

PETROLEUM MARKET STRUCTURE AND PRICING FOLLOWING DEREGULATION

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SUMMARY

Petroleum is Kenya's major source of commercial energy and has, over the years, accounted for about 80% of the country's commercial energy requirements. Demand for oil in Kenya is quite small due to the country's underdeveloped economy, which is heavily dependent on labour intensive and rain-fed agriculture systems. The domestic demand for various petroleum fuels on average stands at 2.5 million tons per year, all of it imported from the Gulf region, either as crude oil for processing at the Kenya Petroleum Refineries Limited or as refined petroleum products.

Prior to liberalisation in October 1994, a significant feature of Kenya's oil industry was a relatively high level of government's direct participation, and a correspondingly low level of private sector involvement. Seven marketing and distribution companies were responsible for procuring and importing their own oil. The National Oil Corporation of Kenya was mandated to supply 30% of the crude oil requirement into the country. The Kenya Petroleum Refineries Limited, Kenya Pipeline Company Limited, National Oil Corporation of Kenya and Kenya Railways Corporation represent the government's presence in the petroleum industry. The Kenya Petroleum Refineries Limited is owned on a 50:50 equity holding between the government and three shippers, namely, Shell, British Petroleum, and Caltex. The Kenya Pipeline Company Limited, Kenya Railways Corporation, and private transporters are involved in transportation of petroleum products from Mombasa to other parts of the country and neighbouring countries.

Prior to 1994, the government, in consultation with the oil marketers, set consumer prices for petroleum products in the country. However, since October 1994, the procurement, distribution, and pricing of petroleum products were liberalized with a view to enhancing operational efficiency of the industry and also attracting private capital. Some of the notable features of the liberalisation process include:

- i) Liberalisation of procurement, distribution, and pricing of petroleum products in the country. Due to inadequate storage capacity, the oil companies were requested to process at least 1.6 million tons of Liquefied Petroleum Gas-rich crude in order to provide the country with the requisite 33,000 metric tons of Liquefied Petroleum Gas per annum.
- ii) Abolition of the White Oil Rule
- iii) Abolition of the 30% National Oil Corporation of Kenya's crude oil supply quota.
- iv) Liberalisation of the oil transportation modes and the attendant tariffs.
- v) Legalisation of minimum operational stocks of petroleum products.
- vi) Introduction of 2% suspended duty on all refined petroleum products imported into the country.
- vii) Licensing of new companies to engage in petroleum business.

Since liberalisation, many new companies have been licensed by the government to engage in petroleum trading, especially import, and export, wholesale and retail of petroleum products. However, despite this initiative, only about ten new entrants are actively trading with a dismal market presence of less than 10% of the market share due to tariff and non-tariff barriers to entry. The prevailing legal and regulatory framework is inadequate to oversee a smooth and efficient administration of the petroleum industry. The Restrictive Trade Practices, Monopolies, and Price Control Act (CAP 504, Laws of Kenya) need to be reviewed to enable the Monopolies Commission to curb uncompetitive trade practices in the petroleum sector. There is need to institutionalise functions of the free market to promote standards and effective regulation in the petroleum industry. On policy, the government should eliminate all tariff and non-tariff barriers to entry into petroleum trading, implement fiscal policies aimed at promoting access to cleaner fuels by the poor, particularly kerosene and Liquefied Petroleum Gas, and review the legal and regulatory dispensation to deepen liberalisation and promote health, environment, and safety standards in the petroleum industry.