JUBINOMICS IN AN ERA OF AUSTERITY: Will the new VAT on fuel lead to an economic crisis?

By Dauti Kahura

Three weeks ago, at the Karen bus stop opposite the Karen Police Station, there was a face-off that pitted passengers against matatu crews and their surrogates, the freelance touts that hang around such stops soliciting for passengers. The 33-seater matatus headed to Ngong town, 10km from Karen, were charging Sh80. Just a couple of weeks ago, the standard fare was Sh30. Occasionally, if the demand outstripped supply, which happens from time to time in the matatu industry, the fare would go up by Sh10. Any increase in fare exceeding Sh40 for the 10km ride, whatever the circumstance, would be considered exorbitant. The passengers won this round, but the lingering problem of arbitrary and surreptitious increases in transport fare had not been solved.

The Nairobi-Karen-Ngong route is a microcosm of the looming confrontation between passengers and matatus. And Karen town could be the flashpoint. The route is a very lucrative one, especially during peak hours. Most of the matatu passengers on this route work in the many church institutions, mega malls, restaurants, schools and universities and a big hospital that are located in Karen. Some work for the wealthy Kenyans who have homes there. There are also a lot of casual labourers working in Karen for whom every penny counts.

The tension that had been building between the passengers and the matatu crews had been palpable: *"Hawa wathii siku moja watachoma hizi matatu, hii hasira yao ni mbaya sana,"* ("These passengers will torch these matatus one of these days, their anger is real") said a matatu driver. Wary of the people's wrath, the matatu crews wait for the people to board the matatu, then ambush and cajole them with the ridiculous fare increase. But a fortnight ago, the people refused to enter the matatus, until the crew members publicly announced the fare they were charging. After a 30-minute stalemate, the matatu crew eventually lowered the fare to Sh100. *"Lakini bado hawa wathii wananung'unika, sasa sijui wanataka tufanye nini."* ("Even after giving them a fairer price, the people are still grumbling, I don't know what they expect us to do.")

Since September 1, 2018, when the new 16 per cent VAT (value added tax) on fuel took effect, there has been a commotion in the public transport industry. The Karen-Ngong town driver who said that angry passengers may one of these days burn down matatus to protest against what they consider to be unfair matatu fares, was voicing a concern that has in the past few weeks put matatu crews on edge. *"Wathii wanateta sana, wengine wanataka tu guoko na sisi…si kupoa,"* said a matatu driver operating on the Nairobi-Limuru town route. *(*"Passengers are really complaining, some are picking fights with us…it is not a good sign.")

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The Karen-Ngong driver who was edgy about passengers' uneasiness with the hiked fares said that he was struggling to remit the Sh8,000 his boss demands at the end of each day. "On several instances, we've had to forego our own pay. At Sh115 a litre, the diesel has become way too expensive. We asked the matatu owner to stabilize his profit to Sh7,000, with the hope of balancing the books, at the end of every day but it is not working. I think some people have cut their reliance on matatus. This has a direct relation with frequency of the roundtrips we make – the fewer the roundtrips, the lesser the money we make."

The matatu cooperatives (Saccos) in Nairobi are in a quandary: they have been mulling (even before the fuel tax increase) over how to "rationalise their increasing costs of operations without being seen as gleeful and uncaring," said a top brass at the Matatu Owners Association (MOA). "The business is really hurting, but so are our customers, yet, somebody has to carry the load and feel the pain. Unfortunately, it has always to be the consumer."

But the Saccos have been hesitant: They are afraid of pushing too hard lest their customers rebel and spark off a wave of street demonstrations. Conversely, the industry is undergoing one of its most trying times in recent times – dwindling fortunes occasioned by a gloomy economic outlook. "How long can they hold on like this? That is the Saccos' bosses' question," said the MOA official.

In a bizarre incident on September 16, a matatu stopped at Corporation stage (that is before Uthiru on the Nairobi-Nakuru highway) to pick passengers to Nairobi. Before the driver could know what was going on, a chap grabbed the matatu keys, scaled the dividing wall of the dual carriageway and ran off with keys. The people milling around the stage seemed unperturbed by the incident and the passengers inside and outside the matatu did not seem to mind the ordeal. Afterwards, when I asked one of the freelance touts why the fellow (who is very well known around the area), was risking his life snatching keys from a matatu, his answer was: *"Hizi mathree zinaumiza watu sana."* ("These matatus are squeezing people financially.")

The matatus operating along long distances are not faring any better. My driver friend who operates a Nairobi-Nyahururu shuttle has been mourning since VAT on fuel was introduced. "I'm now spending Sh5,000 on fuel to and from Nyahururu, up from Sh3,200. Nyahururu is exactly 200km from Nairobi city centre. I used to charge my passengers Sh350 one way from Nairobi to Nyahururu before the fuel increase and I'd still take home between Sh3,200 and Sh3,500. It was reasonable."

After September 1, he increased the fare to Sh400, but this has not helped. *"Ndiraruta wira wa kuhura mai na ndiri."* ("I've resorted to pounding water in a mortar – in short, I'm doing zero work.") Even after increasing the fare by Sh50 per person, the best he can take home at the end of the day, he told me, was Sh3,400, after deducting his expenses. As it is, his transport business was running on a Sh1,800 deficit every day – courtesy of the fuel tax. "I can't dare push the fare more than Sh400: I know my customers, they are also suffering, we've to wait and hope President Uhuru will lower the prices," said the driver nonchalantly.

The journey to Nyahururu is usually a one-way trip: A shuttle leaves Nairobi for Nyahururu in the morning at around 9.00am. The 200km trip usually takes about four hours. If the shuttle is lucky, it will make the return trip to Nairobi by between 5.00pm and 6.00pm, arriving in Nairobi at around 10.00pm. There are between 240 and 260 14-seater shuttles on the Nairobi-Nyahururu route. "If you make the round trip," said my driver friend, "you count yourself lucky."

His prayer about President Uhuru rescinding the implementation of VAT on the fuel sounded half-hearted and without conviction – like a person who already knows it is impossible but hopes for the unexpected to happen. "The truth of the matter," he opined, "is that even if the fuel levy was dropped entirely, there certainly would be some relief, but life as it is, is already tough. Too much money had been stolen under President Uhuru's watch and that is the price we've to pay for the profligacy." But it has become increasingly difficult to hold a discussion on President Uhuru Kenyatta's performance, especially with Jubilee supporters, like my driver friend. *"Nitutigane na uhoro ucio."* ("Let's just leave that topic alone.")

President Kenyatta's recent fulmination against matatu owners increasing fares, lest their licenses are revoked by National Transport and Safety Authority (NTSA) was rebutted by MOA, which argued the threat had no basis in law. "The President," said a Jubilee Party MP, "will soon realise that nobody will be taking his threats any more seriously. He is a lame duck president who is doing his final term and holds no sway whatsoever on the politics of the future."

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On 20 September, the controversial Finance Bill, 2018 was passed by MPs. And without wasting any time, the President assented to the Bill the following day. The Bill's vote in Parliament had been preceded by a little-nested game between the MPs and the President. The Parliamentarians had already threatened to shoot down Uhuru's proposal to halve the VAT to 8 per cent, maintaining that there should be none placed on fuel and defying party chief whips.

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"I'm afraid to tell you that even with that seeming reprieve, nothing much will move immediately," said an oilman who imports oil products and runs several petrol stations in Kenya, Rwanda and Uganda. "These are the reasons: VAT is charged at the point of sale and is calculated as 16 per cent on all other costs of the product, over and above the other taxes and levies other than VAT. No importer will agree to sell at a loss simply because politics have been at play. So, even if the Finance Bill 2018 becomes law, with the President's incorporation of the eight per cent VAT proposal, oil importers will not agree to lower their prices. We must first empty all the fuel bought within the time the VAT on fuel was imposed till we bring in new consignments. And this will take some time. If the people are thinking they are going to enjoy the VAT reprieve immediately, they are deluded."

The oil tycoon told me that such a situation presents a perfect scenario for the industry to play market games. "If, for example, some oil importers, for whatever reason (most obviously, it would be for a quick super profit), choose to create an artificial oil shortage by hoarding their product, the price must necessarily shoot upwards, momentarily disrupting the official levy on fuel products."

Apart from the matatu price jolts, the effects of the VAT on fuel has been heavily felt by the long-distance transport trucks that move all manner of goods from source to different markets. Businessmen who transport goats and sheep from Isiolo, Laisamis, Loiyangalani, Mandera, Maralal, Marsabit, Moyale, Turbi, Sololo and southern Ethiopia to Kiamaiko abattoirs in Huruma, Nairobi, told me that their fuel costs had gone by up by between Sh10,000 and Sh12,000 per trip. These animals are carried for up to 14 hours by 10-wheel Mitsubishi Fuso trucks on some of the roughest roads and in the most bandit-prone territories. "Already the wear and tear of the trucks has been staring down at us, but with this new tax on fuel, it has complicated our business," said one of the transporters.

"The increase in the fuel costs means that they have to also pass down the burden to us butcher-men," said Francis Kimani, a butcher, who goes to Kiamaiko every day to buy meat products, including goats' heads, offal for making *mutura* (sausage-like delicacies) and hoofs for boiling soup. Until recently. Kimani was buying up to 100 goat heads every day at Kiamaiko to sell to his staunchly loyal customers at his outlet at the central bus station in Nairobi. "I arrive at Kiamaiko by 6.00am, pick my stuff and quickly head back to my base, because my customers want to find me ready by latest 11.00am."

Kimani hires a boda-boda (motorcycle taxi) to transport his meat products in a box-like container. "I was paying the driver Sh250 per trip to the bus station, but after the VAT increase, he doubled the amount," he said. But that is not the only burden he has to bear: already the prices of his meat products have gone up by more than 30 per cent. "I'll confess I was doing a roaring business until this VAT thing came. My customers have dwindled, partly because I am buying less goat heads and partly because they are also feeling the pinch." From selling 100 heads by the end of the day, Kimani is now barely selling 30. He said that if nothing improves, he will consider relocating to either Isiolo or Rumuruti in Laikipia County. The business was proving too difficult to sustain. "I was born in Rumuruti, I know there isn't much there, but home is home." *"Nairobi tuokire gwetha ido na muturiri."* ("Nairobi's not home, we just came here to look for money and a living.") He said that in Isiolo he could look for work as a truck driver.

The VAT on petroleum products was first mooted in 2013, just after President Uhuru Kenyatta and his deputy, William Ruto, formed the Jubilee coalition government. The VAT Act 2013, as it came to be known, was not implemented immediately; it was shelved for three years till 2016. When it came for review in September 2016, Treasury mandarins, through the drafting of the Financial Act 2016, postponed its introduction. But in March 2018, the Treasury Principal Secretary, Kamau Thugge, finally signalled the fact that beginning this September, the 16 per cent VAT on fuel would certainly be effected. This would mean that for every litre of fuel sold at a petrol station, Sh18 would be added on top of the original cost: a 14 per cent increase per litre.

Thugge was candid: The government had no option but to swallow the International Monetary Fund (IMF)'s bitter pill. Since 2016, the IMF has wanted the government to levy VAT on fuel as a way for it to collect extra revenue domestically. However, it is important to note that although petroleum products were previously exempt from VAT, they are still one of the most taxed commodities in Kenya.

This time last year, the Jubilee government was reeling from two shambolic elections – both conducted within two-and-half-months. The government was broke and was looking for credit facilities, so it turned to the IMF. The VAT on fuel, therefore, is part of the stringent conditions that the IMF has imposed on the Jubilee government in exchange for access to a standby credit facility – a fallback plan for Kenya's Exchequer in case the economy finds itself in the ICU and needs quick resuscitation.

"Playing good politics," and presumably exhibiting "poor leadership", President Uhuru seemingly chastised MPs for initially rejecting his proposal halve the VAT on fuel to 8 per cent. The truth of the matter is that the President himself, in regard to the "problematic" taxation issues, is neither playing good politics nor exhibiting wise leadership.

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"The Bill according to the Budget highlights by the Cabinet Secretary for the National Treasury and Planning is intended is to raise an additional KSh27.5billion to finance 2018/19 fiscal budget year," observes the *Department Committee on Finance and National Planning: Report on the Consideration of the Finance Bill 2018*. The report says, "total projected expenditure and net lending for 2018/19 estimates amounted to KSh2.533 trillion to be financed through ordinary revenue (KSh1.743 trillion) and AIA (Annual-in-Advance) (KSh179.95 billion). Expected external grants will amount to KSh47.037 billion, bringing the revenue to KSh1.970 trillion. This leaves a fiscal deficit of KSh562.748 billion to be financed through debt. The proportion of revenue estimates to GDP for 2018/19 is 19.6 percent which is equivalent to that of the 2017/18 budget."

The Kenya Association of Manufacturers (KAM), one of the lobby groups that presented its resolutions to the committee, argues in the report that, "(the) local manufacturer was losing competition vs major foreign player. The local industries are manufacturing basic products with low gross margin compared to most foreign players, who can support the duty costs. Local players had to increase their prices around (five percent) and it's the final consumer that will pay for the final bill. This, in turn, was jeopardising local employment."

A Kenyan industrialist who had intended to contract some local companies to manufacture carton boxes for packaging consumer goods, such as milk, in the Democratic Republic of Congo (DRC), told me he took his business to Uganda after he was hit with a prohibitive tax levy. "The Kenyan companies were charging me $0.7 per carton box – that is exclusive of transport logistics and documentation charges," said the entrepreneur. "Yet in Kampala, I was being charged $0.42 – inclusive of transport and documentation costs, what they refer to as free on board (FOB)."

On September 18, 2018, President Uhuru Kenyatta rejected the Bill passed by MPs a fortnight before, citing his reasons in a memorandum that sought to overturn some of the proposals shot down by the MPs – chief among them, the 16 per cent VAT on petroleum products and the National Housing Fund, a new tax where the government hopes to impose a tax of 1.5 per cent of income on employees and their employers, ostensibly to fund a home ownership and social housing programme. According to the memorandum, the 16 per cent VAT on fuel has been scaled down to 8 percent in order to raise Sh17.5 billion in the current financial year.

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Another proposal contained in the President's memorandum was to tax betting companies 15 per cent, down from 35 per cent as the case is now. This proposal, instead, hopes to raid the lottery winners' cash by taxing it 20 per cent. The President is looking to raise between Sh25 and Sh30 billion accrued from the sports gaming taxes. The total computation of President Uhuru's memorandum proposal was collecting Sh100 billion in this financial year.

Gitau Githongo, writing in the *E Review*, succinctly observed that "over the past five years, several tax measures have been introduced, including: 12 per cent Rental Income Tax on landlords from 2015, successive excise duty and fuel levy increases in 2015, 2016 and 2018; VAT on bottled water and juices, VAT on food served by restaurants, as well as, piped water; successive increases in excise duties on spirits, cigarettes and mobile telephony; and 50 per cent Gaming Tax on lotteries and bookmakers in 2017, among a host of others."

Gitau's article touched on the real reasons why President Kenyatta returned Kenya into the arms of hard-nosed IMF economists: "The parlous state of Kenya's national accounts – most notably the KSh 5 trillion stock of public debt and ballooning budget deficit…suggests that the slew of tax measures proposed in Budget 2018 was purely about desperately seeking to finance reckless government spending and not about providing incentives for private sector economic growth."

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