

Economic Issues in Brunei Prior to 2014 Oil Crisis

Isu-isu Ekonomi di Brunei Sebelum Krisis Minyak 2014

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ABSTRACT

The effects of falling oil prices are being felt by oil producing countries including Brunei Darussalam which forced them to take preventive measures. This is another great challenge for Brunei as Brunei is already lacking in diversification, its source of income is highly dependent on oil and gas. Thus, this paper focuses on the economic issues prior to the 2014 oil crisis and suggest recommendations what could have been done to solve the issues. This is important as Brunei is moving towards its national vision – Wawasan Brunei 2035, in formulating policies during the crisis, these problems and recommendations need to be taken into consideration. The methodology of this paper is based on literature reviews from journals, books, annual reports, and newspapers which are related with keywords and research area. Several important policies are believed to be able to help in accelerating the development of the country and the major reforms are identified. Undoubtedly, Brunei has always the potential for development, but it is how Brunei uses the available resources efficiently and effectively with help of a good set of policies and governance.

Keywords: *Diversification, Economy of Brunei, Economic Growth*

ABSTRAK

Kesan kejatuhan harga minyak sedang dirasai oleh negara-negara pengeluar minyak termasuk Brunei Darussalam yang memaksa mereka untuk mengambil langkah-langkah untuk pencegahan. Ini merupakan satu lagi cabaran besar bagi Brunei kerana Brunei kurang dalam mempelbagaikan hasil, sumber pendapatan amat bergantung kepada minyak dan gas. Oleh itu, kertas kerja ini memfokuskan kepada isu-isu ekonomi sebelum krisis minyak 2014 dan mengemukakan cadangan yang perlu dilakukan untuk menyelesaikan isu-isu. Ianya amat penting kerana Brunei sedang menuju ke arah wawasan negara - Wawasan Brunei 2035, dalam merumuskan dasar ketika di dalam krisis, masalah-masalah dan cadangan-cadangan ini adalah perlu difikirkan atau diambil kira. Metodologi kajian ini adalah merujuk kepada kajian lepas dari jurnal, buku, laporan tahunan, dan surat khabar yang berkaitan dengan kata kunci dan bidang penyelidikan. Beberapa dasar penting yang dipercayai boleh membantu dalam mempercepatkan pembangunan negara dan penyusunan semula dapat dikenal pasti. Tidak dinafikan, Brunei sentiasa ada potensi dalam pembangunan, tetapi ia perlu dilihat kepada bagaimana Brunei menggunakan sumber yang ada dengan cekap dan berkesan dengan bantuan set yang baik dalam polisi dan kerajaan.

Kata kunci: *Kepelbagaian, Ekonomi Brunei, Pertumbuhan Ekonomi*

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Introduction

Brunei Darussalam (herein 'Brunei') as a resource-dependent country is believed to be the main cause of its slow growth in its development. Economic diversification and reliance on oil production have always been the problem since Brunei's first national development plan. Brunei only has 18 years to realise Wawasan Brunei 2035. Wawasan Brunei 2035 goals are: the accomplishments of its well-educated and highly skilled people; the quality of life; and the dynamic, sustainable economy (Department of Economic Planning and Development, 2007). However, the effects of falling oil prices are being felt by oil producing countries including Brunei which forced them to take preventive measures. In this paper, several important questions are explored. This paper attempts to answer all the important questions and explore options by discussing the most important policies for accelerating development of Brunei prior to oil crisis in 2014. Thus, content analysis is used by reviewing journal articles, books, annual reports, and newspapers which are related with keywords and research areas.

The paper is organized as follows: the second section briefly introduces development theory which explains the relation of natural resources exploitation and development. The third part of the paper introduces the economy of Brunei prior to 2014 oil crisis, followed by the identification of the factors contributing to the slow development of Brunei. The fifth part will explain the efforts towards the development of Brunei prior to 2014 oil crisis and some important policies will be suggested in the next part. Finally, concluding comments will be offered.

Development Theory

Blomqvist (2010) states that development economists found out that there is a negative relation between resource abundance and economic growth, and a positive relation between a resource abundance and internal conflicts. Therefore, these problems lead to phenomena of rentierism and Dutch disease. These theories are used in order to analyse the situation of Brunei which leads to its slow development.

The slow development as a result of highly dependence on oil and gas is also a phenomenon of Rentierism. Ngwu and Ugwu (2015) explains that rentierism is a general theory to explain why natural resources harm the development of the endowed states. According to Hashim (2010), the economy of Brunei resembles a rentier economy as its revenue solely depends on oil and gas and pays less attention to the non-oil sector. This is supported by Blomqvist (2010) who suggests that by looking at the nature of Brunei's economy, it is best to refer Brunei as a 'rentier state' as most of the national income comes from its natural resources (Blomqvist, 2010).

Yaakub (2012) explains the basic theory behind the phenomenon of Dutch Disease is that when there is an increase in revenue from natural resources, it will deindustrialize a nation's economy by raising the exchange rate which makes the manufacturing sector less competitive. On the other hand, it is an economic concept that tries to explain the seeming relationship between exploitation of natural resources and a decline in the manufacture sector (Yaakub, 2012). According to Yaakub (2012), the existence of Dutch disease in Brunei's economy can be verified as Brunei's economy has shown some sign of weaknesses in the past years especially after the Asian financial crisis.

Brunei in Brief

Brunei is one of the richest countries in the world as a result of its abundant hydrocarbon resources which is the backbone of its economy (Blomqvist, 2010). Brunei is a Sultanate country and the development is based on the philosophy of Malay Islamic Monarchy (MIB). In Southeast Asia, Brunei is the fourth largest oil producer and the oil and gas sector contributes more than half of the country's Gross Domestic Product (GDP) and 90 per cent of its exports (Southeast Asia Globe, 2013). The GDP of Brunei per capita in the year 2012 was \$48,000 in international dollars (Southeast Asia Globe, 2013). As a result of the oil and gas, Brunei manages to perform well above its weight in international politics as a member of the Association of South East Asian Nations, ASEAN (Blomqvist, 2010).

Todaro and Smith (2010) define the developing world by using per capita income and they classify developing countries as those countries with low-, lower-middle, or upper-middle incomes. However, from their analysis, they finally classify Brunei under high income economies in which they measure by Gross National (GNI) per capita. Brunei was ranked 37th with US\$36,710 (World Bank, 2015). High-income countries are those countries with US\$10,726 or more as defined by World Bank in 2005 (Oshodi, 2014).

The living standard of Brunei is considered to be good. This can be looked at the average income per household and the value of Human Development Index (HDI). In 2010/11, the average monthly income per household in Brunei was BND 5,670, where, an urban household received BND 5,822 per month while a rural one receives BND 5,212 (USD 2,445) per month (Department of Economic Planning and Development, 2013). From the figure, it can be seen that there are no significant differences between the urban and rural in the average income. This is further supported by United Nations Development Programme, UNDP (2013) where in term of HDI, Brunei was ranked 30 out of 187 countries in 2012 based on UNDP report and the HDI's value increased from 0.765 to 0.855 between 1980 and 2013 which shows an increase of 12 per cent with 0.3 per cent on annual basis. In addition, Brunei was ranked second among Islamic countries for its Islamic Human Development Index in 2007 by HDR, IDB and WDR (Anto, 2009).

However, there is a question whether the presence of oil and gas sector is a blessing or curse. According to Siddiqui, Athmay and Mohammed (2012), Brunei hydrocarbon reserves are declining since the last several decades and its oil reserves are declining. This is supported by Tasie (2009) stating that sales from oil and gas and the investment enable Brunei to sustain itself until 2020. Therefore, the major concern is, Brunei's ability to sustain the reserves and income after 2020. This is a very important question to ask. Otherwise, it will greatly impact the development of Brunei.

Main Issues in Brunei's Economy

Several studies have been done to identify the important factors which led to the slow growth of development. After reviewing all the literatures, it is believed that there are five major causes contributing to the slow development of Brunei.

Firstly is the problem of overreliance of oil and gas. Brunei's economy has always been blessed by its oil and gas. However, there is another side to the coin. Kong and Fernandes (1991) come up with the important questions, such as, whether the oil industry function as a dominant sector will gradually promote the development of other related industries. If there is an increase in income, will this expand the size of the domestic market which leads to economies of scale and results in the diversification? And how about the use of a large sum of petro-dollars by government to build up a broad and

expanded economic base? This is very important as creating job opportunities has been an ongoing economic goal where an average of 2,500 jobs have to be created annually (South China Morning Post, 2000). However, in 2011, about 18,815 people were unemployed (Department of Economic Planning and Development, 2015). Thus, the dependency on oil and gas led to the problem of unemployment.

Secondly, the slow development of Brunei is the bureaucratic environment for private business. Private sectors play important roles in a country's development such as diversification for economy and provision of jobs for the locals. It can be seen when there is a problem of unemployment due to a discouraging number of companies in private sector in Brunei. Yaakub (2012) explains that new jobs would have been created in the private sector but the 8th National development plan saw a 50 per cent reduction in the government's development spending in this sector. In addition, there are some limitations faced by new businesses, for instance, in hiring the employees. Some new businesses normally require the use of foreign labour. However, to get the permit to employ them is not easy and the process is very time consuming (Blomqvist, 2010). This discourages the private sectors from growing in Brunei's economy.

The third reason is the over-generous public employment. Siddiqui, Athmay and Mohammed (2012) explain that the Brunei government, since its dependency in 1984, has raised the standard of living by providing free health and education, high salaries for government employees, low domestic prices of oil, gas and local landline calls, housing grants, interest-free housing loan and old pensions, while Brunei has been continuously investing the budget surplus in foreign countries. Furthermore, working with the government has always been rewarding, which results in overstaffing which thus reduces efficiency and not improvement (Blomqvist, 2010). Blomqvist (2010) suggests that there should be efforts to reduce privileges of local citizens by offering less attractive welfare package, but retaining the support for the general public will help to solve the problem of diversification problem. This is mentioned by Crosby (2007) pointing out that the weaknesses of Brunei's economy do not lie on the macroeconomic framework. Instead, the slow progress in diversifying its economy, thus, it leads to slow economic diversification.

The fourth reason is its small market size and the non-oil private sector (Hashim, 2010) and severe domestic constraints on the supply side (Duraman, 2011). According to Duraman (2011), the small market has always been the reason of slow development of Brunei. A high per capita income generates strong purchasing power which reflects a strong demand for certain commodities and this is proven by a high demand for imported goods which cannot be produced locally. Therefore, it lies on the supply side related to the government roles which constitute regulations and policies (Duraman, 2011). To grow an industry, the government must design regulations which do not hinder its growth and instead encourage a good environment to promote its growth. Therefore, the key point here is, Brunei should start on economic diversification and the growth of private sectors. The growth of local industries to substitute the imported products is seen to give a lot of benefits to Brunei and this will be further explained and analysed in the later paragraph.

The main problem identified is that of unemployment among the Brunei citizens especially the youth and university graduates. Siddiqui, Athmay and Mohammed (2012) have identified that the major macroeconomic issues in Brunei are an increasing number of unemployed youths and the economy still relies heavily on the oil sector. Siddiqui, Athmay and Mohammed (2012) report that the rate of unemployment among locals now is 12 per cent. The percentage is quite high compared with 4.7 per cent in 1991 and 4.9 per cent in 1995 (Tasie, 2009).

The problem with unemployment in Brunei is that educated Bruneians have a strong preference to work in government sector which results in lack of training or skills as

required by employers and loss of interest in taking risk to become entrepreneurs (Blomqvist, 2010). This is a reason why Bruneian citizens are not enterprising as they are reluctant to opt for jobs outside the government and refuse to do manual works. Bruneians are generally well educated. However, the qualifications they have are not in demand in the labour market and as a result, both newly and existing established firms seek to employ foreign labour.

Policy Recommendations

The challenge of the government is to move away from dependence on petroleum resources and pursue a path of sustainable economic development. Therefore, what are the best policies which can be seen to promote the development of Brunei? On top of all policies, there should be one important factor which acts as a leverage point which could give multiplier effects, thus accelerating the development. The policy is import substitution.

The first major reform that Brunei should pursue is through import substitution. This paper believes that this is a leverage point of Brunei's development. Yaakub (2012) explains that import substitution is an important factor for Brunei to work on as this will allow the creation of new and potential industries that will replace imports with domestic production. This will, on the other hand, result in multiplier effects to the locals, thus reducing the externalities such as unemployment. Clunies-Ross, Forsyth and Huq (2009) explain that the policy of import substitution was designed in order to allow industrialization in poor countries free from the competition of well-established developed countries especially in exports, thus allowing the growth of the poor countries.

The creation of new industries will need to identify the factors that are lacking in its development. It opens up the opportunities for the locals in such a way that will unleash the potential of the locals. As the current job market can no longer absorb the increasing number of graduates, it will also be run by the private sector. The positive effect is that in the long run, it will encourage local entrepreneurs to go to industrial production where a market already exists, the characteristics of the goods demanded are known and nascent domestic industries can be protected in a straightforward way from import competition (Yaakub, 2012). However, Brunei is seen to be in their early stage, thus giving too little protection runs the risk of not encouraging any new industrial activity at all (Yaakub, 2012). This is important for the purpose of protection of infant industries. Brunei needs to secure its economy or market before it is opened for competition, thus will correct or promote the economic stability. On the other hand, Yaakub (2012) explains that limiting the protection, otherwise, will lessen the pressure to increase productivity and led to demands for indefinite continuance of favoured treatment. Therefore, the policies have to be properly monitored and good governance is the key to make sure that it will be a success.

Another policy is to protect the infant industries. In other words, securing its market before join the international market and work on its economic base. Tisdell (1997) explains that Brunei's major challenge to accelerate its development now is that Brunei is just a small market and yet it faces a strong competition from neighbouring countries particularly Singapore. Therefore, it is better to secure the local industries first before Brunei opens its economy for international market. Therefore, it is best to work on the economy base. Tasie (2009) explains that broadening the economic base will create more job opportunities for the locals.

The next policy is privatization to promote development. It can be seen that the slow rate of development due to overreliance on oil and gas sector. Most of the budget allocation are channeled on government sector and social welfare. Thus, a key to the development is through privatization. The benefit of privatization in Brunei is not only that it will reduce the government's administrative and financial burden but also that it will encourage the growth of private sector and their participation in the country's development, thus will accelerate economic diversification and development (Tasie, 2009).

The next policy is Brunei should continue oil exploration and production but invest the oil revenues in productive non-oil sectors so as to sustain the income stream (Duraman, 2011). As oil and gas is a core part of the economy, it is not wise to stop totally or go for a drastic reduction. Brunei must maintain the conservation policy or increase exploitation, provided that the fund must be invested as the future demand for oil and gas is strong, therefore, prices are likely to increase in the future, therefore, appropriate strategy needed and provide incentives (Duraman, 2011). The most important part is how the money obtained from oil and gas sector being utilized and invest properly and channeled for the purpose of a development. This is because investment in other form of capital, such as infrastructure and human resources, will sustain incomes after oil resources have been exhausted and the development of these resources is crucial in efforts to diversify the economy (Duraman, 2011). On top of that, Brunei may consider the exploitation of its renewable energy as Brunei is seen to have potential in its agriculture and ecotourism as well as developed selected manufacturing and service industries (Duraman, 2011).

The last policy is to enhance research in terms of development from Islamic perspective, so that, it will correct the perception on Islam in development. In terms of Islamic Human Development Index (I-HDI), the nature of the country, Brunei has the potential to be a good economic model of Islamic Economy. Therefore, there are a lot of potential industries can be set up, such as Islamic Tourism. Thus, Brunei can attract a large number of Muslim or non-Muslim tourists to experience the different environment of tourism. For instance, Korea is using Brunei's halal certification system in order to help to increase awareness about halal in the East Asian country to allow export of their products to the Middle East (Shahminan, 2013). Therefore, Brunei has always the potential in promoting new industries. It only needs a good set of policies and governance.

Conclusion

It is obvious that the main problems Brunei is facing in terms of development are the dependency on Oil and Gas sector, small market size, and the reliance on government sector for jobs. Brunei has always the potential for development, but Brunei needs to use the available resources efficiently and effectively with help of a good set of policies and governance. Based on the review of literatures above, it can be concluded, major reforms need to be done through import substitution, resulting in multiplier effects which help to improve Brunei in different ways. It will also prepare Brunei for international market. This is very important as Brunei seeks ways to diversify industries for a sustainable economy, less reliance or away from oil-based production, and jobs generation. In addition, Brunei as a Muslim country has the strength in tourism industries, including Islamic tourism which could help Brunei to generate alternative revenue during low oil prices crisis. However, government intervention is required at an early stage. To grow an industry, the government must design regulations which do not hinder its growth and encourage a good environment to promote its growth without compromising local infant industries. The regulations designed need to attract the locals to work at private sectors. No doubt, Brunei has always

the potential for development, but Brunei needs to use the available resources efficiently and effectively with help of a good set of policies and governance. Thus, the development of the country can be accelerated, and Wawasan Brunei 2035 can be realized.

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