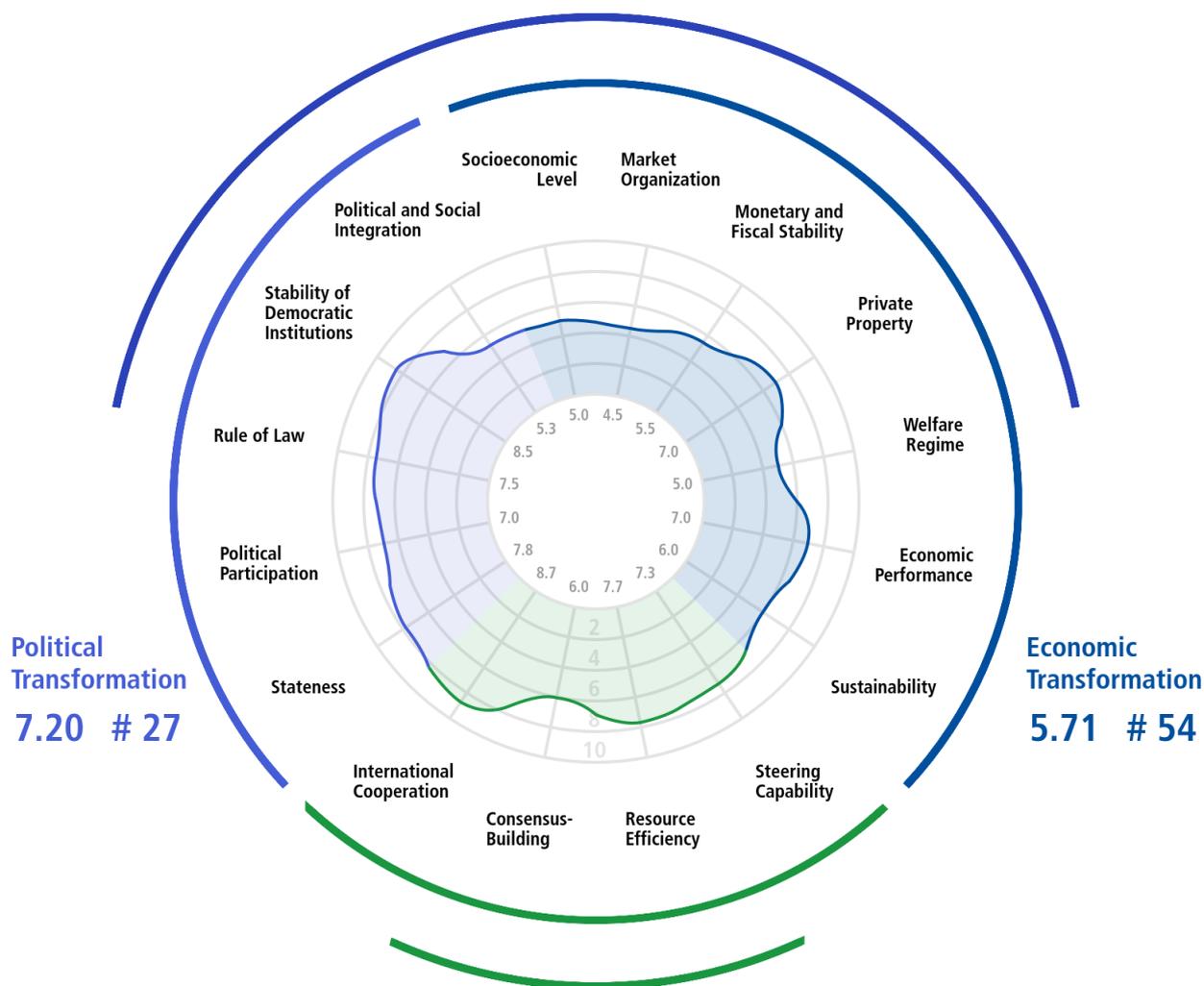


Bhutan

Status Index

6.46 # 34

on 1-10 scale out of 137



Political Transformation
7.20 # 27

Economic Transformation
5.71 # 54

Governance Index

6.66 # 12

on 1-10 scale out of 137

This report is part of the **Bertelsmann Stiftung's Transformation Index (BTI) 2024**. It covers the period from February 1, 2021 to January 31, 2023. The BTI assesses the transformation toward democracy and a market economy as well as the quality of governance in 137 countries. More on the BTI at <https://www.bti-project.org>.

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Key Indicators

Population	M	0.8	HDI	0.666	GDP p.c., PPP \$	-
Pop. growth ¹	% p.a.	0.6	HDI rank of 189	127	Gini Index	28.5
Life expectancy	years	71.8	UN Education Index	0.540	Poverty ³	% 0.5
Urban population	%	43.7	Gender inequality ²	0.415	Aid per capita \$	163.2

Sources (as of December 2023): The World Bank, World Development Indicators | UNDP, Human Development Report 2021-22. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.65 a day at 2017 international prices.

Executive Summary

Bhutan's political and economic system, though stable, faced some key challenges during the review period. The ruling party, Druk Nyamrup Tshogpa (DNT), promised to quickly deliver on its campaign pledges, but due to disruptions caused by COVID-19, these commitments largely remained unmet. Meanwhile, the opposition party, Druk Phuensum Tshogpa (DPT), criticized the ruling party for its lack of progress. Yet, the DPT faced its own criticism for not effectively holding the ruling party accountable and not playing a more active role in governance.

During the period under review, Bhutan's democracy remained steady; however, disputes between the National Council and National Assembly prevented certain legislation from being passed, most notably the Mines and Minerals Act. The government thus had to employ ordinances in order to make the changes it deemed necessary in managing the country's mines and minerals.

While the divisions between the two houses of Bhutan's parliament could be seen as an indicator of healthy competition and transparency in the legislative process, their inability to reach a compromise could also suggest inflexibility and deadlock. To address these challenges, Bhutan's political parties will need to prioritize resolving their differences and fostering innovative policies while expediting their execution. The country is set to hold its fourth parliamentary elections in 2023.

During the review period, civil servants in Bhutan underwent performance evaluations, which forced some to retire prematurely. This practice sparked concerns within the bureaucracy, especially since the pool of qualified job applicants is shrinking. Corruption remained a significant issue in both Bhutan's bureaucracy and judiciary. The Supreme Court responded to public complaints involving conflicts of interest among judges and public accessibility to address concerns. To address these matters, a media and communication unit was established at the court to assess and manage complaints against judges. Additionally, separating judicial services from the Bhutan Civil Service Commission met the long-standing demand for enhanced judicial independence.

Bhutan's economy remained constrained by its heavy reliance on hydroelectricity, a stagnant private sector, and increasing youth unemployment. As Bhutan transitions in 2023 to graduate from the group of the world's least-developed countries, it must bolster its internal strengths to sustain its economic progress. Aside from the pandemic-induced slowdown in 2020/21, Bhutan has maintained robust growth over the past decade. The economy exhibited resilience with a growth rate exceeding three percent in 2021/22, and the outlook indicates potential for even higher growth in the upcoming year. Challenges beyond hydroelectric dependence include a dwindling reserve of Indian currency and foreign exchange, as well as a growing scarcity of labor in vital sectors like health and education. COVID-19 disruptions significantly setback the private sector, particularly the hospitality and tourism segments, which further impeded job growth in this sector. To reinvigorate and foster the private sector, greater government support and reduced control over critical economic sectors are necessary.

Throughout the review period, Bhutan has continued its dialogues with China to address unresolved border matters. However, the escalating tensions between China and India will pose a challenge for Bhutan, considering its reliance on India for border security.

History and Characteristics of Transformation

Since Bhutan embarked on its transition to democracy in 2008, the country's political process has displayed remarkable resilience through the successful conduct of three general elections for the national parliament and local government bodies. Having lost to its main rival in each of these elections, the ruling party relinquished its power, resulting in a peaceful transfer of authority. This accomplishment stands as a remarkable achievement for a fledgling democracy.

In June 1998, the era of direct royal rule came to an end as a cabinet of ministers was established. Progress toward democracy continued in 2005 with the public release of a draft constitution, which, after thorough public consultations, was formally enacted on July 18, 2008. This constitution introduced a parliamentary system and granted the right to form political parties.

The inaugural elections of 2008 witnessed the People's Democratic Party (PDP) receiving 33% of the votes but securing only two out of 47 seats, while the Bhutan Peace and Prosperity Party (Druk Phuensum Tshogpa, DPT) claimed the remaining 45 seats. The country's second general elections in 2013, encompassing both the National Council and National Assembly, experienced lower voter turnout compared to 2008. Among four political parties, two led by women, competing in the primary election, only the DPT and PDP advanced to the general election after the new parties were eliminated. The incumbent DPT, winning 17 seats, conceded to the PDP, which clinched 30 seats, emerging as the new governing party.

Bhutan held its third parliamentary elections in 2018. The National Council elections in April saw a significant voter turnout of over 54%, a substantial increase from the 45% recorded in 2013. Subsequently, the primary round of National Assembly elections was held on September 15, 2018. The unexpected victor in the primary round was the Bhutan United Party (Druk Nyamrup Tshogpa,

DNT), a new left-of-center party formed in 2013 and led by urology surgeon Lotay Tshering. In the general round on October 18, 2018, the DNT secured around 60% of the votes, resulting in 30 out of 47 seats being won. The DNT's seat count grew to 33 after additional victories in by-elections. Notably, voter turnout soared to approximately 71%, surpassing the 66% turnout in the 2013 National Assembly elections. In 2018, gains were made in women's representation, with two female candidates being elected to the National Council and seven out of 10 female candidates winning in the National Assembly elections. In contrast, 2013 saw no women elected to the National Council and only three to the National Assembly.

Bhutan has witnessed rapid economic and social changes, particularly evident in its capital, Thimphu, which expanded from 30,000 residents in 1993 to around 138,736 by 2017, constituting 19.1% of the nation's total population. Despite urbanization's momentum in Thimphu and across Bhutan, 61% of the population remains rooted in rural areas, primarily engaged in agriculture. In 1960, a striking 91% of the populace resided in rural regions.

Traditionally, the Royal Civil Service has absorbed school and college graduates into its workforce. Nevertheless, since 2000, the number of graduates has outpaced available positions, highlighting the necessity for the private sector to contribute to employment opportunities. Slower economic growth rates in 2013 and 2014 underscored the challenge of fostering robust private sector growth in the nation. Even the heightened growth observed in 2017/18 did not alleviate the issue of unemployment, exacerbated by the economic slowdown caused by COVID-19 in 2021/22.

Instances of drug offenses and property crimes have surged, along with an increase in sexual crimes, particularly those involving minors. While Bhutan has made strides in infrastructure, health care, and education, the adverse effects of modernization have become more pronounced in urban areas and have prompted rural migration in certain regions. According to the 2015 Gross National Happiness Survey, urban populations report higher levels of happiness compared to their rural counterparts.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

The state maintains a monopoly on the use of force throughout the country. Responsibility for patrolling the border areas and forests rests with the Royal Bhutan Army, the Royal Bodyguard of Bhutan, and the Royal Bhutan Police. The latter has posts nationwide. An estimated 1% of the GDP is used for military expenditure. No rebel groups or criminal organizations are known to operate in Bhutan.

Relations with neighboring India are close and cooperative, including with the Indian military, which has a presence in Bhutan. In 2020, porous borders with India presented some challenges to enforcing the lockdown to prevent the spread of COVID-19. As of September 2022, Bhutan has required all its citizens to present their passports while entering or exiting the country, including travel to India.

Bhutan has no formal diplomatic ties with its northern neighbor, China, and there is still an unresolved border dispute between the two countries. Negotiations on the dispute have been conducted amicably since 1984. The 24th round of border talks took place in August 2016. In 2017, Bhutan was caught in the middle of a 75-day standoff between India and China in Doklam, a disputed territory between China and Bhutan. The standoff followed China's attempt to extend an existing road in North Doklam into southern Doklam, which is claimed by Bhutan. India has a security treaty with Bhutan, under which the Indian military is obligated to defend Bhutan's territorial integrity. The standoff ended after China halted the construction and Indian troops withdrew. In June 2020, fresh claims by China to Bhutan's Sakteng Wildlife Sanctuary added a new dimension to the dispute between the two countries. In 2020, the New York Times reported that China was building a village inside Bhutanese territory in the Doklam region, but Bhutan denied this. In October 2022, Bhutan and China signed an MoU to expedite boundary negotiations.

Question
Score

Monopoly on the
use of force

9



1

The concept of Bhutan as a nation-state is widely accepted. Before and since the expulsion or flight of thousands of ethnic Nepali Lhotshampas in the late 1980s and early 1990s, the government vigorously promoted the concept of the Bhutanese nation-state. Bhutan's policy, vis-à-vis the thousands of Lhotshampas who remained in the country after the expulsion, remains discriminatory. The 2017 census included no questions about language, ethnicity and religion, which makes it difficult to establish the exact number of Lhotshampas still in Bhutan. Access to citizenship is determined by the 1985 Citizenship Act, the rules of which are strict. Individuals of whom both parents are Bhutanese qualify for citizenship, as do those domiciled before December 31, 1958. Otherwise, applicants for citizenship should be able to prove at least 15 years (public servants) or 20 years (others) of residence in Bhutan, as well as proficiency in the national language. Some external organizations have commented on the “very strict criteria” facing “ethnic-Nepali Bhutanese” when trying to obtain citizenship and security clearances. Failure to secure such clearances can limit access to employment, business ownership, education, and international travel.

Of Bhutan's population, 75% adhere to Mahayana Buddhism. The constitution declares that religion does not interfere with politics and that religious institutions and personalities must remain unpolitical. Thus, the state is officially secular, and no political activity by the Buddhist establishment can be observed. The personnel of religious institutions are prohibited from voting or standing in elections. In spite of all these provisions, however, the constitution does state that preserving the country's religious heritage of Buddhism is important and that society is “rooted in Buddhism.” Buddhism is closely tied with the elites, and there is a strong bias against Hindus in particular. Since the 1980s, Bhutan's “One Nation, One People” policy has sought to promote a uniform religious and cultural identity. The national flag and emblem also draw from Buddhist symbolism.

The state continues to provide some financial support for monasteries and religious activities. Government approval is necessary for the construction of religious buildings. There have been reports of the government favoring the construction of Buddhist religious buildings over Hindu ones. Nevertheless, despite these assertions, a Hindu temple was rebuilt in the southern region in 2015 on the order of the king as a gift in commemoration of the royal wedding. In 2019, a large new Hindu temple was established in the capital, Thimphu. There is a small number of practicing Christians in Bhutan – estimated to be between 2,000 and 25,000 – who meet discreetly. They are not formally recognized by the government and have no religious buildings. Two Christian pastors were fined and sentenced to prison for evangelism in 2016.

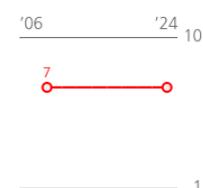
State identity

7



No interference of religious dogmas

7



Bhutan has a generally well-functioning system of public administration, involving central ministries in the capital and their decentralized offices in the districts (dzongkhags). In recent years, there have been calls to modernize the civil service throughout the country. Corruption and poor performance remain major challenges for administrative services. In 2022, the government subjected senior officials to performance tests in an attempt to remove poor-performing bureaucrats. Civil service employees suffer from low morale, poor management, and a high attrition rate. In November 2022, Bhutan enacted a Civil Service Reform Act that reorganized various government departments and agencies to achieve greater efficiency. In February 2021, the Royal Civil Service Commission's Public Service Delivery Division, together with UNDP Bhutan, began a joint initiative to improve public service delivery by including citizens in the implementation and assessment of these services. As of 2017, 98% of the population has access to an improved water source, and 81% has access to improved sanitation, although 18% reported irregular water supplies. From 2019 to 2020, Thimphu and surrounding areas experienced critical water shortages, forcing many businesses and residents to turn to private water vendors. Waste management, especially in the capital Thimphu, remains a major problem. With only two waste pickup trucks in operation, the collection system falls far short of the demand.

Tax as a percentage of GDP rose from 5% in 2004 to 16.1% in 2018, even peaking at 19% in 2016. The value is predicted to increase as incomes rise and hydroelectric projects come into operation. Although only 6% of the population pays any direct tax in Bhutan, this still makes it the country with the highest percentage among the South Asian Association for Regional Cooperation (SAARC) partners.

2 | Political Participation

In 2018, Bhutan held its third election for the National Council (NC) and National Assembly (NA), the two chambers of the national parliament. At the local block (gewog) level, the country also has non-party elections. Bhutan's constitution grants its citizens universal suffrage and secret ballots. For the National Council, which is nonpartisan and seen as a house of review, one member is elected for each district (dzongkhag), regardless of its population size. In November 2020, Bhutan held a by-election for the National Assembly seat in the Choekor-Tang constituency, vacated by the resignation of the opposition leader, Pema Gyamtsho, of the DPT. By winning this seat, the ruling party, the DNT, flipped a constituency that the DPT had held for the last 10 years. On December 24, 2022, Bhutan held the third local government elections, witnessing its highest-ever voter turnout of 68.4%. In the third LG election, over 490 women ran as candidates, which far surpassed the numbers of 165 and 200 women who had participated in the first and second LG elections. In 2022, Bhutan also held three by-elections for vacant NA seats, all of which the ruling DNT won. In 2023, Bhutan will hold elections for both the National Council (NC) and National Assembly (NA), which face the end of their terms in October.

Basic administration

8



Free and fair elections

8



The Election Commission has managed elections strictly and impartially. Elections in Bhutan have been free and fair, with no serious complaints concerning irregularities. Political party campaigns are restricted to issues that are not divisive. According to election rules in 2022, candidates for both NC and NA must have five years of experience working in either the public or private sector. The candidates must also convince Bhutan's Election Commission of their integrity, reputation, and good character. In November 2022, the NA recommended greater scrutiny of national- and local-level elections by the Anti-Corruption Commission and the Election Commission of Bhutan.

Bhutan's political elite is small and has consistently demonstrated loyalty to the state and the king. The military has never challenged the state, the clergy refrain from political involvement, and as of now, neither a trade union movement nor a powerful business lobby exists. In short, there are no active domestic veto players.

However, there are two potential veto players, one domestic and one external. The potential domestic veto player is the king, who is a part of the parliament and has the authority to assent to bills of parliament. He may return bills with recommendations for amendments but must abide by the parliament's final decision if supported by both houses. The king, and even the institution of monarchy as a whole, is held in very high esteem in Bhutan, and the two houses of parliament are highly unlikely to make proposals with which the king would strongly disagree. So far, the king has never taken any overt action that could be interpreted as veto behavior.

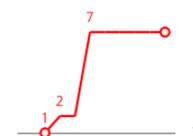
The potential external veto player is India. It provides considerable financial aid to Bhutan and accounts for 80% of all its foreign trade. The country buys most of Bhutan's hydroelectricity – the main source of state revenue – and is also responsible for Bhutan's defense. The Bhutanese government is careful to avoid actions that risk provoking India. For example, a conversation between the prime ministers of Bhutan and China on the sidelines of an international meeting in the run-up to the 2013 election raised speculation that diplomatic relations between the two countries might be established. Soon thereafter, the Indian government removed the subsidies on kerosene and cooking gas exported to Bhutan, leading to a doubling of their prices. Some commentators saw India's action as a warning to Bhutan concerning the adverse consequences of introducing relations with China.

The constitution guarantees freedom of assembly and association, but in practice, there are restrictions on these principles. Citizens can join political parties approved by the Election Commission. Protests or demonstrations are permitted but must be approved by the government beforehand. Public protests, however, are viewed as non-Bhutanese behavior. Freedom of association is limited to groups that are “not harmful to the peace and unity of the country.” As a result, civil society organizations (CSOs) working on refugee or human rights issues, as well as other sensitive policy areas, are not allowed to operate. All CSOs must register with the government. Due

Effective power to govern

7

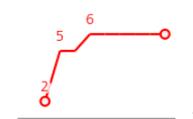
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Association / assembly rights

6

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to the predominantly rural subsistence nature of life in Bhutan, the scarcity of large organizations, and the lack of government support for unions, there are no trade unions. Lastly, COVID-19-related restrictions have not affected freedom of assembly.

Bhutan's constitution guarantees freedom of expression, but the exercise of this principle remains constrained in practice. According to the 2022 World Press Freedom Index, Bhutan has ranked 33rd out of 180 countries, a significant improvement from its 65th place in 2021 and 94th place in 2018. Editors of both print and online media, however, have complained that the government restricts media access to official information by imposing gag orders on government officials. For example, the dismissal of two foresters for speaking to the media was perceived as an attempt to intimidate government officials. In a survey conducted by the Journalist Association of Bhutan (JAB) in 2022, its members reported that their access to information is perceived to be worse than in previous years and that the government actively stonewalls their efforts to obtain information.

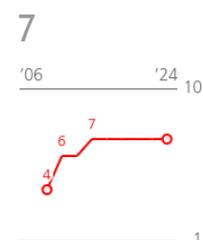
Bhutan also has a Defamation Act, which authorities can use to harass journalists. In 2018, an editor was suspended for running profile stories on National Council candidates after a complaint by the Office of Media Arbitrator. The JAB expressed concern that these practices may hinder journalists from carrying out their duties without fear or bias. In 2018, Bhutan established a Media Council with significant regulatory powers. The council sets the code of conduct for journalists and outlines the accreditation and certification requirements for journalism practitioners.

3 | Rule of Law

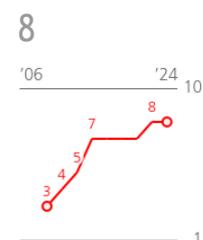
The separation of powers between the executive, legislative, and judiciary is outlined in Bhutan's constitution and is evolving within the context of its new democratic framework. In Bhutan's parliamentary system, the government relies on the support of a majority in the National Assembly. In all three recent elections, the winning party achieved an absolute majority. The judicial branch operates independently from the executive and legislature, with judges appointed by the king based on the judicial council's recommendation. As political and legal conflicts increase in a democratic system, the demands on the judicial system are rising, particularly in cases involving corruption and abuse of power. In 2022, Bhutan's Judicial Service employees gained independence from the Bhutan Civil Service Commission.

The Anti-Corruption Commission (ACC) and the Office of the Attorney General (OAG) also play an important role in the system of checks and balances on the exercise of power. In 2018, the National Law Review Task Force recommended strengthening the separation of powers, resulting in the independence of the ACC and the Election Commission of Bhutan from the Royal Civil Service Commission. The Royal Civil Service Commission, which serves as the central agency for recruiting, training, and transferring civil servants, is no longer overseeing these two bodies.

Freedom of expression



Separation of powers



After the first detection of a COVID-19 case in March 2020, the government swiftly introduced emergency measures. In August, it declared a national lockdown and a strict tracing policy, which was extended in September. Parliament formed a Parliamentary Committee on COVID-19 Preparedness and Response that monitored the government's decisions.

Bhutan's constitution strongly emphasizes the rule of law. The judiciary is the guardian of the constitution and the final authority regarding its interpretation. The Supreme Court stands at the top of the court hierarchy. The decisions of the lower courts can be appealed upwards, and each level of the court system maintains its independence. There has been investment in upgrading the skills and knowledge of officials in the judiciary through foreign technical assistance and with the establishment of the National Legal Institute. In 2015, Bhutan also founded the Jigme Singye Wangchuck School of Law. As recently as 2022, Bhutan's judicial service was delinked from the Bhutan Civil Service Commission to manage its own personnel, further strengthening the separation of power.

Courts at all levels of the judicial system have demonstrated independence by adjudicating cases against government officials and agencies, including members of the cabinet and the military. The judiciary's 2020 annual report concluded that there were insufficient financial resources to expand its infrastructure and to hire and train personnel, which restricted the court's ability to keep up with the increasing demands for judicial services. In 2019, 9,541 cases were registered, with 2,692 pending cases from 2018. Eventually, the courts decided on 9,216 cases. Bhutan's judiciary has been criticized both for slow delivery and a lack of transparency.

Other issues remain as well. For instance, there are complaints that parts of the judiciary are susceptible to corruption or that the judges' rulings lack consistency. In 2017, in response to complaints of possible bias resulting from a plaintiff's relationship with more than one judge, the Supreme Court of Bhutan drafted the Judicial Accountability Guidelines 2017. The guidelines allow individual citizens to file complaints of bias against High Court and Supreme Court decisions. The RAA report, "Review of Judiciary System and Practices, 2019," states that court judgments still remain entirely inaccessible to the public.

As political and legal contests grow with the maturation and consolidation of Bhutan's democratic system, demands for judicial adjudication of constitutional and legal issues are increasing.

Independent
judiciary

7

'06 '24 10



1

The incidence of corruption in Bhutan is low, but there is significant official and public concern over the issue. In his address to the nation in March 2022, Bhutan's King Wangchuk stressed the need to fight corruption. The Anti-Corruption Commission (ACC) has performed well since its establishment in 2006. In its first 10 years of operation, the ACC received 4,333 complaints, conducted 148 investigations, and achieved a 90% conviction rate, indicating a high level of effectiveness. The ACC has not hesitated to prosecute cases involving prominent officials. In response to the ACC's appeal against the High Court's decision to acquit, in March 2019, Bhutan's Supreme Court sentenced nine Royal Bhutan Army officers and a non-commissioned officer to prison terms for their involvement in the embezzlement case of the DeSuung training fund. The ACC also investigated an allegation that the former prime minister, Dasho Tshering Tobgay, misused government funds totaling BTN 3 million to install security infrastructure at his private residence in Taba. In November 2019, the ACC cleared Tobgay of any wrongdoing. In October 2020, Bhutan's High Court convicted the current home minister of insurance fraud; the case was brought to court by the attorney general. In April 2021, the minister resigned after the High Court's larger bench upheld his conviction.

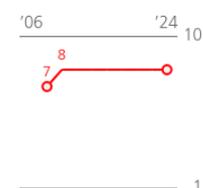
Fundamental civil rights are outlined in Article 7 of the constitution but primarily apply to citizens, encompassing freedoms of speech, opinion, expression, movement, and religion, as well as the right to vote and equality of access to the law and public services. However, Article 33 stipulates that these rights may be suspended in the event of a proclamation of emergency. Furthermore, Article 7 grants the state the authority to impose "reasonable restrictions by law" when the interests of Bhutan's sovereignty, security, unity, and integrity, as well as peace, stability, and national well-being, are perceived to be threatened.

Bhutan's policy vis-à-vis thousands of Lhotshampas, who remain in the country after their mass expulsion, remains discriminatory. The 2017 census did not include any questions about language, ethnicity and religion, making it difficult to determine the precise number of Lhotshampas still in Bhutan. Some members of the ethnic minority do not possess full citizenship and the corresponding rights. Furthermore, an unspecified number of Lhotshampas are still held in Bhutanese prisons.

The police have sometimes been accused of human rights violations, especially by external ethnic-Nepali organizations. There is no capital punishment, according to the U.S. State Department. In 2018, there were no incidents of disappearances, arbitrary killings, or torture. Prisons have been perceived to generally comply with international standards, and rules against arbitrary arrests and detention are observed. While freedom of religion is guaranteed by the constitution, missionaries are banned, and government permission is needed for the construction of religious buildings.

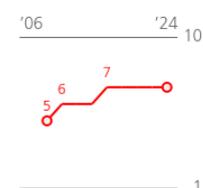
Prosecution of office abuse

8



Civil rights

7



In June 2019, Bhutan’s National Assembly passed the Penal Code Amendment Bill of Bhutan to eliminate discriminatory sections on “unnatural sex” from the Penal Code. The move was a significant victory for the lesbian, gay, bisexual, transgender, intersex, and queer (LGBTQ+) communities in the country. The National Council passed the bill in February 2020 but refused to entirely remove the penal provisions, instead downgrading consensual “unnatural sex” to a petty misdemeanor. However, this punishment was eliminated through an amendment in December 2020, which clarified that homosexuality between adults does not constitute unnatural sex.

Bhutan is a signatory to the Convention on the Elimination of All Forms of Discrimination Against Women and other international agreements. NGOs report little overt discrimination against women and state that women have equal access to public services. However, Bhutan ranked 131st out of 153 countries in the Global Gender Gap Index 2020. Media reports indicate a rise in the incidence of domestic violence and sexual assaults on women. The government acknowledged the seriousness of the issue by passing the Domestic Violence Prevention Act in 2014. Gender-based violence was reported to have increased by 36% in 2020 compared to the previous year. Lastly, accessibility for persons with disabilities remains a significant problem.

4 | Stability of Democratic Institutions

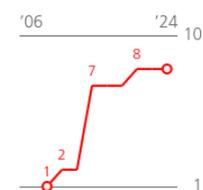
In light of the fact that Bhutan is a young democracy, the country’s democratic institutions function well. Bhutan’s parliament consists of the National Assembly and the National Council. Both houses have equal legislative powers, though the National Council is elected on a nonpartisan basis. Bhutan’s judiciary is granted independent jurisdiction under the constitution. Local governments in Bhutan consist of 20 districts, all equipped with their own district councils, whose members are elected for a five-year term.

At the national level, all three national elections have seen transfers of power from the respective ruling party to its successor. Political parties, while respectful of each other, face growing opposition from their rivals. For example, during the 2018 election campaign, opposition parties questioned the ruling party’s performance in office and criticized the allegedly improper use of government resources. Parties have become more attentive to the electorate’s concerns, such as income inequality and access to health care and drinking water. The opposition DPT has played its role by criticizing the ruling party over matters of budgetary allocations for 2021/22, corruption, and the poor delivery of services to the people. Observers of Bhutanese politics perceive the role of the opposition as too mild.

The election of two women as members of the National Council in 2018 and seven women to the National Assembly also marked an improvement in approaching greater gender equality. In the 2021 local government elections, the participation of women as candidates was significantly higher than in the two previous elections.

Performance of democratic institutions

8

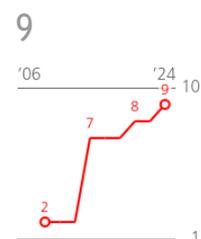


Bhutan's constitution grants equal roles to both houses of parliament in matters of legislation. In cases where there are differences between the two houses, a joint session is required to reach a resolution. However, on certain bills, reaching a resolution has proven to be difficult. For instance, in December 2022, the parliament concluded its session without debating the Mines and Minerals Bill 2021 due to a stalemate between the two houses concerning its provisions. Similarly, during the period of 2019 – 2020, the two houses openly clashed. Furthermore, the National Assembly has tended to disregard or overlook certain legislative initiatives put forth by the National Council. An example of this occurred in January 2020 when the National Assembly outright refused to even deliberate on the Impeachment Procedure Bill 2019, despite its passage by the National Council. Similarly, a standoff between the two houses arose over the Minister and Equivalent Post Holders' Entitlement Bill 2019, which had also been passed by the National Council in the summer of 2019. The two houses of parliament have also clashed over various other issues, including the Crime Bill, salary increases for government employees, and the elimination of grade thresholds for 10th grade students to progress to the higher class. The recurring presence of such differences has raised concerns regarding the effectiveness of parliament.

Bhutan's democratic institutions have steadily consolidated since the initial national democratic elections in 2007 and 2008. There are no active veto players and no individuals or organizations advocating significant changes to the political system. All political parties support the democratic system, and the ruling parties in both the 2013 and 2018 elections seamlessly transferred power to the new majority parties. Similarly, there are no associations, interest groups, or civic organizations openly challenging democracy in the country. This implicit commitment to the country's democratic institutions by all pertinent actors can be interpreted as a steadfast dedication.

The fact that voter turnout in elections for both houses of parliament was higher in 2018 than in 2013 shows increased support for the electoral process. The increasing use of electronic voting machines and postal votes has helped streamline the voting process. Following the 2018 elections, Bhutan's parliament saw strong opposition for the first time. The DPT, which formed Bhutan's first democratic government after the 2008 elections, won 17 seats (36%) in the new parliament. In 2008, the opposition had won only two seats, and 15 seats in 2013.

Commitment to democratic institutions



5 | Political and Social Integration

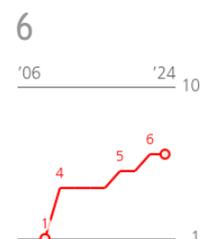
Bhutan's party system is young, lacking strong links to and deep roots in society, with low ideological and programmatic polarization. Parties have small numbers of members, ranging from 142 to 799 for the parties involved in the 2013 National Assembly election. In the 2018 election cycle, the four political parties that participated in the primary round reported increased memberships. The newly established DNT, which now forms the new government, reported over 11,000 members, while the other three parties had between 1,275 and 5,520 members.

In 2018, the DNT won a majority in the National Assembly elections, defeating both the ruling and opposition parties of the previous parliament. As the general round of National Assembly elections is between the top two parties, the runner-up party is recognized as the sole opposition party in parliament, rendering other parties that participated in the primary round largely irrelevant in the governing process. In 2022, the new Druk Thuendrel Tshogpa (DTT) party applied for registration, and its leader, former Druk Phuensum Tshogpa (DPT)'s North Thimphu member of parliament Kinga Tshering, announced his intention to run as a candidate in the 2023 national elections.

The policy platforms of the parties have differed marginally. The Election Commission ensures that parties adhere to the principle that "national interest prevails over all other interests" and demonstrate their commitment to promoting national unity. Three members of the Election Commission, including the chief election commissioner, are appointed by the king from a list recommended by leaders of the legislature and the chief justice of Bhutan. They must also be perceived as pursuing the national development philosophy of Gross National Happiness. Party platforms have been distinguishable only by differences in the strategies highlighted to achieve Gross National Happiness and varying emphasis on particular elements thereof. This was also true in the 2018 elections. However, with the center-left DNT taking power, political parties have started emphasizing popular agendas, and voters are expecting more from them.

Political parties receive limited funding for each candidate from the Election Commission (\$2,167 in 2013) and from members' contributions. The latter way of party financing was capped with a ceiling of \$8,333 in 2013, and this amount remained unchanged during the 2018 elections.

Party system



There are few interest groups in Bhutan, and they have only marginal importance. Currently, there are 64 registered civil society organizations (CSOs), of which 42 are public benefit organizations and 12 are mutual benefit organizations. Some influence comes from business organizations such as the Bhutan Chamber of Commerce and Industry and especially the Association of Bhutanese Tour Operators. However, the private sector has yet to emerge as an influential player. NGOs have been developing but remain few, largely focused on the environment as well as women's and children's affairs. Some NGOs, like the National Women's Association of Bhutan and the Royal Society for the Protection of Nature, receive royal patronage. There are no active trade unions in the country. In November 2021, Bhutan's civil society organizations formed the Bhutan Civil Society Network (BCSN) to coordinate their activities and interests.

CSOs in Bhutan are governed by the Civil Society Act of 2007. CSO leaders have called for amendments to this act for greater clarity and to remove overly restrictive provisions, such as the yearly renewal of registration and tax exemption on a case-by-case basis. A CSO Amendment Bill was passed by the National Council, the upper house, in June 2021. In July 2022, according to the Bhutanese, the joint session of parliament adopted the amendment bill and sent it to the king for approval.

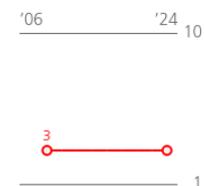
Opinion poll data from and within Bhutan is extremely limited. According to the 2010 Gross National Happiness survey conducted by the Center for Bhutan and GNH Studies, 92% of respondents expressed their intention to vote in the upcoming election, which the survey's reporters interpreted as a commitment to democracy. However, it could also indicate a recognition of civic duty. A national human development report titled "Ten Years of Democracy in Bhutan," released in March 2019 by Prime Minister Lotay Tshering and U.N. Under-Secretary-General, reported on the findings of a survey. The report revealed that over 80% of Bhutanese surveyed were able to exercise their right to freely express their opinions, and 75% reported that they were able to enjoy their constitutional rights.

Compared to 2013, voter turnout was higher in both the National Council and National Assembly elections in 2018. In April 2018, 54.3% of registered voters cast their ballots in the National Council elections, an increase of nine percentage points from 2013. In the primary round of the 2018 National Assembly elections, voter turnout was 12 percentage points higher than the 66% reached in the previous election – an encouraging sign of greater participation. In the general round of the National Assembly election in October 2018, voter turnout reached 71.46%, signifying an increase of five percentage points from the 66% voter turnout in 2013. These figures can be interpreted as reflecting greater awareness and support for democracy.

Traditionally, decision-making focuses on building consensus using mediation, both in the policy process and in the operation of the judiciary. The traditional acquiescence of society to the state, and its acceptance of the state's legitimacy, may have been transferred to the new democratic institutions as their latest manifestation.

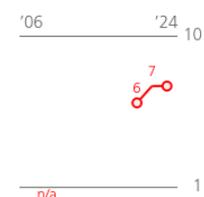
Interest groups

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Approval of democracy

7



The rise of competitive political parties and elections has increased personal contact between political leaders and the public. Additionally, the rapid increase in internet penetration and access to social media in the country has reportedly increased the discussion of politics and policy matters.

Traditional rural Bhutanese society had a variety of civil society organizations. These were locally based, often around Buddhist monasteries, and focused on community functions such as mutual support, water management, and religious festivals. Some of these have survived to the present day, although urban-rural migration and modernization have led to the disappearance of some organizations or at least hampered their work. Kinship networks retain their importance even in urban areas and are characterized by close interaction and the provision of help in times of crisis. However, traditional rural community solidarity has not been replaced by new autonomous organizations in urban areas. There are some NGOs and sports clubs, but modern forms of voluntary association are still rare. The 2015 Gross National Happiness survey recorded a small but statistically significant increase in happiness since 2010, but the scores on community relationships and psychological well-being were “significantly worse.” For example, in 2015, only 26% of respondents reported that they trusted most of their neighbors, compared to 46% in 2010. Correspondingly, there was a rise in respondents who trusted a few of their neighbors – from 14% in 2010 to 34% in 2015. Lastly, the new Civil Society Organization Amendment Act adopted in July 2022 may allow CSOs greater flexibility and funding.

Social capital

5

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II. Economic Transformation

6 | Level of Socioeconomic Development

Bhutan’s economy grew by 4.9% in 2021/2022. The GDP growth rate was projected to be higher in 2023, especially considering the forecasts for a higher growth rate in India. In 2020/2021, the GDP declined by -10.8% due to the disruption caused by the COVID-19 pandemic.

In 2018, Bhutan’s improved gross national income (GNI) qualified the country to graduate from its “least-developed country” (LDC) status in the United Nations Committee for Development Policy (UNCDP) classification. The GNI threshold for graduation is a three-year average of \$1,242 per person. Bhutan also improved its Human Asset Index, another indicator of vulnerability associated with LDC status, from 45 in 2000 to 73 in 2018, driven mainly by an increase in gross secondary education enrollment. However, Bhutan’s graduation date from its LDC status was postponed to 2023, following the government’s request for more time to prepare for this transition. Upon graduation from the LDC, Bhutan will no longer qualify for

Question

Score

Socioeconomic

barriers

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specific kinds of development assistance. In 2018/2019, the country's economy grew by only 4.4%. The forecast for 2020/2021, according to the Asian Development Bank (ADB), ranged between 5.2% and 5.8%, which can be attributed to the country's struggle amid the pandemic.

In 2022, Bhutan achieved the 127th rank in the Human Development Index (HDI), an improvement from the previous year's score of 129th out of 191 ranked countries. Bhutan's HDI places it among countries that have consistently made gains on all human development indicators. The country's value for 2022, at 0.666, is quite remarkable compared to 0.510 in 2005. Bhutan's progress is attributable to increased life expectancy, a higher number of students staying in school, and an increase in per capita income. Since 2005, Bhutan's life expectancy at birth has risen from 64.9 years to 71.8 years in 2019. The expected number of years of schooling has almost doubled in the same period. Despite Bhutan's 2019 HDI being higher than the average for South Asian countries (0.641), when adjusted for inequality, the country's HDI drops to 0.46, representing a loss of 27.2%, which is higher than the average loss for South Asia of 25.9%. From 2017 to 2018, Bhutan maintained an impressive economic growth rate of over 7.5%, making it the fastest-growing economy in developing Asia. The growth rate for 2018 and 2019, according to the Asian Development Bank (ADB), was 3.8% and 4.3%, respectively. The ADB has revised its GDP growth estimate for 2020 to 0.9%, projecting an economic contraction of -3.4% for 2021.

According to the ADB's April 2020 outlook, 8.2% of Bhutan's population of 73 million lives below the national poverty line of \$1.90 PPP per day. The pandemic has exacerbated the traditional economic disadvantages faced by women in Bhutan. A 2022 study by the Bhutan Chamber of Commerce indicates that businesses owned by women were the most severely impacted.

Economic indicators		2019	2020	2021	2022
GDP	\$ M	2535.7	2325.2	2539.6	-
GDP growth	%	5.8	-10.0	4.1	-
Inflation (CPI)	%	2.7	5.6	7.3	5.6
Unemployment	%	2.7	5.0	3.9	3.6
Foreign direct investment	% of GDP	0.5	-0.1	0.3	-
Export growth	%	14.4	-20.2	8.9	-
Import growth	%	-6.2	-12.4	15.7	-
Current account balance	\$ M	-500.8	-381.2	-321.5	-852.6

Economic indicators		2019	2020	2021	2022
Public debt	% of GDP	106.5	122.8	132.4	127.3
External debt	\$ M	2703.8	3036.8	3069.4	-
Total debt service	\$ M	61.6	57.9	118.4	-
Net lending/borrowing	% of GDP	1.6	-2.7	-	-
Tax revenue	% of GDP	15.6	13.0	-	-
Government consumption	% of GDP	18.3	20.8	21.7	-
Public education spending	% of GDP	4.8	6.0	7.0	8.1
Public health spending	% of GDP	2.7	3.4	-	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	-	-	-	-

Sources (as of December 2023): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

7 | Organization of the Market and Competition

In Bhutan's economy, the state plays a major role through state-owned enterprises (SOEs) that contribute 50% of the tax revenue. Of this revenue, hydropower accounts for 85%, signifying a high degree of dependence on this specific source of income. The SOEs, including Druk Holding, provide employment for about 12,600 people, of whom about 3,600 are in SOEs owned by the Finance Ministry. There is government intervention in the pricing of items such as gasoline, bus fares, propane, and meat. There are few large private companies and a small, unregulated commercial informal sector. Generally, market access and demand for Bhutan's goods and services underlie rather favorable conditions due to the country's completely open access to the Indian market as part of one of the most liberal trade agreements in the world. However, market-based competition is still at a rudimentary level in a very small economy.

The informal sector dominates the economy, with only 23.1% of employment categorized as "regularly paid" in the Labor Force Survey Report of 2015. In 2016, the World Bank estimated that Bhutan's informal sector employed 80% of the workforce. According to the Labor Force Survey Report of 2019, agriculture remains the principal source of income and employment for the majority of the population, employing 51.1% of the active workforce. However, in 2018, agriculture accounted for only 16% of GDP. Furthermore, there is still a strong subsistence character to much of the agricultural production. In 2018, the service sector employed 34.9% of

Market
organization

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the workforce, followed by industry, which employed 14%. Tourism is the major contributor to the service sector and was severely disrupted by the pandemic. In 2022, Bhutan raised its Sustainable Development Fee, which it charges foreign visitors upon arrival, from \$65 to \$200. This will have implications for tour operators, hoteliers, and related sectors.

Bhutan has continued to implement regulatory reforms to enhance the business environment and enable greater access to foreign assets for the private sector. The country faces challenges in attracting foreign direct investment (FDI) due to its landlocked position, small domestic market, distance from global and regional markets, limited economies of scale, narrow economic base, and susceptibility to natural disasters. Additionally, the government aims to cap FDI inflow below Bhutan's GDP. Prime Minister Lyonchhen has expressed concerns that an FDI amount exceeding BTN 100 billion could adversely impact the economy. Apart from a negative list, foreign investors are permitted to hold up to 74% equity, and the repatriation of investment and profits in foreign currencies requires government approval. In June 2021, Bhutan passed a customs act that established a uniform import duty rate of 10% for over 500 products, excluding alcohol, tobacco, gold, and silver.

Local businesses report difficulties in gaining access to finance. Some modest liberalization of foreign direct investment rules occurred in 2014, but entry and exit barriers to domestic markets remain particularly high for foreign companies. Starting in 2013, the time it takes to start a business has been reduced by two-thirds. It now takes 12 days and eight procedures, with a cost of 3.5% of GNI per capita. The main hurdle for businesses is the shortage of Indian rupees. The government has reaffirmed the principal role of state-owned enterprises (SOEs) with the passage of the Mines and Minerals Act 2020, as the act grants sole control of the sector to the government-appointed Mining Regulatory Authority. In 2019, the State Mining Corporation Ltd. earned BTN 1.43 billion, achieving a 108% dividend from its coal and gypsum mines.

With the absence of a significant private sector, the state has established a number of enterprises. Some of these have been privatized; others have been corporatized. A substantial state-owned enterprise (SOE) sector remains, presiding over some monopolies such as television, electricity, sand, timber, and postal services. There is a limited number of large private-sector corporations. No laws on anti-competitive practices, monopolies, and cartels are in place, but the Consumer Protection Act was passed in 2012. It sets out the rights and responsibilities of consumers and is administered by the Office of Consumer Protection. There appears to be low awareness of the act, and there are reports of goods being sold above the maximum retail price. Nevertheless, the act has slightly boosted competition in the economy.

Competition policy

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Private sector organizations feel that there is still no level playing field, however. In 2015, instead of competition law, the government of Bhutan decided to adopt the National Competition Policy (NPC). The decision was taken after a careful evaluation of enforcement capacity with the active assistance of UNCTAD. The NPC was drafted to create fair competition, prevent business monopolies, and encourage small and medium-sized enterprises. This occurs through the prerequisite for the government to conduct an impact assessment for new legislation regarding competition, practices and existing laws. Infrastructural facilities and public services are explicitly excluded from the rules of the NPC. The proposed Mines and Minerals Act 2020 grants a monopoly to a government-owned authority for the exploration and marketing of mines and minerals. Bhutan has slightly improved its position in the World Economic Forum's Global Competitiveness Index. It was ranked 97th out of 138 economies in 2016/2017. In the 2018 Competitiveness Index, Bhutan ranked 82nd out of 140 countries. Among its South Asian counterparts, Bhutan ranked second behind India.

Bhutan has made modest efforts to promote trade liberalization and enjoys observer status in the World Trade Organization (WTO). The two major concerns behind the decision not to join the WTO are the impact of membership on Bhutan's Gross National Happiness (GNH) program and doubts about Bhutan's ability to benefit from WTO membership. Additionally, WTO membership could lead to more imports and deficits. Bhutan is a founding member of the South Asian Preferential Trade Area (SAPTA), the South Asia Free Trade Association (SAFTA), and a member of the Bay of Bengal Initiative for Multi-Sectoral Technology and Economic Cooperation (BIMSTEC). Bhutan has yet to join the land transport agreement known as the Bangladesh-Bhutan-India-Nepal (BBIN) Motor Vehicle Agreement. On the bilateral front, Bhutan has a free trade agreement with India, a preferential trade agreement with Bangladesh, and a trade and cooperation agreement with Thailand.

In July 2021, Bhutan revised its customs act to impose a uniform customs duty of 10% on imports from all countries except India and on all goods except automobiles, tobacco, and alcohol. This was a significant reduction compared to the previous rate of 50%.

Bhutan's effective tariff rate has been very low. In 2015, the average tariff rate was 2.82, but it rose to 4.13 in 2019. This situation is reflected in the World Bank's ranking of Bhutan in "trading across borders," where it holds the 26th rank out of 190 countries. Bhutan scores low on the Logistics Performance Index, ranked 135th out of 160 countries in 2016. The landlocked situation of Bhutan creates difficulties similar to those observed in other Asian countries such as Nepal and Mongolia. However, adding to the difficulties, Bhutan has no direct cross-border trade link with its northern neighbor, China. The bulk of Bhutan's imports and exports are from countries with which Bhutan enjoys free trade or preferential trade, notably India, which accounts for over 80% of Bhutan's trade.

Liberalization of
foreign trade

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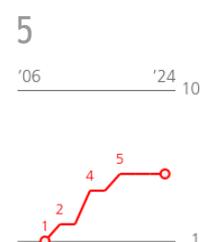
Foreign investments receive the same treatment as similar domestic investments. Foreign ownership is permitted in education services (except technical and vocational institutions), private health care, five-star hotels, infrastructure, research and development, head office services, and information technologies. In the financial services industry, up to 51% foreign ownership is allowed, while in all other activities, up to 74% foreign ownership is permitted. Exceptions to this liberal policy include media and broadcasting, the distribution of services in wholesale, retail and micro trade, as well as mining and the sale of minerals in primary or raw form.

Until 2010, state banks held a monopoly in Bhutan. There are now five banks present, including four commercial banks and the Bhutan Development Bank, which is concerned with financing rural development. Financial market development has improved significantly in recent times, according to the World Economic Forum, from a rank of 111 out of 144 economies in 2014/2015 to 79th in 2016/2017. The banking sector has been advancing “steadily,” according to the ADB. Geographically, this growth in the banking sector has concentrated on the capital city of Thimphu. This centralized regional distribution is, in part, criticized for exposing the sector to vulnerability.

There have been high rates of credit growth in recent years and an increase in nonperforming loans, especially after the government enforced restrictions on Indian rupee credits in 2012. This led to the ratio of banks’ nonperforming loans to total gross loans rising from 3.9% in 2011 to 11.38% in 2016. According to the World Bank, as of March 2018, the gross nonperforming loan ratio was 14.6%, two percentage points higher than a year before, which, in turn, lowered the profits of financial institutions. However, the assets of banks have increased by a greater amount. According to the World Bank, the bank capital-to-assets ratio was 17.8% in 2015.

Access to financing has been consistently identified as the biggest problem for small and medium enterprises in surveys by the World Bank and the World Economic Forum. Most lending is collateral-based, requiring up to 2.5 times the value of the loan in items such as land, equipment, or personal assets. Requirements of this kind are not only the highest among SAARC countries, but even among the highest in the world. Loan rates were cut in 2016 following recommendations of the World Bank’s Financial Development Action Plan. In order to ease access to Indian rupees, Bhutan began the first phase of making RuPay payment cards available to Bhutanese in August 2019. In the second phase, Bhutan’s banks are expected to issue RuPay cards to the citizens, allowing them to access the RuPay network in India.

Banking system



8 | Monetary and fiscal stability

Bhutan's currency in 2022 depreciated by over 7% against the dollar, contributing to the price hike of imported goods. The Bhutanese currency, the ngultrum (BTN), is pegged to the Indian rupee (INR), with one BTN equal to one INR. This makes Bhutan vulnerable to shifts in the Indian economy, particularly the inflation rate. The exchange rate of the ngultrum to the U.S. dollar was approximately 76:1 in 2022.

In the fiscal year 2020/21, inflation reached 8.2% but declined below 5% by November 2022. In 2012, inflation reached its highest-ever value at 10.32%. The shortage of Indian rupees resulted in temporary bans on certain imports, such as cars, and the scarcity of some goods, like building materials.

Since 2012, inflation has steadily dropped to its lowest level ever recorded in 2016, at 3.22%. According to the ADB, inflation was at 2.69% in 2018, 2.8% in 2019, and 3.0% in 2020. For 2021, it is projected to rise to 6.4%. The Indian rupee is recognized as legal tender in Bhutan, but only for notes worth up to 100 INR. The introduction of a general services tax (GST) in India has had a positive impact on lowering inflation since it removes all levies on goods exported out of India. In 2018, Bhutan reported an annual average inflation rate of 2.69%, the lowest inflation since the National Statistics Bureau (NSB) began tracking it 15 years ago.

The Royal Monetary Authority (RMA) is Bhutan's central bank. It is independent from the government and is empowered to regulate the availability of money and its international exchange, supervise and regulate banks and other financial institutions, promote monetary stability, as well as credit and exchange conditions, and foster a financial structure conducive to the balanced growth of the economy. In July 2020, Bhutan passed a Goods and Services Tax (GST) Act introducing a standard single rate of 7%, which would subsume sales tax and modify the excise system. The GST is a consumption-based tax and is intended to eliminate the cascading taxation effect.

In the 2022/23 annual budget report, the finance minister reported a fiscal deficit of BTN 22.882 billion, accounting for 11.25% of the GDP. This followed a deficit of over BTN 17 billion in the 2021/22 budget year, which exceeded Bhutan's 12th plan target of keeping the deficit under 3% of the GDP. In FY 2019/20, Bhutan ran budget deficits of -2% and -6.2% of its GDP, respectively.

As of June 2022, Bhutan's total external debt was BTN 229.52 billion, having increased by 3.3%, or equivalent to BTN 7.4 billion, from March of the same year. Similarly, domestic debt was BTN 28.06 billion, an increase of 9.7%, or BTN 2.49 billion, from March of the same year.

Monetary stability

5



Fiscal stability

6



The increase in domestic debt is due to the issuance of new government bonds for deficit financing. According to the annual audit report 2020/21 released in November 2021, Bhutan's total national debt, as of June 2021, amounted to BTN 238.398 billion. This accounts for 129.06% of the GDP. Bhutan's GDP for the year was recorded at BTN 184.715 billion.

As of June 2020 data, the country's public debt stood at \$8.5 billion, slightly over 100% of its GDP. Of this, \$189.66 billion is external debt.

In fiscal year 2022/23, Bhutan's external debt servicing (principal and interest) was projected to amount to BTN 9.3 billion. The World Bank assessed Bhutan's risk of external debt distress as "moderate" due to "unique and mitigating circumstances." These circumstances include the majority of loans for hydropower construction owed to India, with the Indian government covering all financial and construction risks. Additionally, India purchases Bhutan's surplus electricity. As hydropower projects come on stream, debt is expected to decline substantially to below 50% of GDP by 2026.

To offset the current account deficit, the government borrowed from multilateral banks and the domestic market. In September 2020, Bhutan issued its first-ever sovereign bond worth BTN 3 billion, with a three-year maturity period. Eventually, all the issued bonds were purchased. As of August 2019, remittances sent by Bhutanese working abroad had shrunk to half the amount received in 2018 when they stood at BTN 3 billion. Since the launch of the money transfer platform RemitBhutan in 2016, remittances have generally increased.

In the fiscal year 2021/22, Bhutan's trade deficit stood at over BTN 13 billion, a significant increase from the same period in the previous fiscal year when it was BTN 10 billion. In 2019, the trade balance in current prices was recorded at a deficit of BTN 29.124 billion, accounting for 16.34% of GDP. In 2018, the trade deficit increased by 13.03%. However, according to provisional figures from the Ministry of Finance, Bhutan's trade deficit declined by 32% in the first half of 2020 compared to figures for the same period of the previous year, when the trade deficit decreased from BTN 19 billion to BTN 12.84 billion. The increase in exports was primarily driven by an increase in the export of electricity to India due to the commissioning of the Mangdechhu Hydroelectric Project in June 2019.

Bhutan's foreign exchange reserve sank from \$1.46 billion in April 2021 to \$970 million by the end of December 2021. In November 2020, Bhutan's foreign reserves were at \$1.43 billion.

9 | Private Property

The constitution guarantees Bhutanese citizens the right to hold property, and there are well-maintained records of land holdings and ownership. The Land Act of 2007 provides comprehensive coverage of the regulation and administration of land and is administered by the National Land Commission. There are only a few large landowners, and foreign ownership of land is not permitted. Property rights are viewed as secure in all surveys, and the acquisition of property is not mentioned as a problem by businesses. However, the ACC has expressed concern about possible corruption relating to land matters. Problematically, the Lhotshampa minority of Nepalese origin, whose members cannot become citizens, does not enjoy these property rights.

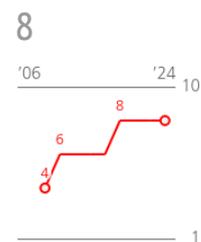
Bhutan recognizes individuals' rights in relation to their intellectual property and has 24 laws in place to safeguard it, according to the World Intellectual Property Organization (WIPO). These laws include the Copyright Act, Legal Deposit Act, Seeds Act and Industrial Property Act, among others. Bhutan is a signatory to international treaties that WIPO identifies as governing intellectual property rights.

The state maintains a dominant role in modernizing Bhutan and its economy. Without a significant private sector presence, the state possesses several enterprises. Among the 16 SOEs under the Ministry of Finance, a few have undergone privatization or corporatization. Bhutan does offer competitive advantages for private sector growth, such as political stability, good governance, low corruption levels, accessible electricity, abundant natural resources, and preferential access to the vast Indian market. Additionally, it has implemented the National Intellectual Property Policy 2018, which introduces the geographical indication system to safeguard product designs.

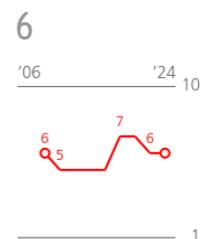
In recent years, the airline industry, banking, and the media in Bhutan have seen the entrance of private sector competition; however, these sectors continue to face significant constraints. Government attempts to enhance innovation in the private sector have had limited success. Bhutan has approximately 28,000 registered businesses, with 92% classified as micro-businesses and 76% employing fewer than five individuals. Despite a notable improvement, Bhutan's rank of 82 out of 140 countries in the Global Competitive Index 2017/18 places the country within the lower half of the rankings.

In 2019, the government formed a 10-member private sector development committee under the Ministry of Economic Affairs to help Bhutan's Chamber of Commerce and Industry expand private sector firms' involvement in the economy. Bhutan's tourism sector, employing around 50,000 people, was the worst affected by COVID-19. Government assistance may not save many tourist sector businesses, especially high-end hotels. This sector may suffer even greater setbacks if Bhutan's Tourism Levy Act 2022, which raised the Sustainable Development Fee for foreign visitors from \$65 to \$200, reduces the number of foreign visitors even further.

Property rights



Private enterprise



10 | Welfare Regime

The state offers free education and health care to all citizens, but it does not provide other welfare benefits such as social security payments, conditional cash transfers, or food subsidies. Public servants, military personnel, employees of state-owned enterprises, and certain private sector employees have access to pension programs. However, the rural population and those working in small-scale enterprises are not eligible for these programs. Periodically, the king grants the traditional gift of kidu (land and citizenship) to vulnerable individuals. The family serves as the primary social safety net in both rural and urban areas. Strong obligations exist to care for one's kin, although these may be weakening due to urbanization. Local religious institutions may offer some assistance to individuals and communities, while NGOs and external organizations occasionally provide temporary relief to those in need.

The Druk Gyalpo's Relief Kidu, launched on April 14, 2020, has provided income support to individuals affected by the COVID-19 pandemic. So far, it has granted BTN 1.4 billion to 34,384 individuals, including a child support kidu of BTN 50.2 million. The Relief Kidu lasted for three months, from January to March 2021, and provided full payments of BTN 10,000 and partial payments of BTN 7,000.

Problems in accessing health services persist – at least one in three children under the age of five suffers from malnutrition, according to UNICEF 2019.

Bhutan does not discriminate based on gender, ethnicity, or social/economic status in its laws. However, in reality, women face unequal access to opportunities. According to the World Economic Forum's Global Gender Gap report of 2022, Bhutan has made progress but still ranks 126th out of 146 countries.

Leadership positions are still dominated by men. In 2013, two of the four parties contesting the primary election for the National Assembly were led by women, but both parties failed to capture enough votes to participate in the general election. In 2018, a party led by a woman participated in the primaries but failed to advance to the general election. In the 2013 to 2018 parliament, only four of the 47 members of the National Assembly were women, and there were only two women in the 25-member National Council, both appointed by the king. In the 2018 elections, seven women were elected to the National Assembly, and two women were also elected to the National Assembly. In the 2022 local government elections, Bhutan saw a larger participation of women as candidates and winners than in earlier elections. Only 0.5% of LG representatives were women in the first LG elections. In 2022, the share rose to 3.41%.

Women increasingly participate in the workforce but lag behind men. According to recent World Bank data (2016), the International Labor Organization (ILO) estimates put the female participation rate at 59%, which, however, stands high in contrast to other Asian countries. The ILO's more recent model estimates indicate that this rate reached 67% in 2018. Furthermore, a higher proportion of women are engaged in

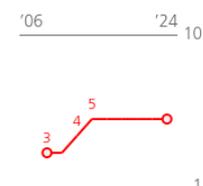
Social safety nets

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Equal opportunity

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agriculture compared to men. Women’s literacy rate stands at 57%, while men’s is 75%. The proportion of women with secondary education and in the labor force is considerably lower than that of men. The education gap is particularly evident in secondary and higher education, as girls’ enrollment in primary education is equal to that of boys. In Bhutan, only 6% of women have attained at least a secondary-level education, as opposed to 13.7% of men.

Discrimination based on language and religion is commonly faced by several minorities. According to the U.S. State Department’s 2017 Human Rights Report on Bhutan, which relied on informed sources, approximately 1,000 stateless families exist, predominantly comprising people who speak Nepali and reside in the southern part of the country. Stateless individuals are deprived of various public services, such as health care, education, and employment prospects.

11 | Economic Performance

Quantitative indicators show that Bhutan’s economy is rebounding from the contraction it experienced in 2020/21 due to COVID-19 shutdowns. According to the ADB forecast, the economy is projected to grow by 4.5% in 2021/22 and 4.0% in 2023.

Bhutan is the wealthiest country in South Asia, with a per capita GDP of \$3,491 in 2022. According to a report by Bhutan’s National Statistics Bureau (NSB) in October 2022, the price of consumer goods and services increased by 6.05% in September 2022, surpassing the previous year’s rate of 4.97%. Inflation was primarily driven by rising food and fuel prices. From 2012 to 2019, Bhutan consistently achieved an average annual GDP growth rate of over 6%. In 2017/18, Bhutan’s GDP grew by slightly over 7%, making it one of the fastest-growing economies, according to the ADB. However, the agricultural sector has experienced little to no growth, despite over 50% of the population relying on it for their livelihoods. Foreign direct investment in Bhutan has been unstable and low, ranging from a peak of \$75.3 million in 2010 to \$8.3 million in 2014 and \$33.6 million (1.6% of GDP) in 2015. The economy suffered significant setbacks in the 2019/20 period due to the COVID-19 pandemic, resulting in a 10% contraction. The growth rate in 2018 and 2019, as reported by the ADB, was 3.8% and 4.3%, respectively. The estimated GDP loss in the first six months of the COVID-19 crisis in 2020 amounted to nearly BTN 5 billion. By May 2020, more than 6,500 Bhutanese individuals had returned to the country from abroad due to the pandemic. Unemployment, particularly youth unemployment, reached approximately 25% in 2020, posing a significant challenge. However, by 2021, this rate had dropped to 20.9%. The overall unemployment rate in 2021 was 4.8%.

Output strength

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In the 2022/23 annual budget report, the finance minister reported a fiscal deficit of BTN 22.882 billion, which is 11.25% of the GDP. This followed a deficit of more than BTN 17 billion in the 2021/22 budget year. This level of deficit far exceeded Bhutan's 12th plan target of keeping the deficit under 3% of the GDP. In FY 2019/20, Bhutan ran budget deficits of -2% and -6.2% of its GDP, respectively. As of June 2022, Bhutan's total external debt was BTN 229.52 billion, an increase of 3.3% or equivalent to BTN 7.4 billion from March this year. Similarly, domestic debt was BTN 28.06 billion, an increase of 9.7% or BTN 2.49 billion from March this year. The increase in domestic debt was due to the new issuance of government bonds for deficit financing. Bhutan's total national debt as of June 2021 stood at BTN 238.398 billion, according to the annual audit report 2020/21 released in November 2021. This is 129.06% of the GDP. Bhutan's GDP during the year was recorded at BTN 184.715 billion. As previously mentioned, according to June 2020 data, the country's public debt stood at \$8.5 billion, slightly over 100% of its GDP. Of the public debt, \$189.66 billion is external.

12 | Sustainability

The constitution declares that it is “a fundamental duty of every citizen to contribute to the protection of the natural environment, conservation of the rich biodiversity of Bhutan, and prevention of all forms of economic degradation.” Bhutan ratified the 1992 U.N. Framework Convention on Climate Change (UNFCCC), the 1997 Kyoto Protocol, and the 2015 Paris Agreement. The country achieved Millennium Development Goal 7 on the environment. Over 70% of its land area is covered by natural forests, and over 50% of the country is protected as national parks, nature reserves, or biological corridors.

There are serious environmental problems, including solid waste disposal, the impact of road construction, the loss of prime agricultural land to urbanization, illegal logging, overexploitation of non-timber forest resources, livestock in excess of the land's carrying capacity in some areas, and a growing number of vehicles. Over 40% of economic activities rely on hydropower, which is highly susceptible to climate change. Bhutan has 573 glacial lakes, of which 17 are reported to be reaching dangerous conditions due to climate change. In 2020, about 65% of households lacked access to waste collection services. Even in urban areas, one-fourth of households are left without access to waste collection. In 2021, there were reports of major corruption in waste management, and in the following year, waste collection facilities in Thimphu were running at capacity. Access to water is also a serious issue. According to a report in Kuensel Online (June 2019), only 1.53% of Thimphu residents have 11 to 18 hours of water supply, with 29% receiving less than two hours of water a day. Water shortage is also causing farmers to cut back on paddy farming. The government plans to implement a water flagship program supported by the European Union, aiming to ease the shortage by 2021. Bhutan's water resources are also under threat. Its glacier-fed rivers, streams, and lakes, the main sources of water, are melting.

Environmental policy

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Considerable improvements have been made in the availability of education in Bhutan. Universal primary education has been achieved, and secondary education has experienced significant growth in recent years, with the gross enrollment ratio reaching 78%. At all levels of secondary education, boys and girls are equally represented. Tertiary enrollments are also on the rise, although they currently only account for 9% of the age group. Bhutan's educational landscape includes two universities: the Royal University of Bhutan and the Khesar Gyalpo University of Medical Sciences of Bhutan. Additionally, many Bhutanese students pursue higher education in India. In 2021, Bhutan boasted a youth literacy rate of 97% for the age group of 15 to 24. As for adult literacy, it reached 66.5% in 2022, showing a noticeable increase from 63% in 2012. Notably, in 2021, Bhutan allocated 7% of its GDP to education.

These figures reflect the late development of mass education in the country. Among young people aged 15 to 24, literacy was 93% in 2017. The amount spent on education was equivalent to 7.1% of the GDP in 2017. Bhutan's value on the U.N. Education Index was 0.496 in 2019.

Supplying books and equipment to remote areas remains a challenge in Bhutan. The country is confronted with a significant shortage of teachers, with 3.6% of educators leaving the profession each year. Teaching is not considered an appealing career choice, resulting in a dearth of qualified teachers.

Education policy /
R&D

5



Governance

I. Level of Difficulty

Bhutan is a landlocked country with a small market, spread across a complex and largely mountainous terrain. Road infrastructure is constantly being improved, and the east-west axis across the country is motorable and used by buses, trucks, and private cars. However, landslides are a hazard in the rainy season, while roads can be blocked by snow in winter. Additionally, earthquakes have sometimes caused considerable damage to roads. Climate change has increased the risk of flash floods and landslides.

Domestic air services, which began in 2012, are currently very limited and unaffordable for most of the population. International air services have begun to react to the increase in tourist numbers and the number of Bhutanese traveling abroad. Prior to 2013, the government-owned Drukair was the only airline, until the introduction of Tashi Air, a private airline, which started international operations that year. However, the expansion of air travel is hindered by the restricted capacity of the primary airport in Paro. The Indian military oversees air traffic control.

Bhutan has successfully reduced poverty rates from 23% in 2007 to 12% in 2012 and further down to 8.2% in 2017. During the period from 2007 to 2017, improvements in living conditions, amenities, and dietary behaviors have contributed to the reduction of poverty in rural areas. However, a significant number of rural households still live near the poverty line. Approximately 30% of all households in Bhutan are led by women, whose familial and care responsibilities prevent them from accessing employment opportunities. The rate of youth unemployment has been on the rise, increasing from 10.7% in 2015 to roughly 25% in 2020, with young people often lacking the necessary skills for modern occupations. Particularly for females, the rate of youth unemployment is even higher than that of males. In 2022, youth unemployment remained above 20%. Bhutan is currently experiencing a labor shortage in the medical and education sectors, particularly in nursing. Many professionals in these fields are either leaving the profession or emigrating from the country.

Structural
constraints

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Bhutan has historically been administered under traditional forms of civil society, where organizations took on functions such as ensuring livelihood security, managing water rights, and preparing festivities. Community leadership and citizen volunteering have sustained these civic engagements. The organizations were based in local communities and sometimes associated with monasteries. Many of these organizations still exist today but face challenges due to rural-urban migration and the resulting depopulation of remote areas.

Modern forms of civil society, such as NGOs and professional associations, are only a recent development in Bhutan. They are governed by the Civil Society Organizations Authority (CSOA), which operates under the terms of the Civil Society Organizations Act.

The Registration Act of 2007 marked the beginning of the development of modern civil society in Bhutan. This process has been gradual, with significant changes occurring over time. In 2010, the CSOA website listed 10 public benefit organizations (PBOs) and one mutual benefit organization (MBO). By 2018, the number of PBOs had grown to 35, while there were nine MBOs. PBOs encompassed a range of fields, including organizations focused on women, youth, the disabled, senior citizens, the environment, animals, sports, and health. On the other hand, MBOs primarily consisted of industry-related associations operating in handicrafts or tourism.

To enhance the functioning of civil society organizations and enhance transparency and accountability, Bhutan's parliament revised the 2007 Civil Society Organization Act in 2022.

Following the expulsion and flight of up to 100,000 Lhotshampa residents, ethnic tensions and conflicts of the early 1990s have subsided. Citizenship requirements have been clarified and appear to be widely accepted, although some Lhotshampas still only have resident status. Most of the refugees in Nepal have been resettled to third countries, and as a result, their political activities and organizations have little or no effect in Bhutan. However, the issue of minority-majority relations could lead to future tensions in Bhutan's society. There are no religious conflicts in Bhutan. Buddhism is seen as the religious foundation of the country, and while religious freedom is guaranteed in the constitution, missionary activity is prohibited, and government permission is required for new religious buildings. There is no political mobilization based on social classes. Decision-making is generally consensual in nature, so overt conflict is avoided. Citizens accept and anticipate the guidance of a strong state.

Civil society traditions

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Conflict intensity

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II. Governance Performance

14 | Steering Capability

The state has a guiding philosophy of national development based around the concept of Gross National Happiness (GNH). GNH describes an idea that originated from Jigme Singye Wangchuck, the fourth Bhutanese king, and to which all political parties and other domestic political actors adhere. It can be seen as an alternative model to measure wealth and development using GDP. There is a long-standing utilization of five-year plans to provide strategic direction to national development within the context of GNH. In 2018, Bhutan completed the 11th five-year plan (2013 – 2018) and began its twelfth (2018 – 2023). The 11th five-year plan focused on strengthening institutions, systems, capacity-building, and enhancing the quality of goods and services. The succeeding five-year plan highlighted the need for the three Cs – coordination, consolidation and collaboration – to ensure the achievement of the plan’s formulated goals.

Due to the COVID-19-related loss of revenue and unforeseen expenditures, the government had to readjust some aspects of the 12th plan’s schedule. As Bhutan is poised to graduate from the Least Developed Country list in 2023, the ruling DNT government is pushing for replacing the five-year plan with a flexible development model. The opposition party DPT opposes this shift.

The increasing costs of funding the five-year plans – over BTN 300 billion for the 12th five-year plan – pose a challenge to government finances. In addition, some of the outputs, most notably the increasing youth unemployment among educated people, are creating new policy problems. In 2017, the World Bank funded several development projects in Bhutan to promote economic growth. These included the Bhutan Living Standard Survey, the Preparation of Strategic Program for Climate Resilience, the Food Security and Agriculture Productivity Project – which aims to reduce reliance on food imports – and the Youth Employment and Rural Entrepreneurship Project – which aims to create more jobs.

In October 2022, the Gross National Happiness Commission (GNHC), which, under the 12th plan, was tasked with overseeing the progress of the three Cs, was dissolved. Commenting on this political decision, the Bhutanese Minister for Economic Affairs declared that “the Gross National Happiness Index, which is highly regarded internationally, would have to allocate more space for economic growth.” The GNH commission consisted of six divisions, which have now been integrated into either the Office of Cabinet Affairs or the Ministry of Finance. This has created a void in terms of symbolic prioritization. However, since the institution’s branches are not abolished but only restructured, it is yet to be seen how the dissolution of the commission will affect the pursuit of the respective policy goals.

Question
Score

Prioritization

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In the previous or current cabinets, little or no internal strife has been reported. However, this is expected in a country where consensus is highly valued, hierarchy is respected, and conflictive politics are avoided. The opposition parties in the national assemblies have questioned government actions, but the greatest scrutiny has come from the nonpartisan National Council. As electoral legislation only permits two parties to be present in the National Assembly and members cannot switch parties, the party that has won the majority forms the government and will always be able to out-vote its opposition. In October 2022, the opposition leader criticized the government for its failure to implement programs without exceeding the budgetary allocations of the 2021/2022 budget. For instance, some of the agencies had exceeded their allocations threefold.

This supports the government in implementing its policies, although rigorous scrutiny from the National Council has resulted in the rejection of some proposed legislation. In 2019/2020, divergences in opinion between the two houses of parliament became more public and contentious. The National Council appears to be acting as a quasi-opposition to the ruling party, but such a role may conflict with the national emphasis on consensus and advancing GNH goals. COVID-19 interrupted the implementation of regular policies, especially in the areas of education, business, and the goals of the 12th five-year plan.

The civil service is responsible for implementing policies and has demonstrated effectiveness in this regard. Recently, concerns have been raised about inefficiencies and corruption. In 2022, senior officials in the civil service underwent performance tests, and some of them were removed from service to increase efficiency. However, the civil service can mostly be credited with the steady improvement in welfare indicators, as it assumes the majority of responsibilities for education, health, infrastructure, agriculture, and other services. It is organized bureaucratically with procedural guidelines, and its component agencies have staff working in the districts (dzongkhags) in a decentralized manner. Some areas of civil service operations lack necessary skills. Efforts to modernize the civil service have been moderately successful and are ongoing. The implementation of policies in remote areas remains a challenge. For the first time, the 12th five-year plan aims to allocate 50% of the planned budget to local bodies.

Bhutan has demonstrated a capacity to learn from its own experiences and from those of other countries – not only neighboring India. The most remarkable instance of policy learning has been the transition from a long-standing authoritarian political regime to a constitutional monarchy. The transition has been smooth and reflects the country's ability to adapt imported institutions to fit the Bhutanese context. However, some authoritarian practices and characteristics remain, such as the difficulties in obtaining information from the government and constraints on the media.

Through multilateral organizations such as the United Nations Development Programme (UNDP), the United Nations Children's Fund (UNICEF), the World Bank and the Asian Development Bank (ADB), as well as a small group of bilateral donors and Western non-governmental organizations (NGOs), the government has.

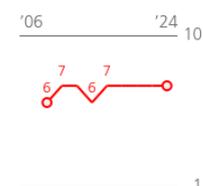
Implementation

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Policy learning

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Government officials have been able to consult with international experts who have provided policy advice, program design assistance, and guidance on good practices. Government officials travel overseas to enhance their knowledge and understanding of specific issues and practices. A significant number of students, relative to the country's population, have been going abroad for training and education. They pursue a wide range of activities, including vocational skills, a large number of postgraduate coursework degrees, and, more recently, higher research degrees. The University of Canberra in Australia has been offering master's-level programs in public administration and business administration in Thimphu in collaboration with the Royal Institute of Management. The government continually seeks innovative policies. For example, the 10-year Bhutan Education Blueprint (2014 – 2024) aims to improve access, quality, equity, and efficiency in the education system. The 12th five-year plan (2018 – 2023) aims to enhance coordination between government organizations, with goals rooted in the government's experience from the previous plan's implementation. In response to COVID-19, Bhutan quickly adapted education and some government services to remote delivery methods.

15 | Resource Efficiency

Bhutan's public administration system has traditionally been bureaucratic, prioritizing hierarchy, seniority, and process. To enhance the performance of its bureaucracy, the government has undertaken public management reforms. In 2022, the Royal Civil Service Commission restructured the civil service agencies into four clusters, with each cluster handling governance, economic, social, and security issues, aiming to boost efficiency and service delivery. As of December 2021, Bhutan was reported to have 26,322 regular civil servants, resulting in a civil servant-to-population ratio of 1:24.

The civil service is governed by the Civil Service Act of 2010, which specifies the details of all human resource management activities, including recruitment, duties, remuneration, promotion, and discipline. The act is administered through the more detailed Bhutan Civil Services Rules and Regulations and concentrates human resource management authority in the Royal Civil Service Commission (RCSC). The RCSC administers human resource tasks and runs the entry exams for all civil service organizations. Entry is only open to university-level graduates through nationwide exams. There have been growing calls for improving the efficiency and transparency of the civil service, since underperformance, low motivation, alcoholism, and corruption are major issues prevailing in the country's public sector. In March 2022, over 40 senior executives were ordered to vacate their positions for failing the leadership assessment test given by the RCSC.

Efficient use of assets

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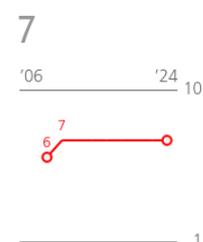


Development assistance in the form of grants has played a significant role in the budget, accounting for an average of 13.5% of GDP between 2003 and 2012. Such funding will be harder to come by when Bhutan graduates from the list of least-developed countries to a middle-income country in 2023. Bhutan relies on India for considerable budgetary support. In 2017/18, it received 48% of India's foreign aid budget, compared to an even higher share of 63% in 2015/16. According to the IMF, Bhutan has maintained “comfortable” levels of reserves in recent years, which are adequate for debt repayments, but may need to change some practices to meet future challenges. Lastly, Bhutan received foreign assistance from South Asia and other countries to meet its COVID-19-related needs.

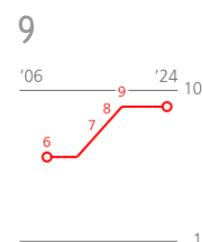
The civil service is governed by the Civil Service Act of 2010, which sets out details for all human resource management activities, including recruitment, duties, remuneration, promotion, and discipline. The relatively small scale of government, the preference for consensual decision-making, and the guiding frameworks of five-year plans have led to a good degree of policy coherence. The Commission for Gross National Happiness, which used to play a major role in coordinating and managing such coherence, was abolished in 2022. Government organizations work according to clearly delineated functional responsibilities that may sometimes hamper more whole-of-government approaches. There is administrative decentralization in the country's 20 districts (dzongkhags). Civil service officials are posted by central government agencies to work in dzongkhag administrations with locally elected officials to produce plans at the dzongkhag and local (gewog) levels. These individual plans then feed into the overall national plans of action. Despite this decentralization, there is still a strong centralized character to government decision-making in Bhutan, and hierarchy remains a major organizational principle.

The government of Bhutan has a good record of containing corruption, which can be explained by six factors. First, smaller governments, such as that of Bhutan, are easier to monitor and audit. Second, there has been a concerted effort by the government over several years to raise the standards of accounting and auditing to international levels. Third, the Accounting and Auditing Standards Board of Bhutan was introduced in 2010 to assist in raising Bhutanese standards in these activities. Fourth, the idea of service to the state and king is ingrained in the civil service and incentivizes the prevention of corruption. Fifth, the ACC, established in 2006, has been a notable force in promoting the anti-corruption message, as well as in investigating and prosecuting corrupt officials. In his National Day address in March 2022, the King of Bhutan noted that corruption was on the rise and called for making accountability a cornerstone of governance. From 2006 to June 2022, the ACC and the Office of the Attorney General (OAG) managed to recover BTN 202M of the much larger amount that the defendants were ordered by the courts to pay back.

Policy coordination



Anti-corruption policy



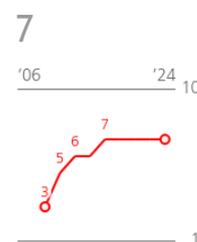
The Royal Audit Authority (RAA) has been a leading force for financial accountability, reporting to the Public Accounts Committee of the National Assembly. Moreover, there is widespread concern among citizens about corruption, which has led to a low tolerance for activities viewed as corrupt. In 2017, the Office of the Attorney General (OAG) received 1,348 applications for cases to be prosecuted, the highest number to date. Out of that number, 1,318 were forwarded by the Royal Bhutan Police, 23 by the ACC, and seven by the Royal University of Bhutan, the Ministry of Agriculture, and the Ministry of Works and Human Settlement. Unfortunately, financial irregularities in public expenditures continue to be a major problem. As of March 2018, the RAA reported unresolved irregularities involving BTN 407 million. In 2020, the Public Accounts Committee discovered BTN 4.3 billion worth of spending pending audit issues. According to the RAA, most of these financial irregularities occurred in major hydroelectricity projects since hydroelectricity is Bhutan's top GDP generator. To combat corruption, the National Assembly made several recommendations in 2018 to review and amend the Anti-Corruption Act of 2011. These recommendations aimed to establish an unambiguous distinction and definition for various types of corruption.

In January 2020, the RAA established new regulations after the parliament passed various resolutions to strengthen the system of accountability in a joint session. In September 2020, the OAG created a Governance and Corporate Legal Service Unit composed of experts in corporate and financial law. The purpose was to reform the existing government procurement and contracting system, and to review the dispute resolution process for commercial disputes. The ACC and the OAG have clashed over their respective roles and responsibilities. For example, the ACC appealed a High Court judgment in a tax evasion case directly to the Supreme Court after the OAG refused the appeal. The ACC also directly prosecuted and won the Trongsa land fraud case after the OAG had dropped it.

16 | Consensus-Building

There is broad agreement among political elites and the bureaucracy on the overarching policy directives set in the country's Gross National Happiness Plan. Accordingly, the third national election in 2018 marked the further consolidation of democracy. Unlike in 2013, when voter turnouts were lower than in previous elections, the turnout in the subsequent 2018 elections was higher for both the National Council and National Assembly. Furthermore, the rural population actively participates in local governments. The ruling DNT party has continuously called on the opposition to collaborate, which was then countered by oppositional demands to be compensated with cabinet positions. This is symptomatic of divergences in opinion that have surfaced between the ruling and opposition parties, as well as between the National Assembly and National Council. This can be seen as an indicator of a maturing and consolidating democracy.

Consensus on goals



Bhutan's economy is still dominated by SOEs. Restrictions on entrepreneurship, such as limited credit access, cumbersome permit acquisition, and high costs for trading across borders, impede the establishment of a market economy. The overall commitment to the philosophy of GNH also restricts governments from fully promoting a market economy. The population generally lacks in-depth knowledge about the complexities of a market economy, and most enterprises are small and simplistic. The financial sustainability of private enterprises, particularly those in the tourism sector, has been further undermined by the COVID-19 pandemic.

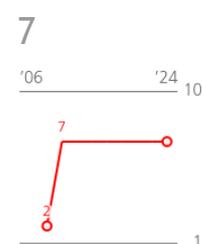
Democratization is widely supported by all relevant actors in society. The monarch's firm support for democratic rule – and high levels of deference to the monarchy among political parties and the public – ensure stability. The monarchy is the only potential domestic veto player in Bhutan, but the king has remained resolute in his support of democratic political arrangements. However, India could potentially act as an external veto player, interfering in Bhutanese politics if it deems the intervention to be beneficial. The main vocal opposition to the government can be found among exiled populations of Nepali descent, but to date, such opposition groups have had no impact on politics inside Bhutan.

Bhutan endured a significant challenge to government authority in the early 1990s, originating from the Lhotshampa population in the southern region of the country. As a result, up to 100,000 members of this group were either expelled or sought refuge in camps located in Nepal. The majority of these individuals have since been resettled in various third countries, with a notable number finding a new home in the United States. During the 1990s, militant groups from India's state of Assam sought refuge in Bhutan, but they were forcefully expelled through a joint operation involving Bhutan's security forces and the Indian army in 2003. Subsequently, there have been incidents of attacks on Bhutanese vehicles in Assam (including those in Bodoland), as well as occasional kidnappings by Indian criminals in Bhutan's southern border regions. However, other ethnic groups within Bhutan pose no conflicts.

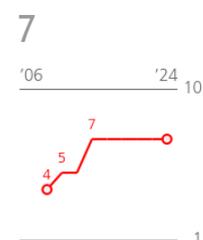
Potential conflict within society is largely mediated through consensus-building mechanisms. Consensus is also the cornerstone of National Happiness Index (NHI) policies. The NHI serves as the overarching framework to which political parties are required to adhere. Bhutan's courts are also increasingly involved in resolving potential conflicts.

Traditional civil society in Bhutan was community-based and focused on local matters such as water rights, human security, and festivities. The introduction of modern civil society in the form of NGOs and professional associations is relatively new in Bhutan. According to the constitution, the state will make efforts to establish a civil society. The Civil Society Organizations Act of 2007 differentiates between public and mutual benefit organizations, as well as foreign CSOs. However, despite their significance at the local level, there is no mention of traditional organizations. Currently, there are few CSOs, but their numbers have increased from 10 public benefit organizations in 2010 to 35 in 2018. In addition, nine mutual benefit

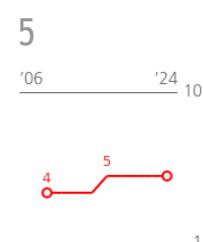
Anti-democratic actors



Cleavage / conflict management

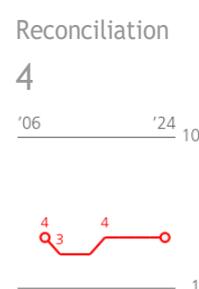


Public consultation



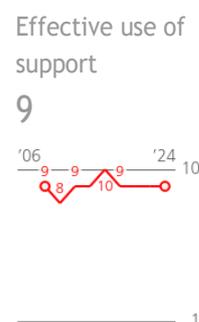
organizations were registered in 2017. CSOs may be consulted by the government in their specific areas of expertise, such as women’s affairs, youth, and the environment. They can also function as professional associations, providing guidance in certain policy areas. Nonetheless, despite the aforementioned positive trends, their influence on policies may be more reliant on their support and participation rather than their organizational capacity. NGOs are prohibited from engaging directly in political activities, necessitating a deliberate approach to pursuing their agendas. Many areas of policymaking lack the presence of NGOs, and trade unions do not exist in the country. Consequently, the overall impact of civil society on the policy process is very limited and selective.

Since the departure of an estimated 100,000 Lhotshampa people from the south of the country in the early 1990s, various organizations, often based in refugee camps in Nepal, have strongly criticized the Bhutan government, occasionally backed by international human rights organizations. Despite a series of meetings between the governments of Bhutan and Nepal, no agreement has been reached regarding the return of these refugees to Bhutan. Instead, Western countries, particularly the United States, have permanently taken in about 90,000 people from the refugee camps. There is no process of reconciliation, but – with the resettlement of most refugees – the significance of this issue has dwindled. There are no relevant contentious groups.



17 | International Cooperation

GNH provides the cornerstone for Bhutan’s development strategy. The 12th five-year plan, active at the time of speaking, seeks to strengthen the role of local bodies in development through the decentralization of roles and resources. The government is strongly dependent on international support and seeks to align international assistance with targets set under the country’s five-year plans. India remains the major supplier of financial and other support to Bhutan. Additionally, it is the largest recipient of India’s foreign aid budget, receiving 48% of it in 2018/19 and 57% in 2017/18. India also assists Bhutan’s five-year plans. As such, it provided INR 45 billion for Bhutan’s 11th five-year plan – about 68% of the total external assistance received. Furthermore, India has provided financial assistance for Bhutan’s hydropower construction. Other aid suppliers include major international financial institutions like the World Bank and the ADB, as well as some U.N. agencies, including UNDP and UNICEF. In addition to India, bilateral donors including Japan, Norway, Denmark, Austria, Australia, and Switzerland have undertaken small programs in Bhutan. Most of these programs provide aid in the form of grants.



Aid is effectively channeled into activities specified in the five-year plans and contributes to the achievement of the Sustainable Development Goals (SDGs). Bhutan’s transition from a least-developed to a middle-income country has been postponed from 2021 to 2023. This delay was requested by Bhutan’s government due

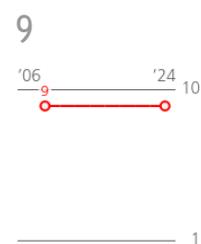
to potential challenges posed by the less favorable terms and conditions for international financial assistance that accompany the transition. To assist with the COVID-19 pandemic, Bhutan received aid from various international sources, including the United Nations, the United States, Singapore, the Asian Development Bank (ADB) and members of the South Asian Association for Regional Cooperation (SAARC).

Bhutan is considered a reliable partner by the donor community. In 2012, the ADB rated Bhutan as the best-performing country in terms of efficient project implementation and effective fund utilization, providing evidence of this perception. Additionally, the World Bank described Bhutan as a “development success” in 2014, reflecting positive outcomes from its World Bank-funded programs. The country has garnered significant international interest and has a commendable reputation for its unique alternative development philosophy of GNH. As of July 2022, Bhutan has diplomatic relations with 54 countries and the European Union. Bhutan signed the Paris Agreement in 2016 and has remained fully compliant, achieving net-zero status. In a revised version of its Nationally Determined Contribution (NDC) in 2021, the country committed to maintaining carbon neutrality. However, Bhutan faced a significant challenge as the International Civil Aviation Organization (ICAO), following its validation mission in August 2018, raised concerns about the country’s lack of effective implementation of relevant ICAO standards. According to ICAO regulations, countries are required to have independent control over air traffic, but Bhutan’s air traffic at the Paro International Airport is currently managed by the Indian Air Force. Furthermore, Bhutan is not a member of the International Labour Organization (ILO). Despite ongoing discussions for a decade, Bhutan’s labor minister publicly stated in 2020 that the country does not have immediate intentions to join the ILO.

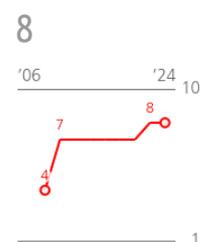
Bhutan has consistently expanded its relations with other South Asian countries. In November 2022, Bhutan signed a memorandum of understanding with ICIMOD, which includes Afghanistan, China, Pakistan, and Tajikistan, to share best practices in climate-resilient approaches aimed at addressing the challenges posed by climate change, biodiversity loss, and pollution. This development is significant due to the existence of 567 glacial lakes in Bhutan, out of which 17 have been recognized as potentially hazardous lakes capable of triggering glacial lake outburst floods.

In 1985, Bhutan became a founding member of the SAARC and has actively participated in its affairs ever since. Alongside other SAARC members, Bhutan ratified the South Asian Preferential Trade Arrangement (SAPTA) in 1993. Bhutan has hosted numerous SAARC conferences and events and held the organization’s chairmanship in 2011. The SAARC Development Fund and the SAARC Forestry Center are both headquartered in Thimphu. Bhutan entered into the South Asian Free Trade Agreement (SAFTA) in 2004, aiming for zero customs duties among members by 2016, though Bhutan was initially granted an additional three years. In order to

Credibility



Regional cooperation



stabilize the regional situation, the government has signed agreements with its neighboring partners on narcotics, terrorism, and human trafficking. Furthermore, Bhutan has joined the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC), alongside India, Nepal, Bangladesh, Sri Lanka, Myanmar and Thailand.

Strategic Outlook

Bhutan's democratic progress is evident through notable advancements in interparty competition, accountability, and the rule of law. As the nation approaches its fourth election in 2023, its political system will need to efficiently address pressing existential concerns such as clean drinking water, health care access, waste management, and employment opportunities. A critical facet of Bhutan's democracy lies in enhancing women's representation at the national level to overcome the prevailing male dominance. The local government elections in November 2022 displayed a heightened voter turnout, reflecting the electorate's eagerness to exercise their voting rights – an encouraging sign for the nation's democratic landscape. The upcoming 2023 national elections will further gauge the extent of voter participation. To secure greater public trust, Bhutan's political parties should emphasize collaboration, pivoting away from adversarial preoccupations.

In his 2022 national day address, the King of Bhutan emphasized the imperative to combat corruption as a foremost national priority. Corruption severely erodes people's confidence in the government and can significantly undermine democratic institutions. Bhutan's Anti-Corruption Commission (ACC), along with the Office of the Attorney General and the Courts, have been instrumental in investigating and prosecuting corruption cases. However, the increasing instances of corruption cast a shadow over these endeavors. Notably, the conviction of a senior justice of Bhutan's Supreme Court in a corruption and conspiracy case, as well as the 2021 conviction and resignation of the home minister on insurance fraud charges, underscore the government's commitment to curbing corruption.

To diversify its economy and enhance employment prospects, Bhutan must expedite efforts to reduce its excessive reliance on hydropower exports. The adverse impact of COVID-19 exacerbated the struggles of an already fragile private sector, particularly within the tourism industry. Rejuvenating the private sector will necessitate substantial support, a challenge compounded by limited government financial resources. Resolving the deadlock between the National Council and National Assembly regarding the Mines and Minerals Bill – largely concerning the allocation of mines and minerals to the private sector – is essential. Opening up certain mines and mineral sectors to private sector participation could prove pivotal for private sector growth and fostering optimism.

Bhutan has continued to expand its international relations while preserving its traditional ties with India and other South Asian countries. While India's role remains pivotal for Bhutan's economic and border security, the nation will continue to collaborate and receive assistance from a diverse range of international stakeholders. Developed nations and international financial institutions, in particular, have a vested interest in sustaining a growth strategy that ensures Bhutan's economic resilience as a middle-income country.