This letter of Development Policy lays out the key elements of the proposed Policy and Institutional Reform Program of the Royal Government of Bhutan’s (RGoB) over the next three years. The RGoB requests the assistance of the World Bank Group in the form of the Development Policy Financing (DPF) instrument for US$30 million. This financing will be used to support the reform areas articulated in the 12th Five-Year Plan (FYP) 2018-2023. The main objective of the 12th FYP is “just, harmonious and sustainable society through enhanced decentralization”. The assistance from the World Bank Group is needed to especially support the RGoB’s efforts to improve fiscal sustainability and to strengthen private sector employment opportunities in the country.

The RGoB would like to thank the International Development Association for providing extensive support through the DPF instrument in the past. Starting with a Development Policy Grant in FY2006, Bhutan has benefited from the use of the DPF instrument in FY2007, FY2009, FY2012, FY2016 and FY2018. All these operations have helped deepen Policy and Institutional Reforms in the country and were deeply embedded in our respective Five-Year Plans as well. As a result, Bhutan made significant progress to achieve the MDGs and reduce poverty from 12 percent in 2012 to 8.2 percent in 2017. The Royal Government of Bhutan also remains committed to realize its long-term Vision 2020 as well as the Sustainable Development Goals (SDGs) by 2030.

The RGoB requests continuing World Bank Group support through the proposed programmatic Development Policy Credit (DPC) to support institutional strengthening in some key areas. Building on the momentum and the lessons learned from the past DPF operations, the RGoB believes that the instrument is highly useful in facilitating development in Bhutan and to enable the World Bank Group in achieving its own twin goals of reducing poverty and boosting shared prosperity across its member states. The RGoB requests selective support for the goals and strategies under the 12th FYP and is committed to implement the institutional and policy reforms described in the policy and results matrix. The following two broad thematic areas are being addressed in this DPC series: (A) Improving Fiscal Sustainability and (B) Strengthening Private Sector Employment Opportunities.
(A) Improving Fiscal Sustainability

Improving fiscal sustainability is one of the overarching objectives of the 12th FYP. Despite sustained economic growth, Bhutan was exposed to macroeconomic vulnerabilities during the last several years. In order to address these vulnerabilities and to smoothen consumption, the RGoB established the Stabilization Fund. Framework for fiscal sustainability will be strengthened further through the formulation of fiscal rules. Furthermore, to improve fiscal responsibility and supplement efforts to increase self-reliance the RGoB also will take steps to broaden tax base including the introduction of a new Goods and Services Tax (GST) under this Program to be implemented in July 2020. To ensure the timely implementation, the government has already tabled GST for the cabinet meeting.

Further, the RGoB believes that improved Public Financial Management (PFM) systems will help to improve the quality of public spending in the country. With that in mind, the RGoB has approved the PFM Reform Strategy. To complement the objectives of the new PFM Reform Strategy, the RGoB through this operation has approved the amended Public Procurement Rules to improve public procurement systems and will roll out electronic Public Expenditure Management System (e-PEMS) by July 2019 to improve the efficiency in the overall government financial management and improve the payment services to all the RGoB client. Furthermore, the government will start establishing interconnectivity of new / existing PFM information systems for automated exchange of data in the next fiscal year. Also, the government aims to seek cabinet approval of the new Public Procurement Bill in the next fiscal year.

(B) Strengthening Private Sector Employment Opportunities

The RGoB continues to play a key role in the economic development of the country as the private sector still remains relatively small and underdeveloped. In order to boost the role of the private sector, the 12th FYP placed great emphasis on economic diversification, skill and human capital, access to finance and sustainable and inclusive development. All these areas form part of the 17 National Key Result Areas of the 12th FYP which greatly emphasis on the development of the non-hydropower sectors and fostering growth of a dynamic private sector that catalyzes a transition to a green and resilient development. As you might be aware that as the only carbon negative country in the world, Bhutan incorporates climate change initiatives within our development planning framework.

Through this operation, the RGoB will provide a direct support to reform its thrust sectors of Education, Health and Cottage and Small Industries to enhance and promote private sector employment opportunities. The RGoB has approved the Non-formal Education Equivalency Framework, removing cut-off point for Class X admission into class XI in public and private schools and Accelerating Child and Maternal Health program to improve the skills and invest in Human Capital. The Non-formal Education Equivalency
ROYAL GOVERNMENT OF BHUTAN
MINISTRY OF FINANCE
TASHICHHO DZONG

Framework is developed to create flexible pathways and equivalency among formal, non-formal and vocational education in learning and development of skills to cope with the changing needs of the society. Whereas providing quality maternal and child healthcare would translate into healthier citizens enabling them to realize their potential as productive members of society. Therefore, investing in human capital is a key to create more inclusive societies and end extreme poverty. Furthermore, the government plans to finalize the Teacher Standards and Teacher Professional Development Program, and the National Education Policy in the next fiscal year.

The RGoB will also take steps to improve bottlenecks such as access to finance and investment climate and use the DPC operation to address these bottlenecks in the country. Implementation of the proposed legal reforms to improve financial infrastructure (credit information bureau, and Global Interchange and Financial Transactions system) and strengthen the legal rights of creditors and borrowers will go a long way in addressing the access to finance constraints. Building on these reforms, the government will revise the FDI policy to ease and harmonize equity restrictions, and issue rules and regulations to facilitate external commercial borrowings.

As highlighted above, the RGoB strongly believes in an economic growth trajectory that is sustainable and inclusive. While Bhutan’s policy planning process naturally incorporates climate change impact, the Economic Development Policy (2016) emphasizes that energy efficiency and conservation measures are institutionalized and promoted. Through this operation, we will support efforts to implement a new energy efficiency program. Therefore, the government will formulate the National Energy Efficiency and Conservation Policy, and the National Climate Change Policy. Furthermore, the government will formulate the National Gender Equality Policy.

Conclusion

The RGoB remains highly committed to our reform progress supported by the proposed programmatic DPC series. We would like to express our appreciation for the support and the assistance extended by the World Bank Group to Bhutan’s socio-economic development. We look forward to continued support and fruitful collaboration in the years to come.

Yours sincerely,

(Namgay Tshering)
FINANCE MINISTER
Recipient’s agreement to the revised terms and the revised Financing Agreement and no further action or approval or change to these Minutes would be required.

(d) **FA Schedule 1, Section II.D:** The two delegations confirmed that the withdrawal of funds from the Financing Account will follow the following protocol:

(i) IDA will deposit the Credit proceeds into the USD Royal Government of Bhutan’s Account at the Royal Monetary Authority of Bhutan upon recipient of an application for withdrawal (Form 2380) duly completed;

(ii) The Bhutanese Ngultrum equivalent (based on the inter-bank exchange rate prevailing on the date of the transfer) will be transferred within five (5) business days into the Royal Government of Bhutan’s Budget Fund Account at the Bank of Bhutan; and

(iii) Within thirty (30) [calendar] days of disbursement of Credit by IDA, the Finance Secretary of the Ministry of Finance shall provide a written confirmation to IDA certifying the receipt of the Ngultrum and USD equivalent to the Credit into the Royal Government of Bhutan’s Budget Fund Account, the date of receipt, and the exchange rate applied to convert the Credit proceeds into Bhutanese Ngultrum as mentioned in the Financing Agreement.

**III. Letter of Development Policy**

4. The Letter of Development Policy was reviewed and agreed. The agreed text of the letter is attached as **Annex 3** to these Minutes.

**IV. Program Document**

5. The Program Document was reviewed and updated to take into account the comments and observations made by the Bhutan Delegation during negotiation. The Bhutan delegation confirmed that there was nothing in the text or data contained in the Program Document of a confidential or sensitive nature, or which could adversely affect the relations between the Kingdom of Bhutan and the World Bank Group.

**V. Public Disclosure**

6. Pursuant to the World Bank Policy on Access to Information, IDA will disclose the Program Document, the legal agreement and other information related to the legal agreement, including any supplemental letters. The Bhutan Delegation confirmed that IDA may publicly release the Program Document after consideration of the operation by IDA Board of Executive Directors.

**VI. Approval of negotiated documents, Statutory Committee, and Legal Opinion**

7. The Head of the Bhutan Delegation indicated that the negotiated documents, including the draft Financing Agreement are approved by the Kingdom of Bhutan and no additional confirmation or evidence of approval of these documents is required prior to the submission of the proposed financing for the consideration by the Bank’s Board of Executive Directors.

8. According to Article V, Section 1(d) of IDA’s Articles of Agreement, an operation proposed to be financed or guaranteed by IDA shall be accompanied by a report/recommendation (the Statutory Committee Report) to be issued by a competent committee (the Statutory Committee) whose members shall include an expert selected by the Governor representing the member in whose territories the operation in question is located. The Governor representing the Kingdom of Bhutan on the IDA Board of Governors agreed, by a letter dated November 19, 2014, that the official designated and authorized by the Government of the
Kingdom of Bhutan to represent the Kingdom of Bhutan in the negotiations of IDA financing provided to or guaranteed by the Kingdom of Bhutan shall be considered to be the Kingdom of Bhutan expert on the Statutory Committee and that said official’s signature of the signed Minutes of Negotiations for such IDA financing shall be deemed to constitute the signature of the Statutory Committee Report. The parties acknowledged the above designation with respect to the IDA financing for this Second Strengthening Fiscal Management and Private Sector Employment Opportunities Development Policy Financing.

9. With respect to the provisions of Section 9.02 of the General Conditions, the Recipient has confirmed that no additional actions will be required to be undertaken after the signing of the Financing Agreement for it to be considered legally binding. Unless in the Association’s opinion the circumstances that justified its decision change, the Association will rely on the Recipient representation and warranty described in Section 9.02 (b) of the General Conditions.

VII. Following Steps

10. The IDA Delegation would submit the Negotiations Package to the IDA Board of Executive Directors for approval. This submission is tentatively scheduled for May 28, 2019. The IDA Delegation stated that in the event that the Board presentation is changed and the change has an effect on the amortization schedule, the amortization schedule would be appropriately adjusted. Therefore the negotiated text of the Financing Agreement would be adjusted accordingly as noted in paragraph 3 (c) above.

Signed in Thimphu, Bhutan on May 21, 2019.

On behalf of the Kingdom of Bhutan

Mr. Nim Dorji
Head of the Bhutan delegation
Secretary
Ministry of Finance

On behalf of the International Development Association

Mr. Yoichiro Ishihara
Head of the IDA delegation
Bhutan Resident Representative/Sr.
Country Economist
South Asia Region

Attachments:
Annex 1: List of Participants
Annex 2: Agreed Financing Agreement
Annex 3: Letter of Development Policy
Annex 1: List of Participants

Members of the Bhutan Delegation

1. Nim Dorji, Secretary, Ministry of Finance
2. Lekzang Dorji, Director General, Department of Macroeconomic Affairs, Ministry of Finance
3. Tshering Yangki, Sr. Program Officer, Department of Macroeconomic Affairs, Ministry of Finance
4. Deki Yangzom, Chief Legal Officer, Ministry of Finance
5. Sangay, Legal Officer, Office of the Attorney General

Members of the IDA Delegation

1. Yoichiro Ishihara, Bhutan Resident Representative/Sr. Economist, SACBT
2. Mona Prasad, Lead Economist, GMTSA
3. Tenzin Lhadan, Operations Officer, SACBT
4. Zoé Kolovou, LEGES
5. Satish Kumar Shivakumar, Finance Officer, WFACS