BANK AL-MAGHRIB

MONETARY POLICY REPORT

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TABLE OF CONTENTS

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FOREWORD

Pursuant to the provisions of Article 6 of Royal Decree No. 1-05-38 of 20 Shawwal 1426 A.H. (November 23, 2005) promulgating Law No. 76-03 on the Statutes of Bank Al-Maghrib, "with a view to ensuring price stability, the Bank adopts and implements monetary policy instruments".

In accordance with these provisions, Bank Al-Maghrib's objective in conducting monetary policy is to ensure price stability in order to preserve the purchasing power of citizens and provide the right conditions for investment and growth.

To achieve these objectives, Bank Al-Maghrib has put in place an analysis and forecasting system which rests on an integrated approach based on a monetary policy model and several satellite models that feed and complement it. Adapted to the current monetary policy framework and exchange rate regime and also to the transition to inflation targeting and gradual flexibility of the exchange rate regime, this new system makes it possible to predict the future course of macroeconomic aggregates, including inflation, and monetary conditions and to assess the impact of the materialization of risks to the central projection.

The assessments of the national economic situation and its medium-term prospects are outlined in the Monetary Policy Report (MPR), prepared by the Bank staff for the Board members. The MPR is published quarterly on the day of the Board meeting once the Board approves it.

In addition to the press release that explains the basis for the monetary policy decision and the overview that summarizes all the economic, monetary and financial developments and macroeconomic projections, the MPR has two parts. The first part, consisting of six chapters, analyzes the change in the main determinants of inflation, namely the international environment, external accounts, demand, supply and the labor market, fiscal policy, monetary conditions and asset prices, and recent trends in inflation. The second part is devoted to the presentation of medium-term prospects for the national economy.

Bank Al-Maghrib Board members:

The Governor, Chairman

The Director General

The Government Representative

The Director of Treasury and External Finance, Representative of the Ministry in charge of Finance

Mr. Abdellatif BELMADANI

Mr. Mohammed BENAMOUR

Mrs. Miriem BENSALAH CHAQROUN

Mr. Bassim JAI-HOKIMI

Mr. Mustapha MOUSSAOUI

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PRESS RELEASE

BANK AL-MAGHRIB BOARD MEETING

Rabat, September 25, 2018

1. The Board of Bank Al-Maghrib held its third quarterly meeting of the year on Tuesday, September 25.

2. At this meeting, it analysed recent economic developments as well as the macroeconomic forecasts prepared by the Bank for the next eight quarters.

3. Based on these assessments, particularly those of medium-term inflation and growth prospects, the Board considered that the current level of the key rate at 2.25 percent remains appropriate and decided to keep it unchanged.

4. The Board noted that, after its low levels of 2017, inflation rose significantly in the first half of 2018, mainly driven by the increase in volatile food prices and regulated prices. It is expected to decelerate in the second half of the year to average 2.1 percent by year-end. In 2019, as these shocks dissipate, inflation would drop to 1.2 percent. As to core inflation, which measures the fundamental price trend, it is expected to stay moderate at around 1 percent in 2018 and 1.2 percent in 2019.

5. Internationally, the global economy remained robust despite the downward trend risks weighing on its prospects, mainly due to the intensification of trade tensions, the strong pressure on the currencies of some emerging countries and the Brexit terms. In the United States, growth would stand at 2.8 percent in 2018, benefitting from the fiscal measures undertaken, before slowing down to 2 percent in 2019. In addition, labor market is expected to continue its momentum with unemployment rates below their natural level. In the euro area, activity is expected to be relatively moderate, with growth falling to 2.1 percent in 2018 and 1.7 percent in 2019. However, labor conditions would continue to improve, and the unemployment rate is expected to decrease to 8.4 percent in 2018 and 2019, its lowest level since the beginning of the crisis. In the main emerging countries, the Chinese economy is expected to remain resilient to trade tensions, while decelerating slightly on account of the rebalancing policy implemented by the authorities. In India, growth is projected to accelerate, as the impact of the demonetisation and the introduction of the new tax on goods and services start to dissipate. In turn, Russia would continue to benefit from the high level of world oil prices, while the Brazilian economy is expected to improve less significantly than expected, particularly due to the transports strikes.

6. On the commodity market, oil prices are expected to trend downward in 2019. After an average of $54.4/bl in 2017, the Brent price would average $69.8/bl in 2018 before dropping to $63.8/bl in

2019. With regard to phosphates and derivatives, prices were overall on an upward trend over the first months of 2018. For the year as a whole, World Bank April projections indicate that the DAP, the TSP, and crude phosphate would increase to $390/mt, 315 dollars/mt and $95/mt, respectively. In 2019, prices are expected to record new, albeit slight, increases.

7. Under these conditions, inflation would continue to hover below the ECB's target in the euro area, reaching 1.7 percent in 2018 and 1.4 percent in 2019. In the United States, it would stand at a level close to the FED target of 2 percent.

8. As regards monetary policy decisions, the ECB decided, during its meeting held on September 13, to keep its rates unchanged, while indicating that it still expects them to remain at their present levels at least through the summer of 2019, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to levels that are below, but close to, 2 percent. It also reiterated that it will reduce, after September, the amount of its net asset purchases to 15 billion euros and expects to end these purchases by the end of the year. On the other hand, the FED decided on August 1 to keep the target range of the federal funds rate unchanged at 1.75 percent to 2 percent and reiterated that its policy stance remains accommodative, thus supporting favourable conditions in the labor market and a sustained return to 2 percent inflation.

9. Nationally, the recent national accounts data for the first quarter of 2018 indicate a year-on-year slowdown of GDP from 3.5 percent to 3.2 percent, covering a slower rise in agricultural value added at 2.5 percent, down from 14.8 percent, and higher increase in nonagricultural activities to 3.4 percent, up from 2 percent. These trends would continue over the medium term, as domestic growth is expected to fall from 4.1 percent in 2017 to 3.5 percent in 2018 and to 3.1 percent in 2019, according to Bank Al-Maghrib's projections. Agricultural value added would increase by 5.1 percent this year then, assuming a normal crop year, would decline by 1.6 percent in 2019. Conversely, nonagricultural activities would continue to recover, with a 3.3 percent growth in 2018 and 3.7 percent in 2019.

10. Labor market conditions improved relatively in the second quarter compared to the same quarter of 2017. The economy generated 117 thousand jobs, including 53 thousands in services. Taking into account a net entry of 97 thousand jobseekers, the participation rate continued its decline, and fell from 47.3 percent to 47 percent. The unemployment rate decreased from 9.3 percent to 9.1 percent at the national level. However, this improvement did not benefit urban youth, aged 15 to 24, among which the unemployment rate edged up to 40.5 percent.

11. With regard to external accounts, preliminary data for the first eight months of the year indicate that exports continued to gain momentum, driven by higher sales in the automotive sector and phosphates and derivatives. Their growth would reach, following BAM forecasts, 8.2 percent at the end of the year and would decelerate to 6.8 percent in 2019. At the same time, due mainly to an increase in capital goods purchases and in the energy bill, imports would reach 7.3 percent for the whole of the year, before slowing down to 3.4 percent in 2019. In turn, after a marked increase

in 2017, travel receipts and remittances of Moroccan expatriates would almost stabilize in 2018 and increase by nearly 4 percent in 2019. Taking into account inflows of grants from GCC partners expected at 4.8 billion dirhams this year and 2.1 billion the following year, current account deficit is expected to widen to 4 percent of GDP in 2018 and to decrease to 3.7 percent in 2019. Net international reserves are expected to almost stabilize at around 240.8 billion dirhams by end-2018 and to reach 252.3 billion by end-2019. Their coverage in months of goods and services' imports would thus reach 5 months and 10 days and then 5 months and 18 days respectively.

12. On the monetary side, the dirham appreciated by 1.9 percent against the euro over the first 8 months of the year and dropped by 0.9 percent against the US dollar. Under these conditions, the effective exchange rate rose during the second quarter by 1.4 percent in nominal terms and 0.9 percent in real terms. As to lending rates, they recorded a quarterly decline of seven basis points, as a result of the decrease in rates applied to businesses, with in particular a drop by 31 points for loans to very small, small and medium-sized enterprises. Conversely, loans to individuals rose by 31 points. Regarding bank lending to the nonfinancial sector, its growth remained almost stable from one month to the next at 3.5 percent in July. It is expected to increase by 4 percent at the end of the year and to slightly accelerate to 4.5 percent in 2019.

13. Regarding public finance, data as at end-August show a fiscal deficit of 27.8 billion dirhams, up 1.9 billion compared to the same period in 2017. Overall expenditure increased by 2.2 percent, reflecting mainly higher spending on goods and services and transfers to local authorities. At the same time, current revenues growth was limited to 0.4 percent, due to the improvement of tax revenues and a decline in non-tax revenues. Under these conditions, BAM revised its forecasts for the fiscal deficit upward to 3.7 percent of GDP in 2018. In 2019, this deficit would fall to 3.3 percent of GDP, assuming the continuation of efforts to keep spending under control and to mobilize resources.

OVERVIEW

In a context marked by the uncertainties caused particularly by the heightened trade tensions and strong pressure on the currencies of some emerging countries, the advanced economies remained robust in the second quarter of 2018. Growth posted a quarter-on-quarter acceleration in the United States from 2.6 percent to 2.9 percent, boosted by household consumption and exports. In the euro area, despite some moderation, the economy remains buoyant, driven by improved employment and positive financing conditions, with a growth rate of 2.1 percent as against 2.4 percent. In addition, GDP grew 1.3 percent in the United Kingdom from 1.2 percent and slowed down in Japan from1.3 percent to 1.1 percent.

In the key emerging countries, growth decelerated from 6.8 percent to 6.7 percent in China and from 1.2 percent to 1 percent in Brazil, while it accelerated from 1.3 percent to 1.9 percent in Russia and from 7.6 percent to 8 percent in India, thanks to improved household consumption and investment.

In the labor market, conditions remained favorable in advanced countries. The unemployment rate stabilized at 3.9 percent in the United States in August, as 201 thousand jobs were created. In the euro area, this rate remained at 8.2 percent in July, its lowest level since December 2008.

In stock markets, the indexes showed divergent trends between July and August, with mainly respective increases of 2.6 percent and 0.5 percent in the Dow Jones and NIKKEI 225 and decreases of 0.6 percent in the EUROSTOXX50 and 0.4 percent in the FTSE 100. In emerging economies, the MSCI EM declined particularly by 19 percent for the index of Turkey, whose currency is under strong downward pressure, and 4.8 percent for that of China.

In sovereign debt markets, the advanced economies' 10-year yields, impacted by rising risks, were overall edging upward between July and August, from 0.61 percent to 0.64 percent in France, from 1.3 percent to 1.4 percent in Spain, from 0.5 percent to 0.6 percent in Ireland, from 4.4 percent to 4.6 percent in Greece and from 2.7 percent to 3 percent in Italy. The US Treasury bonds with the same maturity stagnated at nearly 2.8 percent.

In the foreign exchange markets, the euro depreciated between July and August by 1.2 percent against the dollar and 1.6 percent versus the Japanese yen, due to the political crisis in Italy and the heightened trade tensions, while it appreciated by 1.1 percent against the pound sterling. The currencies of the main emerging countries posted significant depreciations against the dollar with particularly a 19 percent fall of the Turkish lira. The annual bank lending growth stabilized in July at 3.9 percent in the United States and 3 percent in the euro area.

In commodity markets, international prices recorded a general decline. Oil price averaged $73.1 per barrel in August, down 1.8 percent from July. This change could be caused by an increase in the United States' stocks and fears caused by the impact of trade tensions on global growth. Non-energy prices were down 0.6 percent, year on year, reflecting declines of 4.2 percent in metal and mining prices and 0.2 percent in agricultural commodities. Prices for phosphates and derivatives rose from one month to another by 0.7 percent for crude phosphate, 2.1 percent for DAP, 4.1 percent for TSP and 3 percent for urea. On the other hand, the potassium chloride price remained stable for a year now.

Under these conditions, inflation decelerated in August from 2.1 percent to 2 percent in the euro area, and fell from 2.9 percent to 2.7 percent in the United States.

Regarding monetary policy decisions, the ECB decided on September 13 to keep its rates unchanged, while indicating that it continues to expect that these rates will remain at their present levels at least through the summer of 2019 and, in any case, for as long as necessary to ensure the continued sustained convergence of inflation to levels that are below, but close to, 2 percent over the medium term. The ECB also confirmed that it will reduce the monthly pace of the net asset purchases from €30 billion to €15 billion after September 2018 and plans to end these purchases at the end of December 2018. Similarly, the FED maintained in August the target range for the federal funds rate unchanged at 1.75 percent to 2 percent and reiterated that its policy remains accommodative, thereby supporting favorable labor market conditions and a sustained return to 2 percent inflation.

Nationally, the provisional external accounts data for end-August 2018 point out that the momentum of exports would continue, with an improvement of 17.7 percent in the automotive sector sales and 17.6 percent in exports of phosphates and derivatives. Imports rose 10.2 percent, driven mainly by increases of 12.5 percent in purchases of capital goods and 18.8 percent in the energy bill. For the other main components of the current account, the growth of travel receipts and remittances from Moroccan expatriates decelerated sharply since the beginning of the year to 1.2 percent and 1 percent, respectively. As for the main financial transactions, net FDI flows dropped by 18.6 percent, owing to a 7.3 percent drop in revenues and a 28.5 percent increase in disposals. Foreign exchange reserves amounted to 225.8 billion dirhams at end-August, equaling 5 months of imports of goods and services.

Under these conditions, the bank liquidity deficit worsened to 76.3 billion in August. Bank Al-Maghrib thus increased the volume of its injections, bringing it to 77.9 billion, thus helping maintain the weighted average rate on the interbank market close to the key rate. Monetary conditions were also marked in the second quarter by an appreciation of the real effective exchange rate and a decrease in lending rates. In this context, lending to the nonfinancial sector rose 3.5 percent in July, a virtually stable rate compared to June. Also, considering the slowdown in claims on the central government, the M3 aggregate rose by 4.5 percent.

On the public finance side, end-August data show a budget deficit of 27.8 billion dirhams, widening by 1.9 billion compared to the same period of 2017. Overall expenditure rose by 2.2 percent, mainly reflecting higher spending on other goods and services, transfers to local governments and subsidy costs. At the same time, current revenue grew only by 0.4 percent, reflecting improved tax receipts and a decline in nontax revenues. Taking account of the reduction of 2.6 billion in outstanding expenditures, the Treasury recorded a cash deficit of 30.4 billion, down 3 billion compared to the same period of 2017. This need as well as the negative external net flow of 3.1 billion were covered by domestic resources, amounting to 33.6 billion. As a result, direct public debt would have risen by 3.3 percent at end-August compared to its December-2017 level.

In terms of national accounts, data for the first quarter of 2018 show a slowdown in growth from 3.5 percent to 3.2 percent, driven by a sharp deceleration from 14.8 percent to 2.5 percent in agricultural value added. The growth of nonagricultural activities accelerated from 2 percent to 3.4 percent. On the demand side, household final consumption slowed significantly from 5 percent to 3 percent, while general government consumption increased by 2 percent, as against 1.6 percent. Investment rose 9.7 percent, from 6.2 percent a year earlier. The net volume of exports contributed 1.9 percentage point to growth, as opposed to 1.5 point. Against this backdrop, the labor market conditions were characterized by a relative improvement, as 117 thousand jobs were created in the second quarter of 2018, including 53 thousand in services. Considering a net entry of 97 thousand jobseekers, the unemployment rate fell from 9.3 percent to 9.1 percent.

In the real estate market, prices stabilized in the second quarter of 2018, covering particularly an increase for urban land and a decline for residential and commercial property. Transactions were up 0.4 percent, reflecting mainly higher sales of residential property and lower sales of commercial property and urban land sales. Regarding the stock market, the MASI slumped 9.1 percent in the second quarter, and the volume of transactions on the central market amounted to 13 billion dirhams, down 12.2 percent compared to the same period of the previous year.

As forecast in the last Monetary Policy Report, inflation accelerated from 2 percent in the first quarter to 2.6 percent in the second quarter of 2018. Recent data indicate a slowdown to 2.1 percent in July and 1.7 percent in August, driven mainly by a deceleration of volatile food prices. Core inflation, which reflects the underlying trend, remained subdued, standing at 1 percent in July and 1.2 percent in August.

In terms of outlook, global economic activity should continue to grow at a sustained pace in 2018, but would slow in 2019. In the United States, after a 2.2 percent rate in 2017, growth would stand at 2.8 percent in 2018, driven by the tax reforms, before slowing to 2 percent in 2019, due to the dissipation of the impact of the latter and further normalization of the Fed's monetary policy. In the euro area, growth is expected to moderate in the medium term, falling from 2.5 percent to 2.1 percent in 2018 and to 1.7 percent in 2019, partly due to uncertainties surrounding global trade relations and the tightening of monetary conditions expected in 2019. In the labor market, conditions would remain favorable, with respectively low and dropping unemployment rates in the United States and in the euro area.

In emerging countries, economic activity should suffer from uncertainties about the global economy and pressures on their currencies. In 2018 in particular, growth is expected to improve less than expected in Brazil, and would continue in Russia to be supported mainly by higher oil prices. The Chinese economy would remain resilient while continuing to decelerate owing to its economic rebalancing policy.

In the commodity market, the upward trend in oil prices is expected to be reversed in 2019. After averaging $54.4/bl in 2017, the Brent price would stand around $69.8/bl in 2018 before falling back to $63.8/bl in 2019, assuming an increase in production, particularly in the United States, coupled with an expected deceleration in the global economy. Food prices would post slight declines over the forecast horizon. Prices for phosphates and derivatives should increase in 2018 to $390/mt for DAP and to $315/mt for TSP, while prices for crude phosphate would be around $95/mt. In 2019, prices should rise again, albeit slightly. Under these conditions, particularly taking account of the consolidation of domestic demand, inflation should be over the medium term at a level close to the Fed target in the United States, and would stand in the euro area at levels lower than those forecast by ECB.

Nationally, the export momentum would continue in the medium term, with an increase of 8.2 percent in 2018 and 6.8 percent in 2019, driven by the continued performance of phosphates and derivatives in 2018 and the expected rise in the automotive sector sales, with the start-up of the Peugeot plant expected in 2019. Meanwhile, imports would increase by 7.3 percent in 2018 and 3.4 percent in 2019. Travel receipts and remittances from Moroccan expatriates should remain in 2018 close to their 2017 level, before increasing by almost 4 percent in 2019. Considering donations from GCC partners expected at 4.8 billion dirhams in 2018 and 2.1 billion in 2019, the current account deficit would widen to 4 percent of GDP in 2018 and 3.7 percent in 2019. The assumption of an FDI inflow equaling 3.6 percent of GDP in 2018 and 2019 was maintained.

Under these conditions, the stock of international reserves would remain virtually stable at 240.8 billion dirhams at the end of 2018 and reach 252.3 billion at the end of 2019. It would cover around 5 months and 10 days and 5 months and 18 days respectively of imports of goods and services.

Considering these developments and the increase in currency in circulation, the liquidity requirements should widen to 56.9 billion dirhams at end-2018 and stabilize at this level in 2019. Monetary conditions would remain appropriate, with particularly a continued depreciation of the real effective exchange rate in 2018. Lending to the nonfinancial sector would continue to grow moderately, with rates forecast at 4 percent in 2018 and 4.5 percent in 2019.

In terms of public finances, the fiscal deficit was revised upwards to 3.7 percent of GDP in 2018, following the downward revision of tax revenues and the assumption regarding donations from the GCC countries. In 2019, it would decrease to 3.3 percent, driven by efforts to curb spending and revenue mobilization.

After a rate of 4.1 percent in 2017, domestic growth should slow to 3.5 percent in 2018 and 3.1 percent in 2019, mainly reflecting an increase of 5.1 percent in 2018 and a decline of 1.6 percent in 2019 in the agricultural value added. On the other hand, nonagricultural activities would continue to recover, with an increase of 3.3 percent in their value added in 2018 and 3.7 percent in 2019. On the demand side, its domestic component would continue to stimulate growth, while net volume of exports would contribute negatively to growth.

Against this backdrop, inflation would accelerate from 0.7 percent in 2017 to 2.1 percent in 2018, driven by a significant increase in the prices of goods excluded from its core component, before falling back to 1.2 percent. in 2019. Its underlying trend is expected to decelerate to 1 percent in 2018, in conjunction with slower growth in some food prices, before rising to 1.2 percent in 2019.

The central scenario forecast remains surrounded by several risks, with a balance tilted to the downside for growth and to the upside for inflation. Indeed, growth could be negatively impacted by a slowdown in foreign demand addressed to Morocco, due to several factors, including a hieightened trade war between the United States and some of its partners, rising geopolitical tensions in the Middle East, political difficulties in some euro area countries and continuing uncertainties surrounding the Brexit terms. With regard to inflation, a significant rise in energy prices on the international market and possible consequences from the social dialogue would lead to a faster rise in prices.

1.INTERNATIONAL DEVELOPMENTS

In recent months, the international economic environment was marked by heightened trade tensions, with an increased use of protectionist measures, by disturbances on the financial markets due to the depreciation of emerging market currencies following the fall of the Turkish lira, as well as by the persistent geopolitical tensions owing to the reinstatement of US sanctions on Iran. These developments led to a rise in risk aversion on the bond market and underperformance of stock markets.

Despite these disruptions, the global economy remains broadly resilient, as second quarter data show continued economic momentum in the major advanced economies. Thus, growth strengthened in the United States and remains buoyant in the euro area and the United Kingdom, despite a context of uncertainties on the Brexit terms. In the key emerging economies, growth fell in China and Brazil and accelerated in India and Russia.

In the labor markets, conditions remain solid in the advanced countries, with the unemployment rate stabilizing at 3.9 percent in August in the United States and 8.2 percent in July in the euro area, i.e. its lowest level since December 2008.

In addition, international commodity prices were overall edging downward in August. In particular, oil prices declined in conjunction with rising inventories in the United States and fears that trade tensions would affect global growth. Under these conditions, inflation decelerated in both the United States and the euro area. Overall, these developments suggest the moderation of external inflationary pressures over the coming quarters.

1.1 Economic activity and employment

1.1.1 Economic activity

In the second quarter of 2018, growth continued to accelerate in the United States, partly thanks to the tax reform adopted at the end of 2017. Indeed, GDP grew by 2.9 percent, year on year, from 2.6 percent, driven particularly by the good performance of household consumption and exports. In the euro area, while remaining robust, growth decelerated to 2.1 percent from 2.4 percent a quarter earlier. This deceleration reflects mainly slower growth from 2.1 percent to 1.7 percent in France, from 2.1 percent to 2 percent in Germany, from 1.4 percent to 1.2 percent in Italy and from 3 percent to 2.7 percent in Spain.

Table 1.1: YoY change in quarterly growth

	2016		2017				2018	
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Advanced economies								
United States	**1.5**	**1.9**	**1.9**	**2.1**	**2.3**	**2.5**	**2.6**	**2.9**
Euro area	**1.7**	**2.1**	**2.1**	**2.5**	**2.8**	**2.7**	**2.4**	**2.1**
France	0.9	1.2	1.4	2.3	2.7	2.8	2.1	1.7
Germany	2.1	1.9	2.1	2.2	2.7	2.8	2.1	2.0
Italy	0.9	1.0	1.3	1.6	1.8	1.6	1.4	1.2
Spain	3.2	3.0	3.0	3.1	3.1	3.1	3.0	2.7
United Kingdom	**1.7**	**1.7**	**1.8**	**1.8**	**1.7**	**1.3**	**1.2**	**1.3**
Japan	**1.0**	**1.5**	**1.4**	**1.6**	**2.0**	**2.0**	**1.1**	**1.3**
Emerging economies								
China	**6.7**	**6.8**	**6.9**	**6.9**	**6.8**	**6.8**	**6.8**	**6.7**
India	**7.2**	**6.9**	**6.0**	**5.6**	**6.1**	**6.6**	**7.6**	**8.0**
Brazil	**-2.7**	**-2.5**	**0.0**	**0.4**	**1.4**	**2.1**	**1.2**	**1.0**
Turkey	**5.8**	**7.5**	**4.8**	**4.9**	**-0.8**	**4.2**	**5.2**	**5.1**
Russia	**-0.2**	**0.4**	**0.6**	**2.5**	**2.2**	**0.9**	**1.3**	**1.9**

Source : Thomson Reuters Eikon.

On the other hand, despite Brexit-related uncertainties in particular (Box 1.1), economic activity consolidated slightly in the United Kingdom, as GDP grew 1.3 percent from 1.2 percent, thanks to the recovery of household consumption and investment. In Japan, growth accelerated from 1.1 percent to 1.3 percent, driven mainly by the recovery of non-residential private investment. Regarding the main emerging countries, the Chinese economy remained resilient despite trade tensions with the United States, as growth slowed slightly in the second quarter from 6.8 percent to 6.7 percent. Growth in Brazil posted its second successive decline from 1.2 percent to 1.0 percent, mainly due to strikes by transport operators and uncertainties surrounding the presidential elections. In India, after suffering the effects of the demonetization of certain banknotes and the new goods and services tax in 2017, economic activity strengthened in 2018, with growth reaching 8 percent in the second quarter, from 7.6 percent, thanks to improved household consumption and investment. Similarly, growth in Russia accelerated again to 1.9 percent from 1.3 percent in the first quarter.

Box 1.1 : Long-term impact of Brexit on the European Union

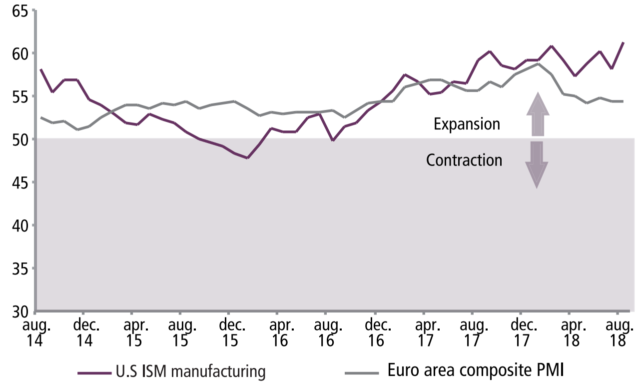
The United Kingdom is one of the largest trading partners of the EU-27, accounting for around 13 percent of trade in goods and services. In addition to their bilateral trade relationship, the EU and the UK also share very important links in the supply chain that involve several countries. Financial interconnections are also substantial, with the gross amount of bilateral flows representing about 52 percent of EU GDP in 2016. Migration movements have also become important for some countries, notably Ireland. Brexit will therefore have negative consequences on income and employment in the EU, irrespective of the final agreement.

According to IMF estimates, if the UK and the EU settle on a standard free trade agreement (FTA), where customs duties on traded goods are low but with higher non-tariff barriers, EU real output would be lower by 0.8 percent and employment by 0.3 percent in the long run than in a no-Brexit scenario. If the parties abide by WTO rules, long-term declines in real output and employment would be even larger. They are estimated at 1.5 percent and 0.7 percent, respectively. However, a "Norway" scenario (European Economic Area, EEA), where membership in the customs union is brought to a standstill, but access to the single market is preserved, the decline in output and employment for the EU-27 would seem insignificant.

The more any country trades with the UK, the larger the Brexit-related hit to its output will be. Thus, EU-27 real output would be lower by 0.2 percent in the long run under the FTA scenario than under a no-Brexit scenario, with the hit to Ireland's income the largest in the EU-27 (about 2.5 percent of income), followed by the Netherlands, Denmark, Belgium and the Czech Republic. These estimated impacts increase in the event of a recourse to WTO rules: the fall in output relative to a no-Brexit scenario would reach 0.5 percent for the EU-27 and 4 percent for Ireland, in particular, given the substantial tightening in both tariff and non-tariff barriers.

Meanwhile, high frequency indicators for the third quarter point to an improvement in economic activity in advanced countries. Indeed, the Eurozone composite PMI rose to 54.5 points in August from 54.3 points in July. Similarly, the US manufacturing ISM data show a rise to 61.3 points from 58.1 points recorded a month earlier.

Chart 1.1: Change in some high-frequency indicators in the U.S and the Euro Area



Source : Thomson Reuters.

1.1.2 Labor market

The labor market conditions continued to improve in advanced countries. In the United States, the unemployment rate stabilized at 3.9 percent in August, with job creation increasing to 201,000 jobs from 147,000 jobs in the previous month. In the euro area, the latest data of July show a stagnation of the unemployment rate at 8.2 percent, which is the lowest level recorded since December 2008. By country, this rate stabilized at 3.4 percent in Germany, while it decreased from 10.8 percent to 10.4 percent in Italy and from 15.2 percent to 15.1 percent in Spain. On the other hand, it rose in France to 9.2 percent from 9.1 percent a month earlier. In the United Kingdom, June-data indicate an increase in the unemployment rate to 4 percent.

Table 1.2: Change in unemployment rate (%)

	2016	2017	2018		
			june	july	august
United States	**4.9**	**4.4**	**4.0**	**3.9**	**3.9**
Euro area	**10.0**	**9.1**	**8.2**	**8.2**	**n.a**
France	10.1	9.4	9.1	9.2	n.a
Italy	4.1	3.8	3.4	3.4	n.a
Germany	11.7	11.2	10.8	10.4	n.a
Spain	19.6	17.2	15.2	15.1	n.a
United Kingdom	**4.8**	**4.4**	**4.0**	**n.a**	**n.a**

Source : Eurostat and BLS.

1.2 Monetary and financial conditions

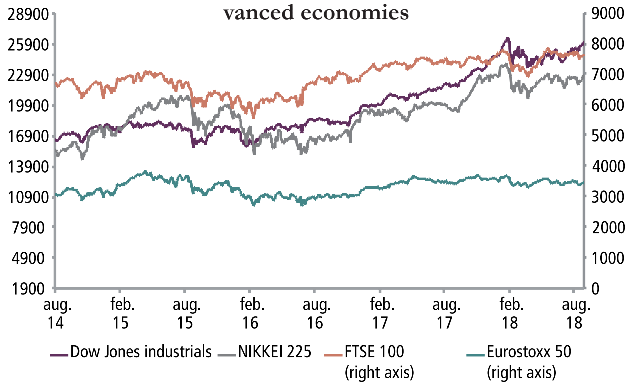
In a context marked by geopolitical tensions and an increase in uncertainties, the international stock markets registered divergent trends and higher volatility. The EUROSTOXX50 fell between July and August by 0.6 percent and the FTSE 100 by 0.4 percent, while the Dow Jones and NIKKEI 225 showed respective increases of 2.6 percent and 0.5 percent. In addition, the fall of the Turkish lira amid a diplomatic crisis between the United States and Turkey shook the main stock markets of emerging countries, raising fears of contagion. The MSCI EM dropped by 1.5 percent, mainly reflecting declines of 19 percent in Turkey and 4.8 percent in China.

On the bond market, the rise in risk aversion led to higher yields in August in some European countries. With the exception of Germany where they stagnated at 0.3 percent, 10-year yields rose from 0.61 percent to 0.64 percent in France, from 1.3 percent to 1.4 percent in Spain, from 0.5 percent to 0.6 percent in Ireland and from 4.4 percent to 4.6 percent in Greece. More particularly, the political crisis in Italy impacted the debt market wher yields rose from 2.7 percent to 3 percent. The US Treasury bonds stagnated at nearly 2.8 percent.

In key emerging economies, 10-year sovereign yields rose between July and August from 17.1 percent to

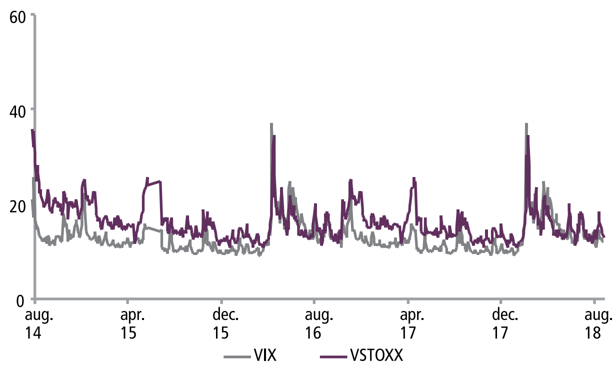
20 percent in Turkey and from 10.4 percent to 10.7 percent in Brazil, while they stagnated in China and India at 3.5 percent and 7.8 percent, respectively.

Chart 1.2: Change in major stock market indexes of advanced economies



Source : Thomson Reuters.

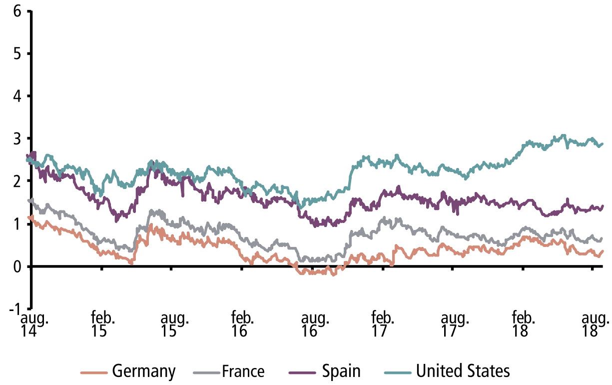
Chart 1.3: Change in VIX and VSTOXX



Source : Thomson Reuters Eikon.

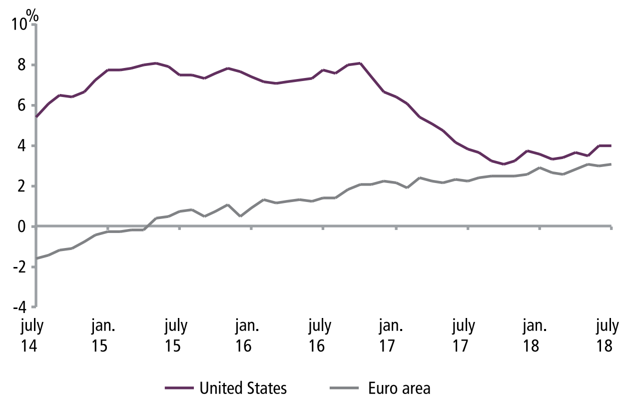
In the money markets, the 3-month Euribor remained unchanged at -0.3 percent and the same-maturity Libor at 2.3 percent. Meanwhile, the annual bank lending growth stabilized in July at 3.9 percent in the United States and 3 percent in the euro area.

Chart 1.4: Change in the yield of ten-year government bonds



Source: Thomson Reuters Eikon.

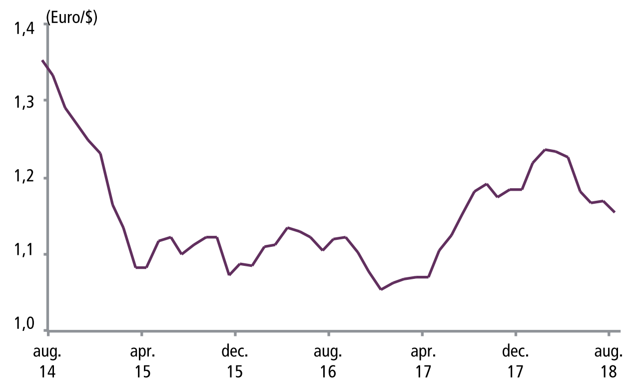
Chart 1.5: YoY change in credit in the United States and the euro area



Source : Thomson Reuters Eikon.

In the currency markets, the slowdown in the euro area's economic activity coupled with growing concerns over trade tensions and the political crisis in Italy weighed on trends of the euro, which depreciated between July and August by 1.2 percent vis-à-vis the dollar and 1.6 percent against the Japanese yen. Conversely, it appreciated slightly by 1.1 percent against the pound sterling. The main emerging countries' currencies depreciated against the dollar by 2.6 percent for the Brazilian real, 1.3 percent for the Indian rupee, 2 percent for the Chinese yuan and 19 percent for the Turkish lira (Box 1.2).

Chart 1.6: Euro/dollar exchange rate



Source : Thomson Reuters Eikon.

As regards monetary policy decisions, the ECB decided on September 13 to keep its rates unchanged, while predicting that they will remain at their present levels at least through the summer of 2019 and, in any case, for as long as necessary to ensure the continued sustained convergence of inflation to levels that are below, but close to, 2 percent over the medium term. It also reaffirmed that its net purchases under the asset purchase program should continue until the end of September 2018 at a monthly pace of 30 billion euros. It expects that after September 2018, the monthly pace of purchases will be reduced to 15 billion euros, until the end of December 2018, and that subject to incoming data confirming its medium-term inflation outlook, these purchases will come to an end.

The FED decided on August 1 to maintain the target range for the federal funds rate unchanged at 1.75 percent to 2 percent and reiterated that its policy stance would remain accommodative, thereby supporting stronger labor market conditions and a sustained return to 2 percent inflation.

At its meeting on September 12, the Bank of England decided to maintain its key rate unchanged at 0.75 percent. It also decided to keep the stock of UK government bond purchases at £435 billion and that of sterling nonfinancial investment-grade corporate bond purchases at £10 billion.

In emerging countries, the Reserve Bank of India decided on August 1 to raise its key rate by 25 basis points to 6.5 percent, in a context of increasing inflation. Similarly, the Russian Central Bank raised its policy rate by 0.25 percentage point on September 14 to 7.5 percent, while indicating a risk of faster inflation and volatile ruble. The Central Bank of Brazil maintained on September 19 its policy rate at 6.5 percent, while underlining that the economic growth evolving at a slower pace than expected suggests that the rate would be maintained at its current level and that the next steps in monetary policy will continue to depend on the economic trends and inflation expectations.

Box 1.2 : Currency crisis in Turkey

The recent heigthening of diplomatic tensions between Turkey and the United States caused the Turkish lira to collapse to record levels. Indeed, the United States, which calls for the release of the American pastor accused by Turkey of espionage and terrorism, decided, on August 10, to double tariffs on their imports of Turkish steel and aluminum.

As a result, the Turkish lira lost 14 percent of its value vis-à-vis the dollar on that day, thus accumulating a loss of nearly 23 percent since early August. Similarly, the stock market recorded its biggest daily drops since 2013. The MSCI Turkey index was down 19 percent from one month to the next in August and its volatility[1] increased significantly from 14.2 to 27.5.

1 Measured by the standard deviation.

Chart B.1.2.1 : Exchange rate of the Turkish pound/dollar

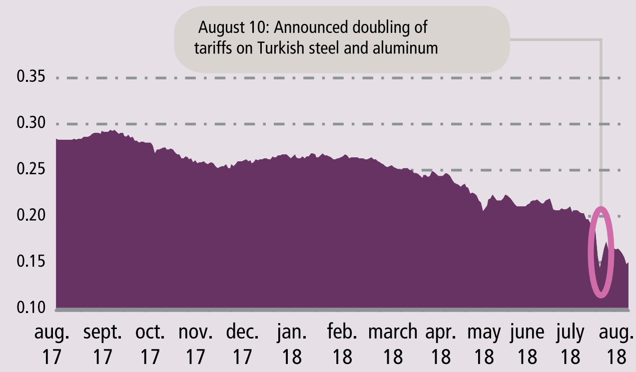
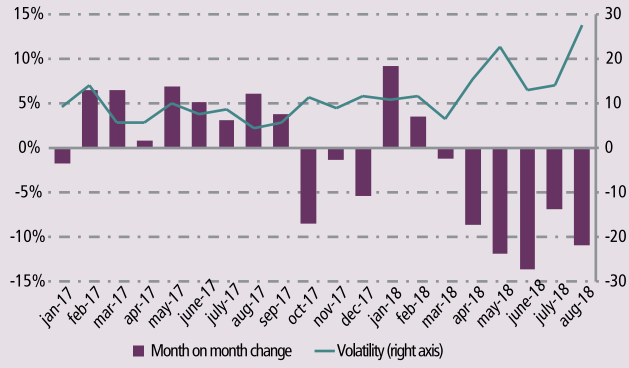


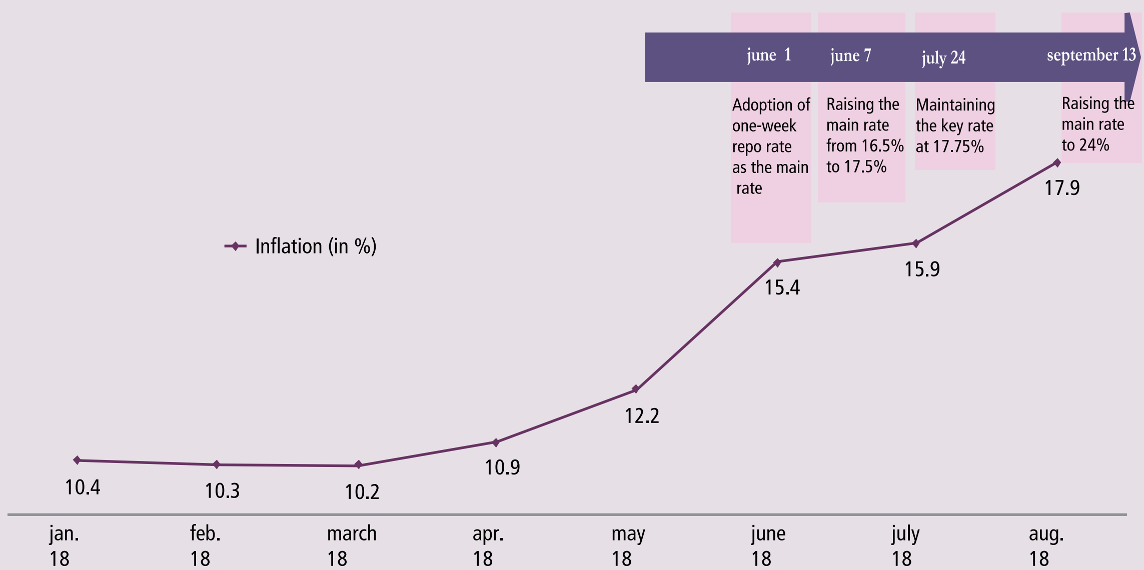
Chart B.1.2.2 : Turkey MSCI index



Source : Thomson Reuters.

Owing to the fall of the lira, inflation soared to 17.9 percent in August, its highest level since the end of 2003. Turkey announced similar measures on several US products (alcoholic beverages, cars, tobacco, rice, coal, etc.) with a tariff increase ranging from 14 percent to 140 percent. Meanwhile, the Central Bank of the Republic of Turkey (CBRT) issued a statement on September 3 stating that it would take the necessary steps to support price stability and that it would adjust its monetary policy stance at its next meeting. Thus, it decided on September 13 to raise its key rate by 625 basis points to 24 percent. It should be noted that from June 1, the BCRT adopted, for reasons of simplification, the one-week repo rate as its key rate. The latter was raised on June 7 from 16.5 percent to 17.75 percent and at the meeting of July 24, it was kept unchanged at this same level.

Chart B.1.2.3 : Inflation and monetary policy decisions



Sources : BCRT & Turkstat.

1.3 Commodity prices and inflation

1.3.1 Energy commodity prices

As a result of rising oil inventories in the United States earlier this month and fears that trade tensions would affect global growth (Box 1.3), Brent prices continued to fall to $73.1 on average in August. They were down 1.8 percent from July, but up 42.4 percent, year on year.

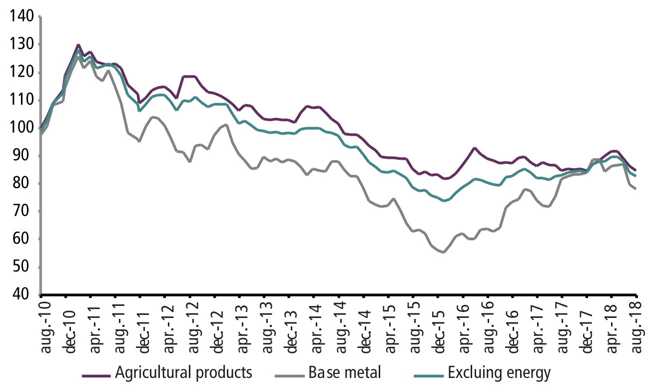
Chart 1.7 : Brent prices in dollars

Source : World Bank.

1.3.2 Non-energy commodity prices

Non-energy commodity prices edged down 0.6 percent in August, year on year, covering a 4.2 percent decline in metal and mining prices and a 0.2 percent increase in agricultural ones. In particular, wheat prices grew by 8.4 percent compared to July and 38.2 percent year on year.

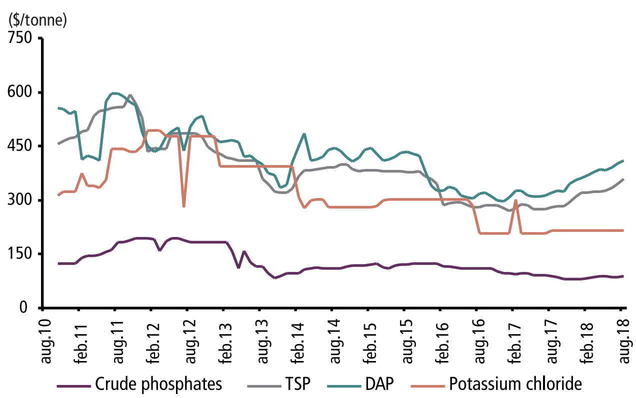
Chart 1.8: Change in non-energy commodity price indexes (2010= 100)



Source : World Bank.

In the international market for phosphate and fertilizers, a virtually generalized price increase was recorded in August, with rates of 0.7 percent to $87.5 for crude phosphate, 2.1 percent to $409 for DAP, 4.1 percent to $358 for TSP and 3 percent to $260 for urea. The potassium chloride price continued to stagnate for a year at $215.5. On an annual basis, data indicate price increases of 27.5 percent for DAP, 27.4 percent for TSP and 35 percent for urea, while reporting a price decline of 1.4 percent for crude phosphate.

Chart 1.9: Change in the world prices of phosphate and derivatives

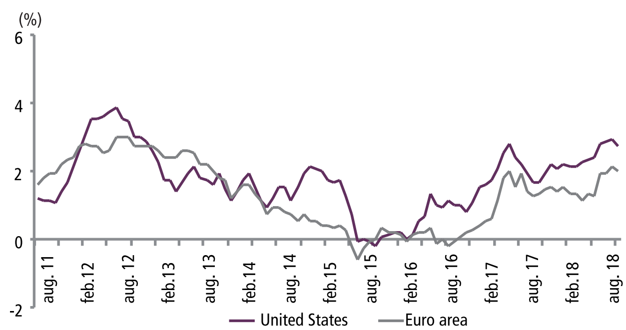


Source: World Bank.

1.3.3 Inflation

In August, inflation in the euro area decelerated from 2.1 percent to 2 percent, reflecting declines from 2.1 percent to 1.9 percent in Germany, from 2.3 percent to 2.2 percent in Spain and from 1.9 percent to 1.6 percent in Italy, as well as stagnation at 2.6 percent in France. For the other major advanced economies, inflation fell from 2.9 percent to 2.7 percent in the United States, and rose from 2.5 percent to 2.7 percent in the United Kingdom and from 0.9 percent to 1.3 percent in Japan. In emerging countries, inflation grew faster in August from 2.1 percent to 2.3 percent in China and from 2.5 percent to 3 percent in Russia. On the other hand, it dropped from 4.2 percent to 3.7 percent in India and from 4.5 percent to 4.2 percent in Brazil.

Chart 1.10: Inflation in the United States and the euro area



Sources : Eurostat and BLS.

Table 1.3 : Recent year-on-year change in inflation in main advanced countries

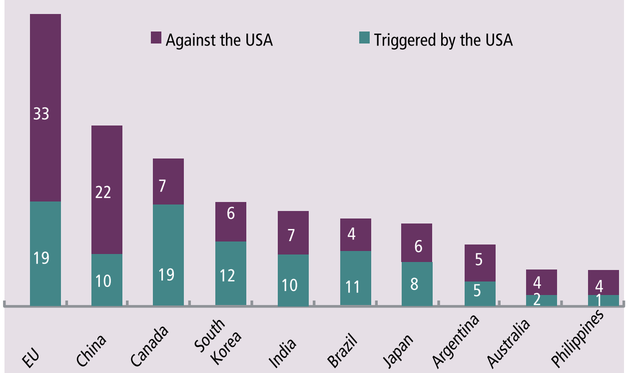
	2016	2017	2018		
			june	july	august
United States	**1.3**	**2.1**	**2.9**	**2.9**	**2.7**
Euro area	**0.2**	**1.5**	**2.0**	**2.1**	**2.0**
Germany	0.4	1.7	2.1	2.1	1.9
France	0.3	1.2	2.3	2.6	2.6
Spain	-0.2	2.0	2.3	2.3	2.2
Italy	-0.1	1.3	1.4	1.9	1.6
United Kingdom	**0.7**	**2.7**	**2.4**	**2.5**	**2.7**
Japon	**-0.1**	**0.5**	**0.7**	**0.9**	**1.3**

Sources : Thomson Reuters, Eurostat and IMF.

Box 1.3 : Implications of the trade war for the global economy

In recent months, a trade war was looming between the United States and several of its trading partners. The stance towards protectionism was first and foremost an election promise of the new U.S administration. In February 2017, the United States announced its intention to renegotiate NAFTA and, in March, it introduced additional tariffs of 25 percent on steel imports and 10 percent on aluminum imports. The focus was subsequently on China, which, because of accusations of unfair commercial practices, particularly in the field of intellectual property and forced technology transfer, was subjected to new tariffs up to 25 percent on its exports to the United States worth of $50 billion[1]. China, who denounced these actions, initiated a series of retaliatory measures targeting imports from the United States, particularly agricultural commodities, automotive equipment and certain chemicals and took the case to the World Trade Organization.

Chart B 1.3.1 : Number of the US trade disputes in 2018



Source : WTO.

1 An initial list, released in June and effective on July 6, concerned $34 billion in industrial goods. It was completed in August by new products worth of $16 billion. It should be noted that all of these products are largely inputs to high technology sectors, such as the automotive industry, aerospace industry, information and communication technologies, machinery and robotics and which benefit from the industrial policy "Made in China 2025".

According to estimates by the ECB[2], an increase of 10 percentage points in US tariffs on imports of goods, which would be accompanied by a similar increase from US trading partners, would result during the first year in declines of 2.5 percent in US GDP, 3 percent in global goods trade and 1 percent in world GDP. A study by the Banque de France, adopting the same scenario, suggests a drop of 0.7 percent in world GDP in the first year and 1 percent in the second year. Assuming a more dramatic increase in tariffs, i.e. 60 percentage points, world GDP could decline by 6 percent. Also, taking into account several other amplifying factors, mainly the fall in productivity and investment in a context of uncertainties, estimates by the Banque de France show that an increase of 10 percentage points in tariffs would cause world GDP to decline by 1.5 percent to 2 percent in the first year and by 2.2 percent to 2.9 percent in the second year.

Morgan Stanley Bank estimates that by imposing a 25 percent tariffs on $50 billion in Chinese products, the impact on global growth would be -0.09 percentage point. In the event of significant spiraling of trade tensions, it would reach -0.32 percentage point, or even -0.81 in a scenario of 25 percent hikes across all imports. The economist Paul Krugman[3] believes that an increase in tariffs of between 30 percent and 60 percent would lead to a very large reduction in world trade of around 70 percent and in world GDP of around 2-3 percent.

On the other hand, there are relatively positive signals after the agreement in principle between the United States and Mexico regarding the new NAFTA. This deal covers 3 areas:

1) a rebalancing of the agreement to support the manufacturing industry of both countries. For this purpose, it stipulates that inputs to the automotive sector be produced to the tune of 75 percent in the United States and Mexico and with shares of 40 percent to 45 percent by workers whose wages are at least $16 an hour;

2) strengthening the agreement to allow fairer trade in agricultural products, including by maintaining tariff-free measures; and

3) modernizing the agreement to support mutually beneficial trade, thereby leading to a freer market, fairer trade and robust economic growth in North America.

2 Benoît Cœuré, member of the Executive Board of the ECB, panel contribution, at the 29th edition of the workshop “The Outlook for the Economy and Finance», organized on April 06, 2018 in Cernobbio, Italy.
3 https://www.nytimes.com/2018/06/17/opinion/thinking-about-a-trade-war-very-wonkish.html

2. EXTERNAL ACCOUNTS

At the end of August 2018, the trade deficit widened by 12.7 billion dirhams to 137.9 billion compared to the same period of the previous year. Imports increased by 29.3 billion or 10.2 percent, mainly reflecting higher purchases of capital goods and higher energy costs. At the same time, exports improved by 16.6 billion or 10.2 percent, particularly with continued momentum in sales of the automotive industry and the phosphates and derivatives sector. The import coverage ratio stabilized at 56.6 percent.

The growth of travel receipts and transfers from Moroccan expatriates decelerated markedly since the beginning of the year to 1.2 percent and 1 percent, respectively. In terms of major financial transactions, the net FDI inflow declined by 18.6 percent to 14.6 billion. Under these conditions and taking account of other items of the balance of payments, Bank Al-Maghrib's net international reserves stood at 225.8 billion dirhams at the end of August, equaling 5 months of imports of goods and services.

2.1 Trade balance

2.1. 1 Exports

Exports improved across all sectors. In particular, the automotive industry sales grew by 17.7 percent and exports of phosphates and derivatives increased by 17.6 percent to 33.8 billion dirhams. Similarly, agricultural and agri-food exports grew by 4.6 percent to 38.2 billion and aviation industry sales improved by 17.2 percent to 8.1 billion. Exports of the textile and leather sector posted an increase of 3.4 percent to 26.5 billion dirhams.

Table 2.1: Change in exports

Sectors/ Segments	jan-aug. 2018	jan-aug. 2017	Change (in millions of Dh)	
			Value	In %
Exports	**179 540**	**162 972**	**16 568**	**10.2**
Phosphates and derivatives	33 768	28 710	5 058	17.6
Automobile	43 629	37 055	6 574	17.7
Agriculture and Agribusiness	38 155	36 471	1 684	4.6
Textile and leather	26 478	25 605	873	3.4
Aeronautics	8 097	6 909	1 188	17.2
Electronics	6 435	6 033	402	6.7
Pharmaceutics	829	770	59	7.7
Others	22 149	21 419	730	3.4

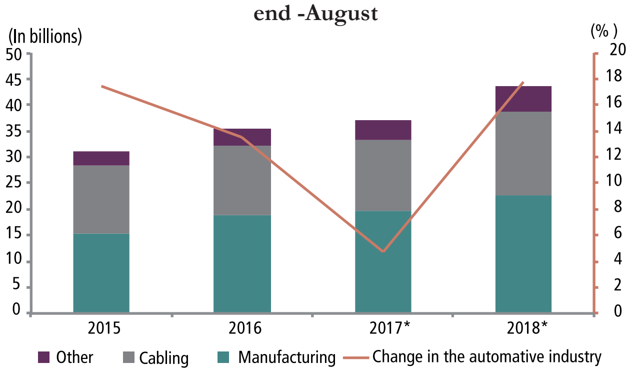
Source: Foreign Exchange Office.

Table 2.2: Change in the exports of phosphates and derivatives (YoY, in %)

	jan-july 2018/jan-july 2017		
	Value	Quantity	Price
Crude phosphates	-4.7	5.1	-9.4
Natural and chemical fertilizers	19.6	8.1	10.7
Phosphoric acid	17.1	-1.1	18.3

Source: Foreign Exchange Office.

Chart 2.1: Breakdown of automotive industry's exports at end -August



* Preliminary data

Source: Foreign Exchange Office.

2.1.2 Imports

The increase in imports reflects mainly a rise of 12.5 percent to 78.7 billion in acquisitions of capital goods and an increase of 18.8 percent in the energy bill to 53.6 billion, with increases of 22.8 percent for "gas oil and fuel oils" and 44.7 percent for "coal, coke and similar solid fuels". Purchases of consumer goods moved up 6.6 percent to 70.7 billion, mainly reflecting a 30.9 percent increase in imports of passenger car components and parts.

In total, the trade deficit widened by 12.7 billion to 137.9 billion dirhams, and the import coverage ratio stabilized at 56.6 percent.

Table 2.3 : Change in imports

Products group	jan-aug. 2018	jan-aug. 2017	Change	
			Value (in millions of Dh)	In %
Imports (CIF)	**317 431**	**288 180**	**29 251**	**10.2**
Energy products	53 574	45 106	8 468	18.8
Equipment goods	78 650	69 914	8 736	12.5
Raw products	16 171	13 687	2 484	18.1
Finished consumer goods	70 662	66 261	4 401	6.6
Semi- finished products	66 329	63 789	2 540	4.0
Food products	31 928	29 319	2 609	8.9

Source: Foreign Exchange Office.

Table 2.4 : Yoy change in major import products (YoY, in %)

	jan-july 2018/jan-july 2017		
	Value	Quantity	Price
Gas oils and fuel oils	17.2	4.7	12.0
Passenger vehicles	-5.7	-11.2	6.2
Parts of cars and passenger vehicles	26.8	23.5	2.6
Petroleum gaz and other fuel	18.4	-7.3	27.7

Source: Foreign Exchange Office.

2.2 Other components of the current account

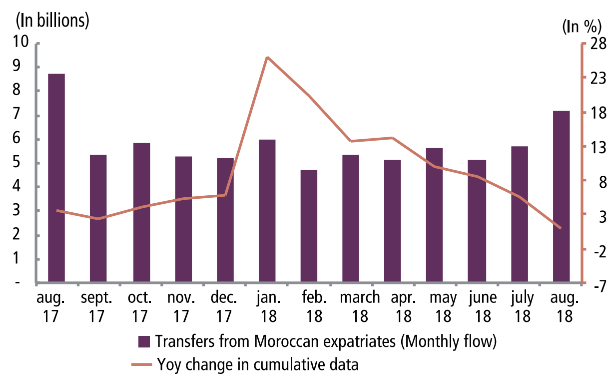
in terms of the services balance, travel receipts rose 1.2 percent to 48.6 billion dirhams, while relevant expenditure grew 9.9 percent to 13.1 billion dirhams. Remittances from Moroccan expatriates reached 44.9 billion dirhams, up 1 percent, year on year.

Table 2.5: Change in the balance of services

(In millions of dirhams)	jan-july 2018	jan-july 2017	Change	
			Value	In %
Imports	**55 784**	**53 061**	**2 723**	**5.1**
Transport service	23 239	21 662	1 577	7.3
Travel	10 746	9 597	1 149	12.0
Exportations	**95 820**	**89 451**	**6 369**	**7.1**
Transport service	19 555	17 212	2 343	13.6
Travel	38 344	35 050	3 294	9.4
Exports	**40 036**	**36 390**	**3 646**	**10.0**

Source: Foreign Exchange Office.

Chart 2.2: Change in transfers from Moroccan expatriates



Source: Foreign Exchange Office.

2.3 Financial account

Net FDI inflow fell by 3.3 billion to 14.6 billion dirhams, due to a 1.7 billion drop in inflows and a 1.6 billion increase in the disposal of investment.

Under these conditions, outstanding net international reserves stood at 225.8 billion at end-August 2018, equaling 5 months of imports of goods and services.

3. MONEY, CREDIT AND ASSETS MARKET

In the second quarter of 2018, monetary conditions were marked by an appreciation of the effective exchange rate and a fall in lending rates. The growth of lending to the nonfinancial sector decelerated, affecting both loans to private enterprises and households. As to other counterparts of the money supply, net claims on the central government continued to accelerate and net international reserves increased after four quarters of decline. Overall, the money supply growth decelerated to 4.8 percent from 5.2 percent a quarter earlier.

On the asset markets, the Real Estate Price Index remained stable in the second quarter of 2018 compared to the previous quarter. By category of goods, this stagnation covers rising prices for urban land and decreases for residential and commercial property prices. At the same time, transactions grew by 0.4 percent, with an increase in residential property sales and decreases for commercial property assets and urban land. On the stock market, the MASI fell 9.1 percent in the second quarter and the volume of transactions stood at 13 billion dirhams, down 12.2 percent compared to the same period of the previous year.

3.1 Monetary conditions

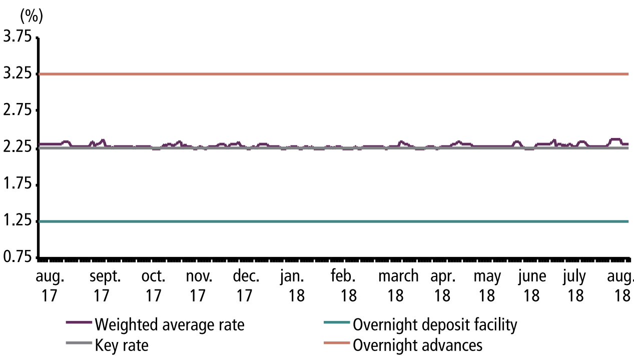
3.1.1 Bank liquidity and interest rates

During the second quarter of 2018, banks' liquidity needs increased to an average of 58.3 billion dirhams, reflecting both lower foreign exchange reserves and higher currency in circulation. Thus, Bank Al-Maghrib increased the amount of its injections to 58.9 billion, of which 55.7 billion as 7-day advances and 3 billion as secured loans granted under the program to support financing of VSMEs.

The latest available data indicate a widening of the liquidity shortage to 64.3 billion in July and 76.3 billion in August.

Against this backdrop, the interbank rate remained close to the key rate and averaged 2.27 percent in the second quarter and 2.30 percent in July and August. In the Treasury bill market, yields did not change significantly, both in the primary and secondary markets.

Chart 3.1: Change in the interbank rate (daily data)

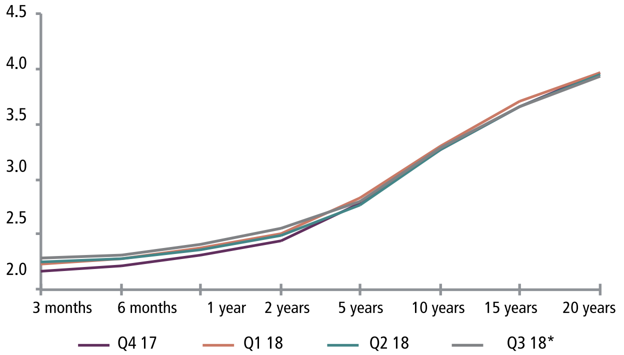


Source : BAM.

Table 3.1: Change in Treasury bond yields in the primary market

	2016		2017				2018		
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	july
52 weeks	2.33	2.30	2.32	2.26	2.36	2.29	2.35	2.31	-
2 years	2.48	2.44	2.52	2.41	2.49	2.44	2.53	2.49	2.57
5 years	2.71	2.69	2.83	2.78	2.83	2.77	2.81	2.77	2.79
10 years	3.22	3.08	3.27	3.27	3.32	3.28	3.27	3.24	3.27
15 years	-	-	3.87	3.87	3.87	3.71	3.68	3.68	3.70

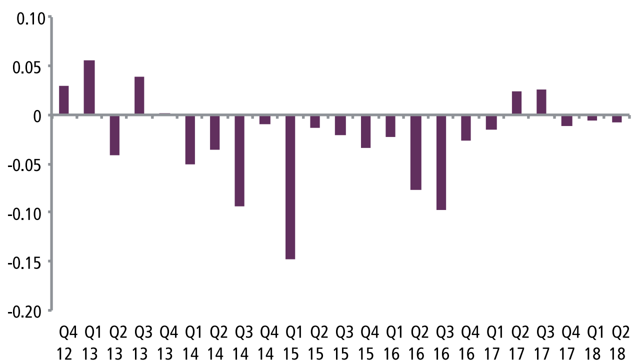
Chart 3.2: Term structure of interest rates in the secondary market



* Observed average in July and August

In other markets, the issuance rates of certificates of deposit remained almost stable during the second quarter. Similarly, deposit rates remained virtually unchanged at 2.78 percent for 6-month deposits and 3.10 percent for one-year deposits. Under these conditions, banks' cost financing[1] was virtually stable in the second quarter of 2018.

Chart 3.3: Change in cost of bank financing



Regarding lending rates, Bank Al-Maghrib's survey with banks[2] shows a drop of 7 basis points in the overall average rate in the second quarter of 2018 to 5.36 percent. This trend reflects a decline of 16 basis points in rates on loans to businesses, with particularly decreases of 31 points for equipment loans and 21 points for cash advances. By company size, rates fell by 30 points for VSMEs and by 3 points for large companies. On the other hand, rates on loans to individuals moved up 31 basis points, with mainly an increase of 6 percentage points in rates on housing loans and a rise of 17 percentage points in consumer loans.

Table 3.2 : Change in lending rates

	Q1 2018	Q2 2018	Change (in bp)
Average lending rate (%)	**5,43**	**5,36**	**-7**
Personal loans	**5,78**	**6,09**	**31**
Real estate loans	4,94	5,00	6
Consumer loans	6,40	6,57	17
Loans to enterprises	**5,28**	**5,12**	**-16**
By economic purpose			
Cash advances	5,23	5,02	-21
Equipment loans	5,51	5,20	-31
Real estate loans	**5,41**	**5,98**	**57**
By size of the company			
VSMEs	6,09	5,78	-31
LE	4,75	4,72	-3
Loans to individual businesses	**6,23**	**7,08**	**85**
Real estate loans	5,78	6,09	28

Source : BAM.

Table 3.3: Deposit rates

	2016				2017				2018	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
6 months	3,31	3,18	2,94	2,9	2,86	2,8	2,81	2,80	2,79	2,78
12 months	3,67	3,55	3,33	3,3	3,2	3,1	3,09	3,10	3,15	3,10

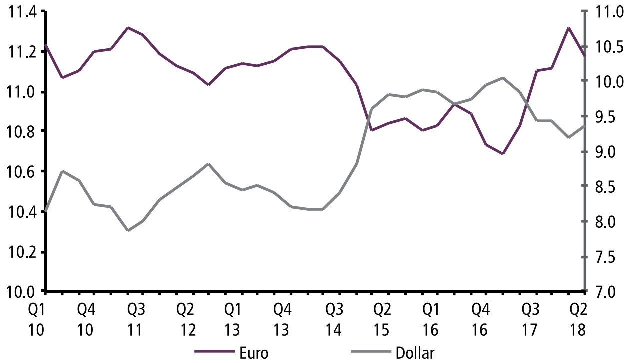
3.1.2 Exchange rate

In the second quarter of 2018, the euro depreciated by 3 percent against the US dollar. Under these conditions, the national currency appreciated by 1.2 percent versus the euro and depreciated by 1.8 percent against the US dollar. Compared to the currencies of the main emerging countries, the dirham appreciated by 12.3 percent against the Turkish lira and by 9.1 percent against the Brazilian real, owing to the pressure exerted on these two currencies in international markets, while it depreciated by 1.4 percent against the Chinese yuan.

1 The cost of financing is calculated as the weighted average of the costs of banks' liabilities.
2 This survey was significantly changed as of the first quarter of 2018, particularly to better understand the financing conditions of companies. The first quarter figures were slightly adjusted from what was published in the previous MPR.

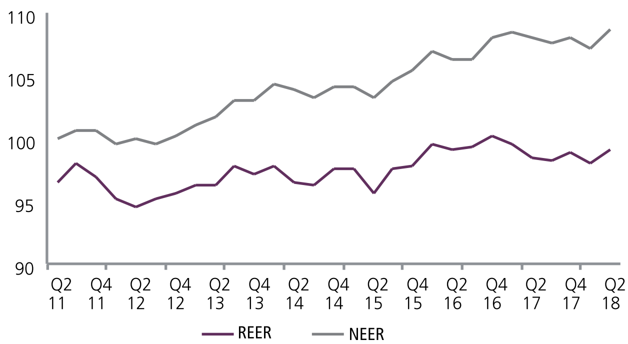
As a result, the effective exchange rate appreciated by 1.4 percent in nominal terms and by 0.9 percent in real terms.

Chart 3.4: Change in the exchange rate of the dirham



Source : BAM.

Chart 3.5: Change in the nominal and real effective exchange rates (Base 100 in 2010)



Source : BAM calculations.

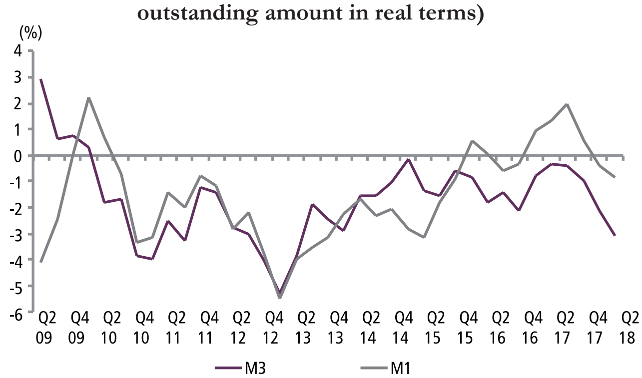
In terms of foreign currency transactions, banks' volume of spot operations with customers rose in the second quarter by 6.3 percent for sales to 20.5 billion dirhams and by 8.6 percent for purchases to 22.2 billion. In contrast, forward sales dropped by 35.6 percent to 2.2 billion and forward purchases fell by 14.8 percent to 9.7 billion. However, Bank Al-Maghrib did not carry out any transaction of purchases or sales of currencies to the banks. Under these conditions, banks' net foreign exchange position stood at 2.2 billion at end-June, from 6.1 billion at end-March 2018.

3.1.3 Monetary position

M3 aggregate growth decelerated from 5.2 percent in the first quarter of 2018 to 4.8 percent in the second quarter. This trend reflects slow growth from 18.8 percent to 8.2 percent in the certificates of deposits and a steeper decline in money market fund shares/units from 5.3 percent to 8.1 percent. Analysis of the other components of money supply indicates a slight deceleration from 7.2 percent to 7 percent in demand deposits, covering a slowdown from 8.2 percent to 7.1 percent in those of households and accelerations from 5.1 percent to 7.9 percent for private companies and from 4.3 percent to 18.4 percent for the public sector. Conversely, time deposits saw a further decline from 1.4 percent to 1.8 percent, reflecting a 38.8 percent decrease in those of the public sector, as against 1.2 percent. The growth of currency in circulation was almost stable at 7.8 percent from one quarter to the next.

By major counterparts, the change in M3 reflects an acceleration from 13.4 percent to 19.2 percent in net claims on the central government, a 1.3 percent increase in net international reserves, as against a decline of 4.6 percent as well as a slowdown from 3.4 percent to 2.2 percent in bank credit.

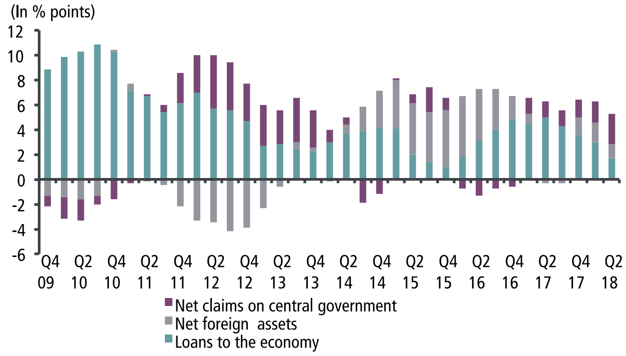
Chart 3.6: Money gap[1] (in % of M3 and M1 equilibrium outstanding amount in real terms)



1:The money gap, calculated in real terms, is the difference between the recorded money stock and the equilibrium level. The latter, defined based on the quantity equation of money, corresponds to the growth of the potential economic activity in real terms, minus the average pace of decrease in the velocity of currency in circulation.

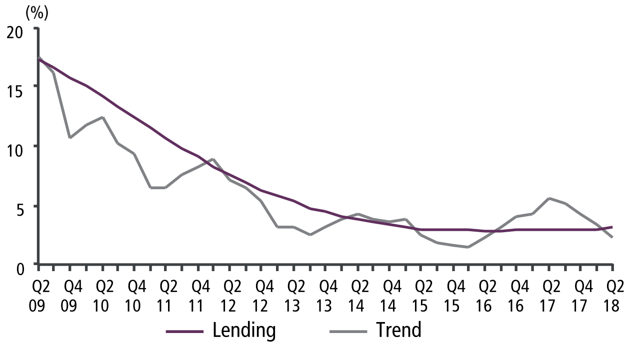
Source : BAM.

Chart 3.7: Contribution of the major counterparts to YoY change in money supply



Source : BAM.

Chart 3.8: YoY change in credit



Source : BAM.

The growth of credit to the nonfinancial sector slowed down from 4.1 percent to 3.9 percent in the second quarter, reflecting a deceleration in both loans to private corporations and to households.

Indeed, the growth of loans to private enterprises moved down from 2.2 percent to 1.6 percent, reflecting a deceleration from 7.1 percent to 6.3 percent in equipment loans and a further decline from 2.3 percent to 2.6 percent in cash advances. Conversely, loans granted to real estate development rose by 1.6 percent from 1.3 percent a quarter earlier. Loans to state-owned enterprises grew faster from 16.1 percent to 21.5 percent, in conjunction with a 32.4 percent expansion of equipment loans compared to 25.1 percent a quarter earlier, while cash advances dropped by 17.7 percent, as against 14.9 percent recorded during the first three months of the year.

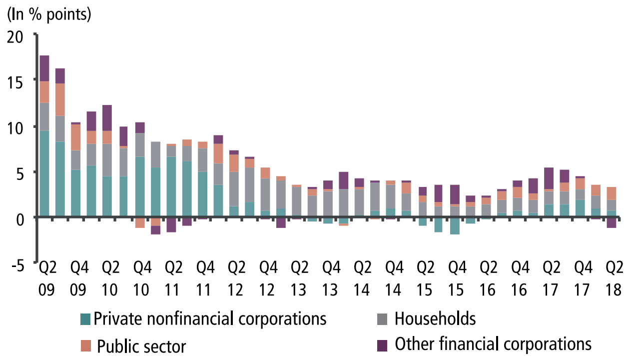
Loans to individual entrepreneurs dropped 0.4 percent, the first decline since the end of 2016. This trend is attributable to a drop of 0.4 percent in equipment loans and 2.2 percent in cash advances, as against respective increases of 3.9 percent and 6 percent a quarter earlier. However, loans to real estate development improved by 12.5 percent, as opposed to 3.1 percent in the first quarter.

By branch of activity, the latest available data show slow credit growth from 10 percent at end-March to 0.4 percent at end-June for the "transport and communication" sector, from 8.6 percent to 1.5 percent for "trade, car repairs and household items" and from 5.6 percent to 2.6 percent for "buildings and public works". Loans to the "electricity, gas and water" sector fell by 6.6 percent, which is a more pronounced decline compared to the 4.1 percent registered at end-March.

Loans to individuals moved up 4.5 percent from 4.7 percent in the first quarter, covering a slowdown of housing loans from 4.2 percent to 3.8 percent and an acceleration of consumer loans from 5.2 percent to 6 percent.

Nonperforming loans (NPLs) posted a rise of 3.1 percent, as against 3.3 percent. This trend reflects increases of 2.5 percent in NPLs of private nonfinancial businesses and 3.7 percent in those of households, as opposed to 2.8 percent and 4.7 percent, respectively. The ratio to bank credit declined from 7.8 percent to 7.7 percent overall, from 11.7 percent to 11.3 percent for businesses, while it rose from 7.6 percent to 7.8 percent for households.

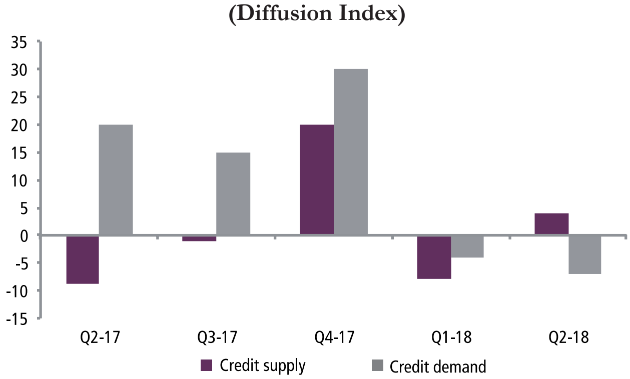
Chart 3.9: Institutional sectors' contribution to YoY change in credit



The lending conditions survey of the second quarter of 2018 indicates a slight tightening of supply conditions for businesses, as against a relative easing for individuals. Demand is set to have stagnated from one quarter to the next for businesses and to have increased for individuals.

Loans granted by nonbank financial companies to the nonfinancial sector grew 4.7 percent at end-June 2018 compared to 4.3 percent a quarter earlier. This trend covers an acceleration from 4.3 percent to 5 percent in loans granted by finance companies and a deceleration from 1.8 percent to 0.7 percent in credit granted by offshore banks.

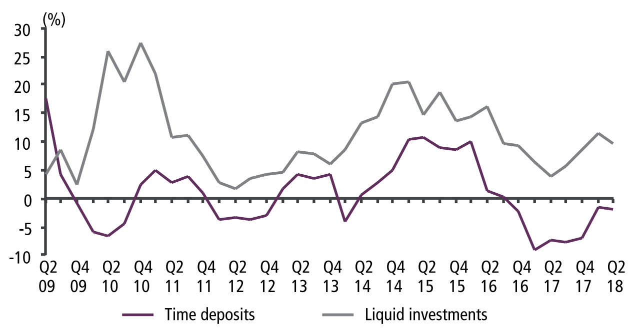
Chart 3.10: Change in supply and demand (Diffusion Index)



The latest available data for July 2018 indicate a further deceleration of bank credit to 2 percent. In particular, the growth of loans to the nonfinancial sector moved down to 3.5 percent, covering a slowdown in loans to both public and private businesses and a virtual stagnation in the growth of household loans.

Liquid investment aggregates rose 9.6 percent, as against 11.4 percent. This change is attributed to slower growth from 2.3 percent to 0.2 percent for treasury bills, from 29 percent to 24.3 percent for equity and diversified UCITS and from 23.6 percent to 22.3 percent for bond UCITS.

Chart 3.11: YoY change in liquid investments and time deposits



3.2 Asset prices

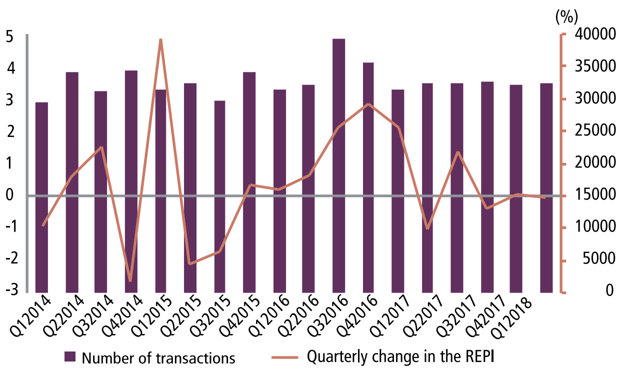
3.2.1 Real estate assets

In the second quarter of 2018, the real estate price index remained stable compared with its level a quarter earlier. By property category, this stagnation covers price decreases of 0.3 percent in residential property and 1.7 percent in commercial property as well as a 1 percent increase in urban land prices.

The number of transactions rose slightly by 0.4 percent, with a 4.2 percent increase in residential property sales and respective declines of 7.2 percent and 9.6 percent in urban land and commercial property sales.

In the major cities, prices showed divergent trends, with respective increases of 2.6 percent and 1.7 percent in Marrakech and Rabat and decreases of 3.8 percent and 1.3 percent in Oujda and Meknes. The number of transactions rose 31.3 percent in Marrakech and 19.6 percent in Rabat, and decreased by 24 percent in Tangier.

Chart 3.12: Change in the REPI and in the number of real estate transactions



Sources : BAM and the National Land Registry and Mapping Agency

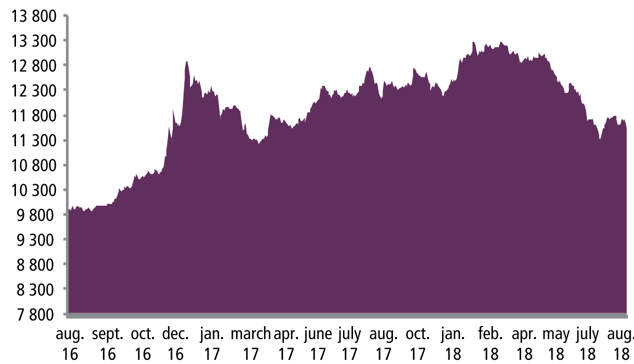
3.2.2 Financial assets

3.2.2.1 Shares

At the end of the second quarter of 2018, the MASI index edged down 9.1 percent, after a rise of 5.4 percent a quarter earlier. This underperformance covered most sector indexes, with decreases of 34.6 percent for "real estate", 12 percent for "insurance", 11.6 percent for "buildings and construction materials", 6.9 percent for "telecommunications" and 6.6 percent for "banks".

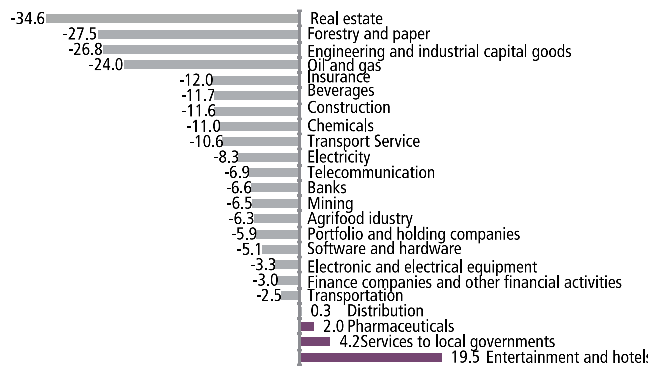
The volume of transactions amounted to 13 billion dirhams in the second quarter of the year, as against 14.8 billion over the same period of the previous year. The central market accounted for 75.4 percent of these transactions, with an average monthly volume of 3.3 billion. Operations on the block market amounted to 1.2 billion dirhams.

Chart 3.13: Daily change in MASI



Source : Casablanca Stock Exchange.

Chart 3.14: Contribution of sectoral indexes in the second quarter 2018 (in%)



Source : Casablanca Stock Exchange.

Under these conditions, market capitalization stood at 605.7 billion at end-June 2018, down 8.3 percent quarter on quarter.

The latest available data point to a slow fall in the MASI to 1.1 percent in July and to 1.7 percent in August and an average transaction volume of 1.7 billion between July and August.

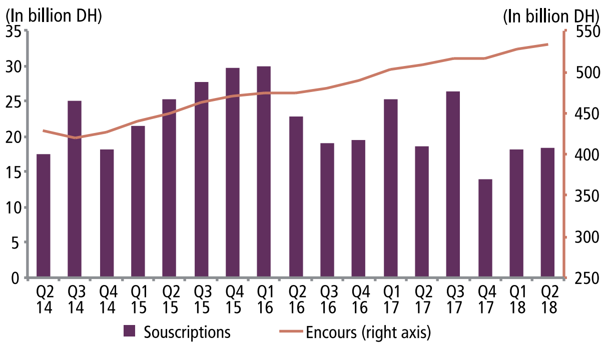
Market capitalization thus stood at 588.9 billion at end-August, down 6.1 percent compared to December 2017.

3.2.2.2 Sovereign debt market

Treasury issues in the domestic market reached 23.1 billion dirhams in the second quarter, showing a virtual stagnation, year on year. 83 percent of these subscriptions concerned medium-term maturities and 13 percent focused on long-term maturities, and the related rates did not change significantly.

The latest available data indicate that Treasury issues amounted to 11.7 billion dirhams in July and 84 percent of them consisted of medium-term maturities and 16 percent of long-term maturities. Considering repayments of 7 billion, outstanding Treasury bills stood at 537.8 billion, up 4.1 percent compared to December 2017.

Chart 3.15: Change in outstanding Treasury bonds



Source : BAM.

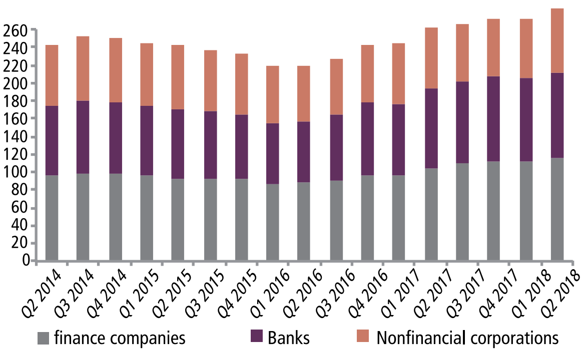
3.2.2.3 Private debt market

In the private debt market, issuances grew by 8.7 billion compared to the previous quarter to 21.5 billion dirhams, of which an amount of 11.9 billion issued by banks.

Issues of nonfinancial businesses grew from 5.4 billion to 7.8 billion dirhams, of which 7 billion as bonds and the rest as commercial papers.

In July, issues amounted to 4.6 billion. Considering repayments, the outstanding private debt amounted to 188.8 billion, up 6.2 percent from December 2017.

Chart 3.16: Change in outstanding private debt per issuer (In billions of dirhams)



Sources : Maroclear and BAM calculations.

3.2.2.4 Mutual fund shares/units

In the second quarter of 2018, subscriptions to mutual fund shares/units showed a quarterly drop of 17.2 percent to 186.8 billion. This trend covers in particular a decline of 29.6 billion for medium and long-term bond UCITS and an increase of 2.5 billion for diversified UCITS.

Taking account of a redemption amount of 196.8 billion and a 1.3 percent decrease in the performance index, UCITS recorded a net outflow of 10 billion, bringing their net assets to 423.8 billion at the end of June, down 13.5 percent, year on year.

4. FISCAL POLICY STANCE

Budget execution in the first eight months of 2018 shows a deficit of 27.8 billion, widening by 1.9 billion from the same period in 2017. Overall spending rose by 2.2 percent, essentially reflecting increases in spending on other goods and services, transfers to local governments and subsidy costs. At the same time, current revenue grew 0.4 percent, reflecting improved tax revenues, despite an 8.5 percent decline in corporate tax receipts and a decrease in nontax revenues, driven by lower donations from GCC countries. The current balance was positive at 5.4 billion, down 2.8 billion from one year to the next, while the positive balance of the Treasury special accounts improved by 1.7 billion to 6 billion.

With a 2.6 billion cut in outstanding expenses, the cash deficit stood at 30.4 billion, easing by 3 billion from the same period in 2017. This need and the negative external net flow of 3.1 billion were covered by domestic resources amounting to 33.6 billion. As a result, direct public debt would have risen by 3.3 percent compared to its December 2017 level. Regarding the Treasury's financing conditions on the auction market, Treasury bill rates fell slightly during the first eight months of 2018 compared to the same period in 2017.

4.1 Current revenues

The Treasury's current revenue increased by 0.4 percent over the first eight months of the year to 164.3 billion, with an execution rate of 62.6 percent compared to the finance law. This development covers an improvement of 2.4 percent to 151.9 billion in tax revenues and a 21.5 percent decrease in nontax receipts to 10.4 billion.

Despite an improvement of 4.1 percent to 28 billion in income tax revenues, proceeds from direct tax fell 2.5 percent to 58.4 billion, driven by an 8.5 percent decline in corporate tax revenue to 28.7 billion. This change is largely attributed to the year-on-year decrease in the March 2018 adjustment installment. Income tax receipts cover a stagnation at 2.7 billion in proceeds from real estate profits and an increase of 2.6 percent to 5.7 billion in revenue from income tax on salaries paid by the Personnel Expenditure Department.

Indirect taxes rose 6.4 percent to 75.9 billion dirhams, mainly reflecting a 7.6 percent increase in VAT receipts to 57.6 billion dirhams. Domestic VAT revenues rose by 10.3 percent to 21.4 billion, taking account of the refund of VAT credits amounting to 3.9 billion, as against 4.5 billion at end-August 2017. Similarly, import VAT revenues rose by 6 percent to 36.2 billion.

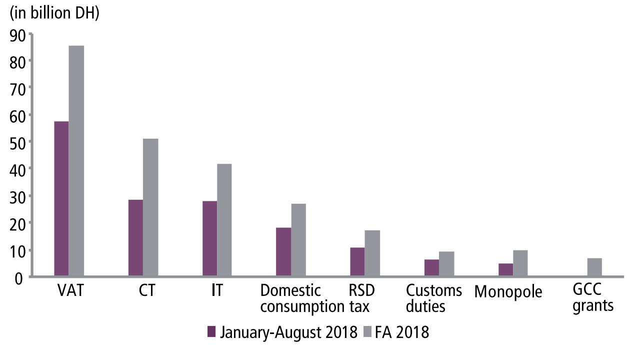
Table 4.1: Change in current revenues (in billions of dirhams)

	Jan.-Aug. 2017	Jan.-Aug. 2018	Change in %	FA 2018	Achievements against the FA (%)
Current revenues	**163.6**	**164.3**	**0.4**	**262.4**	**62.6**
Tax revenues	**148.4**	**151.9**	**2.4**	**237.0**	**64.1**
- Direct taxes	59.8	58.4	-2.5	97.1	60.1
Including CT	31.4	28.7	-8.5	51.2	56.1
I.T	27.0	28.0	4.1	41.7	67.2
- Indirect taxes	71.3	75.9	6.4	112.7	67.3
VAT*	53.6	57.6	7.6	85.5	67.4
DCT	17.8	18.3	3.0	27.3	67.1
- Customs duties	5.7	6.5	12.9	9.7	66.9
- Registration and stamp duties	11.5	11.1	-2.8	17.5	63.6
Nontax revenues*	**13.3**	**10.4**	**-21.5**	**22.1**	**47.1**
- Monopoles	5.4	5.3	-3.0	9.8	53.6
- Other receipts	7.8	5.2	-34.2	12.3	41.9
Including GCC grants	2.5	0.7	-72.6	7.0	9.8
Recettes des CST	**2.0**	**2.0**	**-0.2**	**3.3**	**59.6**

*Taking into account 30 percent of the VAT transferred to local governments.
Sources : Ministry of Economy and Finance (TEFD), VAT reprocessing by BAM.

Domestic consumer tax (DCT) drained a revenue of 18.3 billion, improving by 3 percent, mainly reflecting increases of 7.4 percent in DCT on tobacco to 6.8 billion and 0.5 percent in DCT on energy products to 10.4 billion. Similarly, customs duties grew by 12.

Chart 4.1: Performances of the major revenues compared to the FA



Sources : Ministry of Economy and Finance (TEFD), VAT reprocessing by BAM.
Note :
-VAT : Value added tax - CT : Corporate tax
- IT : Income tax - DCT : Domestic consumption tax
- RSD : Registration and stamp duties - CD : Customs duties

Nontax revenue amounted to 10.4 billion, down 21.5 percent, mainly due to a decline in GCC grants to 687 million, as against 2.5 billion at end-August 2017 and 7 billion programmed in the finance law. Similarly, monopoly revenues dropped by 3 percent to 5.3 billion. They come mainly from Maroc Telecom at 1.45 billion, the National Land Registry and Mapping Agency at 1.25 billion, OCP at 1 billion and Bank Al-Maghrib at 422 million.

4.2 Expenditure

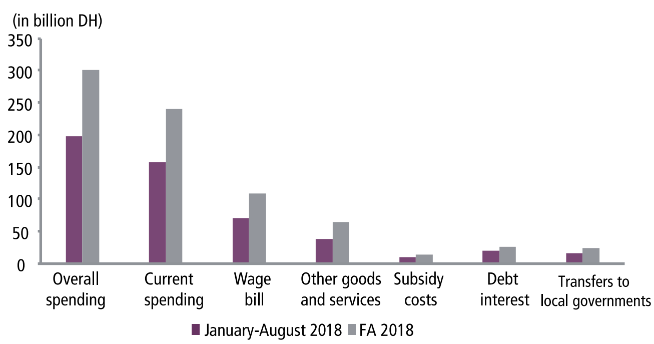
Overall expenditure moved up in the first eight months of the year by 2.2 percent to 198.1 billion, due to an increase of 2.2 percent to 158.9 billion in current expenses and a growth of 1.8 percent in investment sending to 39.3 billion. Spending on goods and services rose by 1.7 percent to 110 billion, reflecting a 3.5 percent increase to 39.5 billion in spending on other goods and services and a rise of 0.7 percent to 70.5 billion in the payroll whose execution rate stood at 64.8 percent compared to the budget law. The change in the latter was attributed to increases of 0.6 percent in the structural payroll and 26.5 percent in back pays. Spending on other goods and services covers increases of 16.3 percent in transfers to public institutions to 15.7 billion and 11.5 percent in those to the Moroccan Pension Fund to 9.7 billion, and a decrease of 5.9 percent in payments to the Treasury special accounts to 1.6 billion.

Table 4.2: Change and execution of public spending (In billions of dirhams)*

	Jan.-Aug. 2017	Jan.-Aug. 2018	Change in %	FA 2018	Achievements against the FA (%)
Overall spending	**193.9**	**198.1**	**2.2**	**301.7**	**65.7**
Current spending	**155.4**	**158.9**	**2.2**	**241.5**	**65.8**
Goods and services	108.1	110.0	1.7	175.0	62.9
Personal	70.0	70.5	0.7	108.9	64.8
Other goods and services	38.1	39.5	3.5	66.1	59.6
Debt interests	20.9	20.4	-2.1	27.1	75.4
Clearing	10.3	11.2	8.3	13.7	81.3
Transfer to local governments	16.1	17.3	7.6	25.6	67.4
Investment	**38.6**	**39.3**	**1.8**	**60.3**	**65.2**

*Taking into account 30 percent of the VAT transferred to local governments.
Sources : Ministry of Economy and Finance (TEFD), VAT reprocessing by BAM.

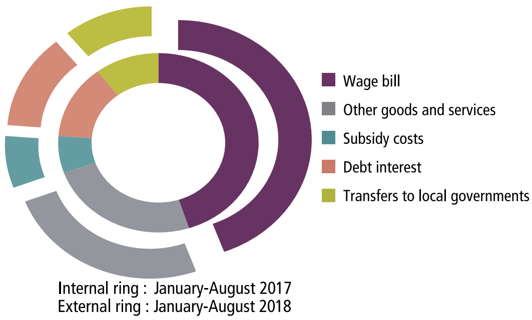
Chart 4.2: spending execution compared to the FA



Sources : Ministry of Economy and Finance (TEFD), VAT reprocessing by BAM.

Debt interest charges fell by 2.1 percent to 20.4 billion, following a decline of 0.3 percent in interest on domestic debt to 18.5 billion and 16.6 percent in interest on external debt to 2 billion.

Chart 4.3: Structure of current spending

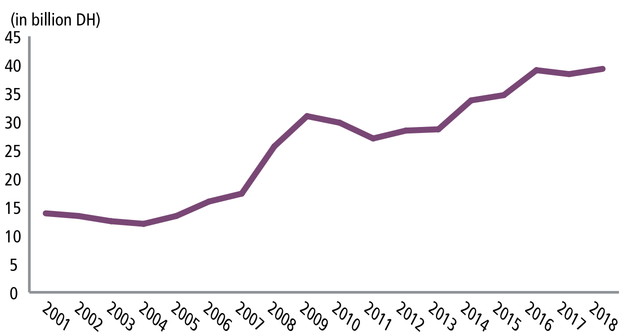


Sources : Ministry of Economy and Finance (TEFD), VAT reprocessing by BAM.

Subsidy costs were up 8.3 percent to 11.2 billion, with an execution rate of 81.3 percent compared to the budget law. According to data from the Subsidy Fund, butane gas subsidies in the first seven months of 2018 stood at 6.5 billion, up 11.3 percent over the same period in 2017, and sugar subsidies almost stabilized at 2 billion.

Investment spending, up 1.8 percent to 39.3 billion, was executed at 65.2 percent compared to the finance law forecast. This trend mainly reflects increases of 2 percent in expenditure by ministries to 24 billion and 1.4 percent in common expenses to 14.1 billion.

Chart 4.4: Investment spending, January to August total

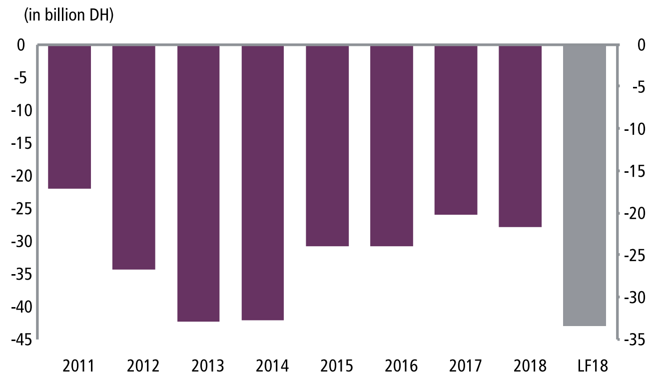


Source : Ministry of Economy and Finance (TEFD).

4.3 Treasury deficit and financing

Considering the change in revenues, expenses and the balance of the Treasury special accounts, the budgetary execution resulted in a deficit of 27.8 billion, widening by 1.9 billion compared to end-August 2017. In addition, the Treasury reduced its outstanding expenses, amounting to 2.6 billion. The cash deficit thus stood at 30.4 billion, easing by 3 billion compared to the same period in 2017.

Chart 4.5: Fiscal balance, January to August total



Source : Ministry of Economy and Finance (TEFD).

The negative external financing flow of 3.1 billion as well as the financing needs were covered by resources, amounting to 33.6 billion dirhams, down 2.1 billion dirhams.

Table 4.3: Absolute gap FA (in billions of dirhams)

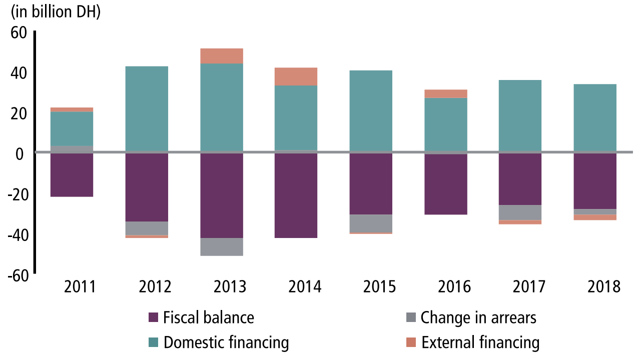
	Jan.-Aug. 2017	Jan.-Aug. 2018	FA 2018	Absolute gap FA/ Jan.-aug. 2018
Current balance	**8.2**	**5.4**	**21.0**	**15.6**
Balance of TSA	4.3	6.0	6.0	0.0
Primary balance	-5.1	-7.4	-6.2	1.2
Fiscal balance	**-26.0**	**-27.8**	**-33.3**	**-5.4**
Change in arrears	-7.4	-2.6	0.0	
Financing requirements	**-33.4**	**-30.4**	**-33.3**	**-2.9**
Domestic financing	35.7	33.6	13.5	-20.0
External financing	-2.3	-3.1	19.8	22.9

Source : Ministry of Economy and Finance (TEFD).

In terms of domestic financing, the use of the auction market concerned a net amount of 22.4 billion, as against 24.5 billion a year earlier. Net subscriptions were mainly made on 2-year notes for 14 billion, 5-year notes for 9.1 billion and 10-year bonds for 8 billion.

At the same time, the main net repayments concerned 52-week bills for 7.2 billion and 26-week bills for 1.1 billion.

Chart 4.6: Fiscal balance and financing , January to August total*



* Privatization receipts, limited and discontinued over time, were included in domestic financing.
Source : Ministry of Economy and Finance (TEFD).

The Treasury's financing conditions on the auction market remain broadly positive for the first eight months of 2018 compared to the same period in 2017. The rates on 5-year notes and 15-year bonds decreased by 3 bps and 19 bps, respectively, while rates on 2-year notes grew by 5 bps. On the other hand, issue rate on 10 years bonds almost stabilized at 3.26 percent.

Table 4.4: Treasury debt outlook (in billions of dirhams)

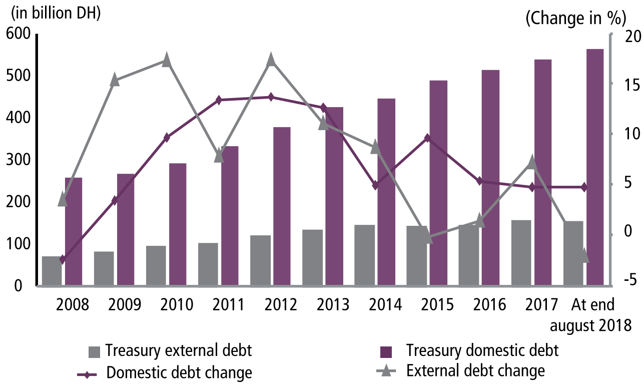
	2013	2014	2015	2016	2017	At end August 2018*
Treasury external debt	**129.8**	**141.1**	**140.8**	**142.8**	**153.1**	**149.9**
Change in %	11.1	8.7	-0.2	1.4	7.2	-2.0
Treasury domestic debt	**424.5**	**445.5**	**488.4**	**514.7**	**539.1**	**564.8**
Change in %	12.6	5.0	9.6	5.4	4.8	4.8
Outstanding direct debt	**554.3**	**586.6**	**629.2**	**657.5**	**692.2**	**714.8**
Change in %	12.3	5.8	7.3	4.5	5.3	3.3

Source : Ministry of Economy and Finance (TEFD).

Concerning debt at end-october 2017, estimates are based on the flows of domestic and external financing.

Under these conditions, direct public debt was up 3.3 percent at end-August 2018 compared to its end-December 2017 level. This trend reflects a 4.8 percent increase in its domestic component and a 2 percent decline in its external component.

Chart 4.7: Treasury debt



Sources : Ministry of Economy and Finance (TEFD), and BAM estimates.

5. DEMAND, SUPPLY AND LABOR MARKET

The latest national accounts data for the first quarter of 2018 show that growth moved down to 3.2 percent from 3.5 percent a year earlier. The agricultural value added slowed down from 14.8 percent to 2.5 percent, while nonagricultural growth accelerated markedly from 2 percent to 3.4 percent. On the demand side, the domestic component contributed 5.1 percentage points, while net exports contributed negatively with 1.9 percentage point.

In view of the latest available infra-annual data, activity would have continued to decelerate compared to 2017, with a rate of around 3.7 percent in the second and third quarters, mainly reflecting slower growth of the agricultural value added. On the other hand, nonagricultural activities would have improved by 2.9 percent over the same period, from 2.8 percent on average a year earlier.

Household final consumption would have increased by an average of 3.4 percent in the second and third quarters, a rate almost unchanged from 2017, due to the continued recovery of nonagricultural activities and a slight improvement in labor market conditions. At the same time, investment would have risen by 5.7 percent, as against an average of 0.7 percent a year earlier. Conversely, the contribution of net external demand to growth was negative.

In the labor market, the national economy created 117 thousand jobs in the second quarter with an increase of 53 thousand jobs in services. Considering a net entry of 97 thousand job-seekers, the unemployment rate fell from 9.3 percent to 9.1 percent nationally, from 14.0 percent to 13.7 percent in the cities and from 3.2 percent to 3 percent in rural areas. Regarding the cost of labor, data for the second quarter show an annual increase of 1.3 percent in the private sector wage index, as against 1.9 percent in nominal terms and a 1.3 percent decrease in real terms, as opposed to a rise of 1.5 percent.

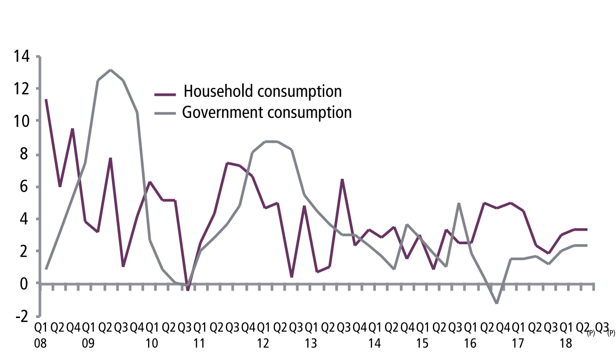
5.1 Domestic demand

5.1.1 Consumption

In the first quarter of 2018, national accounts data show a year-on-year slowdown in household consumption to 3 percent from 5 percent in the same quarter a year earlier. Its contribution to growth moved down from 2.9 percentage points to 1.8 percentage point.

Bank Al-Maghrib's short-term projections of household consumption indicate a growth of around 3.4 percent in the second and third quarters, a pace almost unchanged from 2017, in connection with the continued recovery of nonagricultural activities and the relative improvement in the labor market conditions. This trend is corroborated by the external trade indicators, which show increases of 1 percent in transfers from Moroccan expatriates and 6.6 percent in imports of finished consumer goods. In addition, consumer loans increased at end-July by 5.6 percent, as against 4.7 percent a year earlier. In the same vein, HCP's quarterly household survey indicates that the confidence index improved by 1.5 point to 87.3 points compared to the same quarter of the previous year.

Chart 5.1: Expenses of domestic final consumption (in %)



Sources: HCP, and BAM forecasts.

The growth of general government final consumption accelerated in the first quarter from 1.6 percent to 2 percent. Its pace is expected to hover around 2.4 percent in the second and third quarters, after averaging 1.6 percent a year ago. Indeed, operating expenses rose by 3.8 percent at end-July, compared to a 0.4 percent decrease, following the increase in personnel costs and spending on other goods and services.

5.1.2 Investment

Investment grew by 9.7 percent in the first quarter from 6.2 percent in the same quarter of the previous year. Its contribution to growth stood at 2.9 points from 1.8 point.

In the second and third quarters, investment should accelerate by an average of 5.7 percent, as against 0.7 percent a year earlier. In fact, end-July infra-annual indicators show a 1.8 percent increase in Treasury investments, as against a fall of 1.7 percent, and a recovery of 10.7 percent in loans to real estate developers, as opposed to a decrease of 24.1 percent. In the same vein, end-August preliminary indicators of foreign trade show an increase of 12.5 percent in imports of capital goods, as against a decline of 0.3 percent. The business climate was deemed as ”normal” by nearly two-thirds of the manufacturers surveyed as part of Bank Al-Maghrib’s quarterly survey in industry.

5.2 Foreign demand

Net foreign demand contributed negatively to growth by 1.9 percentage point in the first quarter from 1.5 point a year earlier. Indeed, exports slowed down from 7.3 percent to 6.8 percent in one year. Imports grew faster from 9.4 percent to 9.6 percent.

In the second quarter of 2018, exports would have posted an increase of around 7.5 percent, which should continue in the third quarter, as evidenced by the foreign trade data at end-August. Sales in the automotive, aeronautics and phosphates and derivatives sectors showed significant respective increases of 17.7 percent, 17.2 percent and 17.6 percent. However, imports would have grown by 7.1 percent, as against 5.3 percent, mainly following higher purchases of capital goods and finished products.

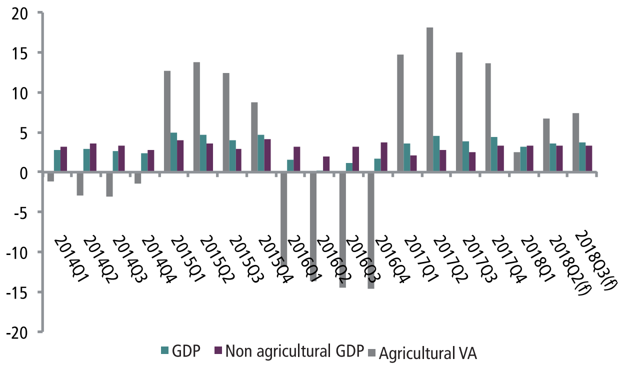
5.3 Overall supply

Economic growth stood at 3.2 percent in the first quarter, compared to 3.5 percent in the same period last year. This slowdown reflects a sharp deceleration of the agricultural value added from 14.8 percent to 2.5 percent, compared with a significant improvement in nonagricultural activities, whose value added accelerated from 2 percent to 3.4 percent. Taxes net of subsidies slowed down slightly from 2.7 percent to 2.2 percent.

In the short term, the economic growth should continue to slow down, with a growth rate of around 3.7 percent in the second and third quarters, compared with an average of 4.2 percent a year earlier. The growth of the agricultural value added is expected to fall from 16.6 percent to 7 percent, following a base effect, and the cereal harvest should reach, according to the Ministry of Agriculture, 103 million quintals, up 7.8 percent compared to 2017.

Nonagricultural activities would continue to improve, albeit at a moderate pace, i.e. 2.9 percent, as against 2.8 percent.

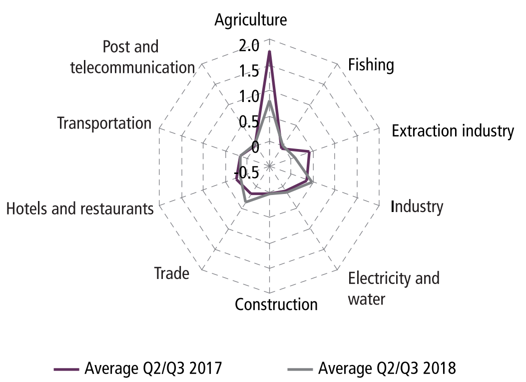
Chart 5.2: GDP per component (chained prices, change in %)



Sources: HCP data, and BAM forecasts.

At the sectoral level, secondary sector activities should slow down in the second and third quarters from 3.5 percent to 2.8 percent, reducing their contribution to growth to 0.7 percentage point. This change would be mainly attributable to a sharp deceleration in the extractive industries from 22.6 percent to 3.6 percent. The construction branch would maintain a low pace not exceeding 1 percent in a context marked by low cement sales. Conversely, the value added of the manufacturing industries and that of the "electricity and water" sector would continue to improve with respective rates of 3.1 percent and 5.3 percent, as against 2.3 percent and 3.3 percent one year ago.

Chart 5.3: Sectoral contribution to growth (in % points)



Sources: HCP data, and BAM forecasts.

In the tertiary sector, activity should evolve at a rate of around 3 percent, from 2.6 percent a year earlier. This trend would reflect an acceleration of activity in the "trade" sector from 2 percent to 4.7 percent and the postal and telecommunications sector from 0.6 percent to 2.5 percent. However, the pace should move down from 12 percent to 5.9 percent in the "hotels and restaurants" sector and from 4 percent to 3.7 percent in transport services.

5.4 Labor market and output capacity

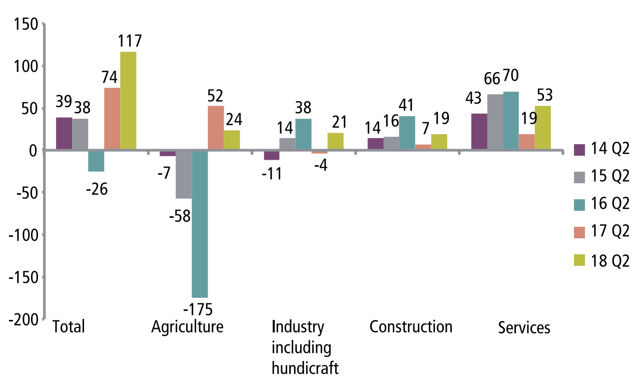
5.4.1 Activity and employment

Labor market conditions were characterized in the second quarter by a further increase of 0.8 percent in the labor force aged 15 and over to 12.2 million, with a rise of 0.9 percent in cities and 0.6 percent in rural areas. Considering a 1.5 percent increase in the working-age population, the participation rate continued to decline from 47.3 percent to 47 percent. By area of residence, it decreased by 0.7 point to 41.6 percent in urban areas and grew by 0.7 point to 56.7 percent in rural areas.

At the same time, the national economy created 117 thousand jobs, of which 75 thousand in urban areas. The employed labor force thus grew by 1.1 percent.

At the sectoral level, services created 53 thousand jobs, agriculture 24 thousand, industry including handicrafts 21 thousand and construction 19 thousand jobs.

Chart 5.4: Job creation by sector (in thousands)



Source : HCP.

5.4.2 Unemployment and underemployment

The unemployed labor force fell by 1.9 percent to nearly 1.1 million people. Given the change in the labor force, the unemployment rate fell from 9.3 percent to 9.1 percent nationally, from 14.0 percent to 13.7 percent in urban areas and from 3.2 percent to 3 percent in rural areas. However, this change did not affect young urban residents aged 15 to 24, whose rate moved up from 40.3 percent to 40.5 percent.

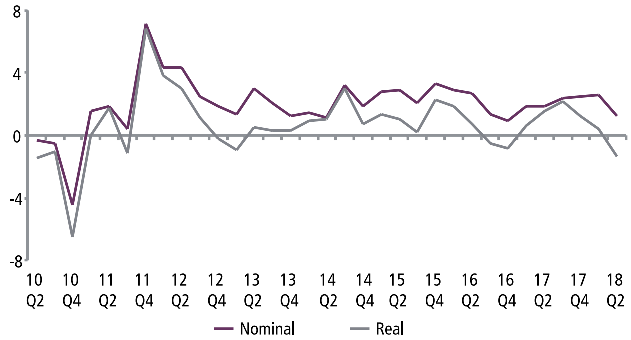
The underemployment rate[1] fell from 9.9 percent to 9.6 percent nationally, from 9.1 percent to 8.7 percent in the cities and from 10.8 percent to 10.6 percent in rural areas.

5.4.3 Productivity and wages

Growth of the apparent labor productivity[2] in nonagricultural activities decelerated from 2.6 percent to 1.5 percent. This change was due to a slight slowdown from 3 percent to 2.9 percent in the value added and an acceleration from 0.3 percent to 1.4 percent in the scale of employment.

In terms of wage costs, data for the second quarter of the year show a year-on-year increase of 1.3 percent in the average wage index, calculated on the basis of CNSS data, as against 1.9 percent in nominal terms and a decline of 1.3 percent after an increase of 1.5 percent in real terms.

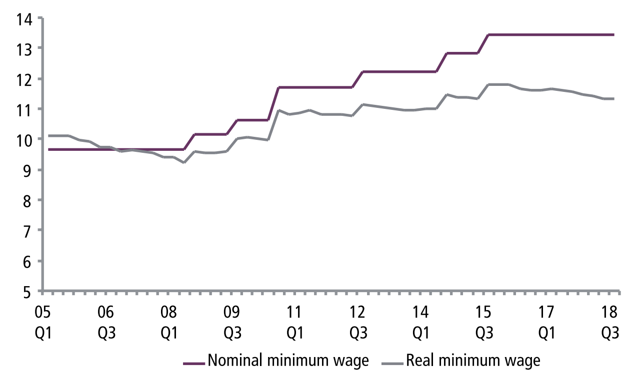
Chart 5.5: Private sector average wage index (YoY change in %)



Sources: CNSS, and BAM calculations.

The hourly guaranteed minimum industrial wage (SMIG) remained in the second quarter of 2018 at 13.46 dh/h in nominal terms. Taking account of a 2.6 percent increase in the consumer price index, the SMIG would have fallen, in real terms, by 2.5 percent, year on year, and should decrease by 2 percent in the third quarter of 2018.

Chart 5.6: Hourly minimum wages in nominal and real terms (in DH/h)



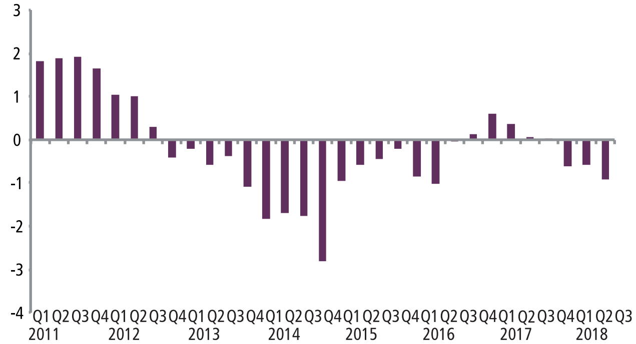
Sources: Ministry of Employment and Social Affairs, and BAM calculations.

Against this backdrop, the output-gap should remain negative in the second and third quarters of 2018.

1 The underemployed population includes persons who worked: (i) during the reference week less than 48 hours but are willing to work additional hours and are available to do so, or (ii) more than the threshold and who are looking for another job or are willing to change their job because of a mismatch with their training or qualification or insufficient income

2 Measured as the ratio of the nonagricultural value added to the employed labor force excluding agriculture.

Chart 5.7: Overall output gap (in %)



Source: BAM estimates based on HCP data.

Table 5.1 : Labor market main indicators

		Q2 2017	Q2 2018
Participation rate (%)		**47.3**	**47.0**
Urban		42.3	41.6
Rural		56.0	56.7
Unemployment rate (%)		**9.3**	**9.1**
Youth aged between 15 and 24 years old		23.5	23.1
Urban		14.0	13.7
Youth aged between 15 and 24 years old		40.3	40.5
Rural		3.2	3.0
Job creation (in thousands)		116	117
Urban		77	75
Rural		39	42
Sectors			
- Agriculture		52	24
- Industrie y compris l'artisanat		-4	21
- BTP		7	19
- Services		19	53
Nonagricultural apparent productivity (change in %)		**2.6**	**1.5**
Average wage index (change in %)	**Nominal**	**1.9**	**1.3**
	Real	**1.5**	**-1.3**

Sources: HPC, CNSS and BAM calculations.

6. RECENT INFLATION TRENDS

In line with the forecasts published in the latest monetary policy report, inflation accelerated significantly in the second quarter of 2018, averaging 2.6 percent from 2 percent a quarter earlier. This upward trend, which started in the third quarter of 2017, reversed in July, as inflation fell back to 2.1 percent in July and 1.7 percent in August, mainly due to lower volatile food prices. These prices posted an average increase of 3.1 percent in the last two months, as against 9.1 percent in the second quarter. The growth of prices for regulated goods decelerated from 2.9 percent to 2.7 percent, as the effect of the previous increase in the DCT on certain tobacco categories dissipated. Core inflation, which reflects the underlying price trend, averaged 1.1 percent, a rate unchanged from the previous quarter.

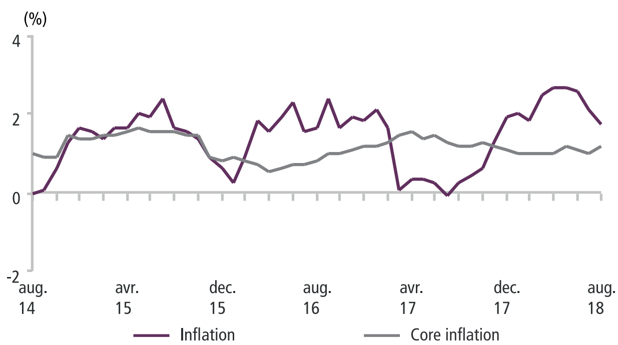
Inflation should thus end the third quarter with an average of 2 percent and its core component would be around 1 percent.

6.1. Inflation trends

After standing at 2.6 percent in the second quarter of 2018, inflation decelerated to 2.1 percent in July and 1.7 percent in August.

This slowdown is mainly attributed to volatile food prices, which rose by only 1.5 percent, as opposed to 4.7 percent in July and 9.1 percent in the second quarter. The growth of prices for regulated goods slowed from 2.9 percent in June to 2.7 percent in July and August. Core inflation averaged 1.1 percent over the same period, a pace unchanged from the second quarter.

Chart 6.1: Headline inflation and core inflation, YoY



Sources: HCP and BAM calculations.

Table 6.1: Change in inflation and its components

(In %)	MoM			YoY		
	june 18	july 18	aug. 18	june 18	july 18	aug. 18
Headline inflation	**0.2**	**-0.9**	**-0.1**	**2.5**	**2.1**	**1.7**
- Volatile food prices	0.3	-6.3	-1.0	7.8	4.7	1.5
- Fuels and lubricants	1.0	-0.2	0.0	9.2	11.8	9.3
- Administered prices	0.0	0.0	0.0	2.9	2.7	2.7
Core inflation	**0.3**	**0**	**0**	**1.1**	**1**	**1.2**
- Food products	0.3	-0.4	0.2	1.1	0.8	1.3
- Clothing and footwear	0.5	-0.2	0.0	1.0	0.9	1.0
- Housing, water, gas, electricity and other fuels[1]	0.1	0.3	0.3	1.6	1.7	1.9
- Furnishings, household equipment and routine house maintenance	0.1	0.5	-0.1	1.0	1.4	1.2
- Health[1]	0.0	0.0	0.0	0.0	0.2	0.4
- Transportation[2]	0.4	0.0	0.0	0.2	0.2	0.1
- Communication	0.0	-0.3	0.0	0	-0.3	-0.3
- Entertainment and culture[1]	0.0	0.1	-0.1	1.5	1.6	1.4
- Education	0.0	0.0	0.0	2.0	2.0	2.0
- Restaurants and hotels	0.4	0.2	-0.2	2.2	2.3	1.6
- Miscellaneous goods and services [1]	0.0	0.1	0	1.6	1.8	1.7

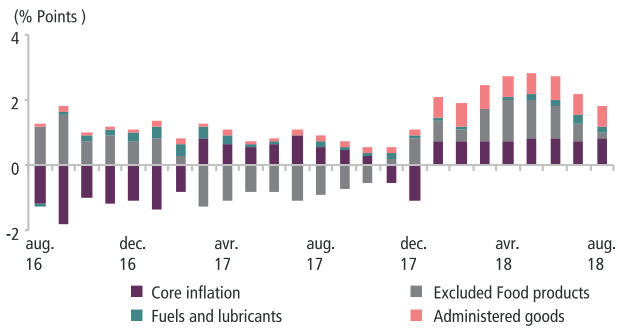
1 Excluding administered goods.
2 Excluding fuels and lubricants and regulated products.
Sources: HCP, and BAM calculations.

6.1.1. Prices of goods excluded from core inflation

The rising demand for fresh foodstuffs, usually registered when approaching and during the month of Ramadan, resulted in a significant increase in volatile food prices in the second quarter of 2018. Indeed, these prices grew by 9.1 percent during the second quarter, mainly due to higher prices for fresh fruits and fresh fish.

Since July, their growth pace has been markedly slowing down, in connection with the improved supply of certain fresh vegetables and the mitigation of the effect of the previous rise in demand for a few fresh products.

Chart 6.2: Contribution of the prices of major CPI items to inflation, YoY

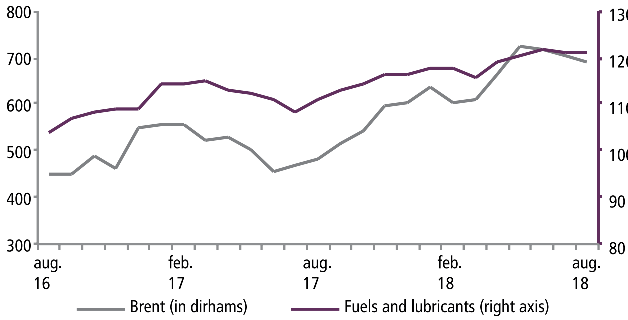


Sources: HCP, and BAM calculations.

In the absence of new regulatory decisions, the growth of prices for regulated goods slowed down slightly in July and August to 2.7 percent from 2.9 percent in the second quarter, due to the dissipation of the effects of the July 2017 increase in the DCT on certain tobacco categories.

However, fuel and lubricant prices grew by an average of 10.5 percent from 7 percent in the second quarter.

Chart 6.3: Change in international prices of Brent and the price index of fuels and lubricants



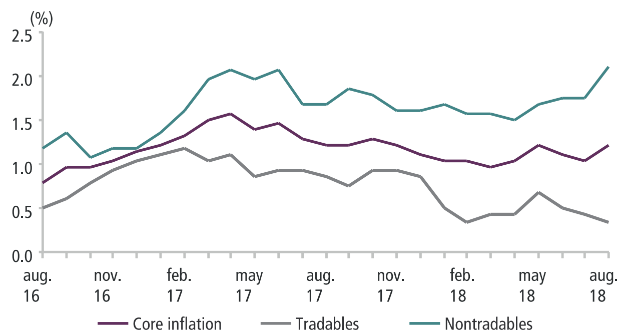
Sources: World Bank, HCP, and BAM calculations.

6.1.2. Core inflation

In July and August, core inflation remained on average at the same pace recorded in the second quarter, or 1.1 percent. Likewise, the increase in food products included in it remained at 1 percent on average over the same period.

The breakdown of the CPIX basket shows slower inflation of tradable goods, offset by faster inflation of nontradables.

Chart 6.4: YoY change in the price indexes of tradables and nontradables



Sources: HCP, and BAM calculations.

Indeed, the rise in prices of tradable goods was limited to 0.3 percent on average, as against 0.6 percent in the second quarter, in conjunction with slower growth of "oils" prices from 1.4 percent to 1 percent and that of "oils and fats" from 12.8 percent to 9.5 percent as well as a 1.5 percent fall in "dry legumes" prices, after a rise of 4.4 percent in the previous quarter.

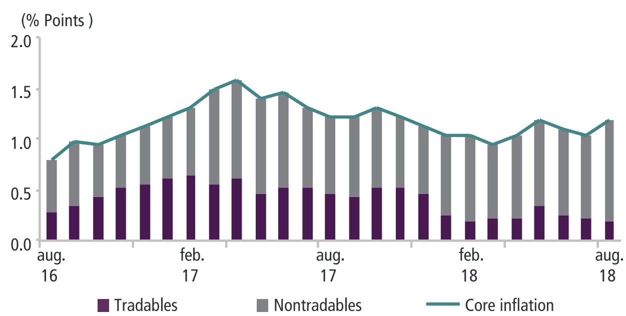
Table 6.2: Change in the price indexes of tradables and nontradables

(In %)	Monthly change			YoY change		
	june 18	july 18	aug. 18	june 18	july 18	aug. 18
Tradables	0.0	-0.1	-0.2	0.5	0.4	0.3
Nontradables	0.4	-0.1	0.4	1.7	1.7	2.1
Core inflation	0.3	0.0	0.0	1.1	1.0	1.2

Sources: HCP, and BAM calculations.

However, prices of nontradables grew by 1.9 percent on average, slightly faster than in the past quarter.

Chart 6.5: Contribution of tradables and nontradables to core inflation, in % points



Sources: HCP, and BAM calculations.

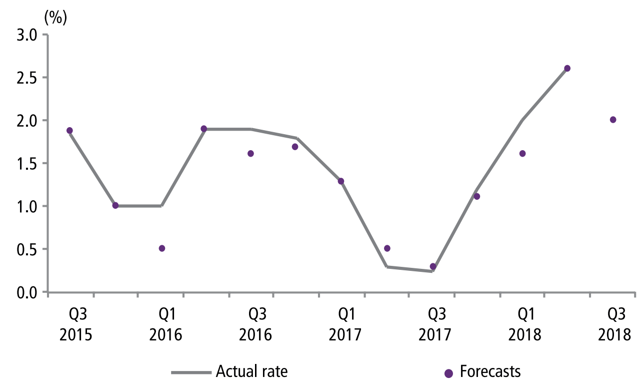
6.2. Short-term outlook for inflation

In the third quarter 2018, the upward trend in inflation is expected to reverse. Indeed, inflation should be around 2 percent, driven mainly by the expected sharp downturn in the growth of volatile food prices. This growth should fall from 9.1 percent to 3.9 percent, reflecting the mitigation of the effect of the one-off increase in demand and improvement in the supply of certain products.

Core inflation, which reflects the underlying inflation trend, should be limited to 1 percent in the next quarter. The growth of prices for regulated goods should slow down to 2.7 percent, as the effects of the July 2017 increase in the DCT on certain tobacco categories would continue to dissipate.

On the other hand, fuel and lubricant prices would register a rise of 9 percent, as against 7 percent a quarter before.

Chart 6.6: Inflation short-term forecasts and actual rates

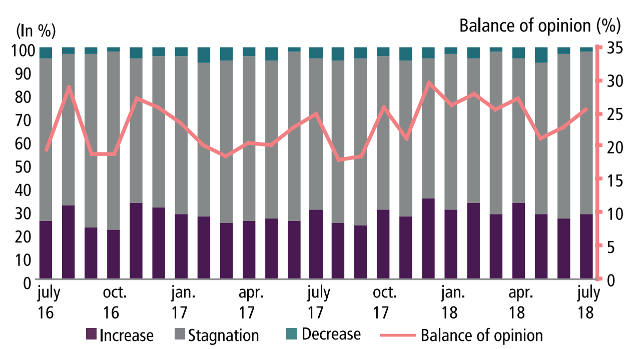


Source: BAM.

6.3. Inflation expectations

The findings of Bank Al-Maghrib's business survey in industry for August 2018 indicate that 28 percent of surveyed manufacturers expect an increase in inflation over the next three months, while only 2 percent anticipate a decline and 70 percent predict stagnation. The balance of opinion stood at 25 percent.

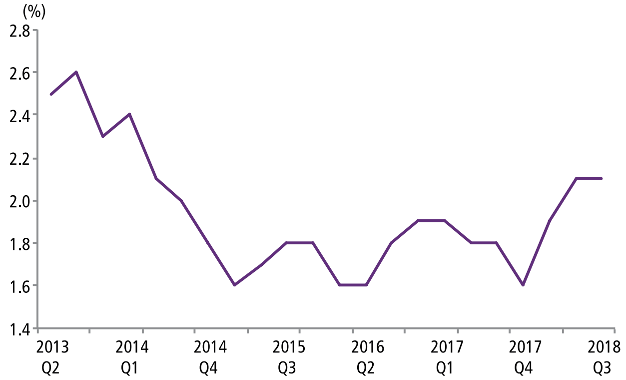
Chart 6.7: Three-month inflation expectations by corporate managers



Source: BAM's monthly business survey.

In addition, Bank Al-Maghrib's inflation expectations survey for the third quarter 2018 show that financial experts anticipate a 2.1 percent inflation over the next eight quarters, which is unchanged from the last quarter.

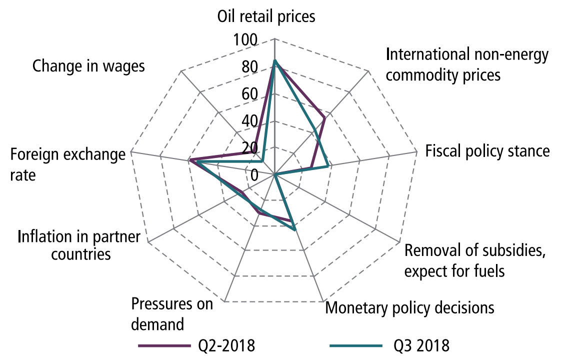
Chart 6.8: Inflation expectations by financial experts*



Source: BAM's quarterly survey on inflation expectations.
* From the second quarter of 2016, the ecpectation horizon increased from 6 to 8 quarters.

These experts believe that changes in prices at the pump and the exchange rate as well as monetary policy decisions and fiscal policy stance would have a significant influence on the future inflation trend

Chart 6.9: Determinants of the future trend in inflation as expected by financial experts

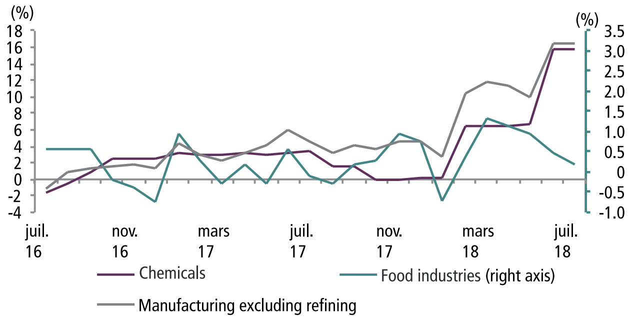


Source: BAM's Quarterly Survey on Inflation Expectations.

6.4. Import and producer prices

After their small increase in 2017, producer prices of manufacturing industries excluding refining were tilted to the upside, with a faster pace of 3.2 percent in July from 2.4 percent in the second quarter and 1.5 percent in the first quarter. This acceleration is mainly driven by a 15.7 percent increase in July in producer prices in the chemical industry, from 9.6 percent. The trend in industrial producer prices is also attributable, but to a lesser extent, to the gradual increase in producer prices in the textile manufacturing industries, since the beginning of the year, reaching 2.5 percent in July from 1.8 percent on average in the second quarter. Similarly, the rise in producer prices in the electrical equipment manufacturing sector remained high at 8.8 percent since January 2018 and contributed significantly to the momentum of producer prices.

Chart 6.10: YoY change major import price indexes



Sources: Foreign Exchange Office, and BAM calculations.

7. MEDIUM-TERM OUTLOOK

Summary

The global economy would continue to grow at a brisk pace in 2018, before slowing down in 2019. However, the outlook remains surrounded by significant risks, particularly due to the intensification of the trade war between the United States and some of its partners, the persistence of uncertainties regarding the Brexit terms and the pressures on the currencies of some emerging economies.

In the advanced countries, activity in the United States would maintain its vigor in 2018, thanks to tax measures, before decelerating in 2019, notably owing to the dissipation of the effects of these measures and the continued normalization of the Fed's monetary policy. In the euro area, economic activity should register some moderation over the medium term, partly impacted by uncertainties in global trade relations and the expected tightening of monetary conditions.

Risks should also weigh on the economic outlook in emerging countries. In 2018 in particular, growth in Brazil is anticipated to improve less than expected and would continue to be supported in Russia mainly by the high levels of world oil prices. The Chinese economy would remain resilient, thanks to accommodative budgetary and monetary policies, while continuing to decelerate due to the economic rebalancing policy.

In commodity markets, the upward trend in oil prices should reverse in 2019. Food prices are forecast to fall slightly over the medium term.

Under these conditions and particularly considering the consolidation of domestic demand, inflation should stand in the medium term at a level close to the Fed target in the United States and would be in the euro area lower than the ECB's level.

Nationally, export momentum would continue in the medium term, driven by the continued performance of phosphates and derivatives in 2018 and a significant increase in automotive sales in the medium term, particularly because of the start of production of the Peugeot plant, expected in 2019. At the same time, growth of imports should accelerate in 2018, mainly due to higher energy bill, before slowing down in 2019. Travel receipts and transfers from Moroccan expatriates should remain in 2018 close to their 2017 levels, before recording increases in 2019. Against this backdrop, assuming donations from GCC partners amounting to 4.8 billion dirhams in 2018 and 2.1 billion in 2019, the current account deficit would widen to 4 percent of GDP in 2018 and fall back to 3.7 percent in 2019. Regarding FDI, the assumption of inflows equaling 3.6 percent of GDP in 2018 and 2019 were maintained.

Under these conditions, the net international reserves (NIRs) would stabilize almost at 240.8 billion dirhams at the end of 2018 and reach 252.3 billion at the end of 2019. Thus, they would cover 5 months and 10 days of imports of goods and services and 5 months and 18 days, respectively.

Monetary conditions would remain broadly appropriate. In particular, the real effective exchange rate (REER) is expected to continue to depreciate in 2018, although at a slower pace than expected in June due to the larger-than-expected depreciation of currencies in some emerging economies, notably Turkey. In 2019, the REER should stabilize, as the nominal appreciation of the dirham in effective terms should be offset by a domestic inflation lower than that of partners and competitors. Growth of lending to the nonfinancial sector should remain moderate, with projected rates of 4 percent in 2018 and 4.5 percent in 2019.

In terms of public finance, the budget deficit was revised upwards to 3.7 percent of GDP in 2018. It should move down to 3.3 percent of GDP in 2019, due to controlled spending and revenue mobilization efforts.

National growth would slow from 4.1 percent in 2017 to 3.5 percent in 2018, reflecting a deceleration from 15.4 percent to 5.1 percent in the agricultural value added, while nonagricultural activities should continue to recover, albeit at a moderate pace of 3.3 percent from 2.7 percent. On the demand side, this trend covers a stronger domestic demand and a negative contribution from net exports. In 2019, growth would continue to slow down to 3.1 percent, covering a decline of 1.6 percent in the agricultural value added, assuming a return to a normal crop year, and a further recovery of nonagricultural activities whose value added would grow by 3.7 percent.

In this context, inflation should accelerate from 0.7 percent in 2017 to 2.1 percent in 2018, reflecting significantly high prices for goods excluded from its core component, before falling back to 1.2 percent in 2019. However, its underlying trend should decelerate to 1 percent in 2018, particularly in connection with the slow growth of prices of certain foodstuffs observed in the first eight months of the year, before rising to 1.2 percent in 2019.

7.1 Underlying assumptions

Strength of the global economy, despite steeper downside risks to its outlook

The global economy would continue to grow at a steady pace in 2018, before slowing down in 2019. However, the downside risks increased significantly, mainly due to the intensification of the trade war between the United States and some of its partners, the persistence of uncertainties regarding Brexit terms and pressures on the currencies of some emerging economies.

After rising to 2.2 percent in 2017, growth would accelerate in the United States to 2.8 percent in 2018, benefiting particularly from fiscal measures, before slowing to close to 2 percent in 2019, mainly due to the dissipation of the effects of these measures and the further normalization of the Fed's monetary policy. In addition, the robustness of the labor market should continue, with unemployment rates remaining below their equilibrium level. On the other hand, growth in the euro area would be somewhat moderate, falling from 2.5 percent to 2.1 percent in 2018 and to 1.7 percent in 2019, impacted by uncertainties surrounding trends in world trade, political tensions in some member countries and the expected tightening of monetary conditions. However, labor market conditions are likely to remain favorable, with the unemployment rate falling to 8.4 percent in 2018 and 2019.

For emerging countries, the trade war, political tensions and pressures on their currencies should weigh on the prospects for their growth. In 2018 in particular, growth in Brazil should improve less than expected, impacted by road transport strikes, while in Russia it would continue to be supported mainly by high levels of world oil prices. The Chinese economy should remain resilient against trade tensions with the United States and would record a growth close to the target of its Government in 2018, thanks to the accommodative stance of monetary and fiscal policies. However, it would continue to decelerate, owing to the economic rebalancing policy.

Chart 7.1: Growth in the euro area

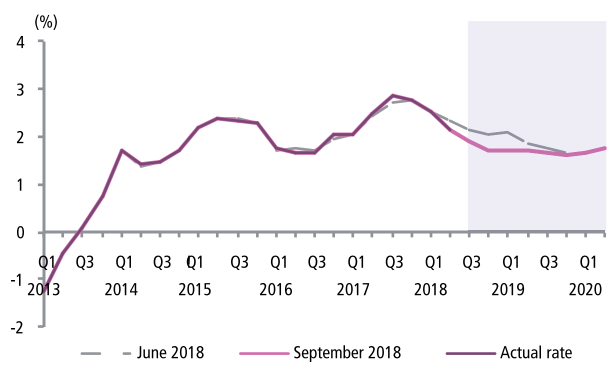
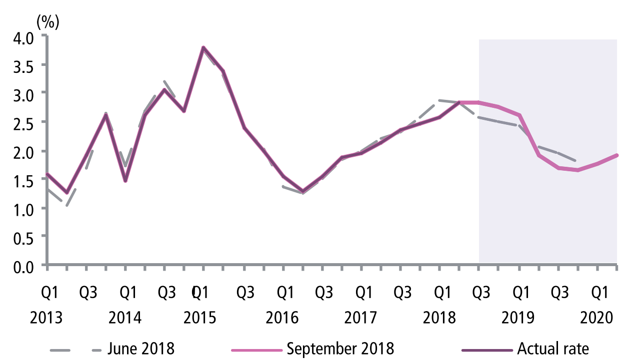


Chart 7.2: Growth in the USA



Source: GPMN[1] forecasts of August 2018.

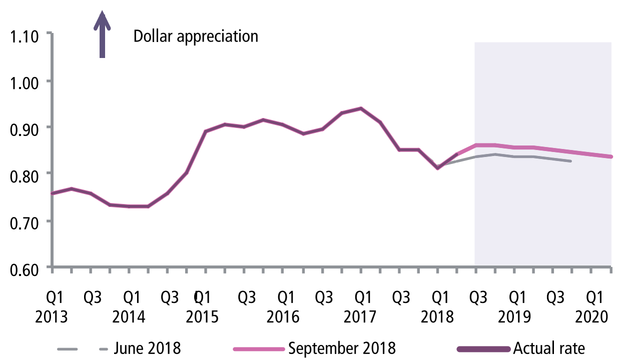
1 Global Projection Model Network.

Rising dollar against the euro

The euro continued to depreciate against the dollar since April 2018, mainly due to the moderate outlook for growth in the euro area and political instability in some member countries. In addition, several other factors supported the dollar, mainly the continued normalization of the Fed's monetary policy, strength of US economic activity and rising risk aversion due to the escalation of global trade tensions. Taking these developments into account, the medium-term forecasts of the euro/dollar parity were slightly revised in favor of the dollar.

At the same time and albeit at contrasting paces, the central banks of the major advanced economies tend to normalize their monetary policies. In particular, the ECB reiterated in September that it will end its net asset purchases at the end of December 2018, if the data confirm its medium-term inflation outlook, and that it will keep rates at their present levels, at least through the summer of 2019 and for as long as necessary to ensure a sustained adjustment of inflation. Also, in order to face the risk of overheating of the economy, the FED would continue to normalize its monetary policy, through a continued increase in the federal funds rates and the gradual reduction of its balance sheet.

Chart 7.3: EUR/ USD exchange rate



Source: GPMN forecasts of August 2018.

Higher energy prices in 2018 and expected decline in 2019

Developments in the oil market were marked by high volatility in recent months, against the backdrop of increased risks of disruption in global supply. Indeed, despite the agreement of the OPEC countries on a rise in production, heightened geopolitical tensions and reinstatement of sanctions on Iran put upward pressure on Brent prices. They averaged $71.5/bl in the first eight months of 2018 and should average $69.8/bl for the year as a whole, which is an upward revision of $2.7 compared to the June report. In 2019, prices should fall to $63.8/bl, combined with an increase in production, particularly in the United States, and the expected deceleration of global economy. In the fertilizer market, the World Bank's latest April projections point to a rise in the price for DAP, TSP in 2018 and, to a lesser extent, for crude phosphate, which is expected to moderate in 2019. World food prices would show slight declines over the forecast horizon.

Under these conditions and particularly considering the consolidation of domestic demand, inflation in the United States should stand over the medium term at a level close to the Fed target of 2.5 percent in 2018 and 2.2 percent in 2019. In the euro area, it would remain below the ECB's target, with projected rates of 1.7 percent in 2018 and 1.4 percent in 2019.

Chart 7.4: Food commodity price index (yoy change)

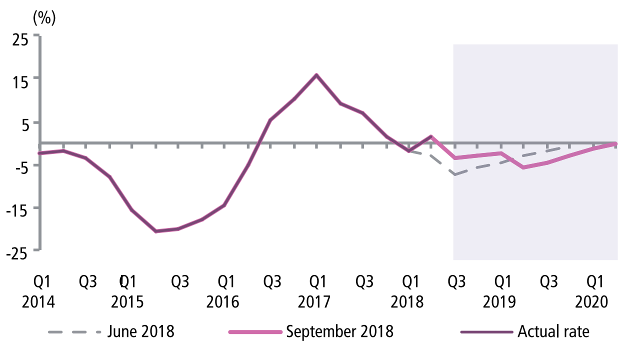


Chart 7.5: Crude oil price

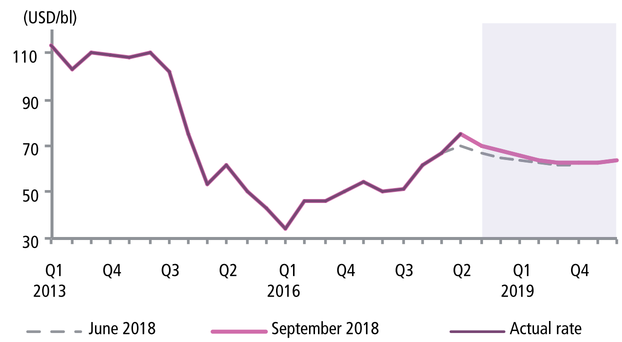


Chart 7.6: Inflation in the euro area

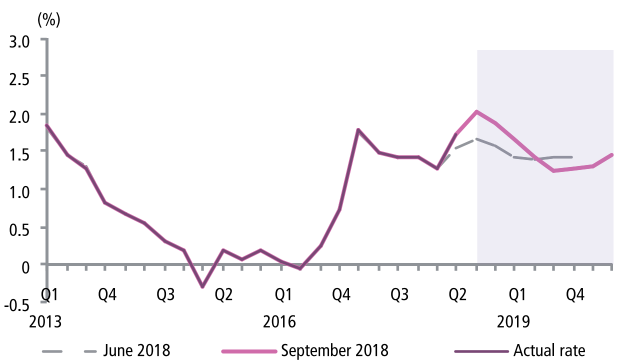
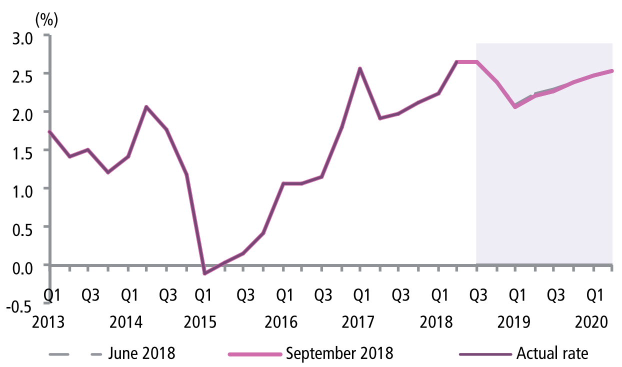


Chart 7.7: Inflation in the United states



Source: GPMN forecasts of August 2018.

Cereal production of 103 million quintals in 2018

Nationally, cereal production for the 2017-2018 crop year stood at 103 million quintals, compared to 95.6 million quintals a year earlier, up 7.8 percent compared to 2.7 percent assumed in June. At the same time, the forecast for the non-cereals component was slightly revised downwards, based on the lower-than-expected output of certain crops, namely fruit trees, livestock, legumes and sugar crops.

In 2019, a cereal production of 70 million quintals is assumed.

Budget deficit above 3 percent in the medium term

The budget deficit is expected to stand at 3.7 percent of GDP compared with 3.4 percent predicted in June. This adjustment reflects a downward revision of tax revenues and the assumption of donations from GCC countries. At the same time, expenses were adjusted upwards, incorporating mainly the new assumptions relating to oil prices and the exchange rate.

In 2019, as a result of continuing efforts to control expenses and mobilize revenues, the deficit should fall back to 3.3 percent of GDP.

7.2 Macroeconomic projections

Current account deficit to widen in 2018 and ease in 2019

The current account deficit should widen from 3.6 percent of GDP in 2017 to 4 percent of GDP in 2018, mainly due to high energy bill. In 2019, it should move down to 3.7 percent of GDP, with particularly the expectedly faster car manufacturing sales.

After a 10.1 percent increase in 2017, exports would increase by 8.2 percent in 2018 and 6.8 percent in 2019, mainly driven by continued performance in the automotive sector sales, with the expected start-up of production in the Peugeot plant in 2019, and by the rise in phosphates and derivatives sales, particularly in 2018. Growth of imports should accelerate from 6.5 percent in 2017 to 7.3 percent in 2018, before slowing down to 3.4 percent in 2019, reflecting changes in the energy bill. Travel receipts and remittances from Moroccan expatriates are projected to remain in 2018 at levels close to those of 2017 and to increase by almost 4 percent in 2019.

Concerning donations from GCC countries, an inflow of 4.8 billion is assumed in 2018 and 2.1 billion in 2019. Regarding FDI, inflows equaling 3.6 percent of GDP in 2018 and 2019 were forecast.

Under these conditions, the NIRs should almost stabilize at nearly 240.8 billion dirhams at the end of 2018 and would reach 252.3 billion at the end of 2019. They cover 5 months and 10 days of imports of goods and services and 5 months and 18 days, respectively.

Table 7.1: Main components of the balance of payments

	Actual rates						Forecasts		Gap (Sept./June)	
	2012	2013	2014	2015	2016	2017	2018	2019	2018	2019
Exports of goods* (change in %)	5.7	0.3	8.3	8.6	3.5	10.1	8.2	6.8	2.4	-0.2
Imports of goods* (change in %)	8.2	-0.8	2.0	-4.9	10.3	6.5	7.3	3.4	0.1	-0.3
Travel receipts (change in %)	-1.8	-0.4	7.7	-1.4	5.0	11.9	0.5	4.0	-7.5	0.0
Expatriate remittances (change in %)	0.6	-1.5	-0.8	4.8	4.0	5.7	1.0	4.1	-5.0	0.0
Current account balance (% of GDP)	**-9.5**	**-7.7**	**-6.0**	**-2.1**	**-4.2**	**-3.6**	**-4.0**	**-3.7**	**-0.1**	**-0.1**
Net international reserves in months of goods and services' imports	**4.0**	**4.2**	**5.4**	**6.0**	**6.2**	**5.6**	**5.3**	**5.6**	**-0.5**	**0.0**

* From Foreign trade perspective
Sources: Foreign Exchange Office and BAM forecasts.

Appropriate monetary conditions and continued moderation of growth of lending to the nonfinancial sector

The depreciation of the real effective exchange rate (REER) should continue in 2018, although at a pace slower than expected in June due to the larger-than-expected depreciation of the currencies of some emerging economies, notably the Turkish lira. In 2019, the REER would stabilize, as the dirham's nominal appreciation in effective terms should be offset by a domestic inflation lower than that of partners and competitors.

Given the revision of the net international reserves forecasts and the significantly high currency in circulation, the liquidity shortage should widen to 56.9 billion dirhams at the end of 2018 and should almost stagnate at 56.4 billion by the end of 2019. Bank lending to the nonfinancial sector would end the year with a growth of 4 percent and increase by 4.5 percent in 2019. Under these conditions and considering the change in the other counterparts of the money supply, the M3 aggregate growth should decelerate to 3.7 percent in 2018 before accelerating to 4.8 percent in 2019.

Table 7.2: Money supply and bank lending

	Actual rates				Forecasts		Gap (Sept/june)	
	2014	2015	2016	2017	2018	2019	2018	2019
Bank lending to the nonfinancial sector (change in %)	3.8	0.3	3.9	3.8	4.0	4.5	0.0	0.0
M3 (change in %)	6.2	5.7	4.7	5.5	3.7	4.8	-1.5	0.6
Liquidity surplus or deficit, in billion dirhams	-40.6	-16.5	-14.7	-40.9	-56.9	-56.4	-17.1	3.2

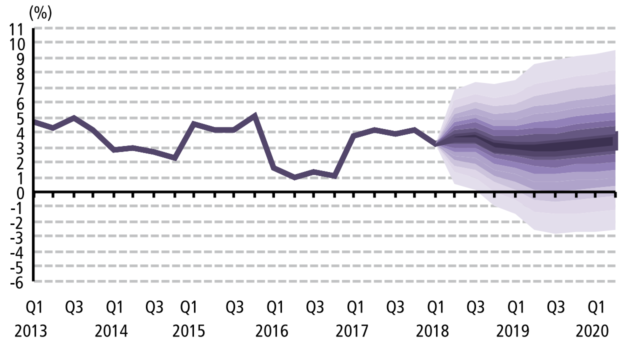
Continued slow recovery of nonagricultural activities

Taking advantage of a good crop year for the second consecutive year, the national growth should stand at 3.5 percent in 2018, from 4.1 percent in 2017. This trend covers a deceleration from 15.4 percent to 5.1 percent in the agricultural value added, which is a slight downward revision compared to June, and a continued recovery of nonagricultural activities whose value added rose by 3.3 percent, as against 2.7 percent a year earlier.

This trend is expected to translate into a stronger domestic demand, driven mainly by investment, which should maintain a steady pace of growth, in conjunction with the expected increase in imports of capital goods. On the other hand, growth of household final consumption would slow down. The contribution of net exports to growth should be negative, reflecting the continued momentum of imports of goods and services. Exports, although decelerating, would maintain a steady growth, benefiting particularly from the uptrend of the automotive sector.

In 2019, economic activity would continue to slow down with growth of 3.1 percent, reflecting a 1.6 percent decline in the agricultural value added, assuming a return to a normal crop year, while nonagricultural activities should continue to improve, as their value added is forecast to rise by 3.7 percent. By demand component, this development reflects a decline in the positive contribution of domestic demand, particularly due to the expected slowdown in household final consumption, which is particularly attributed to a decline in farm incomes. At the same time, the negative contribution from net exports should ease, as a result of a slower growth of imports. Exports should remain dynamic, particularly in connection with the start-up of the Peugeot plant.

Chart 7.8: Growth outlook over the forecast horizon (Q2 2018 - Q2 2020), (YoY)*



* Uncertainty surrounding the central forecast with confidence intervals ranging between 10 percent and 90 percent.

Sources: HCP data, and BAM forecasts.

Table 7.3: Economic growth (%)

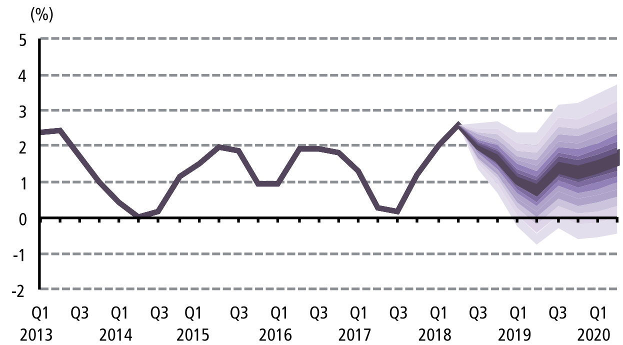
	Actual rates				Forecasts		Gap (Sept./June)	
	2014	2015	2016	2017	2018	2019	2018	2019
Croissance nationale	**2.7**	**4.5**	**1.1**	**4.1**	**3.5**	**3.1**	**-0.1**	**-0.1**
VA agricole	-2.2	11.9	-13.7	15.4	5.1	-1.6	-0.6	0.1
VA non agricole	2.7	1.8	2.2	2.7	3.3	3.7	0.1	0.2
Impôts sur les produits nets des subventions	9.7	18.1	8.8	2.8	3.8	3.9	-1.5	-1.1

Sources: HCP data, and BAM forecasts.

Faster inflation in 2018, while remaining moderate over the forecast horizon

Inflation should rise from 0.7 percent in 2017 to 2.1 percent in 2018. Indeed, the pace of price increases for regulated goods is expected to accelerate, reflecting the upturn in DCT on brown tobaccos and stamp duties. Similarly, after a decline a year ago, volatile food prices are expected to rise. On the other hand, although decelerating compared to 2017, fuel and lubricant prices should continue to rise, due to projected changes in world oil prices and the dollar. On the other hand, core inflation should decelerate from 1.3 percent to 1 percent, partly owing to the slow growth seen during the first eight months of the year in prices for some foodstuffs that are included in it.

Chart 7.9: Inflation forecast over the horizon (Q3 2018 - Q2 2020)*



* Uncertainty surrounding the central forecast with confidence intervals ranging between 10 percent and 90 percent.

Sources: HCP data, and BAM forecasts and calculations.-

Table 7.4: Inflation

	Actual rates				Forecasts			Gap (Sept./june)	
	2014	**2015**	**2016**	**2017**	**2018**	**2019**	**Horizons of 8 quarters**	**2018**	**2019**
Inflation	**0.4**	**1.6**	**1.6**	**0.7**	**2.1**	**1.2**	**1.4**	**-0.3**	**-0.2**
Core inflation	1.2	1.4	0.8	1.3	1.0	1.2	1.3	-0.1	-0.4

Sources: HCP data, and BAM forecasts and calculations.

In 2019, inflation should decelerate to 1.2 percent, assuming that the effect of rising food and energy prices would dissipate. However, its core component should increase to 1.2 percent, with the end of the negative cycle of domestic demand.

Chart 7.10: Change in core inflation and output gap

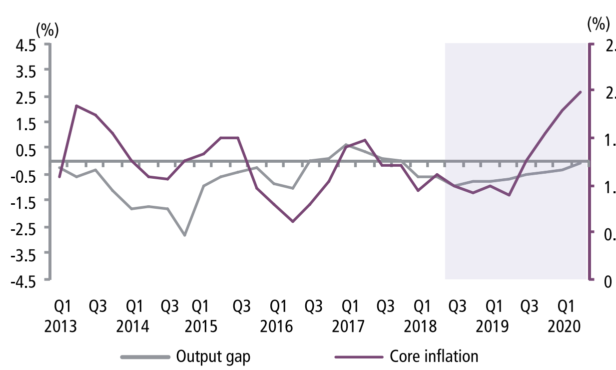
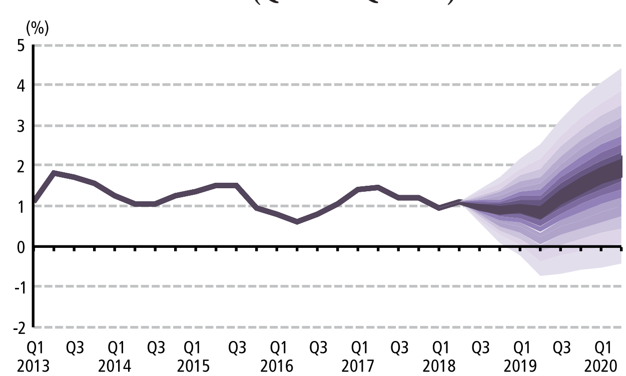


Chart 7.11: Projections of core inflation over the forecast horizon (Q3 2018 - Q3 2020)*



* Uncertainty surrounding the central forecast with confidence intervals ranging between 10 percent and 90 percent.

Sources: HCP, and BAM forecasts and calculations.

7.3 Balance of risks

This exercise takes place in a context of risk continuum surrounding the central forecasting scenario which, in the event of risk materialization, may affect the central projection. The balance of risks is tilted downward for growth and upward for inflation.

With regard to growth, the uncertainties surrounding the robust recovery in global economic activity are increasing. The intensification of the trade war between the United States and some of its partners and its possible effects of contagion, the rise of geopolitical tensions in the Middle East, the political difficulties in some countries of the euro area as well as the persistent uncertainties surrounding Brexit terms could lead to a deterioration in foreign demand.

Regarding inflation forecasts, the risks identified may lead to a higher-than-expected level. Inflationary pressures could come from a more pronounced increase in international energy prices and possible consequences from social dialogue.

LIST OF ABBREVIATIONS

ANCFCC	: National Land Registry Office
APC	: Cement manufacturers professional association
AMMC	: Autorité Marocaine des Marchés de Capitaux (Morroccan Capital Markets Authority)
BAM	: Bank Al-Maghrib
CFG	: Casablanca Finance Group
CNSS	: Caisse nationale de sécurité sociale (National Social Security Fund)
CPI	: Consumer Price Index
CPIX	: Core inflation indicator
CPIXNT	: Consumer price index of nontradables
CPIXT	: Consumer price index of tradables
CT	: Corporate tax
CUR	: Capacity utilization rate
DAP	: Diammonium Phosphate
DCT	: Domestic consumption tax
DH	: Dirham
ECB	: European Central Bank
ESI	: Economic Sentiment Indicator (Indicateur de climat économique)
FA	: Finance Act
FDI	: Foreign direct investments
FISIM	: Financial intermediation services indirectly measured
GCC	: Gulf Cooperation Council
GDP	: Gross domestic product
HCP	: High Commission for Planning
IMF	: International Monetary Fund
IPI	: Import price index
IPPI	: Industrial producer price index
IT	: Income tax
MASI	: Moroccan All Shares Index
MPR	: Monetary Policy Report
MSCI EM	: Morgan Stanley Capital International, Emerging Markets
NPL	: Nonperforming loans
OCP	: Office chérifien des phosphates (Moroccan Phosphates Office)
OECD	: Organization for Economic Cooperation and Development
ONEE	: Office national d’électricité (National Electricity Office)
OPEC	: Organization of the Petroleum Exporting Countries
PER	: Price Earning Ratio
PMI	: Purchasing Managers Index
REPI	: Real estate price index

SMIG : Salaire Minimum Interprofessionnel Garanti (minimum wage)
TEFD : Treasury and External Finance Department
TSA : Treasury special accounts
TSP : Triple superphosphate
QoQ : Quarter-on-quarter
YoY : Year-on-year
UCITS : Undertakings for collective investment in transferable securities
UPC : Unit production cost
VA : Value added
VAT : Value added tax

LIST OF CHARTS

LIST OF TABLES

LIST OF BOXES