

# CURRENT SITUATION IN THE PUBLIC KONZERN BLASCO AND ITS PERSPECTIVE

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## 1. INTRODUCTION

During the last four decades in USSR, shipping as one of the most important sectors of national economy had been well developed. It was integrated with the oceangoing and river shipping companies, ports, shipbuilding industry, science and education.

The sea transport management was based on the principles of direct supervision of shipping industry by the former MORFLOT (Ministry of Merchant Marine) of the Soviet Union. It combined the functions of state control of the industry.<sup>1)</sup> Development project of sea transport was prepared under supervision of the Ministry in Moscow. All purchase of newbuildings from shipyards, imported handling equipment, spare parts, automatic operation systems, procurement of material supplies and distribution of all of these among the enterprises had to be authorized by MORFLOT bodies. The management of merchant fleet and port operation had also been within the scope of MORFLOT's central staff authorities. All revenues gained from fleet, ports, factories and

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1) Tae-Woo Lee, "A Study on the Emergence of Private Shipping Enterprises in Far East Russia and their Impact on Korean Shortsea Shipping.", *Journal of the Korean Institute of Navigation*, Vol. 16, No. 3, 1992, pp.52-53.

other complementary enterprises were transferred to the Ministry.

The hierarchical vertical principle of subordination had been active not only in relations of the enterprises with MORFLOT but also at the level of enterprises themselves. For example, shipping companies had been supervisors of sea ports, shiprepair yards, civil engineering, salvage and diving teams, public catering divisions, agent companies, and motor depots.

The major part of the shipping capacity on the Black Sea is accounted for by two shipping companies - the Black Sea Shipping Company (BLASCO) in Ukraine and the Novorossiysk Shipping Company in Russia, which were formerly regional branches of the all-Union MORFLOT shipping organisation. They were transformed into independent but state-owned shipping companies in 1991.

The current situation in the Ukrainian shipping is very complicated owing to privatisation and reorganisation programmes in economy associated with political struggle with Russia, bureaucratism and socialistic way of thinking.

The purpose of this paper is to point out current problems and some of their solutions in BLASCO and to draw its perspective through the fact-findings and interviews in Moscow and Odessa.

## 2. BRIEF REVIEW OF BLASCO

After the dissolution of the Soviet Union into independent countries and the promulgation of "Enterprise Law", shipping companies, seartransport infrastructure and other enterprises became administratively and financially independent rather than before in Ukraine.

The Department of Sea Transport within the Ministry of Transport of Ukraine, was set up in 1992. New structures made by the Department still conduct state control over the sea transport following state economic and social policy, safety of navigation, and environment control of the sea and coastal areas. Ports and shipyards are no longer part of shipping companies and they have been granted the rights of independent enterprises. Thus, shipping companies from great industrial amalgamation have been transformed into pure shipping enterprises.

In accordance with the decree of Ukrainian President Mr. Kravchuk, BLASCO has

been reorganised into a joint-stock company, the "Public Konzern BLASCO", in August 1993. It consists of 28 different companies, including the government owned, public and private companies. Most of them were former departments of BLASCO. They operate independently under the umbrella of the "Konzern BLASCO". Some new companies will be established and included into it, for example - marine bank, insurance company, freight exchange. All of these companies will be also self-contained.<sup>2)</sup>

According to the decree, Captain Pavel Kudukin was appointed as the head of the Konzern BLASCO. He has introduced major changes at the company, notably a privatisation and restructuring programme that should be under way in the first half of 1994. It is intended to make the company more open to international market.

As far as the Konzern BLASCO is concerned, the privatisation programme<sup>3)</sup> will be taking place in two stages. The first is so called corporatisation process. It will leave the government with at least 51 per cent to 96 per cent of its shares. In the second stage, the ratio of shares the government owns will fall to about 35-40 per cent. Although it does not rule out the possibility of the government still retaining controlling share. During the privatisation, employees will be able to buy its shares. The total value of its shares estimated about USD 1,300-1,500 mil., so it is impossible for them to buy a large amount of shares due to their limited disposable assets. It means that the government will be the main owner of the company and intervene in major decision-making of shipping management.

Table 1 shows deadweight tonnage (dwt) and number of ship by type of BLASCO in 1992. BLASCO has 212 vessels totalling 3.5 mil. dwt. Its fleet's is mainly composed of conventional vessels which account for 53% out of the total tonnage. The bulker sector is the second largest single vessel category at 23.3% of the fleet or 0.8 mil. dwt. It is a striking feature that BLASCO has no tanker fleet.

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2) Galina Vladimirska, 'BLASCO News', *Navigation*, No.4/5 1993, p.20.

3) Since August in 1993, 380,000 out of 500,000 shares totalling 6.7 billion Roubles in the Ukrainian shipping company, Ukrrichflot(Ukrainian River Shipping Company), were sold. The Ukrainian Danube Shipping Company is supposed to follow in 1994, but has suffered considerable losses because of sanctions against the rump Yugoslavia. Economic Intelligence Unit, Ltd., Country Report on Ukraine, Moldova, and Belarus, 4th quarter 1993, p.24.

**Table 1. BLASCO FLEET**

VESSEL TYPE	NO. x DWT*	TOTAL NO. & DWT		%
Bulkers	9x52,450: 6x50,000: 2x24,212	17	820,900	23.3
Ro-Ro	5x20,075: 4x17,665: 8x4,500	17	207,800	5.9
Ro-Flow+	1x5,710	1	5,710	0.3
Container	4x16,030: 2x8,717: 1x6,188	7	88,000	2.5
Reefers	5x4,572	5	23,000	0.7
LPG	2x55,722: 1x27,965	3	139,100	4.0
Multipurpose vessel	3x17,850: 2x12,600	5	79,200	2.3
Conventional vessel	13x16,265: 14x14,900 102x12,000~14,000 8x10,500~4,500	140	1,863,600	53.0
Lighter	3x40,880	3	122,640	3.5
Rail Ferry	2x9,354	2	18,708	0.5
Passanger (ocean going)	1x13,253: 5x15,410: 3x10,000: 3x20,499	12	149,800	4.0
TOTAL		212#	3,518,458	100.0

\* Some figures of DWT were rounded.

+ The ship carries oversized pieces and heavy lifts of up to 700 tons, containers, packaged unit loads or loose cargo, and timber. Cargo is handled either after ship/berth/ship or ship/water/ship technology. In latter case the vessel is sunk down to 9 meters.

# The other types of ships totalling 41, for example, salvage boat, dredgers, and tug boats, were not included into the total number of ships.

Source: BLASCO, 1992.

### 3. CURRENT PROBLEMS IN THE "PUBLIC KONZERN BLASCO"

The Public Konzern BLASCO, born on the basis of the Black Sea Shipping Company, inherited not only its assets, technical bases, and labour but also its problems.

Parliamentary Committee of Basic Industries Development, which has surveyed the its activities in the fourth quarter of 1993, concluded that it is going to be default and that its debts to the Ukrainian government is 106 billion Karbovanets<sup>4)</sup>, equivalent to USD 9.0 million. In addition to this, they concluded that bunker companies will refuse oil and petroleum supply for its fleet and INMARSAT is going to cut the satellite service for its vessels owing to its overdue payments.

The Parliamentary Session was also held to discuss all the matters of the company on 26th January 1994. It adopted a resolution that Ministry of Finance, Ministry of Law, and Ministry of Foreign Relations of Ukraine have to survey the activities, accounting, inventory, credit and commercial agreements of the company and the findings and conclusions of the survey have to been reported to the General Prosecutor's Office. Under the resolution, several legal acts will be introduced soon because existing laws do not quite take into account special natures of shipping activities in Ukraine, including the Konzern BLASCO.

There are four potentially major problems facing it: (i) ageing ships, (ii) difficult financial condition, (iii) excessive level of staff, and (iv) non-existence of bilateral shipping cooperation caused by political disputes and conflicts between Russia and Ukraine.

The competitive power of the company is deteriorated partly because of ageing fleet: about 60 per cent of the ships ever built more than 16 years ago. This is the main problem today. More than 100 conventional vessels have average age of 22 years.<sup>5)</sup> Subsidies for replenishing old vessels from central funds had been practically terminated over the last 5-6 years. Up till 2000 year, by the USSR Ship Register claims, it is necessary for the company to put 162 vessels out of operation. It means that if the solution of ship ageing problem cannot be found within 5 years, considerable conventional tonnage of the fleet will be disappeared.

Another problem the Konzern BLASCO has to overcome is a financial crisis.

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4) The Ukrainian currency unit 'Karbovanets' superseded the 'Cupon' in 13 November, 1992. The latter was introduced in 1 January, 1992.

5) YZHNIIMF(Project and Research Institute), Unpublished paper, Odessa, Ukraine, 1994.

Its Board of Directors is responsible for the debts not covered at the moment of its creation. One year in the past, on the date of 1 March 1993, its debts were USD 172 mil., including the followings:

- more than USD 20.0 mil. for ship repairing, for example - USD 5.0 mil. arrears to NKK ASANO Dockyard in Japan, with more than one year of overdue;
- more than USD 20.0 mil. as payable account for bunker mainly to BOMINFLOT in USSR;
- more than USD 20.5 mil. for disbursement on board;
- more than USD 13.6 mil. for capital acquisition, for example a hotel on the Canarias Islands; and
- others: mainly for new shipbuildings.

The main income sources of the company consist of freight and service payments gained from the service rendered before, and the capital inflow incurred from ship's scrap and selling. They are not enough to repay the above debts in due course.

To make matters worse, its competitive power is also being reduced mainly due to the following reasons:

- Bunker for ships has been supplied by Russia and bunker price was 3-5 times lower than world market price before Perestroika. However, Russia's recent decision to raise the price of the oil it supplies to Ukraine to approximately world prices, and then its threat to halt supplies completely.

- Labour cost for rating class was about USD 30-50 per month, but it now increased more than ten times, not to mention sharp increase of officers' wage.

Excessive staffing level is another very serious problem the Konzern BLASCO currently has. Last year, it operated 212 vessels and employed 450 masters, 445 chief engineers, 18,000 ratings.<sup>6)</sup> It must reduce the present excessive staffing level, considering the number of ships, in order to increase its competitive power.

Finally, the problem it has to tackle is caused by non-economic factor, i.e. main two political struggles: firstly, a trend prompted by what Ukraine sees as interference in its internal affairs, namely the Crimean issue, by senior Russian politicians and by Russia's unwillingness to discuss division of the former Soviet assets and secondly, tension within the Black Sea navy fleet which may lead to a war between two largest

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6) The number of payrolled staff of the Konzern BLASCO, who involved in transportation and cargo management, are 28,000 employees.

Slavic states in the commonwealth. Such political scene gives detrimental impact on bilateral shipping cooperation between Russia and Ukraine.

In the Black Sea region, major sea ports belong to Ukraine. They extended and operated as the means of handling cargoes generated through-out the Soviet Union. Mostly, cargoes belong to seaborne trade between the Mediterranean and the Middle East and Russia, while the cargo volume handled for Ukrainian origins and destinations was limited. After the collapse of the Soviet Union in 1991, Russia drive to be self-sufficient in port services has indeed much diversion of cargo away from Ukrainian ports. As a result, cargo turnover in the ports declined from 120 mil. ton in 1990 to 76 mil. ton in 1993.

There are two sea ports belonging to Russia on the Black Sea. The Port of Novorossiysk is specialised in liquid and bulk cargoes and has no container handling facilities. The small port Tuapse serves for tankers. Both ports have very poor rail facilities. Under the Russian Programme for Renovation of the Merchant Marine, a new sea port will be constructed on the Black Sea.

Although Russia inherited all the tanker fleet on the Black Sea from the old Soviet, it has no container terminal on the Sea.

While Ukraine has container terminals in Odessa and Ilyichevsk ports, it has no tanker fleet to import crude oil for the Ukrainian economy. It is almost totally dependent on Russian oil and gas, for which Russia is now demanding close to world prices. The acute energy shortages have caused constant supply disruptions to its economy since the dispute began in 1992. Total oil requirement of 62 mil. tons was for its economy in 1992, of which 52 mil. imported from Russia and the rest of it from the Middle East and the Caucasus.

Under these circumstances, the bulk amount of capital is required to acquire the tanker fleet for Ukraine and to construct container terminal for Russia, which will not be repaid soon. Thus, both countries are in a complementary position and required to cooperate to maximise welfare in the field of shipping and ports. However, it can be said that as a non-economic factor, unfavourable and stable political scene between Russia and Ukraine is a stumbling block to do so and thus causes to economical losses in the field.

#### 4. SOME SOLUTIONS FOR CURRENT PROBLEMS

Total tonnage of BLASCO amounted to 3.5 mil. dwt tons in 1992(See Table 1). As shown in the table, 53% of total fleet is the type of conventional vessel, which are becoming uneconomical ones owing to shortages of hard currency that results in ship ageing, untimely repairs and maintenance, and difficulties in ship replenishment.

The solution may be easily found in chartering out its vessels on terms of long-term timecharter, which may incur regular income and thus keep them timely in good condition with the charterage income. In addition to this, a part of its income can be accumulated for improving ship's quality.

Another way to replenish the ageing fleet is the creation of relations with foreign banks. Self-financing is not sufficient in conditions of increasing capital intensity and high level of the debt and sharply declining rate of profit in the Konzern BLASCO shipping. Therefore, borrowing becomes necessary. The government, appreciating the importance of shipping in the development of the economy, is in a position to play major role in creating the institutional basis for the rapid development of shipping, thus enabling the company to secure a good position on the world shipping market.

Thus, Ukraine has adopted the law on taxes<sup>7)</sup>, shipping companies were given the right to mortgage their vessels, which are, as a rule, operated under the foreign flag, so as to raise foreign capital from abroad. It may be invested for replacing ageing ships with newbuildings. At present time the Konzern BLASCO has good relationship with some companies in case of financing ships replenishment, for example, with the Bremen Vulkan Shipyard in German.

As an alternative way to solve financial problems, it finds new and more effective forms of operation to increase its earnings. For example, one of the modern passenger vessels, M/V "PETR PERVYY" with passenger capacity 368, was reorganised by USD 3.0 mil. into eye-hospital and clinic ship. So the ship was in the Persian Gulf, now in Spain on the terms of timecharter. She earned USD 9,000 per day. Bunker, wage,

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7) Decrees on taxation, issued in January 1993, attempted to rationalise and liberalise a highly punitive system. Corporate taxes stand on at 30% of enterprise's profits for both local and foreign companies. The VAT rate was reduced from 28% to 20%. In order to stimulate badly needed investment, profits directed to investment will be exempt from taxation. Economic Intelligence Unit, Ltd., op. cit., 2nd quarter 1993, p.18.



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Another ways the Konzern BLASCO may overcome the financial crisis can be suggested as follows: firstly, to establish joint ventures to operate its vessels in Malta, Cyprus, Greece, thanks to internationally horizontal division of labour associated with sufficient foreign shipping financing and secondly, to sell uneconomised ships.

Before the USSR disintegration, the transaction and translation of foreign currency had been made through Vnesheconombank (Foreign Economy Bank). The BLASCO also used the bank. However, it was not satisfied with banking services. Moreover, in case of default, all currency accounts were frozen at the bank.

In order to overcome such problems, the Konzern BLASCO established two money settling centers affiliated with foreign banks abroad: one is IZVESTCO in London and the other MASTOK in Spain. They allows to transfer more quickly and actively the payments to customers. Under this mechanism, credits and debts transacted between a company under the Konzern BLASCO and foreign partners are cleared in the subaccounts of the company through the main accounts of the Konzern without any intervention and delay. It is implicitly independent in decision-making about inflow and outflow of foreign currency.

As discussed in Section 3, the political scene between Russia and Ukraine resulted in economic losses in shipping and ports. A way to solve it may be found from the case of productive bilateral shipping cooperation between the former USSR Republic Moldova and Ukraine. After the disbandment of USSR, Moldova lost the gate to the sea. Moldovan government decided to construct a new sea port on the Danube river, but later, when they calculated all the costs, they recognised that more advantages to reestablish the old relations with Ukraine can be made compared to commitments to the new port construction. Both countries elaborated the way how to operate jointly the fleet and the port and as a result, enjoyed mutual benefit in shipping industry.

## 5. CONCLUSIONS AND PERSPECTIVE

Russia and Ukraine represent the vast majority of the Commonwealth of Independent States' shipping interests. Drastic changes in the structural pattern of shipping sector have been taking place in the present time. Shipping companies, sea ports and other transport-related organisations have been granted economic

independence. Relations among shipping companies, ports, railways, and cargo owners have been changed. Functions of the transport departments have also been transformed. In so doing Ukraine needs to reorganise and privatise its shipping industry as an "open face" to the world market that demonstrates its commitments for the next century.

The process of reorganisation and privatisation contributed to some extent to making the Public Konzern BLASCO more open to international market. The company has passed the first phase - reorganisation, which gave it greater independence in economic and managerial matters. Then it is entering into the second phase - privatisation, which entails big changes not only in managerial and economic functions but also in the economical bases. It is necessary to realise that privatisation is going in two stages. The government will eventually be a major shareholder because the employees of the Konzern BLASCO cannot afford to buy its shares owing to their limited disposable income and low savings. Therefore, despite the privatisation plan, it is made clear that the company retains the loyalty to the government.

The links between the company and the government have been underlined in the recent months by the negotiations on the project of tankers newbuilding for the Ukrainian economy between the Bremen Vulkan Shipyard and the company. It is a national project, in which the company may be involved. So the company sees its future as an independent company that supports the government, and is supported by it.

In the search for alternative ways of reducing energy dependence on Russia, the Ukrainian parliament in June 1993 approved to build a new oil terminal at the Port of Odessa. By employing the tanker fleet provided by the above project, Ukraine could then import crude oil from the Middle East and the Caucasus.

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