

**EXECUTIVE
BOARD
MEETING**

EBS/21/117

Correction 1

December 17, 2021

To: Members of the Executive Board

From: The Secretary

Subject: **Jordan—Third Review Under the Extended Arrangement Under the Extended Fund Facility and Request for Modification of Performance Criteria**

Board Action:

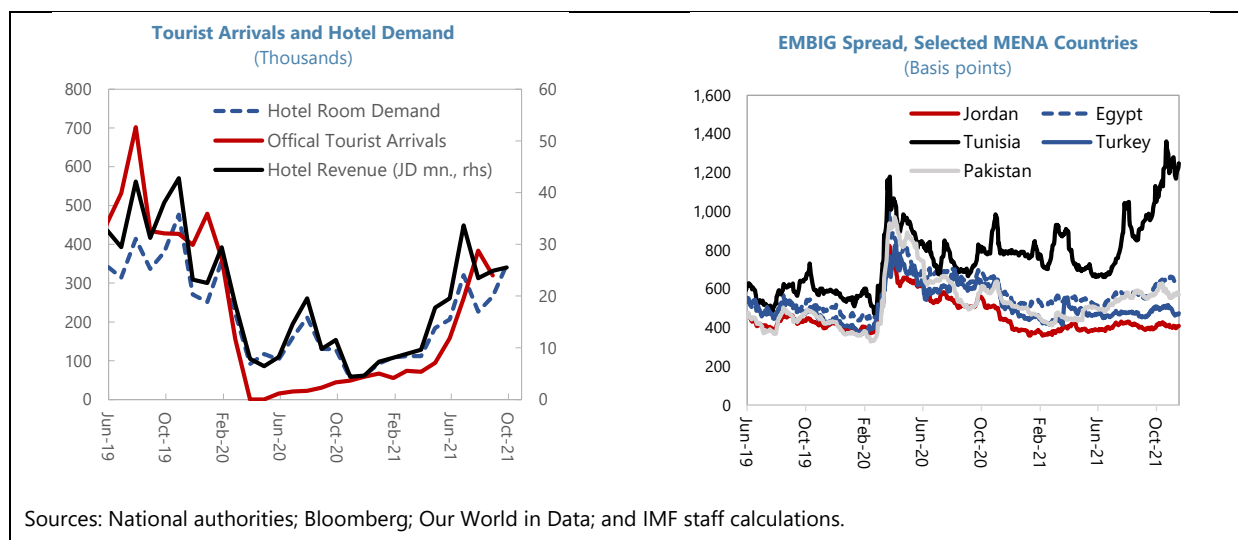
The attached corrections to EBS/21/117 (12/8/21) have been provided by the staff:

Factual Errors Not Affecting the Presentation of Staff's Analysis or Views

Pages 7, 14, 16

Questions:

Mr. Abbas, MCD (ext. 34547)
Ms. Guscina, MCD (ext. 34836)
Ms. Bouza, MCD (ext. 34178)



5. Downside risks to the outlook are considerable. While almost two-fifth of residents have been vaccinated, the emergence of new variants could delay the projected rebound in tourism and the service sector. Persistently high unemployment raises the risk of additional economic scarring, particularly given the decline in labor force participation for young men. Expectations of an earlier monetary policy normalization by the Fed and subsequent repositioning of market participants could further strain Jordan's external and fiscal positions through a tightening of global financial conditions and a rise in external borrowing costs across emerging markets. There is a risk of contingent liability materializations from the broader public sector, including higher-than-expected outlays to address water scarcity. Social discontent, given rising unemployment and poverty rates, could complicate the rollout of reforms. Downside risks are partially mitigated by the authorities' commitment to the program, continued-additional donor support, and a hitherto resilient financial sector. On the upside, improving regional relations may boost exports, remittances, and aid inflows.

POLICY DISCUSSIONS

6. The discussions focused on near-term policies to support the still-fragile recovery, address high unemployment, and facilitate private-sector-led growth, while ensuring debt sustainability. There was agreement that the persistently high unemployment and rising poverty warrant some near-term policy support. In this context, the program envisages: (i) a gradual fiscal consolidation in 2022, accompanied by structural fiscal reforms to close tax loopholes, protect jobs, support the most vulnerable, and mitigate fiscal risks; (ii) proactive measures and oversight to preserve monetary and financial stability; (iii) efforts to ensure the electricity and water sectors to financial sustainability, while accounting for Jordan's energy and water needs; and (iv) continued structural reforms to strengthen job creation, competitiveness, and governance.

place in 2020. NPLs remain low (5.3 percent) but given the debt deferment period for affected borrowers expires end-2021, it will likely take time for the asset quality effects of the pandemic to fully manifest. Accordingly, there is a need for continued close monitoring of banks' asset quality, and sustained application of prudent accounting, reporting, and provisioning standards. Should downside risks materialize, the CBJ should ensure that banks swiftly resolve NPLs, while requiring weaker banks to prepare prudent but feasible capital restoration plans.

Jordan: Bank Soundness Indicators			
	2019	2020	2021^{1/}
Risk-weighted capital adequacy ratio	18.3	18.3	18.3
NPLs (In percent of total loans)	5.0	5.5	5.3
Provisions (In percent of classified loans)	69.5	71.5	75.2
Liquidity ratio	134.1	136.5	136.2
Return on assets	1.2	0.6	1.2
Loans to deposits ratio	81.6	84.5	86.0

Source: Central Bank of Jordan.
^{1/} June 2021 data.

16. Enhancing the regime for Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) is a priority (MEFP ¶120). Notwithstanding the ~~passage of amendments to the enactment of a new~~ AML/CFT law in ~~August-September~~ 2021, Jordan was placed on the Financial Action Task Force (FATF)'s watch list in October 2021 (consistent with the results of the 2019 mutual evaluation). The authorities have committed to an action plan for resolving the identified strategic deficiencies to facilitate exit the watch list by October 2023 (*new proposed SB for October 2023*). The authorities have also committed to intermediate steps, such as an assessment to identify non-profit organizations that are vulnerable to terrorist financing abuse; and addressing AML/CFT deficiencies such that Jordan would no longer qualify for referral to the FATF's ICRG process on the basis of its technical compliance ratings (*new proposed SB for June 2022*).

17. Finally, the authorities are leveraging Fund TA to update their monetary policy and banking supervision frameworks, and payment systems, and are preparing for the financial sector assessment program update in 2022 (MEFP ¶123–24).

C. Reforming the Electricity and Water Sectors

18. NEPCO's financial losses undershot expectations in 2021, but will be higher in 2022. The shift in demand from the business sector to the (more heavily subsidized) household sector during lockdown periods weakened NEPCO's revenues in the first half of the year. However, costs significantly undershot expectations due to delays in the coming online of the Attarat oil shale plant (previously expected in mid-2021), while long-term supply contracts for natural gas largely shielded NEPCO from the surge in global commodity prices. NEPCO losses are projected to be contained to 0.5 percent of GDP in 2021, but will rise to 1 percent of GDP in 2022 as Attarat comes online. Separately, NEPCO

300 MCM of water starting 2028. The authorities are committed to transparent and competitive tendering, aligning project due diligence with requirements under the PPP law (which was enacted after the start of the project), and a careful assessment of fiscal risks (including contingent liability materialization) to ensure the project is consistent with debt sustainability. A recent [deal-declaration of intent](#) to supply solar power in exchange for water from Israel could also contribute to reducing water scarcity in the medium term.

D. Structural Reforms to Strengthen Employment, Investment, and Governance

23. The program supports policies aimed at addressing structural impediments to formal employment.⁷ The government has been working on addressing obstacles to female employment, including by: (i) removing gender-biased articles from labor legislation, (ii) tightening sexual harassment and workplace violence protection (MEFP ¶129); and (iii) improving access to safe and affordable transportation (such as the recently-launched Bus Rapid Transit for Amman). To promote youth employment, the authorities lowered social security contributions in the agricultural and IT sectors and are looking to extend these reduced rates for new workers under the age of 30 for a period of 10 years in all sectors. To address skills mismatch, they are working on strengthening vocational training and internship/employment programs targeted at the youth.

24. Improving the business environment, governance and competition framework is crucial to engendering strong, durable, and inclusive growth (MEFP ¶130). To reduce the cost of doing business, the authorities are streamlining licensing requirements, lowering electricity tariffs for businesses, and are working on strengthening the competition [framework](#) and [operationalizing the insolvency framework](#). A new draft legislation to strengthen the competition framework, including empowering the relevant regulatory body and strengthening antitrust legislation, in line with the UNCTAD Model Law on Competition, will be submitted to Parliament by end-June 2022 (new proposed SB). Building on recent reforms, the government is strengthening the anti-corruption legal framework and the capacity of the Integrity and Anti-Corruption Commission, including on implementing the amended Illicit Gains Law recently passed by Parliament.

PROGRAM FINANCING AND SAFEGUARDS

25. Donors remain engaged. Notwithstanding the small grant shortfall in 2021, grant projections for 2021–22 combined are around US\$100m higher than at the Second Review, with larger USAID and EU contributions. Concessional loans are projected to be US\$280 million weaker primarily due to the [delayed-later than anticipated](#) disbursement of the EU MFA III ~~to~~ (2022Q4 at the earliest) and some reprofiling of World Bank

⁷ The IMF team is working with the ILO on a collaboration concept note with the aim to provide more focused structural recommendations during the upcoming 2022 Article IV discussions.