I. Project Context

Country Context

Morocco’s economy has been growing steadily for over a decade due to sound macroeconomic management and sustained development in non-agricultural sectors. The country’s economy proved relatively resilient vis-à-vis the recent global economic slowdown. However, sluggish external demand, high prices of imported commodities, and lower agricultural output, combined with significant domestic economic rigidities have exposed the fragility of the Moroccan economy. In 2012, the GDP grew at a modest 2.7% compared to 5% of the previous year. Morocco has embarked on a path of political and economic reforms to respond to increasing social demands. The reforms focus on strengthening governance and justice, consolidating public finance, reducing energy subsidies and deepening decentralization to improve the economy’s competitiveness and create jobs.

The wave of political change engulfing the MENA region since 2011 also enveloped Morocco. Transparent elections held in November 2011 were won by the Parti de la Justice et du Développement (PJD), an Islamist party that had traditionally been in active opposition and has
seen its support increasing steadily in recent years. In July 2013, the Party of the Istiqlal - the junior partner in the governing coalition - withdrew its support to the Government citing divergences in economic policy. Five of the six Istiqlal Members of Government resigned, among which the Minister of Economy and Finance and the Minister of Energy, Mining, Water and Environment. The PJD is discussing the formation of a new government with the National Independent Rally (RNI), previously in the opposition.

**Sectoral and institutional Context**

Morocco’s power sector includes public and private operators. The principal public actor remains the ONEE: it is the single buyer in the sector, manages the transmission system, produces around 40% of the electricity, and distributes almost 60% of the electricity. The production sector has a number of independent power producers (IPPs) that produce more than 40% of the electricity and hold power purchase agreements (PPAs) with ONEE. Some concessions exist in important cities for the distribution sector, which also comprises some geographically limited public distribution utilities (Rabat, Casablanca, Tanger, Tetouan).

Electricity demand in 2011 grew at more than 8%, twice as fast as GDP growth. Demand forecasts point to a doubled electricity demand by the year 2020 (with respect to 2011), and tripled by 2030. The installed capacity in 2011 was of 6,377 MW, and ONEE had 4.5 million clients. While 20% of the electricity is imported (mainly through the interconnection with Spain and Algeria to a lesser extent), Morocco is highly energy dependent on foreign countries. Aside from hydro resources, 90% of electricity production in Morocco today comes from fossil fuels (coal, diesel, and gaz). Morocco is hence very much dependent on fuel imports and, therefore, exposed to fuel price volatility. However, ambitious plans are being implemented in the wind and solar sectors, aiming at reaching a 42% of renewable energies production by the year 2020.

Under the 2011-2016 investment plan, an increase of 5,480 MW of capacity is envisaged (an increase of 86% with respect to 2010), complemented by 5,000 km of new transmission lines to reinforce the network and expand to un-served areas (3,000 of 225 kV and 2,000 of 400 kV). These investments are to be financed by ONEE as well as by private actors.

Law 13/09 was recently approved to open up the production of electricity from renewable energy sources by guaranteeing access to the transmission network. Therefore, a partially opened market for renewables coexists with a single buyer market without competition. However, this law does not address some key issues such as a guaranteed buy-in tariff or the access to the low voltage grid. Some of these deficiencies could be addressed by the establishment of a regulator.

The financial situation of the electricity branch of ONEE remains fragile. In 2011, ONEE had a turnover of 22 billion Moroccan Dirhams (MAD). However, during the same year, it produced a deficit of 3.6 billion MAD, making it the Moroccan state-owned enterprise with the most worrisome financial situation. Aside from the increase in demand, this is due to the fact that tariffs are at 60% of cost-recovery levels and not often modified, that the running costs have increased given the increase in fossil fuel prices during the last years, and that ONEE’s debt level is going towards an unsustainable path.

The Government and ONEE are currently negotiating a framework agreement to help ONEE redress its financial position and progress towards more solid financial ground. The agreement has
not been finalized yet but the following elements have been discussed: improvement of operational performances (improvement of technical and commercial indicators), tariff adjustments (except for social tariffs), state recapitalization, recovery of debts from public entities, fiscal benefits (import tax exoneration for electricity projects, harmonization of V.A.T. on fuels, etc.) and provision of state guarantees for projects undertaken by the utility. In return, the utility’s line ministry firmly requests an improvement on the energy efficiency front, so as to be able to control the country’s electricity demand growth. The Government provided an advance payment of 1 billion MAD (equivalent to US$ 120 million) to ONEE late 2012 as an advance transfer of this framework agreement.

A central recent change in the sector has been Law 40/09 on the fusion of the electricity and water utilities to create ONEE, which has been effective since April 2012, and aims at improving the management of both utilities and increasing the cross-sector synergies.

II. Proposed Development Objectives
   A. Current Project Development Objectives – Parent
   The objective of the Project is to increase the efficiency and reliability of electricity supply. This objective will be achieved through:

   - Strengthening of the transmission and distribution infrastructure and supporting reductions in overall technical losses;
   - Support to DSM programs to reduce electricity demand growth;
   - Promotion of wind generation;
   - Assistance to ONE to adjust to a new market environment.

   B. Proposed Project Development Objectives – Additional Financing (AF)

III. Project Description
   Component Name
   Electricity Transmission and Distribution Network in the Project Area
   Comments (optional)
   Includes same transmission lines and substations as original project, except that Dar Bouazza substation was dropped in restructuring in second half 2013.

   Component Name
   Compact Fluorescent Lamps
   Comments (optional)
   Same as in original project. More than 4.8 million CFL have been deployed.

   Component Name
   Technical Assistance
   Comments (optional)
   Same activities as original project, except that activity "Upgrade of Procurement Function" was dropped in restructuring in second half 2013.

IV. Financing (in USD Million)
V. Implementation
The implementation arrangements of the parent project will remain unchanged to implement this additional financing. The Borrower's implementation unit institutional and organizational settings for the supervision and implementation of the project's environmental and social safeguards, procurement, financial management and all remaining fiduciary aspects will not be affected by the merger between ONE and ONEP, i.e. the capacity of the newly created ONEE to follow applicable World Bank guidelines will remain unchanged.

VI. Safeguard Policies (including public consultation)

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<th>Safeguard Policies Triggered by the Project</th>
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<td>Environmental Assessment OP/BP 4.01</td>
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Comments (optional)

VII. Contact point

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