BANK AL MAGHRIB

1959 - 2009

# Monetary Policy Report

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Document prepared for
the Bank Board
March 24, 2009

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بنك المغرب

## LIST OF ABBREVIATIONS

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

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### BANK AL-MAGHRIB BOARD MEETING

Rabat, March 24, 2009

1. The Board of Bank Al-Maghrib held its quarterly meeting on March 24, 2009.

2. During this meeting, the Board examined recent economic, monetary and financial trends, and inflation forecasts up to the second quarter of 2010.

3. Year-on-year headline inflation stood at 3.9 percent in the fourth quarter of 2008, in line with the central forecast published in the Monetary Policy Report of December 23, 2008. The latest data available show that prices rose 3.8 percent in February, down from 4 percent in January. This trend is mostly attributable to the strong increase in fresh food prices, whereas the fundamental trend of prices remains down, as evidenced by the very rapid decline in the growth rate of core inflation which fell from 3.3 percent in December to 2.8 percent in January and 1.3 percent in February.

4. The Board considers that the continued deceleration of inflation is the result of the slowdown in tradables' inflation. In fact, the easing of pressure on prices for non-energy commodities, particularly staple food, and on oil prices, has significantly contributed to the fall of tradables' inflation. This trend is confirmed by the change in industrial producer prices, which were the most impacted by the downward trend in the import prices of oil and non-energy commodities, declining 2.8 percent in December and 7.8 percent in January.

5. In a global context marked by a very strong uncertainty and severe recession in the main advanced countries, national economic growth is expected to remain relatively resilient in 2009, mostly owing to the good performance of the agricultural sector and, to a lesser extent, domestic demand. The latest data and estimates available indicate that GDP growth settled at 4.8 percent in the fourth quarter of 2008, compared with 5.4 percent and 6.5 percent in the third and second quarters, respectively. The impact of global economic slowdown is being particularly felt in exports, tourism, remittances of Moroccans living abroad, and, possibly, foreign direct investments. As a consequence, the growth rate of nonagricultural sectors would slow down in the coming quarters.

6. In addition, monetary conditions show that bank credit continued to decline, registering a year-on-year growth rate of 21 percent in February, down from 25 percent in the last quarter of 2008. For the year 2009, the forecasts predict a 16 percent increase. At the same time, the reduction in nonfinancial agents' monetary surplus contributes to the easing of pressure on prices.

7. Altogether, the central forecast of headline inflation and core inflation for the six coming quarters was revised downwards from the previous forecast of the December Monetary Policy Report. This results from the scale and prolonged nature of the global economic contraction and its repercussions on domestic growth, as well as from the substantial slowdown of world commodity prices and inflation in Morocco's key partners. Over the forecast horizon, headline inflation would permanently remain below 3 percent, with an average forecast of about 2.6 percent up to the second quarter of 2010. For core inflation, the projection shows a rate of about 2 percent over the forecast horizon.

8. Internal and external risks surrounding the central forecast are tilted to the downside over the forecast horizon, notably due to the international outlook that is expected to further deteriorate in the coming quarters. Against this backdrop, demand-driven pressure is projected to ease. The current transmission of the fall in international prices to domestic prices would continue, as indicated by the trend and outlook of import prices, industrial producer prices, and tradables' prices. Beyond the year 2009, the volatility of commodity prices yet constitutes a source of uncertainty.

9. In this context where risks are skewed to the downside and inflation central forecast is in line with the objective of price stability on a long-term basis, the Board decided to reduce the key rate to 3.25 percent, while closely monitoring all the abovementioned elements.

10. The Board, having considered the opinion of the statutory auditor of Bank Al-Maghrib, and upon examination, approved the Bank's accounts and the allocation of profits for fiscal 2008.

11. The Board also examined and approved the internal audit program for 2009 as well as the internal audit charter.

# OVERVIEW

The international environment, marked by the slipping into recession of Morocco's key partner economies and the sharp decline in commodity prices, has certainly impacted inflation trends, confirming the analysis and forecasts published in the previous Monetary Policy Report. The fall in global inflation and in import prices is indeed passing through to domestic prices, though gradually due to the pace of inventory liquidation and profit-driven behaviors. Against this background, headline inflation stood at 4 percent in January, down from 4.2 percent in December, whereas core inflation fell more noticeably from 3.3 percent to 2.8 percent. This decline in inflation is attributable to the deceleration of tradable prices' growth, which significantly reduced the impact of the rise in nontradables' inflation. The fall in inflation is also evidenced by the change in industrial producer prices which went down 7.8 percent in January, after the 2.8 percent drop in December 2008.

Following the deterioration of global economic conditions, forecasts for the national economy published in the Monetary Policy Report of December 2008 have been revised downwards. GDP now would grow 5.8 percent in 2008, instead of the previously projected range of 6 to 6.5 percent. In 2009, economic growth would slightly decelerate to around 5 percent, mainly driven by a better-than-average increase in agricultural activity. The overall output gap in 2009 and 2010 is expected to remain positive, though lower than in 2008.

Growth in agricultural value added would not exceed 3.9 percent, falling to its lowest level in the past six years. Therefore, nonagricultural output gap is projected to be negative in 2009, and would slightly improve in 2010. Actually, the poor economic conditions in the eurozone have certainly affected the national economy, through the real transmission channels, namely exports, foreign direct investments, tourism, and remittances of Moroccans living abroad. This is evidenced by the recent sectoral changes, as shows in particular the output capacity utilization rate in the industry, calculated on the basis of Bank Al-Maghrib's monthly survey, which hit a record low since 2007. Furthermore, the slight improvement in labor conditions over the last quarter of 2008 is solely attributable to the decline in rural unemployment rate, in connection with a better crop year. Altogether, all of these elements suggest significant easing of pressure on prices in the coming quarters.

Monetary conditions also suggest continued easing of pressure on prices. In fact, the slowdown in money creation, which has been observed for several quarters now, led to the continued decline in nonfinancial agents' monetary surplus. Growth in loans continued to slowdown, registering a rate of 21 percent in January and a slight drop on a month-to-month basis, but remains above its long-term trend. Analysis of credit structure shows that the slowdown concerns all nonfinancial agents and in the same proportions. This change suggests that credit growth would gradually return to levels matching its long-term trend.

In lending rates, the findings of Bank Al-Maghrib's survey for the fourth quarter of 2008 indicate a limited increase in the weighted average rate, which particularly conceals a slight increase in interest rates on consumer and real estate loans, and a drop in rates on equipment loans.

Altogether, the analysis confirms the continued downward trend of risks surrounding the future change in prices. The central forecast of headline inflation and core inflation for the six coming quarters was revised downwards compared with the December MPR. This results from the scale and sustainable nature of the global economic contraction and its repercussions on domestic growth, as well as from the substantial slowdown of world commodity prices and inflation decline in Morocco's key partners. Over the forecast horizon, headline inflation would permanently remain below 3 percent, with an average forecast of about 2.6 percent. At the end of the forecast horizon (the second quarter of 2010), headline inflation is expected to hover around 2.6 percent. In the year 2009, headline inflation would average 2.6 percent, dropping to 2.2 percent in the second quarter before stabilizing at around 2.5 percent in the following quarters.

Risks surrounding the central forecast are on a downward trend. Externally, the indicator of foreign demand for Moroccan exports shows that the international outlook is expected to deteriorate in the coming quarters, resulting in a decrease of pressure on inflation. Beyond the year 2009, the volatility of commodity prices yet constitutes a source of uncertainty. Internally, risk factors are on the downtrend too, mainly because of the easing of demand-driven pressures. These might fall further against the background of a worse-than-expected deterioration of economic activity. The current transmission of the fall in international prices to domestic prices would continue, as indicated by the trend and outlook of import prices, industrial producer prices, and tradables' prices. In addition, analysis of aggregate supply and demand conditions suggests an easing of pressures on the labor market. Nonetheless, the 5 percent increase in the minimum wage, scheduled in July 2009, represents a factor of uncertainty as to this trend.

# 1. AGGREGATE SUPPLY AND DEMAND

In a global context marked by severe recession in the major developed countries, domestic growth in 2009 would be about 5 percent, mostly owing to the good performance of the agricultural sector. Nonagricultural value added would slow down to around 3.9 percent, its lowest level in the past six years. The impact of global economic slowdown is being particularly felt in foreign demand, tourism, remittances of Moroccans living abroad, and foreign direct investments. However, trade deficit would narrow following the fall in imports that is particularly attributable to the decline in commodity and energy prices and the slowdown of economic activity. Exports would also drop, being impacted by the fall in the international prices for phosphates and derivates and the decline in some industrial exports. Against this backdrop, current account deficit/GDP ratio would improve compared with last year. Domestic demand would continue to sustain growth, as resident household consumption would remain strong and investment would maintain momentum, albeit at a rate lower than previous years. Analysis of aggregate supply and demand conditions suggests a likely mitigation of pressure on prices over the forthcoming quarters.

## 1.1 Output

In the year 2008, the national economy grew in an unfavorable context marked by the slipping into recession of Morocco's key partner countries. Against this background, the forecasts made as part of the Monetary Policy Report of December 2008 have been revised downwards. At end of 2008, economic growth is projected to reach about 5.8 percent, driven by a nearly 10.5 percent agricultural growth and a mere 5.1 percent growth in nonagricultural activities, down from 6.1 percent a year earlier.

In 2009, economic growth would slightly decelerate to around 5 percent, mainly due to a better-than-average increase in agricultural activity. Nonetheless, growth in nonagricultural value added would not exceed 3.9 percent, falling to its lowest level in the past six years.

In agriculture, the value added of the sector increased 11.6 percent in the fourth quarter of 2008. In the first three months of 2009, it would tick up to about 17 percent, capitalizing on the very favorable weather conditions. Actually, the high rainfall level registered from the beginning of 2008-2009 crop year to February 2009 has led to a substantial improvement in water resources and positively impacted the whole agricultural sector, particularly through the good development in vegetative stages of fall cereal crops, the gradual new fruit planting, and the improvement in range vegetation, advantageous for the breeding activity. These developments, alongside the incentive measures to optimize the existing

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

| | 2007 | 2008 | | | | |
|---|---|---|---|---|---|---|
| Activity branches | QIV | QI | QII | QIII | QIV(P) | QI(P) |
| Agriculture | -21.0 | 10.9 | 11.2 | 10.4 | 11.6 | 17.0 |
| **Nonagricultural value added** | **6.4** | **6.5** | **5.8** | **4.3** | **3.7** | **3.2** |
| Fishing | -8.5 | 44.7 | -16.5 | 17.4 | 15.2 | 3.7 |
| Extractive industry | 5.5 | 2.6 | -1.8 | -2.9 | -3.1 | -4.0 |
| Industry (excluding oil (refining | 5.0 | 5.3 | 4.3 | 2.7 | 2.7 | 2.5 |
| Oil refining and other energy products | 56.5 | 23.1 | -0.4 | -7.7 | -5.0 | -12.0 |
| Electricity and water | 1.0 | 6.6 | 6.3 | -0.1 | -1.1 | -1.0 |
| Building and public works | 9.8 | 10.3 | 10.6 | 9.4 | 8.7 | 8.0 |
| Trade | 3.2 | 5.1 | 5.3 | 2.9 | 2.7 | 2.9 |
| Hotels and restaurants | 3.2 | -1.8 | -1.7 | -3.3 | -5.0 | -10.0 |
| Transportation | 10.2 | 6.2 | 4.2 | 3.6 | 3.1 | 3.5 |
| Post and telecommunications | 10.2 | 11.0 | 13.6 | 9.0 | 8.6 | 7.2 |
| Financial activities and insurance | 21.3 | 20.2 | 19.4 | 17.6 | 11.7 | 10.5 |
| Services to businesses and private individuals | 8.2 | 6.8 | 6.2 | 5.1 | 5.7 | 5.0 |
| General government and social security | 2.8 | 5.7 | 6.3 | 5.4 | 5.5 | 5.0 |
| Education, health and social action | 8.7 | 4.5 | 5.3 | 4.3 | 4.1 | 5.5 |
| **Value added at basis price** | **1.8** | **7.1** | **6.6** | **5.1** | **4.8** | **5.1** |
| Taxes on products net of subsidies | 10.0 | 6.6 | 4.9 | 5.9 | 4.6 | 4.8 |
| **Gross domestic product** | **2.7** | **7.0** | **6.5** | **5.4** | **4.8** | **5.5** |

*Sources: HCP. and BAM forecasts*

potential, should confirm the trend observed since the beginning of the current crop year and reinforce the expected results. The small losses which the Gharb region incurred were minimized by the implementation of a plan to convert the stricken crops.

The national average cumulated rainfall as at February 9, 2009 increased threefold compared with the same period of last year, to 466 millimeters. Similarly, the filling rate of farm dams neared its peak, moving up from 48 percent the previous year to 81 percent. This would prompt an increase in water allocations for irrigated areas, which would mostly benefit market gardening and sugar crops.

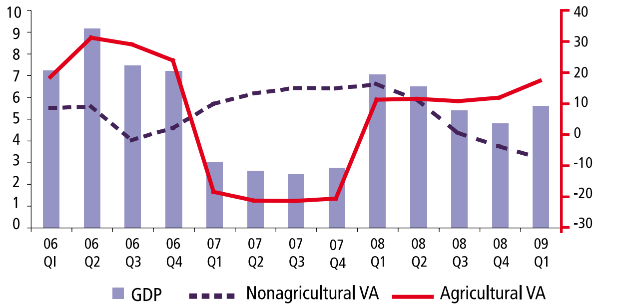
In contrast, exports of early vegetables were on a downward trend, falling from 5.5 percent in the beginning of the export year to 2 percent as at the end of February 2009, whereas those of citrus fruit shrunk 4 percent after a 40 percent increase.

At the same time, cereal sales from June 2008 to January 2009 have more than doubled, compared with the same period of the previous crop year, which would enhance the milling industry and reduce imports.

With regard to the fishing activity, fishing production in 2008 increased 16 percent, up from the 14.4 percent contraction in the same period of last year. This trend is attributable to the growth in the catches of inshore and deep-sea fishing by 14 and 26.8 percent, respectively, following the significant replenishment of pelagic and cephalopod fish resources. In response to the weak results of this sector over the recent years and with a view to improving its performance and raising its contribution to economic growth, a program to modernize the national fleet has been put in place at the end of 2008 and benefits from the financial support of the Government and banks.

The value added of the secondary sector increased 2.8 percent in the fourth quarter of 2008, down from 3.1 percent and 5.6 percent in the third quarter of 2008 and the fourth quarter of 2007, respectively. This growth is expected to decelerate to 2.5 percent in the first quarter of 2009, compared with 6.2 percent in the same quarter of last year.

**Chart 1.1: Quarterly change in GDP and in agricultural and nonagricultural VA,in percentage**




*Sources: HCP, and BAM forecasts*

Table 1.2 : Data of 2008-2009 crop year as at February 9, 2009

| | 2007-2008 (1) | 2008-2009 (2) | Change in % (2)/(1) |
|---|---|---|---|
| **Rainfall indicators** | | | |
| Cumulated rainfall (in mm) | 173.0 | 466.0 | 169.4 |
| Dams' filling rate (%) | 48.0 | 81.0 | - |
| **Cultivated lands (in thousands of Ha)** | | | |
| Fall cereals | 5 000.0 | 5 100.0 | 2.0 |
| Legumes | 235.0 | 251.0 | 6.8 |
| Forage crops | 356.0 | 424.0 | 19.1 |
| Sugar beet | 57.3 | 55.3 | -3.5 |
| **Agricultural imputs (in thousands of quintals)** | | | |
| Seeds | 650.5 | 670.0 | 3.0 |
| Fertilizers | 4 800.0 | 4 850.0 | 1.0 |
| **Exports of citrus fruit and early vegetables (in thousands of tons)** | | | |
| Early vegetables | 430.3 | 437.6 | 1.7 |
| Citrus fruit | 371.0 | 355.5 | -4.2 |

*Sources: Ministry of Agriculture. Rural Development and Fisheries*

## Box 1.1: Forecasting cereal production by Bank Al-Maghrib according to 3 methods

The agricultural sector plays a pivotal role in the national economy, given its influence on economic activity. Therefore, the sector's data are particularly important to fill Bank Al-Maghrib's different forecast models for activity and inflation. Official data on the agricultural sector are available only several months after the end of the crop year, whereas the conditions that mostly direct agricultural output are noticeable well before that date. Therefore, as part of the efforts exerted to improve the framework of growth forecasting, Bank Al-Maghrib has put in place a mechanism for forecasting cereal production and the agricultural value added.

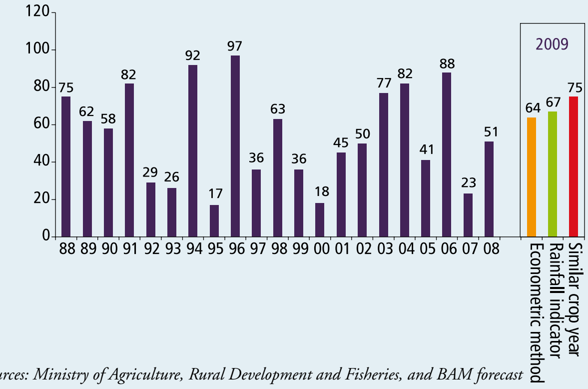
This mechanism includes three forecasting tools:

- An econometric spatial model[1] based on the estimation of linear equations linking output to the monthly rainfall volumes registered from the beginning of the crop year to the forecasting date;

- A method of detecting similar crop years, which consists in determining for each geographical area the crop years whose weather conditions are similar to those prevailing in the current year, based on an analysis of the main components;

- A method based on the construction and use of a rainfall index that is strongly correlated with cereal production and takes into consideration rainfall spatiotemporal distribution for the forecasting of national cereal output.

**Chart B 1.1: Cereal production growth and forecasts (in millions of quintals)**




*Sources: Ministry of Agriculture, Rural Development and Fisheries, and BAM forecast*

The first two methods are applied according to the geographical area and the fall cereal crop (durum wheat, soft wheat, and barley) in line with the recommendations of the Food and Agriculture Organization of the United Nations (FAO) concerning crop production projections. National figures are obtained after the aggregation of results. The third method provides a forecast of the overall cereal production on the basis of the last estimation of the rainfall index.

The implementation of these instruments to rainfall data from the beginning of the crop year to the end of January 2009 shows preliminary projections of 64, 67 and 75 million quintals for the econometric model, the rainfall index method and the similar crop-year detection method, respectively. Accordingly, the average projection is of 68.5 million quintals, up 33 percent from the previous year and 20 percent from the average of the past five years.

According to the type of cereal, soft wheat, durum wheat and barley harvests would grow 37 percent, 6 percent and 47 percent, respectively. The expected low growth in durum wheat production is associated with the weak agricultural performance in the main producing areas which were badly affected by the strong rainfalls at the beginning of the crop year. At the regional level, most cereal-producing areas would see a production surplus compared with the average of the past five years.

However, the harvest of the current year remains dependent on the weather conditions that would prevail in March 2009, a period of ear emergence and seed setting, the average weight of which is an essential component in the shaping of harvest.

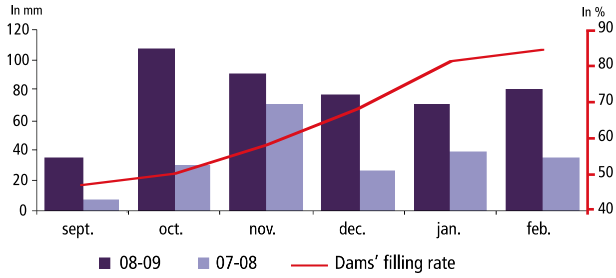
[1] The analyzed spatial units are the geographical areas covered by the regional administrations of the Agriculture Ministry (provincial departments of Agriculture, and the regional offices for agricultural upgrading), which represent good homogeneity.

The value added of the mining activity went down 3.1 percent in the last quarter of 2008. After a period of stagnation over the first nine months of 2008, the saleable output of the OCP declined 7.2 percent. Against this background, exports of phosphates and phosphoric acid shrunk in volume by 15 percent and 28 percent, respectively. In the first quarter of 2009, the sector's value added would follow the same trend, declining 4 percent. As at end of January 2009, exports of phosphates fell 80 percent in volume and 53.7 percent in value. Similarly, exports of phosphoric acid moved down 71 percent in volume and around 29 percent in value.

In the fourth quarter of 2008, the value added of the industrial sector, excluding oil refining, is projected to stand at nearly 2.7 percent. It would not exceed 2.5 percent in the first quarter of 2009, the lowest rate of the past two years. The sector's activity indicators seem to deteriorate. The manufacturing output index indeed registered a 4.4 percent decline in the last quarter of 2008, compared with the same period of 2007. The findings of the January 2009 BAM business survey in the industry reveal that industrial output remained unchanged from one month to the next, and that the orders received were lower than usual , whereas the stocks of finished products were above their usual levels. Propped up by the improvement in domestic sales, overall sales increased in all subsectors, with the exception of textile and leather industries as well as mechanical and metallurgical industries, which were impacted by the contraction in foreign demand. Output capacity utilization rate stabilized at 66 percent month-on-month. Moreover, imports of finished capital goods were subdued as of late January 2009 in value.

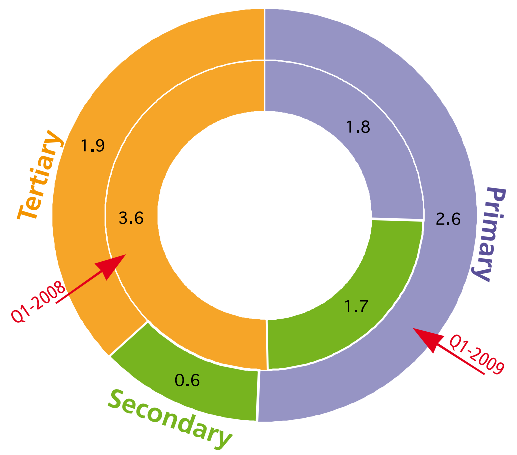
The oil refining sector's value added declined 5 percent in the fourth quarter of 2008, dragged down by a 10.9 percent fall in the SAMIR production as the company was preparing to introduce the 50 ppm diesel to the domestic market. Domestic sales also slowed down, from 14.3 percent in the third quarter of 2008 to 9.4 percent in the last quarter. The value added of energy-related sectors would fall 1.3 percent in the first quarter of 2009, pushed down by a decrease of 12 percent in the value added of the oil refining industry and 1 percent in the "electricity and water" industry.

**Chart 1.2: Change in rainfall during 2008-2009 crop year**



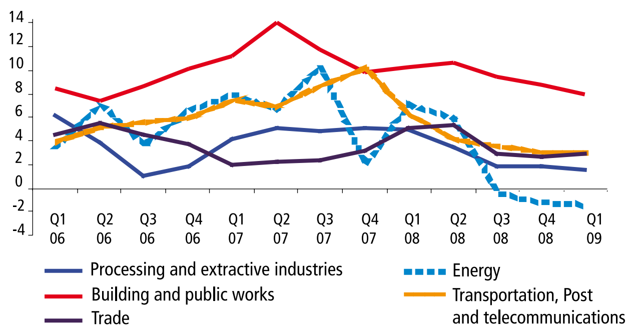

*Source: Ministry of Agriculture, Rural Development and Fisheries*

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




*Sources: HCP, and BAM forecasts*

**Chart 1.4: Year-to-year percent change in the value added**



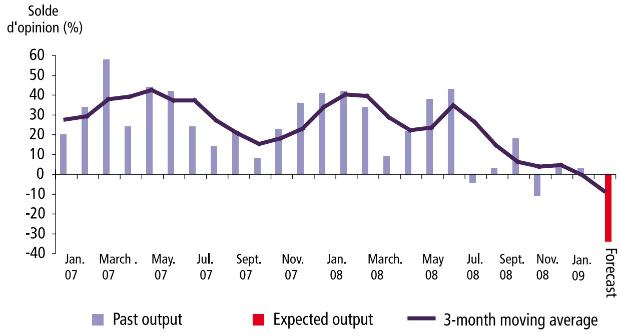

*Sources: HCP, and BAM forecasts*

Despite a slight deceleration, the building and public works sector would grow 8 percent in the first quarter of 2009. Indeed, in January 2009, cement sales rose to 1.1 million tons, 0.45 percent higher than January 2008 and 45 percent than December 2008. This sector should continue to benefit from the ongoing major infrastructure projects, mainly governmental, as well as from the strong demand for new homes. As of the end of January 2009, nearly 45,000 households benefited from the loan guarantee offered under the FOGARIM program, totaling 6.5 billion dirhams.

The slowdown in the growth rate of the tertiary sector, which began in the third quarter of 2008, is projected to persist in the last quarter of 2008 and the first quarter of 2009, increasing 5.2 percent and 4.8 percent, respectively, down from 5.8 percent in the third quarter of 2008 and 7.9 percent in the fourth quarter of 2007. This downshift mostly reflects the fall in the value added of the "hotels and restaurants" industry and the slowdown in the sectors of trade, post and telecommunication, and financial and insurance activities.

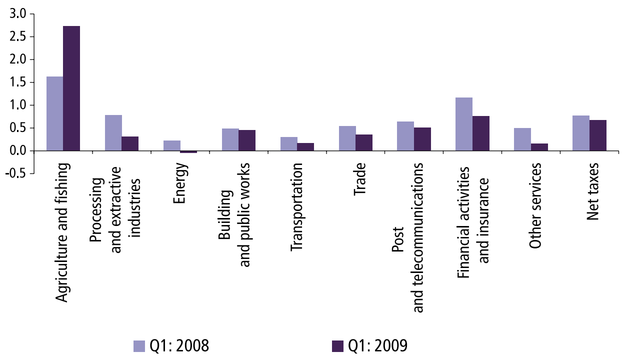
In January 2009, the tourist sector showed signs of slackening. Overnight stays in classified hotels fell 2 percent compared with the same period of last year, in connection with the deceleration of tourist arrivals from 11 percent to 8 percent and the decline in room occupancy rate in the major national destinations. Travel receipts declined more appreciably by 20 percent to 3.5 billion dirhams, compared with 4.3 billion in January 2008, the tourist sector showed signs of weakening. However, the uncertainty surrounding the trend of this sector was reduced when government authorities adopted, early 2009, additional measures besides those previously taken under the tourism strategy. These mainly concerned the cities of Marrakech, Fes, Casablanca and Agadir, with the aim of diversifying tourism supply, strengthening partnerships with tour operators, and preserving the confidence of investors involved in the 2010 Vision projects. Moreover, tourists' preference, mainly the Europeans, for close destinations may constitute an advantageous factor for the sector's short-term growth prospects, following the gradual implementation of the Open Sky agreement in recent years.

**Chart 1.5: Past and expected industrial output**



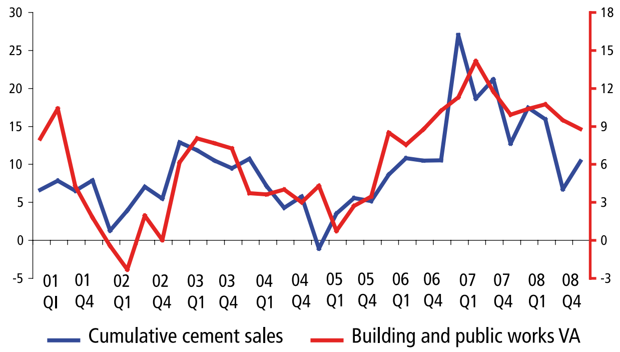

*Source: BAM monthly business survey*

**Chart 1.6: Percent contribution of sectors to overall growth**




*Sources: HCP, and BAM calculations and forecasts*

**Chart 1.7: Year-to-year change in building and public works' value added and in cumulative quarterly cement sales, in %**




*Sources: HCP, and BAM forecasts*

Dragged down by the slowdown in nonagricultural activities, the value added of the transportation sector would grow 3.5 percent in the first quarter of 2009, from 6.2 percent in the same period of last year. This trend may persist as suggests the 3.8 percent drop in the number of air passengers as of the end of January 2009, attributable to the 4.4 percent decline in the number of commercial air passengers the negative impact of which was offset by the 64.2 percent increase in noncommercial passengers. Receipts from international transportation services increased 14.9 percent to 1.6 billion dirhams, up from 1.4 billion in January 2008.

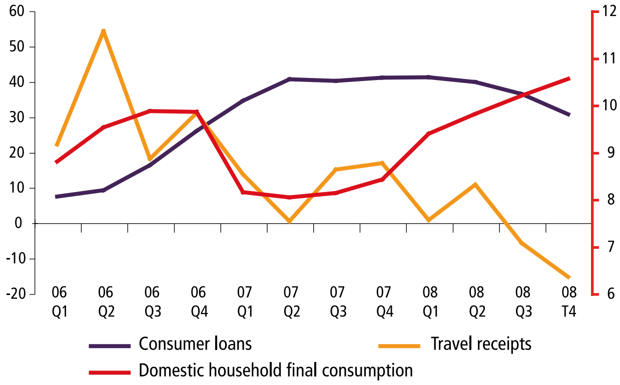
The post and telecommunications sector rose 8.6 percent in the last quarter of 2008. The number of mobile subscribers increased at an annual rate of more than 14 percent to 22.8 million subscribers. Fixed-line market grew 25 percent compared with the previous year. This trend is mostly driven by the growth in fixed-line services with restricted mobility. The total number of internet subscribers increased 44 percent from the year 2007, to 757,453. However, in the first three months of 2009, the sector's growth would stand at 7.2 percent, down from 11 percent in the same period of 2008, thus showing a deceleration in the value added of the sector.

## 1.2 Consumption

Household final consumption increased in 2008. According to the projections of Bank Al-Maghrib, it would rise at a rate of 10 percent in nominal terms, more rapidly than the 8.2 percent reported in 2007. In real terms, it is expected to have grown 5.6 percent, up from 3.8 percent a year earlier. Notwithstanding an unfavorable international background, resident household expenditure was propped up by the improvement in domestic income and employment rate. The rise in net wages following social dialogue and the readjustment of the income tax, in addition to the decline in the unemployment rate all have contributed to improving household purchasing power. Similarly, the subsidization system helped to curb inflationary pressures from increases in food and energy import prices, thus maintaining household purchasing power. In 2008, the Government allocated 31.5 billion dirhams to price subsidization. Accordingly, subsidization costs accounted for 4.7 percent of overall GDP, compared with 2.7 percent a year earlier.

In addition, consumer loans moved up 27.6 percent in 2008, down from 41.4 percent in 2007. At the same time, imports of finished consumer goods grew only 8.5 percent, mainly supported by private car purchases.

**Chart 1.8: Year-to-year quarterly growth of final household consumption, consumer loans and travel receipts, in %**



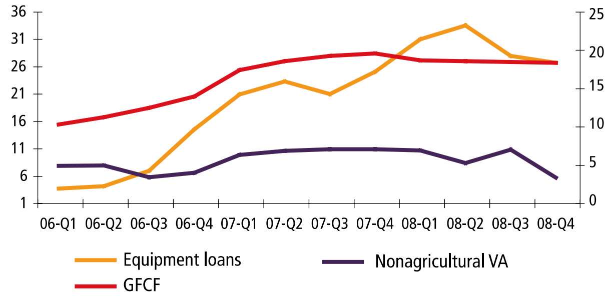

*Sources: HCP, and BAM calculations and forecasts*

Travel receipts declined 3.5 percent in 2008, but remain 29.9 percent higher than the 2003-2007 average. In January 2009, they plunged 20 percent, reflecting the contraction of the tourist sector, which has felt the impact of the global crisis. In 2008, remittances of Moroccans living abroad also dropped at an annual rate of 2.4 percent. This decline may be steeper in the coming months, mainly due to the massive layoffs by European firms. However, this fall may be mitigated by social nets which constitute an extra income for workers in periods of economic slowdown. In January 2009, remittances of Moroccans living abroad fell 14.2 percent, heralding a slackening of nonresident household consumption over the remainder of the year.

General government final consumption rose 5.1 percent in value, and 4.7 percent in constant prices. Operating expenditures increased 8 percent to 106.1 billion dirhams to cover staff expenses and other expenses of goods and services.

Household final consumption would be less strong in 2009, growing 6.9 percent from 10 percent in the year before, as the impact of the global crisis on the national economy would grow more severe. This trend is already noticeable through the weaker outlook of industry and trade sectors, the slowdown in consumer loans, which plummeted from 41.5 percent in January 2008 to 27.4 percent in January 2009, and the fall in foreign transfers. Nevertheless, the upward adjustment of wages and the reduction in the prices of certain types of fuel and food products, as well as the rise in government investments may stimulate domestic aggregate demand. Altogether, growth in final domestic consumption would hover around 6.9 percent.

**Chart 1.9: Year-to-year quarterly growth of gross fixed capital formation, nonagricultural value added and equipment loans, in %**




*Sources: HCP, and BAM calculations and forecasts*

## 1.3 Investment

Investment held up well in the year 2008. Gross fixed capital formation is expected to grow 18.3 percent in nominal terms, at a rate of gross investment of about 36.5 percent of GDP, following the expansion in government investments. Actually, Treasury capital expenditure inched up to 38.2 billion dirhams at the end of 2008, up 35.3 percent compared with 18.3 percent in 2007. Total government investments, including those conducted by government firms, reached 111.2 billion dirhams, equal to 16.6 percent of GDP.

At the same time, 40 projects were validated by the investment committee during the year 2008, representing a total amount of 36.7 billion dirhams. These projects concern the sectors of tourism, infrastructures, food-processing, aeronautics, chemistry, and cement works. In terms of employment, these intended investments are expected to create 12,890 jobs.

Nonetheless, revenues from private foreign investments and loans fell 23.3 percent to 31.7 billion dirhams, from 41.4 billion in 2007. However, they remain above the 30 billion dirhams average of the 2003-2007 period. In this total, returns from foreign direct investments, representing 83 percent, decreased at a rate of 30.6 percent from 38 billion dirhams to 26.3 billion. The sectors which were most hit by this decline were transportation, tourism, and trade.

Reflecting the momentum in investment, imports of finished capital goods rose 26.8 percent in 2008. In volume, they fell 18 percent. Moreover, equipment loans grew at an annual rate of only 19 percent in 2008, down from 27.3 percent in the previous year.

In 2009, business conditions are seemingly deteriorating in the industrial sector, according to the expectations of corporate managers expressed in the Bank Al-Maghrib monthly business survey for January. The survey points to a general downturn in activity over the three coming months, with the exception of food-processing industries. The managers also expect a decrease in foreign sales of textile, leather, electrical, electronic, mechanical and metal industries.

Gross fixed capital formation in 2009 would grow 13 percent, with a gross investment rate of 36.2 percent of GDP, a level lower than that of 2008. The impact of the global economic conditions would be more noticeable in 2009, through the downshift in external demand and foreign investments. Nevertheless, Government measures to shore up the most hit export sectors (textile, leather and car equipment) should contribute to mitigating the effects of the crisis.

## 1.4 Foreign trade

As of the end of January 2009, trade deficit narrowed by 18.9 percent, on a year-to-year basis, to 10.3 billion dirhams. This trend is the result of the decline in imports at a rate higher than that of exports. However, the ratio of imports' coverage by exports shrunk from 46.9 percent to 45.1 percent year-on-year.

The decrease in exports is driven by the fall in the sales of phosphate and its derivatives (-61 percent), following the decline in world prices, as well as by the downturn in the external sales of other products (-16.3 percent). This trend reflects the deceleration of foreign demand against a backdrop of sizeable economic slowdown in our key trade partners. The shrinkage of exports excluding phosphate and derivatives was mainly attributable to the drop in the sales of electrical and electronic equipment (-49 percent), and textile and leather products (-6.2 percent).

The downturn in imports not only reflects the reduction of the energy bill, but also a fall in the other groups of imports, with the exception of capital goods which increased somewhat.

Imports of energy products indeed shrunk 46.7 percent or 2.4 billion dirhams. The energy bill was reduced by 71.8 percent or 1.8 billion dirhams, as the average price per imported ton dropped 43.1 percent and the quantities imported fell 43.1 percent as of the end of January. Similarly, purchases of other energy products dropped 21.7 percent overall. Other imports declined 14.7 percent, mainly due to the fall in the purchases of semifinished products following the moderation in the domestic demand of the processing industries and the building and public works' sector. Purchases of food products edged down, mostly because of the 63 percent drop in the value of wheat imports, in connection with the easing of prices on the international markets (see section 3.3). Similarly, imports of commodities and consumer goods registered a decrease, reflecting the declining purchases of crude sulfur, timber, private cars, and cotton fabric. The weakening of growth prospects in our major trading partner countries, which foreshadows increased contraction in foreign demand for Moroccan exports and other declines in the international price of phosphate, would probably speed up the pace of exports' deceleration.

At the same time, the cost of imports may fall sizably if the international prices of energy, food and mineral commodities decline more rapidly.

**Table 1.3 : Trade balance growth in January (year-to-year)**

| (In millions of dirhams) | January 2008 | January * 2009 | Change Amount | % |
|---|---|---|---|---|
| **Total exports** | **11 199** | 8 446 | **-2 753** | **-24.6** |
| Exports of phosphates and derivatives | 2 077 | 811 | -1 266 | -61.0 |
| **Exports excluding phosphates and derivatives** | **9 122** | **7 635** | **-1 487** | **-16.3** |
| Ready-made garments | 1 894 | 1 761 | -133 | -7.0 |
| Hosiery items | 614 | 632 | +19 | +3.0 |
| Citrus fruit | 656 | 676 | +20 | +3.1 |
| **Total imports** | **23 854** | **18 707** | **-5 147** | **-21.6** |
| Imports of energy products | 5 129 | 2 733 | -2 396 | -46.7 |
| Other imports | 18 725 | 15 974 | -2 751 | -14.7 |
| Wheat | 1 489 | 550 | -939 | -63.0 |
| Capital goods | 5 148 | 5221 | +73 | +1.4 |
| Consumer goods | 3 983 | 3 889 | -94 | -2.4 |
| **Trade deficit** | **-12 655** | **-10 262** | **+2 393** | **-18.9** |

** Provisional data*
*Source: Foreign Exchange Office*

# 2. PRESSURES ON OUTPUT CAPACITY AND LABOR MARKET

*In view of the improvement in the crop year from one year to the next, the overall output gap, according to Bank Al-Maghrib estimates, showed a positive value in the fourth quarter of 2008. However, nonagricultural activity was impacted by the effects of the international crisis on demand. The nonagricultural output gap indeed showed positive values which were below the levels registered over the same period of the preceding year. In addition, the economic recession in our main partner countries would negatively impact this variable in the coming quarters. Output capacity utilization rate in the industrial sector dropped to its lowest level since 2007. Labor market conditions improved somewhat in the last quarter of 2008, solely because of the decline in rural unemployment rate, in connection with a better crop year. The sectors of building and public works, and services recorded a sharp deceleration in net job creation. Altogether, the analysis of all these indicators suggests a moderation of demand-driven pressure on prices in the coming quarters.*

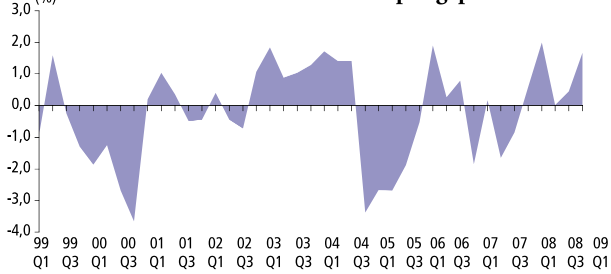
## 2.1 Pressures on output capacity

The overall output gap, based on the latest data of the HCP, registered a positive value in the third quarter of 2008, and should, according to BAM forecasts, increase further in the last quarter of 2008 and first quarter of 2009. This trend is largely attributable to the improvement in the crop year from one year to another.

The nonagricultural output gap marked a slight increase in the third and fourth quarters of 2008. Projections for the first quarter of 2009 suggest that nonagricultural output gap would grow only very slightly, but is expected to remain below the level registered in the same period of last year. However, as chart 2.2 shows, the economic recession in our main partner countries should negatively impact the nonagricultural output gap in the coming quarters (see chapters 1 and 3).

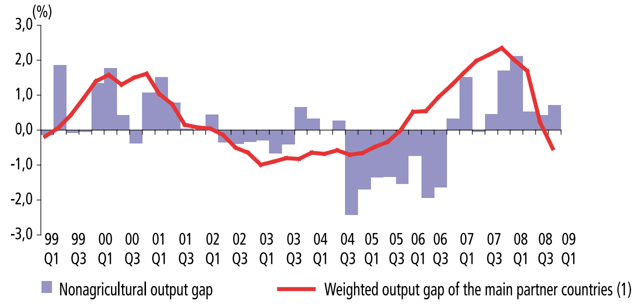
The findings of BAM monthly business survey in the industry for January 2009 indicate that output capacity utilization rate fell to its lowest level since 2007, due to the contraction in some industrial subsectors the exports of which are largely destined for Europe. At the sectoral level, output capacity utilization rate in textile and leather industries saw a sharp decrease, from 70 percent in December 2008 to 61 percent in January 2009, mostly because of the fall in production as exports shrank. In the other sectors, the rate was of 64 percent in the chemical and parachemical industries, down 2 percentage points, 62 percent in the electrical and electronic industries, 65 percent in the food-processing industries, and 73 percent in the mechanical and metal industries.

**Chart 2.1: Overall output gap**




*Sources: HCP, and BAM estimates*

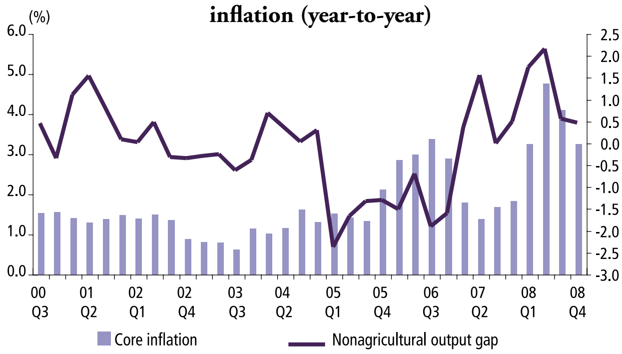
**Chart 2.2: Nonagricultural output gap**




*Sources: HCP, and BAM estimates*

*(1) Calculated on the basis of the GDP of Morocco's first five partners weighted by their respective shares in Morocco's overall exports (see Chapter 6)*

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




*Sources: HCP, and BAM estimates*

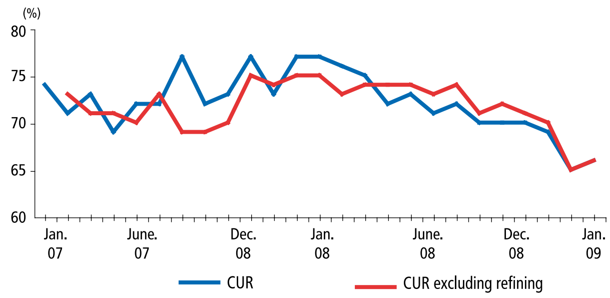
The index of apparent labor productivity[1] in nonagricultural activities remained almost unchanged at 113. This trend is attributable to the rise in urban employment at a rate similar to that of nonagricultural GDP estimated by BAM for the fourth quarter of 2008.

BAM monthly business survey also reveals that the financial costs and energy costs are one of the main sources of increase in unit production costs in the fourth quarter of 2008. Payroll costs have also contributed to the rising unit costs, due to the upward adjustment of guaranteed interoccupational minimum wage (SMIG) which came into force as from the third quarter of 2008. Financial costs increased in the textile and leather industries, against the backdrop of the sector's weakening international conditions which probably affect risk premium. The balance of opinion concerning financial costs moved up from 31 percent to 44 percent from one quarter to the next. Moreover, the survey shows that access to financing in the textile and leather sector deteriorated substantially, with a negative balance of opinion of -32 percent, and borrowing costs increased appreciably (+47 percent).

## 2.2 Pressures on labor market

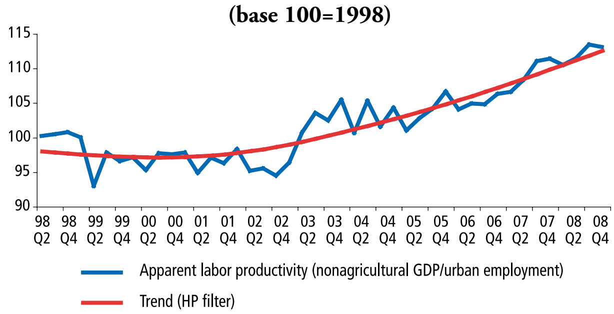
In the fourth quarter of 2008, labor force aged 15 years and over was 11,263,000 persons, increasing 2.7 percent compared with the same period of 2007. This trend results from the growth in both urban and rural labor force by 2.8 percent and 2.7 percent, respectively. Accordingly, labor force participation rate stood at 50.2 percent, up 0.4 percentage point.

**Chart 2.4: Industrial output capacity utilization rate**



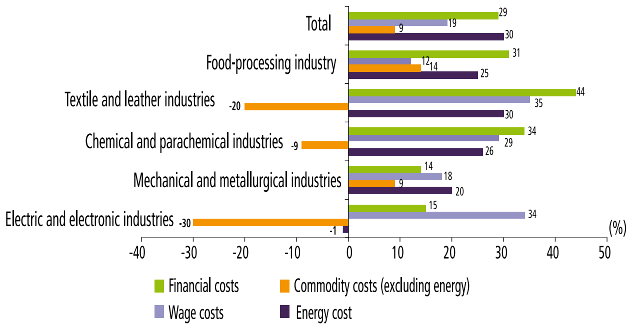

*Source: BAM monthly business survey*

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




*Sources : HCP, and BAM estimates*

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




*Source: BAM monthly business survey*

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

Employed labor force slightly increased in the fourth quarter of 2008, compared with the same quarter of last year. The employment rate rose 0.5 percentage point to 45.5 percent, as the growth rate in the number of jobs was slightly above that of labor force aged 15 years and over. Per place of residence, employment rate moved up more rapidly in rural areas than in urban ones.

Unemployment rate in the last quarter of 2008 dropped nearly three percentage points to 9.5 percent, on a year-to-year basis. On the back of the growth in agricultural activities, job gains solely concerned rural areas, where unemployment rate went down from 4.1 percent to 3.8 percent. Nonetheless, and given the slowdown in activity, the decline in urban unemployment rate reflects the growth rate of unemployed labor force that was less rapid than that of labor force.

The most substantial decline in urban unemployment rate was observed in the 25-34 age group (-0.8 percentage point) and the 15-24 age group (-0.3 percentage point). In contrast, the only sizable increase in unemployment rate was recorded among the age group of more than 44 years, from 1.7 percent to 2 percent in the fourth quarter of 2008.

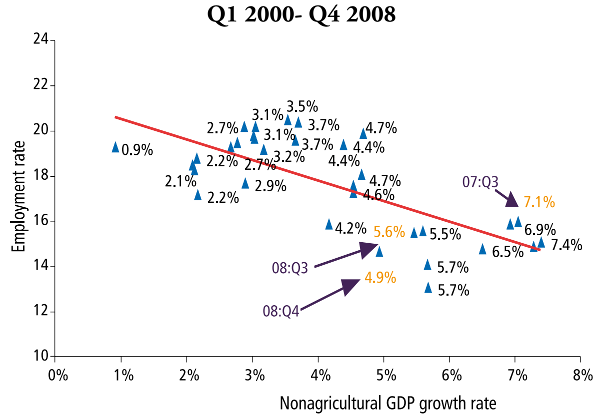
Net creation of gainful employment reached 248,000 in the fourth quarter. Unpaid labor moved up 49,000, attributable to an increase of 61,000 jobs in rural areas and a decline of 12,000 jobs in urban areas. The sector of "agriculture, forestry and fisheries" recorded sizable increase in job creation, with 208,000 new job gains. The other sectors contributed 89,000 new jobs, of which 44,000 in the industry, 25,000 in building and public works, and 23,000 in the service-producing sector. In terms of variation, job creation in building and public works and in services decelerated, as the year-on-year rate of change moved down from 9.7 percent to 2.8 percent and from 4.2 percent to 0.6 percent, respectively.

**Table 2.1: Activity and unemployment quarterly indicators by place of residence(1)**

| In millions | Q4 - 2007 | | | Q4 - 2008 | | |
|---|---|---|---|---|---|---|
| | Urban | Rural | Total | Urban | Rural | Total |
| **Labor force and employment** | | | | | | |
| Labor force (2) | 5.7 | 5.2 | **11.0** | 5.9 | 5.4 | **11.3** |
| Labor force participation rate (%) | 44.3 | 57.6 | **50.0** | 44.4 | 59.0 | **50.2** |
| Employed labor force | 4.8 | 5.0 | **10.0** | 5.0 | 5.2 | **10.2** |
| Employment rate (%)(3) | 37.7 | 55.3 | **45.0** | 37.9 | 56.3 | **45.5** |
| **Unemployment** | | | | | | |
| Unemployed labor force | 0.9 | 0.2 | **1.0** | 0.9 | 0.2 | **1.1** |
| Unemployment rate (in %) | 14.8 | 4.1 | **9.7** | 14.6 | 3.8 | **9.5** |
| By degree | | | | | | |
| . Non-graduates | 7.8 | 2.7 | **4.6** | 7.9 | 2.7 | **4.6** |
| . Graduates | 20.4 | 12.0 | **19.0** | 20.2 | 10.7 | **18.4** |

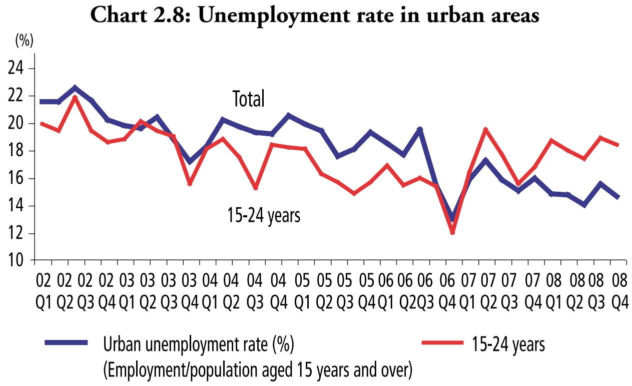
*(1) Data adjusted according to the new population forecasts*
*(2) Population aged 15 years and over (in millions of persons)*
*(3) Employed labor force/total population aged 15 years and over.*
*Source: HCP*

**Chart 2.7: Nonagricultural GDP and urban unemployment Q1 2000- Q4 2008**




*Source: HCP*

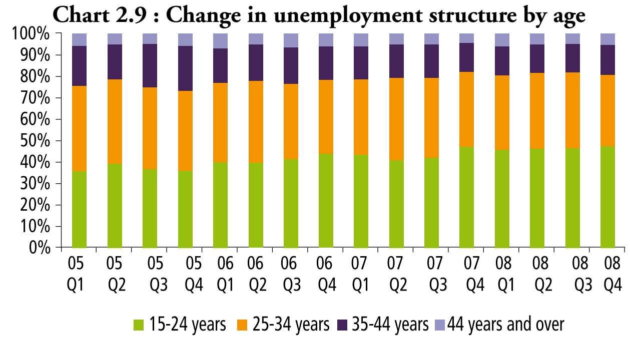
**Chart 2.8: Unemployment rate in urban areas**




*Source: HCP*

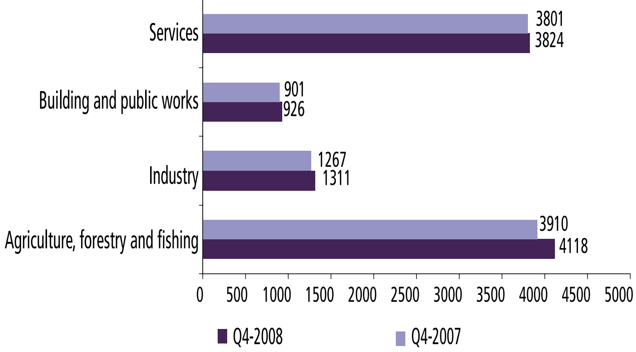
According to the findings of BAM business survey for the fourth quarter of 2008, total labor force employed in industry increased somewhat from one quarter to the next, with a balance of opinion of 13 percent. Nevertheless, textile and leather industries and electrical and electronic industries registered a drop in staff due to the decline in exports.

**Chart 2.9 : Change in unemployment structure by age**



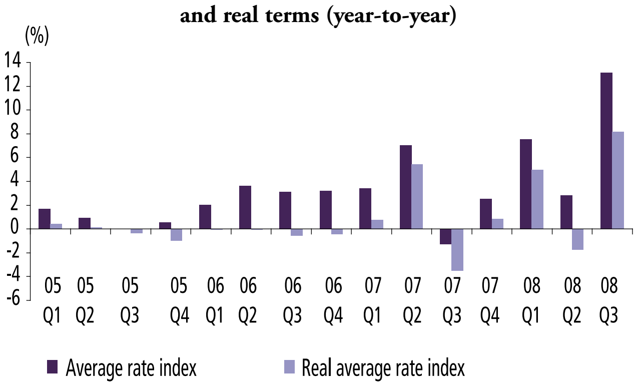

*Source: HCP*

**Chart 2.10 : Change in employment by sector (labor force in thousands)**



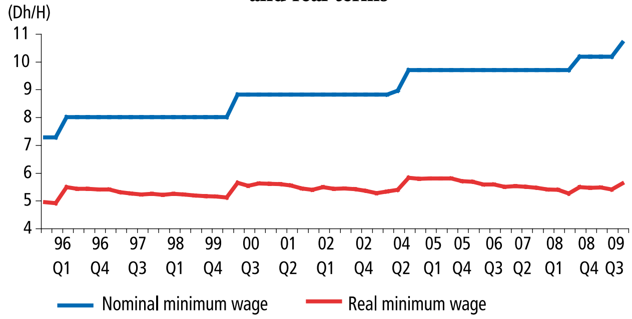

*Source: HCP*

**Chart 2.11 : Private sector average wage index in nominal and real terms (year-to-year)**




*Sources: HCP, and BAM estimates*

**Chart 2.12 : Quarterly minimum wage in nominal and real terms**




*Sources: Ministry of Labor, and BAM calculations*

## 3. IMPORT PRICES

*In a context of substantial slowdown in the global economy and decline in commodity prices, headline inflation in most developed and emerging countries in January 2009 continued the downward trend that began in August 2008. As regards monetary conditions, the international environment remains marked by the massive monetary easing undertaken by the major central banks, as the global economy has entered recession, reconfirmed by IMF's latest projections of January 2009. The sharp and synchronized downturn is becoming increasingly noticeable in the advanced countries, particularly in the euro area, our main trading partner. In Morocco, non-energy import price index, calculated on the basis of the latest provisional data as of late January 2009, shows 6.3 percent drop from the previous month. This trend, which involved import prices of food, mining and semifinished products, was facilitated by the continued decline in world prices since the second half of 2008. Overall, these factors should lead to a gradual easing of inflationary pressures over the coming quarters.*

### 3.1 World inflation

Against a backdrop of rapidly weakening prospects for global growth, evidenced by signs of deep recession in most advanced countries, the downward trend in inflationary pressures that began last August continued in January 2009 in the major developed countries according to Eurostat's latest data available. Headline inflation rate in the euro area increased to 1.2 percent in February 2009, from 1.1 percent a month earlier.

In the United States, headline inflation was nil in January 2009, after reaching 0.1 percent the previous month. It was also nil in Japan, falling from 0.4 percent to 0 percent. In France and Germany, headline inflation fell from 1.2 percent and 1.1 percent to 0.8 percent and 0.9 percent, respectively. Similarly, in Spain and Italy, headline inflation slowed down to 0.8 percent and 1.4 percent, respectively, after rising to 1.5 percent and 2.4 percent the previous month. The reduction in inflationary pressures resulted from the sharp decline in the international prices of commodities, particularly of oil, in connection with the sizable weakening of demand from the advanced economies, notably the United States and the euro area, as well as from the emerging countries, especially China.

This trend is the result of the severe global recession which is further confirmed by IMF predictions. Indeed, the latest IMF projections of January 2009 indicate that headline inflation

**Table 3.1: Recent change in world inflation**
( year-to-year )

| | 2008 Jan. | 2008 Dec. | 2009 Jan. | Forecasts 2009 | Forecasts 2010 |
|---|---|---|---|---|---|
| United States | 4.3 | 0.1 | 0.0 | 0.4 | 0.7 |
| Euro area* | 3.1 | 1.6 | 1.1 | 1.0 | 1.8 |
| Germany | 3.1 | 1.1 | 0.9 | 0.8 | 1.4 |
| France | 2.4 | 1.2 | 0.8 | 0.8 | 1.5 |
| Spain | 4.1 | 1.5 | 0.8 | 0.6 | 2.4 |
| Italy | 2.4 | 2.4 | 1.4 | 1.2 | 2.2 |
| Japan | 1.0 | 0.4 | 0.0 | -1.4 | -0.5 |
| China | 6.3 | 1.2 | 1.0 | - | - |

*(*) Harmonized indices*

*Sources: IMF, Eurostat*

in the advanced countries and in the emerging and developing countries would continue to subside to 0.3 percent and 5.8 percent in 2009, respectively, down from the 1.4 percent and 7.1 percent predicted in November 2008 and 2 percent and 7.8 percent in October.

The worse-than-expected deterioration of global growth prospects, coupled with severely strained financial conditions despite economic stimulus and stabilization policies, suggests inflationary pressures would subside in the short term in most regions of the world.

## 3.2 Oil prices

In February 2009, oil prices fell 4.8 percent on a monthly average, to reach $41.8 a barrel. This new decline boosted the downward trend that began in August 2008. In the fourth quarter of 2008, oil prices averaged $56.1 a barrel, compared with $115.5 in the previous quarter, down 51.4 percent from one quarter to the next. In 2008, the average price of oil, however, rose 46.8 percent year on year, from $71.1 a barrel in 2007 to $97.

The sharp fall in oil prices in February 2009 is mostly linked to the slump in global demand for oil by 980,000 barrels per day in 2009.

In IMF's latest projections of January 2009, baseline petroleum price projection was revised down to $50 a barrel for 2009, from $68 in the November WEO Update and $100.5 in October. In 2010, it is expected to increase to $60 a barrel. In line with these data, oil price on the futures market would average $46.7 a barrel in 2009 and $52.1 in 2010.

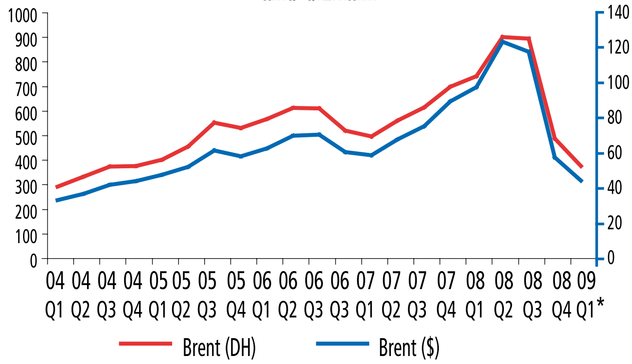
According to most international market participants, the growth forecasts of the global oil market still depend on the future developments in the international economic and financial conditions. Their projections remain conditioned, in part, by the risks of a severe and long-lasting recession of the global economy in 2009. Market participants also anticipate that it would take longer than

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

| | Q1 2009 | Q2 2009 | Q3 2009 | Q4 2009 | Year 2009 | Year 2010 |
|---|---|---|---|---|---|---|
| Futures | 44.8 | 45.2 | 46.5 | 48.3 | 46.7 | 52.1 |

*Source: Bloomberg*

**Chart 3.1: Brent world price in US dollar and dirham**




** The first quarter of 2009 corresponds to the arithmetic average of January and February data.*

*Source: IMF*

expected for financial strains to ease and for stimulus plans to positively impact global economic activity.

## 3.3 Commodity prices

The prices for non-energy commodities continued to slowdown at the beginning of the year, dragged down by the slump in global demand. In the first two months of 2009, the World Bank's non-energy commodity price index for low and middle income countries fell on average 27.1 percent compared with the same period last year. In February, it declined 1.4 percent on a month-to-month basis.

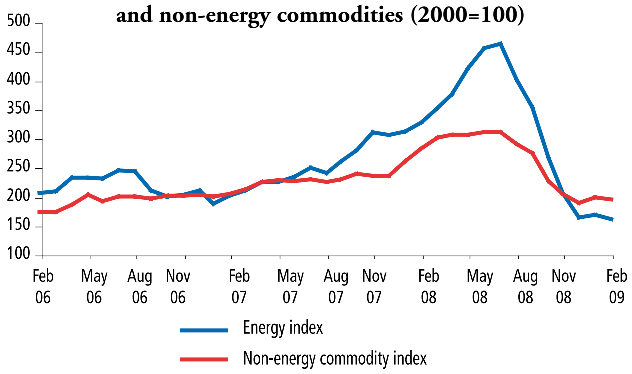
Food price index decreased at a monthly rate of 1.1 percent and an annual rate of 23 percent as of late February 2009. Cereal prices plunged, particularly those of wheat and corn which fell 6 percent and 5.4 percent, respectively, from one month to the next. This trend is mostly attributable to the 3.5 percent annual rise in 2008 production expected by the Food and Agriculture Organization of the United Nations (FAO), which should help to replenish inventories. On a year-to-year basis, wheat and corn prices declined 47.1 percent and 25.7 percent, respectively.

Similarly, the price index of metals and minerals fell 0.4 percent in February 2009, compared with the previous month, largely because of the impact of the global downturn on demand for these commodities.

The major declining metals were zinc and lead, with respective falls of 6.3 percent and 2.8 percent from one month to the next. In contrast, prices of copper and steel increased somewhat in connection with the reduced production in the main producing countries of these two metals since the last quarter of 2008. Metals and minerals index fell 40.2 percent, on a year-to-year basis, as of the first two months of 2009.

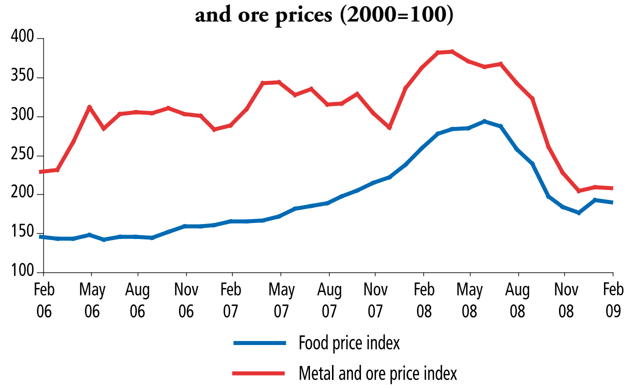
In its latest forecasts, the IMF again revised downward its projections for nonfuel commodity prices, which would now decline 29.1 percent

**Chart 3.2: Price index of energy products and non-energy commodities (2000=100)**




*Source: World Bank*

**Chart 3.3: Index of food, metal and ore prices (2000=100)**



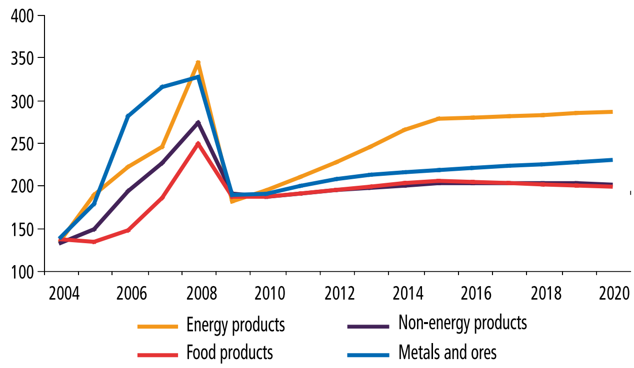

*Source: World Bank*

**Table 3.3 : Change in wheat futures and forecasts**

| Wheat (USc/ bushel) | Q1 2009 | Q2 2009 | Q3 2009 | Q4 2009 | Year 2009 |
|---|---|---|---|---|---|
| Futures | 562.40 | 527.47 | 558.85 | 583.03 | 562.40 |
| Forecasts | 565.00 | 605.00 | 650.00 | 665.50 | 650.52 |

*Source: Bloomberg*

**Chart 3.4: Forecast change in commodity price indexes**




*Source: World Bank*

in 2009. This trend would result from the sharp deterioration of the global economic conditions in 2009 and a downward revision of demand outlook.

Food prices, however, are expected to remain volatile, especially cereals, whose production of 2008 did not allow a good replenishment of inventories and the sowed lands of which in 2009 would be reduced in the main producing countries, particularly the United States and Europe.

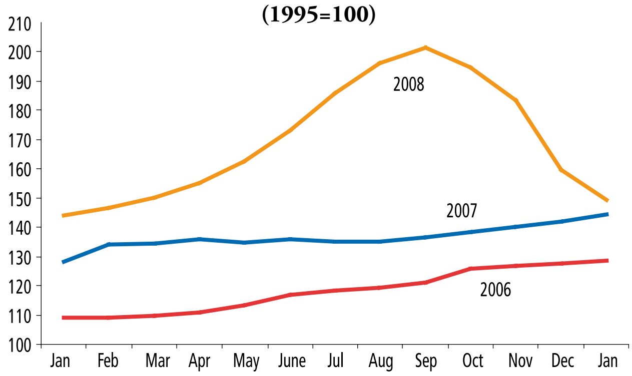
The price trend of metals remains largely dependent on the development of the global economic conditions which are expected to worsen in 2009. In fact, the major international mining groups should continue or even increase the cut in production against a backdrop of credit crunch and falling demand coupled with increasingly rising inventories. In 2009, metals prices would remain highly volatile and trend downward. However, the increase in demand for these commodities may push prices to quite high levels.

## 3.4 Import price indexes

Based on the latest data available as of January 2009, the import price index (IPI) of non-energy commodities shows a 6.3 percent decline compared with December 2008, continuing the downward trend that began in October 2008 (-3.2 percent). This change reflects the new drop in world commodity prices (see section 3.3). Therefore, the import price indexes of food, minerals and semifinished products were down. On a year-to-year basis, non-energy IPI was up 3.6 percent in January 2009, at a level substantially below that recorded in December 2008 (+12.5 percent).

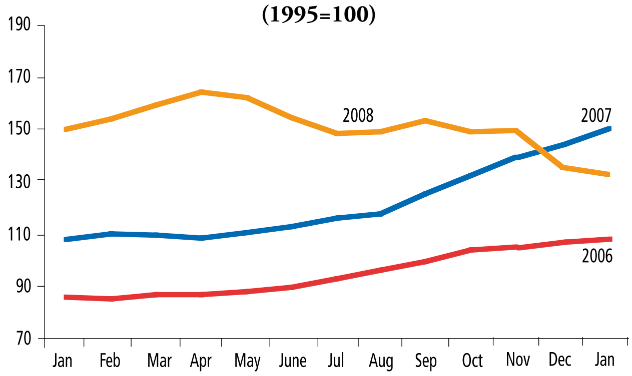
The IPI of food continued to fall in January 2009 (-1.7 percent), on a monthly basis. The import prices of wheat and corn fell sizably due to the rise in global cereal production in 2008 and the drop in Morocco's cereal imports after the relatively good harvest of the 2008-2009 crop

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



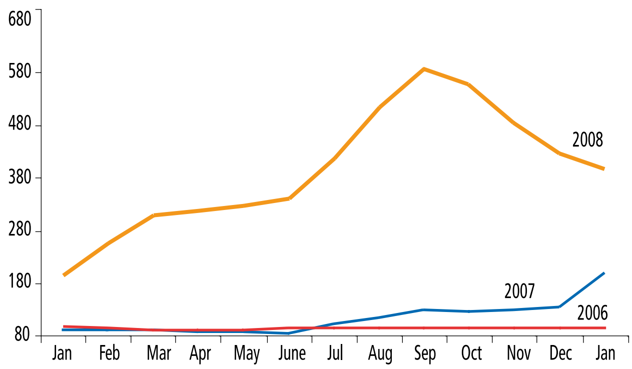

*Sources: Foreign Exchange Office, and BAM calculations*

**Chart 3.6: Food import price index (1995=100)**




*Sources: Foreign Exchange Office, and BAM calculations*

**Chart 3.7: Import price index of mining commodities (1995=100**



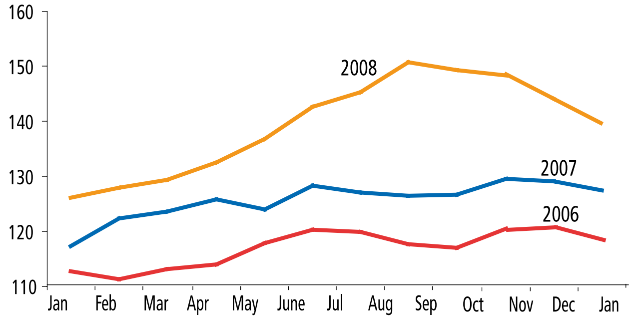

*Sources: Foreign Exchange Office, and BAM calculations* year. Similarly, import prices of raw vegetable oils and dairy products decreased appreciably.

The same trend was observed in the IPI of minerals, with a 6.6 percent decline in January 2009, after a monthly drop of 12 percent in December 2008. Import prices of copper and iron ore slumped at a monthly rate of 29.4 percent and 36.5 percent, respectively, as international prices of most minerals trended downward following the downturn in demand and the positive trend in the world inventories of these products.

Likewise, the IPI of semifinished products declined 2.3 percent in January 2009, compared with December 2008, because of the reduced production in processing industries.

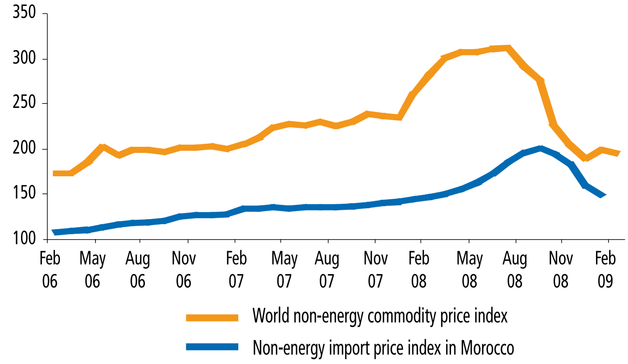
Overall, inflationary pressures arising from import prices are expected to subside in the coming quarters. World commodity prices should, however, remain extremely volatile in 2009.

**Chart 3.8: Import price index of semifinished products (1995=100)**




*Sources: Foreign Exchange Office, and BAM calculations*

**Chart 3.9: Change in the world non-energy commodity price index and the domestic non-energy import price index**




*Sources: World Bank, Foreign Exchange Office*

# 4. MONETARY CONDITIONS AND ASSET PRICES

*The data of the fourth quarter of 2008 and of January 2009 show the continued decline in pressures arising from monetary conditions. The slowdown in money creation reduced nonfinancial agents' excess money. It mostly reflects the negative contribution of net foreign assets and claims on the Government to money growth. The slowdown in credit, underlined in the previous MPR, continued but credit growth rate remained above its long-term average, with an annual rate of 25 percent in the fourth quarter of 2008 and 21 percent in January 2009, due to the 1 percent monthly drop. As regards lending rates, data of BAM survey for the last quarter of 2008 indicate a moderate increase in the weighted average rate, which largely reflects a slight rise in rates on consumer loans and real estate loans, as well as a fall in rates on equipment loans. Deposit rates decreased in January after several quarters of increase, because of the relaxation of banks' liquidity constraints following the 3 percent cut in reserve requirement ratio to 12 percent as from January 1, 2009, and probably the slowdown in credit growth. Stock market prices continued to trend downward, but improved in February. The dirham appreciated against the euro and depreciated against the US dollar.*

## 4.1 Monetary conditions

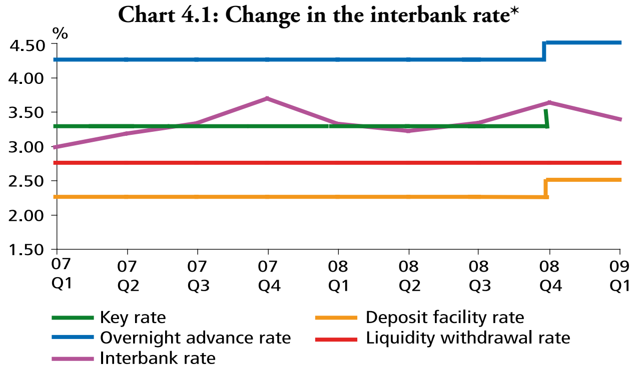
### 4.1.1 Interest rates

At The Board of Bank Al-Maghrib, at its meeting of December 23, 2008, decided to keep the key rate unchanged at 3.50 percent, and to reduce the reserve requirement ratio three percentage points to 12 percent as from January 1, 2009. Against this backdrop, the interbank rate averaged 3.37 percent over the period from January 1 to March 8, 2009, or 3.43 percent excluding the drops linked to the maintenance of reserve requirements, after reaching 3.62 percent in the fourth quarter of 2008.

At the same time, very short-term Treasury bills went downward in January 2009, reversing the upward trend that lasted until the fourth quarter of 2008. Yields on medium and long-term Treasury bills on the secondary market registered a similar trend marked by an increase in the last quarter of 2008 followed by a decline in January and February 2009.

The weighted average rate of deposit rates on 6 and 12-month deposits fell in January to 3.79 percent, after the uptrend of the fourth quarter of 2008.

**Chart 4.1: Change in the interbank rate***

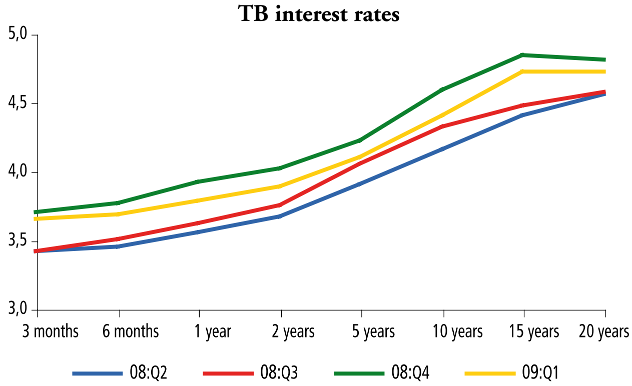



** Observation of the first quarter of 2009 corresponds to the daily average of the period from January 1st to March 8th, 2009.*

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

| | 2007 | | | 2008 | | | | 2009 |
|---|---|---|---|---|---|---|---|---|
| | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | January |
| 13 weeks | 3.30 | 3.29 | 3.63 | 3.58 | 3.41 | 3.42 | 3.69 | 3.65 |
| 26 weeks | 3.34 | 3.32 | 3.58 | 3.59 | - | - | 3.77 | 3.71 |
| 52 weeks | 2.88 | 3.40 | 3.55 | 3.62 | 3.53 | 3.51 | 3.84 | 3.79 |

**Chart 4.2 : Change in maturity structure of secondary market TB interest rates**



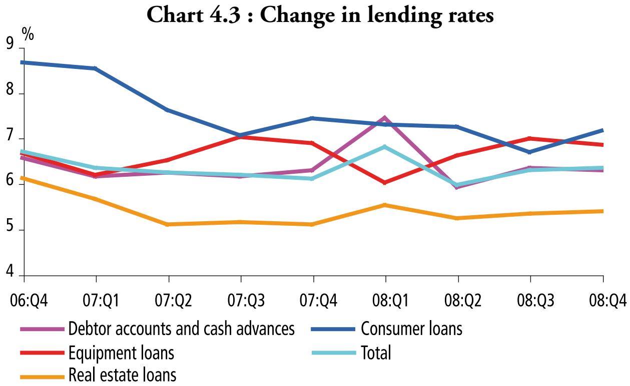
Concerning lending rates, Bank Al-Maghrib quarterly survey among banks shows a moderate increase in the weighted average rate in the fourth quarter of 2008, in response to the degree, real estate loans. Meanwhile, lending rates on cash advances and equipment loans declined 2 and 11 basis points, respectively.

**Table 4.2 : Deposit rates * (time deposits)**

| | 2007 | | 2008 | | | | 2009 |
|---|---|---|---|---|---|---|---|
| | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | January |
| 6 months | 3.41 | 3.49 | 3.37 | 3.55 | 3.50 | 3.90 | 3.76 |
| 12 months | 3.69 | 3.71 | 3.71 | 3.82 | 3.89 | 4.23 | 3.83 |
| Weighted average | 3.60 | 3.62 | 3.56 | 3.72 | 3.77 | 4.13 | 3.79 |

** Quarterly data are simple averages of monthly data*

**Chart 4.3 : Change in lending rates**




## Box 4.1: Liquidity and implementation of monetary policy

During the fourth quarter of 2008, the restrictive trend in autonomous factors increased appreciably, due primarily to the contraction in BAM's net foreign assets. As a consequence, banks' liquidity shortage moved up from 10.4 billion dirhams in the third quarter of 2008 to 17.5 billion in the fourth quarter of 2008.

Foreign currency purchases by commercial banks totaled 20 billion dirhams owing to the rising volatility of international markets in the context of the international financial crisis. Sales of foreign banknotes, which declined sizably compared with the previous quarter, stood at 6.9 billion dirhams. Therefore, the restrictive impact of NFA on liquidity was of 13.1 billion dirhams.

**Chart B 4.1.1: Change in liquidity position (in millions of dirhams) and in the weighted average rate (%) in quarterly average**

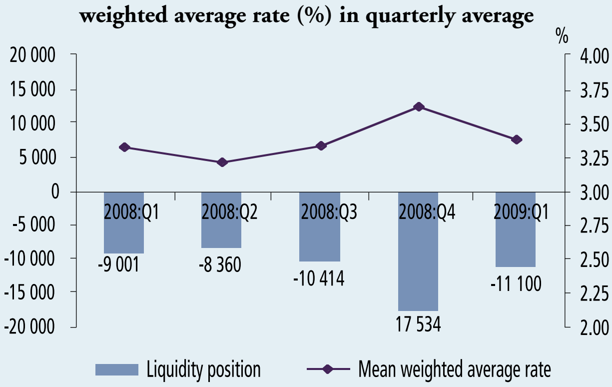
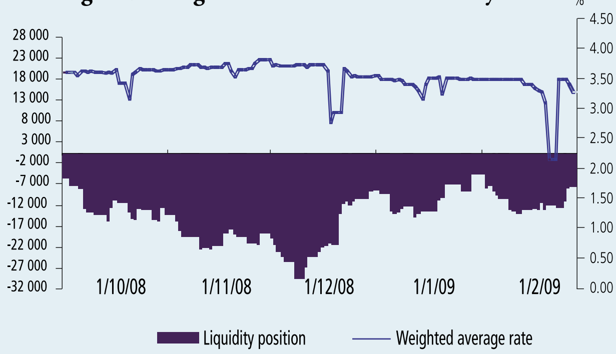



**Chart B 4.1.2: Liquidity position (in millions of dirhams) and weighted average rate of the interbank money market**




Liquidity position : Balance of banks - required reserves +/- BAM interventions

Currency in circulation increased 2.9 billion dirhams, largely because of Eid Al Adha (Feast of the Sacrifice) and the New Year. In contrast, Treasury operations led to an injection of liquidity in amounts of 6.2 billion dirhams, given the accelerated pace of budget execution at the end of the year. In fact, Treasury expenditure increased to 77 billion dirhams, of which 13 billion account for repayments of domestic debt to the banking system and nearly 11.8 billion for subsidization costs. Treasury receipts totaled 70.9 billion dirhams, 20.3 billion of which come from banks' subscriptions to Treasury bill auctions.

Overall, autonomous factors exerted a restrictive effect of 9.8 billion dirhams on banks' liquidity. As liquidity diminished further in the fourth quarter of 2008, the Board of Bank Al-Maghrib decided, at its meeting of December 23, to reduce the reserve requirement ratio 3 percentage points to 12 percent as from January 1, 2009.

The cut in this ratio led to an overall liquidity injection in amounts of 10.4 billion dirhams (7.5 billion on December 21, 2008 and 2.9 billion in January 21, 2009). As a consequence, banks' average liquidity shortage narrowed from 17.5 billion dirhams in the fourth quarter of 2008 to 11.1 billion in the first quarter of 2009.

**Chart B 4.1.3: Change in reserve requirements (in millions of dirhams)**

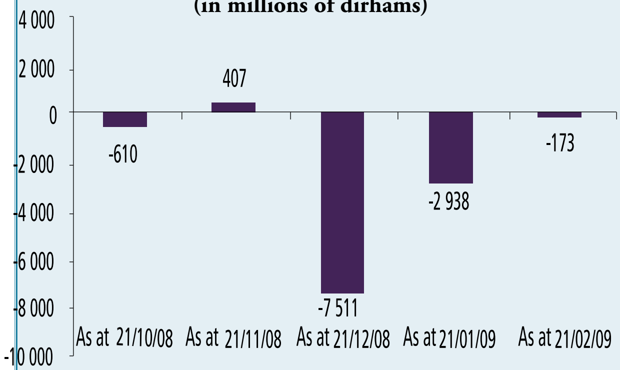
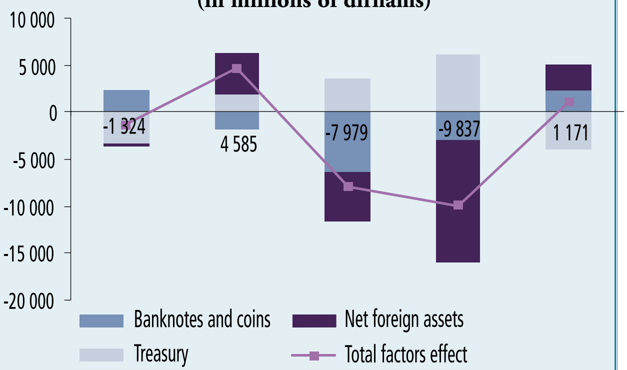



**Chart B 4.1.4: Change in liquidity factors' effect (in millions of dirhams)**




Over the first quarter of 20091[1], autonomous factors slightly impacted banks' liquidity. Treasury operations led to a liquidity drain of 3.9 billion dirhams, mostly attributable to purchases of Treasury bills at auctions.

Treasury assets totaled 48.5 billion dirhams, 15.8 billion of which account for banks' subscriptions to TB auctions. Treasury liabilities rose to 44.6 billion dirhams, 12.4 billion of which represent repayments of domestic debt to the banking system and nearly 3 billion for subsidization costs.

However, foreign asset transactions entailed an injection of liquidity in amounts of 2.7 billion dirhams. Foreign currency purchases by commercial banks, which were substantially lower than the previous quarter, only stood at 1.2 billion dirhams. Moreover, sales of foreign banknotes reached 3.9 billion dirhams.

The decline in currency in circulation, following the significant withdrawals during the New Year and the religious feasts, was 2.3 billion dirhams.

*(1) Data as of the end of February 2009.*

**Chart B 4.1.5: BAM interventions on the money market (in millions of dirhams)**

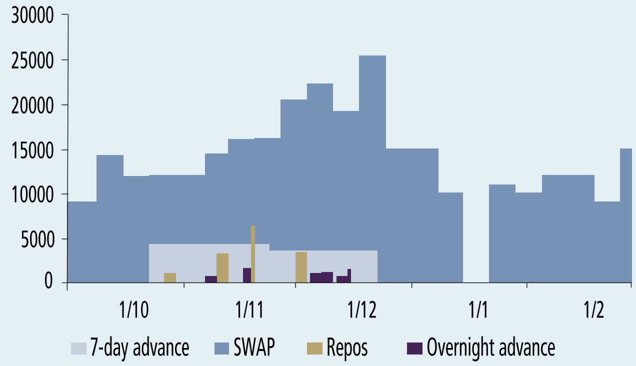
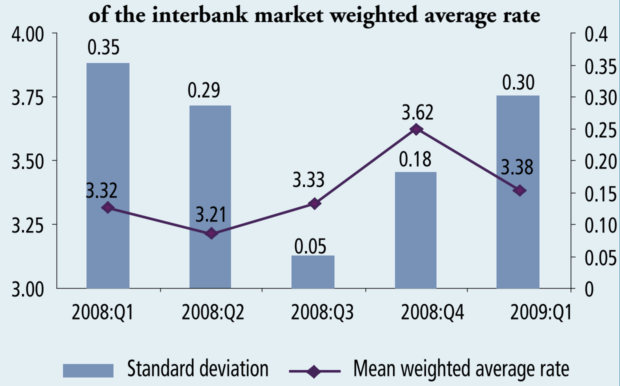



**Chart B 4.1.6: Change in the mean and standard deviation of the interbank market weighted average rate**




Altogether, autonomous factors exerted an expansive effect of 1.2 billion dirhams on banks' liquidity.

To ease banks' liquidity shortage, which averaged 11.1 billion dirhams during this quarter, Bank Al-Maghrib intervened exclusively through 7-day advances, providing an average daily amount of 10.1 billion dirhams.

During the first quarter of 2009, the mean weighted average rate settled at 3.38 percent, down 24 basis points compared with the previous quarter, on account of the following:

- the cut in the required reserve ratio;
- decrease in some banks' funding needs;
- declines in the interbank rate at the end of the reserve period.

Therefore, the end-of-reserve-period adjusted mean weighted average rate reached 3.46 percent at the end of February.

The volatility of the weighted average rate rose 12 basis points, from 0.18 percent to 0.30 percent. Apart from end of reserve periods, the volatility of the weighted average rate stood at 0.09 percent.

## 4.1.2 Money, credit and liquid investments

### M3 growth

Money supply continued to slow down in the fourth quarter of 2008 and January 2009. As a result, excess money, which peaked in the last quarter of 2007, registered a continuous contraction and vanished in the fourth quarter of 2008.

Between the fourth quarter of 2008 and January 2009, the annual growth of money supply remained unchanged at

**Chart 4.4: M3 annual growth and its trend (in %)**

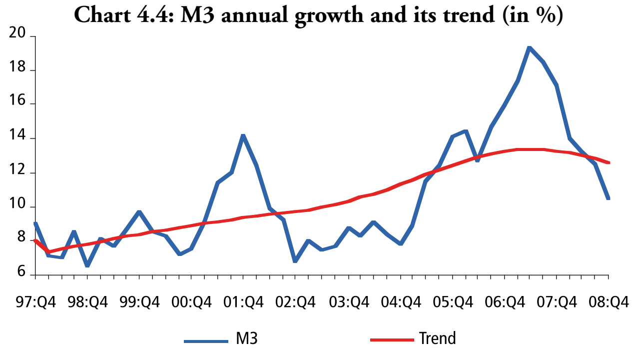
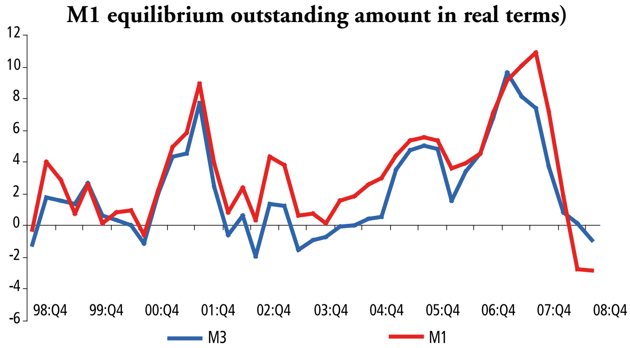



**Chart 4.5: Money surplus (in percentage of M3 and M1 equilibrium outstanding amount in real terms)**



10.4 percent, down from 12.5 percent in the third quarter of 2008. M3 deceleration reflects the slowing pace of money holdings' constitution by all nonfinancial agents. Therefore, the growth rate of total private individuals' deposits slowed down to 9.2 percent, whereas deposits of nonfinancial businesses grew at a rate lower than that of economic growth, at 4.8 percent. Corporate deposits with banks seem to reflect the negative shock which the cash holdings of businesses underwent, as evidenced by the decline in sales announced by the industrial sector businesses and the fall in the service sector's turnover suggested by the drop in tourist receipts. Deposits of Moroccans living abroad, which grew 5.9 percent in the fourth quarter of 2008, saw a deceleration starting from the second half of 2008, under the impact of the decline in their current transfers to Morocco as a result of the deteriorating economic situation in the host countries.

M3 structure by type of cash shows a sharp slowdown in non-interest bearing demand deposits to the benefit of time deposits, the rates of which became more attractive boosted by the increase in banks' refinancing costs and the intense competition among banks on this segment.

In contrast, interest-bearing demand deposits and currency in circulation registered no significant changes.

## Bank loans

The latest data available show the continued deceleration of bank credit, the annual growth of which fell to 25.1 percent at the end of the fourth quarter of 2008 and 20.7 percent in January. On a month-to-month basis, bank loans

**Chart 4.6: Annual growth of M3 components (in %)**

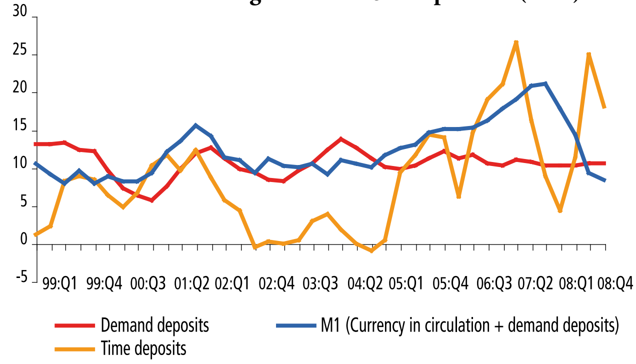



**Chart 4.7: Bank loans' annual growth and trend (in %)**

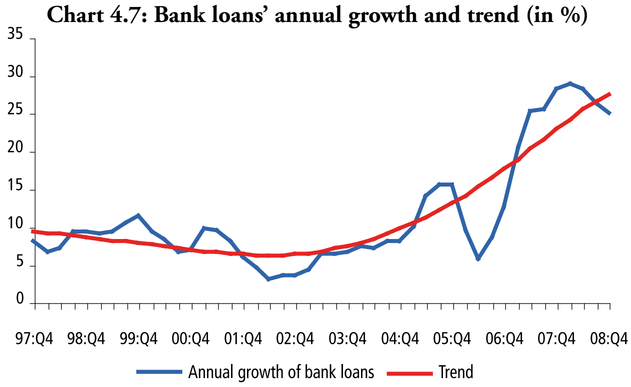



**Chart 4.8: Loans' structure by economic agent (in billions of dirhams)**

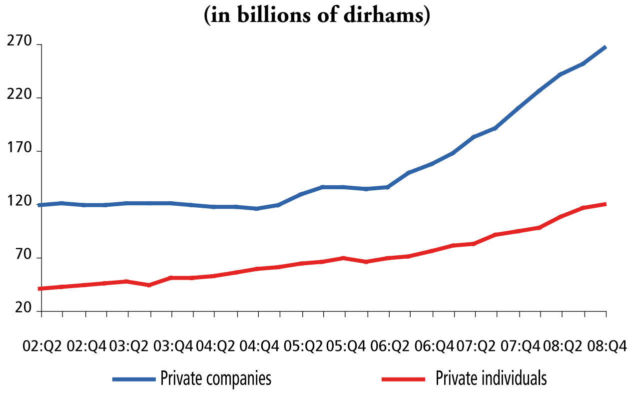
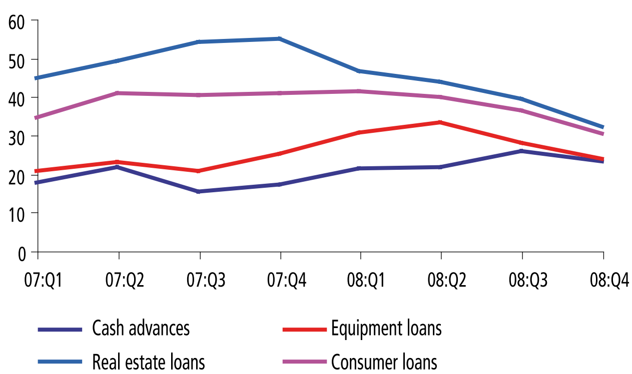



**Chart 4.9: Annual change in the main bank loan categories**



declined 1 percent at the end of January, the lowest level since April 2006.

Analysis of credit structure shows that the slowdown concerns all nonfinancial agents and in the same proportions. Loans to private individuals increased 22.3 percent in January, down from 25.7 percent in the fourth quarter, whereas loans to businesses grew 22.5 percent, compared with 26.7 percent.

In a context marked by the absence of a clear upward trend in lending rates, this change confirms the gradual convergence of credit growth to its long-run trend. According to fragmented data, the slowdown in real estate loans in particular is thought to be caused by the decline in household demand, parallel to the contraction in transactions on some segments of the real estate market.

## Other sources of money creation

Net foreign assets in the fourth quarter of 2008 fell 8.1 percent from one quarter to the next and 4.4 percent on a year-to-year basis, due primarily to the widening trade deficit and the decline in travel revenues and expatriate remittances. Despite a slight recovery of 1.2 percent in January 2009, the amount outstanding of foreign exchange reserves was 6.5 percent lower than that of January 2008.

The pace of contraction in net claims on the Government was subdued in the last quarter of 2008 and January 2009, due to the slight rise in Treasury issuance coupled with the fall in its holdings with Bank Al-Maghrib.

Altogether, all sources of money creation negatively impacted money supply growth in January 2009.

## Liquid investments

At the end of the fourth quarter of 2008, liquid investments decreased 8.7 percent compared with the same period of last year.

Securities of money market UCITS grew at an annual rate of only 26.5 percent, compared with an exceptional growth of around 67 percent in

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

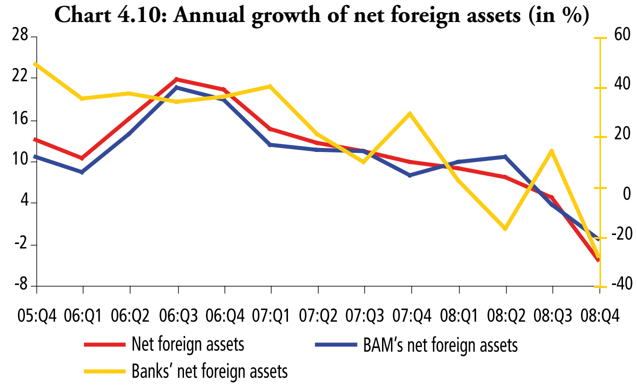



**Chart 4.11: Quarterly change in net claims on the Government (outstanding amount in billions of dirhams)**

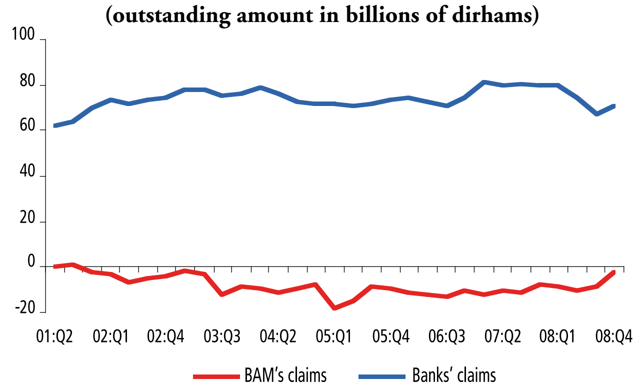



**Chart 4.12: Main counterparties' contribution to money supply growth (in %)**

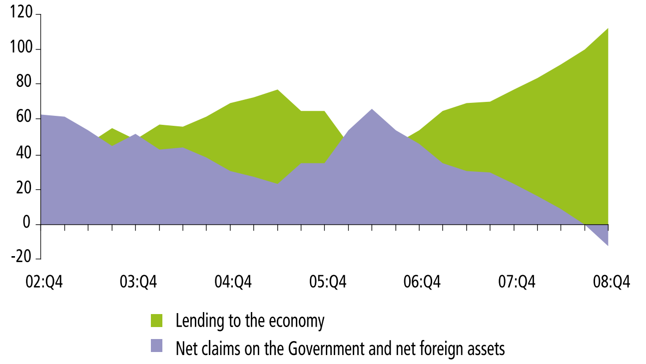
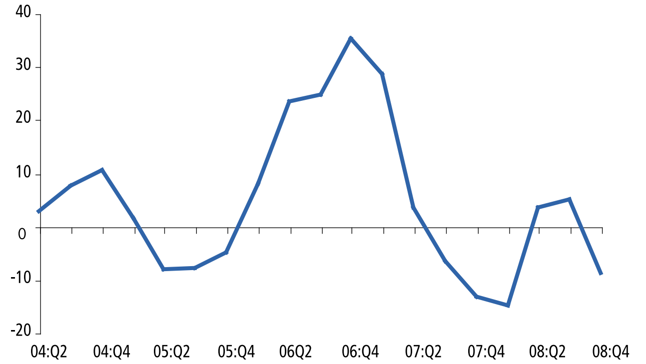


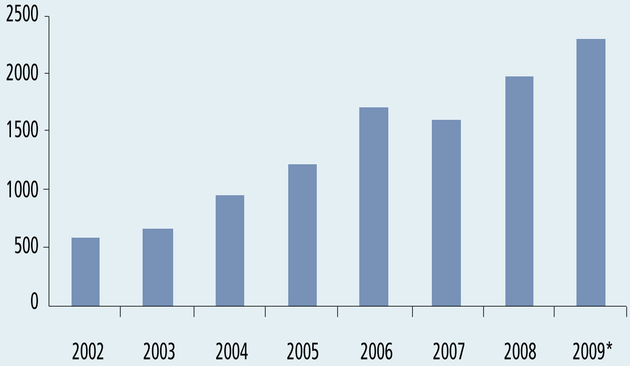

**Chart 4.13: Annual change in liquid investments (in %)**



## Box 4.2: Monetary conditions in Morocco shielded from the direct impact of the international financial crisis

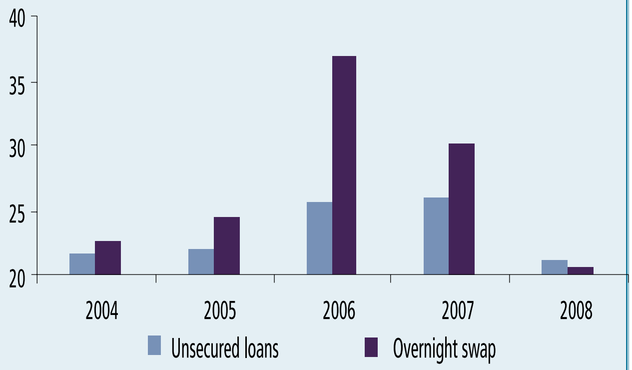
Although the uncertainty prevailing for several months now in the international money markets, as a result of multiple bank bankruptcies, has generally led to a substantial decline in unsecured loans and interbank transactions, monetary conditions in Morocco remain shielded from first-round effects of the international financial crisis. The expansion in the amounts exchanged between Moroccan banks attests to the continued smooth running of the national interbank market.

**Chart B 4.2.1: Average volume exchanged on the Moroccan interbank market (in millions of dirhams)**




* *Average of the first two months of the year*

**Chart B 4.2.2: Euro area interbank market (in billions of euros)**




Similarly, the tightening of credit conditions for businesses and private individuals following the rise of risks and the drying up of liquidity in the developed countries, due to the spreading of confidence crisis, did not affect credit growth in Morocco. Loans indeed grew at a relatively steady pace, despite a slight downward adjustment after periods of excessive growth. The sustained credit growth in Morocco did not require either an expansion of the monetary base[1], in contrast to the change registered in the main countries directly impacted by the financial crisis.

**Chart B 4.2.3: Bank credit in Morocco (in billions of dirhams)**

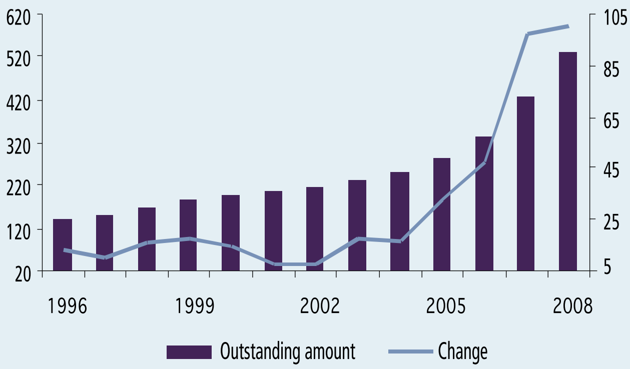
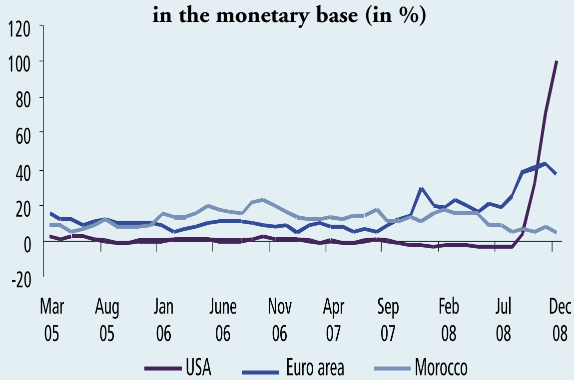



**Chart B 4.2.4: Bank credit in the euro area (in billions of euros)**


**Chart B 4.2.5: Year-to-year change in the monetary base (in %)**




Sources: IMF, BAM

1 The monetary base in Morocco includes currency in circulation, deposits with the central bank and other liabilities of the central bank with the exception of the deposits of the Treasury and the Hassan II Fund.

the previous two quarters. This adjustment largely reflects the contraction in the portfolio of businesses, who generally reduced their investments in UCITS' securities in the fourth quarter of 2008. This is also thought to be attributable to the preference of private individuals for time deposits with banks, the interest rate of which outpaced money market yields.

The trend in liquid investments reflects the continued fall in the securities of bond UCITS, largely because of the depreciation of their value along with the rise in secondary market TB yields. It is also attributable to the contraction in nonfinancial agents' portfolio of securities of equity and diversified UCITS as prices on the Casablanca stock exchange market plummeted.

### 4.1.3 Exchange rates

At the end of the last quarter of 2008 and compared with the previous quarter, the dirham on average rose 7.78 percent against the pound sterling, and 2.34 percent against the euro. Meanwhile, it depreciated 20.38 percent against the Japanese yen, 10.5 percent against the dollar, and 3.25 percent against the Swiss franc. This trend continued in January and February 2009, as the dirham on average appreciated 0.17 percent against the euro and depreciated 0.76 percent against the dollar.

The nominal effective exchange rate of the dirham, based on bilateral exchange rates with regard to Morocco's major partners, rose 0.23 percent in the fourth quarter of 2008 compared with the previous quarter. At the same time, the unfavorable trend in the inflation differential led to a slight rise of 1.07 percent in the real effective exchange rate of the dirham, on a quarter-to-quarter basis.

## 4.2. Asset prices

At the end of the last quarter of 2008, the MASI index continued to trend downward compared with the previous quarter, losing 12 percent, mostly because of the 20.4 percent fall in the real estate index. Against this backdrop, the broad index of the Casablanca stock market lost 13.5

**Chart 4.14: Change in the securities of money market and bond UCITS (in millions of DH)**

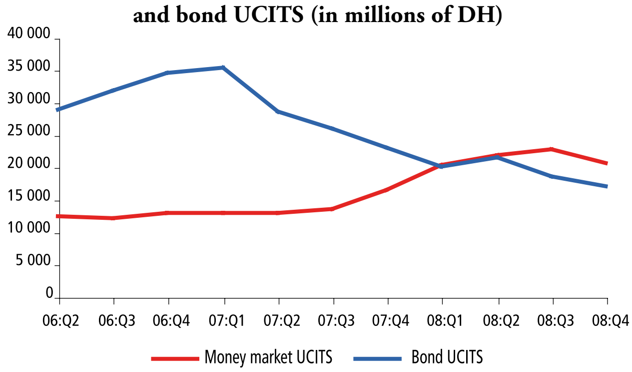



**Chart 4.15: LI4 and MASI (year-to-year in %)**

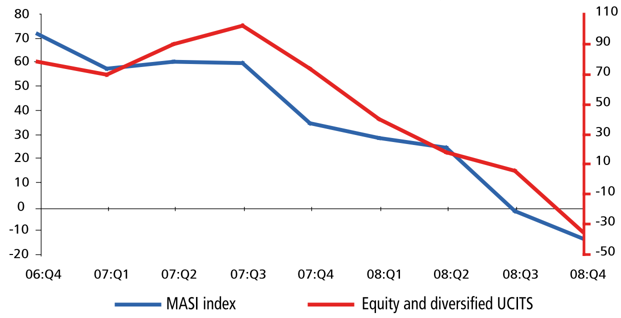
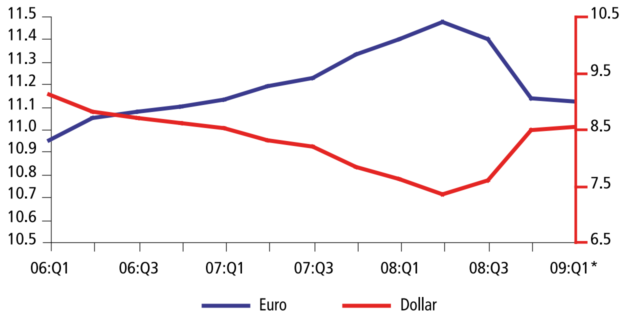
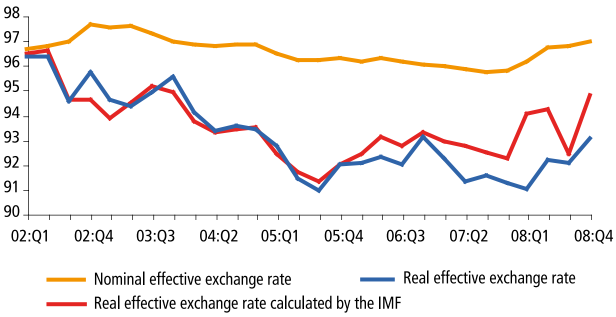



**Chart 4.16: Exchange rate of the dirham (monthly averages)**




** The first quarter of 2009 corresponds to the arithmetic average of January and February data.*

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




**Provisional data*

*Sources: IMF, and BAM calculations*

percent year on year. On March 6, 2009, the index improved somewhat, gaining 0.75 percent.

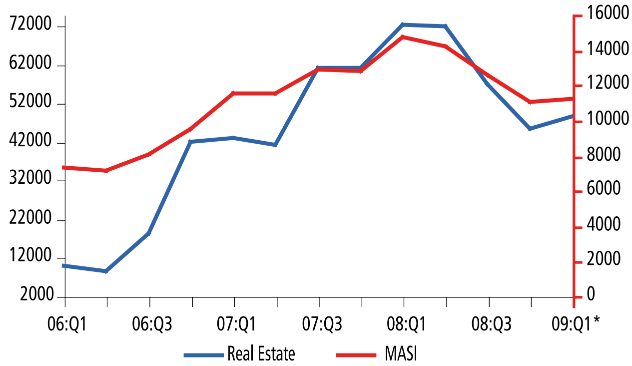
PER of the Casablanca stock market fell from 17.7 to 17.4 from one quarter to the next, but generally remains well above that of the emerging countries.

The volume of transactions more than doubled, on a quarter-to-quarter basis, reaching 91.5 billion dirhams.
Given the drop in prices, stock market capitalization declined at a quarterly rate of 9.4 percent to 531.8 billion dirhams. At the end of the first two months of 2009, stock market capitalization rose 2.4 percent to 544.6 billion dirhams.

At the end of the fourth quarter of 2008, most sectoral indexes fell compared with the previous quarter.

Concerning real estate assets, the fragmented information collected suggest that the sector seems to undergo some slowdown in activity and prices, from one quarter to the next.

**Chart 4.18: Stock market indexes ***




** The first quarter of 2009 ends on March 6, 2009*

**Chart 4.19: Quarterly change in sectoral indexes, Q4/Q3 2008, in %**

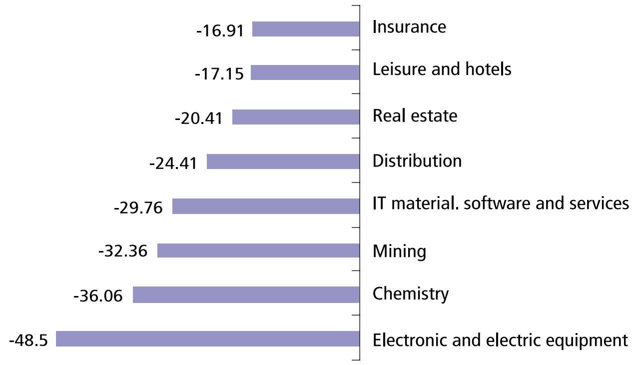



**Table 4.3: Equity markets' PER**

| PER* | 07 :Q4 | 08 :Q1 | 08 :Q2 | 08 :Q3 | 08 :Q4 |
|---|---|---|---|---|---|
| South Africa | 12.38 | 12.71 | 13.36 | 9.76 | 3.48 |
| Argentina | 19.17 | 2.58 | 2.61 | 8.94 | 5.68 |
| Egypt | 18.54 | 15.87 | 14.7 | 13.28 | 7.41 |
| Euro stoxx 50 | 12.5 | 10.5 | 11.14 | 9.45 | 9.21 |
| Hungary | 13.2 | 10.36 | 9.13 | 7.51 | 4.55 |
| **Morocco** | **22.2** | **21.2** | **20.1** | **17.7** | **17.4** |
| Taiwan | 20.26 | 18.36 | 12.91 | 9.58 | 11.46 |
| Turkey | 17.33 | 8.36 | 6.89 | 6.96 | 5.23 |

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

# 5. RECENT INFLATION TRENDS

*In line with Bank Al-Maghrib quarterly projections, data of the fourth quarter of 2008 and January 2009 show a slowdown in both headline inflation and core inflation. In fact, the decline in the international prices for food commodities drove down domestic prices. Nevertheless, as underlined in the previous MPR, the fall in global inflation slowly passes through to inflation in Morocco, due primarily to the pace of liquidation of imported goods' inventories at high prices and profit-driven behaviors of domestic importers and distributors which create downward price rigidity. Against this background, year-on-year headline inflation stood at 4 percent in January 2009, down from 4.2 percent in December. The underlying trend of prices however remains downward, as evidenced by the decline in the growth rate of core inflation from 3.3 percent in December to 2.8 percent. This drop reflects the appreciable slowdown in tradables' inflation which more than offset the rise in nontradables' inflation, particularly services. In fact, the easing of pressure on the international prices of non-energy commodities, particularly staple food, and oil significantly contributed to the fall of tradables' inflation. The downward trend of inflation is also confirmed by the change in industrial producer prices, which were the most impacted by the downward trend in the import prices of oil and non-energy commodities, declining 2.8 percent in December and 7.8 percent in January 2009.*

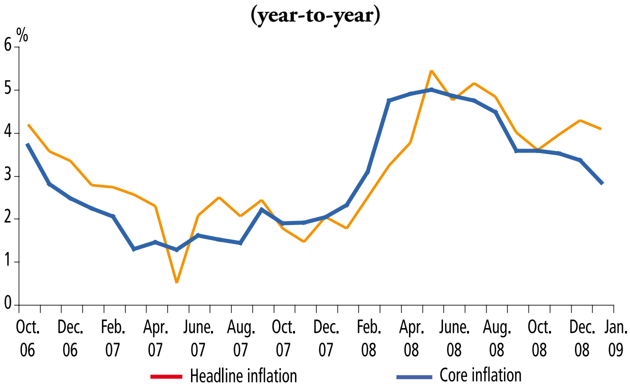
## 5.1 Inflation trends

In January 2009, headline inflation stood at 4 percent, following 3.9 percent and 4.2 percent in November and December, respectively, due mainly to the rise in fresh food prices. In contrast, core inflation, which reflects the underlying trend of prices, fell from 3.3 percent in December to 2.8 in January.

The analysis of inflation trends by major product categories shows that prices for fresh food continued to trend upward in the past three months. They moved up from 4.8 percent in November to 7.4 percent in December and 8.9 percent in January, the increases of November and January being mostly driven by a basic mechanical effect.

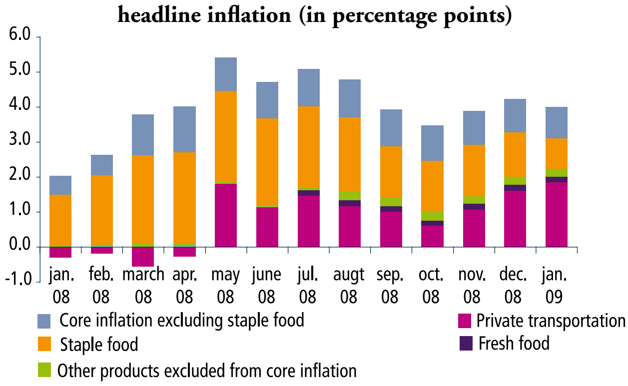
Commodity prices continued to trend downward between November and January, as a result of the decline in the international prices of food commodities largely in connection with the downturn in global demand. As a consequence, staple food prices fell from 10.2 percent in November to 9.1 percent in December and then 6.4 percent in January. The deceleration was mostly noticeable in the prices for cereals and fats, which recorded the highest increases in 2008. Between November and January, they declined from 12 percent to 7.7 percent and 12.1 percent to 4.9 percent, respectively.

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




*Sources: HCP, BAM calculations*

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




*Sources: HCP, BAM calculations*

The slowdown in the price rise of staple food cushioned the impact of the price rises of fresh food on headline inflation, and confirmed the downward trend of core inflation until January 2009. Non-food products contributed less to inflation between November and January. This reflects, on the one hand, a decline in the growth rate of the prices for clothing, communications (basic effect) and leisure durable goods, and, on the other hand, an acceleration in the growth pace of the prices for equipment goods, medical care and public transportation following the increase in freeway tolls as from January 2009.

Private transportation fares moved up from 6.2 percent in December to 6.4 percent in January 2009, as domestic fuel prices remained unchanged. However, as from February 16, 2009, the domestic prices of some types of fuel were adjusted downward. As a consequence, premium gasoline declined 1 dirham to 10.25 dirhams a liter. The price of the new 50 ppm diesel which replaced the 350 ppm diesel was lowered to 7.50 dirhams a liter, down 2.5 dirhams, whereas the price of diesel fuel remained unchanged at 7.22 dirhams a liter.

Core inflation was lower than headline inflation for the seventh month in a row, since July 2008. This gap widened in the past three months, solely because of the behavior of fresh food prices, reaching 0.4, 0.9 and 1.2 percentage point in November, December and January, respectively.

**Table 5.1 : Inflation and its components**

| | Monthly change (%) | | | year-to-year (%) | | |
|---|---|---|---|---|---|---|
| | Nov. 08 | Dec. 08 | Jan. 09 | Nov. 09 | Dec. 09 | Jan. 09 |
| **Headline inflation** | **0.2** | **0.3** | **-2.1** | **3.9** | **4.2** | **4.0** |
| - Fresh food | 0.7 | 2.1 | -2.1 | 4.8 | 7.4 | 8.9 |
| - Private transportation | 0.1 | 0.1 | 0.0 | 6.1 | 6.2 | 6.4 |
| - Other products excluded from core inflation | 0.0 | 0.0 | -0.1 | 4.6 | 4.6 | 4.6 |
| **Core inflation** | **0.0** | **0.1** | **-0.1** | **3.5** | **3.3** | **2.8** |
| Including: - Staple food | -0.3 | -0.6 | -1.7 | 10.2 | 9.1 | 6.4 |
| - Other food products | 0.4 | 0.6 | 0.3 | 4.5 | 4.5 | 4.5 |
| - Clothing | 0.2 | 0.1 | 0.0 | 1.6 | 1.5 | 1.3 |
| - Housing | 0.1 | 0.2 | 0.0 | 0.8 | 0.9 | 0.9 |
| - Equipment | 0.1 | 0.5 | 0.0 | 2.1 | 2.5 | 2.5 |
| - Medical care | 0.1 | 0.1 | 0.6 | 0.3 | 0.3 | 0.9 |
| - Public transportation and communication | 0.1 | 0.0 | 1.1 | 1.9 | 2.0 | 1.4 |
| - Leisure activities and culture | 0.0 | 0.0 | 0.0 | 1.9 | 1.8 | 1.8 |
| - Other goods and services | 0.0 | 0.3 | 0.4 | 2.6 | 2.6 | 2.8 |

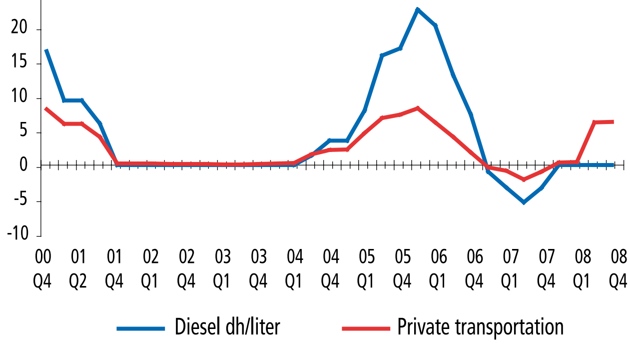
*Sources: HCP, BAM calculations*

**Table 5.2: Domestic selling prices of oil products**

| Products/DH/liter | Jan. 08 | Apr. 08 | Jul. 08 | Sept. 08 | Dec. 08 | Feb. 09 |
|---|---|---|---|---|---|---|
| **Premium gasoline** | 10.25 | 10.25 | 11.25 | 11.25 | 11.25 | 10.25 |
| **Diesel fuel** | 7.22 | 7.22 | 7.22 | 7.22 | 7.22 | 7.22 |
| **Diesel 350/50** | 9.13 | 9.13 | 10.13 | 10.13 | 10.13 | 7.50 |
| **Industrial fuel (Dh/ton** | 2874 | 2874 | 3374 | 3374 | 3374 | 3074 |

*Source: Ministry of Energy and Mining*

**Chart 5.3: Year-to-year change in diesel pump price and transportation price**




*Sources: HCP and Ministry of Energy and Mining*

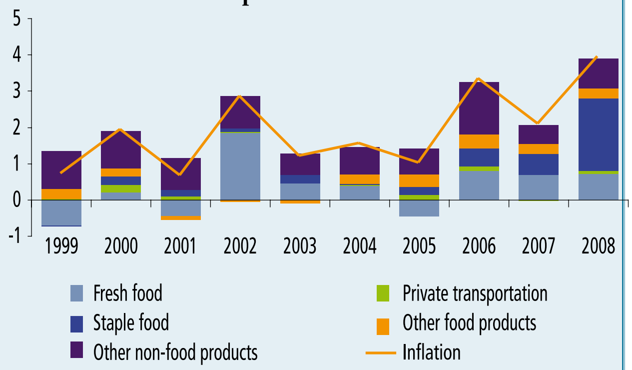
## Box 5.1: Price trends in 2008

In 2008, headline inflation stood at 3.9 percent, from 2 percent a year earlier, well above the 1.8 percent average of the past five years. This upward trend was also registered in core inflation, which edged up from 1.7 percent to 3.9 percent, from one year to the next. Price trends in 2008 mostly reflected cost factors, particularly the sharp rise in international commodity prices.

First, the prices for staple food and fresh food, which increased 14.3 percent and 3 percent, respectively, contributed 1.98 and 0.72 percentage point to headline inflation in 2008. Staple food prices were hit by the global surge in the prices for food commodities which persisted until the end of the first half of the year. However, the decline in international prices starting the second half of 2008, as a result of the slump in global demand, passed through to domestic prices only partially. This rigidity is attributable to several factors, particularly profit-driven behaviors, the pace of inventory liquidation, and the fact that import contracts are generally signed in advance and do not fully take account of future price trends on the international markets.

Likewise, the rise in oil prices, which continued until July 2008 and drove up the Brent price above $130/barrel, significantly impacted domestic fuel prices and consequently the fares of the "private transportation" item, notwithstanding the intervention of the Subsidization Fund throughout the year. Therefore, private transportation costs increased 3.3 percent, from 1.1 percent the year before. This situation heavily impacted the subsidy budget and led the Government to pass a part of this increase on to the domestic prices of certain types of fuel, particularly premium gasoline, starting July 2008. In contrast, the collapse in prices that began in August 2008, because of the sharp contraction in global demand, did not pass through into domestic prices during the second half year.

**Chart B 5.1: Contribution of main components to inflation in 2008**




*Sources: HCP, and BAM calculations*

Against this backdrop, the 5.8 percent rise in tradables prices in 2008 did pass on to the prices of nontradables (2.1 percent in 2008 compared with 0 percent in 2007), services in particular. This spread effect occurred via the increase in inputs and the wage adjustments of July 2008. In response to these second-round effects, Bank Al-Maghrib raised its key rate in September to anchor the expectations of economic agents and prevent the impact of a probable price-wage spiral on inflation.

## 5.2 Goods and services

The breakdown of inflation by prices of goods and services shows continued downtrend in prices for processed goods, on a year-to-year basis, which decreased from 3.6 percent in November to 2.8 percent in January. This change mainly results from the deceleration in the prices of some staple food, particularly fats, and most components of the clothing item.

However, the prices of "unprocessed goods and others" marched upward in the past three months, from 6.8 percent in November to 8.5 percent in January, mostly driven by the substantial rise in fresh food prices. The prices of processed and unprocessed goods jointly contributed to headline inflation 3.2 percentage points in November, 3.5 percentage points in December and 3.3 percentage points in January.

The prices of services, excluding private transportation, grew 1.7 percent in January, up from 1.6 percent in December and 1.5 percent in November. This trend in part reflects the lagged spread effect of SMIG adjustment last July, as show the results of BAM's models[1]. Among the services whose prices increased rapidly were medical consultations and hospitalization, public transportation, healthcare and articles of personal use, and the "restaurants, cafés and hotels" item. Prices of services, including private transportation, contributed 0.7 percentage point to headline inflation, a pattern similar to the previous three months.

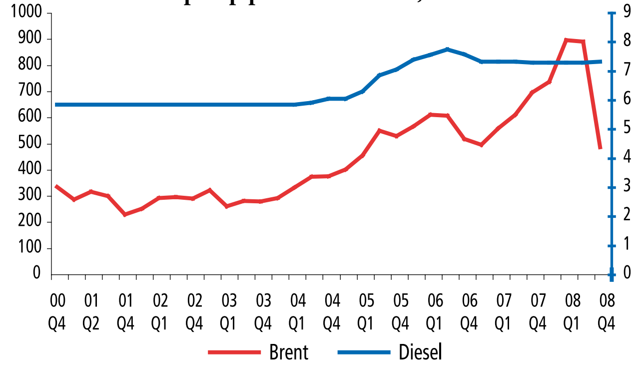
## 5.3 Tradable and nontradable goods

The breakdown of the cost of living index by type of product shows a slowdown in the inflation of tradables compared with a slight increase in that of nontradables.

After an acceleration from 5.7 percent to 7.2 percent between November and December 2008, inflation of tradable goods fell back again in January 2009, to 6.9 percent. Prices of these products, which contributed 2.8 percentage points to headline inflation, remain contingent on the trend of food

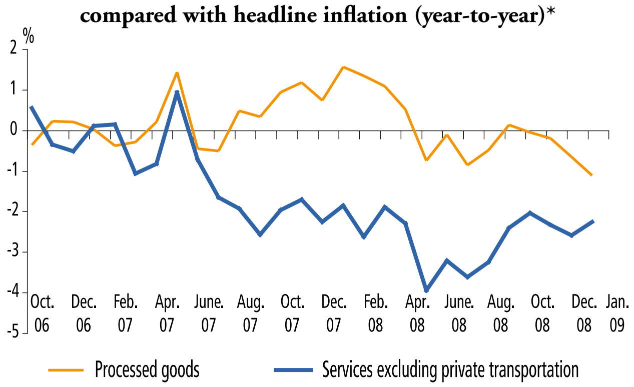
[1] See Box 2.1, page 22, MPR of June 2008.

**Chart 5.4: World oil price and pump price in Morocco, in DH**



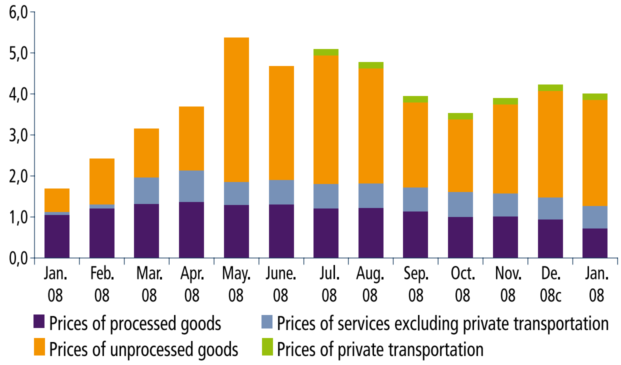

*Sources: IMF, Ministry of Energy and Mining*

**Chart 5.5: Relative prices of processed goods and services excluding private transportation compared with headline inflation (year-to-year)***




*(*) Gap between the inflation rate of processed goods and services excluding private transportation and headline inflation rate.*
*Sources: HCP, and BAM calculations*

**Chart 5.6: Contribution of goods and services prices to headline inflation (year-to-year)**




*Sources: HCP, and BAM calculations*

**Table 5.3: Price indexes for goods and services**

| | Monthly change (%) | | | Year-to-year change (%) | | |
|---|---|---|---|---|---|---|
| | Nov. | Dec. | Jan. | Nov. | Dec. | Jan. |
| Processed goods | 0.0 | 0.0 | -0.2 | 3.6 | 3.5 | 2.8 |
| Unprocessed goods and others | -0.5 | 1.3 | -2.0 | 6.8 | 8.2 | 8.5 |
| Services excluding private transportation | 0.1 | 0.1 | 0.4 | 1.5 | 1.6 | 1.7 |
| Private transportation | 0.1 | 0.1 | 0.1 | 6.1 | 6.2 | 6.4 |

*Sources: HCP. and BAM calculations*

import prices, which in turn were very impacted by the volatility of international commodity prices (see Chapter 3).

The slipping into recession of the major global economies, following the financial crisis, led to a severe downturn in demand and an almost general decline in global food prices. The slowdown in tradables inflation is mostly attributable to the fall in the growth pace of the prices for cereals, fats, fish, and fresh fruit. However, domestic milk prices recorded a lagged increase, in response to the past rise in food and energy commodity prices, particularly during the first half year 2008.

The price index of nontradable goods grew 2.4 percent, from 2.3 percent in December, thereby contributing 1.3 percentage point to headline inflation. The slight acceleration in nontradables inflation mostly reflects the increasing growth pace in the prices of "public transportation", "restaurants, cafés and hotels", and "healthcare and articles of personal use".

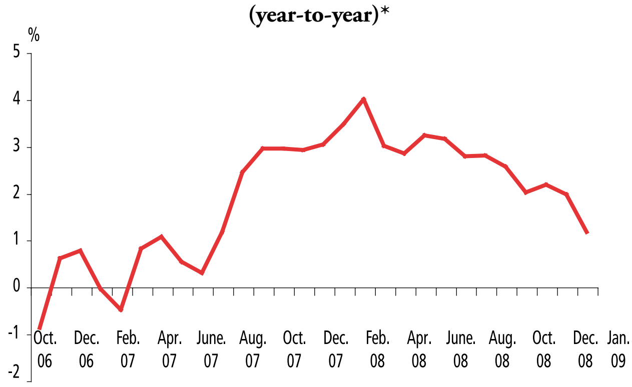
## 5.4 Industrial producer price index

The trend of industrial producer prices in January 2009 shows a collapse in production costs in the main industrial sectors, and therefore an easing of pressures on domestic prices. Indeed, industrial producer price index registered a substantial fall of 7.8 percent, after that of 2.8 percent in December 2008.

Contrary to inflation, the decline in the international prices of non-energy commodities and oil passed through into industrial producer prices at a more rapid pace. This fall is largely the result of the 48 percent drop in the industrial costs of the coking and refining subsector, after the 39.1 percent increase of last December. The negative contribution of coking and refining prices to the change in the benchmark index stood at 14.1 percentage points.

Excluding refining and coking, the pace of growth in the industrial producer price index slowed down from 12.8 percent to 8.9 percent, largely because of the decline in the growth rate of

**Chart 5.7: Gap in inflation rates between processed goods and services excluding private transportation (year-to-year)***




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

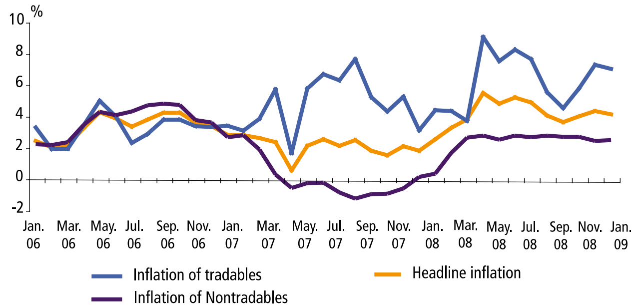
*Sources: HCP, and BAM calculations*

**Tableau 5.4 : Change in the price indexes of tradables and nontradables**

| | Monthly change (%) | | | Year-to-year change (%) | | |
|---|---|---|---|---|---|---|
| | Nov. 08 | Dec. 08 | .Jan 09 | Nov 08 | Dec. 08 | .Jan 09 |
| Tradables | -0.4 | 0.9 | -1.7 | 5.7 | 7.2 | 6.9 |
| Nontradables | 0.1 | 0.1 | 0.3 | 2.6 | 2.3 | 2.4 |

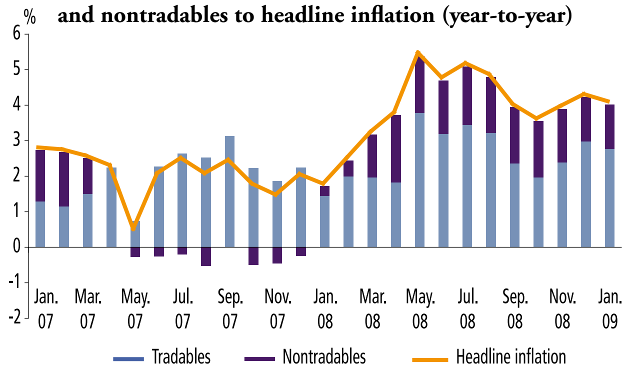
*Sources: HCP, and BAM calculations*

**Chart 5.8 : Price indexes of tradables and nontradables (year-to-year)**




*Sources: HCP, and BAM calculations*

**Chart 5.9: Contribution of tradables and nontradables to headline inflation (year-to-year)**



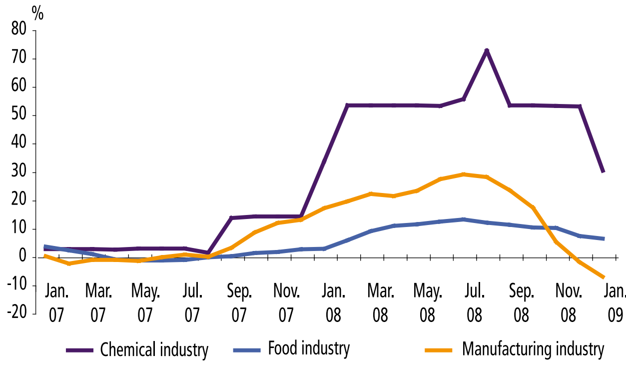

*Sources: HCP, and BAM calculations*

the prices of "food industry", from 6.4 percent to 5.5 percent, and "chemical industry", from 52 percent to 29.5 percent. Prices in the food and chemical industries jointly contributed 5.74 percentage points to the increase in the manufacturing producer price index. These changes occurred in an international economic environment marked by the decline in global demand for some agricultural and energy commodities, as well as by the downward revision of growth and employment forecasts in the developed and emerging countries.

Producer prices in the "metal working" industry grew 4.8 percent, down from 8.8 percent the month before, whereas the rise in those of metallurgical industry remained almost unchanged at 1 percent, despite the sizable fall in the international prices of the main metals.

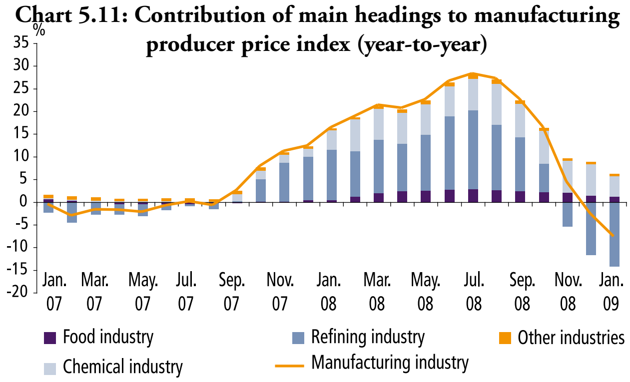
According to the findings of BAM business survey for January, corporate managers noticed the continuation of the downtrend in the prices of finished goods, which began in August. They expected this trend to persist in the next three months, except in chemical and parachemical industries.

**Chart 5.10 : Industrial producer price indexes**



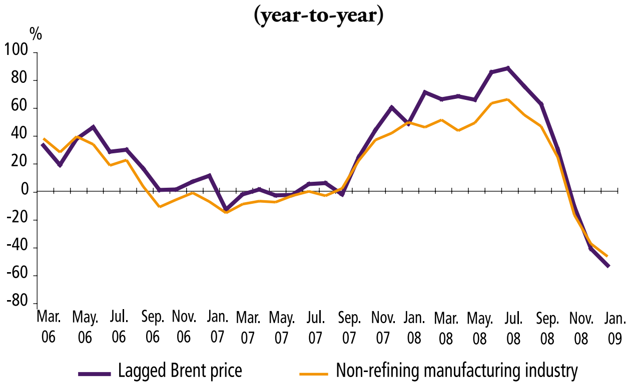

*Sources: HCP, and BAM calculations*

**Chart 5.11: Contribution of main headings to manufacturing producer price index (year-to-year)**



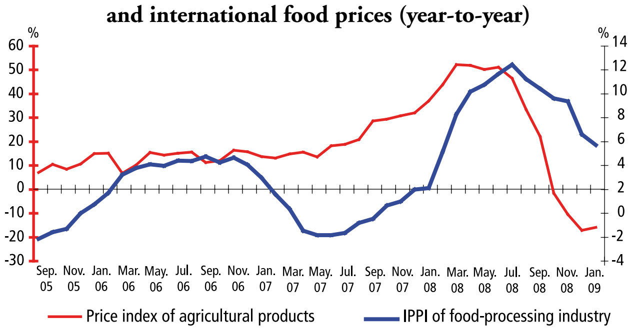

*Sources: HCP, and BAM calculations*

**Chart 5.12: Refining industry index and Brent prices (year-to-year)**




*Sources: IMF, HCP, and BAM calculations*

**Chart 5.13: Domestic and international food prices (year-to-year)**




*Sources: IMF, HCP, and BAM calculations*

# 6. INFLATION OUTLOOK

*Reflecting the deterioration of the international economic situation, the indicator of foreign demand for Moroccan exports shows an easing of pressure on inflation. In addition to this trend, there was a substantial decline in the prices of staple food and oil, and a slowdown in world inflation. The central forecast of headline inflation for the six coming quarters was substantially revised downward compared with the MPR of December 2008. It is worth mentioning that the rate of headline inflation in the fourth quarter of 2008, at 3.9 percent, was in line with the central forecast presented in the previous MPR. Risks surrounding the central forecast for the coming quarters were adjusted downward. However, beyond the year 2009, the volatility of commodity prices constitutes a source of uncertainty. Internally, risk factors are on the downtrend too, mainly because of the fall in demand-driven pressure. These might fall further against the background of a worse-than-expected deterioration of economic activity. The transmission of the fall in international prices to domestic prices has started, as indicated by the trend and outlook of import prices, industrial producer prices, and tradables prices. In addition, analysis of aggregate supply and demand conditions suggests an easing of pressure on the labor market. Nonetheless, the 5 percent increase in the SMIG, scheduled in July 2009, represents a factor of uncertainty as to this trend. On this basis, inflation trends over the coming six quarters would generally remain consistent with the price stability objective, with an average forecast of about 2.6 percent. At the end of the forecast horizon (the second quarter of 2010), headline inflation is projected to remain below 3 percent. For the year 2009, we expect a headline inflation rate of approximately 2.6 percent. The quarterly profile of inflation during the current year indicates a continued decline.*

## 6.1 Baseline scenario assumptions

### 6.1.1 International environment

According to the latest projections of IMF's World Economic Outlook Update of January 2009, economic activity would decelerate appreciably this year. Indeed, global growth in 2009 would not exceed 0.5 percent, down from the 2.2 percent projected in the November 2008 WEO Update. This downward revision is explained by the rapid deterioration of activity across the advanced and emerging economies.

These projections expect the GDP of the United States to contract by 1.6 percent in 2009, up from the 0.7 percent predicted last November. Similarly, GDP in the euro area would fall 2 percent, compared with the 0.5 percent increase projected in November. Growth in emerging and developing economies is expected to stand at nearly 3.3 percent in 2009, in contrast with the 5.1 percent of the November 2008 WEO Update. Against this backdrop, world inflation in February 2009 continued the downward trend that began in August 2008. According to Eurostat data, annual inflation in the euro area was 1.2 percent in February 2009, down from 1.1 percent in January. The fall in inflationary pressures is linked to the weaker growth outlook in the euro area and the continued substantial decline in the prices of energy, particularly oil. According to the February forecasts of the Federal Reserve and the European Central Bank, this general downtrend in inflation would continue in 2009 and 2010. Inflation in the euro area would fall in a range of 0.1 to 0.7 percent in 2009 and 0.6 to 1.4 percent in 2010, whereas in the United States it would range between -0.5 and 1.5 percent in 2009, and 0.7 and 1.8 percent in 2010.

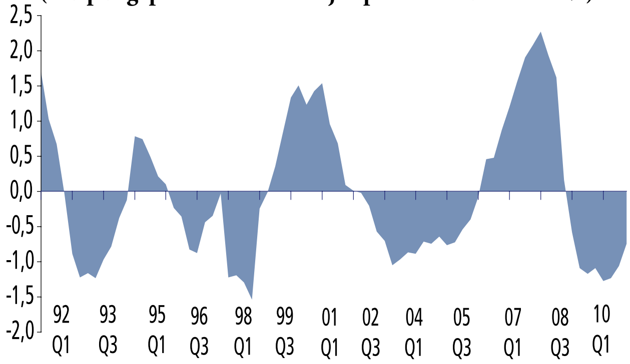
At the same time, oil prices recorded a sharp decline in January 2009 compared with the same period of last year, at $43.9/barrel. For the remainder of the forecast horizon, we expect the price of barrel to be lower than $50 in 2009. Actually, the futures market shows that Brent price would near $46 in 2009 and $52 in 2010. International prices of major commodities would continue to trend downward in the following quarters, with a marked volatility. In this connection, the World Bank projects a fall in global price index of food commodities by nearly 25 percent in 2009 and 0.3 percent in 2010. Import price indexes of energy and non-energy commodities will continue to decrease over the forecast horizon, with a more noticeable contraction in 2009 than in 2010.

Against this extremely uncertain environment where risks weigh on growth rather than on inflation, the major developing countries and some emerging countries implemented expansionary fiscal and monetary policies. Several central banks again eased their monetary policy, the latest measures in this direction being those taken by the Bank of England and the ECB, which cut their policy rates by 50 basis points to 1 percent and 1.5 percent, respectively.

Based on these elements, the assumptions held for the inflation forecasts are consistent with the projection of a sharp decline in global demand. This contraction may extend beyond 2009, with a probable slight recovery as from the second half of 2010, as shows chart 6.1 which presents the assumptions relating to the forecasts of the weighted output gap[1] of Morocco's key trading partner countries. This indicator, which helps to assess the pressures driven by foreign demand on economic activity and inflation in Morocco, would remain negative in 2009 (-1 percent) and 2010 (-1.1 percent) notwithstanding the projected slight recovery as from the fourth quarter of 2010. These assumptions are based on the European Commission's forecasts of growth in Morocco's main partner countries, namely France (-1.8 percent in 2009 and 0.4 percent in 2010), Spain (-2 percent in 2009 and -0.2 percent in 2010), the United Kingdom (-2.8 percent in 2009 and 0.2 percent in 2010), Germany (-2.3 percent in 2009 and 0.7 percent in 2010), and Italy (-2 percent in 2009 and 0.3 percent en 2010).

1 The weighted output gap of the major trading partner countries is assessed by a Hodrick-Prescott filter applied to the weighted average of the GDP of Morocco's first five partner countries ranked according to their share in Morocco's total exports. The share of each country at a specific quarter of the year (Q) is a moving average of its share in the total exports during the last couple of years (Q1 and Q2). This method helps to avoid the possible fluctuations in the series that might arise from changes in the shares from one quarter to the next. The five countries selected contribute 65 percent to Moroccan exports, and are France, Spain, Germany, United Kingdom and Italy.

**Chart 6.1: Indicator of foreign demand for Moroccan exports (Output gap of Morocco's major partner countries in %)**




*Sources: European Commission, and BAM calculations and forecasts*

### 6.1.2 National environment

The expected sharp slowdown in the economic growth of the euro area will impact the Moroccan economy in 2009, through the real transmission channels, namely: exports, foreign direct investments, tourism, and transfers of Moroccans living abroad. This is evidenced by recent trends in sectors and in the balance of payment which suggest that the crisis has started to spread more markedly.

Nonetheless, agricultural activity holds up well, reflecting the prevalence of very good weather conditions until March 2009.

Moreover, the effects of the global economic crisis on the national economy did not impact fiscal sustainability in 2008. This leaves room of maneuver to adopt a contra-cyclical fiscal policy for the year 2009, together with the continued strengthening of medium-run fiscal sustainability, given that the budget assumed an oil price of $100/barrel, a level well above its possible trend.

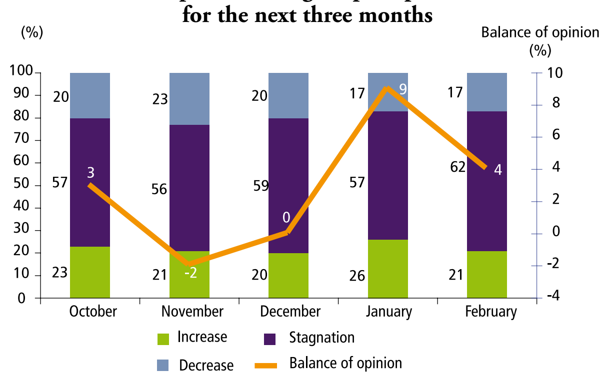
In addition, monetary conditions suggest that pressure on prices would subside throughout the year 2009. Indeed, money supply (M3) is expected to slow down from 12.5 percent in 2008 to 10.5 percent in 2009 and 10.2 percent in 2010.

The baseline scenario adopted for this forecast exercise is based on a GDP growth rate of nearly 5 percent. Therefore, the output gap of the overall GDP is expected to be lower than in 2008, but would remain positive. Agricultural GDP is projected to increase 9.8 percent in 2009, under the assumption of a cereal production of 68 million quintals. Against this backdrop, the agricultural output gap would remain positive over the six quarters of the forecast horizon. Nonagricultural sectors would continue to grow at a pace below the trend of the past years, mainly because of the deterioration of the international environment that is expected to negatively impact nonagricultural output gap in the next quarters. The latter is projected to be negative in 2009, but would improve in 2010. Against this background, demand pressures on inflation arising from the goods and services market as well as from the labor market would be of little impact in the coming quarters.

Concerning internal cost factors, the baseline scenario incorporates the 5 percent rise in the SMIG which would come into effect in July 2009. Diesel price at the pump is expected to remain unchanged at 7.22 dh/liter over the forecast horizon, insofar as global prices do not increase and the new 50 ppm diesel, which would replace the 350 ppm diesel, constitutes a perfect substitute.

According to the findings of BAM monthly business survey of February, the proportion of corporate managers anticipating the stagnation of inflation in the coming three months increased from that of January[1]. In contrast, the percentage of those predicting an increase in inflation was down.

**Chart 6.2: Corporate managers' perception of inflation for the next three months**




*Source: BAM monthly business survey*

1 This question of the survey seeks to collect corporate managers' opinion on inflation trends in the following three months. Answers are not weighted, as they express the manager's perception independently of his/her activity

## 6.2 Inflation outlook and balance of risks

Assuming the non-occurrence of the main risks, the central forecast for the next six quarters remains consistent with the objective of price stability. Inflation forecast for the year 2009 shows a headline inflation rate of approximately 2.6 percent. Over the forecast horizon, headline inflation would average 2.6 percent. Compared with the projection presented in the last MPR, inflation forecast for 2009 was revised downward from 2.9 percent to 2.6 percent, against a backdrop of rapid and substantial fall in global economic activity, coupled with the depreciation of commodity prices and the decline of inflation in Morocco's key partners.

**Table 6.1: Inflation forecast for 2009 Q1 - 2010 Q2**

*Year-to-year*

| | 2009 | | | | 2010 | | Average | | |
|---|---|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | 2008 | 2009 | FH* |
| Central forecast (%) | 3.4 | 2.2 | 2.5 | 2.3 | 2.5 | 2.6 | 3.9 | 2.6 | 2.6 |

** (FH) Forecast horizon*
*Sources: HCP, and BAM forecasts*

For the last three quarters of the current year, we project a headline inflation rate of about 2.5 percent, markedly lower than the first quarter. Then, the average headline inflation rate would stabilize at around this pace over the two remaining quarters of the forecast horizon.

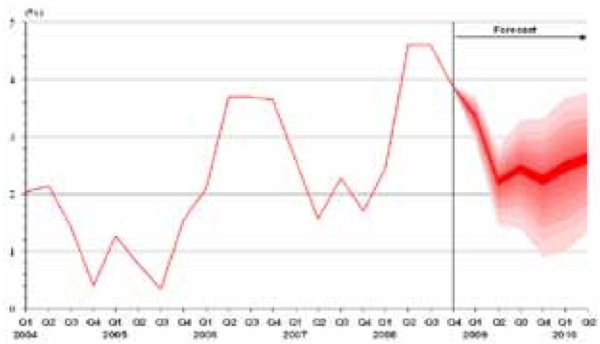
Compared with the predictions published in the MPR of December 2008, inflation projections for all quarters of the forecast horizon were adjusted downward: from 3.5 to 3.4 percent for the first quarter of 2009, from 2.8 to 2.2 percent for Q2, from 2.7 to 2.5 percent for Q3, from 2.6 to 2.3 percent for Q3, and from 2.7 to 2.5 percent for the first quarter of 2010.

These forecasts are surrounded by several sources of uncertainty stemming from both the assumptions held and the models used, which may bias the projection. Analysis of this balance of risks shows an asymmetric forecast range represented in the form of a fan chart. This is a probabilistic evaluation of uncertainty zones surrounding the central forecast.

The fan chart of this forecast exercise indicates that risks to inflation are tilted to the downside, due primarily to the sharp contraction in foreign demand. Risks surrounding the inflation central forecast for the coming quarters were adjusted downward. However, beyond the year 2009, the volatility of commodity prices constitutes a source of uncertainty. Internally, risk factors are also skewed to the downside, mainly because of the fall in demand pressures. These might decline further against the background of a worse-than-expected deterioration of economic activity. The transmission of the fall in international prices to domestic prices has started, as indicated by the trend and outlook of import prices, industrial producer prices, and tradables prices. In addition, analysis of aggregate supply and demand conditions suggests an easing of pressure on the labor market. Nonetheless, the 5 percent increase in the SMIG, scheduled in July 2009, represents a factor of uncertainty as to this trend. The materialization of one of these risks could lead to an inflation rate above the central forecast, at a value included within the forecast range represented on the fan chart (with a probability of 90 percent).

**Chart 6.3 : Inflation forecast fan chart, 2009 Q1 - 2010 Q2 (Quarterly data)**

*Year-to-year*




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

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