



PRIVATE SECTOR DEVELOPMENT IN MOROCCO

Challenges & opportunities in times of Covid-19

Joint report



September, 2021

Joint Country Diagnostic

The African Development Bank (AfDB), European Bank for Reconstruction and Development (EBRD) and European Investment Bank (EIB) jointly prepared this Country Diagnostic for Morocco. The report aims at identifying the key challenges and opportunities in promoting private sector development and investment in Morocco. This collaboration between the AfDB, EBRD and EIB builds on the Country Diagnostic Working Group. The Country Diagnostic Working Group helps IFIs and DFIs to share perspectives and experiences of preparing Country Diagnostics and develop cross-institutional collaboration where possible.

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Preface

At the crossroad of Europe and Sub-Saharan Africa, the Atlantic and the Mediterranean, Morocco is a key partner of our institutions. Morocco is rich in history and tradition, economic and human resources. The emergence of a dynamic and broad-based private sector can become a powerful driver of job creation, social inclusion and economic resilience. This is all the more important in the wake of an unprecedented crisis that has hit the world economy with no exceptions.

Promoting a thriving private sector requires a thorough understanding of the key determinants of firm performance: what are the challenges they face? How to make the most of potential they have? What are the necessary measures to shape a supportive business environment? What is the role of development partners? The African Development Bank (AfDB), the European Bank for Reconstruction and Development (EBRD) and the European Investment Bank (EIB) have joined forces to provide answers to these questions. This report presents the results of a country diagnostic joint mission, months of exchanges of views and common research efforts, leading to a shared assessment that on the one hand capitalises on our already vast expertise on the ground and, on the other, lays an even stronger analytical

foundation for our continued engagement in Morocco. The main findings of the report are that greater economic and financial diversification, deeper integration in global value chains, notably in Sub-Saharan Africa, and participation of more (and smaller) firms in all sectors of the private economy remain crucial going forward to ensure more inclusive and resilient growth in Morocco. Large state-owned enterprises still represent one of the main engines of growth. It is therefore key to foster private sector development. Addressing regional disparities will also be instrumental in this respect.

In 2020, the AfDB, EBRD and EIB together provided more than MAD 18.6 billion (of which more than MAD 4 billion for the AfDB, MAD 7.9 billion for the EBRD, and MAD 6.7 billion for the EIB) in financing for development in Morocco. We remain committed to supporting private sector development and look forward to continuing working with the Moroccan authorities and the private sector, each institution according to its own strategy and remit, and in partnership with local stakeholders and civil society. We would like to sincerely thank the Moroccan authorities and representatives of the public and private sectors for their warm hospitality and cooperation during our mission and the frank and productive discussions.

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Executive Summary

Due to the outbreak of the Covid-19 pandemic, Morocco suffered a recession in 2020, as many other economies in Africa and in the rest of the World. The swift and strong policy response of the Moroccan authorities helped address the economic and health crises. The negative impacts of the pandemic on trade, economic activity and financial market are expected to slow down in 2021. Economic growth is projected to turn positive, supported by rebounding exports to the European Union, a good agricultural season, the partial return of tourists, and resilient remittances. After doubling in 2020, the fiscal deficit should resume its downward trajectory and returns to its long-term average.

Further private sector development could support higher employment and inclusiveness. In the short term, higher general government debt will constrain the fiscal space, and hence public investment. It is therefore paramount for the Kingdom to further enhance private sector dynamics. The pandemic also highlighted the dependence of Moroccan industries to few products and a limited number of markets. Greater economic diversification and participation in global value chains remains crucial going forward to ensure, alongside private sector led growth, a more inclusive and resilient growth. Addressing regional disparities will be instrumental in this respect.

The Moroccan economy has enjoyed a relatively stable political and macroeconomic environment over the past two decades. This stability has allowed the country to benefit from one of the best investment climates in Africa. Morocco now compares and benchmarks its performance and objectives with more advanced economies in Central and Eastern Europe. The government budget remains within acceptable levels of deficit, and public debt is under control and well managed, even after the outbreak of Covid-19. The current account deficit is financed sustainably, and foreign exchange reserves are large and stable. Inflation remains low, which contributes to stabilising the economy and keeping interest rates moderate.

Yet, various challenges hamper more inclusive and sustainable growth. Despite plans to develop sustainable irrigation infrastructure and significant steps taken to diversify the economy through industrial policies, economic output is less volatile than in the past but remains dependent on rainfalls. Moreover, economic growth has not been enough to respond to the population's welfare aspirations, as poverty and regional disparities are salient in significant segments of the population. Economic activity in rural areas remains concentrated in the agricultural sector: the *Plan Maroc Vert*, which ended in 2020, has so far yielded limited success in developing active private entrepreneurship. However, the new strategy "Green generation" covering the period 2020-2030 should help address these issues, by focusing on small farmers, women in rural areas, the youth and people in mountainous areas. In addition, an integrated programme was launched in 2020 to support and finance young small enterprises with less than 24 months of age. Hurdles to regional integration include underdeveloped digitalisation, absence of integrated infrastructure, challenging land access and low levels of education.

This has prompted King Mohammed VI to establish a committee to advise on a new development model. Among other things, this new development model would put emphasis on improving the economic integration of rural areas and fostering the inclusion of women, youth and lower skilled people. The greater role for private sector investment will certainly be crucial for its success, as the public sector, through large state-owned enterprises, is still one of the main engines of growth.

Boosting private investment faces various challenges. The development of the private sector in Morocco has typically focused on attracting foreign direct investment, mainly via the so-called "industrial ecosystems" that concentrate on a small number of companies. While small and medium enterprises make up roughly 90 percent of Moroccan firms, they struggle to invest, increase value added, scale up and

hire. Despite numerous reforms implemented by the authorities over the past two decades, domestic firms regularly report constraints to their operations, such as barriers to entry, difficult access to industrial land, low social capital, bureaucratic hurdles, a slow justice system and a cumbersome public procurement system. Moving forward, the digitalisation of processes in both the private and the public sector, such as upgrading e-governance initiatives, can prove crucial for unlocking private investment opportunities.

Access to finance is an overarching impediment to private investors, large and small alike. Morocco has one of the most developed banking sector in Africa. Yet too many firms, even in the formal sector, struggle to access bank finance, both for working capital and investment. Financial intermediation is held back by the relatively high concentration of bank lending to few large corporates, stringent collateral requirements, and the limited availability of credit information. A large share of the population does not have a bank account or an active relationship with a financial institution. Accelerating the implementation of the National Financial Inclusion Strategy would be essential, including through strengthening the key role of non-bank financial institutions, such as micro-finance institutions and leasing companies.

Private investment in Morocco has the potential to thrive if opportunities offered by stronger involvement in global value chains and deeper integration in Sub Saharan Africa are seized. Many of the aforementioned challenges could be transformed into opportunities for the private sector to engage deeper in economic activity – for example through public-private partnerships and by creating more incentives to invest in activities that support the green and digital

transformation of the economy. Global value chains (GVCs) account for an estimated 60 to 80 percent of global trade. Firms in emerging economies participating in a GVC not only benefit from higher export opportunities, but also from access to foreign technology licensed elsewhere and new forms of management practices. Over the past 15 years, Morocco has implemented proactive industrial strategies and integration in GVCs has increased significantly, notably for three promising sectors and ecosystems, namely health, automotive and aeronautics. Overall, Morocco's participation in GVCs is in line with comparable middle-income countries, but backward participation (i.e. the share of the foreign value added contained in Moroccan gross exports) is comparatively higher. Deeper integration with Sub-Sahara Africa should also enhance the share of domestic value included in exports.

While total exports have increased very rapidly over the past two decades, the main destination markets remain within the European Union. This relative dependence on Europe is currently being balanced by Morocco's efforts to benefit from regional trade and investment opportunities, particularly within Africa. The level of Moroccan trade and investment links to Sub Saharan Africa has been steadily increasing over the last two decades, but it is still modest. The recent expansion of Moroccan banks together with significant Moroccan foreign direct investments to Sub Saharan Africa indicate a deeper integration with the rest of the continent. Looking forward, policy recommendations to promote integration include increasing foreign direct investment, upscaling and supporting GVCs, removing current impediments to a deeper integration in Africa, improving access to finance and diversification of financial instruments, and defining appropriate industrial policies.

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1. Macroeconomic Environment

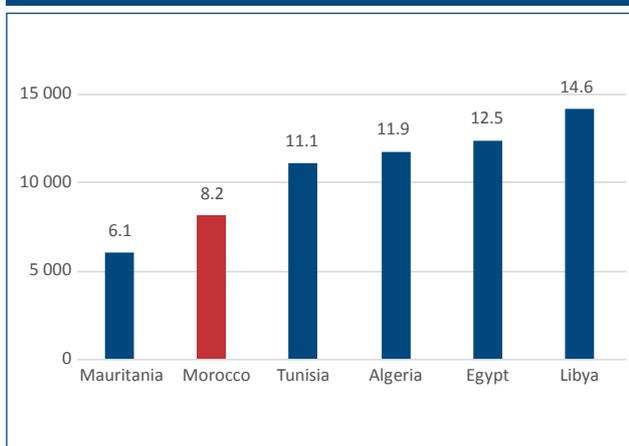
Prudent macroeconomic policies and political stability have fostered sustained economic activity in Morocco over the past two decades, with average annual real GDP growth exceeding 4 percent during the period 2000–19. Despite the increasing relevance of higher-value added services (such as tourism) and export-oriented industrial activities (such as the automotive sector), growth continues to be volatile due to significant reliance on a rain-fed agricultural sector that is vulnerable to adverse weather conditions. The outbreak of the Covid-19 pandemic and a severe drought has had a strong negative impact on the economy in 2020: Morocco suffered a recession and the largest fiscal deficit in the past twenty years. The public policy responses to the health emergency and to support business and households have been strong. However, the pandemic demonstrated the dependence of Morocco’s industries to few products and a limited number of markets. Private sector led growth should aim to be more inclusive and decrease regional disparities. Financial support from development partners will also help Morocco mitigate the impact of the pandemic and strengthen the resilience of the economy in the long term.

1.1 Macroeconomic developments up to 2019

Economic growth in Morocco has been strong over the past two decades, but this positive trend had started to slow down before the outbreak of the Covid-19 pandemic. Morocco is a lower middle-income country with a GDP per capita of USD 3,323 in 2019 (USD 8,148 in purchasing power parity (PPP) terms, Figure 1.1) and a

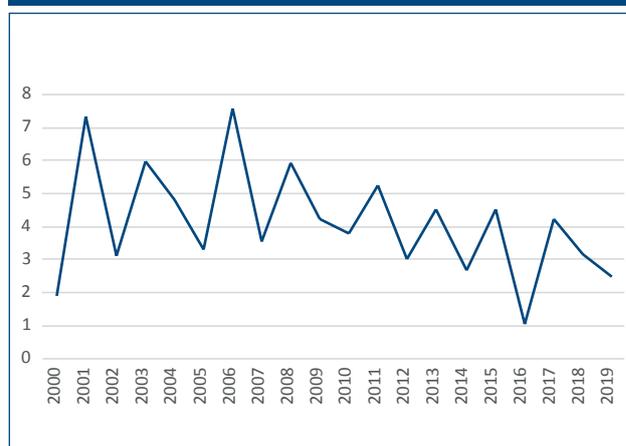
population of 36 million. Prudent macroeconomic policies and political stability have sustained economic activity over the past two decades, with average annual growth exceeding 4 percent during the period 2000–19 (Figure 1.2). However, the rate of real GDP growth has been slowing down in the past five years. It decreased to 2.6 percent in 2019, from 3.1 percent in 2018, constrained by low agriculture output.

Figure 1.1: GDP per capita in 2019 (USD, at PPP)



Source: Haut-Commissariat au Plan (HCP) and IMF World Economic Outlook (April 2021).

Figure 1.2: GDP growth 2000–19 (percent)



Source: Haut-Commissariat au Plan (HCP) and IMF World Economic Outlook (April 2021).

In the past five years, growth has been driven primarily by public spending and private consumption (Table 1.1).

Despite the relevance in Morocco's economic activity of high-value added services (such as tourism) and export-oriented industrial activities (such as the automotive sector) in GDP, growth continues to be volatile due to a rain-fed agricultural sector that is vulnerable to adverse weather conditions. Agriculture – which accounts for about 12 percent of GDP and provides more than 30 percent of jobs – suffered various drought-induced contractions over the past decade, including in the seasons 2018/2019 and 2019/2020.

The prolonged period of economic expansion, albeit volatile, has allowed Morocco to reduce poverty substantially.

Yet, regional disparities persist, and the poverty rate remains high in rural areas. The agricultural sector still accounts for much of economic activity outside urban centres, while income per capita is significantly higher in regions with a high urbanisation rate (Table 1.2). The rural-urban divide translates into large differences in terms of access to public services, infrastructure, health, education, employment opportunities in the formal private sector, and access to finance – notably for women (as highlighted in Chapter 4).

Table 1.1: Real GDP growth and contributors (annual growth rate, unless indicated otherwise)

	2015	2016	2017	2018	2019
Real GDP growth	4.5	1.1	4.2	3.1	2.6
Household consumption	2.3	3.7	3.8	3.4	1.8
Government consumption	2.4	1.5	2.1	2.7	4.7
Gross fixed capital formation	0.2	8.8	-0.2	1.2	1.0
Exports of goods and services	5.5	6.0	11.1	6.0	5.5
Imports of goods and services	-1.1	14.5	7.9	7.4	3.3
Agriculture (percent of GDP)	12.6	12.0	12.4	12.2	12.2
Industry and construction (percent of GDP)	26.1	25.9	26.2	25.9	25.3
Services (percent of GDP)	49.7	50.4	50.0	50.1	50.9

Source: Haut-Commissariat au Plan (HCP) and World Bank's World Development Indicators (April 2021).

Morocco is also struggling with a relatively high unemployment rate. Unemployment reached 9.2 percent of the labour force in 2019, and it is particularly high for women (13.5 percent), the youth (24.9 percent) and young people in urban areas (39.2 percent). Unemployment and underemployment (also estimated at 9.2 percent of

the active population in 2019) are likely to be a larger problem than suggested by official figures, notably due to the large informal sector – which is estimated at about 30 percent of GDP (Medina and Schneider, 2018) – and the low female labour force participation rate (22 percent).

Table 1.2: Regional GDP per capita in 2018 and urbanisation rate in 2017

	GDP per capita (MAD)	GDP per capita (100 = Morocco)	Urbanisation rate (percent)	Share of population (percent)	Share of GDP (percent)
Beni Mellal – Khenifra	24.397	78	50.4	7.3	5.7
Casablanca – Settat	49.654	158	75.1	20.5	32.3
Dakhla – Oued ed Dahab	85.669	272	77.3	0.5	1.3
Drâa – Tafilalet	16.747	53	35.2	4.8	2.5
Fes – Meknes	21.483	68	62.1	12.3	8.4
Guelmim – Oued Noun	36.157	115	66.7	1.3	1.4
Laâyoune – Saguia al Hamra	49.275	157	94.5	1.1	1.7
Marrakech – Safi	19.870	63	43.5	13.3	8.4
Oriental	22.832	73	68.3	6.8	4.9
Rabat – Sale – Kénitra	36.218	115	71.0	13.5	15.6
Souss – Massa	26.479	84	58.9	8.0	6.7
Tanger – Tetouan – Al Hoceima	32.114	102	61.0	0.6	10.8
Morocco	31.473	100	60.8	100	100

Source: Haut Commissariat au Plan: "Compte régionaux de l'année 2018" and "Maroc des régions 2018".

The business environment is considered to be among the best in North Africa. With a rank of 53 out of 190 countries in the 2020 World Bank Doing Business Report (Table 1.3), Morocco is the best performer in North Africa and is among the top three countries in Africa – after Mauritius (global rank 13) and Rwanda (global rank 38). Morocco made significant reforms to the business environment over the past decade, which are reflected in the rapid improvement in the Ease of Doing Business index between 2010 and 2020. Morocco is also ranked 75th out of 141 countries in the 2019 World Economic Forum's Global Competitiveness Report, the best rank in North Africa and the third position in Africa –

after Mauritius (global rank 52) and South Africa (global rank 60).

However, human development remains relatively low compared to other countries in North Africa. Despite the relatively high life expectancy at birth at 77 years, the 2019 UNDP Human Development Report classifies Morocco as a medium development country, with a rank of 121 out of 189 countries, the lowest rank in North Africa after Mauritania (Table 1.3). For example, average years of schooling of adults is only 5.5 years in Morocco, compared to 4.6 years in Mauritania but more than 7 years in the other countries of North Africa.

Table 1.3: Doing Business, Global Competitiveness and Human Development Index rankings

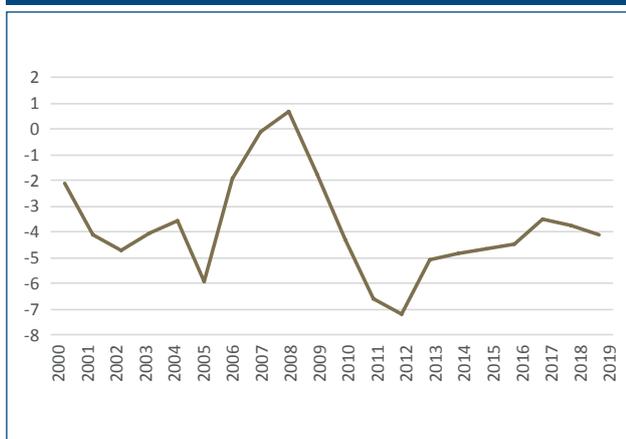
	Ease of Doing Business (DB)		Global Competitiveness Index (GCI)		Human Development Index (HDI)		Change over time		
	2010	2020	2010	2019	2010	2019	DB	GCI	HDI
Algeria	136	157	86	89	84	82	-21	-3	+2
Egypt	106	114	81	93	101	116	-8	-12	-15
Libya	-	186	100	-	53	110	-	-	-57
Mauritania	166	152	135	134	136	161	+114	+1	-25
Morocco	128	53	75	75	114	121	+75	0	-7
Tunisia	69	78	32	87	81	91	-9	-55	-10

Source: World Bank Group, World Economic Forum and UNDP. Note: A lower ranking means a better performance.

During this period of economic and political stability, Morocco has managed to reduce external and fiscal imbalances, on the back of subsidy reforms coupled with a solid fiscal management and financial oversight. The fiscal deficit was reduced to 4.1 percent of GDP in 2019, from the peak of 7.2 percent in 2012 (Figure 1.3). Public debt has gradually increased in recent years: It reached

64.8 percent of GDP in 2019, up from 58.2 percent of GDP in 2012. Before the Covid-19 outbreak, both public and external debt were assessed to be sustainable (IMF, 2020a). However, the growing debt of public enterprises and institutions, which was estimated at 13.8 percent of GDP in 2019, while it amounted to 11.6 percent of GDP in 2012, is a cause of concerns (see Box 1.1).

Figure 1.3: Fiscal balance (percent of GDP)



Source: Haut-Commissariat au Plan (HCP) and IMF World Economic Outlook (April 2021).

Figure 1.4: Current account balance (percent of GDP)



Source: Haut-Commissariat au Plan (HCP) and IMF World Economic Outlook (April 2021).

The current account deficit decreased to 3.7 percent of GDP in 2019, from the peak of 9.5 percent in 2012, helped by declining import prices and subsidies, especially in the energy sector (Figure 1.4). In addition to phosphates, new industrial exports, particularly in the automotive and aeronautics sectors, have improved export performance in recent years. Morocco's main trading partner is the European Union (in particular Spain and France), accounting for more than half of exports.

The inflation rate has remained relatively low in the past decade, at 1 percent on average. Monetary policy in

Morocco aims at maintaining price stability in the context of an exchange rate peg to a basket of currencies. The Moroccan Dirham (MAD) is pegged to a currency basket consisting of EUR (60 percent) and USD (40 percent). Following strong pressure on the foreign exchange market in 2017, the authorities introduced a managed floating exchange rate system in January 2018 and broadened the fluctuation band to ± 2.5 percent range around the reference price (up from ± 0.3 percent previously). On March 6 2020, the floating bands were widened again to ± 5 percent range to support the transition to a more flexible exchange rate regime.

Box 1.1: The growing debt of State-owned enterprises

The State plays an important role in the economy. In 2019, the State portfolio included 225 public companies, 43 companies in which the Treasury has a direct holding as well as 449 subsidiaries or entities in which the State has some participation (the State is the majority shareholder in 54 percent of them).

The modernisation of Morocco is supported by the State's presence in the economy, especially via large infrastructure projects in transport (road, port, airport and railways) but also in the water and energy sectors. State-owned enterprises (SOEs) account for two thirds of public investment and for close to 10 percent of GDP.

The debt of SOEs has reached a high level and now encompasses substantial fiscal risk. SOEs have contracted debt estimated at about 13.8 percent of GDP in 2019. The vast majority (95 percent) of this debt is concentrated among large groups in the sectors of mining, energy, water, waste, and transport. In the analysis of the total public sector debt of Morocco, the debt of SOEs, which is guaranteed by the State, should be added to the central government debt totalling 65 percent of GDP in 2019.

The special commission on the new development model, mandated by the King Mohammed IV, presented its conclusions in May 2021. In this context, Morocco will set up a State participation agency, whose objective will be the strategic and efficient management of State participations.

1.2 Economic outlook: 2020 and beyond

The impact of the Covid-19 crisis has dealt global growth a heavy blow, and Morocco is no exception. In 2020, the real growth rate of global GDP is projected to decrease to -4.2 percent, down from 2.8 percent in 2019, before rebounding to 5.2 percent in 2021 (IMF, 2020b). The GDP of the EU, Morocco's most important commercial partner, should retract to a staggering -7.8 percent, down from 1.3 percent in 2019, before recovering to 4.1 percent in 2021 (European Commission, 2020). Africa's real GDP growth is forecasted at -2.4 percent in 2020 (from 3.2 percent in 2019)¹. In 2020, North Africa should fare better than the rest of the continent with a real GDP growth rate at -1.6 percent².

In 2020, Morocco experienced a recession, the first in more than 20 years, and a concomitant deterioration of its fiscal stance. The real GDP growth rate fell to -6.3³ percent in 2020, from 2.6 percent in 2019. The economy

suffered from the Covid-19 outbreak as well as a drought⁴. In 2021, real GDP growth is expected to rebound to 4.8 percent⁵, above the African continent 3.1 percent average.

The Covid-19 outbreak has implied a wave of external and domestic shocks. The disruptions of global value chains as well as the sudden economic slowdown in the European Union, especially in Morocco's main trading partners (Spain, France, Italy and Germany), have weighed on demand for key Moroccan exports. In 2020, exports dropped by 7.6 percent, according to estimates of the Moroccan Treasury. The contraction has been particularly severe over the second quarter (-27.5 percent), before regaining in the third and fourth quarters, especially in the automobile sector which accounts for a fourth of total exports. Likewise, the two other most important exports, phosphate and derivative as well as agricultural products have rebounded. On another hand, exports of leather and textile have remained subdued.

¹ African Development Bank forecast by the Statistical Department. Average real GDP growth rate for the African continent excludes Libya.

² The North Africa region regroups Algeria, Egypt, Libya, Morocco, Mauritania and Tunisia.

³ The Department of Treasury and External Finances estimated the real GDP growth rate in 2020 at -6.3 percent.

⁴ Morocco experienced three recessions in the 90's, with negative real GDP growth rate in 1992 (-2.09 percent), 1995 (-5.3 percent) and 1997 (-1.56 percent).

⁵ The Moroccan authorities forecast a growth rate of 5.4 percent in 2021.

The decrease in production and in consumer demand have implied a slowdown of imports by 14.1 percent in 2020. Morocco's trade balance is structurally in deficit with a yearly average of -16 percent of GDP over the last five years. This is projected to improve in 2020, given the reduction of imports especially capital good and energy which in 2019 respectively accounted for 28.5 percent and 19.6 percent of

total imports. The substantial drop in oil prices have mitigated the impact of the energy bill on the current account balance. In 2020, the current account deficit improved by 2.2 percentage points of GDP and reached 1.5 percent of GDP, supported by a decrease in imports that was higher than the fall in exports, the resilience of remittances and grants from the European Union.

Table 1.4: Macroeconomic data and projections (annual growth rate or percent of GDP)

	2012-16	2017	2018	2019	2020(e)	2020(p)	2020(p)
Real GDP growth (%)	3.2	4.2	3.1	2.5	-6.3	4.8	3.5
CPI inflation (%)	1.4	0.7	1.6	0.2	0.7	0.1	0.7
Fiscal balance* (% of GDP)	-5.2	-3.5	-3.8	-4.1	-7.7	-6.7	-5.9
Current account balance* (% of GDP)	-5.9	-3.4	-5.3	-3.7	-1.5	-3.1	-4.3

Source: Data from Moroccan authorities, estimates (e) and projections (p) based on AfDB calculations.

Tourist arrivals and total tourism receipts have steadily increased since 2009, with a yearly average of 5 percent and 2 percent respectively. In 2019, tourism receipts represented around 17 percent of exports and 6.5 percent of GDP. In 2020, tourism receipts have fallen by 53.8 percent whereas tourist arrivals are down 79 percent compared to a worldwide 74 percent drop. Concerning worker remittances, in April 2020, the World Bank projected a 20 percent drop, which has not materialised⁷. On the contrary, according to the latest figures communicated by the Office des Changes, worker remittances increased by 5.3 percent in 2020.

Starting mid-March 2020, the Moroccan authorities instituted a three months strict lockdown to contain the spread of the virus (see Box 1.2). Household consumption has slowed down due to the negative impacts of the drought on rural incomes and of the pandemic on the labour market, which experienced a net loss of 432 thousand jobs in 2020, whilst unemployment increased to 11.9 percent in 2020 (5.9 percent in rural areas and 15.8 percent in urban areas), up from 9.2 percent end of 2019. The drop of capital goods imports and of public investment hint to an overall reduction of investment.

Large publicly financed projects have supported investment in recent years. The negative impact of the pandemic on public finance could be a constraint to new projects.

In 2020, the fiscal deficit is projected to double, reaching close to 8 percent of GDP, up from 4.1 percent in 2019. The sharp deterioration of the fiscal stance is due to (i) lower consumption which implied lower taxes on goods and services which account for half of tax revenues; (ii) decreasing direct tax receipts (ii) increasing expenditures in goods and services and civil servant wages. In October 2020, the IMF projected the general government debt over GDP to jump to 76.4 percent of GDP, up from 64.8 percent in 2019. The debt over GDP ratio is expected to revert to a downward trajectory as early as 2021, reaching 70 percent of GDP in 2025. The IMF considers the public debt to be sustainable, despite increased vulnerabilities to shocks (IMF, 2021). While refinancing needs of the country have risen, the risks remain very limited due to long average maturity of the sovereign debt at 7 years and 4 months. The cost of the debt is moderate, at 3.6 percent on average, and the vast majority of the debt is at fixed term (92.5 percent).

⁷ World Bank Predicts Sharpest Decline of Remittances in Recent History, Press Release April 22 2020.

Morocco has been able to access funding to absorb the negative impacts of the pandemic on its financing needs.

Financial support from the IMF and development partners has enabled Morocco to limit the social and economic impact of the Covid-19 pandemic and maintain an adequate level of official reserves to ease balance-of-payments pressures. In early April 2020, the Moroccan authorities drew on all the resources available under the Precautionary and Liquidity Line (about USD 3 billion, or 3 percent of Morocco's GDP) covering the period 2018-20. In early January 2021, Morocco repaid in advance parts of the funds drawn under the IMF Precautionary and Liquidity Line, amounting to USD 936 million. At the end of December 2020, foreign exchange reserves increased by MAD 67.4 billion, an increase of 26.7 percent compared to December 2019, and amounted to MAD 321 billion (USD 36 billion). These reserves, three times the size of the debt due in the short term (over the coming year), mitigate any substantial risk that could threaten macroeconomic stability in the event of an external shock or put excessive pressure on the exchange rate of the dirham. Inflation remains low, and the real effective exchange rate has not appreciated much in recent years. The risk of capital flight is also limited, due to the control on Moroccan residents' financial transactions with the rest of the world. In addition, remittances increased in 2020.

Morocco has not experienced drastic pressures on its currency. In early March 2020, the Moroccan authorities widened the fluctuation band of the dirham to ± 5 percent from ± 2.5 percent (as of January 2018; ± 0.3 percent previously), while keeping the benchmark currency basket

unchanged (60 percent to the euro and 40 percent to the U.S. dollar). The objective is to increase the ability of the economy to absorb external shocks and improve competitiveness. Since the previous adjustment of the dirham fluctuation band in 2018, its volatility has remained moderate, in a stable range of ± 2.0 percent. So far, the Covid-19 crisis has not triggered pressure on the exchange rate. Over the last two years, Bank Al-Maghrib has hardly intervened in the foreign exchange market. Banks have themselves covered their positions and foreign exchange requirements in the interbank market. Following the outbreak of the Covid-19 pandemic, Bank Al-Maghrib decreased its benchmark interest rate, by 25 basis points to 2 percent on 17 March 2020 and by 50 basis points to 1.5 percent on 16 June 2020, to support the economy.

Morocco remains liquid in the international financial markets and continues to benefit from the support its partners through various financial instruments. In September 2020 Morocco issued a Euro 1 billion bond on the international financial market, with two Euro 500 million tranches. The first tranche has a maturity of 5.5 years, and a coupon of 1.375 percent, whilst the second tranche has a 10-year maturity, a coupon of 2 percent. In December 2020, Morocco issued again for a total of USD 3 billion in three tranches: (i) the first tranche has a maturity of 7 years and amounts to USD 750 million, (ii) the second tranche has a maturity of 12 years and amounts to USD 1 billion, and (iii) the third tranche has a maturity of 30 years and amounts to USD 1.25 billion.

Box 1.2: Measures enacted by the authorities to address the Covid-19 crisis

A series of health measures have been implemented to limit the spread of the virus. A state of health emergency was declared on 20 March 2020, which has been extended several times. The authorities adopted various containment measures, including an initial strict three-months lockdown.

At the economic and social level, a number of measures have been taken as well. The authorities established in mid-March a Special Fund for the management of the Covid-19 crisis. The Special Fund aims at strengthening the healthcare system and to mitigate proactively the economic and social impact of the virus. The Fund, whose management is entrusted to the Ministry of Economy and Finance, was endowed with an initial envelope of MAD 10 billion from the State budget. This fund also benefited from contributions of institutional partners, the private sector, citizens and regions and mobilised a total amount of close to MAD 34.6 billion.

An Economic Watch Committee (EWC) has also been created under the leadership of the Ministry of Economy and Finance in order to monitor closely the situation and ensure swift decision-making and execution to support the national economy. The EWC opted for the implementation of a series of actions aimed at reducing the social impacts of the containment measures on affected employees and workers operating in both the formal and the informal sectors. These include the payment of a monthly allowance of MAD 2,000 to employees of companies having difficulties and the introduction of direct monthly assistance ranging from MAD 800 to MAD 1,200 for workers in informal sectors, distributed through various channels including mobile payments.

The Economic Watch Committee introduced a budget and tax package. These fiscal decisions aimed at reducing pressure on companies. They include the suspension of social security contributions from companies between March and June 2020 and a moratorium on bank loans and lease repayments until 30 June without additional costs or penalties for companies requesting it. For microenterprises and SMEs having difficulties, banks established a credit line to provide additional working capital, guaranteed by the State at 95 percent with an interest rate indexed to the central bank's key interest rate, and companies with turnover less than MAD 20 million in 2019 have the possibility of postponing tax filing.

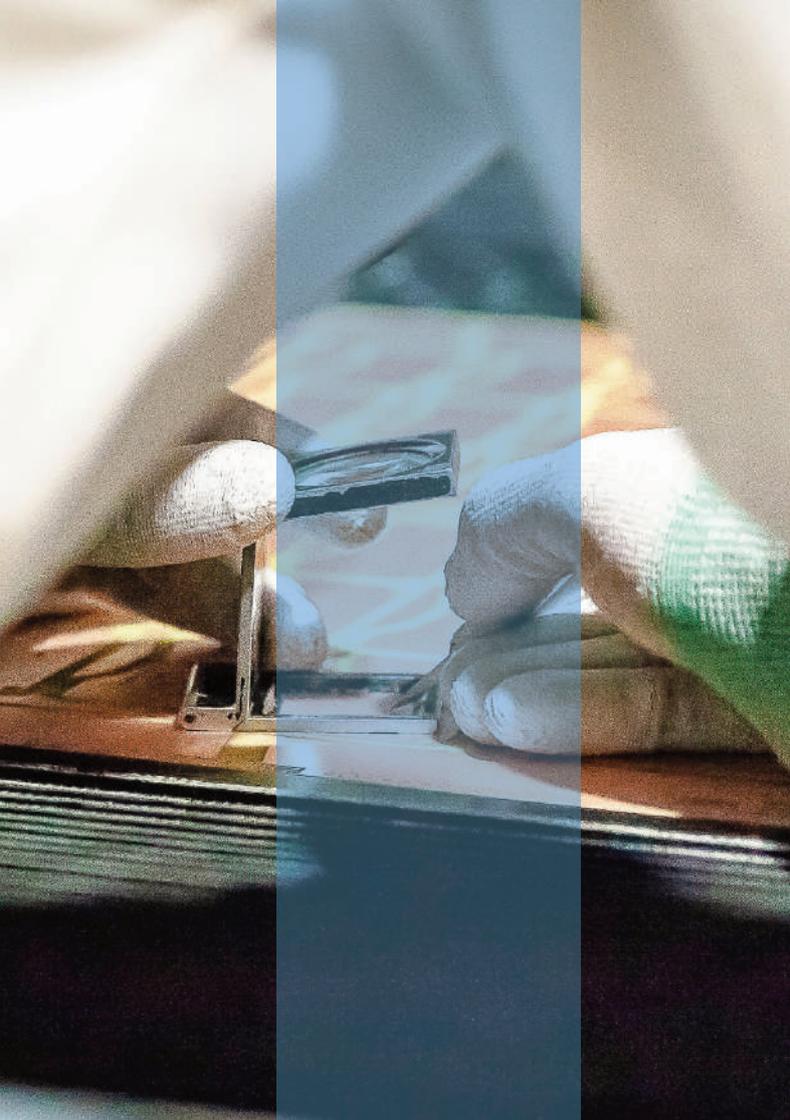
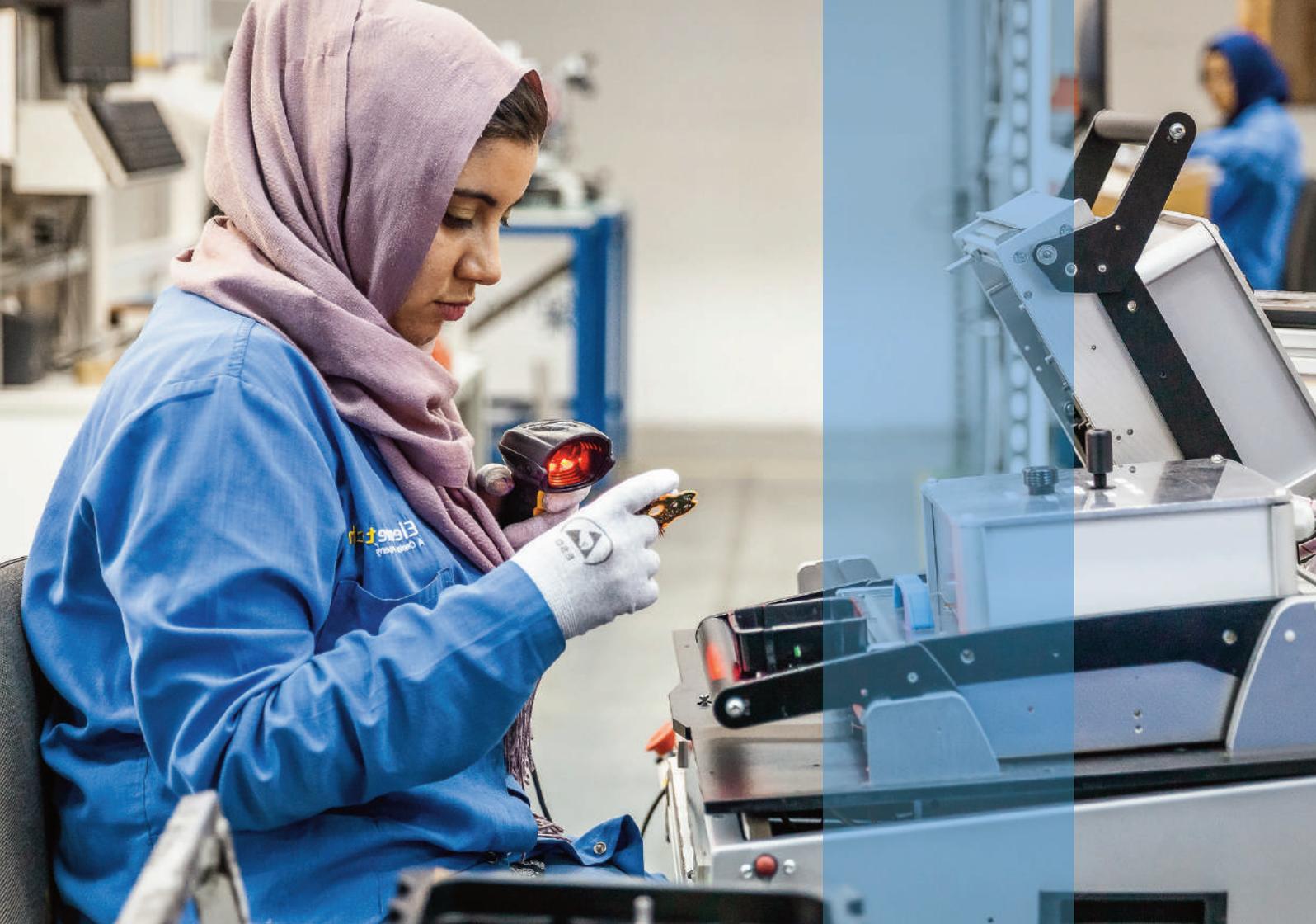
Bank Al-Maghrib has taken monetary and financial measures to manage foreign currency reserves and to give more liquidity space to the banking sector such as the extension of foreign currency swaps against the dirham and the trebling of the refinancing capacity of the central bank and broadening the range of eligible collateral. For microenterprises, BAM broadened the refinancing programme to include working capital loans in addition to investment loans, in addition to reducing the key interest rate by 75 basis points to 1.50 percent, authorising banks to postpone the provisioning of credit risk which will be subject to a moratorium for the period to June 2020, easing capital buffers by 50 basis points for a period of 12 months, reducing the regulatory minimum ratios to 8.5 percent for the tier 1 capital ratio and to 11.5 percent for the capital adequacy ratio and the promoting of the use of mobile payments and the reduction of the use of cash.

1.3 Future challenges

Due to the outbreak of the Covid-19 pandemic, Morocco suffered a recession in 2020, as many other economies in Africa and in the rest of the World. The swift and strong policy response of the Moroccan authorities helped address the economic and health crises. The negative impacts of the pandemic on trade, economic activity and financial market are expected to slow down in 2021. The African Development Bank projects real GDP growth to resume in 2021 at 4.5 percent and to decelerate in 2022 at 3.2 percent. Economic growth is projected to turn positive, supported by rebounding exports to the European Union, a good agricultural season, the partial return of tourists, and resilient remittances. After doubling in 2020, the fiscal deficit should resume

its downward trajectory and return to the long-term average.

Over the medium term, further private sector development could support higher employment and inclusiveness. In the short term, higher general government debt will constrain the fiscal space, and hence public investment. It is therefore paramount for the country to further enhance private sector dynamics. The pandemic also highlighted the dependence of Moroccan industries to few products and a limited number of markets (as highlighted in Chapter 5). The economy should aim to further diversify its exports and its participation in global value chains. Private sector led growth should also aim to be more inclusive and help reduce regional disparities that were relatively high at the onset of the pandemics.



2. Private Sector Overview

Despite strong proactive policies by the government and one of the most diversified and business friendly economies in the region, Morocco's private sector still struggles to create jobs in the formal sector and increase the value of SMEs. The Moroccan government has implemented several development policies via public investments and the activities of state-owned enterprises that represent a substantial part of the country's GDP. Promoting foreign direct investment flows has been at the core of national development policies in Morocco in recent years, with the creation of "industrial ecosystems", providing easy access to economic and human resources for foreign companies. While these ecosystems have been successful in attracting foreign investment, they have resulted in a dichotomy in the Moroccan economy, with the successful establishment of foreign companies but limited spillovers to the local businesses. The authorities have also adopted sectoral and regional development strategies, which have been mostly effective.

2.1 Overview of the local private economy

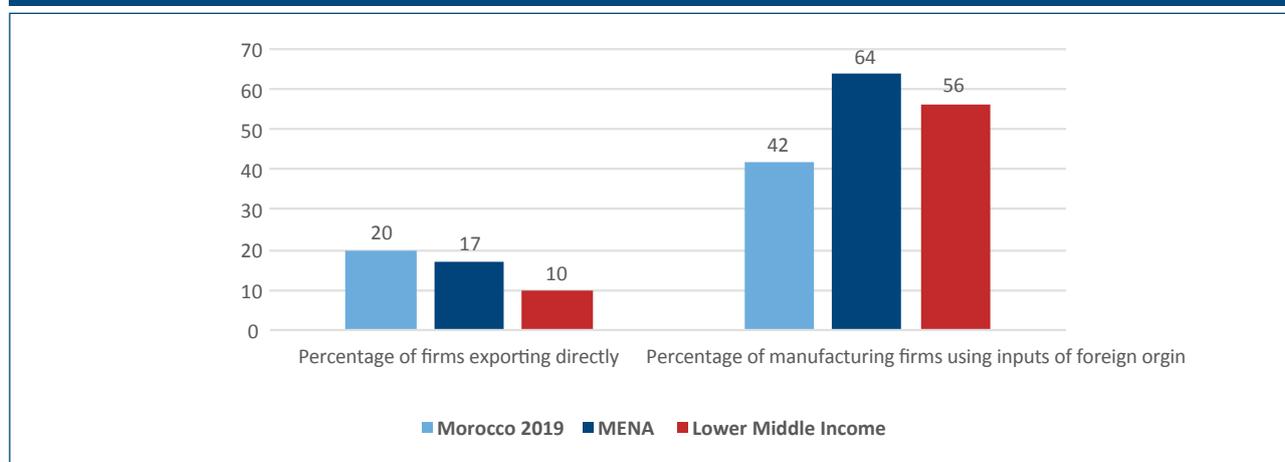
Morocco has one of the most stable investment climates and diversified economies in the region. In 2019, 57 percent of the value added was produced by the services sector, which is a major contributor to the economy. Tourism accounts for 12 percent of GDP and 12.9 percent of total employment, according to the World Travel and Tourism Council, and it is a major source of growth. However, Covid-19 has brought the tourism's activity to a halt and it is difficult to predict how the sector will evolve after the pandemic. 30 percent of the value added was produced by the industry sector, with a major role played by FDI in the textile and automotive sectors, with the textile sector being a major creator of employment.

Agriculture plays a significant role in the economy. It employs 37 percent of the active population and represents

13 percent of value added. The agribusiness sector has a significant potential, but Moroccan companies struggle to go up the value chain. For example, the agriculture strategy *Plan Maroc Vert* resulted in an impressive increase in the production of olives, citrus and red fruits, but the lack of downstream links and transformation process resulted in significant food loss, according to the Food and Agriculture Organisation of the United Nations (FAO).

Moroccan private sector firms remain more active than their peers in neighbouring countries. According to the latest wave of the Enterprise Survey, carried out jointly by the EBRD, the EIB and the World Bank Group, average annual retail growth, reaches on average 13 percent, much better than the average of the MENA peers (at -5 percent). 27 percent of firms spend on R&D investments, higher than the average in the MENA region (23.3 percent)⁸. They also export more than the average in the MENA region (Figure 2.1).

⁸ Enterprise Surveys are firm-level surveys of a representative sample of an economy's private sector. The surveys cover a broad range of business environment topics including access to finance, infrastructure, competition, and performance measures. The Enterprise Survey is answered by business owners and top managers. Formal (registered) companies with 5 or more employees are targeted for interview. Firms with 100 percent government/state ownership are not eligible to participate. The sampling methodology is stratified random sampling. The strata are firm size, business sector, and geographic region within a country. Sector breakdown is manufacturing, retail, and other services. In Morocco, 1,096 enterprises were interviewed between May 2019 to January 2020. For more details about the methodology of Enterprise Surveys and the questionnaires, see: <https://www.enterprisesurveys.org/en/methodology>.

Figure 2.1: Exporters and importers (percent)

Source: EBRD-EIB-World Bank Enterprise Surveys.

Despite an active private sector compared to other MENA countries, investment and value added are concentrated in a small number of companies. Private sector investment is at 16 percent of GDP but 63 percent of value added is owned by large enterprises (“grandes entreprises”, with turnover over MAD 175 million). While SMEs make up roughly 90 percent of Moroccan firms, they struggle to invest, increase value added and scale up. According to Bank Al-Maghrib, SMEs only contribute around 20 percent of GDP and 30 percent of exports. However, they create a significant share of jobs in the informal sector, which is estimated at 30 percent of GDP.

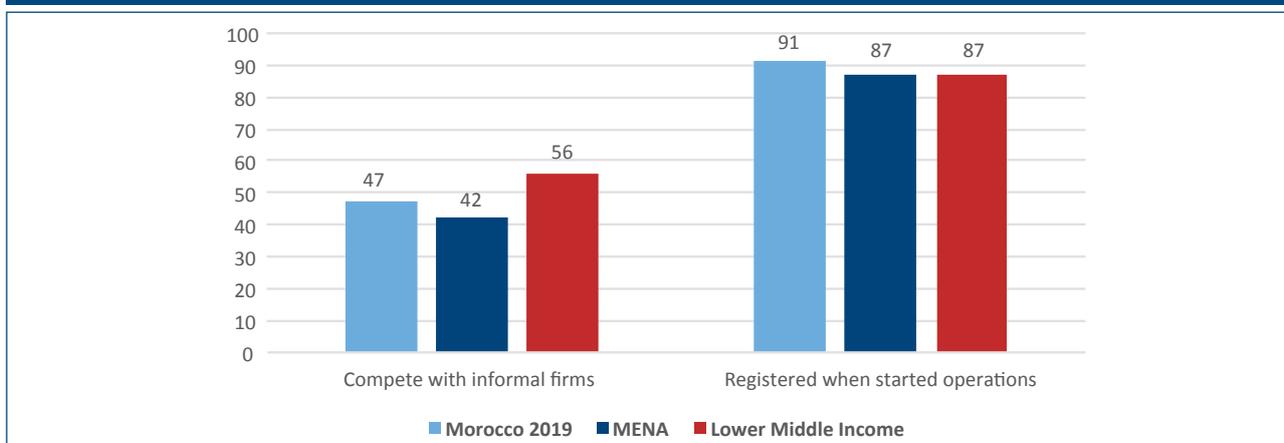
A number of issues in the regulatory environment are not conducive to starting and operating a business. According to the 2020 World Bank’s Doing Business Report, where Morocco ranked 53rd up from 128th a decade earlier, getting credit constitutes the biggest challenge for doing business (ranked 119th out of 190), followed by access to property (81st), and resolving insolvency (73rd).

Private firms in the formal sector also put forward a number of obstacles to private sector development. According to Enterprise Survey, clientelism is the biggest

business environment obstacle (reported by 15.5 percent of the firms), followed by tax rates (15.2 percent), tax administration (14.2 percent), and practices of the informal sector (9.1 percent). A similar result was highlighted by the national firm-level survey conducted by the Haut Commissariat au Plan (HCP) in 2019, where the lack of transparency was mentioned by 15.5 percent of companies that tendered to a public contract.

Informality is also prevalent in the private sector. A large share of firms (47.2 percent) consider that they have to compete against unregistered or informal firms (Figure 2.2). According to Bank Al-Maghrib, the size of the informal economy decreased between 2009 and 2018, but remains high at 30 percent of GDP. The strategies implemented since the early 2000s to improve the institutional, economic and financial environment have helped to reduce the size of the informal economy from 40 percent in 1998. However, the persistence of significant informal activities requires additional structural reforms, including those related to education, the justice system, tax policy and the labour market. Further, the contribution of SMEs to formal employment and to growth remains small and they have been hit particularly hard by the Covid-19 crisis (see Box 2.1).

Figure 2.2: Firms and informality (percent)



Source: EBRD-EIB-World Bank Enterprise Surveys.

Box 2.1: SMEs in Morocco and the Covid-19 crisis

SMEs have been disproportionately affected by the consequences of the Covid-19 crisis compared to medium and large size enterprises. A follow up of the Enterprise Surveys on Covid-19 was conducted between July and August 2020 and suggests that on average, small firms had a stronger decrease in sales that larger firms (50 percent compared to 43 percent) and stronger decrease in weekly hours (56 percent compared to 44 percent). Small firms were also more likely to delay payments (68 percent compared to 51 percent), less likely to have received pandemic-related government support than medium-sized firms, but not large firms (26 percent for small firms, 37 percent for medium size firms and 22 percent for large firms). Further, small firms were more likely to expect that they will not return to the “normal” level of sales. They are also less likely to have started or increased online business activity.

2.2 Public investment and private sector development

The public sector is the major engine of growth in the Moroccan economy. While total investment is at 32 percent of GDP in 2019, the public sector, investing mainly through state-owned enterprises (SOEs), accounts for between half (according to the IFC) and two thirds (according to local public banks) of total investment in the country. The role of the State is also crucial in terms of employment, with 42 percent of employees in the formal sector (Haut Commissariat au Plan et Banque Mondiale, 2017).

In recent years, the government has channelled its development activities via the adoption of national and

regional strategies for development, which have been mostly effective. Sectoral strategies include an industrial strategy adopted for the period 2014–20 aiming at increasing foreign direct investment through a public investment fund of EUR 2 billion, fiscal measures, and promotion of the expansion to Africa. They also include a strategy for the development of the mining sector (exploration, research and exploitation) worth EUR 4 billion of investments; a strategy aiming at digitalising the economy with targets such as providing equipment for small and medium enterprises (SMEs) and skills workshops for IT professionals; and a national plan for sustainable development adopted in 2011 with the year 2030 as a target. Moreover, eight out of the 12 Moroccan regions have adopted so far regional strategies for development, including the use of public funds for infrastructure projects,

as well as the development of public services and education.

Major SOEs are at the core of the development of the Moroccan economic activity, and they have been supported via national plans. SOEs play a major role in infrastructure and development projects. Although the government has revised its approach to intervening in the economy, carrying out privatisations in the 2000s and resuming this process in 2019, public enterprises continue to play a major role in supporting programmes and flagship

projects of the State. The investment spending of public enterprises accounts for the largest share of public investment. In particular, six SOEs represent about two-thirds of all subsidiaries and seven undertook nearly 60 percent of total SOEs investments in 2016. They are mostly focused on natural resources extraction (OCP, the phosphates company), utilities (ONEE, the electricity company), infrastructure (ONCF, the national railway operator), air transport (RAM, the national airlines), logistics (TMSA, the Tangier Mediterranean port company) and insurance (CDG, the asset management fund) (see Box 2.2).

Box 2.2: The role of Caisse de Dépôt et de Gestion in Morocco's development policies

Caisse de Dépôt et de Gestion (CDG, the Deposit and Management Fund) is a state-owned financial institution created in 1959 that manages long-term savings (two large pension funds of employees of state owned companies such as the OCP and public agencies). Since the 1990s, the institution also focuses on the industrial and regional development of the country, as well financial services such as housing finance. According to the IFC, its consolidated balance sheet represented 22 percent of GDP in 2017.

The company is a major investor in the economy through its subsidiaries or via partnerships, in a large range of sectors such as higher education, real estate development or tourism. In 2019, 44 percent of its portfolio was dedicated to real estate and regional development, 19 percent to retail banking and 14 percent to tourism, but the portfolio ranges across all major sectors of the Moroccan economy (Cour des Comptes du Royaume du Maroc, 2019). Thanks notably to its privileged access to land, the CDG also plays the role of crowding in private sector investments or demonstration investments.

2.3 The role of the ecosystems in private sector development

Development policies in Morocco have been focused largely on attracting foreign direct investment (FDI) flows and large investments. In 2019, net FDI recorded 21.3 percent of GDP, mainly in the automotive and aeronautics sectors. The insurance sector was the largest recipient of FDI, although this was largely the result of the sale of a stake in a major local insurance company to a foreign investor. Manufacturing was the second-largest sector, which is encouraging in the context of the government's industrial development plans, followed by real estate.

FDI promotion has been channeled mainly via the development of the so-called "industrial ecosystems" (see Box 2.3). The first of these ecosystems was launched in 2014, with the implementation of the Plan d'accélération industrielle 2014–20 (PAI 1). In 2020, there are 47 industrial ecosystems, with Renault and Airbus deemed as the most successful ones. These ecosystems have been built with strong government support (with the government funding the local training), favourable taxation and access to land.

The focus on FDI has created a strong dichotomy in the Moroccan economy. Foreign companies – mainly in the automotive and textile sectors – have settled in successfully,

but their subsidiaries are often foreign companies and spillovers into Moroccan enterprises are limited. The increase of employment levels has also been disappointing. Moreover, while the ecosystems have attracted FDI, they have created a dichotomy within the Moroccan economy between the firms that operate in free zones and the firms that do not. Indeed, while there have been important benefits for the local and foreign companies integrated in the ecosystem, those outside of the ecosystem have not necessarily seen their business environment improve.

All in all, while there is a strong potential for the development of the private sector given both the levels of diversification and entrepreneurship, entrepreneurs in Morocco still struggle with a number of obstacles to private sector development. The government has focused its policies on investment by the public sector and the development of ecosystems, but it will have to inevitably tackle the remaining issues in order to develop, across all regions and sectors, a solid private sector.

Box 2.3: Ecosystems in the automotive sector

The proactive policy by the government, with the development of the ecosystems, has been quite successful in the automotive sector. The FDI-friendly policies have attracted major players from the automotive sector, led by two French manufacturers (Renault and PSA) and 200 suppliers. In 2019, the industry had the capacity to produce 700,000 cars per year and it employed 180,000 people, according to the Moroccan Association for Automotive Industry and Trade (AMICA). It is also one of the fastest generators of employment in the country, creating 28.8 percent of new jobs between 2014 and 2018, according to the Ministry of Industry, Investment, Trade and Digital Economy.

Despite undeniable successes of the development of this industry in Morocco, there have been limited spillovers into the local economy, with very few Moroccan firms joining the automotive clusters. Moroccan firms are excluded from the main benefits of the ecosystems and lack access to finance, land, as well as access to the labour force formed within the ecosystems. As a result, local sourcing has been limited. The government is however aware of the downsides and is trying to implement new favourable measures with the new *Plan d'Accélération Industrielle* for 2020–25 (PAI 2), currently being defined by the Ministry of Economy, Finance and Administration Reform (MEFRA) in parallel with the more inclusive work on the new development model.



القرض الفلاحي للمغرب
CREDIT AGRICOLE DU MAROC
CHANGE



CHANGE



CHANGE



MoneyGram
تحويل الأموال



AUX CONVOYEURS
E FONDS

RESERVE AUX CONVOYEURS
DE FONDS



Réservé à l'ONE

WEST
UN
من أموال

3. Access to Finance

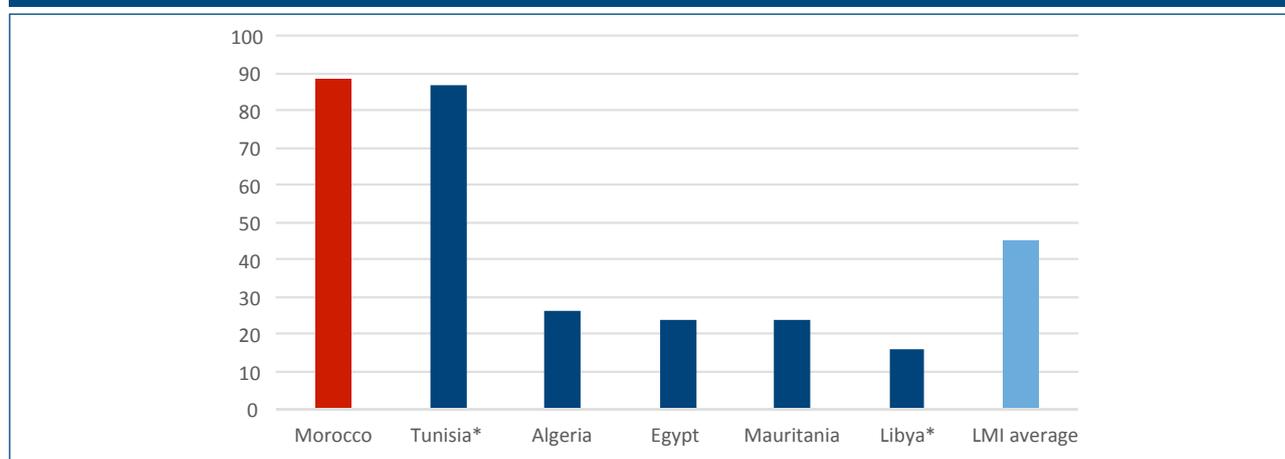
A well-functioning financial sector is essential for private sector development. A financial sector that provides efficient access to finance for individuals and firms can facilitate the exchange of goods and services, the diversification of risk, the mobilisation of savings and the identification of good business opportunities. Better access to finance can also help informal firms move into the formal sector and promotes the financial inclusion of disadvantaged social groups. Despite Morocco's large banking sector, the availability of external finance remains a constraint for many firms. Financial intermediation in Morocco is held back by the relatively high concentration of bank lending to few large corporates, stringent collateral requirements, and the limited availability of credit information. Even though the role of non-bank financial sector in Morocco is growing, its small size limits the choice of financial instruments for smaller firms. Following the outbreak of the Covid-19 pandemic, the authorities have put in place a series of measures to support businesses. Going forward, they will also need to increase digital financial services and financial literacy in order to expand financial inclusion and access to finance.

3.1 Structure of the banking system

Morocco possesses one of the most developed financial systems in Africa. Domestic credit to the private sector is equivalent to 88 percent of GDP in Morocco and is significantly higher than in other North African countries (with the exception of Tunisia) or the average of lower middle income

economies (Figure 3.1). The high level of sophistication of the banking system has allowed large Moroccan banks to develop and expand their activities in Africa, in part to accompany the expansion of large Moroccan corporate groups. Moroccan banks are present in about 35 countries all over Africa and cross-border exposure accounts for more than 20 percent of their assets and a third of their profits.

Figure 3.1: Credit to private sector in 2019 (percent of GDP)



Source: World Bank Group's World Development Indicators. Note: * Data for Tunisia refer to 2017 and for Libya to 2018. LMI average: Average of lower middle-income economies.

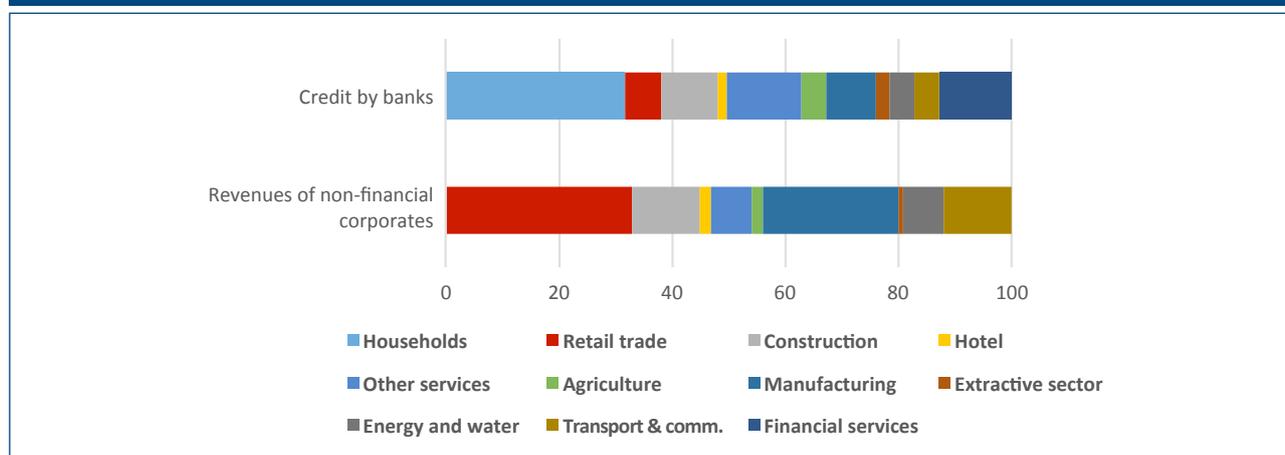
The financial sector is bank centric. It consists of 90 financial institutions, including 19 commercial banks, 12 microcredit associations, 27 financing companies and 6 offshore banks⁹. Total assets of the banking sector amounted to 123 percent of GDP in 2019. There are 7 foreign banks among the 19 banks operating in the country, while the Moroccan State is a majority shareholder in 5 banks. The share of public banks has been declining over the past decades to 18 percent of total assets in recent years (from 40 percent in 2002), while foreign banks represent 16 percent of assets.

The structure of the banking system is characterised by a high degree of concentration. The three largest banks (Groupe Attijariwafa Bank, Groupe BMCE Bank of Africa, and Groupe Banque Populaire) account for about 65 percent – and the five largest banks for about 80 percent – of total banking sector assets, deposits and credit.

Banks' balance sheets are comprised mostly of customer loans, which represent 60 percent of total credit. They are funded mainly by deposits, which account of 68 percent of total funding. About 19 percent of deposits come from Moroccans living abroad. Interbank loans have been declining in recent years to 13 percent of assets, while banks' exposure to securities increased to 22 percent of assets (of which the majority consist of treasury bills).

Households represent about a third of bank credit, while financial services, other services, construction and manufacturing each represent about 10 percent of credit (Figure 3.2). This suggests that credit is relatively diversified across various sectors of the economy. However, credit is often concentrated on the same large corporates, including state-owned corporations, and bank loans to SMEs only account for 18 percent of total credit. Despite strict regulatory limits, risks from large credit exposures have persisted in recent years (IMF, 2021).

Figure 3.2: Economic activity of non-financial corporates and credit by banks in 2019 (percent)



Source: Bank Al-Maghrib, *Rapport sur la stabilité financière, Exercice 2019, Numéro 7*.

⁹ The banking sector accounted for 63 percent of total assets of the financial system in 2019. The financial system also includes an insurance sector (24 insurance and reinsurance companies, which represent about 10 percent of the financial system), 4 pension funds (of which 2 are public) that account for 20 percent of the financial system, and the Casablanca Stock Exchange, which is dominated by banks, telecommunication and construction companies.

Most financial soundness indicators remain relatively comfortable by regional standards. Measures of asset liquidity and profitability, such as return on assets and return on equity, remain relatively comfortable compared to other countries in North Africa (Table 3.1). Capital ratios, however, are tight. The gross non-performing loans (NPLs) ratio of 7.5 percent, though acceptable by regional standards, is relatively high and is expected to increase in the wake of the Covid-19 crisis. Bank provisions as a share of NPLs are considered adequate by rating agencies and expected to increase in response to the deterioration of asset quality, which in turn will reduce the sector's profitability. The main banking sector risks stem from credit concentration – including large credit exposures, but they have been declining since their peak over a decade ago –and the increased exposure of banks' activity to Africa.

The soundness of banks reflects a strong regulatory and supervisory framework, although some challenges

remain. The expansion of large Moroccan banks into Africa provides diversification and profit opportunities, but it increases vulnerabilities too, given the riskier operating environment and lower regulatory standards in some of the countries where Moroccan banks operate (IMF, 2020a). The Central Bank, Bank Al-Maghrib, which supervises and regulates licensed banks in Morocco, enjoys the necessary independence and has built up the required expertise to supervise the banking sector. Basel II standards were adopted in 2007 and Basel III standards, which began to be introduced in 2014, were due for full implementation by end-2020. IFRS 9 was introduced in January 2018. The authorities have also made efforts to address some weaknesses in Morocco's AML/CFT framework (IMF, 2020a). To account for increased risks stemming from cross-border exposure of Moroccan banks, Bank Al-Maghrib has increased its coordination with several sub-Saharan regulatory and supervisory agencies.

Table 3.1: Financial soundness indicators of the banking system in 2019 (percent)

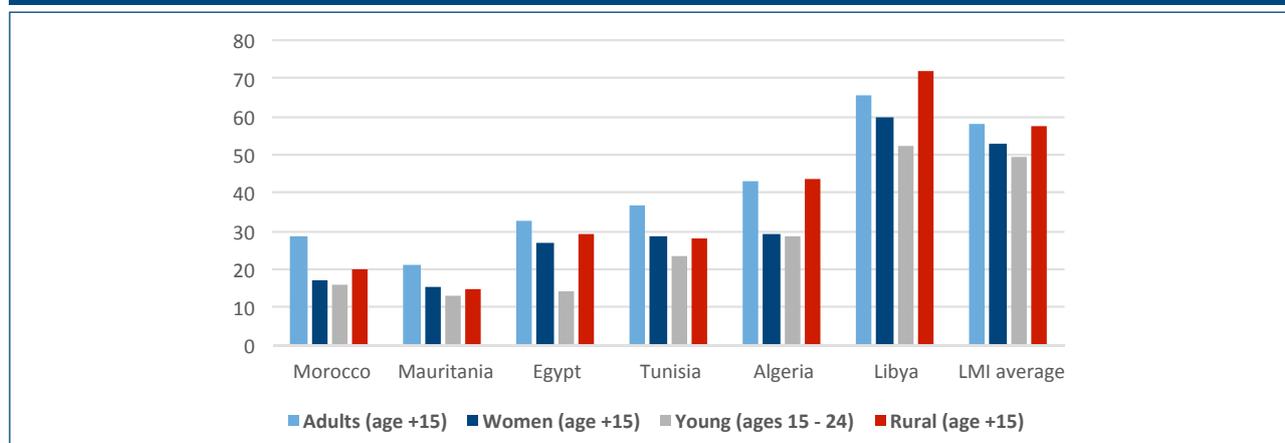
	Morocco	Egypt	Mauritania	Tunisia
Capital adequacy ratio	15.6	17.7	25.3	12.4
NPLs / total loans	7.5	4.2	21.5	13.9
Specific provisions to NPLs	69.3	97.6	76.1	55.1
Return on assets (ROA)	0.9	1.8	0.7*	1.2
Return on equity (ROE)	9.4	23.4	5.1*	13.5**

Source: IMF Country Reports No. 21/2 (Morocco), No. 21/7 (Egypt), No. 20/140 (Mauritania), No. 20/103 (Tunisia). Note: * ROA and ROE in Mauritania refers to 2015. ** ROE in Tunisia refers to 2018. No recent data available for Algeria or Libya. The latest IMF Country Report on Algeria was published in June 2018 and only includes (provisional) data up to 2017. The latest IMF Country Report on Libya was published in May 2013.

3.2 Financial inclusion of households

Despite the rapid progress over the past decades, financial inclusion in Morocco remains low and large segments of the population have limited access to financial services. Women, young adults and people living in rural areas are disproportionately affected and find it more difficult to access

finance. This is reflected in the relatively low share of adults with an account at a financial institution in Morocco. For example, only 17 percent of women, 16 percent of young adults (ages 15 to 24) and 20 percent of people living in rural areas have an account, compared to 29 percent for the adult population (Figure 3.3). In North Africa, only Mauritania performs worse in terms of account ownership.

Figure 3.3: Account ownership in 2017 (percent)

Source: Global Findex Database. Note: LMI average: Average of lower middle-income economies.

The large informal economy and lack of credit information contribute to the low level of financial inclusion. 90 percent of payments in Morocco are in cash compared to 40 percent worldwide (IMF, 2019). For example, utility bills are mostly paid in cash. With 25 bank branches and 29 ATMs per 100,000 adults in 2019 according to IMF Financial Access Survey (FAS) data, bank density and penetration are relatively developed compared to other North African countries or lower middle income economies, but they remain significantly lower in rural areas than urban areas. About one third of remittances is received or payed in cash – unlike in many other economies at a similar level of development, where most remittances are transferred through the banking system¹⁰.

Fostering digitalisation should also help to promote financial inclusion. Access and use of digital payment platforms remain very limited in Morocco. Only 17 percent of Moroccans have either received or made a digital payment during the course of a year, which corresponds to 58 percent of those who have an account. Only 2 percent of the population uses Internet to make payments or buy products and services online. Payments and transfers from the Government to the Moroccan people are also limited. Morocco performs worse than most countries in North Africa in what could be an important leverage for

financial inclusion. The National Financial Inclusion Strategy and the adoption of a new legal framework for crowdfunding and mobile payments will help foster financial inclusion.

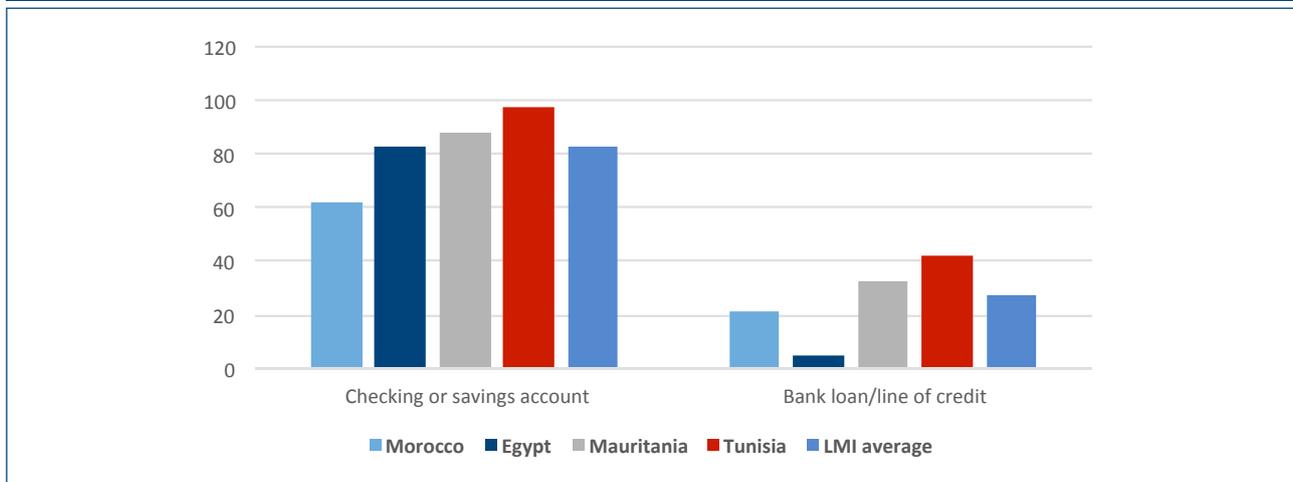
3.3 Access to bank finance by non-financial firms

Despite the size of the banking system in the economy, a significant share of firms do not have access to bank finance. Only 62 percent of firms in the formal sector have a checking or savings account, which is lower than in other North African countries or the average of lower middle income economies, according to the latest wave of the Enterprise Survey, carried out jointly by the EBRD, the EIB and the World Bank Group (Figure 3.4)¹¹. Firm size is strongly associated with having a bank account. In Morocco, only 58 percent of small firms (5 to 19 employees) have a checking or savings account, compared to 66 percent of medium-sized (20 to 99 employees) and 82 percent of large firms (100+ employees). This indicates that a large share of Moroccan companies, especially smaller ones, are excluded from bank finance. The lack of proper accounting systems and the relatively poor coverage of credit bureaus create additional barriers to access to finance for Moroccan firms (IMF, 2019).

¹⁰ Morocco received more than USD 7 billion remittances in 2018, making it one of the largest recipients of remittances in Africa (after Egypt and Nigeria). The major sending countries include France, Spain and Italy (EIB, 2020).

¹¹ Enterprise Surveys are firm-level surveys of a representative sample of an economy's private sector. The surveys cover a broad range of business environment topics including access to finance, infrastructure, competition, and performance measures. The Enterprise Survey is answered by business owners and top managers. Formal (registered) companies with 5 or more employees are targeted for interview. Firms with 100 percent government/state ownership are not eligible to participate. The sampling methodology is stratified random sampling. The strata are firm size, business sector, and geographic region within a country. Sector breakdown is manufacturing, retail, and other services. In Morocco, 1,096 enterprises were interviewed between May 2019 to January 2020. For more details about the methodology of Enterprise Surveys and the questionnaires, see: <https://www.enterprisesurveys.org/en/methodology>.

Figure 3.4: Firms with a checking or savings account, and a line of credit or bank loan (percent)



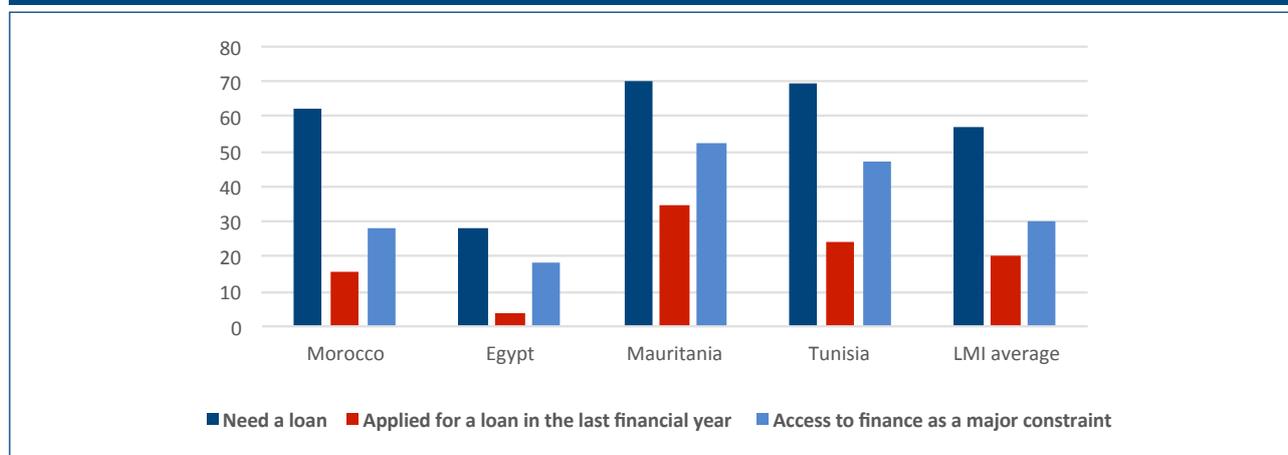
Source: EBRD-EIB-World Bank Enterprise Surveys. Note: No data available for Algeria or Libya. LMI average: Average of lower middle-income economies. The survey year is 2019 for Morocco, 2020 for Egypt and Tunisia, and 2014 for Mauritania.

Most firms do not rely on bank credit to finance investment and prefer to rely on internal finance. Only 21 percent of Moroccan firms have a bank loan or a line of credit outstanding, which is lower than in Tunisia, Mauritania or the average of lower middle economies – but this remains significantly higher than in Egypt. In Morocco, 19 percent of small firms have a bank loan or a line of credit outstanding, compared to 23 percent of medium-sized firms and 39 percent of large firms. Internal funds represent 62.5 percent of investment finance for small firms, compared to 40 percent for medium-sized firms and 49 percent of large firms¹². The guarantee programmes implemented in recent years have allowed to extend access to external finance for smaller enterprises. However, only 6 percent of micro-enterprises have access to bank financing, and microcredit represents only 0.6 percent of GDP (IMF, 2019). This suggests a relatively high degree of credit concentration towards large enterprises, including state-owned enterprises.

Most firms would like to receive bank finance. About 62 percent of Moroccan firms reported the need for a loan in 2019¹³. Moroccan enterprises often suffer from long client payment delays, which increase their need for working capital financing and threaten bankruptcy in extreme cases, especially for smaller firms. However, only 15 percent of companies actually applied for a loan in the previous financial year (Figure 3.5). The gap between the share of firms that need a loan and those that applied for a loan is larger in Morocco than in other North African countries or the average of lower middle-income economies. About 28 percent of Moroccan companies report access to finance as a major constraint to their operations, which is slightly higher than in Egypt and other lower middle-income economies – but this remains significantly below Mauritania and Tunisia.

¹² These figures on bank finance and internal funds to finance investment from the EBRD-EIB-World Bank Enterprise Surveys are similar to those of a national firm-level survey conducted by the Haut Commissariat au Plan (HCP) in 2019.

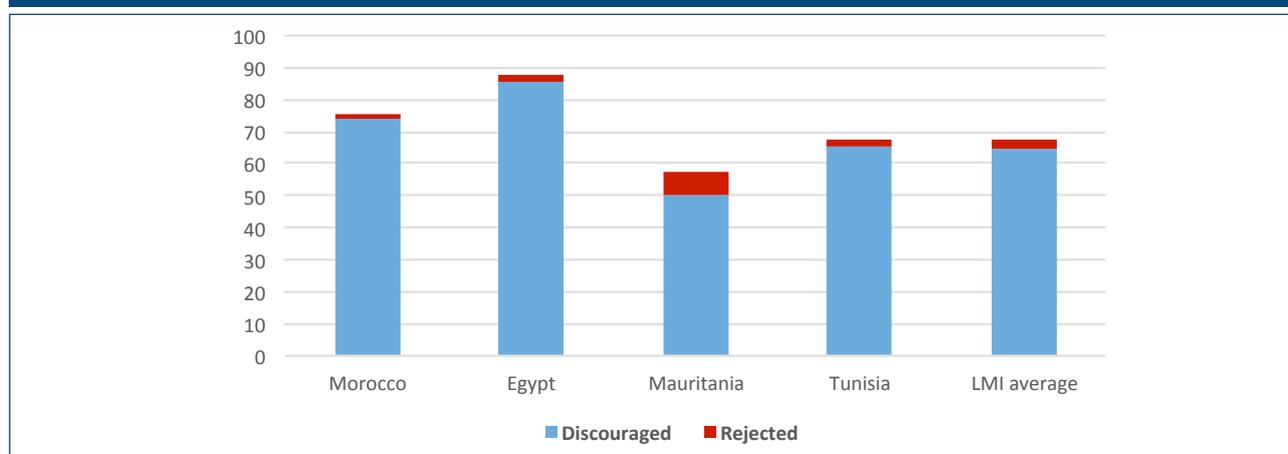
¹³ Some firms do not need to apply for bank finance because they have sufficient capital and can finance working capital or investment using other sources of finance, such as internal funds or retained earnings, purchases on credit from suppliers and advances from customers, or by issuing new equity shares.

Figure 3.5: Firms that need a loan, applied for a loan, and report access to finance as a constraint (percent)

Source: EBRD-EIB-World Bank Enterprise Surveys. Note: No data available for Algeria or Libya. LMI average: Average of lower middle-income economies. The survey year is 2019 for Morocco, 2020 for Egypt and Tunisia, and 2014 for Mauritania.

Many Moroccan firms are discouraged from applying for loans. Firms are considered “credit constrained” when they either (i) applied for a loan but the application was rejected, or (ii) did not apply because they were discouraged. Among the firms reporting the need for a loan, the share of credit constrained firms is 75 percent in Morocco, which is higher than Mauritania, Tunisia or the average of lower middle income economies – but below Egypt, where this share reaches 81 percent (Figure 3.6). In Morocco, the main

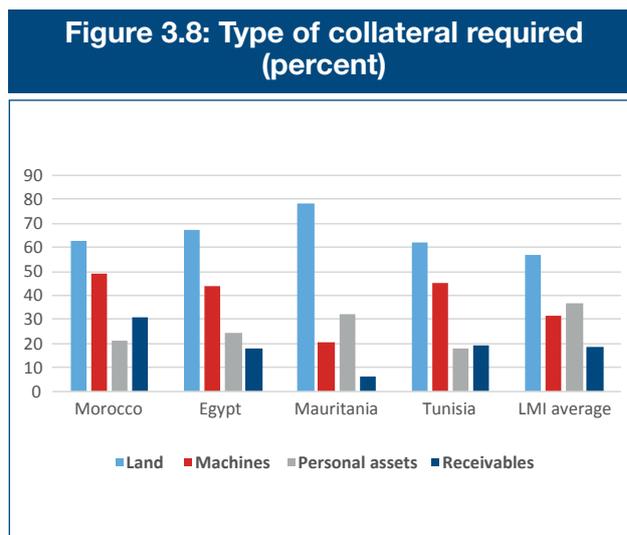
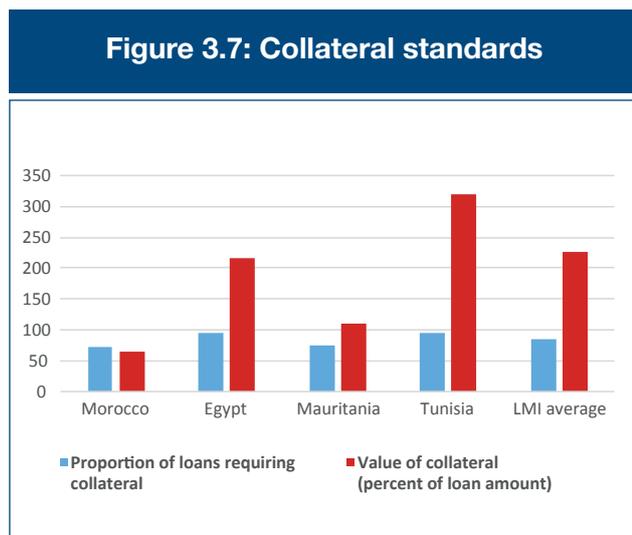
reasons why firms report to be discouraged from applying include procedures that are too complex (26 percent of the firms) and terms and conditions (such as interest rate or maturity of the loan) that are unfavourable (25 percent), while only 11 percent of the firms consider that high collateral requirements is the main reason. Discouraged firms tend to invest and expand less than firms applying for bank loans and hence miss out on growth and job creation opportunities (EBRD, EIB and WB, 2016).

Figure 3.6: Firms that are credit constrained (either discouraged or rejected, percent)

Source: EBRD-EIB-World Bank Enterprise Surveys. Note: No data available for Algeria or Libya. LMI average: Average of lower middle income economies. The survey year is 2019 for Morocco, 2020 for Egypt and Tunisia, and 2014 for Mauritania.

Collateral requirements are less stringent in Morocco than in other North African countries. About 72 percent of bank loans in Morocco require a collateral and the collateral amounts to 63 percent of the loan size on average, which is significantly lower than in other countries in North Africa or the

average of lower-middle income economies (Figure 3.7). Higher collateral ratios are often required by banks to compensate for costly and long processes to foreclose collateral, while a high overall collateral incidence reflects systems based on relatively prudent and conservative lending practices.



Source: EBRD-EIB-World Bank Enterprise Surveys. Note: More than one type of collateral can be required to the firm for a loan by the financial institution. "Land": land and buildings under ownership of the firm; "Machines": machinery and equipment including movables; "Personal assets": personal assets of owner (house, etc.); "Receivable": accounts receivable and inventories. No data available for Algeria or Libya. LMI average: Average of lower middle income economies. The survey year is 2019 for Morocco, 2016 for Egypt, 2014 for Mauritania, and 2013 for Tunisia.

Banks often show reluctance to accept movable assets of the firm as collateral and prefer to request land and buildings or personal assets of the firm's owner instead. In North Africa, movable assets are often used as secondary collateral, in addition to real estate. In Morocco, about 63 percent of loans require land or buildings, which is lower than Egypt and Mauritania but remains slightly higher than Tunisia and the average of lower middle income economies (Figure 3.8). In Morocco, less than half of the loans used machinery and equipment (49 percent) or accounts receivable and inventories (31 percent) as collateral. Smaller firms are much more often requested to pledge personal assets of the owner. A collateral regime that allows for movable assets – such as machinery and equipment, receivable and inventories – tends to facilitate access to finance because the vast majority of assets of most firms are movable (Alvarez de la Campa, 2011). Recent legal reforms in Morocco, including the law on collateral, are expected to further improve the current framework

for collateral and allow smaller enterprises to access bank credit to finance investment (see section 3.6).

3.4 The role of non-bank financial institutions

Even though banks are the main source of external finance for SMEs, the role of non-bank financial institutions in Morocco is growing, especially for small companies where they represent an increasing source of funds. The microfinance sector has experienced steady growth since 2013, targeting microenterprises and low-income clients. Microfinance institutions (MFIs) have an outstanding portfolio of MAD 8.1 billion in 2019 (representing 0.7 percent of GDP) and over 900,000 clients, of which about half are women. The microfinance sector is highly concentrated, with the three largest MFIs accounting for 92 percent of market share (and the five largest MFIs 98 percent of market share). Supervised

by Bank Al-Maghrib, the microfinance sector is stable, with a portfolio-at-risk share of 3 percent for the entire sector.

Legal reforms to increase the maximum lending size have supported the microfinance sector, allowing MFIs to also serve small businesses. The revised regulatory framework will also enhance governance standards and allow MFIs to strengthen and diversify their funding structure. Other reforms aiming at creating the legal form of microfinance banks are under study and could further spur microfinance growth.

The development of participative (Islamic) finance also contributes to financial inclusion by partly reaching out to those that remain outside the financial sector due to religious preferences. The regulation of Islamic financing was introduced in 2015, paving the way to five Islamic bank licenses and the development of Islamic finance products that are expected to grow. Lending by participative banks reached more than USD 1 billion in 2019, up to USD 500 million in 2018, and represent more than 10 percent of loans provided by the banking sector.

The leasing sector has developed against the backdrop of a sound legal and regulatory framework. There are seven main players, all of them subsidiaries of banks. Maroc Leasing, WafaBail (Attijarawafa group) and Maghrebail represent a combined market share of 70 percent. Leasing assets stood at MAD 49.7 billion in 2018, with SMEs representing two thirds of the clients. Leasing is particularly valuable for small businesses without track-record, collateral or other requirements to access traditional bank lending.

Morocco is one of the largest markets in the region for equity finance. With a stock market capitalisation of USD 65 billion in 2019 (55 percent of GDP), the Casablanca Stock Exchange (CSE) is the second largest exchange in Africa by market capitalisation after the Johannesburg Stock Exchange (USD 1,056 billion, or 300 percent of GDP). Morocco is also one of the most active markets for private equity in Africa – after South Africa, Nigeria and Kenya¹⁴. The CSE is highly concentrated – with the ten largest companies accounting for around three-quarters of total market capitalisation – and

does not yet constitute a good alternative for SME finance. The CSE has introduced reforms to encourage SMEs access to the stock market, including a “third window” for firms raising limited volumes. Reforms introduced in 2019 foresee the creation of an alternative exchange dedicated to SMEs, relaxing reporting requirements for smaller and more innovative companies to gradually develop this market¹⁵. The reinforcement of finance for SMEs and start-ups is one of the priorities of the Comité du Marché des Capitaux (CMC). A number of public initiatives focusing on SMEs have also established public-private equity funds in the last decade, targeting specific industries such as agriculture and green energy and more recently venture capital funds to support start-ups. A new crowdfunding law (August 2019) is also opening up new potential venues for alternative SME finance.

3.5 Public sector initiatives to promote financial inclusion

The Moroccan government’s new vision for economic growth and social inclusion requires an inclusive and diversified financial sector. Over the last few years, Morocco has implemented financial sector reforms that contribute to financial inclusion. Two sector-level strategies, the National Financial Inclusion Strategy and the National Strategy for Digital Development (Plan Maroc Numérique), set out the policy priorities and action roadmaps in these areas.

The secured transactions framework has been strengthened with new bankruptcy and collateral regimes approved in April 2018. This is expected to facilitate the use, registration and enforcement of collateral rights. This is a long pending reform area, as Morocco remains below other countries in North Africa, such as Egypt and Tunisia, in the getting credit rank and the sub-indicator “strength of legal rights” of the World Bank’s Doing Business 2020 (Table 3.2). A new law on security over movable assets (April 2019), is expected to help overcome fragmentation of rules in relation to types of assets and complexity of the enforcement process of security interests. It also established an electronic movable collateral registry, administered by the Ministry of Economy and Finance, increasing security and transparency.

¹⁴ According to EMPEA data on the number of private equity deals over the past decade.

¹⁵ SMEs with a balance sheet not exceeding MAD 200 million, and a turnover not exceeding MAD 500 million.

Table 3.2: Doing Business 2020 getting credit rank

	Getting credit rank	Strength of legal rights index (0-12)	Depth of credit information index (0-8)
Morocco	119	2	7
Algeria	181	2	0
Egypt	67	5	8
Libya	186	0	0
Mauritania	132	2	6
Tunisia	104	3	7

Source: World Bank Group Doing Business 2020. Note: A lower ranking (out of 189 countries) in the getting credit rank mean a better performance. A higher value in the strength of legal right index (0-12) and the depth of credit information index (0-8) means a better performance.

The credit reporting system allows access to increased financial information on existing and potential borrowers.

Since 2009, Morocco has both a public credit registry and a private credit bureau. The market for private credit bureaus was liberalised in 2016, leading to the creation of a second bureau and increasing competition in the provision of information services and population coverage. The credit bureaus collect positive and negative information on individual and corporate borrowers of entities supervised by Bank Al-Maghrib. They help SMEs build a track record and leverage this reputation to access finance. New services have been introduced, such as SME credit scoring and portfolio surveillance, as well as the use of alternative data based on utility bill payment information (especially useful for those segments of the population with more limited banking records). Credit bureau coverage increased to 31.6 percent of adults in 2019, up from 24.6 percent in 2016, which is the higher percentage in the region.

The new 2015 Banking law increased competition between banks and non-banks and fostered innovation by allowing a new type of financial intermediary specialised in the issuance of electronic money and able to offer payment services. Since 2015, Bank Al-Maghrib has authorised 11 payment companies, including three telephone operators, and has regulated the introduction of an “m-wallet” and interoperability between banks and payment providers. These reforms can have an important impact on the unbanked population, who will be able to make payments and receive pensions and transfers. The demand of electronic payments, however, may be constrained by a traditional preference for

cash, partly reflecting the large informal sector in the economy. Increasing incentives to promote the use of digital payments, raising the awareness on the benefits of mobile payments, and supporting digital literacy and security are measures that will increase the regular use of mobile payments and foster financial inclusion.

Accelerating the use of digital financial services is a key component of the *Plan Maroc Numérique*, a national strategy to support digital transformation, which targets also e-government services and private sector digitalisation. Recent ICT surveys show that addressing digital divide in infrastructure coverage between urban and rural areas, and a gender gap in access and use of technology, will help to facilitate economic and social inclusion (see Box 4.1 discussing mobile payments as means to develop rural areas). Morocco scores lower in financial education tests than other countries with lower literacy rate, including Zambia, Mozambique and Senegal.

To lead and coordinate the diverse set of financial inclusion activities in Morocco, Bank Al-Maghrib and the Ministry of Economy and Finance launched in 2019 the National Financial Inclusion Strategy. The strategy builds on the recent efforts described in the sections above, aiming to expand financial services to SMEs and excluded populations, by: (i) expanding mobile payments; (ii) boosting micro finance through increased credit ceilings and removal of interest rate caps; (iii) supporting inclusive insurance; (iv) encouraging bank penetration, including through postal agencies and more flexible regulatory requirements for underserved

segments (e.g. in rural areas); (v) facilitating innovative financing tools, supporting the development of new credit scoring systems (e.g. big data analytics based on utility bill payments); (vi) implementing digital payments by the government to public employees and in public procurement contracts; (vii) and promoting financial literacy.

Together with regulatory reforms, government funded initiatives with dedicated loans, public guarantee schemes and technical assistance to SMEs have been used as countercyclical tools during crises and as means to support the development of certain segments (innovation, exports, targeted industries, start-ups, etc).

The key institution implementing these initiatives is the Caisse Centrale de Garanties (CCG), a public financial institution, supervised by Bank Al-Maghrib. With an overall outstanding portfolio of EUR 6.1 billion at the end of 2019, CCG has a number of products (debt, equity, guarantees and technical assistance) to cater to companies' financial needs according to their size and life cycle, with a particular focus on very small and small companies. In response to the Covid-19 crisis, CCG has rapidly increased the size of its portfolio and the number of firms that are supported by their programmes. Through the different guarantee programmes implemented by the CCG during the crisis and to relaunch the economy (notably under the facilities Damane Oxygene and Damane Relance), Moroccan banks provided loans worth close to 5 percent of GDP to more than 75,000 enterprises (as of end-February 2021). The CCG also launched three new facilities to provide financing to very small firms, real estate firms and to firms operating in the tourism sector.

3.6 Long-term challenges

Despite Morocco's large banking sector, the availability of external finance remains a constraint for many firms, especially small ones. Financial intermediation in Morocco is held back by the relatively high concentration of bank lending to few large corporates, stringent collateral requirements, and the limited availability of credit information,

which discourage firms, particularly the small ones, from requesting bank finance. Even though the role of non-bank financial sector in Morocco is growing, its small size limits the choice of financial instruments for smaller firms.

The Covid-19 crisis has exacerbated the difficulties to access finance for firms. 72% of Morocco firms experiencing decreased liquidity or cash flow availability, according to the Enterprise Surveys follow-up on Covid-19¹⁶. Similarly, 62 percent of firms reported to delay payments to suppliers, landlords, or tax authorities. Unsurprisingly, smaller firms are more likely to be affected, reflecting the liquidity or solvency crisis induced by the pandemic.

Banks have been relatively resilient amid the Covid-19 pandemic, helped by relatively sound initial liquidity positions as well as the strong support response by the Central Bank and public guarantee programmes. Credit has continued to increase in 2020, reflecting both the strong response of the Central Bank, which has improved liquidity conditions and cut interest rates, and the government's guaranteed credit schemes (IMF, 2021). The Central Bank also encouraged banks to increase provisioning and suspend the distribution of dividends in 2020 to build capital buffers against a potential deterioration of banks' credit portfolio and asset quality. But the portfolio exposure of many banks is skewed toward cyclical sectors, including agriculture, (commercial) real estate, construction, and tourism, which could create vulnerabilities.

Financial inclusion features prominently in the authorities' agenda, as a crucial vehicle for economic and social inclusion. The implementation of the National Financial Inclusion Strategy and the National Strategy for Digital Development (Plan Maroc Numérique) will be key to relaunch the economy following the outbreak of the Covid-19 pandemic. The reform agenda, initiated in recent years with improvements in financial infrastructure (e.g. collateral requirements and use of credit bureaus), digital financial services and non-banking financial sector, is expected to

¹⁶ Business owners and top managers of the 1,096 Moroccan firms interviewed for Enterprise Surveys between May 2019 and January 2020 were re-interviewed in July and August 2020.

continue. These measures aim to support access to credit and other financial services, but also, and in particular, to close the gaps in access and use identified for specific segments of the market, such as women, young people or those living in rural areas.

To fast-track financial inclusion, digitalisation and financial literacy emerge as key priorities for financial institutions and their clients. The outbreak of the

Covid-19 pandemic has exacerbated the need to urgently address financial inclusion gaps. Digitalisation will not only expand access to financial services for customers, but it will also be critical to enhance the internal processes of banks and other financial institutions, e.g. with the development of new models for credit risk and marketing to approach new markets and smaller enterprises, which should help better channel funding where it is most needed.



4. Integrating the Rural Areas into the Development Model

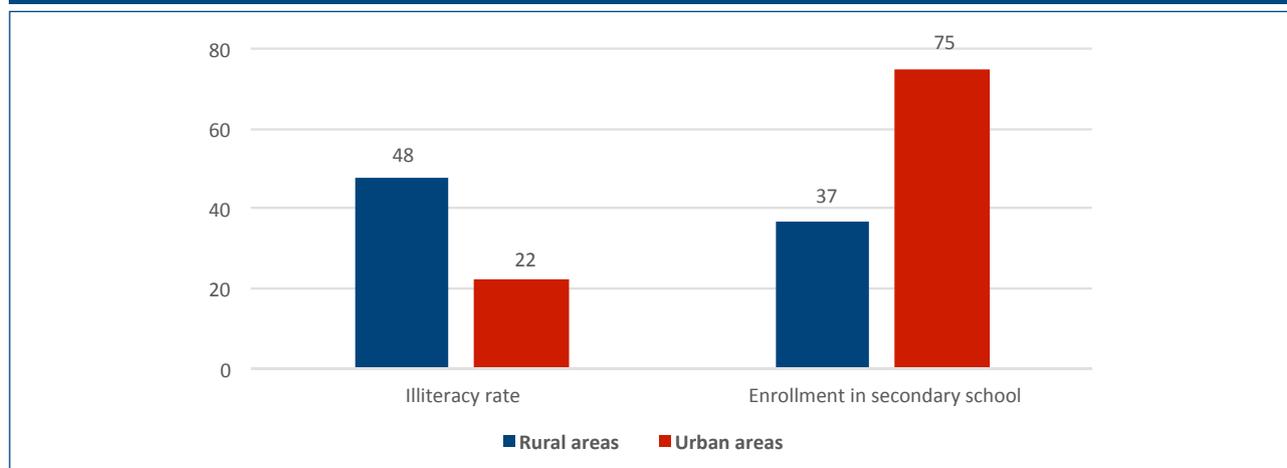
Morocco's rural areas are home to 40 percent of the population but generate only 25 percent of GDP. The rural private sector is hampered by an uneducated workforce with limited entry points for women and youth. Rural economic activity is focused on an underperforming agricultural sector that is particularly exposed to droughts, such as the one in 2020. Beyond agricultural activities, private entrepreneurship remains limited in scope and scale. The government is highly aware of these challenges and has been implementing a number of reforms in recent years focusing on increasing rural connectivity and improving agricultural infrastructure and value added. Despite major efforts, integrating rural areas into Moroccan active urban economy remains a major challenge, and is essential to foster inclusion and to further develop the private sector in the overall economy.

4.1 Better education and agriculture: crucial factors of success for the Moroccan economy

Morocco rural areas are less developed than urban areas due to a low-skilled workforce. The illiteracy rate in rural areas is twice as high as in urban areas (Figure 4.1). The gap is even

larger in terms of gender, with 60 percent of illiterate women in rural areas (31 percent in urban ones) and 35 percent of men (14 percent in urban areas). Rural areas are also among the poorest in the country. As of 2014, 40 percent of Morocco's population lived in rural areas, but they accounted for 79 percent of the overall number of poor people (World Bank, 2018).

Figure 4.1: Level of literacy and secondary education in rural areas and urban areas (percent)



Source: Haut Commissariat au Plan, 2017.

Fostering inclusion of women, youth and low-skilled people is necessary to insure rural development.

While young people represented 34 percent of the overall population in 2018 in Morocco, they face inequalities in terms of gender and place of residence, especially in rural areas (CESE, 2018). In terms of gender, in 2015 most businesswomen came from urban areas (with 73 percent of them coming from the districts of Casablanca and Rabat), while female entrepreneurs are underrepresented in rural areas (AFEM, 2015). Similarly, in 2017, women represented 93 percent of agricultural activities, 40 percent of the agricultural workforce, but only 7 percent of farm managers (AgriMaroc, 2017). In order to foster women's participation in rural areas, *Plan Maroc Vert* called for the development of women agricultural organisations, with positive results (in 2017, 1,779 women cooperatives had been established, gathering more than 32,000 women), as well as the opening of existing organisations to women (in particular made it compulsory to open cooperatives to women in order to obtain project funding).

The rural workforce, and most of the economic activity in rural areas, is concentrated in the agricultural sector.

Economic activity relies mostly on agriculture; the income of 80 percent of the rural population depends on it (Olivié and Pérez, 2018), and 69.4 percent of rural active population was working directly in this sector in 2019. This labour intensity in agriculture reflects lagging modernisation of the sector, with still very small farms (70 percent of farms are smaller than 5 hectares) and limited quality of the soil (*Plan Maroc Vert* assessed that Morocco's mechanisation was eleven times less than Spain).

Agriculture is very much focused on water-intensive crops, especially cereal – with more than 90 percent of water demand coming from agriculture irrigation in 2010 (FAO, 2015). Agriculture is also mostly rain-fed, and poor irrigation systems called for deep reforms that are carried out progressively (FAO, 2015). Through *the Plan National d'Economie d'Eau d'Irrigation* (PNEEI), the authorities supported a more sustainable irrigation model since 2010, in order to optimise water use and increase productivity in irrigated agriculture. If an improved water service is essential, it has to be associated with the use of drought tolerant crops, or at least low-consuming crops, which would enable the agricultural sector to become more resilient and more

productive in reorienting water resources to high-yielding and highly-productive crops (such as market gardening, instead of, e.g., sugar cane).

Beyond agricultural activities, there has been no success so far in developing active private entrepreneurship in rural areas.

Employment in industry and craft in rural areas represented only 4.7 percent of the overall employment in 2019, due to the overrepresentation of the agriculture, forestry and fishing sector (almost 70 percent of employment). SMEs are still underdeveloped in rural areas, as illustrated by the example of the Draa Tafilalet region, the most rural region in Morocco. This region represented less than 3 percent of the overall number of SMEs in 2019, while the Casablanca-Settat region hosted almost 39 percent of Moroccan SMEs (Haut Commissariat au Plan, 2019). In 2014–15, the government and the Moroccan Company for Tourist Engineering (SMIT) settled thematic tourism corridors, and in 2018, a joint report between OECD and Morocco's Minister of Tourism called for the creation of 'tourism clusters' (OECD, 2018). Tourism in rural areas would foster private sector development and facilitate the access of rural producers to local markets, helping them to sell their products. However, these attempts failed to produce tangible results, and the growth of a full ecosystem of SMEs around rural tourism did not happen.

4.2 Rural connectivity and infrastructure

Since the 1990s, the Moroccan government has redoubled its efforts to improve rural connectivity.

Two plans for 'Rural Roads' were launched, between 1995–2005 and 2005–2015 (PNRR 1 & 2), to foster rural access and unlock the potential of these areas. This campaign raised rural accessibility to 80 percent (up from only 54 percent in 2005), and aimed at facilitating access to social services for rural population, guarantee economic exchanges, promote rural resources and activities, and more broadly, increase production while reducing costs with better infrastructure. These efforts to scale up rural development were also directed towards water supply access, which increased from 14 percent to 96 percent between 1994 and 2016, thanks to the Rural Water Supply Programme (PAGER programme), which received the United Nations Public Service Award in 2004. These efforts were also directed towards inclusion and education enrolment (with women and children freed from the task of carrying water).

Another focus of governmental policies was electrification.

With the implementation of the Global Programme on Rural Electrification (PERG), the electrification rate increased from 18 percent to 99.47 percent between 1995 and 2017, combining the dual approach of a network connection for villages whenever possible and solar kits for the most remote areas and scattered households. Meanwhile, access to basic public utilities surged during the last two decades, offering opportunities for the development of rural areas.

Limited digitalisation hampers rural connectivity and constitutes a real hurdle to integration.

In 2017, only 33 percent of households owned a computer in rural areas, compared to 71 percent in urban areas. 47 percent of rural

households had internet in 2015, compared to 76 percent in urban zones. This situation leads to a dual exclusion of people living in rural areas, from the rest of Moroccan society and from the industrial and commercial side of Moroccan agricultural. There is an issue of digital illiteracy, with smartphones being used mainly for social networking and communication, forgoing the potential of increased economic participation, access to public sector services or use of online financial instruments. Moreover, the capability of agricultural digital applications could be used to foster rural development, agricultural productivity (both and the pre-cultivation and post-harvest stages), as well as mobile payment or access to online financial services to develop investments (see Box 4.1).

Box 4.1: Mobile payments as means to develop rural areas

Mobile banking has been used often in development policies as a tool to integrate rural areas, as it allows for rural populations to access basic financial services (where there are no banking structures). It also facilitates exchanges, trade and transactions through the promotion of e-commerce, but also through a better information of producers: from weather forecasts to prices of raw materials on the stock exchanges, an access to internet can direct agricultural decisions and allow instantaneous transactions.

A number of initiatives have been developed in recent years. Regarding access to finance, the Moroccan Agricultural Credit (CAM) launched an important plan of digitalisation in 2017, with both digital services and digital terminals deployed in rural areas lacking proper infrastructures and digitalised banking.

The Support and Financing for Enterprises Programme launched in January 2020 by the Moroccan government targeted specifically rural and semi-rural areas, with a convention agreed between the CAM and Al Barid Bank. It led to specific commitment in terms of loans, especially with the facility “5 years/5 jobs”, which aimed to support young entrepreneurs in creating their SMEs, with the objective of creating at least five jobs after 5 years of support.

Beyond digitalisation, building an integrated infrastructure remains a challenge in the rural areas of Morocco.

Developing freight inter-modality is an example of what could be done to develop trade at all levels, as well as Morocco’s regional integration with the rest of Africa. However, between 2012 and 2016, rail freight transport decreased by 40 percent in Morocco, to less than 25 million tons (Rensma and Hamoumi, 2018). This decrease concerned also non-phosphate freight, with cereal representing only 6 percent of overall transported goods by train. In 2018, this figure increased thinly to

27 million tons. Train freight for agricultural products remains modest, since only the biggest producers benefit from the “logistic plan for cereal” organised by ONCF, the company. Two kind of solutions could be developed. First, there is a need for agricultural hubs to work in coordination with producers associations, established among all Morocco. Second, there is a need for piggybacking transports, articulating both inland freight, by trucks, and train freight, in order to ensure route optimisation and rationalise the logistics sector.

4.3 Increasing the value added of the agricultural sector: *Plan Maroc Vert* and beyond

The government has made strong efforts in recent years to increase the value added of agriculture. *Plan Maroc Vert*, between 2008 and 2020, aimed to double the agricultural value added, and create 1.5 million jobs. New ambitions carried by the government are expected to support the development of geographic denomination, and thus foster local products sales on the markets. *Plan Maroc Vert* focused on local products, with the launch of regional studies identifying local products (such as olive oil, argane oil, dates, clementines, or saffron) and their value chains and promoting specific development plans since 2010. The Agriculture Development Agency (ADA) launched a certification for Morocco's local products (*Terroir du Maroc*), and developed local product bonuses to foster productivity. The 2019 fiscal budget aimed to cover packaging costs for small producers, support 100 producer groups, and support cooperatives in terms of marketing and participation in trade fairs.

***Plan Maroc Vert* has achieved positive results.** Between 2008 and 2018, the agricultural sector was able to attract an investment of MAD 104 billion, of which 40 percent was public investment and 60 percent private investment. All of these investments have improved the performance of the agricultural sector both economically and socially. On the economic front, agricultural GDP experienced an annual increase of 5.3 percent against 3.8 percent for other sectors, thus creating additional added value of MAD 47 billion. On the social level, *Plan Maroc Vert* has allowed the creation of 342,000 additional jobs, and the increase in the number of working days per year and per worker from 110 days / year to 140 days / year following the extension of cultivated areas, crop diversification, and production improvement.

However, *Plan Maroc Vert*, has led to limited results so far, especially regarding the development of private sector in rural areas. *Plan Maroc Vert* aimed to establish six agropoles between 2009 and 2015, i.e. agribusiness competitive hubs, attracting investments and creating jobs in the agricultural sector. These integrated zones aimed at bringing together agribusiness actors, logistics, and support activities, in order to develop high-value chains. However, in 2015, only two out of the six planned agropoles were running

(four in 2019, but still in the commercialisation phase), and less than 30 percent of their total surface was occupied by projects in 2016. Agropoles still struggle to develop, and the high costs of the land in these special areas are one of the main barriers for manufacturers to settle there. More generally, *Plan Maroc Vert*'s success to limit the agricultural decline is challenged by different studies. In a study about returns on physical capital, the Higher Planning Commission (HCP, Morocco's statistical agency) highlighted a decline of investments in the agricultural sector, from 3.3 percent in 1999–2007 to 2 percent in 2007–14 (*Haut Commissariat au Plan*, 2016). Capital intensity in the agricultural sector decreased (from 1.5 percent to 0.8 percent), despite the loss of 13,600 jobs in this sector annually (between 1999 and 2014). Agricultural yields increased overall, but investment and jobs dropped significantly. Eventually, a blurred definition of indicators and aims prevented a concrete evaluation, and led academics to consider that *Plan Maroc Vert* did not design indicators to assess changes in farm income based on increased productive capacities, or farmers' increased ability to play an active role in the governance of agricultural value chains" (Saysse, 2015). A new strategy, "Green Generation", covers the period 2020–2030, capitalises on the results of the *Plan Maroc Vert*, and fills the gaps, in particular those related to marketing, access to water and to agricultural land.

Sector associations aimed to improve the integration of rural areas in the development model. These associations, such as Fimasucre (the Moroccan inter-professional sugar federation), Interprolive (the Moroccan inter-professional olive federation) or Interproberries (the Moroccan inter-professional federation of red fruits), were established, gathering all the actors of a specific sector (see Box 4.2). Thus, these sector associations are playing an increasing role to ensure integrated processes, but collaboration between SMEs is still underdeveloped. Only a few of these sector associations are running, and their success relies on the existence and well-functioning of producers' associations. In addition, this approach, as well as *Plan Maroc Vert*, have limits, since most of the instruments in use are applied to a specific agricultural value chain. Since most of small farmers produce different agricultural products, this approach can appear ineffective, and there is a need to make all the stakeholders participate in these sectoral fora.

Box 4.2: The Interproberries model: an integrated berries sector

The red berries sector (strawberries, raspberries and blue berries) is growing in Morocco, especially in the North. 629 farms produce red berries, and among them, 593 (94 percent) produce strawberries, with a growing surface allotted for this type of agriculture. Land surface increased from 3,035 hectares in 2009–10 to 8,400 hectares in 2018–19, a 176-per-cent increase. The sales revenue reached around €350 million in 2019, while production increased by 84 percent, from 107,000 to 197,000 tonnes during the same period (Médias24, 2019). The red berries market is also growing in terms of exports, which increased from 66,332 tonnes in 2010–11 to 115,442 tonnes in 2017–18.

Interproberries (the Moroccan inter-professional federation of red fruits) was created in 2018, following the model of Fimasucre (which was established in 1971). It gathered two federations, the Moroccan association of red berries (AMPFR) and the Moroccan Association of conditioner exporters of red berries (AMCEFR), and aimed to structure, improve and defend this agricultural sector. In the winter of 2019–20, the European demand for raspberries shrunk, affecting particularly the sector of red berries. Prices fell to between MAD 20 and MAD 40 per kilogram, while the producing price was around MAD 50 per kilogram. The Covid-19 crisis deepened this issue, with the rising prices of shipping. The role of Interproberries was to help the sector to find new outlets, such as China or India, in coordination with the Moroccan government; foster domestic consumption; and think collectively to adapt production to demand, by rationalising new planting plans and limiting the cultivated areas for this specific product.

Rural development is also constrained by the limited access to land, a challenge across the country and especially in rural areas. The complexity and legacy of the land tenure regime in Morocco leads to the concentration of landholding, and difficulties for small farmers to understand – and benefit from – this complex bureaucracy. Plan Maroc Vert, which aimed to develop the acquisition of rural lands by privatising huge areas (700,000 hectares), exacerbated the duality in the system, by favouring mainly large landowners. Buying and registering land is difficult due to lengthy and complex procedures, even for foreign firms seeking to invest in the country (IFC, 2019). Taxing vacant land could limit speculation, and encourage a more transparent land market, fostering investments and SMEs ecosystems' development. Simplifying rules and streamlining procedures would also go a long way in promoting formality in agriculture and the economy at large.

Even if the 'official' informal sector is far lower in rural areas, unpaid work in the agricultural sector, especially in the case of women, is common and must be deterred. Dismantling super-numerary and impractical regulatory hurdles and simplifying (and controlling) new rules is essential to develop a sound economy, in rural areas but also, indirectly, in urban ones.

There is an enormous potential in the rural areas of Morocco, but it lies beyond major obstacles to private sector development. Moroccan authorities are largely aware of the challenges ahead in the rural areas of the country and have been actively implementing ambitious policies such as *Plan Maroc Vert* and *Green Generation*. While public initiatives must focus on increasing the inclusiveness of these areas, private sector initiatives focusing on innovative ideas must also be encouraged.



5. Morocco's Trade Integration and Upgrades in Global Value Chains

Over the past 15 years, Morocco has implemented pro-active industrial strategies¹⁷, which generated increasing exports and foreign direct investment (FDI). The country exports mainly to the European Union (EU), whilst trade with the Arab Maghreb Union (AMU) is minimal. Commercial exchanges with sub-Saharan Africa are increasing, rapidly albeit their level remains limited. Morocco's anchoring to Global Value Chain (GVC) is strong, especially in the automotive sector. However, despite the increase in exports the overall domestic added value incorporated into Moroccan exports stood in 2016 at 74.6 percent against 93 percent for OECD countries. The Covid-19 pandemic negatively impacted exports and overall GDP growth. However, it also demonstrated the reactivity of the Moroccan pharmaceutical sector and its export potential in Sub-Saharan Africa, which over time could enhance the country's resilience and competitiveness.

5.1 Moroccan exports and foreign direct investment

Morocco exports mainly to the European Union. The level of trade with sub-Saharan Africa has increased

over the past 20 years, but from a low base Africa are limited at 5.2 percent of total exports (Table 5.1). However, the share of Moroccan exports to sub-Saharan Africa has significantly increased over the past two decades (Figure 5.1).

Table 5.1: Moroccan exports by destination markets in 2018 (percent of total exports of goods)

	EU	AMU	RoW	Sub-Saharan Africa				
				Total SSA	West Africa	East Africa	Central Africa	Central Africa
Share of total exports	61.57	1.67	31.51	5.25	3.32	0.65	0.58	0.70

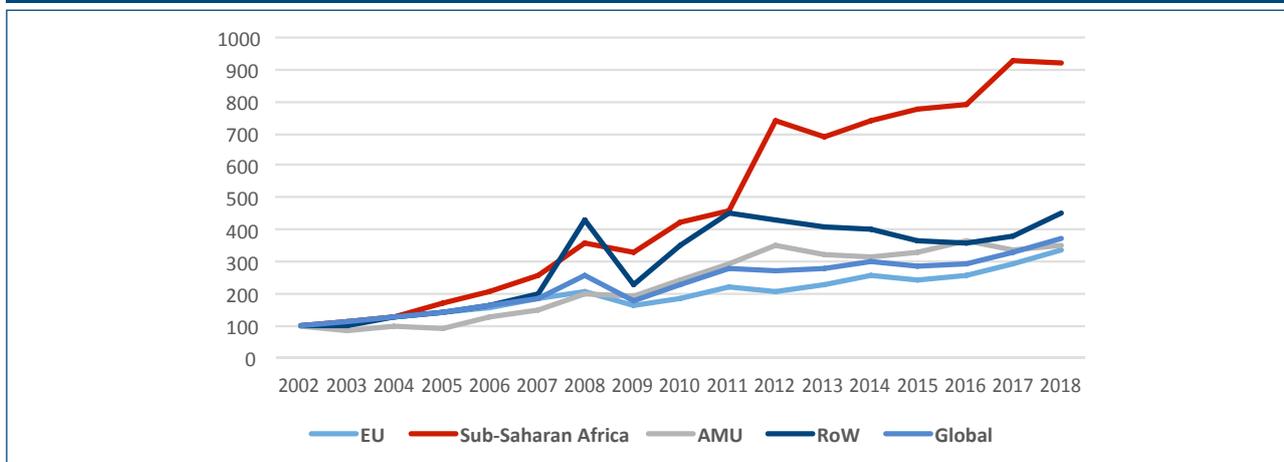
Source: Comtrade Data 2018. Note: EU: European Union; AMU: Arab Maghreb Union; RoW: Rest of the World; SSA: Sub-Saharan Africa.

Between 2002 and 2018, Moroccan total exports have increased by an impressive 275 percent. Despite trade with Africa still modest, the growth of Moroccan exports towards

Sub-Saharan Africa has been the most dynamic between 2002 and 2018, with a growth rate of 818 percent, against 352 percent towards the rest of the World and 235 percent to the EU.

¹⁷ In 2014, Morocco launched the "Industrial Acceleration Plan 2014-2020" (PAI) aiming to create 500,000 jobs by 2020, increase the share of industrial GDP from 14 percent in 2014 to 23 percent in 2020, and strengthen exports.

Figure 5.1: Evolution of Moroccan Exports by Destination Markets (index: 100 in 2002)

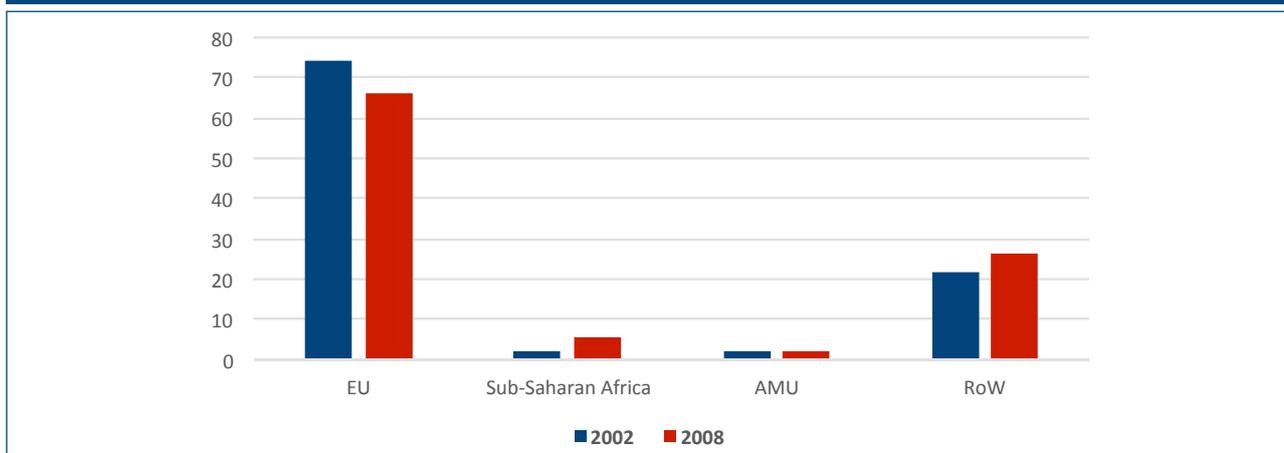


Source: AfDB computations using Comtrade-UNCTAD. Note: EU: European Union; AMU: Arab Maghreb Union; RoW: Rest of the World. RoW is computed by subtracting sub-Sahara Africa, EU and AMU from the total.

The level of Moroccan exports to sub-Saharan Africa was very low in 2002 at 2.3 percent of total exports. The strong growth translated into a substantial increase, yet the overall share of exports Africa remained modest at 5.25 percent in 2018 (Figure 5.2). Regarding other destinations, the general trend is marked by a drop in the share of exports to the EU, which fell from 74 percent in 2002 to just over

61.6 percent in 2018¹⁸. This decrease of exports to the EU (in relative terms) benefited the rest of the World, which currently absorbs 26 percent of Moroccan exports (against 21.7 percent in 2002). The share of exports to the AMU countries, on the other hand, has hardly changed since 2002, still at around 2 percent in 2018 and even slightly trended down¹⁹.

Figure 5.2: Share of Moroccan exports by main destination markets in 2002 and 2018 (percent)



Source: AfDB computations using Comtrade-UNCTAD. Note: EU: European Union; AMU: Arab Maghreb Union; RoW: Rest of the World. RoW is computed by subtracting sub-Sahara Africa, EU and AMU from the total.

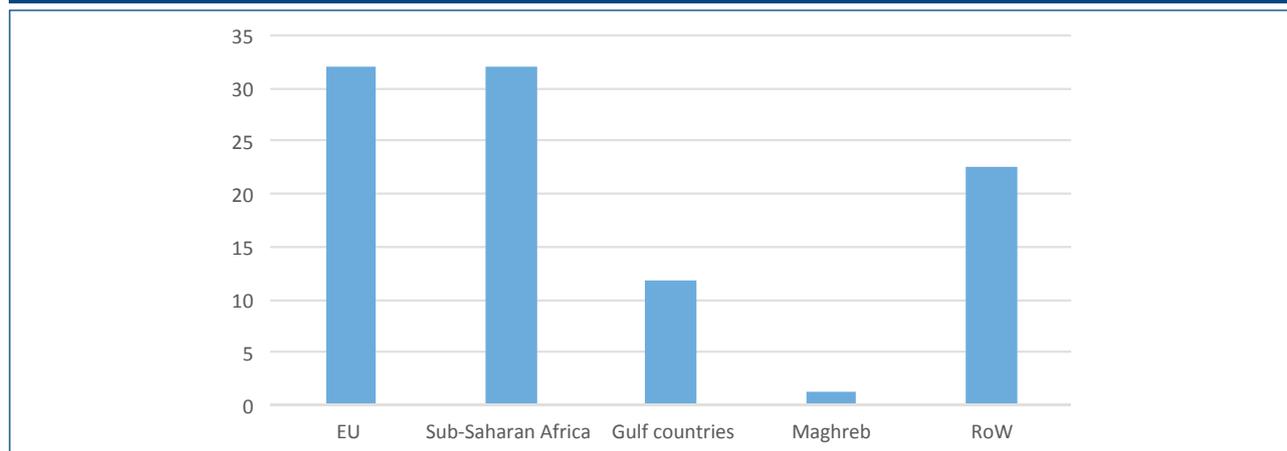
¹⁸ However, total exports to the EU (in volumes) continue to rise (Figure 5.1).

¹⁹ The AMU comprises Algeria, Libya, Mauritania, Morocco, and Tunisia.

Moroccans invest more abroad, hence foreign direct investments have been rising, especially in sub-Saharan Africa. Moroccan foreign direct investment (FDI) has been on the rise over the last two decades, from below 0.20 percent

of GDP in 2000 to 0.66 percent of GDP in 2018. Also, around 32 percent of Moroccan FDI have been invested in sub-Saharan Africa since 2016 confirming a stronger integration of Morocco with the continent (Figure 5.3).

Figure 5.3: Share of Moroccan FDI flow (percent), by destination, average 2016-2018



Source: AfDB computations based on data of the Office des Changes du Royaume du Maroc. Note: EU: European Union; RoW: Rest of the World.

From 2007 to 2018, sub-Saharan Africa received a total of MAD 24.972 billion in investment flows from Morocco (about EUR 2.32 billion). 30.4 percent of investment to sub-Saharan Africa went to Côte d'Ivoire, 21 percent to Mali, 11.4 percent to Senegal, 9.8 percent to Gabon and 7.5 percent to Cameroon²⁰. It is also to those countries that Moroccan exports are the highest. 41 percent of FDI were made in the banking sector, 27 percent in industry, and 19 percent in telecommunications. Nevertheless in 2016, the share of industry reached nearly 53 percent of outflows, with nearly MAD 2.5 billion invested, mainly in Côte d'Ivoire, Benin and Cameroon. The projects include fertilizer production (Gabon, Rwanda, Ethiopia and Nigeria), cement (Côte d'Ivoire, Ghana and Mali), pharmaceutical industry (Côte d'Ivoire, Rwanda), truck assembly (Senegal) and agri-food industry (Guinea, Benin, Cameroon, Côte d'Ivoire, Mauritania or Tanzania).

The expansion of Moroccan banks (as highlighted in Chapter 3) together with significant Moroccan FDI in sub-Saharan Africa indicates deepening integration of

Morocco with the rest of the continent. Looking forward, with the implementation of the African Free Trade Area (AfCFTA), tariffs and non-tariff barriers would diminish, allowing for higher trade integration between Morocco and sub-Saharan Africa.

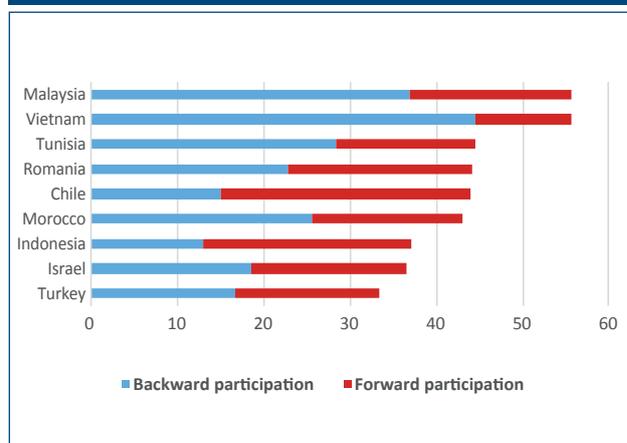
5.2 The rising importance of Global Value Chains

Global value chains (GVCs) account for an estimated 60 to 80 percent of global trade (AfDB/FEMISE, 2019). In developing or emerging countries, firms participating in a GVC increase their probability of exporting. This also translates into productivity progress and better international positioning due to the use of foreign inputs, the obligation to meet certain production and quality standards, the access to new technologies, the possibility of improving employee skills and the access to new information. GVCs can boost growth, create jobs and reduce poverty, provided countries undertake deep structural reforms (World Bank, 2020).

²⁰ The remaining FDIs were received by: Congo (4.3 percent), Nigeria (2.7 percent), Burkina Faso (2.2 percent) as well as Guinea, Togo, Benin, Central Africa (1.4 percent) and seven other African countries (2 percent).

Figure 5.4: Morocco and other Countries GVC Participation Index in 2005-2011 and 2015

Source: OECD- TIVA Database.

Figure 5.5: Morocco and other Countries Backward and Forward Participation in 2015

Source: OECD- TIVA Database.

Morocco's integration in GVCs has increased significantly over the past two decades. One of the most reliable measures for assessing the level of integration is the GVC participation index²¹ which takes into account the content of exports in imported products²² ("backward participation" or "purchased from") and the domestic value added incorporated in the form of intermediate consumption in the gross exports of trading partners ("forward participation" or "sold to").

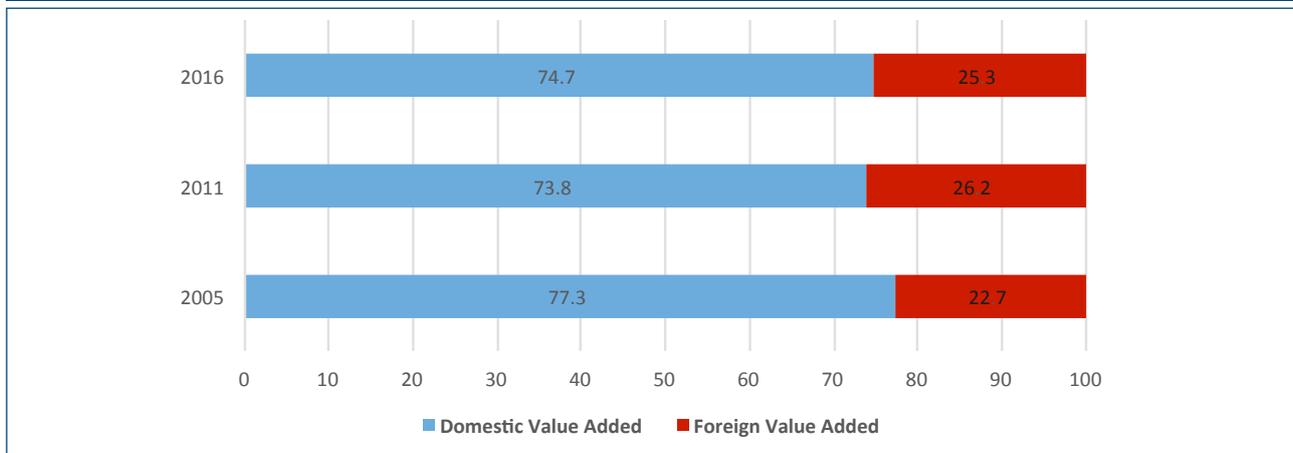
Morocco's participation in GVCs has increased from 39.8 percent of gross exports in 2005 to 43.1 percent in 2015. Figure 5.4 shows the GVC participation index in 2005, 2011

and 2015 in four Mediterranean and five middle-income countries. Although this level is much lower than that of Malaysia and Vietnam, both standing at 55.6 percent, Morocco's participation index is comparable to Tunisia (44.5 percent), Romania (44.2 percent), Chile (44 percent), and above Indonesia (37.1 percent), Israel (36.5 percent) and Turkey (33.4 percent). In 2015, backward participation totaled 25.7 percent in Morocco against 17.5 percent for forward participation (Figure 5.5). The importance of foreign added value in domestic exports is also observed in Tunisia and, more surprisingly, in Malaysia and Vietnam. Only Chile and Indonesia present a forward participation higher than the backward one.

²¹ The participation index presented here is based on the calculation of value-added trade, carried out by the OECD and the WTO (EVA base, Value Added Exchanges, or TIVA, Trade in Value Added). Other databases also provide integration measures in GVCs (GTAP, WIOD, UNCTAD-Eora, IDE-JETRO). However, the TIVA (or EVA) database is one of the most complete. The 2018 edition that covers 64 countries and 36 industry sectors over 2005- 2015, can be accessed at: <https://www.oecd.org/sti/ind/measuring-trade-in-value-added.htm>

²² The most well-known measure of a GVC participation was created by Koopman et al. (2010). This index is based on domestic value added in foreign export (forward participation) and foreign value added in domestic export (backward participation). The upstream participation (backward) of country A is the share of foreign value added included in the gross exports of country A. The downstream participation (forward) of country A is the share of the domestic value added in the exports of its trading partners (in the gross exports of country A). The GVC participation index (expressed as a percentage) is the sum of upstream participation (backward) and downstream participation (forward) divided by the country's gross exports. The value goes from 0 to 100, with 100 representing the highest country's participation in GVC.

Figure 5.6: Share of domestic and foreign value added in Moroccan gross exports (percent)

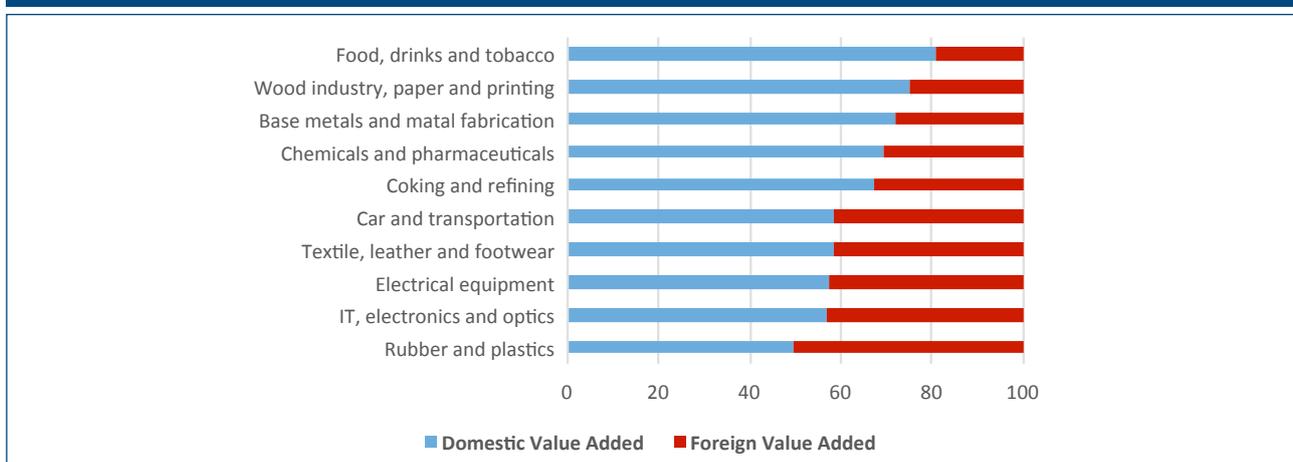


Source: OCDE-TIVA Database.

Concomitant with the increased participation in GVCs, the share of domestic value in Morocco's gross exports declined from 77.3 percent in 2005 to 73.8 percent in 2011 and increased to 74.7 percent in 2016 with important differences across sectors (Figure 5.6). In OECD countries, the average share of domestic value added in gross exports is 93 percent, almost 20 percentage points above that of Morocco. The share the domestic value added in exports of the food products sector and the wood and paper industry sectors are above the Moroccan average, at 80.7 percent and 74.9 percent respectively (Figure 5.7). All other sectors are below the Moroccan average, especially vehicles and

clothing and leather (58.3 percent). The sector of vehicles and other transport equipment as well the sector of textiles, clothing and leather accounts respectively for 16.3 percent and 14.8 percent of total exports. Consequently, increasing the share of domestic value added in these two sectors or rising total exports of food products or of the wood and paper industry, sectors incorporating higher domestic value added could imply higher employment and lower trade deficit. Indeed, being better integrated into the GVCs would increase exports whilst enhancing the share of domestic value added in gross exports, would push Moroccan production capacities, hence create jobs.

Figure 5.7: Domestic and foreign value added of Morocco gross exports in 2016 (percent)



Source: OCDE-TIVA Database.

5.3 A focus on three promising sectors: health, automotive and aeronautics

The medical and pharmaceutical sector, the automotive and the aeronautic sectors offer important opportunities of integrating GVCs. The sectors of renewable energy and digital economy are also promising.

Medical and pharmaceutical sector and the health ecosystem

The Moroccan medical and pharmaceutical sector is a well-structured, organised and innovative modern sector²³.

The pharmaceutical industry is Morocco's second most important chemical activity and occupies the second place on the African continent. Local production covers 65 percent of national needs, whilst 10 percent of the production is exported to European, Asian, African and Arab countries. A study by the AfDB and the Confederation Générale des Entreprises du Maroc CGEM (AfDB and CGEM, 2020) shows that the Moroccan pharmaceutical industry was benefiting from comparative advantages in countries such as Kenya or Cameroun, hence could increase its exports to these markets.

Consequently, the country is well positioned to become an industrial hub for the pharmaceutical industry. However, the sector is exposed to competition from emerging Asian countries (Indonesia, Philippines, Thailand, Vietnam, etc.), as well as Egypt and Tunisia. In a study on the private drug market in Morocco²⁴, IQVIA, the world leader in pharmaceutical data, indicates an encouraging pharmaceutical landscape, positioning the country well for the local production of both princeps (original medicine) and generics. This local production has been growing rapidly in recent years. Hence it could supply local and export markets. Morocco also had opportunities in the medical device sector.

However, the country ratio of health spending to GDP is at 6.5 percent, below the recommendations of the World Bank and the World Health Organization (12 percent). Therefore, there is space for a further expansion of the health

sector given the country's huge investment needs for health equipment and, by extension, consumables. The authorities' Health Plan 2025 aims to organise and expand the sector by simplifying health services, strengthening national health programmes and improving efficiency and governance. The Ministry of Health authorised the marketing of a series of generic drugs manufactured in Morocco. In June 2017, it authorised a generic antiretroviral drug active against the hepatitis B virus produced by a Moroccan pharmaceutical laboratory. A substantial portion of this local production could be exported.

The health sector has shown resilience and pro-active capacity during the Covid-19 crisis.

Moroccan industrialists mobilised, in record time, part of the textile production apparatus for the manufacture of masks. Production capacity increased from 3 million masks per day at the beginning of the pandemic to 16 million masks per day, generating a total production of 340 million masks between March and August 2020²⁵. In line with international standards, Morocco produced its first 100 percent "Made in Morocco" resuscitation beds. In order to support the development of this sector, the authorities should enhance Morocco's visibility abroad, attract foreign capital and industrialists and finally enter into partnerships. The pharmaceutical industry in Morocco could play a role beyond the distribution of medicines. The pharmaceutical industry, in addition to its drug distribution activity, is expected to move upmarket tackling other niches (vaccines, anesthesia, sampling and testing kits, etc.).

The automotive ecosystem

The automotive sector remains one of the main drivers of industrial development and employment in Morocco.

FDI in the sector averaged MAD 3 billion in the post-2012 period as compared to MAD 900 million between 2010 and 2011. According to the International Organization of Automobile Manufacturers (OICA), car production increased 2.4-fold between 2013 and 2019, from 167,452 units to nearly 400,000 units. In 2017, the sectoral turnover amounted to about EUR 6 billion and accounted for a total of 150,000 jobs. As part of the so-called "ecosystems" strategy implemented

²³ According to data from the Moroccan Ministry of Health, the sector represented about 13 billion MAD in 2018 with a total production of 425 million box units spread over a total of 46 production sites. Medical consumption per capita is about MAD 400 per year.

²⁴ The study was carried out on behalf of the association "Companies of Medicines in Morocco" (LEMM) with the main objective of carrying out the first mapping of the drug market in the private sector with relevant and reliable data for the period 2016-2018. The study covers only the private market which accounts for 75 percent of the total market.

²⁵ The certification process of masks in collaboration with the Moroccan Institute of Standardization (IMANOR) and the Technical Centers has been accelerated.

in 2014 involving the government and the Automotive Professional Association (AMICA), ambitious targets have been set. The private sector has committed to creating an additional 66,500 jobs by 2020, increasing the local value added by 21 percentage points and achieve an additional EUR 2.2 billion in exports. The government, for its part, had committed to providing an additional 110 hectares of rental at attractive prices, training around 66,500 people and providing EUR 170 million in investment subsidies. By 2017 some of the targets set in terms of jobs and locally produced added value were already achieved²⁶. The opening and the entry into production of the Renault plant in Tangier in 2012 as well as the PSA (now Stellantis) manufacturing unit in the Atlantic Free Zone of Kénitra in 2019 helped this performance²⁷.

Prior to the pandemic, the automotive sector planned to grow to MAD 110-120 billion exports by 2021 but it has been severely hit by the Covid-19 crisis. At the end of May 2020, exports fell by 40 percent, equivalent to MAD 13.9 billion. By the end of 2020, estimates indicate that the automotive sector could lose MAD 33 billion, or 3 percent of GDP (Aït Ali, 2020). The production of finished products dropped by 36 percent whilst semi-products decreased by 26 percent. Nevertheless, at the end of 2020, car exports amounted to MAD 72.72 billion, down 9.3 percent compared to 2019.

However, the automotive sector has limited spillover on Moroccan local enterprises (as discussed in Chapter 2). Local companies face constraints such as limited access to finance (as also highlighted in Chapter 3), lack of financial expertise and advices, the need to change their approach to quality and management-related problems especially in human resources. Moreover, despite the success of these SMEs, a hindrance to their development persists, namely the preferential treatment given to exporting companies located in free zones.

In the future, Morocco plans to stimulate the local expansion of the automotive industry and to attract new car manufacturers, notably from Spain and China. The Chinese

project envisages the production of the first electric vehicle in Morocco. Morocco also aims to produce 1 million vehicles per year by 2025. Once the Covid-19 crisis has been overcome, Morocco should be the world's leading car manufacturer on the African continent. Nevertheless, the industry remains dominated by labor-intensive activities, such as vehicle assembly and wiring. It is only beginning to expand into higher value-added activities, such as engines. As of yet the transfer of technology has been limited in the automotive ecosystem.

The aeronautic ecosystem

Morocco's aeronautic sector has grown strongly in recent years. According to AMDIE, the sector employed around 20,000 people in 2018 across 150 companies. Morocco is present, at different degrees of maturity, over the entire life cycle of the aeronautical value chain, namely, the manufacturing of aircraft, repair, maintenance and revision. The government's 2020 targets were generally met before the Covid-19 crisis, namely: a total of 23,000 jobs in the sector, an export turnover of about USD1.6 billion, a local integration rate of 38 percent and the installation of 100 new suppliers. Also, the sector has developed a diversified positioning in the value chain (equipment, components, and maintenance). Geographically, the Moroccan aviation industry is concentrated in three sites: Casablanca, Tangier and Kenitra. The industry relies on dedicated industrial platforms and specialised training institutes (including IMA). Morocco's significant success in this sector is due to several endogenous and exogenous factors, namely: a stable political and commercial environment, a strategic geographical positioning, the development of free zones and integrated platforms (P2I), as well as various and varied government incentives (financing taxation, etc.).

In 2020, the Moroccan Aerospace and Space Industries Group (GIMAS) estimates that aeronautic construction would decline by 30 to 40 percent in Morocco due to the pandemic. At the end of 2020, aeronautical exports fell by 14.6% compared to 2019. Exports, in value terms, should fall by at least 30 percent, whilst 15 to 20 percent of staff working in the sector could lose their jobs. In contrast, over the last few

²⁶ According to data from the Ministry of Industry: between 2014 and 2020, the number of jobs created by the Moroccan automotive sector is 161,599, 179 percent above the target for 2020, which is 90,000 jobs.

²⁷ The prospects for continued growth have been reinforced by Renault's plans in 2016 to invest more than EUR 900 million to support its ecosystem, enabling companies to source 65 percent of the components locally and generate an estimated EUR 2 billion in additional revenue and 50,000 new jobs by 2023.

years, the competitiveness of the sector has improved as well as its diversification providing some resilience. The sector has been able to attract core aeronautics industries such as embedded electronics, 3D reproduction (Thales), fiber optics (Nexans) and the signing of a Boeing ecosystem in 2016.

However, the aviation sector faces challenges that Morocco will have to overcome, including real estate given the growing demand for land around Casablanca.

Therefore, to decongest the Casablanca region, new settlement areas could be considered especially in the Tangier Free Zone. Secondly, the high level of regulation, certification and audit specific to the aviation industry creates a major barrier to the entry of new suppliers. Finally, the significant lack of technicians, of practical training in high-tech fields and limited access to finance are regularly highlighted by the professionals of the sector.

5.4 Looking forward: Policy recommendations for promoting trade integration and GVCs

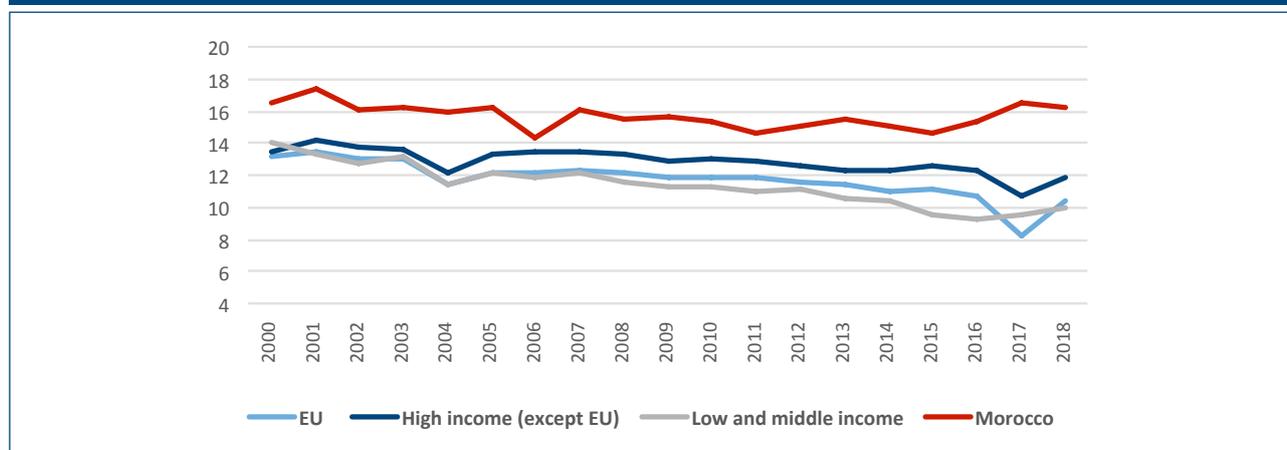
Following a decline during the 2009 global recession, FDI flows to Morocco increased over 2013-2015, exceeding USD 3 billion each year. In 2019, although FDI flows to Morocco decreased by 55 percent to USD 1.6 billion in 2019, according to UNCTAD data, FDI stock reached USD 66 billion in 2019, a rise of more than USD 20 billion as compared to the 2010 level. The direct effect of FDI on the productivity of receiving domestic enterprises is evidenced in the empirical literature (Hanousek et al., 2011 for Central and Eastern European countries; Arnold and Javorcik, 2009 for Indonesia).

This increase in productivity can be explained by the adoption of new technologies in production and the introduction of know-how. The effects may be more or less rapid depending on the type of FDI. Therefore, companies benefiting from the inflow of foreign capital could upscale their participation in GVCs. But given the small number of companies affected by these capital inflows, this direct effect alone cannot improve Morocco's overall positioning in GVCs. To have a more significant impact, the direct effect must be accompanied by positive spillovers. These spillover effects, horizontal and or vertical, could enable domestic companies to become exporters as relationships with foreign firms make them more competitive and better prepared for addressing the demand in international markets. These relationships can also reduce the cost of exporting through better access to information and processes necessary for export.

The positive effects of FDI on overall productivity and the possibility of upscaling on GVCs are far from automatic.

For these effects to occur, it is necessary, (i) to have enough absorption capacity, (ii) to promote, as Morocco has begun to do, the establishment of ecosystems around multinationals (iii) to encourage sustainable relations between multinationals and local enterprises. However, the empirical literature has failed to highlight the positive impact of FDI on the productivity of domestic enterprises apart from those directly affected by the inflow of foreign capital. An in-depth sectoral analyses and firm level analysis could allow to better understand what prevents Moroccan firms from benefiting from the positive effects of FDI.

Figure 5.8: Tariffs on Moroccan products (percent), 2000-2018



Source: AfDB computations using UNCTAD - Trains database.

Tariffs and non-tariffs barriers restrict trade to Africa.

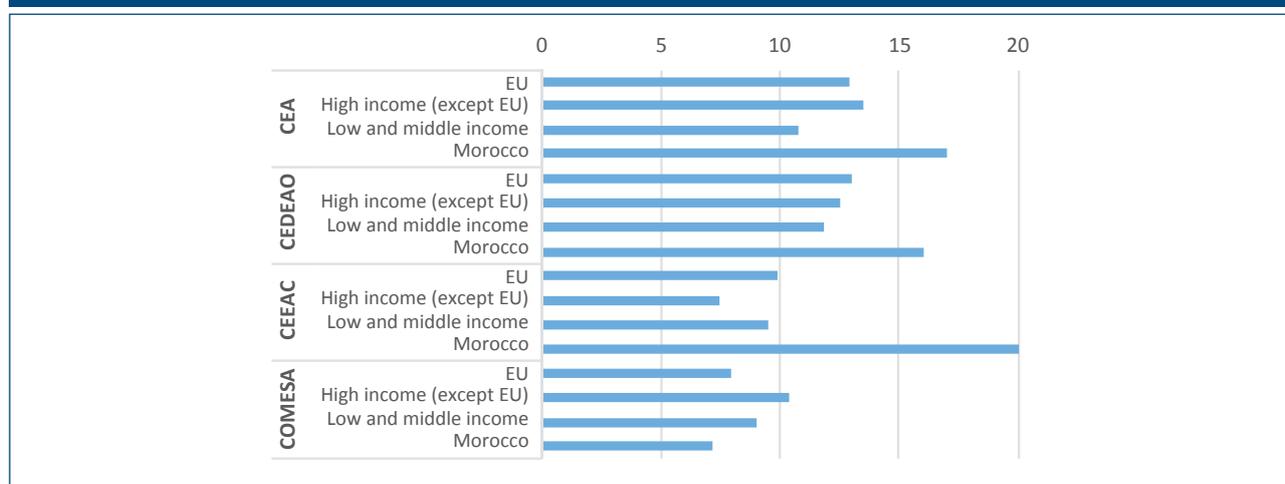
Morocco has signed many trade agreements with African countries. The country joined the African Continental Free Trade Area (AfCFTA) agreement, which came into force in May 2019. Morocco applied for membership of the Economic Community of West African States (ECOWAS) in February 2017. Surprisingly, compared to imports from the EU or other countries, sub-Saharan Africa charges the highest tariffs on products imported from Morocco. The average tariff is 16.25 percent, compared to around 10 percent for EU countries and about 12 percent for other high-income countries (Figure 5.8). Moreover, the rate differential between the average tariff applied to Moroccan products and to European products has increased from 3.5 percentage points in 2012 to more than 6 percentage points in 2018.

Morocco’s exports increased significantly with the country’s anchoring to global value chain. However, the

share of domestic value added in exports remains limited. Potential growth and inclusiveness would benefit from further trade integration provided exports include higher domestic added value. Moreover, enhancing trade with the African countries would allow Morocco to diversify its exports markets.

The average tariffs applied by Africa’s four main regional economic communities, namely the COMESA, the East African Community (EAC), the Central African Economic Community (ECCAS) and the Economic Community of West African States (ECOWAS)²⁸ differ greatly (Figure 5.9). Among its trade partners, COMESA charges the lowest tariffs to Moroccan products at 6.2 percent. In contrast, the average tariffs applied to Moroccan products are the highest among the trade partners of ECCAS, ECOWAS and ECA. Finally, at 20 percent, ECCAS tariffs on Moroccan imports is by far the highest.

²⁸ COMESA: Burundi, Comoros, DRC, Djibouti, Egypt, Ethiopia, Eritrea, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Soudan, Swaziland, Uganda, Zambia, Zimbabwe, and since 2018 Morocco and Tunisia. EAC: Burundi, Kenya, Rwanda, Tanzania and Uganda. ECCAS: Angola, Burundi, Cameroun, Central African Republic, Chad, Congo, DRC, Equatorial Guinea, Gabon and Sao Tomé & Principe. ECOWAS: Benin, Burkina Faso, Cabo Verde, Côte d’Ivoire, Gambia, Ghana, Guinea, Guinea-Bissau, Liberia, Mali, Niger, Nigeria, Senegal, Sierra Leone, Togo.

Figure 5.9: Tariffs on Moroccan products by COMESA, ECCAS, ECOWAS and EAC (percent)

Source: AfDB computations using UNCTAD - Trains database.

Obstacles to Moroccan trade to sub-Saharan Africa are not only limited to tariffs but also include transport, customs formalities or non-tariff barriers (AfDB-CGEM, 2020). Yet, a reduction of tariffs by sub-Saharan African countries as expected under the AfCFTA could have a positive impact on Moroccan exports as those are certainly below their optimal level.

Maghreb countries have numerous trade agreements.

In addition to AMU, Maghreb countries are involved in multilateral trade agreements such as the Great Arab Free Trade Area (GAFTA), the Agadir Agreement as well as bilateral agreements and preferential agreements with the EU. The numerous trade agreements certainly led to a general reduction in tariffs. However, at 7.5 percent, the average tariffs between AMU countries is much higher than the nil tariff of MERCOSUR²⁹, ASEAN³⁰, ECOWAS and EEACS and above the one of COMESA (2.4 percent). Moreover, no rules of origin protocols exist within AMU countries³¹. The application

of different protocols in terms of rules of origin complicates customs crossings and the convergence of non-tariff measures. Only the Euro-Mediterranean Association Agreements include a component on non-tariff measures. Hence, AMU countries should also consider agreements on non-tariff measures.

Moroccan trade with the EU is also subject to impediments.

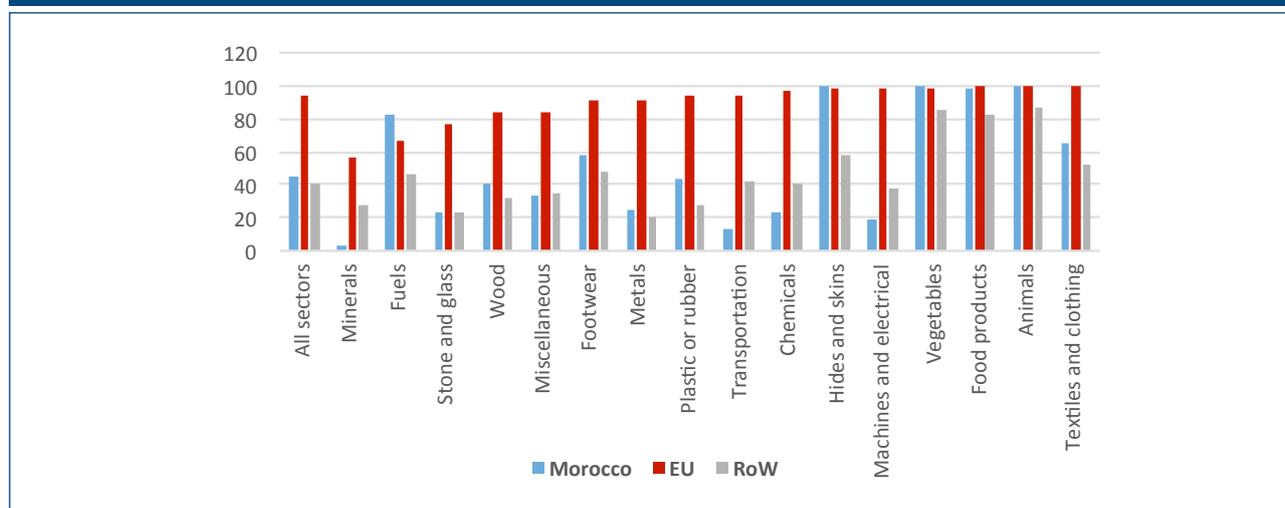
Moroccan exporters to the EU quote non-tariff barriers included in community acquis and/or the one imposed by the various European countries as the main impediment to trade. A quantitative analysis of non-tariff barriers confirmed the experience of Moroccan exporters. Figure 5.10 highlights the percentage of imported products on which at least one non-tariff barrier applies. In most sectors, the EU imposes non-tariff barriers, including in sectors where Morocco has a comparative advantage (textile/clothing, agricultural products, skin and leather, and footwear), whilst the share of imports into the EU subject to non-tariff barriers is above 90 percent and even frequently reaches 100 percent.

²⁹ Mercosur is an economic and political bloc comprising Argentina, Brazil, Paraguay, Uruguay, and Venezuela.

³⁰ The Association of Southeast Asian Nations (ASEAN) promotes economic, political, and security cooperation among its ten member countries: Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Vietnam.

³¹ The rules applied are the one of (i) the Regional Convention of Pan-Euro-Mediterranean Rules of Origin (PEM Convention), for Algeria, Morocco and Tunisia and/or (ii) the one of the GAFTA for all the Maghreb countries except Mauritania.

Figure 5.10: Share of imports subject to at least one non-tariff barriers in the EU, Morocco and the Rest of the World (percent)



Source: UNCTAD non-tariff barriers TRAINS database. Note: EU: European Union; RoW: Rest of the World.

Even though the EU makes around two thirds of Moroccan exports, it could increase further provided a diminution of non-tariff barriers especially concerning sectors in which Morocco has a comparative advantage. Accordingly, Moroccan exports to sub-Saharan Africa and Maghreb countries could increase drastically given that they are currently largely under-exploited. Defining appropriate industrial policies and support to GVCs needs to become a priority. Numerous work³² recommended better logistics, financing, market knowledge and human capital development in order to increase Morocco's participation to GVCs.

Morocco has several sectoral strategies (energy, logistics, trade, ICT, employment and tourism) for competitiveness.

The ambitions and visions of these strategies are generally clearly established. However, the creation of a cross-cutting and inter-ministerial public body, under the direct supervision of the Head of Government, could improve the effectiveness of those strategies. This body would be responsible for the development, planning and improvement of the coherence and coordination of sectoral public policies. In addition, it could develop a culture of evaluation and accountability within public administration. The following sections focusses on other areas that could positively impact competitiveness in Morocco and a better anchoring to GVCs.

In the context of emerging sectors such as the pharmaceutical one, the authorities should review the objectives of the national innovation strategy. Morocco could benefit from establishing an independent innovation policy management structure equipped with financial and human resources to enable it to respond effectively to demands (such as those implemented in Turkey or Malaysia). In order to encourage private sector involvement in the financing of research and development, the authorities could provide indirect support mechanisms through tax credits. This mechanism, easy to use, has been useful in other countries. On another hand, strong links between universities and the private sector have a positive impact on research and innovation. As such, it is crucial to create an adequate regulatory framework governing the status of researchers.

Supporting local SMEs to speed up their integration into GVCs is an important priority.

The 2014 PAI pays special attention to FDI. While this strategy has succeeded in attracting FDI into dynamic sectors, it has not fully enabled the modernization and the competitiveness of Moroccan SMEs. The SME sectors currently faces the following market distortions: i) offering incentives for FDI especially those located in free zones; ii) directing the majority of services provided by the Moroccan Investment and Export Development

³² AfDB/FEMISE (2019); AfDB-CGEM (2020), AMDIE (2019) and IMIS (2021).

Agency (AMDIE) towards relatively large companies; iii) the possibility for companies exporting more than 70 percent of their production to be located in free zones. Those issues should be tackled for SMEs to benefit from GVCs.

Morocco has put in place development policies and programs that have led to notable improvements. The country has greatly expanded its transport infrastructure (maritime, air, road), improving international connectivity. Further modernization of the logistics sector, better linking logistics development strategy and transport policy, including strengthening coordination and cooperation among stakeholders could further benefit Morocco's exports. It could prove useful to foster the emergence of strong formal local players through a change in the structure of the domestic road transport and logistics sector, which is marked so far by a high degree of informality.

Standards and certifications help to develop quality products making it possible for those products to access foreign markets. Although Morocco has produced

standards, their adoption by companies remains weak. Hence, better support for the compliance to standards and certifications and/or production processes would be helpful as well as the following measures: (i) to promote the adoption of standards and accreditation by companies by strengthening the support of stakeholders; (ii) to increase the establishment and accreditation of laboratories and other inspection bodies; (iii) to improve import and export compliance assessment procedures. Those policy recommendations are timely given the ongoing reflection on Morocco's new development model as requested by King Mohammed VI. Indeed, the special Commission on the New Development Model mandated by the King Mohammed VI presented its conclusions in May 2021. The development goals targeted at the 2035 horizon aim for a Morocco that is prosperous, skilled, inclusive and supportive as well as bold. The generalization of social protection encompassing universal health insurance, retirement, unemployment insurance and family allowances should enable the Kingdom to return to strong, inclusive and resilient growth over the medium term.

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