

EBS/84/129

CONFIDENTIAL

June 6, 1984

To: Members of the Executive Board
From: The Secretary
Subject: Morocco - Staff Report for Review Under Stand-By Arrangement

Attached for consideration by the Executive Directors is the staff report for a review under the stand-by arrangement for Morocco. A draft decision appears on pages 16 and 17.

This subject will be brought to the agenda for discussion on a date to be announced.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Bhatia (ext. 73253), Mr. Fassassi (ext. (5)8392), or Mr. Sacerdoti (ext. (5)8514).

Att: (1)

INTERNATIONAL MONETARY FUND

MOROCCO

Staff Report for Review Under Stand-By Arrangement

Prepared by the African Department and the
Exchange and Trade Relations Department

(In consultation with Fiscal Affairs, Legal,
and Treasurer's Departments)

Approved by J.B. Zulu and S. Kanesa-Thanan

June 5, 1984

I. Introduction

On September 16, 1983 the Executive Board approved an 18-month stand-by arrangement with Morocco (EBS/83/178) for an amount equivalent to SDR 300 million (98 percent of quota). ^{1/} The first review under the arrangement was completed by the Executive Board on April 9, 1984 (EBS/84/71). To date Morocco has purchased three installments totaling SDR 170 million under the arrangement (Table 1); pursuant to the completion of the first review and on the satisfaction of the performance criteria for end-April, the third purchase of SDR 40 million was made by Morocco on May 31, 1984. The next purchase of SDR 40 million will become available on July 31 subject to the completion of the present second review of the program and the satisfaction of the performance criteria for end-June 1984. A third review, to be completed before November 30, 1984, constitutes one of the performance criteria governing the last two installments under the arrangement. During that review the Government will reach understandings with the Fund on the fiscal policy to be reflected in the 1985 Budget Law. If all the purchases are made under the arrangement, use of Fund credit by Morocco at the end of the stand-by arrangement would amount to SDR 1,090.6 million (or 355.7 percent of quota); excluding the CFF purchases, total Fund credit outstanding would amount to 278.6 percent of quota.

The present review comprehends the reaching of understandings on quantitative performance criteria for the second semester of 1984, and covers the progress made by Morocco toward the implementation of the fiscal reform, the program set up by Morocco with respect to the overhang of capital expenditure allocations, the liberalization of the pricing in the oil sector and of import and exchange restrictions, and the policies pertaining to agricultural producer prices. Discussions

^{1/} Summaries of Morocco's relations with the Fund and the World Bank Group are contained in the attached Appendices I and II.

Table 1. Morocco: Fund Position During Period of Arrangement

	Outstanding at	1984							1985
	beginning of arrangement 1/ Aug. 31, 1983	1983 Sept.- Dec.	January- March	April	May- June	July- Sept.	Oct.- Dec.	Jan.- March	
(In millions of SDRs)									
Transactions under tranche policies (net) 7/	--	30.00	--	100.00	23.78	29.24	29.51	29.24	
Purchases	--	30.00	--	100.00 2/	40.00 3/	40.00 4/	50.00 5/	40.00 6/	
Ordinary resources	--	(13.64)	(--)	(40.03)	(--)	(--)	(--)	(--)	
Enlarged access resources	--	(16.36)	(--)	(59.97)	(40.03)	(40.00)	(50.00)	(40.00)	
Repurchases	--	--	--	--	-16.22)	-10.76	-20.49	-10.76	
Ordinary resources	--	(--)	(--)	(--)	(-7.03)	(-7.03)	(-7.03)	(-7.03)	
Supplementary financing	(--)	(--)	(--)	(--)	(-9.19)	(-3.73)	(-13.46)	(-3.73)	
Transactions under special facilities (net) 8/	--	--	--	--	--	--	--	--	
Purchases	--	--	--	--	--	--	--	--	
Repurchases	--	--	--	--	--	--	--	--	
Total Fund credit outstanding (end of period)	848.82	878.82	878.82	978.82	1,002.60	1,031.84	1,061.35	1,090.59	
Under tranche policies 7/	612.42	642.42	642.42	742.42	766.20	795.44	824.95	854.19	
Special facilities 8/	236.40	236.40	236.40	236.40	236.40	236.40	236.40	236.40	
(In percent of new quota)									
Total Fund credit outstanding (end of period)	276.8	286.6	286.6	319.2	327.0	336.5	346.2	355.7	
Under tranche policies 7/	199.7	209.5	209.5	242.1	249.9	259.4	269.1	278.6	
Special facilities 8/	77.1	77.1	77.1	77.1	77.1	77.1	77.1	77.1	

Source: International Monetary Fund.

1/ End of the calendar month in which the staff paper was issued.

2/ Based on end-September 1983 and end-December 1983 performance criteria and completion of current review.

3/ Based on end-April 1984 performance criteria.

4/ Based on end-June 1984 performance criteria and completion of second review before end-June 1984.

5/ Based on end-September 1984 performance criteria and completion of third review before end-November 1984.

6/ Based on end-December 1984 performance criteria.

7/ Ordinary and enlarged access resources.

8/ Compensatory financing facility.

that provided the basis for this review were held in Rabat during the period May 7-19, 1984. 1/ A letter from the Minister of Finance summarizing the conclusions of the review discussions and proposing performance criteria for the second semester 1984 is attached.

II. Background

The present program with the Fund was introduced in mid-1983 and covers the period until the end of 1984. During the second half of 1983, the Moroccan authorities implemented the measures envisaged under the program, and noticeable progress was made in reducing the domestic and external imbalances and inflation, increasing the savings rate, and narrowing the resource gap. The current account deficit of the balance of payments (before debt rescheduling) was reduced by more than 5 percentage points of GDP, from 13.2 percent of GDP in 1982 to 8 percent in 1983, while the overall balance of payments deficit was lower than programmed (Table 2). The overall budgetary deficit was reduced from 12.5 percent of GDP in 1982 to 9.1 percent in 1983 before debt rescheduling, or to 8.4 percent after debt rescheduling. Also, all the performance criteria were met, with the exception of credit to the Government at end-1983 which was higher than programmed due to smaller disbursements of external loans for the budget than had been projected under the program; the Fund granted a waiver in respect of this criterion. 2/

For 1984 the program aims at further reducing the current account deficit of the balance of payments to 7.5 percent of GDP before rescheduling. After taking into account the debt relief already agreed 3/ and the exceptional external assistance expected to be disbursed in 1984, this target implies that the overall balance of payments would register a small surplus. The program also aims at containing the rate of inflation to below 11 percent and assumes a real rate of growth in GDP of 3 percent.

To achieve the above objectives, the program envisaged a further reduction in the budget deficit to 7.2 percent of GDP before debt relief and 6.1 percent of GDP after debt relief, mainly through limiting recruitment combined with a general wage freeze, containing other expenditures, raising new revenues, a further increase in certain administered prices, a significant restraint in credit expansion, a further depreciation of the exchange rate, export promotion measures

1/ Staff members participating in the mission were Mr. R.J. Bhatia (head-AFR), Mr. A. Tahari (AFR), Mr. J. Clément (ETR), Mr. Y. Fassassi (AFR), and Ms. R.M. Casaromani (secretary-AFR).

2/ For more details on developments in 1983, see EBS/84/71 and SM/84/63.

3/ Including the terms of rescheduling presently proposed by commercial banks (see below).

Table 2. Morocco: Selected Economic and Financial Indicators, 1981-84

	1981	1982		1983		1984	
		Prog.	Actual	Prog.	Prel. actual	Prog.	Rev.
<u>(Annual percent changes, unless otherwise specified)</u>							
National income and prices							
GDP at constant prices	-1.3	4.0	5.6	3.1	0.6	3.0	3.0
GDP deflator	10.8	12.0	9.2	10.1	6.5	11.7	11.7
Consumer prices	12.5	12.0	10.6	10.1	6.3	11.0	11.0
External sector (in SDRs)							
Exports, f.o.b.	4.4	13.3	-2.8	1.3	2.4	8.7	12.0
Imports, f.o.b.	12.4	3.4	6.5	-11.1	-14.6	1.8	3.9
Export volume	2.1	8.5	0.2	9.2	14.9	6.5	6.6
Import volume	4.8	-0.9	6.0	-9.1	-9.6	-0.5	1.1
Terms of trade (deterioration -)	-4.5	-0.2	-5.2	-5.1	-5.7	1.0	2.2
Nominal effective exchange rate (depreciation -) <u>1/</u>	-10.7	-3.5	-4.3	...	-6.0
Real effective exchange rate (depreciation -) <u>1/</u>	-9.1	...	-4.4	...	-6.6
Government budget							
Revenue (excluding grants)	17.4	20.0	14.8	7.5	3.0	16.2	17.1
Total expenditures <u>2/</u>	27.5	-0.8	9.2	-2.6	-7.9	7.3	9.8
Money and credit							
Domestic credit	19.6	13.8	13.8	20.0	20.0	8.8	9.9
Economy	(17.5)	(20.2)	(20.6)	(14.8)	(11.5)	(14.1)	(14.9)
Government	(21.2)	(9.5)	(9.2)	(23.9)	(26.4)	(5.3)	(6.6)
Money and quasi-money	16.4	8.5	12.5	16.6	17.4	10.4	11.7
<u>(In percent of GDP)</u>							
Central Government							
Budget deficit (before rescheduling) <u>2/</u>							
Excluding grants	14.5	8.2	12.5	8.7	9.1	7.2	7.7
Including grants	12.4	8.2	12.2	7.7	8.0	7.2	7.6
Budget deficit (after rescheduling) <u>2/</u>							
Excluding grants	14.5	8.2	12.5	...	8.4	6.1	6.6
Including grants	12.4	8.2	12.5	...	7.4	6.1	6.5
Domestic bank financing	4.8	2.6	2.5	5.2	7.1	1.7	2.0
Foreign financing (incl. grants)	9.4	5.3	7.0	5.0	3.6	5.0	5.1
Gross domestic investment	22.4	22.4	22.9	18.8	21.0	21.0	20.5
Gross domestic savings	8.7	12.6	9.4	10.0	12.2	12.7	13.8
External current account deficit (before rescheduling)							
Excluding grants	12.6	9.9	13.2	8.9	8.0	7.5	7.2
Including grants	10.5	9.9	11.9	7.8	6.9	7.5	7.1
External current account deficit (after rescheduling)							
Excluding grants	12.6	9.9	13.2	...	6.7	6.4	6.1
Including grants	10.5	9.9	11.9	...	5.6	6.4	6.0
External debt <u>3/</u> (inclusive of use of Fund credit)	62.0	6.12	78.0	82.2	87.1	95.0	95.0
Debt service ratio (in percent of exports of goods and nonfactor services and private transfers)							
Before rescheduling	33.2	33.7	41.4	42.4 <u>4/</u>	45.8 <u>5/</u>	54.0	50.1
After rescheduling	33.2	33.7	41.4	...	35.0 <u>5/</u>	27.0	24.8
<u>(In millions of SDRs, unless otherwise specified)</u>							
Overall balance of payments							
Before rescheduling	-208	-404	-578	-612	-496	-1,020	-1,030
After rescheduling	-208	-404	-578	...	-101	12	12
Gross official reserves (months of imports)	0.9	0.8	0.8	0.8	0.5	1.3	1.3

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

1/ Based on Morocco's currency basket.

2/ Excluding changes in "fonds réservés."

3/ Including short-term debt; for 1982-84 includes military debt.

4/ Excludes arrears on the servicing of the military debt.

5/ Includes arrears on the servicing of the military debt.

(including a reduction of 5 percentage points in the special import tax), further liberalization of the trade system. In addition, stringent limits were adopted on short-term debt and on new nonconcessional external loans.

III. Developments During the First Four Months of 1984

As indicated in the staff report on the first review of the stand-by arrangement (EBS/84/71, dated March 28, 1984), several of the measures noted in Section II have been put in place. The implementation of the program remains on track, and all performance criteria for end-April were met (Table 3). Since the completion of the first review by the Fund, in line with the flexible exchange rate policy followed by the Government, the Moroccan dirham has been depreciated by an additional 2 percent in April, bringing the cumulative depreciation to 7 percent from the end-1983 level (Chart 1). Further liberalization of the trade and exchange system, including transferring a number of imported commodities to the (free) list A and reducing the requirement for import deposits, was effected as programmed. The share of the free list of imports in total imports increased from 17 percent in mid-1983 to 24 percent at end-1983, and measures have been put in place to increase the share to 42 percent by mid-1984.

Economic and financial developments in the first four months of 1984 have been satisfactory. The annual rate of inflation in this period was about 7 percent, or well within the programmed rate of 11 percent. The overall budgetary deficit was also within the program limit; current revenue increased at a higher rate (16 percent), compared to the same period in the previous year (Table 4), while budgeted expenditure declined by 4 percent. As nonbank borrowing was higher than projected, the Treasury was able to reduce further the stock of "fonds réservés" (unpaid bills) by DH 500 million. The expansion in total credit by 2.5 percent and net credit to the Government by 1.8 percent was within the program ceilings, and the rate of growth of the money supply decelerated to 2 percent (Table 5).

On the external side, during the first four months of 1984 exports increased at a higher rate than expected, due in particular to a sharper increase in exports of phosphoric acid. Imports followed a trend consistent with the estimates included in the program with the exception of oil imports, which, reflecting boat arrival schedules, increased at a higher rate, and imports of wheat and sugar, which are administratively controlled, were also higher. However, the imports of these items are still projected to remain within the annual amount provided for in the initial estimates. On the basis of these developments during the first four months of the year, the 1984 outcome of the trade balance is now estimated to be slightly better than originally forecast. In volume terms, phosphoric acid is projected to increase by 19 percent in 1984 instead of the original estimate of

Table 3. Morocco: Quantitative Performance Criteria for 1984

	<u>April</u>		<u>June</u>	<u>September</u>	<u>December</u>
	<u>Program</u>	<u>Preliminary</u>		<u>Program</u>	
	<u>(In billions of dirhams)</u>				
Net borrowing by the Treasury <u>1/</u>	1.90	1.74	3.40	5.47	7.24
Total bank credit <u>2/</u>	52.30	51.97	53.10	54.67	55.71
Bank credit to the Treasury (net) <u>2/</u>	28.60	28.46	28.90	29.54	29.94
Changes in " <u>fonds réservés</u> " <u>3/</u>	0.30	-0.49	0.30	0.30	0.30
	<u>(In millions of U.S. dollars)</u>				
New nonconcessional foreign borrowing contracted or guaranteed by the Government or approved for public enterprises by the Government with maturity of 1 to 15 years	500.00	16.00	500.00	500.00	500.00
Of which 1 to 5 years	250.00	--	250.00	250.00	250.00
Short-term debt (outstanding)	1,000.00	961.00	1,000.00	1,000.00	1,000.00

Sources: Data provided by the Moroccan authorities.

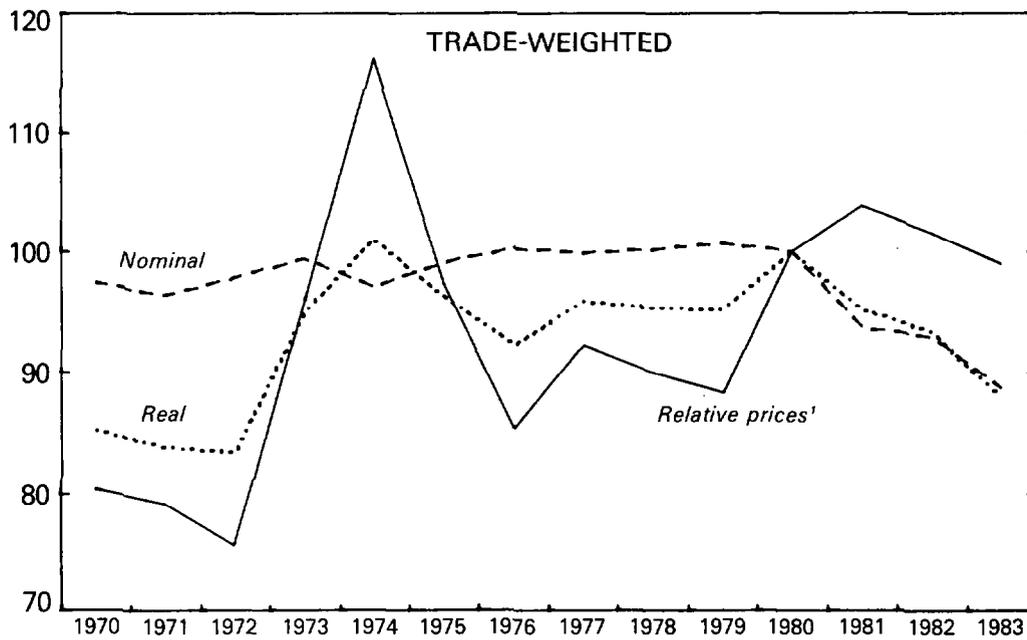
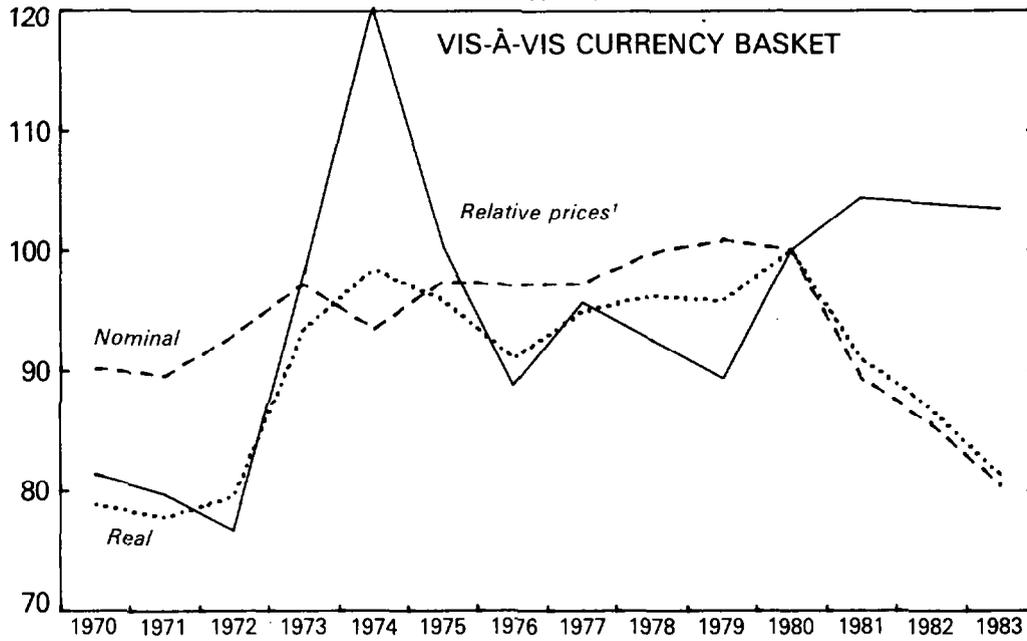
1/ As defined in paragraph 9 of the Annex to EBS/83/178.

2/ As defined in paragraph 11 of the Annex to EBS/83/178. These limits will be automatically reduced up to DH 400 million if corresponding additional external concessional assistance is received.

3/ Cumulative limits.

CHART 1
MOROCCO
NOMINAL AND REAL EFFECTIVE
EXCHANGE RATES, 1970-83

(1980=100)



Source: Currency weights supplied by Moroccan authorities, decrease in index indicates depreciation.
¹Relative prices: Domestic price indices/Weighted partner price indices.



Table 4. Morocco: Financial Transactions of the Central Government, 1982-84

(In millions of dirhams)

	1982	1983		1983	1984	1984	
	Actual	Program	Actual	First four months	Program	Revised	
Current revenue	20,480	22,022	21,094	6,733	7,779	24,516	24,704
Of which: OCP <u>1/</u>	(710)	(725)	(750)	(--)	(200)	(1,100)	(1,100)
Current expenditures	20,475	22,672	21,525	7,757	7,477	23,261	23,449
Interest payments on public debt	(3,144)	(3,869)	(3,526)	(1,178)	(1,281) <u>2/</u>	(3,930) <u>2/</u>	(4,118) <u>2/</u>
Expenditures on goods and services	(15,336)	(17,259)	(16,367)	(5,572)	(5,471)	(17,151)	(17,151)
Consumer subsidies	(2,000)	(1,544)	(1,632)	(1,007)	(725)	(2,180)	(2,180)
Current surplus or deficit (-)	5	-650	-431	-1,024	302	1,255	1,255
Capital expenditures	12,481	8,000	7,979	1,592	1,514	7,955	8,494
Extrabudgetary operations (net) <u>3/</u>	1,368	-100	407	468	-530	--	--
Overall deficit (-)	-11,108	-8,750	-8,003	-2,148	-1,742	-6,700	-7,239
Changes in " <u>fonds réservés</u> " (decrease -)	2,061	-2,061	-2,282	-2,235	-490	-300	-300
Cash financing	9,047	10,811	10,285	4,383	2,232	7,000	7,539
Grants	285	1,008	1,010	318	139	--	139
Foreign borrowing (net)	5,913	4,042	2,382	671	1,120	5,400	5,400
Domestic bank borrowing (net)	2,174	5,184	6,703	2,796	726	1,800	2,200
Central bank	(1,520)	(4,472)	(4,081)	(2,404)	(168)	(1,100)	(638)
Domestic money banks	(654)	(712)	(2,622)	(589)	(558)	(700)	(1,562)
Other domestic sources (net)	675	577	190	598	247	-200	-200
<u>Memorandum items:</u>							
Deferred interest payments	--	...	626	--	275	1,174	1,174
Overall deficit/GDP <u>4/</u>	12.5	8.7	8.4	6.1	6.6

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

1/ Contribution of the state-owned phosphate company.2/ Excluding debt relief on interest payments.3/ Excluding changes in "fonds réservés" (stock of unpaid bills).4/ After debt relief.

Table 5. Morocco: Monetary Survey, 1982-84

(In millions of dirhams; end of period)

	1982	1983	March	1984				
	Dec.	Dec. <u>1/</u>		April Prog.	April Prel.	June Prog.	Sept. Prog.	Dec. Prog.
Foreign asset (net)	-2,192	-3,528	-3,719	-3,600	-4,061	-3,550	-3,490	-3,425
Central bank	(-3,744)	(-5,381)	(-5,638)	(...)	(-6,120)	(...)	(...)	(...)
Deposit money banks	(1,552)	(1,853)	(1,919)	(...)	(2,059)	(...)	(...)	(...)
Domestic credit	42,258	50,693	52,166	52,293	51,969	53,093	54,674	55,712
Claims on the Government (net)	24,068	30,412	32,188	31,112	30,969	31,512	32,062	32,412
Banking system	21,043	27,734	29,536	28,634	28,460	28,934	29,534	29,934
Central bank	(12,746)	(16,128)	(17,320)	(17,373)	(16,419)	(16,524)	(16,679)	(16,766)
Deposit money banks	(8,297)	(11,606)	(12,216)	(11,261)	(12,041)	(12,410)	(12,855)	(13,168)
Nonbank private sector <u>2/</u>	3,025	2,678	2,652	2,478	2,509	2,578	2,528	2,478
Claims on the economy	18,190	20,281	19,978	21,181	21,000	21,581	22,612	23,300
<u>Assets = Liabilities</u>	<u>40,066</u>	<u>47,165</u>	<u>48,447</u>	<u>48,693</u>	<u>47,908</u>	<u>49,543</u>	<u>51,184</u>	<u>52,287</u>
Money plus quasi-money	38,959	45,744	46,832	47,382	46,682	48,226	49,903	51,106
Money	31,631	36,142	36,942	37,436	36,787	38,099	39,424	40,374
Currency outside banks	(12,023)	(13,636)	(13,781)	(14,124)	(13,841)	(14,288)	(14,784)	(15,141)
Demand deposits <u>3/</u>	(19,608)	(22,506)	(23,161)	(23,312)	(22,946)	(23,811)	(24,640)	(25,233)
Quasi-money	7,328	9,602	9,890	9,946	9,895	10,127	10,479	10,732
Import deposit	288	576	434	250	350	200	100	--
Other (net)	819	845	1,181	1,061 <u>4/</u>	876	1,117 <u>4/</u>	1,181 <u>4/</u>	1,181 <u>4/</u>

Source: Data provided by the Moroccan authorities; and staff projections.

1/ The data for December 1983 differ somewhat from those published in the Recent Economic Developments Report (SM/84/51) because of the availability of more recent informations on credit.

2/ Counterparts of postal checking deposits, private sector deposits with the Treasury, and import deposits transferred to the Treasury.

3/ Includes checking deposits with deposit money banks, private sector deposits with the central bank, postal checking deposits, and private sector deposits with the Treasury.

4/ Includes valuation change.

6 percent, while its unit price is projected to increase by more than 7 percent instead of the original estimate of 6 percent. Regarding other exports, their trends are expected to remain as projected originally, except for citrus products, resulting from somewhat lower 1983/84 production than originally estimated, and for fertilizers, compensating somewhat for higher exports of phosphoric acid. All in all exports are expected to increase by 12 percent in SDR terms, while exports of phosphates and derivatives are expected to increase by 19 percent (Table 6). On the imports side, as mentioned earlier, during the first four months of 1984 imports followed a trend consistent with the original estimates with the exception of some administratively controlled imports--oil, wheat, and sugar-- , which have increased at a higher rate. However, the increase in imports of oil for the whole year is expected to remain the same as originally forecast. Total imports for the year 1984 should register an increase of no more than 4 percent, compared to the 2 percent originally projected, with the higher imports being mainly those of sulfur, reflecting higher exports of phosphoric acid. In addition, import volume of wheat has been revised upward because of a lower 1983/84 production than originally estimated. The terms of trade are expected to improve by slightly more than originally estimated.

Private transfers have been revised upward following their good performance in 1983, and the estimates of other services transactions remain as originally estimated. On the capital account, the estimate relating to the public sector remains virtually unchanged, while that relating to the private sector, including errors and omissions, has been revised downward. Overall, the balance of payments for 1984 is still projected to register the initially targeted surplus of SDR 12 million. Accordingly, in setting the performance criteria (see Section IV below) for the rest of 1984, the authorities intend to keep unchanged the main thrust of the policies under the program. The medium-term projections of the balance of payments and external debt described in EBS/84/71 remain valid. These projections had indicated that the current account deficit (after taking into account the debt rescheduling obtained in 1983 and 1984) would decline steadily to 1.3 percent of GDP in 1988 and would move into a surplus in the following years, while the debt service ratio (after 1983-84 rescheduling) would average 61 percent during 1985-89 and then decline gradually to 26 percent by 1990.

The Moroccan authorities are in the process of completing debt rescheduling agreements. The non-Paris Club official creditors have agreed to reschedule debt on terms similar to, or even more favorable than, the Paris Club offer. Also, all the financial terms on rescheduling with commercial banks, including rollover of the outstanding short-term debt, have been agreed upon; the only remaining issue relates to central bank guarantee in respect of the rescheduled loans.

Table 6. Morocco: Balance of Payments, 1982-84

(In millions of SDRs)

	1982	1983		1984	
		Prog.	Prov.	Prog.	Rev.
Merchandise trade (net)	-1,585	-1,174	-1,032	-918	-915
Exports	1,882	1,895	1,928	2,095	2,159
Phosphates and derivatives	(833)	(765)	(834)	(934)	(989)
Other	(1,049)	(1,130)	(1,094)	(1,161)	(1,170)
Imports, f.o.b.	-3,467	-3,069	-2,960	-3,013	-3,074
Services (net)	-1,065	-886	-855	-893	-897
Freight and insurance	-328	-264	-259	-268	-284
Other transport	41	40	36	44	38
Tourism	298	343	351	404	404
Investment income	-671	-676	-755 ^{1/}	-804	-815
Government and other services	-405	-329	-228	-269	-240
Private transfers (net)	886	860	892	871	910
Current account	-1,764	-1,200	-995	-940	-902
Nonmonetary capital (net)	1,186	588	499	-80	-128
Private ^{2/}	152	40	6	50	-13
Official grants	266	144	132	--	15
Public sector loans (net)	849	404	361	-130	-130
Disbursements ^{3/}	(1,618)	(1,216)	(1,262)	(1,041)	(1,041)
Government	1,246	731	625	815	815
Guaranteed debt	372	485	637	226	226
Amortization	(-769)	(-812)	(-901) ^{4/}	(-1,171)	(-1,171)
SDR allocation	--	--	--	--	--
Debt relief (net)	--	...	395	1,032	1,042
Overall balance	-578	-612	-101	12	12
Financing	578	612	101	-12	-12
Net use of Fund credit	401	151	91	183	183
Change in foreign assets (increase -)	-76	--	10	-195	-195
Financing gap	--	461	--	--	--
Arrears	253	--	--	--	--
<u>Memorandum items:</u>					
Current account deficit in percent of GDP (before rescheduling)	13.2	8.9	8.0	7.5	7.3
DH/SDR	6.65	...	7.61	8.9	8.9

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

^{1/} Taking into account the payment of part of end-1982 outstanding arrears of SDR 24 million.

^{2/} Including errors and omissions.

^{3/} Short-term debt included on a net basis.

^{4/} Taking into account the payment of part of end-1982 outstanding arrears of SDR 36 million.

During the first four months of 1984 the authorities have also made noticeable progress in delineating some main policy issues as they relate to capital expenditures, petroleum prices, fiscal reform, and agricultural producer prices.

In the staff report for the first review of the program (EBS/84/71, pages 23-4) a reference was made to the large amount of outstanding budgetary authorizations for capital expenditures from previous years' appropriations, which could jeopardize effective financial management. It was recommended that these allocations be reviewed with a view to their orderly cancellation or drawdown in relation to available finance. In this respect, the Government obtained technical assistance from the World Bank, which has submitted a report making recommendations with a view to reducing the gap between the authorizations outstanding and commitments which could be undertaken in a given years expenditure program. The report estimates that, after making allowance for the allocations of DH 6 billion already cancelled in 1983, the present stock of such budgetary authorizations amounts to DH 22 billion. Taking into account the normal system of processing of government capital expenditure, this overhang implies a wide divergence between the potential demand for cash payments and the financial resources of the Government. Accordingly, the report recommends that nonpriority projects be stretched out or canceled, that the justification and the profitability of certain projects be reexamined, and that the participation of the Government in the financing of investment in certain public enterprises be gradually reduced. However, even if these recommendations were implemented, the remaining outstanding commitments would exceed the amount of DH 8 billion presently included in the program for 1984; the gap created by the outstanding stock of authorizations due would also persist for some years. The Government proposes to follow up on this study and plans to make an inventory of such outstanding allocations for each sector at various stages between commitment and actual payment, with a view to establishing a systematic plan for their orderly liquidation, beginning with the 1985 budget law. This program, as well as the 1985 budgetary policies, would be covered by the third review under the present stand-by arrangement before end-November 1984. In the meantime, in order to meet urgent demands for payments and to enable the private sector to improve its financial management, the Government is proposing an increase in the programmed cash payments for investment and thus in the budgetary deficit, by DH 540 million (about 0.5 percent of GDP), of which DH 140 million are covered by additional external grants already received but not anticipated in the initial program estimates and possibly up to DH 400 million will be financed by additional recourse to the domestic banking system. The authorities are expecting to receive further external assistance and have proposed that any such aid would be used initially to reduce the credit ceilings to the Government by amounts up to the above-mentioned DH 400 million and that they would consult with the Fund on the utilization of any remaining amount.

The authorities have also completed a study of the pricing mechanism for petroleum products and have instituted a system whose objective is to avoid any global subsidies to the petroleum sector (both producers and consumers). Under the system, the pricing and cost structure is to be reviewed every three months with a view to making necessary adjustments. Moreover, prices are to be set so as to allow the sector to absorb some limited cost increases, if necessary, between points of adjustment. The new procedures of price determination have been put in place, and the first review of prices took place in April and resulted in an increase in the price of gasoline by 7 percent. At the existing prices, the global petroleum operations are estimated to yield a small surplus.

An important element of the fiscal policy in 1984 relates to the implementation during 1984 of the long-awaited tax reform concerning the setting up of a corporate income tax, a general income tax, and the substitution for the tax on production and services of a value-added tax. A "Loi cadre" relating to this fiscal reform has just been promulgated by a Royal decree and should facilitate the introduction of the reform as scheduled. The authorities have already completed draft laws to institute the corporate income tax and the general income tax and expect to complete the draft law relating to the VAT in the very near future. The three drafts will be submitted to the Council of Ministers for approval, with a view to presenting them to the legislative assembly for enactment during its next session after legislative elections fixed for September 1984.

To promote agricultural production, producer prices, which had remained unchanged for the 1982/83 crop season, were raised in September 1983 by between 7 and 30 percent for cereals, cotton, sugar cane, and sugar beets. As envisaged under the program the authorities intend to continue providing adequate pricing incentives to producers. For the next crop year a preliminary examination of the evolution of cereal producer prices, cost of production, and the terms of trade vis-à-vis other sectors in the economy indicate that an increase in agricultural producer prices of around 15 percent would be desirable. The authorities have agreed to the principle of adjusting these prices before the beginning of the next season in September, but the size of adjustment is still to be determined.

IV. Performance Criteria for the Second Semester of 1984

The present stand-by arrangement contains performance criteria relating to (1) the ceiling on short-term external debt; (2) the ceilings on contracting and guaranteeing by the Government of new non-concessional external borrowing with maturities of between 1 and 15 years and 1 and 5 years; (3) the ceiling on increases in "fonds réservés"; (4) the ceiling on total net borrowing by the Treasury; (5) the ceiling on net bank credit to the Treasury; and (6) the ceiling

on total bank credit. The ceilings relating to external borrowing (both short- and medium-term) and to increases in "fonds réservés," which were already fixed for the period through end-1984 and are shown in Table 3, would remain unchanged.

The proposed ceilings relating to the total net borrowing by the Treasury, net bank credit to the Treasury, and total bank credit (4 through 6 above) take into account the above-mentioned proposed increase in government capital expenditure and, consequently, in the overall budget deficit, by DH 540 million. In addition, and in keeping with the restrictive posture of credit policy, the credit increase to the private sector will be limited to 15 percent for the whole year, accordingly, total credit will increase by about 10 percent. In the attached letter the Government has proposed that total net borrowing by the Treasury (as originally defined, including changes in "fonds réservés," and corresponds to the revised budgetary deficit) not exceed DH 5.47 billion by end-September 1984 and DH 7.24 billion by end-December. Total bank credit, which amounted to DH 50.69 billion at end-December 1983, will not exceed DH 54.67 billion on September 30, 1984 and DH 55.71 billion on December 31, 1984. Net bank credit to the Treasury, which amounted to DH 27.7 billion at end-December 1983, will not exceed DH 29.54 billion and DH 29.94 billion for the same dates, respectively. Accordingly, of the total proposed expansion in credit of 10 percent for the year, 40 percent would be used by the Treasury compared to 75 percent in 1983. Based on the already-secured external finance (mostly concessional), 73 percent of the financing needs of the Treasury will be covered by foreign borrowing and the above-mentioned small amount of grants already received, while net domestic bank borrowing is now projected to finance 29 percent of the Treasury deficit, compared to 65 percent in the previous year.

On the basis of the proposed ceilings, and assuming that the overall balance of payments would register the targeted surplus of SDR 12 million, the increase in money supply in 1984 is now estimated at 11.7 percent, or well below the projected increase in nominal GDP of 15 percent. As for interest rates, the present rates are significantly positive and considered as adequate.

V. Staff Appraisal

Since the inception of the program under the current stand-by arrangement in mid-1983, the Government has implemented the envisaged measures. All the performance criteria for end-April 1984 have been observed, and the program continues to be on track. Developments so far in 1984 have been satisfactory and indicate that the program targets for 1984 should be achieved. In the first four months of 1984 the annual inflation rate has been limited to about 7 percent; the overall budgetary deficit was within the program's limit; and exports, in particular of phosphate derivatives, increased at a rate higher than

projected under the program. The staff shares the authorities' view that, for the remainder of 1984 the thrust of the program should be maintained.

In addition to fixing the performance criteria for the second half of the year, the present review concentrated on four main topics: a plan to reduce the gap between budgetary capital expenditure authorizations from past years and actual capital outlays; agricultural producer prices; pricing system in the petroleum sector; and fiscal reform. Regarding the first issue, a study has been prepared in consultation with the World Bank, which is to be followed by a further inventory-taking of outstanding commitments at various levels of Government. The authorities intend to establish a program for their settlement to bring them more in line with available finance, beginning with the 1985 budget law. This program, as well as the budgetary policies for 1985, will be part of the next review before end-November 1984. In the meantime the Government has requested a small increase (by 0.5 percent of GDP) in the programmed cash payments on investment expenditures in 1984 and thus in the targeted overall budgetary deficit.

The staff considers it imperative that a systematic plan be followed to liquidate the overhang of capital expenditure allocations. In the meantime, it regards the requested increase in the deficit as financeable, while maintaining the original external targets of the program. The increase in the deficit will be financed by unanticipated external grants already received and higher recourse to the domestic banking system than originally projected. The authorities are expecting to receive additional external assistance which would in the first instance be used to reduce bank financing to the original program target. The authorities would also consult with the Fund should such assistance exceed DH 400 million.

As for agricultural producer prices, the authorities have agreed to adjust them in September before the next crop year, in light of the evolution of real producer prices, the cost of production, and the relative terms of trade between the agricultural and other sectors. The staff has stressed that the policy on producer prices should not be inhibited by the concerns to keep down subsidized consumer prices. At the same time, it has drawn the authorities' attention to the possible budgetary costs (via consumer subsidies) of such increases in producer prices, and has stressed that consumer prices could not be allowed to remain frozen without impeding the progress towards financial viability.

As envisaged under the program, the Government has put into place a system of determining petroleum prices so as to avoid any global subsidies in this sector. Given the experience with it during the April adjustment of prices, the staff is satisfied that the authorities have fulfilled their commitment to introduce a system that would ensure its global financial equilibrium.

Regarding the fiscal reform, the "Loi cadre" instituting the VAT, the corporate income tax, and the general income tax has been promulgated by decree and there are clear indications that the reform will be introduced in time for the 1985 budget law; draft laws regarding these three taxes are expected to be submitted for enactment to the next Parliament in September.

The satisfactory developments during the second half of 1983 and in the first four months of 1984, the implementation of all the measures envisaged under the program, and the determination of the authorities to implement the program rigorously for the remainder of 1984 indicate that the program is on track and that its objectives should be achieved. However, the staff believes that the improvement is as yet fragile and needs to be consolidated. Partly because of this, but also because the underlying imbalances are still large and could be corrected only over a few years, the staff, in its discussions with the authorities, has stressed the importance of a sustained application of adjustment measures over an extended period.

VI. Proposed Decision

In view of the above the following draft decision is proposed for adoption by the Executive Board:

1. Morocco has consulted with the Fund in accordance with paragraph 4(b) of the stand-by arrangement for Morocco (EBS/83/78, August 19, 1983), and paragraph 2 of the letter of the Minister of Finance dated July 30, 1983 attached to the stand-by arrangement, in order to reach understandings subject to which purchases may be made by Morocco under the stand-by arrangement.

2. The letter of the Minister of Finance, dated May 18, 1984, shall be attached to the stand-by arrangement for Morocco, and the letters of July 30, 1983 and March 18, 1984 shall be read as supplemented by the letter of May 18, 1984.

3. Morocco will not make purchases under the stand-by arrangement that would increase the Fund's holdings of Morocco's currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12.5 percent of quota during any period in which the data for the first nine months of 1984 or for the entire year, respectively, indicate that:

(i) the ceilings on total net borrowing by the Treasury specified in paragraph 3 of the letter of May 18, 1984; or

(ii) the ceilings on total credit specified in paragraph 3 of the letter of May 8, 1984; or

(iii) the ceilings on net bank credit to the Treasury specified in paragraph 3 of the letter of May 18, 1984; or

(iv) the ceiling on increases in the "fonds réservés" specified in paragraph 3 of the letter of March 18, 1984; or

(v) the ceilings on contracting and guaranteeing new nonconcessional external borrowing with a maturity of between 1 and 15 years, and 1 and 5 years, described in paragraph 6 of the letter of March 18, 1984; or

(vi) the ceilings on short-term external debt also described in paragraph 6 of the letter of March 18, 1984 are not observed.

Morocco: Relations with the Fund
(As of April 30, 1984)

I. Membership status

- (a) Date of membership - April 25, 1958
- (b) Status - Article XIV

(A) Financial Relations

II. General department (General Resources Account)

- (a) Quota: SDR 306.6 million
- (b) Total Fund holdings of member's currency: SDR 1,285.4 million; 419.2 percent of quota

	<u>Millions of</u> <u>SDRs</u>	<u>Percent of</u> <u>quota</u>
(c) Use of Fund credit	978.8	319.2
Credit tranches	225.0	73.4
EFF	137.4	44.8
SFF	137.5	44.8
EAR	242.5	79.1
CFF	236.4	77.1
(d) Repurchase obligations (April 1983-March 1985)	58.2	19.0

III. Current stand-by arrangement

- (a) Duration: September 16, 1983-March 15, 1985
- (b) Amount: SDR 300 million.
- (c) Utilization: SDR 170 million.
- (d) Undrawn balance: SDR 130 million.
- (e) Previous stand-by and extended arrangements: extended arrangement approved in October 1980 in an amount of SDR 810 million, 540 percent of quota, raised to SDR 817 million in March 1981, following increase in quota. Stand-by arrangement (one-year) approved in April 1982 in an amount of SDR 281.25 million, 125 percent of quota.

IV. SDR department

- (a) Net cumulative allocation: SDR 85.7 million.
- (b) Holdings: SDR 11.2 million; 13.1 percent of net cumulative allocation.

V. Administered accounts

Trust Fund loans

- (i) Disbursed: SDR 110.43 million
- (ii) Outstanding: SDR 101.98 million

VI. Overdue obligations to the Fund - None

(B) Nonfinancial Relations

VII. Exchange system: Other managed floating; SDR 1 = DH 8.5061

VIII. Last Article IV Consultation and Stand-By Review--December 1983, completed by the Executive Board on April 9, 1984. Decisions as follows:

Article IV Consultation

1. The Fund takes this decision relating to Morocco's exchange measures subject to Article VIII, Section 2 (a) in concluding the 1983 Article XIV consultation with Morocco, and in the light of the 1983 Article IV consultation with Morocco conducted under Decision No. 5392-(77/63), adopted April 29, 1977 ("Surveillance over Exchange Rate Policies.")

2. The Fund encourages the authorities in their determination to eliminate the remaining bilateral payments arrangements with two Fund members.

Review Under Stand-By Arrangement

1. Morocco has consulted with the Fund in accordance with paragraph 4 (b) of the stand-by arrangement for Morocco (EBS/83/178, August 19, 1983), and paragraph 2 of the letter of the Minister of Finance dated July 30, 1983 attached to the stand-by arrangement, in order to reach understandings subject to which purchases may be made by Morocco under the stand-by arrangement. Morocco has also requested the Fund to waive observance of the performance criterion in paragraph 4(a)(iv) of the stand-by arrangement for end-December 1983.

2. The letter of the Minister of Finance, dated March 18, 1984, shall be attached to the stand-by arrangement for Morocco, and the letter of July 30, 1983 shall be read as supplemented by the letter of March 18, 1984.

3. The Fund grants the waiver requested by Morocco.

4. Morocco will not make purchases under the stand-by arrangement that would increase the Fund's holdings of Morocco's currency in the credit tranches beyond 25 percent of quota or increase the Fund's holdings of that currency resulting from purchases of borrowed resources beyond 12 1/2 percent of quota during any period in which the data for the first four months of 1984 and the first semester of 1984 indicate that:

- (i) the ceilings on total net borrowing by the Treasury specified in paragraph 3 of the letter of March 18, 1984; or
- (ii) the ceiling on increases in the "fonds réservés" specified in paragraph 3 of the same letter; or
- (iii) the ceilings on total bank credit specified in paragraph 5 of the same letter; or
- (iv) the ceiling on net bank credit to the Treasury specified in paragraph 5 of the same letter; or
- (v) the ceilings on contracting or guaranteeing new nonconcessional external borrowing with a maturity of between 1 and 15 years, and 1 and 5 years, described in paragraph 6 of the same letter; or
- (vi) the ceiling on short-term external debt also described in paragraph 6 of the same letter

are not observed.

IX. Technical assistance

- (a) CBD: None
- (b) Fiscal: Tax reform (1982, 1983, 1984)

X. Resident representative/Advisor - None

Morocco: Financial Relations with the World Bank Group 1/

(In millions of U.S. dollars)

	<u>Total</u>		<u>Disbursed</u>	<u>Undisbursed</u>
	<u>IBRD</u>	<u>IDA</u>		
Agricultural and rural development	457.9	14.0	66.4	405.5
Education	188.0	--	39.4	148.6
Energy, power, and utilities	178.0	--	53.0	125.0
Transportation	62.0	--	44.8	17.2
Industry and tourism	338.8	--	68.4	270.4
Urban development	54.0	--	9.5	44.5
Other (after 1974)	371.2	--	77.7	293.5
Other (prior to 1974)	<u>802.8</u>	<u>38.6</u>	<u>841.4</u>	<u>--</u>
Total	2,452.7	52.6	1,200.6	1,304.7
Of which has been repaid	<u>-322.0</u>	<u>-1.8</u>		
Total outstanding	2,130.7	50.8		
IFC investments		54.6		

Recent economic and sector missions:

- Telecommunication Sector Mission, November 1981
- Public Sector Investment Review, December 1981 and April 1982
- Housing Sector Mission, November 1982
- Petroleum Exploration Mission, January 1983
- Irrigation Project Mission, February 1983
- Financial Intermediation Mission, August-September 1983
- Country Implementation Review, October-November 1983
- Several missions on the Industrial and Trade Policy Adjustment loan
- Policy Reforms in the Education Sector, October 1983
- Public Investment Review, April 1984

Source: World Bank.

1/ As of April 30, 1984. Does not include the Housing Development Project Loan of US\$60 million, signed April 11, 1983; the Oulmes-Rommani Agriculture Development Project loan of US\$30 million, signed May 23, 1983; the Communal Infrastructure Fund Project loan of US\$16 million, signed May 23, 1983; the Petroleum Exploration and Appraisal Project loan of US\$75.2 million, signed May 23, 1983; the Fourth Highway Project loan of US\$85 million approved March 29, 1983; and the Small- and Medium-Irrigation Project loan of US\$42 million, approved March 29, 1983.

KINGDOM OF MOROCCO

MINISTRY OF FINANCE

THE MINISTER

Rabat, May 18, 1984

Sir:

Under the present stand-by arrangement with the International Monetary Fund a second review of the program was envisaged before June 30, 1984. This review was to cover the progress under the program during the first several months of 1984 and the setting of performance criteria for the second half of 1984. It was also to examine producer prices for the next agricultural season, the modalities of a policy of liberalizing petroleum prices to be in place before end-June 1984, the introduction of the fiscal reform, and the examination of the plan established in consultation with the World Bank to reduce the gap between the total of "budgetary credits" ("crédits budgétaires") and available resources ("moyens de paiement"). The conclusions of this second review of the program with the staff of the Fund, which was held in Rabat in May 1984, are as follows:

1. During the first four months of 1984 the economic and financial developments were satisfactory and indicated that the objectives of the program for 1984, such as communicated to the Fund in my letter of March 18, 1984, will be realized. During this period the Government has vigorously applied the program, and the measures envisaged in the framework of the program were executed, including especially an additional depreciation of the exchange rate of 5 percent between February and April and a further liberalization of the trade system. On the basis of provisional figures all the performance criteria at the end of April 1984 were fulfilled. For the first quarter the rate of inflation has decelerated to 1.8 percent, the global budgetary deficit was within the limits of the program, and the rate of growth of exports was higher than was projected.
2. As was envisaged in the program, a mission of the World Bank has just completed a study of the budgeted investment projects, including those for which budgetary credit ("crédits de report") had been committed in previous years. This study has the objective of establishing a plan to reduce the difference between the amount of budgetary credits opened ("crédits budgétaires ouverts ou engagés") or committed and available resources. The study shows that, taking into account commitments already made by different ministries and the normal rhythm of procedures for payment, the demands for payment for 1984 would exceed the amount of DH 8 billion originally included in the program and that this difference between commitments and means of

payment will persist for some years, even after stretching or canceling projects considered of low priority. The Government plans to make an inventory of commitments already made in each sector and at different stages of payment procedures with a view to establishing a program for their reduction beginning with the 1985 budget law. This program, as well as the budgetary policies for 1985, will be the subject of an examination with the Fund in the course of the next review of program before end-November 1984. In the meantime, in order to permit the private sector to improve its financial management, the Government proposes to increase somewhat, by DH 540 million, the budgetary credits for payments under capital investment as initially programmed and as a consequence to increase the overall budgetary deficit by the same amount. This increase in the deficit will be financed by additional external grants of DH 140 million that were not anticipated and by additional domestic bank credit of DH 400 million. The Government expects to receive supplementary concessional assistance that it will utilize for capital expenditures with a view to reducing further the gap between commitments and means of payment. In such an event the Government will consult the Fund with a view to reviewing the ceiling relating to the overall deficit of the Treasury. It is understood that this concessional aid will first of all be used to cover the amount of DH 400 million in increased bank credit to the Treasury mentioned above.

3. In conformity with the objectives of the program, and as performance criteria for the second half of the year, the increase in total net borrowing by the Treasury (as defined in paragraph 9 of the memorandum on economic and financial policies attached to my letter of July 30, 1983) will not exceed DH 5.47 billion of the period January-September 1984 and DH 7.24 billion for the year 1984. The total bank credit (as defined in paragraph 11 of the above-mentioned memorandum) will not exceed DH 54.67 billion at end-September 1984 and DH 55.71 billion at end-December 1984. During the same period net bank credit to the Treasury (as defined in paragraph 11 of the above-mentioned memorandum) will not exceed, respectively, DH 29.54 billion and DH 29.94 billion at end-September and end-December. These criteria imply, taking into account the program's objective regarding the balance of payments, an increase of 11.7 percent in money supply, while the projected increase in GDP is 15 percent. The above-mentioned credit limits will be reduced by the amount of net loans to the Treasury and grants that exceed the projected amount (DH 3.77 billion at end-September and DH 5.54 billion for the whole year). The Government does not propose any other modification in the performance criteria relating to the changes in "fonds réservés" and the external debt for the second half of 1984 from the level already included in the program and mentioned in my letter of March 18, 1984.

4. Following a study completed in March, the Government has put into place a system of determining petroleum prices that assures global financing equilibrium of the sector. The formulas of systematic

adjustment of prices at the refinery level and of retail prices had been worked out and would be reviewed every quarter in order to determine whether a price revision is necessary with a view to avoiding any subsidy to this sector. This mechanism had already led to an increase of about 7 percent in the price of gasoline in April.

5. In order to encourage agricultural production, the Government will adjust producer prices before end-September for the next crop season. These adjustments will take into account the evolution of prices, cost of production, and the relative terms of trade between the agricultural and the other sectors. A preliminary examination of these factors with the staff of the Fund during the course of the current review indicated that a significant revision of prices would be desirable.

6. A "Loi cadre" relating to the fiscal reforms has just been promulgated by a Royal decree. This reform concerns the setting up of a general tax on income, a tax on the corporations, and a substitution of the tax on goods and services by a value-added tax. As envisaged under the program, the Government has completed a draft law to institute the VAT. This draft, as well as those related to IS and IGR, will be submitted to the Council of Ministers in the near future. The Government will submit this draft text at the House of Representatives during its next session after legislative elections fixed for September 1984.

Very truly yours,

/s/

Abdellatif JOUHRI
Minister of Finance

Mr. Jacques de Larosière
Managing Director
International Monetary Fund
Washington, D.C. 20431