Finance law reforms help to encourage foreign investment in Algeria

Houda Sahri, Jean-Jérôme Khodara and Nahla Djabi of Matouk Bassiouny in association with SH-Avocats explore how the Algerian government is moving to diversify its economy, and consider the application of the 49/51 rule

Over two years have passed since the issuance of the 2020 Finance Law (FL 2020) in December 2019, which has removed most of the restrictions curtailing foreign investment, namely the state's pre-emption right on the transfer of shares by or to foreign shareholders, the prohibition on investors to finance their projects in Algeria with facilities from foreign lenders, and the so-called '49/51 rule' pursuant to which the capital of Algerian companies must be at least 51% owned by Algerian resident persons or entities, thus limiting foreign investors' stake to 49% (the 49/51 rule).

By any measure, the 49/51 rule had become the most notorious symbol of challenges impeding foreign investment. The 49/51 rule used to apply across the board to all industries. The FL 2020 provided that the 49/51 rule shall apply only to purchase and resale activities and to sectors considered as 'strategic'.

Since then, other laws and regulations have been issued to complete, clarify and detail the application of such rule in addition to the amendment of other regulations. Such restructuring of foreign investment framework is emphasised by the need of Algeria to diversify its economy and create autonomy from the oil and gas industry, which has been the main source for income of the country in terms of hard currency. Creating a balance between opening its market and protecting its fragile emerging economy, while stimulating recovery after years of closure is the challenge facing Algeria.

In this article, we provide a status update on the reforms that were initiated and their application.

Background

It seems that the Algerian economy has started to recover in 2021 thanks to the relaxation of containment measures and a rebound in hydrocarbon prices and production.

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Indeed, led by the oil and gas sector, the Algerian economy expanded by 3.9% year-on-year during the first nine months of 2021, after contracting by 5.5% in 2020, however, as of September 2021, non-hydrocarbon GDP was still 3% below its pre-pandemic level (World bank Algeria's economic updated, April 2022)..

In other terms, where GDP is expected to rebound to its pre-pandemic level in 2022 due to the rise of hydrocarbon production and exports, we are still to witness the impact of the implementation of the government's structural reform agenda in the private sector.

Alleviation of the 49/51 rule

The first significant alteration to the 49/51 rule was initiated under the FL 2020, which loosened the application of the 49/51 rule, where the FL 2020 provided that the 49/51 rule shall only apply to "production and service activities which are strategic for the national economy". Accordingly, the FL 2020 has transformed the 49/51 rule from a general rule to a rule of exception by means of limiting its application to strategic sectors.

Pursuant to the Supplemental Finance Law for 2020 (promulgated on June 4 2020, the SFL 2020) and to the Finance Law for 2021 (promulgated on December 31 2020, the FL 2021), sectors that remain subject to the 49/51 rule include importation for resale without transformation and the following strategic sectors: mining, energy, defence, transport infrastructure, and pharma. Decree No. 21-145 dated April 2021 has clearly defined the strategic sectors in terms of codes of activities.

It is worth noting that most of the pharmaceutical activities are concerned with the 49/51 rule while the sectors of (i) the electricity production from renewable energies; and (ii) the downstream of the hydrocarbon sector (except for the

"Algeria needs to diversify its economy and create autonomy from the oil and gas industry"

transportation through pipeline) including services, refining or oil drilling have been excluded from such rule.

Sectors that remain subject to the 49/51 rule

Importation activities

Algerian authorities continue their policies of curbing importations in order to protect the country's balance of payments and to preserve its reserves of foreign currency. In this context, a series of stringent rules have been issued since the issuance of the SFL 2020 to increase the authorities' oversight on the importation sector which remains subject to the 49/51 rule.

Indeed, the sector of importation for resale without transformation has gone through major changes these last two years. First, companies undertaking this activity have been required to restrict their importation to one industry only. In practice, the implementation of this new rule consists in requiring importation companies to amend their scope of activity (and hence to amend their trade register) to limit their importation activity to one industry only.

In this context and in order to streamline the activities of the importation, the Trade Register has re-organised the labelling (i.e. the wording used to describe a given activity) and the code numbers of importation activities and has required all importation companies to update their trade register by December 31 2021.

While economically, the Algerian foreign balance is recovering due to the rise in the hydrocarbon prices, we do not expect a relaxation in the importation sector, especially in the pharma and automotive sectors.

Strategic sectors

In April 2021, an executive regulation has been issued (Decree 21-145 dated April 7 2021, setting forth the list of activities considered as strategic) to set forth the detailed activities (based on the classification of the trade register) which fall within the scope of the above strategic activities (except for the defence industry).

The financial law for 2022 (FL 2022) has brought some clarifications on the strategic sectors subject to the 49/51 rule. Indeed, it has excluded activities relating to exploitation of the national mining domain, as well as the upstream energy activities, and all other activities governed by the law on hydrocarbons from the list of activities considered strategic. However, these activities remain subject to the local partnership rules according to the conditions provided for by specific laws.

Such exclusion confirmed that renewable energy is not included in the list of strategic sectors. As a result, independent electricity producers would no longer be subject to the 49/51 rule. This may create unique market opportunities for players in the field of renewables, especially when considering that Algeria is initiating a national green energy project with an ambitious programme for the development of renewable energies (RE) and energy efficiency.

In this context, the newly created Algerian Ministry of Energy Transition and Renewable Energies has launched in December 2021, a call for tenders to investors for the development of photovoltaic solar centrals with a total capacity of 1000 MW throughout the territory.

The creation of the Ministry of Energy Transition and Renewable Energies in 2020 was by itself a clear move confirming the commitment of Algerian Authorities to

"Creating a balance between opening Algeria's market and protecting its emerging economy is the challenge"

their optimistic programme in the field of renewables with a targeted installed capacity of 22,000 MW by 2030 for the domestic market.

Indeed, under this call for tenders, foreign companies may own up to 66% of the joint-venture company undertaking the execution of the project in partnership with SHAMS, the newly created state-owned company that will be responsible for renewable energies.

Automotive industry

The automotive sector is one of the most controversial topics in Algeria. Indeed, the Decree 20-227 dated August 19 2020, (the Automotive Decree), has restricted the activity of importers/dealers to Algerian companies which 100% owned by Algerian residents, hence foreign investors are prohibited from carrying-out these activities (except those involved in local manufacturing).

The Automotive Decree provides for stringent requirements on importers and resellers of new cars such as (i) the limitation of the license for distribution to only one approval (license) by a distributor for a maximum of two automobile brands and three engine brands; and (ii) the requirement to develop a national sales network within one year following the obtaining of the approval.

However, to date the Automotive Decree has not been implemented and no new license has been issued. The Ministry of Industry has already launched the review of the Automotive Decree. Hopefully, such review will result in foreign investors being allowed back in the activities of importation and distribution of automobiles.

New draft of the Investment Law

The creation of a new legislative and regulatory framework for investment in Algeria is part of the overall goal of addressing the shortcomings identified since the issuance of the previous investment law in 2016.

With the ultimate goal of creating a stable, predictable, fair, and transparent environment to facilitate and encourage investment, and, in particular, attract foreign direct investment (FDI), the Algerian authorities are discussing a new investment law to create a healthy climate and a trustworthy environment that shields the investors from arbitrary administrative decisions and frequent policy shifts.

The draft of the new investment law aims to restructure the institutional ecosystem tasked with enforcing investment regulations and endow it with the necessary authority and capacity to translate these regulatory reforms into actual measures to improve the business climate.

The draft of the new investment law provides for different regimes of incentives including (i) the general incentive regime; (ii) an incentive regime for activities that are considered a priority by the Algerian government which list is yet to be defined; (iii) incentive regime for investment in areas requiring special support such as the south region of Algeria; (iv) incentive scheme for structuring investments which are related to investments that are considered of great interest to the country; and (v) incentive scheme relating to activity zones such as industrial zones and logistics zones.

The incentives vary between those attributed at the implementation phase such as customs exemptions or facilitation, a reduction of rental fees for the plots of land granted by the state during the construction phase and those attributed during the exploitation phase which varies from tax exemptions (including VAT and income taxes) to reduction of the rental fees.

To this end, it is planned to create within the National Agency for Development, which will bear a new name 'Algerian Agency for the Promotion of Investment', a one-stop-shop dedicated to major investments and foreign direct investment as well as a regional one-stop-shop for investment, in charge of all the steps necessary for the realisation of investment projects.