

land, infrastructure) are growing bottlenecks. Water scarcity will force Morocco to revisit traditional ways of expanding irrigated production, without leaving agricultural output, which accounts for almost one-fifth of value added, subject to rainfall-driven fluctuations. It will also require attention to the long-term relationship between supply and demand of potable water, not only in large cities but also for deprived rural communities; fewer than 15 percent of rural households have access to safe water, compared with over 90 percent of urban households.

9. External trade patterns are stable, although the country is vulnerable to external shocks. Over 60 percent of Morocco's merchandise trade is with the EU, which is also the source of most tourism receipts and foreign investment flows. This concentration of trade with the EU is likely to increase further with a Trade Agreement, while trade flows with other Maghreb countries, despite the creation of the Arab Maghreb Union (UMA), remain negligible. In general, the currency denomination of Morocco's foreign exchange earnings is closely aligned with that of its payments, reducing the country's vulnerability to cross-currency exchange rate fluctuations. It is now urgent to develop a foreign exchange market and to move towards full capital account convertibility of the dirham. This will support an outward-looking investment strategy and will secure a stable access to external financial markets and direct foreign investment to help finance privatization and fuel private sector growth and export capability. This requires further modernization of the financial and monetary sectors.

10. Macroeconomic Outlook. Morocco's prospects suggest that medium-term GDP growth of 4-5 percent per year with low inflation is feasible under a base case scenario; this would modestly improve the country's external debt indicators, and broadly maintain its internal and external macroeconomic balances. Under conservative assumptions, growth would increase gradually above levels attained in recent years. Over the medium term, growth would average 4-5 percent, with manufacturing and service sectors leading at 5 and 6 percent, respectively. However, prospects for 1995 look unfavorable due to delays in rainfall. The current account deficit would continue to decline, and debt service ratios would improve somewhat. Domestic absorption would be higher, with moderate increases in both investment and consumption. The development challenge for Morocco is to move beyond maintaining past performance, however commendable it may be, and to increase growth performance above demographic growth and up to at least 7-8 percent annually circa 2000.