MOROCCO ECONOMIC MONITOR

The Recovery is Running Dry

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The Moroccan economy staged a strong recovery in 2021. With a real GDP growth rate of 7.9 percent, Morocco outperformed regional peers and recovered the output losses undergone during the first year of the pandemic. This rebound was sustained by an extraordinary agricultural season, solid manufacturing and agro-industrial export, and the recovery of domestic demand, partly fueled by a successful vaccination campaign, supporting macroeconomic policies and unprecedented levels of workers’ remittances.

However, Morocco is once again suffering the impact of a string of adverse shocks. The beginning of the agricultural season has been unusually dry, and a poor cereal crop is to be expected for 2022. This coincides with a slowing of the global economy and rising international commodity prices, adverse trends that severely intensified following the Russian invasion of Ukraine. Importantly, these shocks have turned out to be mutually reinforcing given that the drought is forcing Morocco to import larger volumes of cereals at substantially higher prices due to the war. In this more adverse context, the economy could decelerate sharply in 2022, and we now project a growth rate of 1.3 percent in 2022.

Ongoing shocks are affecting fiscal and external balances. The public sector is cushioning the impact of the shocks through pre-existing price subsidies and various ad hoc emergency measures. As a result, the budget deficit is on the rise, although Morocco still presents better fiscal indicators than most emerging markets and developing economies. Given that Morocco relies on imported fuels and cereals (particularly in dry years), net imports are also increasing markedly. In this context, we project the budget and the current account deficits to reach 6.4 and 5.2 percent of GDP in 2022, respectively. The risks posed by such twin deficits are mitigated by a comfortable stock of foreign exchange reserves, the solid structure of Morocco’s public debt, and maintained good access to international financial markets.

Albeit somewhat more moderately than in other countries, Morocco is beginning to face intense inflationary pressures. Despite the cushioning impact of price subsidies, annual inflation reached 5.9 percent in April 2022. In combination with the drought and the economic slowdown, these price pressures are having significant social impacts on the poor and vulnerable. So far, the central bank is treating this price shock as temporary and has not revised the orientation of its accommodative monetary stance. If price pressures do not recede, the central bank may eventually be forced to raise interest rates. Although necessary to avoid a de-anchoring of inflation expectations, such a move would be procyclical, and further feed the stagflationary headwinds that the economy is beginning to face.
Recent droughts serve as a stark reminder of the exposure of the Moroccan economy to rainfall shocks. Large oscillations in rainfall levels contributed to amplify the 2020 recession and the 2021 recover and will once again slow growth in 2022. This report includes a special focus chapter on the macroeconomic impacts of droughts and water scarcity in Morocco, using part of the analysis that is included in a soon to be published World Bank diagnosis: the Country Climate and Development Report (CCDR). It emphasizes the importance that rainfall shocks have as a source of macroeconomic volatility in Morocco. In recent decades, however, droughts tended to be followed by strong rebounds, and the recurrence of such shocks did not impede a solid long-term agricultural GDP growth. Going forward, climate change may turn water scarcity into a more permanent condition, which would have severe long-term impacts on the economy.

**Infrastructure development is a necessary but not sufficient condition to cope with water scarcity.** Historically, Morocco has relied on massive water storage and irrigation investments to cope with highly variable rainfall patterns. Such investments are more necessary than ever, but international experience suggests that to cope with water scarcity, "engineering solutions" need to be coupled by effective water demand management policies.