JORDAN

Highlights

- **A difficult regional environment is constraining Jordan's economic recovery.** Conflict in neighbouring Iraq and Syria is affecting Jordan through disruptions to trade routes, falling tourism receipts, weak investment and large influxes of refugees.
- **Jordan is, however, benefiting significantly from low global oil prices.** This development is positive for both the current and fiscal accounts, given that Jordan imports 96 per cent of its energy needs and the government subsidises the national electricity company.
- **Structural reform progress has been mixed.** Progress has been made in energy reforms, financial sector modernisation and some aspects of the business environment. However, significant obstacles to doing business remain and tax reforms could have been more ambitious.

Key priorities for 2016

- **Further consolidation is needed to put public debt firmly on a downward path.** For the central government, this requires moving on equity-enhancing tax reform as well as strengthening tax administration and public financial management. Enhancing energy sustainability and the continuation of energy sector reforms are also essential. There is a need to diversify energy sources, increase both transmission and distribution capacity, further liberalise fuel distribution markets and promote more energy-efficient production. Furthermore, continued implementation of the authorities' comprehensive tariff reform plans will be required to bring the national electricity company to cost recovery and to reduce mounting arrears.
- **Labour market reform remains a key challenge.** Unemployment, particularly among educated youth, remains structurally high. Refugee inflows are adding to the labour market strain, especially in the informal sector. More extensive efforts are needed to address skills mismatches, reform public sector hiring practices and compensation, and boost female participation.
- **Further improvements to the business environment are needed to unlock higher growth.** Addressing poor access to finance, investor protection and contract enforcement are priorities.

Main macroeconomic indicators %

	2011	2012	2013	2014	2015 proj.
GDP growth	2.6	2.7	2.8	3.1	2.8
Inflation (average)	4.2	4.5	4.8	2.9	-0.6
Government balance/GDP[1]	-5.7	-8.9	-11.1	-10.3	-3.0
Current account balance/GDP	-10.2	-15.2	-10.3	-6.8	-7.4
Net FDI/GDP [neg. sign = inflows]	-5.0	-4.8	-5.2	-4.7	-4.1
External debt/GDP	61.2	61.0	71.1	69.9	n.a.
Gross reserves/GDP	36.6	21.5	35.8	39.3	n.a.
Credit to private sector/GDP	79.2	77.3	76.3	73.0	n.a.

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[1] Central government. Figure includes grants and transfers to national electricity and water companies.

Macroeconomic performance

Deteriorating regional conditions are weighing on growth and straining resources. Growth in 2014 averaged 3.1 per cent – well below average growth rates of around 6 per cent over the last decade – and dropped to 2.0 per cent year-on-year in the first quarter of 2015. The worsening turmoil in neighbouring Syria and Iraq has weighed on goods exports and tourism, while poor weather also led to a contraction in construction activity in the first quarter of the year. The Syrian crisis has led to a huge influx of refugees into Jordan – officially over 600,000 but unofficially likely to be far more – straining public services, government finances and labour markets. Significant falls in the unemployment rate have been elusive, with the latest figure (in the second quarter of 2015) at 11.9 per cent, compared with 12.0 per cent a year earlier.

The fiscal deficit is narrowing thanks to consolidation efforts and lower oil prices. The fiscal deficit (including grants and transfers to state-owned companies) decreased to 10.3 per cent of GDP in 2014, compared with 11.1 per cent in 2013. Fiscal consolidation efforts have been ongoing both by the national electricity company (NEPCO) and at the central government level, with the aim of putting debt on a sustainable path. Lower oil prices have also helped, by reducing NEPCO's operating losses. Gross public debt (including publicly guaranteed debt) has broadly started stabilising this year after reaching 89 per cent of GDP at the end of 2014, and is expected to begin declining next year.

Jordan's external balances are benefiting significantly from lower oil prices, but regional instability is hurting export performance. The deficit narrowed significantly from 10.3 per cent of GDP in 2013 to 6.8 per cent of GDP in 2014. This was driven by a reduction in import spending, aided by lower oil prices (Jordan imports 96 per cent of its energy needs) that more than made up for a fallback in grant receipts as a share of GDP. Lower oil prices will continue to benefit Jordan this year, with energy import spending falling by over 50 per cent on the year in the second quarter of 2015. However, regional instability is having an increasingly pronounced effect on export performance, with both merchandise exports and tourism receipts falling by nearly 19 per cent on the year in the second quarter. The foreign reserve position remains comfortable at over seven months of imports.

Jordan's economic recovery is constrained by a difficult regional environment. Although growth is expected to pick up gradually in 2015 and 2016 and low oil prices will benefit the fiscal and external accounts, risks are skewed to the downside and pertain primarily to heightened regional instability.

Major structural reform developments

The business environment remains difficult, although some progress has recently been made. Jordan ranks 113th out of 189 countries in the World Bank's *Doing Business 2016* report for ease of doing business. Although Jordan performs relatively well in the areas of cross-border trade, paying taxes and getting electricity, the country lags significantly in accessing credit, protecting minority investors and resolving insolvency. Progress has recently been made in addressing obstacles to doing business. A new Investment Law was passed towards the end of 2014 that empowers the Jordan Investment Board to act as a one-stop-shop for foreign and domestic investors (this became operational in April 2015) and streamlines permitting and licensing procedures. However, by-laws dealing with Jordan's numerous restrictions on foreign direct investment (FDI) are still pending. A public-private partnerships (PPP) law was also passed in September 2014 that sets up a PPP unit within the Ministry of Finance to design, evaluate, prioritise and implement projects. In addition, a joint World Bank-OECD project is ongoing to strengthen investment regulations and improve investor protection.

Fiscal reforms – particularly to subsidies – are advancing, but tax measures are lagging. The authorities are pursuing a fiscal consolidation strategy with the aim of reducing public debt to around 70 per cent of GDP over the medium term while also increasing capital spending to meet public investment needs. Subsidy reforms are advancing well. Fuel subsidies have already been eliminated (a step accompanied by a cash transfer scheme to support low-income groups)

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and electricity and water subsidies are gradually being reduced. The national electricity company (NEPCO), which posted losses estimated at 4.5 per cent of GDP in 2014, is getting closer to operational cost recovery. Less progress has been made in deep reforms of the tax system, however. Although a new income tax law was passed in December 2014, its revenue impact was weakened by the introduction of new tax exemptions, of which there is already an excess. Moreover, the personal income tax threshold remains very high, meaning that only 3 per cent of the population pays personal income tax.

Financial sector regulation is being modernised. Amendments to the Central Bank of Jordan (CBJ) Law to expand its mandate to include safeguarding financial stability, in line with international best practice, have been adopted by the cabinet and will now be sent to parliament. The central bank is already in the process of strengthening its macro-prudential framework through, for example, issuing new regulations to limit maturity mismatches; improving information systems for collecting financial soundness indicators and monitoring systemic risk; and expanding its supervision of Jordanian banks' cross-border operations, which account for over 40 per cent of their assets. In addition, amendments to the banking law that strengthen corporate governance and managerial accountability have also been approved.

Some progress is being made in enabling better access to credit. Work on the licensing of a credit bureau, which should help address low financial access by improving information on borrower creditworthiness, is ongoing. The bureau is expected to begin operations in early 2016. There has also been some progress in strengthening the legal framework to encourage lending activities. A new secured lending law has been drafted, although it has not yet been adopted by parliament. The country's first bankruptcy/insolvency law – which increases protection afforded to lenders – has also been drafted but revisions are needed to bring the draft law in line with international best practice.