The Relationship Between Central Banks and Islamic Banks A Study of Liquidity Between Flexibility and Regulation – A Case Study of Al Baraka Bank

Aouatef MAHCENE [1,], Saida TELLI [2], Djamel BETTAYB [3]
[1] Faculty of Economics, Business and Management Sciences, University of Ouargla (Algeria)
(mahcene.aouatef@univ-ouargla.dz)
[2] Faculty of Economics, Business and Management Sciences, University of Ouargla (Algeria)
(saidatelli@gmail.com)
[3] Faculty of Economics, Business and Management Sciences, University of Ouargla (Algeria)
(djamelbettayebf@gmail.com)

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Summary: This study aims to examine the nature of the relationship between the Bank of Algeria and Al Baraka Bank of Algeria. It also aims to examine the extent of its flexibility in terms of banking liquidity, by reconciling compliance with international regulatory standards and its specific characteristics. Although legislation governing the operations of these banks has been enacted, such as Article 71 of the Monetary and Banking Law No. 23-09, The Bank of Algeria has not provided any exceptions or a liquidity management infrastructure for these banks. We used a descriptive-analytical approach to examine Al Baraka Bank's liquidity management strategies, relying on financial analysis criteria.

One of the most significant findings is Al Baraka Bank's capability to meet international regulatory standards, including the quantitative and qualitative requirements of Basel III. Although it has established appropriate strategies for managing liquidity risk, it still maintains substantial excess liquidity, as in the case with other Islamic banks, continues to hold significant liquidity excess due to the absence of Sharia-compliant mechanisms and instruments, such as Islamic sukuk, as well as a lack of liquidity management infrastructure, including an absence of an Islamic financial market and liquidity-supporting bodies.

Keywords: Bank of Algeria, Al Baraka Bank, liquidity risk, Islamic banks, risk management.

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* Aouatef MAHCENE mahcene.aouatef@univ-ouargla.dz

I-Introduction:

The supervisory methods and mechanisms adopted by the Bank of Algeria to oversee banking liquidity have been established in line with those of conventional banks. Consequently, banks are able to manage their liquidity with ease. However, for Islamic banks, liquidity issues are of particular concern in cinventional banking. This issue is particularly evident in Algeria, where the Bank of Algeria does not fully consider the unique characteristics of Islamic banks. This is despite the recent amendment to Monetary and Banking Law No. 23-09, which formally recognized Islamic banking in Article 71. These banks are unable to borrow from the Central Bank as a lender of last resort, and they cannot borrow from other banks due to interest rates. The prohibition of

interest, whether as a lender or a borrower, is one of their core principles. In light of the above, the following question arises:

What challenges do Islamic banks face in their relationship with the Central Bank regarding liquidity management? To what extent are they effective in managing these risks, particularly in the case of Al Baraka Bank Algeria?

Research Objectives: Through this paper, the study aims to:

-Clarify the relationship between the Bank of Algeria and Islamic banks in terms of liquidity management;

-Clarify the liquidity risks facing Islamic banks;

-Provide an overview of methods for assessing and quantifying liquidity levels at banks;

-Identify the strategies and mechanisms adopted to address liquidity risks in Islamic banks;

-To assess the extent of Al Baraka Bank Algeria's compliance with national and international regulatory standards.

Significance of the Research : The topic of liquidity and its management is a strategic issue and one of the greatest challenges facing Islamic banks operating within an unified legal framework. Effective liquidity risk management ensures the survival, growth, and development of these banks. The recent global financial crisis offers a prime example of this, underscoring the critical importance of effective risk management for the development of strategies and standards to address various risks, including liquidity risks.

I.1. The Relationship Between Central Banks and Islamic Banks

The relationship between central banks and Islamic banks poses a challenge for some countries operating within an unified legal framework. The root of the problem lies in the incompatibility of the laws governing these banks with the operational mechanisms of Islamic banks. As these regulatory, supervisory, and oversight laws were drafted, their controls and standards were derived from the specific nature of conventional banks. However, the unique characteristics and operational mechanisms of these banks were not taken into account.

The Central Bank is linked to Islamic banks through three aspects :

- A regulatory relationship;
- A guidance and supervision relationship ;
- A relationship of support for Islamic banks.

Perhaps the most significant outstanding issues between the Bank of Algeria and Islamic banks, to name a few, include:

1. Central banks employ the same liquidity ratio for Islamic banks as they do for conventional banks, without considering any of their unique characteristics.

2. Islamic banks are subject to the same required reserves as their conventional counterparts. The legal reserve issue for them, and for Al-Baraka Bank in particular, lies in: (Suleiman, 2006, p. 280)

-The required reserve ratio is calculated based on the total deposits held by the bank, with demand deposits guaranteed by the bank excluded. Demand deposits account for approximately 20% of deposits; most other deposits are received by the bank on a speculative basis, i.e., under a profit- and loss-sharing system; consequently, the bank guarantees them only in the case of a loss.

- Al-Baraka Bank, like other banks, receives interest on funds deposited as required reserves with the Central Bank (Bank of Algeria). However, as an Islamic bank, Al-Baraka Bank does not deal in interest.

3. The difficulty of obtaining financing from central banks when necessary, due to the absence of a backup option for borrowing, is a matter of concern. Since the Bank of Algeria has not taken into account the specific nature of Islamic banks. Consequently, Islamic banks are obliged to maintain higher liquidity reserves than their conventional counterparts, which results in a loss of potential investment and trading opportunities and their associated returns. (Al-Shuwayat, 2015, p. 20)

4. Islamic banks' inability to benefit from the rediscount mechanism.

5. Central banks' open market operations conflict with the nature of Islamic banking.

6. The reserve requirement ratio is applied to Islamic banks just as it is applied to conventional banks.

7. Central banks rely on interest rates when imposing penalties and financial fines, such as reduction in the required reserve ratio .

The nature of the relationship between the Bank of Algeria and Islamic banks Despite the recent amendments to the Monetary and Banking Law through Law No. 23-09 of 2023, which formally recognized Islamic banking in Article 71, and subsequent Regulations 20-02 dated March 15, 2020, which outlined banking operations related to Islamic banking, the relationship between the Bank of Algeria and Islamic banks remains unchanged. This includes the Instruction 20-03 dated April 2, 2020, which defined the products related to Islamic banking. Despite their unique nature and the absence of the tools and mechanisms to manage liquidity that are characteristic of conventional banks, these banks continue to be treated as conventional banks.

I. 2. A Study of Liquidity in Islamic Banks

I. 2. 1- The Concept of Liquidity:

- It refers to the availability of sufficient cash and its equivalents to meet the institution's obligations and development requirements. Accordingly, the definition encompasses physical cash, bank deposits, and government deposits. (Daghi, 2017, p. 5). Therefore, liquidity can be defined as the institution's capacity to convert its assets into cash through two dimensions: (Bouraqba, 2011, p. 02)

- The initial dimension, is the duration required to convert an asset into cash; the shorter this time, the greater the asset's liquidity.

-The second dimension, is the degree of certainty associated with the conversion process, i.e., the degree of certainty regarding the price at which the asset will be converted into cash without resulting in a significant loss for the institution.

- The International Monetary Fund defines it as: "the extent to which financial assets can be sold at or near market notice with short notice is a key consideration."; (Monetary International, 2016).

- Definition of banking liquidity, this term refers to the extent to which a bank can meet its obligations and finance increases in assets without having to liquidate assets at unfair prices or resort to high-cost sources of funds. (Dweik, 2010, p. 05);

The term "banking liquidity" as used in the context of Islamic banking refers to the ability to meet current obligations in a manner that ensures the smooth operation of activities without problems or obstacles, as well as the prudent investment of available assets to achieve the maximum possible return in light of the provisions and principles of Islamic Sharia (Shehata, 2010, p. 14).

- The Basel Committee defines it as: "the ability to finance increases in assets and meet obligations as they fall due without incurring unacceptable losses." (Jedidia, 2013, p. 74)

I. 2. 2-The Importance of Liquidity in Islamic Banks: Cash liquidity in Islamic banks is of paramount importance for the following reasons:

- Liquidity is the most critical method of safeguarding banks against the risk of bankruptcy and ensuring their capacity to fulfill immediate payment obligations.
- It prevents Islamic banks from seeking out high-cost funding sources;
- The Islamic bank must maintain its reputation for having an excessive cash surplus. This excess suggests that the bank lacks investment programs and is freezing funds. However, a cash deficit could expose the bank to problems, leading to a loss of confidence and causing depositors and investors to rush to withdraw their funds. (Shehata, 2010, p. 15)
- Liquidity is widely recognized as one of the paramount indicators that customers consider when evaluating banks and making selection decisions (Bouraqba, 2011, p. 3). This is also regarded as a positive indicator by financial markets and international rating agencies, which can raise the bank's credit rating if managed effectively.
- Islamic banks are unable to offset a decline in cash liquidity through conventional riba-based banks. Similarly, they are not permitted to invest excess capital in such banks to avoid interest, as this is prohibited under Sharia law. (Al-Shuwayat, 2015, p. 5)
- Islamic banks lack a clear regulatory framework, as most central banks do not take their specific nature into account and treat them the same as conventional riba-based banks.

As illustrated above, the cash liquidity problem in Islamic banks differs from its conventional riba-based bank counterpart in both nature and severity. Therefore, it is essential to develop effective strategies to manage it. (Suleiman, 2006)

I. 2. 3-Liquidity Components and Risks in Islamic Banks : After defining and explaining the importance and implications of banking liquidity, we will examine the components of liquidity in Islamic banks and the factors influencing them.

A. Components of liquidity in Islamic banks: Liquidity in Islamic banks consists of two components:

- **Cash liquidity:** This consists of:
- Cash Holding in Islamic bank: This refers to the total cash available at the Islamic bank, i.e., the cash in the bank's vault, whether in local or foreign currency;

- Checks in collection: This is the total of checks submitted by the bank's customers for collection and deposit into their accounts at the Islamic bank;
- Amounts due to domestic banks and foreign correspondent banks: These are current accounts, which refer to the total deposits held with local banks, whether conventional or Islamic. They also refer to balances held with correspondents banks abroad;
- Cash reserves and credit balances due to the Central Bank: The cash reserves consist of two components: those imposed and determined by the Central Bank, representing a percentage of total deposits, and current accounts opened by Islamic banks with the Central Bank. (Jaafar (Han, 2012, p. 65).

- **Near-cash liquidity:** These are securities representing short-term assets that can be liquidated, sold, or pledged (Bouraqba, 2011, p. 3)and consist of:
- Shares of government and non-government companies;
- Mudaraba or Musharakah Certificates: (Han, 2012, pp. 66–67).Such certificates are issued by Islamic banks, and their holders generate profits. These financial instruments can be traded and sold to individuals and other financial institutions. In times of liquidity needs, the buyer takes the place of the certificate holder;
- Islamic sukuk: This documentation represents equivalent value, which is used to track ownership of tangible assets, benefits, or services, or specific project assets or private investment activities.

B. Factors Affecting Bank Liquidity: The liquidity position of Islamic banks is impacted by various factors, including: (Han, 2012, p. 66)

- Maturity: The shorter maturity tend to have higher liquidity ratings;
- The capacity to offer the asset in the financial market, particularly in secondary markets;
- The bank's strong financial standing instills confidence in its customers, motivating them to maintain their balances within the bank;
- It is essential to maintain a balanced equilibrium between withdrawal and deposit activity;
- The diversity of deposits at the Islamic bank decreases the likelihood of a simultaneous withdrawal.

C. Liquidity Risks for Islamic Banks and Financial Institutions: The term refers to the risk associated with discrepancies in the timing of cash flows between incoming and outgoing cash for the bank's operational needs and debt obligations. Liquidity risk has a significant impact on banks' performance, including their profits and capital. (Heramza, 2023–2024, p. 77)

A bank's inability to meet its financial obligations when they become due, as well as its short-term obligations, is also defined as a deficit. If a bank's deficit persists, it can lead to bankruptcy. (Qandouz & Baradiya, 2014, p. 16), Liquidity risk has two dimensions:

- **The first dimension involves liquidity funding risk:** This arises from the difficulty of obtaining liquidity at a reasonable cost.
- **The second dimension involves asset sale (liquidation) risk:** This is due to the inability to sell the institution's or bank's assets to obtain liquidity.

In the corporate finance realm, liquidity risks have been methodically categorized into two distinct categories: funding risks and market liquidity risks. Funding liquidity risk, as defined, pertains to the potential inability of Islamic financial institutions to manage cash flows, both anticipated and unanticipated, without compromising their financial operations or financial position. The liquidity risk faced by Islamic financial institutions comes in the form of their inability to enter or exit open financial positions in the market with ease. This is due to insufficient market depth or market disruptions. (Board, p. 10)

II– Methods and Materials:

II. 1. Bank Liquidity Measurerment Indicators :

A bank's liquidity ratio is calculated by dividing the number of loans by the total deposits. This ratio indicates how much the bank allocates its deposits to meet customer requests for loans. Generally, a higher ratio indicates greater efficiency. Various ratios are utilized in this process, the most significant of which are:

There are several methods for measuring liquidity risk adopted by Al Baraka Bank Algeria, including:

II. 1. 1- Liquidity Gap Analysis: The liquidity gap is the difference between cash inflows and cash outflows for the same period. The Liquidity Risk Department is responsible for preparing forecasts for the coming week, month, year, and up to the next five years by projecting cash inflows and outflows.

II. 1. 2- Liquidity Ratios Analysis

A. Liquid Assets to Total Assets Ratio:

The ratio is calculated by dividing the bank's liquid assets (cash and near- cash equivalents) by total assets. This ratio is essential for determining the relative importance of liquid assets to total assets. By calculating this ratio, we can identify the bank's liquidity position in relation to its other uses on an ongoing basis. It is calculated using the following formula :

Liquid Assets to Total Assets Ratio = Total Liquid Assets (Cash andNear- Cash Sssets) / Total Assets

B. Calculating the ratio of liquid assets to total deposits :

This is calculated by dividing the bank's liquid assets (cash and near cash equivalents) by total deposits. This ratio indicates the bank's capacity to repurchase its deposits at short notice and is calculated as follows :

Liquid Assets to Total Deposits Ratio = Total Liquid Assets (Cash and Cash Assets) / Total Deposits

II. 1. 3- Liquidity Ratios Analysis (Using Financial Ratios) : Here we present the financial ratios adopted by the bank, which are :

A. Required Reserve Ratio: According to Circular No. 02-2023 dated April 13, 2023, amending and supplementing Circular No. 02-2004 dated March 13, 2014, Islamic banks maintain a reserve with the Central Bank that typically constitutes a certain percentage of the total deposits held by the Islamic bank, regarding the required reserve system, set the

required reserve ratio at 3% effective as of April 15, 2023 (Article 2). It is calculated using

Required Reserve Ratio = Balance with the Central Bank / Total deposits + Other liabilities

the following formula :

As approved by Required reserve ratio the Monetary Policy Committee in accordance with economic conditions, it has undergone numerous adjustments since then. We can summarize the rate for the period from 2018 through the end of 2023. (See Appendix)

B. Cash Ratio : This enables the bank to assess its liquidity, which is affected by withdrawal and deposit transactions. The liquidity balance is calculated as follows :

Cash ratio = Balance with the Central Bank + Vault Cash / Total deposits

C. Liquidity Ratio: It is also referred to as relative solvency ratio, which calculated by dividing current assets by short-term liabilities. This ratio indicates the presence of net working capital, i.e., the safety margin.

This ratio is submitted to the Central Bank monthly in accordance with Circular 07/2011 using the following forms: MOD5000., 5001, 5002, 5003, 5004, 5005, 5006.It must be greater than one and is calculated using the following formula :

Liquidity Ratio = Current Assets / Short-Term Liabilities

D. Permanent Funding Ratio: This ratio indicates the extent to which permanent funds cover the bank's fixed assets, and it must be greater than one (1). Pursuant to Circular 07/2011, this ratio is to be submitted to the Central Bank using forms MOD4000, 4001, and 4002.

Permanent Funding Ratio = Permanent funds / Fixed assets

II. 1. 4-Measuring bank liquidity based on the Basel III Accords:

A. Liquidity Ratios (Quantitative Standards): Measures related to the management of liquidity risk have been implemented in response to the instructions of the Central Bank and in accordance with the provisions approved by international regulatory bodies through Basel III. Algeria adopted two key regulations in 2011: Regulation 11/04, dated May 24, 2011, which defines, measures, manages, and monitors liquidity risk, and Circular 07/11, which covers liquidity ratios such as cash reserves, cash balances, general liquidity, and permanent funding. The LCR and NSFR ratios are used to address short- and medium-term liquidity risks. They are not distinguished between Islamic and conventional banks.

While it did not consider the unique characteristics of Islamic banks, which experience a lack of Sharia-compliant instruments in the short term, it applied these two ratios:

- **Liquidity Coverage Ratio (LCR) :** The Basel Committee (Basel III) has proposed the implementation of this ratio, which reflects a bank's capacity to fulfill short-term obligations by utilizing its available cash within 30 days. The monthly calculation of this ratio, initiated in January 2015, is mandatory, with a minimum requirement of 100%. At Al Baraka Bank Algeria, its implementation began in January 2012 (Bettayeb, 2017–2018, p. 69)

Liquidity Coverage Ratio (LCR) = High-quality liquid assets / Net cash outflows over 30 days

- **Net Stable Funding Ratio (NSFR):** This ratio aims to achieve the highest levels of long-term funding liquidity (one year) and measures the value of long-term funding sources available to the bank compared to asset investments and the likelihood of funding demands resulting from off-balance-sheet commitments, provided that it exceeds 100%. The calculation is as follows:

Net Stable Funding Ratio (NSFR) = Required Stable Funding / Available Stable Funding

With regard to short-term liquidity, the Liquidity Coverage Ratio (LCR) has consistently exceeded the required threshold of 100%. Regarding long-term liquidity, the Net Fixed Funding Ratio (NFFR) experienced a slight decline in the first quarter of 2016. (Bank Al Baraka, 2016, p. 20)

B. Qualitative Standards for Basel III: The qualitative criteria involved conducting stress tests for internal liquidity. These tests involved developing scenarios or contingency plans that anticipate a liquidity crisis over various time horizons short, medium, and long term, up to five years. These scenarios include (Bettayeb, 2017–2018, p. 38):

1. Withdrawal of the ten largest deposits;
2- An increase in liabilities due within 30 days while liquid assets remain stable;
3- Scenarios (conversion of signature obligations into fund financing)

In 2016, Al Baraka Bank conducted two stress tests. The first was based on financial information as of March 30, 2016, while the second was based on information available as of September 30, 2016. All test results were satisfactory. (Bank Al Baraka, 2016, p. 2)

II. 2. Strategies for Managing Liquidity Risk and Their Management Challenges in Islamic Banks

Every month, the Liquidity Risk Department prepares a report (Synthèse analysis) on liquidity risk management. This report measures the liquidity gap and all the liquidity ratios and indicators discussed earlier. These include cash reserve ratios, cash balances, general liquidity, cash, and permanent funding. The review covers LCR and NSFR ratios, in addition to stress testing, and the results are reported to the Board of Directors according to Islamic Financial Services Board Standard 12 on liquidity risk management.

This Liquidity Risk Management Summary is submitted to the Board of Directors monthly for review.

Among the concentration limits adopted by Al Baraka Bank Algeria is that the customer concentration ratio must not exceed 2% (Bettayeb, 2017–2018, p. 38).

Furthermore, the bank's analysis of current deposits over the past 10 years revealed that 50% of these deposits are stable within the bank. Consequently, the bank can allocate 50% of these deposits to its financing activities and operations (Bettayeb, 2017–2018, p. 38)

- **Liquidity buffer:** This term refers to a designated sum of cash that a bank sets aside in anticipation of potential emergency scenarios or liquidity shortfalls.

Islamic banks are facing challenges due to excess liquidity, which is a result of a lack of sufficient outlets for obtaining cash. To mitigate the risk of sudden withdrawal requests, these banks are adopting a conservative approach to liquidity management. This involves maintaining a portion of their financial resources in the form of cash or bank deposits that exceeds the liquidity ratios established by monetary authorities. This is in contrast to the practices of conventional banks, which invest these funds in order to generate returns for depositors and maintain financial stability. (Qandouz & Baradiya, 2014, p. 10)

Islamic banks' reliance on maintaining substantial liquidity will inevitably influence the returns they offer to their customers, which encourage them to seek institutions that provide more favorable returns.

- **Liquidity Management Issues in Islamic Banks:**The most significant challenges confronting Islamic banks in liquidity management can be outlined as follows: (Dweik, 2010, p. 18)), (See Appendix)

III- Results and discussion:

III. 1. Requirements for Effective Liquidity Management in Islamic Banks:

There are several requirements that contribute to the efficient and effective management of liquidity in Islamic banks, including :

III. 1. 1- Cash Flow Planning in Islamic Banks: Cash flows must be analyzed, classified, and reconciled so that the bank can provide a certain level of liquidity to meet the following needs: (Berradiah Hakim, 2010–2011, p. 42)

- Regular and current demands from current account holders;
- Regular and sudden requests from savings account holders;
- Regular and sudden requests from investment deposit holders if the deposits can be withdrawn before maturity;
- The bank’s regular expenses;
- Various financing requests for participation, murabaha, and mudaraba;
- Seizing investment opportunities available to the bank.

III. 1. 2- Applying the maturity matching principle as an approach to liquidity management: Banks have to allocate internal resources to designated uses based on their maturities in specific proportions. Where, some banks pool and mix all their resources together in a single pool. The distribution of these assets is conducted without regard for their maturity dates and terms, which is not an appropriate method for managing available resources. This approach may expose the bank to the risk of bankruptcy. Therefore, they must be allocated as follows: (Rice, 2009, p. 271)

- These deposits are allocated to cash balances, bank balances, and short-term financing instruments such as murabaha;

- Investment deposits: a portion of these is allocated to cash and short-term financing, as well as long-term financing such as profit-sharing and murabaha;
- Savings deposits are allocated to cash, bank balances, short-term financing, and long-term investments;
- Funds owned by the bank are allocated to the bank's fixed assets and long-term investments.

III. 1. 3- Compliance with international standards and recommendations:

The bank strives to comply with the standards and recommendations of international bodies through:

- Adherence to the guidelines on liquidity management contained in Standard 12 is required. Standard 12 was issued by the Islamic Services Council in Kuala Lumpur, Malaysia, in March 2012 (Islamic Services Council, No date)
- adherence to the standards approved by the Basel Committee Ⅲ regarding liquidity standards is mandatory, despite their focus on conventional banks:

III. 2. Proposed solutions to prevent liquidity risk:

Islamic banks are seeking solutions to address issues related to liquidity shortages or excesses .

III. 2. 1- In the case of excess liquidity: Most field economic studies have confirmed that the majority of Islamic banks suffer from a problem of excess cash liquidity, and researchers in this field have addressed it through study and analysis due to its direct negative impact on their performance and profitability. The axcess liquidity in conventional banks is not considered problematic because it can easily be invested in other banks for any duration and at any time in exchange for riba-based interest. However, Islamic banks cannot engage in such transactions due to their unique operational principles. Islamic banks have adopted certain solutions to address this problem, including:

- **Relying on short-term investments, particularly the Murabaha or International commodity Murabaha:** Many Islamic banks allocate their excess capital to short-term investments, predominantly through murabaha and international murabaha arrangements. However, this strategy leads to substantial imbalances in their financing activities and undermines their intended developmental role. (Suleiman Nasser, 2002, p. 325)
- **Using excess liquidity in the formation of Investment Portfolios:** Some projects require significant financial resources that banks may not be able to provide independently. Investment portfolios are created to address this need, allowing banks to allocate funds for long-term financing. This strategy resolves the challenge of short-term financing that is common for Islamic banks.
- **Investing excess liquidity in Islamic Sukuk:** Investing financial excess in government or non-government Islamic sukuk is an option that should be incorporated into Islamic banks' liquidity management strategies, as it would enable the deployment of excess liquidity into short- or medium-term investment channels via sukuk. The absence of Islamic secondary markets limits these banks' ability to deploy their excess liquidity through the issuance of sukuk traded on the secondary market. Many countries currently lack legislation to regulate the issuance and trading of sukuk. (Jordan, 2015)
- **Speculation in Stock Exchanges and Financial Markets:**In modern economics, the term "speculation" has a different connotation than in Islamic jurisprudence and economics. Speculation in economics refers to the practice of purchasing a commodity with the intention of reselling it

when its price rises to profit from the resulting rise in price. Some Islamic banks utilize their surplus funds in the global stock exchange and financial markets to speculate in stocks, bonds, currencies, and precious metals. This method is permissible under Islamic law provided that the Sharia standards issued by the fiqh councils are adhered to (Shehata, 2010, p. 23)

- **Depositing excess liquidity with conventional riba-based banks without interest and on a reciprocal conditions :** Some Islamic banks deposit excess cash reserves with conventional riba-based banks for a limited period without interest, provided that the conventional bank lends the Islamic bank an equivalent amount for the same duration, also without interest. These practices, however, are subject to significant criticism. The most important of these criticisms is that conventional banks have led many Muslims to refuse to deal with Islamic banks by spreading the notion that Islamic banks invest their funds in conventional banks (Shehata, 2010, p. 22) Some individuals also choose to deposit their excess funds in local or international conventional banks to access banking services. However, this practice is subject to significant legal challenges. (Shehata, 2010, p. 22)
- **Investing excess liquidity in investment funds:**This strategy entails allocating surplus liquidity into various investment funds to generate returns, including Money Market Funds for short-term liquidity, Sukuk Funds for stable yields, Commodity Murabaha Funds for Sharia-compliant trading, and Sovereign Wealth Funds for capital preservation. Its objective is to optimize returns on idle capital while maintaining adequate liquidity levels for future operational requirements

III. 2. 2- In the case of a liquidity shortfall : If an Islamic bank faces a shortage or deficit in liquidity, it employs the following mechanisms:

- **Securitization (Sukuk Issuance):** Securitization is the process of converting investment financial instruments into securities that are easily traded—bought and sold—in the securities market. Islamic jurists have conventionally termed securitization operations within the Islamic framework as "tassekik" operations; which consist of the following steps:

- In conventional finance, assets are typically loans or other receivables. In Islamic finance, assets consist of those eligible for securitization in accordance with the provisions and principles of Islamic Sharia, such as assets subject to ijara ;
- In order to transfer ownership of the assets to a special-purpose entity that is serving as the issuer, they must first be structured as securities (i.e., Sukuk);
- Issuing the securities (sukuk) to investors.

- **Asset Securitization:**In situations where a liquidity shortfall occurs, an Islamic bank may sell (liquidate) a portion of its assets to obtain liquidity and cover the shortfall. That way, the bank can avoid collapse and bankruptcy**.**
- **Implementation of an emergency plan:** Islamic banks implement emergency plans to address liquidity shortfalls or shortages. These plans are based on strategies developed for any emergency scenario.
- **Interbank financing among Islamic banks:**The Islamic bank provides coverage for deficits through cash exchange agreements and contracts with other Islamic banking partners.

III-Conclusion:

- Despite the amendment of the Monetary and Banking Law through Law No. 23-09 of 2023, the Bank of Algeria and Islamic banks still have an unsatisfactory relationship. This amendment formally recognized Islamic banking in Article 71 and Regulation 20-02, which governs banking operations related to Islamic banking. While Islamic banks possess distinct characteristics and are not equipped with the same liquidity management tools and mechanisms as their conventional counterparts, the regulatory framework continues to impose liquidity and legal reserve requirements.
- Al-Baraka Bank, like many other Islamic banks, faces challenges due to significant financial excess. The bank is currently seeking to implement new mechanisms to effectively utilize these excess funds.
- Islamic financial and monetary instruments such as Islamic sukuk, investment certificates of deposit, and Islamic mudaraba bonds are not currently available to Algerian Al-Baraka Bank, which limits its ability to leverage its cash excess.
- Al Baraka Bank Algeria is committed to applying the standards set by the Central Bank, as well as the Basel III liquidity standards in both their quantitative and qualitative aspects. The bank adheres to quantitative standards through the LCR and NSFR ratios, as well as qualitative standards through stress testing and the adoption of a liquidity risk management strategy overseen by both the Risk Department and the bank's Board of Directors.
- When confronted with liquidity shortfalls, Al Baraka Bank Algeria has a contingency plan that it implements.

Recommendations: Based on these findings, we offer the following recommendations :

- The Central Bank's legal and regulatory frameworks for liquidity management in Islamic banks should be amended to take into account their specific characteristics and comply with the quantitative standards of international bodies and the Islamic Financial Services Board;
- The objective is to propose a collaborative plan for Islamic banks to address the liquidity issue by establishing joint investment funds.
- The Algerian Central Bank working to establish the necessary legal framework that will allow Islamic banks to use Islamic financial instruments, including: Islamic sukuk, Islamic mudaraba bonds, and other financial instruments are also used.

Our thorough examination of the research issues has revealed that the subject has multiple aspects and other angles that still require study and scrutiny.

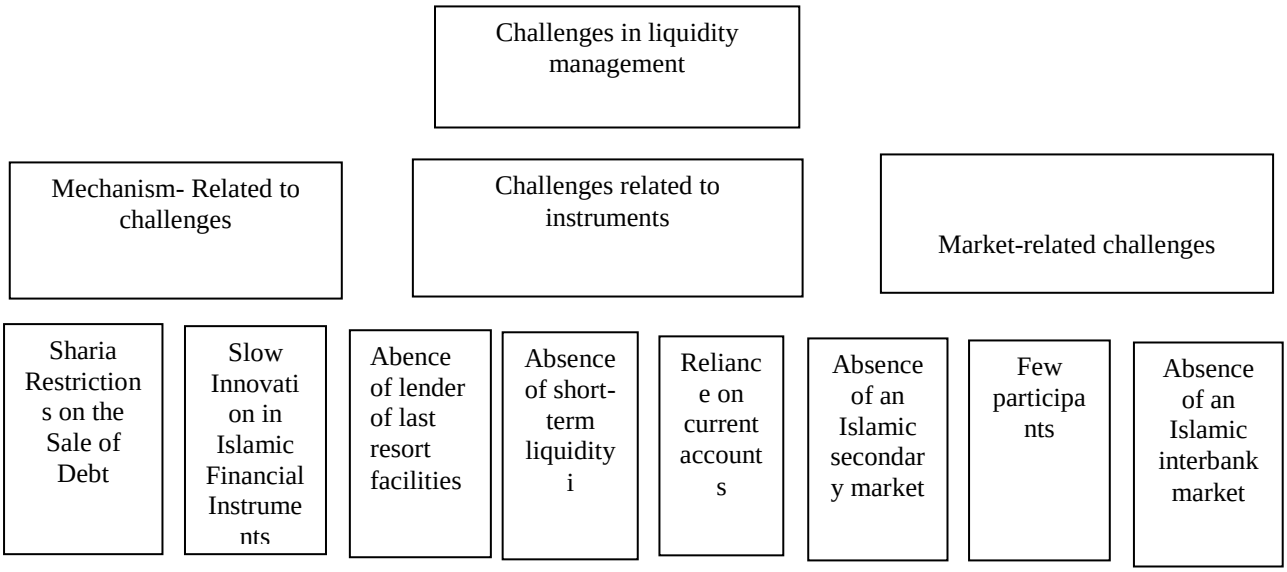
Appendices:

Table1: Required Reserve Ratio for the Period (2018–2023)

Year	2018	2019	2019	2020	2020	2020	2021	2023
Reserve ratio	8%	12%	10%	8%	6%	3%	2%	3%
Effective Date	01/15/2018	02/15/2019	12/15/2019	03/15/2020	May15, 2020	09/15/2020	02/15/2021	04/15/2023

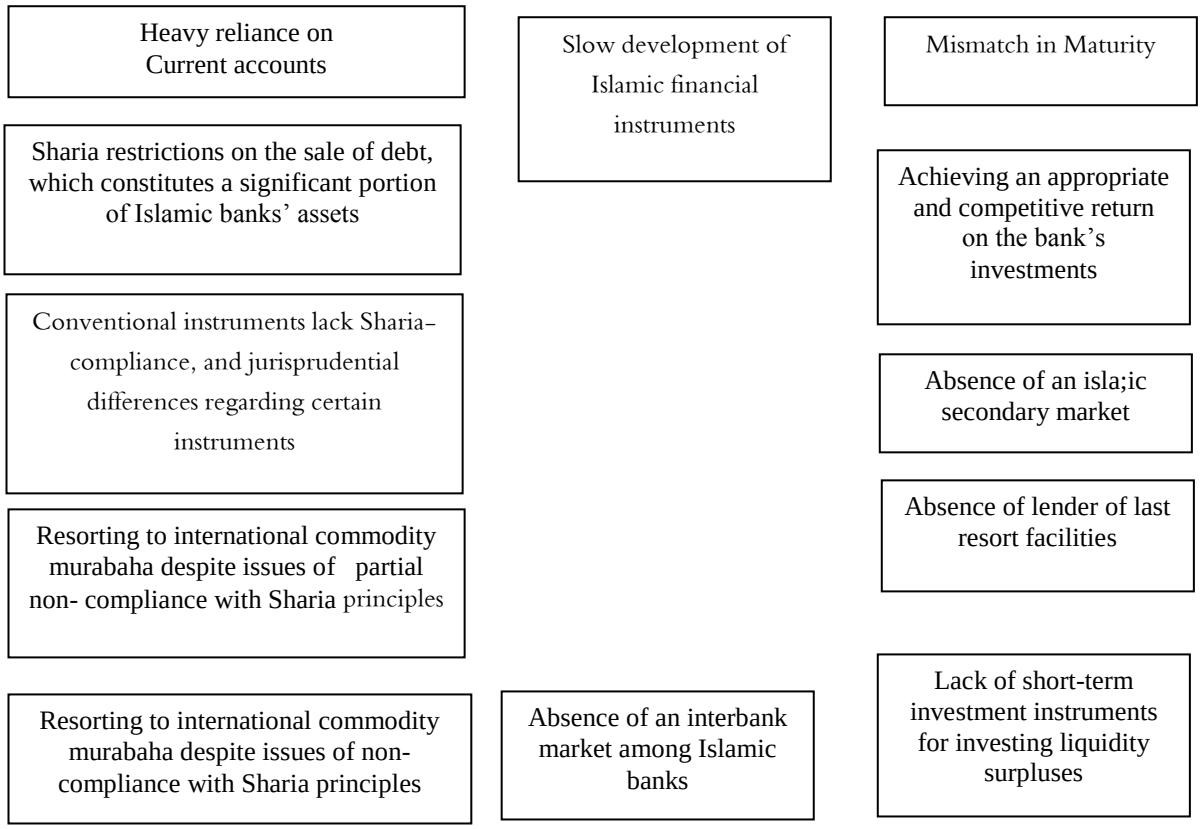
Source : Prepared by the researchers without relying on data from the Bank of Algeria

Figure1:Key Challenges in Liquidity Management at Islamic Bank



Source: Abdulkarim Qandouz, Arab Monetary Fund, Issue 121/2023, 2017, p. 11

Figure 2: Liquidity Risk Management Issues in Islamic Banks



Source: Abdelkader Dweik, Liquidity Management in Islamic Banks, Fifth Conference of Islamic Banks and Financial Institutions in Syria, Damascus, 2010, p.

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