MOROCCO

Highlights

- **Growth is recovering after a sluggish performance in 2014.** Agricultural output has rebounded and non-agricultural output is picking up in 2015. As a result, unemployment has fallen in the first half of this year.
- **Morocco's external position has improved significantly, in part thanks to industrial policy efforts.** Low global oil prices and strong export performance – notably including in the high value-added, newly developed sectors such as automobile – have helped the current account deficit narrow sharply. This has helped boost reserves to over six months of imports as of mid-2015.
- **Progress has been made in strengthening financial sector supervision**. The central bank's role has been expanded to enable it to impose prudential measures for systemically important banks and provide it with special resolution mechanisms to resolve banking crises. Cross-border cooperation with supervisory authorities in countries in which Moroccan banks have expanded has also improved.

Key priorities for 2016

- **Reform in the infrastructure sector is urgently needed, especially at the municipal level.** The challenge is to build municipal capacity to manage, run and efficiently operate large infrastructure projects including transparent participation of the private sector through public-private partnerships (PPPs). This can support the planned decentralisation/regionalisation.
- **More needs to be done to improve efficiency in the agricultural sector.** Poverty remains pocketed in rural areas which are heavily dependent on weather conditions, with limited risk hedging and management tools. Challenges include developing a competitive processing industry and enabling firms to move up the value chain.
- **Improving access to finance for small and medium-sized enterprises (SMEs) remains a key priority.** The establishment of a moveable asset collateral registry and increasing flexibility in using moveable assets as collateral would help boost SME lending, as these companies typically have insufficient collateral.

Main macroeconomic indicators %

	2011	2012	2013	2014	2015 proj.
GDP growth	5.2	3.0	4.7	2.4	4.9
Inflation (average)	0.9	1.3	1.9	0.5	1.7
Government balance/GDP	-6.6	-7.3	-5.2	-4.9	-4.3
Current account balance/GDP	-7.9	-9.5	-7.9	-5.5	-2.3
Net FDI/GDP [neg. sign = inflows]	-3.2	-3.8	-4.3	-3.9	-3.8
External debt/GDP	30.9	33.8	36.0	43.0	n.a.
Gross reserves/GDP	21.5	17.4	17.4	20.0	n.a.
Credit to private sector/GDP	72.0	73.4	70.2	70.6	n.a.

CONTINUES

Macroeconomic performance

The economy is recovering after a sluggish performance in 2014. Growth accelerated to 4.2 per cent year-on-year in the first half of 2015, after sluggish growth of 2.4 per cent in 2014. Following a contraction last year, agricultural output is rebounding, aided by favourable weather conditions. The gradual recovery in other sectors such as manufacturing continues, although the tourism sector continues to struggle as a result of regional security problems. Improved growth has made a dent in unemployment, which fell to 8.7 per cent in the second quarter of 2015, after averaging 9.7 per cent last year. Meanwhile, inflation remains low at under 2.0 per cent so far this year.

The fiscal deficit continues to narrow thanks to fiscal consolidation measures. The deficit declined slightly to 4.9 per cent of GDP in 2014 and is expected to continue improving this year. The authorities' fiscal consolidation efforts have focused on energy subsidy reforms and gradual containment of the public wage bill. As a result of subsidy cuts and falling oil prices, spending on subsidies alone fell by over 20 per cent on 2014, allowing a reallocation of some public expenditure towards investment, which grew by 14 per cent in the same period. Morocco continues to enjoy access to international capital markets, with both the sovereign and state-owned enterprises successfully issuing bonds recently. Despite having risen since the global financial crisis, public debt stands at around 63 per cent of GDP.

The external position has improved significantly. The current account deficit narrowed from 7.9 per cent of GDP in 2013 to 5.5 per cent of GDP in 2014 and fell further to 1.9 per cent of GDP in the first quarter of this year. This has been the result of lower global commodity prices, which have resulted in falling food and oil imports, combined with strong export performance. Automobile exports continued to grow strongly in 2014 and into this year, while traditional phosphate exports have bounced back. These trends have more than offset struggling tourism receipts and, alongside sustained foreign direct investment (FDI) inflows and recent international bond issuances, have driven up reserves to nearly six months of imports as of July 2015.

Growth is expected to slow in 2016 as agricultural output normalises. Strong agricultural performance is expected to drive overall growth of 4.9 per cent in 2015. Growth is expected to slow to 3.8 per cent in 2016 as agricultural output normalises, with a modest pick-up in non-agricultural activity supported by low oil prices and a recovery in Europe. Worse-than-expected growth in Europe and domestic and regional security problems present downside risks to this forecast.

Major structural reform developments

While the business environment and investment climate are on a broadly positive path, key obstacles remain. Morocco has seen significant improvements in its business regulatory environment towards best practices as reflected in the World Bank's *Doing Business 2016 report*, with the country ranked 75th (out of 189 countries) compared with 128th in 2010. This is mainly driven by regulatory reforms related to the ease of starting a business, dealing with construction permits, trading across borders and paying taxes. The country lags behind, however, on access to credit, where Morocco ranks 109th (this relates particularly to restrictions on access to finance for SMEs such as the need to increase the flexibility of using moveable assets as collateral), and minority investor protection with a current ranking of 105th. Moreover, evidence from the EBRD/World Bank Business Environment and Enterprise Performance Survey (BEEPS V) reveals that intense informal sector competition, corruption and lack of workforce skills - specifically, the wide skills gap between university graduates and private sector needs - are the most severe business environment obstacles.

CONTINUES

A proposed public-private partnership law would be a positive development in the infrastructure sector. The draft law, which was issued in December 2014 and is currently subject to public consultation, creates a new category of contract for public-private partnerships. This complements the existing legal framework, under which private participation in infrastructure projects has been carried out under delegated management in the form of concessions. The law is expected to come into force soon, and the Ministry of Infrastructure, Transport and Logistics is currently carrying out studies on over 20 PPPs.

Morocco has taken steps to reduce fiscal vulnerabilities by committing to a programme of fiscal consolidation. Major progress was achieved in energy subsidy reforms, particularly given the difficult social and political context. Energy subsidies on liquid petroleum products were removed as of January 2015 (and will be liberalised fully by November 2015), while measures were taken to strengthen the social safety net. A major development was the adoption of the Organic Budget Law (OBL) in May 2015, which will be progressively implemented over the next five years. The OBL aims at enhancing the efficiency of the fiscal framework, increasing the transparency of public finances along with the involvement of parliament. The financial situation of the pension system remains fragile, and significant reforms are needed to ensure its sustainability. These include raising the retirement age, boosting contribution requirements and reducing final salary entitlements. Reform proposals have gone through a consultative process with trade unions, and the authorities plan to adopt the reforms in 2015 and implement them in 2016.

Efforts to boost industrial output are bearing fruit, and a new national industrial acceleration programme has been announced. The 2014-2020 industrial strategy, which was launched in April 2014, aims to increase the contribution of industrial sectors to GDP and job creation, and focus on the ongoing development of high-value added sectors such as automobiles, aviation, electronics and off-shoring. As part of this programme, a new public investment fund endowed with 2 billion euros will be set up, and tax incentives will be introduced to facilitate the integration of small informal enterprises into the formal sector. Morocco has already had considerable success in increasing its industrial output and diversifying its exports towards higher value-added goods over the past five years, supported by the expansion of industrial free zones in Tangier and Casablanca. In 2014, automobile exports outstripped phosphate exports to become the highest foreign exchange earner for the country for the first time.

Progress continues in strengthening financial supervision and regulation and deepening the financial sector. Basel III norms are being progressively integrated and a new banking law was adopted by parliament in November 2014. The law broadens the central bank, Bank Al-Maghrib's (BAM), regulatory and supervisory role. For instance, the BAM now has the ability to impose prudential measures on banks that are identified as systemic institutions, and special resolution mechanisms to resolve banking crises. A new central bank law is under revision and is expected to increase BAM's independence and expand its supervisory role. Given the rapid cross-border expansion of major Moroccan banks, into sub-Saharan Africa in particular, BAM also increased its cooperation with host countries' supervisory authorities. However, little progress has been made on cross-border banking resolution. A new Islamic finance law was finally adopted by parliament in November 2014 as part of the effort to boost the economy and attract more foreign investment - in particular from the Gulf - allowing the establishment of Islamic banks and authorising private companies to issue Islamic debt.

The process of decentralisation remains slow, given the complexity of reforms, but still in motion. Regionalisation has been slow to materialise since it was outlined in the new constitution of 2011. However, progress of note is the adoption of the Moroccan parliament in June 2015 of an organic law governing the operation of the regions and expanding the prerogatives of the local authorities.