

**Morocco: Request for an Arrangement Under the Precautionary and Liquidity Line—
Staff Report; Press Release on the Executive Board Discussion; and Statement by the
Executive Director for Morocco.**

In the context of the request for an arrangement under the Precautionary and Liquidity Line, the following documents have been released and are included in this package:

- The staff report on the request for an arrangement under the Precautionary and Liquidity Line, prepared by a staff team of the IMF, following discussions that ended on July 6, 2012, 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 28, 2012. 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 Press Release summarizing the views of the Executive Board as expressed during its August 3, 2012 discussion of the staff report that completed the request and/or review.
- A statement by the Executive Director for Morocco.

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

Letter of Intent sent to the IMF by the authorities of Morocco*
Technical Memorandum of Understanding*

*Also included in Staff Report

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

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

INTERNATIONAL MONETARY FUND

MOROCCO

Request for an Arrangement Under the Precautionary and Liquidity Line

Prepared by Middle-East and Central Asia Department
(in Consultation with other Departments)

Approved by Adnan Mazarei and Tom Dorsey

July 28, 2012

Mission: Rabat, July 2–6, 2012. The mission met with Minister of Economy and Finance Baraka, Bank Al-Maghrib Governor Jouahri; Minister Delegate to the Minister of economy and finance in charge of the Budget El Azami; and other senior officials.

Team: Mr. Guillaume (head, WHD); Mr. Dauphin, Mr. Furceri, and Ms. Mazraani (all MCD); and Mr. Leichter (SPR). Mr. Mazarei (MCD) and Mr. Dairi (OED) participated in key meetings.

Discussions: In light of economic risks in Europe, and of uncertainties on global oil prices that could affect the balance of payments, the focus was on the role of a precautionary PLL, on policies to support potential growth, reduce unemployment, increase Morocco's resilience to external risks, and on fiscal measures to ensure macroeconomic stability.

PLL request: The authorities have requested a two-year PLL arrangement, which they intend to treat as precautionary, with access of 400 percent of quota (SDR 2.35 billion) in the first year, and an additional 300 percent of quota (SDR 1.77 billion) during the second year to help protect the economy against external risks.

Publication: The authorities have agreed to the publication of the staff report.

Exchange arrangement and Article VIII status: Morocco has a conventional peg arrangement and 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

Recent developments: Morocco has a track record of strong economic policies and solid economic performance. But, it has recently been affected by high international oil prices, domestic and regional social tensions, and a weaker external environment. In response to the social movements, a political reform process was initiated in 2011, and culminated in the appointment on November 29, 2011 of the head of the Justice and Development Party to lead the new coalition government. Despite headwinds, real GDP growth accelerated to about 5 percent in 2011, the highest rate in the Middle East and North Africa (MENA) region, while average inflation declined below 1 percent, the lowest rate in MENA. However, higher oil prices led to a widening of the current account and fiscal deficits, the latter being largely driven by an increase in the subsidy bill. These pressures persisted into the beginning of 2012, prompting the authorities to take corrective measures, including the increase in energy-related administered prices in early June, and to outline a medium-term consolidation strategy to ensure fiscal sustainability, while supporting inclusive growth.

Outlook: Domestic demand is expected to support strong nonagricultural GDP growth in 2012, and potential growth is expected to increase by one percentage point (pp) over the medium term, reflecting policy measures to enhance the business climate, governance, and competitiveness. The current account deficit is expected to decline by 0.6 pp to 7.4 percent of GDP in 2012, and improve further over the medium term. The fiscal deficit is also expected to decline by about 0.8 pp in 2012 to 6.1 percent of GDP, to 5.3 percent in 2013, and to less than 3 percent by 2017, largely on account of a significant reduction in subsidy outlays.

Risks: Notwithstanding Morocco's sound policies and fundamentals, there are risks to its balance of payments, mainly from a potential shock to international oil prices and a sharp growth decline in Europe. To insure against these risks, the authorities have expressed interest in a PLL arrangement, which they intend to treat as precautionary. There are also risks of social tension, especially if political uncertainty in the region increases.

PLL Discussions: Staff's assessment is that Morocco meets the PLL qualification criteria of sound economic fundamentals and institutional policy frameworks, performs strongly on three of the five PLL qualification areas without substantial underperformance in any area, and does not face any of the circumstances under which the Fund may not approve a PLL arrangement. Given the potential size and persistence of oil prices and euro-zone-related economic uncertainties, staff believes that a two-year precautionary arrangement would be appropriate, with access equivalent to 400 percent of quota (SDR 2.35 billion) in the first year, and an additional 300 percent (SDR 1.77 billion) in the second year. A PLL arrangement would support the authorities' medium-term framework, and facilitate continued market access, while addressing potential balance of payments needs and vulnerabilities.

I. RECENT ECONOMIC AND POLITICAL DEVELOPMENTS

1. **A political reform process was initiated in March in 2011 in response to the “February 20” social protest movement.** A new constitution was adopted by referendum on July 1, 2011, elections were held in November 2011, and the head of the Justice and Development Party, which received the highest number of votes during the elections formed a new coalition government in January 2012. Local elections will follow the adoption of the planned new regionalization and budget organic laws.
2. **The new constitution paves the way for broad-ranging political changes and reforms.** These include strengthening the role of parliament through greater oversight powers over the executive; elevating the status of the prime minister to that of head of government; enhancing the independence of the judiciary; respecting universally recognized human rights; establishing important institutions, including the National Council for Human Rights, the Competition Council, and the National Authority for Integrity and for the Prevention and Fight against Corruption; and establishing advanced regionalization as a democratic and decentralized system of governance. While these political reforms are important steps in addressing social demands, pressures persist for further reforms to address, among other issues, still-high youth unemployment, income inequalities, and governance.
3. **Despite sluggish growth in Europe and regional tensions, real GDP growth accelerated from 3.7 percent in 2010 to 4.9 percent in 2011, the highest rate in the MENA region** (Figure 1). The negative impact of weak external demand was more than offset by strong investment in manufacturing and construction, as well as robust private consumption supported by an increase in real wages, low inflation, and an acceleration of private-sector credit growth. Unemployment declined slightly from 9.1 percent in 2010 to 8.9 percent in 2011, but remained high among the youth at 17.9 percent.
4. **Average inflation declined to about one percent, the lowest rate in MENA** (Figure 2). The absence of significant demand pressures and a decline in food prices contributed to reduce inflation to 0.9 percent in 2011. Period-average core inflation, excluding food and energy items, also remained moderate at 0.7 percent. Following the increases in several domestic energy prices, inflation increased to 1.9 percent (year-on-year) in June, while core inflation remained low at 0.6 percent.
5. **Rising oil prices led to a widening of the current account deficit from 4.3 percent of GDP in 2010 to about 8 percent in 2011, despite strong export performance, and high growth of remittances and tourism** (Figure 1). Notwithstanding a 50 percent increase in net FDI, the financial account also weakened somewhat, resulting in a decline of gross international reserves from \$23.6 billion (equivalent to 5.7 months of imports of goods and services) in 2010 to \$20.6 billion in 2011 (equivalent to about 5 months of imports). The dirham depreciated by 1.9 percent in real effective terms, remaining broadly in line with

fundamentals (Figure 1).¹ A high energy import bill associated with high international oil prices, delays in disbursement of official financing, and a deceleration of remittances and tourism receipts resulted in a further decline in gross international reserves of about \$3½ billion in the first six months of 2012.

6. Higher oil prices also contributed to a widening of the fiscal deficit from 4.4 percent of GDP in 2010 to 6.9 percent in 2011 (Figure 3). While an increase in the wage bill in response to pressing social demands was offset by a reduction in nonessential current spending, higher oil prices translated into higher subsidy outlays and a widening of the fiscal deficit. As a result, government debt increased from 51 percent of GDP in 2010 to about 54 percent in 2011. However, the cyclically-adjusted balance (net of subsidies spending) improved from -0.1 percent of GDP in 2010 to 1.1 percent of GDP in 2011, reflecting a significant decrease in non-subsidy discretionary spending. During the first five months of 2012, expenditure and revenue were on track to meet budget targets. While the subsidy bill reached about 50 percent of the annual budget projections due to high international oil prices, this was offset by lowered investment and other expenditure.

7. Monetary and financial conditions remained broadly supportive of growth (Figure 2). The financial system continued to be an important driver of economic growth, and remained resilient to the financial turmoil in Europe. Despite a slight decline in liquidity associated with higher money in circulation and lower international reserves, the growth of credit to the economy accelerated from 7.4 percent in 2010 to about 10 percent in 2011, driven by high housing and private consumption credit. However, credit growth decelerated from 10 percent at end-2011 to 7 percent at end-March 2012. To mitigate the decline in structural liquidity, the central bank expanded its money market intervention, increased its refinancing to banks to 5 percent of bank deposits at the end of July 2010, and progressively lowered reserve requirements to 6 percent while withdrawing passbook savings accounts from the reserve base. Interbank and short-term government yields stayed close to the policy rate. Long-term government bond yields also remained stable at about 4.2 percent—0.3 percent lower than at the time of the last international bond issuance in September 2010.

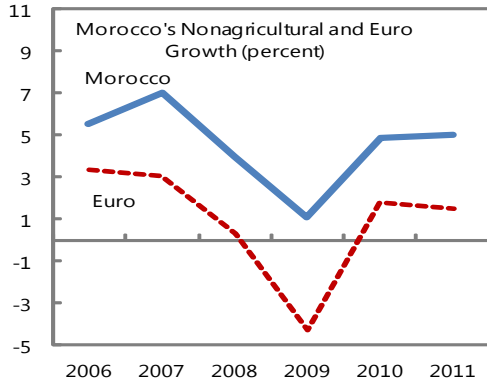
8. To address the increasing macroeconomic pressures, the authorities have taken action, through, among other measures, significant increases in several domestic energy prices in early June.² The domestic energy price increases are part of a broader agenda to

¹ While the medium-term current account deficit is lower than the current account norm, this difference is not statistically significantly different from zero.

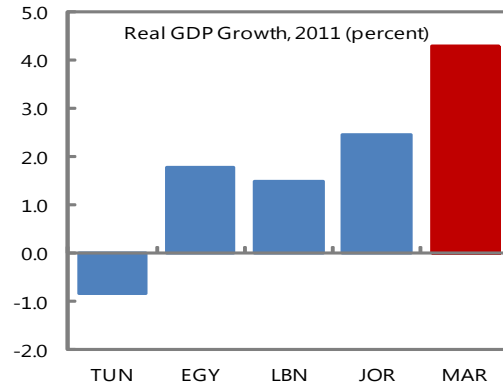
² On June 2, the prices of diesel, gasoline, and fuel oil were increased from 7.15 dirham/liter to 8.15, 10.18 dirham/liter to 12.18, 3678 dirham/ton to 4666.04, respectively. To fully close the gap with international prices (including distribution margin and costs and taxes), the prices of diesel and fuel should increase by more than 30 percent, the price of gasoline by about 15 percent.

Figure 1. Morocco: Real and External Developments

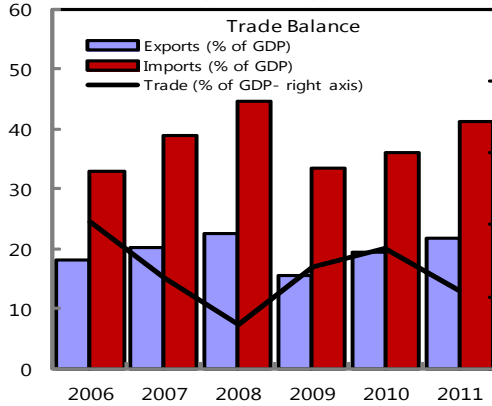
Despite the slowdown in the euro zone, nonagricultural growth slightly accelerated in 2011...



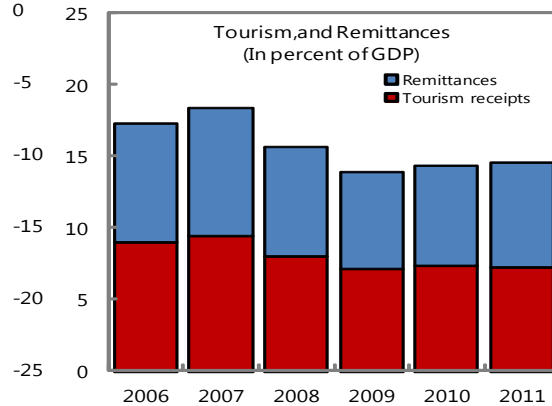
...and overall growth remained the highest in the region.



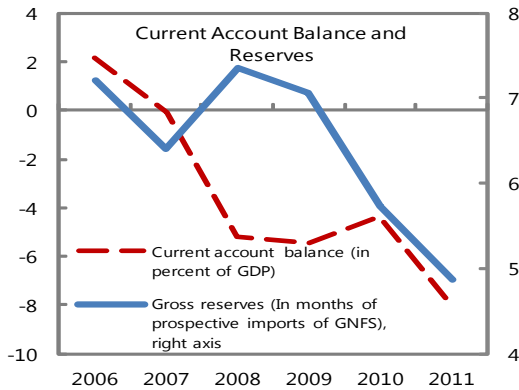
Imports grew faster than exports, due to higher energy prices,



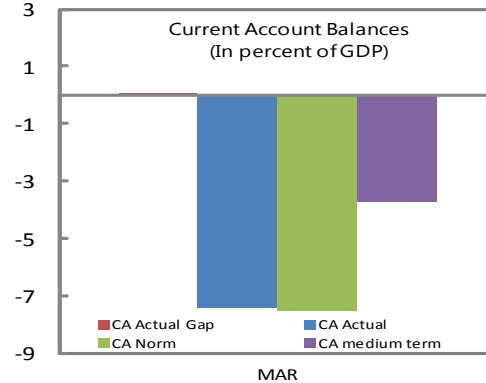
...and despite stable tourism receipts, and an increase in remittances...



...the current account deficit widened, leading to some decline in reserves.



However, the current account remains in line with fundamentals.

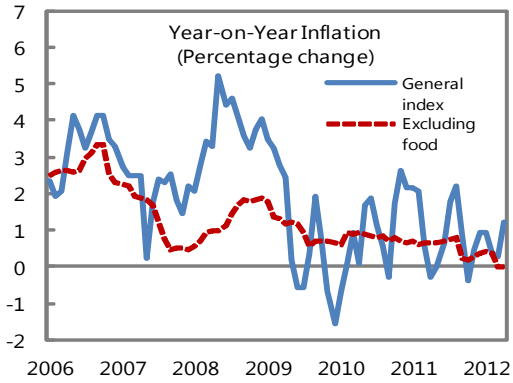


Source: RES EBA exercise.

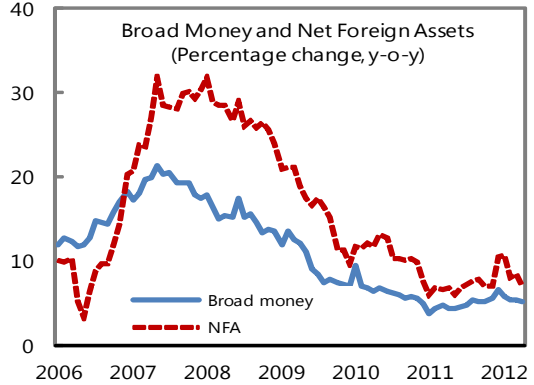
Sources: Moroccan authorities; and IMF staff estimates.

Figure 2. Morocco: Monetary and Financial Sector Developments

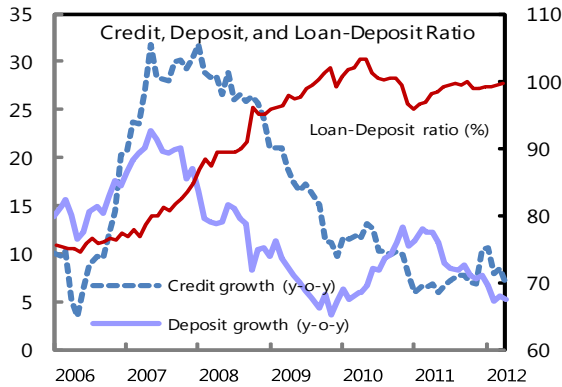
Inflation remains low.



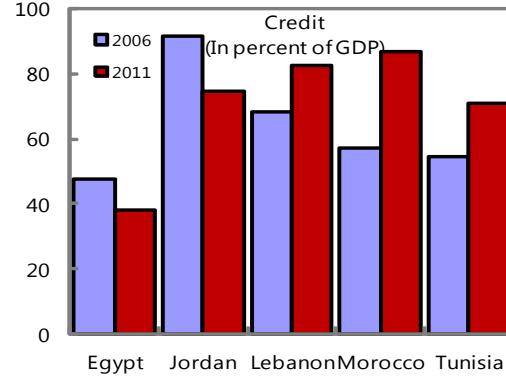
Broad money growth has increased moderately, as has credit growth...



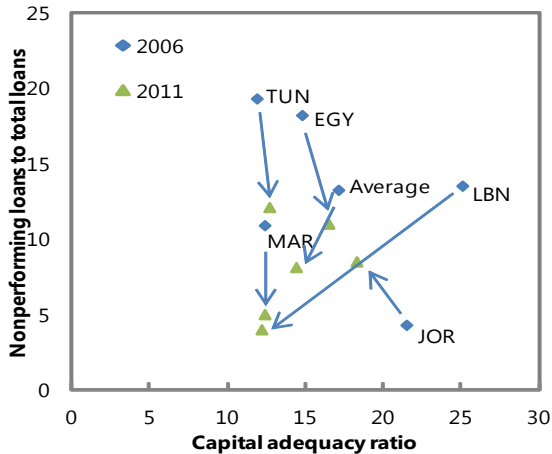
...despite a decline in liquidity.



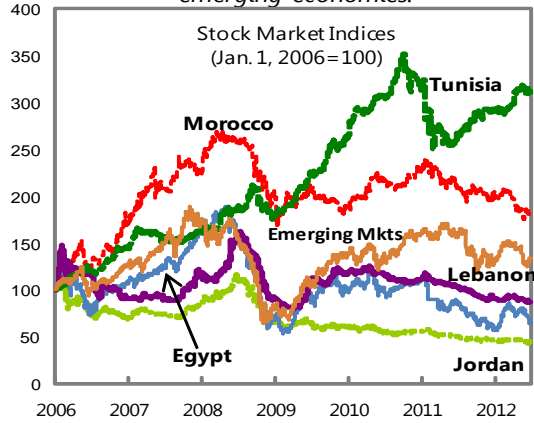
Financial deepening has increased markedly in recent years.



Financial soundness indicators also improved,



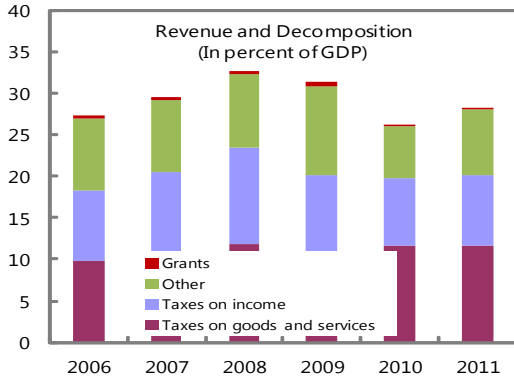
...and the growth in the stock market index remained higher than in other emerging economies.



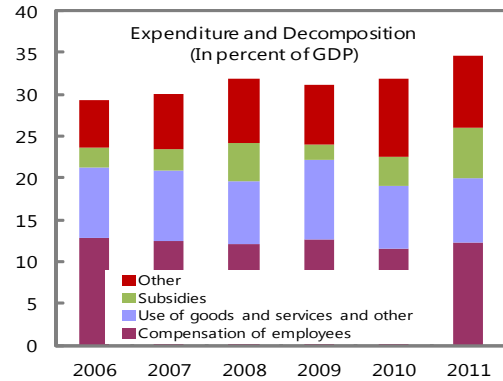
Sources: Moroccan authorities; and IMF *Global Financial Stability Report*.

Figure 3. Morocco: Fiscal and Financial Market Developments

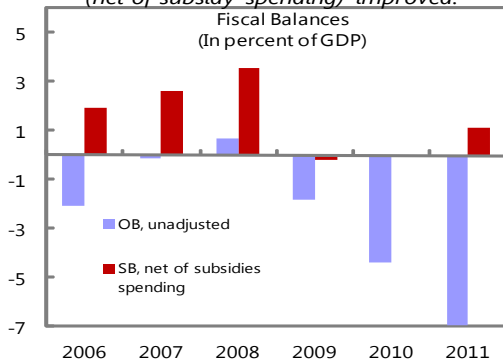
Despite lower tax rates, revenues remained broadly stable,...



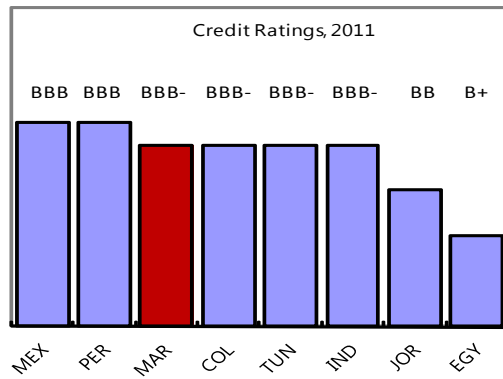
...while expenditures increased, mainly as a result of higher subsidy outlays,



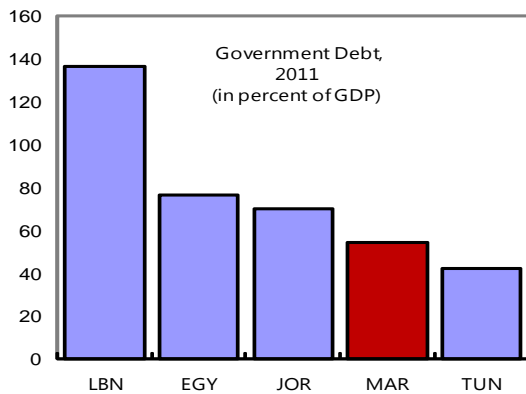
...resulting in a worsening of the overall fiscal deficit, though the structural balance (net of subsidy spending) improved.



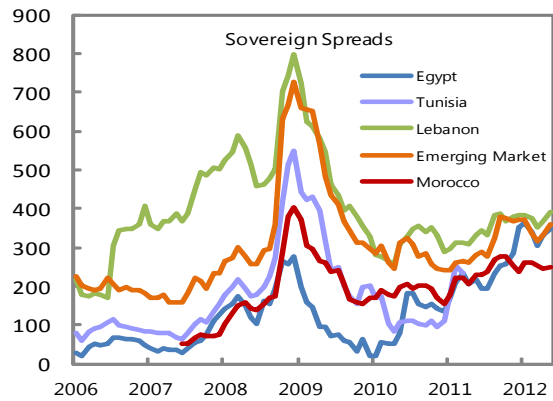
Rating confirms adequate payment capacity,...



...and the public debt-to-GDP ratio remains one of the smallest in the region,



....as do sovereign spreads.



Sources: Moroccan authorities; and IMF staff estimates.

improve the targeting and effectiveness of social protection, and ensure fiscal sustainability. These fiscal measures, combined with the recent decline in international oil prices, are expected to help contain the current account deficit and maintain international reserves at a comfortable level.

II. MACROECONOMIC OUTLOOK AND AUTHORITIES' POLICIES

A. Growth, Employment, and Inflation Outlook

9. **Overall real GDP growth is projected to slow from 4.9 percent in 2011 to 2.9 percent in 2012, largely as a result of poor rainfall.** Despite sluggish growth in advanced economy trading partners, nonagricultural GDP growth is projected to decline only slightly, from 5.0 percent in 2011 to 4.7 percent in 2012, as domestic demand will remain supported by an increase in government productive spending, and favorable monetary conditions. The nonagricultural output gap is projected to remain positive in 2012.

10. **A stable macroeconomic environment and the authorities' comprehensive structural reform agenda are expected to increase potential growth over the medium term** (Box 1) (Attachment I, ¶ 5). The authorities' program focuses on enhancing competitiveness, the business climate, and governance, while supporting sectors with high value added. As a result, potential growth is projected to increase from an average of 4.5 percent over the past decade to 5.6 percent by 2016. These reforms should also help support continued strong export performance and FDI inflows.

11. **The authorities have made job creation an important priority** (Box 1) (Attachment I, ¶ 5). They aim at reducing unemployment from 8.9 percent in 2011 to 8 percent by 2016, and at increasing labor force participation rates, by strengthening ongoing active labor market programs (IDMAJ, TAEHIL, and MOUKAWALATI) and fostering employment outside the main cities in the context of the regionalization reform.

B. External Sector Outlook

12. **The current account deficit is expected to decline from 8 percent of GDP in 2011 to 7.4 percent in 2012, and to improve further over the medium term.** Recent measures to tighten fiscal policy, and a decline in international oil prices, combined with an increase in export volumes of phosphates and derived products, the production for exports of new industrial plants, and a pick-up in seasonal tourism receipts should contribute to stabilizing foreign exchange reserves in the second half of 2012, while the authorities' expected international bond issue in the Fall could provide an extra cushion. Over the medium term, the further expansion of new industrial plants and the planned fiscal consolidation will contribute to a reduction of the current account deficit to GDP ratio by almost 3 percentage points over the next two years. FDI is also expected to increase with the implementation of several large- scale investment projects in the tourism, energy, automobile, and aeronautic

Box 1. Morocco: Planned Structural Reforms to Increase Potential Growth

Potential growth is expected to increase by one percentage point over the medium term as a result of the implementation of current and planned policies, including:

1. Further improvement of the business climate by removing remaining barriers to entry, simplifying the regulatory environment for doing business, strengthening administrative information sharing among all agencies interacting with firms, and reducing delays in payments to small and medium-size enterprises;
2. Improvement of economic governance by increasing transparency and accountability, strengthening the efficiency of public-private partnerships, and improving independence of the judiciary system;
3. Strengthening of the ongoing trade policy reform and trade facilitation by improving the regulatory framework for import standards, and strengthening tariff rationalization;
4. Further development of highly productive economic sectors such as aeronautics, car manufacturing, and electronics;
5. Development of access to alternative energy sources by investing in and developing renewable energy sources, notably solar energy;
6. Reduction of the informal sector by improving business regulation, and reforming the tax treatment of SMEs; and
7. Reduction of structural unemployment, and increase in labor force participation rates by strengthening the ongoing active labor market programs (IDMAJ, TAEHIL, and MOUKAWALATI), improving labor market flexibility, reducing hiring costs, and fostering employment outside of the main cities in the context of the regionalization reform.

sectors, highlighting Morocco's welcoming environment for FDI.³

C. Monetary and Exchange Rate Policies

13. **Monetary policy will continue to focus on controlling inflation, while being supportive of growth** (Attachment I, ¶ 7). Headline inflation is expected to rise to 2½ percent in 2012 due to the recent measures to increase the pass-through of international energy prices, although core inflation will be more contained. Against a background of weakening growth prospects and moderate inflation pressures, the central bank decided to cut the policy rate from 3.25 percent to 3 percent in March 2012. In addition, new measures to boost bank lending to SMEs have recently been introduced. However, the central bank stands ready to act to counter possible second-round impact of domestic energy-related price increases.

14. **The authorities envisage an eventual move to formal inflation targeting in conjunction with a more flexible exchange rate.** While the central bank has a strong record of maintaining low and stable inflation, it is considering over the medium term a move to a more formal inflation-targeting framework in coordination with the planned subsidy reform. Although a more flexible exchange rate regime would be of limited effect in response to shocks affecting Morocco's trading partners (such as an oil shock or a shock to the euro-zone), it would help protect international reserves and help strengthen Morocco's competitiveness vis-à-vis its main competitors.

D. Financial Sector Policies

15. **The authorities are also ensuring that banks have the necessary liquidity.** Bank Al-Maghrib (BAM) will offer to banks a broader range of refinancing instruments to adjust their balance sheets, such as securitization and covered bonds. It will continue to monitor the implementation of refinancing plans adopted by some banks, in order to ensure that credit growth is supported by stable resources. It will also see that banks hold appropriate liquidity buffers on their balance sheets and adopt plans to deal with liquidity crises.

16. **The central bank is progressively translating the norms of Basel III, particularly those related to capital and liquidity** (Attachment I, ¶ 8). It has already increased the capital adequacy requirement to 12 percent and core capital requirements to 9 percent, effective June 2013. It will also bring up the liquidity ratio in line with international norms and strengthen rules for risk management. BAM will maintain its requirements for adequate funding of such loans. In addition, BAM will strengthen its micro-prudential surveillance in the context of the risk-based approach. In parallel, the Ministry of Finance, BAM, and other regulators will strengthen their coordination in order to preserve financial stability.

³ Morocco's OECD FDI regulatory restrictiveness index score is close to the average for OECD countries and outperforms those of many other emerging economies.

17. **The authorities intend to further develop the financial system by expanding capital markets, while strengthening banks.** Preparatory work for the development of Casablanca into a major regional financial center is on track, and banks and other large companies are now starting to finance themselves on the capital markets.

E. Fiscal Policy

18. **The government increased the administered prices of several energy products in June to limit the impact of higher oil prices on subsidy outlays, and to help reduce the fiscal deficit from 6.9 percent of GDP in 2011 to 6.1 percent in 2012** (Table 3).⁴ The increase in energy prices has helped to reduce the fiscal deficit by 0.6 percent of GDP in 2012. The government intends to continue reducing the fiscal deficit to 5.3 percent in 2013, mainly on account of the full-year impact of these measures. Tax revenues are expected to remain broadly stable in percent of GDP, reflecting improved tax control and monitoring. Nonessential recurrent spending will continue to be reined in, offsetting an increase in the wage bill of about ¼ percent of GDP related to upgrading of the public workforce in the priority areas of health, education, security, and defense, and the full-year effect of the wage increase of May 2011. Starting in 2013, the compensation of employees as a share of GDP is expected to decline owing to a gradual moderation of the public payroll, reflecting the implementation of an improved payroll control and monitoring system, and a stabilization of the workforce. Public investment spending is also projected to increase by about ½ percent of GDP, in 2012 and 2013, to improve basic infrastructure, and will be complemented by a major investment effort of key public enterprises, thereby supporting domestic demand.

19. **Over the medium term, the government intends to ensure better targeting and efficiency of the existing subsidy and social protection system, while limiting its cost** (Box 2). The government strategy to reform the subsidy system will be finalized after broad consultations. The strategy is expected to be based on four pillars:

i. A reduction of subsidies:

- The recent pass-through in some domestic energy prices will reduce subsidy costs by 25 percent on a full year basis;
- Further reduction of subsidies on some sectors has been implemented or is being contemplated. In July 2012, subsidies benefiting the fisheries sector were eliminated ;

⁴ “Other account payables” reported in Table 3 refers to domestic annual flows of accrued but unpaid payments on expenditure items (as per GFSM2001 presentation) common in many countries and do not reflect arrears on previous debt.

ii. Financing for the subsidies:

- The creation of a solidarity fund, as legislated in the 2012 budget law: the fund is expected to be financed by: (i) taxes on tobacco and alcohol; (ii) taxes on public land purchases; and (iii) raising revenues from the more privileged, including through taxes on luxury cars;

iii. Targeting:

- A fully targeted social protection system. The government is currently examining different targeting options, such as the creation of a list of beneficiaries on the basis of the RAMEL system (Box 2), or using the scoring methodology, in consultation with the World Bank;

iv. Hedging mechanism:

- The introduction of a hedging mechanism against oil price volatility, thereby containing the subsidy bill.

20. Fiscal policy aims at reducing the fiscal deficit to 3 percent of GDP over the medium term to ensure fiscal sustainability, while enhancing potential growth

(Attachment I, ¶ 6).⁵ The medium-term fiscal consolidation rests on: (i) moderating the wage bill through an introduction of performance-based compensation, and significant projected retirements; (ii) modernization of the social protection system, including a reduction of subsidies to 3 percent of GDP by 2016; (iii) a gradual moderation of the public payroll; (iv) rationalization of nonessential recurrent spending, including through an improved bidding process; and (v) more effective investment spending through multi-year programming and enhanced coordination of programs. The government also intends to reform the public pension fund to ensure its sustainability. Tax reform will continue to be supportive of growth while stabilizing revenue in percent of GDP through broadening the tax base, strengthening tax administration, and eliminating nonproductive tax exemptions.

III. RISKS TO THE OUTLOOK

21. Recent regional and domestic tensions have highlighted the importance of steadfast implementation of the planned social and economic reforms. While inclusive growth has been enhanced in the past decade (Box 3; Figure 4), resolute implementation of the planned governance, regionalization, and social reforms is necessary to respond to remaining unmet expectations. However, political risks, associated with the implementation of the subsidy reform and the related fiscal consolidation plan, remain.

⁵ The overall and cyclically adjusted deficits are projected to be reduced to less than 3 percent by 2017. The cyclically adjusted budget balance (net of subsidies) is projected to be reduced over the medium term as subsidy outlays are reduced more quickly than other discretionary budget spending.

22. **A marked deterioration of economic activity in the economies of advanced trading partners could have sizeable real spillovers on growth and the balance of payments** (Box 4). However, with low inflation and strong domestic demand, nonagricultural growth is expected to remain resilient to limited shocks. In a severe adverse scenario where advanced economies experience a slowdown similar in magnitude to the one that occurred during the great recession, nonagricultural growth could drop by 2½ percentage points. Financial spillovers are, however, expected to remain limited. The authorities' structural reform agenda to enhance potential growth should increase the economy's resilience to external shocks in the medium term.

23. **Morocco is vulnerable to a spike in international oil prices.** An increase of \$10 per barrel would result in an increase in the energy import bill of about \$0.7 billion (0.6 percent of GDP). Higher oil prices would also hurt Morocco's trading partners, further increasing the current account deficit and reducing growth. Morocco is planning to diversify energy sources, through sizeable investments in renewable energies to reduce its oil dependency in the medium term. It is also considering adopting a hedging strategy against oil price fluctuations.

IV. PRECAUTIONARY AND LIQUIDITY LINE

A. Role of PLL

24. **A precautionary PLL arrangement will support the authorities' policies by providing insurance against exogenous shocks.** The authorities are implementing policies to address external and fiscal vulnerabilities linked to potential adverse developments in Morocco's trading partners and in international oil prices. However, it will take time to rebuild fiscal and external buffers. In this context, a PLL arrangement will provide access to additional financing in the event that actual balance of payments needs arise from risks materializing in the short-term. A PLL arrangement would also strengthen investors' confidence and facilitate international market access by signaling that Morocco's current policies are sound, and that the authorities have adequate resources to draw upon if needed.

Box 2. Morocco's Social Protection System

Morocco's current social protection system relies primarily on a generalized subsidy system, but also includes several more targeted initiatives. The government aims to introduce a more efficient system by gradually replacing universal subsidies with well-targeted assistance, building on the existing framework, including the National Initiative for Human Development, and the targeted pilot programs "RAMED" and "Tayssir." The next steps involve better identification of vulnerable groups and developing a consensus on reform modalities and programs.

The generalized subsidy system—"compensation" system—currently comprises flour, sugar, and petroleum products, including fuel, butane gas, and diesel. While spending on subsidies has averaged 2.4 percent of GDP for the period 2000–10, it almost doubled in 2011 as a result of higher oil prices. Subsidies amounted to about 6.1 percent of GDP in 2011. Energy subsidies alone accounted for 84 percent of the total subsidy bill (or 5.1 percent of GDP) in 2011.

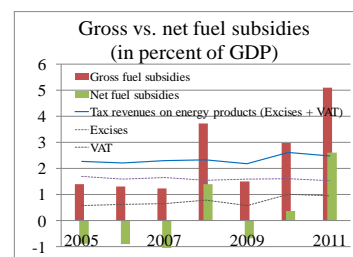
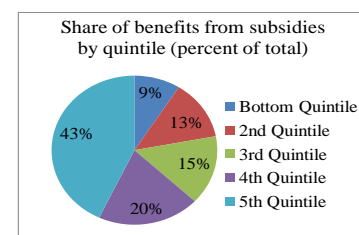
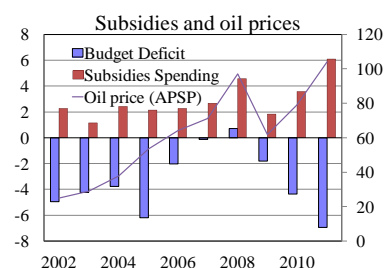
Subsidies are not well targeted, with limited benefits for the poor.

Because the "compensation" subsidy system is universal, access to subsidies is open to the whole population. Studies based on household data published by *Haut-Commissariat au Plan* indicate that about 43 percent of total food and fuel subsidies go to the top quintile of the population. By contrast, the poorest quintile receives only 9 percent of all subsidies. Diesel and fuel subsidies are the most inequitable: only one percent of payments goes to the poorest segments of the population, while 75 percent goes to the top-earning groups.

The VAT and excise taxes levied on energy products partly offset the gross cost of subsidies. VAT tax receipts on energy products have averaged almost 0.75 percent of GDP since 2005. The government increased the VAT rate in 2010 from 7 percent to 10 percent. Excise tax receipts averaged 1.6 percent annually since 2005. While gross fuel subsidies were almost 2.5 percent on average since 2005, fuel subsidies net of tax receipts were close to 0.1 percent on average since then.

The National Initiative for Human Development is the first public program that attempts to comprehensively target vulnerable groups. The initiative was established in 2005 under the Ministry of the Interior. It currently adopts a dual geographic and social targeting approach against poverty in rural communities and specific urban areas. In the first phase (2005–10), 22,000 projects were initiated to benefit a total of 5 million citizens (approximately 15 percent of the population) in several areas (infrastructure, vocational training, improvement of living conditions, etc.).

Two pilot programs "RAMED" and "Tayssir" provide financial support to the poor in the areas of education and health. The program "Tayssir" is designed to prevent school dropout in five targeted geographical areas: l'Oriental, Marrakech-Tensift-Al Haouz, Meknes-Tafilalet, Souss-Massa-Draa and Tadla-Azilal. Scholarships are paid to students subject to compliance conditions (school absences fewer than four times per month). The number of student beneficiaries increased from 88,000 in 2009 to 450,000 in 2011. The program "RAMED" was introduced in 2008 as a pilot in the Tadla-Azilal region. Those eligible receive full or partial benefits for medical services related to hospitalization, surgery, and childbirth. The program is expected to be generalized to 8.5 million people in the country, including 4 million poor inhabitants and another 4.5 million who are vulnerable, in addition to 160,000 prisoners, homeless persons, and orphans.



Box 3. Inclusive Growth in Morocco

Morocco's social indicators have improved over the past decade. Higher economic growth, lower unemployment, better health and educational outcomes, easier access to basic infrastructure, and a marked reduction in poverty rates are tangible evidence of the remarkable progress made by the authorities in fostering inclusive growth. Additional efforts are, however, needed: to improve educational outcomes, and to further reduce the still high youth unemployment and inequality in the distribution of income and access to health care, particularly across regions.

Growth has accelerated remarkably. Real per capita growth has increased considerably over the past two decades, from an average of 1.2 percent per year during the period 1990–99 to 3.6 percent over the period 2000–09.

Unemployment rates have declined substantially. The overall unemployment rate in Morocco has declined from 13.4 percent in 2000 to 8.9 percent in 2011. Youth unemployment has also decreased, but remains relatively high at about 17.4 percent.

Poverty rates have markedly declined. Over the past decade, about 1.7 million people have moved out of poverty, resulting in a 40 percent decline in the poverty rate, which is relatively lower than in other countries in the region. In particular, on the basis of the national poverty line, the share of the population classified as “poor” has decreased from about 16 percent in 1999 to less than 9 percent in 2008.¹ In addition, the reduction in poverty has been uniform between urban (about 50 percent) and rural areas (about 40 percent). However, a large share of the population remains at risk of being poor.

Access to infrastructure has improved. Owing to the launch of several programs, basic infrastructure has significantly improved over the past two decades, particularly in terms of access to drinkable water, electrification rates, and road access rates.

Illiteracy rates have decreased. In conjunction with a marked increase in primary completion rates, the adult illiteracy rate has decreased by 13 pps during the past decade, and remains very low compared to those of other countries. However, despite the marked decrease at the national level, illiteracy rates remain high in rural areas.

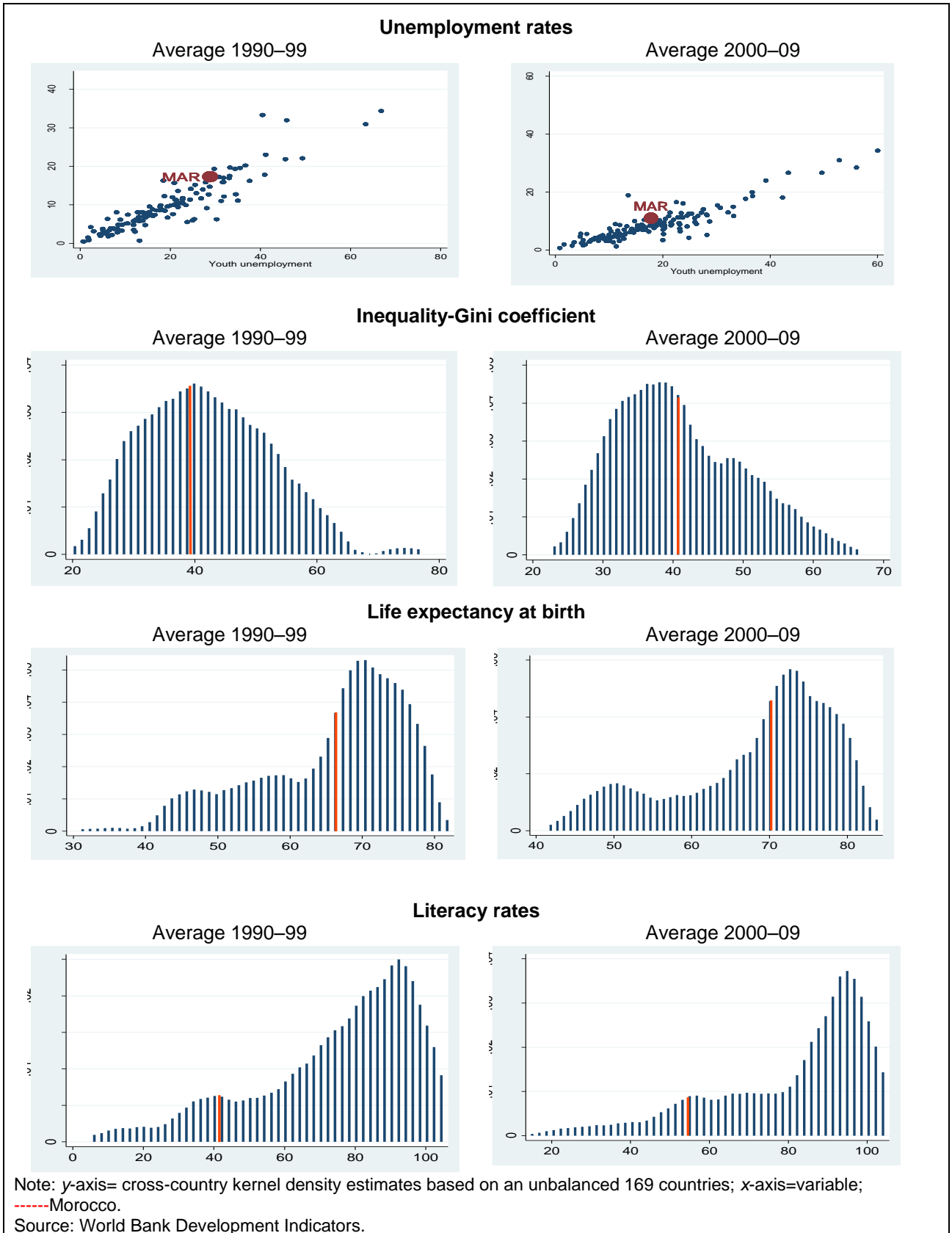
Health outcome indicators have recorded a significant improvement. Life expectancy at birth has increased by almost four years over the past two decades, and mortality rates have dropped by almost 30 percentage points. However, despite these significant improvements at the national level, health outcomes remain unequal across regions and social levels.

Income inequality has increased slightly. The substantial decline in poverty rate has not been matched by a similar improvement in inequality. Indeed, descriptive statistics of the GINI coefficient suggest that inequality has slightly increased over the past decade, and remains persistently high in both urban and rural areas. Similarly, the income share held by the poorest 20 percent of the population has not increased and remains relatively low.

Additional efforts are needed to strengthen inclusive growth. These should focus on improving educational outcomes, and on reducing youth unemployment and inequality in the distribution of income and access to health care, particularly across regions. The implementation of the authorities' planned structural reforms, including the regionalization program, improvement of economic governance by increasing transparency and accountability, strengthening ongoing active labor market programs, and subsidy reform complemented by a better-targeted transfer mechanism and improved social protection, are important steps in this direction.

1/ Other poverty measures (poverty gaps and headcount ratios at \$1.25 to \$2 a day) also point to a significant reduction in poverty over the past decade.

Figure 4. Morocco: Selected Indicators of Inclusive Growth, 1990–2009



Box 4. Advanced Economy Trading Partners

Sluggish growth performance in advanced economy trading partners is expected to hurt short-term growth and current account prospects. By contrast, financial spillovers are expected to be limited.

Real Spillovers are expected to be sizeable.

The deterioration of the economic situation of European trading partners is expected to reduce near-term growth. Staff estimates suggest that a decline of one percentage point in European real GDP growth would result in a decline of about 0.3 percentage point in Morocco's nonagricultural GDP growth, with the effect materializing mainly in the first two quarters and rapidly subsiding afterwards.

A sharp decline in Europe's demand for Moroccan exports is expected to widen the balance of payments. Staff estimates suggest that a one percentage point reduction in growth in Europe could reduce Morocco's balance of payments by about 1.2 percentage points of GDP—0.7 percentage point through the trade balance, 0.3 percentage point through services, 0.1 percentage point through transfers, and 0.1 percentage point through lower FDI.

Financial Spillovers are expected to be limited.

Direct financial spillover risks are low. Gross reserves in excess of eight times foreign wholesale funding should help mitigate the negative impact of a possible drop in foreign wholesale funding. Moreover, deposits with European bank subsidiaries represent only 19 percent of total deposits, and are mostly in local currency and not convertible. In the extreme case of a run on European subsidiaries, the central bank could provide enough local currency liquidity to maintain stability. Furthermore, the non-convertibility of the Dirham significantly reduces the risks of a run on the currency.

Indirect financial spillover risks are also limited. A prolonged recession in advanced economy trading partners may lead to an increase in NPLs. Staff estimates suggest that, on average, a fall of one percent in GDP growth of advanced economy trading partners may increase NPLs by about 0.2 percent due to domestic demand.

B. Qualification Criteria

25. **Morocco has sound economic fundamentals and institutional frameworks, a track record of implementing strong policies; the authorities are committed to maintaining sound policies in the future.** The Executive Board positively assessed Morocco's policies at the most recent Article IV consultation.⁶ Thanks to several years of sound macroeconomic policies, Morocco was well equipped to withstand the 2008 international crisis and to respond to the social demands that have emerged during the Arab Spring. The authorities are committed to maintaining sound policies in the future: these include ensuring medium-term fiscal sustainability, strengthening the resilience of the financial sector, and implementing an ambitious agenda to boost employment and inclusive growth.

26. **Morocco performs strongly in three out of the five areas for PLL qualification (financial sector and supervision, monetary policy, data adequacy) while underperforming moderately in the other two areas (fiscal policy, external position and market access).** While recent increases in the fiscal deficit have resulted in an assessment of moderate underperformance of fiscal policy, the government is committed to a consolidation path consistent with debt sustainability, and has recently taken significant action to reduce subsidies. The moderate underperformance of the external position is related to the recent widening of the current account deficit, which is largely due to exogenous international oil price shocks.

Fiscal policy area (Figure 7).

27. **Morocco has a record of sound public finances over a prolonged period.** In the past five years (2007–11), fiscal policy has been prudent. The overall fiscal balance and the cyclically-adjusted balance have averaged 2.6 and 2.7 percent of GDP, respectively. The primary budget over the same period has been fully balanced and lower than the debt-stabilizing levels. Public debt was on a declining trend until 2011, when rising international oil prices resulted in a significant increase in the fiscal deficit.

28. **The authorities are committed to restoring medium-term fiscal sustainability.** In response to the significant increase in the fiscal deficit, and in line with the macroeconomic stability principle included in the new constitution, the authorities are committed to reducing the deficit and ensuring medium-term sustainability. In particular, fiscal projections for 2012 and 2013 envisage an annual reduction of 0.8 percentage point in the deficit, as a first step

⁶ In the October 2011 Article IV consultations, Directors praised the authorities for “their sound macroeconomic policies and structural and political reforms that have helped Morocco weather the global crisis and respond to pressing social needs.” *The Acting Chair's Summing Up, Morocco Article IV Consultation (SUR/11/87)*.

toward reducing the fiscal deficit to 3 percent of GDP by 2017, partly reflecting a reduction of subsidies to 3 percent of GDP by 2016. This consolidation effort would steadily lower public debt as a percent of GDP, and strengthen medium-term sustainability.⁷

External position and market access area (Figures 8 and 9).

29. **Morocco has experienced an extended period of moderate external vulnerability.** Current account deficits averaged 4.6 percent of GDP over 2007–11, and reserves steadily increased until 2011. While reserves remain at a comfortable level,⁸ recent increases in oil prices have led to a widening of the current account deficit and downward pressures on reserves.

30. **The authorities are implementing policies to strengthen private external flows and reduce external risks.** Recent measures to tighten fiscal policy, and export production of new industrial plants should contribute to stabilizing foreign exchange reserves in the second half of 2012. Over the medium term, Morocco’s welcoming business environment makes it well placed to continue attracting large-scale FDI projects in high-value-added sectors. In addition, the authorities’ ongoing efforts to improve competitiveness and reduce dependence on oil imports—through diversification of its energy sources and investment in renewable energy—will further reduce external vulnerabilities.

31. **Morocco’s exchange rate regime is consistent with the fiscal-monetary policy mix.** While the peg to a currency basket has helped to enhance price stability and insulate the economy from nominal shocks, fiscal and monetary policy have supported robust domestic demand within an environment of stable and low inflation. While the deterioration in fiscal and external positions, including continued loss of reserves, has weakened the appropriateness of the exchange rate regime in relation to the fiscal-monetary policy mix, the authorities have taken actions to restore the fiscal sustainability and consistency of the policy mix.

32. **Morocco has a successful record of access to sovereign international capital markets.** Morocco issued a euro 1 billion bond in September 2010 at 4.5 percent interest

⁷ A favorable interest-growth differential will also contribute to the decline in the public-debt-to-GDP ratio. In particular, during the period 2012–17, the Public Sector Debt Sustainability Framework baseline assumes an average nominal interest rate of 4.5 percent (0.3 percentage point higher than recent levels of long-term government bond yields), derived as nominal interest expenditure divided by previous debt stock and, consistent with an expected increase in nonagricultural potential growth, real overall output growth of 5.1 percent. The increase in real potential growth is not expected to put upward pressures on inflation or nominal interest rates.

⁸ Gross international reserves currently exceed: (i) US\$16.4 billion, (ii) four months of imports, (iii) 1000 percent of short-term external debt on a residual maturity basis, and (iv) 85 percent of the Fund’s composite reserve adequacy metric.

rate. Long-term government bond yields have remained stable at about 4.2 percent—0.3 percent lower than at the time of the 2010 issuance. International bond spreads have increased moderately and remain low compared to other emerging economies (Figure 3). Morocco is considering further issuance of international bonds in Fall 2012.

Monetary policy area (Figure 10).

33. **Monetary policy is credible and transparent, and has a strong record of maintaining low and stable inflation.** Monetary policy has kept inflation at 1.8 percent on average over 2007–11, in line with the objectives set by BAM. BAM affects inflation and inflation expectations by influencing the overnight interest rate (operational target) and the reserve requirement rate, while maintaining a fixed exchange rate against a basket of currencies. Moreover, lending rates and treasury rates have regularly responded to changes in policy rates, suggesting a well-operating monetary transmission mechanism. Detailed information on monetary statistics, policy instruments, and monetary policy decisions is widely accessible to the public, including from the website of the BAM.

Financial sector soundness and supervision area

34. **The financial sector is sound and has been resilient to the financial turmoil in Europe.** The policy of strengthening core capital has been generally successful: (i) the capital adequacy ratio has increased from 11.2 percent in 2009 to 11.7 percent in 2011; (ii) NPLs have steadily declined from 6.1 percent of total loans in 2008 to 4.8 percent in 2011.

35. **The banking sector is the largest in the region, exceeding 110 percent of GDP, and has been supportive of growth.** Furthermore, the authorities are taking steps to promote access to banking and saving services, particularly in rural areas, and to support deposit mobilization. The establishment of the Casablanca Stock Exchange—already one of the most capitalized and diversified in Africa—as a regional and international financial center will also contribute to financial deepening, and will enhance growth and job creation.

Data adequacy area

36. **Morocco subscribes to the Special Data Dissemination Standard (SDDS).** Data provision has been appropriate in all sectors.

Approval Criteria

37. **Morocco does not face any of the circumstances under which the Fund may not approve a PLL:**

- It does not have sustained inability to access international capital markets: it successfully accessed international bond markets in 2010, and bond spreads have remained broadly stable;

- There is no need to undertake a large macroeconomic or structural policy adjustment;
- The public debt position is sustainable in the medium term, with a high probability: the DSA results show moderate risk of debt distress;
- There are no widespread bank insolvencies: financial soundness indicators confirm banking sector stability.

C. Access

38. **The authorities have requested a two-year precautionary arrangement with access of 400 percent of quota in the first year (SDR 2.35 billion) and an additional 300 percent of quota in the second year (SDR 1.77 billion).** They believe a two-year arrangement is appropriate in light of the persistence of external risks. Access of 400 percent of quota (SDR 2.35 billion) for the first year is justified by the potentially severe shocks relating to a European sovereign debt crisis and oil prices. An additional 300 percent of quota (SDR 1.77 billion) would provide a buffer against a scenario of persistent shocks (Box 5). The requested access is near the median and below the average access for recent exceptional cases (Table 12). Morocco meets the criteria for exceptional access (Box 6).

D. Modalities

39. **The conditionality under the PLL arrangement includes indicative targets that quantify government objectives regarding the fiscal deficit and net international reserves, and semi-annual reviews** (Attachment I, Table 1). The fiscal target of the first year of the program is set in line with the 2012 and 2013 fiscal objectives, and the authorities' objective of reducing the budget deficit to less than 3 percent of GDP in the medium term. The indicative target on net international reserves is consistent with maintaining gross international reserves at a comfortable level. Indicative targets for the third review will be proposed at the time of the second review. As required under the PLL decision, the PLL for Morocco includes standard performance criteria on trade and exchange restrictions, bilateral payments arrangements, multiple currency practice, and external arrears. Detailed information on government quantitative objectives and review dates is presented in Tables 1 and 2 of the authorities' written communication, and in Attachment II.

E. Exit

40. **The authorities are committed to reducing external vulnerabilities in the near term.** Notwithstanding Morocco's sound institutional policy frameworks, uncertainty about the euro-zone and possible international oil supply disruptions are key risks to the near-term outlook, risks which are expected to be lowered by the end of the program horizon. To

Box 5. Access Level

Staff prepared a stress case scenario based on a combined oil price and EU growth shock. The proposed access level of 400 percent of quota in the first year of the arrangement, and an additional 300 percent in the second year, would broadly cover the financing needs arising in such a scenario (Table 13).

The scenario assumes:

- an increase of oil prices by US\$10 during the first year of the program, and by about US\$8 during the second year. This increase can be decomposed into: (i) a negative oil supply shock which increases oil prices by about US\$25—equivalent to one standard deviation of the last ten-year average annual change in oil (Brent) price—during the first year of the program, and by US\$18—equivalent to $\frac{3}{4}$ of the standard deviation of the average annual change—for the second year of the program; and (ii) a reduction in oil prices of US\$15 for the first year, and US\$10 for the second year, due to lower growth in Europe;
- a reduction in Morocco’s advanced economy trading partners’ GDP by 4 percentage points during the first year of the program, and 2.5 percentage points during the second year. This shock can be decomposed into: (i) a negative shock to the EU, which reduces advanced economy trading partners’ GDP by 3 percentage points during the first year, compared to the WEO baseline, and 2 percentage points during the second year¹; and (ii) a negative oil-driven growth shock of 1 percentage point during the first year, and 0.5 percentage point for the second year.

Under this scenario, higher oil prices would increase energy imports and widen Morocco’s trade deficit; lower growth in the advanced economy trading partners would widen Morocco’s current account deficit and reduce FDI; and, spillovers from the EU would negatively affect Morocco’s nonagricultural GDP growth, which in turn would partially offset the direct negative effect on the trade balance.

This scenario does not include potential additional financing commitments from bilateral and multilateral sources because they have not been identified at this stage.

The financing gap is defined as the level of financial support needed to bring back gross international reserves to 85 percent of the Fund’s reserve metric, corresponding to the level under baseline projections, after the shock. The use of the 85 percent threshold for the reserve metric² instead of 100 percent is justified by a lower weight for broad money, consistent with the non-convertibility of the Dirham and limited capital controls to residents on outflows. The scenario results in a potential access of SDR 2.35 billion for the first year, and an additional SDR 1.77 billion for the second year, which are in line with access under previous Fund arrangements (Table 12).

A financing gap of similar magnitude could be generated by considering two more extreme individual shocks: (i) an augmentation of oil prices equivalent to an increase of two standard deviations of the last ten-year average annual change in oil (Brent) price—as experienced between April 2010 and May 2011—during the first year of the program, and $1\frac{3}{4}$ of the standard deviation for the second year of the program; (ii) a drop in Morocco’s advanced-economy trading partners’ GDP by 5 percentage points during the first year of the program—in line with previous sovereign debt default events³—and 3 percentage points during the second year.

¹The magnitudes are in line with the stress case scenario presented in the IMF *Spillover Report* (July 2012).

²The metric is defined as a combination of: (i) short-term debt (30 percent); (ii) medium- and long-term debt and equity liabilities (15 percent); (iii) broad money (10 percent); and (iv) exports of goods and services (10 percent).

³Furceri, D., and A. Zdzienicka (2012). “How Costly Are Debt Crises?” *Journal of International Money and Finance*, 31(4), pp 726–742.

Box 6. Exceptional Access Criteria

The authorities' request for a PLL arrangement involves exceptional access and staff's evaluation is that Morocco meets the four exceptional access criteria:

- **Criterion 1:** *The member is experiencing or has the potential to experience actual or potential exceptional balance of payments pressures on the current or capital account, resulting in a need for Fund financing that cannot be met within the normal limits. Morocco does not face actual balance of payments pressures. However, it is exposed to risks of increases in oil prices and economic disruptions in Europe. Staff is of the view that the realization of a stress scenario could give rise to financing needs beyond normal access limits.*
- **Criterion 2:** *A rigorous and systematic analysis indicates that there is a high probability that the member's public debt is sustainable in the medium term. However, in cases where there are significant uncertainties that make it difficult to state categorically that there is a high probability that debt is sustainable over this period, exceptional access would be justified if there is a high risk of international systemic spillovers. Staff analysis is that there is a high probability that the debt will remain sustainable in the medium term. Gross public debt is currently at 54.3 percent of GDP and would decrease based on the authorities' medium-term fiscal strategy. Stress tests indicate that under the standard shocks, debt ratios would remain sustainable over the medium term.*
- **Criterion 3:** *The member has prospects of gaining or regaining access to capital markets within the timeframe when Fund resources are outstanding. In 2010, Morocco issued a €1 billion Eurobond with a maturity of 10 years and an interest rate of 4.5 percent. Investor demand exceeded €2.3 billion, reflecting confidence in Morocco in the international monetary market. Currently, international bond spreads have increased moderately and remain low compared to other emerging economies (Figure 3). Staff is of the view that Morocco could re-issue Eurobonds at present with similar favorable terms.*
- **Criterion 4:** *The policy program of the member provides a reasonably strong prospect of success, including not only the member's adjustment plans but also its institutional and political capacity to deliver that adjustment. Staff judges that the authorities' program has strong prospects of success, with respect to sound policy plans and also to the institutional and political capacity to deliver on those policy plans. Morocco's economic program, based on fiscal restraint and a central bank committed to policies consistent with maintaining price stability, has strong prospects of success. The authorities' track records of sound macroeconomic policies, supported by solid institutions, including an independent central bank, and the macroeconomic resilience observed during the recent global crisis and uprisings that have emerged across the MENA region since early 2011, give confidence in continued sound policies and stability over the longer term.*

reduce vulnerabilities against these risks by the end of the PLL arrangement, the authorities are committed to: (i) increasing near-term growth prospects; (ii) developing access to alternative energy sources; (iii) adoption of a hedging strategy against oil price volatility; (iv) reducing the fiscal deficit by 1½ percent of GDP by 2014; and (v) strengthening reserves. buffer through international bond issuance. As risks from exogenous shocks are reduced, and as external buffers are built, the exit prospects are high.

V. IMPACT ON FUND FINANCES, RISKS AND SAFEGUARDS

41. **Access under the proposed PLL of 700 percent of quota (SDR 4.12 billion) is small relative to the Fund's liquidity.** The Fund's liquidity is expected to remain adequate after approval of a PLL arrangement for Morocco, as discussed further in the supplement assessing the impact on the Fund's finances and liquidity position (Supplement 1).

42. **Risks to the Fund are relatively small.** The authorities are not expected to draw upon the PLL, which is intended to be drawn upon only in the event of actual balance of payment needs arising from adverse shocks. In the event that Morocco were to draw the entire amount available, it would be well-positioned to repay the Fund. However, political and external risks to the program and capacity to repay remain (Supplement 1).

43. **Morocco has agreed to undergo a safeguards assessment, as required under the PLL framework.** The assessment has already been initiated. BAM regularly publishes its audited financial statement in its annual report.

VI. STAFF APPRAISAL

44. **Morocco's track record of sound economic policies helped it withstand the recent economic crisis and regional social events.** Thanks to several years of sound macroeconomic policies, Morocco was well equipped to address the 2008 international crisis and to respond to domestic social demands. The prudent fiscal stance of previous years created the fiscal space necessary to support the political reform process and ensure social cohesion. The exchange rate regime contributed to ensuring low and stable inflation, and in staff's view there is no significant exchange rate misalignment. Staff considers BAM's decision early this year to cut the policy rate by 25 basis points, against a background of weakening growth prospects and moderate inflation, to have been appropriate. The financial sector is sound and has been resilient to the financial turmoil in Europe. Although banks' solvency appears strong by international standards, staff welcomes BAM's efforts to reinforce banks' core capital.

45. **High oil prices have contributed to a build-up of fiscal and external pressures, but the authorities have taken action to address these vulnerabilities and are committed to continuing implementation of sound policies.** Staff believes that the recent increase in domestic administered oil prices is a tangible signal of the authorities' commitment to reform the subsidy system over the medium term. The subsidy reform is a key pillar of the authorities' plan to reduce the fiscal deficit over the medium term and ensure fiscal

sustainability. Staff also welcomes the authorities' agenda of structural reforms to improve social indicators, reduce unemployment, boost competitiveness, and increase long-term potential growth.

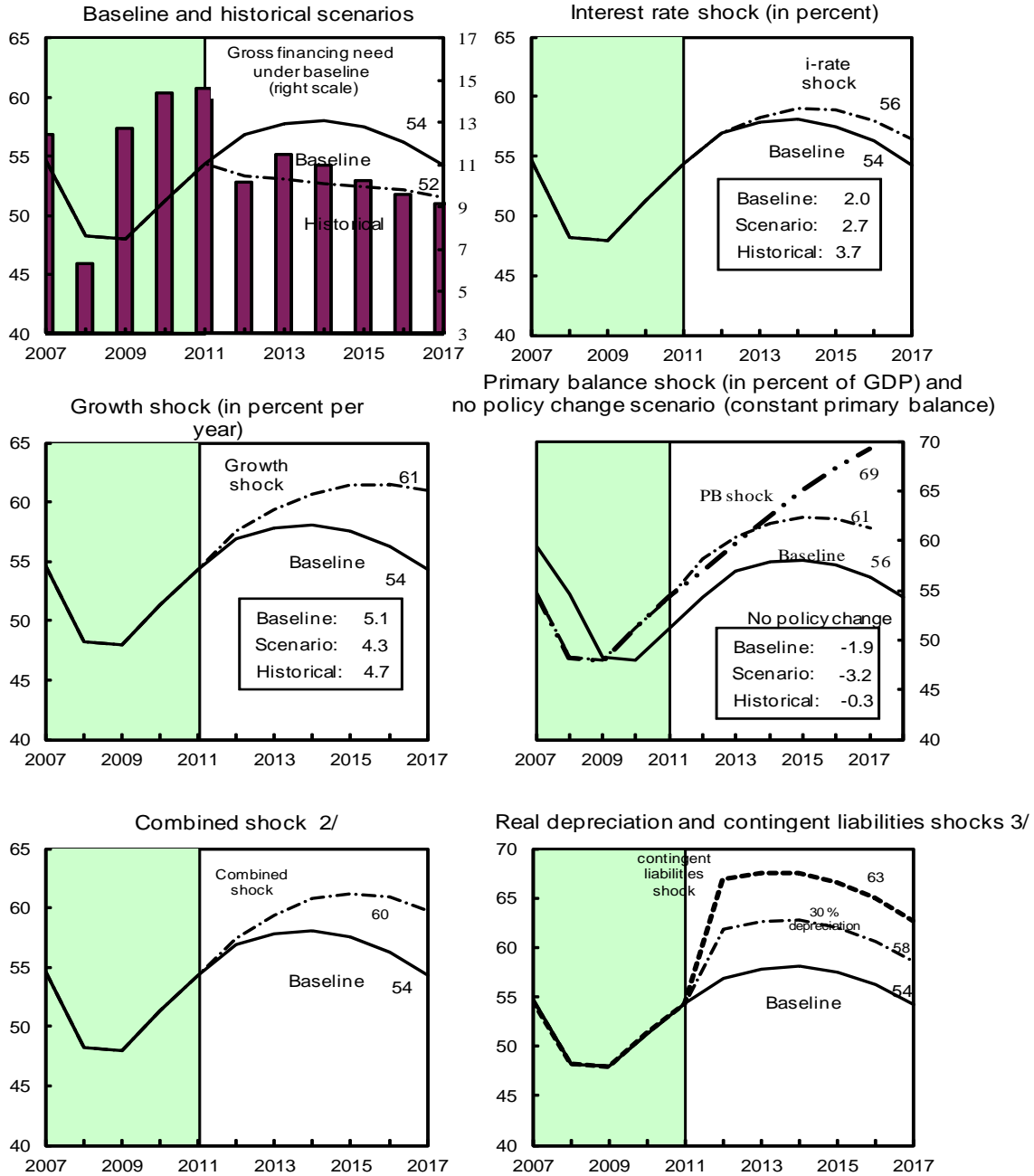
46. **Notwithstanding these positive prospects, Morocco faces external risks that could translate into balance of payments financing needs should an adverse scenario materialize.** Morocco is an oil importer with a large concentration of exports in Europe, making it particularly vulnerable to continued uncertainty in the euro-zone and to possible international oil supply disruptions. These vulnerabilities will be reduced over the medium term by the authorities' intention to: (i) increase potential growth; (ii) diversify energy sources; (iii) adopt a hedging strategy against oil price volatility; and (iv) strengthen reserves buffers through international bond issuance.

47. **Staff assessment is that Morocco meets the PLL qualification criteria.** It has sound economic fundamentals and institutional policy frameworks, and performs strongly on three of the five PLL qualification areas. In addition, Morocco does not substantially underperform on the remaining two qualification areas, fiscal policy and external position. Morocco does not face any of the circumstances under which the Fund may not approve a PLL arrangement. Given the potential size and persistence of oil prices and euro zone related economic uncertainties, staff believes that a two-year precautionary arrangement would be appropriate, with access equivalent to 400 percent of quota in the first year, and an additional 300 percent in the second.

48. **A precautionary PLL arrangement would support the authorities' policies by providing a financing buffer against exogenous shocks.** While the authorities are not expected to draw upon the PLL unless Morocco experiences actual balance of payments needs arising from a significant deterioration in external conditions, the PLL would provide an important source of financing that could help preserve stability and reduce the need for contractionary adjustments in the event of temporary shocks. Moreover, the PLL arrangement should strengthen investor confidence and facilitate access to international capital markets. The level of access requested by the authorities is commensurate with a reasonable stress scenario.

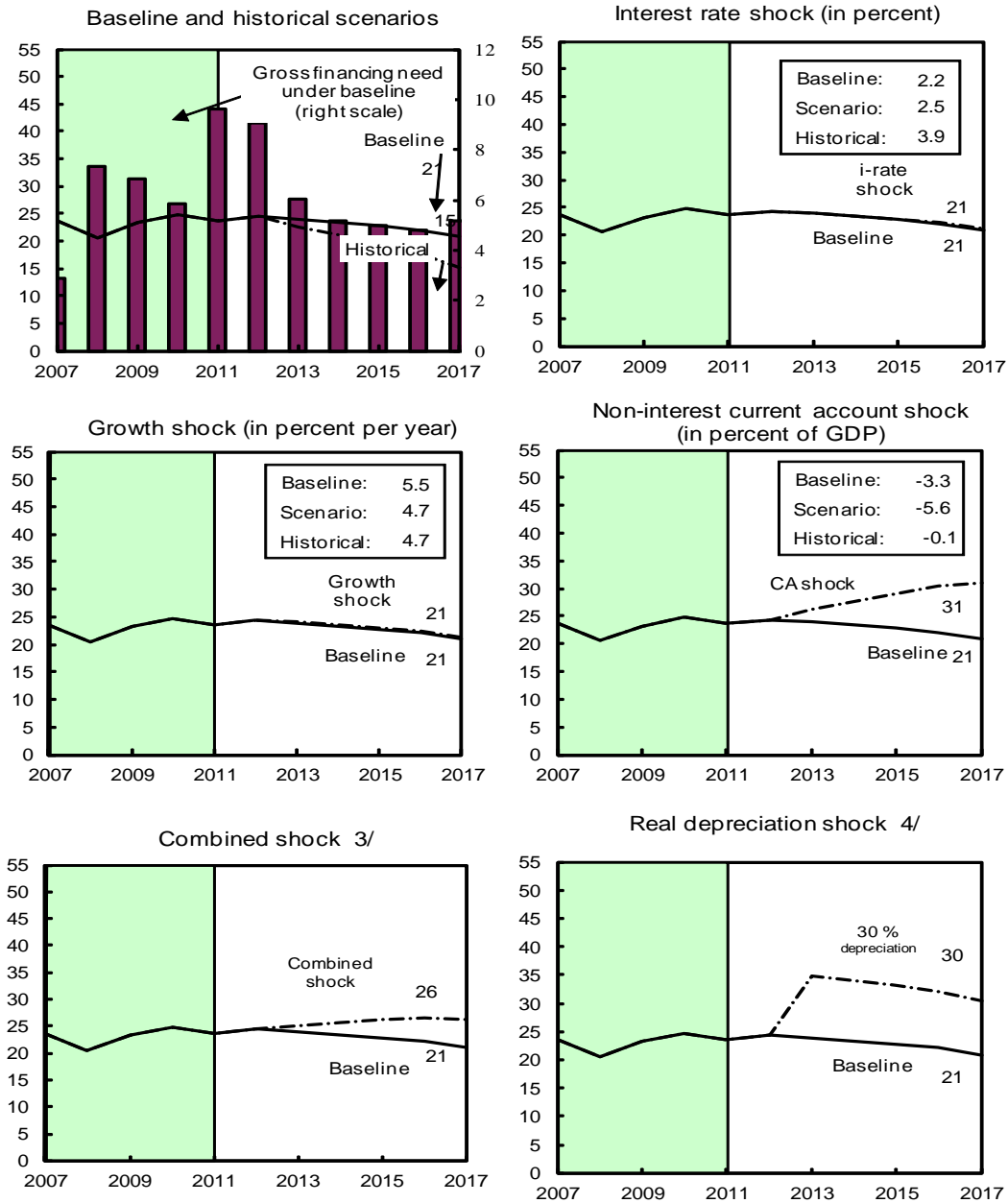
49. **Indicative targets on fiscal and external vulnerabilities are appropriate for Morocco's circumstances.** The fiscal target of the first year of the program is set in line with the 2012 and 2013 budget, and with the authorities' objective of reducing the budget deficit to less than 3 percent of GDP in the medium term. The indicative target on net international reserves is consistent with maintaining gross international reserves at a comfortable level. In light of substantial recent measures to reduce subsidies and a strong commitment to implement policies consistent with these targets, as well as a strong track record of policy formulation and implementation for an extended period of time, staff believes indicative targets are sufficient to monitor implementation of the authorities' policies.

Figure 5. Morocco: Public Debt Sustainability: Bound Tests 1/
(Public debt in percent of GDP)



Sources: IMF country desk data; and IMF staff estimates.
 1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
 2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.
 3/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2012, with real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Figure 6. Morocco: External Debt Sustainability: Bound Tests 1/ 2/
(External debt in percent of GDP)



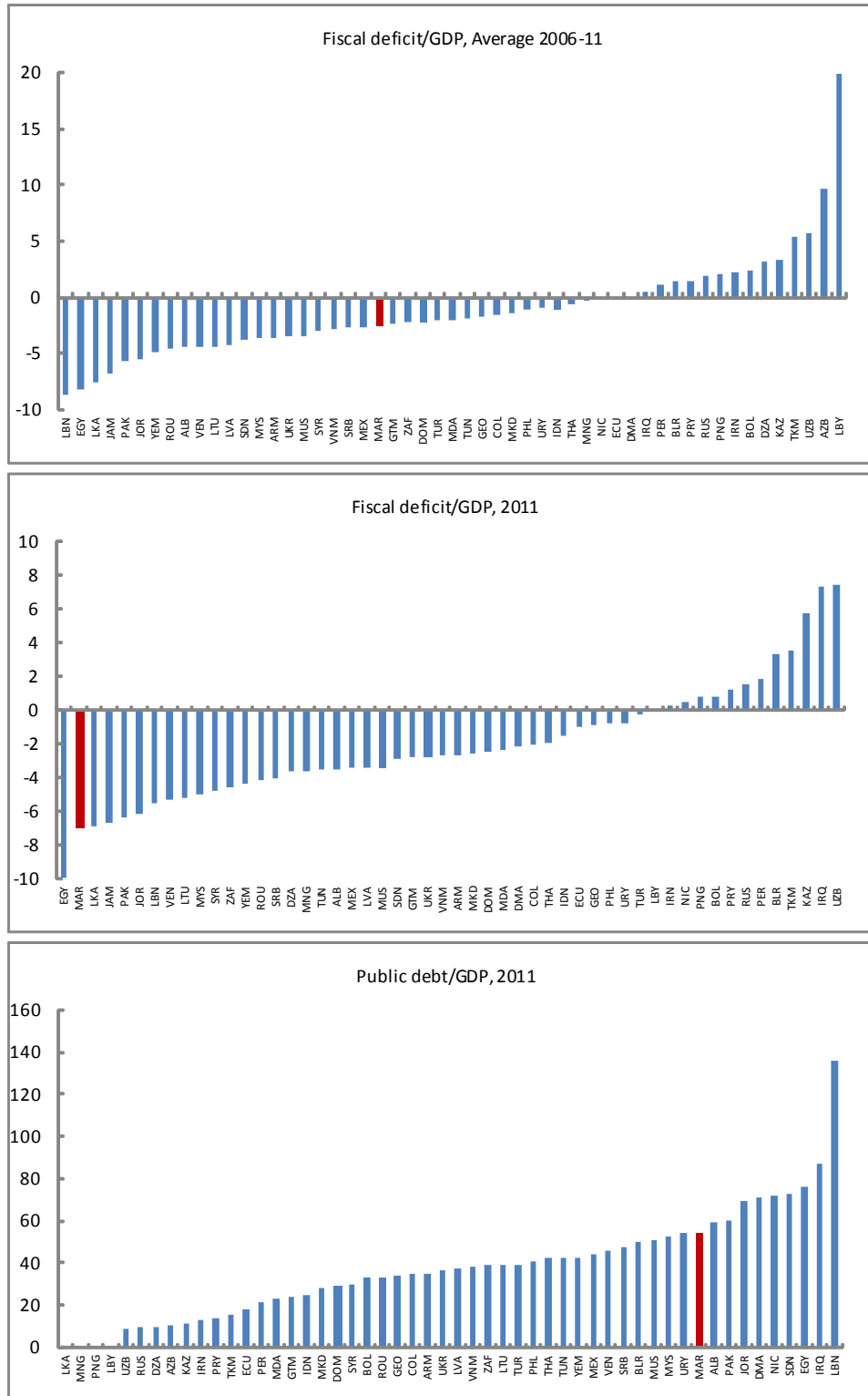
Sources: IMF country desk data; and IMF staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

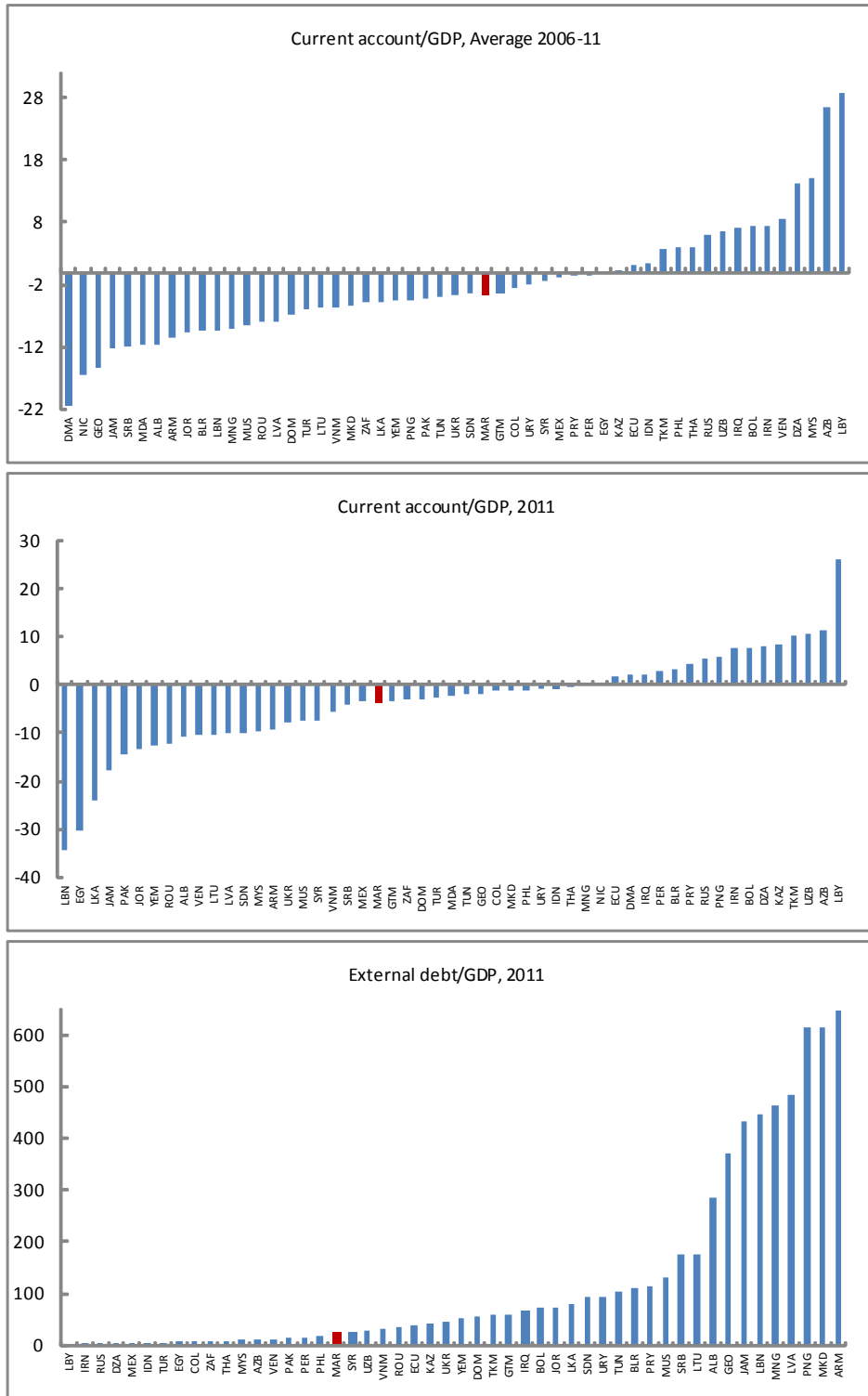
4/ One-time real depreciation of 30 percent occurs in 2012.

Figure 7. Morocco: Public Sector, 2006–11



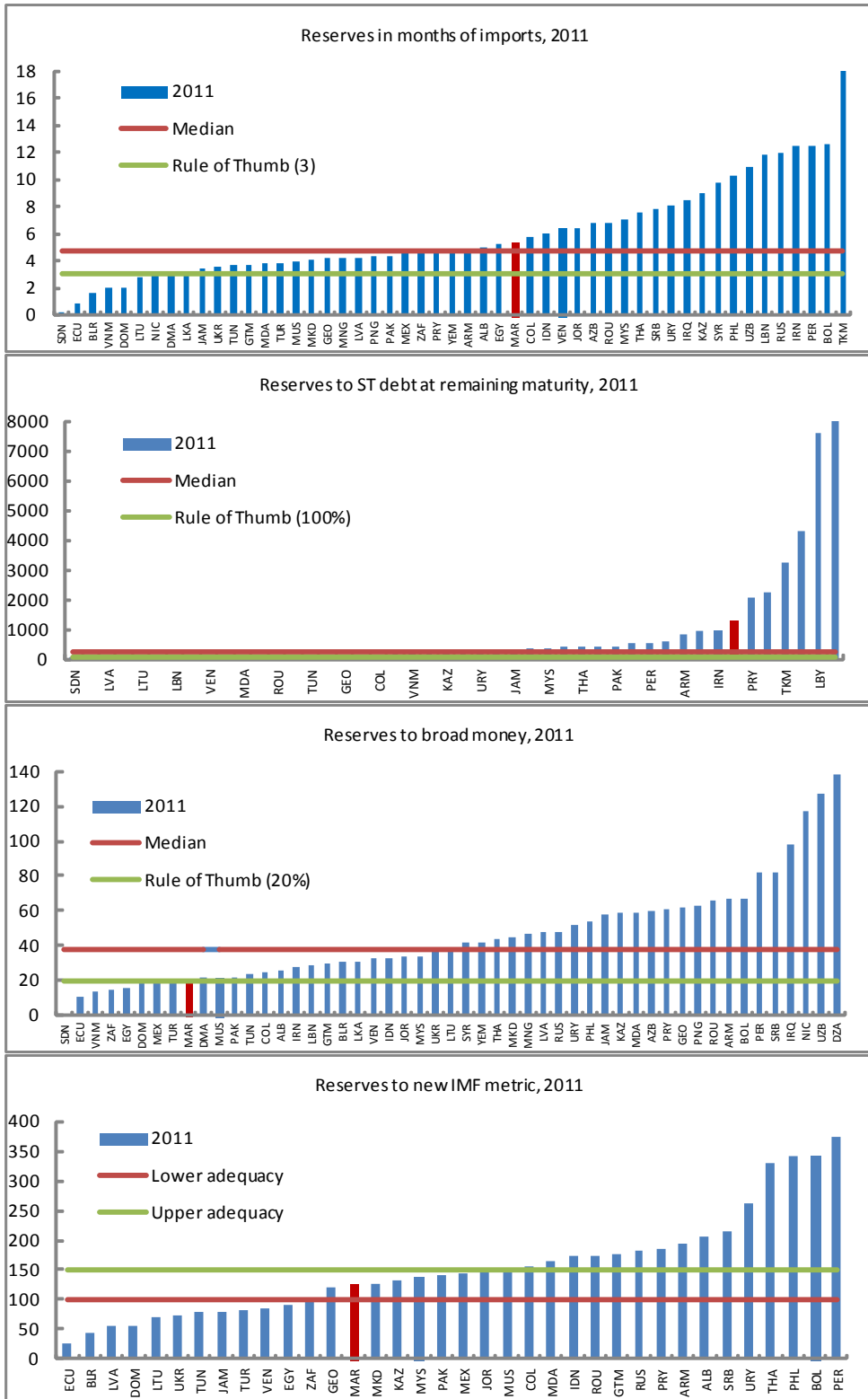
Sources: IMF *World Economic Outlook*, April 2012; and IMF staff estimates.

Figure 8. Morocco: External Sector, 2006–11



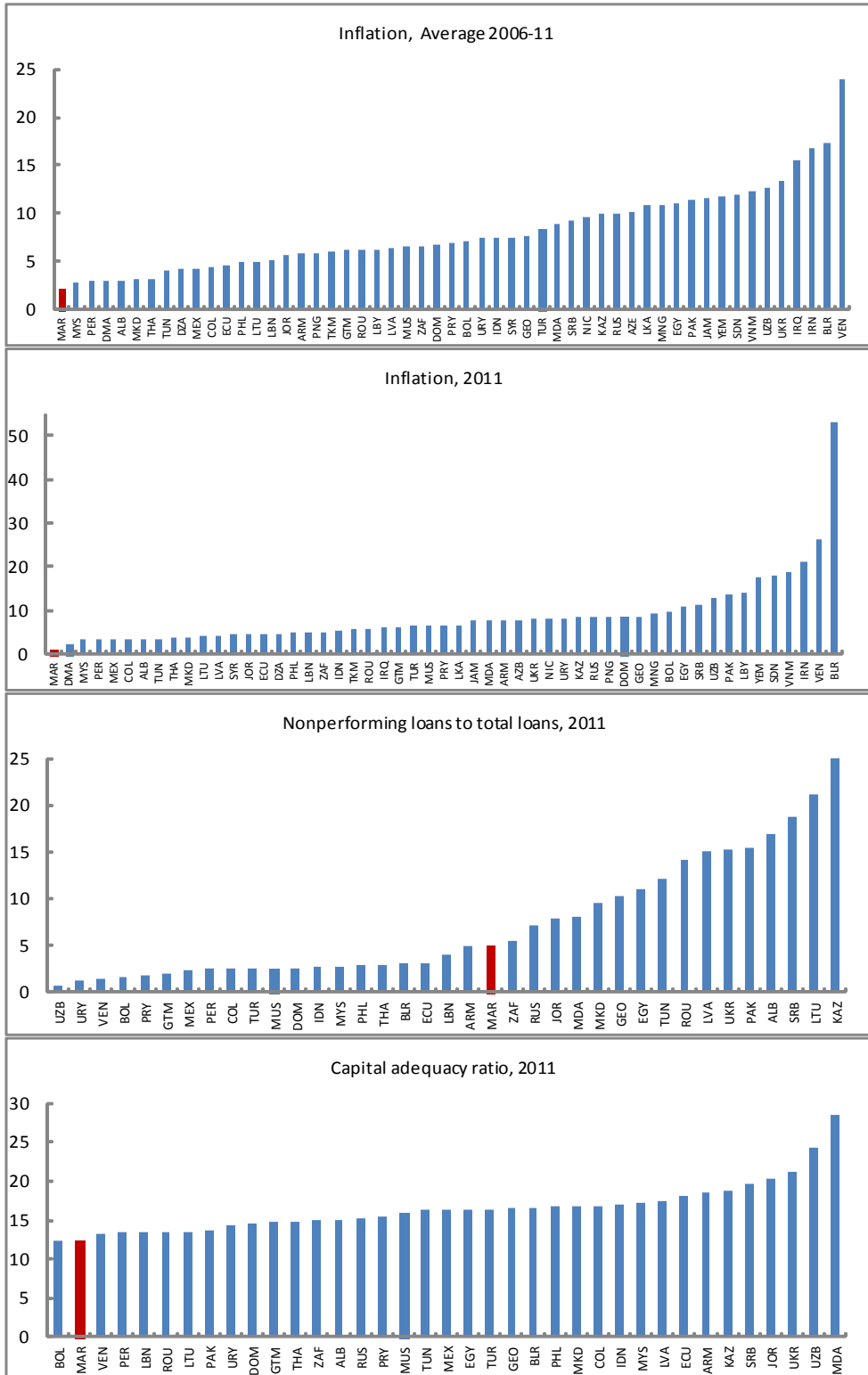
Sources: IMF *World Economic Outlook*, April 2012; and IMF staff estimates.

Figure 9. Morocco: Reserve Coverage in International Perspective, 2011



Sources: IMF *World Economic Outlook*, April 2012; and IMF staff estimates.

Figure 10. Morocco: Monetary and Financial Sector, 2006–11



Sources: IMF *World Economic Outlook*, April 2012; and IMF staff estimates.

Table 1. Morocco: Selected Economic Indicators, 2010–17

	2010	2011	Projections					
			2012	2013	2014	2015	2016	2017
	(Annual percentage change)							
Output and Prices								
Real GDP (market price)	3.7	4.9	2.9	5.5	5.1	5.3	5.6	5.9
Real nonagricultural GDP (market price)	4.9	5.0	4.7	5.0	5.2	5.4	5.7	6.1
Consumer prices (end of period)	2.2	0.9	2.5	2.5	2.5	2.5	2.5	2.6
Consumer prices (period average)	1.0	0.9	2.2	2.5	2.5	2.5	2.5	2.6
	(In percent of GDP)							
Investment and Saving								
Gross capital formation	34.8	34.6	35.0	35.1	35.2	35.4	35.4	35.3
<i>Of which:</i> Nongovernment	30.9	30.0	29.9	29.3	29.5	29.7	29.8	29.7
Gross national savings	30.4	26.6	27.7	30.6	31.5	31.7	31.8	31.6
<i>Of which:</i> Nongovernment	28.4	27.3	28.3	29.3	29.7	29.2	28.8	28.3
	(In percent of GDP)							
Public Finances								
Revenue 1/	27.5	27.6	28.3	28.1	27.5	27.3	26.7	26.6
Expenditure	31.9	34.5	34.4	33.3	32.1	31.0	29.9	29.5
Budget balance	-4.4	-6.9	-6.1	-5.3	-4.6	-3.8	-3.2	-2.9
Primary balance (excluding grants)	-2.3	-4.8	-4.3	-4.1	-3.3	-2.5	-1.8	-1.4
Total government debt	51.3	54.3	56.9	57.8	58.1	57.5	56.3	54.3
	(Annual percentage change; unless otherwise indicated)							
Monetary Sector								
Credit to the private sector 2/	7.4	10.0	8.0	8.3	...	...	...	...
Broad money	4.9	6.6	6.2	6.8	...	...	...	...
Velocity of broad money	0.8	0.8	0.8	0.8	...	...	...	...
Three-month treasury bill rate (period average, in percent) 3/	3.4	3.5	3.2	...	...	...	...	...
	(In percent of GDP; unless otherwise indicated)							
External Sector								
Exports of goods (in U.S. dollars, percentage change) 4/	25.3	22.4	7.0	15.6	7.9	6.9	5.8	6.4
Imports of goods (in U.S. dollars, percentage change)	7.7	25.4	3.4	7.0	5.8	6.9	6.1	7.1
Merchandise trade balance	-16.6	-19.6	-19.7	-17.9	-17.1	-17.0	-16.8	-16.7
Current account excluding official transfers	-4.6	-8.4	-8.1	-5.9	-5.0	-4.8	-4.7	-4.7
Current account including official transfers	-4.3	-8.0	-7.4	-4.5	-3.7	-3.6	-3.6	-3.7
Foreign direct investment	0.8	2.3	2.5	2.7	2.6	2.5	2.3	2.2
Total external debt	24.7	23.6	24.4	23.9	23.4	22.7	22.1	21.0
Gross reserves (in billions of U.S. dollars)	23.6	20.6	17.9	18.8	20.3	21.6	22.8	23.3
In months of next year imports of goods and services	5.7	4.9	4.0	3.9	4.0	4.0	4.0	3.9
In percent of short-term external debt (on remaining maturity basis)	1,546	1,259	1,094	1,144	1,235	1,315	1,388	1,423
Memorandum Items:								
Nominal GDP (in billions of U.S. dollars)	90.8	99.3	98.2	104.8	112.7	121.1	130.7	142.1
Unemployment rate (in percent)	9.1	8.9	...	...	...	...	...	...
Net imports of energy products (in billions of U.S. dollars)	-8.1	-11.1	-11.3	-10.5	-10.2	-10.2	-10.1	-10.2
Local currency per U.S. dollar (period average)	8.4	8.1	...	...	...	...	...	...
Real effective exchange rate (annual average, percentage change)	-4.1	-1.7	...	...	...	...	...	...

Sources: Moroccan authorities; and IMF staff estimates.

1/ Includes changes in the balance of other special treasury accounts.

2/ Includes credit to public enterprises.

3/ Most recent data for 2012.

4/ Starting in 2012, exports of goods growth reflects the export production of Renault.

Table 2. Morocco: Central Government Finance, 2010-17
(In millions of dirhams)

	2010	2011	Projections					
			2012	2013	2014	2015	2016	2017
Revenue	210,390	221,653	239,596	257,295	272,158	290,563	307,908	333,611
Taxes	179,045	189,711	205,290	219,880	234,130	251,052	267,648	290,864
Taxes on income, profits, and capital gains	62,668	68,460	72,363	78,050	83,685	89,931	96,838	105,344
Taxes on property	8,651	9,231	10,522	11,222	12,131	13,156	14,287	15,542
Taxes on goods and services	88,569	93,717	100,124	107,406	115,110	124,654	135,395	147,288
Taxes on international trade and transactions	13,606	13,653	13,173	14,249	14,054	13,952	14,344	15,315
Other taxes	5,551	4,651	9,109	8,953	9,150	9,360	6,784	7,374
Grants	1,869	1,310	4,940	10,890	10,890	11,690	11,690	11,690
Other revenue	29,475	30,631	29,366	26,525	27,138	27,821	28,570	31,057
Expense	214,269	240,332	248,640	252,060	260,406	270,221	280,160	299,526
Compensation of employees	88,588	98,038	106,188	110,548	115,302	120,080	124,763	135,622
Use of goods and services	19,149	22,742	24,049	30,233	31,866	33,587	35,400	38,481
Interest	17,566	18,234	20,244	22,003	23,681	25,561	27,630	30,035
Subsidies	27,195	48,830	51,550	39,422	37,495	36,211	34,537	32,524
Grants	29,180	27,623	29,713	32,956	35,164	37,885	40,932	44,495
Other expense	32,591	24,865	16,897	16,897	16,897	16,897	16,897	18,368
Gross operating balance	-3,880	-18,679	-9,044	5,235	11,752	20,342	27,748	34,084
Net acquisition of nonfinancial assets	29,510	37,097	43,041	53,519	56,862	60,605	64,726	70,360
Net lending / borrowing (overall balance)	-33,390	-55,776	-52,085	-48,284	-45,110	-40,263	-36,979	-36,276
Net lending / borrowing (incl. privatization)	-33,434	-50,126	-48,885	-44,616	-41,163	-36,003	-32,374	-31,671
Net lending / borrowing (excl. grants)	-35,259	-57,086	-57,025	-59,174	-56,000	-51,953	-48,669	-47,966
Cyclical adjusted balance	-27,597	-39,863	-37,494	-36,530	-38,094	-40,465	-36,979	-36,261
Cyclical adjusted balance (net subsidies)	-402	8,967	14,056	2,892	-598	-4,254	-2,442	-3,737
Change in net financial worth	-33,390	-55,746	-52,085	-48,284	-45,110	-40,263	-36,979	-36,276
Net acquisition of financial assets	14	-5,376	-3,200	-3,667	-3,947	-4,260	-4,605	-4,605
Domestic	14	-5,376	-3,200	-3,667	-3,947	-4,260	-4,605	-4,605
Shares and other equity	44	-5,650	-3,200	-3,667	-3,947	-4,260	-4,605	-4,605
Foreign	0	0	0	0	0	0	0	0
Net incurrence of liabilities	33,404	50,370	48,885	44,616	41,163	36,003	32,374	31,671
Domestic	17,496	43,307	36,737	42,193	38,912	33,612	30,330	31,489
Other accounts payable	6,886	9,851	-5,275	0	0	0	0	0
Foreign	15,908	7,063	12,148	2,423	2,251	2,391	2,044	182
Memorandum Item:								
GDP	764,302	803,155	847,715	917,036	988,090	1,066,194	1,154,314	1,254,784

Sources: Ministry of Economy and Finance; and IMF staff estimates.

Table 3. Morocco: Central Government Finance, 2010-17
(In percent of GDP)

	2010	2011	Projections					
			2012	2013	2014	2015	2016	2017
Revenue	27.5	27.6	28.3	28.1	27.5	27.3	26.7	26.6
Taxes	23.4	23.6	24.2	24.0	23.7	23.5	23.2	23.2
Taxes on income, profits, and capital gains	8.2	8.5	8.5	8.5	8.5	8.4	8.4	8.4
Taxes on property	1.1	1.1	1.2	1.2	1.2	1.2	1.2	1.2
Taxes on goods and services	11.6	11.7	11.8	11.7	11.6	11.7	11.7	11.7
Taxes on international trade and transactions	1.8	1.7	1.6	1.6	1.4	1.3	1.2	1.2
Other taxes	0.7	0.6	1.1	1.0	0.9	0.9	0.6	0.6
Grants	0.2	0.2	0.6	1.2	1.1	1.1	1.0	0.9
Other revenue	3.9	3.8	3.5	2.9	2.7	2.6	2.5	2.5
Expense	28.0	29.9	29.3	27.5	26.4	25.3	24.3	23.9
Compensation of employees	11.6	12.2	12.5	12.1	11.7	11.3	10.8	10.8
Use of goods and services	2.5	2.8	2.8	3.3	3.2	3.2	3.1	3.1
Interest	2.3	2.3	2.4	2.4	2.4	2.4	2.4	2.4
Subsidies	3.6	6.1	6.1	4.3	3.8	3.4	3.0	2.6
Grants	3.8	3.4	3.5	3.6	3.6	3.6	3.5	3.5
Other expense	4.3	3.1	2.0	1.8	1.7	1.6	1.5	1.5
Gross operating balance	-0.5	-2.3	-1.1	0.6	1.2	1.9	2.4	2.7
Net acquisition of nonfinancial assets	3.9	4.6	5.1	5.8	5.8	5.7	5.6	5.6
Net lending / borrowing (overall balance)	-4.4	-6.9	-6.1	-5.3	-4.6	-3.8	-3.2	-2.9
Net lending / borrowing (incl. privatization)	-4.4	-6.2	-5.8	-4.9	-4.2	-3.4	-2.8	-2.5
Net lending / borrowing (excl. grants)	-4.6	-7.1	-6.7	-6.5	-5.7	-4.9	-4.2	-3.8
Cyclical adjusted balance	-3.6	-5.0	-4.4	-4.0	-3.9	-3.8	-3.2	-2.9
Cyclical adjusted balance (net subsidies)	-0.1	1.1	1.7	0.3	-0.1	-0.4	-0.2	-0.3
Change in net financial worth	-4.4	-6.9	-6.1	-5.3	-4.6	-3.8	-3.2	-2.9
Net acquisition of financial assets	0.0	-0.7	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Domestic	0.0	-0.7	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Shares and other equity	0.0	-0.7	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	4.4	6.3	5.8	4.9	4.2	3.4	2.8	2.5
Domestic	2.3	5.4	4.3	4.6	3.9	3.2	2.6	2.5
Other accounts payable	0.9	1.2	-0.6	0.0	0.0	0.0	0.0	0.0
Foreign	2.1	0.9	1.4	0.3	0.2	0.2	0.2	0.0

Sources: Ministry of Economy and Finance; and IMF staff estimates.

Table 4. Morocco: Central Government Balance Sheet, 2010-17 (GFS2001)
(In millions of dirhams)

	2010	2011	2012	2013	2014	2015	2016	2017
Net financial worth	-382,408	-428,922	-474,792	-522,428	-566,394	-605,758	-641,828	-673,499
Financial assets	2,040	1,980	1,980	1,980	1,980	1,980	1,980	1,980
Domestic	2,040	1,980	1,980	1,980	1,980	1,980	1,980	1,980
Currency and deposits 1/	2,040	1,980	1,980	1,980	1,980	1,980	1,980	1,980
Foreign	0	0	0	0	0	0	0	0
Liabilities	384,448	430,902	476,772	524,408	568,374	607,738	643,808	675,479
Domestic	292,123	332,302	374,314	416,507	455,419	489,031	519,361	550,850
Securities other than shares 1/	292,123	332,302	374,314	416,507	455,419	489,031	519,361	550,850
Foreign	92,325	98,600	102,458	107,901	112,954	118,707	124,447	124,629
Loans 1/	92,325	98,600	102,458	107,901	112,954	118,707	124,447	124,629

1/ Data for the remaining instruments are currently not available.

Table 5. Morocco: Central Government Finance, 2012 Monthly Projections
(In millions of dirhams)

	Projections 2012					Annual
	June	July	August	September	October	
Revenue	124,826	144,970	159,941	182,045	197,570	239,596
Taxes	104,088	123,064	137,525	157,805	171,437	205,290
Taxes on income, profits, and capital gains	39,588	43,946	47,250	56,750	59,830	72,363
Taxes on payroll and workforce	0	0	0	0	0	0
Taxes on property	6,172	7,054	7,853	8,615	9,468	10,522
Taxes on goods and services	50,494	60,137	68,629	76,489	84,684	100,124
Taxes on international trade and transactions	5,106	8,231	9,213	10,198	11,148	13,173
Other taxes	2,727	3,697	4,580	5,753	6,307	9,109
Grants	0	0	0	0	0	4,940
Other revenue	20,739	21,906	22,417	24,240	26,134	29,366
Expense	128,469	148,497	168,526	188,555	208,583	248,640
Compensation of employees	52,590	61,523	70,456	79,389	88,322	106,188
Use of goods and services	11,058	13,223	15,388	17,553	19,719	24,049
Consumption of fixed capital (if available)	0	0	0	0	0	0
Interest	11,635	13,070	14,505	15,939	17,374	20,244
Subsidies	28,964	32,729	36,493	40,257	44,021	51,550
Grants	12,252	15,162	18,072	20,982	23,892	29,713
Other expense	11,969	12,791	13,612	14,433	15,255	16,897
<i>Gross operating balance</i>	-3,642	-3,527	-8,585	-6,510	-11,013	-9,044
Net acquisition of nonfinancial assets	17,661	21,518	23,408	26,590	30,588	43,041
Net lending / borrowing (overall balance)	-21,304	-25,046	-31,993	-33,100	-41,601	-52,085
Net lending / borrowing (excl. grants)	-21,304	-25,046	-31,993	-33,100	-41,601	-57,025
Change in net financial worth	-21,304	-25,046	-31,993	-33,100	-41,601	-52,085
Net acquisition of financial assets	326	-11,023	-11,483	-6,741	-6,650	-3,200
Net incurrence of liabilities	21,630	14,022	20,510	26,359	34,951	48,885
Domestic	17,969	17,634	22,937	25,068	25,574	36,737
Foreign	3,661	-3,612	-2,427	1,291	9,377	12,148

Sources: IMF staff estimates.

Table 6. Morocco: Central Government Finance, 2012 Monthly Projections
(In percent of annual GDP)

	Projections					
	June	July	August	September	October	Annual
Revenue	14.7	17.1	18.9	21.5	23.3	28.3
Taxes	12.3	14.5	16.2	18.6	20.2	24.2
Taxes on income, profits, and capital gains	4.7	5.2	5.6	6.7	7.1	8.5
Taxes on payroll and workforce	0.0	0.0	0.0	0.0	0.0	0.0
Taxes on property	0.7	0.8	0.9	1.0	1.1	1.2
Taxes on goods and services	6.0	7.1	8.1	9.0	10.0	11.8
Taxes on international trade and transactions	0.6	1.0	1.1	1.2	1.3	1.6
Other taxes	0.3	0.4	0.5	0.7	0.7	1.1
Grants	0.0	0.0	0.0	0.0	0.0	0.6
Other revenue	2.4	2.6	2.6	2.9	3.1	3.5
Expense	15.2	17.5	19.9	22.2	24.6	29.3
Compensation of employees	6.2	7.3	8.3	9.4	10.4	12.5
Use of goods and services	1.3	1.6	1.8	2.1	2.3	2.8
Consumption of fixed capital (if available)	0.0	0.0	0.0	0.0	0.0	0.0
Interest	1.4	1.5	1.7	1.9	2.0	2.4
Subsidies	3.4	3.9	4.3	4.7	5.2	6.1
Grants	1.4	1.8	2.1	2.5	2.8	3.5
Other expense	1.4	1.5	1.6	1.7	1.8	2.0
<i>Gross operating balance</i>	-0.4	-0.4	-1.0	-0.8	-1.3	-1.1
Net acquisition of nonfinancial assets	2.1	2.5	2.8	3.1	3.6	5.1
Net lending / borrowing (overall balance)	-2.5	-3.0	-3.8	-3.9	-4.9	-6.1
Net lending / borrowing (excl. grants)	-2.5	-3.0	-3.8	-3.9	-4.9	-6.7
Change in net financial worth	-2.5	-3.0	-3.8	-3.9	-4.9	-6.1
Net acquisition of financial assets	0.0	-1.3	-1.4	-0.8	-0.8	-0.4
Net incurrence of liabilities	2.6	1.7	2.4	3.1	4.1	5.8
Domestic	2.1	2.1	2.7	3.0	3.0	4.3
Foreign	0.4	-0.4	-0.3	0.2	1.1	1.4

Sources: IMF staff estimates.

Table 7. Morocco: Balance of Payments, 2010-17
(In billions of U.S. dollars, unless otherwise indicated)

	2010	2011	Projections					
			2012	2013	2014	2015	2016	2017
Current account	-3.9	-8.0	-7.2	-4.7	-4.2	-4.4	-4.7	-5.3
Trade balance	-15.1	-19.4	-19.3	-18.7	-19.2	-20.5	-21.9	-23.7
Exports, f.o.b.	17.6	21.5	23.0	26.6	28.7	30.7	32.5	34.5
Agriculture	3.2	3.0	3.2	3.4	3.6	3.8	4.0	4.3
Phosphates and derived products	4.2	6.0	6.7	7.4	8.2	9.0	9.7	10.6
Imports, f.o.b.	-32.6	-40.9	-42.3	-45.3	-47.9	-51.2	-54.4	-58.2
Energy	-8.1	-11.1	-11.3	-10.5	-10.2	-10.2	-10.1	-10.2
Capital goods	-7.9	-8.6	-9.0	-9.9	-10.9	-12.0	-13.3	-14.7
Food products	-3.5	-4.7	-4.9	-5.2	-5.7	-6.5	-6.7	-6.9
Services	5.1	5.4	5.5	6.0	6.4	6.7	7.1	7.5
Tourism receipts	6.7	7.3	7.0	7.2	7.3	7.4	7.5	7.7
Income	-1.3	-2.0	-2.0	-2.1	-2.0	-2.0	-1.9	-1.9
Transfers	7.3	8.1	8.7	10.1	10.7	11.3	12.0	12.8
Private transfers (net)	7.0	7.8	8.0	8.7	9.3	9.9	10.6	11.4
Workers' remittances	6.4	7.2	7.1	7.6	8.1	8.7	9.4	10.1
Official grants (net)	0.2	0.3	0.7	1.4	1.4	1.4	1.4	1.4
Capital account	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	5.4	5.6	4.6	5.7	5.8	5.9	6.0	5.9
Direct investment	0.7	2.3	2.5	2.9	2.9	3.0	3.1	3.1
Privatization	0.0	0.0	0.4	0.4	0.5	0.5	0.5	0.5
Portfolio investment	0.1	-0.2	0.1	0.1	0.1	0.1	0.1	0.1
Other	4.6	3.6	2.1	2.8	2.8	2.8	2.8	2.7
Private	2.0	1.9	1.2	1.4	1.4	1.4	1.4	1.8
Public medium-and long-term loans (net)	2.5	1.7	0.9	1.4	1.4	1.4	1.5	0.9
Disbursements	3.8	3.2	2.5	2.9	2.9	2.9	2.9	2.9
Amortization	-1.3	-1.5	-1.6	-1.6	-1.5	-1.5	-1.4	-2.0
Reserve asset accumulation (-increase)	-1.2	2.4	2.6	-1.0	-1.6	-1.5	-1.3	-0.6
Errors and omissions	-0.3	-0.3	0.0	0.0	0.0	0.0	0.0	0.0
					(In percent of GDP)			
Current account	-4.3	-8.0	-7.4	-4.5	-3.7	-3.6	-3.6	-3.7
Trade balance	-16.6	-19.6	-19.7	-17.9	-17.1	-17.0	-16.8	-16.7
Services	5.6	5.4	5.6	5.7	5.7	5.6	5.4	5.3
Income	-1.4	-2.1	-2.1	-2.0	-1.8	-1.6	-1.5	-1.3
Transfers	8.0	8.2	8.8	9.6	9.5	9.4	9.2	9.0
Capital account	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	5.9	5.7	4.7	5.5	5.1	4.9	4.6	4.1
Direct investment	0.8	2.3	2.5	2.7	2.6	2.5	2.3	2.2
Portfolio investment	0.1	-0.2	0.1	0.1	0.1	0.0	0.0	0.0
Other	5.0	3.6	2.2	2.7	2.5	2.3	2.2	1.9
Memorandum items:								
Current account balance excluding official grants (percent of GDP)	-4.6	-8.4	-8.1	-5.9	-5.0	-4.8	-4.7	-4.7
Terms of trade (percentage change)	-9.0	0.8	-0.4	0.5	-0.3	-0.6	0.3	0.0
Gross official reserves 1/	23.6	20.6	17.9	18.8	20.3	21.6	22.8	23.3
In months of prospective imports of GNFS	5.7	4.9	4.0	3.9	4.0	4.0	4.0	3.9
Debt service (percent of export of GNFS and MRE) 2/	5.5	5.4	5.5	4.7	4.2	3.8	3.4	3.9
External public and publicly guaranteed debt (percent of GDP)	22.7	23.4	23.1	22.6	22.2	21.7	21.2	20.1
DHs per US\$, period average	8.4	8.1	8.6	...	...	...	...	...
GDP (\$)	90.8	99.3	98.2	104.8	112.7	121.1	130.7	142.1
Oil price (US\$/barrel; Brent)	79.6	111.0	106.5	95.8	91.6	90.2	88.2	87.6

Sources: Ministry of Economy and Finance; Office des Changes; and IMF staff estimates and projections.

Table 8. Morocco: Monetary Survey, 2010-13

	2010	2011	Projections	
			2012	2013
(In millions of dirhams)				
Net foreign assets	192,620	168,754	163,754	157,754
Monetary authorities	187,672	164,765	160,880	154,433
<i>Of which</i> : Gross reserves	197,328	177,051	155,865	164,357
Deposit money banks	4,949	3,988	2,873	3,320
Net domestic assets	711,925	795,356	860,131	935,755
Domestic credit	726,046	811,775	879,990	954,903
Net credit to the government	91,963	114,509	127,113	139,771
Banking system	91,963	114,509	127,113	139,771
Bank Al-Maghrib	3,524	2,216	2,030	1,740
<i>Of which</i> : deposits 1/	-3,962	-3,361	-3,547	-3,838
Deposit money banks	88,440	112,293	125,083	138,031
Credit to the economy	634,082	697,266	752,877	815,132
Other liabilities, net	14,121	16,419	19,859	19,147
Broad money	904,546	964,110	1,023,885	1,093,509
Money	552,403	590,637	634,011	671,015
Currency outside banks	144,660	158,127	166,900	180,548
Demand deposits	407,743	432,510	467,111	490,466
Quasi money	335,037	351,761	365,831	380,464
Foreign deposits	17,106	21,712	24,043	42,030
(Annual percentage change)				
Net foreign assets	0.0	-12.4	-3.0	-3.7
Net domestic assets	6.3	11.7	8.1	8.8
Domestic credit	6.8	11.8	8.4	8.5
Net credit to the government	2.9	24.5	11.0	10.0
Credit to the economy	7.4	10.0	8.0	8.3
Broad money	4.9	6.6	6.2	6.8
(Change in percent of broad money)				
Net foreign assets	0.0	-2.6	-0.5	-0.6
Domestic credit	5.4	9.5	7.1	7.3
Net credit to the government	0.3	2.5	1.3	1.2
Credit to the economy	5.1	7.0	5.8	6.1
Other assets net	-0.5	-0.3	-0.4	0.1
Memorandum items:				
Velocity (GDP/M3)	0.84	0.83	0.83	0.84
Velocity (non-agr. GDP/M3)	0.73	0.76	0.77	0.78
Credit to economy/GDP (in percent)	83.0	86.8	88.8	88.9
Credit to economy/non-agr GDP (in percent)	96.3	101.1	101.7	102.2

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

1/ Includes Fonds Hassan II.

Table 9. Morocco: Financial Soundness Indicators of the Banking Sector, 2005–11
(In percent, unless indicated otherwise)

	2005	2006	2007	2008	2009	2010	2011
Regulatory capital 1/							
Regulatory capital to risk-weighted assets 2/	11.5	12.3	10.6	11.2	11.8	12.3	11.7
Tier 1 capital to risk weighted assets	10.0	11.0	9.2	9.6	9.2	9.7	9.6
Capital to assets	7.7	7.4	6.9	6.9	7.2	8.3	8.1
Asset quality							
Sectoral distribution of loans to total loans							
Industry	21.9	19.9	19.6	15.9	15.8	16.4	16.8
Agriculture	5.4	4.8	4.8	6.9	6.0	6.1	5.8
Commerce	7.5	6.7	6.4	6.5	7.0	6.7	6.6
Construction	6.2	7.4	10.1	15.9	14.1	13.3	13.9
Tourism	2.9	2.3	2.5	2.6	3.2	2.9	2.8
Finance	10.2	11.4	14.0	13.1	12.4	12.1	11.3
Public administration	3.4	3.1	2.8	3.0	4.3	5.0	4.8
Transportation and communication	5.4	5.9	5.2	4.5	4.2	4.0	4.1
Households	26.0	28.6	28.4	26.5	27.6	28.1	27.6
Other	11.1	9.9	6.2	22.7	5.8	5.4	5.7
FX-loans to total loans	1.9	2.7	2.3	2.4	2.5	2.5	3.5
Credit to the private sector to total loans	92.7	93.1	94.0	93.3	91.0	91.0	92.0
Non Performing Loans (NPLs) to total loans	15.7	10.9	7.9	6.0	5.5	4.8	4.8
Specific provisions to NPLs	67.1	71.2	75.2	75.3	74.1	70.1	68.7
NPLs, net of provisions, to Tier 1 capital	57.2	30.3	20.1	13.9	12.7	12.2	12.9
Large exposures to Tier 1 capital	388	381	413	314	376	336	354
Loans to subsidiaries to total loans	...	6.5	7.0	6.4	6.7	6.1	6.0
Loans to shareholders to total loans	...	1.3	1.9	2.0	1.0	1.1	1.0
Specific provisions to total loans	10.5	7.8	5.9	4.5	4.0	3.4	3.5
General provisions to total loans	1.2	0.9	0.9	1.0	0.5	0.5	0.5
Profitability							
Return on assets (ROA)	0.5	1.3	1.5	1.2	1.2	1.2	1.1
Return on equity (ROE)	6.3	17.4	20.6	16.7	15.2	14.2	13.4
Interest rate average spread (b/w loans and deposits)	4.8	4.7	4.4	3.2	3.1	3.3	3.3
Interest return on credit	6.1	6.1	5.8	5.8	5.8	5.7	5.7
Cost of risk as a percent of credit	1.5	0.5	0.6	0.4	0.5	0.5	0.5
Net interest margin to net banking product (NPB) 3/	80.1	75.8	75.9	78.1	76.7	76.3	75.8
Operating expenses to NPB	50.0	48.4	46.5	47.8	47.5	46.4	47.9
Operating expenses to total assets	2.3	2.2	2.0	1.7	1.7	1.8	1.8
Personnel expenses to non-interest expenses	53.1	50.7	52.3	51.9	49.7	49.1	49.4
Trading and other non-interest income to NPB	19.6	23.9	24.1	21.9	23.3	23.7	24.2
Liquidity							
Liquid assets to total assets	29.0	27.0	23.6	24.4	17.3	12.0	11.4
Liquid assets to short-term liabilities	40.2	36.8	30.7	24.7	23.0	16.0	16.3
Deposits to loans	144.9	146.0	135.2	113.0	108.0	104.0	99.0
Deposits of state-owned enterprises to total deposits	3.7	4.6	3.9	5.1	4.8	5.2	4.8
Sensitivity to market risk							
FX net open position to Tier 1 Capital	18.1	8.0	9.4	7.6	15.6	12.1	12.1

Source: Bank Al-Maghrib.

1/ Financial Soundness Indicators (FSIs) are calculated according to guidelines of the IMF FSIs compilation guide, 2004.

2/ For 2007, the ratio is computed following Basel II standards. According to Basel I, it would have been 12 percent.

3/ Net Banking Product (NPB)=net interest margin-commissions paid+commissions received.

Table 10. Morocco: Public Sector Debt Sustainability Framework, 2007-17
(In percent of GDP, unless otherwise indicated)

	Actual					Projections					
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Baseline: Public sector debt 1/	54.6	48.2	48.0	51.3	54.3	56.9	57.8	58.1	57.5	56.3	54.3
Of which foreign-currency denominated	10.7	9.9	10.8	12.1	12.3	12.1	11.8	11.4	11.1	10.8	9.9
Change in public sector debt	-4.8	-6.4	-0.3	3.3	3.1	2.6	0.9	0.3	-0.6	-1.3	-2.0
Identified debt-creating flows (4+7+12)	-4.1	-4.3	0.6	3.6	4.0	5.1	2.1	1.5	0.6	-0.1	-0.5
Primary deficit	-3.0	-3.4	-0.6	2.1	4.7	3.8	2.9	2.2	1.4	0.8	0.5
Revenue and grants	29.9	32.5	29.3	27.5	27.6	28.3	28.1	27.5	27.3	26.7	26.6
Primary (noninterest) expenditure	26.9	29.2	28.7	29.6	32.3	32.0	30.9	29.7	28.6	27.5	27.1
Automatic debt dynamics 2/	-1.6	-2.6	-0.8	1.0	-0.2	-0.5	-1.9	-1.8	-1.9	-2.0	-2.1
Contribution from interest rate/growth differential 3/	-0.6	-3.1	-0.5	0.3	-0.2	-0.5	-1.9	-1.8	-1.9	-2.0	-2.1
Of which contribution from real interest rate	0.9	-0.4	1.8	2.0	2.2	1.0	1.0	1.0	1.0	1.0	1.0
Of which contribution from real GDP growth	-1.5	-2.7	-2.2	-1.7	-2.4	-1.5	-2.9	-2.7	-2.8	-3.0	-3.1
Other identified debt-creating flows	0.5	1.6	2.0	0.5	-0.4	1.8	1.1	1.1	1.1	1.1	1.1
Privatization receipts (negative)	-0.8	0.0	0.0	0.0	-0.7	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Recognition of implicit or contingent liabilities	1.3	1.3	1.4	1.4	1.5	1.5	1.5	1.5	1.5	1.5	1.4
Other (specify, e.g. bank recapitalization)	0.0	0.3	0.6	-0.9	-1.2	0.6	0.0	0.0	0.0	0.0	0.0
Residual, including asset changes (2-3) 5/	-0.7	-2.1	-0.9	-0.3	-1.0	-2.5	-1.2	-1.2	-1.2	-1.2	-1.4
Public sector debt-to-revenue ratio 1/	182.6	148.3	163.8	186.3	196.9	201.3	206.0	210.9	211.1	210.9	204.1
Gross financing need 6/ in billions of U.S. dollars	12.5 9.4	6.3 5.6	12.8 11.6	14.4 13.1	14.6 14.5	10.2 10.0	11.5 12.1	11.0 12.4	10.3 12.4	9.6 12.6	9.2 13.0
Scenario with key variables at their historical averages 7/					54.3	53.4	53.1	52.8	52.4	52.1	51.6
Scenario with no policy change (constant primary balance) in 2011-2016					54.3	57.0	59.7	62.5	65.1	67.4	69.2
Key Macroeconomic and Fiscal Assumptions Underlying Baseline											
Real GDP growth (in percent)	2.7	5.6	4.9	3.7	4.9	2.9	5.5	5.1	5.3	5.6	5.9
Average nominal interest rate on public debt (in percent) 8/	5.6	5.4	5.3	5.0	4.7	4.6	4.6	4.5	4.5	4.5	4.6
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	1.7	-0.4	3.9	4.4	4.4	2.0	2.1	2.0	2.0	2.0	2.0
Nominal appreciation (increase in US dollar value of local currency, in percent)	9.6	-4.8	3.0	-5.9	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	3.9	5.9	1.3	0.6	0.2	2.6	2.5	2.5	2.5	2.5	2.6
Growth of real primary spending (deflated by GDP deflator, in percent)	5.6	14.4	3.2	7.0	14.3	2.1	1.9	1.0	1.4	1.4	4.4
Primary deficit	-3.0	-3.4	-0.6	2.1	4.7	3.8	2.9	2.2	1.4	0.8	0.5

Sources: IMF country desk data; and IMF staff estimates.

1/ Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.

2/ Derived as $[(r - \pi(1+g) - g + \alpha(1+r))/(1+g+\pi+g\pi)]$ 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 denominator 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 $\alpha(1+r)$.

5/ For projections, this line includes exchange rate changes.

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

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

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

9/ 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 11. Morocco: External Debt Sustainability Framework, 2007-17
(In percent of GDP, unless otherwise indicated)

	2007	2008	Actual					Projections				
			2009	2010	2011	2012	2013	2014	2015	2016	2017	
Baseline: External debt	23.7	20.6	23.3	24.7	23.6	24.4	23.9	23.4	22.7	22.1	21.0	
Change in external debt	-0.2	-3.1	2.7	1.4	-1.1	0.8	-0.5	-0.6	-0.6	-0.6	-1.2	
Identified external debt-creating flows (4+8+9)	-5.8	-0.7	3.4	2.5	1.6	1.1	-2.4	-2.7	-2.5	-2.2	-1.8	
Current account deficit, excluding interest payments	-0.8	4.3	4.6	3.6	7.3	6.6	3.8	3.1	3.2	3.2	3.4	
Deficit in balance of goods and services	9.8	14.4	12.0	11.0	14.2	14.1	12.1	11.4	11.4	11.3	11.4	
Exports	36.2	37.6	28.9	33.2	35.7	37.8	39.7	39.5	39.0	38.2	37.2	
Imports	46.0	52.1	40.9	44.1	49.9	51.9	51.8	50.9	50.4	49.5	48.6	
Net non-debt creating capital inflows (negative)	-2.9	-2.3	-1.6	-1.9	-4.3	-5.6	-5.6	-5.3	-5.0	-4.6	-4.3	
Automatic debt dynamics 1/	-2.1	-2.8	0.4	0.8	-1.3	0.1	-0.6	-0.6	-0.7	-0.8	-0.9	
Contribution from nominal interest rate	0.9	0.9	0.9	0.8	0.8	0.8	0.7	0.6	0.5	0.4	0.3	
Contribution from real GDP growth	-0.6	-1.1	-1.0	-0.9	-1.1	-0.7	-1.3	-1.1	-1.1	-1.2	-1.2	
Contribution from price and exchange rate changes 2/	-2.5	-2.5	0.5	0.9	-1.0	...	...	...	...	...	...
Residual, incl. change in gross foreign assets (2-3) 3/	5.7	-2.4	-0.7	-1.1	-2.7	-0.4	1.9	2.1	1.8	1.6	0.7	
External debt-to-exports ratio (in percent)	65.4	54.7	80.5	74.4	66.1	64.6	60.3	59.2	58.3	58.0	56.3	
Gross external financing need (in billions of US dollars) 4/ in percent of GDP	2.2 2.9	6.5 7.3	6.2 6.8	5.3 5.8	9.6 9.6	8.9 9.1	6.4 6.1	5.8 5.1	6.0 5.0	6.2 4.8	7.3 5.2	
Scenario with key variables at their historical averages 5/						24.4	22.5	21.2	19.6	17.8	15.3	
Key Macroeconomic Assumptions Underlying Baseline												
Real GDP growth (in percent)	2.7	5.6	4.9	3.7	4.9	2.9	5.5	5.1	5.3	5.6	5.9	
GDP deflator in US dollars (change in percent)	11.6	11.9	-2.5	-3.7	4.3	-3.9	1.1	2.3	2.1	2.1	2.6	
Nominal external interest rate (in percent)	4.4	4.4	4.3	3.3	3.4	3.3	2.9	2.5	2.2	1.9	1.6	
Growth of exports (US dollar terms, in percent)	25.7	22.6	-21.4	14.7	17.7	4.6	12.1	7.0	6.3	5.5	6.1	
Growth of imports (US dollar terms, in percent)	32.5	33.7	-19.7	7.8	23.5	2.9	6.5	5.6	6.5	5.9	6.9	
Current account balance, excluding interest payments	0.8	-4.3	-4.6	-3.6	-7.3	-6.6	-3.8	-3.1	-3.2	-3.2	-3.4	
Net non-debt creating capital inflows	2.9	2.3	1.6	1.9	4.3	5.6	5.6	5.3	5.0	4.6	4.3	

Sources: IMF country desk data; and IMF staff estimates.

1/ Derived as $[r - g - \rho(1+g) + \alpha(1+r)] / (1+g+\rho+g\rho)$ 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, ϵ = nominal appreciation (increase in dollar value of domestic currency), and α = share of domestic-currency denominated debt in total external debt.

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

3/ For projection, line includes the impact of price and exchange rate changes.

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

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

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

Table 12. Morocco: Proposed Access

	Proposed Arrangement PLL	Proposed Arrangement (Percentile)	High-Access Cases 1/			
			20th	65th	80th Percentile	Median
Access						
In millions of SDRs	4,117	40	1,473	11,310	15,418	6,934
Average annual access (percent of quota) 2/	350	61	171	439	616	293
Total access in percent of: 3/						
Actual quota	700	59	307	801	1,053	584
Gross domestic product	6	54	4	8	10	6
Gross international reserves	35	27	27	63	91	49
Exports of goods and nonfactor services 4/	17	35	11	32	40	22
Imports of goods and nonfactor services	10	21	10	26	41	20
Total debt stock 5/						
<i>Of which:</i> Public	12	47	9	17	31	13
External	27	91	7	15	21	12
Short-term 6/	381	100	20	48	102	35
M2	5	15	8	17	26	13

Sources: Executive Board documents, MONA database, and IMF staff estimates.

1/ High access cases include available data at approval and on augmentation for all the requests to the Board since 1997 which involved the use of the exceptional circumstances clause or SRF resources. Exceptional access augmentations are counted as separate observations. For the purpose of measuring access as a ratio of different metrics, access includes augmentations and previously approved and drawn amounts.

2/ Correspond to quotas prior to 2008 Reform.

3/ The data used to calculate ratios are the actual values for the year prior to approval for public, external, and short-term debt, and the projection at the time of program approval for the year in which the program was approved for all other variables (projections for 2012 were used).

4/ Includes net private transfers.

5/ Refers to net debt.

6/ Refers to residual maturity.

Table 13. Morocco: External Financing Requirements
(millions of U.S. dollars unless specified otherwise)

	T		T+1		T+2	
	Baseline		Baseline	Adverse 1/	Baseline	Adverse 1/
Gross Financing Requirements	9513		8870	12817	6308	8518
Current account deficit	7986		7231	11177	4703	6912
Trade Deficits	19427		19335	21971	18718	20366
Transfers and other deficits	-11441		-12104	-10794	-14015	-13454
ST debt amortization (original maturity)	51		48	48	46	46
MLT debt amortization	1476		1592	1592	1560	1560
Financing sources	9513		8870	12817	6308	8518
FDI (net)	2272		2454	2246	2871	2635
Portfolio investment	-233		58	58	57	57
o/w Bond Issuance	0		0	0	0	0
ST debt disbursement	48		46	46	44	44
Change in gross reserves (- accumulation)	2373		2583	6737	-1022	1424
MLT debt disbursement	3345		3118	3118	3061	3061
Other 2/	1709		611	611	1297	1297
Overall Balance	0		0	0	0	0
Total size of shock in adverse scenario	...		...	3920	...	2416
Gross international reserves (GIR)	20642		17932	14012	18762	12552
Reserve adequacy metric	21013		21076	20712	22054	21836
GIR as % of reserve adequacy metric	98		85	68	85	57
Excess (+:buffer)/ shortfall (-financing) of GIR relative to 85% of reserve-adequacy metric 3/	2781		17	-3593	16	-6009
Financing gap in % of quota	N/A		N/A	395	N/A	661

Source: IMF staff estimates and projections.

1/ The adverse scenario assumes: (1) an oil price increase of at 10\$/bbl for the first year (T+1) and 8\$/bbl for the second year (T+2); (2) a decrease of growth in Europe of 4 pps for the first year and 2.5 pps for the second year.

2/ Includes capital account balance and net errors and omissions.

3/ The reserve adequacy metric is computed as 30% of short-term debt (at remaining maturity) + 15% of portfolio liabilities + 10% of broad money + 10% of exports.

Table 14. Morocco: Indicators of Fund Credit, 2012-17
(in millions of SDR)

	2012	2013	2014	2015	2016	2017
Existing Fund credit						
Stock 1/	0.0	0.0	0.0	0.0	0.0	0.0
Obligation	0.12	0.26	0.26	0.26	0.26	0.26
Disbursements						
Proposed PLL 2/						
Disbursements	2352.8	1764.6	0.0	0.0	0.0	0.0
Stock 1/	2352.8	4117.4	4117.4	3823.3	2426.3	661.7
Obligations	21.2	60.8	93.6	393.5	1484.0	1789.6
Principal (repayments/repurchases)	0.0	0.0	0.0	294.1	1397.0	1764.6
Charges and interest	18.3	40.3	46.5	46.5	38.3	18.8
GRA surcharges	2.9	20.5	47.1	52.9	48.7	6.3
Stock of existing and prospective Fund	2,352.8	4,117.4	4,117.4	3,823.3	2,426.3	661.7
in percent of quota	400	700	700	650	412.5	112.5
in percent of GDP 3/	3.6	6.3	5.9	5.1	3.0	0.8
Obligations to the Fund from existing and prospective Fund arrangements	21.3	61.0	93.9	393.8	1484.3	1789.9
in percent of quota	3.6	10.4	16.0	66.9	252.3	304.3
in percent of GDP 3/	0.03	0.09	0.13	0.53	1.85	2.06

Source: IMF Finance Department; and IMF staff estimates.

1/ End of period.

2/ Assumes a new PLL arrangement of 700 percent of quota (400 percent in the first year and 300 percent in the second) conditional upon Board approval.

3/ SDR/Dollar Exchange rate of 0.664016 as of July 17, 2012.

ATTACHMENT I. WRITTEN COMMUNICATION

Rabat, Morocco
July 27, 2012

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Ms. Lagarde,

1. We welcome the recent approval by the International Monetary Fund of the Precautionary and Liquidity Line (PLL) as a new financial instrument designed for countries with sound fundamentals and policies, but moderate vulnerabilities. This line can operate as insurance fulfilling immediate financing needs if external shocks or an unexpected deterioration of the international environment.
2. Morocco has sound economic fundamentals and a track record of sound policies. In a difficult external environment, Morocco's economic performance was broadly satisfactory. Growth averaged 4½ percent during 2009-11; inflation remained around 1 percent; and reserve coverage remained comfortable. Unemployment markedly declined from 13.6 percent in 2000, stabilizing at around 9 percent in 2011, even though youth unemployment remains high. The financial system is sound and remained resilient to the global financial crisis and more recently, to the financial turmoil in Europe. Morocco's investment grade sovereign debt rating has been reconfirmed, reflecting its strong economic performance in a difficult external environment
3. Even though Morocco does not currently have a balance of payments need, we continue to face risks arising from uncertainties in the global economy, particularly regarding the potential for adverse developments in Morocco's main trading partners and international oil prices. While we remain committed to following strong policies and to responding appropriately to any deterioration in the external environment, these risks could cause a widening of the trade deficit and a significant reduction in foreign reserves, and may undermine our growth and employment strategy.
4. In this context, a PLL arrangement would support our economic strategy by enhancing investor confidence and supporting macroeconomic stability, including by providing rapid access to resources in the event of external shocks or a worsening international situation which puts pressure on the balance of payments. We would like to request that the IMF approve a precautionary PLL arrangement covering 24 months in the amount of SDR 4.12 billion (700 percent of quota), with a maximum of 2.35 billion SDRs

(400 percent of quota) available during the first twelve months of the agreement. We intend to draw only in the event of unforeseen external shocks or a worsening of the international outlook relative to current assumptions.

5. In line with the government program adopted by Parliament in January 2012, and the macroeconomic stability principle enshrined in our constitution adopted July 1, 2011, the government pursues economic and financial policies to boost growth and reduce unemployment, while continuing to strengthen our fiscal and external sustainability. The objective of the Government's program is to increase the rate of real GDP growth to 5½ percent over the period 2012–16, based on three main drivers, namely supporting domestic demand, promoting private sector development, and the continued implementation of structural reforms and sectoral strategies. With regard to reducing unemployment, mainly among the young, the government will intensify its efforts to strengthen the adequacy of training needed for economic sectors and the ongoing active labor market programs.

6. In terms of fiscal policy, the government program envisages a steady reduction of the budget deficit to about 3 percent of GDP by 2016, by strengthening the rationalization and efficiency of public spending, as well as revenue optimization. As envisaged in the Government program, particular emphasis is given to the rationalization and efficiency of public spending. In this context, a draft decree which aims to modernize regulations governing public procurement is being adopted. At the same time, a project to redesign the organic budget law introducing program budgeting and a focus on a results-based framework is being developed. The reform of the subsidy system is also one of the priorities of the government to improve the system of protection of vulnerable populations by targeting these expenses, and to reduce expenses to preserve spending on public investment. In this context, we intend to hold before the end of the year a broad consultation with our economic partners and civil society to determine the best strategy to reform the subsidy system in order to improve social protection and reduce its cost to a sustainable level in line with our fiscal consolidation objectives. In addition, we intend to redesign compensation in the public sector to better link it with performance. This reform will be implemented in parallel with that of the pension system in order to ensure its long-term sustainability. Regarding the optimization of revenue, a global strategy encompassing tax revenues, revenues from government property and from monopolies is under consideration within the government. The objective is to broaden the tax base, improve collection, streamline tax and property expenditures, and raise the value of the private assets of the state, while maintaining a climate conducive to private sector activity. On this basis, the fiscal deficit (excluding privatization revenues, including grants) should be reduced from 6.9 percent of GDP in 2011 to 6.1 percent in 2012 and 5.3 percent in 2013.

7. In terms of monetary policy the statute governing Bank Al-Maghrib (BAM) enacted in 2006, establishes price stability as its fundamental mission, and gives adequate independence in defining and conducting monetary policy. The Board of BAM will continue to ensure price stability over the medium term, while following closely the changing internal and external environment, particularly any risks that may put pressure on prices. As part of the implementation of monetary policy, BAM will continue to provide the necessary liquidity to ensure appropriate financing of the economy. The effective management of liquidity has always allowed the money market rate to remain close to the policy rate on a daily basis. To

address structural liquidity needs, BAM has gradually reduced the reserve requirement ratio from 16 ½ to 6 percent. Banks now have a satisfactory level of reserves providing a safety margin in case of need. As for interest rate, the Central Bank will continue its efforts to strengthen capacity and instruments for effective regulation of the money market. Indeed, BAM now utilizes long-term repos in its interventions. In this context, it also expanded the collateral required for lending to banks. In addition, BAM will offer banks a broader range of refinancing instruments to adjust their balance sheets such as securitization and covered bonds. In this regards, it will continue to monitor the implementation of refinancing plans adopted by some banks, in order to ensure credit growth is supported by stable resources that are better suited for their use. It will also ensure that banks hold appropriate liquidity buffers on their balance sheets and adopt plans to deal with liquidity crises.

8. BAM will continue to monitor the health of the banking system through strong regulation and effective supervision. To this end, it will gradually adhere to the norms of Basel III, in particular those relating to capital adequacy and liquidity. BAM has already increased the Tier 1 capital to risk-weighted asset ratio to 9 percent and the regulatory capital adequacy ratio to 12 percent, which will take effect in June 2013. It will then carry out the reform of the liquidity ratio towards international standards. Starting from 2013, banks will be required to comply with stricter rules on risk diversification. Nonperforming loans (NPLs) of banks have fallen from 6 percent at the end of 2010 to 5.1 percent at the end of May 2012. BAM will maintain its requirements for adequate funding of such loans. In addition, BAM will strengthen its micro-prudential surveillance in the context of the risk-based approach. In parallel, the Ministry of Finance, BAM and other regulators are strengthening their coordination in order to preserve financial stability.

9. We will maintain a fixed exchange rate relative to a euro-dollar basket for the time being, which has contributed to economic stability in the last decade. We will continue to maintain an adequate level of international reserves. In particular, gross international reserves are expected to stabilize in the second half of 2012 at about four months of imports, mainly due to lower international oil prices, combined with an increase in export volumes of phosphates and derivatives, the export production of new industrial plants, and a pick-up in tourism receipts. Moreover, the government's financing strategy comprises the possibility of accessing international financial markets.

10. In summary, our sound economic fundamentals and institutional policy framework, and our track record of sound policies recognized by the positive assessment of the Executive Board of the IMF in the context of our most recent Article IV consultations, as well as our commitment to such policies in the future, provide sufficient assurance that we will respond appropriately to deal with any potential problem of financing of the balance of payments.

11. We will provide the Fund all needed information to monitor economic and policy developments under the requested PLL arrangement, including in relation to the indicators listed in Attachment II and Table 1. We will also observe the standard criteria related to trade and exchange restrictions, bilateral payments arrangements, multiple currency practices, and non-accumulation of external debt payments arrears, in accordance with requirements under the PLL.

12. We believe that the policies contained in this communication are adequate to achieve our economic goals supported by the PLL, and will take any additional measures that may be necessary for this purpose. Morocco will engage with the Fund in accordance with relevant Fund policies, towards the success of our economic policies.

/s/
Nizar Baraka
Minister of Economy and Finance

/s/
Abdellatif Jouahri
Governor of Bank Al-Maghrib

Table 1. Morocco: Quantitative Indicative Targets

	2011 12/31 Actual	2012 10/30	2013 4/30
Indicative targets 1/			
Net international reserves (NIR) of Bank Al-Maghrib (BAM) (floor, end of period (eop) stock, in millions of U.S. dollars (US\$))	20,268	16,752	16,557
Fiscal deficit (ceiling, cumulative since beginning of fiscal year, eop in millions of dirham)	-55,776	-41,601	-18,556
Memorandum item:			
Adjustor on NIR (in millions of U.S. dollars) 2/		1,095	928
Adjustor on the fiscal deficit (in millions of dirham) 3/		0	3,248

1/ Evaluated at the program exchange rate (end-April 2012 8.429 MAD/US\$) for the years 2012 and 2013.

2/ The adjustors are specified in the Technical Appendix. Accordingly, the floor on NIR of BAM will be adjusted downward in the event of a shortfall of official grants and budget support loans relative to projections.

3/ The adjustors are specified in the Technical Appendix. Accordingly, the fiscal deficit ceiling will be adjusted upward in the event of a shortfall of budget support grants relative to projections.

Table 2. Morocco: Schedule and Terms Under the Precautionary and Liquidity Line Arrangement

Review Date	Conditions for access	Indicative targets 1/		Credit Available 4/			
		Central government fiscal deficit, ceiling, cumulative since beginning of fiscal year (eop in millions of dirham) 2/	Net international reserves (NIR) of Bank Al-Maghrib (BAM), floor, eop stock, in millions of U.S. dollars (US\$) 3/	Million SDR 5/	Million Dollars 6/	Percent of Quota, cumulative	Percent of Total Access
August 3, 2012 7/	Board approval of the PLL	-55,776	20,268	2,352.8	3,543.3	400	57
February 2, 2013	First review, based on October 30, 2012 indicative targets	-41,601	16,752	2,352.8	3,543.3	400	57
August 2, 2013	Second review, based on April 30, 2013 indicative targets	-18,556	16,557	4,117.4	6,200.8	700	100
February 2, 2014	Third review, based on October 30, 2013 indicative targets	To be set in the second review	To be set in the second review	4,117.4	6,200.8	700	100
Total				4,117.4	6,200.8	700	100

Source: Fund Staff estimates.

1/ Evaluated at the program exchange rate (end-April 2012 8.429 MAD/US\$) for the years 2012 and 2013.

2/ The adjustors are specified in the Technical Appendix.

3/ The adjustors are specified in the Technical Appendix.

4/ Credit available assuming no purchase.

5/ Additional access equivalent to 300 percent of quota will be available on August 3, 2013.

6/ SDR/Dollar Exchange rate of 0.664016 as of July 17, 2012.

7/ Corresponds to the date of approval of the PLL arrangement.

ATTACHMENT II. TECHNICAL APPENDIX

1. Under the first year of the PLL arrangement, quantitative indicative targets as defined in Table 1 of our written communication will be set for end-October 2012 and end-April 2013. They include:

- Floor on the level of net international reserves (NIR) of Bank Al-Maghrib (BAM), as defined in Table 1, calculated as an end-of-period stock. The exchange rate that will be used to monitor NIR during the first year of the program is Moroccan dirham (MAD) 8.4291 per U.S. dollar, the rate prevailing on April 30, 2012. Foreign currency accounts denominated in currencies other than the U.S. dollar and monetary gold will be valued in U.S. dollars at the exchange rates and gold prices prevailing on April 30, 2012. BAM will report to the IMF the level of NIR and gross international reserves (GIR) no later than one week after the end of each week both at the program exchange rates and at the market exchange rates.
- Ceiling on the level of the fiscal deficit of the central government defined as revenues, including grants, less expenditure less net acquisition of nonfinancial assets as reported in the GFSM 2001 format, calculated as a cumulative flow from January 1 of each year. The central government is defined as all budgetary units of the central government. It includes the general government budget, special-treasury accounts and autonomously managed government services. The Ministry of Economy and Finance will report to the IMF in monthly and cumulative flows from January 1 of each year the fiscal deficit, including grants, but excluding net acquisition of shares and other equity (privatization receipts) and the relevant budget aggregates (revenues, expenditures, etc.) for each month before the end of the following month.

2. The indicative targets on NIR will be adjusted downward (upward) by the amount below (above) official grants and loans received by the central government from bilateral and multilateral agencies relative to program projections, and the ones on the fiscal deficit will be adjusted upward (downward) by the amount below (above) budgetary grants received by the central government from bilateral and multilateral agencies relative to program projections as indicated in Table 1 of our written communication.

3. Regarding the continuous zero ceiling on the accumulation of new external payment arrears during the duration of the arrangement, the payment arrears are defined as external debt-service obligations (principal and interest) that have not been paid at the time that are due as specified in the contractual agreements, on central government and central government-guaranteed debt. Overdue debt and debt-service obligations that are in dispute will not be considered as external payment arrears.

4. The reviews by the Executive Board will be completed by no later than February 2, 2013 for the first review, August 2, 2013 for the second review, and February 2, 2014 for the third review.

Table 1. Definition of GIR and NIR of BAM
for the purpose of monitoring indicative targets

Gross international reserves are defined as the sum of:

- Foreign currency assets in convertible currencies held abroad, and as vault cash that are under the direct and effective control of BAM, readily available for intervention in the foreign exchange market or the direct financing of the balance of payments;
- The reserve position of Morocco in the IMF;
- Holding of SDRs; and
- Monetary gold.

Excluded from the definition of GIR are:

- Foreign currency assets that are in any way encumbered or pledged, including, but not limited to, reserve assets used as collateral or guarantee for third-party external liabilities;
- Foreign currency assets in nonconvertible currencies and precious metals other than gold;
- Foreign currency claims on entities incorporated in Morocco;
- Any other foreign currency claims on residents; and
- Capital subscriptions in international institutions.

NIR is defined as GIR less:

- All outstanding liabilities of Morocco to the IMF, excluding SDR allocation; and
 - Foreign currency liabilities in convertible currencies to nonresidents and contingent commitments to sell foreign exchange arising from transactions in derivative assets, including forward contracts, foreign currency swaps, and other futures market contracts.
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Press Release No. 12/287
FOR IMMEDIATE RELEASE
August 3, 2012

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US\$6.2 Billion Arrangement for Morocco under the Precautionary Liquidity Line

The Executive Board of the International Monetary Fund (IMF) today approved a 24-month arrangement for Morocco under the [Precautionary Liquidity Line](#) (PLL) in an amount equivalent to SDR 4,117.4 million (about US\$6.21 billion, 700 percent of quota). The access under the arrangement in the first year will be equivalent to SDR 2,352.8 million (about US\$ 3.55 billion, 400 percent of quota), rising in the second year to cumulatively US\$ 6.21 billion.

The PLL will allow the authorities to continue with their home-grown reform agenda aimed at achieving rapid and inclusive economic growth, while providing them with a useful insurance against external shocks. The Moroccan authorities have stated that they intend to treat the arrangement as precautionary and do not intend to draw on the line, unless Morocco experiences actual balance of payments needs from a deterioration of external conditions.

The PLL was introduced in 2011 to meet more flexibly the liquidity needs of member countries with sound economic fundamentals and strong record of policy implementation but with some remaining vulnerabilities.

Following the Executive Board discussion on Morocco, **Christine Lagarde, IMF Managing Director** and Chair of the Board, made the following statement:

“Morocco’s track record of strong economic policies and wide-ranging structural reforms has contributed to solid macroeconomic performance, notably robust growth, low inflation, and a resilient banking system. These positive developments, together with strong economic fundamentals and institutional frameworks, have helped Morocco cushion the impact of the global crisis and respond to pressing social needs.

“High oil prices have contributed to a build-up of fiscal and external pressures. The authorities have already taken action to address these vulnerabilities, and are committed to maintaining sound policies. The recent increase in domestic administered oil prices is a tangible signal of the authorities’ resolve to reform the subsidy system and to ensure fiscal

sustainability more broadly. The authorities' economic program aims to improve social indicators, reduce unemployment, boost competitiveness, and increase the potential for higher and more inclusive growth. The authorities will continue to monitor the health of the financial system to preserve its soundness, and to maintain an adequate level of international reserves.

“Notwithstanding these comprehensive policy measures and favorable macroeconomic prospects, Morocco faces external risks linked to uncertainties in the euro zone and potential oil price increases. A two-year arrangement under the Precautionary and Liquidity Line will provide Morocco with a useful insurance policy for meeting immediate financing needs if these risks materialize, strengthening market confidence and facilitating better access to private capital markets. The authorities intend to treat the arrangement as precautionary.”

Statement by Mohammed Dairi, Alternate Executive Director for Morocco
August 3, 2012

Introduction

On behalf of my Moroccan authorities, I would like to thank staff for the hard work and constructive dialogue during the PLL discussions, as well as the quality of their analysis and assessment, which my authorities broadly share. I also thank management for their efforts toward successful conclusion of these discussions. Morocco's request for a PLL arrangement is the first such a request following the November 2011 reform of the Fund's toolkit, which established this facility to help members with sound policies protect their economies against exogenous shocks under current circumstances of high uncertainties and interconnectedness. The Board's approval of the authorities' request—for which they would be also grateful—would be a further demonstration of the IMF's commitment, as announced by the Managing Director, to support the historic transformation process of the Arab Spring countries, which are determined to meet the legitimate aspirations of their people to dignity, social justice, equal opportunities, and employment.

Political and economic developments in 2011

To maintain social stability and move the reform process decisively forward, the authorities announced a vast program of political transformation, as early as March 2011, and developed an ambitious plan to support employment and incomes, which helped maintain confidence. The political reform agenda included a new constitution approved in July 2011, which consecrated human and political rights, and principles of social justice, equal opportunities and good governance. Free and fair elections followed, leading to a new coalition government headed by the party with the largest number of seats, as required under the new constitution.

Supportive budgetary and monetary policies helped mitigate the impact of the high oil prices and weak international environment, including from the euro area crisis, as well as the effects of the severe drought. As a result of its strong political and economic fundamentals, and the authorities' judicious mix of supportive policies while preserving macroeconomic stability, in accordance with the principle enshrined by the new constitution, Morocco has demonstrated strong resilience to social unrest and the unfavorable external environment. As staff indicates, economic performance in 2011 was satisfactory, with the highest growth rate and the lowest inflation in the region, unemployment stabilizing at around 9 percent, and reserves remaining at a comfortable level.

Government economic program

The Government's program presented to Parliament in January 2012 aims at increasing the growth rate over the medium term by 1 percentage point to reach 5.5 percent, maintaining inflation at 2 percent, and reducing unemployment to 8 percent. To achieve these objectives, the main reforms include: improvement in the business climate and in competitiveness by strengthening governance and the rule of law, reforming the judiciary, enhancing transparency and accountability, fighting corruption and rent-seeking behavior, strengthening infrastructure,

including through public-private partnerships, improving education and health, and modernizing administration to enhance productivity and service delivery, and facilitate personnel redeployment under the Advanced Regionalization.. The Government will also develop active labor market policies, and promote SMEs and reduce informality. Sectoral policies will target high value-added and high job-content sectors, where Morocco has already made significant inroads, and revitalize other key sectors through performance contracts. The program also aims at reducing inequalities in incomes and opportunities, both broadly and across regions and genders, and strengthening social service delivery and social protection.

Fiscal deficit under the Government's program should be reduced to 3 percent of GDP by 2016. This involves, on the revenue side, a tax reform to broaden the base, lower the rates, while enhancing equity and reducing exemptions, as well as measures to improve revenue from government property and public property use. On the expenditure side, in addition to the planned subsidy reform (see below), reforms will focus on: modernizing the budget legal framework and enhancing spending efficiency, including through strengthening the procurement law to ensure greater competition and reduce costs, and reform of investment incentives. The program also includes a review of the public sector compensation system to link it to productivity, which will be conducted in coordination with a reform of the pension system to ensure its long-term sustainability and reduce risks to the budget. Improvement in governance and monitoring of performance of public enterprises should strengthen their investment capacity and help prepare the non-strategic ones for privatization. To further improve data quality and credibility and better inform decisions, independence of the government unit in charge of statistics will be enhanced by transforming it into an autonomous agency.

Fiscal policy in 2012

The worsening of the euro area crisis and the drought have impacted growth and fiscal performance in 2012, with GDP growth now projected at around 3 percent, as against an earlier projection of some 4 percent. Together with continued increase in oil prices in the first months of the year, this has had a significant impact on the budget. While maintaining support to the economy, including through higher appropriations for infrastructure spending, the government took a number of measures to reduce the deficit. As indicated in the report, these include new tax measures, improvement in tax and nontax revenue collection, reduction in nonessential recurrent spending, in subsidies (see below), and in transfers to public enterprises, without hindering their investment program. Along with the impact of delayed approval of the budget, these measures should reduce the deficit by 2 percent of GDP, compared to what it would have been otherwise.

Subsidy policy

The authorities agree that the current untargeted subsidy system is costly and inefficient. The increase in international petroleum prices has been particularly challenging for a country that is almost entirely dependent on imports for its energy needs. Moreover, Morocco's domestic petroleum prices are relatively high, by regional standards, including as a result of VAT and excises amounting to some 2.5 percent of GDP (half of subsidy costs). The authorities did not want to take the easy way of reducing subsidies by lowering energy taxation. In 2011 and early 2012, the economy was hit by a new spike in international energy prices which accounted for the bulk of the increase in the current account and the fiscal deficits. The pass through of the sharp increases in world prices was not politically feasible during a period of heightened social demands, and ongoing political transformation and change of government, in the context of a

drought-related decline in agricultural production, and in the absence of a well-targeted social safety net. As a result, subsidy costs and the fiscal deficit increased by 2.5 percent of GDP in 2011 and were expected to increase further in 2012.

On June 1, the Government raised the prices of several petroleum products, at a time when world prices were declining, which will reduce the cost of subsidies by 0.65 percent of GDP (1 percent on an annual basis). Other measures will follow, including partial indexation of industrial fuel and reductions in subsidies for other large users. Moreover, a Social Cohesion Fund was created which will raise new taxes to help finance the subsidy reform. The authorities are committed to gradually reducing the subsidy bill, consistent with their medium-term fiscal consolidation objectives, including through the introduction of a well-targeted cash transfer system, in line with best international experiences. Preparations for the introduction of this system, in close consultation with the World Bank, are underway, with pilot projects expected to be rolled out in due course. The Government intends to consult with its economic partners and civil society by end-2012 to discuss options for effective targeting.

While the subsidy reform should promote efficient energy use, Morocco has embarked on large-scale projects in renewable energy, including a major solar program, which will help reduce energy dependency, protect the environment, and improve the external position. The Government also intends to establish a hedging system against oil price volatility, as indicated in the report.

Monetary and exchange rate policy and the financial sector

The central bank has succeeded in maintaining inflation well below its medium-term target while meeting banks' liquidity needs. Improved governance and transparency of monetary policy have enhanced its credibility. Efforts are being made to strengthen the monetary policy framework, as indicated in the written communication. The authorities agree that the current peg to a euro/\$ basket has helped price stability, and that the dirham is broadly in line with fundamentals. They continue to consider a gradual move to flexible exchange rate policy, along with implementation of inflation targeting and further liberalization of capital flows, once all the prerequisites are in place and the external environment is more stable. The financial system is sound and has demonstrated resilience to the global slowdown and the euro area crisis. Banks were able to meet the economy's needs while preserving credit quality. The written communication describes the measures undertaken by the central bank to strengthen regulation and supervision, including implementation of Basel III.

PLL and foreign reserves

Morocco's eligibility to the PLL is well established, as indicated in the report, including as a result of its strong fundamentals and the authorities' track record of sound policy implementation, and their commitment to preserving macroeconomic and financial stability, enhancing growth and employment performance, and rebuilding fiscal and reserves buffers to absorb shocks. They have also demonstrated their resolve in starting to address the subsidy issue, the main area of fiscal and external vulnerability, despite the high political sensitivity. The 2-year duration of the requested facility, and the 700 percent of quota access level, of which 400 percent for the first year, are appropriate, in view of the risks from heightened euro area crisis and Morocco's strong linkages with the area, and from a sharp increase in oil prices stemming from intensified geopolitical tensions.

As indicated in the report, the increase in oil prices was the main factor behind the deterioration in the fiscal and external deficits in 2011, even though exports, tourism, worker remittances, and FDI performed well. During the first half of 2012, the current account balance weakened, compared to the first half of 2011, largely as a result of worsening euro area crisis and higher oil prices, while FDI remained broadly unchanged. However, disbursements on public debt were much lower than usual, partly reflecting delays in investment budget execution and, as a consequence, and in view of the higher current account deficit, reserves declined significantly, while remaining at a comfortable level. With lower oil prices foreseen for the second half of the year, the usual seasonal recovery in tourism and remittances, the impact of the fiscal measures undertaken by the authorities, and higher drawings on public debt and grants, reserves are expected to stabilize by end-year 2012 at their current level.

The authorities intend to treat the PLL arrangement as precautionary and draw on the facility only in the event of an exogenous shock. They are also considering access to international markets, which should be at favorable terms in view of Morocco's reconfirmed sovereign investment grade rating and the confidence effect of the PLL. Durable improvement in the euro area situation and a strengthening in the global economy should increase the chances of early exit.

Conclusion

As indicated in the written communication, the authorities are firmly committed to their reform agenda to achieve their objectives of high and more inclusive growth, and greater job creation, while preserving macroeconomic and financial stability. They are grateful to their international partners for their support. They will remain closely engaged with the Fund for successful implementation of their policies.