FOR INFORMATION

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To: Members of the Executive Board

From: The Secretary

Subject: **Morocco—Staff Note on Purchase Under the Precautionary and Liquidity Line Arrangement**

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Staff Note for Information of the Executive Board
Morocco—Purchase Under the Precautionary and Liquidity Line (PLL) Arrangement

1. On April 7, 2020, the Moroccan authorities purchased all available resources under the PLL arrangement (SDR2.15 billion or 240 percent of quota and about 3 percent of GDP) in order to replenish and bolster reserves and help preserve economic stability in the context of heightened uncertainties. In line with the PLL procedure, this note informs the Executive Board ex post about the purchase. It summarizes the recent developments in Morocco, describes the balance of payments need arising primarily from external and domestic shocks due to the Covid-19 pandemic, and discusses the economic outlook following the purchase. Staff's view is that the purchase is commensurate with Morocco's actual balance of payments need and that Morocco is in compliance with applicable conditions under the arrangement.

A. Recent Developments

2. The pandemic is severely affecting Morocco's economic activity and external position in 2020 (Table 1). Morocco had reported 735 confirmed cases of Covid-19 and 47 deaths as of April 3, 2020. Domestically, both demand and supply disruptions are observed following proactive measures to contain the outbreak in the country. The external shock has already led to sharp declines in export and tourism revenues, remittances, and capital inflows. Against this background, the dirham has depreciated by about 6 percent since end-February 2019 (staying within its recently widened fluctuation band).

3. In response, the authorities have relied on several policy levers. Following immediate containment efforts, an emergency committee chaired by the Minister of Finance was created to monitor the situation and coordinate policy actions. On the fiscal front, a new crisis fund of about 3 percent of GDP, financed by public and private contributions, will cover medical expenses and support businesses and households. On the monetary front, in addition to broadening the dirham's fluctuation band to +/-5 percent on March 6 (from +/-2.5 percent), Bank al-Maghrib (BAM) reduced the policy rate by 25 bp to 2.0 percent on March 19. While BAM has not intervened in the foreign exchange market since March 2018, official reserves declined from USD26.4 to 25.9 billion between end-2019 and March 27, due in part to increased foreign exchange provision to banks (including as a result of pressures on correspondent banking relationships). A range of measures were adopted to meet bank demand for liquidity and to support bank credit to affected sectors and SMEs, including partial and temporary relaxations of liquidity coverage (LCR) and capital conservation buffer requirements – in combination with increased public guarantees.

B. Balance of Payments Need and PLL Purchase

4. Official reserves are no longer considered an adequate buffer given the large and sudden shock that Morocco faces. The impact of the pandemic represents a more severe adverse scenario than the one underlying the request for the PLL arrangement in late 2018, and it likely entails heightened risks of pressures on Morocco's official reserves for the rest of this year. Morocco needs to strengthen official reserves to a level exceeding the threshold used to determine the PLL access level, which is 80 percent of the ARA metric.

5. Staff's view is that drawing on PLL resources in full is commensurate with Morocco's actual balance of payment needs (Table 2). Staff agrees with the authorities that such a drawing, combined with other new external financing already secured (including from the World Bank and other international institutions), will have a key role in weathering current external pressures and maintaining an adequate reserves buffer. After drawing on the PLL, Morocco would have adequate capacity to repay the Fund, while credit and liquidity risks to the Fund would remain low (Table 3). Fund obligations would represent only a small share of Morocco's total external debt (a maximum of 3.3 percent over the projection period), gross international reserves (4.7 percent), and exports (2.6 percent).

C. Outlook

6. For 2020, in a highly uncertain environment, staff expects a recession of about 4 percent, a current account deficit of about 8 percent of GDP, and lower-than-expected capital inflows. Domestically, growth will be handicapped by the temporary freeze in economic activity, while low precipitation will adversely impact agricultural output and depress growth further this year. On the external side, both imports and exports will be affected negatively, with tourism and remittances experiencing unprecedented declines. These projections take into account the temporary fiscal, monetary and financial sector policy responses announced to date, and remain subject to considerable uncertainty given the rapidly changing external and domestic circumstances.

7. Against this background, holding a robust reserves buffer will help Morocco preserve economic stability and growth. Following the purchase, Morocco's reserves will increase above 80 percent of the ARA metrics and external debt will remain sustainable. This will facilitate the ongoing policy efforts to contain the impact of the pandemic and will help preserve the gains achieved in recent years in strengthening the economy's resilience and growth potential. Assuming that a global growth recovery starts to materialize gradually in the second half of 2020, especially in key European partner countries, growth in Morocco could rebound to about 5 percent (aided by the agricultural recovery) and the current account deficit could narrow to about 4 percent of GDP in 2021. These projections are also subject to significant uncertainty and downside risks related to the shape and pace of the global economic recovery.

8. In light of the current uncertainties, the authorities intend to remain closely engaged with Fund staff. With the full purchase of available PLL resources, the PLL arrangement expired automatically. However, a close policy dialogue between the authorities and staff will be maintained. The authorities have expressed readiness to take further policy action, should the impact of the pandemic be more severe than expected.

Table 1. Morocco: Selected Economic Indicators, 2018–21

		Prelim.		Proj.		
		PLL 1/	Rev.	PLL 1/	Rev.	
	2018	2019		2020		2021
Output and Prices (Annual percentage change)						
Real GDP	3.0	2.8	2.2	3.7	-3.7	4.8
Real agriculture GDP	4.0	-2.8	-5.4	3.3	-3.0	7.0
Real non-agriculture GDP	2.9	3.4	3.2	3.7	-3.8	4.5
Consumer prices (period average)	1.9	0.4	0.0	1.2	0.3	1.3
Public Finances (In percent of GDP)						
Budget balance	-3.7	-4.0	-4.1	-3.8	-7.1	-4.5
Primary balance (excluding grants)	-1.7	-1.7	-1.8	-1.6	-4.8	-2.1
Cyclically-adjusted primary balance (excl. grants)	-1.4	-1.4	-1.5	-1.5	-3.4	-1.4
Total government debt	65.3	66.0	65.8	65.7	73.7	72.9
External Sector (In percent of GDP)						
Current account deficit	-5.3	-5.1	-4.1	-3.9	-7.8	-4.3
Total external debt	32.1	32.8	33.1	32.7	38.1	37.3
Gross reserves (in billions of U.S. dollars)	24.4	25.5	26.4	25.8	23.2	25.5
In percent of Fund reserve adequacy metric 2/	85.4	86.4	87.7	81.8	80.5	80.4

Sources: Moroccan authorities; and IMF staff estimates.

1/ Refers to the macro framework for the Second Review Under the PLL Arrangement in CR No. 20/14.

2/ Based on revised ARA weights.

Table 2. Morocco: External Financing Requirements and Sources, 2019–2021

Billions of USD (unless otherwise specified)

	2019	2020	2021
	Prelim.	Proj.	Proj.
Gross Financing Requirements	**60.8**	**55.3**	**64.2**
Imports of Goods and Services	54.9	49.6	58.6
FDI Payments	2.9	1.5	2.3
Interest Payments	0.9	0.9	0.9
of which Central Government and SOEs	0.9	0.9	0.9
Debt Amortization	2.2	3.4	2.5
of which Central Government and SOEs	2.2	3.4	2.5
Gross Financing Sources	**60.8**	**55.3**	**64.1**
Exports of Goods and Services	44.0	36.2	47.2
of which tourism receipts	8.2	4.1	8.6
Remittances	6.7	4.7	6.9
FDI Inflows	3.5	0.7	4.3
SOE borrowing	1.4	1.6	1.6
Grants	0.3	0.7	0.2
of which European Union	0.2	0.5	0.2
of which CCG	0.2	0.1	0.0
Private sector borrowing	1.6	1.2	1.5
of which trade credit	1.2	1.0	1.1
of which other	0.4	0.2	0.4
Central Government borrowing	2.6	3.2	2.8
of which markets	1.1	0.8	0.0
of which loans	1.5	2.4	2.8
of which Bilateral		0.5	
of which Multilateral		1.9	
Other inflows (net)	2.5	0.6	2.2
of which portfolio flows	1.2	0.9	1.6
Change in Reserves (-increase)	-2.0	3.4	-2.5
IMF Financing	**0.0**	**3.0**	**0.0**
GAP (Needs - Sources)	**0.0**	**0.0**	**0.0**
Memorandum items:			
Gross Official Reserves	26.41	20.12	22.45
Gross Official Reserves	26.41	23.01	25.49
Percent of ARA	87.70	80.50	80.40

Table 3. Morocco: Capacity to Repay Indicators, 2018–25 1/

	2018	2019	2020	2021	2022	2023	2024	2025
Exposure and repayments (in SDR million)								
GRA credit to Morocco	0.0	0.0	0.0	0.0	0.0	537.7	1,075.4	537.7
(In percent of quota)	0.0	0.0	0.0	0.0	0.0	60.1	120.2	60.1
Charges due on GRA credit	0.0	0.0	29.0	32.0	32.1	30.6	11.9	1.7
Principal due on GRA credit	0.0	0.0	0.0	0.0	0.0	537.7	1,075.4	537.7
Debt service due on GRA credit	0.0	0.0	29.0	32.0	32.1	568.3	1,087.3	539.4
Debt and debt service ratios								
In percent of GDP								
Total external debt	32.1	33.1	38.1	37.3	36.2	35.4	34.9	33.3
Public external debt	28.7	29.6	34.1	33.4	32.4	31.7	31.4	29.8
GRA credit to Morocco	0.0	0.0	0.0	0.0	0.0	0.6	1.0	0.5
Total external debt service	2.7	2.7	2.8	2.7	2.5	2.9	3.3	2.6
Public external debt service	1.7	1.7	1.8	1.7	1.5	2.0	2.4	1.7
Debt service due on GRA credit	0.0	0.0	0.0	0.0	0.0	0.6	1.1	0.5
In percent of gross international reserves								
Total external debt	154.8	148.6	217.0	203.0	190.7	175.7	157.8	145.7
Public external debt	138.4	133.0	194.2	181.6	170.5	157.4	141.6	130.5
GRA credit to Morocco	0.0	0.0	0.0	0.0	0.0	2.8	4.7	2.2
In percent of exports of goods and services								
Total external debt	113.4	117.7	131.0	136.7	140.2	144.2	149.5	151.6
Public external debt	101.5	105.4	117.2	122.3	125.3	129.1	134.0	135.7
GRA credit to Morocco	0.0	0.0	0.0	0.0	0.0	1.4	2.6	1.2
In percent of total external debt								
GRA credit to Morocco	0.0	0.0	0.0	0.0	0.0	0.9	1.7	0.8
In percent of public external debt								
GRA credit to Morocco	0.0	0.0	0.0	0.0	0.0	1.1	1.9	0.9
Memorandum items:								
Nominal GDP (in billions of U.S. dollars)	117.9	118.6	114.6	122.1	129.1	136.6	144.5	153.0
Gross international reserves (in billions of U.S. dollars)	24.4	26.4	20.1	22.4	24.5	27.5	32.0	34.9
Exports of goods and services (in billions of U.S. dollars)	43.2	44.0	36.2	47.2	51.7	55.6	59.2	63.1
Quota (in millions of SDRs)	894.4	894.4	894.4	894.4	894.4	894.4	894.4	894.4

Source: IMF staff estimates and projections.
1/ Upon approval of the second review of the PLL arrangement Morocco can draw up to 240 percent of quota. The Moroccan authorities have expressed their intention to treat the arrangement as precautionary, and the table presents the full drawing scenario.