

FINANCIAL ANALYSIS

A. Background

1. The financial position of the government was reviewed, and the sustainability of the grant-funded program was assessed at the fiscal and project levels in accordance with the Asian Development Bank (ADB) guidelines.¹ As the project has no revenue-earning component, the financial costs and benefits were not assessed.²

B. Government Fiscal Position

2. Bhutan's macroeconomic conditions have improved since the Indian rupee shortage crisis of 2012–2013, and its gross domestic product (GDP) in FY2017 is estimated at 6%. In 2015, the current account deficit reached 29.1% of GDP due to imports for hydropower projects, almost all of which were financed through loans from India.³ In 2017, however, the current account deficit narrowed to 20.5% due to lower hydropower imports and more electricity export. While the economic outlook is favorable, risks to macroeconomic stability from high-public sector debt remain. The International Monetary Fund policy recommendations from the 2016 Article IV Consultation included avoiding a large easing of the fiscal stance.⁴

Table 1: Selected Macroeconomic Indicators, 2012–2017

Indicator	FY2013	FY2014	FY2015	FY2016	FY2017 (est.)
GDP growth (%)	3.6	4.0	6.1	6.2	6.0
Inflation (%)	11.3	10.0	6.4	3.9	3.4
Current account balance (% of GDP)	(25.4)	(26.4)	(28.3)	(29.1)	(20.5)
Total GGE as a % of GDP	34.4	29.8	27.4	30.9	28.4

() = negative, est. = estimated, FY = fiscal year, GDP = gross domestic product, GGE = general government expenditure.

Source: International Monetary Fund. 2016. *Article IV Consultation Staff Report*. Washington, DC.

3. Bhutan's economy is susceptible to external shocks because of its close economic ties with India. Structural reform delays within the Indian economy and growth slowdown can potentially slow Bhutan's growth. In addition, growth projections in future years depend on the success of hydropower investments that are yet to be realized (footnote 4). However, a favorable growth outlook and a projected increase in revenue inflows from hydropower investments can translate into significant fiscal space for the health sector. Monitoring and advocacy are needed to ensure that government investments in health increase proportionately with economic growth.

C. Financial Sustainability

4. To inform the financial sustainability of the sector and project investments, trends in government resource allocation and Ministry of Health (MOH) budget utilization were reviewed. Several factors are straining Bhutan's health financing, including greater demand for health care because of a rise in chronic diseases, escalating unit costs of care from more complex health conditions, and management and delivery challenges. The sustainability of the health sector and

¹ ADB: Financial Due Diligence – A Methodology Note, January 2009, ISBN 978-971-561-763-5, Publication Stock No. 120308.

² ADB. 2005. *Financial Management and Analysis of Projects*. Manila; ADB. 2009. *Financial Due Diligence: A Methodology Note*. Manila.

³ World Bank. 2016. *Bhutan Economic Update 2016*. Washington, D.C.

⁴ International Monetary Fund. 2016. *Staff Report for the 2016 Article IV Consultation*. Washington, DC.

project investments will depend on (i) the government maintaining its priority for the health sector in the resource allocation process, proportionate to its economic growth; (ii) adequate recurrent expenditure in the MOH budget; and (iii) more fiscal space through more health-specific resources and greater efficiency in management and service delivery.

5. **Government priority and trends in sector resource allocation.** Total health expenditure (THE) as a percentage of GDP has decreased from 5.2% in 2010 to 4.4% in 2015.⁵ General government health expenditure as a percentage of GDP also declined over this period, from 5% in 2010 to about 3%. Since the sector is largely publicly financed, and the government contributes about three-fourths of THE, a decrease in government health spending also significantly impacts overall financing trends.

Table 2: Trends in Health Expenditure, 2011–2016

	2010	2011	2012	2013	2014	2015
THE as a percentage of GDP (%)	5.2	3.6	3.8	n/a	4.44	4.40
GGHE as a percentage of GDP (%)	5.0	n/a	n/a	n/a	3.09	2.97
Government share of THE (%)	88.0	73.4	73.8	n/a	72.00	70.00
GHE as a percentage of GGE (%)	11.0	n/a	n/a	n/a	8.00	9.00

GDP = gross domestic product, GGE = general government expenditure, GGHE = general government health expenditure, GHE = government health expenditure, THE = total health expenditure, n/a = not available.

Source: Government of Bhutan, National Health Accounts, 2011–2013 and 2014–2016. Thimphu; World Health Organization. 2017. *The Kingdom of Bhutan Health System Review: Health Systems in Transition*. New Delhi.

6. In general, there is a recently declining trend in government priority to the health sector relative to its GDP growth. Government health expenditure as a percentage of general government expenditure fell from 11% in 2010 to 9% in 2015 (Table 2). The composition of the government's overall five-year plan allocation also shows a reduction in the share of allocation to the health sector—from 7.3% in 2008–2013 (Tenth Five-Year Plan) to 6.5% (Eleventh Five-Year Plan) (Table 3). The reductions were driven by a shift in the government's investment priority toward revenue-generating infrastructure projects.

7. However, while government health expenditure proportionately declined as a percentage of GDP and the overall general budget, the absolute budget amount allocated to the health sector shows an increasing trend (Table 3). This suggests that the government has maintained a good level of priority for the health sector, and also attests to good financial capacity and budget utilization trends on the part of the MOH.

Table 3: Five-Year Plan Allocation of Budget to the Ministry of Health and the Dzongkhag Health Sector

Plan	Plan Period	Budget Allocated to MOH and	Composition of Outlay
		District Health Sector (Nu million)	(%)
8	1997–2002	2,904.11	7.3
9	2002–2008	4,505.83	6.4
10	2008–2013	10,809.73	7.3
11	2013–2018	13,952.96	6.5

MOH = Ministry of Health.

Source: World Health Organization. 2017. *The Kingdom of Bhutan Health System Review: Health Systems in Transition*. New Delhi.

⁵ However, it should be noted that compared with other countries, Bhutan still spends a significant amount on health. THE as a percentage of GDP was 1.4% (2014) in India, 0.8% (2014) in Bangladesh, and 2.3% (2014) in Nepal. (The World Bank. Human Development Indicators. [https://data.worldbank.org/indicator/.](https://data.worldbank.org/indicator/))

8. Bhutan is in the process of finalizing its 12th 5-year plan (2018–2023). Based on preliminary projections, the total government outlay for that plan is expected to be about Nu300,000 million, of which 61% is for current expenditure and 38% for capital expenditure.⁶ The 12th 5-year plan will have a strong focus on decentralization, with a significant increase in the ratio of sector budgets to be given to districts. Previously, the government had benchmarked a sector budget ratio of central to districts of 80:20 (e.g., 80% of the health sector budget to the MOH and 20% to districts), and that ratio will now increase to 50:50 across all sectors under the 12th 5-year plan.

9. The indicative capital outlay for the MOH budget in the 12th 5-year plan is Nu3,600 million, which shows a slight decrease over the approved Eleventh Five-Year Plan allocation of Nu3,839 million (footnote 6).⁷ However, compared with other sectors affected by the ongoing decentralization of sector budgets, the decrease in the MOH central budget has not seen such a dramatic decrease when compared to other sectors, owing to the MOH's good budget performance and achievements in key sector result areas. For example, the Ministry of Education budget decreased by 51.6% and that of the Ministry of Home and Cultural Affairs dropped by 48.0% (footnote 6). This further demonstrates a good level of government commitment to the health sector and good budget performance by the MOH.

10. **Trends in Ministry of Health budget utilization.** Table 4 shows that the MOH has a trend of fully utilizing their planned budgets from 2013 to 2016. FY2015 and FY2016 show spending above the allocated budget, but the overspending was kept to less than 10% of the total allocation. In FY2014, the MOH used 94.7% of the total budget that was allocated; in FY2015, the MOH utilized 107.8% of their budget allocation; and in FY2016, they utilized 104.3% of their allocation (see Table 4). This indicates little discrepancy between allocation and expenditure, and sound financial planning and adequate absorptive capacity by the MOH.

Table 4: Ministry of Health – Total Expenditure vs. Budgeted Plan, 2013–2016

Year	Budget Type	MOH Portfolio (Nu million)			Difference in Planned Budget and Actual Expenditure					
					Total Unutilized Budget		Unutilized Current Budget		Unutilized Capital Budget	
		Total	Current	Capital	Nu million	%	Nu million	%	Nu million	%
FY2014	Planned budget	3,139.431	1,977.015	1,162.416						
	Actual expenditure	2,974.14	2,049.47	924.670	165.2	5.3	(72.4)	(3.7)	237.7	20.5
FY2015	Planned budget	3,206.024	2,302.862	903.162						
	Actual expenditure	3,457.65	2,473.890	983.760	(251.6)	(7.8)	(171.0)	(7.4)	(80.5)	(8.9)
FY2016	Planned budget	3,934.338	2,662.080	1,272.258						

⁶ Government of Bhutan, Gross National Happiness Commission. 2018. *12th Five Year Plan Guidelines*. Thimphu.

⁷ The Nu3,600 million under the Twelfth Five-Year Plan does not include the recurrent component (expected to be about 30:70 under the plan) and decentralized health budget to districts (estimated at 50% of the overall sector budget). Bhutan goes through an annual budget exercise, and actual fiscal-year allocations cumulated over the 5-year plan period would likely exceed the initial 5-year plan allocations significantly.

Year	Budget Type	MOH Portfolio (Nu million)		Difference in Planned Budget and Actual Expenditure						
				Total Unutilized Budget		Unutilized Current Budget		Unutilized Capital Budget		
				Nu million	%	Nu million	%	Nu million	%	
	Actual expenditure	4,103.190	2,732.030	1,371.160	(168.8)	(4.36)	(69.9)	(2.6)	(98.9)	(7.8)

() = negative, FY = fiscal year.

Source: Government of Bhutan, National Health Accounts. *Annual Financial Statements and Yearly Budget Documents*. Thimphu.

11. Table 5 shows the MOH's expenditure by recurrent versus capital expenditure, which has implications for the sustainability of project capital investments. In FY2012, the recurrent and capital expenditure were 60.4% and 39.6% respectively and by FY2016, they were 66.6% and 33.4% respectively. The increasing trend in recurrent expenditure indicate the MOH's commitment to maintaining and operating their existing capital assets.

Table 5: Ministry of Health – Capital and Recurrent Expenditure (actual), FY2012–FY2016

	FY2012	FY2013	FY2014	FY2015	FY2016
MOH expenditure (Nu million)	2,954.67	2,951.8	2,974.14	3,457.65	4,103.19
MOH recurrent expenditure (Nu million)	1,783.51	1,920.17	2,049.47	2,473.89	2,732.03
MOH capital expenditure (Nu million)	1,171.16	1,031.63	924.67	983.76	1,371.16
MOH recurrent expenditure (% of total)	60.4%	65.1%	68.9%	71.5%	66.6%
MOH capital expenditure (% of total)	39.6%	34.9%	31.1%	28.5%	33.4%

FY = fiscal year, MOH = Ministry of Health.

Source: Government of Bhutan. 2016. *Annual Financial Statements, 2011–2016*. Thimphu.

12. **Future Ministry of Health expenditure projections.** The MOH annual incremental capital and recurrent expenditure projections were estimated based on the average of projected annual increases in GDP growth for Bhutan during 2016–2023.⁸ The elasticity of government health spending to GDP was assumed at 1.0, implying that 1% growth in GDP would be associated with an average 1% increase in government health spending. This assumes that the government maintains priority for the health sector in line with GDP growth. During the 12th 5-year plan (2018–2023), the ratio of recurrent to capital expenditures of the MOH is estimated to increase to 70:30 because (i) greater population coverage by health facilities will lower capital investment needs, (ii) MOH's policy of 'consolidation' focuses on quality and sustainability, and (iii) a pay increase is planned for civil servants. By 2023–2024, total MOH expenditure is expected to be Nu7,840 million, of which 70% will be for recurrent costs (Table 6). The project's incremental recurrent costs are estimated at only 0.55% of the estimated THE and at 0.79% of estimated recurrent health expenditure for 2017–2018.⁹ Therefore, the financial sustainability of project investments can be assured. The government is expected to be able to maintain project recurrent costs after project completion.

⁸ The average of annual increases in GDP growth for Bhutan during 2016–2023 is 8.43%. International Monetary Fund. *World Economic Outlook Database*, April 2018. <https://www.imf.org/external/pubs/ft/weo/2018/01/weodata/index.aspx> (accessed 20 July 2018). The percentage change from FY2012 to FY2016 was 11.4% for recurrent expenditure and 5.9% for capital expenditure.

⁹ Project recurrent costs 1 year after project completion are \$0.457 million (based on ADB estimates).

Table 6: Ministry of Health – Expenditure Projections
(Nu million)

Year	Recurrent	Capital	Total
FY2019	3,662	1,569	5,231
FY2020	3,970	1,702	5,672
FY2021	4,305	1,845	6,150
FY2022	4,668	2,001	6,669
FY2023	5,061	2,169	7,230
FY2024	5,488	2,352	7,840

FY = fiscal year.

Note: Ministry of Health future expenditure was calculated based on average projected percentage change in gross domestic product growth during 2016–2023, which is 8.43%. A ratio of 70:30 was applied for current to capital allocation of the projected total health expenditure.

Source: Asian Development Bank estimates.

13. In summary, the sustainability of the Health Sector Development Program’s project investments can be ensured given the increasing share of sector budget to recurrent expenditures, the MOH’s strong financial capacity, and overall government commitment to the health sector. However, as health care costs and the MOH’s requirements increase, sustainability of the sector will require additional financial resources and efficiency gains in the future. The program’s investments in the Bhutan Health Trust Fund (output 2) and e-health (output 3) are expected to increase the longer-term fiscal space and efficiency for the health sector. Additionally, as hydropower generation sets in and the government accrues revenue from electricity exports, the prospects for more fiscal space for health are promising. Given Bhutan’s constitutional commitment toward free basic health services for all citizens, the health sector should benefit from accelerating GDP growth. Adequate monitoring and advocacy are needed to ensure that the government increases its health spending in proportion to GDP growth. As the government further decentralizes its budget allocation to districts, district-specific advocacy and capacity building are also needed to ensure adequate budget and spending for health.