

## **POLITICAL ECONOMY OF SABAH'S ECONOMIC DEVELOPMENT: ECONOMIC POLICY AND FEDERAL-STATE RELATIONS**

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### **1. INTRODUCTION**

The formation of Malaysia in 1963 is one of the important histories in Southeast Asia. Despite the formation is a controversial one because other nations like the Philippines and Indonesia pose threats to the union however the Borneo states (Sabah and Sarawak) and the Federation of Malaya managed to materialise the formation of Malaysia with much deliberation and diplomacy. Cobbold commission has been instrumental to show the people in Borneo state agreed to the 'Malaysia project', though only one-third of the population favours the union, the decision incorporating Sabah to form a federation of Malaysia has benefited the state to a certain extent. The main purpose of Sabah's agreement to form Malaysia is that the federation will ensure special rights of the state, which is spelled out in the federal constitutions, and improve socio-economic development. The formation of Malaysia also means the country has expanded its domestic market, utilisation of resources, land, and labour. The central government must ensure sufficient growth of every state, while it is the right of the state to demand strategic development to improve socio-economic welfare.

Sabah's economic development has been impressive for the past decade. Under the previous Barisan National ruling coalition various economic programs have been devised to promote socio-economic development, physical infrastructures, human capital development, employment and create various economic opportunities. However, Sabah's economic development is not stellar it remains to lag in terms of socio-economic developments. So, this raises the concern what are the problems associated with slow economic development in Sabah? Why does Sabah's developmental outcome fall behind despite being rich with resources? Such questions are linked to the nature of economic activities in Sabah that are primarily dominated by resource-based activity. It is known resource-based activity cannot pull the rest of the economy as compared to industrial development. Industrialising the economy at the state level is linked to federal-state relations that imply state economic policymaking. This paper will address the federal-state relations using the role of institutions to understand the challenges of economic policymaking.

Scholars of political economists have long observed that uneven economic development lies in the institutions. The institutions structure the federal-state relationships and organises interaction between political and economic actors. The role of institutions forms the 'rules of the game' for political and economic actors in economic policymaking. Institutions organised policy actors in policy processes and how collective actions are engaged among actors in pursuit of economic development. It is institutions that enable policy actors to devise economic planning, transfer of resources, the focus of sectional interest on development, and

interpretation of rules. Institutions are influenced by several factors such as history, political pressure, and power relations. These factors can influence how actors interact in economic policy-making institutions, in turn, could engender different economic outcomes of the state. Uneven economic development, especially in the Sabah case due to institutions structures the federal and state relations, implies the economic development and direction. Centralisation of economic planning at the federal level tends to have a predilection in policy interest and configuration. This article explores the role of institutions in Malaysia which implies economic development outcomes.

## 2. METHODOLOGY

This research uses a qualitative research method to explore the politics and economic dynamic of Sabah's economic development. The study attempts to highlights policymakers configuring preferences and define interests for industrial development. This includes institutional constraints in designing industrial policy which is central to modernise the state. Exploring constraining factors does not view assessment from the federal government but also the state level. While most political economy studies lend themselves to the quantitative method, this research employs a more in-depth analysis using the qualitative method. The qualitative method gives the edge to explore a more detailed and in-depth phenomenon of the social reality in the policy-making process. The key advantage of qualitative is to understand a social phenomenon beyond texts or numbers, it is an attempt to interpret a phenomenon to provide meaning to the surrounding situation. The meaning is formed through connecting actions, policy documents, narratives, discourse, and the current situation. All this process can provide valuable insights into the dynamic of economic policy processes that influence by existing political economy institutions in a particular state. This research uses a wide range of secondary data – descriptive statistical analysis and government report from published and unpublished materials, journal articles, news articles, expert opinion blogs. The secondary data forms a document analysis for this research. Primary data was also used in this research but due to covid-19 respondents are quite limited

## 3. RESULTS AND DISCUSSION

Sabah seems to be falling behind in socio-economic development. This is largely linked to the institutions that structure the federal-state relations which imply economic policy-making institutions. In the policy-making institutions between federal and state, there is less attention to devise strategic sectors based on value-added activities or expansion from the current economic activities to promote growth. Value-added sectors are associated with economic activities that go beyond primary extractions. It is moving up the value chain for instance in semi-finished goods or finished goods. There is little effort in economic policy from the central government to emphasises such growth in Sabah. The focus of industrial development is mainly centred in peninsular Malaysia, for instance, Selangor, Penang, and Johor. While these states have established a strong industrial base, undoubtedly, such states receive wider attention in development budgets for the industrial sector and other downstream activities. This also provides those states with more funds for building physical infrastructures to support value-added activities along with investment in technology. This creates a comparative advantage for peninsular states in the manufacturing sector as compared to Sabah (Lo, 2019; Suffian, 2018b). Industrialising a state that links to wide manufacturing activities does not occur spontaneously, it requires the strategic role of the central government to spur industrial development (Suffian, 2019). The role of the government is to structure the market to facilitate industrial activities.

This includes investment in human capital, physical infrastructures, technology, among others. Hence, this will facilitate structural change

Modernising an economy requires the state to engage in industrial activities- from low value-added to high value-added activities (R&D and capital-intensive activities). The key to moving up the value chain in the development of the manufacturing sector. By this, it means the economy must invest in downstream industries with manufacturing based. Manufacturing is the key to increase productivity, diversify the economy, employment, income, and value-added activities. According to Kaldor (1967), it can pull the rest of the economy (primary, secondary, and tertiary sector). Industrialisation is pertinent to improve the competitiveness of the economy and improve productivity growth by moving up the value chain. For states in the federation to grow requires manufacturing-based to push the economy. This lies in the policy-making institutions between federal and state to configure economic preferences and changes in the economic structure of the state. However, change in economic structures is often political and bound to power relations because it involves the transfer of resources, substantial allocation of funds, and physical infrastructure development.

To improve Sabah's economic development is to prioritise our resources in a key sector that could generate economic growth, and this lies in the industrial sector or downstream activities (Suffian, 2018a). One important caveat here is that other sectors like service (tourism), agriculture, quarry and mining, and constructions do contribute to development, but it should not be the handmaiden to promote growth. Voluminous research on development has pointed out the key to economic growth is to invest in industrial sectors. This sector is linked to manufacturing sectors (downstream processes) which involve turning goods or materials into semi-finished or finished activities. Such economic activities require semi-skilled and skilled workers. By converting our resources to semi-finished and finished products require substantial labour force (not just low but also skilled worker). Instead of exporting our raw material value-added activities involve, this can increase the productivity of the state, thus improve income, and provide vast job opportunities. In Sabah, the economic profile does not seem to reveal the state prioritises the manufacturing sector as key to promote growth, rather it focuses on resource extraction activities which make the state a 'captive market' for low-end production activities. Evidence can be seen in the GDP contribution whereby agriculture, mining, and quarry constituted a big part of the GDP. The government needs to avoid a mismatch of priority in the economic development plan. The government needs to prioritise manufacturing sectors as the primary engine of growth (Rafiq & Mansur 2020). Investment in downstream activities is crucial for the state to use its existing resources effectively, hence will create a more progressive economy (Ibid 13). Manufacturing doesn't mean heavy industries, it is associated with downstream industries which can be linked to food processing, carpentry, packaging, etc if it involves value-added activities. Though Sabah has its downstream activities, it is limited and does not contribute much to the GDP. Government must re-prioritise the focus of this state's economic development (Suffian, 2018a). The state government needs to move away from a 'captive market' and move up the value chain (Jomo & Wee 2014; Lo, 2021). Industrial policy needs to be formulated to coordinate our resources and investment plan for industries to grow, otherwise, this state will continue to be lagged.

Although the federal government controls most of the industrial development funds, the state government needs to devise its industrial policy and reprioritise the state resources to pursue industrial development. This is part of bargaining and putting pressure on the federal government the need to industrial the state. Thorough planning is needed by political and

economic actors to configure strategic sectors to develop the state downstream industries. Even though federal-state relations can be institutional constraints in economic policymaking, this does not mean the state is unable to push its economic agenda. Uneven power relations are not static, constant pressures from the state actors can push the central government to take the state interest seriously.

#### 4. CONCLUSION

While industrialising the state is crucial but above all to promote economic growth, it goes back to institutions had on structuring the relationship between federal and state. The state government of Sabah can identify strategic economic sectors to enhance economic development with the support of the federal government. Bottom-up economic planning is rather crucial rather than top-down. Sabah's economic development could not merely based on the captive market or low-end production activities. It must graduate into higher production activities and more diversified economic structures. It is noted that the institutions feature uneven power relations between federal and state governments in policymaking. But the state government must come out with a coherent industrial policy to promote growth. Conjoin efforts between political actors, bureaucrats, and reliable business groups are crucial to designing coherent industrial policy. This can provide constant pressure for the federal government to allocate resources for industrial development. Sabah elite policymaker needs to work in a way 'punch above their weight' to make sure the federal government pays close attention to the state development project. A certain degree of autonomy should be conferred to the state to decide its economic policy and development trajectory.

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