بنك المغرب
BANK AL MAGHRIB

MONETARY POLICY REPORT

N° 16 / 2010

Document prepared for
the Bank Board
September 21, 2010

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LIST OF ABBREVIATIONS

APC	:	Cement manufacturers professional association
BAM	:	Bank Al-Maghrib
BPW	:	Building and public works
CFG	:	Casablanca Finance Group
CNSS	:	Caisse nationale de sécurité sociale (National Social Security Fund)
CPI	:	Consumer Price Index
CPIX	:	Core inflation indicator
CPIXNT	:	Consumer price index of nontradables
CPIXT	:	Consumer price index of tradables
CUR	:	Capacity utilization rate
DH	:	Dirham
ECB	:	European Central Bank
FDI	:	Foreign direct investments
FISIM	:	Financial intermediation services indirectly measured
GDP	:	Gross domestic product
HCP	:	High Commission for Planning
IMF	:	International Monetary Fund
IPI	:	Import price index
IPPI	:	Industrial producer price index
MASI	:	Moroccan All Shares Index
MPR	:	Monetary Policy Report
OCP	:	Office chérifien des phosphates (Moroccan Phosphates Office)
OECD	:	Organization for Economic Cooperation and Development
ONE	:	Office national d'électricité (National Electricity Office)
OPEC	:	Organization of the Petroleum Exporting Countries
PER	:	Price Earning Ratio
REPI	:	Real estate price index
SMIG	:	Salaire Minimum Interprofessionnel Garanti (minimum wage)
UCITS	:	Undertakings for collective investment in transferable securities
UPC	:	Unit production cost
VA	:	Value added

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PRESS RELEASE

BANK AL-MAGHRIB BOARD MEETING

Rabat, September 21, 2010

1. The Board of Bank Al-Maghrib held its quarterly meeting on Tuesday, September 21, 2010.

2. At this meeting, the Board examined recent economic, monetary and financial trends, and inflation forecasts prepared by the Bank staff up to the fourth quarter of 2011.

3. The Board noted that, as assumed in the most recent projections of Bank Al-Maghrib, inflation remained moderate, due to the absence of significant domestic demand-related pressures and low inflation in the major trading partner countries. Headline inflation in August 2010 thus fell to 0.6 percent, year on year, down from 1.1 percent in July. At the same time, core inflation, which reflects the underlying trend of prices, has hovered around 0.4 percent in the last four months, up from the 0 percent rate observed since the end of 2009. Industrial producer prices, which are determined by developments in international markets, reported an increase by 6.4 percent in July, compared with 7.5 percent in June and 11.6 percent in May.

4. Internationally, uncertainties persist in relation to the still stringent credit conditions and the high unemployment rates in the advanced economies. This trend continues to threaten the prospects for a stronger global economic recovery.

5. In Morocco, the latest available data show that nonagricultural activity continues the upward trend that began in the last quarter of 2009. Therefore, despite the expected decline in the agricultural value added, overall GDP would expand by nearly 4 percent for the full year 2010. Nonagricultural output gap, more relevant for the assessment of inflationary pressures, would be slightly positive.

6. Analysis of monetary conditions, based on data as at end July 2010, suggests the continued moderate growth of M3, down to 6.3 percent year on year from an average of 6.5 percent in the second quarter 2010. Under these circumstances, monetary surplus remains almost nil, while growth in bank credit, albeit slower, maintains momentum at 11.6 percent.

7. On the basis of these data, the central inflation forecast remains close to that of June. On average, headline inflation would indeed reach about 1 percent in 2010 and hover around 2 percent over the next six quarters. At the end of this forecast horizon (fourth quarter of 2011), it would remain close to 2 percent. Core inflation would continue to grow moderately, not exceeding 2 percent.

8. Under these circumstances where the balance of risks is slightly tilted to the upside, mostly in connection with the projected trend in import prices, and the central inflation forecast is consistent with the price stability objective, the Board decided to keep the key rate unchanged at 3.25 percent.

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In line with recent forecasts published under the June MPR, inflation remained subdued, owing both to the absence of any significant demand-driven pressures and to low inflation levels in Morocco's major trade partners. Headline inflation at annual rates receded from 1.9 percent in June to 1.1 percent in July. At the same time, core inflation, which reflects the underlying trend of prices, stabilized around 0.4 percent between the second quarter and July. Industrial producer price index slowed down to 6.4 percent in July, compared with 7.5 percent in June and 11.6 percent in May.

Internationally, the easing of concerns about the sovereign-debt crisis developments along with the successful fund-raising in some countries helped to reduce pressures on European financial markets. However, the normalization of financial conditions is still limited and accompanied with strong investor risk-aversion. Moreover, pressures on interbank markets persist and bank lending conditions are largely tightened, which may even obstruct the still vulnerable world economic recovery.

Meanwhile, real sector indicators in advanced economies show varied trends across countries at the end of July. While growth in the United States was more modest, it accelerated in the euro area, mostly in response to the rebound in Germany's GDP. Available data point to upward revisions in the 2010 growth outlook for major emerging and advanced economies.

With the current recovery in commodity prices, particularly oil and agricultural commodities, world inflation in July 2010 further accelerated year on year. In the short run, it is expected to remain subdued in advanced economies, owing to the still modest growth outlook, weak output capacity utilization and feeble growth in credit.

At the national level, the gradual increase in foreign demand and the improvement in domestic demand maintained nonagricultural growth well above the levels seen in 2009. Despite an 8.6 percent decline in agricultural value added, overall GDP growth stood at 3.5 percent in the first quarter and is expected to exceed 4 percent in the second and third quarters. For the full year, the overall growth projection was kept unchanged at a rate ranging between 3 percent and 4 percent, reflecting a slight upward revision of nonagricultural growth and a sharper drop in agricultural value added. Under these circumstances, nonagricultural output gap, which is particularly relevant to the analysis of inflationary pressures, was slightly positive during the second quarter of 2010, and is expected to be hovering around that level.

Monetary data show a slight moderation in M3 annual growth, which subsided to 6.3 percent in July from 6.5 percent in the second quarter. Consequently, monetary surplus remained virtually nil. At the same time, annual credit growth, albeit slower than the 13.4 percent and 13.8 percent levels recorded in the second quarter and in the first half of the year, respectively, remained sustained at 11.6 percent. Concerning lending rates, the BAM survey for the second quarter shows that the weighted average rate decreased from 6.65 percent to 6.36 percent, owing primarily to the drop in the interest rates applied to equipment loans and cash advances. Recent figures on the real estate price index point to an increase in that index in the second quarter of 2010, after the decline observed in the first quarter. As for financial asset prices, the MASI index gained 3.1 percent in the second quarter of 2010, before dropping 0.3 percent between July and August.

In light of these elements and the most likely assumptions concerning various inflation determinants, the central inflation forecast for the six coming quarters remained roughly unchanged. Headline inflation is therefore expected to be broadly consistent with price stability objective, hovering around a 2 percent average over the six coming quarters and in the end of the projection period, i.e. the fourth quarter of 2011. Core inflation, on the other hand, is forecast to remain below 2 percent. The balance of risks to the central forecast is slightly skewed to the upside, mainly in light of the outlook for import prices.

1. AGGREGATE SUPPLY AND DEMAND

Recent business indicators point to stronger recovery in nonagricultural activities and a decline in the primary sector's value added. The slow but sustained improvement in foreign demand and the good performance of domestic demand, which is driven by the growing momentum in household consumption and the upturn in private investment, both helped to maintain growth in the secondary and tertiary sectors well above the levels seen in 2009. Despite an 8.6 percent decline in agricultural value added, overall GDP growth stood at 3.5 percent in the first quarter, and is expected to exceed 4 percent in the second and third quarters, as shown by end-of-July monthly indicators. Compared with recent forecasts under the June Monetary Policy Report, nonagricultural growth outlook for the full year was slightly revised upward, and is now expected to range between 4.5 percent and 5.5 percent. With a sharper-than-expected decline in agricultural value added, the overall growth forecast was maintained at a range between 3 and 4 percent.

1.1 Output

National accounts of the High Commission for Planning show that national economy grew by 4.9 percent in 2009, reflecting a feeble 1 percent increase in nonagricultural activities and a 30.6 expansion in agricultural value added. On a quarter-to-quarter basis, recent updates point to a 2.2 percent decline in nonagricultural activities in the first quarter of 2009, followed by a gradual recovery in the second and third quarters and a net upward adjustment corresponding to a 5.4 percent growth in the fourth quarter.

In 2010, national growth would see a sharper-than-expected decline in agricultural value added and better prospects for nonagricultural growth, which would range between 4.5 and 5.5 percent. Overall, national economy would grow at a rate between 3 and 4 percent.

At the sectoral level, the 2009-10 crop year's cereal production reached 74.6 million quintals, nearly 26.6 percent lower than the previous crop year, thus in line with the Bank's estimates based on data published on May 20, 2010 (see box 1.1, June 2010 MPR). Consequently, the decline

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

Activity sectors, in%	2009				2010		
	QI	QII	QIII	QIV	QI	QII (f)	QIII (f)
Agriculture	30.7	31.2	29.4	31.1	-8.6	-8.9	-8.9
Nonagricultural VA	-2.2	0.1	0.9	5.4	5.6	4.5	4.8
Extractive industry	-46.8	-31.0	-21.9	14.0	107.9	80.8	92.3
Processing industry	-1.5	-1.0	-0.1	3.3	1.6	1.4	1.4
Electricity and water	6.2	2.3	3.3	2.2	6.7	6.5	6.0
Building and public works	2.6	3.9	1.0	6.1	2.9	4.3	5.5
Trade	3.1	2.7	3.0	5.3	1.6	1.9	2.2
Hotels and restaurants	-5.8	-2.0	0.1	2.9	6.7	4.3	4.1
Transportation	1.5	2.6	2.3	4.9	0.1	0.9	1.2
Post and telecommunication	2.8	3.3	3.9	1.1	1.9	2.1	2.7
General government and social security	7.7	7.7	7.6	7.6	3.4	3.4	3.3
Other services*	3.5	3.7	3.5	4.0	4.1	4.0	4.0
Taxes on products net of subsidies	4.0	3.1	6.5	5.1	4.1	3.6	3.8
GDP excluding agriculture	-1.5	0.4	1.5	5.4	5.4	4.4	4.7
Gross domestic product	2.2	4.2	4.9	8.6	3.5	4.2	4.2

(*) Including financial activities and insurance, services to companies and personal services, education, health, and social action, and the FISIM.

Sources: HCP, and BAM estimates and forecasts

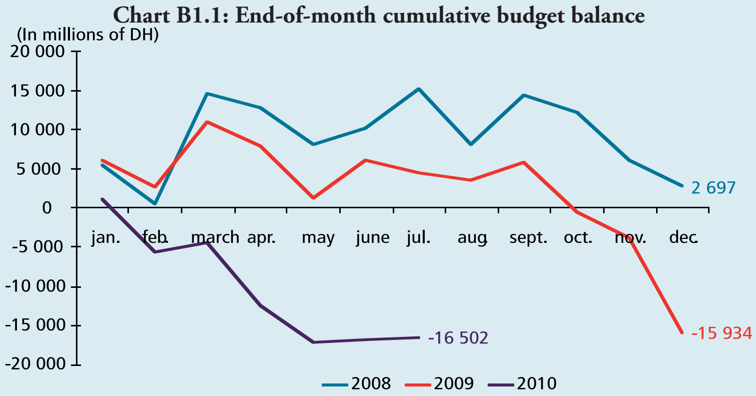
Box 1.1: 2010 budget execution as at end-July

As at end-July 2010, budget execution showed a deficit of 16.5 billon dirhams, compared with 16.8 billion dirhams at the end of June and a surplus of 4.8 billion dirhams in the same period of last year. This situation resulted from the expansion in subsidization costs by 9.6 billion dirhams, along with the slight decline in tax revenues.

Tax receipts, which amounted to 103.5 billion dirhams, were down 413 million dirhams from the end of July 2009, reflecting a 17.7 percent decline in revenues from direct taxes and a 14.5 percent increase in indirect taxes. Other tax revenues increased, however. The largest decrease was registered in corporate tax revenues, which shrunk by 22 percent to 21.6 billion dirhams. By contrast, the value added tax (VAT) stood at 39.7 billion dirhams, up 5.8 billion dirhams from the same period a year earlier, owing primarily to the 21.2 percent increase in imports' VAT. Similarly, revenues from customs duties and registration and stamp fees rose by 11.4 percent and 4.9 percent, respectively, relative to the previous year, while non-tax revenues receded by 2.8 percent.

On the opposite, ordinary expenses rose by 15.3 percent to 97.2 billion dirhams, driven by the expansion both in subsidization expenses, which surged to 15.1 billion dirhams from 5.5 billion dirhams a year earlier, and in operating expenses, which moved up by 3.6 billion dirhams. Capital expenditure declined 6.4 percent to 28 billion dirhams, of which nearly 65 percent were covered by public savings that amounted to 18.3 billion dirhams, compared with 31.8 billion dirhams in the same period of the previous year.

Chart B1.1: End-of-month cumulative budget balance



Source: Ministry of Economy and Finance

Under these circumstances, and taking into account the negative balance of the Treasury special accounts amounting to 6.8 billion dirhams and the formation of payment arrears at 1.4 million dirhams, fiscal deficit stood at 16.5 billion dirhams compared with a surplus of nearly 5 billion a year earlier. Up to 67 percent of that shortfall was covered by exclusively non-money domestic financing. Money domestic financing, on the other hand, declined following the improvement in the Treasury net position toward Bank Al-Maghrib by nearly 2 billion dirhams and the decrease in the Treasury liabilities to other depository corporations. The remainder of that shortfall was covered by net external flows amounting to 5 billion dirhams.

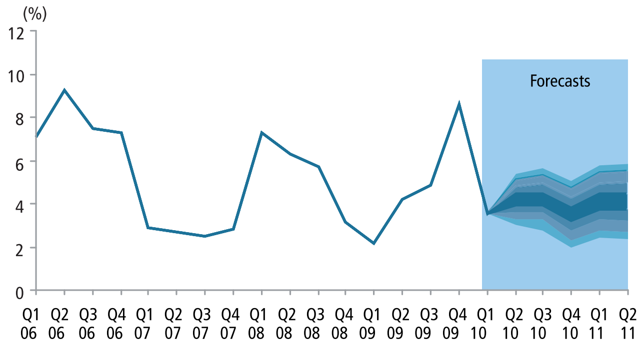
in the agricultural value added in the first quarter is set to be further confirmed in the coming quarters, as evidenced by the ¼ point drop in cereal sales late in June and the 71 percent surge in imports. Yields on vegetation productions are estimated to achieve satisfactory levels. In addition, the state of vegetation cover, which is already supportive for animal husbandry, should benefit from the abundant rainfall.

With the gradual improvement in foreign demand and the ongoing positive trend in domestic demand, nonagricultural activities should pursue the recovery that began in the second quarter of 2009. There would be however a slight slowdown during the coming quarters, mainly with the dissipation in base effects, which had led to a 5.6 percent growth of these activities in the first quarter of 2010.

With regard to fisheries, catches of inshore and small-scale fishing at the end of July 2010 grew by 16 percent. This growth covers an 18 percent increase in pelagic catches, along with a decline both in whitefish catches (by 2 percent) and in cephalopod and crustacean catches (by 19 percent). However, the corresponding value improved by 4 percent.

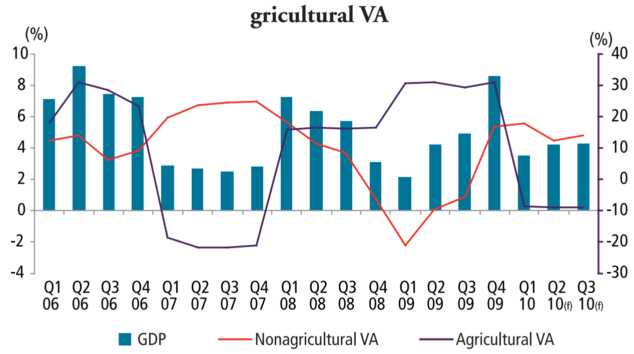
In the second quarter of 2010, the secondary sector would have contributed 3.4 percentage points to overall growth, thus reversing the negative course seen a year earlier. This recovery mainly reflects the improvement in extractive industry, in response to the 92.1 percent expansion in phosphate production at the end of June 2010, due in part to the strong rebound in international demand for phosphate products.

Chart 1.1: Growth forecasts Q2 2010-Q2 2011*



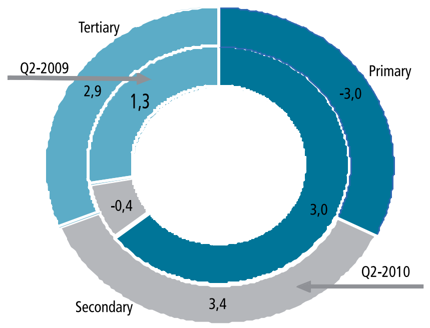
(*) Fan chart prepared on the basis of the standard deviation
Sources: HCP, BAM forecasts and estimates

Chart 1.2: Change in the GDP and the agricultural and nonagricultural VA



Sources: HCP, and BAM forecasts

Chart 1.3: Contribution of the primary, secondary and tertiary sectors to overall VA growth, in percentage points



Sources: HCP, and BAM calculations and forecasts

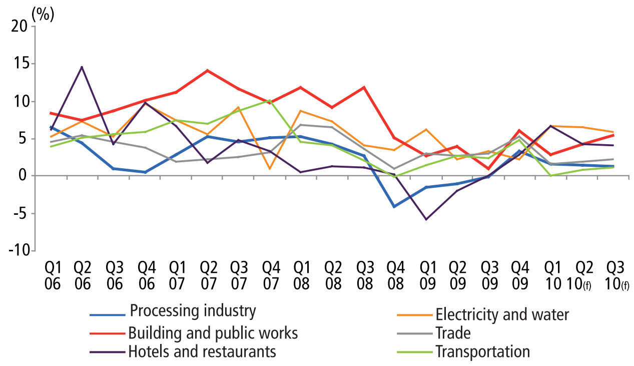
Having severely suffered from the fall in foreign demand over several quarters, the value added of processing industries should pursue the improvement that began in the fourth quarter of 2009. Its growth rate is expected, however, to ease to 1.4 percent in the second and third quarters. These trends reflect a moderate growth in non-refining industry and a gradual easing in the decline of oil refining activities. These estimates are underpinned by the BAM July business survey in the industrial sector, which shows that production would grow in all sectors and that the outlook for the coming months would be broadly supportive.

The electricity-and-water sector should grow by more than 6 percent during the second quarter, supported by an 11.8 percent increase in net production of the Office national d'Electricité (ONE).

Growth in the building-and-public-works sector is expected to be better than in 2009. It would range between 4 percent and 5.5 percent in the second and third quarters, compared with 2.9 percent in the first quarter. Construction activities, in particular, should resume growth after slowing down during the first three months of the year, due to some vagaries. At the end of June, the sector's indicators such as cement sales and loans to the sector show positive trends.

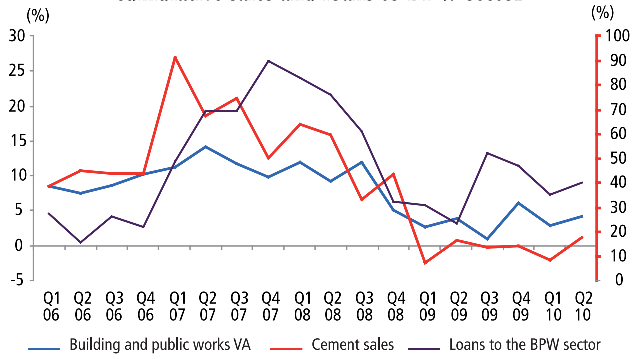
With regard to services, the improvement in international and national business conditions has had a positive impact on most branches. The sector's value added should grow by around 3 percent in the

Chart 1.4: Year-on-year change in value added



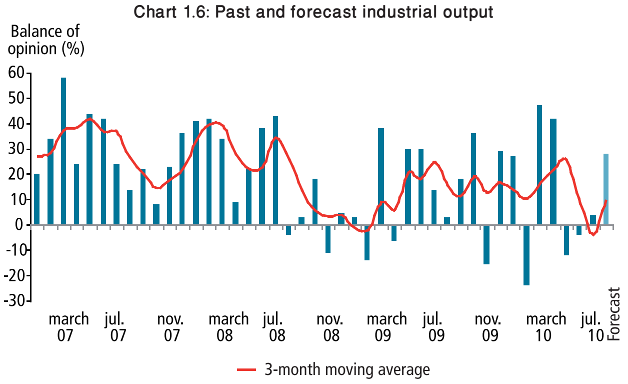
Sources: HCP, and BAM forecasts

Chart 1.5: Year-on-year change in building and public works' value added, cement quarterly cumulative sales and loans to BPW sector



Sources: APC, and BAM forecasts

Chart 1.6: Past and forecast industrial output



Source: BAM monthly business survey in the industry second quarter and would contribute 0.9 percentage point to overall growth.

Tourism key indicators trended upward at the end of July 2010. The influx of tourists and overnight stays in classified hotels increased by 10 percent and 12 percent, respectively, while travel receipts rose by 6.9 percent.

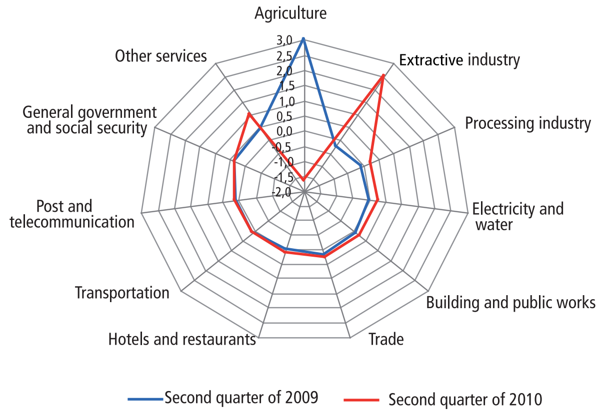
The transportation value added is expected to grow moderately in the second quarter of 2010, since the recovery in nonagricultural activities would be mitigated by the decline in agricultural value added. Receipts from transportation services rose by 3.3 percent at the end of July 2010. Meanwhile, trade should grow by less than 2 percent during the second and third quarters of 2010.

1.2 Consumption

The 2009 national accounts show that real domestic final consumption edged down to 5.5 percent, from 5.8 percent in 2008, despite the unfavorable effects of the international economic crisis. This performance can be explained by the 11.2 percent expansion in public consumption, compared with 4.8 percent in 2008, and the resilience in household consumption, which, though decelerating grew by 4 percent, after 6 percent in 2008.

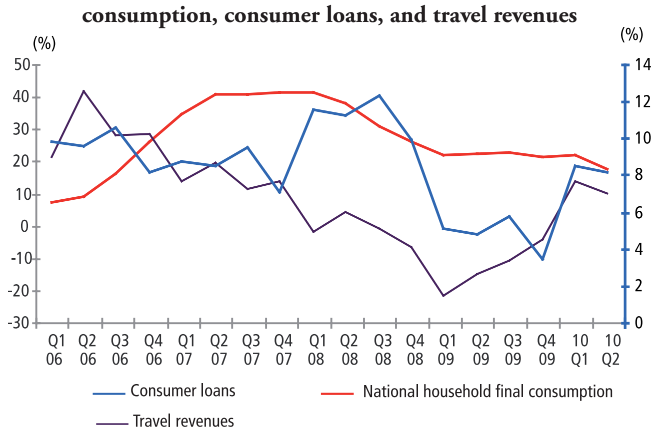
End-of-July data for 2010 show that household consumption improved, in response to the combined effect on household income of moderate rise in prices, the growth in nonagricultural value added and the upturn in remittances by Moroccan expatriates. Several indicators seem to underpin this positive trend. These include a 17.2

Chart 1.7: Sectors' contribution to overall growth



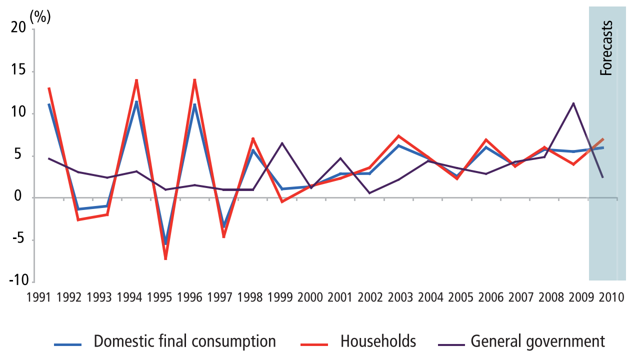
Sources: HCP, and BAM forecasts and calculations

Chart 1.8: Year-on-year quarterly change of households' final consumption, consumer loans, and travel revenues



Sources: HCP, Foreign Exchange Office, and BAM forecasts and calculations

Chart 1.9: Volume change in household final consumption



Sources: HCP, and BAM forecasts and calculations percent increase in VAT revenues and a 4.6 percent rise in imports of consumer finished products.

Public consumption is projected to slow down, after its rapid expansion in 2009, the highest in the past three decades. At the end of July, operating expenses grew by 5.4 percent, which represents an implementation rate of nearly 57.5 percent of the 2010 Finance Act projections.

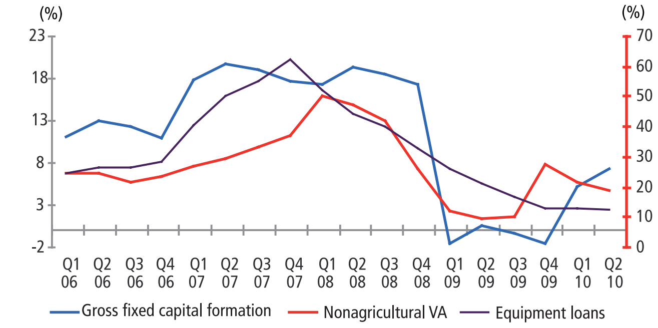
The various coincided and leading indicators show that the estimated growth of overall consumption expenses should be kept at the same range of 6 percent to 7 percent, with yet a stronger household consumption and slower general government consumption.

1.3 Investment

Amid deteriorating economic conditions and prospects following the international economic crisis, investment markedly decelerated in 2009. Real gross fixed capital formation, which was accompanied with a significant building of inventories, grew by a mere 2.5 percent, compared with 11.5 percent in 2008.

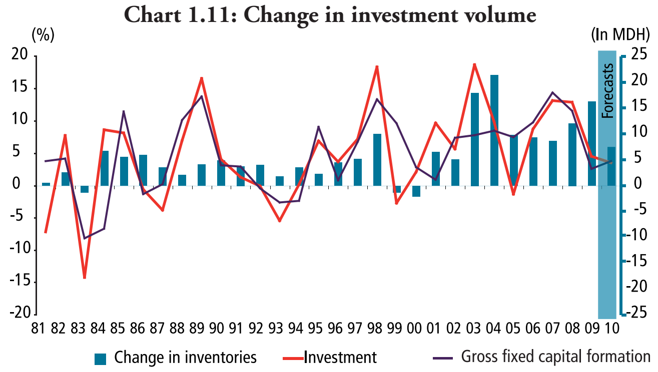
For the current year, end-of-July indicators point to a gradual recovery in private investment, driven by the current expected strength in nonagricultural activities. In addition to the rise in production and with capacity utilization rate remaining above the levels seen in 2008 and 2009, the BAM quarterly industry business survey points to an increase in investment expenses in all sectors in the second quarter. Corporate managers anticipate an increase in investment expenses during the coming quarters.

Chart 1.10: Year-on-year quarterly change in gross fixed capital formation, nonagricultural VA and equipment loans



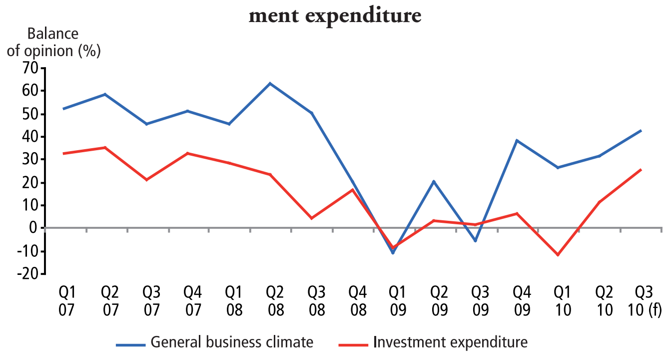
Sources: HCP, and BAM forecasts and calculations

Chart 1.11: Change in investment volume



Sources: HCP, and BAM forecasts and calculations

Chart 1.12: Change in the general business climate and investment expenditure



Source: BAM business survey in the industry

Several other indicators seem to underpin this favorable trend in investment. Chief of these are the recovery in imports of industrial finished capital goods, after their downward trend that began in 2008, as well as the nearly sustained increase in equipment loans since early this year.

Concerning public investment, Treasury investment expenses at the end of July declined by 6.4 percent to 28 billion dirhams, or an implementation rate of 60.9 percent compared with the 2010 Finance Act forecasts. This decrease is mainly due to the higher levels achieved during the last four years.

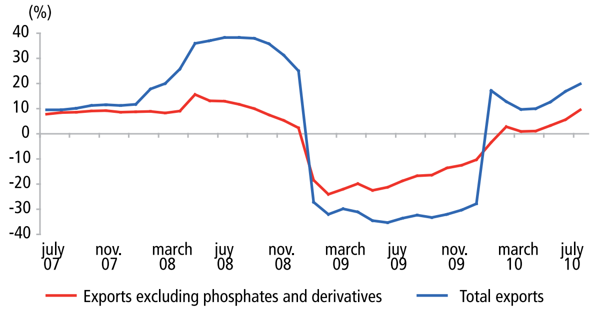
Overall, the sharp slowdown in gross fixed capital formation in 2009 is expected to induce a significant base effect, which should, together with the cited supportive trends, lead to a volume growth ranging between 3.5 percent and 4.5 percent of the gross fixed capital formation in 2010.

1.4 Foreign trade

End-of-July foreign trade data confirm the recovery in foreign demand, on the back of a marked upturn in exports. Growth in imports is less significant but remains sustained. Year-on-year trade deficit is less pronounced than in the previous months and the coverage ratio improved.

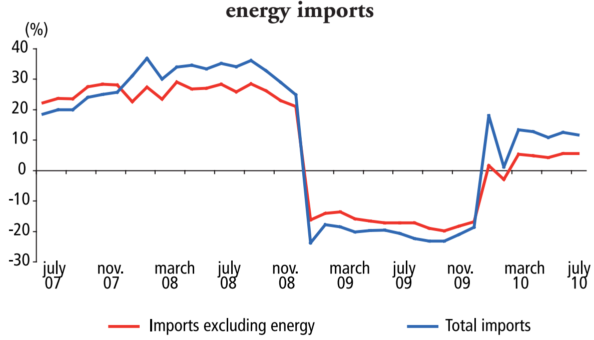
Trade balance at the end of July 2010 turned negative at 90 billion dirhams, up 5 percent from the same period a year earlier, after worsening by 8.9 percent and 9.2 percent at the end of June and May 2010, respectively. This deterioration resulted mainly from an 11.5 percent import expansion to 17.6 billion dirhams, which is higher in absolute terms than exports, which moved up 19.6 percent to 13.3 billion dirhams. Consequently, the

Chart 1.13: Year-on-year change in total exports and non-phosphates exports



Source: Foreign Exchange Office

Chart 1.14: Year-on-year change in total imports and non-energy imports



Source: Foreign Exchange Office

Table 1.2: Year-on-year change in the trade balance, at the end of July 2010

(In millions of dirhams)	jan-july 2009	jan-july 2010*	Change Amount	Change %
Total exports	67 836.9	81 130.6	+13 293.7	+19.6
Phosphate and derivatives' exports	10 989.5	19 061.9	+8 072.4	+73.5
Exports excluding phosphates and derivatives	56 847.4	62 068.7	+5 221.3	+9.2
Electronic equipment	2 115.6	2 950.3	+834.7	+39.5
Canned fish	2 587.3	2 648.2	+60.9	+2.4
Ready-made garments	11 873.2	10 388.0	-1 485.2	-12.5
Hosiery items	4 060.7	3 818.0	-242.7	-6.0
Total imports	153 580.0	171 167.8	+17 587.8	+11.5
Energy products' imports	28 540.5	39 439.6	+10 899.1	+38.2
Imports excluding energy products	125 039.5	131 728.2	+6 688.7	+5.3
Semi-finished products	30 788.8	36 317.0	+5 528.2	+18.0
Consumer goods	31 050.2	32 480.3	+1 430.1	+4.6
Capital goods	39 824.0	39 516.5	-307.5	-0.8
Food products	15 248.3	15 181.3	-67.0	-0.4
Wheat	4 049.7	2 738.9	-1 310.8	-32.4
Trade deficit	-85 743.1	-90 037.2	4 294.1	+5.0

** Provisional data*
Source: Foreign Exchange Office

coverage ratio rose to 47.4 percent from 44.2 percent at the end of the same period a year earlier.

The export growth is exclusively driven by the 73.5 percent expansion in the sales of phosphate and its derivatives. Other exports improved by 9.2 percent. Sales of electronic equipment and canned fish increased 39.5 percent and 2.4 percent, respectively. At the same time, sales of electricity wires and cables improved by 34.4 percent. On the other hand, exports of ready-made garments, hosiery items and shellfish slumped by 12.5 percent, 6 percent and 7.7 percent, respectively.

On the contrary, import expansion is largely prompted by the energy bill's jumping by nearly 38.2 percent to 39.4 billion dirhams. Meanwhile, purchases of semi-finished products, consumer finished goods and crude products rose by 18 percent, 4.6 percent and 1.9 percent, respectively. Purchases of food produce and capital goods, on the other hand, dropped by 0.4 percent and 0.8 percent, respectively.

Oil products' imports increased sizably, as the crude oil average price per imported ton and volume rose by 49.3 percent and 8.6 percent, respectively. The imported ton average price stood at 4,705 dirhams, compared with 3,152 dirhams in the same period a year earlier. Similarly, the purchases of gasoline and fuel-oil, as well as those of oil gas and other hydrocarbons increased by 19 percent and 49.1 percent, respectively. Likewise, non-energy imports rose by 5.3 percent, mostly owing to the increase in purchases of semi-finished products, as purchases of "iron and steel" and of "chemical products" expanded by 32.6 percent and 23 percent, respectively. There was also an increase in imports of consumer goods, following the 7.8 percent rise in imports of private cars. At the same time, imports of mineral crude products and finished industrial capital goods rose by 12.2 percent and 1.2 percent, respectively. On the other hand, purchases of food produce declined, mainly because of the 32.4 percent fall in wheat imports. Similarly, purchases of agricultural capital goods contracted by 34.6 percent.

2. PRESSURES ON OUTPUT CAPACITY AND LABOR MARKET

In line with BAM estimates under the last MPR, nonagricultural output gap was slightly positive in the second quarter of 2010 and would remain unchanged in the third quarter. This trend mostly reflects the ongoing strength in domestic demand and the gradual recovery in some partner countries. The industrial capacity utilization rate stabilized around 71 percent in July, a level lower than its pre-crisis average. The labor market in the second quarter of 2010 saw a slight year-on-year rise in the national unemployment rate, mainly with the increase in rural unemployment rate. Available data on wages point to a moderate real-terms increase in the private sector's wages. As well as underpinning the continued recovery in domestic business conditions, analysis of these data suggests slight easing in demand pressures on prices for the coming quarters.

2.1 Pressures on output capacity

Given the upturn in domestic demand and the slow but steady recovery in external demand from our key trade partners, growth in nonagricultural activities would have slightly exceeded the trend rate since the second quarter of 2010. However, the outlook for nonagricultural growth is still surrounded by uncertainties linked to recent developments in the euro area and their impact on the sustainability of recovery in our key partners.

The BAM July business survey in the industrial sector indicates that the capacity utilization rate stabilized at 71 percent, a level that remains lower than the pre-crisis average. This stagnation involved all sectors except for the food processing industries, where capacity utilization rate rose by 4 percentage points to 78 percent. In other sectors, this rate reached 73 percent in chemical and parachemical industries, 79 percent in electrical and electronic industries, 60 percent in mechanical and metallurgical industries, and 71 percent in textile and leather industries.

Apparent labor productivity in the nonagricultural sector, which is

Chart 2.1: Nonagricultural output gap

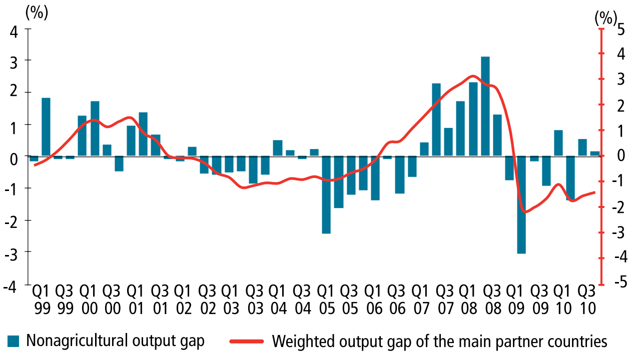
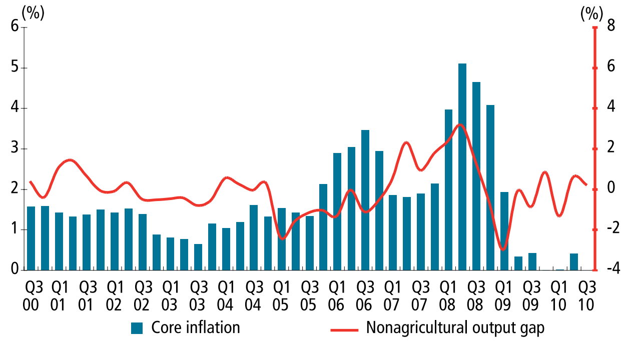


Chart 2.2: Nonagricultural output gap and core inflation (year-on-year)



Sources: HCP and BAM's estimates

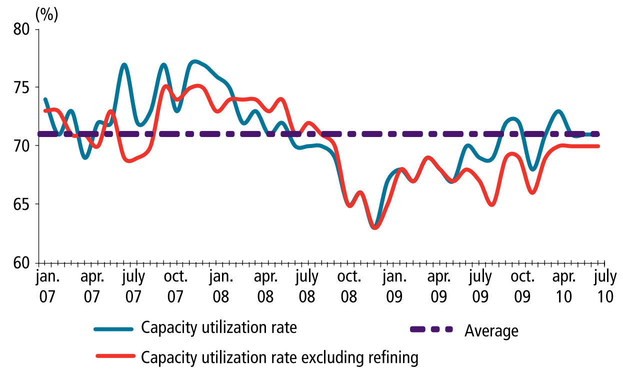
highly volatile due to fluctuations in nonagricultural GDP and urban employment (at annual rates), rose by a year-on-year 2.6 percent to nearly 111 points in the second quarter of 2010. This increase is attributable to the fact that urban employment grew less rapidly than nonagricultural GDP, in line with BAM estimates for the second quarter of 2010.

The BAM business survey points to an increase in the unit production cost (UPC) in the second quarter of 2010, with a positive balance of opinion standing at 24 percent. This increase involved all sectors, notably the food processing industries, and the electrical and electronic industries. By component, the increase in the UPC resulted from the surge in non-energy commodity prices with a balance of opinion of 35 percent, and, to a lesser extent, from the rise in wage costs, with a balance of opinion of 20 percent. As per sector, commodity and wage costs were the major sources of the increase in the UPC in all industries except for textile and leather, where financial costs were reported to be the second contributory factor to that cost increase.

2.2 Pressures on labor market

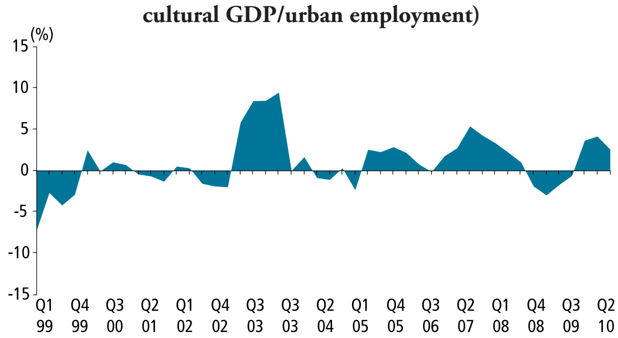
In the second quarter of 2010, labor force aged 15 and above reached 11,628,000 persons, up 1.5 percent from the same period of 2009. This increase reflects a

Chart 2.3: Industrial output capacity utilization rate



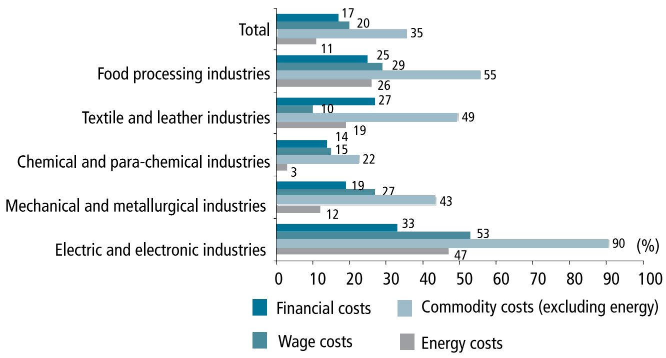
Source: BAM monthly business survey

Chart 2.4: Year-on-year apparent labor productivity (Nonagricultural GDP/urban employment)



Sources : HCP, and BAM estimates

Chart 2.5: Change in components of unit production cost per sector (Balances of opinion in %, in Q2 of 2010)



Source: BAM monthly business survey

rise in labor force both in urban and rural areas, respectively by 1.9 percent and 1.3 percent. Labor force participation rate stood at 50.5 percent, down 0.2 percentage point. This decrease reflects a less rapid growth in the labor force aged 15 and above then in the overall population.

Concerning employment, the employed labor force in the second quarter of 2010 was slightly higher than in the same period a year earlier. Nevertheless, employment rate dropped 0.2 percentage point to 46.4 percent, as the number of jobs grew at a rate somewhat slower than that of the labor force aged 15 and above. Per place of residence, urban and rural employment rates both dropped by 0.2 and 0.1 percentage point to 38.4 percent and 58.1 percent, respectively.

Between the second quarters of 2009 and 2010, job creation reached 140,000 jobs, including 92,000 jobs in urban areas and 48,000 jobs in rural areas. At the same time, 158,000 gainful jobs were created, while unpaid labor dropped 18,000 jobs, corresponding to the creation of 15,000 jobs in cities and the loss of 33,000 jobs in the countryside.

At the sectoral level, the "agriculture, forestry and fisheries" sector lost 83,000 jobs, down 1.9 percent, as agricultural production contracted after the bumper harvest of 2009. The "building and public works" registered a net creation of 109,000 jobs, followed by the "services"

Table 2.1: Activity and unemployment quarterly indicators per place of residence, on a year-on-year basis (1)

	Q2 - 2009			Q2 - 2010		
In millions / in %	Urban	Rural	Total	Urban	Rural	Total
Labor force and employment						
Labor force (2)	5.91	5.53	11.45	6.02	5.6	11.62
Labor force participation rate (%) (3)	44.1	60	50.6	43.9	60.1	50.5
Employed labor force	5.17	5.36	10.53	5.26	5.41	10.67
Employment rate (%) (4)	38.6	58.2	46.6	38.4	58.1	46.4
Unemployment						
Unemployed labor force	744	167	911	763	186	949
Unemployment rate (in %) (5)	12.6	3	8	12.7	3.3	8.2
By degree						
. Non-graduates	7.4	1.9	3.9	7.2	2.1	3.9
. Graduates	16.9	9.3	15.3	16.9	9.7	15.4

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

Chart 2.6: Nonagricultural growth and urban unemployment Q1 2001 – Q2 2010

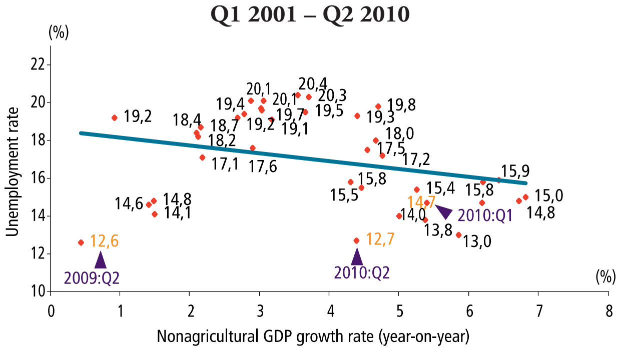
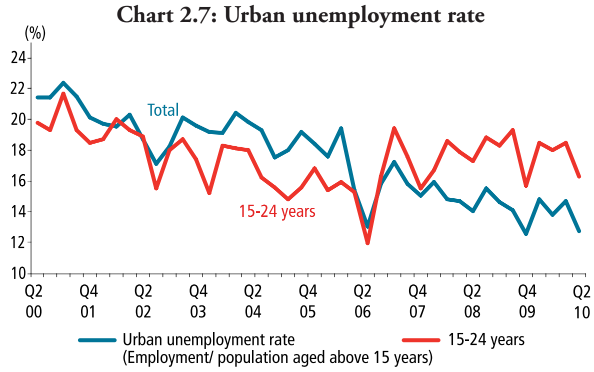


Chart 2.7: Urban unemployment rate



Source: HCP

sector with new 92,000 jobs. The industrial sector added 11,000 new jobs, mainly in response to the improvement in foreign demand.

The BAM business survey for the second quarter shows that the workforce stabilized quarter-on-quarter, with yet a decrease in the workforce in mechanical and metallurgical industries and a stagnation in that of chemical and para-chemical industries. In the short run, corporate managers expect the total labor force employed in the industrial sector to maintain its current level in all industries.

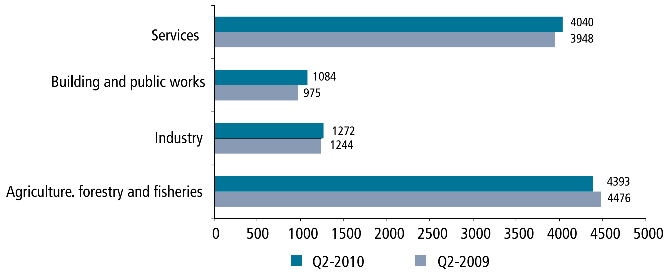
In this context, unemployment rate in the second quarter of 2010 edged up from 8 to 8.2 percent year-on-year, as it increased by 0.3 percentage point in urban areas to 3.3 percent, and almost stagnated at 12.7 percent in rural areas. By age category, unemployment rate increased by 0.6 percentage point among the 15-24 age group, 0.3 percentage point among the 25-34 age group, and 0.5 percentage point among the 45 and above age group. Among the 35-44 age group, however, it decreased by 0.2 percentage point.

In terms of wage cost, the manufacturing sector's relative unit labor cost in the second quarter seemed to be rising at a slower pace than apparent labor productivity. Indeed, the relative unit labor cost was 0.7 percent higher than in the same quarter a year earlier. Likewise, the growth of Morocco's relative unit labor cost in the second quarter of 2010

Chart 2.8: Change in unemployment structure by gender, age, and degree

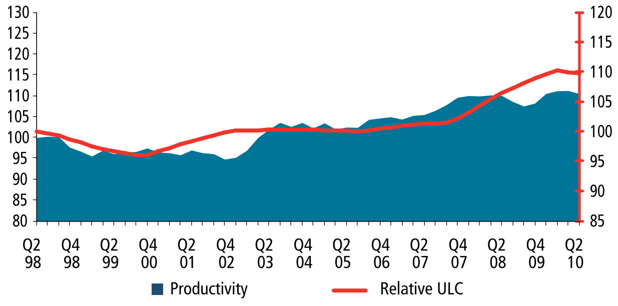
Source: HCP

Chart 2.9: Employed labor force per sector (in thousands)



Source: HCP

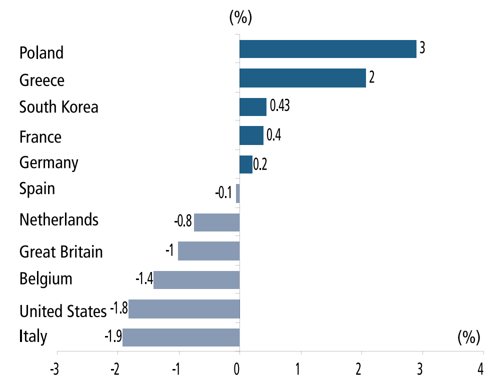
Chart 2.10: Relative unit labor cost and apparent labor productivity (Q1 1998- Q2 2010)



Sources: DataStream, and BAM calculations exceeded that of Poland, Greece and South Korea by 3 percent, 2 percent and 0.5 percent, respectively. However, it increased at a slightly slower pace than in Belgium, Hungary, the United States and Italy.

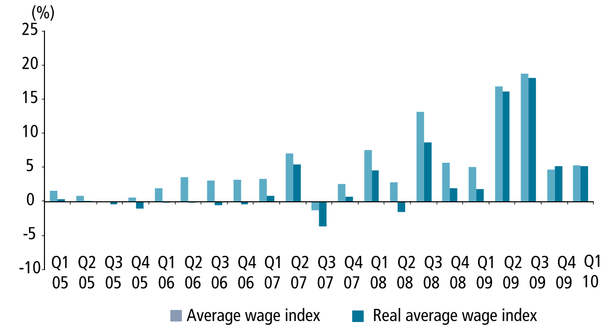
The quarterly average wage index, as measured by the HCP based on the CNSS data, rose by a year-on-year 5.31 percent in the first quarter of 2010. In real terms, it grew by 5.18 percent, compared with the same quarter a year earlier. The BAM business survey reports an increase in wage costs in the second quarter of 2010, with a balance of opinion standing at 20 percent. The rise covered all industries, more particularly electrical and electronic industries. However, the minimum wage remained unchanged in nominal terms, but slightly depreciated in real terms.

Chart 2.11: Increase of the unit costs of the manufacturing sector labor force in Morocco compared with other countries, Q2 2009 – Q2 2010 (in %)



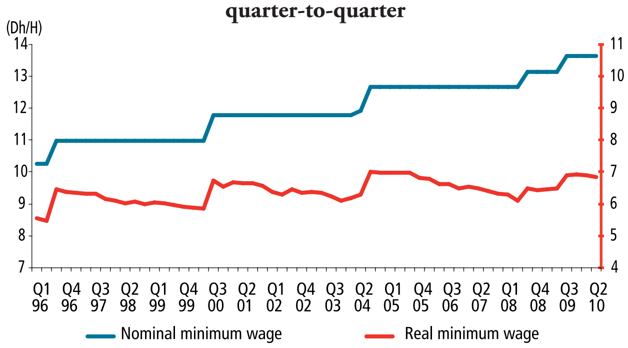
Sources: Datastream and BAM calculations

Chart 2.12: Change in the average wage index in the private sector in nominal and real terms, year-on-year



Sources: HCP, CNSS, and BAM estimates

Chart 2.13: Real and nominal minimum wage, quarter-to-quarter



Sources: Ministry of Employment, and BAM calculations

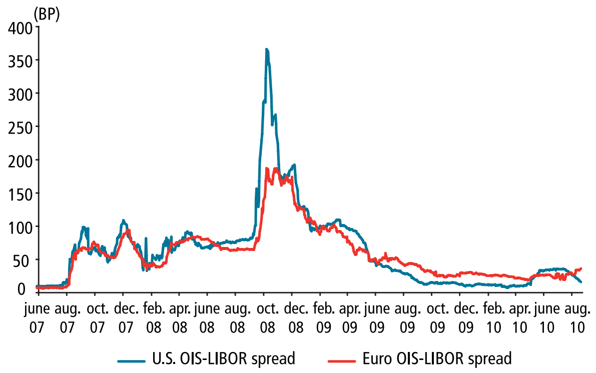
3. INTERNATIONAL ENVIRONMENT AND IMPORT PRICES

After the deterioration revealed in the latest Monetary Policy Report, international financial conditions improved in the United States and less markedly in the euro area. The calm spell on European financial markets, which resulted from easing of concerns about the sovereign debt developments and the successful fund-raising in some countries, is still weak and accompanied with strong investor risk-aversion. More recent data show that recovery continued throughout the last four months, mainly on the back of strong growth in emerging countries. In the advanced countries, national accounts for the second quarter of 2010 and high-frequency indicators of July 2010 show differences in trends between countries. Growth in the United States was more moderate in the second quarter of 2010, following the strong recovery that began in the fourth quarter of 2009. Growth in our key trade partner, the euro area, accelerated in the second quarter, driven essentially by the rebound in Germany's GDP. As for the short-term outlook, available data show upward revisions in growth outlook for 2010 in the main emerging and advanced economies. Nevertheless, the recent financial strains, particularly in European markets, could act as drags on growth during the coming months, mostly in Europe. World inflation, which has trended upward since November 2009, accelerated further in July 2010, year-on-year, following the recovery in commodity prices, particularly of oil and food produce. Inflation in the short run should however remain subdued in advanced countries, as the growth outlook is still modest and the output capacity utilization continues to show weakness. International developments, which constitute a source of the easing in external inflationary pressures, are expected to contribute slightly to the consolidation in nonagricultural growth.

3.1 Global financial conditions and economic activity

During the quarter under review, financial markets remained unstable, and particularly marked by pressures in advanced countries' sovereign debt markets. This instability is more noticeable in the euro area than in the United States. Regarding the economic activity, growth in the euro area accelerated substantially, while the pace of recovery in the United States slowed somewhat and growth drivers seem less dynamic, which would require the introduction of new fiscal and monetary policy measures.

Chart 3.1: Change in the OIS-LIBOR spread



Source: Datastream

3.1.1 Financial conditions

Money markets, notably in the euro area, continued to suffer from pressures. The 3-month Euribor maintained the upward trend it began in May 2010, and achieved 0.91 percent on August 6, 2010, its highest level in last year, after 0.78 percent early last month. The strains on interbank markets in the euro area can be explained mainly by uncertainties over banks' commitments with regard to sovereign debt in troubled countries. Inversely, the lull observed last month is ongoing on the U.S. money market and the 3-month dollar Libor moved from 0.45 percent at the end of July to 0.30 percent in August. Consequently, the OIS-Libor[1] gap moved from 27.8 basis points at the end of July 2010 to 33 points in August 2010 in the euro area, while it receded from 26.9 basis points to 11.4 points in the United States. Overall, these gaps are largely higher than their 2006 pre-crisis levels, by 3 basis points in the euro area and 7 points in the United States.

In August 2010, there was a very moderate increase in stock market indexes in advanced and emerging economies, owing to the uncertainties over economic developments and the multiplication of unfavorable business indicators mainly on the U.S. real estate and labor markets. Turning to the main relevant indexes in advanced economies, the Nikkei rose by 0.2 percent and the DAX by a peak 1 percent in August, compared with a month earlier. Similarly, the main indexes in emerging countries rose by 3.5 percent, as evidenced by the trends observed in the MSCI EM[2].

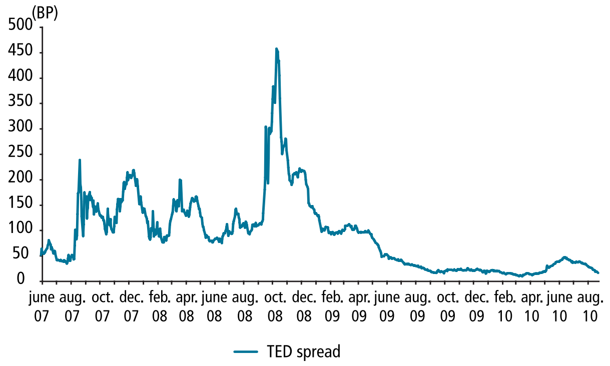
Lending growth in advanced economies has recently stabilized at positive rates. In the euro area, the lending change rate picked up year-on-year from 0.5 percent in June 2010 to 0.9 percent in July. In the United States, after its contraction since September 2009, this rate stood at 0.6 percent in July 2010, compared with -1.4 percent a month earlier.

There was an improvement in bond markets, as evidenced by the slackening in yields on bonds in most advanced countries. Yields on ten-year government bonds in Portugal, Spain and Italy dropped in August 2010 to 5.18 percent, 4.08 percent and 3.8 percent, respectively, from 5.39 percent, 4.41 percent and 4.01 percent a month

1 The OIS-LIBOR spread reflects an interest-rate risk and is equivalent to the difference between the three-month interbank rate (Libor eurodollar) and overnight indexed swap rates (OIS) with the same maturity.

2 The MSCI EM index measures equity market performance in countries of Central Europe, the Middle-East and Africa (Czech Republic, Hungary, Poland, Russia, Turkey, Israel, Jordan, Egypt, Morocco, and South Africa).

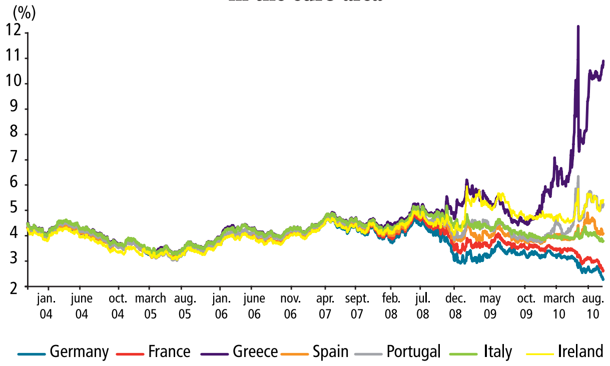
Chart 3.2: Change in the TED spread[1]



Source: Datastream

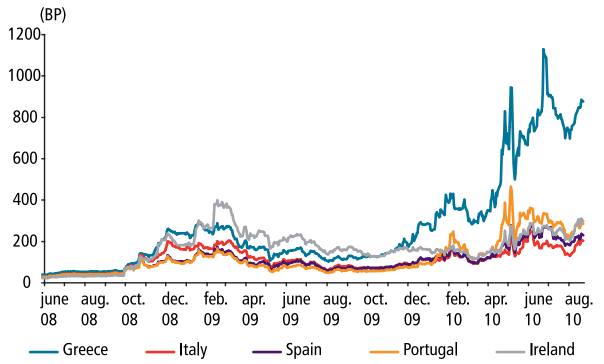
1 The TED spread represents a credit risk and corresponds to the difference between the interest rate on three-month Treasury bills and the three-month interbank rate in US dollars.

Chart 3.3: change in rates of ten-year government bonds' yields in the euro area



Source: Datastream

Chart 3.4: Change in CDS[2] in euro area peripheral countries



Source: Datastream

2 Credit Default Swaps (CDS) on the sovereign debt of emerging countries corresponds to insurance premiums against the default risk of a given sovereign debt.

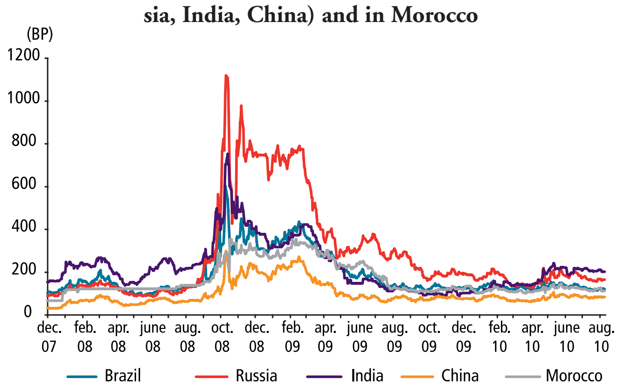
earlier. Likewise, yields on Germany's Bund and France's government bonds over the same period declined from 2.65 percent and 2.98 percent, to 2.36 percent and 2.68 percent, respectively. However, bond markets are still exposed to pressures stemming mainly from the risk of rating degradation in a number of advanced countries, which have been thus far sheltered from these pressures. Broadly, the trends observed in yields on government bonds in advanced countries certainly point to a return of confidence in States' solvency, but can also reflect a risk aversion, which causes investors to clearly prefer safe-haven currencies represented by sovereign securities.

Moreover, credit default swaps (CDS) in advanced economies, notably in European countries, continued to trend upward, reflecting persistent uncertainties over the situation of their public finance. In emerging countries, by contrast, CDS remained at quite low levels.

On the exchange markets, the euro appreciated against the dollar at an average monthly rate of $1.29 in August, compared with $1.28 a month earlier. On a month-to-month basis, the single currency in August 2010 appreciated by 0.8 percent against the dollar, but declined 1.6 percent against the Japanese yen and 1.5 percent against the pound sterling. In August, the yen reached a record high against the dollar, as the latter traded on average at 85.5 yens, its lowest since 15 years.

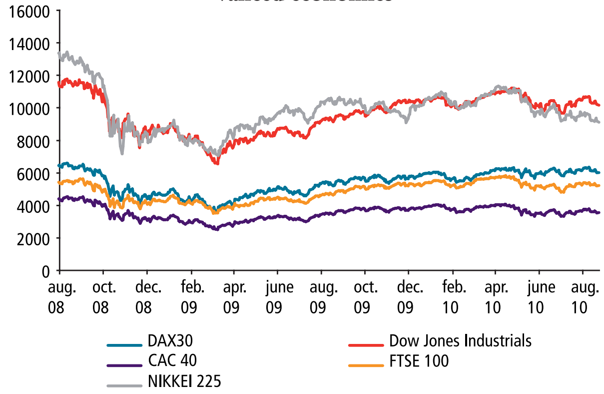
Under these circumstances, the main central banks in advanced economies, following their meetings in August 2010, decided to maintain the status quo and postpone the implementation of exit strategies. Consequently, the ECB kept its key rate unchanged at 1 percent. Likewise, the U.S. Federal Reserve, during its latest meeting on August 10, 2010, kept its key rate at a range between 0 percent

Chart 3.5: Change in CDS in emerging countries (Brazil, Russia, India, China) and in Morocco



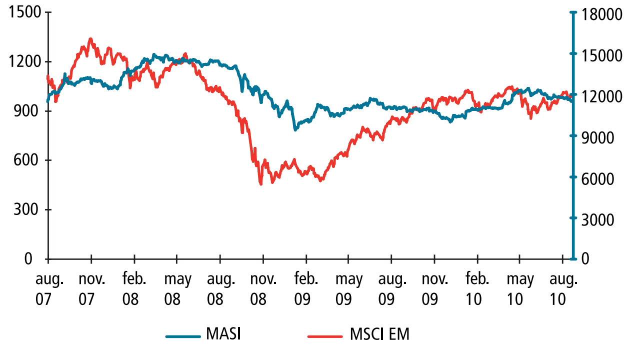
Source: Datastream

Chart 3.6: Change in the main stock market indexes in advanced economies



Source: Datastream

Chart 3.7: Change in the MSCI EM and MASI indices



Source: Datastream

and 0.25 percent, and decided to repurchase U.S. government bonds to support the economy. This mechanism consists in reinvesting mortgage-backed securities and those of Fannie Mae and Freddie Mac, which were held during the crisis by the Fed, in U.S. treasury bonds. Similarly, the Bank of England kept its key rate unchanged at 0.5 percent and did not rule out the possibility to extend its quantitative easing measures.

Although the transmission of sovereign risks is limited to the financial sphere, as indicated by the trends observed at the end of August, there are growing chances that real economy would suffer from adverse effects, particularly in case of hasty exit from the unconventional fiscal policy measures.

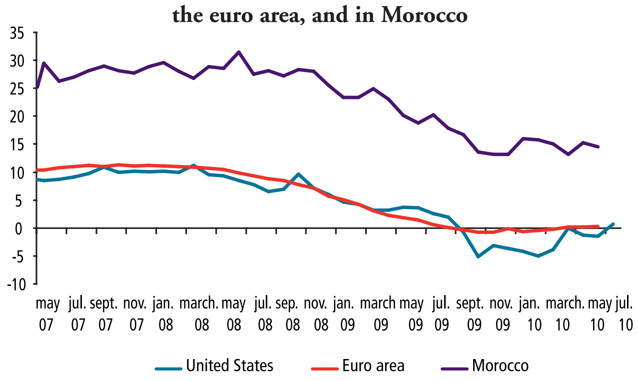
3.1.2 Global economic activity

Recent indicators show an ongoing world economic recovery in the second quarter of 2010, supported by the vigorous growth in emerging and developing countries, especially in Asia and Latin America. Advanced economies, however, showed uneven trends marked by an accelerated growth in the euro area and a slowdown in the United States.

Economic growth remained strong in Asian emerging economies, particularly in China, where GDP in the second quarter of 2010 rose to 10.3 percent year-on-year, after 11.9 percent a quarter earlier, partially supported by the momentum in household consumption.

In the United States, growth in the second quarter of 2010 continued but at a slower pace. This development would mainly reflect the increase in imports and the slowdown in corporations'

Chart 3.8: Year-on-year change of loans in the United States, the euro area, and in Morocco



Source: Datastream

Table 3.1: Global growth outlook

	Forecasts					
	World Bank		OECD*		IMF*	
	2010	2011	2010	2011	2010	2011
Global GDP	3.3	3.3	-	-	4.6	4.3
United States	3.3	2.9	3.2	3.2	3.3	2.9
Euro area	0.7	1.3	1.2	1.8	1	1.3
Germany	1.6	1.9	1.9	2.1	1.4	1.6
France	1.6	1.9	1.7	2.1	1.4	1.6
Italy	0.8	1.4	1.1	1.5	0.9	1.1
Spain	-0.6	1	-0.2	0.9	-0.4	0.6
United Kingdom	1	1.8	1.3	2.5	1.2	2.1
China	9.5	8.5	11.1	9.7	10.5	9.6
India	8.2	8.7	8.3	8.5	9.4	8.4
Brazil	6.4	4.5	6.5	5	7.1	4.2
Russia	4.5	4.8	5.5	5.1	4.3	4.1

**OECD (May 2010); World Bank (June 2010); IMF (July 2010)*

Sources: IMF, World Bank and OECD.

Table 3.2: Quarterly growth change, on a year-on year basis

	2009				2010	
	Q1	Q2	Q3	Q4	Q1	Q2
United States	-3.8	-4.1	-2.7	0.2	2.4	3.0
Euro area	-5.2	-4.9	-4.1	-2.1	0.6	1.7
France	-3.9	-3.1	-2.7	-0.5	1.2	1.7
Germany	-6.6	-5.5	-4.4	-2	2	3.7
Italy	-6.5	-6.1	-4.7	-2.8	0.5	1.1
Spain	-3.3	-4.2	-4	-3.1	-1.3	-0.2
China	6.2	7.9	9.1	10.7	11.9	10.3

Sources: Eurostat, Datastream and US Trade Department inventories. Despite its quarter-on-quarter slowdown, the U.S. GDP grew by a 3 percent year-on-year rate in the second quarter, after 2.4 percent in the previous quarter.

In the euro area, which saw a moderate recovery since the third quarter of 2009, growth picked up in the second quarter, with GDP increasing at a year-on-year 1.7 percent, compared with 0.6 percent a quarter earlier. This growth mainly reflects the marked performance of Germany, where GDP rose by a year-on-year 3.7 percent. Regarding Morocco's main partners, Spain's and Italy's GDP in the second quarter grew at respective year-on-year rates of -0.2 percent and 1.1 percent, compared with -1.3 percent and 0.5 percent in the previous quarter. France's GDP increased at 1.7 percent, from 1.2 percent a quarter earlier.

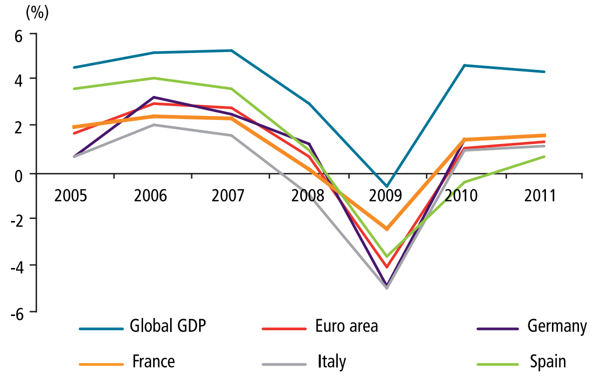
In Japan, economic growth slowed down in the second quarter, with GDP growing at 0.1 percent, after 1.1 percent a month earlier, owing to the decline in domestic demand.

Recent high-frequency indicators, which seem to evolve less compatibly with growth figures in some advanced countries, continue to suggest a short-term sustained recovery.

In the United States, the manufacturing output index posted a new annual increase of 13.5 percent in July and reached 55.5 points. In the euro area, the PMI composite index in July rose to 56.7 points, from 55.6 points in June, up 20.6 percent year-on-year. The PMI manufacturing index in the euro area stood at 56.7 in July, after 55.6 in June, up 22.5 percent year-on-year.

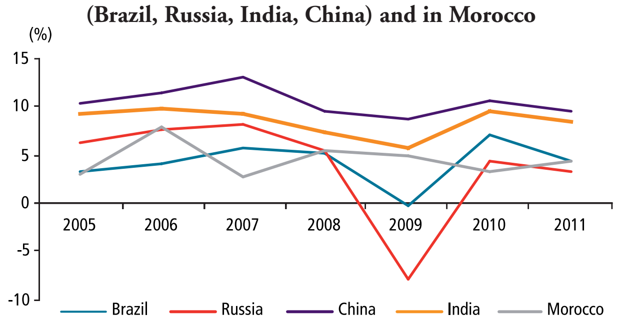
Despite these broadly supportive trends in sectoral indexes, unemployment rate remained elevated. In the United States, it stabilized at 9.5 percent in July 2010, compared with a month earlier. Likewise, in the euro area, it remained

Chart 3.9: Year-on-year GDP change in the world, the euro area and in partner countries



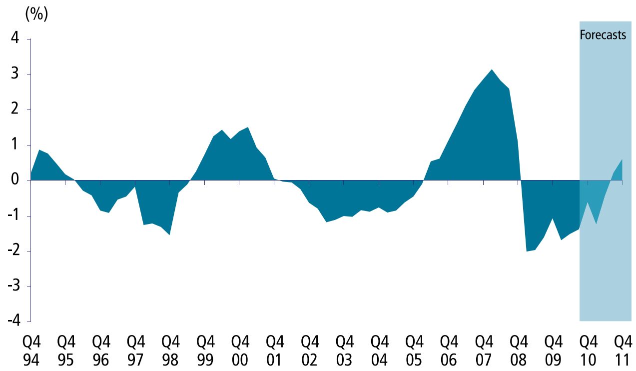
Source: IMF

Chart 3.10: GDP change in emerging countries (Brazil, Russia, India, China) and in Morocco



Source: IMF

Chart 3.11: Output gap of the main partner countries



Sources: European Commission and BAM calculations unchanged at 10 percent from one month to the next. In partner countries, recent available data show that unemployment rate increased both in France and in Spain, to 10 percent and 20 percent, from 9.9 percent and 19.8 percent, respectively, a month earlier.

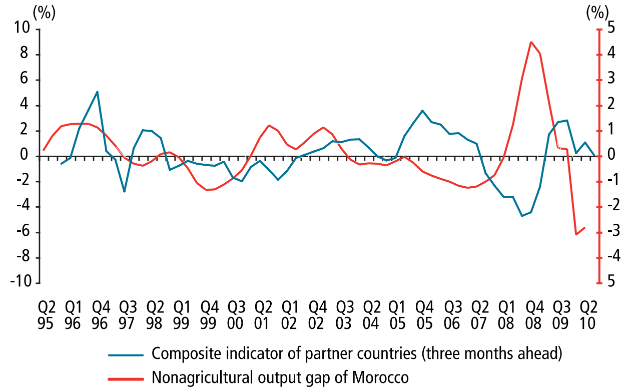
The IMF July World Economic Outlook points to an overall improvement, compared with the April outlook.

Concerning the outlook for the euro area, the IMF integrates uncertainty factors surrounding the future developments in financial markets and focuses on the appropriate measures to put in place, in order to strengthen medium-term growth outlook.

Consequently, the IMF expects the euro area's GDP to increase by 1 percent in 2010, a rate identical to that expected by the January 2010 outlook. The IMF outlook for 2011 was revised downward from 1.5 percent to 1.3 percent. In Morocco's main partners, the IMF outlook for 2010 and 2011 projects the GDP to grow by 1.4 percent and 1.6 percent both in France and in Germany, and by 0.9 percent and 1.1 percent in Italy. In Spain, however, the IMF expects the GDP to contract by 0.4 percent in 2010 before rising by 0.6 in 2011. In the United States, the IMF expects the GDP to grow by 3.3 percent and 2.9 percent in 2010 and 2011, respectively (compared with 3.1 percent and 2.6 percent under the January outlook). In Japan, the GDP is expected by the IMF to grow by 2.4 percent and 1.8 percent in 2010 and 2011, respectively (compared with 1.9 percent and 2.0 percent under the previous outlook).

Recent forecasts by the World Bank expect global GDP to grow by 3.3 percent and 3.5 percent in 2010 and 2011, respectively (compared with 2.7 percent and 3.2 percent under its January edition). For the United States, the World Bank revised upward GDP growth outlook to 3.3 percent and 2.9 percent in 2010 and 2011, respectively

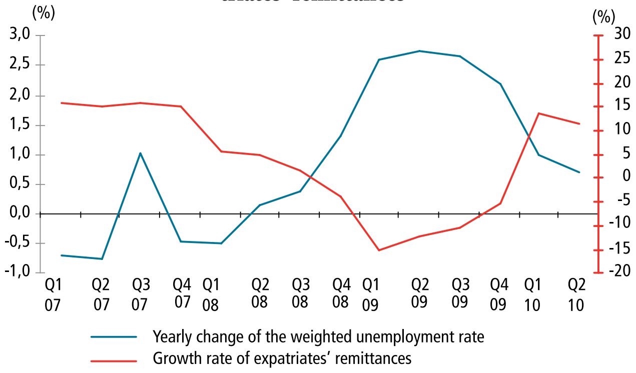
Chart 3.12: Weighted Composite Leading Indicator of partner countries*



**The Weighted Composite Indicator of partner countries is prepared on the basis of the cyclical component of the OECD Composite Leading Indicator (CLI) in Morocco's main partner countries (France, Spain, Germany and Italy), weighted by the share of these countries in Morocco's exports.*

Sources: OECD, and BAM calculations

Chart 3.13: Year-on-year change of main partner countries' weighted unemployment rate and of the growth rate of expatriates' remittances*



** The Weighted unemployment indicator is prepared on the basis of the unemployment rate in Morocco's main partner countries (France, Spain, Germany, Italy, Benelux, United States, the Netherlands and United Kingdom), which constitute, by themselves, 90.1 percent of Moroccan expatriates' remittances, weighted by the share of these countries in these remittances.*

Sources: Datastream and BAM calculations

Table 3.3: Recent trend in world inflation, on a year-on year basis

	july 2009	may 2010	june 2010	july 2010	Forecasts 2010	Forecasts 2011
United States	-2.1	2	1.1	1.2	2.1	1.7
Euro area*	-0.7	1.6	1.4	1.7	1.1	1.3
Germany	-0.5	1.2	0.9	1.2	0.9	1
France	-0.7	1.6	1.5	1.7	1.2	1.5
Spain	-1.4	1.8	1.5	1.9	1.2	1
Italy	0	1.4	1.3	1.7	1.4	1.7
Japan	-2.2	-0.9	-0.7	-	-1.4	-0.5
China	-2	0.6	1.9	1.5	3.1	2.4

(*) Harmonized indexes

Sources: IMF, Eurostat, BAM forecasts for Morocco, and IMF forecasts for other countries (compared with 2.5 percent and 2.7 percent). On the opposite, projections for the euro area were adjusted downward to 0.7 percent and 1.3 percent (from the 1 percent and 1.7 percent forecast by the World Bank in January).

3.2 World inflation

Against a background of slow but sustained economic recovery and rising commodity prices, the Eurostat preliminary data show that inflation in the euro area edged down to 1.6 percent in August 2010, from 1.7 percent a month earlier.

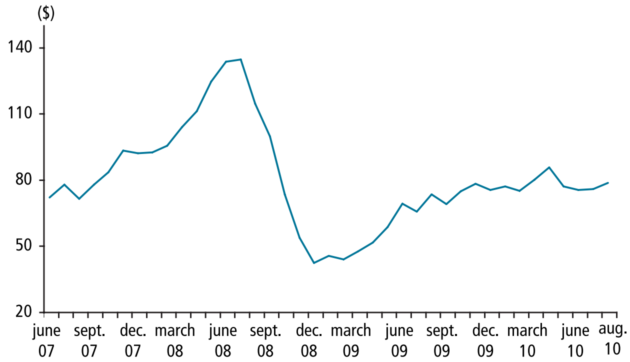
July data show a moderate inflation increase in most advanced and emerging countries (table 3.2).

Inflation in the euro area stood at 1.7 percent in July, after 1.4 percent a month earlier. In Morocco's partner countries, inflation in Italy and Spain accelerated to 1.9 percent and 1.7 percent, respectively, compared with 1.5 percent and 1.3 percent. In France and Germany, consumer prices moved up to 1.7 percent and 1.2 percent, respectively, from 1.5 percent and 0.9 percent a month earlier.

In the short run, the IMF July World Economic Outlook show that consumer prices in advanced countries would rise by 1.4 percent and 1.3 percent in 2010 and 2011, respectively. In emerging and developing countries, inflation is also expected to rise by 6.3 percent and 5 percent in 2010 and 2011, respectively.

In light of the latest developments in the global economic situation, inflation in the medium term would continue to move up moderately, notably in advanced countries, since growth prospects remain modest and the capacity utilization rate is still weak.

Chart 3.14: World oil price (Brent)



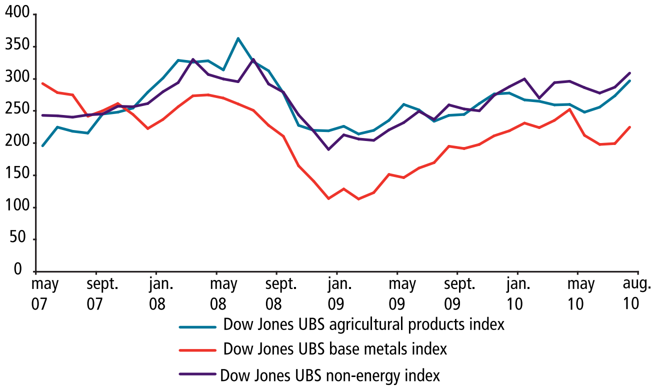
Source: Datastream

Table 3.4: Forecasts of the current price of oil (Brent) in the futures market (in US dollars)

Q3:10	Q4:10	Q1:11	Q2:11	2011	2012	2013
79.16	80	81	83.5	86.75	92	87.5

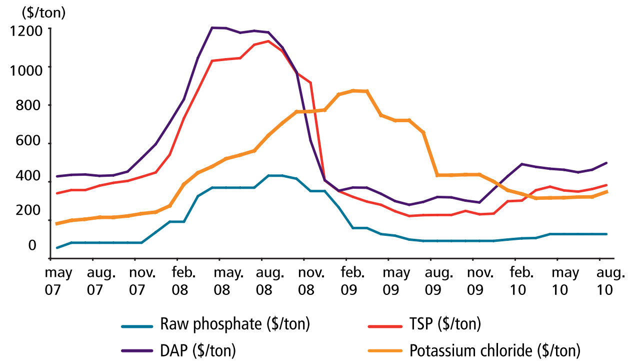
Source: Bloomberg

Chart 3.15: Change of the Dow Jones UBS indices of non-energy commodity prices (base year= 2006)



Source: Datastream

Chart 3.16: Change in the world prices of phosphates and derivatives



Source: World Bank

3.3 Oil prices

Oil prices were higher by a 2.3 percent average in August than in July and stood at $76.9 a barrel. This increase can be explained by the growth in demand, which was mainly driven by China, India, the Middle East and Latin America. Over the first eight months of 2010, Brent prices posted a year-on-year 37.3 percent increase.

The IMF July 2010 World Economic Outlook expects oil prices to average $ 75.24 a barrel in 2010 and $ 77.50 a barrel in 2011. The International Energy Agency (IEA) revised upward its projections on global demand for oil in 2010 and 2011, which should now reach 86.6 and 87.9 million barrels a day. Likewise, the OPEC expects demand for oil to increase to 85 million barrels a day in 2010, but keeps its projections for 2011 unchanged.

On the futures market, oil prices would stand on average at $ 86.75 a barrel in 2011, $92.00 in 2012, and $ 87.50 in 2013.

3.4 Non-energy commodity prices

In July and August 2010, there was an increase in non-energy commodity prices, reflecting a price rise both in base metals and in agricultural commodity. Consequently, the non-energy Dow Jones-UBS commodity index grew by 3.3 percent in July and 7.6 percent in August, month on month. It was 19.1 percent higher than in August 2009.

The Dow Jones-UBS base-metal index in August 2010 rose by 12 percent month-on-month and by 14.6 percent year-on-year, mainly because of the decline in the dollar and the stronger demand in emerging countries.

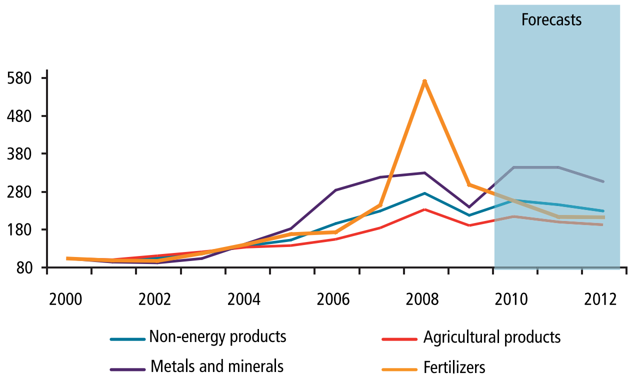
The Dow Jones-UBS agricultural index followed the same pattern, and increased by 22 percent

Table 3.5: Quarterly change of wheat futures and forecasts

Wheat (USc/ bushel)	Q3:10	Q4:10	Q1:11	Q2:11	2011	2012
Futures	664.8	737.34	749.43	727.38	709.5	693.56
Forecasts	550	560	600	630	630	639.62

Source: Bloomberg

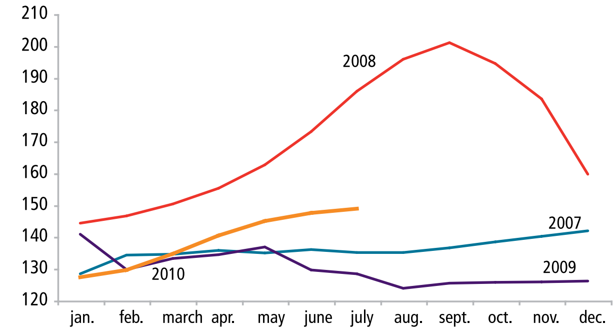
Chart 3.17: Change perspectives of commodity price indices*



(*) Updated on July 11, 2010

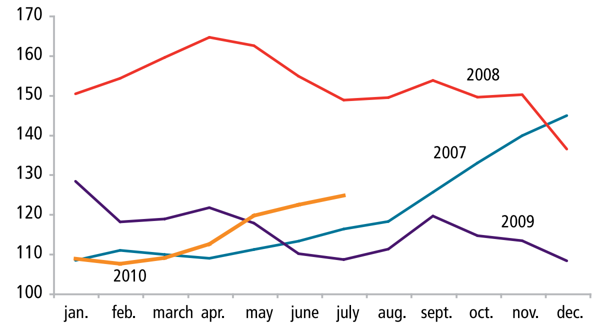
Source: World Bank

Chart 3.18: Non-energy import price index (Base year: 1996)



Sources: HCP, and BAM calculations

Chart 3.19: Food products' import price index (Base year: 1996)



Sources: HCP, and BAM calculations

year-on-year and by 8.5 percent month-on-month. Pressures on the prices of agricultural products stemmed from the rapid increase in demand from emerging economies, the hike in wheat prices due to the extreme weather conditions in Russia and Eastern Europe in July 2010, as well as the rise in cotton prices following the adverse supply shocks resulting from the floods in Pakistan and China.

Prices of phosphate and its derivatives also increased in August 2010. DAP and TSP prices rose by 7.5 percent and 5.7 percent month on month and by 55.7 percent and 62.2 percent year on year. Crude phosphate prices maintained the same level observed since April 2010, $125 a ton.

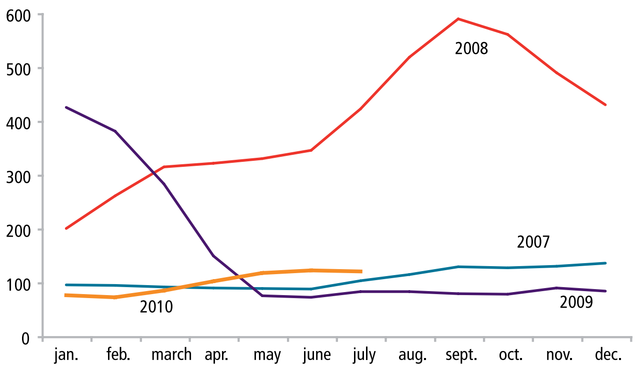
The hike in commodity prices should continue in the short term, owing to the increasing global demand, while the inventories of the various products could decline significantly.

3.5 Morocco's import unit value index

Recent available data indicate that the non-energy import price index (IPI) increased in July 2010 at a monthly rate of 0.9 percent, compared with 1.7 percent in June. Food product IPI grew by a month-on-month 1.9 percent, compared with 2.3 a month earlier, owing mainly to the rise in the unit import price of wheat (by 3.8 percent) and of corn (by 2 percent). At the same time, semi-finished products' IPI rose at a monthly rate of 1.8 percent, down from 2.1 percent in June, owing to the 1.9 percent increase in the average unit import price of plastics. On the other hand, the IPI of mining products declined at a monthly rate of 1.3 percent, after growing by 4.1 percent a month earlier, due to a 3.3 percent drop in the unit import price of iron and steel.

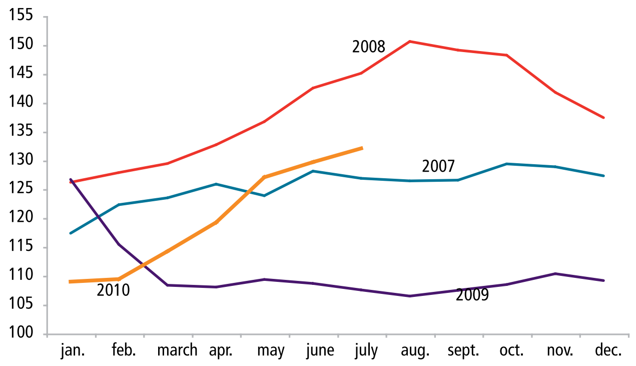
Year-on-year non-energy IPI rose by 15.9 percent, compared with 13.8 percent in June. Mining

Chart 3.20: Mining products' import price index (Base year: 1996)



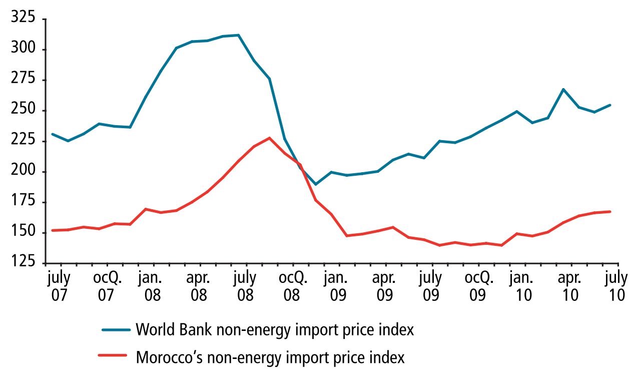
Sources: HCP, and BAM calculations

Chart 3.21: Semi-finished products' import price index (Base year: 1996)



Sources: HCP, and BAM calculations

Chart 3.22: Change of world commodity price index and domestic non-energy import price index (Base year: 2000)



product IPI increased by 46.1 percent, owing mainly to the 78.8 percent expansion in the unit import price of iron and steel. Similarly, food product IPI moved up by 14.8 percent, as the unit import price of wheat surged by 57.1 percent, and that of sugar rose by a moderate 5.7 percent. Meanwhile, semi-finished product IPI rose by 22.8 percent, following the 30.4 percent increase in the unit import prices of plastics.

In light of recent developments and the volatility in world commodity prices, import price-driven inflationary pressures, which are still moderate, could heighten in the coming quarters.

4. MONETARY CONDITIONS AND ASSET PRICES

Recent available data as at end July show the continued moderation in M3 annual growth, which increased by a modest 6.3 percent, down from 6.5 percent in the second quarter. Under these circumstances, monetary surplus remained virtually nil. At the same time, growth in bank credit, albeit at a slower pace, remained sustained, reaching 11.6 percent from 13.4 in the second quarter of 2010. Concerning lending rates, the BAM survey among banks for the second quarter of 2010 points to a decline in the weighted average lending rate, mostly because of the fall in interest rates on equipment loans and cash advances. The effective exchange rate of the dirham depreciated by 1 percent in nominal terms quarter-on-quarter and by 1.6 percent in real terms, as inflation rate in Morocco was generally lower than in the major partner and competitor countries. Property prices, according to the new real estate price index calculated by BAM, went up in the second quarter, after a decline in the first quarter. Altogether, the outlook for monetary and financial conditions suggests moderate pressure on inflation in the coming quarters.

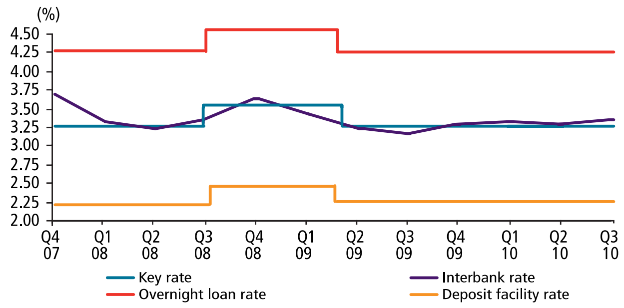
4.1 monetary conditions

4.1.1 Interest rates

In a context where risks are slightly skewed to the upside and the inflation central forecast is consistent with the price stability objective, the Bank Board decided at its meeting of June 15, 2010 to keep the key rate unchanged at 3.25 percent. Under these circumstances, the interbank overnight rate averaged 3.33 percent in July and August 2010, up by 6 basis points from the previous quarter.

Rates on short-term Treasury bills issued on the primary market reported a decline in the second quarter and July, reversing the upward trend that began in October 2009. Medium and long-term rates broadly fell somewhat. The same trend was observed on the secondary market, both in short-term yields as well as in medium and long-term maturities.

Chart 4.1: Change in the interbank rate*



** Observation of the second quarter of 2010 corresponds to the daily average of the period from July 1 to August 24.*

Table 4.1: Change in Treasury bonds' yield rates on the primary market

	2009				2010		July10
	Q1	Q2	Q3	Q4	Q1	Q2	
13 weeks	3.58	3.26	3.25	3.25	3.44	3.39	-
26 weeks	3.65	3.31	3.27	3.28	3.56	3.45	-
52 weeks	3.75	3.35	3.33	3.37	3.62	3.55	3.48
2 years	3.90	3.44	3.48	3.57	3.73	3.69	3.67
5 years	4.05	3.69	3.68	3.74	3.95	3.90	3.88
10 years	-	-	-	-	4.20	4.19	4.16
15 years	-	-	-	-	4.32	4.35	-

The weighted average rate of deposit rates on 6 and 12-month deposits, which remained stable in the second quarter, moved up in July by 3 basis points to 3.51 percent. This change reflects an increase by 3 basis points on 6-month deposit rates and 1 basis point on 12-month deposit rates.

Concerning lending rates, BAM survey among banks for the second quarter of 2010 indicates a drop in the weighted average rate of bank loans from 6.49 percent to 6.36 percent. This trend is mostly attributable

Chart 4.2: Change in maturity structure of TB interest rates

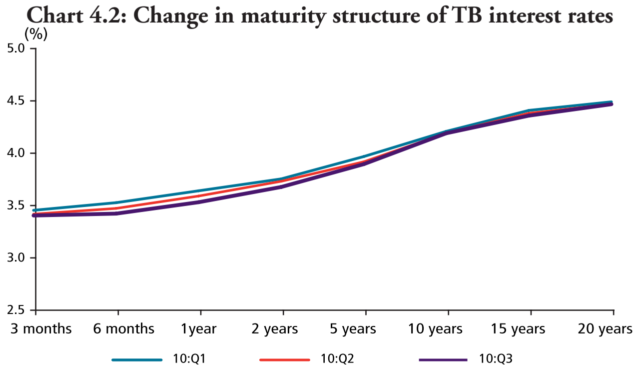


Table 4.2: Rates on time deposits

	2009				2010		
	Q1	Q2	Q3	Q4	Q1	Q2	july10
6 months	3.61	3.52	3.31	3.24	3.28	3.32	3.35
12 months	3.91	3.96	3.68	3.69	3.65	3.64	3.65
Weighted average	3.78	3.78	3.55	3.54	3.48	3.48	3.51

Box 4.1: Liquidity and monetary policy implementation

Despite the restrictive impact of the autonomous factors in the second quarter 2010, liquidity needs of the banking system stabilized at around 19 billion dirhams, following the Bank Board decision on March 30, 2010 to reduce the required reserve ratio by 2 percentage points. This cut resulted in an overall liquidity injection of 8.2 billion dirhams (5.2 billion dirhams on March 21, and 2.9 billion dirhams on April 21). Consequently, the average liquidity shortage narrowed from 19.3 billion dirhams in the first quarter 2010 to 18.7 billion dirhams in the second quarter.

Transactions in foreign assets led to a liquidity drain of 7.4 billion dirhams resulting from the difference between purchases of foreign currency by commercial banks with a total of 12.7 billion dirhams and sales of foreign banknotes, which totaled 5.2 billion dirhams.

The rise in currency in circulation reached 2.6 billion dirhams, following the cash outflows at the start of the summer season.

On the opposite, Treasury operations caused a liquidity injection of 2.8 billion dirhams, attributable to the repayment of domestic debt installments to the banking system (19.7 billion dirhams).

Overall, the autonomous factors exerted a restrictive effect of 7.3 billion dirhams on the banking system's liquidity.

Chart B 4.1.1: Change in liquidity position and in the weighted average rate in quarterly average

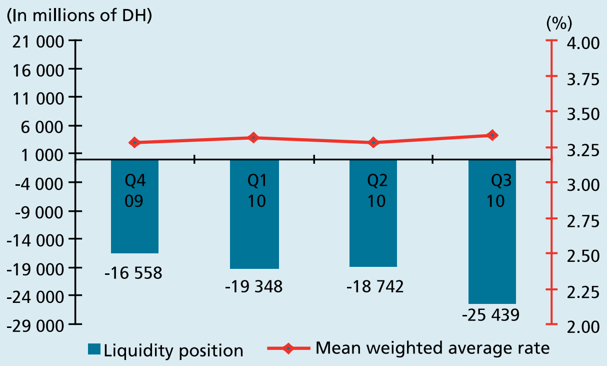
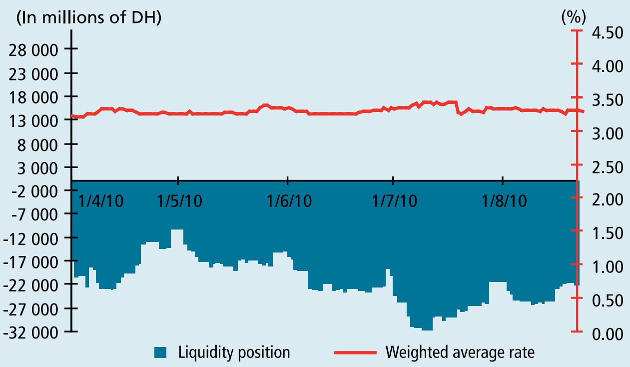


Chart B 4.1.2: Liquidity position and weighted average rate of the interbank money market



Notwithstanding the expansive effect of the autonomous factors in the third quarter 2010, the amounts injected by Bank Al-Maghrib increased from 15.6 billion dirhams in the second quarter to 23 billion in the third quarter due to the significant surpluses of the Treasury from tax receipts (second installment of corporate tax for fiscal 2010) which were not invested in the money market. As a consequence, average liquidity shortfall increased from 18.7 billion dirhams in the second quarter 2010 to 25.4 billion in the third quarter.

Indeed, transactions in foreign assets led to a liquidity injection of 7.2 billion dirhams resulting from the difference between sales of foreign banknotes which reached 10.2 billion dirhams and purchases of foreign currencies by commercial banks with a total of 3.1 billion dirhams. In contrast, Treasury operations adversely affected banks' liquidity by 418 million dirhams. Treasury assets amounted to 46.2 billion dirhams, including 6.5 billion corresponding to banks' purchases of Treasury bills at auctions. Treasury expenses stood at 45.8 billion dirhams, 14.4 billion of which correspond to the repayment of domestic debt to the banking system. Moreover, currency in circulation increased by 5.1 billion dirhams in conjunction with the summer vacations.

Altogether, the autonomous factors exerted an expansive impact of 1.6 billion dirhams on the banking system's liquidity.

Chart B 4.1.3: Change in reserve requirements

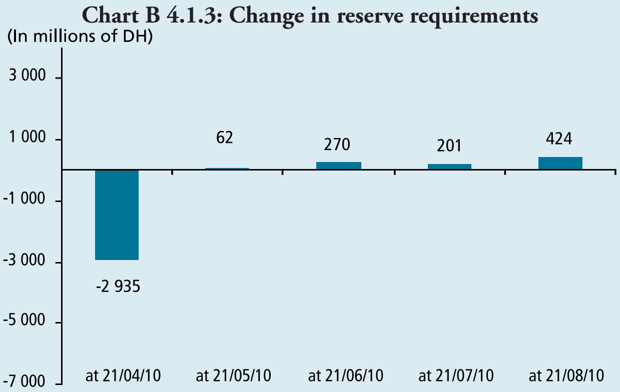
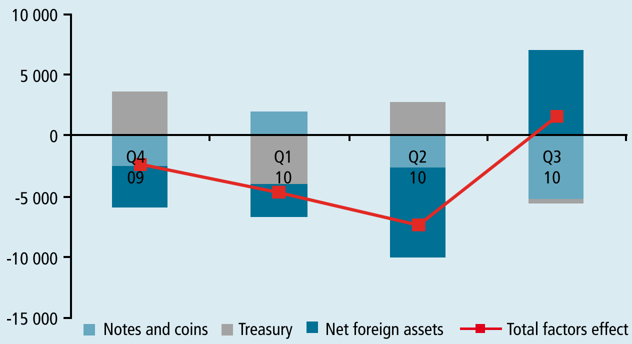


Chart B 4.1.4: Change in liquidity factors' effect



In order to overcome the shortage in banks' liquidity, which averaged 25.4 billion dirhams during this quarter, Bank Al-Maghrib intervened through the 7-day advances at an average daily amount of 22.9 billion dirhams. And to reduce the upward pressure exerted on the weighted average rate throughout the quarter, the Bank provided liquidity also by means of a repurchase agreement operation of an amount of 2 billion dirhams and overnight advances at amounts of 500 billion and 1 billion, respectively.

During the third quarter of 2010, the mean weighted average rate stood at 3.33 percent, up 6 basis points from the previous quarter. Its volatility increased by 1 basis point to 0.05 percent, from 0.04 percent previously, mostly because of the upward pressure on the weighted average rate in July and whose mean rose to 3.35 percent.

Chart B 4.1.5: BAM interventions on the money market

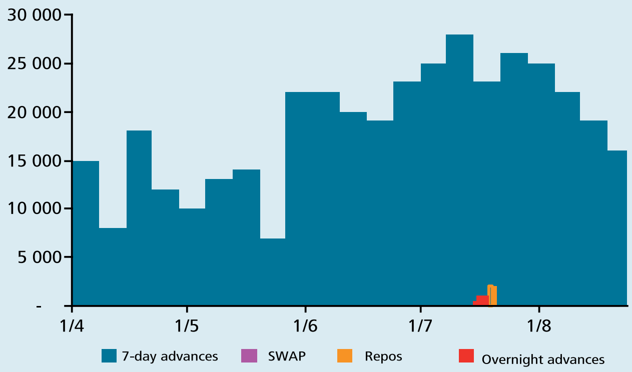
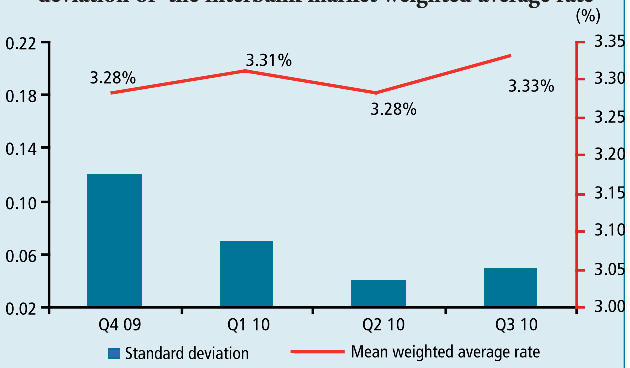
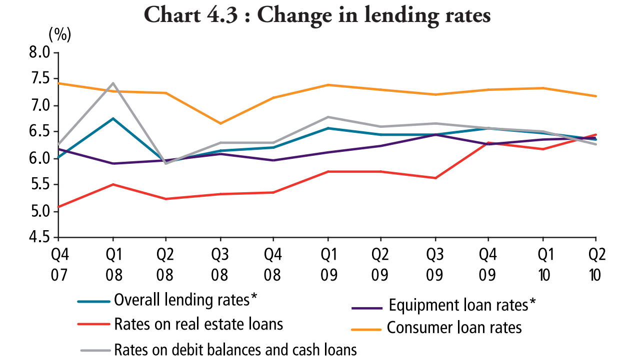


Chart B 4.1.6: Change in the mean and standard deviation of the interbank market weighted average rate



to a dip in rates on cash advances, and to a lesser degree a decline in consumer loan rates. In contrast, equipment loan rates remained broadly unchanged, while rates on real estate loans slightly adjusted upward, after the fall registered in the previous quarter.

Chart 4.3 : Change in lending rates

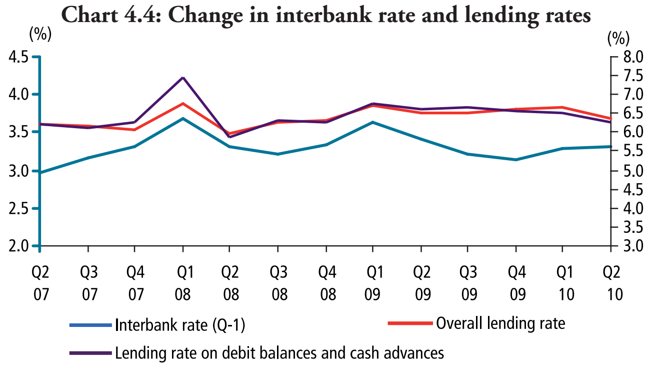


* *Revised series*

4.1.2 Money, credit and liquid investments

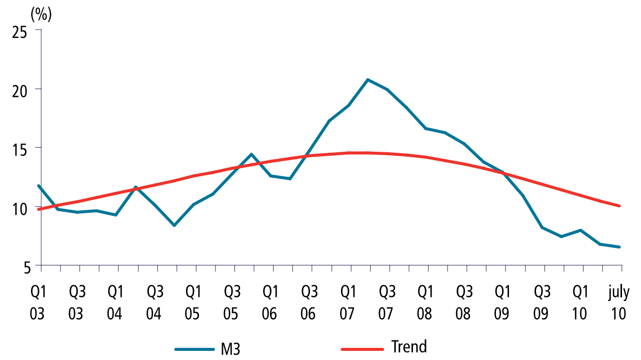
M3 growth

Chart 4.4: Change in interbank rate and lending rates



New monetary data, compiled since May 2010 in accordance with the methodology of the IMF's Monetary and Financial Statistics Manual, show further moderation in M3 annual growth, at 6.3 percent in July from 6.5 percent in the previous quarter. As a result, monetary surplus remained close to zero, indicating that monetary inflationary pressures remain largely under control in the short run.

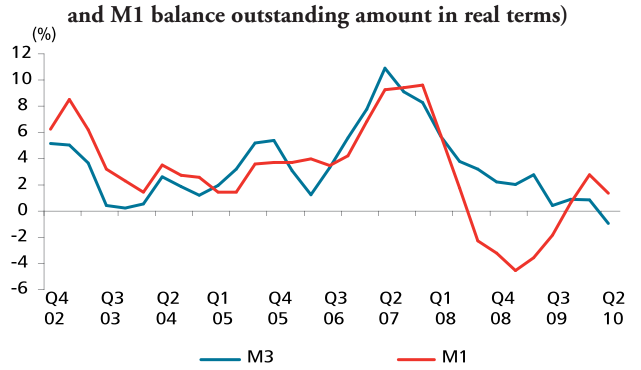
Chart 4.5: M3 growth and its trend, year-on-year



As well as the slowdown in bank credit and the decline in net foreign assets, this trend in M3 reflects different changes in the main components.

In fact, bank money grew at an annual rate of 7.3 percent in July, after hovering around 10.4 percent on average during the first half of the year. The slowdown was also reported in currency in circulation and demand deposits, the annual growth of which was limited to 5.8 percent and 7.4 percent, respectively, down from 6.2 percent and 8.2 percent a quarter before. Time deposits continued the downward trend observed since the beginning of the

Chart 4.6: Money surplus (in percentage of M3 and M1 balance outstanding amount in real terms)



year, declining by 7.3 percent in July, year on year. However, securities of money market UCITS, now included in broad money, positively contributed to M3 growth, registering a rise in July, after the slowdown that had begun early this year.

By economic agent, household deposits grew in July at an annual rate of 4.6 percent, close to the rates registered in the last two quarters. They thus remain the major contributor to the growth in deposits, as compared to private nonfinancial corporations whose contribution was much less significant. Nevertheless, public sector deposits still negatively contribute to the growth in deposits, particularly time deposits that recorded a year-on-year decline.

Bank loans

Latest available data suggest that growth in bank credit, albeit slower, remains generally strong. In July it grew at an annual rate of 11.6 percent, down from an average of 13.8 percent in the first half of the year.

The breakdown of loans by economic agent shows further deceleration in loans to private nonfinancial corporations, which recorded a year-on-year increase of 9 percent in July, down from 11.6 percent in the second quarter. Their contribution to credit growth therefore fell to 4.1 percentage points, from 5.3 percentage points in the second quarter.

Chart 4.7: Contribution of the major components to money supply growth

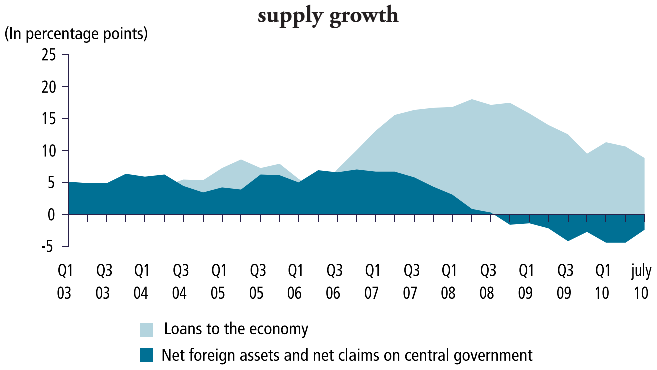


Chart 4.8: Year-on-year change in the major M3 components

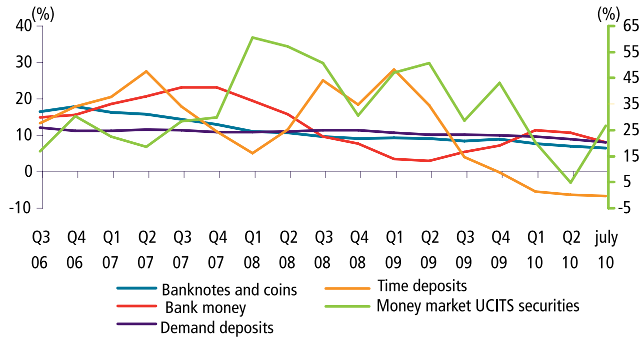


Chart 4.9: contribution of nonfinancial agents to the growth of total deposits

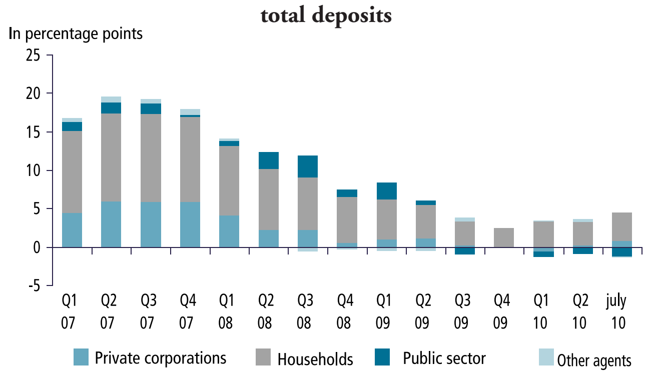
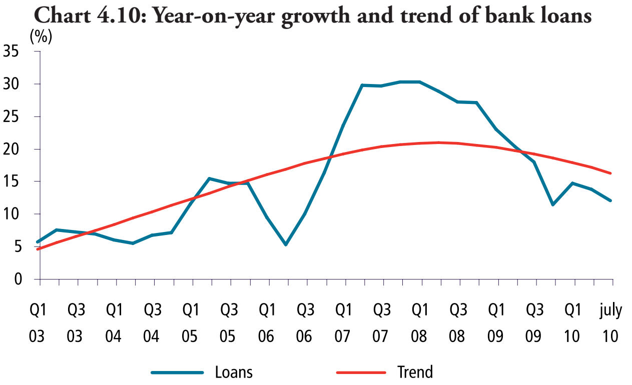


Chart 4.10: Year-on-year growth and trend of bank loans



Box 4.2: Impact of monetary statistics reform

Since June 2010, Bank Al-Maghrib has been publishing monetary statistics in accordance with the requirements of the IMF's Monetary and Financial Statistics Manual (MFSM), 2000. The adoption of this new methodology has involved an increase in money supply, mainly due to the inclusion of new economic agents in terms of money issuers and holders. Thus, money issuers, composed of financial corporations called "depository corporations", some liabilities of which are included in the new definition of money supply, now include money market UCITS in addition to Bank Al-Maghrib and commercial banks. Under the new methodology, securities issued by money market mutual funds meet the selection criteria for monetary assets, insofar as they are quickly and easily transformed into means of payment without significant risk of capital loss. Concerning the money-holding sector, it was expanded to all resident institutional sectors other than depository corporations and the central government. The purpose of this box is to analyze the impact of the changeover to the new methodology of monetary statistics on monetary policy implementation in BAM. The objective is to check whether the assessment of recent monetary pressures on prices would have been the same as if it were based on statistics of the old methodology. To this end, the analysis was focused on two main series that are most relevant to the analysis of monetary pressures, namely broad money and credit.

Chart B 4.2.1: Year-on-year M3 growth

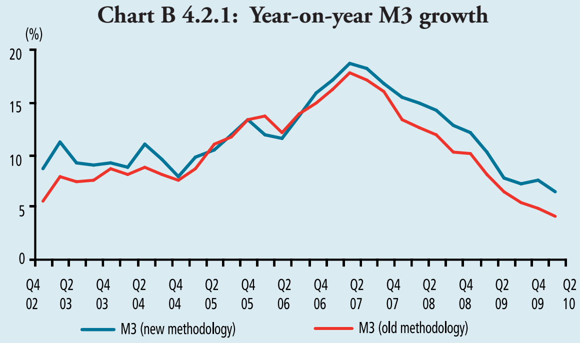
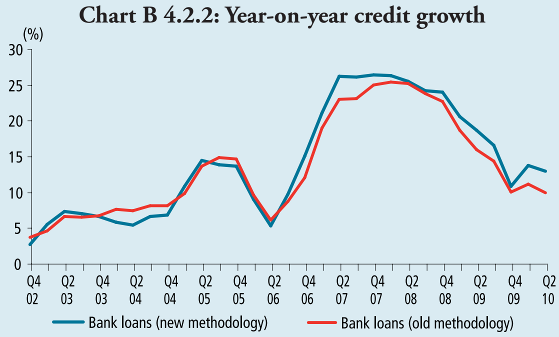


Chart B 4.2.2: Year-on-year credit growth



The new M3 and credit series grew at high rates until 2008, before scoring a reversal as from 2009, with a continued slowdown. Charts B4.2.1 and B4.2.2 trace similar change between old and new series and identify the correlation between turning points. It is certain that since the fourth quarter of 2008, the monetary surplus indicator in the old M3 series shows a sign opposite to that based on the new series. However, in both cases, this indicator was not significantly different from 0 (Chart B4.2.3).

Chart B 4.2.3: Monetary surplus growth, in real-terms

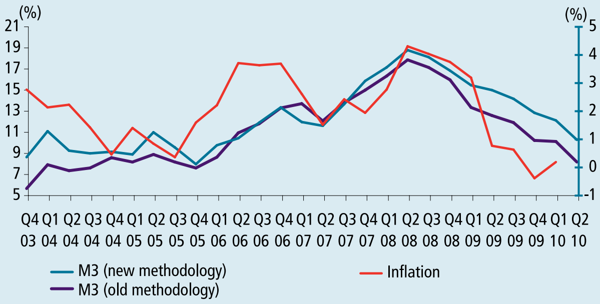
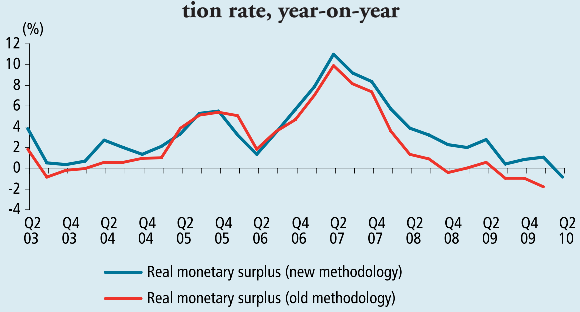


Chart B 4.2.4: Four-quarter lagged money supply and inflation rate, year-on-year



Moreover, the chart B4.2.4 suggests a positive correlation between, on the one hand, the annual changes in the old and new four-quarter lagged M3, and on the other hand inflation measured by the CPI year on year. Similarly, results of significance tests of M3 growth (Table B2.1) indicate that from the delay four, both the old and new M3 series significantly contribute to explaining the future evolution of inflation in Morocco (at a 5 percent threshold).

Table B 4.2.1 : Granger causality test between M3 (YoY) and inflation

Lag in quarters	Assumption	F-statistics	Probability
2	M3 (new series) does not cause inflation	2.36	0.12
2	M3 (old series) does not cause inflation	3.18	0.06
4	M3 (new series) does not cause inflation	7.29	0.00
4	M3 (old series) does not cause inflation	5.20	0.01
6	M3 (new series) does not cause inflation	4.86	0.01
6	M3 (old series) does not cause inflation	5.47	0.01
8	M3 (new series) does not cause inflation	4.12	0.07
8	M3 (old series) does not cause inflation	16.63	0.00

Sources : HCP and BAM calculations

In contrast, loans to households were up 11.2 percent from about 10 percent in the second quarter, with a contribution of 3.8 percentage points, up from 3.3 points in the previous quarter.

By economic purpose, credit growth points to diverging trends in the major categories. Cash advances were 1 percent down year on year in July, following an increase of 5.7 percent in the second quarter. Real estate loans and consumer loans reported a slowdown, as their annual growth rates stood at 10.4 percent and 14.7 percent in July, respectively, compared with 12 percent and 17.2 percent in the preceding quarter. On the opposite, the annual growth of equipment loans remains high, as it moved up from 23.1 percent in the second quarter to 26.2 percent in July.

Other sources of money creation

Net foreign assets in the second quarter of 2010 declined 8.2 percent, compared with the same period of last year, mostly because of the widening trade deficit and falling revenues from private foreign investments and loans. Despite a 2.7 percent increase in July, the highest in the last two years, the outstanding amount of foreign exchange reserves was 6.7 percent lower than the previous year.

Net claims on central government, after falling at an annual rate of 21.6 percent in the second quarter, were again down 8.8 percent in July, mainly due to the

Chart 4.11: Contribution of nonfinancial agents to credit growth

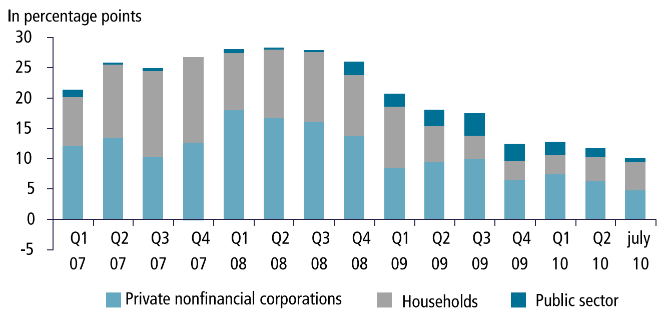


Chart 4.12: Annual growth of major bank credit categories

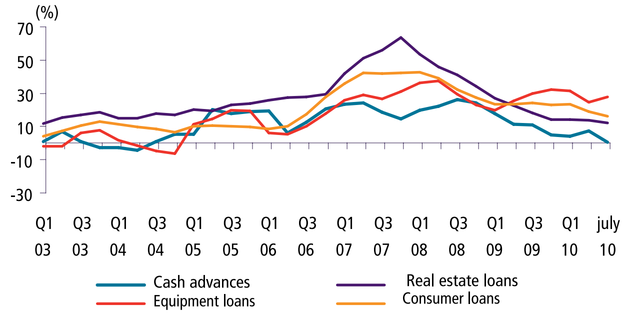


Chart 4.13: Contribution of the various loan categories to bank credit growth

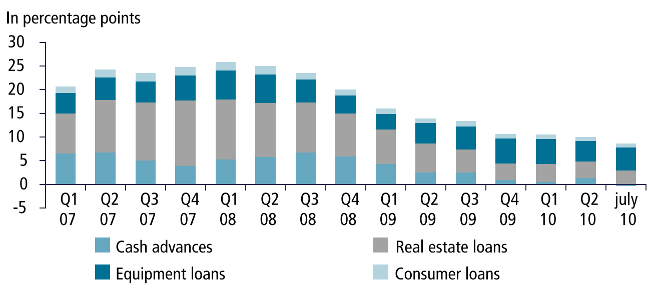
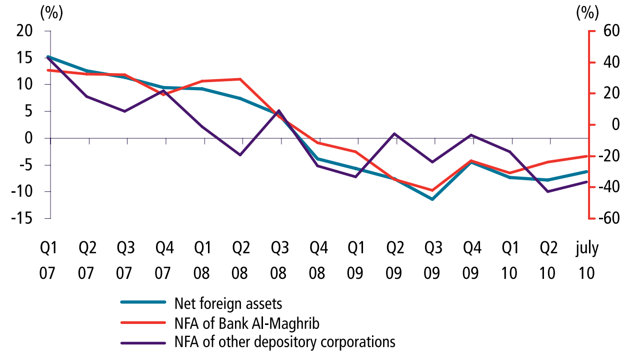


Chart 4.14: Annual growth of net foreign assets



decreasing net claims of other depository corporations.

Liquid investments

Liquid investment aggregates maintained momentum in July 2010, growing at an annual rate of 20.7 percent from 24.8 percent in the second quarter.

This trend is driven by the growth in assets included in LI1 aggregate, particularly negotiable Treasury bills that represent its major component. After the sizable increases reported in the first half-year, the outstanding amount of Treasury bills grew less rapidly in July year on year, mostly because of the small volume of transactions on the Treasury bill market. At the same time, securities of equity and diversified UCITS, included in the LI3 aggregate, continued to slow down, reflecting the trend in prices on the Casablanca stock market.

Securities of bond UCITS, comprised in the LI2 aggregate, again increased mostly due to the appreciation of their value under the effect of falling yields of secondary market TB.

Exchange rates

Over the second quarter of 2010 and compared with the previous quarter, the dirham appreciated by 1.55 percent against the euro. Similarly, it traded against the dollar, the Japanese yen and the pound sterling at rates lower than the averages reported in the previous quarter, at 6.71 percent, 5.23 percent and 2.30 percent, respectively. In July and August, the dirham on average appreciated

Chart 4.15: Quarterly change in the outstanding amount of net claims on the central government

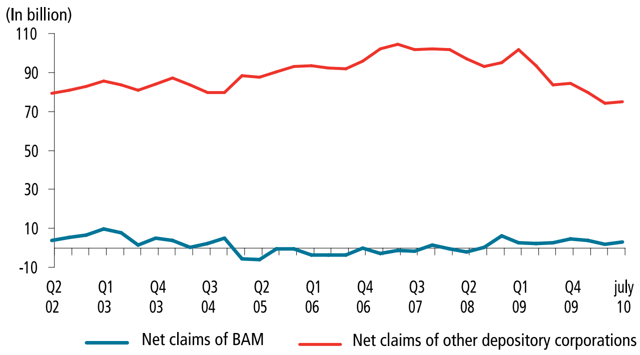


Chart 4.16: Annual change of liquid investments and time deposits

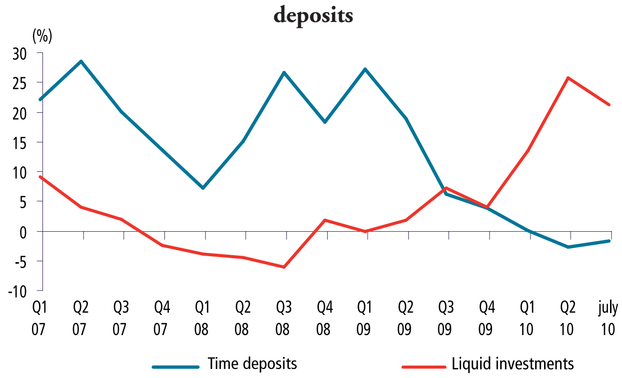


Chart 4.17: Change in LI1 and LI2 aggregates

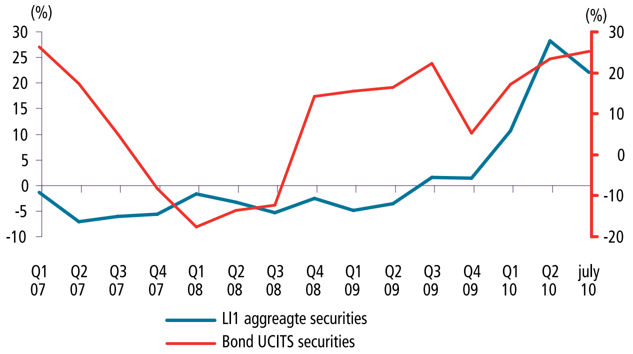
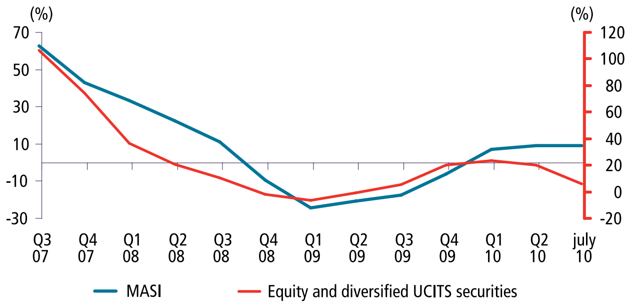


Chart 4.18: Annual growth of LI3 and MASI



1.03 percent against the dollar and fell 0.23 percent against the euro.

The dirham's nominal effective exchange rate, based on bilateral exchange rates with Morocco's major partners and competitors, again declined 1 percent quarter-on-quarter. In real terms, the dirham depreciated 1.6 percent, owing to a negative inflation differential.

4.2. Asset prices

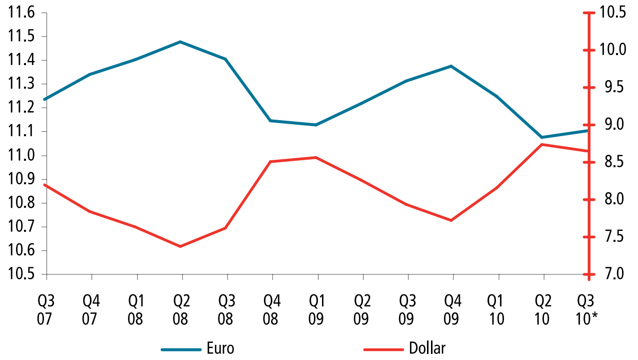
4.2.1 Real estate assets

Internationally, recent available data for the second quarter 2010 show the continued recovery in property prices, which started in the fourth quarter of 2009. In the United Kingdom, home prices increased by 4.6 percent year on year, while in Spain their declining pace was contained at 3.6 percent, from 4.5 percent in the first quarter.

In Morocco, the real estate price index (REPI) in the second quarter of 2010 rose 2.2 percent, compared with a 3.2 percent decline in the previous quarter. On a year-on-year basis, the REPI appreciated 1.4 percent, after the 2.1 percent contraction reported in the first quarter.

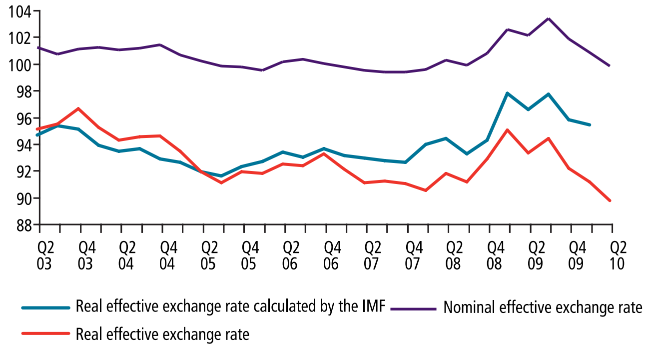
Meanwhile, sales of residential property registered at the Land Registry Office continued to trend downward in the second quarter of 2010, falling at an annual rate of 11 percent to 14,735 transactions. This decrease affected both apartments and houses, albeit at different proportions. However, sales of villas increased somewhat. As opposed to the previous quarter, the

Chart 4.19: Exchange rate of the dirham



**Observation of the third quarter of 2010 corresponds to the arithmetic average of data from July 1 to August 24*

Chart 4.20: Effective exchange rate (Base year= 2000)



Sources: IMF and BAM calculations

Chart 4.21: Year-on-year change in the real estate price index in Spain, United Kingdom, France and Morocco

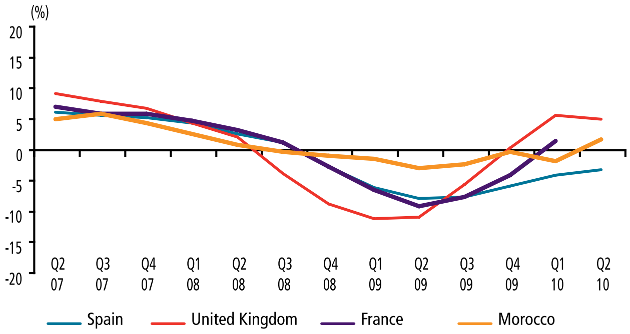
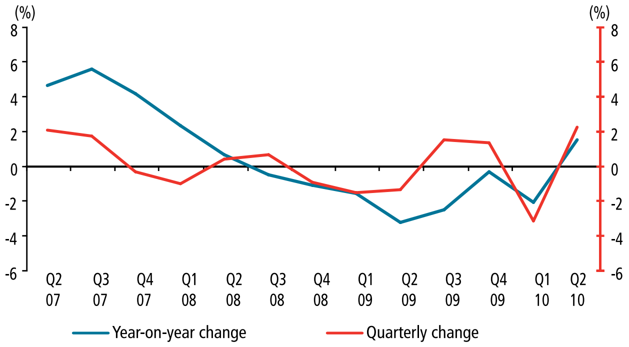


Chart 4.22: Real estate price index (REPI)



upward trend in real estate asset prices seems correlated to the uptrend in home loans, which increased by about 13 percent year on year. The stock exchange real estate index posted a 3.2 percent quarterly increase, but registered a sizable 15.3 percent decrease year on year.

4.2.2 Stock prices

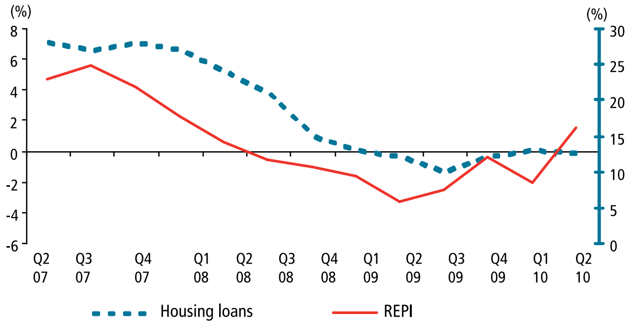
In the second quarter of 2010, the Moroccan All Share Index (MASI) gained 3.1 percent from the first quarter and 12.3 percent compared with last year. The index, however, lost 0.3 percent in August, after a slight rise of 0.1 percent in July. Likewise, the stock market real estate index increased by 1.36 percent over the second quarter, but decreased in August by 6.7 percent.

The PER of the Casablanca stock market moved up quarter-on-quarter from 16.9 to 18.1, and fell to 17.9 at the end of August, while remaining higher than in other stock markets of similar size. The price/book ratio was 3.2 in August.

Moreover, the volume of transactions increased by 39.8 percent to 58.6 billion dirhams in the second quarter, up from 42 billion dirhams a quarter earlier. It decreased to 13.6 billion in August.

Market capitalization increased by 1.6 percent in the second quarter to 569.5 billion dirhams. However, recent available data show a decline in August as market capitalization depreciated to 529.3 billion dirhams.

Chart 4.23: Year-on-year change in the REPI and housing loans*



** Housing loans do not include loans to real estate developers*

Chart 4.24: Year-on-year change in the REPI and the real estate stock market index

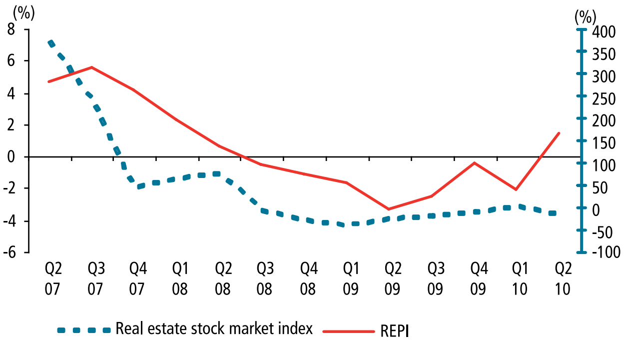


Chart 4.25: Stock market indexes

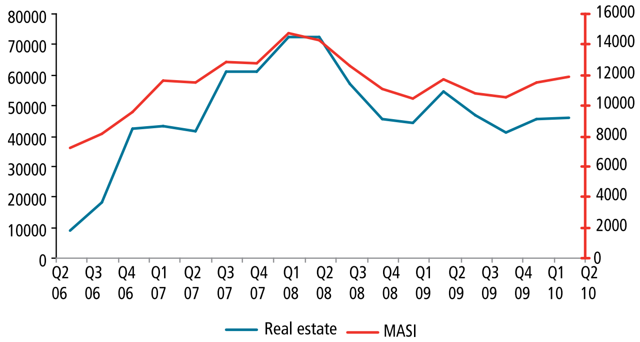


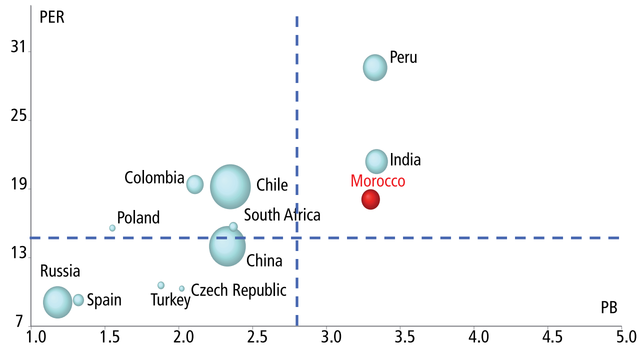
Table 4.3: Equity market's PER

PER	Q2:09	Q3 :09	Q4 :09	Q1 :10	Q2 :10	July 10	Aug. 10
Argentina	12.4	17.0	16.5	17.5	12.0	10.5	10.9
Brazil	9.6	11.1	12.8	16.3	14.8	15.2	12.8
Mexico	16.6	18.1	19.7	17.0	13.5	14.1	14.0
Turkey	8.4	10.8	9.9	10.9	12.0	11.6	11.7
Morocco	16.4	15.8	15.7	16.9	18.1	17.5	17.9

Sources: Datastream and CFG

With the exception of the sectoral indexes of engineering and industrial capital goods, telecommunication, and beverages, which fell by 7.2 percent, 7.5 percent and 9 percent, respectively, all other sectoral indexes registered quarterly increases. Indeed, the stock market index of the leisure and hotels sector posted the highest rise with 42.2 percent, while growth in other sectoral indexes ranged between 0.1 percent for the banking sector and 24.6 percent for the mining sector.

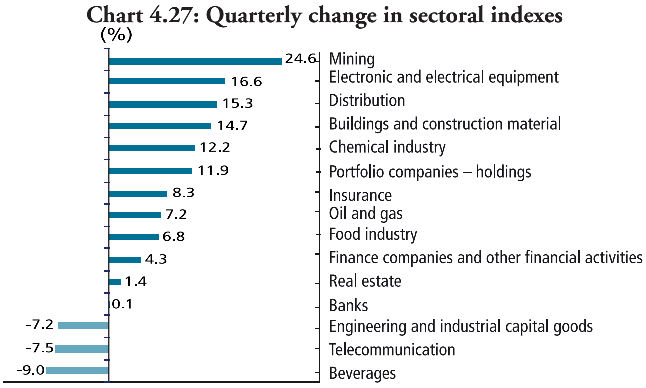
Chart 4.26: Equity market's PER in Morocco and in some emerging countries (*) at the end of June 2010



(*) The size of bubbles depends on the market capitalization/ GDP ratio.

Sources: Datastream, CFG Gestion, and BAM calculations

Chart 4.27: Quarterly change in sectoral indexes



5. RECENT INFLATION TRENDS

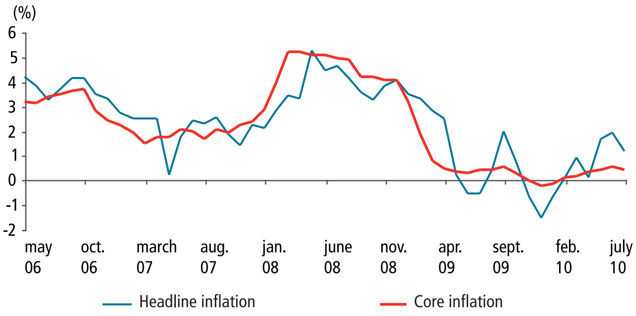
Data for the second quarter and July 2010 come in line with the forecasts of Bank Al-Maghrib published in the previous Monetary Policy Report. Actually, prices continued to rise moderately because of the absence of significant pressure from demand and the still low inflation rate in Morocco's major trading partners. Annual headline inflation reached 1.1 percent in July, down from 1.7 percent in May and 1.9 percent in June, with an average of 1.2 percent in the second quarter. Reflecting the underlying trend of prices, core inflation has changed only very slightly, hovering for several months around an average somewhat above zero. It indeed grew by 0.4 percent in the second quarter and July. The trend in core inflation still reflects the negative impact of the change in the CPIXT and the moderate growth in the CPIXNT excluding volatile food and administered prices. In July, these components respectively contributed -0.4 and 0.6 percentage point to headline inflation. Despite the one-time hikes in the international prices of oil in June, their moderate growth later contributed to slowing down the rise in manufacturing producer prices, which fell to 6.4 percent in July compared with 7.5 percent in June and 11.6 percent in May.

5.1 Inflation trends

In the absence of significant demand pressure and substantial rise in inflation in our major partners, headline inflation, measured by the annual growth in the consumer price index (CPI), remained relatively low. Overall, retrospective analysis shows that headline inflation has fallen markedly since the peak of May 2008, on the back of the downward trend in food inflation, especially staple food. This trend continued until December 2009 when headline inflation fell to -1.6 percent before increasing again, mostly driven by the rise in the prices for "volatile food products" and the less rapid annual decline in the prices for certain staple food. Excluding volatile food and administered prices which account for about 33 percent of the CPI basket, core inflation also declined, though with less volatility.

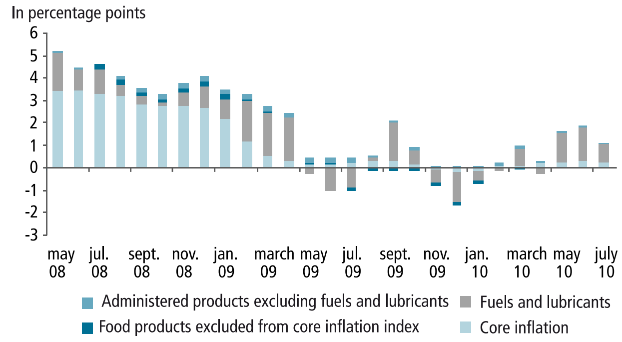
Headline inflation reached 1.1 percent in July, down from 1.7 in May and 1.9 percent in June, mainly due to the marked slowdown in the price rise of "volatile food products" because of the slower increase in the prices for vegetables and fresh fruit from 28.6 percent and 11.1 percent

Chart 5.1: Headline inflation and core inflation, year-on-year



Sources: HCP and BAM calculations

Chart 5.2: Contribution of the main components to headline inflation, year-on-year



Sources: HCP and BAM calculations

to 13.8 percent and 8.7 percent, respectively. Increase in nonfood prices remained unchanged at 0.9 percent, like prices for fuels and lubricants which stabilized both month on month and year on year. Altogether, the moderate prices under this heading, amid elevated volatility in oil prices, are attributable to the freezing of the indexation mechanism which insulates the national market from international fluctuations.

The burden of oil price changes then falls on the State's budget, through the Subsidization Fund. Administered prices, excluding fuels and lubricants, increased by 0.4 percent.

Core inflation has been subdued for several months now, standing at 0.4 percent in July, down from 0.5 percent in June and 0.4 percent in May. The absolute gap between headline inflation and core inflation, which was 1.4 point in June, shrank by half in July to 0.7 point.

5.2 Tradable and nontradable goods

Inflation trends can also be analyzed through the breakdown of the CPI into an index of tradable goods and another of nontradable goods. The respective weights of these two indexes in the overall index represent 49 percent and 51 percent. Prior to May 2009, prices for tradables contributed positively and significantly to headline inflation, while prices for nontradables moved up at a moderate nearly-stable pace. Subsequently, prices for tradable goods started to decline under the impact of some volatile fresh food prices. In July, the index of tradable goods appreciated by 1.0 percent, down from 2.3 percent in June, thereby contributing 0.5 percentage point to headline inflation, compared with 1.2 percentage point in the previous month.

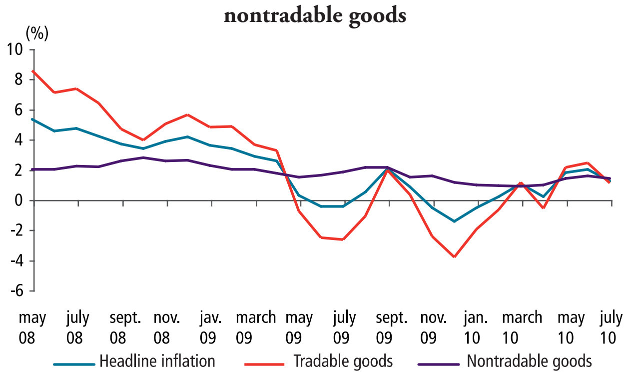
Table 5.1: Inflation and its components

	Monthly change (%)			Year-on-year (%)		
	May 10	June 10	July 10	May 10	June 10	July 10
Headline inflation	0.0	-1.0	-0.6	1.7	1.9	1.1
Including: - Food products excluded from core inflation	0.1	-7.2	-4.1	9.9	12.0	6.5
- Fuels and lubricants	0.0	0.0	0.0	0.1	0.0	0.0
- Administered goods except fuels and lubricants	0.1	0.0	0.0	0.5	0.5	0.5
Core inflation	0.1	0.3	0.2	0.4	0.5	0.4
Including: - Food products	-0.1	0.1	0.1	-0.6	-0.3	-0.4
- Clothing and shoes	-0.2	-0.3	-0.2	0.3	0.2	-0.1
- Housing, water, gas, electricity and other fuels*	0.1	0.1	0.0	0.8	0.9	0.7
- Furniture, household appliances and common house maintenance	0.1	0.1	-0.1	0.8	0.9	0.7
- Health*	0.3	0.1	0.0	-0.2	-0.2	-0.2
- Transportation*	-0.1	0.0	0.0	0.5	0.2	0.2
- Communication	-0.1	0.0	0.0	-0.4	-0.5	-0.5
- Leisure activities and culture	-0.2	-0.3	-0.1	-0.6	-0.9	-0.9
- Education	0.0	0.0	0.0	3.8	3.8	3.8
- Restaurants and hotels	0.1	0.2	0.3	3.0	2.9	2.6
- Miscellaneous goods and services	0.1	0.1	0.3	1.3	1.4	1.7

** Excluding administered goods*

Sources: HCP, and BAM calculations

Chart 5.3: Year-on-year change in price indexes of tradable and nontradable goods



Sources: HCP, and BAM calculations

Table 5.2 : Domestic selling price of oil products

Products (Dh/Liter)	Dec. 08	Feb. 09	Apr. 09	July 09	Jan. 10	Apr. 10	July 10
Premium gasoline	11.25	10.25	10.25	10.25	10.25	10.25	10.25
Gasoline*	7.22	7.22	-	-	-	-	-
Diesel 350/50 *	10.13	7.50	7.15	7.15	7.15	7.15	7.15
Industrial fuel (Dh/Ton)	3374	3074	3074	3074	3074	3074	3074

(*) The Diesel 50PPM replaced the diesel 350 in February 2009 and the ordinary diesel in April2009.

Source: Ministry of Energy and Mining

Except for "volatile food products" and "administered goods", prices for tradable goods have been declining since March 2009, on a year-on-year basis. The inflation of tradable goods appears to be highly correlated with fluctuations in international consumer prices (chart 5.6). It stood at -1 percent in July, down from -1.2 in June, because of the less marked annual decrease in the prices of cereals and oils. This trend is also attributable, to a lesser degree, to the decline in the prices of consumer durable goods. The index of nontradable goods, excluding volatile and administered products, which is particularly relevant to the assessment of domestic inflationary risks, has been hovering around 2 percent since early 2009, after moving up almost steadily in 2008. In July, it grew by 2 percent, from 2.4 percent June, with the slower rise in the prices for fresh meat and restaurant services.

5.3 Goods and services

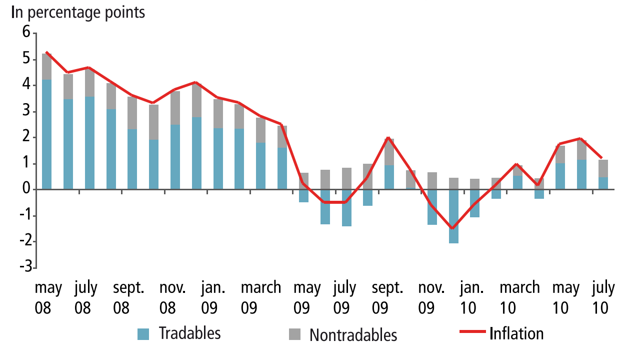
Mostly composed of volatile food products, unprocessed goods caused inflation to fall in July, as in the previous month. Prices for processed goods, services, and fuels and lubricants continued to trend as in the month before. Because of the slowdown in the inflation of unprocessed goods from 8.1 percent to 4.5 percent, their contribution to annual headline inflation fell from 1.7 percentage point in June to 1 percentage point in July. Prices for processed goods, excluding fuels and lubricants, remained almost unchanged from one month to the next, declining at an annual rate of 0.8 percent in July. The downward effect that this component exerts on headline inflation is starting to wear off, as its contribution inched down from -0.7 percentage point in December 2009 to -0.4 percentage point in June 2010 and -0.3 percentage point in July. The annual contribution of services prices to headline inflation has stabilized at 0.5 percentage point since last January.

Table 5.3: Change in the price indexes of tradables and nontradables

	Monthly change (%)			Year-on-year change (%)		
	May 10	June 10	July 10	May 10	June 10	July 10
Tradables	0.0	-2.1	-1.6	2.0	2.3	1.0
Nontradables	0.0	0.2	0.6	1.3	1.5	1.3

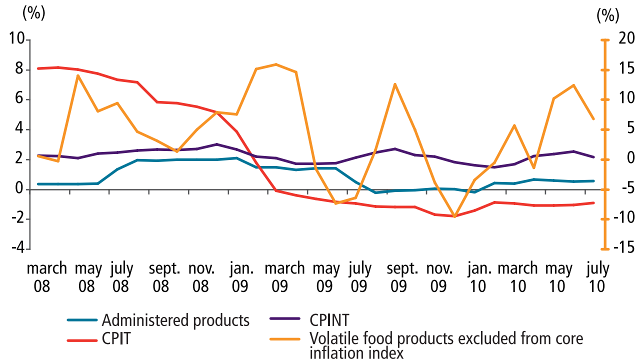
Sources: HCP and BAM calculations

Chart 5.4: Contribution of tradables and nontradables to headline inflation (year-on-year)



Sources: HCP and BAM calculations

Chart 5.5: Year-on-year change in the prices of tradables and nontradables excluding volatile food products and administered products



**The two acronyms refer to tradables and nontradables excluding volatile food products and administered products*

Sources: HCP and BAM calculations

Table 5.4: Price indexes of tradables and nontradables excluding volatile and administered products

	Monthly contribution to inflation		Year-on-year contribution to inflation	
	June 10	July10	June 10	July10
Products excluded from core inflation index Of which:	1.0	-0.6	1.5	0.9
Administered products	0.0	0.0	0.1	0.1
Volatile food products	-1.0	-0.6	1.5	0.8
CPIXT	0.0	0.0	-0.4	-0.4
CPIXNT	0.0	0.0	0.8	0.6

Sources: HCP and BAM calculations

5.4 Industrial producer price index

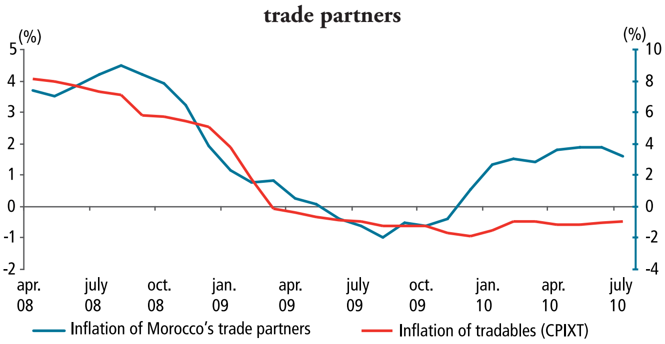
The annual growth in industrial producer prices continued to slowdown, from 11.6 percent in May and 7.5 percent in June to 6.4 percent in July. This trend mostly reflects a similar change in the "coking and refining industry" whose growth fell from 30.5 percent in June to 24.9 percent in July, contributing 6.2 percentage points to the increase in the industrial producer price index, down from 7.3 percentage points in the previous month.

Excluding the coking and refining industry, the producer price index posted a mere annual increase of 0.2 percent, down from 0.3 percent, attributable to the continued moderation in non-energy producer prices. This trend in part reflects an accelerated rise in the prices for "paper and cardboard industry" which edged up from 8.2 percent to 12.1 percent. It also covers a less rapid growth in "chemical industry" prices from 0.5 percent in June to 0.2 percent in July. The producer price index for the food industry fell 1.1 percent, more markedly than the 0.9 percent decline of June. Divergent trends were observed in the prices of other industries, ranging between 3.1 percent for "metallurgy" to -2.7 percent for "metal working". Generally, producer prices in industries except coking and refining contributed 0.1 percentage point to the increase in the industrial producer price index.

5.5 Inflation expectations

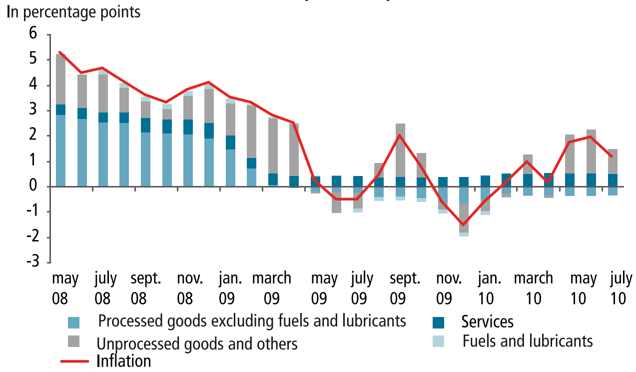
Inflation expectations are assessed based on the results of the BAM business survey. The latter indicates that in July 2010 the percentage of corporate managers anticipating stagnant inflation increased between April and June and fell in July, but remains high. During the same period, the percentage of those expecting a rise in inflation declined before moving up slightly in July (chart 5.11).

Chart 5.6: Year-on-year change in inflation of tradables excluding volatile and administered products and inflation in trade partners



Sources: HCP, IFS and BAM calculations

Chart 5.7: Contribution of goods and services prices to inflation (year-on-year)



Sources: HCP and BAM calculations

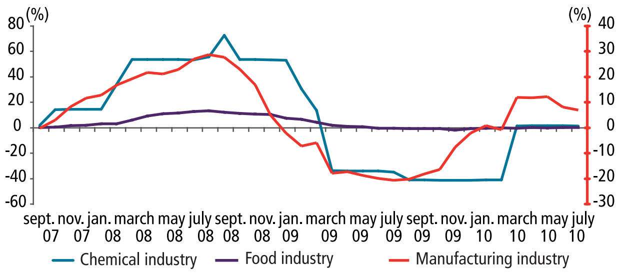
Table 5.5: Price indexes for goods and services

	Monthly change (%)			Year-on-year change (%)		
	May 10	June 10	July 10	May 10	June 10	July 10
Processed goods*	0.0	0.0	0.1	-0.9	-0.8	-0.8
Unprocessed goods and others	0,0	-4.2	-2.5	6.8	8.1	4.5
Services	0.1	0.0	0.1	1.6	1.6	1.5
Fuels and lubricants	0.0	0.0	0.0	0.1	0.0	0.0

** Excluding fuels and lubricants*

Sources: HCP and BAM calculations

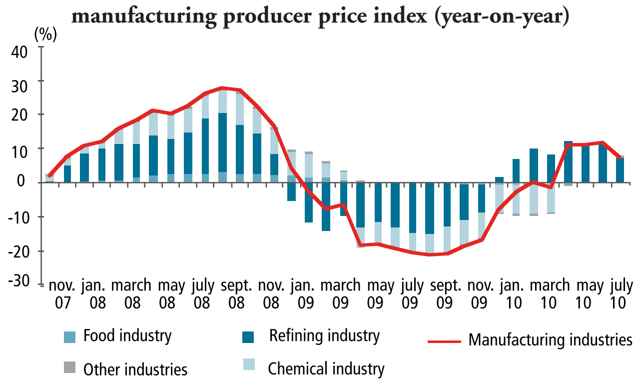
Chart 5.8: Change in industrial producer price indexes (year-on-year)



Sources: HCP, and BAM calculations

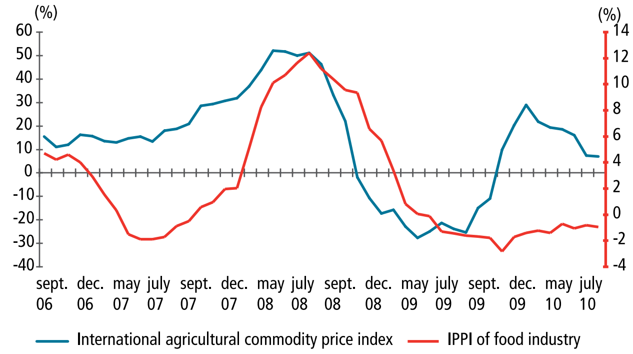
According to corporate managers' expectations, the balance of opinion shows that the producer prices of finished goods would continue to increase in all industries except for textile and leather industries, mechanical and metallurgical industries, and electrical and electronic industries (chart 5.12).

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



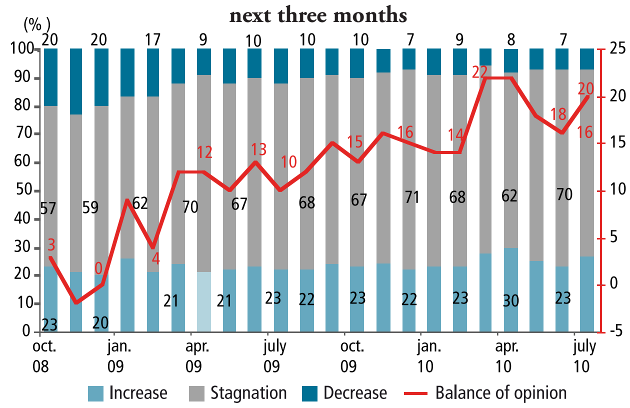
Sources: HCP, and BAM calculations

Chart 5.10: Change in domestic and international food prices (year-on-year)



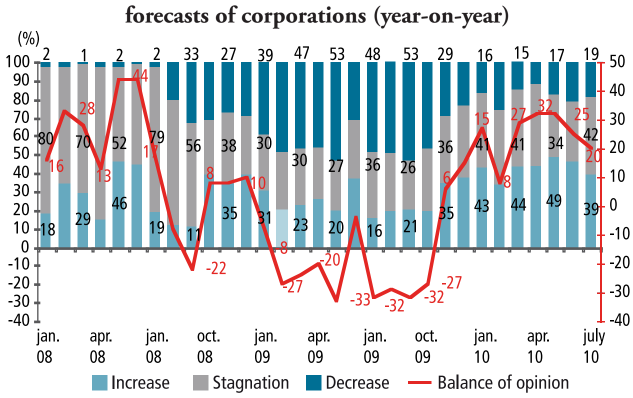
Sources: World Bank, HCP and BAM calculations

Chart 5.11: Corporate managers' perception of inflation for the next three months



Source: BAM monthly business survey

Chart 5.12: Change in industrial producer price index and forecasts of corporations (year-on-year)



Source: BAM monthly industrial business survey

6. INFLATION OUTLOOK

This section presents the inflation trend deemed most probable (central forecast) over the next six quarters and examines the major associated risks (balance of risks). The central forecast scenario therefore depends on the assumptions and trends envisaged for a series of variables affecting economic activity and inflation. Assuming the non-occurrence of the major risk factors identified, inflation over the coming six quarters remains in line with the price stability objective, with an average forecast of about 1.9 percent. This projection was adjusted upward (from 1.7 percent earlier) in comparison with the June MPR. In 2010, headline inflation should hover around 1 percent, slightly below the level projected in the last MPR (1.2 percent). The balance of risks surrounding this forecast is slightly skewed to the upside because of uncertainties surrounding the future trend in import prices.

6.1 Baseline scenario assumptions

6.1.1 International environment

Global activity continues to show positive growth despite the financial turmoil that marked the second quarter of this year. On the back of the strong recovery in emerging markets, particularly in Asia, industrial production and international trade increased noticeably. Similarly, private demand has strengthened, showing promising signs of growth and renewed confidence among consumers who were mostly encouraged by the exceptional stimulus measures that followed the crisis.

However, economic activity in advanced countries still seems to grow moderately, characterized by substantial differences from one country to another. Indeed, GDP growth in the second quarter of this year reached around 3.7 percent in Germany and 3 percent in the United States, compared with 1.7 percent in France. Spain, with a growth rate of -0.2 percent, was hard hit by the crisis that continues to negatively impact its economy.

Moreover, the trend in the labor market of developed countries remains generally uncertain. Following the reductions in the number of hours worked caused by the drop in aggregate demand, the upturn in activity is likely to be accompanied by an increase in hours worked rather than a significant net job creation. As a consequence, unemployment rates in the developed countries continue to be well above the pre-crisis levels, as evidenced by the latest figures of the second quarter of this year which indicate an unemployment rate of 9.7 percent in the United States and 10 percent in the euro area.

Regarding growth prospects, the International Monetary Fund has slightly revised upward its forecast for U.S. economic activity in the current year and next year. In the July report, the IMF expects a growth rate of about 3.3 percent in 2010 and 2.9 percent in 2011, up from the 3.1 percent and 2.6 percent, respectively, which had been announced in its April report. However, expectations for the euro area have not undergone any significant change, as the IMF still projects a growth rate of around 1 percent for 2010. The forecast for 2011 was however revised slightly downward from 1.5 percent (April report) to 1.3 percent. The downside risks to growth have risen considerably. In the short term, the main threat is the increasing uncertainty about the risk of sovereign debt, which can potentially engender a further increase in financing costs and weaken bank balance sheets, thereby causing tightened credit conditions, lower confidence of corporate managers and consumers, and fluctuations in exchange rates. In fact, in a context where economies are intertwined, global demand could again decline markedly. Moreover, domestic demand could be impacted by a poorly planned or too strict fiscal consolidation, especially as it is still weak.

Based on these developments, the baseline scenario for this Monetary Policy Report expects the weighted growth rate of our main trade partners (France, Germany, Italy and Spain) to stand at around 1 percent in 2010 and 1.3 percent in 2011. These assumptions are similar to those made in the previous MPR. It should be noted that this growth rate is calculated on the basis of an average weighted by the respective share of these countries in the Moroccan foreign trade.

Despite the rising inflation in the euro area in recent months, compared to the relatively low rates of last year, inflation should remain broadly subdued. This level reflects inflation expectations which remain well anchored in line with the ECB price stability objective that targets an inflation rate below but close to 2 percent, as well as low domestic pressure on prices due to underutilization of productive capacity. As a result, the European Central Bank expects an inflation rate of 1.5 percent both for 2010 and 2011.

Risks surrounding the outlook for inflation in the euro area remain broadly balanced. Indeed, the upward pressure could result from higher commodity prices in the medium term. Also, due to the fiscal consolidation which must be carried out in the coming quarters, increases in direct taxation and administered prices are likely to feed inflationary pressures. However, these risks would be offset by a limited change in internal costs.

Under these circumstances, the ECB would keep its policy rate on the short-term unchanged at 1 percent. The baseline scenario for this MPR points to an average Euribor rate of 0.88 percent in the second half of the current year. This rate should then gradually rise to 0.97 percent in the first half of the year 2011 and 1.08 percent in the second half.

Finally, in an international context marked by significant rise in commodity prices and sustained demand from emerging countries, the non-energy import price indicators included in the forecast models developed by Bank Al-Maghrib were slightly revised upward compared to the last MPR of June.

6.1.2 National environment

Economic growth outlook for 2010 remains broadly promising. Nonagricultural sectors have held up well since the fourth quarter of 2009. However, given the base effect linked to the bumper crop produced in 2009, agricultural activity should impact the growth rate of national economy.

According to recent estimates by the Ministry of Agriculture, the 2009-2010 crop year ended with a cereal production of 74.6 million quintals. This figure, in line with the assumption made in the June MPR (76 million quintals), remains above the average of the last five crop years.

Nonagricultural activity, though lower than the average level observed in recent years, continues to show sustained momentum as evidenced by the latest indicators. For the current year, this sector is expected to grow between 4.5 percent and 5.5 percent, up from 1 percent in 2009. This performance is primarily attributable to the improvement in industrial activity (particularly in the construction, mining and processing industries) and services. This upturn is also driven by domestic demand which should benefit from the good crop year and the measures taken under the Finance Act 2010 to support household consumption and investment, as well as the renewed increase in remittances by Moroccan expatriates.

Similarly, foreign demand continues to grow positively, owing to a more favorable international environment. Nevertheless, it remains less strong compared to the trend observed in recent years due to a still modest recovery in our major trading partners.

Under these conditions, overall GDP would expand by 3 to 4 percent. For the 2010-2011 crop year, the central scenario adopted in this forecasting exercise indicates an average cereal production of between 60 and 65 million quintals.

Available data on the labor market for the second quarter of 2010 show an unemployment rate of 8.2 percent, up from 8 percent in the same quarter of last year. This increase is attributable to rural unemployment which grew 0.3 percent following a decline in agricultural production. Urban unemployment rate remained almost stable.

The Bank Al-Maghrib business survey for June 2010 reported stable workforce for the current quarter. Similarly, the positive outlook for economic activity, particularly the upturn in nonagricultural sectors, suggests a possible improvement in the labor market. However, these conditions are not expected to influence the future change in wages, and no increase in the minimum wage is expected under the baseline scenario over the six quarters of our forecast horizon.

Finally, the latest IMF projections (July 2010) on the barrel price (basket) were adjusted downward and now stand at $75.25 in 2010 and $77.5 in 2011, reflecting the emergence of tensions in financial markets that caused a decline in global demand for oil products. Forecasts of the World Bank expect a price (basket) of $82.04 per barrel in 2010 and $80.69 in 2011. These projections suggest that the national subsidization system would remain sustainable in view of the budget allocated to it in the 2010 Finance Act based on a scenario of $75 a barrel. Under these circumstances, the central forecasting scenario assumes the diesel pump price to stagnate at 7.15 dirhams per liter.

6.2 Inflation outlook and balance of risks

In case the major risks do not materialize, the central forecast for the coming six quarters would run at 1.9 percent, a level in line with the objective of price stability. Compared with the figures projected in the previous MPR, the inflation forecast for 2010 was slightly revised downward from 1.2 percent to 1 percent.

Projections over the coming six quarters suggest a decline in the third quarter of 2010 when inflation would reach about 0.6 percent. Prices would then recover in the fourth quarter of this year, rising by 2 percent. The same trend is expected to continue in 2011, with an average rate of around 2.2 percent. Therefore, inflation would reach 2.5 percent in the first quarter and 2.2 percent and the second and third quarters (up from the respective 1.9 percent, 2 percent and 1.8 percent published in the latest MPR). In the fourth quarter of 2011, inflation would reach 2 percent.

These forecasts are made on the basis of assumptions deemed most probable. Nonetheless, many uncertainties stemming from the future trend in exogenous variables as well as from the forecasting models might lower or increase the expected inflation rate. Analysis of the balance of risks shows an asymmetrical forecasting range, which is represented in the form of a fan chart. It is a probabilistic estimation of the uncertainty areas surrounding the central forecast (Chart 6.1).

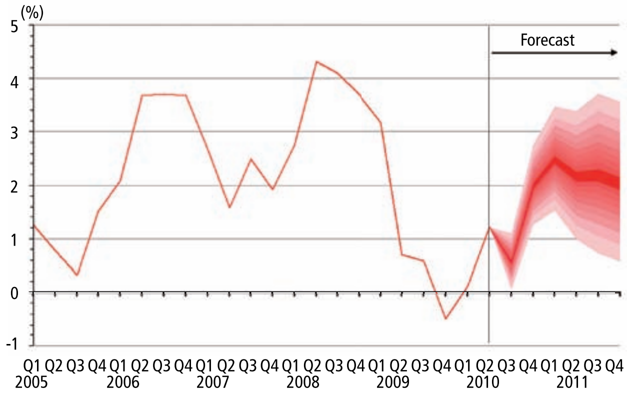
The fan chart of this forecasting exercise shows a slight upward asymmetry. The latter is mostly due to the potential risks arising from uncertainties over the future change in import prices. The occurrence of one or more of these risks may deviate the inflation rate from the central forecast, to a level included (with a 90 percent probability) within the forecasting range represented in the fan chart.

Table 6.1: Inflation outlook for Q3 2010- Q4 2011

	2010		2011				Average		
	Q3	Q4	Q1	Q2	Q3	Q4	2010	2011	FH*
Central forecast (%)	0.6	2.0	2.5	2.2	2.2	2.0	1.0	2.2	1.9

(Quarterly data,, Year-on-year)
**Forecast horizon*

Chart 6.1: Inflation forecast, Q3 2010- Q4 2011
(Quarterly data, Year-on-year)



(*) This chart represents the confidence interval of inflation forecast based on the baseline scenario (dark red); confidence intervals between 10 percent and 90 percent are also reported. Each addition of intervals with the same color, on both sides of the central forecast, increases by 10 percent the probability of fall in headline inflation 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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Legal deposit: 2007/0033

BANK AL-MAGHRIB

Central Administration
277, Avenue Mohammed V - B.P. 445 - Rabat

Phone: (212) 5 37 70 66 45
Fax: (212) 5 37 20 67 68

E mail: deri@bkam.ma

www.bkam.ma