Investment inefficiency and downward trend of its private component in Morocco: what role should public investment play?

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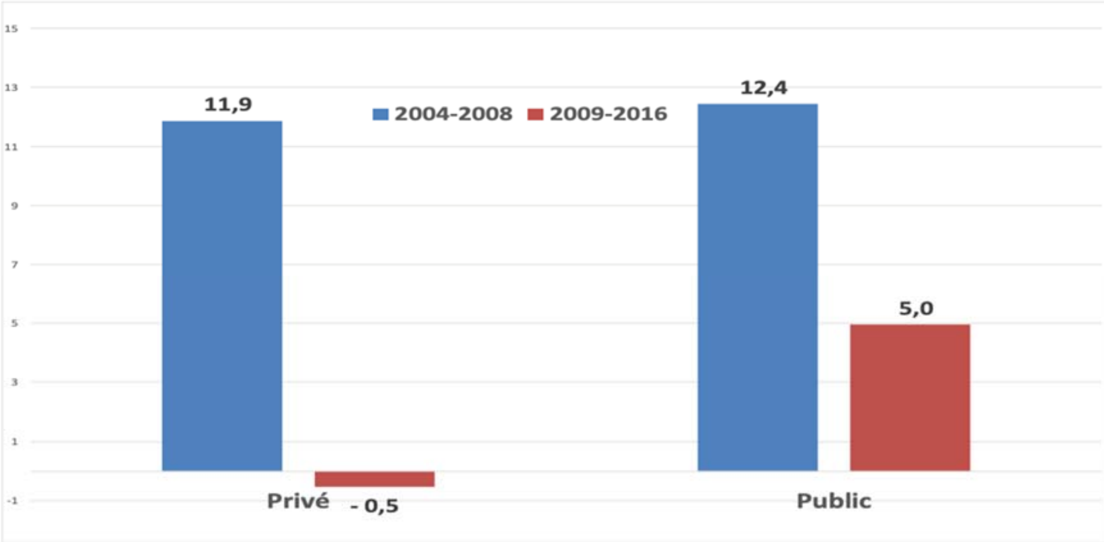
The central role of investment in promoting economic growth and development cannot be disputed. From a theoretical perspective, no one can deny the importance of Investment in terms of economic growth and development via the expansion of productive capacity (mainstream economists) and via aggregate demand expansion (heterodox economists). The latter "investment" is related to different macroeconomic and social indicators which has made countries focus on the guidance of investment choice and decisions, and creating better climate for economic development and wealth creation.

Morocco is averaging high rates of total investment to GDP for a long period (30,36% between 2009-2017) compared to the lower middle-income countries (26,52%) and rather equivalent to that of upper middle-income countries (31,35%) during the same period. Few countries can carry on such an effort over a long period of time. However, the country is far from being at the top of the table in terms of return on investment. After averaging high growth rates (8.1%) in the period 2000-2008, Total investment growth has dropped in the recent years since 2009 to average only 1,3%, contributing to economic growth only by 0.4 points which is 5.75 times less than the observed in the previous period. Considering its marginal effectiveness, it is very weak. Indeed, the ICOR (Incremental Capital-Output Ratioof 7.2 is among the highest in the world: in other words, for an increase of one percent point of product, it is necessary to increase investment to GDP ratio by 7.2 percentage point. The benchmark achieved by the High Commission for Planning (HCP) shows that countries like Turkey (5.2), Chile (4.2), Malaysia (3.5) and better still South Korea (2.9) have an ICOR lower than that of Morocco showing a better investment efficiency. With an investment rate of about 28% of GDP, emerging and developing countries have achieved a higher economic growth rate over the last fifteen years (6% per year on average) than Morocco (4.4%), even though the latter has maintained an investment rate of over 30% of GDP throughout this period. These numbers aroused a lot of attention especially among economists and government, and which started a debate about the weak performance of the economy relative to the effort deployed by the country in terms of investment.

Looking deeply in these numbers, the dynamic of private investment, which should be the engine of any growth process, has been steadily declining since 2008 recording a negative growth rate (-0.5%) over the last decade, compared to 11.9% between 2004 and 2008. And If the depreciation rate is reduced, the decrease in the investment will be even more drastic. The downward trend in private investment during the recent decade has been accompanied by a slowdown in economic activity illustrated in a decrease of nonagricultural GDP growth from an annual average of 4.7% over the 2000-2008 period to 3% between 2009 and 2017.

Figure 1 : Average annual growth rate of gross private and public investment



Source : Memorandum : Pour un modèle alternatif de développement du Maroc

Given the gravity of the situation, public authorities have conducted many plans to give a new breath to private investment in order to enhance economic growth. The rate of corporation tax has been reduced from 35% to 30% which has led to a decrease in tax burden from 25.9% to 20.9%. Similarly, equipment credit rate lost 280 basis points between 2006 and 2018. Other tax incentives in recent years have not changed the position of investors. Also, public authorities deployed many projects in order to promote business climate which allow Morocco to gain 67 places in the "Doing Business" Index in record time between 2009 and 2018. Yet, it must be noted that the private investment and growth have not recovered.

Indeed, all the measures undertaken in the recent period have shown their ineffectiveness in terms of revitalizing private investment and, as a corollary, economic growth. Despite this, the public authorities continue to pull the same strings, ignoring the fact that productive capacities are permanently underutilized. However, companies can only start new investment if there is a high demand that is putting pressure on their capacities and opening up profit prospects. The productive capacity rate did not exceed 65% starting from late 2015 (except some periods) and started fluctuating around 60% from 2017. These numbers show that the fall of private investment performance and the slowdown of economic growth is a matter of aggregate demand.

Figure 2 : Productive capacity utilization rate

Source: CEIC Data

Household consumption cannot play the role of private investment stimulator and ensure a high and sustained growth. In fact, beside the huge contribution of the latter to growth (an average contribution of around 61%), its evolution depends on real income whose progression can only continue in the long term if productivity gains are realized (with some hypothesis on its distribution). The later has been growing in a slow pace averaging 1.5% between 1990 and 2017 which is too low compared to the lower middle-income countries (3,8%).
The external component of demand also depends, inter alia, on productivity gains. This component is in a structural deficit and its contribution to growth is at best null.

Considering these stylized facts, the only viable lever capable of launching private investment and creating the necessary dynamics for a sustainable economic growth is public spending and especially public investment. in addition of creating demand and growth via the multiplier the latter also affects the productive capacity and thus productivity by promoting structural changes, namely stimulating technical progress by means of industrial policies. So, public investment can play the role of a catalyst for private investment with positive externalities on growth.

Looking at the available data, Morocco is deploying a big effort in term of public investment. According to the OECD's repport "*Investissement public efficace pour un développement territorial inclusive et durable, 2018*", Direct and indirect investment by the entire public sector is significant and amounts to around 17% of GDP (2015). This is the result of a considerable shift in public investment in Morocco, which has more than doubled in 2015 compared to ten years before. But considering only direct investment of the State and local authorities excluding public enterprises, public investment, in its strict sense, represented 4,4% of GDP in 2015 which is higher than the average share of OECD countries (3.1%). This places Morocco well above the average of OECD countries (3,1%) with a similar level to countries like Norway, Sweden and Slovenia.

However, these high public investment rates contrast with the status of economic activity that has remained modest. A report of the HCP in 2016 outlines that Morocco's growth rate does not reflect the investment effort made over the last few years. These numbers launched a debate in Morocco about the effectiveness of public investment, and more particularly on the means to reinforce the effects on economic growth of the economic policies carried out and especially of the public investment.

Barriers to effective public investment are often more related to governance issues and the choice of projects and sectors targeted by the government. The IMF calculations show that better governance of public investment could increase the potential gains of this investment by 30%. The HCP believes that the transformation of economic structures in Morocco, accompanied by the continued accumulation of human capital and the improvement of governance, would allow, over time, growth gains of more than nearly 3 points. According to the same institution, more effective governance would bring additional gains in economic growth by almost one point (Office of the High Commissioner, 2016).

Since it was agreed that the return of vigorous job-creating growth requires a new public investment strategy, the central question then is: how to improve the governance of public investment in Morocco? The OECD emphasizes the key role to play by local authorities in economic and social development of their territories in the advanced regionalization framework pursued by Morocco. In order to avoid any kind of public investment that is disconnected to the specific needs of different territories, it would be better to mobilize local and regional knowledge to develop public investment strategies, and then invest using differentiated regional strategies, reflecting the specific advantages and needs of the latters.

Tamsamani Y., Moroccon economist, Emphasized the important role of public investment to revitalize private investment and, in corollary, economic growth. He stated that main problem of private investment is the permanent underutilization of productive capacities. And in order to give new breath to private investment in the very short term, there is no lever other than a "**useful**" public investment which is characterized by a maximum return and ensures that the latter is coherent and harmonious as a whole. The idea is to focus on certain criteria of efficiency, effectiveness and coherence in the choice of projects and sectors targeted by public investment in order to generate the highest and best distributed training effect across sectors and territory, especially since the room for maneuver is very tight due to the sustainability constraint of the public debt

For public investment to be "***useful***", it should fulfil some criteria.
The first concerns the maximization of the knock-on effect by avoiding dry foreign currency leakage. That is by targeting sectors that have strong backward and forward linkage with the others, and branches whose share of inputs in production is high, and preferably locally produced inputs.
In addition, public investment must target areas where there is under-utilization of production's potential and also take into account the positioning of the economy on its cycle in order to maximize the multiplier effect.
Third, public authorities should conduct public investment in the direction of creating very positive externalities, especially the focus on the return of private capital on the one hand and on the establishment of the foundations of a state of social justice on the other hand. And that is by investing in sectors like education and health which will establish social justice in one hand, and impacts positively private investment return and productivity in the other hand.
Fourth, in order to maintain a continuous dynamic of investment, the choice of public investment should focus on projects that ensure a return on investment in a short time which would generate other investment cycles. Also, the choice of projects and their sizing must go hand in hand with the level of development of the country and therefore the absorption capacity of its economy.