BANK AL MAGHRIB

Monetary Policy Report

N° 09 / 2008

Document prepared for
the Bank Board
december 23, 2008

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LIST OF ABBREVIATIONS

AWI	:	Average wage index
BAM	:	Bank Al-Maghrib
CDG	:	Caisse de Dépôt et de Gestion (Deposit and Management Fund)
CFG	:	Casablanca Finance Group
CLI	:	Cost of living index
CNSS	:	Caisse nationale de sécurité sociale (National Social Security Fund)
CUR	:	Capacity utilization rate
DF	:	Deposit facility
DH	:	Dirham
ECB	:	European Central Bank
GDP	:	Gross domestic product
GFCF	:	Gross fixed capital formation
HCP	:	High Commission for Planning
HFC	:	Household final consumption
HP	:	Hodrick-Prescott
ICT	:	Information and communication technologies
IMF	:	International Monetary Fund
IPI	:	Import price index
IPPI	:	Industrial producer price index
LI	:	Liquid investments
LW	:	Liquidity withdrawal
MASI	:	Moroccan All Shares Index
MPR	:	Monetary Policy Report
NFA	:	Net foreign assets
OC	:	Office des Changes (Foreign Exchange Office)
OCP	:	Office chérifien des phosphates (Morroccan Phosphates Office)
OECD	:	Organization for Economic Cooperation and Development
OMPIC	:	Office marocain de la propriété industrielle et commerciale (Moroccan Industrial and Commercial Property Office)
ONE	:	Office national d'électricité (National Electricity Office)
RCAR	:	Régime collectif d'allocation de retraite (Collective Scheme for Retirement Allowances)
TB	:	Treasury bills
UCITS	:	Undertakings for collective investment in transferable securities
VA	:	Value added
VAT	:	Value added tax

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PRESS RELEASE

BANK AL-MAGHRIB BOARD MEETING

Rabat, December 23, 2008

1.The Board of Bank Al-Maghrib held its quarterly meeting on Tuesday December 23, 2008.

2. At this meeting, the Board examined recent economic, monetary and financial trends and the inflation forecasts made by the Bank staff up to the first quarter of 2010.

3. Available data show that, in line with the forecasts, year-to-year headline inflation fell to 3.9 percent in November, from 4.6 percent in the second quarter of 2008. This trend was also reflected in core inflation, which slowed from 4.9 percent in the second quarter to 3.5 percent in November.

4. The Board considered that the gradual deceleration in prices was primarily driven by tradable goods, particularly imported staple foods, which were affected by the fall in commodity prices on world markets. Concurrently, industrial producer prices rose by 16.5 percent in October, compared with 22.5 percent in September.

5. The latest data available and Bank Al-Maghrib estimates suggest that the fundamentals of the economy remain strong, despite the effects that the economic contraction of our main trading partners has had on some sectors. Economic growth stood at 6.7 percent during the first half of 2008. Bank loans however continued to grow at a rapid pace, of about 26.5 percent in the third quarter, mainly propelled by the momentum in corporate loans in the form of cash advances, as well as in equipment and real estate loans.

6. In 2009, the slowdown in world economy is expected to weigh on some domestic sectors. This impact would however be softened by the resilient domestic demand.

7. Taking note of the Board decision of September 23, 2008 and bearing in mind the impact the rapid and likely continued decline in world economy could have on inflation, the central inflation forecast for the six coming quarters was revised downwards. In the first quarter of 2010, it should settle at a rate lower than 3 percent year-on-year. Over the forecast horizon, it would now stand at 3 percent on average, instead of 3.8 percent predicted in the last Board meeting.

8.The risks and uncertainties surrounding the central inflation forecast for the next quarters broadly follow a downward trend, essentially driven by the sharp contraction in external demand. This likely trend, however, is partly contingent upon the extent of the transmission of world commodity price decline to domestic prices.

9.In this context marked by a downward trend in the balance of risks and an inflation forecast in line with the objective of price stability, the Board decided to keep the key rate unchanged at 3.50 percent, while closely monitoring all of these elements, particularly the materialization of the transmission of import price decline to inflation and pressures on the labor market.

10. Noting the scope and sustained nature of liquidity shortage on the money market, and in light of forecasts for the change in liquidity factors, the Board decided to reduce required reserve ratio by 3 percent, bringing it to 12 percent as of January 1, 2009.

11. The Board also examined the three-year budget forecasts and approved the budget of fiscal 2009.

12. The Board agreed on the schedule of its meetings for the year 2009 as follows:

- March 24, 2009
- June 16, 2009
- September 22, 2009
- December 22, 2009

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OVERVIEW

In line with Bank Al-Maghrib projections, there was a gradual decline in both headline inflation and core inflation during the third quarter of 2008, primarily following the easing of pressures originating from international commodity prices and the marked contraction in global growth. In fact, after having peaked at nearly 4.6 percent in the second quarter of the year, headline inflation fell to 3.9 percent in September and then to 3.5 percent in October. This trend was also reflected in core inflation, which slowed from 4.9 percent to 3.5 percent, then to 3.4 percent over the same period. Moreover, prices for tradables, particularly staple foods, were affected by the fall in commodity prices on world markets. Inflation of nontradables remained stable, running at about 2.6 percent since August. The slowdown in inflation is also visible, albeit to a lesser degree, in industrial producer prices, which dropped from 22.5 percent in September to 16.4 percent.

At the end of 2008, despite a sharp contraction in our key partners' economies, domestic economic growth is expected to hover between 6 and 6.5 percent, slightly below the level predicted in the last Monetary Policy Report. This rate reflects the buoyancy of domestic demand, following a better crop year than that of 2007. According to the latest data available, economic growth in the first half of 2008 stood at 6.7 percent, notably as both agricultural and nonagricultural value added increased by 11.2 and 6.2 percent, respectively. In the second half of the year, economic growth is expected to decelerate to 5.8 percent. Against this backdrop and according to Bank Al-Maghrib estimates, the overall output gap remained positive in the second quarter of 2008.

Similarly, nonagricultural output gap remained positive, at a rate higher than that reported in the second quarter of the previous year. It is projected to decrease in the last two quarters of 2008, while posting a positive value. Output capacity utilization rate in the industrial sector went down, during the third quarter of 2008, by around three percentage points year-on-year. Against this backdrop, the national unemployment rate stood at 9.9 percent, unchanged from the same period of last year. In 2009, the slowdown in world economy should affect some domestic sectors, particularly the industry and services. This impact would be partly cushioned by the good performance of the agricultural sector, owing to the favorable weather conditions which marked the beginning of the crop year. Altogether, the analysis of all these indicators suggests a moderation of pressures on prices in the coming quarters.

Turning to monetary data, the latest available figures show continued gradual deceleration in money creation, firstly announced in the June 2008 MPR. In fact, after having recorded an annual growth of 12.4 percent in the third quarter of 2008, down from 13.4 percent a quarter earlier, the M3 aggregate increased at a modest 9.3 percent in October, on a year-to-year basis. As a result, nonfinancial agents' monetary surplus was virtually nil, suggesting an easing in monetary-driven inflationary pressures during the next months. Bank loans yet continued to grow rapidly, at nearly 26.5 percent in the third quarter and in October 2008, mainly propelled by the momentum in corporate loans in the form of cash advances as well as equipment and real estate loans. This trend would, however, slow down in the last quarter of the year and in 2009. The findings of the half-yearly survey conducted by Bank Al-Maghrib among banks show that the annual rate of credit growth, which is expected to stand at 23 percent at end 2008, would decelerate in 2009.

As to lending rates, the latest findings of BAM survey for the third quarter of 2008 show a slight increase of around 29 points in the overall average rate compared with the second quarter.

Based on all these elements and considering the expected impact of the last Board decision of September 23, the central inflation forecast for the six coming quarters was revised downwards, compared with the forecasts presented in the previous Monetary Policy Report. This basically reflects the rapid and substantial easing of some external upside risks, together with the pronounced and likely continued slowdown in global economy. By the end of the forecast horizon (the first quarter of 2010), the central inflation forecast would settle at around 2.7 percent, down from the rate predicted in the September 2008 MPR. Over the six coming quarters, it would stand on average at 3 percent. For the fourth quarter of 2008, we expect a fall in inflation compared with the third quarter, from 4.6 to 3.9 percent.

The risks and uncertainties surrounding the central inflation forecast broadly follow a downward trend, essentially driven by the sharp contraction in external demand. This likely trend, however, is partly contingent upon the extent of the transmission of world commodity price decline to domestic prices, and, internally, on the pressures on the labor market.

1. AGGREGATE SUPPLY AND DEMAND

At the end of 2008, the national economy would grow between 6 and 6.5 percent, a level slightly lower than that foreseen in the previous Monetary Policy Report, thus reflecting the effects of our key partner economies' slipping into recession. Quarterly growth dropped from 7 percent in the first quarter to 6.5 percent in the second and would hover between 5.5 percent and 6 percent for the remainder of the year. Moreover, foreign exchange indicators as at end October point to deterioration compared with the previous year. This development is linked to the moderate increase in exports excluding phosphates and derivatives, the decline in remittances from Moroccans living abroad, and the drop in travel receipts and those from private foreign investments and loans. In contrast, domestic demand would continue to sustain growth, as domestic household consumption would remain strong and investment would keep its momentum, particularly in the building and public works sector. In 2009, the slowdown in world economy would certainly impact some domestic sectors, particularly industry and services. This impact would be partly mitigated by the good performance of the agricultural sector following the favorable weather conditions which marked the beginning of the current crop year.

1.1 Output

Economic growth is expected to slightly slow down from 7.0 percent to 5.5 percent between the first and fourth quarters of the current year, following the downturn in world demand.

In the first half of 2008, growth stood at 6.7 percent, driven by an increase in both agricultural and nonagricultural value added by 11.2 and 6.2 percent, respectively. In the second half-year, GDP would grow to 5.8 percent, thus reflecting a deceleration compared with the first half-year.

Growth in agricultural value added should be around 10.1 percent in the second half of 2008. After the adverse weather conditions which prevailed over the last two years, the 2008-2009 crop year has benefited from significant rainfall. In these conditions, the pace of fall crops and agricultural input sales has significantly accelerated since September 2008 (see table 1.2). These favorable developments are mirrored in the downward trend observed, since the start of the current marketing year, in cereal imports which declined in volume by 21 percent as at end October 2008, compared with an expansion by 123 percent in the same period last year. Concurrently, exports of early vegetables and citrus fruits continued their upward trend. It should be noted that the growth rate of citrus fruit exports (40 percent) is higher than that of early vegetables (5.9 percent). This situation is attributable to the delayed planting of early vegetables, whose mass production is expected to start in mid-November.

Table 1.1: Year-to-year growth of quarterly GDP at 1998 chained prices per major activity branches

	2007*		2008			
Activity branches	QIII	QIV	QI	QII	QIII(P)	QIV(P)
Agriculture	**-21.7**	**-21**	**10.9**	**11.2**	**10.5**	**9.8**
Nonagricultural value added	**6.4**	**6.4**	**6.5**	**5.8**	**5.5**	**5.1**
Fishing	-15.1	-8.5	44.7	16.5	5.0	7.0
Extractive industry	9.4	5.5	2.6	-1.8	0.7	1.2
Industry (excluding oil refining)	4.1	5.0	5.3	4.3	4.4	4.5
Oil refining and other energy products	66.1	56.5	23.1	-0.4	-1.0	-1.2
Electricity and water	9.1	1.0	6.6	6.3	6.5	6.7
Building and public works	11.7	9.8	10.3	10.6	10.8	10.4
Trade	2.4	3.2	5.1	5.3	5.0	4.5
Hotels and restaurants	4.8	3.2	-1.8	-1.7	-2.3	-2.0
Transportation	8.7	10.2	6.2	4.2	4.0	4.3
Post and telecommunications	8.7	10.2	6.2	4.2	4.0	4.3
Financial activities and insurance	19.1	21.3	20.2	19.4	17.8	15.0
Services to businesses and private individuals	8.1	8.2	6.8	6.2	5.8	5.5
General government and social security	2.8	2.8	5.7	6.3	5.8	5.5
Education, health and social action	7.9	8.7	4.5	5.3	4.5	4.5
Taxes on products net of subsidies	8.1	10.0	6.6	4.9	4.5	4.6
Gross domestic product	**2.5**	**2.7**	**7.0**	**6.5**	**6.0**	**5.6**

(*) Revised data

Sources: HCP, and BAM forecasts

Livestock state of health is generally satisfactory, given the regeneration of the vegetational cover of ranges, the availability of livestock feed, and the efforts made to preserve livestock.

The second half of 2008 would be marked by a 5.9 percent growth in fishing activities, down from 9.8 percent in the first half-year. As at end October, the catch of inshore and artisanal fisheries grew by 13 percent in volume to 602,395 tons, and by 28 percent in value to 3,768 million dirhams. These developments are attributable to the significant catches of pelagic fish and the rise in cephalopod prices.

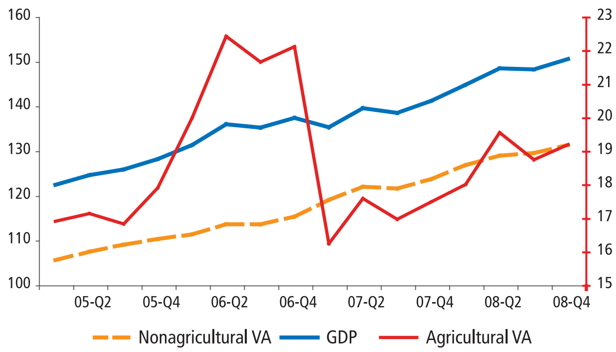
The value added of nonagricultural activities should be affected by growth slowdown in our major partners, making respectively 5.5 and 5 percent in the third and fourth quarters of the year, compared with a 6.2 percent increase in the first half of 2008.

After posting a drop in the second quarter, the value added of mining activities would start to recover in the third quarter of 2008, to grow by 0.7 percent. This rebound is projected to continue in the fourth quarter of the year with an expected growth of nearly 1.2 percent. Exports of phosphates, as at end October, increased in value by more than 11 billion to 16.4 billion dirhams. This trend is the result of the strong rise in raw phosphate prices, which averaged more than 1,511 dirhams per ton, compared with 431 dirhams in October 2007. In terms of volume, these exports declined by 6.7 percent.

The value added of energy activities should continue its upward trend, increasing by 6.3 and 6.5 percent in the third and fourth quarters of 2008, respectively, mostly stimulated by the strength in the "electricity and water" branch, which grew by 6.6 percent in the second half of 2008. Net domestic production of the Office National d'Electricité (ONE) as at end July 2008 rose by 7.1 percent, compared with a 2.9 percent fall in July 2007. The ONE overall sales were up by 7.5 percent during the same period.

The value added of industrial activities excluding oil refining should drop slightly from 4.5 percent in the third quarter 2008 to 4 percent in the fourth quarter. The findings of the October 2008 BAM

Chart 1.1: Quarterly change in GDP agricultural and nonagricultural VA, in billions of dirhams



Sources : HCP, and BAM forecasts

Table 1.2 : Data of 2008-2009 crop year as at November 28, 2008

	2007-2008 (1)	2008-2009 (2)	Reference (*) (3)	Change in % (2)/(1)	Change in % (2)/(3)
Rainfall indicators					
Cumulated rainfall (in mm)	72.0	203.0	93.2	181.9	117.8
Dams' filling rate (%)	44.0	50.0	50.0	-	-
Cultivated lands (in thousands of Ha)					
Fall cereals	1 100.0	3 300.0	1 650.0	200.0	100.0
Legumes	40.0	100.0	54.0	150.0	85.2
Forage crops	198.0	281.0	225.0	41.9	24.9
Sugar beet	45.5	50.3	40.0	10.5	25.8
Agricultural inputs (in millions of quintals)					
Seeds	574.0	614.0	530.0	7.0	15.8
Fertilizers	2 133.3	2 880.0	2 504.3	35.0	15.0
Exports of citrus fruit and early vegetables (in thousands of tons)					
Early vegetables	135.0	143.0	96.0	5.9	49.0
Citrus fruit	100.0	140.0	98.0	40.0	42.9

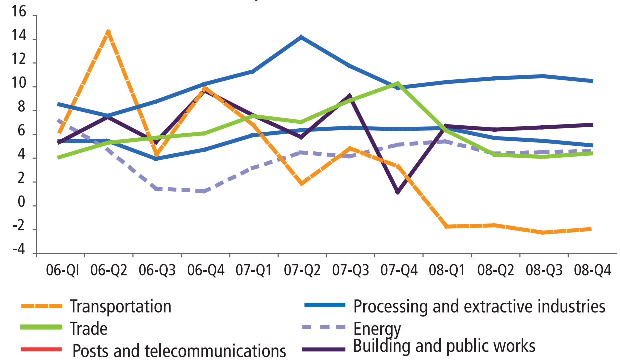
(*) Average of the last five crop years

Sources: Ministry of Agriculture and Fisheries, and BAM calculations business survey in the industry reveal a decline in orders received, a drop in local sales and exports, and a reduction in prices for finished products. Output capacity utilization rate stabilized at 70 percent. Excluding refining, this rate stood at 71 percent. Moreover, imports of finished capital goods, as at end October, grew in value by 28.5 percent to nearly 59.7 billion dirhams. This growth is attributable to the increase by 18.3 percent in the purchases of machines and sundry devices, 95.3 percent in grinding and agglomerating material, and 26.3 percent in imports of industrial vehicles. Exports of finished capital goods totaled 13.1 billion dirhams, up by 12.8 percent, stimulated by exports of electricity wires and cables (+11.6 percent) and industrial vehicles (+39 percent).

The building and public works sector should maintain momentum in the second half of 2008, growing from 10.4 percent in the first half to 10.6 percent. This positive trend is mostly driven by the strength in demand for new homes, the ongoing large infrastructure projects and the expansion in real estate loans. Cement sales, as at end September, rose by 11.9 percent to 11 million tons, compared with 9.8 million tons during the same period in 2007.

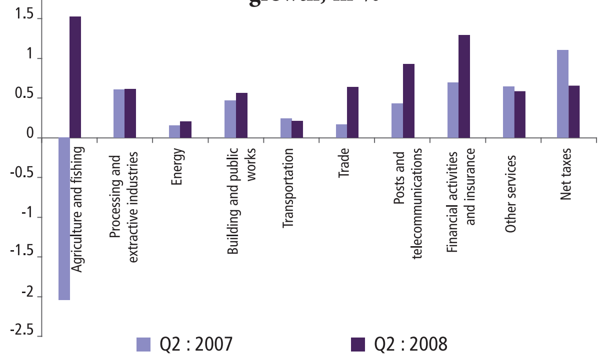
Trends in the key indicators of tourism activity were divergent. On the one hand, the influx of tourists slightly decelerated as of the first half of 2008, growing by only 6 percent as at end October 2008, down from 14 percent in 2007, to 6.7 million tourists instead of 6.3 million tourists in the same period last year. This involved an 18 percent drop in the number of English visitors, and an 8 percent increase in the number of nationals from other countries. On the other hand, the negative performance of overnight stays in classified hotels, registered since the beginning of the year, notably at the level of nonresidents in Agadir and Marrakech, was offset by the steady progress in resident overnight stays. The upward trend in the overnight stays of residents is expected to continue through 2009, supported by the strengthening of tourism infrastructure especially under the "Biladi" and "Mada'In" Plans. Likewise, room occupancy rate continued to fall and travel receipts went down by 1.5 percent to 49 billion dirhams. With the aim of reducing the downturn in main tourist-generating markets, the public authorities have

Chart 1.2: Year-to-year change in the value added of some activity branches, in %



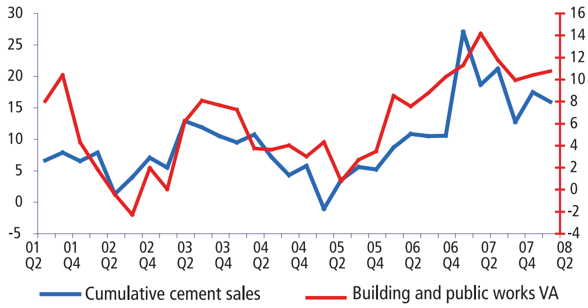
Source : HCP, and BAM forecasts

Chart 1.3: Contribution of activity branches to overall growth, in %



Sources: HCP, and BAM calculations

Chart 1.4: Year-to-year change in building and public works' value added and in cumulative quarterly cement sales, in %



Sources: HCP, and BAM forecasts

decided to readjust the marketing tools in order to promote the new features of the tourist offer as from next year and to foster partnerships with tour operators.

In the second half of 2008, the value added of the transportation sector should maintain the same rate of the second quarter of the year, growing by 4.2 percent, after 6.2 percent in the first quarter. Receipts from international transportation services, as at end October, increased by 14.5 percent to 14 billion dirhams, whereas expenditures of transportation services rose by 5.1 percent to 15.4 billion dirhams. The number of international passengers having passed through Morocco's airports, as at end October, increased to 9.3 million, up by 10 percent compared with the same period last year.

The value added of the posts and telecommunications sector is expected to remain consistent with the sector' positive trend. Over the third and fourth quarters of 2008, this value added should rise by 12 and 11.5 percent, respectively. The number of mobile, fixed-line and internet subscribers, as at end September 2008, grew by 16, 25 and 41 percent, respectively, reaching in thousands 22,294, 2,834 and 689.5, thus confirming this momentum. Moreover, mobile and fixed-line penetration rates stood at 72.3 and 9.2 percent, respectively. Revenues of call centers as at end October totaled 2.6 billion dirhams, up by 21.6 percent compared with a 9 percent decrease in their expenditures.

Altogether, GDP is expected to grow by around 6 and 5.5 percent in the third and fourth quarters of 2008, respectively. At the end of 2008, the growth rate of the national economy would range between 6 percent and 6.5 percent, supported by an increase of 5.5 to 6 percent in the nonagricultural value added and 10 percent in the agricultural value added.

In 2009, the Moroccan economy is expected to feel the impact of global slowdown. Economic growth would decelerate only slightly, on the back of a 7 to 8 percent increase in the agricultural value added, under the assumption of a cereal production of 60 to 70 million quintals.

1.2 Consumption

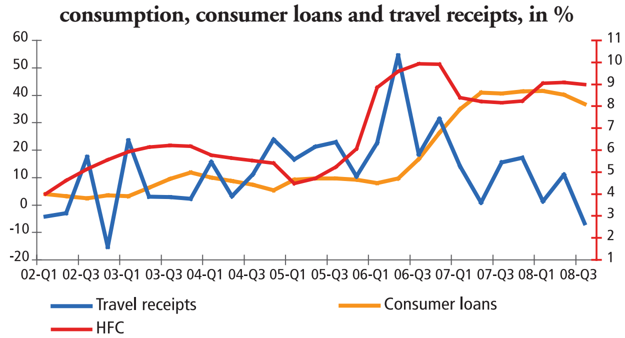
The positive trend in domestic final consumption is expected to grow stronger in the remainder of the year, which will help sustain the overall economic growth. The momentum in consumption is chiefly driven by the measures undertaken by the public authorities to maintain the prices of food and energy products. In the first ten months of the year, the budget allocated to subsidized products increased by 14.2 billion to nearly 27.2 billion dirhams, 109 percent higher than in the same period of 2007.

In addition, the 2.2 percent rise in the share of gainful employment in total labor in the third quarter of 2008 and the increase in wages in July 2008 contributed to maintaining household purchasing power. Also, consumer loans grew by 32 percent as at end October 2008.

The strength in household consumption is further evidenced by the change in the imports of finished consumer products and food products. As at end October 2008, they increased by 11.5 and 26.1 percent, respectively, particularly on the back of a 31.8 percent growth in private car imports.

However, nonresident household consumption is expected to decelerate, as travel receipts would slightly slow down to 49 billion dirhams and remittances from Moroccans living abroad would stabilize at nearly 46.2 billion dirhams.

Chart 1.5: Year-to-year quarterly change in household final consumption, consumer loans and travel receipts, in %



Sources: HCP, OC, and BAM calculations

As for general government consumption, operating expenditure increased by 6.1 percent as at end October to 84.5 billion dirhams, to cover outlays for staff and the other goods and services, whose year-to-year growth rate stood at 6.7 and 4.9 percent, respectively.

In 2008, domestic final consumption would grow by 8.1 percent, with an increase of 8.9 percent in household final consumption and 5.4 percent in general government final consumption.

1.3 Investment

Gross fixed capital formation is expected to continue its upward trend for the remainder of the year, making an annual growth of 15.8 percent.

Investment was mainly supported by the growth in the imports of finished capital goods and in equipment loans, which stood as at end October at 28.5 and 34.1 percent, respectively.

Moreover, enterprise creation remains vigorous. It concerned in particular the sector of services ahead by 52 percent of the total incorporation certificates issued as at end September 2008, followed by the trade sector (23.5 percent) and the building and public works' sector (13.5 percent). Overall, the OMPIC issued 45,751 incorporation certificates, 6 percent higher than in the same period of 2007.

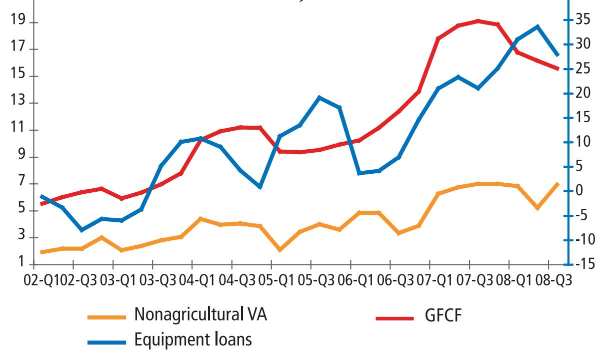
Earnings from private foreign investments and loans fell by 16.8 percent to 25.6 billion dirhams at the end of October, down from 30.7 billion dirhams in the same period of last year. However, compared with the average of January through October of the past five years, these receipts exhibit a 17.9 percent increase.

Bank Al-Maghrib business survey for the third quarter of 2008 shows that 63 percent of corporate managers think the business climate is broadly positive, particularly in chemical and parachemical industries and mechanical and metallurgical industries. The growth outlook for the coming months remains positive as well.

According to the balance of payments as at end June 2008, receipts from foreign direct investments fell by 9.7 percent to 15.7 billion dirhams, from 17.4 billion dirhams a year earlier. This decline was particularly reported in the sectors of transportation (97.4 percent), trade (80.3 percent) and tourism (61 percent), whereas investment in real estate and banking sectors grew at respective rates of 62.8 percent and 52.3 percent. France maintained its last year's leading position ahead with 35.4 percent of total FDI, followed by the United Arab Emirates with 27.6 percent.

In the public sector, capital expenditure of the Treasury as at end October 2008 rose by 8.6 billion dirhams to 29.6 billions, up 40.9 percent from the same period last year.

Chart 1.6: Year-to-year quarterly growth of gross fixed capital formation, nonagricultural value added, and equipment loans, in %



Sources: HCP, and BAM calculations

1.4 Foreign trade

In the first ten months of 2008, trade balance deficit has widened by 28.1 percent year-on-year, down from 34.2 percent in the same period of 2007. Exports grew from 11.6 to 32.8 percent, whereas imports rose from 22.4 to 30.3 percent. Accordingly, year-on-year coverage ratio slightly improved from 47.7 to 48.6 percent.

The strength in exports is mainly driven by the threefold increase in the sales of phosphates and derivatives, benefiting from high prices, though export quantities have decreased. Excluding phosphates and derivatives, exports grew by only 3.4 percent, owing to the slowdown of foreign demand in the context of recession in the Eurozone. International economic situation has negatively impacted the sales of ready-made garments, hosiery items and electronic components. A downward trend has been observed in exports of ready-made garments since the third quarter of 2007, and in exports of hosiery items as of the fourth quarter of 2007. Exports of sea products, electrical wires and cables and citrus fruit grew by 13.7 percent, 11.6 percent and 14.8 percent,

respectively.
Expansion in imports is attributable to the higher energy bill and the increase in other imports. In fact, purchases of gasoline and fuel-oil have almost doubled in value and grew by 41 percent in volume. Oil purchases rose by 34.5 percent in value and fell by 8 percent in volume, as the average price per imported ton grew by 46.1 percent. As a result, the energy bill went high by 46.9 percent. Other imports posted an increase of 26.1 percent, mostly driven by the rise in purchases of capital goods as part of the strength in investment. Similarly, imports of crude products significantly increased due to an expansion by 450.5 percent in the purchases of crude sulfur and the growing imports of vegetable oil. Imports of semifinished products also moved up, boosted by the rise in iron and steel prices and the steady demand of the processing industries. Following the same upward trend, imports of food commodities and consumer goods have been sustained by the increase in wheat and corn imports, on the one hand, and private cars, spare parts and medicines, on the other.

The worsening outlook for world growth, particularly in the eurozone, and the recent drop in phosphate international prices are expected to significantly decelerate the growth rate of Moroccan exports. At the same time, the current fall in commodity prices and the prospects for a positive crop year in Morocco should help reduce the cost of imports, particularly for energy and food products.

Table 1.3: Trade balance growth between January and October (year-to-year)

(in millions of Dhs)	J-O 2007	J-O 2008	Change Amount	%
Total exports	**101 873**	**135 243**	**+33 370**	**+32.8**
Exports of phosphates and derivatives	18 109	48 630	+30 521	+168.5
Exports excluding phospha-tes and derivatives	83 764	86 612	+2 848	+3.4
Ready-made garments	16 887	15 768	-1 119	-6.6
Hosiery items	6 561	5 517	-1 044	-15.9
Citrus fruit	2 015	2 314	+299	+14.8
Total imports	**213 381**	**278 034**	**+64 653**	**+30.3**
Energy product imports	43 245	63 535	+20 290	+46.9
Other imports	170 136	214 499	+44 363	+26.1
Wheat	7 120	9 809	+2 689	+37.8
Capital goods	46 487	59 714	+13 227	+28.5
Consumer goods	40 032	44 627	+4 595	+11.5
Trade deficit	**-111 508**	**-142 791**	**+31 283**	**+28.1**

Source: Foreign Exchange Office

2. PRESSURES ON OUTPUT CAPACITY AND LABOR MARKET

According to BAM estimates, the overall output gap continued its upward trend in the second quarter of 2008, while remaining positive, given the improvement in the crop year from one year to the next. Nonagricultural output gap was also positive, above the rate observed in the same period last year, as nonagricultural sectors maintained momentum. In the third quarter, output capacity utilization rate in the industrial sector fell by one percentage point from one quarter to the next. In the labor market, national unemployment rate remained flat in the third quarter, compared with the same period of previous year. This reflects the drop in urban unemployment rate supported by the vigor in nonagricultural activities, on the one hand, and the rise of unemployment rate in rural areas, on the other hand. The sectors of building and public works and services are still the major job suppliers. Available wage indicators point to an increase in real private sector wages over the second quarter. Another increase in the minimum wage is scheduled for July 2009, subsequent to the rise introduced in July 2008. Overall, all of these indicators suggest that pressures on prices will continue through the coming quarters, albeit at a level lower than the one indicated in the latest MPR.

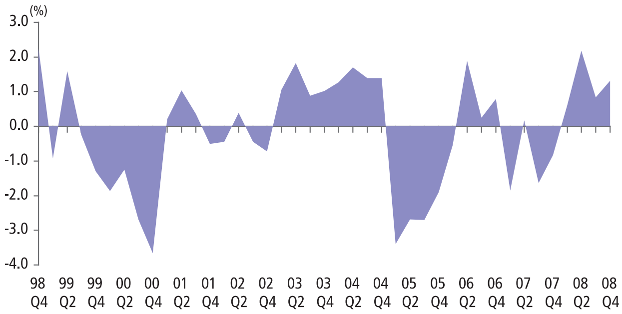
2.1 Pressures on output capacity

Based on the latest HCP data, overall output gap continues to be positive over the year 2008, reflecting a better crop year and the steady growth of other sectors. Overall output gap peaked in the second quarter and is set, according to BAM projections, to slow down over the last two quarters of 2008, while remaining positive.

Nonagricultural output gap accelerated significantly in the first two quarters of 2008, supported by the strong growth in nonagricultural sectors. Projections for the second half of 2008 suggest narrowing of nonagricultural output gap, which would yet remain positive. These prospects are traced back to the current worsening of the international situation, marked by the economic deceleration of our major partners which would essentially impact foreign demand for Moroccan exports and tourist sector.

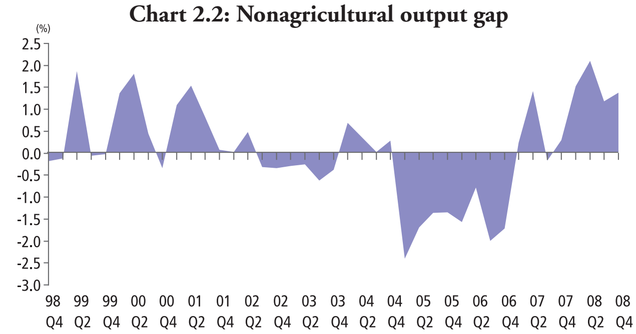
The findings of BAM business survey in the industry for October show that output capacity utilization rate stabilized around 70 percent from one month to the next. Excluding refining industry, this rate stood at 71 percent, down by one percentage point. As per sector, output capacity utilization rate reached 73 percent in textile and leather industries, and chemical and parachemical industries, 68 percent in electrical and electronic industries, and food-processing industries, and 63 percent in mechanical and metallurgical industries.

Chart 2.1: Overall output gap



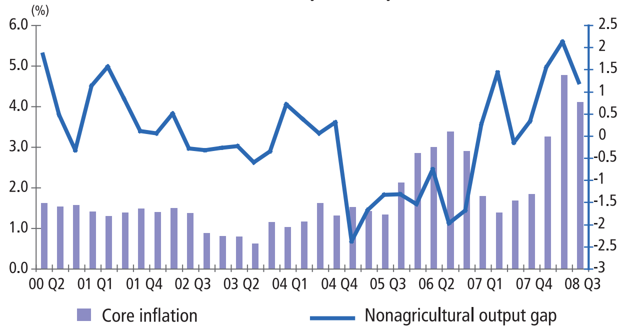
Sources: HCP, and BAM estimates

Chart 2.2: Nonagricultural output gap



Sources: HCP, and BAM estimates

Chart 2.3: Nonagricultural output gap and core inflation (year-to-year)



Sources: HCP, and BAM estimates

Apparent labor productivity[1] in nonagricultural activities significantly expanded, continuing the upward trend that began in the fourth quarter of 2006. This increase is attributable to the rise in urban employment that grew less rapidly than the nonagricultural GDP estimated by BAM for the third quarter of 2008.

The results of the survey also reveal that the costs of commodities, other than energy, remain the primary source of increase in unit production costs in the third quarter of 2008. However, payroll costs rose from one quarter to the next, with a balance of opinion of 56 percent instead of 27 percent in the previous quarter, largely due to the upward adjustment of minimum wage which came into force as of the third quarter of 2008. This increase involved all sectors of activity, particularly mechanical and metallurgical industries, and chemical and parachemical industries.

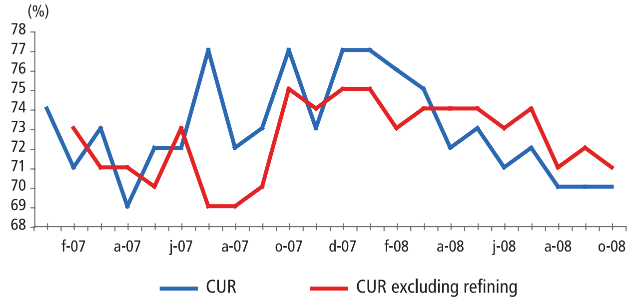
2.2 Pressures on labor market

At the end of quarter three of 2008, labor force aged 15 years and over was 11,298,000 persons, increasing by 1.5 percent compared with the same period of 2007. This is the result of a 2.9 percent growth in urban labor force, and the stagnation of rural labor force. Accordingly, labor force participation rate stood at 50.6 percent, down by 0.2 percentage point.

Employed labor force slightly increased in the third quarter, compared with the same quarter of last year.

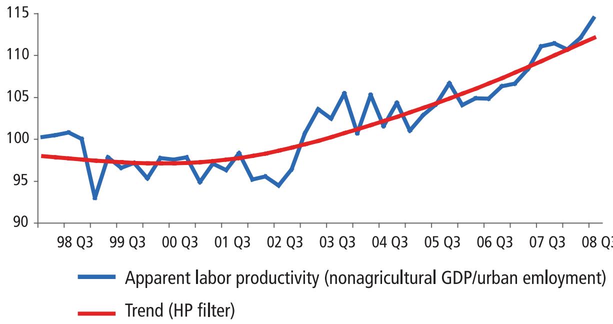
Nonetheless, the employment rate declined by 0.2 percentage point to 45.6 percent, as the growth rate in the number of jobs was slightly below that of labor force aged over 15 years. Per place of residence, employment rate moved up from 37.3 percent to 37.6 percent in urban areas, and declined by 0.8 percentage point to 57 percent in rural areas.

Chart 2.4: Industrial output capacity utilization rate



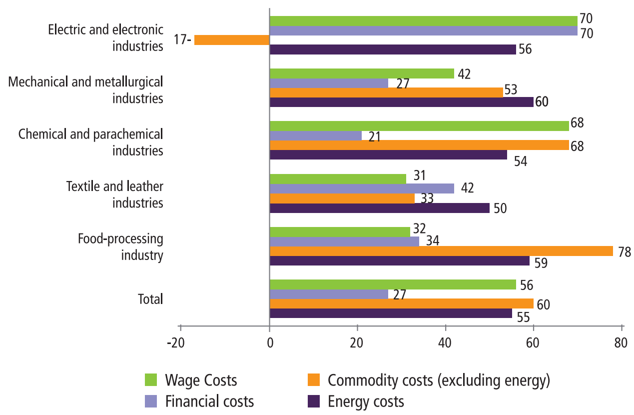
Source: BAM monthly business survey

Chart 2.5: Apparent labor productivity (base 100=1998)



Sources : HCP, and BAM estimates

Chart 2.6: Change in unit production cost components per sector (balances of opinion in % in Q3 of 2008)



Source: BAM monthly business survey

1 Apparent labor productivity is measured by the ratio between output and employed labor force. This indicator must be interpreted with precaution, as it does not take into account the efficiency with which labor force is used in production.

Unemployment rate remained stable around 9.9 percent compared with the same quarter of previous year. However, on the back of the steady growth in nonagricultural activities, job gains primarily concerned urban areas, where unemployment rate went down from 15.9 percent to 15.5 percent. In rural areas, this rate increased by 0.4 percentage point to 3.9 percent.

The most significant decline in urban unemployment rate was observed in the 35-44 age group (-1.1 point) and the 25-34 age group (-0.7 point). In contrast, the only increase in unemployment rate was recorded among young people aged below 25 years, from 16.7 percent to 18.8 percent in the third quarter of 2008. This expansion may be explained by the rise in the cost of youth first recruitment following the upward adjustment of minimum wage as of July 2008.

Net creation of gainful employment stood at 337,000 in the third quarter, compared with 192,000 net losses in unpaid labor. Job gains were essentially concentrated in the sectors of services with 108,000 new jobs (+2.9 percent) and building and public works with 62,000 jobs, up 7.4 percent.

According to the findings of BAM business survey for the third quarter of 2008, total labor force employed in industry grew from one quarter to the next, with a balance of opinion of 14 percent. Except for textile and leather industries which observed a drop in staff due to the decline in exports, the other sectors saw a strengthening in labor force. According to the expectations of corporate managers participating in the survey, this trend would continue in all sectors during the fourth quarter of 2008.

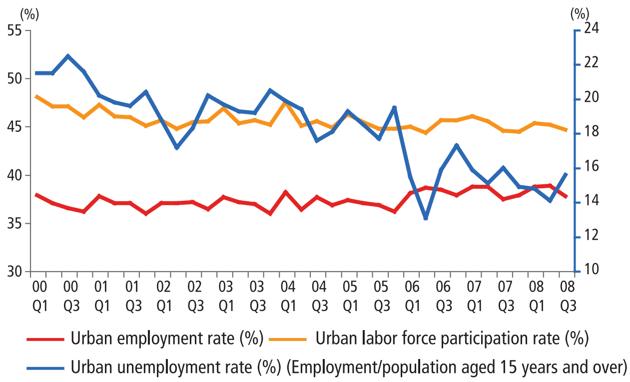
The quarterly average wage index, calculated by the HCP on the basis of CNSS data and in reference to the average wage of the year 2004, recorded in the second quarter of 2008 a rise of 5.5 percent year-on-year and of 5.2 percent compared with the previous quarter. In real terms, this index grew by 0.8 percent from the same period of last year. Similarly, the results

Table 2.1: Activity and unemployment quarterly indicators per place of residence (year-to-year [1])

In millions	Q3 - 2007			Q3 - 2008		
	Urban	Rural	Total	Urban	Rural	Total
Labor force and employment						
Labor force [2]	5.69	5.43	**11**	5.86	5.43	**11.3**
Labor force participation rate (%)	44.4	59.9	**51**	44.5	59.3	**50.6**
Employed labor force	4.79	5.23	**10**	4.95	5.22	**10.2**
Employment rate (%)[3]	37.3	57.8	**46**	37.6	57	**45.6**
Unemployment						
Unemployed labor force	0.9	1.09	**1.1**	0.91	0.21	**1.12**
Unemployment rate (in %)	15.9	9.9	**9.9**	15.5	3.9	**9.9**
By degree						
. Non-graduates	9.5	5.1	**5.1**	8.9	2.6	**4.8**
. Graduates	21.3	19.2	**19**	21.1	12.4	**19.5**

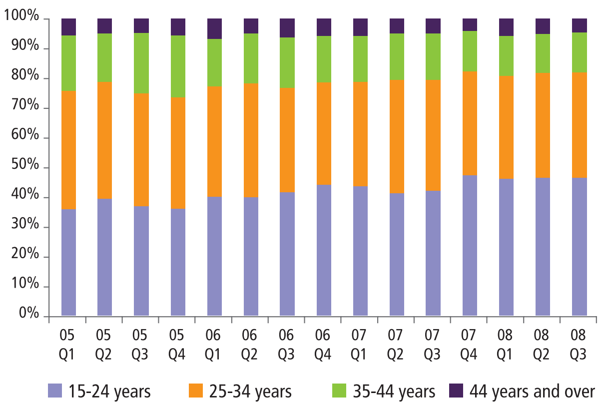
(1) Data adjusted according to the new population forecasts
(2) Population aged 15 years and over (in millions of persons)
(3) Employed labor force/total population aged 15 years and over.
Source: HCP

Chart 2.7: Rates of labor force participation, employment and unemployment in urban areas



Source: HCP

Chart 2.8: Change in unemployment structure by age



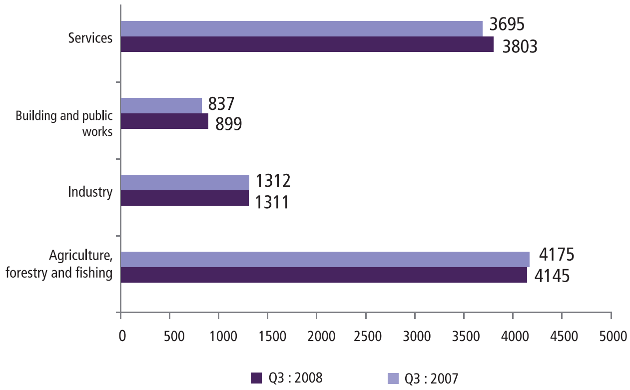
Source: HCP

of BAM business survey in the industry for the second quarter show an increase in wage level with a positive balance of opinion at 24 percent.

In addition, the first phase of the readjustment of minimum wage and public sector wages, following social dialogue between the Government and trade unions, has come into force in July 2008. Thus, the minimum hourly wage increased by 5 percent in the third quarter of 2008, from 9.66 to 10.14 dirhams. It also showed slight rise in real terms, moving up from 5.22 to 5.44 dirhams, after a downward trend that began in the third quarter of 2004.

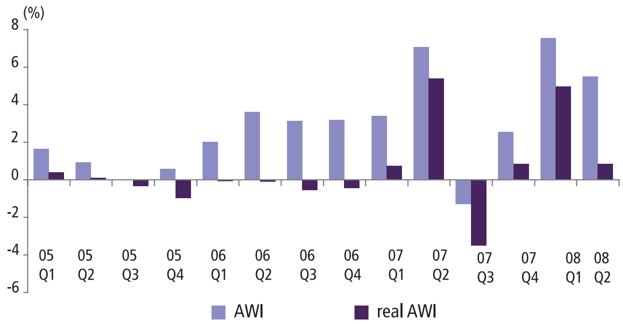
Analysis of these recent trends suggests a likely mitigation of demand pressure on prices over the forthcoming quarters.

Chart 2.9: Net job creation by sector (staff in thousands)



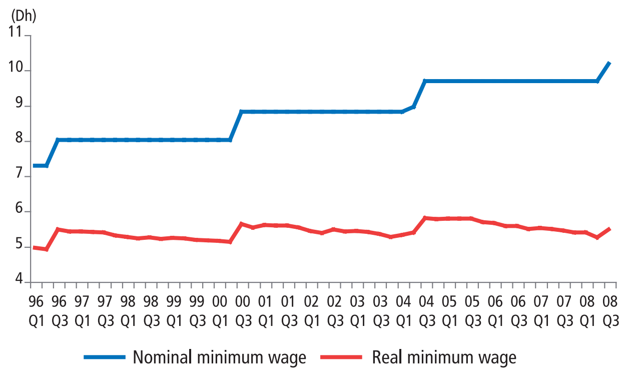
Source: HCP

Chart 2.10: Private sector average wage index in nominal and real terms (year-to-year)



Sources : HCP, and BAM estimates

Chart 2.11: Quarterly minimum wage in nominal and real terms



Source: Ministry of Labor

3. IMPORT PRICES

In October 2008, inflation was down in advanced economies and, to a lesser extent, in the emerging economies. This trend has been reported since August in the majority of these countries. The current international environment is characterized by a sharp volatility in exchange rates and commodity prices as well as by a significant easing of monetary policies by the major central banks, driven by world growth slowdown and deflation risks. The marked slowdown in economic activity is becoming increasingly pronounced in OECD countries, notably in the United States and the Eurozone, coupled with the persisting financial turmoil. The fall in major commodity prices, which started last August, continued through October 2008 and became more marked particularly in oil, the prices of which fell sharply over the recent period, hitting a record low since the beginning of 2007. The current trend in the prices of commodities will contribute to curbing inflation in both advanced and emerging countries. However, inflationary risks persist in many of these countries, due to the fact that the volatility and the continuing high levels of commodity prices as well as the pressures on supply have all led to mounting wage claims. In Morocco, import price index excluding energy, based on the available data of the first eight months of the year 2008 which do not include the recent trends in world markets, increased by 42.8 percent, a level more moderate than the 51 percent registered in July on a year-to-year basis. After the rise in the prices of some fuels in July, subsidized domestic prices remained unchanged. Taken together and bearing in mind the recent context and the outlook for the international economic situation, inflationary pressures stemming from import prices and the overall conditions of global demand are expected to regress over the next quarters as foreseen in the previous MPR.

3.1 World inflation

Amid an international context of severe economic slowdown, which prompted the majority of central banks throughout the world to take substantial measures of monetary easing, the preliminary data published by Eurostat point to a drop in inflation in November 2008 in the Eurozone, to 2.1 percent from 3.2 percent in the previous month.

The easing of inflationary pressures which has been observed since last August became more pronounced in October 2008 in the main developing countries, according to the latest data available (see table 3.1).

In the United States, inflation reached 3.7 percent in October 2008, compared with 4.9 percent a month earlier. In the Eurozone, it stood at 3.2 percent instead of 3.6 percent in September. The same trend was observed in France and Germany with respective rates of 3 percent and 2.5 percent, from 3.3 percent and 4.6 percent. Similarly, in both Spain and Italy inflation rate fell to 3.6 percent from 4.6 percent and 3.9 percent, respectively, in the previous month (see table 3.1).

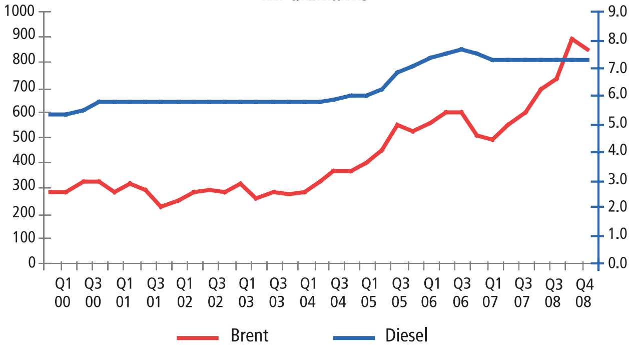
Table 3.1: Recent evolution of world inflation
(year-to-year)

	2007	2008	2008	Forecasts	
	Oct.	Sept.	Oct.	2008	2009
United States	3.5	4.9	3.7	3.1	1.6
Eurozone*	2.5	3.6	3.2	2.9	1.7
Germany	2.5	3	2.5	2.4	0.8
France	2	3.3	3	2.6	1.6
Spain	3.6	4.6	3.6	3.6	2.2
Italy	2.1	3.9	3.6	4.6	1.6

(*) Harmonized indexes

Sources: IMF, Eurostat

Chart 3.1: World oil price and pump price in Morocco, in dirhams

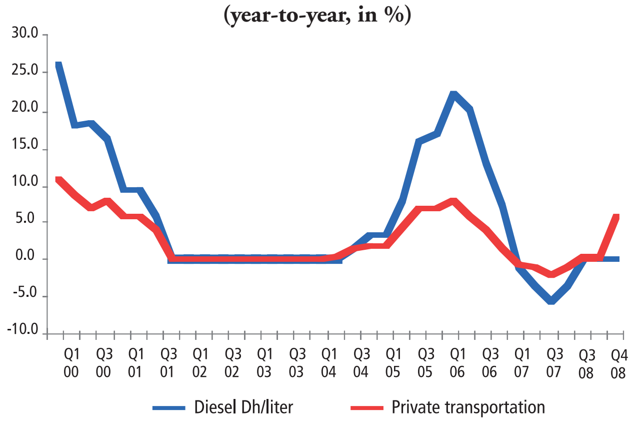


Sources: IMF and Ministry of Energy and Mining

This inflation slowdown was driven by the ongoing strong economic recession and a continued drop in the international prices of commodities and energy products, particularly oil the price of which has fallen sharply since last August. Inflation is expected to continue declining significantly until the end of 2009 in the advanced economies, and to contract more gradually in emerging economies.

In addition, the deteriorating outlook for world economic growth in 2009, as predicted in the November projections of the IMF and the OECD, together with the continued deterioration of global financial conditions and the underemployment of the available resources due to the economic recession in the advanced economies, all suggest that inflationary pressures would continue to ease in the short term.

Chart 3.2: Fuel pump price and transportation price (year-to-year, in %)



Sources: HCP and Ministry of Energy and Mining

3.2 Oil prices

The downward trend in oil prices that began last August continued in November, when the barrel price stood on average at 54 dollars compared with 72.7 dollars a month earlier, down by 25.7 percent from one month to the next.

This drastic shift results from the sharp contraction in energy consumption in the United States and the Eurozone as well as from the downward revision of the economic outlook due to the increasingly pronounced impact of the financial crisis.

However, over the first eleven months of 2008, oil prices on a year-to-year basis settled on average at $102 a barrel, up from $69.5 during the same period of last year.

According to the latest IMF projections of November 2008, the average oil price for the year 2008 was revised downwards to $68 a barrel from the $107.3 expected last October. Also, the OECD latest economic forecasts of November suggest an average oil price of $60 a barrel in 2008. On the futures market, oil price would average $59.7 a barrel in 2009 and $69.3

Table 3.2: Brent price on the futures markets (in US $)

	Q4 2008	Q1 2008	Q2 2009	Q3 2009	Year 2009	Year 2010
Futures	64.9	54.1	57.4	60.9	59.7	69.3

Source: Bloomberg

Table 3.3 : Domestic selling prices of oil products

Products *(Dh/Liter)*	Dec. 2007	Jan. 2007	Apr. 2007	July 2008	Sept. 2008	Nov. 2008
Premium gasoline	10.25	10.25	10.25	11.25	11.25	11.25
Diesel fuel	7.22	7.22	7.22	7.22	7.22	7.22
Diesel 350	9.13	9.13	9.13	10.13	10.13	10.13
Industrial fuel (Dh/Ton)	2874	2874	2874	3374	3374	3374

Source: Ministry of Energy and Mining

a barrel in 2010 (see table 3.2). Nonetheless, the growth forecast of the international oil market depends on the future developments of the global economic and financial conditions.

These predictions suggest, on the one hand, risks of severe economic recession in 2009 for the majority of the advanced countries, and on the other hand, a longer, indefinite period before a general return of confidence to market investors.

This volatile context surrounded by great uncertainty should continue in the short term to originate in downward pressures on global demand for commodities, and for energy in particular.

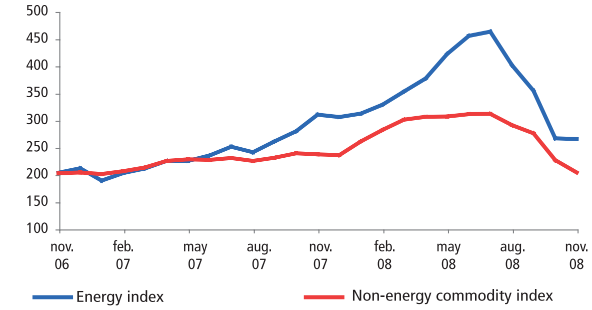
In Morocco, after the upward adjustment of some types of fuel in July, the domestic prices of diesel, the main fuel used in transportation, remain buffered against fluctuations in world prices through the support of the Subsidization Fund.

3.3 Commodity prices

Prices for non-energy commodities continued to fall, mostly driven by the slowdown in world economic growth and dollar appreciation. However, current commodity prices remain at high levels compared with the previous year.

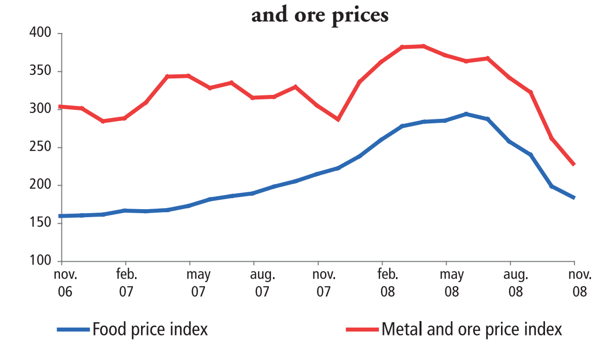
Over the first eleven months of 2008, World Bank commodity price index excluding energy, covering the developing countries, on average remained 24.9 percent higher than the same period of last year. In contrast, the monthly development suggests that the index would fall in November by 10.1 percent, compared with the previous month. This trend affected food products, the index of which declined on average by 7.2 percent. Indeed, wheat price dropped by 4.5 percent from one month to the next, due chiefly to the promising-looking harvest of the 2008-2009 crop year. The latter is expected to restore balance between supply and demand, and therefore significantly improve the replenishment of wheat stocks of the major exporting countries which have already announced some upward adjustments of their

Chart 3.3: Index of energy and non-energy commodity prices



Source: World Bank

Chart 3.4: Index of food, metal and ore prices



Source: World Bank

Table 3.4: Change in wheat futures and forecasts

Wheat *(USc/bushel)*	Q4 2008	Q1 2008	Q2 2009	Year 2009
Futures	555.09	570.25	570.25	585.41
Forecasts	676.50	702.50	688.00	680.96o

Source: Bloomberg

short-term stock estimates. Under the impact of these same factors, the price for corn and barley declined by 10.5 and 9.3 percent, respectively, from one month to the next. Nevertheless, on the average of the first eleven months of 2008, wheat price remained 31.5 percent higher than the level reported in 2007, that of corn 39.9 percent and barley 20.8 percent.

Metals and ores price index also went down by 12.7 percent in November compared with the previous month, mainly owing to the impact of slowing global growth on the demand for these products. This decline has particularly concerned the prices for copper, zinc and lead, which fell by 24.5 percent, 11.4 percent and 12.8 percent, respectively, from one month to the next. Similarly to food price index, the upward change in metals and ores price index over the first eleven months of 2008 remained 7.3 percent higher than the previous year. This change reflects, in part, a rise in the average prices for iron, steel and copper by 66 percent, 58.4 percent and 2.7 percent, respectively, compared with the levels reported in 2007. It also includes a fall by 15 percent and 40 percent in the prices for lead and copper, respectively.

In the latest IMF forecast, the prices of non-energy commodities were significantly revised downwards and should remain volatile under continuing bleak growth outlook and financial market turmoil at the global level. Food prices would continue to fall, as harvest of the 2008/2009 crop year and stocks would be better than expected. Furthermore, the continuing downward trend in oil prices should lead to a drop in the prices for fertilizers. It would also redirect demand for biofuels downwards, thus allowing a drop in food prices. However, world demand for food products is likely not to be affected, to a large extent, by the trend reversal in world economic growth.

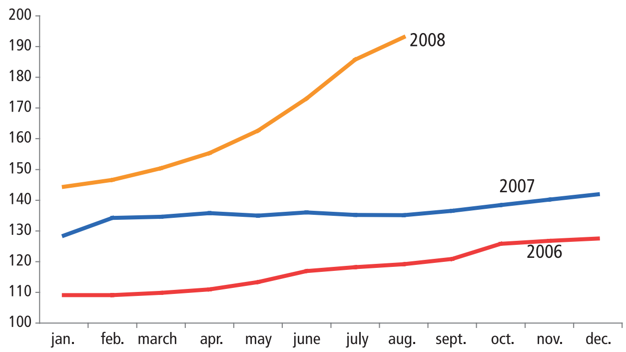
Being closely linked to the level of investments, particularly in the building sector, the change in demand for metals will depend on growth forecasts which suggest a slowdown in world economy. As a result, metal prices are projected to continue their downward trend during the next quarter.

3.4 Import price indexes

In August 2008, import price index (IPI) excluding energy rose by 3.9 percent compared with July, making a slight increase (of 3.4 percent) from one month to the next. This change is linked to the rise in the IPI of mineral and semifinished products, as food products IPI virtually stabilized in August. On a year-to-year basis, non-energy IPI increased by 42.8 percent, a level more moderate than that of July (+51 percent). The downward trend of commodity prices appears to be the cause of the gradual slowdown of that index.

Year-to-year increase in food import price index stabilized in August at 26 percent, a trend similar to that of the previous month.

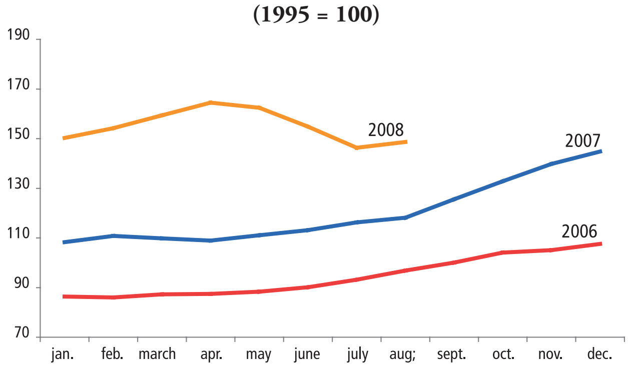
Chart 3.5: Non-energy import price index (1995 = 100)



Sources: Foreign Exchange Office, and BAM calculations

Chart 3.6: Food import price index

(1995 = 100)



Sources: Foreign Exchange Office, and BAM calculations

Box 3.1: Volatility of world commodity prices

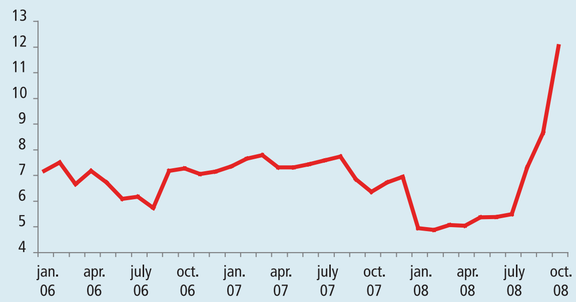
Over the first ten months of 2008, the change in commodity prices was marked by volatility at variant degrees depending on the category of products. Indeed, a surge in prices, with elevated levels in some products, was observed in the first half of 2008. Then followed a period of price downturn that lasted until November 2008.

The run-up in commodity prices is primarily driven by imbalance between inadequate supply and a strongly steady demand, dollar weakness and interest-rate easing in the United States, which encouraged investment funds to move heavily into the commodity markets. The reversal of trend, however, reflects the noticeable downturn in the growth of emerging and developing economies, as well as the improvement in supply conditions and in world stocks of major commodities.

Oil prices showed elevated volatility, which reached 36.5 percent in the first ten months of 2008, up from 6 percent in 2007. On average, oil prices peaked in July at 133 dollars a barrel, and then rapidly fell by 45.3 percent in the subsequent three months, to settle at 73 dollars a barrel in October. Such severe volatility is attributable to the irregular trend in the dollar exchange rate. Actually, the change in the dollar and in oil prices reveals a reverse correlation between these two variables.

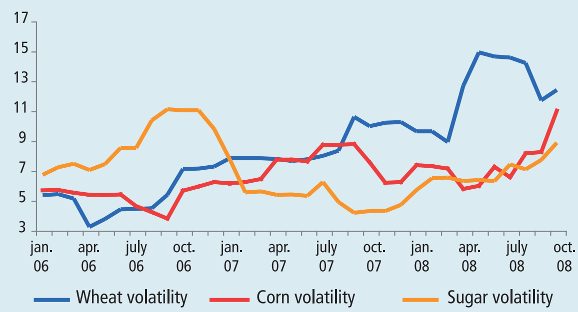
Cereal prices were also volatile during the first ten months of 2008. Volatility in wheat prices was higher than in other cereals, at 26 percent, a level similar to that reported in the same period of last year. Wheat prices were at their peak in March with 419.6 dollars a ton, but decreased thereafter to their lowest level of 185.9 dollars a ton in October, down by 55.7 percent in 7 months.

Chart B 3.1: Change in oil volatility



Sources: World Bank, and BAM calculations

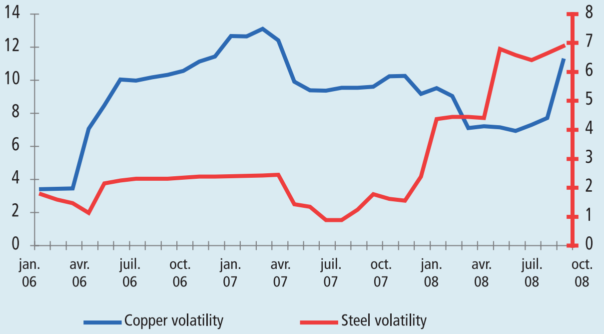
Chart B 3.2: Volatility of major food products



Sources: World Bank, and BAM calculations

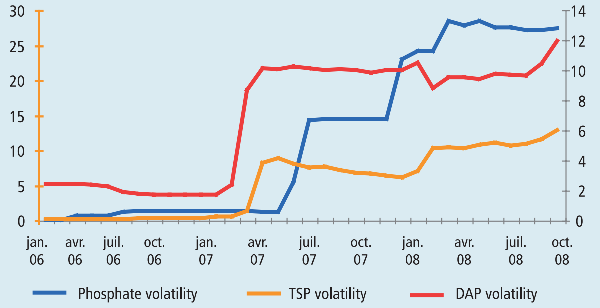
Metal prices followed an irregular trend marked by two phases: an upswing phase over the first five months of 2008 and then a downswing period. In 2008, iron prices, fixed in the beginning of each year, were 66 percent higher than previous year. The upward trend in steel price index continued through the year and has slightly moderated since September. Copper price volatility persisted throughout the first ten months of 2008, rising to 18 percent, from 3 percent in the same period of 2007. Copper price reached its highest level in April, and later declined on average by 43.3 percent until October.

Chart B 3.3: Copper and steel volatility



Sources: World Bank, and BAM calculations

Chart B 3.4: Volatility of phosphates and derivatives



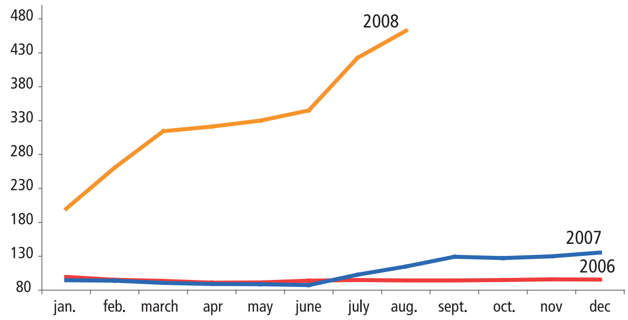
Sources: World Bank, and BAM calculations

Prices for phosphate and its derivatives experienced a surge, owing primarily to increased production of biofuels which stimulate world demand. The average prices of phosphate and Triple Superphosphate (TSP) reached their record high in August at 430 dollars a ton and 1131.5 dollars a ton, respectively, while those of Diammonium phosphate (DAP) in April at 1200.6 dollars a ton. However, since September, prices of phosphate and its derivatives have been experiencing a trend reversal. In October, phosphate average price declined by 3.7 percent compared with the previous month, that of TSP by 14.7 percent and DAP by 19.2 percent, compared with the peaks registered since the beginning of the year.

On a monthly basis, the growth of this index saw a deceleration. However, the growth rate of import prices of corn, sugar and butter remain, from one month to the next, relatively higher than those of other food products. Likewise, milk import price rose, from one month to the next, in response to the increase in livestock feed prices during the previous months.

The increase rate of mining products' IPI slowed in August, compared with the previous month. Nevertheless, on a year-to-year basis, the index increased noticeably, driven primarily by the still ongoing sharp rise in the import price of sulfur, an essential input in the production of phosphated products. Iron price also contributed to that rise, given that its initial price fixed early this year was 66 percent higher than that of 2007. These trends should therefore continue to keep the IPI on the uptrend in the months to come.

Chart 3.7: Import price index of mining commodities



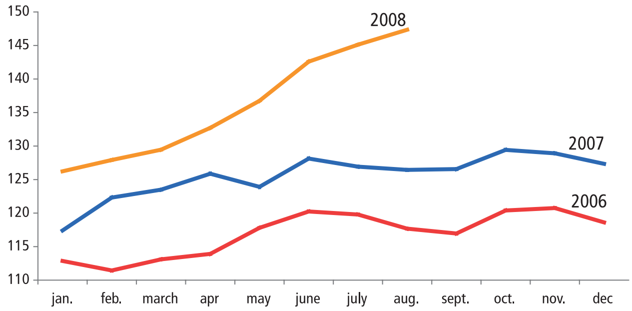
Sources: Foreign Exchange Office, and BAM calculations

In August 2008, the IPI of semifinished products showed a more moderate rise than that of the previous month. However, it achieved a significant growth at an annual rate, mostly because of the rise in the import prices of such products as paper, wood and, more particularly, plastics.

This trend might continue, given the high demand for imports of semifinished products particularly from the processing industries.

As expected by the latest MPR, the inflationary pressures so far exerted on import prices would ease during the remainder of 2008. They would yet remain elevated compared with the previous year.

Chart 3.8: Import price index of semifinished products



Sources: Foreign Exchange Office, and BAM calculations

4. MONETARY CONDITIONS AND ASSET PRICES

The data of the third quarter and October 2008 confirm the gradual slowdown in money creation. This trend caused the monetary surplus accumulated by nonfinancial agents to become virtually nil, suggesting an easing of monetary-driven inflationary pressures in the months to come. Bank credit maintained momentum, with an annual growth rate of 26.5 percent in the third quarter and in October, mostly driven by lending to businesses in the form of cash advances, as well as by equipment loans and advances to real estate developers. This trend should however slow down during the next five quarters, as indicated by the findings of BAM quarterly survey among banks, which expect an annual rate of 23 percent at end of 2008 and 16 percent at end of 2009. As to the interest rates applied by banks to transactions with customers, the conclusions of BAM survey for the third quarter of 2008 show a slight increase in lending rates. At the same time, deposit rates posted a rise in the third quarter and in October, concurrently with banks' persisting need for liquidity and the slowdown in the growth rate of non-interest bearing deposits, particularly of demand deposits. Stock market assets fell sharply at the end of quarter three 2008 and continued to decline in October and November. In the period under review, the dirham appreciated against the euro and depreciated against the US dollar, thus following a trend opposite to that observed in the previous quarter.

4.1 Monetary conditions

4.1.1 Interest rates

At its meeting of September 23, 2008 the Board of Bank Al-Maghrib decided to raise the key rate by 25 basis points to 3.50 percent. Against this backdrop, the interbank rate on average went up from 3.21 percent in the second quarter to 3.33 percent in the third, and 3.65 percent in October and November.

Meanwhile, short-term Treasury bills issued at auction went upwards, reflecting a reversal of the trend observed since early this year. The upward trend was equally noticeable on the secondary market both for short-term maturities whose yields remain close to those of the primary market, and for rates on medium and long-term bills.

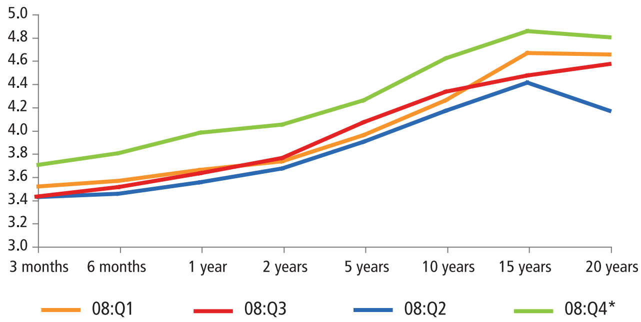
As for deposit rates, the weighted average rate of 6 and 12-month deposits continued its upward trend in the third quarter and in October 2008, primarily in response to the rise in 12-month deposit rates.

During the third quarter, lending rates broadly maintained the average level observed last year. The findings of Bank Al-Maghrib quarterly survey among banks suggest a rise in the weighted average rate, in response to the increase in rates on cash advances, equipment loans and, to a lesser degree, real estate loans. On the other hand, rates on consumer loans continued the downward trend that began early this year.

Table 4.1: Change in short-term TB yield rates on the primary market

	2007				2008			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	October
13 weeks	2.73	3.30	2.29	3.63	3.58	3.41	3.42	3.70
26 weeks	2.85	3.34	3.32	3.58	3.59	-	-	3.80
52 weeks	2.97	3.88	3.40	3.55	3.62	3.53	3.51	3.86

Chart 4.1: Change in maturity structure of secondary market TB interest rates*



** Observation of the fourth quarter of 2008 corresponds to the daily average of the period from October 3 to November 19, 2008.*

Table 4.2: Deposit rates * (time deposits)

				2008			
	Q2	Q3	Q4	Q1	Q2	Q3	October
6 months	3.52	3.41	3.49	3.37	3.55	3.50	3.62
12 months	3.63	3.69	3.71	3.71	3.82	3.89	4.18
Weighted average	3.58	3.60	3.62	3.56	3.72	3.77	4.05

** Quarterly data are simple averages of monthly data*

4.1.2 Money, credit and liquid investments

M3 growth

Money creation slowed down again in the third quarter, causing nonfinancial agents' surplus money to fall virtually to nil.

After posting an annual growth of 12.4 percent in the third quarter of 2008, down from 13.4 percent in the previous quarter, the M3 aggregate showed a one-time monthly drop in October, bringing down its annual growth to 9.3 percent, because of the contraction in the public sector's time deposits (see Box 4.2). Excluding this sector, time deposits registered an annual growth of 13.2 percent, reflecting the continuing switching from cash holdings to remunerated assets, thus leading to the slowing growth in time deposits, the annual rate of which fell back to 8.7 percent in October.

Chart 4.2: Change in lending rates

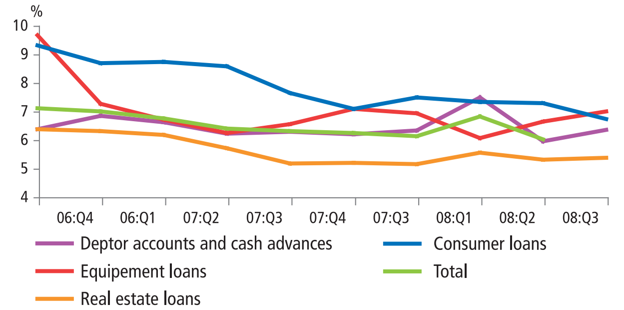
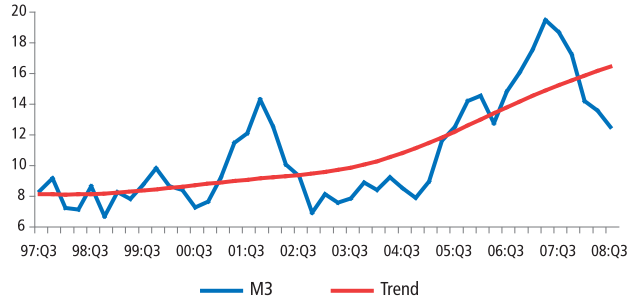


Chart 4.3: M3 annual growth and trend (in %)



Box 4.1: Liquidity and implementation of monetary policy

During the third quarter of 2008, the expansive trend in autonomous factors was reversed, due primarily to the rise in demand for banknotes, and the speed-up in foreign currency purchases by commercial banks. Autonomous factors exerted a restrictive effect of 8 billion dirhams on banks' cash holdings, and the increase in required reserves totaled 1.4 billion dirhams. As a result, banks' liquidity shortage stood on average at 10.4 billion dirhams in the third quarter of 2008, up from 8.4 billion the previous quarter.

Net withdrawals of notes and coins totaled 6.4 billion dirhams in summer and operations on foreign assets led to a contraction in banks' cash holdings by 5.2 billion dirhams. Foreign currency purchases by commercial banks reached 20 billion dirhams, due primarily to the Eurodollar's increased volatility. However, these foreign currency purchases were in part offset by sales of foreign banknotes, whose pace accelerates during summer vacations, making an amount of 14.9 billion dirhams. On the other hand, Treasury operations triggered a liquidity injection of 3.6 billion dirhams, chiefly in response to the reduction of Treasury's debt to the banking system.

Chart B 4.1: Change in liquidity position (in millions of dirhams) and in weighted average rate (%) in quarterly average

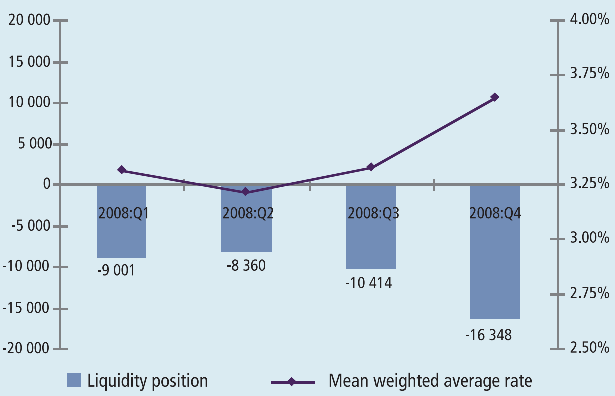


Chart B 4.2: Liquidity position (in millions of dirhams) and weighted average rate of the interbank money market

In the last quarter of 2008, the restrictive impact of autonomous factors persisted, driven in particular by the contraction in Bank Al-Maghrib's net foreign assets. As a result, banks' liquidity shortage went up from 10.4 to 16.4 billion dirhams, from one quarter to the next.

Foreign currency purchases by commercial banks totaled 16.9 billion dirhams, owing to the increased volatility in international markets amid the global financial crisis. Moreover, the sales of foreign banknotes, showing a sharp fallback compared with the previous quarter, amounted to 3.7 billion dirhams. The restrictive effect of net foreign assets on liquidity was of 13.2 billion dirhams.

In contrast, Treasury operations caused a liquidity injection of 5.3 billion dirhams, chiefly attributable to subsidization costs. In fact, Treasury expenditure increased to 42.3 billion dirhams, 7 billion of which correspond to repayments of domestic debt to the banking system and nearly 7.3 billion for the costs of the Subsidization Fund. Treasury receipts totaled 37 billion dirhams, 9.6 billion of which come from bank's subscriptions to Treasury bill auctions.

Currency in circulation had almost no impact on banks' cash holdings over this quarter, increasing by only 218 billion dirhams.

Overall, autonomous factors exerted a restrictive effect of 7.7 billion dirhams on banks' liquidity. Moreover, the amount of required reserves increased by 203 billion dirhams, with almost no effect on banks' liquidity.

Chart B 4.3: Change in reserve requirements (in millions of dirhams)

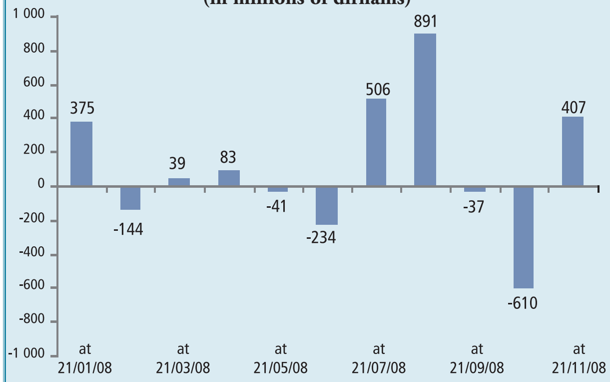
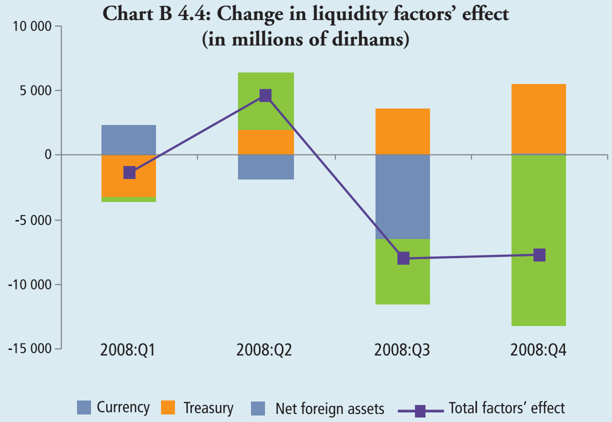


Chart B 4.4: Change in liquidity factors' effect (in millions of dirhams)



In response to banks' liquidity shortage, which averaged 16.4 billion dirhams during this quarter, Bank Al-Maghrib used various instruments of monetary policy to bolster liquidity, providing an average daily amount of 16.6 billion dirhams. 82 percent of this amount, or 13.6 billion dirhams, were allotted through the 7-day advances.

Given the structural nature of liquidity shortage, BAM also conducted foreign currency swap operations, with an average daily amount of 2.6 billion dirhams, accounting for 16 percent of the overall amount of liquidity injections.

Chart B 4.5: BAM interventions on the money market (in millions of dirhams)

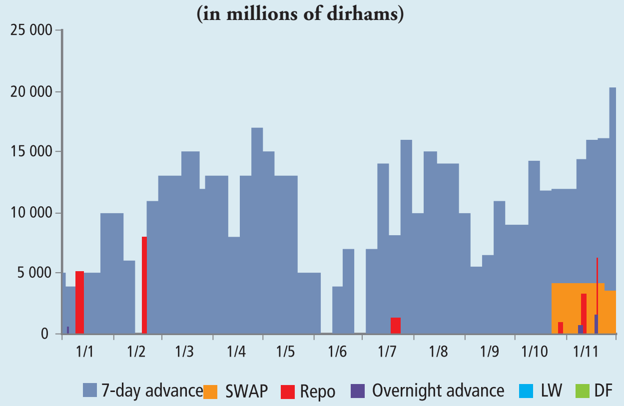
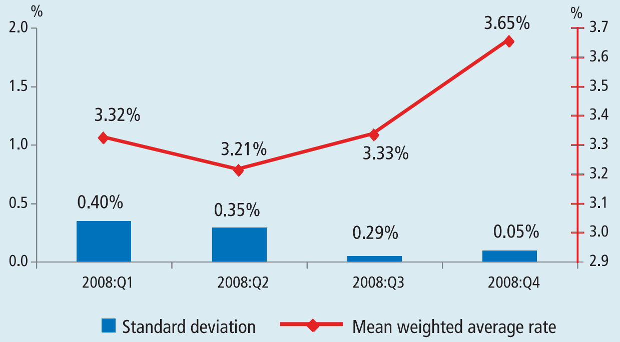


Chart B 4.6: Change in the mean and standard deviation of the interbank market weighted average rate



In an effort to contain the upward pressure underwent by the interbank rate primarily during November, Bank Al-Maghrib carried out fine-tuning operations in the form of TB repurchase agreements for an average daily amount of 315 billion dirhams (2 percent of the total amount of interventions). Moreover, overnight advances to banks totaled 89 billion dirhams on a daily average.

During this quarter, the mean weighted average rate settled at 3.65 percent, up by 32 basis points compared with the previous quarter, on account of the following:

- The Bank Board decision of September 23 to raise the key rate to 3.50 percent;
- The increase in banks' liquidity shortage;
- Increase in some banks' funding needs
- Inadequate collateral in some banks.

Consequently, the volatility of the weighted average rate rose by 5 basis points, from 0.05 percent to 0.10 percent.

Per type of depositor, the structure of demand accounts shows that the slowdown involves all nonfinancial agents, particularly businesses whose holdings in banknotes and coins increased only by 3.5 percent on a year-to-year basis, compared with 4.2 percent in the third quarter. Similarly, the annual growth rate of demand deposits held by private individuals fell back to 6.9 percent in October, down from 10.6 percent in the third quarter of 2008.

Chart 4.5: Annual growth of M3 components (in %)

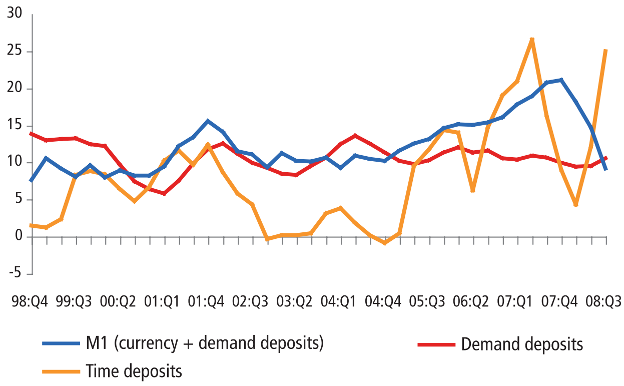


Chart 4.4: Money surplus (in percentage of M3 and M1 equilibrium outstanding amount in real terms)

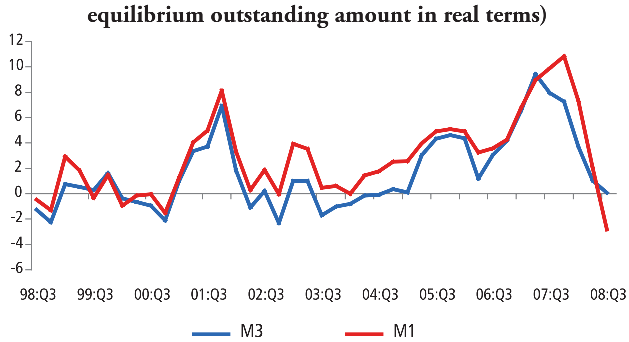
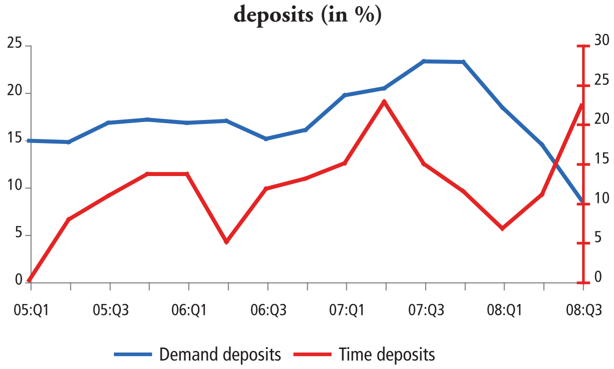


Chart 4.6: Annual change in nonfinancial agents' demand deposits (in %)



Bank loans

After its exceptional increase as of the third quarter of 2006, followed by stabilization at a high level of 28 percent between the third quarter of 2007 and the second quarter of 2008, the annual growth rate of bank loans11 slightly decelerated to 26.5 percent in the third quarter and in October.

The breakdown of bank credit per economic agent points to a slowdown in loans offered to private individuals. Loans to businesses remained, however, virtually stable. On their turn, loans to the public sector were substantially high in October, driven by the financial loan granted by a banking consortium to the OCP (see Box 4.2). Excluding this transaction, the annual growth of bank loans remains rapid, at 25 percent.

Analysis by economic purpose indicates that, despite the slight deceleration observed in the third quarter and in October, all loan categories maintained momentum.

The growth rates in real estate loans and consumer loans, which stood in 2007 at a level much higher than the overall growth of loans, continued their gradual slowdown, though at a weak extent, to settle at 34.4 percent and 32 percent, respectively, in October. However, cash advances and equipment loans, mostly granted to businesses, do not seem to follow any major deceleration trends. Their growth rate has indeed remained close to the overall growth rate of bank loans.

The decline in loans' distribution in the third quarter and in October 2008 spells the beginning of a slowdown cycle that is expected to continue through the forthcoming year, to bring bank loans' growth rate closer to that of nominal economic growth. Indeed, according to the findings of Bank Al-Maghrib half-yearly survey among banks' directors general, the annual growth of credit would settle at 23 percent at the end of December

1 [1] Bank credit data provided in this Report differ from those published in monetary statistics. Indeed, accounting treatments have been recently carried out to specify the distribution of loans per economic object by means of reclassifying some loans granted to real estate developers under heading «Real estate loans». In addition, the loan granted to the OCP to finance the outsourcing of its internal pension fund was reclassified under the heading "Others" instead of "Equipment loans".

Chart 4.7: Bank loans' annual growth and trend (in %)

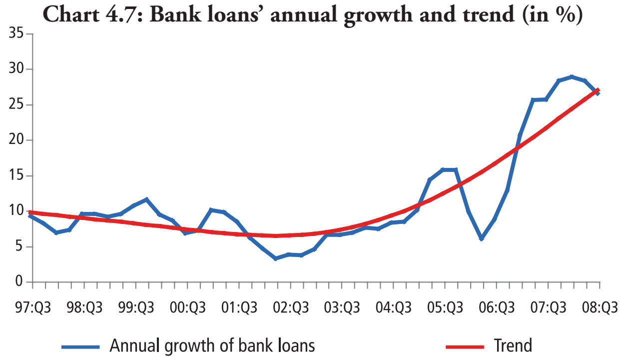


Chart 4.8: Loans' structure per economic agent (in billions of dirhams)

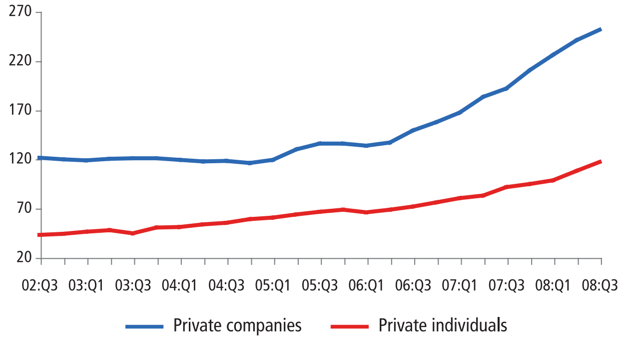
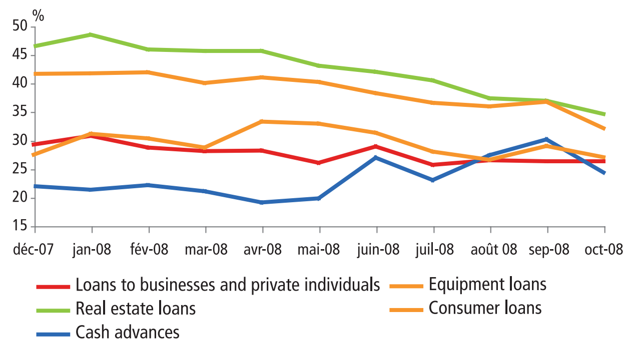


Chart 4.9: Annual change in the different loan categories



2008, down from 29 percent in 2007, and would later fall back to 16 percent in 2009.

The expected deceleration would involve all loan categories, except for equipment loans which, after posting a weak increase during the last two months of 2008, would again show a marked expansion in 2009 and end the year at a level 26 percent higher than that of December 2008.

Other sources of money creation

Net foreign assets followed their downward trend observed since the fourth quarter of 2006. They recorded a significant deceleration in the third quarter of 2008 before declining by 3.2 percent, on a year-to-year basis, at the end of October, the first-ever decline in several years. This trend, which covers a drop in Bank Al-Maghrib NFA and a sharp contraction in banks' NFA in October, largely reflects a further widening in trade deficit and the contraction of tourist receipts and remittances of Moroccans living abroad.

The level of net claims on Government, despite the one-time increase registered in October, remained 7.3 percent lower than that reached as at end October 2007, chiefly under the effect of reduction in the Treasury debt to banks during the first three quarters.

The month of October was also marked by the significant increase in banks' nonmonetary assets, particularly financial borrowings. That occurred when a large share of public sectors' time deposits was withdrawn from monetary circulation (see Box 4.2) and invested again with banks in the form of assets not included in the money supply.

Liquid investments

At the end of October 2008, liquid investments' outstanding amount was 4.6 percent higher than same period of 2007, in spite of the falls observed over the last two months.

During the third quarter, the change in liquid investments was again marked by the growth in the securities of monetary UCITS the outstanding amount of which reached 22.7 billion, almost 50 percent of the overall UCITS securities held

Table 4.3: Projected change in bank loans

	Amounts outstanding in billions of DH				Change (year-to-year in %)			
	dec. 07	oct. 08	dec. 08	dec. 09	oct. 08 / oct. 07	dec. 07 / dec. 06	dec. 08 / dec. 07	dec. 08 / dec. 09
Amounts outstanding	**422.6**	**506.1**	**518.7**	**602.5**	**26.1**	**29.1**	**22.7**	**16.2**
Loans to finance companies	42.0	49.0	50.8	55.3	23.2	49.9	20.9	9.0
Cash advances	115.9	140.7	145.1	168.0	24.2	21.8	25.2	15.8
Equipment loans	81.4	93.6	96.9	121.9	26.8	27.3	19.1	25.7
Consumer loans	19.7	24.6	25.8	33.0	32.0	41.4	31.2	28.1
Real estate loans	119.9	149.0	153.0	176.3	34.4	46.3	27.7	15.2
Nonperforming loans	33.3	31.4	31.0	31.7	-9.7	-6.4	-6.8	2.2
Other loans	10.4	17.9	16.0	16.1	73.9	18.8	53.3	0.9

Source: Banks' forecasts, and BAM survey

Chart 4.10: Annual growth of net foreign assets (in %)

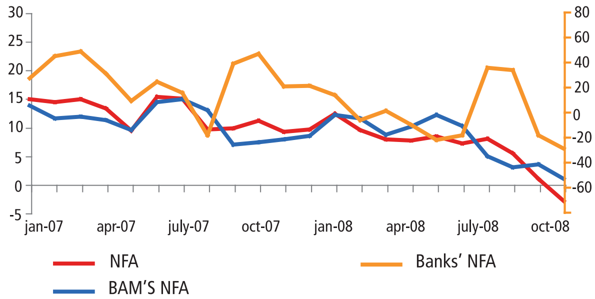


Chart 4.11: Quarterly change in net claims on the Government (in billions of dirhams)

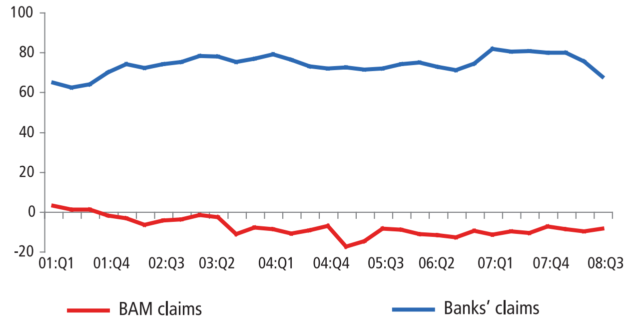
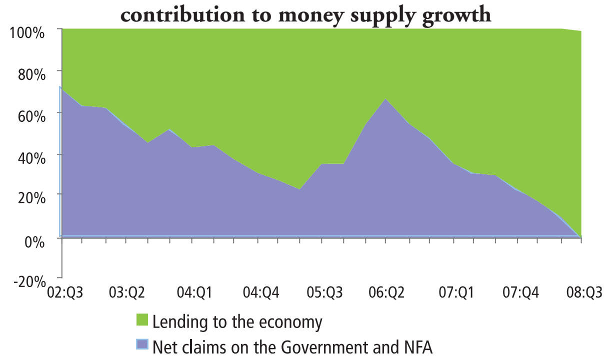


Chart 4.12: Main counterparties' relative contribution to money supply growth



Box 4.2: Outsourcing of OCP internal pension fund: the impact on money and its counterparts

The outsourcing of the OCP internal pension fund to the Collective Scheme for Retirement Allowances (RCAR), branch of the CDG, for an amount of 28 billion dirhams, was implemented on October 21, 2008.

This operation was financed up to 21.1 billion dirhams by the OCP's own resources - through the appropriation of a part of its time deposits and the purchase of UCITS securities, while the remainder was obtained through bank loans. In order to avoid any impact on banking liquidity, the refund by the CDG of about 90 percent of the overall amount to the banking system was conducted on the same time in coordination with Bank Al-Maghrib and the OCP, through repurchase agreements.

However, in view of the noticeable changes underwent by the structure of the banking balance sheet as a result of this operation, the impact on the money supply and its counterparts was significant. Thus, between September and October M3 fell by 5.8 billion, and banks' nonmonetary liabilities increased by about 11 billion. At the same time, bank loans recorded a monthly increase of 2.7 percent. Finally, monetary UCITS, which had been up almost continuously for many quarters, fell by 3 billion in October.

by nonfinancial agents. The increasing yields of these instruments on the money market and their rather liquid nature seem to be the reason behind their preference over bond UCITS securities whose outstanding amount fell back to 18.7 billion from 25.9 billion a year earlier.

The momentum in monetary UCITS securities was however shortly interrupted in October, as their outstanding amount decreased by 3 billion from one month to the next. Similarly to time deposits, this fallback resulted from the withdrawal by the OCP of a large part of its interest-bearing investments to fund the outsourcing of its pension fund.

Securities of equity and diversified UCITS continued to slow down. In the third quarter of 2008, they registered an annual growth rate of only 4.9 percent before falling sharply by 20.6 percent between September and October, due to the lackluster performance of prices on the Casablanca stock market.

4.1.3 Exchange rates

At the end of quarter three of 2008 and in comparison with the previous quarter, the national currency on average appreciated by 0.88 percent against the pound sterling, 0.62 percent against

Chart 4.13: Annual change in liquid investments (in %)

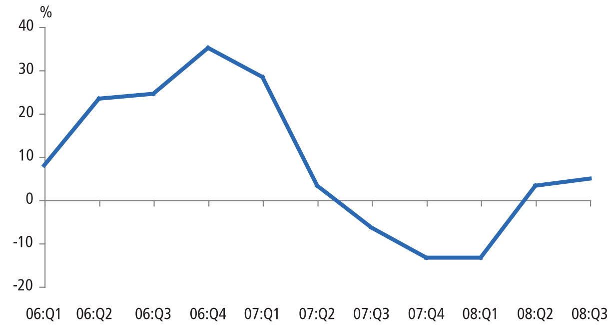


Chart 4.14: Change in monetary and bond UCITS securities (in millions of dirhams)

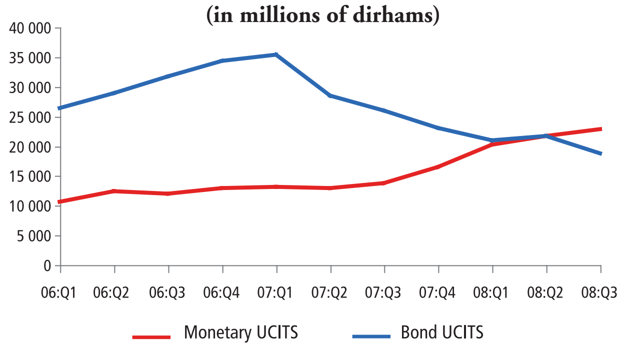
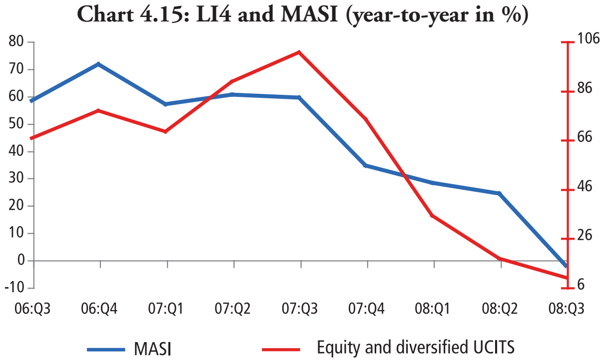


Chart 4.15: LI4 and MASI (year-to-year in %)



the euro and 0.59 percent against the Swiss franc. On the contrary, it depreciated by 3.20 percent against the dollar and 0.49 percent against the yen.

This trend continued through October and November. The national currency on average was 2.56 percent up against the euro and 11.36 percent down against the dollar.

The dirham nominal effective exchange rate, based on bilateral exchange rates with regard to Morocco's major partners, remained almost stable compared with the previous quarter. However, the unfavorable trend in the inflation differential led to a very slight rise in the real effective exchange rate of 0.17 percent compared with the last quarter.

4.2. Asset prices

At the end of the second quarter of 2008, the MASI index and the real estate index dropped substantially by 12 percent and nearly 21 percent, respectively, compared with the previous quarter. Therefore, their performance since the turn of the year fell to -1.6 percent and -6.7 percent. At the end of October and November, both indexes continued their downward trend, falling by 11 percent and 19.1 percent, respectively.

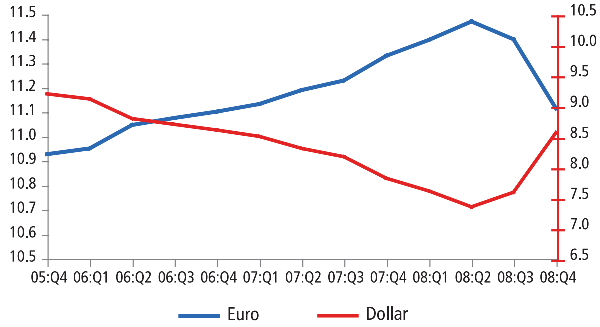
The volume of transactions increased by 6.2 percent to 43.8 billion dirhams. At the end of the first two months of the fourth quarter, stock market turnover did not exceed 32.4 billion dirhams.

Stock market capitalization declined by 9.4 percent to 598.6 billion dirhams. At the end of November, it continued its downward trend to settle at 543.6 billion dirhams.

PER on the Casablanca stock market fell from 20.1 to 17.7 from one quarter to the next, in connection with the depreciation of prices. This level yet remains higher than that reported in foreign stock markets, particularly in the emerging economies.

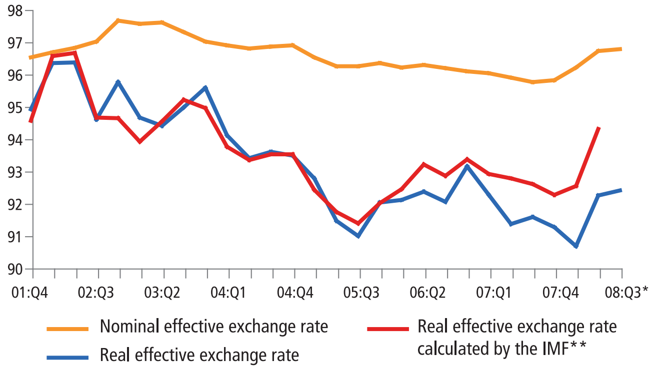
Concerning real estate assets, the fragmented information available suggest that the sector seems to undergo some stagnation in prices, particularly for luxury homes.

Chart 4.16: Exchange rate of the dirham (monthly averages)



** 2008: Q4 corresponds to the arithmetic average of October and November data.*

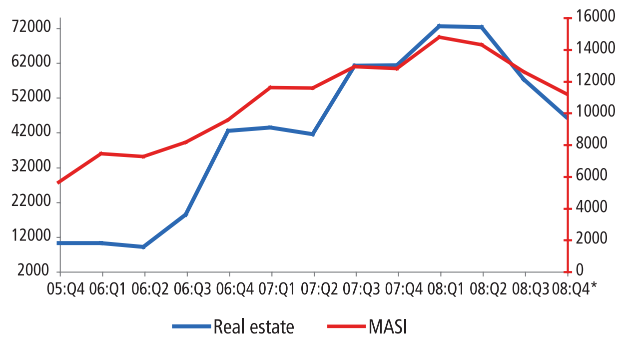
Chart 4.17: Effective exchange rate *
(Base 100 in 2000)



** Provisional data*
*** Data of 2008 quarter 2*

Sources: IMF, and BAM calculations

Chart 4.18: Stock market indexes *



** 2008: Q4 closes at the end of November 2008*

Table 4.4: Equity markets' PER

PER	07 :Q3	07 :Q4	08 :Q1	08 :Q2	08 :Q3
South Africa	13.12	12.38	12.71	13.36	9.76
Argentina	20.63	19.17	2.58	2.61	8.94
Egypt	15.62	18.54	15.87	14.7	13.28
Euro stoxx 50	12.9	12.5	10.5	11.14	9.45
Hungary	13.5	13.2	10.36	9.13	7.51
Morocco	**22.9**	**22.2**	**21.2**	**20.1**	**17.7**
Taiwan	22.57	20.26	18.36	12.91	9.58
Turkey	16.06	17.33	8.36	6.89	6.96

PER: Price Earnings Ratio
Sources: Bloomberg and CFG (Morocco PER)

5. RECENT INFLATION TRENDS

The downward trend observed in both headline inflation and core inflation since last August confirms BAM forecasts that projected a slowdown in the growth rate of the general level of prices after the third quarter of 2008. In fact, after having peaked at nearly 4.6 percent in the second quarter of the year, headline inflation saw a deceleration in the last three months, falling from 4.8 percent in August to 3.9 percent in September and then to 3.5 percent in October. Core inflation followed the same downtrend, as it fell from 4.9 percent in the second quarter to 4.4 percent, 3.5 percent and 3.4 percent in the past three months, successively. Recent price trends were mostly driven by the prices of tradables, particularly food staples, the prices of which were impacted by the drop in the international prices of commodities. Nontradables' price rise remained almost unchanged around 2.6 percent, as the spread effect of tradable input prices to nontradables has started to stabilize over the past three months. The prices for fresh produce have also contributed to reducing inflation, because of the marked deceleration of their growth rate since last August. The downward trend of inflation is also confirmed by the evolution of producer prices, which were affected by the overall depreciation in the prices for oil and imported non-energy commodities.

5.1 Inflation trends

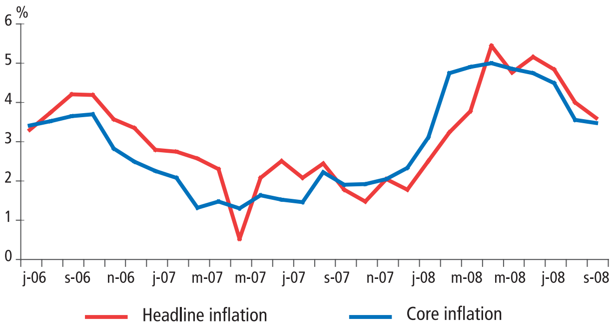
Over the past three months, year-to-year headline inflation continued to slow down, falling from 4.8 percent in August to 3.9 percent in September and then to 3.5 percent in October 2008. This trend mainly results from the deceleration of food staple prices between August and October. It is also attributable to the slowdown in the price rise of fresh produce for the third month in a row. Core inflation substantially decelerated between August and September, decreasing from 4.4 percent to 3.5 percent, and then almost stabilized at 3.4 percent in October.

Core inflation was mostly impacted by the change in staple food prices, and to a lesser degree by the deceleration of prices for capital goods and "other goods and services". Core inflation, excluding staple food, remained almost unchanged, from 1.8 percent in August to 1.7 percent in October. Furthermore, core inflation has been lower than headline inflation since July, as it does not take account of the direct effects of price rises in some products, particularly fuel in July and tobacco in August.

Analysis of price trends in the major components shows continued deceleration in fresh produce prices over the past three months (5.1 percent in August, 4.4 percent in September, and 2.6 percent in October), which is largely attributable to the change in prices for vegetables and fresh fruit.

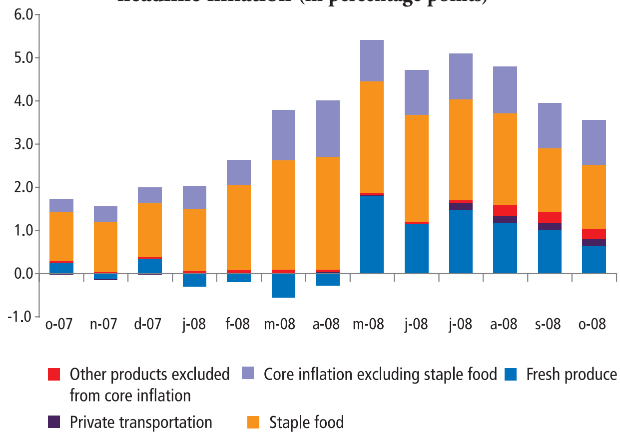
Staple food prices saw substantial deceleration, as their annual growth rate declined from 15.3 per-

Chart 5.1: Headline inflation and core inflation
(year-to-year)



Sources: HCP, and BAM calculations

Chart 5.2: Contribution of main components to year-to-year headline inflation (in percentage points)



Sources: HCP, and BAM calculations

cent in August to 10.2 percent in September and October. Accordingly, the increase in cereal prices fell from 19.9 percent in August to 13.1 percent in October, that of dairy products from 3.4 percent to 0.5 percent and fats from 17.1 percent to 13.3 percent. This trend is linked to the continued stabilization of international commodity prices which spread to domestic prices through the decrease in the growth rate of food import prices. This decline is linked as well to the base effect of the marked price rise registered in these products in the first half year of 2007.

Private transportation fares, the trend of which is dependent on fuel prices, registered the same growth rate of the previous three months, 6.1 percent, because of the base effect of the price rise in premium gasoline last July. Conversely, the current drop in oil prices on the international markets has not yet spread to domestic prices.

Other components contributed to the slowdown in headline inflation in general, and core inflation in particular. They mainly concern prices for capital goods (from 2.8 percent in August to 2.4 percent in October) amid the global economic slowdown, and prices for "other goods and services" (from 2.7 percent in August to 2.4 percent in October).

Table 5.1: Headline inflation and its components

	Monthly change (%)			Year-to-year (%)		
	Aug. 08	Sept. 08	Oct. 08	Aug 08	Sept. 08	Oct. 08
Headline inflation	**0.4**	**0.5**	**-0.1**	**4.8**	**3.9**	**3.5**
- Fresh produce	0.5	1.4	-0.5	5.1	4.4	2.6
- Private transportation	0.1	0.1	0.1	6.1	6.1	6.1
- Other products excluded from core inflation	3.8	0.1	0.0	4.8	5.1	4.9
Core inflation	**0.2**	**0.2**	**-0.1**	**4.4**	**3.5**	**3.4**
Including: - Staple food	0.3	0.9	-0.5	15.3	10.2	10.2
- Other food products	0.3	0.7	-0.2	3.8	4.0	3.8
- Clothing	0.2	0.4	0.1	1.8	1.9	1.7
- Housing	0.0	0.1	0.1	0.7	0.7	0.7
- Equipment	0.1	0.1	0.1	2.8	2.7	2.4
- Medical care	0.1	0.0	0.0	0.3	0.3	0.2
- Public transportation and communication	0.1	-0.1	0.0	2.0	1.8	1.8
- Leisure activities and culture	0.0	0.7	0.4	1.7	1.7	2.0
- Other goods and services	0.4	0.1	0.0	2.7	2.7	2.4

Sources: HCP, and BAM calculations

5.2 Goods and services

The breakdown of inflation per goods and services shows continued downtrend in prices for processed goods, on a year-to-year basis, which decreased from 4.2 percent in August to 3.4 percent in October. This change mainly results from the deceleration in the prices of all staple food, partly because of a favorable base effect. The domestic prices of these products reflect renewed downward trend in the international prices for food commodities.

Mitigation in inflation growth rate was also observed in the prices of "unprocessed goods and others".

Their annual growth rate indeed declined from 8.7 percent in August to 5.3 percent in October, reflecting the change in some fresh produce, particularly vegetables (from 5.8 percent in August to -3.7 per-

Table 5.2: Change in goods and services price index

	Monthly change (%)			Year-to-year change (%)		
	Aug. 08	Sept. 08	Oct. 08	Aug. 08	Sept. 08	Oct. 08
Processed goods	0.9	0.7	-0.2	4.2	4.0	3.4
Unprocessed goods and others	0.4	1.0	-0.4	8.7	6.3	5.3
Services excluding private transportation	0.1	0.2	0.1	1.5	1.5	1.4
Private transportation	0.1	0.1	0.1	6.1	6.1	6.1

Sources: HCP, and BAM calculations

cent in October) and fresh fruit (from 5.2 percent to 0.1 percent).

In addition, the pace of price rises in services excluding private transportation stabilized at about 1.5 percent in August and September, and later slightly decreased to 1.4 percent in October. This near stagnation reflects, in part, a deceleration in the prices for "medical consultations" by 1.6 percent in August and 1 percent in October, and for "restaurants, cafés and hotels" from 2.9 percent to 2.3 percent. On the other hand, it covers an acceleration in the prices for "education" from 1.7 percent to 2.1 percent.

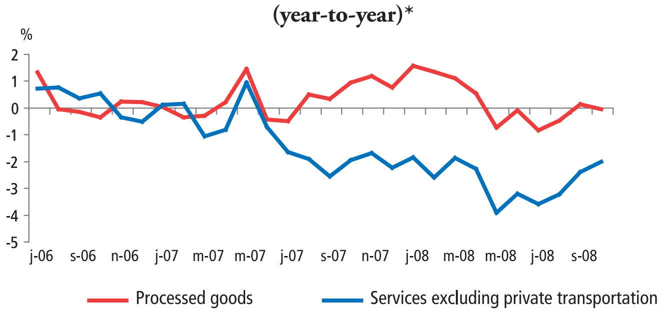
The continued slowdown in the increase rate of processed goods' prices and the stable trends in the prices of services excluding private transportation made it possible to reduce the relative gap between both indexes. It thus moved from 2.8 percentage points in August to 2.5 percentage points in September and 2 percentage points in October. Should this trend persist in the coming quarters, it might lead to gradual wearing off of the spread effect to prices for services.

The overall contribution of processed and unprocessed goods to headline inflation on a year-to-year basis was of approximately 3.3 points on average over the past three months and 2.8 points in October. Services, including private transportation, contributed to headline inflation by 0.8 point on average over the past three months and in October.

5.3 Tradable and nontradable goods

The breakdown of the cost of living index per type of product shows a more marked slowdown in tradables inflation than in nontradables. In October, tradables price index contributed, to a lesser degree, to the rise in the price index, reflecting in part the deterioration of the unfavorable international economic condition which, in turn, has led to a drop in staple food prices. It is worthwhile to underline as well that inflation differential between both indexes is at its lowest level since April 2008.

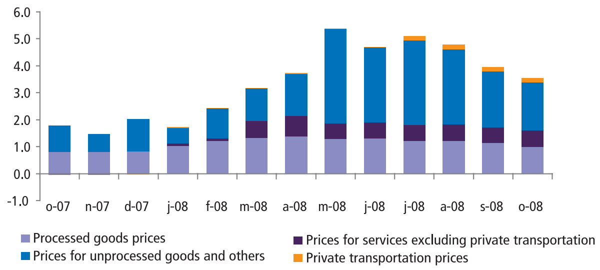
Chart 5.3: Relative prices of processed goods and services excluding private transportation compared with headline inflation (year-to-year)*



(*) Gap between the inflation rate of processed goods and services excluding private transportation and headline inflation rate.

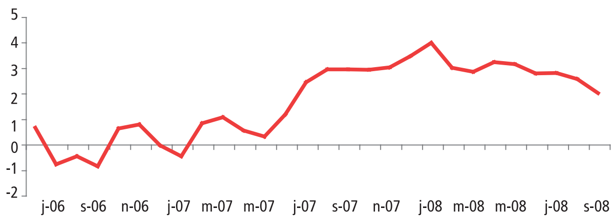
Sources: HCP, and BAM calculations

Chart 5.4: Contribution of goods and services prices to headline inflation (year-to-year)



Sources: HCP, and BAM calculations

Chart 5.5: Gap in inflation rates between processed goods and services excluding private transportation (year-to-year)*



(*) The gag between the inflation rate of processed goods and of services excluding private transportation

Sources: HCP, and BAM calculations

Tableau 5.3: Change in the price index of tradables and nontradables

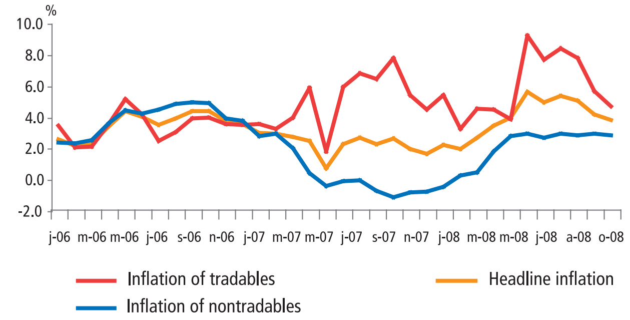
	Monthly change (%)			Year-to-year (%)		
	Aug. 08	Sept. 08	Oct. 08	Aug. 08	Sept. 08	Oct. 08
Tradables	0.6	1.2	-0.6	7.5	5.4	4.4
Nontradables	0.3	0.0	0.2	2.6	2.7	2.6

Sources: HCP, and BAM calculations

The increase rate of tradable prices declined from 5.4 percent to 4.4 percent, and contributed by 1.96 percentage point to headline inflation. This trend is attributable to the deceleration of the prices for some fresh produce, namely fish and fruit, as well as for staple food.

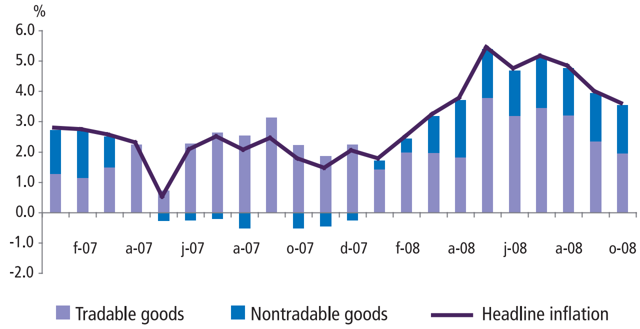
In turn, the price rise of nontradables remained stable at around 2.6 percent, contributing by nearly 1.58 percentage point to headline inflation. This trend mostly results, on the one hand, from the fall in meat prices' increase rate, and, on the other hand, from the continuing spread effect of the price rise to some services. Most significant rises affected the prices of "private transportation", "education", "healthcare and articles of personal use", and "restaurants, cafés and hotels".

Chart 5.6: Indexes of tradables and nontradables (year-to-year)



Sources: HCP, and BAM calculations

Chart 5.7: Contribution of tradables and nontradables to headline inflation (year-to-year)



Sources: HCP, and BAM calculations

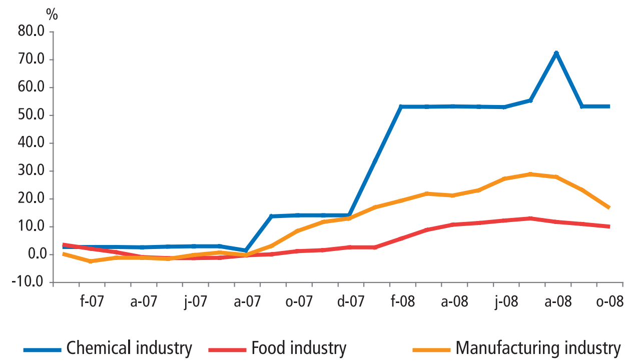
5.4 Industrial producer price index

The analysis of industrial producer price trends shows a slight easing of pressures on output costs and, therefore, on domestic prices. Indeed, the recent changes in the international prices of energy and agricultural commodities led to a continued slowdown, in October, in the growth rate of manufacturing industries' prices, on a year-to-year basis, standing at 16, 4 percent after 22.5 percent in September. Despite this decline, the growth rate of prices in the major manufacturing branches remains quite elevated.

This deceleration mainly resulted from the decline that began in August 2008 in the annual growth rate of coking and refining prices from 45.1 percent to 23.0 percent, contributing about 6.3 percentage points to the increase of the benchmark index.

Excluding oil refining, the growth rate of producer prices in the manufacturing industries was on a downward trend for the second month in a row, on a year-to-year basis. It went down from 14.4 percent to 13.9 percent, in response to the decline in the growth rate of the "food industry" branch from 10.2 percent to 9.4 percent. In contrast, the annual growth of output costs in the "chemical in-

Chart 5.8: Industrial producer price indexes (year-to-year)



Sources: HCP, and BAM calculations

Box 5.1: Recent developments in world inflation

The recent downward trend in world inflation is felt throughout all groups of economies, be they advanced, emerging or developing. This development is the result of some global common factors, namely the slump in oil prices, the behavior of international prices for non-energy commodities, and the implications of the current financial crisis on growth and demand. Until the second half of 2008, the surge in the prices for oil and other commodities, particularly food and metals, drove inflation up in all countries. Evidently, this rise was more noticeable in countries with a strong demand for these products. More particularly, food products represented a more significant share in household consumption in emerging countries than in the developed economies. Morocco was no exception to this rule. Our key partners were also affected by this trend. Thus, inflation rate between January 2007 and July 2008 went from 2.7 percent to 5.1 percent in Morocco, from 1.8 percent to 4.1 percent in the Eurozone and from 2.1 percent to 5.6 percent in the United States. The soaring prices of oil and commodities stem from a combination of interrelated factors, including notably the decline in output capacities and reserves, high demand particularly from emerging economies like China, and financial speculation. In addition to these factors, there are other elements linked to the additional demand for agricultural commodities intended for the production of biofuels. In common with Morocco, the soaring food and energy prices led to the worsening of inflationary pressures in the emerging markets, thus heightening wage claims.

Following this period of inflationary pressures, the growth rate of prices decelerated in the different countries as from the third quarter of 2008, after a peak in the second quarter. This reversal in trend is driven by the impact of the financial crisis reflected in slowing growth and weaker global demand. In this context, the pressures emanating from imported prices and foreign demand moved downwards. As a result, a decline in inflation has been registered since August 2008 and is expected, according to IMF projections, to continue during the next quarters (from 3.6 percent in 2008 to 1.4 percent in 2009 in the developed economies and from 9.2 percent to 7.1 percent in the emerging and developing economies). However, uncertainties still surround future inflation trends, in view of the high volatility in commodity prices and the persisting impact of the financial crisis.

Chart B 5.1: Inflation per country group (Year-to-year in %)

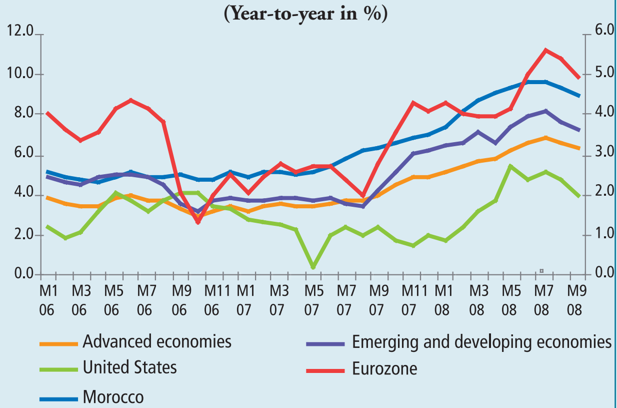
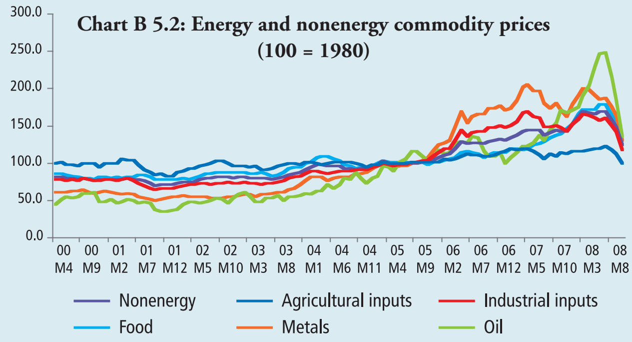
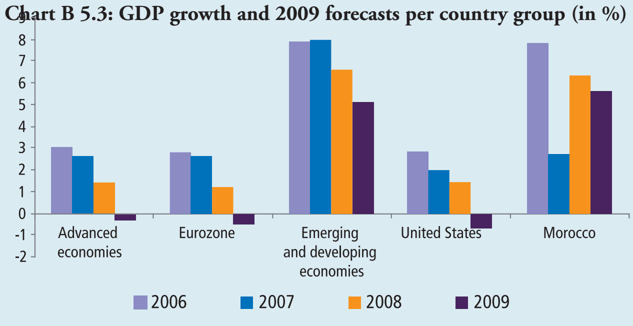


Chart B 5.2: Energy and nonenergy commodity prices (100 = 1980)



Source: World Economic Outlook (October and November 2008)

Chart B 5.3: GDP growth and 2009 forecasts per country group (in %)



Source: World Economic Outlook (October and November 2008) dustry" branch remained unchanged, yet at a relatively elevated level of 52.5 percent.

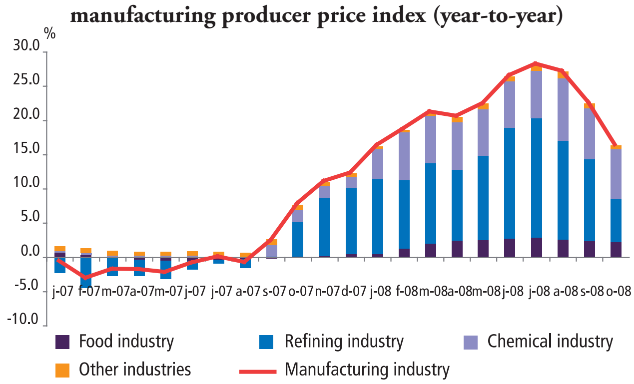
This slowdown was partly predictable, given the current international situation marked by stabilization in the prices for the major agricultural and energy commodities. Energy commodity prices, which reached record-high levels in the first half of 2008, began to fall in July 2008.

In the other non-energy producing branches, the output costs for metallurgy rose moderately by 1 percent, after 1.8 percent, while those for "metal working" went up by 8.5 percent compared with 14.4 percent.

This trend is traced back to the decline in the growth rate of some inputs, notably aluminum, copper and zinc. The annual growth rate of "textile industry" prices remained unchanged at 0.3 percent.

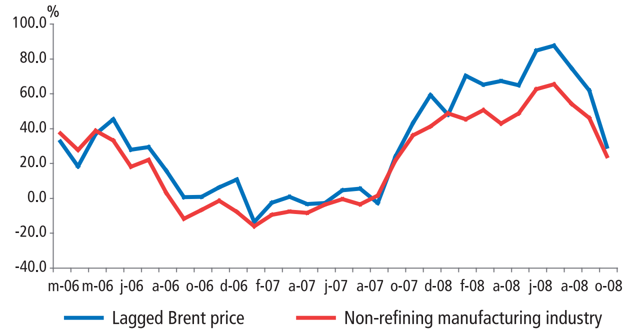
The findings of BAM business survey for October corroborate these analyses, as they confirm the continued downward trend in finished product prices that began in August. For the next three months, business managers project a decline in prices, except in textile and copper.

Chart 5.9: Contribution of main headings to the manufacturing producer price index (year-to-year)



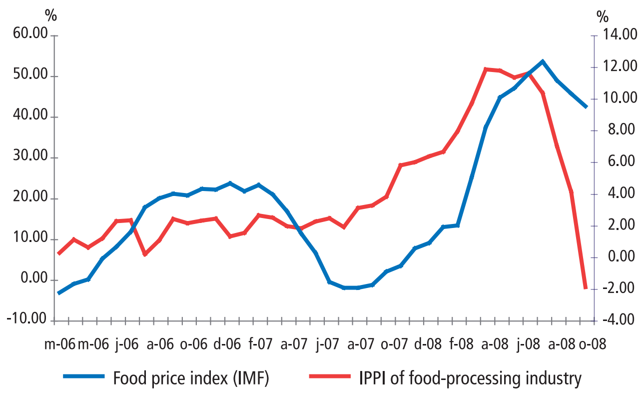
Sources: HCP, and BAM calculations

Chart 5.10: Refining industry index and Brent price (year-to-year)



Sources: IMF, HCP, and BAM calculations

Chart 5.11: Change in food prices in Morocco and on international markets (year-to-year)



Sources: IMF, HCP, and BAM calculations

6. INFLATION OUTLOOK

This section outlines the inflation trend deemed to be the most probable (central forecast) over the next four quarters and examines the major risks associated thereto (balance of risks). The central forecast scenario is therefore dependent on the assumptions and trends envisaged for a series of variables affecting activity and inflation. In an environment marked by a drop in commodity prices and pronounced slowdown in global economy, and considering the impact of the last Board decision of September 23, 2008, the central inflation forecast for the next six quarters was revised downwards, compared with the forecasts presented in the previous Monetary Policy Report. Assuming the non-occurrence of the major risk factors identified, the inflation trend over the coming six quarters remains in line with the price stability objective, with an average forecast of about 3 percent. At the end of the forecast horizon (the first quarter of 2010), headline inflation is expected to hover around 2.7 percent. For the year 2009, we project a headline inflation rate of approximately 2.9 percent. The quarterly profile of inflation during the year to come shows continuous drop in headline inflation over the first two quarters (3.5 percent then 2.8 percent) followed by stabilization at around 2.7 percent in the last two quarters. In the coming quarters, the risks and uncertainties surrounding the central inflation forecast are generally skewed to the downside, particularly because of the sharp contraction in foreign demand. However, this probable trend is, in part, contingent on the extent of the transmission of the fall in global commodity prices to domestic prices. Internally, it mainly depends on pressures on the labor market.

6.1 Baseline scenario assumptions

6.1.1 International environment

Since the last MPR of September 2008, the major international institutions have adjusted downwards their world economic growth outlook. The slowdown is driven by the advanced countries, the economy of which is expected to undergo in 2009 the first-ever annual contraction in more than sixty years. Actually, since September 2008, the impact of the financial turmoil that originated in the United States in mid 2007 has been felt in the entire global financial system, and tensions spread to the real economy. The massive measures taken by American and European governments, in addition to the substantial rate cuts carried out by the chief central banks, should contribute to stabilizing the financial situation. Beyond the direct effect of the financial crisis, the loss of confidence increasingly holds back economic activity, as households and businesses increasingly expect a prolonged period of bleak outlook in terms of labor and income.

Under such conditions, a marked slowdown in world growth is expected for 2008 and no slight improvement would occur before the second half of 2009. The advanced countries will plunge into recession, or get close to it, in the second half of 2008 and early 2009. The improvement expected during 2009 will be gradual. In most emerging or developing countries, growth would fall below its cyclical level. Therefore, OECD henceforth expects a growth rate in 2008 of 1 percent for the Eurozone and 1.4 percent for the United States, compared with 1.3 percent and 1.8 percent previously, and rates of -0.6 percent and -0.9 percent, respectively, for the year 2009.

In the United States, economic activity would slow down in the first half of 2009, before gradually improving as the impact of credit crisis lessens, the fall of the housing sector comes to end, and the measures to boost the economy begin to be felt. Nonetheless, the recovery will probably be slow, because consumption would be held back by the depreciation of real and financial assets.

In the Eurozone, growth will be severely affected by the tightening of financial conditions and the erosion of confidence. In fact, the toughening of financial conditions, the low growth of income, and the negative wealth effects resulting from the drop in equity and home prices are expected to curb consumption and investment. Then, recovery would be progressive and driven by the effects of monetary easing and recovery plans.

On this basis, we assume as a central forecast for this Report a growth rate in our major partner countries (France, Germany, Italy and Spain) of 0.9 percent in 2008 and -0.5 percent in 2009.

These rates represent a substantial downward revision of the assumptions we made in the previous MPR, which were of 1.1 percent for 2008 and 1.3 percent for 2009. It should be mentioned that this growth rate is calculated on the basis of a weighted average of growth rates in our main partners.

Over the next two years, headline inflation is expected to go down in all OECD countries. It would be under 1.8 percent for the year 2009, and some countries would even face a low risk of deflation. This drop would result from the combined effect of weakening global demand and falling commodity prices. In the Eurozone, headline inflation will probably decrease significantly early next year to a level that is in line with the ECB inflation objective, to hover around 1.4 percent throughout the year 2009.

6.1.2 National environment

Considering that the 2008-2009 crop year has just begun and that the forecast of agricultural output is a complex exercise, we assume a cereal output of 60 million quintals for the 2008-2009 crop year, corresponding to an average crop year, as set out in the previous MPR. The same assumption is adopted for the forthcoming crop year of 2009-2010.

A number of indicators reinforce this scenario for the current crop year, namely cumulated rainfall and a dam filling rate that are more important than those registered in the same period of 2007 (data as at end of November), larger surface areas of cultivated lands, and heavier use of agricultural inputs. The continuous improvement of these indicators has led to taking account of a probable uptrend in the 2008-2009 cereal harvest, compared with the 60 million quintals. This was incorporated in the balance of risks of this forecast exercise and analyzed through the formulation of an alternative scenario.

According to BAM estimates, the effects of an improvement in agricultural output on inflation are mitigated and of a small extent. The direct impact is reflected, on one hand, in a reduction in Morocco's cereal imports and an increase in domestic supply (easing of pressures on prices), and on the other hand by increased demand, chiefly in the rural areas, and pressures on rural wages. However, due to the earliness of the crop year, agricultural output still depends on the rainfall of early spring and the harsh winter.

The adopted central scenario for this forecast exercise corresponds to a 10 percent rise in agricultural GDP in 2008. Against this backdrop, the agricultural output gap is expected to remain positive over the six quarters of the forecast horizon. The performance of nonagricultural sectors would continue at a pace slightly below the trend of the past years, mainly because of the deterioration of the international environment.

The 2007-2008 crop year being below the average, rural unemployment in the third quarter of 2008 increased to 3.9 percent. Overall, the unemployment rate remained stable owing to the recovery in the urban labor market. Concerning the Quarterly Wage Index in the private sector, calculated by the HCP, it shows an increase in real wages by about 0.8 percent year-to-year, in the second quarter 2008. For the year 2009, the future outlook suggests a recovery of labor growth due to improved activity in the agricultural sector. The expected rise in minimum wage in July 2009 is incorporated in the central scenario.

The deteriorating conditions in the advanced countries have negatively impacted global demand for hydrocarbons. This has entailed a downward trend in crude prices which should continue over the coming year. The different measures taken by the producing countries, in a context of dollar appreciation, have so far been inefficient in redressing this trend. Consequently, the trend of oil price for the year 2009 would be further tilted downwards, as the IMF and the OECD predict an average price of $68 and $60, respectively, in the year 2009. Prices would later increase to $70 on average in 2010. This price prediction, shared by a number of international institutions and banks, is strengthened by trends in the futures market that show prices of about

$70 per Brent barrel for 2009 and $95 for 2010.

In Morocco, except the price rise of some types of fuel in July 2008, the freezing of the indexation mechanism has made it possible to significantly reduce the impact of these rises on the domestic market. Hence, subsidization costs, including those for oil products, are projected to increase, for the year 2008 as a whole, to 29.7 billion dirhams, or 4.4 percent of GDP. The 2009 Finance Act devotes a budget of 28.9 billion dirhams to the overall subsidization costs, excepting arrears, on the basis of a scenario of $100 a barrel, compared with the $75 projected in the Finance Act of 2008.

The uncertainty resulting from the change that might occur early 2009 in the range of domestic fuels and the downward trend in world oil prices, further complicates the analysis of future trends in diesel price at the pump. Moreover, the central forecast suggests stagnation in diesel price at the pump at 7.22 dirhams per liter over the forecast horizon.

Table 6.1: Inflation forecast for 2008 Q4 - 2010 Q1

Year-to-year

	2008	2009				2010	Average		
	Q4	Q1	Q2	Q3	Q4	Q1	2008	2009	FH*
Central forecast (%)	3.9	3.5	2.8	2.7	2.6	2.7	3.9	2.9	3.0

BAM forecasts

** (FH) Forecast horizon*

6.2 Inflation outlook and balance of risks

On the assumption of non-occurrence of the main risk factors discussed below, the central forecast for the next six quarters is expected to be on average in line with the price stability objective. As stated in the last MPR, headline inflation would reach 3.9 percent for the whole year 2008, a level noticeably above the 2 percent registered in 2007. Forecasts for the year 2009 show a headline inflation rate of approximately 2.9 percent. In the first quarter of 2010, it would hover around 2.7 percent. Compared with the projections presented in the September MPR, inflation forecast for 2009 was revised downwards from 3.6 percent to 2.9 percent, against a backdrop of rapid and substantial fall in global economic activity, coupled with the depreciation of commodity prices.

For the last quarter of the current year, we project a headline inflation rate of about 3.9 percent, down from 4.6 percent in the previous quarter. This decrease should continue during the first two quarters of 2009, with an inflation forecast going down from 3.5 percent to 2.8 percent. Then, the average headline inflation rate would stabilize at around 2.7 percent over the three remaining quarters of our forecast horizon (see table 6.1). Compared with the projections published in the Monetary Policy Report of September 2008, the inflation forecast for the four quarters of 2009 was adjusted downwards: from 4.1 percent to 3.9 percent for quarter one, from 3.4 percent to 2.8 percent for Q2, from 3.2 percent to 2.7 percent for Q3, and from 3.5 percent to 2.6 percent for the fourth and last quarter.

These projections were developed based on assumptions considered as being the most probable. However, there are still many sources of uncertainty stemming from future trends in exogenous variables as well as from the forecasting models, which may impact the projected inflation rate either upwards or downwards11. Analysis of this balance of risks shows an asymmetric forecast range represented in the form of a fan chart. This is a probabilistic evaluation of uncertainty zones surrounding the central forecast (see chart 6.1). The fan chart of this forecast exercise suggests a downward trend of risks on inflation, mainly due to the sharp contraction of foreign demand. Nonetheless, this probable trend is in part conditional on the extent of the transmission of the fall in global commodity prices to domestic prices. Internally, it mainly depends on the effects of the expected rise in the minimum wage in July 2009, on pressures on the job market, and on the change to be introduced to the structure of fuel prices at

1 For a brief presentation of inflation forecast models, see Box B6.1, page 28 of the MPR of March 27, 2007.

the pump. The materialization of one or more of these risks could lead to a deviation of the inflation rate from the central forecast, at a value included (with a probability of 90 percent) within the forecast range represented on the fan chart.

Chart 6.1 : Inflation forecast fan chart, 2008 Q4 - 2010 Q1 (Quarterly data)

Year-to-year

(*) This chart represents the confidence interval relative to inflation projection derived from the baseline scenario (dark red). Confidence intervals from 10 percent to 90 percent are also reported. Each addition of intervals of the same color, on both sides of the central forecast, increases by 10 percent the probability that headline inflation would fall within the range delimited by these intervals. Therefore, if we consider the range delimited by the fifth interval around the central forecast, this means that we have a 50 percent chance that headline inflation would fall within this range in the future.

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