

# Path breaking Ideas in Economics

This series aims to introduce the readers to the some of the path breaking ideas in Economics. A path breaking idea is an idea or a body of knowledge that brings about a significant shift in our understanding of a discipline. It could be a philosophical shift, or, an augmentation of an old model with more sophisticated tool of analysis that allow us to make the knowledge more meaningful. The path breaking ideas often meet with stiff resistance from the status quo-ist but have the logical strength to overcome such challenges. The first pick is the philosophy of Gross National Happiness developed in the Royal Kingdom of Bhutan .

## Idea 1: The philosophy of Gross National Happiness

Central focus of Economics has always been creation of wealth, material progress and preference satisfaction (utility). To serve this focus, mainstream economics requires single minded pursuit of self-interest without any exception. The concept of GDP, based on hedonistic utilitarian principle, became a leading indicator of the materialistic progress of nations- higher GDP per capita reflects higher level of general welfare. GDP centric approach necessitated creation of policies, processes and institutions that aims at promoting material progress. The trade-off between material progress and overall happiness was ignored if not understood properly. So powerful was the impact of

GDP orientation that 'positive economics' emerged as a major branch of economics, which is all about being value neutral. Although, some philosophers questioned the utilitarian approach to GDP as it neglected other considerations such as distribution of income and sustainability of such progress, they only looked at the possibility to fine tune GDP or combine it with some other indicators. Such efforts did not represent a major shift as GDP still remained at the helm.

In 1970s, a new idea emerged in Bhutan that questioned the very basic foundation of GDP by attempting to shift the focus away from material progress to spiritual progress. The idea was coined as Gross National Happiness, with an intent to replace GDP. It was probably for the first time that any country attempted such an experiment to move away from GDP orientation. This idea provided a new light to the dismal science- a possibility to bring the overall happiness of human being at the centre of development efforts. Rooted in the Buddhist philosophy, GNH aims to synthesize material and spiritual wellbeing and moves away from the profit maximisation to the maximisation of general level of happiness. The philosophy of GNH offered an alternative that has potential to mitigate the crises caused by the 'value less' growth- rising disparities, increasing stress, fracturing families and social systems, environmental degradation, greater insecurity and limited respect for others. Initially, there was limited appreciation, if not outright rejection, of this idea from the mainstream economists and policy makers outside Bhutan. Ultimately, the new idea started getting greater acceptance and appreciation because it provided a hope in the times of despair.

GNH orientation of development philosophy requires a different set of policies, instruments, processes and insti-

tutions. GNH philosophy, based on a social contract, rests on the idea that development should have four essential features - equitable socio economic development, protection of tradition and culture, preservation of environment and good governance. Promotion of GNH requires a behavioural shift from strict individualism towards collaboration, cooperation and coexistence and focuses on common interest. Such behavioural shift is only possible with a new set of value system. GNH orientation places spirituality, which is different from the religious fundamentalism, at the centre stage. A wider application of this idea requires tying up of the loose ends- better understanding of the constructs of happiness, identification of a congruent set of policies, processes and institutions, and, finally its functional measurement.

Although, the concept of GNH is unrefined and not ready to replace GDP, it has potential to bring about a shift in the pure materialistic orientation of economic activities. It bring a new hope to repair the system. GNH orientation of development philosophy has the potential to give us a world that is not only sustainable but also a better place to live. It will build a world where human being will be respected for what value they have rather how much wealth they possess. It is a path breaking idea because it offers a scope for redefining the objective of development.

**-Sanjeev Mehta, Professor in Economics**

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## Perception of youth on youth unemployment

-Purna Maya Gurung, 5th semester

### Introduction

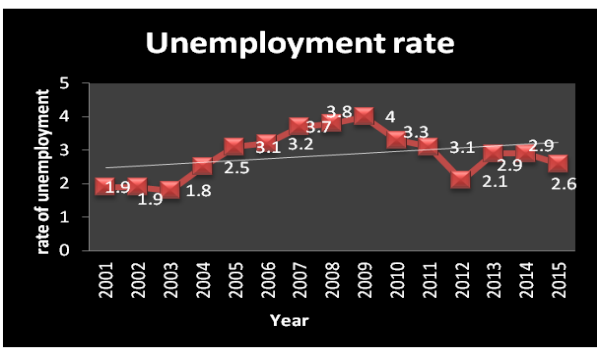
Unemployment refers to those who are actively looking for job as percentage of labour force but not getting job. There are three types of unemployment namely natural rate of unemployment where there will be some percent of the people left unemployed, actual rate of unemployment refer to the unemployment in an economy and frictional rate of unemployment is the difference between natural rate of unemployment and actual rate of unemployment.

Bhutan initiated its development plans through the inception of first five year plan in 1961 to 1981 which brought improvements in agriculture, irrigation, hydropower project and transportation and in 2014, World Bank and Finance Corporation have released the Ease of doing business Index 2014, encouraging small business to start up and operate among 200 countries (World bank, 2015).

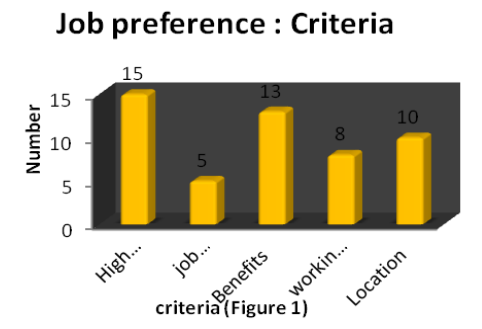
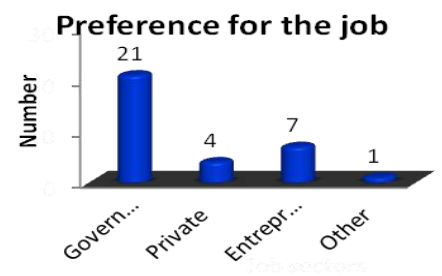
According to the Doing Business Report in Bhutan (2015), Bhutan ranked 125 out of 189 economies. One of the UN Millennium Development Goals is to achieve universal primary education. Bhutan joined MDGs in 2008, where Bhutan achieved rapid expansion in education system resulting into more number of educated youth and creating unemployment in market.

In current situation majority of the jobs demand those who have persuaded higher education, skills and experience. In Bhutan majority of the Bhutanese population are under the age of 30, indicating more number of youth population (MoLHR, 2013). Therefore, majority of the youth prefer to avail higher education such as diploma and degree to meet the criteria demanded in the market.

Though Bhutan has achieved developmental activities, there is the anxiety for the increasing number of youth unemployment in Bhutan. The graph shows rise in unemployment from 2001 till 2009, declined from 2009 till 2012 but increased from 2013(NSB, 2014). The reasons for rise in youth unemployment are due to mismatch of skills, limited sectors for more number of youth populations and the preference for the white color jobs. On the other hand youth unemployment has declined due to various types of programs provided by the government of Bhutan such as the overseas programs, training programs and job fairs. However unemployment trend is still increasing. Youth unemployment in Bhutan is a major concern in present decade, since every year there are more youth graduating and entering the labour market in search of jobs. Therefore, my research motive was to find out the factors contributing to youth unemployment and solutions provided by the government of Bhutan to ease youth unemployment.



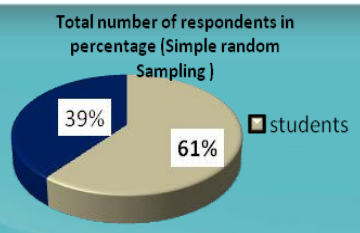
The above graph shows job preference, majority of the respondents preferring to join government job followed by entrepreneurship, private and others includes Non-Government Organization such as UNICEF and WWF because of various types of benefits offered by the government such as allowance and accommodation. Preference for the private is less because of the risk involved in it, such as chances of incurring loss. Entrepreneurship is being encouraged by the government by providing loan for commencing business



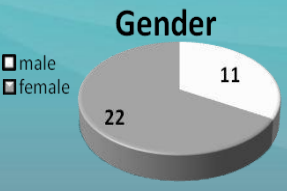
The figure one shows the preference for the job in terms of various criteria as mention in the graph. Majority have selected high income category followed by the benefits, location, working environment and job description. As per the salary expectation, most of the respondents prefer Nu.10000-50000 remuneration and only two below 10000. Only two respondents prefer below 10000 because they

### Findings

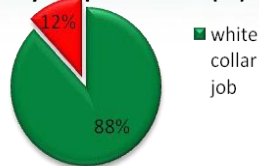
In terms of qualification, majority of the people are studying followed by the undergraduates. There is rise in the number of literate people especially for the better qualification to meet the criteria as per the market force leading to more number of graduates to the job market.



On the other hand, based on the gender wise qualification undergraduate consist of less of female than male because in past parents used to think that a girl has to stay at home for house hold chores and distance of schools. At the same time under the currently studying consist of more number of female than male as it is associated with the gender equality and US MDGs (United Nation Millennium Development Goals).



### Types of job preferred by respondents (%)



More number of people prefers to have white collar job (88%) than blue collar job (12%) indicating ignorance of the agriculture jobs (manual working) and preferring to work under companies, corporation and organization.

Finally my research finding for the youth perception of youth unemployment, it is not the shortage of job in market that rises the youth unemployment but it is the level of education followed by the attitudes of the youth on location, income, skills and benefits provided.

### Solutions

As per my research findings, government needs to encourage more number of entrepreneurship to get employed by providing loan in low interest rate. The skills and experience required by the job market needs to be fulfilled with more number of vocational training programs such as Technical Training Institutes, Bhutan International School of Hospitality and Tourism and encourage youth to avail internship. Government should focus on sustainable development activities of rural-urban areas to reduce internal migration rate and increase the FDI (Foreign Direct Investment) in Bhutan.

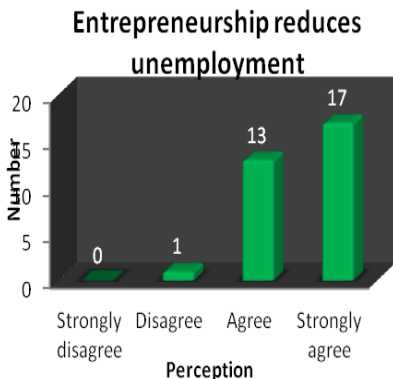
### Conclusion

Government of Bhutan is trying to eradicate the youth unemployment rate through overseas programs, internship programs, Student Exchange Programs and training programs to gain a better knowledge, skills and experience about the course, support by the government to start a business by providing loans at low interest rate.

As per the survey conducted, majority of the youth prefer the high income job and better facilities that has been provided by the organization reflecting the attitude of the youth. Internal migration rate is high in urban areas leading to more population. The major causes for the rise in youth unemployment rate in Bhutan are due to attitude, mismatch of skills and lack of experience. Youth and unemployed participants showed positive insight interms of government overseas programs to increase employment.

### Recommendation

Youth unemployment being the concern of Bhutan is still on rise every year besides the programs provided by the government to reduce the youth unemployment in Bhutan. Therefore government needs to focus more on improving the skills and training centers with rise in youth population and recommend bringing quality of skills and programs. Perception of the youth on youth unemployment consist of different perceptions and further I recommend other researcher in future to do research on youth unemployment with the change in years and trends.



The graph shows whether entrepreneurship in Bhutan reduces the rate of unemployment in Bhutan or not. Majority of them agreed that it reduces the unemployment rate. When there is more number of self employed people in an economy, it reduces the unemployment rate and those who are unemployed can employed by the entrepreneur.

### Discussion

Findings of my research states that there are 8 numbers of youth who have graduated and still 20 are studying indicating that in future there will be more number of people pursuing graduates and less people pursuing till class 12 creating more competition for jobs, therefore the youth population determines the rise in youth unemployed. With the level of education, they prefer high income, benefits and the place of working. Therefore level of education determines the other factors (income, benefits and location). Majority of the youth prefer white collar jobs than blue collar jobs.

The open ended questions were to know the views of government programs and jobs that they will refuse to know their perception on youth unemployment in Bhutan. Majority of the respondents stated that programs provided by the government is effective and good measures to tackle the problem of youth unemployment, they are able to gain more knowledge, experience and earn more through the overseas programs where as very few stated that it is not a good measures to send student abroad because it may results in to brain-drain and less labour force in Bhutan. On the views of youth unemployment, most of them stated that rise in the youth unemployment is due to the attitude of the youth towards high income and white collar jobs followed by the mismatch f skills and experience. Low income and location determines the refusal of job by them followed by the blue collar job and working environment.

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# Weighted mean

~Rishabh Mehta

B.A Development Economics

$$A = \frac{(xa * wa + xb * wb + \dots + xn * wn)}{w}$$

Where x represents

Weighted mean (Doane & Seward, 2010) is a type of measure of central tendency. It is expressed as  $\bar{x} = \frac{\sum_{i=1}^n x_i w_i}{\sum_{i=1}^n w_i}$  where  $x_i$  represents mean of individual domains of a, b ... n and w represents weight of each domain and N represents the number of domains. The researcher should be careful about the use of weights- such that the sum of the weights should always be equal to one (it should be expressed as a ratio or percentage). In this case, the denominator value in the equation is equal to one hence of no utility. For this reason weighted mean is also weighted sum of given domains.

It is an important variant of arithmetic mean which is based on the assumption that all the elements of a mean value are not uniformly important- some are more important than others. If a researcher or analyst believe that some elements of a mean are more important, he assigns more weights to that element, which means that mean value is greatly affected by that particular element. Usually, the weights are assigned on the basis of subjective assessment- what the researcher or analyst believe. It is therefore important that we have a strong logic for the weight we use. For example, while calculating the consumer price index (CPI) in Bhutan 52% weightage is assigned to food products category (RGoB, 2015). The selection of weight was based on the fact that average Bhutanese consumers spend about 52% of their income on food products.

Let me illustrate this with help of an example- suppose there are three persons in a society- X, Y and Z. their incomes are 1000, 7000 and 22,000 respectively. Simple average of their income is 10,000. But if a society thinks that welfare of poor person is more important than others and assign weights of 50%, 40% and 10% respectively to X, Y and Z. hence per capita income of the society will be  $- 0.5*(1000)+ 0.4*(7000)+ 0.1*(22000)$ , i.e.- 5500. As we give more importance to poor person, the per capita income would change significantly.

Many of the popular concepts such as Human Development Index (HDI) and poverty adjusted GDP use the concept of weighted mean. For example the human development index uses three variables – knowledge base indicators, longevity indicator and per capita income. It gives equal weight to all the indicator that is 0.333 (UNDP, 2015). This is also one of the major criticism that it is based on equal weight concept which does not reflect reality.

The concept of weighted mean is also applied in the sampling process where proportionate stratification is required.

Despite conceptual superiority of this concept, it suffers from some weaknesses. The major weakness of this concept is the decision about how the weights are assigned. Application of weights require in-depth knowledge of the situation and should be based on real time data. Such knowledge or data base is often absent or inadequate. The use of weight leaves a lot to the discretion of the researchers or analyst which induces scope for personal biases. Often the bureaucrats and politicians are criticized for manipulating average or mean value by assigning inappropriate weights. Many times ordinary people are not aware of such methodology and consequently they remain in dark about the reality. Let me illustrate this point through an example – Suppose the price index consists of food and nonfood products, and the food prices rise by 15% and nonfood price rise by 5%, the weighted mean can give different answers depending on how weights are assigned. If I am interested in showing low inflation rate I would assign 90% weight to nonfood commodities and 10% to the food products.

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## Examination of the causes of rupee shortage and recommendations

~Wangchuk  
Graduate of 2015, RTC

Rapid economic transition from agrarian self-reliant economy to modern economy allied with perpetual negative trade balance with India are some of the main causes of Rupee crunch which have become major economic issue in the Bhutanese economy today. Bhutan was Agrarian self-reliant economy before the initiation of developmental plans by the third King in 1961. The first Five Year Plan (FYP) which took place from 1961-1966 was fully funded by India with a total budget of Rs 174.7 million (Gross National Happiness Commission, n.d). The first FYP was an attempt towards what Rostow (1960) defined in his growth model as pre-condition for take-off. The introduction of modern development plan suddenly made the country from self-reliant agrarian to fully aid dependent to carry out the developmental activities. The fourth King realized the heavy dependence on external aid and mentioned on his coronation address in June 2, 1974 that, Bhutan must strive for economic self-reliance. Therefore, the fifth FYP (1981-1986) shifted its focus from the usual strengthening of basic infrastructure to the sectors that generated revenue such as hydro power. This shift was considered as paradigm shift in the approach of FYPs. However, ever since the launch of FYPs, there has been import of huge capital and labour especially from India with little exports which led to perpetual negative trade balance. Thus, Rupee crunch is a gradual process which began from the start of FYPs, and became prominent in 2012 which still continues to remain one of the major economic concerns. If we look at the causes of the Rupee crunch, the main causes revolves around current account deficit, credit growth and lack of Rupee reserve.

The current account deficits was mainly attributed by negative trade balance. India is a major trading partner of Bhutan with 84.1% of import and 89.4% of export of overall trade taking place with India in 2014 as per Royal Monetary Authority (RMA) of Bhutan, Annual Report 2014/15 (RMA, n.d, p.126). "Trade can make everyone better off" (Mankiw, 2009) and certainly trade with India has benefited both Bhutanese and Indians. Bhutan enjoys comparative advantage in the production of hydro-electricity and thus electricity export constituted 33.4% of total exports to India in 2014 (RMA, n.d, p.123). However, India enjoys both comparative and absolute advantage in the production of almost all goods and services other than hydro-electricity but still trade benefits both the parties and there is existence of free trade agreement between India and Bhutan. As a result of trade with India, the current account deficit amounted to Nu. 36,084.7 million which comprised of 30.2% of GDP with that of trade balance of goods alone with a deficit of Nu. 19,048.7 million which is 21.8% of GDP in 2014 (Refer figure 1).

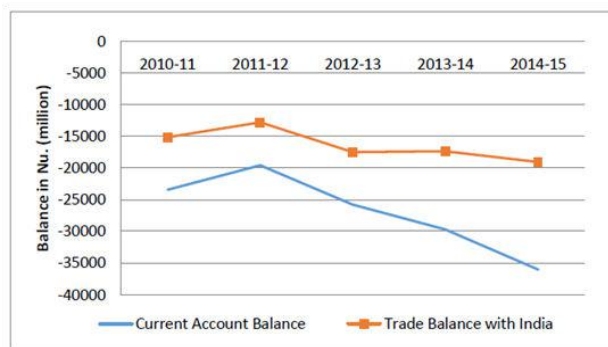


Figure 1: Current Account Balance & Trade Balance with India (2010-14)  
Note: Data adapted from RMA Annual Report 2014/15, Key Economic Indicators of Bhutan

Majority of the imports were in the category of mineral products, oils and fuels with 27.9% of the total imports. However, if the percentages of all other consumptions are added excluding the consumption of fuels, it comes to 25.9% (Table 1) which implies majority of the Indian Rupee (INR) is spent on consumption of goods. If the fuel used for purely consumption purpose is separately available (not the fuel consumed in construction of hydro-electric power and other investment purposes) and added to the consumption of goods in Table 1, then there is high probability that consumption of goods would comprise the highest percentage of imports from India. For instance, food imports rose to Nu 7 billion in 2012 from that of just Nu 1.8 billion in 2004 (Ura, 2015). Such practice of spending huge amount of Rupee on consumption will not earn Rupee as it a consumption expenditure rather than investment and will increase the demand of Rupee further as a result of higher aggregate demand for goods.

Table 1: Import of Consumption Goods from India (2014)

Composition of Consumption Imports	Percentage
Live Animals and Animal Products	5.6
Vegetables, Fruits, Nuts, Coffee, Tea	7.4
Spices, Cereals, Grains and Seeds	2.1
Animal or Vegetable Fats and Oils	4.2
Textiles, Foot wear and Hats/Headgear	1.7
Wood and Wood Pulp Products	4.9
<b>Total</b>	<b>25.9</b>

Source: Adapted from Table 24A of RMA Report 2014/15, p. 122

The credit growth in the economy is largely contributed by banks' lending on construction sector and vehicle imports in 2012 when Rupee crunch was critical. Such lending by banks still continues after the ban on loans on vehicle import and construction materials was lifted in 2014. Banks continue to provide such loans because they have limited investment opportunity. The credit on hydro-electricity sector also contributed significantly. For instance, it was 52% of GDP (World Bank, 2014) and the debt service remain a grave concern although the general perception of hydro-power loan being self-liquidating. It is a grave concern because the cost of almost all the ongoing hydropower projects escalates over 100% and thus as stated by Mehta (2012) "...unless the rate of return on the borrowed money exceeds rate of interest, the ability to repay without compromising fiscal sustainability remains doubtful." For instance, the initial cost of PHPA II was 37.78 billion and now it is estimated at 93.75 billion and Tala Project's completion cost was three times its initial cost (Gyelmo, 2015). Even if the variability of global climate change is assumed to be at ceteris paribus, the time of net earnings from hydro-power remains a far dream.

There is just marginal reserve of Indian Rupee and it has been decreasing gradually. It is more alarming that both the INR and US Dollar (USD) reserve are declining at the same time. The INR reserve decreased from Rs. 20 billion to 16 billion from September 2015 to February 2016 while in the same period USD reserve decreased from 833 million to 784 million (Gyeltshen, 2016). The international currency reserve with RMA is predominantly dominated by USD. The inadequate reserve of INR also contributed to Rupee crunch and as a result puts pressure on the parity peg of Ngultrum and INR leading to unofficial (illegal) exchange market in the bordering town. Ngultrum 100 was exchanged with Rupee 90 and some shops in the bordering town did not even accept Ngultrum which otherwise was not an issue before the Rupee crunch. The unofficial exchange rate is calculated to be 1.11

$$\text{Forex rate } (e) = \frac{\text{Domestic Currency (100)}}{\text{Foreign Currency (100)}} = 1 \quad \text{Official rate (Parity Peg)}$$

$$e = \frac{100}{90} = 1.11 \quad \text{Unofficial rate (in the bordering town) after the Rupee crunch}$$

When the demand for INR increases while the supply remaining the same (Figure 2), Nu depreciates against INR and thus the exchange rate rises from 1 to 1.11. Majority of the reserve for a country should be the currency with which the country trades most in order to avoid shortfall. Bhutan has the least share of currency reserve of major trading partner country amongst the similar trade practices in the world (Table 2). Insufficient low reserve of INR also contributed to the loss of confidence in Nu (Rashid, n.d) and thus depreciation of Nu occurred.

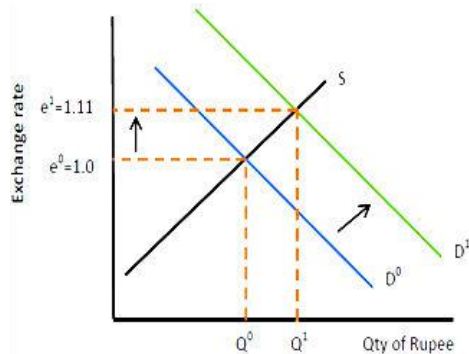


Figure 2: Determination of Unofficial Exchange Rate between Nu and INR

Namibia and Swaziland has similar trade practices with South Africa as Bhutan with India. However, their share of South African currency Rand in the international reserve is 33% and 60% respectively. If there is adequate reserve of INR, there will not be issue of INR shortfall even if there is huge current account deficit and also no impact on the parity peg system.

Table 2: Share of Main Trading Partner's Currency in International Reserve

Country	Main Trading Partner	Share of Import from Main Trading Partner	Share of Exports to Main Trading Partner	Share of Main Trading Partner's Currency in International Reserves
Bhutan	India	75.00%	77.00%	1.90%
Namibia	South Africa	80.00%	29.00%	32.90%
Nepal	India	57.00%	49.00%	31.80%
Swaziland	South Africa	92.90%	45.00%	60.00%

Source: Table II, Rashid, Understanding the Cause of Rupee Shortfall

The following are the most relevant recommendations suggested to ease the issue of Rupee crunch in the Bhutanese economy:

**I.** Invest in the Agriculture sector so as to reduce the trade deficit by way of producing our own food requirements or at least reduction in the demand of food imports. Bhutan import

almost half of its rice requirement and Indian vegetables enjoy a large market share. The self-sufficiency rate of rice of Bhutan in 2011 was 51% according to the Ministry of Agriculture and Forestry's (MoAF) report, RNR Statistics 2012, (MoAF, 2013) and today the situation is not different as the rice topped the list in food import with 79,306 metric tons in 2014 (MoAF, 2015). The government can intervene in this market through way of imposing taxes on Indian vegetables and rice to raise the price or by way of application of price supports. Government may buy the rice and vegetables from the Bhutanese farmers although the price is high and this will be an incentive for other farmers and thus they will also start producing. Therefore, within a year or two, the supply will be increased leading to fall in price. For instance, when Chili is sold for the first time in the vegetable market, it fetches Nu 150.

However, as the supply increases, the price keeps on falling and reaches up to Nu 50 (Figure 3). The failure to allocate income distribution fairly by the "invisible hand" can also be overcome by such intervention of government in the market as Bhutanese farmers may begin to earn income through sale of vegetables and rice.

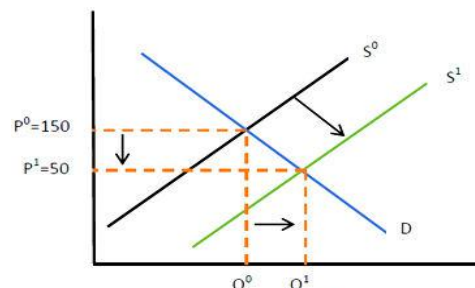


Figure 3: Fall in Price of Chilli due to Increased Supply

**II.** Keep at least 30% of the international reserve in the form of INR as learned from the experiences of Namibia and Swaziland. The reserve could be kept with Indian Banks and earn interest. When there is sufficient reserve, there will not be shortfall even if there is huge current account deficit and thus no impact on the parity peg arrangement of Ngultrum with INR.

**III.** Selling of USD when INR depreciates with USD. This is a short term measure and not sustainable as INR is spent on consumption to a great extent. However, if USD is sold to buy INR when the value of INR is low with USD, Bhutan could benefit by earning higher INR and as Ngultrum and INR are pegged at parity.

The recommendation number I is the best solution in the long run, because it involves some structural changes in the economy and thus can lead to reduction of the current account deficit. The long run is not that long for agricultural production as the length of the period depends upon the time taken to change the factors of production. Therefore, for agriculture crops and vegetables, it is seasonal and within a year or two, the inputs such as seeds, fertilizer and so on can be changed. Bhutan can even export vegetables during summer when it is scarce in the bordering states of India. Gradually, production in the Agriculture sector can induce production in the Manufacturing sector also especially those that depend heavily on electricity.

Thus, Bhutan can specialize in the areas that have competitive advantage over India and then trade with India. If Bhutan can produce its own rice needs and vegetables allied with development in agro-industry, then there would be favorable trade balance for Bhutan.

The slow process of Rupee crunch began since from the start of FYPs in 1961 which was oblivious to the policy makers and government of Bhutan. The major causes of the Rupee crunch were perpetual current account deficit allied with unchecked credit growth and lack of INR reserve. The issue became critical in 2012 and there were quantitative restrictions placed by way of ban on vehicle import and restricting the loan on import of construction materials. Government even resorted to the sale of USD occasionally to meet the demand of INR and prevent the black market exchange rate in the bordering town. Today, people have the notion that INR issue is resolved, but the rationing of INR still continues indicating that the issue still persists. The demand for INR is met from the sale of USD reserve which is not sustainable as it only aggravates the aggregate demand for consumption. Unless, the structural changes take place in the economy, the Rupee shortfall will continue to remain.

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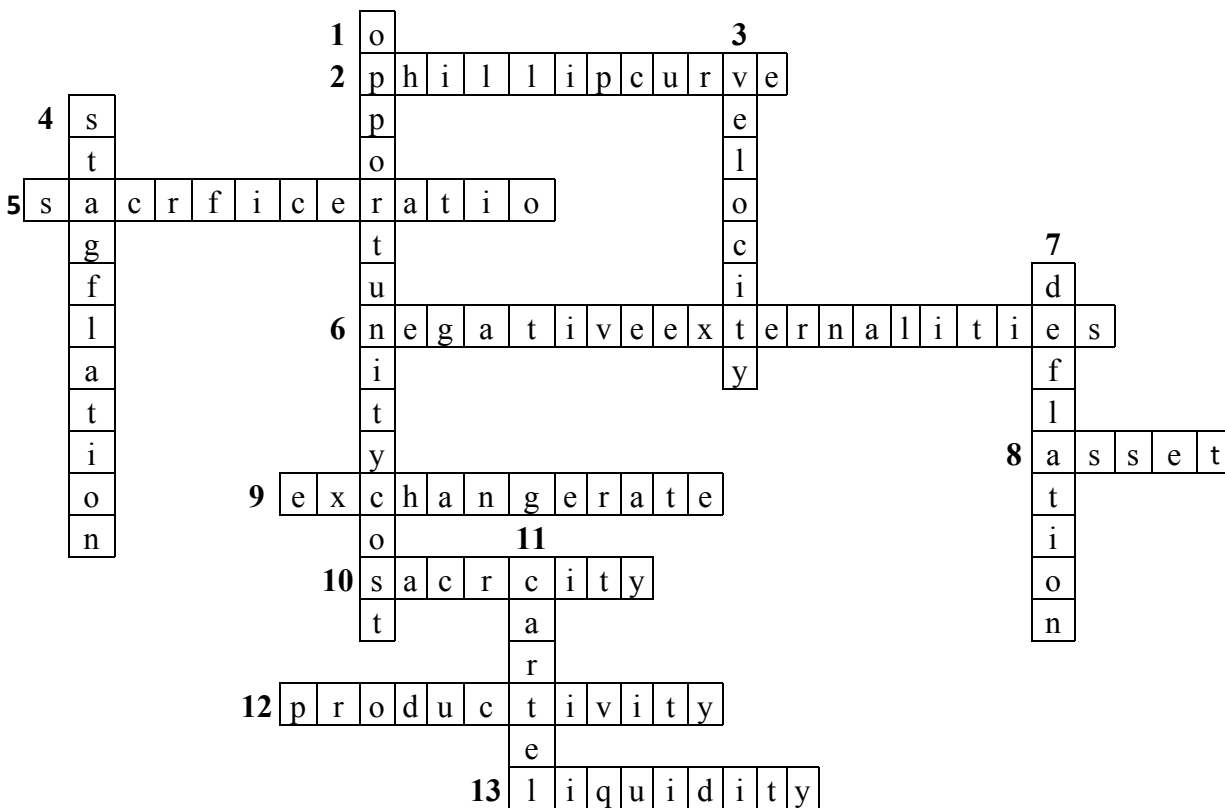
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## Events for REES—Fall 2016-17

1. Coffee Table discussion (every Friday)
2. Budding Economist of RTC  
-Written test and panel discussion ( will be held next semester)
3. ECONFLUENCE (25th-26th of October)
4. Academics guidance by Senior classes
5. Guest lecture

## Crosswords: Economic terms

### Answer from Last issue



#### Across

- 2. Phillip Curve
- 5. Sacrifice Ratio
- 6. Negative Externalities
- 8. Asset
- 9. Exchange Rate
- 10. Scarcity
- 12. Productivity
- 13. Liquidity

#### Down

- 1. Opportunity Cost
- 3. Velocity
- 4. Stagflation
- 7. Deflation
- 11. Cartel