Jordan

Second Equitable Growth and Job Creation Development Policy Financing (Loan No. 8982-JO)

Release of the Second Tranche

Tranche Release Document

I. Background

1. **The World Bank approved a programmatic series of two development policy loans in June 2018 and June 2019, respectively.** The program development objective of the series is to support Jordan to set foundations to: (i) reduce business costs and improve market accessibility; (ii) create more flexible and integrated labor markets and provide better and more efficient social assistance; and (iii) improve fiscal sustainability and take more informed decisions regarding risk. The Equitable Growth and Job Creation Development Policy Financing (DPF1) was approved by the Board on June 27, 2018, in the amount of $500 million, including a contribution of $111 million from the Global Concessional Finance Facility (GCFF), and has been fully disbursed. The Second Equitable Growth and Job Creation Development Policy Financing (DPF2) was approved by the Board on June 4, 2019, in the amount of $1.45 billion. Of the total DPF2 amount, $250 million is guaranteed by the United Kingdom and $200 million is guaranteed by the Kingdom of Saudi Arabia**.** DPF2 consists of two equal tranches, with the first tranche of $725 million disbursed on June 6, 2019. DPF2 supported the reform agenda initiated under DPF1, as well as reforms to boost growth (such as FDI liberalization, procurement reform) and to strengthen the financial sustainability of the electricity sector (Roadmap for Financial Sustainability of the Electricity Sector).

2. To provide a comprehensive response to the COVID-19 pandemic, the Government of Jordan and the World Bank have agreed to reduce the amount of the DPF2 second tranche from $725 million to $225 million and redirect the remaining resources towards other priorities in light of the COVID-19 shock.

II. Recent economic developments and macroeconomic outlook

3 **Jordan ended 2019 with mixed results in its macroeconomic indicators; while growth remained relatively resilient, public debt increased.** Jordan's economy achieved 2 percent growth in 2019, slightly lower than the 2.2 percent anticipated owing in part to lower investment. Importantly, while the economy proved resilient in 2019 (annual GDP growth has averaged 2 percent since 2016), the growth rate was not sufficient to improve debt dynamics or to create the large number of jobs needed for the growing population. These dynamics, coupled with weak tax collection and significant below-the-line spending, resulted in an expansionary fiscal policy and a surge in public debt. As a result, Jordan's overall fiscal balance (excl. grants) widened to -7.2 percent of GDP and its primary balance (excl. grants) to -3.6 percent of GDP. The public debt-to-GDP ratio rose to 98.9 percent of GDP in 2019, 4.3 percentage points higher than projected under DPF2. At the same time, healthy growth in exports and travel receipts, a reduction in oil prices, and lower imports stemming from the weaker economy, led Jordan's current account to improve to -2.8 percent of GDP at end-2019, better than the -7 percent of GDP originally anticipated.

4. **While the COVID-19 shock is adding severe (and rapidly evolving) stress onto an economy that already had limited buffers, the macroeconomic policy framework is assessed as being (borderline) adequate for the purpose of DPF2, even though downside risks have increased in the current global**

economic context. In 2020, Jordan is expected to experience its worst recession since 1989. Bank staff expects public debt to jump from 98.9 percent of GDP in 2019 to 111.7 percent of GDP in 2020, to peak in 2021 and then return to its 2020 level by 2024. Achieving this economic trajectory requires Jordan to: (1) fully and timely implement the fiscal adjustment agreed in the context of the 2020-23 IMF Extended Fund Facility (EFF) program; (2) fully and timely implement the structural reform program supported by the DPF series and the IMF EFF so that economic growth accelerates; (3) obtain continued sizeable concessional support; and (4) take corrective measures should downside risks materialize. The balance of risks surrounding this baseline macroeconomic framework is tilted to the downside. The commitment to maintain this trajectory is supported by the GOJ-IMF agreement on the new IMF EFF program for 2020-23 ($1.3 billion, approved on March 25, 2020). The IMF also approved emergency financial assistance under the Rapid Financing Instrument (RFI) of about $396 million on May 21, 2020.

III. Program performance

5. **Jordan has made progress on implementing the program on all three pillars, though implementation risks have further increased owing to the COVID-19 shock.** DPF1 and DPF2 comprise a complex program that seeks to support the Government of Jordan to change policies to set new foundations for economic growth and job creation. The overall program includes 24 results indicators (RIs). Staff's assessment is that 17 RIs are on track to be met by the program's closing date. However, 7 RIs, particularly in the energy sector, are at risk of not being achieved by closing date and will require sustained Government commitment for their timely implementation.

- <u>*Pillar 1 - Reduce business costs and improve market accessibility*</u>: Jordan has implemented the Insolvency bylaws, the Inspection bylaws and advanced the Licensing reform agenda. It is implementing the Procurement bylaws, although refinements of the instructions are expected to be issued by end-2020 following the first year of implementation. A challenging and critical area has been FDI regulations: Jordan opened 22 sectors to foreign investment under a DPF2 prior action but reversed the decision pertaining to tour operators and travel agencies in December 2019. On April 1, 2020, Cabinet cancelled the December decision (publication in the Official Gazette took place on June 16, 2020).
- <u>*Pillar 2* - Create more flexible and integrated labor markets and provide better and more efficient social assistance</u>: Jordan has improved targeting of the National Aid Fund and increased the number of beneficiaries that the Fund supports; it has also introduced flexibility in the labor markets, especially regarding part-time work, improved employment opportunities for women, and simplified the acquisition of work permits.
- <u>*Pillar 3 - Improve fiscal sustainability and take more informed decisions regarding risk*</u>:
    - On fiscal and public management issues, the PPP law was approved by the Parliament (Official Gazette publication on April 2, 2020) but, separately, delays occurred in rolling out the public investment management system and revenue mobilization remains tepid.
    - On energy issues, Jordan implemented some of the key aspects of the Roadmap for Financial Sustainability of the Electricity Sector: (i) it turned a National Electricity Power Company (NEPCO) loss of JD 77 million in 2018 into a small surplus in 2019; (ii) it took concrete steps to increase NEPCO's revenues, reduce its costs, and restructure its debts; and (iii) it made progress on increasing energy security by diversifying sources of gas supply and increasing renewable energy capacity. Yet, there are significant implementation risks with regards to NEPCO debt optimization plan to deal with NEPCO's legacy debts and future contingent liabilities arising from significant PPAs. Therefore, further attention is needed to manage the

short and medium-term financial sustainability of NEPCO, stemming from the increasing cost structure, sluggish demand growth and implementation challenges.

IV. The tranche release conditions status update

6. There were seven 2nd Tranche Release Conditions, namely:

- ***Second Tranche Release Condition #1***: *FDI- Retaining and expanding investments: The Council of Ministers approved an investor grievance mechanism that enables the Jordan Investment Commission to identify, track, manage and solve grievances arising between investors and public agencies within specified time periods*.

  The Investor Grievance Management (IGM) Policy was approved by the Council of Ministers (CoM) on October 14, 2019 and the IGM Regulation was approved on October 30, 2019, published in the Official Gazette on November 24, 2019. A subsequent instrument, the IGM Instruction, was approved by the CoM on January 15, 2020. The IGM mechanism became effective on January 23, 2020 and was launched to the public on January 26, 2020.

- ***Second Tranche Release Condition #2****: Targeting: The Borrower's Council of Ministers approved a targeting mechanism for delivering electricity support benefits that will help in providing social protection to the poor.*

  The CoM approved the targeting mechanism on October 10, 2019. The targeting mechanism is based on a combination of social welfare indicators and technical aspects and aims to ensure that electricity support benefits reach the categories eligible for support so that both households and the electrical system benefit alike.

- ***Second Tranche Release Condition #3****: Energy: The CoM has approved the "Roadmap for Financial Sustainability of the Electricity Sector," and Energy and Minerals Regulatory Commission (EMRC) has conducted Quarterly Tariff Reviews at the end of Quarter-2 and Quarter-3 of 2019 consistent with the financial model adopted by the EMRC.*

  CoM approval took place on April 4, 2019; the EMRC's Q2-2019 and Q3-2019 Tariff Reviews were submitted to the CoM and the respective evidence was shared with the World Bank on October 10, 2019.

- ***Second Tranche Release Condition #4****: Energy: The CoM has adopted the "Electricity Bill Recovery Mechanism" to achieve reduction in distribution companies' receivables from electricity bills of the public sector*.

  CoM approval took place on November 4, 2019 (Decision No. 7230). The Bill Recovery Mechanism covers: (i) ministries and governmental departments and institutions; (ii) official bodies subject to the Public Budget Law; (iii) public bodies subject to the Governmental Units Budget Law; (iv) Water Authority and its companies; and (v) municipalities and the Greater Amman Municipality electricity bills.

- ***Second Tranche Release Condition #5****: Energy: The CoM has approved the NEPCO debt optimization implementation plan*.

  CoM approval took place on April 5, 2020 (Decision No. 9196). The Decision specifies seven actions as part of the debt optimization implementation plan.

- ***Second Tranche Release Condition #6**: Energy: Ministry of Energy and Mineral Resources submitted to the Council of Ministers the results of a review of the power purchase agreements and other related agreements for significant power generation projects.*

  Satisfactory evidence has been provided by the Borrower.

- ***Second Tranche Release Condition #7:** Public-Private Partnerships: The Council of Ministers has submitted a revised PPP Law to the Parliament (a) reflecting modifications provided by Cabinet Decision No. 56/10/6/17135 dated April 18, 2019; and (b) reinforcing provisions on government controls of fiscal risks and contingent liabilities as contained in PPP law No. 31 (2014).*

  The CoM approved the draft law and submitted it to Parliament on November 20, 2019; the law was approved by Parliament and published in the Official Gazette on April 2, 2020. The new law eliminates provisions for any exemptions and requires all future Independent Power Producers (IPPs) to: (1) undertake a robust analysis to demonstrate that they are fiscally affordable; and (2) follow a competitive and transparent procurement process.

Overall, Jordan is progressing moderately satisfactorily on the three-pillar program supported by DPF1 and DPF2. There are significant risks to implementing the agreed energy sector reforms. In addition, this Program faces increased implementation risks as the economy is under significant stress and the magnitude of the adjustment required is even larger than it was before COVID-19.

V. Adjusting the loan amount amid the COVID-19 shock

7. **To facilitate a comprehensive response to the COVID-19 pandemic, the Government of Jordan and the World Bank have agreed to reprioritize the existing World Bank loan portfolio and reduce the amount of the DPF2 second tranche from $725 million to $225 million.** As indicated in the recent economic developments section, Jordan is anticipating a challenging remainder of 2020, with potential spillovers into 2021. In order to be able to support the Government's comprehensive response to the challenges posed by the COVID-19 crisis, the Bank is further deploying additional financing to Jordan for both new and ongoing operations, including to support Jordan's emergency cash transfer program to mitigate the social impact of COVID-19 crisis, create economic opportunities for Jordanians and non-Jordanians, and support the education sector reform program underway. The Bank will continue to explore opportunities for providing additional financial resources to Jordan in the coming months.