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Jordan's Economy at a Crossroads

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For decades, Jordan has displayed remarkable economic stability. Through serious challenges—the Syrian Civil War, the Arab Spring, and simmering demographic tensions—the country has survived without serious economic or political disruptions. Yet, in May and June, the Kingdom saw massive protests, some of the largest in its history, as tens of thousands of protestors took to the streets to oppose government corruption, proposed tax increases, and staple goods subsidy cuts.[1] This was a series of protests driven by well-educated, middle class, young Jordanians fearful that government economic reforms would endanger their livelihoods.[2]

While the resignation of the prime minister and foreign aid from Saudi Arabia and its allies have since temporarily quieted economic concerns, the Hashemite Kingdom's economic challenges will reemerge. Though the Kingdom is attempting to follow an international reform plan, and has additional programs of its own, King Abdullah II and the Jordanian leadership are facing a suffocating confluence of international influences and internal pressures. Both public unrest and demographic difficulties threaten the ability to impose long- or short-term reforms. These economic challenges are revealing that Jordan's economic stability is dependent on massive government deficits buoyed by fickle foreign aid. In the long run, the Kingdom needs to undergo economic reforms that unleash the private sector, stabilize government finances, and create jobs to meet the demands of a growing population.

While the Jordanian economy has not collapsed under the unrest caused by the Arab Spring, slowdown in global economic growth, or spillover from the Syrian Civil War, it is experiencing extraordinarily sluggish growth. According to the World Bank, 2017 GDP growth was around two percent.[3] This is nowhere near the sufficient level needed to provide work and prosperity to the Kingdom's young and rapidly-growing population. In fact, by the end of 2017, unemployment was 18.5 percent, and the labor force participation rate was just over 38 percent. This problem is only going to grow more severe, as over a third of the population is under the age of 14.[4] It will then be compounded if the Syrian Civil War worsens or reaches a stalemate that does not allow the well over one million Syrian refugees in Jordan to return. Civil unrest will only worsen, especially as the number of young people without jobs grows, unless Jordan can undergo structural changes to increase long term growth.

Slow growth and the threat of rising unemployment are further exacerbated by Jordan's soaring levels of government debt. Largely due to excessive government spending, as well as decreases in foreign aid, the Syrian Civil War, and the management and absorption of Syrian refugees, Jordan's debt-to-GDP ratio is now about 96 percent, compared to about 61 percent in 2010.[5] This led the country to seek assistance, and, on August 24, 2016, the International Monetary Fund approved a three-year arrangement under which it loaned Jordan $723 million to support financial and economic reform.[6] As part of the program adopted under this agreement, the government is attempting to decrease its deficit and halt the increasing debt-to-GDP ratio. That is why it proposed an income tax increase and a cut to subsidies on bread and other staples.[7]

Maneuvers to improve the government's fiscal health are critical. For example, the high government debt level has begun to crowd out private sector investment by decreasing available credit and raising interest rates.[8] Though the removal of the original government in the wake of the protests paused these reforms, they will need to be resumed, in some form, if the country is to continue with its IMF plan and to develop healthier finances.

There are some reasons to be hopeful. The country is not in recession, so the government has some flexibility to make the necessary reforms for long-term growth. The track record of economic stability, even during this period of high debt, is important. Except for a brief period of deflation before 2016, due to low global oil prices, inflation has stayed relatively constant at under five percent for years.[9]

This history is important evidence that the government will not pressure the Central Bank of Jordan into using seigniorage—printing excess money to pay for government expenditures to close the deficit. Seigniorage can devastate an economy, as the excess money causes inflation. At its worst, it can trigger Zimbabwe-esque hyperinflation, but even at more moderate levels it can raise inflation to problematic levels. Both Egypt and Syria have used seigniorage in the past decade to fund government expenditures, triggering high levels of inflation.[10] In fact, Egypt has been unable to get inflation below 10 percent due to its use of seigniorage.[11] The Central Bank of Jordan has been able to resist this sort of pressure before: a former central bank chief said in 2011 that he successfully thwarted government efforts to print money to pay civil servants. Such temptations must continue to be resisted if the country is to avoid high inflation.[12]

Other macroeconomic elements are positive as well. The country has maintained its currency, the Jordanian dinar, pegged to the United States dollar.[13] Maintaining such a peg in the presence of seigniorage is typically extremely challenging, and it also facilitates easier international trade and improves stability for international investors, critical for building a prosperous private sector.

The challenges emerge in the fiscal realm. A critical component of the government's success at maintaining economic stability has been public programs and services. Spending on government services in the country is enormous, and public expenditure encompasses a sizeable portion of the economy. Official figures put government spending at around 30 percent of GDP, an amount similar or less than developed economies.[14] Yet when other public entities, like the Central Bank, Social Security Corporation, and independent government agencies, are included, this figure rises to over 50 percent of GDP.[15] According to a Jordanian government agency report from the Economic and Social Council, the Kingdom has the largest public sector in the world compared to its population, and it is one mired in inefficiency and corruption.[16]

The rampant corruption undermines public trust in the government and further erodes any potential popular support for tax increases to maintain government spending. Wasta, as it is called in Jordan, is a form of nepotistic corruption that is rampant throughout the public sector. One a government official told a newspaper that cronyism, nepotism, and patronage are ruining the potential of the public sector to run effectively and efficiently.[17] Indeed, a major demand of protestors was accountability for corruption.[18] Furthermore, the government's finances are opaque, with a Jordanian professor in the US saying, "We as Jordanian citizens are discouraged from discussing these things and [are] sometimes criminalised."[19]

Meanwhile, Jordan's private sector is not seeing the success it needs, as evidenced by the Kingdom's poor GDP growth. The fastest growing sector of the economy is agriculture, which grew at around 16 percent in 2015, yet it employs only around two percent of Jordanians. Manufacturing, which employs approximately 10 percent of the country, according to government data, grew in 2015 at just around six percent, two percent less than its growth rate of the previous five years.[20] Indeed, the sectors experiencing the fastest growing wages from 2010 to 2016 were the agricultural, governmental and public administration sectors.[21] Yet while the World Bank, Jordanian government, and IMF say they are looking to the private sector to lead growth, they were preparing to raise already high corporate taxes.[22]

The proposed tax law that helped spark this year's protests would raise the corporate tax rate on financial institutions and insurance companies from 30 percent to 40 percent, and it would raise taxes on the mining industry from 24 percent to 30 percent.[23] For context, only two countries, the United States and the United Arab Emirates, have their top marginal corporate tax rates above 35 percent.[24] Using staggeringly high taxes to fund government spending will ultimately only stifle the ability of the private sector to grow and serve as a job creation engine.

While austerity measures cutting expected public programs are challenging in any country, the critical reason Jordan is not attempting any significant reevaluation of government programs is its fragile demographic makeup. The IMF is pessimistic about any attempt to cut government spending, writing that “There is no significant room to cut public spending without increasing unemployment or resorting to other cuts that would lower government’s ability to spend more on education, health, and domestic security.”[25]

This contention is not completely accurate. Real reform could shift the Kingdom to a vibrant economy driven by the private sector. Yet it currently functions on an economic model that sees it funneling massive subsidies toward vital goods and to public sector employment. The government spends massively on its military, almost five percent of GDP, and it plans on increasing this expenditure by almost $500 million this year.[26] It heavily subsidizes electricity, and accumulated energy debt peaked at 17.8 percent of GDP, although this has fallen slightly in recent years.[27] These areas, and others, would seem ripe for spending cuts. Nevertheless, the IMF notes, “Based on discussions with the Jordanian government over the past two years, it was agreed that other measures [besides tax increases] would be more difficult to implement and costly in terms of growth and social impact.”[28] This now insinuates the truth: the decision to avoid public sector austerity is primarily for social, not economic, concerns.

The social demographics of the Kingdom are complex. Jordan’s population of 10.2 million, over two million of whom are refugees without citizenship, is growing at around two percent annually, and it is mostly divided between two groups: East Bank Jordanians, who are originally from the East Bank of the Jordan River, and Palestinians, some of whom lack citizenship.[29] Although an estimated 55-70 percent of Jordanians are of Palestinian origin, the King relies on the support of powerful East Bank tribal leaders.[30] There are deep social, economic, and political divides between the two groups.

Palestinians dominate the business elite and economic hierarchy, though there are more than a million, often-impoverished Palestinian refugees, as well. East Bank Jordanians have been less successful in the business world on the whole, but they dominate the political elite.[31] Palestinians generally cannot work in the military or in public security, and they have very limited employment opportunities in other public sectors.[32] Employment in the civil service and public sector is then very important for the East Bank Jordanians, and for King Abdullah to retain their support.

Perhaps surprisingly, the protests in Jordan calling for political reform during the Arab Spring in 2011 and 2012 were led by East Bank Jordanians, not Palestinians. They were focused on economic, political, and social reform, with special emphasis placed on the perceived unfairness of the economic gap between the wealthier Palestinians and poorer East Bank Jordanians. Palestinians generally were much less involved, owing both to a greater fear of government retribution and an understanding that a motivating factor was anger over Palestinian wealth.[33]

Given this history of East Bank Jordanian willingness to protest, especially over economic discontent, as well as the King's reliance on the loyalty of tribal leaders, it is immensely important for the government to preserve stability by placating the East Bank Jordanians. Yet King Abdullah must know that while these recent protests were relatively restrained, he may still yet lose his critical tribal support if prosperity is lost. According to a Jordanian journalist, Osama Al-Sharif, "Jordan's young men and women have now dispersed. But they are still out there—watching the new government's every move."[34]

These dynamics are now reaching a tipping point. It is clear, from Jordan's growing government debt and need to take an IMF loan, that its status quo government policies are unstable. But the Kingdom is resisting taking difficult steps to shrink the size of the government because doing so risks angering East Bank Jordanians and potentially destabilizing the delicate social balance in the Kingdom. Simultaneously, the IMF reform plan of higher taxes and limited subsidy cuts has triggered massive protests that were only quelled by the resignation of the government. Together, the bloated public sector and the volatile social situation make it very challenging for any reform to succeed.

***There is another piece of this story, which is the important element of international and regional involvement in the Kingdom. The next edition of Iqtisadi will examine the Kingdom's foreign grants, the impact of the Syrian Civil War, as well as evaluate its reform plans and potential for success.

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