

ALGERIA



ECONOMIC UPDATE

Continuing the
Diversification
Effort

Fall 2023



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Middle East & North Africa

Algeria Economic Update

Continuing the Diversification Effort

Fall 2023



Middle East and North Africa Region

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LIST OF ACRONYMS

BoA	Bank of Algeria	NEER	Nominal effective exchange rate
BTU	British thermal unit	OAIC	Algerian Interprofessional Office of Cereals
CPI	Consumer Price Index	OECD	Organization for Economic Cooperation and Development
DZD	Algerian Dinar	ONS	National Statistical Office
EIA	Energy Information Agency	OPEC	Organization of Petroleum Exporting Countries
EUR	Euro	GDP	Gross Domestic Product
EPT	Administrative regions	Pp	Percentage points
FAO	Food and Agriculture Organization	PSR	Special refinancing program
IMF	International Monetary Fund	REER	Real effective exchange rate
FRR	Revenue Regulation Fund	SMMEEI	Steel, metal, mechanical, electrical and electronic industries
LNG	Liquefied natural gas	SOE	Public economic enterprises – should be SOE
LPG	Liquefied petroleum gas	TTF	Securities Transfer Facility
IDE	Foreign direct investment	US\$	United States Dollar
JODI	Joint Initiative on Organizational Data	WB	World Bank
Kb/d	Thousands of barrels per day		
MARS	Monitoring Agricultural Resources		
Mb/d	Millions of barrels per day		
MENA	Middle East and North Africa		
Mtoe	Million tons of oil equivalent		

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This Algeria Economic Update reports on the main recent economic developments and policies. It places them in a global and longer-term context and assesses the implications of these developments and policy changes for Algeria's economic prospects. The report is intended for a broad audience, including policymakers, business leaders, financial market participants, and the community of analysts and professionals working in/on Algeria. The report is divided into two chapters. Chapter 1 presents macroeconomic developments in Algeria over the year 2022 and the first half of 2023, while Chapter 2 describes the short- and medium-term outlook for the Algerian economy. **The deadline for data entry and forecast preparation was September 22, 2023.**

The Algeria Economic Update is the work of the Middle East and North Africa (MENA) section of the World Bank's Macroeconomics, Trade, and Investment (MTI) practice area. It was prepared by Cyril

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EXECUTIVE SUMMARY

Algeria's GDP recovered to its pre-pandemic level in 2022, while high oil and gas prices allowed for marked improvements in its external and fiscal balances. After GDP fell by 5.1 percent in 2020, hydrocarbon output recovered to its 2019 level in 2021, while nonhydrocarbon output recovered in 2022. Despite this recovery in levels, however, GDP is yet to return to its pre-pandemic trend. The current account and fiscal deficits averaged over 10 percent prior to the pandemic, but as oil and gas prices gradually increased after 2020, Algeria's current account deficit narrowed in 2021 and posted a record surplus in 2022, while its fiscal deficit shrunk to its lowest level in a decade, allowing for a replenishment of foreign exchange reserves and budget savings. Meanwhile, inflation accelerated from 2.4 percent in 2020 to 9.3 percent in 2022, driven by food prices.

The recovery continued during the first half of 2023, albeit at a slower pace, supported by nonhydrocarbon activity and investment. GDP growth decelerated slightly in Q1-2023 (+3.0 percent y-o-y), supported by robust nonhydrocarbon growth (+4.0 percent y-o-y) driven by strong investment spending. While this stimulated the construction and industrial sectors, services activity slowed in line with private consumption, while agricultural output was subdued amid droughts. Nightlights data suggests lower but continued dynamic nonhydrocarbon growth in Q2-2023. On the other hand, hydrocarbon production increased moderately, and exports fell in H1-2023, as higher gas output offset declining oil production, amidst lower OPEC quotas.

Oil and natural gas prices and exports declined in H1-2023, adding pressure on external and fiscal balances. After the current account posted a US\$ 19 billion surplus in 2022 (9.8 percent of GDP), a US\$ 7.7 billion decline in hydrocarbon exports in H1-2023 relative to H2-2022, combined with a recovery in equipment imports, reduced it to US\$ 2.9 billion. Foreign exchange reserves kept rising, reaching 17.2 months of imports at end-June 2023. After the fiscal deficit narrowed from 7.2 percent in 2021 to 2.9 percent in 2022, it is expected to have widened again in H1-2023, as declining hydrocarbon budget revenues outweighed increasing tax revenues, and spending growth remained elevated due to civil service wage increases and higher transfers, maintaining pressure on public investment. Public debt reached 55.6 percent of GDP at end-2022 and increased in H1-2023, but so did Treasury savings, reducing the financing gap.

Inflation remained elevated, reaching 9.7 percent in H1-2023, now driven by fresh food prices, mostly produced domestically. The prices of the latter increased by 24.1 percent y-o-y, amidst another dry winter, making up 43 percent of H1-2023 inflation. After the Bank of Algeria put an end to fourteen consecutive years of depreciation in H2-2022 to curb imported inflation, the dinar stabilized in H1-2023. Monetary policy has remained unchanged since the reserve requirement was increased April 2023, and money supply growth tapered in Q2-2023. Credit growth to the private sector remained subdued, while that to SOEs accelerated slightly. As part of the government's

purchasing power protection program, civil service wages and transfers are increasing again in 2023, along with state control and scrutiny over food prices.

Growth is expected to recover in 2024 and 2025, while the fiscal and external balances would stabilize after an initial drop. GDP growth would increase to 2.6 percent in 2024, with hydrocarbon output growing moderately as OPEC quotas and European gas demand recover. Investment growth would remain robust as large investment projects move forward, and keep supporting industrial activity, service activity would remain dynamic, and agricultural production would recover. Inflation is expected to decline gradually in 2024 and 2025 owing to a return to normal rainfall and more moderate growth in money supply, public spending, and import prices. After it shrinks in 2023, the current account balance would remain positive in 2024 and 2025, as export and import volumes stabilize. Driven by lower hydrocarbon revenues and higher current spending, the fiscal deficit is expected to widen in 2023 and 2024 before narrowing. The public debt-to-GDP ratio would increase moderately, with oil savings partially financing the fiscal deficits.

The macroeconomic outlook hinges on volatile hydrocarbon prices, and the regional context underscores the reality of the climate risks to which Algeria is also exposed. Authorities have built more foreign exchange reserves and oil savings, which strengthened the medium-term resilience of the

Algerian economy, while higher gas prices and rising oil prices in H2-2023 could extend the hydrocarbon windfall. Nonetheless, the risks of structural macroeconomic imbalances remain large, as GDP, exports and budget revenues remain sensitive to global oil prices, generating both upside and downside risks for Algeria's growth, external and public finance outlook, amidst an uncertain global geopolitical context. Lastly, recent extreme natural events in the region, together with Algeria's own experience, highlight the risks that they pose for the country's agricultural sector and economic outlook.

These risks underscore the importance of sustainably improving macroeconomic balances, while continuing efforts to foster private sector-led investment, growth, and diversification. Diversifying export revenues away from hydrocarbons and attracting foreign investment would improve Algeria's resilience to oil and gas price fluctuations. On the fiscal front, higher spending rigidity contrasts with volatile hydrocarbon revenues, generating significant uncertainty. This underlines the need to raise more tax revenues and strengthen spending efficiency in an equitable way, notably that of public investment. Consistent with the 2021 Government Action Plan, continued implementation of reforms to stimulate private investment and enable the formalized private sector to become the engine of sustainable and diversified growth remains essential to the performance and resilience of the Algerian economy.



RÉSUMÉ ANALYTIQUE

Le PIB de l'Algérie a retrouvé son niveau pré-pandémique en 2022, tandis que les prix élevés du pétrole et du gaz ont permis d'améliorer sensiblement les soldes extérieur et budgétaire. Après une chute du PIB de 5,1 % en 2020, la production d'hydrocarbures a retrouvé son niveau de 2019 en 2021, tandis que la production hors hydrocarbures l'a retrouvé en 2022. Malgré cette reprise en niveau, le PIB n'a pas encore retrouvé sa trajectoire pré-pandémique. Les déficits du compte courant et budgétaire atteignaient en moyenne plus de 10% du PIB avant la pandémie, mais l'augmentation progressive des prix du pétrole et du gaz après 2020 a permis au déficit du compte courant de se réduire en 2021 et d'afficher un excédent record en 2022, alors que le déficit budgétaire atteignait son niveau le plus bas en dix ans, permettant de reconstituer les réserves de change et l'épargne du Trésor. Dans le même temps, l'inflation s'est accélérée de 2,4% en 2020 à 9,3 % en 2022, sous l'effet de la hausse des prix des produits alimentaires.

La reprise s'est poursuivie au S1-2023, bien qu'à un rythme plus modéré, soutenue par l'activité hors-hydrocarbures et l'investissement. La croissance du PIB a légèrement ralenti au cours du T1-2023 (+3,0% en g.a.), soutenue par une croissance hors-hydrocarbures robuste (+4,0% en g.a.) tirée par le dynamisme de l'investissement. Cela a stimulé les secteurs de la construction et de l'industrie, tandis que l'activité des services a ralenti suivant

la consommation privée, tout comme la production agricole dans un contexte de faible pluviométrie. Les données d'éclairage nocturne suggèrent une croissance hors hydrocarbures moins élevée mais toujours dynamique au T2-2023. Par ailleurs, la production d'hydrocarbures a connu une hausse modérée et les exportations ont diminué au S1-2023, la hausse de la production de gaz compensant la baisse volontaire des quotas de production de pétrole.

Les prix et les exportations de pétrole et de gaz naturel ayant baissé au S1-2023, les pressions sur les équilibres extérieur et budgétaire s'est accrue. Après que le compte courant ait enregistré un excédent de 19 G\$ US en 2022 (9,8 % du PIB), une baisse des exportations d'hydrocarbures de 7,7 G\$ US au S1-2023 par rapport au S2-2022, combinée à une reprise des importations d'équipements, l'a ramené à 2,9 G\$ US. Les réserves de change ont continué à augmenter, atteignant 17,2 mois d'importations à la fin-juin 2023. Après une réduction du déficit global du Trésor de 7,2 % du PIB en 2021 à 2,9 % en 2022, il est attendu qu'il se soit creusé au S1-2023. La baisse des recettes des hydrocarbures a dépassé l'augmentation des recettes fiscales, et la croissance des dépenses est demeurée élevée en raison de l'augmentation des salaires dans la fonction publique et celle des transferts, maintenant une pression sur l'investissement public. La dette publique a atteint 55,6 % du PIB à la fin 2022 et a augmenté au S1-2023, mais l'épargne du Trésor a également augmenté, réduisant ainsi les besoins de financement.

L'inflation reste élevée, atteignant 9,7% au S1-2023, désormais tirée par le prix des produits agricoles frais, principalement produits localement. Le prix de ces derniers a augmenté de 24,1% en g.a. dans le contexte d'un autre hiver sec, expliquant 43% de l'inflation au S1-2023. Après que la Banque d'Algérie ait mis fin à quatorze années consécutives de dépréciation au S2-2022 pour limiter l'inflation importée, le dinar s'est stabilisé au S1-2023. La politique monétaire est restée inchangée depuis l'augmentation du taux de réserves obligatoires en avril 2023, et la croissance de la masse monétaire a ralenti au T2-2023. La croissance du crédit au secteur privé est restée modeste, tandis que celle aux entreprises publiques s'est légèrement accélérée. Les salaires dans la fonction publique et les transferts ont augmenté à nouveau en 2023, dans le cadre du programme triennal de protection du pouvoir d'achat du gouvernement, tandis que le contrôle et la surveillance des prix des produits alimentaires par l'État se sont accrus.

La croissance devrait être plus élevée en 2024 et 2025, tandis que les soldes budgétaire et extérieur se stabiliseraient après une baisse initiale. La croissance du PIB atteindrait 2,6 % en 2024, la production d'hydrocarbures augmentant modérément suivant la reprise des quotas de l'OPEP et celle de la demande européenne en gaz. L'investissement demeurerait robuste grâce à la progression de grands projets et continuerait à soutenir l'activité industrielle, l'activité des services resterait dynamique et la production agricole devrait se redresser. L'inflation diminuerait progressivement en 2024 et 2025, grâce au retour à un niveau normal de pluviométrie et à une croissance plus modérée de la masse monétaire, des dépenses publiques et des prix à l'importation. Après une contraction en 2023, la balance du compte courant resterait positive en 2024 et 2025, les volumes exportés et importés se stabilisant. Sous l'effet de la baisse des recettes d'hydrocarbures et de l'augmentation des dépenses courantes, le déficit budgétaire se creuserait en 2023 et 2024 avant de se résorber. Le ratio dette publique sur PIB augmenterait modérément, l'épargne pétrolière finançant partiellement les déficits budgétaires.

Les perspectives macroéconomiques demeurent tributaires des prix volatiles des hydrocarbures, et le contexte régional souligne la réalité des risques climatiques auxquels l'Algérie est également exposée. Les autorités ont constitué davantage de réserves de change et d'épargne pétrolière, renforçant la résilience à moyen terme de l'économie algérienne, tandis que l'augmentation des prix du gaz et la hausse des prix du pétrole au cours du S2-2023 pourraient prolonger la manne des hydrocarbures. Néanmoins, les risques de déséquilibres macroéconomiques structurels restent importants car le PIB, les exportations et les recettes budgétaires demeurent sensibles aux prix mondiaux du pétrole, générant des risques haussiers et baissiers pour les perspectives de croissance, les équilibres extérieurs et les finances publiques, dans un contexte géopolitique mondial incertain. Enfin, les phénomènes naturels extrêmes récents dans la région, ainsi que l'expérience algérienne, soulignent les risques que ceux-ci font peser sur le secteur agricole et les perspectives économiques du pays.

Ces risques soulignent l'importance de l'amélioration durable des équilibres macroéconomiques, et de la poursuite des efforts visant à encourager l'investissement privé, la croissance et la diversification. La diversification des recettes d'exportation hors-hydrocarbures et l'attraction des investissements étrangers amélioreraient la résilience externe face aux fluctuations des prix du pétrole et du gaz. Sur le plan budgétaire, la rigidité des dépenses courantes contraste avec la volatilité des recettes venant des hydrocarbures, générant une forte incertitude. Cela souligne l'importance de la mobilisation accrue des recettes fiscales et d'une meilleure efficacité des dépenses, notamment celle de l'investissement public. En cohérence avec le Plan d'Action du Gouvernement de 2021, l'accélération de la mise en œuvre des réformes visant à stimuler l'investissement privé et à permettre au secteur privé formel de devenir le moteur d'une croissance durable et diversifiée demeure essentielle à la performance et à la résilience de l'économie algérienne.

ملخص تنفيذي

احتياطات الصرف في الزيادة، حيث وصلت إلى 17.2 شهر من الواردات في نهاية جوان 2023. بعد انخفاض العجز الإجمالي للجزيرة من 7.2% من الناتج المحلي الإجمالي في عام 2021 إلى 2.9% في عام 2022 إلا أنه من المتوقع أن يرتفع العجز مرةً أخرى في النصف الأول من عام 2023 وذلك لأن إيرادات قطاع المحروقات انخفضت بنسبة تفوق الزيادة في الإيرادات الجبائية، وظل نمو الإنفاق مرتفعاً بسبب الزيادات في رواتب الموظفين العمومي والتحويلات، هذه العوامل مجتمعة ساهمت في الحد من الاستثمار العمومي. بلغ الدين العمومي 55.6% من الناتج المحلي الإجمالي في نهاية عام 2022 وارتفع في النصف الأول من عام 2023، لكن مدخرات الخزينة زادت أيضاً مما قلل من الاحتياجات التمويلية.

لا يزال التضخم مرتفعاً، حيث وصل إلى 9.7% في النصف الأول من عام 2023، و يُعزى الأمر حالياً إلى ارتفاع أسعار المنتجات الزراعية الطازجة وبشكلٍ أخص المحلية منها. ارتفعت أسعار هذه المنتجات بنسبة 24.1% سنوياً بعد شتاءٍ آخر جاف، مما يفسر 43% من التضخم في النصف الأول من 2023. في النصف الثاني من عام 2022 وبعد أن استطاع بنك الجزائر الحد من انخفاض قيمة العملة والتي استمرت أربعة عشر عاماً نتيجة التضخم المستورد، أسفر عن هذه الخطوة استقرار الدينار الجزائري في النصف الأول من عام 2023. لم يطرأ أي تغيير على السياسة النقدية منذ زيادة نسبة متطلبات الاحتياطي في أبريل 2023، وتباطأ نمو التدفق النقدي في الربع الثاني من عام 2023. وظل نمو الائتمان الممنوح للقطاع الخاص متواضعاً في حين تسارع نمو الائتمان الممنوح للمؤسسات العمومية بشكلٍ طفيف. كما سيتم زيادة رواتب الموظفين العمومي والتحويلات الاجتماعية مرةً أخرى في عام 2023 في إطار البرنامج الثلاثي للحكومة لحماية القدرة الشرائية، ذلك بجانب تشديد مراقبة الحكومة والسيطرة على أسعار المواد الغذائية.

ومن المتوقع أن يكون النمو أعلى في عامي 2024 و2025، في حين تستقر أرصدة الميزانية و المبادلات الخارجية بعد الانخفاض الأولي. وسيصل نمو الناتج المحلي الإجمالي إلى 2.6% في عام 2024 وذلك تزامناً مع زيادة إنتاج قطاع المحروقات بشكل معتدل بعد تحسن الطلب الأوروبي على الغاز وحصص أوبك. ومن المتوقع أيضاً أن يحافظ الاستثمار على قوته بفضل التقدم المحرز في المشاريع الكبرى، وأن يستمر في دعم النشاطات الصناعية،

استطاع الناتج المحلي الإجمالي للجزائر أن يسترجع مستواه لما قبل الجائحة في عام 2022، بينما ساعدت أسعار النفط والغاز المرتفعة في تحسين الأرصدة الخارجية والميزانية بشكل كبير. بعد انخفاض الناتج المحلي الإجمالي بنسبة 5.1% في عام 2020، عاد إنتاج المحروقات إلى مستوى عام 2019 في عام 2021، بينما استعاد الإنتاج خارج المحروقات مستواه في عام 2022. وعلى الرغم من هذا الانتعاش في المستوى، لم يستعيد بعد الناتج المحلي الإجمالي المسار الذي كان عليه ما قبل الجائحة. وبلغ معدلي العجز في الحساب الجاري والميزانية أكثر من 10% من الناتج المحلي الإجمالي قبل الوباء، ولكن ارتفاع أسعار النفط والغاز تدريجياً بعد عام 2020، ساعد على تخفيف العجز في الميزان التجاري في عام 2021 وتحقيق فائض قياسي في عام 2022، بينما انخفض عجز الميزانية إلى أدنى مستوى له منذ عشر سنوات، مما دعم احتياطات الصرف ورصيد المدخرات. في الوقت نفسه، أدى ارتفاع أسعار المواد الغذائية إلى ارتفاع نسبة التضخم من 2.4% في عام 2020 إلى 9.3% في عام 2022. استمر الانتعاش الاقتصادي في النصف الأول من عام 2023 وإن كان بوتيرة أبطأ، وذلك بفضل نشاط قطاع خارج المحروقات والاستثمار. خلال الربع الأول من عام 2023 تراجع نمو الناتج المحلي الإجمالي قليلاً (+3.0% سنوياً)، مستنداً على النمو القوي لإنتاج قطاع خارج المحروقات (+4.0% سنوياً) بسبب الاستثمار النشط. حفز ذلك قطاعات البناء والصناعة، في حين تباطأ نشاط الخدمات تالياً الاستهلاك الخاص والإنتاج الزراعي في ظل الجفاف وقلة الأمطار. أن البيانات الصادرة عن الإضاءة الليلية تشير إلى نمو بوتيرة أبطأ خلال الربع الثاني من عام 2023. من ناحية أخرى، شهد إنتاج قطاع المحروقات ارتفاعاً نسبي، وانخفضت الصادرات في النصف الأول من عام 2023، بحيث أن الزيادة في إنتاج الغاز قامت بتعويض الانخفاض الطوعي في حصص إنتاج النفط.

مع انخفاض أسعار وصادرات النفط والغاز الطبيعي في النصف الأول من عام 2023 زاد الضغط على توازوني الميزانية والميزان الخارجي. بعد أن سجل الحساب الجاري فائضاً قدره 19 مليار دولار أمريكي في عام 2022 (9.8% من الناتج المحلي الإجمالي) إلا أنه انخفض إلى 2.9 مليار دولار أمريكي، ويعزى السبب إلى انخفاض صادرات المحروقات بمقدار 7.7 مليار دولار أمريكي في النصف الأول من عام 2023 (مقارنة بالنصف الثاني من عام 2022) وإلى استئناف استيراد المعدات والآليات. استمرت

كبير بأسعار النفط العالمية مما يولد مخاطر ايجابية او سلبية على آفاق النمو وعلى المالية العامة و التوازنات الخارجية ، في سياق جيوسياسي عالمي غير مستقر. وأخيرا، فإن الظواهر الطبيعية الحادة التي شهدتها المنطقة مؤخرا، إضافة الى تجربة الجزائر مع هذه الظواهر، تسلط الضوء على المخاطر التي يمكن أن تسببها هذه التغييرات الطبيعية على القطاع الزراعي و التوقعات الاقتصادية للبلاد.

تؤكد هذه المخاطر على أهمية الإستدامة في تعزيز التوازن في الاقتصاد الكلي، بجانب التأكيد على دور القطاع الخاص في قيادة الاستثمار وتعزيزه وتنويعه. إن من شأن تنويع الإيرادات من الصادرات خارج المحروقات وجذب الاستثمار الأجنبي القدرة على تعزيز صمود الاقتصاد الجزائري أمام التقلبات في أسعار النفط والغاز. وعلى صعيد المالية ، تتناقض صلابة النفقات الجارية مع تقلب إيرادات النفط والغاز، مما يولد قدرا كبير من عدم اليقين. وهذا يؤكد الحاجة إلى جمع المزيد من الإيرادات الجبائية وتعزيز كفاءة الإنفاق ، ولا سيما الاستثمار العمومي. وماشيا مع مخطط عمل الحكومة لعام 2021، فإن مواصلة تنفيذ الإصلاحات الرامية إلى تحفيز الاستثمار الخاص وتمكين القطاع ليكون المحرك الأساسي للنمو المستدام والمتنوع يبقى ضرورياً لصمود الاقتصاد الجزائري وادائه الفعّال.

وأن يظل قطاع الخدمات نشيطاً، التعافي المتوقع للإنتاج الزراعي. ومن المتوقع أن ينخفض التضخم تدريجياً في عامي 2024 و2025، وذلك بفضل العودة إلى المستوى الطبيعي من الأمطار والنمو المعتدل في التدفق النقدي والإنفاق العام وأسعار الواردات. وبعد الانكماش في عام 2023، سيظل رصيد الحساب الجاري إيجابيا في عامي 2024 و2025، مع استقرار أحجام الصادرات والواردات..وبتأثير انخفاض إيرادات المحروقات وزيادة النفقات الجارية، من المتوقع أن يتسع عجز الميزانية في عام 2023 و 2024 قبل أن ينخفض. وستظل نسبة الدين العمومي إلى الناتج المحلي الإجمالي مستقرة، والادخار النفطي يمول جزئياً عجز الميزانية.

تستند توقعات الاقتصاد الكلي بشكل كبير على أسعار المحروقات المتقلبة ويسلط السياق الإقليمي الضوء على حقيقة المخاطر المناخية التي تتعرض لها الجزائر أيضا. قامت السلطات الجزائرية بتقوية احتياطات الصرف ورفع من المدخرات النفطية الأمر الذي أدى إلى تعزيز صمود الاقتصاد الجزائري على المدى المتوسط، في حين أن ارتفاع في أسعار الغاز و النفط خلال النصف الثاني من العام 2023 قد يطيل أمد مكاسب قطاع المحروقات. ومع ذلك تبقى مخاطر إختلال بنية الاقتصاد الكلي كبيرة ذلك أن الناتج المحلي الإجمالي والصادرات وإيرادات الميزانية مرتبطة بشكل



RECENT ECONOMIC DEVELOPMENTS

Strong Nonhydrocarbon Output Growth Continued in H1-2023

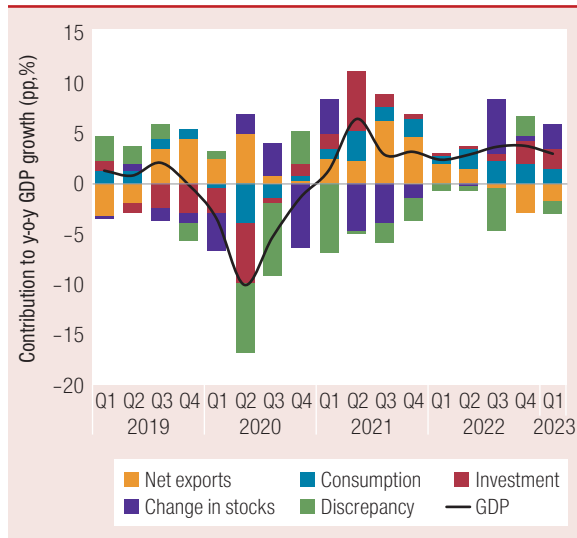
Dynamic Nonhydrocarbon output growth continued into H1-2023, albeit at a slower pace, supported by investment and government consumption. Nonhydrocarbon GDP expanded by 4.3 percent in 2022, the strongest growth rate since 2015, and output surpassed its pre-pandemic level. Along with a slight decrease in hydrocarbon output (-0.6 percent), GDP growth reached 3.2 percent. Dynamic nonhydrocarbon growth extended into Q1-2023 (+4.0 percent y-o-y). Driven by rapid civil service wage and social spending increases, public consumption grew at its fastest rate in five years (+3.0 percent y-o-y) and compensated for decelerating private consumption (+2.1 percent y-o-y). Strong investment growth in Q4-2022 extended to Q1-2023 (+5.2 percent y-o-y), despite a slowdown in public investment. Combined with a 1.4 percent y-o-y increase in hydrocarbon output, overall growth decelerated to 3.0 percent in Q1-2023. Nightlights data also suggest slower but continued dynamic

nonhydrocarbon activity growth in Q2-2023, driven by strong growth in the North-Center and North-West regions (Figures 1 and 2).

Strong investment growth stimulated the construction and industrial sectors, but subdued rainfall constrained agricultural output. After a strong rebound in 2022, Q1-2023 agricultural output growth slowed down to 2.2 percent, and crop development was below average at the end of the winter harvest (Q2-2023), following rainfall deficit over the winter in most wilayas.¹ Responding to investment growth, construction output accelerated to 4.9 percent y-o-y in Q1-2023, supporting the recovery of other industrial sectors, including steel, metal, mechanical, electrical and electronic industries (SMMEEI), construction materials, chemicals, water and energy, and wood and paper. Nonetheless,

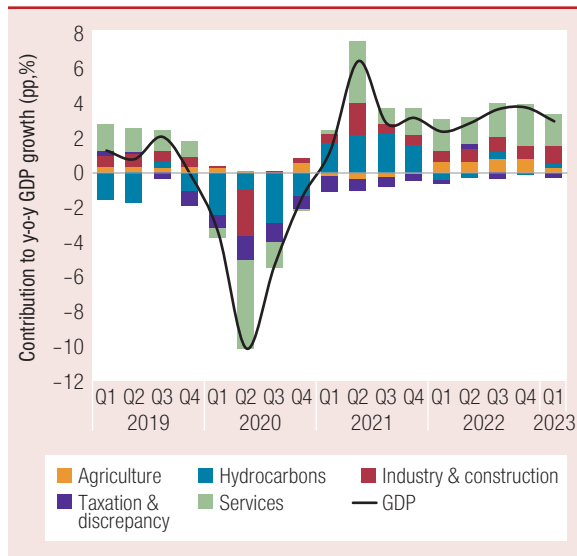
¹ Anomaly Hotspots of Agricultural Production (ASAP) satellite estimates produced by the European Commission's Joint Research Centre (JRC) indicate that below-average rainfall has caused cereal biomass to be below average in the large majority of wilayas.

FIGURE 1 • Investment supported dynamic nonhydrocarbon sector growth in Q1-2023...



Source: Office National des Statistiques (ONS) and World Bank (WB) estimates.

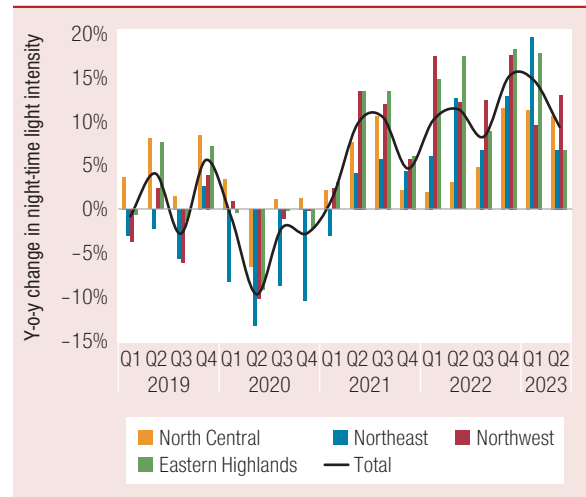
FIGURE 3 • Dynamic industrial activity supported growth...



Source: ONS and WB estimates.

state-owned enterprise (SOE) manufacturing activity remained markedly below pre-pandemic levels, in contrast to the full recovery in the private manufacturing sector. As private consumption decelerated in Q1-2023, commercial service growth also slowed (+4.4 y-o-y), yet it remains the main contributor to growth (Figures 3 and 4).

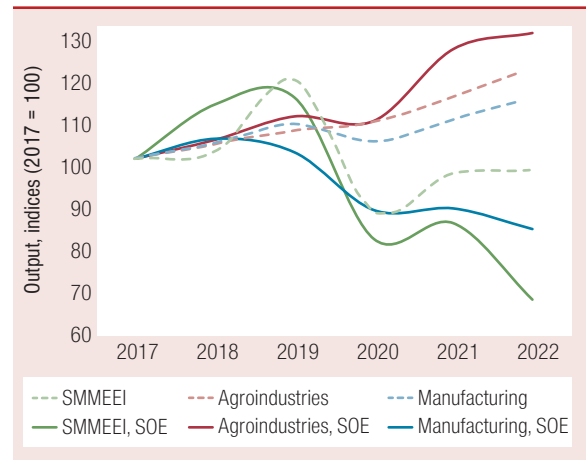
FIGURE 2 • ...and nightlights data suggest continued dynamism in Q2-2023



Source: NASA and WB estimates.

Note: Nightlights data, adjusted for the impact of oil and gas activity, are robust leading indicators of economic activity (World Bank, 2023a). The regions correspond to the Espaces de Programmation Territoriale (EPT).

FIGURE 4 • ...but did not allow for a recovery in SOE manufacturing



Source: ONS and WB estimates.

Note: Total activity uses real GDP and activity of state-owned enterprises (SOE) uses the industrial production index. SOEs represent 29 percent of manufacturing activity and are mostly active in the SMMEEI (45 percent), agro-industrial (23 percent) and construction material (21 percent) sectors.

Reductions in Oil Production Contrasted with Growth in Natural Gas Output in H1-2023

Owing to OPEC production cuts, oil production and exports decreased in H1-2023. Oil production took two years to recover from the quota reductions decided

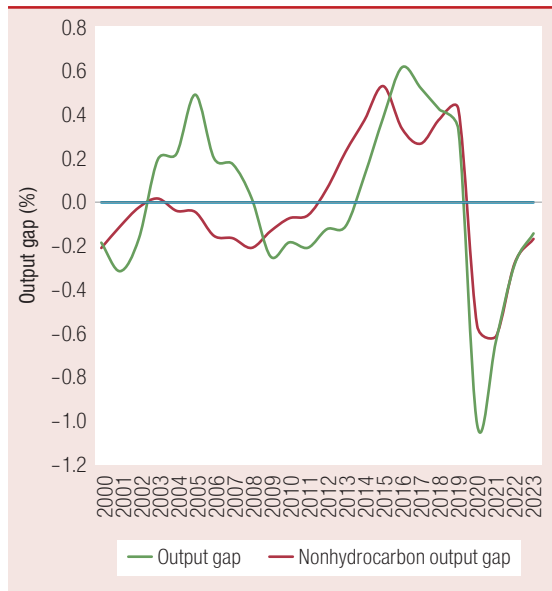
BOX 1: CATCHING UP WITH THE PRE-COVID GROWTH TREND

Like in the rest of the world, the COVID-19 pandemic led to a deep recession in Algeria. GDP contracted by 5.1 percent in 2020 as private consumption fell amid lockdowns and capital expenditures decreased drastically. Industrial output (-3.1 percent) and services (-4.3 percent) were hit especially hard by the lockdowns. The concurrent global recession reduced the demand for and prices of hydrocarbon exports, leading OPEC and Algeria to lower oil production quotas.

Algeria's overall and nonhydrocarbon GDP recovered to pre-pandemic levels by 2022. Hydrocarbon GDP recovered to its pre-pandemic level by 2021, and nonhydrocarbon output by 2022. Private consumption recovered by 2021 as the economy reopened, supporting the recovery of services by 2022. Although government investment has remained below pre-pandemic levels since 2020, the private investment recovery has stimulated industrial output, which exceeded its 2019 level by 2021.

GDP could exceed its pre-pandemic trend by 2024, thanks to stronger-than-expected hydrocarbon output. Although the level of GDP recovered to its pre-pandemic level by 2022, Bank projections suggest that real GDP would match what it would have been under the pre-pandemic growth trend by 2024. Despite a marked recovery in 2021 and 2022, the output gap remains negative, and GDP below potential. Looking ahead, nonhydrocarbon GDP is likely to have incurred a long-term loss in level due to the COVID-19 pandemic, similar across the agricultural, industrial and services sectors. In other words, growth would need to be stronger for nonhydrocarbon GDP to match what it would have been absent the COVID-19 pandemic. On the other hand, Europe's natural gas sourcing shift away from Russia has allowed for stronger natural gas output and is expected to allow a stabilization in hydrocarbon GDP, breaking its pre-pandemic downward trend.

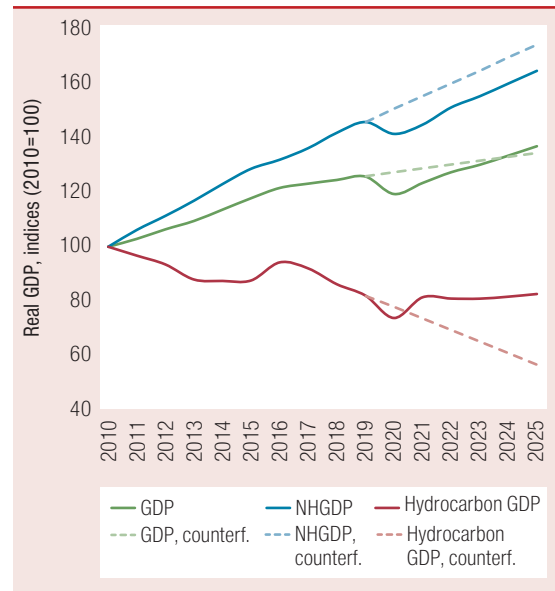
FIGURE 5 • The output gap remained slightly negative in 2022...



Source: ONS and WB estimates and projections for 2023.

Note: Output gap estimated based on 1974–2022 data and 2023–2025 forecasts using a Hodrick-Prescott (HP) filter with a smoothing parameter of 100.

FIGURE 6 • ...while real GDP could catch up with its pre-pandemic trajectory by 2024



Source: ONS and WB estimates and projections for 2023–2025.

Note: NH = nonhydrocarbon. Counterf. = Counterfactual, relative to a pre-pandemic trend estimated using a linear extrapolation of 2016–2019 data.

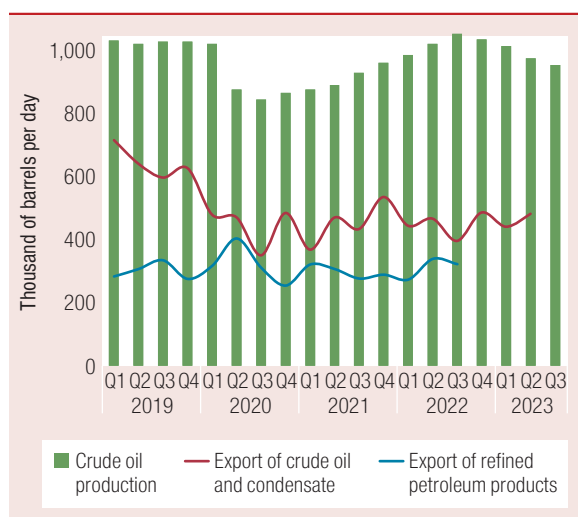
during the COVID-19 pandemic, reaching its pre-pandemic level in Q2-2022. Since then, OPEC decided on voluntary oil output quota reductions to support falling prices, with Algeria reducing its quota from 1055 kb/d in October 2022 to 1007 kb/d in November and to 959 kb/d in May 2023. The government also announced a further 20,000 barrels per day cut for the month of August 2023, reducing output to 939 kb/d for

one month.² As a result, oil production fell by 3.6 percent q-o-q in Q2-2023, and was 5.7 percent lower compared to its Q3-2022 peak.³ Oil tanker tracker data suggests, however, that crude oil exports remained stable in H1-2023 while condensates exports surged,

² APS (July 3, 2023).

³ OPEC Monthly Oil Market Report, August 10, 2023.

FIGURE 7 • OPEC quota cuts have limited oil production and exports...



Source: Bank of Algeria (BoA) for exports to Q3-2022, Organization of Petroleum Exporting Countries (OPEC) for crude oil production, WB estimates using Bloomberg Tanker Tracker data for exports for Q4-2022, Q1-2023 and Q2-2023.

suggesting a decline in refined petroleum production and exports, with the latter being exacerbated by rising domestic consumption (Figure 7).

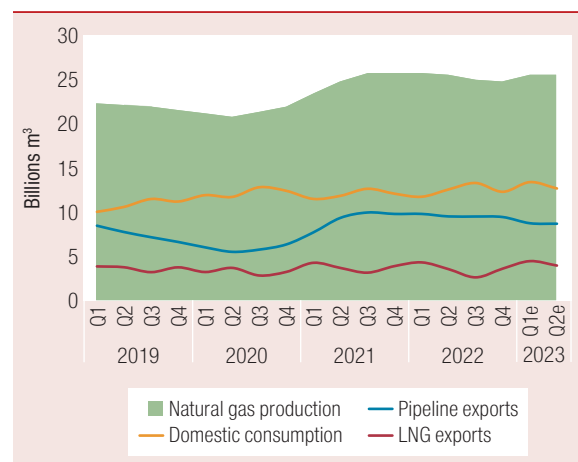
As surging domestic demand overcompensated for a steep decline in external demand, natural gas production increased in H1-2023.

After a rapid expansion and peak in 2021 (+17.1 percent), natural gas output declined moderately in 2022 (-3.4 percent) although it remained well above pre-pandemic levels. Pipeline exports fell in H1-2023 (-15.4 percent y-o-y), notably due to lower European demand amidst a milder winter,⁴ in part compensated by higher liquefied natural gas (LNG) exports (+6.8 percent y-o-y). Nevertheless, natural gas production was up 4.8 percent y-o-y in H1-2023, implying a steep increase in domestic demand, consistent with dynamic industrial activity (Figure 8).

Declining oil and gas prices compounded the effect of lower export volumes, and hydrocarbon exports fell markedly as a result.

Algeria's reference crude oil price peaked in June 2022 at US\$122.7 per barrel, before decreasing steadily to US\$83.7 in August 2023, amid slowing global economic activity and the introduction of a price cap on Russian oil. On the other hand, gas export prices are determined by longer-term contracts which, before Russia's war on Ukraine, meant

FIGURE 8 • ...while natural gas production increased, despite a decline in external demand



Source: Joint Organisations Data Initiative (JODI), WB estimates.
 Note: Data are presented as a rolling four-quarter average to eliminate the effect of seasonality. Domestic consumption is estimated as the difference between gross production and pipeline and liquefied natural gas exports, as Algeria does not import natural gas.

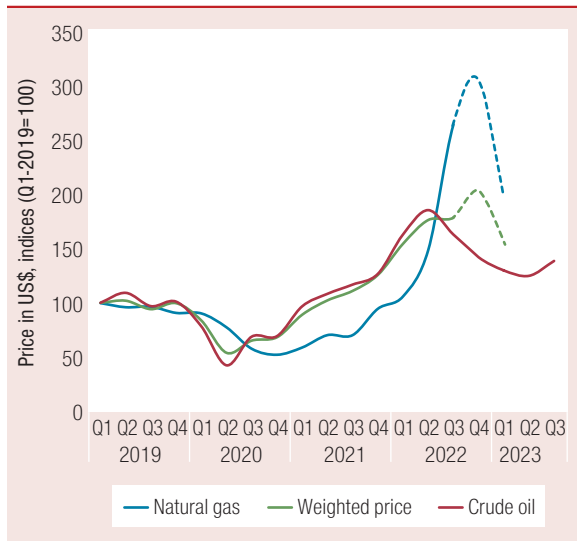
that natural gas prices tracked the dynamics of oil prices with a delay.⁵ As of mid-2022, however, the relationship between natural gas and oil prices changed, as Sonatrach renegotiated gas delivery contracts with its European counterparts,⁶ leading to a marked increase in the price of natural gas exported through pipelines, which tripled between Q4-2021 and Q4-2022. In H1-2023, the decline in oil and gas export volumes, that in oil prices, and the expected decline in natural gas prices caused the value of hydrocarbon exports to decrease by US\$ 7.7 billion relative to H2-2022, from US\$ 32 billion to US\$ 24.4 billion (Figures 9 and 10).

⁴ Natural gas consumption in Europe fell by about 16% y-o-y during the 2022-23 heating season. Residential and commercial usage was notably reduced by a warmer winter as well as gas saving measures, while demand from the power and industry sectors declined as they coped with higher prices. (IEA Gas Market Report, Q2-2023).

⁵ Algeria Economic Update, Spring 2022.

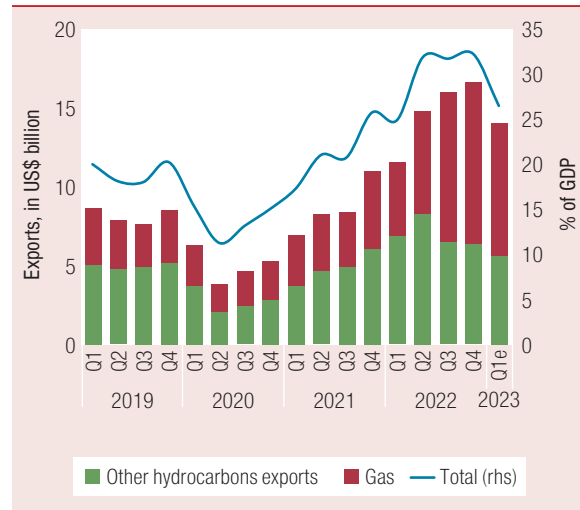
⁶ Notably with Italy's ENEL and ENI, Spain's Naturgy, and France's ENGIE. (Sonatrach Annual Report, 2022, p. 41). Absent public information regarding the new contractual terms, the change in the relationship between oil and natural gas prices means that there is considerable uncertainty about the dynamics of Algeria's natural gas export prices after Q3-2022.

FIGURE 9 • Gas prices surged as supply contracts were renegotiated...



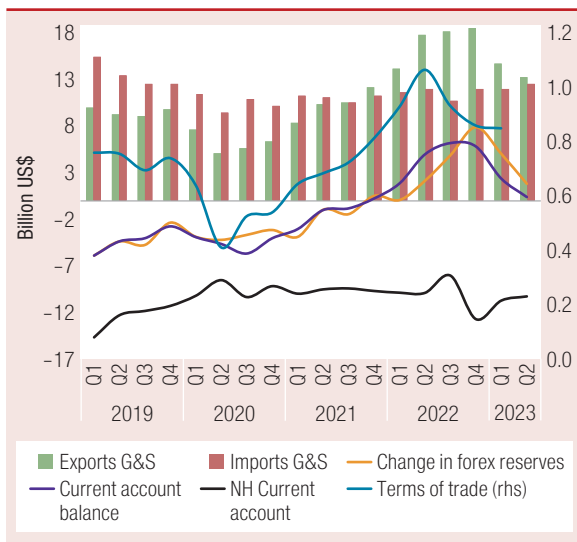
Source: BoA and WB estimates for Q4-2022 and Q1-2023.

FIGURE 10 • ...and natural gas exports came to represent most of Algeria's hydrocarbon exports



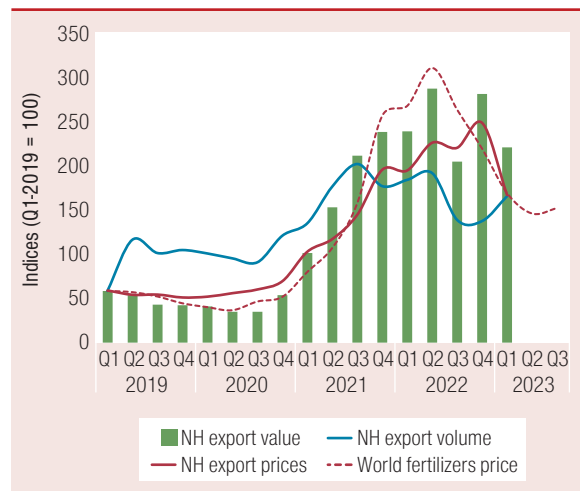
Source: BoA and WB estimates for Q4-2022 and Q1-2023.

FIGURE 11 • Falling hydrocarbon export prices drove down the current account in H1-2023...



Source: International Monetary Fund (IMF), ONS and WB estimates. NH = nonhydrocarbon. Forex reserves = foreign exchange reserves.

FIGURE 12 • ...and were compounded by a decline in nonhydrocarbon export prices



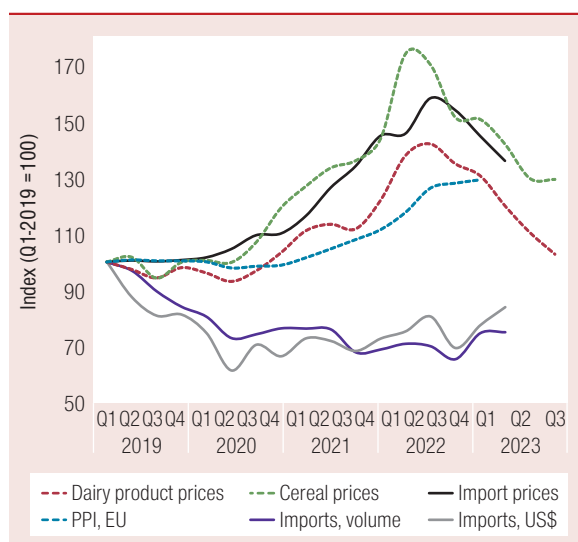
Source: ONS and WB estimates for nonhydrocarbon export prices and volumes, WB Commodity Markets Outlook for the composite fertilizer index. NH = nonhydrocarbon. Nitrogenous fertilizers and ammonia represent around 33 and 20 percent of nonhydrocarbon exports, respectively.

Lower Hydrocarbon Exports Drove Down the Current Account Surplus in H1-2023

Driven by falling hydrocarbon and nonhydrocarbon exports, as well as recovering imports, the current account surplus shrank during H1-2023. In the five

years before the pandemic, the current account deficit averaged 13 percent of GDP but flipped from a deficit of 2.7 percent in 2021 to a surplus of 9.8 percent of GDP in 2022, owing to high oil and natural gas prices. In the meantime, the value of nonhydrocarbon exports had increased by 27.9 percent, driven by the increase in the price of nitrogenous fertilizers and

FIGURE 13 • Imports increased despite declining prices...



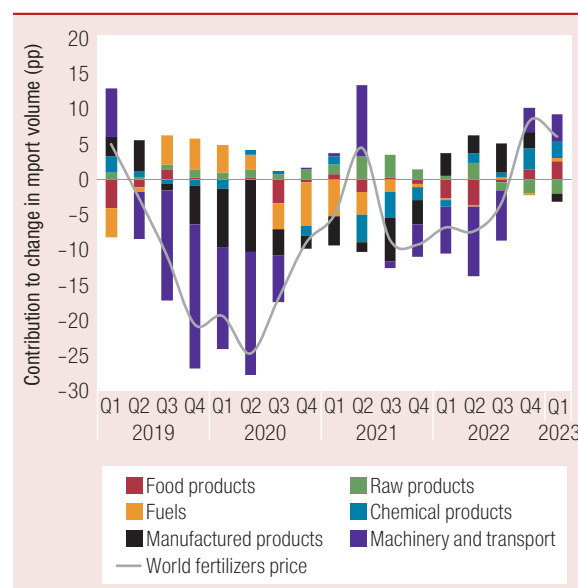
Source: ONS, Organization for Economic Cooperation and Development (OECD) & Food and Agriculture Organization (FAO).

Note: PPI, EU = Producer Price Index for the European Union.

ammonia,⁷ correlated with hydrocarbon prices. During H1-2023, the current account fell from a US\$ 12.1 billion surplus in H2-2022 to US\$ 2.9 billion, with overall export values falling by 23.6 percent y-o-y and imports recovering by 5.1 percent. The significant decline in hydrocarbon exports was compounded by declining fertilizer prices, lowering the value of nonhydrocarbon exports, as well as the recovery in equipment imports. As a result, terms of trade (the ratio of the export and import price indices) declined in H1-2023, owing to declining export prices, after having surged by 50 percent in 2022. Nonetheless, the current account surplus meant that Algeria was able to add significant foreign reserves, reaching US\$ 68.8 billion or 17.2 months of imports in June 2023, up from US\$ 61.7 billion or 15.9 months of imports of goods and services at end-2022 (Figures 11 and 12).

The increase in imports in H1-2023 was driven by equipment imports to meet strong investment demand, overcompensating for the decline in food import prices. Car import regulations were eased, but other recent quantitative and qualitative import control measures were maintained,⁸ while a High Council for the Regulation of Imports was created. Import volumes had remained flat in 2022 (-3.0 percent), while the prices of goods increased by 15.5 percent, which resulted in a 11.9 percent increase

FIGURE 14 • ...as rising domestic investment stimulated equipment imports



Source: ONS and World Bank calculations.

in the value of imports. In H1-2023, the import bill increased by 6.9 percent y-o-y, led by a steep increase in equipment imports (+20.2 percent y-o-y), a category responsive to strong investment demand, as well as rising imports of non-food consumption goods (+13.0 y-o-y). In contrast, easing global cereal and dairy product prices contributed to a decline in the value of food imports (-2.9 percent y-o-y) (Figures 13 and 14).

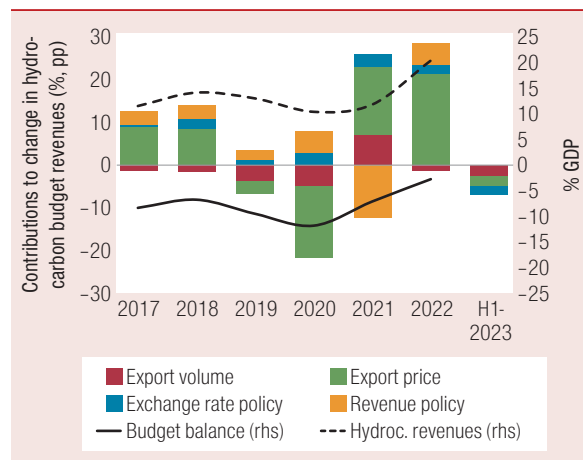
Lower Hydrocarbon Revenues are Putting Pressure on the Fiscal Deficit

The falling hydrocarbon prices and an increasing civil service wage bill are putting pressure on the fiscal deficit. After averaging 10.8 percent of GDP in the five years before the pandemic, the fiscal deficit narrowed from 7.2 percent of GDP to 2.9 percent in 2022, driven in large part by increasing hydrocarbon revenues, and despite surging spending on wages and social transfers (+2.1 percent of GDP). As a result, the nonhydrocarbon fiscal deficit deteriorated, from 19 to 23.3 percent of GDP. In

⁷ Representing the majority of Algeria's nonhydrocarbon exports (Trademap.org).

⁸ Algeria Economic Update, Fall 2021.

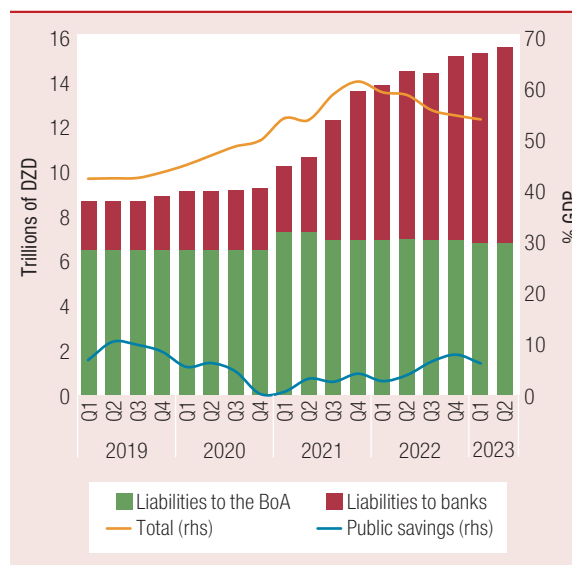
FIGURE 15 • Declining hydrocarbon revenues during H1-2023 increase pressure on public finances...



Source: Ministry of Finance, ONS, WB estimates for H1-2023.
 Note: Figure decomposes the log change in hydrocarbon budget revenues. Revenue policy is defined as the share of hydrocarbon export revenues that accrue to the budget. H1-2023 estimates are produced by assuming that revenue policy does not change relative to 2022.

H1-2023, falling hydrocarbon exports (-27.2 percent relative to H2-2022) are expected to lead to a proportional decline in budget revenues, reinforced by the dinar's appreciation. On the other hand, current spending is expected to keep increasing, notably driven by the second of three annual rises in civil service wages and the rising cost of unemployment benefits,⁹ while capital spending is expected to recover, as announced in the 2023 Budget Law. This will be partly compensated by rising tax revenues, on the back of increasing wages, consumption, investment, and imports, as well as a significant increase in Sonatrach dividends (Figure 15).

FIGURE 16 • ...but public debt only increased moderately in H1-2023



Source: IMF, WB estimates.
 Note: On the right-hand axis, variables are related to GDP over four rolling quarters.

Nonetheless, public debt only increased moderately in H1-2023, while Treasury savings at the Bank of Algeria kept increasing. After peaking at 62.9 percent of GDP at end-2021, the combination of a smaller budget deficit in 2022 and a significant rise in nominal GDP led to a decline of the debt-to-GDP ratio to 55.6 percent.¹⁰ In H1-2023, public debt grew by

⁹ Consistent with the Budget Law's anticipation of large budget increases for the Ministry of Finance, the Ministry of Labor, the Ministry of Interior, and the Ministry of Education.
¹⁰ Public debt is domestically held, at long maturities and negative real interest rates.

BOX 2: THE DYNAMICS OF PUBLIC FINANCES SINCE 2020

Akin to recent decades, Algeria's public finances reacted strongly to the volatility of oil and gas prices during and after the COVID-19 crisis.

Tracking global hydrocarbon prices, which have been their most important driver for over thirty years, budget revenues fell markedly in 2020 (-14.6 percent), before an even steeper recovery in 2021 and 2022 (+17.0 and +43.5 percent, respectively). On the other hand, public spending fell (-8.5 percent) as public investment was slashed in 2020, before recovering in 2021 and 2022 (+4.4 and +25.3 percent), on the back of large increases in wages and transfers. The decrease in 2020 is evocative of the public investment consolidation that took place after the 2008 and 2015 oil price crashes, while the ensuing increase in current spending resembles that which took place in 2008-2012. (Figures 17 and 18, Annex 1.1.)

Spending dynamics in 2020-2022 are consistent with recent history, whereby in difficult times current spending increases but capital spending declines. Fiscal policy is countercyclical if the budget deficit increases during downturns and decreases during upturns, helping to stabilize the economic cycle. Overall expenditures in Algeria are cyclically neutral, meaning that on average they do not vary with the

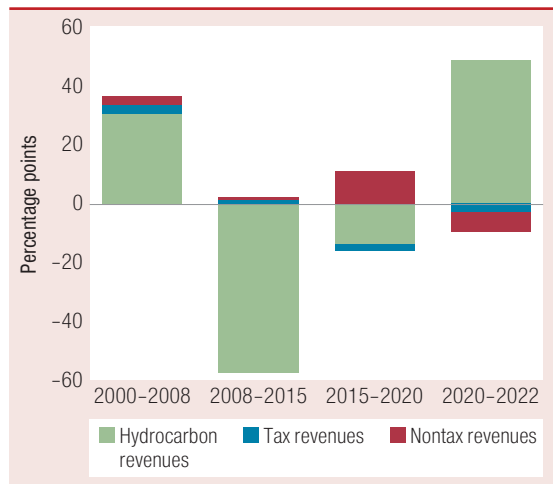
(continued on next page)

BOX 2: THE DYNAMICS OF PUBLIC FINANCES SINCE 2020 *(continued)*

state of the economy. This compares favorably with peer countries, whose spending is more procyclical, exacerbating business cycle fluctuations. However, it hides important underlying heterogeneity. In Algeria, current expenditures have been used countercyclically for the past two decades, rising when the hydrocarbon output fell below its potential amidst declining OPEC quotas, which has been associated with falling oil prices. Capital expenditures, on the other hand, have been strongly procyclical, declining when oil prices and output fell, lowering budget revenues. (See Annex 1.2.)

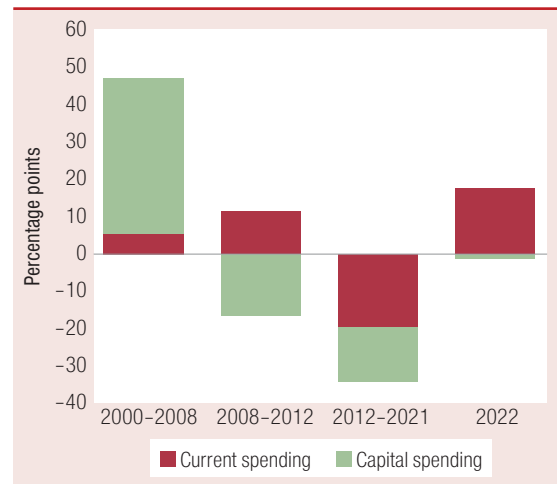
The divergent dynamics of current and capital spending also reflect and increase spending rigidity, increasing budget sensitivity to global hydrocarbon prices. Increasing current spending countercyclically can help support households during economic downturns but increases budget rigidity, defined as the share of public spending that cannot be easily reduced, such as the public wage bill or pension spending. Although Algeria's rigid spending remains below that of peer countries, it has increased significantly since 2008, as less-rigid investment spending has been replaced by more-rigid current and pension spending. As a result, there is increasing pressure to achieve fiscal consolidation by cutting back public investment, as in 2020 and 2021. (See Annex 1.3.)

FIGURE 17 • Change in the revenues-to-nonhydrocarbon GDP ratio, 2000-2022



Source: Ministry of Finance and ONS.

FIGURE 18 • Change in the spending-to-nonhydrocarbon GDP ratio, 2000-2022



Source: Ministry of Finance and ONS.

4.3 percent in nominal terms, financed via regular Treasury issuances, suggesting a relative stabilization of the debt-to-GDP ratio. In the meantime, Treasury savings at the Bank of Algeria, representing 10 percent of GDP at end-2022, rose by 25 percent between December 2022 and June 2023.¹¹ They are mostly comprised of the oil savings fund (*Fonds de Régulation des Recettes*, or FRR) which, after being depleted in 2017 and again in 2020, was replenished in 2021 and 2022 (Figure 16).

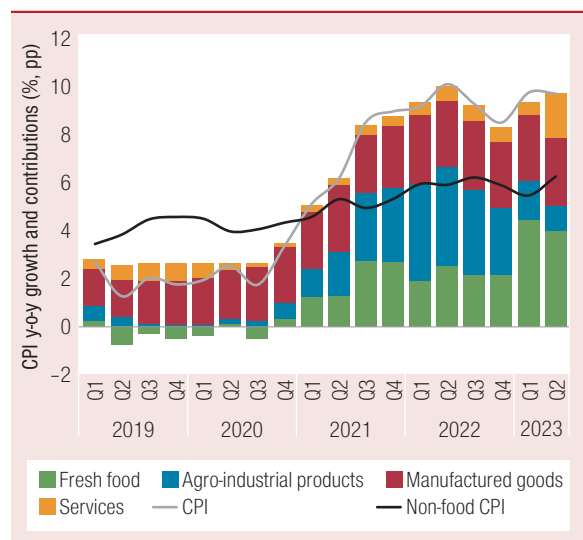
Inflation Remains Elevated in 2023, Due to Fresh Food Prices

Inflation reached 9.7 percent during the first eight months of 2023 with food inflation even

higher at 14.0 percent. Following years of relatively moderate inflation, the consumer price index (CPI) rose by 7.2 percent in 2021 and by 9.3 percent in 2022. During 8m-2023, inflation further increased to 9.7 percent, with fresh food inflation considerably higher (24.1 percent), likely to be partially driven by droughts and lower agricultural yields, and with a disproportionate impact on lower-income households. At the same time, the contribution of processed food to

¹¹ The apparent disconnection between the trajectory of public debt and savings, on the one hand, and that of the fiscal deficit, on the other hand, could in part be attributed to the use of SOE liquidity to finance the deficit during a given year. As a result, public debt accumulation is an imperfect proxy for fiscal financing needs.

FIGURE 19 • Inflation remained elevated, driven by fresh food products...

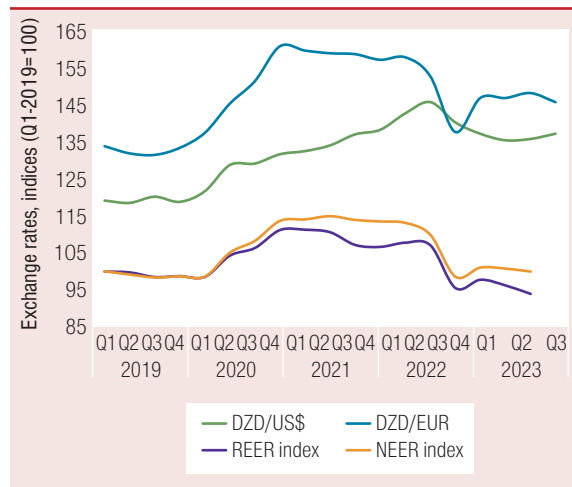


Source: ONS, WB estimates.

inflation fell from 41.0 percent in Q2-2022 to 10.8 percent in Q2-2023 and that of manufactured products remained stable, as the authorities forbade private imports of cereals and pulses, supported an appreciation of the exchange rate, and as the increase in imported food and manufactured products prices slowed down. Because fresh foods and services are much more likely to be domestically produced than processed food and manufactured products,¹² their larger combined contribution to inflation (up from 32 to 60 percent between Q4-2022 and Q2-2023) suggests that domestic factors now play a larger role in inflation dynamics.

After the authorities supported the appreciation of the dinar to curb imported inflation in H2-2022, the exchange rate stabilized in H1-2023. After fourteen consecutive years of exchange rate depreciation, the dinar appreciated by 6.2 percent against the US dollar and 4.0 percent against the Euro in H2-2022, as the Bank of Algeria's aimed to curb imported inflation. In H1-2023, the dinar's exchange rate stabilized against major currencies, as falling hydrocarbon prices threatened to put renewed pressures on Algeria's external balances, and in Q3-2023, it depreciated by 0.7 percent against

FIGURE 20 • ...despite the dinar's deliberate appreciation since June 2022 to limit imported inflation



Source: Investing.com, ONS, WB estimates.

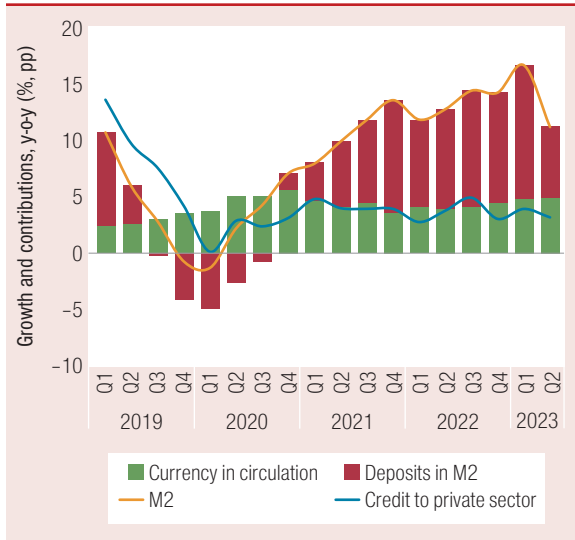
Note: REER = real effective exchange rate, NEER = nominal effective exchange rate.

the US dollar. As the dinar followed a similar trajectory against the currencies used with its major trade partners (US dollar, Euro, Yuan), the nominal and real effective exchange rates (trade weighted) also strengthened markedly in H2-2022, before stabilizing in H1-2023 (Figure 20).

Monetary policy has remained unchanged since the April 2023 increase in the reserve requirement, but money supply growth eased in Q2-2023. In April 2023, the Bank of Algeria restored the reserve requirement rate from 2 to 3 percent, returning to the pre-pandemic level, to reduce inflationary pressures. Meanwhile, money supply growth decelerated, as banking deposit growth declined from 19.6 percent y-o-y in Q1-2023 to 10.4 percent in Q2-2023, amidst the fall in hydrocarbon deposits and the increase in the reserve requirement. Private sector credit growth remained moderate, while SOE credit growth mildly accelerated (Figures 21 and 22).

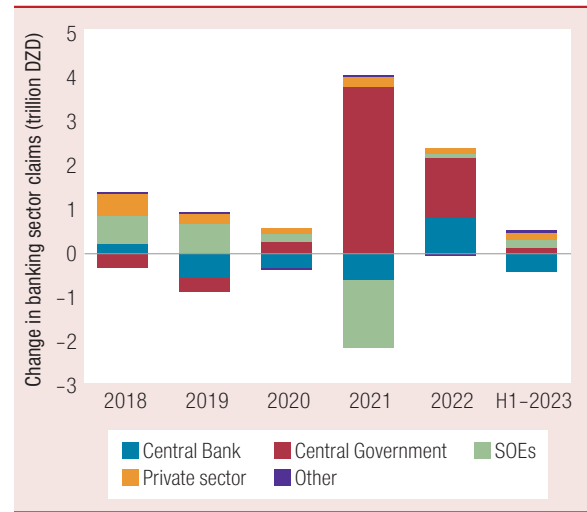
¹² According to the ONS's input-output tables, only 13.4 percent of fresh foods and 2.1 percent of services are imported, as opposed to 29.5 percent for processed foods and 63 percent for manufactured products.

FIGURE 21 • Liquidity growth eased in Q2-2022...



Source: IMF and World Bank estimates.

FIGURE 22 • ...with little expansion in private sector credit



Source: IMF and World Bank estimates.

OUTLOOK AND RISKS

Nonhydrocarbon Output Will Continue to Drive Economic Growth

In 2023, dynamic nonhydrocarbon sector growth should contrast with moderate hydrocarbon output growth. In the baseline scenario, overall growth is expected at 2.5 percent in 2023, supported by nonhydrocarbon sectors (+2.7 percent). Hydrocarbon output is expected to increase moderately (+1.6 percent), despite declining oil output, constrained by OPEC quotas. Activity is expected to be driven by investment growth as large mining and transport investment projects move forward,¹³ stimulating the construction and industrial sectors. Amidst a slowdown in private consumption, services sector growth is expected to taper. After Algeria experienced its third consecutive winter drought,¹⁴ agricultural output is forecast to decrease. Net exports would contribute negatively to growth, as investment and lower agricultural output stimulate imports while lower oil production quotas and European gas demand curb exports.

GDP growth is expected to increase in 2024 and 2025, as agricultural output recovers and crude oil production tracks recovering OPEC quotas. Hydrocarbon output would grow moder-

ately as OPEC quotas and European gas demand recover. Investment spending growth is expected to remain robust and keep supporting industrial activity, while it would be driven by the private sector, amidst continued prudent public investment policy. Private consumption is expected to slow down moderately as the base effect from COVID-19 subsidies and high inflation reduces real purchasing power, as would public consumption, amidst a slowdown in the growth of government spending. As a result, services sectors growth would slow down. Assuming a return to normal weather conditions, agricultural production would also rebound.

Inflation is expected to remain above 9 percent in 2023 and decrease gradually in 2024 and 2025. With food inflation higher than headline inflation, lower-income households are especially exposed to a drop in their purchasing power. The recent strengthening of price controls on cereal and pulses would limit the increase in processed food

¹³ Such as the integrated phosphate project in eastern Algeria, and the iron ore extraction project in the Tindouf wilaya.

¹⁴ European Commission Joint Research Centre.

prices, however, instead putting pressure on public subsidy spending. Inflation is expected to decline gradually in 2024 and 2025 as rainfall returns to normal levels, as the growth in money supply, in public spending, and in food import prices tapers, and due to the delayed effect of the dinar's appreciation. In addition, policies that improve product market competition as well as strengthen food security against climate shocks, could support lower and more stable domestic prices in the longer run.

Fiscal and External Balances Are Expected to Initially Deteriorate, then Stabilize

The current account is expected to remain positive in 2024 and 2025, amidst limited growth in exports and imports. With hydrocarbon prices falling and oil output decreasing following OPEC quota cuts, the current account is expected to shrink from a record 9.8 percent of GDP surplus in 2022 to 2.8 percent in 2023, before reaching 1.4 percent in 2024 and 0.5 percent in 2025. The value of hydrocarbon exports would decrease due to a combination of decreasing volumes owing to rising domestic consumption and decreasing prices owing to the global economic slowdown. At the same time, the value of imports would increase with investment driving industrial equipment imports and subdued agricultural output driving food imports in 2023. However, the accumulation of reserves since 2021 has allowed Algeria to build a safety cushion, and it is expected that the foreign exchange reserves will be maintained at between 16 and 17 months of imports of goods and services between 2023 and 2025.

Driven by lower hydrocarbon revenues and higher spending, the fiscal deficit is expected to widen in 2023 and 2024 before resorbing. Hydrocarbon revenues are expected to decline in 2023, but this will be offset by a marked rise in Sonatrach dividends. Nevertheless, the sharp rise in wage spending and a moderate increase in capital expenditure would push up the budget deficit. In 2024, the return to a moderate level of dividends and the continued rise in salary spending would generate a further increase in the deficit, before stabilizing in 2025, assuming a prudent spending policy. Thus, after rising from 2.9% of

GDP in 2022 to 6.8% in 2023 and 8.9% in 2024, the overall budget deficit would moderate in 2025.

Public debt is expected to increase moderately, with transfers from the Revenue Stabilization Fund partially financing the fiscal deficit. In the baseline scenario, the public debt-to-GDP ratio would increase by 5 percentage points of GDP between 2023 and 2025, reaching 60.2% of GDP by 2025. The use of the savings accumulated in the FRR would allow for a slower pace of debt accumulation over the projection period, and regular issues of Treasury bills would partially meet budget financing requirements.

Volatile Oil Prices Remind of the Economic Diversification Imperative

Economic growth, as well as the fiscal and external balances, remain sensitive to fluctuations in hydrocarbon prices. In 2022, high hydrocarbon prices led to a record current account surplus and a significant narrowing of the fiscal deficit. With lower hydrocarbon prices these trends are expected to have reversed in 2023. The evolution of hydrocarbon prices represents a significant risk for the 2024 and 2025 outlook, both to the upside and to the downside, driven by the fragility of the global outlook, developments in Russia's war on Ukraine, and the resurgence of conflict in the Middle East.

Continued reforms to foster private sector investment, growth and diversification are needed improve the performance and resilience of the economy. The risks posed by oil prices underscore the need to sustainably improve macroeconomic balances. Diversifying export revenues away from hydrocarbons and attracting foreign investment would improve Algeria's external resilience against oil price fluctuations. On the fiscal front, higher spending rigidity from current spending amidst volatile hydrocarbon revenues increases pressure to raise more tax revenues and strengthen spending efficiency in an equitable way, while containing public investment growth. Therefore, and consistent with the 2021 Government Action Plan,¹⁵ continued imple-

¹⁵ Government Action Plan for the Implementation of the Program of the President of the Republic.

mentation of reforms to stimulate private investment and enable a formalized private sector to become the engine of sustainable and diversified growth remains essential to the performance and resilience of the Algerian economy.¹⁶

Beyond hydrocarbons, recent extreme natural phenomena in the region, and Algeria's own experience, underscore the risks that they pose for growth and development. Like other countries in North Africa, Algeria is exposed to several climate and geological risks, such as flooding, earthquakes, and droughts. Over the past three years, drought episodes

have notably had strong effects on agricultural production and prices. As disasters can disrupt all sectors of the economy and jeopardize hard-earned development gains, scaling up disaster risk reduction and financing can contribute to saving lives and protecting economic growth, building on Algeria's existing legal disaster risk management framework.

¹⁶ Furthermore, the production and publication of data on private sector activity and the dynamics of informality would allow for an appreciation of the progress made.

TABLE OF INDICATORS

	2019	2020	2021	2022	Projections		
					2023	2024	2025
Output and prices							
Real GDP	1.0	-5.1	3.4	3.2	2.5	2.6	2.6
Nonhydrocarbon	2.7	-3.8	2.3	4.3	2.7	3.0	3.0
Hydrocarbon	-4.9	-10.2	10.5	-0.6	1.6	0.8	1.0
Per capita	-1.0	-6.9	1.7	1.6	0.9	1.0	1.0
Consumer price index (period average)	2.0	2.4	7.2	9.3	9.5	8.6	7.9
GDP (in billions of current US\$)	171.8	145.7	163.4	195.0	216.4	234.0	245.1
GDP per capita (US\$)	3955.2	3292.9	3631.7	4265.6	4659.6	4958.8	5111.3
Crude oil production (thousand barrels per day)	1023.0	899.0	911.0	1020.0	976.2	1002.3	1039.0
Natural gas production (billions of m3)	86.1	87.7	102.8	99.2	103.4	107.7	112.2
External sector							
Current account	-9.9	-12.8	-2.7	9.8	2.8	1.4	0.5
Trade balance	-9.1	-12.3	-1.6	11.5	4.0	2.6	1.6
Exports of goods and services	22.4	17.1	25.5	35.4	27.3	24.9	23.9
Hydrocarbon exports	19.4	13.7	20.8	30.5	23.1	20.5	19.1
Nonhydrocarbon exports	3.1	3.4	4.6	4.9	4.2	4.4	4.8
Imports of goods and services	31.6	29.4	27.1	24.1	23.3	22.3	22.2
Gross official reserves (months of imports)	14.0	13.7	12.5	15.8	16.4	16.9	16.7
Exchange rate (Algerian dinar per US\$; period average)	119.4	126.8	135.1	142.0			
Sahara Blend export price (US\$/barrel)	64.4	42.1	72.7	100.9			
Central Government Finance							
Government revenue and grants	32.2	30.5	29.9	34.2	32.8	29.0	27.9
Hydrocarbon revenue ^a	13.0	10.4	11.8	20.4	19.0	14.7	13.9
Nonhydrocarbon revenue	19.2	20.1	18.1	13.8	13.8	14.3	14.0
Expenditures	37.8	37.3	33.7	34.9	39.7	38.0	36.0
Current expenditures	23.9	27.1	24.8	27.4	31.4	30.4	29.2
Capital expenditures	13.9	10.2	8.9	7.5	8.2	7.6	6.8
Special Account Balance and Treasury Interventions	4.0	5.1	3.4	2.2	2.6	2.4	2.4
Overall budget balance ^b	-9.6	-11.9	-7.2	-2.9	-6.8	-8.9	-8.1
Primary overall budget balance	-9.0	-11.0	-6.5	-1.4	-5.4	-7.5	-6.6
Nonhydrocarbon overall budget balance	-22.6	-22.3	-19.0	-23.3	-25.8	-23.7	-22.0
Total central Government debt	45.5	51.8	62.9	55.6	55.2	57.6	60.2
Domestic debt	44.8	51.0	62.1	55.1	54.8	57.2	59.8
External debt	0.7	0.8	0.7	0.5	0.5	0.4	0.4

^a Includes dividends from Sonatrach and hydrocarbon revenues transferred to the oil savings fund.

^b Includes special account balance and Treasury interventions

ANNEX 1: ANALYSES IN ALGERIA'S PUBLIC FINANCES

1. Algeria's Public Finance Trends, 2000 to 2022

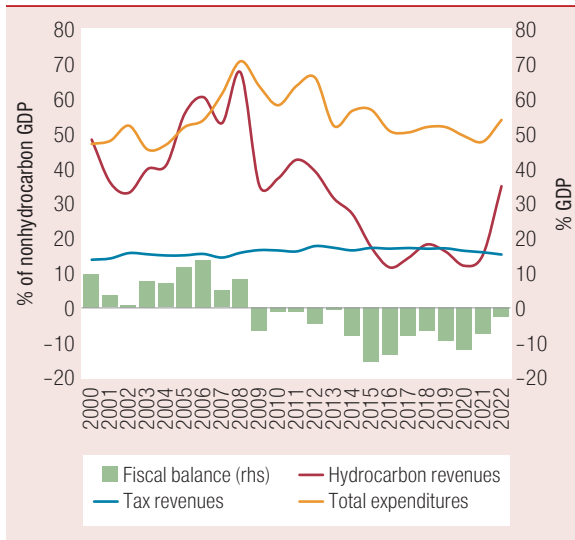
Algeria's public finances have been very reactive to oil and gas prices over the last two decades, with their fall driving expansions in the budget deficit. After running a significant budget surplus between 2000 and 2008, Algeria has run a small budget deficit after the fall in oil prices during the 2009 recession, which expanded following the crash in oil prices, in 2014–2015. Accumulated oil savings in the Revenue Stabilization Fund were nearly depleted by 2017, followed by a steep rise in public debt accumulated as part of the 2017–2019 monetary financing program, worth 32 percent of 2019 GDP, and the 2021–2022 special refinancing program. Public debt levels declined for the first time in a decade in 2022, when oil and gas prices rose, and the budget deficit shrunk.

Hydrocarbon prices have been the most important driver of budget revenues, and plummeted after the 2008 and 2014–2015 oil shocks, before recovering in 2022. Hydrocarbon revenues increased rapidly in the 2000s, reaching 37 percent of GDP in 2008, before the oil price drop when they dropped to 24 percent. They fell to between 10 and 15

percent GDP in the early 2010s, before recovering in 2022, when they reached at 24 percent of GDP. Hydrocarbon budget revenues have been mainly driven by oil and gas prices, with the decline in export volumes contributing negatively on average, and exchange rate depreciation contributing positively on average. Meanwhile, tax revenues remained stable for the last two decades, between 10 and 15 percent of GDP (15 and 18 percent of NHGDP). The relative decline in revenues was reversed in 2022, as oil and gas prices increased markedly.

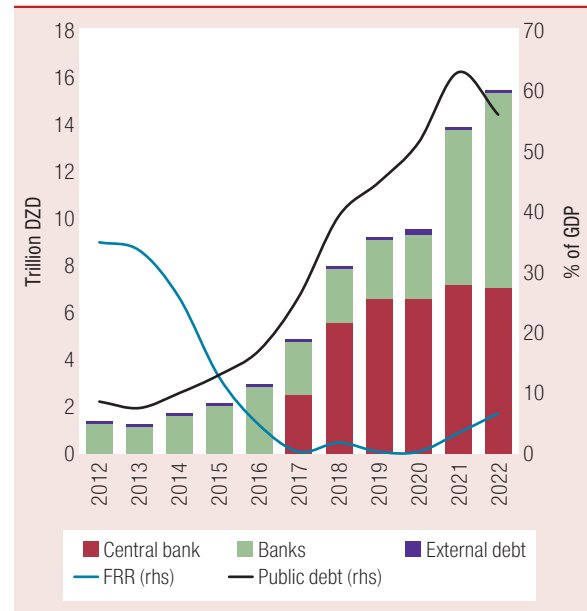
Following a significant increase in budget expenditures in the 2000s, Algeria pursued expenditure consolidation after 2008. In the years leading up to the 2008 oil shock, the government increased public investment to finance large infrastructure projects (transport, water and agriculture, housing) and transfers, while also paying back its debt ahead of schedule. However, when oil prices crashed and budget revenues fell, Algeria cut public investment but increased public hiring and wages, leading current expenditures to increase. After 2012, capital expenditure consolidation continued, and was compounded by a decline in current expenditures, which was ultimately reversed in 2022 to finance increases in public sector wages and pensions and social spending.

FIGURE 23 • After budget surpluses in the 2000s, falling hydrocarbon revenues led to persistent deficits in the 2010s...



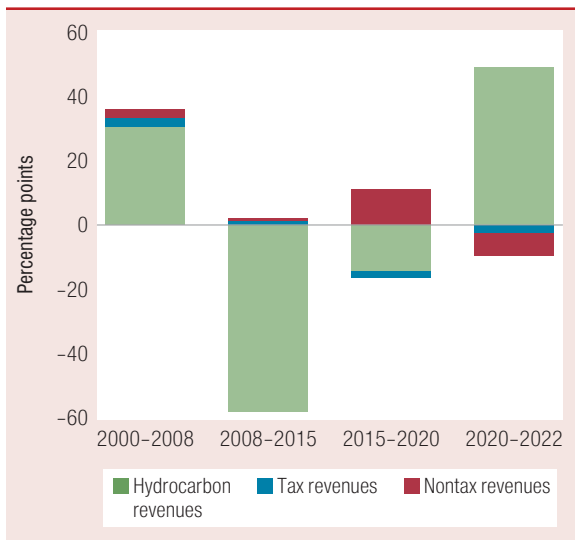
Source: Ministry of Finance and ONS. The variables are presented as a share of nonhydrocarbon GDP, to abstract from variations in the ratio that are led by volatile oil prices.

FIGURE 24 • ...leading to significant domestic public debt accumulation



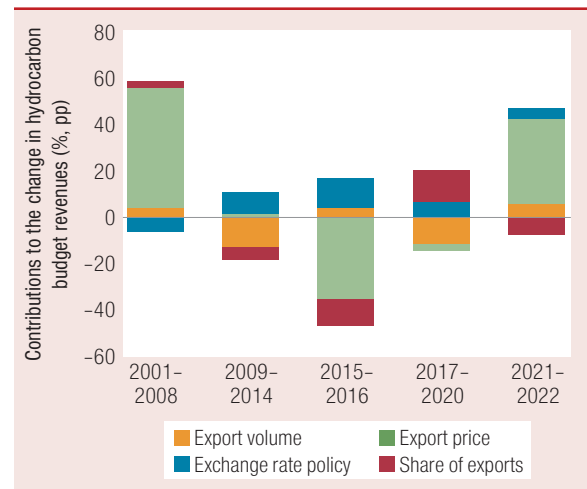
Source: Ministry of Finance and ONS.

FIGURE 25 • Budget revenues have been mostly driven by hydrocarbon revenues...



Source: Ministry of Finance and ONS. The figure computes the overall percentage change in the revenue-to-nonhydrocarbon GPD ratio and decomposes it between its three components.

FIGURE 26 • ...which, in turn, depended on oil and gas export prices



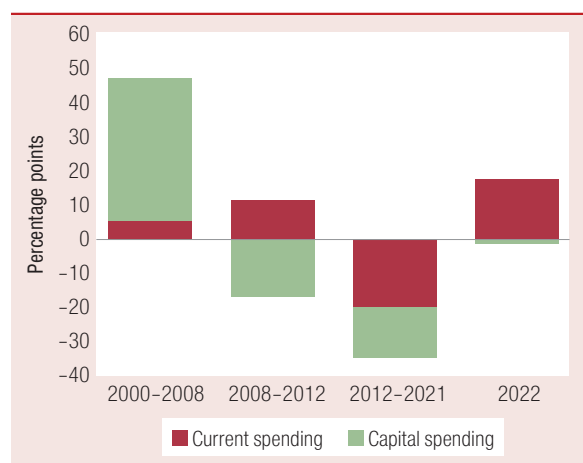
Source: Ministry of Finance and ONS. The figure computes the overall percentage change in the dinar value of hydrocarbon revenues accruing to the budget and decomposes it between its four drivers: the price of exported hydrocarbons, the quantity exported, the dinar-US dollar exchange rate, and the share of US\$ hydrocarbon exports that accrue to the budget ("revenue policy").

2. Budget Spending Along the Economic Cycle

Evaluating the relationship between fiscal policy and the economic cycle allows us to understand

its role in macroeconomic stabilization. Fiscal policy is countercyclical if the budget deficit increases during economic downturns and decreases during economic upturns. Because a reduction (increase) in taxation or an increase (reduction) in budget

FIGURE 27 • Significant spending consolidation efforts took place in the 2010s



Source: Ministry of Finance, ONS, and World Bank estimates.
 Note: The figure shows changes in the nonhydrocarbon expenditure-to-GDP ratio, broken down into its two components.

spending are expected to increase (decrease) aggregate demand, a countercyclical policy is desirable because it helps stabilize the economic cycle. On the other hand, a procyclical fiscal policy will exacerbate the economic cycle, reducing demand during downturns, and increasing demand during upturns.

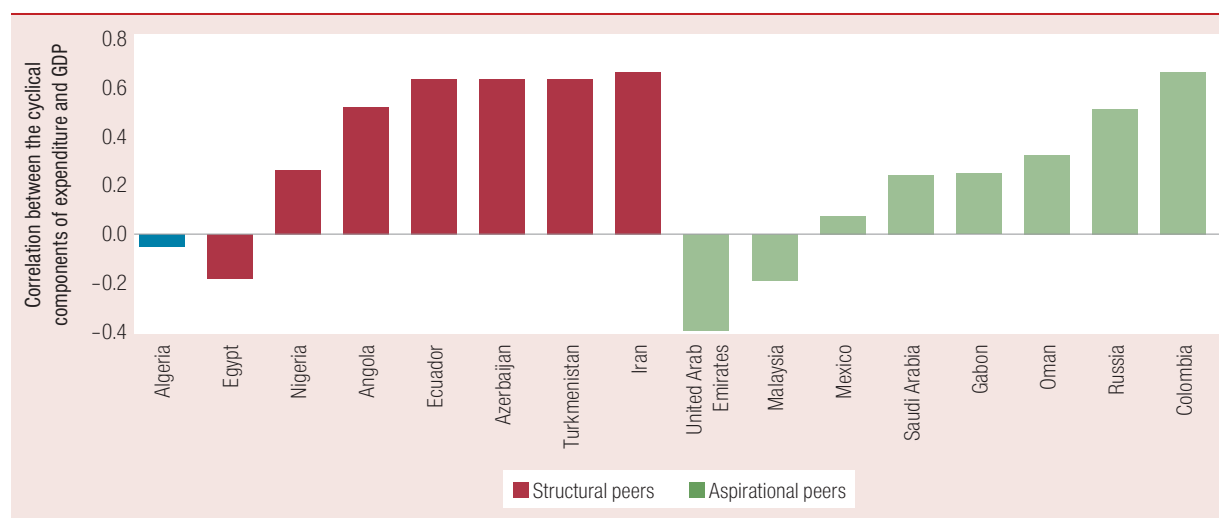
Cyclicity is measured here as the correlation between the cyclical components of expenditures and output. The cyclical components

of expenditures and output are measured by applying a filter to disaggregate the evolution of a variable into its long-term trend (structural component) and short-term fluctuation (cyclical component). Expenditure is referred to as pro-cyclical if its cyclical component shows a positive correlation with the cyclical component of output, while it's referred to as counter-cyclical if the correlation is negative.

Overall expenditures in Algeria are cyclically neutral, which compares favorably with peer countries. Over the last two decades, most peer countries exhibited strong cyclicity in expenditures: they spent more during good times and less during bad times. In Algeria, the correlation between the cyclical component of spending and output was -0.05 between 2002 and 2022 which suggests that expenditures were cyclically neutral, a significant development relative to pro-cyclical spending patterns in the preceding decades. (Figure 28).

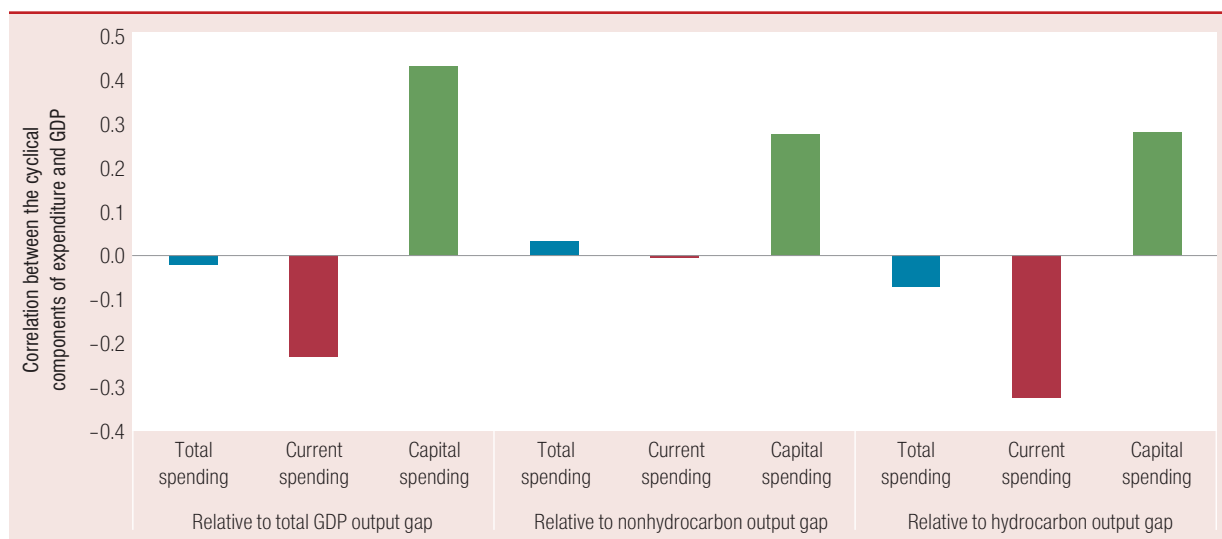
Current expenditures have been used countercyclically for the past two decades, when the hydrocarbon output gap expanded. The correlation between the cyclical component of current spending and the cyclical component of output is negative between 2000 and 2022, suggesting that current spending exhibited countercyclical behavior, driven by the increase in the wage bill and transfers

FIGURE 28 • Expenditures are less cyclical in Algeria than in most peer countries



Source: Ministry of Finance and ONS.
 Note: Peers are countries whose economies have similarities in terms of size, levels of development and role of the hydrocarbon sector in the economy. Structural peers have similar income levels, while aspirational peers have higher income levels.

FIGURE 29 • Capital expenditures are procyclical, but current spending is countercyclical...



Source: Ministry of Finance, ONS, and World Bank estimates.

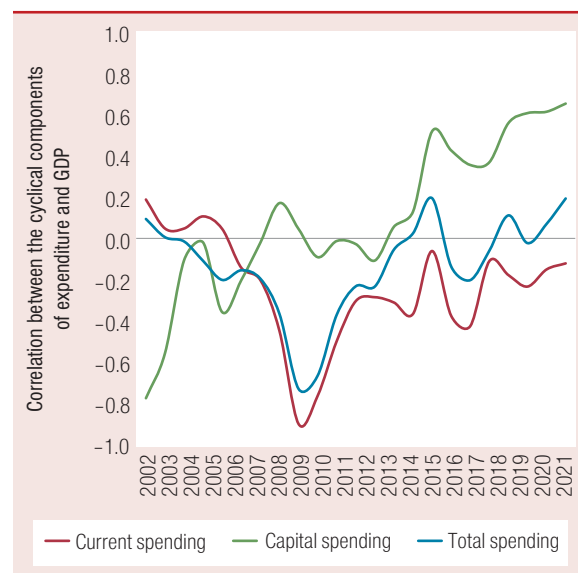
during downturns. This relationship is driven by the negative correlation with the hydrocarbon output gap, suggesting that spending has been raised in times where hydrocarbon output fell, which has been associated with falling oil prices and its effect on oil production quotas.

Capital expenditures, on the other hand, have been strongly procyclical. The correlation between the cyclical component of capital spending and the cyclical component of output was strongly positive between 2000 and 2022, suggesting that capital spending exhibited procyclical behavior. This relationship is driven both by the positive correlation with the hydrocarbon output gap and nonhydrocarbon output gap. In the case of the former, capital spending has been reduced in times where oil prices, hydrocarbon output and budget revenues fell. In the case of the latter, the relationship could also be driven by the effect of capital spending on growth—reduction in public investment leading to slowdown in growth.

3. The Rigidity of Public Expenditures

Spending rigidity is defined as the sum of public expenditures that are assumed to be beyond policy makers' control at least in the short term. If the

FIGURE 30 • ...as a result, expenditure policy has been cyclically neutral



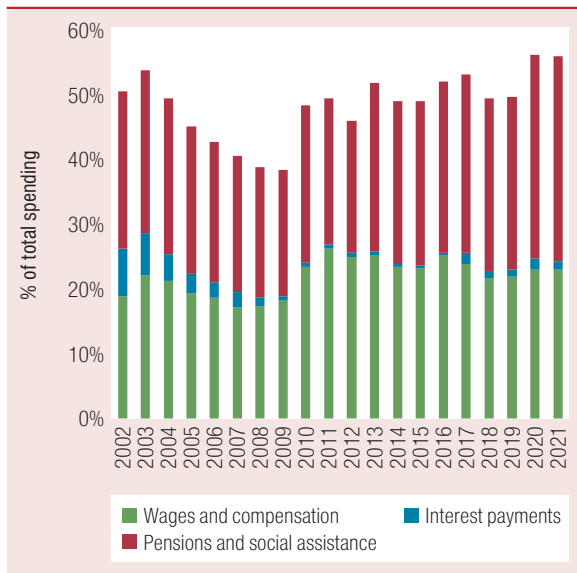
Source: Ministry of Finance, ONS, and World Bank estimates.

Note: The coefficients shown are rolling averages, to limit the effect of short-term variations.

share of rigid expenditures is high, fiscal policy is less able to smooth the economic cycle by reducing budget spending during economic upturns. Wages and compensation, interest payments and social security and assistance spending are assumed to be rigid expenditures and, in Algeria, their share declined from

50 percent of all expenditures (including social security spending) in 2002 to 38 percent in 2009. Notably, interest payments shrunk from 7.4 percent of spending in 2002 to below 1 percent by 2009, though they have increased to 1.4 percent by 2021. Then during the 2010s, rigidity increased in line with spending on wages and compensation as well as pension spending, reaching 55.3 percent of expenditures by 2022.

FIGURE 31 • Budget rigidity has increased in recent years...



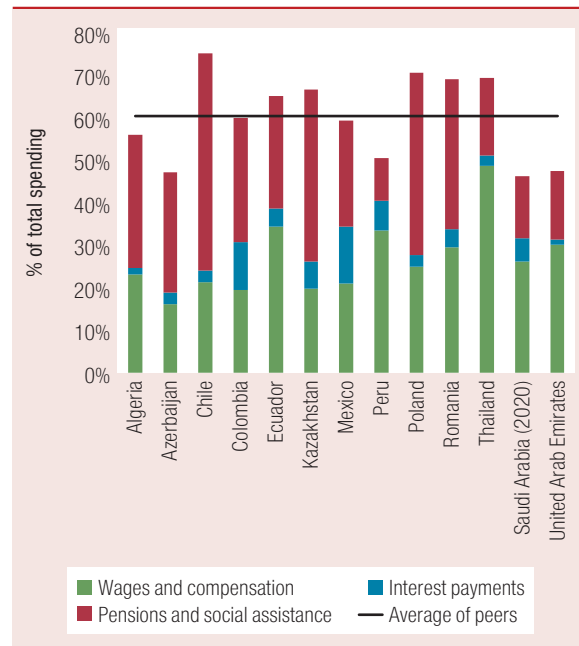
Source: MoF, ONS, and WB estimates.

Note: Spending on pensions and social assistance are measured as the sum of estimated spending by social security funds, Mujahidin pensions, food subsidies, and public healthcare spending. Total spending includes spending through social security funds.

Nonetheless, budget rigidity appears to remain below the average of peer countries.

Compared to regional and aspirational (with similar economies, but higher GDP per capita) peers for which spending measures are readily available, Algeria does not exhibit especially high budget rigidity, despite spending a relatively high share of its overall expenditures on wages and pensions.

FIGURE 32 • ...but remains below the average of peer countries



Source: MoF, IMF, and WB estimates.

ANNEX 2: LATEST SPECIAL SECTIONS OF THE ALGERIA ECONOMIC UPDATE

Fall 2022: “Estimating Economic Activity from Nightlights Data.”

Nightlights data is a tool now commonly used to assess economic activity. Since 2012, satellite data have been available daily and are publicly available on the Group on Earth Observations website. For Algeria, the empirical link between nightlights data and economic activity is strong, both for oil production (geolocated by gas flaring sites), gas production, and nonhydrocarbon activity. The strong correlation between nightlights and nonhydrocarbon activity allows us to mobilize these data to estimate the recent level of economic activity, and to produce spatialized estimates of the level and dynamics of activity, useful for sectoral or local development analyses.

Fall 2022: “Estimation of the Fiscal Multipliers in Algeria.”

The sharp increase in government spending in 2022 raises the question of its effects on economic activity. The propensity of public spending to support economic activity and generate additional economic activity is captured by the fiscal multiplier. An analysis

conducted on quarterly Algerian data since 2000 finds a weak multiplier effect of Algerian public spending on GDP, notably caused by the effect of an increase on the deterioration of the trade balance, resulting from its impact on imports. The spillover effect of spending on private consumption is observed but is limited, while the analysis finds a more marked effect of public spending on the construction sector.

Spring 2022: “Does Algeria Benefit from Rising Gas Prices?”

The export price of Algerian natural gas follows a distinct dynamic from the reference price of gas on international markets. Thus, while the Henry Hub gas reference price has gained nearly 50% between Q2 and Q3-2021, the export price of Algerian natural gas has increased by only 0.5% over the same period. Indeed, these prices are established contractually, sometimes on a long-term basis, and based on bilateral negotiations with buyers. An econometric modeling exercise allows us to establish that the export price of Algerian natural gas is characterized by a strong inertia, as well as a delayed linkage to the oil price. The model

presented allows to explain 88% of the variation of the exported natural gas prices.

Spring 2022: “The Impact of Macroeconomic Factors on Inflation in Algeria”

Inflation is on the rise in 2021 and 2022, both globally and in Algeria, but the underlying causes vary from country to country. In Algeria, the price increase that began in 2021 was driven by food prices. A model of the consumer price index since 2009 shows that it is characterized by strong short-term inertia, but that the depreciation of the dinar, the increase in the price of imported goods, the rise in public spending and the increase in currency in circulation explain more than 40% of the variation in the CPI after two years. In addition, the importance of these factors varies according to the categories of goods and services, reflecting the intensity of imports of these products and the characteristics of the Algerian market both in terms of production and distribution.

Fall 2021: “Evolution of Non-Monetary Poverty and Inequality in Algeria.”

The multidimensional poverty indicator improved in Algeria between 2013 and 2019, reflecting progress in all its dimensions: education, health, and living conditions. Although Algeria performs well in the MENA region, and despite notable improvements, multidimensional poverty varies considerably across regions and between rural and urban areas. The North-Central and North-Eastern regions face lower levels of deprivation than the rest of the country, while the Central Highlands region faces a higher level of deprivation. The most vulnerable regions improved more rapidly between 2013 and 2019, showing convergence with the richer regions. Health and education have become more important dimensions of deprivation, underscoring the policy priorities for Algeria’s human development.

Fall 2021: “Resilience of Algeria to Climate and Natural Disaster Risks.”

The Algerian territory is exposed to a range of climatic and geological hazards, particularly in urban areas, which are experiencing rapid population growth and concentrate a significant share of economic activity. Floods are the most frequent disasters in Algeria, but the greatest economic losses have been caused by earthquakes. Algeria has a modern legal framework for disaster risk management (DRM), a clear decision-making framework for emergency response, and recognizes the importance of protecting strategic infrastructure and critical sectors. Serious efforts have been made to reduce risk, especially in emergency response management and reconstruction, at the expense of prevention. Moreover, information sharing is not systematic, leading to inconsistencies, especially in disaster prevention, and enforcement of GRC legislation can be improved. Significant efforts should still be made for comprehensive and cross-sectoral climate and disaster risk reduction and management.

Spring 2021: “Effects of COVID-19 on Inequality in the MENA Region and Algeria.”

Survey results from the Middle East and North Africa (MENA) region confirm that the poorest individuals are more likely to report a deterioration in their living conditions since the beginning of the COVID-19 crisis. Despite the lack of recent data on household welfare in Algeria, the characteristics of vulnerable individuals suggest that inequality has also increased. They are more likely to contract COVID-19 or lose their jobs during the pandemic, have less adequate social protection, and are likely to be disproportionately affected by ongoing macroeconomic and fiscal adjustments. A sustainable and inclusive recovery will therefore require offering the most vulnerable the opportunity to recover what they have lost.

Spring 2021: “Towards an Equitable Reform of the Algerian Health System.”

The consequences of the COVID-19 pandemic have shown the need for a fair reform of the Algerian health system. Although officially the number of cases and deaths remains low, the pandemic has highlighted the limitations of the health system. A double burden of communicable and non-communicable diseases, as well as limited resources, suggest a need to strengthen

it. Although the health system receives substantial public financial support and requires relatively little individual expenditure, and although life expectancy and control of noncommunicable diseases are comparable to peer countries, health outcomes remain below those of middle- and high-income countries, particularly in terms of equity in maternal and child health conditions. The need for physical and human resources and for a better distribution of health coverage are major challenges. Finally, declining public financing and health system capacity pose risks to health system resilience.

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