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Monitoring of countries graduating and
graduated from the LDC category:

Bhutan



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Summary

Bhutan started to recover in 2022 from the significant decline in economic activity caused by the COVID-19 pandemic, returning to the robust pre-COVID growth. The country meets all graduation criteria and continues to make steady progress on GNI and HAI.

Bhutan has submitted its annual report on the preparation of a smooth LDC graduation and has been well responsive to CDP communications. The Committee recommends that the Government continues its efforts to foster economic diversification by supporting the development of small and medium sized enterprises and cottage industries to help expand domestic production and reduce import dependency.

Macroeconomic situation

Bhutan saw robust economic growth over the decade 2010 and 2019 with more than five per cent average annual GDP growth. The economy is closely linked to that of India, which is the source of more than 80 per cent of imports and the destination of more than 80 per cent of exports. The currency is pegged to the Indian Rupee, which has served the country well in terms of maintaining the macroeconomic stability.¹ The period of growth and stability over the past decade has translated into a significant drop in poverty, as the number of people living below the national poverty line has dropped from 23.2 per cent in 2007 to 8.2 per cent in 2017. Revenues from selling hydropower exports and tourism have allowed investment in human capital development with notable improvements in service delivery, education and health. Hydroelectric power production, agriculture, forestry and tourism are the mainstays of the economy.

Table 1. Selected macroeconomic data for Bhutan, 2016-2021

Indicator	2016	2017	2018	2019	2020	2021
GDP growth rate (per cent, constant price)	8.1	4.7	3.1	5.8	-10.1	-3.7
Inflation rate (%)	3.2	5.0	2.7	2.7	5.6	4.2
Government revenue (billions of national currency)	42.0	42.7	52.1	42.0	54.6	59.7
Government expenditure (billions of national currency)	44.7	50.0	56.3	44.1	57.6	59.5
Government balance (billions of national currency)	-2.6	-7.3	-4.2	-2.0	-3.0	0.2
Government balance (per cent of GDP)	-1.9	-4.8	-2.6	-1.2	-1.7	0.1
Net ODA received (millions of US dollars)	51.6	118.5	107.9	178.7	202.4	126.9
Balance of Payments (millions of US dollars)						
Current Account	-622.7	-540.4	-478.2	-500.8	-381.2	-321.5
Goods, Credit (Exports)	496.5	554.6	602.8	609.3	651.9	719.4
Goods, Debit (Imports)	1,029.9	1,025.1	1,020.2	1,010.5	963.0	890.4
Balance on Goods	-533.4	-470.5	-417.5	-401.2	-311.0	-171.0
Services, Credit (Exports)	145.8	161.7	182.9	168.2	134.7	22.2
Services, Debit (Imports)	207.4	209.8	228.3	219.2	225.5	136.2
Balance on Services	-61.6	-48.1	-45.4	-51.0	-90.8	-113.9

¹ IMF (2022) Article IV Consultation: Bhutan

Balance on Goods and Services	-595.0	-518.6	-462.9	-452.2	-401.8	-284.9
Balance on Income	-171.7	-199.3	-216.1	-221.1	-148.5	-154.6
Balance on Current Transfers	143.9	177.4	200.8	172.5	169.2	118.0
Capital Account	191.7	186.4	165.5	124.6	144.0	100.7
Financial Account	-461.7	-263.5	-302.0	-204.0	-194.2	-441.1
Direct investment (net)	-11.9	16.6	-2.6	-13.0	2.8	-6.8
Portfolio investment (net)	0.0	0.0	83.3	0.0	0.0	15.4
Financial derivatives (other than reserves) and employee stock options	0.0	0.0	0.0	0.0	0.0	0.0
Other investment (net)	-639.2	-260.4	-426.1	-257.2	-438.4	-421.2
Reserve assets	189.3	-19.6	43.5	66.2	241.5	-28.5
Reserves (months of imports)	9.4	9.9	7.9	10.0	12.9	10.5

Source: GDP growth is from UN DESA, WESP 2023 for 2021 data and UNSD for 2016-2020 data. Inflation is from UN DESA, WESP 2023. Government balance is from IMF, World Economic Outlook Database. Net ODA is from OECD, OECD.Stat. All external sector indicators are from IMF, Balance of Payment Data Reports.

The COVID-19 pandemic and related border closures and lockdowns interrupted this progress and had a devastating impact on the economy. The tourism sector was hit particularly hard with a complete stop in international visitors, while manufacturing, construction and non-hydro exports also suffered from trade disruptions, foreign labor shortages, and depressed external demand². The GDP contracted by 10.1 per cent in 2020² and 3.7 per cent in 2021³. Growth returned in the second half of 2021, supported by an easing of social distancing and quarantine restrictions measures. The services sector has rebounded, even though foreign tourist arrivals did not restart until September 2022, while the industrial sector, which contracted by 13 per cent in the 2020 fiscal year, has yet to fully recover.⁴

The stringent containment measures and a successful vaccine program have been effective at protecting the population from the pandemic with the number of cases remaining low. As of January 2023, about 2 million vaccine doses have been administered and only 63 thousand cases and 21 confirmed deaths have been registered.⁵

The unemployment rate jumped from 2.7 per cent before the pandemic to 5 per cent in 2020. The tourism sector, which 16 per cent of the working population are dependent for work, was hit hard. Returning migrants workers also make up a significant share of the unemployed.

Short and medium-term risks to the economy are primarily inflation and growing fiscal and trade deficits, areas in which the international crises have adversely impacted Bhutan. Inflation peaked at 8.2 per cent in the 2020/21 fiscal year (FY), stays high at 5.9 per cent in 2021/22 and is projected to rise back up to 7 per cent in the FY 2022-23, according to the Government.⁶ The rising inflation is contributing to a rise in poverty rates and is weighting on businesses and government.

Following relaxation of containment measures, the growth in imports has been much stronger than the exports and current account deficit has widened from 15 per cent of GDP prior to the pandemic to 28 per

² UNSD, National Accounts Statistics: Analysis of Main Aggregates (AMA) database

³ UN DESA, WESP 2023

⁴ Ministry of finance, Macroeconomic Situation Report: Forth quarter update FY 2021-2022, August 2022

⁵ World Health Organization, <https://covid19.who.int/region/searo/country/bt>, Accessed Jan 10 2023

⁶ According to UN DESA, WESP 2023, the inflation (calendar year) is estimated and projected as 5.6, 4.2, 6.1, and 7.2 per cent in 2020-2023, respectively.

cent in the 2021/22 fiscal year with only minor improvements projected in the near term. The negative balance of payments may lead to depletion of overall reserve assets posing risk to the constitutional mandate of meeting 12 months of essential imports. Falling revenues has increased the fiscal deficit to an estimated 8.9 per cent of GDP in FY 2021/22, against 1.9 per cent in FY 19/20.² This adds further to public debt, which has increased rapidly from 61 per cent of GDP in 2010 to an estimated 128 per cent in 2021.⁷ However, most of this debt is directly linked to the hydropower construction projects, where the credit is secured against long term power purchase agreements. The external debt is therefore unlikely to lead to debt distress.

Longer term risks include a failure to implement structural change and diversify the economy. The impact of external shocks on cottage and small industries is a particular concern, as such enterprises are particularly vulnerable. Bankruptcies and contraction in this sector could severely hamper efforts to expand and broaden the country's economic base. The country is heavily reliant the hydropower sector for revenues and state-owned enterprises for goods and services and will need to pursue an enabling environment for growth and employment including incentives for private sector investment. Furthermore, the dependency on hydropower and agriculture brings environmental risks, such as vulnerability to low rainfall which could lower output.

LDC criteria and supplementary indicators

Bhutan continues to make progress in all of the LDC criteria. The latest three-year (2019-2021) average GNI per capita is 2,914, over the level of two time of the graduation threshold established at 2021 triennial review. HAI is 82.6, well above the threshold of 66, and EVI is 25.2, below the threshold of 32 with comfortable margins.

Table 2: Criteria for LDC identification, Bhutan, 2019-2023

Year	GNI per capita	EVI	HAI
2019	2,609.4	25.8	80.0
2020	2,764.9	26.0	81.2
2021	2,943.2	25.8	81.7
2022	2,970.4	25.4	82.3
2023	2,914.1	25.2	82.6

Source: CDP Secretariat Time series estimates (LDC criteria) dataset (2002-2023), available at <https://bit.ly/LDC-data>

Notes: a) Year refers to the year of a (actual or hypothetical) review. The timeliness of source data varies by indicator; generally, criteria capture data up to two years prior to a review. See the 'read me' in the source as well as the data sheet (Annex 1) for details on original data sources.

b) Data for 2021 might differ from official triennial review data and previous monitoring reports due to data revisions.

Supplementary graduation indicators for Bhutan presents areas for further attention by the CDP (see table 3). Remittances and ODA have increased during the COVID-19 pandemic while tourism has fallen sharply. The share of employment in agriculture remains high. Broadband subscription fell by half during the COVID-19 pandemic, which needs to be observed if it can recover soon to pre-COVID-19 level.

⁷ Ministry of finance, Macroeconomic Situation Report: Fourth quarter update FY 2021-2022, August 2022

Table 3: Supplementary indicators for Bhutan, 2018-2021

Indicator	2018	2019	2020	2021
Remittances (% of GDP)	2.4	2.2	3.6	
ODA received as percentage of GNI	4.8	7.7	9.3	
Tourism receipts as share of exports	15.4	15.4	10.7	
Share of employment in agriculture	56.5	56.1	56.5	56.0
Fixed broadband subscriptions per 100 people	1.4	1.1	0.4	0.4

Source: CDP Secretariat, Supplementary graduation indicators

Data gap

Bhutan's statistical score was 60 in 2020, about the LDC average, but well below the average of other countries in South Asia (69). Methodology and availability of source data is a particular concern, while the country scores better on periodicity.

Smooth transition, national plan and country specific factors

Bhutan is scheduled to graduate in December 2023. The participation rate of Bhutan in the monitoring exercise is 83 per cent (three reports for four occasions, two meetings out of two). Bhutan attended both consultation meetings in 2022 and 2023, and submitted annual reports to CDP in 2021, 2022, and 2023.

Bhutan pursues a unique developmental approach that prioritizes overall well-being and environmental sustainability, termed Gross National Happiness (GNH). GNH is a multi-dimensional perspective on development that seeks to achieve a balance between material well-being and spiritual, emotional, and cultural needs. It prioritizes access to education, health, and finance. The country is currently implementing its 12th five-year plan, which is based on the GNH philosophy and is closely aligned with the 2030 Agenda and the SDGs. The Government has particularly highlighted the importance of SDGs 1 (No Poverty), 13 (Climate action) and 14 (Life on land) for development in Bhutan.⁸

A Smooth Transition Strategy task force which includes representatives from key sectors related to Bhutan's graduation led by the erstwhile Gross National Happiness Commission Secretariat was formed in April 2021. Bhutan will be integrating its Transition Strategy into the next national development plan) which is expected to come into effect from December 2023.

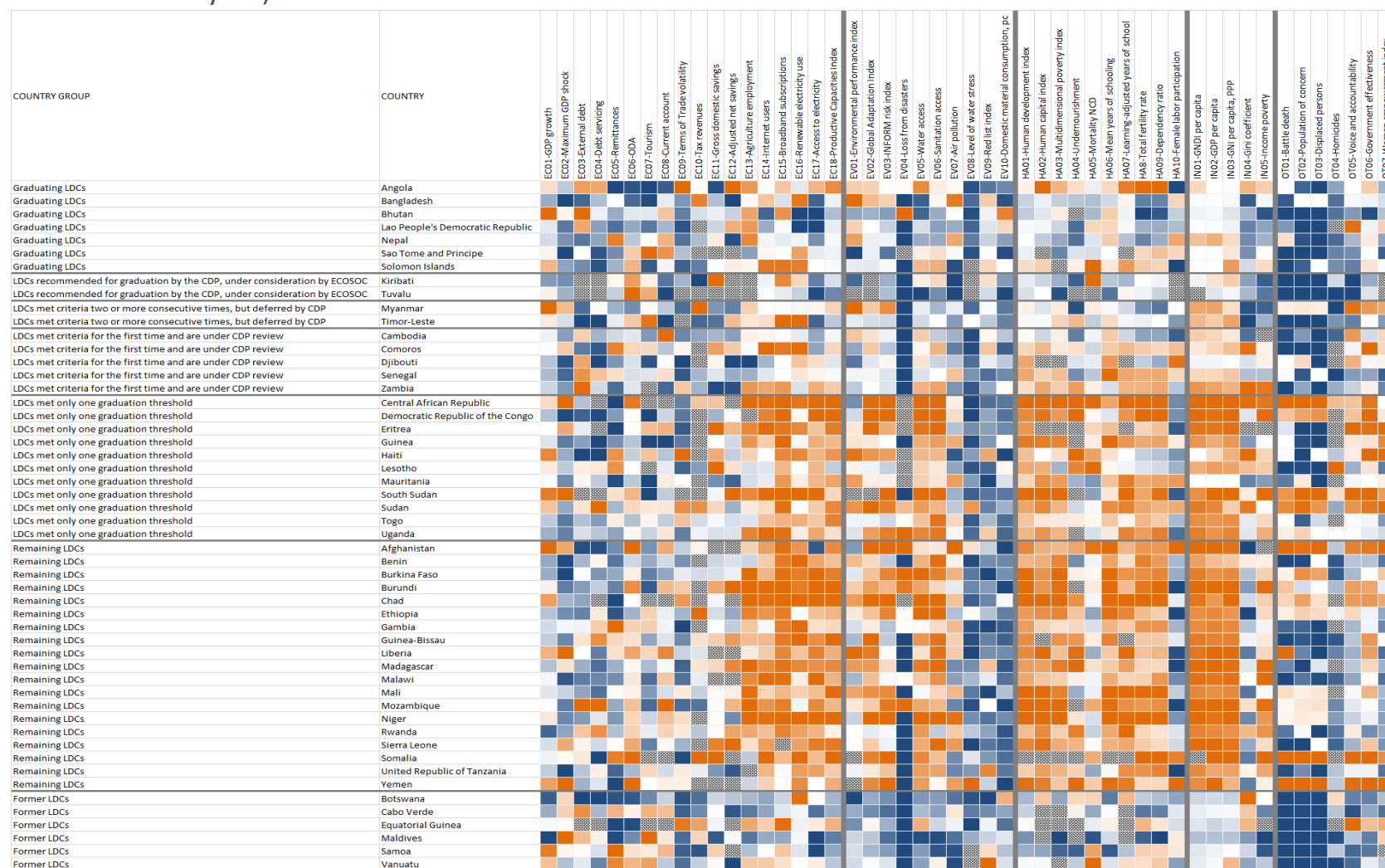
During country consultations on 15 December 2022, the Government highlighted that reforms are ongoing and that there are discussions underway to explore strategies for economic diversification. In response to questions about fiscal deficits a government representative responded that measures taken had already reduced the deficit and that further action is under consideration. There are expectations that tourism revenues will rebound in the coming year and ease pressure on the balance of payments. The Government is in negotiations with the EU to join the Generalised Scheme of Preferences+ (GSP+) incentive arrangement and has also approached other trading partners including Japan.

Challenges to a smooth transition from LDC status include the mobilization of domestic resources and prudent management of hydropower revenues to substitute for declining foreign grants and maintain macroeconomic stability. Total ODA flows were around \$178.7 million in 2019, a significant increase from previous year. Bhutan is also receiving support through the Global Environment Facility (GEF) 12 and the Green Climate Fund (GCF). While the support received through the Least Developed Countries Fund

⁸ Gross National Happiness Commission (2018). 12th Five Year Plan 2018-2023 Retrieved from: <https://www.gnhc.gov.bt/en/wp-content/uploads/2017/05/Finalized-Guideline.pdf>



(LDCF), managed by the GEF, is ending with graduation from the category, general support through the GEF remains open. Development partners have pledged around \$865 million for the implementation of the 12th five-year plan, half of which has already been received. The Government has received financial and in-kind assistance from a range of multilateral and bilateral donor agencies to combat the impacts of COVID-19. The Government also highlighted assistance in accessing different sources of finance as an area where UN support would be welcomed during the country consultation.

Annex 1: Heatmap extract of the supplementary graduation indicators (SGIs) for LDCs and former LDCs (2023 or latest available year)



Legend:

- Indicator furthest below reference point, indicating most concern (5th percentile)
- Indicator furthest above reference point, indicating least concern (95th percentile)

 Reference point (e.g. 33th percentile)
 No data available