

ECONOMIC THEORY, APPLICATIONS AND ISSUES

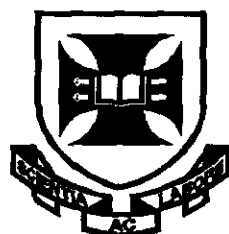
Working Paper No. 12

**Tourism as a Contributor to the Economic
Diversification and Development of Small
States: Its Strengths, Weaknesses and
Potential for Brunei**

by

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† Professor of Economics, The University of Queensland, Brisbane 4072 Australia.
Email: c.tisdell@economics.uq.edu.au

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For more information write to Professor Clem Tisdell, School of Economics, University of Queensland, Brisbane 4072, Australia or email c.tisdell@economics.uq.edu.au

Abstract

Tourism as a Contributor to the Economic Diversification and Development of Small States: Its Strengths, Weaknesses, and Potential for Brunei

As a rule, the economies of small states lack economic diversification and scope for diversifying their economic activities is limited compared to large states. One of the reasons for this is that they lack a diversified natural resource-base due to their small geographical area. In a globalising world economy involving greater freedom of trade and capital movements, the economies of small states are liable in most cases to become more specialised and vulnerable to external economic conditions. Therefore, policies are sometimes adopted by these states, or recommended by external agencies, to keep these economies more diversified than otherwise would be so. For instance, action to simulate tourism development is sometimes a part of the diversification strategy of small states, such as Brunei.

While tourism development can make a significant contribution to the economic diversification and development of small states, its limitations must be recognised. In small states, these can include significant income-leakages via imports and overseas remittances of profit by foreign investors in the tourism industry, adverse cultural impacts on the local community, unfavourable environmental consequences, little employment of locals because of (needed) reliance on guest-workers or expatriates, and where the industry relies heavily on inbound tourists, a high degree of economic volatility. Sometimes, it is even possible for growth in tourism to reduce the diversity of a local economy and generate the “Dutch disease”. Much depends on the particular circumstances because the tourism industry can also act as a growth pole and stimulate the development of other industries via backward economic linkages. Furthermore, it can provide a profitable extra economic opportunity for small states that have limited economic alternatives. Therefore, depending on its nature, the tourism industry can make a positive contribution to the economic diversification and development of small states.

Brunei aims to become a “Service Hub for Trade and Tourism (SHuTT)” in its region. In this paper, once the general review of tourism as a contributor to the economic diversification and development of small states is completed, Brunei’s basic policies for SHuTT are outlined and examined, paying particular attention to the tourism component.

Tourism as a Contributor to the Economic Diversification and Development of Small States: Its Strengths, Weaknesses, and Potential for Brunei

1. Introduction

Small nation states, such as Brunei, usually lack economic diversification and usually have limited possibilities for diversifying their economies compared to larger states. Reasons can include the particular nature of their natural resource-base, as in Brunei, and the small size of their domestic market. The latter may hamper the development of manufacturing and tertiary industries requiring substantial scale economies in order to be competitive internationally. In addition, since it is widely predicted, on the basis of economic theory, that increased free trade fosters greater specialisation in economic activity, economic globalisation is likely to result in the economic activities of small nations becoming less diversified. While this may increase their income in the short- to medium-term, it is liable to increase their economic risks and may result in their unsustainable development (Tisdell and Fairbairn, 1984).

In order to respond to this possibility, Brunei aims to diversify its economy so it will be less dependent on crude oil and natural gas for its future economic prosperity. As a part of this strategy, the Government of Brunei has a vision and a mission of creating Brunei Darussalam as a Service Hub for Trade and Tourism by the year 2003 (The Government of Brunei Darussalam Official Website, accessed 25/09/01). The Government of Brunei believes that Brunei has a promising opportunity to be a service hub for trade and tourism in the BIMP EAGA, that is the Brunei, Indonesia, Malaysia and Philippines East Asian Growth Area. As pointed out by the Sultan, Brunei is engaged in a long-term national programme of economic diversification. "This involves becoming a service hub for tourism for Borneo Island and its surrounding areas" (Bolkich, 1999, p.34).

The program to make Brunei Darussalam a service hub for trade and tourism ('SHuTT') aims to promote the following:

- “ • Import and export through Brunei Darussalam
- Travel to and through Brunei Darussalam
- Do your business in and through Brunei Darussalam
- Communicate from and through Brunei Darussalam ”

(The Government of Brunei Darussalam Official Website, accessed 25/09/01).

The development of tourism clearly plays an important part in this strategy as does boosting the number of all visitor arrivals to Brunei whether their visits are for the purpose of tourism, business, visiting relatives, transit or otherwise. All these aspects are important in promoting Brunei for SHuTT, and in this context tourism should be interpreted in a broad sense.

In this paper, the advantages and disadvantages of tourism as a means to diversify and develop small economies generally are outlined first. Then the nature of tourism in Brunei and its potential for development are considered.

2. The Advantages and Disadvantages of Tourism for the Economic Diversification and Development of Small States

For small nation states having few possibilities to diversify and develop their economies sustainably, tourism can sometimes provide a valuable economic opportunity. As a rule, all profitable possibilities to diversify such economies are to be welcomed. Nevertheless, international tourism is a highly competitive industry and as a result of modern transport systems, foreign tourists have a lot of opportunities these days to choose from. The returns from developing the tourism industry in a small state will depend on its ability to meet foreign competition. This ability needs to be assessed specifically for each small state under consideration. The cost and time taken to travel to the country and whether or not it is en route to other destinations or on an isolated spur in travel routes (such as are Tuvalu, and some other Pacific island nations) can all have an influence. Furthermore, the attractions of the country and the cost of these and of staying there must all be assessed against substitute destinations and activities. Tourism is not a magical industry for economic growth but its development can provide some nations with worthwhile economic opportunities.

Countries able to provide tourist attractions that are relatively unique and not able to be easily replicated by other nations should enjoy a long-term competitive advantage in tourism from these (Tisdell, 2001, Chs. 5&10; Khan, 1986). Features may include unique man-made objects e.g. the Sphinx and pyramids in Egypt and other antiquities, and natural wonders such as the Grand Canyon in the United States or unique wildlife

attractions as in African and in Borneo. On the other hand, if the country's main tourist attractions can be easily replicated by other countries, its long-term competitive position will depend on its being able to supply its tourism services at lower costs than competitors or potential competitors. Many of Singapore's tourist attractions are man-made and can be replicated. Examples of tourist attractions that can be replicated include theme parks and gambling casinos. Some of these attractions are subject to tourism product cycles (Tisdell, 1991, Ch.10), and area-related or environmental tourism cycles (Butler, 1980). Where the type of tourism being considered for development is subject to a product cycle, profit from investment in such tourism depends upon the stage at which entry into this type of tourism occurs. If entry occurs in its expansion phase above normal returns may be obtained, but entry in the mature phase is liable to bring little return. In the mature phase, the industry can be expected to be highly competitive because at this stage of the product cycle, tourists having many competing opportunities to choose from. In the circumstances, suppliers unable to meet the competition can expect to make a loss.

Tourism development can provide a means to diversify the product-mix of a small economy. Diversification often provides a means to reduce economic risk and volatility in incomes. For example, it is possible that the development of a tourism industry catering for foreign visitors could reduce the volatility of a small nation's foreign exchange earnings. However, such diversification is not always effective in this regard and in some cases, it may actually increase the volatility of foreign exchange earnings and macroeconomic uncertainty.

If the volatility of foreign earnings from tourism are greater than from existing imports and if the level of these earnings are highly and positively correlated, then the development of a tourism industry based on foreign tourists, although it adds to economic diversification, will increase the volatility of foreign exchange earnings and may add to macroeconomic uncertainty. Nevertheless, if the earnings from tourism are large enough and if other national industries are declining or less competitive, a government may still opt to encourage the development of tourism. However, that development, even when it results in economic diversification, may bring less rather than greater economic security to the nation.

In this regard, the findings of Sinclair and Tsegaye (1990) are worth noting. They examine data for several industrialised and for several developing countries to determine whether their diversification into the non-traditional tourism sector has decreased the instability of their export earnings. They find that “although tourism has the advantage of high growth rates and is a major source of foreign currency receipts, earnings from tourism did not bring about a significant decrease in the instability of export earnings of most of the developing and industrialised countries considered. Furthermore, a net increase in the instability of earnings from tourism and merchandise exports occurred in a number of countries, and this may be a particular problem in small, open developing economies” (Sinclair and Tsegaye, 1990, p.487).

There are several characteristics of international tourism that make it inherently volatile. First, demand for it is highly income elastic. When economic conditions in source countries for tourists deteriorate and incomes and employment prospects decline, such as occurred with the Asian financial crises, demand for international tourism and travel declines sharply. Secondly, unlike for the export of physical commodities and for many (but not all) services, foreign exchange income from tourists is dependent on the customer (in this case the tourist) actually visiting and staying in the host country. The customer is therefore subjected to personal risk. Major depression in tourist visits to a country can occur because of war, terrorist acts, epidemics and, in general, heightened risks to the health and safety of visitors, including deterioration in law and order in the host country. Most international tourists feel extremely vulnerable, especially if they are in a country with a different culture and language, since they do not have with them their usual social support systems and often lack knowledge about how to obtain help in their host country if some disastrous event occurs.

To some extent, the risks from developing a tourism industry based on foreign tourists can be reduced by diversification within the tourism industry itself. For example, it may be possible to diversify the countries of origin of visitors and the tourism market segments catered for. While this can reduce risk, it is unlikely to eliminate it completely.

Another problem, especially for modern sectors of the tourism industry, such as hotels, airline services and airports is that a large proportion of their cost is fixed or overhead

cost (cf. Kotas, 1982). Consequently, if demand for their services falls and excess capacity arises, they are liable to suffer losses (see Tisdell, 2000, Vol.I, pp.xxix-xxxi). For example, hotels usually need to operate at a minimum of two-thirds designed capacity just to break even (Lundberg et al., 1995). A similar situation may exist for airlines. In a highly competitive situation, it is possible that hotels and similar tourism services can all operate with excess capacity and just make an average return on their capital (cf. Tisdell, 2000, Vol.I, p.xxxiii). In such cases, they are extremely vulnerable to any depression in general demand for their services, as occurred for many airlines after the terrorist attacks in New York and Washington in September 2001.

It may, however, also be the case that many modern extractive industries and manufacturing industries have high overhead costs, and that their profitability is highly sensitive to the degree to which their designed capacity is utilized. Most capital-intensive industries in modern societies rely for their profitability on demand of their product remaining high enough to ensure a high degree of capacity utilisation of their plants.

It is sometimes suggested that foreign tourism is a much less attractive means to develop small economies (or remote regions) than may appear to be so at first sight. This is based upon the view that import leakages are very high for foreign tourism in a small country (Britton, 1982; Archer, 1989). But the importance of such income leakages can be exaggerated. The net income remaining in an economy is more important than that which leaks away. An industry with a high leakage can make a higher income injection than one with a low leakage if the gross income earned by the former is much higher (Tisdell, 1993, pp.171-190). Furthermore, most modern industries located in small economies have relatively high import leakages (cf. Prasad and Tisdell, 1998).

In some cases, development of a local tourist industry can be highly dependent on guest workers. This may be because locals are not keen to perform menial tasks associated with tourism e.g. housekeeping or cleaning duties in hotels, or they may lack language and cultural skills needed to cater for hosts. For example, the resort industry in the Maldives is highly dependent on foreign personnel (Sathiendrakumar and Tisdell, 1989). Even in relation to Japanese tourism in Australia, considerable use is made if

Japanese guest workers because of their language skills and cultural knowledge. This implies that either locals do not like to accept all the types of jobs created by foreign tourism, or that they are not prepared or able to develop all the skills and knowledge necessary to service it competitively.

Kakazu (1994, Ch 5) demonstrates that the Northern Mariana Islands has become highly dependent on migrant workers for the development of its tourism industry and its tourism industry tended to 'crowd out' its traditional industries therefore, a kind of 'Dutch disease' has arisen. The tourism industry has not been a 'growth-pole' for the Northern Mariana Islands, whereas in parts of China, such as Yunnan, it may constitute a growth pole or key industry to stimulate development (Wen and Tisdell, 2001).

Note that it can be unwise to try to stem import leakages. For example, some imports may be essential to cater for the tastes of foreign visitors. In the absence of such imports, their demand for visits may collapse.

There are also environmental and sustainability issues to consider in relation to tourism. Tourism is sometimes considered to be a 'green industry' (Wen and Tisdell, 2001) or an environmentally benign industry. But tourists and the tourist industry unless well managed are capable of having serious adverse environmental consequences. These may arise from provision of services for tourists and wastes from tourists e.g. water supplies, energy supply, sewage disposal, destruction of natural environments to make way for the provision of tourist facilities such as roads airport, resorts and hotels, and destruction directly by tourists e.g. coral collection by tourists, destructive graffiti on tourist attractions. The list of possible adverse environmental effects from tourism can actually be quite long.

On the other hand, if tourism is developed in a manner sympathetic to the environment, as is a goal of ecotourism, it may be more supportive of environmental protection than alternative industries. It can be an environmentally friendly industry. Particularly, in the case of ecotourism, it can provide a positive economic incentive to conserve nature. It can provide a stimulus to the conservation of biodiversity. As in the case of most industries, the environmental impact of tourism depends on how well it is managed. By

good management, it is possible to develop a tourism industry that is environmentally friendly and relatively sustainable.

In some countries, concerns also arise about possible adverse social impacts from tourism. There are fears that it may, for example, undermine established values in the host country, contribute to crime, prostitution and disorder. However, much seems to depend on how the host country itself addresses such matters. If the nation acts in a disciplined way, as for example, has been done Singapore, the problems may be few (Khan et al., 1988) and in fact, the disciplined safe-nature of the host country may be a positive attraction for the bulk of tourists. The Maldives copes with this problem by geographically separating tourists from the mainstream of society. In some previous communist countries, guided group tours were favoured as a means of separating tourists from the rest of society. In practice, it seems likely that most tourists interact little with local residents in their host countries. Their contacts are probably limited, in most cases, to those servicing tourism, and are strictly of an impersonal business nature. It is, however, true that tourists can cause offence to locals if they do not respect local customs. This problem may be addressed by making visitors aware of local customs, and by also encouraging local residents to show some tolerance of those not a part of their society and culture.

To conclude this section, the development of tourism can provide profitable opportunities to small nation states to diversify their economies if appropriate preconditions are satisfied. However, tourism is not a magical industry for creating economic wealth and reducing economic uncertainty and volatility. In fact, in the modern globalised world, there do not seem to be any such magical industries.

3. Features of Inbound Tourism to Brunei and the Potential for Further Development

Consider now features of inbound tourism to Brunei Darussalam and the potential for further development of its tourist industry.

The first feature to note is the mode of passenger arrivals in Brunei. Arrivals are predominantly by land, presumably mostly from the surrounding Malaysian states, then follows arrivals by sea and air in that order (see Table 1). Arrivals by sea fell in the

1990s compared to the 1980s. Arrivals by land showed the most rapid proportionate increase followed by arrivals by air (Table 1).

Table 1 Passenger Arrivals in Brunei, 1987 and 1992 by Mode of Transport – Numbers and Percentages, in Parentheses

Year	Total	Air	Sea	Land
1987	904,862	189,348	317,893	397,585
	(100)	(20.9)	(35.1)	(44.0)
1992	1,156,992	253,140	278,588	625,264
	(100)	(21.9)	(24.1)	(54.0)

Source: Basic data from The Government of Brunei Official Website b. Accessed 25/09/01

Most of the arrivals in Brunei are accounted for by returning residents and this proportion has been rising (see Table 2) in relation to total arrivals. Between 1987 and 1992 it seems to have risen from around half to almost two-thirds. It is apparent that Brunei residents make more visits abroad than are made by foreigners to Brunei. In view of this overall situation, it seems likely that Brunei has a substantial deficit on its external tourism account, and this deficit might be rising rather than falling. The exact figures do not seem to be available but circumstantial evidence suggests this as a possibility.

Table 2 Resident and Non-Resident Arrivals in Brunei, 1987 and 1992 by Number and Percentage, in Parentheses.

Year	Total	Residents	Non-Residents
1987 (a)	904,862	382,239	522,233
	(100)	(42.2)	(57.8)
1992	1,116,992	745,116	411,876
	(100)	(64.4)	(36.6)
1987 ^(b)	750,165	382,239	367,926
	(100)	(51.0)	(49.0)

Notes: (a) Estimated from The Government of Brunei Official Website. Accessed 25/09/01.

(b) Re-estimated from *Brunei Darussalam Statistical Yearbook 1999*. The non-resident data in the original website statistics for 1987 appears to have an irregularly high number of 'other visitors'.

The composition of passenger arrivals in Brunei is interesting. Table 3 gives the more detailed composition of its passenger arrivals for 1992. The largest numbers by far involve returning residents, after that comes a large number for visits to relatives, then follow visits for business, transit purposes, and tourism with a large number in the 'others' category. In reality of course such classifications are far from watertight. For example, many of those visiting relatives probably engage in tourism activities as do many coming on business. The definitions do not seem to be designed to accord with those of the World Tourism Organization. If, however, visits purely for the purpose of tourism, as identified by Brunei officially, are considered, they form a very small share of its total visitor arrivals.

Table 3 Arrivals in Brunei 1992 by Purpose – Numbers and Percentages of the Total

Category/Purpose	Numbers	%
Residents	745,116	64.4
Relations	159,867	13.82
Business	79,023	6.83
Transit	38,552	3.33
Tourists	38,035	3.29
Others	96,426	8.33
TOTAL	1,157,019 ^(b)	100.00 ^(a)

^(a) May not add up to 100 because of rounding.

^(b) This Ministry of Communication figure is much higher than that in Table 4 because it includes returning residents.

Source: Based on statistics in Government of Brunei Website document. <http://www.mineom.gov.bu/shutt/creation/6.htm>

Table 4 sets out numbers of visitor arrivals in Brunei in the period 1985-98, as well as its foreign tourist numbers and expresses the latter as a percentage of the former. In the period 1985-1998, tourist numbers always remained at less than 10 percent of total visitor arrivals in Brunei. They rose from less than 2 percent of total visitor arrivals in Brunei in the mid-1980s to exceed 9 percent in the period 1992-1994 but by 1998 had fallen back to 2.5 percent of total visitor arrival. This was probably partly a result of the Asian financial crisis. But even before this, Brunei's tourism numbers were in decline after having peaked in 1994.

Table 4 Arrivals of Foreign Visitors in Brunei and Foreign Tourists 1985-1998 by numbers, with the latter given as a percentage of the former

Year	(1) Number of Visitor Arrivals	(2) Number of Tourists	(1)/(2) %
1985	367,926	6,418	1.7
1986	410,928	6,578	1.6
1987	522,257	9,004	1.7
1988	457,410	9,017	2.0
1989	392,751	8,549	2.2
1990	376,636	8,010	2.1
1991	343,944	28,640	8.3
1992	411,876	38,035	9.2
1993	488,909	44,921	9.2
1994	622,354	58,090	9.3
1995	782,216	36,751	4.7
1996	1,260,901	55,497	4.4
1997	na.	na.	na.
1998	1,310,493	32,738	2.5

Source: Number of visitor arrivals and tourists from the *Brunei Darussalam Statistical Yearbook 1999*

The total number of visitors to Brunei and its total number of tourists are graphed in Figure 1. While considerable growth in visitor numbers occurred in the 1990s and in tourist numbers compared to the 1980s, annual growth rates have been erratic with the relative volatility of tourist numbers being greater on the whole than for total visitor arrivals in Brunei. Table 5 sets out the annual absolute change and proportionate change in visitor numbers and tourist numbers for Brunei for the period 1986-1998.

Figure 1 Number of visitor arrivals in Brunei and foreign tourists, 1985 to 1998

[1997 figures are unavailable and are interpolated]

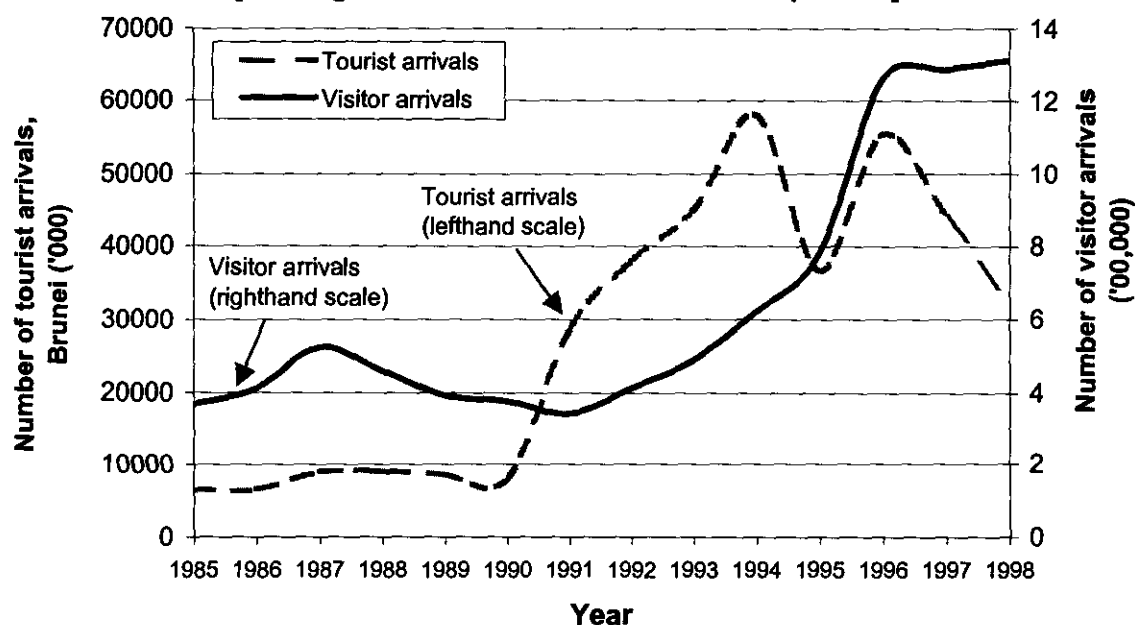


Table 5 Annual Changes in Visitor Arrivals and Tourist – Numbers and Percentage Change

Year	Visitor Arrivals		Tourist Arrivals	
	Change in numbers	Percentage change	Change in numbers	Percentage change
1986	43,002	11.7	160	2.5
1987	11,659	27.2	2426	36.9
1988	-65,177	-12.5	13	0
1989	-64,659	-14.1	-468	-5.2
1990	-16,115	-4.1	-539	-6.3
1991	-32,692	-8.7	20,630	254.7
1992	67,932	19.8	9,395	32.8
1993	77,033	18.7	6,886	18.1
1994	133,445	27.3	13,169	29.3
1995	159,856	25.7	-21,339	-36.7
1996	478,691	61.2	18,746	51.0
1997	na.		na.	
1998 ^(a)	49,592	3.9	-22,759	-41.0
Average		19.6		52.20

Note: ^(a) Change compared to 1996 because figures for 1997 are not available.

The erratic annual changes in inbound tourism numbers for Brunei in the period 1985-1998, highlighted in Table 5, support the earlier hypothesis that international tourism can be highly volatile. It can be much more volatile than experienced by Brunei. Nevertheless, international tourism to Brunei has expanded greatly in the space of about 15 years. In 1998, the number of its visitor arrivals was nearly 3.5 times that in 1985 and the number of its international tourists was over 5 times that in 1985.

Features which may make Brunei Darussalam attractive to tourists include

1. Its peace and tranquillity and a high degree of assurance of personal safety. This contrasts, for example, with the unsettled situation in Indonesia.
2. Relatively unique natural and man-made attractions in a small area.
3. Modern and reliable services and facilities, such as reliable availability of electricity supplies and a well developed infrastructure in both urban and rural areas, for example established roads.
4. Direct international air links.
5. Friendly and helpful people.
6. Considerable variety of scenery within a small area, with natural scenery close to urban areas such as Berakas Recreational Forest next to Berakas Beach, and Bukit Shahbandar Forest Park close to Jerudong Park Playground.
7. A convenient base to sample, or to be introduced to, the natural attractions of Borneo, such as Asia's highest peak, Mount Kinabalu in Sabah and the renowned Mulu National Park in Sarawak.

What particular tourists find an attraction is of course liable to vary with their background, their education and the aims of their travel. For those interested in learning as a result of travelling, Brunei provides excellent opportunities to learn about other cultures and historical experiences, about much of the nature of Borneo; and even Brunei's industries, such as its oil industry, can be of interest to tourists.

Nevertheless, Brunei does experience competition for tourists and travellers in its region. Singapore constitutes a very dominant international communication and transport node. Its presence limits Brunei's scope for establishing itself as a major regional service and tourism hub. But there is no doubt that Brunei offers a different

tourist experience to Singapore, and it seems to be a much safer destination than either Malaysia or Indonesia.

Malaysia, however, can offer similar but not identical cultural attractions to Brunei, and provide opportunities, possibly superior opportunities, to experience nature in the wild in Borneo. But this nature may not be as easily accessed as in Brunei. It is interesting to note that Singapore has been able to turn 'captive' nature into one of its major tourist attractions, via its bird-park, zoo, botanical gardens and aquarium, each of which is a major and popular tourist attraction. Viewing of 'captive' species is popular but does not appeal to everyone. Singapore is not in a position to show most of the rare or endemic species of Southeast Asia under natural conditions. But Brunei is able to engage in wildlife-based ecotourism, and much of this wildlife can be accessed with relative ease. For example, the proboscis monkey *Nasalis larvatus*, a unique species endemic to the island of Borneo, can be seen in mangrove habitats, such as the readily accessible Rangu Island close to the Sultan's palace, just a few minutes drive from the capital city.

4. Concluding Comments

Growth of the tourism industry can contribute beneficially to the economic diversification and development of small states, if appropriate preconditions are satisfied and care is taken in developing the industry. Even large nations, such as China (Wen and Tisdell, 2001), have been able to benefit substantially from the growth of foreign tourism. But growth in foreign inbound tourism is not a panacea for sustainable economic development of a nation nor always a highly effective means of economic diversification, if the purpose of diversification is to cushion the economy against the vagaries of fluctuations in market demand. The tourism industry can display a high degree of economic volatility as is apparent from many studies. As the world becomes more globalized, the international risks to tourism appear to grow.

In a period of less than two decades Brunei has made substantial progress in expanding the number of its visitor arrivals and foreign tourists. Compared to its neighbours and nearby countries, Brunei has the potential to expand these numbers further. Research into ways to bring this about in a sustainable manner should be of considerable value to policy-makers in Brunei. While there are limits to the extent to which Brunei

Darussalam can become a service and tourist hub within Southeast Asia, there are reasons to believe that these limits have not yet been reached, especially as far as its tourism development is concerned.

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