

Morocco: 2001 Article IV Consultation—Staff Report; Public Information Notice; and Statement by the Executive Director for Morocco

Under the Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2001 Article IV consultation with Morocco, the following documents have been released and are included in this package:

- the Staff Report for the 2001 Article IV Consultation, prepared by a staff team of the IMF, following discussions that ended on **April 30, 2001**, with the officials of Morocco on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on June 20, 2001.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a Public Information Notice (PIN), summarizing the **views of the Executive Board as expressed during its July 11, 2001 discussion** of the staff report on issues related to the Article IV consultation.
- a statement by the Executive Director for Morocco.

The documents listed below have been or will be separately released.

Statistical Appendix

The policy of publication of staff reports and other documents by the IMF allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to Publicationpolicy@imf.org.

Copies of this report are available to the public from
International Monetary Fund • Publication Services
700 19th Street, N.W. • Washington, D.C. 20431
Telephone: (202) 623 7430 • Telefax: (202) 623 7201
E-mail: publications@imf.org • Internet: <http://www.imf.org>

Price: \$15.00 a copy

**International Monetary Fund
Washington, D.C.**

INTERNATIONAL MONETARY FUND

MOROCCO

Staff Report for the 2001 Article IV Consultation

Prepared by the Staff Representatives for the 2001 Consultation with Morocco

Approved by Paul Chabrier and Masood Ahmed

June 20, 2001

- Discussions for the 2001 Article IV were held in Rabat during March 28–April 12, 2001 and continued in Washington, D.C. during the Spring Meetings.
- The staff team included Messrs. Nashashibi (Head), Gardner, Fanizza, and Martin, as well as Ms. Bazzoni, Jaumotte, and Catany (assistant) (all MED).
- The mission met with Prime Minister Youssoufi, Minister Oualalou (economy, finance, privatization, and tourism), Governor Seqat (Bank Al-Maghrib), Minister El Fassi (social development, solidarity, and employment), Minister Aouad (economic projections and planning), Minister Lahlimi (social economy, in charge of the general affairs of the government), Minister Mansouri (industry and commerce), Minister Saaf (education), Minister Alaoui (agriculture), Minister Chbaâtou (fishing), Secretary of State Fihri (foreign affairs), and Messrs. Azoulay and Kabbaj (counselors to the King). Mr. Daïri, Alternate Executive Director for Morocco, participated in all the meetings. The staff also met with public officials from various ministries and with representatives of the business and banking community.
- At the conclusion of the last Article IV consultation on June 7, 2000, Executive Directors commended the authorities for maintaining macroeconomic stability through a period of recurrent droughts and changes in the political landscape but were concerned by the slowdown in growth observed during the 1990s, and the associated increases in poverty and unemployment. Directors supported the authorities medium-term plans to improve the growth outlook by accelerating structural reform and reducing the fiscal deficit to a more sustainable level. Some Directors believed that a more flexible exchange rate policy could play an important role in strengthening competitiveness and spurring faster growth. Other Directors took the view that the fixed exchange rate arrangement had served Morocco well and remained appropriate for preserving financial stability.
- Morocco has accepted the obligations of Article VIII, Sections 2, 3, and 4.
- Morocco has agreed to participate in a Financial Sector Assessment Program/Financial System Stability Assessment in January 2002. The authorities have agreed to publish the staff report.
- The principal authors of this report are Messrs. Nashashibi and Fanizza.

Contents		Page
Executive Summary		4
I. Background		6
A. Recent Economic Developments and Outlook for 2001		6
B. Policy Developments.....		11
II. Policy Discussions		15
A. Fiscal Policy		17
B. Monetary Policy		22
C. Exchange Rate Policy.....		24
III. The Challenges for the Medium Term.....		27
IV. Structural Policies		31
V. Statistical Issues		34
VI. Staff Appraisal		34
Text Boxes		
1. Privatization of the Telecommunication Sector		9
2. Public Finance Developments in the 1990s		13
3. Trade Liberalization.....		16
4. Some Indicators of Fiscal Stance.....		18
5. Sources of Growth		29
6. Developments in the Agricultural Sector.....		33
Figures		
1. Real GDP Growth, 1991–2001		7
2. Real Domestic Demand Growth, 1991–2001		7
3. Monetary Developments, 1997–2000.....		8
4. Consumer Prices, 1991–2001		10
5. External Balances, 1991–2001.....		10
6. Fiscal Developments, 1993–2000.....		12
7. Southern Mediterranean Arab Countries, Tax Revenue, 1999/2000.....		20
8. Exchange Rate Indicators, 1991–2001		25
9. Export Performance, 1990–2000		26
Tables		
1. Selected Economic and Financial Indicators, 1996–2001		38
2. Medium-Term Baseline Scenario, 1991–2006		39
3. Medium-Term Adjustment Scenario, 1991–2006		40
4. Public Finance, 1996–2001.....		41

5.	Monetary Survey, 1996–2001.....	42
6.	Balance of Payments, 1996–2001.....	43
7.	Balance of Payments, Medium-Term Baseline Projections, 2000–06	44
8.	Basic Social and Demographic Indicators, 1971–2000	45
9.	Indicators of External and Banking Sector Vulnerability, 1996–2000.....	46
 Appendices		
1.	Fund Relations	47
2.	Financial Relations with the World Bank Group.....	50
3.	Statistical Issues	53

EXECUTIVE SUMMARY

A recovery is underway, following the economic stagnation experienced during the last two years. A rebound of agricultural production is behind the recovery, whereas nonagricultural growth is expected to improve as a result of the strong performance of tourism, telecommunications, and construction. Productivity has increased over the last few years, spurred by structural reforms and increased investment. Nevertheless, the rise in productivity and a decline in the price of capital relative to labor have resulted in lower employment creation.

The successful sale of 35 percent of Maroc Telecom for US\$2.1 billion (6 percent of GDP) has boosted official reserves to comfortable levels. The open and transparent privatization process has signaled a substantial improvement in the country's economic and investment climate.

Structural reforms have proceeded on several fronts, including the liberalization of the telecommunications sector, the elimination of the price subsidies on edible oils, the implementation of rural infrastructure programs, actions to improve governance, and trade liberalization in the context of the free trade agreement with the European Union.

After a decade of fixing the nominal exchange rate against a currency basket, the authorities modified the basket to better reflect the growing importance of the euro area in Morocco's trade accompanied by a 5 percent depreciation of the dirham on April 25, 2001. In spite of a comfortable external position, further strengthened by privatization receipts, this devaluation was a response to the slow growth in exports, to the appreciation of the dirham vis-à-vis the euro and more generally to the significant real effective appreciation of the dirham during the 1990s.

Inflation has remained below 2 percent so far, but it is expected to increase to 3.0-3.5 percent by end-2001. The deficit of the external current account remains modest. Unemployment remains high and poverty continues to be widespread, but the authorities are launching a major effort to attain universal primary education by 2003 and to improve other social indicators.

Relying on the proceeds from privatization, fiscal policy has taken a pro-cyclical stance, resulting in a significant fiscal stimulus since 1999/2000. Monetary policy has taken an accommodating stance and has provided liquidity to maintain low interest rates and to encourage private investment. The expansionary financial policies cannot constitute a viable strategy for a sustained acceleration in growth over the medium term. Deepening structural reforms, together with actions to improve external competitiveness, are essential for enhancing Morocco's medium-term growth outlook.

While a number of significant one-off factors have contributed to the expansion in the fiscal deficit expected in 2001, corrective fiscal action needs to be taken as soon as possible. Recent policies have exacerbated rigidities in government spending while

increasing tax exemptions. A deficit reduction target for the 2002 budget in the range of 2–2.5 percent of GDP would provide a clear signal of government's commitment to fiscal consolidation.

The central bank, Bank Al-Maghrib, needs to closely monitor inflation developments to protect the credibility it has established by achieving price stability. If needed, interest rates should be allowed to move up to dampen inflationary pressures which might emerge from both the devaluation of the dirham and the fiscal stimulus.

The devaluation of the dirham constitutes a positive action, considering the competitiveness losses accumulated over the last decade. The staff expects it to be a first step toward a more flexible exchange rate policy that better fits Morocco's needs to respond to exogenous shocks, the challenges posed by trade liberalization, and the need to strengthen competitiveness.

Further progress in structural reform is needed to both attract foreign investment and to favor private sector development. The reform agenda should focus on the phasing-out of tariff protection for wheat and sugar producers, reforming the civil service toward improved service delivery and wage bill reduction, modernizing the judicial system, improving governance, and passing the new labor code.

The main policy challenge is to ensure a sustained increase in the growth rate to reduce unemployment and trigger a durable decline in poverty. An acceleration of structural reforms, a flexible exchange rate policy, and the return to fiscal consolidation would translate into an improved growth performance over the medium term. However, the authorities could reasonably aim at a more ambitious growth target of 6 percent per year to fully absorb new entrants to the labor force and trigger a sustained reduction in unemployment and poverty. To achieve this target, the authorities may want to explore a whole range of policies, including: a faster liberalization of imports; an active exchange rate policy, and a deepening of structural reforms to attract larger private and foreign investments.

I. BACKGROUND

1. **Morocco's political transition is progressing.** The current government, made up of a seven party coalition headed by the socialist party, took power after the first elections of the house of representatives by universal suffrage in September 1997. Since then, the government—headed by Mr. Abderrahmane El Youssoufi, a prominent socialist leader of the opposition before 1997—has attempted to foster political democratization and modernization with the support of the new monarch (Mohammed VI).¹ The gradual opening of the political system has translated into significant progress on human rights and an active political debate. In the context of the growing role of civil society, policies have begun to favor social participation and political decentralization. Government policies have placed increasing emphasis on improving governance and fighting corruption. Social issues, including poverty reduction, improved opportunities for women, and rural development have become prominent on the government's policy agenda.

2. **The next legislative elections will take place in 2002.** The congress of the socialist party has already opened the political debate. The congress has renewed support in favor of government policies, despite the defections of a large trade union and the socialist youth organization. Increased support for government policies would be necessary to accelerate the pace of structural reforms, which have been hindered by limited success in the government's attempts in building consensus on key issues.

3. **The government continues to face the challenge of improving Morocco's economic conditions and living standards** after a decade of disappointing growth. The relaxation of the political system has allowed pent-up social demands to emerge, increasing the urgency of higher economic growth and the reduction of urban unemployment and poverty.

A. Recent Economic Developments and Outlook for 2001

4. **The Moroccan economy is recovering from the stagnation experienced during 1999 and 2000.** After two years of severe droughts, better rainfall—although unevenly distributed—should lead to a 25 percent increase in agricultural output in 2001 with favorable spillovers on other sectors (Figure 1). Thus, real GDP growth is projected at 6 percent, up from 0.8 percent in 2000 and -0.7 percent in 1999. Nonagricultural output is expected to increase by 3.8 percent driven by construction activity, telecommunications, and tourism, which has benefited from the government's efforts to attract foreign investors and tour operators. Major projects in electronics, tourism, and motor vehicle components were launched with foreign direct investment (FDI) financing. On the demand side, the most dynamic components are government consumption and private investment (Figure 2).

¹ King Mohammed VI acceded to throne after the death of his father, Hassan II, in 1999.

Figure 1. Morocco: Real GDP Growth, 1991–2001

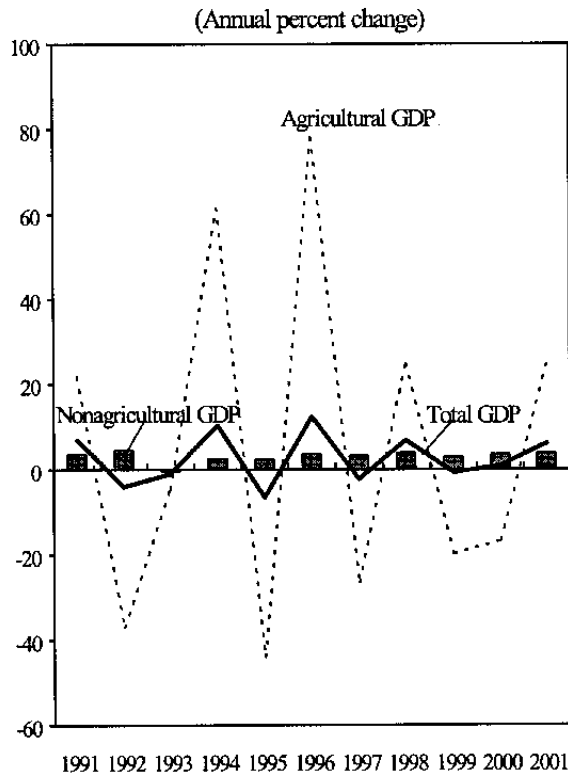
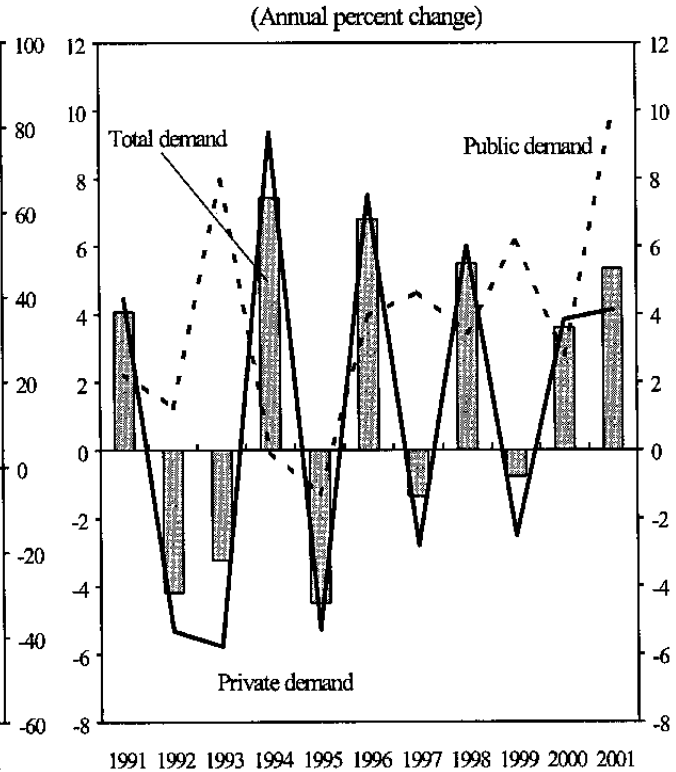


Figure 2. Morocco: Real Domestic Demand Growth, 1991–2001

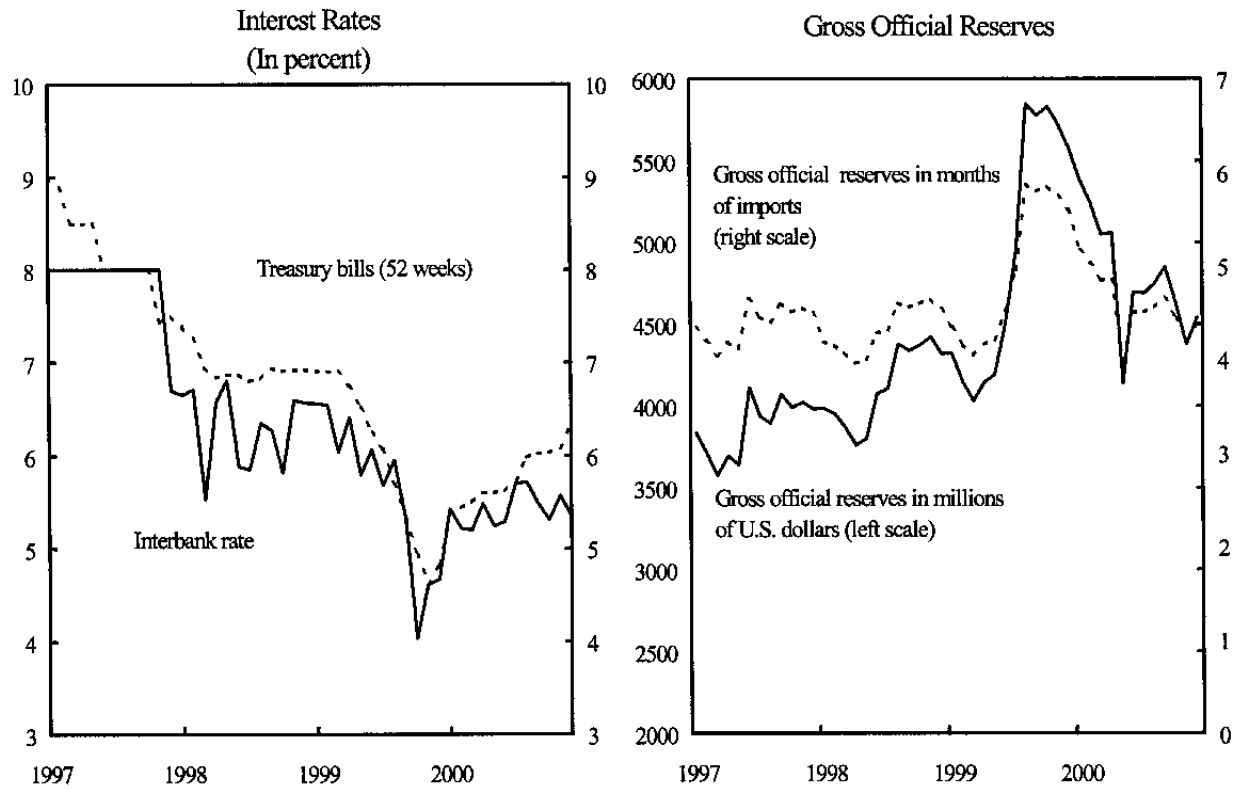


Sources: Moroccan authorities; and IMF staff estimates.

5. Economic prospects have brightened during the first quarter of 2001 with the privatization of 35 percent of Maroc Telecom for US\$2.1 billion (6 percent of GDP). This was achieved in an exemplary process of openness and transparency (Box 1); the price obtained substantially exceeded the authorities' and foreign analysts' expectations considering the severe downturn in the world telecommunication market. Sterilization of a large part of these proceeds, coupled with close coordination between Bank Al-Maghrib (BAM) and the treasury, ensured a smooth operation of the money market and avoided the sharp drop in interbank interest rates that took place when the second mobile telephone (GSM) license was sold in 1999 (Figure 3).² The treasury also exerted its presence in the bond market even when financing was not needed.

² In view of the proceeds from the second GSM license, the treasury was less active in borrowing from the domestic market. To absorb the resulting excess in liquidity BAM had to sell all its stock of government securities, introduce a deposit facility, and significantly tighten reserve requirements on commercial bank deposits in 1999 (see SM/00/92; 5/18/00). Instead, in 2001, the treasury repaid its outstanding debt with BAM and blocked part of the privatization proceeds earmarked for investment purposes in a special BAM account.

Figure 3. Morocco: Monetary Developments, 1997–2000



Sources: Moroccan authorities; and IMF staff estimates.

6. After a decade of fixing the nominal exchange rate against a currency basket, during which there was a significant appreciation of the real exchange rate, the authorities modified the basket to better reflect the growing importance of the euro area in Morocco's trade accompanied by a 5 percent depreciation of the dirham on April 25, 2001. Under the fixed exchange rate regime, a 22 percent appreciation of the real effective exchange rate during the last decade resulted in rising competitive pressures on the traded goods sector. In particular, over the last two years, the dirham appreciated in nominal terms vis-à-vis the euro, which accounts for more than two-thirds of Morocco's export transactions. The association of textile producers, which operate on very narrow margins, reported the loss of 29,600 jobs in the textile sector since 1999 (12.2 percent of employment in the sector). The trade balance also appears to have worsened during the first quarter of 2001. Partly in response to these pressures, the authorities decided on April 25, 2001, to readjust their currency basket by giving greater weight to the euro and to devalue the dirham by 5 percent.

Box 1. Morocco: Privatization of the Telecommunications Sector

The Moroccan government started privatizing the telecommunications sector in 1999 under conditions of great transparency.¹ An international tender awarded a mobile telecommunications license in August 1999, challenging the dominance of the state-owned telecommunications monopoly, Maroc Telecom. The winner of the mobile license, Medi Telecom, paid US\$1.1 billion (one of the highest prices ever paid for a mobile license relative to population size). This operation was followed by the sale of 35 percent of Maroc Telecom to Vivendi in December 2000 for US\$2.1 billion.

Allowing the private entrant to compete with the state monopoly was crucial for the success of the operation. In 1996, a telecommunications law allowed for competition in all the segments of the market and set up an independent regulatory agency. The terms of the mobile license created a competitive environment by allowing the new entrant to develop its own network and by leaving open the possibility of extending the range of services it can provide; this prompted the state monopoly to improve its services while it made the mobile license more attractive for potential buyers, increasing the bids not only in financial terms but also in terms of commitment to quality, coverage, and price of the offered services.

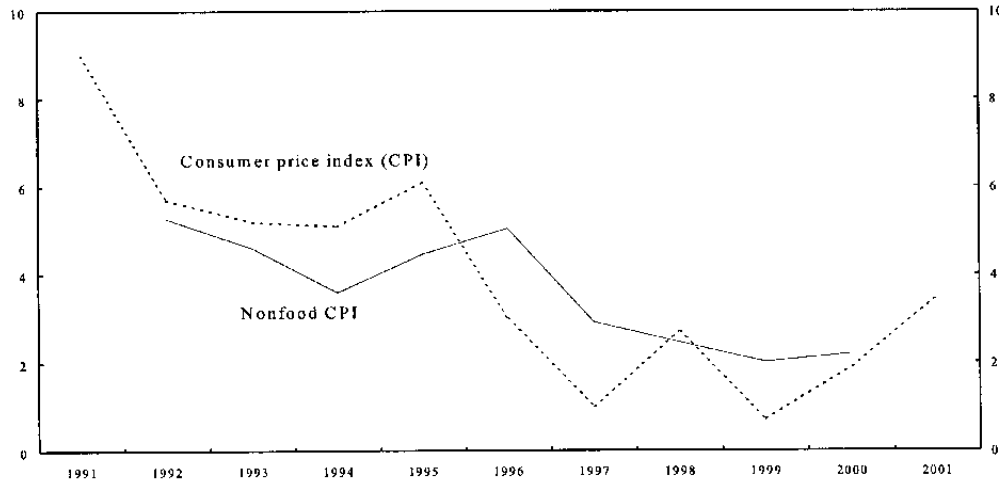
Privatization has led to higher efficiency. As the authorities were preparing the tender for the mobile license in 1998, Maroc Telecom started to improve the quality of its services, expand its network coverage, and reduce its tariffs. Substantial benefits are also expected from the mobile license itself since the bidders have committed to population and road length coverage above the minimum requirements set by the government: the mobile network has already covered 90 percent of Morocco's population, a result originally expected by end-2003. As a result of the introduction of competition in the mobile market, the total of Maroc Telecom's GSM subscribers jumped from 16,600 in 1998 to over 2.4 million by end-2000. Tariffs were reduced four times in less than two years and fell to less than one-half what they had been before the issue of the tender. They are now within 10 percent of the best European prices.

Significant benefits in terms of future taxes and employment creation are also expected. According to World Bank estimates, by 2008 the mobile license should generate an additional fiscal revenue of up to US\$2.5 billion in present value terms. Medi Telecom is also expected to create 3,000 jobs directly and an additional 20,000 jobs indirectly.

¹ The licensing process was conducted by an independent regulatory agency created in 1996, the Agence nationale de réglementation des télécommunications (ANRT). The ANRT set out the criteria for evaluating the bids in a tender document and asked qualified bidders to make technical and financial bids. A bid evaluation report was also published on the ANRT website.

7. **Consumer price inflation remained subdued in 2000 at about 2 percent year-on-year** (Figure 4). The government's decision not to pass through all of the increase in international prices for petroleum products contributed to this outcome. Inflation figures through March 2001 point to continued price stability. However, the prospects for 2001 are for an acceleration of inflation to 3–3.5 percent on account of the April 2001 devaluation of the dirham and of a pick-up in domestic demand.

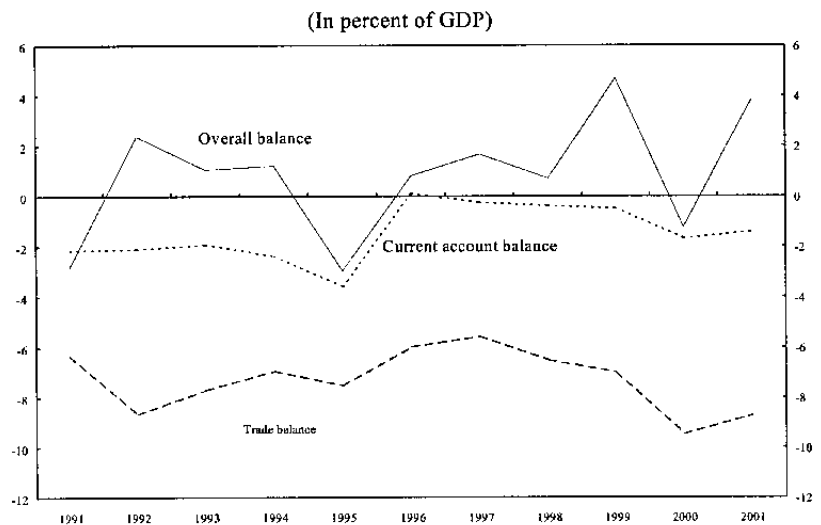
Figure 4. Morocco: Consumer Prices, 1991–2001
(Annual percent change)



Source: Moroccan authorities; and staff estimates.

8. **The external position remained comfortable.** Foreign reserves were close to US\$5 billion at end-2000, about US\$1 billion lower than in 1999 when they had been boosted by the sale of the second license for GSM operators. The proceeds from the sale of 35 percent of Maroc Telecom again boosted reserves to US\$7 billion at end-April 2001; by the end of the year reserves will likely be at US\$6 billion (or the equivalent of 5.5 months of imports). The external current account deficit widened to 1.7 percent of GDP in 2000 from 0.5 percent in 1999 (Figure 5) because of several factors: (a) increased agricultural imports were needed to offset the fall in domestic production; (b) there were large imports of telecommunication equipment goods; (c) the national airline (Royal Air Maroc (RAM)) purchased new planes; and (d) oil import prices increased substantially while prices of phosphate exports declined. These factors are not likely to recur in 2001, leading, together with the devaluation of the dirham, to a small improvement in the external balance despite the acceleration of domestic demand. Moreover, private savings are likely to improve and benefit the external current account since the increase in agricultural incomes will not be perceived as permanent.

Figure 5. Morocco: External Balances, 1991–2001



Source: Moroccan authorities; and staff estimates.

B. Policy Developments

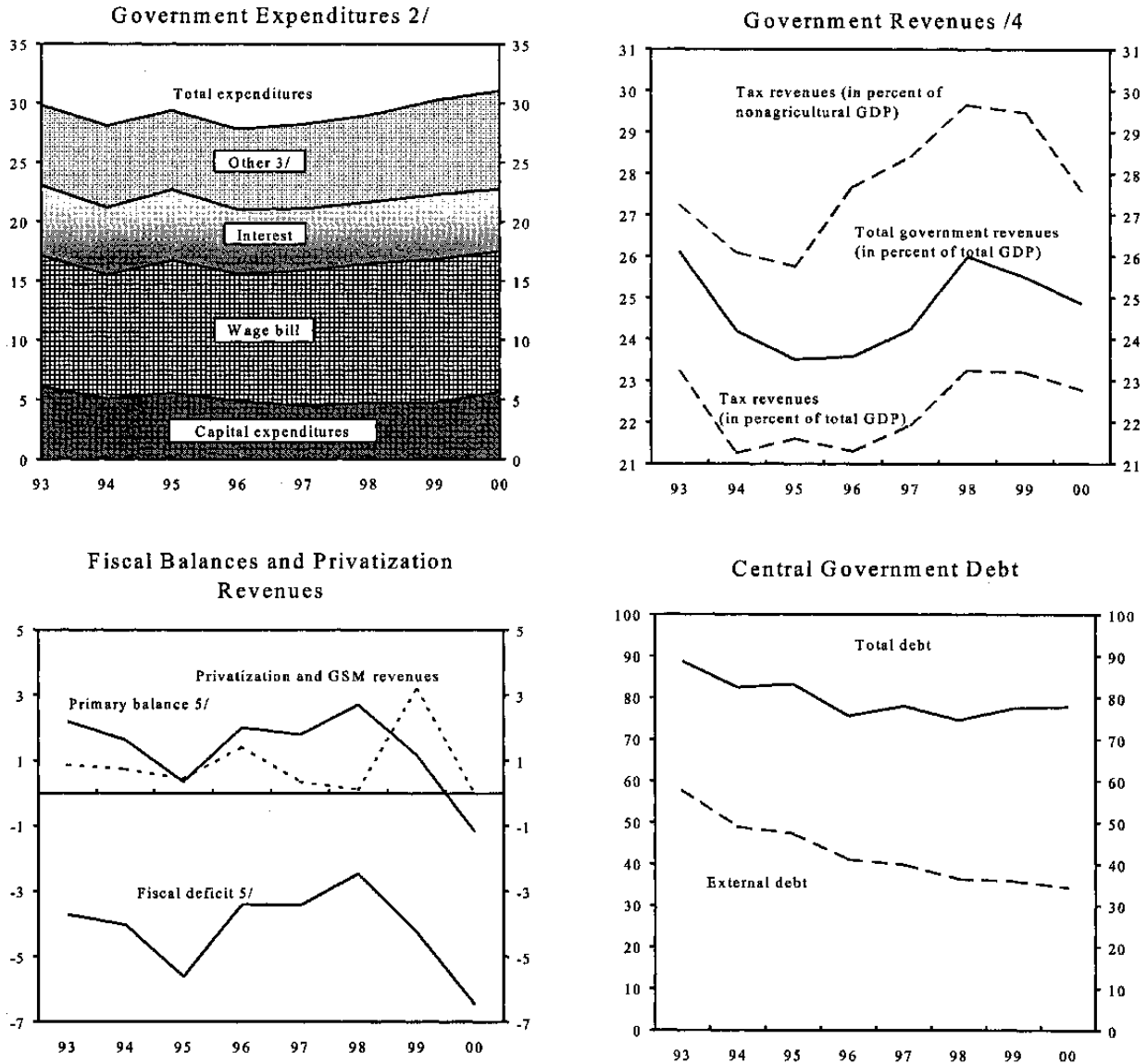
9. **Financial policies have taken a pro-cyclical stance since mid-2000.** Fiscal policy has been adding stimulus to aggregate demand and monetary policy was loosened to encourage private investment.
10. **The budgetary position started to deteriorate in FY 1999/2000, and fiscal policy took an increasingly expansionary stance during the year 2000** (Figure 6 and Box 2). The fiscal deficit reached 4.3 percent of GDP in FY 1999/2000 (excluding privatization receipts) up from 2.5 percent in the previous fiscal year as a result of higher wage outlays, price subsidies for petroleum products,³ and lower nontax revenues. The special six-month budget covering the second half of 2000 envisioned a substantial increase in government outlays (investment and drought-related spending) and resulted in a widening of the deficit, to be financed through the proceeds from the sale of the 35 percent of Maroc Telecom, which were expected by end-2000.⁴ Since these proceeds were only received in February 2001, the government was reluctant to finance the increased spending by issuing government securities that would have raised interest rates. Instead, the government increased budgetary arrears for more than 3 percent of GDP.
11. **The central bank loosened monetary policy starting from end-2000 in response to the tightening of bank liquidity stemming from the accumulation of budgetary arrears.** It injected liquidity through the purchase of government securities and by extending advances to commercial banks. As a result, broad money grew by 8.4 percent in 2000, 1.5 percentage points above the upper limit of the target-range set by BAM but still 2 percentage points less than in 1999 (when monetary policy had been substantially relaxed). The overshooting of the monetary target occurred in conjunction with a lower-than-anticipated accumulation of net foreign assets (about US\$0.8 billion) and reflected substantially higher-than-expected government bank financing (despite the buildup in budgetary arrears), which increased by more than 12 percent in 2000.

³ The authorities' decision not to pass through the increases in international prices for petroleum products resulted in subsidies for one-half percentage point of GDP in 1999/2000 and one-half percentage point of annual GDP in the second semester of 2000.

⁴ Until June 2000, the budget year covered the period from July in one year to June of the following year. Beginning 2001, the budget changed to calendar year coverage. Thus, a special budget was adopted for the period from July to December 2000 to bridge the two annual budgets. The deficit widened in the second half of 2000 to 9.4 percent of GDP on an annualized basis but, because spending and revenues are not uniform throughout the year, the annualized six-month deficit/GDP ratio may overstate the full year deficit.

Figure 6. Morocco: Fiscal Developments, 1993–2000 1/

(In percent of GDP)



Sources: Data provided by the Moroccan authorities; and IMF staff estimates.

1/ Between 1996 and 1999, fiscal year beginning in July of the indicated year.

2/ Excluding net lending and expenditures by special treasury accounts and including expenditures of the Hassan II Fund.

3/ Including transfers to local governments.

4/ Excluding privatization and GSM revenues and excluding tax revenues of special treasury accounts.

5/ Including the balance of special treasury accounts, net lending, and expenditures of Hassan II Fund, but excluding privatization and GSM revenues.

Box 2. Morocco: Public Finance Developments in the 1990s

After the fiscal adjustment of the late 1980s and early 1990s, which resulted in a decline of the central government's overall deficit from 9.6 percent of GDP in 1985 to 2.2 percent in 1992, there was **no significant improvement in the fiscal position between 1992 and 2000.**

The fiscal position deteriorated between 1992 and 1995 mainly as a result of a 2.3 percentage point decline in the revenue-to-GDP ratio, which brought the primary balance from a surplus equivalent to 3 percent of GDP to close to balance. **It improved between 1995 and 1999**, reflecting a 3.8 percentage point increase in the revenue-to-GDP ratio that was partially offset by an increase in noninterest spending (1.4 percentage points of GDP).

Over the 1992–99 period, **the increase in revenues (mostly direct taxes and “other taxes”) was offset by an equivalent increase in noninterest current expenditure** (wages, food subsidies, and other current spending), while capital expenditures remained essentially unchanged.

In 2000, due to a decline of revenues (other tax revenues) and a rise of expenditures (subsidies and capital expenditures), **the primary balance shifted into a deficit (1.2 percent of GDP)** for the first time since 1985.

Revenue

Tax revenue increased to 24.2 percent from 23.9 percent between 1992 and 2000, but **this increase reflected only the declining importance of agriculture** that is not taxed and shrank to 12.4 percent from 15.4 percent of total output over the same period.

The ratio of tax revenue to nonagricultural GDP provides a better picture of revenue performance. This ratio dropped to 27.6 percent from 28.2 percent between 1992 and 2000. After declining sharply between 1992 and 1995 (to 25.8 percent), this ratio recovered between 1995 and 1999 (to 29.5 percent).

Both **external trade liberalization and growing exemptions from import tariffs** led to a decline in import taxes as a portion of nonagricultural GDP (from 6.0 percent to 5.4 percent), explaining only part of the weakening revenue performance. The proliferation of tax exemptions and the end of the extension of preferential tax rates reduced **value-added tax collections**, also explaining the weakening revenue performance.

Higher personal income tax revenues, mainly a result of creeping tax brackets, and higher other revenues from public enterprises offset, in part, the decline of trade and indirect taxes.

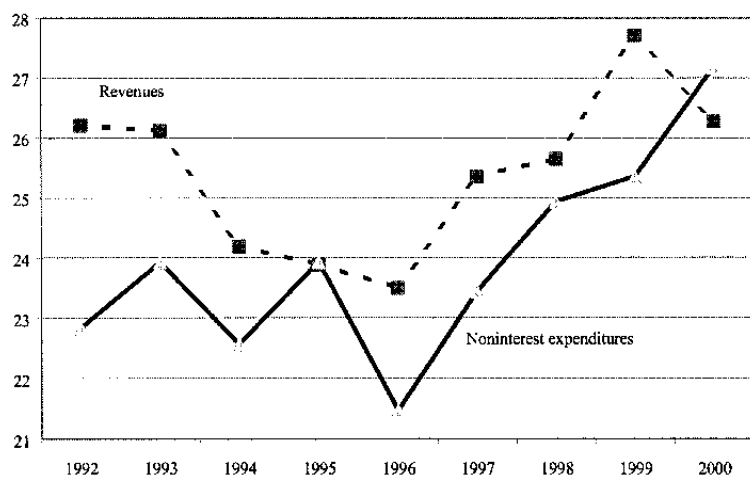
Expenditure

Total expenditures grew during the 1990s from 28.4 percent of GDP in 1992 to 32.4 percent in 2000. This increase reflects a rise in noninterest current expenditures (from 15.8 percent to 19.4 percent of GDP) and an increase in capital expenditures (from 5.2 percent to 6.0 percent of GDP), mostly following the establishment of the Hassan II Fund.¹ At the same time, interest payments decreased by 0.3 percent of GDP to 5.3 percent in 2000.

The rise in noninterest current expenditures resulted from **increases in the wage bill, in food subsidies, and social spending as well as in other current spending.** A 14 percent expansion in public employment matched with a 12 percent increase in real average wages boosted the wage bill to 11.9 percent of GDP in 2000 from 10.8 percent in 1992.

Central Government Revenues and Noninterest Expenditures

(In percent of GDP)



Source: Moroccan authorities.

¹ The Hassan II Fund was established as an extra-budgetary fund to protect part of the privatization proceeds from financing current outlays and to promote infrastructure investment in partnership with the private sector as well as social projects.

12. **External public debt fell below 50 percent of GDP at end-2000** in line with government policy since the mid-1990s to reduce foreign indebtedness. Active debt management, FDI flows, the substitution of domestic debt for external debt, and further appreciation of the dollar vis-à-vis the euro reduced external public debt from US\$17.5 billion in 1999 to US\$16.1 billion in 2000. In 1999–2000, Morocco signed debt-swap agreements with bilateral creditors including France and Spain, resulting in a debt reduction of about US\$365 million. Morocco's external debt service remains relatively high at 25 percent of exports of goods and services (21 percent when including workers remittances). Although the dirham is fully convertible for nonresidents, portfolio investment has remained modest. However, inclusion of the Moroccan stock exchange in the Morgan Stanley's emerging market index in June 2001 is expected to attract more foreign investors.

13. **The accommodating stance of monetary policy continued during the first quarter of 2001** with a reduction in BAM's benchmark interest rates in the interbank market in March.⁵ As mentioned earlier, improved coordination between the central bank and the ministry of finance has facilitated monetary management of the inflows linked to privatization in February 2001. In fact, the ministry of finance has agreed to repay its outstanding debt with the central bank and block part of the proceeds earmarked for the recently established public investment fund (Hassan II Fund) in a special central bank account.⁶

14. **Structural reforms proceeded on several fronts.** The liberalization and privatization of the telecommunications sector has not only brought in substantial financial benefits, but also reduced communication prices while creating a large number of jobs (see Box 1). Moreover, the reform of the regulatory framework and the transparent procedures followed for the sale of both Maroc Telecom shares and the second GSM phone license have strengthened Morocco's credibility as a destination for foreign investment. The government has also eliminated the generalized price subsidies on edible oils in conjunction with its price and import liberalization, which caused adverse incentives for agricultural production and mostly benefited large producers and intermediaries. The rural infrastructure programs (electricity, drinking water, and roads) have accelerated; a social development agency has been established to address pressing poverty needs; and a program that helps disadvantaged women and children has been reformed. Better labor market intermediation has been established through the new National Agency for Employment. The Royal Commission on Education Reform, established in 1999, has launched a number of reform measures, including implementation of universal primary education by 2003.

⁵ BAM reduced both its rate for seven-day advances by 25 basis points to 4.75 percent and its rate on five-day advances by 75 basis points to 5.75 percent.

⁶ The Hassan II Fund was established as an extra-budgetary fund to protect part of the privatization proceeds from financing current outlays and to promote infrastructure investment in partnership with the private sector as well as social projects. Up to 50 percent of privatization proceeds can be earmarked for investment projects under the Hassan II Fund.

15. **The government has also started to take actions to improve transparency and governance in the public sector;** these include: (a) a draft law establishing new rules and procedures for public procurement; (b) a code of conduct and financial disclosure for senior civil servants; (c) the adoption of a law on the operation of public monopolies by the private sector; and (d) the establishment of a competition council. A parliamentary commission has been established to examine responsibilities in a number of corruption episodes, including the one concerning the real estate public bank (Crédit Immobilier et Hôtelier (CIH)). Moreover, the government has established a forum with social partners to identify administrative and legal improvements that would reduce the scope for corruption and rent-seeking behavior. In parallel, the business association announced a best practices charter in corporate governance.

16. **Trade liberalization has progressed as planned.** In the context of the Association Agreement with the European Union (AAEU), tariffs on some industrial goods and processed agricultural products declined by 25 percent in 2000 and 2001 and the number of goods subject to reference prices was reduced (see Box 3). To facilitate the implementation of the AAEU, the European Union (EU) provides support to Morocco through the MEDA program, which has committed €143.6 million for the period 2000–01, after disbursing €167.1 million during 1995–99.⁷

II. POLICY DISCUSSIONS

17. **The policy discussions took place against the backdrop of the incipient economic recovery and the successful sale of Maroc Telecom.** The authorities were optimistic about Morocco's economic prospects, believing that their efforts toward structural reform were already yielding results and improving the general economic climate. After years of difficult economic conditions, when various exogenous factors had constrained growth, the authorities thought that Morocco finally had the opportunity to grow at rates that implied a significant improvement in per capita income. Private fixed investment has been rising steadily, increasing to 21.6 percent of GDP in 2000 from 16.3 percent in 1996. In their view, the presence of substantial slack in the economy, the favorable supply conditions in agriculture, a strong external reserve position, and Morocco's strong track record of macroeconomic stability could justify a fiscal stimulus supported by monetary policies aimed at avoiding increases in interest rates that could choke off the recovery. Moreover, a good portion of the fiscal stimulus provided in 2001 resulted from increased government investment (through the Hassan II Fund), which was aimed at removing infrastructure bottlenecks and providing seed money for private investments.

18. **The mission shared the authorities' view that economic reforms had begun to take hold. Nevertheless, the policy challenge was to ensure a sustained increase in the growth rate to reduce unemployment and trigger a durable decline in poverty.**

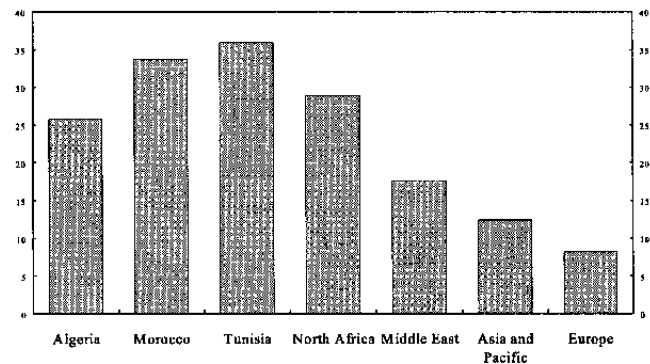
⁷ None of the funds committed for 2000–01 have been disbursed so far.

Box 3. Morocco: Trade Liberalization

Substantial trade liberalization has been achieved since the mid-1980s. For nonagricultural products, the maximum custom tariff (including the special import tax) has been reduced from over 70 percent in the mid-1980s to 50 percent in 2001. The special import tax and the custom tariff were unified in 2000. The number of tariff bands has been reduced from 26 in the 1980s to 8 in 2001, and most quantitative restrictions were lifted or transformed into tariff equivalents (live animal, meat, dairy products, and other agricultural products). Morocco has been a World Trade Organization (WTO) member since 1994.

However, Morocco's trade regime is still restrictive. Morocco's most-favored nation (MFN) tariffs are above those of most other countries in the region and elsewhere (see Figure). Morocco's trade regime is ranked an 8 out of 10 on the Fund's index of trade restrictiveness, in line with other North African countries. The rank results from an unweighted average MFN tariff rate of 33.9 percent and moderate nontariff barriers. The latter includes license requirements for specific goods on health and security grounds and reference prices—mainly for textiles, clothing, and electrical household appliances. The deadline for the elimination of reference prices, which was agreed with the WTO, is July 2001. If Morocco eliminates the reference prices, its rank could drop to 5, putting Morocco among the moderate trade regimes (e.g., Brazil, Saudi Arabia, and Turkey)

Simple Average MFN Tariff Rates, 2000
(In percent)



Source: IMF staff estimates.

Morocco is liberalizing its trade regime through a bilateral agreement with the European Union (EU). The Association Agreement with the EU (AAEU), which became effective in 2000, aims at creating a free trade zone for industrial products by 2012.

Tariff dismantling. Tariffs on capital goods were eliminated in 2000, and those on noncompeting goods have been reduced by 50 percent and will be eliminated by 2003. Tariffs on competing products will be dismantled starting in 2003. As a result, tariff rates on imports of manufactured goods from the EU are today 4 percentage points lower than under the MFN regime (see Table), and the average effective tariff rate was reduced to 12.6 percent in 2000 (15.2 percent in 1999)

Morocco has entered into other trade agreements, including with countries of the region. In 1997, Morocco signed an agreement similar to the AAEU with the members of the European Free Trade Area (EFTA). Morocco also maintains preferential trade arrangements with Algeria, Guinea, Iraq, Libya, Mauritania, Saudi Arabia, and Senegal. It has entered into bilateral free-trade agreements with Egypt, Jordan, and Tunisia, and is a signatory to the Greater Arab Free Trade Agreement (GAFTA).

Morocco: Average Tariff Rates, 2001–02

	MFN 2001	EU Tariffs	
		2001	2002
All products	33.7	30.0	28.8
Agriculture	52.9	50.8	50.5
Manufacturing	30.5	26.5	25.2

Source: IMF staff estimates.

A proposal for a new tariff reform is under consideration by the authorities. The reform would reduce the number of MFN tariff rates from 8 to 5 and the maximum rate from 50 percent to 40 percent. With the reform, the simple average tariff rate would be in the range of 25–28 percent depending on the distribution of goods across bands. The authorities estimated the revenue cost of this reform at about DH 1 billion (0.3 percent of GDP). The reform would contribute to reducing the widening gap between MFN and EU tariff rates. However, for this to be maintained over time, additional trade liberalization will be needed.

While existing trade agreements contribute to trade liberalization, the following concerns remain:

- Agriculture is currently excluded, and negotiations with the EU—expected to open in 2001—have been delayed to allow for a decrease of tariffs on cereals and sugar in Morocco, and increased access of Moroccan agricultural products in Europe.
- Effective protection has increased as a result of the AAEU agreement, therefore Morocco's industry has not yet been exposed to strong competition, but pressures will arise soon. Competitive pressures will intensify as a result of the dismantling of textile quotas under the WTO (multifiber agreement) and, as of 2005, textile and clothing exports from all countries will receive quota-free access to the EU, Morocco's main export market.

Stimulating domestic demand could not constitute a viable strategy for a sustained acceleration in growth over the medium term. To this purpose, a deepening of structural reforms together with actions to improve external competitiveness would be essential. A return to a more cautious fiscal stance is also needed to ensure that pressures on available resources do not diminish private sector activity either through increases in the real interest rate or price increases for nontradable goods that would further erode the competitiveness of Morocco's exports. While the expansionary financial policies have not yet resulted in noticeable adverse effects on macroeconomic stability, inflationary pressures are bound to emerge as the recovery gains momentum, using any slack the economy may have left.

A. Fiscal Policy

19. **The overall fiscal balance will deteriorate in 2001 and worsen the government financial position.** Excluding proceeds from privatization, the budget for 2001 envisions a deficit of about 7.9 percent of GDP, up from 4.3 percent in 1999/2000. However, delays in the implementation of investment spending under the Hassan II Fund and a small favorable impact on revenue collections of the devaluation of the dirham are likely to bring the deficit down to 7.2 percent of GDP. Total financing needs would amount to 10.6 percent of GDP when the repayment of arrears (3.4 percent of GDP) is taken into account. The proceeds from privatization (6.3 percent of GDP) will cover only part of the expected government financial needs in 2001. With negative foreign financing of 1.7 percent of GDP, domestic government financing will need to increase to 6.0 percent from 4.3 percent of GDP between 2000 and 2001.

20. **The authorities stressed that the widening of the deficit in 2001 will reflect, in part, a number of special factors that would only have a small impact on the underlying fiscal position;** these include: (a) large retroactive wage payments; (b) drought-related spending; (c) exceptional capital transfers to public enterprises and investment spending under the Hassan II Fund; and (d) a return to normal levels of income tax collection, which had been boosted by exceptional factors (such as payments of tax arrears from Charbonnages du Maroc and the Office National d'Electricité) in 1999/2000. The authorities underscored the fact that the wide yearly fluctuations in GDP make yearly comparisons difficult to interpret. Moreover, they noted that part of the increase in spending was unlikely to translate into a demand stimulus since it reflected outlays for the recapitalization of public banks. In response to these views, the staff constructed two measures of fiscal stance (see Box 4):

- (i) The structural fiscal balance where these one-off factors are taken out and trend GDP is used instead of the actual GDP. This measure shows that the structural deficit increases much less than the overall deficit (4.9 percent of GDP in 2001 as compared to 4.2 percent in 1999/2000). Nevertheless, there has been a widening in the structural deficit since 1996/97 toward levels that would not be sustainable or in keeping with the downward path of the fiscal deficit envisaged under the authorities' five-year plan, ending with a deficit of about 2.5 percent of GDP in 2004 (excluding privatization proceeds).

Box 4. Morocco: Some Indicators of Fiscal Stance

Cyclically Adjusted Balance. Attempts to estimate the fiscal position that would prevail if actual and trend output were the same. It is calculated by correcting revenues and expenditures for the impact of short-term GDP fluctuations.

On the **revenue** side. Assuming a unit elasticity of tax revenues with respect to nonagricultural output (used as a proxy of their tax base), adjusted tax revenues are calculated as the actual tax ratio to nonagricultural GDP times the trend nonagricultural GDP. On the **expenditure** side: adjusted budgetary spending on food subsidies is calculated by subtracting its cyclical component, which depends on domestic agricultural production and international food prices. In the absence of an unemployment insurance scheme, we assume other outlays reflect output fluctuations only to a negligible extent.

Over the last few years, the budgetary impact of short-term GDP fluctuations was limited. This is due to the fact that Morocco's output fluctuations originate mainly from the impact of droughts on agricultural output. Since agriculture is not taxed, the fiscal impact of these fluctuations is negligible.

Actual and cyclical adjusted balances were very close. In recent years they tend to coincide because of the narrowing of the nonagricultural output gap.

Morocco: Fiscal Balances

(In percent of GDP)

	FY 1996/97	FY 1997/98	FY 1998/99	FY 1999/2000	2000	2001
Overall balance	-3.4	-3.4	-2.5	-4.3	-6.5	-7.2
Less: budgetary impact of short-term GDP fluctuations	0.3	0.2	0.0	-0.1	0.1	0.0
Cyclically adjusted balance	-3.1	-3.2	-2.5	-4.3	-6.4	-7.2
Less:						
Net repayments from lending	-0.1	-0.9	-0.3	-0.1	-0.1	0.0
Balance of special treasury accounts 1/	-0.7	0.4	-0.2	-0.3	0.3	0.0
Extraordinary tax revenues	0.0	0.0	-1.8	-0.2	-0.2	-0.1
Plus: extraordinary expenditures	0.0	-0.3	0.4	0.8	1.9	2.3
Structural balance	-4.0	-4.1	-4.4	-4.2	-4.5	-4.9
Modified cyclically adjusted balance	-3.6	-4.0	-2.8	-4.2	-6.0	-6.6
Fiscal stimulus	...	0.3	-1.1	1.3	1.9	0.6

Sources: Moroccan authorities; and IMF staff estimates.

1/ Including road fund and subsidy fund.

The modified cyclically adjusted balance. It is used to measure the fiscal stimulus defined as the impact of fiscal policy on aggregate demand. It is computed by correcting the cyclically adjusted balance for the components of exceptional revenues and expenditures, which do not directly affect aggregate demand (e.g., recapitalization of banks and fishing license revenues). The fiscal stimulus is then calculated as the annual change of this modified cyclically adjusted balance.

The budgetary policy has been expansionary in recent years. The fiscal stimulus amounted to 1.3 percentage points of GDP in FY 1999/2000 and to 1.9 percentage points in 2000. In 2001, it should be positive for the third year in a row, amounting to 0.6 percentage point of GDP.

Structural Balance. It provides indications of the size of the underlying fiscal position by correcting the cyclically adjusted balance for one-off government payments and one-off revenues. It is calculated:

- by subtracting from cyclically adjusted revenues any exceptional revenue, including amnesty payments, payments of tax arrears, and exceptional dividend payments; and
- by subtracting from expenditures the extraordinary outlays which include: drought-related expenditures (mostly investment); retroactive payment of salaries increases; financing of the oil subsidy; Hassan II Fund expenditures; net lending; and exceptional transfers to public enterprises.

The structural balance has widened over time. While this balance was around 4 percent of GDP between 1996 and 1999, it amounted to 4.5 percent of GDP in 2000 and is projected to be at 4.9 percent of GDP in 2001. This widening mainly reflects the decrease of fiscal revenues (relative to GDP) and the increase of the wage bill. Because of the high level of exceptional expenditures in 2000 and 2001, the structural balance deteriorates much less than the actual or the cyclically adjusted balance.

- (ii) The modified cyclically adjusted fiscal balance, where the components of revenues and expenditures which do not directly affect demand are taken out. This measure indicates that the fiscal stimulus is still positive in 2001 (0.6 percent of GDP), although significantly lower than in 2000 (1.9 percent of GDP).

21. **The authorities expect total budgetary spending to be 31.5 percent of GDP in 2001, unchanged from 1999/2000.** Current outlays would decline to 23.9 percent of GDP in 2001 (from 24.7 percent of GDP in 1999/2000), mainly as a result of the elimination of subsidies on edible oils and petroleum products, and savings in interest payments. Capital outlays are expected to reach 7.6 percent of GDP up from 6.8 percent in 1999/2000,⁸ as a result of project spending under the Hassan II Fund.

22. **The staff noted that the 2001 budget worsens the expenditure structure, while increasing budgetary rigidities.** In particular, the 2001 budget will raise the wage bill to 12.2 percent of GDP instead of lowering it toward the 9–9.5 percent range established for 2004 by the five-year plan.⁹ This will result from the generalization of automatic promotions to all government ministries and from the expansion in employment (net increase of 12,000 employees in addition to 4,000 temporary workers becoming permanent).¹⁰ Moreover, a high wage drift (3.1 percent per year) coupled with low inflation has implied an increase in real wages even in the absence of discretionary wage increases. The staff believed that the ensuing budget rigidity leaves little room for maneuvering. The wage bill, together with interest payments, absorbs almost 74 percent of tax revenues, leaving few resources for financing other essential outlays such as operations and maintenance, or for meeting exogenous shocks such as droughts or higher energy costs. The authorities responded that they were fully aware of the heavy wage burden imposed on the budget. They stressed that for 2001 most of the recruitment would be directed toward education, consistent with the plan to achieve enrollment of all children in school by 2003. Nevertheless, the authorities are determined to undertake a reform of the civil service. To avoid the buildup of wage pressures in the future, the authorities will soon appoint a high commissioner to tackle the issue of remuneration of government employees and internal promotions. The staff also noted that while the Hassan II Fund could play a key role in promoting infrastructure and social investment, it will be essential that: (a) its operations are

⁸ These figures include transfers to local authorities (which include contributions to investment projects) and are significantly higher than the national accounts definition of public investment.

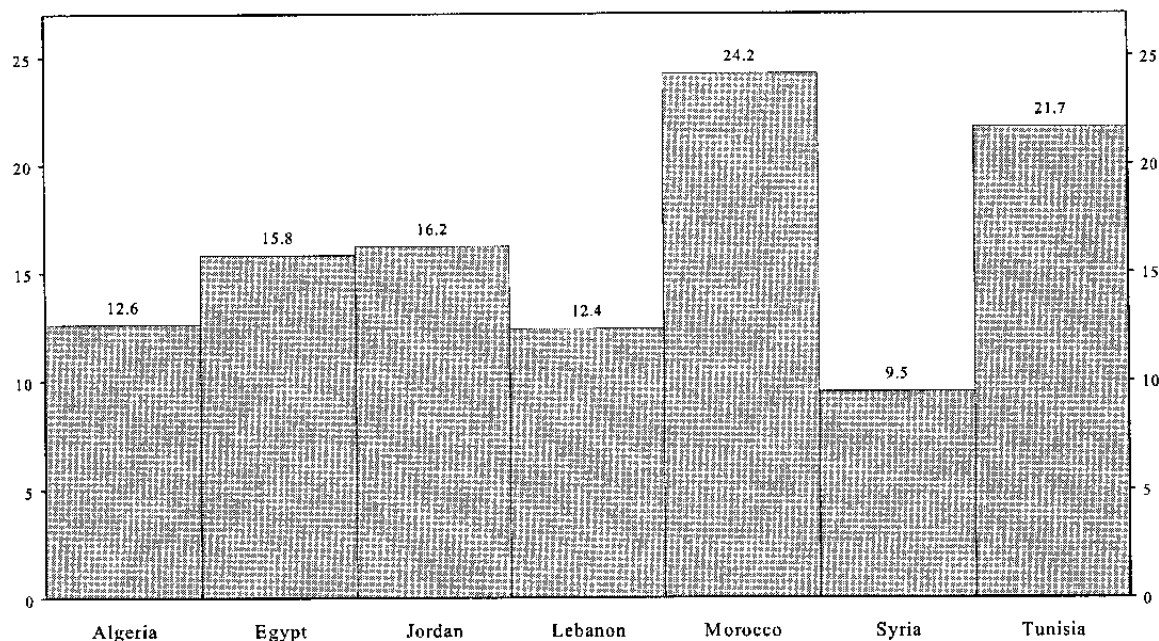
⁹ With the inclusion of retroactive wage increases of about 0.4 percent of GDP, the actual wage bill in 2001 amounts to 12.6 percent of GDP.

¹⁰ Following wage negotiations in 1996, the authorities had agreed to grant promotions for the education and health ministries on a seniority basis only, de facto abolishing the pre-existent quota limits.

closely coordinated with the budgeted capital expenditures to avoid duplications; and (b) its spending decisions take into full account their impact on future, recurrent outlays.

23. **The 2001 budget targets revenues at 24.3 percent of GDP, down from 27 percent in 1999/2000.** This decline reflects: (a) a tax base that does not include agriculture and, thus, does not benefit from the upswing in agricultural production; (b) the narrowing of the tax base through increased tax exemptions, partly in the attempt to counteract competitiveness losses resulting from the real appreciation of the dirham; (c) the adverse impact of revenue measures introduced by 2001 budget, such as the lowering of excise taxes on energy production; and (d) further reductions in external tariffs in the context of the association agreement with the EU.¹¹ The latter trend will continue as Morocco liberalizes its trade regime during the coming years, further reducing the margins for budgetary maneuvering. Nevertheless, the staff believes that it is possible to restore the tax revenue ratio about 25 percent of GDP, given Morocco's strong track record in tax administration which raised its tax ratio above those of other countries in the region (Figure 7).

Figure 7. Morocco: Southern Mediterranean Arab Countries Tax Revenue, 1999/2000
(In percent of GDP)



Sources: Data provided by country authorities; and IMF staff estimates.

¹¹ Moreover external tariffs earmarked for price subsidies on edible oil products were eliminated in 2000. However, the impact of this revenue reduction on the overall fiscal balance is offset by a decline in spending for the subsidy.

24. **The staff believes that the expansionary fiscal stance in 2001 presents limited risks for macroeconomic stability in the near term. However, if not corrected, it would have an adverse impact on inflation and the external position when capacity constraints emerge.** Under current policies, the fiscal deficit in 2002 would be about 6 percent of GDP, a level that could entail crowding out of the private sector activity and excessive demand pressures. Second, the rigidities created by the increase in expenditure in 2000 and 2001 and the weakening in revenue performance will make deficit reductions more difficult in the future, when privatization proceeds will no longer be available, although exceptional investment expenditures would decline as well. While these proceeds have allowed the public debt-to-GDP ratio to decline even in the face of widening fiscal deficits during 1999/2000–01, this ratio at 77 percent remains high and should decline further. Moreover, a number of contingent liabilities and future claims on budgetary resources could further burden the fiscal position. These include: (a) the financial position of the social security funds for the military personnel and civil service (CMR), for the national railway company (ONCF), and for other public enterprises;¹² (b) the cost of extending medical coverage to the poor; (c) the cost of introducing universal primary education; and (d) adequate recapitalization of the two specialized banks (see paragraph 31 below) and social safety net provided to poor farmers.

25. **The mission believes that corrective fiscal action needs to be taken as soon as possible** in order to converge to the fiscal consolidation path envisioned by the five-year plan. While privatization proceeds have been utilized to finance debt reduction and public investment, they can also finance the costs of one-off structural reforms such as the much-needed reorganization of the civil service and further price liberalization in agriculture.

26. **Some actions could already be taken in 2001.** In particular, the elimination of the generalized price subsidies for wheat and sugar—which mostly benefit intermediaries—could be done through administrative procedures. The recent favorable experience with eliminating the subsidy for edible oils has shown that this can be done without causing social opposition. The taxation of diesel fuel could be brought in line with that of the other petroleum products. On an annual basis, these measures could yield the equivalent of 0.8 percent of GDP. It will also be important that the existing automatic price adjustment mechanism for domestic petroleum prices be allowed to operate without government interference to avoid the subsidies which emerged in 1999–2000.¹³

¹² A case in point is Morocco's state-owned phosphate producer (OCP), which is plowing its profits into funding its pension scheme. While this does not entail budgetary contributions, it has resulted in dividends foregone.

¹³ The operation of the automatic price mechanism was suspended in September 1999, when energy prices shot up. Consumption prices for petroleum products were brought in line with international prices in September 2000 but have not been adjusted since then.

27. **A key test of fiscal management will be the 2002 budget. A substantial deficit reduction (in the range of 2–2.5 percentage points of GDP) is necessary in order to: (a) reverse the decline in government savings since 1999; and (b) signal the authorities' intention to resume the fiscal consolidation** established during the first years of the government's tenure when the deficit amounted only to 2.5 percent of GDP (excluding privatization). This would, no doubt, improve the chances for continued economic recovery by providing room for private investment. The authorities had not yet started discussing the budget for 2002. However, they believed that most of the recent widening in the fiscal deficit could be reversed. They emphasized that, although 2002 was an election year, they were determined to achieve a significant fiscal deficit reduction with the 2002 budget. Among the measures suggested by the mission were a freeze in net civil service recruitments and discretionary salary increases, a broadening of the tax base by reducing tax exemptions, and a consolidation of value-added tax (VAT) rates in line with technical assistance recommendations.¹⁴ Important elements of tax reform would include a broader VAT tax base, the revision of the personal income tax brackets and tax-exempt income threshold, and the harmonization of the corporate tax rate in the financial sector. The authorities are taking important steps to improve tax administration, in line with the recommendations of a recent fund technical assistance mission, but need to tackle some important tax policy issues.¹⁵

B. Monetary Policy

28. **In light of the favorable inflation outcome for end-2000, the authorities believe a loosening of monetary policy at the beginning of 2001 could help support the ongoing recovery without threatening price stability.** The authorities do not see inflation as a significant risk in the near term and believe that existing controls on capital flows for residents allow some role for monetary policy even under a fixed exchange rate. The authorities' monetary program for 2001 envisions an increase in the growth of broad money to 9.5 percent from 8.4 percent in 2000. Despite a significant accumulation of net foreign assets and only a limited reduction in credit to government, this would allow credit to the private sector to grow at a rate of 10 percent, unchanged from 2000. BAM's money growth target for 2001 is significantly higher than its medium-term range target growth (6–7 percent) and assumes a decline in money velocity as a result of the improved general economic climate and agricultural production.¹⁶

¹⁴ See Fiscal Affairs Department (FAD) Technical Report, February 2001, "Modernisation du système fiscal et de son administration."

¹⁵ The authorities are implementing most of the recommended measures on tax administration with assistance from FAD. However, the authorities have not yet decided whether to modify the present system of division of responsibilities in tax administration between the treasury (collection) and the tax department (enforcement).

¹⁶ BAM's monetary projections use nonagricultural GDP as the basis for computing velocity of money. However, BAM believes that the projected large increase in agricultural incomes will

(continued)

BAM plans, however, to revise its money growth target downward in case its accumulation of net foreign assets is lower than envisaged. BAM expects to return to its medium-term range target growth rate for broad money beginning in 2002, when money velocity would improve only slightly.

29. **While BAM has certainly succeeded in establishing low rates of inflation during the recent years, the loosening of monetary stance in the presence of a fiscal stimulus poses risks. It is essential that BAM remains vigilant against possible inflationary pressures, allowing interest rates to move up, if necessary.** This is even more important now that the dirham has been devalued in conjunction with a significant fiscal stimulus, which is expected to raise inflation to 3–3.5 percent in 2001. More generally, the adoption of a pragmatic approach to exchange rate policy will require a strengthening of the monetary policy framework and the development of a broad set of indicators to assess monetary conditions, including a measure of underlying inflation. Fund technical assistance is available, should the authorities request it.

30. **The authorities are beginning to address the financial situation of the two troubled development banks, CIH and Caisse Nationale de Crédit Agricole (CNCA).**¹⁷ A two-year plan has been adopted to restructure the CIH, which entails support from the government and an increased capital contribution from shareholders (including BAM).¹⁸ While the plan envisions an overhaul of the CIH operations and new management, it will not recapitalize the bank sufficiently so that it can meet prudential regulations before 2003. In regard to the CNCA, which has suffered from the recurrence of droughts and weak management, a restructuring plan is still under discussion. This plan could involve debt forgiveness and rescheduling, and would transfer assistance to small farmers affected by droughts to the budget, limiting the CNCA operations to commercial lending. Prompt actions to bring both the CIH and the CNCA to capital adequacy and full provisioning are needed to ensure soundness of these banks and to fully identify the budgetary cost of these operations. Moreover, an intensification of efforts to collect the nonperforming loans would provide credibility to the restructuring plan and help to improve governance in banking. The mission cautioned the authorities to limit any debt forgiveness and

have an impact on money demand, which would therefore justify the assumed decline in velocity.

¹⁷ The increase in the nonperforming loans of these two public banks contributed for about 50 percent in the increase of the banking system nonperforming loans observed in 2000. The ratio of problem loans to capital of the banking system increased from 98 percent in 1999 to 121 percent in 2000 (see Table 9).

¹⁸ The nonperforming loans of CIH amounted to DH 15.7 billion in 2000; provisions for these loans amounted to DH 1.8 billion, DH 2.7 billion less than required by BAM's capital adequacy ratio. The restructuring plan envisions a direct government loan of DH 1 billion along with government guaranties on commercial bank loans to the CIH for an additional DH 3 billion.

rescheduling only to poor farmers in order to avoid a moral hazard, which would undermine credit relations in the future.

31. **The remaining commercial banks satisfy prudential requirements and maintain an average capital assets ratio of 13 percent.**¹⁹ BAM has strengthened its supervision function by modifying the computation methods for the liquidity ratio, extending prudential requirements to the specialized financial institutions, and establishing stricter sanctions for noncompliance. The authorities intend to strengthen the independence of the supervisory authority of the banking system and the stock market as well as strengthening the internal audits in the banking sector. The authorities have requested participation in a Financial Sector Assessment Program/Financial Sector Stability Assessment (FSAP/FSSA) with the Fund and the World Bank. A mission is expected to go to Rabat early in 2002.

C. Exchange Rate Policy

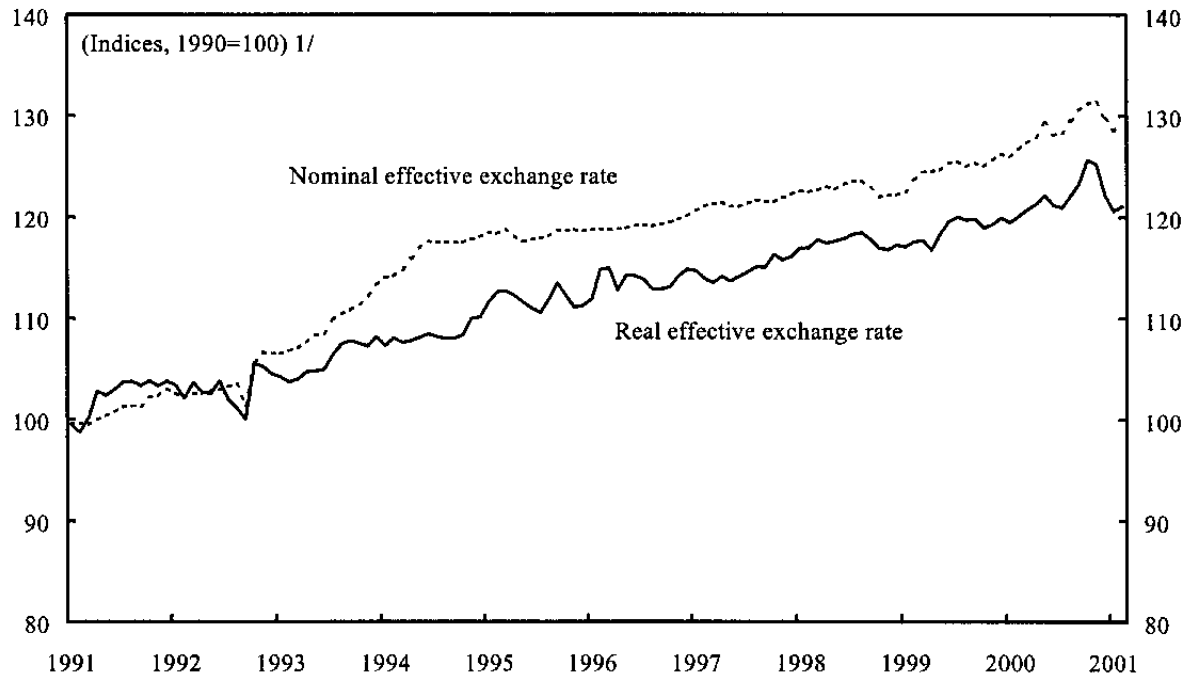
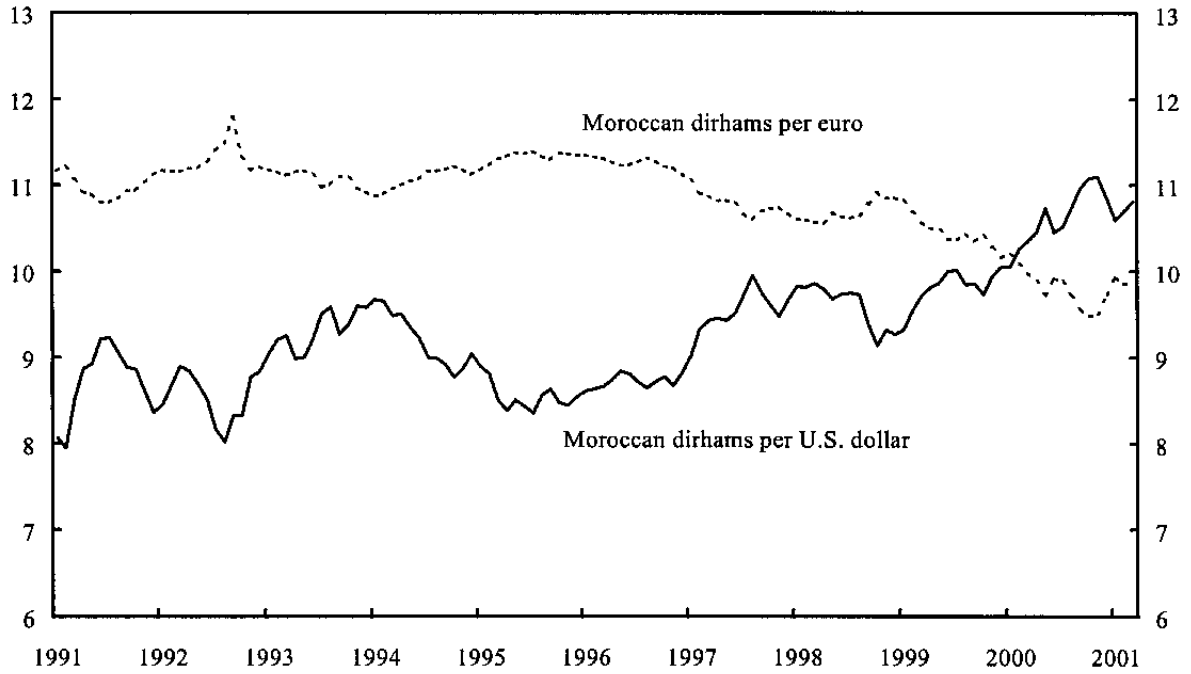
32. **The authorities believe that the fixed exchange rate policy has been behind Morocco's successful macroeconomic stabilization in the 1990s.** In their view, the real effective appreciation of the dirham in the last two years mostly reflected the strength of the dollar vis-à-vis the euro, rather than domestic demand pressures on the price of nontradable goods. They felt that Morocco reached a level of inflation broadly in line with that of its main trading partners in both 1999 and 2000. Moreover, they indicated that there was no decline in the volume of textile exports and that receipts from tourism and workers remittances, which originate mainly from European countries, had increased significantly over the past two years. However, following the adverse movements in the U.S. dollar/euro exchange rate, the dirham was devalued by 5 percent. The authorities also increased the weight of the euro in the currency basket to better reflect the composition of Morocco's trade flows.

33. **The staff commends the authorities' decision to devalue the dirham, even if by a small amount. The mission considers it to be a positive action toward a more pragmatic approach to exchange rate policy and expect it to be a first step toward a more flexible exchange rate policy.** The real appreciation of the dirham has hampered Morocco's export growth which has remained broadly unchanged in dollar terms while world markets have grown substantially during the last five years; import volumes have grown faster than export volumes by an average 1.3 percentage points during the last decade (see Figures 8 and 9). So far, the real appreciation of the dirham has not produced sizable adverse effects on the external current account because of low economic growth and favorable developments in the terms of trade through 1998 and tourism since 1998. However, under a higher growth strategy and continued trade liberalization, a more active exchange rate policy was warranted.²⁰

¹⁹ The performance and conditions of the commercial bank sector were topics discussed at some length in SM/00/105 (5/26/00), Section V, and SM/98/45 (2/13/98).

²⁰ See SM/00/92, Section II-D.

Figure 8. Morocco: Exchange Rate Indicators, 1991–2001

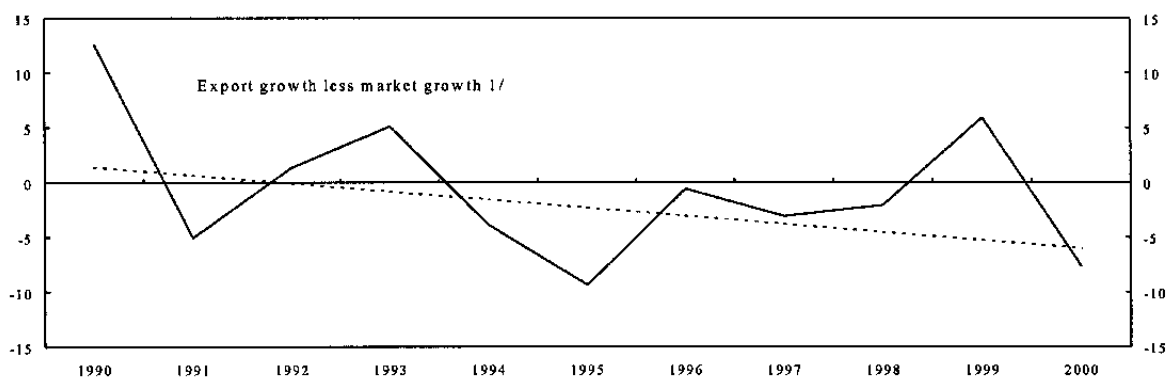


Sources: Information Notice System and *International Financial Statistics*.

1/ An increase in the index reflects an appreciation.

Figure 9. Morocco: Export Performance, 1990–2000

(In percent)



Sources: World Economic Outlook (WEO); Moroccan authorities; and IMF staff estimates.

1/ Volume of goods and services. Market growth is calculated by the WEO as the weighted average of import growth of trading partners, with weights that reflect each country's share of total Morocco's exports.

34. **The staff also reiterated that Morocco needs a more flexible approach to the exchange rate, which could take the form at a crawling peg periodically adjusted to maintain competitiveness or to respond to exogenous shocks.²¹ Maintaining a fixed nominal exchange rate for the dirham has three major drawbacks:**

- (i) It deprives Morocco of an adjustment instrument in response to exogenous shocks, such as changes in the terms of trade. In the absence of exchange rate flexibility, fiscal policy would be normally required to bear the burden of adjustment. Although fiscal policy had contributed to price stability, it could not prevent the substantial real appreciation of the 1990s.
- (ii) It would complicate Morocco's adjustment to trade liberalization, which is equivalent to a real appreciation of the dirham. While trade liberalization will result in productivity gains, which may well offset the implicit appreciation, this will take time since productivity growth is likely to lag behind trade liberalization. Therefore, import competing activities (as well as exports) would require some exchange rate policy support until these gains materialize.

²¹ A discussion of the different possible exchange rate regimes was covered in the 2000 Article IV consultation (see SM/00/92).

(iii) Morocco will eventually integrate its financial markets with the international financial system. As this integration proceeds, defending a fixed parity of the dirham becomes more costly and riskier because of the possibility of speculative attacks. Introducing flexibility in exchange rate policy would facilitate the move toward full convertibility of the dirham for both residents and nonresidents.

35. **However, a move to a more flexible exchange rate regime should be supported** by strict fiscal and monetary policies, and, possibly by an income policy to avoid the possibility that inflationary pressures end up driving exchange rate adjustments. Moreover, the monetary policy framework should be strengthened by adopting broad money growth as a nominal anchor.

36. **The realignment of the currency basket with trading partners' shares will provide greater protection from euro/U.S. dollar fluctuations to most exporters.** This is particularly the case for textile and apparel exports, which are almost entirely destined to European markets. However, Morocco also needs to diversify its exports to other areas. An appreciation of the euro vis-à-vis the U.S. dollar would hinder such diversification. The concentration of more than two-thirds of Morocco's exports in the European market poses some risks considering that it is a low growth market and that Morocco would align its export performance with the European business cycle.

37. **After the recent devaluation of the dirham, the authorities have confirmed to the staff that they stand ready to consider the feasibility and appropriateness of a move to a more flexible exchange rate policy.** They will evaluate the impact of the recent depreciation and closely monitor economic developments in the months ahead. They will consider the opportunity of further policy actions, including a tightening of financial policies. As for the realignment of their currency basket, they felt that their move was justified by the fact that the exports with the highest price elasticity (including tourism services) are destined to Europe.

III. THE CHALLENGES FOR THE MEDIUM TERM

38. **Morocco has experienced a volatile and disappointing growth performance during the 1990s.** Agriculture's contribution to growth has been negative since droughts have become more frequent and severe output fluctuations more pronounced. This was partly due to incentives in favor of cereal crops, which are ill suited to Morocco's dry climatic conditions. Nonagricultural growth remained at an annual average of 3.2 percent per year in the 1990s, a rate insufficient to absorb new entrants to the urban labor force (3.5 percent growth per year). During the second half of the 1990s, the real appreciation of the exchange rate compounded with trade liberalization and declining interest rates reduced the relative price of capital with respect to labor, thus providing incentives to substitute capital for labor (see Box 5). While this has resulted in productivity gains, it has been mostly through lower job creation.

39. **Since the mid-1990s, socially oriented policies have gained momentum, particularly policies geared toward improving education and rural infrastructures.** Some significant results have already been achieved, such as a great improvement in the enrollment of girls in primary rural education and a concrete plan with yearly targets for enrollment of all children by 2003. However, an acceleration in the rate of growth of the economy remains the necessary condition for achieving a sizable reduction in poverty.

40. **The success attained in macroeconomic stabilization together with the recent progress in structural reforms presents Morocco with a unique opportunity for lifting the existing constraints to growth and creating an economic environment that favors poverty reduction.** Low inflation has been credibly established; debt ratios have been reduced markedly; and external reserves have been strengthened; all of which position Morocco favorably to jump-start the economy through bold measures.

41. **The staff stressed that policy reforms, geared toward bringing the economy to a higher growth path, needed to be part of a medium-term strategy.** The structural policy reforms can be supported by privatization receipts. They need to be complemented by macroeconomic policies geared toward export-led growth by keeping demand pressures on nontradable goods under check, creating room for private investment and protecting competitiveness through a flexible exchange rate policy.

42. **To illustrate the policy challenges and opportunities that Morocco is currently facing, the staff discussed with the authorities two medium-term policy scenarios which attempt to quantify the benefits from policy adjustment.** Under the current fiscal stance, the pace of structural reforms and a fixed nominal exchange rate may stabilize growth at a slightly higher level but well short of the authorities' ambitions.²² Under an alternative scenario, a resumption of fiscal consolidation coupled with a flexible exchange rate policy aimed at stabilizing the real effective exchange rate and an acceleration of structural reforms would lead to a significant improvement in growth performance. However, only an improvement in competitiveness—in addition to the measures included in the alternative scenario—can achieve sustained growth rates in the 6 percent range.

43. **In the baseline scenario (current policies), real GDP growth rises from an average annual growth of 2.1 percent over the last decade 1991–2000 to about 3.5 percent per year,**

²² As outlined in the five-year plan already presented in SM/00/92.

Box 5. Morocco: Sources of Growth

Morocco's real GDP growth has been on a declining trend since the beginning of the 1980s. It averaged 2.7 percent in the 1990s versus 3.9 percent in the 1980s. In per capita terms, real GDP grew at an average 1 percent in the 1990s versus 1.6 percent in the 1980s.¹

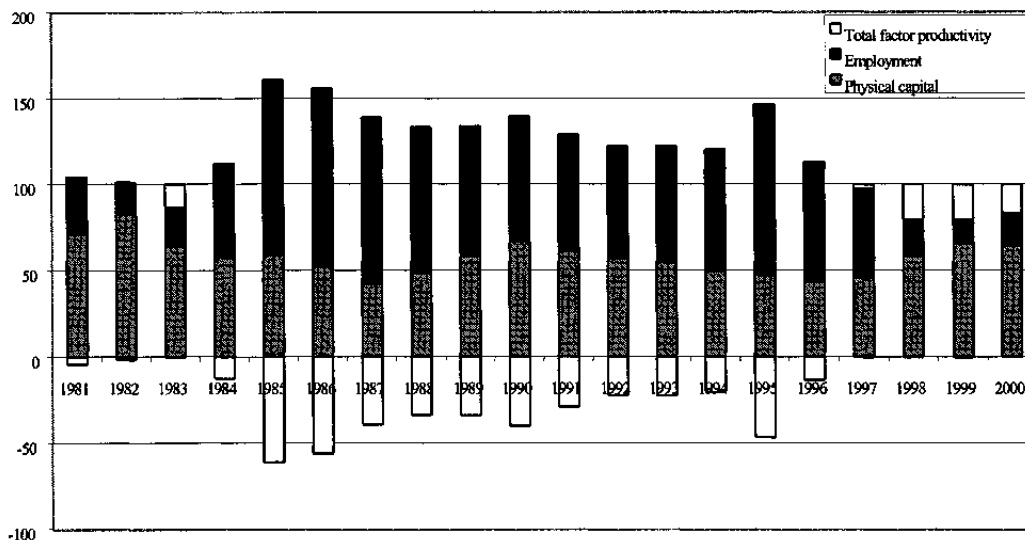
Although greater recurrences of droughts in the 1990s were partially responsible for this slowdown, about one-half of the decrease in GDP growth resulted from a slowdown in nonagricultural growth. Nonagricultural growth averaged 3.2 percent per year in the 1990s versus 3.9 percent per year in the 1980s. The slowdown was broad-based.

On the expenditure side, most of the slowdown can be attributed to a sluggish private demand and faster growth of import volumes than export volumes. Private consumption grew at an average 0.8 percent in the 1990s (3.3 percent in the 1980s), while private investment grew at an average 1.5 percent (6 percent in the 1980s). After being negative in 1990–95, private investment growth picked up strongly in 1995–2000.

Public consumption became the fastest growing component of demand in the 1990s, with an average growth of 3.5 percent (2 percent in the 1980s). The acceleration of public consumption mostly took place in 1995–2000.

On the factor inputs side, the slowdown resulted from decelerating growth rates of capital and employment, while total factor productivity (TFP) growth actually accelerated since the mid-1990s.² Capital grew at an average 4.1 percent in the 1990s versus 5.8 percent in the 1980s. Employment grew at an average 2.7 percent in the 1990s versus 4.1 percent in the 1980s. In contrast, TFP growth accelerated over the period, becoming less negative and ending positive at 0.3 percent per year in 1995–2000. This suggests that the structural reforms of the mid-1990s may have contributed to growth.

Contribution of Factor Inputs to Real GDP Growth



Lower job creation accompanied a surge in the capital-labor ratio, for which the real appreciation of the dirham may be partially responsible. The capital-labor ratio grew at an average 2.2 percent in 1995–2000 (1.2 percent in 1980–95), while employment growth dropped to 1.6 percent (3.8 percent in 1980–95). The real appreciation of the dirham in the 1990s may have contributed to these developments in two ways. On the one hand, it lowered the cost of capital relative to labor. On the other hand, it may have forced producers to improve their productivity by substituting capital for labor to regain competitiveness.

¹ The data on GDP and employment have been smoothed using the Hodwick-Prescott filter.

² The growth accounting exercise for the nonagricultural sector assumes a Cobb-Douglas production function with capital and labor shares of 0.4 and 0.6, respectively.

while nonagricultural growth increases from 3.2 percent to 3.9 percent.²³ The permanence of a significant fiscal imbalance produces adverse effects on private investment, but its effects on growth are mitigated by the impact of continued structural reforms on productivity. The fiscal imbalance may generate pressures on the price of nontradable goods and services leading to further real appreciation of the dirham. The external current account would initially improve following the April 2001 devaluation and widen later as a result of a real appreciation of the dirham; this scenario could lead to fiscal unsustainability as the combination of substantial budget deficits and low growth would bring the government debt-to-GDP ratio back to 77 percent by 2006, despite significant proceeds from privatization.

44. **The alternative scenario is based on a two-pronged strategy:** more forceful fiscal adjustment, and an acceleration of structural reforms leading to larger improvements in total factor productivity. In this scenario, real nonagricultural growth increases to about 5 percent by 2005–06. Inflation would decline to 2 percent by the end of the period because of lower fiscal stimulus and favorable supply response to structural reforms. The external current account would initially improve but would widen later because of increased investment and growth. Strong fiscal adjustment and higher GDP growth would result in a reduction of the government debt-to-GDP ratio to 65 percent by 2006.

45. **The alternative scenario is predicated on the reduction of the fiscal deficit to 2.3 percent of GDP by 2006 through a compression of the government wage bill in relation to GDP, the elimination of subsidies, and the strengthening of government revenues in the face of declining customs tariff receipts.** This would generate larger public savings to finance some increases in government investment, but mostly to create a more favorable financial environment for private investment. This fiscal stance would be supported by a flexible exchange rate policy, which, at the very least, would maintain a stable real exchange rate.

46. **An accelerated pace of structural reforms would also contribute to higher growth in the alternative scenario.** In particular, this scenario is built on: (a) scaling back of the civil service (with targeted yearly reductions in the wage bill in relation to GDP); (b) passing the long delayed labor code; (c) strengthening the commercial court system; (d) further liberalizing agricultural prices in conjunction with the elimination of remaining generalized subsidies; and (e) liberalizing trade along the lines proposed by the authorities to accompany the implementation of the AAEU. Morocco would also facilitate its trade relations with its Maghreb neighbors, by reducing tariffs, eliminating nontariff barriers, and harmonizing customs procedures in the context of the Maghreb Arab Union (UMA). This would be essential for the creation of a large regional market which would encourage foreign investors to locate their productive capacity in the region.

²³ This growth outlook for the nonagricultural sector is based on a growth of total factor productivity broadly in line with the higher level experienced during the last three years. Private investment would improve because of the impact of structural reforms.

47. **On the one hand, the two scenarios illustrate the limits of the current policy stance, and, on the other hand, the benefits from a more ambitious fiscal adjustment combined with a stable real exchange rate.** The second scenario, in particular, shows that although significant, the benefits of fiscal adjustment and accelerated structural reforms may not be sufficient to significantly reduce unemployment and poverty over the next five years. In the staff's view, the authorities should explore a whole range of actions to jump-start the economy to a growth target of at least 6 percent per annum, which would be necessary to meet these objectives. Reorienting the economy firmly toward the traded goods sector through a—faster than presently envisaged—liberalization of imports, an active exchange rate policy, and a deepening of structural reforms (particularly to facilitate private investment) may all be needed to attract much larger FDI and strengthen Morocco's integration with the global economy.

IV. STRUCTURAL POLICIES

48. **The mission congratulated the authorities for their bold initiatives in education, rural development, labor market reform, and governance. The authorities have placed increasing emphasis on social policies.** While economic growth is essential to poverty reduction, improving public expenditure composition can also have an impact on poverty levels. In particular, agricultural support policies have been biased toward large farmers. Education spending has also mainly benefited urban and better-off segments of the population since it uses most of its resources to provide secondary and upper education free of charge, with an insufficient focus on primary and rural education. Most of the expenditures in the health sector have also been concentrated in urban areas and in highly specialized facilities with insufficient provision of basic services, especially in rural areas. The staff welcomes the authorities' plans to offer free primary education to all children and extend medical insurance coverage to the poor. However, this will be possible only if actions are taken to redirect resources away from benefits to well-off segments of the population and realize savings in low priority spending. The quality and effectiveness of public spending could also benefit from the ongoing decentralization process that—through enhanced autonomy for local entities and increased accountability—would make it possible to better match spending priorities and needs, particularly in health and education. It will be essential, however, that the decentralization process not result in duplication of government functions, further increasing general government spending. At the request of the authorities, the World Bank will be conducting a public expenditure review covering the areas discussed above to help improve the prioritization of public expenditures.

49. The negative contribution of the agricultural sector growth in the 1990's underscores the need for an overhaul of agricultural policies. The high tariff protection of wheat and sugar has distorted the incentive system favoring of their production and increased Morocco's vulnerability to droughts (Box 6). The mission has stressed that the elimination of the price subsidies on wheat and sugar should be accompanied by the lowering of customs tariffs in order to shift incentives to alternatives crops. In view of the large rural population involved in these activities, this can only be a gradual process that needs to be accompanied by financial and technical assistance to

redirect farmers to other crops. However, a start has to be made, and the authorities have shown that they can take bold actions in similar areas.²⁴

50. More labor market flexibility is essential for increasing the elasticity of employment creation to growth. The authorities now expect parliament's approval of the new labor code after considerable delays and controversy. The new version of the code allows for a more liberal system of hiring and labor shedding, which should favor the reallocation of labor to the tradable sector. The authorities increased the minimum wage by 10 percent in July 2000, which has been translated into a shift of the overall wage structure and a further reduction of the relative price of capital. This increase also penalizes the modern formal sector of the economy which abides by the minimum wage, and may benefit "insiders" who are employed instead of reducing unemployment.

51. The reform of the civil service and the reorganization of government activities remain top priorities. The high wage bill is not the only reason for civil service reform. An opaque and complex compensation system together with excessive regulations have limited staff redeployment and led to excessive recruitment; there is also a pressing need for updating the skill mix of the civil service to the needs of a modern administration. The staff believes that the government should intensify its efforts to simplify rules, reduce the administration's discretionary powers, and increase accountability.

52. The government has acted to improve governance and fight corruption. This would go a long way toward creating an environment favorable to private sector activity. For this purpose, it will be important to improve the management of public resources in the context of the public expenditure review started in collaboration with the World Bank. The success obtained by the recent customs reform needs to be complemented by streamlining investment procedures, which would attract larger foreign investment. The staff also encourages the authorities to follow up on the conclusions of the parliamentary commission set up to inquire about the alleged mismanagement of the CIH. The authorities have also requested a Report on the Observance of Standards and Codes (ROSC) on corporate governance which the World Bank would be leading toward the end of the year.

53. The successful privatization of Maroc Telecom has shown that privatization can generate substantial efficiency gains (see Box 1). Thus, it is important that the privatization program maintains momentum. A call for bids has been issued for the tobacco monopoly (Régie de tabacs) and the authorities are envisaging a further (15 percent) privatization of Maroc Telecom. An acceleration of privatization in other areas (e.g., sugar refineries, RAM, and the National Development Bank) would provide a stronger signal to investors that the government is fully committed to establish a market-driven economy.

²⁴ Charbonnages du Maroc, which employed several thousand workers, was liquidated after mounting losses.

Box 6. Developments in the Agricultural Sector

The share of agricultural GDP in total GDP dropped from 21 percent during 1970–74 to 16 percent during 1995–99. Agriculture employed 48 percent of the labor force and 62 percent of the total female labor force in 1999. There has been some improvement in the proportion of irrigated areas from 10 percent of total arable land in 1974 to 14 percent in 1996. High producer prices and external tariffs were established to encourage cereal production, which expanded into rainfed areas. Most of the cereal production consists of wheat and barley. At the same time, consumer price subsidies were provided on wheat flour to reduce the burden of protection on the consumer. This subsidy is now limited to a fixed quantity of wheat (1 million tons). The same price support system was applied to oil seeds, which discouraged the production of olive oil, and to sugar beet and cane. Recently, prices for oil seeds were liberalized and the subsidy eliminated while the subsidy on sugar was eliminated only for quantities destined for industrial use. The authorities are considering various ways to eliminate these remaining subsidies.

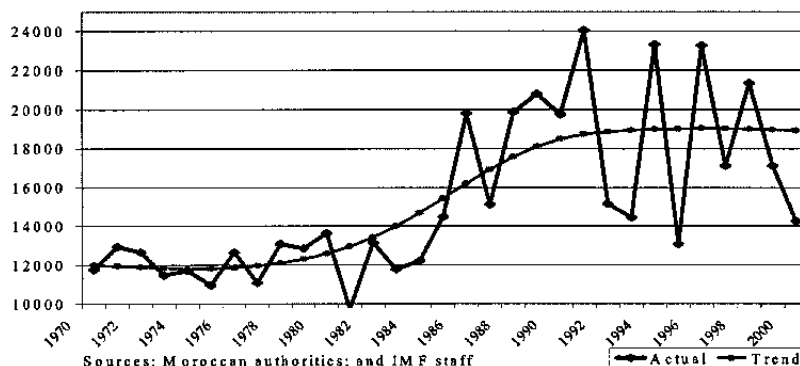
After the expansion of cereal cultivation, the structure of agricultural production remained broadly unchanged during the last decade: 54 percent of Morocco's total cultivated area is cultivated with cereals, including 500,000 hectares in irrigated areas. After increasing significantly during the 1980s, agricultural production stagnated during the 1990s (see Figure). As a result, agriculture's contribution to GDP growth went from 8.2 percent of GDP over the 1981–90 period to a negative contribution during the 1990s (-5.1 percent of GDP).

The increased frequency and severity of droughts (six between 1990 and 2000), in presence of a cropping pattern that favors drought-sensitive crops such as cereal, is the major factor behind the stagnation of agriculture production. It also explains the increased volatility of agricultural production growth; its standard deviation went from 10 percent in the 1970s to 24 percent in the 1980s and to 42 percent in the 1990s.

The stagnation of agricultural production also reflects other structural impediments: (a) a large proportion of small family holdings; (b) the limited use of modern production and stocking techniques; (c) high transport costs; and (d) a low ratio of irrigated/cultivated area.

Real Agricultural Production

(In millions of 1980 dirhams)



V. STATISTICAL ISSUES

54. **Morocco provides adequate statistical information for surveillance.** Information is increasingly made available via the Internet for virtually all sectors of the economy. Cooperation with the staff has been excellent. Morocco received multitopic technical assistance from STA in 1998, and follow-up visits on national accounts methodology and the consolidation of fiscal accounts for general government statistics. The authorities have indicated they intend to subscribe to the Special Data Dissemination Standards (SDDS), and have requested a STA mission to conduct a ROSC on statistics to identify areas where improvements are needed and facilitate accession to SDDS.

VI. STAFF APPRAISAL

55. Over the last decade, Morocco has been able to establish macroeconomic stability and industrial country levels of inflation. External reserves have reached comfortable levels; the external current account deficit remains modest; and foreign debt continues to decline. A long-awaited economic recovery is taking hold, and there are signs that the structural reforms initiated over the last five years are starting to yield results. At the same time, increasing attention is being given to improvement of social conditions, most notably a drive to achieve big strides in literacy and education. Governance is improving as well, with various legislative initiatives and a general increase in transparency. A case in point was the privatization of Maroc Telecom, which was carried out under exemplary conditions of openness and clarity, testifying to the importance that the government attaches to the country's administrative and institutional renewal.

56. Serious policy challenges remain, however. Economic growth needs to rise to a higher plateau to produce a significant reduction in unemployment on a sustained basis and a lasting reduction in poverty. To achieve this, the authorities need to tighten their macroeconomic management and accelerate their structural reforms.

57. The relaxation of both the fiscal and monetary policies in 2001 presents limited risks for macroeconomic stability in the near term. On the inflation front, the recovery from two years of drought has helped contain the impact of increased demand on prices in 2001. On the external front, the impact on the current account has been offset by an improvement in the agricultural balance and by better terms of trade. Nevertheless, the staff believes fiscal and monetary policies need to be redirected toward a more cautious stance as soon as possible.

58. The widening of the fiscal deficit since 1999–2000 has been accompanied by both a decline in revenue performance and a deterioration in the structure of expenditures. A rapidly growing wage bill is increasingly absorbing more tax resources, leaving little to finance other essential current spending and the needed increase in capital outlays. The availability of substantial revenues from privatization has made it possible to increase spending without increasing debt during the last two years. While the staff agrees with the authorities that many of the factors that have caused the widening of the fiscal deficit in 2001 will not recur in future years, the staff is concerned that the deterioration of the fiscal position since 1999/2000 could

place fiscal policy on an unsustainable path. Unless it is reversed, the current fiscal stance would lead to an increase in the government debt as a ratio to GDP over the medium term when privatization proceeds will dwindle. Moreover, a number of contingent liabilities weigh on the medium-term fiscal position, such as the imbalance of some social security and pension funds, the need to recapitalize specialized banks, and the cost of extending medical coverage to the poor, while continued trade liberalization will result in further tax revenue losses.

59. For these reasons, the staff has suggested that the authorities take steps to readjust fiscal policy. To this end, it would be desirable that the budget for 2002 target a deficit reduction of 2–2.5 percentage points from the 2001 level, with the objective of reducing the fiscal deficit further over a five-year horizon. Resuming fiscal consolidation will require taking bold actions both on the revenue and on the expenditure sides. On the revenue side, efforts should focus on: (a) eliminating special tax exemptions; (b) redesigning the VAT by broadening its coverage and reducing the number of rates; and (c) harmonizing the taxation of petroleum products. On the expenditure side, the top priority is to curb the growth of the wage bill by reducing the high wage drift through civil service reform and by freezing net hiring. The costs of the civil service reform may be significant in terms of severance payments and retraining, but it could be financed by the expected proceeds from privatization in 2002. In this sense, future privatization proceeds could help reduce budgetary rigidities instead of building up inertia in government spending.

60. As the economy uses up any slack it may have left, inflation pressures are bound to emerge which, if validated by a continued loosening in monetary policy, would be detrimental to the external balance and inflation. It is essential that BAM follow inflation developments closely and be ready to tighten monetary conditions by allowing interest rates to rise in response to any inflationary pressures.

61. The fixed exchange rate of the dirham constituted an impediment to higher economic growth in the 1990s since it resulted in a significant exchange rate appreciation, which constrained Morocco's export performance well below potential. The authorities' decision to devalue the dirham by 5 percent signaled their intention to place greater emphasis on export growth and on the traded goods sector in general. The staff welcomes this decision since it moves in the direction of the more pragmatic approach to exchange rate policy. Nevertheless, the staff believes that this devaluation should only be a first step toward a more flexible exchange rate policy that better fits Morocco's need to respond to exogenous shocks, the challenges posed by the ongoing trade liberalization, and the need to strengthen competitiveness. At the very least, the authorities should avoid any real appreciation of the exchange rate. Increased flexibility in exchange rate policy would need to be supported by the resumption of fiscal consolidation and a tighter wage policy. Greater exchange rate flexibility would also shift the burden of achieving price stability onto monetary policy, which would need to be particularly vigilant, closely monitoring various inflation indicators.

62. The staff encourages the authorities to complement trade liberalization in the context of the AAEU with a reform of the multilateral tariff system. Lowering multilateral tariffs will not only help reduce risks of trade diversions but also position Morocco in a more liberal trade environment, consistent with its status as an emerging market. Morocco would also benefit from improved trade relations with other Maghreb neighbors in the context of the UMA. A mutual reduction in customs tariffs, the harmonization of trade procedures, and the elimination of nontariff barriers would go a long way in developing a large regional market, thereby encouraging foreign investors, in particular European, to locate their plants in the Maghreb countries.

63. Morocco's private banks have continued their strong performance, typically exceeding their prudential requirements. Nevertheless, the staff welcomes BAM's measures to strengthen its supervisory function and to extend its prudential requirements to the specialized public banks. In this respect, the staff encourages prompt action to bring both the CIH and the CNCA to capital adequacy and full provisioning.

64. Important progress was achieved with the liberalization and privatization of the telecommunications sector and the elimination of edible oil subsidies. This momentum needs to be maintained to both attract foreign investment and strengthen private sector development. In particular, the staff supports the authorities in their efforts to improve governance and fight corruption; however, more needs to be accomplished. The further strengthening of the judicial system and the simplification of the regulatory environment would be essential to improve the investment environment. The passage of the long-awaited labor code, which is aimed at greater labor market flexibility, should facilitate the reallocation of labor to the tradable goods sector and would be beneficial to creation of employment.

65. Agriculture in Morocco has strong potential and should contribute to growth instead of dampening it. The disappointing performance of the agricultural sector over the last decade, notwithstanding the higher frequency of droughts, calls for an overhaul of agricultural policies. Phasing out the protection of cereals and sugar, together with liberalizing their prices and eliminating their inefficient subsidies, would reorient incentives toward a cropping pattern better suited to Morocco's climatic conditions. This may require a social safety net to support poorer farmers who would be adversely affected by this measure, but the one-off privatization revenues would be ideal to finance this reform during a transitional period.

66. Sustained growth is key for poverty reduction provided government spending is redirected toward areas which directly impact the poor. The staff strongly supports the authorities' emphasis on primary education and rural infrastructure development. Much remains to be done, however, in health spending which should be channeled more to help the poor by providing greater access to healthcare in rural areas. The introduction of national health insurance, which the authorities are considering, is certainly a step in the right direction.

67. The resumption of fiscal consolidation, the deepening of structural reforms, and the introduction of a flexible exchange rate policy would, no doubt, significantly improve Morocco's growth outlook over the medium term. The staff believes, however, that the authorities could

reasonably aim for a more ambitious growth target—in the range of 6 percent on a sustained basis—to significantly reduce employment and poverty. This would require an upfront improvement in competitiveness by accelerating the liberalization of the trade regime, pursuing an active exchange rate policy and further deepening of structural reforms. The staff believes that this strategy would tap into the vast potential of productivity gains which would emanate from trade dynamics and closer integration with the global economy.

68. The efforts to improve the timeliness and dissemination of statistical data are yielding results. The staff welcomes the authorities request to undertake a ROSC on statistics this year with the objective of identifying the area of improvement needed to subscribe to the SDDS. It also supports the authorities request to participate in the FSAP and to receive an FSSA mission in early 2002.

69. It is recommended that the next Article IV consultation with Morocco be held on the standard 12-month cycle.

Table 1. Morocco: Selected Economic and Financial Indicators, 1996–2001

	1996	1997	1998	1999	Prel 2000	Proj. 2001
	(Percent change, unless otherwise indicated)					
Nominal GDP (in billions of U.S. dollars)	36.6	33.4	35.7	35.0	33.3	34.6
Real GDP growth	12.2	-2.2	6.8	-0.7	0.3	6.0
Real nonagricultural GDP growth	3.6	3.2	3.9	3.0	3.5	3.8
CPI inflation (period average)	3.0	1.0	2.7	0.7	1.9	3.0
	(In percent of GDP)					
Central government finances 1/						
Revenue 2/	24.6	25.4	27.4	27.0	26.3	24.3
Expenditure 3/	28.7	28.4	29.9	31.5	32.4	31.5
Overall balance 4/	-3.4	-3.4	-2.5	-4.3	-6.5	-7.2
Privatization and GSM receipts	1.4	0.3	0.1	3.2	0.0	6.3
Overall balance (including privatization and GSM receipts)	-2.0	-3.1	-2.4	-1.1	-6.4	-0.9
	(Changes as percent of broad money at the beginning of the period)					
Money and credit						
Broad money	4.8	9.0	5.8	10.3	8.4	9.5
Domestic credit	8.2	7.1	6.5	3.4	11.2	6.8
Net credit to government	1.6	2.3	-0.8	-3.9	3.9	-0.7
Credit to private sector	6.6	4.8	7.3	7.3	7.4	7.5
Interest rate (52-week treasury bills, in percent) 5/	9.0	7.5	7.0	4.8	6.3	5.8
	(In billions of U.S. dollars, unless otherwise indicated)					
Balance of payments						
Exports, f.o.b.	6.9	7.0	7.1	7.5	7.4	8.0
Imports, f.o.b.	9.1	8.9	9.5	10.0	10.6	11.0
Net services	-0.3	-0.4	-0.2	0.1	0.2	0.2
Net transfers	2.6	2.2	2.3	2.2	2.4	2.3
Current account	0.0	-0.1	-0.1	-0.2	-0.6	-0.5
(In percent of GDP)	0.1	-0.3	-0.4	-0.5	-1.7	-1.4
Overall balance (deficit -)	0.3	0.6	0.2	1.6	-0.4	1.3
Reserves						
Gross official reserves (end of period) 6/	4.0	4.2	4.6	5.7	4.8	6.0
(In months of imports of goods and nonfactor services)	4.4	4.7	4.8	5.7	4.6	5.5
Debt						
External debt 7/	21.3	19.1	19.3	17.5	16.1	14.9
External debt service ratio (in percent) 7/ 8/ 9/	26.0	27.1	23.9	20.8	20.8	19.3
External debt (in percent of GDP) 7/	58.2	57.1	54.2	50.1	48.3	43.1
Domestic government debt (in percent of GDP) 10/	34.6	38.2	38.3	41.6	43.5	45.7
Total government debt (in percent of GDP) 10/	75.6	78.0	74.6	77.4	77.8	76.6
Use of Fund resources						
Repurchases	32.5	2.3	0.0	0.0	0.0	0.0
Fund credit outstanding	2.3	0.0	0.0	0.0	0.0	0.0
Exchange rate						
Exchange rate (dirham/U.S. dollar, period average)	8.7	9.5	9.6	9.8	10.6	...
Real effective exchange rate (in percent change, appreciation +)	1.7	0.9	2.4	1.0	2.8	...
Terms of trade (in percent change; deterioration -)	1.4	0.1	11.7	-3.4	-10.2	2.5

Sources: Ministry of finance; Bank Al-Maghrib; and IMF staff estimates and projections.

1/ Fiscal years starting in July of that year from 1996 to 1999. Calendar years for 2000 and 2001.

2/ Excluding privatization and GSM license receipts.

3/ Including expenditures of Hassan II Fund.

4/ Including the balance of the special treasury accounts.

5/ As of December for 1996–2000 and March for 2001.

6/ Excluding reserve position at the Fund.

7/ Government and government guaranteed debt.

8/ Debt service ratio in terms of exports of goods and nonfactor services, and private transfers.

9/ Excluding early amortization (debt swaps).

10/ Does not include government guaranteed debt.

Table 2. Morocco: Medium-Term Baseline Scenario, 1991–2006

Calendar years	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
	(In percent)															
Real GDP growth	6.9	-4.0	-1.0	10.4	-6.6	12.2	-2.2	6.8	-0.7	0.8	6.0	4.5	3.9	3.4	3.4	3.5
Real GDI growth 1/	8.4	-3.3	-1.1	8.8	-3.8	12.0	-1.9	10.3	-1.0	-2.2	6.7	5.2	4.5	3.7	3.8	3.8
Real nonagricultural GDP growth	3.6	4.6	-0.4	2.6	2.3	3.6	3.2	3.9	3.0	3.5	3.8	3.8	3.8	3.9	3.9	3.9
Inflation (CPI)	9.0	5.7	5.2	5.1	6.1	3.0	1.0	2.7	0.7	1.9	3.5	3.0	2.7	2.3	2.2	2.2
Export growth in U.S. dollars	-1.7	6.9	-2.1	7.9	17.9	6.5	-1.2	4.8	6.6	-2.3	6.9	8.0	6.6	6.9	7.1	7.0
ICOR 2/	2.8	4.4	7.6	3.7	4.4	3.4	5.4	4.8	10.0	4.9	3.9	4.2	4.3	4.5	4.5	4.5
Real effective exchange rate	102	103	106	108	112	114	115	117	119	122	117	118	119	120	121	121
	(In percent of GDP)															
Gross investment	22.6	23.2	22.5	21.3	20.7	19.6	20.7	22.5	24.2	24.7	24.8	24.4	24.2	24.3	24.2	24.2
Government	2.8	2.7	3.6	3.2	3.7	3.1	3.3	2.8	2.9	3.1	3.0	2.7	2.8	3.0	3.1	3.1
Private 3/ 4/	19.9	20.5	18.9	18.2	17.0	16.5	17.4	19.8	21.2	21.7	21.8	21.7	21.4	21.4	21.2	21.1
National saving	20.9	21.3	20.9	18.6	17.3	19.7	20.4	22.1	23.7	23.0	23.4	24.1	24.1	23.8	23.5	23.2
Government	4.0	5.6	5.8	4.2	2.7	2.6	2.6	1.7	3.4	1.3	0.4	1.0	1.2	1.3	1.3	1.3
Private 3/	16.9	15.7	15.1	14.4	14.5	17.1	17.8	20.4	20.3	21.7	23.1	23.1	22.9	22.6	22.2	21.9
External saving (=current account balance)	-1.7	-1.9	-1.6	-2.8	-3.5	0.1	-0.3	-0.4	-0.5	-1.7	-1.4	-0.4	-0.2	-0.5	-0.7	-1.1
GDP (in billions of U.S. dollars)	27.8	28.5	26.8	30.4	33.0	36.6	33.4	35.7	35.0	33.3	34.6	37.3	40.0	42.6	45.3	48.2
Calendar/fiscal years	1991	1992	1993	1994	1995	1996/ 97	1997/ 98	1998/ 99	1999/ 2000	2000	2001	2002	2003	2004	2005	2006
	(In percent of GDP)															
Fiscal balance 5/	-3.1	-2.2	-3.7	-4.0	-5.6	-3.4	-3.4	-2.5	-4.3	-6.5	-7.2	-6.0	-5.9	-5.8	-5.8	-5.9
Primary balance	2.4	3.4	2.2	1.6	0.4	2.0	1.8	2.7	1.2	-1.2	-2.2	-1.0	-1.1	-1.0	-1.0	-1.0
Borrowing requirement	1.0	2.4	2.6	3.2	3.3	1.9	3.4	3.8	0.5	2.5	4.2	3.5	4.2	4.6	4.9	5.2
Government debt ratio 6/	66.4	79.0	88.7	82.4	83.2	75.6	78.0	74.6	77.4	77.8	76.6	74.7	74.2	74.7	75.5	76.7
Privatization receipts	0.0	0.0	0.9	0.7	0.4	1.4	0.3	0.1	3.2	0.0	6.3	2.4	1.6	1.1	0.8	0.6

Sources: Ministry of finance, Bank Al-Maghrib, and IMF staff estimates and projections.

1/ Real Gross Domestic Income (GDI) = Real GDP adjusted for terms of trade effects.

2/ Ratio of nonagricultural fixed capital formation to change in nonagricultural GDP.

3/ Includes public enterprises.

4/ Includes stockbuilding.

5/ Overall balance, excluding privatization and GSM revenues but including expenditures by the Hassan II Fund.

6/ Domestic and external remunerated central government debt, end of calendar year.

Table 3. Morocco: Medium-Term Adjustment Scenario, 1991–2006 1/

Calendar years	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
	(In percent)															
Real GDP growth	6.9	-4.0	-1.0	10.4	-6.6	12.2	-2.2	6.8	-0.7	0.8	6.0	4.7	4.4	4.3	4.6	4.9
Real GDI growth 2/	8.4	-3.3	-1.1	8.8	-3.8	12.0	-1.9	10.3	-1.0	-2.2	6.7	5.3	4.9	4.6	5.0	5.2
Real nonagricultural GDP growth	3.6	4.6	-0.4	2.6	2.3	3.6	3.2	3.9	3.0	3.5	3.8	4.0	4.3	4.6	4.9	5.2
Inflation (CPI)	9.0	5.7	5.2	5.1	6.1	3.0	1.0	2.7	0.7	1.9	3.5	2.8	2.3	2.0	2.0	2.0
Export growth in U.S. dollars	-1.7	6.9	-2.1	7.9	17.9	6.5	-1.2	4.8	6.6	-2.3	6.9	8.2	7.3	7.6	7.9	8.1
Incremental Capital-Output Ratio 3/	2.8	4.4	7.6	3.7	4.4	3.4	5.4	4.8	10.0	4.9	3.9	4.2	4.4	4.6	4.4	4.3
Real effective exchange rate	102	103	106	108	112	114	115	117	119	122	117	117	117	117	117	117
	(In percent of GDP)															
Gross investment	22.6	23.2	22.5	21.3	20.7	19.6	20.7	22.5	24.2	24.7	24.8	24.9	25.2	25.7	26.3	27.0
Government	2.8	2.7	3.6	3.2	3.7	3.1	3.3	2.8	2.9	3.1	3.0	2.8	2.9	3.1	3.3	3.5
Private 4/ 5/	19.9	20.5	18.9	18.2	17.0	16.5	17.4	19.8	21.2	21.7	21.8	22.1	22.3	22.6	23.1	23.4
National saving	20.9	21.3	20.9	18.6	17.3	19.7	20.4	22.1	23.7	23.0	23.4	24.5	25.2	25.3	25.6	25.7
Government	4.0	5.6	5.8	4.2	2.7	2.6	2.6	1.7	3.4	1.3	0.4	2.2	3.0	3.8	4.5	5.3
Private 4/	16.9	15.7	15.1	14.4	14.5	17.1	17.8	20.4	20.3	21.7	23.1	22.3	22.2	21.6	21.2	20.5
External saving (=current account balance)	-1.7	-1.9	-1.6	-2.8	-3.5	0.1	-0.3	-0.4	-0.5	-1.7	-1.4	-0.4	-0.1	-0.4	-0.7	-1.2
GDP (in billions of U.S. dollars)	27.8	28.5	26.8	30.4	33.0	36.6	33.4	35.7	35.0	33.3	34.6	36.9	39.4	42.1	45.0	48.2
Calendar/fiscal years	1991	1992	1993	1994	1995	1996/ 97	1997/ 98	1998/ 99	1999/ 2000	2000	2001	2002	2003	2004	2005	2006
	(In percent of GDP)															
Fiscal balance 6/	-3.1	-2.2	-3.7	-4.0	-5.6	-3.4	-3.4	-2.5	-4.3	-6.5	-7.2	-5.0	-4.3	-3.6	-3.0	-2.3
Primary balance	2.4	3.4	2.2	1.6	0.4	2.0	1.8	2.7	1.2	-1.2	-2.2	-0.1	0.4	1.0	1.5	2.0
Borrowing requirement	1.0	2.4	2.6	3.2	3.3	1.9	3.4	3.8	0.5	2.5	4.2	2.5	2.7	2.4	2.1	1.7
Government debt ratio 7/	66.4	79.0	88.7	82.4	83.2	75.6	78.0	74.6	77.4	77.8	76.6	73.7	71.7	69.8	67.5	64.8
Privatization receipts	0.0	0.0	0.9	0.7	0.4	1.4	0.3	0.1	3.2	0.0	6.3	2.4	1.6	1.1	0.8	0.6

Sources: Ministry of finance, Bank Al-Maghrib, and IMF staff estimates and projections.

1/ This scenario assumes fiscal consolidation, accelerated structural reforms, and no further appreciation of the real effective exchange rate.

2/ Real Gross Domestic Income (GDI) = Real GDP adjusted for terms of trade effects.

3/ Ratio of nonagricultural fixed capital formation to change in nonagricultural GDP.

4/ Includes public enterprises.

5/ Includes stockbuilding.

6/ Overall balance, excluding privatization and GSM revenues but including expenditures by the Hassan II Fund.

7/ Domestic and external remunerated central government debt, end of calendar year.

Table 4. Morocco: Public Finance, 1996–2001

	1996/97	1997/98	1998/99	1999/00	July/Dec 2000	Prel 2000 1/	Budget Law 2001	Proj 2001
	(In billions of dirhams)							
Revenue 2/	78.6	84.0	93.8	94.2	43.3	92.9	93.7	94.3
Tax revenue 2/	71.3	76.5	84.4	86.2	40.9	85.5	85.6	86.2
Nontax revenue	7.3	7.5	9.4	8.0	2.5	7.4	8.1	8.1
Noninterest expenditure	74.1	76.6	84.9	90.9	51.2	96.0	105.4	102.8
Wages	34.2	37.6	40.3	42.1	21.2	42.0	48.9	48.9
Food subsidies 3/	5.4	6.1	6.1	8.2	4.3	9.4	5.0	4.2
Other current spending	13.0	14.8	16.5	17.3	8.7	17.3	20.3	20.3
Transfers to local governments 4/	5.4	5.3	5.7	6.3	3.3	6.4	6.5	6.6
Capital expenditures 5/	16.5	16.0	17.4	17.5	13.6	21.2	24.7	22.8
Of which: Hassan II Fund	...	...	...	0.3	1.7	1.9	4.9	3.0
Net lending 6/	-0.4	-3.1	-1.2	-0.5	0.0	-0.3	0.0	0.0
Balance of special treasury accounts	1.9	-1.4	0.4	0.8	0.9	-1.0	0.0	0.0
Primary balance	6.4	5.9	9.3	4.0	-6.9	-4.2	-11.7	-8.4
Interest	17.3	17.3	17.7	18.9	9.6	18.6	19.2	19.4
Overall budget balance (commitment basis)	-10.9	-11.3	-8.5	-14.8	-16.6	-22.8	-30.9	-27.8
Change in arrears	0.2	-1.4	-5.0	1.5	11.9	13.8	-2.2	-13.2
Overall budget balance (cash basis)	-10.7	-12.7	-13.5	-13.3	-4.7	-9.0	-33.1	-41.0
Privatization and GSM revenues	4.6	1.2	0.4	11.1	0.0	0.0	21.3	24.3
Financing	6.1	11.6	13.1	2.2	4.6	9.0	11.8	16.7
Domestic financing	10.7	17.8	18.3	9.2	6.9	15.3	18.1	23.2
Bank	1.0	3.3	-1.4	-3.4	6.8	9.7	2.0	-2.1
Nonbank	9.8	14.5	19.7	12.6	0.1	5.6	16.1	25.3
External financing 7/	-4.6	-6.2	-5.2	-7.0	-2.2	-6.3	-6.2	-6.5
	(In percent of GDP)							
Revenue 2/	24.6	25.4	27.4	27.0	24.5	26.3	23.9	24.3
Tax revenue 2/	22.4	23.2	24.6	24.7	23.1	24.2	21.8	22.2
Nontax revenue	2.3	2.3	2.8	2.3	1.4	2.1	2.1	2.1
Noninterest expenditure	23.2	23.2	24.8	26.1	29.0	27.2	26.9	26.5
Of which:								
Wages	10.7	11.4	11.8	12.1	12.0	11.9	12.5	12.6
Food subsidies 3/	1.7	1.8	1.8	2.4	2.4	2.7	1.3	1.1
Other current spending	4.1	4.5	4.8	5.0	4.9	4.9	5.2	5.2
Transfers to local governments 4/	1.7	1.6	1.7	1.8	1.9	1.8	1.7	1.7
Capital expenditures 5/	5.2	4.8	5.1	5.0	7.7	6.0	6.3	5.9
Of which: Hassan II Fund	...	...	...	0.1	0.9	0.5	1.3	0.8
Net lending 6/	-0.1	-0.9	-0.3	-0.2	0.0	-0.1	0.0	0.0
Balance of special treasury accounts	0.6	-0.4	0.1	0.2	0.5	-0.3	0.0	0.0
Primary balance	2.0	1.8	2.7	1.2	-3.9	-1.2	-3.0	-2.2
Interest	5.4	5.2	5.2	5.4	5.5	5.3	4.9	5.0
Overall budget balance (commitment basis)	-3.4	-3.4	-2.5	-4.3	-9.4	-6.5	-7.9	-7.2
Change in arrears	0.1	-0.4	-1.5	0.4	6.7	3.9	-0.6	-3.4
Overall budget balance (cash basis)	-3.3	-3.9	-3.9	-3.8	-2.6	-2.5	-8.4	-10.6
Privatization and GSM revenues	1.4	0.3	0.1	3.2	0.0	0.0	5.4	6.3
Financing 7/	1.9	3.5	3.8	0.6	2.6	2.5	3.0	4.3
Memorandum item:								
Structural fiscal balance 8/	-4.0	-4.1	-4.4	-4.2	...	-4.5	...	-4.9
GDP in billions of dirhams 9/	318.8	330.5	342.8	348.3	176.7	353.4	392.3	387.8

Sources: Ministry of economy and finance; and IMF staff estimates.

1/ Sum of realizations for the first half of the 1999/2000 budget and for the second half of 2000.

2/ Includes tariffs earmarked for food subsidies (*équivalent tarifaires*), and revenues of the Fonds routier, but excludes GSM licensereceipts in 1999/2000.

3/ Includes food subsidies financed from earmarked tariffs (*équivalents tarifaires*). It also includes, for 1999/2000 and July/December, petroleum product subsidies, which were financed by arrears accumulation. Their amount was estimated on the basis of the difference between domestic and international petroleum prices.

4/ Corresponds to 30 percent of VAT revenue.

5/ Budgetary capital expenditures and Fonds routier. Excluding investment spending by the Hassan II Fund.

6/ In 1997/98, it includes net repayment of DH 2.6 billion by ONE to the state.

7/ Includes selected grants.

8/ Cyclically adjusted overall budget balance adjusted for one-off revenues and expenditures.

9/ Calendar years in 2000 and 2001, fiscal years otherwise.

Table 5. Morocco: Monetary Survey, 1996–2001

	1996	1997	1998	1999	Actual 2000	Proj. 2001
(In billions of Moroccan dirhams, end of period)						
Net foreign assets	35.5	41.1	43.4	59.6	55.3	70.9
Domestic credit	230.7	245.4	260.0	268.2	297.9	317.4
Net credit to the government	88.7	93.4	91.5	82.2	92.4	90.5
Credit to the economy	142.1	152.0	168.5	185.9	205.4	226.9
Money and quasi money	207.7	226.4	239.6	264.3	286.6	313.9
Money	150.4	162.3	174.5	194.9	230.1	206.1
Currency outside banks	46.4	48.7	50.6	56.7	58.2	63.7
Demand deposits	103.9	113.6	123.8	138.2	152.1	166.4
Quasi money	57.3	64.1	65.1	69.4	76.3	83.9
Other liabilities, net	58.6	60.1	63.8	63.5	66.5	74.4
(Change in percent, from preceding year)						
Domestic credit	7.6	6.4	6.0	3.1	11.1	6.6
Net credit to the government	3.8	5.3	-2.0	-10.1	12.4	-2.1
Credit to the economy	10.1	7.0	10.8	10.3	10.5	10.5
Money and quasi money	4.8	9.0	5.8	10.3	8.4	9.5
(Change over 12 months, as percent of broad money at the beginning of the period)						
Net foreign assets	1.2	2.7	1.0	6.8	-1.6	5.5
Domestic credit	8.2	7.1	6.5	3.4	11.2	6.8
Net credit to the government	1.6	2.3	-0.8	-3.9	3.9	-0.7
Credit to the economy	6.6	4.8	7.3	7.3	7.4	7.5
Other assets net	-4.7	-0.7	-1.6	0.1	-1.2	-2.7
Memorandum items						
Velocity (GDP/M3)	1.6	1.4	1.4	1.3	1.2	1.2
Velocity (nonagricultural GDP/M3)	1.2	1.2	1.2	1.1	1.1	1.1
Money multiplier	3.5	3.6	3.6	3.4	3.6	3.6
Credit to economy/GDP	40.0	50.0	48.6	54.2	58.2	64.3
Credit to economy/nonagricultural GDP	60.0	60.0	60.0	63.6	66.5	73.4

Sources: Bank Al-Maghrib; and IMF staff estimates.

Table 6. Morocco: Balance of Payments, 1996–2001

(In millions of U.S. dollars, unless otherwise indicated)

	1996	1997	1998	1999	Prel. 2000	Proj. 2001
Trade balance	-2,193	-1,864	-2,323	-2,448	-3,151	-3,002
Exports, f.o.b.	6,886	7,039	7,143	7,508	7,414	8,016
Phosphates and derived products	1,256	1,367	1,300	1,361	1,250	1,457
Imports, f.o.b.	-9,080	-8,903	-9,467	-9,957	-10,565	-11,018
Energy	1,285	1,296	922	1,326	2,041	1,951
Services balance	-348	-428	-160	124	183	194
Nonfactor services	961	747	864	1,112	1,016	1,042
Tourism receipts	1,675	1,446	1,744	1,949	2,013	2,077
Net investment income	-1,309	-1,175	-1,023	-988	-833	-848
Private transfers (net)	2,527	2,158	2,293	2,144	2,313	2,286
Official grants (net)	50	48	52	10	94	48
Current account	35	-87	-138	-170	-562	-474
Capital account 1/	99	23	52	259	1	-4
Financial account	158	617	334	1,549	146	1,815
Direct investment	327	1,071	313	653	103	2,255
Other private (including errors and omissions)	111	521	429	1,411	906	209
Public medium- and long-term loans (net)	-280	-975	-408	-515	-862	-648
Disbursements	1,632	1,017	1,543	1,501	833	1,043
Amortization	-1,912	-1,992	-1,951	-2,016	-1,695	-1,691
Reserve asset accumulation (-increase)	-292	-553	-247	-1639	415	-1337
Memorandum items						
Trade balance (in percent of GDP)	-6.0	-5.6	-6.5	-7.0	-9.5	-8.7
Current account balance (in percent of GDP)	0.1	-0.3	-0.4	-0.5	-1.7	-1.4
Excluding official grants (in percent of GDP)	0.0	-0.4	-0.5	-0.5	-2.0	-1.5
Gross official reserves 2/	3,965	4,152	4,600	5,700	4,796	5,987
(In months of imports of goods and nonfactor services)	4.4	4.7	4.8	5.7	4.6	5.5
Debt service as percentage of export of goods, nonfactor services and private transfers 3/ 4/	26.0	27.1	23.9	20.8	20.8	19.3
External public and publically guaranteed debt (in percent of GDP)	58.2	57.1	54.2	50.1	48.3	43.1

Sources: Ministry of finance; Office des changes; and IMF staff estimates and projections.

1/ Includes the grant element of debt swap operations with France and Spain.

2/ Excluding the reserve position in the Fund.

3/ Public and publically guaranteed debt.

4/ Excluding early amortization on account of debt swaps.

Table 7. Morocco: Balance of Payments, Medium-Term Baseline Projections, 2000–06

(In millions of U.S. dollars)

	<u>Prel.</u>	<u>Projections</u>					
	2000	2001	2002	2003	2004	2005	2006
Trade balance	-3,151	-3,002	-2,830	-2,956	-3,257	-3,549	-3,897
Exports, f.o.b.	7,414	8,016	8,672	9,225	9,852	10,553	11,298
Phosphates and derived products	1,250	1,457	1,587	1,690	1,801	1,939	2,087
Imports, f.o.b.	-10,565	-11,018	-11,502	-12,180	-13,109	-14,102	-15,195
Energy	2,041	1,951	1,819	1,710	1,786	1,866	1,975
Services balance	183	194	254	351	399	480	531
Nonfactor services	1,016	1,042	1,145	1,225	1,284	1,344	1,400
Tourism receipts	2,013	2,077	2,234	2,405	2,577	2,759	2,951
Net investment income	-833	-848	-891	-873	-884	-864	-869
Private transfers (net)	2,313	2,286	2,393	2,492	2,593	2,697	2,802
Official grants (net)	94	48	48	48	49	49	49
Current account	-562	-474	-136	-65	-216	-324	-515
Capital account 1/	1	-4	-4	-4	-5	-5	-5
Financial account	146	1,815	377	257	317	354	499
Direct investment	103	2,255	1,144	1,057	907	846	785
Other private (including errors and omissions)	906	209	178	192	194	196	197
Public medium- and long-term loans (net)	-862	-648	-946	-993	-783	-687	-483
Disbursements	833	1,043	715	719	904	1,000	1,097
Amortization	-1,695	-1,691	-1,661	-1,712	-1,687	-1,687	-1,581
Reserve asset accumulation (-increase)	415	-1337	-237	-188	-97	-26	20
Memorandum items							
Trade balance (in percent of GDP)	-9.5	-8.7	-7.6	-7.4	-7.6	-7.8	-8.1
Current account balance (in percent of GDP)	-1.7	-1.4	-0.4	-0.2	-0.5	-0.7	-1.1
Excluding official grants (in percent of GDP)	-2.0	-1.5	-0.5	-0.3	-0.6	-0.8	-1.2
Gross official reserves 2/	4,796	5,987	6,243	6,464	6,595	6,655	6,668
(In months of imports of goods and nonfactor services)	4.6	5.5	5.5	5.3	5.1	4.7	4.4
Debt service as percentage of export of goods, nonfactor services and private transfers 3/ 4/	20.8	19.3	17.3	16.1	14.7	13.4	11.8
External public and publically guaranteed debt (in percent of GDP)	48.3	43.1	37.5	32.7	29.0	25.9	23.5

Sources: Ministry of finance; Office des changes; and IMF staff estimates and projections.

1/ Includes the grant element of debt swap operations with France and Spain.

2/ Excluding the reserve position in the Fund, including valuation adjustments.

3/ Public and publically guaranteed debt.

4/ Excluding early amortization on account of debt swaps.

Table 8. Morocco: Basic Social and Demographic Indicators, 1971–2000

	1971	1987	1993	1997	1998	1999	2000
	(In millions, unless otherwise specified)						
Population characteristics							
Total population	15.4	22.7	25.6	27.3	27.8	28.2	28.7
Rural population	10.0	12.2	12.6	12.8	12.8	12.8	12.9
Population under 15 year of age	7.0	9.6	9.8	9.6	9.3	9.3	9.3
Birth rate (per 1,000)	41.0	31.4	27.3	23.2	22.8	22.4	21.9
Death rate (per 1,000)	17.4	7.4	7.0	6.3	6.2	6.1	5.9
Life expectancy	52.4	65.0	67.3	68.8	69.2	69.5	...
Population growth	2.8	2.4	2.0	1.7	1.7	1.7	1.6
Urbanization rate	35.1	46.0	50.4	53.2	53.8	54.5	55.2
Number of children per woman	7.4	4.5	4.1	3.1	3.0	2.9	...
Health, food, and nutrition							
Infant mortality (per 1,000)	125.2	82.0	65.6	51.0	...	47.8	...
Persons per physician (in thousands)	13.7	4.4	3.1	2.8	2.6	2.4	2.3
Education							
Literacy rate (in percent)	14.0	34.0	45.0	49.0	51.7	51.7	...
Primary enrollment (in percent)	52.5	71.7	88.3	88.6	...	...	...
Secondary enrollment (in percent)	12.6	38.0	44.9	49.9	...	...	...
Pupils per teacher in primary schools	35	27	28	28	28	29	...
Pupils per teacher in secondary schools	20	20	17	19	18	19	...
	(In percent, unless otherwise specified)						
Urban employment							
Total employment (in percent of urban population)	23.6	26.7	27.7	28.5	27.3	26.4	26.4
Female employment (in percent of urban population)	...	6.6	6.0	6.8	6.1	6.0	6.0
Unemployment rate	2.3	14.4	15.9	16.9	19.1	22.0	21.5
Young unemployment rate (15–24 years)	...	27.1	30.2	29.9	34.7	37.8	37.6
Salary and income							
GDP per capita (1980 dirhams)	3,132	4,042	4,292	4,548	4,776	4,665	4,628
GDP per capita (current U.S. dollars)	275	819	1,027	1,224	1,284	1,239	1,159
Minimum wage (in 1980 dirhams per hour) 1/	2.17	2.21	2.72	2.84	2.76	2.74	2.82
	(In percent of GDP)						
Social investment							
Government total expenditure on education 2/	...	4.8	5.9	5.4	5.8	6.0	6.3
Government total expenditure on health 2/	...	0.8	0.9	1.0	1.1	1.4	1.4

Sources: Moroccan authorities; World Bank; and IMF staff estimates.

1/ Minimum wage in the nonagricultural sector.

2/ Between 1996 and 1999, fiscal year beginning in July of the indicated year.

Table 9. Morocco: Indicators of External and Banking Sector Vulnerability, 1996–2000

(In percent of GDP, unless otherwise indicated)

	1996	1997	1998	1999	2000
Financial indicators					
Central government debt (remunerated)	75.6	78.0	74.6	77.4	77.8
Broad money (percent change, 12-month basis)	4.8	9.0	5.8	10.3	8.4
Private sector credit (percent change, 12-month basis)	10.1	7.0	10.8	10.3	10.5
52-week treasury-bill yield (nominal)	9.0	7.5	7.0	6.0	5.7
52-week treasury-bill yield (deflated by 12-month CPI)	5.8	6.4	4.1	5.3	3.7
Overnight interbank rate (annual average)	7.3	6.7	6.3	5.6	5.4
External indicators					
Exports (percent change, in U.S. dollars)	0.2	2.2	1.5	5.1	-1.3
Imports (percent change, in U.S. dollars)	-2.9	-1.9	6.3	5.2	6.1
Terms of trade (percent change)	1.4	0.1	11.7	-3.4	-10.2
Current account balance	0.1	-0.3	-0.4	-0.5	-1.7
Capital and financial account balance	0.7	1.9	1.1	5.2	0.4
<i>Of which:</i>					
Inward portfolio investment (debt securities, etc.)	0.4	0.2	0.2	0.0	0.1
Inward foreign direct investment	0.8	3.3	1.1	2.7	0.7
Gross official reserves (in billions of U.S. dollars; end of period)	4.0	4.2	4.6	5.7	4.8
Central bank foreign liabilities (in billions of U.S. dollars)	0.1	0.1	0.1	0.1	0.1
Foreign assets of the banking sector (in billions of U.S. dollars)	0.3	0.4	0.5	0.5	0.6
Foreign liabilities of the banking sector (in billions of U.S. dollars)	0.3	0.4	0.5	0.5	0.4
Official reserves in months of imports GNFS	4.4	4.7	4.8	5.7	4.6
Broad money to reserves (in percent)	631	590	590	476	603
Total gross external debt/GDP	59.3	60.1	57.6	56.4	54.0
<i>Of which: central government debt/GDP</i>	40.4	40.0	38.0	36.4	33.6
Total gross external debt to exports GNFS (in percent)	227.8	215.1	198.6	191.1	167.9
Total short term external debt to reserves (percent) 1/	63.6	64.7	59.8	50.5	57.5
External gross interest payments to exports GNFS (in percent)	15.6	14.2	12.4	11.4	11.1
External amortization payments to exports GNFS (in percent)	19.9	20.9	19.6	19.0	16.3
Exchange rate (per U.S. dollars, period average)	8.72	9.53	9.60	9.80	10.63
REER appreciation (+) (annual average)	1.7	0.9	2.4	1.0	2.8
Banking sector indicators					
Solvability ratio 2/	11.3	11.2	12.6	12.1	13.4
Share of foreign currency deposits in total deposits (in percent)	0.6	0.7	0.6	0.7	0.2
Share of construction and hotel credit in total credit (in percent)	6.7	7.4	8.1	7.8	6.9
Financial market indicators					
Stock market index (IGB)	447	668	804	777	658
Stock market transactions	6.4	11.1	17.0	28.2	10.9
Moody's rating for foreign currency bonds and note	n.a.	n.a.	Ba1	Ba1	Ba1

Sources: Bank Al-Maghrib; treasury; Office des changes; and IMF staff estimates.

1/ Includes long- and medium-term debt coming due in the next year.

2/ In 2000, excluding Crédit Immobilier et Hôtelier (CIH) and Caisse Nationale de Crédit Agricole (CNCA).

MOROCCO—FUND RELATIONS

(As of March 31, 2001)

Membership Status: Joined 04/25/1958; Article VIII

General Resources Account:	SDR Million	Percent of Quota
Quota	588.20	100.0
Fund Holdings of Currency	517.76	88.0
Reserve position in Fund	70.44	12.0

SDR Department:	SDR Million	Percent of Allocation
Net cumulative allocation	85.69	100.0
Holdings	89.33	104.3

Outstanding Purchases and Loans: None**Financial Arrangements:**

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-by	01/31/1992	03/31/1993	91.98	18.40
Stand-by	07/20/1990	03/31/1991	100.00	48.00
Stand-by	08/30/1988	12/31/1989	210.00	210.00

Projected Obligations to Fund: None**Exchange System**

Morocco maintains an exchange system that is free of restrictions on the making of payments and transfers on current international transactions. However, Morocco maintains restrictions for security reasons against Iraq and the Federal Republic of Yugoslavia (Serbia and Montenegro), pursuant to relevant U.N. Security Council resolutions.

The exchange rate of the Moroccan dirham is pegged to a basket of currencies representing Morocco's principal trading partners. Bank Al-Maghrib (BAM) intervenes in the foreign

exchange market to maintain this exchange rate. It fixes daily rates for the rated currencies on the basis of variations in the value of the basket. Rates for most currencies quoted in Morocco are established on the basis of the daily dirham-euro rate and the cross rates for those currencies in relation to the euro in the international exchange markets. On May 21, 2001, the SDR-dirham exchange rate was SDR 1=DH 14.74. After remaining constant in relation to the basket from May 1990 to April 2001, the dirham exchange rate was devalued by 5 percent on April 25. At the same time the composition of the BAM's reference currency basket was changed so as to reflect a shift in trade geographical patterns consistent with the association agreement with the European Union.

Article IV consultation

Morocco is on the 12-month consultation cycle. The last consultation discussions took place in Rabat during February 22–March 2, 2000 and were concluded by the Executive Board on June 9, 2000.

Technical assistance

March 7–21, 1996: STA—advising on improving trade statistics

June 30–July 3, 1996: FAD—advising on ways to improve tax administration

October 17–November 2, 1996: FAD—advising the authorities on the implementation of a modernization program for custom and direct taxes administration

February 25–March 13, 1997: FAD—examining the impact of fiscal and tariffs reforms

January 12–23, 1998: FAD—advising the authorities on improving custom procedures and controls

March 19–April 2, 1998: STA—multisector assessment of statistical systems in preparation of an action plan toward Special Data Dissemination Standard subscription

April 12–24, 1998: FAD—advising on custom computerization

September 9–21, 1998: MAE—advising on domestic debt management

November 9–22, 1998: FAD—reviewing progress in reforming the custom organization and its procedures

December 11–22, 1998: STA—advising on improving national account statistics

February 2–17, 1999: STA—advising on improving general government and monetary statistics

February 16–29, 2000: STA—following up on government finance statistics improvement

November 7–22, 2000: FAD—advising the authorities on developing a modernization program for tax policy and tax administration

Resident representative: None

MOROCCO—FINANCIAL RELATIONS WITH THE WORLD BANK GROUP

(In millions of U.S. dollars)

Loans/Credits Summary¹

	IBRD	IDA	Total
Original principal	8,626,800,001	53,458,951	8,680,258,952
Cancellations	1,156,418,055	8,297,887	1,164,715,942
Disbursed	6,890,940,359	45,161,065	6,936,101,424
Undisbursed	459,738,555	0	459,738,555
Repaid	3,715,938,618	19,163,900	3,735,147,518
Due	3,077,902,866	25,997,164	3,103,900,030
Exchange adjustment	-391,340,202	0	-391,340,202
Borrower's obligation	2,686,562,660	25,997,164	2,712,559,824
Sold third party	20,113,796	0	20,113,796
Repaid third party	20,113,796	0	20,113,796
Due third party	0	0	0

Net Lending by the World Bank (fiscal year), 1998–2001

	1998	1999	2000	2001 ²
Commitments	384.0 ³	440.0	7.5	97.6
Projects	284.0	89.0	7.5	32.6
Policy	100.0	351.0	0.0	65.0
Disbursements	260.5	401.1	106.8	121.0
Projects	161.6	100.1	106.8	71.0
Policy	98.9	301.0	0.0	50.0
PRSL	0.0	250.0	0.0	0.0
Financial sector	98.9	0.0	0.0	0.0
Telecommunications	0.0	51.0	0.0	50.0
Debt service IDA	1.6	1.7	1.6	1.6
Debt service IBRD	518.5	513.1	532.4	578.0
Interest ⁴	218.2	215.8	200.4	231.3
Principal	300.3	297.3	332.0	347.0
Net transfers	-258.0	-112.0	-425.6	-457.0

¹ As of April 2001.

² Data for FY 2001 are projected. Debt service estimated on a calendar year basis.

³ It includes US\$184 million for guarantee on Jorf Lasfar electricity project.

⁴ Includes charges.

Country assistance strategy

The Executive Board of the World Bank approved a new three-year Country Assistance Strategy (CAS) on May 31, 2001. The CAS proposes a “base core” lending program that would remain at about the same level as the last five years, US\$250 million per year, which would be divided into a core program (focussing on poverty, unemployment, and human development) and a sector reform support component. The core component would comprise three operations totaling US\$150 million per year. The sector program would support priority reforms through analytical and advisory work.

The CAS also envisions a “high case” scenario that would respond to the implementation by the government of a package of macroeconomic, structural, and social reforms having the potential to accelerate economic growth and the pace of poverty reduction. Under such a scenario, World Bank financial assistance could reach up to US\$450 million per year.

Policy loans

A two-tranche US\$101 million **Telecommunication Sector Adjustment Loan** has been negotiated in late 1998. This loan supports the liberalization of the telecommunications sector in Morocco and, in particular, the concession of a second GSM license for mobile phone operation. The Executive Board approved the loan on May 6, 1999.

A single-tranche **Policy Reform Support Loan (PRSL)** for US\$250 million was approved by the Executive Board on June 1, 1999. Parallel financing of US\$200 million by the African Development Bank had already been approved. The PRSL is to support government’s commitment to establishing and maintaining a sound macroeconomic framework and to implementing a broad reform program covering public sector reform, private sector development, and poverty reduction and human resource development.

A single-tranche US\$65 million **Information Infrastructure Development Sector Loan (IISDL)** was presented to the Executive Board on May 31, 2001 along with the Morocco CAS. The loan aims to support the government’s efforts that build on the legal and institutional foundations already established, and aim to: (a) develop a modern Information Infrastructure Sector throughout the country; (b) expand telecommunications, postal, and information technology services beyond the market to marginal urban and rural populations; and (c) fosters the use of IT applications to improve private sector competitiveness, public sector efficiency and provision of social services to citizens by either public or private providers. In this context, the operation is based on three main sets of reforms: (a) the privatization of Itissalat Al-Maghrib (IAM) through a transparent and competitive bidding, and with license terms and conditions (cahier des charges of IAM) that reflect the government’s sector strategy; (b) the formulation and implementation of an ambitious strategy for the use and development of information technologies; and (c) the formulation of a national strategy for the postal sector, including the financial services provided through the postal network

Project loans

During FY 1998, the following loans were approved: a municipal finance project (US\$70 million), a rural water supply project (US\$10 million), and a water resource project (US\$20 million).

During FY 1999, the following loans were approved: a Fez rehabilitation project (US\$14 million), a health management project (US\$66 million), a Lakhdar watershed management project (US\$4 million), and a pilot fisheries project (US\$5 million).

During FY 2000, the following loans were approved: a legal and judicial development project (US\$5.3 million), and a Sustainable Coastal Tourism Development project (US\$2.2 million).

In the current FY 2001, the Irrigation Based Community Development project (US\$32.6 million), and the Information Infrastructure Development Sector project (US\$65 million) are scheduled to go to the Executive Board.

Technical assistance

The IBRD has provided extensive technical assistance to Morocco through its various lending operations for projects, as well as through its sectoral adjustment loans. Small-scale technical assistance on specific issues has been provided since 1990 with the support of Institutional Development Fund grants.

In addition, at the authorities' request, the World Bank has prepared a number of policy notes on sectoral issues such as education, administration and the financial sector, and related long-term prospects.

MOROCCO—STATISTICAL ISSUES

Available economic and financial data have been provided to the staff on a regular basis and most of these data are also published or made available on publicly accessible web sites. In 1998, the Statistics Office prepared a medium-term strategy for the development of national statistics. A framework law on statistics, providing additional budgetary allocations, was also approved. Following the Fund's multisector statistics mission in March 1998, the authorities started implementing an action plan for the upgrading of the country's statistical system and have received Fund technical assistance on real sector, monetary, and public finance statistics. The authorities intend to subscribe to the Special Data Dissemination Standards. They have also agreed to participate in the preparation of the data module for the Reports on the Observance of Standards and Codes.

Real sector

The ministry of planning is also working on rebasing the national accounts from 1980 to 1998 and on bringing them in conformity with the United Nations revised system of national accounts. The ministry plans to finalize the 1998 national accounts in 2002 (the flow-of-funds and input-output tables would be released in March), the 1999 and 2000 national accounts in 2003, and to abandon definitely the old base in 2005. The progress on rebasing the producer price index and wholesale price index has been slow. A complete revision of the consumer price index will only be worthwhile once the results of the new household budget survey are available.

Government finance

Central government finance data are generally available to MED with one two-month lag. The latest *Government Finance Statistics Yearbook (GFSY)* data reported by Morocco for publication in *GFSY* are for 1999; their coverage is limited to the budget of the central government, the Moroccan pension fund, the national social security fund, and partial information on the extrabudgetary funds. Data on local governments are still not available. Monthly data are reported to STA by Bank Al-Maghrib for publication in *International Finance Statistics (IFS)*. The monthly data cover the general budget, annexed budgets, and special accounts. A STA technical assistance mission was in Rabat in February 1999 to assist the government in establishing appropriate consolidation procedures for a presentation of general government data. The mission noted areas for further improvement in the compilation of both central and local government statistics. A follow-up mission took place in February 2000 to pursue this effort. A timetable for timely and regular reporting of consolidated central government data for publication in the *GFSY* and *IFS* and the production of statistics for the various entities of local government was agreed with the authorities. The ministry of planning is currently working on a survey of central and local government investment.

Monetary accounts

Monetary data were revised in 1998 and as a consequence reporting to STA was disrupted. However, with STA technical assistance (February 1999), *IFS* publication of Moroccan monetary statistics resumed in July 1999. A new accounting system for banks that is more consistent with international standards has been implemented since January 2000.

Bank Al-Maghrib provides weekly data on the level of its official reserve assets. Monthly data on their different components and on its other foreign currency assets are provided during Fund missions.

External sector

Data on public external debt are provided by the ministry of finance during Fund missions. They are broken down by maturity and by type of creditors. Data are also provided on future debt service payments due on the outstanding public debt. However, the recording of private foreign debt, in particular short-term debt, needs to be improved.

Since May 1998, the Office des changes has been publishing monthly statistics on trade, tourism, private transfers, and incoming foreign direct investment on its new Internet site. These data are available with a lag of between two and three months. Improvements of data on transport and insurance as well as tourism are still underway. Balance of payments statistics are now reported in accordance with the fifth edition of the *Balance of Payments Manual*.

Morocco: Core Statistical Indicators

As of May 31, 2001

	Exchange Rate	International Reserves	Reserve/ Base Money	Central Bank Balance Sheet	Broad Money	Interest Rate	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Government Balance	GDP/ GNP	External Public Debt
Date of latest observation	05/24/01	05/18/01	03/31/01	03/31/01	03/31/01	05/15/01	03/31/01	03/31/01	12/31/00	02/28/01	2000	Dec 2000
Date received	05/30/01	05/24/01	05/31/01	05/31/01	05/31/01	05/15/01	05/18/01	05/15/01	02/15/01	03/05/01	03/12/01	03/12/01
Frequency of data	D	W	M	M	M	M	M	M	Q	M	Y	Semi-annual
Frequency of reporting	W	W	M	M	M	M	M	M	Q	M	Y	Semi-annual
Source of data	CB/Office des changes	CB	CB	CB	CB	CB Press	Statistical Office	MoF/ Office des changes	MoF/ Office des changes	MoF/ Direction du trésor	Statistical Office	MoF/ Direction du trésor
Mode of reporting	Internet/ fax/mail	Fax/mail	Fax/mail	Fax/mail	Fax/mail	Fax/mail	Internet	Internet/ fax/mail	Fax/mail	Internet	Mission/ official publications	Mission
Confidentiality	U	U	U	U	U	U	U	U	U	U	U	U
Frequency of publication	W	M	M	M	M	M	M	M	Q	M	Q	A

D = daily; W = weekly; M = monthly; Q = quarterly; CB = central bank; MoF = ministry of finance; U = unrestricted.



INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL
RELATIONS
DEPARTMENT

Public Information Notice (PIN) No. 01/80
FOR IMMEDIATE RELEASE
August 2, 2001

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes 2001 Article IV Consultation with Morocco

On July, 11, 2001, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Morocco.¹

Background

Due to two successive years of severe drought, Morocco experienced in 2000 a second year of economic stagnation. As agricultural production contracted by 17 percent, GDP real growth was limited to 0.3 percent (after -0.7 percent in 1999). Nonagricultural GDP growth declined slightly, from 3.0 percent in 1999 to 2.8 percent in 2000. The most dynamic sectors were construction and public works (5.7 percent), and transport and communications (5.2 percent). Major projects in electronics, tourism, and motor vehicle components were launched with foreign direct investment. On the demand side, the most dynamic components were private consumption and exports.

Consumer price inflation remained subdued in 2000 at about 2 percent year-on-year. Inflation data through May 2001 point to continued price stability.

External reserves amounted to US\$4.8 billion at end-2000 and are expected to reach at least US\$6 billion (the equivalent of 5.5 months of imports) by end-2001, as a result of the privatization proceeds of Maroc Telecom. The external current account deficit widened to 1.5 percent of GDP in 2000 from 0.5 percent in 1999 because of increased agricultural imports, large imports of telecommunication equipment goods, and a substantial increase in oil import prices coupled with a decline in phosphate exports prices. During the first four months of 2001,

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. This PIN summarizes the views of the Executive Board as expressed during the July, 11, 2001 Executive Board discussion based on the staff report.

exports declined in dirham terms by 0.9 percent compared to the same period of 2000, while imports increased by 1.9 percent. However, performance of tourism receipts and workers remittances was strong, increasing by 30 percent and 20 percent, respectively.

Financial policies have taken an expansionary stance since mid-2000. Fiscal policy has been adding stimulus to aggregate demand, and monetary policy was loosened to encourage private investment. The fiscal deficit reached 4.3 percent of GDP in FY 1999–2000 (excluding privatization receipts) up from 2.5 percent in the previous fiscal year when the government benefited from proceeds of the tax amnesty totaling 1.4 percent of GDP. While tax revenue (excluding the effect of tax amnesty) improved in 1999–2000, this was offset by higher wage outlays, price subsidies for petroleum products, and a decline in non-tax revenues due to non-renewal of the fishing license with the European Union. The special six-month budget covering the second half of 2000 envisioned a substantial increase in government outlays (investment and drought-related spending); and resulted in a widening of the deficit to be financed through the proceeds from the sale of 35 percent of Maroc Telecom, which was expected by end-2000. Since these proceeds were only received in February 2001, the treasury incurred budgetary arrears for more than 3 percent of GDP to avoid issuing government securities that would have resulted in a substantial increase in interest rates. During the first four months of 2001, budgetary revenues and expenditures were in line with budgetary projections, whereas domestic arrears built-up at end 2000 were eliminated.

Bank Al-Maghrib (BAM) loosened monetary policy starting from end-2000 in response to the tightening in bank liquidity stemming from the accumulation of budgetary arrears. As a result broad money grew by 8.4 percent in 2000, 1.5 percentage points above the upper limit of the target range set by BAM. This overshooting of the monetary target reflected substantially higher than expected credit to government (despite the buildup in budgetary arrears), which increased by more than 12 percent in 2000. The accommodating stance of monetary policy continued during the first quarter of 2001 with a reduction in BAM's benchmark interest rates in March.

After a decade of fixing the nominal exchange rate against a currency basket, during which there was a significant appreciation of the real exchange rate, the authorities modified the basket to better reflect the growing importance of the euro area in Morocco's trade accompanied by a 5 percent average depreciation of the dirham on April 25, 2001. Notwithstanding a strong balance of payments position, this action was taken in response to the appreciation over the last two years of the dirham in nominal terms vis-à-vis the euro, as a result of the appreciation of the U.S. dollar against the euro, which accounts for more than two-thirds of Morocco's export transactions.

Structural reforms proceeded on several fronts. The liberalization and privatization of the telecommunication sector has not only brought in substantial financial benefits, but also increased efficiency and competition resulting in reduced communication prices while creating a large number of jobs. The government has also eliminated the generalized subsidy on edible oil in conjunction with its price and import liberalization, which caused adverse incentives for agricultural production and mostly benefited large producers and intermediaries. The rural infrastructure programs (electricity, drinking water, and roads) have accelerated; a social fund

has been established to address pressing poverty needs; and a program that helps disadvantaged women and children has been reformed. Better labor market intermediation has been established through the New National Agency for Employment. The Royal Commission for Educational Reform has launched a program to reach universal primary education by 2003. Trade liberalization has progressed as planned in the context of the Association Agreement with the European Union, with a 25 percent reduction in tariffs on some industrial and processed agricultural products. The problems of the two troubled financial institutions, Credit Immobilier et Hotelier (CIH) and Caisse Nationale du Crédit Agricole (CNCA), are being addressed by a restructuring plan for CIH and by a recapitalization of CNCA. The government has also started to take actions to improve governance, including the reform of public procurement and customs administration, and a code of conduct for civil servants.

Economic prospects have brightened during the first quarter of 2001 with the privatization of 35 percent of Maroc Telecom for US\$2.1 billion (6 percent of GDP). This privatization process was open and transparent, and the price obtained substantially exceeded expectations, considering the downturn in the world telecommunication market.

Better rainfall—although unevenly distributed—should lead to a 25 percent increase in agricultural output in 2001 with favorable spillovers on other sectors. Real GDP growth is projected at 6 percent in 2001. Nonagricultural output is expected to increase by 3.8 percent driven by construction activity, telecommunications, and tourism, which has benefited from the government's efforts to attract foreign investors and tour operators. Inflation should increase to 3 percent in 2001, largely on account of the April 2001 devaluation of the dirham. The fiscal deficit is now projected to reach 7.2 percent of GDP (on a commitment basis and excluding privatization proceeds). The external current account balance should improve slightly.

Executive Board Assessment

Executive Directors commended the authorities for achieving macroeconomic stability, as evidenced by the comfortable external position and the maintenance of inflation at industrial countries' level, despite adverse weather conditions and terms of trade developments. The economic reforms initiated over the last five years are beginning to yield tangible results as witnessed by increasing productivity, expansion in tourism, and higher foreign direct investment. Directors also welcomed the authorities' increased emphasis on improving social conditions as well as their efforts to improve governance and transparency in the management of public resources.

Directors noted that Morocco faces important remaining challenges in raising growth sufficiently to reduce unemployment and poverty on a sustained basis. To achieve this objective, they considered that macroeconomic policies will need to be tightened and structural reforms accelerated.

Directors noted the widening of the fiscal deficit excluding privatization since 1999–2000, particularly the reduction in budgetary flexibility resulting from the growing wage bill. They recognized that special factors, including drought-related spending, have contributed to this

widening and that the substantial proceeds from privatization have thus far allowed increased spending without increasing government debt. Directors agreed, however, that the fiscal stance could be placed on an unsustainable path unless measures are taken to bring the fiscal position more in line with the authorities' medium-term objectives.

Directors, therefore, welcomed the authorities' determination to achieve a significant budget deficit reduction, as confirmed by the prime minister's recently issued guidelines setting the overall deficit target for 2002 at 3 percent of GDP (including privatization proceeds). They underscored the importance of strict adherence to this target and of further deficit reductions over the medium term. Directors noted that fiscal consolidation will require bold actions both on the revenue and expenditure side, with civil service reform—aimed at curbing the growth of the wage bill—to be given the highest priority. They also highlighted the importance of rationalizing remaining subsidies and reducing tax exemptions. A number of Directors also encouraged the authorities to envisage broadening the coverage of the value-added tax in order to offset future declines in custom revenues.

Directors agreed that the relaxation of both fiscal and monetary policies in 2001 presents limited risks for macroeconomic stability in the near term. Noting the recent monetary easing, they emphasized that BAM should be ready to tighten monetary policy in response to any sign of inflationary pressures. Directors highlighted the continued strong performance of Morocco's private banks as well as the recent progress in strengthening banking supervision and extending prudential requirements to the specialized public banks. They urged the authorities to address promptly the nonperforming loans of two public banks and ensure their full capitalization. Directors welcomed the authorities' decision to participate in the Financial Sector Assessment Program.

Directors were encouraged by the recent decision to change the basket of currencies used for determining the exchange rate of the dirham, which was accompanied by a devaluation of 5 percent. They particularly welcomed the authorities' readiness to examine the feasibility and appropriateness of moving to a more flexible exchange rate system. Nearly all Directors considered that such a move would help Morocco to respond better to exogenous shocks, meet the challenge of competitiveness against the backdrop of ongoing trade liberalization, and pursue a more ambitious growth target. Directors noted that increased flexibility in exchange rate policy would need to be supported by fiscal consolidation, a strict wage policy, and a monetary policy framework that can provide a nominal anchor to replace the exchange rate. A few Directors considered that such a framework should be in place before moving toward greater flexibility.

Directors commended the authorities for proceeding with wide-ranging structural reforms that are key to achieving higher investment and growth levels in the medium term. They welcomed the trade liberalization achieved in the context of the Association Agreement with the European Union and encouraged its extension on a multilateral basis to avoid the risks of trade diversion.

Directors had a useful discussion on the agricultural sector in Morocco. They welcomed the decision to eliminate the consumption subsidy and external protection for edible oils but noted

the need for additional steps to improve, in various ways, agricultural performance. Directors encouraged the authorities to explore further opportunities for price liberalization which would help reorient incentives toward a cropping pattern better suited to Morocco's climatic conditions as well as closer to the longer-term comparative advantages of the country. Some Directors noted that such a reorientation should also be supported by a removal of trade barriers which Morocco's agricultural sector is facing in its export markets. Directors also stressed the importance of developing a social safety net to safeguard poorer farmers during the transitional period.

Directors congratulated the authorities for the transparency that had characterized the liberalization and privatization of the telecommunications sector, and commended their ongoing efforts toward better governance in the public as well as the corporate sectors. They looked forward to further progress in strengthening the judicial system, simplifying the regulatory environment, and adopting the new labor code, which will enhance labor market flexibility and employment creation.

Directors supported the authorities' determined efforts in achieving universal schooling by 2003, improving the status of women, and attacking rural poverty. They expected that the forthcoming public expenditure review will help set appropriate spending priorities toward progress in these areas.

The authorities' efforts aimed at improving the timeliness and dissemination of statistical data are yielding results, and Directors welcomed their request to undertake a Report on the Observance of Standards and Codes on statistics this year, with the objective to subscribe to the Special Data Dissemination Standard.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board.

Morocco: Selected Economic Indicators

	1996	1997	1998	1999	2000
Domestic economy					
			In percent		
Change in real GDP	12.2	-2.2	6.8	-0.7	0.3
Change in real nonagricultural GDP	3.6	3.2	3.9	3.0	2.8
Urban unemployment rate	18.1	16.9	19.1	22.9	21.5
Change in consumer prices	3.0	1.0	2.7	0.7	1.9
External sector					
			In billions of U.S. dollars 1/		
Exports, f.o.b.	6.9	7.0	7.1	7.5	7.4
Imports, f.o.b.	9.1	8.9	9.5	10.0	10.6
Tourism receipts	1.7	1.4	1.7	1.9	2.0
Private transfers (net)	2.5	2.2	2.3	2.1	2.3
Current account balance	0.0	-0.1	-0.1	-0.2	-0.5
In percent of GDP	0.1	-0.3	-0.4	-0.5	-1.5
Direct investment and other private flows	0.4	1.6	0.7	2.1	1.0
Public borrowing, net	-0.3	-1.0	-0.4	-0.7	-0.8
Overall balance	0.3	0.5	0.2	1.6	-0.4
Gross official reserves	4.0	4.2	4.6	5.7	4.8
Financial variables					
			In percent of GDP 1/		
Central government balance 2/	-3.4	-3.4	-2.5	-4.3	-6.5
Structural fiscal balance 3/	-4.0	-4.1	-4.4	-4.2	-4.5
Central government debt 4/	75.6	78.0	74.6	77.4	77.8
Of which: external	41.0	39.8	36.4	35.9	34.3
Debt service ratio (in percent of exports of goods nonfactor services and private transfers)	26.0	27.1	23.9	20.8	20.8
Change in broad money	4.8	9.0	5.8	10.3	8.4
Interest rate 5/	9.0	7.5	7.0	4.8	6.3

Sources: Data provided by the Moroccan authorities; and IMF staff estimates.

1/ Unless otherwise noted.

2/ Excluding privatization and GSM receipts. From 1996 to 1999, data refer to fiscal year beginning in June. In 2000, data refer to calendar year.

3/ Cyclically adjusted balance, excluding one-off revenue and expenditure measures.

4/ End-year debt over calendar year GDP.

5/ 52-week treasury bills, last available observation in the year.

**Statement by Mohammed Daïri, Alternate Executive Director for Morocco
July 11, 2001**

Morocco has been undergoing major political and social changes over the past three years. The new government was successful in maintaining political and social stability during the period immediately preceding and following the passing away of King Hassan II and the enthroning of King Mohammed VI in July 1999. Significant progress was also made in opening up the political system, strengthening transparency, governance, the rule of law, and human rights protection. Moreover, at a time when the country was hit by two consecutive catastrophic droughts, the authorities have maintained their good track record in stabilizing and reforming the economy, and have strengthened their fight against poverty and exclusion. My authorities wish to express their appreciation for the hard work and useful analysis and advice of the staff. They highly value the Executive Board's views and recommendations, and broadly agree with the thrust of the staff appraisal. In what follows, I will comment on recent economic and social developments, monetary and financial policies in 2000 - 2001, and the main challenges for the period ahead.

I. Macroeconomic stability and growth during 1996–2000

Growth performance was limited to an average 3.4 percent during 1996–2000, mainly as a result of three years of drought, including the two severe droughts of the past two years, leading to a further decline in the primary sector's real value added in 2000 by 17 percent after a drop of 20 percent in 1999. Cereals crop in 2000 fell to an all-time low of 1.9 million tons, half of its already very low level of 1999 (against a long-term average of 5 million and a record of 10 million in 1996). While growth of non-agricultural GDP was affected by the lower demand from rural population (45 percent of the total), it was maintained at 3½ percent. Investment increased to 25 percent of GDP in 2000 from 20 percent in 1996; however, this was insufficient to avoid an increase in unemployment, especially among the young and the educated. National savings also increased over the period from less than 20 percent of GDP to 23 percent. The impact of the droughts on the population was attenuated by emergency programs implemented by the authorities, including drinking water supply, assistance to cattle breeders, small irrigation schemes, well-targeted public works, and limited support for job-creating activities. These programs were carried out in a transparent and efficient manner, with full participation of stakeholders and in full compliance with budgetary controls and procedures.

Despite the droughts and the low growth performance, the authorities succeeded in maintaining macroeconomic stability. Inflation was kept at industrial countries' level (1.9 percent on average), and the current account deficit averaged ½ percent of GDP despite the effect of the higher energy prices in 2000, equivalent to 2 percent of GDP, the higher cereal imports, the sharp drop in agricultural exports stemming from the lower production, and the significant decline in phosphate derivatives prices. Private capital flows, mainly relating to privatization, together with active debt management policy, helped to achieve a further reduction in external public debt (to 48 percent of GDP in 2000 from 58 percent in 1996) and

to maintain a comfortable level of foreign reserves (five months of imports of GNFS). The strengthening of the external position coincided with the first repayments falling due after the grace period under the London Club rescheduling of 1990 (tranche A), amounting to some US\$300 million per year (1 percent of GDP), starting from 1999.

II. Poverty reduction

The authorities are deeply concerned about the high proportion of the population living below the poverty line (19 percent in 1999). In view of the higher frequency and severity of the droughts, the government has redoubled its efforts at fighting poverty mainly in rural areas. While poverty has increased in the late 1990s, compared to the early 1990s, this trend was largely accounted for by direct and indirect effects of the more frequent and severe droughts. In cooperation with the World Bank and NGOs, the authorities have strived to improve poverty tracking and to identify the most vulnerable groups. Efforts were geared at improving access to education, health, and other basic services, with a special focus on remote areas and women. Social spending increased as a share of total spending from 21 percent to 24 percent over the past four years. The authorities' efforts yielded noticeable success, particularly as regard to the most vulnerable groups, but greater efforts are still needed to improve social indicators which remain weak, compared to the region as a whole. The authorities believe that, together with strengthened and well-targeted social policies, significant strides in reducing poverty could only be achieved through establishment of an enabling environment for private sector development.

III. Structural reforms and private sector development

Efforts at enhancing efficiency and increasing the private sector role have continued unabated, although the difficult circumstances of the droughts and the recent terms of trade shock did not facilitate a faster pace of reforms. The opening of the political system and the new areas of reform—including in decentralization, governance, human rights, transparency, and gender issues—rendered the reform agenda more demanding. However, strengthened consultative approach and greater involvement of the civil society have also made the reform process more sustainable.

Important progress has been achieved in major structural reform areas over the past three years. These include privatization and public enterprises reform, opening of new sectors for private sector investment, liberalization of prices and adoption of a competition law, liberalization of the edible oil sector and phasing out of related subsidies, liberalization of road transportation, reform of the education system to achieve general enrollment and improve the adequacy of education with labor market needs, modernization of job intermediation, and further financial sector reform with strengthening of bank supervision, modernization of capital markets, and reform of the insurance sector.

The authorities are addressing the problems faced by the two public financial institutions (CIH and CNCA). A restructuring plan has been drawn for CIH, including recapitalization by shareholders and government guaranteed loans. It is expected that this bank will also benefit

from the strong recovery in tourism and housing. A recapitalization plan for CNCA has been recently announced, together with the restructuring of agricultural loans with due consideration to repayment capabilities and drought-related losses, while avoiding moral hazard. This plan includes partial debt relief (15 to 40 percent) for over-indebted farmers in rain-fed areas. It is expected that this plan will facilitate restoration of the culture of debt repayment and normal access to credit in the agricultural sector.

Significant progress is also being made in the area of governance, including the reform of public procurement and customs administration, the adoption of a code of good governance in the civil service, and the anti-corruption campaign, including inquiries carried out by a parliamentary commission. It is widely recognized that the high standards of professionalism and transparency that have characterized the recent privatizations in Telecoms were responsible for their success.

IV. Key economic and financial policy issues during 2000–01

1. **Budgetary policies during 2000–01:** Progress in fiscal consolidation was hindered by the lower-than-expected growth performance and by the extension to other civil servants of wage measures taken under the previous government. However, the authorities do not believe that financial policies in 2000–01 were expansionary or procyclical. The fiscal stimulus, as measured in the staff report, is small relative to the fall in private consumption following the droughts of the past two years and did not jeopardize recent gains in macroeconomic stabilization. Inflation remained low, and the external position strong, despite the terms of trade shock and the droughts. Interest rates, while remaining positive in real terms, declined in tandem with progress in disinflation. Credit to the private sector increased by 10 percent on average in 1999 - 2000, as against less than 2 percent growth in credit to the government. Furthermore, reform of the process of Treasury's domestic borrowing with greater transparency, reliance on market mechanisms, and elimination of directed credit at below market rates has enabled a leveling of the playing field and higher efficiency.

The underlying fiscal balance, which is adjusted for one-off revenue and expenditure measures, did not reflect a significant deterioration in 2000 despite the weaker growth performance. The overall balance, including privatization, increased in 2000 since the sale of the 35 percent of Maroc Telecom, expected for end-2000 and amounting to more than 6 percent of GDP, did not materialize until early-2001. This explains the involuntary increase in domestic arrears at the end of 2000. It was indeed difficult to fully offset the shortfall in privatization revenue of such magnitude through domestic borrowing without putting unsustainable pressures on interest rates in a context of depressed economic activity. Budgetary developments in 2000 (on a commitment basis) were also affected by the sharp hike in international petroleum prices, compounded by the depreciation of the dirham against the US dollar, which could not be fully passed through to the consumer. The authorities announced that they would temporarily subsidize domestic petroleum prices, and the necessary appropriations were provided for in the 2001 budget. Prices (before taxes) were brought back to parity with international prices by end-2000. On the basis of resumption of

growth to 6 percent, the 2001 budget deficit on a commitment basis, including privatization, is expected to decline to 0.9 percent of GDP from 6.5 percent of GDP in 2000.

My authorities consider that privatization revenues have a restructuring effect in that they enhance prospects for higher growth and fiscal revenue. They also believe that the use of such revenue for investment—mainly in areas where it could play the role of seed money and remove infrastructure bottlenecks for private investment at a time when growth is clearly below potential—is appropriate. Moreover, investments carried out in the context of the Hassan II Fund are selected and implemented in full consistency with budget priorities and control procedures and with due consideration to their future recurrent spending implications. In view of their strategy with regard to privatization revenue and their intention to widen its scope in the future, my authorities prefer to treat such revenue above the line while avoiding its use as a means of financing current expenditure. Recognizing that privatization revenues are temporary, they are utilizing these resources mainly for debt reduction and to finance exceptional investment expenditures which are also temporary. The overall level of expenditure would be expected to decline, once privatization revenues dwindle.

The improvement in weather conditions in 2001 benefited only the Northern part of the country; a large area, particularly the South, was subject to a severe drought for the third consecutive year. The authorities strengthened their emergency assistance programs in favor of the affected population with a budgetary cost of 0.6 percent of GDP. Moreover, as indicated in the staff report (para. 8), it is likely that most of the increased agricultural income will be saved in view of uncertainties regarding future weather patterns.

2. **Monetary policy:** Monetary policy during 1999–00 did not deviate from its well-established prudence. In 1999, Bank Al-Maghrib did face some problems in its attempt to sterilize the large and unexpected GSM license inflows. This resulted mainly from insufficient coordination between the Treasury and Bank Al-Maghrib. However, by the fourth quarter of 1999, Bank Al-Maghrib took the necessary measures to bring the interbank rate within the policy range. In 2000, the short delay in receiving the payment from the sale of Maroc Telecom (over 6 percent of GDP) could not be offset by Treasury's borrowing in the market, and this led to accumulation of domestic arrears. Bank Al-Maghrib had to alleviate some of the resulting liquidity squeeze by purchasing Treasury bills held by the banks.

Bank Al-Maghrib's decision to reduce policy rates in early-2001 was justified by the still weak domestic economy. While the budget will exert a positive fiscal impulse in 2001, this stimulus will be limited and should not pose a threat to macroeconomic stability. In view of the improved coordination between Bank Al-Maghrib and the Treasury, there is evidence that the present policy mix is appropriate and does not signal any undue relaxation of macroeconomic policy. In any case, the monetary authorities will continue to monitor developments closely and will not hesitate to adjust interest rates, if warranted.

3. **Exchange rate policy:** The authorities continue to monitor closely exchange rate developments and to assess competitiveness trends. The external position remains comfortable, with continued improvement in debt indicators and the reserve position. After increasing by 6½ percent in 1999, exports of goods and services in US dollar remained broadly constant in 2000, in part as a result of the sharp decline in food exports following the drought and because of the continued appreciation of the US dollar vis-à-vis the euro. While import volumes grew faster than export volumes by an average of 1.3 percent per year during the 1990s, this trend was reversed in 1999–2000 with export volumes outpacing imports by an average of 4 percentage points. There is also indication of export diversification with a rapid increase in electronics and electrical products. Some restructuring of downstream textiles may be unavoidable in view of the on-going reorientation of the world supply toward countries with the lowest wages. More job losses in low value-added textile exports may be looming in view of the upcoming dismantling of reference prices and of the multifibre agreement.

The authorities believe that the present phase of trade liberalization under the FTA with the EU—where tariffs are reduced, starting with equipment and raw materials—provides the industry with an opportunity to restructure and enhance productivity before the harder phase of tariff dismantling on manufactured goods is reached. Indeed, the staff point to recent improvement in productivity resulting from structural reforms, and it is very likely that this trend will accelerate, with further progress in implementing the reform agenda.

In recent months, the authorities were concerned with the continued appreciation of the dirham against the euro, resulting from further depreciation of the latter against the US dollar when most analysts expected a reversal of this trend. They were also cognizant of the slowdown in export value growth in 2000 and the erosion in 1999 – 2000 of the terms of trade gains of the earlier period. Under these circumstances, to better reflect the growing importance of trade and financial flows with the euro-zone while providing exporters with some breathing space, the authorities decided to change the basket of currencies used for determining the exchange rate by increasing the weight of the euro. The change was accompanied by a depreciation of 5 percent.

The authorities are confident that the current policy stance will enable the achievement of their macroeconomic objectives. Exports of phosphates and derivatives are recovering strongly in volume and price, and it is expected that other exports would also recover following the exchange rate change. Tourism receipts and workers remittances have increased so far at a much faster pace than assumed during the consultation discussion, and it is very likely that the external position in 2001 will be stronger than originally projected. Inflation is also running at a slower pace than in 2000, and there is a good chance that it will remain below the 3–3.5 percent range. However, in view of the uncertainties regarding future developments in the exchange rate of the euro vis-à-vis the US dollar, and to protect competitiveness, the authorities have indicated their readiness to examine the feasibility and appropriateness of moving to a more flexible exchange rate system.

V. Policies for 2002 and beyond

The upcoming elections will be a major test of the on-going democratization process. Major reforms of the election process are underway to improve its credibility. The authorities have indicated their firm commitment to maintain fiscal discipline during the run-up to the elections, to return to their original path of fiscal consolidation as soon as possible, and to accelerate and broaden their structural reforms. This is indeed necessary in order to achieve their objective of higher growth and a significant reduction in unemployment and poverty.

To signal the authorities' strong resolve to further fiscal consolidation in 2002, the Prime Minister has recently issued guidelines for the preparation of the budget. On the basis of growth forecast of 4–5 percent (assuming an average crop), inflation of 3 percent, and a current account deficit of ½ percent of GDP, the budget deficit target has been set at 3 percent of GDP. The guidelines call on ministries to observe strict limits on expenditures, including reduction in non-interest current spending, freeze on new hiring, except for priority areas, and strict selectivity in investment spending. A FAD mission has visited Morocco last February to help identify the necessary reforms in both tax policy and administration. The authorities express their gratitude to the mission for the quality of their work and recommendations to which they will give their highest attention.

The authorities believe that the ongoing political and economic reforms will result in enhanced private sector confidence and higher growth. However, they are also fully cognizant of the remaining agenda of reforms. They are encouraged by the strong interest expressed recently by major international groups in key areas, such as telecom, electronics, and tourism—with large projects being implemented with significant effects in terms of employment, exports, and transfer of technology. They are firmly committed to improving attractiveness of Morocco to domestic and foreign investors through continued liberalization and modernization of the economy, enhancing policy visibility and credibility, strengthening transparency and accountability, removing impediments to growth and private investment, and upgrading human resources and the institutional framework. The labor code has reached the final stage of preparation, and its discussion in Parliament should take place later this year. A Communal Charter is under preparation aimed at achieving greater decentralization and broader participation.

The authorities attach high priority to strengthening and modernizing the financial system, including through greater autonomy for bank and financial sector supervisory bodies. The authorities have requested participation in the joint Fund/Bank FSAP, which has been scheduled for early-2002. Following the modernization of corporate laws and accounting and auditing standards, greater attention will be given to monitoring large conglomerates and improving corporate governance. A World Bank mission will soon conduct a ROSC on corporate governance with the objective of helping the authorities in identifying weaknesses and vulnerabilities as well as the needed reforms. The authorities also recognize the importance of improving quality, access, and timeliness of economic data in order to enhance the efficiency of the decision-making processes and level the playing field. A STA mission is

scheduled to visit Morocco in October 2001 to review the data system and propose the necessary enhancements in order to meet the SDDS requirements.

The privatization program is to be accelerated and expanded with further opening of the capital of Maroc Telecom, preparation of the privatization of the remaining public banks, and extension of the program to new sectors, including the Tobacco Company (Régie des Tabacs), the national airline (RAM), and the phosphates sector. Domestic and foreign investments, as well as access to markets, will benefit from the recent adoption of legislation on industrial property rights. This legislation has been presented recently to the WTO and has been favorably received by Morocco's partners.