KfW Research
Emerging Markets Spotlight

››› Morocco – a better future through better education

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Economic situation

- Real growth
- Private consumption (yoy)
- Inflation rate

Recovery of the agricultural sector drives economic growth

A severe drought was responsible for disappointing GDP growth of 1.5 % in 2016. The recovery of the agricultural sector this year is having a positive influence on economic output, which is expected to rise by 4 %. Growth is being sustained by robust domestic demand. A persistently low inflation rate of less than 2 % from 2012 to 2016 provides planning certainty for all economic actors.

Growth financing

- Budget balance to GDP
- Current account balance / GDP
- Government debt / GDP

Chronically negative current account, but borrowing is long-term

The current account deficit of 4.4 % in 2016 was much lower than in 2012, when it stood at 9.3 %. Foreign direct investment is contributing a significant portion of funding, making the economy less vulnerable to rapid capital outflows. The buildup of currency reserves as a liquidity buffer is also having a stabilising effect. Public debt is relatively high at 64 %. In a bid to prevent a further increase, the government is planning to cut spending and reform the public administration.

Growth resources

- Investment ratio
- Share of agriculture
- Labour market participation

Low productivity and labour market participation

The investment rate in Morocco is a high 31 % of GDP. However, investment focuses on sectors with low productivity. The very low participation rate of 51 % (2016) is also worrying, as it is a sign of poor use of labour as a production factor. The integration of young workers into the workforce is particularly difficult (see focal theme).

Economic relations with Germany

- Germany's share of exports
- Germany's share of imports
- FDI inflows from Germany

Expanding trade relations with Germany

Germany's share in Morocco's total imports increased by two percentage points in the past four years. At more than 50 %, motor vehicles and parts, machines and electrical equipment are the most important imports from Germany, while Morocco exports mostly clothing, leather, leather goods and agricultural products to Germany. German direct investment is limited owing to the relatively small size of the market.

Legend (see p. 5 for detailed explanation of methodology) — very good — good — neutral — poor — very poor

Investment climate – assessment by our local experts

Morocco is not considered a classic emerging market but nevertheless offers interesting investment opportunities. Thanks to its proximity to the European market and well-developed infrastructure, its economy is gradually becoming integrated into international production processes. Unlike many neighbouring countries, its political situation is stable. Morocco already acts as a regional hub of the continent. Africa is also increasingly becoming a focus of Morocco's economic and foreign policy. The economic structure is changing but the process is slow. One of the main factors hampering the structural transformation is the lack of skilled workers.

Continued on p. 2

Focal theme: Educational and labour market reforms are crucial

The country's growth potential is dampened by inefficient use of labour as a production factor. Problems lie in both supply and demand for workers. On the one hand, workers often do not have the desired qualifications owing to low training standards and on the other, rigid labour market regulation is dampening the already weak employment growth. The latter affects young workers in particular. Reforms in the educational sector are planned, but it will take some time for successes to become visible. It is important for entrepreneurs to tap into the labour potential in a targeted manner, for example through specific selection and preparation procedures and extra-occupational training.

Continued on p. 2

Investment climate – assessment by our local experts

Morocco has close geographic, cultural, political and economic ties with Europe. The coast of Spain is only 14 km away, French is recognised as an official language, and a privileged partnership – the 'statut avancé' – promotes convergence with European standards and joint dialogue, e.g. on human rights, investment certainty and gradual economic integration into the EU internal market. In addition, the EU is Morocco's most important trading partner.

The political situation is relatively stable. Reigning King Mohammed IV has embraced a moderate style of governance and is driving the country's development. Morocco is also scoring points with a solid infrastructure that is being gradually modernised and expanded in a bid to integrate the country more closely into international production processes. These factors are also reflected in the 'Africa Attractiveness Index' introduced by the consulting firm Ernst & Young. It ranks Morocco as the continent's most attractive location for foreign direct investment.

Morocco is increasingly evolving into a regional hub. With its readmission to the African Union and its (still to be confirmed) accession to the Economic Community of West African States (ECOWAS) in 2017, Morocco has underscored its ambition to take on a more prominent political and economic role on the African continent. The country is already a commercial port of entry for foreign investors looking to tap into the continent. In 2016, some 12 % of all FDI projects on the African continent were carried out in Morocco. Finance City in Casablanca, where Moroccan and international banks are vigorously developing their business on the African market, is emblematic of these two trends. The chemical industry, especially fertiliser production, plays an important role thanks to large phosphate deposits. Interesting sectors include logistics, renewable energy and the automobile sector, where firms such as Renault, Nissan and Siemens already have local representations. The country's strong average economic growth, however, is not benefiting all groups of the population – and youth unemployment in particular is raising concern.

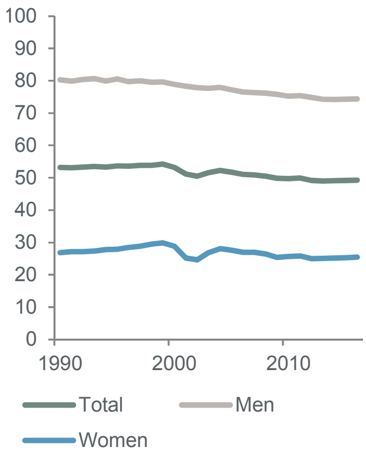
Low level of education and cumbersome bureaucracy are major location problems. It is hard for entrepreneurs to find qualified workers. The level of education is low and the illiteracy rate exceeds 35 %. Bureaucratic processes are laborious and corruption is still widespread. There is generally little dynamism and entrepreneurial spirit.

Both the king and the newly elected government are willing to introduce reforms – if in small steps. Existing restrictions on capital movements are to be gradually eliminated in a bid to completely liberalise the dirham. Education sector reforms are being initiated, but their implementation will take time. Foreign investors may profit from cooperating with a local partner.

Based on an interview conducted with Alexander von Kap-herr (Director of the KfW Development Bank Office in Rabat) on 22 June 2017. ■

Figure 1: Participation rate

In per cent



Source: ILO

Focal theme: Education and labour market reforms are crucial

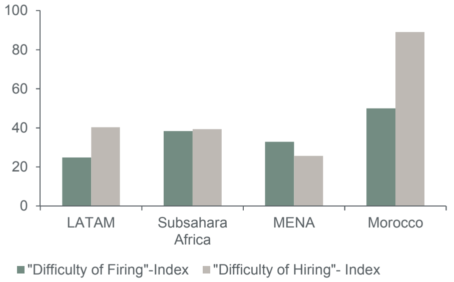
Despite positive developments, Morocco still faces considerable challenges on the path to becoming an upper middle income country. The employment rate is too low: just one in two Moroccans of working age have a job. The participation rate of women is at 25 % particularly low and falling (Figure 1). This is detrimental to the economy because a significant portion of the labour force potential remains untapped.

Demand for labour is developing at a (very) slow rate. Across the past decade, the economy expanded by 3.9 % on average. But the strong growth rate has had only a limited effect on employment creation. One per cent more economic growth led to a mere 0.3 % more employment, significantly less compared to the average of other developing countries (0.7 %). The low employment growth – lower than in comparable lower and middle income countries such as Egypt or the Philippines – is insufficient to provide work for the 270,000 new jobseekers entering the workforce each year.

In order to strengthen the industrial basis, the Moroccan government has implemented the 'Industrial Acceleration Plan'. It aims to create 500,000 new manufacturing jobs by 2020. This intended structural transformation is so far running at a sluggish pace. New jobs are emerging mostly in industries characterised by low productivity. Of the 1.1 million jobs (excluding

Figure 2: Labour market regulation

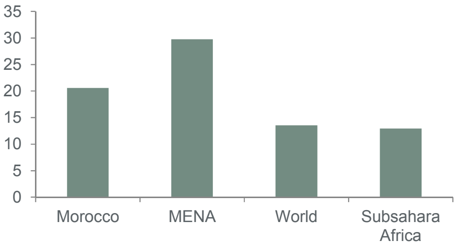
2016



Source: World Bank, Doing Business, own calculation.

Figure 3: Youth unemployment

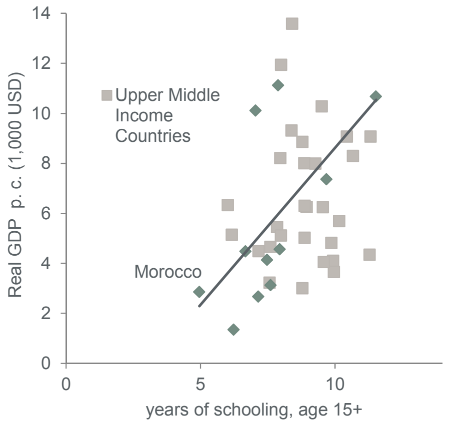
2016, in per cent



Source: World Bank

Figure 4: Level of education and prosperity

As of 2010



Source: World Bank. The comparison group includes the emerging economies listed here (Brazil, China, India, Indonesia, Mexico, Russia, South Africa and Turkey) including Algeria and Egypt. The definition of upper middle income countries follows that of the World Bank.

agriculture) newly created in the period of 2000–2014, 570,000 were in hospitality and construction alone.

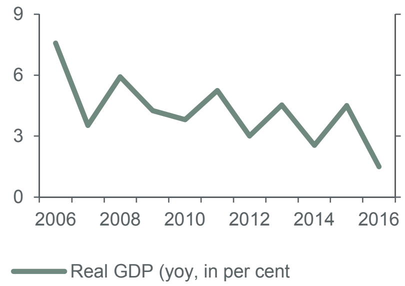
With regards to the supply side, the labor force does not have the skills needed. For local entrepreneurs, the lack of skilled workers is one of the most pressing problems. The educational system is deemed inefficient and in need of reform. Public expenditure on education is on an international level, at 5 % of GDP, but Moroccan students perform below average in comparable attainment tests. Some 72 % of students leave the educational system without a formal certificate. Many workers therefore lack the general and specific qualifications required to successfully integrate into working life. Their qualifications are not aligned with the employers’ needs – a classic skills mismatch. This discrepancy is particularly striking among university graduates. In contrast with most economies, unemployment among graduates is 21 %, significantly higher than among workers with lower qualifications.

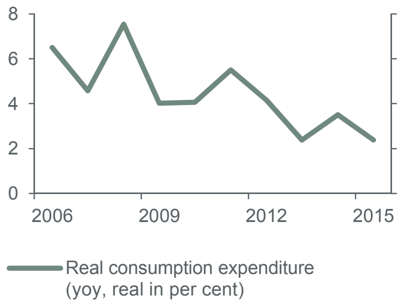
Labour market regulation receives a poor grade. A permeable and flexible labour market helps align labour supply and demand. According to the World Economic Forum, Morocco ranks only 124th of 138 economies in labour market performance. Hiring processes are particularly difficult (Figure 2), as high non-wage labour costs combined with inflexible regulation make labour a very expensive production factor. That puts a dampener on employers’ demand for labour. These adverse effects are particularly hard on young career entrants. In 2016, youth unemployment exceeded 20 % (Figure 3). Furthermore, many young career entrants also work in precarious employment relationships, with only 12 % of employed youths working on the basis of an official employment agreement (in 2015).

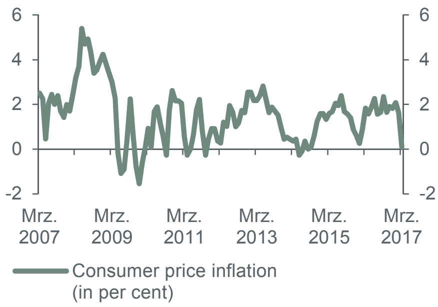
The development of relevant human capital is one of the most important structural drivers of economic growth. In order to rise to the status of upper middle income country, Morocco must raise labour participation in particular. Modern and more efficient labour market regulation and a comprehensive education reform are urgently needed to achieve this (Figure 4). The problems have been identified, as Morocco has already formulated a long-term strategy for reforming the educational system (‘strategic vision for Moroccan education reform 2015–2030’). Its focus lies on, among other things, creating equal opportunities by improving access to education for all groups of the population, improving the quality of education for students and teaching staff, and reducing the dropout rate. But it will take time to implement this vision. In this situation it is particularly important for local businesses to become active themselves to identify and effectively close existing skills gaps. A structured needs analysis across all business functions forms the basis for implementing targeted measures such as introducing an efficient recruitment process or selective basic and advanced training measures. ■

Charts

Economic situation

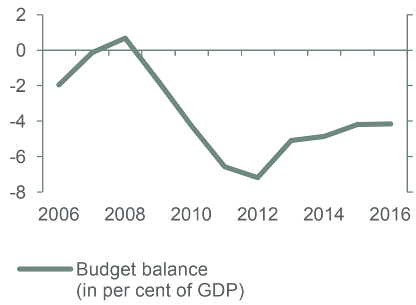


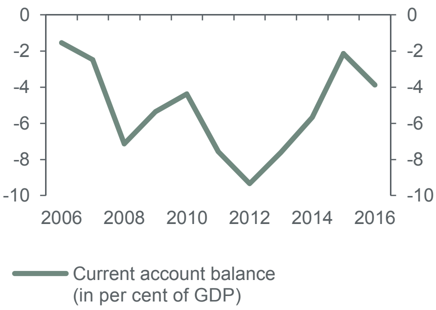


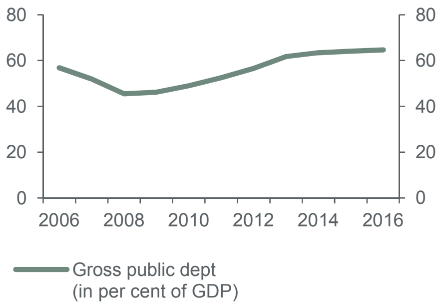


Sources: Datastream; IMF, World bank; own calculations

Growth financing

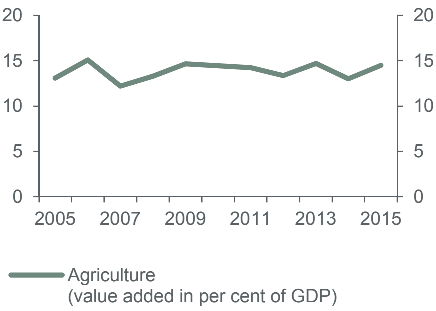


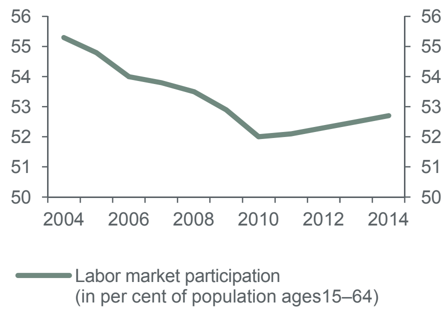




Sources: Datastream; IWF, World bank, own calculations

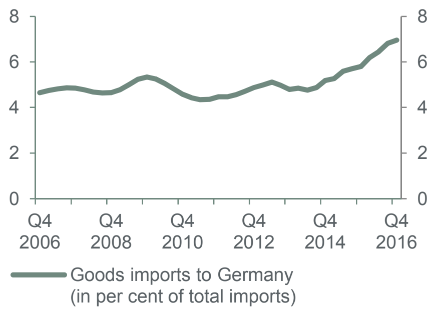
Growth resources

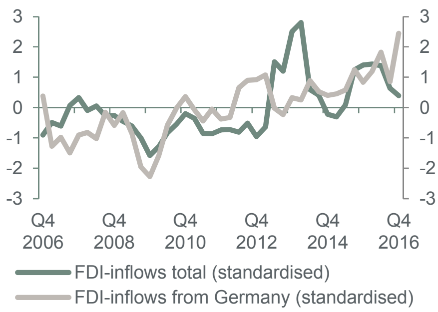




Sources: Datastream; World bank

Economic relations with Germany





Sources: Deutsche Bundesbank; Datastream; IMF; UNCTAD; own calculations

Methodology

In the Emerging Markets Spotlight, a selected country is analysed based on various macroeconomic indicators. These indicators are grouped into four categories: economic situation, growth financing, growth resources and economic relations with Germany.

- Quintile 1
- Quintile 2
- Quintile 3
- Quintile 4
- Quintile 5

The indicators are used to compare the country's situation with its peers. The group comprises Brazil, China, India, Indonesia, Mexico, Russia, South Africa and Turkey. The comparison is based on a quintile ranking in five categories, which are labelled in different colours (see chart):

The country is assigned to a quintile of the country group for each indicator analysed. The best quintile may be different for each indicator. For example, higher growth rates are better, so here the upper quintile is coloured dark green, but higher debt rates are a negative factor, so here the upper quintile is coloured dark red.

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