# Bank of Algeria's short note for the BIS Annual Meeting of Emerging Market Deputy Governors

## The changing nature of the financial system: implications for economic resilience and long-term growth

Bank of Algeria

While the financing of infrastructure and long-term growth had dominated Algeria's financial scene since 2002, a resurgence of twin deficits following the 2014 oil shock led to the use of so-called "unconventional"[1] financing to support the economy. This already vulnerable financial situation was further weakened by the double shock of the Covid-19 pandemic and the collapse in oil prices. This led to the emergence of new refinancing programs, such as the Special Refinancing Program, to support the national economic recovery program launched in June 2020. These factors, combined with internal political developments and recent geostrategic events, have triggered changes in Algeria's financial landscape.

## Changes to the financial landscape

**Key events** include the adoption of the new *Monetary and Banking Act* in June 2023, which aims to adapt the legal and regulatory framework to tackle profound economic and financial changes, as well as technical and technological challenges, and enable the opening up to new players.

**In addition to strengthening the governance of the banking system, greater attention is being paid to financial stability and financial inclusion**. This has been demonstrated by the creation of a Financial Stability Committee, tasked with macroprudential oversight and crisis management, and a National Payments Committee, entrusted with drawing up the draft national strategy for the development of electronic means of payment and monitoring their implementation.

Islamic finance is also gaining momentum in Algeria. A good number of banks now offer a range of products and services in line with Islamic precepts, helping to mobilize savings.

**While the central role of banking intermediation in the Algerian financial system persists**, with a predominance of public banks, the opening up of the capital of a public bank, namely "Le Crédit Populaire d'Algérie" in January 2024, represents a pivotal step in the transformation of the Algerian financial market. This decision is

[1] Amendment to article 45 of the Ordinance on Money and Credit, in 2017, instituting, on an exceptional basis and for a period of five (5) years, the purchase, by the Bank of Algeria, directly from the Treasury, of securities issued by the latter.

part of the ongoing reform of the financial sector, with a view to improving governance and access to financing, particularly for the private sector.

## Resource allocation and long-term growth

**As financial reforms progress, capital markets will become an important source of financing for long-term growth in Algeria.** Indeed, a shift in the importance of banking intermediation and capital markets is essential to diversify and increase the sources of financing required for sustainable, inclusive growth. With this in mind, it is expected that the capital of a second public bank will be opened up before the end of 2024, to revitalize the Algiers stock exchange and the Algerian financial market.

**This is particularly necessary** in the light of the fact that several factors have limited the efficiency of Algerian banks in financing long-term growth, notably the concentration of the banking sector, which limits competition and the diversification of products and services offered. The structure of private sector companies, most of which are small, is also an obstacle to the efficient allocation of resources for financing long-term growth.

**To overcome these challenges and reduce the risk of crowding out lending to the private sector**, a lot of efforts have been, and continue to be, deployed. Of note is **the adoption of a new investment law, as of July 2022**, that enshrines freedom to invest as well as transparency and equality in the treatment of investments. Also, the development of an internal credit rating system for non-financial companies will enable the growth of credit to small and medium-sized enterprises in the private sector.

**In the same vein**, digital innovation has the potential to expand access to financing, stimulate economic growth and reduce informality in Algeria. The informal sector occupies a significant share, **another drag on the banking system's efficient allocation of resources**. In this regard, the reforms currently undertaken also aim at promoting digital innovation in Algeria's financial sector, **which will facilitate a better allocation of capital, thus boosting the country's growth potential.**

## Excessive finance and resilience, long-term growth and policy measures

**To ensure robust and sustainable growth while maintaining a balanced financial structure**, Algeria must pursue the ongoing structural reform program. These reforms include diversifying the economy and sources of financing, promoting financial inclusion and stimulating financial markets, while also ensuring financial and macroeconomic stability.

**To achieve this, it is crucial to:**

- **invest in research and development,** education and training,
- improve the regulatory environment,

- encourage financial innovation,
- invest in technology and human capital,
- develop non-oil sectors,
- strengthen financial institutions, and
- adopt pragmatic and prudent fiscal and monetary policies.

In Algeria, markets with strong development potential include credit and bond markets, as well as equities and mutual funds, where significant growth is expected to be one of the outcomes of current financial reforms.

**Thus, the role of the central bank, in addition to ensuring price stability**, involves implementing monetary policies conducive to financial stability, regulating the banking system and overseeing payment systems, stimulating financial innovation and actively collaborating with market players. **This will also benefit from** the opportunities for long-term growth offered by digital innovations, while mitigating emerging risks.

This set of structural measures will facilitate the improvement and consolidation of a business climate conducive to the emergence of a competitive private sector in an environment favourable to sustainable and balanced territorial development.

**Finally, it is noteworthy that the "optimal" financial structure is a dynamic** concept that requires permanent adjustments and adaptations, depending on economic developments and conditions.