

NATIONAL REPORT

Mid-Term Review of the Vienna Programme of Action for Landlocked Developing Countries for the Decade 2014-2024



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*Gross National Happiness Commission
Royal Government of Bhutan*

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1. INTRODUCTION

Bhutan is a small landlocked least developed country, located in the ecologically fragile Himalayan Ranges, nestled between India and China. It has a resident population of 727,145 (PHCB 2017). Guided by the visionary leadership of our monarchs and people centered development philosophy, Bhutan has witnessed rapid socio-economic development over the last five and half decades. Most of the Millennium Development Goals were achieved by 2015. Poverty has been reduced from 31.7 percent in 2003 to 8.2 percent in 2017. Access to education and health services have improved, and resulted in positive outcomes in terms of reduction in mortality rates and higher learning outcomes. Living standard has improved manifold, and both rural and urban infrastructures have improved.

Bhutan is also home to a total of 677 glaciers and 2,794 glacial lakes and has experienced no less than 21 glacial lake outburst floods in the last 2 centuries of which, 4 outbursts were reported in the last forty years. It lies in the seismic zones IV and V and is thus highly vulnerable to landslide, floods, windstorm, and forest fires. It is one of the world's youngest democracies with parliamentary democracy introduced in 2008. Bhutan cannot escape its geographic realities of being a small landlocked nation with a small population surrounded by economic giants and the particular challenges as well as opportunities that these conditions pose.

2. MAINSTREAMING OF THE VIENNA PROGRAMME OF ACTION INTO THE NATIONAL DEVELOPMENT PLAN

Gross National Happiness (GNH) as the development philosophy continues to guide the overall socio-economic development framework of the country. GNH is a multi-dimensional development framework that places people at the centre of development. The multi-dimensional concept of GNH has been translated into a practical guideline for development through the identification of strategic thematic areas known as the four pillars of GNH. The four pillars are: sustainable and equitable socio-economic development; preservation and promotion of culture; conservation and sustainable utilization and management of environment; and promotion of good governance.

Bhutan plans against a five-year horizon, with subsequent Five-Year Plans providing the framework to prioritize development actions and direct domestic and international investment. These plans are guided by Bhutan's Vision 2020, which will be renewed upon its expiry against a longer time horizon. Bhutan has recently completed the implementation of its 11th Five-Year Plan (2013-2018). The Vienna Programme of Action (VPoA) and its 6 priority areas were integrated in the 11th Five Year Plan and its 16 National Key Result Areas (NKRA). All central agencies and local governments contributed towards the delivery of the NKRA through their respective programs.

The 12th Five Year Plan (2018-2023) will focus on realizing the overarching goal of “a Just, Harmonious and Sustainable Society with Enhanced Decentralization” through the Plan’s 16 National Key Result Areas and Key Performance Indicators. The goals and priorities of the VPoA have also been mainstreamed into the plan and closely resonates with priorities under 12th Five Year Plan NKRA 1: Macroeconomic Stability Ensured, NKRA 2: Economic Diversity and Productivity Enhanced and NKRA 9: Infrastructure, Communications and Public Service Delivery Improved. As the 12th Five Year Plan programs are currently under formulation at the agency and local government levels, there is opportunity to further integrate the VPoA, in particular strategies to achieve its specific objectives, into the central agency and local government programs. Bhutan also plans to graduate from the list of Least Developed Countries on the conclusion of the 12th Five Year Plan period.

3. COHERENCE AND LINKAGES WITH THE POST-2015 DEVELOPMENT AGENDA AND OTHER GLOBAL PROCESSES

As a nation pursuing a holistic goal of maximizing GNH, international frameworks such as Agenda 2030 for Sustainable Development, Addis Ababa Action Agenda and Paris Agreement find a natural place within the GNH framework. They share a common vision of prosperity, where all people and the planet live in peace and harmony, where wellbeing is a primary measure of progress, and where no one is left behind. Bhutan is working towards delivering results against its commitments both at home and abroad.

Following the adoption of the 2030 Agenda for Sustainable Development Goals (SDGs) in September 2015, a rapid integrated assessment conducted by United Nations Development Programme in October 2015, indicated high level of integration of the SDG targets into Bhutan’s development plan. Out of 143 SDG targets relevant to Bhutan, 134 SDG targets were included in the 11th Five Year Plan, excluding targets related to SDG 14 on Life below Water.

While all 17 Goals are important, Bhutan prioritized three SDGs (Goal 1 – No Poverty; Goal 13 - Climate Action; and Goal 15 – Life on Land) for immediate implementation in the 11th Five Year Plan (July 2013-June 2018). These goals were prioritized on the basis of urgency to address the issue (No Poverty), Bhutan’s commitment to the global community to remain carbon neutral at all times (Climate Action); and be a champion and world leader by showcasing Bhutan’s success in terms of biodiversity (Life on Land). Efforts were focused on implementing policies and programs that would have multiple impacts on number of SDGs.

Subsequently, preliminary assessment of the 12th Five Year Plan National Key Result Areas and Key Performance Indicators with the SDGs shows a high level of alignment. The 16 National Key Result Areas are closely related with 16 of the 17 SDGs and close to 100 targets and indicators of

SDGs are aligned with the NKRA and KPIs. Central agencies and local governments will identify SDGs which are relevant to their sectors; and the lead agencies for sectors and local governments have integrated relevant SDGs into their key results areas.

In March 2015, Bhutan achieved a key development milestone as it was found eligible for graduation from the UN's list of Least Developed Countries (LDCs) for the first time during the 2015 triennial review of the Committee for Development Policy (CDP). Bhutan fulfilled the threshold levels for the Gross National Income (GNI) per capita and Human Asset Indicator (HIA) criterion but did not meet the threshold for the Economic Vulnerability Indicator (EVI). As Bhutan continued to meet the thresholds in the same two criteria, the CDP during its March 2018 Triennial Review recommended Bhutan for graduation from the list of LDCs to the ECOSOC. The final decision on Bhutan's graduation from the LDCs along with the decision on the transition period will be taken during the United Nations General Assembly session in the latter part of 2018.

A standard transition period of 3 years is granted to a graduating country once the decision to graduate is taken. However, the Royal Government had conveyed to the CDP the need for a longer transition period of 5 years to coincide with the completion 12th Five Year Plan. The 12th Five Year Plan, being the last plan before graduation, focuses on enhancing productivity, diversifying growth, bringing about gainful employment and stimulating private sector growth towards creating a more resilient economy. The longer transition period was requested to address the last mile challenges in all sectors to ensure sustainable graduation. Graduation will be approached in the context of achieving the VPoA, Istanbul Programme of Action and the 2030 Agenda for Sustainable Development. If the request for the longer transition period is granted, Bhutan will be graduating from the United Nations' list of LDCs in 2023.

4. ASSESSMENT OF KEY ECONOMIC, SOCIAL AND ENVIRONMENTAL DEVELOPMENT TRENDS

The social, economic, and environmental dimensions of sustainable development are integral elements of Bhutan's development framework reflecting deep interdependencies that exist between people's welfare, the nation's prosperity and environmental protection. Nearly 60 percent of the population relies on agriculture to make a living, while economic growth is highly dependent on hydropower fed by the Himalayan rivers.

In the 11th Five Year Plan, Bhutan made tremendous progress in reducing both income and multidimensional poverty. Income poverty reduced from 12 percent in 2012 to 8.2 percent and multidimensional poverty more than halved to 5.8 percent from 12.7 in the same period. The GNH Survey 2015 revealed that living standard of Bhutanese had improved from 10.3 percent in

2010 to 11.0 percent in 2015. Within the three indicators under the living standard domain, the most significant change was witnessed in the housing indicator which had increased by 12 percent, followed by assets at 7 percent and household per capita income at 6 percent.

Several targeted interventions were developed and initiated to reduce poverty such as the Rural Economy Advancement Program (REAP), Targeted Household Poverty Program (THPP) and National Rehabilitation Program (NRP). However, despite the progress made, targeting the poorest of the poor and addressing the last mile needs, and securing adequate funds are expected to challenge future poverty reduction programs.

Since conservation and sustainable utilization and management of environment is one of the pillars of GNH, Bhutan has always maintained a balance between development activities and conservation of the environment. This has been acknowledged through our commitment to remain carbon neutral in the 2009 Conference of Parties in Copenhagen and further reaffirmed in 2015 Paris agreement. As per Article 5.3 of the Constitution, 'a minimum of sixty percent of Bhutan's total land shall be maintained under forest cover for all time.' As such, currently, 71 percent of the country's total area is maintained under forest cover of which 51.4 percent accounting to 16,396 sq. km as protected areas, 8.6 percent as ecological corridors and the royal botanical parks constitutes another 0.1 percent. However, the growing population with a skewed distribution, the limited arable land, and the topography are expected to exert increasing pressure on the environment.

In the economic frontier, Bhutan experienced an average growth rate of 5.59 percent over the period 2013 (2.14 percent) to 2016 (7.99 percent), and is projected to have a growth rate of 6.88 percent in 2018. The sustained level of economic growth has translated into significant progress in terms of human development, poverty reduction, and an overall improvement in living standard. The Gross Domestic Product (GDP) per capita increased from USD 2,464 in 2013 to USD 2,879 in 2016. The foreign reserves position improved from USD 916.86 million in 2013 to USD 1,140 million as of June 2018. The inflation rate has been reduced from 8.77% in 2013 to 4.96% in 2017.

The growth was largely driven by the industry sector, particularly the construction sector at 13.3 percent in 2016. Bhutan continues to evolve into a modern economy with the industry and services sectors growing more rapidly than the agriculture sector (primary sector). The share of the primary sector reduced from 27 per cent in 2000 to 16.5 per cent in 2016. On the other hand, the shares of secondary and tertiary economic sectors have grown from 35 per cent to 41 percent and 38 per cent to 42 per cent respectively, during the same reporting period.

Through the adoption of the Economic Development Policy 2016, priority areas referred to as the “Five Jewels” which consist of hydropower, agriculture, cottage and small industries, tourism and mining, have been identified for their potential to generate revenue and create employment. A set of broad strategies including diversification of exports and economic base, development of ‘Brand Bhutan’ and industrial cluster approach is set to propel the development of these select priority sectors.

While the economy has experienced stable growth rates over the plan period, Bhutan faced significant challenges in diversifying its economy, in part because of the inherent constraints associated with being landlocked with a small population. Institutional setbacks such as lack of policy coherence, coordination and slow implementation progress in major programs continued to deter the growth of private investment. Lack of adequate infrastructure, land, access to finance and issues associated with labor market were prominent binding constraints faced by the private sector. In addition, the country’s debt to GDP ratio increased to almost 117 percent by mid-2016, and trade deficit of 25 percent of GDP.

Moreover, the growth did not translate into meaningful employment for youth. Although the overall unemployment rate stood at 2.4 percent, the youth unemployment rate posed a serious challenge to Bhutan over the period. The youth unemployment rate rose from 9.4 percent in 2014 to 10.6 percent in 2017, despite adoption of various strategies such as the Guaranteed Employment Scheme (GES) and other employment service including entrepreneurship trainings. This trend is likely to continue with increasing number of young graduates entering the job market yearly. Therefore creating more jobs, accelerating youth entrepreneurship and improving the productive capacity of the economy are national priorities. To this effect, CSI development, organic agriculture, rural enterprise development, and business start-ups have been identified as key initiatives in the 12th Five Year Plan.

5. PRIORITY AREA 1: FUNDAMENTAL TRANSIT POLICY ISSUES

- Bhutan’s Customs Act 2015 seeks to bring its customs rules and regulations into line with best international practice as recommended under the VPoA. Bhutan is now implementing an Automated Customs System allowing the electronic declaration of goods and advanced paper management.
- Acknowledging the international importance of dry ports, Bhutan has initiated the process of accession to the *Intergovernmental Agreement on Dry Ports* to improve operational efficiency and enhancing the environmental sustainability of transport. A mini ‘dry port’ facility, which is the first dry port facility in the country, is currently being constructed under the ADB-South Asian Sub-regional Economic Cooperation road connectivity project at Phuntsholing to speed up the transit of goods. Three more dry port

infrastructures are being explored in the Southern border areas (Pasakha, Nganglam, and Gelephu).

- Bhutan is considering accession to the *Framework Agreement on Facilitation of Cross-Border Paperless Trade in Asia and the Pacific*.
- The India-Bhutan bilateral trade treaty signed in July 2017 will enhance Bhutan's access to countries beyond India. The treaty permits a wide range of Bhutanese goods destined for third-party markets to transit India without paying Indian duties.
- Initiatives have been undertaken to improve trade links between Bhutan, India, Nepal and Bangladesh across the north-east of the Indian sub-continent. For example, Bhutan is a member of BIMSTEC (Bay of Bengal Initiative for Multi-sectoral Technical and Economic Co-operation), and has also signed a bilateral Trade and Economic Co-Operation Agreement with Nepal. Within the framework of BIMSTEC, members are working towards adoption of an Agreement on Cooperation and Mutual Assistance in Customs Matters for BIMSTEC.
- Bilateral talks with Bangladesh on transit agreement are at an advanced stage to deepen trade relations, and give Bhutan better access to Chittagong and Mongla ports in Bangladesh. In addition, Bhutan is seeking to improve access to waterways connected to the Brahmaputra river, which could link Bhutan directly to Chittagong. Bhutan is also exploring the possibility of acquiring a railway connection as part of an extended rail transport system linking the four 'north-eastern' countries together.

6. PRIORITY AREA 2: INFRASTRUCTURE DEVELOPMENT AND MAINTENANCE

Expansion and modernization of transport, energy and communication infrastructure network is an essential component of Bhutan's growth strategy. Promoting synergy and integration across these infrastructures is expected to bring about significant economic gains through enhanced efficiency and cost effectiveness.

Transport

- Recognizing the importance of access and connectivity in facilitating and delivering socio-economic services, the Royal Government has focused on improving both surface and air transport services.
- As of June 2018, more than 18,396 kilometers of roads have been built, linking the capital—Thimphu with the central and eastern districts, and a series of north-south connections to the Indian Border, including the main access between Thimphu and the international border at Phuentsholing. All districts are connected by blacktopped motorable roads forming part of the National Highway Network.
- To improve connectivity, as of June 2018, 180 Gewog Centres (GC) roads have been blacktopped, 11 new GC roads are under construction, and 147 Gewogs have been

connected with public transport. 11,196 kilometers of farm roads have also been built across the country.

- With regard to air transport, up gradation of facilities of the two domestic airports in the east, and expansion of Gelephu domestic airport in the south will facilitate integration of regional trade and business for larger economic gains. Establishment of helicopter services further strengthened the sector.
- To meet the objectives of “Bhutan Transport 2040: Integrated Strategic Vision”, the Royal Government updated its National Transport Policy to provide for an ecosystem approach to promote sustainable and inclusive transportation that is safe, reliable, accessible and affordable, encompassing land, air, and water transport.
- To accelerate the implementation of this strategic vision, Bhutan is working towards a low-emission transport system, with priority on electric vehicles through the establishment of a network of quick charging stations and provision of other incentives in the 12th Five Year Plan.
- A Nationally Appropriate Mitigation Action plan for transport is in place seeking investments. With air pollution on the rise, a tripling of light vehicles on the road since 2005, and the population of the capital set to double by 2040, investing in a green transport system for the future will be fundamental to realize Bhutan’s carbon neutral promise. Possibility of introducing Bus Rapid Transit to reduce light vehicles and decongest core cities will also be explored in the 12th Five Year Plan.
- Given the importance of maintaining high quality road infrastructure owing to geographical rugged terrain, approximately Nu.1254.449 million, equivalent to \$17.9 million, was spent on road maintenance in the 11th Five Year Plan with an average of Nu.250 million, equivalent to \$3.57 million, per year.
- Despite the progress made, as a landlocked country situated in a geographically difficult terrain, transportation poses a challenge both within and beyond Bhutan’s border. This has resulted in higher cost of trade, construction and production. These challenges hinder Bhutan’s ability to pursue greater regional and international connectivity for greater market integration.

Energy and ICT

Energy:

- Affordable, reliable and renewable energy is key to sustainable development and the transition to a modern society. Power generation in Bhutan relies on hydropower to meet the domestic and industry demand, and has underpinned the economy’s rapid growth. As of 2017, 96.6 percent of the households in Bhutan use electricity as the main source of energy for lighting.
- While Bhutan has an estimated hydropower potential of 30,000 MW, only 23,760 MW is techno-economically feasible, and the current installed capacity is 1448 MW. 70 percent

of the total power generated is exported to India, however during the dry season when the river flow reduces, Bhutan cannot meet its own peak system demand necessitating energy import from India. This is expected to ease with the commissioning of the Punatsangchhu I & II and the Mangdechhu hydro projects, which will bring the total installed capacity to around 5000 MW by 2020.

- Bhutan Sustainable Hydropower Development Policy 2008 provides a framework and guidelines for sustainably harnessing hydropower energy. However, the sustainability could be hampered by adverse impacts of climate change.
- The Alternative Renewable Energy Policy has been adopted to diversify sources of energy and promote alternative sources of renewable energy. The policy aims to generate 20 MW from various technologies by 2025. The country has installed a 600 kW wind power plant on a pilot basis that electrifies 300 households. A domestic feed in tariff policy is under formulation. Further, to encourage use of renewable energy, rural households are provided with 100 units of free electricity a month.
- To reduce dependency on import of energy for household needs and improve energy security, the country has so far promoted use of energy efficient cooking stoves and installed about 4,403 biogas plants. Other initiative includes promotion and distribution of Light Emitting Diode (LED) bulbs nationwide at subsidized rates.
- Demand-side management of energy and improvements in the energy performance standards have been carried out in the areas of industry, transport, buildings and appliances through adoption of energy efficiency and conservation standards.
- At the regional level, given the benefits of optimal sharing of the limited energy resources, especially in the field of hydropower energy, a trilateral cooperation among Bhutan, Bangladesh, and India for investment in hydropower project is being discussed.
- Furthermore, National Energy Efficiency and Conservation Policy has also been drafted to ensure sustainable use of energy across all sections of the consumers and to encourage general improvements in the energy performance standards of four major sectors of industry, transport, buildings and appliances.
- Despite the progress made in harnessing renewable energy, challenges remain. The impact of climate change on hydropower sector would have dire consequence and is vulnerability for Bhutan. Successfully ensuring access to affordable, reliable, sustainable and climate resilient infrastructure through scaling the above initiatives will require significant investment in terms of human resources, and technology transfer. The Royal Government will continue efforts to improve the investment climate through review of relevant policies and regulatory frameworks to attract financing.

ICT:

- Seamless information exchanges that are affordable and available all the time to all is the basis for an efficient and interconnected business environment, people-to-people connectivity, efficient resource-use as well as transparent governance. Bhutan's focus in

recent years has been on strengthening ICT infrastructure such as fiber optic connectivity, government intranet system and national data center. Critical infrastructure such as optical ground wire (OPGW) national backbone, fiber optics and internet connectivity are already laid out in all the 20 districts.

- Recognizing Telecommunications and Broadband as important contributors to the socio-economic development of the country, the Bhutan Telecommunications and Broadband Policy was approved in 2014. The Bhutan Telecommunications and Broadband Policy 2014 has been guiding and shaping the development of telecommunications and broadband sector in the country. The main objectives of the policy are: connectivity for all, strengthening of rules and regulations, creation of conducive environment for private investments and competition leading towards an efficient market and affordable broadband and telecom services.
- Today, all 20 Districts and 205 blocks have access to cellular connectivity; internet and broadband penetration in all 20 Districts is up to 75%; Government to Citizen services consist of 155 e-services and 19 m-services and three out of five banks in the country provide e-payment services.
- In addition, electronic-government interoperability framework and enterprise architecture to enable efficient sharing of information has been developed.
- Bhutan has developed its first Tech Park with support from multilateral donors and Public Private Partnership with the objective of employment generation and promoting knowledge-based society. The park also serves as innovation hub for startup businesses.
- To foster innovation and ICT enabled growth, Bhutan is investing in Start-Up innovation camps and has established a Business Start-Up Center in the capital.
- Despite the progress, the use of the Internet is still low in the country. In the Inclusive Digital Index, an indicator that measures 7 aspects of ICT and telecommunication namely mobile cellular subscriptions, international Internet bandwidth, households with computer, households with Internet access, individuals using the Internet, broadband subscriptions and mobile broadband subscriptions, Bhutan ranked 121 (out of 178 countries) with IDI value at 3.69 (out of 10) in 2017, a drop from rank 119 in 2016.
- During the 11th Five Year Plan, the Royal Government undertook intensive projects targeted towards development of ICT infrastructure. The primary focus of these programs was to improve accessibility, affordability, reliability and security of ICT and telecom services, and also to empower ICT sector within the country. The 12th Five Year Plan will focus on consolidation ICT related infrastructure to improve public service delivery through the Digital Drukyl Flagship Program.

7. PRIORITY AREA 3: INTERNATIONAL TRADE AND TRADE FACILITATION

International trade

- Given our small domestic market with limited scope for expansion, building export capacity is essential in view of Bhutan's vision for sustainable growth and economic self-reliance. While the export structure has undergone some degree of transformation during the four decades from primary based exports to higher value-added products, the export basket remains highly concentrated with narrow range of commodities. The top ten export commodities constituted an average 81.5% of the total export during the period 2012-16. The composition of export basket at product level is largely dominated by few range of products besides electricity, namely: Ferro-silicon, Steel, Portland cement, Calcium Carbide, Silicon Carbide, Cardamom, Dolomite, and Gypsum. With an average share of 82% of the total trade, India has been the major trading partner for decades. In 2016, export to India constituted 85.58% of the total export followed by Bangladesh at 10.79%. In terms of import, India alone accounted for 82% of the total imports last year.
- A Diagnostic Trade Integration Study was conducted with support from the Enhanced Integrated Framework (EIF) in incorporating trade into the national development strategy. Key strategies include diversification of export markets, trade liberalization, private sector and infrastructure development, and institutional and professional capacity development.
- Bhutan adopted the Economic Development Policy 2016 which provides the strategic direction for growth and key guiding policy in Bhutan's drive towards economic diversification through development of sectors that have the highest potential. The EDP has a total of 252 Policy provisions and provides the overall enabling environment to continue creating a transparent and conducive environment for business and investment in the Bhutanese economy.
- In addition to creating an enabling environment for private sector growth, the Royal Government continues to emphasize on prioritizing the Five Jewels of the economy, namely-Hydropower, Tourism, CSIs, Mining and Agriculture; enhancing service delivery and reducing administrative burden for businesses; diversifying exports and enhancing productivity; and progress towards becoming a knowledge based and self-reliant society.
- To complement the EDP 2016, the Parliament of Bhutan enacted the Fiscal Incentives Act of Bhutan 2017. This Act effectively grants fiscal incentives in the form of both direct and indirect tax exemptions and concessions to stimulate economic growth, foster private sector development and generate employment. Incentives and exemptions ranging from income tax holiday, reinvestment allowance, tax rebate, income exemption, additional expenditure deduction, TDS exemption, sales tax exemption, customs duty exemption, and concessional customs duty have been granted. The general incentives are applicable to all the sectors of the economy and the sector specific incentives are applicable to the priority sectors identified under the EDP including the Five Jewels.

Trade facilitation

- Bhutan currently maintains observer status at the WTO to allow national stakeholders to gain better understanding of the multilateral trading system. Nonetheless as part of the accession process, four Working Party Meetings were held followed by two subsequent informal meetings. Efforts to create awareness on WTO for the benefit of the businesses and general public, including NGOs continue to be made.
- A national level committee on trade facilitation was instituted under the title “National Trade and Transport Facilitation Committee” with participation of all relevant stakeholders including representatives of the private sector. The committee aims to engage the core public and private sector trade facilitation stakeholders in the country to identify and address legal and regulatory obstacles and bottlenecks in the import and export process, and ensure proper coordination and smooth implementation of the cross-sectoral trade facilitation program.
- Bhutan National Single Window for international trade has been identified as one of the key initiatives in the 12th Five Year Plan to provide seamless end to end facilitation of cross border trading. The online system will streamline procedures between traders and government agencies in order to reduce time and cost whilst enforcing required controls.

8. PRIORITY AREA 4: REGIONAL INTEGRATION AND COOPERATION

Bilateral Level:

- Bhutan has a bilateral Free Trade Agreement with India. The agreement was originally signed in 1972, and since then, the agreement has been renewed five times (1983, 1990, 1995, 2006 and 2016)
- Besides India, Bhutan has a bilateral preferential trade agreement with Bangladesh, a bilateral economic cooperation agreement with Thailand and is also pursuing a bilateral trade agreement with Nepal.

Regional Level:

- Bhutan is a founding member of the South Asian Association for Regional Cooperation (SAARC) and is part of the South Asian Free Trade Area (SAFTA) and the Trade Liberalization Programme under SAARC. To take the process of regional economic integration further, the scope of SAFTA has been expanded to include trade in services, enhanced investment and harmonized standards, and customs cooperation.
- Bhutan is a member of BIMSTEC (Bay of Bengal Initiative for Multi-sectoral Technical and Economic Co-operation) and is part of the Framework Agreement on the BIMSTEC Free Trade Area (FTA), which was signed on 8th February 2004 to stimulate trade and investment, increase intra-regional trade, and to enhance trade and investment in BIMSTEC member states by other countries. Bhutan actively engages in negotiation

through the BIMSTEC Trade Negotiation Committee (TNC) for the fulfillment of the obligations arising from the Agreement such as the tariff elimination schedule, reduction of the negative list and other responsibilities resulting from the on-going negotiations.

- Bhutan is also part of the BIMSTEC Chamber of Commerce which was founded in 2003 to coordinate between the private sectors in BIMSTEC member states and organize the Business Convention meetings
- In terms of regional investment cooperation, Bhutan has, so far, been able to attract 21 FDIs from BIMSTEC member countries with concentration in hotel services and manufacturing industries.

Multilateral Level:

- Bhutan is an observer to the World Trade Organization.

9. PRIORITY AREA 5: STRUCTURAL ECONOMIC TRANSFORMATION

- Bhutan launched its first Five Year Development Plan in 1961 with a focus on development of basic infrastructure aimed at reducing Bhutan's physical isolation by building transportation links and improving internal communications. The development priorities have evolved from building up basic infrastructure to investment in services and boosting the economy. In the last 10 years alone, the GDP in Bhutan has more than tripled and per capita income has increased to \$2879.07 as of 2016. Sectoral share of agriculture has gone down from 43% to 17% while share of industry has increased from 12% to 41% reflecting the structural transformation of the economy. Under the services sector, tourism sector has emerged as one of the major sources of foreign exchange.
- Bhutan's industrial sector has been largely driven by hydropower and construction. Economic growth was sustained by the growth of construction sector (10.33 per cent) in 2017. Other industry sub-sectors recorded modest growth: the manufacturing sub-sector remains relatively small accounting for only about one-fifth of the industrial sector. The narrow-based manufacturing sector is also dominated by a small number of major operators and a larger number of small manufacturing plants concentrated in the food processing activities and cottage industries. In general, the manufacturing sector in Bhutan is locked into relatively low value-added products. Furthermore, with a resident population of only 727,145, the small size of domestic market offers limited opportunities to harness economies of scale for production. Capacity constraints and negligible investment in the area of science, technology and innovation are major constraints facing the Bhutanese economy.
- Bhutan has adopted numerous key policy instruments such as the Economic Development Policy 2016, the FDI Policy 2016 and the Public Private Partnership Policy 2016 in order to boost investment in key sectors, attract investors and create a greater role of the private

sector. The Priority Sector Lending Regulations was operationalized in 2018 to incentivize flow of credit to the CSI sector. Bhutan has also established a Stabilization Fund to create macroeconomic stability and long-term fiscal sustainability. The Fund will support counter-cyclical measures during business cycle fluctuation and economic crisis, and smoothen public expenditure during times of high revenue volatility.

- Programs like the One Gewog One Product (OGOP) that promote production of authentic Bhutanese produce for both domestic and international market, contribute to poverty alleviation, improve rural livelihood, and promote entrepreneurship among the Bhutanese people have been successfully initiated and will need to be scaled up. The program covers the entire value chain ranging from production, value addition, and standardization to marketing.
- Bhutan faces significant challenges in diversifying its economic base mainly because of the inherent constraints associated with being landlocked and small population. While efforts to tap hydropower will continue, Bhutan needs to expand investments in tourism, organic agriculture, and cottage and small industries. Initiatives will also need to be undertaken in establishing 'entrepreneurship ecosystem' to provide platform for innovation to generate green jobs, promote green economy through attraction of green investments, with participation of corporate and private sectors. Bhutan aims to keep unemployment under 2.5 per cent, increase share of national revenue from non-hydro sectors to over 75 per cent and attract approximately Nu. 10 billion (\$150 million) in FDI into non-hydro sectors in the 12th Five Year Plan period.

Private Sector Development

- The Royal Government recognizes the importance of private sector development as driver of growth, employment generation and sustaining economic development.
- The implementation of Economic Development Policy (EDP) 2016 is one of the most important policy enablers that has been instituted to provide the overall enabling environment for conducive economic development and lay out clear strategies ranging from incentives to policies and financing to enable private sector growth in sectors of high potential.
- Policy instruments to facilitate private sector development in Bhutan have been put in place such as the Fiscal incentives, Licensing Policy 2015 and Public Private Partnership Policy 2016.
- Better Business Council was established in June 2014 to provide a platform for promoting better public-private dialogue to strengthen business environment. The council is tasked with the objective of encouraging entrepreneurship, improve access to finance and skilled labor, FDI and enhance ease of doing business.

- An Economic Stimulus Plan with a budget of Nu.5 billion, equivalent to USD 86.2 million, was instituted to stimulate investment and promote priority sector lending to enhance production, generate employment, increase exports and substitute imports.
- Priority Sector Lending scheme was introduced in 2017 to promote cottage and small industries. The Scheme provides an integrated platform that coordinates interventions from several government agencies to stimulate the CSI sector through improved access to finance. Under the Scheme, financial institutions have been mandated to meet their annual incremental priority sector lending targets.
- Small domestic market, shortage of professionals, lack of skills and low productivity of labor are some of the challenges for growth of businesses and private sector.

10. PRIORITY AREA 6: MEANS OF IMPLEMENTATION

Domestic resource mobilization:

Bhutan's five-year plan financing thus far have been sourced mainly through ODA and domestic resources. With prudent fiscal management, the Royal Government is able to finance up to 64 percent of its development expenditure through domestic revenue. Domestic resource mobilization was given the highest priority as manifested through the 11th Five Year Plan's objective of self-reliance. Some of the efforts put in place to mobilize resources from domestic sources are broadening the tax base including green tax and sales tax on vehicles and fuels, rationalization of recurrent expenditure, enhancing efficiency of state owned enterprises and fostering public private partnerships. Other financial instruments such as bonds and capital market are also explored to supplement financing of our commitments. Bhutan is also implementing the Bhutan for Life Program, an innovative green financing mechanism to augment its resource requirements for conservation of Environment.

Official development assistance:

ODA funds about 34 percent of Bhutan's development, and Bhutan has been effectively utilizing ODA to the maximum benefit. With sound governance and conservation policies in place, Bhutan has been successfully implementing international finance commitments. As Bhutan sets to graduate from LDC by 2023, the 12th Five Year Plan as the transition plan for graduation will require continued ODA.

Foreign direct investment:

Despite enormous efforts in attracting FDIs through policy reforms and provision of incentives, Bhutan has had limited success in attracting global investors. In 2015, the FDI net inflow into Bhutan was reported to be only 0.4 per cent of GDP. The net FDI inflow per capita in Bhutan is even further behind the average level of South Asian countries, LDCs and Asian LDCs. However, efforts are underway to improve ease of doing business and creating a favorable investment climate by investing heavily on infrastructure, energy, transportation and Government to Business services. Bhutan's rank in the Ease of Doing Business has improved from 148 in 2013 to 75 in 2017. FDI Policy 2010 was also amended in 2014 to further improve the investment climate in Bhutan.

South-South cooperation:

Bhutan has accorded importance in building and strengthening bilateral ties with other countries that share common aspiration and interest. Through this process, depending on the relevance and interest of the participating countries, Bhutan has initiated and implemented cooperation in the areas of economic, social, cultural, environmental and technical frontiers. Some of the priority cooperation areas for Bhutan are i) agriculture and rural development, ii) sustainable tourism, iii) agri-business, iv) technical and vocational education, v) human resource development, and vi) disaster management. In order to promote south-south cooperation, Bhutan has used mechanisms such as bilateral ties, regional mechanisms such as South Asian Association for Regional Cooperation (SAARC) and multilateral mechanisms such as the UN and multilateral development banks.

11. MONITORING OF IMPLEMENTATION AND REVIEW

The Royal Government considers monitoring and evaluation as critical development management measures for effective implementation. The success and effectiveness of development efforts are contingent on devising a coherent plan with measurable indicators and targets underpinned by a sound theory of change.

Recognizing this, Bhutan follows a results-oriented planning approach based on the principles of theory of change in formulating its five-year plans and programs. On an annual basis, the five-year plans and programs are translated into annual performance objectives with measurable performance targets at agency level which are further cascaded down to activities for individual civil servants in their work plans.

Alignment of aspirations, actions and resources is considered key to ensuring effective delivery of results of plans and programs. Annual budget is allocated as per the annual performance

objectives of implementing agencies. Upon approval of the performance objectives and budget, annual performance agreements are signed between the Head of Government and respective heads of agencies including the local governments.

Monitoring and evaluation is based on clearly formulated five year plans and programs and agreed annual performance targets. The monitoring and evaluation of the implementation of VPoA is conducted in a manner that is harmonized with the monitoring and evaluation of the Plan to avoid duplication of efforts. GNH Commission is the apex body for monitoring, implementation and review of VPoA.

The priorities and actions of VPoA are aligned with the relevant national, agency and local government key result areas and their KPIs. Since the VPoA will be implemented through the five-year plan, monitoring and review will be carried out following the Royal Government's Monitoring and Evaluation (M&E) system.

The national M&E system framework lays out the institutional set up and procedures required for effective monitoring and evaluation of development plans and programs. It also provides an integrated framework within which the management information systems of Planning, Budgeting, Expenditure Management and Performance Management are deployed to function seamlessly as a unified system, automating workflow processes and producing reports for decision making. As per the M&E system, NKRA's are reviewed in the middle of a Five-Year Plan period and at the end of the Five-Year Plan, while AKRA's, LGKRA's and program outputs are monitored annually through the Government Performance Management System (GPMS). The Royal Government ensures that the national M&E system meets the monitoring and reporting requirements of all its international commitments.

12. CONCLUSION AND WAY FORWARD

Bhutan has made significant progress in the implementation of the VPoA. Bhutan has achieved stable economic growth rates over the last five years, enhanced social development through reduction of both income and multidimensional poverty, and improved infrastructure for access and connectivity. In spite of the progress, various cross cutting challenges still remain. These stem mainly from the inherent constraints associated with being landlocked with a small population, limited economic diversification, high costs of trade and limited regional and international market integration.

Looking forward, the Royal Government will undertake key initiatives in the 12th Five Year Plan to address these developmental challenges. The 12th Five Year Plan will focus on the principle of "Consolidation, Coordination and Collaboration (CCC)" to strengthen partnerships and

coordination among all the sectors and development actors in the country--government, corporations, private sectors and civil society organizations. The following are some of the key initiatives that will be required to overcome the remaining challenges:

National priority actions

- Achieving the VPoA objectives requires economic transformation and productive capacity building. Bhutan will need to expand investment into tourism, organic agriculture, and Cottage and Small Industries. Establishing an entrepreneurship ecosystem to provide platform for innovation to generate green jobs with participation of corporate and private sectors must be a priority.
- In order to address the last mile challenges of eradicating poverty in all its forms, address needs of vulnerable groups, enhance learning outcomes, match demand and supply of skills and ensure gainful employment, especially for the youth, strategic alignment of economic, employment, environmental and social policies must be undertaken. Strategies should include creating conditions to support job creation capacity, especially in SMEs.

Regional and international priority actions

- As a principle of state policy, the Royal Government of Bhutan strives to promote goodwill and cooperation with nations, foster respect for international law and treaty obligations, and encourage settlement of international disputes by peaceful means in order to promote international peace and security. To this end, Bhutan has developed and maintained friendly relations with all countries in the region and beyond.
- To ensure successful implementation of the VPoA, Bhutan will need to continue its efforts to strengthen regional and international partnerships through North-South, South-South and triangular cooperation, particularly in exchanging good practices and technical assistance.
- As a landlocked least developing country, continued support of development partners is of paramount importance to successfully implement the VPoA.
- The Comprehensive High-Level Midterm Review (MTR) of the VPoA should accord special emphasis and support to ensure smooth and sustainable graduation from the list of LDCs. Support to prepare a smooth transition strategy to manage the losses of any LDC related preferences will be essential. Specific aid for production and productive sector development and technical support to enhance national capacity to accessing complex international financing mechanisms particularly in areas of green climate funds will be required before Bhutan's effective graduation.
- Going forward, support in attracting and retaining foreign investment, in particular to high value-added sectors, is required from the UN and specialized agencies. Support to

establish a preferential market access scheme specifically for exports will become important post-graduation.

- The MTR should also accord importance to providing international assistance for enhancing innovation and technology transfers for the LLDCs especially in the areas of research and development.
- Assistance to implement the VPoA in the form of guidance on strategies required to accelerate the process of structural transformation and develop appropriate policy responses that address the special development needs is also required.
- Annual progress reports could be submitted to OHRLLS by the member states that are structured along different themes every year to ensure in-depth progress reporting and more effective monitoring. Specific outcome of the MTR could be the development of an annual progress report format to ensure successful monitoring and implementation of the VPoA.