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# Bhutan Country Assistance Evaluation

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## Abbreviations and Acronyms

AAA	Analytical and Advisory Activities
ADB	Asian Development Bank
AIDS	Acquired Immune Deficiency Syndrome
BCCI	Bhutan Chamber of Commerce and Industry
CAE	Country Assistance Evaluation
CAS	Country Assistance Strategy
CEM	Country Economic Memorandum
CPIA	Country Policy and Institutional Assessment
DFS	Department of Forestry Services
EDP	Educational Development Project
EEC	European Economic Commission
EFC	Environmentally-Friendly Construction
ESW	Economic and Sector Work
FDC	Forestry Development Corporation
GDP	Gross domestic product
GEF	Global Environmental Facility
GNH	Gross National Happiness
HIV	Human immunodeficiency virus
IDA	International Development Association
IDI	Institutional Development Impact
IMF	International Monetary Fund
IMF	International Monetary Fund
OED	Operations Evaluation Department
PMR	Project Management Report
PPP	Purchasing Power Parity
QAG	Quality Assurance Group
RGOB	Royal Government of Bhutan
SDC	Swiss Development Corporation
TFDP	Third Forestry Development Project
TM	Task Manager
UN	United Nations
UNDP	United Nations Development Program
WBI	World Bank Institute
WDI	World Development Indicators

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## **Preface**

This evaluation provides an independent assessment of the role of World Bank assistance to Bhutan during the period 1993–2003. The Country Assistance Evaluation (CAE) examines whether: (a) the objectives of Bank/IDA assistance were relevant; (b) the Bank's assistance program was effectively designed and consistent with its objectives; and (c) the Bank's program achieved its objectives and had a substantial impact on the country's development during this period. Examining these questions allows the CAE to draw lessons and recommendations for future Bank assistance. Annex D describes the methodological approach.

The basis for the CAE consists of OED project assessments, sectoral reviews, and interviews with Government officials, Bhutanese civil society, other donors, and Bank staff. A list of those interviewed is shown in Annex C. An OED mission visited Bhutan during May 2003.

The Regional Management of the Bank provided comments which are found in Annex E. The report was also sent to the Bhutanese authorities whose comments are in Annex F. OED has taken account of factual and editorial comments in this draft.

This Country Assistance Evaluation was written by Gene Tidrick (Consultant) with the assistance of Daniel Ritchie (Consultant). Tatsuhide Kanenari (Consultant) provided support on the education sector as well as overall research assistance. This evaluation also benefited from comments of three peer reviewers: Mr. Sudhir Shetty (PRMPR); Mr. Asita De Silva (OEDCR); and Mr. Ronald Parker (OEDST). Danuta Danilova provided additional research assistance. Betty Casely-Hayford and Janice Joshi provided administrative and editorial support.



## Summary

1. Bhutan has a well-deserved reputation for good economic management and environmental stewardship. The national development strategy of maximizing “Gross National Happiness” seeks to balance the pursuit of conventional GDP growth with preservation of the country’s cultural and environmental heritage. It has broadly succeeded on both fronts. Helped by exports of hydropower and substantial foreign aid, output per capita has grown at an annual average rate of 4 percent over the past two decades, social indicators have improved significantly, and yet Bhutan has avoided many of the problems of social dislocation and environmental degradation of other countries. Nevertheless, Bhutan is still a poor country with tremendous geographical barriers to development; its environment remains fragile and subject to pressure from a growing population; employment is growing too slowly to absorb the increasing number of secondary school graduates; and there is a still only partly-resolved dispute over citizenship claims of refugees of Nepalese origin.
2. IDA is a small player in this heavily-aided country, ranking as the 8<sup>th</sup> largest donor and providing less than 2 percent of Bhutan’s foreign assistance during the 1990s. The Bank’s assistance strategy has recognized IDA’s limited role and has given priority to analytical and advisory activities (AAA) while engaging in selective lending for education, forestry, and (more recently) infrastructure. Bank strategy shifted in the late 1990s, however, as the Bank actively sought opportunities for engagement and government willingness to borrow increased. Two new projects in infrastructure (urban development and rural access roads) were approved, and the Bank expressed a willingness to provide economy-wide program lending. At the same time, the Bank stated that its comparative advantage was in transferring knowledge and ideas rather than finance, and it proposed a large program of AAA.
3. The shift in strategy articulated in the 2000 CAS has not been implemented. In the event the government was not prepared for program lending and Bank involvement in many of the proposed studies did not materialize, primarily because alternative support from Asian Development Bank (ADB) was available and because multiple donor involvement is burdensome. More generally, the government is wary of taking on too many studies which, even if free, have a high opportunity cost in terms of scarce senior official involvement. The Bank has provided some useful analytical work and policy advice over the years, however. The last Country Economic Memorandum was in 1996, but in the last five years, the Bank carried out (in collaboration with the government and other donors) a *Private Sector Survey*, a country financial accountability assessment, an informal analysis of the macroeconomic impact of the hydropower boom, and informal sector work related to Bank projects. No formal sector work has been done.

4. Bank lending in Bhutan has been a basic program of infrastructure development—roads, schools, water supply and sanitation and forest management—reflective and respectful of the needs of a traditional society still in the early stages of its development process. Each project has included basic capacity building, usually funded by bilateral partners with grant assistance, while the focus of the Bank’s investment has been on building basic physical infrastructure. The lending program has been client-driven, carried out in partnership with bilateral agencies and reflective of the country’s holistic approach to development (including its cultural and traditional values). In a sense, it has been a model of the comprehensive development framework long before it found its way into the Bank lexicon.

5. The Bank lending program has been largely effective. Five of six completed projects (six of seven counting a Bank-executed Global Environmental Facility project) had a satisfactory outcome. One of the strengths of the lending program has been the use of co-financing for technical assistance and other “soft” activities to complement the Bank’s funding for construction and other “hard” components. There have been weaknesses as well: insufficient sector work to underpin sector strategy; inadequate preparation of two infrastructure projects; weaknesses in supervision; lack of staff continuity; and occasional insensitivity to the special requirements of a small country.

6. The Bank has made an important contribution to improving access and quality of education in Bhutan. In forestry, the outcome of its assistance has been mixed, with the most recent forestry project rated moderately unsatisfactory. The overall outcome of Bank assistance to Bhutan is rated moderately satisfactory. Sustainability is rated likely and institutional development impact is rated substantial.

7. Some of the lessons arising from the evaluation of Bank assistance to Bhutan may be relevant in other small countries, or in other situations in which the Bank plays an unaccustomed small role. The Bank was effective in Bhutan when it listened to what the government wanted rather than trying to figure out what the government needed and then trying to persuade the government to accept its proposals. Proposals for the Bank to serve primarily as a knowledge bank have not been successful as most of the Bank offers of knowledge services were not taken up by the government. Other lessons include: co-financing is an especially useful instrument in a small country; staffing continuity is critical for effectiveness; and, above all, it is essential to remain selective and focused. It is a mistake to try to be a “full service bank” in a small country unless the Bank is the dominant lender. Nor is it easy to be a knowledge bank in a small country. The Bank needs to invest resources in order to provide useful advice based on local conditions and to inform a selective lending program, while the government is constrained by the limited time of senior officials to work with the Bank

8. The main recommendation is that the Bank should return to the more selective approach of its earlier assistance strategy, but make it more effective through prior sector work. The Bank also needs to develop ways to compensate for its lack of field presence. It could usefully follow the example of the ADB in having annual rolling program consultations and making better use of United Nations Development Program (UNDP) facilities to improve coordination with other donors based in Bhutan. Finally, the Bank should increase its sensitivity to the constraints of a small country by reviewing its procedures on procurement, reporting, and core economic studies.

Gregory K. Ingram  
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# 1. Background

## Country Characteristics

1.1 Bhutan is a small, isolated Buddhist kingdom with a distinctive development strategy. Because of its strategy, its location, and its development constraints, Bhutan has attracted considerable outside interest and support.

1.2 *Isolation.* Bhutan is isolated by geography and, historically, by policy. Located in the Eastern Himalayas between India and the Tibet region of China, Bhutan has an estimated population of about 750,000<sup>1</sup> within an area about the size of – but more rugged than – Switzerland. Within fewer than 100 km the altitude varies from less than 200 meters in the South to over 7,000 meters in the North. More than half the population lives at least half a day's trek from the nearest road. Historically, Bhutanese policy has reinforced the isolation imposed by geography in an effort to preserve political and cultural independence. Until 1959 Bhutan remained inaccessible by road, and access by road and air remains limited, unreliable, and costly.

1.3 *Dependence on India and hydro power exports.* Bhutan's budget, trade, and production are heavily dependent on the much larger Indian economy (900 times as large as Bhutan's). Although smaller than in earlier years, Indian grant aid still covers nearly one quarter of Bhutan's government expenditure and about 10 percent of GDP.<sup>2</sup> Bhutan's trade is integrated with the Indian economy by transport links (India built the first road into Bhutan and still directly maintains 30 percent of Bhutan's main road network) and institutional arrangements (a free trade agreement and currency links).<sup>3</sup> India accounts for 95 percent of Bhutan's exports and 78 percent of imports (three-year average). Finally, Bhutan has become increasingly dependent on the power sector. In recent years power has contributed about 11 percent of GDP, 40 percent of export earnings, and 40 percent of government revenue. The power sector, in turn, is also dependent on India. India has funded several major hydro power projects through a combination of grants and soft loans, and electricity exports go exclusively to India.

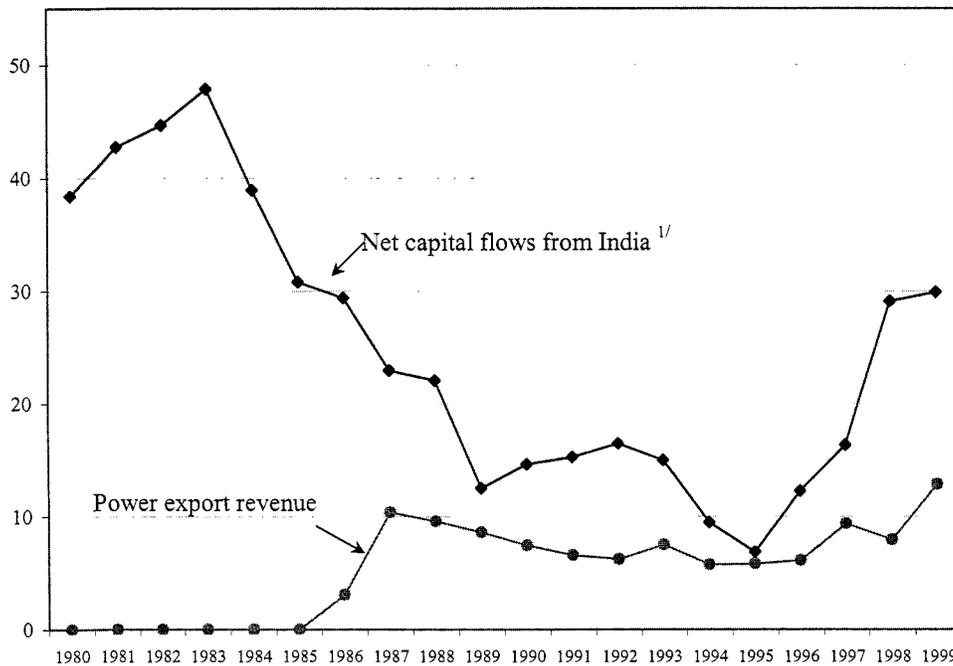
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<sup>1</sup> There is a wide range of population estimates. For 1998 the government estimated total population at 636,500 while the United Nations (UN) estimate was 1,948,000. The World Bank estimate for the same year was 759,150. The United Nations (UN) continues to project population from the higher estimate used by the government at entry to the UN in 1971.

<sup>2</sup> After Indian independence, India took over British budget support to Bhutan (arising from a war in the 19<sup>th</sup> century in which Bhutan was defeated by the British and ceded lowland territory to colonial India). The first two five-year plans in the 1960s were entirely financed by India.

<sup>3</sup> Although Bhutan has traditional cultural and trade ties with the Tibet region of China, the border is officially closed to trade and the potential is limited in any case by the absence of roads and difficult terrain.

**Figure 1.1: Bhutan - Net Capital Inflows from India and Power Export Revenues**  
(as percentage of GDP)



Source: RMA Annual Reports (various issues).

1/ Consists of concessional loans and grants.

1.4 *Bhutan's development strategy.* Bhutan's approach to development is often defined as maximizing Gross National Happiness (GNA).<sup>4</sup> The concept of GNH, introduced by the King in 1980, implies an attempt to balance material progress with environmental sustainability and preservation of Bhutan's national independence and religious and cultural heritage. The country's leadership wishes to preserve Bhutan's traditional way of life as much as possible and avoid the mistakes of other countries, particularly deforestation and uncontrolled urbanization. In line with these objectives, Bhutan has vowed to maintain forest cover for at least 60 percent of its area, not only for preservation of its own environment but in "trust for mankind". Similarly, Bhutan's guarded approach to opening up to outside cultural and economic forces is reflected in its restrictions on direct foreign investment, exports of logs, and mass tourism. Nevertheless, Bhutan has gradually opened up the country and the economy in the past two decades and has enjoyed a high rate of growth of Gross Domestic Product (GDP), the common international measure of material output.

1.5 *Political and social issues.* Bhutan is in the process of drafting a written constitution to establish parliamentary democracy. The country enjoys a reputation for good government, including low corruption and efficient administration. Land reform in the 1960s abolished serfdom and created a relatively equal distribution of arable land.

<sup>4</sup> See, for example, Royal Government of Bhutan (RGOB) Planning Commission, *Bhutan 2020: A Vision for Peace, Prosperity and Happiness* (1999), and Centre for Bhutan Studies, *Gross National Happiness* (1999).

Women have equal status in law and by tradition, because of matrilineal land inheritance among the largest ethnic group. But there are also tensions arising from an exodus in the early 1990s of people of Nepalese origin from Bhutan, many of whom ended up in refugee camps in Nepal. An agreement reached in 2003 provides for a settlement, but it still remains to be implemented.<sup>5</sup> In addition, revolutionaries seeking to gain independence for Assam from India operated for some years from bases in southeastern Bhutan. The Bhutanese army expelled the rebel groups from camps in its territory in December 2003.

## Overview of Economic and Social Development

1.6 *Growth and macro management.* Bhutan has had sustained high growth of GDP averaging 6.6 percent per annum (4.0 percent per capita) over the past 20 years (Table 1.1). Growth has been driven by power sector development and supported by a high level of external assistance. Revenue from hydro power averaged over 10 percent of GDP during the 1990s. Aid averaged about 40 percent of GDP during the 1980s and 27.5 percent during the 1990s.<sup>6</sup> Unlike some countries with large natural resource exports and foreign aid inflows, Bhutan has skillfully managed its foreign exchange and government revenue bonanza in three important respects. First, it has maintained a high rate of investment, averaging well over 40 percent in the 1990s. Second, a large share of public expenditure has been directed toward education, rural development, and other activities which help share the benefits of power and aid resources widely. Third, macro management has been prudent. Domestic borrowing has been low during most of the past two decades, inflation has remained in single digits except during the early 1990s, and Bhutan has steadily accumulated rupee and convertible foreign exchange reserves.<sup>7</sup>

1.7 High investment rates and spending for social development have helped counter the tendency for the power sector to become an enclave. Although the power sector was one of the largest contributors to growth, other sectors have contributed more and all sectors have grown (see Figure 1.2). Reflecting the government's success in promoting broadbased growth and good macro management, the Bank's internal Country Policy and Institutional Assessment (CPIA) ratings have placed Bhutan in the upper quintile of IDA countries in most years.<sup>8</sup>

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<sup>5</sup> Around 100,000 people have been living in refugee camps jointly run by UNHCR and the government of Nepal. The RGOB maintains that many of those in refugee camps were recent illegal immigrants or may never have lived in Bhutan at all. See the Government's comments in Annex F.

<sup>6</sup> These figures are based on RGOB data. WDI data show lower, though still substantial, shares of aid (14.3 percent of GDP during the 1980s and 22.5 percent during the 1990s). The discrepancy arises because the WDI figures exclude Indian aid.

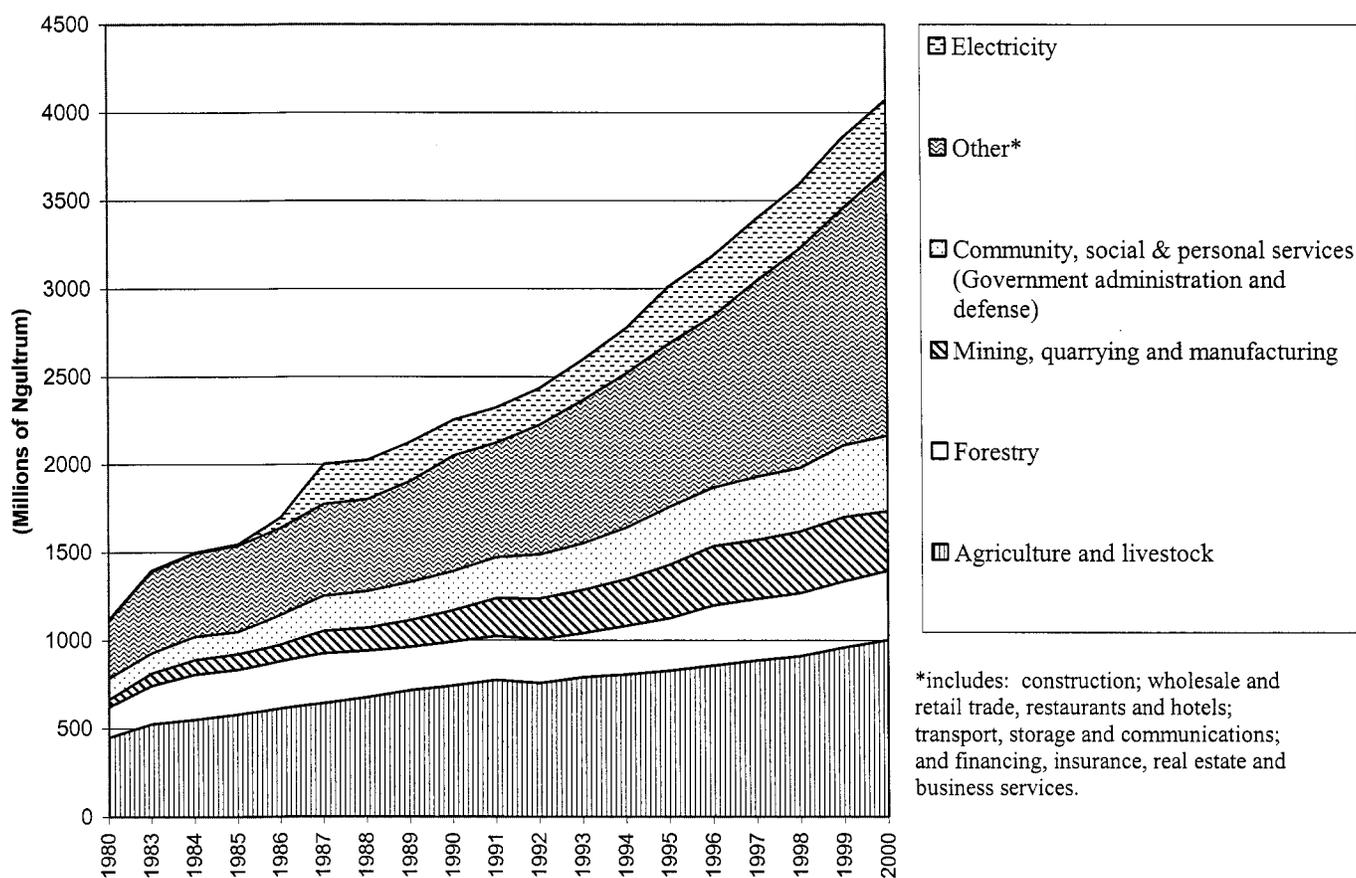
<sup>7</sup> The overall budget deficit including grants rose to 11 percent of GDP during 2001 because of lumpy capital expenditures and delays in foreign aid receipts, but the deficit fell again in 2002 and 2003.

<sup>8</sup> Ratings were recalibrated in the last round to reflect that, while outcomes in some areas such as quality of budgetary and financial management were high, institutional development lagged. Despite this recalibration, Bhutan's rating remained in the top quintile.

**Table 1.1: Bhutan - Selected Macroeconomic Indicators**

Indicator	Unit	Period Averages				
		1981-85	1986-90	1991-95	1996-00	2001-02*
GDP per capita	constant 1995 US\$	272.4	358.4	411.9	492.9	566.9
GDP per capita growth	annual %	4.7	6.0	2.7	3.8	4.4
Exports of goods and services	current million US\$	24.9	71.3	85.9	126.8	122.2*
Exports of goods and services	% of GDP	14.4	26.4	32.8	31.0	23.2*
Power exports	% of GDP	0.0	7.8	6.4	9.1	
Imports of goods and services	% of GDP	45.3	44.9	44.8	45.6	43.4*
Aid (WDI definition)	% of GDP	10.8	17.7	28.0	17.0	12.6*
Total Net Capital Inflow	% of GDP	52.0	30.3	24.7	31.5	
Gross domestic savings	% of GDP	9.4	16.2	36.1	26.5	27.9*
Gross capital formation	% of GDP	40.3	34.7	48.1	41.1	48.1*
Overall budget balance, including grants	% of GDP	-1.9	-5.3	-0.2	3.8	-10.0*
Current revenue, excluding grants	% of GDP	10.6	19.6	22.7	22.7	
Current revenue, including current grants	% of GDP	36.0	39.8	42.4	39.7	
Inflation, consumer prices	annual %	9.4	9.0	11.2	8.2	2.8

\* 2001 data only.

**Figure 1.2: Composition of GDP at Factor Cost in 1980 Prices, by Sector**

1.8 Despite overall good management and performance, Bhutan still faces a number of challenges. Foremost among these is the challenge of providing jobs for a growing labor force. Neither the power sector nor associated power-intensive industries provide many jobs. The government sector has also ceased to expand employment just as large numbers of secondary school graduates with high expectations are coming into the labor market. A second, related challenge is to create a policy environment for private sector development. Non-power exports have declined in recent years. This appears to have more to do with restrictions on exports of unprocessed timber than with exchange rate overvaluation (“Dutch disease”), but it is a concern nonetheless. Finally, grant aid is likely to decline in future. Although this is a problem arising from Bhutan’s success, the projected decline poses a challenge for debt and public expenditure management.

1.9 *Social development and poverty reduction.* Bhutan’s social indicators have improved significantly over the past 20-25 years (see Table 1.2). Between 1977 and 2000 life expectancy rose by 43 percent, child mortality was nearly cut in half, and the adult literacy rate tripled. Improvements reflected both economic growth and government programs in health, education, and road-building to improve access to economic opportunities and social services. The advances are all the more notable because of the scattered population and difficult terrain. For example, for most children in rural areas secondary schooling requires boarding. The government provides free room and board as well as free tuition at all levels.<sup>9</sup> Basic health services are free and are provided by 454 outreach clinics (in 2000) as well as 160 basic health units and 28 hospitals. The biggest increases in social indicators came in the earlier years, but indicators have continued to improve and the government has stated that it hopes to meet most Millennium Development Goals ahead of time (before 2015).

**Table 1.2: Bhutan Social Indicators**

	1977	1990	1994	2000
Life expectancy at birth (years)	46.1		66.1	66.1
Population growth rate (%)	2.3		3.1	2.5
Total fertility rate (births/women)	n.a		5.6	4.7
Infant mortality rate	n.a	90	70.7	60.5
Under 5 mortality rate	162	123	96.9	84
Immunization coverage (%)		84		90
Access to clean water	31	45	57	77.8
Number of basic health units	31	71	71	160
Number of primary schools	92			250
Total enrollment in schools (000)	14.6	70.3	70.3	109.9
Gross primary enrollment rate		55		72
Adult literacy rate (%)	18		48	54

Source: Royal Government of Bhutan, *Bhutan 2020: A Vision for Peace, Prosperity and Happiness* and RGOB, *Bhutan 2003: People at the Center of Development*, Eighth Round Table Meeting, February 2003, Geneva.

<sup>9</sup> But as the Bhutan 2020 document cautions: “Although free basic education and health care are today reaching these pockets of disadvantaged and vulnerable groups, the need to contribute to the construction and maintenance of buildings, the cost of travel, contributions to school welfare funds, the cost of school and so forth, while modest, are sufficient to place the services beyond the reach of the poorest farmers and their families.”

1.10 Many of these estimates are subject to a wide range of error because of uncertainty over total population size (see Table 1.3). The UN's estimate of total population is three times higher than that of the government. Depending on whether indicators are based on samples or on gross numbers, differences range from relatively minor (less than 10 percent for life expectancy) to enormous (a six-fold difference for enrollment rates). Amidst these confusing estimates, two conclusions stand out. First, there is less disagreement about the trend than the level of social indicators. All sources agree that social indicators have improved significantly over time. In most cases, even the levels are not that different. For example, UNDP's 2003 Human Development Report places Bhutan among the group of countries with a medium human development index (HDI = .511) even though Bhutan is still a low-income country. Second, however, the conflicting estimates will not be cleared up until there is a population census and other improvements in data.

**Table 1.3: Bhutan-Discrepancies between UN and RGOB Estimates of Social Indicators**

<i>1997 Estimates</i>	<i>UN</i>	<i>RGOB</i>
Life expectancy a birth (years)	60.7	66.1
Adult literacy (%)	44.2	54
Combined enrollment ratio	12	72
Real GDP per capita (PPP\$)	1,467	1,534
Human Development Index	0.459	0.581

*Source:* Bhutan – National Human Development Report 2000.

Note: As noted in the report, the differences in estimates arise from the fact that RGOB uses estimates based on the most recent demographic survey whereas the UN's estimates are based on demographic projections. Related to this fact is the difference in population estimates: UN estimates the population to be 1.9 million whereas RGOB estimates it to be 0.64 million in 1998.

1.11 The level and trend of poverty are more difficult to assess. A Bank report succinctly voiced the view that has long been the conventional wisdom on poverty in Bhutan: “few Bhutanese are hungry, landless or homeless.”<sup>10</sup> But while few Bhutanese face severe deprivation, a 2001 Asian Development Bank pilot household survey found a poverty rate ranging from 25.3 percent to 36.3 percent of the population (Table 1.4).<sup>11</sup> Poverty is largely a rural phenomenon and is associated with limited cultivable land holdings, low productivity of land, and poor access to markets and economic opportunities. Poverty also differs by region, with a higher share of poor people in the far North and in the Southeast.

1.12 *Environment.* Bhutan's environmental management has effects far beyond its borders. It is a major repository of bio-diversity for the world as a whole and its seven river valleys feed the Brahmaputra system. Bhutan's watershed management thus affects

<sup>10</sup> *Bhutan: Development Planning in a Unique Environment* (World Bank, Report No. PUB7189, 01/31/89).

<sup>11</sup> The poverty lines were calculated by grossing up a food poverty line based on the cost of a basket of 32 items which would provide 2124 calories per person. The food poverty line was Nu. 458.9 per capita per month, using current prices in the capital, Thimphu. The “lower poverty line” was Nu. 612.1 per month (equivalent to about PPP \$1.10 per day) and the “upper poverty line” was Nu. 748.1 per month (PPP \$1.35 per day). See RGOB, *Millennium Development Goals Progress Report 2002*. PPP equivalents estimated using WDI 2002 data for the year 2000.

not only the sustainability of its own hydropower industry, but also helps protect downstream users in India and Bangladesh from erosion and flooding.

**Table 1.4: Bhutan - Poverty Incidence in 2000**

<i>Category</i>	<i>Sub-category</i>	<i>Units</i>	<i>2000 Note</i>
Poverty Incidence	Lower Poverty Line	(Nu612.1/month)	25.3
	Upper Poverty Line	(Nu748.1/month)	36.3
% of Poor to Total Population	Lower Poverty Line (Urban)	%	2.9
	Lower Poverty Line Rural	%	29
	Upper Poverty Line (Urban)	%	6.4
	Upper Poverty Line (Rural)	%	41.3
	Poverty Gap (% of GDP)	Lower Poverty Line	%
	Upper Poverty Line	%	11.0

*Source:* ADB Country Strategy and Program Update (2003-2005). Bhutan. July 2002. Table A1.2.

1.13 Bhutan has earned widespread recognition for its conservation efforts. Under the Bhutan Trust Fund for Environmental Conservation (see Box 3.2 in section 3 below), one-quarter of the country's area was set aside for conservation, and the government made a recent "Gift to the Earth" of another 9 percent for wildlife corridors to prevent habitat fragmentation. In the past decade forest cover has increased from 65 percent to 72 percent of the national territory, well beyond the national target of 60 percent. The emphasis placed upon conservation of the environment is illustrated by the following statement given in the Bhutanese Environmental Assessment Sectoral Guidelines, produced in 1997 by the National Environment Commission:

Over the past two decades there has been an increasing recognition by the RGOB that if forests were not to go through a process of deterioration similar to some of Bhutan's neighbors, a systematic forest management program would have to be put in place. The management program should be based on a balancing of conservation and economic development goals through long-term, sustainable, multi-purpose forest management. This has been the focus of a revised forest policy drafted in 1991. The primary focus of the new policy is to ensure conservation of the environment, and only thereafter aim at derivation of economic benefits from the forest as a rationally managed resource.

1.14 Despite its strong conservation record, Bhutan faces growing pressures on the environment. Overall population density is low, but Bhutan's rural population per unit of arable land is higher than that of India and Pakistan, and Bhutan has the highest rate of population growth in the region.<sup>12</sup> Especially in Eastern Bhutan farmers are bringing steep, marginal, non-arable land under cultivation. Urbanization is also contributing to ecological pressures. With very little land suitable for urban growth and infrastructure—even finding a suitable site for a landfill for a small town is a major challenge—urban growth is largely at the expense of forested slopes, agricultural land, or wetlands. Water erosion now affects 10 percent of agricultural land and localized water shortages have been increasing due to growing sediment loads in rivers. Bhutan also faces the unusual environmental risk of glacier lake outburst floods. The most recent of these (in 1994) killed 22 people and affected hundreds of others. A recent United

<sup>12</sup> The comparisons are based upon WDI figures, but they would still be true using the government's lower figures for population total and growth.

Nations Environmental Program (UNEP) sponsored study identified 24 glacial lakes in Bhutan (and 20 in Nepal) as potentially dangerous.

1.15 Bhutan has a good record of environmental management, but the fragility of its environment requires special vigilance and poses difficult choices for development strategy.

## 2. The Bank's Role in Bhutan

### Context: The Bank as a Small Player in a Small Country

2.1 The World Bank is a small player in a heavily aided country. During the 1990s IDA was only the 8th largest donor in Bhutan. The Bank's small role partly reflected the government's preference for using the grant aid which most bilateral donors provided. Overall, more than 90 percent of assistance to Bhutan during the 1990s was on grant terms. But IDA also disbursed less than 60 percent as much as the Asian Development Bank, the other major source of concessional loans.<sup>13</sup>

2.2 The overall level of aid to Bhutan was about \$100 per capita (give or take 12 percent)—high compared to neighboring South Asian countries but similar to other small countries (see Figure 2.1).<sup>14</sup> IDA disbursements to Bhutan during the 1990s (averaging \$1.80 per capita per annum) were lower than to comparable small low-income countries, and lower even than per capita Bank assistance to much larger low-income countries such as Bangladesh and Pakistan. However, from 2001-2003 IDA disbursements to Bhutan increased nearly four-fold to an average of \$6.80 per capita per annum. The government has expressed interest in continuing to borrow more from IDA than in the past because of uncertainty over the future level of bilateral grant aid.<sup>15</sup>

2.3 IDA has provided ten credits totaling \$95 million to Bhutan in the past twenty years, for education, forestry, industry, rural roads, urban development and technical assistance (Table 2.1). The Bank was also executing agency for a \$10 million GEF grant.<sup>16</sup> Lending has been episodic, coming in batches of closely-spaced loans (within an 18 month period): three in the early 80s, two in the late 80s, and three in the late 90s, with several years of no new lending in between. The most recent education project (Education Development Project in FY04) is expected to be followed by projects for

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<sup>13</sup> Based on Royal Monetary Authority, *Annual Report 2001/2002*, for the years 1992/93-2001/02. Other main donors were India, Denmark, Japan, Asian Development Bank (ADB), Austria, Switzerland (Helvetas and Swiss Development Corporation), Netherlands, UNDP, and EEC. On a grant element basis, IDA was the 12<sup>th</sup> largest donor. See Annex A for details.

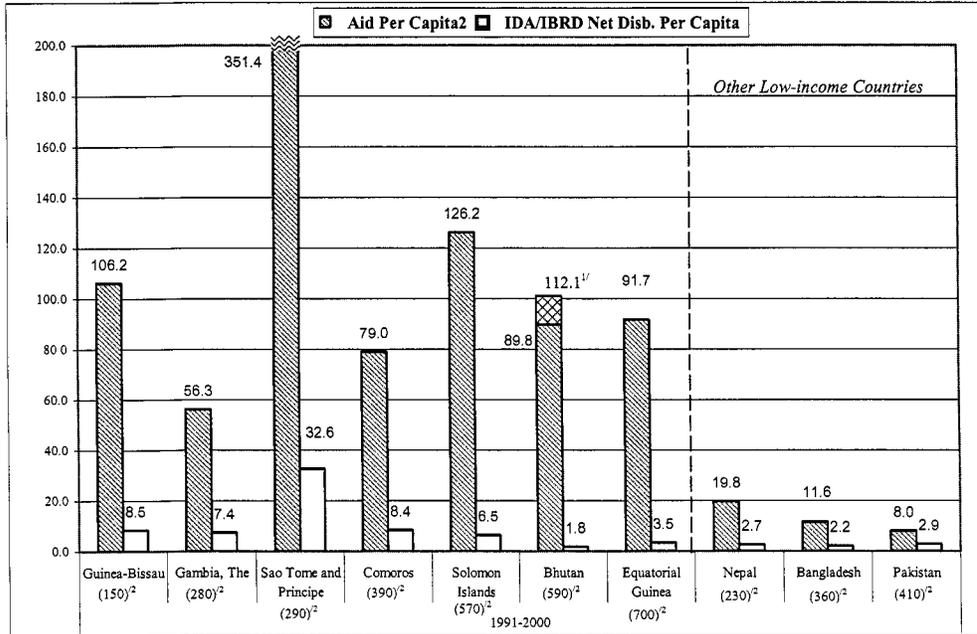
<sup>14</sup> According to WDI figures, aid per capita to Bhutan averaged \$89.8 per annum during the 1990s, but government data show an average of \$112.1 for the same period. The discrepancy arises because government figures have a more complete coverage of Indian aid.

<sup>15</sup> Denmark plans to phase out its grant aid to Bhutan because of the increasing availability of revenue from hydropower exports. Bhutan also considers the future level of Indian aid uncertain.

<sup>16</sup> IFC also approved an investment loan in December 2003 of up to \$10 million in Bhutan Resorts Corporation Limited. Bhutan became a member of IFC in 2003.

HIV/AIDS, decentralized rural development, and private sector development, plus a new GEF grant for land management.

Figure 2.1: Comparison of Bank Lending and Foreign Aid Flows to Small and Low-income



<sup>1/</sup> RGOB data. All other data are from World Bank Development Indicators. RGOB data show a higher level of aid because they have a more complete coverage of Indian aid.

<sup>2/</sup> GNIPC 2002 (Gross National Income Per Capita).

Table 2.1: Bank Group Lending to Bhutan 1983-2003

Project	Amount (\$M)	Approval Date	Status
Technical Asst.	3.0	10/18/83	Closed
Forestry I	5.5	4/17/84	Closed
Calcium Carbide	9.0	5/16/85	Closed
Primary Education	4.2	4/19/88	Closed
Forestry II	1.1	4/19/88	Closed
Third Forestry Devel. Project	5.4	7/16/93	Closed
Education II	13.7	3/3/98	Active
Urban Development	10.8	12/21/99	Active
Rural Access	11.6	12/21/99	Active
Educ. Devel. Project	31.0	8/21/03	Active
Memo: Trust Fund for Env. Cons.	10.0 (GEF grant)		Closed

## Bank Assistance Strategy

2.4 The Bank's assistance strategy for Bhutan, articulated first in 1993 and again in 2000, is aligned with the government's development goals.<sup>17</sup> Bank strategy statements have consistently stressed three themes: the Bank's limited role; priority for analytical and advisory activities; and selective lending. Practice has not always followed theory, however.

2.5 *Limited role.* The Bank has always acknowledged that it has to adapt its strategy to fit IDA's role as one of Bhutan's smallest foreign aid donors.<sup>18</sup> During most of the 1980s and 1990s this meant responding to government requests for projects rather than actively promoting lending. Because of the availability of grants, the government did not even take up the IDA allocation to which it would have been entitled on grounds of income and performance. The Bank was also content to let UNDP and ADB take the lead among multilateral institutions operating in Bhutan.<sup>19</sup> This changed in the late 1990s, however, with the change in regional management. Although Bank strategy statements still stressed IDA's limited role, the Bank actively sought opportunities for engagement, while government willingness to borrow increased. As a consequence, the IDA lending program was ramped up significantly. Two projects (Urban Development and Rural Access) were presented along with the CAS in FY00, and the third education project, the Educational Development Project (EDP), was approved by the Board in FY04.

2.6 *Priority for analytical and advisory activities (AAA).* Analytical work has always figured prominently in the Bank's assistance strategy for Bhutan. In the first decade of its relationship with Bhutan, the Bank wrote two economic reports and advised the government on sector strategies in forestry and basic education. Economic policy advice was one of three proposed priority areas in the Bank's 1993 strategy (the other two were natural resource management and primary education). Because of limited resources, the Bank proposed focusing AAA on budget analysis. The 2000 assistance strategy was even more explicit on the priority of AAA. IDA's comparative advantage was seen as transferring knowledge and ideas rather than finance. Emphasis on analytical work also made sense in terms of filling the Bank's information and knowledge gaps resulting from limited past involvement in Bhutan. The proposed program to implement the 2000 strategy included potential AAA on a vastly expanded range of topics.<sup>20</sup>

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<sup>17</sup> The 2000 CAS, prepared in 1999, stated that IDA's mission is "to help Bhutan manage its considerable natural, institutional, cultural and environmental assets in ways that can translate economic growth into rapid and inclusive social transformation and improvements in living standards."

<sup>18</sup> The 1993 country assistance strategy envisioned a limited and selected role for IDA in Bhutan's development. The 2000 CAS said that the Bank has a highly selective mission to fit IDA's continuing role as one of Bhutan's smallest donors.

<sup>19</sup> According to a former senior manager in the World Bank's South Asia Region, there was no formal understanding that ADB would be the lead multilateral lending agency, but the World Bank was happy to play a secondary role in the smaller countries of South Asia.

<sup>20</sup> The Region has commented that the proposed AAA program reflected government requests and was indicative. See footnote 1 in Annex B4 of the CAS document and the Region's comments in Annex E.

2.7 *Selective Lending.* The bulk of Bank lending has been for education, forestry, and infrastructure. The 1993 strategy limited lending to education and forestry. The strategy introduced in 2000 stressed that the Bank would continue to be selective and to be, in effect, the lender of last resort—IDA lending would be limited to sectors and activities for which grant funding was not readily available. But the scope of project lending could be expanded to cover infrastructure, e.g. the two new projects for urban development and rural access roads, as well as education and forestry. Moreover, the Bank expressed a willingness to provide economy-wide program lending, provided this was preceded by a public expenditure review, baseline poverty assessment, macroeconomic monitoring in collaboration with the IMF, and a Poverty Reduction Strategy Paper (PRSP).

2.8 *Gap between theory and practice.* There was a marked break in the Bank's assistance strategy for Bhutan in the late 1990s. The rhetoric of selectivity and the Bank's limited role remained the same as in the early 1990s, but in practice the Bank embarked on a much more ambitious program. The overall level of lending increased sharply; the proposed program of AAA expanded enormously; and the Bank moved into new areas of lending, and even raised the prospect of program lending, while at the same time saying that lending would remain a secondary activity.

2.9 The strategy articulated in 2000 has not been implemented. Although the Bank has expanded into lending for infrastructure and has other projects planned, nothing came of the proposed program lending. Moreover, the Bank's preparation of the two infrastructure projects in FY2000 was hurried.<sup>21</sup> Finally, the proposal to expand ESW and effectively act as a knowledge bank was never taken up by the government.

2.10 In some respects, the Bank's position in Bhutan is similar to its position in many middle income countries. The Borrower has alternative sources of finance and a clear sense of what it wants from the Bank.<sup>22</sup> The Bank is eager to be responsive, but risks being marginalized. One response to low demand for borrowing is to pursue a knowledge bank role. But it is difficult to construct an assistance strategy based entirely on a role as a knowledge bank in any country, and even more difficult in a low-income country such as Bhutan for several reasons. First, Bhutan lacks the capacity to interact with the Bank on a wide range of AAA (see below). Second, relevant knowledge on most issues depends on familiarity with local conditions as well as international experience. Except in sectors of active lending, the Bank lacks this knowledge in Bhutan. Third, the ADB with its larger involvement and its annual allocation of \$1.5 million of technical assistance grants to Bhutan is much better placed to provide a wide range of AAA and TA than the World Bank.

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<sup>21</sup> Some interviewees in the Bank saw this as an effort to increase the amount and scope of lending. The Region commented that the two projects were prepared rapidly to respond to the government's request. See Annex E for further details and for Regional Management's comment on program lending.

<sup>22</sup> See the Region's comments in Annex E. As in most countries, line agencies may have their own agendas. In preparation for the CAS, some agencies were asking the Bank for projects or studies which were subsequently turned down by the Ministry of Finance. The central authorities, too, sometimes change their views, but compared to most countries, the government has a clear idea of what it wants from the Bank.

2.11 The effort to increase the relevance of the Bank by expanding its role has not worked out. The government has, in effect, asked the Bank to continue its historical role of lending to selected sectors and providing AAA on a few issues. This is a realistic assistance strategy for the Bank in Bhutan and one which the Bank has performed reasonably well. The outcome of the Bank's evolving strategy is evaluated in the following two sections.

### 3. Implementation of the Bank's Program

3.1 Four areas of operational emphasis have dominated the Bank's program in Bhutan over the past decade: economic policy advice through analytical and advisory activities (AAA), and lending in education, forestry, and (more recently) infrastructure. This section will evaluate progress in implementing the Bank's strategy through AAA, lending, and cooperation with other donors.

#### Analytical and Advisory Activities (AAA)

3.2 The Bank has produced four country reports on Bhutan: in 1983, 1989, 1994, and 1996.<sup>23</sup> Since 1996 only one formal report has been produced: *Bhutan: Private Sector Survey* (published June 14, 2002). The Bank also produced a country financial accountability assessment (CFAA) in 2002 as part of its fiduciary safeguard work. There has been no formal sector work.

3.3 The economic reports provided a good overview of Bhutan's development progress and issues. The 1983 report is especially noteworthy for its highly informative *tour de force*, rich in institutional and sector detail. Several themes recurred in the reports, with varying degrees of emphasis:

- Human resource development, not finance, is the main constraint on Bhutan's development.
- Considerable unexploited potential exists for forestry development. This view was especially prominent in early reports, less so later.
- Fiscal management is the main macroeconomic constraint. Increased revenues are vital for funding recurrent expenditure domestically. Expenditure planning needs to take better account of the recurrent expenditure implications of capital investments.
- The government needs to encourage private sector development to diversify the economy and provide jobs for a growing labor force. This theme became increasingly prominent, culminating in the *Private Sector Survey*.
- Poverty reduction is a matter of growth and public expenditure for social services. As the 1994 CEM put it: "There appears to be relatively little scope for reducing poverty through redistributive measures. This suggests the

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<sup>23</sup> The first two were published: *Bhutan: Development in a Himalayan Kingdom* (PUB4307 01/31/84), and *Bhutan: Development Planning in a Unique Environment* (PUB7189 01/31/89). The 1994 and 1996 reports are unpublished: *Bhutan: Country Economic Memorandum* (Report No. 13495, 11/29/94), and *Bhutan: Country Economic Memorandum* (Report No. 16113, 12/20/96).

solution to poverty has to come through economic growth and development of the human capital base. The latter will require prudent fiscal policies to ensure that resources are available to properly fund social services for the poor.”

3.4 Bhutan’s achievements in fiscal management and provision of social services have been substantial. (Achievements in education and forestry are discussed below). Domestic tax revenue has risen from 7.2 percent of GDP in 1993 to 9.9 percent in 2001, though total domestic revenue (excluding grants, but including power royalties) declined marginally from 23.8 percent of GDP to 22.9 percent over the same period. In most years there has been a surplus of domestic revenue over recurrent expenditure. Education and health account for 35 percent of recurrent spending and 25 percent of overall budget outlays.

3.5 What is unclear is how much influence the Bank had on economic policy. The 1993 assistance strategy foresaw the Bank complementing IMF macroeconomic advice through periodic review of budget documents to assist the government and other donors in planning and fiscal management. In the event, Bank advice in this area seems to have been marginal. The Bank offered advice on recurrent costs and budgetary methods which prompted some discussion and probably brought some benefit. The authorities asked for advice on two issues: the exchange rate regime and management of the budget deficit. On the first issue, the Region’s Chief Economist gave advice which was well-received. On budget management, the Bank responded by trying to develop a RMSMX model for projections but this came to little because of data problems.

3.6 The 2000 assistance strategy stressed the Bank’s comparative advantage in transferring knowledge and ideas rather than finance. The CAS stated that the government had asked for consultations on macro policy, financial sector strategy, long-term health and education strategies, and accounting and auditing standards, and for assistance in poverty generation and analysis. In addition, the Bank proposed possible analytical and advisory work on private sector development, foreign direct investment, trade and investment reform, public expenditure management, employment analysis, school curriculums, rural road capacity development, and policy frameworks for economic and sector development.

3.7 The Bank did very little of this work. Although one government agency had expressed interest in financial sector work from the Bank, another had asked the ADB to do a financial sector study. In the end, ADB was asked to do the study and the World Bank gave informal comments. ADB also did the poverty survey, which has proved to be very influential in changing perceptions about the nature and extent of poverty. The Bank did carry out a private sector survey in collaboration with the Ministry of Trade and Industry, the Bhutan Chamber of Commerce and Industry (BCCI), and UNDP. This study provides useful advice on a number of important issues and was very well received by both BCCI and the ministry, though some officials in the Ministry of Finance felt that the report was more a useful summary of what was known about private sector development than a source of new ideas. The Bank also did an informal study of the macroeconomic impact of the hydropower export boom in 2002. This highly relevant

and carefully-done study concluded that Bhutan has avoided the “Dutch disease” phenomenon in which a natural resource boom (or large foreign aid inflow) discourages production and investment in other tradables. However, this is an issue which bears revisiting as better data on prices become available, especially in view of recent export trends and urban property values. Finally, the Bank conducted a country financial accountability assessment in 2002 with the support of the Dutch government. Although there is a culture of fiscal conservatism and civil service probity in Bhutan, it is recognized that institutional procedures need to be developed to assure accountability and transparency in a more complex economy. The report provides several recommendations to that end, and has been followed by an IDF grant for institutional strengthening.

3.8 In brief, the Bank has provided some useful economic policy advice to the government, but the scope of activity has been far less than anticipated. Why was the World Bank not involved in the finance and poverty studies? Primarily, it seems, because the government does not want donors separately involved in studies. It is too costly and burdensome for a small country with a small civil service. Since Bhutan has a long relationship with the bigger donor (ADB), the government opted for ADB support. More generally, the government is wary of taking on too many studies which, even if free, have a high opportunity cost in terms of scarce senior official involvement. The Bank now seems to have recognized the danger of study overload. It has limited its proposed economic work to public expenditure analysis, which is an area in which the Bank is experienced and could provide useful support in helping integrate recurrent and capital budgets into a medium term expenditure framework. Moreover, the Bank has offered to adopt a low-key, informal approach—more like TA than AAA—which recognizes capacity constraints.<sup>24</sup> Capacity constraints also have implications for the PRSP process (Box 3.1).

### **Box 3.1. Bhutan’s PRSP**

For small countries with capacity constraints the PRSP process presents a special challenge. In Bhutan, it also posed a risk of strategy fatigue. The *Vision 2020* exercise supported by UNDP had already developed sector strategies and an overall strategy of growth and equitable development. These underpinned the government’s own 9<sup>th</sup> Five Year Plan, which was a highly inclusive process of bottom-up decentralized planning. The government was understandably hesitant, therefore, to embark on a PRSP. But the Bank and Fund agreed with the government that the 9FYP was, in effect, the government’s PRSP, with the proviso that the government prepare a cover note placing the Plan within a macro framework and outlining a monitoring and evaluation system. This agreement has encouraged Bhutan to go forward with a PRSP.

Bhutan is using the PRSP to round off and complete the strategic planning process started in *Vision 2020* and the 9FYP at minimum cost. This is a sensible approach, and it may be worth considering using a similar approach more pro-actively in future. This would have higher costs, but also higher benefits. The cost would be the opportunity cost of doing other activities. Potential benefits over the medium term could be: (a) sharpening the focus of the Five Year Plans to relate these to reform priorities, including the allocation and management of all public spending, both investment and recurrent; (b) focusing attention on better systems for monitoring income and non-income poverty trends; and (c) helping to shape donor programs and align them with the government’s priorities. This hybrid approach could serve as both a Plan and a PRSP. Bhutan will have to decide how much effort it wants to put into the planning/PRSP process to maximize net benefits.

<sup>24</sup> The government has recently asked for Bank TA for development of multi-year budgeting capacity.

3.9 The Bank's AAA, especially its economic and sector work (ESW), has objectives other than to influence government policy, notably to inform Bank management, other donors and the outside world about development issues and progress, and to lay the foundation for the Bank's strategy and lending. On most of these other dimensions the Bank's ESW in Bhutan has been effective for a small country program. Economic reports have usually been tabled as background documents for Donor Roundtable meetings. Other donors found these valuable. Some of the Bank's informal ESW, such as the study of Dutch disease and the work on forestry, has also proven useful to other donors.

3.10 The main shortcoming of the Bank's AAA in Bhutan has been inadequate sector work to provide a grounding for the Bank's lending and policy dialogue.<sup>25</sup> Over the course of involvement in education and forestry, the Bank has produced a useful body of analytic and strategic work, but it has tended to be too little, too late as well as too scattered and inaccessible to provide an adequate basis for institutional memory.<sup>26</sup> There have been signs of improvements recently. With the *Private Sector Survey* and an informal transport sector note, the Bank seems to have improved the link between analysis and lending.

## Lending

3.11 Bank lending in the two decades of involvement in Bhutan has been concentrated on education, forestry and infrastructure. Apart from an early technical assistance operation to build local government capacity for development and one foray into industry (a calcium carbide operation with a large forestry component), all ten Bank-financed projects have been to help build schools, manage forest resources or build local roads and urban infrastructure.

3.12 This concentration reflects the government's preference for using grants wherever possible. IDA credits are sought primarily for infrastructure investment such as school construction because grant funding is less readily available for infrastructure. This has also often led to a division of labor within projects in which IDA finances construction and other "hard" elements while a co-financier funds technical assistance (TA) and other "soft" elements with grants.

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<sup>25</sup> The Region has commented (see Annex E) that "the Bank is faulted for pushing AAA, but it is recommended that sector work should be increased upfront (thus implicitly in a 'supply-driven' mode)—although traditionally the government has not been interested in this type of Bank assistance." However, as noted above, ESW has multiple purposes and audiences. The Bank needs sector work to formulate a strategy and analytical framework for projects. It is as much a part of the way the Bank does business as appraisal reports and safeguard procedures.

<sup>26</sup> The Bank dropped a proposed "Natural Resources Management Policy Review" after it became clear that the government is not interested in further Bank lending. This should be reconsidered. Bhutan is a small country, but an important one for forestry issues. The Bank could fulfill its knowledge bank role by trying to distill lessons for Bhutan, other countries, and Bank sector assistance strategy. Since a considerable amount of informal work has already been done, the marginal cost of doing such a study should be relatively low.

3.13 Table 3.1 gives OED's ratings for completed projects (including the GEF project). The overall impact of the program has been positive with outcome ratings above the Bank average for the past decade.

**Table 3.1: OED Review Ratings**

<i>Project</i>	<i>Outcome</i>	<i>Institutional Development</i>	<i>Sustainability</i>
Technical Assistance	Satisfactory	Substantial	Likely
Forestry I	Satisfactory	Substantial	Uncertain
Forestry II	Satisfactory	Substantial	Uncertain
Education I	Satisfactory	Modest	Likely
Calcium Carbide	Satisfactory	Modest	Uncertain
Third Forestry	Moderately Unsat.	Modest	Non-evaluable
Memo: Trust Fund for Env. Cons. (GEF)	Satisfactory	Substantial	Likely

### ***Education***

3.14 Access to education has expanded enormously since the introduction of a modern educational system 40 years ago. Gross primary enrollment has increased to 82 percent and secondary enrollment (grades 7-10) to 49 percent;<sup>27</sup> the proportion of girls has risen to 47 percent in primary and 45 percent in secondary; and the quality of education is high by regional standards. Challenges remain, however. Enrollment remains below the South Asian average because of the difficulty of serving a remote and scattered population. In addition, only 71 percent of children entering primary school complete the full cycle; annual repetition rates are 12-13 percent; and performance on public examinations has declined somewhat in recent years. These problems reflect the lag in supply of qualified teachers in the face of rapidly growing enrollment. They also suggest that the education authorities are trying to maintain high standards, but they raise concerns nonetheless. Finally, there is a growing problem of unemployment among secondary school leavers despite a shortage of skilled labor. This reflects some combination of unrealistic expectations and a shortcoming of schools in providing needed skills.<sup>28</sup>

3.15 The Bank has been one of the largest donors in Bhutan's education sector.<sup>29</sup> Half the Bank's lending commitments in Bhutan have been for education (\$48.9 million of \$95.3 million total commitments). The third and most recent project (Education

<sup>27</sup> From the latest government figures using a population base of 600,000. Using population figures from the 2001 Labor Force Survey, the estimates are about 5 percent lower. Education at all levels is free. The medium of instruction is English.

<sup>28</sup> The 2003/2004 budget speech notes: "The perception of an emerging unemployment crisis arises largely from the mismatch between the skills of the school leavers and the jobs available in the economy. While most school leavers aspire for white-collar desk jobs in the civil service, the government cannot absorb all job seekers, as it would lead to an increase in the bureaucracy and additional costs on the economy."

<sup>29</sup> Bank assistance is estimated to have been 15-20 percent of external aid to education and its share will increase in the next five years. Other donors active in education include Switzerland, India, Denmark, Canada, Australia, Japan, UNICEF, and UNESCO (see Annex A, Table A.4 for activities by donor). ADB has been a large donor in education, with a program similar in size to that of IDA, but the government has decided not to borrow for education from ADB in future.

Development Project for \$31 million approved in June, 2003) alone accounts for nearly one-third of IDA's commitments in Bhutan.

3.16 The basic objectives of all three projects has been to increase capacity at the primary and junior high school level to meet the demand of a burgeoning school-age population (school enrollment is growing at about 8 percent per annum) and improve education quality through enhanced teacher preparation, improved learning processes and assessment and stronger management. The first two projects were co-financed with the Swiss Development Corporation (SDC), who financed teacher training and other "software" elements. Bank funds have mainly been used for construction of a total of 23 primary and junior high schools, accommodating over 14,000 students or more than 13 percent of the total number of students in grades K-12 in the country. Over 80 percent of the recently-approved EDP will also be devoted to school construction. The project has no external co-financing, though the Bank is coordinating with Switzerland, Denmark, and other donors who are financing complementary projects.

3.17 The contribution of funding school construction should not be disparaged. The government finds it difficult to obtain grant funding for construction and is very appreciative of the Bank's support. OED's recent Ghana education impact evaluation found that building quality had a significant impact on education outcomes.<sup>30</sup> The Bank has shown attention to quality and respect for Bhutanese tradition in its building designs. The schools built with Bank funding under the first two projects were constructed in traditional stone and wood designs, some with elaborate paintings on both facades and interior spaces. The additional costs compared to "standard" designs were not estimated, but may have added 15-20 percent to the basic cost.

3.18 Although the bulk of IDA lending goes for construction, the Bank has been engaged in all aspects of educational development. The Bank has done no formal sector work in education, but it has accumulated considerable sector knowledge through project-financed studies and it played a key advisory role in helping the government develop its education strategy in 2000. Bank projects have supported education improvements including continuous assessments, in-service training, examinations and local language textbooks. The decentralization of education administration is also being supported. There has been no separate project implementation unit for Bank projects, which remained the responsibility of several departments within the Ministry of Education. This has helped promote an integrated approach to education development issues.

3.19 The main shortcoming of Bank support for education has been the lack of formal, up-front sector work. There have also been weaknesses in project implementation. Monitoring and evaluation of education outcomes have been weak, despite attempts to address M&E systems in Bank projects. Construction delays have also slowed the implementation of Bank projects.<sup>31</sup> The first operation took nine and a half years to be completed, including an 18 month extension of the original closing date. The second

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<sup>30</sup> OED (2004). "Books, Buildings and Learning Outcomes: An Impact Evaluation of World Bank Support to Basic Education in Ghana".

<sup>31</sup> There is a shortage of local stone masons to construct the traditional stone and wood buildings. The government has been reluctant to give work permits for Indian workmen to accelerate construction.

project has been extended two years beyond its original closing date to June 30, 2005, in order to complete all the schools.

3.20 The main strength of Bank support for education has been its continuous involvement in the sector. The two completed education projects have largely met their objectives and the sustainability of their reforms is likely, due to the ownership of the program, clarity of goals, and the strong partnership among donors and the Ministry. The new EDP is designed to address the weaknesses found in the first two projects. The project will introduce a new prefabricated building design and technique to speed construction while preserving the traditional appearance of school buildings. The project will also help redesign the mathematics curriculum, improve M&E, and conduct tracer and other studies to evaluate the relevance of the curriculum for the local labor market. Although it is too early to evaluate its impact, the project design appears relevant and responsive to difficulties identified in earlier projects.

### *Forestry and natural resource management*

3.21 Forests play a central role in Bhutan's socio-economic development. Forestry activities account for about 11 percent of GDP, 3 percent of government revenue through product sales and royalties, and 20 percent of export revenue, second only to electricity. Rural households are dependent on forests for fuel (Bhutan has the highest per capita consumption of firewood in the world), building material, and cattle grazing. Indirectly, forests are essential for protection of soil and water regimes as well as to hydropower generation.

3.22 The government gives high priority to protecting the environment and has therefore followed a cautious policy of commercial exploitation. The area covered by forest has actually increased over the past decade and is currently estimated at 72 percent of total land area. The Department of Forestry Services (DFS) is responsible for forestry management and regulation. A semi-autonomous public entity, the Forestry Development Corporation (FDC), is responsible for commercial exploitation, though some logging operations are contracted out to private operators. At the same time, the government sees forests as a development asset and wants to promote wood industries, primarily through the private sector.

3.23 A critical issue for development strategy is whether Bhutan has the balance between conservation and economic exploitation right. Or to put it more restrictively, within the constraints of sound conservation, is Bhutan effectively exploiting the sustainable economic potential of its natural resources?

3.24 The Bank has generally argued that Bhutan has not effectively exploited the sustainable economic potential of its forests. The first two economic reports argued that potential was far greater than production, and early projects sought to promote plantation forestry. In retrospect, it seems clear that the Bank has a history of over-estimating the potential for expanding the country's commercial forestry production by failing to

recognize significant logistical and manpower constraints.<sup>32</sup> Beginning in the early 1990s, the Bank began to give more emphasis to using forest resources to improve rural livelihoods through community-based natural resource management (social forestry), though it continued to support improved forest management practices and development of wood-based industries.

3.25 Although the Bank's economic reports addressed forestry issues, there was no formal sector work. Informal sector work addressed pricing and marketing issues (see Annex B) as well as overall sector strategy, but the main instrument of Bank strategy was projects. The Bank has made three loans for forestry, in FY84, FY88 and FY94 for a total of \$12.0 million. The last two projects were co-financed with the Swiss Development Corporation.<sup>33</sup> In addition, the Bank was executing agency for a Global Environmental Facility grant of \$10 million for the Trust Fund for Environmental Project (see Box 3.2); supported a large forestry component under an early industrial sector project (the Calcium Carbide Project in 1985); and provided an IDF grant (Forestry Institutional Development Initiative) for \$500,000.

**Box 3.2: Trust Fund for Environmental Conservation**

An innovative Trust Fund financed by a Global Environmental Facility (GEF) grant of \$10 million in 1992 has drawn world-wide attention to Bhutan's conservation efforts. This was the first such Trust Fund in the world. Co-financing and earnings on investments enabled the Fund's assets to grow to \$36 million before market reverses in 2001-2002.

Earnings from the Trust Fund were used to strengthen and extend Bhutan's protected area system which, with the recent separate "Gift to the World" allocation of connecting corridors, now covers 36 percent of Bhutan's land area. The Fund has become the primary source of finance for the recurrent costs of protected areas.

The Trust Fund has become a frequently-cited model for financing bio-diversity conservation. It has helped reinforce Bhutan's already-high commitment to conservation. It has also contributed to Bhutan's potential for eco-tourism, both by enhancing the country's international reputation and by alerting the country's leadership to the possibility of generating revenue from forests through conservation and tourism as well as (or instead of) commercial logging.

OED rated the outcome of the Trust Fund project Satisfactory in 1998. Institutional development was rated Substantial and sustainability Likely. Outcomes on the ground are difficult to assess because of time lags in monitoring species and habitats, but the Trust Fund's governing board has recognized the need for outcome monitoring to improve effectiveness of conservation investments and to promote accountability.

3.26 The overall impact of the Bank in the forest sector has been mixed. The three projects tested new approaches to plantations, reforestation, environmental management and social forestry. Physical targets under the First Project were met or exceeded, but reforestation and plantation techniques introduced under the project have not been widely replicated in Bhutan. Their impact has been very modest. The Second Project helped train staff in techniques for dealing with pest management and improved processes for salvage of overage and diseased trees. But it left unresolved a number of questions

<sup>32</sup> This is the conclusion of an internal draft paper by the South Asia Region which reviewed forest sector cooperation between Bhutan and the World Bank between 1983- 2002.

<sup>33</sup> Other donors active in the sector include Germany and ADB. See Annex A, Table A.4.

regarding the profitability and role of the Bhutan Logging Corporation (BLC) and emerging issues of forest product pricing and marketing.

3.27 The Third Forestry Project in FY94 focused on Eastern Bhutan and sustainable forest management practices, including scientific management and extraction of natural forests, introduction of social forestry for community-based forest management, trial reforestation techniques and institutional strengthening, especially for decentralization of the DFS. Although not specified as such, the project was probably the first effort in the South Asia Region to introduce “reduced impact logging,” an innovative approach. The project also introduced more systematic and professional approaches to forest management and formed the basis for a shift in thinking about community engagement in forest protection and exploitation.

3.28 On the other hand, stated objectives of introducing financially self-sustaining commercial forestry into Eastern Bhutan and rationalizing the economic and financial incentive framework through changes in price policy and forest legislation were not achieved. Decisions to ban the export of unprocessed logs (1999) and semi-finished products (2000) changed market conditions radically and only 84 percent of the logs harvested during the project period were ever sold. The Bank might have had more impact if it had done more systematic sector work at an earlier stage (see Annex B) and enforced project conditionality more strictly.<sup>34</sup>

3.29 OED rated outcome of the Third Forestry Project Moderately Unsatisfactory. The social forestry and reforestation components of the project were unsuccessful, due in part to the reluctance of the DFS to cede responsibilities to local communities, as well as the lack of a clear policy on grazing that has impeded the natural regeneration of forests in the Region. Implementation was adversely affected by frequent turnover of Bank staff and inadequate supervision (see para. 3.39 below). Given the regional nature of the project, the Bank had limited influence on national forest policies.

3.30 The Swiss Development Corporation agreed that the low rating of project performance was justified. The Bhutan Government has decided not to borrow again for forestry, despite the intense interest of the DFS. This suggests that both the borrower and funding partners found the Bank’s visible impact in the forestry sector to have been rather limited.

### ***Infrastructure***

3.31 *Urban Development Project.* In December 1999, the Bank made a loan of \$10.8 million to support development of urban infrastructure in 10 provincial towns.<sup>35</sup> The loan supports investments in water supply and solid waste management in all ten towns, and selective investments in street improvement, footpaths, markets and river protection. It

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<sup>34</sup> The government resisted implementing covenanted pricing reforms. For this and other reasons, a supervision mission proposed rating the project unsatisfactory, but this was overruled by regional management. This sent mixed signals and may have delayed reform. Shortly thereafter, an internal assessment review rated the Bank’s supervision of the project unsatisfactory (see below).

<sup>35</sup> This is the first Bank project in urban development in Bhutan. Other agencies involved in the sector include DANIDA, ADB, and UNDP.

also strengthens service delivery capacity. The basic objective is to improve the quality of life in these communities to slow migration to Bhutan's two major cities.

3.32 The project was approved too quickly before preparation had been completed, with a resulting delay in implementation of almost two years and an unsatisfactory rating for implementation progress (since upgraded). Implementation has since picked up and the project is likely to be completed by the scheduled closing date of December 31, 2005.

3.33 Supervision missions have expressed concern over the lack of adequate supervision locally or from Thimphu. The OED mission noted considerable variability in the apparent competence of local engineering staff. Staff at the Dzongkhag (provincial) level did not yet seem to feel "empowered" by the decentralization process. Investments in some localities appear to be based more on sentiment than economic analysis (such as the \$1 million for Trongsa with a population of 2,500 and no room to expand).

3.34 *Rural Access Project.* Also in December 1999, the Bank approved an \$11.6 million loan to finance 122 km of feeder roads in three eastern provinces of Bhutan. The investment represents over one-third of the road length to be built under the 8<sup>th</sup> Five Year Plan (1997-2002). Poverty is concentrated in remote villages more than a day's walk from the nearest road. The project is designed to provide access and reduce transportation costs.<sup>36</sup> Road construction is based on the concept of Environmentally-Friendly Construction (EFC) methods, an approach that was developed under the project and reflects Bhutan's commitment to protection of the environment in its development effort. Co-financing from the Netherlands provides technical assistance.<sup>37</sup>

3.35 The Rural Access program suffered the same teething problems as the Urban Development Project. It was rushed through the Board without adequate preparation. The EFC techniques were new to Bhutan and it took time to understand and build competence in using EFC. However, the EFC approach has now been adopted on all feeder roads in Bhutan—a significant impact of the project.

### ***Strengths and weaknesses of lending***

3.36 Bank lending in Bhutan has been a "no-frills" program of infrastructure development—roads, schools, water supply and sanitation and forest management, reflective and respectful of the needs of a traditional society still in the early stages of its development process. Each project has included basic capacity building, usually funded by bilateral partners with grant assistance, while the focus of the Bank's investment has been on building basic physical infrastructure.

3.37 The lending program has been client-driven, carried out in partnership with bilateral agencies and reflective of the country's holistic approach to development (including its cultural and traditional values). In a sense, it has been a model of the

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<sup>36</sup> The project is estimated to bring over 25,000 people living up to two days' walk from the nearest road to within half a day's walk or less. A study in one of the project districts showed that this degree of improved access is associated with a doubling of both school enrollment and household income.

<sup>37</sup> Other donors in the sector include India, Japan, Switzerland, and ADB.

comprehensive development framework long before it found its way into the Bank lexicon. The lending program has been:

- **Responsive.** Bhutan has borrowed only when grant funding has not been available. The government has decided the sectors and overall size of the lending operations. Education, forestry and infrastructure have been, and remain, high priority sectors for the development of the economy. Project designs have respected Bhutan's cultural and environmental traditions, even at somewhat higher cost.
- **Effective.** As indicated in table 3.1 above, five of the six completed projects have been judged to have had satisfactory outcomes, although sustainability has been considered uncertain in three operations.<sup>38</sup> Institutional development impact has been mixed, with three of the projects rated substantial (four including GEF) and three modest.
- **Hardware-oriented but with associated technical assistance.** Bhutan has used IDA funds primarily to finance the physical aspects of projects. However, all projects have had significant technical assistance funded by grants from bilateral partners.

3.38 At the same time, the lending program has had some shortcomings:

- **Sometimes inadequately prepared.** Two recent projects, for Urban Development and Rural Access, were prepared in a great hurry and submitted together with the Bhutan CAS without sufficient preparation. The result was a loss of up to two years in implementation, and an unsatisfactory IP rating for the Urban Project in 2002.
- **Sometimes indifferently supervised.** Supervision has also been problematic. Projects in remote areas were rarely visited by financial or procurement staff. An internal assessment review rated the Region's supervision of the Third Forestry Project as unsatisfactory in 1998. The review and the subsequent ICR criticized supervision missions for this project for being poorly prepared and spending too little time in the field. Management oversight and follow-up actions were also criticized (see footnote 29), the review concluded that the Borrower had little commitment to the operation. The Bank appears to have responded to these criticisms, however, because a follow-up review in 1999 rated supervision of the same project satisfactory.
- **Lack of continuity.** Staff turnover has been a problem. Forestry III had six task managers, which may partly account for its poor outcome. Continuity was exemplary for many years in the education sector, but EDP has had three TMs, lost a year in preparation and frustrated the principal partner of the first two

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<sup>38</sup> The Calcium Carbide project has proven to be sustainable, though it was rated uncertain shortly after completion.

projects—Helvetas of Switzerland—into going its own way. Urban Development is on its third TM in three years.

- **Insensitive to size.** The overall Bank lending program has respected Bhutan’s approach to development—the concept of Gross National Happiness—and is well regarded by borrower representatives. However, project requirements have not reflected the extremely small size of the country. With a civil service of less than 15,000, including teachers but excluding the military, Bhutan lacks the staff capacity to conform easily to Bank requirements for reporting, financial management and procurement. The Urban and Rural Access Projects were required to adopt the “LACI” approach to financial reporting with its Project Management Report (PMR)-based disbursements which proved beyond the capability of many larger borrowers (and has since been simplified). Procurement rules such as pre-qualification requirements for bidders have not made accommodation for the unique circumstances of a nascent contracting industry.

### *Donor cooperation*

3.39 The government is the main aid coordinator at the economy-wide and sector level. The Bank formally co-chairs (with UNDP) the periodic Round Table meetings between the government and donors, and usually provides an economic report or other background document on the economy, but the main estimates of aid requirements come from the FYP process. Similarly, at the sector level, the government decides which donors will be involved in which sectors and in which kind of activities. Donors share information at the sector level, though India tends to operate outside that network and deal directly with the government.

3.40 For the Bank, the main form of donor cooperation has been at the project level, through co-financing. Co-financing has been a critical element in most IDA projects because of the government’s preference for using grants wherever available. This typically leads to a division of labor in which IDA mainly funds infrastructure and other “hard” elements and the co-financier funds technical assistance and other “soft” elements. When the Bank has funded a project without co-financing it has sensibly sought assurances from the government that complementary TA will be provided by others if Bhutan does not want to borrow from IDA for this purpose. Coordination needs to work well to ensure project success and, for the most part, it has. Even when the project outcome has been less than satisfactory the Third Forestry Development Project (TFDP) co-financing was a strength. Cooperation with the Swiss Development Corporation (SDC) ensured many positive technical outcomes, provided flexibility on financial procedures and topping up which the Bank did not have, and provided project continuity to help offset the high turnover of Bank task managers.

3.41 Nevertheless, there have been criticisms, including from co-financiers, of the Bank’s cooperation with other donors. SDC stated that its contribution to TFDP was inadequately acknowledged, that its concerns and proposals during supervision missions were not taken seriously enough by the Bank, and that no one from Bank management

had ever visited the project area.<sup>39</sup> Field representatives of other donors said that visiting Bank missions did not always brief other donors active in the sector on their activities, in contrast to ADB which regularly briefed Bhutan-based sector donor groups convened by UNDP. And, as noted earlier, delays in Bank decisions led Helvetas to withdraw from co-financing EDP.<sup>40</sup>

3.42 These criticisms should be kept in perspective. The critics stressed that their experience of working with the Bank had been largely positive, and that some of the difficulties reflected the normal strains of working together. Delays and conflicting procedures have arisen on both sides, or were sometimes due to government decisions (or indecision). Critics also recognized that the absence of local representation complicated Bank coordination. Working relations also varied from task manager to task manager, and some of the problems arose because of staff turnover.

3.43 What can the Bank do to improve cooperation with other donors? One thing it should not do is avoid co-financing simply to avoid the complications of coordination. There are too many benefits to the Bank and to Bhutan of internalizing coordination at the project level. The most obvious positive thing the Bank can do is to provide better continuity of staffing. The Bank could also use the UNDP office to help liaise with other donors. Visiting missions should make a point of discussing mission plans and findings through briefings of other donors at the beginning and end of missions. At the programming level the Bank should coordinate with ADB on its proposed ESW to avoid duplication.

## **4. Evaluation of the Bank's Assistance**

4.1 Bhutan has successfully used a large aid program and foreign exchange earnings from hydropower exports to promote growth and provide widespread social benefits to the population. In this, Bhutan provides a rare example of successful management of windfall resources for broad-based social and economic development in the face of severe development constraints.<sup>41</sup> This section will evaluate the extent to which the World Bank's small assistance program contributed to this success in the areas in which the Bank sought to help, and the impact of Bank assistance in helping address Bhutan's development. The section will rate the outcome, sustainability, and institutional development impact of the Bank's assistance, and examine Bank performance.

4.2 The Bank's early strategy was to provide economic policy advice and lending assistance to selected sectors. In pursuing this limited role, the Bank recognized its position as a relatively minor player. In 2000, the Bank broadened the proposed scope of its activity considerably. While recognizing that it couldn't do everything, it was prepared in principle to consider doing anything the government wanted. Moreover, the

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<sup>39</sup> These statements were made in the donor comment annex of the project ICR.

<sup>40</sup> Although separate Danish and Swiss projects will proceed in parallel with EDP, the absence of formal co-financing links may be a handicap for the Bank.

<sup>41</sup> Botswana is the leading successful example among small economies.

Bank sought to increase its relevance to Bhutan by offering its services as a knowledge bank in line with its presumed comparative advantage.

### **Outcome of the Bank's Assistance**

4.3 The overall rating of the outcome of Bank assistance depends mainly on the relevance of the Bank's assistance strategy and the efficacy and efficiency of its products and services in the main operational areas of Bank support. Outcome depends not only on the Bank's performance (discussed separately below) but also on the performance of the government and other donors and on external events. Annex D elaborates the definitions and methodology used by OED in its ratings.

4.4 *Relevance of Bank assistance.* The Bank's assistance strategy was broadly relevant during the past decade. The three main objectives of Bank assistance during most of the period—providing economic policy advice, supporting education development, and improving forestry management—were all important development issues, and the way the Bank provided assistance followed government preferences and complemented the assistance of other donors.

4.5 In education the bank moved steadily from helping expand primary schooling opportunities to expanding secondary schools and, more recently, to trying to link school curriculum to the practical needs of the labor market, while promoting private sector development to increase provision of jobs. In forestry the Bank initially had unrealistic expectations of the scope for economic and sustainable commercial exploitation. But in the past decade, the Bank enhanced the relevance of its assistance by scaling back earlier expectations of forestry development potential and putting greater emphasis on reduced impact logging, pricing issues, and social forestry. With respect to economic policy advice, proposed assistance on fiscal management and later, private sector development, were both relevant, but the ambitious expansion of proposed AAA was unrealistic and insufficiently selective. More generally, the proposal to act primarily as a knowledge bank in Bhutan was inconsistent with what the Bank was actually doing (expanding lending) and not that relevant to Bhutan's needs or the Bank's (or Bhutan's) capacity. In practice, however, the areas of assistance accepted by the government continued to be relevant.

4.6 *Efficacy of Bank assistance.* Although the Bank generally set relevant objectives and had a realistic strategy for achieving them, efficacy in implementing these objectives has been mixed. Five of six project outcomes (six of seven counting the Bank-executed GEF project) have been rated satisfactory, but the exception—the largest, most important, and most recent forestry project—was an important one. The AAA which the Bank has provided has been sound, though the impact of recent studies remains to be seen. Moreover, the absence of sector work before lending was a serious shortcoming.

4.7 *Efficiency of Bank assistance.* It is difficult to obtain a meaningful estimate of the efficiency of Bank assistance to Bhutan because of the special circumstances of the country. The average cost of lending, supervision, and ESW per approved project for the period FY93-FY02 was \$1.157 million—significantly below the average for the South Asian Region (\$1.627 million) and for the Bank (\$1.456 million)—but this comparator is

unreliable because of the lumpiness of the Bhutan lending program. Different periods give substantially different results. Supervision costs per project during the late 1990s (FY96-FY99) were about 16 percent higher than the Bank average, but given Bhutan's difficult terrain and the location of the TFDP in Eastern Bhutan, it is doubtful whether the Bank allocated enough funds for proper supervision during this period. On balance, there is no reason to believe that administration of the Bank's program in Bhutan was inefficient.

4.8 *Overall outcome.* Based on the outcome of individual objectives and the relevance, efficacy, and efficiency of the Bank's products and services, overall outcome of Bank assistance to Bhutan is rated *moderately satisfactory*.

### **Sustainability of Positive Outcomes**

4.9 Using a simple project count, only two Bank projects (three counting GEF) were rated as likely to be sustainable. Taking into account ongoing as well as completed projects, sustainability of development impact is likely in the education sector and in rural road construction (where EFC has already been adopted as the standard throughout the country). In forestry, the outlook is mixed; many technical achievements appear sustainable, but innovations in social forestry appear unlikely to be sustained at this stage, and the future of the pricing and marketing regime is unclear. The sector rating for sustainability in forestry, like that for the latest project, is non-evaluable. Similarly, it is too soon to evaluate the Bank's program in urban development. On balance, overall sustainability is rated *likely*.

### **Institutional Development Impact**

4.10 Institutional development impact (IDI) was rated substantial for three of the Bank's six completed projects (four of seven counting GEF) and in the remaining three projects IDI was rated modest. A separate IDF grant in forestry has had a substantial impact on IDI both within DFS and in helping create an Association of Wood-Based Industries. The Bank has also brought several Bhutanese officials to Washington to work as interns within the Bank for several months. This has reportedly had a positive impact. Overall, the Bank's small program has had a *substantial* institutional development impact.

### **Bank Performance**

4.11 Bank performance has been very mixed. On the one hand, the Bank has been very responsive to government wishes, sensitive to Bhutan's cultural and environmental traditions, and effective in using partnerships with other donors to complement Bank contributions to projects. On the other hand, the lack of sector work, inadequate preparation and supervision for some projects, and occasional frictions in cooperation with other donors have limited the effectiveness of Bank assistance. Bank performance has been affected by continuity in staffing and attention. Excessive and sudden attention can be as unproductive as inattention in a small country because it is overwhelming. Continuity was exemplary at the country officer level and in education, especially during

the 1990s, but was seriously lacking in forestry and in the aftermath of Bank reorganization. Recently the Bank seems to have improved on this issue.

## 5. Lessons and Recommendations

5.1 Some of the following lessons and recommendations may be applicable to the Bank's assistance strategy in other small countries, or in other situations in which the Bank plays an unaccustomed small role.

5.2 *Listening enhances effectiveness.* The Bank was effective in Bhutan when it listened to what the government wanted rather than trying to figure out what the government needs and then trying to persuade the government to accept the proposal. Thus, providing funding for basic infrastructure has generally been successful because this is what the government wanted from the Bank. Proposals in the 2000 CAS for the Bank to serve as a knowledge Bank have not been successful because, in the event, the government did not request the Bank to move in this direction.<sup>42</sup>

5.3 *Co-financing is an especially useful instrument in a small country.* In Bhutan co-financing gave the Bank financial flexibility and invaluable local and specialized technical knowledge. It also provided continuity in the face of Bank staff turnover and helped make up for the Bank's lack of field presence.

5.4 *Need for staffing continuity.* This is particularly difficult in a small country with episodic Bank involvement, but it is important nonetheless. One reason for the better outcomes in education than in forestry was high staff turnover in the latter sector. The lack of field presence puts an even higher premium on continuity of staffing in Washington.

5.5 *The importance of being selective and focused.* It is a mistake to try to be a "full service bank" in a small country unless the Bank is a dominant lender. It is better to be involved in depth and over time in a few areas in order to have an impact. It is too costly for the Bank and for the country to have the Bank involved in a large number of activities. Also, from Bhutan's point of view, a wide-ranging program increases the risk of "donor tourism" in which many managers and staff visit Bhutan once or twice but contribute little to the country. This is a concern because of the burden it imposes on Bhutan's scarce administrative resources.<sup>43</sup>

5.6 *It is necessary to be selective in AAA as well as lending* because of capacity constraints on both sides. It is hard to be a knowledge bank in a small country. The Bank needs to invest resources in order to provide useful advice based on local conditions. The government is constrained by the limited time of senior officials to work with the Bank or

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<sup>42</sup> See the Region's comments in Annex E. See also footnote 21 above.

<sup>43</sup> See the Region's comments in Annex E. Management and staff visits are necessary for any agency to conduct business and can be beneficial for both the program and the country. But the burden this places on a small country should be recognized by all donors.

discuss the issues. A stand-alone non-lending services program is likely to be of limited value.

5.7 *More upfront sector work is needed.* Selectivity in lending and in AAA should be joined. The Bank should return to the more selective approach of its earlier country assistance strategy, but make it more effective through prior sector work. Indeed, ESW can help support the selection process, as has been the case for private sector development.

5.8 *The Bank needs to develop ways to compensate for its lack of field presence.* The Bank has no field office in Bhutan. It would be expensive to provide an office for a small program and the government does not want it. Nor does the government wish to be part of country unit based in a regional hub. To help serve Bhutan better with these constraints, the Bank could adopt some of the procedures of the ADB which also coordinates its Bhutan program from its headquarters in Manila. The most important of these are annual rolling program consultations and use of UNDP facilities by visiting missions to liaise with other donors based in Bhutan.

5.9 *Sensitivity to constraints of a small country.* Many Bank procedures (procurement and reporting) are poorly adapted to a small country with a small civil service. The high and growing demands of the Bank and other agencies for reporting on a standard set of issues (fiduciary safeguards, environment, etc.) and for formulating strategies to meet national and international targets (PRSP, Vision 2020) while each valuable individually, add up to a formidable burden for small countries. The Bank should adapt its procedures to adjust to the special circumstances of small countries.

## Annex A: Foreign Assistance by Donor and Sector

**Table A.1: Grant Assistance by Donor, 1992/93-2001/02**  
(millions of \$US using FY average exchange rates)

	<i>Total</i> (92/93-01/02)	<i>Share of Total</i> (%)
India	322.9	51.1
DANIDA	65.6	10.4
JICA	45.7	7.2
Netherland	27.4	4.3
UNDP	17.8	2.8
Austria	17.7	2.8
Helvetas	17.9	2.8
SDC	16.4	2.6
EEC	15.2	2.4
UNCDF	13.5	2.1
Others*	71.2	11.3
<b>Total</b>	<b>631.3</b>	<b>100.0</b>

Source: RMAAR 01/02, p.140.

\*These are grants going directly to the central government budget under revenue, and do not include grant.

**Table A.2: Concessional Loans Disbursed by Donor, 1981/82-2001/02**

	<i>Total</i> Million US\$	<i>% of Total</i>
India*	215.5	56.7
ADB	62.5	16.4
WB	36	9.5
KFAED	27.7	7.3
Austria	20.4	5.4
IFAD	15.7	4.1
Mitsui & Co.	1.7	0.4
EFIC Australia	0.8	0.2
<b>Total</b>	<b>380.3</b>	<b>100.0</b>

Source: RMAAR 01/02, Table 24, p.83

\*FY average exchange rates were used to convert annual Rupee loans post 1995/96, and simple average of FY average exchange rates were used.

**Table A.3: Grant Assistance by Sector, 1990/91-2001/02(millions \$US)**

	<i>Total</i> (90/91-01/02)	<i>Share of Total</i> (%)
Agriculture	119.5	16.9
Communications	85.2	12.0
Culture and Youth	13.7	1.9
Health and Education	106.6	15.0
Power	83.0	11.7
Trade and Industry	4.5	0.6
Other Government Agencies <sup>1</sup>	132.2	18.7
Autonomous	5.4	0.8
Others <sup>2</sup>	158.8	22.4
<b>Total</b>	<b>708.9</b>	<b>100.0</b>

Source: RMAAR 01/02, p.141

<sup>1</sup>Capacity building of government agencies.

<sup>2</sup>Program Grants from India.

Table A.4: Bhutan's Comprehensive Framework of Ongoing Development Assistance

Dev. Partner	Governance	Education	Health	Forestry	Environment	Rural Dev't	Roads	Urban Dev	Power	Telecomm
Austria					Bhutan Trust Fund Land use & Environ. Planning Bhutan Trust Fund	Agro-Industries		Thimphu & Phunsholing	Basochu	
Denmark	Decentralization, Strengthen Royal Audit Authority, Tax Administration Assistance		Integrated Primary Health Care, Essential Drugs & Safe Water							
Germany		Tech. & Vocational Education Teacher Salaries, School Construction	Upgrading Health Posts Malaria Eradication	Conserv. & Sust. management		Promotion of cash crops	Construction & maintenance Paro roads and bridges		Tal, Kurichu, Bumakha Micro-hydel	Radio transmission Microwave Tel. Network
India						Paro Rural Dev.				
Japan										
Netherlands	Decentralization									
Norway					Bhutan Trust Fund					
Switzerland	Strengthen Royal Audit Authority	Primary/secondary Teacher training (with IDA)		Sustainable use, Protection & mgt. Of forest		Promotion of cash crop, Livestock Dev., Natural Resource Training Center	Bridges & Trails			
ADB	Strengthen Min. of Finance	Tech. & Vocational Education		Forest Development		Irrigation Support	Highway maintenance planning	Town Development	Rural Electrification	
EU						Livestock/Agr. Ext. Service				
GEF										
IDA	Round Table, Econ. & Budget Advice	Prim. & Lower Sec. Teacher Training	Consultations on long-term health finance and infectious disease	Sustainable Use, Protection & Mgt of Forests	Bhutan Trust Fund GEF supervision of Bhutan Trust Fund		Support RgoB Prog. Of improving rural access, initially in Zhemgang, Trashigang, Trashiyangse & Lhuentse	Secondary Towns		Telecomm corporatization
UNDP	Round Table, Planning & Budgeting, Aid Coord., Priv. Sector Dev., Modernization of Legal System				National Parks & Biodiversity	Promotion of Cash Crops				
UNICEF		Prim. & Lower Sec. Teach Training, Prim. Educ., Adult Literacy School Meals	Immunization, MCH, Family Planning							
WFP										
WHO			Disease Prevention, Human Res. Dev.				Food-For-Work			
WWF					Bhutan Trust Fund					

Source: 2000 CAS.

## **Annex B: Forestry Pricing and Marketing Policies**

1. Until 1969 use of forestry was free to all. For many years thereafter differential log prices were set for four categories of users: rural, urban, industrial, and export. Export prices were market-based and domestic prices were administratively set at below-market rates with highest subsidies for rural users. In 1991 a pricing reform eliminated subsidies to urban consumers, and subsidies to rural users have gradually been reduced and the category of eligible rural consumers has been narrowed.
2. In 1999 the government introduced a reform that established public timber auctions for all sales and banned exports of round-wood, sawn wood, and firewood. The new policy had multiple objectives: to promote more efficient use of forest resources, to strengthen incentives for domestic wood industries, and to make timber available for domestic consumers at affordable prices. The export ban was not total. Surpluses in the domestic market are sold through special auctions open to international buyers. After the new system was introduced, prices rose markedly. The government suspected leakage through export of partially-processed products and collusion among sawmill owners. It responded by extending the export ban to semi-finished products and by setting up state-owned sawmills to compete with the private sector.
3. The Bank had encouraged the government to simplify the pricing structure, reduce and improve targeting of subsidies, and introduce an auction system, but it recommended against an export ban. In a letter to the government before the policy was introduced, the Bank pointed out that international experience suggested an export ban is an inefficient instrument for protecting a local wood-processing industry. Restricting log exports tends to lower domestic log prices, thus encouraging inefficient processing and environmentally unfriendly harvesting practices. Financial returns from inefficient local processing may end up being lower than those from direct export of raw logs. An export tax would be a more efficient instrument for this purpose, though in view of India's reluctance to accept an export tax it could not be used. The Bank noted that the proposed system of exemptions to the ban might work as a second-best expedient but this should be monitored closely to avoid negative outcomes.
4. After the 1999 reform was introduced, the Bank and the Swiss Development Corporation did a study of the timber market which found no evidence of collusion among sawmillers. The study concluded that other factors (inelastic public sector demand, fragmented markets) accounted for pricing patterns and trends, and it recommended against public investment in sawmills. The government went ahead, however. More recently, the *Private Sector Survey* reported that the auction system had several shortcomings (such as auctioning only mixed lots of wood) that did not meet buyer preferences. This led to wastage, low prices for some high-value varieties, and high costs for local producers. Under an IDF grant (Forestry Institutional Development Initiative) the Bank supported a working group that brought together the private sector and forestry officials and catalyzed formation of an Association of Wood-Based Industries that successfully lobbied the ministry to rationalize guidelines for export of semi-finished products.
5. The Bank has offered good analysis and advice on forestry pricing and marketing and has been persistent, but its overall impact on policy has been limited. The Bank might have had more impact if had done more systematic sector work at an earlier stage and enforced project conditionality more strictly.



## Annex C: List of People Interviewed

### Ministry of Finance

Lyonpo Yeshey Zimba  
Minister of Finance

Dasho Wangdi Norbu  
Secretary for Finance

### Department of Aid & Debt Management

Aum Yanki T. Wangchuk,  
Director General

Mr. Lepo  
Senior Program Officer

Mr. Ugyen Norbu  
Program Officer

### Department of Education

Mr. Pema Thinley  
Director General

Ms. Pema Lhazom  
Project Manager

Mr. Thinley Rinzin  
Project Manager for SEP

### Rural Access Project

Mr. Kunzang Wangdi  
Project Manager

Mr. Niralal Rai  
Assistant Project Manager

### Urban Development Project

Mr. Tshering Dorji  
Director General

Aum Lhaden Pem  
Project Manager

### Ministry of Trade and Industry

Mr. Achyut Bhandari  
Director General, Department of Trade

Mr. Sonam Yangley  
Director, Department of Industry

Mr. Sonam P. Wangdi  
Head, PPD,  
Ministry of Trade and Industry

Ms. Karma  
PPD, MTI

Mr. Sonam Wangchuk  
Head, Foreign Trade Division, MTI

### Dzongkhag Administration, Bumthang

Daso Nima Tshering  
Dzongdag

Mr. Sangay Wangchuk  
Deputy Dzongdag

Mr. Namgay  
District Education Officer

Mr. Tempa Gyaltshen  
District Engineer

Mr. P.L. Subba  
Project Engineer

### Wangchholing Junior High School

Ms. Karma Choden  
Headmistress

Chume High School

Mr. Pema Chopel  
Principal

Dzongkhag Administration, Trongsa

Mr. Pema Thinley  
District Engineer

Mr. T.R. Gurung  
Project Engineer

Department of Forestry Services

Mr. Ugyen Thinley  
Director

Mr. Gopal  
Joint Director

SNV, Thimphu

Mr. Peter Newsum  
Acting Country Director

Mr. Henrick Visser  
Engineer, EFRC, SNV

Helvetas/SDC Coordination Office

Mr. Erwin Koenig  
Resident Coordinator  
UNDP

Ms. Reneta Lok Dessalien  
Resident Representative

Danish Liaison Office, Thimphu

Mr. Torben Bellers  
Resident Coordinator

Government of India, New Delhi

Mr. Ghanshyam  
Director, Nepal and Bhutan  
Ministry of External Affairs

World Bank

Sadiq Ahmed, Sector Director  
Simon C. Bell, Sector Manager  
Guan Zhe Chen, Sector Manager  
Christian Eigen-Zucchi, Economist  
Subramanian V. Iyer, Lead Financial  
Analyst  
Peter Jipp, Sr. Forestry Specialist  
Toshiaki Keicho, Sr. Urban Environment  
Specialist  
Mark LaPrairie, Education Specialist  
Chingboon Lee, Lead Education Specialist  
Alastair J. McKechnie, Country Director  
Peter Nicholas, Lead Country Officer  
Enrique Pantoja, Country Officer  
Daniel M. Sellen, Sr. Agric. Economist  
Frederick Swartzendruber, Consultant  
Marilou Jane Uy, Sector Director  
Tara Vishwanath, Lead Economist  
John W. Wall, Country Director

Former World Bank Staff

Chris Keil  
Mieko Nishimizu  
Manuel Penalver  
Grant Sinclair  
Joseph Wood

## **Annex D: Guide to OED's Country Assistance Evaluation Methodology**

1. This methodological note describes the key elements of OED's country assistance evaluation (CAE) methodology.<sup>44</sup>

### ***CAEs rate the outcomes of Bank assistance programs, not Clients' overall development progress***

2. An assistance program needs to be assessed on how well it met its particular objectives, which are typically a sub-set of the Client's development objectives. If an assistance program is large in relation to the Client's total development effort, the program outcome will be similar to the Client's overall development progress. However, most Bank assistance programs provide only a fraction of the total resources devoted to a Client's development by donors, stakeholders, and the government itself. In CAEs, OED rates only the outcome of the Bank's program, not the Client's overall development outcome, although the latter is clearly relevant for judging the program's outcome.

3. The experience gained in CAEs confirms that program outcomes sometimes diverge significantly from the Client's overall development progress. CAEs have identified assistance programs which had:

- satisfactory outcomes matched by good Client development;
- unsatisfactory outcomes in Clients which achieved good overall development results, notwithstanding the weak Bank program; and,
- satisfactory outcomes in Clients which did not achieve satisfactory overall results during the period of program implementation.

### ***Assessments of assistance program outcome and Bank performance are not the same***

4. By the same token, an unsatisfactory assistance program outcome does not always mean that Bank performance was also unsatisfactory, and *vice-versa*. This becomes clearer once we consider that the Bank's contribution to the outcome of its assistance program is only part of the story. The assistance program's outcome is determined by the *joint* impact of four agents: (a) the Client; (b) the Bank; (c) partners and other stakeholders; and (d) exogenous forces (e.g., events of nature, international economic shocks, etc.). Under the right circumstances, a negative contribution from any one agent might overwhelm the positive contributions from the other three, and lead to an unsatisfactory outcome.

5. OED measures Bank performance primarily on the basis of contributory actions the Bank directly controlled. Judgments regarding Bank performance typically consider the relevance and implementation of the strategy, the design and supervision of the

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<sup>44</sup> In this note, *assistance program* refers to products and services generated in support of the economic development of a Client country over a specified period of time, and *client* refers to the country that receives the benefits of that program.

Bank's lending interventions, the scope, quality and follow-up of diagnostic work and other AAA activities, the consistency of Bank's lending with its non-lending work and with its safeguard policies, and the Bank's partnership activities.

### ***Evaluation in Three Dimensions***

6. As a check upon the inherent subjectivity of ratings, OED examines a number of elements that contribute to assistance program outcomes. The consistency of ratings is further tested by examining the country assistance program across three dimensions:

- (a) a *Products and Services Dimension*, involving a "bottom-up" analysis of major program inputs -- loans, AAA, and aid coordination;
- (b) a *Development Impact Dimension*, involving a "top-down" analysis of the principal program objectives for relevance, efficacy, outcome, sustainability, and institutional impact; and,
- (c) an *Attribution Dimension*, in which the evaluator assigns responsibility for the program outcome to the four categories of actors (see paragraph 4. above).

### ***Rating Assistance Program Outcome***

7. In rating the outcome (expected development impact) of an assistance program, OED gauges the extent to which major strategic objectives were relevant and achieved, without any shortcomings. Programs typically express their goals in terms of higher-order objectives, such as poverty reduction. The country assistance strategy (CAS) may also establish intermediate goals, such as improved targeting of social services or promotion of integrated rural development, and specify how they are expected to contribute toward achieving the higher-order objective. OED's task is then to validate whether the intermediate objectives produced satisfactory net benefits, and whether the results chain specified in the CAS was valid. Where causal linkages were not fully specified in the CAS, it is the evaluator's task to reconstruct this causal chain from the available evidence, and assess relevance, efficacy, and outcome with reference to the intermediate and higher-order objectives.

8. Evaluators also assess the degree of Client ownership of international development priorities, such as the Millennium Development Goals, and Bank corporate advocacy priorities, such as safeguards. Ideally, any differences on dealing with these issues would be identified and resolved by the CAS, enabling the evaluator to focus on whether the trade-offs adopted were appropriate. However, in other instances, the strategy may be found to have glossed over certain conflicts, or avoided addressing key Client development constraints. In either case, the consequences could include a diminution of program relevance, a loss of Client ownership, and/or unwelcome side-effects, such as safeguard violations, all of which must be taken into account in judging program outcome.

### ***Ratings Scale***

9. OED utilizes six rating categories for **outcome**, ranging from highly satisfactory to highly unsatisfactory:

<i>Highly Satisfactory:</i>	The assistance program achieved at least acceptable progress toward all major relevant objectives, <u>and</u> had best practice development impact on one or more of them. No major shortcomings were identified.
<i>Satisfactory:</i>	The assistance program achieved acceptable progress toward all major relevant objectives. No best practice achievements or major shortcomings were identified.
<i>Moderately Satisfactory:</i>	The assistance program achieved acceptable progress toward <i>most</i> of its major relevant objectives. No major shortcomings were identified.
<i>Moderately Unsatisfactory:</i>	The assistance program did <i>not</i> make acceptable progress toward <i>most</i> of its major relevant objectives, <i>or</i> made acceptable progress on all of them, but either (a) did not take into adequate account a key development constraint or (b) produced a major shortcoming, such as a safeguard violation.
<i>Unsatisfactory:</i>	The assistance program did not make acceptable progress toward <i>most</i> of its major relevant objectives, <i>and</i> either (a) did not take into adequate account a key development constraint or (b) produced a major shortcoming, such as a safeguard violation.
<i>Highly Unsatisfactory:</i>	The assistance program did not make acceptable progress toward <i>any</i> of its major relevant objectives and did not take into adequate account a key development constraint, while also producing at least one major shortcoming, such as a safeguard violation.

10. The **institutional development impact (IDI)** can be rated as: *high, substantial, modest, or negligible*. IDI measures the extent to which the program bolstered the Client's ability to make more efficient, equitable and sustainable use of its human, financial, and natural resources. Examples of areas included in judging the institutional development impact of the program are:

- the soundness of economic management; the structure of the public sector, and, in particular, the civil service;
- the institutional soundness of the financial sector;
- the soundness of legal, regulatory, and judicial systems;
- the extent of monitoring and evaluation systems;
- the effectiveness of aid coordination;
- the degree of financial accountability;
- the extent of building NGO capacity; and,
- the level of social and environmental capital.

11. **Sustainability** can be rated as *highly likely*, *likely*, *unlikely*, *highly unlikely*, or, if available information is insufficient, *non-evaluable*. Sustainability measures the resilience to risk of the development benefits of the country assistance program over time, taking into account eight factors:

- technical resilience;
- financial resilience (including policies on cost recovery);
- economic resilience;
- social support (including conditions subject to safeguard policies);
- environmental resilience;
- ownership by governments and other key stakeholders;
- institutional support (including a supportive legal/regulatory framework, and organizational and management effectiveness); and,
- resilience to exogenous effects, such as international economic shocks or changes in the political and security environments.

## **Annex E: Bhutan Country Assistance Evaluation Comments from the Bank's Country Management Unit, South Asia Region**

Overall, the CAE team is to be commended for preparing a very comprehensive and well written evaluation report on Bank engagement in Bhutan. The team have pulled together a substantive amount of relevant information from a wide range of sources and perspectives, and present the conclusions in a constructive and independent fashion. The report will be very a valuable input to the new CAS for Bhutan, currently planned for FY05.

While we agree with the report in general, we would like to raise the following issues for your consideration before finalizing the report:

**The CAE still unfairly conveys the notion that the CAS was prepared without consulting RGOB.** This notion is exemplified in the statement offered in the Memorandum to the EDs and the President: *“The government was not prepared for program lending and did not agree to Bank involvement in many of the proposed studies, primarily because alternative support from ADB was available and because multiple donor involvement is burdensome”*(emphasis added). This type of statements run throughout the report, and culminate in Section 5 (Lessons and Recommendations) with the somewhat unbalanced statement that *“Proposals in the 2000 CAS for the Bank to serve as a knowledge Bank have not been successful because the government had not asked the Bank to move in this direction.”* (Para 5.2, p. 27)

As we explained before, **when the CAS was prepared in 1999, the government was in full agreement with the role proposed for the Bank**, i.e., increasingly placing its knowledge resources at the disposal of the government without tying them to IDA credits. As stated in the CAS (p. iii), at the time, *“[t]he government ha[d] already requested such knowledge based consultations on macroeconomic policy, a financial sector strategy, long-term health and education strategies, and accounting and auditing standards.”* In contrast, the CAE gives the impression that the Bank pushed aggressively and unilaterally for AAA. Examples of statements that may mislead the reader are: in the Memorandum (p.2), *“Proposals for the Bank to serve as a knowledge bank have not been successful because in the event most of the Bank offers of knowledge services were not taken up by the government.”* In the main text, *“The proposed program to implement the 2000 strategy included AAA on a vastly expanded range of topics”* (para 2.6). A look at Annex B4 of the CAS document, shows that the proposed AAA program reflected government requests, while footnote 1 specifically shows that the program was indicative, more so since *“AAA assistance [was] seen as open-ended in that it will respond to the needs of the government and when needed, and will therefore continue while it is justified in terms of knowledge transfer needs of the government.”*

Interestingly, the CAE's recommendation in this regard has an implicit contradiction: the Bank is faulted for pushing AAA, but it is recommended that sector work should be

increased upfront (thus implicitly in a “supply-driven” mode) – although traditionally the government has not been interested in this type of Bank assistance.

**At the same time, the CAE unwittingly gives the impression that the Bank was also trying to increase lending volumes during CAS preparation.** Contrary to what is assumed in the CAE, the two projects that went to the Board with the CAS were prepared rapidly in part to respond to the government’s request, not mainly to “increase the amount and scope of lending.” (CAE, para 2.9, p.11). For the record, the lending volumes in Bhutan have traditionally been so small that they do not have any impact on regional or Bank wide levels.

**In this respect, the CAE needs to reflect better the context of CAS preparation and implementation.** The government policy in 1999 was to rely as much as possible on grants, as there were serious concerns with Dutch disease symptoms, debt management, and expectations of continuous grant flows. Thus, RGOB had informed the Bank that it did not intend to borrow from IDA, particularly after the two projects that were being prepared and that went to the Board with the CAS. The Government, however, wanted the Bank to continue providing non-lending services as needed. For your information, RGOB still prefers to borrow IDA for capital investments, use grants for TA and finance recurrent expenditures with domestic revenue.

**What the Bank should be perhaps faulted with is not having prepared a new CAS sooner,** particularly as it became evident that (i) the government was not seeking as much Bank assistance in non-lending services as initially envisaged; and that (ii) Bhutan was increasingly interested in borrowing from IDA as grant flows declined and the financing gap for capital investments in the Ninth Five Year Development Plan (2002-2007) could not be fully bridged.

**The report also misrepresents the CAS statement regarding program lending.** The government has expressed interest during CAS consultations, as mentioned in the CAS, “in greater harmonization of donor support and in discussing the merits of more program-oriented funding and ha[d] asked for IDA’s help in thinking through the issues.(p.14)” The CAS did not assert that the government was prepared for program lending, or that this was a specific deliverable for the CAS period. In line with the government’s thinking, the CAS mentions program lending as a *possibility*, while explaining that before this could take place, further capacity building was needed in areas such as public expenditure management, financial management and auditing and accounting.

**In relation to above, the CAE should also make more explicit that priorities of RGOB changed rapidly** (and often after agreeing with the Bank on specific tasks such as the Financial Sector Report) On the other hand, we should recognize that the Bank has not done enough to educate its Bhutanese counterparts on what the Bank can offer in terms of knowledge services. This trend along with the related fact that the government has not always been clear on the assistance needed, indicates that the country has not fully benefited from the knowledge resources available at the Bank. But to be fair to the

Bank, the CAE should not so easily assume that “the Borrower has...a clear sense of what it wants from the Bank.” (Para 2.10, p. 11).

Additional Suggestions / Corrections:

Para 5.5, p.27: notion of “donor tourism” is somewhat harsh. For a small country with a small budget and without a country office with lower cost national staff, it is perhaps inevitable that managers and some staff visits are infrequent. Even if a person visits only once, the information gained is highly valuable for a contribution from Washington or management oversight. The key point is in para. 5.4, the need for staff continuity.



## Annex F: Comments from the Government of Bhutan



དངུལ་ཚིམ་ལྷན་ཁག།

གྲོགས་རམ་དང་རྒྱུན་འགྲུལ་འཛིན་སྐྱོང་ལས་ཁུངས།  
 DEPARTMENT OF AID & DEBT MANAGEMENT  
 MINISTRY OF FINANCE  
 ROYAL GOVERNMENT OF BHUTAN

DADM/IDE/ 5876  
 June 8, 2004

Mr. R. Kyle Peters  
 Senior Manager  
 Operations Evaluation Department  
 The World Bank  
 Washington DC 20433, USA.  
 Fax No. 001 202 477-6391

**Re: Comments on Country Assistance Evaluation Report**

Dear Mr. Kyle,

Kindly refer to your letter date 1<sup>st</sup> June 2004.

In this regard, we would like to submit the following comments on Para 1.5 – *Political and social issues* of Page 2.

The sentence “*Bhutan’s political system is in transition to a constitutional monarchy with a partly-elected, non-party national assembly and a written constitution.*” should be rephrased as “*Bhutan is in the process of drafting a written constitution to establish parliamentary democracy.*”

“*But there are also tensions arising from the application of Bhutan’s cultural preservation policy. In the early 1990s, there was an exodus of Nepali speaking people from Bhutan following the introduction of a new Citizenship Act.*”

This statement is not correct. The reason why a large number of ethnic Nepalese left Bhutan was because many of them were found to be illegal immigrants during a nation wide census exercise carried out in 1988. In order to curb the serious problem of illegal immigration and also protect the interests of the genuine Bhutanese citizens of Nepalese origin, mechanisms were instituted to identify illegal immigrants. Unfortunately, vested interest groups and some ambitious individuals opposed this and persuaded the illegal immigrants as well as some genuine Bhutanese citizens of Nepali origin to leave Bhutan. The promise of a safe haven in Nepal and a victorious return to Bhutan led to the congregation of such people in the camps in eastern Nepal.

Hence the so termed “tensions” are directly related to the detection of large numbers of economic immigrants of Nepali origin who had entered Bhutan illegally. Therefore, the reference to “cultural preservation” and “new citizenship laws” are factually incorrect and should be deleted.



དངུལ་རྒྱུ་ལྷན་ཁག།

གྲོགས་རམ་དང་སྤྱི་འགྲུལ་འཛིན་སྐྱོང་ལས་ཁུངས།

DEPARTMENT OF AID & DEBT MANAGEMENT  
MINISTRY OF FINANCE  
ROYAL GOVERNMENT OF BHUTAN

*"An agreement reached in 2003 provides for the return of refugees pending vetting for proof of citizenship by joint Bhutanese Nepali committee but the status of the refugees...pose significant challenge."*

The above statement is factually incorrect as the "return of refugees" is not contingent on the proof of citizenship alone. The issue of the people in the camps is not a typical refugee problem because it involves the politicization of issues related to various categories of people like: illegal immigrants; non-Bhutanese; Bhutanese who voluntary emigrated; criminal elements, etc. In view of this complexity the Government of Bhutan and Nepal have been working on a bilateral mechanism to find ways and means to resolve the problem.

The Governments of Bhutan and Nepal agreed during the 1<sup>st</sup> Ministerial Joint Committee (MJC) held in Kathmandu, in October 1993, to verify and categorize people in the camps into one of the four following categories.

Category 1	Bonafide Bhutanese who were forcefully evicted
Category 2	Bhutanese who emigrated
Category 3	Non-Bhutanese people
Category 4	Bhutanese who committed criminal acts

A Joint Verification Team (JVT), a technical team composed of senior officials from each side was formed following the 10<sup>th</sup> MJC, held in Kathmandu, in December 2000. The JVT was directed to implement the decisions of the MJC on verification, categorization and harmonization.

The agreement reached between the two governments at the 15<sup>th</sup> MJC held in Thimphu in October 2003 agreed that Category 1, 2 and 4 would be repatriated or resettled according to the "harmonized position" of the two governments and the citizenship laws of the two countries. The harmonized position states that Bhutan will take full responsibility for those in Category 1. The people in Category 2 will be given the option to either apply for Bhutanese or Nepali Citizenship according to the laws of the two countries. The people in Category 4 would be given the opportunity to prove their innocence in the court of law.

The 15<sup>th</sup> MJC directed the Joint Verification Team to:

- finalize the categorization of those in Category 3;
- conduct briefings in the camp on the respective terms and conditions of the two governments on each of the categories as applicable.
- to start implementation of the agreed process for implementation of the harmonized position in respect of those in Category 1, 2 and 4.

The JVT was given two and a half months from (1<sup>st</sup> December 2003 to 15<sup>th</sup> February 2004) to complete the process and for voluntary repatriation to start by 16<sup>th</sup> February 2004.



དངུལ་ ཚུལ་ ལྷན་ བཀའ་

གྲོགས་ རམ་ དང་ རྒྱུན་ འགུལ་ འཛིན་ རྒྱུང་ ལས་ འཁུངས་

DEPARTMENT OF AID & DEBT MANAGEMENT  
MINISTRY OF FINANCE  
ROYAL GOVERNMENT OF BHUTAN

As per the directives of the 15<sup>th</sup> MJC, the Bhutanese and Nepalese officials went to Khudunabari Camp on 22 December 2003, to present a briefing on the terms and conditions as presented in point (b) above. While the JVT from the two sides were conducting the briefing, a number of youths forced their way in to the meeting hall, halfway through the briefing session, and physically attacked the Bhutanese members of the JVT. The Bhutanese officials suffered serious injuries and one member even required three stitches on his forehead. The news of the unprovoked assault on the Bhutanese JVT officials and the callous manner in which the Nepalese government handled the affair shocked and angered the Bhutanese public. The Bhutanese people could not understand why anyone wanted to disrupt the final stages of a process that was on the verge of bringing about a resolution to this long and complex problem.

If this incident had not happened, the repatriation process for those eligible and wishing to return to Bhutan would have started on 16<sup>th</sup> February 2004. In the absence of proper security arrangements, the safety of the BVT at stake and in consideration of the trauma, the shock and outcry in Bhutan, the Bhutanese team was forced to leave Nepal on 23 December 2004.

In view of the seriousness of the incident and the public outcry in Bhutan following the incident, the Royal Government has asked the Nepalese Government to conduct a thorough investigation into the incident, identify and take action against the culprits and put in place adequate security measures to enable the consideration of resumption of the process.

Bhutan recently received a report submitted by Nepal on the incident at Khudunabari on 22 December 2003. Preliminary examination of the report indicates serious shortcomings as it does not confirm to our request and contains factual in-accuracies. However, in the larger interest of the bilateral process in finding a resolution of the problem, the Royal Government is examining the report positively. Security for our officials continue to remain of high concern to the Royal Government, given that the overall security and law and order situation in Nepal continues to remain highly fluid. There are also the vested interest groups who would not like to see the closure of the camps and are bent on derailing the bilateral process. The Royal Government of Bhutan is committed to finding a lasting and durable solution through the bilateral process.

We would appreciate if you could incorporate our comments appropriately and rephrase Para 1.5 accordingly.

Best regards,

Sincerely,

  
(Pema Chewang)  
Offg. Director

Cc:

Mr. Tashi Wangyel, PPD, Ministry of Foreign Affairs, Thimphu for information.



**Annex G: Bhutan Country Assistance Evaluation  
Management Action Record**

<i>Recommendations</i>	<i>Management Response</i>
<p>1. <i>Selectivity.</i> The Bank should return to the more selective approach of its earlier assistance strategy. To improve the effectiveness of its lending and policy advice, the Bank should pursue a more integrated approach with upfront sector work and development of a clear sector strategy.</p>	<p>Selectivity is indeed critical for Bank assistance in Bhutan, given limited IDA resources and relative high cost of managing the country program. Accordingly, selectivity will be applied in the new CAS that will be prepared in FY05, especially considering the country's increasing need to borrow from IDA and the results-based orientation of the Bank strategy. Selectivity will also require that the Bank better inform its government counterparts about what we have to offer in terms of lending and non-lending services, while establishing periodic program reviews.</p>
<p>2. <i>Compensating for the lack of field presence.</i> The Bank should compensate for its lack of field presence through annual program consultations with the government, making better use of UNDP facilities to improve coordination with other donors based in Bhutan, and ensuring better staffing continuity.</p>	<p>Recognizing that Bank engagement in Bhutan has been affected by the lack of field presence, we are discussing with UNDP on future arrangements to have access to their facilities, logistical support for Bank missions, and increased coordination with other development partners assisting Bhutan.</p> <p>Ensuring staff continuity has been a challenge due to the small size of the portfolio in each sector, which results in task team leaders being reassigned to larger programs when work pressures demand it. In a broader sense, it is difficult to build a Bhutan country team given that the various TTLs and team members are fully engaged in the larger countries and for the most part have only one activity in Bhutan.</p>
<p>3. <i>Sensitivity to constraints of a small country.</i> The Bank should review its procedures on procurement, reporting, and core economic studies to adapt to Bhutan's capacity constraints.</p>	<p>This is a problem not only in Bhutan, but in general in IDA countries with limited technical and institutional capacity. In small countries, however, the problem is even more acute, and we are considering ways to take full advantage of current Bankwide efforts to use country systems, and to approach the mandated diagnostic work, i.e., PER, CFAA, etc., in a flexible manner, e.g. by consolidating tasks together, or by seeking exemption when justified on substance and small country grounds.</p>



**Annex H: Chairman's Summary**  
**COMMITTEE ON DEVELOPMENT EFFECTIVENESS (CODE)**  
**Bhutan Country Assistance Evaluation**  
**Meeting of September 8, 2004**

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1. The Informal Subcommittee (SC) of the Committee on Development Effectiveness (CODE) met on September 8 to discuss the Bhutan Country Assistance Evaluation (CAE) prepared by the Operations Evaluation Department (OED).

2. **Background.** According to the OED report, the Bank's lending program in Bhutan has been client-driven, carried out in partnership with bilateral agencies, and sensitive to Bhutan's cultural and traditional values. OED's evaluation noted that IDA is a relatively small player in Bhutan, and its strategy has been to give priority to analytical and advisory services, while engaging in selective lending for education, forestry and infrastructure. The Bank has provided some useful analytical work and policy advice over the years, but no formal sector work has been done. The report noted that while the Bank has made important contribution to improving quality and access to education in the country, the outcome of its assistance in forestry has been mixed. According to the OED report, the main lessons from the Bank's experience in Bhutan are: (i) usefulness of co-financing in a small country context; (ii) importance of staffing continuity for effectiveness; and (iii) selectivity and focus are crucial. The report pointed out the difficulty of being a full-service and a knowledge Bank in a small country, and stressed the need to provide advice based on local conditions and to inform a selective lending program, while recognizing that the Government is constrained by the limited time of senior officials to work with the Bank. The OED evaluation concluded that some of lessons from Bhutan experience might be relevant in other small countries or situations when the Bank plays an unaccustomed small role.

3. Management commended OED's sound evaluation of the Bank's engagement in Bhutan and noted that its recommendations will be taken into account during preparation of the results-based country assistance strategy for Bhutan in the next few months. Management noted that despite the overall emphasis on analytical and advisory services, Bhutan has not benefited as it should have from the knowledge resources available at the Bank, mainly due to low implementation capacity, lack of knowledge of what the Bank can provide and availability of alternative resources. Management added that, in response to that challenge, it is going to approach diagnostic work more flexibly to better respond to the needs and capacity of the country, and that it has intensified dialogue with the government to increase its awareness of Bank products and identify emerging opportunities to rely more on country systems.

4. The Chair representing Bhutan welcomed the discussion and thanked OED for a candid and thought-provoking report that contained lessons not only for Bhutan, but also for other small landlocked poor countries, especially on infrastructure development and the knowledge-bank role of the World Bank. He noted that despite recent achievements, the main challenges for Bhutan remain providing employment for growing population and enhancing productivity of the country's limited arable land. The important lesson to be drawn by the Bank is that it is doing business in an increasingly competitive

environment where clients tend to prefer less cumbersome and more cost- and time-effective partnerships. He stressed that the Bank will have to increasingly tailor its product to the needs of the client.

5. **Main Conclusions and Next Steps.** The Subcommittee welcomed the CAE and agreed with the OED rating of the outcome of Bank assistance as moderately satisfactory. They encouraged management to consider the CAE's recommendations when formulating the next country assistance strategy and stressed the importance of drawing lessons from the Bank's experience in Bhutan for future involvement in small countries where the Bank is not the primary lender.

The following points were raised.

6. **Lessons learned.** Members noted that the Bank has operated in a different-than-usual environment in Bhutan - being a marginal lender in a very small country, and stressed that it should adapt better to the country circumstances and show more flexibility, focus and client orientation. Many members emphasized the importance of lessons learned and asked about the implications for Bank assistance in similar situations - being a non-primary lender in a small country, constrained by shortage of staff on the Bank's side and limited administrative capacity of the client. OED replied that it will be preparing a brief "lessons note" on the Bank's work in small countries, looking at: (i) selectivity, especially in the context of coordination with other donor; (ii) types of knowledge products to be delivered by the Bank and the modes of their delivery; and (iii) staff continuity in the resource-constrained environment. Management welcomed the OED initiative and added that in the past, the Small States Task Force has identified the high transaction costs and the limited capacity among the main constraints, and that recent work aimed at reducing transactions costs is covered in a status report which serves as a background document for the upcoming Small States Forum to be held in tandem with the World Bank-IMF Annual Meetings.

7. **Donor coordination.** Many members stressed the importance of better coordination with other donors in order not to crowd out the country's scarce administrative resources and take advantage of the knowledge accumulated by other institutions. Some members were interested in seeing a more explicit approach to co-financing strategy. Questions were raised about the reasons of Bank's secondary role in Bhutan vis-à-vis the ADB. OED explained that this is a result of Bank's conscious strategy in the past of letting other multilateral donors take the lead in small countries. OED added that other major factors are: physical proximity of some of the donors (ADB) and abundance of grant assistance from India. Management concurred with the OED and noted that it is likely that the Bank will remain a small player in the country, relative to other donors.

8. **Bank's program.** Some members were interested in the reasons for the limited role of the Bank in Bhutan - whether it was the large share of grants from other donors, or the availability of more attractive alternative sources. In that context, some members asked about the future of the Bank's program, noting that the Bank does not necessarily have to play the leading role, but be a better complementary player. Management replied

that the situation has changed in terms of Bhutan's demand for IDA funds, and the authorities have recently expressed interest in the full envelope of IDA loans. Management added that Bank's program would focus on education and infrastructure, with a limited number of AAA products. Several members stressed the need to include statistical capacity building. Management replied that while the Bank is not engaged in a full-fledged capacity building activity in Bhutan, it is providing necessary assistance on an ad hoc basis in selected areas. A speaker asked whether the comprehensive development framework for Bhutan should be oriented to reducing the ratio of gross capital formation to GDP growth in order to stimulate growth and increase employment. OED replied that the relatively high ratio reflects the capital intensity of the hydropower sector, and the lumpiness of investment, as well as the fact that the revenues from the power sector are often used for long-term social investments.

9. **AAA.** Members generally agreed with OED on the need to improve the selectivity of the Bank's analytical products and noted the importance of raising client awareness of their usefulness and potential benefits. They noted the mixed results of AAA work in Bhutan and asked whether the evaluation of the AAA products could have been more quantitative. Some members felt that the overall conclusion of the OED assessment of inadequacy of sector work vis-à-vis lending program could have been substantiated by more analysis, and brought up the example of the successful program in education that was not preceded by analytical work. OED replied that many of the problems in other sectors do reflect inadequate sector work, and noted that because the education projects were directed at expanding physical capacity, the lack of prior sector work was less significant.

Chander Mohan Vasudev  
Chairman



**STATISTICAL TABLES**

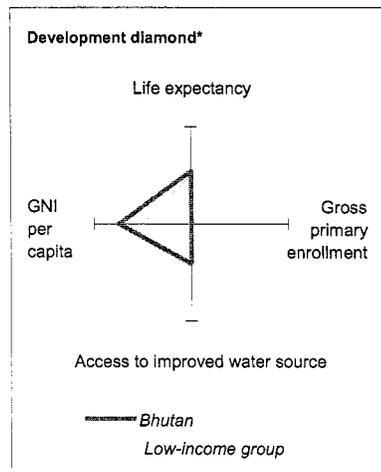


# Bhutan at a glance

9/30/04

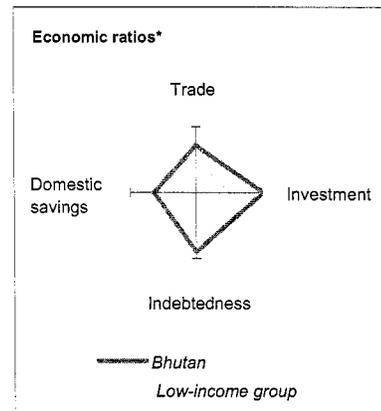
## POVERTY and SOCIAL

	Bhutan	South Asia	Low-income
<b>2003</b>			
Population, mid-year (millions)	0.87	1,425	2,310
GNI per capita (Atlas method, US\$)	670	510	450
GNI (Atlas method, US\$ billions)	0.59	726	1,038
<b>Average annual growth, 1997-03</b>			
Population (%)	2.8	1.8	1.9
Labor force (%)	2.6	2.3	2.3
<b>Most recent estimate (latest year available, 1997-03)</b>			
Poverty (% of population below national poverty line)	..	..	..
Urban population (% of total population)	9	28	30
Life expectancy at birth (years)	63	63	58
Infant mortality (per 1,000 live births)	74	68	82
Child malnutrition (% of children under 5)	19	48	44
Access to an improved water source (% of population)	62	84	75
Illiteracy (% of population age 15+)	..	41	39
Gross primary enrollment (% of school-age population)	..	95	92
Male	..	103	99
Female	..	88	85



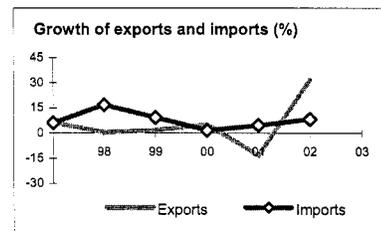
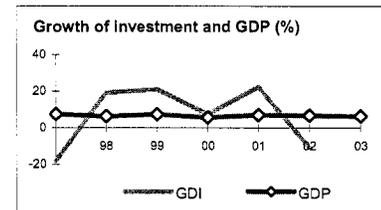
## KEY ECONOMIC RATIOS and LONG-TERM TRENDS

	1983	1993	2002	2003
GDP (US\$ billions)	0.18	0.24	0.60	0.71
Gross domestic investment/GDP	39.8	46.1	40.0	..
Exports of goods and services/GDP	12.7	31.5	28.4	..
Gross domestic savings/GDP	8.4	33.6	24.6	..
Gross national savings/GDP	..	..	26.9	..
Current account balance/GDP	-42.6	-29.8	-6.9	-3.0
Interest payments/GDP	0.0	1.0	0.3	0.3
Total debt/GDP	1.0	41.0	62.6	59.5
Total debt service/exports	0.0	7.8	4.6	4.7
Present value of debt/GDP	..	..	57.6	..
Present value of debt/exports	..	..	250.6	..
	<b>1983-93</b>	<b>1993-03</b>	<b>2002</b>	<b>2003</b>
(average annual growth)				
GDP	6.5	6.7	6.7	6.5
GDP per capita	4.1	3.6	3.8	3.7
Exports of goods and services	18.0	4.5	31.6	..



## STRUCTURE of the ECONOMY

	1983	1993	2002	2003
(% of GDP)				
Agriculture	53.3	40.0	33.7	33.2
Industry	25.5	39.7	39.4	39.5
Manufacturing	5.5	10.7	7.3	7.7
Services	21.2	20.3	26.9	27.3
Private consumption	66.8	49.2	54.4	..
General government consumption	24.8	17.3	21.0	..
Imports of goods and services	44.1	44.0	43.7	..
	<b>1983-93</b>	<b>1993-03</b>	<b>2002</b>	<b>2003</b>
(average annual growth)				
Agriculture	3.2	4.0	2.5	4.2
Industry	10.4	8.2	11.1	7.3
Manufacturing	14.9	3.7	4.9	2.1
Services	8.2	7.8	4.5	7.9
Private consumption	3.4	9.9	5.5	..
General government consumption	2.8	8.2	9.7	..
Gross domestic investment	7.5	6.1	-10.7	..
Imports of goods and services	6.7	8.1	8.3	..

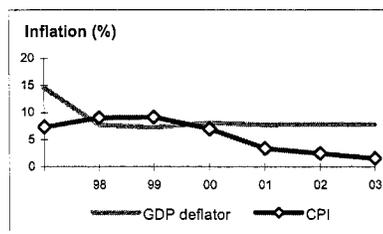


Note: 2003 data are preliminary estimates.

\* The diamonds show four key indicators in the country (in bold) compared with its income-group average. If data are missing, the diamond will be incomplete.

## PRICES and GOVERNMENT FINANCE

	1983	1993	2002	2003
<b>Domestic prices</b> (% change)				
Consumer prices	..	13.6	2.5	1.6
Implicit GDP deflator	8.8	6.7	7.8	7.8
<b>Government finance</b> (% of GDP, includes current grants)				
Current revenue	..	23.0	30.3	25.2
Current budget balance	..	5.7	15.0	10.6
Overall surplus/deficit	..	-12.8	-4.2	-8.3



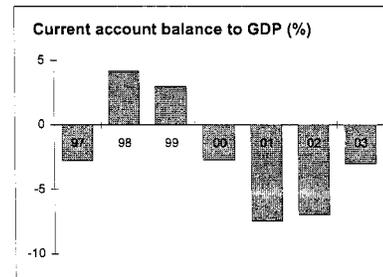
## TRADE

	1983	1993	2002	2003
(US\$ millions)				
Total exports (fob)	16	66	98	113
Agricultural products	..	12	14	15
Electricity	..	19	49	55
Manufactures	..	..	..	..
Total imports (cif)	66	125	188	189
Food	..	31	53	72
Fuel and energy	..	10	25	36
Capital goods	..	..	..	..
Export price index (1995=100)	38	82	177	..
Import price index (1995=100)	38	82	177	..
Terms of trade (1995=100)	100	100	100	..



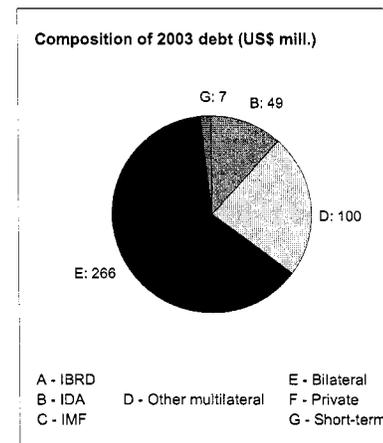
## BALANCE of PAYMENTS

	1983	1993	2002	2003
(US\$ millions)				
Exports of goods and services	31	92	130	139
Imports of goods and services	107	162	228	231
Resource balance	-76	-70	-99	-92
Net income	0	0	-25	-13
Net current transfers	0	0	82	84
Current account balance	-76	-70	-42	-21
Financing items (net)	74	84	62	81
Changes in net reserves	2	-14	-20	-59
<b>Memo:</b>				
Reserves including gold (US\$ millions)	..	94	317	376
Conversion rate (DEC, local/US\$)	10.1	30.5	48.2	47.1



## EXTERNAL DEBT and RESOURCE FLOWS

	1983	1993	2002	2003
(US\$ millions)				
Total debt outstanding and disbursed	2	97	378	422
IBRD	0	0	0	0
IDA	0	19	39	49
Total debt service	0	7	6	7
IBRD	0	0	0	0
IDA	0	0	1	1
Composition of net resource flows				
Official grants	5	35	32	..
Official creditors	1	9	93	22
Private creditors	0	-2	0	0
Foreign direct investment	0	0	0	..
Portfolio equity	0	0	0	..
World Bank program				
Commitments	0	5	0	31
Disbursements	0	1	6	7
Principal repayments	0	0	0	0
Net flows	0	1	5	7
Interest payments	0	0	0	0
Net transfers	0	1	5	6



Annex Table 2: Bhutan - Economic and Social Indicators, 1992-2002

Series Name	BHUTAN											AVERAGE 1992-2002						
	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	Bhutan	Banglad- esh	India	Nepal	South Asia	Low income	Middle income
	GDP growth (annual %)	4.3	5.9	8.1	6.8	5.5	7.8	7.1	7.0	7.0	7.0	7.7	6.7	4.9	5.8	4.4	5.4	4.3
GNI per capita, Atlas method (current US\$)	390	360	380	380	410	460	450	470	510	560	590	450.9	344.5	403.6	227.3	401.8	406.4	1,701.8
GNI per capita, PPP (current international \$)	..	..	..	..	..	..	..	..	..	..	..	..	1,391.8	2,028.2	1,186.4	1,921.8	1,698.2	4,540.9
GDP per capita growth (annual %)	1.3	2.8	5.0	3.7	2.4	4.7	4.0	3.9	3.9	4.0	4.8	3.7	3.1	4.0	1.9	3.5	2.3	2.2
Agriculture, value added (% of GDP)	39.8	40.0	42.0	40.6	39.8	38.4	37.7	35.8	36.7	35.4	33.9	38.2	24.8	27.7	41.6	27.2	26.7	11.0
Industry, value added (% of GDP)	28.9	29.0	29.6	34.0	33.8	35.9	34.3	35.2	34.3	36.2	37.4	33.5	24.0	26.7	22.1	26.1	30.2	36.4
Services, etc., value added (% of GDP)	31.3	31.0	28.4	25.4	26.4	25.7	28.1	29.1	29.0	28.4	28.8	28.3	51.2	45.6	36.3	46.7	43.1	52.6
Exports of goods and services (% of GDP)	32.7	31.5	29.5	37.2	33.8	32.9	31.0	29.8	27.4	23.2	..	30.9	11.8	11.5	21.9	13.1	21.8	25.4
Imports of goods and services (% of GDP)	57.2	44.0	39.4	42.0	43.5	42.3	46.2	47.8	48.2	43.4	..	45.4	17.4	12.5	31.9	14.9	23.1	25.1
Current account balance (% of GDP)	-10.1	-29.8	-14.8	-11.1	12.9	5.5	4.2	3.0	-2.8	-7.6	-7.0	-5.2	-1.1	-0.8	-2.1	0.0	0.0	0.0
Total debt service (% of exports of goods and services)	6.9	7.8	9.0	10.9	6.1	6.1	7.2	5.4	4.7	4.2	..	6.8	11.3	21.3	6.9	19.4	19.9	17.9
External debt (% of GNI)	41.1	45.6	41.7	39.2	38.1	32.5	49.3	49.2	47.9	56.3	..	44.1	37.1	26.7	52.0	31.8	57.0	36.1
Gross international reserves in months of imports	8.5	..	10.6	11.3	17.2	14.7	16.9	17.1	13.7	12.5	14.7	13.7	3.6	5.9	6.0	5.6	4.9	6.4
Current revenue, excluding grants (% of GDP)	17.5	20.2	18.4	18.0	17.4	16.3	18.4	18.6	20.8	19.7	..	18.5	9.3	12.3	10.1	13.1	14.9	67.7
Expenditure, total (% of GDP)	33.7	33.3	34.0	36.7	35.3	31.9	27.6	38.0	38.3	43.0	..	35.2	12.7	15.6	16.7	17.0	17.6	70.2
Overall budget balance, excluding capital grants (% of GDP)	..	..	..	..	..	..	..	..	..	..	..	..	-3.1	-5.4	-6.1	0.0	0.0	0.0
Gross domestic savings (% of GDP)	25.6	37.0	45.0	43.9	35.1	24.3	22.3	25.0	25.7	27.9	..	31.2	15.1	21.9	13.8	20.3	20.6	25.3
Inflation, consumer prices (annual %)	16.0	11.2	7.0	9.5	8.8	6.5	10.6	6.8	..	..	..	9.5	4.7	7.7	7.2	0.0	0.0	0.0
Illiteracy rate, adult total (% of people ages 15 and above)	..	..	..	..	..	..	..	..	..	..	..	..	61.7	45.1	61.7	47.7	41.3	14.9
Immunization, DPT (% of children under 12 months)	86.0	79.0	86.0	87.0	86.0	87.0	86.0	88.0	..	88.0	..	85.9	76.1	62.2	63.7	61.1	59.7	88.3
Improved water source (% of population with access)	..	..	..	..	..	..	..	..	62.0	..	..	62.0	97.0	84.0	88.0	84.4	75.6	81.9
Life expectancy at birth, total (years)	57.7	..	..	59.5	..	60.7	..	..	62.2	62.7	63.2	61.0	59.8	62.1	57.7	61.6	58.4	69.2
Mortality rate, infant (per 1,000 live births)	75.0	..	..	67.8	..	63.0	..	..	57.6	74.0	..	67.5	66.8	72.1	79.4	73.7	83.7	33.6
Improved sanitation facilities (% of population with access)	..	..	..	..	..	..	..	..	70.0	..	..	70.0	48.0	28.0	28.0	34.0	42.5	59.9
School enrollment, preprimary (% gross)	..	..	..	..	..	..	..	..	..	..	..	..	57.6	7.0	3.2	13.7	15.1	37.2
School enrollment, primary (% gross)	..	..	..	..	..	..	..	..	..	..	..	..	85.8	100.3	112.6	95.4	91.8	110.7
School enrollment, secondary (% gross)	..	..	..	..	..	..	..	..	..	..	..	..	28.6	47.8	43.3	44.1	38.9	65.7
Population, total (in million)	0.6	0.7	0.7	0.7	0.7	0.7	0.8	0.8	0.8	0.8	0.9	0.7	124.6	965.6	21.5	1,283.0	2,273.8	2,607.7
Population growth (annual %)	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.8	2.7	2.6	2.9	1.7	1.7	2.4	1.9	2.0	1.1
Urban population (% of total)	5.5	5.7	5.8	6.0	6.2	6.5	6.7	6.9	7.1	7.4	7.6	6.5	23.4	27.0	10.9	26.7	28.5	49.4
Gross capital formation (% of GDP)	50.0	49.5	54.9	48.7	44.8	33.7	37.6	43.0	46.5	48.1	..	45.7	20.7	22.8	23.8	22.1	21.9	25.0

Source: WB SIMA database as of March 23, 2004

### Annex Table 3: Bhutan - Development Assistance and World Bank Lending

Table 3a: Total Receipts Net (OOA+OOF+Private), 1992-2001 (USD million)

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	Total
JAPAN	11.9	20.6	27.5	19.2	12.7	16.2	7.6	17.8	7.1	11.8	152.4
DAC DONORS	21.6	51.5	55	61.5	41.8	79.5	38.5	50.9	24.3	41.4	466
AS. D B	-	-	-	-	-	-	-	-	-	-	-
AS. D B SPECIAL FUNDS	3.2	3.4	2.7	3.8	2.4	6.7	3.8	1.5	6.3	6.2	40
EC	5.8	3.4	2.8	1.7	4.8	3.5	2.8	3.5	0.9	1.6	30.8
UNDP	4.9	4.3	3	1.6	2.4	3	3.1	3.9	3.4	1.4	31
TOTAL MULTILATERAL	22.5	20.9	16.1	16.2	15.8	24.7	16	14.7	20	18	184.9
TOTAL DONORS	42.7	72.4	71.3	78.2	57.8	103.9	53.3	64.7	43.9	58.1	646.3
IBRD	-	-	-	-	-	-	-	-	-	-	-
IDA	0.6	0.9	1.3	1.1	1.2	0.9	0.5	0.7	3.3	5.7	16.2
IDA as a % of Multilateral Assistance	3%	4%	8%	7%	8%	4%	3%	5%	17%	32%	9%
IDA as a % of Total Assistance	1%	1%	2%	1%	2%	1%	1%	1%	8%	10%	3%

Source: OECD Database 2003

Table 3b: World Bank (IDA) Lending by Sectors, 1992-2004 (USD million)

	1994	1998	2000	2004	Total
Education		13.7		31.0	44.7
EDUCATION II		13.7		31.0	13.7
Education Development Project					31.0
Rural Sector	5.4				5.4
Third Forestry Development Project	5.4				5.4
Transport			11.6		11.6
RURAL ACCESS ROAD			11.6		11.6
Urban Development			10.8		10.8
URBAN DEVELOPMENT PROJECT			10.8		10.8
Overall Result					72.5

Source: Business Warehouse as of March 23, 2004

Annex Table 4: Bhutan - A Selected list of Analytical and Advisory Work, 1992-2004

Document Title	Date	Report No
<b>Country Assistance Strategy Document</b>		
Bhutan - Country assistance strategy Vol. 1 (English)	2/22/2000	20158
Bhutan - Country assistance strategy public information notice (CPIN) Vol. 1 (English)	8/29/2000	PIN40
<b>Economic Report</b>		
Bhutan - Country economic memorandum Vol. 1 (English)	12/20/1996	16113
Bhutan - Country economic memorandum : 1995 Vol. 1 (English)	11/29/1994	13495
<b>Environmental Action Plan</b>		
Bhutan - Seventh five year plan 1992-1997 : vol 1 main plan document Vol. 1 (English)	12/31/1991	E7

Source: World Bank Imagebank as of March 23, 2004

**Annex Table 5: Bhutan - OED and QAG Ratings****Table 5a: OED Ratings, Exit FY 1992-2004 (In USD million)**

Country	Total Evaluated (\$M)	Outcome % Sat (\$)	Inst Dev Impact % Subst (\$)	Sustainability % Likely (\$)	Total Evaluated (No)	Outcome % Sat (No)	Inst Dev Impact % Subst (No)	Sustainability % Likely (No)
<b>Bhutan</b>	<b>16</b>	<b>67</b>	<b>39</b>	<b>42</b>	<b>5</b>	<b>80</b>	<b>60</b>	<b>50</b>
Bangladesh	3,668	82	29	61	55	75	24	48
India	22,861	74	41	65	151	71	44	59
Nepal	835	80	25	45	33	66	28	38
SAR	36,491	74	34	62	364	71	34	53
<b>The World Bank</b>	<b>226,949</b>	<b>77</b>	<b>43</b>	<b>66</b>	<b>3,000</b>	<b>71</b>	<b>39</b>	<b>56</b>

Source: Business Warehouse as of March 23, 2004

**Table 5b: QAG Ratings**

Data as of: 3/21/2004

Country	Number of Projects	Net Commitment Amt	Number of Projects at Risk	% At Risk	Commitment At Risk	% Commitment at Risk
<b>Bhutan</b>	<b>4</b>	<b>67</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
Bangladesh	24	2,186	5	21	585	27
India	65	12,693	7	11	1,118	9
Nepal	8	333	2	25	130	39
SAR	126	17,127	22	17	2,927	17
<b>The World Bank</b>	<b>1,354</b>	<b>94,444</b>	<b>267</b>	<b>20</b>	<b>17,722</b>	<b>19</b>

Source: Business Warehouse as of March 23, 2004

Annex Table 6: Bhutan - Millennium Development Goals

	1990	1995	2001	2002
<b>1. Eradicate extreme poverty and hunger</b>	<i>5 target = halve 1990 \$1 a day poverty and malnutrition rate</i>			
Population below \$1 a day (%)	..	..	..	..
Poverty gap at \$1 a day (%)	..	..	..	..
Percentage share of income or consumption held by poorest 20%	..	..	..	..
Prevalence of child malnutrition (% of children under 5)	37.9	..	18.7	..
Population below minimum level of dietary energy consumption (%)	..	..	..	..
<b>2. Achieve universal primary education</b>	<i>2015 target = net enrollment to 100</i>			
Net primary enrollment ratio (% of relevant age group)	..	..	..	..
Percentage of cohort reaching grade 5 (%)	..	82.1	90.4	..
Youth literacy rate (% ages 15-24)	..	..	..	..
<b>3. Promote gender equality</b>	<i>2005 target = education ratio to 100</i>			
Ratio of girls to boys in primary and secondary education (%)	..	..	..	..
Ratio of young literate females to males (% ages 15-24)	..	..	..	..
Share of women employed in the nonagricultural sector (%)	..	..	..	..
Proportion of seats held by women in national parliament (%)	2	2	9	9
<b>4. Reduce child mortality</b>	<i>2015 target = reduce 1990 under 5 mortality by two-thirds</i>			
Under 5 mortality rate (per 1,000)	166	133	95	..
Infant mortality rate (per 1,000 live births)	75	67.8	74	54
Immunization, measles (% of children under 12 months)	93	85	78	..
<b>5. Improve maternal health</b>	<i>2015 target = reduce 1990 maternal mortality by three-fourths</i>			
Maternal mortality ratio (modeled estimate, per 100,000 live births)	..	500	..	..
Births attended by skilled health staff (% of total)	..	14.9	..	..
<b>6. Combat HIV/AIDS, malaria and other diseases</b>	<i>2015 target = halt, and begin to reverse, AIDS, etc.</i>			
Prevalence of HIV, female (% ages 15-24)	..	..	..	..
Contraceptive prevalence rate (% of women ages 15-49)	..	18.8	30.7	..
Number of children orphaned by HIV/AIDS	..	..	..	..
Incidence of tuberculosis (per 100,000 people)	..	..	136.5	..
Tuberculosis cases detected under DOTS (%)	..	29	27	..
<b>7. Ensure environmental sustainability</b>	<i>2015 target = various (see notes)</i>			
Forest area (% of total land area)	64.2	..	64.2	..
Nationally protected areas (% of total land area)	..	21.3	21.2	25.1
GDP per unit of energy use (PPP \$ per kg oil equivalent)	..	..	..	..
CO2 emissions (metric tons per capita)	0.2	0.4	0.5	..
Access to an improved water source (% of population)	..	..	62	..
Access to improved sanitation (% of population)	..	..	70	..
Access to secure tenure (% of population)	..	..	..	..
<b>8. Develop a Global Partnership for Development</b>	<i>2015 target = various (see notes)</i>			
Youth unemployment rate (% of total labor force ages 15-24)	..	..	..	..
Fixed line and mobile telephones (per 1,000 people)	..	..	..	..
Personal computers (per 1,000 people)	..	..	5.8	..
<b>General indicators</b>				
Population	600.1 thousand	695.1 thousand	828.0 thousand	850.8 thousand
Gross national income (\$)	292.3 million	265.1 million	460.3 million	505.2 million
GNI per capita (\$)	490	380	560	590
Adult literacy rate (% of people ages 15 and over)	..	..	..	..
Total fertility rate (births per woman)	5.9	5.8	5.2	5.1
Life expectancy at birth (years)	57.7	59.5	62.7	63.2
Aid (% of GNI)	17.6	26.6	12.6	..
External debt (% of GNI)	31.4	39.2	56.3	..
Investment (% of GDP)	36.1	48.7	48.1	..
Trade (% of GDP)	60.5	79.3	66.5	..

Source: World Development Indicators database, April 2002.

Note: In some cases the data are for earlier or later years than those stated.

Goal 1 targets: Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day. Halve, between 1990 and 2015, the proportion of people who suffer from hunger.

Goal 2 target: Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling.

Goal 4 target: Reduce by two-thirds, between 1990 and 2015, the under-five mortality rate.

Goal 5 target: Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.

Goal 6 targets: Have halted by 2015, and begun to reverse, the spread of HIV/AIDS. Have halted by 2015, and begun to reverse, the incidence of malaria and other major diseases.

Goal 7 targets: Integrate the principles of sustainable development into country policies and programs and reverse the loss of environmental resources. Halve, by 2015, the proportion of people without sustainable access to safe drinking water. By 2020, to have achieved a significant improvement in the lives of at least 100 million slum dwellers.

Goal 8 targets: Develop further an open, rule-based, predictable, non-discriminatory trading and financial system. Address the Special Needs of the Least Developed Countries. Address the Special Needs of landlocked countries and small island developing states. Deal comprehensively with the debt problems of developing countries through national and international measures in order to make debt sustainable in the long term. In cooperation with developing countries, develop and implement strategies for decent and productive work for youth. In cooperation with pharmaceutical companies, provide access to affordable, essential drugs in developing countries. In cooperation with the private sector, make available the benefits of new technologies, especially information and communications.





