EXECUTIVE BOARD MEETING

EBS/20/182
Correction 1

December 17, 2020

To: Members of the Executive Board

From: The Secretary

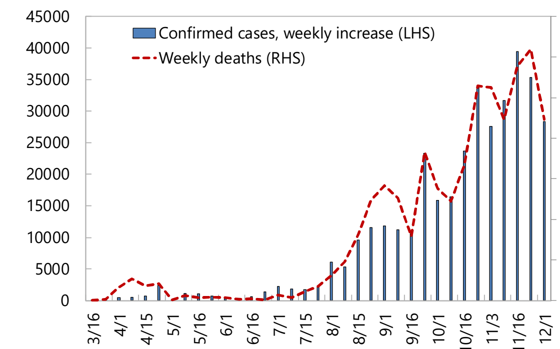
Subject: **Morocco—Staff Report for the 2020 Article IV Consultation and Proposal for Post-Program Monitoring**

Board Action:	The attached corrections to EBS/20/182 (12/4/20) have been provided by the staff:
Evident Ambiguity	**Page 24 (Figure 2, sources for charts)**
Factual Errors Not Affecting the Presentation of Staff's Analysis or Views	**Pages 6, 10, 11, 24 (Figure 2, second and third chart, data) 27, 31, 34**
Questions:	Mr. Cardarelli, MCD (ext. 38059) Mr. Queyranne, MCD (ext. 36297) Mr. Noah Ndela Ntsama, MCD (ext. 39772) Mr. Balima, MCD (ext. 37379)

ECONOMY HARD HIT DESPITE A SWIFT POLICY RESPONSE

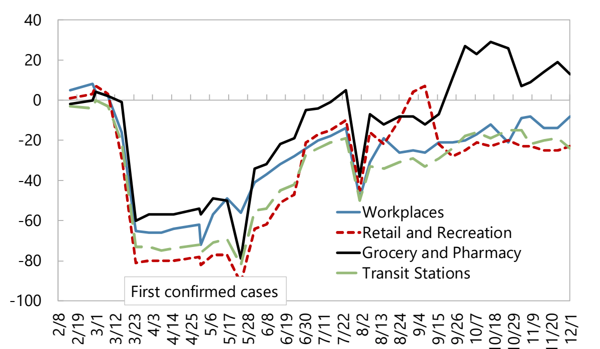
1. **Morocco managed to contain the pandemic in the first months of the outbreak but has experienced a resurgence of new infections since the summer.** In March, the authorities declared a state of health emergency and adopted stringent confinement measures. Partial reopening started in mid-June, with most businesses authorized to resume, domestic travel restrictions lifted, and international borders partially reopened. Since mid-July, however, the number of confirmed cases and deaths has increased significantly, mainly in large urban areas.[1] In response, the authorities reintroduced restrictions in a few large cities, and extended the state of health emergency till December 2020.

COVID-19 Confirmed Cases and Deaths
(Number of persons)



Source: Hale et al. (2020).

Google Mobility Trends
(Percentage change from baseline)



Source: COVID-19 Community Mobility Reports.

2. **Despite strong policy actions, the Moroccan economy has been heavily affected by the combined effects of the drought and the pandemic** (Figure 1). The authorities acted swiftly to mitigate the economic and social impact of the pandemic (Table 1). Still, the lack of rain affected agricultural output (the production of cereals fell by 39~~40~~ percent relative to last year), while the fall of external demand and the effect of domestic lockdown measures led to a significant contraction in non-agricultural output in Q2 (with sectors tied to tourism being the most affected). Economic slack caused a fall in inflation and the unemployment rate rose to 12.7 percent in Q3 from 9.4 percent last year, mostly driven by lower employment and despite a fall of the participation rate (of about 1½ percentage points). The pandemic is expected to impact disproportionately the most vulnerable, especially in high contact sectors (such as tourism and transportation), which also have a high degree of informality. The poverty rate is expected to increase to 6.6 percent in 2020 (from 4.8 percent in 2014), and vulnerability to poverty to 19.9 percent (from 17.1 percent last year).[2]

[1] As of December 2, Morocco has experienced 364,190 confirmed cases of COVID-19, with 5,985 deaths.

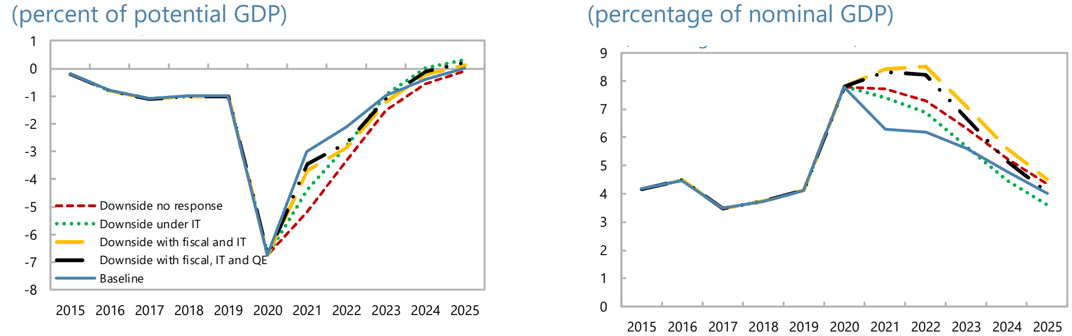
[2] HPC, UN, World Bank, "Impact social & économique de la crise du Covid-19 au Maroc, " July 2020.

further aggravating the decline in investment and raising concerns about the funding of government financing needs. A slower than expected pace in the implementation of structural reforms and the emergence of pandemic-driven social discontent could exacerbate those risks.

9. Further stimulus may be needed in case the downside risks on growth were to materialize. Staff simulated a downside scenario, in which a more prolonged duration of the health crisis would subtract about 3 percentage points to GDP growth next year (from 4½ percent in the baseline to 1½ percent). In such scenario, additional fiscal stimulus of about 1 percent of GDP would limit the additional damage to Morocco's economy and minimize the impact on the most vulnerable. The compression of non-essential current spending and measures to raise fiscal revenues would help limit the increase of public debt (which would peak at about 82 percent of GDP). Further cuts of the policy rate, a more depreciated Dirham under an inflation targeting (IT) monetary policy framework, and BAM purchases of Treasury bonds in secondary markets could also contribute to mitigating the impact of the shock on both the output gap and inflation. In staff's model, the combined fiscal and monetary policy responses would offset about half of the impact of the negative shock on GDP growth, allow a faster closure of the output gap and contribute to a quicker convergence of inflation to a long-term target of 2 percent.

Output Gap
(percent of potential GDP)

Overall Deficit
(percentage of nominal GDP)



Source: IMF staff.

Authorities' Views

10. The authorities emphasized the uncertainty around the forecasts. They viewed staff's baseline scenario as excessively pessimistic, given the signs that several important sectors of the Moroccan economy have begun to rebound starting in June. They expect growth ~~to be close to~~at -~~6~~ 5.8 percent in 2020, 4.8 percent in 2021 and above 4 percent thereafter, with a faster return to pre-crisis output levels thanks to the sizable recovery plan, the boost to investment, and a new generation of sectoral strategies (focusing on manufacturing and agriculture).

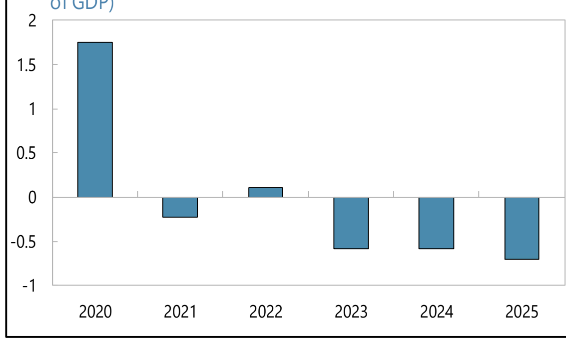
POLICY DISCUSSIONS: REBUILDING BUFFERS WHILE SUSTAINING THE RECOVERY

A. Fiscal Policy

11. The fiscal response to the crisis has been appropriate. For 2020, the authorities have let automatic stabilizers work on the revenue side and used the private and public sector contributions to the COVID-19 Fund to finance the increase in discretionary spending. While budget neutral, these spending measures have had a significant redistribution effect and are estimated to have contributed to growth by about 0.6 percent. Nonetheless, with the overall fiscal deficit at 7.7 percent of GDP and the debt-to-GDP ratio about 76.5 percent, staff sees Morocco's fiscal space to be at risk.

12. The 2021 Budget envisages a gradual reduction of the fiscal deficit. The overall fiscal deficit is expected to fall to 6.3 percent of GDP in 2021, maintaining the fiscal stimulus injected this year. The composition of the stimulus will shift to investment, both directly (through the Mohammed VI Investment Fund that will seek partnerships with the private sector to invest in infrastructure and small and medium enterprises—SME—development) and indirectly (though the large program of subsidized and state guaranteed credit).[3] Spending is also expected to increase (by about 0.5 percent of GDP) because of the extension of the public medical insurance scheme to self-employed and low-income people. Over the medium term, the overall fiscal deficit is expected to fall gradually to 4.8 percent of GDP by 2024, due to a significant increase in non-tax revenues (from the mobilization of the government real estate assets of about 4½ percent of GDP between 2021 and 2024), and gradual compression of the wage bill. Privatization receipts of about 1⅓ percent of GDP will reduce financing needs.[4] As a result, the debt-to-GDP ratio is expected to remain at around 77 percent, and gross financing needs at around 17 percent of GDP, over the next four years.

Fiscal impulse
(change in cyclically adjusted primary deficit; in percent of GDP)



13. Staff agrees that fiscal consolidation should be gradual and recommends starting it as soon as the recovery is established. In the short run, the priority is to sustain the fragile recovery and address the shortcomings in the social protection system exacerbated by the crisis. Over the medium and longer term the priority is to rebuild fiscal buffers and safeguard debt sustainability.

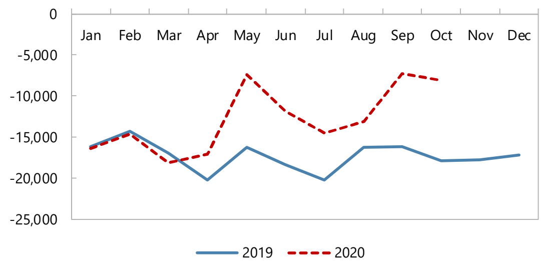
[3] The Mohammed VI Investment Fund, created in the 2020 supplementary budget, has been endowed with DH 15 billion (about 1.5 percent of GDP). The Fund is expected to develop into a private company, responsible for attracting private funding (with a target of DH 30 billion) and invest in infrastructure and the development of small private firms, including through participation in private equity funds.

[4] The authorities announced in late October 2018 a multi-year privatization program that started in 2019. After pausing this year, the program is expected to resume in 2021.

Figure 2. Morocco: External Developments

As both good exports and imports fell, the trade balance has improved so far in 2020 compared to last year.

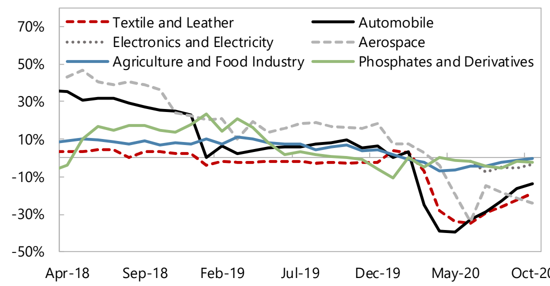
Trade Balance
(mil Dirhams)



Source: Haver.

Exports fell but are now showing signs of a recovery, particularly for automotive and textile sectors.

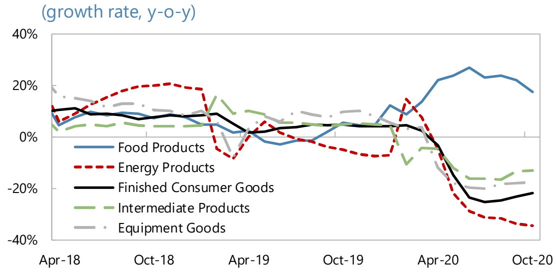
Goods Exports
(growth rate, y-o-y)



Sources: National authorities; and IMF staff estimates.

Imports fell across the board, except for food (also reflecting the loss in domestic agricultural production).

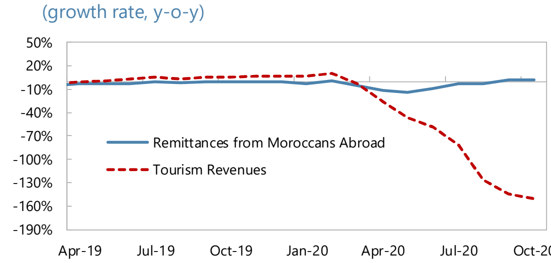
Goods Imports
(growth rate, y-o-y)



Sources: National authorities; and IMF staff estimates.

While tourism revenues have collapsed, remittances have been resilient.

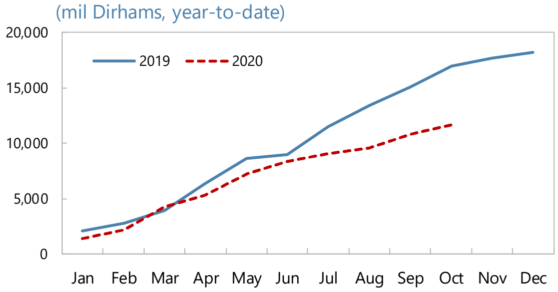
Tourism Revenues and Remittances
(growth rate, y-o-y)



Source: Haver.

Net FDI have been resilient, as the decline of Moroccan investment abroad more than offset lower inward FDIs.

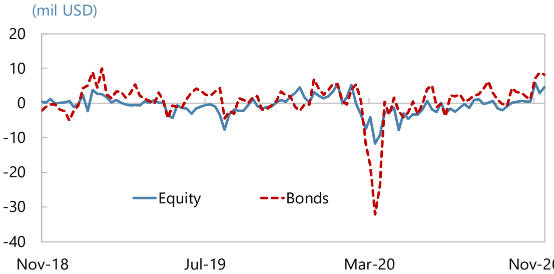
Net FDI
(mil Dirhams, year-to-date)



Sources: National authorities; and IMF staff estimates.

Portfolio flows experienced a sharp decline at the onset of the pandemic but recovered recently (particularly bonds).

Morocco: ETFs/Mutual Funds, Flows
(mil USD)



Sources: National authorities; and IMF staff estimates.

Table 1. Morocco: Selected Economic Indicators, 2016–25

					Pre-COVID	Proj.					
	2016	2017	2018	2019	*2020*	2020	2021	2022	2023	2024	2025
					(Annual percentage change)						
Output and Prices											
Real GDP	1.1	4.2	3.1	2.5	*3.7*	-7.2	4.5	3.9	3.6	3.7	3.7
Real agriculture GDP	-13.7	15.2	3.7	-5.8	*3.3*	-5.0	7.0	3.9	4.0	4.1	4.2
Real non-agriculture GDP	3.0	2.9	3.1	3.5	*3.7*	-7.5	4.2	3.9	3.6	3.6	3.7
Consumer prices (end of period)	1.7	1.7	0.2	1.1	*1.2*	0.2	0.8	1.2	1.6	1.8	2.0
Consumer prices (period average)	1.5	0.7	1.6	0.2	*1.2*	0.2	0.8	1.2	1.6	1.8	2.0
Output gap (percentage points of non-agricultural GDP)	-0.8	-1.1	-1.0	-1.0	*-0.4*	-7.0	-3.0	-2.1	-1.0	-0.4	0.0
Unemployment rate (in percent)	9.9	10.2	9.5	9.2	…	…	…	…	…	…	…
					(In percent of GDP)						
Investment and Saving											
Gross capital formation	32.4	32.6	33.4	32.2	*32.9*	28.1	28.5	28.9	29.4	29.5	29.6
Of which: Nongovernment	26.7	27.2	28.2	27.6	*28.7*	23.1	23.7	23.7	23.9	24.0	24.1
Gross national savings	28.3	29.2	28.1	28.1	*29.1*	22.0	23.1	24.1	25.1	25.1	25.9
Of which: Nongovernment	32.8	32.7	31.9	32.2	*26.7*	29.7	29.4	30.4	30.7	30.0	29.1
					(In percent of GDP)						
Public Finances											
Revenue	26.1	26.6	26.1	25.6	*26.2*	26.9	26.2	26.4	26.6	26.8	27.2
Expenditure	30.5	30.1	29.9	29.7	*29.9*	34.6	32.6	32.7	32.2	31.7	31.3
Budget balance	-4.5	-3.5	-3.7	-4.1	*-3.8*	-7.7	-6.3	-6.2	-5.6	-4.8	-4.0
Primary balance (excluding grants)	-2.7	-2.0	-1.7	-1.8	*-1.6*	-5.5	-3.9	-3.7	-2.8	-2.1	-1.2
Cyclically-adjusted primary balance (excl. grants)	-2.5	-1.7	-1.4	-1.5	*-1.5*	-3.2	-3.0	-3.1	-2.5	-1.9	-1.2
Total government debt	64.9	65.1	65.2	65.0	*65.7*	76.5	76.9	77.3	77.7	77.3	76.6
					(Annual percentage change; unless otherwise indicated)						
Monetary Sector											
Claims to the economy	5.9	3.3	3.4	5.4		…	…	…	…	…	…
Broad money	4.7	5.5	4.1	3.7		…	…	…	…	…	…
Velocity of broad money	0.8	0.8	0.8	0.8		…	…	…	…	…	…
					(In percent of GDP; unless otherwise indicated)						
External Sector											
Exports of goods and services (in U.S. dollars, percentage chang	3.3	12.7	11.6	1.8	*6.9*	-23.8	18.1	9.4	7.3	6.1	7.4
Imports of goods and services (in U.S. dollars, percentage chang	9.5	9.3	12.2	-1.0	*3.3*	-15.2	13.3	6.9	5.5	5.7	5.9
Merchandise trade balance	-17.1	-16.5	-17.2	-16.7	*-15.6*	-14.6	-15.1	-14.8	-14.6	-14.6	-14.6
Current account excluding official transfers	-5.0	-4.5	-5.6	-4.3	*-4.2*	-6.7	-5.8	-5.1	-4.6	-4.5	-3.8
Current account including official transfers	-4.1	-3.4	-5.3	-4.1	*-3.9*	-6.0	-5.4	-4.8	-4.3	-4.4	-3.7
Foreign direct investment	1.5	1.5	2.4	0.5	*1.6*	1.2	1.1	1.3	1.4	1.4	1.5
Total external debt	33.7	35.0	32.0	32.8	*32.7*	39.7	39.3	39.3	39.9	39.0	39.1
Gross reserves (in billions of U.S. dollars)	25.1	26.2	24.4	26.4	*25.8*	32.0	32.3	33.1	33.8	35.2	38.8
In months of next year imports of goods and services	6.1	5.7	5.3	6.8	*5.0*	7.3	6.9	6.7	6.5	6.3	6.9
In percent of Fund reserve adequacy metric 1/	98.6	92.3	85.4	87.7	*81.8*	99.5	92.7	90.3	86.7	85.7	88.9
In percent of CA deficit and ST debt at rem. mat. basis	404.8	439.0	287.3	361.9	*359.6*	346.7	353.6	388.9	412.7	412.2	494.8
Memorandum Items:											
Nominal GDP (in billions of U.S. dollars)	103.31	109.7	118.1	119.7	*123.6*	113.0	124.2	131.1	138.2	145.7	153.8
Nominal GDP per capita (in U.S. dollars, percent change)	1.0	5.1	6.5	0.3	*3.6*	-6.5	8.8	4.6	4.4	4.4	4.6
Population (millions)	34.5	34.9	35.2	35.6	*36.0*	36.0	36.3	36.7	37.0	37.4	37.7
Population growth (in percent)	1.06	1.06	1.06	1.04	*1.03*	1.03	1.00	0.98	0.96	0.94	0.92
Net imports of energy products (in billions of U.S. dollars)	-5.6	-7.2	-8.8	-7.9	*-7.7*	-3.9	-5.0	-5.1	-5.2	-5.6	-5.9
Local currency per U.S. dollar (period average)	9.8	9.7	9.4	9.6	…	…	…	…	…	…	…
Real effective exchange rate (annual average, percent change, depreciation -)	2.1	-0.4	0.9	0.5	…	…	…	…	…	…	…
Interest rate (money market rate, end of period, in percent)	2.30	2.32	2.32	2.26	…	…	…	…	…	…	…

Sources: Ministry of Economy and Finance; and IMF staff estimates.
1/ Based on revised ARA weights.

Table 5. Morocco: Monetary Survey, 2016–20

	2016	2017	2018	2019	2020-proj.
			(Billions of dirhams)		
Net foreign assets	247.4	268.6	256.3	265.7	275.0
Net domestic assets	961.0	1,006.8	1,070.4	1,124.1	1,208.5
Domestic claims	1,100.0	1,157.3	1,225.9	1,292.3	1,369.0
Net claims on the government	142.4	167.8	203.0	212.4	254.0
Bank Al-Maghrib	-0.3	0.2	0.8	0.6	0.8
Of which: deposits	-4.9	-3.9	-2.9	-3.3	-3.1
Deposit money banks	142.6	167.6	202.2	211.9	253.2
Claims to the economy	957.6	989.5	1,022.9	1,078.5	1,115.0
Other liabilities, net	-139.0	-150.5	-155.5	-168.5	-160.5
Broad money	1,202.4	1,269.1	1,320.6	1,370.5	1,439.6
Money	751.9	811.0	858.7	911.8	1,000.8
Currency outside banks	203.2	218.8	233.6	250.2	303.6
Demand deposits	548.6	592.2	625.1	661.6	697.2
Quasi money	407.3	417.0	424.5	416.6	395.2
Foreign deposits	43.2	41.1	37.4	42.0	43.7
			(Annual percentage change)		
Net foreign assets	7.4	8.5	-4.6	3.8	3.8
Net domestic assets	4.0	4.8	6.3	5.0	7.5
Domestic ~~credit~~ claims	4.6	5.2	5.9	5.4	5.9
Net claims on the government	-3.8	17.8	21.0	4.6	18.4
Claims to the economy	5.9	3.3	3.4	5.4	3.4
Banking credit	4.2	3.1	3.2	5.3	3.4
Broad money	4.7	5.5	4.1	3.8	5.1
			(Change in percent of broad money)		
Net foreign assets	1.5	1.8	-1.0	0.7	0.7
Domestic ~~credit~~ claims	4.2	4.8	5.4	3.9	5.6
Net claims on the government	-0.5	2.1	2.8	0.7	2.9
Claims to the economy	4.7	2.7	2.6	4.1	2.7
Memorandum items:					
Velocity (GDP/M3)	0.84	0.84	0.84	0.84	0.75
Velocity (non-agr. GDP/M3)	0.75	0.74	0.75	0.75	0.66
Claims to economy/GDP (in percent)	94.5	93.1	92.3	93.7	103.9
Claims to economy/nonagricultural GDP (in percent)	106.1	104.9	103.9	105.5	117.5

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

Table 8. Morocco: FSAP Key Recommendations—Status as of October 2020

Recommendations		Priority [1/]	Implementation Status
Banking Regulation and Oversight			
Address banking supervisor's capacity constraints; strengthen on-site supervision capacity.		I	In progress. Internal reorganization implemented and increase of effectives to respond to on site supervision.
Review loan classification and provisioning rules on a solo basis; conduct an impact study for implementing the relevant IFRS9 in coordination with tax authorities.		NT	On a consolidated basis, IFRS 9 was adopted by Moroccan banks on January 1, 2018. Bank Al-Maghrib (BAM) conducted the impact studies of this standard before implementation and adopted, on this basis, a transitional arrangement for the prudential impact on regulatory capital in line with Basel Committee provisions. On a solo basis, the loans classification and provisioning rules have been finalized and should be published after the validation of the National Council of Accountancy.
Advance recovery & resolution plans; more frequent comprehensive assessments for SIFIs		I/NT	The R&R circular was examined by the CEC in July 2017 and communicated to banks for their implementation. Following the adoption of BAM circular in Q3 2017, three systemic banks submitted to BAM during Q4 2018 their first recovery plans. The remaining banks have submitted their first recovery plans in 2020.
Macro Prudential Oversight			
Amend laws governing regulators for capital markets, and insurance and pensions to include financial stability objective.		I/NT	In progress. Legal framework addressing overlap among various regulatory bodies being designed. The opportunity to integrate the amendment of capital market and insurance laws within a more comprehensive reform is being assessed. Work in progress and expected to finalize by 2022.
Implementation of countercyclical capital buffer (CCB); expand data coverage for the risk map; include more targeted sectoral instruments.	Expand data coverage for the risk map	NT	Risk mapping reviewed in first semester 2017 and consist of six risk pillars. A new pillar dedicated to payment systems and market infrastructures was introduced. Work is underway to introduce the emerging risks related to FinTech, cyber risk, and green finance. The data coverage has been extended in many ways but still work to be done : (i) **sample to monitor non-financial firms indebtedness** has been improved, in terms of quality and representativeness of the Moroccan economy, from 1684 to 72100 public and private non-financial enterprises; (ii) **data for real estate risks** (to calculate LTV (loan-to-value) has been collected from Property registry Agency; (iii) **Sample to monitor Household sector** has been improved, in terms of quality and representativeness, from 182471 to ~~265084~~ more than 400000 borrowers. The ongoing work aims to set a dedicated survey to this matter.
	Implementation of new specific macroprudential instruments		**Capital overload for systemically important banks**: The methodology for the identification of Domestic Systemically Important Banks (D-SIB) as well as the calibration approach of the capital surcharge applicable to them were put in place and approved by the financial stability committee in December 2017. Already identified the three largest systemic banks. Calibration still in process for identifying the systemic largest conglomerates. **LTV Cap**: data requirements are being introduced to collect data for calculating LTV. IMF technical assistance took place in late April 2019.

[1/] "I-Immediate" is within one year; "NT-near-term" is one to three years; "MT-medium-term" is three to five years.