

# Structural Transformation of Bhutan's Economy: Challenges Remain

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## Summary

*In spite of its structural transformation, Bhutan's economy is not performing well. While the tourism sector has seen growth, the other sectors are not performing up to expectations. The economy also continues to be highly dependent on the hydropower sector. Bhutan also remains highly dependent on India for market, trade, money and technology.*

## Introduction

Bhutan's economy underwent significant structural transformation in recent years. As a result, the country is slated to graduate from the United Nation's (UN) list of Least Developed Countries to a Lower Middle-Income Developing Country by December 2023. This decision was endorsed during the 73<sup>rd</sup> session of the UN General Assembly held in New York in December 2018.<sup>1</sup>

The *Bhutan Development Report 2019*, published by the World Bank Group, stated that Bhutan has successfully eliminated extreme poverty in the country. This report used various data from 2017 to analyse the country's economic situation. The national poverty rate in Bhutan declined from 23 per cent in 2007 to eight per cent in 2017, and the country's per capita Gross Domestic Product (GDP) increased by more than four times between 2000 and 2017 to US\$3,100 (S\$4,217).<sup>2</sup> However, many challenges remain. This paper discusses the contribution of the major sectors to Bhutan's economy and examines the problems they face.

## Importance of the Hydropower Sector

Bhutan has the capacity to generate about 30,000 megawatts (MW) of hydroelectricity each year. Of this, only about 2,400MW are currently being generated. The export of hydropower energy contributes around 40 per cent of Bhutan's external revenue. This sector's contribution to the country's domestic revenue is about 25 per cent.<sup>3</sup>

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<sup>1</sup> Tshering Palden, 'Bhutan Enters "Preparatory Period" Of Five Years To Graduate From Its Least Developed Countries Status', *Daily Bhutan*, 17 December 2018, <https://www.dailybhutan.com/article/bhutan-enters-preparatory-period-of-five-years-to-graduate-from-its-least-developed-countries-status>. Accessed on 30 January 2020.

<sup>2</sup> World Bank Group, 'Bhutan Development Report 2019: A Path to Inclusive and Sustainable Development', <http://documents.worldbank.org/curated/en/259671548449315325/pdf/134060-WP-PUBLIC-25-1-2019-13-34-54-BDRJanuary.pdf>. Accessed on 29 January 2020.

<sup>3</sup> Ibid.

Due to the lack of financial resources and technology, Bhutan has to depend heavily on India to generate hydropower. In 1961, India and Bhutan signed their first hydropower cooperation pact. It was to harness hydroelectricity from the transboundary river, Jaldhaka, which was completed in 1966. Since then, the two countries have cooperated on many such hydropower projects. Under the agreement of 2006 and an additional protocol signed in 2009, India will assist Bhutan to develop a minimum of 10,000MW of hydropower by the end of 2020.

Some of the major India-aided ongoing hydropower projects in Bhutan are Punatsangchhu-I (1,200MW), Punatsangchhu-II (1,020MW), Sunkosh (4,060MW) and Kuri-Gongri (1,800MW). Some of the joint-venture project include Kholongchhu, Chamkharchhu-I, Wangchhu and Bunakha Reservoir. The Mangdechhu hydropower plant, one of the major India-aided projects in Bhutan, was completed and inaugurated in 2019.

While the hydropower projects have generated much-needed revenue, they are also responsible for pushing Bhutan into a serious debt problem. According to Bhutan's *Annual Financial Statement, 2018*, of the total external debt, hydropower debt constitutes Nu. 132,532.919 million (\$2.58 billion), accounting for 74.4 per cent of the total external debt, while the non-hydropower debt stock was Nu. 44,619.477 million (\$0.87 billion), which is 25.57 per cent of the country's GDP. The loan from India, as per the *Annual Financial Statement, 2018*, is about ₹133,190.701 million<sup>4</sup> (\$2.59 billion) with ₹119,452.841 million (\$2.32 billion) as hydropower debt stock, representing 89.7 per cent of the Bhutan's total outstanding debt to India.<sup>5</sup>

## Growth in the Tourism Sector

Tourism is another important sector through which Bhutan earns foreign currency. The country opened its doors to international tourists in 1974.

According to the *Bhutan Tourism Monitor, 2018*, Bhutan received 274,097 visitors in 2018 which represented an increase of about 7.6 per cent over 2017. International tourists increased by 1.8 per cent to 63,367 while tourists from regional markets (India, Bangladesh and the Maldives) grew by 10.4 per cent.<sup>6</sup> Among the international tourists, arrivals from the United States recorded a 14.5 per cent growth, China 7.1 per cent, the United Kingdom 10.4 per cent, Germany 15.2 per cent, Malaysia 6.2 per cent and Australia 21.8 per cent.<sup>7</sup>

In terms of the number of tourists, like in the past, India continued to be the main source market for Bhutan in 2018. To encourage and promote tourism to Bhutan, India launched the RuPay Card in 2019, which could be used now in Bhutan instead of cash payments. The

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<sup>4</sup> Nu1 is equal to ₹1.

<sup>5</sup> Ministry of Finance, Royal Government of Bhutan, 'Annual Financial Statement 2018'. <https://www.mof.gov.bt/wp-content/uploads/2019/05/AFS2017-18English.pdf>, p. 30.

<sup>6</sup> Dechen Tshomo, 'Tourists Number Records Growth Of 7.61%: Bhutan Tourism Monitor 2018', *Kuensel*, 8 April 2019, <https://www.dailybhutan.com/article/tourists-number-records-growth-of-761-bhutan-tourism-monitor-2018>. Accessed on 30 January 2020.

<sup>7</sup> Ibid.

two countries also discussed the feasibility of the Bharat Interface for Money app in Bhutan to promote cashless payments for travellers. In recent times, one of the star tourists from India to Bhutan was India's male cricket team captain, Virat Kohli, and his actress wife, Anushka Sharma. They took a two week-long trip to Bhutan in November 2019.

In an attempt to make changes in the country's tourism policy, the Lower House of Bhutan's Parliament passed the 'Tourism Levy and Exemption Bill of Bhutan' on 3 February 2020. The new law makes it mandatory for visitors from India, Bangladesh and the Maldives to pay ₹1,200 (\$24) per day as Sustainable Development Fees with effect from July 2020. Children aged between 6 and 12 years from these countries will be required to pay ₹600 (\$12) while those under the age of five will be exempted.<sup>8</sup> At present, an international tourist has to pay a fee of approximately US\$250 (\$347) per day while tourists from India, Bangladesh and the Maldives are exempted from such a fee.<sup>9</sup>

## Underperforming Agriculture Sector

About 57.2 per cent of Bhutan's total labour force is involved in the agriculture sector, which accounts for about 17.4 per cent of the country's GDP. According to *Population and Housing Census of Bhutan, 2017*, 59.3 per cent of the total employed women of Bhutan work in the agriculture sector while the percentage of males engaged in this sector is 34.2.<sup>10</sup>

In 2013, the government started a programme to make Bhutan the world's first 100 per cent organic farming country. However, one of Bhutan's major concerns is that it has yet to achieve self-sufficiency in food grain production. According to *Bhutan Living Standards Survey, 2017*, about 2.7 per cent of the Bhutanese households experienced food insufficiency for one or more months in a year. Bhutan is only 46.7 per cent self-sufficient in the production of rice, 86 per cent of maize, 84 per cent of vegetables and 37 per cent of meat.<sup>11</sup>

It is estimated that a large area under agriculture in Bhutan remains fallow. According to the Ministry of Agriculture and Forests, in 2016, of the total estimated 129,036 acres of dry land in the country, 51,279 acres (39.7 per cent) were left fallow. In the wet land category, of the total 53,055 acres, 6,402 acres (12.1 per cent) remained fallow.<sup>12</sup> There is also an issue of frequent attacks by pests. At the same time, there have been a growing number of attacks by wild animals on people living near the forest areas. According to a survey carried out in 2015 by *Gross National Happiness Commission*, about one in ten people (9.9 per cent)

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<sup>8</sup> Suhasini Haider, 'Bhutan Ends free Entry for Indians', *The Hindu*, 5 February 2020. <https://www.thehindu.com/news/national/bhutan-ends-free-entry-for-indian-tourists/article30737792.ece>. Accessed on 11 February 2020

<sup>9</sup> 'Bhutan to impose fee of Rs 1,200 per day on Indian tourists', *Business Today*, 5 February 2020. <https://www.businesstoday.in/latest/trends/bhutan-to-impose-fee-of-rs-1200-per-day-on-indian-tourists/story/395496.html>. Accessed on 11 February 2020.

<sup>10</sup> Gross National Happiness Commission, Royal Government of Bhutan *Twelfth Five Year Plan (2018-2023)*, <https://www.gnhc.gov.bt/en/wp-content/uploads/2019/05/TWELVE-FIVE-YEAR-WEB-VERSION.pdf>. Accessed on 30 January 2020.

<sup>11</sup> Ibid.

<sup>12</sup> Department of Agriculture, Ministry of Agriculture & Forests, Royal Government of Bhutan, 'Agriculture Statistics 2016'. <http://www.moaf.gov.bt/download/Statistics/#wpfb-cat-2>, p 14-15.

reported to having left their land fallow in the past, and in one year specifically, because of wildlife threats.<sup>13</sup> In 2017, it was estimated that about 1,284 million tonnes (MT) of paddy, 5,151MT of maize, 78MT of buckwheat, 221MT of vegetables and 1,407MT of potato were lost to wild animals and pests.<sup>14</sup>

In an effort to deal with all such challenges in the agriculture sector, the *Twelfth Five Year Plan* (2018-2023) envisages some measures such as encouraging cultivation of fallow land; expanding and strengthening the irrigation system; enhancing farm labour supply; establishing a network of post-production and marketing facilities; strengthening price support for agriculture produce; and strengthening research and extension services.<sup>15</sup>

The phenomenon of climate change is another major challenge for the ecosystem in Bhutan. It is anticipated that, due to climate change, Bhutan will witness frequent floods and landslides, changes in weather cycle, receding glaciers and other natural hazards. They will affect Bhutan's agriculture sector. To deal with such situations, in 2017, the Bhutan government developed the 'Enhancing Sustainability and Climate Resilience of Forest and Agricultural Landscape and Community Livelihoods in Bhutan' project whose objective is to strengthen the biological corridors to build resilience for the adaption to climate change and to support sustainable agriculture in Bhutan by 2023.<sup>16</sup>

## Poor Infrastructure and Human Resources

Primarily, Bhutan's economy is state driven. State-owned enterprises (SOEs) operate all sectors such as manufacturing, energy, natural resources, financial, communications, aviation, trading and real estate. The strong presence of SOEs inhibits a level-playing field for private investments and discourages them from participating in these sectors.<sup>17</sup> *Bhutan 2020: A Vision for Peace, Prosperity and Happiness* emphasises the importance of private sector development and decentralisation.<sup>18</sup> Since its *Sixth Five Year Plan* (1987-1992), Bhutan has encouraged the participation of the private sectors in the country's economy. However, it is still a minor player.

The SOEs and the infant private sector have not been able to transform the country's infrastructure which is a big challenge due to the country's topography. India's Border Road Organisation (BRO) assists Bhutan in making roads in the country. In 2018, the BRO completed the construction of a strategically important road, linking the border town of Phuentshogling to the capital city of Thimphu. This 30-kilometre long Damchu-Chukha road, which criss-crosses rugged and difficult terrain, has been constructed under an India-

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<sup>13</sup> Gross National Happiness Commission, Royal Government of Bhutan *Twelfth Five Year Plan* (2018-2023), op. cit.

<sup>14</sup> Ibid.

<sup>15</sup> Ibid.

<sup>16</sup> Gabrielle Doran, 'Sustainable Agriculture in Bhutan', *The Borgen Project*, 21 January 2018. <https://borgenproject.org/sustainable-agriculture-in-bhutan/>. Accessed on 30 January 2020.

<sup>17</sup> World Bank Group, 'Bhutan Development Report 2019: A Path to Inclusive and Sustainable Development', op cit.

<sup>18</sup> Planning Commission Royal Government of Bhutan, 'Bhutan 2020: A Vision for Peace, Prosperity and Happiness, Part II', <https://www.greengrowthknowledge.org/sites/default/files/downloads/policy-database/Bhutan%20Vision%202020%20II.pdf>, p. 72.

assisted development programme.<sup>19</sup> The new road is expected to reduce the travel time between Phuentshogling and Thimphu by one hour and reduce the steep uphill journey by 19.5 kilometres.<sup>20</sup> The distance between Phuentshogling and Thimphu is about 165 kilometres which used to take more than five hours to cover.

The Japan International Cooperation Agency has also provided grant aid for the replacement of bridges and for road construction equipment.<sup>21</sup> In the *Eleventh Five-Year Plan* (2013 to 2018), the “strategic development of infrastructure” was prioritised and a commitment to the development of transportation infrastructure (including national highways) development was declared.<sup>22</sup>

Besides, the Asian Development Bank (ADB) has been supporting Bhutan since 1982 to develop renewable energy production, transport connectivity and urban infrastructure projects.<sup>23</sup> In 2018, the ADB approved four projects, including two grant projects focusing on skills and health programme. Through its assistance, the ADB aims to help generate revenue, support inclusive growth and promote environmental sustainability in Bhutan.<sup>24</sup>

As a small country, Bhutan has limited human resources. According to *Bhutan 2020: A Vision for Peace, Prosperity and Happiness*, Bhutan’s “skills base is extremely narrow and just over one-half of our [Bhutan’s] population can be considered literate and numerate.”<sup>25</sup> Although there has been an increase in primary and secondary school enrolment, the high dropout and repeat rates are a genuine cause for concern for the country.<sup>26</sup>

According to information available in the *Twelfth Five Year Plan* (2018-2023), as of 2018, the adjusted net primary enrolment rate in Bhutan stood at 96.8 per cent. This means that about 97 per cent of children between the aged of 6 and 12 years are attending primary education and other equivalent forms of structured learning.<sup>27</sup> The document underlines that the gross enrolment ratio for secondary education (Classes VII-XII) was estimated at 89.3 per cent. Overall, the literacy rate in Bhutan increased from 59.5 per cent in 2005 to 71.4 per cent in 2017, representing an increase of 11.9 percentage points.<sup>28</sup>

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<sup>19</sup> ‘Border Roads Organisation completes strategic road in Bhutan’, *The Economic Times*, 22 July 2018. <https://economictimes.indiatimes.com/border-roads-organisation-completes-strategic-road-in-bhutan/articleshow/65092484.cms>. Accessed on 30 January 2020.

<sup>20</sup> Ibid.

<sup>21</sup> Department of Roads, Ministry of Works and Human Settlement Kingdom of Bhutan, ‘Data Collection Survey on Road Connectivity in the Kingdom of Bhutan Final Report, September 2014’, [http://open.jicareport.jica.go.jp/pdf/12183323\\_01.pdf](http://open.jicareport.jica.go.jp/pdf/12183323_01.pdf). Accessed on 30 January 2019.

<sup>22</sup> Ibid.

<sup>23</sup> ‘Bhutan’s Economy to Moderately Grow in 2019 and 2020 on Strong Hydropower and Tourism Outlooks – ADB’, *Asian Development Bank*, 16 April 2019. <https://www.adb.org/news/bhutans-economy-moderately-grow-2019-and-2020-strong-hydropower-and-tourism-outlooks-adb>. Accessed on 15 December 2019.

<sup>24</sup> Ibid.

<sup>25</sup> Planning Commission Royal Government of Bhutan, ‘Bhutan 2020: A Vision for Peace, Prosperity and Happiness, Part II’, op. cit.

<sup>26</sup> Ibid.

<sup>27</sup> Gross National Happiness Commission, Royal Government of Bhutan, *Twelfth Five Year Plan* (2018-2023), op. cit.

<sup>28</sup> Ibid.

However, the rise in the enrolment rate does not correspond with the number of skilled workers in Bhutan. Even today, Bhutan has to depend significantly on expatriate workers, mainly from India. Most of the Indian hydropower companies send workers from India to build hydro plants and to do other auxiliary works in Bhutan.

## Conclusion

According to the *Bhutan Development Update* published by the World Bank in 2019, the country faces three major risks. They are delays in the hydropower projects, which negatively affects the economy through lower exports and revenues; scarcity of donor financing and undeveloped domestic debt markets (limited financing sources which could constrain development spending and negatively affect future growth and development); and adverse weather events, which could negatively affect the economy through lower electricity generation from existing hydropower plants and moderating tourist inflows.<sup>29</sup> Unless these maladies are addressed, Bhutan's economy will not perform anywhere near its potential.

In conclusion, Bhutan faces several major challenges in its economic development, due largely to inadequate technology and limited financial resources. In both these areas, Bhutan relies heavily on other countries, in particular India, with which it carries out 85 per cent of its trade. This overdependence on India has pushed the country into a serious debt problem. The country needs to find ways to address its economic issues if it wants to truly realise its potential.

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<sup>29</sup> Yoichiro Ishihara & Tenzin Lhaden (2019), 'Bhutan Development Update: Harnessing Urbanization (English)'. <http://documents.worldbank.org/curated/en/244991561011294417/Bhutan-Development-Update-Harnessing-Urbanization>. Accessed on 30 January 2020.