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BHUTAN

Country Snapshot

The World Bank Group



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ECONOMIC OVERVIEW

Table 1

	2015
Population, million	0.8
GDP, current US\$ billion	2.0
GDP per capita, current US\$	2,532
Poverty rate (\$1.9/day 2011 PPP terms)a	2.2
Poverty rate (\$3.1/day 2011 PPP terms)a	13.5
Gini Coefficient a	0.4
School enrollment, primary (% gross) b	102
Life Expectancy at birth, years b	69

Sources: National Statistics Bureau, Bhutan, World Development Indicators 2016.
Notes: a/ most recent value (2012), b/ 2014

Bhutan has maintained solid macroeconomic performance in the first half of 2016. Large ongoing investments in hydropower projects, supportive fiscal and monetary policy have been contributing to the growth momentum. The single-digit inflation, relatively stable exchange rate and accumulating international reserves attest to a stable macroeconomic environment. Rapid growth in a relatively calm macroeconomic context is likely to continue for the next few years, which should result in a steady reduction of poverty. However, Bhutan's structural challenges remain: large current account deficits, elevated public debt, an underdeveloped private sector and high youth unemployment rates. To address these challenges, the Royal Government of Bhutan (RGoB) is in the process of revising the Economic Development Policy (EDP) and has started preparatory work on the 12th five-year plan (FYP) which will commence in 2018.

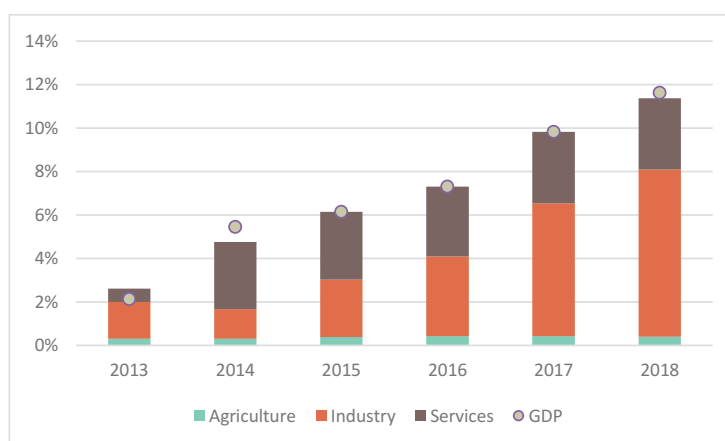
Recent developments

Bhutan's economy has been steadily recovering from the aftermath of the shortage of the Indian Rupee of 2012. GDP growth revived from a low of 2.1 percent in 2013 to about 6 percent (estimated) in 2015. The re-

covery has been sustained by a combination of accelerated investments in hydropower, good agriculture harvests, and supportive fiscal and monetary policy to boost the implementation of five-year-plan. On the demand side, private consumption has been supported by a resumption of credit (20 percent y/y as of June 2016), with services, automobiles and personal loans showing strong growth. Investments remained robust in hydropower through construction and services. The improved growth performance has been accompanied with macroeconomic stability. Inflation has been below 5 percent, exchange rate has marginally depreciated, and international reserves covered 11 months of goods and services imports in the first half of 2016. Although there have been high current account deficits (higher than 25 percent of GDP), these are related to hydropower projects and thus are mostly financed by loans from India.

In 2012, Bhutan reduced extreme poverty to 2 percent, measured by the international poverty line of US\$1.90 a day (PPP). This is among the lowest rate in the South Asia region and substantially lower than the regional poverty rate of 19 percent. Even using a higher international poverty line of US\$3.10 a day, Bhutan still shows an impressive poverty reduction from 29 percent in 2007 to 13 percent in 2012. During the same period, expenditures of households at the bottom 40 percent of the distribution grew virtually at the same rate as the overall average and the income share held by the

Figure 1: Bhutan / GDP growth



Source: National Statistics Bureau, World Bank

bottom 40 percent of the population remained at 17 percent. Equally impressive improvements have been made in access to basic services and asset ownership. The Gross National Happiness Survey, Bhutan's unique measure of economic, social and spiritual development, showed further improvements in 2015. Ninety-eight percent of the households own mobile phones and 99 percent have access to electricity. The overall unemployment rate fell from an already low level of 2.9 percent in 2013 to 2.5 percent in 2015. However, youth unemployment rate exceeds 10 percent.

Outlook

Growth is expected to accelerate in 2016-2018 period. Construction will start at three hydro-power projects in the next three years and two hydropower dams will become operational in 2018. Macroeconomic stability would allow fiscal and monetary policy flexibility to keep supporting economic activities. Given the close economic

relationship with its southern neighbor, a positive economic outlook in India will also help Bhutan's growth to accelerate. Low global commodity prices and the pegged exchange rate against the Indian Rupee are expected to anchor a stable inflation rate. While high current deficits are likely to continue due to imports associated with hydropower constructions, these are expected to be covered by secured financing sources. Projections based on GDP growth indicate steady and continuous poverty reduction since 2012, the last year for which survey-based estimates are available. Poverty headcount rate is projected to fall to 10.9 percent by 2015 and 6.0 percent by 2018 at the US\$3.10 a day line.

Risk and Challenges

The construction and commissioning of hydro-power projects is likely to stimulate domestic demand, which would result in additional pressure on the overall balance of payments. To mea-

TABLE 2: BHUTAN / MACRO POVERTY OUTLOOK INDICATORS (ANNUAL PERCENT CHANGE UNLESS INDICATED OTHERWISE)

	2013 a	2014 a	2015 e	2016 f	2017 f	2018 f
Real GDP growth, at constant market prices	2.1	5.5	6.1	7.3	9.8	11.6
Private Consumption	13.1	18.0	7.1	7.5	7.0	6.5
Government Consumption	-10.1	2.4	10.1	5.4	1.8	0.2
Gross Capital Investment	-35.7	38.3	6.1	11.7	11.0	13.5
Exports, Goods and Services	3.9	-6.0	-0.2	-2.0	6.0	8.0
Imports, Goods and Services	-1.8	-3.5	4.3	5.5	3.2	3.3
Real GDP growth, at constant factor market prices	2.1	5.5	6.1	7.3	9.8	11.6
Agriculture	2.4	2.4	3.0	3.4	3.5	3.6
Industry	3.9	3.1	6.1	8.5	14.0	17.0
Services	1.6	8.2	8.1	8.2	8.3	8.4
Inflation (Consumer Price Index)	8.8	8.3	5.2	4.6	4.3	4.0
Current Account Balance (% GDP)	-23.1	-24.6	-30.0	-29.4	-23.7	-15.7
Fiscal Balance (% GDP)	-0.2	2.7	-0.7	-4.2	-3.0	4.1
Debt (% GDP)	98.1	96.4	98.2	102.1	103.2	97.7
Primary Balance (% GDP)	2.0	4.4	0.8	-2.8	-1.9	6.2
Poverty Rate (\$1.9/day PPP terms) a,b,c	2.1	2.1	1.9	1.7	1.3	0.9
Poverty Rate (\$3.1/day PPP terms) a,b,c	13.2	12.4	10.9	10.5	8.5	6.0

Source: World Bank, Macroeconomics and Fiscal Management Global Practice, and Poverty Global Practice

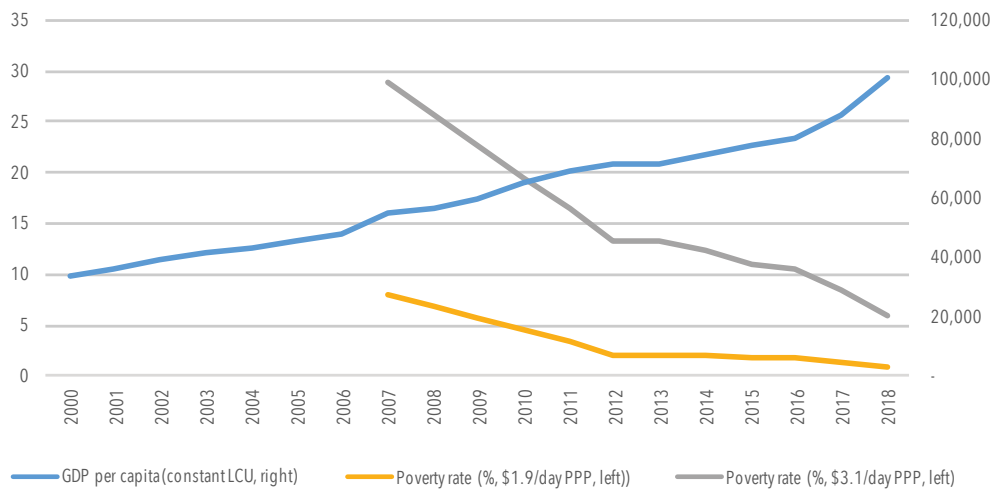
Notes: e=estimate, f=forecast

(a) Calculations based on SARMD harmonization, using 2012-BLSS

(b) Projection using natural distribution (2012) with pass-through =0.7 based on GDP per capita constant PPP

(c) Projections are from 2013 to 2018

Figure 2: Bhutan / Actual and estimated poverty rates and GDP per capita (PPP)



Source: World Bank (see notes to table 2).

sure these risks, credit growth and international reserves will have to be carefully monitored. Increasing foreign direct investment (FDI) and remittance will be more important to finance the current account deficits. The impact of the slowdown of the global economy on Bhutan's economy is expected to be modest due to the country's limited linkage with the rest of the world other than India. Nevertheless, deceleration of the global economy will be felt through its effect on the Indian economy or the tourism sector. The latest debt sustainability analysis (DSA) in mid-2016 concluded that Bhutan's external debt risk is moderate, as much of the external debt is linked to the India hydropower project loans. Besides the challenges related to hydropower, a large current account deficit, underdeveloped private sector and high youth unemployment are the other major challenges. The implementation of the new Economic Development Policy (EDP) is expected to improve the business climate, which in turn would expect to create jobs especially for youth. Bhutan remains largely rural, with an estimated 61 percent of population living in rural areas in 2015. The urban-rural gap is evident in many areas, including poverty, food security and access to services. While poverty incidence is low, urban areas face a higher unemployment rate (6.3 percent) than rural areas (1.0 percent). Youth unemployment in urban areas is high and increasing: 21 percent in 2010, 23 percent in 2013 and 28 percent in 2015. Long lines for those seeking public sector

employment and a scarcity of high-paying jobs for urban youth reflect a supply and demand gap in the labor market. The country is therefore in urgent need of private sector development to diversify its economy, building on the foundation created by the hydropower industry. The development of the private sector will also help curtail its urban youth unemployment

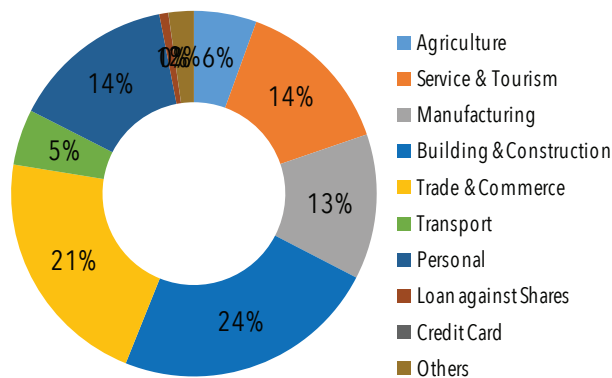
RECENT SECTOR DEVELOPMENTS

Monetary and financial sectors

The financial sector and the regulator's supervisory capacity need to be developed. Following the external imbalances with India in 2012



Figure 2: Credit distribution (as of May 2016)



and rising pressures on the demand for Indian Rupees (INR), the Royal Monetary Authority (RMA) temporarily suspended access to INR to finance imports of vehicles and construction materials. These restriction were lifted in 2014, but credit quality appears to have been adversely impacted. The financial sector and the RMA's supervisory capacity are underdeveloped, majority of the transactions are cash backed, there is a lack of investment avenues, an asset-liability mismatch, and a heavy reliability on traditional (land as property) collateral-based lending. Bhutan has undertaken several measures in 2015 and 2016 to address these weaknesses. A Financial Inclusion Policy has been drafted for adoption and the Macro Prudential Regulations on Disclosure requirement has been implemented. The government has issued Investment Guidelines for Insurance Business, a directive on Abandoned Property, and Credit Information Bureau Regulations. A Financial Sector Development Action Plan (FSDAP) has been developed for approval by the cabinet in 2016.

The liquidity position of Bhutan's banking sector has improved but continues to be volatile, fueled by credit expansion. Liquidity in the financial system has been erratic. The overall Credit-to-Deposit Ratio (CDR) jumped from 59 percent in December 2010 to a range of 82–87 percent between December 2011 and December 2013 and eased to 72 percent in March 2016. Total credit increased by 18 percent (March 2016, year-on-year) mainly driven by strong demand for housing, personal loan and in the trade/commerce sector. Deposits

have increased by 31 percent (March 2016, year-on-year). The Statutory Liquidity Requirement (SLR) of the banks has been comfortably met and surplus liquidity in the system increased to US\$0.27 billion in March 2016 compared to US\$0.15 billion in March 2015. Banks continue to rely heavily on corporate deposits (46 percent of total deposits) as the key source of funding and thus are left with funding their loan portfolios with short term commitments.

There is a need to increase price competition (interest rate), lending to priority sectors, as well as competition for the best customers' government deposits, and long-term deposits. However, compared to the past years of stickiness in interest rates, the financial sector has experienced some movement in interest rates in the past three years following the introduction of "base rate" mechanism (now in its fourth year of implementation) and tight liquidity in the financial system.

Banking sector profitability declined in the first quarter of 2016. While year-end results record profits of Nu 2.8 billion for 2015, a 25 percent increase over the previous year (Nu 2.25 billion), the financial institutions incurred a loss for the first quarter in 2016 owing to an increase in provisions to cover loan losses that resulted from an increase in non-performing loans (NPL). The NPL ratio has increased from 10.2 percent in March 2015 to 11.4 percent in March 2016. As a result, Return on Asset (ROA) deteriorated from -.05 percent in March 2015 to -1.83 percent and Return on Equity (ROE) from -0.27 percent to -0.31 percent during the same period.

Bank credit to the private sector stood at 47.5 percent of GDP as of 2014/15, which is similar to the levels of FY2012/13 (48 percent) and FY2013/14 (47 percent). Credit restrictions were put in place after FY2011/12 to prevent a liquidity crunch. However, the ratio is slightly above the South-Asia Region average of 45.8 percent of GDP.

Bhutan has been gripped by erratic movement in its liquidity position since early 2012. Measures undertaken by RMA were focused on containing rapid credit growth. In terms of credit

concentration, the building/construction (housing), trade/commerce and personal loans make up around 59 percent of the loan portfolio.

The banks continue to face challenges in asset and liability management from balance sheets comprised of traditional forms of lending (fixed rate, medium and long term) and increasingly short term, mobile and individually large deposits. Retail deposits, considered more stable than corporate deposits, account for 54.8 percent in March 2016 compared to 43.5 percent in March 2015. The total financial sector deposits increased by 31.3 percent in March 2016 over March 2015 driven by Demand Deposit and Time Deposit, which grew by 41.2 percent and 19.4 percent respectively. However, the share of short term deposits in the total deposits increased from 54.5 percent in March 2015 to 58.6 percent in March 2016 while the asset side of banks' balance sheet remains dominated by long-term lending. The resulting mismatches have given rise to significant liquidity and interest rate risks in the banking system.

While the capital market activity improved during 2014 and 2015 with various new issues of rights, bonus and off market transactions and new IPO, Bhutan does not have an adequate supply of either longer-term public sector debt (bonds) or short-term T-bills with market-based pricing to reflect demand, market conditions and maturities. The Royal Stock Exchange of Bhutan Limited (RSEBL) established in 1993 is now registered under the Companies Act with brokers holding a 51 percent share, 21 listed companies as of January 2016, a small total market capitalization of US\$0.33 billion (up from US\$0.32 billion previous year, and 62,991 shareholders (slightly up from 62,687 in the previous year). While the secondary market traded volume and value increased by 37 percent and 6 percent respectively in December 2015 over December 2014, there have been virtually no new listings since 2010, and inadequate opportunity to create commission-based income for market participants. Consequently, highest priority is being given to actions that will increase the number and value of listings on the exchange and, hopefully, increase the level of secondary activity. A Capital Market Master Plan, with this objective in mind, was approved in late 2013 but there has been little progress toward its implementation. It called for RSEBL to adopt a 5-year strategy that covers hu-

man resource mobilization, industry participation, feedback loops, monitoring and evaluation, and accountability mechanisms. It is difficult to conduct monetary policy effectively without an adequate supply of Treasury bills (T-bills). The government plans to address this problem by adopting a new public debt policy that will allow for some government borrowing to meet monetary policy and capital market development purposes as well as to meet cash needs.

The World Bank has been supporting the RGoB to develop and implement the Financial Sector Development Action Plan (FSDAP) prepared in the context of Bhutan's Vision 2020 document and the 11th Five Year Plan (2013-2018) objectives and priorities. The FSDAP has been approved by the Royal Monetary Authority (RMA) Board and is expected to be adopted by the Cabinet by the end of September 2016. The FSDAP aims to address key financial sector issues. As Bhutan's future becomes increasingly linked to a globalized world, building and maintaining a sound and effective financial sector is fundamental to achieving satisfactory economic growth with equity which is a main pillar of Gross National Happiness. Among issues in the FSDAP, RMA has requested Bank' assistance in the areas of an organization review of RMA, financial deepening, building capacity in the regulation/supervision of Non-Bank Financial Institutions (insurance and pensions) and strengthening the SME sector.

Poverty and Statistical Capacity Building

Bhutan is a star performer in poverty reduction, with only 12 percent of the population below the national poverty line in 2012, compared to 23 percent in 2007. Bhutan ranks third among least poor



countries in South Asia behind Maldives and Sri Lanka, with only 2.2 percent of the population below the \$1.90 international poverty line in 2012, compared to 8 percent in 2007. This remarkable progress is founded on high per-capita annual GDP growth of 5 percent. Bhutan outpaces comparable countries in poverty reduction in the world.

Bhutan's statistical system has limited human resources, an absence of legal framework, data weaknesses and limited data coordination. However, notable progress has been made in selected areas such as price data collection and dissemination using a map portal. The National Statistics Bureau (NSB) successfully completed the update of the National Statistics Development Strategy (NSDS) in December 2014. The NSB has also successfully switched to Computer-Assisted Personal Interview (CAPI), paperless surveys to improve the efficiency and quality of data collection. The tablets have been used for the collection of Bhutan Labor Force Survey (2014 and 2015), Gross National Happiness Survey (2015) and Enterprise Survey (2015). The World Bank is supporting the implementation of the NSDS and the country move to CAPI-based technology for surveys. It is also the key partner for poverty assessments.

Private Sector

The private sector remains small. While 15-to-24-year-olds represent a fifth of the Bhutanese population, youth unemployment remains relatively high at above 10 percent. Bhutan's private-sector potential is still to be realized, with industry concentrated in ferro-alloys and a few food and beverage manufacturing activities. Subsistence agricul-



ture remains dominant, and the tourism sector is heavily regulated. State-owned enterprises (SOEs) operate in key strategic areas of the economy, including energy, banking, manufacturing, transport, telecommunications, and infrastructure. SOEs contributed 42 percent of government revenues in FY2014/15. There were about 30,000 formal private sector businesses in 2015, of which 99 percent were micro and small. There are about 350 limited liabilities companies (LLC), and a handful of joint-stock companies and partnerships. The remaining businesses are de-facto sole proprietors, with or without employees.

Bhutan has comparative advantages in a number of areas. They include in hydropower, tourism, agribusiness, a stable and low-corruption political environment, a wide-spread knowledge of English, an educated workforce, access to low-cost and reliable electricity, preferential access to the large Indian market, and easy access to skilled and unskilled labor from India. Against these advantages, private-sector development is limited due to the size of the economy, limited access to finance, mismatched skills of the labor force, weak investment climate, and lack of adequate infrastructure.

Despite ongoing reforms, Bhutan's ranking in the ease of doing business remains almost unchanged between 2015 (70th) and 2016 (71th). This suggests that there is room for improving the business climate. Bhutan ranks 105th of 140 countries in the World Economic Forum's Global Competitiveness report, which shares the finding of the World Bank's 2015 Enterprise Surveys that access to finance is the greatest constraint to doing business. Inadequate infrastructure and restrictive labor regulations are the next most commonly cited constraints by executives.

To spur private-sector development, a number of policies and laws have been formulated. They include: the Economic Development Policy (EDP); the FDI policy and rules and regulations; the Renewable Energy Policy; the Micro, Small, and Medium Enterprises (MSME) Policy; the Licensing Policy; the amended Company Act and the Public Private Partnership (PPP) policy. An enterprise registration bill and the Movable and Immovable Property Act Amendments have been approved by Cabinet and are awaiting parliamentary approval. Forthcoming policies and laws include the indus-

trial infrastructure development policy which will govern economic zones, the mineral development policy, and the consumer protection bill. With the support of the World Bank, Bhutan launched its first Information Technology Park in 2012 as a PPP. To improve the business environment, the National Land Commission recently introduced a new computerized land information system connecting the Thromde with the cadaster¹ and the Bhutan Power Corporation improved process efficiency for obtaining electricity connections.

The World Bank is supporting government efforts to further improve the investment climate, through a comprehensive programmatic technical assistance and development policy lending, including in the areas of business registration and land registration (through the introduction of new eGovernance solutions); the usage of movable assets as collaterals through the Central Registry for Secured Transaction; the revision of the Bankruptcy Act; improvements of the existing financial infrastructure, and strengthened legal rights for creditors and borrowers; as well as a strong financial sector development strategy.

Education

Bhutan's education expenditures are strong. Public education expenditure stood at 7.5 percent of GDP and 15.2 percent of total government spending in 2013-2014 (Ministry of Finance, June 2015). These figures are among the highest in the South Asia region. The Constitution (2008) provides for the state to ensure free education up to Grade 10 for all children of school-going age, and to make technical and professional education generally available, and higher education equally accessible to all on the basis of merit. At the same time, this progress has led to a refocus by development partners on other priorities, which may make it difficult to sustain high education spending.

Bhutan has achieved the Millennium Develop-

¹ "Thromde" is a municipality. The National Land Commission has an online land transaction system which was initially introduced for the rural area. The system is capable of processing land transaction in its entirety, along with the cadastral map and scanned copied of the legal documents. Of recent, the NLC has cloned the rural system for the urban as well. The system is currently functional in four Thromdes (municipalities).

ment Goals (MDGs) in education. Bhutan has established and built up an organized public education system since the 1960s. This diversified sector now includes over 650 schools and institutes, more than 180,000 students and nearly 9,000 teachers. Notably, gender parity has been achieved up to Grade 10. Females constitute nearly 50 percent of enrollment in higher secondary education and nearly 40 percent at tertiary level. The gross enrollment ratio was 78 percent at secondary level and 30 percent at tertiary level in 2013.

A key issue is that despite high enrollment and significant levels of public financing, learning levels remain low. Poverty remains key among constraints on enrollment and attendance, as corroborated by data from the Poverty Analyses, demonstrating that Gewogs, where fewer children attend school, tend to be those with comparatively higher poverty rates. This is mainly due to the high out-of-pocket expenditure for households. Sector-wide, the majority of education service delivery is through the public sector. The exception is higher secondary education (HSS, Grades 11-12), where 50 percent of the students are in private institutions. The Royal University of Bhutan is the main reference point for the quality assurance and accreditation framework. The 11th Five Year Plan (FYP-11) expansion targets for tertiary education are ambitious, but essential for Bhutan to build up a human resource base to support a knowledge-based economy. Student intake is to increase to 15,000 (from just over 5,000 currently). To keep this from overburdening public expenditures, a greater role for the private sector is seen, but this raises new issues of quality and relevance.

The World Bank is not directly engaged in the health and education sectors in Bhutan. A recent



World Bank public finance study notes that health and education will be among the fastest growing sectors in Bhutan in terms of needs and demand, and that fruitful partnership with the private sector both for service provision and purchasing need to be explored.

Health

Bhutan has sustained investment in health over the last two decades and made remarkable progress. In FY2014/15, public health expenditures stood at 8.8 percent of the total expenditures, higher than other South Asian countries. The expansion of health facility networks now ensures that 90 percent of the population live within three hours walk of a health facility, there are 25 traditional medicine units at Basic Health Units, and there are more than two functioning ambulances at each district hospital. For the FY2016/17 budget, US\$67.16 million is allocated for the sector.

Access to health services is satisfactory, though still room for improvement. The Constitution provides for free basic public health services to all citizens. As of now, all health services (barring a handful of dental, cosmetic, and other services) continue to be provided by the government for free. Some outreach centers are very remote and require health workers, the unsung heroes of the country's public health system, to endure long walking hours (or even days) prior to reaching the remote facilities. There has been an increase in the demand for traditional medicines. Farmers are encouraged to grow medicinal plants to meet this demand and thereby also, generate additional income.

Although the burden of non-communicable diseases



is growing, the health services continue to spend most of their resources at district level on the traditional infectious diseases such as common cold, diarrhea, skin diseases, and conjunctivitis. In addition, alcoholism remains a significant health challenge. Although there has been progress against malnutrition and stunting in recent years, rates are nevertheless still high. The RGoB finalized the draft of the National Food and Nutrition Security policy during 2012. The final report of the "Nutrition in Bhutan: Situational Analysis and Policy Recommendations" was published in June 2014.

Overall, based on the most recent Gross National Happiness (GNH) survey, the health of the people has improved. The number of healthy days² on an average has increased from 26.2 days in 2010 to 28.4 days in 2015. The government has launched the National Health Promotion Plan and strategy and is in the process of reviewing the Medical and Health Council Act.

Social Protection

In addition to social programs like free health and education services, the RGoB has in recent years introduced a range of social protection programs. Social protection programs include both large universal programs and a few smaller targeted ones. The largest targeted programs are the civil service pensions and the Kidu fund which was set up under the aegis of the Office of the *Gyalpoi Zimpon* (Office for People's Welfare and Wellbeing). Civil society organizations such as Tarayana also provide social services to the elderly, the disabled, the destitute, and other poor or vulnerable groups. About 0.9 percent of Bhutan's GDP is spent on social protection.

Continued effort is needed to expand social protection support. The coverage of social protection provisions ranges from less than 1 percent (entrepreneur support and homes for the elderly) to 58 percent (rural electrification subsidy), depending on the scheme. More than 85 percent of the country's labor force is outside the existing retirement benefit scheme. Bhutan is still an agrarian country: most of the population resides in rural areas and

2 The number of healthy days is an aggregation of good physical and mental health as reported in the past 30 days.



a majority of workers engage in agriculture, often small-scale and subsistence agriculture. A majority of Bhutanese are thus frequently affected by climate- and nature-related shocks. Fourteen percent of households reported a decline in income due to a shock in the last 12 months. Poor households, rural households, and households attached to informal jobs experience more shocks, with many of them related to climate. However, existing formal social protection support mechanisms offer only limited support for such shocks. As a result, many shocks trigger high losses in income, assets and food consumption that can be catastrophic.

While social protection coverage cuts across a range of categories, its availability is limited. In Bhutan, the type of a worker's contract as well as his or her location, gender and level of education determine his or her access to social protection. Workers who are male, have regular contracts, live in urban areas, and have a high level of education have better access to social protection than other workers. Coverage of work-related fringe benefits and social assistance benefits is particularly good for public sector employees and their households and have increased in recent years. This has to be one of the main factors so many strive to get public sector jobs in Bhutan.

In the private sector, the implementation of work-related social protection programs is often lacking. Since 2007 the Ministry of Labor and Human Resources (MoLHR) has introduced a range of regulations meant to improve access by private sector workers to social protection programs and benefits. Newly-introduced benefits include access to different types of leave and the requirement for

employers to contribute to a provident fund. However, the implementation of these regulations has been lagging and has not been closely monitored. As a result, many employers have, for instance, not deducted the contributions for the provident fund from their workers' salaries or have not matched their employees' contributions to the fund.

Social protection for most people in the informal economy (including small-scale and subsistence agriculture) is inadequate, leaving those who are most vulnerable most at risk. Workers in the informal economy often have less education and lower earnings. They are also likely to lack private protection against risks such as ill health, accidents, death and old age. The provision of public social protection programs for workers in the informal economy thus presents a complex challenge. Most of the poorest 20 percent have no social protection coverage. Other support to the elderly exists only through family and social networks, and through the *kidu* program. This program has been able to provide for some of the country's most vulnerable population.

The RGoB has been drafting a social protection framework for workers, which attempts to equalize options and opportunities for workers in different segments of the private sector, including informal work. These efforts are in addition to those aimed at improving social protection for workers in the formal economy and employees of private companies. Among other things, the draft social protection framework suggests the introduction of pensions that are easily portable across different types of work and greater use of existing insurance schemes (like those offered by the Royal Insurance Corporation of Bhutan) that are in principle open to all but in practice used mostly by specific groups.

Opportunities to develop human capital and con-



nect people to productive employment have been expanded as part of the RGoB's efforts to lower unemployment. Social protection programs closely linked to the labor market—such as training, scholarships and enterprise development grants—mostly reach beneficiaries who live in urban areas, are well-educated, and come from households with at least one public sector worker. This pattern aligns closely with the group of people who are unemployed, who are for the most part concentrated among urban, well-educated youth. Although the new opportunities to develop human capital and connect people to productive employment have reached this group and certain others that struggle to find their place in the labor market, they do not reach individuals from poorer households or those who engage in relatively unproductive, unprotected employment in small-scale and subsistence agriculture and other segments of the informal economy. The Gross National Happiness Commission (GNHC) is in the midst of designing the first poverty targeted households program (THPP).

Employability of Bhutanese youth is a key priority. Employment opportunities for youth are limited. There is a particular problem with access to higher-level managerial jobs due to a skills and job mismatch in the market. Many people seek a white collar job, one that is in an urban area and in the public sector; but such opportunities are limited. As a consequence, the unemployed are relatively better educated and come from wealthier families. There are indications that a number of other, less obvious and well-documented but nevertheless pressing challenges exist. In particular, informal employment (over 75 percent, according to the latest Bhutan Labor Force Survey (BLFS)) and under-employment appear to be widespread, especially in rural areas. Additionally, chronic or long-term unemployment might be a problem for certain parts of the Bhutanese labor force. The government target is to bring down the youth unemployment rate to 5 percent or less by the end of the current plan period (2013-2018). In 2015, the overall unemployment rate slightly dropped to 2.5 percent from 2.6 percent in the previous year. However, the youth unemployment rate increased from 9.4 percent to 10.7 percent. Urban unemployment has also slightly increased, especially among women, the young and well educated. Within this context, MoLHR has decided to develop a strategy to provide more equity of social protection to those who

work across different sectors, and to provide support to senior citizens outside of the formal sector.

The World Bank has been preparing an in-depth study of the labor market, which will soon be released.

Agriculture

Bhutan is predominantly an agriculture-based society. The agriculture sector is dominated by smallholder subsistence farmers who occupy the majority of the arable land and produce most of the crop and livestock products. The agriculture sector provides a livelihood for 57 percent of the total population, contributing to 17 percent of GDP.

While the contribution of the agriculture sector to GDP has been declining, it continues to be an important sector. It is particularly important as a source of employment and a force in reducing poverty. However, the sector's growth remained insufficient to adequately address poverty and attain food security. Immigration from rural to urban areas, particularly by youth and men looking for a more modern life style, has resulted in the feminization of the agriculture sector particularly in the lagging areas.

A range of policies is needed to improve rural life. Physical access to rural areas and between rural areas and markets needs to be improved. The dispersed and small-scale production hinders adoption of good agricultural practices. Greater access to credit and technology is needed, as well as sustainable approaches to pest and wildlife encroachment. Other issues include loss of agriculture land for other development, lack of infrastruc-



ture such as irrigation, farm roads and post-harvest storage, labor shortage, and the scarcity of market traders and wholesalers.

The agriculture sector needs to grow at 4 percent. To achieve eradication of national poverty to less than 5 percent and rural poverty below 10 percent, the sector needs to grow at an annual rate of 4 percent. The 11th FYP is expected to adopt a multi-dimensional approach to develop the lagging regions. To achieve this, the Ministry of Agriculture and Forestry has a mandate to improve food security and nutrition, rural livelihoods to overcome poverty and sustainable management and use of natural resources.

The World Bank is supporting rural development through an IDA-financed Remote Rural Community Development Project (RRCDP), which focuses on increasing agriculture productivity and access to community assets in remote areas. A Food Security and Agricultural Productivity project funded by the Global Agriculture Food Security Program (GAFSP) is being prepared.

Environment

Environmental conservation is a cornerstone of Bhutan's development approach. Bhutan remains endowed with dense and virtually untouched forests, abundant water resources and diverse wild species. Nevertheless, it confronts chronic pressures primarily related to land degradation and biodiversity loss due to development and population growth. Land degradation can stem from inappropriate agriculture production and mining practices, overgrazing, and excessive forest harvesting, as well as solid waste disposal in and around population centers. Threats to biodiversity



include illicit forest harvesting, human-wildlife conflict, poaching, and habitat fragmentation arising from land development.

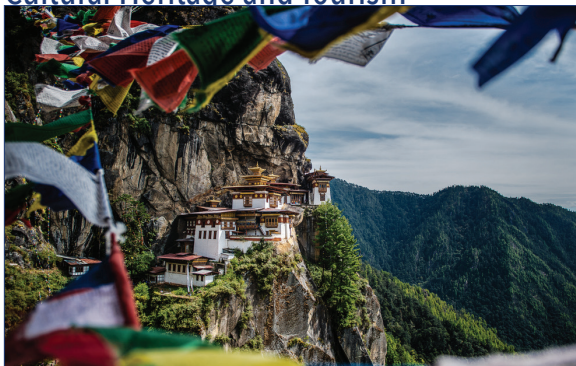
A particularly important element is the need for integrated water management. Despite the positive outlook for water availability, incipient challenges relate to the sustainability of urban water supply systems and functionality of existing rural water supply schemes. Ongoing soil erosion and deforestation threaten watershed conditions and their functional integrity. Concerns about water quality stem from the rise in domestic and industrial waste generation, along with improper disposal and runoff from agricultural fields and urban centers.

The government has taken several important steps to preserve the environment. Bhutan's environment policies include: (i) mandating in the Constitution a minimum forest cover of 60 percent of the country's total land area; and (ii) increasing the proportion of land under protected area status to around 50 percent at present from 26 percent in 2000. The Bhutan Trust Fund for Environmental Conservation (BT FEC) is working towards the adoption of more modern governance and business practices. With grants made possible by BT FEC, conservation projects began to be implemented in the high-altitude northern areas that form part of the fragile eastern Himalayan ecosystem. The wildlife crime unit within the Department of Forest and Park Services is in the process of upgrading the Bhutan Forest Enforcement Database into an online reporting system on wildlife offenses and expanding programs for raising public awareness and sensitivity to forest and wildlife crime. Environmental sustainability is at the core of Bhutan's five-year plans, including the 11th Plan currently under implementation.

The World Bank is providing support: (i) through a Global Environment Facility (GEF) project, the improvement of the operational effectiveness and institutional sustainability of the BT FEC and the management of the conservation of high-altitude northern areas; (ii) through a regional IDA project, the building of capacity, institution, knowledge and incentives to collaborate in tackling regional wildlife conservation threats; and (iii) the Reducing Emissions from Deforestation and Forest Degradation (REDD+) agenda and through it the National

Forest Inventory (Bhutan REDD Readiness).

Cultural Heritage and Tourism



Bhutan has taken important steps to preserve its cultural heritage. The country's rich cultural assets, both tangible and intangible, are highly valued as intrinsic sources of community vitality and socioeconomic development, and their protection is a key focus of Bhutan's Gross National Happiness, as well as the government's five-year development plans, its "Vision 2020", and the Constitution.

Despite that, non-monumental cultural assets such as traditional villages, their immediate natural landscapes, and the skills and ways residents have been using both to build and maintain community life for centuries are increasingly under threat from a number of unprecedented challenges and influences. These range from unplanned urban expansion and adoption of imported materials and methods for building construction to neglect or simply abandonment through urban migration. Such loss has had a direct impact on people's happiness. According to the 2015 GNH Index, only 38 percent of people in rural areas report being happy. The factors that contribute most to the happiness of rural Bhutanese are cultural diversity, community vitality, and good governance. It may also have major economic implications for the country, given the decay of valuable human, cultural, and environmental attributes of Bhutanese traditional villages, and the loss of their future economic workforce.

To combat the socioeconomic and cultural loss of such assets and the resulting weakening of community vitality, the government is in the process of approving the Cultural Heritage Bill. The bill represents a significant new approach to how the country defines, promotes, and protects its cul-

tural assets, by stewarding not only monuments and cultural expressions, such as handicrafts and music, but also the wider social, environmental, and economic settings – traditional villages and their surroundings – in which physical structures are located and expressions have been shaped and performed for centuries.

The government is also in the process of reviewing its tourism policy. Despite its worldwide reputation as a "high-value, low impact" destination, overarching issues of limited accessibility, high seasonality, lack of product diversity, ineffective marketing, travel packaging, and the dual tariff system for international and regional tourists are negatively affecting the sector competitiveness and performance. Action and changes at all levels are felt to be required to ensure that Bhutan remains a sustainable, inclusive, and high-quality destination in the long-term.

The World Bank is providing support to prepare a plan for the implementation of the Cultural Heritage Bill and to review the draft tourism policy, with a focus on preserving traditional ways of life, environmental conservation, and distribution of cultural and tourism benefits to some of the poorest communities in the country, which tend to live in traditional houses and villages across the country.

Disaster Risk Management and a Changing environment

Bhutan is highly prone to disasters and climate-related risks. Its rugged topography, geographic and climatic features make it prone to flooding, landslides, glacial lake outburst floods, drought, and earthquakes. Over the past 40 years, several





earthquakes above a magnitude of 6 on the Richter scale have occurred. According to the World Bank report on Natural Disaster Hotspots (2005), 31.3 percent of Bhutan is in risk areas, and 60.8 percent of the population is at high mortality risk from a number of hazards. Between 1994 and 2011, approximately 87,369 people were affected by natural disasters and 304 people were killed.

With climate change, the frequency and intensity of extreme weather events is expected to increase. The country has become increasingly vulnerable to glacial lake outburst floods, other flooding, drought, forest fires, and loss of vegetation/biodiversity. Heavy seasonal monsoon rains and glacial melt contribute to flooding and landslides. Most of Bhutan's productive infrastructure (hydropower plants, roads, airports, and so on), fertile agricultural land, and over 70 percent of the settlements are located along the main drainage basins, which puts them at high risk of flooding. This poses not only a threat to the development of hydropower in the country but also a threat to food security.

The performance of Bhutan's key economic sectors also depends on managing weather and disaster risks. Some of the key economic sectors driving Bhutan's economy, such as agriculture, hydropower, tourism, water resources, and infrastructure, are heavily dependent on weather, water, and climate-related information. However, such information is highly limited. Therefore, in addition to strengthening community resilience, improved development of hydromet-based information services can make important contributions to the performance of key economic sectors in Bhutan.

The government adopted the Disaster Management Act in 2013 to strengthen the disaster

management system. The act decentralizes disaster management activities, empowers the nodal institutions with the legal status to implement disaster reduction strategies, and emphasizes a consultative process at the village level. The Department of Disaster Management under the Ministry of Home & Cultural Affairs as the national coordinating agency is formulating a comprehensive National Disaster Risk Management Strategy for Bhutan. Key challenges include: (i) strengthening preparedness and early warning systems; (ii) mainstreaming disaster risk management, including in construction; and (iii) strengthening disaster response capacity.

An important aspect of disaster risk mitigation, climate adaptation, and early warning systems is improved capacity for hydro meteorological monitoring and forecasting. Importance of hydromet services is well recognized in FYP-11. In Bhutan, the main agency responsible for these services and for weather, hydrological, and flood forecasting is the Department of Hydromet Services (DHMS) under the Ministry of Economic Affairs. DHMS was established in 2011. It is a relatively new agency in significant need of capacity strengthening. At present, there is no legal or regulatory framework for delivering hydromet services or a national framework for climate services. Most of the existing observation network is manual with limited capacity for real-time monitoring. Capacity for snow, permafrost, and glacier monitoring within DHMS is only now beginning. Bhutan at present features only 24-hour weather forecasts; there is a need to improve the lead time to better prepare communities. Also, the current practice issues flood warnings only when the water level is high. While DHMS's activities are being supported by several development partners, such as the U.N. Development Program and Japan International Cooperation Agency, there is substantial room for strengthening DHMS to support its transformation into a modern service delivery agency that can support disaster risk mitigation, and also provide climate services in various sectors such as agriculture, water resources, and hydropower.

The World Bank is active in this area through: (i) a Policy and Human Resources Development grant for improving resilience to seismic risk; (ii) Hydromet Services and Disaster Improvement Regional Project – a grant funded project to strength-

en Bhutan's capacity for hydromet services and disaster preparedness (iii) supporting the government in preparing a Strategic Program for Climate Resilience under the Pilot Program for Climate Resilience (PPCR).

Urban Development



Bhutan is undergoing a rapid transition from a rural economy to an urban society. The average annual urban population growth rate has been around 4 percent since 2007. The Bhutan National Urban Strategy (NUS, 2008) projects that by 2020, the country will be most likely 60 percent urbanized. As Bhutan evolves into a more urbanized society, the government has recognized the country's unique challenges in urban development – the rapid rate of urbanization and the limited availability of serviced land.

The urbanization rate across the country is skewed toward the Western region. Thimphu and Phuentsholing are the two most favored destinations for migrants. These cities, especially Thimphu, are experiencing urban sprawl and densification with consequent rise in demand for municipal services. Through the enactment of the Local Government Act (2009) and the approval of the Municipal Finance Policy (2012), the government has established four autonomous cities (Thimphu, Phuentsholing, Gelephu and Samdrup-Jokhar). Under the proposed National Urban System, these urban centers would play an important role as future engines of growth.

Bhutan is relatively well positioned to meet the challenge of rapid urbanization, given its low population. Nevertheless, urban institutional and governance systems need to be strengthened. Spa-

tial planning is also needed, as lack of affordable and housing for lower-income groups is becoming a critical issue. Another important issue related to the rapid urbanization is to provide jobs for an increasingly urban youth population.

The World Bank is supporting the government through the Second Bhutan Urban Development Project and its additional financing. That provides resources for sites and services development in northern Thimphu and for municipal finance and management systems development in the four cities, as well as for related capacity building. The World Bank is also supporting the formulation of an inter-governmental resource framework for urban local governments. Finally, the World Bank is supporting improving green urban public transport.

Energy

Hydropower development has underpinned the rapid growth of Bhutan's economy. The total installed capacity of existing hydropower plants is 1,606 megawatts (MW). Of total annual power generated, the overwhelming majority is exported to India after meeting domestic consumption. Power exports account for the largest source of national revenue in the form of taxes and dividends, currently generating 40 percent of government revenue. This is expected to increase to 60% by 2025. Hydropower contributes currently 25 percent of GDP, and its contribution to economic growth will further increase as the RGoB plans to commission close to 12,600 MW of new hydropower over the next decade.

Bhutan's hydropower generation potential raises the prospect of tremendous development opportunities for the country: fast-increasing export revenue, sustained economic growth, and rapid poverty reduction.

Generation projects have been implemented in partnership between the Government of Bhutan and the Government of India under three different development models:

- The Inter-Governmental model: The Government of India is responsible for mobilizing the project's funding and implementing the project until the time of commissioning. The project ownership is then transferred to the



Government of Bhutan, with a certain amount of debt repayment to the Government of India. The Government of India buys all the electricity generated in surplus of domestic consumption, at a price determined on a cost-plus basis, guaranteeing a net return of 15 percent to the Bhutanese government above debt repayment and the project's operating cost.

- The Joint-Venture model: Projects are developed and commissioned under a Joint venture of Bhutan and India Public Sector Undertakings (PSUs) under a 50/50 percent ownership, with 70 percent being financed by loans raised by the PSUs, and 30 percent equity participation, out of which the Bhutanese share is financed from grants provided by the Government of India.
- The PPP model: So far, two PPP projects have been developed with the support of the ADB and the Government of Austria.

Bhutan has also begun to develop renewable energy to diversify the energy supply base through wind, solar, biomass, and small and micro hydropower. Wind-power projects have the potential to generate clean energy to supplement hydropower in winter dry seasons. Bhutan also has biogas development potential as an alternative energy source to replace fuel wood for cooking in rural areas. Rural households depend heavily on fuel wood, which emits indoor air pollutants and poses a health hazard. To promote renewable energy, a national policy must be established and financial and fiscal incentives provided to help overcome the entry and financial barriers for development.

The World Bank has supported the government in carrying out an assessment of the macroeconomic, environmental and social (E&S) impacts of current

and future hydropower development in Bhutan, and is currently providing technical assistance to formulate national guidelines for the preparation and construction of hydropower projects. The requested assistance to the sector aims to help the government prepare a realistic action plan for implementation of hydropower projects based on absorptive capacity of the economy and social-economic impacts. The World Bank has also been asked by RGoB to support the development of a strategic roadmap for future hydropower development in Bhutan, and to conduct preparatory studies and design for one hydropower project.

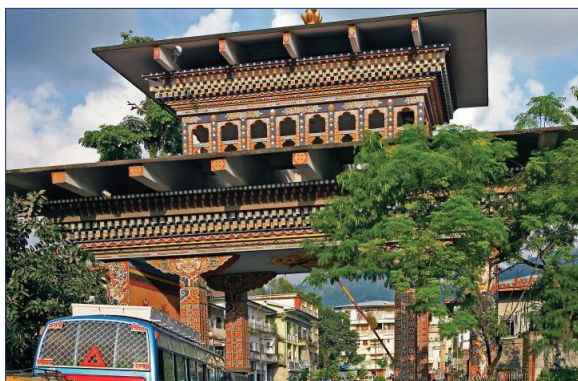
Transportation

Transportation remains one of Bhutan's foremost development challenges in both rural and urban areas.

In rural areas, transport connectivity is a key determinant of affordable access to basic social and economic services. The Bhutan Living Standards Survey (2012) reports that transportation services alone account for approximately 23 percent of the cost incurred when households sought health care to address sickness or injury. In the broader economic context, roughly 40 percent of all firms and 70 percent of large firms surveyed had experienced losses due to ground transportation difficulties. Bhutan's landlocked geography, absence of rail connections, and limited air connectivity make the road and bridge network's reliability particularly vital to providing the access that households and businesses require.

The World Bank is supporting Bhutan's Department of Roads (DOR) efforts to get more out of expenditures on road maintenance and to improve





the resilience of roads and bridges. In 2016, it completed a technical assistance initiative that helped the DOR develop a road and bridges asset management system and assess the condition of 1,800 km of Bhutan's national highways. This activity used a grant from the Global Facility for Disaster Risk Reduction (GFDRR) and was unique both for what it accomplished and how it accomplished it. The approach to developing DOR's new system relied on low cost and open source technologies to conduct condition assessments. It involved adapting low cost GPS-equipped cameras that were originally intended for recording extreme sports, for example from a skydiver's helmet). The cameras provide a video record of road conditions along with a synchronized GPS track that can be loaded into Google Earth or other open-source GIS systems. Engineers populate an excel-based database with information from video recorded condition assessments. Google Nexus tablets provide a template for bridge condition assessment along with the capability to take and store pictures on site. Each set of hardware costs less than US\$ 1,500 and does not require an incremental fee for software use. The database is excel-based and requires no special software training to use or adapt. The DOR is now conducting condition assessments for an additional 400 km of roads using this system. Results will enable DOR to develop an investment program for maintenance from the "assets up" whereas this was previously not possible. The Bank is continuing to mentor this process and may provide additional training or assistance to support DOR as it begins to develop more sophisticated planning and budgeting approaches for Bhutan's road network. The envisaged impacts of this work are improved use of financial resources and more effective maintenance of roads and bridges.

Bhutan's urban areas are also undergoing a significant transition that requires upgraded transport services. Between 1990 and 2010, the number of Bhutanese living in urban areas nearly tripled. Increasing rates of motor vehicle ownership and use have accompanied this trend bringing impacts on the urban environment. In response, RGoB has both limited the import of private vehicles at times and increased taxes on vehicle purchases. These measures have helped curtail the growth of private vehicle ownership but their long term effectiveness has been limited by the lack of alternatives to private transport. Restrictions on vehicles have also resulted in unmet needs for urban mobility. Bhutan's urban public transport systems are still developing to meet increasing demand and customer expectations for a higher quality of service. As a result, less than one third of urban households in Bhutan reported using public transport in a given month in 2012. Improving the availability and quality of urban transport services in Bhutan offers an opportunity to meet the expanding demand for urban mobility through services that both meet the needs of lower income households and offer environmental benefits compared to private transport.

The Bank is targeting two interventions that will support improvements in urban transport in the capital city of Thimphu. These include (i) a US\$ 2.5 – 3 million investment in bus shelters and accessibility improvements for people with disabilities that will endeavor to tap a grant from the Global Partnership on Output-Based Aid (GPOBA); and (ii) an urban transport master plan for Thimphu. A concept note for investments in bus shelters and accessibility improvements has been developed. It is awaiting consideration by the GPOBA Panel of Experts, which is tentatively planned for fall 2016. A detailed Terms of Reference has also been developed for Thimphu's urban transport master plan. The goal of this plan will be to position Thimphu for a step change in the use of public transport services and non-motorized forms of transport. The Team is pursuing funding sources that could support the urban transport master plan's implementation.

There is growing recognition of the benefits of economic integration in South Asia particularly among the BBIN (Bangladesh, Bhutan, India, and Nepal) countries. Removing obstacles to trade through improved transport connectivity, logistics facilitation measures and lowering tariffs and other trade

barriers has become a high priority for these countries. This is shown by recent sub-regional agreements, notably the BBIN Motor Vehicle Agreement, and the renewed Protocol on Inland Water Transit and Trade signed between Bangladesh and India, but with potential to benefit all BBIN countries. In addition, there is evidence that limited regional broadband connectivity is currently hampering the development of ICT-enabled regional services, including efficient cross-border trade. The South Asian Telecommunications Regulators' Council is pursuing various initiatives to harmonize policies and address some of the regulatory restrictions to greater infrastructure and services integration.

Bhutan as a landlocked country stands to benefit significantly from greater regional integration. Bhutan suffers from typical problems affecting landlocked countries, notably dependence on sea ports in neighboring countries, inefficiencies at land border crossings, and limitations on routes for transit cargo. Partly as a result, Bhutan is among the poorer performers in the World Bank's Logistics Performance Index, placing 135 out of 160 countries. Bhutan's landlocked status also has affected the reliability and affordability of its international telecommunications connectivity. The distance between Bhutan's borders and the coastal landing stations of the submarine cables presents a significant challenge for operators and Internet Service Providers (ISPs) attempting to access low-cost bandwidth. Bhutan currently relies on international telecommunications connectivity through two gateways - Phuentsholing-Siliguri and Gelephu-Bongaigaon - both of which have a single point of potential failure at the narrow Siliguri Corridor (or Chicken's Neck). The price of international broadband services in Bhutan is nearly ten times that of India and double that of Nepal, and represents a key deterrent to improved digital connectivity. This affects digitally enabled trade in both goods and services, private sector development and job creation.

The World Bank is supporting the Government to address some of the main contributing factors to Bhutan's high trade costs and inherent risks and high costs of IT broadband connectivity through a Bhutan Regional Connectivity Project under preparation. This project is a \$55 million operation financed through regional and national IDA (\$50 million total) and government contribution (up to

\$5 million). It supports the RGoB's revised Economic Development Plan and 11th Five-Year Plan and is a priority in the Bhutan Country Partnership Strategy (CPS) for FY15-19 and the South Asia Regional Strategy of the World Bank. The Project is scheduled to be presented to the Board for approval in November 2016.

Governance, Public Financial Management and Procurement

Bhutan outperforms its neighbors on Transparency International's Corruption Perception Index. In 2012, Bhutan moved up the index, from 38th to 33rd, in recognition of additional steps it has taken to strengthen its anti-corruption legal framework, including passage of the 2011 Anti-Corruption Act, the establishment of an Anti-Corruption Commission (ACC), and further strengthening of rules governing asset declaration by public servants in 2012. In 2015, Bhutan rose to 27th in the index. A key element for improving governance has been an ambitious government-to-citizen program to provide services electronically through community centers, a particularly important development in light of geographical barriers. Similarly, with support from the International Finance Corporation (IFC), the government has developed a government-to-business e-portal to provide a comprehensive inventory of licenses and other information on business processes.

Public financial management (PFM) reforms are part of national priorities. Bhutan over the years has been making progress in the area of accounting, budget execution oversight, control, and reporting. Parliamentarians increasingly pay attention to the budget approval process and also in



reviewing the audit observations through public accounts committee. Recently, the National Assembly Act of Bhutan was amended to allow reference of Budget Bill to a committee. The government continues to take steps to strengthen PFM in the country. The public at large has also become more demanding in terms of transparent and efficient government. Nevertheless, further improvement is needed on oversight of public-sector entities, predictability in funds available for expenditures, the quality and timeliness of budget reports and financial statements, implementing the standards on auditing and accounting, PFM information systems, availability of professionally qualified staff, and effectiveness of internal audits.

Significant progress has been achieved on public procurement reforms. Among the outcomes are: (i) introduction of the procurement rules and regulations and standard Bidding Documents for Goods, Works and Services in April 2009; (ii) establishment of the Public Procurement Policy Division in August 2008 which is now fully functional with qualified staff; (iii) establishment of a central procurement web portal where all rules/regulations, standard bidding documents, and relevant procurement news are available for the stakeholders; (iv) system development for the first phase of electronic government procurement (e-GP) which includes electronic tendering; (v) the putting in place of career path and recruitment tools for a procurement profession – procurement cadre service; (vi) the generally well-functioning procurement market; (vii) a strong framework for control and audit, spearheaded by the Royal Audit Authority and the ACC; (viii) set up and full operation of the Government Procurement and Property Management Division to conduct centralized procurement and framework agreement of common items; and (ix) formation of an independent review body to handle procurement grievances.

World Bank's support. The World Bank has provided an Institutional Development Fund (IDF) grant to help the government improve financial management in the public and private sectors by strengthening internal audit in the public sector, assisting in the implementation of Bhutanese Accounting Standards, and supporting the government in establishment of Bhutanese Institute of Chartered Accountants. The World Bank has also provided a grant from a global multi-donor trust

fund to the Royal Monetary Authority (RMA) to support the implementation of International Standards for Supreme Audit Institutions.

Building on this progress, the World Bank is moving toward use of country systems for all procurements up to the International Competitive Bidding Thresholds in Bhutan from end FY2014/15. The Alternative Dispute Resolution Act of Bhutan, 2013 has come into being and formal arbitration expertise needs to be built in the country. In endeavoring to professionalize the procurement function, Bhutan has enrolled more than 300 government staff in the World Bank's Certificate Program in Public Procurement.

To get an update on the progress made since the last Public Expenditure and Financial Accountability (PEFA) Assessment of 2010, a PEFA update as per the latest 2016 Framework is currently being undertaken by Bhutan. This activity is being led by World Bank. The World Bank is supporting the establishment of a Multi-Donor Fund for Public Financial Management in the country, co-funded by the European Commission and the Austria Development Agency. This fund will serve a programmatic approach to PFM reforms in Bhutan.

THE WORLD BANK PROGRAM IN BHUTAN

The Board endorsed the Country Partnership Strategy (CPS) in September 2014. The overarching goal of the CPS (FY2015-2019) is to support Bhutan's aspirations to achieve sustainable and inclusive growth. The CPS is aligned with the 11th FYP and WBG activities are organized under three results areas: (i) improving fiscal and spending efficiency; (ii) increasing private-sector growth and competitiveness; and (iii) supporting green development. IDA financing is expected to continue mainly in the form of development policy lending, supplemented by a limited number of specific investments in key areas, particularly infrastructure, and a robust analytic program.

Bhutan's IDA17 allocation is about \$56 million over three years, given that Bhutan has one of the highest Country Policy and Institutional Assessments in the IDA cohort. Although Bhutan is not yet creditworthy for the IBRD, it has exceeded the gross

national income per capita threshold a couple of years ago and will move toward a blend status. . The program is small but active, with four IDA operations under implementation: (i) Development Policy series of two operations (\$20 million each); (ii) Urban Development II (\$12 million) and additional financing (\$17 million); (iii) Remote Rural Community Development (\$9 million); and (iv) it is a participating country in the regional IDA wildlife project (\$2.9 million). The total net commitment value is \$41.9 million plus \$20 million of development policy credit. Bhutan also has about 12 trust funded-operations, including a GEF sustainable financing for biodiversity and several grants on disaster management, REDD+, hydromet, corporate governance, PFM, intergovernmental fiscal relations, ICT, tourism and cultural heritage, hydropower environmental and social impact assessment, urban public transport, financial sector (FIRST), South-South knowledge exchange, statistical capacity building.

Two IDA operations are being prepared. The first Development Policy Credit (of a series of two) became effective in July 2015 for a total of \$20 million. The next IDA operations are: (i) the regional connectivity project (National IDA of \$8 million, with additional regional IDA of \$42 million) and (ii) the second Development Policy Credit. These operations will be presented to the Board for approval in Q2 FY2017.

Bhutan Portfolio performance is moderately satisfactory with no problem projects. Implementation challenges relate to the capacity of civil servants being stretched in the absence of dedicated project management units. Significant progress has been made in the enhanced use of country systems. We are increasingly moving toward a programmatic approach in managing our portfolio, consolidating around a few themes, task team leaders and joint missions.

The World Bank also provides key knowledge support to Bhutan. Recent analytic work includes a Public Finance Note - a Just In Time Note to assess the short, medium and long term impact of hydropower development on the Bhutanese macro-economy and the role of public finance in addressing related challenges; Poverty assessment, a green growth study; Assistance to build a public expenditure database (BOOST); Update of the National Sta-

tistical Strategy and implementation of the World Bank-developed CAPI technology which assists in conducting surveys; Update of the Information and Communications Technology Roadmap; Enterprise Survey 2015; Support the development of Bhutan's Social Protection Strategy ; Technical research on electric vehicles and international experiences with EV incentives; Study on the environmental and social impact of hydropower and financial sector Development Action Plan.

Ongoing FY17 analytic work includes an in-depth labor market study, an agribusiness note and an investment climate assessment, review of Bhutan's tourism policy, technical analysis of hydromet, disaster management and climate change, technical assistance on tax reforms and a social assistance technical assistance. The World Bank is also working on a procurement review to allow Thimphu municipality to use Alternative Procurement arrangements (APA) per the World Bank new Procurement Policy.

INTERNATIONAL FINANCE CORPORATION (IFC)

The IFC has a total committed investment portfolio in Bhutan of about \$34 million as of June 2016. The portfolio consists predominantly of IFC's equity participation in Bhutan National Bank (BNB) which was the largest FDI in Bhutan and support for the expansion of a local hotel which was the first cross border commercial loan availed by a fully Bhutanese private entity. IFC, using some of its own funds and mobilizing funds from the ADB and GAFSP, will provide \$12 million assistance to a hazelnut plantation project in Bhutan. IFC's first debt assistance of \$10 million to a local hotel was made in 2003 and successfully liquidated in June 2015. This investment had a profound demonstration effect in promoting tourism in Bhutan.

The advisory portfolio includes advice in structuring PPPs, improving Bhutan's investment climate and enhancing access to financial services. IFC successfully completed a post-transaction advisory engagement with the Thimphu Municipality for the development of a multi-level car park PPP project which was amongst the first professionally structured PPPs in the transport sector. The engagement

involved advising municipal and government officials in managing PPP projects using the case of the ongoing project. IFC is also providing assistance to the Ministry of Economic Affairs and Druk Holding and Investments to help them consider setting up a power trading company in India.

IFC continues to explore areas of assistance in the hydropower, tourism, manufacturing, agribusiness, climate change, and education sectors, among others. IFC's advisory support on investment climate reforms, infrastructure development through PPPs

and enhancing financial inclusion and SME development is expected to continue.

MULTILATERAL INVESTMENT GUARANTEE AGENCY (MIGA)

On October 21, 2014, Bhutan became the 181st member of MIGA. In light of Bhutan's recent membership, MIGA has not provided guarantee coverage for investment in Bhutan to date.

BHUTAN: SECOND URBAN DEVELOPMENT PROJECT AND ADDITIONAL FINANCING (BUDP2)

KEY DATES:

<i>Initial:</i>	<i>Additional:</i>
Approved: April 29, 2010	May 16, 2014
Effective: August 24, 2010	
Closing: December 31, 2015	June 30, 2019

FINANCING IN MILLION USDOLLARS*:

Financier	Financing	Disbursed	Undisbursed
IDA	12.01	6.23	5.39
Royal Government of Bhutan	0.7		
Project Cost	12.71		
Additional financing	17.4		
Total Project cost	30.11		

**As of August 23, 2016*

BACKGROUND AND OBJECTIVES:

The Kingdom of Bhutan has been experiencing rapid social and economic development over the past two decades, and this socio-economic transition is fueling rapid urbanization. Meeting the challenges of urban development, management, and finance is now a key developmental agenda of the government and its international development partners. The World Bank started its support with the Bhutan Urban Development Project (1999-2006), which helped develop urban infrastructure systems in 10 secondary towns. The government showed strong interest and appreciation of the Bank's policy advice through the project and technical assistance to prepare the National Urbanization Strategy (2008) and the Thimphu City Development Strategy. On the government side, the Local Government Act of 2009 and Municipal Finance Policy (2012) provide the framework for the roles and responsibilities of urban local governments. In that context, the ongoing BUDP2 focuses on supporting urban/municipal development in Thimphu (the capital and Bhutan's largest city) and Phuentsholing (second largest city and a commercial hub), as well as technical assistance for the urban local governments and the Ministry of Works and Human Settlement.

The project development objectives are to (i) support Bhutan's municipal reform program by strengthening municipal finance and management services in Thimphu and Phuentsholing; and (ii) improve infrastructure services in northern Thimphu where no formal services are currently available.

The original BUDP2 as well as the Additional Financing consists of three components: municipal finance and management, Thimphu Northern Area Development, and capacity building.

- Component 1 aims at strengthening the institutional systems of Thimphu and Phuentsholing Thromdes, or city corporations. The support for the city-specific reforms is being done broadly through strengthening both the local revenue administration systems and processes, and the expenditure management systems and financial management systems and processes of the two city corporations. Two new towns (Gelephu and Samdrup Jongkhar) will also be covered under the Additional Financing. This component also supports government policy reforms aimed at setting up a policy framework for municipal financing.
- Component 2 supports the development of basic infrastructure systems in two "local area plans" in northern Thimphu, including roads, storm-water drainage, water supply, sewerage, and street lighting, as well as support for increasing low-income housing units in these areas.
- Under Component 3, resources are being provided for training programs, equipment, technical assistance, and studies based on the needs of Thimphu and Phuentsholing Thromdes as well as preparation and implementation of urbanization-related policies by the Ministry of Works and Human Settlement. This component aims to significantly upgrade each city corporation's capacities in various aspects of their internal work processes and service delivery to citizens through training of operational staff and provision of relevant equipment.

KEY ACHIEVEMENTS AND EXPECTED RESULTS:

- Increase in local revenue collection: 50 percent by Thimphu and 40 percent by Phuentsholing.
- New building permits issued for serviced plots: 175 (in two Thimphu "local area plans" being developed).
- Number of households with new piped water and sewerage connections: 600 (in two Thimphu "local area plans").
- Number of municipal staff trained: 250 (with 150 in Thimphu and 100 in Phuentsholing)

KEY PARTNERS:

Ministry of Works and Human Settlement, Ministry of Finance; Thimphu, Phuentsholing, Gelephu and Samdrup Jongkhar Thromdes.

BHUTAN: REMOTE RURAL COMMUNITIES DEVELOPMENT PROJECT (RRCDP)

KEY DATES:

Approved: October 2, 2012
Effective: November 15, 2012
Closing: May 31, 2018

FINANCING IN MILLION USDOLLARS*:

Financier	Financing	Disbursed	Undisbursed
IDA	9.00	6.025	2.9
Total Project Cost	9.00		

**As of August 23, 2016*

PROJECT BACKGROUND:

The Remote Rural Communities Development Project (RRCDP) project area covers 26 gewogs, or village administrative units, and six dzongkhags or districts, in southwestern and south central Bhutan. The RRCDP is designed to improve living conditions and incomes in the poorer and more remote rural areas. The populations in these areas currently rely on subsistence agriculture, and lack roads, irrigation, technologies, and community and social infrastructure that would allow them to improve their incomes and social integration.

The main objective of the project is to increase agriculture productivity in remote rural areas by improving access to markets, irrigation, agricultural technologies, and community infrastructure. Improvement in market access would be achieved by investments in farm roads and marketing infrastructure. Agricultural productivity and rural incomes would increase through promotion of improved irrigation and agronomic practices, and rehabilitation of productive assets for key commodities. Community-led investments will improve the access of the poorest people to the critical and missing infrastructure in the selected area. The RRCDP consists of three components:

- Rural Infrastructure: Connects the communities to larger roads and regional markets and to improve production potential through improved availability of irrigation.
- Community, Marketing and Productive Infrastructure: Covers investments in marketing and post-harvest infrastructure, critical community-level infrastructure, and investments identified by producers to increase agricultural productivity.
- Project Management and Institutional Strengthening: Supports project management, including the monitoring and evaluation functions. It covers technical and financial management; procurement; and supervision of compliance with environmental and social safeguards.

KEY ACHIEVEMENTS AND EXPECTED RESULTS:

- Formation cutting and construction of permanent works on all five farm roads are in progress.
- 34 irrigation schemes have already been completed or near completion.
- A total of 76 sub-projects have been financed benefitting 27,387 persons in 4,393 households (13,829 males and 13,558 females).
- A total of 78,223 grafted seedlings and 258,248 cardamom suckers have been supplied. A total of 225 cows and 15,662 pullets have been distributed. Farmers from the five project supported dzongkhags have been able to earn a cash income of Nu 12.444 million and Nu 7.231 million from the sale of 1,387,074 eggs and 2,98,413 liters of milk respectively.
- The project has supported 33 community forest groups benefitting 2520 households in 22 gewogs from 6 dzongkhags. Plantation area covered is now 77.25 ha and 5.35 ha under nursery.

KEY PARTNERS:

Ministry of Agriculture and Forests

BHUTAN: IMPROVING BHUTAN INVESTMENT CLIMATE

KEY DATES:

Approved: April 6, 2015
Effective: April 6, 2015
Closing: June 30, 2017

FINANCING IN MILLION USDOLLARS*:

Financier	Financing	Disbursed	Undisbursed
IBRD	0.235	0.115	0.12
IDA			
Government of			
Other	0.19	0.14	0.05
Total Project Cost	0.425	0.255	0.17

**As of August 23, 2016*

PROJECT BACKGROUND:

This programmatic Technical Assistance (TA) seeks to improve the investment climate of Bhutan across two pillars. The first pillar supports the DPC2 operation by addressing key constraints in the investment climate, in the areas of:

business registration, property registration, and insolvency. These constraints were highlighted and prioritized by the Government in the 2013 Investment Climate Reform Memorandum and the ensuing Action Plan.

The second pillar consists of an enterprise survey that updates and expands the 2009 survey, and policy notes on competitiveness issues and agribusiness.

The support provided to RGoB to meet the investment climate policy triggers includes:

Revision of the Bankruptcy Act to provide a framework for businesses to resolve insolvency and strengthen the rights of secured creditors.

Introduction of a single window for online business registration.

Improvements of the electronic property and land registration system

KEY ACHIEVEMENTS AND EXPECTED RESULTS:

The first pillar of the Technical Assistance is currently in progress. The WBG has delivered to the Government ICT and workflow assessments of the company registry and the land registry. Based on those, the Government has hired two vendors that will develop the updated system solutions. The Enterprise Survey was conducted in 2015, and the results are publicly available in the Enterprise Survey website. The policy notes on the competitiveness of the agribusiness sector, and the broad investment climate are currently being drafted.

IMPLEMENTING AGENCY:

National Statistics Bureau (enterprise survey), Ministry of Economic Affairs (the rest of the TA).

KEY PARTNERS:

Ministry of Information and Communication, National Land Commission, Ministry of Agriculture; G2C Office

BHUTAN: IMPROVING RESILIENCE TO SEISMIC RISK

KEY DATES:

Approved: Feb 4, 2013
Effective: May 23, 2013
Closing: May 30, 2017

FINANCING IN MILLION USDOLLARS*:

Financier	Financing	Disbursed	Undisbursed
PHRD	1.28	0.81	0.48
Total Project Cost	1.28		

**As of August 23, 2016*

BACKGROUND AND OBJECTIVES:

Bhutan lies in a high risk seismic zone in the fragile Himalayan ecosystem. The earthquake in September 2009 (magnitude 6.1 on the Richter scale) which caused damages estimated at approximately \$52 million followed by floods throughout the country again revealed Bhutan's vulnerability to adverse natural events. The earthquake caused 12 deaths and 47 injuries in three eastern districts. Nearly 91 educational institutions, including schools, 25 basic health units, 3 hospitals, 50 local government offices, and numerous cultural and religious structures such as monasteries and temples were damaged during this earthquake. In total, 4,614 individual houses were damaged, out of which 446 houses were classified as beyond repair. Major challenges faced during the 2009 earthquake were the unavailability of a standard post disaster assessment format, manuals for reconstruction of traditional structures with incorporation of seismic resilient techniques. The unavailability of adequate information on seismic activities in Bhutan was mentioned as a challenge for developing adequate building codes for the Bhutan. The Policy and Human Resources Development Grant (PHRD) for \$1.285 million was approved in February 2013 to address the above challenges.

The objective of the Project is to improve the understanding of earthquake risk in Bhutan as well as opportunities and challenges associated to its mitigation. The Project consists of the following Components:

- Investigations and mapping for improved understanding of seismic risk: \$0.29 million (implemented by the Department of Geology and Mines under the Ministry of Economic Affairs)
- National vulnerability assessment and retrofitting: \$0.55 million (implemented by the Department of Engineering Services under the Ministry of Works and Human Settlement)
- Improving Seismic Resilience of Traditional Bhutanese Buildings: \$0.20 million (implemented by the Department of Culture under the Ministry of Home and Cultural Affairs)
- Development of emergency structural assessment capacity: \$0.05 million (implemented by the Department of Engineering Services under the Ministry of Works and Human Settlement)
- Project Management, Monitoring and Evaluation: \$0.1955 million (implemented by the Department of Disaster Management under the Ministry of Home and Cultural Affairs)

KEY ACHIEVEMENTS AND EXPECTED RESULTS:

- Strengthen the seismic network with installation of 6 seismic stations across the country including communication items
- Work on site for retrofitting of all four public buildings started
- Typology survey of rammed earth buildings in Bhutan completed and first draft of General guideline for seismic resilient construction techniques for the rammed earth structures in Bhutan prepared

IMPLEMENTING AGENCY:

Department of Disaster Management, Ministry of Home and Cultural Affairs; Department of Geology and Mines, Ministry of Economic Affairs; Department of Engineering Services, Ministry of Works and Human Settlement; Department of Culture, Ministry of Home and Cultural Affairs.

BHUTAN: HYDROMET SERVICES AND DISASTER IMPROVEMENT REGIONAL PROJECT

KEY DATES:

Expected Effective: September 15, 2016
Expected Closing: June 30, 2020

FINANCING IN MILLION US DOLLARS*:

Financier	Financing	Disbursed	Undisbursed
Global Facility for Disaster Reduction and Recovery	3.30		
South Asia Water Initiative (SAWI)	0.50		
Total Project Cost	3.80		

*As of August 23, 2016

BACKGROUND AND OBJECTIVES:

Bhutan is highly exposed to natural disasters and climate risks. Some of the major hydrometeorological hazards facing Bhutan include riverine floods, glacial lake outburst floods (GLOFs), flash floods, landslides, forest fires, and windstorms. These have significant economic and social consequences. The 2009 cyclone Aila alone resulted in damages of approximately \$17 million (roughly 1.7 percent of Bhutan's GDP in 2009). However, at present, Bhutan faces significant challenges in terms of providing accurate weather forecasts and early warnings to communities. Flood-affected communities or infrastructure operators get flood warnings but do not get flood forecasts with sufficient lead time. Some of the key economic sectors driving Bhutan's economy, such as agriculture, hydropower, tourism, aviation, water resources, and infrastructure, are heavily dependent on weather, water, and climate-related information. However, information products tailored to these sectors are highly limited. Despite the severity of natural hazards, Bhutan also faces significant challenges in its disaster response and emergency preparedness capacity. In the past decade, Bhutan has demonstrated steady and pro-poor economic growth and a strong commitment to peace and democratic governance. For it to maintain and build on its development gains and economic reforms, it must strengthen disaster preparedness and improve development of hydromet and climate services.

The project development objective is to strengthen Bhutan's capacity for hydromet services and disaster preparedness. It has three main Components:

- Hydromet Services Improvement: \$1.60 million (implemented by the Department of Hydromet Services under the Ministry of Economic Affairs)
- Disaster Preparedness and Response Capacity Improvement: \$2.00 million (implemented by the Department of Disaster Management under the Ministry of Home and Cultural Affairs)
- Design of an Agromet Decision Support System: \$0.2 million (implemented by the Department of Agriculture under the Ministry of Agriculture and Forests)

EXPECTED RESULTS:

- The project is expected to support increase in the number of hydromet services provided to users such as wind advisories for aviation sector and flood forecasts to vulnerable communities.
- The project will also result in improved capacity for disaster preparedness through construction of a national emergency operating center and strengthened emergency communications capacity at the district level.

IMPLEMENTING AGENCIES:

Department of Disaster Management, Ministry of Home and Cultural Affairs; Department of Hydromet Services, Ministry of Economic Affairs; Department of Agriculture, Ministry of Agriculture and Forests.

BHUTAN: STRATEGIC PROGRAM FOR CLIMATE RESILIENCE

KEY DATES:

Expected Effective: October 01, 2016

Expected Closing: October 30, 2017

FINANCING IN MILLION US DOLLARS:

Financier	Financing	Disbursed	Undisbursed
Climate Investment Funds	1.50		
Total Project Cost	1.50		

**As of August 23, 2016*

BACKGROUND AND OBJECTIVES:

Even though Bhutan is a net sequester of greenhouse gases (GHG), the effects of climate change and variability are becoming increasingly visible. Bhutan is highly exposed to hydro-meteorological hazards such as floods, flashfloods, landslides, Glacier Lake Outburst Floods (GLOF), windstorms and cyclones. According to the International Disaster Database, the 10 most significant natural disasters in Bhutan have all occurred in the last twenty years in terms of casualties and number of people affected. With climate change, the frequency and intensity of major hydro-meteorological hazards is expected to increase and this will have a major impact on all key socio-economic sectors such as agriculture, hydropower, tourism, transport, infrastructure and water, particularly affecting marginal and poorer communities. The country is also increasingly experiencing prolonged and extreme droughts which in turn increases the risk of loss of biodiversity, crop yield, agricultural productivity, as well as forest fires. To address these risks, the Royal Government of Bhutan (RGoB) is undertaking a variety of actions with support from different agencies and sectors in Bhutan. However, what is unclear is how they are embedded in a long term vision, how adaptation in Bhutan can be understood in the context of a low carbon development path, which sectors to prioritize or what the role of the private sector can play in supporting climate resilience.

Bhutan's National Adaptation Action Plan focused on identifying "urgent and immediate projects and activities that can help communities adapt to climate change," and the Intended Nationally Determined Contributions put a broad spectrum of priorities for both mitigation and adaptation for low GHG emission development and broadly describes how this will be implemented. But there is a need to take a more long term and strategic view of how Bhutan can position itself for addressing climate related risks. In order to develop such a strategic vision, Bhutan has been selected as a participating country for support through the Climate Investment Funds (CIF). This pipeline project supports the development of this strategic vision and the Strategic Program for Climate Resilience (SPCR).

The project development objective is to strengthen the capacity of the RGoB for improving climate resilience. The output of the process will be the SPCR document which is expected to develop a programmatic approach outlining country priorities and capacity development, and articulate a program of investments to achieve climate resilience. It will also inform the formulation of the National Adaptation Plan (NAP) and inform the 12th Five Year Plan (July 2018-June 2023) now being prepared.

The Project will consist of the following Components:

Development of the SPCR: \$1.10 million

Project Management, Capacity building and Institutional coordination: \$ 0.40 million

EXPECTED RESULTS:

- Improved capacity to mainstream climate issues into national development plans
- Strategic Climate resilience investment plan developed and agreed by RGoB

IMPLEMENTING AGENCY:

Gross National Happiness Commission

KEY PARTNERS:

National Environment Commission, Department of Hydromet Services, Department of Engineering Services, Watershed Management Division, Department of Disaster Management

BHUTAN: FOREST CARBON PARTNERSHIP FACILITY (FCPF) READINESS AND IMPLEMENTATION

KEY DATES:

Effective: March 19, 2015
Closing: June 30, 2020

FINANCING IN MILLION USDOLLARS*:

Financier	Financing	Disbursed	Undisbursed
Forest Carbon Partnership Facility	3.8		
Total Project Cost	3.8		

**As of August 23, 2016*

BACKGROUND AND OBJECTIVES:

Bhutan is a FCPF member country. The Grant Agreement for REDD+ Readiness Preparation was signed between the WB and the Ministry of Finance in March 2015, and the REDD+ Readiness Preparation project was launched officially on May 27, 2015. The REDD+ Secretariat in the Watershed Management Division, MoAF has a strong team and is delivering the REDD readiness activities on schedule ensuring to develop a robust in-house capacity for leading on a number of readiness analytical studies. Keeping the current pace of delivery disbursements are likely to reach if not exceed 50% by mid-term, one of the eligibility main criteria for the \$5 million in additional funding. As part of the Readiness activities, the RGoB has completed data collection for the National Forest Inventory. One of the underlying studies under the REDD+ Readiness - to assess the drivers of deforestation and forest degradation- is ongoing with plans to contract a number of consultancies in Q2. As part of the Readiness, the Secretariat is in the process of developing a pilot PES system for the Bhutan Sustainable Hydropower Development Policy that has a provision to support Environmental Services.

KEY PARTNERS

Ministry of Agriculture and Forests

BHUTAN: SUSTAINABLE DEVELOPMENT OF HYDROPOWER

KEY DATES:

Approved: September 9, 2015
Closed: June 30, 2016

FINANCING IN MILLION USDOLLARS:

Financier	Financing	Disbursed	Undisbursed
South Asia Water Initiative, Energy Sector Management Assistance Program	0.5	\$0.5	
Total Project Cost	0.5		

**As of August 23, 2016*

BACKGROUND AND OBJECTIVES:

In February 2015, the RGoB requested the World Bank's assistance to carry out an assessment of the environmental and social impacts of the current and future hydropower development in Bhutan. The requested assistance aimed to support the RGoB to prepare a realistic plan for action for implementation of hydropower projects based on absorptive capacity of the economy and social-economic impacts. The study complemented the Macro-economic impact assessment of the Government's planned 10,000 MW hydropower development initiative, also led by the World Bank, thereby providing the RGoB with a complete sustainability analysis and assessment of its planned hydropower development. The development objective was to support sustainable hydropower development in Bhutan at the strategic level through an assessment of Bhutan's policy framework, institutional capacity, and the expected high-level impacts of hydropower development. The immediate objectives of the ESW are to:

- Apply the Hydropower Sustainability Assessment Protocol for one hydropower project in Bhutan,
- Conduct a geographic analysis of potential environmental and social impacts of hydropower in Bhutan
- Conduct a review of the Bhutanese policy framework and the institutional capacity for hydropower development
- Provide advice on how Bhutan could improve environmental and social practices for hydropower development.

KEY ACHIEVEMENTS:

- The project has identified and documented main gaps in the current planning and management, including the absence of basin planning and cumulative impact assessments of hydropower development in Bhutan. The interim results of the study (Interim Report, November 20, 2015) was an important input to a 2-day discussion on the country's capacity to develop hydropower in the 16th Session of the National Council (the Lower Chamber) of RGoB.
- The identification of these gaps led to concrete recommendations, which were presented at a workshop on April 12-13, 2016, for more than 50 participants from key ministries, hydropower developers, and NGOs. Key recommendations, including urgently conducting national studies relating to cumulative impacts and improving guidelines for preparation and implementation of hydropower, were agreed, and were summarized in the Final Project Report: Managing Environmental and Social Impacts of Hydropower in Bhutan (June 15, 2016)
- A request for conducting planning studies for hydropower development, including the cumulative impact assessments on the national scale and improved guidelines, has been requested by the RGoB (Letter to World Bank January 15, 2016), which led to a new technical assistance project. The new Hydropower Policy, currently being drafted by the Department of Hydropower and Power Systems (DHPS), is being informed by the results of this project;

IMPLEMENTING AGENCY:

Department of Hydropower and Power Systems, National Environmental Commission, Gross National Happiness Commission.

BHUTAN: HYDROPOWER SUSTAINABILITY SUPPORT

KEY DATES:

Approved: May 19, 2016
Closing: January 31, 2018

FINANCING IN MILLION USDOLLARS:

Financier	Financing	Disbursed	Undisbursed
Water Partnership Program	0.7	0.1	0.6
South Asia Water Initiative	0.3	0	0.3
Total Project Cost	1.0		

**As of August 23, 2016*

BACKGROUND AND OBJECTIVES:

The recent review of management of environmental and social (E&S) impacts of hydropower in Bhutan concluded that despite awareness and a good regulatory framework, challenges remain in upstream planning and in the implementation of the assessment and mitigation of impacts, mainly due lack of capacity among key governmental institutions to quality assure and enforce good practices. The focus on developing hydropower as the main revenue for the RGoB has also given concern of being too dependent on only one sector. The Bhutan Development Update 2015 highlighted that the low growth rate of only 2 percent in 2013 was partly caused by delays in the construction of some of the major hydropower projects due to geological challenges. This indicates that technical sustainability of the hydropower development is important for the economic growth. Given the significance of hydropower for the economy of the country, and the rapid pace with which Bhutan intends to develop its hydropower potential, the RGoB has therefore realized that it must ensure that the hydropower investments are durable, safe and sustainable to deliver expected power and revenues. The Department of Hydropower and Power Systems (DHPS) is the main governmental authority responsible for hydropower development in Bhutan. With the rapid development of hydropower now occurring, DHPS must establish rules and ensure that these are followed. As part of this role, DHPS is currently updating the Hydropower Policy for Bhutan. To support the update of the regulatory framework for hydropower development in Bhutan, the RGoB has requested the World Bank for assistance for preparation of guidelines for preparation of hydropower and strengthening and building of institutional capacity.

The development objective is to support sustainable hydropower development in Bhutan by providing guidelines and strengthening institutional capacity for preparing and implementing new hydropower projects. The main outcome will be informed policies and practices for hydropower development in Bhutan. The new Hydropower Policy in Bhutan, being formulated during 2016, will give the overall direction for the guidelines and be influenced by them in turn. The guidelines will provide more details than the Hydropower Policy, especially focused on implementation of the policy advices

KEY ACHIEVEMENTS AND EXPECTED RESULTS:

- The main technical consultant has been procured and project inception has been conducted. A first workshop for a broad range of stakeholders was held in August, 2016, focusing on the methodology and approach for the work.
- Draft guidelines are expected to be presented in February 2017.

IMPLEMENTING AGENCY:

Department of Hydropower and Power Systems, under the Ministry of Economic Affairs

PARTNERS:

A task force has been created including key stakeholders, such as Druk Green Power Corporation, Bhutan Power Corporation, National Environmental Commission, and Bhutan Electricity Authority

BHUTAN: IFC'S INVESTMENT IN ZHIWA LING HOTEL

KEY DATES:

Approved: June 16, 2015

Effective:

Closing:

FINANCING IN MILLION USDOLLARS:

Financier	Financing	Disbursed	Undisbursed
IBRD			
IDA			
Other – IFC	3.5	1.5	0
Total Project Cost	3.5		

**As of August 23, 2016*

BACKGROUND AND OBJECTIVES:

Zhiwa Ling Hotel has been operational since 2005. It is a locally owned and operated 45-room five-star property located in Paro. The investment of \$3.5 million to expand the Zhiwa Ling Hotel is the first external commercial borrowing by a private-sector entity in Bhutan and has involved significant legal work and very close government engagement.

EXPECTED RESULTS:

The project will contribute to the development of the tourism sector in Bhutan. More specifically it will:

- Have a catalytic effect with regard to attracting private investment into Bhutan in general and to high-end hotels in particular;
- Help create jobs;
- Support the government's "high value - low impact" approach to expanding the tourism sector in Bhutan by attracting high spending, environmentally conscious and culturally interested visitors to the country;
- Transfer international best practices in hotel management – including service and quality standards, occupational health and safety, and environmental management – from an experienced sponsor to the emerging Bhutanese tourism industry;
- Encourage utilization of a significant proportion of goods and services required by the resort guests from local sources, which will help develop the local supply base and encourage the growth of SMEs;

KEY PARTNERS:

Zhiwa Ling Hotel, Paro.

