Country Report

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The Economist Intelligence Unit

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Highlights

Editor: **Edward Bell**
Forecast Closing Date: **June 21, 2013**

Outlook for 2013-17

- Abdelaziz Bouteflika's third term will come to an end in 2014. Mr Bouteflika suffered a mini-stroke in April 2013, but at present he has no clear successor. A consensus candidate is likely to emerge closer to the election.
- Abdelmalek Sellal, the prime minister, will continue to carry out modest political and economic reforms. Although the changes will be minimal, a serious outbreak of political unrest during the forecast period is not expected.
- Security risk will again be a priority for the government following a hostage crisis at a natural gas facility in January. The threat of terrorism will deter some foreign investors from taking on projects in Algeria.
- The fiscal balance will be vulnerable to movements in oil prices. High social spending will mean it will remain in deficit in 2013-17, moving from 1.9% of GDP in 2013 to around 3.3% during the rest of the forecast period.
- Real GDP growth will be 3.3% in 2013 as some additional oil production comes online, but hydrocarbons investment will face delays as a result of January's militant attack. Growth will average around 3.6% thereafter.
- Banque d'Algérie (the central bank) will continue to operate a managed float of the Algerian dinar against the US dollar. It will manage the value of the currency in line with a policy of curbing demand for imports.
- Algeria's external balances will be highly sensitive to movements in oil prices. The Economist Intelligence Unit now expects a much smaller current-account surplus in 2013 of around 3.9% of GDP, which will decline thereafter.

Review

- Mr Bouteflika appeared in a televised meeting with the prime minister in mid‑June. Mr Sellal said that the president continued to issue directives and was being made aware of Algeria's political and security situation.
- In June a large cadre of officials from Algeria's state-run power company, Sonelgaz, were charged by an Algiers court in relation to a corruption investigation linked to the awarding of power plant contracts. The investigation has similarities to an inquiry into Sonatrach in 2010.
- The Turkish prime minister, Recep Tayyip Erdogan, visited Algiers in early June to consolidate economic and political relations between the two countries. Turkey is an increasingly important market for exports of Algerian liquefied natural gas.
- The current-account surplus slumped markedly in the first quarter, down by around 80%, as hydrocarbons exports dropped and income debits rose. However, Algeria's large stock of foreign reserves, US$189bn at the end of March, will mean there will be little pressure on financing imports.

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Outlook for 2013-17

Political stability

The Economist Intelligence Unit expects Algeria's political scene to remain relatively stable in 2013-17. A powerful security-military establishment (le pouvoir), a recent history of brutal civil violence and some modest political liberalisation mean that Algeria should avoid the revolutionary upheavals seen in other Arab countries, despite similar discontent over economic and political conditions. The president, Abdelaziz Bouteflika, has been in power since 1999, and his current, third mandate runs until 2014. In April 2013 Mr Bouteflika suffered a mini-stroke and has been convalescing since. He has made a televised public appearance as the regime attempts to quash rumours that his health has deteriorated substantially, but it is nevertheless proving prickly about the president's condition. The Ministry of Justice has brought legal action against the editor of two journals in Algeria for suggesting that the president had fallen into a coma. It still remains uncertain who will succeed Mr Bouteflika as president in 2014 or in the interim should his health prevent him from completing his full mandate. There will be some jockeying for position among the leaders of Algeria's political scene as potential candidates attempt to build up a support base, but, at present, we expect the transition to a new leadership to be relatively smooth. It is unlikely that any successor would depart radically from Mr Bouteflika's policy of slow and modest political and economic reform. A terrorist attack on the In Amenas natural gas facility in south-eastern Algeria in mid-January will raise concerns about security and lead to a strengthening of the military's role in politics.

The prime minister, Abdelmalek Sellal, was appointed in September 2012, and is seen as a close ally to Mr Bouteflika, having run his presidential campaigns in 2004 and 2009. He is among the most prominent figures in Algeria who could be considered as a successor to Mr Bouteflika, but as yet he has made no announcements to indicate that he is prepared to run. We expect the government to continue the president's programme of modest political liberalisation. A reform body has begun work to make amendments to Algeria's constitution, but substantial political liberalisation or additional empowering of parliament is unlikely. Mr Sellal has said that his focus will be on improving services, creating jobs and expanding the housing stock—these have been hallmarks of previous Algerian governments but have had limited success because of bureaucratic inefficiency.

The social imbalances that contributed to the Arab Spring, such as high youth unemployment, limited political expression and perceptions of corruption, exist to a large degree in Algeria. Riots and protests, particularly over the supply of housing, are set to remain a concern in the forecast period. The government will be able to meet some of the economic demands of protesters (by keeping wages high, for example) because it has a large oil stabilisation fund, which in 2012 was estimated at AD5.6trn (around US$75bn), equivalent to roughly 35% of GDP.

Election watch

The Front de libération nationale (FLN) controls nearly half of the seats in the Assemblée populaire nationale (the lower house) on its own. Parliament has little impact on policymaking, however, and will continue to act as a body to approve presidential decrees and decisions by the cabinet.

The 2014 presidential election will dominate the political scene in 2013-14. At present, we expect that an establishment figure will emerge as the leading candidate to replace Mr Bouteflika. The former prime minister, Ahmed Ouyahia, who appears to have the backing of the military establishment, is a potential candidate, as is Mr Sellal. However, there is a possibility that, should his health improve dramatically, Mr Bouteflika could attempt another run for the presidency. Given the regional trend against dynastic leadership, we would expect Mr Bouteflika to face social pressure and probable advice from other members of Algeria's political leadership against such a move.

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International relations

Maintaining a constructive relationship with the EU will be a priority, as the region is a major consumer of Algerian gas. Algerian-US relations will continue to be focused on dealing with militant Islamism and on US companies' interest in the oil and gas sector. Transnational militant groups operating in the Sahel will be a risk during the forecast period and Algeria's government will continue to co-ordinate policies with its neighbours to contend with the threat.

Algeria is developing its relationships with the governments in the region that were transformed during the Arab revolutions of 2011, while making it clear that such transitions are unwelcome at home. However, its influence on dynamics, such as supporting intervention against the regime of Syria's president, Bashar al-Assad, is limited compared with other regional powers. Algeria's relations with Morocco are complicated by the two countries' opposing views on the status of Western Sahara, which Algeria recognises as independent.

Policy trends

The government will encourage the development of the private sector and the financial sustainability of state-linked companies as Algeria frets about its heavy reliance on oil and gas income. In May a major house-building scheme was launched that will be financed by public banks, rather than the state directly. The prime minister has also called on public enterprises to improve their performance and not depend on state bail-outs. Despite this constructive tone, Algeria's private sector is small and the government will continue to dominate the economy in the forecast period. In June the minister responsible for investment announced that Algeria would be taking a majority stake in ArcelorMittal's steel-production facility, ostensibly to support a plan to increase capacity (but there may also be motivation to ensure jobs are not lost). The government will maintain high current spending on wages and subsidies in an attempt to prevent social unrest. Increasing the supply of electricity and gas to meet growing demand will be a priority, and a challenge, for Mr Sellal's government. Restrictions on foreign investment, including a tough tax regime and a limit of 49% on foreign ownership, and policies to reduce imports will be used to protect Algeria's national economic interests and promote domestic industry, but these could be relaxed during the forecast period to encourage foreign businesses to set up locally, with their production replacing some imports.

As the dominant sector of the economy, hydrocarbons will receive preferential treatment. An amended hydrocarbons law is meant to encourage foreign investors to participate in exploration and expand production. A new tax framework through which foreign oil companies will be taxed on profits rather than turnover has been designed to entice some foreign players into the sector. However, the attack on a natural gas facility in January will deter some firms from investing in Algeria and has already led to some speculation over existing operators slowing down investment in the country. The Ministry of Energy and Mining has ambitious plans to nearly double refining capacity, but progress will be slow given the scale of the projects and poor perceptions of the business environment. Nevertheless, Sonatrach, the state oil and gas company, will spend up to US$80bn over the next five years to meet demand for refined products and replace reserves through new exploration. The government will also try to diversify the economy away from its heavy reliance on oil and gas by taking advantage of the availability of feedstock to invest in related industries, such as petrochemicals and fertilisers.

The government is now more actively engaging in international economic forums to improve Algeria's influence on the global stage. In October 2012 it contributed US$5bn to the IMF and announced plans to sign new trade agreements in a prelude to joining the World Trade Organisation. We expect Algeria—a hawkish member of OPEC—to become increasingly vocal as it seeks to maximise income from its declining oil production.

Fiscal policy

Algeria will be aware of the need to consolidate spending as the government grows concerned about its vulnerability to oil price movements. The 2013 budget sets spending at AD6.878trn (US$90.5bn at the government's forecast exchange rate), down by 11% from the figure agreed in the 2012 supplementary budget. Current spending is budgeted to be 12% lower, and capital spending is also lower than in the 2012 supplementary budget. The government has a history of underspending, particularly on the capital budget, having spent only around 55% of its total allocated budget in 2011. However, we expect that the government will be wary of stoking unrest if it cuts total spending too far and too quickly. Despite the government's efforts at diversification, we expect oil receipts to remain the largest component of fiscal revenue. We have revised down our forecast for the fiscal deficit in 2013, to around 2% of GDP, as lower oil export revenue dampens revenue growth. Thereafter, the government will record deficits of an average of around 3.3% of GDP. Public debt is, however, at relatively low levels and Algeria's sizeable oil stabilisation fund means that the government will be able to finance any fiscal shortfall comfortably.

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Monetary policy

The official aim of Banque d'Algérie (BdA, the central bank) is to control the money supply in order to contain inflation, although it does not publish its monetary growth target. In recent years the BdA has adopted a more active policy by raising reserve requirements, increasing its purchase of excess deposits and lengthening the maturity of repurchase facilities to sap excess deposits generated by high oil and gas income. The central bank maintains a large stock of foreign reserves (US$189bn in February 2013), which means it could adopt a more robust monetary policy to affect the value of the dinar.

International assumptions

	2012	2013	2014	2015	2016	2017
Economic growth (%)						
US GDP	2.2	2.1	2.5	2.3	2.3	2.4
OECD GDP	1.4	1.3	2.1	2.2	2.1	2.2
World GDP	2.1	2.1	2.7	2.8	2.8	2.9
World trade	2.4	3.7	5.2	5.4	5.5	5.6
Inflation indicators (% unless otherwise indicated)						
US CPI	2.1	1.7	2.2	2.2	2.3	2.3
OECD CPI	2.2	1.7	2.1	2.2	2.3	2.2
Manufactures (measured in US$)	-0.6	-3.1	0.6	0.9	1.6	1.9
Oil (Brent; US$/b)	112.0	106.6	104.8	107.3	110.0	115.0
Non-oil commodities (measured in US$)	-10.9	-3.7	0.6	-0.2	0.6	2.2
Financial variables						
US$ 3-month commercial paper rate (av; %)	0.2	0.1	0.2	0.3	1.2	2.2
Exchange rate AD:US$ (av)	77.5	78.2	75.3	73.0	71.8	70.5
Exchange rate US$:€ (av)	1.29	1.31	1.29	1.27	1.26	1.27

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Economic growth

We expect the economy to grow by 3.3% in 2013, as the impact of the attack on the In Amenas natural gas facility has led to delays in work on natural gas projects. Throughout the forecast period, real GDP growth rates will remain modest despite the country's large and easily accessible hydrocarbons resources and the government's ample financing capabilities. Government expenditure will continue to account for a large share of the economy, as the authorities will remain wary of cutting back on spending too fast and provoking unrest, and the size of the private sector is small. High wages for public-sector workers will support private consumption, but price pressures and restrictions on credit will limit their impact. Private investment growth will be constrained by a lack of financing and uncertainty over whether Algeria will experience mass protests, now compounded by the unprecedented In Amenas attack. Infrastructure projects (expanding the housing stock and road and rail construction) are under way, but are often subject to delays, despite the availability of state funding. The economy will grow by an annual average of 3.6% in 2014-17.

Hydrocarbons will remain the dominant sector in the forecast period, despite the government's diversification strategy. Investment in the sector has been held up by corruption scandals at Sonatrach and uninviting licensing rounds, and it will also be constrained by concerns over security risks. A new round of investigations into the power sector has again raised the spectre of corruption in Algeria. A modest liberalisation of the hydrocarbons law, long-desired by foreign firms, has so far had little success in increasing investor interest, with some smaller foreign companies seeking to sell down their assets in Algeria. New oil production from the El Merk processing facility (estimated to bring on up to 150,000 barrels/day of crude and condensates) will be largely offset by declining output from Algeria's older fields, but we believe it will make a limited net gain at present. Additional oil is set to come on stream in the rest of the forecast period but will be at marginal levels. Natural gas production will increase over the forecast period, but exports will show only modest growth as domestic demand increases sharply and Algeria's markets improve energy efficiencies and cut down on consumption. An agreement with Qatar to provide two liquefied natural gas carriers will give Algeria greater flexibility in its gas exports markets. Investment in the energy sector is often subject to delays, and a plan to nearly double refining capacity is probably too ambitious. The government has now also signed deals to invest further in downstream capacity (fertiliser and petrochemicals). The government will make some progress on industrial diversification: a joint Algerian-Qatari steel plant will be operational by 2017 and a Renault assembly plant will be opened by 2014, helping to diversify the industrial sector of the economy.

Economic growth

%	2012[a]	2013[b]	2014[b]	2015[b]	2016[b]	2017[b]
GDP	2.7	3.3	3.7	3.2	3.5	3.9
Private consumption	3.3	4.9	4.9	5.2	5.7	7.3
Government consumption	10.0	7.0	8.5	4.3	2.0	1.0
Gross fixed investment	5.7	4.0	5.2	3.0	5.0	5.4
Exports of goods & services	-2.0	-4.4	-1.7	-0.2	-0.4	1.4
Imports of goods & services	3.4	2.2	4.4	4.5	5.7	8.2
Domestic demand	5.4	5.4	5.9	4.4	4.5	5.2
Agriculture	2.3	2.1	2.0	1.5	1.5	1.5
Industry	1.5	2.5	3.0	5.5	5.0	5.0
Services	4.3	4.6	4.9	0.3	1.7	2.8

[a] Economist Intelligence Unit estimates. [b] Economist Intelligence Unit forecasts.

Inflation

We expect inflation to slow to an average of around 4% in 2013, owing to a high base effect from 2012 and easing food prices. Prices rose by 5.9% year on year in the first quarter, down from around 9% in 2012 as a whole. Inflation will stay relatively stable at around 4-5% during the rest of the forecast period as price increases for food, of which Algeria is a major importer, stay relatively benign and the local industrial sector begins to match some national demand for capital goods. Food products are a large component of Algeria's inflation basket (43%), meaning any movements in the price of international agricultural goods leave the country vulnerable to imported inflation. Moreover, the import sector is heavily restricted, which can create bottlenecks and lead to price spikes. The government has also increased wages for public-sector workers in nearly all sectors to stem the rise of unrest in the country.

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Exchange rates

The BdA will manage the float of the Algerian dinar with the aim of meeting government policy goals, such as reducing the cost of imports to make foreign capital inputs more affordable or, at other times, trying to limit demand for imports. So far in 2013, the dinar has remained relatively stable, moving between AD77.93-79.02:US$1 in the first four months of the year. We expect a modest appreciation over the forecast period as the government relies on foreign capital inputs to meet infrastructure investment needs and the BdA manages the exchange rate to control import costs. The central bank has large foreign-exchange reserves, estimated at around US$189bn in February 2013, which would enable it to counter any serious downward pressure on the dinar, should it occur.

External sector

Algeria recorded a sharply lower current-account surplus in the first quarter of 2013 compared with the same period a year earlier. A large drop in hydrocarbons export revenue (down by 13.9%) contributed to a surplus of just US$846m, compared with over US$4.1bn in 2012. A higher income deficit, probably a result of international firms moving cash out of the country following the militant attack on the In Amenas facility, also helped to push the balance lower. In the light of the weak first-quarter figures, we have revised down our forecast for 2013 as a whole; we still expect Algeria to achieve a current-account surplus, but of only 3.9% of GDP, compared with close to 6% in 2012 and 9% in 2011. The data again demonstrate the high sensitivity of Algeria's external balances to movements in international oil prices and trade patterns. Hydrocarbons dominate the trade balance, accounting for over 96% of exports in the first four months of 2013. These are structural concerns for Algeria's external account, and the government is encouraging export-oriented diversification in petrochemicals and metals manufacturing. We forecast that the current-account surplus will decline gradually over the forecast period, reaching 0.9% of GDP in 2017 as oil and gas exports are outpaced by import growth.

Forecast summary

Forecast summary
(% unless otherwise indicated)

	2012[a]	2013[b]	2014[b]	2015[b]	2016[b]	2017[b]
Real GDP growth	2.7	3.3	3.7	3.2	3.5	3.9
Crude oil ('000 b/d)	1,170[c]	1,195	1,215	1,220	1,218	1,180
Natural gas production (bn cu metres)	82	76	80	80	82	84
Hydrocarbon exports (US$ bn)	69.7	66	64.0	68.1	73.7	79.8
Unemployment rate (av)	10.2	9.8	9.5	9.5	9.3	9.2
Consumer price inflation (av)	8.9[c]	3.9	5.1	4.3	4.8	4.7
Consumer price inflation (end-period)	9.1[c]	2.5	4.2	4.6	4.7	4.5
Government balance (% of GDP)	-1.6	-1.9	-3.4	-3.0	-3.8	-3.2
Exports of goods fob (US$ bn)	71.8	68.1	66.5	70.8	76.6	82.9
Imports of goods fob (US$ bn)	51.6	52.7	55.3	58.9	61.7	67.3
Current-account balance (US$ bn)	12.3	8.7	3.9	4.7	3.8	3.5
Current-account balance (% of GDP)	5.8	3.9	1.5	1.6	1.1	0.9
External debt (end-period; US$ bn)	5.7	5.4	5.2	5.6	6.0	6.5
Exchange rate AD:US$ (av)	77.54[c]	78.20	75.30	73.00	71.80	70.50
Exchange rate AD:US$ (end-period)	78.10[c]	79.75	75.15	72.40	71.15	69.85
Exchange rate AD:¥100 (av)	97.18[c]	79.56	73.82	70.87	70.39	69.80
Exchange rate AD:€ (av)	100.02[c]	102.44	97.14	92.71	90.47	89.54

[a] Economist Intelligence Unit estimates. [b] Economist Intelligence Unit forecasts. [c] Actual.

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Data and charts

Annual data and forecast

GDP	2008[a]	2009[a]	2010[a]	2011[a]	2012[b]	2013[c]	2014[c]
Nominal GDP (US$ bn)	171.5	137.7	161.8	198.5	212.1	226.9	260.0
Nominal GDP (AD bn)	11,077	10,007	12,034	14,481	16,448	17,745	19,577
Real GDP growth (%)	2.4	2.4	3.3	2.5	2.7	3.3	3.7
Expenditure on GDP (% real change)							
Private consumption	4.9[b]	6.1[b]	5.9[b]	7.6[b]	3.3	4.9	4.9
Government consumption	8.7[b]	6.5[b]	12.9[b]	5.4[b]	10.0	7.0	8.5
Gross fixed investment	11.8[b]	8.2[b]	7.0[b]	3.1[b]	5.7	4.0	5.2
Exports of goods & services	-2.9[b]	-10.3[b]	-0.5[b]	-3.8[b]	-2.0	-4.4	-1.7
Imports of goods & services	17.7[b]	12.8[b]	4.0[b]	-1.2[b]	3.4	2.2	4.4
Origin of GDP (% real change)							
Agriculture	-5.3	2.7	3.3	2.2[b]	2.3	2.1	2.0
Industry	1.4	2.5	3.3	4.7[b]	1.5	2.5	3.0
Services	9.3	2.1	3.3	-0.1[b]	4.3	4.6	4.9
Population and income							
Population (m)	34.7	35.3	36.0	36.7	37.5	37.9	38.3
GDP per head (US$ at PPP)	7,807	7,929	8,136	8,352	8,547	8,871	9,279
Recorded unemployment (av; %)	11.3	10.2	10.0	10.4[b]	10.2	9.8	9.5
Fiscal indicators (% of GDP)							
Public-sector balance	9.0	-5.7	-0.6	-0.2	-1.6	-1.9	-3.4
Public-sector debt interest payments	0.6	0.4	0.3	0.3	0.3	0.4	0.5
Public debt	6.6	8.2	9.2	8.4	7.8	11.9	19.3
Prices and financial indicators							
Exchange rate AD:US$ (av)	64.58	72.65	74.39	72.94	77.54[a]	78.20	75.30
Exchange rate AD:€ (av)	94.94	100.98	98.93	101.38	100.02[a]	102.44	97.14
Consumer prices (av; %)	6.7	5.7	3.9	4.5	8.9[a]	3.9	5.1
Stock of money M1 (% change)	17.3	1.1	14.6	24.1	7.6[a]	7.9	10.3
Stock of money M2 (% change)	16.0	4.8	13.5	19.9	10.9[a]	10.5	10.4
Lending interest rate (end-period; %)	8.0	8.0	8.0	8.0	8.0[a]	8.0	8.0
Current account (US$ m)							
Trade balance	40,600	7,780	18,200[b]	25,950[b]	20,240	15,348	11,265
Goods: exports fob	78,590	45,180	57,090[b]	72,880[b]	71,810	68,089	66,529
Goods: imports fob	-37,990	-37,400	-38,890[b]	-46,930[b]	-51,570	-52,741	-55,263
Services balance	-7,590	-8,690	-8,340[b]	-8,790[b]	-7,290	-7,314	-8,755
Primary income balance	-1,340	-1,310	-360[b]	-2,040[b]	-3,676	-1,314	-2,216
Secondary income balance	2,780	2,630	2,670	2,650	3,170	2,029	3,625
Current-account balance	34,450	410	12,150[b]	17,700[b]	12,300	8,750	3,920
External debt (US$ m)							
Debt stock	6,210	7,368	7,211	6,072	5,730	5,405	5,186
Debt service paid	1,249	1,051	672	634	881	1,048	944
Principal repayments	1,056	907	554	531	777	957	840
Interest	193	145	118	103	103	91	104
Debt service due	249	1,051	672	634	881	1,048	944
International reserves (US$ m)							
Total international reserves	143,544	149,347	162,915	183,122	191,597[a]	200,104	200,243

[a] Actual. [b] Economist Intelligence Unit estimates. [c] Economist Intelligence Unit forecasts.
Sources: IMF, International Financial Statistics; Banque d'Algérie.

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Quarterly data

	2011 2 Qtr	3 Qtr	4 Qtr	2012 1 Qtr	2 Qtr	3 Qtr	4 Qtr	2013 1 Qtr
Prices								
Consumer prices (2000=100)	126.3	129.3	130.6	136.0	138.3	139.7	142.4	143.9
Consumer prices (% change, year on year)	4.0	5.4	5.2	9.0	9.5	8.0	9.0	5.9
Petroleum prices Saharan-46 (US$/barrel)	113.5	104.4	108.6	124.0	96.6	111.5	111.6	n/a
Financial indicators								
Exchange rate AD:US$ (av)	71.9	72.5	74.4	75.1	75.6	80.4	78.9	78.3
Exchange rate AD:US$ (end-period)	71.7	74.0	76.1	74.1	78.9	79.3	78.1	79.0
Deposit rate (av; %)	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
Discount rate (end-period; %)	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0
Lending rate (av; %)	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0
Treasury bill rate (av; %)	0.2	0.2	0.3	0.5	0.6	0.6	0.2	0.5
M1 (end-period; AD bn)	6,308	6,744	7,142	7,500	7,523	7,675	7,682	7,966
M1 (% change, year on year)	16.5	19.9	24.1	20.4	19.3	13.8	7.6	6.2
M2 (end-period; AD bn)	9,015	9,513	9,929	10,523	10,626	10,945	11,013	11,380
M2 (% change, year on year)	16.3	17.9	19.9	20.0	17.9	15.0	10.9	8.1
Sectoral trends								
Crude petroleum production (m barrels/day)	1.26	1.28	1.16	1.16	1.16	1.18	1.16	1.15
Foreign trade (US$ m)[a]								
Exports fob	19,392	18,557	18,265	15,773	14,218	13,299	14,266	n/a
Imports cif	-12,890	-11,432	-12,081	-11,158	-13,737	-12,566	-14,354	n/a
Trade balance	6,502	7,125	6,184	4,615	481	733	-88	n/a
Foreign reserves (end-period; US$ m)								
Reserves excl gold (end-period)	176,177	176,602	182,822	187,101	186,951	188,906	191,297	n/a

[a] DOTS estimates.

Sources: IMF, International Financial Statistics, Direction of Trade Statistics (DOTS); Oil Market Intelligence; International Energy Agency, Oil Market Report; Office national des statistiques, Statistiques Algérie.

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Monthly data

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Exchange rate AD:US$ (av)												
2011	73.39	72.87	72.31	71.71	72.17	71.94	72.13	72.09	73.34	73.62	74.84	74.84
2012	76.23	74.79	74.42	74.15	75.00	77.72	80.69	81.15	79.47	79.21	79.42	78.19
2013	77.93	77.86	79.02	78.49	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Exchange rate AD:US$ (end-period)												
2011	72.79	72.62	72.18	71.30	71.99	71.66	72.13	71.94	73.97	73.04	76.06	76.06
2012	75.34	74.39	74.07	74.23	76.84	78.86	81.91	80.04	79.33	79.18	78.52	78.10
2013	77.42	78.34	79.02	78.49	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Real effective exchange rate (2005=100; CPI-basis)												
2011	78.61	77.81	76.91	76.06	76.52	76.94	77.68	77.98	78.60	79.12	78.41	79.85
2012	80.99	82.09	83.58	84.65	84.88	83.32	81.20	79.85	80.34	81.40	80.85	81.47
2013	81.86	82.21	84.30	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M1 (% change, year on year)												
2011	17.9	17.3	19.3	21.1	21.4	16.5	20.8	23.9	19.9	19.5	23.1	24.1
2012	22.1	22.6	20.4	16.9	15.0	19.3	16.2	10.9	13.8	13.7	11.0	7.6
2013	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
M2 (% change, year on year)												
2011	15.8	15.4	16.7	18.9	19.3	16.3	18.5	20.8	17.9	17.9	20.2	19.9
2012	19.7	20.5	20.0	16.5	15.1	17.9	16.4	12.6	15.0	15.2	13.0	10.9
2013	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Industrial production (% change, year on year)												
2011	-2.6	0.0	-2.6	-1.7	0.3	0.8	-1.0	-1.3	-0.4	-3.7	-8.0	-9.2
2012	-7.5	3.3	5.0	-0.4	-1.9	0.8	0.6	1.7	1.8	3.5	3.5	6.9
2013	7.2	-4.8	-0.7	0.8	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Deposit rate (av; %)												
2011	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
2012	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
2013	1.8	1.8	1.8	1.8	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Lending rate (av; %)												
2011	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0
2012	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0
2013	8.0	8.0	8.0	8.0	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Consumer prices (av; % change, year on year)												
2011	3.6	3.5	3.4	4.5	3.9	3.7	5.2	5.7	5.1	5.5	4.9	5.1
2012	7.5	9.3	10.1	11.0	9.0	8.7	8.2	7.2	8.8	9.9	8.1	9.1
2013	7.8	5.4	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Total exports fob (US$ m)												
2011	6,097	4,955	6,187	6,840	6,850	5,701	6,369	6,303	5,885	5,945	6,874	5,445
2012	4,806	4,641	6,326	5,158	5,038	4,022	4,403	4,880	4,016	4,560	4,528	5,178
2013	4,809	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Total imports cif (US$ m)												
2011	3,191	3,316	4,318	4,221	4,354	4,315	4,106	3,607	3,718	3,720	4,205	4,156
2012	3,269	3,379	4,510	4,203	4,900	4,634	4,322	4,027	4,216	4,725	4,559	5,070
2013	4,283	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Trade balance fob-cif (US$ m)												
2011	2,906	1,639	1,869	2,620	2,496	1,386	2,262	2,696	2,167	2,225	2,669	1,290
2012	1,536	1,262	1,817	954	138	-612	80	853	-200	-165	-31	108
2013	526	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a

Sources: IMF, International Financial Statistics, Direction of Trade Statistics; Haver Analytics.

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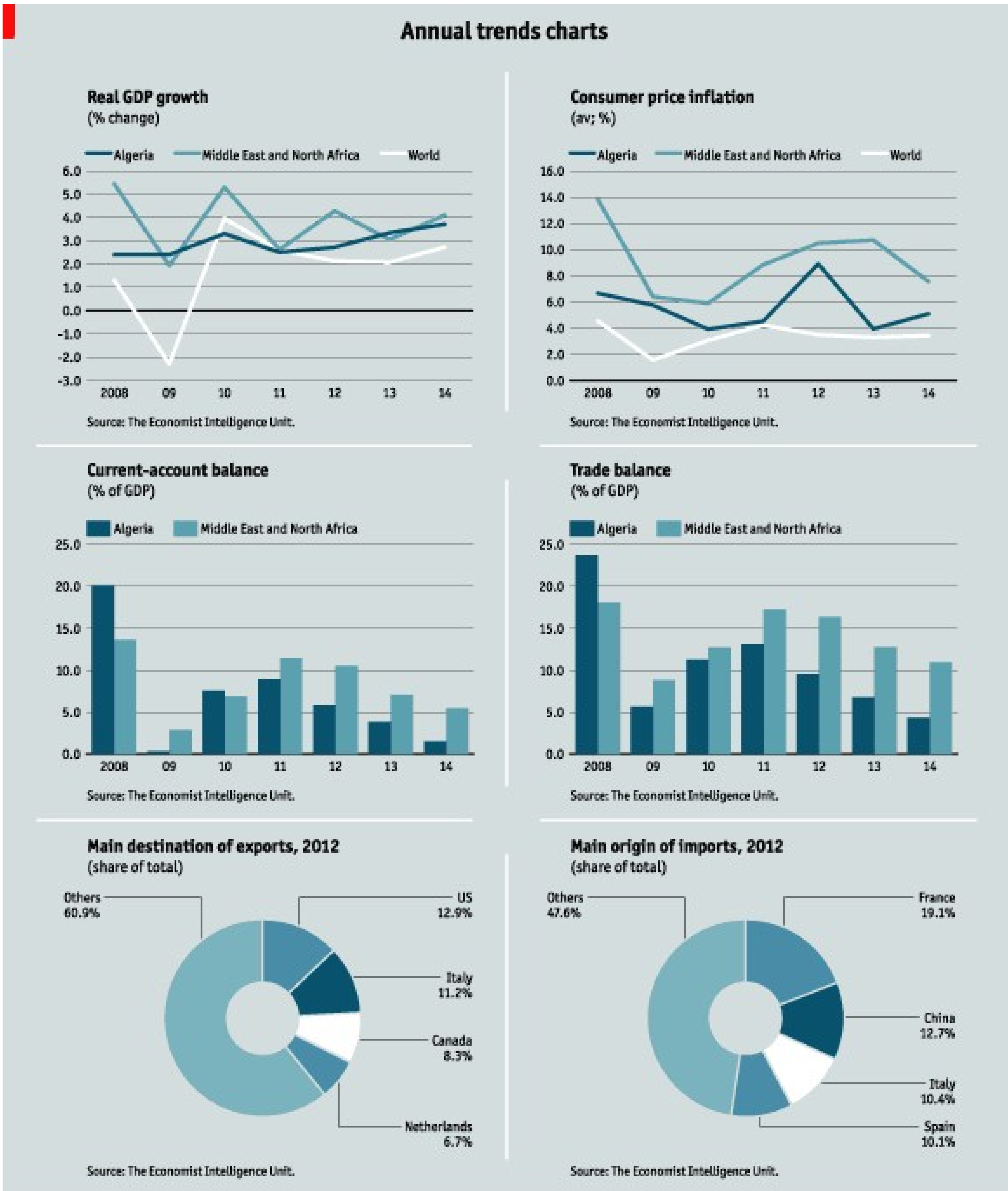
Annual trends charts



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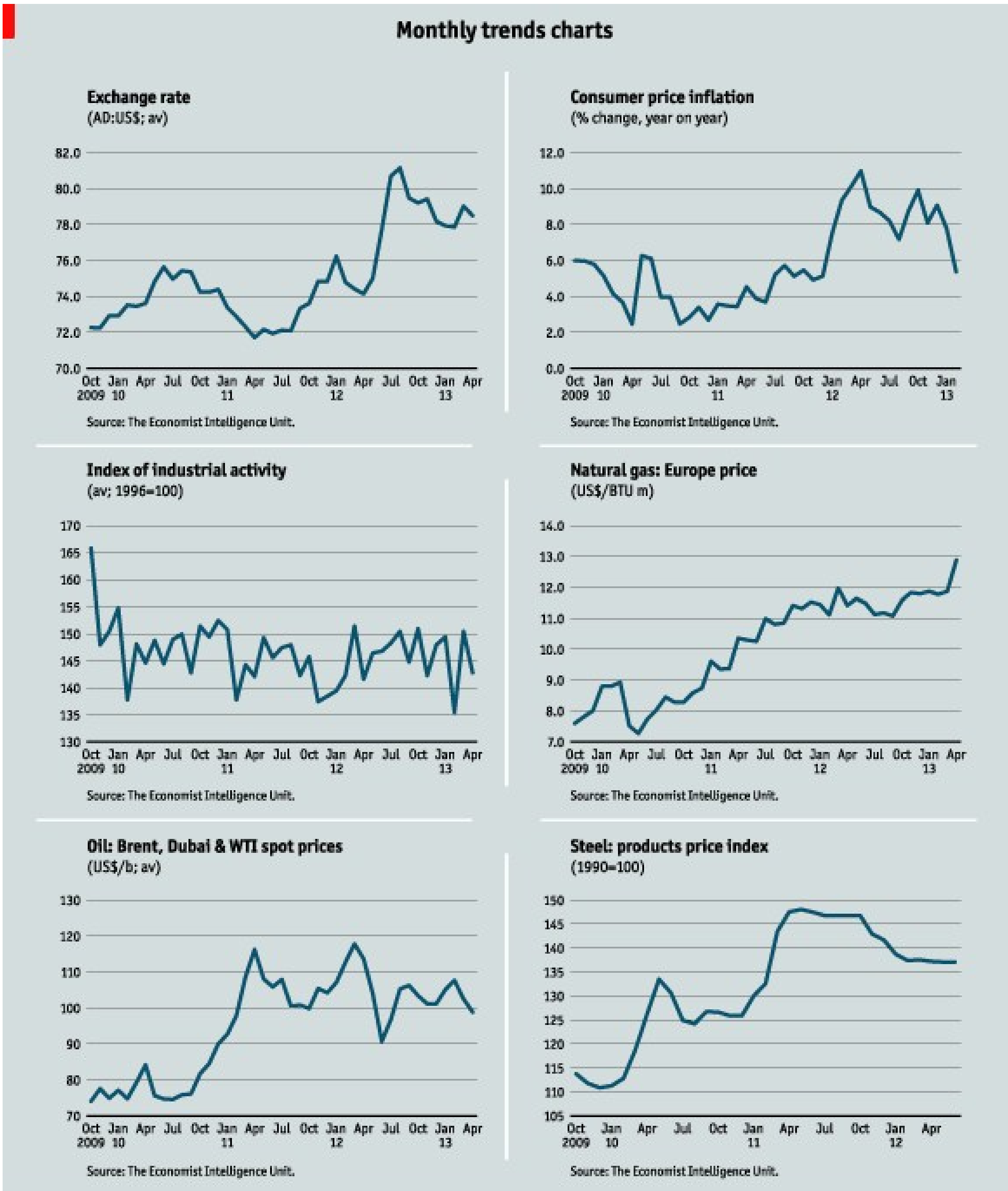
Monthly trends charts



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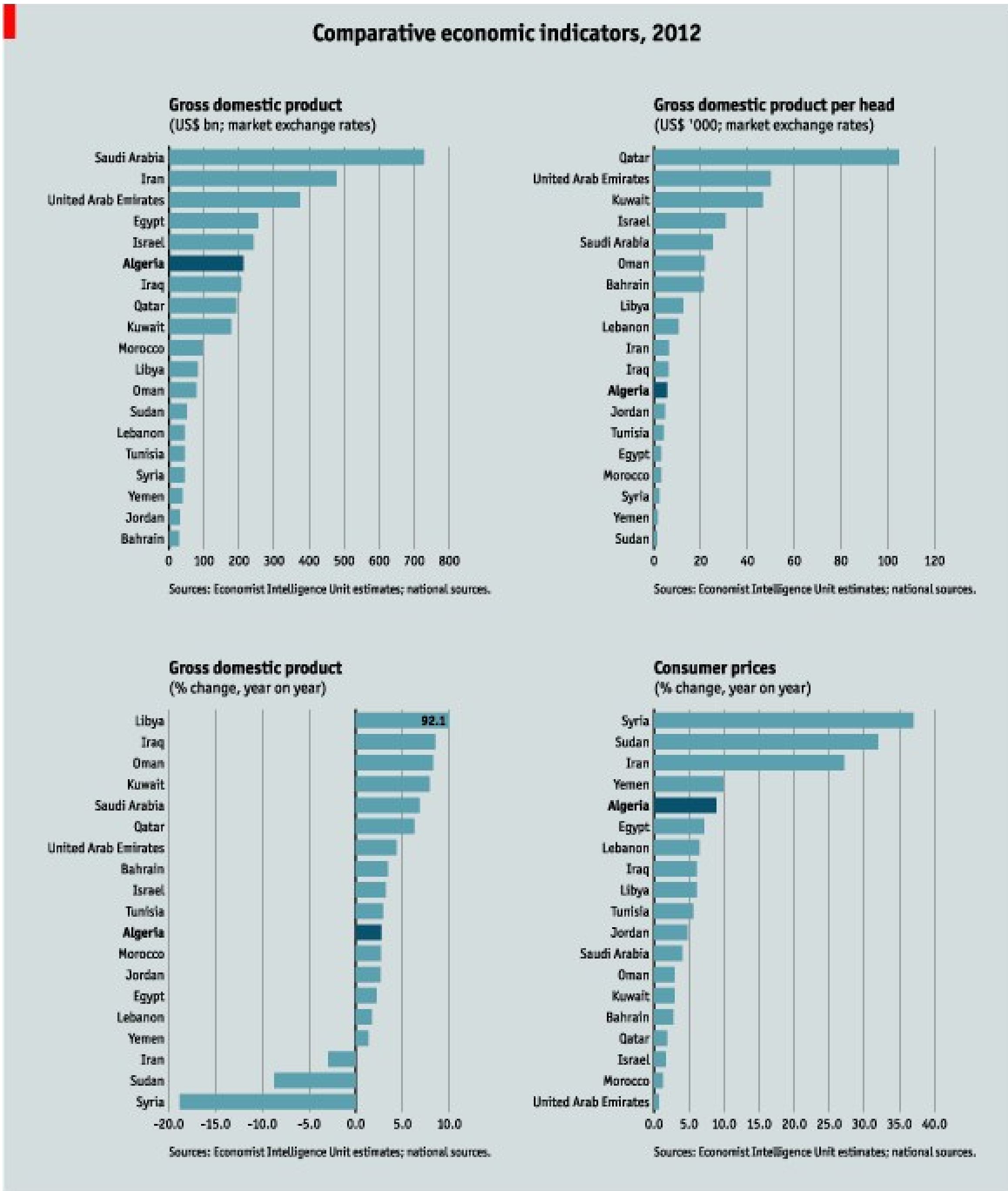
Comparative economic indicators



Basic data

Land area

2,381,741 sq km

Population

37.1m (January 1st 2012; Office national des statistiques estimate)

Population of main urban areas in '000s (mid-2006 Economist Intelligence Unit estimates):

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Greater Algiers (incl capital): 4,825

Oran: 1,150

Constantine: 810

Annaba: 580

Climate

Temperate on the coast, hot and dry in the south

Weather in Algiers (altitude 59 metres)

Hottest month, August, 22-29°C; coldest month, January, 9-15°C (average daily minimum and maximum); driest month, July, 1 mm average rainfall; wettest month, December, 140 mm average rainfall

Languages

Arabic (official); Berber language (Tamazight) and French are also used

Measures

Metric system

Currency

Algerian dinar (AD) = 100 centimes or 20 douros

Time

GMT in the winter months; GMT plus one hour in the summer

Public holidays

All Muslim holidays are observed in accordance with the lunar calendar, and the dates are therefore approximate: Prophet's birthday (January 24th 2013); Eid al-Fitr (August 8th 2013); Eid al-Adha (October 15th 2013); Islamic New Year (November 4th 2013). Other public holidays: New Year's Day (January 1st); Labour Day (May 1st); Independence Day (July 5th); Anniversary of the Revolution (November 1st)

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Political structure

Official name

People's Democratic Republic of Algeria

Legal system

Based on the constitution of 1976, revised in 1989 and 1997

Legislature

Bicameral: the lower house, the Assemblée populaire nationale, with 462 members, was first elected in June 1997; the upper house, the Conseil de la nation, which has 144 seats, was formed in December 1997, with two-thirds of its members elected through municipal polls and the remainder appointed by the president

National elections

May 10th 2012 (legislative); April 9th 2009 (presidential); November 27th 2007 (provincial and municipal councils); next presidential election due in April 2014

Head of state

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President, currently Abdelaziz Bouteflika, elected for a third term on April 9th 2009; Mr Bouteflika is also defence minister

Executive

Council of Ministers presided over by the prime minister, who is appointed by the head of state. A new government was appointed in September 2012

Main political parties

Front de libération nationale (FLN), previously the sole legal party; Rassemblement national démocratique (RND); Front des forces socialistes (FFS); Rassemblement pour la culture et la démocratie (RCD); Mouvement de la réforme nationale (El Islah, Islamist); Mouvement de la société pour la paix (MSP; Islamist); Parti des travailleurs (Labour Party)

The government

Prime minister: Abdelmalek Sellal

Minister delegate at the Ministry of Defence: Abdelmalek Gueneiza

Key minister

Agriculture: Rachid Benaissa

Defence: Abdelaziz Bouteflika

Energy & mining: Youcef Yousfi

Environment, territorial planning & towns: Amara Benyounes

Finance: Karim Djoudi

Foreign affairs (minister of state): Mourad Medelci

Health & population: Abdelaziz Ziari

Housing: Abdelmadjid Tebboune

Industry, small & medium-sized enterprises & investment promotion: Cherif Rahmani

Interior & local government: Dahou Ould Kablia

Justice: Mohammed Charfi

Labour & social security: Tayeb Louh

National education: Abdelatif Baba Ahmed

National solidarity: Souad Bendjaballah

Parliamentary affairs: Mahmoud Khedri

Post & information & communications technology: Moussa Benhamadi

Prospective planning & statistics: Bachir Messaitfa

Public works: Amar Ghoul

Trade: Mustapha Benbada

Transport: Amar Tou

Water resources: Mohammed Necib

Central bank governor

Mohammed Laksaci

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Recent analysis

Generated on July 29th 2013

The following articles were published on our website in the period between our previous forecast and this one, and serve here as a review of the developments that shaped our outlook.

Politics

Forecast updates

June 21, 2013: Election watch

President appears in public meeting with prime minister

Event

Algeria's president, Abdelaziz Bouteflika, has made his first televised appearance since his transfer in April to a hospital in Paris for the treatment of a mini stroke. He appeared in discussions with the prime minister, Abdelmalek Sellal, and the chief of staff of the national army, Ahmed Gaid Saleh.

Analysis

Mr Sellal told the state news agency, Algérie Presse Service, that he had given the president a "general situation report" on the country, and that the two had discussed the government's operations and the political and the security situation. The president had reacted "very well" and his state of health seemed "decent", although he was still "convalescing". Mr Bouteflika instructed the prime minister to complete the supplementary finance bill and other legislation ahead of the next cabinet meeting, according to an official statement from the presidency.

The images showed that Mr Bouteflika has reached at least a basic level of health, but revealed little about his ability to govern and the his condition. But the meeting is significant in that it shows a willingness on the part of the establishment to demonstrate that Mr Bouteflika is still in charge. The absence of images of the president in recent weeks had led to growing speculation of an early presidential transition—ahead of scheduled elections in April 2014.

One opposition party, the nationalist Front national algérien (FNA) voted on June 15th for its president, Moussa Touati, to stand in the election, while a moderate Islamist party, the Mouvement de la société pour la paix (MSP), said that it was "yet to declare" for the election because of the "ambiguity" of the political scene. The MSP is in consultations with other political parties to adopt a position on the election, its president, Abderrezak Mokri, said on June 15th.

Impact on the forecast

At present, we still do not believe it is likely that Mr Bouteflika will run for a fourth term in 2014 and that a consensus candidate from the establishment, possibly Mr Sellal, could emerge as a leading contender. However, we will not rule out an attempt by the president to run again should his health improve dramatically.

Analysis

June 12, 2013

Doubts raised over Bouteflika's ability to resume duties

Algeria's president, Abdelaziz Bouteflika, continues to convalesce in a hospital in Paris, weeks after suffering a mini stroke. Algeria's media have been barred in effect from commenting on the president's condition, and public figures have provided reassuring, yet unsupported, assurances about his condition. There is now growing speculation over Mr Bouteflika's ability to resume his duties as president when he fully recovers. The absence of a clear successor will serve as a catalyst for the political establishment, particularly the powerful military, to select a figure who can run in next year's presidential election.

In recent weeks, Algeria's government and key political figures have remained steadfast in their insistence that

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Mr Bouteflika is making a good recovery, that he will return to Algeria to resume his duties and that any speculation to the contrary is inherently unpatriotic. In early June Abdelmalek Sellal, the prime minister, along with the head of the Algerian army visited the president at his hospital in Paris and said that Mr Bouteflika was in good health and had provided instructions and guidance.

Loyal opposition

Mr Bouteflika's illness will "soon be no more than a bad memory," said Mr Sellal, on May 22nd. The interim leader of the Rassemblement national démocratique (RND), Abdelkader Bensalah, denounced those who were "spreading despair" about Mr Bouteflika's health, and said that the institutions of state were functioning in a "normal manner" in his absence. The political reform programme launched by the president during the Arab Spring in 2011 was "progressing serenely" and passing to the "last phase" of constitutional amendments, Mr Bensalah said. The head of the Parti des travailleurs, Louise Hanoune, said in early June that she had heard from a "source close to the head of state" that Mr Bouteflika was "doing well" and that his health was "constantly improving". There was "no reason" for a transition process to be set in motion, Ms Hanoune said.

Such has been the speculation about the president's health that the French president, François Hollande, broke his silence on the subject on May 31st, saying that although it was not down to him to give health updates on Mr Bouteflika, he would say that after a period in the Val‑de‑Grâce hospital the Algerian president was convalescing in Les Invalides, where he had access to "all the necessary care". Mr Hollande said that Mr Bouteflika would return to Algeria, and hoped that it would be soon. Mr Hollande also said that he had faith in the "solidity" of Algeria's institutions in the president's absence.

Media blackout

The French media, though, has been less restrained. *Le Parisien* quoted a senior diplomatic source who said that although Mr Bouteflika might return to Algeria in the coming days or weeks, he was "in no state" to continue in his presidential duties and it would be "wise" for the Algerian authorities to begin the transition process. Some dissenting voices in Algeria, including a former colonel of the Departement du renseignement et de la securité, Mohammed-Chafik Mesbah, and a retired general, Mohand-Tahar Yala, have called for the transition process to begin.

Speculation over the president's health has been fuelled by what *El Watan*, a French-language Algerian daily, described as a "blackout" on information in Algeria. In late May Algeria's authorities took legal action against the editor of two journals for an article that commented on the health of the president.

Silent speculation

Just ten months ahead of the next president election, a lack of visual evidence that Mr Bouteflika is in fact making a strong recovery gives credence to the view that he will not resume his presidential duties. Assuming he does indeed return to Algeria, though, this is not as dramatic as it sounds. Ever since his illness in 2005, public appearances by Mr Bouteflika, who is now 76, have become increasingly few and far between. There have been periods in recent years when months have gone by without the president making a public appearance, something that would be unheard of for a leader in most other countries. A great deal of power is vested in the position of the Algerian president, who can rule by decree if he chooses—and Mr Bouteflika has often chosen to do so when it comes to important policy areas. But much of that power is dependent on the support of a powerful elite behind the scenes, known as *le pouvoir*, comprising powerful figures from the era of Algeria's battle for independence in the 1950s and early 1960s, and from the civil war in the 1990s. It was the support of these, mainly military, figures, that was the bedrock of Mr Bouteflika's first presidential election victory in 1999. Despite his best efforts he has been unable to break free from their control.

Pouvoir preparing

There is no doubt that *le pouvoir* will want to line up a successor for Mr Bouteflika, and the president's current incapacity is likely to bring urgency to this process. The lack of an obvious successor to Mr Bouteflika has long created concerns over the country's long‑term stability. Whether a transition takes place at the next election in April 2014 or before then, it will be a delicate process. As long as Mr Bouteflika is alive, though, whether or not he is around to play an active part in leading the country is not so important.

Although it remains unclear who will take over as president, Algeria's political elite is relatively homogeneous, with most parties having bought in to Mr Bouteflika's policy of slow and piecemeal political reform. We expect the transition to a new leader to be relatively smooth, although there will be some chance of social unrest should it appear that the government is stage-managing the process in too heavy-handed a way.

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Economy

Forecast updates

June 7, 2013: External sector

Turkish prime minister visits Algiers

Event

Turkey's prime minister, Recep Tayyip Erdogan, made a two‑day state visit to Algeria in early June as part of a tour of North Africa that has also taken the Turkish leader to Morocco and Tunisia.

Analysis

Algerian officials were keen to stress that they had no interest in interfering in Mr Erdogan's domestic matters as social pressure builds on the prime minister. Mohammed Larbi Ould Khelifa, the president of Algeria's parliament, said that Algeria wished to continue its policy of neighbourliness and non-interference in the affairs of foreign nations. Algeria's prime minister, Abdelmalek Sellal, talked of the "privileged" relations between the two countries. The Turkish prime minister, who faces protests on his return to Turkey, also received an honorary doctorate from the University of Algiers for his "contribution to humanity".

Turkey and Algeria signed a friendship and co-operation treaty in May 2006, and the two countries are important trading partners. Mr Erdogan's visit was accompanied by a business forum in which more than 200 Turkish companies met with Algerian counterparts to explore partnership opportunities, particularly in automotives, industry and agro-industry. The aim of the visit was the consolidation of the economic and political relations between the two countries, said Mr Erdogan. He said that Turkey planned to remove visa requirements for Algerian citizens travelling to the country.

At a time when the global market for Algeria's gas is softening, Turkish demand for Algerian gas is an important component of the country's overseas trade. In January the two countries agreed to extend a contract under which Algeria provides Turkey with 4bn cu metres/year of gas for another ten years, continuing an agreement originally signed in 1989. Trade between the countries has increased by almost 400% in the past ten years, to US$5bn in 2012, according to Mr Sellal. Turkey has been particularly active in investment in textiles and steel, and a Turkish company is building an iron and steel plant in Oran. Mr Sellal encouraged Turkish companies to invest in Algeria's US$286bn five‑year infrastructure development programme, which runs from 2010 to 2014.

Impact on the forecast

We anticipate that Turkey will remain an important market for Algerian liquefied natural gas and will continue to factor this trade in to our forecasts for Algeria's external trade balance. We will also maintain our view that Algeria will have a cool attitude towards popular protest movements across the region and continue to support established regimes in most cases.

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June 11, 2013: External sector

First-quarter current-account surplus narrows sharply

Event

Algeria's current-account surplus contracted sharply in the first quarter of 2013 compared with a year earlier.

Analysis

Mohammed Laksaci, the governor of Banque d'Algérie (BdA, the central bank), said that Algeria recorded a current-account surplus of just US$846m in the first three months of 2013. This compares with a surplus of over US$4.1bn in the first quarter of 2012 (an 80% drop year on year). The major contributor to the substantial decline has been a drop off in hydrocarbons revenue (down by 13.9% year on year in the first quarter), while imports rose by nearly 9% in the same period. Although it did not provide detailed figures, the BdA also blamed an increase in the income deficit and decrease in net transfers for the lower current-account surplus. Part of the higher income deficit may be related to international firms seeking to repatriate funds out of Algeria following the militant attack on a natural gas facility in January.

At an annualised pace, Algeria would record a current-account surplus of US$3.4bn in 2013 if similar levels to the first quarter continued throughout the year. This would be the lowest level since 2009, when Algeria managed just a US$410m surplus in its external balance as oil prices dropped by nearly 40%. Algeria's oil production stayed roughly steady at around 1.15m barrels/day in the first four months of 2013 (around the same as a year earlier), but gas exports are likely to have fallen as a result of interruptions to supply from the attack in January.

Algeria's foreign-exchange reserves have stayed relatively stable. According to the central bank, reserves not including gold were at US$189.8bn in the first quarter, compared with US$190.7bn at the end of 2012. The central bank also indicated that gross external debt at the end of March was just US$3.5bn, comfortably dwarfed by the BdA's reserves. Owing to its very high level of foreign reserves, Algeria is unlikely to face any financing issues in 2013 (current reserves would provide Algeria with around three years of import cover). But the decrease in the current-account surplus indicates the outsized influence variances in oil and gas prices and production can have on the economy. Any dramatic reduction in hydrocarbons production will make Algeria's external balances vulnerable in the near term.

Impact on the forecast

In the light of the very weak level recorded in the first quarter, we will reduce our forecast for Algeria's current-account surplus from 5% of GDP in 2013.

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June 18, 2013: Policy trends

El Hadjar steel plant to be renationalised

Event

Algeria's government is preparing to buy back the majority stake in the El Hadjar steel plant, in the north-east of the country.

Analysis

Speaking to the government news agency, Cherif Rahmani, the minister for industry, small and medium-sized enterprises and investment promotion, said that negotiations to repurchase a controlling share in the facility—run by ArcelorMittal—would be "completed" by the end of the summer. The Luxembourg-based international steel giant holds a 70% stake in the facility, with the Algerian state owning the remainder though its steel industry agency, Sider. The repurchase of the facility, which was opened to the private sector in 2001, will follow Algeria's 51/49 foreign investment law, through which the government will acquire a 51% stake in the plant; ArcelorMittal will retain the remainder. Mr Rahmani said that the furnaces would remain open and the government would begin the process of valuing the stake in the facility.

The El Hadjar plant has been widely discussed in the local press as being continually on the brink of bankruptcy, with losses in 2012 estimated at US$45m. The investment from the government would ensure that the facility had adequate capital to continue operating and serving a market with demand of around 5m tonnes/year (t/y). The government announced in April that it had reached a deal with ArcelorMittal for a US$1bn expansion of production capacity, to 2.2m t/y. Algeria is heavily reliant on imports of construction materials, and moves to ensure that local production remains steady fit within broader macroeconomic strategies to cut down on imports.

The renationalisation of the plant appears slightly at odds with recent government announcements to encourage greater private-sector involvement in the economy and attempts to lessen reliance on government-run enterprises. However, the government's calculation will have considered the potential cost of the steel facility ceasing production and the associated labour unrest and import costs.

Impact on the forecast

The renationalisation of the El Hadjar facility falls in line with our view that the government will maintain a heavy presence in the economy, despite efforts to encourage the private sector.

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June 24, 2013: Policy trends

Michelin sells plant to local giant Cevital

Event

A local private conglomerate, Cevital, has reached a deal with a French tyre manufacturer, Michelin, through which it will take over the company's only producing facility by the end of 2013. Under the agreement, Cevital will initially take a 67% share in the manufacturer's local subsidiary, Michelin Algérie. It will take over the company in its entirety at the end of the year, at which point it will cease tyre production.

Analysis

Michelin has said that its decision to sell its operation is due to difficult market conditions. The small facility in Algiers, the location of which makes expansion difficult, does not benefit from the economies of scale that would make it viable during a time when automotive demand in Europe is suffering from a major downturn. Michelin has been operating in Algeria since 1959 and currently has between 600-700 employees.

Cevital has promised to continue to employ all the staff at the plant at one of its manufacturing facilities. Cevital has operations in sectors ranging from food processing to automotive sales and glass manufacturing. The tyre plant will be "converted", but there has been no announcement what it will be used for. The value of the deal also remains under discussion. It will be calculated based on the value of the working capital at the time of the transfer of the remaining shares in the company to Cevital at the end of the year.

Michelin's decision to pull out of Algeria seems to be a straightforward one, and there is no reason to look beyond difficult market conditions for an explanation. It also announced in June its decision to divest from its operations in Colombia for similar reasons. The deal with Cevital is a convenient way for the company to withdraw without facing problems over the loss of jobs. The deal is also consistent with the government's aim to promote the interests of local companies while aiming to ensure that the private sector contributes significantly to the economy.

Impact on the forecast

The sale of Michelin's assets to Cevital falls in line with our view that the Algerian government will encourage the deepening of the private sector in the country.

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June 25, 2013: Fiscal policy outlook

Pension rise reinforces fiscal account's oil dependency

Event

An 11% increase in pensions will cost the Algerian government AD36bn (US$453m at market exchange rates) a year, according to a statement by the labour and social security minister, Tayeb Louh.

Analysis

The increase, which is due to come into force by the end of June, will affect more than 2m pensioners. It is the latest in a series of pension increases in recent years, alongside substantial increases in public-sector wages. But continued increases in public spending are becoming increasingly unsustainable for the government.

Revenue from oil exports, which accounts for around 70% of government income, fell by nearly 14% in the first quarter of 2013 compared with a year earlier. The governor of the central bank, Banque d'Algérie, Mohammed Laksaci, described the situation as a balance-of-payments "shock" and admitted that Algeria's reliance on oil exports was "not sustainable".

For the time being, there is ample coverage for any downturn in the fiscal and external balances, although the accumulation of capital is slowing considerably. The oil stabilisation fund, the Fonds de régulation des recettes (FRR), is the 14th largest in the world, at US$77.2bn, according to a recent report by the US-based Sovereign Wealth Fund Institute, but it will be called upon to meet an official projected budget deficit of 20% of GDP. The budget is based on an oil price of US$37/barrel (which is well below our forecast of US$106.6/b in 2013), with any surplus going into the FRR. Algeria's sizeable foreign-exchange reserves stood at US$189.8bn excluding gold at the end of the first quarter, but the expected increase to US$200bn appears to have halted, and reserves fell by US$900m from the end of 2012.

The government has acknowledged that it cannot afford to continue with huge government spending programmes, and that it needs to increase private-sector involvement in the economy, but there has been little concrete evidence of this happening. Speaking in mid-June the finance minister, Karim Djoudi, said that there would be "no new taxes", and that the government's US$286bn 2010–14 infrastructure spending plan would "not be reduced". The minister promised that the supplementary budget would address bureaucratic inefficiencies, but this is unlikely to have a major impact.

Impact on the forecast

We continue to expect that the government will maintain high current expenditure, and, as a result of the drop in oil export revenue, we will increase our forecast for the fiscal deficit in 2013 from 0.9% of GDP at present to closer to 2%.

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June 28, 2013: Policy trends

FDI flows fell sharply in 2012

Event

Net flows of foreign direct investment (FDI) into Algeria fell sharply in 2012 according to recently published data from the UN Conference on Trade and Development (UNCTAD).

Analysis

Algeria recorded US$1.48bn in inflows of FDI in 2012, down by over 40% compared with a year earlier. Outflows turned positive in 2012, indicating a divestment of positions in overseas firms or assets held by Algerian firms. Net flows into Algeria were US$1.53bn, over 25% lower than a year earlier.

The levels were Algeria's lowest since 2007, when net flows were US$1.4bn. In 2008-11 inflows of FDI remained well above US$2bn. The downturn in 2012 will have reflected the general uncertainty in the global economy, with aggregate FDI inflows dropping to US$1.35trn, 18% lower than a year earlier, as investors remained cautious in searching for returns. However, relatively unfriendly local regulations towards foreign investment have consistently held back Algeria's potential and, given the size of its economy, it appears to be an FDI laggard compared with its regional peers. In 2012 inflows into Morocco rose by over 10% to US$2.8bn, and flows turned positive again in Egypt, reaching US$2.8bn, despite the political uncertainty there. Algeria's stock of FDI is modest at just 11% of GDP, compared with around 30% in Egypt and close to 50% in Morocco.

Algeria still remains a potentially attractive market for FDI given the relatively untapped sectors that international firms could enter. The government prioritises investment in the hydrocarbons and infrastructure sectors and has managed a constructive, if at times testy, relationship with foreign companies. However, restrictions that include limiting foreign partners to a 49% stake in any project and mandating them to keep a foreign-currency surplus in the country while operating in Algeria do much to deter foreign players from entering the market. Nationalisation risk is also prominent in the country as the government has made operating conditions difficult for companies it perceives to be "excessively" profitable. The government is continuing its efforts to exercise its right of first refusal to buy Djezzy, the local brand of Egypt-based Orascom Telecom, a process that has been under way since 2010, and had the potential to scupper Orascom Telecom's merger into VimpelCom, a Russian telecoms giant.

Impact on the forecast

We continue to expect that the government will maintain rigid restrictions on FDI into Algeria in an attempt to protect local industry and what it views as its national economic interests.

Analysis

June 5, 2013

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Government calls for improvements in non-oil sector

A recent weakening in the price of Algeria's benchmark crude oil has prompted the government to reconsider the economy's over-reliance on hydrocarbons. The government plans to shift the driver of the economy from the public sector to private sector and to support export-oriented diversification. The government is also eager for state-linked enterprises to improve their performance. However, the process will not be quick and will leave Algeria's economy exposed to fluctuations in the international hydrocarbons markets for some time.

According to Karim Djoudi, the finance minister, the economy has reached a "crucial moment" because of the need to make the transition from public demand to "private demand, household businesses and exports". Mr Djoudi has compared the state budget to that of a household, saying that if households "spend too much", they can "lose everything". The downward trend in international oil prices had led Algeria to adopt "greater prudence" in budgetary policy, he said, in remarks quoted on the state news agency, Algérie Presse Service.

The price of Sahara Blend, Algeria's benchmark crude, dropped by more than US$8/barrel in March because of maintenance outages at several European refineries, according to figures published by OPEC in May. The average price for Sahara Blend in March was US$108.87/b, down from US$116.99/b in February, a drop of 6.9%.

The relationship between oil revenue and Algeria's budget is not straightforward. On May 7th the Ministry of Finance announced that the budget deficit for the 2012 calendar year was AD3,281bn (US$41bn), equivalent to 21% of GDP. This was an increase from deficits of AD2,469bn in 2011 and AD1,496bn in 2010. Budget receipts in the first two months of the year amounted to AD935bn, compared with spending of AD1,033bn, according to the director-general of the Treasury at the finance ministry.

The reported deficit figures, though, are misleading. The government's figures are based on an oil reference price of US$37/b, far below the actual price. Any revenue generated from above the reference price goes to the government's oil stabilisation fund, the Fonds de regulation des recettes (FRR), which is then used to finance the deficit. According to the latest figures published by the government, of the AD3,166bn of oil revenue generated in the year to end-September 2012, AD1,519bn went towards the budget and AD1,647.1bn into the FRR. The government had reached its target oil revenue for full-year 2012 by the end of April.

Fiscal programmes depend on high oil prices

The government in recent years has adopted an expansionary fiscal policy, based around the latest five-year plan, in which US$286bn is earmarked for investment in infrastructure, and an expansion of government salaries, in part motivated by a concern by the government to buy off social discontent. Current economic conditions mean that the government must be "much more nuanced" when it comes to increases in salaries, said Mr Djoudi.

Nevertheless, Algeria's continued dependence on oil revenue remains extremely troubling. In the first quarter of 2013, Algeria's non-oil exports increased by 76% year on year to US$617m, according to the latest figures from the state customs agency, Centre national de l'informatique et des statistiques des douanes (CNIS). But this figure, equivalent to US$2.5bn a year, is a paltry amount for such a large economy. Non-oil exports in the first quarter of 2013 amounted to just 3.38% of total exports, according to the CNIS. These non-oil products included petroleum derivatives, with agricultural products the other major component of export earnings. Although oil prices are expected to remain high in the coming years, Algeria remains vulnerable to an oil price shock.

Equally worrying is the decline in Algeria's oil and gas output in recent years. Gas production declined from 88.2bn cu metres/year in 2005 to 78bn cu metres/y in 2011, according to BP's *Statistical Review of World Energy*. Liquids production, which includes crude oil, condensates and other related natural gas liquids, has been steadily declining too, from 2,015,000 barrels/day (b/d) in 2005 to 1,729,000 b/d in 2011, according to BP. Crude oil production fell to 1.16m b/d in April 2013 from 1.41m b/d in 2008, according to the International Energy Agency. The market for Algerian hydrocarbons is also softening. The US imported about 120,000 b/d of Algerian crude in 2012, compared with a peak of 443,000 b/d in 2007, according to the US government's Energy Information Administration. Shale gas production in the US and expected new gas production from Australia and Mozambique will continue to threaten Algeria's market position in the medium term.

Declining fields

Output from Algeria's major oil and gas regions is in decline, while new production is coming on stream only slowly. The El Merk oil facility came on stream in February, and will eventually have production of 127,000 b/d of crude and condensates and 30,000 b/d of liquefied petroleum gas, while oil projects at Bir Seba and Takouazet promise new production of some 60,000-80,000 b/d by 2014-15. New gas production of some 16bn cu metres/y is due to come on stream from Algeria's tight gas-rich south-west regionin 2016, two years behind schedule. But a vast programme to

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increase power generation capacity to meet rapidly rising domestic demand is likely to absorb much of the increase in output.

Mr Djoudi's statements on the need for a reorientation of the economy away from the public sector and towards the private sector are an important rhetorical shift for a government whose philosophy is firmly rooted in its socialist past. But the combination of security concerns with bureaucratic and regulatory barriers will make any such changes difficult to make.

June 7, 2013

African development under discussion in Asia

The fifth Tokyo International Conference on African Development (TICAD V) was held in Yokohama on June 1st–3rd. The importance of the conference was highlighted by the presence of an impressive list of leaders and senior politicians from Africa and a wide range of high-ranking officials from other countries, multinational development partners and private-sector organisations. The conference included US$32bn of new finance from Japan to support African development projects and the first concrete steps in setting out a new international development framework once the Millennium Development Goals run their course in 2015.

TICAD V was jointly hosted by the government of Japan, the UN, the UN Development Programme, the World Bank and, for the first time, the African Union Commission (AUC). Numerous African heads of state attended the three-day conference, as did the Japanese prime minister, the UN secretary-general, Ban Ki-moon, and the World Bank president, Jim Yong Kim. Attendees at the conference included high-ranking delegations from 51 African countries, 35 partner countries, 75 international and regional organisations from Africa and Asia, the private sector and civil society. The slogan for TICAD V was "Hand in Hand with a More Dynamic Africa", in recognition of the rapid pace of economic growth over the past decade in Africa and indicating greater confidence in the outlook for the continent since TICAD IV in 2008, which came under the slogan "Towards a Vibrant Africa".

Japan jockeys for position

The Japanese prime minister, Shinzo Abe, opened TICAD V with the announcement of a five-year, US$32bn package to support infrastructure and human capital development in Africa. This support goes beyond any altruistic instincts and seeks to help enhance Japan's trade ties to the region in the face of stiff competition for market access and raw material supplies, particularly from China and India. Indeed, the conference recognised the importance of Africa as a promising market with rapid growth rates, abundant natural resources and increasing populations, and marked another step in Japan's reshaping of its foreign policy approach to Africa. While maintaining its traditional role as a donor state for many African countries, the Japanese government is seeking to encourage greater direct investment and much stronger trade ties with the continent. In addition, it views the AUC as pivotal to future foreign policy diplomacy around continent-wide issues such as sustainable growth, climate change and international security.

China's focus on exploring how it can deepen Sino-African ties has been a key driver behind a more proactive and strategically thought approach from Japan towards the African continent. In particular, Japan is making a late charge to counteract China's increasing and changing role in the region, where it continues to engage on the ground and strengthen ties through substantial direct investment. In July 2012, the fifth Forum on China-Africa Co-operation (FOCAC) ministerial conference in Beijing produced the Beijing Action Plan (2013-15), and promised US$20bn in Chinese foreign aid over the following three years. FOCAC moves beyond resource exploitation to emphasise support for the development of Africa's infrastructure, agriculture and manufacturing industry, as well as the region's small and medium-sized enterprises.

A new Japanese plan for action

TICAD V culminated in delegates agreeing on a Yokohama Declaration complete with Action Plan covering the period from 2013 to 2017. The Yokohama 2013 Declaration identifies the areas of focus, whereas the Yokohama Action Plan (2013-2017) sets out the basis of implementation, monitoring and evaluation. These documents focus on three fundamental pillars of economic, political and social development for Africa: a robust and sustainable economy; an inclusive and resilient society; and peace and stability. Underpinning these overarching objectives are six key strategic approaches that aim to shape the direction of development in Africa, and Japanese engagement with the continent, during 2013-17. These strategic approaches entail the promotion of private-sector-led growth; accelerated infrastructure and capacity development; empowering farmers as mainstream economic actors; promoting sustainable and resilient growth; creating an inclusive society for growth; and consolidating peace, stability and good governance across the continent. These are ambitious aims, but ones that Japan hopes will help position it as a development partner with a holistic and pragmatic approach to African development, and which should ultimately

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benefit Japanese interests.

Concrete steps in post-2015 planning

The UN secretary-general's High-level Panel on the Post-2015 Development Agenda released a report at TICAD V that provided the first concrete steps towards the design of the next global development agenda. While the eight Millennium Development Goals (MDGs), which aim to cut global poverty, have formed a blueprint and framework for African development and international assistance since 2000, many countries are now looking beyond the deadline year of the MDGs' realisation, which is in September 2015.

In recognising the enormous economic, political and social changes since the MDGs were first introduced, the report calls for the new post-2015 goals to carry forward the gains of the MDGs and tackle wider issues focused on sustainable development. The report's aim is to drive five major transformational shifts by 2030: a move from "reducing" to ending extreme poverty; placing sustainable development at the core of the development agenda; transforming economies to drive inclusive growth; building accountable institutions that ensure good governance and peaceful societies; and forging a new global partnership based on co-operation, equity and human rights. The report builds on the outcome of the Rio+20 conference in 2012 and is likely to provide key input to the communication of the UN secretary-general to member states in September 2013 on the progress of post-2015 planning.

June 20, 2013

New round of corruption investigations target power sector

Three years after a major investigation into allegations of corruption in the award of contracts by the state oil and gas company, Sonatrach, a new round of investigations—known as Sonatrach II—is now under way into contracts awarded by the state power company, Sonelgaz. Three major power plant contracts awarded to major international companies are under investigation, and numerous senior officials at Sonelgaz have been placed under judicial supervision. The president, Abdelaziz Bouteflika, came to power with a mandate to clean up corrupt practices in Algeria, but the investigations may have alternative and politically driven motivations.

The head of Sonelgaz, Noureddine Boutarfa, his predecessor, Abdelkrim Benghanem, and 15 other executives in Algeria's power sector have been charged by a court in Algiers with breaching regulations under the state contracts code and the 2006 corruption law, according to a report in *El Watan*, a local French-language newspaper, on June 17th. The charges concern the price for which contracts were awarded to Alstom, a French industrial conglomerate, and General Electric (GE) in 2007 for two 1,200 mw power stations. Alstom won the contract to build a plant at Terga for US$2.2bn, while GE charged US$2.3bn to build a facility at El Tarf. By comparison, in 2005, SNC-Lavalin, a Canadian engineering firm, agreed to build the 1,200 mw Hadjret Ennous power station at Tipasa for US$826m, and Sonelgaz's original budget for the two plants in total was US$3.4bn. Alstom and GE were asked at the time to submit reduced bids, but refused, according to *El Watan*. GE was also recently awarded a US$2.5bn contract to supply turbines for six power plants due to be delivered between 2015-17.

SNC-Lavalin blacklisted

Meanwhile, Sonelgaz has blacklisted SNC-Lavalin on suspicion of misconduct over the Tipasa contract. The company has been sanctioned "as a precaution" pending the conclusion of a judicial inquiry into the award of the contract, according to a statement by Mr Boutarfa, quoted in a report by the state news agency, Algérie Presse Service (APS), on June 11th. According to the report, the Canadian company is suspected of having given "bribes" to an intermediary in exchange for winning the contract. SNC-Lavalin has said that it will co-operate with any investigation but has not commented further. Sonelgaz, which is a 10% shareholder in the project company that carried out the Hadjret Ennous power plant, Sharikat Kahraba Hadjret Ennous (SKH), denied any wrongdoing, saying it had "signed nothing" with SNC-Lavalin. SKH is jointly owned by state companies and a holding company, Algerian Utilities International, which itself is 51% owned by SNC-Lavalin and Mubadala, an investment arm of the Abu Dhabi government. Mr Boutarfa has met his counterpart at SNC–Lavalin, Robert Card, who denied that the company had used an intermediary and that an inquiry carried out by the company had not uncovered any impropriety, the Sonelgaz chief told APS.

The case is part of a wider investigation into all the contracts awarded to SNC–Lavalin in Algeria during the 2005-12 mandate of the Sonelgaz vice-president, Riyad Benaissa. Mr Benaissa has been arrested and detained in Switzerland on charges of corruption. The other contracts under investigation include that for a power plant at Skikda and a gas treatment plant at Rhourde Nous near Adrar. Mr Card has said he is willing to co-operate with the inquiries "in Algiers and elsewhere". In April the World Bank banned the Canadian firm and its subsidiaries from competing for its contracts for a ten-year period for misconduct in a project in Bangladesh—the longest sanction ever imposed by the

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organisation.

Motivations for investigation

Even though the latest corruption investigations in Algeria have a very high profile, it is unlikely that they will be genuinely comprehensive. Corruption in the Algerian government's business deals is a sensitive issue. Senior state officials and members of a powerful conservative elite, known locally as *le pouvoir*, are widely believed to benefit from deals done with private companies, and power is still equated with patronage. The country ranked 105th of 176 in Transparency International's Corruption Perceptions Index (compared with 88th for Morocco and 118th for Egypt). Mr Bouteflika, has promised to eradicate corruption since the early days of his first term as president, which began in 1999, but with little determination, and little success. In the end, the first major corruption investigation—into contracts awarded by Sonatrach—was launched in 2010 by the Département du renseignement et de la sécurité , Algeria's intelligence service. The investigation appeared to target the relatively liberal allies of Mr Bouteflika, including the then energy minister, Chakib Khelil, who lost his job in the fall-out. The investigations may have been a backlash against attempts in the preceding years to make the country's business environment more open to foreign companies and a reminder to Mr Bouteflika to whom he owed his allegiance. The name of Mr Khelil has come up again in this latest round of investigations.

For all the limitations of the government's anti-corruption credentials, it appears that the current investigation is being carried out in earnest, and could have implications for those companies involved. Saipem, an Italian oil and gas services contractor, is still under investigation in Algeria and Italy for allegedly corrupt deals uncovered in the first round of investigations. Any direct action against Mr Khelil, though, seems unlikely. Despite allegations dating back to 2010 of his involvement in the awarding of corrupt contracts, he has not been made the subject of a judicial inquiry. There is speculation that this may be because other figures close to the regime, perhaps even including the president's brother, Said Bouteflika, were also involved. The removal of all of Sonatrach's senior executives in 2010 suggests that in the current investigation officials at Sonelgaz may be vulnerable. At a time when Algeria has embarked upon a rapid power-generation construction programme in order to meet growing demand and avoid the summer blackouts that are becoming increasingly common, the investigations could create difficulties for the country's power sector and affect confidence among foreign investors .

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