11

Conclusion and Recommendations

GARY CLYDE HUFBAUER AND CLAIRE BRUNEL

When the Morocco-US Free Trade Agreement (FTA) came into force in January 2006, both parties had high expectations. After three years of implementation, the results of the FTA are mixed. The two countries have succeeded in deepening bilateral trade and investment relations, but since trade and investment levels started from a low base, they have not reached the magnitudes that both parties expected. In particular, Moroccan business leaders are concerned about the poor performance of Moroccan exports to the United States and the inability to attract US foreign direct investment.

In this study we have tried both to assess the implementation of the FTA and to formulate recommendations to better leverage the agreement. Based on the analyses of the preceding chapters, we offer the following findings and recommendations.

Overview of Morocco

Morocco's economic performance over the last decade has been relatively strong—the country averaged 4.6 percent annual growth, and its trade with the world more than quadrupled, as did inward stocks of foreign direct investment. In 2008 Morocco's macroeconomic picture was relatively sound and its banking system robust. These are significant achievements in the midst of the severe global financial crisis of 2008–09. Nonetheless, as a

Gary Clyde Hufbauer has been the Reginald Jones Senior Fellow at the Peterson Institute for International Economics since 1992. Claire Brunel is a research assistant at the Peterson Institute for International Economics.

small open economy, and one that is highly dependent on remittances and tourism, Morocco stands to suffer from the impact of the crisis on its trading partners, especially through falling demand in the European Union.

Morocco initiated an extensive process of economic reforms beginning in the 1980s, and since 2000 has articulated an agenda of ambitious new projects. Nonetheless, the country's human and social development remains weak, particularly because of low performance in education.

A key dimension of the economic reforms was the opening of the Moroccan economy through trade agreements, notably the Morocco-US FTA. On the US side, the FTA was motivated by the foreign policy objective of cementing relations with a stable partner in an otherwise unstable region. For Morocco, this FTA provided opportunities for new market access, increased investment, and a validation of the Kingdom's progress through economic reforms. The United States provides financial assistance to Morocco for the implementation of the FTA through the USAID, the Middle East Partnership Initiative (MEPI), and the Millennium Challenge Corporation (MCC).

Morocco's Performance under the FTA

Based on a gravity model analysis and the experience of other US FTA partners, chapter 2 shows there is potential for further expansion of both bilateral trade and investment flows between Morocco and the United States in the future. With respect to trade, before the FTA, Moroccan goods had broad access to the US market, whereas entry of US goods on the Moroccan market was restricted. This disparity explains the unequal increase of bilateral trade after implementation.

With respect to the shortcomings of the Morocco-US FTA on the investment front, an essential step for Morocco to attract investment from the United States and other sources is the acceleration and completion of its economic reforms. Progress is crucially needed in liberalizing Morocco's trade regime on a nondiscriminatory basis. Improvements are necessary in transparency and the elimination of corruption. Reinforcement of legal protection for intellectual and other property rights would certainly help. And there is room for improvement in labor productivity.

Agrifood

Assessments of the Morocco-US FTA in the agrifood sector differ between US and Moroccan firms. On the US side, firms have benefited from large trade preferences and from an efficient network of organized associations to promote their exports. US success stories center around firms that implemented long-term strategies, with the help of business associations, to take advantage of the FTA provisions. Some associations, such as the US

Grain Council, prepared for the FTA before it entered into force; through the preferential terms of the agreement, and by establishing relations with their counterparts in Morocco, US grain exporters became more attractive than competitive suppliers.

On the Moroccan side, firms have identified a series of obstacles for their exports to the United States: the burden of systematic scanning at the US border, high labor costs in Morocco, weak logistical support, lack of brand promotion and image, difficulty in meeting the size of orders, and low reliability of Moroccan shipments. Another impediment is that the dollar exchange rate has been unfavorable to Moroccan exports for most of the past three years; the reference point for Moroccan firms is the euro, which has generally been strong against the dollar.

Three major concerns should be addressed. The first is the excessive specialization of Moroccan firms, partly due to the terms of the FTA, in producing red meat and common wheat. Morocco should reform its policy so it is neutral from the standpoint of production incentives and active from the standpoint of public support. The second is that investment in the agrifood sector has been particularly low, despite the opportunities created by the Moroccan government for partnership projects on state land. Third, the United States should dramatically accelerate the liberalization of its agricultural lists, particularly in fruits and vegetables, to open new markets for Morocco.

Textiles and Clothing

Moroccan producers wishing to export to the United States face multiple challenges. Specific to the textile industry, Morocco's role is mainly one of "finishing"—manufacturing products from textile and accessories supplied by industrial clients. However, the fashion industry has now switched to a model of fast retail, which demands the production of finished products without the industrial client having to assemble and ship inputs to the Moroccan firm. To succeed in the new model, Morocco will need to develop its own sourcing system for inputs to satisfy the demand for finished products. Furthermore, since the "fast fashion" model reduces order volumes, cuts delivery times, and increases the frequency of orders, Moroccan firms must adjust to faster turnaround of smaller shipments.

In addition, English-speaking middle management personnel are few and costly to hire. The geographical distance between Morocco and the United States makes it hard to meet delivery deadlines. The strong euro makes the EU market more attractive, especially since Moroccan products are more adapted to the EU market than to the US market. And the industry has changed so that supplier responsiveness is more important than textile quotas, especially as quotas are condemned to disappear. In fact, most quotas are not filled.

Above all, the rules of origin in the agreement are highly disadvantageous for Morocco. The FTA follows the same rules as the North American Free Trade Agreement (NAFTA), which essentially requires textile firms in Mexico to use inputs from the United States. This model is not well suited to Morocco, which is too small and too far away to create an economic "zone" for integrated textile production with US firms. Moreover, since buyers are now demanding the fast delivery of finished products, FTA rules of origin that require Moroccan textile firms to use US inputs don't mesh with the time requirements of the market. In addition, US buyers are discouraged by the costs of complying with complex rules of origin.

Therefore, the main recommendation is straightforward: The rules of origin should be amended to mirror those of the Jordanian and Egyptian qualifying industrial zones (QIZs) or of the US FTAs with Jordan and Israel. Due to the difficulty of returning to the US Congress and Moroccan Parliament to modify the text of the agreement, three solutions are proposed. The first is to establish a list of inputs used in the textile sector that are not produced by either the United States or Morocco and exclude them from the rules of origin. The second is to make use of the provisions for revising the agreement if it does not succeed in boosting trade and modify the rules of origin accordingly. The third is to create QIZs with simplified rules of origin, imposing content requirements for US products (instead of Israeli ones), similar to the Egyptian and Jordanian agreements.

Services

Following WTO terminology (used in the GATS), the Morocco-US FTA covers services in Mode 1 (transborder supply), Mode 2 (foreign consumption), and Mode 3 (commercial presence). Mode 4 was excluded to avoid the contentious issues associated with immigration. The parties used the negative list approach, so all services are covered in the respective modes unless specifically scheduled for exclusion.

The FTA has been useful for Morocco's development as it acknowledges the essential role of services in economic expansion, promotes transparency, and prompted a revision of Moroccan laws to comply with the agreement. However, the FTA has provided few advantages for US firms. Two-way services trade has not expanded much.

One obstacle has been the lack of cultural understanding between the two partners. Services retain a strong human dimension. Understanding the culture of a country improves communication and helps firms adapt to the needs of the market. Therefore, a critical step to developing services between Morocco and the United States would be programs that foster mutual understanding of cultures, a feature that already characterizes relations between Morocco and the European Union.

Further liberalization of trade in services, particularly in transportation and finance, could boost Morocco's economic growth. Morocco's financial sector remains largely disconnected from global financial systems. One recommendation would be for Morocco to continue on the path of measures designed to achieve a degree of integration between the Moroccan and US financial systems. Removing restrictions on the use of credit cards and relaxing the rules for convertibility would be immensely helpful. Administrative controls on foreign exchange should be relaxed so that capital can move more freely. Only then will Morocco be able to achieve its goal of positioning Casablanca as a regional financial center for the Maghreb and West Africa. Proper regulation can ensure the achievement of this goal in a manner that does not expose Morocco to an echo of the global financial crisis of 2008–09.

Aviation

Aviation catalyzes innovation and growth by expanding access to new markets, revolutionizing delivery systems, and facilitating cross-border supply chains. Air transportation should therefore be a key element of a trade development strategy, and indeed Morocco has taken important steps to boost aviation. It reformed the aviation regulatory regime, concluded Open Skies agreements with trading partners, including the United States, invested in airport infrastructure, and aligned goals for air traffic with its national tourism strategy. Yet commerce between Morocco and the Unites States is conducted with only one direct scheduled route, and air traffic between Morocco and the United States has not increased since the Open Skies agreement or the FTA (although the global crisis and downturn in the aviation industry are largely to blame). Thus despite Morocco's efforts, much remains to be done, especially with respect to institutional deficits that hamper trade and aviation sector development.

Tanger-Med, a major port and industrial zone on the Mediterranean coast, has the potential of becoming a global center for the transportation and logistics industry. The integration of air service in the Tanger-Med development plan would bring multimodal efficiency and create new opportunities for Morocco's aviation sector. An air transportation system effectively connected to the new port facilities would help position Morocco as a trade platform for the entire Mediterranean region.

To take full advantage of the benefits of air transport (speed and volume), Morocco also needs to develop an indigenous industry of time-critical manufacturing, assembly, and distribution. As discussed, the production of finished textile products would respond well to this prescription.

Finally, a key ingredient for the success of Tanger-Med is to ensure independent governance and operation of the airport and its logistics platforms. To develop the aviation sector as a whole, Morocco should lift obstacles to private-sector investment in the ownership and operation of aviation systems. Morocco's airport directorate should become an independent agency, and the government should proceed with its plans to privatize the Moroccan national airline, RAM, and end its monopoly status.

Intellectual Property

Intellectual property rights (IPR) were, from the US point of view, a crucial aspect of the FTA. By raising its standards on IPR to the level required by the United States, Morocco hoped to boost the investment potential of the FTA and position Morocco as an attractive investment destination for other sources as well.

Implementation of the FTA provisions for intellectual property is not easy for Morocco. First, the informal sector, including piracy and contraband, is extensive and important in some Moroccan regions, and the FTA's severe penalties on IPR violations will curtail these activities. Second, concerns linger about the FTA's effects on public health and agriculture. Third, the use of new information and communication technologies could raise new IPR issues.

Solutions require management methods that both allow public access to critical knowledge and ensure the protection and defense of intellectual property. Moreover, while Morocco has succeeded in raising the standards of its legal system, questions remain about the competence and independence of the courts.

Data are not available to determine whether strong IPR protection has led to more investment and technology transfers into Morocco. Improvements in the country's business climate, beyond IPR, will remain a key determinant of Morocco's capacity to attract investment. A wider agenda should include better targeting of support policies in the food, health care, and services sectors and the strengthening of Morocco's technological capacity. The government should develop a strategy to assist Moroccans who make their living from piracy and counterfeiting.

With a comprehensive reform program, Morocco will more likely see concrete benefits from its IPR commitments under the FTA.

Lessons from the Jordan-US FTA

The Jordan-US FTA succeeded in boosting bilateral trade to a remarkable extent. It also helped Jordan diversify its economy by broadening the variety of products exported. According to the Jordanian government, the agreement contributed to the creation of over 50,000 jobs and to the tripling of foreign direct investment stocks in Jordan. Since the entry into force of the FTA in 2000, Jordan has grown at an average annual rate of

7 percent (although that rate will decrease to about 4 percent in 2009 because of the global economic crisis).

Important lessons can be drawn from the experience of Jordan. First, the country's chamber of commerce, manufacturers' associations, and consumer groups (with some support from the government) were key in promoting Jordanian businesses in the United States.

Second, Jordan implemented reforms to promote trade and investment, such as measures to expedite customs procedures and to help local firms meet US standards, and partnerships between small and medium enterprises (SMEs) and the academic sector to provide technical expertise to SMEs. Some initiatives benefited from USAID funding.

Third, based on Jordan's experience, a QIZ system in the Maghreb could be a powerful tool for export promotion and development. Shortcomings in Jordan's QIZ are a result of inefficiency on the part of Amman, not an inherent weakness in the model itself.

Finally, the FTA spurred collateral reforms in Jordan, notably in women's rights, labor rights, and intellectual property protection, and it raised awareness of the important role of trade policy in bettering the environment. Overall, the Jordan-US FTA helped Jordan compete more effectively in global markets.

The experience of Jordan can also serve as a caution for Morocco. The prospects of preference erosion due to multilateral trade liberalization and new US bilateral FTAs are sources of concern for Jordan. The benefits of an FTA with a major power, such as the European Union or the United States, should be viewed as a stepping stone, not a permanent resting place.

Lessons from the Chile-US FTA

Chile's successes in exporting to the United States stem in large part from a broad strategy of openness. Nonetheless, Chile offers a number of important lessons for taking advantage of the opportunities offered by an FTA.

Chile's long-standing commitment to openness, combined with stable political conditions, provided a secure and reliable business environment for companies. On a related note, strong institutions underpin Chile's high rankings in business climate indices, which in turn raised the country's attractiveness to foreign businesses and investors.

By expanding its network of FTAs, Chile provided opportunities for domestic companies to diversify their export markets, both in destinations and products, and not concentrate unduly on a few markets. Chile built strong relationships, based on transparency and trust, with trade professionals in partner countries, in part specifically to promote the exchange of information among firms in both countries about opportunities for trade and investment in the other. Thanks to these relationships, when trade conflicts arose, Chile was well positioned to resolve them quickly and efficiently.

Chile also engaged in widespread domestic outreach to advertise the opportunities created by the Chile-US FTA. Thirteen permanent regional offices provide information and answers to questions. A crucial aspect of Chile's openness strategy was the development of its human capital, particularly training for high-technology and English language skills.

Finally, the Chilean government maintained a flexible approach to its economic strategy. For example, it is starting to move away from its previous strict adherence to neutral trade and investment policies between sectors of the economy. Instead, Chile is targeting investment promotion programs to strengthen its technology and services sectors.

Lessons from the Morocco-EU Trade Agreement

The United States could learn from successful aspects of the Morocco-EU experience. The work that Morocco and the European Union have done to align Moroccan standards and legislation with EU norms is often cited as one of the main advantages to trading with the European Union compared with the United States. Through mutual recognition and customs reforms, Morocco has succeeded in removing many nontariff barriers to trade between the two parties. Another strength of the EU agreement with Morocco lies in established institutional links between the two parties, which are being further developed through Morocco's Advanced Status.

The European Union has made noteworthy contributions to Morocco's environmental agenda, as it is prominently involved in all major environmental projects in Morocco and the Maghreb as a whole, notably through Horizon 2020. Moreover, as the European Union continues to move in the direction of tighter environmental regulation, it will export those standards to Morocco. This will affect US companies wanting to invest in Morocco.

Morocco-EU trade relations are important because they affect the political economy of Morocco-US relations. And conversely, one concern regularly raised by Moroccans is that, in deepening its relations with the United States, Morocco must at the same time be careful to preserve its ties with the European Union.

Conclusion

Persistent themes in explaining the low performance of Moroccan exports to the United States include the lack of channels for Moroccan firms to access the information they need to export to the US market, such as standards and customs procedures. In addition, there is little Moroccan representation in the United States to promote Moroccan goods and opportunities to invest in Morocco. The language barrier is consistently cited as a major obstacle to trade. Language is an obstacle to investment as well since US companies cannot find the English-speaking skilled labor they need. Improved training in English would be a major step forward for Morocco for trading both with the United States and with the world.

Because of geographical proximity and historical ties, Morocco will naturally look north to the European Union for trade and investment. Cultural differences are smaller than with the United States. A strong euro against the dollar makes the EU market more profitable for Morocco. Moroccan exporters have established links with the EU market and adapted their production to the needs of that market. Moroccan companies sometimes pass over opportunities to export to the United States because it is easier to deal with the European Union. But they will not successfully penetrate the US market unless strategies similar to those of Chile and Jordan are implemented to put firms in contact with appropriate partners, familiarize them with the rules and standards, and establish a market presence in the United States.

With the right strategies, Morocco and the United States could reap greater benefits from the FTA. Morocco would improve its access to the US market. The United States could use Morocco as a platform for the entire Maghreb and parts of the Middle East and Africa.

As we explained in *Maghreb Regional and Global Integration: A Dream to Be Fulfilled*, the Morocco-US FTA represents a step in the right direction for the economic integration of the Maghreb. Pursuing this theme, the gains from the Morocco-US FTA could be significantly boosted if accompanied by a comprehensive process of regional integration in the Maghreb. Through the FTA, the United States could promote such integration by allowing for the cumulation of origin for products from neighboring Maghreb countries using a QIZ system, specifically by conditioning QIZ-type benefits on zero rate Moroccan tariffs on inputs from other Maghreb countries. The experience of the EU Pan-Euro-Med cumulation systems is estimated to have increased trade flows among participating countries by 43 percent (Augier, Gasiorek, and Lai-Tong 2004). In addition, the United States should encourage the regional harmonization of investment regimes, business regulations, customs procedures, and standards in key industries.

References

Augier, Patricia, Michael Gasiorek, and Charles Lai-Tong. 2004. *The Impact of Rules of Origins on Trade Flows*. Available at http://129.3.20.41/eps/it/papers/0404/0404001.pdf (accessed on July 13, 2009).

Hufbauer, Gary C., and Claire Brunel, eds. 2008. *Maghreb Regional and Global Integration: A Dream to Be Fulfilled.* Policy Analyses in International Economics 86. Washington: Peterson Institute for International Economics.