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Ex-ante evaluation statement

Accompanying the document

**Proposal for a DECISION OF THE EUROPEAN PARLIAMENT AND OF THE
COUNCIL**

**providing further Macro-Financial Assistance to the
Hashemite Kingdom of Jordan**

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**Ex-ante evaluation statement on
EU macro-financial assistance to Jordan**

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1. PROBLEM ANALYSIS AND NEEDS ASSESSMENT

1.1. Introduction

In recent years, the Jordanian economy has been significantly affected by regional unrest, notably in neighbouring Iraq and Syria. This regional unrest has taken a heavy toll on external receipts and has strained public finances. Lower tourism and FDI inflows, blocked trade routes for 8 years, and repeated disruptions to the flow of natural gas from Egypt, which forced Jordan to replace gas imports from Egypt with more expensive fuels for electricity generation, have put a drag on growth and weighed on Jordan's external and fiscal positions. The Syrian conflict has impacted Jordan not only by disrupting trade with and through Syria but also by causing a large inflow of around 1.3 million of Syrians refugees (according to estimates from the Jordanian authorities) of which 660,330 are registered with the office of the United Nations High Commissioner for Refugees – UNHCR (data as of 4 august 2019). This large inflow of Syrian refugees into Jordan has increased pressure on Jordan's fiscal position, public services and infrastructure.

A broadly appropriate policy response and large-scale international support helped the country to preserve macro-economic stability. Jordan was supported by a financial assistance programme by the International Monetary fund (IMF) and other international donors. As part of this assistance package, the EU implemented two macro-financial assistance (MFA) programmes totalling EUR 380 million to alleviate the short-term financing pressures Jordan has been facing, while supporting economic reforms and the reduction of vulnerabilities. Key economic reforms in the context of the above-mentioned programmes (such as the abolition of energy subsidies and the expansion of the tax base) helped the country to lower external and fiscal deficits, to replenish part of its foreign reserves and to avoid a balance of payment crisis.

However, Jordan's economy remains vulnerable to external shocks. Despite improvements, real growth receded to 1.9% in 2018, the lowest rate since 1996. Unemployment jumped to 19% in early 2019, while FDI plummeted to 2.4% of GDP in 2018, the lowest inflow since 2003. The replenishment of Jordan's international reserves proceeded more slowly than expected. Despite efforts, fiscal consolidation was not sustained at the initially programmed pace, as a result of lower than expected growth, which weakened tax revenues, and the generation of losses by the electricity company in the absence of cost-reflective tariffs. Public debt has barely decreased and Jordan remains dependent on foreign aid. Indeed, Jordan continues to face considerable external financing needs including payment obligations on Eurobonds and other external market borrowing which comes due in 2020-22.

The "London Initiative" conference, held in February 2019, played an important role in securing additional concessional financing and budget grants from donors to help Jordan to bridge its external financing gap for the next years in a way that would safeguard debt sustainability. In this context, seeking support for the country's renewed balance of payments needs, including the replenishment of international reserves, the **Jordanian authorities requested further MFA from the EU on 11 July 2019** in the amount of EUR 500 million in three instalments.

Taking into consideration this request and following an in-depth assessment of the political and economic situation in Jordan, **the European Commission is submitting to the European Parliament and the Council a proposal to provide MFA of EUR 500 million to Jordan in the form of loans.** Having taking into account the preliminary discussions of the Jordanian authorities with IMF staff for a new IMF programme for Jordan beyond March 2020, the proposed MFA operation envisages three instalments. The proposed MFA will

cover part of Jordan's residual external financing needs in 2020 and 2021 in the context of the prospective new IMF programme. These needs are estimated at USD 5.8 billion (approximately EUR 5.1 billion) after taking into account financing resources that have been approved by the IMF and the World Bank until June 2019. The EU's renewed assistance would be expected to reduce the economy's short-term balance of payments and fiscal vulnerabilities, while supporting the government's adjustment and reform programmes through an appropriate package of accompanying policy measures to be agreed with the Jordanian authorities in a Memorandum of Understanding.

1.2. Jordan's macro-economic situation

The Jordanian economy has been particularly affected by the conflict in Syria, which broke out in 2011. Following a period of robust growth averaging 6.2% during 2001-2010, Jordan's GDP growth has decelerated to an average of 2.4% in 2011-2018. While reflecting Jordan's long-standing macro-economic and structural weaknesses, the economic slowdown was largely driven by a series of external shocks including the disruption of critical export routes and markets from protracted regional conflicts, the sharp decline in FDI, the hosting of Syrian refugees, and rising oil prices and borrowing costs reflecting the rise of Fed's rates.

The weakening of economic activity continued in 2018, as real GDP growth slowed to 1.9% in 2018 (from 2.1% in 2017) marking the lowest rate of expansion since 1996. Positively, tourist inflows and exports recovered somewhat and two border crossings with Iraq and Syria were reopened in 2018. In the fourth quarter of 2018, low-cost gas imports from Egypt also resumed. However, these developments have yet to manifest themselves in growth figures: in the first quarter of 2019, real GDP increased by 2%, essentially unchanged when compared with the pace of recent years.

Against this background, unemployment rose to 19% in Q1 2019 from 18.4% a year earlier, marking a significant upward trend since 2014, when it stood at 12.9%. Unemployment for youth (38.5%) and women (28.9%) remains high compared to unemployment for men (16.4%).

Inflation rose to 4.5% in 2018 (from 3.3% at the end of 2017) reflecting the increase in oil prices during much of 2018 and the rise of the General Sales Tax in various basic products that was enacted in January. However, in the first four months of 2019 inflation moderated to 0.6% as the effect of the tax increases faded away. The Central Bank of Jordan increased the re-discount rate in seven steps from 3.75% to 5.75% between February 2017 and December 2018. This broadly mirrors the Fed's rate rises, given the peg of the Jordanian Dinar to the US dollar. The tightening cycle coincided with a gradual yet moderate increase in inflation, as mentioned earlier. In June 2019, the re-discount rate remained unchanged (at 5.75%) as foreign exchange pressures, which had persisted in 2018, eased in light of a fading and eventual reversal of market expectations for further US monetary policy tightening. Nevertheless, in the context of the second review of the IMF programme, the authorities expressed their readiness to tighten monetary policy, if needed, to ensure reserve targets are met.

Jordan made significant progress in consolidating its public finances in the past years, but on the back of the weak growth profile and lack of progress in addressing the losses of the public electricity and water supply providers, this progress could not be sustained in 2018. The overall fiscal deficit (including grants) widened to 3.3% of GDP in 2018 from 2.2% of GDP in 2017. The combined public sector deficit – a fiscal metric that takes into account the balance of NEPCO (the public electricity provider) and WAJ (the Water Authority of Jordan) – jumped to 4.3% of GDP in 2018 from 2.9% of GDP in 2017 reflecting increased cost of oil combined with the absence of cost-reflective tariffs in the electricity and water sectors, which

encourages over-consumption. For 2019, the IMF programme foresees the reduction of the fiscal and of the combined public sector deficit to 2.3% and 2.6% respectively. In the first four months of 2019 the fiscal deficit narrowed to 3% of GDP from 3.8% of GDP year-on-year. However, tax revenues declined by 1.4% year-on-year raising concerns about the budget execution until the end of 2019.

At the end of March 2019, total gross public debt stood at 94.4% of GDP, practically unchanged from end-2018. External public debt amounted to 39.4% of GDP, out of which 72% was denominated in USD, to which the Jordanian Dinar is pegged. While the elevated level of public debt is a source of vulnerability, the IMF judges it to be sustainable, provided that the country continues to deliver on fiscal adjustment and growth enhancing reforms and that the international and regional donor community continues to provide significant support to Jordan.

With respect to the external sector, Jordan's current account deficit narrowed in 2018 to USD 2.9 billion or 7% of GDP (10.3% excluding grants) from 10.5% of GDP in the same period in 2017. This reflected a moderate increase in goods exports (which increased by 3.4% in value terms), while goods imports decreased (by 1.3% in value terms). In the first quarter of 2019, goods exports performed even more strongly, recording a 9.3% increase in value terms, while goods imports decreased by 3.2% in value terms. In the same period, income from tourism increased by 6.1% year-on-year while remittances increased only marginally.

Foreign direct investments (FDI) plummeted to USD 959 million in 2018 (2.2% of GDP), down by 52% in US dollar terms compared to 2017. This marked the lowest net FDI inflow since 2003. This downward trend is consistent with the long-term weakening of FDI (as a share of GDP) since the Syrian conflict: from an average of 12.7% in 2005-2010 to 4.5% in 2011-2018. The regional conflict, which blocked trade routes for 8 years, the economic slowdown in Gulf countries, which were Jordan's major investors, but also the country's structural weaknesses, such as rigid labour markets, constraints to foreign investors and high business costs, contributed to the decline of FDI inflows.

The decline in FDI created further pressures on the capital and financial account, as did a decline in public borrowing from around USD 1 billion in 2017 to less than USD 500 million in 2018. These pressures contributed to a sizeable decrease of the commercial banks' net foreign assets (by around USD 900 million) in 2018, partially caused by tighter monetary policy in neighbouring countries and the political instability in Jordan in mid-2018 (when the Prime Minister resigned in response to public discontent notably over tax reform plans). Conversely, a small net inflow of USD 41 million in private portfolio investments in 2018 (compared to a large net outflow in 2017), as well as a considerable increase by around USD 600 million in other investments supported the capital and financial account in 2018.

The current level of reserves – standing at USD 13.2 billion (or 7.1 months of imports) at the end of April 2019 – **should be increased** to make the country more resilient to the above factors. This is particularly important given the vulnerability of the external position, the elevated risks from regional conflicts or geo-political tensions, the exchange rate peg and exposure to oil price shocks.

Table 1. Jordan – Selected Macro-economic indicators, 2015-2021

	2015	2016	2017	2018	2019 ⁽²⁾	2020 ⁽²⁾	2021 ⁽²⁾
Real GDP change, %	2.4	2.0	2.0	1.9	2.2	2.4	2.6
Consumer price inflation, %, end of period	-1.6	0.8	3.2	3.6	2.5	2.5	2.5
Key monetary policy rate, end of period	3.75	3.75	4.75	5.25	5.25	-	-
Unemployment rate, % LFS	13.1	15.3	18.5	18.7	19.0	-	-
Overall fiscal balance including grants, % of GDP	-5.3	-3.2	-2.2	-3.3	-2.3	-2.3	-1.9
Combined public sector balance⁽¹⁾, % of GDP	-7.1	-3.8	-2.9	-4.3	-2.6	-1.7	-0.6
Grants to the Budget, % of GDP	3.3	3.0	2.5	3.0	2.4	2.1	1.6
Government gross public debt, % of GDP	93.4	95.1	94.3	94.4	94.6	94.1	92.4
Gross external public debt, % of GDP	35.3	37.5	39.9	37.4	41.3	42.3	44.4
Current account balance, % of GDP	-9.1	-9.5	-10.6	-7.0	-7.0	-6.2	-6.6
International reserves, USD billion	15.7	14.5	14.2	12.5	14.3	15.7	17.4
International reserves, months of imports	8.5	8.2	7.5	6.4	7.0	7.4	7.9
Foreign direct investment, % of GDP	3.7	4.0	4.9	2.2	3.6	4.3	4.3

Source: IMF, CBJ, MoF

(1) Defined as the sum of the primary central government balance (excl. grants and transfers to NEPCO and WAJ), NEPCO operating balance, WAJ overall balance, and, starting in 2019, Aqaba, Miyahuna and Yarmouk Water Distribution Companies' overall balance.

(2) IMF projections - May 2019

Despite the favourable developments in exports and tourism, a number of vulnerabilities remain. The country continues to operate under a difficult economic environment impacted by the protracted regional conflict, the hosting of Syrian refugees, the disruption or slow recovery of critical export markets and the marked fall of FDI. As a result, growth has remained in very low levels and is insufficient to reduce high unemployment. As happened in 2018, the pace of future fiscal adjustment could be lower than envisaged if growth weakens further and Jordan fails to mobilise tax revenues through combating tax evasion and increasing the capacity of tax administration. The same could happen if Jordan does not achieve to restructure effectively the loss-making state-owned (electricity and water) companies which add to the general government's deficit. In addition to the above risks, borrowing costs are higher compared with Jordan's Eurobonds that will mature in the coming years (many of which were US-guaranteed), rendering a roll-over of the bonds costly. For the above reasons, the current projection for the decline of public debt to 83.7% by 2024 remains fragile and depends on the success of fiscal adjustment and growth-enhancing reforms that the authorities have committed to do, as well as on their ability to continue attracting sizeable donor and market financing. Reserves remain below IMF adequacy standards and could come under renewed pressure in 2020-2021, when the country is expected to make around USD 3.1 billion of payments (interest and principal) on sovereign and Eurobonds external debt. In this context, the further replenishment of Jordan's international reserves seems necessary, and the EU's additional MFA could usefully support this effort, both directly (through its disbursements) and indirectly (as a catalyst for private capital inflows and instilling confidence in the local currency).

In conclusion, Jordan's economy remains fragile with substantial external financing needs and exposed to a number of vulnerabilities. In this context, continued support from the IMF and Jordan's international partners, including the EU, remains essential.

1.3. IMF and other donor support

In August 2016, the IMF approved a three-year Extended Fund Facility (EFF) programme for Jordan of around USD 723 million (150% of quota). This programme followed a three-year Stand-By Arrangement (SBA) in the amount of USD 2 billion (800% of quota) which was approved by the IMF in August 2012 and completed in August 2015.

The primary purpose of the EFF programme is to aid the country to achieve a gradual but steady fiscal adjustment to lower public debt and to implement broad structural reforms to enhance the conditions for higher and more inclusive growth. The main elements of the EFF arrangement, when it was approved, were:

- To achieve gradual and steady fiscal consolidation to bring the public debt down to safer levels (from 94% in 2016 to 77% of GDP by 2021) while protecting vulnerable parts of the population. Structural benchmarks in the fiscal area included: the revamping of the tax exemption framework of the General Sales Tax, implementing a more broad-based income tax law, the adoption of a new public debt management strategy as well as measures to maintain NEPCO's operational balance and reduce the WAJ's deficit.
- To boost structural policies in order to improve the business climate and promote growth and jobs. In this regard, the IMF programme had envisaged streamlining inspection procedures for businesses and improving the operation of the single investment window by automating and integrating the services provided by Jordan's Investment Commission.
- To deepen the financial sector and facilitate access to finance. Measures in this area included the establishment of a new bank resolution framework, the adoption of new legislation on insolvency and on secured lending operations.

Since the approval of the EFF, in August 2016, macro-economic conditions have worsened markedly. In the period 2016-2018 economic growth averaged to 2% from 3.3% initially envisaged. Tax revenue shortfalls, the absence of effective measures to ensure financial viability of the electricity and water companies, and delays in implementing a new broad-based income tax law, slowed down the pace of fiscal consolidation: at the end of 2018, the combined fiscal deficit (which includes the balance from the electricity and water utilities) was recorded at 4.3% of GDP from 2% of GDP forecasted in 2016 while public debt is now expected to decline to 92.4% of GDP in 2021 from 77% of GDP as forecasted in 2016. At the same time, new external financing needs appeared for 2020-2021 estimated by the IMF to USD 5.8 billion.

The implementation of the IMF programme advanced with significant delays due to uneven reform implementation and to the re-emergence of significant external financing needs. A first disbursement of USD 72.3 million was made available to Jordan on approval of the EFF programme, while a second disbursement of USD 71 million was made available with the completion of the first review of the programme, which was approved in June 2017 by the IMF Executive Board. Following delays in the implementation of tax policy benchmarks (notably the new income tax law which was adopted in December 2018, instead of March 2017 as initially agreed), the IMF reached a staff-level agreement with the Jordanian authorities in February 2019 on the completion of the second review. However, the review was only completed on 6 May 2019 by the IMF Executive Board, after the provision by the international community of sufficient financial assurances (of around USD 5.1 billion) to cover Jordan's external financing gap for the period 2019-2023. The financial assurances from the international community will support a comprehensive medium-term reform programme – the so-called Five-Year Reform and Growth Matrix⁶ – that Jordan devised with the assistance of the World Bank and presented at the “London Initiative” conference on 28 February 2019.

Following the completion of the second programme review, a total of USD 310 million (out of USD 723 million) had been disbursed from the IMF programme. At the same time, the IMF Board decided to extend the time-span of the programme until March 2020. In this context, the third programme review is expected to take place in September 2019 and the fourth and last programme review in March 2020. The focus of the remainder of the EFF

programme will be on actions that enhance the financial sustainability of the electricity and water utilities in Jordan. Other benchmarks include strengthening the PPP framework and the monitoring of contingent liabilities, transferring the supervision of insurance market to the Central Bank of Jordan and studying different options for a temporary lowering of the payroll tax for women and the youth.

The Jordanian government has already started preliminary discussions with the IMF staff for a follow-up programme beyond March 2020.

Since the onset of the Syrian conflict in 2011, the USD 2.8 billion extended by the IMF (through a Stand-By Arrangement and an Extended Fund Facility) for Jordan has been complemented by substantial support from Jordan's bilateral partners, including the EU. The World Bank has extended loans of USD 3.1 billion under different instruments while the EU has extended around EUR 2.1 billion for the same period. Other international financial institutions such as the EBRD and the EIB and bilateral donors such as France, Germany, Italy, the US, Japan and the countries of the Gulf Cooperation Council have also significantly scaled up their activity to support the country to cover its financing needs and increase its resilience.

The High-level mission to Jordan led by EU Commissioner Hahn in June 2019 and composed of eight International and European financial institutions and partners was an important sign of coordinated international support to Jordan in facing its economic challenges and in implementing its socio-economic reforms. The proposed macro-financial assistance will build on these efforts to align international support in order to help Jordan stimulate inclusive growth, jobs creation and macro-economic stability and contribute to ensure that reform momentum is maintained.

1.4. External financing needs

Jordan continues to face considerable external vulnerabilities. While the country's monetary policy followed closely the movements in US interest rates, it did not prevent a decline of almost USD 1 billion of gross international reserves in 2018. Part of the shortfall was covered in early 2019 (partly due to USD deposits by Saudi Arabia, Kuwait and the UAE). However, the process of replenishment of reserves has been slower than initially programmed by the IMF.¹ As a result, as of April 2019 foreign exchange reserves remain well below the IMF's reserve adequacy metric.² Thus, further reserve build-up is needed to reduce external liquidity risks, in particular in light of the repayment obligation of USD 3.1 billion of external debt (principal and interest) falling due in 2020-21.

According to the estimate of Jordan's financing needs by the IMF in May 2019, **Jordan faces an external financing gap of USD 6.4 billion, or EUR 5.6 billion,³ in 2020-2021** (see Table 2). A considerable portion (USD 2.4 billion) of the country's external financing needs relates to the accumulation of international reserves programmed to reach 113% of the reserve adequacy metric of the IMF. The remainder (USD 4 billion) corresponds to the balance of payments deficit.

¹ A waiver of non-observance of performance criterion on the Net International Reserves of the Central Bank of Jordan (CBJ) was provided during the second IMF programme review in May 2019.

² This metric is composed of three indicators that measure reserves in relation to months of future imports, broad money and short-term external debt repayments. As a rule of thumb, reserves within 100-150% of the metric are considered adequate. Jordan's reserves stand at 97%.

³ All conversions in this document are based on a EUR/USD exchange rate of 1.13.

Part of the external financing gap should be financed by the IMF and the World Bank arrangements, with net disbursements of USD 554 million. Taking the IMF and World Bank net disbursements into account, Jordan's residual external financing needs will still amount to USD 5.8 billion (approximately EUR 5.1 billion) in 2020-2021, of which USD 2.8 billion in 2020 and USD 3.0 billion in 2021. **The proposed EUR 500 million MFA from the EU would thus cover 9,7% of the residual external financing gap for the period 2020-2021.** Compared with the IMF estimates of May 2019, the EU's increased MFA contribution would enable Jordan to reduce its Eurobond issuance in 2020 from USD 1.25 billion (as assumed in the IMF Country Report accompanying the May 2019 programme review) to around USD 1 billion, thus helping to contain interest costs and contributing to debt sustainability. Despite significant contributions also from other bilateral and multilateral donors aside from the IMF, the World Bank and the EU, an amount of USD 1.7 billion has yet to be identified for 2021.

(USD million)	2018	2019	2020	2021	Total 2020-2021
1. Current account balance ⁽¹⁾	-2.973	-4.007	-3.668	-3.895	-7.563
2. Capital and financial account ⁽²⁾	2.040	1.569	1.377	2.222	3.599
3. Overall balance (1+2)	-933	-2.438	-2.291	-1.673	-3.964
4. Reserves ("-" indicates increase)	954	-1.863	-1.046	-1.398	-2.444
5. Overall External Financing Gap (3+4)	20	-4.301	-3.337	-3.071	-6.408
6. Exceptional Financing by IMF and WB	-20	1.450	572	-18	554
Net IMF Disbursements	-493	-81	41	-18	23
Disbursements		336	241	0	241
Repayments		-417	-200	-18	-218
Disbursements of World Bank's DPL	473	1.531	531	0	531
7. Residual Financing Gap (5+6)	0	-2.851	-2.765	-3.089	-5.854
Financing of the gap					
EU MFA-II loan		115	0	0	0
EU MFA-III loan		0	339	226	565
EU budget support grants		94	30	21	51
UK grants		110	110	0	110
Netherlands grants		57	0	0	0
USA grants		750	475	475	950
Saudi Arabia grants		50	50	50	100
United Arab Emirates grants		50	50	50	100
Other grants		67	76	86	162
France loan		118	119	119	238
Germany loan		185	58	58	116
Italy loan		54	54	0	54
Japan loan		200	100	100	200
Kuwait loan		100	100	100	200
Saudi Arabia loan		25	25	0	25
UAE loan		25	25	0	25
Arab Monetary Fund loan		100	100	100	200
Islamic Development Bank loan		26	27	0	27
Other loans (off-budget)					0
Eurobonds ⁽³⁾		725	1.025	0	1.025
Total identified sources		2.851	2.763	1.385	3.123
<i>Other unidentified financing sources</i>		<i>0</i>	<i>2</i>	<i>1.704</i>	<i>1.706</i>
Total MFA-III as % of the residual gap for 2020-2021					9,7%

⁽¹⁾ Amounts in EUR have been converted on the basis of a EUR/USD exchange rate of 1.13.

⁽²⁾ For the period 2019-2021 excludes official grants in the form of policy-based budgetary support.

⁽³⁾ For the period 2019-2021 excludes official loans in the form of policy-based budgetary support.

⁽⁴⁾ Part of the Eurobond that comes due in 2020 (USD 1,250 million) is expected to be covered by MFA funds.

1.5. Structural reforms

Reform achievements in 2016-2018, with uneven progress across sectors

Within a challenging external environment Jordan continued efforts for the implementation of its reform agenda in order to reduce macro-economic imbalances and to generate employment. These efforts were supported by large-scale financial and technical assistance provided by multilateral and bilateral partners, including the IMF, the World Bank and the EU (MFA-II). However, Jordan's efforts delivered only uneven success as the reform process was challenged by regional instability, the low growth environment and rising unemployment as well as by domestic political and social tensions and vested interests which continued to exert influence on policy-making in the country.

Despite these domestic challenges and the difficult economic and external situation, Jordan managed to push through reforms in a variety of sectors, many of which supported through conditionality under MFA II.

In the area of **public finance management**, the authorities – in line with MFA conditionality – adopted and published, in June 2017, an updated Medium-Term Public Debt Strategy with a view to enhancing debt management, improving market access conditions and increasing the average maturity of public debt. The strategy applies to central government debt, as well as to the publicly guaranteed debt of independent public institutions. By increasing the volume and maturity external borrowing, this strategy helped to prevent an increase in interest payments, which decreased marginally to 3.34% of GDP at end-2018 from 3.39% at end-2015, despite an environment of rising global interest rates in much of this period, especially for emerging markets.

Also, the authorities strengthened the external audit function by adopting a new Audit Bureau Law, in September 2018, which enhanced the autonomy of the Jordan's Supreme Audit Institution with regard to the formulation of its budget. Formal acceptance of the INTOSAI rules as the working standard for the Audit Bureau was also reflected, for the first time, in the new legislation. Furthermore, the Audit Bureau withdrew from contacting pre-audits in the Internal Control Units of the Ministry of Finance strengthening their capacity and increasing transparency. Moreover, the government strengthened the public procurement function by adopting a new by-law in May 2019 which is consistent with internationally good practice and is expected to generate considerable fiscal savings for the state.

When it comes to **tax policy**, the government that took office in June 2018 adopted a new Income Tax Law in December 2018 following long-standing preparations and consultations, amid popular discontent. The law broadened the tax base by lowering the exemption thresholds for individuals and households (a joint condition with the IMF programme), increases taxes on certain corporate sectors and sets the basis for a greater focus on tax evasion and tax law enforcement. However, the broadening of the tax base, especially when it comes to the personal income taxation (PIT), was less ambitious than initially proposed due to the high political cost it carried. Thus, the fiscal performance of the PIT-related changes is expected to yield around 0.2% of GDP in additional revenues annually over the medium term, whereas the rest of the interventions in other areas of the law (corporate tax, reduction of tax exemptions, improvements in tax compliance) are expected to yield around 0.6% of GDP in the medium term. Overall, the new law was a measure in the right direction and paved the way to the completion of the second review of the IMF programme by the Executive Board on 6 May 2019.

In addition, in 2017 and 2018, the Jordanian government enacted a set of measures to increase the general sales tax rate on more than 160 items. In this context, the general sales tax was increased to 10% for commodities that were previously subject to rates of 0%-4%. Also, the

authorities decided to lift food subsidies on bread, to introduce a levy of JOD 500-JOD 1,500 (about EUR 630-EUR 1,900) on imported cars and to raise a special tax on carbonated drinks from 10% to 20%. Finally, an increase in excise tax on Octane 95 and 98 gasoline to 30% was enacted, as well as an increase in tax on cigarettes to reach JOD 0.20 per pack. The above measures were a good step towards the rationalisation of the tax exemptions framework in the indirect taxation (general sales tax and custom duties). Nevertheless, their revenue performance was lower than expected due to the slowdown of the economy.

With regard to **social protection**, the authorities made substantial progress towards establishing an operational National Unified Registry (NUR), an automated data exchange system which will improve the targeting of social transfers to help protect vulnerable groups more effectively. They also envisage the gradual extension of cash transfers to more recipients. Moreover, they prepared new studies to estimate poverty lines over updated data – for the first time since 2010 – to determine their approach on poverty reduction. They also took multiple measures including lifting restrictions and providing vocational training with a view to generate employment for Syrian refugees. In addition, the government amended its labour regulations to allow part-time employment as well as to allow hiring of non-Jordanians in highly specialised occupations and positions, especially in technical sectors such as communications, energy, engineering, and professional services.

Some important reforms for **enhancing growth performance** were completed in 2018:

- Four by-laws for businesses’ monitoring and inspection were enacted following the adoption of the relevant law in 2017, leading to around 94,000 labour inspections in 2018. The streamlining of inspection regulations is expected to reduce duplication of inspections by different government departments as well as to enhance monitoring of business activities in an effort to reduce informal employment.
- The law on secured lending was adopted in May 2018 with relevant by-laws following in November 2018. Along with the completion of an online Movable Collateral Registry, this reform is expected to increase lending to SMEs by 7% annually.
- The insolvency law, which was enacted in May 2018, enables the re-organisation of businesses (under certain deals reached with creditors) and regulates the insolvency proceedings of foreign companies in Jordan according to international conventions.
- The abolition of pre-registration approvals issued by the Ministry of Interior for business activities that have low or no impact on public safety and security was also adopted in 2018, while a “Regulatory Predictability Framework” was developed to improve the process of issuing regulations that affect businesses, including instructions and decisions.
- Finally, new governance frameworks were adopted for Public Investment Management, Public-Private Partnership and Venture Capital financing, including specific tax treatment for the Venture Capital funds in Jordan.
- Acknowledging the importance of financial inclusion to growth, the government developed the National Financial Inclusion Strategy (2018–20) to ensure that all segments of society, including individuals and organisations, can access financial services through banks and other financial institutions.

Main government reform priorities for the future

Acknowledging the need for more and deeper structural reforms, the government launched in November 2018 a two-year work plan under the name Path to Revival for 2019–20 (widely known as the Renaissance plan), which is centred on three main pillars: 1) strengthening the rule of law, 2) increasing productivity and 3) enhancing solidarity. Actions in the context of the first pillar aim at improving relevant legislation, developing political life, protecting public freedoms, combating corruption, enhancing integrity and transparency and advancing

decentralisation as well as citizens' participation in their communities. Actions in the context of the second pillar aim at creating 30,000 additional jobs by 2020 (mostly through the manufacturing sector, the garment and textile industries, the tourism and hospitality sector) increasing exports by 5% annually, reducing the cost of energy imports by 15% by end-2020, increase FDI flow by 10% by end-2020 and at bolstering the performance of public administration. The third pillar will have a focus on increasing social protection and improving the level of public services, such as health, education, water, environment and transport.

With a view to tackling economic challenges more effectively, Jordan has **embarked on a more ambitious, comprehensive and wide-ranging reform programme** which was prepared in collaboration with the World Bank and presented during the "London Initiative" conference in February 2019. This reform programme – the so-called **Five-Year Reform and Growth Matrix** – aims to preserve macro-economic stability, to increase Jordan's growth prospects, to make the economy more competitive and export-led and to attract new investment. Many of the actions in the Five-Year Reform and Growth Matrix cover targets envisaged by the Renaissance plan. The government has identified a set of cross-cutting (horizontal) reforms and sectoral (vertical) reforms over the following Pillars:

Horizontal Reform Pillars:

1. Pursue macro-economic adjustment, narrow imbalances, manage risks, and improve public sector efficiency
2. Reduce business costs, improve regulatory quality, and increase competition
3. Drive FDI and promote export development of products, services, and markets
4. Deepen access to finance from banks and non-bank financial institutions
5. Create more flexible labor markets for job creation
6. Expand and improve social safety nets to better protect the poor and vulnerable.

Vertical Reform Pillars

7. Improve public transport efficiency and access
8. Increase energy efficiency and access
9. Promote water security and agribusiness

Some of the **envisaged reforms are relevant to improve Jordan's fiscal performance**, such as the enhancement of the financial sustainability of the electricity and water companies, the implementation of a new public procurement system for the public sector, the increase of revenue mobilisation by combating tax evasion and enhancing tax administration capacity, the review of the frameworks for Public Investment Management and Public Private Partnerships, and the improvement of the framework for assessing contingent liabilities.

Other reforms of a more structural nature will be essential for Jordan in order to achieve **higher and more inclusive growth** and to reduce unemployment especially among women and youth. In this regard, reducing business cost, raising domestic firm-level productivity, streamlining licencing and inspection requirements, reducing the regulatory compliance burden, possibly open new sectors to investments would help local firms to integrate into global value chains and therefore could raise FDI and export potential.

Labour market reforms, in the direction of reducing labour market fragmentation, increase flexibility, reducing skills mismatch through vocational training, improve working conditions, enhancing the supervisory and inspection role of the Ministry of Labour and providing incentives for employment of women and youth will be important to bring unemployment down.

Given the challenging economic context and the rise of unemployment, the **social protection system** in Jordan needs to be supported in order to be more effective. Actions to improve the

identification of more vulnerable citizens should continue. The cash transfers scheme should be better targeted and more effectively combined with the provision of social services. There is also a scope to increase its coverage in the next years as its targeting improves.

While the government plans go in the right direction, **implementation of the reforms is likely to be challenging** for the authorities. Given the scale and scope of the reform plan, close engagement and **coordination** with various government constituents (Prime Minister, the Minister of Planning and International Cooperation, the Secretaries General of the key line ministries, and other key determinants of ownership of the programme) will be critical for success. **Targeted policy conditionality linked to international support programmes, such as the proposed EU MFA, can play an important role in strengthening domestic reform implementation.** Close coordination with and between development partners on reform priorities and disbursement conditionalities is essential in this context. A new multi-donor trust fund with seed funding of about USD 18.5 million over five years from the United Kingdom, as well as foreseen contributions from other donors including the EU, will help supporting this coordination, including through a dedicated Secretariat in the Ministry of Planning and International Cooperation. Last but not least, communication by the authorities with the general public will be essential to ensure popular buy-in to the reform programme and overcome vested interests.

2. OBJECTIVES AND RELATED INDICATORS OF THE MACRO-FINANCIAL ASSISTANCE

2.1. Objectives

The objectives of the proposed MFA operation are to:

- (i) contribute to covering the external financing needs of Jordan in the context of a sizeable external financing gap brought about by lower-than-expected growth and private capital flows, significant external debt amortisation, additional fiscal cost of hosting the Syrian refugees and the need to build up foreign exchange reserves;
- (ii) alleviating Jordan's budgetary financing need;
- (iii) support the fiscal consolidation and external stabilisation efforts in the context of the IMF programme;
- (iv) support structural reform efforts aimed at improving the overall macro-economic management, strengthening economic governance and transparency, improving conditions for sustainable growth, reducing unemployment and enhancing debt sustainability;
- (v) facilitate and encourage efforts of the authorities of Jordan to implement measures identified under the EU-Jordan Association Agreement and the Partnership Priorities in the context of the bilateral cooperation programmes, support regulatory convergence and economic integration with the EU and strengthen the EU's economic policy dialogue with the authorities.

2.2. Monitoring Indicators

The fulfilment of the objectives of the assistance will be assessed by the Commission, including in the context of the ex-post evaluation (see below), on the basis of the following indicators:

- Progress with macro-economic and financial stabilisation, notably by assessing the degree of adherence to the IMF-supported programme.

- Progress with the implementation of structural reforms, notably the specific policy actions identified as conditions for disbursement of the assistance, which will be included in a Memorandum of Understanding to be negotiated between the Commission and the Jordanian authorities.

3. DELIVERY MECHANISMS AND RISK ASSESSMENT

3.1. Delivery mechanisms

The proposed new MFA would amount to EUR 500 million disbursed in three instalments. The Commission proposes to disburse the full amount in the form of medium- to long-term loans. As usual, these loans will have favourable conditions in terms of long maturities (of up to 15 years on average) and a low interest rate (the rate at which the EU, benefiting from its high credit rating, borrows the funds in the international capital markets). This form of financial support is similar to the one provided under the previous two MFA programmes that were implemented in 2015-2019. It is consistent with the treatment granted by the World Bank and the IMF to Jordan.

MFA provides untied and undesignated macro-economic support, which helps the beneficiary country to meet its external financing needs, and may contribute to alleviating budgetary financing needs. The funds would be paid to the Central Bank of Jordan. Subject to provisions to be agreed in the Memorandum of Understanding, including a confirmation of residual budgetary financing needs, the funds may be transferred to the Ministry of Finance of Jordan as the final beneficiary.

3.2. Risk assessment

There are fiduciary, policy and political risks related to the proposed MFA operation.

First, there is a risk that the MFA could be used in a *fraudulent way*. As MFA is not designated to specific expenses by Jordan (contrary to project financing, for example), this risk is related to factors such as the general quality of management systems in the Central Bank of Jordan and the Ministry of Finance, administrative procedures, control and oversight functions, the security of IT systems and the appropriateness of internal and external audit capabilities.

To mitigate the risks of fraudulent use several measures will be taken. The Loan Agreement will comprise a set of provisions on inspection, fraud prevention, audits, and recovery of funds in case of fraud or corruption. It is further envisaged that a number of specific policy conditions will be attached to the assistance, including in the area of public finance management, with a view to strengthening efficiency, transparency and accountability. Also, the assistance will be paid to a specific account of the Central Bank of Jordan.

Moreover, in line with the requirements of the Financial Regulation, the Commission services will carry out an Operational Assessment of the financial and administrative circuits of Jordan to ascertain that the procedures in place for the management of programme assistance, including MFA, provide adequate guarantees. The assessment will cover areas such as budget preparation and execution, public internal financial control, internal and external audit, public procurement, cash and public debt management, as well as the independence of the central bank. The preliminary findings of the consultancy company to be engaged with this Operational Assessment are to be received in the first quarter of 2020. Developments in that area will be further closely monitored by the EU Delegation in Amman. The Commission is also using budget support assistance to help the Jordan authorities improve their PFM systems, and these efforts are strongly supported by other donors.

Finally, the assistance will be liable to verification, control and auditing procedures under the responsibility of the Commission, including the European Antifraud Office (OLAF), and the European Court of Auditors.

Second, a risk stems from the possibility that Jordan will *fail to service the financial liabilities* towards the EU stemming from the proposed MFA loans (default or credit risk), which could be caused for example by a significant additional deterioration of the balance of payments and fiscal position of the country. A potential trigger for this risk could be the deterioration of the regional geopolitical situation, in particular the protracted conflict in Syria, which obstructs regional trade flows and acts as an important deterrent to private capital inflows. A worsening of the regional geopolitical situation could have a negative impact on Jordan's macro-economic stability, affecting the performance of the IMF programme and the disbursement and/or repayment of the proposed MFA.

This risk is mitigated, however, by the fact that the EU's MFA is part of an international package of official assistance led by the IMF that is supporting an adjustment and reform programme aimed at restoring fiscal and balance of payments sustainability through the implementation of a series of policy measures, included those to be agreed in the Memorandum of Understanding between the EU and the Jordanian authorities. Moreover, the risks for the EU budget are cushioned by the EU's Guarantee Fund for external actions.

Finally, there is a risk of *weak reform implementation*. This might be due to possible social unrest in the face of a difficult economic environment, high unemployment and the continuation of fiscal consolidation and the related rise in taxes or adjustment in utility tariffs. Specific professional groups or other vested interests may attempt to obstruct or weaken reform decisions resulting in insufficient reform implementation.

However, despite the difficult regional economic and social environment, the Jordanian authorities have requested further MFA, knowing that disbursements will be conditional on the implementation of reforms to be agreed. This conditionality provides a tool to support reform-oriented forces in the country. Also, the MFA will be part of large-scale support from the international community which will facilitate a better and more coordinated overview of the government's performance over implementation of the reforms. Moreover, politically Jordan remains highly committed to the Association Agreement and the Partnership Priorities with the EU, which foresee close cooperation under three pillars: a) strengthening cooperation on regional stability and security including counter-terrorism; b) promoting economic stability, sustainable and knowledge-based growth, quality education and job creation; and c) strengthening democratic governance, the rule of law and human rights.

Having made a thorough assessment of the risks, the Commission services consider that there are sufficient grounds and guarantees to proceed with the proposed MFA to Jordan. The Commission services will maintain close contacts with the Jordanian authorities during the implementation of the MFA in order to address quickly any concerns that may arise.

4. ADDED VALUE OF EU INVOLVEMENT

The proposed MFA to Jordan reflects the country's strategic importance to the EU and is in line with the objectives of the European Neighbourhood Policy (ENP). The MFA instrument is a policy-based instrument that aims to alleviate short- and medium-term external financial needs. As a part of the overall EU package of assistance, it would contribute to supporting the Union's objectives of economic stability, economic development and resilience in Jordan and, more broadly, in the South European neighbourhood.

The MFA programme will highlight the EU's solidarity with and confidence in Jordan, as well as Jordan's geo-political importance for the EU in the context of the Syrian crisis. This is

consistent with EU's commitments towards Jordan as expressed on several occasions in recent years including in the London Initiative conference in February 2019 and in the Brussels III conference in March 2019.

By supporting the Jordan authorities' efforts to establish a stable macroeconomic framework and implement ambitious structural reforms, the proposed MFA operation enhances the added value of the overall EU involvement in Jordan and improves the effectiveness of other forms of EU financial assistance to the country, including budget support operations and grants available through external financial instruments under the current multiannual financial framework for 2014-2020.

In addition to the financial impact of the MFA, the proposed programme will strengthen the government's reform commitment and further foster its aspiration towards closer relations with the EU, as reflected by the Association Agreement that entered into force in May 2002 and the Partnership Priorities with the EU that have been in force since 2016. This result will be achieved, inter alia, through appropriate conditionality for the disbursement of the assistance. In a larger context, the programme will signal to the other countries in the region that the EU is ready to support countries embarking on a clear path towards economic reforms.

The proposed MFA is also an integral part of overall international support for Jordan and will continue to complement and add value to the assistance provided by other multilateral and bilateral donors. By complementing the resources made available by the IFIs and other donors, EU MFA contributes to the overall effectiveness of the financial support agreed by the international donor community. Furthermore, by providing long-term financing on highly concessional terms, usually lower than the other multilateral or bilateral donors, the MFA programme will contribute to enhancing Jordan's debt sustainability, while helping the country to preserve necessary social spending amid the persistent economic and social pressures arising from the challenging regional context. MFA conditions will also help fostering a sustainable balance of payments and budgetary position, raising potential growth, promoting integration and regulatory convergence with the EU and strengthening public finance management.

5. CHARACTERISTICS OF MACRO-FINANCIAL ASSISTANCE

5.1. Exceptional Character and Limited Timeframe

The proposed MFA operation would be exceptional, aiming to support the restoration of a sustainable external finance situation of Jordan. It would have an availability period of 2.5 years from the entry into force of a Memorandum of Understanding, as part of conditionality requirements described below. The operation is expected to run along with continued IMF programme engagement with Jordan. While the current IMF programme is set to expire in March 2020, the Jordanian authorities and IMF staff have started discussions in order to engage in a follow-up programme from March 2020 onwards. Against this background and given the time required for the legislative process in the European Parliament and the Council, the EU's assistance is expected to be implemented in 2020 and 2021. Subject to the implementation of the policy measures to be agreed, the disbursement of the first instalment could take place in the second quarter of 2020, the disbursement of the second instalment could take place in the fourth quarter of 2020, while the disbursement of the third instalment could be made available in the spring of 2021.

5.2. Political preconditions and EU-Jordanian relations

MFA is available to third countries that are politically, economically and geographically close to the EU. Countries that are covered by the ENP, like Jordan, are in principle eligible for MFA. In order to receive MFA, the beneficiary country needs to respect effective democratic mechanisms (including a multi-party parliamentary system) and the rule of law and guarantee the respect for human rights.

Political preconditions: The political preconditions for receiving MFA may be considered to be fulfilled in the case of Jordan. Jordan has continued its political reform efforts to strengthen parliamentary democracy and the rule of law. The country maintained its commitment to improve the general human rights situation, and recorded legislative improvements notably as regards the independence of the judiciary and women's rights. It has to be noted that social cohesion was threatened by regional instability, high unemployment, terrorist incidents and emerging risks of radicalisation. In this context, the increased need for security and political stability was not conducive to further democratisation, strengthening of human rights and expanding fundamental freedoms. Therefore, challenges remain, especially in the areas of gender-based violence and gender equality, fundamental freedoms, death penalty, torture and child protection as well as in freedom of expression and association. Nevertheless, overall, Jordan's progress in enhancing its democratic governance and strengthening the rule of law under substantial challenges, represents an important case in particular when compared with other countries in the region.⁴

EU-Jordanian relations: The EU and Jordan enjoy excellent relations and have been linked by an Association Agreement since 2002 (advanced status since 2010). In 2016, they signed the Partnership Priorities which were extended until 2020 and enhanced cooperation in the following areas: a) strengthening cooperation on regional stability and security including counter-terrorism; b) promoting economic stability, sustainable and knowledge-based growth, quality education and job creation; and c) strengthening democratic governance, the rule of law and human rights. The EU and Jordan are allies in international politics (e.g. International Syria Support Group, Middle East Peace Process) and have largely congruent views on the root causes of and responses to regional and global crises.

Trade relations between the EU and Jordan are governed by the Association Agreement. This agreement established a Free Trade Area opening up two-way trade in goods between the EU and Jordan. In July 2016, the EU and Jordan agreed to make the rules of origin that Jordanian exporters use in their trade with the EU more flexible. Both sides reviewed and improved this initiative in December 2018. The EU is Jordan's first trading partner, accounting for 17.1% (in value terms) of Jordan's total trade in 2018. Jordanian goods exports to the EU amounted to EUR 300 million in 2018 while goods imports from the EU amounted to EUR 3.6 billion (in value terms).

The EU is also an important source of assistance to the reform process in Jordan. The EU has already disbursed to Jordan EUR 380 million in the context of two MFA programmes implemented over the period 2015-2019. Since the onset of the Syrian conflict in 2011, the EU has extended around EUR 2.1 billion to Jordan under different instruments. In addition, the EIB has signed projects of EUR 486 million and the EBRD has signed projects of EUR 1.3 billion in the same period to support infrastructure development and private sector activity, among others.

⁴ A more detailed assessment of the compliance with this criterion, provided by the European External Action Service (EEAS), is reproduced in the Annex of this Staff Working Document.

5.3. Complementarity

The proposed MFA would complement and add value to the assistance to the country provided by other multilateral donors in the context of the IMF-led economic programme as well by the EU itself, through external financial instruments under the current multiannual financial framework for 2014-2020. By supporting the adoption by the Jordanian authorities of an appropriate framework for macro-economic policy and structural reforms, the EU's MFA would enhance the added value of the overall EU involvement, increasing the effectiveness of the EU's intervention including through other financial instruments. The proposed MFA would also contribute to the EU's leverage on policy making in Jordan by helping the country reduce economic vulnerabilities and promote higher and more inclusive economic growth.

5.4. Conditionality

Disbursements under the proposed MFA operation would be conditional on successful reviews under the **IMF programme** and on the effective drawing by Jordan on IMF funds, as well as on the fulfilment of the political preconditions. In addition, the Commission – on behalf of the EU – and the Jordanian authorities would agree on a **specific set of structural reform measures, to be defined in a Memorandum of Understanding**. These reform measures would support the authorities' reform agenda and complement the programmes agreed with the IMF, the World Bank and other donors, as well as those strategies and reforms supported through the EU's budget support operations. They would be consistent with the main economic reform priorities agreed between the EU and Jordan in the context of the Association Agreement and the Partnership Priorities.

Paying attention in particular to the Five-Year Reform and Growth and reform Matrix elaborated by the Jordanian government with assistance from the World Bank (see Section 1.5), possible areas of conditionality could include: economic governance, including PFM and tax administration; the utility sector; labour market and business environment reforms; social policy and social cohesion. Specific attention will be put on the coordination and alignment of those conditions with EU and other financial institutions in order to maximise the leveraging effect of EU assistance and the impact of international support to Jordan.

5.5. Financial Discipline

The planned assistance would be provided in the form of a loan and should be financed through a borrowing operation that the Commission will conduct on behalf of the EU. The budgetary costs of the assistance will correspond to the provisioning, at a rate of 9%, of the amounts disbursed in the guarantee fund for external lending of the EU, from budget line 01 03 06 ("Provisioning of the Guarantee Fund"). Assuming that the first loan disbursement will be made in the second quarter of 2020, the second loan instalment in the fourth quarter of 2020 and the third loan instalment in the second quarter of 2021 for a total amount of EUR 500 million, and according to the rules governing the guarantee fund mechanism, the **provisioning of the loan will take place in the budgets for 2022 (for EUR 27 million) and 2023 (EUR 18 million)**.

Based on current projections on the utilisation of the budget line 01 03 06, the Commission assesses that the budgetary impact of the proposed MFA operation for Jordan can be accommodated.

In line with the requirements of the Financial Regulation, the European Commission services would carry out in the first quarter of 2020, as noted, an Operational Assessment of the financial and administrative circuits of Jordan. Developments in this area will continue to be

closely monitored also through the regular assessment of PFM reforms by the EU Delegation in Amman.

6. EVALUATION AND COST-EFFECTIVENESS

This assistance is of exceptional and macro-economic nature and its evaluation will be undertaken in line with the standard Commission procedures.

6.1. Evaluation

Ex-post evaluations of MFA operations are foreseen in the Multi-Annual Evaluation Programme of the Commission's Directorate-General for Economic and Financial Affairs. An ex-post evaluation of the proposed MFA to Jordan will be launched within a period of two years after the completion of the operation. A provision for the ex-post evaluation is included in the proposed Decision for the assistance, and will also be included in the Memorandum of Understanding. Budget appropriations from the MFA budget line will be used for this evaluation.

6.2. Achieving cost-effectiveness

The proposed assistance would entail a high degree of cost-effectiveness for several reasons:

- (i) First, since the assistance would be leveraged by that provided by the international financial institutions, with which, as noted, it would be closely coordinated, its ultimate impact could be very significant compared to its cost. Moreover, in negotiating specific policy conditions, the Commission will be able to draw on the expertise of those institutions, including the IMF and the World Bank, and to influence their conditionality as well in ways that will take into account the EU's views.
- (ii) Second, providing a coordinated macro-economic support to Jordan on behalf of the EU countries, the MFA would be more cost efficient than the provision of a similar total amount of financial support by EU Member States individually.
- (iii) Third, all of the assistance would be provided in the form of loans, through which scarce budgetary funds are effectively leveraged, thus enhancing the impact of the EU budget.
- (iv) In addition, the Commission will aim to achieve synergies with other EU policies and instruments used to support the implementation by the beneficiary of the relevant measures (notably in the area of public finance management).

EUROPEAN EXTERNAL ACTION SERVICE



Brussels, 11 July 2019
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Assessment of Democracy, Human Rights, the Rule of Law and Political Reforms in Jordan

Jordan has continued its political reform efforts to strengthen parliamentary democracy and the rule of law. The country maintains its commitment to improve the general human rights situation, and has recorded legislative improvements notably as regards the independence of the judiciary and women's rights. A new reform-oriented government under the leadership of Omar al-Razzaz was appointed on 5 June 2018.

Political reform continues despite daunting challenges

Jordan has continued its political and economic reform efforts against the background of persistent political, economic and social challenges.

The instability in the region pressed the authorities to maintain a strong focus on the stability of the political system. The deteriorating economic conditions (high youth unemployment, decrease of investments and trade resulting from the regional context) pose a threat to social cohesion, risk increasing the attractiveness of extremist ideology and terrorist activities, and as such also reinforced the authorities' priority goal to ensure domestic stability. As a result, the country's efforts to further democratise and strengthen the protection of human rights largely continued to take a backseat. The challenge remains for Jordan to pursue a significant reform path and enhance an open and inclusive society.

On the human rights front, specifically, Jordan has recorded legislative improvements as regards the independence of the judiciary and women's rights. The 31st session of the UN Universal Periodic Review (UPR) in November was an occasion for Jordan to reiterate its commitment to uphold human rights standards, and the EU recognised the progress made and commended the efforts to improve the general human rights situation in the country. Nevertheless, challenges remain, especially in the areas of gender-based violence and gender equality, fundamental freedoms, death penalty, torture and child protection. The erosion of the space for freedom of expression and association, in particular, has continued. Civil society actors are increasingly concerned by anti-terrorist legislation potentially limiting fundamental freedoms, the growing number of reported cases of torture and mistreatment in detention and more generally by their diminishing public space. Restricted freedom of expression has also been noted in the media.

Despite this challenging context, the goal to gradually reform the system is broadly shared across the political spectrum. Significant legislation has been adopted, which needs to be implemented. Since taking office in June 2018, Prime Minister Razzaz has relaunched the reform process. No significant changes are expected in the short term to the current institutional system in Jordan and the process of political reform will need to be pursued to strengthen the legislative and judiciary power branches and enhance their independence. On the individual rights front, further steps are necessary to ensure access to justice and the right to a fair trial, prohibition of torture and women's rights. Economic and political empowerment of youth and women will be essential to enhance stability and democracy in the country. EU financial support is oriented amongst others towards enhancing democratic governance in Jordan, through institutional support as well as through support of democratic stakeholders.

Overall, Jordan's progress in enhancing its democratic governance and strengthening the rule of law under substantial challenges, represents an important case, in particular when compared with other countries in the region.

EU-Jordan Relations

The EU and Jordan enjoy excellent relations and have been linked by an Association Agreement since 2002 (advanced status since 2010).

The EU and Jordan are allies in international politics (e.g. International Syria Support Group, Middle East Peace Process) and have largely congruent views on the root causes of and responses to regional and global crises. For instance, the King of Jordan has been an advocate for a tolerant society and inter-religious and inter-cultural dialogue (Aqaba Process). Jordan has concluded a peace treaty with Israel (1994). Jordan has played an active role on the multilateral and regional front (e.g. Union for the Mediterranean co-presidency with the EU since 2012).

Overall, the excellent EU-Jordan relations have been symbolised by a number of highest-level meetings during the past year. The King visited Brussels in December 2018, and met with the HRVP and the Commission and Council Presidents. Numerous EU high-level visits to Jordan recently took place (HRVP, Commissioner for European Neighbourhood Policy and Enlargement Negotiations, Commissioner for Humanitarian Aid and Crisis Management and the EUMC Chair). Furthermore, the King met the HRVP on a side meeting of the Arab League summit in April 2019, and the President of the Commission in the margins of the Christchurch Call to Action Summit in Paris in May 2019. The **EU-Jordan Association Council** held in Luxembourg on 17 June 2019 further confirmed the strong and solid partnership between the EU and Jordan.

The high intensity of contacts reflects both:

- (i) The mutual commitment to further strengthen the EU-Jordan partnership, going beyond the humanitarian and development domain (e.g. security, mobility, trade);
- (ii) The high expectations from Jordan's side that the EU will continue to sustain its financial support to Jordan, notably in view of the impact of the refugee crisis. Following a request from Jordan, further flexibilities to the relaxation of the Rules of Origin scheme were approved at the 4 December 2018 meeting of the Association Committee.

The EU and Jordan have extended until the end of 2020 their Partnership Priorities, which cover political dialogue and assistance across a range of areas: security including counter-terrorism; trade; bilateral assistance in support of economic stability and development, job creation, quality education; democratisation, the rule of law and human rights.

An EU Electoral follow-up Mission (EfM) visited Jordan in September 2018 to assess the implementation of the recommendations of the EU Election Observation Mission (EOM) fielded on the occasion of the 2016 parliamentary elections, and the opportunities and challenges facing Jordan in improving the rule of law and elections procedures. The EfM noted some progress in implementation of the EOM recommendations and encouraged Jordan to take further steps in this regard.

In sum, while major political, security, economic and social challenges remain, Jordan has made progress towards a more effective democratic political system based on the rule of law and respect for human rights. The EU is fully committed to supporting Jordan in this challenging transition process. In this context, the political preconditions for Macro-Financial Assistance may be considered to be satisfied.