

EBS/85/157
Correction 1

CONFIDENTIAL

July 5, 1985

To: Members of the Executive Board
From: The Acting Secretary
Subject: Morocco - Staff Report for the 1985 Article IV Consultation
and Request for Stand-By Arrangement

The following corrections have been made in EBS/85/157 (6/21/85):

Page 17, Table 7, column 1, line 15: for "152" read "255"
line 16: for "185" read "112"
line 17: for "849" read "850"
line 18: for "(1,618)" read "(1,619)"
column 2, line 14: for "359" read "418"
line 15: for "-134" read "-199"
line 16: for "132" read "133"
line 17: for "361" read "484"
line 18: for "(1,262)" read "(1,349)"
line 19: for "(-901)" read "(-865)"

Page 33, para. 1, line 7: for "cereal rice" read "cereal price"

Pages 60a and 60b: inadvertently omitted

Corrected pages are attached.

Att: (4)

Table 7. Morocco: Balance of Payments, 1982-85

(In millions of SDRs)

	1982	1983	1984		1985	
	Revised	Revised	Prog. EBS/84/71	Rev. Prog. EBS/84/129	Est. Proj.	
Merchandise trade (net)	-1,605	-1,136	-918	-915	-1,350	-998
Exports	1,850	1,951	2,095	2,159	2,115	2,345
Phosphates and derivatives	(827)	(865)	(934)	(989)	(985)	(1,057)
Other	(1,023)	(1,086)	(1,161)	(1,170)	(1,131)	(1,288)
Imports, f.o.b	-3,456	-3,087	-3,013	-3,074	-3,465	-3,343
Services (net)	-1,085	-769	-893	-897	-816	-792
Freight and insurance	-328	-171	-268	-284	-220	-195
Other transport	41	36	44	38	22	33
Tourism	298	350	404	404	405	479
Investment income	-671	-755	-804	-815	-904	-1,028
Government and other services	-425	-220	-269	-240	-120 ^{2/}	-81 ^{2/}
Private transfers (net)	889	914	871	910	918	990
Current account	-1,802	-992	-940	-902	-1,248	-800
Nonmonetary capital (net)	1,217	418	-80	-128	-307	-76
Private ^{1/}	255	-199	50	-13	27	-30
Official grants	112	133	--	15	15	297
Public sector loans (net)	850	484	-130	-130	-350	-343
Disbursements ^{3/}	(1,619)	(1,349)	(1,041)	(1,041)	(934)	(1,100)
Amortization	(-769)	(-865)	(-1,171)	(-1,171)	(-1,284)	(-1,443)
Debt relief	--	588 ^{4/}	1,032	1,042	1,333 ^{4/}	...
Overall balance	-585	15	12	12	-222	-876
Financing	585	-15	-12	-12	222	876
Net use of Fund credit	401	91	183	183	133	72 ^{5/}
Change in other net foreign assets (increase-)	-69	147	-195	-195	-13	-152
Financing gap to be filled by debt relief	--	--	--	--	--	1,059
Arrears	253	-253	--	--	63 ^{6/}	-63 ^{6/}
Delays in completing bank rescheduling	--	--	--	--	40	-40
Memorandum items:						
Current account deficit in percent of GDP (before debt relief)	13.3	8.0	7.5	7.3	10.7	6.5
End-year gross reserves (months of imports)	0.6	0.4	1.3	1.3	0.2	0.6
DH/SDR	6.65	7.61	8.9	8.9	9.0	10.1

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

^{1/} Including errors and omissions.^{2/} Excludes military debt service payments which are now included under investment income and amortization.^{3/} Including net increases in public sector short-term debt.^{4/} Assumes debt rescheduling for 1983/84 to have been completed.^{5/} Includes Fund purchases under proposed program of SDR 40 million (SBA) and SDR 85.5 million (CFF).^{6/} Represents late payments of rescheduled debt at end-1984. This definition of arrears excludes amounts to be rescheduled for which agreements have not yet been signed.

15 percent to 10 percent in January 1984 and eliminated in July. The elimination of the export monopoly of the Office de Commercialisation et d'Exportation (OCE) for processed food exports and the elimination of export licensing requirement for industrial and most agricultural products were measures taken as part of the program to promote exports.

These policies achieved some success in 1984. Exports, at SDR 2.1 billion, were in line with the revised program target, and represented an 8.4 percent increase over the revised level recorded in 1983. In volume terms exports grew by 4.6 percent reflecting a strong performance of finished and semi-finished goods which offset the weak demand for Morocco's traditional exports, such as phosphate rock, and lower agricultural exports resulting from adverse weather conditions. However, imports on a c.i.f. basis grew by 13.1 percent, substantially more than the 3.9 percent projected in the program. Two thirds of the excess relative to target can be attributed largely to the drought, which made necessary the higher imports of cereals and of fuel, to compensate for the reduced production of hydroelectric power. The remaining one third reflected some restocking after the severe import restrictions in 1983, the relatively high degree of liquidity in the economy at the beginning of the period, and some recovery in investment in the public enterprise sector.

The higher than projected trade deficit was partially offset by an improved performance on the services and transfers accounts, which reflected, inter alia, lower freight charges, and a rapid rise in tourist receipts. Nonetheless, the current account in 1984 registered a deficit of SDR 1,248 million (10.7 percent of GDP), substantially higher than had been programmed (see Table 7).

Capital inflows were significantly lower than had been anticipated, but this was offset to some extent by higher debt relief than originally estimated, resulting from better terms obtained from non-Paris Club official creditors. The overall balance of payments recorded a deficit of SDR 222 million compared with a programmed surplus of SDR 12 million. The projected reconstitution of reserves to an amount equivalent to 1.3 months of imports did not take place; gross reserves declined instead by SDR 52 million to a level of SDR 50 million and net reserves other than net liabilities to the Fund remained stable after taking into account a reduction of certain foreign liabilities of the Central Bank. There was an accumulation of external arrears of SDR 63 million on payments of rescheduled military debt; the authorities stressed that these arrears were caused by administrative delays by certain government departments in the processing of obligations falling due and that requests for foreign exchange had not been presented to the Central Bank. SDR 5 million of these arrears were paid in January 1985. In March 1985 the authorities stated that the remaining arrears would be paid as soon as possible, after verification of the amounts, and in any case before end-July 1985.

The gradual elimination of subsidies and the reform of the system will be accompanied by measures, which are being prepared in consultation with the World Bank in the context of a structural adjustment loan for agriculture, aimed at promoting cereal production and improving marketing; these measures are required by the fact that the low subsidized retail price of flour, together with rigidities in marketing arrangements, depresses the cereal price obtained by the majority of producers at a level well below the official producer price, thereby hampering production incentives. The reforms are to be finalized in the second half of 1985; they will include an increased participation of the private sector in the marketing, processing and storage of cereals, the reform of the procurement system to broaden the coverage of the flour price support system, the development of a new methodology for the establishment of support producer prices which should give a greater role to market mechanisms, and a change in import policy to ensure that it does not adversely affect the incentives to domestic production.

The progress in the reform of the subsidy system and in the implementation of the agricultural reforms mentioned above will be examined by the staff in the context of the second review of the program.

5. External policies and prospects

To achieve the current account targets, the main monetary and fiscal policies described above are being supplemented with a continuation of a flexible exchange rate policy. Improvements in the medium-term structure of the balance of payments will be aided by appropriate debt management, and by a continued liberalization of trade. Between end-December 1984 and end-May 1985 the nominal effective exchange rate, measured both vis-à-vis the currency basket and on a trade-weighted basis depreciated by 10 percent. This more than compensates for the further reduction from 10 percent to 7.5 percent in the special import tax in January 1985 and for the real appreciation of the dirham in the latter part of 1984. The export and import competing sectors will be helped by continued exchange rate flexibility in light of anticipated relative inflation so as to maintain through the rest of 1985 the improved competitiveness achieved so far. Exchange rate policy will be re-examined during each review in the light of the progress that will have been achieved in the balance of payments, taking into account the quarterly indicative targets for net foreign assets; the exchange rate policy for 1986 will be established in the context of the program for 1986. In addition, measures are being taken in the context of the World Bank ITPA II loan to streamline customs procedures for exporters and to reduce the number of both export and import items subject to licensing.

Total exports are projected to rise by 10.8 percent in SDR terms in 1985 and by a further 8.3 percent in 1986 (Table 9). SDR export prices are expected to rise on average by 1.8 percent each year, reflecting a small projected decline in the price of phosphate rocks and derivatives, and export volumes to grow by 9.1 percent in 1985 and 6.8 percent in 1986. Increased orders from Eastern Europe and Asia are expected to raise phosphate rock exports by 10.4 percent to 16,500 tons in 1985. Phosphoric acid and fertilizer export are also expected to expand by 10 percent in 1985 and 9 percent in 1986 as more capacity becomes available. Morocco's market share in phosphates and derivatives is projected to rise aided in part by relative cost advantages. The volume of finished manufactured goods, whose growth averaged 8 percent between 1980 and 1984, is projected to rise by 7.9 percent in 1985 and 10.5 percent in 1986 reflecting improved competitiveness.

Total imports in SDRs are projected to decline by 3.5 percent in 1985 and to increase slightly by 1.2 percent in 1986. With the adjustment measures designed to keep imports other than cereals, sugar and crude oil little changed between 1984 and 1986, the fall in imports in 1985 and the subsequent partial recovery is attributed to declines in these three categories of imports. Despite some improvement in rainfall and therefore in the cereal harvest, relative to 1984, cereal imports in 1985 are projected to be 2.2 million tons, compared to 2.7 million tons in 1984 and 1.9 million tons in 1983. The authorities also stated that crude oil imports could be kept to about 7 percent less than the 1984 figure which had reflected some restocking, and substitution for lower hydroelectric power.

The trade deficit is thus projected to be reduced by SDR 350 million in 1985 and a further SDR 155 million in 1986. A small overall improvement in the services and transfer accounts is achieved by a continued sharp growth of tourism, lower freight costs as imports fall, and increased workers' remittances (aided by interest rates and exchange rate policies) which offset the increase in scheduled interest payments on external debt. The current account deficit is, therefore, projected to decline to SDR 800 million (6.5 percent of GDP) in 1985 and SDR 544 billion (4.25 percent of projected GDP) in 1986. Preliminary external trade data for the first quarter of 1985 indicate a substantial decline in imports in SDR terms, by 7 percent, from the level in the first quarter of 1984, reflecting in particular a substantial drop in imports of cereals and of semi-finished products, as programmed. On the export side, exports of agricultural and manufactured products increased markedly in comparison in the first quarter of 1984; there was, however, a decline in the exports of phosphate derivatives due to some special factors, which are expected to be corrected in the ensuing months. Reflecting the performance of phosphate derivatives, total exports in SDR terms were 8 percent below the level of the first quarter of 1984.

Table 1. Morocco: Quantitative Performance Criteria for 1985

	1984	1985			
	Dec. Actual	March prelim.	July	Sept. Programmed	Dec.
(In millions of dirhams)					
Cumulative overall Treasury deficit	7,457	3,530	6,500 <u>1/</u>	8,600 <u>1/</u>	11,000 <u>1/</u>
Total domestic credit	55,532	57,533	59,600 <u>2/</u>	60,272 <u>2/</u>	61,122 <u>2/</u>
Bank credit to the Government	29,917	32,045	32,450 <u>2/</u>	32,617 <u>2/</u>	32,717 <u>2/</u>
Net outstanding " <u>fonds réservés</u> "	962	851	1,000	1,000	1,000
(In millions of U.S. dollars)					
New nonconcessional foreign borrowing with maturities of 1 to 15 years <u>3/</u>	263	...	500	500	500
Of which: with maturities of 1 to 5 years <u>4/</u>	160	...	(250)	(250)	(250)
Maximum outstanding short-term external credit <u>5/</u>	918	...	1,000	1,000	1,000
External payment arrears	62	42 <u>6/</u>	0	0	0

1/ Deficit before debt relief on interest payments. This limit will be reduced by the amount of the debt relief obtained on interest payments and the amount of external grants not used to reduce payment arrears.

2/ This limit will be reduced by the amount of external grants not used to reduce payment arrears and of possible increase in other net external resources.

3/ Contracted, guaranteed or approved by Government.

4/ These credits will be reduced by the equivalent of the amount of drawings on loans with maturities in excess of five years contracted directly by the Government on the international financial market.

5/ Credits contracted by the Government and public enterprises.

6/ At end-May.

Table 2. Morocco: Net External Assets of the Banking System

	1984		1985			
	December		March provis.	July	Sept. programmed	Dec.
	In millions of DH	In millions of SDR				
<u>A. Bank of Morocco</u>						
1. Gold holdings	125	13	13	13	13	13
2. Net foreign exchange holdings <u>1/</u> (international reserves)	315	34	113	57	122	168
Gross holdings	(467)	(50)	(138)	(73)	(198)	(184)
Liabilities	(-152)	(-16)	(-25)	(-16)	(-16)	(-16)
3. Net holdings of nonconvertible currencies	17	2	2	2	2	2
<u>B. Use of IMF credit</u>						
4. Net liabilities <u>2/</u>	...	-1,011	-1,091	-1,135	-1,136	-1,086
<u>C. Commercial banks</u>						
5. Net external assets	2,111	225	226	235	240	245
Total (A + B + C)	...	-737	-737	-828	-759	-657

1/ Holdings of convertible currencies, AMF subscription, SDR, less external liabilities in convertible currencies (excluding net liabilities to IMF).

2/ Based on proposed time-table drawings.