Out of the Box Thinking or Garbage Can Policy: Is Jubilee’s Government Protectionism and Economic Controls Good for the Country?

In October last year, Uhuru Kenyatta fired a broadside at imports of fish from China: “The Finance bill has passed but we can think outside the box. We might as well say the fish imported is bad then we lock it. There are many ways the government can work if we really intend on serving our people.”

The trick backfired. The ban was imposed in November and lifted two months later following what was reported as a “biting shortage”. Had he taken a quick peek into the Economic Survey – the government’s annual statistics report that should be on his desk – he would have noted a steady decline in domestic fish production over the last five years – from 160,000 tonnes to 98,000 tonnes, a difference of 35,000 tonnes. Imports in 2018 were 22,000 tonnes, not enough to plug the deficit. On several occasions prior to the ban, senior government officials had been widely reported explaining that Kenya has a large and growing fish deficit. That they went ahead to implement a harebrained roadside declaration tells us everything we need to know about the state of sycophancy in the Jubilee government.

The latest from the Uhuru Kenyatta out-of-the-box policy institute is a proposed ban on used motor vehicle parts. Initially reported as a blanket ban, the Government has since clarified that it is limited to particular parts that endanger safety, such as brake pads. Sensible, isn’t it? Roads full of overloaded matatus and Proboxes with faulty brakes is a scary thought.

Road safety is not the business of trade policy. The person most at risk from a defective vehicle is the driver so, a safe, roadworthy car is in their interest. That said, drivers do kill and maim themselves and others far too often, not just because of defective vehicles but also by dangerous driving, notably speeding and drink driving. I can say without fear of contradiction that defective drivers, and not defective vehicles, are the single largest cause of road accidents. Moreover, there is no law that compels owners to service their vehicles. In many countries, vehicles over a certain age are required to undergo regular roadworthiness inspections. In the absence of a law requiring vehicle owners to replace worn parts, banning the import of used parts is an exercise in futility. What, then, is the ban in aid of?

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Some economic history background is helpful and this is the history of the import control regime that was in place from the early 70s to the early 90s. The regime was a two-stage process, the first of which was the acquisition of an import licence. Import licences were issued by a committee of the Ministry of Commerce and Industry known as the Import Management Committee (IMC). Having acquired an import licence, one proceeded to apply for a Foreign Exchange Allocation Licence (FEAL) at the Central Bank. The role of the IMC was to implement quantitative restrictions. It would review the imports to be authorised based on the domestic production capacity and adjust the amount of imports that would be allowed in accordingly. Obviously, it is impossible to do this for hundreds of products when both the production capacity and the size of the market are constantly changing. Moreover, for some strategic products, importers were required to obtain a “no objection” from the domestic monopoly.

While import substitution industrialisation became the accepted justification, this was actually not how the control regime came about; import substitution industrialisation had been proceeding satisfactorily using tariff protection without import and foreign exchange controls. The regime was put in place in response to the effects of the 1973 oil price shock on foreign exchange and the controls were supposed to be temporary, to be lifted once the effects of the shock subsided. The effects subsided and were, in fact, followed by a coffee boom that more than offset the oil price shock, but the control regime remained.

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Once it was in place, people discovered that it was useful in other ways. Everything about the regime was subject to bureaucratic discretion that could be abused – and was abused – in two ways. First, the determination of import tariffs was completely discretionary, and was determined to a considerable extent by political influence as opposed to economic logic. Second, influential incumbents were able to buy protection not just from imports but also from potential domestic competitors. Suppose an established incumbent noticed a competing product from a new local manufacturer on the shelf. With sufficient influence, the incumbent would get the bureaucrats to frustrate the competitor by denial or long delays in obtaining import licences or foreign exchange allocations. The surest way of buying influence was to have a business relationship with powerful people in government, either as sleeping partners or as distributors or suppliers. The overall effect was a corrupt, distorted, unpredictable policy regime that stifled competition and rewarded inefficiency, effectively undermining investment and entrepreneurship.

It should not come as a surprise then that by the early 80s, import substitution industrialisation had stalled. In Sessional Paper No.1 of 1986 on Economic Management for Renewed Growth, the government owned up to the failure of import substitution industrialisation and ushered in the era of market liberalisation and economic policy reforms known as structural adjustment programmes (SAPs). The paper argued that the state-centric protectionist economic model had reached a dead end. In particular, it highlighted the system's failure to create jobs and warned that, unless it was reformed, we would be "overwhelmed" by population growth.

The trade regime was one of the first targets for reform. The first task of the reform agenda was an exercise known as tariff harmonisation, which culminated in three tariff bands: 0 per cent for raw materials and capital goods, a 10 per cent band for intermediate products and a 25 per cent band for finished goods. Also included was a list of items prohibited for health and safety reasons. The second task was the removal of import licences and foreign exchange controls, which was completed in 1993. The same regime was subsequently adopted by the East African Community. The effect of these reforms was to level the playing field and to tie the government's hands, and the policy regime itself became stable and predictable. It is this policy straightjacket that the out-of-the-box solutions are meant to circumvent.

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Up until 1993, the reforms had been proceeding in fits and starts, with several reversals in between due to resistance from vested interests. But in the aftermath of the 1992 general elections, the Goldenberg chickens came home to roost. Staring an economic meltdown in the face, Moi accepted to open up the economy in exchange for a financial bailout. The impact was immediate; trade boomed and within a year, Nairobi's city centre was transformed into one big bazaar. People spruced up. On the streets, you could no longer tell people's socio-economic status by their appearance – everyone was well dressed. In the rural areas, patched up clothes disappeared. Everyone wore shoes. Motor vehicle ownership boomed. Vehicle registrations, which had been in decline, rebounded immediately, growing 22 per cent per year over the next five years, and 12 per cent per year over the decade (see chart). Owning a decent car ceased to be a status symbol for the upper echelons of society, and they resented it – some still do.

The rationale for foreign exchange controls – that liberalisation would cause scarcity – was blown out of the water; foreign exchange availability actually improved. But most importantly, the prognosis of the 1968 Sessional Paper on employment was vindicated; employment growth doubled from 4.8 per cent in the previous decade, to 9.4 per cent in the decade following liberalisation. This labour absorption was driven by an explosion in micro and small enterprises, particularly in trade, but also in jua kali manufacturing and in other sectors as well. Supermarket shelves featured a wide variety of colourful, affordable local brands of consumer goods – toiletries, shoe polish, vegetable oils – where previously choice was limited to two or three staid multinational brands that had remained unchanged for twenty years or more.

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The used spare parts ban opens a window for bureaucrats to rummage through every consignment of used car parts looking for prohibited parts. Bribes, demurrage and other transaction costs will go up. Many businesses, particularly small ones, will be driven out of business. Maintaining the diverse models of imported used cars will become a challenge and the used-car import trade will be strangled to death by regulation and bureaucracy.

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The Draft National Automotive Industry Policy featured in this column a month ago has precisely this situation as one of its objectives. This ban complements the plan to initially lower the maximum age of used-car imports to five years from the current seven, and then to three years, effectively putting cars out of reach for many people.

But the Government has a plan – model rationalisation and homologation. Model rationalisation means reducing the number of models sold in the market while homologation simply means state certification. The policy is “geared towards an entry model for the local market based on acceptability and affordability”. In short, the state will choose one model of car that will be mass-produced for the local market.

The logic of this is as follows: because we are a small market, having too many models makes it difficult for the local assemblers to have economies of scale. This of course means that the chosen model will be frozen in time technology-wise, and will probably be available in just a couple of colours. But of course, in other markets, design and technology will be moving on and therefore, this will only work if “the people’s car” is protected from the imported used cars that consumers would prefer.

This has been done before; India had the Ambassador, the Soviet Union had the Lada, and East Germany the Trabant. We had the Peugeot 504, which we kept assembling for at least a decade after it had gone out of production. I had the good fortune of visiting Berlin in my youth, just a year before German reunification, and I still recall the surreal images of Trabants sputtering along on one side of the Wall while BMWs, Audis and Mercedes Benzes whizzed by on the other. I find it difficult to contemplate that, thirty years on, and on the cusp of the fourth industrial revolution, we have apparatchiks formulating communist industrial policy.

In the decade after the 1993 “big bang” as we called it, the economy created four million jobs – 400,000 a year, compared to 80,000 a year in the preceding decade. In the absence of these reforms, Kenya would have preceded Zimbabwe on the route to land invasions and economic meltdown. We may not have led then, but we are certainly doing our best to follow now.