

Non-Equity Modes of Trade in ASEAN

Promoting new forms of trade between
Japan and ASEAN

PAPER 1
SEPTEMBER
2021

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ASEAN-JAPAN CENTRE

ASEAN Promotion Centre on Trade, Investment and Tourism



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NOTES

The terms “country” and “economy” as used in this study also refer, as appropriate, to territories or areas. The designations employed and the presentation of the material do not express any opinion whatsoever on the part of the ASEAN-Japan Centre (AJC) concerning the legal status of any country, territory, city or area; or of the authorities; or of delimitations of frontiers or boundaries.

The tables use the following symbols:

- Two dots (..) indicate that data are not available or are not separately reported.
- A dash (-) indicates that the item equals zero or its value is negligible.
- Use of an en dash (–) between dates representing years, e.g., 2015–2016, signifies the full period involved, including the beginning and end years.
- Reference to “dollars” (\$) means United States dollars, unless otherwise indicated.

The series includes 10 papers in total. Nine (Cambodia, Indonesia, Lao People’s Democratic Republic, Malaysia, Myanmar, Philippines, Singapore, Thailand and Viet Nam) have been published. This is the last paper in this series.

Paper 1. Brunei Darussalam

Paper 2. Cambodia (published in August 2019)

Paper 3. Indonesia (published in March 2021)

Paper 4. Lao People’s Democratic Republic (published in March 2020)

Paper 5. Malaysia (published in July 2021)

Paper 6. Myanmar (published in March 2020)

Paper 7. Philippines (published in March 2018)

Paper 8. Singapore (published in July 2021)

Paper 9. Thailand (published in April 2020)

Paper 10. Viet Nam (published in December 2018)

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KEY MESSAGES

- Brunei Darussalam relies heavily on the oil and gas industry, which accounts for 90 per cent of its total exports. However, due to the decrease in the demand for and price of oil and gas, the trade volume dropped drastically by 60 per cent in 2020. To diversify the economy, the Government of Brunei Darussalam introduced and implemented various initiatives to reduce reliance on the oil and gas industry.
- Over the last 10 years, foreign direct investment stock increased significantly by 80 per cent in Brunei Darussalam. However, interest in transnational corporations (TNCs) to engage in non-equity modes (NEMs) of trade with their Bruneian counterparts has been considerable. The low tariff rates make NEM exports from Brunei Darussalam attractive.
- Bruneian firms are involved in various types of NEMs, including franchising, outsourcing/subcontracting and licensing. The type of NEM varies by industry.
- The food and beverage (F&B) industry is flourishing in Brunei Darussalam. International F&B largely dominates the franchise mode of investment in Brunei Darussalam. Manufacture of F&B products contributed between Brunei dollar (BND) 29.2 million (\$22 million)¹ and BND25.5 million (\$19.2 million) (at constant prices) to the country's gross domestic product (GDP) over the past five years. Members of Generation Z are more likely to consume international F&B brands. As a result, F&B franchising in Brunei Darussalam normally earns at least 50 per cent to 60 per cent of gross profit.
- The textiles and garments industry in Brunei Darussalam flourished in the late 1990s, employing more than 1,500 people and exporting products mostly to North America. However, the country started to lose out to the People's Republic of China and other ASEAN countries due to their comparatively more competitive labour markets. In the last five years, Bruneian textiles and garments manufacturing has fluctuated between contributing BND34.2 million (\$25.7 million) and BND38.6 million (\$29 million) (at constant prices) to the country's GDP. The typical subcontract awarded to local NEMs is for cut, make, trim where the main international contractor supplies materials. This has enabled local NEMs to generate at least 15 per cent to 50 per cent in gross profits.
- The automotive industry in Brunei Darussalam is flourishing due to the high per capita income of the population. TNCs give local automobile dealers licensing rights to sell cars. Despite the COVID-19 pandemic, sales of automobiles in Brunei Darussalam increased by 5 per cent in 2020 compared with the same period in 2019.
- Engaging in NEMs provides many opportunities for both local NEMs and TNCs, such as the provision and creation of jobs for locals. Such activity also contributes to the transfer of knowledge to local NEMs in terms of management know-how. For example, local NEMs learn international standard operating procedures for managing firms. Nevertheless, engaging in NEMs also creates some challenges for local NEMs where local customs, regulations and requirements might not be suited to the TNC strategy, which could affect the longevity of the relationship.
- To maintain and further attract NEMs in Brunei Darussalam, the capability of local firms should be improved by leveraging technology and innovation, upskilling the labour force through training and re-training and promoting research and development and intellectual policy.
- Infrastructure also plays an important role in attracting TNCs to award local NEMs. Improving logistics systems through infrastructure development and modernization will be imperative, especially for exporting NEMs. An efficient and cost-effective logistics system will be beneficial for local NEMs and enhance their competitiveness.

¹ This paper uses an exchange rate of \$1 for BND1.33.

1. INTRODUCTION: OVERVIEW OF THE ECONOMY OF BRUNEI DARUSSALAM

Blessed with natural oil and gas resources and with a population of approximately 460,000, Brunei Darussalam has one of the highest gross domestic products (GDPs) per capita in the region at Brunei dollar (BND) 39,989 (\$30,000) and an overall GDP of BND18.4 billion (\$13.8 billion) in 2019 (Department of Economic Planning and Statistics 2019). Economically, the country is generally viewed as stable, as its limited exposure to toxic assets and adequacy of capital and large structural liquidity during the global downturn in 2008 reflects (International Monetary Fund 2010). Brunei Darussalam also benefits from its human development capacity, as exemplified by its literacy rate of 97 per cent in 2018 (World Bank 2021). Brunei Darussalam ranked 47th globally in the Human Development Index at 0.838 in 2019, among the highest in ASEAN (United Nations Development Programme 2020).

At the national level, the country is currently pursuing Brunei Vision 2035 (Wawasan Brunei 2035), which has three main goals:

Goal 1: Educated, highly skilled and accomplished people

Goal 2: High quality of life

Goal 3: Dynamic and sustainable economy

Goal 3 (dynamic and sustainable economy) encompasses numerous strategies, including the creation of economic opportunities beyond the oil and gas industry. Prior to COVID-19, oil and gas accounted for more than 90 per cent of total exports. However, in March 2020, a year-on-year decline occurred, as major exports of oil and gas decreased by more than 60 per cent (Department of Economic Planning and Statistics 2020), which highlights the need to diversify the economy amid concerns of fluctuating oil prices. In this context, the Brunei Economic Development Board (BEDB), a statutory board created in 2001, was tasked with developing and diversifying the economy in line with Brunei Vision 2035. Within the board's purview, it has identified five main clusters, namely, downstream oil and gas, manufacturing and other services, food, tourism and information and communication technology (ICT).

The FDI [foreign direct investment] Action and Support Centre was created to facilitate the development of these five main clusters, tasked with attracting investment to Brunei Darussalam by highlighting the country's favourable tax regime and protection for intellectual ownership and highlighting Brunei Darussalam as a credible partner. From a trade perspective, Brunei Darussalam has strived to improve its performance on the Ease of Doing Business index, ranking 66 out of 190 economies in 2020, by significantly improving its score of 69.6 (adjusted) in 2019 to 70.1 in 2020, placing Brunei at fourth place among ASEAN countries. Nevertheless, in the index category of Easiest in Getting Credit, it maintained its first place for 2020 (World Bank Group 2020).

Towards a Dynamic and Sustainable Economy: Economic Blueprint for Brunei Darussalam (2020; henceforth Brunei Economic Blueprint) notes the emphasis on FDI, highlighting that FDI stock has significantly increased in Brunei Darussalam from BND5.3 billion (\$3.9 billion) in 2010 to BND9.6 billion (\$7.1 billion) in 2019, an 80 per cent increase in the last 10 years (Ministry of Finance and Economy 2020).

However, FDI is distinct from non-equity modes (NEMs) of investment as the latter does not require equity contributions from transnational corporations (TNCs). NEMs refer to establishing contractual relationships that are conducted without any equity involvement from TNCs. In contrast, FDI relates to cross-border financial transactions between countries and TNCs that involve a minimum degree

of equity (normally 10 per cent or more) and control on the part of the TNCs. In 2011, the United Nations Conference on Trade and Development (UNCTAD) noted that, from a policy perspective, if TNCs want to “pursue the integration of developing economies into global value chains, it is no longer enough to focus on attracting FDI and TNC affiliates, on the one hand, or to promote arm’s-length trade on the other. Policymakers need to consider a myriad of alternative networked forms of TNC operations” (UNCTAD 2011, p. 124).

In Brunei Darussalam, despite the emphasis on FDI (BEDB 2020), TNCs have been consistently interested in being involved in the food and beverage, automotive and textiles and garments industries. Favourable tax incentives, such as no personal tax, no value added tax and a low corporate tax rate of 18.5 per cent, have aided this development. Import duties vary depending on the nature of the goods. In general, basic foodstuffs and goods for industrial use are exempt from import duties. Motor vehicles are subject to import duty depending on the vehicle’s capacity. Furthermore, exports leaving Brunei Darussalam do not incur tariffs.²

All countries, including ASEAN countries, have varied NEM-related interests, thus NEMs develop in varying forms. Table 1 shows the three primary forms of NEM that are of particular interest to Brunei Darussalam, which subsequent sections will describe further.

Table 1. Examples of NEMs in Brunei Darussalam

Types	Description	Typical Industries	Company Examples
Franchising	An international firm (franchisor) allows a host country firm (franchisee) to run a business following the franchisor’s system in return for a fee or mark-up on the goods and services provided.	Food and beverages	Gloria Jean’s Coffee (United States), Pretzels (United States), Sushi Tei (Singapore), Ochado (Singapore), Gongcha (Taiwan Province of China), Burger King (United States)
Licensing	An international firm (licensor) allows a host country firm (licensee) to utilize an intellectual property (e.g., copyrights, trademarks) in return for a royalty fee.	Automotive	Maju Motors (Volkswagen, Germany), Happy Motoring (Honda, Japan), Grand Motors (Mazda, Japan)
Outsourcing	An international firm seeks a host country firm to produce or manage services/processes related to the international firm’s development of product(s).	Textiles and garments	Famous Textile (Brunei Darussalam), Nazmi Textile (Brunei Darussalam), Madison Textile (Brunei Darussalam)

Source: Authors.

The food and beverage industry is a popular franchising industry in Brunei Darussalam that comprises local and international outlets. According to the United States Department of Commerce, U.S. food brands, notably fast foods, are well-received in Brunei Darussalam, with many U.S. food and beverage franchises already operating in the country, such as Auntie Anne’s Pretzels, McDonalds, KFC, Pizza Hut and Dairy Queen. More recently, in 2014, Starbucks and Burger King joined the range of U.S. franchises and have now expanded to four and six outlets respectively. In 2016, Wayback Burgers also entered the market, highlighting the perceived profitability of food franchises in the country (Department of Commerce 2021b).

² <https://www.aseanbriefing.com/news/import-and-export-procedures-in-brunei-best-practices/>

Due to the lack of public transport, Bruneians have an insatiable appetite for cars, which are sold through licensing agreements (Table 1), which has contributed to mitigating the spread of COVID-19 in the country. The ASEAN Automotive Federation (n.d.) indicates that 5,388 units were sold in Brunei Darussalam in the first five months of 2020, compared with 4,966 units, an 8.5 per cent increase. This contrasts with other ASEAN countries, which saw a 43 per cent decrease in the same year, mostly due to coronavirus lockdowns (Khan 2020). According to the ASEAN Fuel Economic Roadmap for Transport Sector 2018–2025, Brunei Darussalam is the only ASEAN country that has reached 100 per cent saturation, indicating high vehicle ownership (ASEAN Secretariat 2019).

Another NEM-related industry is the textiles and garments industry through subcontracting (Table 1). Although the economic downturn in 2002 affected the textile industry, some initiatives occurred in the garment industry with international institutions outsourcing the production of branded garments to manufacturing-based garment companies in Brunei Darussalam (Wong 2019).

2. CHARACTERISTICS OF NON-EQUITY MODES IN BRUNEI DARUSSALAM

NEMs are contractual relationships without equity between TNCs and partner firms in other countries. As in the case of equity investments, the motivations of TNCs relative to NEMs mostly surround three categories: resource seeking (usually joint ventures for both FDI and NEMs), efficiency seeking (contract manufacturing, subcontracting or outsourcing for NEMs) and market seeking (brand licensing, product licensing, process licensing, franchising, etc., for NEMs). TNCs influence their partner firms in the host countries based on bargaining power, which varies by mode (UNCTAD 2011). In this defining context, the characteristics of NEMs in Brunei Darussalam also vary, as NEMs are practised to low to moderate degrees in some sectors and are still emerging in other sectors. The following systematically discusses NEMs in Brunei Darussalam.

2.1 Scale and Scope of NEMs

TNCs aiming to expand business internationally increasingly use NEMs to enter foreign countries. NEM operations entail low risk because they are less demanding in terms of investment requirement and control from headquarters (Krusei and Zamborsky 2016). NEM operations include trade modalities such as contract manufacturing and exporting, franchising, licensing, contract farming, management contracts, concession agreements and any other forms of contractual relationships that enable TNCs to manage and influence the activities of partner firms in host countries. However, to some extent, NEMs can be associated with FDI from the TNC's motivational perspective. NEMs are intersecting subsets between FDI and trade as they appear either as substitutes for or as complementary to FDI operationalization in contributing to the value chain of TNCs.

Cross-border NEM activity in the sphere of FDI is where TNCs' internalized and externalized strategies play pivotal roles. TNCs activate internalized systems of affiliates in host countries when they need to operationalize within a controlled corporate network, while the externalized system works when TNCs do not control partner firms. TNCs that do not control partner firms enter into reasonable contractual agreements in the cross-border trade with host country partner firms that fall directly into the NEM category. In 2010, total global cross-border trade under NEMs was estimated at about \$2 trillion (UNCTAD 2011), which has grown rapidly since because of enhanced trade liberalization, globalization and regional cooperation. As an oil and gas rich economy, Brunei Darussalam attracts

FDI mostly in the energy sector; however, other areas such as exporting manufactured goods and machinery and transport equipment have also attracted reasonable FDI. Export gains through FDI in the economy provide the momentum and motivation for NEMs. Usually, high tariffs reduce exports generated from FDI (Rugman 1985). This is not the case in Brunei Darussalam as the country maintains low, in some cases negligible, tariff rates for exports associated with FDI, especially in industrial parks, which inspires exports. Table 2 illustrates the FDI inflows to and exports from Brunei Darussalam in recent years.

Table 2. FDI inflows and exports of Brunei Darussalam by commodity, 2014–2018 (\$ millions)

	2014	2015	2016	2017	2018
FDI inflows	568	173	-150	460	382
Crude materials export	13.0	9.4	17.4	16.7	19.1
Mineral fuels export	9,082.6	5,919.9	4,364.2	5,046.2	5,898
Chemicals export	439.6	138.3	237.2	204.8	243.1
Manufactured goods export	49.6	53.7	37.8	24.7	64.5
Machinery and transportation equipment export	133.2	182.2	241.2	141.2	169.4

Source: Commonwealth Secretariat (2019); Department of Economic Planning and Statistics (2014, 2019).

Several industrial parks have been slated for export production and to accommodate FDI in Brunei Darussalam (Department of Commerce 2021a), including

- Sungai Liang Industrial Park (SPARK) for gas-based petrochemicals;
- Pulau Muara Besar for oil and gas downstream and supporting activities;
- Salambigar Industrial Park for food, pharmaceuticals, cosmetics and light industries;
- Rimba Digital Junction for higher-order technology industries and data center services;
- Bukit Panggal Industrial Park for energy-intensive industries;
- Telisai Industrial Site for aquaculture and mixed industries and
- Anggerek Desa Technology Park (ADTP) (phase 3) for ICT-related industries.

In addition to FDI and FDI-geared, export-oriented peripheral NEMs, other primary forms of NEMs are also gaining a foothold in Brunei Darussalam. For instance, contractual agreements and contract farming in aquaculture recently emerged on a limited scale. Service-oriented firms or TNCs establish NEM operations in Brunei Darussalam because the service-based products are mostly people intensive, demand less control from headquarters and require less fixed investment. Besides the peripheral NEMs connected to FDI, the primary and dominant forms of NEMs in Brunei Darussalam are franchising, licensing and subcontracting, which the latter part of this section will discuss.

In general, NEMs volume in Brunei Darussalam stays low to moderate because of the small population, or, in other words, due to a small domestic consumer base. However, this small size allows the consumer base to rapidly become familiar with business products under NEMs, which consequently may achieve recognition. High disposable incomes and living standards in Brunei Darussalam also form a good ground for NEMs operations' growth.

In terms of ensuring a friendly business environment, inclusive policy and country strategy is pivotal for maximizing the benefits from NEMs. For instance, promoting NEMs in national policy and assisting domestic businesses to become involved in NEMs provide an enabling and transparent legal and institutional charter to ensure fair competition, protect labour rights and the environment, address risk factors posed by NEMs and enhance the negotiating power of domestic NEM business partners (OECD 2009; UNCTAD 2015; Krusei and Zamborsky 2016). More importantly, establishing agencies to facilitate and attract TNC partners are critical for reaping the benefits from NEMs for a country. In the 2020 Ease of Doing Business annual rating by the World Bank, Brunei Darussalam ranked 66 out of 190 economies, indicating that the country is a reasonably good place for business (World Bank Group 2020). Generally, full ownership by foreign companies through licensing is possible in Brunei Darussalam without finding a local partner to enter the market. In some instances, TNCs are required to find a local licensing partner to enter the market. However, no specific legislation covers franchised operations in Brunei Darussalam besides contract law and commercial law (Wong and Chew 2018). The Business Licenses Act of Brunei is also applicable to franchising businesses. Other laws such as the Trade Marks Act, Unfair Contract Terms Act and Companies Act apply to Bruneian franchising operations. Any franchise in Brunei Darussalam must register with the Office of Registrar of Companies according to Chapter 39 of the Companies Act.

The following is an overview of the dominant forms and features of NEMs in Brunei Darussalam.

(1) Franchising

As a contractual relationship between a franchisor (a TNC) and a franchisee (host country firm), franchising refers to running a business that follows an already established business model developed by the franchisor in return for a fee (UNCTAD 2011). Capturing the market is the primary motivation of franchising. Franchising is also an efficient marketing and distribution tool for products and services (Wong and Chew 2018). It spreads with the increasing economic growth and market size of a nation, the people's purchasing power and the congenial business atmosphere of a country. Franchising takes different forms in various sectors such as retail (high-street retail of luxury brands, retail in shopping malls and grocery), restaurants (fast food and beverages), hotel chains and other services sectors (ranging from education to personal care services). Consumer goods and retail, including food and beverages, are the most common sectors where franchising grows rapidly. As a NEM operation, franchising permits TNCs to focus on core activities and allows outsourcing of non-core activities (UNCTAD 2011). Consequently, franchising benefits TNCs, allowing them to access markets through specialization and economies of scale.

The worldwide franchising market was estimated at \$2.5 trillion in 2010; out of this \$330–350 billion comprised the contribution from cross-border franchising. In the same year (2010), sales from franchising were estimated at \$170 billion in Asia, and cross-border franchising contributed about \$42.5 billion or 25 per cent (UNCTAD 2011). Globally, franchisors mostly come from developed countries. The franchising market in Brunei Darussalam indicates a mixed perspective. On the one hand, in proportion to its market size, Brunei Darussalam has a relatively large number of franchises, which is dominated by the food and beverages sector, though some retail (apparel) is also present. On the other hand, every year Bruneians spend a large amount of money abroad on products and services, much of which could be retained in the country as demonstrated during the COVID-19 pandemic, indicating further growth opportunities for NEMs.

Existing franchises currently operating in Brunei Darussalam are from the food and beverages sector, including Auntie Anne's Pretzels, Dairy Queen, Burger King, McDonalds, KFC, Pizza Hut, Starbucks and Natural Health Farm. Brunei Darussalam is fertile ground for food chain franchises for several reasons. The travel experiences of the country's increasing affluent class shows a growing demand for franchised food outlets, as they are exposed to a wide range of international food franchises and

products. Also, about a half of the Bruneian population is young (under the age of 24) and frequently consumes international food products. Franchised food chains are also attractive for tourists coming to Brunei Darussalam. Such opportunities transfer the service experience and operating knowledge and model from TNCs to local businesses.

Worth noting is that some local food businesses have grown to a level that could easily expand through franchising in foreign countries, especially in the ASEAN region. Implementation of the single market concept such as through the ASEAN Economic Community (AEC) and the recently signed Regional Comprehensive Economic Partnership Agreement among 15 Asia-Pacific nations, including ASEAN member states, will further lower trade barriers (ASEAN Secretariat 2008, 2020), paving the way for NEM operations such as franchising. Local Bruneian food businesses such as Excipade Sushi, Fratini's Italian Restaurant, Tasconi's Pizza and Mochi Yogurt House have either franchised or are planning to franchise overseas. A local coffee shop, Roasted Sip, has immense potential to franchise overseas. Bruneian halal foods and goods such as halal medical and cosmetic products of Faceshop and Simpor Pharmaceuticals form a niche business domain that could be gradually built into an indigenous franchise industry. Recently, the state-owned Brunei Darussalam Holdings made efforts to build a Bruneian brand in the United Kingdom for halal foods and products, but a dedicated agency could further support local businesses to franchise overseas.

(2) Licensing

Licensing is one of the vehicles through which TNCs enter a host-country market. Transfer of intellectual property and contract protection are two critical elements in licensing (Erramilli *et al.* 2002; Majocchi *et al.* 2013). Licensing refers to a contractual relationship between a licensor (for example, an international firm or a TNC) and a licensee (for example, a host country firm), where the licensor permits the licensee to utilize an intellectual property in exchange for a royalty fee. In other words, a firm can acquire a licence from another firm (in-licensing) or a firm can sell intellectual property to other firms (out-licensing) (UNCTAD 2011). Intellectual property denotes trade secrets, copyrights, patents, trademarks and industrial design rights. NEM operations through licensing are eventually transferred as intellectual property to a host country and drive increasing availability of sophisticated partners in emerging markets.

UNCTAD (2011) estimated that about \$340–360 billion in sales were generated globally through cross-border, NEM-related licensing in 2010. In Brunei Darussalam, business investments through licensing are promoted. A foreign company or its branch or its agent needs to get a licence by registering under the Company Act before commencing the business in Brunei Darussalam. In addition, other pieces of legislation that govern investment through licensing include the Investment Incentive Order (2001) and the amended Income Tax Order (2001). Activities that are incentivized through licensing under the Investment Incentive Order generally include construction, building and heavy equipment, environmental technologies, ICT, industrial equipment, marine technology, metal manufacturing and some services sector activities such as consultancy and research, automotive and ground transportation, education, finance, media and entertainment and travel.

Prominent businesses that provide services through licensing in Brunei Darussalam include a branch of the Standard Chartered Bank in finance; Maju Motors, Happy Motoring (a branch of Honda) and Grand Motors (a branch of Mazda) in the automotive industry and the Institute of Brunei Technical Education (IBTE) and the Jerudong International School in education. In the automotive industry, Maju Motors Sdn. Bhd. is licensed as a branch of Volkswagen, Singapore, and is the sole distributor of Volkswagen vehicles in Brunei Darussalam. Happy Motoring Co. Sdn. Bhd. is registered as a private limited liability company and is the exclusive distributor of Honda vehicles. The Standard Chartered Bank Brunei and the Hongkong Shanghai Banking Corporation have been licensed to provide banking and financial services in Brunei Darussalam.

(3) Outsourcing/subcontracting

Outsourcing or subcontracting, or contract manufacturing, to a host country firm is a popular form of NEM that TNCs engage in worldwide. This form of NEM refers to a contractual relationship where an international firm seeks a host country firm to produce goods or manage services or process elements in its global value chain. Taking advantage of globalization and trade liberalization, TNCs outsource their non-core activities and business support functions to external providers to reduce internal costs or bring efficiency to the value chain. UNCTAD (2011) estimated that TNCs' outsourcing or contract manufacturing services contributed about \$1.1–1.3 trillion in global sales in 2010.

Recently, Brunei Darussalam has attracted several TNCs that engage in outsourcing or contract manufacturing activities. In fact, Brunei Darussalam is a strategically valuable location as a manufacturing base in the Borneo region. Its location in the Brunei Darussalam, Indonesia, Malaysia, Philippines–East ASEAN Growth Area (BIMP-EAGA) is ideal for manufacturing businesses such as foods, food ingredients, pharmaceuticals and petrochemicals. In recent years, the contribution (in current prices) of manufacturing to the GDP of Brunei Darussalam was BND2,120.0 million (\$1,594 million) with 12.5 per cent share in 2017, BND2,574.2 million (\$1,935 million) with 13.8 per cent share in 2018 and BND2,499.4 million (\$1,879 million) with 13.4 per cent share in 2019 (Department of Economic Planning and Statistics 2019). Although only gradual improvements occurred, the garments industry and training for the local workforce involved in manufacturing have gone through subcontracting experiences in Brunei Darussalam. For example, Bruneian Famous Textile recently exported garments to Disney, Hard Rock and Universal through a subcontracting arrangement. Table 3 presents textiles and garments exports for Brunei Darussalam by country in 2018.

Table 3. Main Bruneian textiles and garments exports by country, 2018

Country	Exports (\$ thousands)
United Arab Emirates	3,709.96
United States	3,430.85
Singapore	1,115.49
Malaysia	810.15
Philippines	662.42
Hong Kong, China	432.32
United Kingdom	159.50
Viet Nam	24.96
France	19.98
People's Republic of China	10.79
Germany	10.52
Australia	6.80

Source: WITS (2021).

In another instance, a joint venture of PTAS Aker Solutions Sdn. Bhd. is providing local employees of Brunei Shell Petroleum training on execution capability based on Aker Solutions' international expertise in transferring values to the local partner. In pharmaceuticals, Vivapharm (Brunei) Sdn. Bhd. produces halal pharmaceutical and nutraceutical products for a Canadian firm that targets the growing halal market overseas. Vivapharm also focuses on exporting halal-certified natural health products and drugs to Asia-Pacific regional markets, the Middle East, Western Europe and the United

States. In petrochemicals, SPARK is a good example of partnership in contract manufacturing between Japan and Brunei Darussalam. The SPARK methanol plant is an export facility that is connected by a subsea pipeline system established by the BEDB. To facilitate the export of methanol via tankers, the methanol export facility that is commonly referred to as Single Point Mooring is connected through the subsea pipeline system to a loading buoy. In another instance, the Korean household electronic company Cuckoo has a strong water purifier market in Brunei Darussalam. The after-sales services of Cuckoo filters have been outsourced to an agent company in Brunei Darussalam.

In addition to these three dominant types of NEMs, contract farming has just started evolving in Brunei Darussalam. Within the contract farming mode, services outsourcing has also been identified. In aquaculture, a Taiwanese seafood company, Golden Corporation Sdn. Bhd., has established its operational headquarters in Brunei Darussalam in partnership with a Bruneian company, Semaun Marine Resources Sdn. Bhd. This partnership recently signed two memoranda of understanding with other two Bruneian marketing companies, Unima Distribution and Aqua Star Pty. Ltd., to export blue shrimp to EU and Australian markets, respectively. This is an example of marketing services outsourcing by a TNC lead in partnership with a host country firm. In another instance, Hong Kong-based Pure Fresh and Bruneian state-owned Ghanim International Corporation have started a project to invest about BND400 million (\$300 million) over five years to develop an export-oriented supply chain aquaculture in Brunei Darussalam targeting blue shrimp as their flagship product.

2.2 Brunei Darussalam NEMs by Type

Many foreign firms and TNCs do business with local partners in the form of NEMs in various industries. The ways they are involved in NEMs and their contributions to the national economy vary by modality and industry. This section examines the franchising, subcontracting and licensing modes through case studies of industries that rely on them.

(1) Franchising: Food and Beverages

Several international franchise food and beverages (F&B) companies have mushroomed in the country in recent years (Box 1). This growth also helps international franchise development by increasing the awareness of international brands among members of Generation Z.

Box 1. International F&B franchise in Brunei Darussalam

Various modes of franchise agreement are commonly practiced in Brunei Darussalam:

1. Direct franchise agreement (Figure 1),
2. Joint-venture franchise agreement from overseas master franchisee (Figure 2) and
3. Master franchise agreement with a fully owned foreign subsidiary (Figure 3).

Some TNCs appoint a local corporation from a particular ASEAN country to be their master franchisee. Due to small markets, most of the international franchises in Brunei Darussalam would usually go through the regional master franchisee (see Figure 2). Nevertheless, in some instances the TNC awards a direct franchise agreement (see Figure 1). The remaining franchise companies are a result of direct investment by the master franchisee.³ Box figure 1.1 shows some examples of franchise F&B companies in Brunei Darussalam.

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³ Source: Feedback from an interview with an F&B business owner who previously managed an international franchise company in Brunei Darussalam.

Box 1. International F&B franchise in Brunei Darussalam (Concluded)

Box figure 1.1. Examples of F&B franchises in Brunei Darussalam



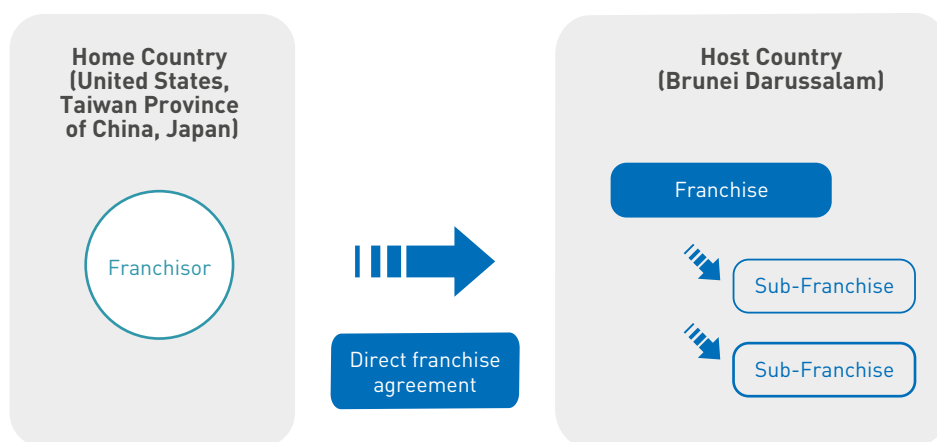
Source: Author photos.

Over the last five years, the F&B industry in Brunei Darussalam has contributed steadily to the country's GDP, from BND29.2 million (\$22 million) to BND25.5 million (\$19.2 million) between 2015 to 2019 (Department of Economic Planning and Statistics 2019). Numerous F&B franchises from Australia, Japan, Malaysia, Republic of Korea, Thailand and United States can be found in Brunei Darussalam. U.S. brands such as Starbucks (Box 2) and Burger King entered the Bruneian market in 2014 and have expanded to four and six outlets, respectively. Other F&B franchise companies in Brunei Darussalam include Gong Cha from Taiwan Province of China and Ochado Drinks and Pezzo from Singapore, to name a few. This industry remains quite attractive to local NEMs as the gross profit margin can range from 50 per cent to 60 per cent.⁴

⁴ An interviewee who is an owner of a local F&B company and used to manage an international F&B franchise in Brunei Darussalam provided this range. The owner's family also runs and owns other international F&B franchises in Brunei Darussalam.

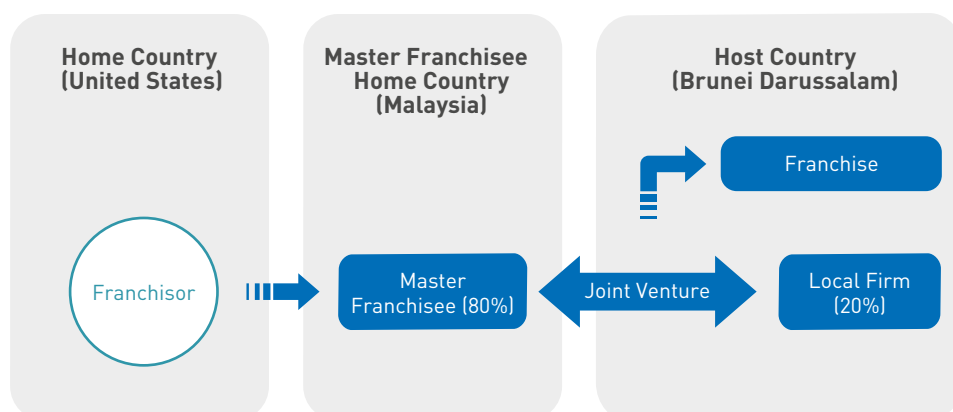
Various types of franchise arrangements are practised in Brunei Darussalam. The simplest form is the direct franchise agreement, under which the franchisee can either be awarded to open a single franchise unit or multiple franchise units. Franchisees that are awarded multiple franchise units will receive a schedule that determines when the franchisee is expected to open the units. Figure 1 illustrates this form of arrangement.

Figure 1. **Direct franchise agreement** (E.g., Burger King)



Source: Author.
 Note: Blue color indicates NEM relationship.

Figure 2. **Joint-venture franchise agreement from overseas master franchisee** (E.g., Starbucks)



Source: Author.

Box 2. Starbucks in Brunei Darussalam



Photo from the authors.

Starbucks Brunei, which is operated by Berjaya Food Supreme Brunei Sdn. Bhd., is a joint venture between the master franchisee in Malaysia, BFI Sdn. Bhd., and Deluxe Daily Food Sdn. Bhd.

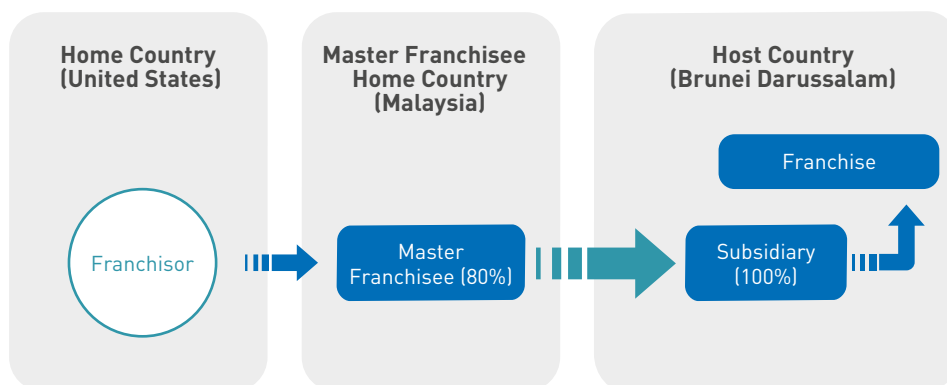
On 7 October 2013, Berjaya Food (International) Sdn. Bhd. (“BFI”), a wholly owned subsidiary of BFood, entered a joint venture, with shareholders’ agreement, with Deluxe Daily Food Sdn. Bhd. (“Deluxe”) for

80 per cent equity interest in Berjaya Food Supreme Sdn. Bhd., a Brunei Darussalam incorporated company, to operate a Starbucks Coffee chain of cafes in Brunei Darussalam for a total cash consideration of about BND2.40 million (or \$1.8 million). Deluxe underwrote the remaining 20 per cent.

On 16 February 2014, Starbucks opened its first store in Brunei Darussalam at the Mabohai Shopping Complex. The store features a traditional coffee bar also known as “slow bar”, which allows customers to savour their coffee using the “pour over” brewing method. On 7 September 2014, Starbucks opened its first drive-through concept store in Beribi. As of 30 June 2019, four Starbucks stores are operating in Brunei Darussalam.

Source: <https://www.berjaya.com/berjaya-food/corporate-profile.php>

Figure 3. Master franchise agreement with a fully owned foreign subsidiary (E.g., KFC)



Source: Author.

As per Figure 2, the Starbucks franchise in Brunei Darussalam took the form of a joint venture with the Malaysian master franchisee in which the master franchisee owned 80 per cent of the share. This is quite different from the case of KFC where the Bruneian KFCs are 100 per cent owned by the Malaysian master franchisee.⁵

⁵ Source: Feedback from an interview with an F&B business owner who previously managed KFC in Brunei Darussalam.

Other forms of franchise agreements may be practiced in Brunei Darussalam. However, whatever the form of agreement, the local franchisee still needs to pay the franchise fee for using the franchisor's brand name, product and intellectual property. Franchise fees typically start with an initial payment due to the franchisor at the signing of the franchise agreement. Franchise fees are usually used to pay for the marketing, technical and operational support of the franchisees. Other fees might also be involved, such as the royalty fees that are usually a certain percentage of the franchisee's gross or net revenue.

Franchise contracts provide various benefits to the country's economy. A franchise is a platform for local firms to understand international standard operating procedures for running a business, especially in F&B. Management know-how, capacity building and technology transfer are some of the knowledge that international franchisees can expect to acquire during their period of contract. Experiential learning is the best way to develop new skills and knowledge that the country's existing educational system might need to adopt. Thus, the franchisee and its workforce would learn what is required to run a business locally and internationally. In some instances local firms used the knowledge and skills gained to open their own business brands. For example, a former manager of an international franchise now owns two branches of successful restaurants. For TNCs, franchising is the most inexpensive way to expand their business and brand recognition without directly investing in the host country.

(2) Subcontracting: Textiles and Garments Manufacture

According to the Brunei Darussalam yearly statistics book, from 2015 to 2019 textiles and garments contributed an estimated 0.2 per cent of the total GDP of Brunei Darussalam annually, or between BND34.2 million (\$25.7 million) and BND38.6 million (\$29 million) (BDYSB 2019).

In the textiles and garments industry in Brunei Darussalam, subcontractors are hired by a project's general contractor, which is responsible for completing the whole project. Most TNCs use firms from ASEAN states as subcontractors to perform parts of the textiles and garments manufacturing process. In Brunei Darussalam, the common subcontract awarded is for CMT, which is the easiest, but has low value added (see Box 3). This type of arrangement typically results in an expected gross profit margin that ranges from 15 per cent to 50 per cent.⁶

Box 3. Subcontracting apparel businesses for garment export

Apparel businesses that subcontract for garment exports typically apply one of the following four modes of export.

1) CMT (cut, make, trim)

CMT is the easiest export method in the apparel industry and has the lowest value added. Under this method, TNCs offer all the inputs for production including raw materials, transportation, designs and specific requirements, while manufacturers carry out only the stages of cutting, sewing and trimming the products. Businesses working under this export method need only a basic understanding of design patterns and the ability to produce finished products.

2) OEM (original equipment manufacturing)

OEM entails buying raw materials and producing and selling final products and creates higher value added than CMT. Unlike CMT, local firms buy necessary material inputs instead of being supplied with them directly from their buyers.

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⁶ Feedback from the owner of a local garment NEM.

Box 3. Subcontracting apparel businesses for garment export (Concluded)

3) ODM (original design manufacturing)

ODM entails purchasing fabric and materials, cutting, sewing, finishing, packaging and shipping products. The ability to design reflects a higher level of knowledge by the providers and brings higher added value for products. ODM businesses create designs, finish products and sell them to buyers, which are most of the world's major brand owners.

4) OBM (original brand manufacturing)

This production method is an improvement over OEM, as manufacturers are responsible for their own designs and sign domestic and foreign goods supply contracts for their own brands. Under the OBM method, manufacturers in developing economies distribute products mainly in their domestic market and neighbouring countries' markets.

Source: ASEAN-Japan Centre.

The first and one of the largest garment factories in Brunei Darussalam is Brutex Manufacturing. Brutex, located near the town of Muara, was established in the late 1990s and employs more than 1,500 employees. It produces around 60,000 pieces of children's clothing per month and then exports them to North America.⁷ However, the textiles and garments industry faced direct competition with the low cost of labour and materials from the People's Republic of China. Currently, only one local firm managed to survive and secure contracts to manufacture apparel for a TNC. Famous Textile is currently the only local firm subcontracted by a TNC to produce garments and clothing. The company was incorporated in Brunei Darussalam in 2003. The initial reason for its establishment was to take advantage of the Bruneian quota-free status, cheap energy costs, comparatively inexpensive labour, no import duties, low inflation and political stability.⁸ The good reputation of Brunei Darussalam in terms of its labour standards and ranking 46th in the Environmental Performance Index by Yale and Columbia Universities has proved to be an added value for local NEMs in being awarded a contract by TNCs.

Famous Textile has actively brought in other small local garment companies in Brunei Darussalam to be part of its supply chain. One such company is Cerita Fabrikku. Cerita Fabrikku was established by the company's former i-Ready scheme employees (Box 4). Famous Textile also extended its assistance to help the Government of Brunei Darussalam develop and provide a two-month sewing operator course for vocational students (Box 5). The company also issues a conditional offer of employment to 100 trainees with the condition of simply completing the course. This programme has benefited local garment companies in terms of knowledge and skills transfer to the Bruneian work force.

Box 4. TNC subcontracting garments manufacturing to Bruneian firms

i-Ready trainees launch startup manufacturing garments for export⁹

Through a subcontract with Brunei's biggest textiles producer, the all-local team of Cerita Fabrikku has produced 5,000 shirts for Hard Rock and Universal Studios.

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⁷ <https://textilevaluechain.in/2020/08/22/fashion-in-brunei/>

⁸ <http://www.splaopdr.com/BRUNEI/FAMOUS-TEXTILE-SDNBHD-BRUNEI.html>

⁹ <https://www.bizbrunei.com/2019/12/i-ready-trainees-launch-startup-manufacturing-garments-for-export-cerita-fabrikku/>

Box 4. TNC subcontracting garments manufacturing to Bruneian firms (Concluded)



Source: Stephen So, MD of FT.

Out of luck in searching for jobs related directly to their academic backgrounds, a group of six Bruneian graduates in science, engineering, technology and linguistics arrived at the doorstep of Brunei's biggest textile production facility located in Jerudong in the final quarter of 2017. Led by its owner Stephen So, Famous Textile (FT) produces some 250,000 shirts monthly – almost entirely for export and supplied to renowned brands including Disney, Hard Rock and Universal. FT's 42,000 square feet factory with 360 sewing machines and 200 employees has been a well-oiled machine since setting up in 2003 as an extension of its parent company, Hong-Kong based Booma Fat Garment. But it's role in

mentoring the six Bruneian graduates – who entered FT under the government-sponsored i-Ready apprenticeship programme – that's set to make local headlines. "They [the i-Ready trainees] have decided to set up their own garment manufacture company called Cerita Fabrikku," said So. "It will be locally run, locally owned with 100% local sewers, which I think might be a first for the garment industry in Brunei." Since setting up at the Ministry of Culture, Youth and Sports' (MCYS) Youth Development Centre (YDC) two months ago, Cerita Fabrikku has made over 5,000 shirts for Hard Rock and Universal Studios sub-contract supply agreement with FT. «When FT started in Brunei nearly 20 years ago we began with 400 staff, about 10% were Bruneians," said So. "Within a week they had left. But now we are starting to see a (gradual) shift, and Cerita Fabrikku is at the centre of that change."

Building local competency - If Nurul Fatini Hj Abdul Malik had to guess what her first formal apprenticeship would be after graduating from the UK three years ago, it would be working inside a laboratory and not a factory. The diminutive MSc in Medical Molecular Microbiology and Immunology graduate from the University of Aberdeen's response to being unemployed was to keep an open mind and upskill through taking a short sewing course making *baju kurung* (traditional Malay dress) at IBTE. On September 11, 2017, she got her opportunity, submitting an i-Ready application to be a production supervisor trainee at FT through JobCentre. Eight days later she began her first day with five other Bruneians, not knowing that she would go onto start and lead her own garment company two years later. "It was what I (initially) expected; there was no air-conditioning and we sat for hours on the sewing machines learning all the basic processes," said Nurul, who is now the CEO and product development officer of Cerita Fabrikku. "What made things challenging wasn't just the learning curve (at FT) but the fact that not many around me (friends and family) understood why I would put up working in a factory; something entirely outside what I had studied in university. But it was necessary for us to function effectively as supervisors, and looking back it was even more important for us because without it there would be no way we could have started our own garment company." After Fatini's batch, other four i-Ready graduates arrived as trainee supervisors, designers and programmers. Collectively, they were the first batch of Bruneians to work at FT in several years, and their rapid development renewed discussions amongst FT's management if locals could be trained not only as supervisors but also as sewers. Six months after the i-Ready trainees began, So entered discussions with the Centre of Capacity Building (PPK) – who provide vocational training to secondary school leavers – to develop a two-month sewing operator course for Bruneian youth. Then, put pen to paper and committed 100 conditional offers of employment (COE) to FT for those who completed the course. FT would also lease machinery to PPK for the training and develop the course's content that is today delivered today by the six founders of Cerita Fabrikku.

Source: BizBrunei, reprinted with permission.

Box 5. Brunei initiates training program to boost garment sector¹⁰



Source: Photo courtesy of Famous Textile.

The Brunei Industrial Development Authority (BINA), an agency under the Ministry of Industrial and Primary Resources, Government of Brunei Darussalam, is working with Famous Textile, a local textile company to initiate a garment training programme for industry professionals in the country, according to the Brunei Times. The pilot project is still in its initial stages, and its complete details, as well as eligibility criteria for the training, are yet to be finalized, states the report. Announcing the proposed training programme, BINA said it would identify and guarantee buyers for the apparel made by the entrepreneurial programme participants.

As part of the programme, Famous Textile would look for sponsors to encourage and nurture young entrepreneurs to venture and become successful entrepreneurs in Brunei's clothing industry. The company would guide and help those who take part in the training programme in their first business transaction from the process of design, submission, and execution to delivery, invoicing and receiving payment. The programme would allow young entrepreneurs to be creative while assisting them in successfully launching their enterprises. The programme would also include seminars on applying embellishment to readymade garments using techniques such as screen printing, embroidery, sublimation, and batik designing.

Moreover, young entrepreneurs taking the course would be asked to create designs featuring various aspects of Bruneian culture and the country's picturesque sights like coral reefs and rainforests. Famous Textile Sendirian Berhad is a manufacturer of a complete range of garments and clothing items for men, women and children. With over two and a half decades of expertise in the industry, the company specializes in offering high quality manufactured knit and woven wear.

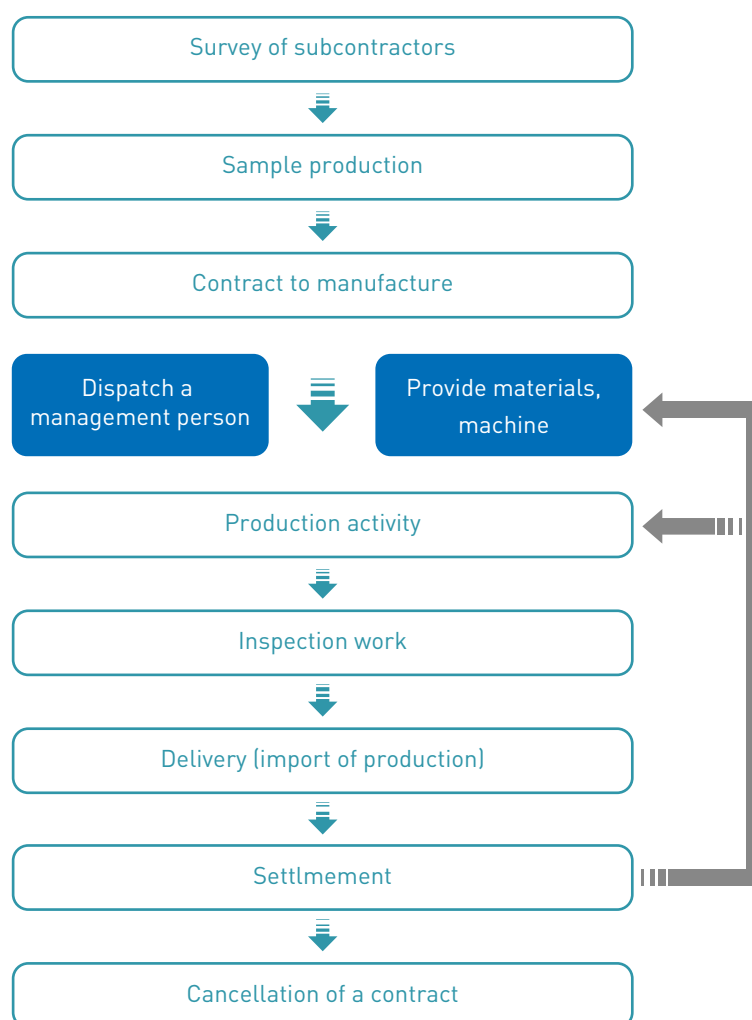
Source: Fibre2fashion.com, reprinted with permission.

For the past few years, the Government of Brunei Darussalam has designed and run various initiatives with the assistance of a local textiles and garments firm to revive the country's industry. As Bruneian labour cost is still considered high among the ASEAN member states, current and future local firms are expected to compete on other factors such as health and safety, international labour standards, responsible sourcing, product safety and product footprint. These are some examples of areas that TNCs look at when evaluating firms that apply for subcontracts.

Nevertheless, at present, local firms are only involved in CMT activities in the entire textiles and garments supply chain. For raw materials procurement, garments manufacturers rely heavily on the People's Republic of China, which is now the main supplier of fabrics and raw materials (see Figure 4 for the common flowchart of contract manufacturing). Thus, local firms will only charge for their CMT services and other logistics costs. No cost is incurred in raw material procurements.¹¹

¹⁰ https://www.fibre2fashion.com/news/manufacturingnews/newsdetails.aspx?news_id=165805

¹¹ Feedback from the owner of a local garments NEM.

Figure 4. **Flowchart of contract manufacturing**

Source: ASEAN-Japan Centre.

(3) Licensing: Automotive

Licensing is a business arrangement in which one company gives another company permission to manufacture, sell and distribute its products or services for a specified price. Being awarded the only licensed distributor or seller for another company's products or services means that no other companies within the area/region or country are allowed to perform such activities. Thus, the awarded company has the legal rights to sue any company that manufactures, sells or distributes the same product within the same region.

With a high income per capita, the population of Brunei Darussalam also has a high ownership of cars per person. Table 4 shows that the number of newly registered cars exceeded 10,000 vehicles per year for the past three years. Brunei Darussalam has the highest total registered motor vehicles per 1,000 population at 962.9 among ASEAN countries, followed by Malaysia and Thailand with 897.4 and 583.1 respectively in 2018 [ASEAN Secretariat 2019]. The country also has many

registered distributors of automobiles. Having a licensed distributor in the host country means that TNCs can rely on the local firm to generate income. According to the ASEAN Automobile Association, motor vehicles sales in Brunei Darussalam increased by 5 per cent in 2020 from the previous year, while other ASEAN countries saw on average a drop of 27 per cent for their overall sales due to the pandemic.¹²

Goh Hock Kee Sdn. Bhd. is a local firm and the only authorized dealership in Brunei Darussalam for Mitsubishi vehicles and Daihatsu from Japan (Box 6). The company is also licensed to sell other international brand vehicles such as Alfa Romeo, Jeep, Dodge, *etc.* Other car dealers licensed to sell and distribute domestic vehicles are Maju Motors Sdn. Bhd., Grand Motor Shd. Bhd., QAF Motor Sdn. Bhd., Jati Transport Sdn., among others. Each company has the licence to sell only one or more international brand vehicles.

Table 4. Newly registered cars per year, 2017–2019

Year	2017	2018	2019
Length of road (km)	3,693.0	3,708.4	3,713.6
Land Transport			
Newly registered vehicles (numbers)	11,390	11,140	12,258
Private cars	10,743	10,442	11,383
Goods vehicles	211	334	321
Motorcycles/scooters	319	241	309
Others	117	123	245

Source: Department of Economic Planning and Statistics 2019.

Box 6. Local automobile firm licensed to sell Japanese cars



Source: Author photo.

Goh Hock Kee Motor, which later changed to GHK Motors Sdn. Bhd., was founded in 1970 and registered as a private limited company in 1984 and supplies passenger cars in Brunei Darussalam. Bruneian Goh King Chin established the company in 1970 primarily selling reconditioned European, American and Japanese cars. The company

started to gain a good reputation for selling used cars after the first three years of its establishment, motivating the founder to venture into the automotive industry by importing new cars seriously. In 1973, the Daihatsu Motor Corporation (Japan) granted the franchisee licence to distribute and sell trucks and passenger cars in Brunei Darussalam.

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¹² <https://www.asean-autofed.com/index.html>

Box 6. Local automobile firm licensed to sell Japanese cars (Concluded)

The company has set a pace to grow exponentially by upgrading its facilities, hiring more staff and investing in equipping its staff, especially the mechanics, with the latest industry know-how. The mechanics were sent to Japan to improve their efficiency and competitiveness in dealing with day-to-day operations at the company. At the same time, the founder was determined to expand further the company's share of the local automotive market; as a result, the company received the sole distributorship of Mitsubishi trucks and cars by Mitsubishi Motor Corporation in 1979.

The company prides itself on providing quality cars and quality services and has grown steadily since its founding. GHK Motors also became the sole distributor of Fiat Chrysler Automotive in the sultanate. It started selling the Jeep and Alfa Romeo brands in the local market in 2006. The company also acquired the rights to distribute and market Chevrolet, Chrysler, Jeep, Dodge and Perodua models.

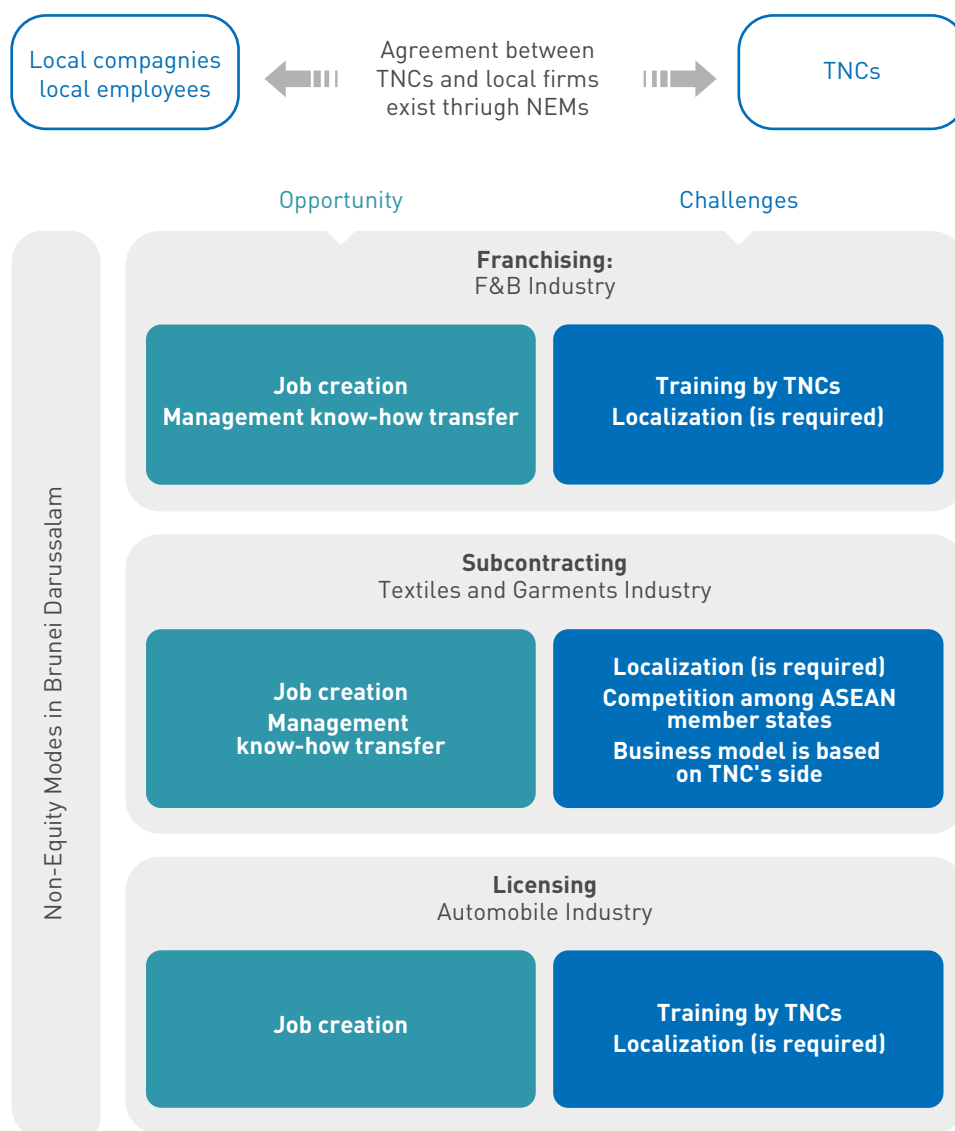
The company pushed further horizontally, establishing its sister company in 2000: GHK Auto Assembly Sdn. Bhd. In 2019, GHK introduced the first in the country, a locally built multipurpose segment vehicle. The model is the Daihatsu Gran Max line of vehicles for commercial customers. It is custom designed to meet the demand for food trucks from small business entrepreneurs in the country.

3. OPPORTUNITIES AND CHALLENGES FOR NEMS IN BRUNEI DARUSSALAM

This section describes the opportunities and challenges the country might face in promoting and utilizing NEMs (Table 5). NEMs can benefit local industries in many ways such as capacity building, technology and knowledge transfer and innovation. Engaging with TNCs through NEMs will help accelerate the country's economic diversification towards non-oil-based industries.

As the most politically and socially stable country in the region, Brunei Darussalam has an advantage in attracting more TNCs. However, the high cost of labour, limited raw materials and deficient logistics present competitive challenges for local firms as compared with firms in the country's ASEAN counterparts such as Cambodia and Viet Nam.

Table 5. Opportunities and challenges for NEMs in Brunei Darussalam



Source: Authors.

3.1 Business Continuity

The main feature of NEMs is that TNCs do not need to own the local firms running their business activities directly. However, they still have indirect control over the local firms. Thus, through various modes, the TNCs awarding contracts still have quasi-ownership over the local company or corporations. Participating in NEMs with their TNC counterparts provides Bruneian local firms various advantages. Table 6 shows that local firms can benefit a lot from TNCs through knowledge, skills and technology transfers to the locals; international exposure, management know-how and job creation, to name a few.

Table 6. Opportunities and challenges for local firms engaged in NEMs

Opportunities	Typical industries concerned	Challenges
Continuity problems		
Easier to find TNC partners, both in and outside the country through, for example, matching events (because TNCs do not directly invest in the business)	Subcontracting: Textiles and Garments	Easier for TNCs to terminate contracts and long-term relationships are not guaranteed, if quality of services or goods do not meet TNCs' standards and if local firms in other countries are more competitive (e.g., strong competitors exist in the garment industry in Cambodia and Myanmar)
Typical NEMs issues		
Easier to enter new market or new area even though demand is present in the country. Skills, talents, or resources available in the country but not required in the country can be usefully utilized outside the country.	Franchise: Food and Beverages	Franchisees or local firms may face difficulties in adapting TNCs' original strategy to local tastes and need to learn through the experience before becoming part of the community (e.g., franchisees need to localize the TNCs' strategy to meet local demands and tastes that TNCs are not aware of).
	Subcontracting: Textiles and Garments Demand and markets are outside the country.	Demand from TNCs may change depending on the interest and taste of their customers.
Capacity-building issues		
Many opportunities exist for local firms to develop new businesses and boost sales. Easier for local employees to work in NEM activities, even with low skills. They may be able to improve their skills through working.	Subcontracting: Textiles and Garments	Not easy for local firms to build further capacity apart from receiving orders from customers, as they receive only relevant know-how at best (e.g., upgrading value chain activities through their own efforts is not easy especially on the logistics issue of exporting the orders to the TNC)
Initiatives and local embeddedness issues		
Local firms need to take the initiative to lead operations and embed knowledge while maintaining the TNC's basic strategy. Through these activities, local firms can open new business opportunities and improve management capability.	Franchise: Food and Beverages Licensing: Automobile	Not easy for local companies (franchisees; licensing) to adopt TNCs' original strategies to localize. Local companies need to learn through operating.

Source: ASEAN-Japan Centre.

Nevertheless, TNCs, such as in the textiles and garments industry, can relatively easily terminate their contracts and find new production sources to manufacture their products. One of the main factors influencing TNCs in the textiles and garments industry in awarding production contracts is the cost of labour. Brunei Darussalam has a high cost of living relative to many ASEAN countries, and high labour costs will definitely raise never-ending challenges to ensure that TNCs keep renewing their contracts. Thus, this is the main challenge that the textiles and garments industry in Brunei Darussalam faces.

3.2 Characteristics of NEMs

One opportunity of NEMs is that it is much easier for local firms to enter a new market or new area even though demand is not present in the country. For example, a franchisee can get full support from the franchisor in almost all aspects of its operations. The TNC can provide all standard operating procedures up to the supply of materials. Thus, TNCs can make productive use of excess skills, talents or resources available but not required in the country through NEM arrangements with local companies. Nevertheless, in the food and beverages industry, franchisees or local firms may face difficulties adapting the TNCs' original strategy to local demands and tastes, which the TNC may not be aware of, and thus becoming part of the community. In some instances food or drinks have needed to be adjusted to local demand. Furthermore, local Bruneian firms rely heavily on imported raw materials. Lack of local production can be a challenge for franchisees to keep their prices competitive compared with their local competitors. For the textiles and garments industry where production is based on contract demand from TNCs, government policy changes might affect the continuation of contracts.

3.3 Capacity Building

Local firms engaging with TNCs have many opportunities to develop new businesses and boost sales. Technology transfer and know-how usually flow from TNCs to local firms. The technology transfer from TNCs in the textiles and garments industry enables local firms to offer services to other companies either locally or internationally, which builds capacity for local firms, enhancing productivity and efficiency. It is also much easier for local employees to work in NEM activities where TNCs provide proper training. Being employed by NEMs will further improve their skills. However, as Box 4 shows, it is not easy for firms in the textiles and garments industry to build additional capacity apart from receiving orders from customers, as they receive only relevant know-how at best. Furthermore, upgrading value chain activities through their efforts is not easy, especially regarding the logistics issue of exporting their orders internationally.

3.4 Initiatives and Local Embeddedness

Engaging TNCs in NEMs also enables local firms to take the initiative to engage in activities that could lead to business opportunities and management capability improvement while maintaining the TNC's basic strategy. Engaging with TNCs would enable the local firms to build their self-confidence in offering their services to others. This will also lead to market confidence in their services. Learning through operating would benefit the local textiles and garments industry to adapt to new technologies and be on par with international standards. However, local firms may not be able to adopt and implement the same standards required by the TNCs with other clients. This could be due to the high cost incurred by maintaining the same standards. Therefore, the local firm could only use the standards as a reference when offering their services to other local or international corporations.

4. POLICY IMPLICATIONS

Local firms, TNCs and the host country face some challenges and opportunities in adopting NEMs as a mode of investment. Nevertheless, the Government of Brunei Darussalam should see this as an opportunity to diversify its economy and move away from dependence on oil and gas production. The recent downturn in global oil prices, which has been exacerbated by the COVID-19 pandemic, has forced Brunei Darussalam to push its economic diversification initiatives further.

In early January 2021, the country launched the Brunei Economic Blueprint, which provides the country's guidelines for achieving the third goal of the Brunei Vision 2035 strategy, *i.e.*, developing a dynamic and sustainable economy. Six aspirations are the focus of the economic blueprint:

1. To develop a productive business environment by leveraging technology and innovation;
2. To promote continuous learning, training and reskilling of the workforce;
3. To ensure the economy is open and globally connected;
4. To ensure preservation of the environment;
5. To develop infrastructure to support and grow businesses; and
6. To ensure good governance and public service excellence.¹³

Usually, firms owned wholly or jointly by local and foreign TNCs that rely on export markets in ASEAN have been the most vulnerable to external shocks, as experienced in Malaysia, the Philippines, Singapore and Thailand during the global financial crisis of 2007–2008. More importantly, because TNCs often repatriate their profits to their home countries, local NEM firms (as domestically owned firms) can help reduce the wholesale repatriation of profits. Developing resilient NEM firms will also help deepen the reservoir of domestic capital for national expansion. Hence, government policy should strongly consider promoting NEMs as a critical economic growth strategy. The Government of Brunei Darussalam can focus on broad institutional improvement and changes. Fortunately, these proposed improvements and changes are mostly in the pipeline and were extensively discussed in the recently released Brunei Economic Blueprint.

4.1 Enhancing the Capability of Local Firms

Attracting TNCs to sign deals with local firms requires a more convincing presentation of the local firms' capabilities. TNCs will be more comfortable awarding any contract knowing that local firms have the technological and managerial know-how. TNCs usually consider the availability of local firm capabilities as part of their business risk assessment. Thus, the first two aspirations of the Brunei Economic Blueprint will fulfil these needs. The first and second aspiration will assist NEMs at the industry level and the individual business level, respectively.

At the industry level, industrial or business associations and the Government of Brunei Darussalam can jointly support these initiatives:

- Developing a productive business environment by leveraging technology and innovation. Various strategic priorities were laid out to help the country to reduce its dependency on oil and gas. A broad-based approach to growth will be promoted by strengthening priority sectors including exploring new economic activities. This will include promoting FDI and NEMs to spur economic growth.

¹³ <https://www.aseanbriefing.com/news/brunei-launches-economic-blueprint-salient-features/>

- Promoting local firms' greater involvement in global value chains (GVCs). The Government of Brunei Darussalam can promote upgrading and upscaling local firms' capabilities in GVCs through various strategies. One is by providing locals with meaningful and high-value jobs to meet industry needs. Upskilling the labour force will make hiring local firms as part of their value chain attractive to TNCs.
- Another strategy stated in the blueprint report is shifting towards higher value-added activities and products through innovation and compliance with international standards. Innovation and intellectual policy need to be in place to support this strategy. Brunei Darussalam established its Intellectual Property Order in 2013. Such a policy will build more confidence among TNCs in dealing with local firms both via FDI and NEMs, especially for technology- and intellectual property-oriented industries.

At the individual firm level, the government needs to support these efforts:

- Local firms need to train and re-train their employees to ensure that they keep up with TNC labour skill requirements. Thus, the government should promote continuous learning, training and reskilling of the local workforce. Ensuring that workers stay relevant by being innovative and having the right skills to meet future industry demands and adapt to any disruptive global trends is crucial.
- Local firms need to inculcate research and development (R&D) practices into their annual planning. The government needs to be more proactive in assisting local firms with their R&D requirements by providing research grants and expertise. As per the government blueprint aspiration, one of its strategies to support the third goal is to strengthen research, development and innovation capacity to support industrial development.
- Darussalam Enterprise (DARE) is a statutory body established by His Majesty the Sultan and Yang Di-Pertuan of Brunei Darussalam with the key objective of building enterprises into dynamic and resilient drivers of economic growth, to enable enterprise growth through a pro-business ecosystem with necessary infrastructure, reliable support and effective development programmes.¹⁴ DARE can expand its function to be the local business advisory centre where local firms can learn NEM operations or activities. Local firms need to be aware of the big picture of changes and future demands in the industry, not only of their current operations. The government can support this by connecting individual firms (horizontally and vertically) in the industry. The centre should cover all aspects of NEM establishment: forming, executing and evaluating contracts and increasing knowledge about NEM operations. It also can assist in the globalization and localization strategies of the NEM.

4.2 Enhancing Basic Infrastructure

The government has created various initiatives to attract FDI to Brunei Darussalam. Various types of infrastructure were developed to ease business operations in the country. Brunei Darussalam has seen remarkable improvements in the Ease of Doing Business rankings (it is currently in 66th place worldwide and 4th place in ASEAN). The country also maintained its first-place ranking for ease of getting credit (World Bank Group 2020). Nevertheless, improvement in transportation and logistics infrastructure is critically needed to assist local firms' export activities. Shortfalls in these areas might deter not only FDI but also NEMs in Brunei Darussalam. However, one of the policy directions

¹⁴ <https://www.dare.gov.bn/>

under the fifth aspiration of the Brunei Economic Blueprint (2020) is the improvement of road, sea and air connectivity (passengers, freight and logistics) to boost productivity and growth of the economy. NEM firms could enjoy low cost and timely operation if this policy were to be implemented.

Infrastructure simultaneously follows and fosters economic development as an important element of logistics systems. Enhancing logistics systems through infrastructure development and modernization is crucial as a competitive advantage that would motivate TNCs to engage in NEMs in a specific nation (host country). In other words, infrastructure creates adhesiveness for NEMs in an otherwise competitive region, which in turn enhances regional development efforts (Sakalayan 2014). That is, efficient infrastructure in regional or peripheral locations may assist in developing an ecosystem or hub to attract investments and NEMs. For example, Singapore's transport hub concept, which consists of efficient seaport and airport infrastructure, compelled the Maersk shipping lines to leave the dedicated terminal services of Tenjung Pelepus Port in Malaysia. Some infrastructure development plans under the Belt and Road Initiatives also have the capacity to enhance the attractiveness to invest in regional areas. In turn, NEMs bring in investments that boost the economy, support resilient growth and induce further demands for effective logistics systems where infrastructure development remains pivotal.

In general, TNCs choose NEMs for the effective transfer of their competencies to the host-country firm. In NEMs, the host-country partner's bargaining power and efficiency largely depend on the quality and extent of the logistics systems and infrastructure in the host country. In other words, TNCs influence the NEM partner firms in the host country based on the host country's level of bargaining power (UNCTAD 2011). The NEMs along the value chain often include activities in the inbound logistics such as contract farming and procurement and contract manufacturing and distribution activities in the outbound logistics or contract logistics. Underdeveloped infrastructure and logistics systems may reduce the bargaining power of the NEM host-country firms or may even preclude NEMs.

The infrastructure and logistics systems of Brunei Darussalam have undergone a reasonable development phase. The government is now accelerating diversified and transformative strategies in logistics systems for further resilient growth. Logistics systems in tourism; agriculture, including aquaculture; energy and halal sectors may benefit from NEMs for their diversification. Integrating the logistics systems of these sectors into GVCs through diversification and development schemes is critical for the future resilient growth of Brunei Darussalam.

A key component of plugging into GVCs is the logistics facilities that connect to many just-in-time processes. A relatively faster, more efficient and reasonably priced logistics system would support the ability of Brunei-based firms to participate in GVCs. Faster and more cost-effective logistics services would ensure quicker arrivals of machinery and raw materials and prudent distribution or transportation of finished products. Otherwise, smaller Bruneian firms might find it difficult to connect and operate in larger markets, even through e-commerce platforms where quicker and inexpensive shipping services are the usual expectation of suppliers and consumers. The efficient internal logistics systems of Brunei Darussalam are the critical conduits to provide such faster and inexpensive shipping and logistics services where ensuring port connectivity and incentivizing third-party logistics service providers form core elements.

The challenges Brunei Darussalam faces in providing fast and inexpensive shipping and other logistics services include a small domestic market or internal demand, lack of competitiveness with regional market players and inadequate shipping alternatives such as port connectivity to link GVCs. In other words, the absence of competitive advantages, low-cost internal logistics services and efficient port connectivity will make it harder not only for local businesses in Brunei Darussalam, but also for TNCs to form better financial cases for investments linking GVCs.

Despite these challenges, the Government of Brunei Darussalam has so far delivered several good pieces of logistics and infrastructure and has planned to implement some others in the near future that will certainly revamp and integrate the country's internal logistics a step further. These include the 30-km long Temburong Bridge that integrates domestic freight and passenger movements, assists in ecotourism, helps achieve parity in national development and enhance the strategic location and geographical hierarchy of Brunei Darussalam in the region (Commonwealth Secretariat 2019). This bridge, along with the already-built air freight infrastructure, will eventually present the Brunei-Muara Port as a multimodal logistics hub in the region with the gradual improvement of internal logistics services and manufacturing potential. However, at present the air freight facility is occasionally over- and underutilized due to fluctuating and occasional demands; however, it raises the future adaptability and opportunities for businesses and signals the TNCs that Brunei Darussalam is a coherent business location.

In promoting logistics services, including halal industry logistics, Brunei Darussalam strategizes several options, such as the establishment of the Brunei-Guangxi Economic Corridors, implementation of a Bruneian halal food and beverage production facility and strengthening of the collaboration between the Brunei Darussalam BIMP-EAGA Business Council (BD-BEBC) and the Labuan Halal Hub to position Brunei Darussalam as a transshipment hub. The full implementation of the Brunei halal food and beverage production facility will provide a leap for logistics services including refrigerated warehousing and storage facilities in the country. This will further enhance freight shipping, logistics networks and warehousing that often together serve as a basis for building franchising operations.

In the recent past, cruise shipping attached to ecotourism has shown reasonable growth in Brunei Darussalam. In addition, development of health logistics for health tourism coupled with ecotourism could also be further investigated. For all the aforementioned logistics systems development, port connectivity enhancement remains pivotal. Port connectivity, in general, fosters geographical concentration, which is one of the main characteristics of agglomeration economics (Sakalayan 2014). At present, Brunei-Muara Port has limited capacity with only one 250-metre container terminal wharf that can serve one container ship at a time, thus restricting quick logistics services, cargo shipment and internal transportation due to port congestion. However, Brunei-Muara port and logistics services are heavily subsidized by the Government of Brunei Darussalam due to the complexity of export and import imbalance, low port throughput and suboptimal logistics services. In the future, an effective public-private partnership in building one or two additional container terminal wharfs could enhance Brunei-Muara port connectivity to regional and global value chains.

4.3 Promoting Integration into Global Markets

Local firms can take advantage of having NEMs to expand their networks internationally. The ASEAN Economic Community drives towards a more integrated ASEAN economy. With zero to low tariffs among member states, the AEC encourages more ASEAN NEMs to expand their operations regionally and internationally. As an ASEAN member state Brunei Darussalam should take advantage of the trade preference given by ASEAN international counterparts such as ASEAN+3, ASEAN-EC, *etc.* Nevertheless, a favourable and supportive Bruneian government policy towards international trade is still needed. According to the World Bank Group (2020), Brunei Darussalam is in the 149th place of the Trading Across Borders Index, with BND9.6 billion (\$7.2 billion) of FDI stock in Brunei Darussalam for 2019 and total exports of goods and services worth BND10 billion (\$7.5 billion). This is not a good reflection on the image of Brunei Darussalam. However, the government has recognized this problem and plans to improve the international trade and index.

The recently published Brunei Economic Blueprint stated that it aspires to turn Brunei Darussalam into an open and globally connected economy. Some of the policies in the pipeline include promoting and strengthening economic ties with trade partners, bilaterally, regionally and multilaterally for broader market access; supporting trade facilitation to assist export-ready companies through efficient, competent authorities and encouraging businesses to maximize international trade opportunities. These policies will hopefully encourage more NEMs in Brunei Darussalam.

4.4 Developing STI Infrastructure and Promoting Connectivity and Coordination

The co-location of organizational support for NEM firms alone is not sufficient to stimulate technological upgrading. Strong connectivity and coordination must also exist between basic and science, technology and innovation (STI) infrastructure organizations and NEM firms. Whereas emphasis on necessary infrastructure will enable the firms to execute efficient business practices with short lead times and low costs, the development of STI infrastructure—science parks, industry-university linkages and organizations—and the resulting high-quality, technically skilled workers and university graduates will help in stimulating innovation synergies among firms. These are critical for firms to upgrade technologically and enjoy participation in high value-added activities.

In Brunei Darussalam, some of these initiatives have been implemented or are currently in the pipeline. BEDB initiated development of ADTP and Brunei Agro Technology Park (BATP). ADTP is currently in Phase 3. Existing facilities include a design and technology building and a multi-storey car park, the iCentre building¹⁵ and Knowledge Hub building¹⁶ and Kontena Park.¹⁷ Meanwhile, the vision for BATP highlights building strong relations between academic and business circles at both the national and international level, ensuring an investor-friendly atmosphere to secure leading global technology investors to promote modern agriculture innovation and healthy and safe agricultural products and to introduce green tourism and export-oriented agriculture to Brunei Darussalam. Coordinated effort and connected stakeholders in STI infrastructure will help NEMs to flourish.

4.5 Mainstreaming Sustainable Development

United Nations sustainable development goals, also known as global goals, were adopted by its member states in 2015. They provide a shared blueprint for peace and prosperity for people and the planet, now and into the future.¹⁸ This provides opportunities for the Government of Brunei Darussalam to shape NEM firms' conduct and mainstream the 17 goals. This report will examine relevant goals related to workers and human rights and the environment. In any bilateral trade, the common practice is to look at environmental and labour standards as prerequisites for future cooperation. Brunei Darussalam must ensure that its human rights and environmental policy comply with United Nations standards.

¹⁵ iCentre is a startup incubation program and co-working space for entrepreneurs with access to capacity-building programmes and the startup ecosystem. iCentre works closely with local and regional collaborators to develop and conduct workshops in the areas of ideation, market validation and fund raising.

¹⁶ Knowledge Hub (KHub) is a platform for developing the creative and multimedia industry through programmes and activities that are run in partnership with companies such as Microsoft and Sesame World Technology.

¹⁷ Kontena Park is an area with the aim to provide a platform for foodpreneurs to test and validate their product in a real market setting.

¹⁸ <https://sdgs.un.org/goals>

The only Bruneian textiles and garments NEM firm has gone through the international assessment of workers and human rights. The Disney Facility and Merchandize Authorization application that local NEM firms complete must satisfy Disney International Labour Standards.¹⁹ As stated on its website, “Disney’s International Labor Standards Program seeks to foster safe, inclusive, and respectful workplaces wherever Disney-branded products are made”. This is in line with the second aspiration of the Brunei Economic Blueprint (2020, p. 10), which aims to instill a healthy work-life balance to ensure a productive workforce. Thus, Brunei Darussalam needs to monitor its labour or workforce welfare to ensure its welfare or interests are kept at an international standard.

Seventy-two per cent of Brunei Darussalam land is still covered by pristine forest, and the country has committed 58 per cent of its land area to be conserved under the Heart of Borneo initiative. As a result, Brunei Darussalam is ranked 46 in the aforementioned Environmental Performance Index. A sustainable environment is the fourth aspiration under the Brunei Economic Blueprint (2020). Various policy directions were laid out such as instilling a culture that promotes the preservation of the environment and ecosystems in economic activities; promoting green growth initiatives and a sustainable blue economy; promoting research, development and innovation to develop and adopt environmentally friendly and resource-efficient technologies; promoting and investing in environmentally and green-friendly industries and limiting land and environmental degradation in any economic development activities.

5. CONCLUDING REMARKS

As one of the smaller ASEAN member states with the smallest population, Brunei Darussalam has much to gain from NEMs. The three types of NEMs, *i.e.*, subcontracting, franchising and licensing, illustrate that many other industries are not being tapped into. Even though existing and future local NEMs face or potentially face some challenges, the economic and social opportunities that NEMs could bring to the country are undeniable. With more articulated government policies, especially with the recent release of the Brunei Economic Blueprint on 16 January 2021, considering Brunei Darussalam as a business and trading partner looks promising for foreign investors and TNCs. NEMs are a strategic tool for these companies to do business in the country and a developmental tool for local firms.

¹⁹ <https://thewaltdisneycompany.com/responsible-supply-chain/>

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