MOROCCO

POLICY MIX UNCHANGED

Morocco's heavy dependency on oil and wheat imports mean that it will suffer consequences from the conflict in Ukraine. However, it will be able to absorb the trade shock thanks to comfortable FX reserves. Moreover, the rise in energy and food subsidies does not compromise the expansionary fiscal policy, and the central bank plans to maintain its accommodative stance despite strong but still under control inflationary pressure. Government support remains crucial at a time when the economy is facing a significant drop in agricultural output, and therefore real GDP growth. In the short term, state solvency and external liquidity are not at risk. However, there is a high level of uncertainty about how large the shock will be and how long it will last.

HIGHLY VULNERABLE TO THE COMMODITY PRICE SHOCK

Morocco will be hard hit by the indirect consequences of the conflict in Ukraine. Trade relations are limited, since Russia and Ukraine account for only 3% of Morocco's external trade, and almost non-existent for tourism activity and investment. However, around 20% of Morocco's cereal imports come from the two countries, which means it will have to find new sources at a time when global prices are soaring and when Morocco's domestic production is about to fall dramatically because of a serious drought during the winter. Morocco depends on external supply to cover around 60% of its needs. In addition, the weight of food in the consumer price basket is heavy (37.5%). Although Morocco has relatively large wheat reserves (five months), the higher cost of cereals will put serious pressure on Morocco's trade position and inflation. The energy shock may be even greater. With hydrocarbon imports over 6% of GDP in the last five years, Morocco's economy is one of the most vulnerable to oil price movements in the MENA region. Nevertheless, it is also one of the most robust to deal with the shock.

EXTERNAL LIQUIDITY: SIGNIFICANT BUFFERS

Morocco's external stability is not under threat. Although imports are expected to rise sharply – each $10 increase in the Brent crude price raises energy imports by 1% of GDP – exports will also perform well. This is due in particular to high global prices for phosphates (20-25% of Morocco's exports). They rose 67% in 2021 to their highest level since 2012, and the outlook is well oriented in tandem with the strong dynamic of agricultural commodity prices. Morocco is the world's fifth-largest exporter of fertilisers and could even gain market share. Other factors should also be taken into account, starting with the rebound of tourism. Although the Covid-19 pandemic still represents a risk, the progress of vaccination programmes in both Morocco and Europe gives grounds for hope that tourism will start to recover after two difficult seasons. A rise in tourism receipts by 50-60% is thus hoped this year before moving back close to its pre-pandemic level in 2023. Receipts were still 56% below that level in 2021. In addition, remittances from the Moroccan diaspora will continue to play a shock-absorbing role, although they could fall from the record of MAD93.2 billion (10.7% of GDP) seen in 2021.

In the circumstances, the current account deficit is expected to widen significantly to 5.7% of GDP in 2022, before narrowing to 4.8% in 2023. Although the widening of Morocco's sovereign spreads on foreign currency bonds has remained limited at 260bp compared with 350bp for the average of emerging countries, external financing conditions are also likely to be less favourable than in the last two years. However, the Moroccan economy has some significant buffers. FX reserves currently cover seven months of goods and services imports. Limited exposure to portfolio investment flows is also a stabilizing factor in the current context. In addition, the authorities are not ruling out asking the IMF for a new precautionary and liquidity line should pressure on the balance of payments becomes too strong. At the moment, that pressure appears manageable. The fluctuation of dirham does not point out any particular sign of stress chart 1). Its fall against the US dollar just after the conflict broke out is mainly linked to the weakening of the euro against the dollar. The dirham also remains within fluctuating bands and forward rates show limited currency risk at this stage.

FORECASTS

	2019	2020	2021e	2022e	2023e
Real GDP growth, %	2.6	-6.3	7.1	0.7	4.5
Inflation, CPI, year average, %	0.2	0.6	1.4	4.6	2.1
Central Gov. balance / GDP, %	-4.0	-7.6	-6.4	-6.3	-5.5
Central Gov. debt / GDP, %	64.8	76.4	74.5	76.6	76.7
Current account balance / GDP, %	-4.1	-1.5	-2.5	-5.7	-4.8
External debt / GDP, %	45.6	57.1	49.2	50.4	50.7
Forex reserves, USD bn	25.3	34.7	34.3	32.4	31.4
Forex reserves, in months of imports	5.5	9.0	7.1	5.8	5.5

TABLE 1 e: ESTIMATE & FORECASTS
SOURCE: BNP PARIBAS ECONOMIC RESEARCH

MOROCCO: NOMINAL EXCHANGE RATE

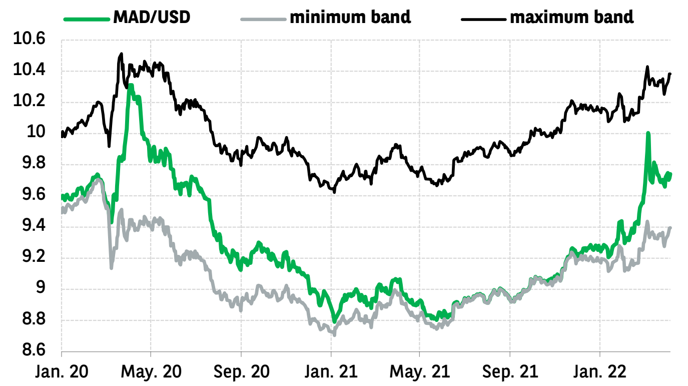

CHART 1 SOURCE: CENTRAL BANK

NO CHANGE IN FISCAL POLICY...

Public finances also offer some room for manoeuvre, at least in the short term. Unlike other countries in the region, the Moroccan government has not been subsiding petroleum prices since 2015. It has announced targeted measures to support transport companies, but these remain limited to 0.2% of GDP. However, subsidies for butane and wheat flour will increase sharply. According to the latest estimates, they are likely to reach 2.4% of GDP this year against 1.4% initially budgeted, and this additional cost will come on top of other support measures for the tourism and agriculture sectors. In response, the government is planning to mobilize additional revenues thanks notably to excellent performances of state-owned phosphates producer OCP.

The deficit target of 6.3% of GDP in 2022 (5.9% including privatisation proceeds) remains unchanged. Although some assumptions are still fragile, the government has already declared that a supplementary financing bill will be not necessary. There are also no plans of spending reallocations despite the historically high public investment of more than 20% of GDP – including state-owned enterprises, local authorities and the Mohammed VI strategic fund- budgeted in 2022 and the launch of the social protection extension, which will cost an estimated 1.5% of GDP per year in the next five years. The fact that the government is not planning to use the SDRs (0.9% of GDP) allocated by the IMF in August 2021 is another sign of confidence. In any case, the government will still be able to rely on a liquid, captive domestic market in order to continue accessing funding at favourable conditions. Although the central government debt is high at 75% of GDP, interest payments absorb only 12% of revenue thanks to one of the lowest apparent interest rates in the region (3.3%). The debt structure is also favourable, with 77% denominated in local currency and held by Moroccan residents, limiting vulnerability to external shocks.

... AND MONETARY POLICY FOR THE MOMENT

By deciding to leave its key interest rate unchanged at 1.5%, Morocco's central bank has wanted to send a reassuring signal. Inflation is accelerating, as it is all around the world, but the surge is recent and relatively mild (chart 2). In 2021, consumer prices rose at an average annual rate of only 1.4%. In February 2022, they were up 3.6% y/y and the situation will only get worse given the pressures on global commodity markets and the drop-off in national agricultural production. Three quarters of the acceleration in inflation in recent months reflects higher prices for food (+5.5% in February 2022) and transport (+6%), essentially due to external factors. Excluding these two categories, the growth in prices was less than 2%. Domestic pressures are mild. Average private sector wages grew only 1% in nominal terms in Q4 2021, while bank lending to the economy was up 3.3% y/y in February. Both of those increases are lower than the inflation rate. Moreover, with an unemployment rate at 11.9%, up from 10.2% in Q4 2019, the economy has not fully recovered job losses induced by the pandemic shock while the cycle is deteriorating again. Although inflation is expected to be 4.6% this year and there is a lot of risk on the upside, the central bank thus has a strong case for maintaining its accommodative stance.

MOROCCO: CONTRIBUTION TO INFLATION AND KEY POLICY RATE

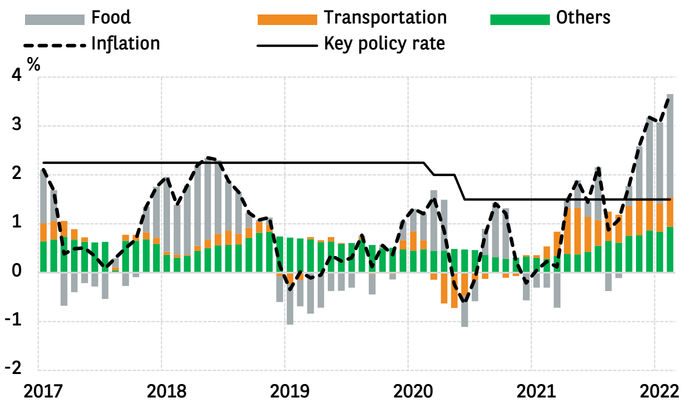

CHART 2 SOURCE: CENTRAL BANK, HIGH COMMISSION FOR PLANNING

GROWTH: ABRUPT HALT AND RISKS

After the strong rebound seen in 2021, growth will come to an abrupt halt this year. The central bank has just cut its growth forecast to only 0.7% because of the 20% drop in value added in the agricultural sector. Although late rainfall could help to save the crop somewhat, the primary sector's poor performance will inevitably drag down growth given its significant weight into the economy (10-12% of GDP). Non-agricultural activity could also be hit hard by developments in the global economy. Downward revisions have been limited so far. Growth outside the agricultural sector is expected to slow because higher inflation will affect household consumption. But it should remain relatively solid at around 3% thanks to monetary stimulus and expansionary fiscal policy. On the sectoral side, the expected rebound in tourism activity should also support economic growth. Nevertheless, there is limited visibility due to the high level of uncertainty about how large the shock will be and how long it will last. If the European economy contracts sharply, this could seriously hold back Morocco's manufacturing sector, which was crucial to the 2021 upturn. Above all, the authorities could be forced to change their policy priority if purchasing power falls too sharply or if the public finances come under persistent pressure. Spending could be reallocated, or monetary policy tightened, which would weaken further a convalescing economy.

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