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Title: *Agribusiness development in Morocco under the Free Trade Agreement with the United States*

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Problem Statement

The implementation of trade liberalization in Morocco will lead to major transformations in agriculture and the rural economy. The eventual elimination of tariffs will result in lower margins and reduced production of certain cereal crops, notably wheat and oil seeds. Offsetting these rural income and employment losses will require a shift toward higher value-added production and the creation of new businesses and job opportunities in both rural areas and smaller towns and cities.

Low agricultural productivity and agribusiness value added

Moroccan experts well understand that the country must shift to higher value-added crops in order to increase agricultural productivity and incomes. However, protective tariffs, insufficient market development, and the inefficient use of scarce inputs, especially water, contribute to low competitiveness in world markets. Morocco clearly aims to integrate itself into the global economy, and has already achieved greater openness under the Association Agreement with the European Union, Turkey FAT and Agadir Agreement. Despite Morocco's commitment to even more liberalization under the US-Morocco FTA, the Moroccan private sector remains remarkably focused on serving domestic consumers and traditional export markets in Western Europe. Global consumer trends are not monitored and researched sufficiently to identify niche and broader market opportunities for Moroccan producers. Moroccan farmers and agribusinesses do not look beyond traditional Western European markets, and have not effectively progressed up the value-added chain through domestic processing of exportable agricultural products. They are unfamiliar with the U.S. market and have not diversified into countries newly joining the European Union. In addition, short supply periods and volatility in deliveries to agricultural packing and processing plants undermine the return to agribusinesses.

Within the Moroccan economy, agriculture accounts for 12 to 24% of GDP depending on annual climate change, and 80 % of employment in rural areas. Agricultural products also account for 18% of Morocco's export earnings.

Annual exports of fresh, frozen, and processed fruits, vegetables, and nuts total slightly less than US\$1 billion. More importantly, the agricultural sector has strong linkages to the rest of the economy. It has an important influence on overall economic performance. Although rain fed agriculture accounts for 87 % of cultivated area, it contributes a smaller proportion to the total value-added from crop production. Agriculture in the rain fed areas is characterized by low productivity and large fluctuations in production due to low and highly variable rainfall. By contrast, irrigated crops account for a minority of cultivated area, but represent a larger proportion of the value-added from crop production. Most of Morocco's agricultural exports are grown on irrigated land (exact figures concerning the value-added contributions from rain-fed versus irrigated agriculture are the subject of much discussion and debate).

Employment in irrigated and rain fed areas shows a pattern similar to that of the value of agricultural production. The intensive nature of irrigated agriculture generates many times more jobs per unit of land than extensive rainfed agriculture. In addition, irrigated areas produce a range of crops with labor-intensive forward linkages. It is estimated that the processing, packaging, and other activities involved in vegetable and fruit marketing and trade create at least as many jobs as the number needed on the farm. Indeed, when considering production and employment, agriculture constitutes the backbone of Morocco's rural economy and even has strong linkages with urban-centered processing and packaging industries.

The transformation of Morocco's agricultural base toward higher value-added production depends on a number of factors, including: improvements in market research and marketing, better product development, improved production practices, including more efficient use of scarce water resources, timely availability of working and investment capital, and a supportive legal and policy environment.

Shifts in cropping patterns toward crops that have export potential or inputs to value-added food agricultural products and away from cereals could add further pressure on water resources, as higher value-added crops typically demand better water management. Water scarcity is exacerbated by inefficiencies in water use in agriculture, particularly by small and medium sized farmers, and includes such practices as: irrigation by flooding of fields, wasteful pivot irrigation systems, elevated evaporation losses from open canal conveyance of water, poor timing of water release in relation to farmer and plant growth needs, as well as poor economic demand management. These practices all contribute to water wastage and result in poor productivity from irrigated agriculture.

The current irrigation infrastructure and on-farm water delivery systems need to be updated, and alternative ways of valuing water need to be examined. Investments at both the system and on-farm levels will be required in order to realize a shift to water-saving irrigation technologies, and different, higher value-added cropping patterns.

High labor costs and inadequate training limit the competitiveness of the workforce

The Government of Morocco has made major progress in the last year with the adoption of a new, unified labor code that addresses issues such as the hiring of temporary workers, conditions for dismissal, and severance pay. However, foreign and local experts believe that additional actions are needed to improve the functioning of training and labor markets. For example, labor productivity per unit costs is high in comparison to competitor countries per studies conducted by the World Bank and the Government of Morocco. Low skill levels and high mandatory levels of employer payments for pension and health insurance both contribute to this problem.

Limited Finance for Business Development

Morocco is implementing a major program of financial reform. Two bills are now being addressed before parliament. However, banks are still highly liquid, heavily invested in Moroccan treasury issues, and prospect little beyond secured, constructed loans with their customary, well established clients. Small businesses are underserved; private financing for municipal infrastructure that would facilitate private business development is virtually non-existent.

According to business owners, liens and guarantees on fixed and moveable assets, working capital, and owner off-balance sheet assets are all typically required before any bank credit is made available. Additionally, other constraints include: unclear property laws, inability to assess risk for non-secured loans, and lack of capacity building for small enterprise to develop business plans and complete applications for credit. Such multiple undertakings from the borrower increase transaction costs to both the borrower and banks and depress the availability of credit. Lack of predictability in work out and bankruptcy proceedings may also account for some of the reluctance of banks to extend credit to small borrowers. This lack of articulation of Morocco's financial sector impedes development of small businesses.

The market for agricultural credit is dominated by a single, majority state-owned institution which has a high percentage of non-performing loans. Although it has been the subject of reform efforts, this institution alone is unable to meet the

future capital requirements of a dynamic agriculture sector. Commercial banks provide credit for agribusinesses, but to this date have not seriously ventured into the more risky agriculture credits, except for major, well-known private clients.

Objectives

USAID's economic growth strategy is to assist Morocco in successfully responding to the challenges and opportunities of the more liberalized trading environment that will be brought about by the Free Trade Agreement with the US., the Association Agreement with the European Union other FTAs, the WTO Doha Development Round, and Morocco's own reform efforts. There are three intermediate results (IRs) which are key to achieving this objective:

1. *Increased productivity in agriculture and agribusiness*
2. *Creation of new business opportunities outside of agriculture and agribusiness*
3. *An improved business environment.*

The focus of this activity is on Intermediate Result 1, which requires a shift into the production and processing of higher value crops, increased use of appropriate technology, human resource development, greater availability of capital, and far-sighted public policies.

Prior USAID Experience in Agriculture and Agribusiness in Morocco

This program will build upon USAID's prior work in developing Morocco's agricultural and agribusiness sectors through interventions that spanned basic research, development of agricultural institutes of higher education, advanced training in agricultural economics, water management and irrigation efficiency, and agribusiness market development. Among the previous USAID-funded programs are:

- *Agribusiness Promotion Project*: (\$ 18 million, 1991 to 1999). The objective was to increase the capacity of the private agribusiness sector to produce, package, and market a wide variety of agricultural commodities. The program included four major components: export market development; policy support; support to industry organizations and institutions; and human resource development.
- *Tadla Resources Management* (\$ 10.6 million, 1992-1999): project introduced level-basin technology to increase water saving through improved

irrigation management and through improved on-farm water-use efficiency.

- Water Resources Sustainability (\$ 11.4 million, 1995-2003)
- Dryland Agriculture Applied Research (\$ 50 million, 1978-1995)
- Planning, Economics and Statistics for Agriculture(\$ 13.2 million, 1983-1995)
- Agronomic Institute (\$ 28.5 million, 1980-1999)

Ongoing USAID Economic Growth Programs

The new program will be implemented in the context of USAID's ongoing efforts to create jobs and increase incomes by improving the business environment and promoting new business opportunities. All of the programs mentioned below are ongoing and are funded under USAID's 2000-2004 Strategy:

Business Climate:

- Commercial Law and Courts Modernization (\$4.4 million; 2000-2005): Program of assistance to the Ministry of Justice for the modernization of commercial laws and courts in Morocco.
- Investment Reform (\$2.2 million; 2003-2005): Program is working with the national investment office and the regional investment centers to simplify existing procedures, improve transparency, and help regions develop and promote their investment potential to local and foreign investors. It builds on studies and pilot projects completed under Investors Roadmap Phases I, II, and III.
- Microfinance Sector Development (\$1,200,000; 2003 to 2005): Local and foreign expertise to provide help to develop new products (e.g. housing, rural, tourism), establish a credit reference bureau, and improve information systems and governance.
- Microfinance Guaranties (about \$ 400,000 in guaranty authority; 2003-2008): Program makes use of USAID's Development Credit Authority (DCA) to provide loan guaranties for local microfinance institutions to raise up to about \$16 million in loan capital from private sources.

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- *Rural Microfinance*: (\$ 700,000 equivalent in dirhams; 2003-2004): Program provides capital to microfinance associations for expansion into rural areas that may be affected by FTA.
 - *Environmental Assistance* (\$ 280,000; 2003-2005): Program to provide training and capacity building to enable the Department of the Environment to better enforce GOM environmental laws. Funding supports logistics and travel of EPA experts.

Agriculture, Agribusiness, and Water Resources Management

- *Souss-Massa Integrated Water Management Project (SIWM)* (\$ 8.2 million; 2000-2004): project aimed at introducing water saving/ delivery techniques through the participation of all local water management stakeholders.
- *Water Protection and Management Project (WPM)* (\$ 3 million¹; 2001-2004): project introduced integrated rural development in targeted regions to protect the environment, control soil erosion and create income generating activities.
- *Agricultural Strategy* (\$300,000; 2003-2005): Assistance to the Ministry of Agriculture to help prepare a strategy for agriculture sector reform that will better position Morocco for a World Bank structural adjustment loan.
- *Agribusiness Associations Development* (\$ 250,000; 2003-2004): The program is working with selected agribusiness associations on the export of fresh and processed agricultural products. Information and expertise is being provided on market demand, Sanitary and Phytosanitary Standards (SPS), Hazard Analysis and Critical Control Points (HACCP), packaging, pricing, and marketing channels.
- *Tree Planting* (\$ 300,000; 2003-2004): Fruit-bearing trees have been donated through rural based non-profit associations to families in rain-fed wheat growing regions (Meknès-Fès) in order to increase incomes and reduce migration to cities.

Business Development

- *Rural Tourism* (\$ 3.1 million; 2002-2005): The program supports local public and private organizations in developing and marketing new rural

¹ Dh 21 million equivalent from trust funds

tourism products to complement existing beach and imperial cities destinations.

- *Fast Track Trade Program* (\$ 2.65; 2003-2005): The program is helping Moroccan companies to identify U.S. business partners and advising them on marketing, packaging, and U.S. environmental and safety standards.

Expected Results

To assist farmers, agro-processors, agribusinesses and related industries in the growth and improved profitability of complete product chains, from the initial production stage through processing and distribution to the market.

1. Improved Public Policies and Institutions in Support of More Competitive Agriculture and Agribusiness
2. Increased productivity and variety in agriculture and livestock production
3. Improved competitiveness of agro-processing industries
4. Enhanced capacity of other agribusinesses, firms, and institutions to support competitive value chains