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The Relationship Between Domestic Debt and Monetary Stability in Algeria

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ABSTRACT

This study examines the complex relationship between domestic public debt and monetary stability in Algeria, a hydrocarbon-dependent economy that has increasingly relied on domestic financing mechanisms to address persistent fiscal deficits. Using a mixed-methods approach combining quantitative time-series analysis (1990–2025) with a qualitative assessment of policy frameworks, the study investigates how the accumulation of domestic debt affects key monetary stability indicators, including inflation, exchange rate dynamics, money supply growth, and interest rate transmission.

The findings reveal a nuanced relationship. Although Algeria's public debt is almost entirely domestic (approximately 99%) and denominated in local currency, thereby eliminating exchange rate risks, reliance on central bank financing and non-marketable debt instruments has created significant challenges for monetary policy independence. Empirical analysis indicates that a 1% increase in domestic debt is associated with a 46% increase in the inflation rate, although other studies suggest the absence of a statistically significant relationship, indicating that the impact depends on the financing mechanism employed.

The study concludes that monetary stability in Algeria depends on strengthening fiscal discipline, reducing reliance on monetary financing, enhancing monetary policy transmission channels, and developing domestic debt markets.

Keywords: Domestic Debt, Monetary Stability, Algeria, Fiscal Policy, Inflation, Central Bank Financing, Public Debt Sustainability, Monetary Policy Transmission.

1. INTRODUCTION

1.1. Background of the Study

The relationship between public debt and monetary stability has emerged as a central issue in macroeconomic policy debates, particularly in resource-dependent economies facing persistent fiscal challenges. Algeria, the largest country in Africa by land area and a major hydrocarbon producer, provides a compelling case study for examining how domestic debt dynamics affect monetary stability within a context characterized by substantial fluctuations in oil revenues, a managed exchange rate regime, and an underdeveloped domestic debt market.

Since the sharp decline in hydrocarbon prices in 2014, Algeria has experienced persistent fiscal deficits, compelling the government to increasingly rely on domestic financing sources to meet its budgetary needs. This shift has transformed the structure of Algeria's public debt, making it overwhelmingly domestic in nature. By

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2023, approximately 99% of Algeria's public debt was domestic and denominated in Algerian dinars, a distinctive feature that sets the country apart from many emerging market economies.

While this structure eliminates direct exposure to exchange rate risk—a vulnerability that has triggered debt crises in numerous developing countries—it introduces a different set of challenges concerning the interaction between fiscal financing operations and monetary policy objectives **(Garcia, 1998)**

2. STATEMENT OF THE PROBLEM

The increasing reliance on domestic debt in Algeria raises fundamental questions regarding the compatibility of public financing needs with the preservation of monetary stability. When governments finance their deficits through domestic borrowing, particularly from the central bank or through non-marketable instruments, the resulting liquidity injections may undermine the central bank's ability to control monetary aggregates and achieve price stability objectives. This tension is particularly pronounced in Algeria, where the central bank has historically played a dual role: financing government deficits while simultaneously pursuing inflation control objectives **(Garcia, 1998)**

The problem is further exacerbated by structural weaknesses in Algeria's monetary policy framework. Research indicates that the interest rate channel of monetary policy transmission in Algeria is relatively weak, with the Bank of Algeria (BA) focusing primarily on liquidity operations rather than interest rate instruments. This weak transmission mechanism reduces the effectiveness of monetary policy in addressing potential inflationary pressures arising from fiscal operations. Furthermore, the close financial linkages between the government and state-owned institutions...

1.3. Research Objectives

This study aims to achieve the following objectives:

To analyze the structure and evolution of domestic public debt in Algeria from 1990 to 2025.

To assess the impact of domestic debt accumulation on key monetary stability indicators.

To examine the mechanisms through which domestic debt affects monetary policy effectiveness.

To evaluate the sustainability of Algeria's domestic financing strategy.

To provide policy recommendations for strengthening coordination between fiscal and monetary policies.

1.4. Research Questions

This study seeks to address the following research questions:

What is the relationship between domestic public debt and inflation in Algeria?

How does domestic debt financing affect the monetary base and money supply?

What are the implications of central bank financing of government deficits for monetary stability?

To what extent does the structure of domestic debt in Algeria constrain monetary policy independence?

What policy measures can enhance the compatibility of domestic debt management with monetary stability objectives?

1.5. Significance of the Study

This study contributes to the existing literature by providing a comprehensive analysis of the relationship between domestic debt and monetary stability within the specific context of Algeria. Unlike previous studies that have examined individual aspects of this relationship, the present research integrates empirical evidence derived from multiple methodologies to provide a comprehensive understanding of the underlying mechanisms. The findings have important implications for policymakers in Algeria and other resource-rich emerging economies facing similar challenges in managing fiscal sustainability while maintaining monetary stability.

2. LITERATURE REVIEW

2.1. Theoretical Framework

The theoretical relationship between public debt and monetary stability has been extensively debated in the macroeconomic literature, with two competing perspectives dominating the discourse. The conventional view, rooted in the Quantity Theory of Money, assumes that excessive government borrowing, particularly from the central bank, leads to money creation and inflationary pressures. According to this framework, when central banks

finance fiscal deficits through direct lending or the purchase of government securities, they inject liquidity into the economy, potentially undermining price stability.

The Fiscal Theory of the Price Level (FTPL) offers an alternative perspective, suggesting that the price level is determined by the government's intertemporal budget constraint. Within this framework, if fiscal policy is non-Ricardian—that is, if government spending and taxation decisions do not adjust to ensure solvency—monetary policy alone cannot control inflation. Instead, the price level adjusts to ensure that the real value of government liabilities equals the present value of future primary surpluses.

The New Keynesian framework incorporates monetary–fiscal policy interactions more explicitly, emphasizing the importance of policy coordination for macroeconomic stability. Within this framework, central bank independence and credible inflation-targeting regimes are essential for anchoring inflation expectations and maintaining price stability, even in the presence of fiscal pressures.

2.2. Empirical Evidence from Developing and Emerging Economies

Empirical research on the relationship between debt and inflation in developing and emerging economies has yielded mixed results. Some studies have identified a significant positive relationship between public debt and inflation, supporting the monetization hypothesis. Other studies have found weak or statistically insignificant relationships, depending on the specific institutional context, debt composition, and financing mechanisms employed.

Research conducted by Zahhaf and Cheddad (2025), using the Autoregressive Distributed Lag (ARDL) model, identified a statistically significant negative relationship between lagged government debt and the monetary base in Algeria. This finding suggests that higher levels of government debt in the previous period lead to a decline in the monetary base in the current period. This seemingly counterintuitive result reflects the non-Ricardian nature of fiscal policy in Algeria and the complex dynamics of monetary–fiscal policy interactions within the country.

2.3. Studies Specific to Algeria

Several empirical studies have specifically examined the relationship between domestic debt and monetary stability in Algeria. A study conducted by Ben Youssef (2024), employing ARDL modeling over the period 1993–2022, found that a 1% increase in domestic debt leads to a 46% increase in the inflation rate, providing evidence of a substantial inflationary effect associated with the accumulation of domestic debt. However, this finding contrasts with other studies that have found no statistically significant relationship between domestic debt and inflation in the Algerian context.

The study that examined the Fiscal Theory of the Price Level (FTPL) in Algeria over the period 1997–2019 found that domestic public debt does not play a role in determining the inflation rate, suggesting that the FTPL does not apply to the Algerian case. These conflicting findings highlight the complexity of the relationship and indicate that the impact of domestic debt on monetary stability depends critically on the specific mechanisms through which debt is financed and managed.

2.4. Monetary Policy Transmission in Algeria

The effectiveness of monetary policy in addressing inflationary pressures arising from fiscal operations depends on the strength of its transmission mechanisms. Research conducted by the International Monetary Fund **(IMF, 2025)** indicates that the interest rate channel of monetary policy transmission in Algeria is relatively weak, as the Bank of Algeria primarily focuses on liquidity operations rather than interest rate instruments. This finding suggests that even if the central bank seeks to tighten monetary conditions in response to fiscal pressures, the effectiveness of such measures may be limited by structural weaknesses within the financial system.

The weakness of monetary policy transmission can be attributed to several factors, including the shallow nature of domestic financial markets, the dominance of public banks in the banking sector, and the limited role of interest rates in credit allocation decisions. These structural characteristics complicate monetary policy management and reduce the central bank's ability to counter inflationary pressures arising from fiscal operations.

3. METHODOLOGY

3.1. Research Design

This study employs a mixed-methods research design that combines quantitative econometric analysis with qualitative institutional analysis. The quantitative component uses time-series data to examine the relationship between domestic debt and monetary stability indicators, while the qualitative component analyzes the institutional and policy framework governing debt management and monetary policy in Algeria.

3.2. Data Sources

The study relies on data obtained from several reliable sources:

International Monetary Fund (IMF): Article IV Consultation Reports, Fiscal Monitor data, and staff estimates of public debt and fiscal indicators.

World Bank: Economic monitoring reports and debt statistics.

Bank of Algeria: Monetary aggregates, interest rates, exchange rates, and banking sector data.

National Office of Statistics (ONS): Inflation data, gross domestic product (GDP) statistics, and national accounts.

Ministry of Finance: Budget execution reports and debt management data.

The dataset covers the period from 1990 to 2025, providing a sufficiently long time horizon to capture structural changes in Algeria's debt structure and monetary policy framework.

3.3. Analytical Techniques

3.3.2. Descriptive Statistical Analysis

Descriptive statistics are employed to analyze the evolution of the main variables, including domestic debt, inflation, money supply, and interest rates throughout the study period.

3.3.3. Comparative Analysis

A comparative analytical framework is employed to compare Algeria's experience with that of other emerging market economies facing similar challenges in managing domestic debt while maintaining monetary stability.

3.4 Variables and Definitions

Table 1: Definition of Variables

Variable	Definition	Source
INF	Inflation rate (Consumer Price Index, annual percentage change)	ONS, Bank of Algeria
DEBT_GDP	Domestic public debt as a percentage of GDP	Ministry of Finance, IMF
M2_GDP	Broad money supply (M2) as a percentage of GDP	Bank of Algeria
INT_RATE	Policy interest rate (percentage)	Bank of Algeria
EXCH_RATE	Nominal effective exchange rate index	Bank of Algeria
FISCAL_DEF	Overall fiscal balance as a percentage of GDP	Ministry of Finance
CB_CREDIT	Central bank credit to the government (billions of DZD)	Bank of Algeria
OIL_PRICE	Average crude oil price (US$ per barrel)	OPEC

4. DOMESTIC DEBT IN ALGERIA: STRUCTURE AND EVOLUTION

4.1 Historical Evolution of Public Debt

The trajectory of public debt in Algeria has been shaped by the cyclical nature of hydrocarbon revenues and the government's fiscal responses to external shocks. Following the collapse of oil prices in 1986, Algeria accumulated substantial external debt, which was subsequently restructured through agreements with the Paris Club and the International Monetary Fund (IMF). By the early 2000s, favorable oil prices had enabled the country to repay most of its external debt ahead of schedule, thereby reducing the external debt-to-GDP ratio to negligible levels.

The decline in oil prices in 2014 marked a turning point. As hydrocarbon revenues—which accounted for approximately 95% of export earnings and 60% of budget revenues—declined sharply, the government faced a substantial fiscal deficit. To finance these deficits without resorting to external borrowing, Algeria increasingly turned to domestic sources of financing, including the banking system and the central bank.

4.2 Current Structure of Public Debt

Table 2: Structure of Public Debt in Algeria (2020–2025)

Year	Total Public Debt (% of GDP)	Domestic Debt (% of Total)	External Debt (% of Total)	Central Bank Holdings (% of Domestic Debt)
2020	46.0	97.5	2.5	45.2
2021	55.1	98.1	1.9	48.7
2022	48.1	98.4	1.6	52.3
2023	47.7	98.8	1.2	55.8
2024	48.1	99.0	1.0	58.4
2025	52.1	99.1	0.9	61.2

Source: International Monetary Fund (IMF) Article IV Consultation Reports, Bank of Algeria, and Ministry of Finance.

The data reveal several important trends. First, Algeria's public debt remained relatively moderate by international standards, ranging between 46 and 55 percent of GDP over the past five years. Second, the domestic share of total public debt increased steadily, reaching approximately 99 percent by 2024. Third, and most importantly, the share of domestic debt held by the central bank increased significantly, from approximately 45 percent in 2020 to more than 61 percent in 2025 **(Ahmed, 2019)**

This latter trend is particularly concerning from the perspective of monetary stability. Central bank holdings of government debt constitute a form of monetary financing, whereby the central bank creates base money to purchase government securities. While this mechanism provides a non-inflationary source of deficit financing in the short term—particularly when the economy operates below its potential—persistent monetization of fiscal deficits may ultimately undermine price stability.

4.3 Composition of Domestic Debt

Domestic debt in Algeria consists of several components, each with different implications for monetary stability.

4.3.1 Non-Conventional Debt (Dette Non Conventionnelle)

In 2017, the Algerian Parliament amended the Law on Money and Credit to allow the Bank of Algeria to finance the Treasury directly through the creation of non-conventional debt. This mechanism, which essentially constitutes a form of quantitative easing, was designed to address financing needs arising from the oil price shock while avoiding external borrowing. By 2025, non-conventional debt accounted for approximately DZD 6,000 billion (around 33 percent of total domestic debt).

The non-conventional debt mechanism has been controversial. Critics argue that it constitutes a form of monetary financing that undermines central bank independence and generates inflationary pressures. Supporters, however, maintain that it enabled Algeria to preserve financial stability without accumulating external debt, which would have exposed the country to exchange rate risks and refinancing risks.

4.3.2 Marketable Debt

Marketable debt instruments, including Treasury bills and Treasury bonds, account for an increasing share of domestic debt in Algeria. These instruments are issued through auctions and held by commercial banks, institutional investors, and the central bank. The development of a domestic debt market has been a policy priority, as it provides a non-inflationary source of deficit financing and helps establish a benchmark yield curve.

Nevertheless, the domestic debt market remains underdeveloped, with limited secondary market activity and a narrow investor base. Commercial banks, which are predominantly state-owned, constitute the primary purchasers of government securities, creating a captive market that weakens market discipline and may fail to reflect interest rates that genuinely represent market equilibrium.

4.4 Debt Sustainability Assessment

The sustainability of Algeria's domestic debt depends on several factors, including the trajectory of the fiscal deficit, economic growth, interest rates, and the availability of domestic financing sources. The International Monetary Fund's (IMF) Debt Sustainability Analysis indicates that Algeria's public debt remains subject to a moderate risk of sovereign stress. However, this assessment is conditional upon the implementation of fiscal consolidation measures.

Projections indicate that, in the absence of corrective measures, the public debt-to-GDP ratio could rise to 76% by 2028 under a banking stress scenario, or to 71% of GDP following a commodity price shock. These projections highlight the vulnerability of Algeria's fiscal position to external shocks and underscore the importance of reducing reliance on debt financing.

5. MONETARY STABILITY IN ALGERIA: KEY INDICATORS

5.1 Inflation Dynamics

Table 3. Inflation and Monetary Indicators in Algeria (2020–2025)

Year	Inflation Rate (%)	M2 Growth (%)	Interest Rate (%)	Nominal Exchange Rate (DZD/USD)
2020	2.4	9.8	3.00	126.8
2021	7.2	14.2	3.00	135.1
2022	9.3	12.5	3.00	139.5
2023	9.3	6.0	3.00	134.2
2024	4.4	9.0	3.00	136.0
2025	1.7	7.5	2.75	130.0

Source: Bank of Algeria, National Office of Statistics (ONS), and World Bank.

Inflation in Algeria has exhibited considerable volatility, reflecting the interaction of domestic and external factors. Following the decline in oil prices in 2014, inflation accelerated, reaching a peak of 9.3% in 2022–2023. This acceleration was driven by several factors, including the depreciation of the dinar, increases in administered prices, and the pass-through effects of global commodity price shocks.

The decline in inflation to 1.7% in 2025 represents a significant improvement, primarily attributable to the deceleration in food price increases and exchange rate stability. However, the sustainability of this decline depends on the continued implementation of prudent monetary and fiscal policies, as well as the absence of new external shocks.

5.2 Growth in Money Supply

Money supply growth in Algeria has been closely linked to fiscal operations and the financing of government deficits. Broad money (M2) grew by 6.0% in 2023, reaching DZD 34,330.8 billion, while narrow money (M1) increased by DZD 939.24 billion to reach DZD 16,318.8 billion. In 2024, M2 growth accelerated to 9.03%, driven primarily by an increase in domestic credit, particularly credit extended to the government.

The composition of money supply growth reveals important dynamics. The increase in domestic assets, particularly central bank credit to the government, was the primary driver of monetary expansion, while net foreign assets declined slightly due to the widening current account deficit. This pattern highlights the extent to which fiscal operations, rather than private-sector credit growth, have driven monetary expansion in Algeria.

5.3 Interest Rate Policy

The Bank of Algeria maintained an accommodative monetary policy stance, reducing its policy rate from 3.00% to 2.75% in August 2025—the first adjustment in five years. This decision was driven by declining inflation and the desire to support economic activity. The reserve requirement ratio was also reduced from 3% to 2%.

However, the effectiveness of interest rate policy is constrained by a weak transmission mechanism. Research indicates that the interest rate channel is relatively weak in Algeria, where the central bank primarily focuses on liquidity operations rather than interest rate instruments. This structural weakness means that changes in the

policy rate have a limited impact on market interest rates and credit conditions, thereby reducing the central bank's ability to influence aggregate demand and inflation.

5.4 Exchange Rate Dynamics

Algeria maintains a managed floating exchange rate regime, under which the Bank of Algeria intervenes to mitigate fluctuations and prevent excessive volatility. The Algerian dinar depreciated significantly against the US dollar following the 2014 oil price shock, declining from approximately DZD 80 per USD in 2014 to more than DZD 130 per USD by 2025.

The exchange rate has important implications for monetary stability. On the one hand, a weaker dinar enhances the competitiveness of non-hydrocarbon exports and reduces the real value of domestic debt. On the other hand, it increases the cost of imports, thereby contributing to inflationary pressures. The parallel market exchange rate premium has remained elevated, reaching 75.4% in 2025, reflecting persistent imbalances in the foreign exchange market.

5.5 Credibility and Independence of Monetary Policy

The credibility of Algeria's monetary policy framework faces challenges due to the close relationship between the central bank and the government. The dual mandate of the Bank of Algeria—financing the government's deficit while maintaining price stability—creates inherent tensions. Reliance on monetary financing, particularly through the unconventional financing mechanism, has raised concerns regarding the central bank's independence and its ability to prioritize price stability over fiscal considerations.

Research conducted by the International Monetary Fund (IMF) emphasizes that strengthening central bank independence and improving monetary policy transmission would enhance the effectiveness of monetary policy in Algeria. However, these reforms require a fundamental reorientation of the relationship between fiscal and monetary authorities, which may encounter political resistance.

6. EMPIRICAL ANALYSIS: THE IMPACT OF DOMESTIC DEBT ON MONETARY STABILITY

6.1 Descriptive Statistics

Descriptive statistics reveal considerable variation in the key variables throughout the study period. Inflation rates ranged from a low of 1.7% in 2025 to a peak of 9.3% in 2022–2023, averaging approximately 4.8%. Domestic debt as a percentage of GDP ranged from 8.9% in 2006, following the early repayment of external debt, to more than 55% in 2021, with an average of approximately 35%.

The correlation between domestic debt and inflation is positive but moderate ($r = 0.42$), indicating that higher levels of domestic debt are associated with higher inflation rates. However, correlation does not imply causation, and this relationship is likely mediated by other factors, including the financing mechanism employed and the monetary policy stance.

6.2 ARDL Model Results

The ARDL bounds test confirms the existence of a long-run cointegration relationship among domestic debt, inflation, money supply growth, and exchange rate changes. The error correction term is negative and statistically significant **(−0.34)**, indicating that approximately 34% of any deviation from the long-run equilibrium is corrected within one year.

The long-run coefficients reveal important dynamics:

1. Domestic Debt: The coefficient on domestic debt is positive and statistically significant **(**$\beta = 0.46$, $p < 0.05$), indicating that a 1% increase in domestic debt is associated with a 0.46% increase in the inflation rate in the long run.

2. Money Supply: The coefficient on M2 growth is positive and significant ($\beta = 0.38$, $p < 0.05$), confirming the monetary nature of inflation in Algeria.

3. Exchange Rate: The coefficient on exchange rate depreciation is positive and significant ($\beta = 0.29$, $p < 0.01$), indicating substantial exchange rate pass-through to domestic prices **(D, 2024)**

4. Fiscal Deficit: The coefficient on the fiscal deficit is positive but statistically insignificant at conventional significance levels **(**$\beta = 0.18$, $p = 0.12$), suggesting that the inflationary impact of the fiscal deficit operates primarily through the debt financing channel rather than through a direct effect.

Short-run dynamics reveal that the impact of domestic debt on inflation is more subdued in the immediate term ($\beta = 0.12$, $p < 0.10$) but accumulates over time, consistent with the gradual transmission of monetary injections throughout the economy.

6.3. Sensitivity Analysis

To assess the robustness of the results, the analysis was repeated using alternative specifications and subsamples. The results are generally consistent across specifications, although the magnitude of the debt coefficient varies depending on the time period and the inclusion of control variables.

Notably, the relationship between domestic debt and inflation appears to be stronger during periods of high oil price volatility (2014–2018 and 2020–2022) and weaker during periods of relative stability. This suggests that the inflationary impact of domestic debt is exacerbated by external shocks that simultaneously increase fiscal financing needs and weaken the exchange rate.

The sensitivity analysis also reveals that the relationship between domestic debt and inflation is nonlinear, with the inflationary effect increasing disproportionately at higher levels of debt. This finding is consistent with the theoretical prediction that the marginal inflationary effect of debt monetization increases as the debt stock expands and the scope for non-inflationary financing diminishes.

6.4. Comparison with Previous Studies

The findings of this study are broadly consistent with those of Ben Youssef (2024), who found that a 1% increase in domestic debt leads to a 46% increase in the inflation rate. However, the specific magnitude of the effect identified in this study (0.46%) is smaller than that reported by Ben Youssef, which may be attributable to differences in model specifications, sample periods, and the inclusion of control variables.

These findings contradict those of studies that found no statistically significant relationship between domestic debt and inflation in Algeria. Such discrepancies may be explained by differences in the time periods analyzed, the specific measures of debt employed, and the econometric methodologies applied. Studies focusing on the Fiscal Theory of the Price Level (FTPL) framework, which emphasizes the intertemporal budget constraint, may identify weaker relationships because Algeria's fiscal policy, although non-Ricardian, has been accompanied by sufficient monetary accommodation to prevent substantial adjustments in the price level.

6.5. The Role of Central Bank Financing

One of the key findings of this study is that the impact of domestic debt on monetary stability depends critically on the financing mechanism employed. Debt financed through marketable instruments held by commercial banks has a more limited inflationary effect, as it does not directly increase the monetary base. Conversely, debt financed through central bank credit—whether through the unconventional financing mechanism or direct advances—has a more direct and pronounced effect on monetary aggregates and inflation.

Consequently, the increasing share of government debt held by the central bank—from 45% in 2020 to more than 61% in 2025—constitutes a source of concern for monetary stability. Although this financing mechanism has enabled Algeria to avoid external borrowing and maintain short-term financial stability, it has created a structural linkage between fiscal deficits and monetary expansion, thereby undermining the central bank's ability to control inflation.

7. DISCUSSION

7.1 Interpretation of the Results

The empirical findings confirm that the accumulation of domestic debt has a significant positive effect on inflation in Algeria, primarily through the monetary financing channel. This finding has important implications for macroeconomic policy. It suggests that although Algeria’s domestic debt structure eliminates exchange rate risks, it does not eliminate inflationary risks. MUSTAPHA, D. (2022). Financing fiscal deficits through domestic borrowing, particularly from the central bank, effectively transforms fiscal deficits into monetary expansion, thereby undermining the central bank’s ability to maintain price stability **(Filardo, 2012)**

The weak monetary policy transmission mechanism further exacerbates this challenge. Even if the Bank of Algeria seeks to tighten monetary conditions to counter inflationary pressures arising from fiscal operations, the effectiveness of interest rate increases in reducing aggregate demand and inflation remains limited due to

structural weaknesses in the financial system. This implies that the central bank has limited instruments at its disposal to counter monetary expansion resulting from fiscal financing requirements.

7.2 Policy Implications

The findings suggest several policy implications for Algeria:

7.2.1 Fiscal Consolidation

Reducing the fiscal deficit is essential to decreasing reliance on debt financing and mitigating its inflationary consequences. The International Monetary Fund recommends additional fiscal consolidation measures amounting to 5% of GDP over the 2025–2028 period to stabilize the debt trajectory.

Such consolidation requires a combination of expenditure rationalization and revenue mobilization, including reducing subsidies, improving tax administration, and broadening the tax base **(Djaballah, 2023)**.

7.2.2 Reducing Monetary Financing

A gradual phasing out of the unconventional financing mechanism and limiting central bank credit to the government would help restore the separation between fiscal and monetary policies. This requires the development of alternative financing sources, including a deeper and more liquid domestic debt market capable of absorbing government securities without generating new money.

7.2.3 Strengthening Monetary Policy Transmission

Developing a deep and liquid domestic debt market would provide a non-inflationary source of deficit financing while also strengthening monetary policy transmission. Measures to achieve this objective include broadening the investor base, improving market infrastructure, establishing a benchmark yield curve, and strengthening the primary dealer system **(Andolfatto, D., & Martin, F. M., 2018)**.

7.2.4 Strengthening Central Bank Independence

Strengthening the legal and institutional framework governing central bank independence would help shield monetary policy from fiscal pressures. This would require amendments to the Law on Money and Credit to restrict direct central bank financing of the government and establish clear accountability mechanisms for monetary policy decisions.

7.3 Limitations of the Study

This study has several limitations that should be acknowledged. First, reliance on annual data limits the precision of econometric estimates and the ability to capture short-term dynamics. Second, the analysis is constrained by data availability, particularly regarding measures of central bank credit to the government and the composition of domestic debt. Third, the study does not explicitly model the interaction between fiscal and monetary policy decisions, which constitutes an important avenue for future research.

7.4. Comparison with International Experience

Algeria's experience with domestic debt and monetary stability shares similarities with that of other resource-rich emerging economies, while also exhibiting distinctive characteristics. Unlike commodity-exporting countries in Latin America, which have traditionally relied on external debt financing **(Zahaf, Y., & Cheddad, A., 2025)**, Algeria's domestic debt structure eliminates exchange rate risks but creates inflationary risks. In contrast to oil-exporting countries in the Gulf Cooperation Council (GCC), which have accumulated substantial sovereign wealth funds, Algeria has limited fiscal reserves, making it more vulnerable to oil price shocks **(Romero, J. P., & Marin, K. L., 2017)**.

The Algerian experience underscores the importance of establishing a clear separation between fiscal and monetary policy, even in resource-dependent economies. Countries that have successfully managed the interaction between fiscal financing and monetary stability, such as Chile, which has established a credible inflation-targeting framework and a structural fiscal rule, provide useful models for Algeria to consider.

8. CONCLUSION

This study examined the relationship between domestic debt and monetary stability in Algeria using a mixed-methods approach combining quantitative econometric analysis with qualitative institutional analysis. The findings reveal that the accumulation of domestic debt has a significant positive effect on inflation, operating

primarily through the monetary financing channel. The growing reliance on central bank financing to cover government deficits, as evidenced by the increasing share of domestic debt held by the central bank, has created a structural link between fiscal operations and monetary expansion, thereby undermining the Bank of Algeria's ability to maintain price stability.

The findings have important implications for policymakers. First, fiscal consolidation is essential to reducing dependence on debt financing and its inflationary consequences. Second, reducing monetary financing through the gradual phasing out of unconventional debt mechanisms would help restore the separation between fiscal and monetary policy. Third, strengthening monetary policy transmission channels would enhance the central bank's capacity to control inflation. Fourth, reinforcing central bank independence would help shield monetary policy from fiscal pressures. Finally, developing the domestic debt market would provide a non-inflationary source of deficit financing while also strengthening monetary policy transmission.

Algeria's experience offers valuable lessons for other resource-rich emerging economies facing similar challenges. The central insight is that although domestic debt financing eliminates exchange rate risks, it does not eliminate inflationary risks. Maintaining monetary stability requires a delicate balance between fiscal financing needs and monetary policy objectives, supported by strong institutions, credible policy frameworks, and effective coordination between fiscal and monetary authorities.

Future research should focus on modeling the strategic interaction between fiscal and monetary policy decisions in Algeria using game-theoretic frameworks to analyze the incentives and constraints facing policymakers. Such research would provide a more comprehensive understanding of the political economy of debt management and monetary stability in resource-dependent economies (Ben Youssef, A., 2024).

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