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Morocco: 2005 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Morocco

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2005 Article IV consultation with Morocco, the following documents have been released and are included in this package:

- the staff report for the 2005 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on May 10, 2005, 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 July 14, 2005. 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 August 29, 2005 discussion of the staff report that concluded the Article IV consultation.

- a statement by the Executive Director for Morocco.

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

Selected Issues Paper
Statistical Appendix

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

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MOROCCO

Staff Report for the 2005 Article IV Consultation

Prepared by Staff Representatives for the 2005 Consultation with Morocco

Approved by Amor Tahari and Matthew Fisher

July 14, 2005

- Discussions for the 2005 Article IV consultation were held in Rabat during April 25–May 10, 2005. The staff team comprised Ms. Eken (head), and Messrs. Sarr, Bouhga-Hagbe, Vandenbussche (all MCD), and Mulder (MFD).

- The mission met with Prime Minister Jettou, Ministers Oualalou (Finance and Privatization), Mansouri (Labor), Mechahouri (Foreign Trade), Boussaid (Public sector modernization), Mezouar (Industry and Commerce), Central Bank Governor Jouahri, Advisor to the King Azoulay, other senior government officials, and representatives of the private sector and labor unions. Mr. Daïri (Alternate Executive Director for Morocco) attended most of the meetings.

- At the conclusion of the last Article IV consultation on May 5, 2004, Executive Directors commended the Moroccan authorities for maintaining macroeconomic stability. They agreed that the key challenge facing Morocco is to achieve sustainable high rates of economic growth to reduce unemployment and poverty. They stressed the importance of supportive macroeconomic policies and accelerated structural reforms to foster private investment and enhance productivity. In these regards, Directors encouraged the authorities to further liberalize and simplify the trade regime and to improve the business environment, and stressed that fiscal consolidation was an essential part of the higher growth strategy. Directors noted that the current fixed exchange rate regime has served Morocco well. They welcomed the authorities' willingness to review the desirability and operational modalities of alternative exchange rate regimes to accompany Morocco's integration into the world economy.

- Morocco accepted the obligations of Article VIII, Sections 2(a), 3, and 4 in 1993. The capital account is open for nonresidents. Morocco's exchange rate is officially pegged to a basket of currencies dominated by the Euro. Morocco maintains an exchange system that is free of restrictions on the making of payments and transfers on current international transactions.

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EXECUTIVE SUMMARY

- Morocco has achieved macroeconomic stability since the early 1990s, with low inflation and a strong external position. However, growth has been volatile and insufficient to significantly reduce unemployment and poverty.

- Macroeconomic and financial conditions remain stable. In 2004, inflation remained low, the current account continued to register a surplus, and external reserves increased further. The budget deficit declined on account of a good revenue performance and the debt-to-GDP ratio declined because privatization receipts helped finance the deficit. Overall GDP growth slowed down reflecting the performance in the primary sector, but nonagricultural GDP growth picked up because of a dynamic tertiary sector and a recovery in mining and energy. In 2005, a decline in agricultural output, petroleum price increases, and the abolition of textile quotas will affect economic developments. In particular, the overall GDP growth is projected to decline to about 1 percent and nonagricultural GDP growth is expected to slow down. With the current policies, the budget deficit is projected to widen.

- The key challenge is to achieve sustained high rates of growth to reduce unemployment and poverty. To meet their high-growth objectives, the authorities intend to gradually reduce the budget deficit and move expeditiously with their remaining structural reform agenda in a context of continued macroeconomic stability and increasing integration into the world economy.

- Although the current fiscal stance and debt level do not pose a risk to macroeconomic stability in the short term, current policies, if maintained, could lead to a higher debt-to-GDP ratio, reduce the authorities' ability to absorb unfavorable shocks and raise expectations of higher taxes and interest rates. Achieving the authorities' high-growth and fiscal consolidation objectives would require a reform of the tax system that will widen the tax base and allow a cut in tax rates, a reduction in the wage-bill-to-GDP ratio that will enhance the flexibility of the budget, an overhaul of the food subsidy system and its replacement by targeted support to vulnerable groups which could lead to a diversification of agricultural production, and the implementation of the petroleum price adjustment mechanism. The authorities are already making efforts in these areas. Fiscal consolidation would also release resources for productive investments in rural areas where poverty is pervasive, which could generate a steadier income stream in those areas.

- The authorities have made significant progress in implementing their structural reform agenda, particularly in aspects related to trade liberalization, the financial sector, public enterprises, and the labor market. However, much remains to be done to strengthen private sector activity and enhance efficiency and productivity. Priority areas are further trade liberalization, improvements in the business environment, and financial sector reforms.

- The current fixed exchange rate regime has served Morocco well and there are no signs of a misalignment of the dirham. However, forward-looking considerations, in particular the increasing opening up of the Moroccan economy and the envisaged structural reforms to increase efficiency and productivity favor a gradual transition to a more flexible exchange rate regime. The authorities are reviewing pros and cons of alternative regimes. At their request, the staff prepared a paper on the exchange rate regime. The authorities intend to take the conclusions of the paper into consideration in their internal deliberations.

I. Background

1. **Morocco's political situation remains stable.** The current coalition government took power after the September 2002 parliamentary elections and the next parliamentary elections are scheduled for September 2007. The authorities believe that poverty, unemployment, and social exclusion are the root causes of Islamic extremism, which is a major political concern. Achieving social development is therefore at the top of the government's agenda. To this end, the authorities are putting more emphasis on access to education, health care, housing, and basic infrastructure, and on rural development. New family and labor codes were recently passed reflecting their commitment to promote social cohesion and stability.

2. **As noted in previous staff reports,[1] Morocco has achieved macroeconomic stability since the early 1990s, but growth has been volatile and insufficient to reduce significantly unemployment and poverty.** Real growth averaged 3 percent over the last decade, and urban unemployment was 18 percent in 2004. Poverty,[2] which is particularly pervasive in rural areas, is estimated at 15 percent of the population, and the economically vulnerable reaches 40 percent. Overall real GDP growth has been volatile because cereal production, which accounts for a large share of Moroccan agriculture, is highly sensitive to droughts. Growth improved during 2001–04 because agriculture benefited from good weather conditions, while nonagricultural output growth accelerated (Table 1).[3]

3. **The balance of payments remains strong despite low export growth.** After rising steadily between 1993 and 2001, export growth slowed since 2001 even though the dirham was devalued by 5 percent in 2001 (Figure 1). However, because of a surge in workers' remittances and tourism receipts, the current account deficit turned into a surplus and national savings increased significantly. Balances on services, income, and transfers more than covered the trade deficit. The overall balance of payments remained in surplus, and international reserves increased to about 10 months of imports. As a result, Morocco's foreign currency debt rating, although below investment grade, saw its outlook upgraded from stable to positive and secondary market spreads declined significantly (Figure 2).

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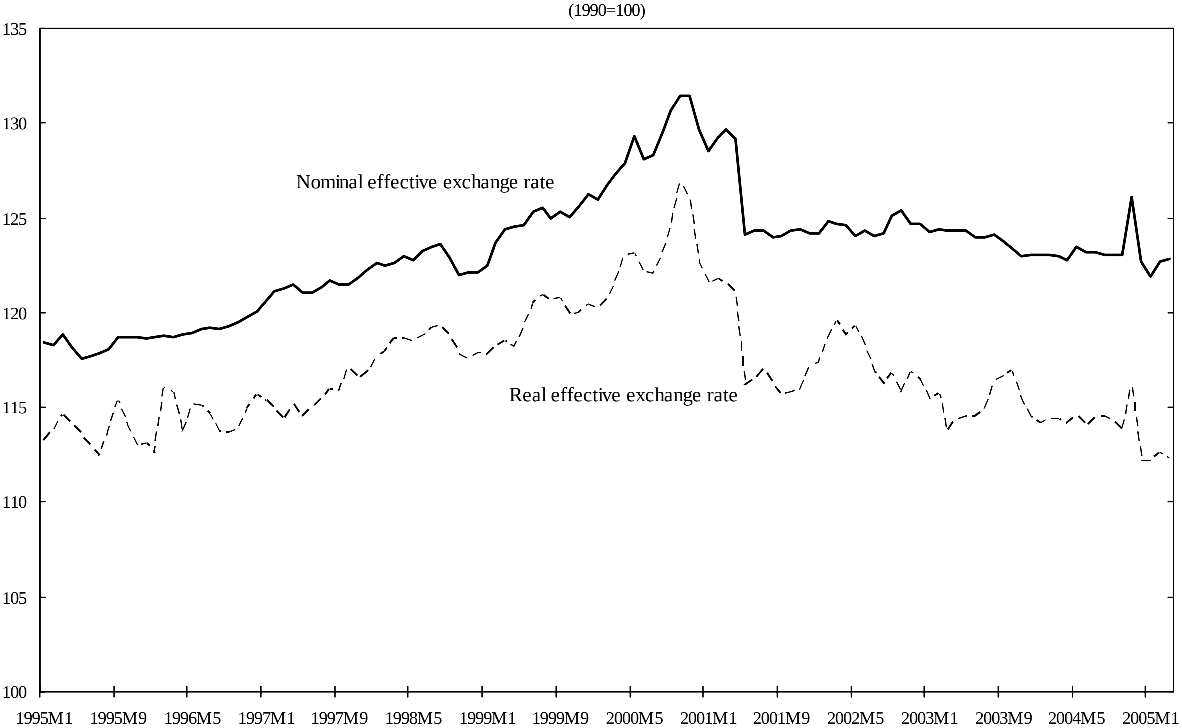
[1] See SM/04/121 and SM/03/119.

[2] The national poverty line was at about US$350 per year per person in 1999.

[3] See SM/05/277, Supplement 1 for more detailed analysis of Morocco's growth performance.

Figure 1. Morocco: Nominal and Real Effective Exchange Rates, 1995–2005

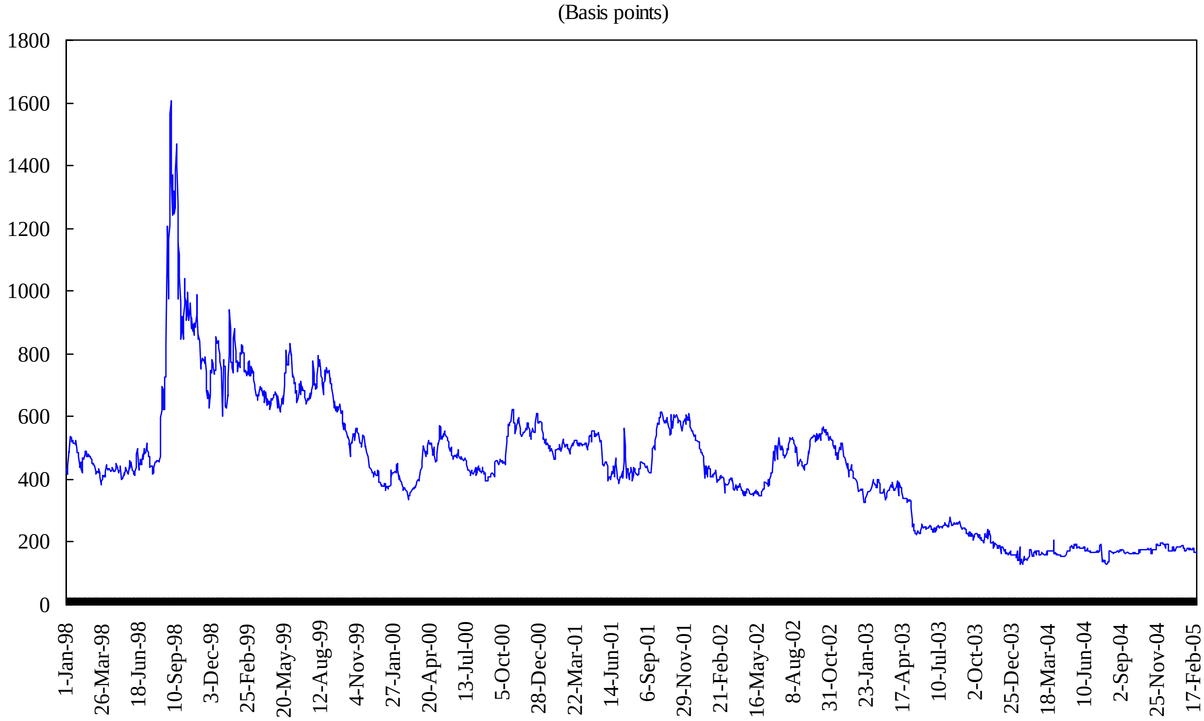
(1990=100)



Source: Internaional Monetary Fund, Information Notice System.

Figure 2. Morocco: Emerging Markets Bond Index Spread (EMBI), 1998–2005

(Basis points)



Source: JP Morgan (EMBI).

4. **In an attempt to spur growth in the late 1990s, the authorities ran an expansionary fiscal policy** with increases in wage expenditures and tax and import tariff exemptions, which eventually triggered more wage increases and exemption demands. The fiscal deficits (including Fond Hassan II expenditures and excluding privatization receipts) increased from an annual average of 3.6 percent of GDP in 1996–99 to 5.5 percent in 2000–04, putting the fiscal position on a potentially unsustainable path.[4] However, the debt-to-GDP ratio declined by about 15 percentage points during 2000–04 mainly because privatization receipts helped finance fiscal deficits and the authorities reduced debt through debt/equity swaps. In the absence of these operations, the debt-to-GDP ratio would have increased by about 6 percentage points.

5. **In recent years, the authorities have taken measures in line with Fund policy recommendations** (see Box 1 for details). Although progress has been slow in some areas, the authorities accelerated their reform agenda starting from 2002.

II. Recent Developments and Short-Term Outlook

6. **In 2004, macroeconomic and financial conditions remained stable and nonagricultural GDP growth picked up.** While overall GDP growth slowed down to 4.2 percent on account of a decline in growth in the primary sector, nonagricultural GDP growth picked up because of a dynamic tertiary sector and a recovery in mining and energy. On the external side, the trade deficit widened with the decline in agricultural exports due to supply constraints, the stagnation in textiles exports, and the increase in the petroleum import bill (Table 2). Nevertheless, the current account remained in surplus reflecting strong tourism and remittance inflows. With increased foreign direct investment and privatization receipts, gross official reserves increased further. The balance of payments surplus in the context of the pegged exchange rate continued to result in abundant liquidity in the banking system and led to a decline in interbank interest rates. The central bank allowed interest rates to decline given the very low inflation rate and moderate domestic demand.

7. **The fiscal deficit declined in 2004, but some budgetary policies did not support fiscal consolidation.** The fiscal deficit declined by 0.4 percentage point to 4.9 percent of GDP and was much lower than envisaged in the 2004 budget (Table 3). This development mainly reflected good revenue performance. Expenditures were higher than envisaged because of increases in: (a) investment following an acceleration in project executions; (b) the wage bill following new salary increases; and (c) subsidies because the food subsidy reform was postponed and the petroleum price adjustment mechanism was not fully implemented. The authorities were able to prevent further expenditure increases related to the El-Hoceima earthquake and a locust invasion by reallocating budgetary appropriations. Public debt declined to 66 percent of GDP because privatization receipts helped finance the deficit.

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[4] A commonly accepted approach to assessing debt sustainability is to view fiscal policy as sustainable if it delivers a ratio of public debt-to-GDP that is stable, and then calculate the primary balance that would be required to achieve that. During 2000–04, the primary deficit averaged 1 percent of GDP, while the differential between growth and the implicit interest rate on public debt averaged a negative 1 percent, implying that a primary surplus would have been required to at least stabilize the debt-to-GDP ratio before privatization.

Box 1. Past Fund Surveillance

Over the past five years, Fund surveillance has focused on policies aimed at maintaining macroeconomic stability, achieving fiscal consolidation, and accelerating growth to reduce unemployment and poverty. The staff recommended (a) tax and expenditure reforms to lower the fiscal deficit and debt-to-GDP ratios, dispel the risk of future tax increases and higher interest rates, and create fiscal space; (b) an exchange rate policy that would reverse the real effective exchange rate appreciation that took place in the 1990s; and (c) structural reforms to foster private investment, productivity, and the efficient allocation of resources.

The authorities have taken steps along the lines of the Fund's recommendations but progress has been slow in some areas.

Macroeconomic stability has been preserved but fiscal consolidation has not yet been achieved. The authorities have implemented a no net new hiring policy, but the wage bill ratio increased further because of ad hoc salary increases and promotions. The authorities eliminated edible oil subsidies, but flour and sugar continue to be subsidized and the automatic petroleum price adjustment mechanism has not been fully operating. On the revenue side, the authorities made progress in modernizing tax administration, but the provision of tax exemptions rendered the tax system more complex and its administration more difficult.

The authorities devalued the dirham by 5 percent in 2001, partly reversing its real appreciation during the 1990s, and the real effective exchange rate has depreciated further since then. Fund surveillance has recently focused on the desirability of moving gradually to a more flexible exchange rate regime. The authorities have entered into a dialogue with the staff on this issue.

The authorities accelerated structural reform. Trade liberalization is proceeding both at multilateral and bilateral levels. The authorities reduced the number and level of tariff rates, eliminated reference import prices, implemented customs reform, and have signed trade agreements with their major trading partners. Financial sector reform is proceeding in line with the Financial Sector Assessment Program (FSAP) recommendations. Major public enterprises have been privatized, the remaining ones are being reformed, and steps have been taken to put pension funds on a sounder footing. A new labor code has been promulgated. Progress in reforming the judicial system, improving contract enforcement, and rendering the public services more efficient are needed to further improve the business environment.

8. **A decline in agricultural output, petroleum price increases, and the abolition of textile quotas will affect economic developments in 2005.** The primary sector will contract sharply and some agro industries will be adversely affected because of bad weather earlier this year. Growth in the manufacturing sector is expected to slow down, reflecting the difficulties in the textile sector (see Box 2). Strong performance in tourism and construction sectors and remittance inflows are expected to continue. Consequently, overall GDP growth is projected to decline to about 1 percent and non agricultural GDP growth is expected to slow down. The external current account is projected to register a small deficit because of higher oil prices and food imports, and weak textile exports. The overall balance of payments position is expected to

continue to register a surplus, even if the effects of privatization are excluded. With delayed implementation of domestic petroleum price adjustments, the impact of higher international petroleum prices on growth and inflation will be limited, and the budget will bear the subsidy cost (estimated at 0.8 percent of GDP). A recently announced policy package, which will reallocate budget appropriations, should help alleviate the impact of the poor harvest on rural areas.

Box 2. Recent Developments in the Textiles and Clothing Sector

In 2004, the textiles and clothing sector accounted for 17 percent of manufacturing value added, 50 percent of manufacturing employment and 32.5 percent of merchandise exports. Therefore, the worldwide abolition of quantitative restrictions on exports of textile and clothing that came into effect on January 1, 2005 will have important consequences for Morocco.

During the first four months of 2005, Moroccan exports of clothing declined by 16.1 percent and exports of hosiery by 21 percent in local currency value compared with the first four months of 2004. These two product categories together accounted for 30.6 percent of Moroccan merchandise exports in 2004.

It is not clear yet to what extent the early adjustments following the abolition of the quota system are indicative of longer term trends. However, a study by the United Nations using the Global Trade Analysis Project (GTAP) computable general equilibrium model suggests that Morocco could experience a long-term reduction in textiles and clothing exports of respectively 11 and 18 percent as a result of the quota phase-out.[1] This would correspond to a loss of 0.22 percent of GDP. Using an alternative GTAP specification, a recent World Bank study[2] obtains similar results. In addition, it estimates the labor market impact of the quota removal. The findings suggest that 15 to 16 percent of unskilled workers in Morocco's textiles and clothing sector could lose their job.

To avert these looming losses of employment and income, Moroccan policy makers have taken measures to accelerate the current transition of the sector towards higher value-added production and increased vertical integration. The recently concluded free trade agreement with Turkey—a large and diversified producer of textiles—is an important component of that strategy, since it will enable Moroccan firms to source textiles production in Turkey while respecting the rules of origin requirements of the European Union. The free-trade agreement with the US could also benefit the sector, since the US is currently a virtually untapped market.

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[1] See UNECA (United Nations Economic Commission for Africa), "Comment Sauver le Textile Maghrebin?", 2005, paper presented at the UMA/CEA conference in Tunis (February 14–15, 2005).

[2] See Manole, V., "Winner or Loser? Effects of Quota Abolition in World Markets for Textile and Apparel," 2005, World Bank Working Paper.

9. **Current policies are expected to lead to a deterioration in the fiscal deficit to about 5.5 percent of GDP in 2005,** despite a continued favorable revenue performance. Expenditures would significantly increase taking into account the repercussions on wage payments of the 2004 wage negotiations, the voluntary retirement program, the new universal health insurance program, the delay of the food (wheat and sugar) subsidy reform, and the partial adjustment in mid-May of domestic petroleum prices. Excluding the cost of the early retirement program and other one-off wage related payments, the 2005 fiscal deficit is projected at 4.5 percent of GDP. The authorities intend to eliminate outstanding arrears (0.7 percent of GDP), which have been used to partly finance subsidies in 2004 and early 2005. Large privatization receipts from the sale of government shares in Maroc Telecom will again help finance the deficit. At end-2005, the debt-to-GDP ratio is projected to increase to 70 percent of GDP, taking into account the issuance of debt to cover old pension fund arrears (2.4 percent of GDP).

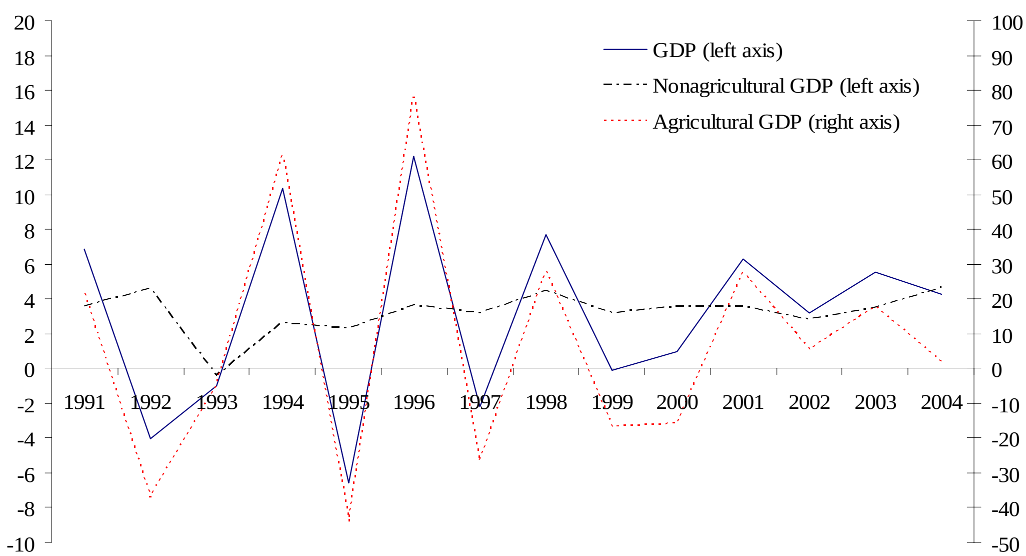
III. Report on Policy Discussions

10. Policy discussions focused on gaining a common understanding of the economic environment and drawing an integrated strategy to address the growth and unemployment challenges. Meeting these challenges will require putting conditions in place to foster investment and productivity growth.

A. The Economic Environment and Key Challenges

11. **The Moroccan economy remains characterized by three key features:** (a) output growth has been volatile and insufficient to significantly reduce unemployment and poverty (Figure 3); (b) the country is facing increased competition from abroad; and (c) the macroeconomic environment has been stable despite relatively high fiscal deficits.

Figure 3. Real GDP Growth
(In percent)



Source: Moroccan authorities and IMF Staff estimates.

12. **Morocco's growth performance reflects extreme volatility of the agricultural sector and low nonagricultural growth.** The share of the agricultural sector has fluctuated around 15 percent since 1991, but its growth has been extremely volatile. Indeed, the standard deviation of the agricultural sector growth rate for the period 1991–2004 has been 35 percent, while that of the nonagricultural sector has been only 1.3 percent. During the same period, growth of the nonagricultural sector has been low, averaging 3.2 percent per annum. An acceleration of growth in the nonagricultural sector, by increasing its share in total GDP, would therefore help reduce overall volatility over the medium term. Moreover, cross-country empirical evidence suggests that a reduction in output volatility could have growth-enhancing effects.[5] To these ends, increases in investment and total factor productivity in the nonagricultural sector are needed.[6] In addition, measures to attack some structural causes of agricultural output volatility, such as the plan announced by the authorities in May 2005 to encourage crop diversification over the next five years, would also help improve economic performance over the medium term.

13. **In the context of ongoing trade liberalization, the nonagricultural sector is subjected to increasing international competition.** To maximize exports opportunities and better withstand competition from abroad in the domestic market, efforts to improve Morocco's competitiveness will need to be accelerated. Such an environment would also foster investment. In the past few years, nongovernment investment has shown signs of revival, contributing significantly to domestic demand growth. However, domestic demand remains sluggish despite the abundance of national savings and low monetary policy interest rates, suggesting the existence of structural constraints to its dynamism.

14. **Abundant liquidity, supported by a surge in remittance flows, has facilitated the financing of high fiscal deficits at low costs without crowding out private credit or undermining macroeconomic stability.** Indeed, interest rates have been on a declining trend along the maturity spectrum. In the circumstances, the authorities did not accelerate fiscal consolidation. However, they took advantage of the situation to substitute domestic for external debt, develop a domestic debt market, and reduce external vulnerability.[7] Nevertheless, if economic activity picked up, the balance of payments surplus disappeared, and/or the capital account opened up to resident outflows, the current fiscal policies could spur an increase in interest rates and become a binding constraint on growth.

15. **In the above described context, policy discussions focused on two areas that could help achieve sustained growth to significantly reduce unemployment and poverty:** (a) maintaining macroeconomic stability and reducing the fiscal deficit while creating fiscal flexibility for demand management and room for productive expenditures; and (b) accelerating

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[5] For details, see World Economic Outlook, April 2005, Chapter II.

[6] For developments in total factor productivity, see SM/05/277, Supplement 1.

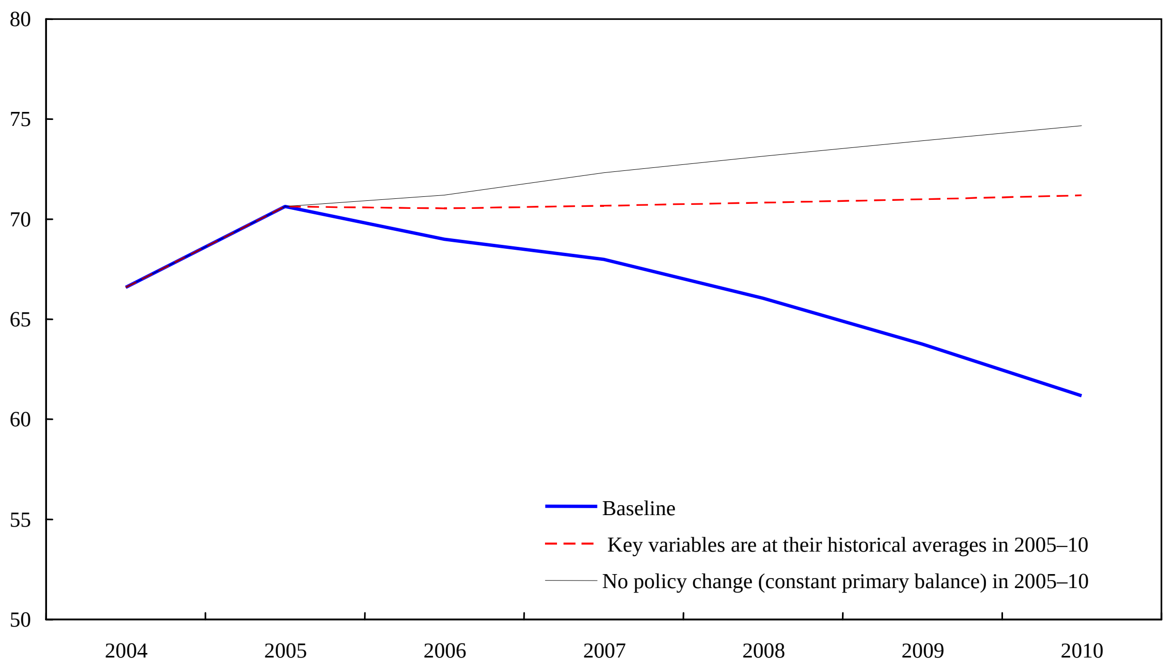
[7] Indeed, high public debt has favorable maturity and currency composition (see Table 4 and SM/04/124, Supplement 1) with low exposure to exchange rate and interest rate risks. The maturity of domestic debt was further increased in 2004 and short-term debt represents only 20 percent of government debt.

structural reforms, including trade liberalization. Discussions were also held on the pros and cons of alternative exchange rate regimes as the economy undergoes structural transformation and faces greater international competition.

B. Fiscal Policy

16. **The fiscal stance and the debt level do not pose a risk to macroeconomic stability in the short term in the present macroeconomic environment, but current policies would not put public finances on a sustainable path.** If current policies continue, the debt-to-GDP ratio would be increasing, with no cushion to absorb shocks, especially output shocks (Table 5 and Figure 4). Standard debt dynamics suggest that a primary surplus of 0.8 percent of GDP would be required to stabilize the current debt-to-GDP level given Morocco's growth experience and the average implicit interest rate on public debt, compared to the projected primary deficit of 1 percent of GDP in 2005, excluding exceptional expenditures. The debt ratio is sensitive not only to slower fiscal consolidation but also to slower growth. The fiscal deficit should therefore be reduced to at least 3 percent of GDP over the medium term (corresponding to a primary surplus of 1 percent of GDP) to lower the debt ratio on a sustained basis, and enhance fiscal flexibility and resilience to output shocks.

Figure 4. Debt-to-GDP Ratio (in percent)

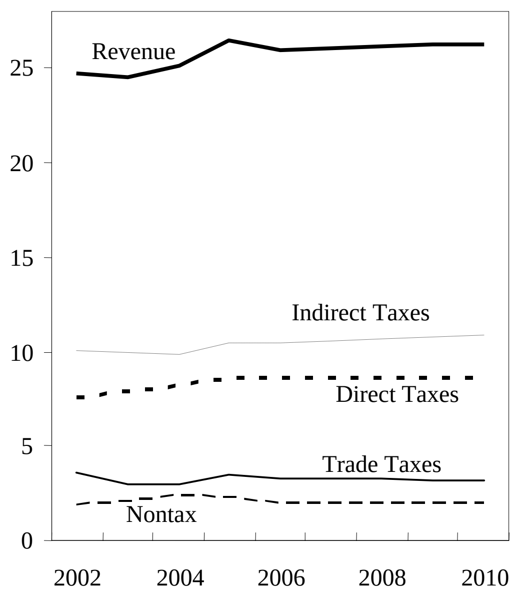


Moroccan authorities; and IMF Staff estimates.

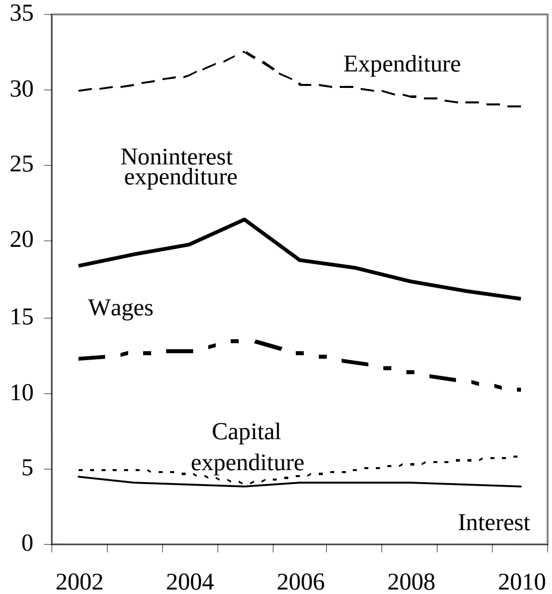
17. **The authorities agree with the staff that fiscal consolidation is an essential part of the high growth strategy.** They do not consider the current fiscal stance as unsustainable. However, they remain committed to reducing the fiscal deficit to 3 percent of GDP by 2009 (Table 6). The achievement of this objective and its compatibility with a high growth scenario will require actions on both the revenue and expenditure sides (Figure 5).

Figure 5. Fiscal Developments and Medium-Term Projections
(In percent of GDP)

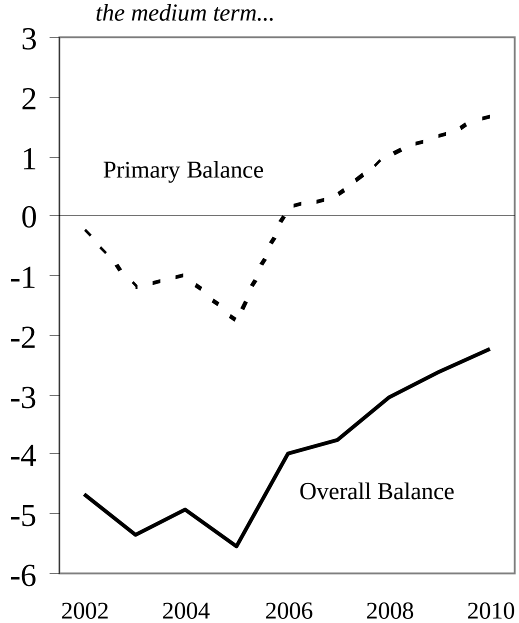
Tax reform, in particular of the VAT, would help stabilize revenue as import taxes decline with trade liberalization...



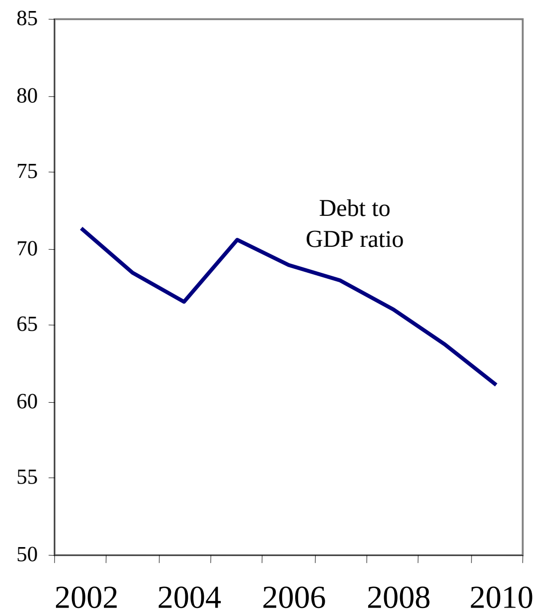
Expenditures would be reduced in the medium term through containment of noninterest current expenditure...



Fiscal balances would improve over the medium term...



The debt to GDP ratio would decline.



Source: Moroccan Authorities and IMF staff estimates and projections.

18. **The authorities and the staff agreed that a reform of the tax system, in line with the recommendations of recent FAD technical assistance missions, would widen the tax base, eliminate tax induced distortions, and ultimately allow a reduction in tax rates that would release resources to the private sector for their efficient allocation.** Morocco's tax revenue-to-GDP ratio and its distribution between direct and indirect taxes compare well with other countries (Table 7). However, the proliferation of tax exemptions over the years and a growing direct tax revenue-to-GDP ratio, suggest an increasing tax burden on a narrow tax base. The marginal personal income tax rate, at 44 percent, is high and the private sector blames it for higher wage demands of skilled workers. The VAT system with 5 tax rates and widespread exemptions is complex and difficult to administer. The corporate tax base is also eroded by exemptions and special tax treatments. In this context, the authorities intend to initiate tax reform, particularly of the VAT in 2006 and to present a tax expenditure report with the 2006 budget to raise awareness about the inefficiency of the tax system.

19. **On the expenditure side, the authorities plan to reduce the wage bill ratio and improve the quality of expenditures.** To reduce the wage bill ratio, they plan to contain the wage drift to 2–3 percent, continue their no net new hiring policy, and implement a modern human resource management and remuneration system. The voluntary departure/early retirement program[8] will eliminate some 30,000 positions and will result in significant wage savings. The staff and the authorities agree that the implementation of these measures should allow a reduction of the wage bill ratio by 2 percent of GDP by 2009. The authorities also intend to eliminate gradually general food subsidies over three years, enhance targeted support to vulnerable groups, and privatize sugar companies, as well as reflect gradually international price developments on domestic petroleum product prices (except for butane gas). In addition, they intend to continue to reform pension funds to dispel the contingent risks to the budget.[9]

20. **The staff agreed with the authorities that their planned expenditure policies are in line with their medium-term macroeconomic objectives.** Staff noted that a lower wage bill ratio would enhance budget flexibility, including to dampen income and consumption volatilities, without compromising debt sustainability. Containment of salary increases would also limit increases in private sector wages. An overhaul of the food subsidy system and the elimination of petroleum price subsidies, which do not mainly benefit vulnerable groups, could release resources for more productive expenditures, including for rural infrastructure. The elimination of food subsidies and their replacement with targeted support to vulnerable groups should lead in the medium-to-long run to a diversification of agricultural production that is less dependent on weather vagaries. In addition, the planned implementation, in collaboration with the World Bank, of a medium-term budget framework and the continuation of the decentralization and performance budgeting program should render the public administration more efficient and transparent.

[8] The authorities estimate that the budgetary cost of the voluntary departure/early retirement program would amount to about 0.7 percent of GDP in 2005.

[9] See SM/04/121, Box 1 on the financial situation of the main pension funds.

C. Structural Reforms

21. **The authorities have a broad based structural reform agenda** to increase productivity and promote private sector activity, and facilitate Morocco's increasing integration into the world economy. Discussions focused on the following priority areas: (a) continued trade liberalization; (b) the promotion of an internationally competitive business environment; and (c) financial sector reforms.

Trade liberalization

22. **The authorities view trade liberalization and integration into the world economy as essential to enhance export opportunities and foster the efficiency of the economy.** In 2004, MFN tariffs were reduced to a maximum of 10 percent for goods freely traded with the European Union. Also, trade agreements were signed with the United States, Turkey and regional partners (Tunisia, Jordan, and Egypt) to complement the association agreement with the European Union. The trade agreement with the United States is expected to play a catalytic role in attracting foreign direct investment and in transforming Morocco into an export platform to Europe and the United States taking advantage of its geographical position and the soon to be completed Tanger-Med port complex. In addition, the authorities are keen to achieve trade liberalization at the regional level in order to establish a large regional market and attract foreign investment.

23. **Staff noted that the proliferation of bilateral accords made the trade system complex and underscored the need to reduce the number, dispersion, and average level of tariffs.**[10] More specifically, the staff recommended an acceleration of tariff reduction and the elimination of variable import tariffs together with the elimination of food subsidies. The smaller than previously expected negative impact of trade liberalization on tax revenues provides room for an acceleration. The authorities noted that, if confirmed, the good import tax revenue performance would be a welcome development that could support faster trade liberalization.

Business environment

24. **The authorities intend to keep improving the business environment to increase the economy's growth potential.** They have made significant progress in certain areas, notably with the liberalization of air transport that positively impacted tourism and of the telecommunications sector that is flourishing. Morocco's business community feels that critical reforms aimed at improving the business environment in other areas have been initiated in recent years, but many of them remain to be effectively implemented. The new labor code, if fully implemented, should contribute to clarifying employer/employee relationships. The reform of the judicial system, which the authorities have been discussing with the World Bank, should also proceed faster. Access to land is difficult and the law on domestic competition remains to be effectively implemented. The authorities intend to continue reforming the

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[10] The average tariff rate was 26 percent in 2004. There are eight multilateral tariff lines, which vary from 0 to 50 percent for nonagricultural and nonfood products.

transport sectors and the logistics chain, in particular port services, to improve the competitiveness of Moroccan enterprises and their logistical support. Privatization and public enterprise restructuring programs will also continue.

25. **The authorities are reviewing their industrial policy strategy and have sponsored a study by an international consulting firm to help them identify sectors with growth potential.** The staff encouraged the authorities to promote a neutral and internationally competitive business environment and resist pressures for the provision of exemptions or special incentives in favor of specific sectors.

Financial sector reforms

26. **The authorities intend to further strengthen the financial sector.** Provisioning and capital adequacy ratios have recently improved. Nonperforming loans have stabilized but remain high (Table 8). High NPLs increase the cost of intermediation. Because of high costs of intermediation, the reduction in monetary policy interest rates, discussed below, has not led to significantly lower real lending interest rates, especially for SMEs. The cost of intermediation may also constrain other potentially desirable policies. Progress in reducing nonperforming loans and increasing the efficiency of domestic banks more generally will need to be achieved before significant capital account liberalization can be allowed for residents. On the other hand, gradual capital account liberalization could put competition pressures on banks and help the transfer of risk management technologies.

27. **Bank Al-Maghrib (BAM) has made significant progress in the implementation of FSAP recommendations to strengthen banking supervision and improve banks' risk management practices.** The imminent promulgation of the new central bank and banking laws will further enhance the supervisory power and autonomy of BAM. To this end, steps have been taken to strengthen banking supervision capacity in BAM and it started to withdraw from both the capital and management of credit institutions. Progress was also made in the restructuring of specialized banks. The Crédit Immobilier et Hotelier is currently seeking an international partner and the Crédit Agricole du Maroc will no longer finance quasi-fiscal operations. The authorities indicated that they will not extend their exemptions from prudential regulations beyond June 2007. The staff recommended that all banks be brought to compliance with prudential regulations as early as possible, if necessary by new capital injections. The authorities intend to continue their efforts to implement FSAP recommendations. The World Bank is preparing a financial sector adjustment loan to accompany those efforts.

28. **Limited access to and high cost of credit for small- and medium-size enterprises (SMEs), which represent the core of Morocco's enterprise sector, is of major concern to the authorities.** A World Bank survey found that problems related to the information system on enterprises, property rights, contract enforcement, and the lack of financial management skills in the enterprise sector were the main structural constraints. The staff underscored the importance of removing the above structural constraints to enhance the availability and reduce the cost of credit to SMEs. Moroccan banks are receiving assistance from the IFC to better assess credit to SMEs. The authorities intend to support SME financing through a guarantee fund that will have its own capital and be supported by donors to dispel contingent budget

risks. Beneficiaries would need to adhere to minimum corporate governance and transparency requirements to access the guarantee fund.

D. Monetary and Exchange Rate Policies

29. **Monetary policy is being implemented in a context of abundant liquidity and relatively weak domestic demand.** BAM, while keeping its announced main policy rate at 3.25 percent, effectively reduced interbank interest rates to about 2.50 percent since 2004 (Figure 6) by limiting the volume of liquidity mopped up from the market. Banks deposit most of their remaining excess liquidity at the money market floor deposit facility rate of 2.25 percent because of the absence of unsatisfied credit demand. The authorities explained that they considered inappropriate to formally reduce their announced main policy rate to the observed interbank rate in a context characterized, in their view, by uncertainty on inflation, the absence of unsatisfied credit demand, and in view of the level of interest rates abroad. They also indicated that a further reduction in interest rates would mainly be reflected in deposit rather than lending rates, particularly SME lending rates (Table 9).

30. **In view of the very low inflation, the staff considered BAM's effective reduction of monetary policy interest rates appropriate.** The staff noted, however, that the differential between the announced policy rate and the effective money market rate affects the transparency of monetary policy, which has been enhanced by BAM's recent simplification of its monetary policy instruments. Staff argued that a formal reduction of BAM's main policy rate would be desirable, and pointed out that the use of the deposit facility, normally available at banks' initiative on an exceptional basis to effectively reduce interest rates, does not foster interbank activity. Staff also noted that BAM's directive to banks to provide information on loans granted at interest rates below reference rates could constrain competition, as some banks pointed out to the mission.

31. **The authorities consider that the current fixed exchange rate regime has served Morocco well.** The balance of payments is strong, inflation is low, the real effective exchange rate has depreciated since 2001, and equilibrium exchange rate estimates do not point to a misalignment (Figure 7). The staff shared the authorities' views and noted that the current regime could be appropriate if Morocco's historical characteristics (heavy reliance on trade with the Euro area, the low impact of terms of trade shocks on economic activity, and the relatively low level of capital flows) remained the same.[11] However, staff argued that forward looking considerations favor a gradual transition to a flexible exchange rate regime. As the economy opens up and is potentially more vulnerable to external shocks, a flexible exchange rate regime would facilitate adjustment to those shocks. Structural reforms, by increasing productivity and efficiency, could justify a strong currency, but these may take time to materialize. Exchange rate uncertainty would be amplified by an opening of the capital account. A flexible exchange rate would also be necessary to maintain monetary independence if the capital account were opened up, and would be desirable to avoid providing implicit exchange rate guarantees.

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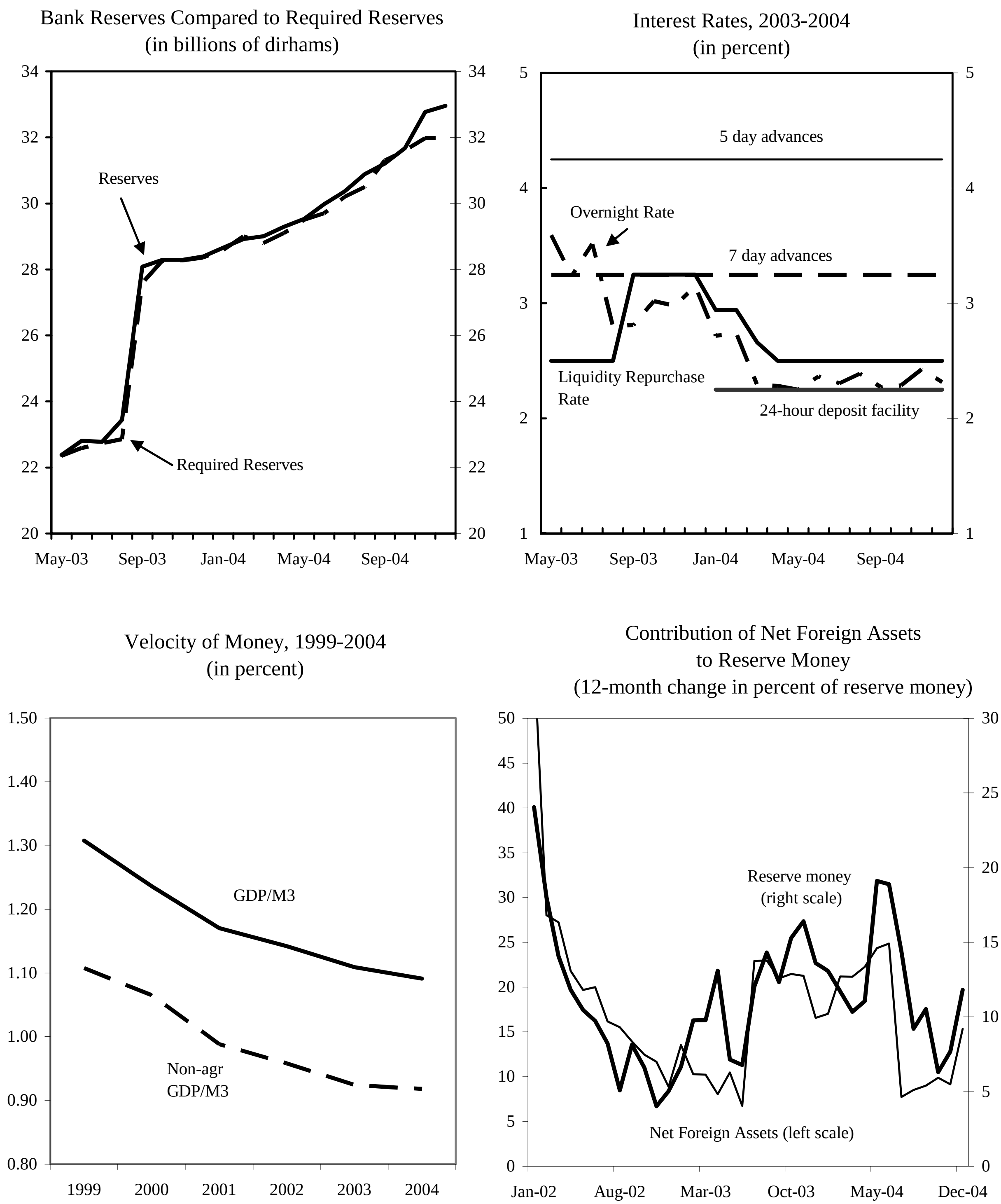
[11] For more details, see Section C of the exchange rate regime paper (SM/05/277, Supplement 1).

Figure 6. Morocco: Monetary Developments

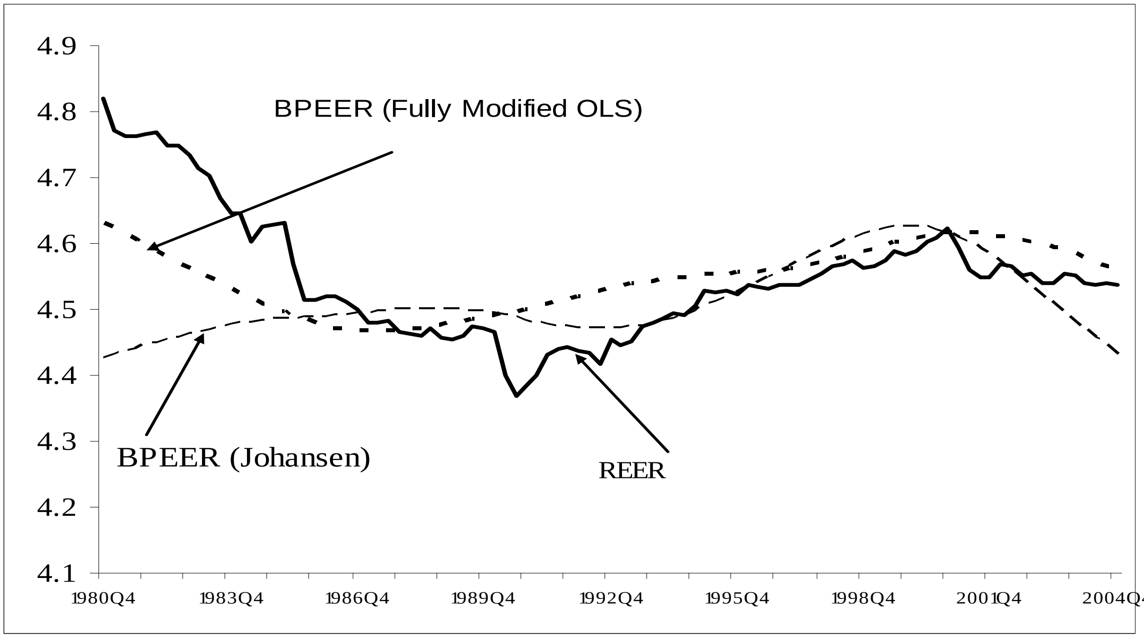


Source: Moroccan authorities
1/ Interest rate for BAM's 7-day advances.

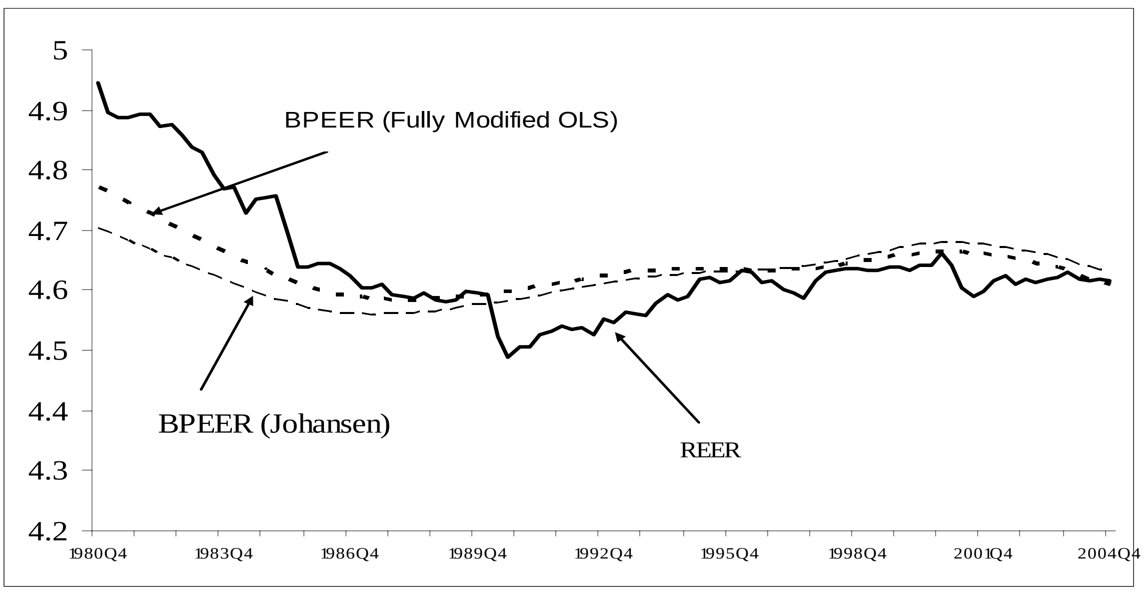
Figure 7. REER vs. Balance of Payments Equilibrium Exchange Rate (BPEER) 1/

(↑ = appreciation, in logarithm)

Using 1989–91 trade weights



Using 1999–2001 trade weights



Source: IMF staff estimates.
1/ The model of the balance of payments equilibrium exchange rate (BPEER) was used to estimate Morocco's equilibrium exchange rate. See SM/05/277, Supplement 1 for details.

32. **The authorities noted the possibility of an appreciation of the dirham if the exchange rate regime became flexible in the context of balance of payments surpluses, which could hurt exports and investment.** The staff argued that an appreciation of the dirham under a flexible exchange rate regime was possible but would lead to higher imports of consumption and investment goods, which would dampen the appreciation. Over time, however, it is difficult to know what the dynamics of a move to a more flexible exchange rate would look like.

33. **The authorities intend to review the pros and cons of alternative exchange rate regimes,** taking into account the characteristics of the Moroccan economy and their future policy intentions. They are open to the idea of a possible gradual move to a flexible exchange rate regime. At the request of the authorities, the staff prepared a paper on the exchange rate regime.[12] The staff also discussed at the technical level operational and institutional issues that would be involved in a transition to a flexible regime, including a new monetary policy framework to provide a nominal anchor, the development of foreign exchange markets and risk management capacities in the financial sector, and the design of intervention policies. The authorities indicated that they would take the conclusions and recommendations of staff into consideration in their internal deliberations.

E. Medium-Term Framework and Risks

34. **The staff, in consultation with the authorities, prepared a medium-term framework aimed at achieving the high growth objective.** The framework assumes that, in the context of moderate export growth in an increasingly competitive international environment, the domestic market would continue to be the main source of growth. Structural reforms, public investment in infrastructure, and reduced output volatility would foster private investment. As the economy grows and tax burdens are reduced and shared among a widened tax base, a more stable and steadily increasing private consumption growth pattern would enhance private investor confidence. Also tied to fiscal consolidation and ongoing structural reforms, private investment and productivity are forecast to steadily increase and unemployment to steadily decline (Table 10). In this context, the staff noted that a gradual transition to a flexible exchange rate would ensure a proper balance between all sources of growth. Growth is expected to significantly rebound in 2006 following the negative agriculture shock in 2005, with a gradual increase in nonagricultural growth thereafter. The increase in nonagricultural growth is expected to come from higher private investment and productivity increase with the envisaged structural reforms.

35. **The macroeconomic framework forecasts a widening of the current account deficit as investment picks up** (Table 11). The projected deficits would not pose a problem to the balance of payments since they would be financed by the private sector and existing national savings. Foreign exchange reserve accumulation would slow down over the medium term but reserves coverage would remain comfortable. Standard external debt sustainability analysis shows that Morocco’s external debt will remain sustainable over the medium term (Table 12).

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[12] See SM/05/277, Supplement 1.

Moreover, the authorities believe that the deterioration in the trade balance would be less because of their optimism about petroleum prices and textile exports.

36. **There are risks to the medium-term framework.** It is difficult to forecast the exact magnitude of the impact the envisaged policies will have on the growth performance as well as the lags that will be experienced in the process. Thus, higher nonagricultural growth may take longer to materialize and growth may be lower than projected in the near future. In addition, there are risks to the balance of payments outlook with the increased competition in textile exports. Studies by OECD and World Bank staff indicate that Maghreb countries are becoming more specialized in textile market segments that require quick product delivery, making their vertical integration and geographical proximity to Europe key comparative advantages. New investments are being made by international textile firms confirming this view. Nevertheless, difficulties are ahead for textiles in Morocco, but the strong external position can withstand shocks to the textile industry.

F. Other Issues

37. **A fiscal ROSC was conducted in May 2004 and found that the authorities complied with most fiscal transparency requirements.** Main recommendations to improve transparency, which the authorities are already implementing, were to: (a) put in place a medium-term budget framework and performance budgeting system; (b) evaluate government contingent liabilities; (c) extend budget coverage to local governments and nonmarket public enterprises, including *Fonds Hassan II*; and (d) increase accountability through timely reporting and audit of budget execution. The authorities plan to publish the fiscal ROSC.

38. **Morocco's statistical database is appropriate for surveillance.** A STA mission overlapped with the Article IV consultations to review the authorities' progress towards meeting SDDS subscription. The STA mission concluded that Morocco could subscribe to the SDDS by October 2005 if the agreed action plan is fully implemented, which the mission determined was within reach.

IV. Staff Appraisal

39. **Macroeconomic conditions remain stable in Morocco.** In recent years, the external current account has remained in surplus and gross official reserves have increased. The balance of payments surpluses have contributed to abundant liquidity in the financial system and a decline in interest rates, which were appropriately accommodated given the low inflation rate. This has facilitated the financing of high fiscal deficits at low costs without constraining private credit and undermining macroeconomic stability. With additional privatization receipts and debt/equity swaps, the public debt-to-GDP ratio continued to decline.

40. **Growth continues to be volatile and insufficient to reduce unemployment and poverty.** Overall growth has been volatile because agriculture is dominated by cereal production which is highly vulnerable to droughts. In recent years, private domestic demand supported by strong remittances flows and declining interest rates has been the primary source of growth.

41. **Shifting the Moroccan economy to a sustainable higher growth path remains the key challenge.** A set of mutually reinforcing policies could help meet this challenge in the context of Morocco's increasing integration into the world economy. First, macroeconomic stability should be maintained and the fiscal position should be put on a sustainable path. Second, structural reforms should be accelerated to render the business environment internationally competitive and foster productivity and private investment. Finally, a gradual transition to a flexible exchange rate regime would be desirable to support the economy as it goes through structural transformation, faces greater international competition, and integrates financially. However, it is difficult to forecast precisely the magnitude and the timing of the impact of these policies on the growth performance. Thus, sustained high rates of growth may not be achieved for some time.

42. **Fiscal consolidation is essential in the medium term.** Although the current fiscal stance and public debt level do not pose a risk to macroeconomic stability in the short term, current policies would not place public finances on a sustainable path. Therefore, the staff welcomes the authorities' objective of reducing the deficit to 3 percent of GDP by 2009. The achievement of this objective and its compatibility with a high growth scenario will require: (a) a reform of the tax system that will widen the tax base and allow a reduction in tax rates; (b) a containment of public salary increases, which affect private sector wages and the competitivity of Moroccan producers, and a reduction in the wage bill-to-GDP ratio, which will enhance the flexibility of the budget including to dampen income and consumption volatilities; (c) an overhaul of the food subsidy system and its replacement by targeted support to vulnerable groups, which should lead to a diversification of agricultural production and more stable income and consumption levels in rural areas; and (d) the implementation of the petroleum price adjustment mechanism, which will release resources to be channeled to more productive investments. In order to buttress private sector confidence in the maintenance of macroeconomic stability, it is important to avoid slippages in fiscal consolidation.

43. **The authorities have recently made commendable progress in implementing structural reforms,** most importantly related to trade liberalization, the financial sector, public enterprises, and the labor market. However, much remains to be done to strengthen private activity and enhance productivity. Therefore, it is encouraging that the authorities are determined to move expeditiously with a broad-based structural reform agenda.

44. **The authorities intend to fully exploit the benefits of trade integration.** To this end, the staff encourages the authorities to simplify the tariff structure, reduce tariffs, and eliminate variable tariff rates in parallel with the reform of the food subsidy system. The authorities' efforts to liberalize trade at the regional level should help establish a large regional market and attract foreign investment.

45. **Improving the business environment should increase the growth potential.** To this end, the authorities have initiated important reforms. The staff encourages effective implementation of the new labor code and the law on domestic competition, and speedy progress with reform of the judicial system. In an effort to improve the business environment, provision of exemptions or special incentives in favor of specific sectors should be avoided.

46. **The financial system remains sound, but needs to be further strengthened.** Non performing loans, although stabilized, remain high. Progress was made in the restructuring of

specialized banks, but it is imperative that all banks be brought to comply with prudential regulations as early as possible. Significant progress was made in the implementation of FSAP recommendations to strengthen banking supervision. The promulgation of the new central bank and banking laws will further enhance the supervisory power of BAM. The authorities' intentions to implement the remaining FSAP recommendations and further reform the financial sector with an adjustment loan from the World Bank are welcomed. It is also essential to remove the structural constraints to enhance the availability and reduce the cost of credit to SMEs, which represent the core of Morocco's enterprise sector.

47. **The current fixed exchange rate regime has served Morocco well and there are no signs of misalignment of the dirham.** However, forward-looking considerations, in particular the increasing opening of the Moroccan economy and the envisaged structural reforms to increase efficiency and productivity, favor a gradual transition to a flexible exchange rate. The review the authorities are undertaking of the pros and cons of alternative regimes is very timely. The staff welcomes the openness of the authorities to the idea of a possible gradual move to a flexible exchange rate regime.

48. **Morocco's economic data base is sufficient for conducting effective surveillance.** Authorities have made important progress toward meeting SDDS standards. The staff encourages the authorities to implement the agreed action plan expeditiously to enable Morocco to subscribe to the SDDS by October 2005.

49. It is recommended that the next Article IV consultation be conducted on the standard 12-month cycle.

Table 1. Morocco: Selected Economic and Financial Indicators, 2000–05

Quota: SDR 588.20 million
Population: 29.8 million
Per capita income: US$ 1,677 (2004)

	2000	2001	2002	2003	2004 Prel.	2005 Proj.
	(Annual percentage change; unless otherwise indicated)					
Production and income						
Nominal GDP	2.5	8.2	3.8	5.5	5.8	2.8
Real GDP	1.0	6.3	3.2	5.5	4.2	1.0
Real nonagricultural GDP	3.6	3.6	2.8	3.5	4.7	4.0
GDP deflator	1.5	1.8	0.6	-0.1	1.5	1.8
Consumer price index (CPI), average	1.9	0.6	2.8	1.2	1.5	2.0
	(In billions of U.S. dollars; unless otherwise indicated)					
External sector						
Exports of goods, f.o.b.	7.4	7.1	7.8	8.8	9.7	10.2
Exports of goods, f.o.b. (percent change)	-1.2	-3.7	9.8	11.8	11.2	4.6
Imports of goods, f.o.b.	10.7	10.2	10.9	13.1	16.2	18.7
Imports of goods, f.o.b. (percent change)	7.0	-4.6	7.2	20.1	23.9	15.2
Oil imports f.o.b.	1.4	1.3	1.2	1.0	1.6	2.2
Net services and income	0.3	1.1	1.2	1.8	2.7	3.0
Net transfers	2.5	3.6	3.3	4.1	4.9	5.1
Current account (in percent of GDP)	-1.4	4.8	4.1	3.6	2.2	-0.9
Overall balance (deficit -)	-0.4	3.8	0.6	1.6	1.8	0.2
	(In percent of GDP)					
Central government						
Revenue, excluding grants and privatization	26.2	25.0	24.7	24.5	25.1	26.4
Total expenditure (including *Fonds Hassan II*)	32.4	31.1	29.9	30.3	30.9	32.4
Overall balance 1/	-6.4	-5.7	-4.7	-5.3	-4.9	-5.5
Privatization and GSM receipts	0.0	6.1	0.2	2.9	2.3	2.6
Overall balance, incl. privatization 1/	-6.4	0.4	-4.5	-2.5	-2.6	-2.9
	(Annual percentage change; unless otherwise indicated)					
Money and credit						
Broad money	8.4	14.2	6.3	8.6	7.5	5.8
Interest rate (Avg, money market rate, in percent)	5.4	4.4	3.0	3.2	2.4	...
Official reserves						
Gross official reserves (in billions of US$, end-period)	4.8	8.4	10.1	13.9	16.3	16.0
In months of imports of goods and services	4.6	8.2	9.1	10.4	10.0	8.6
Debt (short, medium and long term)						
Total external debt (in billions of US$)	18.0	15.9	15.7	16.8	16.6	16.0
Total external debt (in percent of GDP)	55.0	47.8	40.9	35.1	30.8	30.2
Domestic government debt (in percent of GDP) 2/	47.3	45.8	48.1	50.1	49.9	55.2
Total government debt (in percent of GDP) 2/	81.5	74.7	71.4	68.5	65.8	69.9
Memorandum items:						
GDP at current prices (in billions of DH)	354.2	383.2	397.8	419.5	443.7	456.0
GDP at current prices (in billions of US$)	33.3	33.9	36.1	43.8	50.0	...
Exchange rate: dirham/US$ (average period)	10.63	11.30	11.02	9.57	8.87	...
Real effective exchange rate (appreciation +)	2.8	-4.1	-0.3	-1.3	-0.6	...
Terms of trade (deterioration -)	-7.7	7.6	-7.3	5.7	-10.8	-3.1
Excluding oil	-2.4	7.9	-8.6	8.5	-10.3	-0.5
Unemployment rate (in percent)	13.7	12.8	12.5	11.4	10.8	...
Urban	21.5	20.3	18.0	19.3	18.4	...
Rural	5.2	4.2	6.2	3.4	3.1	...

Sources: Data provided by the Moroccan authorities; and Fund staff projections.
1/ Commitment basis including *Fonds Hassan II*.
2/ Gross debt including net central bank credit.

Table 2. Morocco: Balance of Payments, 2001–05
(In millions of U.S. dollars; unless otherwise indicated)

				Est.	Proj.
	2001	2002	2003	2004	2005
Current account	1,611	1,477	1,591	1,109	-455
Trade balance	-3,022	-3,061	-4,334	-6,489	-8,505
Exports, f.o.b.	7,142	7,839	8,762	9,739	10,191
Agriculture	1,477	1,648	1,825	1,532	1,633
Phosphates and derived products	1,171	1,160	1,241	1,625	1,819
Imports, f.o.b.	-10,164	-10,900	-13,095	-16,228	-18,696
Petroleum	1,282	1,167	963	1,639	2,157
Capital goods	2,042	2,378	3,131	3,881	4,189
Food products	1,363	1,374	1,194	1,534	2,461
Services	1,910	1,946	2,617	3,388	3,724
Tourism receipts	2,583	2,646	3,225	3,920	4,267
Income	-832	-738	-790	-651	-740
Transfers	3,555	3,330	4,098	4,861	5,066
Private transfers (net)	3,535	3,223	4,017	4,729	4,957
Workers' remittances	3,261	2,877	3,612	4,218	4,459
Official grants (net)	20	107	81	132	109
Capital account	91	84	-10	-8	-6
Financial account	2,011	-644	374	982	680
Direct investment 1/	2,727	452	2,302	822	1,316
Privatization	2,068	0	1,471	0	1,442
Portfolio investment 2/	-7	-8	8	529	9
Other	-709	-1,089	-1,936	-370	-645
private 3/	370	205	-798	781	-220
Public medium- and long-term loans (net)	-1,079	-1,294	-1,139	-1,151	-425
Disbursements	628	661	1,409	925	1,338
Amortization	-1,707	-1,956	-2,548	-2,076	-1,763
Reserve asset accumulation (-increase)	-3,848	-638	-1,643	-1,835	-220
Errors and omissions	131	-297	-341	-268	0
Memorandum items:					
Exports of goods' volume (percentage change)	5.7	11.1	-6.9	5.7	2.1
Imports of goods' volume (percentage change)	11.6	1.0	5.9	5.7	9.2
Trade balance (in percent of GDP)	-8.9	-8.5	-9.9	-13.0	-16.0
Current account balance (in percent of GDP)	4.8	4.1	3.6	2.2	-0.9
Excluding official grants (in percent of GDP)	4.7	3.8	3.4	2.0	-1.1
Terms of trade (percentage change)	7.6	-7.3	5.7	-10.8	-3.1
Excluding oil	7.9	-8.6	8.5	-10.3	-0.5
Impact of US$1 increase in oil prices (US$, mlns)	52.7	46.8	33.3	43.4	45.5
Gross official reserves 4/	8,431	10,107	13,858	16,346	16,021
(In months of imports of goods and nonfactor services)	8.2	9.1	10.4	10.0	8.6
Debt service as percentage of export of goods, nonfactor services and MRE 5/	16.3	16.4	18.0	12.8	10.6
External public and publicly guaranteed debt (US$, blns)	14.1	13.9	14.4	14.0	13.6
In percent of GDP	42.2	36.3	30.1	26.0	25.7
DHs per US$, period average	11.30	11.02	9.57	8.87	...
DHs per US$, period end	11.51	10.38	8.75	8.22	...
Oil price (US$/barrel)	24.3	25.0	28.9	37.8	47.4

Sources: Ministry of Finance; *Office des Changes;* and Fund staff estimates and projections.

1/ In 2005, a nonresident company (Vivendi) sold part of its shares in Maroc Télécom to a resident company.
2/ The increase in 2004 is due to a sale of government shares of Maroc Télécom in the Casablanca and Paris stock exchange.
3/ Includes the loans that Moroccan banks gave in 2003 and will give in 2005 to the company (Vivendi) that bought part of Maroc Télécom in 2003 and additional shares in 2005.
4/ Excluding the reserve position in the Fund.
5/ Public and publicly guaranteed debt.

Table 3. Morocco: Central Government Finance, 2001–05 1/

	2001	2002	2003	Budget 2004	Est. 2004	Budget 2005	Proj. 2005
				(In billions of dirhams)			
Revenue 2/	95.8	98.3	102.9	103.4	111.3	110.9	120.6
Tax revenue 2/	87.4	91.0	94.2	95.3	100.8	101.7	110.4
Direct taxes	28.4	30.4	33.1	33.2	36.5	37.2	39.5
Indirect taxes	39.2	40.1	41.9	42.6	43.9	44.9	47.8
Import taxes	14.0	14.2	12.6	12.1	13.3	11.9	16.1
Other tax revenues	5.8	6.4	6.6	7.4	7.1	7.7	7.0
Nontax revenue (excl. privatization)	8.4	7.2	8.6	8.1	10.6	9.2	10.2
Expenditures and net lending (excl. *Fonds Hassan II*)	119.3	117.9	125.4	128.8	135.5	136.0	144.2
Current expenditures	90.4	90.7	97.5	100.4	105.0	107.0	115.0
Wages	48.0	48.6	53.2	55.4	56.6	60.8	61.5
Food and petroleum subsidies 3/	5.1	4.0	4.9	3.4	7.8	3.4	8.8
Interest	18.8	17.6	17.4	17.5	17.4	17.3	17.2
Other current spending	18.5	20.5	22.1	24.1	23.2	25.5	27.5
Capital expenditures (budget) 4/	20.4	19.3	18.6	18.2	20.5	17.9	17.9
Road fund	0.9	1.0	1.1	2.1	1.6	2.2	1.5
Transfers to local governments 5/	7.0	7.2	7.8	8.2	8.7	9.0	9.8
Net lending	0.6	-0.3	0.2	0.0	-0.3	0.0	0.0
Balance of other special treasury accounts	2.1	1.8	1.9	0.0	3.6	0.0	2.0
Overall balance (commitment basis, excl. *Fonds Hassan II*)	-21.4	-17.8	-20.6	-25.4	-20.6	-25.1	-21.6
Fonds Hassan II expenditures	0.6	0.9	1.8	4.4	1.2	2.0	3.6
Overall balance (commitment basis, incl. *Fonds Hassan II*)	-22.0	-18.6	-22.4	-29.8	-21.9	-27.1	-25.2
Grants	0.3	0.3	0.4	1.4	1.3	0.7	0.7
Privatization and GSM revenues	23.4	0.6	12.0	12.0	10.4	12.0	12.0
Change in arrears	-11.0	-0.2	-2.1	0.0	2.0	-13.8	-14.1
Overall balance (cash basis, incl. *Fonds Hassan II*, grants & privatization)	-9.3	-18.0	-12.1	-16.3	-8.2	-28.2	-26.6
Financing	9.3	18.0	12.1	16.3	8.2	28.2	26.6
Domestic financing	19.4	29.7	21.3	22.8	15.9	31.6	30.1
External financing 5/	-10.1	-11.7	-9.2	-6.4	-7.7	-3.4	-3.4
Memorandum items:							
Current balance	5.4	7.6	5.3	3.1	6.3	3.9	5.6
Primary balance	-3.2	-1.0	-5.1	-12.3	-4.5	-9.8	-8.0
Primary balance (incl. grants and privatization)	20.4	-0.1	7.3	1.2	7.2	2.9	4.7
Total central government debt (end period) 6/	286.2	284.0	287.3	303.6	292.1	331.3	318.7
Domestic 6/	175.6	191.2	210.3	233.1	221.6	0.0	...
External	110.6	92.8	77.0	70.6	70.5	0.0	...
GDP in billions of dirhams	383.2	397.8	419.5	443.7	443.7	456.0	456.0

Table 3. Morocco: Central Government Finance, 2001–05 (concluded) 1/

	2001	2002	Est. 2003	Budget 2004	Est. 2004	Budget 2005	Proj. 2005
	(In percent of GDP)						
Revenue 2/	25.0	24.7	24.5	23.3	25.1	24.3	26.4
Tax revenue 2/	22.8	22.9	22.5	21.5	22.7	22.3	24.2
Direct taxes	7.4	7.6	7.9	7.5	8.2	8.2	8.7
Indirect taxes	10.2	10.1	10.0	9.6	9.9	9.9	10.5
Import taxes	3.7	3.6	3.0	2.7	3.0	2.6	3.5
Other tax revenues	1.5	1.6	1.6	1.7	1.6	1.7	1.5
Nontax revenue (excl. privatization)	2.2	1.8	2.1	1.8	2.4	2.0	2.2
Expenditures and net lending (excl. *Fonds Hassan II*)	31.1	29.6	29.9	29.0	30.5	29.8	31.6
Current expenditures	23.6	22.8	23.3	22.6	23.7	23.5	25.2
Wages	12.5	12.2	12.7	12.5	12.8	13.3	13.5
Food and petroleum subsidies 3/	1.3	1.0	1.2	0.8	1.8	0.7	1.9
Interest	4.9	4.4	4.1	3.9	3.9	3.8	3.8
Other current spending	4.8	5.1	5.3	5.4	5.2	5.6	6.0
Capital expenditures (budget) 4/	5.3	4.8	4.4	4.1	4.6	3.9	3.9
Road fund	0.2	0.2	0.3	0.5	0.4	0.5	0.3
Transfers to local governments 5/	1.8	1.8	1.9	1.8	2.0	2.0	2.2
Net lending	0.2	-0.1	0.1	0.0	-0.1	0.0	0.0
Balance of other special treasury accounts	0.5	0.5	0.5	0.0	0.8	0.0	0.4
Overall balance (commitment basis, excl. *Fonds Hassan II*)	-5.6	-4.5	-4.9	-5.7	-4.6	-5.5	-4.7
Fonds Hassan II expenditures	0.2	0.2	0.4	1.0	0.3	0.4	0.8
Overall balance (commitment basis, incl. *Fonds Hassan II*)	-5.7	-4.7	-5.3	-6.7	-4.9	-5.9	-5.5
Grants	0.1	0.1	0.1	0.3	0.3	0.2	0.2
Privatization and GSM revenues	6.1	0.2	2.9	2.7	2.3	2.6	2.6
Change in arrears	-2.9	-0.1	-0.5	0.0	0.4	-3.0	-3.1
Overall balance (cash basis, incl. *Fonds Hassan II* , grants & privatization)	-2.4	-4.5	-2.9	-3.7	-1.8	-6.2	-5.8
Financing	2.4	4.5	2.9	3.7	1.8	6.2	5.8
Domestic financing	5.1	7.5	5.1	5.1	3.6	6.9	6.6
External financing	-2.6	-2.9	-2.2	-1.5	-1.7	-0.8	-0.8
Memorandum items							
Current balance	1.4	1.9	1.3	0.7	1.4	0.9	1.2
Primary balance	-0.8	-0.3	-1.2	-2.8	-1.0	-2.1	-1.8
Primary balance (incl. grants and privatization)	5.3	0.0	1.7	0.3	1.6	0.6	1.0
Total Central Government debt (end period) 6/	74.7	71.4	68.5	68.4	65.8	72.7	69.9
Domestic 6/	45.8	48.1	50.1	52.5	49.9	...	...
External	28.9	23.3	18.4	15.9	15.9	...	...

Sources: Ministry of Finance; and Fund staff estimates and projections.

1/ Including *Fonds Hassan II.*

2/ Includes tariffs earmarked for food subsidies (*équivalents tarifaires)* and revenues of the road fund *(Fonds Routier).*

3/ Includes food subsidies financed from earmarked tariffs *(équivalents tarifaires).*

4/ Budgetary capital expenditures excluding *Fonds Routier* and investment spending by the *Fonds Hassan II* .

5/ Corresponds to 30 percent of VAT revenue.

6/ Gross debt including net central bank credit.

Table 4. Morocco: Selected Vulnerability Indicators, 2000–05

	2000	2001	2002	2003	2004	2005 1/	Latest observation
Key economic and market indicators							
Real GDP growth (in percent)	1.0	6.3	3.2	5.5	4.2	1.0	Proj
CPI inflation (period average, in percent)	1.9	0.6	2.8	1.2	1.5	2.0	Proj
Short-term (ST) interest rate (in percent)	5.4	4.6	3.0	3.2	2.4	...	31-Dec-04
EMBI secondary market spread (bps, end of period)	584	518	390	160	170	159	30-May-05
Exchange rate NC/US$ (end of period)	10.8	11.5	10.4	8.7	8.2	...	31-Dec-04
External sector							
Exchange rate regime	(Peg to a basket of currencies dominated by the Euro)						
Current account balance (percent of GDP)	-1.4	4.8	4.1	3.6	2.2	-0.9	Proj
Net FDI inflows (percent of GDP)	1.1	8.0	1.3	5.3	1.6	2.5	Proj
Exports (percentage change of US$ value, GNFS)	-1.6	6.9	9.2	16.7	16.4	5.8	Proj
Real effective exchange rate (1995= 100)	108.2	103.7	103.4	102.0	101.4	101.3	Proj
Gross international reserves (GIR) in US$ billion	4.8	8.4	10.1	13.9	16.3	16.0	Proj
GIR in percent of ST debt at remaining maturity (RM)	177.3	291.6	360.0	626.8	533.8	512.5	Proj
GIR in percent of ST debt at RM and banks' FX deposits	174.7	286.1	353.5	599.6	521.4	500.4	Proj
Net international reserves (NIR) in US$ billion	4.6	8.3	9.9	13.6	16.1	15.8	Proj
Total gross external debt (ED) in percent of GDP	55.0	47.8	41.0	35.1	30.8	30.2	Proj
o/w ST external debt (original maturity, in percent of total ED	5.3	5.8	5.6	0.8	7.8	7.4	Proj
o/w ED of domestic private sector (in percent of total ED)	10.7	11.6	11.3	14.2	15.6	14.9	Proj
ED to foreign official sector (in percent of total ED)	71.1	71.1	72.8	70.0	70.0	70.0	Proj
Total gross external debt in percent of exports of GNFS	171.9	142.5	128.8	118.1	100.3	91.1	Proj
Gross external financing requirement (in US$ billion) 2/	2.9	0.1	0.5	1.0	1.0	2.2	Proj
Public Sector (PS) 3/							
Overall balance (percent of GDP)	-6.4	-5.7	-4.7	-5.3	-4.9	-5.5	Proj
Primary balance (percent of GDP)	-1.1	-0.8	-0.3	-1.2	-1.0	-1.8	Proj
Debt-stabilizing primary balance (percent of GDP) 4/	3.2	-1.3	1.8	0.4	0.1	1.9	Proj
Gross PS financing requirement (in percent of GDP) 5/	17.4	22.6	18.4	24.0	20.2	21.9	Proj
Public sector gross debt (PSGD, in percent of GDP)	76.4	74.8	71.5	68.8	66.4	69.9	Proj
o/w Exposed to rollover risk (in percent of total PSGD) 6/	9.4	18.0	13.7	21.3	19.1	19.9	Proj
o/w Exposed to exchange rate risk (in percent of total PSGD) 7	44.8	38.6	32.6	26.7	23.6	20.4	Proj
o/w Exposed to interest rate risk (in percent of total PSGD) 8/	13.6	22.6	19.2	27.3	22.9	23.1	Proj
Public sector net debt (in percent of GDP) 11/	81.5	74.7	71.4	68.5	65.8	69.9	Proj
Financial Sector (FS) 9/							
Capital adequacy ratio (in percent)	12.8	12.6	12.2	9.3	10.2	...	Dec-04
NPLs in percent of total loans	17.5	16.8	17.2	18.1	19.4	...	Dec-04
Provisions in percent of NPLs	47.8	52.9	54.7	54.9	59.3	...	Dec-04
Return on average assets (in percent)	0.7	0.9	0.3	-0.2	0.8	...	Dec-04
Return on equity (in percent)	8.1	10.2	1.9	-2.1	10.9 ...		Dec-04
FX deposits held by residents (in percent of total deposits)	0.2	0.3	0.2	0.3	0.2		Dec-04
FX loans to residents (in percent of total loans)	1.0	1.1	1.4	1.5	2.2		Dec-04
Net open forex position (in percent of capital) 10/	5.8	4.4	3.3	4.0	9.2	...	
Government debt held by FS (percent of total FS assets)	21.4	23.0	23.2	21.4	18.7	...	Dec-04
Credit to private sector (percent change)	7.9	4.0	3.8	8.3	7.2	9.1	Proj.
Memorandum item:							
Nominal GDP in billions of U.S. dollars	33.3	33.9	36.1	43.8	50.0	...	Dec-04

Sources: Moroccan authorities; and Fund staff estimates.

1/ Staff estimates, projections, or latest available observations as indicated in the last column.
2/ Current account deficit plus amortization of external debt.
3/ Public sector covers: central government.
4/ Based on averages for the last five years for the relevant variables (i.e., growth, interest rates).
5/ Overall balance plus debt amortization.
6/ ST debt and maturing medium- and long-term debt, domestic and external, excluding external debt to official creditors.
7/ Debt in foreign currency or linked to the exchange rate, domestic and external, excluding external debt on concessional terms.
8/ ST debt and maturing medium- and long-term debt at variable interest rates, domestic and external.
9/ Financial sector includes banks.
10/ Sum of on- and off-balance sheet exposure.
11/ Gross debt including net central bank credit to government.

Table 5. Morocco: Public Sector Debt Sustainability Framework, 2000–10

(In percent of GDP; unless otherwise indicated)

	Actual							Projections						
	2000	2001	2002	2003	2004			2005	2006	2007	2008	2009	2010	
								I. Baseline Projections						**Debt-stabilizing primary balance 10/**
Public sector debt 1/	81.5	74.7	71.4	68.5	65.8			**69.9**	**67.8**	**66.8**	**64.8**	**62.5**	**59.9**	**-0.8**
o/w foreign-currency denominated	34.2	28.9	23.3	18.8	16.1			14.9	12.8	11.2	9.6	8.2	6.9	
Change in public sector debt	0.2	-6.8	-3.3	-2.9	-2.7			4.1	-2.0	-1.0	-2.0	-2.3	-2.6	
Identified debt-creating flows (4+7+12)	7.3	-4.6	-1.1	-4.9	-2.6			0.3	-2.0	-1.0	-2.0	-2.3	-2.6	
Primary deficit	1.1	0.8	0.2	1.1	0.7			1.6	-0.4	-0.5	-1.2	-1.5	-1.8	
Revenue and grants	26.2	25.1	24.8	24.6	25.4			26.6	26.1	26.2	26.2	26.3	26.4	
Primary (noninterest) expenditure	27.3	25.8	25.0	25.7	26.1			28.2	25.7	25.6	25.0	24.8	24.6	
Automatic debt dynamics 2/	6.2	0.8	-1.1	-3.1	-0.9			1.3	-1.1	-0.1	-0.4	-0.5	-0.5	
Contribution from interest rate/growth differential 3/	3.3	-1.3	1.7	0.4	0.2			2.0	-1.1	-0.1	-0.4	-0.5	-0.5	
Of which: contribution from real interest rate	4.1	3.5	4.0	4.2	2.9			2.6	2.7	2.7	2.7	2.6	2.6	
contribution from real GDP growth	-0.8	-4.7	-2.3	-3.7	-2.7			-0.6	-3.8	-2.8	-3.1	-3.1	-3.1	
Contribution from exchange rate depreciation 4/	2.9	2.0	-2.8	-3.6	-1.1			-0.7	0.0	0.0	0.0	0.0	0.0	
Other identified debt-creating flows	0.0	-6.1	-0.2	-2.9	-2.4			-2.6	-0.6	-0.4	-0.4	-0.3	-0.3	
Privatization receipts (negative)	0.0	-6.1	-0.2	-2.9	-2.4			-2.6	-0.6	-0.4	-0.4	-0.3	-0.3	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes (2-3) and arrears flows	-7.1	-2.2	-2.2	2.0	0.0			3.8	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 1/	310.7	297.8	288.3	278.1	259.4			262.7	259.9	255.4	247.2	237.8	227.3	
Gross financing need 5/	22.6	21.6	21.0	22.5	20.5			21.2	19.8	19.7	19.0	18.4	17.6	
in billions of U.S. dollars	7.5	7.3	7.6	9.9	10.2			11.2	11.3	12.0	12.3	12.8	13.3	
Key Macroeconomic and Fiscal Assumptions						10-Year Historical Average	10-Year Standard Deviation							Projected Average
Real GDP growth (in percent)	1.0	6.3	3.2	5.5	4.2	3.1	5.4	1.0	5.9	4.5	5.0	5.1	5.3	4.4
Average nominal interest rate on public debt (in percent) 6/	6.7	6.5	6.2	6.1	6.1	6.5	0.3	5.9	6.3	6.4	6.4	6.5	6.5	6.3
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	5.1	4.7	5.6	6.2	4.6	4.7	2.2	4.1	4.3	4.4	4.4	4.5	4.5	4.4
Nominal appreciation (increase in US dollar value of local currency, in percent)	-7.3	-5.8	10.9	18.6	6.5	1.3	9.4	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	1.5	1.8	0.6	-0.1	1.5	1.7	2.3	1.8	2.0	2.0	2.0	2.0	2.0	2.0
Growth of real primary spending (deflated by GDP deflator, in percent)	13.4	0.6	-0.4	8.8	5.7	4.7	6.7	9.2	-3.4	4.0	2.6	4.1	4.3	3.4
Primary deficit	1.1	0.8	0.2	1.1	0.7	-0.5	1.6	1.6	-0.4	-0.5	-1.2	-1.5	-1.8	-0.6
								II. Stress Tests for Public Debt Ratio						**Debt-stabilizing primary balance 10/**
A. Alternative Scenarios														
A1. Key variables are at their historical averages in 2005–09 7/								**69.9**	**69.8**	**69.9**	**70.0**	**70.2**	**70.4**	**0.7**
A2. No policy change (constant primary balance) in 2005–09								**69.9**	**70.0**	**71.2**	**72.0**	**72.7**	**73.5**	**-0.9**
B. Bound Tests														
B1. Real interest rate is at historical average plus two standard deviations in 2005 and 2006								**69.9**	**70.9**	**73.0**	**71.0**	**68.6**	**66.0**	**-0.8**
B2. Real GDP growth is at historical average minus two standard deviations in 2005 and 2006								**69.9**	**81.5**	**98.5**	**103.6**	**108.2**	**112.4**	**-1.3**
B3. Primary balance is at historical average minus two standard deviations in 2005 and 2006								**69.9**	**70.9**	**73.2**	**71.2**	**68.8**	**66.2**	**-0.8**
B4. Combination of B1-B3 using one standard deviation shocks								**69.9**	**76.8**	**84.5**	**82.4**	**79.9**	**77.1**	**-1.0**
B5. One time 30 percent real depreciation in 2005 9/								**69.9**	**74.5**	**73.5**	**71.5**	**69.1**	**66.5**	**-0.8**
B6. 10 percent of GDP increase in other debt-creating flows in 2005								**69.9**	**77.8**	**76.8**	**74.8**	**72.4**	**69.7**	**-0.9**

1/ Public sector debt refers to central government gross debt including net debt to the central bank (excludes arrears on which reliable data is not available).

2/ Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ε = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the numerator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as -g.

4/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.

5/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

6/ Derived as nominal interest expenditure divided by previous period debt stock.

7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8/ The implied change in other key variables under this scenario is discussed in the text.

9/ Real depreciation is defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

10/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Table 6. Morocco: Central Government Finance, 2004–10 1/

	Budget	Est.	Budget	Projections					
	2004	2004	2005	2005	2006	2007	2008	2009	2010
	(In billions of dirhams)								
Revenue 2/	103.4	111.3	110.9	120.6	127.6	136.3	146.4	157.5	169.6
Tax revenue 2/	95.3	100.8	101.7	110.4	117.7	125.8	135.2	145.5	156.7
Direct taxes	33.2	36.5	37.2	39.5	42.7	45.5	48.7	52.2	56.1
Indirect taxes	42.6	43.9	44.9	47.8	51.2	55.1	59.7	64.7	70.1
Import taxes	12.1	13.3	11.9	16.1	16.3	17.1	18.1	19.3	20.5
Other tax revenues	7.4	7.1	7.7	7.0	7.6	8.1	8.7	9.3	10.0
Nontax revenue (excl. privatization)	8.1	10.6	9.2	10.2	9.8	10.5	11.2	12.0	12.9
Expenditures and net lending (excl. *Fonds Hassan II*)	128.8	135.5	136.0	144.2	146.3	155.2	162.8	172.7	183.4
Current expenditures	100.4	105.0	107.0	115.0	112.4	116.3	119.4	124.2	129.2
Wages	55.4	56.6	60.8	61.5	61.8	62.6	63.1	64.4	65.7
Food and petroleum subsidies 3/	3.4	7.8	3.4	8.8	2.0	1.0	0.0	0.0	0.0
Interest	17.5	17.4	17.3	17.2	20.1	21.2	22.5	23.6	24.6
Other current spending	24.1	23.2	25.5	27.5	28.6	31.5	33.7	36.1	38.8
Capital expenditures (budget) 4/	18.2	20.5	17.9	17.9	21.7	25.8	29.3	33.2	37.6
Road fund	2.1	1.6	2.2	1.5	1.7	1.8	1.9	2.1	2.2
Transfers to local governments 5/	8.2	8.7	9.0	9.8	10.5	11.3	12.3	13.3	14.4
Net lending	0.0	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Balance of other special treasury accounts	0.0	3.6	0.0	2.0	1.5	1.6	1.7	1.8	1.9
Overall balance (commitment basis, excl. *Fonds Hassan II*)	-25.4	-20.6	-25.1	-21.6	-17.2	-17.4	-14.7	-13.4	-11.8
Fonds Hassan II expenditures	4.4	1.2	2.0	3.6	2.0	2.0	2.0	2.0	2.0
Overall balance (commitment basis, incl. *Fonds Hassan II*)	-29.8	-21.9	-27.1	-25.2	-19.2	-19.4	-16.7	-15.4	-13.8
Grants	1.4	1.3	0.7	0.7	1.0	1.0	1.0	1.0	1.0
Privatization and GSM revenues	12.0	10.4	12.0	12.0	3.0	2.0	2.0	2.0	2.0
Change in arrears	0.0	2.0	-13.8	-14.1	0.0	0.0	0.0	0.0	0.0
Overall balance (cash basis, incl. *Fonds Hassan II* , grants & privatization)	-16.3	-8.2	-28.2	-26.6	-15.2	-16.4	-13.7	-12.4	-10.8
Financing	16.3	8.2	28.2	26.6	15.2	16.4	13.7	12.4	10.8
Domestic financing	22.8	15.9	31.6	30.1	19.9	21.0	18.3	17.0	15.4
External financing 5/	-6.4	-7.7	-3.4	-3.4	-4.6	-4.6	-4.6	-4.6	-4.6
Memorandum items:									
Current balance	3.1	6.3	3.9	5.6	15.2	19.9	27.1	33.3	40.5
Primary balance	-12.3	-4.5	-9.8	-8.0	0.8	1.9	5.8	8.2	10.8
Primary balance (incl. grants and privatization)	1.2	7.2	2.9	4.7	4.8	4.9	8.8	11.2	13.8
Total Central Government debt (end period) 6/	303.6	292.1	331.3	318.7	333.9	350.3	364.0	376.4	387.2
Domestic 6/	233.1	221.6	...	...	...	...	...	...	...
External	70.6	70.5	...	...	...	...	...	...	...
GDP in billions of dirhams	443.7	443.7	456.0	456.0	492.3	524.6	561.8	602.5	646.8

Table 6. Morocco: Central Government Finance, 2004–10 (concluded) 1/

	Budget 2004	Est. 2004	Budget 2005	Projections 2005	2006	2007	2008	2009	2010
	(In percent of GDP)								
Revenue 2/	23.3	25.1	24.3	26.4	25.9	26.0	26.1	26.1	26.2
Tax revenue 2/	21.5	22.7	22.3	24.2	23.9	24.0	24.1	24.1	24.2
Direct taxes	7.5	8.2	8.2	8.7	8.7	8.7	8.7	8.7	8.7
Indirect taxes	9.6	9.9	9.9	10.5	10.4	10.5	10.6	10.7	10.8
Import taxes	2.7	3.0	2.6	3.5	3.3	3.3	3.2	3.2	3.2
Other tax revenues	1.7	1.6	1.7	1.5	1.5	1.5	1.5	1.5	1.5
Nontax revenue (excl. privatization)	1.8	2.4	2.0	2.2	2.0	2.0	2.0	2.0	2.0
Expenditures and net lending (excl. *Fonds Hassan II*)	29.0	30.5	29.8	31.6	29.7	29.6	29.0	28.7	28.3
Current expenditures	22.6	23.7	23.5	25.2	22.8	22.2	21.2	20.6	20.0
Wages	12.5	12.8	13.3	13.5	12.5	11.9	11.2	10.7	10.2
Food and petroleum subsidies 3/	0.8	1.8	0.7	1.9	0.4	0.2	0.0	0.0	0.0
Interest	3.9	3.9	3.8	3.8	4.1	4.1	4.0	3.9	3.8
Other current spending	5.4	5.2	5.6	6.0	5.8	6.0	6.0	6.0	6.0
Capital expenditures (budget) 4/	4.1	4.6	3.9	3.9	4.4	4.9	5.2	5.5	5.8
Road fund	0.5	0.4	0.5	0.3	0.3	0.3	0.3	0.3	0.3
Transfers to local governments 5/	1.8	2.0	2.0	2.2	2.1	2.2	2.2	2.2	2.2
Net lending	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Balance of other special treasury accounts	0.0	0.8	0.0	0.4	0.3	0.3	0.3	0.3	0.3
Overall balance (commitment basis, excl. *Fonds Hassan II*)	-5.7	-4.6	-5.5	-4.7	-3.5	-3.3	-2.6	-2.2	-1.8
Fonds Hassan II expenditures	1.0	0.3	0.4	0.8	0.4	0.4	0.4	0.3	0.3
Overall balance (commitment basis, incl. *Fonds Hassan II*)	-6.7	-4.9	-5.9	-5.5	-3.9	-3.7	-3.0	-2.6	-2.1
Grants	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Privatization and GSM revenues	2.7	2.3	2.6	2.6	0.6	0.4	0.4	0.3	0.3
Change in arrears	0.0	0.4	-3.0	-3.1	0.0	0.0	0.0	0.0	0.0
Overall balance (cash basis, incl. *Fonds Hassan II*, grants & privatization)	-3.7	-1.8	-6.2	-5.8	-3.1	-3.1	-2.4	-2.1	-1.7
Financing	3.7	1.8	6.2	5.8	3.1	3.1	2.4	2.1	1.7
Domestic financing	5.1	3.6	6.9	6.6	4.0	4.0	3.3	2.8	2.4
External financing	-1.5	-1.7	-0.8	-0.8	-0.9	-0.9	-0.8	-0.8	-0.7
Memorandum items:									
Current balance	0.7	1.4	0.9	1.2	3.1	3.8	4.8	5.5	6.3
Primary balance	-2.8	-1.0	-2.1	-1.8	0.2	0.4	1.0	1.4	1.7
Primary balance (incl. grants and privatization)	0.3	1.6	0.6	1.0	1.0	0.9	1.6	1.9	2.1
Total Central Government debt (end period) 6/	68.4	65.8	72.7	69.9	67.8	66.8	64.8	62.5	59.9
Domestic 6/	52.5	49.9	...	...	...	...	...	...	...
External	15.9	15.9	...	...	...	...	...	...	...

Sources: Ministry of Finance; and Fund staff estimates and projections.

1/ Including *Fonds Hassan II.*

2/ Includes tariffs earmarked for food subsidies (*équivalents tarifaires)* and revenues of the road fund *(Fonds Routier).*

3/ Includes food subsidies financed from earmarked tariffs *(équivalents tarifaires).*

4/ Budgetary capital expenditures excluding *Fonds Routier* and investment spending by the *Fonds Hassan II*.

5/ Corresponds to 30 percent of VAT revenue.

6/ Gross debt including net central bank credit.

Table 7. Morocco: Revenue Structure and International Comparisons

	1990	1995	2000	2004
	(In percent of GDP)			
Total revenue	24.0	23.9	26.2	25.1
Tax revenue	21.8	22.0	24.1	22.7
Direct taxes	5.5	5.7	7.6	8.2
Indirect taxes	9.4	10.7	10.3	9.9
Customs duties	4.7	4.2	4.7	3.0
Other taxes	2.1	1.4	1.5	1.6
Nontax revenue	2.1	1.9	2.1	2.4
	(In percent of total revenue)			
Total revenue	100.0	100.0	100.0	100.0
Tax revenue	91.1	92.1	92.0	90.5
Direct taxes	23.2	24.0	28.9	32.8
Indirect taxes	39.3	44.7	39.5	39.4
Import taxes	19.7	17.6	17.9	11.9
Other taxes	8.9	5.8	5.7	6.4
Nontax revenue	8.9	7.9	8.0	9.5

(Tax revenue comparisons in percent of GDP) 1/

Average 1997–2001	OECD	Central Europe	Russia and CIS	Africa	Latin America	Asia	Middle East
Tax Revenue:	29.4	28.4	16.8	17.4	17.2	13.7	13.8
Direct taxes	9.8	5.5	2.1	4.8	3.8	4.4	4.9
Indirect taxes	10.0	11.8	8.2	4.8	7.2	5.3	3.9
Customs duties	0.6	1.2	1.3	6.8	3.1	3.1	3.1
Other	9.0	9.9	5.2	1.0	3.1	0.9	1.9

	Egypt		Iran		Jordan		Lebanon		Tunisia		Morocco	
	1990	2000	1990	2000	1990	2000	1990	2000	1990	2000	1990	2000
Tax Revenue	16.7	16.0	6.2	11.6	14.4	15.9	9.2	16.6	19.5	26.0	21.8	24.1
Direct taxes	4.4	6.0	2.4	3.8	4.3	4.5	1.3	2.9	3.3	5.6	5.5	7.6
Indirect taxes	3.1	6.0	0.7	3.8	2.7	8.1	0.8	9.3	6.6	11.1	9.4	10.3

Sources: Moroccan authorities; and Fund staff estimates.

1/ Crandall, W., and J-P Bodin, draft IMF Working Paper, "Revenue Administration in the Middle East."

Table 8. Morocco: Financial Soundness Indicators, 1998–2004

(In percent; unless otherwise indicated)

	1998	1999	2000	2001	2002	2003	2004
	Dec.	Dec.	Dec.	Dec.	Dec.	Dec.	Dec
Number of banks	21	21	21	19	18	18	17
Capital adequacy							
Regulatory capital to risk-weighted assets*	12.6	12.1	12.8	12.6	12.2	9.3	10.2
Commercial banks 1/	13.1	13.0	14.7	15.3	15.3	13.0	13.5
Regulatory Tier I capital to risk-weighted assets*	12.6	12.1	12.8	12.6	12.2	9.3	13.4
Capital (net worth) to assets	10.3	10.0	9.8	8.7	8.5	7.6	7.6
Asset composition and quality							
Sectoral distribution of loans to total loans*							
Agriculture	13.4	12.7	11.7	10.7	9.9	10.5	9.2
Housing and Public Works	19.3	19.5	19.2	18.9	20.1	22.4	25.2
Industry	17.6	15.5	15.6	15.8	17.7	19.6	18.8
Public administration	4.9	4.3	3.8	3.5	4.1	3.5	3.9
Commerce	9.6	9.9	9.9	9.4	8.4	8.3	7.7
Tourism	3.5	3.2	2.8	3.6	4.5	4.8	3.7
Other	31.7	34.9	37.0	38.1	35.4	30.9	31.5
Geographical distribution of loans to total loans							
Casablanca	62.9	64.8	56.7	56.7	56.3	54.1	57.9
Marrakech	3.5	3.2	3.9	3.6	3.9	4.3	4.0
Rabat	9.9	8.9	16.0	15.9	15.8	15.9	14.9
NPLs to gross loans*	14.6	15.3	17.5	16.8	17.2	18.1	19.4
Commercial banks 1/	8.9	9.1	9.1	10.7	11.2	12.3	12.4
NPLs net of provisions to capital*	44.9	49.3	70.5	55.5	57.1	66.5	61.9
Commercial banks	11.9	12.8	15.0	19.9	18.7	23.3	20.5
Provisioning ratio	61.6	51.9	47.8	52.9	54.7	54.9	59.3
Commercial banks	67.6	68.7	68.5	69.8	71.5	71.5	72.2
Large exposures to capital*	159.0	196.0	212.0	194.0	149.4	175.3	...
Earnings and profitability							
ROA*	0.9	0.7	0.7	0.9	0.3	-0.2	0.8
Commercial banks	1.1	1.1	1.1	1.1	0.6	0.5	0.9
ROE*	9.5	8.2	8.1	10.2	1.9	-2.1	10.9
Commercial banks	12.4	12.5	13.0	12.7	6.4	6.4	10.7
Interest margin to gross income*	15.0	73.4	80.0	77.8	82.0	82.4	80.7
Noninterest expenses to gross income*	46.8	47.4	49.1	46.2	53.4	53.4	51.2
Personnel expenses to noninterest expenses	29.0	27.5	26.0	26.8	22.5	19.8	20.0
Trading and fee income to total income	13.6	14.5	18.1	20.6	17.7	18.2	20.7
Spread between reference loan and deposit rates	5.5	5.3	5.1	4.8	4.5	4.2	...
Liquidity							
Liquid assets to total assets*	62.7	58.5	...	...	123.1	122.3	120.8
Liquid assets to total short-term liabilities*	24.1	22.9	20.4	22.7	26.9	30.5	28.9
Customer deposits to total (non-interbank) loans	113.5	112.0	113.4	120.3	125.9	127.8	131.7
FX liabilities to total liabilities	7.1	7.4	5.6	4.9	4.3	3.8	3.1
Average bid-ask spread in the securities market	3.8	6.0	4.6	6.6	...	...	...
Average daily turnover in the securities market	6.8	5.6	5.4	4.8	...	...	...
Sensitivity to market risk							
Net position in FX to capital*	...	2.1	5.8	4.4	3.3	4.0	9.2

Source: Moroccan authorities.

* Included in the "core set" of Financial Soundness Indicators.

1/ Excludes specialized government banks.

Table 9. Morocco: Monetary Survey, 2001–05

	2001	2002	2003	2004	Proj. 2005
	(In millions of dirhams)				
Net foreign assets	102,605	111,269	128,266	146,163	149,791
Monetary authorities	99,920	104,979	123,156	137,123	140,751
Of which:					
Gross reserves	96,640	101,760	120,012	134,001	137,629
Net Fund position	1,023	974	916	899	899
Deposit money banks	2,685	6,290	5,110	9,040	9,040
Net domestic assets	224,806	236,931	249,878	260,448	280,261
Domestic credit	294,257	305,944	323,629	334,166	352,240
Net credit to the government	85,610	89,470	89,098	82,725	77,799
Banking system	78,348	82,086	81,415	75,015	70,015
Bank Al-Maghrib	5,187	5,163	4,292	2,982	-2,018
o/w deposits 1/	-10,806	-11,322	-13,801	-15,484	-20,484
Deposit money banks	73,161	76,923	77,123	72,033	72,033
Treasury-IMF	-1,023	-974	-916	-899	-899
Credit to the economy	208,647	216,474	234,531	251,441	274,441
Other liabilities, net	69,451	69,013	73,751	73,718	71,979
Money and quasi money	327,411	348,200	378,144	406,611	430,052
Money	243,117	264,863	290,784	318,870	337,253
Currency outside banks	66,025	69,556	74,890	79,439	84,019
Demand deposits	177,092	195,307	215,894	239,431	253,234
Quasi money	84,294	83,337	87,360	87,741	92,799
	(Annual percentage change)				
Net foreign assets	85.7	8.4	15.3	14.0	2.5
Net domestic assets	-2.8	5.4	5.5	4.2	7.6
Domestic credit	0.4	4.0	5.8	3.3	5.4
Net credit to the government	-7.4	4.5	-0.4	-7.2	-6.0
Credit to the economy	4.0	3.8	8.3	7.2	9.1
Money and quasi money	14.2	6.3	8.6	7.5	5.8
	(In percent of broad money)				
Net foreign assets	16.5	2.6	4.9	4.7	0.9
Domestic credit	0.4	3.6	5.1	2.8	4.4
Net credit to the government	-2.4	1.2	-0.1	-1.7	-1.2
Credit to the economy	2.8	2.4	5.2	4.5	5.7
Other assets net	-2.7	0.1	-1.4	0.0	0.4
Memorandum items:					
Velocity (GDP/M3)	1.17	1.14	1.11	1.09	1.06
Velocity (nonagr. GDP/M3)	0.99	0.96	0.92	0.92	0.91
Credit to economy/GDP (in percent)	54.5	54.4	55.9	56.7	60.2
Credit to economy/nonagr. GDP (in percent)	64.5	64.9	67.1	67.4	70.1
NPLs/Gross loans (in percent) 2/	16.8	17.2	18.1	19.4	...
o/w commercial banks	10.7	11.2	12.3	12.4	
NPLs net of provisions/capital (in percent)	55.5	57.1	66.5	61.9	...
o/w commercial banks	19.9	18.7	23.3	20.5	...
Capital adequacy ratio (in percent)	12.6	12.2	9.3	10.2	...
o/w commercial banks	15.3	15.3	13.0	13.5	...
Liquid assets to total assets (in percent)	...	123.1	122.3	120.8	...
Domestic nonbank debt/GDP (in percent)	26.1	31.7	35.3	38.1	41.9
Credit to gov/dom debt (in percent)	48.8	46.8	42.4	36.6	30.4
Lending interest rate (in percent)	8.9	8.5	8.1	7.8	...
Deposit interest rate (in percent)	5.0	4.5	3.8	3.6	...
Money market rates (in percent)	4.4	3.0	3.2	2.4	...
DHs per US$, period end	11.51	10.38	8.75	8.22	...

Sources: Bank Al-Maghrib; and Fund staff estimates and projections.
1/ Includes *Fonds Hassan II.*
2/ This ratio was 19.6 at end-June 2004.

Table 10. Morocco: Selected Macroeconomic Indicators, 2001–10

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
					(Percentage change)						
Real GDP growth	1.0	6.3	3.2	5.5	4.2	1.0	5.9	4.5	5.0	5.1	5.3
Real nonagricultural GDP growth	3.6	3.6	2.8	3.5	4.7	4.0	4.3	4.7	5.3	5.5	5.6
Inflation (CPI)	1.9	0.6	2.8	1.2	1.5	2.0	2.0	2.0	2.0	2.0	2.0
Export growth in US$	-1.6	6.9	9.2	16.7	16.4	5.8	6.7	6.7	7.2	7.4	7.6
ICOR 1/	6.5	4.4	8.6	6.1	4.4	5.9	4.9	4.5	4.2	4.2	4.1
Employment growth	0.3	0.9	2.5	4.6	3.6	1.0	4.5	3.1	3.3	3.4	3.4
					(In percent of GDP)						
Gross investment	23.7	22.9	22.7	24.1	25.0	24.6	25.4	25.8	26.2	26.5	26.8
Government	3.0	2.9	2.8	2.6	2.7	2.6	2.6	2.9	3.0	3.2	3.3
Private 2/	20.7	20.0	19.9	21.4	22.4	22.0	22.8	22.9	23.2	23.4	23.5
of which: Stockbuilding		0.6	-0.2	0.1	0.5	-0.2	0.1	0.1	0.1	0.1	0.1
National saving	22.3	27.6	26.8	27.7	27.3	23.7	25.3	25.2	25.1	24.7	24.3
Government	0.7	0.9	1.9	1.3	1.4	1.2	3.1	3.8	4.8	5.5	6.2
Private 2/	21.6	26.7	24.9	26.5	25.8	22.5	22.2	21.5	20.3	19.2	18.0
External saving											
(=current account balance)	-1.4	4.8	4.1	3.6	2.2	-0.9	-0.2	-0.6	-1.2	-1.8	-2.6
Total External debt 3/	55.0	47.8	41.0	35.1	30.8	30.2	27.7	25.8	23.9	22.2	20.7
GDP (in billions of U.S. dollars)	33.3	33.9	36.1	43.8	50.0	53.0	57.0	60.8	65.1	69.9	75.1
Fiscal balance 4/	-6.4	-5.7	-4.7	-5.3	-4.9	-5.5	-3.9	-3.7	-3.0	-2.6	-2.1
Primary balance	-1.1	-0.8	-0.3	-1.2	-1.0	-1.8	0.2	0.3	1.0	1.3	1.7
Borrowing requirement	2.5	2.4	4.5	2.9	1.8	5.8	3.1	3.1	2.5	2.1	1.7
Government debt ratio 5/	81.5	74.7	71.4	68.5	65.8	69.9	67.8	66.8	64.8	62.5	59.9
Privatization receipts	0.0	6.1	0.2	2.9	2.3	2.6	0.6	0.4	0.4	0.3	0.3
Arrears	3.9	-2.9	-0.1	-0.5	0.4	-3.1	0.0	0.0	0.0	0.0	0.0

Sources: Ministry of Finance; Bank Al-Maghrib; and Fund staff estimates and projections.

1/ Ratio of nonagricultural fixed capital formation to change in nonagricultural GDP.
2/ Includes public enterprises.
3/ Including private debt.
4/ Overall balance, excluding privatization and GSM revenues but including expenditures by the *Hassan II Fund.*
5/ Gross domestic and external central government debt, net of central bank credit, end of calendar year.

Table 11. Morocco: Balance of Payments, 2004–10
(In millions of U.S. dollars; unless otherwise indicated)

	Est.	Projections					
	2004	2005	2006	2007	2008	2009	2010
Current account	1,109	-455	-92	-352	-761	-1,293	-1,932
Trade balance	-6,489	-8,505	-8,521	-9,306	-10,234	-11,300	-12,490
Exports, f.o.b.	9,739	10,191	10,870	11,536	12,319	13,180	14,131
Agriculture	1,532	1,633	1,753	1,851	1,954	2,064	2,204
Phosphates and derived products	1,625	1,819	1,912	1,992	2,118	2,267	2,428
Imports, f.o.b.	-16,228	-18,696	-19,391	-20,842	-22,553	-24,480	-26,621
Petroleum	1,639	2,157	2,301	2,399	2,520	2,666	2,857
Capital goods	3,881	4,189	4,445	4,888	5,381	5,934	6,531
Food products	1,534	2,461	2,024	2,097	2,205	2,322	2,446
Services	3,388	3,724	4,097	4,425	4,772	5,143	5,550
Tourism receipts	3,920	4,267	4,567	4,946	5,354	5,796	6,283
Income	-651	-740	-841	-806	-783	-764	-767
Transfers	4861	5066	5172	5335	5484	5629	5776
Private transfers (net)	4,729	4,957	5,064	5,226	5,375	5,520	5,667
Workers' remittances	4,218	4,459	4,551	4,695	4,828	4,958	5,090
Official grants (net)	132	109	109	109	109	109	109
Capital account	-8	-6	-6	-6	-6	-6	-6
Financial account	982	680	1,942	2,036	2,268	2,518	2,790
Direct investment 1/	822	1,316	1,219	1,221	1,357	1,509	1,679
Privatization	0	1,442	347	232	232	232	232
Portfolio investment 2/	529	9	8	8	8	8	9
Other	-370	-645	714	807	903	1,000	1,102
Private 3/	781	-220	873	931	998	1,070	1,151
Public medium-and long-term loans (net)	-1,151	-425	-159	-125	-95	-70	-48
Disbursements	925	1,338	1,621	1,634	1,646	1,659	1,672
Amortization	-2,076	-1,763	-1,780	-1,758	-1,741	-1,729	-1,720
Reserve asset accumulation (-increase)	-1835	-220	-1844	-1679	-1501	-1219	-853
Errors and omissions	-268	0	0	0	0	0	0
Memorandum items:							
Exports of goods' volume (percentage change)	5.7	2.1	5.8	5.5	5.7	5.8	5.9
Imports of goods' volume (percentage change)	5.7	9.2	3.6	7.2	7.6	7.8	7.8
Trade balance (in percent of GDP)	-13.0	-16.0	-14.9	-15.3	-15.7	-16.2	-16.6
Current account balance (in percent of GDP)	2.2	-0.9	-0.2	-0.6	-1.2	-1.9	-2.6
Excluding official grants (in percent of GDP)	2.0	-1.1	-0.4	-0.8	-1.3	-2.0	-2.7
Terms of trade (percentage change)	-10.8	-3.1	0.8	0.4	0.4	0.4	0.3
Excluding oil	-10.3	-0.5	0.8	-0.1	-0.1	0.0	0.0
Impact of US$1 increase in oil prices (US$, mlns)	43.4	45.5					
Gross official reserves 4/	16,346	16,021	17,878	19,568	21,082	22,317	23,188
(In months of imports of goods and nonfactor services)	10.0	8.6	9.3	9.5	9.4	9.2	8.8
Debt service as percentage of export of goods, nonfactor services and MRE 5/	12.8	10.6	10.9	10.4	9.7	9.1	8.5
External public and publicly guaranteed debt (US$, blns)	14.0	13.6	13.4	13.3	13.2	13.1	13.1
In percent of GDP	26.0	25.7	23.5	21.9	20.3	18.8	17.5
DHs per US$, period average	8.87	...	...	...	...	...	...
DHs per US$, period end	8.22	...	...	...	...	...	...
Oil price (US$/barrel)	37.8	47.4	47.5	46.3	45.0	44.0	43.5

Sources: Ministry of Finance; *Office des Changes;* and Fund staff estimates and projections.

1/ In 2005, a nonresident company (Vivendi) sold part of its shares in Maroc Télécom to a resident company.
2/ The increase in 2004 is due to a sale of government shares of Maroc Télécom in the Casablanca and Paris stock exchange.
3/ Includes the loans that Moroccan banks gave in 2003 and will give in 2005 to the company (Vivendi) that bought part of Maroc Télécom in 2003 and additional shares in 2005.
4/ Excluding the reserve position in the Fund.
5/ Public and publicly guaranteed debt.

Table 12. Morocco: External Debt Sustainability Framework, 2000–10

(In percent of GDP; unless otherwise indicated)

	Actual							Projections						
	2000	2001	2002	2003	2004			2005	2006	2007	2008	2009	2010	
								I. Baseline Projections						**Debt-stabilizing noninterest current account 6/**
External debt	53.9	46.9	43.5	38.4	33.2			**30.1**	**27.7**	**25.8**	**24.0**	**22.3**	**20.7**	**-4.2**
Change in external debt	-2.2	-7.0	-3.4	-5.1	-5.2			-3.1	-2.4	-1.9	-1.8	-1.7	-1.6	
Identified external debt-creating flows (4+8+9)	3.5	-13.7	-8.2	-16.6	-8.6			-3.5	-4.1	-3.2	-2.6	-1.9	-2.5	
Current account deficit, excluding interest payments	-1.5	-7.3	-6.2	-5.3	-3.5			-0.2	-0.9	-0.5	0.2	0.9	1.7	
Deficit in balance of goods and services	6.3	3.3	3.1	3.9	6.2			9.0	7.8	8.0	8.4	8.8	9.2	
Exports	31.4	32.9	33.8	32.5	33.1			33.0	32.8	32.8	32.9	32.9	32.9	
Imports	37.6	36.2	36.9	36.4	39.3			42.1	40.6	40.9	41.2	41.7	42.1	
Net nondebt creating capital inflows (negative)	-1.1	-8.0	-1.3	-5.3	-1.6			-2.5	-2.1	-2.0	-2.1	-2.2	-3.6	
Automatic debt dynamics 1/	6.1	1.7	-0.8	-6.0	-3.5			-0.8	-1.0	-0.7	-0.7	-0.7	-0.7	
Contribution from nominal interest rate	2.9	2.6	2.1	1.7	1.3			1.1	1.1	1.1	1.0	0.9	0.9	
Contribution from real GDP growth	-0.6	-3.3	-1.4	-2.0	-1.4			-0.3	-1.6	-1.2	-1.2	-1.1	-1.1	
Contribution from price and exchange rate changes 2/	3.8	2.4	-1.4	-5.7	-3.3			-1.6	-0.5	-0.6	-0.5	-0.5	-0.5	
Residual, incl. change in gross foreign assets (2-3)	-5.7	6.7	4.8	11.4	3.5			0.4	1.7	1.3	0.8	0.2	0.9	
External debt-to-exports ratio (in percent)	171.9	142.5	128.8	118.1	100.3			91.1	84.4	78.6	72.9	67.7	62.8	
Gross external financing need (in billions of US dollars) 3/	3.3	1.1	1.4	1.8	1.1			3.5	3.2	3.5	3.9	4.4	5.0	
In percent of GDP	9.8	3.2	3.9	4.2	2.2			6.6	5.6	5.7	5.9	6.3	6.7	
Key Macroeconomic Assumptions						10-Year Historical Average	10-Year Standard Deviation							Projected Average
Real GDP growth (in percent)	1.0	6.3	3.2	5.5	4.2	3.1	5.4	1.0	5.9	4.5	5.0	5.1	5.3	4.4
Exchange rate appreciation (US dollar value of local currency, change in percent)	-7.7	-6.0	2.6	15.1	8.0	0.6	7.7	3.2	-0.5	0.1	0.1	0.1	0.1	0.5
GDP deflator in US dollars (change in percent)	-6.3	-4.3	3.2	15.0	9.5	2.4	8.5	5.0	1.5	2.1	2.1	2.1	2.1	2.5
Nominal external interest rate (in percent)	4.9	4.9	4.7	4.6	3.8	5.1	0.8	3.4	3.8	4.0	4.2	4.2	4.3	4.0
Growth of exports (US dollar terms, in percent)	-1.6	6.9	9.2	16.7	16.4	8.2	7.0	5.8	6.7	6.7	7.2	7.4	7.6	6.9
Growth of imports (US dollar terms, in percent)	4.9	-2.1	8.4	19.8	23.3	8.1	9.8	13.4	3.7	7.4	8.1	8.4	8.6	8.3
Current account balance, excluding interest payments	1.5	7.3	6.2	5.3	3.5	3.7	2.1	0.2	0.9	0.5	-0.2	-0.9	-1.7	-0.2
Net nondebt creating capital inflows	1.1	8.0	1.3	5.3	1.6	2.6	2.4	2.5	2.1	2.0	2.1	2.2	3.6	2.4
								II. Stress Tests for External Debt Ratio						**Debt-stabilizing noninterest current account 6/**
A. Alternative Scenarios														
A1. Key variables are at their historical averages in 2005–10 4/								**30.1**	**25.5**	**20.4**	**14.9**	**8.9**	**3.7**	**-2.6**
A2. Country-specific shock in 2005, with reduction in GDP growth (relative to baseline) of one standard deviation 5/								**30.1**	**27.7**	**25.8**	**24.0**	**22.3**	**20.7**	**-4.2**
A3. Selected variables are consistent with market forecast in 2005–10								**30.1**	**27.7**	**25.8**	**24.0**	**22.3**	**20.7**	**-4.2**
B. Bound Tests														
B1. Nominal interest rate is at historical average plus two standard deviations in 2005 and 2006								**30.1**	**28.5**	**27.3**	**25.4**	**23.7**	**22.0**	**-4.2**
B2. Real GDP growth is at historical average minus two standard deviations in 2005 and 2006								**30.1**	**31.9**	**33.7**	**31.3**	**28.8**	**26.2**	**-5.4**
B3. Change in US dollar GDP deflator is at historical average minus two standard deviations in 2005 and 2006								**30.1**	**33.1**	**37.0**	**34.3**	**31.5**	**28.6**	**-5.9**
B4. Noninterest current account is at historical average minus two standard deviations in 2005 and 2006								**30.1**	**29.1**	**28.1**	**26.2**	**24.4**	**22.8**	**-4.2**
B5. Combination of B1-B4 using one standard deviation shocks								**30.1**	**32.6**	**35.0**	**32.5**	**30.2**	**28.0**	**-5.7**
B6. One time 30 percent nominal depreciation in 2005								**30.1**	**39.8**	**37.3**	**34.6**	**31.7**	**28.8**	**-5.9**

1/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\varepsilon > 0$) and rising inflation (based on GDP deflator).

3/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

4/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both noninterest current account and nondebt inflows in percent of GDP.

5/ The implied change in other key variables under this scenario is discussed in the text.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and nondebt inflows in percent of GDP) remain at their levels of the last projection year.

MOROCCO—FUND RELATIONS

As of April 30, 2005

I. Membership Status: Joined: April 25, 1958; Article VIII

II. General Resources Account:	**SDR Million**	**%Quota**
Quota	588.20	100.00
Fund holdings of currency	517.76	88.02
Reserve position in Fund	70.44	11.98
Holdings exchange rate		

III. SDR Department:	**SDR Million**	**%Allocation**
Net cumulative allocation	85.69	100.00
Holdings	67.75	79.07

IV. Outstanding Purchases and Loans: None

V. Latest Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-by	Jan 31, 1992	Mar 31, 1993	91.98	18.40
Stand-by	Jul 20, 1990	Mar 31, 1991	100.00	48.00
Stand-by	Aug 30, 1988	Dec 31, 1989	210.00	210.00

VI. Projected Payments to Fund
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2005	2006	2007	2008	2009
Principal					
Charges/Interest	0.31	0.45	0.45	0.45	0.45
Total	0.31	0.45	0.45	0.45	0.45

VII. Implementation of HIPC Initiative: Not Applicable

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 UN Security Council resolutions. The exchange rate is freely determined in the interbank foreign exchange market which was created in 1996. Bank Al-Maghrib (BAM) intervenes in the market to maintain the exchange rate within its target range, defined around a fixed central rate. Morocco has a conventional peg arrangement. The central exchange rate of the Moroccan dirham is pegged to a basket of currencies representing Morocco's principal trading partners. During 2001, the authorities changed the basket of currencies by increasing the weight of the Euro to better reflect the weight of external trade with EU countries. BAM 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. In January 2005, the SDR/dirham exchange rate was SDR 1 = DH 13.09.

Article IV consultation

Morocco is on the 12-month cycle. The last consultation discussions took place in Rabat during February 12–23, 2004, and were concluded by the Executive Board on May 5, 2004.

Technical assistance

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

November 7–22, 2000: FAD—advising on improving the design of the tax system and its administration

January 16-30, 2002: STA—ROSC Data Module Mission

February 9–20, 2004: MFD—Monetary Framework

May 17–24, 2004: FAD—Modernizing the tax system and its administration.

June 28–July 7, 2004: FAD—ROSC Fiscal Module.

2004: MFD—Peripatetic visits—internal credit rating system.

Resident representative: None

MOROCCO: FINANCIAL RELATIONS WITH THE WORLD BANK

(As of March 31, 2005)

The Bank FY05 portfolio in Morocco (measured in number of active Loans and TFs and in commitment value as of today) consist of 16 operations (10 IBRD loans and 6 Trust Funds) with total commitments of US$325 million approximately. Disbursements for investment projects amounted to US$26.3 million in FY04 compared to US$34.2 million (projected) in FY05. Key indicators of disbursement compared with Bank averages leave room for improvement. Indeed, the Disbursement Ratio for the Morocco portfolio fell from 15.5% in FY02 to 10.3% in FY04 and currently stands at 8.1 % in FY05, well below the Bank wide and the region average.

Despite the fact that the quality of the portfolio has improved over the last five years, institutional capacity for project implementation needs to be further strengthened. A participatory Country Portfolio Performance Review (CPPR) took place in June 2002 and a follow-up CPPR in February 2003. A new CPPR is scheduled for May 2005 to tackle this issue through ongoing participatory monitoring and capacity building activities. It will be followed by periodic reviews in order to address the issue of low disbursement and to reassess progress made on key actions agreed upon to improve project and portfolio management.

From FY99 to FY01, the Bank has provided extensive technical assistance through its various lending operations for projects, as well as through its sectoral adjustment loans (SAD). Three SAD were approved, amounting to US$416 million, to support the Government in establishing a sound macroeconomic framework and in implementing a broad reform program covering public sector reform, private sector development, poverty reduction and human resource development and telecommunications regulatory framework. This FY, the Bank has approved an innovative operation in the education sector amounting US$80 million, adopting a Sector Wide Approach (SWAp), to be implemented as a pooled-financed investment operation. This operation is the first SWAp project in the MENA region. This approach uses the Borrower’s fiduciary and technical systems and procedures.

In addition, investment and learning and innovative loans (LIL) were approved during FY99-03, amounting respectively to US$89 million, US$7.5 million, US$32.6 million, US$5 million and US$30.9 million. They include assistance to: legal and judicial development (US$5.3 million), Sustainable Coastal Tourism Development project (US$2.2 million), Irrigation Based Community Development (US$32.6 million), Support to Social Development Agency project (US$5 million), Adult Literacy (US$4.1 million) and Rainfed Agriculture Development (US$26.8 million) and are mostly designed with participatory and community driven approaches.

Also, to move the reform agenda forward in areas where agreement was reached with Government, we have developed intermediary products such as narrowly targeted, small budget support operations. To that extent, the Board approved last June an operation to improve Government's management of real assets held by social sector ministries (Asset Management Reform Loan, US$45 million).

As prospects for lending have been reduced, due to large privatization receipts (telecom license and privatization) and a deterioration of the fiscal stance, our program has increasingly turned toward knowledge transfer through participatory approaches. After a number of policy notes on sectoral issues such as education, administration and the financial sector, and related long-term prospects were prepared, the Bank has provided strong analytical and institutional support to budget and public administration reform to the Moroccan Government. Participatory approaches (Programmatic Economic and Sector Work-PESW) have been developed in the area of public sector and price policy reforms. Continued support through PESW is foreseen in the budgetary and public administration reform, agriculture reform, tertiary education and decentralization and municipal development areas.

Due to improved economic performance in 2002 and 2003, and plans to reduce the fiscal deficit to 3% by 2007, the country economic management appears to be on a fiscally sustainable path. As a result of this, Morocco is now in a position to engage in structural reform loans, as envisioned in the enhanced base case scenario of the CAS. Such Bank's support (adjustment lending) has been requested by the Moroccan authorities for reform formulation and implementation in the areas of public reform, financial, education, agriculture and housing sectors.

Two projects are scheduled to be negotiated shortly and be presented to the Board of Directors before the end of this FY: a Financial Sector Development Policy Loan (tentatively US$200 million) and a Housing Sector Development Policy Loan (tentatively US$100 million).

Morocco: Financial Relations with the World Bank

(As of March 31, 2005)

	Total Net Commitments	Undisbursed Balance
	(In millions of U.S. dollars)	
IBRD lending operations		
128 loans closed [1/]	7,268	
10 active loans		
- Sewerage & Water Reuse II	28.0	7.5
- Fès Medina Rehabilitation	9.6	5.1
- Health Management	45.7	44.0
- Irrigation Based Community Devt.	32.6	31.1
- Social Devt. Agency	5.0	6.2
- Adult Literacy	4.1	4.6
- Asset Management	45.0	26.6
- Rainfed Agriculture Devt.	26.8	31.2
- Rural Roads	36.9	37.6
- Basic Education Reform Support	80.0	78.3
Total active loans	313.7	272.2
Repayments [2/]	5,714.5	
Debt outstanding [2/]	2,442.9	

	1999	2000	2001	2002	2003	2004	2005 [2/]
Net lending by the World Bank (by fiscal year) [3/]							
Commitments	440	7.5	97.6	5	75.9	36.9	180
Disbursements	411.4	106.8	115.8	52.7	58.7	112.3	119.1
Debt service	514.6	533.9	425.5	427.5	420.5	443.8	444.6
Principal	298.6	333.3	246.3	270.2	283.9	328.4	381.3
Interest [4/]	216	200.6	179.2	157.3	136.6	115.4	63.3
Net transfer [5/]	-103.2	-426.5	-309.7	-374.8	-361.8	-331.5	-321.8

1/ Less cancellations, includes adjustment lending, does not include guarantees.
2/ As of February 28, 2005.
3/ Fiscal years start July 1 and end June 30.
4/ Includes charges.
5/ Equal to disbursement minus debt service.

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. Data provision is adequate for surveillance purposes.

A data ROSC mission, which took place in January 2002, carried out a review of Morocco's data dissemination practices according to the GDDS, as well as an in-depth assessment of the compilation of national accounts, CPI, PPI, government finance, monetary, and balance of payments statistics. As the authorities maintain a strong interest in subscribing to the SDDS, the mission also identified areas to be strengthened to meet the SDDS requirements. A subsequent mission (April-May 2005) noted that the authorities have made important progress toward meeting SDDS requirements. Morocco meets most of the SDDS requirements in terms of coverage, periodicity, and timeliness. The mission proposed an action plan to address the remaining issues. If implemented, it would enable Morocco to subscribe to the SDDS by October 2005.

Real sector

The Statistical Office is working on rebasing national accounts from 1980 to 1998 and on bringing it in conformity with the *System of National Accounts 1993*. This reform program has made good progress and the first series of accounts for 1998 -2000 has been finalized. The new series of accounts covering the period 1998 – 2004 will be released during 2005 once the work on the years 2001 – 2004 is completed. The revision of the consumer price index is also planned to be completed during 2005, with the update of weights based on the results of the 2001 household budget survey. A consistent monthly time series for the producer price index based on the 1995 industrial register's weights has been released since 1997. With respect to SDDS subscription, the authorities need to produce an index of wages/earnings, and improve the timeliness of gross domestic product statistics. They intend to avail themselves of a flexibility option for the industrial production index.

Government finance

Central government finance data are generally available to MED with a few months lag. *GFS* data reported by Morocco for publication in the *GFS Yearbook* are not timely (no data have been submitted for the past three years), and their coverage is limited to the budgetary central government, the Moroccan pension fund, and the National Social Security Fund. No data for the central government on a monthly or quarterly basis are reported to STA for publication in *IFS.* A technical assistance STA mission in February 1999 and a follow-up mission in February 2000 advised on further improvements in the compilation of both central and local government statistics and assisted the government in establishing appropriate consolidation procedures for a presentation of general government data. Substantial progress has been made by the Accounting Office for the compilation of local government data and their consolidation with central government budgetary data. The actual use of those new rich source data for general government compilation may require further clarification of responsibilities between various directorates. Regarding the monthly *Treasury's expenditure and revenue table*, the ROSC data module recommended some reclassifications (transfers, privatization), to maintain the *Fonds Hassan II* within the coverage of the table, and, for dissemination purposes, to complement the table with more details and data on financing and improve the format of dissemination. The ROSC mission generally recommended various actions to improve dissemination formats and practices towards meeting the SDDS GFS standards. The recent SDDS mission prepared an action plan for the production of data on the consolidated general government operations, envisaging completion by October 2005.

Monetary and financial statistics

Bank Al-Maghrib disseminates monetary and financial and other macroeconomic statistics to the general public primarily through its website (bkam.ma). The statistical part of the site includes web-based versions of the Bank's weekly, monthly, quarterly, and annual publications. The timeliness of reporting of the accounts of the central bank and those of the banks (35–37 days lag) has improved recently, but remains lower than that prescribed under the SDDS (two-week lag). The degree of detail in the breakdown of financial assets and liabilities by resident institutional sector could be more extensive; at present, this problem is reflected in the lack of precision in some of the monetary aggregates, including credit indicators.

Balance of payments

The ROSC mission found that in general Morocco's balance of payments statistics are in line with the concepts and definitions set out in the fifth edition of the *Balance of Payments Manual (BPM5)*. However, further work is needed to implement certain recommendations on scope, classification, and basis for recording. Thus, recent measures to exclude the effects of changes in exchange rates from the valuation of transactions in reserve assets should be continued, and transactions in foreign currency assets and liabilities of intermediary banks at their correspondent banks should be excluded from transactions in reserve assets. Also, the *Office des Changes* (OC) is planning to treat operators in free trade zones as residents. Offshore banks located in Morocco should also be considered residents. The OC lacks a firm legal basis for compiling and disseminating balance of payments statistics, relying for the time being exclusively on customs and exchange control data. These data are gradually to become less available and too limited as liberalization proceeds and as participation of foreign investors in the Moroccan economy increases. The OC has initiated legislative measures that would give it access to statistical data collected directly from economic operators as needed among other things to record private foreign debt, and more generally of the international investment position. Furthermore, the ROSC mission recommended the introduction of quarterly surveys of enterprises and other agencies to improve the scope, classification, and valuation of balance of payments transactions, in particular for goods for processing, transportation services, and financial transactions. Since May 1998, the OC has been publishing, in its new internet site, monthly statistics on trade, tourism, private transfers, and incoming foreign direct investment in accordance with the *BPM5*. The quality of balance of payments statistics will significantly improve with the planned inclusion of free trade zones and offshore banks located in Morocco in its economic territory.

The authorities are compiling the Data Template for International Reserves and Foreign Currency Liquidity (Reserves Template) in broad conformity with SDDS requirements. The SDDS mission suggested minor adjustment to the data available and the regular dissemination of the Reserves Template. The authorities also need to compile quarterly external debt data in order to subscribe to the SDDS; source data are available and this information should be regularly disseminated by the Ministry of Finance and Privatization starting October 2005. The international investment position data are disseminated annually with a timeliness within SDDS requirements.

Morocco meets or exceeds the GDDS recommendations in the external sector, except for the twice a year publication of the external debt service schedule and the quarterly publication of public and publicly-guaranteed external debt statistics. The quarterly publication of balance of payments statistics is in line with the SDDS recommendations, but the timelines exceeds the SDDS requirements with three months. To further comply with the SDDS requirements, the data template on international reserves and foreign currency liquidity should be used and disseminated.

The latest BOP and IIP information received from Morocco, and published in the IFS, relates to quarterly BOP data for 2003 and annual IIP data for 2002 and 2003 (which was reported for the first time in 2004). Furthermore, Morocco reports on a regular basis international liquidity data to STA for publication in the *IFS*.

Morocco: Table of Common Indicators Required for Surveillance

As of June 8, 2005

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]
Exchange Rates	05/31/05	05/31/05	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	04/30/05	05/31/05	W	W	W
Reserve/Base Money	04/30/05	05/31/05	M	M	M
Broad Money	04/30/05	05/31/05	M	M	M
Central Bank Balance Sheet	04/30/05	05/31/05	M	M	M
Consolidated Balance Sheet of the Banking System	04/30/05	05/31/05	M	M	M
Interest Rates[2]	05/31/05	05/31/05	D	D	D
Consumer Price Index	03/31/05	05/31/05	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	03/31/05	05/31/05	...	...	...
Revenue, Expenditure, Balance and Composition of Financing[3] – Central Government	03/31/05	05/31/05	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	03/31/05	05/31/05	A	A	A
External Current Account Balance	03/31/05	05/31/05	M	M	M
Exports and Imports of Goods and Services	03/31/05	05/31/05	M	M	M
GDP/GNP	12/31/04	05/31/05	Q	Q	Q
Gross External Debt	03/31/05	05/31/05	Q	Q	Q

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA).

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IMF Concludes 2005 Article IV Consultation with Morocco

On August 29, 2005, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Morocco.[1]

Background

Morocco has achieved macroeconomic stability since the early 1990s. Inflation has remained low anchored by the exchange rate peg and thanks to a prudent monetary policy. The external current account has been in surplus since 2001 and external reserves increased to a comfortable level. However, fiscal deficits have remained large and the authorities have used part of the privatization receipts to finance increased expenditures.

Growth has been volatile and insufficient to significantly reduce poverty and unemployment. Growth averaged three percent over the last decade. It has been volatile because of the dependency of agriculture to rainfalls, and recurrent droughts contribute to increasing poverty in rural areas. The unemployment rate remains high, particularly in urban areas. Although the growth of the nonagricultural sector has become more resilient to agricultural output shocks, it is insufficient to significantly reduce unemployment.

[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 August 29, 2005 Executive Board discussion based on the staff report.

Morocco continues to implement its broad based structural reform agenda. Large state-owned enterprises have been privatized and remaining public enterprises are being restructured or prepared for privatization. In the area of trade liberalization, the implementation of the association agreement with the European Union, Morocco's main trading partner, is proceeding as scheduled. Trade agreements were signed with the United States, Turkey, Tunisia, Jordan and Egypt to complement the association agreement with the European Union. Most Favored Nation tariffs were reduced to a maximum of 10 percent for goods freely traded with the European Union. The financial sector is being strengthened. The imminent promulgation of a new central bank and banking laws will further enhance the autonomy of the central bank and its supervisory power. A new labor code has been approved and is expected to improve labor relations and flexibility in the labor market. The government is pursuing its efforts to fight poverty, improve social conditions, and enhance the rights of the female population. The impact of these reforms on Morocco's growth rates should be observed in the medium term.

In 2004, macroeconomic and financial conditions remained stable. While the overall GDP growth slowed down to 4.2 percent on account of a decline in growth in the primary sector, nonagricultural GDP growth picked up because of a dynamic tertiary sector and a recovery in mining and energy. Inflation remained below 2 percent. The current account was in surplus, and external reserves increased further and covered about ten months imports of goods and services as well as the public and publicly guaranteed external debt.

The fiscal deficit (including Hassan II Fund and excluding privatization receipts) declined by 0.4 percentage points to 4.9 percent of GDP, reflecting good revenue performance. However, some budgetary policies did not support fiscal consolidation. Expenditures were higher than envisaged because of increases in: (i) investment following acceleration in project execution; (ii) the wage bill following new salary increases; and (iii) subsidies because the food subsidy reform was postponed and the petroleum price adjustment was not fully implemented. The authorities were able to prevent further expenditure increases related to the El-Hoceima earthquake and a locust invasion by reallocating budgetary appropriations. Public debt declined to 66 percent of GDP because privatization receipts helped finance the deficit.

The unfavorable agricultural campaign is expected to affect macroeconomic conditions in 2005. The overall GDP growth rate is projected at about 1 percent. The current account is likely to register a small deficit partly because of a high level of imports of food products and higher oil bill. Nonetheless, the overall balance of payments is expected to remain in surplus. The fiscal deficit (excluding privatization revenue but including spending by Hassan II Fund) is expected to increase to about 5.5 percent of GDP (but to decline to 4.5 percent of GDP, excluding one-off factors) despite continued favorable revenue performance. Expenditures will increase reflecting the repercussions on wage payments of the 2004 wage negotiations, the voluntary retirement program, the new universal health insurance program, the delay of the food subsidy reform, and the partial adjustment in May and August of domestic petroleum prices. Large privatization receipts will help contain the debt to GDP ratio at about 70 percent, despite the issuance of debt to cover old pension fund arrears (2.4 percent of GDP).

Executive Board Assessment

Executive Directors commended the Moroccan authorities for maintaining macroeconomic stability and for continuing to implement their structural reform agenda in 2004. Inflation remained low, nonagricultural output growth accelerated, and foreign exchange reserves increased further. Good revenue performance contributed to the narrowing of the fiscal deficit and the debt-to-GDP ratio declined. Considerable progress has been made in the implementation of structural reforms, most importantly, those related to trade liberalization, the financial sector, public enterprises, and the labor market.

Despite these achievements, Directors noted that growth continues to be volatile and insufficient to significantly reduce unemployment and poverty. To these ends, they agreed that Morocco needs to achieve sustained high rates of growth in non agricultural output. In the context of Morocco's increasing integration into the world economy, they considered accelerated structural reforms and fiscal consolidation essential elements of a high growth strategy. They, therefore, welcomed the authorities' resolve to move expeditiously with their remaining structural reform agenda in a context of continued macroeconomic stability and fiscal consolidation.

Although the current fiscal stance and debt level do not pose a risk to macroeconomic stability in the short term, Directors considered that current policies, if maintained, could reduce the authorities' ability to absorb unfavorable shocks, which could constrain growth. They, therefore, welcomed the authorities' targeted reduction of the fiscal deficit to 3 percent of GDP over the medium term. They agreed that the achievement of this objective and its compatibility with a high-growth strategy would require a reform of the tax system that would widen the tax base and allow a reduction in tax rates, a decline in the wage-bill-to-GDP ratio, an overhaul of the food subsidy program, and the implementation of the petroleum price adjustment mechanism.

Directors welcomed the authorities' plan to implement a medium term budget framework to enhance the efficiency of fiscal policies. They supported the authorities' efforts to initiate a tax reform, particularly of the VAT, and to present a tax expenditure report with the 2006 budget to raise awareness about the need to improve the efficiency of the tax system. They encouraged the authorities to move expeditiously on a broad-based tax policy and tax administration reform. Directors welcomed the authorities' decision to continue their no net new hiring policy, implement a modern human resource management and remuneration system and a voluntary retirement/departure program, and pointed to the importance of controlling salary adjustments and bonuses. Directors welcomed the increased emphasis on social development, including through improved access to education, healthcare, housing and basic infrastructure and rural development, to be financed within the medium-term budget objectives. They also greeted the recent recognition of old pension fund arrears, and supported the authorities' efforts at adopting and implementing a comprehensive plan to put the pension system on a sound footing.

Directors agreed that the Moroccan authorities have made commendable progress in liberalizing the economy. The recently signed free trade agreements with the United States, Turkey and regional partners will help attract foreign direct investment and boost Morocco's growth and export performances. However, to fully exploit the benefits of trade integration, Directors urged the authorities to simplify the tariff structure, further reduce tariffs, and eliminate variable tariff rates in parallel with the reform of the food subsidy system while providing targeted support to vulnerable groups. They noted that liberalization measures in the area of telecommunications contributed to the current dynamism of the sector and those related to air transportation have positively impacted tourism. They encouraged the authorities in their efforts to liberalize other sectors of the economy.

Directors urged the authorities to fully implement the new labor code, which should help clarify employer/employee relationships, and to accelerate judicial reforms, which should enhance investors' confidence. Directors encouraged the authorities to accelerate the implementation of the remaining measures needed to improve the business environment. In particular, they noted the need to improve governance and transparency. Directors called for caution in the provision of exemptions or special incentives in favor of specific sectors as a measure to foster investment.

Directors welcomed the authorities' continued efforts to strengthen the financial sector and implement the recommendations of the Financial Sector Assessment Program. The promulgation of the new central bank and banking laws will further enhance the autonomy and supervisory power of the central bank. Directors noted the progress made in the restructuring of the three weak state-owned banks. They urged the authorities to accelerate the implementation of the measures required to bring these banks to compliance with prudential regulations as soon as possible. Directors encouraged the authorities to continue addressing the remaining vulnerabilities in the financial system, including the high level of non performing loans, and to remove the structural constraints in order to enhance the availability and reduce the cost of credit to small-and-medium-size enterprises, which represent the core of Morocco's enterprise sector. They commended the adoption of a bill to combat the financing of terrorism, and looked forward to action on anti-money laundering legislation.

Directors noted that the current peg of the dirham has served the economy well and contributed to keeping inflation low, and that there are no signs of an exchange rate misalignment. Given the increasing integration of the Moroccan economy into the rest of the world, they noted that a gradual transition to a flexible exchange rate regime would be advisable. They welcomed the authorities' openness to consider the desirability of alternative exchange rate regimes taking into account the characteristics of the Moroccan economy.

Directors commended the authorities' efforts to improve the statistical database. In particular, they noted the progress made toward meeting the Special Data Dissemination Standards, and encouraged the authorities to implement the agreed action plan to enable Morocco to subscribe to the SDDS in the coming months.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Table 1. Morocco: Selected Economic and Financial Indicators, 2000–05

Quota: SDR 588.20 million
Population: 29.8 million
Per capita income: US$ 1,677 (2004)

	2000	2001	2002	2003	2004 Prel	2005 Proj.
	(Annual percentage change; unless otherwise indicated)					
Production and income						
Nominal GDP	2.5	8.2	3.8	5.5	5.8	2.8
Real GDP	1.0	6.3	3.2	5.5	4.2	1.0
Real nonagricultural GDP	3.6	3.6	2.8	3.5	4.7	4.0
GDP deflator	1.5	1.8	0.6	-0.1	1.5	1.8
Consumer price index (CPI), average	1.9	0.6	2.8	1.2	1.5	2.0
	(In billions of U.S. dollars; unless otherwise indicated)					
External sector						
Exports of goods, f.o.b.	7.4	7.1	7.8	8.8	9.7	10.2
Exports of goods, f.o.b. (percent change)	-1.2	-3.7	9.8	11.8	11.2	4.6
Imports of goods, f.o.b.	10.7	10.2	10.9	13.1	16.2	18.7
Imports of goods, f.o.b. (percent change)	7.0	-4.6	7.2	20.1	23.9	15.2
Oil imports f.o.b.	1.4	1.3	1.2	1.0	1.6	2.2
Net services and income	0.3	1.1	1.2	1.8	2.7	3.0
Net transfers	2.5	3.6	3.3	4.1	4.9	5.1
Current account (in percent of GDP)	-1.4	4.8	4.1	3.6	2.2	-0.9
Overall balance (deficit -)	-0.4	3.8	0.6	1.6	1.8	0.2
	(In percent of GDP)					
Central government						
Revenue, excluding grants and privatization	26.2	25.0	24.7	24.5	25.1	26.4
Total expenditure (including *Fonds Hassan II*)	32.4	31.1	29.9	30.3	30.9	32.4
Overall balance 1/	-6.4	-5.7	-4.7	-5.3	-4.9	-5.5
Privatization and GSM receipts	0.0	6.1	0.2	2.9	2.3	2.6
Overall balance, incl. privatization 1/	-6.4	0.4	-4.5	-2.5	-2.6	-2.9
	(Annual percent change; unless otherwise indicated)					
Money and credit						
Broad money	8.4	14.2	6.3	8.6	7.5	5.8
Interest rate (Avg, money market rate, in percent)	5.4	4.4	3.0	3.2	2.4	...
Official reserves						
Gross official reserves (in billions of US$, end-period)	4.8	8.4	10.1	13.9	16.3	16.0
In months of imports of goods and services	4.6	8.2	9.1	10.4	10.0	8.6

Debt (short-, medium-, and long-term)						
Total external debt (in billions of US$)	18.0	15.9	15.7	16.8	16.6	16.0
Total external debt (in percent of GDP)	55.0	47.8	40.9	35.1	30.8	30.2
Domestic government debt (in percent of GDP) 2/	47.3	45.8	48.1	50.1	49.9	55.2
Total government debt (in percent of GDP) 2/	81.5	74.7	71.4	68.5	65.8	69.9
Memorandum items:						
GDP at current prices (in billions of DH)	354.2	383.2	397.8	419.5	443.7	456.0
GDP at current prices (in billions of US$)	33.3	33.9	36.1	43.8	50.0	...
Exchange rate: dirham/US$ (average period)	10.63	11.30	11.02	9.57	8.87	...
Real effective exchange rate (appreciation +)	2.8	-4.1	-0.3	-1.3	-0.6	...
Terms of trade (deterioration -)	-7.7	7.6	-7.3	5.7	-10.8	-3.1
Excluding oil	-2.4	7.9	-8.6	8.5	-10.3	-0.5
Unemployment rate (in percent)	13.7	12.8	12.5	11.4	10.8	...
Urban	21.5	20.3	18.0	19.3	18.4	...
Rural	5.2	4.2	6.2	3.4	3.1	...

Sources: Data provided by the Moroccan authorities; and Fund staff projections.
1/ Commitment basis including *Fonds Hassan II.*
2/ Gross debt including net central bank credit.

Statement by Mohammed Daïri, Alternate Executive Director for Morocco
August 29, 2005

Morocco continues to enjoy macroeconomic stability and to take strides toward achieving high growth, strengthening the economy's resilience to shocks, and improving social conditions. In 2004, GDP growth reached 4.2 percent despite the effects of the locust invasion and Al Huceïma earthquake, reflecting stronger performance of the non-agricultural sector. Inflation remained subdued and the external position robust, notwithstanding the increase in oil prices and the slow growth in the EU, Morocco's main trading partner. Unemployment declined by 2 percentage points in the past two years, but remains high. The fiscal position improved as a result of stronger revenue performance. Progress was made in key structural reforms, aimed at raising growth potential by enhancing efficiency and improving the business environment. The economy's resilience to weather vagaries has increased significantly over the past few years as a result of improved performance in the non-agricultural sector. As indicated in Figure 3 of the staff report, there has been a significant increase in non-agricultural GDP's resilience to agricultural GDP fluctuations. However, the exceptional drought of 2004/05 led to a fall in cereal production of close to two-thirds, bringing projected GDP growth to 1-1½ percent in 2005, despite an increase in non-agricultural GDP of 4 percent. The authorities intend to build on their good track record, in order to achieve higher and more sustainable growth and further reduce unemployment, and are committed to continued prudent policies supported by acceleration of structural reforms.

Fiscal policies

While progress has been made in fiscal consolidation, leading to a decline in the debt-to-GDP ratio, the authorities believe that further consolidation, through structural revenue and expenditure measures, will be necessary to put fiscal sustainability on a firmer trajectory and to bring about an environment more conducive to private sector development. They also attach high importance to greater fiscal transparency and adequate treatment of contingent liabilities, including in the pension system, in order to reduce fiscal vulnerabilities.

The authorities do not believe that, under present circumstances, the current fiscal stance is unsustainable. Indeed, there are no pressures on inflation, the external current account, or interest rates, and the fiscal deficit is being financed at market rates, while the debt to GDP ratio continues to decline. Staff indicate in paragraph 4 that the debt-to-GDP ratio declined mainly because privatization helped finance fiscal deficits and as a result of debt/equity swaps. In 2000-04, the debt to GDP ratio declined by 15.7 percentage points, whereas privatization revenue amounted to a cumulative 11.6 percent of GDP, and debt/equity swaps and early repayment of expensive debt amounted to some 4 percent of GDP each, which indicates that privatization revenue was used for debt reduction and not for financing the deficit. Moreover, the authorities have reservation regarding staff measure of the fiscal deficit, which excludes privatization revenues, in view of their exceptional nature, whereas exceptional expenditure carried out by the Fonds Hassan II and financed by privatization revenue are included. These expenditures are not of a recurring nature, nor do they generate recurring expenditures for the government; they contribute as seed money to the financing of investment carried out by non-government agencies in the areas of road construction, social housing, other key economic and social infrastructure, and in restructuring of priority sectors facing temporary shocks.

The fiscal position in 2004 turned out better than budgeted and much stronger than anticipated during the last consultations. The overall deficit, according to staff definition, declined by 0.4 percent of GDP, reflecting stronger tax revenue collection. Moreover, unexpected spending following the locust invasion and the earthquake, as well as part of the subsidy cost of domestic petroleum prices, which were not increased in the aftermath of the significant increase in world prices, were accommodated through redeployment of spending.

While the fiscal deficit is expected to increase in 2005, a number of exceptional factors should be highlighted. First, the decline in cereals production reduces GDP growth significantly, while generating new spending in view of the need to offset, partly through expenditure redeployment, some of the losses incurred by the agricultural sector. Second, some wage increases, expected to be implemented in 2004 were carried over to 2005 since relevant regulatory requirements were not met, whereas their effect will start from 2004. Third, expenditures by Fonds Hassan II, which are of exceptional nature, are projected by staff to increase by 0.5 percent of GDP in 2005, whereas the authorities believe that their increase in 2005 would be smaller than projected by staff, as was the case in recent years. Finally, the projection includes exceptional expenditure to the tune of 0.7 percent of GDP related to the voluntary early retirement scheme (see below).

Consistent with the planned reform of the civil service and the objective of reducing its size, the authorities are implementing an ambitious program of voluntary early retirement, which would reduce the size of the civil service by about 5-6 percent. While the one-off cost of the program for 2005 may be high and could reach some 1.5 percent of GDP, the net savings, taking full account of the effect on the public pension fund, would lead to a decline in the wage bill of 1 percent of GDP per year over the medium term.

The authorities remain committed to further reducing food subsidies; however, an appropriate timing and the establishment of a well-targeted social safety net are key to successful progress in this area. Petroleum prices were raised twice in 2005, except for butane, which is mainly used by low-income households. This, however, did not allow for full recovery of the large increase in international prices. It should be noted that Morocco's domestic petroleum products prices remain well above international prices as a result of the high excises amounting to about 2 percent of GDP. Nevertheless, the authorities will seize future opportunities to raise prices in light of market developments and intend to return as soon as possible to automatic implementation of the price indexation formula. They have also indicated their intention to use a more realistic price assumption in preparing the 2006 Budget and to include appropriations to clear remaining arrears on petroleum subsidies.

The authorities aim at increasing revenue through broadening of the tax base, enhancing efficiency, and simplifying administration. Tax reforms implemented recently include the establishment of Large Taxpayer Units, consolidation of VAT audit and collection, and substitution of VAT to some distortionary excises, consistent with FAD recommendations.

The authorities intend to deepen tax reform by overhauling and simplifying the VAT, reviewing the income tax, and reducing exemptions. An FAD mission is expected in Morocco early October to discuss options for tax reform and TA needs.

A major reform of the pension system is being carried out in close cooperation with the World Bank, with the objective of ensuring its sustainability, reducing contingent liabilities, and strengthening savings mobilization. The internal pension funds of some public enterprises have been put on a sound footing, and other public enterprises will follow, whereas contribution rates have been increased for major pension funds. In conformity with the authorities' rehabilitation program for the major civil service pension fund, arrears accumulated over the past decade have been recognized and settled through debt issuance equivalent to some 2.2 percent of GDP.

The authorities thank the staff team that has conducted the fiscal transparency ROSC which was indeed a useful exercise in reviewing Morocco's practices in this area. They broadly concur with staff assessment that Morocco's fiscal management system is reliable and supported by legal safeguards and adequate for steering budget performance. They take note of the report's recommendations to improve the system and will take them into consideration in future budget reform. They agreed to publication of the report.

Monetary policy and financial sector reform

Monetary policy under the pegged exchange rate regime has been successful in bringing inflation to industrial country level and achieving a high degree of credibility. While the task of monetary management has been complicated by the large foreign inflows from workers' remittances, tourism receipts, and privatization, Bank Al Maghrib (BAM) has been able to limit the effect of excess liquidity on the economy. The monetary framework and BAM's organization are being modernized, with assistance from MFD, in order to further improve monetary management under the new central bank charter, which increases its independence and sets price stability as the main objective of monetary policy.

BAM's directive referred to in paragraph 30 of the staff report does not introduce a minimum lending rate. It has been issued at the request of the banking association (GPBM) to address practices in lending rates that reflect unhealthy competition. The directive requests banks to provide information on loans granted at interest rates below Treasury paper, in order to allow the central bank to identify instances where the rate is below costs.

Financial sector regulation and supervision are being strengthened, drawing on FSAP recommendations, and the new banking law, under discussion in Parliament, will increase BAM's regulatory powers. Following an increase linked to tighter classification rules, commercial banks NPLs have stabilized, and their financial soundness indicators have improved. The authorities have also made significant progress in restructuring of the public specialized banks (OFSs). While these banks do not pose risks to the financial stability in view of their limited links to the rest of the banking sector, it was the authorities' view that their restructuring should be completed as soon as possible in order to avoid moral hazard and to demonstrate the authorities' resolve in dealing with troubled banks. It is the authorities' firm intention to ensure that all OFSs are in full compliance with prudential regulations by mid-2007, including through equity injections where necessary, and no extension of this deadline can be granted according to the new banking law. The authorities are concerned about low access of credit by SMEs and the insufficient transmission of reductions in policy rates to conditions applied to these enterprises. They have taken a number of measures to improve transparency and risk assessment of SMEs and are examining how to identify and alleviate remaining impediments to their financing in consultation with GPBM.

Exchange rate policy and external developments and policies

The authorities appreciate the staff's Selected Issues paper prepared at their request on the exchange rate regime. The paper confirms the authorities' long lasting view that the present exchange rate regime has served Morocco well and concludes that there is no sign of misalignment of the dirham. It also suggests that a gradual move to a more flexible exchange rate regime is advisable if the authorities decided to open the capital account to residents. The authorities remain open to considering a more flexible exchange rate regime and will take staff analysis into consideration in their internal deliberations.

The strength of the external position has enabled a large build-up of reserves and, together with active debt management, has led to a significant improvement in external debt indicators. External debt to GDP ratio declined from 42 percent in 2001 to 26 percent in 2004, and the debt service ratio from 16 percent to below 13 percent. Progress in macroeconomic stabilization and structural reforms, as well as a stronger external position, have led Standard & Poor's to upgrade the sovereign debt rating twice in 2005, from BB stable to BB positive and further to BB+, bringing it just one notch below investment grade. Reflecting investors' appetite for Morocco's paper, secondary market spreads have declined significantly.

Tourism has recently strengthened its performance as a major source of growth, foreign exchange, and employment. Indeed, since 2001, tourism receipts, together with workers remittances, accounted for most of the strengthening of the current account. Significant progress has been achieved under the authorities' plan, developed in partnership with professionals, to reach 10 million tourists in 2010, and investment is increasing significantly following elimination of land bottlenecks and liberalization of air transport.

The dismantling of the MFA quotas has had a significant toll on Morocco's exports. Although the net effect on the balance of payments has been limited, since most of the inputs are imported, the employment effect has been larger, especially on the unskilled workers. The authorities are developing a strategy to deal with the situation, taking advantage of proximity to Europe, and of FTAs with the EU, US, and Turkey, and concentrating on the upper end of the garment market. Improving managerial and technical skills is a key element of this strategy. They have also succeeded in attracting upstream investment by major textile groups. Trade liberalization continues to be pursued both at the multilateral and the regional level, including with Arab countries, and is expected to boost growth and exports.

Growth strategy and structural reforms

The authorities are fully aware of the need to accelerate growth performance which, despite recent gains, remains insufficient to significantly reduce unemployment. In addition to current strategies regarding tourism and textiles, they have commissioned a comprehensive study, conducted by McKinsey, in order to assess the present situation of the Moroccan industry and to identify the major sources of growth. Among the key sectors with high potential for growth in view of Morocco's comparative advantages are: fisheries, agro-industry, construction, car equipment, electronics and electrical equipment, and off-shoring. The conclusions of the study are under evaluation and would be used to develop a coherent strategy. The successful liberalization of the Telecom and transport sectors and on-going efforts aimed at strengthening transparency and governance, reforming the judiciary, and alleviating investment bottlenecks will go a long way in improving the business climate and increasing growth potential.

The authorities wish to thank staff for the Selected Issues paper on growth performance. They agree that there is a significant potential for improvement in productivity, for which acceleration of structural reforms will be key as evidenced by recent trends in total factor productivity in the non-agricultural sector. The attention given in the paper to trade opportunities from recently concluded FTAs and to the need to monitor labor market conditions is also well placed.

Social policies

The authorities' efforts at addressing poverty and improving social conditions have been significantly strengthened following the announcement by King Mohammed VI of the National Initiative for Human Development (INDH). This initiative aims at reducing social and geographic disparities, developing sources of income and employment, and assisting vulnerable population through a transparent and participatory process. The initiative will 'be financed from the central government, within the medium-term budget envelope, and local governments, with contributions from donors. The total cost of the initiative for the period 2006-2010 is estimated at 10 billion dirhams, equivalent to 2 percent of GDP. The INDH will complement on-going social programs aimed at improving social service delivery, especially in the rural areas, reducing the large deficit in social housing, and improving social conditions. Moreover, the new health care system will expand protection to the work force outside government, financed by employer/employee contributions, and to the needy segments of the population, to be financed by the budget.

A recent STA mission found that Morocco would be able to subscribe to SDDS by October this year. The authorities have announced their intention in this regard to the public. They are committed to addressing the few remaining issues in order to meet this timeframe.

The authorities wish to express their appreciation to the staff for their hard work and dedication, and to management and the Board for their continued support. They remain firmly committed to staying the course of prudent macroeconomic policies and to create a propitious environment for private sector-led growth to achieve their objectives of improved incomes and living conditions and higher employment. They look forward to the Board's assessment and advice.