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MOROCCO

August 2014

REQUEST FOR AN ARRANGEMENT UNDER THE PRECAUTIONARY AND LIQUIDITY LINE AND CANCELLATION OF THE CURRENT ARRANGEMENT—STAFF REPORT; PRESS RELEASE AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR MOROCCO

In the context of the request for an arrangement under the Precautionary and Liquidity Line and cancellation of the current arrangement, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on July 28, 2014, following discussions that ended on June 18, 2014, with the officials of Morocco on economic developments and policies underpinning the IMF arrangement under the Precautionary and Liquidity Line. Based on information available at the time of these discussions, the staff report was completed on July 11, 2014.
- An **Assessment of the Impact of the Proposed Precautionary and Liquidity Line Arrangement on the Fund's Finances and Liquidity Position**.
- A **Press Release** including a statement by the Chair of the Executive Board.
- A **Statement by the Executive Director** for Morocco.

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INTERNATIONAL MONETARY FUND

MOROCCO

July 11, 2014

REQUEST FOR AN ARRANGEMENT UNDER THE PRECAUTIONARY AND LIQUIDITY LINE AND CANCELLATION OF THE CURRENT ARRANGEMENT

EXECUTIVE SUMMARY

Morocco's economic track record was challenged in recent years by a series of exogenous shocks, to which the authorities responded vigorously. Facing a difficult international environment, the authorities adopted, with the support of the Fund's Precautionary and Liquidity Line (PLL), a policy program aimed at restoring fiscal and external buffers while strengthening competitiveness and promoting higher and more inclusive growth. The program remained broadly on track and the authorities did not draw on the PLL.

The outlook is improving but remains subject to significant downside risks. Growth will slow in 2014, but it is expected to accelerate over the medium term owing to structural reforms and improved global conditions. However, this outlook remains subject to major external risks. A protracted period of slower growth in Europe, a surge in global financial market volatility linked to the exit from unconventional monetary policies in large advanced economies, and higher oil prices resulting from geopolitical tensions could significantly degrade the balance of payments.

The authorities are requesting a two-year successor PLL arrangement with a lower access (550 percent of quota) than the first arrangement. The current PLL has provided useful insurance against external risks while anchoring the authorities' reform agenda and sending positive signals to markets. Given significant global risks, a successor arrangement, which the authorities intend to treat as precautionary, would continue to support their policies. The lower access reflects the strengthening of the economy in the past two years as well as a balance of risks lower than two years ago.

Staff considers that Morocco continues to qualify for a PLL arrangement and recommends the approval of the authorities' request. The proposed arrangement carries low risks to the Fund and would have minimal impact on the Fund's liquidity were the authorities to draw on the full amount available. The authorities' policy package provides reasonable prospects of exit at the end of this arrangement if external circumstances warrant.

Approved By
Adnan Mazarei and Mark Flanagan

The staff team consisted of Mr. Dauphin (head), Ms. Garcia Martinez, Messrs. Kalonji and Versailles (all MCD); and Mr. Ahokpossi (SPR). The discussions took place in Rabat, June 11-18, 2014.

The mission met the Minister of Economy and Finance Mr. Boussaïd, the Minister of Labor and Social Affairs Mr. Seddiki, the Minister Delegate of the Budget, Mr. Azami Al Idrissi, the Minister Delegate of General Affairs and Governance Mr. Louafa, Governor of the Central Bank Mr. Jouahri, and other senior officials and representatives of the private sector and civil society. Mr. Dairi (OED) participated in most of the meetings.

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CONTEXT

1. **Morocco's economic track record was challenged in recent years by a series of exogenous shocks**. After a decade of strong economic performance, high international oil prices, the crisis in Europe, and the transition in Arab countries took a toll on macroeconomic balances. Both fiscal and external deficits widened significantly in 2011–12 while growth suffered from low agricultural output. Inflation remained low. Unemployment has been high, particularly among the youth. Despite some progress over the past decade, more is needed to reduce poverty, which remains pervasive.[1]

2. **Supported by a Precautionary and Liquidity Line (PLL) arrangement, the authorities adopted an ambitious program to reduce vulnerabilities while addressing medium-term challenges.** The Executive Board approved a 24-month PLL arrangement on August 3, 2012 in the amount of SDR 4.1 billion (700 percent of quota, about US$6.2 billion). The program aimed at restoring fiscal and external buffers, mainly through fiscal consolidation, while pursuing structural reform to strengthen competitiveness and promote higher and more inclusive growth. The program remained broadly on track throughout its implementation, and the Board completed the third and last review on January 31, 2014. The authorities have treated the PLL as precautionary and did not draw on the line despite a more challenging external environment than anticipated at the inception of the arrangement.

3. **As this PLL comes to an end, the authorities have requested a successor two-year arrangement, which they intend to treat as precautionary.** The authorities consider that the PLL has served them well, providing useful insurance against external risks, anchoring their program of reforms, and sending positive signal to markets.[2] In light of this experience, and in an external environment that remains subject to significant downward risks, they consider that a successor arrangement would usefully continue to support their program and provide important insurance against external risks. In particular, the economy would be significantly affected by a protracted period of slower growth in Europe, heightened financial market volatility linked to the exit from unconventional monetary policy, and a surge in oil prices resulting from geopolitical risks. The authorities wish to cancel the current arrangement upon approval of the new one.

RECENT DEVELOPMENTS

4. **A new ruling coalition led by the Justice and Development Party (PJD) was formed in October 2013.** The previous coalition, also headed by the PJD, a moderate Islamist party, ended in

[1] For an overview of social indicators, see "Inclusive Growth in Morocco: Stylized Facts and Policies" (CR/13/110).

[2] For instance, at end-April 2014, Fitch reaffirmed Morocco's sovereign ratings and stated that the program had been a strong anchor for the reform dynamics and noted that a potential continuing IMF involvement should support further reforms.

the summer 2013 when the junior party Istiqlal withdrew from it. The center-right National Rally of Independents (RNI) replaced Istiqlal after protracted negotiations, ending a period of uncertainty that had delayed policymaking and affected consumer and investor confidence. Since the formation of the new coalition, the pace of reforms has picked up significantly. Local elections are expected mid-2015 and parliamentary elections in 2016.

5. Growth has slowed, reflecting the weak external demand and a return to normal of agricultural production after an exceptional 2013. Overall growth was 4.4 percent in 2013, as a bumper crop pushed agricultural growth close to 20 percent. Non-agricultural growth slowed to 2.3 percent from an average of 4.5 percent over the past 10 years, mostly reflecting the weak European economy. In the first quarter of 2014, total growth further decelerated to 1.7 percent (year-on-year), pushed down by a return to normal cereal yields. Nonetheless, leading conjonctural indicators point to an acceleration of activity as confidence returns and external demand rebounds. Inflation remained low in 2013, averaging about 2 percent despite the increase in the prices of some subsidized energy products. Through the first five months of 2014, inflation stayed low at 0.4 percent year-on-year, as a result of a contraction in food prices (-1.2 percent) while core inflation was about 1½ percent. Unemployment in the first quarter of 2014 increased to 10.2 percent from 9.2 percent in 2013, remaining particularly high among the youth.

6. Fiscal performance so far in 2014 remains consistent with achieving further reduction in the deficit. The fiscal deficit was significantly reduced from a peak of 7.4 percent of GDP in 2012 to 5.5 percent of GDP in 2013, through expenditure cuts. During the first five months of 2014, tax revenue was in line with projections based on observed past years' seasonality, reaching about 40 percent of the annual target (about 9 percent of GDP). Grants and nontax revenue were slightly lower than expected, but these typically do not follow a regular seasonal pattern. Expenditure performance over the period was mixed. Wage expenditure was at the expected level (about 5¼ percent of GDP) and subsidy outlays decreased by 7½ percent compared to the same period last year, as the government's efforts in this area bore fruit. However, spending on goods and services and grants reached about 46 percent of the annual projection as the authorities accelerated transfers to public entities at the beginning of the year, affecting the infra-annual pattern of spending within the year, but not the overall annual envelope, which, by law, is a binding ceiling. Capital spending reached 46 percent of the annual target during the first five months of 2014. This reflected in part a decision to reduce the grace period for carrying over unspent credits from the previous year as a way to improve spending programming throughout the year, but it is not expected to affect total capital spending. The authorities continue to closely monitor budget execution. In particular, the two committees that were set up in 2013 following the 2012 higher-than-projected fiscal deficit continue to meet regularly.[3] Separately, on May 1, 2014, the authorities

[3] These were a committee chaired by the Minister of Economy and Finance to closely monitor budget execution and a committee to better align transfers to public entities with their cash-flow needs and the overall fiscal objective.

announced that the minimum wage for public servants will be raised by 200 dirham (an increase of about 7 percent).[4]

7. Reserves increased sharply in recent months. The current account balance improved by 2 percent of GDP in 2013, thanks largely to a lower trade deficit. Together with sizeable foreign direct investment (FDI), this helped stabilize international reserves above four months of imports. Through May 2014, and relative to the same period in 2013, exports grew by 7.5 percent notwithstanding a significant decline in phosphate exports, owing to the strong performance of exports from newly developed industries (e.g., cars and aeronautics). Imports grew by 4.0 percent, reflecting higher imports of food (wheat) and fuel products. As a result, the trade deficit increased by 0.8 percent. At the same time, lower remittances were more than offset by higher tourism receipts. FDI declined in January–May 2014 compared to the same period last year when it was exceptionally boosted by foreign acquisitions of domestic companies. The reserve position improved sharply since the issuance of US$1.8 billion Eurobonds in the international financial market by the state-owned phosphate office (OCP) in April and May and a €1 billion sovereign issuance in June. As of June 20, reserves were US$22.4 billion, equivalent to 4.8 months of imports of goods and services or 97 percent of the Fund's Assessing Reserves Adequacy (ARA) metric.[5]

8. The central bank (BAM) has left its policy rate unchanged at 3 percent since March 2012, in consideration of the weak external demand and the potential inflationary impact of the subsidy reform. Liquidity conditions improved and, consequently, BAM's interventions decreased. During the first quarter of 2014, liquidity conditions improved following the cut from 4 percent to 2 percent in the required reserve ratio in March 2014 and BAM liquidity advances at 7 days declined to 39 billion dirham on daily average in 2014Q2 from 52 billion dirham in 2014Q1. BAM has also continued with the implementation of measures to facilitate access to finance to very small, small and medium enterprises.[6] Liquidity further improved in the second quarter of 2014 following the increase in international reserves.

9. Credit growth has accelerated slightly, while nonperforming loans (NPLs) remain on the rise. Credit to the economy grew at 4.4 percent year-on-year in April 2014, up from 3.9 percent at end-December 2013. This acceleration was in all categories of credit except real estate. Reflecting the slowdown in activity, NPLs increased to 6.4 percent of total loans in April 2014 from 5.9 percent in December 2013 but remain adequately provisioned. Lending rates decreased by 56 basis points to 5.96 percent, reflecting a decline in the rate of cash advances for companies.

10. The authorities have steadily moved ahead with their fiscal reform agenda. Significant progress has been made recently on several fiscal fronts:

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[4] The 2014 increase will be paid retroactively in 2015 and its impact on public wage expenditure will be minimal as the full-year fiscal impact of the measure will be about 0.02 percent of GDP.

[5] Using 2014 data for the ARA metric variables.

[6] See the 2013 Article IV report, paragraph 31 (CR/14/65).

- *Organic budget law* (OBL). A draft new OBL was adopted by the first chamber of Parliament on July 8, 2014 and is now being discussed by the economic and financial commission of the second chamber. As described below, the draft new law introduces welcome improvements over the current law.

- *Subsidies*. The authorities eliminated subsidies on gasoline and industrial fuel in February, and on the fuel used for electricity production in June. To compensate for the higher fuel cost, the authorities have entered a program contract with the public electricity company (ONEE) that includes direct cash transfers during the next four years as well as measures to improve the financial viability of the company, notably through a revision of electricity tariffs. The authorities began implementing quarterly reductions of the per-unit subsidy on diesel at the beginning of the year.

- *Pension*. A parametric reform of the main public pension fund was announced to social partners on June 18, during a high-level meeting chaired by the head of government. The goal is to finalize the details of the parametric changes with social partners in the coming weeks and make the necessary legal changes so the reform can enter into force in 2015.

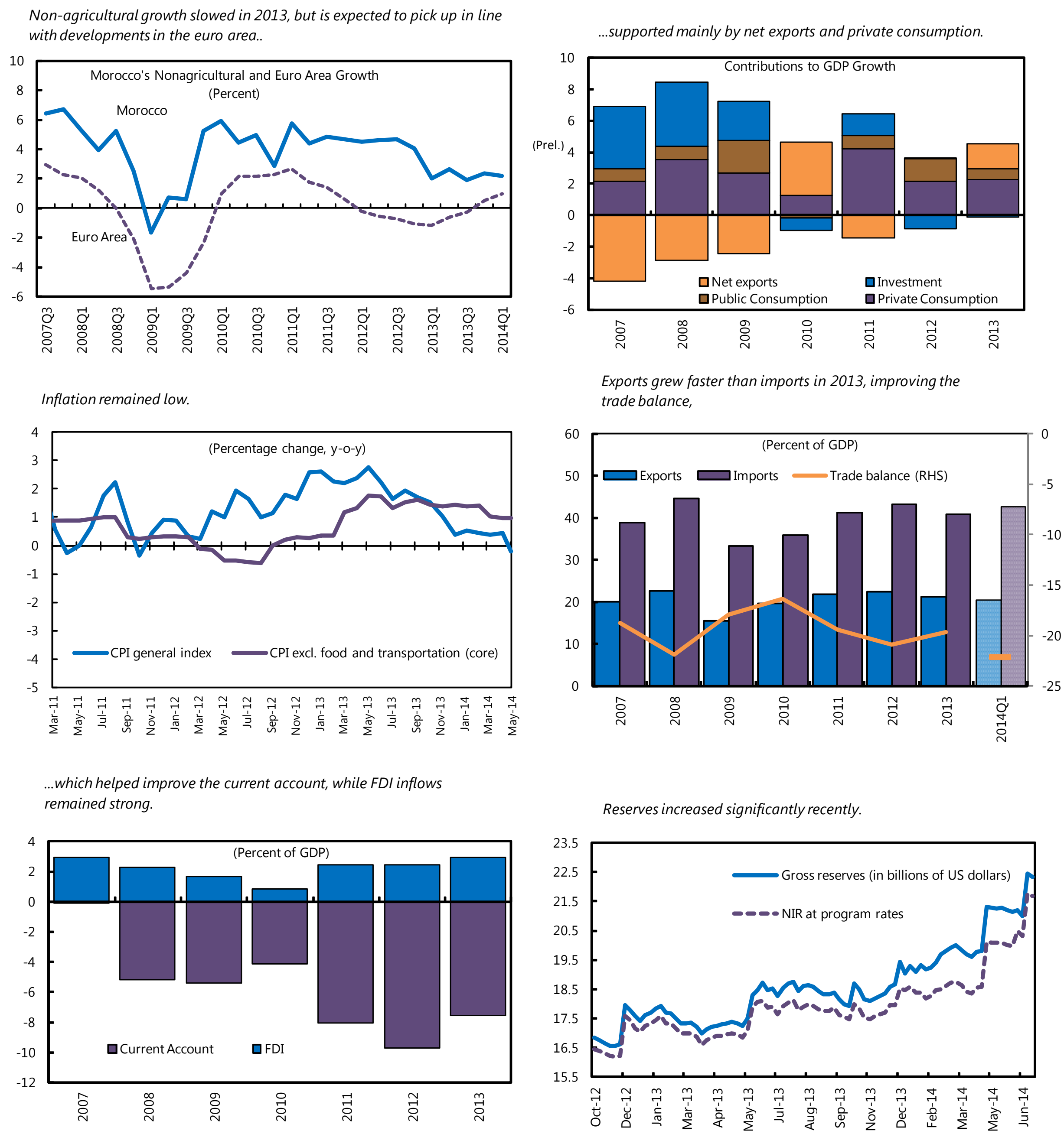
- *Tax*. In addition, the authorities have started implementing changes aimed at making the fiscal system more equitable and more supportive of competitiveness. Measures introduced in 2014 include the removal of tax exemptions on large agricultural firms and the progressive reduction in the number of VAT rates as well as an acceleration of VAT reimbursements to help improve the cash flow of enterprises.

OUTLOOK AND RISKS

11. Growth in 2014 will be lower than in 2013, but is expected to pick up in the medium term. Following a bumper crop in 2013, agricultural growth is projected to be negative in 2014 as cereal production returns to normal. Non-agricultural growth is expected to accelerate, supported by stronger domestic demand, improving growth prospects in Europe, and continued strong performance of the new industries. Overall growth should thus reach about 3½ percent in 2014. Despite some increases in energy prices, inflation is expected to remain low at about 1 percent on average. Over the medium term, the impact of past plans to develop new sectors, the expansion of Morocco's companies to new markets (e.g., sub-Saharan Africa), the effect of structural reforms, and an overall improvement in global conditions are expected to lift potential growth to about 5½ percent.

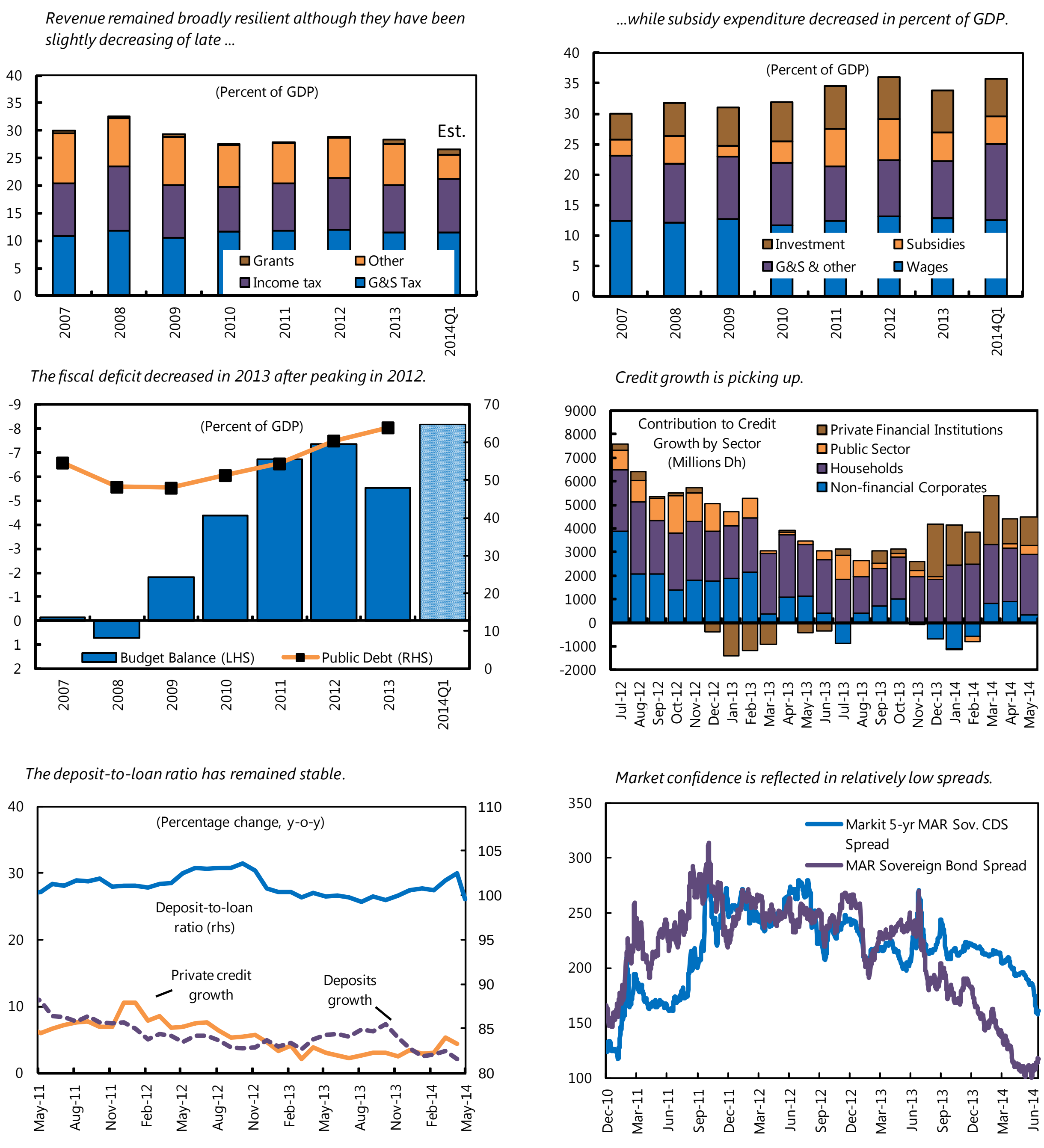
12. The fiscal deficit is expected to narrow further in 2014 through expenditure containment. The 2014 budget targets a reduction of about half a percent of GDP in the overall fiscal deficit to 4.9 percent of GDP. This reduction hinges on lower spending on subsidies that result from measures taken during the year. The reduction in the deficit will also be supported by a rationalization of capital spending. Revenue performance is expected to be slightly weaker than in 2013, due to the effects on income and profits taxes of the slowdown in non-agricultural GDP.

Figure 1. Morocco: Real and External Developments



Sources: Moroccan authorities; and IMF staff estimates.

Figure 2. Morocco: Fiscal and Financial Market Developments



Sources: Moroccan authorities; and IMF staff estimates.

13. The current account balance is expected to continue improving. As a result of the reduction in the fiscal deficit, improving external demand, lower global energy prices, and the rapid development of exports from newly developed sectors, the current account deficit is expected to further decline below 7 percent of GDP in 2014. Reserves are projected to increase by close to US$2 billion in 2014 and end the year around 4.5 months of imports or 91 percent of ARA metric.[7] They are projected to gradually increase above 100 percent of the ARA metric over the medium term.

14. The outlook remains subject to significant downside risks. A protracted period of slower growth in trading partners from advanced economies, especially in the euro area, could affect growth and the balance of payments. A surge in global financial market volatility, related to the exit from unconventional monetary policies in large advanced economies, could hamper access to international capital markets and indirectly affect FDI. Geopolitical risks in the Middle East, as well as in Ukraine/Russia could trigger commodity price volatility, and higher oil prices in particular, which would negatively affect both the current account and fiscal deficits. Pressing social demands may slow implementation of the necessary reforms. On the upside, better-than-assumed agriculture production would have a positive effect on growth and the current account.

ECONOMIC POLICIES

15. The authorities' economic program aims to continue reducing external and fiscal vulnerabilities while fostering higher and more inclusive growth. In line with their current program, the authorities' policy package relies on fiscal consolidation supported by fiscal policy reforms and a strengthening of the fiscal framework, sound monetary and financial policies, and structural reforms to boost competitiveness, growth and employment (see the authorities' written communication (W-COM.), ¶3, attached).

A. Fiscal Policy

16. The authorities are committed to achieving a fiscal deficit target of 3 percent of GDP by 2017, while preserving growth (W-COM.-¶4). The reduction in the fiscal deficit targeted for 2014 is in line with the medium-term target. Between 2015 and 2017, the cyclically adjusted primary deficit would be almost halved from 2.6 percent to 1.4 percent of GDP and close to zero percent by 2019. Such a primary balance path is consistent with putting the public debt-to-GDP ratio on a downward path after its expected peak in 2015 so it is gradually reduced closer to 60 percent of GDP by 2019. Revenue is expected to remain broadly stable in percent of GDP. Fiscal adjustment will thus continue to come from expenditure rationalization, notably the reduction in the subsidy bill and the gradual moderation of the public payroll, while space is made for higher pro-growth spending on investment in infrastructure and human capital, including social protection programs.

[7] A reduction in reserves from their June 2014 level is anticipated, as their spike in May-June reflect one-off financing operations. In addition, the profile of short-term liabilities suggests these would pick up in the third quarter.

As noted in paragraph 6, the fiscal outturn through end-April suggests that the annual fiscal deficit objective for 2014 is achievable. As they did in 2013, the authorities are committed to reducing nonpriority spending as needed, should revenue or expenditure developments warrant adjustment in the course of the year to meet the deficit target.

17. The authorities are reforming the tax system following the recommendations of their national tax conference in April 2013 (W-COM.-¶5). The strategy is not intended to increase tax revenues, which are already among the highest in the region, but to widen the tax base and contain high tax expenditures. The authorities intend to make the tax system fairer and more supportive of competitiveness. The 2014 budget introduced measures in that direction, notably by starting to remove tax exemptions on large agricultural firms and to reform the VAT regime. It also introduced measures to better enforce tax payments by self-employed and liberal professions. The authorities intend to continue implementing the national tax conference's action plan through the 2015 budget and beyond.

18. Subsidy reform has shifted to a higher gear and is bearing fruit (W-COM.-¶6). As noted in paragraph 10, significant progress has recently been made in advancing the reform of the subsidy system, helping achieve a substantial reduction in its cost and associated fiscal risks. The government is committed to pursuing the reform beyond the measures already taken. Further reduction in the diesel subsidy will be implemented through gradual adjustments, with a view to completely eliminating this subsidy by mid-2015. By then, all energy subsidies, except those on butane, will have been removed, which will help bring the subsidy bill below 3 percent of GDP (subsidy outlays were 6.6 percent of GDP in 2012 and 4.8 percent of GDP in 2013).[8] Through recent and planned measures, the authorities are considerably shielding the budget from risks linked to the volatility of international oil prices. Furthermore, the authorities are looking at ways to progressively reduce subsidies on wheat and butane, the latter in part through measures aimed at substituting butane consumption in agriculture by the use of renewable energy. At the same time, social protection for the most vulnerable is being expanded through dedicated programs, including programs to support access to health care for the poor and access to education for school-age children.[9]

19. The effects of measures to contain the high public wage bill will be gradual over the medium term (W-COM.-¶7). The authorities intend to bring the public payroll below 11 percent of GDP in the medium term (from a projected 13 percent of GDP in 2014). Their strategy appropriately relies on several measures, including limiting the net creation of new positions, salary advances, and promotions to a well-defined budget envelope, in order to reach their medium-term goal. Achieving

[8] The authorities had originally planned to reduce subsidy outlays to 3 percent of GDP by 2016. The recent measures on industrial fuel used for electricity and the projected removal of diesel subsidies will accelerate the reduction in subsidy spending.

[9] The authorities have also introduced programs to support low-income widows and physically-disabled individuals. Furthermore, they are providing support to the public transportation sector to mitigate the impact on the fares of higher fuel prices.

this objective is an important part of fiscal consolidation and will contribute to making space for pro-growth, pro-equity spending.

20. A new Organic Budget Law (OBL) will strengthen the budgetary framework (W-COM.-¶8). Adopting a new OBL is among the authorities' top priorities for fiscal reform. Following its vote by the first chamber of parliament, the draft is currently under discussion in the second chamber. It enhances the existing 1998 OBL by introducing multiyear and program budgeting, performance management, and greater fiscal transparency. It also addresses weaknesses in the budgetary framework that became evident in 2012, by making wage expenditure appropriations binding ceilings and limiting the carryover of investment appropriations, although the related provisions would only be effective in 2016 and 2017 respectively, to give enough time to build capacity in line ministries that will be responsible, under the new framework, for enforcing these new limits.[10] The authorities' objective is to ensure that the law is adopted in time so the 2015 budget can be prepared under the new framework with respect to multiyear and program budgeting, subject to the validation of the new OBL by the Constitutional Court. Putting in place a strong regulatory framework deriving from the new OBL will be important. The Fund stands ready to provide technical assistance in this area to support the authorities' efforts. Before permanent wage bill and investment carryover provisions of the new OBL become effective, the authorities will continue with the current technical measures to exert control in these two areas.

21. The first step of the authorities' two-stage pension reform was launched in June 2014 (W-COM.-¶9). The financial situation of the pension system, particularly of the main public pension fund (*Caisse Marocaine de Retraites*, CMR), is tenuous. The authorities have prepared a two-stage reform. The first stage consists of a parametric reform aimed at improving the actuarial situation of the CMR and prolonging its viability. It was launched in June 2014 (paragraph 10). To put the system as a whole (public and private) on a sustainable footing, the second stage will consist of a broader structural reform including the merging of the existing four pension funds into two funds (one public, one private).

B. Monetary and Exchange Rate Policies

22. BAM will continue to conduct monetary policy in support of price stability while the authorities are preparing for a transition toward a more flexible exchange rate regime and a new monetary anchor (W-COM.-¶¶10, 11). In the context of a pegged exchange rate regime, BAM has been successful at achieving low inflation and anchoring inflation expectations. Although the peg has served Morocco well in the past, greater flexibility in the exchange rate regime would help support competitiveness, the resilience of the economy to exogenous shocks, and the authorities' trade and financial diversification strategy. The authorities are preparing to make such a move within the next three years, if macroeconomic conditions, and especially the fiscal position, are supportive.

[10] For a fuller discussion of the draft organic budget law, see CR/14/66 (third review under the current PLL arrangement).

The Fund is providing technical assistance in this area, including assistance on options for and operational management of a more flexible exchange rate regime and on strengthening BAM's forecast and policy analysis capacity to support a new nominal anchor for monetary policy.

C. Financial Policies

23. Financial policies will continue to be geared toward strengthening banking supervision and regulation while promoting greater financial deepening (W-COM.-¶10). Banking supervision and regulation is being strengthened through the implementation of Basel III norms. In June 2013, BAM increased the capital adequacy requirement to 12 percent and the core capital requirements to 9 percent. In August 2013, it adopted new definitions of prudential capital that entered into force in January 2014, and of the short-term liquidity ratio, which is being introduced in line with the Basel III calendar. BAM continues to closely monitor potential risks linked to the expansion of Moroccan banks in sub-Saharan Africa, in coordination with relevant supervisors in host countries. This includes consolidated control and supervision of banking groups as a whole, as well as joint on-site visits with host supervisors. A new banking law, which aims at strengthening BAM regulation and supervision competencies, reinforcing the macroprudential framework, and fostering the development of Islamic banking, was adopted by the first chamber of parliament on June 25. A new draft of the Central Bank Statute, which already includes best international practices in a number of areas, aims to further strengthen BAM's independence and extend its competence, is being finalized for submission to parliament.

D. Structural Reforms

24. The authorities are advancing their structural reform agenda, which aims at improving competitiveness, labor market conditions, and growth (W-COM.-¶12). To improve the business environment in 2014, an action plan comprising 30 measures is being implemented. These measures include streamlining administrative procedures for enterprises, improving investor protection by amending the law on limited-liability companies, strengthening public-private partnerships, and implementing measures to ensure the smooth application of the new procurement code. In April 2014, the authorities unveiled a new national industrial acceleration program, which seeks to further foster the development of new industries. A reform of the judiciary has also been launched, which is crucial to improve transparency, governance, and the business environment. The government is revamping its active labor market policies because most of them have had limited success so far, while initiating a discussion with social partners on how to make the labor code more supportive of job creation while promoting adequate work conditions. At the end of April 2014, the government announced a 10 percent increase in the minimum wage spread over the next two years, which runs the risk of deepening informality but is unlikely to affect competitiveness.

PLL QUALIFICATION

25. Staff believes that Morocco continues to qualify for a PLL arrangement. In addition to the generally positive assessment of Morocco's policies by the Executive Board in the context of the

2013 Article IV consultation in January 2014, staff considers that Morocco meets the PLL qualification criteria.

A. General Assessment

26. Morocco's economic fundamentals and institutional policy frameworks are sound, and the country is implementing, and has a track record of implementing, sound policies.

- **Economic performance has been strong**. It kept a low fiscal deficit (averaging 2.5 percent of GDP during 2007–11) as well as low inflation (less than 2 percent) and a current account deficit of about 4.6 percent of GDP. Growth averaged almost 4½ percent during that period. The banking system has been stable. Over the medium term, the growth rate is expected to remain reasonably high and stable in the context of low inflation. Both public and external debt levels are assessed to be sustainable.

- **Despite an external environment that proved more difficult than initially anticipated, Morocco successfully managed to lower vulnerabilities over the course of its first PLL arrangement owing to sound policies** (Box 1). With higher oil prices and lower growth than expected in advanced economy trading partners, external conditions were challenging throughout the implementation of the authorities' program. The impact was felt mostly in 2012, with a significant widening of the fiscal and external deficits but, owing to a strong policy response, the fiscal deficit was brought back in 2013 close to its initial target at the inception of the PLL. During the 2013 Article IV consultation, Directors praised the resilience of the economy in "the face of significant external shocks and challenging domestic conditions." They "welcomed recent measures that successfully helped reduce fiscal and external vulnerabilities."

- **The authorities are committed to maintaining sound policies in the future, including ensuring medium-term fiscal sustainability.** They are targeting a medium-term fiscal deficit of 3 percent of GDP by 2017, which corresponds to a primary balance of 1.4 percent of GDP (consistent with a gradual reduction in public debt). In addition to medium-term fiscal sustainability, the government's main objectives are to improve competitiveness and productivity; reduce the unemployment rate to 8 percent over the medium term; and improve access to education and vocational training, health, and social protection. In this context, the authorities are committed to implementing an ambitious agenda for the promotion of higher and more inclusive growth.

- **The policy framework is sound, and has proven responsive to challenges.** Morocco's track record of strong economic performance has been supported by a strong policy framework. In particular, the authorities have shown a commitment to taking corrective actions in the face of unforeseen difficulties. After the unanticipated fiscal slippage in 2012, they have quickly implemented measures to rationalize spending and improve the monitoring of budget execution, pending the adoption of a new organic budget law that would structurally address the identified weaknesses.

Box 1. Morocco: Achievements under the First PLL Arrangement

Morocco has made progress under its first PLL arrangement, with the authorities demonstrating strong commitment to reforms in 2013*. However, vulnerabilities, especially on the external side, were not reduced so much as expected because of a worse-than-expected external environment and, initially, a slower pace of reforms. An unanticipated deterioration of the fiscal balance at the end of 2012 uncovered some institutional weaknesses that are being addressed.*

The program was expected to strengthen growth and narrow fiscal and external deficits, supported by a moderate improvement in the external environment and domestic reforms. Growth was projected to reach 2.9 percent of GDP in 2012 and 5.5 percent in 2013. The fiscal target was set at 6.1 percent of GDP and 5.3 percent of GDP in 2012 and 2013 respectively, in line with the authorities' objective of a budget deficit of 3 percent of GDP in the medium term. The current account deficit was projected to reach 7.4 percent in 2012 and 4.5 percent in 2013. Reserves were expected to lower to 3.9 months of imports. The macroeconomic scenario was supported by the following external assumptions and domestic reforms:

- Euro zone GDP growth was projected to improve by 1.5 percent of GDP from 2012 to 2013. Oil prices were expected to fall from 106.5 in 2012 to 95.8 in 2013.
- The authorities intended to reform the subsidy system by increasing the pass-through to reduce cost by 25 percent and to further reduce subsidies in other sectors. They aimed at moderating the wage bill by introducing performance-based compensation and stabilization of the workforce. The authorities also intended to reform the public pension fund and the tax system. The authorities planned to increase potential growth in the medium term by 1 percentage point of GDP by implementing structural reforms, including further improvement of the business climate and economic governance.

Morocco: Original PLL vs. Current Macro Framework

	2011		2012		2013		
	PLL 1/	Act.	PLL 1/	Act.	PLL 1/	Act.	Diff.
	(In percent of GDP, unless otherwise specified)						
Output and Prices							
Real GDP	4.9	5.0	2.9	2.7	5.5	4.4	-1.1
Consumer prices (period average)	0.9	0.9	2.2	1.3	2.5	1.9	-0.6
Public Finances							
Budget balance	-6.9	-6.7	-6.1	-7.4	-5.3	-5.5	-0.2
Primary balance (excluding grants)	-4.8	-4.6	-4.3	-5.0	-4.1	-3.6	0.5
Revenue	27.6	27.8	28.3	28.7	28.1	28.3	0.2
Expenditure	34.5	34.5	34.4	36.1	33.3	33.8	0.5
Of which: Wages	12.2	12.4	12.5	13.2	12.1	12.9	0.8
Subsidies	6.1	6.1	6.1	6.6	4.3	4.8	0.5
Total government debt	54.3	54.4	56.9	60.4	58.1	63.9	5.8
External Sector							
Current account including official transfers	-8.0	-8.0	-7.4	-9.7	-4.5	-7.6	-3.1
Current account excluding official transfers	-8.4	-8.4	-8.1	-10.0	-5.9	-8.3	-2.4
Exports + remittances + tourism receipts	36.2	36.2	37.8	34.9	39.4	35.8	-4.7
Imports, excluding petroleum	-30.0	-29.7	-31.6	-28.6	-33.2	-28.8	4.4
Petroleums imports	-11.2	-11.2	-11.6	-12.3	-10.0	-12.1	-2.1
Total external debt	23.4	25.1	23.1	29.8	22.6	31.1	8.5
Gross reserves (in billions of U.S. dollars)	20.6	20.6	17.9	17.5	18.8	19.3	0.5
In months of G&S imports	4.9	5.0	4.0	4.2	3.9	4.3	0.4
External environment							
World GDP growth	3.9	3.9	3.5	3.1	4.1	3.0	-1.0
Euro zone GDP growth	1.4	1.5	-0.3	-0.6	0.9	-0.6	-1.5
Oil prices (brent, $/barrel)	111.0	111.0	106.5	112.0	95.8	108.8	13.0
Phosphate prices ($/metric ton)	122.0	185.0	118.0	186.0	114.0	145.0	31.0
Terms of trade (percentage change)	0.8	2.3	-0.4	-10.8	0.5	-2.4	-2.9

Sources: Moroccan authorities; and IMF staff estimates.

1/ Original PLL framework.

Box 1. Morocco: Achievements Under the First PLL Arrangement (concluded)

However, the external environment turned out significantly worse than expected and domestic reforms were initially delayed. Growth in the euro area trade partners was worse by 1.5 percentage points than expected, while oil prices were 13 dollars higher than forecasted. These factors, combined with a very poor domestic harvest in 2012, reduced real GDP growth by 0.2 percent of GDP, while inflation was 0.6 percentage point lower than expected. In addition, the implementation of the subsidy reform was initially delayed as reaching consensus on some specifics of the reform proved more challenging than anticipated.

As a result, the twin deficits widened in 2012, while weaknesses in public financial management (PFM) were uncovered. The current account deficit deteriorated significantly, to 9.7 percent of GDP instead of contracting to the expected 7.6 percent of GDP. The fiscal deficit also widened, reaching 7.4 percent of GDP. This sharp deterioration, mainly explained by overruns in wages, subsidies, and capital transfers, was neither prevented nor anticipated. It exposed the need to strengthen the monitoring of budget execution and to address weaknesses in the budgetary framework, notably by making wage appropriations binding and tightening the rules to carry over investment appropriations across budget years.

The authorities reacted by stepping up the pace of reforms, which helped achieve some of the outcomes as projected at the outset of the program. In 2013, the authorities implemented a series of measures that helped achieve their fiscal deficit objective, lower fiscal risk, and strengthen PFM. The budget framework was strengthened through temporary measures pending the implementation of a new organic budget law (OBL). Owing to tighter control, investment spending remained consistent with the overall fiscal objective, despite higher-than-projected carryover of unspent investment allocation from the previous year's budget. From September 2013 to June 2014, the authorities implemented measures to partially index the prices of some subsidized petroleum products to international prices, and to reduce or eliminate subsidies on a number of products. However, the public debt and external debt at end-2013 were 6 percent of GDP and 8 percent of GDP, respectively, higher than projected at the onset of the program. Reserves remained resilient, at 4.3 months of imports, 0.5 months of imports higher than projected, owing in part to sovereign borrowing.

B. Assessment of Specific Criteria

27. **Morocco performs strongly in three out of the five areas for PLL qualification, namely financial sector soundness and supervision, monetary policy, and data adequacy**. In addition, it does not substantially underperform in the remaining two qualification areas, namely external position and market access, and fiscal policy.

External position and market access

Overall, Morocco does not substantially underperform in the external position and market access area.

- *Criterion 1. A sustainable external position*. At end-2013, the current account deficit remained high at 7.6 percent of GDP, but was significantly lowered from its 2012 peak of 9.7 percent of GDP. Data available at this stage indicate that the current account deficit has continued to shrink so far in 2014. The exchange rate assessment still shows some evidence of moderate overvaluation of the dirham, though less than a year ago. Although the external debt increased over the past few years because of a combination of increasing financing needs and low spreads of international bonds, it remains sustainable under anticipated policies.

- *Criterion 2. A capital account position that is dominated by private flows*. Private flows, usually dominated by FDI, have increased over the past few years and now constitute the largest share of the capital account. Nonetheless, public flows remain sizable, at around 30 percent of external debt inflow in 2013. Access to international financial markets by Moroccan corporations is nascent and still modest in size compared to other emerging markets.

- *Criterion 3. Track record of steady sovereign access to capital markets at favorable terms*. With three sovereign bond placements at favorable terms over the past 18 months, Morocco's market access remains well established. On June 13, 2014, Morocco issued a €1 billion 10-year bond at 3.5 percent, following successful issuances in December 2012 and May 2013. International market access for corporate Morocco is also on the rise. Following an issuance by a Moroccan bank in November 2013, the National Phosphate Company successfully tapped the international market with a US$1.55 billion Eurobond in April 2014 and an additional US$0.3 billion in May 2014. Nonetheless, even though sovereign access to international capital markets is well established, Morocco is still rated below investment grade by one international rating agency.

- *Criterion 4. A reserve position that is relatively comfortable*. Although external pressures and uncertainties continue to be a concern, reserves have been broadly stable for more than a year. Considering existing controls on capital outflows that partially insulate them from capital account vulnerabilities, they have remained adequate above 90 percent of the Fund's reserve metric for emerging markets. The stabilization of reserves is owed in part to the improvement in the current account deficit, but mostly to strong FDI inflows, substantial development partner assistance, and external sovereign borrowing. Reserves are expected to increase above 100 percent of the ARA metric over the medium term. However, reserves are not comfortable enough should the country be hit by some external shocks (Box 2).

Fiscal policy

Morocco does not substantially underperform in the fiscal area.

Criterion 5. Sound public finances, including a sustainable public debt.

- Morocco remains committed to a sustainable fiscal path, and has a record of sound public finances, despite the challenges of 2012. The authorities have taken commendable actions to strengthen Morocco's fiscal position and address the weaknesses they identified in their fiscal framework, reducing vulnerabilities in this area. Their policy program is consistent with further reducing the fiscal deficit to 3 percent of GDP by 2017. Staff's assessment remains that Morocco does not substantially underperform in the fiscal area, based on the following considerations.

- The authorities achieved their fiscal deficit objective in 2013. The deficit, including grants, was reduced by almost 2 percent of GDP to 5.5 percent of GDP, as programmed at the time of the second PLL review and very close to the initial target at the inception of the PLL arrangement. This reduction was achieved, as expected, in part because of higher external grants and lower global oil prices, but also thanks to strong policy action to limit the subsidy bill and to rationalize capital spending.

- The 2014 budget targets a continued prudent reduction in the deficit through structural fiscal reforms. The further reduction to 4.9 percent of GDP is to be achieved mainly through a continued reduction in the cost of energy subsidies while social protection for the most vulnerable is being expanded through dedicated programs. Furthermore, the tax system is being adequately reformed and progress was made in quantifying the much-needed parametric reform of the main public pension fund. Budget execution so far in 2014 remains consistent with achieving the annual fiscal deficit target. The authorities are committed to taking appropriate actions to meet their annual target, as they did in 2013, should revenue or expenditure developments require adjustment.

- The budget framework is being strengthened through the adoption of a new organic budget law (OBL). Until the relevant provisions of the OBL enter into force, technical measures to better control the wage bill and investment spending will remain in place.

- Public sector debt remains sustainable, based on a rigorous and systematic debt sustainability analysis.[11] The public debt is about 64 percent of GDP and is resilient to shocks to real GDP, the primary fiscal balance, the real exchange rate, and the real interest rate. After peaking at just under 66 percent of GDP in 2015, it is projected to progressively fall closer to 60 percent in the medium term as a result of fiscal adjustment. There are some risks linked to relatively high gross financing needs. The debt remains sustainable under a stress test involving the same shock that would generate the potential financing need under the proposed PLL arrangement.

Monetary Policy

Morocco performs strongly in the monetary policy area.

Criterion 6. Morocco has maintained low and stable inflation, in the context of a sound monetary and exchange rate policy framework. BAM has effectively anchored inflation expectations in the context of the exchange rate peg. Inflation has averaged 1.7 percent over the past 10 years and never exceeded 4 percent. Staff considers that the current monetary policy stance is appropriate within the existing monetary and exchange rate framework. The nonprimary output gap is moderately negative (-0.6 and -0.3 in 2013 and 2014, respectively) and risks to growth are tilted to the downside; nevertheless, monetary policy should remain cautious about the possible effects on inflation of price increases related to the subsidy reform. BAM has solid policy analysis capacity, which is currently being strengthened with technical assistance from the IMF. As discussed in previous staff reports,

[11] See the attached debt sustainability analysis.

the monetary framework will need to evolve in line with a move toward a more flexible exchange rate.

Financial sector soundness and supervision

Morocco performs strongly in the financial sector area.

- *Criterion 7. The financial system is sound and there is no solvency problem that may threaten systemic stability.* As of December 2013, the capital adequacy ratio was 13.3. Moroccan banks mainly fund themselves with domestic deposits (about 80 percent of non-equity funding). Liquidity pressures have decreased recently, helped by the March 2014 cut in the reserve ratio and international bond issuances. NPLs have increased to 6.4 percent of total loans as of April 2014, reflecting the slowdown in activity, but they continue to be closely monitored and adequately provisioned. At the institutional level, BAM supervisory powers cover not only banking institutions but also other financial institutions including, offshore banks, microcredit associations, and funds transfer companies. Coordination is being strengthened between BAM and other supervisory agencies, including the Insurance Supervisory Authority.

- *Criterion 8. Financial sector supervision is effective.* BAM is further strengthening banking supervision in line with new Basel III standards. The capital adequacy ratio was increased in June 2013. New definitions of prudential capital and short-term liquidity ratio have been adopted in August 2013 and are in the process of being implemented. Moroccan banks fund themselves mainly through domestic deposits, but have started expanding their sources of funding to include the issuance of international bonds. BAM is closely monitoring potential risks linked to the expansion of Moroccan banks in sub-Saharan Africa and reinforcing coordination and exchange of information with supervisory and regulatory agencies in host countries, including consolidated supervision of groups and on-site visits. BAM has an adequate range of tools for intervention in noncompliant banks or those engaging in unsafe or unsound practices that put the interests of depositors and creditors at risk. A financial sector assessment (FSAP) update is scheduled for spring 2015.

Data adequacy

Morocco performs strongly in the area of data adequacy.

Criterion 9. Data transparency and adequacy. Data provision and quality are fully adequate. Morocco meets the PLL requirement on data transparency and integrity. Morocco subscribes to the Special Data Dissemination Standard and its data are adequate for surveillance and program monitoring. The authorities are committed to continuing to improve data quality and access, notably through participating in the OpenData Platform (ODP), for which a joint technical assistance mission was conducted by STA and the African Development Bank in January 2014.

C. PLL Approval Criteria

28. Morocco does not face any of the circumstances under which the Fund may not approve a PLL arrangement. Specifically: (i) as noted above, Morocco has access to international capital markets; (ii) there is no need to undertake large macroeconomic or structural policy adjustment; (iii) the public debt position is sustainable in the medium term, with a high probability; and, (iv) there are no widespread bank insolvencies.

ACCESS LEVEL AND DURATION

29. Morocco does not face a financing gap under the baseline scenario. Gross external financing requirements are expected to stabilize around US$9.7 billion in 2014, after peaking at almost US$11 billion in 2012 (Table 9). They are expected to be financed mostly through net FDI inflows (US$2.8 billion), medium- and long-term borrowing (US$6.4 billion), and net private and other capital flows (US$2 billion). Net international reserves are projected to remain broadly stable as measured in months of imports. In the absence of external shocks, reserves are projected to rise slightly above 90 percent of the composite reserve metric.

30. Nevertheless, risks to the balance of payments from external shocks remain, justifying access under a PLL arrangement. Notwithstanding the reduction of vulnerabilities achieved under the 2012 PLL arrangement, the external and fiscal positions remain vulnerable to external shocks. Relative to the 2012 PLL arrangement, and as highlighted in the latest WEO and GFSR, the balance of risk for global growth has improved, largely reflecting improving prospects for advanced economies. However, important downside risks remain, and new risks have emerged, particularly for emerging economies, whose risks have increased. The risks that would most significantly affect the Moroccan economy include:

- A protracted period of slower growth in Morocco's main advanced-country trading partners, particularly in Europe. Notwithstanding the improved baseline prospects, Europe still faces a high risk that growth will turn out lower than anticipated. If this risk materializes, FDI could be lower and the current account would worsen because remittances, tourism, and exports would weaken.

- Surges in global financial market volatility, triggered by exit from unconventional monetary policy (UMP) in the United States. The immediate implication of this risk for Morocco is that it would face higher rates in the international bond market. The higher cost of borrowing would result in a higher current account deficit. In addition, volatility in the global financial market would result in lower portfolio and FDI flows.

- Geopolitical risks related to the Middle East and, to a lesser extent, to Ukraine/Russia. These could trigger substantial rises in oil prices, which would have an adverse effect on Morocco's current account and fiscal deficits. In addition, given the links of Ukraine and Russia with Europe, a recession in the former would also affect growth in Europe, which in turn would affect Morocco through the channels described above.

31. The shocks are expected to affect the balance of payments through both the current and the financial accounts (Box 2 and Table 9). The potential magnitude of the shocks is discussed in Box 2. These shocks would affect the trade deficit the most: it would be 2.5 percent of GDP higher than in the baseline under the assumed scenario, as exports to the euro area would slow considerably and oil-related imports would increase. Remittances shortfall and others deficits would amount to 1.3 percent of GDP. FDI inflows are conservatively assumed to be 0.7 percent of GDP lower than in the baseline, while portfolio inflows would decrease by 0.2 percent of GDP (Figure 3).

Estimated impact of the shocks

(Changes relative to baseline)

Trade deficit	Higher by 2.5% of GDP
Current transfer and other deficits	Higher by 1.3% of GDP
FDI Inflows	Lower by 0.7% of GDP
Portfolio Inflows	Lower by 0.2% of GDP
Minimum gross reserves	Current level relative to Fund reserve adequacy metric (90%)

Source: IMF staff estimates.

32. The estimated financing gap that would result from these shocks does not factor in potential increased financing from other multilateral and bilateral sources. This is because no additional commitments have been identified in the event of a significant adverse shock. In the case of a long-lasting adverse shock or if expected financing were to fall durably short, staff recommends that the authorities develop a broader financing plan and pursue a more rapid fiscal consolidation to limit a possible drain on official reserves. In that context, the insurance provided by the PLL would help address likely short-term turbulences and smooth the path toward the necessary long-term adjustment. Moreover, the authorities are also encouraged to seek financial assistance from both multilateral and bilateral donors to meet financing needs.

33. The requested access level of the new arrangement is lower than in the first PLL. On balance, potential financing requirements are expected to be smaller than under the 2012 PLL arrangement, reflecting the strengthening of the economy's self-reliance achieved by the authorities' program under the first PLL arrangement, and an overall balance of risks somewhat less adverse than recently. Under a stress scenario, which is consistent with past crises and in line with Flexible Credit Line cases (Figure 3), and based on a financing gap determined by a shortfall of reserves relative to 90 percent of the Fund's composite reserve adequacy metric (i.e., the level of reserve would remain broadly as expected in 2014 under the baseline), potential needs by 2016 would be consistent with a total access level of 550 percent of quota (US$5.0 billion) (Box 2). This access level, which falls under the exceptional access policy, is significantly below the median and below the average access for recent exceptional cases (Table 10). Morocco continues to meet the criteria for exceptional access (Box 3).

34. The new arrangement would have a duration of two years, and the authorities intend to treat it as precautionary. Staff believes that a two-year precautionary arrangement would be appropriate, given the likely persistence of global and euro zone economic uncertainties, and of supply-side uncertainties surrounding oil prices. A two-year period would also provide sufficient time to continue strengthening the economy's resilience and prepare it for a successful exit if external circumstances warrant.

35. The arrangement will include standard performance criteria and indicative targets on the fiscal deficit and net international reserves (W-COM.-¶13 and W-COM.-Table 1).

36. The authorities' program will be instrumental in strengthening the economy's resilience, providing a reasonable prospect of exit from the PLL. The policy package will help pursue the reduction in the fiscal and current account deficits. Regarding the current account, the authorities' strong push for diversification of exports is already paying off: exports from newly developed industries (automobile and aeronautics) have now overtaken exports of traditional products like phosphate or textiles. As a result, total exports were stable in 2013 relative to 2012 (in nominal terms), in spite of a 22.9 percent decline in phosphate-related exports, traditionally the main export product of Morocco. The newly developed industries will play even bigger roles in years to come and will further improve the resilience of the economy to external shocks. On the fiscal side, the sharp reduction of subsidies by end-2015 will protect the budget against external shocks. The resiliency of the economy, along with the prospect of better global conditions, will improve the macroeconomic position. Under the baseline macroframework, the primary fiscal deficit will decrease below the debt-stabilizing balance in 2016, putting the public debt on a downward path after its peak of 66 percent of GDP in 2015. The current account deficit by the end of the arrangement will be close to the norm expected for an emerging market like Morocco while the reserves level will increase above 100 percent of the Fund's ARA metric and would be adequate to support an exit at the expiration of the new arrangement if external circumstances warrant. The reduced access level considered for the proposed arrangement already signals progress toward exit.

Box 2. Morocco: Access Level

The adverse scenario developed by staff assumes shocks to various components of Morocco's balance of payments. In addition to risks considered under the 2012 PLL arrangement (an oil shock linked to geopolitical tensions in the Middle East and a negative shock to European growth), new risks may significantly affect Morocco. These are risks linked to the tapering of unconventional monetary policy as well as commodity price shocks originating from tensions in Ukraine/Russia, in addition to tensions in the Middle East. The adverse scenario simulated by staff does not assume the concomitant occurrence of all these shocks, but explores the possibility that the risks of a protracted period of slow growth in Europe and a temporary significant surge in energy prices from geopolitical tensions materialize at the same time. As described below, the materialization of risks these would pull in some instances the economy in opposite directions.

The combination of the assumed shocks would translate into:

- an increase in oil price by US$20 resulting from: (i) a negative shock stemming from geopolitical risks related to the Middle East and/or Ukraine/Russia, triggering an increase in oil prices assumed to be by US$30—slightly higher than the $25 assumed under the 2012 PLL arrangement to account for the new shock from Ukraine/Russia; and (ii) a reduction in oil prices by US$10 due to lower growth in Europe;[1] and,
- a reduction in Morocco's advanced-economy trading partners' GDP growth by 2.5 percentage points, reflecting: (i) a slowdown in the European Union, which is assumed to reduce growth in Morocco's advanced-economy trading partners' GDP by 1.5 percentage points;[2] and (ii) a negative shock of 1 percentage point resulting from geopolitical risks in the Middle East and/or Ukraine/Russia.[3]

These shocks would affect the current account through lower exports, lower remittances, lower tourism receipts, higher energy imports, and somewhat higher interest payments. Furthermore, the capital account would also be affected through a fall in foreign direct investment (FDI) and equity portfolio inflows. Specifically, staff assumed a decline in FDI by 25 percent relative to the baseline (equivalent to an FDI level of 85 percent of the 2011-13 average FDI) and in equity portfolio inflows by 90 percent relative to baseline. These assumptions are somewhat conservative relative to Morocco-specific movements observed in recent years (reduction of net FDI inflows of 26 percent and 33 percent in 2009 and 2010, respectively).

Source of risks	Shock assumptions/expected impact			
	Oil Price (US$)	EU Growth (Percentage points)	Interest Rate (Basis points)	FDI (Percent of baseline)
Protracted period of slow growth in EU	-10	-1.5	...	-20
Geopolitical (increase in oil prices)	30	-1	...	-5
UMP Tapering	...	-0.1	50	-10
Cumulative impact (if all shocks were simultaneous)	20	-2.6	50	-35
Simulated impact for determining access level	**20**	**2.5**	**0**	**-25**

The financing gap is defined as the level of financial support needed to bring gross international reserves to 90 percent of the Fund's reserve adequacy metric after the shock, broadly corresponding to the 2014 level under baseline projections (Table 9).

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[1] This is consistent with the assumption that growth in Morocco's advanced trading partners would be lower by 2.5 percentage points: the 2014 Spillover Report estimates that a one percentage point decline in advanced economies' growth would lower commodity prices by about 4 percent.

[2] This represents less than half the shock stimulated in the 2012 PLL. This assumption is consistent with analysis in the 2013 spillover report, which estimates that a slowdown in the euro area could result in the GDP level in the euro area to be 4 percent below the baseline after four years.

[3] Staff's analysis based on the IMF's Flexible System of Global Models estimates that a 25 percent temporary increase in oil prices associated with weaker confidence would lower global GDP by 1 percent.

Box 3. Morocco: Exceptional Access Criteria

The new PLL arrangement would involve exceptional access; staff's evaluation is that Morocco continues to meet each of the four substantive criteria for exceptional access:

- *Criterion 1.* The member is experiencing or has the potential to experience exceptional balance of payments pressures on the current or capital account, resulting in a need for Fund financing that cannot be met within the normal limits. Morocco does not face actual balance of payments pressures; however, it is exposed to risks of a protracted period of slower growth in advanced partner countries, commodity price shocks linked to geopolitical tensions, and surges in global financial market volatility. Staff is of the view that the realization of a stress scenario could give rise to financing needs beyond normal access limits.

- *Criterion 2.* A rigorous and systematic analysis indicates that there is a high probability that the member's public debt will remain sustainable. Gross public debt has increased to 63.9 percent of GDP and is projected to peak at 65.7 in 2015. Thereafter, it would decrease closer to 60 percent of GDP in the medium term as the authorities continue fiscal consolidation efforts. Stress tests indicate that under the standard shocks, debt ratios would remain sustainable over the medium term.

- *Criterion 3.* The member has prospects of gaining or regaining access to capital markets while Fund resources are outstanding. Morocco has successfully tapped into international capital markets recently, including the issuance of a €1 billion in June 2014, and a US$1.5 billion international sovereign bond in December 2012, which they extended by US$750 million in May 2013. Each issuance benefited from low spreads and long maturities (10 and 30 years) reflecting the confidence placed in Morocco by the international monetary market. Sovereign spreads continue to decrease and are now at 115.9 basis points (as of June 20, 2014). Staff is of the view that Morocco could continue to tap markets at similarly favorable terms.

- *Criterion 4.* The policy program and institutional and political capacity to deliver it provide a reasonably strong prospect of success. Morocco's economic program is based on fiscal restraint and a central bank committed to policies consistent with maintaining price stability. The authorities' track record of sound macroeconomic policies, supported by solid institutions, including an independent central bank, and the macroeconomic resilience observed during the recent global crisis and uprisings that have emerged across the MENA region since early 2011, give confidence in continued sound policies and stability over the longer term.

IMPACT ON FUND FINANCES AND SAFEGUARDS

37. Capacity to repay the Fund. Morocco did not draw on its first PLL and has no outstanding debt to the Fund. The authorities intend to continue to treat the PLL arrangement as precautionary. However, in the event that Morocco drew on the entire amount available, it would continue to have adequate capacity to repay the Fund. Full drawing under the requested PLL arrangement would bring Morocco's outstanding use of GRA resources to an amount equivalent to SDR 3.235 billion. This would represent a modest share of Morocco's external debt, which would remain moderate with Fund credit reaching about 1/8 of total external debt at its peak. External debt service would increase over the medium term. Morocco's projected debt service to the Fund would peak in 2018 at about 1.6 percent of GDP. However, the reserve coverage ratio would be comfortable.

38. The proposed arrangement present manageable credit and liquidity risks to the Fund (Supplement 1). The authorities intend to treat the arrangement as precautionary. Were the authorities to draw the full amount available in the event of exceptional shocks, the Fund's liquidity position would remain adequate. This assessment is supported by the reduced access which underscores the authorities' intention to exit as external risks subside, and rigorous ex ante and focused ex post conditionality.

39. An update of the February 2013 safeguards assessment of the BAM has been initiated in the context of the proposed successor PLL arrangement. The previous assessment found a robust safeguards framework with strong control mechanisms. BAM has made good progress in implementing safeguards recommendations from the previous assessment, including publication of audited annual financial statements. Outstanding recommendations include amending the central bank law to formally enshrine existing good governance practices and key safeguards, and to further strengthen the autonomy of the central bank. The authorities have prepared amendments to the law which are under consideration by the government.

STAFF APPRAISAL

40. The authorities have made important strides in rebuilding policy space and addressing medium-term challenges. They have been consolidating their fiscal position while pursuing an ambitious agenda of structural reforms to address vulnerabilities while strengthening competitiveness and promoting higher and more inclusive growth. The significant progress made in reforming the subsidy system is particularly commendable. The first PLL arrangement has provided insurance against external risks and a strong anchor for policy implementation in the face of a more challenging external environment than anticipated at the onset of the arrangement.

41. The external environment remains subject to significant downside risks. Morocco would be significantly affected by a protracted period of slow growth in Europe, heightened financial market volatility linked to the exit from unconventional monetary policy, and/or a surge in oil prices resulting from geopolitical tensions. Therefore, Morocco could face a need for balance of payments financing. Under those circumstances, staff considers it appropriate to renew the insurance provided by the PLL while the authorities continue to strengthen the capacity of the economy to withstand shocks and foster higher and more inclusive growth over the medium term.

42. Staff's assessment is that Morocco continues to meet the PLL qualification criteria. The Executive Board's assessment in concluding the 2013 Article IV consultation was generally positive. Morocco continues to perform strongly in three out of the five areas for PLL qualification, namely financial soundness and supervision, monetary policy, and data adequacy, and does not substantially underperform in the area of external position and market access or in the area of fiscal policy. Morocco does not face any of the circumstances under which the Fund may not approve a PLL arrangement. Staff also considers that Morocco meets the criteria for exceptional access.

43. The authorities' policy package appropriately addresses the short- and medium-term challenges. Staff considers that the program described in the authorities' written communication is appropriate for reducing fiscal and external vulnerabilities, including by putting the public and external debts on downward paths and by increasing reserves to a more comfortable level, while laying the foundation for higher and more inclusive growth. Expenditure control will be key to achieving the desired strengthening of public finances. Staff welcomes the authorities' determination to advance major and much-needed reforms, including those of subsidies, pension, and the tax system. The timely adoption of a new organic budget law will be particularly important to strengthen the budget framework and address vulnerabilities in this area. Staff encourages the authorities to move towards a more flexible exchange rate regime in coordination with other macroeconomic policies. Advancing structural reforms to improve the business climate, the judicial system, access to finance, and the labor market will be crucial to achieving higher growth and employment.

44. Staff recommends the approval of a new two-year PLL arrangement of SDR 3.2351 billion (550 percent of quota, of which 500 percent of quota would be available in the first year). Such access is consistent with the size of downside risks as evaluated in staff's adverse scenario. It is less than in the first arrangement, reflecting the improvement in global conditions from two years ago and the strengthened resilience of the economy. Nonetheless, the phasing is to be flatter to help insure against the possibility that several independent risks materialize at the same time and, in that context, to avoid too abrupt a reduction in the insurance coverage from the existing level, which could unsettle markets. The duration of two years is consistent with the possible persistence of external risks. The current arrangement will be cancelled upon approval of the new one.

45. Staff's view is that the proposed successor PLL arrangement carries low risks to the Fund. The requested arrangement will have minimal impact on the Fund's liquidity and, even though Morocco intends to treat the PLL as precautionary, GRA credit to Morocco would be low in the event of a full drawing by Morocco of available resources. In addition, risks would be further mitigated by Morocco's relative low debt levels and external debt service obligations.

Table 1. Morocco: Selected Economic Indicators, 2011–19

			PLL 1/	Rev. 2/	PLL 1/	Rev. 2/			Proj.		
	2011	2012	2013		2014		2015	2016	2017	2018	2019
(Annual percentage change)											
Output and Prices											
Real GDP	5.0	2.7	4.5	4.4	3.9	3.5	4.7	5.0	5.3	5.4	5.4
Real agriculture GDP	5.6	-8.9	...	19.0	...	-1.3	3.5	4.0	4.5	5.0	5.0
Real non-agriculture GDP	4.9	4.4	...	2.3	...	4.3	4.9	5.2	5.5	5.5	5.5
Consumer prices (end of period)	0.9	2.6	0.4	0.4	2.5	2.2	1.8	2.3	2.3	2.3	2.3
Consumer prices (period average)	0.9	1.3	1.9	1.9	2.5	1.1	2.0	2.3	2.3	2.3	2.3
(In percent of GDP)											
Investment and Saving											
Gross capital formation	36.0	35.3	34.7	34.2	35.3	34.3	34.8	35.0	35.3	35.5	35.5
Of which: Nongovernment	30.6	29.7	29.5	28.9	30.7	29.7	29.8	29.4	29.3	29.2	29.0
Gross national savings	27.9	25.5	27.2	26.6	28.8	27.5	29.0	29.9	30.9	31.2	31.6
Of which: Nongovernment	27.5	25.9	25.9	25.3	27.6	26.2	25.9	25.6	25.8	25.7	25.5
(In percent of GDP)											
Public Finances											
Revenue	27.8	28.7	27.9	28.3	27.4	27.9	28.1	28.2	28.2	27.9	28.0
Expenditure	34.5	36.1	33.4	33.8	32.4	32.9	32.4	31.6	31.2	30.8	30.5
Budget balance	-6.7	-7.4	-5.5	-5.5	-4.9	-4.9	-4.3	-3.5	-3.0	-2.9	-2.5
Primary balance (excluding grants)	-4.6	-5.0	-3.6	-3.6	-2.8	-2.9	-2.6	-1.8	-1.4	-0.5	0.0
Cyclically-adjusted primary balance (excl. grants)	-4.3	-4.7	-3.4	-3.5	-3.3	-3.4	-2.6	-1.8	-1.4	-0.5	0.0
Total government debt	54.4	60.4	61.7	63.9	62.5	65.5	65.7	65.0	63.9	62.8	61.4
(Annual percentage change; unless otherwise indicated)											
Monetary Sector											
Credit to the private sector 3/	10.6	4.6	3.6	3.9	5.6	4.4	4.7	4.7	4.4	4.9	5.2
Broad money	6.4	4.5	3.9	2.8	4.6	4.5	5.0	5.5	5.5	6.0	6.0
Velocity of broad money	0.8	0.8	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9
Three-month treasury bill rate (period average, in percent)	3.4	3.4	...	...	...	...	...	...	...	...	...
(In percent of GDP; unless otherwise indicated)											
External Sector											
Exports of goods (in U.S. dollars, percentage change)	21.7	-0.9	1.8	2.5	9.1	8.3	8.7	9.7	9.9	10.0	10.1
Imports of goods (in U.S. dollars, percentage change)	25.3	1.4	0.7	2.1	6.8	6.3	5.5	7.0	7.5	7.5	7.6
Merchandise trade balance	-19.4	-20.9	-19.0	-19.6	-18.1	-18.8	-17.7	-17.0	-16.5	-16.0	-15.4
Current account excluding official transfers	-8.4	-10.0	-8.0	-8.3	-7.5	-8.1	-6.8	-6.0	-5.2	-4.5	-4.0
Current account including official transfers	-8.0	-9.7	-7.4	-7.6	-6.5	-6.8	-5.8	-5.1	-4.4	-4.4	-3.9
Foreign direct investment	2.4	2.4	2.9	2.9	2.9	2.5	2.6	2.6	2.8	2.8	2.8
Total external debt	25.1	29.8	30.9	31.1	31.5	32.9	33.2	33.0	32.2	31.7	31.2
Gross reserves (in billions of U.S. dollars)	20.6	17.5	19.3	19.3	20.0	21.1	22.7	24.7	26.8	29.3	32.0
In months of next year imports of goods and services	5.0	4.2	4.3	4.3	4.3	4.5	4.5	4.6	4.6	4.7	4.8
In percent of Fund reserve adequacy metric	109.9	87.0	...	89.3	...	91.1	92.3	95.2	98.5	102.6	107.7
Memorandum Items:											
Nominal GDP (in billions of U.S. dollars)	99.2	95.9	105.5	103.8	115.1	112.6	121.9	131.8	141.8	152.8	164.5
Unemployment rate (in percent)	8.9	9.0	8.9	9.2	...	...	...	...	...	...	...
Population (millions)	32.2	32.5	32.9	32.9	33.2	33.2	33.5	33.8	34.2	34.5	34.8
Net imports of energy products (in billions of U.S. dollars)	-11.2	-12.3	-12.2	-12.1	-13.0	-12.8	-13.3	-13.9	-14.7	-15.6	-16.6
Local currency per U.S. dollar (period average)	8.1	8.6	8.4	8.4	...	...	...	...	...	...	...
Real effective exchange rate (annual average, percentage change)	-1.7	-1.1	0.1	0.1	...	...	...	...	...	...	...

Sources: Moroccan authorities; and IMF staff estimates.

1/ Refers to the macro framework for the 3rd review in CR/14/22.
2/ Revised macro framework.
3/ Includes credit to public enterprises.

Table 2. Morocco: Budgetary Central Government Finance, 2011–19

(Billions of dirhams)

	2011	2012	2013 PLL 1/	2013 Rev. 2/	2014 PLL 1/	2014 Rev. 2/	2015 Proj.	2016 Proj.	2017 Proj.	2018 Proj.	2019 Proj.
Revenue	223.3	237.7	246.9	247.0	258.4	257.1	276.2	297.1	319.8	341.5	368.8
Taxes	189.0	202.7	199.5	199.5	211.3	208.5	226.5	245.9	265.8	292.2	315.9
Taxes on income, profits, and capital gains	69.2	77.4	75.1	75.1	77.2	76.7	85.5	92.3	99.9	109.7	118.3
Taxes on property	9.3	11.6	11.6	11.6	14.1	14.1	13.4	14.5	16.0	17.2	18.5
Taxes on goods and services	94.6	99.0	99.8	99.8	106.9	105.1	114.5	125.2	135.4	148.3	159.8
Taxes on international trade and transactions	10.7	9.4	8.0	8.0	8.1	8.1	8.3	8.8	9.4	10.4	12.1
Other taxes	5.3	5.4	4.9	4.9	5.0	4.5	4.8	5.1	5.1	6.6	7.1
Grants	1.3	0.5	6.0	6.1	10.6	12.3	10.5	10.3	10.3	2.2	2.2
Other revenue	33.0	34.6	41.4	41.4	36.5	36.3	39.3	40.8	43.7	47.1	50.8
Expense	234.2	252.5	249.3	249.3	262.0	260.4	268.4	275.2	286.5	299.7	316.0
Compensation of employees	99.8	108.9	112.4	112.4	118.8	119.2	124.5	128.0	131.4	134.8	138.4
Of which: wages and salaries	89.0	96.7	...	98.6	...	103.7	107.4	110.3	113.3	116.3	119.3
social contributions	10.9	12.2	...	13.7	...	15.5	17.2	17.6	18.1	18.6	19.1
Use of goods and services and grants	53.5	56.6	59.0	59.0	67.9	68.5	72.0	78.2	83.2	89.7	95.7
Of which : transfers to ONEE	...	...	...	...	...	2.8	4.8	4.8	1.6	0.0	0.0
Interest	18.2	20.1	22.5	22.5	24.8	25.7	26.5	28.1	29.1	30.9	34.5
Subsidies	48.8	54.9	41.6	41.6	35.0	32.2	23.2	17.5	18.1	18.9	19.9
Other expense 3/	13.8	12.1	13.9	13.9	15.4	14.8	22.1	23.4	24.7	25.4	27.3
Net acquisition of nonfinancial assets	43.0	46.1	45.9	45.9	43.0	42.1	49.7	58.5	67.4	77.0	85.5
Net lending / borrowing (overall balance)	-53.9	-60.9	-48.3	-48.1	-46.5	-45.4	-41.8	-36.6	-34.2	-35.2	-32.7
Net lending / borrowing (excluding grants)	-55.2	-61.3	-54.3	-54.3	-57.1	-57.7	-52.3	-46.9	-44.5	-37.4	-34.9
Change in net financial worth	-53.9	-60.9	-48.3	-48.1	-46.5	-45.4	-41.8	-36.6	-34.2	-35.2	-32.7
Net acquisition of financial assets	-5.7	-3.3	0.0	0.0	0.0	-2.0	0.0	0.0	0.0	0.0	0.0
Domestic	-5.7	-3.3	0.0	0.0	0.0	-2.0	0.0	0.0	0.0	0.0	0.0
Shares and other equity	-5.6	-3.3	0.0	0.0	0.0	-2.0	0.0	0.0	0.0	0.0	0.0
Foreign Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	48.2	57.6	48.3	48.1	46.5	43.4	41.8	36.6	34.2	35.2	32.7
Domestic	40.9	42.3	37.1	37.0	31.1	27.7	27.7	22.2	25.6	21.4	18.6
Currency and Deposits	-6.3	-6.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Securities other than shares	37.4	37.4	37.1	45.6	31.1	39.6	27.7	22.2	25.6	21.4	18.6
Other accounts payable	9.9	9.9	0.0	-8.6	0.0	-11.9	0.0	0.0	0.0	0.0	0.0
Foreign Loans	7.3	7.3	11.2	11.1	15.4	15.7	14.2	14.4	8.6	13.7	14.1
Memorandum Item:											
Total investment (including capital transfers)	56.8	58.1	59.7	59.7	58.4	56.8	71.8	81.9	92.1	102.4	112.9
GDP	802.6	827.5	883.5	872.8	941.5	919.7	981.9	1,054.3	1,134.6	1,222.0	1,316.1

Sources: Ministry of Economy and Finance; and IMF staff estimates.

1/ Refers to the macro framework for the 3rd review in CR/14/66.

2/ Revised macro framework. More disaggregated data which were not available at the time of the 1st review have allowed for an enhanced classification of goods and services and grants as per GFSM 2001 guidelines.

3/ Includes capital transfers to public entities.

Table 3. Morocco: Budgetary Central Government Finance, 2011–19
(Percent of GDP)

	2011	2012	2013 PLL 1/	2013 Rev. 2/	2014 PLL 1/	2014 Rev. 2/	2015 Proj.	2016 Proj.	2017 Proj.	2018 Proj.	2019 Proj.
Revenue	27.8	28.7	27.9	28.3	27.4	27.9	28.1	28.2	28.2	27.9	28.0
Taxes	23.5	24.5	22.6	22.9	22.4	22.7	23.1	23.3	23.4	23.9	24.0
Taxes on income, profits, and capital gains	8.6	9.4	8.5	8.6	8.2	8.3	8.7	8.8	8.8	9.0	9.0
Taxes on property	1.2	1.4	1.3	1.3	1.5	1.5	1.4	1.4	1.4	1.4	1.4
Taxes on goods and services	11.8	12.0	11.3	11.4	11.4	11.4	11.7	11.9	11.9	12.1	12.1
Taxes on international trade and transactions	1.3	1.1	0.9	0.9	0.9	0.9	0.8	0.8	0.8	0.8	0.9
Other taxes	0.7	0.6	0.6	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Grants	0.2	0.1	0.7	0.7	1.1	1.3	1.1	1.0	0.9	0.2	0.2
Other revenue	4.1	4.2	4.7	4.7	3.9	3.9	4.0	3.9	3.9	3.9	3.9
Expense	29.2	30.5	28.2	28.6	27.8	28.3	27.3	26.1	25.3	24.5	24.0
Compensation of employees	12.4	13.2	12.7	12.9	12.6	13.0	12.7	12.1	11.6	11.0	10.5
Of which : wages and salaries	11.1	11.7	...	11.3	...	11.3	10.9	10.5	10.0	9.5	9.1
social contributions	1.4	1.5	...	1.6	...	1.7	1.7	1.7	1.6	1.5	1.4
Use of goods and services and grants	6.7	6.8	6.7	6.8	7.2	7.5	7.3	7.4	7.3	7.3	7.3
Of which : transfers to ONEE	0.0	0.0	...	0.0	...	0.3	0.5	0.5	0.1	0.0	0.0
Interest	2.3	2.4	2.5	2.6	2.6	2.8	2.7	2.7	2.6	2.5	2.6
Subsidies	6.1	6.6	4.7	4.8	3.7	3.5	2.4	1.7	1.6	1.5	1.5
Other expense 3/	1.7	1.5	1.6	1.6	1.6	1.6	2.2	2.2	2.2	2.1	2.1
Net acquisition of nonfinancial assets	5.4	5.6	5.2	5.3	4.6	4.6	5.1	5.5	5.9	6.3	6.5
Net lending / borrowing (overall balance)	-6.7	-7.4	-5.5	-5.5	-4.9	-4.9	-4.3	-3.5	-3.0	-2.9	-2.5
Net lending / borrowing (excluding grants)	-6.9	-7.4	-6.1	-6.2	-6.1	-6.3	-5.3	-4.5	-3.9	-3.1	-2.7
Change in net financial worth	-6.7	-7.4	-5.5	-5.5	-4.9	-4.9	-4.3	-3.5	-3.0	-2.9	-2.5
Net acquisition of financial assets	-0.7	-0.4	0.0	0.0	0.0	-0.2	0.0	0.0	0.0	0.0	0.0
Domestic	-0.7	-0.4	0.0	0.0	0.0	-0.2	0.0	0.0	0.0	0.0	0.0
Shares and other equity	-0.7	-0.4	0.0	0.0	0.0	-0.2	0.0	0.0	0.0	0.0	0.0
Foreign Loans	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	6.0	7.0	5.5	5.5	4.9	4.7	4.3	3.5	3.0	2.9	2.5
Domestic	5.1	5.1	4.2	4.2	3.3	3.0	2.8	2.1	2.3	1.8	1.4
Currency and Deposits	-0.8	-0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Securities other than shares	4.7	4.5	4.2	5.2	3.3	4.3	2.8	2.1	2.3	1.8	1.4
Other accounts payable	1.2	1.2	0.0	-1.0	0.0	-1.3	0.0	0.0	0.0	0.0	0.0
Foreign Loans	0.9	0.9	1.3	1.3	1.6	1.7	1.4	1.4	0.8	1.1	1.1
Memorandum items:											
Total investment (including capital transfers)	7.1	7.0	6.8	6.8	6.2	6.2	7.3	7.8	8.1	8.4	8.6

Sources: Ministry of Economy and Finance; and IMF staff estimates.

1/ Refers to the macro framework for the 3rd review in CR/14/66.

2/ Revised macro framework. More disaggregated data which were not available at the time of the 1st review have allowed for an enhanced classification of goods and services and grants as per GFSM 2001 guidelines.

3/ Includes capital transfers to public entities.

Table 4. Morocco: Budgetary Central Government Balance Sheet, 2011–19

(Billions of dirhams)

	2011	2012	2013 PLL 1/	2013 Rev. 2/	2014 PLL 1/	2014 Rev. 2/	2015 Proj.	2016 Proj.	2017 Proj.	2018 Proj.	2019 Proj.
Net financial worth	-428.9	-493.3	-481.9	-550.7	-581.9	-594.9	-638.0	-677.8	-717.9	-760.6	-800.5
Financial assets	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Domestic	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Currency and deposits 3/	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Foreign	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Liabilities	430.9	495.3	540.4	552.7	583.9	596.9	639.9	679.8	719.9	762.6	802.5
Domestic	331.3	378.4	414.4	422.9	442.5	451.4	480.3	505.7	537.2	566.2	592.0
Securities other than shares 3/	331.3	378.4	415.6	424.0	446.7	463.7	491.4	513.5	539.1	560.5	579.1
Foreign	99.6	116.9	126.0	129.8	141.4	145.5	159.7	174.1	182.7	196.4	210.5
Loans 3/	99.6	114.2	126.0	129.8	141.4	145.5	159.7	174.1	182.7	196.4	210.5
Memorandum Item:											
GDP	802.6	827.5	883.5	872.8	941.5	919.7	981.9	1,054.3	1,134.6	1,222.0	1,316.1

Sources: Moroccan authorities; and IMF staff estimates.

1/ Refers to the macro framework for the 3rd review in CR/14/66.

2/ Revised macro framework.

3/ Data for the remaining instruments are currently not available.

Table 5. Morocco: Balance of Payments, 2011–19

(In billions of U.S. dollars, unless otherwise indicated)

	2011	2012	2013 PLL 1/	2013 Rev. 2/	2014 PLL 1/	2014 Rev. 2/	2015 Proj.	2016 Proj.	2017 Proj.	2018 Proj.	2019 Proj.
Current account	-8.0	-9.3	-7.8	-7.9	-7.4	-7.7	-7.1	-6.7	-6.2	-6.7	-6.5
Trade balance	-19.3	-20.1	-20.0	-20.4	-20.9	-21.2	-21.6	-22.4	-23.4	-24.4	-25.4
Exports, f.o.b.	21.6	21.4	21.8	22.0	23.8	23.8	25.9	28.4	31.2	34.3	37.7
Agriculture	3.5	3.5	3.8	3.9	4.0	4.2	4.4	4.7	5.1	5.5	5.9
Phosphates and derived products	6.0	5.5	4.7	4.7	5.0	4.6	5.0	5.6	6.3	7.0	7.7
Imports, f.o.b.	-40.9	-41.5	-41.9	-42.3	-44.7	-45.0	-47.5	-50.8	-54.6	-58.7	-63.1
Energy	-11.2	-12.3	-12.2	-12.1	-13.0	-12.8	-13.3	-13.9	-14.7	-15.6	-16.6
Capital goods	-8.4	-8.4	-9.2	-9.4	-9.9	-10.4	-10.9	-11.8	-12.7	-13.8	-14.8
Food products	-4.8	-4.8	-4.2	-4.3	-4.5	-4.7	-4.7	-5.0	-5.5	-5.8	-6.1
Services	5.3	5.2	5.7	5.6	6.4	6.3	7.1	8.2	9.1	10.1	10.9
Tourism receipts	7.3	6.7	6.9	6.8	7.4	7.4	8.0	8.8	9.5	10.4	11.2
Income	-2.0	-2.2	-1.9	-1.8	-2.2	-2.3	-2.4	-2.6	-2.6	-2.7	-2.7
Transfers	8.0	7.7	8.4	8.7	9.3	9.5	9.7	10.1	10.7	10.3	10.8
Private transfers (net)	7.7	7.4	7.8	7.9	8.0	8.1	8.5	8.9	9.5	10.1	10.6
Workers' remittances	7.1	6.7	6.9	6.9	7.1	6.9	7.3	7.7	8.2	8.8	9.3
Official grants (net)	0.3	0.2	0.6	0.8	1.2	1.4	1.2	1.2	1.2	0.2	0.2
Capital account	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	5.7	6.2	9.2	8.9	7.8	9.4	8.5	8.7	8.3	9.3	9.1
Direct investment	2.4	2.3	3.0	3.0	3.4	2.8	3.2	3.5	3.9	4.3	4.6
Privatization	0.7	0.4	0.0	0.0	0.0	-0.3	0.0	0.0	0.0	0.0	0.0
Portfolio investment	-0.2	0.1	0.2	0.2	0.2	0.2	0.3	0.3	0.3	0.3	0.3
Other	3.5	3.7	5.9	5.7	4.3	6.4	5.0	4.9	4.1	4.6	4.2
Private	1.9	1.0	3.4	3.2	1.4	2.1	2.2	2.3	2.2	2.1	1.6
Public medium-and long-term loans (net)	1.7	2.7	2.6	2.5	2.9	4.3	2.8	2.7	1.9	2.5	2.6
Disbursements	3.2	4.3	4.3	4.3	4.8	6.1	4.7	4.5	4.5	4.5	4.5
Amortization	-1.5	-1.6	-1.7	-1.8	-1.9	-1.8	-1.9	-1.9	-2.6	-2.0	-1.9
Reserve asset accumulation (-increase)	2.6	3.5	-1.4	-1.4	-0.4	-1.7	-1.4	-2.0	-2.1	-2.6	-2.6
Errors and omissions	-0.3	-0.3	0.0	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
(Percent of GDP)											
Current account	-8.0	-9.7	-7.4	-7.6	-6.5	-6.8	-5.8	-5.1	-4.4	-4.4	-3.9
Trade balance	-19.4	-20.9	-19.0	-19.6	-18.1	-18.8	-17.7	-17.0	-16.5	-16.0	-15.4
Exports, f.o.b.	21.8	22.3	20.7	21.2	20.7	21.1	21.2	21.5	22.0	22.4	22.9
Agriculture	3.6	3.7	3.6	3.7	3.5	3.8	3.6	3.6	3.6	3.6	3.6
Phosphates and derived products	6.0	5.7	4.4	4.5	4.4	4.1	4.1	4.3	4.4	4.6	4.7
Imports, f.o.b.	-41.2	-43.3	-39.7	-40.8	-38.8	-40.0	-38.9	-38.5	-38.5	-38.4	-38.4
Petroleum	-11.3	-12.9	-11.5	-11.7	-11.3	-11.3	-11.0	-10.6	-10.4	-10.2	-10.1
Capital goods	-8.5	-8.8	-8.7	-9.1	-8.6	-9.2	-9.0	-9.0	-9.0	-9.0	-9.0
Food products	-4.8	-5.0	-4.0	-4.1	-3.9	-4.2	-3.9	-3.8	-3.9	-3.8	-3.7
Services	5.4	5.5	5.4	5.4	5.5	5.6	5.9	6.2	6.4	6.6	6.6
Tourism receipts	7.3	7.0	6.5	6.6	6.4	6.6	6.6	6.7	6.7	6.8	6.8
Income	-2.1	-2.3	-1.8	-1.7	-1.9	-2.0	-1.9	-2.0	-1.9	-1.8	-1.7
Transfers	8.1	8.0	8.0	8.4	8.0	8.4	8.0	7.7	7.5	6.7	6.6
Private transfers (net)	7.7	7.8	7.4	7.7	7.0	7.2	7.0	6.8	6.7	6.6	6.4
Workers' remittances	7.2	7.0	6.6	6.7	6.2	6.1	6.0	5.8	5.8	5.8	5.6
Official grants (net)	0.3	0.3	0.6	0.7	1.1	1.2	1.0	0.9	0.8	0.1	0.1
Capital account	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	5.7	6.4	8.7	8.6	6.8	8.4	6.9	6.6	5.9	6.1	5.5
Direct investment	2.4	2.4	2.9	2.9	2.9	2.5	2.6	2.6	2.8	2.8	2.8
Privatization	0.7	0.4	0.0	0.0	0.0	-0.2	0.0	0.0	0.0	0.0	0.0
Portfolio investment	-0.2	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Other	3.6	3.9	5.6	5.5	3.7	5.7	4.1	3.8	2.9	3.0	2.5
Private 3/	1.9	1.0	3.2	3.1	1.2	1.9	1.8	1.7	1.5	1.4	1.0
Public medium-and long-term loans (net)	1.7	2.9	2.4	2.4	2.5	3.8	2.3	2.0	1.4	1.7	1.6
Disbursements	3.2	4.5	4.1	4.1	4.1	5.4	3.8	3.4	3.2	3.0	2.8
Amortization	-1.5	-1.7	-1.6	-1.7	-1.6	-1.6	-1.5	-1.4	-1.8	-1.3	-1.2
Memorandum items:											
Exports of goods and services (percentage growth)	3.9	-1.3	5.4	4.7	8.4	11.8	8.5	8.8	8.5	8.5	8.6
Imports of goods and services (percentage growth)	7.4	-1.1	0.7	1.1	7.0	7.5	5.9	7.0	6.9	6.9	6.8
Current account balance excluding official grants (percent of GDP)	-8.4	-10.0	-8.0	-8.3	-7.5	-8.1	-6.8	-6.0	-5.2	-4.5	-4.0
Terms of trade (percentage change)	2.3	-11.9	-2.8	-2.6	0.7	-2.9	0.1	0.5	0.1	0.2	0.2
Gross official reserves 3/	20.6	17.5	19.3	19.3	20.0	21.1	22.7	24.7	26.8	29.3	32.0
In months of prospective imports of GNFS	5.0	4.2	4.3	4.3	4.3	4.5	4.5	4.6	4.6	4.7	4.8
In percent of the Assessing Reserve Adequacy (ARA) metric	109.9	87.0	…	89.3	…	91.1	92.3	95.2	98.5	102.6	107.7
Debt service (percent of export of GNFS and remittances) 4/	5.3	5.8	6.6	6.7	6.7	6.6	6.3	6.2	7.0	5.5	5.0
External public and publicly guaranteed debt (percent of GDP) 5/	23.6	25.7	26.5	26.9	27.4	29.3	29.8	29.7	29.0	28.6	28.1
DHs per US$, period average	8.1	8.6	8.4	8.4	…	…	…	…	…	…	…
GDP (US$)	99.2	95.9	105.5	103.8	115.1	112.6	121.9	131.8	141.8	152.8	164.5
Oil price (US$/barrel; Brent)	111.0	112.0	108.9	108.8	109.5	107.9	104.0	99.8	97.0	95.3	94.1

Sources: Ministry of Finance; *Office des Changes*; and IMF staff estimates and projections.

1/ Refers to the macro framework for the 3rd review in CR/14/66.

2/ Revised macro framework.

3/ Excluding the reserve position in the Fund.

4/ Public and publicly guaranteed debt.

5/ Ratio calculated using debt stock and GDP in dirhams.

Table 6. Morocco: Monetary Survey, 2011–15

	2011	2012	2013 PLL 1/	2013 Rev. 2/	2014 PLL 1/	2014 Rev. 2/	2015
	(Billions of dirhams)						
Net foreign assets	173.6	148.1	159.6	150.3	162.7	164.5	175.4
Monetary authorities	171.9	145.4	156.8	153.2	159.9	167.3	178.1
Of which : Gross reserves	177.1	147.9	159.3	156.9	162.4	173.6	184.4
Of which : Net Fund position	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Deposit money banks	1.7	2.7	2.8	-3.0	2.8	-2.8	-2.7
Net domestic assets	775.7	844.1	871.2	870.1	915.6	901.8	944.2
Domestic credit	781.0	833.2	881.3	877.7	930.0	911.6	957.6
Net credit to the government	93.0	113.3	125.6	130.1	131.9	130.8	140.3
Banking system	93.0	113.3	125.6	130.1	131.9	130.8	140.3
Bank Al-Maghrib	2.2	0.5	0.2	0.8	-0.2	0.6	0.2
Of which : deposits	-3.4	-4.5	-4.7	-4.6	-5.1	-4.8	-5.2
Deposit money banks	90.8	112.9	125.4	129.2	132.0	130.2	140.1
Credit to the economy	688.1	719.8	755.6	747.7	798.1	780.8	817.2
Other liabilities, net	5.4	-10.9	10.0	7.6	14.4	9.8	13.3
Broad money	949.3	992.2	1,030.9	1,020.4	1,078.3	1,066.3	1,119.6
Money	586.8	612.2	645.5	625.7	680.5	657.6	702.7
Currency outside banks	158.3	163.6	174.6	171.6	186.0	180.8	193.1
Demand deposits	428.5	448.5	470.9	454.1	494.5	476.8	509.7
Quasi money	340.9	354.7	368.9	371.5	383.7	386.4	401.9
Foreign deposits	21.6	25.3	16.4	23.2	14.1	22.3	15.1
	(Annual percentage change)						
Net foreign assets	-11.8	-14.7	7.8	1.5	1.9	9.5	6.6
Net domestic assets	11.6	8.8	3.2	3.1	5.1	3.6	4.7
Domestic credit	12.0	6.7	3.1	5.3	5.5	3.9	5.0
Net credit to the government	23.8	21.9	8.7	14.8	5.0	0.6	7.3
Credit to the economy	10.6	4.6	3.6	3.9	5.6	4.4	4.7
Broad money	6.4	4.5	3.9	2.8	4.6	4.5	5.0
	(Change in percent of broad money)						
Net foreign assets	-2.6	-2.7	1.2	0.2	0.3	1.4	1.0
Domestic credit	9.4	5.5	2.6	4.5	4.7	3.3	4.3
Net credit to the government	2.0	2.1	1.0	1.7	0.6	0.1	0.9
Credit to the economy	7.4	3.3	2.6	2.8	4.1	3.3	3.4
Other assets net	-0.4	1.7	0.1	-1.9	-0.4	-0.2	-0.3
Memorandum items:							
Velocity (GDP/M3)	0.85	0.83	0.86	0.86	0.87	0.86	0.88
Velocity (non-agr. GDP/M3)	0.73	0.73	0.73	0.73	0.75	0.75	0.76
Credit to economy/GDP (in percent)	85.7	87.0	85.5	85.7	84.8	84.9	83.2
Credit to economy/nonagricultural GDP (in percent)	98.8	99.3	100.5	99.9	98.8	98.2	96.1

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

1/ Refers to the macro framework for the 3rd review in CR/14/66.

2/ Revised macro framework.

Table 7. Morocco: Financial Soundness Indicators, 2008–13
(Percent, unless otherwise indicated)

	2008	2009	2010	2011	2012	2013
Regulatory capital 1/						
Regulatory capital to risk-weighted assets	11.2	11.7	12.3	11.7	12.3	13.3
Tier 1 capital to risk weighted assets	9.6	9.2	9.7	9.6	10.2	11.1
Capital to assets	6.9	7.2	8.3	8.1	8.5	8.7
Asset quality						
Sectoral distribution of loans to total loans						
Industry	18.7	18.3	18.4	18.4	18.1	18.3
Of which : agro-business	...	3.6	3.8	3.4	3.2	3.5
Of which : textile	...	1.9	1.4	1.3	1.2	1.0
Of which : gas and electricity	...	2.9	3.9	4.5	4.8	4.8
Agriculture	4.1	3.4	4.1	4.2	4.1	4.1
Commerce	6.5	7.0	6.7	6.6	6.7	6.1
Construction	15.9	14.1	13.3	13.9	12.6	12.5
Tourism	2.6	3.2	2.9	2.8	2.9	2.4
Finance	13.1	12.5	12.1	11.9	11.0	12.3
Public administration	3.7	4.3	5.0	4.8	5.0	5.2
Transportation and communication	4.5	4.2	4.0	4.1	4.0	3.8
Households	26.5	27.6	28.1	27.6	28.9	29.7
Other	4.4	5.4	5.4	5.5	6.4	5.6
FX-loans to total loans	2.4	2.5	2.5	3.5	2.9	2.8
Credit to the private sector to total loans	93.3	91.0	91.0	92.0	91.0	91.0
Nonperforming Loans (NPLs) to total loans	6.0	5.5	4.8	4.8	5.0	5.9
Specific provisions to NPLs	75.3	74.1	70.1	68.7	67.8	64.0
NPLs, net of provisions, to Tier 1 capital	13.9	12.7	12.2	12.9	13.6	17.0
Large exposures to Tier 1 capital	314.0	376.0	336.0	354.0	347.0	327.0
Loans to subsidiaries to total loans	6.4	6.7	6.1	6.3	5.4	7.2
Loans to shareholders to total loans	2.0	1.0	0.8	1.2	1.0	1.3
Specific provisions to total loans	4.5	4.0	3.4	3.5	3.3	3.8
General provisions to total loans	0.2	0.1	0.2	0.3	0.7	0.6
Profitability						
Return on assets (ROA)	1.2	1.2	1.2	1.1	1.0	1.0
Return on equity (ROE)	16.7	15.2	14.2	13.4	11.8	10.6
Interest rate average spread (b/w loans and deposits)	3.2	3.1	3.3	3.3	3.2	3.2
Interest return on credit	5.8	5.8	5.7	5.7	5.6	5.5
Cost of risk as a percent of credit	0.4	0.5	0.5	0.5	0.8	0.9
Net interest margin to net banking product (NPB) 2/	78.1	76.7	76.3	75.8	76.5	74.0
Operating expenses to NPB	47.8	47.5	46.4	47.9	47.5	47.7
Operating expenses to total assets	1.7	1.7	1.8	1.9	1.8	1.8
Personnel expenses to noninterest expenses	51.9	49.7	49.1	49.4	49.2	48.4
Trading and other noninterest income to NPB	21.9	23.3	23.7	24.2	23.4	26.0
Liquidity						
Liquid assets to total assets	24.4	17.3	12.0	11.7	10.5	12.0
Liquid assets to short-term liabilities	24.7	23.0	16.0	16.1	14.7	16.6
Deposits to loans	113.0	108.0	104.0	99.0	96.1	96.2
Deposits of state-owned enterprises to total deposits	5.1	4.8	5.2	4.8	3.4	1.9
Sensitivity to market risk						
FX net open position to Tier 1 Capital	6.5	13.5	10.3	7.3	7.4	11.3

Source: Bank Al-Maghrib.

1/ Financial Soundness Indicators (FSIs) are calculated according to guidelines of the IMF FSIs compilation guide, 2004.
2/ Net Banking Product (NPB)=net interest margin-commissions paid+commissions received.

Table 8. Morocco: Capacity to Repay Indicators, 2013–20 1/

	2013	2014	2015	2016	2017	2018	2019	2020
		Proj.						
Exposure and repayments (in SDR million)								
GRA credit to Morocco	0.0	2,941.0	3,235.1	3,235.1	2,867.5	1,360.2	110.3	0.0
(In percent of quota)	0.0	500.0	550.0	550.0	487.5	231.2	18.7	0.0
Charges due on GRA credit	0.0	29.3	59.7	65.0	68.6	41.4	8.2	0.6
Principal due on GRA credit	0.0	0.0	0.0	0.0	367.6	1,507.3	1,249.9	110.3
Debt service due on GRA credit	0.0	29.3	59.7	65.0	436.2	1,548.7	1,258.1	110.9
Debt and debt service ratios								
In percent of GDP								
Total external debt	31.1	36.9	37.4	36.9	35.4	33.1	31.3	30.6
Public external debt	27.7	33.6	34.1	33.6	32.2	30.0	28.2	27.6
GRA credit to Morocco	0.0	4.1	4.2	3.9	3.2	1.4	0.1	0.0
Total external debt service	2.7	2.7	2.6	2.6	3.4	3.9	3.4	2.1
Public external debt service	2.5	2.5	2.5	2.4	3.2	3.7	3.2	1.9
Debt service due on GRA credit	0.0	0.0	0.1	0.1	0.5	1.6	1.2	0.0
In percent of gross international reserves								
Total external debt	167.8	197.1	200.8	196.9	187.6	172.6	161.2	152.4
Public external debt	149.6	179.4	183.1	179.6	170.8	156.3	145.3	137.1
GRA credit to Morocco	0.0	21.7	22.4	20.7	17.1	7.5	0.6	0.0
In percent of exports of goods and services								
Total external debt	92.1	118.4	129.7	138.4	143.0	144.3	146.8	154.4
Public external debt	82.1	107.8	118.3	126.3	130.2	130.7	132.3	139.0
GRA credit to Morocco	0.0	13.0	14.5	14.5	13.0	6.2	0.5	0.0
In percent of total external debt								
GRA credit to Morocco	0.0	11.0	11.1	10.5	9.1	4.3	0.3	0.0
In percent of public external debt								
GRA credit to Morocco	0.0	12.1	12.2	11.5	10.0	4.8	0.4	0.0
Memorandum items:								
Nominal GDP (in billions of U.S. dollars)	103.8	112.6	121.9	131.8	141.8	152.8	164.5	177.0
Gross international reserves (in billions of U.S. dollars)	19.3	21.1	22.7	24.7	26.8	29.3	32.0	35.6
Exports of goods and services (in billions of U.S. dollars)	35.1	38.7	42.0	46.0	50.3	55.0	59.8	65.0
Quota (in billions of SDRs)	588.2	588.2	588.2	588.2	588.2	588.2	588.2	588.2

Source: IMF staff estimates and projections.

1/ Assumes a new PLL arrangement of 550 percent of quota (500 percent in the first year and an additional 50 percent in the second year). The Moroccan authorities have expressed their intention to treat the arrangement as precautionary.

Table 9. Morocco: External Financing Requirements
(Millions of US dollars unless specified otherwise)

	T	T+1		T+2	
	Baseline	Baseline	Adverse 1/	Baseline	Adverse 1/
Gross Financing Requirements	9,816	9,682	13,837	9,148	13,939
Current account deficit	7,871	7,689	11,844	7,113	11,904
Trade Deficits	20,378	21,210	23,914	21,613	24,741
Transfers and other deficits	-12,506	-13,520	-12,070	-14,500	-12,838
ST debt amortization (original maturity)	46	46	46	51	51
MLT debt amortization	1,899	1,947	1,947	1,985	1,985
Financing sources	9,816	9,682	13,837	9,148	13,939
FDI (net)	3,027	2,838	2,117	3,170	2,366
Portfolio investment	219	184	18	273	28
Of which : Bond Issuance	0	0	0	0	0
ST debt disbursement	46	51	51	54	54
Change in gross reserves (- accumulation)	-1,399	-1,744	3,232	-1,352	4,428
MLT debt disbursement	4,373	6,378	6,378	4,954	4,954
Other 2/	3,550	1,976	2,041	2,048	2,108
Overall Balance	0	0	0	0	0
Total size of shock in adverse scenario	…	…	4,961	…	5,749
Gross international reserves (GIR)	19,256	21,082	16,121	22,678	16,929
Reserve adequacy metric 3/	21,561	23,136	22,914	24,558	24,309
GIR as percent of reserve adequacy metric	89	91	70	92	70
Excess (+:buffer)/ shortfall (-financing) of GIR relative to 90 percent of reserve-adequacy metric 3/	929	260	-4,502	576	-4,949
Financing gap in percent of quota 4/	N/A	N/A	494	N/A	543

Source: IMF staff estimates and projections.

1/ The adverse scenario assumes: (1) an oil price increase of $20/bb; (2) a decrease of growth in Europe/advanced trade partners of 2.5 percentage points; and (3) FDI 25 percent lower relative to baseline.

2/ Includes commercial credits and net errors and omissions.

3/ The reserve adequacy metric is computed as 30 percent of short-term debt (at remaining maturity) + 15 percent of portfolio liabilities + 10 percent of broad money + 10 percent of exports.

4/ The financing gap is defined as the level of financing support needed to bring gross international reserves to 90 percent of the Fund's reserve adequacy metric, broadly corresponding to the 2014 level under baseline projections, after the shock.

Table 10. Morocco: Proposed Access

	Proposed Arrangement PLL	Proposed Arrangement (Percentile)	High-Access Cases 1/ 20th	65th	80th	Median
			Percentile (Ratio)			
Access						
In millions of SDRs	3,235	35	1,473	11,421	16,076	7,152
Average annual access (percent of quota)	275	41	174	453	652	300
Access during the first year (percent of quota)	500					
Average annual access (percent of total) 2/	275	8	300	800	1,052	579
Total access in percent of: 3/						
Actual quota	550	32	341	802	1,143	644
Gross domestic product	4	19.4	4.2	7.3	9.6	6.3
Gross international reserves	24	11	27	61	88	49
Exports of goods and nonfactor services 4/	12	19	11.6	28.8	39.0	20
Imports of goods and nonfactor services	18	43	10.3	23.8	35.7	19
Total debt stock 5/						
Of which: Public	7	14	9	18	31	13
External	18	69	7	15	22	12
Short-term 6/	355	94	21	51	104	35
M2	4	5	7	15	25	12

Sources: Executive Board documents; MONA database; and IMF staff estimates.

1/ High access cases include available data at approval and on augmentation for all the requests to the Board since 1997 which involved the use of the exceptional circumstances clause or SRF resources. Exceptional access augmentations are counted as separate observations. For the purpose of measuring access as a ratio of different metrics, access includes augmentations and previously approved and drawn amounts.

2/ Correspond to quotas prior to 2008 Reform.

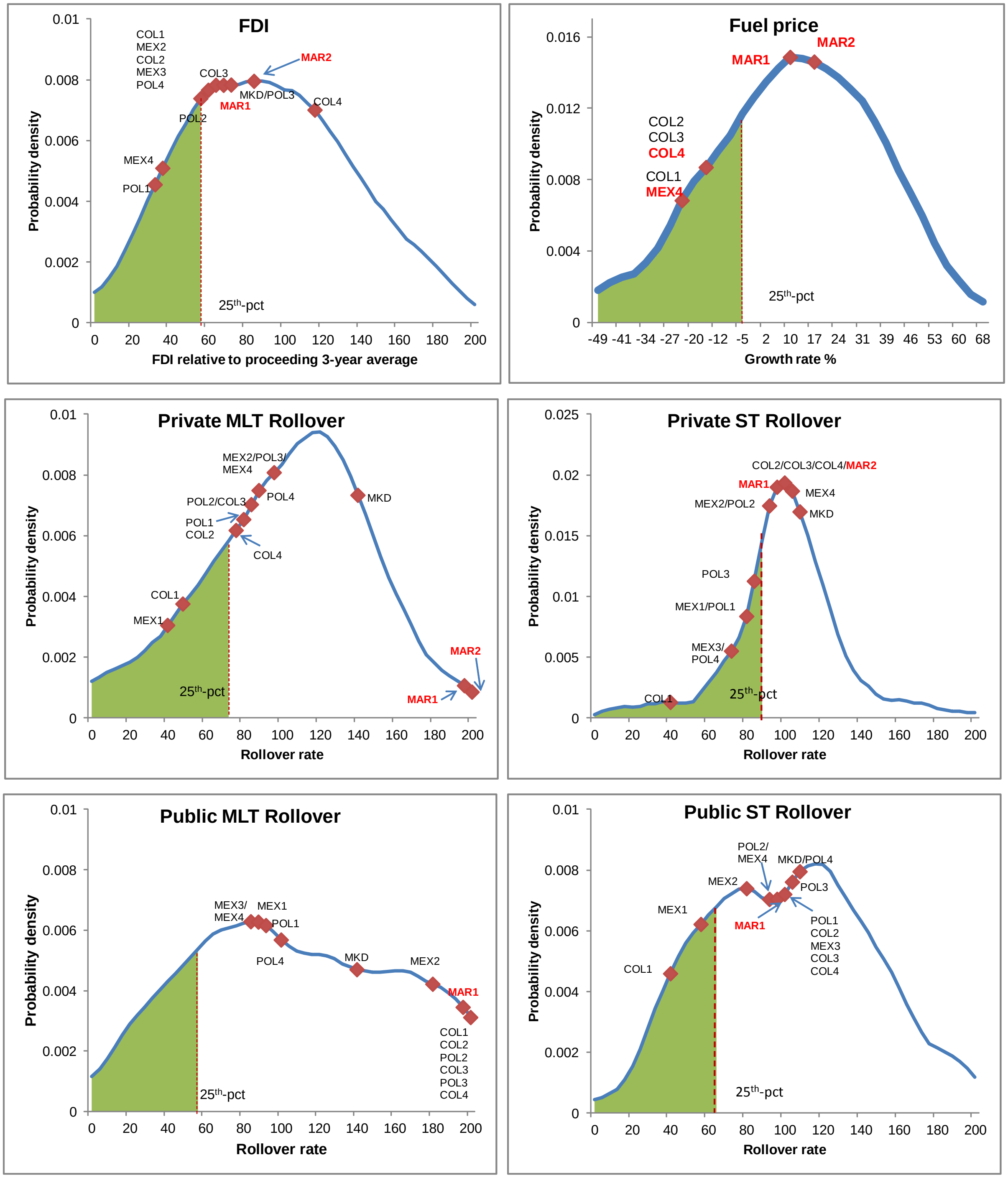
3/ The data used to calculate ratios is the actual value for the year prior to approval for public, external, and short-term debt, and the projection at the time of program approval for the year in which the program was approved for all other variables (projections for 2014 were used).

4/ Includes net private transfers.

5/ Refers to net debt.

6/ Refers to residual maturity.

Figure 3. Morocco: FCL/PLL Cases Compared with Distribution of Historical Shocks to Emerging Markets 1/



Source: IMF staff estimates.

1/Kernel density distributions of the variables are estimated from past exogenous stress episodes for emerging markets. FCL-PLL arrangements shocks parameters are then placed in these empirical distributions. For example, the FDI shock under the current PLL request is a 25 percent reduction relative to the baseline, or an FDI level after shock representing 85 percent of the FDI level of the last three years. This shock is not extreme, as about 50 percent of empirical shocks were more severe than this.

Annex. Morocco: Debt Sustainability Analysis (DSA)

Public DSA

Morocco's public sector gross debt ratio to GDP was on a declining path between 2000 and 2010. However, since then, a combination of external shocks and domestic vulnerabilities has caused the debt ratio to rise. Nevertheless, at about 64 percent of GDP, public debt remains sustainable. The DSA shows the debt level to be resilient to various shocks, and vulnerabilities linked to the profile of the debt appear for the most part moderate. However, gross financing needs have been high (mainly linked to the rollover of existing debt) and have exceeded the benchmark of 15 percent of GDP over the past three years, highlighting some risks despite the relatively moderate level of debt.

1. **This DSA updates the DSA conducted for the 2013 Article IV consultation.**[1] Although the overall picture hasn't changed significantly from the previous analysis, gross financing needs have been revised upward for 2012-13 as a result of updated debt service outturn, including the maturing of two-year treasury bonds issued in 2011. In addition, the relatively large issuance of one-year bonds in 2013 led to a 2 percent increase in the share of short-term debt in the total highlighting some rollover risk. However, the authorities have been actively managing their debt portfolio and maturity profile in order to minimize such risks. As a result, gross financing needs linked to rollover operations are projected to decline in the short and medium term.

2. **After steadily declining over the previous decade, Morocco's public debt-to-GDP ratio started rising in 2010 as macroeconomic performance deteriorated.** Rising international commodity prices contributed to a significant increase in the fiscal deficit, mainly through the cost of higher food and fuel subsidies. Public debt rose from 48 percent of GDP in 2009 to 64 percent in 2013. About half of this increase occurred in 2012 as the economy was severely impacted by the crisis in Europe (Morocco's main trade partner) and higher oil prices, and the authorities encountered difficulties in containing the fiscal deficit. However, the authorities' fiscal consolidation efforts are expected to help bring the debt ratio down toward 60 percent of GDP in the medium term.

3. **Risks to debt sustainability range from low to high (see heat map below).** Baseline projections are realistic when compared to a group of market access countries. Morocco's projected fiscal consolidation efforts aimed at lowering the overall deficit to 3 percent of GDP in the medium term do not appear exceptional relative to the distribution of other country cases. The debt level remains below the debt burden benchmark of 70 percent of GDP for emerging markets when various shocks are assumed.[2] Vulnerabilities linked to the profile of debt are mostly moderate except for an exceptional increase in short-term debt in 2013; relevant

[1] See CR/14/65.

[2] Under a scenario combining all shocks (real GDP, primary balance, real exchange rate, and real interest rate), the debt level would peak just above 70 percent of GDP before declining.

indicators exceed the lower early warning benchmarks but not the upper risk assessment ones (see chart). Gross financing needs exceed the benchmark of 15 percent under the baseline in 2013 (20 percent of GDP) but are expected to decline under the benchmark by 2016. This highlights the importance of continuing on the path of fiscal consolidation to reduce debt-financed deficits and to carefully manage the maturity profile of debt instruments.

Figure 1. Morocco: Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

(in percent of GDP unless otherwise indicated)

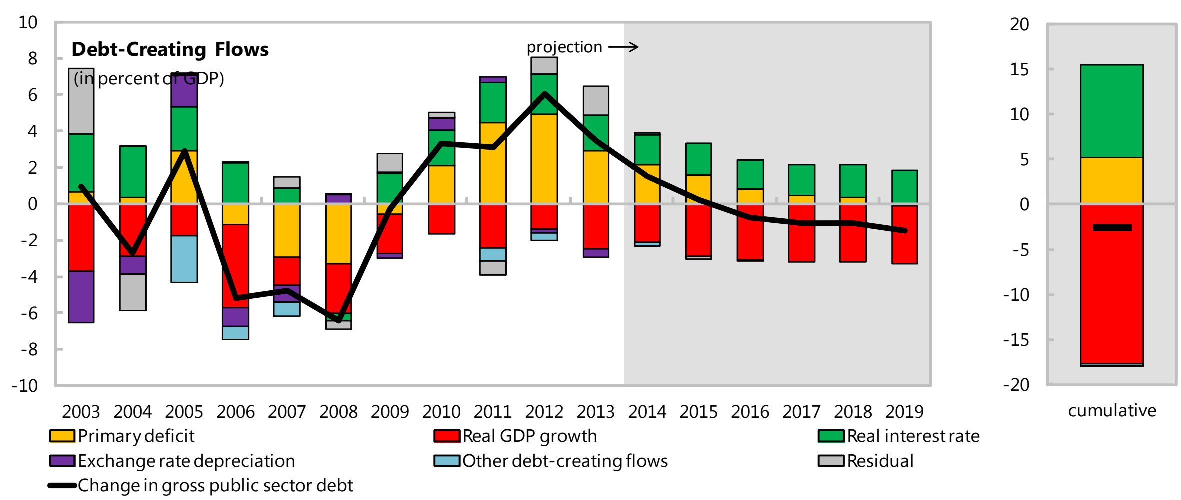
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2003-2011 [2/]	2012	2013	2014	2015	2016	2017	2018	2019
Nominal gross public debt	56.3	60.4	63.9	65.5	65.7	65.0	63.9	62.8	61.4
Public gross financing needs	12.7	17.7	20.0	15.7	15.6	14.4	14.1	13.5	12.9
Real GDP growth (in percent)	4.8	2.7	4.4	3.5	4.7	5.0	5.3	5.4	5.4
Inflation (GDP deflator, in percent)	1.9	0.4	1.0	1.8	2.0	2.2	2.2	2.2	2.2
Nominal GDP growth (in percent)	6.8	3.1	5.5	5.4	6.8	7.4	7.6	7.7	7.7
Effective interest rate (in percent) [4/]	5.4	4.6	4.5	4.6	4.9	4.9	5.1	5.3	5.4

As of June 24, 2014		
Sovereign Spreads		
Spread (bp) 3/		117
CDS (bp)		158
Ratings	Foreign	Local
Moody's	Ba1	Ba1
S&Ps	BBB-	BBB-
Fitch	BBB-	BBB

Contribution to Changes in Public Debt

	Actual			Projections							
	2003-2011	2012	2013	2014	2015	2016	2017	2018	2019	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	-1.0	6.06	3.50	1.5	0.2	-0.7	-1.1	-1.1	-1.5	-2.6	
Identified debt-creating flows	-1.3	5.11	1.91	1.5	0.4	-0.7	-1.1	-1.1	-1.5	-2.4	
Primary deficit	0.3	4.9	2.9	2.1	1.6	0.8	0.4	0.4	-0.1	5.2	-1.3
Primary (noninterest) revenue and gra	27.5	28.7	28.3	27.9	28.1	28.2	28.2	27.9	28.0	168.4	
Primary (noninterest) expenditure	27.8	33.7	31.2	30.1	29.7	29.0	28.6	28.3	27.9	173.6	
Automatic debt dynamics [5/]	-1.0	0.6	-1.0	-0.5	-1.1	-1.5	-1.5	-1.4	-1.3	-7.4	
Interest rate/growth differential [6/]	-0.7	0.8	-0.6	-0.5	-1.1	-1.5	-1.5	-1.4	-1.3	-7.4	
Of which: real interest rate	1.9	2.2	2.0	1.7	1.8	1.6	1.7	1.8	1.8	10.3	
Of which: real GDP growth	-2.6	-1.4	-2.5	-2.1	-2.9	-3.1	-3.2	-3.2	-3.1	-17.7	
Exchange rate depreciation [7/]	-0.3	-0.2	-0.5	…	…	…	…	…	…	…	
Other identified debt-creating flows	-0.5	-0.4	0.0	-0.2	0.0	0.0	0.0	0.0	0.0	-0.2	
CG: Privatization Proceeds (negative)	-0.5	-0.4	0.0	-0.2	0.0	0.0	0.0	0.0	0.0	-0.2	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
(Specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	0.3	1.0	1.6	0.1	-0.2	0.0	0.0	0.0	0.0	-0.1	



Source: IMF staff.

1/ Public sector is defined as central government.

2/ Based on available data.

3/ Bond Spread over U.S. Bonds.

4/ Defined as interest payments divided by debt stock at the end of previous year.

5/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the denominator in footnote 4 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).

8/ For projections, this line includes exchange rate changes during the projection period.

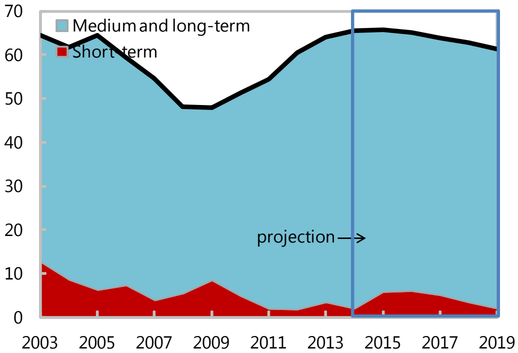
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 2. Morocco: Public DSA - Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

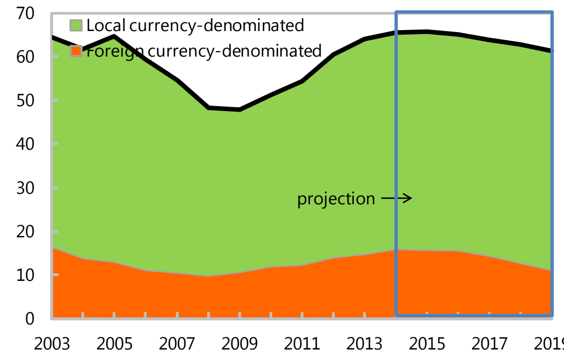
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

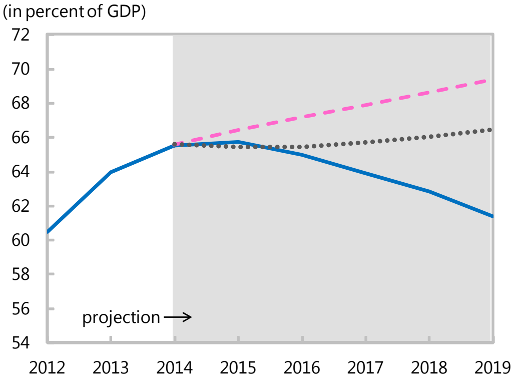


Alternative Scenarios

Baseline Historical Constant Primary Balance

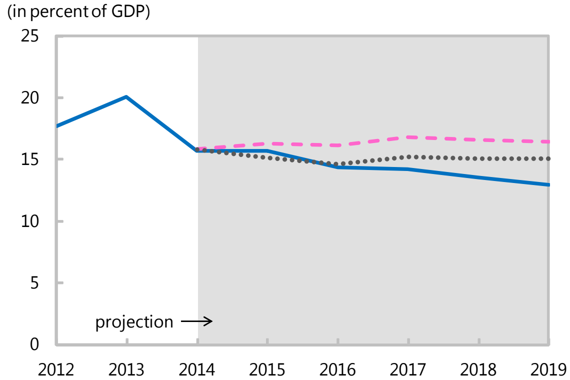
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

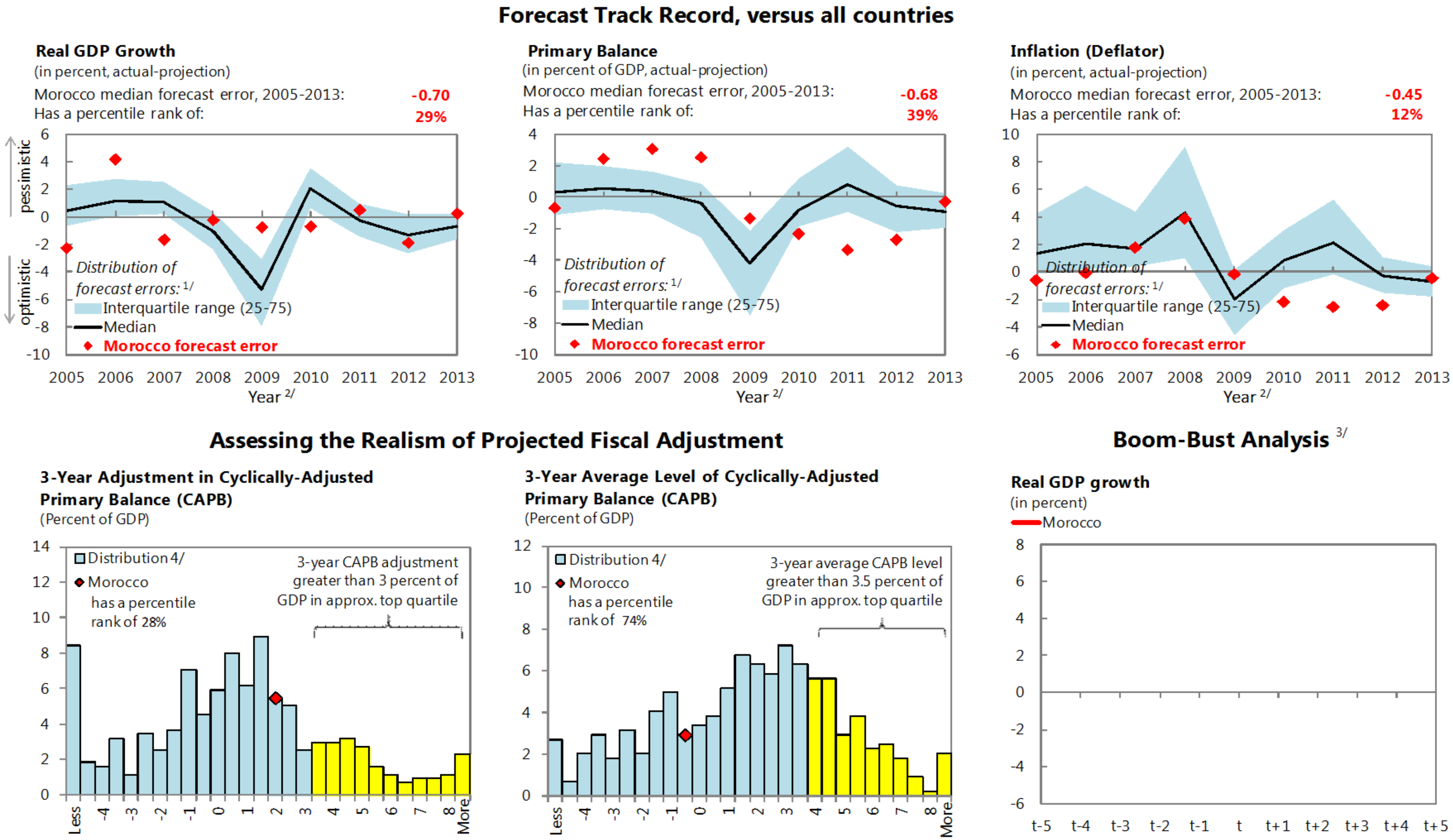
(in percent)

Baseline Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	3.5	4.7	5.0	5.3	5.4	5.4
Inflation	1.8	2.0	2.2	2.2	2.2	2.2
Primary Balance	-2.1	-1.6	-0.8	-0.4	-0.4	0.1
Effective interest rate	4.6	4.9	4.9	5.1	5.3	5.4
Constant Primary Balance Scenario						
Real GDP growth	3.5	4.7	5.0	5.3	5.4	5.4
Inflation	1.8	2.0	2.2	2.2	2.2	2.2
Primary Balance	-2.1	-2.1	-2.1	-2.1	-2.1	-2.1
Effective interest rate	4.6	5.0	5.1	5.3	5.4	5.5

Historical Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	3.5	4.4	4.4	4.4	4.4	4.4
Inflation	1.8	2.0	2.2	2.2	2.2	2.2
Primary Balance	-2.1	-1.0	-1.0	-1.0	-1.0	-1.0
Effective interest rate	4.6	5.0	5.2	5.5	5.7	5.9

Source: IMF staff.

Figure 3. Morocco: Public DSA – Realism of Baseline Assumptions



Source : IMF Staff.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

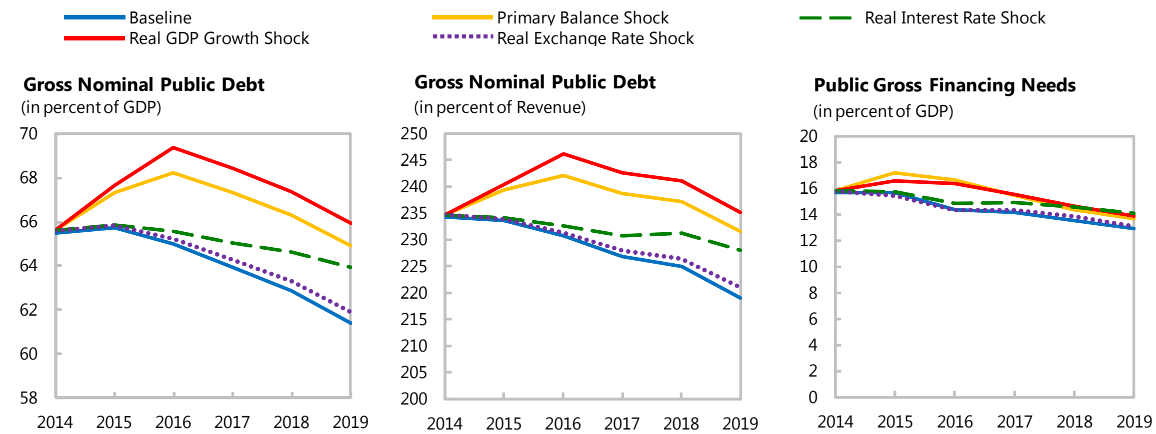
2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Morocco.

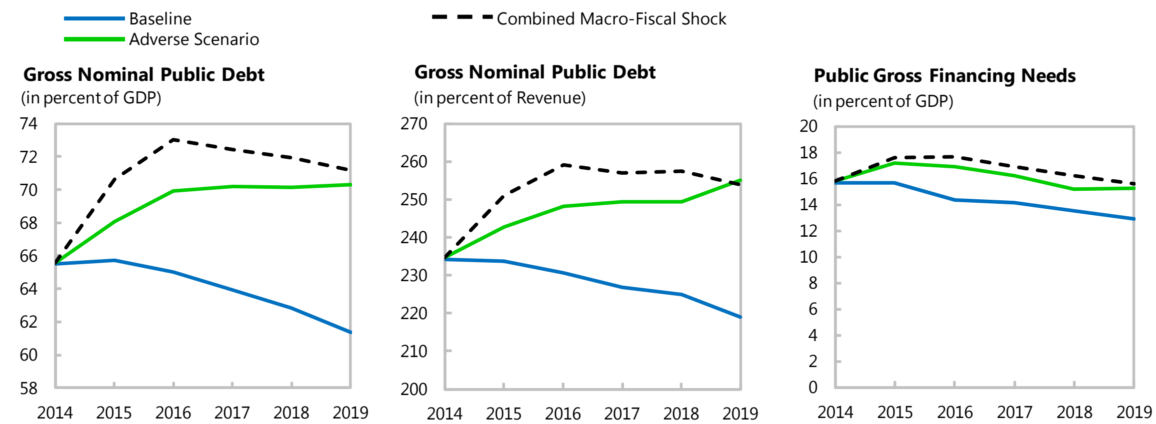
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 4. Morocco: Public DSA - Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions
(in percent)

Primary Balance Shock	2014	2015	2016	2017	2018	2019
Real GDP growth	3.5	4.7	5.0	5.3	5.4	5.4
Inflation	1.8	2.0	2.2	2.2	2.2	2.2
Primary balance	-2.1	-3.0	-2.3	-0.4	-0.4	0.1
Effective interest rate	4.6	5.0	5.2	5.5	5.5	5.6
Real Interest Rate Shock						
Real GDP growth	3.5	4.7	5.0	5.3	5.4	5.4
Inflation	1.8	2.0	2.2	2.2	2.2	2.2
Primary balance	-2.1	-1.6	-0.8	-0.4	-0.4	0.1
Effective interest rate	4.6	5.0	5.6	6.1	6.4	6.7
Combined Shock						
Real GDP growth	3.5	3.2	3.5	5.3	5.4	5.4
Inflation	1.8	1.6	1.8	2.2	2.2	2.2
Primary balance	-2.1	-3.0	-2.3	-0.4	-0.4	0.1
Effective interest rate	4.6	5.1	5.6	6.1	6.4	6.8
Adverse Scenario						
Real GDP growth	3.5	3.1	3.4	3.7	3.8	3.8
Inflation	1.8	2.0	2.2	2.2	2.2	2.2
Primary balance	-2.1	-2.8	-2.1	-0.5	-0.2	-0.3
Effective interest rate	4.6	5.0	5.4	5.7	5.7	5.8

Real GDP Growth Shock	2014	2015	2016	2017	2018	2019
Real GDP growth	3.5	3.2	3.5	5.3	5.4	5.4
Inflation	1.8	1.6	1.8	2.2	2.2	2.2
Primary balance	-2.1	-2.1	-1.9	-0.4	-0.4	0.1
Effective interest rate	4.6	5.0	5.2	5.4	5.5	5.6
Real Exchange Rate Shock						
Real GDP growth	3.5	4.7	5.0	5.3	5.4	5.4
Inflation	1.8	5.3	2.2	2.2	2.2	2.2
Primary balance	-2.1	-1.6	-0.8	-0.4	-0.4	0.1
Effective interest rate	4.6	5.1	5.1	5.3	5.5	5.6

Source: IMF staff.

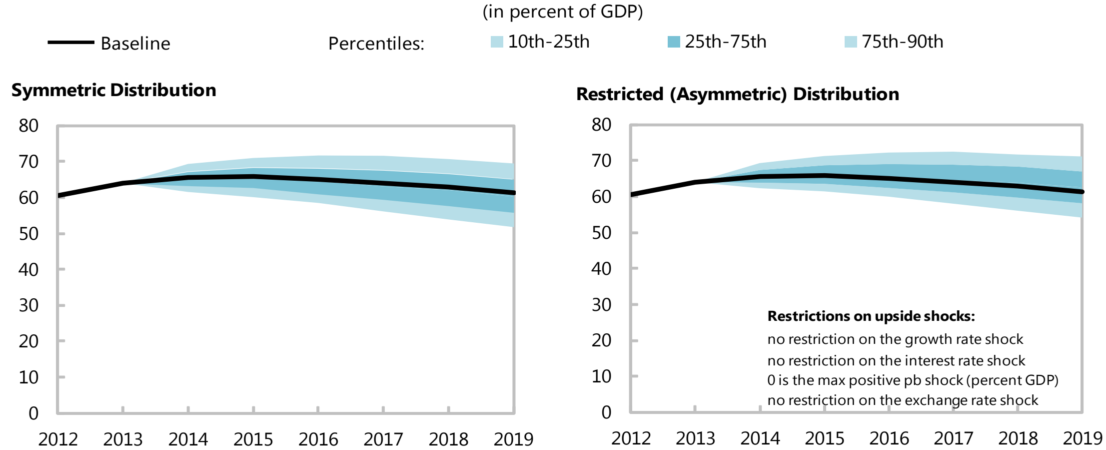
Figure 5. Morocco: Public DSA - Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term	Public Debt Held by Non-Residents	Foreign Currency Debt

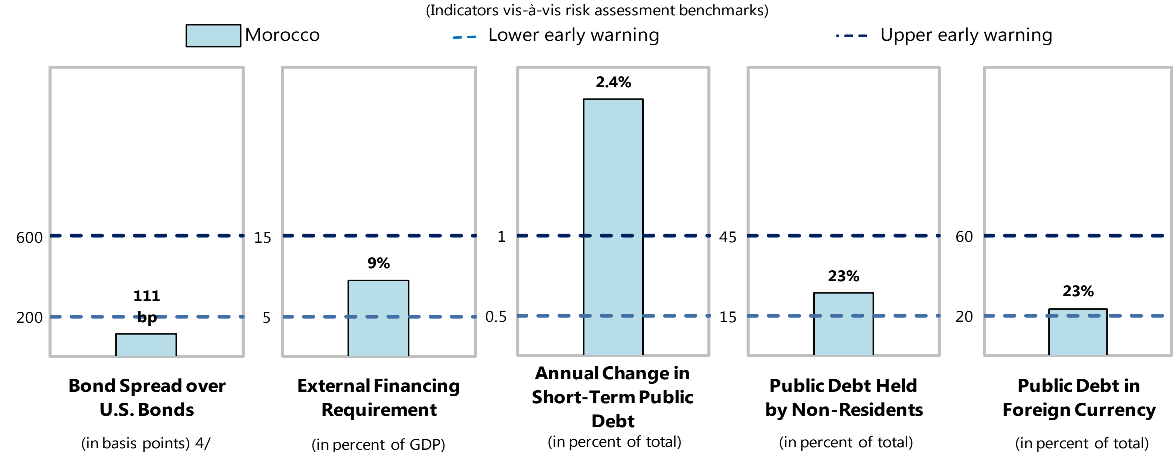
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70 percent is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15 percent is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

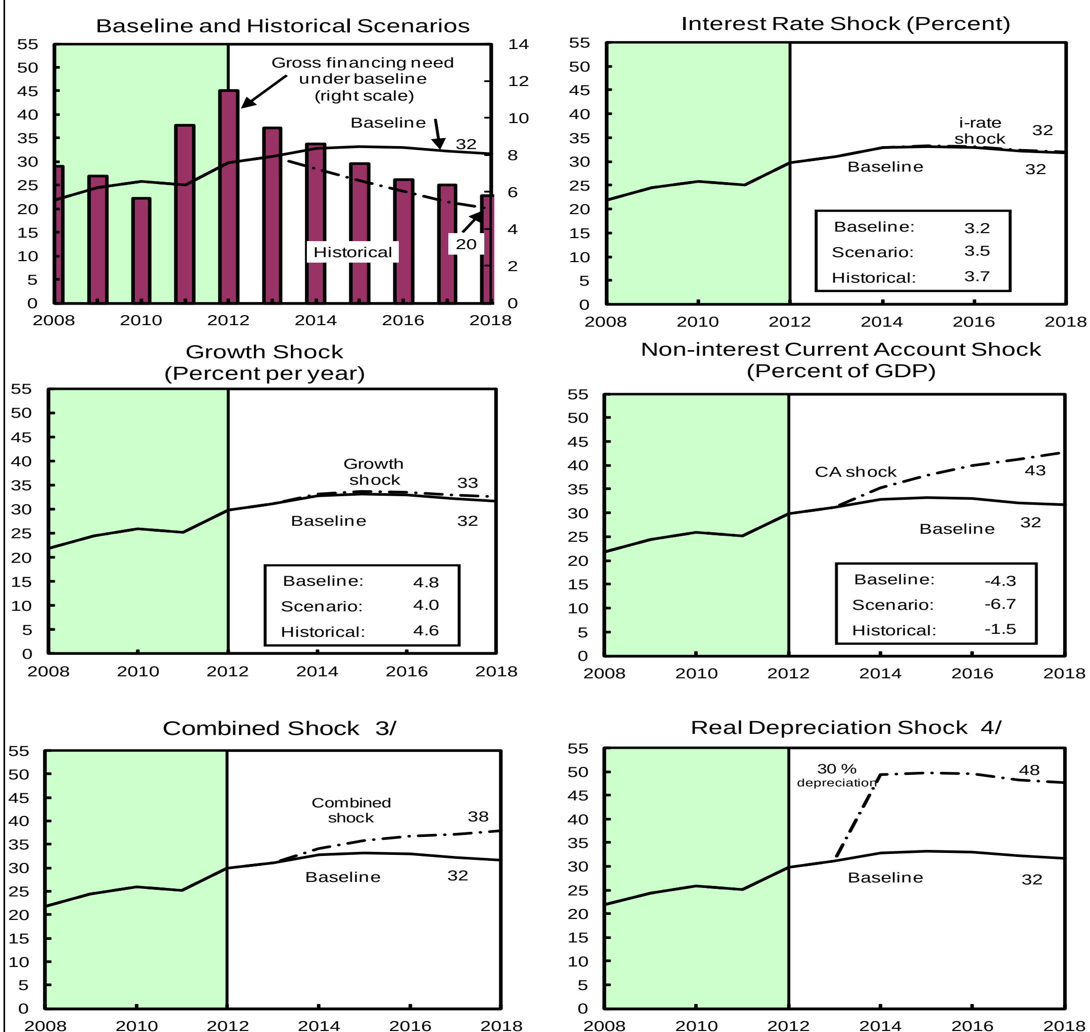
200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ An average over the last 3 months, 26-Mar-14 through 24-Jun-14.

External DSA

Morocco's external debt-to-GDP is expected to remain stable over the medium-term, but some vulnerabilities exist. After rising rapidly between 2010 and 2012, external debt would decline and then stabilise around 32 percent of GDP in 2018. However, with a 30 percent exchange rate depreciation—the most extreme shock—the debt-to-GDP ratio would increase to 48 percent. The shock to interest rates would also result in a significant increase of debt to GDP (43 percent), indicating that the country could be vulnerable to volatility in the international bond market.

Morocco: External Debt Sustainability: Bound Tests 1/ 2/
(External debt in percent of GDP)



Sources: IMF country desk data, and IMF staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2014.

Morocco: External Debt Sustainability Framework, 2008–18

(Percent of GDP, unless otherwise indicated)

	Actual					Projections					
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Baseline: External debt	21.8	24.4	25.8	25.1	29.8	**31.1**	**32.9**	**33.2**	**33.0**	**32.2**	**31.7**
Change in external debt	-3.2	2.6	1.4	-0.7	4.7	1.3	1.7	0.3	-0.2	-0.8	-0.5
Identified external debt-creating flows (4+8+9)	-0.7	3.3	3.2	3.7	8.1	3.2	3.1	1.6	0.7	-0.2	-0.3
Current account deficit, excluding interest payments	4.3	4.6	3.4	7.3	8.9	6.7	5.9	4.9	4.1	3.4	3.4
Deficit in balance of goods and services	14.4	12.0	10.8	14.1	15.4	14.3	13.3	11.9	10.8	10.1	9.4
Exports	37.6	28.9	33.4	35.8	36.1	33.8	34.3	34.5	34.9	35.5	36.0
Imports	52.1	40.9	44.2	49.9	51.5	48.1	47.6	46.3	45.7	45.5	45.3
Net non-debt creating capital inflows (negative)	-2.1	-1.6	-0.9	-2.2	-2.5	-3.1	-2.7	-2.8	-2.9	-3.0	-3.1
Automatic debt dynamics 1/	-3.0	0.3	0.7	-1.4	1.7	-0.3	-0.1	-0.5	-0.5	-0.6	-0.7
Contribution from nominal interest rate	0.9	0.8	0.7	0.8	0.8	0.9	0.9	0.9	1.0	1.0	0.9
Contribution from real GDP growth	-1.2	-1.0	-0.9	-1.2	-0.7	-1.2	-1.0	-1.4	-1.5	-1.6	-1.6
Contribution from price and exchange rate changes 2/	-2.7	0.5	0.9	-1.0	1.6	...	...	...	...	...	...
Residual, including change in gross foreign assets (2-3) 3/	-2.5	-0.7	-1.8	-4.4	-3.4	-2.0	-1.4	-1.2	-0.9	-0.6	-0.2
External debt-to-exports ratio (in percent)	58.0	84.5	77.3	70.2	82.7	92.1	95.7	96.3	94.5	90.7	88.2
Gross external financing need (in billions of US dollars) 4/	6.6	6.2	5.1	9.5	11.0	9.8	9.7	9.1	8.8	9.0	8.8
Percent of GDP	7.4	6.9	5.7	9.6	11.5	9.5	8.6	7.5	6.6	6.4	5.8
Scenario with key variables at their historical averages 5/						**31.1**	**28.5**	**25.9**	**23.6**	**21.5**	**19.9**
Key Macroeconomic Assumptions Underlying Baseline											
Real GDP growth (percent)	5.6	4.8	3.6	5.0	2.7	4.4	3.5	4.7	5.0	5.3	5.4
GDP deflator in US dollars (change in percent)	11.9	-2.4	-3.7	4.1	-5.8	3.7	4.7	3.4	2.9	2.2	2.2
Nominal external interest rate (percent)	4.2	3.9	2.9	3.4	3.3	3.2	3.2	3.1	3.4	3.2	3.1
Growth of exports (US dollar terms, percent)	22.6	-21.4	15.4	17.1	-2.6	1.5	10.1	8.7	9.5	9.3	9.2
Growth of imports (US dollar terms, percent)	33.7	-19.7	7.8	23.4	-0.2	1.1	7.3	5.4	6.7	7.2	7.2
Current account balance, excluding interest payments	-4.3	-4.6	-3.4	-7.3	-8.9	-6.7	-5.9	-4.9	-4.1	-3.4	-3.4
Net non-debt creating capital inflows	2.1	1.6	0.9	2.2	2.5	3.1	2.7	2.8	2.9	3.0	3.1

Sources: IMF country desk data; and IMF staff estimates.

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

Appendix. Written Communication

Rabat, Morocco July 11, 2014

Madame Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Madame Managing Director :

1. Despite a difficult external environment, Morocco's economic performance over the past two years has been satisfactory. Between 2011 and 2013 economic growth was on average 4 percent; inflation stayed below 2 percent; the budget deficit was reduced by 1.2 percent of GDP; foreign exchange reserves stabilized; and the current account deficit was reduced considerably in 2013. The unemployment rate stood at around 9 percent on average, but youth unemployment has remained high. The financial system has remained sound. Conditions for access to international financial markets have remained favorable for both the public and private sectors.

2. In the past two years, the precautionary and liquidity line (PLL) has responded well to Morocco's needs. The PLL has supported our economic strategy by providing insurance against external risks and by strengthening investor confidence. However, significant risks continue to weigh on the global economy, in particular from our main partners' growth, financial market volatility, and energy prices. Accordingly, we are requesting IMF support in the form of a new PLL arrangement covering 24 months in the amount of SDR 3.2351 billion (550 percent of quota), of which SDR 2.941 billion (500 percent of quota) would be available during the first twelve months. We also wish to cancel the current arrangement approved on August 3, 2012, effective upon approval of the new PLL arrangement. Morocco intends to treat the new arrangement as precautionary, and does not intend to draw on this line except in the event of unforeseen exogenous shocks or a significant worsening of the world economy. The reduction in the level of access compared with the first PLL arrangement, from about SDR 4.1 to SDR 3.2 billion, is testimony to the strengthening of our economic fundamentals over the period covered by the first arrangement, and the attenuation of the risks facing Morocco.

3. The objective of our program that would be supported by the new arrangement is to strengthen macroeconomic stability and promote stronger and more job-rich growth. In order to strengthen macroeconomic stability, we will continue to reduce vulnerabilities in the fiscal and external sectors, notably by reducing the fiscal and current account deficits, which will contribute to increasing international reserves and strengthening the economy's resilience.

4. In terms of fiscal policy, the government is committed to continue to press on with the gradual reduction of the budget deficit to 3 percent of GDP by 2017, with intermediate objectives of 4.9 percent of GDP in 2014 and 4.3 percent of GDP in 2015. Tax revenues should increase slightly over the medium term in percent of GDP. The reduction of the budget deficit will nonetheless be achieved mainly through ongoing efforts to rationalize government expenditure, prioritizing pro-growth expenditures on investment in infrastructure and human capital, and social programs. The government is committed to taking the measures needed to achieve the fiscal deficit target set for 2014, and to creating additional space, to the extent possible, for financing priority spending.

5. As regards revenues, a reform of the tax system is under way to make it more equitable and supportive of competitiveness, in accordance with the action plan agreed following the recent National Tax Conference ("Assises Fiscales"). In that context, and with a view to easing corporate cash-flow, the 2014 budget law introduced a number of measures in particular on the establishment of a procedure for reimbursement of the value-added tax (VAT) credit resulting from the "*règle du butoir*" and the elimination of the one-month time lag for deduction of VAT. Through the 2015 budget, the government will continue to simplify the VAT regime and reduce tax expenditures, in particular through a progressive taxation of the agricultural sector, which has already started under the current budget.

6. The government is committed to reducing the cost of the generalized subsidies system to less than 3 percent of GDP by 2016. The significant measures that were taken in 2012 and 2013, notably the introduction of the indexation mechanism in September 2013, helped bring the subsidy bill down from 6.6 percent of GDP in 2012 to 4.8 percent of GDP in 2013 and substantially reduced fiscal risks. Furthermore, last February subsidies on super gasoline and industrial fuel were eliminated, and in February and April, the per-unit subsidy on diesel was reduced. The reduction of the diesel subsidy will be continued throughout the remainder of 2014, with quarterly adjustments, leading to its complete elimination in 2015. Moreover, within the framework of the program contract to restore the financial viability of the national electricity and drinking water utility (ONEE), the subsidies on fuel for electricity generation were eliminated on June 1, 2014 and will be temporarily replaced by direct transfers to the ONEE, which will be capped in nominal terms and eliminated in 2017. Furthermore, we are examining the possible progressive reduction of the butane subsidy, by introducing incentives for using renewable energy sources, as well as measures to gradually reduce the subsidy on soft wheat flour. In parallel, social protection of the most vulnerable groups will continue to be broadened, in particular under dedicated programs such as RAMED (health sector) and TAYSSIR (education sector).

7. The government's objective over the medium term is to gradually reduce the civil service wage bill, including employer contributions, to below 11 percent of GDP. The strategy adopted for reaching this objective includes measures related to limiting the budget impact of net creation of new positions, salary advances, and promotions. This strategy also includes increasing the mobility of civil servants as part of the public sector modernization plan, and which will help control the wage bill.

8. A draft organic budget law (OBL) was passed in the first chamber of Parliament on July 8 2014, and has been submitted to the second chamber. The government will make every effort to ensure that amendments that may be introduced to the draft law strengthen the budget framework, and that the OBL is adopted in the course of this session of Parliament. As such, the 2015 budget could be prepared under the new budget framework—subject to approval of the OBL by the Constitutional Court. The new OBL improves the budget framework, notably through the introduction of multi-year budgeting and of a fiscal rule limiting new borrowing to the financing of capital spending and debt amortization, the establishment of program budgeting, and the strengthening of results-based management and fiscal transparency. It also makes wage expenditures appropriations binding ceilings, reduces the carryover of investment appropriations, and imposes tighter rules for the creation and maintenance of the special Treasury accounts. Moreover, in order to shield the budget from changes that other laws could introduce, a new provision has been introduced into the draft OBL, by virtue of which only finance laws may modify tax and customs provisions. Although the provisions of the new OBL are to be implemented in a gradual manner, the measures taken in 2013 to limit risks related to the carryover of investment appropriations and the wage bill will be rolled over until the entry into force of the relevant provisions of the new OBL. Strengthening of the budget framework will be pursued through the implementing regulations of the OBL.

9. A significant parametric reform of the Moroccan Retirement Fund (CMR) was announced on June 18, 2014 in the national commission in charge of the pension system reform. The legislation needed for its implementation is being prepared, and will be submitted for approval with a view to its entry into force in 2015. The parametric reform includes modifications with regard to the statutory retirement age, contribution rates and retirement benefits. It will extend the sustainability of the CMR and will ensure a balance between contributions and benefits immediately upon its entry into force. Over the medium term, the institutional structure is expected to shift toward a bipolar system (private sector/public sector).

10. Monetary policy conducted by Bank Al-Maghrib (BAM) will continue to aim at ensuring price stability and at providing under appropriate conditions the necessary liquidity for the financing of the economy. To that end, BAM has strengthened its mechanism for facilitating access to financing for very small, small, and medium-sized enterprises (VSSME), notably for those in industrial sectors and those whose production is export-oriented. Moreover, a new support fund has been created for the VSSME and intermediate-sized enterprises that are viable but are experiencing temporary difficulties. The banking sector continues to show its resilience. BAM will continue to strengthen bank supervision, through the implementation of the Basel III standards, and to closely monitor the potential risks linked to the presence of Moroccan banks in sub-Saharan Africa, in cooperation with the relevant authorities in the host countries, including through joint audit missions and a consolidated supervision of the banking groups. A draft banking law adopted last month by the first chamber of Parliament aims at broadening the bank regulatory and supervisory role of BAM, strengthening the macro-prudential and crisis resolution frameworks, defining the regulatory and supervisory frameworks for participatory banks, strengthening banks' governance, and improving the management of the deposits insurance system. The charter of BAM is likewise under revision,

with a view to increasing its independence and broadening its remit, notably by including its contribution to financial stability. In this regard, the framework for monitoring the stability of the financial system under normal circumstances has been undergoing continuous improvement since its establishment by BAM and its partners. Furthermore, the crisis simulation exercise, carried out once again in partnership with the World Bank in May 2014, produced satisfactory results. An update of the Financial Sector Assessment Program is expected in the spring of 2015.

11. The peg of the dirham against a euro/dollar basket has served Morocco well by providing an important nominal anchor. We believe that greater flexibility in the exchange rate regime, well-coordinated with other macroeconomic policies and appropriate structural reforms, would provide more levers to the economy to address exogenous shocks, as well as strengthen competitiveness and promote trade diversification and the country's economic and financial integration with the world economy. We are at present studying the possibility of introducing greater flexibility in the exchange rate regime over the course of the next three years, by defining a new nominal anchor for monetary policy, once impacts have been properly evaluated and preconditions met. In addition to the progress achieved on the operational front and in the supervision of foreign exchange activities and coverage of the related risks, BAM is in the process of strengthening its analytical capacities in regards inflation forecasting, in preparation for moving to a new monetary regime.

12. The authorities are implementing ambitious structural reforms to improve competitiveness and potential growth and boost employment creation. The objective of the recently announced industrial acceleration strategy is to move to a higher growth path by increasing the contribution of the industrial sector to GDP and job creation. This strategy aims at capitalizing on the ongoing geographical and sectoral diversification of exports, in particular in the food-processing, automobile, aviation, and offshoring sectors, and at increasing the integration of the productive fabric through encouragement of industrial offsets and import substitution. The business climate will continue to be improved, and the country's attractiveness for direct foreign investment reinforced further. Economic governance will be improved by the implementation of the new law on public procurement, which applies also to public enterprises since 2014, as well as by the entry into effect of the laws on the Competition Council and on price liberalization, adopted by Parliament last June. The reform under way in the judicial system aims to boost judicial independence and effectiveness and to improve transparency. The active employment policies undertaken by the government are being adapted, following the completion of their evaluation. At the same time, the labor code is currently being discussed with the social partners, with the dual objective of making it more favorable to job creation, while at the same time ensuring adequate protection of workers.

13. We will provide the IMF with all the information needed in order to monitor economic and policy developments within the framework of the PLL arrangement, in particular with respect to information relating to the indicators enumerated in Table 1 and in the attachment. In line with the requirements of the PLL, we will also observe the standard criteria related to trade and exchange restrictions, bilateral payments agreements, multiple currency practices, and nonaccumulation of external debt payment arrears.

14. We are confident that the policies described in this communication are adequate to achieve the objectives of the economic program supported by the PLL arrangement, and we will take all additional measures that are seen to be necessary to that end. Continued strengthening of the economy's resilience, including by further reducing the fiscal and external deficits and strengthening the reserve position, is expected to position Morocco well for exiting the PLL, once the exogenous risks to which the economy is exposed have significantly declined. Morocco will engage with the IMF, in accordance with relevant Fund policies, towards the success of our economic policies.

/s/

Mohamed Boussaïd
Minister of Economy and Finance

/s/

Abdellatif Jouahri
Governor of Bank Al-Maghrib

Table 1. Morocco: Quantitative Indicative Targets

	9/30/14	3/31/15
	Target	
Indicative targets		
Net international reserves (NIR) of Bank Al-Maghrib (BAM) 1/ (end-of-period (eop) stock, in millions of U.S. dollars (US$))	20,310	20,492
Fiscal deficit (cumulative since beginning of fiscal year, eop in millions of dirham)	-32,768	-10,556
Memorandum item:		
Adjustor on NIR (in millions of U.S. dollars) 2/	1,628	3,513
Adjustor on the fiscal deficit (in millions of dirham) 3/	8,200	2,619

Source: IMF staff estimates.

1/ Evaluated at the program exchange rate for both years 2014 and 2015 (end-March 2014, 8.1496 MAD/US$).

2/ Adjustments are specified in the technical appendix. The floor on NIR of BAM will be adjusted downward (upward) in the event of a shortfall (surplus) of official grants and loans received by the central government from bilateral and multilateral agencies relative to program projections. The adjustors for 2014 are cumulative from end-March 2014.

3/ Adjustments are specified in the technical appendix. The fiscal deficit ceiling will be adjusted upward (downard) in the event of a shortfall (surplus) of budgetary grants received by the central government from bilateral and multilateral agencies relative to program projections. The adjustors for 2014 are cumulative from end-December 2013. The adjustors for 2015 are cumulative from end-December 2014.

Table 2. Morocco: Schedule and Terms Under the Precautionary and Liquidity Line Arrangement

Review Date	Conditions for access	Indicative targets 1/ Central government fiscal deficit, ceiling, cumulative since beginning of fiscal year (eop in millions of dirham) 2/	Indicative targets 1/ Net international reserves (NIR) of Bank Al-Maghrib (BAM), floor, eop stock, in millions of U.S. dollars (US$) 3/	Credit Available 4/ Million SDR 5/	Credit Available 4/ Million Dollars 6/	Credit Available 4/ Percent of Quota, cumulative	Credit Available 4/ Percent of Total Access
July 28, 2014	Board approval of the PLL			2,941	4,548	500	91
January 27, 2015	First review, based on September 30, 2014 indicative targets	-32,768	20,310	2,941	4,548	500	91
July 27, 2015	Second review, based on March 31, 2015 indicative targets	-10,556	20,492	3,235	5,003	550	100
January 27, 2016	Third review, based on September 30, 2015 indicative targets	to be set in the first review	to be set in the first review	3,235	5,003	550	100
Total				3,235	5,003	550	100

Source: IMF staff estimates.

1/ Evaluated at the program exchange rate (end-March 2014 8.1496 MAD/US$) for 2014 and 2015.
2/ The adjustors are specified in the Technical Appendix.
3/ The adjustors are specified in the Technical Appendix.
4/ Credit available assuming no purchase.
5/ Full access will be available on July 27, 2015.
6/ SDR/Dollar Exchange rate of 0.646625 as of May 19, 2014.

Attachment: Technical Appendix

1. Under the first year of the PLL arrangement, quantitative indicative targets as defined in Table 1 of our written communication will be set for end-September 2014 and end-March 2015. They include:

- Floor on the level of net international reserves (NIR) of Bank Al-Maghrib (BAM), as defined in Table 2, calculated as an end-of-period stock. The exchange rate that will be used to monitor NIR during the first year of the program is Moroccan dirham (MAD) 8.1496 per U.S. dollar, the rate prevailing on March 31, 2014. Foreign currency accounts denominated in currencies other than the U.S. dollar and monetary gold will be valued in U.S. dollars at the exchange rates and gold prices prevailing on March 31, 2014. BAM will report to the IMF the level of NIR and gross international reserves (GIR) no later than one week after the end of each week both at the program exchange rates and at the market exchange rates.

- Ceiling on the level of the fiscal deficit of the central government defined as revenues, including grants, less expenditure less net acquisition of nonfinancial assets as reported in the Government Finances Statistics Manual 2001 format, calculated as a cumulative flow from January 1st of each calendar year. The central government is defined as all budgetary units of the central government. It includes the central government budget, special treasury accounts and autonomously managed government services (SEGMA). The Ministry of Economy and Finance will report to the IMF in monthly and cumulative flows from January 1 of each year the fiscal deficit, including grants, but excluding net acquisition of shares and other equity (privatization receipts) and the relevant budget aggregates (revenues, expenditures, etc.) for each month before the end of the following month.

2. The indicative targets on NIR will be adjusted downward (upward) by the amount below (above) official grants and loans received by the central government from bilateral and multilateral agencies relative to program projections. The indicative targets on the fiscal deficit will be adjusted upward (downward) by the amount below (above) budgetary grants received by the central government from bilateral and multilateral agencies relative to program projections as indicated in Table 1 of our written communication.

3. Regarding the continuous zero ceiling on the accumulation of new external payment arrears during the duration of the arrangement, the payment arrears are defined as external debt-service obligations (principal and interest) that have not been paid at the time that are due as specified in the contractual agreements, on central government and central government-guaranteed debt. Overdue debt and debt-service obligations that are in dispute will not be considered as external payment arrears.

4. Assuming the approval of this arrangement by the IMF Executive Board on July 28, 2014, the reviews will be completed by no later than January 27, 2015 for the first review, July 27, 2015 for the second review, and January 27, 2016 for the third review.

Definition of GIR and NIR of BAM for the Purpose of Monitoring Indicative Targets

Gross international reserves are defined as the sum of:

- Foreign currency assets in convertible currencies held abroad, and as vault cash that are under the direct and effective control of BAM, readily available for intervention in the foreign exchange market or the direct financing of the balance of payments;
- The reserve position of Morocco in the IMF;
- Holding of SDRs; and
- Monetary gold.

Excluded from the definition of GIR are:

- Foreign currency assets that are in any way encumbered or pledged, including, but not limited to, reserve assets used as collateral or guarantee for third-party external liabilities;
- Foreign currency assets in nonconvertible currencies and precious metals other than gold;
- Foreign currency claims on entities incorporated in Morocco;
- Any other foreign currency claims on residents; and
- Capital subscriptions in international institutions.

NIR is defined as GIR less:

- All outstanding liabilities of Morocco to the IMF, excluding SDR allocation; and
- Foreign currency liabilities in convertible currencies to nonresidents and contingent commitments to sell foreign exchange arising from transactions in derivative assets, including forward contracts, foreign currency swaps, and other futures market contracts.

MOROCCO

ASSESSMENT OF THE IMPACT OF THE PROPOSED PRECAUTIONARY AND LIQUIDITY LINE ARRANGEMENT ON THE FUND'S FINANCES AND LIQUIDITY POSITION

July 14, 2014

Approved By
Andrew Tweedie and Mark Flanagan

Prepared by the Finance and Strategy, Policy, and Review Departments

CONTENTS

INTRODUCTION

1. **This note assesses the impact of the proposed Precautionary Liquidity Line (PLL) arrangement for Morocco on the Fund's finances and liquidity position, in accordance with the policy on exceptional access.**[1] The authorities wish to cancel the current arrangement upon approval of the proposed PLL. This arrangement would be the second under the PLL for Morocco, and would cover a 24-month period beginning July 28, 2014, with access in an amount up to SDR 3,235 million (550 percent of quota) available in one or more purchases. Of this access, an amount equivalent to SDR 2,491 million (500 percent of quota) would be available in the first year of the arrangement and the balance of SDR 294 million would be made available at the beginning of the second year, subject to the completion of the relevant six-monthly reviews.[2] Morocco does not have an actual balance of payments need and intends to treat the arrangement as precautionary.

PAST USE OF FUND RESOURCES

2. **Morocco's first PLL, which provided access of 700 percent of quota, was approved on August 3, 2012.** (See Annex I for prior use of Fund resources). As originally envisaged at the time of approval, Morocco has not drawn on its PLL; it is scheduled to expire on August 2, 2014. Morocco made progress reducing its fiscal and current account deficits, and reserves have kept pace with the growth of risk-weighted liabilities. While the program remained broadly on track, a more challenging than expected external environment and weaknesses in public financial management led to a higher than programmed fiscal deficit in 2012. In the context of fiscal deficit reduction, prices on several subsidized petroleum products were increased and partially indexed to international prices, although the over-all cost of subsidies remained somewhat higher than originally programmed. The authorities continue to work towards a new Organic Budget Law to modernize and fully address revealed weaknesses in public financial management.

RISKS AND IMPACT ON FUND FINANCES

3. **Morocco's total external debt has increased recently but remains manageable.** Total external debt is estimated to increase over 6 percentage points of GDP since 2010 to almost 32 percent in 2014 (see Table 1, Figure 1 Panel A). Nearly all of this is public or publically guaranteed debt, which amounts to about 29 percent of GDP. The public and private sectors'

[1] See paragraph 5 of Decision No. 14064-(08/18), February 22, 2008, as amended, and *The Acting Chair's Summing Up- Review of Access Policy under the Credit Tranches and the Extended Fund Facility, and Access Policy in Capital Account Crises - Modifications to the Supplemental Reserve Facility and Follow-Up Issues Related to Exceptional Access Policy* (3/5/03) http://www.imf.org/external/np/sec/pn/2003/pn0337.htm.

[2] After the first six months of the arrangement, any purchases are subject to completion of six-monthly reviews under the PLL arrangement.

short-term debt on a residual maturity basis is small, limiting any roll-over risk. Under the baseline scenario, in which the PLL remains precautionary, public external debt is projected to peak at 30 percent and decline in the second half of the program and fall to 28 percent by 2019, consistent with a substantial improvement in the fiscal deficit by 2016. Relative to other precautionary programs, Morocco has relatively low external debt and a low external debt service burden reflecting the near absence of private external debt (Figure 1, panels A & C). Sustainability analyses show both external and public debt remaining manageable under a range of scenarios, including the adverse scenario, though the combined macro-fiscal shock reflects the highest and possibly destabilizing risk.

Table 1. Morocco: External Debt Structure, 2008-2012 1/

	2010	2011	2012	2013	2014 (proj.)
	(In Billions of US$)				
Total External Debt	23.5	24.9	28.6	32.3	37.1
Public	20.8	22.0	25.2	28.8	33.2
Short-term 2/	1.4	1.6	1.8	1.8	1.9
Long-term	19.4	20.4	23.4	27.0	31.4
Private	2.7	2.9	3.4	3.5	3.7
Short-term 2/	0.2	0.2	0.2	0.2	0.2
Long-term	2.5	2.7	3.2	3.3	3.5
	(In Percent of GDP)				
Total External Debt	25.8	25.1	29.8	31.1	32.9
Public	22.9	23.6	25.7	26.9	29.3
Short-term 2/	1.6	1.7	1.8	1.7	1.6
Long-term	21.4	21.9	23.9	25.2	27.7
Private	2.9	1.5	4.1	4.2	3.6
Short-term 2/	0.2	0.2	0.2	0.2	0.2
Long-term	2.7	1.3	3.9	4.0	3.4

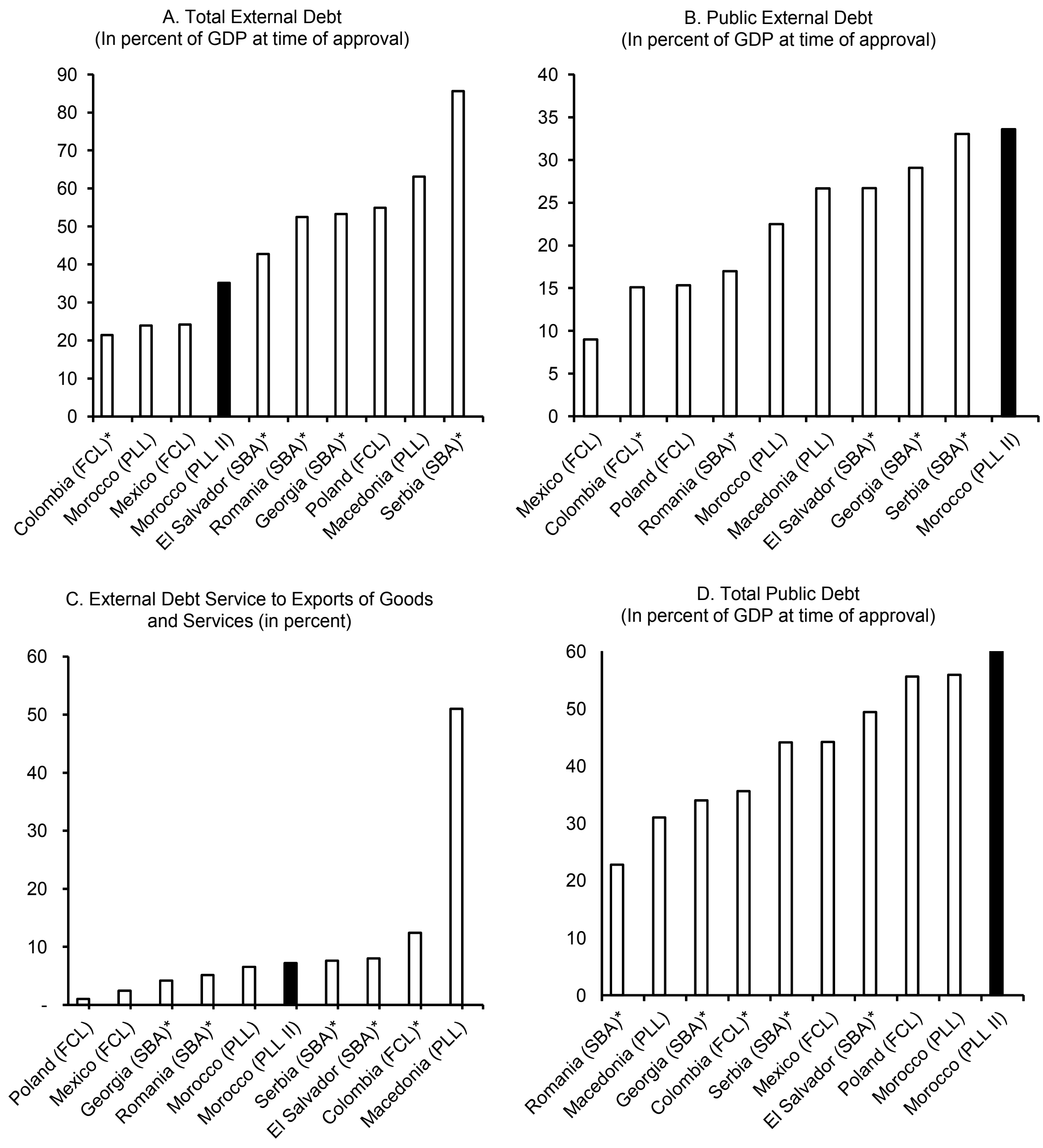
Source: Moroccan Authorities and IMF staff estimates.
1/ End of year unless otherwise indicated.
2/ Including residual maturity medium- and long-term debt.

4. **Morocco's public debt ratios on the other hand are relatively high compared to other recent precautionary arrangements.** Morocco's total public external debt tops the peer group (Figure 1, panel B). Morocco's total public sector debt, including domestic debt, has increased substantially and, although sustainable, continues to be among the highest of recent precautionary arrangements, reflecting an area of potential—though limited—risk to the program and Morocco's capacity to repay the Fund (Figure 1, panel D). This points to the critical importance of the authorities' fiscal program—which focus on fiscal consolidation (targeting a fiscal deficit of 3 percent of GDP in 2017), a reduction in subsidies and the public wage bill, pension reform, and strengthening the budgetary framework. This perspective is consistent with the Public Debt Sustainability Assessment in the staff report, which suggests that a two year delay in adjusting the primary fiscal balance would raise the public debt peak to near 70 percent of GDP, and combined with a GDP growth shock, the public debt peak would approach 74 percent and would remain above 70 percent through 2019.

5. The structure of Morocco's medium-term capital flows suggest limited vulnerability to capital account shocks relative to other recent precautionary arrangements. Figure 2 suggests that Morocco's integration into international capital markets is lower than comparators and that export earnings are not substantially concentrated. As shown in Table 2, short-term external debt is low in nominal terms and in percent of reserves relative to Morocco's peer group (Figure 2, panel A). Panel B suggests that Morocco has little net inflows of hot money that are susceptible to fast reversals; in fact, non-residents often sell more Moroccan assets than they purchase, creating net negative or nearly zero combined portfolio and other liability flows over five years. Foreign direct investment inflows,[3] which tend to be a relatively stable component of the capital account, relative to financing needs from the current account, and export concentration by trading partner place Morocco more or less in the middle of the comparators (Figure 2, panels C and D).

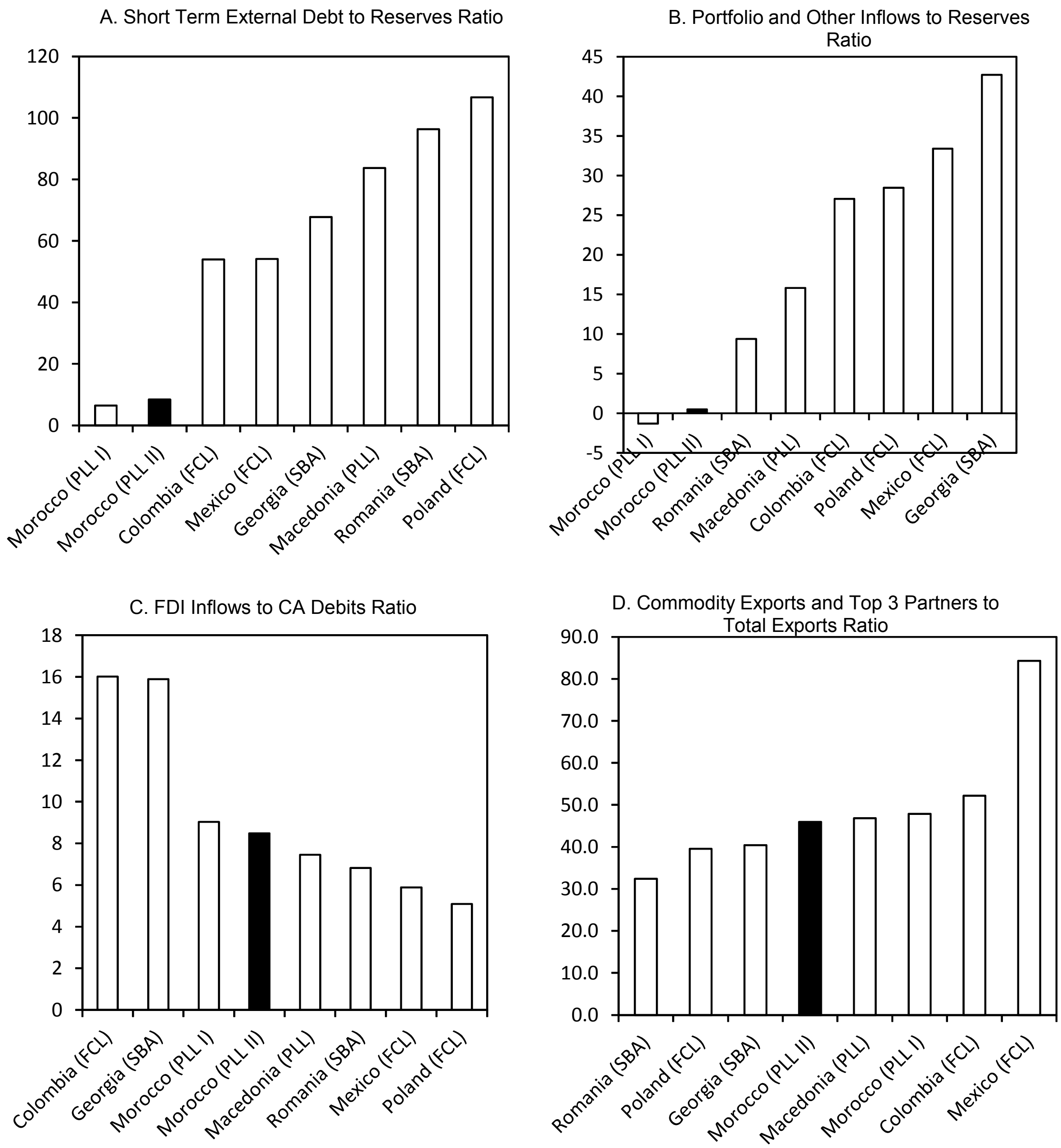
[3] While Panel C of Figure 2 is designed to facilitate cross-country comparisons and focuses on FDI, relatively stable inflows of remittances at over 6 percent of GDP are an important source of external financing for Morocco.

Figure 1. Debt Ratios for Recent Precautionary Arrangements 1/



Source: IMF Staff calculations.
1/ Estimates as reported in each staff report on the request of the arrangement.

Figure 2. Morocco: Medium-Term BOP Ratios 1/



Source: Staff calculations, IFS, WEO, and JEDH.

1/ Five year averages ending the first full year immediately prior to the most recent program.

6. Morocco has lower reserve coverage relative to other precautionary arrangements, though the scenarios that analyze external shocks suggest that it has only a moderate risk of needing to draw from the Fund. Table 2 illustrates nominal reserves and reserves as a share of risk weighted liabilities using the Fund's framework for assessing reserve adequacy.[4] The table also illustrates the impact on reserves of a shock to external flows based on the magnitude of historical shocks, using the methodology used to determine access.[5]

- Morocco's international reserves in relation to risk-weighted liabilities (RAM) at 92 percent falls far short of other members with exceptional access, precautionary arrangements.[6]
- On the other hand, Morocco's relatively low external flows suggest that Morocco's external financing short-fall and proportionate decline in reserves (to 73 percent) in a stressed environment is low relative to other precautionary users (Figure 2, panel B also suggests that Morocco's external flows are unlikely to be vulnerable to abrupt reversals).
- For comparison, Macedonia, which drew on its PCL, had a more comfortable level of reserves at the start of its arrangement (103 percent), but its relatively high external flows pointed to a higher ex ante need to draw on Fund credit, as, in the illustrative shock scenario, international reserves fell to 23 percent of RAM.

Table 2. Probability of Drawing: External Flows, Shocks, and Reserve Adequacy (billions of US dollars)

	Morocco PLL II	Morocco PLL	Colombia FCL	Mexico FCL	Poland FCL	Romania FCL	Macedonia PLL
	2014			2012			2011
International Reserves	21	18	36	161	104	41	2.3
Risk-Weighted Liability Stock (RAM) 1/	23	21	24	135	77	27	2.3
ST Debt	2.1	1.9	22	82	94	46	2.6
Exports	39	35	66	386	225	67	5.7
M2	133	116	148	860	298	66	5.4
Other Portfolio Liabilities	35	35	67	483	226	63	2.7
International Reserves in percent of RAM	***92***	***84***	***152***	***119***	***134***	***154***	***103***
Shock Scenarios at 25th Percentile 2/							
External Financial Short-Fall	-4.6	-2.6	-16	-45	-36	-15	-2.0
International Reserves in percent of RAM 3/	***73***	***71***	***86***	***87***	***92***	***104***	***23***

Source: Staff calculations. International Financial Statistics and Staff Reports requesting respective arrangements.
1/ Weighted as 30, 10, 5 and 5 percent (floating exchange rate systems) or 30, 15, 10, and 10 percent (other exchange rate systems) for short-term debt, other portfolio liabilities, broad money, and exports, respectively.
2/ Twenty-fifth percentile of univariate kernal distribution for declines of exports, FDI, and short- and medium-term debt roll-over rates consistent with historical crises. See *Review of the Flexible Credit Line and Precautionary Credit Line* (11/1/2011).
3/ Assumes 100% absorption of external financial short-fall by reserves without exchange rate adjustment.

[4] *Assessing Reserve Adequacy - Further Considerations* (11/14/13) http://www.imf.org/external/np/pp/eng/2013/111313d.pdf .

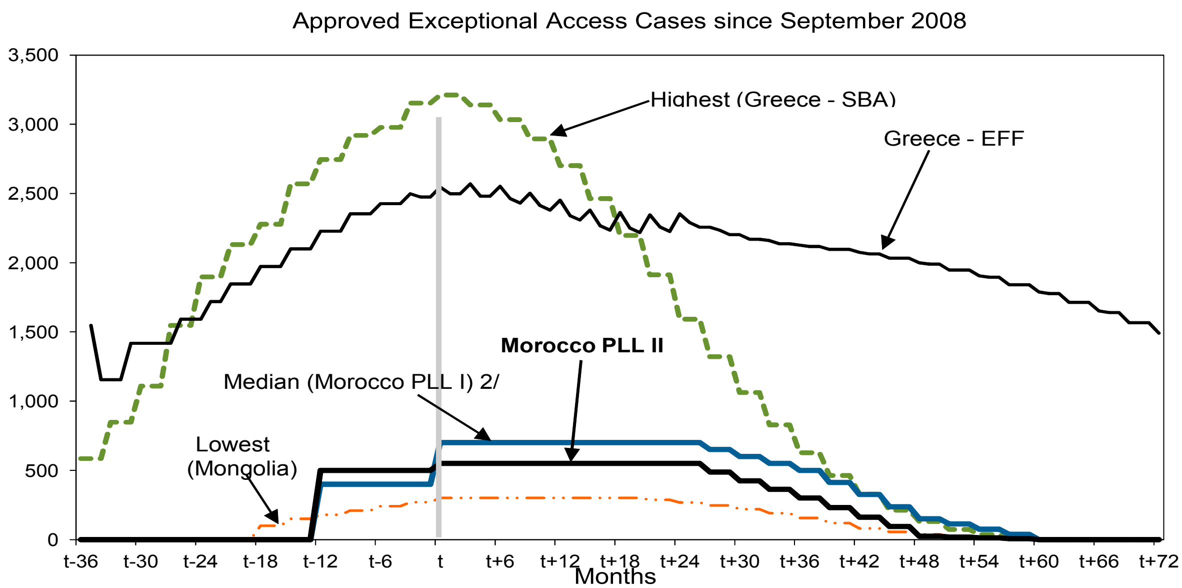
[5] *Review of the Flexible Credit Line and Precautionary Credit Line* (11/1/2011) http://www.imf.org/external/np/pp/eng/2011/110111.pdf. Also, see Box 2 and Table 9 of the current Staff Report requesting the PLL for Morocco.

[6] However, due to the non-convertibility of the Dirham and limited capital controls, a lower ARA metric for reserves of 85% instead of 100% is considered relevant. See *Morocco—Request for an Arrangement Under the Precautionary and Liquidity Line*, Box 5 (7/28/2012) http://www.imf.org/external/pubs/ft/scr/2012/cr12239.pdf.

7. If the full amount available under the proposed PLL arrangement were to be purchased:[7]

- **Access would be slightly below the median and significantly below the mean exposure of recent exceptional access cases, and far below the access of recent crisis resolution programs (Figure 3).** Morocco's outstanding use of GRA resources would reach SDR 2,941 million in the first year and SDR 3,235 million in the second year (Table 3).
- **Fund credit would represent a modest share of Morocco's low external debt (Table 3).** Assuming full purchases, total external debt is projected to rise to 37 percent of GDP, and public external debt would rise to 34 percent of GDP. At its peak, Morocco's outstanding use of GRA resources would account for about 12 percent of public external debt and over 22 percent of gross international reserves.
- **External debt service would increase moderately over the medium-term but remain manageable under staff's medium-term macroeconomic projections (Table 3)**. Morocco's projected debt service to the Fund would peak in 2018 at a manageable level of SDR 1,549 million, equivalent to about 1.6 percent of GDP, almost 9 percent of gross international reserves, and under 5 percent of exports.

Figure 3. Fund Credit Outstanding around Peak Borrowing 1/
(In percent of quota)



Source: IFS, Finance Department, and IMF staff estimates.

1/ Peak borrowing 't' is defined as the highest level of credit outstanding for a member. Repurchases are assumed to be on an obligations basis. For illustrative purposes, assumes Morocco makes full purchases of available commitment.
2/ Median credit outstanding at peak is 700 percent of quota; average is 1,022 percent of quota.

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[7] The figures on debt service used in this report are calculated assuming that 500% of quota is purchased upon approval of the arrangement, with an additional 50% of quota purchased a year later, and that all repurchases are made as scheduled.

Table 3. Morocco: Capacity to Repay Indicators 1/

	2012	2013	2014	2015	2016	2017	2018	2019
Exposure and Repayments (In SDR millions)								
GRA credit to Morocco 2/	-	-	2,941	3,235	3,235	2,867	1,360	110
(In percent of quota)	-	-	500	550	550	488	231	18.8
Charges due on GRA credit 3/	-	-	29.3	59.7	65.0	68.6	41.4	8.2
Commitment Fee 4/	-	-						
Debt service due on GRA credit 5/	-	-	29.3	59.7	65.0	436	1,549	1,258
Debt and Debt Service Ratios /6								
In percent of GDP								
Total external debt	29.8	31.1	36.9	37.4	36.9	35.4	33.1	31.3
External debt, public	25.7	26.9	33.6	34.1	33.6	32.2	30.0	28.2
Total public debt	61.9	65.4	70.9	70.9	69.2	67.1	63.8	60.8
GRA credit to Morocco	-	-	4.1	4.2	3.9	3.2	1.4	0.1
Total external debt service 7/	2.5	2.7	2.7	2.6	2.6	3.4	3.9	3.4
Public external debt service 7/	2.4	2.5	2.5	2.4	2.4	3.1	3.7	3.1
Debt service due on GRA credit	-	-	0.0	0.1	0.1	0.5	1.6	1.2
In percent of General Government Revenues								
Public external debt service 7/	8.3	8.7	8.8	8.6	8.5	11.1	13.2	11.1
Debt service due on GRA credit	-	-	0.1	0.3	0.3	1.7	5.8	4.4
In percent of Gross International Reserves								
Total external debt	163	168	197	201	197	188	173	161
External debt, public	144	150	179	183	180	171	156	145
GRA credit to Morocco	-	-	21.7	22.4	20.7	17.1	7.5	0.6
Debt service due on GRA credit	-	-	0.2	0.4	0.4	2.6	8.5	6.4
In percent of Exports of Goods and Services								
Total external debt service 7/	7.0	8.0	7.9	7.7	7.4	9.5	10.9	9.2
Public external debt service 7/	6.6	7.3	7.2	7.0	6.8	8.9	10.3	8.6
Debt service due on GRA credit	-	-	0.1	0.2	0.2	1.4	4.5	3.4
In percent of Total Public External Debt								
GRA credit to Morocco	-	-	12.1	12.2	11.5	10.0	4.8	0.4
In percent of Total Public External Debt Service								
Debt service due on GRA credit	-	-	1.6	3.2	3.3	15.5	44.0	39.6

Sources: Moroccan authorities, Finance Department, World Economic Outlook, and IMF staff estimates.

1/ Assumes full drawings except where noted.
2/ Assumes full purchase of available amount: SDR 2,941 mn at approval and SDR 294.1 one year later.
3/ Includes GRA basic rate of charge, surcharges and service fees.
4/ A commitment fee is charged on undisbursed balances and is refunded if purchases are made. The charges shown assume no purchases are made.
5/ Includes charges due on GRA credit and payments on principal.
6/ Staff projections for external debt, GDP, gross international reserves, and exports of goods and services, as used in the staff report that requests the proposed PLL.
7/ Interest on and amortization of medium and long-term debt, including debt service on GRA credit.

8. The impact of the proposed PLL arrangement on the Fund's liquidity and potential credit exposure would be low (Table 4). The Fund's liquidity measured by the Forward Commitment Capacity (FCC) would decline slightly upon approval of the proposed—and expiration or cancellation of the current—arrangements (see Table 4, footnote 2). If fully drawn, exposure to Morocco would represent a small share of the Fund's total credit outstanding and about a quarter of the Fund's reserves. Due to the limited capacity of burden sharing due to the low interest rate environment and borrowing by the Fund, potential charges for Morocco would significantly exceed the Fund's capacity to absorb charges in arrears.

Table 4. PLL Arrangement for Morocco—Impact of GRA Finances
(In SDR millions, unless otherwise indicated)

	as of 6/17/2014
Liquidity measures	
Forward Commitment Capacity (FCC) before approval 1/	265,200
FCC on approval 2/	262,994
percent change	-0.8
Prudential measures	
Fund GRA commitment to Morocco including credit outstanding	
in percent of current precautionary balances	25.4
in percent of total GRA credit outstanding 3/	3.9
Fund GRA credit outstanding to top five borrowers	
in percent of total GRA credit outstanding 3/	87.7
in percent of total GRA credit outstanding including first Moroccan purchase	86.0
Morocco's projected annual GRA charges for 2015 in percent of the Fund's residual burden sharing capacity	765
Memorandum items	
Fund's precautionary balances (FY14)	12,730
Fund's Residual Burden Sharing Capacity 4/	7.8

Sources: Finance Department and IMF staff estimates.

1/ The FCC is defined as the Fund's stock of usable resources less undrawn balances under existing arragements, plus projected repurchases during the coming 12 months, less repayments of borrowing due one year forward, less a prudential balance. The FCC does not include about US$461 billion in bilateral pledges from members to boost IMF resources. These resources will only be counted towards the FCC once: (i) individual bilateral agreements are effective and (ii) the associated resources are available for use by the IMF, in accordance with the borrowing guidelines and the terms of these agreements.
2/ Current FCC minus new access plus access under the expiring program adjusted for the NAB financed portion of the expiring commitment (about SDR 3,088 million or 525 percent of quota) which is not available to finance new commitments under the currrent activation. This amount could be included in possible future NAB activations.
3/ As of June 17, 2014, does not include proposed first purchase.
4/ Burden-sharing capacity is calculated based on the floor for remuneration at 85 percent of the SDR interest rate. Residual burden-sharing capacity is equal to the total burden-sharing capacity minus the portion being utilized to offset deferred charges and takes into account the loss in capacity due to nonpayment of burden sharing adjustments by members in arrears.

ASSESSMENT

9. The risks to the Fund's finances and liquidity position associated with a PLL for Morocco appear to be manageable. Morocco represents a moderate risk of drawing and should the arrangement be fully drawn, credit to Morocco would represent a small share of total GRA credit outstanding and would be exceeded by precautionary balances by a comfortable margin. Furthermore, reforms implemented during the first PLL have increased Morocco's capacity to absorb shocks even as the external environment has improved over the past two years, consistent with reduced access. Risks from the Fund from exposure to Morocco appear to be limited but two closely linked areas of potential risk will require close monitoring.

- *Policy implementation risk*. Policy slippage in the area of fiscal reforms needed to realize long-term stability, particularly with respect to rationalization of subsidies and transfers, would affect capacity to repay. As noted in paragraph 4, Morocco's public debt is relatively high and at over 62 percent of GDP end-2013 and is over 8 percentage points higher than projected at the expiring program's inception. The combined macro-fiscal shock in the DSA illustrates the downside risks to Morocco's capacity to repay should fiscal and growth stimulating reforms fall short of expectations.

- *Exogenous risks*. While conditions in Europe have stabilized somewhat relative to two years ago, downside risks remain and the euro area represents about 67 percent of Morocco's exports. Further, geopolitical risks in the Middle East could trigger commodity price volatility and, with higher petroleum prices particularly, could have significant negative ramifications for Morocco's current account deficit and fiscal balance, particularly if subsidy reform stalls. The tapering of unconventional monetary policy could have adverse effects on Morocco as a result of financial market volatility, the impact on trading partners' growth, and the possible reduction in FDI.

10. The limited risks to the Fund are mitigated by several factors. Morocco's relatively low reserve level is mitigated by low short-term external debt and balance of payments flows where the risk of sudden stop or reversals is limited. The authorities made important progress during the past program to stabilize the economy, particularly gaining fiscal policy space and increasing external buffers and making progress on structural reforms. At the same time, they are committed to furthering these reforms—focused on improving fiscal institutions, further lowering the fiscal deficit and subsidies, and addressing structural constraints to growth—under the proposed arrangement.

Annex I. Morocco's Relations with the Fund

Prior to the recent PLL, Morocco made extensive use of Fund resources between the late 1970s and early 1990s, including SBA and EFF arrangements. Morocco made use of financing via the First Credit Tranche, Contingent Financing Facility, and the Oil Facility that resulted in credit outstanding of about SDR 232 million by end-1979. In 1980, the first of two EFFs was approved, followed by seven SBA arrangements between 1982 and 1993 (see Table 1). The largest commitment of these arrangements in terms of quota was the first EFF at 540 percent, of which only 30 percent was drawn. Peak nominal credit outstanding occurred in 1985 at about SDR 1,106 million or 380 percent of quota. Morocco has a history of meeting its obligations to the Fund in a timely basis; outstanding credit was fully repaid in 1997.

Annex Table. Morocco: IMF Financial Arrangements, 1980-2012
(In millions of SDRs)

Year	Type of Arrangement	Date of Arrangement	Date of Expiration or Cancellation	Amount of New Arrangement	Arrangement as a Percent of Quota	Amount Drawn	Total Exposure 1/	
							SDR	percent of quota
1979							231.9	154.6
1980	EFF	08-Oct-80	08-Mar-81	810.0	540.0	147.0	358.4	159.3
1981	EFF	09-Mar-81	25-Apr-82	817.1	363.1	136.5	497.4	221.1
1982	SBA	26-Apr-82	25-Apr-83	281.3	125.0	281.3	897.5	398.9
1983	SBA	16-Sep-83	15-Mar-85	300.0	133.3	300.0	985.5	321.4
1984							1,107.2	361.1
1985	SBA	12-Sep-85	15-Dec-86	200.0	65.2	10.0	1,160.6	378.5
1986	SBA	16-Dec-86	30-Apr-88	230.0	75.0	230.0	894.4	291.7
1987							789.1	257.4
1988	SBA	30-Aug-88	31-Dec-89	210.0	68.5	210.0	711.1	231.9
1989							646.6	210.9
1990	SBA	20-Jul-90	31-Mar-91	100.0	32.6	48.0	526.9	171.9
1991							401.5	131.0
1992	SBA	31-Jan-92	31-Mar-93	92.0	30.0	18.4	319.1	74.6
1993							207.2	48.4
1994							101.1	23.6
1995							34.8	8.1
:								
2011								
2012	PLL	3-Aug-12	2-Aug-14	4,117.4	700.0	0.0		
2013								

Source: Finance Department.

1/ As of end-December.

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International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$5-Billion Arrangement for Morocco Under the Precautionary and Liquidity Line

The Executive Board of the International Monetary Fund (IMF) today approved a new 24-month arrangement for Morocco under the Precautionary and Liquidity Line (PLL) in an amount equivalent to SDR 3.2351 billion (about US$5 billion, or 550 percent of Morocco's quota at the IMF). The access under the arrangement in the first year will be equivalent to SDR 2.941 billion (about US$4.5 billion, 500 percent of quota), rising in the second year to a cumulative US$5.0 billion. Morocco's first 2-year PLL arrangement was approved on August 2, 2012 (see Press Release No 12/287).

The Moroccan authorities have stated that they intend to treat the arrangement as precautionary, as they have done with the 2012 PLL, and do not intend to draw under the arrangement unless Morocco experiences actual balance of payments needs from a significant deterioration of external conditions.

The PLL arrangement will allow the authorities to pursue their homegrown reform agenda aimed at achieving rapid and more inclusive economic growth while providing them with useful insurance against external shocks.

The PLL was introduced in 2011 to meet more flexibly the liquidity needs of member countries with sound economic fundamentals and strong records of policy implementation but with some remaining vulnerabilities.

Following the Executive Board discussion on Morocco, Mr. Noayuki Shinohara, IMF Deputy Managing Director and Acting Chairman of the Board, made the following statement:

"Morocco's sound economic fundamentals and overall strong record of policy implementation have contributed to a solid macroeconomic performance in recent years. Despite a difficult external environment, the authorities made important strides in reducing vulnerabilities, rebuilding policy space and addressing medium-term challenges over the course of the first arrangement supported by a PLL. They have been consolidating Morocco's fiscal position while pursuing an agenda of structural reforms to address vulnerabilities, strengthen competitiveness, and promote higher and more inclusive growth. The significant progress made in reforming the subsidy system is particularly commendable.

"The external environment remains subject to significant downside risks. In particular, protracted and slower–than-expected growth in Europe than currently projected, heightened financial market volatility, or a surge in oil prices resulting from geopolitical tensions could significantly affect the Moroccan economy. In this context, the successor PLL arrangement will continue to provide insurance to support the authorities' economic policies.

"The authorities are committed to further reducing fiscal and external vulnerabilities while laying the foundations for higher and more inclusive growth. To achieve these goals, it will be important to control expenditure as well as advance major reforms, including those of subsidies, pension and the tax system. The timely adoption of a new organic budget law will be essential in order to strengthen and modernize the budget framework. Moving toward a more flexible exchange rate regime, in coordination with other macroeconomic policies would also help support competitiveness and enhance the economy's capacity to absorb shocks. Advancing structural reforms to improve the business climate, the judicial system, access to finance, and the labor market will be crucial to achieving higher growth and employment," Mr. Shinohara said.

Morocco has been a member of the IMF since 1958 and has a quota of SDR588.2 million (about US$903.4 million).

Statement by Mohammed Daïri, Alternate Executive Director for Morocco

July 28, 2014

My Moroccan authorities wish to express their appreciation to staff, management, and the Executive Board for their support under the 2012 PLL, which has enabled Morocco to weather the weaker and more volatile global and regional environment, and provided a valuable insurance against exogenous shocks. Along with the advice provided under Article IV consultations and Fund technical assistance, the PLL was instrumental in helping the authorities strengthen the economy's resilience and maintain their reform momentum toward achieving their objectives of higher and more inclusive growth, while consolidating the gains in macroeconomic and financial stability. My authorities are grateful to staff for the productive and candid discussions on a new PLL arrangement at the expiration of the current one. They appreciate the well-written and focused report, agree with the thrust of its analysis and recommendations, and look forward to Board approval of their request. As with the current PLL, the authorities will continue to treat the arrangement as precautionary, and will not draw on it, except in case of a significant deterioration in the global environment from current baseline assumptions.

Performance under the 2012 PLL

Performance under the PLL-supported program was satisfactory, considering the more adverse exogenous conditions than projected at its inception, as illustrated in Box 1 of the staff report, and the time and efforts needed to build consensus on some crucial reforms. The authorities demonstrated strong ownership throughout the program, even during the prolonged transition to a new government in the summer of 2013. They were successful in limiting the impact of these adverse developments on the budget and the balance of payments, addressing the weaknesses in budget implementation faced at end-2012, and putting the fiscal and external positions on the right path for reaching their medium-term targets. They also made significant strides in key structural reforms to strengthen the economy's performance and resilience, and to reduce vulnerabilities. The milestone reform of the subsidy system, which is at an advanced stage of implementation, gives confidence that the targeted reduction in total subsidy cost to 3 percent of GDP could be achieved in 2015, one year ahead of schedule, and that the related vulnerabilities will be significantly reduced. Key to the success of the authorities' efforts was the priority given to maintaining social stability through close consultation with partners, and by strengthening the social safety net to mitigate the impact of reforms on the most vulnerable.

The new PLL-supported program

The successful implementation of the first PLL, notwithstanding the less favorable external environment than originally assumed, gives confidence to the authorities that they are on the right path for meeting their medium term objectives**.** Consequently, they have kept these objectives unchanged, including strengthening growth to 5½ percent, maintaining inflation at around 2 percent, reducing unemployment to 8 percent, bringing the current account deficit down to 4–5 percent of GDP, and increasing reserves to around 5 months of imports.

Maintaining the same objectives in a more difficult external environment is challenging, but the authorities are firmly determined to face the challenge. They will further strengthen their sound macroeconomic policies, while being attentive to their impact on growth, and will accelerate structural reform implementation aimed at ensuring a more enabling environment for private sector development and for attracting FDI.

1- Macroeconomic policies

Fiscal policy will continue to seek a reduction in the deficit to 3 percent of GDP by 2017, which would help put public debt on a downward trajectory to less than 60 percent of GDP by 2020. The achievement of this deficit target is within reach, requiring average annual consolidation of 0.6 percent. In this regard, the authorities are committed to reducing the deficit from 5.5 percent of GDP in 2013 to 4.9 percent in 2014, and will aim at a further reduction to 4.3 percent in 2015.

Fiscal consolidation will rely primarily on close control and rationalization of current expenditures, in particular the wage and subsidy bills, which would also help create fiscal space for more spending on infrastructure, human capital and social protection, as well as continued strengthening of the fiscal framework and public financial management. A broadening of the tax base to improve the system's buoyancy and equity, reduce distortions, and enhance competitiveness is also expected to strengthen revenue collection. The recently announced reform of the pension system, starting with the public pay-as-you-go system for the civil service (Caisse Marocaine des Retraites, CMR), would improve the sustainability of the system and reduce risks to the budget. The Written Communication and the staff paper elaborate in detail on these policies and reforms, the significant strides made so far in their implementation, and the way forward.

Monetary policy will continue to focus on price stability in the context of a strengthened framework and institutional setting, while ensuring that adequate resources are available to the banking sector to finance the economy. In this regard, Bank Al-Maghrib (BAM) will continue to promote financial inclusion, including through support to very small, small and middle-sized enterprises. Financial sector policies will seek further strengthening and deepening of the system to increase its contribution to growth, with enhanced regulation and supervision, broader regulatory powers of the central bank, and increased independence of financial sector supervisors. Efforts are also being made to improve cooperation among supervisors and coordination between macro and micro-prudential regulations, and to strengthen cross-border cooperation with host country supervisors of Moroccan banks established abroad.

The external position will continue to strengthen. After declining from 9.7 percent of GDP in 2012 to 7.7 percent in 2013, the current account deficit is projected to decrease further to 6.8 percent of GDP in 2014, mainly reflecting continued dynamism of the new export sectors and a recovery in textiles and tourism. With continued strong FDI flows and larger borrowing from international capital markets, this would help increase reserves further to 4.5 months of imports, or 91 percent of the Fund's Assessing Reserve Adequacy metrics (ARA), slightly below the 100-150 percent recommended range. Staff rightly indicates that, in view of existing capital controls, this level of reserves is adequate for Morocco, in particular since, with relatively low external flows, the impact of external shocks on reserves would be smaller than for other precautionary arrangement users. Under recent proposals for revising Fund metrics to take account of capital controls, Morocco's reserve level would be at the upper end of the 100-150 percent ARA metrics range.

Preparations are underway for a potential move to greater exchange rate flexibility, once the necessary conditions are met. Continued progress in strengthening fiscal and external sustainability and reducing related vulnerabilities, including the ongoing reform of the subsidy system, improves the likelihood of such a move over the medium term. The authorities are in the process of assessing available options and related operational issues, as well as the degree of preparedness in this area, with Fund TA. In this regard, while the central bank's capabilities have been significantly strengthened, it will be important to ensure that the financial sector, but also the corporate sector, can effectively and prudently operate under a more flexible regime.

2- Structural Reforms

Progress in structural reforms will continue unabated, despite a very heavy legislative agenda, including the many organic laws and other legislation and regulations that have to be enacted in the near term in compliance with the new constitution. The draft organic budget law (OBL) passed recently by the first Chamber of parliament is under discussion in the second Chamber. It provides for a significant strengthening of the budgetary framework through multi-year and program-based budgeting, introduces a golden fiscal rule, addresses in a more permanent way the weaknesses that affected budget implementation in 2012, and enhances transparency of the budget and parliamentary control powers. The authorities will do their utmost to speed up the adoption of the draft OBL so that, subject to approval of the Constitutional Court, the 2015 budget can be adopted in conformity with the new OBL.

The subsidy reform will reach its medium term target in 2015, when all subsidies will be eliminated, except for butane, sugar, and a limited volume of flour, with a combined cost of remaining subsidies at less than 3 percent of GDP. It should be noted, in comparison, that energy taxes, excluding VAT, amount to some 2.5 percent of GDP. As indicated in the Written Communication, consideration is being given to further reducing these subsidies through adequate incentives to substitute solar energy for butane, as well as other cost-saving measures. At the same time, the social safety net is being strengthened through provision of basic social services and targeted assistance to the most vulnerable segments of society.

The authorities will continue to strengthen competitiveness, address key impediments to private investment, and improve the business climate by streamlining regulations and enhancing governance and the rule of law. In addition, the sector-specific strategies designed in close cooperation with the business community have been effective in strengthening performance of the economy and boosting new engines of growth and exports, and will be developed further. Continued attention will be given to improving infrastructure through the budget, but also through state-owned enterprises and public-private partnerships.

The ongoing restructuring of the public electricity and water company (ONEE) will help increase efficiency and investment, reduce power generation costs through the use of alternative, less costly, and more environment-friendly sources of energy, improve cost recovery, while protecting the most vulnerable, and reduce budgetary costs and risks. More broadly, efforts will continue to strengthen the financial position of state-owned enterprises and their contribution to growth, including through implementation of the new procurement law and increased transparency. The efficiency of labor market intermediation and active labor market policies, including vocational training programs and incentives for self employment, will be enhanced to increase employability and reduce long-term and youth unemployment. Finally, several tax and other incentives are being put in place to facilitate the integration of the informal sector into the modern economy, with positive impact in terms of formal employment, tax revenue, the pension system, and social protection.

Conclusion

The authorities are committed to continue to strengthen macroeconomic stability and structural reform implementation to reduce vulnerabilities to exogenous shocks and put the economy on a higher and more inclusive growth trajectory, while accelerating employment creation. They will do the utmost to meet their ambitious targets under the PLL-supported program. The unwavering commitment of the authorities in this regard bodes well for continued strong performance in the run up to the upcoming local and general elections. They are grateful to their partners for their continued support.