

Evolution of participatory finance in Morocco : What effect on economic growth?

Evolution de la finance participative au Maroc : Quel effet sur la croissance économique ?

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Abstract

During the second half of the century, investments were directed towards activities that promoted economic growth while preserving social harmony. The financial crises that took place at the beginning of the nineteenth century demonstrated that the current financial system can be reconsidered. This questioning of the conventional system has led some operators and researchers to take an interest in Islamic finance. This form of financial participation is called participatory finance, it is a project that involves banks, insurance companies and the capital market. Bringing real opportunities for the growth of savings and investment, this project deserves a collaborative approach between institutions and other actors that would contribute to economic and social development and thus support the development of Morocco's strategies. The aim of this article is to study the impact of the evolution of participatory finance on economic growth in Morocco.

Keywords : Participatory finance ; Financial crisis ; Investment ; Economic growth; development.

Résumé

Au cours de la seconde moitié du siècle, les investissements ont été orientés vers des activités favorisant la croissance économique tout en préservant l'harmonie sociale. Les crises financières qui ont eu lieu au début du XIXe siècle ont démontré que le système financier en vigueur peut être reconsidéré. Cette remise en cause du système conventionnel a conduit certains opérateurs et chercheurs à s'intéresser à la finance islamique. Cette forme de participation financière est appelée finance participative, il s'agit d'un projet qui implique les banques, les compagnies d'assurances et le marché des capitaux. Porteur de véritables opportunités de croissance de l'épargne et de l'investissement, ce projet mérite une approche collaborative entre les institutions et les autres acteurs qui contribueraient au développement économique et social et accompagneraient ainsi l'élaboration des stratégies du Maroc.

L'objectif de cet article est d'étudier l'impact de l'évolution de la finance participative sur la croissance économique au Maroc.

Mots clés : Finance participative ; crises financières ; Investissement ; Croissance économique ; développement.

Introduction

Morocco has seen steady growth in its local market since the introduction of sharia-compliant financial services in 2017. The players have significantly evolved and now have a wide range of offerings such as different banking products and Islamic bonds (sukuk) plus Islamic insurance (takaful). Islamic banks, takaful companies, the regulator and other stakeholders are working closely on finalizing the entire Islamic financial services setup and enhancing their capabilities.

The field of offering sharia-compliant products was a late entrant in Morocco. Unlike Egypt, which had introduced such products in the early 1960, it wasn't until 2011 that Moroccan officials started talking about Islamic banking. Known widely as participatory banking in Morocco. In 2015, a law described by many analysts as landmark legislation came into being not only giving an outline structure to the segment but also setting up a board within the Supreme Council of Islamic Scholars to oversee compliance of financial products and services with sharia law. The approval for the first five participatory banks was granted by Bank Al Maghrib (BAM), Morocco's central bank in January 2017. Subsequent laws were passed in 2018 and 2019: one regarding solvency and another regarding liquidity. Without which the entire system would go haywire with instability since these are the cardinal controls over stability that underpins all else within such a dynamic sector.¹

The Islamic finance landscape of Morocco is still under development. Currently, Islamic banking is facilitated through windows or subsidiaries in conventional banks. A Sharia Committee for Finance was set up by the High Council of Ulemas in 2015 to oversee the compliance of sharia products offered by Islamic finance entities from 2022 onwards, an external sharia audit was mandated on Islamic banks by the central bank. In 2022, the government broadened the scope of sukuk to be issued including murabaha, salam, istisna, wakala, mudaraba and musharaka; ijara sukuk were previously only allowed. The regulatory framework for takaful was finalized in 2021.

Liquidity challenges are faced by Islamic banks. The financing-to-deposit ratio of the sector stood at 238% at the end of 2022 while that for conventional banks was 93%. Deposit mobilization in Islamic banks is curtailed by keen competition for deposits as well as a large portion of unremunerated accounts (71% of total sector deposits at end 2022), which does not

¹ Rapport du Fonds monétaire internationale (FMI), 2019

attract customers' interest to place funds with Islamic banks, even though there is notable credit demand for Islamic financing, particularly on the retail side. The central bank unveiled in 2020 the Wakala Bil Istithmar deposit product, which allows Islamic banks to draw liquidity from conventional banks, even their conventional parents and other entities like public sector entities or corporates. The deposits are costlier but more needed as an additional source of liquidity. Customers also offer investment deposits to customers but these are not guaranteed under the deposit insurance fund of participatory banks. This might affect consumer demand for such products.²

Our contribution aims to answer the following main question : To what extent does the evolution of participatory finance influence economic growth in Morocco?

1. Litterature review : Economic growth , Participatory finance

1.1 Economic growth

At its core, economic growth can be defined as an expansion of total output produced within an economy. This typically results in a boost to the national income. GDP is the total value of goods and services produced by a country in a certain period of time. Historically, GDP has been recognized as the primary indicator of a nation's economic growth since it takes into consideration the whole economic value produced by the country— goods and services sold both within and outside the nation's borders. While higher production does often lead to increased average marginal productivity (even though it's not a strict rule), and consequently more income, which in turn motivates consumers through what they earn and leads them to spend on more purchases , there is also the aspect of improving quality of life. As people tend to use the additional income to enhance their material well-being and overall living standards. The concept of economic growth can be described as an expansion of total output produced in an economy. It typically shows up as a growth in national income. Although not always, often times aggregate production gains are paralleled by increase average marginal productivity and this leads to higher levels of income. In turn, higher income levels act as incentives for consumers to spend more out of their disposable income which raises the demand even further. This results in a better-quality material life and higher standard living for the people within the economy.³the only way to achieve economic growth is for either the labor or capital to increase with the technology level to stave off decreasing returns of growth driven by an

² Fitch Ratings, "Morocco's Islamic Finance Industry Is Nascent; Faces Key Challenges"

³ [What Is Economic Growth and How Is It Measured? \(investopedia.com\)](https://www.investopedia.com/what-is-economic-growth-and-how-is-it-measured/)

increase in the capital stock or the labor force (Snowdon & Vane 2005). Economic growth was solely influenced by investment, determined by savings. An increase in saving leads to a decrease the interest rate, thereby increasing investment to balance out the reduction in consumption due to higher levels of savings. However, a decrease in savings will increase the interest rate and depress investment, and hence depress economic growth (Baumol 1999).

1.2 Participatory finance

The term “finance” is derived from the Latin word *finis* which means “the term”. In French from 3rd century, the verb *finer* first means “to finish a transaction and therefore pay”. In the 18th century, at the time of the emergence of the Classical School, finance became a sub-discipline of economics (Larousse Etymological Dictionary, 1971). According to Dembinski, finance is an economic subsystem that performs three functions specific: guarantee the circulation of financial transactions, collect savings and put them at the service of investment projects, and assess the risk so that it is profitable (Dembinski, Paul H. and Morais, Natasha, 2001).

In the 18th century, with the rise of the classical school, finance became a branch of economics. Islamic finance presents itself as a branch of finance, aiming to establish an economic and financial order consistent with Islam. The founder and main theorist of Islamic economics is the Pakistani theologian Sayyid Abul Ala Maududi, who in his main contribution *The Economic Problem of Man and Its Islamic Solution*, indicates that Islamic finance would form a third way between capitalism and communism which would aim to establish a fairer economic order (Taki, 2015). According to the Director of the Banque de France Christian Noyer, Islamic finance is also “an interesting alternative finance” (Fredj Jawadi, 2012)⁴. The ultimate goal is to provide stability and strength in harsher environments. Several economists have supported the idea of the efficiency of Islamic banks compared to conventional banks as demonstrated by Hassan and Bashir (2003) Sarker (1999), Bashir (1999) Yudistira (2004) and Hassen (2004) (Said Jaouadi, 2014).

For Bank Al Maghrib, participatory finance is an issue of stability and regulation. Certainly, the BAM has the duty to manage the particularities of this finance so as not to dismantle the conventional banking sector.

⁴ Fredj Jawadi, « La finance islamique est-elle à l'abri de la crise financière globalisée ? »

For the treasury, this finance represents a financing challenge to the extent that it can find in Sukuks a choice to diversify its sources of financing, but also a appropriate means to meet its liquidity needs.

For the financial market, the challenge will be to improve the attractiveness of the Casablanca market by increasing its level of liquidity (Adil Cherkaoui, 2016).

The development of Islamic finance in Morocco should make it possible to increase the banking rate by attracting new clients who are currently prohibited, for religious reasons, from placing their savings in conventional banks. Since 2008, the occurrence of the subprime crisis and that of sovereign debts have weakened the financial system to the point of creating an economic crisis. We have gradually moved towards a more responsible, more equitable world of finance. It was notable during the crisis that Islamic financial institutions were relatively more stable than conventional institutions.

Since 2008, the subprime crisis and the sovereign debt crisis have weakened the financial system and caused an economic crisis. Indeed, since the creation of money, humans have designed a financial system disconnected from the realities of the world by creating mechanisms such as refinancing vehicles. The subprime mortgage crisis first hit the U.S. housing market in August 2007. The interest rate depends on the value of the home (the more the home appreciates, the lower the interest rate because the risk is lower) and the market rate. However, as interest rates increased, stone prices in the United States began to decline. Households find themselves unable to pay their debts, and credit institutions find themselves facing a liquidity crisis, causing losses for the banks that bet on them. The subprime mortgage crisis has led to a serious cash drain. On September 15, 2008, the bankruptcy of the major American investment bank Lehman Brothers caused great panic on the financial markets⁵. The banking system almost completely collapsed and subsequently triggered a major global financial crisis (2008-2009). It has rapidly spread to most international financial and monetary systems, including developed and emerging countries. Among other things, the crisis showed the failure of traditional banks, control systems, ineffective risk management and the dangers of traditional finance, which is intrinsically attached to capitalism and market economies.

⁵ Arnaud BALVAY, « CRISE DES SUBPRIMES, en bref », *Encyclopædia Universalis* [en ligne], consulté le 24 Juillet 2024. URL : <https://www.universalis.fr/encyclopedie/crise-des-subprimes-en-bref/>

1.3 “Participatory finance, a tool for inclusion and a lever for development”

Within the last half-century, the world economy grew by a factor of six and average per capita income nearly tripled— never-before-seen achievements driven by rapid population growth (that increased the number of workers) and healthy gains in labor productivity. But in the future, as this vast economic expansion will soon decrease sharply if productivity is not enhanced, because the population growth rate is falling and as a result labor force participation relative to total population is declining too. If there are less overall workers that can contribute to their economy, each worker's productivity must then increase for GDP growth to keep up.

Gauging economic expansion can be tricky. It is relatively simple to count tangible goods like the amount of TVs produced within a nation. However, matters tend to get complicated once we delve into services or non-physical products such as IP or research outcomes. Yet economists traditionally rely on GDP, a figure meant to summarize the total value of all goods and services produced in a country during a year, to indicate whether an economy is growing or declining. But this, as we will discover later, is not really an appropriate index metric that fully describes an economy's state.⁶

In recent years, economists have developed new endogenous economic growth models that take into account the effects of policies on growth and how outcomes vary across countries.

These models address topics such as growth, how financial markets work, trade policy, government spending, and taxation.

Recent empirical studies on the link between Islamic finance and economic growth are limited and more focused on a single country. Furqani & Mulyany (2009), study the causality between Islamic financial development and economic growth in Malaysia using a VECM model on quarterly data for the period 1997-2005. The authors use as an indicator to measure the Islamic financial system, namely the total Islamic financing⁷. Their results show that in the long run, total Islamic financing is positive and significantly correlated with economic growth and capital accumulation in Malaysia. They also show that the direction of causality between financial development and economic growth is in favor of the unidirectional hypothesis and follows the reference (demand following approach), which means that economic growth encourages

⁶ Bashir, A.-H. M. (1999). Monetary Policy and Economic Growth: An Islamic Perspective. Proceedings of the Third Harvard University Forum on Islamic Finance. Centre for Middle Eastern Studies, Harvard University, pp. 13–22.

⁷ Le totale de financement Islamique est égale à la somme des opérations suivantes : *Qard Hasan, Mourabahah, Ijarah, Moudarabah, Moucharakah, Salam, Istisna*

Islamic banking institutions to evolve and grow. Majid & Kassim (2010), empirically examine the relationship between Islamic finance and economic growth in Malaysia. The authors also show that the direction of causality runs from Islamic financial development towards economic growth by referring to Patrick's (1966) framework (supply-leading approach). Abduh & Omar (2012) develop a cointegration analysis on quarterly data for the period 2003-2010 to study the relationship between Islamic financial development and economic growth in Indonesia. The results of the ARDL model used by the authors highlight that the direction of causality between Islamic development and economic growth in Indonesia is bidirectional, meaning that on the one hand, economic growth encourages Islamic banks to develop. and on the other hand that the development of the Islamic financial system stimulates economic growth in Indonesia. In a more recent article, Yazdan Gudarzi Farahani, Masood Dastan, (2013) use three econometric methods namely ARDL (Auto Regressive Distributed lag), VAR (Vector Autoregressive Model), to study the relationship between Islamic financial development and economic growth on a sample of eight countries (Bahrain, UAE, Saudi Arabia, Kuwait, Qatar, Yemen Malaysia, Indonesia, and Egypt) over the period 2000-2010. The results show that Islamic financial development (measured by total Islamic financing as a proportion of GDP) positively affects long-term economic growth.

On the basis of a sample composed of 15 countries, observed over five successive quadrennial periods⁵⁵ from 1990 to 2009, Rym & al (2013) examine the long-term relationship between Islamic financial development and Economic Growth. Liquid liabilities of Islamic banks, total Islamic financing, and the volume of overall banking activity translated by retail activity and wholesale activity are used to measure the development of the Islamic financial sector. The econometric results from the generalized method of moments (GMM) show that the indicator of the depth of Islamic finance measured by the liquid liabilities of Islamic banks as a proportion of GDP has a negative effect on economic growth, but this effect remains weak.

2. Impact of participatory finance on economic growth in Morocco

Presently, the participative finance landscape in Morocco comprises five banks and three participative windows, making a total of eight banking institutions. two banks established participative windows in the first half of 2017 and four other banking institutions followed suit in the second half of 2017. At present, there are eight banking

⁸ ARDL (autoregressive distributed lag approach) est un modèle autorégressif à retards échelonnés

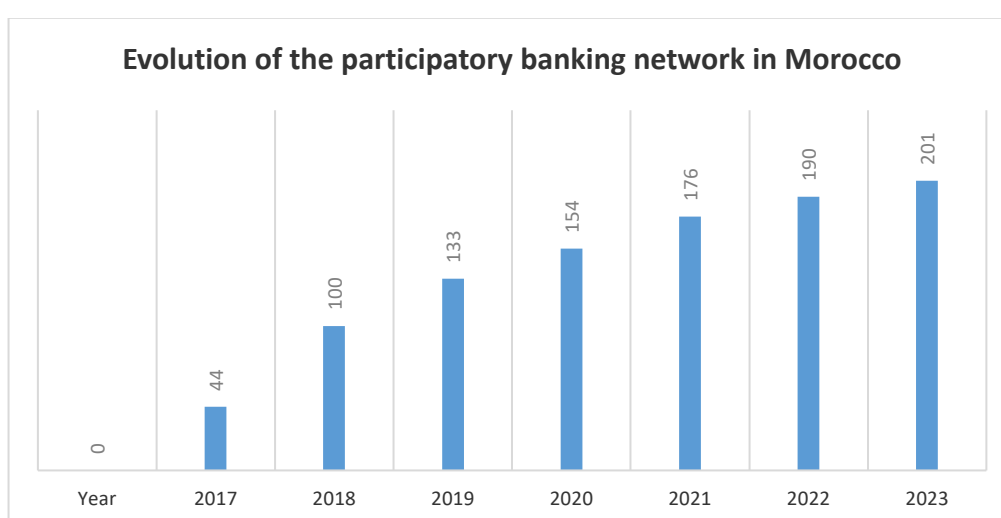
institutions in the participative banking sphere in Morocco, comprising five banks and three participative windows.

Based on research carried out by the Islamic Finance Advisory and Assurance Services (IFAAS), the introduction of participative banks was highly awaited by most of the Moroccan population, where about 79% of those interviewed expressed keen interest in participative banking services upon launch (IFAAS, 2014).

2.1 A documentary statistical research

2.1.1 Evolution of the participatory banking network in Morocco

Figure N°1 : Evolution of the participatory banking network



Source : Autors

According to Bank AlMaghrib's annual reports, it has been noted that the young ecosystem of participatory finance has seen its network of agencies continue to multiply and grow rapidly, with a creation of 44 agencies at the end of 2017, increasing to 100 in 2018 by the opening of 56 new branches, then to 133 in 2019 with an increase by 33 new branches banks opened by participatory banks. In 2020, the participatory banking network reached 154, an increase of 21 agencies. Similarly in 2021, the number of branches increased to 176, an annual variation of 10.4%, then to 190 in 2022, to reach 201 at the end of December 2023. This indicates that the banking network of participatory banks continues to grow regularly. This constant growth reflects a strategic expansion with a regular opening of new branches that reflects a desire to reach a wider audience and to strengthen the presence in the market. On the one hand, the resilience demonstrated in difficult economic times suggests that the sector is adaptable, and on the other hand, the stable year-on-year variations suggest a gradual maturation, and the continuation of this growth indicates continued confidence in the market potential. This shows that there is real potential that is now being exploited by the banks.

2.1.2 Participatory banking does not know the crisis

Figure N°2 : Evolution of the participatory banking



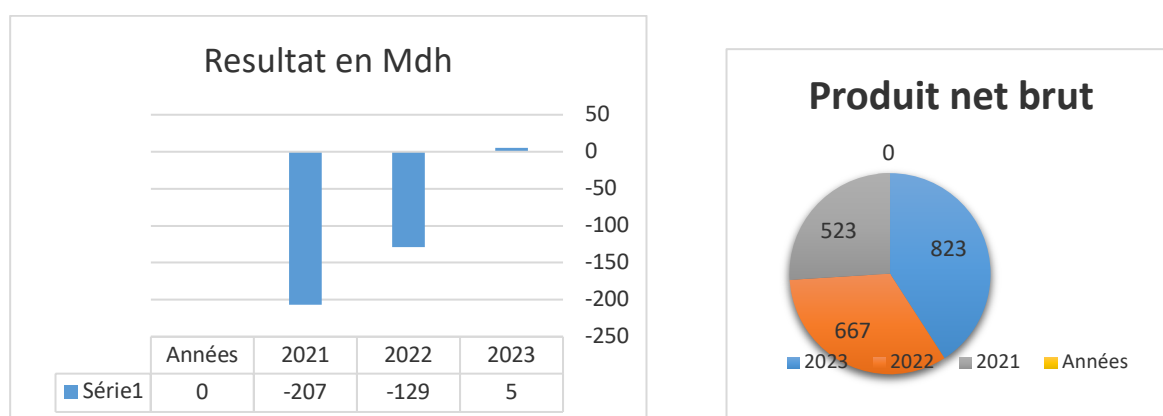
Source : report of Bank Almaghrib

The report from Bank Al Maghrib indicates a significant increase of 20.9% in the cumulative balance sheet of both banks and participatory windows, amounting to 32.7 billion. This growth is attributed to an active crowdfunding environment, bolstered by sight deposits, investment deposits, "wakala bil istithmar," and equity.

Sight deposits have reached 9.1 billion, and investment deposits have hit 3 billion, bringing the total deposits to 12.1 billion, up from 9.5 billion in 2022, an increase of 28.1%.

Crowdfunding totalled 21.3 billion in 2023, up from 17.4 billion recorded in 2022. This increase is mainly attributable to real estate financing, which accounts for 80.4% of the total.

Figure N°3 : Results and Net banking income



Source : Autors

In terms of profitability, the sector has posted significant results. Net banking income (NBI) reached 823 million, compared to 667 million in 2022, and 523 million in 2021.

In addition, the net result rose to 5 million, contrasting with the negative results of -129 million in 2022 and -207 million in 2021.

2.2 Promising future prospects

Product diversification and resource valorization cannot depend solely on Murabaha if they must be reinforced by participatory finance in Morocco, according to sector experts. They encourage banks that practice participatory finance to invest in other segments while inviting them not to depend solely on it, and to diversify their products in order to meet the needs of their customers (mainly businesses and individuals at the search for savings and investment solutions). Participatory banks also face another significant resource challenge: they are unable to generate enough deposits to finance their growth. When opting for more expensive financing like Wakala Bil Istithmar, participatory banks end up compromising their profitability, hence the need to establish a solid deposit base that can ensure their sustainability. "The first weakness concerns the level of current account deposits, because it has not kept pace with financing, especially in the first years, but today things are already better because the growth rate of deposits is very good and very high especially since we created investment deposits", explains Abderrahmane Lahlou, president of the Academy of Participatory Finance.

Morocco's Islamic finance industry is still in its infancy and faces structural challenges that could limit its full growth potential. However, the increasing popularity of Islamic mortgage financing may serve as a significant growth source and may influence the industry's course of development⁹. The difficulties associated with the industry are underdeveloped Islamic financial ecosystems and regulations, a limited amount of Islamic merchandise, a small base of Islamic banks, the lack of public knowledge and comprehension of Islamic finances, and the lack of faith in the Islamic official's commitment to Sharia compliance.

Banks still find it difficult to quickly adapt their operating models. As well as participative banks have managed to make their place in the Moroccan market, and are now seeking to diversify their products based on new technologies. It should be mentioned that the emergence of crowdfunding in Morocco is part of a broader global trend. In a Thomson Reuters report, it is indicated that the global Islamic finance market will reach \$3.8 trillion in 2026. Morocco has built its own model, and has specificities that other countries do not have from a structural and organizational point of view: after having set up participatory banks, Sukuks and takaful insurance. The Moroccan model has started.

⁹ Elimane Sembène, " Les défis qui attendent la finance participative au Maroc, selon Fitch Ratings", [Les défis qui attendent la finance participative au Maroc, selon Fitch Ratings | le360.ma](https://www.le360.ma)

Conclusion

The long-term growth potential of the Islamic finance industry in Morocco is significant, as the country is majority Muslim. Islamic finance may also contribute to the expansion of financial inclusion in Morocco, around 56 percent of the country's adult population lacked a bank account in 2021, according to the World Bank, around 19 percent of the unbanked population cited religious reasons as a barrier (among the highest globally). The sector has significant economic and social potential for development at the national level, and participatory banks can help promote financial dynamics in the Moroccan banking sector, due to the estimated value of more than \$500 billion in financing global participatory.

Recognizing the undeniable potential of participatory finance to promote financial inclusion, economic development and ensure the stability of the national financial system, Morocco has adopted a proactive posture. Indeed, in recent years, Morocco has launched some initiatives aimed at promoting participatory finance: establishing an environment favorable to its development and wealth through solid support and making it a major pillar of the diversification of the financial landscape.

Morocco's initiatives to promote participatory finance represent a proactive approach to creating a more inclusive and diversified financial landscape. Through regulatory support, public awareness campaigns, investment attraction, and collaboration with various stakeholders, Morocco is laying the groundwork for a thriving participatory finance ecosystem that can drive economic growth and improve the overall well-being of its citizens. Future research should consider these aspects to better understand the factors that influence the success or failure of participatory finance projects.

Overall, the research provides valuable insights into the potential of participatory finance to drive Morocco's economic development, emphasizing the importance of an integrated approach involving all stakeholders. Future studies could explore the impact on employment, wealth creation, and poverty reduction, as well as compare Morocco's experience with other emerging countries to better understand the long-term benefits of participatory finance.

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