I. Project Context

Country Context

Bhutan’s ability to increase Gross National Happiness (GNH) is highly dependent on the performance of its Renewable Natural Resources Sector (RNR), of which agriculture is a major component. Food security, employment, export earnings, poverty reduction, and the welfare of rural people are all heavily influenced by RNR sector growth and development. Driven by its secondary and tertiary sectors, particularly hydroelectric power, Bhutan’s economy is rapidly growing. Annual average GDP growth averaged about 9% in real terms from 2000-2008. During the same period, per capita GDP rose from USD749 to USD1,800, and the poverty rate fell from 36% in 2000 to 23.2% in 2007. Further growth and poverty reduction are now being sought under the Tenth Five-Year Plan (FYP) for National Development (2008-2013) through the development of industry and infrastructure, continued emphasis on balanced regional development, and measures to boost private sector activity. The underlying objectives of the Tenth FYP are to: continue growth of 9% per annum and further reduce the poverty rate to 15%. Bhutan’s RNR sector, however, is growing slowly, despite its potential for high-value fruit and vegetable production and exports; proximity to large, readily accessible export markets; and extensive support from government institutions. Annual sector growth averaged 2.2% in real terms during the period 2000-2009, and its share of GDP fell from 27% to 19%. This slower progress is a concern given that rural areas account for 65% of total employment and 98% of Bhutan’s poor (based on 2007 data).
Bhutan is on track to achieve its Millennium Development Goals, although the mid-term report notes worsening of conditions affecting those suffering from severe poverty. Several indicators in the report underline the poverty challenge that confronts Bhutan. It also points out that household food security is linked to low food production and weak agricultural productivity, limited access to land and other productive assets, extensive crop destruction by wildlife and pests, inadequate opportunities for rural employment, poor food utilization, and weak access to road and transport infrastructure.

Bhutan's mountainous terrain is a fundamental constraint to growth and rural poverty reduction. Poor road access isolates a large proportion of rural people from markets and social services, and limits their livelihood to subsistence agriculture. The Royal Government of Bhutan (RGoB) and donors have responded to this constraint by constructing over 1,500 kilometers of farm roads and tracks since 2003. The proportion of rural people within 1 hour walking distance of a road head increased from 40.2% in 2000 to 53.0% in 2008 as a result; the proportion within 6 hours walking distance increased from 83.5% to 90.0% (Agricultural Census 2009). Most of the areas that reaped the benefits of improved access were in the central highlands, leaving out the more remote areas in the south and south-west, where there are high poverty rates and a large number of poor people out of mainstream development. Poverty rates currently are the highest in the Zhemgang, Samtse, Mongar, and Lhuntse dzongkhags (districts).

II. Sectoral and Institutional Context

Average annual growth in RNR GDP during the period 2000-2009 was 1.4%, 1.35% for crop GDP, 1.8% for livestock GDP, and 1% for forestry GDP. Citrus and potatoes have been the main sources of crop sector growth due to their high growth rates and high contribution to crop sector GDP. The high-value fruit and vegetable crops that dominate commercial agriculture and agricultural exports have also demonstrated strong growth. In contrast, the real value-added of maize, paddy, wheat, and barley the main food staples has declined substantially. As the rural road network expands, it is likely that this divergence in the growth trajectories of cereal crops versus fruit and vegetable production will widen. More farmers will have access to markets for fruit and vegetables, and low price rice imports will penetrate deeper into the rural areas. Equally importantly, these results highlight the need to resolve the serious disease problems that currently threaten key cash crops such as citrus and cardamom. Unless the advance of these diseases is halted, Bhutan will lose the most important drivers of agriculture sector growth.

Recent trends in agriculture productivity reflect low levels of technology adoption; inadequate capacity to deal with crop diseases; poor management of land, water, and forest resources; and the predominance of subsistence agriculture, particularly in the more remote areas. Bhutan’s small, dispersed rural population, mountainous terrain, and subsistence-oriented farming systems render the development of competitive production and marketing systems difficult. At the domestic level, market infrastructure and wholesale systems are largely absent. Although the Tenth Five Year Plan recognizes the need to address this constraint, it continues to rely on the marketing activities of public agencies such as the Food Corporation of Bhutan. Private sector activity is weak, and dominated by foreign buyers and assemblers. Recent RGoB initiatives to promote farmer cooperatives and contract farming have not yet had an impact. Labor productivity has increased modestly, as measured by real GDP per capita of the rural population. Low rates of technology use and adoption, and low consequent productivity strongly suggest that improved connectivity is a necessary but insufficient condition for agriculture sector development. It also appears that resource poor farmers receive a small share of the benefits of improved connectivity as measured by growth...
in agriculture productivity and sales.

The Ministry of Agriculture and Forests (MoAF) proposed a geographic focus for assistance programs in the country’s more remote areas, especially those having least benefited from past or on-going RGoB and donor-funded programs. These areas are home to the poorest and most vulnerable households in the country (Agricultural Census 2009). In these areas, the most important constraints to agriculture and natural resource productivity include: (i) difficult access due to the absence or inadequacy of the road and transportation network; (ii) underutilization of land resources with a high proportion of land left fallow; (iii) very limited irrigation infrastructure in spite of available spring and river water sources; (iv) nonexistent links to marketing facilities and infrastructure; (v) fragmented and largely low-productivity subsistence farming systems; (vi) significant food and nutrition insecurity issues; (vi) high pre-harvest losses due to wildlife-related crop damage, pests, and diseases and (v) high post harvest losses due to lack of storage and processing facilities.

For over two decades, the RGoB has been strongly supporting a decentralized policy to stimulate capacity for self-governance and self-action, and thus reduce the reliance on the central government. The recent transition to a Constitutional Democracy placed greater urgency on decentralization as a means to alleviate poverty. Responsibility for planning and implementing development activities now lies with the dzongkhags. Under the present administrative system, applications for investment support are initiated and prepared at the geog (sub-district) level and submitted to the dzongkhag for screening. If approved, the responsibility for implementation remains with the dzongkhag or is delegated to the geog. The MoAF has invested substantially in the physical infrastructure and human resources needed to ensure that Bhutan’s farmers have reasonable access to extension services. An RNR center has been established in each of the 205 geogs, and most are staffed with one extension agent (EA) per sector who operates under dzongkhag-level sector coordinators. These agents are the frontline for implementing MoAF development programs, and district RNR plans in farming communities, including oversight over construction of farm roads.

In 2008, a comprehensive review of the rural road program led to critical changes that rationalized the basis for financing road maintenance under the decentralized system. Responsibility for maintenance now lies with the dzongkhag or gewog during the first two years after construction. Routine maintenance that can be performed with hand tools and labor is then transferred to community Road User Groups, but responsibility for all other maintenance remains with the dzongkhag or gewog. The decision to allocate more of the maintenance responsibilities to local government is expected to result in better road maintenance, with higher social and economic returns. The draft Eleventh FYP reinforces this policy by containing a provision to provide financial support to user groups for the maintenance of farm roads.

The proposed project is designed to improve living conditions and incomes in the country’s poorest and most remote rural areas. The populations in these areas currently rely on subsistence agriculture, and lack roads, irrigation, technologies, and community and social infrastructure that would allow them to improve their incomes and social integration. The Bank has a comparative advantage in supporting this investment because it builds on the lessons learned from over three decade of lending to the rural development sector in all regions, and the successful experience of two ongoing operations in Bhutan scheduled to close within the next two years. The Decentralized Rural Development Project initially financed rural infrastructure such as road, bridges and irrigation and agricultural extension services. Activities under the additional financing grant are focused on
the improving rural infrastructure (primarily irrigation) and addressing production constraints in maize, potato and rice. The Sustainable Land Management Project finances improvements in agricultural technologies and community infrastructure, but does not finance critical road construction. In contrast to these earlier investments, the proposed project will provide comprehensive livelihoods support to areas that are more remote and have higher concentrations of poverty.

III. Project Development Objectives
The project development objective is to increase agriculture productivity and access to community assets in remote rural areas by improving access to markets, irrigation, agricultural technologies and community infrastructure.

IV. Project Description
Component Name
Rural Infrastructure. The focus of this component is to connect the communities to larger roads and regional markets and to improve production potential through improved availability of irrigation. Community, Marketing and Productive Infrastructure. This component will finance marketing and post-harvest infrastructure, community-level infrastructure, and investments identified by producers Project Management and Institutional Strengthening. This component supports project management, including the monitoring and evaluation functions of the project.

V. Financing (in USD Million)

<table>
<thead>
<tr>
<th>For Loans/Credits/Others</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>BORROWER/RECIPIENT</td>
<td>0.00</td>
</tr>
<tr>
<td>International Development Association (IDA)</td>
<td>9.00</td>
</tr>
<tr>
<td>Total</td>
<td>9.00</td>
</tr>
</tbody>
</table>

VI. Implementation
At national level: overall implementation of the project will be coordinated by the MoAF. The MoAF will provide oversight, technical support and guidance to dzongkhag and geog RNR staff, who will guide implementation of project activities on a day-to-day basis. A dedicated Project Director, appointed by MoAF, will be assisted by part-time Component Coordinators, who will be senior MoAF technical staff drawn from Departments of Agriculture, Livestock, Forestry, Marketing and Policy and Planning within the MoAF as well as technical staff from other agencies under MoAF that are relevant to the implementation of specific components and activities of the project. These part-time Component Coordinators will be individually responsible for overseeing and guiding the implementation of specific components or sub-components of the project. The Project Director and Component Coordinators will form the Project Management Team (PMT).

Given the multi-sectoral and multi-level nature of the project, a Project Steering Committee (PSC) will be established to facilitate cross-sectoral coordination and to improve institutional mandates in support of the many inter-related activities of the project. The PSC will be chaired by the Secretary of MoAF and include representatives of the MoAF’s Departments of Agriculture, Livestock, Forestry, Marketing, Policy and Planning, the Ministry of Finance, the Gross National Happiness Commission (GNHC), and other relevant agencies necessary for the coordination of the project activities. The PSC will provide policy guidance, support the alignment between project activities and the respective national sectoral plans and programs of the government, help coordinate with the
Department of Budget and Accounts (DBA) on matters relating to fund flow and project accounting, and facilitate coordination with the Royal Audit Authority (RAA) on program audits.

Local government level. The dzongkhag administration will be responsible, in particular for implementation of farm road and irrigation related activities. Geog administration will be responsible for implementation of rehabilitation of productive assets of existing groups and establishment of community infrastructure. It will also liaise with other government and private sector agencies involved in order to facilitate program implementation and to enable the access to technical support and financial resources from other on-going projects and programs. The geog administration will ensure that appropriate technical guidance is provided through the geog RNR staff or through dzongkhag staff (e.g. engineering support) for specific activities.

At the chiog level, mobilization and organization of communities and selection of priority community investments or activities would be undertaken by a small team consisting of geog RNR staff, Tshogpa (village head) and supplemented by additional contractual or seconded staff, if needed. This team would co-opt technical staff from other government institutions and private sector institutions for supporting specific project activity as needed. In order to facilitate the management of irrigation schemes, WUAs will be established or existing associations will be strengthened. This will entail training and capacity building related to water management and maintenance of irrigation systems, and will address the institutional issues related to registration, elections, and financial management.

VII. Safeguard Policies (including public consultation)

<table>
<thead>
<tr>
<th>Safeguard Policies Triggered by the Project</th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>Environmental Assessment OP/BP 4.01</td>
<td>✗</td>
<td></td>
</tr>
<tr>
<td>Natural Habitats OP/BP 4.04</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Forests OP/BP 4.36</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Pest Management OP 4.09</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Physical Cultural Resources OP/BP 4.11</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Indigenous Peoples OP/BP 4.10</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Involuntary Resettlement OP/BP 4.12</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Safety of Dams OP/BP 4.37</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Projects on International Waterways OP/BP 7.50</td>
<td></td>
<td>✗</td>
</tr>
<tr>
<td>Projects in Disputed Areas OP/BP 7.60</td>
<td></td>
<td>✗</td>
</tr>
</tbody>
</table>

VIII. Contact point

**World Bank**
Contact: Winston Dawes
Title: Senior Rural Development Specialist
Tel: 458-9202
Email: wdawes@worldbank.org

**Borrower/Client/Recipient**
Name: Ministry of Finance
Contact: Nim Dorji
Title: Joint Secretary
Implementing Agencies
Name: Ministry of Agriculture and Forests
Contact: Department of Agriculture
Title:
Tel: (975-2) 322-545
Email:

IX. For more information contact:
The InfoShop
The World Bank
1818 H Street, NW
Washington, D.C. 20433
Telephone: (202) 458-4500
Fax: (202) 522-1500
Web: http://www.worldbank.org/infoshop