economy.

### Implementation Status of the 2014 Article IV Recommendations

Recommendation	Implementation status
<b>Consolidate macroeconomic and financial stability</b>	
Adopt a full-fledge fiscal rule	The authorities are preparing a new organic budget law that is expected to include a fiscal rule.
Undertake fiscal consolidation	The authorities took little action to contain the fiscal deficit in 2015, other than to freeze public sector hiring. The 2016 budget, however, calls for a 9 percent nominal reduction in spending and a 4 percent increase in tax revenues.
Gradually phase out subsidies and develop a targeted cash-transfer system	The authorities have initiated subsidy reform by raising the prices of fuel, electricity, and natural gas.
Avoid a deviation of the dinar from its equilibrium value.	The real effective exchange rate depreciated somewhat in 2015 but remains significantly overvalued.
Strengthen public financial management	The authorities are moving toward adopting a medium-term budget framework and program budgeting.
Preserve the stability of the financial sector	The central bank is working on better aligning its regulatory and supervisory framework with international standards and implementing the 2013 FSAP recommendations, including expanding the credit registry to include households.
<b>Ensure external stability</b>	
Relax FDI restrictions	The 51/49 rule is being taken out of the investment code so it can be more easily amended through budget laws in the future.
Remove trade restrictions	The authorities have tightened import restrictions.
<b>Accelerating economic growth and job creation</b>	
Develop the financial sector	A ban on consumer lending was lifted.
Improve the business environment	Recent measures taken with technical assistance from the World Bank have not yet been reflected in the Doing Business ranking.

## Annex V. Implementation of FSAP Recommendations

Recommendation	Responsible	Timeline	Implementation
<b>Leverage hydrocarbon revenue for financial sector development:</b> Improve intergenerational smoothing of hydrocarbon revenue (full-fledged fiscal rule, sovereign wealth fund (SWF)).	BA/MoF	MT-LT	Partial progress. The authorities are working on a revision of the organic budget law that aims to include a fiscal rule that ties current spending to nonhydrocarbon revenues.
<b>Exchange controls:</b> Gradually reduce restrictive measures on foreign exchange transactions.	BA/MoF	MT-LT	No progress.
<b>FX market:</b> Allow nonhydrocarbon exporters to sell directly into the foreign exchange market, to stimulate its development, including for forward contracts	BA	ST	No progress. An MCM technical assistance (TA) mission helped identify the TA needs for the development of FX markets.
<b>Liquidity management:</b> Create a structural liquidity shortage to facilitate monetary policy implementation.	BA	ST	Partial progress: Excess liquidity is being reduced notably by the impact of lower oil prices. The BA continued to absorb excess liquidity using term deposit facilities, taking into account the government's debt issuance plans. The BA is also strengthening its liquidity forecasting capacity.
<b>Emergency liquidity facility assistance (ELA).</b> Clarification of the emergency liquidity assistance framework	BA	ST	Partial progress. In July 2015, the BA published a regulation defining the framework for discount operations and outright loans.
<b>SOB reform:</b> Complete corporate governance reform agenda	MoF	ST-MT	No progress. A governance improvement program is being prepared with the support of the World Bank.
<b>Consumer lending:</b> Replace consumer lending restrictions with prudential measures; introduce an effective public credit registry for households, and introduce a personal bankruptcy framework.	BA	MT	Partial progress. The credit registry was extended to individuals. The ban on consumer lending was lifted. No progress on personal bankruptcy.
<b>Banking supervision:</b> Facilitate the write-off of NPLs; improve the operational framework for supervision; continue moving toward Basel II/III standards; improve macroprudential oversight; develop stress-test expertise; introduce consolidated supervision.	BA	ST-MT	Partial progress. New regulations on capital adequacy related to pillar I of Basel II and elements of Basel III were introduced in 2014. The BA introduced a number of liquidity instruments (minimum liquidity and transformation ratios) to manage liquidity risks. Loan classification requirements were strengthened to cover the treatment of overdraft and restructured loans. New regulations allow fully-provisioned, small NPLs to be

			written off. The BA is currently conducting its first macro stress test exercise. No progress on writing off the current NPL stock. The BA has prepared a draft regulation on consolidated supervision, but the current supervisory assessment is still conducted on a standalone basis.
<b>Small and medium-sized enterprise (SME) lending:</b> Revisit existing government support programs for microenterprises and SMEs, including partial credit guarantee funds.	MoF	MT	No progress.
<b>Insurance:</b> Adapt MTPL premiums and reduce compulsory reinsurance.	Insurance Dir.	MT	No progress.
<b>Insolvency regime:</b> Modernize the insolvency regime to mitigate risk and strengthen the credit environment.	MoJ, MoF	MT	No progress.
<b>Collateral regime:</b> Improve debt enforcement procedures.	MoJ, MoF	ST–MT	No progress.
<b>Criminal sanctions:</b> Clarify Criminal Code sanctions on mismanagement of funds in state-owned enterprises (SOEs), with judicial training on implementation.	MoJ	ST	No progress. However, the September 2014 tripartite meeting agreed on the principle of lifting the criminal sanctions for management errors.
<b>Payment systems:</b> Set up a payment system council to monitor the modernization of payment systems and formalize a plan to decrease the proportion of fiduciary money in M2.	BA	MT	Partial progress. A system is in place for the development of electronic payments, and a draft law on electronic certification has been adopted.
<b>Capital market development:</b> Finance budget deficits through the issuance of t-bonds along the yield curve and revisit the issuance policy at the MoF to foster liquidity.	MoF	ST-MT	Partial progress. Positive net t-bill and t-bond issuances in 2015.
<b>Stock exchange:</b> Implement the modernization program set-up by the COSOB in 2012.	COSOB/MoF	LT	Partial progress. Training programs were established for professionals hired since 2014. A new regulation governing stock market traders was issued. Information systems are being upgraded. The COSOB approved capital opening for one SOE.
<b>Crisis management:</b> Establish (i) special resolution regime (SRR) for failing financial institutions; (ii) memorandum of understanding (MoU) outlining principles for financial crisis management; and (iii) MoU between safety net participants on information exchange and decision-making processes.	BA, MoF	LT ST	No progress.



# ALGERIA

## STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

April 29, 2016

Prepared By

The Middle East and Central Asia Department  
(In collaboration with other departments)

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## RELATIONS WITH THE FUND

(As of March 31, 2016)

**Membership Status:** Joined: September 26, 1963; Article VIII.

### General Resources Account

	SDR Million	Percent Quota
Quota	1,959.90	100.00
IMF's holding of currency (holdings rate)	1,771.82	90.40
Reserve tranche position	188.08	9.60

### SDR Department

	SDR Million	Percent Allocation
Net cumulative allocation	1,198.18	100.00
Holdings	898.59	75.00

### Outstanding Purchases and Loans

None

### Financial Arrangements (In millions of SDR)

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
EFF	5/22/1995	5/21/1998	1,169.28	1,169.28
Stand-by	5/27/1994	5/22/1995	457.20	385.20
Stand-By	6/03/1991	3/31/1992	300.00	225.00

### Projected Obligations to Fund

(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2016	2017	2018	2019	2020
Principal	0.00	0.00	0.00	0.00	0.00
Charges/interest	0.13	0.17	0.17	0.17	0.17
Total	0.13	0.17	0.17	0.17	0.17

**Implementation of HIPC Initiative: Not Applicable.**

## Exchange Rate Arrangement

1. From January 21, 1974 to October 1, 1994, the exchange rate of the dinar was determined on the basis of a fixed relationship with a basket of currencies, adjusted from time to time. On October 1, 1994, the Bank of Algeria introduced a managed float for the dinar through daily fixing sessions that included six commercial banks. This system has been replaced by an interbank foreign exchange market as of January 2, 1996. On April 15, 2016, the average of the buying and selling rates for the U.S. dollar was US\$ 1 = DZD 108.96, equivalent to SDR 1 = DZD 153.15. No margin limits are imposed on the buying and selling exchange rates in the interbank foreign exchange market, except for a margin of DA 0.015 between the buying and selling rates of the Bank of Algeria for the dinar against the U.S. dollar.

2. The *de jure* exchange rate arrangement is managed floating and the *de facto* exchange regime is classified as other managed arrangement with no preannounced path for the exchange rate. Algeria maintains an exchange system free from restrictions on the making of payments and transfers for current international transactions.

## Article IV Consultation

The last Article IV consultation was concluded by the Executive Board on December 1, 2014 (IMF Country Report 14/341). The discussions for the 2016 Article IV consultation were held in Algiers from March 1 to March 14, 2016.

## Technical Assistance

STA	Monetary and financial statistics and financial stability indicators	April 2012
MCM	Banking supervision, macro-prudential policy and monetary policy	September 2012
FAD	Public financial management	September 2012
FAD	Subsidy reform	March 2013
FAD	Tax policy	November 2013
MCM	Bank supervision	December 2013
FAD	Tax administration	April 2014
STA	International investment position statistics	September 2014
MCM	Foreign exchange market development	September 2014
FAD	Multiyear budgeting	September 2014
FAD	Tax policy	January 2015
MCM	Interbank financial market development	February 2015
FAD	Organic budget law	April 2015
FAD	Tax administration	April 2015
MCM	Management of foreign exchange reserves	April 2015
RES	Macro-modeling	May 2015
MCM	Macroprudential policies and financial stability	July 2015
MCM	Liquidity management, monetary operations, and interbank market developments	September 2015

## ALGERIA

MCM	Enhancing bank regulation and supervision	November 2015
FAD	Tax and customs administration	November 2015
MCM	Setting up a liquidity committee	December 2015
MCD	Stress testing banks	December 2015
FAD	Tax administration	February 2016
MCM	Financial stability and macroprudential policy framework	April 2016

### **Financial Sector Assessment Program**

Algeria first participated in the FSAP in 2003. The FSAP was updated in 2007 and in 2013. The Executive Board discussed the Financial System Stability Assessment on January 24, 2014 (IMF Country Report No. 14/161).

### **Resident Representative/Advisor**

None.

# RELATIONS WITH THE WORLD BANK GROUP

## JMAP Implementation, FY16

(As of April 20, 2016)

Title	Products	Provisional timing of missions	Expected delivery date
<b>A. Mutual Information on Relevant Work Programs</b>			
Bank work program in next 12 months	<p>a. <b>Sector work</b></p> <ul style="list-style-type: none"> <li>• Algeria Vision 2035</li> <li>• Policy Notes on Subsidies and Social Programs Reform</li> </ul> <p>b. <b>Technical assistance</b></p> <ul style="list-style-type: none"> <li>• AGID: Capacity Building in Integrated Desert Management</li> <li>• ANGEM: Strengthening capacities for M&amp;E and Impact Evaluation of Programs</li> <li>• ADS: Strengthening capacities for M&amp;E an Impact Evaluation of Programs</li> <li>• BA: Stress Tests</li> <li>• BA: Training of On-sites Inspectors</li> <li>• MPT: Broadband Strategy Phase I</li> <li>• BA: Modernization of Public Credit Registry</li> <li>• Support to the National Doing Business Committee</li> <li>• BA: Governance of State-Owned Banks</li> <li>• MADR: Integrated Value Chain in Agriculture</li> </ul>	<p>June 2016</p> <p>June 2016</p>	<p>March 2017</p> <p>March 2017</p> <p>October 2017</p> <p>June 2017</p> <p>June 2016</p> <p>March 2017</p> <p>March 2017</p> <p>August 2016</p> <p>December 2016</p> <p>June 2016</p> <p>September 2016</p> <p>December 2017</p>
IMF work program in next 12 months	<p>Staff visit</p> <p>Staff visit</p> <p>2017 Article IV consultation</p> <p>Continued technical assistance expected in the following areas:</p>	<p>July 2016</p> <p>October 2016</p> <p>March 2017</p>	<p>May 2017</p>

	<ul style="list-style-type: none"> <li>• Liquidity management</li> <li>• Public financial management</li> <li>• Tax administration</li> <li>• Debt management</li> <li>• Macroprudential policy</li> <li>• Bank supervision and regulation</li> </ul>		
<b>B. Requests for Work Program Inputs</b>			
Fund request to Bank	<p>Analysis related to subsidy reform</p> <p>Sectoral analysis</p>	<p>As needed</p> <p>As needed</p>	
Bank request to Fund	<p>Assessment of macroeconomic stance and prospects</p> <p>Data sharing</p>	<p>Semiannual (and on ad hoc basis if requested)</p> <p>Ongoing</p>	Following Article IV and staff visits
<b>C. Agreement on Joint Products and Missions</b>			
Joint products in next 12 months	Continuous close coordination on the reform agenda	Ongoing	

## STATISTICAL ISSUES

<b>I. Assessment of Data Adequacy for Surveillance</b>	
<b>General:</b> Data provision has some shortcomings, but is broadly adequate for surveillance.	
<b>National Accounts:</b> Following STA recommendations, the NSO compiles annual national accounts (ANA) at prior year prices. The ANA broadly follow the 1993 SNA recommendations, but nonprofit institutions serving households are not taken into account. The NSO started publishing quarterly national accounts in 2015.	
<b>Price Statistics:</b> Data are published with a delay of less than one month.	
<b>Government finance statistics:</b> Key shortcomings include insufficient institutional coverage (coverage is limited to Budgetary Central Government, albeit in a wide sense, including the general budget, the annexed budget, and the special treasury accounts), classification problems, long lags for production of statistics, and lack of reconciliation of financing with the monetary accounts. Key factors behind these weaknesses include the lack of financial resources allocated to the compilation of statistics, insufficient interagency coordination, and concern about accuracy that give rise to reluctance to publish provisional data.	
<b>Monetary statistics:</b> Monetary statistics compiled by the authorities are largely in line with the methodology in the Monetary and Financial Statistics Manual, 2000 and its companion Compilation Guide, 2008. Timeliness of reporting by state-owned commercial banks has significantly improved; consequently, data on depository corporations—as well as finance companies—are usually available within a period of two to three months. Reporting formats (balance sheet and appendices) applied to commercial banks and finance companies were updated in 2009 and the updated version was enforced in 2010. All respondents now provide all requested data. Data on insurance corporations are not yet collected, but the Banque d'Algérie, with the continuing support of the IMF Statistics Department, launched a project to this end in 2009.	
<b>Balance of payments:</b> Balance of payments statistics are generally of good quality. Estimates of international investment position data are now available for 2011-2013 but have not yet been compiled for more recent years.	
<b>II. Data Standards and Quality</b>	
Algeria began participation in the General Data Dissemination System (GDDS) on April 21, 2009.	No data ROSC is available.

<b>ALGERIA: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE</b>					
<b>As of March 31, 2016</b>					
	Date of latest observation	Date received	Frequency of Data <sup>7</sup>	Frequency of Reporting <sup>7</sup>	Frequency of publication <sup>7</sup>
Exchange Rates	03/31/16	03/31/16	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities <sup>1</sup>	12/15	03/03/16	D	M	Q
Reserve/Base Money	12/15	03/03/16	D	M	Q
Broad Money	12/15	03/03/16	D	M	Q
Central Bank Balance Sheet	12/15	03/03/16	D	M	Q
Consolidated Balance Sheet of the Banking System	12/15	03/03/16	M	M	Q
Interest Rates <sup>2</sup>	12/15	03/03/16	M	M	Q
Consumer Price Index	03/16	04/19/16	M	M	M
Revenue, Expenditure, Balance and Composition of Financing <sup>3</sup> —Central Government <sup>4</sup>	11/15	02/18/16	M	I	A
Stocks of Central Government and Central Government-Guaranteed Debt <sup>5</sup>	12/15	02/18/16	I	I	A
External Current Account Balance	Q4, 2015	02/18/16	Q	I	Q
Exports and Imports of Goods and Services	Q4, 2015	02/18/16	Q	I	Q
GDP/GNP	Q4, 2015	04/25/16	Q	Q	Q
Gross External Debt	Q4, 2015	02/18/16	Q	I	Q
International Investment Position <sup>6</sup>	2013	03/03/16	I	I	NA
<p><sup>1</sup>Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.</p> <p><sup>2</sup>Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes, and bonds.</p> <p><sup>3</sup>Foreign domestic bank, and domestic nonbank financing.</p> <p><sup>4</sup>The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.</p> <p><sup>5</sup>Including currency and maturity composition.</p> <p><sup>6</sup>Includes external gross financial asset and liability positions vis-à-vis nonresidents. Data are partial, because of shortcomings in the compilation of FDI.</p> <p><sup>7</sup>Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); and Not Available (NA), Partially available (PA)</p>					