

## Morocco

### Satisfactory performance

*Between difficulties in Europe and a poor agricultural harvest, Morocco faces numerous headwinds. Growth slowed in 2019 for the second consecutive year. Yet domestic demand remains robust, bolstered among other factors by low inflation and an accommodating monetary policy. The authorities are also counting on major privatisation proceeds to soften fiscal consolidation without worsening public debt. Above all, the ongoing development of the automobile industry raises hopes for a rebound in GDP growth in 2020, while lower oil imports should help to reduce the current account deficit.*

#### ■ Growth slows but is still robust

The economic slowdown continues. GDP growth dropped to 3% in 2018 from 4.2% in 2017, and according to the latest HCP figures, will reach 2.7% at best this year. Between difficulties in Europe and a poor agricultural harvest, the Moroccan economy faces numerous headwinds. Yet the overall picture is much more nuanced than it might seem, raising hopes for a rebound in activity as of 2020.

The slowing down in the economic activity during the first six months of the year can be attributed primarily to the 3% contraction in agricultural value added, which accounts for a significant share of GDP (11%). For the rest of the economy, the dynamics is rather encouraging. Non-agricultural GDP growth also slowed to 3.2% y/y in Q2, compared to 3.6% in Q1. But this is still robust compared to the 2016-2018 average of 2.9%. Most of the sectors vulnerable to the European cycle, including tourism and manufacturing, have proven to be fairly resilient so far. Moreover, two new major projects have just been completed, the Tangier port expansion and the start-up of the Peugeot plant in Kénitra. As the plant is ramped up in 2020, the increase in automobile production should provide a new impulse to what has become a strategic industry, although its pace has been slowing recently. Automobile exports increased only 2.2% since the beginning of the year, after more than doubling between 2013 and 2018.

Robust domestic demand will also be a key supportive factor. Household consumption is buoyant (+3.8% y/y in the first 6 months of the year) and should continue going strong thanks to extremely low inflation – less than 1% since end-2018 – and the boost from the 10% increase in the private sector minimum wage. Low inflationary pressures also give the central bank some extra manoeuvring room. With a key policy rate of only 2.25% and a mandatory reserve rate recently cut to 2%, monetary policy is already accommodating. The status quo is likely to persist even though with the real interest rate at a positive 1.5%, there is still room for further cuts if necessary. In any case, financial conditions will remain favourable for households and corporates. The weighted average interest rate on lending to the economy hit a low of 4.98% in Q2. Budgetary execution during the first 8 months of the year also demonstrates the authorities' determination to stimulate the economy.

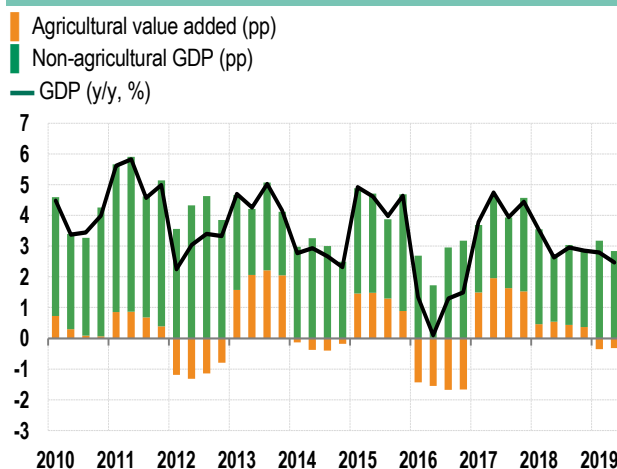
With non-agricultural GDP growth of 3.4% and assuming a normal agricultural harvest, economic growth could reach 3.5% in 2020. \*

#### 1-Forecasts

	2017	2018	2019e	2020e
Real GDP growth (%)	4.2	3.0	2.7	3.5
Inflation (CPI, year average, %)	0.7	1.8	0.6	1.1
Central. Gov. balance / GDP (%)	-3.6	-3.7	-4.0	-3.8
Central. Gov. debt / GDP (%)	65.1	65.3	65.9	65.5
Current account balance / GDP (%)	-3.6	-5.5	-5.1	-4.1
External debt / GDP (%)	47.1	44.4	46.5	46.7
Forex reserves (USD bn)	26.2	24.5	25.0	26.1
Forex reserves, in months of imports	6.4	5.3	5.3	5.4
Exchange rate USDMAD (year end)	9.4	9.6	9.6	9.5

e: BNP Paribas Group Economic Research estimates and forecasts

#### 2- Sector contribution to growth



Source: HCP, BNP Paribas

This would make the Moroccan economy one of the top performers in the region. Given the country's development needs, however, this is still not enough. At 8.5%, the unemployment rate is chronically high, as is the proportion of the population excluded from the labour market (the employment rate is only 42%). Yet the economy continued to create jobs in H1 2019 despite the massive destruction of farm sector jobs, which highlights again the solidity of Morocco's economic performances despite a deteriorating international environment.



### ■ Softer fiscal consolidation

After the major budget overruns reported in 2018, public finances deteriorated further in 2019. From January to August, the main budget components continued to rise, whether operating expenses (+5.5%) or capital investment (+4.9%). Despite the rather good dynamisms of fiscal revenues excluding privatisation (+3.4%), the budget deficit widened again. It is expected to reach 4% of GDP in 2019, up from 3.7% in 2018 (and an initial target of 3%), before gradually narrowing again as of 2020.

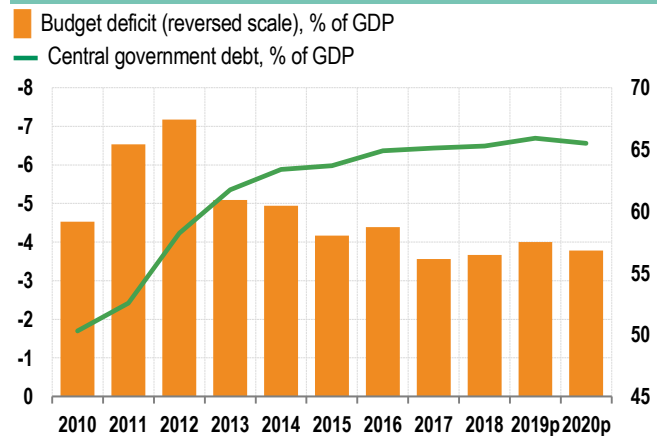
While the government has opted for a smoother fiscal consolidation programme, the situation generally seems to be under control. In terms of both revenues and spending, the main risk factors behind the 2018 budgetary slippages have since dissipated. Financial assistance from the Gulf countries is expected to be modest and the authorities have put in place a hedging strategy to insulate the budget against the volatility of oil prices: last year's surge in oil prices resulted in a 26% overrun in the budget allocation for energy subsidies. The government is also planning to increase recourse on public-private partnerships to ease the pressure on the public accounts. Public investment, the second largest spending item behind public sector wages, is high at about 6% of GDP. Above all, the authorities are counting on privatisation proceeds of about 0.4% of GDP a year through 2021 to stabilize government debt at 65% of GDP. With the partial disposal of the government's stake in Maroc Télécom in July, its 2019 target has already been met, and other privatisation operations have been identified.

In any case, government debt does not seem to be a major source of risk. Unlike many emerging countries, Morocco has hardly called on the international financial markets. Two Eurobond issues are expected to be made in the short term. With a risk premium of 150 basis points, they should be completed under good conditions, especially since the S&P rating agency has just revised outlook for Moroccan sovereign risk from negative to stable. Moreover, the debt profile will not change fundamentally, with 80% denominated in the local currency, and the government's financing conditions have rarely been so advantageous, both in terms of interest rates and maturity. With an apparent cost of debt of only 4%, the government has comfortable manoeuvring room.

### ■ Solid external position

The deterioration of the economic situation in Europe could strain the dynamics of Morocco's external accounts, albeit without threatening its stability. With the exception of remittances from the Moroccan diaspora (-1.3% y/y), the main sources of hard currency were still on the rise in the first 8 months of the year, with exports and tourist revenues up 3.7% and 4.5%, respectively. Imports grew at a similar pace, however, so the trade deficit widened slightly, but the situation could improve in the months ahead thanks to an upturn in automobile sales. Automobiles already account for a quarter of Moroccan exports. In an unstable external environment, and while commodities (phosphates) still account for a large share of trade, the move towards higher value added exports strengthens the economy's resilience. Downward pressure on oil prices (15-20% of imports) could also help improve the external accounts.

### 3- Public finance indicators



Source: Ministry of Finance, BNP Paribas

With the current account deficit estimated at 5.1% of GDP in 2019 and 4.1% in 2020, compared to 5.5% in 2018, Morocco should easily cover its financing needs. Net flows of foreign direct investment (FDI) are robust at about 1.5-2.5% of GDP, and external debt is moderate at 44% of GDP. Buffers are also adequate. Foreign reserves cover more than 5 months of imports of goods and services, and Morocco benefits from a USD 3 billion precautionary credit line with the IMF through end-2020 to protect the economy against any balance of payment shocks. As with previous IMF programmes, the authorities are unlikely to draw on these funds.

Lastly, after the dirham's fluctuation band was widened in January 2018 to +/-2.5% on either side of reference parity (vs. +/-0.3% previously), the central bank almost never has to intervene in the forex exchange market, which reduces the pressure on external liquidity. MAD volatility has been extremely mild and is expected to remain so as the authorities proceed as cautiously as ever to introduce greater flexibility in the exchange rate regime.

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