PROGRAM INFORMATION DOCUMENT (PID)
CONCEPT STAGE

April 8, 2015

Report No.: AB7713

Operation Name	JORDAN - Energy/Water Sector Reforms Development Policy Loan
Region	Middle East and North Africa
Global Practice Department	Energy and Extractives
Country	Jordan
Sector	General energy sector (65%); General water, sanitation and flood protection sector (35%)
Operation ID	P154299
Lending Instrument	Development Policy Lending
Borrower(s)	Hashemite Kingdom of Jordan
Implementing Agency	
Date PID Prepared	April 8, 2015
Estimated Date of Appraisal	
Estimated Date of Board Approval	August 25, 2015
Corporate Review Decision	Following the corporate review, the decision was taken to proceed with the preparation of the operation.

I. Key development issues and rationale for Bank involvement

1. The proposed operation in the amount of US$ 200 million - the first in a programmatic series of two Development Policy Loans (DPLs - aims to support fiscal and policy reform programs undertaken by the Government of Jordan (GoJ) in the energy and water sectors. The policy program supported by the proposed DPL is necessary for improving the fiscal position of the Government and laying the groundwork for implementation of short and medium term efficiency gains to promote the long term sustainability of these sectors. The proposed DPL series will address key sector issues and mitigate risks identified by the Jordan Systematic Country Diagnostic, under preparation, and promote economic growth, fiscal balance and private sector development.

2. Two successive external shocks—the global recession and the regional turmoil that followed the Arab Spring—have exacerbated Jordan's long-term structural vulnerabilities. Following the global financial downturn of 2008, growth decelerated sharply in Jordan. Turmoil throughout the region further undermined Jordan's outlook, which led to (i) slower growth and lower fiscal revenues, and (ii) initially, increased public spending to partly accommodate social pressures. This has resulted in an accumulation of a large public debt whose servicing exacerbates the fiscal strain. In particular, interruptions in Egyptian natural gas supply, which in 2009 fueled about 90 percent of Jordan's power generation, forced the country to increasingly rely on more expensive and less efficient diesel and heavy fuel oil during a time of high oil prices. The GoJ's initial decision not to pass-through the higher fuel costs to final consumers resulted in a significant increase in the National Electricity Power Company's (NEPCO) operating losses. As a result, NEPCO has been running deficits of around 4-5 percent of GDP per year since 2011 and

accumulated total operating losses of about US$ 6.44 billion, for which debt servicing has been directly covered by the budget. As a result, gross public debt has risen rapidly and is estimated to have reached around 90 percent of GDP at the end of 2014. Further budgetary losses equivalent to 1 percent of GDP were added in [2012] by the water sector because of limited cost recovery in the sector and increasing dependence on high cost technologies to make water available.

3. The Government consequently has embarked on a major program aimed at strengthening its macroeconomic framework. Recent policy adjustments within the framework of the IMF Standby Arrangement (SBA)[1] and the Bank's closing Programmatic Development Policy Loan have already achieved a significant reconfiguration of fiscal policies, improvements in the business climate, and a broadening of the revenue base. The unsustainable large cost of energy subsidies has also led the Government to embark on a major subsidy reform program supported by the IMF SBA which in November 2012 completely eliminated subsidies on petroleum products except for Liquefied Petroleum Gas (LPG) cylinders mainly used for household cooking. The Government is also implementing a five year electricity tariff adjustment plan that aims to enable NEPCO to recover its operational costs by 2017. In order to promote energy security, Government is also seeking to diversify its energy sources through scaling up renewable energy and developing a Liquefied Natural Gas (LNG) terminal in Aqaba planned for completion in 2015. In addition, the Government is implementing a water sector strategy that aims to achieve operation and maintenance cost recovery by 2020 by strengthening operational efficiency in the water sector. This will be achieved through a combination of revenue increases and cost reductions (the latter mostly brought about by improving the utilization of water resources and the implementation of an energy savings program).

4. Despite the IMF-supported program addressing fiscal pressures caused by the energy and water sectors and the likely positive impact of falling oil prices on government's deficit, it is more critical for Jordan to implement broader policy and structural reforms to sustain Government's efforts. The economy in Jordan is expected to grow at about 3 percent annually, which will increase electricity and water demand at average annual rates of 6 and 5 percent respectively, and put further stress on public resources if underlying fundamental stress factors in these sectors are not addressed. To that end, key elements of the Government efforts focus on restoration of the financial viability of sector utilities, in particular NEPCO - the backbone of the electricity sector - and on improving the operational performance of the energy and water sectors through efficiency gains. Government also seeks to reduce the cost of electricity and water supplies, which would yield significant savings in system operations and therefore reduce the fiscal burden on Jordan's public resources.

5. Therefore, the overall objective of this proposed programmatic Development Policy Loan (DPL) is to support fiscal and policy reform programs undertaken by the Government of Jordan (GoJ) in the energy and water sectors. The policy program supported by the proposed DPL is necessary for improving the fiscal position of the Government and laying the groundwork for implementation of short and medium term efficiency gains to promote the long term sustainability of these sectors. The proposed DPL series will address key sector issues and mitigate risks

[1] The IMF SBA was approved by the IMF board in August 2, 2012 in the amount of SDR 1,364 million (about $2 billion)

identified by the Jordan Systematic Country Diagnostic, under preparation, and promote economic growth, fiscal balance and private sector development.

II. Proposed Objective(s)

6. The program development objective of the proposed DPL is to support the improvement of financial viability and increase efficiency gains in the energy and water sectors in Jordan

III. Preliminary Description

7. The DPL policy program will be structured under two main pillars: *Pillar A: improving the financial viability of the electricity and water sectors; and Pillar B: increasing efficiency gains in the energy and water sectors*. The first pillar will support Government's plan to bring the water and energy sectors to sustainable cost recovery and efforts to restore NEPCO's creditworthiness by addressing its accumulated debt which will allow improve the financial standing of NEPCO in financing its own investments in system maintenance and expansion. The second pillar will support Government's programs that aim to strengthen efficiency gains both in the supply and demand sides of the energy and water sectors through deeper diversification to more economic fuel supply resources and power generation mix, scale up of energy efficiency programs, and efficient utilization of water resources.

IV. Poverty and Social Impacts and Environment Aspects

Poverty and Social Impacts

8. The policies and programs supported by the DPO may have a negative impact on the poor and vulnerable. The policy actions are made up of those actions aimed to improve the financial viability of the sector through increases in the electricity and water tariffs that will increase the cost of the service for consumers. The Government is however mitigating impact of electricity prices on the poor and vulnerable by limiting price increases to household consumption above 600 KWh. The water tariff restructuring in 2011 has also left the sector with a tariff structure that allows for the price impact to be mostly felt by residential users who use large quantities of water, or non-residential users. During the preparation of the proposed DPL, simulations will however be carried out to assess potential poverty impact of electricity and water tariff adjustments supported by the DPL and assess potential mitigation measures in case of a possible impact on the poor and vulnerable consumers. The results of such simulation will be considered in the final design of the policy program supported by the DPL. Further, the Government was able to mitigate the effect of the 2012 fuel subsidy reform by introducing the Fuel Cash Compensation Program applied earlier during periods of high oil prices. Therefore, in the context of electricity and water tariff increase, the Government could also use the same compensation mechanism to mitigate any impact of electricity and water price increases on poor and vulnerable consumers.

Environment Aspects

9. The implementation of the policy actions supported by the proposed DPL is not likely to have significant impact on environment, forests, and natural resources. The tariff reform programs supported under Pillar A that aim to improve the financial viability of the electricity and water sectors, will help in curbing the growth in energy and water demand resulting in less environmental degradation. Similarly, efficiency gains programs under Pillar B promoting growth in renewable energy and energy efficiency development and deeper utilization of natural gas in power

generation instead of the more polluting fuel oil will also produce significant environment benefits and reduced carbon emissions. In Jordan, project development should be in compliance with country environmental and social requirements and best international experience. Detailed Environmental Impact Assessment must also be developed by the project owner and approved by the Ministry of Environment before the start of the project implementation.

V. Tentative financing

Source:		($m.)
Borrower		0
International Bank for Reconstruction and Development		200
Borrower/Recipient		
IBRD		
Others (specify)		
	Total	**200**

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