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Broadening Share Ownership

Final Report

MAY 4, 1994

Price Waterhouse L.L.P.

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Mr. Hassan Amrani, Chargé de Mission auprès du Premier Ministre
Coordinateur de la Privatisation
Département de la Privatisation
Ministère de la Privatisation
Rabat, Maroc

May 4, 1994

Dear Mr. Amrani:

We are pleased to submit the English version of our final report on broadening share ownership. This final report takes into account comments received during our recent visits.

This report contains a substantial amount of recommendations and actions that the Ministry of Privatization could undertake or champion in order to achieve this important component of economic development in Morocco. We encourage the Ministry to perform a legal review of our report to assess what legal changes, if any, might be required for the implementation of these recommendations.

Please do not hesitate to contact us should you have any additional questions or comments regarding this study. We appreciate the assistance provided to us by the Ministry during this activity and look forward to our continuing relationship.

Sincerely,

Auguste E. Rimpel, Jr.
Project Partner
Price Waterhouse International Privatization Group

cc: Susan Riley, USAID

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EXECUTIVE SUMMARY

I. BACKGROUND AND SETTING

Privatization seeks to stimulate a vigorous and growing private sector economy by transferring the ownership and the risk of state-owned enterprises to private ownership. Opening share ownership in privatized enterprises to all levels of society is a key objective of the Moroccan Government's privatization program. Measures to help achieve this objective are the subject of this report.

The report explores the premise that achieving broadened share ownership will require reforms and changes to the current financial system to establish, promote, and stimulate active and vigorous capital markets. It is these markets that channel savings into risk capital, both equity and long-term debt, and thereby make it possible for enterprises to be successful. Morocco is not unlike many developing countries that have yet to develop their capacity to generate long-term savings and risk capital markets. Past misuse of the financial system and the low priority accorded to private enterprise in favor of state owned industries have driven away both the supply and demand for this type of capital.

Thus, the concept of broadening share (i.e. capital) ownership must be considered within the context of the policy, operational and regulatory environment of capital markets. To broaden share ownership is to increase the participation of individual investors and institutions in the capital markets, beyond just equity investments and beyond the privatization program. This requires the removal of policy or legal obstacles in order to create an enabling environment that favors not only the growth of capital markets but the development and modernization of the entire financial sector. It also requires engaging in educational programs which promote public understanding of capital markets instruments and their investment potential.

II. FINDINGS AND CONCLUSIONS

A. There appears to be substantial repressed demand for corporate equities and other securities:

Although there have been no new public offerings of corporate shares since 1985, three recent public offerings, including two privatization transactions, were significantly oversubscribed. This is a powerful demonstration that the capital markets can be accelerated in Morocco and that widespread shareholding can be one of the features of these markets.

Moreover, liquidity among potential investors appears to exist in sufficient volume for new financial investments without jeopardizing the Government's access to the financial resources required to meet its budgetary requirements. The potential investor base in Morocco is significant. It is comprised of individuals and institutions (insurance companies, mutual funds, etc.) with the resources, knowledge and interest required to become active capital markets participants. The privatization program can play a critical role in injecting new life into the capital markets particularly if the enabling environment constraints as defined in this report are addressed.

B. Privatization is Needed to Supply the Market with New Shares:

The most powerful, effective influence that will energize the capital markets of Morocco is the privatization program. The privatization of companies through the equity markets, in whole or in part, will supply new "product" i.e. shares to the markets. The addition of new listings from the Government's inventory of state-owned industries will bring new investment and a whole new class of investors to the markets. The additional product will stimulate trading among the secondary market participants which will improve market liquidity.

C. There is a need to Upgrade the Transparency and Efficiency of Stock Exchange Operations:

The impediments to broadening share ownership are also found in the manner in which the markets are actually organized. Practices that are tolerated by the stock exchange management such as restrictive listing rules, incomplete and untimely transaction reporting, poor quality of disclosure of material information by listed firms to the public, unreliable company accounts, a cumbersome and risky clearing and settlement system and high trading fees for exchange transactions will have to be addressed and corrected in the near future. The goal of more active and vigorous capital markets with the broadest possible participation of the people of Morocco is clearly beneficial to the country and to the stock exchange as well.

D. Government Debt Financing Operations have constrained capital markets development:

The past financial policies of the Government have inhibited the development and diversification of financial instruments and inhibited the growth of the capital markets. The principal distortion in the financial markets results from the practice of the Department of the Treasury in its conduct of government debt financing operations. Both the rates that government will pay and the amounts that will be required are determined by government fiat and not by the market. The effect is to preclude the development of a true market for money and relevant market determined interest rates. This practice exercises a profound repressive influence on all other markets for money in Morocco.

E. There has been Excessive Dependance on Credit for Enterprise Financing:

The Moroccan financial system has not created the institutions and organizations of an active capital market which is yet able to intermediate savings into the risk capital markets. Until recently, excessive reliance was placed on the financing of businesses with bank credit which was dispensed more out of motive to comply with credit targets established by the government than by sound credit standards. Loans often took unusual risks, becoming in effect a form of "quasi equity" which substituted for capital generally supplied by the markets. New systems of bank prudential control are being applied which will bring some rigor to the credit analysis of new credits and which will force potential borrowing enterprises to observe more acceptable standards of corporate finance. In this connection, legal changes may be required to permit the pledging of stock by its owner in financial transactions.

F. There is a Need for New Institutions:

Moreover, the financial system lacks many of the institutions needed for effective capital markets. Such institutions as mutual funds are newly provided for in the law. Others such as investment banks, competing stock exchanges, clearing and settlement institutions, depositories, independent brokers and dealers, will emerge only if the markets continue to develop. In this respect, the regulatory authorities are urged to adopt an encouraging stance toward attempts by industry participants to organize these services which will invigorate life into the capital markets of Morocco.

G. There is a need to Equalize the Tax Burden on all Financial Products:

A tax regime which favors certain financial instruments over others distorts the financial markets. Tax free savings accounts and tax free interest on certain government bonds and notes tend to unduly attract savings into those instruments and away from the financing of private sector growth, pushing up risk-adjusted interest rates for all such companies.

III. RECOMMENDATIONS FALLING UNDER THE RESPONSIBILITY OF THE MINISTRY OF PRIVATIZATION.

Recommendations to achieve the goal of broadening share ownership must necessarily be placed within the context of the capital markets and must acknowledge supply and demand issues as well as the enabling environment. As a result, the implementation of many of the recommendations presented in this report is not within the direct purview of the Ministry of Privatization (M.P.). However, with their vested interest in the successful outcome of the privatization program, they can play a catalytic role by championing the reforms recommended in this report.

A. The Ministry of Privatization (M.P.) should continue and even increase the utilization of Initial Public Offerings (IPO) as a key component of the transaction structure.

- The M.P. should consider alternative procedures in the execution of public offerings which force sales and distribution of shares to be accomplished through networks which reach all parts of the country.

- As M.P. and market institutions gain experience, the M.P. should attempt to involve competing institutions as underwriters to take more responsibility for improving the pricing and distribution of privatization issues, within Valuation Authority guidelines. This measure will assist in developing the professionalism of the industry. The involvement of broad-based mutual funds in specific transactions should be actively encouraged.

- The M.P. should consider incorporating new financial instruments in the structure of its contemplated privatizations.

B. The M.P. should carefully define its targeted investor base and set up systems to track progress.

- Individual investors to be targeted include the top 470,000 urban households with particular concentration in the industrial regions of the Center (Casablanca) and the North-West (Rabat-Kenitra-Tanger). RMEs (Moroccans living abroad) constitute a second base of investors to be targeted, particularly those residing in the European Community. These groups need not be exclusive and attempts should be made to distribute shares beyond these groups to the extent possible.

- M.P. should develop a tracking system to gather data on each public issue and analyze the progress made toward building a population of shareowners. The data for such studies should be easily available from the issue managers and company officials responsible for the register of owners.

- Institutional investors represent a significant portion of investing through OPCVMs. The creation of the latter is predicated on CDVM being operational. (See IV. below.)

C. The M.P. should consider establishing special financing structures to encourage broad participation by special groups such as employees.

- An Employee Stock Fund (ESF) should be established to assist employee purchases of company shares during a privatization. Detailed design of the operations of this proposed fund are presented in section III.B.3.

- The organization of Employee Stock Ownership Plans (ESOP) should be promoted within the corporate structure. The ESF proposed above could be an important means of encouraging worker participation in such ESOPs.

D. The M.P. should undertake regular public relations and educational activities to create visibility for its program and nurture public confidence in the integrity and transparency of it share issue operations.

- Specific recommendations are contained in the Section III.C. that will improve public relations activities towards the general public and target groups of potential shareholders.

- A one day seminar should be organized, for multiple presentation, to the personnel of financial institutions, the press, and potential private issuers and social groups. This should be done in coordination with the Ministry of Finance. The purpose of this seminar is to educate these groups in the operations of the capital markets. A specific scope of the seminar is presented in Section III.C.2.

- A three to five day seminar should be organized for intensive instruction of the members of the press to improve the quality financial reporting by creating an understanding of the new financial markets, transparency, event reporting, material disclosure etc. The detailed syllabus of this seminar in presented Section III.C.3.

IV. MEASURES THAT DO NOT FALL UNDER THE RESPONSIBILITY OF THE MINISTRY OF PRIVATIZATION BUT WHICH ARE NECESSARY TO THE FURTHER GROWTH OF CAPITAL MARKETS.

To create an enabling environment for broadening share ownership, the Ministry of Privatization (M.P.) should champion certain policy and institutional reforms that are the responsibility of other Ministries in order to reduce distortions and inefficiencies that affect the capital markets. The most important of these measures are presented here. More detail about them is presented in the body of the report and in the detailed recommendations in Section III.

- The CDVM is the cornerstone of the development of the capital markets. It is urgent and fundamental for this organization to be in full operation. CDVM will only play its role as catalyst and regulator of market transactions if its management and staff are of the highest quality, aware of their roles and capable of fulfilling their functions.

- Treasury should allow the interest rate on all its instruments to be determined by the market. Treasury debt financing operations should be shifted to a market basis through the use of public auctions and listing of all Treasury's financing instruments. CDG's fiduciary portfolio should also be invested in the market. These measures alone would facilitate the growth and liquidity of a true market in government debt, establishing reference interest rates against which a true yield curve can be developed.

- The capital markets regulators are urged to take an encouraging stance toward the attempt by new groups to organize new capital markets institutions and services. New institutions such as interbank market and money market funds along with investment banks and mutual funds are imminent. The privatization of specialized financial institutions (SNI, BNDE, CIH) via OPCVMs is one example.

- The transparency and efficiency of the stock exchange should be upgraded. These measures include new rules to promote transparency and to enforce them through self-policing organizations of the brokers and members of the exchange. Effective enforcement of proper standards of disclosure of corporate material events and financial performance is an immediate need for listed companies.

- A modern central Clearing and Depository institution to reduce the risks involved in share trading should be implemented. Provisions to make stock pledging legal may also be necessary.

- The stock exchange should either reduce its listing requirements to levels more appropriate to the Moroccan reality, or the regulators should permit the organization of separate "boards", or a separate exchange to list small and medium companies which cannot meet the rather high requirements of the stock exchange.

- Off-floor trading should be limited to trading between principals, under stock exchange supervision with immediate reporting.

- The BVC should mandate currently listed companies to increase the "float" of their shares to meet at least the new listing requirements of 20% of shares outstanding.

- The Finance Ministry should reconsider the present tax treatment of financial instruments to remove the most important inequities among different instruments.

I. INTRODUCTION

A. OBJECTIVES OF STUDY

The success of a privatization program, indeed of any private sector growth strategy, hinges on the existence of active, vigorous markets for risk capital. Capital markets supply both equity capital and long-term loans necessary to commercial enterprises. In the first instance, a successful privatization of existing state-owned enterprises depends on the willingness of both institutions and individuals to invest their capital in these enterprises. However, this is only the beginning stage in that enterprise's relationship with the capital markets. As its capital needs change over time, the enterprise will want and need to access the capital markets in many different ways to provide for its corporate finance needs, whether this be for a new bond issue, a rights issue, new capital infusion, a merger or hedging instruments to cope with various kinds of risk. The Moroccan financial sector will have to develop all these many forms of services in an organized set of capital markets if its private sector economy is to grow and be successful in the world economy.

In designing a privatization strategy, consideration must be given to the supply and demand for shares and the institutional framework within which this exchange operates. Key participants who must be brought into this process and who have a stake in the workings of the capital markets include the Government's representatives in the divestiture of state-owned enterprises (the Ministry of Privatization), the Government's finance authorities (Ministry of Finance/Treasury), and capital markets' participants and regulators including the Moroccan Securities Exchange (Bourse des Valeurs Mobilieres), the capital markets' supervision authority (Conseil Deontologique des Valeurs Mobilieres), stock exchange intermediaries (brokers) and financial institutions (banks and specialized financial institutions). In a broader context, the individuals and institutions supplying the capital and the corporations soliciting such capital have a vested interest in the regulatory and operational framework of the capital markets.

Opening share ownership in privatized enterprises to all levels of society is a key objective of the Moroccan government's privatization program. In recognition of the Moroccan Government's commitment to privatization, the U.S. Agency for International Development (USAID/Rabat) established a Privatization Sector Assistance Fund to support the privatization program. A principal aim of the policy dialogue associated with this fund is encouraging the government to realize the above objective.

The purpose of this study, funded under a USAID/Rabat buy-in to the Price Waterhouse Privatization and Development Project, is to provide guidelines to the Ministry of Privatization (M.P.) on measures it might implement to ensure the effective realization of the Government's objectives of broadening share ownership.

B. CONCEPTS AND METHODOLOGY

The concept of broadening share ownership has many components. From an implementation standpoint, it involves ownership mechanisms which are both direct and indirect. Within the context of the financial markets, it is directly linked to the level of savings and a wide range of instruments for both equity and debt investments. Within the context of the enabling environment, it involves policy, regulatory and operational issues as they relate to each player in the process. Below we provide a definition of broadening share ownership, presenting first its application within the context of the financial and capital markets, and describe the methodology employed to conduct the study.

1. Share Ownership within Context of Financial Markets

The objective of broadening share ownership must be evaluated in the context of a definition of the capital markets. In Fig. 1, an idealized graphic description of the capital markets details the many sub-markets that supply the great variety of the kinds of financing needed by the corporate or enterprise sector. The part that is comprised of equity shares is only one part of the capital markets. Even in most developed markets, trading in equities does not represent the highest dollar volume among all these instruments.

In general, the use of the term "capital markets" is intended to mean the market for long-term risk capital, as opposed to the broader term "financial markets" which also encompasses the short-term operations of commercial (deposit-taking) banks, finance companies and the like which deal mostly in short-term deposits and loans. Normally, as countries develop their financial sectors, the proportion of the total financial sector assets held by the banking sector declines, as more and more activity takes place in the longer term capital markets. In a sample of some developed financial markets, the assets held by the banking sector constituted only some 37% of the total assets of the financial system. By contrast, in a sample of developing country financial sectors, assets held by the banking sector averaged over 70% of the total financial sector, with correspondingly weak capital markets. Thus, the notion of broadening share ownership is in reality another way of expressing measures that would develop and modernize the entire financial sector, especially the long-term risk capital markets.

To acknowledge the breadth of these capital markets, the definition of broadening of share ownership must encompass ownership and trading of all of the various kinds of instruments traded in the capital markets. Initially, this entails participation of the greatest number of the population in the processes of the initial offerings of the SOEs to be privatized. In the following stages, it encompasses participation of the greatest number of investors, either directly or indirectly, in the secondary markets (i.e. the stock exchanges and off-floor trading).

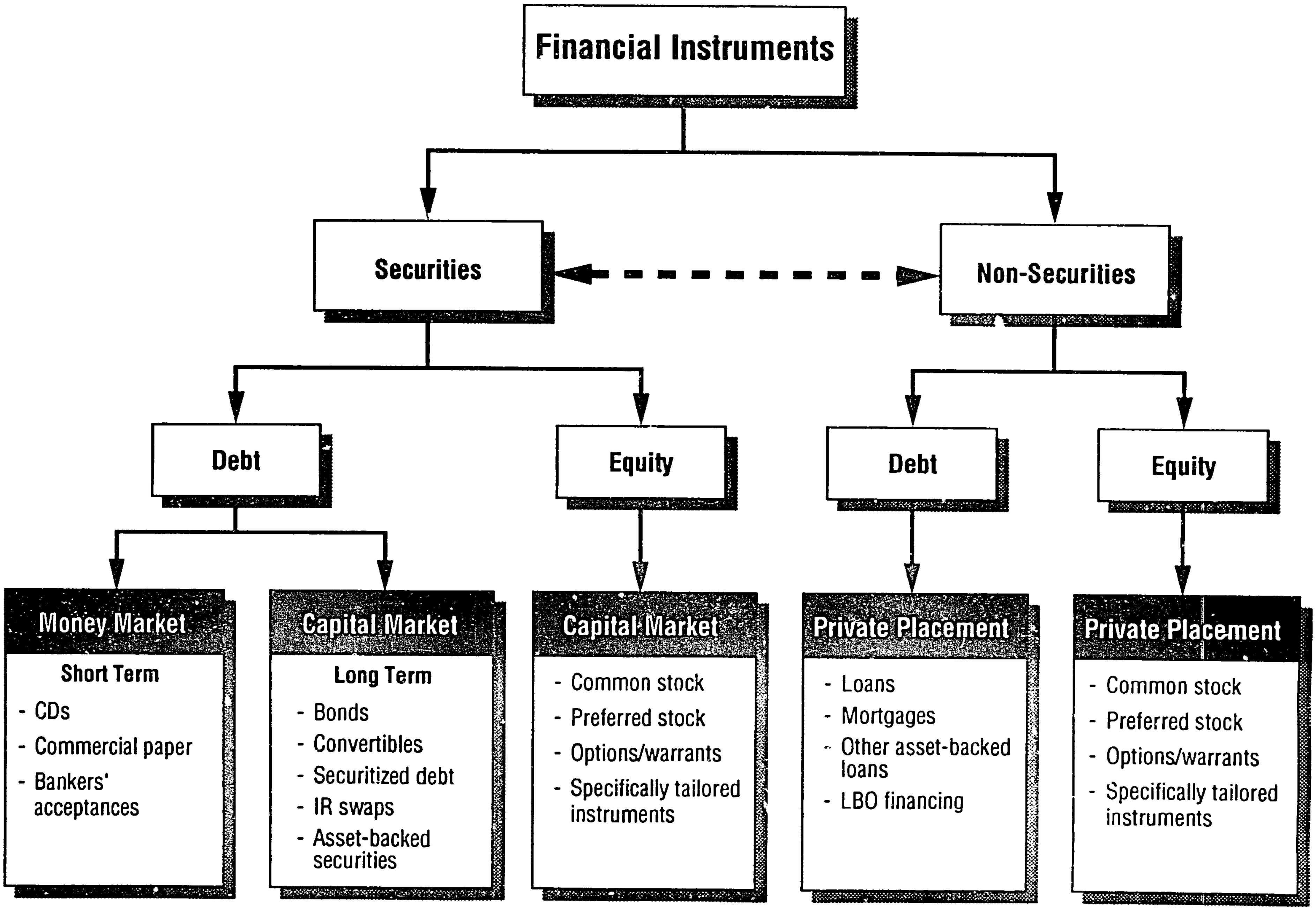

Figure I

USAID Morocco 10/93
Intl IPG

Individual share ownership must also encompass the notion that individuals often choose to participate in trading of shares of equity or debt through their choice of institutions. Mutual Funds are an excellent device to raise the participation level of the individual investor in the capital markets. But, there are other institutions that intermediate between the capital markets and the individual. The most popular of these are pension schemes and life insurance companies. The active participation of these two kinds of institutions (contractual savings institutions) in the capital markets (both primary and secondary) is an important precondition to raising the level of individual participation in these markets. Other institutions that are effective in intermediating savings are such arrangements as ESOPs and other schemes of worker share ownership.

2. Definition of Broadening Individual Share Ownership

Our definition of broadening individual share ownership includes the increased participation of the general population in the capital markets through opportunities to:

- purchase new issues of equity and debt issued by existing private and to be privatized companies

- participate in the ownership of both equity and debt shares in the secondary markets, and to trade these positions as they consider convenient.

Broadening share ownership includes removing the legal and policy constraints to the above goals, enabling the development of investment vehicles and instruments, and engaging in educational programs that promote public understanding of their savings potential. In the final analysis, measures to increase the supply of shares will invigorate the financial markets and will attract participation by individuals and institutions who are seeking to obtain the most favorable returns possible. The major prerequisite for the above is an environment that favors the growth of a healthy private sector economy.

From the standpoint of the privatization of enterprises, M.P. actions to achieve the broadening of individual share ownership include:

- through effective education and public relations, creating awareness among key target groups of share ownership and that such investments are within their reach

- structuring privatization transactions to promote broad participation among the Moroccan populace. This might include:

    * special approaches to public offerings to promote the sale of shares widely throughout the country

* actively promoting new instruments/mechanisms through which individuals can participate in the purchase of shares of privatized enterprises (such as OPCVMs and the creation of a employee stock funds to aid employees to purchase shares in the company they work for)

* restricted tenders to targeted groups such as regional interests or farmers.

3. Methodology of Study

Our methodology was based upon in-depth interviews and data collection with the financial sector (banks, insurance companies and other financial institutions), the Central Bank, the Ministry of Finance (Treasury, Tax, Capital Markets, Credit), the Office of Foreign Currency, the industrial and service sectors, professional associations and social organizations. In drafting our report, the PW/IPG team worked closely with the PW/IPG advisors to the Moroccan privatization program who helped put our findings and analysis into the context of the M.P.'s activities. A list of persons interviewed is included as an appendix to this report.

The final promulgated version of legal texts with respect to corporate disclosure, the Securities Exchange, the creation of new investment vehicles and the establishment of a regulatory agency for the capital markets were analyzed. The recent laws covering the banking industry, mandatory accounting and reporting rules and practices were also reviewed.

As an emerging market, Morocco is changing rapidly which inevitably results in findings and recommendations becoming outdated. Our initial analysis was based upon fieldwork which ended in August 1993 and documented in a draft report issued in November 1993. Market trends and financial sector statistics presented are based upon the most recent available data at that time. (1990 for insurance data, 1992 for Treasury data). This final report has been adjusted to broadly reflect changes in the environment through February 1994 as a means of validating our conclusions and recommendations, although detailed analysis of major new events (such as the CIOR transaction) have not been included and time series have not been extended. This final report also reflects comments to our draft report received from USAID and the Ministry as well as issues which arose during the March 1994 "round table" which might impact our conclusions and recommendations.

The Ministry of Privatization has a full-time legal advisor funded by USAID through Price Waterhouse's contract. We urge the Ministry of Privatization to perform a legal review of selected recommendations in this text in order to identify what legal changes, if any, may be required for the implementation of said recommendations.

C. ORGANIZATION OF THE REPORT

Section II presents our analysis of the key features of the Moroccan financial system which impact the broadening of share ownership. Section III our Recommendations and Section IV presents an Action Plan along with comments on the issues of AID policy dialogue with respect to the Privatization Sector Assistance Fund. Our report is organized along the following broad themes:

- Key Features of the Moroccan Financial System

In Section II.B, we provide an overview with respect to equity, credit, interest rates and liquidity issues. We then present an analysis of the regulatory and operational environment, followed by an analysis of current financial instruments - availability and constraints.

- Profiling Potential Share Owners

In Section II.C we provide an overview of savings levels, sources of these savings and savings channels. The analysis then focuses upon individuals, Moroccans living abroad (RMEs), institutional investors, and employees and special interest groups. Tax related issues follow in Section II.D.

- Issues related to Public Offerings

In Section II.E we provide an analysis of the two recent public offerings, WAFABANK and CTM-LN and a brief summary on the CIOR IPO which occurred after the end of our fieldwork.

Based on the "supply side" diagnostic, recommendations in Section III.A are presented with respect to the execution of future public offerings, the development of new financial instruments, self-policing rules for the stock exchange intermediaries, improvements required to stock exchange operations and the role of Treasury and specialized financial institutions.

The "demand side" diagnostic concludes with recommendations in Section III.B to stimulate demand including the definition of target groups of individual investors and methods to track participation, accompanying tax measures, and issues with respect to special target groups.

Our report also includes a summary of the M.P.'s promotional activities and recommendations to enhance these are provided in Section III.C.

II. KEY FEATURES OF THE FINANCIAL SYSTEM

A. BACKGROUND

The Moroccan financial system has not yet developed the features and institutions necessary to support the financing needs of an active and growing private sector economy. The capital markets which intermediate the demand and supply of long term risk capital are only in a early stage of development.

The banking system, which holds the predominant share of the assets of the financial system, mobilizes short-term deposit money to the extent that government ceilings on deposit interest rates attract depositors. Recent policy changes have considerably improved the environment in which the banks work. The GOM has implemented several reforms and has planned more which will unshackle the institutions of the financial sector leaving them freer to respond to market forces. While most of the practices of mandatory credit allocation i.e. "encadrement" have been swept away, the effects on the bank's ability to operate in a competitive environment given the many years this system has been in effect are still apparent.

Contractual savings institutions such as insurance companies and pension funds are not the vigorous participants in the capital markets that they are in other financial systems. These kinds of institutions are some of the most potent and influential sources of demand for securities in capital markets.

Nevertheless, there are still many practices or controls by the public sector which continue and which cause severe distortions in the markets for money. The primary effect of these distortions is to impede the growth of markets for long-term risk capital. In this section we detail some of the more important issues and distortions which are still prevalent in the financial sector of Morocco, with special attention to those which have the most adverse effect on the further development of the capital markets.

Unless indicated otherwise, the source of the data in this section is the Central Bank.

B. CURRENT INSTRUMENTS AND TRADING

1. Current Issues of Corporate Finance

a. Equity

Evidence gathered by the IMF from the banks supports the perception that most private companies are undercapitalized. Excessive borrowing by larger companies is due to the relative ease of obtaining bank credits. For private companies, most equity has traditionally been mobilized through personal arrangements, i.e. friends and family. The primary capital markets have not been a significant source of new enterprise financing. This is due to many reasons, among which two stand out: Many companies are closely held family businesses that do not wish to share control and distortions and disincentives in the financial system have repressed the development of the capital markets in Morocco.

(1) Domestic Equity:

Nevertheless, Moroccan companies have raised new capital. According to the Central Bank, 2,240 new companies raised initial capital of Dh 838 million in 1991. Another 1,115 existing companies raised their capital by Dh 6 billion. Companies listed on the Bourse des Valeurs de Casablanca accounted for half of this amount (3 billion), of which around 50% was through rights issues (cash) and 50% through stock dividends (incorporation of retained earnings).

On average, companies listed on the Stock Exchange raised Dh 44 million each, existing private business Dh 2.9 million each, and new businesses Dh 375,000 each.

(2) Foreign Equity:

Morocco experienced large increases in foreign direct investment (FDI) during 1991-1992, reflecting both a general expansion of FDI and the institution of a liberal and comprehensive foreign investment policy. The financial sector has been the largest FDI beneficiary, with foreign investment accounting for almost one-third of inflows. FDI originates mostly from Europe, and France in particular. In 1991, direct foreign investment amounted to Dh 2.9 billion[1].

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1 Source: Bank Al Maghrib

b. Access to Credit

Total lending to the private sector amounted to approximately Dh 98 billion in 1991, the year of credit deregulation; it was largely (56%) short term. It had grown by about 23% over the previous year. The Central Bank contributed Dh 11.3 billion (12%), the commercial banks Dh 56.5 billion (58%), and State-owned specialized institutions Dh 25 billion (26%). The corporate sector participated with Dh 5 billion in the form of commercial paper.

(1) Domestic Loans and non-bank borrowing:

Credit resources to industry generally include banks, insurance companies and pension funds, domestic bond issues and foreign loans. Several factors limit the capacity of banks to lend long-term and reinforce their tendency towards the short-term. Limited by the ceiling on lending rates, medium-term rates cannot rise sufficiently to establish a positively sloped yield curve for corporate risk.

The assets of insurance companies, social security funds, pension funds, and special public savings funds are generally required to be invested in Treasuries and municipal bonds, and only perhaps one percent is directly allocated to manufacturing industries. The high concentration of medium- and long-term financial savings in public debt reflects both legal and practical constraints. Legally, insurance companies are required to invest up to 40 percent of their technical reserves in Treasury instruments and Civil Service pension funds can only invest in Treasury instruments. Private pension funds are mandated to hold a portion of their funds in Treasury paper. As a practical matter, the lack of alternatives leads institutional investors to hold more Treasuries than their mandatory minimum.

Private companies have issued short-term commercial paper, which is endorsed by the banks and not subject to government authorization or ceilings; however, issuance of this paper has fallen since the elimination of credit ceilings (encadrement du credit). This is a natural development, since commercial paper generally competes with the banks in the short-term "money market". The previous form of commercial paper was not market oriented, but simply a service from the banks. As commercial lending becomes more advanced and professional, one could expect to see a true commercial paper market develop. Overall, long term corporate bond issuance has not yet developed in the Moroccan financial markets.

(2) International borrowing

Domestic businesses had no recourse to borrowing funds abroad until current Dirham convertibility was established in 1993, leading Citibank to lend $30 million to ONA, the largest domestic conglomerate.

c. Interest Rates

(1) Overview

Interest rates were partially deregulated in late 1990. The rate formula by which deposit and lending rates were determined was changed to be tied to Treasury's cost of funding. Following the deregulation, the ceiling interest rate rose by some 1.7%, to 16.0%. Effective loan rates charged by commercial banks have risen by 2-3 percentage points, from about 12 percent to the current 14-15 percent.[2]

(2) Deregulation and competition

The interest rate liberalization of 1990, together with the lifting of credit ceilings at the beginning of 1991, resulted in sharp competition among banks to attract deposits and to expand their loan portfolio. The actual short-term lending rates are near the ceiling rate. The interest rate ceiling may have been critical in the transition from administered to competitive interest rates and prior to the stringent prudential banking regulations approved in 1992. Nevertheless, the issue facing regulators today is what role the government will play in setting rates. If continued in the future, these ceilings will do more damage to the development of competitive banking and will repress the incentive of the banks to undertake higher risk lending. The private corporate sector and especially newly formed companies will feel the negative impact of these policies most acutely.

(3) Treasury's artificial rate curve

Partial interest rate liberalization has affected the interaction between the two major protagonists of the Moroccan financial system, the Treasury and the commercial banks. The absence of other major independent financial forces has not made the need for a market reference rate apparent. Consequently, there is no real yield curve on which to peg lending rates or relate risk spreads.

Treasury has artificially created a positively-shaped interest curve for its instruments. It is not based on real supply and demand as expressed in the markets. By regulation, it has forced the banks to adhere to it. A true yield curve may develop only by moving the operations of government finance into an auction market system. This would permit the Treasury to remove one of the most market distorting features of the existing system, the Mandatory Allocations, which preempt a high percentage of bank deposit resources for loans to the government at below market rates.

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2 Source: IMF, The World Bank

Both the prerogatives and the obligations of the banks' current short-term financing monopoly should disappear simultaneously to the Treasury's borrowing monopoly. In the future, Banks will be subjected to a prudential control system in which the banks are free to compete with each other as long as their financial viability is maintained. These controls are indirect. Their effectiveness is based on the dismissal of direct controls over bank deposits and lending rates at the same time as Treasury liberalizes its funding mechanisms. Such a liberalization will free the Central Bank from its attempts to control money supply through the banking sector.

2. "Regulatory and Operational" Environment

New laws concerning the capital markets were enacted in October 1993. With the major exception of a law or regulation regarding corporate disclosure, these laws provide a needed base to widen the existing financial system by stimulating the growth of capital markets. These laws create an improved environment, with the creation of new participants and vehicles as well as the redefinition of the role of existing ones.

Inspired by the legal and regulatory framework existing in countries that have successfully developed capital markets, the Ministry of Finance (MOF) has proposed legal reforms that can facilitate the emergence and development of active capital markets. These reforms are generally inspired by the French model, which is prevalent in the whole Moroccan legal system.

These laws lay the necessary bases for market efficiency, transparency and integrity. The reforms focus on (a) the organization and operations of the Securities Exchange; (b) the organization and operations of stock exchange intermediaries; (c) the creation of an authority (Conseil Deontologique des Valeurs Mobilieres or CDVM) responsible for the supervision of all matters pertaining to the capital markets, including control over corporations seeking to issue securities to the public, as well as over the instruments used for that purpose; and (d) the legal base for investment funds (SICAVs and FCPs).

a. Law redefining the role, functions and operations of the Securities Exchange

The Bourse des Valeurs Mobilieres (BVC), the current Moroccan securities exchange, has been operating under a decree dating back to 1967. The reform introduces operating structures and mechanisms that will enable the reformed securities exchange to participate effectively in the financing of the economy. This law defines a new management and operating framework for the BVC, the functions of the intermediaries (Intermediaires de Bourse, stockbrokers) and rules to protect their clients.

The Stock Exchange will be a private corporation, owned by the stockbrokers under a concession of the State. This corporation will earn a commission fixed by the MOF on all BVC trades. It will supervise the performance of all BVC operations, manage the clearing and settlement of transactions, and report to CDVM on deviant market activities. However, this corporation will operate under the direction, supervision and control of CDVM and MOF; it has no independence of action.

b. Definition and Control of the Role and Activities of Stock Exchange Intermediaries

Stock exchange intermediaries must be legally organized and licensed by MOF, through CDVM. Although they may not be a commercial bank or other financial institution, they may be owned by them. The Intermediaires de Bourse (IBs) will be corporations, will have capital according to their type of activities, will contract insurance coverage reflecting their volume and types of operations and will contribute to a guarantee fund substantial enough to indemnify the clients of a failing IB.

Their main purpose is to execute securities transactions, to participate in the placement of new issues, to act as counterparty to their clients' transactions, to do the safekeeping of securities, to manage portfolios and to advise their clients. Their activities must be supported by higher financial, technical, and training requirements and more rigorous control mechanisms. Beside minimum capital requirements and prudential rules regarding liquidity and solvency, stockbrokers will be required to record transactions according to specific rules. Stock exchange intermediaries' activities and financial situation will be controlled by the CDVM, both on documents and in situ, with possible disciplinary and penal sanctions for non-compliance.

The Association des Intermediaires de Bourse ("AIB") will be a new professional body. AIB will have to produce its own ethical and self-policing rules. The existence of such an association will instill confidence in individual investors, heighten their attraction to share and other instruments ownership. Outside technical assistance is recommended to expedite this process. (see recommendation III.A.8.: Self policing rules)

Disclosure of stock exchange intermediaries' ownership, financial situation and results is required and monitored by CDVM. In order to limit conflicts of interest, stock exchange intermediaries' management may not be on the board of directors of companies whose shares they trade or hold in portfolio.

c. Law creating CDVM, a supervisory authority to control capital market operations

(1) Role

This law redresses many past shortcomings regarding corporate disclosure and regulation of public offerings and securities trading. It defines the process of public offerings of securities to the public, expands the information required from issuers of securities and establishes an agency (CDVM) responsible for the supervision and enforcement of the above requirements and proper market operations.

CDVM is created as a financially autonomous State agency to supervise the issuers, their public issues, the instruments of these issues, the capital market operators, the transparency of their operations and their disclosure. Its statutes are dictated and its members are nominated by the MOF. CDVM has been vested with five essential tasks:

- to supervise and control corporate compliance by corporations issuing securities to the public to disclose material and financial information to shareholders and the public at large: the statutes define the obligations of the issuers to inform fairly and permanently and provide a definition of insider and distorted information;

- to provide assurance that public offerings are supported by an appropriate information memorandum, the contents of which it may dictate and modify;

- to control the securities exchange management corporation, stockbrokers, security safe-keeping, mutual funds and other issuers;

- to generally maintain market integrity by investigating public complaints and by applying severe sanctions for use of insider information among others.

- to advise MOF and to propose appropriate regulations regarding the above.

(2) Operations

The CDVM law is the cornerstone of the financial market reform. The law will be operational upon completion of the statutes and regulations of the agency itself, which are being drafted currently. Without the regulatory foundation in place, the development of active and vigorous capital markets will be jeopardized. The CDVM will play its role as catalyst and "controller of the market" only if its management and staff are of the highest quality, fully cognizant of their role and capable of fulfilling their function.

(3) New Issuers and Instruments

CDVM will also be responsible for the introduction of new instruments. The basic rules for structuring and trading such new instruments as debentures, preferred shares, investment certificates, convertible bonds, warrants, commercial paper and securitized instruments (such as mortgage-backed securities currently studied under another USAID program) will have to be established by this authority in order to expand the range of products offered through the markets to an expanding base of investors.

(4) Pledging of shares

The pledging of shares is not currently done and it is uncertain whether the law governing the capital markets permits the pledging of shares so that they could be used as collateral for other economic transactions. This may be a deficiency. We would strongly recommend that if necessary, amendments to the law be considered to permit the pledging of shares as collateral for loans or other financial transactions. In addition, the ability to pledge shares will facilitate stock lending which in the future will greatly facilitate market liquidity.

d. Law on Investment Vehicles (OPCVM)

The MOF has set basic legal guidelines for the creation and transparent operations of the new investment vehicles.

Two investment vehicles are allowed: SICAVs (Sociétés d'Investissement à Capital Variable, or open-ended investment corporations) and FCPs (Fonds Communs de Placement, or open-ended investment funds). Both vehicles have proven to be effective in channeling individual savings to the capital markets. Their success has resulted mainly from the operating simplicity, security, and liquidity that these vehicles offer to investors.

Their introduction creates one of the most powerful financing mechanisms to broaden the investor population, as well as some of the most potentially influential institutions of the capital markets. Their format, regulatory framework and operations provide basic security and protection to investors.

(1) Definitions of SICAVs and FCPs

These vehicles are financial intermediaries; their sole purpose is to manage risk diversified security portfolios and to maintain the liquidity necessary to meet their legal obligation. Their features are particularly useful in markets lacking trading liquidity. They serve to stimulate demand of individual investors through organized marketing and selling efforts, including advertising.

SICAVs issue and repurchase shares at the current market value of their portfolio, upon request of the investor. The value of each SICAV share is established frequently and is pro rata to the value of the investment portfolio net asset value. It must be certified each time by an independent auditor. SICAVs are managed from within; they issue to and repurchase shares from their shareholders. SICAV shares can be nominative or bearer and can be traded on the stock exchange.

The portfolio of FCPs are managed by outside investment advisors. They issue nominative certificates that represent a portion of an undivided interest in the investment portfolio. The value of the certificate is pro rata to the value of the investment portfolio net asset value.

(2) Operating conditions

The purpose of the regulatory conditions imposed on OPCVMs is to provide security to investors. OPCVMs are legally bound to operate entirely for the benefit of their investors. The MOF reviews the proposed statutes, minimum capital (Dh 5 M), strategy, procedures and operations of OPCVMs prior to authorizing their sale to the public. Sales must be paid for in cash immediately. The CDVM supervises and controls the transparency and adequacy of their market operations and may suspend their activities when losses exceed 50% of their capital.

The share certificates composing the portfolio will be kept by an arms-length custodian or depository company, a list of which is defined by MOF. Such depository must establish the OPCVM's inventory of securities at least quarterly. Both depositories and management companies must prove that their staff, technical and financial means are adequate for the proposed operations and are jointly and severally responsible towards the investors.

As mentioned, the MOF has set basic legal guidelines for the creation of new investment vehicles and transparency of their operations. While some guidelines should be relaxed (eliminating such statutory requirements as setting fees and commissions), others could be enhanced by additional voluntary disclosure and flexibility.

(3) Obligations and control

OPCVMs are subject to the same information requirements imposed upon all corporations seeking public investment. Their initial information memorandum must include a clear statement of their investment strategy. OPCVMs must follow risk diversification guidelines set to limit excessive exposure to any one issuer at the exception of the State. As there are few offerings, Treasury will benefit initially from this rule.

The sponsors of OPCVMs must declare their ownership in the investment company and the mechanism whereby their shares may be sold or their participation may be increased. They may not give self-serving instructions to the portfolio manager, must include at least two outsiders on their Board of Directors and must disclose security transactions with their OPCVM if such trades are off-market. Heavy sanctions provide a strong incentive for proper compliance.

e. Other Participants

Other financial market players are commercial banks, the Treasury, the insurance companies as well as the Specialized Financial Institutions. Their role and potential for Broadening Share Ownership is described in Section C: "Profiling Potential Share Owners".

3. Bourse des Valeurs de Casablanca

a. A Single Class of Equity Share:

Moroccan law does not generally separate the right to share in profits from the right to vote, with two specific exceptions noted below. Thus, financial instruments such as non-voting shares with priority dividends, investment certificates, and other participatory share instruments are not recognized.

Conversely, the law provides the means to confer certain privileges to holders of certain shares in the statutes. By means of "privileged shares", it is possible for a group possessing less than half of a company's capital to carry a majority representation at all general shareholder assemblies ("shares having a plural vote") and/or a majority on the board of directors ("priority shares for allocation of board seats").

Both of these provisions of the law will serve to repress the growth of share ownership; the first by limiting the kinds of equity instruments that can be issued, and the second by locking up the control of corporations into the hands of a few.

b. Listing on the Exchange

Certain conditions will be imposed on the issuers and the securities issued. Issues will be authorized by CDVM according to the size, structure, capitalization, disclosure and past performance of the issuers. Independent financial audit requirements apply to all issuers. The regulatory standards that will apply to both issuers and securities are:

(1) Corporate Conditions of Issuance

- The company must be incorporated in a form following recourse to financing by the public (S.A. and S.C.A.)

- Minimum paid-in capital: Dh 15 M

- Minimum existence: 3 years
- Audited and certified accounts: 3 years
- Minimum float of 20% of capital

(2) Conditions of issuance of securities

- The issue is minimum Dh 20 M
- The issuer meet the corporate criteria
- The minimum nominal value of shares, currently Dh 50, is not mentioned. BVC customarily sets it at Dh 100
- Instruments issued or guaranteed by the State and municipalities are listed automatically and without conditions.

In addition, foreign corporations may list upon approval of the MOF.

Given the information we have reviewed earlier concerning the capitalization of new companies and the average sizes of capital increases of existing companies in Morocco, it would seem that the above conditions for listing are too restrictive.

As set by the law, the minimum issue size is 4 or 5 times the current average capital of many existing companies. Such restrictions will preclude many potential issuers from access to the capital markets. It would be advisable for the authorities to lower these limits to ranges that more closely approximate the Moroccan reality. This could be done in several ways. The limits for the BVC could be lowered, or alternatively, the authorities could sponsor a separate "board" or "second marché" (similar to the Over the Counter Exchange of India) on which new issues of small and medium size companies would be listed. The conditions of listing would be much lower and would recognize small and promising companies.

It is also unnecessary to limit the listing of new issues to those that have three years of audited financials. Many newer companies of great promise, and equally great risk, are thereby excluded unnecessarily from acquiring new capital infusion. At the same time, many investors are precluded from sharing in the opportunities and the risks of investing in such enterprises.

The usual argument for these restrictions stress the need for investor protection from scams or false investment schemes. This is a valid goal of regulation, but the manner of exercising this protection by excluding companies from presenting themselves to the investing public is damaging to the markets. The emphasis of the regulator is better placed on ensuring that all companies issuing shares to the public undertake rigorous disclosure obligations. As long as the risks of an investment are properly presented, the regulator should leave it to the judgement of the potential investor to decide if he will invest his funds and at what price. Only he can properly appraise his tolerance for risk.

c. Trading on the BVC

Trading volume has ranged between 1% and 3% of market capitalization since 1989. There were 14 members, including 12 banks registered on the Bourse des Valeurs de Casablanca ("BVC"), the Moroccan stock exchange. These stockbrokers reported unprofitable operations. Trading commissions, even if high, did not cover fixed charges. Despite their operating losses, none of the stockbrokers discontinued operations. Their losses were offset by their parent institutions.

Stock Exchange activity has been limited. Share transactions traded on the floor made 2 percent of BVC volume in 1990-1991, compared with registered off-floor share transactions of approximately 20 times more shares and 15 times more money. Most on-floor trading has historically been in government and state-owned enterprise bonds, not company shares. The trend now seems to be toward company shares, as for the first time in 1992, share trading made over half of BVC's volume.

Inactive equity trading on the Stock Exchange is more an indication of the lack of new issues than it is evidence of the lack of investors. This is demonstrated by the recent WAFABANK, CTM-LN and CIOR public offerings, all of which were significantly oversubscribed.

The customary existence of off-floor trading among large institutions must be seen in the context of glaring inefficiencies in the operations of the BVC, which include high costs and inefficient settlement conditions. Thus the conditions which give rise to off-floor trading also repress BVC trading activity generally. These include (1) restrictive listing rules, (2) weak laws on disclosure and minority shareholders protection, (3) unreliable company accounts, (4) a cumbersome purchase, clearing and settlement mechanism, and (5) high stock exchange fees.

The BVC has been as self-contained and geared to the status quo as Treasury, the banks or the CDG. Serious reforms to open the operations of the exchange to scrutiny and reform as well as modernize its procedures will be necessary before it can attract much larger volumes of listings and trading activity. Once these reforms are made it will be necessary for the regulator to order that off-floor trades be reported within minutes of striking the agreement. This reported volume and price information should be incorporated into the exchanges reporting of trades in sequence with other trades and be made available to the public in accordance with its rules.

In the Annexes to this report are graphs depicting trading trends as well as comparative information on other emerging markets. (See Annexes 5 and 6 in particular.)

d. Off-floor Transactions - "Cessions Directes"

Market making is off-floor, among large stockholders. Off-floor trading has represented historically over 90% of BVC's entire share trading activity. As expected, the most actively traded shares off-floor are also more actively traded on the floor; off-floor transactions were only 70% of the total traded volume of these shares. Off-floor trading has stemmed from the lack of trading liquidity in the market and other constraints such as the high commissions charged by the BVC.

With the new reforms, the MOF has maintained off-floor trading. MOF recognizes that its lack of transparency is a weakness, but that it is compensated by its ability to generate some liquidity. The need for transparency can be satisfied by limiting off-floor trading to trading between principals only, requiring trades for third parties (i.e. brokered transactions) to be made on the exchange, and imposing rigorous reporting rules on transactions between principals as noted above.

Ultimately, the existence of off-floor trading will be determined not by regulators, but by the effectiveness of the stock exchange in offering such attractive services that institutions prefer to conduct their trading through its mechanisms. As the market becomes more developed and serves more clients with more issues, the opportunity is presented for the exchange to make itself attractive to all investors.

4. Other Financial Instruments

a. Corporate Bonds

There is no history of corporate bonds issuance which is only subject to Ministry of Finance notification. Upon reception of a bond issue notification, Treasury has the right to oppose it for reasons of (i) rates being lower than its own 10 year bond or (ii) dates conflicting with Treasury's own issues.

The 1946 law covering corporate bonds has been abrogated in the new financial markets laws. It would be advisable for the Treasury to drop all controls on the issuance of bonds by private corporations in the local market, leaving them subject to the requirements imposed on all issuers by the CDVM.

b. Government Securities Operations:

The Government of Morocco through its Treasury engages in debt financing operations that profoundly influence the character and direction of the financial system. It is one of the principal conclusions of this report that these operations, as currently conducted, repress the financial markets, particularly the further growth and development of the capital markets. In Annex 3, there are graphs depicting Treasury borrowing.

(1) Government Debt Instruments:

Total Treasury borrowing outstanding stands at some Dh 67 billion as of December 1992. These funds have been mobilized though the issuance of 32 different types of domestic instruments. Thirteen of these instruments are short-term, i.e. of one year or less. Thirteen of these instruments are medium term, between two years and five years, and six issues are for terms of six years or longer. The banking and insurance sectors purchase the vast majority of Treasury issues, mostly on instruction and on terms determined by the Treasury.

(2) Mandatory "plancher" bonds

Commercial banks must invest deposits in government bonds (the "plancher" requirement). At the end of 1992, the Treasury paid only about 4.25% on Dh 17 billion of "plancher" notes representing some 15% of the banks' total income-earning assets. This rate was about 10-11 percentage points below corporate lending rates. This mandatory allocation accounted for about 26% of Treasury indebtment, and was 6 to 8 points below usual Treasury borrowing rates.

On the remaining Dh 50 billion of domestic debt, the Treasury paid rates ranging from 8.5% to 13%, with an average of approximately 11.5% on maturities from 1 week to 15 years.[3]

(3) Bonds

Various bonds worth Dh 31 billion accounted for 46% of all Treasuries in 1992, bearing interest rates at 11-13%. Earnings were tax-free on Emprunts Nationaux for individuals until June 1993 and there was an arbitrage market for them on the BVC, where insurance companies were buying them.

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[3] Source: Bank Al Maghrib

(4) Short-term bills

With of over Dh 11 billion outstanding, Treasury's 3-6 month tax-free bills which then paid 9.5-10.50% were sold daily to individuals, corporations and the financial sector through the General Treasury and the banks. Addressed to institutional investors, the 6 and 12 month bill auctions (started in 1989) yielded about 12% in 1992 on an annual basis. These types of issues are often under-subscribed as banks can lend at higher interest rates (although at higher risk) to businesses. The auction is perceived as functioning poorly. The government plans to improve the transparency of the auction system, to lengthen maturities, and to allow "blue chip" private businesses and individuals to participate.

(5) Issues

The financial policies of the Treasury tend to have a weakening effect on the financial sector, increase the cost of funds to the whole economy, and discourage the growth of the capital markets. The key issues associated with current Treasury debt operations are:

(a) Mandatory Allocations

Mandatory Allocations are the amounts of a bank's deposits that must be provided to the government as a "loan" at less than market rates of interest. In the past, Treasury has relied on the liquidity developed in the banking system and among insurance companies and pension funds for financing government operations. These funds were preempted from these organizations by direction and at various rates.

So far, Treasury seems to have lacked satisfactory evidence to move it to eliminate mandatory allocation of financial resources by the banks and other institutions. The existing Treasury policy of mandatory financing is a system based on the beliefs that (a) national savings do not exist in sufficient amounts to fund both Treasury operations and the private sector, (b) market-driven rates may not be controllable and (c) market rates would increase the borrowing costs of the State. As a result, Treasury has not gained much experience in the trading of financial instruments or the auction process for original sale of government paper. Nor has it gained experience from co-existing with corporate bonds since none have been issued.

These policies tend to supplant the market and make it irrelevant in the setting of interest rates. In addition, they limit the capacity of the banks to invest their liquidity in productive private sector business and preclude insurance companies from investing in the long-term risk capital markets.

(b) Interest rate controls

Treasury has structured more market-binding agreements, which are all designed to ensure the predominance of its borrowing over other sources of demand for funds. In some cases the risk-free treasury bonds offered by Treasury tend to attract resources away from the capital markets where they might otherwise be invested in shares.

Treasury has legally segmented its funding instruments by lending groups (banks, non-banks, individuals), to assure (a) its top borrower position in each group and (b) no rate competition among these groups.

- By prohibiting interest-bearing checking accounts, it has provided banks with an inexpensive source of funding for their mandatory allocation. The practice ensures that banks will earn a gross spread of 4.25% on the mandatory assets. However, Treasury has allowed the Tresorerie Generale to offer interest-bearing checking accounts to individuals; this "service" is competing directly with the non-interest accounts of the banks.

- Treasury has put a ceiling on the interest paid by the banks on passbook accounts. This ceiling is set under a formula rate of Treasury's own "market" cost of borrowing, thereby allowing Treasury to offer more attractive rates on similar maturities.

Treasury operations should do away with these controls and practices and move government debt financing toward a market basis, with new issues being auctioned at true market prices. In the context of professionally designed auctions, Treasury would most likely find that its concerns about losing its traditional funding sources would be unwarranted. In fact, Banks would be among the bidders for this new government paper as would other institutions including insurance companies, pension funds, mutual funds and individuals.

c. Mutual Funds

As described earlier, the new laws have allowed the creation of Organismes de Placement Collectif en Valeurs Mobilieres (OPCVM). The following is a description of the Maroc Privatisations OPCVM and conclusions that can be drawn from the implementation of this new instrument.

This mutual fund was created under French law to invest an initial amount of FF 20 million (Dh 30 M): 50% in French fixed income instruments (to ensure minimum returns and liquidity) and 50% in shares of privatized companies in Morocco. Its target investors are French RMEs. The fund, created by SGMB (Societe Generale de Banque Marocaine), will be managed initially by Societe Marseillaise de Credit, which already manages 3 such funds in France, Spain and Italy. The fund will establish a weekly liquidation value for its shareholders.

For SGMB, this fund is a first exposure to managing capital. Actual operating systems might not be transferred to Morocco for some time. Although this fund is the first one to have been advertised, SGMB does not expect that market regulations will be operational in the near future, by which time slower competitors will be ready also. SGMB expects that all OPCVMs including its own fund will grow tenfold within the first 12 months of their existence.

Assuming that the financial institutions carry out their stated intentions, 10 funds will be established as soon as CDVM becomes operational. If the size of Maroc Privatisations is representative, there will be an investment pool of some Dh 300 million available for privatization at that time. According to SGMB's forecasts, that pool would grow to Dh 3 billion within a 12 month period. If all by transfer from bank deposits, this pool would not dent the banking resources much: the growth of the new financial markets might not cause any major short-term disruption of the financial system.

d. Commercial Paper

From 1986 and until 1990, commercial paper was a means for banks to arrange financing outside of their credit ceilings (outstanding Dh 7 billion at year-end 1990). Bank credit deregulation later resulted in reduced outstandings (Dh 5.3 billion at year-end 1991). Commercial paper may be issued with maturities from 1 to 6 months and must be endorsed by a bank. Although trading in commercial paper is allowed, banks are not permitted to hold it in inventory, thereby effectively limiting its issuance. In addition, a Central Bank circular to state-owned enterprises forbids them to invest in commercial paper, thereby forcing them towards Treasury instruments[4]. Commercial paper is inherent to the money market and often attractive to park short-term liquidities.

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[4] Source: Bank Al Maghrib, MOF

5. Constraints to Share Listing/Trading and General Conclusions

We have already covered the constraints to the capital market caused by the preemptive actions of the government debt market operations. What follows are other constraints inherent in the securities market itself.

a. There is a Lack of "Product" to Sell in the Capital Markets.

The most important reason for the lack of dynamism of the capital markets in Morocco is the lack of companies bringing shares to the public markets. The privatization of former SOEs will measurably add to the number of companies on the exchange. There are many reasons for a lack of product: the relative ease of obtaining bank credit which in effect becomes a form of "quasi-equity" which reduces the motivation of company owners to sell equity to the public; the rudimentary state of formation of the securities markets participants which promote market growth; the lack of participation by the contractual savings organizations which normally channel savings into the securities markets; the poor regulatory climate of these markets; and the failure to establish proper disclosure standards that make for a level playing field for all participants.

b. Bank Credit is the Prevailing Method of Enterprise Finance.

The tax structure, as in many countries, favors interest over equity capital. Companies tend to borrow the maximum amount possible, even in excess of reasonable and prudent ratios of debt to equity if they are permitted to do so by the banks. In such circumstances, companies have little or no incentive to raise capital to support their corporate finance needs. The same set of circumstances explains the lack of a securitized debt market. There has been no incentive to raise debt through the capital markets as long as credit was available from the banking system.

Unsustainable debt burdens may inevitably cause the performance of corporations to fall and will jeopardize the financial health of the banks. As prudential norms begin to take hold, the banks will be forced to face up the potential losses due to the failure to employ proper credit standards in the lending process. Policies will change, and companies will feel the natural signals of the market and will be forced to seek new capital, and long term debt, to support their growth needs.

In addition to the elimination of "encadrement" and other controls and ceilings on credit and interest rates, the elimination of mandatory "crowding out" by the Government will put the banks into a position where they can compete. The imposition of prudential norms for borrowing will prevent the banks from issuing loans that effectively substitute for equity in companies with excessive debt to equity ratios. Under these conditions the banks return to the proper role of banks and the need for the risk capital markets becomes apparent to all participants.

c. Companies Have Tended to Limit the "Float" of Shares on the Market.

The new law requires that companies have to list a minimum of 20% of their shares outstanding. It has been estimated that many companies listed under prior rules listed less than this amount. World Bank sources estimated that only an average of 6% of outstanding shares were listed. If there are fewer shares available for sale, there will be less trading.

This condition is reinforced by the practice of companies to incorporate reserves into capital and to issue stock dividends to its existing shareholders. This practice tends to concentrate any increases of shares in the same hands that hold the original shares. This practice is acceptable to institutions or other investors that are prepared to accept non-cash dividends.

It is also said that the rights issues are always fully subscribed by existing shareholders, thus limiting the number of new shares that could reach the portfolios of new investors from this source.

Through its listing agreements, the BVC should force the companies to take more responsibility for inactive trading of their shares. This could require the company to list a greater proportion of total outstanding shares through public offerings in order to maintain its position on the market. Companies that do not meet the minimum of 20% of shares outstanding listed should be mandated by exchange authorities to reach this minimum over a reasonable period of time (1-2 years).

This and other measures to subject the banks to prudential norms of banking increase the pressure on company boards to institute measure to make their companies more attractive to the capital markets.

d. Market Capitalization is not Representative

Market capitalization is artificial when a few trades without liquidity are used to set the value. It has limited meaning when it is calculated only on listed shares which are being traded, which may represent only 6% of the total listed shares (source: the World Bank). During April 1993, trading in only seven shares accounted for 94% of BVC volume. The capitalization of these shares represented 56% of the market's. Annualized, official floor trading in these shares in April was less than 4% of market capitalization. In 1992, trading in the same companies ranged between 0.7 and 7.3% of their market capitalization, excluding WAFABANK, whose public offering happened in December 1992.

e. Disclosure is Incomplete and Reporting is Deficient

Disclosure on the BVC is inadequate and advertising has been poor, rendering it difficult to create a clear picture of the stock market activity through BVC's reports.

The data produced in the annual and monthly reports is not standardized, thereby making reconciliation and cross-comparisons difficult. The information selected and its commentary generally address activities favorable to the BVC. BVC does not publish its trading volumes in daily newspapers. Off-floor transactions are not reported regularly in commercial publications. Although the size of current volumes may not justify this additional effort, regular reporting would be useful in the future.

BVC generally records each actual movement of a share as both a buy and a sell transaction, thereby doubling the volume of its activity. Although it may be a convenient method to calculate BVC's commissions (which are charged on both buys and sells) it is not illustrative of the real trading volume and tends to mislead the public. (All calculations herein have used BVC's methods, thereby effectively doubling all Dh volumes measured on a real transaction basis.)

f. Antiquated Operations

No major inefficiency has appeared at current trading levels. In the context of the new financial markets and higher trading volumes generated by a larger group of investors, BVC's antiquated operations will become constraining.

BVC is anticipating this possibility. Its management is currently contemplating moving the Exchange within two years to more appropriate quarters. The move will be accompanied by a hardware update assimilated to software changes which will include a new stock index. To that effect, the BVC is negotiating with the Lyon and Montreal Stock Exchange to acquire their systems and with manufacturers (including an American one) to provide the supporting hardware for installation at the new site.

g. Few Knowledgeable Issuers

After completion of the privatization program, many issuers will be private companies. They are currently not well prepared for the role. Private companies, many family owned, do not generally need transparency or knowledge of the financial market to operate. Generally, their corporate assets contain a large and family-owned real estate component to serve them in times of difficulty.

As highlighted above, in 1991, the average initial business capitalization of a privately-owned business was Dh 375,000; average capital increase was Dh 2.9 million for privately-held companies and Dh 44 million for companies listed on the BVC[5]. Since only a few of the listed companies actually raised capital that year, their average is lower than the actual capital raised, but the point remains: corporate needs vary enormously depending on corporate ownership.

5 Source: Bank Al Maghrib

C. PROFILING POTENTIAL SHARE OWNERS

1. Overview

In Section I of this report, a definition of Broadening Individual Share Ownership is provided. This section attempts to define a population which may serve as a realistic base for broadening share ownership. In the Annexes to this report, tables and graphics depicting statistics and trends in this regard are included. (See Annexes 1,2 and 7 in particular.)

Morocco's most privileged 10% of households collected some 31% of the country's revenues in 1991. Yet, lack of data on income, earnings and financial transactions prevents the determination of savings and their availability for investment. We had to define a tentative target of potential share owners by using the consumption survey from census data collected by the Direction de la Statistique, Ministry of Economic and Social Affairs in 1991.

a. Savings Levels

Savings seem to exist in enough volume to enable new financial investments without jeopardizing Treasury's access to the financial resources needed to fund the requirements of the State. Whereas no formal analysis of savings exists in Morocco, evidence suggests that savings do exist in sufficient volume for stock investment:

- pension funds and life insurance are growing steadily: Al Amane, a major insurance company launched and sold 6,400 policies of a new annuity over a two week period in June 1993;

- real estate construction has grown without extensive recourse to housing credits;

- together, the WAFABANK, CTM-LN and CIOR issues have directly mobilized an investment in excess of Dh 1.3 billion;

- by extending the average individual cash mobilization in the recent stock issues to the potential targets, the available stock investment pool appears to be in a range of Dh 10-80 billion;

- over the last few years, bank deposits have grown by some Dh 10 billion annually;

- an estimated 40-50% of all banknotes in circulation might be hoarded (Dh 14 billion);

- the Centre Marocain de Conjoncture figured that 40-70% of the country's economy is informal; in current macro-economic terms, it could translate in an estimated range of informal savings of Dh 34-50 billion (before tax);

- the 1975 Sahara bond mobilized Dh 100 billion, some 10 times the then existing financial resources; this issue stressed savings: the Central Bank took 8 years to reabsorb the money supply created by the large amounts that were soon returned; yet, in relation, it might suggest that a savings pool of some Dh 100 billion exists today.

The soft evidence gathered above supports the World Bank's view that a sizeable stock of savings may be available in various forms.

b. Individual Contribution to Savings

According to the Bank Al Maghrib, in 1991, individuals appear to have saved approximately Dh 4-5 billion in the form of bank notes (calculated on the basis of cash rotation), Dh 5-6 billion in sight deposits, up to Dh 7 billion in time deposits, Dh 1.5 billion in Treasury instruments and some Dh 2-3 billion in corporate capital, for a total estimated at Dh 20-22 billion. Excluding real estate investments, individual savings in 1991 are nearly half the financial savings of the formal economy (Dh 43.8 billion) and about the size of the whole privatization program.

More striking is the fact that about 50% of newly created savings were kept in cash form. In addition, about 70% of the financial savings stock of Dh 130 billion held by individuals was in banknotes and sight deposits. Although a population with relatively low means would make provision for short-term needs, so much liquidity is also symptomatic of a lack of attractive investment alternatives. The exception to this is Treasury instruments. Supported by attractive interest rates and a tax-free status, individual investment in Treasury instruments have grown by Dh 2.2 billion over the 1991-92 period, almost entirely from the 6 and 12-month bills on tap.

Another point relative to equity investment is the amount of cash actually committed by investors for their subscriptions to the three public offerings (WAFA, CTM-LN and CIOR). In each case, unmet demand was some DH 600-1,000 million. The money flushed out by the offerings is the actual proof of investors' demand. The mitigating factor is that investors, knowing that they will be served less than their subscription, subscribe (and have to make payment) for more than their contemplated investment. This problem could be eliminated by closing the subscription periods as soon as there is evidence that it has been filled. (See Recommendation A.2 in Section III.)

The annexes to this report provide various statistics which support the above analysis and conclusions.

2. Current Savings Channels

a. Caisse d'Epargne Nationale (CEN) Passbook Savings Accounts

The CEN is a semi-autonomous arm of the National Office of Post and Telecommunications and is subject to Ministry of Finance supervision. It gathers deposits through the post office's branch network, which covers approximately 85% of the communes in Morocco, and is a funnel for RME remittances. The CEN was offering in 1992 a passbook savings account earning 9% p.a. which, unlike deposit accounts in commercial banks, is tax free. There are about 620,000 passbook owners, carrying an average Dh 3,400 deposit each as of 1991[6].

b. Commercial Bank Deposit Accounts

Commercial banks offer passbook savings accounts paying the current legal ceiling (8.5% as of December 1993). They negotiate rates on term deposit accounts. All are subject to taxation according to the individual or corporate tax laws. These deposits make the bulk of savings and liquidity.

There were about 1.7 million individual checking and deposit accounts, worth altogether about Dh 90 billion as of 1991. The average bank deposit was Dh 21,000. This immediate liquidity held by individuals is about 5 times the size of Morocco's privatization program.

c. Deposit Accounts with other Specialized Institutions

Treasury has started offering interest-bearing checking accounts, impinging on the banks' monopoly. Certain specialized financial institutions such as BNDE and CIH, which are privatizable, are trying to develop a depositor base in order to alleviate future financial sourcing without State guarantee. Their deposits were around Dh 5 billion in 1991.

3. Individuals

We have viewed the potential of individuals as a target group in terms of top urban households, the market analysis completed by LMS as well as average individual deposit base. Additional analysis to that below is included in the Annexes to this report

It is important to note that conclusions have been drawn based upon consumption and savings trends and statistics. Yet, there is no certainty that households spending over DH 100,000 in 1991 were left with savings that could be used for investment in shares. **Only the detailed study of actual investors would allow us to improve the comfort level of this cutoff.**

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6 Source: Bank Al Maghrib

In 1991, the typical head of a top urban household was a 46 year-old male who spent Dh 107,500 (Dh 10,000 was not for consumption). In Moroccan terms, the spending of that top urban household translates as 2.8 times the national average and 1.9 times that of its rural counterpart. There were 457,000 such urban households in the country in 1991. Altogether, this 9% of all households did 28% of the nation's spending. These 457,000 urban households are the first recommended target for broadening individual share ownership (see section III.B).

Within the top 457,000 urban households, the top households of the Casablanca-Rabat-Tanger axis (360,000 households) seem to be the category within the Moroccan population that has the most potential for becoming share owners. This 10 to 15% of the total population has a purchasing power that allows for savings. The regional analysis of 2 recent stock issues shows that 67% of all shares requested came from the urban and industrial regions of the Center (Casablanca) and the North West (Rabat-Kenitra-Tanger), the economic backbone of the country.

LMS conducted a study of the CTM advertising campaign and as such, it cannot produce conclusive evidence based on hard data. However, the results of the LMS analysis support the above conclusion. LMS concluded that the top 48% socio-professional urban population (the A/B group) intends to buy shares during the privatization process, a significantly higher proportion than in the other groups. According to LMS, the A/B groups represent some 10% of the individual population. A detailed definition of the A/B group is included in Annex 1.

Taken as a multiple of average bank deposits, savings mobilized by investors in recent public issues were at least twice the size of the average client deposit. It suggests that these investors, some 160,000-400,000 households, controlled the largest deposits.

4. Residents Marocains a l'Etranger (RMEs)

RMEs are Moroccans living abroad. In search of employment, people from eastern and southern Morocco started emigrating to Europe during the 1960s. They found work, created their family there, and started building their business. About 1.7 million Moroccans live abroad, 1.3 million of them in the EC: 40% in France, 11% in Holland, 10% in Belgium and 9% each in Spain and Italy. As their standards of living improved, they saved and remitted these savings back to Morocco.

First generation emigrants look back to the mother country, as there is a family to assist financially, a desire to build a house and the dream to set-up a business.

The currency inflow that RMEs generate has grown larger than exports or tourism, to become the biggest commercial earners of foreign currency. In 1991, they added almost Dh 2.6 billion in domestic bank sight deposits. In 1992, RMEs sent back some Dh 18 billion - an estimated average of Dh 45,000 per household.

RMEs appear to control about 30% of the money deposited in the Moroccan banking system. They maintain some 450,000 bank accounts in Morocco, 80% of which are with BCP, the largest domestic state-owned bank. They hold conservatively Dh 30 billion in various bank deposits in 1992.

Having given early consideration to their personal and economic importance, the State has kept contact with them through a Ministry dedicated to their needs. Morocco is very well-positioned to include the RMEs in its privatization program and to target them as potential share owners. Yet, prompt action is required, for 60% of all RMEs are under 25 years of age. Brought up in foreign countries, they do not have the money-transfer instincts of their fathers.

RMEs' liquidity should be of concern to the banks, particularly BCP, its largest recipient. Transfer of some of that liquidity to the capital markets would inevitably have a boosting effect on their development. A RME reduction in bank deposits of 30% would reduce Treasury's mandatory allocation financing by a third, or Dh 6 billion. Treasury would be left to seek such financing in the financial markets, while banks would have to reduce their corporate lending by some Dh 25 billion, or 40%. Banks would be forced to tap the financial markets to fund their credit portfolio, to cancel many credit lines to decrease their exposure, and to encourage their clients to reduce their use of bank credit by issuing commercial paper. They would drive the large corporations to the capital markets, where their over-leveraged structure would initially require issuance of equity, thereby enhancing the broadening of share ownership.

With their liquidity and propensity to save and transfer these savings in the existing savings mechanisms, RMEs are the second largest target (see recommendation III.B). For example, their investing 30% of their liquidity in privatization would retire 50% of that program. The potential ripple effect of RMEs' transfers from the mechanisms they currently used (i.e. regular savings accounts or bank deposits) to share ownership based mechanisms whether direct ownership or through an OPCVM, has an even greater potential.

5. Institutional Investors

a. Insurance Companies

(1) Overview

The insurance sector consists of 19 commercial and 3 mutual companies. Four of them accounted for 38% of all policies. Automobile premiums represented 38% of total 1990 inflows; life insurance and annuities 19%; work-related policies 12%; and individual accident coverage 11%. Other inflows come from various smaller sources such as marine insurance, airplanes, hail, etc. Direct savings policies (life and annuities) were barely Dh 31 per Moroccan in 1990[7].

Insurance companies, which are regulated by the MOF, are major investors in government securities, and contrary to experience in other markets, very small holders of equities. They place a large portion of their liquid assets in Treasury bonds or bonds guaranteed by the Government, at rates fixed by the MOF. They are attracted by high paying instruments such as the Emprunts Nationaux (EN) that they obtain through the BVC. Their portfolios of corporate shares are small. They are not active traders in the stock market. Kept low by regulation, insurance premiums do not currently cover their payment of damages, which limits their profit re-investment capability.

(2) Portfolio management

In 1990, Dh 6.8 billion of the insurance sector's total portfolio of Dh 13 billion was in securities and Dh 4.5 billion in short term assets. Real estate investment accounted for Dh 1.3 billion and loans for less than Dh 300 million. Government securities were Dh 7 billion (54%), and only Dh 1 billion (8%) was in listed shares - less than real estate. Yet, their stock portfolio represented some 15% of the then current market capitalization on the BVC, making insurance companies a major stock holder.

Reserves for damages accounted for Dh 10 billion, the majority (63%) of their technical reserves of Dh 16 billion. Mathematical reserves were Dh 5 billion, 86% of which were for life and annuities; and 95% of those corresponded to corporate pension plans. As mentioned above, because premiums are State-controlled, the insurance sector has experienced over the last few years a deficit of premiums over damages. This deficit absorbs the profit on premiums and their portfolio income. A premium adjustment would open up insurance profits for re-investment.

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7 Source: MOF

Private insurance companies manage a large portion of the portfolios of state-owned entities. Their interest to create OPCVMs to compete for savings makes sense if such investment vehicles are not treated as insurance companies themselves. Should MOF limit their role to the prudent management of forced savings, the best companies will grow by designing innovative products for the corporate sector.

Al Amane is a company vying for first place in the sector, with Dh 620 million worth of premiums collected in 1992 and technical reserves in excess of Dh 2.7 billion. French giant UAP retains a majority in the company. Al Amane absorbed another large company (L'Entente) in 1986, in what is a sign of times to come in this industry: concentration. Its portfolio is split among government bonds (50%), shares (30%) and real estate (12%); balance is cash, other short term deposits and guarantees (8%).

(3) Distribution

The most dynamic insurance companies have been diversifying the distribution of their products through the banking network, which provides better coverage than the usual insurance agents and brokers who are concentrated in Casablanca. In addition to distribution, economics drive the insurance companies towards the banks: since most damage policies (including car, air, maritime and work-related accidents) show a deficit, banks' lower distribution costs are attractive.

(4) Impact on Share Ownership

Like other investment intermediaries, insurance companies contribute indirectly to the broadening of share ownership. Although the size of their portfolio is large, only Dh 5 billion represented annuities in 1990. Regarding life and retirement insurance (the annuities), insurance companies have so far performed better in the corporate market than in the individual market. As more companies offer their employees retirement plans and more security, they create pools of employee-employer savings that must be invested in assets which yield a sufficient return to fund the defined retirement benefit.

b. Commercial Banks

(1) Overview

The Moroccan banking system of 14 commercial banks had deposits of Dh 106 billion in 1992; it extended Dh 62 billion in private credits and some Dh 40 billion to finance the Treasury. With over 1,000 branches, the banking network correlates well with the urban population, but is not as dense as the Tunisian one. Deposits grew by 31% over the 1990-

1992 period as a result of competition spurred by deregulation[8].

Banks are currently the backbone of the financial and capital markets. Besides their usual deposit-taking and lending activities, they are active in stock brokerage, industrial participations, insurance distribution, and are the major channel for RMEs' remittances. Current account convertibility and international borrowing have been introduced in 1993 and 4 of the 5 state-owned banks are slated for privatization as early as 1994.

A new banking law was passed in December 1992. It adds much precision to the activities and obligations of banks and other credit institutions, to their controls by the authorities, to the protection of deposits, depositors and clients, and the public transparency (independent audits). The new law has also introduced prudential measures such as the Cooke ratio, client risk ratio (7% of capital + reserves) and strict directives for loss provisions. Banks will have to comply with these new requirements by the end of 1995. Some banks have already increased their capital through the markets (WAFABANK, BCM) while others are in the process (CDM, BMCI).

Annexes 4 and 7 provide graphics and tables which support the analysis below.

(2) Deposits

About 80% of all banking deposits are held by individuals in checking accounts (liquidity), passbook savings (semi-liquidity) and term deposits (savings). About 80% of the cash mobilized for investment in recent public issues was derived from bank deposits, either used directly or as collateral to borrow. Deposits are the first source of liquidity for new investments.

Mutual funds, which have a built-in liquidity features, may prove more attractive than bank deposits for individuals to hold short term liquidity, unless bank deposit rates are so high as to prevent the transfer to mutual funds. Under present conditions, the main lever to lowering interest rates is to lower the legal ceiling rate on passbook accounts to one marginally higher than current inflation (about 5%). Removing the ceiling would open competition for money in the whole system and would provide an expanded lending rate range.

Source: Direction de la Statistique; La Vie Economique

(3) Credits

Banks extend short term loans with stringent collateral requirements, mostly to the best and largest companies. The lack of a real interbank market limits bank access to liquidity and encourages them to keep short-term assets available. Accounting/reporting weaknesses and delays, and uncertainties in the bankruptcy proceedings, increase the risk of corporate lending, which short-term loans minimize.

Although MOF has allowed banks to lend longer to corporations as a quid pro quo to letting state-owned entities penetrate the deposit market, banks have remained cautious: lack of corporate transparency and a narrow range of interest rates do not allow proper risk assessment and loan pricing. Consequently, most lending is based on status (family name) lending and banks have not developed much expertise in credit analysis or corporate research. These tools will be necessary in the more vigorous capital markets lying ahead.

So far, banks have not been aggressive in developing knowledge of client base that would facilitate (a) marketing products, including the placement of shares from privatization, and (b) restructuring around services, which is needed to face the new capital markets.

Financing privatization may be done through the financial markets (OPCVMs) instead of the banks. Financing individual investors is a credit decision on the client and the collateral. Such credit is short term for small holders who are after a quick capital gain. Banks may wish to develop securities lending as a new activity.

(4) Bank Classification[9]

BCP, BMCE and BCM form the first bank cluster (Group 1). They collect 64% of all bank deposits, extend 53% of bank credits and account for about 50% of the entire bank branch network. They are growing faster than the other groups and have gained market share in terms of both deposits and credits from the third, smallest bank group.

Group 2 (WAFABANK, BMCI, CDM, SGMB) is about half the size of Group 1. Collectively, these banks accounted for 31% of the branches, 27% of deposits and 36% of credits in 1992. Their growth is by and large comparable to Group 1, particularly in the cases of WAFABANK and SGMB.

Group 1 and 2 are most likely to be instrumental in the public placement of public offerings under the privatization program. They also are the most likely to lose deposits because of share purchasing.

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9 Source: Direction de la Statistique

Group 3 is composed of 7 banks, 4 of them foreign-owned. Their share of branches (22%) is disproportionate to their deposits (9%) or lending (11%), suggesting that they operate under the critical mass. They may aspire to niches such as foreign loans (like Citibank's for ONA), foreign exchange, exports, bilateral business, but will most probably not grow to any national position. Their possible participation in the privatization effort has little potential to broaden share ownership.

(5) Impact on share ownership

Commercial banks, as the major player in the current financial markets can affect both the supply and the demand side of broadening share ownership. On the supply side, the example of WAFABANK can and will be followed by other private banks. The privatization of the state owned banks through public offering will also increase share ownership as banks are well known and for the most part financially stable.

On the demand side, the aggregate placing power of banks through their domestic and overseas networks have a unique resource to promote the broadening of share ownership in Morocco. Commercial banks could help individuals purchase shares by creating new activities such as securities lending as well as provide investors with bridge investments to allow investors to maintain returns on their capital in between investments. They can also use their network in the promotion of OPCVMs and to market the shares of new issues widely throughout the country.

c. Specialized Financial Institutions

There are five specialized financial institutions, all State owned: Caisse de Depot et de Gestion (CDG, a fiduciary portfolio management), Banque Nationale de Developpement Economique (BNDE, industrial development), Credit Immobilier et Hotelier (CIH, real estate), Caisse Nationale de Credit Agricole (CNCA, agriculture) and Caisse Centrale de Garanties (CCG, guarantees). BNDE and CIH are privatizable. By 1991, these five institutions provided some Dh 31 billion to the economy, 80% in the form of medium and long term loans for housing, corporate development and agriculture.

As a direct lender to Treasury, this group (Dh 6.6 billion) was, size-wise, similar to insurance companies. Most lending to Treasury originated from CDG (Dh 5 billion) and from CNCA (Dh 1.4 billion). With direct lending to the State of Dh 5 billion, CDG may well be its largest single lender.

SNI and ODI are two other noteworthy SOE holding companies and CEN is the national savings bank tied to the post office system.

(1) CDG

CDG's own securities portfolio of Dh 3 billion (1992) exceeded that of the largest insurance company, making this non-privatizable a force in the financial implementation of various government projects in the private sector. CDG has a large portfolio of hotels and golf courses across Morocco.

As fiduciary, CDG managed various funds worth Dh 18 billion in 1992. The Social Security (CNSS) and National Pension fund was the largest (Dh 13 billion) and entirely invested in State bonds and State guaranteed securities. The management agreement between the CDG and the CNSS is incongruous and not competitive. Each year, the CNSS earns on its incremental portfolio a rate negotiated on the basis of current Treasury rates. Effectively, the forced savings annuity of the CNSS subscribers subsidizes government borrowing at rates under current market conditions. CNSS's blended annuity rate was less than 9%, while the market rate was 11-12.5% as of the end of 1993 [10]. Given Morocco's explosive demographic growth, the CNSS might not be able to accumulate reserves large enough to face its future obligations on such an annuity. Under a competitive system of financial management, the CNSS might be able to earn market rates on its portfolio, serve its subscribers better and contribute to the broadening of share ownership by adding liquidity to the markets.

(2) BNDE, CIH, CNCA

BNDE, CIH and CNCA have been successful in obtaining large amounts of aid-related foreign financing (Dh 13 billion - 1991). The upcoming privatization of the first two will not automatically mean a curtailment of their foreign resources (altogether Dh 4 billion), since they might well pursue privately the same policies that led to receiving this financing in the first place.

CIH and CNCA are expanding their independence from State guaranteed financing by developing a deposit base that reached almost Dh 5 billion at the end of 1991. This amount is equal to 50% of the deposits accumulated by Bank Group 3, an amalgam of the smallest commercial banks.

CNCA's lion share of these deposits (Dh 2.8 billion) and their fast growth (20% in 1991) indicate that there is increasing liquidity coming from the agricultural population, which probably remains liquid because its needs are more immediate. Some portion might be placed in an agricultural investment fund.

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10 Source: CDG

CIH also demonstrates its proximity to a large population of homeowners, with deposits of some Dh 1.6 billion that are growing rapidly (49% in 1991). CIH is a good candidate to develop a real estate investment fund with potential for broadening share ownership and may be the natural issuer of mortgage-backed securities in the future.

BNDE has lost deposits which may account for its attempt to acquire BMAO (a small bank) and for its orientation as a merchant bank (financial advisors for the CIOR privatization). Depending upon its performance in the CIOR transaction, BNDE might be a useful resource to the Ministry of Privatization for future offerings.

BNDE's large industrial portfolio is managed as a financial holding, the revenues of which are essentially re-invested in its operating companies.

(3) The National Savings Bank (CEN)

CEN counted some 620,000 subscribers to its passbook deposits earning 9% tax-free as of the end of 1992. Despite a rate more favorable than banks (8.5%, taxed), CEN's deposit base was only Dh 2 billion at the end of 1992. CEN caters to a population of lower means: its average deposit was a mere Dh 3,400, compared to Dh 21,000 at the banks. CEN has no immediate potential as a mechanism for broadening share ownership, but could become a money market fund manager in the new financial markets.

(4) SNI and ODI

Over time, SNI has essentially become a holding company. SNI's statutes and special legal standing limit its being an active market-maker as it cannot resell its participations without paying taxes on its capital gains. Consequently, SNI's strategy has been to re-invest its portfolio revenues in new and increased participations. SNI has developed a stock brokerage activity (SOMACOVAM) that caters to about 500 clients; their average portfolio is Dh 250,000. SNI is privatizable.

ODI was created as a sort of venture capital fund. ODI has a portfolio of generally smaller companies, many in need of restructuring.

6. Employees and Special Interest Groups

One of the objectives of the Moroccan privatization program is to broaden share ownership to specific target groups including employees and investors outside the normal sphere of share ownership who have a stake in the enterprise, such as investors within a privatizable's region or to farmers who supply the inputs to the agro-industries.

Below we discuss the general concepts of employee stock ownership plans and present the activities the Ministry has or is planning to undertake with respect to special target groups.

a. ESOPs

(1) Concept

Employee stock ownership plans (ESOPs) essentially rely on the decision by the employees of a company to dedicate some share of their disposable income, plus a stream of future disposable income, to purchase a part or the whole of their company. The decision to forego the certainty of income is in exchange for the expectation of a long-term appreciation of the value of their corporate stock.

ESOPs suppose that employees have:

- some savings and a current disposable income
- the professional training necessary to contribute positively to, and to supervise, their company's success
- the economic understanding necessary to trade off a tangible current revenue against a hypothetical future capital gain
- understanding of and access to a stock market that is liquid and capable of proper corporate valuations
- access to cash flow based financing to complement their initial investment.

(2) Moroccan Framework

It would be naive to conclude that state-owned enterprise employees meet all of the above requirements. However, implementation of ESOPs in the Moroccan context is feasible if certain conditions are met.

The Moroccan Government has demonstrated its commitment to allocate a portion of privatizables' shares to employees by providing in law a 15% discount on the share price for employee purchases. The principal constraints to employee participation concern the transfer structure, the availability of financing and limitation on share resale in order to qualify for the 15% discount.

Under current law, the purchase of privatizable shares must be paid for in cash up front. Deferred payment is not allowed under Moroccan law for the transfer of privatizables' shares. Secondly, in order for the 15% discount to apply, the employees must purchase the shares themselves or through an employee owned fund. The concept of a financial intermediary which can purchase the shares at a 15% discount on behalf of the employees is not recognized in the law. Given the financial resources of many SOE employees and their inability to secure loans from the banking sector, this inevitably excludes them from share ownership. Finally, the shares do not offer immediate liquidity in the event that the employee wishes to sell them. Shares bought at a 15% discount must be retained for three years. The justification for this latter issue is that employee purchases may result in speculation as was the case in the WAFABANK issue. (see Section II.E)

In Section III.B.3 we provide a detailed recommendation which appears to be within the legal framework, although the M.P. 's legal advisors would have to confirm this.

This recommendation for an Employee Stock Fund would be applicable to other special target groups as well. Essentially, the recommendation suggests that employee shares be retained and managed by an employee owned fund which might be in the form of a cooperative or OPCVM (FCP). Financing would come from Treasury at its three year lending rate and perhaps from donors in the form of a revolving loan.

b. M.P. Current and Planned Activities

The M.P. intends to include employee and special group participations in current and upcoming share offerings but has met with limited success to date.

It is hoped that an ESOP component of the CTM-LN transaction will be finalized. The major obstacle encountered to date has been the lack of financing. Discussions with a commercial bank to obtain a loan at preferential rates were not fruitful. (The Ministry has also approached USAID to request financing assistance.). Other employee participations envisioned by the M.P. include CIOR and SNEP although none have materialized to date.

With respect to targeting special interest groups, the CIOR transaction structure initially included 10% of the shares reserved specifically for investors in the Fez/Oujda region where CIOR is located. However, due to the tremendous over-subscription of the initial public offering, the portion allocated to regional investors was sold to the general public. Given the high demand which has been demonstrated in each of the recent offerings, transactions with respect to regional share ownership should probably be concluded prior to offerings to the general public.

D. TAX ISSUES RELATED TO BROADENING SHARE OWNERSHIP

It was beyond the scope of this engagement to perform a thorough study of the tax system and policies driving it. We offer here only few observations concerning several obvious anomalies which tend to distort incentives for investors.

1. Tax Policy Distorts Patterns of Investment, and Bears Unevenly on Different Financial Instruments.

Reform of the fiscal system since the mid-1980s has not focused yet on the uneven incidence of taxation on varying types of investment vehicle. The income tax system taxes interest income; it uses four different rate mechanisms and applies different rules for individuals and corporations. A flat 15% tax on cash dividends paid to individuals is withheld at the source, while corporations must declare dividends earned, which are taxed at an effective tax rate of 5.7 percent. Moreover, the new capital markets legislation introduces certain special tax treatments for dividends paid on long-held shares, for those paid by the new investment vehicles and for those re-invested in shares traded on the BVC. They are particularly beneficial to small stockholders. Finally, the capital gains tax on real estate, effectively less than 15%, remains a more favorable treatment than that accorded to any financial savings or corporate investment.

The most significant distortion contained in current tax policy is the exemption from taxes of earnings on government bonds. These exemptions are being phased out with an initial tax rate of 10% on selected instruments, possibly increasing over the medium term to 30%

2. Dividends are Subject to Double Taxation

In the absence of a tax credit or a deduction as tax expense, neither corporations nor recipients are allowed any deduction (or credit) for taxes paid on corporate income distributed as dividends. Thus, while dividend taxation appears more favorable than the taxation on interest income, it is actually less favorable when taking into account the high corporate tax (38%) paid on profits before distribution. New special incentives for reinvestment in listed Stock Exchange companies only confuse the issue. In fact, it is difficult to say that this measure would of itself repress the growth of the capital markets, since double taxation of dividends in a feature of many active markets.

3. Capital Gains as well as the Issuance of Rights and Stock Dividends Remain Un-taxed

There is no explicit tax obligation on earnings distributed in the form of stock dividends (i.e. free shares), even upon their eventual sale. Between 54% and 72% of all dividends have been distributed in this form over the last four years. The firms listed on the BVC distributed Dh 715 million in cash dividends and Dh 1,587 million in stock dividends in 1991. Such a tax-oriented distribution has concentrated share ownership among original shareholders to the extent these holders will tolerate the lack of cash dividends. On the other hand, the exemption of taxation of capital gains is a very positive incentive for the broadening of share ownership.

4. Hybrid Financial Instruments Result in Complex Tax Treatment

Hybrid instruments such as convertible bonds, investment certificates, preferred shares and warrants could be defined as fixed income, dividend rights or free shares. As such, they could be simultaneously subject to widely different tax regimes. This would not be the case in a streamlined system, which is preferable for the growth of the capital markets.

E. RECENT EXPERIENCE IN IPOs

We have compared the CTM-LN offering to WAFABANK, two recent public issues on the BVC. WAFABANK preceded CTM-LN and was its structural inspiration. Whereas the WAFABANK issue is not a component of the privatization program, a summary is included herein due to its relevance to IPOs. In Annexes 1, 2 and 7 we provide graphs and tables on these two transactions. This analysis and comments are based upon the end date of our field work and report drafting. (August - September, 1993)

We have not done a full analysis or comparison of the CIOR public offering as it occurred three months after the end of our fieldwork. A brief summary of the CIOR issue is presented in item 5 of this section.

The newly appointed Minister of Privatization has indicated that each privatization transaction will be considered for public offering. This might be taken a step futher by having the Ministry undertake to structure requests for bids so as to allow for public offerings, even where the Ministry thinks such a response unlikely, and to educate potential offerors that underwriting and public offerings will be acceptable. Such a move would require flexibility on the part of the Transfer Commission and Valuation Authority with respect to transaction structure and selling price.

1. Comparison of WAFABANK and CTM-LN Offerings

Both issues set a share offering range that limited the concentration of shares. It was for the benefit of smaller, individual investors.

The two issues have been oversubscribed more than 3 times. 99% of the investors were individuals who requested 90% of the shares, demonstrating the attractiveness of corporate shares as a savings allocation.

The issues required prior cash payment by the investor. This did not hinder the bidding since in each case the average amount of cash mobilized by investors was at least twice the amount of the average client deposit. This cash surplus indicates that investors have larger than average bank accounts.

The issues have created over 10,000 new local individual investors and generated participation by over 4,000 Moroccans living abroad (RMEs). Since secondary trading has been limited to date, an investor base has been established.

Some 40% of demand was for the minimum amount of shares offered, in both cases worth Dh 5,000. If logistically feasible, a lower minimum investment amount might attract a larger participation of smaller investors.

The par value of both shares was set at Dh 100, the BVC convention and higher than the legal minimum of Dh 50. Basing the share issuance value on the minimum nominal value may enhance the broadening of share ownership.

Altogether, both issues have mobilized an investment potential in excess of Dh 1 billion in cash, which suggests that the unallocated balance of Dh 700 million might be available for CIOR and other forthcoming issues.

Both lead managers were banks, placing the vast majority of shares (80%+) through their own network. Banks acting as lead manager will tend to place shares within their own client base, which may not be favorable to the broadening of the individual investor base and may mitigate against letting network banks manage issues.

Both placement syndicates were identical. With the exception of the managers, the same members (BCM, SGMB, BMCE) placed the most shares.

Banks are well-positioned to place share issues thanks to their good branch coverage of the urban population. For the important CTM-LN public offering test, the Ministry was justified in forming a banking syndicate.

BCP's placement of CTM-LN was more evenly distributed across the country than WAFABANK's, but both issues confirm that share ownership is particularly attractive to people with the higher economic exposure found in the Casablanca to Tangier regions.

Foreign institutional participation was almost non-existent, more because of the share limitation rule than by lack of interest.

BCP and WAFABANK established new internal operational procedures, including computerized statistical gathering and control processes, for their placements. As a result, they have collected substantial data on the investors.

Secondary activity on the official market was initially and temporarily generated by small holders (including WAFABANK's employees). It indicates that they unloaded their position for a profit within the first three weeks of trading. Employees and other small holders may be tempted by speculation, but have a preference for liquidity or other saving priorities.

2. WAFABANK Issue

WAFABANK is a private bank, 82 percent owned by private Moroccan interest and 18 percent by the French Suez group. As part of its development program, WAFABANK undertook a significant capital increase program involving three issues. One was an initial public offering for 999,875 shares worth altogether Dh 200 M. In a unique move, the existing shareholders voluntarily renounced part of their preferential subscription rights to enable the bank to open its capital to its clientele and to the general public. WAFABANK is the first Moroccan bank to have opened its capital to the general public.

The publicly announced strategy for the capital increase was to open the bank's capital to a precisely defined group of investors. An overall placement budget was developed whereby all shares were allocated according to three criteria: a) number of clients, b) volume of deposits and c) number of employees among the WAFABANK's network. Consequently, WAFABANK placed most shares in the Casablanca-Tanger regions.

The bank undertook an information campaign via different media, including press announcements in daily publications, information brochures placed on the bank's counters, multi-language posters, etc., to explain the institutional nature of WAFABANK, the importance of the capital increase operation to the bank's development plan, and the importance of having investors who understand the institution.

To encourage share ownership, subscribers were guaranteed a minimum of 25 shares. A second tranche was allotted for demands between 25 shares and 10,000 shares, in relationship to the total number of shares offered, after serving the minimum demand. Demand over 10,000 was met on a pro rata basis, subject to availability.

A ten-day subscription period was established from 7-17 December 1992, with payment required upon subscription. Institutional investors tended to subscribe on the last day of the subscription period because of the requirement to pay upon subscription. The issue was 300% oversubscribed. The oversubscription resulted in a second capital increase in April 1993 to meet the unsatisfied demand of the subscribers in the first capital increase issue.

The WAFABANK shares were offered publicly at a price of Dh 200 per share, or Dh 5,000 per minimum order. The par value of the shares was set at Dh 100, which represents the conventional par value for shares quoted on the Bourse.

The syndicate was composed of fifteen local financial institutions, including thirteen banks, the Public Treasury, and one portfolio management company. WAFABANK placed 89% of the shares, followed by Banque Commerciale du Maroc (3.7%) and Societe Generale Marocaine de Banques (2.3%). The WAFABANK issue, like the CTM-LN issue, highlights the important placing power of banking networks in broad share distribution as well as the lead manager's capability to place shares among its clientele.

Over 96 percent of the issue was placed domestically. Demand exceeded budgeted allocations in all units of the bank's network. The breakdown of shareholders by socio-economic strata indicates that the major purchasers were professionals and shopkeepers, enterprise managers and junior executives. The average age of purchasers was between 35-45. The domestic distribution indicated a particular concentration in the most economically advanced area of Casablanca. The distribution of shares to RMEs was concentrated in Belgium and Holland.

From the bank's point of view, the issue had significant positive implications: the issue was placed mostly with the existing clientele which WAFABANK knows well. It showed that people have disposable funds for good business opportunities. Forms of payment for shares purchased included transfers from bank accounts (transformation of deposits into equity), external free funds, sales of Treasury bonds, and collateralized loans obtained from WAFABANK by its clients to purchase shares.

Specific implications may be difficult to extrapolate to the national level, except in terms of an enormous underground potential. The creation of new products and expanded financial instruments may be able to draw this potential out.

Two categories of people returned shares immediately following the public issue: 50 to a 100 small savers and WAFABANK employees who chose to realize their special issue discount of Dh 60 per share. Unlike CTM-LN's, the WAFABANK issue carried no limitation on share resale by employees. The fact that employees sold shares immediately raises the question of whether employees in privatizables can be a viable target without conditions imposed with respect to the resale of shares.

The WAFABANK stock has not gained much value after its introduction. Secondary trading was mildly active during the first 15 market sessions following the IPO. When market activity abated, a few larger off-market transactions took place. Trading in the stock has now fallen to BVC's current, somewhat inactive pattern.

3. CTM-LN

CTM-LN is an inter-urban bus company that is a household name in Morocco; following its restructuring a few years ago, it has become profitable. Its strong management has developed a business plan for the company's future growth. It was an ideal test case for privatization through a public offering.

The strategy for privatizing CTM-LN involved an initial private placement of shares to a reference group of local financial institutions. It was followed by a public issue on BVC, and will be finalized by an allocation of shares to employees. The original private shareholders and the State retained minority shareholdings. This first privatization by Initial Public Offering was listed on 3 June 1993. It was also the first BVC initial public offering aimed at the general public since 1985.

a. Private Placement

The privatization of CTM-LN first involved a private placement on a restricted tender basis of 35% of CTM-LN stock at a price of Dh 338 per share to a consortium of Moroccan financial institutions which assumed responsibility for ensuring financial and management continuity during a five-year period. The group was selected from a field of three syndicates.

b. Initial Public Offering

For the second phase of the privatization strategy, 40% of total shares (377,244 bearer common shares) were sold through an IPO. With a nominal value of Dh 100, the shares were sold at Dh 250 per share. The minimum allotment was for 20 shares, understandable from a logistical viewpoint. The minimum investment was Dh 5,000, a significant amount given that it represents 13% of average urban household consumption in 1991.

The placement syndicate was under BCP leadership and included the Central Bank, 11 commercial banks and three brokerage houses. The CTM-LN issue was not underwritten, thereby reducing the incentive to most syndicate members to wörk hard at broad distribution. Analysis of the syndicate's performance indicates that BCP placed 75% of the shares, followed by SGMB (6%) and BCM (4%). BCP was most successful in placing shares with domestic individuals, both in terms of original demand and number of shares sold per person. Due to the short time frame given to organize the placement, BCP was somewhat less successful in reaching the RMEs, 65% of BCP's deposit base in 1992.

The CTM-LN issue was successful in achieving the M.P.'s publicly stated objectives to foster the emergence of popular shareholding, to assure regional distribution in all economic zones, to reach out to RMEs, and to favor the participation of individuals.

The M.P. launched over several weeks a substantial Dh 5 million multi-media communication campaign on the privatization program. The overall campaign was supplemented by a campaign focused specifically on the CTM-LN issue (See Section E.6 below for a summary of the PR campaign). As syndicate leader, BCP organized a marketing effort targeted at its largest clients, sent letters to more than 500,000 local and RME clients, and held information meetings with clients in Morocco and abroad.

The placement involved a single transaction fee of 0.7% to BCP and the syndicate members. The 0.7% fee is low by normal standards, particularly in emerging markets where fees typically range from 1.5% to 3%. The syndicate leader performed a public service for the government. BCP's acceptance of a non-market fee structure set a precedent for future issues that may be detrimental to their placements.

The price of the publicly offered shares was fixed by the Valuation Authority. This pricing procedure is not flexible. Consideration should be given to introducing "circling", the usual mechanism whereby interested investors indicate the price at which they would purchase certain volumes.

Another pricing factor concerns the establishment of the nominal value of shares. Had the nominal value of CTM-LN's shares been set at DH 50, the shares would have been priced at DH 125, possibly resulting in even broader share distribution among individuals. In Section III.A.2. we address these issues and provide recommendations to the M.P. in this regard for future offerings.

In a manner similar to WAFABANK and in order to broaden the ownership of their stock, all applicants were guaranteed a minimum of 20 shares, and were limited to a maximum of 3,000 shares. Demand above the minimum amount was met on a pro rata basis. On average, the size of the purchase was 35 shares for domestic individuals and 27 shares for RMEs, much less than their requests of 150 and 80 shares respectively.

A seventeen-day subscription period was established from 12-28 May 1993. Payment was required upon subscription. The long subscription period combined with minimum/maximum limitations on the amount of shares purchased and the requirement that payment be made upon subscription raises several important issues. Overall, the CTM-LN issue was 300 percent oversubscribed. Demand reached 99.5% of the total issue after ten days, one week before the closure of the subscription period. The last two days of the subscription period witnessed a doubling in subscriptions. Demand totalled 1,540,447 shares. 224,760 shares were allocated according to the minimum and 152,643 shares were allocated pro rata (11.59%) to demand in excess of the minimum.

Because of its rules on oversubscription, the CTM-LN issue has frustrated those who paid cash early to purchase a desired amount of shares. Allotment flattened out actual demand because excess interest developed during the last week of subscription.

Individual (domestic and RME) subscribers represented 98.7% of total subscribers. Placement was much more representative of the regional population distribution than in the WAFABANK issue. BCP's placing power as syndicate leader was evidenced by the fact that it placed 75% of total shares.

Individuals purchased 90% of the publicly offered shares. A significant proportion of investors were BCP clients and RMEs. Only slightly more than two out of five investors bought more than the minimum of 20 shares (Dh 5,000). This may argue for a lower share issue price.

The 11,000 investors in the CTM-LN issue represented 5.5 times the pre-issue estimation of 2,000 investors, based on the Wafabank results. Some investors seemed to come from outside the banking system. Detailed analysis is needed to quantify this and other savings patterns. Some suggested that CTM-LN investors were oriented to speculation and that shifting savings away from deposits, real estate, jewelry, and hoarding is unlikely on a permanent basis. Such comment are pure speculation and cannot be verified.

The CTM-LN issue also highlights the broad placing power of banking networks. Nonetheless, non-banking financial intermediaries may contribute through other channels, for example in attracting foreign institutional investors.

M.P.'s cautious approach to the CTM-LN public offering and the issue's success would facilitate the safe inclusion of the suggestions herein in the structuring of subsequent public offerings in such a manner as to encourage the widest distribution of shares possible. Such techniques are used in other successful markets and would make sense in the Moroccan market if only to engage the interests of the widest possible portion of the citizens of Morocco in the privatization program.

c. Allocations to Employees

The third phase of the CTM-LN transaction was intended to be the allocation of shares to employees. The formation of some form of non-profit entity of the employees is under consideration.

4. Post-issue Trading

Following the WAFABANK IPO, secondary trading has been 1.4% of the float, 43% of it at the official market (the floor). Floor trading averaged 647 shares per session over the first 87 sessions and was more active during the first 15 sessions. When floor activity abated, 10 larger off-market transactions took place, an average of 7,928 shares. Hovering around Dh 213-218, WAFABANK share price has not moved much from its initial offering at Dh 200[11].

WAFABANK undertook a valuation study of five major quoted and unquoted local banks and concluded that its stock is undervalued and suffers from a lack of trading activity. WAFABANK does not actively manage the value of its shares or make a market in its stock.

For CTM-LN's first 23 sessions since the offering, average floor trading was 1,550 shares, while off-floor average was 2,181 shares and occurred during 21 sessions. The price of CTM-LN shares rose steadily following the issue, from Dh 250 to just under the Dh 338 price paid by the reference group. The price was Dh 310 in early October 1993.

WAFABANK's off-floor trading has been much less frequent (10% of total sessions) but for much larger volumes (12.5 times the shares) than CTM-LN's, for which off-floor occurred during 48% of the sessions and for 1.4 times the average shares traded on the floor.

Since their respective offerings, 1.4% and 4.9% respectively of WAFABANK's and CTM-LN's floats have traded, indicating a larger activity by CTM-LN's small shareholders. These findings support the impression that many small CTM-LN buyers were oriented towards speculation and cashed out as the share price climbed.

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11 Source: BVC

While many small CTM-LN buyers have made money on their speculation, they also left the market. Effectively, they sold their shares to institutional investors. Their motives may have been a quick return, or they may have feared the loss of the gain they had already made. This behavior is quite common in many markets. While the early sale of their shares contributes somewhat to the reconcentration of shares through the secondary market, this effect may be temporary. It is difficult to draw a conclusion as long as there is such a small quantity of shares on the market for trading.

Equally important are issues pertaining to disclosure and to the role of the reference shareholders. There has been no public mention that the CTM-LN stock was being managed by its institutional investors. And their strategy has not been different with CTM-LN than it has been in the past with their other stockholdings.

5. CIOR

The CIOR IPO has confirmed the findings and conclusions drawn from the WAFABANK and CTM-LN offerings. Valued at Dh 1.2 MM, CIOR is four times the size of CTM-LN. The privatization is attractive because its size allows the combination of all privatization objectives:

- the Swiss company Holderbank, a world force in cement, will hold 51% of the capital and provide technical know how;
- 24% of the capital will be floated on the Stock Exchange;
- regional interests will have access to 10% of the capital;
- employees will obtain a share up to 10%.
- the choice of Holderbank creates additional competition in the local cement market, where Lafarge and Ciments Français are present through minority participations in other cement companies.

BNDE, itself a privatizable, advised the ministry and lead the placement. BNDE does not have the placement power of commercial banks; hence, this IPO proved that the separation of the management and the placement of an issue is possible. BNDE had a reasonable period to organize the placement syndicate unlike BCP. Confirming prior performance, BCP, BCM and SGMB placed 90% of the shares. The remaining members of the placement syndicate placed the balance.

The CIOR IPO took place in December 1993 after the preparation of the draft of this report. Some brief comments on this transaction have been included in this final report based upon information provided by the BVC.

CIOR's privatization has confirmed the existence of an overall demand for shares: the issue was more than 6 times oversubscribed, for a total amount exceeding DH 1.4 billion.

More than 16,000 individuals represented over 82% of the total subscription, which diffused through all regions. As expected, geographic concentration was evident in the richer and more urban regions of Casablanca (80%), Rabat (8%), Fes (6%) and Oujda (2.6%).

RMEs were fewer to participate (3,271) than in CTM-LN; nonetheless, average demand (98.5 shares) exceeded that for RMEs in the CTM offering (80 shares). Most noticeable was the increased participation of both local and foreign institutional investors (U.S. and U.K. in particular.)

Our preliminary conclusions are summarized here:

(1) Improvements in the offering memorandum would lead to more transparency and financial accuracy. While these improvements would be a welcome addition for local investors, they are a necessity for the foreign investors.

(2) Contrary to local perception, CIOR's IPO was not an underwriting transaction. The pricing was fixed by the Valuation Authority without regard for market demand and the syndicate had the further obligation to support price for a period of 6 months.

(3) Supporting the issue price would be an illegal procedure in the U.S. and U.K. Its purpose here is to provide share price protection to the local investor during an initial trading period. We believe that this support is not necessary given the local pent-up demand for investments; it also in essence postpones real trading by 6 months. In addition, this procedure bears a high share price risk for or cash commitment by the placement manager, which is not warranted when placement fees are minimal.

(4) If commissions, already low, remain unpaid, the Ministry may have difficultly finding placement agents thus jeopardizing the privatization program.

(5) A clause of the placement contract covered the Manager's obligation to provide detailed information on the investors in order to establish an investor profile and index. BNDE has yet to fulfill this obligation and BCP is waiting for guidance from the M.P. to format and analyze the data which had been collected by them. It is important that the M.P. enforce the production of such investor reports by the syndicate managers and be given authority to impose appropriate sanctions in the event of non-compliance. Since no customer profile or index has been developed so far, it is not possible to determine investor characteristics. Specifically, it is not known if the CIOR investor population is made of repeat investors or is an expansion of the previously existing investor base.

Detailed analyses of the WAFABANK, CTM-LN and CIOR offerings will enable the Ministry to refine its "investor profile" as well as have a clearer picture of the financial resources which may be tapped. Results from the placement leaders will enable the Ministry to revise public offering strategies as necessary to ensure continued broad-based participation. Secondary trading will validate the conclusions.

6. Advertising, Public Relations, and Education Campaigns to Support Privatization

In April 1993, the M.P. launched, over a period of several weeks, a substantial Dh 5 million multi-media communication campaign to explain the privatization program to the general public. The campaign was carried both in French and in Arabic. It included TV, radio, press, posters, and brochures made available at banks, post offices, the Treasury, and the Bourse (BVC). The original batch of brochures has been exhausted and 40,000 copies have been reprinted.

The results of the generic campaign on the urban population have been analyzed by LMS, a marketing research company (See Section II.C.3 for conclusions reached by LMS). Overall, the campaign was well-spread and well-received; TV had the highest penetration, followed by the press and the radio. The campaign created motivation (85%) and carried a sense of opportunity (83%), its posters had impact (73%) and its general message was received and understood by 62% of the urban people surveyed.

As to the other side of the campaign, 70% did not understand the positive impact of privatization on the economy, 66% did not receive enough information on the privatization process and 65% felt that the goals of privatization were not explained well enough. Too many did not know where to buy shares (80%) or how to participate in the privatization program (54%). Of those surveyed, 3.3% intended to buy shares.

The generic campaign was supplemented by a campaign focusing specifically on the CTM-LN issue. The M.P. produced an information memorandum on CTM-LN, available to interested parties through the banking network. Availability was somewhat uneven. The CTM-LN campaign was undertaken by the CHEMS Advertising Firm. It included press releases, posters, and media spots on TV. The good quality of the campaign is demonstrated by the fact that CHEMS won a number of awards at a recent Geneva based, francophile media symposium for its CTM-LN campaign.

The M.P. deserves public recognition for its accomplishments and its dedication to privatization. The M.P. has taken the importance of adequate public relations seriously. The Transfer Commission has met with a number of advertising firms who have presented strategies for various PR campaigns.

Additional organized communications would create more visibility for privatization, convey its purpose more frequently, explain its process repetitively, advertise its future operations and nurture public confidence through the transparent disclosure of its activities. The whole staff of the Privatization group could come into the limelight on a regular basis to maintain visibility, to develop a sense of identity and to humanize privatization in the eye of the public.

Experience so far indicates that a substantial investment potential exists. Communicating facts is the practical means to convert this investment potential into reality and to convey an example of disclosure and transparency .

In Section III.C. below, recommendations to enhance communications and public relations are provided.

III. RECOMMENDATIONS

A. RECOMMENDATIONS TO INCREASE SUPPLY

Recommendations 1 and 2 are directly addressed to the Ministry of Privatization. These are recommendations the M.P. can undertake as they are under its scope. Recommendations 3 to 10 could be sponsored by the M.P. The impact, effect or attributes of these last recommendations are not under the scope of the M.P., but would achieve the overall goal of broadening share ownership.

1. More Public Offerings are needed

The M.P. is encouraged to pursue the movement successfully started with CTM-LN and CIOR. More Initial Public Offerings are needed in the capital market. The supply provided will attract new investors and will make investing in privatized shares a familiar experience for the general public. From the over-subscriptions of the CTM-LN, CIOR and WAFABANK offerings, it is expected that future IPOs may have similar success.

Secondary Public Offerings should also be put forward for those companies already listed on the BVC (such as SOFAC and EQDOM). See recommendation III.A.9.e. on already listed companies.

2. Technical Improvements for future IPOs are needed

a. Broader Marketing and Distribution Channels

The M.P. should consider the use of broader mechanisms for the marketing and distribution of its public offerings. Commercial banks are already being used, their network is large and relatively spread out throughout the country. Commercial banks will tend to place the shares to their own clientele and not try to reach out to other potential investors. The lead position should be opened to non-banks or rotated among the banks in order to reach at least the client base of the syndicate leader, and thereby broadening share ownership. Insurance agencies might not be currently efficient at stock distribution and may be prevented from doing so by the existing financial laws.

b. Underwriting

The Privatization Unit should consider undertaking one of the privatizations earmarked for a public offering on an underwriting basis. This approach could have the benefits of closer-to-market pricing, a better informed and more motivated syndicate and placement among a broader group of investors. The fee structure of an underwritten transaction should reflect the risks associated with the underwriting and provide an incentive to all syndicate members to place securities. The CIOR privatization was not an underwriting.

c. Placement Syndicates

Placement syndicates should be expanded to non-bank financial institutions. Diversifying the syndicate leadership and distribution to include new financial intermediaries such as Interfina, Upline, Casablanca Finance Group, etc. could enhance public offerings by opening them to other investors, in particular, foreign.

d. Additional IPO technical factors

- **Fix the nominal value of shares at the minimum Dh 50 permitted by law to test the impact of unit pricing on small individual savers.** For example, had the nominal value of CTM-LN's shares been set at Dh 50, the shares would have been priced at Dh 125, possibly resulting in even broader share distribution among individual savers.

- **Obtain and analyze the data on investors gathered by the banks during the WAFABANK, CTM-LN and CIOR offerings.** This data should be fairly easy to collect and may serve as the basis for upcoming offerings. In addition, this information could be used by the Index as described in section III. B. below.

- **The contractual agreement between the M.P. and the issue manager should include an analysis of its impact on broadening share ownership as well as an analysis of post-issue trading.**

- **The Subscription period of each offering should be closed when the total amount of shares offered has been sold.** This practice would allow investors to subscribe to the number of shares that they actually want to purchase. The current system elicits investors to over-subscribe (thus skewing demand) and to place their order on the closing day of the subscription period.

- **The terms of the offering should provide an over-allotment which permits the issue manager to manage unanticipated excess demand.** Over subscription of an issue is an indication that the price of the issue was set too low to balance demand and supply. As underwriters and placement syndicate gain more experience in the markets, one can expect that pricing decisions would more closely approximate the market. Pricing of IPOs can never be an exact science; only experience in the market can serve as a guide.

3. Specialized Financial Institutions Initiatives should be Considered

a. State holding companies could transfer their portfolio into OPCVMs to be sold to the public

BNDE, CIH and SNI are all privatizables that could sell their risk-diversified portfolios to the public.

The method by which the specialized financial institutions will be privatized is a complex issue because of their extensive holdings of other privatizables. The interests of the State, the general public, the financial markets and individual investors may be better served if State holding companies transfer their independently valued portfolio of companies to OPCVMs and sell these OPCVMs' shares to the public and invest the proceeds in money market funds until their privatization. **We urge the M.P. to consider this option.**

Each specialized financial institution should establish its own OPCVM. Excess participations would be transferred up to the maximum contemplated by the OPCVM law. Creating OPCVMs could avoid politically charged discussions on how to privatize the financial institutions. In all cases, cash proceeds would revert to Treasury.

b. CDG's fiduciary portfolio should be invested in the market

The CDG financial circuit is currently separate from the main (banking) financial circuit as a source of Treasury financing. In item 4 below we recommend the listing of all Treasury instruments. Similarly, we recommend that the funds managed by CDG transit through the financial markets. The composition of CDG's portfolio would remain unaffected since all CDG investments are in Treasuries prescribed by law. Opening its financial flows to the market will reinforce CDG's fiduciary function. The swing through the market will not only create liquidity but will also provide both the Treasury and the CNSS with optimized costs and returns, respectively.

4. Government Financial Sector Reform Measures should be considered

Treasury borrows in a manner that constrains the growth of a sound, competitive financial sector. Its specific instruments are designated for specific investors and do not pay "market" rates. Treasury pays too little on mandatory instruments and too much on others. For Treasury to reach a financing balance through the markets is very material to the broadening of share ownership. **The M.P. should promote reforms that create more market fluidity, enable more trading activity, and facilitate access to liquidity.**

a. Listing of Treasury Instruments

Treasury auctions should be open to all investors for all maturities. Treasury should tap a larger and more diversified group of investors, through a well organized auction process.

Immediately and throughout the privatization process, the listing of all its instruments would acknowledge and validate the existence of the new financial market, allow trading (hence liquidity) of Treasury's instruments. Treasury's elimination of EN bonds and mandatory bank allocation would activate the capital markets and make them the focus of investment and liquidity.

b. Mandatory Allocation

Mandatory allocation may be swapped for an early enforcement of the new prudential rules (in particular, anticipated loan loss provisions) in the form of any Treasury instrument. By allowing the market to select maturities, Treasury would know on which instruments to concentrate its use of the market.

c. Freeing Treasury's Interest Rates

Treasury should allow the interest rate on all its instruments to be determined by the market. This procedure will be most easily introduced when all instruments are listed on the BVC and offered through an auction process where the financial institutions (including money-market OPCVMs) participate as principals and/or on behalf of their clients. **Treasury should review the terms and conditions of issuance of the Emprunts Nationaux** (EN), particularly the high coupon. ENs are costly to the State and the effective base for corporate lending rates. Such review might lead to the creation of a bond market, as described later.

The lending rate ceiling should be eliminated to allow risk lending by the banks. As banks would be freed from ceiling rates on lending, the Central Bank and MOF should pay close attention to the evolution of liquidity both in the markets and at the banks. Excessive bank destabilization would stress both the nascent financial markets and the corporate sector, with unfavorable consequences. Banque Al Maghrib's control over rates would be implemented by its own participation to the auctions and in the secondary market. All bank lending rates would be freed simultaneously with Treasury auctions all its instruments.

The ceiling on bank deposit rates (carnets de dépôt) might have to be maintained for a transitional period to facilitate the transfer of liquidity to the financial markets.

d. Tax Issues

Current tax policy distorts patterns of investment and bears unevenly on different financial instruments. While dividends are subject to double taxation, capital gains and the issuance of rights and stock dividends remain un-taxed. Hybrid financial instruments would result in complex tax treatment. **The Finance Ministry should be encouraged to reconsider the present tax treatment of financial instruments to remove the most important inequities among different instruments.**

5. Money Market Funds and Interbank Market should be Created

The M.P. should encourage the creation of Money Market Funds (MMF). MMF should exist as a deeper, cheaper and more flexible funding alternative to banks. Ultimately, MMF will enhance share ownership because they enable short term liquidity to exist in the financial markets and might draw liquidity from people outside the target, for instance through a MMF managed by CEN.

The voluntary development of a transparent interbank market open to all holders and seekers of liquidities would, among others, justify that CDG lend to banks while the Central Bank seeks to constrain liquidity by soaking it out of the market. Such a money market would similarly enable the Central Bank's controls, fund managers to place dis-invested funds and corporations to issue commercial paper without subjection to banks' policies and intermediation. As said earlier, the money market provides the liquidity needed by the capital (share) market.

Capital markets unencumbered by the frictions described earlier would be efficient and effective in tapping equity for over-leveraged companies, while offering new and attractive investment opportunities to investors.

6. New Financial Instruments should be considered

The M.P. should propose new financial instruments to create alternative investment opportunities which will stimulate broadening of share ownership. The utilization of new financial instruments in the process of privatization has potential for the broadening of share ownership, either directly in the case of hybrid equity instruments, or indirectly in the case of debt instruments purchased by the new SICAV and FCP vehicles. All these instruments are, at various degrees, appropriate for public investment. They will be under scrutiny of both MOF and CDVM, the authorities responsible for their creation and supervision.

Whereas the CDVM law might allow new financial instruments, the Commercial Code in its present form (Dahir of August 11, 1922) specifically limits corporate shares to common shares and two more restrictive types. Currently under revision, the Code will not facilitate the creation of new instruments for some time, even if SAs and SCAs (corporations seeking recourse to public savings) have been given priority review. No formal legal opinion has been received on this matter of the rule of law for the purposes of this report. **The M.P. legal counsel should render an opinion on this issue in close coordination with CDVM.**

Following is a description of the new financial instruments envisioned.

a. Straight and Convertible Bonds as Part of the Transactions structure

The M.P. should attach top priority to incorporating a bond component as part of the transaction structure of selected privatization candidates. Diverse instruments broaden investors' choices. Not all privatizables will or should be "IPO'ed". Some tenders might be structured to include a corporate bond issue offered to the public. For example, the General Tire transaction could have been structured to include a convertible debenture sold to the public which might have resolved the share price differences between Buyer and Seller. The presence of bonds should not affect the next asset value of the privatizable company or the cash proceeds to the State.

Convertible bonds have remained in draft form since the 1970s. Concerned about the public's ability to understand this instrument, MOF has considered its complexity negatively. The new professionally managed investment funds provide the opportunity to introduce this financial instrument to them in a manner which allays MOF's concerns.

The decision to use straight or convertible bonds is a matter of market appetite, financing structure and negotiations. Potentially suitable bond issuers among the 1994 privatizables might include BCP and Brasseries du Maroc.

b. Corporate Bond Issues should be encouraged

The M.P. should also champion the use of corporate bonds in the private sector. The emergence of bonds would make them more commonplace among the public and would contribute to the development of investment alternatives. Corporate bonds are generally issued at a spread over Treasuries; thus, the introduction of a corporate bond market would provide the Treasury with additional rate and volume markers, enabling it to position its own products with greater certainty. It would contribute to the development of the yield curve. The appearance of new issuers would not be incompatible with the Treasury's need to assure its own financing. It would create a demand which could be further stimulated by the investment funds (SICAVs and FCPs).

Commercial banks are limited in their ability to meet the medium- and long-term financing demand of private industry. To date, only selected state-owned agencies have issued bonds, all with government guarantees. Three agencies offered seven issues in 1991 for a total of

Dh 2.2 billion, compared with Treasury issues of Dh 19.5 billion. Private companies have issued commercial paper, but no bonds. Fostering corporate access to the bond market would supplement term funds from specialized financial institutions.

The current narrowness of the financial market calls for a dialogue between the Treasury and the principal financial intermediaries to coordinate and control bond issuance during a transition phase. Transitional fiscal incentives in the form of a tax abatement according to maturity could be considered, and a tax credit on bond interest reinvested in other bonds as exists for dividends and the purchase of shares. A more active financial market based on a more competitive auction of Treasury bonds would facilitate bond issues by private companies.

c. Hybrid Equity Instruments

Certain financial instruments which are not available within the new legal framework play various roles in other mature financial markets. **The M.P. should consider championing the introduction of such instruments in Morocco.**

(1) Certificates of Investment ("CIs")

These certificates represent a form of equity ownership without voting rights. CIs and similar instruments have been utilized successfully in countries with many closely-held family businesses, like France and Italy. They can open the door to BVC listing for family businesses without giving up control. The instrument would be suitable currently: management and shareholders are not yet separate, but the next generation will be more likely to split control between management and ownership. A company could issue CIs now and would move to issuance of common shares at a later date.

(2) Certificates of Investment Preferred Dividends (CIPs)

This form of CI offers a preferred dividend to compensate for the non-voting rights of CIs. CIs and CIPs have some liquidity disadvantages because of their non-voting, "intuitu personae" characteristics. They may have limited suitability in the context of portfolio diversification.

One local financial institution believes the instrument could work now in Morocco. This institution would purchase CIs and CIPs for a SICAV that it contemplates to create.

(3) Preferred Stock and Convertible Preferred Stock

These instruments would provide flexibility to corporate issuers and investors alike. Their introduction is not feasible without adjusting the legal framework for share issuance, either by incorporating appropriate clauses in the Commercial Code or by allowing through decree or de facto the CDVM to rule on such usage.

d. Mortgage-Backed Securities

Mortgage-backed securities consist in bundling up assets to back securities sold to the public and offer a standardized mechanism for the financing of housing and other real estate. Investors refinancing through this mechanism may transfer their newly-found liquidity to share investment. Yet, Roman law does not allow for the assignment of mortgages ("intuitu personae"). The Ministry of Finance has commissioned a USAID study on securitization. This study should serve as reference.

7. Credit Analysis/Corporate Research Expertise is Required

Banks have not developed much expertise in credit analysis or corporate research. These tools will be necessary in the more vigorous capital markets lying ahead. As there is little expertise in credit analysis and corporate research, **an independent and professional organization should be created to guide investors and banks alike with a rating, or at least an assessment, of each issuer and each issue.**

Both CFG and Upline, two private sector companies, have started producing corporate research with a view towards filling some of the credit and information needed by investors. In order to standardize and improve the quality of information, the CDVM should join forces with the Stock Exchange and the Association of Stockbrokers (AIB) to facilitate the creation of an independent rating organization.

8. Self Policing Rules are Required for Stock Exchange Intermediaries

The Ministry of Finance is supporting the broadening of share ownership by initially vesting all market supervisory powers with CDVM. **The Ministry of Privatization should champion the implementation of self policing rules for the stock exchange intermediaries which will have an effective impact on the privatization program and the capital markets.** The Ministry of Finance's scrutiny will create more transparency and will force more fluidity in stock exchange dealings.

The SEI Association ("AIB") will be a new professional body. AIB will have to produce its own ethical and self-policing rules. They are a very important component of Broadening share ownership. **The M.P. should provide technical assistance to the association to ensure that its self-policing rules protect the SEIs' clients and respect the integrity and transparency of the markets where both SEIs' and clients are active.**

The basic principles for self-policing rules should include:

- The interests of the clients come first;

- The respect of the integrity and transparency of the local financial markets must be policed by operating guidelines that meet the standards of security found in international markets and that are formulated similarly;

- Each brokerage house must establish its own rules and do so within the guidelines defined by the Association.

The parameters for the development of self-policing rules include:

- **Organization:** use the legal, human and technical resources necessary to avoid conflicts of interest, in particular keeping at arm's length the roles of trader, portfolio manager and counterpart;

- **Client information:** should be clear, complete and immediate on each transaction; describe the risks inherent to each contemplated transaction; communicate the status and completion of each transaction quickly;

- **Contractual agreement:** enter with each client into a written agreement including the general terms of operations, specific conditions applicable to the account (as broker or manager), pricing for services and mutual obligations;

- **Control:** a compliance officer must be designated by the firm and confirmed by the controlling authority (CDVM); he must be provided the means (including the recording of all telephone conversations) to perform his duties; the ultimate responsibility for control remains with the firm's top management who should be subject to CDVM scrutiny;

- **Staff:** set rules regarding employees' own transactions; a trading account and trading activity must be disclosed to the employer and must be in-house; confidentiality of information and transactions must be maintained; trading on insider news and information must be prohibited; the house cannot charge preferential fees or commissions to the staff; client and firm trading have priority over personal trading, which is only allowed on securities not otherwise handled directly; no employee may have a role as counterpart;

Sanctions: at a minimum, they should cover the responsibility of each individual and the firm towards third parties (including clients) and the respect of both in-house operating rules and the integrity and transparency of the market; they should be graduated from internal to external, by the authorities, under civil and penal laws.

9. CDVM must be operational and the BVC's Operations must be improved

The CDVM law is the cornerstone of financial market reform. **It is urgent and fundamental that this organization be in full operation immediately.** Without the regulatory foundation in place, the development of active and vigorous capital markets will be jeopardized. The CDVM will be successful in its role as regulator and catalyst only if its management and staff are of the highest quality, fully cognizant of their role and capable of fulfilling their task. Some in the private sector have suggested to retain an international recruiter to search for a top-notch head of the CDVM.

The drafting of the statutes and regulations of the newly created CDVM has begun. The Ministry of Finance and the Conseil Deontologique des Valeurs Mobilieres may need the immediate assistance of Securities Exchange Commission and/or Commission des Operations de Bourse experts to help in the quick and effective of drafting the statutes and regulations of the agency. **The M.P. should provide input to the drafts and start communicating to the general public the purpose of the CDVM, the process and progress of its creation in order to bolster confidence and stimulate the broadening of share ownership.**

The operations of the BVC will need improvement to face a more sophisticated market. **The M.P. should champion that changes be made to BVC operations.**

a. Disclosure

The public would be served, and its confidence in the new systems would improve, with the principles of corporate disclosure and the protection of minority shareholders written either in the Commercial Code instead or CDVM's regulations. Since both texts are still to be written, the first one to be produced will serve as a practical base.

Failure to provide accurate disclosure and quality financial reporting would result in public cynicism and jeopardize the public trust in all financial market operations. Effective disclosure should encompass not only the accuracy of financial statements, but equally important, the timely public announcement of all material events relating to the company. Broadening individual share ownership hinges on the trust of the investor. That trust can take years to establish; and can be destroyed by only a single incident of unfair trading.

b. Central Clearing and Depositary

A scripless book entry system to transfer ownership (i.e. settle transaction) should be implemented to facilitate trading and to reduce systemic risks. The first public offering under privatization was CTM-LN. Because of its popular success, actual shares could not be distributed to all their owners for 2 months after the issue. Yet, CTM-LN trading was active on BVC, without actual shares being exchanged. The financial system had effectively "de-materialized" the CTM shares and intuitively adopted a book entry system to record the CTM-LN transactions. That a scripless system occurred so informally is the indication that its usage could be easily accepted by the market.

It is interesting to note that the legal draft on the standardization of physical securities certificates describes their size, the quality of the paper and the colors to be used, the positioning of information on the document and their maximum and minimum measurements and tolerances. The purpose of these requirements being to avoid counterfeits and easy manipulation. This end would be better served by a scripless book entry system.

Eliminating the delivery of securities (set at 21 days in the new law) would reduce human errors, physical theft of stock and the credit and delivery risks on the brokers.

c. Listings Requirements

Requirements for listing are too high. They should be reviewed to be more in accordance with Moroccan reality where the average amount of capital raised by companies are smaller than in developed markets.

Alternatively, the authorities could sponsor a separate "board" or "second marché" (similar to the Over the Counter Exchange of India) on which new issues of small and medium size companies would be listed. The conditions of listing would be much lower and would permit small and entrepreneurial companies to gain access to the capital market. It is understood that higher risk will be attached to such companies, nevertheless as long as the prospectus fully discloses all material risks, investors should be allowed to make decisions based on their own assessments. (see above recommendation on disclosure)

d. Off-Floor Trading

MOF recognizes that off-floor trading is flawed, but has maintained it in order to facilitate market liquidity. **Off floor trading should be limited to trading between principals, under stock exchange supervision with immediate reporting.**

e. The BVC should mandate currently listed companies to increase the "float" of their shares to meet at least the new listing requirements of 20% of shares outstanding.

Companies should take more responsibility for creating conditions favorable to the liquidity of their listed shares. Listing agreements of most exchanges around the world require measures such as ensuring 500, or more, individual shareholders, or higher percentage of the company's shares outstanding to help create improved conditions for liquidity. There is no reason why the BVC should not enforce similar provisions to attract core business for itself and to assure investors that it will impartially protect their interests as well as these of listed companies. Ultimately, the BVC has an obligation to be equally fair to all three groups: issuers, brokers and investors.

10. Stock Pledging should be Allowed by the Law

It is strongly recommended that the Ministry's legal counsel render an opinion on whether stock pledging is allowed under the law. In the event it is not, the M.P. should champion an amendment to the law to permit stock pledging, along with language that supports the rights of the party receiving the collateral to act on his lien and liquidate the stock if necessary to meet the obligation.

B. RECOMMENDATIONS TO STIMULATE DEMAND

Recommendations 1 to 3 are addressed to the M.P. while recommendation 4 is to be sponsored by the M.P.

1. New Individual Investors should be Targeted

Both economic efficiency and Morocco's social make-up suggest that the M.P. focus its Broadening Individual Share Ownership efforts on certain core targets and results measured against them. A realistic **target** of individual owners of corporate shares would cover some 857,000 households, of which 400,000 live abroad (RME).

a. Target A: Top Urban Households

From the analysis presented in Section II, it follows that the top 457,000 urban households of 1991 are most likely to have saveable income and to understand financial markets and savings instruments. **This is Target "A".** The most prone to buy shares within the group appear to be among the core 360,000 Casa-Tanger households. To attract these potential investors, a revised taxation of investment instruments and several promotional activities are recommended. (See recommendations B.2 and C. below)

b. Target B: Residents Marocains a l'Etranger

The Moroccans living abroad (RMEs), particularly in the EC, constitute a geographically separate target of some 400,000 households of relatively higher means. **RMEs constitute Target "B".** It is separated from target "A" because of its different geographic focus.

In addition to general public relations initiatives recommended in Section C. below, the Ministry of Privatization should target overseas media that is specifically aimed at Maghreb residents, primarily radio based. Such media via France or other EC country could be used effectively to convey investment promotion messages.

Similarly, several Moroccan commercial banks are linked to or have representative agreements with foreign banks in EC countries. The latter could address messages directly to the households via their regular customer communication. The Maroc Privatization Mutual Fund described earlier is probably one of the best mechanism to tap RMEs savings in France. Other similar funds should be promoted for other EC countries.

c. International Investors

Current efforts by the M.P. to include international investors should be encouraged. Foreign participation in privatization transactions, if carefully structured, will have a positive effect on the confidence level of domestic investors.

However, it should be noted that opportunity for foreign investments is limited when the market is void of instruments, when 5 or 7 stocks dominate BVC trading, and when there is little financial fluidity for lack of money markets. The currency market is key to accessing foreign liquidity. Foreign currency accounts have been the single most important factor in the newly-found liquidity of Egypt's financial market. Additionally, Latin American countries generally experienced a foreign capital inflow upon allowing full convertibility of their currency.

2. The M.P. should Keep Track of New Individual Investors through an Investor Base Index

a. Creating an Investor Profile

The M.P. should develop a standard investor profile based on both existing macro-economic data and data collected by the manager of each public offering.

The M.P. could use the profile as a guide to launch its public privatizations and as a benchmark to analyze the results. The standard profile would be used over time to measure the progress realized in building a population of shareholders, both within the core and the expanded targets.

A standard investor profile would include the distribution of share purchasers by age, economic breakdown and regional origin, date and number of shares requested, first-time or repeat share investor, client of or outsider to placement syndicate members, mode of financing of purchase (fresh cash, bank deposit, etc.), committed amount of each purchase in relation to the size of the purchaser's revenues, bank deposits and, if possible, size and nature of other savings.

b. Setting an Investor Base Index

With the exception of BCP's and WAFABANK's data on investors (see section II.E.), we have found no evidence of the existence of a meaningful population of individual share owners from which to establish a current base. Consequently, we have fixed the base at level 100 on January 1, 1993. We have assumed that the shares of the WAFABANK's IPO of the previous month were distributed later.

An **Investor Base index** to measure over time the absolute growth of individual share owners and the relative penetration of share ownership in both core and expanded targets can be derived from the statistical analysis of data collected during each new public share issue from both new and existing share owners. The nature of the data is social, demographic, professional, economic and financial. In the absence of statistical reference to macro-economic data on income and savings, the index must be self-supporting and integrative.

The minimum standard investor profile data would be gathered by anonymous questionnaire. It would include:

- parameters of each specific issue;
- distribution of committed investors, size of requested shares and region by member of the placement syndicate;
- distribution of share purchasers by age, economic breakdown and regional origin;
- distribution by subscription date, number of investors and shares requested;
- distribution by purchasers' income and size of bank deposit(s);
- mention of a first-time or repeat share investor;
- mention as client of or outsider to placement syndicate members;
- mention of reason of investment;
- mode of financing of the share purchase (fresh cash, transfer, bank deposit, etc.);
- source of fresh cash or transfer;
- committed amount of each share purchase; its size relative to revenues and assets;
- size and nature of the other savings of the investor;
- detailed participation to any health or retirement plan (including Social Security), life insurance, etc;
- use contemplated for the liquidity disengaged from the share purchase because of share allotment.

The M.P. should use the index as a guide to launch future public privatizations and as a benchmark for their results. Over time, the standard profile could also be used to measure the progress realized in building a population of shareholders, within both the core and the expanded targets. In addition, as recommended in section III.A.3.d. above, the M.P. should require the syndicate leaders of upcoming IPOs to provide an analysis of the IPO and post issue trading.

3. The Financing issue for Employees and Special Interest Groups should be addressed

(The following mechanism specifically addresses shares for employees. Appropriate changes could be applied to other types of social ownership.)

The M.P. should promote the creation of an Employee Stock Fund ("ESF") that would manage and finance the shares that the State dedicates to employees and special interest groups.

As discussed in Section II.C.6 above, any plan to incorporate employees in the divestiture process must take into account 1)that shares must be paid for in cash up front; 2) that any investment fund must be employee-owned to qualify for the 15% discount; and 3) that employees must retain their shares for three years to qualify for said discount.

The recommended approach below addresses the constraints listed above and appears to be within the privatization legal framework **The M.P. is urged to review and modify this employee proposal as necessary in order to finalize a framework which can support each employee transaction.** In this regard, the M.P.'s legal counsel should review the relevant legislation to render a legal opinion on the final plan's validity. In addition, the M.P. should appoint an "ESOP specialist" among its professional staff who will assume responsibility for employee education and participation in the privatization program. Required training should be provided as appropriate.

a. Recommended Operations

The following are the recommended guidelines for the implementation and operation of an ESF:

- The employee stock fund must be established as employee-owned. This might be in the form of a cooperative or an FCP. Each enterprise for which employee ownership is envisioned will have a separate employee-owned fund. The existence of each ESF will be 3 years.

- The ESF should be managed by an outside investment adviser. CDG, which handles pension/social security funds, could serve in this fiduciary role.

- The ESF will establish a savings plan with each employee and will hold their shares on their account.

- Financing for the ESF would be provided by Treasury at its 3 year lending rate. The ESF would reimburse Treasury over a three year period. The M.P. could also approach bilateral and multilateral donors to set up a revolving fund which would serve to finance all or part of selected ESFs.

- Each employee will purchase of ESF "units" to be converted into full shares once the full price is paid. Actual shares will be delivered to the employees at the end of the three years when the time period for earning the 15% discount has been met. As an incentive to participate, the unpaid income tax would be deferred during the life of the ESF and forgiven at maturity. **Tax policy to this effect must be championed by the Ministry of Privatization.**

- Each unit will represent 10 DH in value and will constitute a fraction of the offering share price, discounted for employees and increased for the management and finance costs associated with the ESF's operations (3 years).

- If an employee decides to end his participation before the three year period, he recoups his investment less certain costs and penalties as described in item (e) below. Ability to leave the plan is critical to ensure the liquidity of their investment.

b. Introducing ESF to the Social Groups

A M.P. seminar for employees would be held in each company slated for privatization with an employee stock participation. This seminar would explain the privatization process and its consequences. It would also detail precisely the opportunity, including any tax savings, to acquire shares in the company and the financial obligations that employees will incur to benefit from this opportunity. Moreover, the seminar should discuss stock price volatility and describe dividends, dilution and investment alternatives such as housing, (additional) pension funds and health plans, and investment in OPCVMs.

c. Election by the Members of the Social Groups

Within two weeks of the seminar and prior to announcing the privatization, employees would have to declare their willingness to participate in the ESF and, if so, for how many units. Each unit will represent a fraction of the corporate share price offered to employees at issuance, plus 1.6 times the then current 3-year interest rate p.a. on Treasury notes, and plus 6% for the 3-year ESF management fee. A DH 10 value of each unit is small enough to facilitate employee participation; 1.6 (times the 3 year Treasury rate) is based upon the average financing outstanding under an assumption of even repayment installments; a 2%

annual management fee or 6% over 3 years is reasonable given the expected small size of the employee funds.

Demand for units that, when converted in shares, would exceed the legal maximum of 10% employee share ownership would be allotted. The plan would be declared immaterial if less than 20% of all employees participate, or if their participation does not reach altogether a minimum 3% of corporate ownership. Employees should also be asked then if they would have preferred to participate in other investment plans described during the seminar, which one(s) and to what extent.

d. Conversion in Shares

Any time an employee has accumulated enough units for conversion into one share, the employee may elect:

(i) to let ESF convert them is a share held in his name;

(ii) to notify ESF to pay him the cash value of the redeemed units net of deferred income tax and other charges.

e. Leaving ESF

An employee may notify his employer and ESF of his decision to drop out of ESF at any time prior to expiration of the 3-year period. He would then receive an amount (net of deferred income tax) equal to the current cash value of the shares in his name plus the cash value of any unredeemed units, minus the amount of the original 15% employee discount and minus the ESF management fee (2, 4 or 6% if he drops out during year 1,2 or 3 respectively).

An employee leaving the company will be associated to someone dropping off the program, while someone being fired will only receive the lesser of the cash value of all collected units or the then current market value of their share equivalent, net after deduction of the original employee discount and deferred income tax. An employee retiring from the company will receive his accumulated shares and the cash equivalent of any unconverted units **free of tax**.

At the end of the 3-year period, ESF would deliver to the employees their corporate shares and an amount of cash pro-rata any operating bonus.

f. ESF exposure and risk to the financial intermediary

ESF's exposure is limited to the cash risk on units not yet converted into shares and only in the event that share prices decrease; this exposure is minimized by the up-front interest factor, the pooled employee share discount and the "drop out pool" that accumulates the proceeds of shares sold over time at a price in excess of the units' cash redemption value.

4. Institutional Investors Should be Encouraged

Fund management has become prevalent in developed and emerging countries alike. Professional investing is better investing and an important factor to broadening individual share ownership. Private sector competition, through advertising and other marketing techniques, will enhance the public knowledge of securities.

The banking community is primed to participate in OPCVM development and is awaiting the creation of CDVM. As highlighted throughout this report, without the CDVM in place, the initiatives to invigorate the capital markets will simply not occur.

Insurance companies should be allowed to establish OPCVMs which should act independently and be governed under OPCVM rules as banks and specialized financial institutions. **Insurance companies and the financial sector should be encouraged to create OPCVMs and/or to sell OPCVM certificates.**

C. PUBLIC RELATIONS

Experience so far indicates that a substantial investment potential exists. Communicating facts is the means to convert this investment potential. More communications organized by the M.P. would create more visibility for privatization, convey its purpose more frequently, explain its process repetitively, advertise its future operations and nurture public confidence through the transparent disclosure of its activities.

An advertising and public relations campaign to attract RMEs into the privatization program would be particularly timely as many RMEs have received better exposure to the financial reforms and privatization opportunities in Morocco. The M.P. should lend its support and credibility to an effort by the commercial banks in this regard.

1. Regular PR activities by the M.P. should be undertaken

Various activities have been undertaken by the Ministry of Privatization. **The following PR activities are recommended both to enhance the privatization program and to serve as a champion for recommended financial markets reforms:**

a. Publish a monthly Bulletin de Liaison (newsletter) to circulate news on current M.P. actions to other Ministries, financial institutions, banks, the media, etc.

b. Invite TV to present future privatizables and their management, and to interview individuals who have become shareholders through the privatization process regarding their motivations and expectations.

c. Proceed to a thorough de-briefing of each operation for the media, including: the rationale behind each privatization strategy; the hurdles and humorous moments encountered during the operation; the benefits to the country and the national economy.

d. Invite TV to report frequently on privatizations, the Ministry's staff and its activities in order for the public to better understand privatizations, to feel closer to their process, to be more concerned by their results and to grow more interested to hold shares of privatized corporations.

e. Use M.P.'s Minitel line to provide a daily (weekly) update on privatization: data on companies for sale, contemplated mode of transfer, list of people handling each industry or group.

f. Organize the "privatization vacation": a travel circuit within Morocco for foreign CEOs and Emerging Country Fund managers to discover and understand the country, to see privatizables, to hear valuation experts, to be briefed on the whole privatization program and their possible participation in it.

g. In conjunction with the RME Ministry and the various banks targeting RMEs, the M.P. should create an "RME" approach to share ownership. Such a strategy should suggest alternatives to idling funds in bank deposits and inform this target group on forthcoming privatization opportunities.

There are at least four Moroccan institutions that plan to or currently cater to the RMEs. Their initiatives towards their clients should be left to their discretion. To support these private initiatives towards the RMEs, the M.P. should actively promote and advertise to them the strict controls and rules of ethics to which the new financial vehicles must subscribe under an efficient and capable CDVM.

2. Information Seminar on Broadening Individual Share Ownership should be held

The objective of the seminar will be to create transparency by explaining the directions taken by the M.P. and the actions expected from all institutions, to set a base for understanding the new capital markets and to induce confidence in their process and therefore share ownership. As noted above, many of the recommendations aimed at broadening share ownership reflect changes to the enabling environment and are not under the direct control of the M.P. **The M.P. can enhance its role as champion of these changes through a broad based seminar targeted to the financial institutions, the press, potential private issuers and social groups.** Participants/presenters should include representatives from the M.P. and MOF, the Conseil Deontologique des Valeurs Mobilieres (CDVM), the Bourse des Valeurs de Casablanca (BVC), institutions having formed or forming investment funds. Potential investors will have a forum in which to present their concerns and questions through open dialogue.

The seminar might be a day-long event that could cover the following subjects:

- need for market liquidity: attracting investors (savings, RME and foreign investments), market-making and secondary markets, tie to other financial markets
- CDVM & Bourse: operation, supervision, self-policing and regulation
- purpose & code of conduct of transparent SICAVs & FCPs
- actual transparent vehicles (OPCVMs): their own standards, managing institutions, strategies and operations
- existing and future investment instruments (shares, bonds, convertibles, preferred, etc.)
- Tax homogenization of financial instruments: today and future expectations
- the need for transparency and disclosure: what it means, how it is achieved
- rights of shareholders: information, off-market transactions & take overs
- SOE transfers and individual ownership: availability, security and liquidity
- preview of upcoming SOE transfers and privatizations.

3. Seminar for the media on financial environment, analysis and writing should be held

A seminar addressed to l'Economiste, La Vie Economique, Enjeu, La Lettre du CMC, other economic journalists and staff of financial institutions, should be conducted to create an understanding of (i) the new financial markets, institutions, vehicles and instruments and (ii) actual transparency and financial analysis to improve understanding and (iii) media coverage leading to accurate reporting to the public.

Subjects would include:

- **New Financial environment**: Public Finance, Treasury, Financial markets, Banking, Securities Exchange, OPCVMs, international trade and financial markets

- **Transparency**: disclosure and accuracy - what it means in language, in accounting, in statistics, for corporate disclosure; the cultural impact of statism, of an informal economy and family-owned companies

- **Corporate Finance and analysis**: reading financial statements, financial reporting, financial analysis and ratios, sectoral characteristics, interaction among sectors and with Public Finance, the notion of exposure and risk

- **Event reporting, economic and financial writing**: fact gathering, event and environment, writing for whom, driving to the point; a live case to write on

- **Case discussion and conclusion**: participants' presentation of their article; review and discussion.

4. TV Program on Investing should be considered

An ambitious but potentially highly effective component of the M.P.'s public relations plan would be the development and implementation of a TV program. This would be accomplished jointly with other capital markets players who have a stake in broadening individual awareness of capital markets. In addition, the Casablanca Finance Group has indicated interest in providing assistance on the conception and realization of such a program. The program would be broadcast as a long-term TV series. Its principle and contents have been discussed with RECOM, the company producing "Entreprendre", the only regular economic series on Moroccan TV. Its purpose will be to build confidence in the whole financial system and gain familiarity with it. It will be done in a lively format of interviews with practitioners and "field trips" to investment institutions, the issuers, the regulatory agencies, etc.

The program would describe such issues as:

- the purpose of investing and how to do it (practicalities), how it compares to other forms of savings (jewelry, cash, real estate, bank deposits, retirement funds, life insurance);
- the functions, rewards and risks associated with various forms of savings;
- why transparency makes it a safe process; financial information and the legal obligations towards all investors, whatever their size;
- why the individual can benefit from the process in the same way as the large investor or the institutions;
- existing financial instruments and their function, how and why they are used by issuers and investors;
- buying alone or through professionals; the costs and benefits;
- investment vehicles (SICAV, FCP) available to the public, their managers, operating principles and strategies, their transparency and the regulatory environment;
- the issuers (State, agencies, municipalities, corporations) and their specific risks; how privatization is part of the process;
- the stock exchange, CDVM and other regulatory entities;
- how stocks compare with other savings instruments (bonds, notes, bank deposits, etc.), including their tax treatment;
- how and why to choose among various existing investment vehicles; discussions with their managers (strategies, methods, results);
- where to go and how to buy and sell shares and other investment instruments;
- keeping track of the actual results of the various forms of savings and comparing them;

The program would be a sort of televised presentation of the various aspects (the norms mentioned above) of safe investment (the transparent investment funds). It will raise issues such as protection of minority shareholders and will extend the concept of transparency to potential issuers outside the privatizable SOE group as professional investors state their analytical requirements.

Its educational value could be enhanced by "Transcripts", chapters of a book on savings and investing to be made available to the public by request.

The producers of "Entreprendre", the main economic program on Moroccan TV, are interested in such a series. It could begin in early 1994. RECOM produces "Entreprendre" for monthly prime time broadcast (9:15 p.m.) 10 times per year on RTM (national Moroccan TV channel). It is relayed by satellite to Europe for the benefit of RMEs. RECOM estimates its audience at 14 million people (this is a questionable claim). RECOM buys airtime from RTM and finances its production mainly by selling the video films to the featured companies and somewhat by selling commercials during broadcast. After 2 years of operations, the production breaks even financially.

According to RECOM, a series of 22 installments is feasible on RTM. The program could be aired twice a month in 26 minute installments including no more than 1.5 minutes of commercial time (3 spots earning Dh 16,000 each). Its production cost is estimated at Dh 5 000/minute (Dh 4 million in total).

Alternatively to RTM, such a series could be aired by 2M, the private channel. We could not meet with its management. While RTM has the advantage of a much larger audience, 2M benefits from targeting the profile of current share investors, broadcasts generally more attractive programs and is present in many public places.

Not surprisingly, the issue of financing would have to be resolved. It would be preferable that the series not be sponsored by financial institutions in order to avoid the appearance of self-serving advertising. As the exclusion of such a natural source of financing puts financial pressure on producing the show, assistance from other resources would be needed. As mentioned elsewhere in the report, other TV initiatives might include features on the upcoming privatization transactions to be aired on the "Entreprendre" program.

IV. RECOMMENDED ACTION PLAN

A. AID POLICY DIALOGUE WITH RESPECT TO THE PRIVATIZATION SECTOR ASSISTANCE FUND

In recognition of the Moroccan Government's commitment to privatization, USAID/Rabat established a Privatization Sector Assistance Fund to support the privatization program. Conditions precedent to the disbursement of funds (three tranches) are largely based on achievement of actual progress in implementation. Such progress is measured by completion of specified numbers of actions related to the preparation and execution of transactions. Conditions precedent also relate to public relations and the broadening of share ownership. Concerning the latter, the sale of shares via the stock exchange or a public offering is defined and quantified. Remaining conditions precedent for broadening share ownership are defined as "certain measures, to be mutually agreed to by the parties prior to the disbursement" of funds.

In the recommendations presented in this report, we define certain measures which should be implemented by the Ministry of Privatization (M.P.) to achieve the objectives of broadening share ownership. We also provide accompanying measures to the enabling environment that are required to strengthen the regulatory and operational aspects of the capital markets which will free them of distortions and essentially develop and modernize the entire financial sector. As these are not within the purview of the M.P., we have recommended that the M.P. sponsor or champion the implementation of these recommendations.

The notion of sponsoring or championing policy and operational changes can take several forms. Organized "roundtables" similar to the one held in March 1994 can be effective forums for creating awareness on key issues and constraints and developing through consensus pragmatic solutions. These need to be organized such that key decision-makers from various Government Ministries participate in dialogue among themselves as well as with private sector leaders from the financial community. In addition, such roundtables should go beyond mere discussion to the development of concrete proposals with Ministries/individuals held accountable for selected actions.

Measures recommended in the report with respect to public relations such as seminars, articles in leading business publications, monthly bulletins and the like can serve both the Ministry directly by promoting the privatization program as well as encouraging capital markets reforms.

Finally, the Ministry can champion reforms through leading by example in the transaction structure and procedural operations of its public offerings.

B. ACTION PLAN

We have prioritized the recommendations included in Section III of this report into an action plan depicting our judgement of when specific actions should be completed. The action plan also indicates the groups responsible for their implementation. The action plan is included at the end of this section. Below we summarize the key recommendations, differentiating between those which can be implemented directly by the Ministry of Privatization and those which the Ministry of Privatization can champion.

1. M.P. Direct Measures

The M.P. should continue to consider public offerings as part of the transaction each time such inclusion seems appropriate. (Recommendation III.A.1.)

Technical improvements for future IPOs should be considered. (Recommendation III.A.2.)

The Ministry of Privatization should consider the privatization of BNDE, CIH and SNI, which offer the potential of ready-made portfolios of assets that could be sold to the public, through OPCVMs. (Recommendation III.A.3.)

New individual investors should be targeted and the M.P. should keep track of them through an Investor Base Index. The targets as well as the base for the tracking system are detailed in Recommendations III.B.1 and 2.

The M.P. should promote the creation of an Employee Stock Fund ("ESF") that would manage and finance the shares that the State dedicates to employees and special interest groups. The ESF and its operations are described in Recommendation III.B.3.

The M.P. should encourage/support initiatives by private financial institutions to create and/or to sell OPCVM certificates. (Recommendation III.B.4)

Other recommendations are geared towards public information and relations. The M.P. should undertake regular and specific public relations activities. Recommendations 1-4 in Section III.C provide concrete examples.

2. Accompanying Measures to be Championed by the M.P.

As the attached action plan indicates, there are a number of recommendations which are not the sole responsibility of the M.P. However, it could have a role in sponsoring further study or implementation of such recommendations.

The M.P. should champion certain reforms which will serve to create more market fluidity, to enable more trading activity, and to facilitate access to liquidity:

- CDG's fiduciary portfolio should be invested in the Market. (Recommendation III.A.3.b)

- Treasury should list all its instruments, with Treasury auctions open to all investors for all maturities. (Recommendation III.A.4.a)

- Plancher bonds (mandatory allocation) should be eliminated (Recommendation III.A.4.b.)

- Treasury should allow the interest rate on all its instruments to be determined by the market. (Recommendation III.A.4.c)

- The Finance Ministry should be encouraged to remove the most important inequities among different financial instruments. (Recommendation III.A.4.d)

The M.P. should encourage the financial law makers to foster the creation of Money Market Funds (MMF). (Recommendation III.A.5.)

In addition to leading by example through its own public offerings, the M.P. should champion the development of new financial instruments to create alternative investment opportunities which will stimulate broadening of share ownership. (Recommendation III.A.6.)

The M.P. should encourage the creation of an independent and professional rating organization. (Recommendation III.A.7)

The Ministry of Privatization should champion the implementation of self-policing rules for the stock exchange intermediaries which will have an effective impact on the privatization program and the capital markets. (Recommendation III.A.8)

The M.P. should actively champion the immediate implementation of CDVM. It should also encourage operational changes to the BVC. (Recommendation III.A.9)

The M.P. should encourage any reforms required to allow for the collateralization of shares. (Recommendation III.A.10)

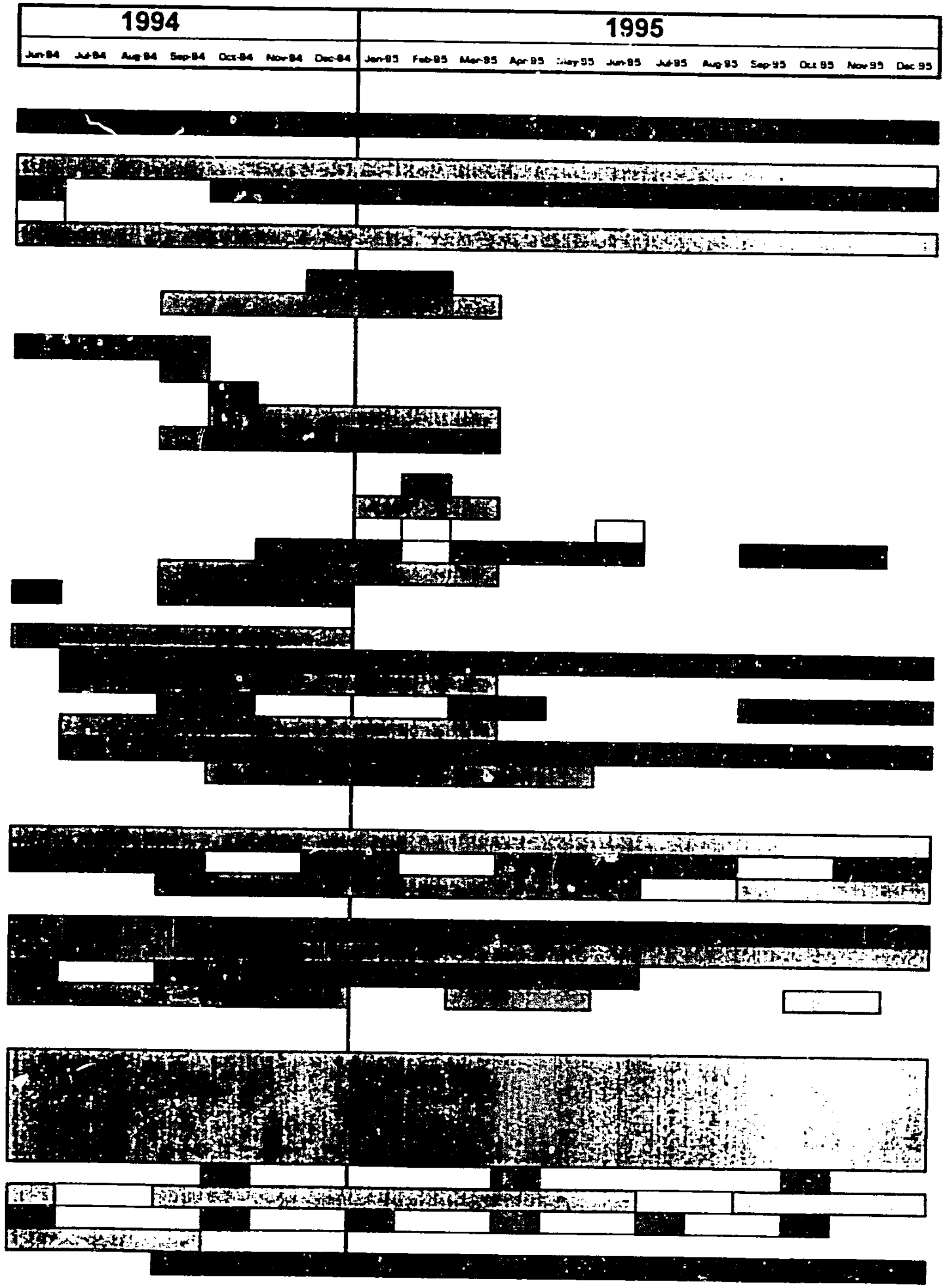
RECOMMENDATIONS

Report Reference

- **A. 1 More IPOs**
- **2 Technical Improvements**
  - a. Broadening Distribution
  - b. Underwriting
  - c. Expanding Placement Syndicate
  - d. Other Technical Factors
- **3 Specialized Financial Institutions**
  - a. Privatization through OPCVMs
  - b. CDG-managed Portfolios through Markets
- **4 Reforming State Financing Practices**
  - a. Listing all Treasury instruments on BVC
  - b. Eliminating Plancher Bonds
  - c. Freeing Treasury Interest Rates
  - d. Tax Matters
- **5 Money Market Funds & Inter-Bank Market**
- **6 New Financial Instruments**
  - a. Corporate Bonds
  - b. Convertible Bonds
  - c. Hybrid Instruments
  - e. Mortgage Securitization
- **7 Credit & Corporate Research Agency**
- **8 Self-regulation Code for StockBrokers**
- **9 CDVM & BVC**
  - \- CDVM
  - a. Transparency towards the Public
  - b. Clearing & Delivery System
  - c. Listing Requirements on BVC
  - d. Off-floor Transactions (cessions directes)
  - e. Secondary Offerings by Listed Companies
- **10 Collateralization of Shares**

- **B. 1 Targetted Investors**
  - a. Privileged Urban Households
  - b. RMEs
  - c. International Investors
- **2 Creating an Index and a Profile of Investors**
  - a. Investor Profile
  - b. Investor Index
- **3 Creation of an Employee Stock Fund**
- **4 Supporting Initiatives by Private Financial Institutions**

- **C. 1 Regular Public Relations Activities**
  - Monthly Newsletter
  - TV Presentations of Current Privatizations
  - Media Presentations of Completed Operations
  - Frequent TV Interviews of the Privatization Process
  - Weekly Minitel Update
  - Organization of Privatization Trips
  - Regular RME Programs
- **2 Privatization Seminars**
- **3 Media Seminar on Financial Analysis & Writing**
- **4 TV Educational Program**



Responsibility

MP
MP
MP, Com. Transf., Org. Eval.
MP, BVC, Syndicate Mgrs
MP, SNI, BNDE, CIH
CDG, CNSS, others
MoF, CDVM, BVC
Al Maghrib, MoF
Al Maghrib, MoF
CDVM, BVC, Private Sector
CDVM, MP, Private Sector
CDVM, MP, Private Sector
CDVM, CIH, Private Sector
MF, CDVM, CIH
CDVM, BVC, AIB, Private Sect
AIB, Private Sector
MoF
MP, CDVM, BVC, Private Sect
CDVM, BVC
MP, BVC, Private Sector
CDVM, BVC
CDVM, BVC, Private Sector
MoF, Private Sector
MP, BVC, Syndicate Mgrs
MP, BVC, Syndicate Mgrs
MP, BVC, Syndicate Mgrs
MP, Syndicate Mgrs
MP, Syndicate Mgrs
MP, Syndicate Mgrs
MP
MP, MoF, MRME
MP
MP, RTM
MP, Economic Media
MP, RTM
MP
MP
MP, MRME
MP
MP, CDVM
MP, RTM/2M, RECOM

Appendix I Acronyms

AIB
Association des Intermediaires de Bourse
BCM
Banque Commerciale du Maroc
BCP
Banque Commerciale Populaire
BMCE
Banque Marocaine du Commerce Exterieur
BMCI
Banque Marocaine pour le Commerce et l'Industrie
BNDE
Banque Nationale de Developpement Economique
BVC
Bourse des Valeurs de Casablanca
CCG
Caisse Centrale de Garanties
CDM
Credit du Maroc
CDVM
Conseil Deontologique des Valeurs Mobilieres
CEN
Caisse d'Epargne Nationale
CIH
Credit Immobilier et Hotelier
CNCA
Caisse Nationale de Credit Agricole
CNSS
Caisse Nationale de Securite Sociale
COB
Commission des Operations de Bourse
CSF
Corporate Stock Fund
CTM-LN
Compagnie de Transport Marocain - Lignes Nationales
Dh
Dirham
E.N.
Emprunts Nationaux
FF
French Franc
IB

Intermediaires de Bourse

IMF
International Monetary Fund

IPO
Initial Public Offering

M
Million

M.P.
Ministere de la Privatisation

MM
Billion

MOF
Ministry of Finance

ODI
Office de Developpement Industriel

ONA
Omnium Nord Africain

OPCVM
Organisme de Placement Collectif en Valeurs Mobilieres

PR
Public Relations

RME
Residents Marocains a l'Etranger

S.A.
Societe Anonyme

SEC
Securities Exchange Commission

SGMB
Societe Generale Marocaine de Banque

SNI
Societe Nationale d'Investissements

USAID
United States Agency for International Development

Appendix II Interviews conducted in Morocco and U.S.A.

A. Financial Institutions

i. **Al Amane - L'Entente**
Mr. Mohamed El Mehdi Boughaleb
Président Directeur Général
Casablanca

ii. **Bank Al-Amal**
Mr. Ahmed Aouam
Fondé de pouvoirs
Casablanca

Mr. Ahmed Rida Tadili
Sous Directeur
Casablanca

iii. **Bank Al-Maghrib**
Mr. Ahmed Bennani
Directeur Central
Département des Etudes
Rabat

iv. **Banque Centrale Populaire (BCP)**
Mr. Eric Aouani
Directeur Central de Comptabilité Financière
Cellule Marché de Capitaux
Casablanca

Mrs. Asma Bellamine
Directrice
Direction des Etudes
Casablanca

Mr. Mohamed Belqziz
Directeur Commercial
Casablanca

Mr. Youssef Ibnabdeljalil
Directeur Central du Marketing
Casablanca

v. **Banque Commerciale du Maroc (BCM)**

Mr. Youssef Alaoui
Responsable de Département des Crédits
d'Investissement et de l'ingénierie Financière
Casablanca

Mr. Ali Iben Mansour,
Directeur Général
Casablanca

Mr. Rachid Tlemcani
Département des Crédits d'Investissement et de l'ingénierie Financière
Casablanca

vi. **Banque Marocaine du Commerce Extérieur (BMCE)**

Mr. Mamoun Belghiti
Directeur Général
Département Crédit et Trésorerie
Casablanca

Mr. M'Fadel El Halaissi
Sous Directeur
Direction de l'Investissement et du Crédit
Département Investissement et Restructuration
Casablanca

vii. **Banque Marocaine pour le Commerce et l'Industrie (BMCI)**

Mr. Ahlam Abakhti-Mchachti
Direction Générale
Département des Affaires Financiers et de la Trésorerie
Casablanca

Mr. Omar Akalay
Vice President Directeur General
Casablanca

Mr. Mohamed Nour-Eddine Mrini
Chef du Département des Affaires Financières et de la Trésorerie
Casablanca

Mr. Ahmed Ouadoud
Chef de Département Titres et Caisses
Casablanca

viii. **Banque Nationale pour le Développement Économique (BNDE)**

Mr. Mohammed Aissaoui
Directeur Général Adjoint
Rabat

Mr. Mohamed Jafari
Adjoint au Chef du Département de Crédits Spécialisés et de la Promotion
Rabat

ix. **Bourse des Valeurs de Casablanca (BVC)**

Mr. Abderrazak Laraki
Directeur Général
Casablanca

x. **Caisse de Dépôt et de Gestion (CDG)**

Mr. Ahmed Darouich
Directeur des Etudes et de la Formation
Rabat

Mrs. Samira Dassouli
Directeur Adjoint
Adjoint du Directeur Financier
Rabat

Mr. Youssef Iraqui Houssaini
Directeur Financier
Rabat

xi. **Casablanca Finance Group (CFG)**

Mr. Amyn Alami
Administrateur Délégué
Casablanca

Mr. Adil Douiri
Administrateur Délégué

Casablanca

xii. **Crédit du Maroc (CM)**

Mr. Mustapha Moussaoui
Directeur de l'Exploitation
Casablanca

xiii. **Groupement pour l'Investissement et le Développement**

Mr. Noredine Rabhi
Secrétaire Général
Rabat

xiv. **International Finance Corporation (IFC)**

Mr. Pierre Sala
Représentant Régional pour l'Afrique du Nord
Casablanca

Mr. Younès Marrakchi
Investment Officer
Casablanca

Mrs. Yasmin Saadat
Regional Economist
Central Asia, Middle East and North Africa
Washington, D.C.,

xv. **Moussahama, S.A.-S.P.P.P.**

Mr. Jalal Alaoui,
Directeur
Casablanca

Mr. Sâad Bendidi,
Directeur General
Casablanca

xvi. **Société Générale Marocaine de Banques (SGMB)**

Mr. Abdennaji Eddahar
Sous-Directeur Adjoint
Département des Titres
Casablanca

Mr. Abderrahim Rhiati Salih
Secrétaire du Conseil
Chargé des Filiales et Participations
Casablanca

xvii. **Société Nationale d'Investissement (SNI)**

Mr. Abdelhai Bouchareb
Chargé de mission
Casablanca

Mr. Abdelkrim Lahlou
Directeur Général Adjoint
Casablanca

xviii. **The World Bank**

Mr. Charles P. Humphreys
Principal Economist
Maghreb Department
Middle East and North Africa Region
Washington, D.C.,

Mr. Ali M. Khadr
Senior Country Economist for Morocco
Maghreb Department
Middle East and North Africa Region
Washington, D.C.,

xix. **WAFABANK**

Mr. Hassan Bousbaa
Division Marketing des Particuliers
Casablanca

Mr. Abdelhak Erakhmi,
Chef du Département, Gestion de Fonds
Casablanca

Mr. Ahmed Harti
Chef du Département des Titres
Casablanca

Mr. Mustapha Nafakh Lazraq
Directeur du Groupe
Marché des Particuliers et des Professionnels
Casablanca

B. Government of Morocco Ministries

i. Ministère de l'Intérieur (MoI)

Dr. Chemao El Fihri
Mohammed El Mountassir
Administrateur
Rabat

ii. Ministère des Finances (MoF)

Mr. Youssef Allal Albakhti
Chef de la Division des Banques et du marché des capitaux
Direction du Trésor et des finances extérieures
Rabat

Mr. Barki
Chef de Service
Division du Trésor et des Marchés
Rabat

Mr. Aissa El Mauiaui
Attaché de Direction
Office des Changes
Rabat

Mr. Abdeljalil Faddili
Direction des Etablissements Publics et Privatisations
Rabat

Mr. Abdellatif Faouzi
Sous Directeur
Direction du Trésor
Rabat

Mr. Rachid Haboub
Head of the Capital Market Sub-Division
Treasury Department
Rabat

Mr. Abdelouahed Kabbaj
Adjoint du Directeur
Direction des Etablissements Publics et de Participations

Rabat

Mr. Abdallah Khial
Chef de la Division des Etudes Juridiques et Techniques
Direction des Assurances et de la Prévoyance Sociale
Rabat

Mr. Mohamed Kourti
Chef de Service de la Dette Interieure
Direction du Trésor
Rabat

Mrs. Zoulikha Nasri
Adjoint du Directeur
Direction des Assurances et de la Prévoyance Sociale
Rabat

Mr. Ouassini Ramdane
Directeur
Direction des Etablissements Publics et de Participations
Rabat

Mr. Thami Yahyaoui
Inspecteur des Finances
Chef de Division
Rabat

iii. **Ministère du Commerce, de l'Industrie et de la Privatisation**

Mr. Hassan Amrani
Directeur de la Privatisation
Chargé de Mission auprès du Premier Ministre
Département de la Privatisation
Rabat

Mr. Abdesselam El Ftouh
Détaché auprès du département de la Privatisation
Rabat

Mr. Olivier Fremond
Price Waterhouse
Détaché auprès du département de la Privatisation
Rabat

Mr. Alfred Saulniers
Price Waterhouse
Détaché auprès du département de la Privatisation
Rabat

C. **Other Interviews**

i. **Mr. Omar Azziman**

Docteur en Droit
Avocat Conseil (Agréé près la Cour Suprême)
Rabat

ii. **Cabinet Royal**

Mr. Hicham Senoussi
Chargé de Mission
Rabat

iii. **Confédération Générale Economique Marocaine**

Mr. Abderrahmane Bennani-Smires
Président
Casablanca

iv. **Conseiller Royal**

Mr. André Azoulay
Rabat

iv. **Dibrina S.A.**

Mr. Mustapha Chegdali
Directeur Financier
Casablanca

v. **Embassy of Morocco**

Mr. Rachid Aguassim
First Secretary
Washington, D.C.,

vi. **Filatis**

Mr. Bentaibi Monsef
Diplômé Expert Comptable
Directeur Financier
Casablanca

vii. **Groupe LMS Conseil/LMS Marketing**

Ms. Oumnia Benjellun
Consultante
Casablanca

Mr. Abdenbi Louitri
Administrateur Délégué
Consultant en Marketing
Casablanca

viii. **Grupo Tavex/Settavex, S.A.**

Mr. Abdelmajid Ben Sassi
Responsable Service Risques
Settat

ix. **Groupement Professionnel des Banques du Maroc**

Mr. El Hadi Chaibainou
Délégué Général Adjoint
Casablanca

x. **Inter American Management Consulting Group (IMCC)**

Mr. Alain de Maynadier
Principal Conseiller Financier
Casablanca

xi. **Radio Télévision Marocaine (RTM)**

Mr. Mohamed Boudkhili
Rabat

Mr. A. Moufakir
Rabat

xii. **Shem's Publicité**

Mr. Noureddine Ayouch
Président
Casablanca

xiii. **United States Agency for International Development (USAID)**

Mr. Abderrahim Bouazza
Economiste
Division des Programmes
Rabat

Mr. Martin Dagata
Mission Director
Rabat

Mr. T. Mark Kraczkiewicz
Economiste
Rabat

Ms. Susan Riley
Project Officer
Rabat

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