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Economic and Development Cooperation between India and Bhutan since the End of the Cold War

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Abstract

Since the end of the Cold War, India–Bhutan relations have evolved into one of South Asia's most stable and enduring development partnerships, grounded primarily in hydropower-led economic interdependence and sustained development assistance. Over the past three decades, this bilateral cooperation has expanded beyond traditional aid frameworks to encompass multi-sectoral engagement in areas such as connectivity, trade facilitation, human resource development and emerging cross-border growth corridors. This paper examines the transformation of India–Bhutan economic and development cooperation from the early 1990s to the mid-2020s, highlighting how foundational pillars such as hydropower cooperation and plan-based financial assistance have been progressively complemented by new strategic priorities. Special attention is given to initiatives promoting regional connectivity, investment partnerships and sustainable urban development, particularly Bhutan's ambitious Gelephu Mindfulness City project, which reflects a shift toward diversified economic planning and border-region prosperity. Employing a qualitative historical–institutional methodology and systematic review of policy documents, official statements and project-level data, the study maps major agreements, flagship hydropower ventures and structured financial support aligned with Bhutan's Five Year Plans. It also critically examines persistent challenges, including project delays, environmental concerns associated with large hydropower infrastructure and the evolving dynamics of grant–loan financing. The paper argues that India–Bhutan cooperation has gradually transitioned from a predominantly project-based financing model to a more comprehensive "development ecosystem" approach. This emerging framework integrates energy trade with infrastructure development, private sector participation and community-level initiatives, thereby broadening the scope and impact of bilateral engagement. Overall, the study underscores how economic cooperation between India and Bhutan has adapted to changing regional and global contexts while continuing to reinforce mutual interdependence, sustainable development goals and long-term strategic partnership.

Keywords: India–Bhutan relations, Development Cooperation, Hydropower Diplomacy, Trade and Transit, Connectivity, Five Year Plans, Gelephu Mindfulness City.

Introduction

The post–Cold War period fundamentally restructured the economic logic of India–Bhutan cooperation by aligning Bhutan's development priorities with India's regional strategy and long-term neighborhood policy. As a small Himalayan state with a limited industrial base, Bhutan faced structural constraints in achieving rapid economic growth, its vast hydropower potential emerged as a strategic asset that could be transformed into a sustainable source of national revenue and development finance. In this context, India played a pivotal role as a principal financier, technical partner and guaranteed market for Bhutanese electricity exports. This partnership became deeply institutionalized through structured, plan-based assistance aligned with Bhutan's Five Year Plans, ensuring predictability and continuity in development financing rather than ad hoc aid. The energy-centered nature of cooperation is evident in landmark intergovernmental hydropower projects such as Chukha, Kurichhu, Tala and Mangdechhu, which collectively transformed Bhutan into a major exporter of clean energy while simultaneously supporting India's renewable energy goals. Over time, this model created a mutually reinforcing economic interdependence: Bhutan gained fiscal stability and development resources, while India strengthened its regional energy security and diplomatic influence. However, the relationship has not remained confined to hydropower alone. In the evolving regional environment of the 21st century, India–Bhutan cooperation has expanded into connectivity development, trade facilitation, cross-border infrastructure and investment partnerships. The renewal of trade and transit frameworks has helped Bhutan overcome the disadvantages of being landlocked by ensuring smoother access to Indian markets and ports. A significant contemporary shift is reflected in India's official endorsement of Bhutan's Gelephu Mindfulness City (GMC) project, which represents a new economic vision focused on urban development, regional connectivity and investment-driven growth in border regions. This initiative signals a transition from a narrow project-financing model to a broader development ecosystem that integrates infrastructure, private sector participation and community-level development. Against this backdrop, the paper examines how India–Bhutan economic and development cooperation has evolved since the early 1990s, identifies its major pillars and critically analyzes the constraints such as project delays, environmental concerns and financing structures along with emerging opportunities that will shape the future trajectory of this strategic partnership.

Energy Diplomacy Phase (1990s–2000s)

During the 1990s and early 2000s, India–Bhutan economic cooperation became firmly consolidated around two interlinked pillars hydropower-led development and structured plan-based assistance which together laid the foundation for Bhutan's modern economic transformation. In the post–Cold War context, Bhutan strategically adopted an export-oriented hydropower model, recognizing its abundant river resources as a sustainable pathway to growth. This model was heavily supported by India, which emerged as the principal financier, technical partner and assured buyer of electricity. The commissioning of the Chukha Hydropower Project (336 MW) marked a turning point, demonstrating how large-scale energy infrastructure could generate steady export revenue for Bhutan while contributing to India's clean energy needs. This success encouraged further expansion through mega-projects such as the Tala Hydropower Project (1,020 MW), which became one of the largest bilateral development ventures in South Asia. The financing structure typically a combination of Indian grants and soft loans reduced Bhutan's upfront fiscal burden while ensuring long-term income through electricity exports to India. This arrangement created a durable pattern of economic interdependence: Bhutan secured a reliable revenue stream to fund social and infrastructural development, while India strengthened regional energy security and deepened diplomatic ties. Parallel to hydropower cooperation, India institutionalized its development support by aligning assistance with Bhutan's Five Year Plans, thereby moving beyond ad hoc aid toward a systematic, planning-based partnership. Through this framework, Indian assistance financed critical sectors such as road connectivity, education infrastructure, healthcare facilities and public administration capacity-building. This approach enabled Bhutan to integrate external support into its national development strategy, ensuring coherence between domestic priorities and external financing. Over time, this dual-track cooperation energy exports and plan-based development aid created a predictable and stable financial architecture, allowing Bhutan to pursue long-term socio-economic goals with confidence. Thus, the 1990s–2000s phase represents a period of consolidation in which hydropower diplomacy and institutional development assistance together shaped the core structure of India–Bhutan economic relations.

Institutional & Social Development Phase (2010s)

During the 2010s, India–Bhutan economic cooperation entered a new phase characterized by institutional strengthening and a conscious shift toward community-centered development. One of the most significant developments of this decade was the institutionalization of trade and transit arrangements through the renewal of the *Agreement on Trade, Commerce and Transit* in 2016. This agreement established a largely free-trade regime between the two countries and provided Bhutan with assured transit facilities through Indian territory, which is crucial for a landlocked country dependent on external markets and seaports. By creating predictable and legally binding rules for cross-border movement of goods, the agreement reduced transaction costs, improved market access for Bhutanese exports and enhanced investor confidence. The continued validity of this framework into the mid-2020s, as noted on

Bhutan's official trade relations portal, demonstrates that bilateral economic engagement is no longer dependent solely on large development projects but is increasingly governed by rule-based institutional mechanisms. This shift represents the maturation of the partnership from project-centric cooperation to a structured economic relationship anchored in trade norms, regulatory predictability and long-term policy continuity. India's development assistance strategy diversified through the expansion of High Impact Community Development Projects (HICDPs). Unlike mega infrastructure projects, HICDPs are smaller, decentralized interventions aimed at delivering immediate and visible social benefits at the grassroots level. These projects focus on building schools, health centers, irrigation systems, rural roads, drinking water facilities and skill development centers across Bhutan. By directly targeting community needs, HICDPs strengthened social infrastructure and improved quality of life in remote and underserved areas. Official data from the Indian Embassy in Thimphu confirms that HICDPs formed a key component of India's committed support under Bhutan's 12th Five Year Plan, highlighting India's intent to balance macro-level development with micro-level social transformation. This dual approach combining institutionalized trade frameworks with people-centric development initiatives significantly broadened the scope of cooperation during the 2010s. It reinforced the idea that India–Bhutan relations are not limited to strategic infrastructure or energy diplomacy, but also prioritize inclusive development, social welfare and grassroots empowerment. Consequently, this decade marks a critical transition toward a more comprehensive and socially responsive development partnership.

Connectivity & Investment Phase (2020s)

The 2020s represent a transformative phase in India–Bhutan economic cooperation, marked by diversification of hydropower projects, innovative financing mechanisms and the emergence of new development narratives centered on connectivity and investment corridors. One of the most prominent trends is the continued expansion of Bhutan's hydropower sector through milestone commissioning of large projects such as Punatsangchhu-II. According to reports by the South Asia Subregional Economic Cooperation (SASEC), the commissioning of individual units of this project signifies a major step in enhancing Bhutan's power generation capacity and export potential. This expansion reinforces hydropower's centrality to Bhutan's economy while demonstrating India's sustained technical and financial involvement. The gradual operationalization of such mega projects ensures long-term revenue stability for Bhutan and contributes to India's clean energy transition, thereby maintaining energy interdependence as a strategic pillar of bilateral relations. A second significant trend in the 2020s is the adoption of new financing instruments to complement traditional grant-based assistance. While plan-based support remains important, India has increasingly relied on credit lines and concessional financing to strengthen energy ties. Reuters has reported that alongside the inauguration of hydropower projects, India extended substantial credit lines to Bhutan, reflecting a hybrid development toolkit that combines aid with structured financial instruments. This shift indicates a more sophisticated economic partnership where Bhutan gains access to flexible capital for infrastructure development, while India strengthens economic engagement through long-term financial linkages. Such diversification of financing tools also reflects Bhutan's growing institutional capacity to manage development loans and integrate them into national planning frameworks. The third and perhaps most forward-looking trend is the emergence of Gelephu Mindfulness City (GMC) as a new corridor-oriented development pivot. During His Majesty the King of Bhutan's official visit to India in December 2024, a joint statement issued by Bhutan's Ministry of Foreign Affairs confirmed India's political endorsement of this ambitious urban development project. GMC is envisioned as a cross-border economic hub aimed at promoting sustainable urbanization, investment inflows and regional connectivity, particularly in Bhutan's southern border areas. India's support for this initiative is significant because it reflects a strategic shift from a purely hydropower-centric engagement to a broader development ecosystem approach. By integrating infrastructure, private investment, tourism, digital services and logistics, GMC represents a new economic narrative focused on border-region prosperity and long-term regional integration. Collectively, these trends demonstrate how the 2020s have redefined India–Bhutan cooperation moving beyond energy dependence toward diversified growth corridors and innovative development frameworks that align with evolving regional and global economic dynamics.

Table 1: *Phases of India–Bhutan Economic & Development Cooperation (1990s–2025)*

ase	**me Period**	**ain Focus**	**y Features**
ase I	**90s–2000s**	ydropower + Plan Assistance	ergy-export model, grant–loan funding, Five Year Plan support
ase II	**10s**	ade Facilitation + Community Development	ade & transit agreement renewal, HICDPs, grassroots development
ase III	**20s**	nnectivity + Energy Expansion + New Corridors	natsangchhu-II milestones, credit lines, GMC border-development model

Hydropower & Energy Security

Hydropower cooperation continues to serve as the core foundation of India–Bhutan economic interdependence, shaping both countries' development trajectories since the post–Cold War period. According to official resources of the Government of India, major intergovernmental hydropower projects such as Chukha (336 MW), Kurichhu (60 MW), Tala (1,020 MW) and Mangdechhu (720 MW) have been successfully commissioned through bilateral collaboration, collectively transforming Bhutan into a significant exporter of clean energy. These projects dramatically increased Bhutan's installed power capacity and positioned hydropower exports as the country's primary source of foreign exchange earnings. Among these, the Tala Hydropower Project stands out as one of the largest joint ventures, with Bhutan's Ministry of Foreign Affairs highlighting its strategic importance and distinctive grant–loan financing structure, under which India provided a combination of financial assistance and concessional loans. This innovative funding model reduced Bhutan's immediate fiscal burden while ensuring long-term revenue flows through electricity exports to India. The strategic importance of hydropower cooperation is multifaceted. For Bhutan, it provides a stable revenue stream, strengthens fiscal capacity and enables the government to invest in social infrastructure such as education, healthcare and transportation networks. Hydropower earnings have become central to Bhutan's development planning and poverty reduction strategies.

For India, Bhutanese hydropower offers a reliable source of renewable energy imports, supporting India's climate commitments and energy diversification goals while reinforcing political stability in its Himalayan neighborhood. This interdependence has created a mutually beneficial relationship in which energy security and economic development are deeply intertwined. Furthermore, recent reports by *Reuters* indicate a gradual expansion of private sector participation in Bhutan's hydropower development, signaling a shift from purely state-driven cooperation to a more diversified implementation model. The growing involvement of Indian private companies reflects increasing investor confidence and introduces new dimensions of technical expertise, efficiency and innovation into project execution. This trend also aligns with India's broader economic diplomacy strategy of combining public sector leadership with private sector engagement in regional development initiatives. Hydropower cooperation has evolved from a bilateral development project framework into a strategic economic partnership that anchors India–Bhutan relations. By integrating long-term financing, infrastructure development and energy trade, this sector continues to act as the backbone of bilateral economic engagement, ensuring sustained interdependence, regional stability and shared growth in the Himalayan region.

Five-Year Plan Cooperation

India's development cooperation is closely aligned with Bhutan's Five Year Plans. For Bhutan's 12th Five Year Plan, India's mission documentation states a commitment of Nu./Rs. 45 billion, with components including Project Tied Assistance, High Impact Community

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Development Projects and Program Grant. Earlier MEA/official statements also record committed assistance figures for plan periods (e.g., Rs. 4500 crore for Bhutan's 11th Plan in one official release), reflecting the continuity of plan-based support.

Table 2: *Components of India's Development Assistance under Bhutan's 12th Five Year Plan*

omponent	**ırpose**	**idence (Source)**
oject-tied assistance	ıancing large and intermediate infrastructure and sectoral development projects	nbassy of India, Thimphu – 12th Plan details
ICDPs (High Impact Community Development Projects)	ecentralized, community-level projects with direct social impact	nbassy of India, Thimphu – 12th Plan details
ogram grants	ıdgetary and programmatic financial support to the Royal Government of Bhutan	nbassy of India, Thimphu – 12th Plan details

Source: Embassy of India, Thimphu (indembthimphu.gov.in)

This structure supports the argument that cooperation has matured into a financing architecture with both "big push" infrastructure and community-level interventions.

Trade & Transit Framework

The Agreement on Trade, Commerce and Transit, renewed in 2016, has emerged as a crucial institutional pillar of India–Bhutan economic relations by establishing a rules-based framework for cross-border trade and movement of goods. This agreement ensures largely duty-free access for Bhutanese exports to the Indian market and provides Bhutan with assured transit facilities through Indian territory to third-country markets. For a landlocked country like Bhutan, which lacks direct access to seaports, such guaranteed transit rights are economically vital. They significantly reduce transportation costs, logistical delays and procedural uncertainties that often constrain landlocked economies. By institutionalizing trade and transit rules, the agreement creates predictability and legal certainty for traders, investors and logistics providers, thereby encouraging higher trade volumes and private sector participation. The renewal of this agreement in 2016 also reflects the maturation of bilateral economic cooperation from project-based assistance to a more structured and legally anchored partnership. Rather than relying solely on political goodwill or ad hoc arrangements, the trade–transit framework embeds cooperation within formal regulatory mechanisms. This has strengthened Bhutan's external sector stability by safeguarding market access for key exports

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such as electricity, minerals, agricultural products and manufactured goods. At the same time, Indian traders benefit from simplified procedures and stable regulatory conditions, reinforcing mutual economic interdependence. The continuation of this agreement into the 2020s signals long-term commitment and policy continuity, which are essential for sustaining investor confidence. In an era of global supply chain disruptions and regional competition, having a stable trade governance structure shields Bhutan's economy from sudden external shocks. It also complements India's broader neighborhood policy by promoting economic integration and development-led regional stability. Thus, the Trade, Commerce and Transit Agreement functions not merely as a commercial instrument but as a strategic economic bridge that underpins long-term cooperation, supports Bhutan's development aspirations and reinforces India's role as Bhutan's primary economic partner.

Emerging Sectors: Agriculture, Environment and Human Development Linkages

Although hydropower remains the central pillar of India–Bhutan economic cooperation, the partnership has gradually expanded into emerging sectors such as agriculture, environmental conservation and human development, reflecting a more holistic approach to development collaboration. Recent media reports, including those highlighted by *The Times of India*, point to growing institutional cooperation in agriculture through initiatives such as farmer training programmes, exchange of best practices and capacity-building workshops aimed at improving productivity and sustainable farming techniques. These collaborative efforts are particularly significant for Bhutan, where a large segment of the population depends on agriculture for livelihood and where climate change poses increasing risks to food security. Similarly, environmental cooperation has gained prominence through joint afforestation drives, sapling exchange programmes and collaborative initiatives focused on biodiversity conservation and climate resilience. Such initiatives resonate strongly with Bhutan's global image as an environmentally conscious nation and align with India's commitments to sustainable development and regional ecological stability. While these activities may be smaller in scale compared to large hydropower projects, their developmental impact is deeply rooted at the community level. Agricultural training enhances rural incomes, promotes organic and climate-resilient farming practices and strengthens food systems, while environmental cooperation contributes to carbon sequestration, ecosystem preservation and disaster risk reduction. These softer dimensions of economic engagement also foster people-to-people ties, knowledge exchange and institutional networking between the two countries. Importantly, they help diversify the cooperation portfolio, reducing overdependence on energy-based engagement and broadening the developmental footprint of bilateral relations. Human development linkages such as educational exchanges, skill development programmes and technical training play a crucial role in strengthening Bhutan's human capital base. Indian institutions often provide scholarships, professional training and technical expertise, thereby contributing to Bhutan's long-term socio-economic capacity building.

Border Development & GMC Initiative

The Gelephu Mindfulness City (GMC) project represents a transformative development narrative in India–Bhutan relations, signaling a strategic shift toward border-oriented growth corridors and diversified economic engagement. Envisioned as a planned urban and economic hub in southern Bhutan near the Indian border, GMC is designed to attract investment, promote sustainable urbanization and strengthen regional connectivity. India's official political endorsement of this ambitious initiative was clearly articulated in the December 2024 joint statement issued during His Majesty the King of Bhutan's visit to India, where GMC was explicitly framed as a project that would enhance bilateral economic and investment linkages while contributing to prosperity in border regions. This endorsement is significant because it elevates GMC from a purely domestic Bhutanese development project to a bilateral strategic platform that aligns Bhutan's modernization goals with India's neighborhood and connectivity policies. Subsequent communications and credible reporting from Bhutanese and Indian official sources further reaffirm GMC's importance, portraying it as a flagship interface between Bhutan's internal economic transformation and India-linked regional connectivity. The project is expected to integrate sectors such as tourism, wellness industries, digital services, education, logistics and green infrastructure, thereby diversifying Bhutan's economic base beyond hydropower. For India, GMC holds strategic value as it complements broader regional connectivity initiatives and strengthens economic integration in South Asia's eastern Himalayan corridor. By facilitating cross-border movement of goods, services and people, GMC has the potential to transform border areas from peripheral spaces into dynamic zones of growth and cooperation. GMC also reflects a new development philosophy that combines economic growth with sustainability and well-being, resonating with Bhutan's Gross National Happiness framework. India's support for this vision demonstrates its willingness to engage with Bhutan's unique development model while simultaneously advancing shared economic interests. In this sense, GMC symbolizes the evolution of India–Bhutan cooperation from a hydropower-centric partnership to a multi-dimensional development ecosystem that includes urban planning, private sector participation, innovation and cross-border investment flows. As such, GMC is poised to become a cornerstone of future economic cooperation, reinforcing long-term interdependence and regional stability.

Constraints and Challenges

Despite its strengths, India–Bhutan economic cooperation faces recurring constraints:

1. **Project delays and cost escalations (especially in hydropower):** Large hydropower projects are complex and prone to geological and implementation risks. Milestone-based

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reporting around projects like Punatsangchhu-II highlights progress but also reflects the long gestation typical of mega-hydropower.

2. **Environmental and social concerns:** External studies and civil-society research have raised issues about river ecology impacts in hydropower development, emphasizing the need for stronger sustainability safeguards.
3. **Financing mix and fiscal sustainability:** Grant–loan mixes are central to the model. While they enable rapid capacity creation, the debt component can create fiscal sensitivities, particularly if projects face delays or if export revenues fluctuate. (This is an inference based on the widely documented grant/loan structure and typical megaproject risk profiles, the financing structure itself is explicitly described in official sources.)
4. **Changing regional context:** As Bhutan's external environment evolves, India's economic cooperation increasingly carries a "strategic reassurance" function as well something visible in high-level announcements combining energy deals, credit lines and investment support.

Conclusion

Since the end of the Cold War, India–Bhutan economic and development cooperation has undergone a remarkable transformation, evolving from a relationship largely centered on aid and hydropower into a broad-based, institutionalized development partnership. Hydropower continues to remain the backbone of bilateral economic engagement, supported by intergovernmental collaboration and structured grant–loan financing models that have enabled the successful commissioning of major projects such as Chukha, Kurichhu, Tala and Mangdechhu. These projects have not only strengthened Bhutan's export revenues and fiscal stability but have also contributed to India's renewable energy security and regional development strategy. At the same time, India's plan-based assistance aligned with Bhutan's Five Year Plans has expanded the scope of cooperation into critical social sectors, including education, healthcare, road connectivity and public infrastructure. The inclusion of High Impact Community Development Projects (HICDPs) further reflects a shift toward people-centric development, ensuring that cooperation delivers tangible benefits at the grassroots level and promotes inclusive growth across regions. Additionally, the renewal of the Agreement on Trade, Commerce and Transit has institutionalized a rules-based framework for cross-border trade, reducing uncertainty for traders and enhancing Bhutan's external sector stability, particularly in light of its landlocked geography. In the 2020s, the partnership has acquired a new strategic dimension, moving beyond a hydropower-centric narrative toward connectivity-driven development and investment linkages. India's official endorsement of Bhutan's Gelephu Mindfulness City (GMC) vision marks a significant milestone in this transition. GMC symbolizes a new growth corridor aimed at promoting sustainable urbanization, border-region

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prosperity and private sector participation, thereby indicating the emergence of a broader development ecosystem. This shift underscores India's commitment to supporting Bhutan's modernization while aligning with its own neighborhood and connectivity policies. Looking ahead, the sustainability of India–Bhutan cooperation will depend on several critical factors, including the timely completion of large infrastructure projects, the adoption of stronger environmental governance mechanisms to address ecological concerns associated with hydropower and the successful implementation of diversification initiatives in sectors such as tourism, agriculture and digital services. If effectively managed, these complementary strategies will ensure that energy interdependence continues to anchor the relationship while new sectors add resilience and depth to the partnership. Overall, India–Bhutan economic cooperation stands as a model of mutually beneficial development diplomacy, combining strategic interests with long-term commitments to sustainable growth and regional stability.

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