



# **Annual Report on the Preparation of Bhutan's Transition Strategy for smooth LDC graduation**

**November 2022**

## Background

Bhutan is scheduled to graduate from least developed country (LDC) status in 2023. This is in line with the request to the United Nations for the graduation date to coincide with the end of the implementation of Bhutan's 12<sup>th</sup> Five-Year Plan (12 FYP) in December 2023. Bhutan's graduation was endorsed during the 73<sup>rd</sup> Session of the UN General Assembly held in December 2018.

Bhutan was found eligible for graduation from the UN's list of LDCs for the first time during the 2015 Triennial review of the Committee for Development Policy (CDP) under UN Economic and Social Council (ECOSOC). Bhutan successfully met and fulfilled the threshold levels for the Gross National Income (GNI) per capita and Human Asset Indicator (HAI) criterion. For a country to be recommended for graduation, a country must meet graduation thresholds for two of the three criteria or have at least twice the income threshold in two consecutive Triennial reviews.

### Bhutan's Performance in the Triennial Reviews of 2015, 2018, 2021

Criteria	Thresholds	2015	2018	2021
GNI per capita (US \$)	Graduation Thresholds	1,242	1,230	1,222
	Bhutan's Performance	2,277	2,401	2,542.4
HAI (score)	Graduation Thresholds	66 and above	66	66
	Bhutan's Performance	67.9	72.9	76.9
ECI (score)	Graduation Thresholds	32 and below	32	32
	Bhutan's Performance	40.2	36.3	25.7

### Concise Summary of the consultative mechanism and the support by the relevant United Nations institutions in convening the meetings

The paper prepared by UNCTAD which outlined the key considerations for the Royal Government of Bhutan has indicated that focus of the Government of Bhutan to ensure

smooth transition has to be on implementing measures and strategies within the seven themes or issues such as ensuring macroeconomic stability, expanding trade, building productive capacities and economic diversification, promoting technological advancement, mitigating vulnerability and building resilience, enhancing finances and aid, and sustaining global level support measures and commitment that is extended to LDCs.

The LDC task force comprising representatives from various key agencies related to Bhutan's LDC graduation that was formed in April 2021 led by the erstwhile Gross National Happiness Commission met to discuss the format of the Smooth Transition Strategy for Bhutan's LDC graduation.

The task force recommended integrating the Smooth Transition Strategy into the 13<sup>th</sup> FYP instead of having a separate document. Thus, the preparation of the 13<sup>th</sup> FYP has become the key consultative mechanism for the implementation of the Smooth Transition Strategy.

The concept note for the 13<sup>th</sup> FYP has been prepared by the erstwhile Gross National Happiness Commission Secretariat and consultations with all the relevant stakeholders have been carried out. Consultation with the stakeholders included representatives from autonomous agencies, central agencies, local Government agencies, the already existing political parties, United Nations Country Team and others.

With Gross National Happiness Commission Secretariat now dissolved, the planning mandate of the commission has been put under the Office of the Cabinet Affairs and Strategic Coordination under the Cabinet Secretariat of the Royal Government of Bhutan. Hence, the preparation of the 13<sup>th</sup> FYP is continued with the ultimate objectives to achieve Prosperity, Progress and wellbeing of the People.

The process of the formulation of the 13<sup>th</sup> FYP which will also serve as the strategy for smooth transition of Bhutan has been and will be consultative and inclusive in nature considering all the LDC parameters required to be discussed. Agency wide consultations and engagement of all relevant stakeholders will be ensured in the process of finalizing the 13<sup>th</sup> FYP.

The 12<sup>th</sup> FYP will also be reviewed and nation-wide consultations will be carried out towards the end of the 12<sup>th</sup> FYP for the purpose. The 13<sup>th</sup> FYP will account for the gains and shortfalls of the 12<sup>th</sup> FYP, impacts of COVID 19 pandemic, and provide impetus to the impending graduation from the LDC category in 2023 which coincides with the beginning of the 13<sup>th</sup> FYP.

Assistance has been also received from the UNDESA and UNCTAD in capacity building of Bhutanese officials in mainstreaming resilience-building and smooth transition strategies into national policy-making and in promoting exports through information sharing of new product requirements and markets. Under this project, officials from the erstwhile Gross National Happiness Commission have received the special training by the Committee for Development Policy, dated 17th May 2022 on Innovative Financing and Enhanced Monitoring Mechanism.

### **Information on international support for graduation- commitments on phasing out LDC- specific international support measures**

United Nations organizations and agencies such as the OHRLLS, UNCTAD, UNESCAP and the WFP have committed to provide technical support to Bhutan's smooth transition and to continue support after graduation.

Bhutan is not yet a member of WTO nor has the accession process resumed, soliciting special and differential treatment provisions provided under the WTO framework for LDCs is at a moot point and yet to be discussed.

Bhutan is expected to benefit from certain support measures such as the Enhanced Integrated Framework (EIF), United Nations Capital Development Fund (UNCDF), and the UN Technology Bank in post-graduation up to 5 years.

One of the core concerns remains the cessation of LDC related climate funds. Under the Global Environment Facility (GEF)-the Least Developed Countries Fund (LDCF) will phase out. However, its support rendered through the projects such as 'Enhancing sustainability and climate resilience of forest and agriculture landscape and community livelihood (NAPA III Project)' will continue to progress beyond graduation as there are legal agreements concerning its operations, indicated through the start and end date.

Further, the Royal Government of Bhutan and UNDP-Bhutan are presently working on a project titled 'ACREWAS Advancing Climate Resilience of Water Sector in Bhutan' to access GEF-LDCF, prior to graduation, which if approved shall progress even after Bhutan's graduation.

With regards to the Green Climate Fund- Country Readiness and Preparatory Support Programme, a slight decrease in the country's Readiness share is foreseen. However, Bhutan will be able to access a maximum amount of USD 1 million as it is kept

open for all NDA- National Designated Authorities.

During the 15<sup>th</sup> Round Table Meeting (RTM), the EU confirmed that assistance to Bhutan would continue beyond Bhutan's graduation in 2023. Bhutan will continue to access duty-free quota-free market access for three years after graduation besides the Multi-annual Indicative Programme (MIP) for seven years and MIP+facilitated by the EU.

Development partners such as Japan International Cooperation Agency (JICA) and the Government of India (GoI) will continue to support Bhutan's socio-economic development even after Bhutan's graduation from the LDC category.

### **Implications of COVID-19 on preparations for graduation from the LDC category and preparation of transition strategy**

COVID-19 has had implications on Bhutan's socio-economic sectors. In 2022, the country witnessed two lockdowns from mid-January to March 2022. Although Bhutan is assessed as well on track to graduate based on Bhutan's performance in the triennial review 2021, with Bhutan fulfilling the graduation thresholds for all three criteria, the country's economic situation is yet to fully recover from the impacts of the pandemic.

COVID-19 has contributed to slowing the economic growth of Bhutan and has affected its macroeconomic indicators, for instance Gross Domestic Product (GDP) and Gross National Income (GNI). The GDP growth rate in 2020 suffered a negative growth of 10.08% but in 2021, it grew by 4.1% and is expected to grow by 4.9% at the end of 2022. Similarly, the GNI per capita has seen a drop to USD 3,109.33 in 2019 but it has increased by 4.1% in 2021. Despite the fact that the country's GDP and GNI are showing positive growth, the economy is yet far from achieving macroeconomic stability.

One of the biggest economic sectors of Bhutan i.e tourism came to a complete halt due to the pandemic. The revenue generation from the sector fell by 92 percent with the closure of the international border. With the tourism sector coming to a standstill, more than 50,000 employees working in tourism and allied sectors were displaced. The international border was recently opened on 23<sup>rd</sup> September, 2022 and tourist arrivals in Bhutan have been renewed.

The sector has also undergone transformation in view of further strengthening the Brand Bhutan and to further promote Bhutan as an exclusive high-end tourist destination. A major change in the tourism policy has been the increase in the Sustainable Development

Fee (SDF) for international tourists to USD 200 per tourist per night from the previous fee of USD 65 which was met from the Minimum Daily Package Rate. The gains from the sector are yet to be realized and harnessed.

Bhutan's total debt has also increased due to increasing government expenditure. The total public debt stock of Bhutan stands at Nu 256,993.907 million as of 30 September 2022 accounting for 132.9 percent of GDP. Although the overall risk is deemed moderately manageable, the debt is expected to further increase in the coming years.

With the normalization in the situation and resumption of economic activities, trade flows have picked up surpassing the pre-pandemic threshold. However, the increase in imports has been much higher compared to exports leading to a huge trade deficit of 19.3 percent in the Fiscal Year 2021-22 from 6.9 percent in the fiscal year 2020-21. If a similar trade pattern continues in the upcoming months, Bhutan's trade deficit is projected to further worsen by the end of 2022, with overall import value standing at Nu. 111.3 billion and export at Nu. 60.4 billion.

Since the onset of the pandemic, Bhutan has seen increased imports which have impacted the country's foreign reserve. As of October 2022, the reserve stands at US\$ 792.87 million and it is sufficient to meet 14 months of essential imports. The Government has undertaken immediate measures to safeguard and protect the foreign currency reserves through imposition of moratorium on import of vehicles from 18th August 2022 to maintain a minimum reserve enough to meet the constitutional requirement of maintaining at least one year's essential imports. The reserve is closely monitored so that Bhutan does not suffer from serious reserve shortfalls.

Despite all the undesirable impacts of COVID-19 on Bhutan socio-economic sectors, the pandemic did not bear major hindrances to Bhutan's preparation towards graduation and the preparation of the smooth transition strategy. The formulation of the next plan which will embrace the challenges and measures to ensure smooth graduation and serve as the smooth transition strategy is under progress.

The plan that is in preparation will emphasize and strive to achieve high income status by focusing on trade diversification, enhancing economic opportunities, increasing exports and strengthening productive capacities among others. Since human capital is the ultimate driver of economic growth, focus on honing the economic capabilities of the country's human resources will also be an important focus in the next plan.

### **Information on the Smooth Transition Strategy**

As mentioned earlier, the task force for Smooth Transition Strategy which comprised

members from the agencies related to Bhutan's least developed country status came together to discuss the preparation of the Smooth Transition Strategy in April last year. With UNCTAD's support, the team discussed the draft Smooth Transition Strategy based on UNCTAD's white paper.

The task force reviewed the draft Smooth Transition Strategy and recommended that the strategy be integrated in the next national plan instead of keeping it as a separate document. The strategy provides discussions on the development trajectory, elaborates on the implications of graduations and the loss of international support measures in terms of trade and development, development cooperation, contributions to UN system and travel assistance, and the other vulnerabilities in lieu of the graduation.

To ensure smooth transition and adjust to the post graduation era, the strategy emphasizes on sustaining Bhutan's graduation with momentum, building resilience, addressing remaining structural challenges, and adjusting to the loss of LDC benefits. Towards these ends, focus is on stabilizing the macroeconomic environment by placing due importance on prudent fiscal management plan and implementation of sound debt policy. Trade expansion is proposed as another area for attention which calls for addressing exogenous and endogenous trade challenges such as volatility of global trading system, restrictive customs procedures, supply constraints and inadequacies of trade-related infrastructure, loss of preferences in specific key markets due to graduation, undiversified export basket and export markets.

Other measures include enhancing productive capacities and economic diversification, fostering technological advancement and enhanced human capital development, mitigating vulnerability and building resilience.

As mentioned earlier, the Smooth Transition Strategy will be integrated and mainstreamed in the 13<sup>th</sup> FYP. Compared to the normal times, the plan preparation process has taken an ambitious and transformational mode with major national level reforms and restructuring of the agencies taking place. One of the reform outcomes is that the planning role of the erstwhile Gross National Happiness Commission is merged with Cabinet Secretariat with dissolution of the former, and the new team is currently working on the national level and cluster level objectives and the key performance indicators, process and guidelines of the 13<sup>th</sup> FYP which will soon be completed keeping in mind all the LDC parameters.

Since the 13<sup>th</sup> FYP will also serve as the implementation of a smooth transition strategy, the plan will drive all the sectors to incorporate elements of Bhutan's preparations towards imminent graduation in their agency level programs and plans. Aside from this, the

sectors relevant to Bhutan's graduation will also develop other plans and strategies that will ensure minimal implications with Bhutan's graduation.

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