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INFORMATION

August 23, 1985

To: Members of the Executive Board
From: The Acting Secretary
Subject: Algeria - Staff Report for the 1985 Article IV Consultation

The following corrections have been made in SM/85/185 (6/27/85):

Page 2, 2nd para., line 4: for "54.2 billion" read "54.2 million"
for "32.2 billion" read "33.3 million"

Page 16, 1st full para., line 8: for "cars,...which"
read "cars and equipment goods which"

line 10: for "automobiles which"
read "imports of automobiles which"

Corrected pages are attached.

Att: (2)

Other Distribution:
Department Heads

INTERNATIONAL MONETARY FUND

ALGERIA

Staff Report for the 1985 Article IV Consultation

Prepared by the 1985 Staff Representatives for the 1985
Article IV Consultation with Algeria

Reviewed by the Committee on Article IV Consultations

Approved by A.D. Ouattara and S. Kanesa-Thanan

June 26, 1985

I. Introduction

The 1985 Article IV consultation discussions with Algeria were held in Algiers during the period April 23-May 6, 1985. The Algerian representatives included Mr. Benhamouda, Minister of Finance; Mr. Oubouzar, Minister of Planning; Mr. Bouraoui, Governor of the Central Bank; and other senior officials of ministries and agencies concerned with economic and financial matters. The staff representatives were Mr. E.L. Bornemann (head), Mr. F. Sacerdoti, Mr. I. Lienert, Mrs. L. Schmitz, Mr. L. Dicks-Mireaux (EP), all of the African Department, and Ms. J. Arnold (secretary-GEN). Mr. Salehkhoul, Executive Director for Algeria, attended the final policy discussions.

Algeria continues to avail itself of the transitional arrangements of Article XIV.

II. Recent Economic Developments and Policies

1. Background

Algeria is an important producer of hydrocarbons, and unlike other oil producers, it has achieved relatively rapid GDP growth in the early 1980s, despite the international recession and declining oil prices. This performance has been facilitated by a diversification of its export mix (away from crude oil and towards natural gas and condensate), and the development of a relatively large industrial sector. The economy is centrally planned with tight government controls over investment and imports, and a large number of public enterprises in producing and distribution activities. Beside providing nearly all export receipts, the publicly-owned hydrocarbon sector has been a major source of government revenue.

In the early 1980s, the Algerian authorities have introduced greater flexibility into economic management. In particular, public enterprises are being restructured, a greater role has been assigned to market prices, productivity has been boosted by a wage bonus system, some limited liberalization of imports has taken place, and finally, the development of complementary private sector activities has been encouraged.

2. Recent economic developments

Real GDP growth in 1984 is estimated to have accelerated to around 6 percent, ^{1/} the highest rate recorded in the 1980s (Table 1 and Chart 1). Crude oil production in 1984 rose for the first time since peak output of 54.2 million tons in 1978. At 33.3 million tons, output in 1984 reached the OPEC ceiling, nearly 40 percent below Algeria's 1978 output level. Production of refined petroleum products rose by 12 percent in 1984 to reach a new peak; in part this was due to increased gasoline refining capacity and a new production unit of bitumen and lubricants. Similarly, the opening of a new LPG production unit was responsible for a near doubling of LPG output. The increase in natural gas and condensate production slowed down in 1984, after having experienced particularly rapid growth during 1980-83.

GDP outside the hydrocarbon sector also grew more rapidly in 1984 than during the two preceding years. Manufacturing, construction, and public works increased rapidly, at 8-11 percent. The number of housing units completed in 1984 was 110,000, twice the level of completions in 1980. Finally, there was a rebound in agricultural output, following two years of decline induced in part by the droughts of 1982 and 1983. Concerning expenditure, both consumption and investment remained broadly stable as a percent of GDP; there was only a marginal increase in the resource surplus, to nearly 3 percent of GDP.

The increase in consumer prices as recorded by the official index, was 6.5 percent in 1984, somewhat higher than the 4.6 percent recorded in 1983. In part, this reflected the passing through to consumer prices of higher producer prices for agricultural crops in the 1983/84 season. The prices of bread, cereals and flour, were raised further in March 1985, by 15-33 percent. Minimum wages have been frozen since January 1983, but some wage-earners will receive increases in basic wages during 1985, back-dated to January 1, in accordance with the continuing implementation of a nationally harmonized salary scale applicable to all sectors of the economy.

^{1/} The Algerian authorities have not prepared national accounts in constant prices since the late 1970s. The data referred to are staff estimates, which are based on available production volume and price data.

around 9 percent. On the other hand, there is some reluctance to raise lending rates, which traditionally have been kept quite low; it is expected that this policy conflict will be resolved in coming months. The draft laws reform and codify the relationship between the commercial banks, the Central Bank, and the Treasury; the latter institution has so far played a fundamental role in financial intermediation in Algeria. There will be an increased role for the commercial banks, especially for the provision of medium-sized investment credits. These are presently provided by the Algerian Development Bank (BAD), which in turn is funded by long-term loans from the Treasury. Finally, a new bank specializing in finance for local authorities is being created, in addition to the agricultural sector bank established in 1982. This will enhance further the aim of widening the network of banks within the country.

With regard to the availability of monetary statistics, the creation of the agricultural sector bank had resulted in important delays in the provision of estimates for monetary aggregates for 1983 and 1984, and the unavailability of quarterly data for 1984. The mission was assured that the creation of another new bank would not create similar difficulties, and that the reporting of monetary aggregates would improve during 1985.

3. External policies and prospects

Commenting on export prospects for 1985 and beyond, the Algerian representatives expect further diversification away from crude oil and refined petroleum products. Exports of crude oil will fall again in 1985, due to a 9 percent decline in Algeria's OPEC quota to 663,000 barrels per day. New extraction facilities will allow an expansion of condensate exports as from late 1985. LNG exports are expected to increase rapidly in 1985-86 due to expanded sales to major European clients; the Algerian representatives were also confident that a presently-inoperative contract with a large non-European customer will be successfully renegotiated. Work is underway on the construction of additional gas pipelines in Algeria to enable sales to Italy to reach the full contract level of 12.5 billion m³ of natural gas in 1986 (slightly over half this amount was exported in 1984). In total, hydrocarbon exports during the 1985-89 plan period are projected at 4 percent volume growth per annum. The Algerian representatives stressed that this projection is at the lower end of possible scenarios. Export receipts in 1985-86 will also be boosted by two equal retroactive payments from Spain amounting to US\$250 million in each year; these result from the final settlement of a dispute concerning a 1975 contract. The staff team expressed doubt that nonhydrocarbon exports would increase by 20 percent per annum, as projected in the 1985-89 Plan. The Algerian representatives recognize that at the present time, they have

few products of adequate quality and price to export. Nonetheless, they indicated that action is being considered to raise the quality of domestically produced goods, to lighten export procedures, to extend bilateral trade agreements, and if necessary, to subsidize producers of exportables.

Imports are programmed to remain stable in dinar terms in 1985. The Algerian representatives explained that the stabilization of imports is possible because of continuing increases in domestic production of import substitutes. Moreover, they indicated that actual imports are likely to be close to planned imports in 1985 because of improvements in program execution by importing public enterprises. Since early 1983, the authorities have encouraged the importation of cars and equipment goods which are financed from abroad. As a result, there was a strong expansion in 1983-84 of imports of automobiles which are financed by workers' savings abroad. The Algerian authorities view this development favorably, as it is an alternative method of channelling workers' remittances toward the country, thereby reducing the burden on official foreign exchange resources. For the same reason, the limit applicable to imported equipment goods without official foreign exchange payment was raised from DA 100,000 to DA 200,000 in the 1985 budget. However, the Algerian authorities stated that the external constraints are likely to require continuing tight control over the planning of imports in the medium-term. The projected annual 6 percent growth rate for imports must be seen as a maximum, and could be lower depending upon export prospects and prospective capital flows.

A significant feature concerning invisible transactions is a likely decline in interest payments on foreign debt over the medium-term, reflecting the Government's policy of reducing outstanding external debt and also lower interest rates in international capital markets. In sum, the current account surplus may increase to nearly 1 percent of GDP in 1985. Such a surplus could continue thereafter, assuming there are no major adverse disturbances in world oil markets, and provided Algeria exercises flexibility in pricing arrangements in order to increase the volume of gas exported.

The staff team inquired about recent and prospective borrowing policies. The Algerian representatives pointed out that the country had returned to the international capital markets in 1983-84 because borrowing conditions were considered to be favorable. They cited as an example the latest loan of US\$600 million concluded in early 1985; it carries an interest rate of 1/2 a percentage point over LIBOR, and has a grace period for 5 years. They stressed that the Government was firmly committed to reducing foreign debt levels, but at the same time, external reserves will be maintained at an adequate level in terms of flows of imports.