

AFRICA RISK CONSULTING

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The International Monetary Fund (IMF) warns that Algeria's foreign exchange reserves have fallen 26% since 2013. The government needs to enact wide ranging structural reforms to preserve growth in the medium term. State-owned natural resources company Société Nationale pour la Recherche, la Production, le Transport, la Transformation, et la Commercialisation des Hydrocarbures (Sonatrach) embarks on a \$3.2 billion programme to expand Algeria's gas pipeline infrastructure. Sonatrach also awards contracts for refineries, oil extraction, oil services and mining to China, France, Germany, Holland, Japan and United Kingdom-based companies. Russia's foreign minister Sergei Lavrov meets President Abdelaziz Bouteflika (1999-present) for talks on greater security cooperation in Libya and Syria. The Russian delegation also discusses greater investment in Algeria's energy sector and the possible construction of a nuclear power plant by a Russia-based company.

IMF warns of falling foreign currency reserves

The **International Monetary Fund (IMF)** reported that Algeria's foreign currency reserves fell \$35 billion in 2015 to a total of \$143 billion on 14 March.¹ Algeria has dug deep into its considerable foreign currency reserves in order to fund its budget deficit. The IMF warned that the country needs to speed up the progress of its economic reforms in order to avoid running out of capital. **North Africa** staff leader **Jean-Francois Dauphin** said:

*"Rapidly declining fiscal savings mean that Algeria will need to rely more on borrowing to finance future deficits... Wide-ranging structural reforms are needed to help support economic activity during fiscal consolidation and to diversify the economy to achieve high and inclusive growth over the medium term."*²

The low price of oil has reduced Algeria's foreign reserves by 26% from \$194 billion in 2013; they were at \$178.94 billion in December 2014.³ The recent figures fall short of the \$151 billion that finance minister **Abderrahmane Benkhalfa** projected for year-end 2015 in the 2016 Finance Bill in November 2015.⁴ Benkhalfa projects that by the end of 2016, reserves will fall a further 15% to \$121 billion.⁵ This is equivalent to 23 months of import cover.⁶

The government's income from energy, which makes up 95% of export revenues and 60% of the budget, fell by 41% across 2015.⁷ Energy income totaled \$35.72 billion in 2015, down from \$60.54 billion in 2014. The IMF predicts that this will drop further in 2016 to \$26.4 billion.⁸ The treasury

¹ APS, 14 Mar 2016.

² Dauphin, in APS, 14 Mar 2016.

³ APS, 14 Mar 2016.

⁴ Jeune Afrique, 15 Mar 2016.

⁵ APS, 14 Mar 2016.

⁶ Jeune Afrique, 15 Mar 2016.

⁷ APS, 14 Mar 2016.

⁸ APS, 14 Mar 2016.

predicts total 2016 revenue to be \$46 billion, meaning that oil and gas revenues will account for 65% of government income.⁹

The IMF estimated that Algeria's budget deficit for 2016 will be 16% of gross domestic product (GDP).¹⁰ This is more than the \$30.5 billion, or 14% of GDP, the treasury projects.¹¹ It forecasts strong growth of 3.7% across the year (5% for the non-oil sector) and inflation at 4.8%.¹² According to local economic sources, Algeria is still managing its deficit sensibly, despite the decrease in reserves:

"Algeria is in a stronger position than other oil dependent economies on the continent because it has such extensive reserves...the government is right to spend them rather than passing the buck along to businesses and consumers, damaging growth. However, it places a time limit on their programme to rebalance the economy, and currently we are running out of reserves faster than it is growing non-oil exports."¹³

Sonatrach embarks on expansion plans and awards multiple tenders

State-owned oil and gas company **Société Nationale pour la Recherche, la Production, le Transport, la Transformation, et la Commercialisation des Hydrocarbures (Sonatrach)** has embarked on an expansion of its operations, upgrading its infrastructure and awarding contracts to multiple international firms in the oil, gas and mining sectors. This is moving away from its previous position of being wary of awarding contracts to companies based outside Algeria:

"We have tried to do business with Sonatrach before, but they were very slow and didn't want to give their money away to us...now they are coming back and telling us to submit for tenders. It is a big change."¹⁴

Sonatrach announced a four-year \$3.2 billion pipeline expansion programme on 8 March.¹⁵ Algeria is increasing its natural gas production capacity but lacks the infrastructure to transport the commodity for internal power generation or export.¹⁶ **Arbi Bey Slimane**, Sonatrach's vice president for pipelines and transportation, made the announcement to the media.¹⁷ The company will invest a total of \$3.2 billion to increase its transport capacity between 2016 and 2020.¹⁸ This includes spending \$350m in 2016.¹⁹ The investment will support a new network of 1,650km of pipeline and six compression stations.²⁰ Algeria currently produces 27.44 billion cubic metres of gas and 1.1 billion barrels of oil per day.²¹ New finds at new gas fields in the south and west of the country are expected to come online from this year and will substantially increase gas production (see *ARC Briefing Algeria February 2016*).²² The government is in talks with the **European Union (EU)** to export gas to reduce the bloc's reliance on **Russia** as a supplier.²³ According to an industry source:

"Production in Algeria flat-lined for the past ten years, they have been a mid-level exporter but not able to offer a serious alternative to Russia or Norway... they are now offering a better proposition for major export markets."²⁴

⁹ Jeune Afrique, 15 Mar 2016.

¹⁰ APS, 14 Mar 2016.

¹¹ Jeune Afrique, 15 Mar 2016.

¹² APS, 14 Mar 2016.

¹³ Source, economist, Algiers

¹⁴ Source, oil and gas company, Brussels

¹⁵ Le Matin, 8 Mar 2016.

¹⁶ Le Matin, 8 Mar 2016.

¹⁷ Reuters, 8 Mar 2016.

¹⁸ Reuters, 8 Mar 2016.

¹⁹ Le Matin, 8 Mar 2016.

²⁰ The Africa Report, 8 Mar 2016.

²¹ Le Matin, 8 Mar 2016.

²² The Africa Report, 8 Mar 2016.

²³ The Africa Report, 8 Mar 2016.

²⁴ Source, oil and gas analyst, London

Sonatrach is also expanding its refining capacity. It awarded a front-end engineering and design (FEED) contract for three new refineries to **United Kingdom (UK)**-based firm **Amec Foster Wheeler** on 9 March.²⁵ The three new refineries at **Biskra**, **Tiaret** and **Hassi Messaoud** will each have a capacity of 5 m tonnes/year. They will produce refined oil and gas products including liquefied petroleum gas (lpg), bitumen, and lubricant oil.²⁶ The sites will also have laboratories, storing and shipping facilities.²⁷ Amec Foster Wheeler expects to complete the contracts in the third quarter of 2017.²⁸

On the production side Sonatrach awarded **Japan**-based **JGC** a \$339m contract to increase production at its largest oilfield on 3 March.²⁹ JGC will work with Sonatrach to increase production at the Hassi Messaoud oil field by upgrading and improving the current systems of production.³⁰ The field currently produces 350,000 barrels of crude oil per day.³¹ JGC has worked with Sonatrach for over 40 years. Major projects include the **Gassi Touil** gas processing plant completed in 2013 and the **Rhourde Nouss** oil processing plant completed in 2012.³²

The company also executed contracts to services suppliers. According to senior officials the company is aiming to expand its list of approved suppliers and contractors.³³ It awarded an \$880m contract to supply oil and gas drilling tubes to four international firms on 11 March.³⁴ The companies are **Germany**-based **CCC Machinery**, **Netherlands**-based **Van Leeuwen**, **Japan**-based **Marubeni-Itochu**, and **France**-based **Vallourec Tubes**.³⁵ According to a Sonatrach official, they will be awarding tenders on a broad basis across the year:

*"We urge all the contractors to participate en masse in the next tenders."*³⁶

Sonatrach is also expanding its mining business. The company is in talks with **China**-based **China Civil Engineering & Construction Company (CCECC)** to develop Algeria's largest iron ore deposit.³⁷ Algeria imports its steel at considerable cost and has looked for a partner to develop iron ore prospects for some years. The CCECC is looking to develop the **Gara Djebilet** iron ore prospect in **Tindouf** province.³⁸ The mining ministry estimates the project has reserves of approximately 2.5 billion tonnes of iron ore.³⁹ The Algerian government has operated a mine on the site since 1952, but it has been out of use for almost 50 years due to the poor infrastructure to the remote site.⁴⁰ The CCECC and mining ministry have been discussing the prospect of the development since late February. Sonatrach has had to delay the project several times due to technical difficulties since it started trying to develop it in 2009.⁴¹

Algeria and Russia in security and energy talks

President **Abdelaziz Bouteflika** (1999-present) discussed greater security operations and energy projects in Algeria with Russia's foreign minister **Sergei Lavrov** during talks in **Algiers** on 29

²⁵ ICemE, 9 Mar 2016.

²⁶ ICemE, 9 Mar 2016.

²⁷ ICemE, 9 Mar 2016.

²⁸ ICemE, 9 Mar 2016.

²⁹ Bloomberg, 3 Mar 2016.

³⁰ Bloomberg, 3 Mar 2016.

³¹ Bloomberg, 3 Mar 2016.

³² www.jgc.com

³³ Reuters, 11 Mar 2016.

³⁴ Reuters, 11 Mar 2016.

³⁵ Reuters, 11 Mar 2016.

³⁶ Sonatrach official in Rigzone, 11 Mar 2016.

³⁷ Mining Weekly, 11 Mar 2016.

³⁸ Mining Weekly, 11 Mar 2016.

³⁹ Reuters, 10 Mar 2016.

⁴⁰ Reuters, 10 Mar 2016.

⁴¹ Reuters, 10 Mar 2016.

February.⁴² Algeria and Russia are historic allies and have grown closer economic ties in recent years. Russian-Algerian trade in 2015 totaled \$2 billion, growing 120% on 2014.⁴³ Lavrov also met with prime minister **Abdelmalek Sellal** and foreign minister **Ratmane Lamrara**, both of whom are considered potential candidates to succeed the ageing president.⁴⁴

The talks focused on security – fighting organised crime and terrorist organisations in North Africa. The two issues often overlap with **Al Qaeda in the Islamic Maghreb (AQIM)** and **Islamic State (IS)** affiliated groups involved with drug smuggling through Algeria’s southern regions.⁴⁵ Lavrov told the media that the president had expressed support for Russian president **Vladimir Putin’s** (1999-2004, 2012-present) plan to create a unilateral anti-terror coalition under the auspices of the **United Nations (UN)**.⁴⁶ He also said Bouteflika agreed that Algeria would support Russia’s efforts to reach a solution to instability in **Syria**.⁴⁷ Russia, in turn, will support Algeria’s efforts to create a stable government and state in **Libya**.⁴⁸ Libya is a major hub of regional instability and provides organised crime and terrorist organisations with an easy route into **Europe** and the **Middle East**.⁴⁹

The talks also focused on the energy sector. Algeria and Russia will continue to cooperate under the framework of the **Forum of Gas Exporting Countries (FGEC)**. Sonatrach will explore more contracts with Russian companies looking to invest in Algeria.⁵⁰ Lavrov remained in Algeria for bi-lateral talks on non-energy uses of nuclear power, which started on 1 March.⁵¹ There he discussed the potential development of a Russian-designed power plant in Algeria.⁵² Algeria is seeking to diversify its energy generation in order to reduce its reliance on imported liquefied natural gas and plans to build a nuclear power plant by 2030.⁵³

Implications

Algeria’s considerable foreign reserves give it a financial buffer that other oil dependent economies lack. However, the current overspend by the state casts doubt on whether Benkhalfa’s plans to diversify the economy before foreign reserves run out will succeed. Despite the multiple finance bills in 2015 and 2016 there is little evidence of actual structural reform in Algeria of the kind that will encourage businesses to grow.

Sonatrach has undertaken significant reform since **Amine Mazouzi** came in as CEO last year. The company is losing its reputation for reluctance to issue tenders to international companies. It is also spending money to expand its operations while the oil price is low. This is part of the wider government strategy to increase output to put the economy on a better footing if the oil price rises again. With a rush of contracts, investors should also be aware of the historic concerns over corruption in Sonatrach, which Mazouzi claims are no longer a danger.

Algeria is the most active player in securing the stability of North Africa as well as areas of the **Sahel**. It has hosted running peace talks on Libya since 2011. Russia’s offer of joint security cooperation will help Algeria lobby for the solutions it wants in the region and help it advance in international standing. Algeria offers Russia a regional ally to help prevent the root causes of its domestic terrorism concerns and to back its plans to secure a peace deal in Syria.

⁴² L’Expression, 29 Feb 2016.

⁴³ TASS, 29 Feb 2016.

⁴⁴ TASS, 29 Feb 2016.

⁴⁵ TASS, 29 Feb 2016.

⁴⁶ TASS, 29 Feb 2016.

⁴⁷ TASS, 29 Feb 2016.

⁴⁸ TASS, 29 Feb 2016.

⁴⁹ TASS, 29 Feb 2016.

⁵⁰ TASS, 29 Feb 2016.

⁵¹ L’Expression, 29 Feb 2016.

⁵² L’Expression, 29 Feb 2016.

⁵³ APS 29 Feb 2016.

About Africa Risk Consulting:

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