MOROCCO

Highlights

- **Growth decelerated at the beginning of 2016 after a strong rebound in 2015**, as agricultural output faltered (due to a winter drought) while non-agricultural growth remained weak. Unemployment marginally improved, averaging 9.3 per cent in 2016.
- **The fiscal deficit narrowed further thanks to continued fiscal consolidation.** This was mainly driven by the authorities' efforts to reduce energy subsidies (supported by lower oil prices) and progressive containment of the public wage bill. Fuel prices were fully liberalised in December 2015.
- **The process of decentralisation regained momentum.** In September 2015, Morocco held free regional and municipal elections, a notable step in implementing its regionalisation strategy, which aims to decentralise decision-making and empower local authorities. Fiscal decentralisation has been initiated, with a progressive delegation of spending and increased allocation of central government tax revenue to local authorities.

Key priorities for 2017

- **Pension reforms should be swiftly implemented.** The financial situation of the pension system, especially civil pensions, is fragile. The long-awaited pension reform bill adopted by parliament in July 2016, which includes an increase in the retirement age and contribution requirements, should be urgently implemented.
- **Measures are needed to address persistent regional disparities.** This includes improving access in rural areas to basic infrastructure services, transport, education and health facilities, as well as measures to enhance the productivity and resilience of the agricultural sector, the modernisation of agriculture practices, irrigation and the development of the agro-industry.
- **Removing constraints to access to finance for small and medium-sized enterprises (SMEs) should remain high on the policy agenda.** To ease access to credit for SMEs, which are typically under-collateralised, a number of financial infrastructure areas must be improved relating to the regulatory framework and the breadth of credit information, such as allowing a more flexible use of movable assets as collateral and setting up a movable asset collateral registry.

Main macroeconomic indicators %

	2012	2013	2014	2015	2016 proj.
GDP growth	3.0	4.5	2.6	4.5	1.5
Inflation (average)	1.3	1.9	0.4	1.6	1.5
Government balance/GDP	-7.3	-5.2	-4.9	-4.4	-3.5
Current account balance/GDP	-9.3	-7.6	-5.7	-1.9	-1.2
Net FDI/GDP [neg. sign = inflows]	-2.4	-2.8	-2.8	-2.5	-2.5
External debt/GDP	33.8	36.2	43.1	44.2	n.a.
Gross reserves/GDP	17.3	17.3	20.1	23.2	n.a.
Credit to private sector/GDP	71.6	67.9	68.4	64.5	n.a.

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Macroeconomic performance

Growth decelerated at the beginning of 2016 after a 4.5 per cent rebound in 2015 as agricultural output faltered. GDP growth in 2015 reached 4.5 per cent, driven primarily by a strong agricultural sector rebound of 12.8 per cent, while non-agricultural growth was modest at 1.9 per cent. Growth slowed down, however, to 1.7 per cent year-on-year in the first quarter of 2016, after a decline in agricultural output of 9.0 per cent due to a severe drought in the winter, while non-agricultural growth remained weak at 2.5 per cent, reflecting muted tourism sector growth (1.2 per cent year-on-year) and more modest growth in manufacturing (2.9 per cent year-on-year compared with 5.0 per cent in the first quarter of 2015). Unemployment averaged 9.7 per cent in 2015 against 9.9 per cent in 2014. On a quarterly basis, the average unemployment rate over the two first quarters of 2016 remained stable at 9.3 per cent compared with the same period a year earlier. Youth unemployment, however, remains high at about 21.5 per cent.

The fiscal deficit narrowed further thanks to continued fiscal consolidation. The central government deficit declined further to 4.4 per cent of GDP in 2015, down from 4.9 per cent in 2014, and the trend continued at the beginning of 2016. This was mainly driven by the authorities' efforts to reduce energy subsidies (supported by lower oil prices) and contain the public wages bill. Fuel subsidies were fully liberalised in 2015, resulting in a significant decrease in subsidies and transfers of 44 per cent over 2015 and providing more fiscal space for investment spending, which saw an increase of 8.0 per cent over the same year. The increase in public wages and salaries decelerated and was contained to 1.2 per cent over 2015 compared with 2.5 per cent in 2014. In July 2016 Morocco secured another two-year Precautionary and Liquidity Line (PLL) with the International Monetary Fund (IMF), totalling US$ 3.47 billion, after two successive 24-month PLL arrangements.

The external position has further improved. The current account deficit narrowed from 5.7 per cent of GDP in 2014 to 1.9 per cent of GDP in 2015, due to lower oil prices and a stronger exports performance (8.6 per cent increase over 2015), in addition to the tourism receipts increase of 3.1 per cent. A bright spot is Morocco's successful industrial strategy of developing high value-added exports in sectors such as automotives and aeronautics. These are now Morocco's main exports, surpassing more traditional exports such as phosphates. Foreign direct investment (FDI) receipts increased in 2015 by 9.2 per cent compared with 2014. Morocco was among the top five host African economies for FDI in the same year. Gross international reserves stood at US$ 26.4 billion at the end of September 2016, or over 7 months worth of imports, an 18 per cent increase year-on-year. Morocco is gradually moving to greater exchange rate flexibility and an inflation-targeting regime, which would ease external pressures, improve competitiveness and, assuming it is accompanied by greater financial liberalisation, boost Casablanca's standing as a regional finance hub.

Growth is expected to decelerate in 2016 to 1.5 per cent, as a result of several factors, including the aforementioned drought, sluggish growth in Europe – Morocco's main trade partner – and continued modest non-agricultural growth. Worse-than-expected growth in Europe and domestic and regional security problems represent the main downside risks to this forecast.

Major structural reform developments

Despite notable improvements in the business climate due to a number of regulatory reforms, key constraints to the private sector remain. The business regulatory environment in Morocco has improved significantly over recent years due to a number of regulatory reforms that eased the process of starting a business, dealing with construction permits, paying taxes and trading across borders. However, as highlighted by the World Bank's *Doing Business 2017* report, constrained access to credit and weak investor protection (for which the country is ranked 101st and 87th, respectively, out of 190) remain major impediments to the private sector, and SMEs in particular. In addition, the latest EBRD/World Bank MENA Enterprise Survey (MENA ES) shows that competition from the informal sector, corruption and lack of workforce skills are the top three business environment obstacles faced by firms. This is in line with the World Economic Forum's Global Competitiveness Index, which reveals a weak educational system and training (ranked 104th out of 138 countries) and an inefficient labour market (ranked 124th).

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A number of measures have been taken to improve the investment climate and address obstacles to private sector development. A new Law No. 86-12 on public-private partnerships was approved in December 2014, and became effective after a decree was adopted in May 2015 defining its implementation conditions and modalities. It should reinforce the participation of the private sector in infrastructure development projects and concurrently limit risks to the budget. A Competition Council Law and its implementation decrees were adopted in 2015, providing the Competition Council with significant powers to investigate and impose sanctions for anti-competitive behaviour. To address the public sector's long payment delays, which particularly affect SMEs, a decree was adopted in July 2016 which restricts these delays to a maximum of 60 days and imposes penalties for non-compliance. This should assist SMEs in alleviating their cash flow problems, although the law will only be enforced a year after being passed. The government launched a national strategy for the fight against corruption in 2015 after a new law was adopted in June 2015 establishing an independent agency in charge of government policies to combat corruption. In the context of the 2014-2020 industrial strategy, the government has also announced plans to reform the investment code with a focus on strengthening export promotion agencies and including new incentives.

Morocco has made further progress in reducing fiscal vulnerabilities. Subsidies on all liquid petroleum products were removed as of January 2015, and prices fully liberalised in December 2015, while measures were taken to strengthen the social safety net. The phasing out of fuel subsidies will provide significantly more fiscal space for the government to support much-needed public investment in infrastructure, health and education. Most of the provisions of the new Organic Budget Law (OBL) – which was adopted in May 2015 with the aim to enhance the efficiency of the fiscal framework – became effective in January 2016; specifically, those related to transparency of public finances, fiscal performance management and the involvement of parliament. Other provisions are to enter into force gradually by 2020. However, the financial situation of the pension system, especially civil pension, remains fragile. A major development is the parliamentary adoption of the long-awaited pension reform bill in July 2016, despite resistance from trade unions. Changes to the state pension rules include raising the retirement age (from 60 to 63 by 2022) and boosting workers' and state contribution requirements.

The process of decentralisation regained momentum. In September 2015, Morocco held free regional and municipal elections, a notable step in implementing its regionalisation strategy, which aims to decentralise decision-making and empower local authorities. Fiscal decentralisation has been initiated. Together with increased delegation of spending, local government resources will continue to be improved via increased allocation of central government tax revenue as well as the increase of the local authorities' own resources. Local spending responsibilities are being progressively widened to cover a number of dimensions such as education, health, housing, transport and economic development.

Progress continues in strengthening financial supervision and regulation. After a new Banking Law was adopted in November 2014, the central bank (Bank Al-Maghrib or BAM) developed over 2015 the regulations defining the implementation procedures of the Law. In the area of macro-prudential regulation, the central bank developed macro-prudential instruments recommended by the Basel Committee to regulate potentially systemic risks. Supervision of Moroccan banks with operations in sub-Saharan Africa is being strengthened through enhanced cooperation and information exchange between BAM and host countries' supervisory authorities. However, a draft of the new central bank law – aiming to increase BAM's independence, clarify its objectives and expand its supervisory and resolution role – is still pending approval, and is expected to be submitted to parliament by the end of 2016.

EU-Morocco's 2012 agricultural trade agreement was partially annulled by the EU General Court. EU-Morocco's agreement concerning reciprocal trade liberalisation measures on agricultural products, processed agricultural products, fish and fishery products was partially annulled in December 2015 by the General Court over certain aspects of the agreement and in particular in relation to the disputed Western Sahara region. The European Council lodged an appeal against the ruling in March 2016. These developments have potential implications for the Deep and Comprehensive Free Trade Agreement (DCFTA) negotiations with Morocco that were launched in March 2013.