



Port of Odessa

Turbulent times face Ukraine's traditional ports as public-private relations have frozen in the wake of legislation that has discouraged investors and operators. Arthur Nitsevych and Wouter van Nus ask the question: can post-election Ukraine turn the tide and regain the confidence of international investors?

Black Sea blues

Private sector interest in the Ukrainian port sector is rapidly diminishing, especially in public port authorities such as the Odessa and Illichevsk Sea Commercial Ports, after the Ukrainian central government in Kiev has proved unable to create a sustainable, stable or competitive business environment for entrepreneurial investment.

Ukraine has significant transshipment potential and

has both the EU and Russia in its sights; it is anticipated that economic development could see the country's transport sector flourish once more. However, to unlock its economic value, Ukraine needs foreign direct investment from international operators and soft loans from international financial institutions such as the European Bank for Reconstruction and Development (EBRD).

Unfortunately, a multitude

of institutional issues exist that threaten to stall this growth, among them a basic lack of experience in attracting and managing international private partners and specific government policies that deter private investment in the port sector.

JAA battlefield

Although independence in 1991 meant a significant change in economic policy, Ukraine's administration still

has difficulty opening up to private capital in the port sector. Contracts are governed by Joint Activity Agreements (JAAs) – Ukraine's draconian version of public-private partnerships (PPPs). In this scheme, both the public port authority and the private operator are formally linked in a single commercial entity to develop and operate the terminal facility.

Unlike most PPPs, however, which only

need to be managed and formalised through a concession agreement, the Ukrainian interpretation turns the operating company's boardroom into a public-private battlefield, paralysing the operator when it comes to making investment decisions and managing the operations.

Recently the JAA arrangements in Illichevsk, just south of Odessa, saw the National Container Company subsidiary, Ukrtranscontainer, forced out of the port after a legal dispute. The local port authority accused its private-sector partner of violating many clauses in the JAA, including the timing and currency of fee payments, financing of non-joint activity assets and the allocation of non-joint activity operational expenses.

After a high court battle, the JAA was annulled and Ukrtranscontainer had to seize its own container-handling activities in the port. Disputes such as these make private investors think twice before entering into such arrangements, let alone committing to significant investment. Currently operations at the 850,000 teu facility, which plans to expand to 4m teu by 2020, are managed by the public authority.

Auctions procedure

Selection of suitable private investors is an arduous task in Ukraine. Tender procedures are known as 'auctions', which in principle are organised by the port authorities managing



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the public assets and basically provide the exclusive right to enter into negotiations.

Nearly all authorities use tendering as a tool to select the most suitable investor/operator for their scarce and strategic terminal assets. With its Resolutions 703 and 530, the Kiev government prides itself on having a clear and formalised procedure for such auctions.

The problem is that these processes still do not provide sufficient comfort for the private sector, with project and contract specifications continually changing due to the involvement of a variety of public institutions, including the Ministries of Transport, Finance and Economic Affairs, the State Property Fund and, of course, the relevant public port authority.

All these entities need to give their formal approval and can request amendments – and with no clear timescale the process is drawn out, resulting in escalating transaction costs.

In normal practice, private



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operators would base their investment decisions on the feasibility of the business case. However, in Ukraine the authorities are often unable to provide reliable or timely information with regards to investment timing and allocation, operational timing and tariff policies.

A good example of Ukrainian tender procedures not succeeding was seen in the Port of Odessa, where the Odessa Sea Commercial Port encountered recurring setbacks in achieving a major expansion of its container capacity. As a result, the envisaged greenfield project, adjacent to the existing HPC facilities, has been unable to attract many international bidders, for a second time.

Looking forward

These issues have to be dealt with by the private sector in the best way possible. Because of them, at present

the main public ports of Odessa and Illichevsk are unable to attract much-needed private capital and expertise; Ukrtranscontainer has had to leave Illichevsk; APMT has made no headway in the same port; and Odessa is still looking for private investors and recently was only able to provide CMA CGM with a small plot.

In contrast, in Yuzhny, only 35 km to the east of Odessa, the 430,000 teu facility of private operator TIS has been developed successfully. With only minor public involvement, it is expected that this terminal will be a safe haven for future development, including the planned Phase 2, which by 2012 will increase its capacity to 1.8m teu. That is, of course, unless Kiev further hardens its position towards the private sector.

If there is no improvement soon, the country's traditional commercial ports will continue to lose market share and will be unable to compete with international and domestic initiatives. In this situation, financial and economic value might be lost, to the detriment of the whole country.

Kiev now holds the power to turn the tide. Will the post-election administration be proactive in paving the way to value-creating PPPs in Ukraine's ports, or will development come to a standstill in this important part of the Black Sea? ■

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